Education: College

SAFRA Stinks

Neal McCluskey 08.10.09, 6:10 PM ET

Something called the Student Aid and Fiscal Responsibility Act (SAFRA) zipped through the House Committee on Education and Labor recently.

Odds are you haven't heard much about it, maybe because of the deafening health care clamor, but it would do something pretty big, ending the 44-year-old Federal Family Education Loan (FFEL) program--which uses federal bucks to back tens of billions of dollars of student loans from private lenders--and replacing it with lending straight from Uncle Sam. In other words, it would destroy what little chance there was of student loans being constrained at all by economic realities.

"First, we saw a drive toward complete government takeover of our nation's health care system," lamented ranking Education and Labor Committee member Rep. John Kline, R-Minn., during deliberation over the bill. "Now, we see government seizing control of student lending, forcing the private sector out and welcoming in a mountain of public debt."

Contrary to what Kline suggests, guaranteed lending is about as close to a free market as a biplane is to the Starship Enterprise. Under FFEL, Washington guarantees lenders--including Fannie's cousin, Sallie--a profit on student loans, reimbursing them almost completely on defaults and paying big subsidies. Making matters worse, legislation was enacted last year that lets the feds more or less directly finance FFEL loans if lenders can't access sufficient funds through private capital markets.

So SAFRA's major problem isn't that it would kill guaranteed lending. It's that it would replace it with federal direct lending--which would amount to about a quarter of FFEL's size--and completely cut out private capital markets, making Uncle Sam your sole choice of lender. With the government acting as lender, there is no reason for economic realities to constrain student loans.

This is especially troubling because too many people are pursuing degrees. About a third of college students take at least one remedial course, only 56% graduate within six years and 29% of Americans have bachelor's degrees even though only a quarter of American jobs require them.

Another sad consequence of moving entirely to direct lending is that it would likely crowd out what little non-governmental lending currently occurs. Many lenders would likely have to shutter their non-government arms if they couldn't continue participating in much bigger, federal lending operations.

All that said, this is hardly the destruction of capitalism. But then there's what this bill *wouldn't* do.

SAFRA supporters assert that transitioning from guaranteed to direct lending would save $87 billion over 10 years. That is doubtful. The cost of quintupling the volume of direct lending is, at best, tough to predict, and bureaucracies have a strong, inherent tendency to grow. Still, there should be some savings. But SAFRA wouldn't give it to taxpayers, or dedicate most of it to paying down the nation's staggering deficit. Instead, any saving would be spent.

Among numerous recipients, SAFRA would direct $47 billion to Pell grants and require that grant amounts rise annually at the rate of inflation-plus-one-point. That would assist low-income students better than federal loans, but also set an ever-rising floor under which schools would never lower tuition prices, negating its value.

Next, SAFRA would send about $9.5 billion to community colleges; $2.5 billion would go toward improving facilities, and the remainder toward grants intended to push schools to improve their program-completion and job-placement rates. But don't get your hopes up: Community colleges could qualify for the money simply by providing "student support services" and implementing "other innovative programs"; that's legislative jargon for "free money."

And much to the ivory tower's chagrin, Congress has other groups it wants to pay off. So $8 billion is slated to go to early-childhood education and $4 billion to repairing and modernizing not just public college buildings, but elementary and secondary schools as well.

Finally, roughly $10 billion is supposed to go toward reducing the federal government's deficit, a ludicrously small figure considering that it recently surpassed $1 trillion for fiscal year 2009 and the SAFRA bill supposedly creates savings without causing current beneficiaries any pain. If all the proclaimed savings don't appear, the last two words in "Student Aid and Fiscal Responsibility" become an even bigger joke.

All of which explains why SAFRA is flying below the radar. Yes, bigger things are going on in Washington. In the end, what seems like a transformative bill might be nothing but business as usual. But for students, "business as usual" is not affordable any longer.

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