INSIDESOURCES

CON: Take a student loan, repay the student loan

Neal McCluskey

February 27, 2020

You take a student loan, you repay your student loan. That should be the obvious, baseline understanding of how student lending works. There may be times when that should not apply, but contra presidential candidates Bernie Sanders and Elizabeth Warren, those times should be rare, and dependent on specific circumstances.

Federal loans constituted about 88% of total student loan volume in the 2018-19 school year. Let's be clear what they do: give taxpayer money to students so the recipients can get a degree and vastly increase their lifetime earnings.

Georgetown University's Center on Education and the Workforce has estimated that the typical person who ends their formal education with a bachelor's degree will earn about $1 million more over their lifetime than someone topping out at a high school diploma. That's a big payoff, and there is no justification for making taxpayers eat associated debt, which for the 69% of 2018 grads with debt was $29,800 on average.

What would wide-scale forgiveness be? Straight up robbing Peter to enrich Paul.

Such forgiveness would not just be morally wrong, it would exacerbate many huge higher education problems, ranging from rampant price inflation — the more money people are able to pay, the more colleges can charge — to the amenities arms race. If students don't think they would have to repay their debt, why not accept higher student fees for, say, a fancy on-campus water park?

That said, there are two situations in which it may be reasonable to forgive loans, especially if they are private, but possibly even federal: when it is either physically or financially impossible for borrowers to repay.

Physical inability to repay is easy to envision. If someone has an accident and ends up with a disability that makes it impossible to work, or work at the level of remuneration they had reasonably expected, it makes sense to forgive their loans. This applies whether the loans are federal or private — if one is rendered utterly incapable of earning enough to repay, there is nothing reasonably to be done.

What about financial failure? This one is tougher if it does not stem from an act of God. If someone spends on luxuries, or buys too big a house, and renders themselves unable to repay their debts, they can declare bankruptcy, empowering a court to create a repayment plan that can discharge some debt. But they should really remain responsible for what they owe — the situation was of their own making.

In such a situation student loans are harder to discharge than other liabilities such as credit card debt. For student debt, one has to demonstrate that repayment would create an "undue hardship," which is considered to be a high bar, though it is poorly defined in law.

For federal loans, having a high bar makes sense. Such loans are made with money taken from taxpayers who had no choice in the matter. Making the taxpayers whole should be a top priority.

Private loans are fundamentally different in that the lenders freely choose to do business with students, and stand to reap profits. It is far more reasonable to make those loans dischargeable on terms similar to other debt.

Even with some justification for making private loans more easily discharged in bankruptcy, rules for existing loans should not be changed retroactively. Easier bankruptcy should apply only to loans originated after reforms are passed, so that lenders can adapt their policies and terms.

The norm for student loan repayment should be consistent with basic — and frankly, obvious — fairness: you take out the loan, you repay it. In rare circumstances that may not be possible, and we should consider tweaking such things as bankruptcy laws. But the fact that one should repay one's debts should not be the least bit controversial.

Neal McCluskey is the director of the Cato Institute's Center for Educational Freedom.