The Detroit News

Find a fix for student loan mess

The government's increased involvement in loans has enabled political battles over interest rates

June 23, 2013

The refrain may sound familiar: Stop interest rates on student loans from doubling to 6.8 percent July 1. That's because the exact same debate over how to handle interest rates on subsidized federal loans took place last June. Congress and the White House have to find a long-term solution and stop using loans for political grandstanding.

After artificially lowering the interest rate in 2007, Congress faced the expiration of that rate last summer — in a contested presidential election year. So even though the decision came down to the wire, lawmakers passed a one-year extension that kept the rates at 3.4 percent on need-based subsidized Stafford loans for one more year.

That was a temporary patch to an ongoing problem. Plus, it cost taxpayers $6 billion, while only offering around 7 million student borrowers a paltry savings of less than $10 a month.

The pandering over loans is a symptom of the government's increased involvement in the loan business. "It's part of what you get when you set rates through the political process," says Lindsey Burke, an expert in education policy at the Heritage Foundation.

Through a provision attached to the new health care law, Congress gave the Obama administration control of the student loan industry by ending federal subsidies to private lenders; this placed the government in control of issuing and servicing all federal student loans.

As the availability of federal aid has ballooned in recent years, so has college tuition. That's not a coincidence, according to higher education experts at the Cato Institute, the Center for College Affordability and Productivity and Heritage. While the government says it's trying to help more students get to college, especially low-income students, all the aid floating around is encouraging universities to hike their prices. "It's a vicious cycle," says Burke.

Last month, the U.S. House passed a reasonable bill that would create more of a lasting, market-based answer to student loan interest rates. But the Senate has pretty much ignored it.

House Education and the Workforce Committee Chairman John Kline, R-Minn., says the Smarter Solutions for Students Act deserves the president's support and President Barack Obama should encourage the Senate to pass it.

That's not likely, even though the bill ties interest rates to the market through the 10-year Treasury note — just as Obama had said he supported in his budget. According to Kline's office, the House bill would prevent student loan interest rates from doubling; protect against high interest rates through a reasonable cap; and offer taxpayers and students around the same savings as the president's proposal.

Andrew Kelly, an education policy scholar at the American Enterprise Institute, recently argued in Forbes Magazine that while there are differences between the House plan and Obama's, "the gap between the two sides is simply not that wide." Surely a compromise is in order.

Yet Burke doesn't think any of the plans proposed go far enough to protect taxpayers. She says the government must set interest rates on student loans based on fair-value accounting — preferred by the Congressional Budget Office. Current federal accounting practices do not take into account market risks, such as how likely a student will be able to pay back a loan. That inevitably is leaving taxpayers on the hook for the many students who will never complete college or repay their debts. Burke says this means student loans likely cost the government, even though the loans are supposed to be a money-maker.

In the end, politicians are obsessing over a shortsighted battle. Student debt is now more than $1 trillion, and students are borrowing more each year. Increased federal involvement is only making the situation worse.