The College Loan Landscape: An Overview of How the U.S. Federal and Private Student Loan Programs Operate

The Federal Student Loan Programs: How They Operate

The U.S. Department of Education operates two federal student loan programs: the Federal Family Education Loan Program (FFELP) and the Direct Loan Program. Loans offered through the two programs carry the same interest rates, terms and conditions for borrowers, and are generally much cheaper than private college loans.

Under FFELP, the federal government guarantees and subsidizes the loans that lenders issue to students and parents. The program's loans account for 74 percent of all federal college loan volume.

Under the Direct Student Loan program, the federal government offers the loans directly to students, securing loan capital from the U.S. Treasury. Currently, Direct Loans account for about 26 percent of all federal college loan volume.

Currently, it is up to colleges and universities to determine which federal college loan program they will participate in: FFELP, the Direct Loan Program, or both.

More than 1,600 schools currently participate in the Direct Loan Program. Almost 4,500 schools are currently using the FFELP for federal student loans.

The Differences between Federal and Private Student Loans

In addition to federally guaranteed college loans, some lenders also offer private (or "alternative") college loans directly to borrowers. Private loan volume has grown significantly in recent years. According to the College Board, during the 2007-2008 school year, private college loans accounted for 23 percent of all education loans.

Unlike federal loans, which have fixed interest rates of up to 6.8 percent, private college loans can carry interest rates as high as 19 percent, and also carry different terms and conditions than federal loans.

According to the Consumers Union, nearly 50 percent of undergraduate private education loan borrowers fail to exhaust their low-cost federal government loans before turning to more expensive private loans to pay for college. The research showed that students and parents often could not identify the best priced loan and that private loan lenders do not always adequately disclose important terms and rates that families need to compare loan options.