

Adam Looney

The comments expressed here my own views and not necessarily the University of Utah or any other organization.

Income-driven repayment (IDR) plans offer financial relief to student loan borrowers experiencing temporarily low income by reducing or eliminating entirely their monthly payments. After a period of time (20 years for undergraduate borrowers) any remaining debts are discharged. On average, borrowers enrolled in IDR plans are expected to repay less (in present value) than the amounts they borrow, which means IDR plans result in a subsidy from the federal government to IDR borrowers and the institutions they attend. A large and rising share of borrowers are enrolled in IDR plans, which has increased the total subsidy (and cost) associated with federal student loans.

In this regulatory process, the Administration proposes to revise the parameters of income driven plans to make plans more favorable to borrowers. While the details of the proposed rule are not yet known, during [negotiated rulemaking](#) earlier this year participants discussed several potential changes that would reduce borrower payments and/or accelerate loan forgiveness, including reducing the percent of discretionary income borrowers pay each month (e.g. from 10% to 5%); changing the definition of discretionary income to a higher threshold (e.g. income above 200% of the poverty line instead of 150%); reducing the number of years until loan forgiveness (e.g. from 20 years to 15 years); and other changes to parameters like interest accrual. In addition, the Department is proposing new rules that increase the generosity of related policies, like public sector loan forgiveness, which increases the benefits of IDR for eligible borrowers. The above changes, especially if implemented simultaneously, are likely to increase the cost of the student loan program and the subsidy to certain students.

I am not writing to advocate for any specific policy choice or set of parameters. Instead, I write to suggest that the Department of Education and the Office of Information and Regulatory Affairs (OIRA) consider several likely economic and budgetary effects of the proposed rule, include a discussion of these effects in its regulatory impact assessment (RIA), and design the regulation in consideration of these effects.

In particular, regulators and OIRA should examine the budgetary cost of the regulation taking into account changes in borrower and institutional behavior likely to occur, its distributional effects, and its economic effects.

According to the Congressional Budget Office's (CBO) baseline budget [estimates](#), on average, new student loan borrowers are expected to repay (in present value) about \$1 for each \$1 they borrow. In other words, on average, it costs about the same to a student (and nothing to federal taxpayers) if a student pays for college out of pocket or with private grants than if the student instead uses a student loan. Some borrowers pay more and some less. In particular, CBO recently [projected](#) that borrowers currently enrolled in IDR plans repay \$0.83 for each dollar they borrow (which is one reason why enrollment in IDR has increased and the cost of federal student programs have increased).

Changes in IDR plans that reduce the amounts borrowers repay are likely to increase the subsidy cost of student loans. Plausible changes in IDR parameters (like those discussed in negotiated rulemaking) are likely to result in substantial subsidies for a large share of new students, for many existing borrowers,

and at specific institutions and programs. It is plausible that it will more beneficial to choose to pay for college and graduate school with student loans rather than out of pocket for a large share of students and at many institutions and programs. If so, students are likely to borrow more and repay loans more slowly in general, and particularly at higher cost and lower-quality institutions, where the benefits of IDR enrollment is greatest. The stakes are large. Existing borrowers owe \$1.6 trillion. Enrolled students borrow close to \$100 billion in new loans each year. The educations financed by these loans are among the most important and valuable investments Americans make in their lives. Hence, it is important to understand how changes to IDR affect the budgetary cost, distributional effects, and economic consequences of the student loan system, and OIRA and regulators should examine how any specific proposal affects such outcomes.

The remainder of my comments outline several potential impacts of changes to IDR regulations, motivates why they are important to consider, and suggests some specific elements to consider:

First, what is the effective subsidy cost for new student loans in the aggregate and for borrowers who are expected to enroll in IDR?

The average subsidy or cost per dollar borrowed is important for understanding the total cost of new loans, the incentives students have to take out loans or increase the amount they borrow, the incentives of existing borrowers in fixed-payment plans or non-IDR plans to switch to IDR plans, the incentives for students to enroll in different programs or institutions, and the incentives for institutions to raise tuition prices or expand program offerings.

As recently as 2017, the CBO estimated that, on average, student loan borrowers would repay about \$1.11 for each \$1 they borrow. For loans issued in 2022, they expect borrowers to repay about \$1 for each \$1 they borrow. If IDR's generosity is increased substantially, it is likely that, on average, new borrowers will be expected to repay less than \$1 for each dollar they borrow (with the remainder eventually forgiven). How much below \$1 will it be?

If borrowers will expect to repay less than \$1 for each \$1 they borrow, the consequences could be significant. For some students, loans would be equivalent to grants (in the sense they will expect not to pay them back); other students might view them as partial grants. The incentives to take out a student loan and enroll in IDR would be quite different than today or in earlier years, when IDR operated as a cost-neutral insurance program in which most borrowers repay their loans (with interest), while protecting unlucky borrowers against temporary periods of unemployment or low-income.

Second, what is the budgetary impact of the proposal?

A direct effect of a proposal to increase the generosity of IDR plans is to increase the cost associated with loans currently enrolled in IDR. Today there are about \$540 billion of loans enrolled in IDR plans. One effect of an increase in IDR generosity is to reduce the payments of those borrowers depending on the changes.

However, only 34% of loans (and 19% of borrowers) are enrolled in IDR plans. If generosity of IDR plans is increased, it's likely that some or many of those borrowers will choose to take advantage of the new plan, and they will switch. Moreover, there are twice as many dollars not enrolled in IDR today than are

enrolled, so the budgetary impact could be as much as twice as large as the direct effect on those already enrolled in IDR. Hence, the RIA should account for the budget impact of that switch.

In addition, if it is cheaper to pay for college or graduate school with a student loan than it is to pay in cash, it is likely that more students will choose to use student loans and will borrow more when they borrow.

In 2016, according to the National Postsecondary Student Aid Study, undergraduates borrowed \$48 billion in Stafford loans, parents borrowed \$12 billion in Parent Plus, and graduate students borrowed \$34 billion between Stafford and PLUS loans (a total of \$94 billion).

However, students were eligible to borrow much more but elected not to: Undergrads were eligible to borrow \$105 billion more (above and beyond the \$48 billion they did borrow), Parents an additional \$79 billion, and graduate students an additional \$37 billion. That's \$221 billion in additional borrowing students and their families are currently eligible to borrow each year but choose not to.

The budgetary cost of any change to IDR should account for the fact that some fraction of people who do not take loans or don't borrow the maximum will choose to borrow. The potential scope is large and it could have a material impact on the total amount borrowed and the cost of the change.

Finally, it is likely that any increase in the subsidy associated with going to college or graduate school will increase demand for programs that are subsidized under the program, increasing enrollment in those programs, increasing the prices charged by programs, and increasing total borrowing. That also could be an important contributor to the cost of the regulation.

Third, what are the distributional effects of the program—who benefits?

I suggest measuring the distributional effects of the proposal across two dimensions. First compared to current policy, which individuals will benefit from the proposed changes to IDR? I realize this is a challenging modeling exercise given that IDR's benefits depend on an individual's debts, earnings, and family structure each year over a period as long as many as 25 years, but it is essential to understanding who benefits from the proposal.

Even in the absence of a formal model, it is obvious that changes to IDR parameters will have important distributional effects. For example, if the threshold defining discretionary income is increased from 150% to 200% of the poverty line, by definition, individuals earning less than 150% of poverty will not benefit, borrowers earning between 150% and 200% of the poverty benefit to some degree, and borrowers earning over 200% of the poverty line benefit the most. Likewise, reducing the percent of discretionary income from 10% to 5%, for example, affects certain borrowers depending on the size of their debts and their incomes. If, for example, IDR's parameters are set to define discretionary income as income above 200% of poverty and borrowers pay 5% of income, then monthly payments would be lower under IDR compared to the standard 10-year plan for a large share of borrowers, including well-educated, high-earning individuals.

To understand which borrowers benefit, it would be helpful to summarize which groups of borrowers will benefit from IDR and how much they will benefit along dimensions like their income class, demographics, and educational attainment. Student loan borrowers are, on average, from higher-

income families, are better educated, and earn more than other Americans, so it's important to understand whether proposed changes to IDR reduce or increase inequalities on those dimensions.

Second, it would be useful to determine which institutions and programs would be subsidized by the new rule. For instance, if the threshold for zero payment under IDR was 200% of poverty, then looking at the College Scorecard at programs where the median borrower would make zero payments in the second year after graduation, 75% of zero-dollar borrowers will have attended for-profit schools. It seems likely that the programs that benefit the most from more generous IDR plans will be low-quality programs where students cannot find good jobs, like for-profit schools, because their students will have their loan payments suspended or reduced because their earnings are so low. However, it also seems likely that very high-cost programs will benefit even when students find good jobs because their debt levels are so high. In either circumstance, it is plausible that if an institution raises its tuition by \$1 (or recruits an additional borrower), that additional cost will be born by federal taxpayers rather than the student or the institution. Regulators should examine which institutions and programs gain the most from IDR changes and whether these are the programs they intend to subsidize.

Finally, what are the likely economic consequences of the proposed changes?

Increases in the generosity of IDR could increase the benefits of borrowing student loans, increase the duration of loans (because people would repay them more slowly), and alter the cost and benefit of attending different programs and different institutions.

Because of the size of the loan program and the importance of educational investments to economic activity, it would be useful to understand the economy-wide effects of the proposal and its effects on the quality and quantity of education American students pursue. For instance, to the extent the proposal increases the amount of borrowing and reduces the amount borrowers repay, by how much will aggregate student debt rise over time? How will that affect borrowers' finances, access to credit, their perceptions of their financial wellbeing, and their contribution to the aggregate economy?

Given which institutions and programs will benefit, how will enrollment in those programs change and how will those students fare after enrollment? If subsidies increasingly flow to high-cost, low-quality institutions, will that change enrollment in those programs, and, if so, what will be the long-term effects for those students and the broader economy?

Thank you for your consideration as you pursue this important work.

Sincerely,
Adam Looney