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Seven Reasons Why President Biden's Student-Loan Debt Transfer Is Bad for America

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KEY TAKEAWAYS

President Biden's plan to cancel student-loan debt and extend a repayment pause means that the government is transferring debt from borrowers to taxpayers.

This plan is expensive, regressive, and fundamentally unfair to all Americans, especially those who did not take out student loans or who paid them off entirely.

Not only is this policy on shaky legal grounds, it also creates a host of moral hazards that does not lower college costs or fix the broken higher education system.

On August 24, 2022, the U.S. Department of Education announced a plan to cancel $10,000 in student-loan debt for each borrower earning less than $125,000, up to $20,000 for each borrower under the income cutoff if that borrower received a Pell grant, and $250,000 if the borrower files taxes as married or as head of household. The Biden Administration also announced an extension of the student-loan repayment moratorium through December 31, 2022, which has permitted borrowers to delay required loan payments without accruing any interest since March 2020.[1]

The Administration's broad-based student-loan-debt "forgiveness," accurately described as a debt transfer from borrowers to American taxpayers, suffers from several policy and legal problems. The plan is expensive, regressive, arbitrary, and fundamentally unfair to those who avoided education debt or repaid their debt. It also fails to consider pernicious effects on tuition in the future, is on shaky legal ground, and creates a host of moral hazards that will burden an already broken higher-education-financing system.

The Breathtakingly High Cost

About 93 percent of student loans originate with the U.S. Department of Education through the Direct Loan programs (Direct Subsidized Loans, Direct Unsubsidized Loans, and Direct PLUS Loan). Canceling $10,000 in student loan debt per borrower earning less than $125,000 annually will cost American taxpayers $311 billion according to estimates from the Penn Wharton Budget Model.[2] Over the short term, this cost will be financed by increasing the national debt, which must ultimately be paid either with higher taxes or with even more inflationary money printing by the Federal Reserve. The costs amount to more than $2,000 in higher taxes per taxpayer, even though the overwhelming majority of taxpayers have no student loan debt.[3] "Canceling" student loan debt is effectively a debt transfer onto all American taxpayers.

The Penn Wharton figures do not include the higher $20,000 amount per Pell grant recipient. The Biden Administration estimates that about 27 million borrowers will be eligible for the additional $10,000 gift,[4] on top of the 16 million eligible for the base amount of $10,000, which would cost taxpayers up to another $270 billion. As a result, this cancelation plan could cost close to $600 billion in the first year.

Built-In Regressivity

Penn Wharton also estimated that approximately 70 percent of the $10,000 debt cancelation would benefit borrowers in the top 60 percent of income earners because a disproportionate amount of debt is held by couples close to the income cap.[5] The distribution of student-loan debt is largely skewed toward upper-income earners, with the wealthiest 40 percent of Americans owing 60 percent of outstanding student-loan debt. The lowest 40 percent of earners by income distribution hold just 20 percent of outstanding student-loan debt. Furthermore, while just 14 percent of Americans over the age of 25 hold graduate degrees, more than half (56 percent) of student-loan debt is held by households with graduate degrees.[6]

About 43 million people have federal student loans.[7] Since an estimated 27 million have received Pell grants, there are roughly 16 million people with loans who did not qualify for Pell grants, many of whom will qualify for the $10,000 level of cancelation. Pell students more often fail to graduate, and they more often attend two-year programs.[8] As a result, they have lower incomes than non-Pell students. Even so, the plan remains highly regressive even with the income caps, particularly when factoring in the extended pause on repayments.

Not only does the pause enable borrowers to avoid making even a single payment on their loans, but it also stops any interest from accruing. The Department of Education estimates that each month it loses more than $5 billion in accrued interest.[9] The planned pause of an additional four months will constitute a loss of another $20 billion. This loss is a massive gain to professionals, such as doctors and lawyers with debt from medical and law school. The Committee for a Responsible Federal Budget (CRFB) estimates that since the pause began, those holding medical degrees have received the equivalent of $48,500 in debt cancelation due largely to the pause on interest accrual, while those with law degrees have received the equivalent of $29,500. The CRFB estimates that if the pause were to continue through August 2023, doctors and lawyers would have respective total benefits of $89,500 and $54,500 per person.[10] Although the Biden Administration has claimed once again that the next pause will be the last one, it has failed to keep its promises before.

The Sheer Unjustness

Beyond the high cost and regressive nature of loan cancelation and repayment pauses, the proposal is breathtakingly unjust. Loan cancelation transfers the debt of an individual who freely agreed to repay a loan onto other individuals (through higher taxes and inflation) who did *not* agree to take out that loan. Many individuals made a conscious decision *not* to attend college in order to avoid debt. Loan cancelation foists someone else's debt onto them. Others chose not to go to college because they believed it was a bad value proposition. Still others worked their way through college to avoid debt. Many borrowers lived modestly after graduation in order to pay down their loans. The Biden debt transfer punishes the 240 million Americans who do not hold college degrees, who constitute more than half of the population ages 25 and above and are less able to bear this new burden.[11] It also punishes the millions of responsible Americans who diligently repaid the loans they agreed to take out.

The Inflationary Effect on Tuition Rewards Colleges that Waste Money

Open-ended federal subsidies have distorted the market for higher education, enabling colleges to raise tuition beyond what students and their parents otherwise would have been able to afford. The tuition bonanza has financed a "facilities arms race" replete with lazy rivers, climbing walls, and other campus extravagances. It has enabled colleges to amass large swaths of real estate in an increasingly digital age, including many classroom buildings that are largely vacant large parts of the week. And it has lined the pockets of the endowments of woke institutions. Harvard's endowment currently stands at $53.2 billion;[12] Yale's endowment tops $42.3 billion.[13]

More fundamentally, this bailout does not address rising college costs. Rather, it will significantly exacerbate them. The possibility of future bailouts will drive more students to take on higher debt burdens, which many colleges will gladly encourage for the sake of increased tuition. History demonstrates that federal subsidies have enabled colleges to raise prices with abandon. Since the 1991–1992 academic year, total federal aid (including student loans and grants) increased by 295 percent.[14] In response, universities more than doubled their tuition and fees in real terms.[15]

The Questionable Legality

A January 2021 memo from the Office of the General Counsel at the U.S. Department of Education clearly explains that the department has no authority to "forgive" or cancel student loans *en masse*.[16] Principal Deputy General Counsel Reed Rubinstein argued that "the Secretary does not have the statutory authority to cancel, compromise, discharge, or forgive, on a blanket or mass basis, principal balances of student loans, and/or to materially modify the repayment amounts or terms thereof." Rubinstein gave many reasons, including the following:

- The "Appropriations Clause" of the U.S. Constitution limits spending by the executive branch to congressional appropriations. Congress enforces its authority through the Antideficiency Act. Furthermore, the Federal Claims Collection Act "obligates agencies to 'try to collect a claim of the United States Government for money,'" while federal regulation 31 CFR 901.1(a) requires the Secretary to "aggressively collect all debts."

- "Congress does not impliedly delegate a policy decision of massive economic and political magnitude," such as loan cancelation, "to an administrative agency"; rather, Congress must directly authorize such a major decision. But "Congress has explicitly authorized cancellation...only in very limited circumstances."

Even Speaker of the House Nancy Pelosi agrees with this assessment, stating during a July 28, 2021, press conference: "People think that the President of the United States has the power for debt forgiveness. He does not. He can postpone. He can delay. But he does not have that power. That has to be an act of Congress."[17]

Finally, even if these reasons were not persuasive, mass loan cancelation "might be appropriately and necessarily considered a legislative rule under the Administrative Procedure Act," which would require a process of public notice and public comment. This is so because student debt cancelation alters the legal rights and relations of the federal government vis-à-vis borrowers. The Biden Administration, however, adopted this massive plan to cancel student debt without any opportunity for public notice and comment.

The latest General Counsel's memorandum accompanying the department's cancelation announcement effectively rescinds the prior memo, calling it substantively incorrect.[18] But the new memo offers no response to the prior counsel's opinion that an act to cancel student debt for wide swathes of borrowers would be effectively legislative and need to proceed through notice and comment before going into effect. Moreover, the new memo fails to justify the Biden Administration's chosen policy in the terms of the Health and Economic Recovery Omnibus Emergency Solutions (HEROES) Act, which purportedly authorizes the debt cancelations. That is, the memo fails to explain how canceling $10,000 of debt for borrowers who have not received Pell grants in the past, and $20,000 of debt for borrowers on the basis that they have received Pell grants at some point in the past, only for borrowers making less than $125,000 annually, is necessary to protect borrowers whose ability to pay their loans was directly impacted by the pandemic, as the HEROES Act requires. The affected classes of borrowers clearly contain many individuals whose ability to repay the loans was not impaired and who remain able to discharge their original loan obligations.

The Disastrous Policy Problems

A one-time cancelation of debts is unfair not only to those who avoided or paid off student debt in the past; it is also unfair to those who accrue such debt in the future. Do existing students qualify? Do students who started class last week or will start next week qualify? In many cases, the older siblings in a family will qualify while the younger siblings will not. Do parent borrowers receive forgiveness for the same alumnus who is already getting forgiveness, whether or not the alumnus has exhausted the full available benefit?

By opening the door to debt amnesty now, this Administration and future ones will face growing pressure for new rounds of amnesty. Until the core policy problem of easy federal money is resolved, there is no real solution to the college debt crisis. For example, without risk sharing by institutions—having a measure of responsibility when students default on their loans or must choose income-driven repayment—colleges have weaker incentives to ensure that more students graduate and earn sufficient income to fulfill their loan obligations.

The Moral Hazards

Colleges and universities are not the only entities that face perverse incentives to prolong and extend the student debt crisis by raising tuition and enrolling students who are unlikely to graduate or have sufficiently lucrative careers. Students also face moral hazards from debt cancelation and the easy money that has become even easier due to cancelation.

Many people in the past two years have chosen not to go back to work after the upheavals of 2020. With low or zero monthly payments ahead, how many will delay return to the workforce even longer?

Debt cancelation today also offers a realistic hope of more cancelation tomorrow. Why would a borrower pay down his or her debt or pay principal ahead of schedule if the loan might be forgiven? Why would a student or parent save for college rather than rely on loans that could be forgiven? Why shop for an affordable college when the unaffordable one might become affordable later? Why work during college or choose a higher paying but less satisfying job?

Moreover, this cancelation rewards college dropouts. Students who receive Pell grants have to return the unearned amounts if they drop out of school before 60 percent of their current term has passed. Presuming that Pell debts are covered by the cancelation plan, students with Pell grants will have a new incentive to take a chance on future forgiveness and drop out early in the term instead of sticking it out and perhaps completing their courses after all. This situation reduces the incentive for Pell recipients to finish their degrees, so college completion is likely to decline below its already abysmal rate of fewer than three in five students completing a “four-year” degree within six years.

Many students and parents will make financially riskier decisions out of hope that the government will bail them out.

The Most Expensive Higher Education Agenda in History?

The Biden Administration's move to "cancel" debt and extend the pause on student-loan repayments are just two parts of a broader plan that could prove to be the most expensive executive agenda in higher education history. Besides the loan cancelation and the extended payment pause, the plan includes major changes to income-driven repayment. These changes would not only cut payments in half and reduce the time to full cancelation by half, but they would also significantly raise the level at which borrowers pay nothing in the first place.[19]

Although total outstanding student loan debt is high in the aggregate, totaling approximately $1.7 trillion, it is manageable for most people at the individual level. Average student-loan debt for bachelor's degree holders who graduated in 2020 was $28,400,[20] and a majority of all Americans with student loans in 2021 owed less than $25,000.[21] In 2019, almost three in 10 Americans reported not being required to make any payments on their loans because multiple forbearance options are available, and among those making payments, typical required payments were in the $200–$299 range per month.[22] Large balances are generally held by individuals pursuing medical and law degrees—those most likely to be high-income earners. And for those having trouble making payments, the four existing income-driven repayment programs cap monthly payments at a very small proportion of discretionary income.

The Biden Administration's massive debt amnesty will exacerbate inflation. The CRFB found that the $10,000 forgiveness plan alone would counteract the first six years of the alleged deficit reduction predicted through the so-called Inflation Reduction Act. Debt cancelation and the repayment pause extension will also make the labor market worse. Heritage Foundation economists have found that young Americans ages 20 to 24 have had the largest declines in employment since the start of the pandemic (other than those ages 65 and older).[23] The fact that they have not had to repay any amount of their student loans has made it easier for them not to work. Wiping away upwards of $20,000 from their debts will give them even less incentive to engage in productive, career-building work.

There are nearly two job openings for every unemployed worker today. If the Biden Administration wants to make it easier for people to repay their student loans, government policy should make it easier for people to work and earn rising incomes. Instead, federal policies and anti-business actions not only have raised barriers to work, but also have driven rampant inflation that has erased $5,100 of value from the average worker's paycheck over just the past year.[24] That is far more of a burden than the entirety of the average annual student loan payment.

If the Administration were serious about reducing college costs and providing relief to students and taxpayers, it would begin to wind down the federal student-loan program. In fact, as the Administration has tacitly admitted through the very act of canceling student loans, the existing federal loan program does not work.

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