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Background and Summary

The student debt crisis in the United States threatens the viability of the American Dream. For decades, a college degree served as a ticket into the middle class and a guarantee of upward economic mobility. In recent years, this path has grown far more difficult and financially risky as the price of a four-year degree has regularly grown faster than inflation. The federal government sought to realize the gains of an educated populace when Congress passed the Federal Family Education Loan (FFEL) program and started backstopping student loans. Unfortunately, while this program and subsequent legislation greatly expanded educational access to a wider swath of the population than ever before, it also contributed to the immense burden of the current student debt that far too many Americans struggle under today.

Although the initial policy held the best intentions and the reasons for the magnitude of debt are manifold, we propose a solution that can attract the bipartisan support necessary to pass Congress and begin to address the crisis. The combination of administrative mismanagement, low graduation rates, and moral hazard on the part of universities has led to the unsustainable debt levels we face today. Our proposal focuses on removing interest from federal loans and moving all loans to income-based repayment plans with the duration based on the course of study. These proposals will remove the broken incentives from both students and universities while acting as an essentially budget neutral intervention. As recent reports have shown, viewing student loans as a potential revenue center deeply misunderstands the economics of our current system. This new proposed system will supercharge economic growth by increasing opportunity, expanding access, and building human capital in the next generation.

Proposal

The first aspect of the student loan crisis that we would like to address is the rapid growth of debt for borrowers who currently make their mandated payments. We propose that all federally administered student loans come at zero interest, preventing the payment amount from ever exceeding the principal. The government will no longer bring in interest revenue, but the revenue from increased economic growth and activity from graduates no longer burdened by growing debt will dwarf the lost revenue. In 2021, the Government Accountability Office (GAO) estimated that the federal government had lost $197 billion despite previous estimates that the government would actually gain $114 billion in revenue. A significant portion of this shortfall stems from the pandemic repayment pause, but an unexpectedly higher proportion of students enrolling in Income Based Repayment (IBR) programs explains a much larger portion of the $311 billion shortfall. IBR plans limit the monthly payments that borrowers have to pay in proportion to their income; the program forgives the remaining debt after a sufficient period of payment without any delinquency. Charging interest on student loans misaligns the goals of the program as revenue generating instead of driving economic growth. The government should provide these loans not as a business, but rather as a public good to create a more educated and productive workforce, serving as an engine for upward economic and social mobility.

We propose shifting the IBR program to a model that Purdue University piloted starting in 2019. This program rethinks student debt as equity-based on the earnings potential of the student's major. Our proposal creates a nationwide program where every borrower enrolls in an income-based repayment plan, typically capped at 5% of discretionary income. At the time of enrollment, the borrower enters a contract where, depending on their major, they are obligated to make the 5% payment of their discretionary income for a prescribed number of years. Given a specific list or series of majors, the income-based repayment program requires that all borrowers pay the same proportion of income, but to control for the variance in compensation between different majors, those that have higher income preferences need to complete fewer payments to earn full forgiveness. At the end of the repayment period, if a borrower makes all payments, the Department of Education calculates the remaining balance and the government forgives half of the loan while the university must forgive the other half. In the case that the borrower earns enough that they pay more than the initial value of the loan, then their payments would meet their obligation to repay at 120% of principal. This protocol incentivizes universities to ensure that students both graduate and have the necessary skills to have lucrative careers along with career support. Additionally, any borrower that enters into government service or non-profit work qualifies for PSLF or whichever repayment plan has the shortest period in which case the government would extrapolate their current earnings to the end of the repayment period and cover those payments as well.

The main goal of this program is to realign incentives and remove the moral hazards of the current system. Students gain access to higher education, though they must factor in the relative earning potential of different majors while selecting careers. Students may still pursue less lucrative majors that may require longer payback periods, or cut their repayment period by going into public service. For universities, they now have significantly greater incentive to support students to graduate as well as providing sufficient career training and placement. Additionally, they would not necessarily want to steer students away from low income majors because those include more years of repayments and thus greater late career earning potential. At the same time, they must keep tuition low or else be liable for a significant portion of the outstanding debt at the end of the repayment period. The government can adjust the years based on labor market needs and has now forced universities to consider rising costs. Investigations into the IBR and Public Service Loan Forgiveness (PSLF) programs have shown significant shortcomings and thus the Department of Education would need to more aggressively commit to maintaining a streamlined process for managing this program. This proposal would appropriate sufficient funding to create a portal for universities and students alike to manage and view the current status of their payments and loans, as well as the corresponding infrastructure to manage and process loans.

Passage

We believe that this bill can garner bipartisan support, particularly from the Chairs of the House Committee on Education and Labor. Chairman Scott and Ranking Member Foxx have cosponsored the LOAN and REAL Acts respectively. This proposal would address many of the problems both of those bills attempt to address including limiting interest, preventing owing significantly more than the principal, disincentivizing universities from raising tuition, and expanding the PSLF program. In the Senate, HELP Chair Senator Murray has advocated overhauling and improving the PSLF system. As a concession to Ranking Member Burr (as well as Reps. Foxx and Stefanik,) the proposal can include an explicit limitation on the executive branch forgiving any further student debt. While the overhaul of the IBR and PSLF programs may require additional spending, we propose closing the carried interest loophole, which has bipartisan support. This measure would raise approximately $14 billion over ten years, which would more than cover the administrative costs and allow the bill to reduce the deficit. The underlying concept stems from a Purdue University program which was put in place during the tenure of President Mitch Daniels, the former Republican Governor of Indiana. Overall this proposal's key priorities focusing on limiting universities' moral hazard to raise tuition while still expanding access should garner bipartisan support and pass out of committee and then both chambers through regular order.

Additionally this proposal can attract significant advocate support to help shepherd it through the legislative process. Overall, the solution would encourage STEM degrees which would attract advocacy groups like the Chamber of Commerce and Business Software Alliance. Union groups for public service workings including AFSCME and teachers unions would likely also advocate for the proposal as it would streamline the IBR and PSLF programs for their members. Universities can appreciate that the program standardizes the student loan process, reducing their cost of management and gives them a potential upside if students have particularly lucrative careers. Overall this proposal will increase American competitiveness, enrich our workforce, and most importantly expand educational opportunities to all students.