



policy paper

Ontario and the Repayment Assistance Plan

October 2009

prepared by:

rob lanteigne, vice president university affairs
brock university students' union

justin williams, vice president education
federation of students, university of waterloo

Introduction

The federal government announced in 2008, and implemented in August 2009, the Repayment Assistance Plan (RAP) to replace its existing Interest Relief (IR), Debt Reduction in Repayment (DRR), and Revision of Terms (RoT) programs. The RAP, IR, DRR and RoT were all designed to meet the same goal of mitigating the negative effects of student loan repayment, but have done so through different mechanisms. Ontario borrowers through OSAP can apply to RAP for assistance with the federal portion of their loans, but must currently rely on the Ontario programs of IR, DRR and RoT for the provincial portion. Several provinces (British Columbia, New Brunswick, Nova Scotia, and Saskatchewan) have harmonized their provincial systems with the federal RAP already¹.

Backgrounder

Interest Relief (IR)

Eligibility for IR is based on gross family income, family size, and the size of a monthly loan payment. Borrowers can apply to the program and be approved for six-month periods whereby no payments need to be made, while interest is paid by the government. If any payments are made during this time, they are applied directly to the principle of the loan. At the expiry of the six-month period, a re-application is necessary. Up to nine periods can be granted, for a total of 54 months of interest relief. IR is an all-or-nothing program based on a series of pre-set cut-offs (adjusting for both family size, and the size of regular payment), meaning that an applicant who makes \$1 more than the cut-off will be denied IR, and must make all regular payment amounts².

Debt Reduction in Repayment (DRR)

When someone has exhausted all of their options through Interest Relief (they have been out of school at least five years, and have received at least 30 months of IR), they become eligible for DRR. Up to three lump-sum payments can be applied directly to the principle of the loan, with a minimum 12-period between each reduction. The current DRR amounts are:

- First reduction: Up to \$4,300 (but no more than 50% of the outstanding loan)
- Second reduction: Up to \$2,200 (but no more than 50% of the outstanding loan)
- Third reduction: Up to \$2,200 (but no more than 50% of the outstanding loan)

In the periods between DRR lump-sum payments, monthly payments including interest must be paid on the remaining principle³.

Revision of Terms (RoT)

¹ CanLearn Website, "Student Financial Assistance – Repayment Assistance Plan"; accessed online at: <http://www.canlearn.ca/eng/main/spotlighton/bdg2008/rap.shtml>

² OSAP Website, "Ontario Student Loans Plan Interest Relief Program"; accessed online at: http://osap.gov.on.ca/eng/not_secure/Repay_int_rel_ont_1234.htm

³ OSAP Website, "Help With Paying – Debt Reduction"; accessed online at http://osap.gov.on.ca/eng/NOT_SECURE/Repay_debt_red_123.htm

If an applicant is ineligible for either IR or DRR, debt can be restructured by lengthening the period of repayment from 9 and 1/2 years after graduation, to 15 years after graduation. This results in lower minimum payments per month, but also increases the amount of interest needed to service the loan⁴.

Repayment Assistance Plan (RAP)

All three programs described above are now consolidated federally into the Repayment Assistance Program. RAP takes into account two factors to determine eligibility:

- Gross family income
- Family size

RAP calculates an 'affordable payment' amount based on the two factors described above, and reduces any necessary payments to the calculated affordable amount. This begins at 0% of family income (for a family size of 1 person, this falls at an income of less than \$20,210), with incremental increases until a maximum percentage is reached. For provinces who have harmonized their provincial loans with RAP, this maximum percentage is 20% (at \$59,210 for that same individual). For provinces which have not yet signed on, the federal portion of the loan is capped at 13.3% of gross income.

RAP works in two stages. During the first five years after graduation, any affordable payment is applied to the principal first, and then to the interest. Any interest which remains unpaid is automatically forgiven (paid by the government), and any principle which remains unpaid is automatically rolled over to the next month at no penalty. After the initial five years have passed, the loan is re-amortized over a further ten-year period. Once the affordable payment is applied, any amount that is remaining, whether it is principle or interest, is automatically forgiven (paid by the government). This ensures that, no matter the size of the outstanding loan, or the size of the affordable payment, all outstanding loans will be eliminated or paid off within 15 years.⁵

Principles

Principle One: Repayment of graduate debt must be structured in a fair and progressive manner.

The governments' (or other lenders') policies around loan repayment can be the determining factor in whether the financial aid system is manageable or not, and what sort of broader effects that debt may have on a student's life in the long term. While obtaining a post-secondary education brings a major return on investment for graduates, this rate of return is diminished as a student's debt level rises.

In order to not penalize students who turn to the provincial financial aid system for assistance, the government must ensure that repayment policies are fair. The repayment structure must also be progressive, and respect the fact that there is a vast disparity in earnings after graduation. This is not only due to the different earning potentials of different types of employment, but there are wage variations within many fields. What is a manageable monthly payment for some former students will be impossible to repay for others. Furthermore, high interest rates result in more costly loans for borrowers who take longer to

⁴ OSAP Website, "Revision of Terms"; accessed online at http://osap.gov.on.ca/eng/NOT_SECURE/Repay_rev_term_123.htm

⁵CanLearn Website, "Repayment Assistance Plan"; Accessed online at <http://www.canlearn.ca/eng/after/repaymentassistance/rpp.shtml>

repay. The government must not unduly penalize people who do not work in the most lucrative industries, or who take other socially important roles such as having children shortly after graduation.

Principle Two: The financial aid system must provide additional assistance for those facing difficulty in repayment.

Even in the best-designed financial aid system, some individuals will face difficulty in meeting their financial obligations, for a variety of reasons. If the financial aid system is to be seen as an investment in social and individual development, then the program must work to assist former students who are unable to repay their loans. This principle would benefit both students who face financial difficulties, and the financial aid system as a whole, which must shoulder the cost of loan defaults.

Concerns

Concern One: Many students face difficulty in repaying their student loans.

Student loans are often the first major financial responsibility shouldered by young people and like any form of debt, they must be managed responsibly. At present, a large proportion of students in post-secondary education are taking on some form of debt, with 40.7 percent of Ontario students holding government student loans⁶.

A large proportion of graduates, 24 percent, reported difficulty in repaying their loans in 2000. Additionally, 14% of graduates had loans of greater than \$25,000. This figure does not include the significant proportion of students (41 percent) who pursue additional education after graduation⁷.

Worse still, a sizeable number of borrowers enter default; in 2008, OSAP reported a loan default rate of 8.4 percent⁸. Human Resources and Social Development Canada reported a three-year blended CSL default rate in Ontario of 14% percent in 2006/07. Also, it was estimated there would be an increase of 2% in defaults for students entering repayment in 2006/07⁹. This is the proportion of the loan value entering repayment that the Canada Student Loan Program (CSLP) anticipated would default (in arrears for more than 270 days) within three years of consolidation. Analysis done by the CSLP found that debt loads above \$15,000 were associated with a higher likelihood of default; this category encompasses about one in five borrowers in the program. Borrowers with debt loads of \$27,000 or higher faced 3 percent increased probability of default for every extra \$1000 in debt¹⁰.

These statistics are troubling for both the borrowers and the financial aid system as a whole. Not surprisingly, high debt loads and loan defaults lead to long-term financial difficulties for the borrower. Furthermore, defaulted loans cost the OSAP system \$96 million in 2002/03, which was 27% of their overall

⁶ Being updated

⁷ Being Updated

⁸ OSAP Website, "Ontario Student Loan Recipients and Defaults for Ontario Postsecondary Institutions, 2008 and 2007"; accessed online <https://osap.gov.on.ca/eng/PDF/0809/2008%20Default%20Rate%20-%20Sector.pdf>

⁹ Human Resources and Social Development Canada, Canada Student Loans Program Annual Report 2006-2007 (Ottawa: HRSDC, 2008); accessed online at http://www.hrsdc.gc.ca/eng/learning/canada_student_loan/Publications/annual_report/2006-2007/annual_report.pdf

¹⁰ Human Resources and Social Development Canada, Canada Student Loans Program Annual Report 2003-2004 (Ottawa: HRSDC, 2006), p.33-35; accessed online at http://www.hrsdc.gc.ca/en/hip/cslp/publications/07_pu_AnnualReport20032004.pdf.

expenditures, more than the amount spent on all provincially-funded bursaries and scholarships¹¹. Clearly, reducing the level of defaulted loans would be in the best interests of the provincial government.

Concern Two: There is little flexibility in the OSAP loan repayment process for borrowers with different income levels and/or fluctuations in income.

There are measures in place for students who have low incomes and cannot afford the monthly payments through Interest Relief and Debt Reduction in Repayment programs; however, they are primarily intended for students who face severe and/or prolonged financial difficulties. Students' loan obligations must comprise a large proportion of their incomes, particularly for students with the heaviest debt loads, in order to qualify for interest relief or debt reduction. For example, a student with a \$1,400 combined monthly payment on all student loans cannot qualify for interest relief unless their income is lower than \$3,305 per month¹². In this case, it disqualifies a student whose monthly payments comprise less than 42.4% of their income.

For students who do not qualify for interest relief but are still having difficulty meeting their loan obligations, there are no measures in place to make loan payments more manageable. The all-or-nothing approach of Interest Relief disadvantages many students whose incomes lie just above their applicable cut-off, leading these students towards default if their payments are truly unmanageable.

Concern Three: Barriers to repayment of loans do not stop simply at gross income and family size.

The existing Interest Relief and Debt Reduction in Repayment programs in Ontario use only gross income and family size in their determination as to whether financial relief is necessary. However, there are a number of other criteria which can severely restrict a graduate's ability to pay back their loan. Living in downtown Toronto is significantly costlier than Owen Sound, where an equivalent gross income could result in significant differences in disposable income. Graduates with private loans and other private debts also face greater challenges in paying back loans under two separate systems.

Concern Four: Students are accumulating high debt loads, which can lead to them abandoning their studies.

The heavy reliance on loans in Ontario's student financial aid system has left students in the province with significant debt loads. In the most recent survey of university graduates, 40.7 percent of Ontario's class of 2000 reported having government student loan debt, averaging \$22,700. This was significantly higher than the national average of \$18,900, and does not include students holding private loans. There are indications that debt levels are continuing to rise; the Canada Millennium Scholarship Foundation reports university graduate debt in 2006 at an average of \$24,047¹³.

While the size of debt loads is a significant concern, the broader effects of debt are even more worrisome. As the Canada Millennium Scholarship Foundation notes, there is clear empirical evidence that qualified

¹¹ Ibid

¹² OSAP Website, "Eligibility Chart" accessed online at <http://osap.gov.on.ca/eng/PDF/0506/Income%20Eligibility%20Chart%20-%20August%201%20%202005.pdf>

¹³ Canada Millennium Scholarship Foundation, "Raising expectations"; accessed online at http://www.millenniumscholarships.ca/images/news/AGM_2006_EN.pdf.

students can be driven to abandon their post-secondary studies due to high debt loads. Research conducted by Lori McElroy found that the larger the annual loan allocation, the lesser the probability that a student would complete their degree. Students with annual loans in the range of \$3,000 to \$9,999 had a 51 percent probability of degree completion, and student with annual loans greater than \$10,000 had just a 34 percent probability of graduating¹⁴. These students will not be able to access the full economic benefits of receiving a post-secondary degree through increased income levels, and will also be saddled with heavy debts. Statistics Canada reports an employment rate of 76.7 percent for individuals who have completed a bachelor's degree, but only a 63.1 percent rate of employment for those who have only some post-secondary experience¹⁵.

Not only is a well-structured debt-repayment program crucial for the future of those who have left their studies, it can be a key factor in motivating students to finish their studies. While research about the informational barriers around debt repayment has not been conducted, if students were aware of repayment methods that allowed them to escape the burden of massive debt levels, surely more would be willing to see their degree through to completion.

Recommendations

Recommendation One: The provincial government should harmonize their debt repayment program with the federal RAP.
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Affordable Payment Structure

The current Interest Relief program provides a very specific dollar cut-off for applicants, and if someone makes just \$1 too much, they lose any of the benefits afforded under the existing programs, including reduced payments. By the same token, someone making \$1 less than the cut-off receives the exact same benefit as somebody who makes \$5000 less than they do. ¹⁶

In contrast, RAP uses a sliding scale with fourteen cut-off points, and caps the level of affordable payment to provide some relief to not only low-income earners, but also middle and higher-income earners.

Repayment Amount First Applied to Principle

Many people in society, former students and others alike, are stuck on debt treadmills with various sources of private loans. By making minimum payments, or even full payments, the vast majority of the payment is applied to the interest first, and only a miniscule amount ever begins to reduce the principle of the debt in the first few payments.

RAP is progressive and unique as it allows all payments to be applied to the principle first, and then to the interest second. If any interest is not covered by the affordable payment, it is automatically forgiven by the government. After the first five years, the same process happens with unpaid principle. This ensures that the principle is continuously being paid down, and debt levels do not remain stagnant, or even increase as they might in the private sector.

¹⁴ Canadian Millennium Scholarship Foundation, "Price of Knowledge 2004: Ontario"; accessed online at <http://www.millenniumscholarships.ca/en/research/pokon.asp>

¹⁵ Statistics Canada, "People employed, by educational attainment" (Ottawa: Statistics Canada, 2006); accessed online at <http://www40.statcan.ca/101/cst01/labor62.htm>

¹⁶ OSAP Website, "Eligibility Chart" accessed online at <http://osap.gov.on.ca>

Increased Time Period of Relief

Under IR, a former student is only able to apply for relief for nine periods of six months each. After this option has been exhausted, there are no other options to reduce the burden of interest. In fact, the one option that can reduce monthly payments, a Revision of Terms, actually paradoxically increases the overall interest burden in the long run as it stretches out payments.

Under RAP, however, every month until the fifteen-year period of exhaustion can provide interest relief for the neediest of borrowers.

Ongoing Support to Forgive Unmanageable Portions Loan Principle

Under DRR, the provincial government provides up to three lump-sum payments applied directly to reduce the principle. While these portions are much larger than any individual amount of monthly assistance under RAP, the frequency is limited, and the amount is limited to no more than half of the outstanding debt.

After the five-year mark, the same beginning point for DRR, RAP provides continued, ongoing forgiveness of the principle and the interest together, if affordable payments are not enough to manage both. At monthly frequencies, these provide more opportunities for the borrower to change their financial circumstances for the better and reduce the immediate DRR burden for those who end up with better-paying jobs. At the same time, it provides more stability for those who are unable to improve their own situation, and could eventually lead to the government forgiving more than 50% of the debt, if that is what's necessary to support the return to freedom from debt.

Guaranteed Date After Which Debt is Fully Forgiven

Despite attempts through IR, DRR and RoT, a student may simply not make enough money to make mortgage-style payments through the 5th to 15th years of their debt. If this is the case, a missed payment or a further extension of terms could lead into debts which stretch for decades. No student should have to be paying for their student loans two-or-three life stages after they have left school.

The restructuring and amortization of debt after the 5th year of repayment guarantees debt-freedom from public debt after no more than fifteen years. If any debt does remain at that time, it will be automatically forgiven, allowing the former student to enter a new phase of their life, with an increased ability to change their financial situation for the better.

Guaranteed Funding Based on Eligibility

The federal government has committed to a RAP program that will fund every eligible student, without budgetary restrictions if the actual uptake differs significantly from the projection. In the economic times which we are currently in, this is a powerful commitment to students that their aid will not be reduced, and that they will not have to compete with others for a limited pot of funding.

Program Stream for Borrowers with Permanent Disabilities

Borrowers with permanent disabilities have unique needs, and a second stream of RAP has been developed to provide expressly for those considerations. To provide assistance for students with disabilities, RAP has an additional program called the Repayment Assistance Plan for Borrowers with a Permanent Disability (or RAP-PD). The RAP-PD program is different from the RAP program in a number of ways. First, the RAP-PD program also considers costs associated with a person's disabilities in their assessment. This insures that a borrower can pay for necessary expenses before they need to pay for

their loans. Additionally, RAP-PD has a shorter maximum repayment length than RAP. Borrowers enrolled in RAP-PD have a maximum repayment period of 10 years¹⁷.

A Simpler Debt Relief Program

Informing students, both current and former, about their financial aid and repayment assistance options is more confusing when programs differ in their implementation. Despite the fact that Ontario has adopted a harmonized application form, the mechanics behind the system are not easy to see, nor easy to understand. Any level of confusion reduces the likelihood of program uptake, especially if it appears complex or could be misunderstood as multiple levels of acceptance.

A harmonized RAP would allow for one unified message about repayment options, and provide better estimations on all government-supported web-based calculators and estimators. It would also allow all borrowers to find the same information in multiple places, and ease any confusion with respect to the address on the repayment cheque which they write each month.

Recommendation Two: The Ontario government must seek improvements to the current RAP program during the period of harmonization.

Despite RAP being a superior method of repayment, there are still necessary reforms to the program. By harmonizing with RAP, the Ontario Government would have the ability to negotiate changes to the program. There are several changes that the Ontario government should negotiate with the Federal government: calculate affordable payment based on after tax income; eliminate penalties for borrowers in default; ensure that marginal interest increases are not used to pay for the RAP program; ensure that borrowers do not need to make payments while on Employment Assistance; and ensure that the program is easy to navigate with an annual renewal.

Calculate Affordable Payment Based on After-Tax Income and Private Student Debt

RAP assesses an affordable payment based on gross income, rather than a borrower's disposable income. While cost-of-living to reflect geographic disparities would be the ideal model, the determination of an affordable payment should at least be based on after-tax income, recognizing both provincial disparities in income due to differential tax rates, as well as reflecting an individual's discretionary income over which the individual has no legal control. For students who required both public and private debt sources to finance their education, the obligated private debt payment amounts should be subtracted from any assessed affordable payment on the public debt.

Eliminate the Penalty for Borrowers in Default

The current Canada Student Loan Program (CSLP) policy is that borrowers currently in default will be ineligible for RAP unless they pay a penalty equivalent to three months at their last assessed payment level. This is a disincentive to those most in need of the program, and may prevent many people from applying to RAP. Enrolling these people into the program will allow for some payments and recovery of costs on behalf of the government, rather than a zero recovery as some participants may spiral towards bankruptcy.

Guarantee that RAP will not be Funded by Increasing Interest Rates

¹⁷ CanLearn Website, "Repayment Assistance Plan for Borrowers with Permanent Disabilities"; Accessed Online at <http://www.canlearn.ca/eng/after/repaymentassistance/rppd.shtml>

There is a concern that the government may increase the interest rate for its fixed rate payments, or the marginal interest rate on a floating repayment as a revenue generator to pay for RAP. The marginal interest rates on the remaining borrowers must not increase in order to fund this program.

Assess Recipients of Employment Insurance a Payment of \$0

The current threshold where RAP assesses an affordable payment of \$0 is \$20,210 for a single individual. Currently, the maximum amount that an EI recipient can receive is \$447 per week, translating into \$23,244 per year. EI recipients face enormous cost pressures as their income is suddenly 55% of what they previously made, or less, but their costs for food, transportation, housing and utilities do not change substantially, or quickly. Under the current model, EI recipients with student loans could potentially have to make payments, as the maximum amount is above the threshold at which RAP begins. When one arm of the government provides assistance for someone in need, the other arm of government should not be reaching into the pocket to claw some back.

Enrolment in RAP Facilitated Through an Easy-to-Navigate System

The design of RAP, much like EI, will require borrowers to reapply every six months. Given the cumbersome application process is one of the weaknesses of IR, we are concerned that this replication will not solve the problem that prevents more than half of eligible borrowers from receiving assistance with their debt payments. Substantial paperwork, overly strict methods of confirming income, or mail-in procedures after initial enrolment all contribute to declining uptake for valuable programs.

Conclusion

The time has come for the Ontario government to immediately enter into discussions with their federal counterparts to develop a synchronized RAP for Ontario borrowers. While the current IR, DRR and RoT programs are based upon the same principles and needs as RAP, the federal government adjusted to the new model based on the additional benefits that RAP provides to students. A harmonized system would be superior to the current system, because it would develop a more affordable repayment system for borrowers, lower the principle on a debt first, dramatically increase the potential period of relief, provide ongoing support for unmanageable portions of a loan principle, develop a guaranteed end date for a loan, provide assistance to everyone who is eligible, provide a dedicated stream for borrowers with permanent disabilities and make the entire process of debt relief much simpler for borrowers in Ontario. Overall, these changes will decrease default rates and ensure that more loan is repaid to the Province, whereby making the entire system more affordable for all parties.

Recognizing that RAP is already preferable to the existing programs, there are still some modifications which have been identified that could enhance RAP even further. Necessary changes for the success of RAP include changing the affordable payment calculation to be based on after tax income, eliminating the penalty for borrowers in default, guaranteeing that RAP will not be funded through increases to the interest rates, assessing recipients on employment insurances a payment of \$0, and developing an easy to navigate process for enrolment in RAP. Ontario, through its size and influence, can request and achieve these changes within a harmonized program, providing a better model for former students in Ontario who need assistance with their loan repayments.

RAP policy **statement**

WHEREAS repayment of graduate debt must be structured in a fair and progressive manner.

WHEREAS the financial aid system must provide additional assistance for those facing difficulty in repayment.

WHEREAS many students face difficulty in repaying their student loans.

WHEREAS there is little flexibility in the OSAP loan repayment process for borrowers with different income levels and/or fluctuations in income.

WHEREAS barriers to repayment of loans do not stop simply at gross income and family size.

WHEREAS students are accumulating high debt loads, which can lead to them abandoning their studies.

BIRT the provincial government should harmonize their debt repayment program with the federal RAP.

BIFRT the Ontario government must seek improvements to the current RAP program during the period of harmonization.