The Fallacy of Forgiveness

IF THE FEDS WIPE OUT STUDENT DEBT, WHO WILL BENEFIT MOST?

During the 2020 presidential primaries, Democratic candidates proposed forgiving $640 billion in outstanding federal student-loan debt. Proponents of loan forgiveness argue that this debt places overwhelming burdens on today's young graduates—and college dropouts—and that lightening their load would help both the borrowers and the economy overall. Yet these proposals have raised questions about who would benefit most and whether student-debt relief is efficient. Is loan forgiveness for all a good idea? Beth Akers is a senior fellow at the Manhattan Institute for Policy Research, a center-right think tank. Sandy Baum is a nonresident senior fellow for the Center on Education Data and Policy at the Urban Institute, which leans toward the center-left. In this forum, both authors argue against universal loan forgiveness.

MASS DEBT FORGIVENESS IS NOT A PROGRESSIVE IDEA

by SANDY BAUM

IN 2011, when the Occupy Wall Street movement called the nation's attention to the wealth-and-income gaps between the top 1 percent of the population and everyone else, activists began to promote the idea of forgiving student-loan debt. Those in the Occupy Student Debt campaign argued that all current education debt should be eliminated immediately. They asserted that policies such as limiting loan payments to an affordable share of income were "micro-cosmetic," and that creditors needed to free debtors from their "bondage."

At the time, only a small minority of people subscribed to the idea, but recently it has gone mainstream, with Democratic presidential candidates Elizabeth Warren and Bernie Sanders proposing *(continued on page 82)*

TAILOR DEBT RELIEF TO THOSE WHO NEED IT MOST

by BETH AKERS

THE POPULAR-MEDIA COVERAGE of student loans would have you believe that a generation of young workers is being crushed by unaffordable student-loan debt they can't escape. Indeed, when presidential candidate Senator Elizabeth Warren last year put forth a proposal to cancel $640 billion dollars in education debt, the plan met with popular approval. According to a May 2019 poll by Politico/Morning Consult, 56 percent of voters supported Warren's proposal, while just 27 percent opposed it.

Popular support notwithstanding, widespread student-loan forgiveness is a bad idea—not because such a program would be too costly or because it would undermine the social compact for individual responsibility. Rather, it's a bad idea because the problem *(continued on page 83)*

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broad student-debt forgiveness policies. To help families cope with financial pressures during the Covid-19 crisis, the Democratic Party platform calls for up to $10,000 in student-debt relief per borrower. Longer-term provisions in the platform include forgiving all debt on undergraduate tuition loans for those who earn under $125,000 and who attended public institutions. That benefit would also apply to those who hold tuition debt from attending historically Black private colleges and universities.

Democrats included a student-debt relief provision in their proposals for the Covid-19 rescue package. Ultimately, the Coronavirus Aid, Relief, and Economic Security Act of March 2020 suspended loan payments and waived interest for six months but did not include debt forgiveness. The payment waiver now extends to the end of the year.

Proponents of large-scale erasure of education debt characterize the idea as progressive, in part because such a policy, which would benefit relatively affluent people, might be financed (as Bernie Sanders proposed) by people who are even better off. Truly progressive policies, though, provide disproportionate benefits to households in the lower reaches of the income distribution. They are designed to diminish the gaps between the haves and the have-nots.

The realities of student debt in our country make it clear that proposals to eliminate these obligations do not meet the criteria for progressive policies. Households in the upper half of the income distribution hold more student debt than those in the lower half. The highest-income quartile of households owes about one-third of that debt; the lowest-income quartile owes about 12 percent. People who don't go to college don't have student debt. They have lower incomes and more constrained job opportunities than others.

There are some people who borrowed and either didn't complete their programs or never saw the anticipated earnings payoffs to the credentials they did earn. These individuals make up a large share of the low-income adults who *do* hold student debt. The circumstances of these borrowers explain why the government has developed an income-driven repayment system for federal student loans. The system is far from perfect, but it does not require payments until a borrower's income exceeds 150 percent of the poverty level and then generally requires payments equal to 10 percent of the borrower's income beyond that level. Those whose incomes never support affordable repayment of their debts will see their remaining balances forgiven after 20 years (or 10 years for those with public-service jobs and 25 years for those with graduate school debt).

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Just 7 percent of borrowers owe more than $100,000 in student loans. This small share of borrowers owes more than one-third of the outstanding balances. Doctors and lawyers and MBAs have lots of debt, but they also tend to have high incomes. About 40 percent of federal student loans go to graduate students each year. There are strict limits on how much undergraduate students can borrow from the federal government—$31,000 total for those who are dependent on their parents and $57,500 for those who are older, married, or otherwise independent of their parents. Graduate students, though, can borrow virtually unlimited amounts.

More than one-third of borrowers owe less than $10,000. They hold just 5 percent of the outstanding student debt. Many of them are the borrowers who struggle most to pay back their loans because their limited skills restrict their job opportunities.

In short, forgiving all student debt would deliver a big windfall to a few people: those who can afford to pay. Virtually all of those with the largest debts have bachelor's degrees, and most have advanced degrees. *(continued on page 84)*

Senator Bernie Sanders backed loan forgiveness.

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it's designed to address isn't the one that needs fixing.

The picture of the issue painted by the media is distorted. Why? First of all, the typical student borrower has but a modest monthly payment to make relative to his or her income. That's because college degrees, on average, pay big dividends in the form of higher wages over the course of one's working career. The typical college graduate with debt will have borrowed $28,500 in pursuit of a bachelor's degree. The borrower can repay that amount with monthly installments of $181 on a standard, 20-year repayment plan.

Second, the media narrative generally ignores the fact that the federal student-loan program, which accounts for more than 90 percent of the outstanding student-loan balances in the country, has since 2009 allowed borrowers to reduce their monthly payments to an amount that's pegged to their current income. According to a recent report from the Congressional Budget Office, almost half of borrowers are currently making reduced payments on an income-based repayment plan.

So, for the most part, student loans aren't unaffordable. Nor are they inescapable. Pundits and politicians often mention the fact that such loans aren't easily dischargeable in bankruptcy—but, in fact, the federal loan program includes protections to prevent borrowers from reaching the brink of bankruptcy. When federal student-loan debt remains unaffordable for a long time, that is, when the borrower's investment in education has failed to yield returns in the form of a well-paying job, the debt is automatically forgiven. That process takes 20 years for those who work in the private sector (or don't work at all) and 10 years for borrowers who work in public service. Either period is a long time to have a large debt hanging over your head, but, as noted above, borrowers needn't be making unaffordable monthly payments during that time, since all are eligible to make reduced, income-based monthly payments. Those with very little or no income don't have to make payments at all.

The problem, generally, with wide-scale student-loan forgiveness is that it would be layered onto a system that already does a decent job of helping out those who need help the most. Any expansion of eligibility for education-loan forgiveness would almost necessarily bring about a regressive change in the allocation of resources—increasing the proportion of aid being delivered to already well-off borrowers.

For example, a recent report from the often-left-leaning Brookings Institution analyzed the distribution of benefits that would result from the loan-forgiveness plan that Warren proposed. They found that the benefits would disproportionately accrue to higher-income households. The bottom 60 percent of households would receive only 34 percent of the benefits.

Those who struggle the most to pay back education loans are borrowers who don't complete their degree programs. Often, these individuals have not acquired the skills or credentials to secure the higher-paying jobs that can make loan repayment affordable. Even with the safety nets that are now woven into the federal student-loan program, many in this group face financial distress. Instead of lessening the cost of college for those who've "made it" by offering broad loan forgiveness, policymakers should consider tailoring solutions to those who most need help. One possibility would be to allow students who are normally eligible to receive federal Pell Grants during each semester of enrollment to collect more of these funds in their initial semesters. Shifting more of the grant aid to the first year or two of college would mean that students could potentially accrue less debt early on. This relatively modest change in the timing of Pell Grants could go a long way toward reducing the financial distress among student borrowers. The highest rate of default on student loans is among borrowers with less than $5,000 in debt, who are often those who started college but did not finish.

Advocates of blanket student-loan forgiveness sometimes concede the points I've made here but continue to defend the policy on the grounds that it would be "good for the economy." There is some sense in that. Sending taxpayer *(continued on page 85)*

The typical student borrower has but a modest monthly payment to make relative to his or her income—because college degrees usually pay big dividends in the form of higher wages.

Elizabeth Warren of Massachusettts proposed canceling $640 billion in student debt.

BOB DAEMMRICH / ALAMY STOCK PHOTO

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That is not a progressive policy.

The CARES Act provided for one-time relief payments of up to $1,200 to individuals making no more than $99,000 annually. The idea of sending checks to everyone did not survive—there is an income limit. Maybe there should not be an income limit. Maybe the checks should be much bigger. But would anyone explicitly propose sending checks only to those who went to college? This would be shocking even absent the reality that highly educated workers are more likely than others to be able to work remotely. Many of the restaurant workers, taxi drivers, retail clerks, and maintenance staff who have lost their incomes did not go to college and do not have student loans. If they do have loans, they may well not have been required to make payments even before the implementation of the waiver and might eventually have their debts forgiven under existing policies.

The call to relieve each borrower of up to $10,000 in debt would be akin to sending a check in that amount only to those with outstanding student loans. Quite a few people in addition to those who never went to college would be left out under such a policy: Borrowers who have just finished repaying their loans, for instance, and students who worked long hours to avoid borrowing. Imagine college classmates from similar families who borrowed similar amounts. Student A decided to work hard to pay off all his debt before following his dream to try to make it as a musician. Student B decided to travel around the world and postpone paying her loans. Now, under loan forgiveness, the taxpayers will repay Student B's loans, but Student A, who paid back every dime on his own, will receive no such benefit.

What about borrowers who put their student-loan payments on their credit cards to avoid default? They'd be out of luck. What about those Americans who have debt from medical procedures? From utility bills? From payday loans? Or fines that accumulate when debts go unpaid?

Aside from all of these inequities, one-time elimination of student debt makes little sense if future students will continue borrowing similar amounts. Some students might even feel encouraged to borrow more in the hope that those debts, too, will be forgiven. Many advocates hope that college will become tuition free, solving this problem. But the reality is that "free" college will not eliminate borrowing for college. Public colleges are already essentially tuition free for a large share of low-income students, because Pell Grants and state grants cover those charges—but many of those students still borrow to cover living expenses. In fact, students who pay no tuition graduate with almost as much debt as those who do pay tuition.

We *should* forgive some student debt, such as that carried by students who borrowed for education that did not pay off or who were defrauded by their schools. We already have separate policies to deal with those issues—policies that should be simplified, improved, and carried out.

Universal forgiveness would benefit many students from relatively affluent families who attended expensive private colleges. It would also be a gift to those who borrowed for graduate school. The Congressional Budget Office recently examined the potential cost of the existing income-driven repayment plans designed to protect borrowers from unaffordable debt payments. The study found that 20 percent of those in repayment are graduate borrowers. These borrowers owe half of the funds that are now in repayment. So, half of the benefit of forgiving that debt would go to people who went to graduate school.

Wiping out the student debt of borrowers who took these loans to invest in themselves and who are reaping the benefits of their education is not a progressive policy. Most of these individuals will have increased earnings potential and a wide range of opportunities throughout their lives that would not otherwise have been available to them. The federal government is right to provide the loans that create these opportunities. Eliminating the federal student-loan program or restricting its ability to serve students who have not yet proven themselves would erode opportunities for upward mobility. The government should continue to offer student loans while ensuring that students can't use those loans at very poorly performing institutions and that borrowers don't have to make payments that would deprive them of the ability to meet basic needs.

The economic crisis wrought by the pandemic has highlighted the sad reality that too many Americans were living on the edge even before the virus hit. Some of the people now facing the most serious struggles do have student debt, and they need a lot of support—not only so they can keep up with their education debt but also, more urgently, so they can pay rent, have enough to eat, and provide for their children. The majority of student debt, however, is owed by people who are in better circumstances than most Americans.

Student-debt relief should be a targeted policy that is part of a truly progressive agenda—not a special-interest subsidy that disproportionately helps a segment of the relatively privileged. ■

Many of the restaurant workers, taxi drivers, retail clerks, and maintenance staff who have lost their incomes during the pandemic did not go to college and do not have student loans.

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dollars out to those who are likely to spend them does have the potential to stimulate the economy (as long as the effect isn't offset by others anticipating their taxes will go up and reducing consumption accordingly). But if the main goal is stimulating the economy rather than supporting borrower welfare, there are other policy options that would more effectively achieve that end. Even throwing dollar bills out of a helicopter might work.

Under the CARES Act, Congress temporarily excused all borrowers from making payments on their federal student loans, which was a reasonable step. Even though it likely delivered poorly targeted benefits, disproportionately aiding borrowers who didn't lose their jobs, it ensured that workers who did lose income wouldn't face negative repercussions from missing a payment; nor would they need to hustle to sign up for an income-based repayment plan that would excuse them from making payments.

With that benefit set to expire at the end of 2020, the policy conversation has progressed beyond stopgap measures to a more comprehensive overhaul of the system. Senator Lamar Alexander, chair of the Senate education committee, introduced a proposal that is largely consistent with the ideals I've laid out above. Rather than offering widespread loan forgiveness, he has proposed a streamlining of the existing safety-net provisions, which will more effectively ensure that those with unaffordable debt won't have to pay. Alexander's proposal offers borrowers two options: a standard 10-year plan and an income-based plan. Under the latter, borrowers with no income would be excused from making payments. When a borrower starts earning income, the payment would be capped at 10 percent of the person's income that surpasses 150 percent of the federal poverty line. Higher-income earners would not be eligible for this benefit.

Unlike some Democratic plans that call for a one-time pardon from debt for all, Alexander's plan ensures a system that will work to ease the economic burden of student debt for troubled borrowers today but will also ensure student-loan affordability during future downturns, and even when individuals face personal financial crises.

It's easy to appreciate why widespread student-debt relief is an appealing proposal. Those of us with some years behind us empathize with today's young adults who are coming of age in a difficult economy. We want them to have every opportunity to succeed, but borrowing for education actually creates opportunities for most people. Loan forgiveness should be reserved for those who truly need it. ■