Statement before the Senate Committee on Banking, Housing, and Urban Affairs
Subcommittee on Financial Institutions and Community Development

Back to School: Shedding Light on Risks and Harm in the Private Student Lending and Servicing Market

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Good afternoon, Chairman Warnock, Ranking Member Tillis, and distinguished Subcommittee Members. Thank you for the opportunity to testify today on the issues and concerns facing private student loans and servicers, as well as the state of federal student lending.

At present there are more than 1.74 trillion dollars in student loans outstanding in the US economy.[i] This is a massive amount of money that represents serious liabilities for millions of borrowers across the United States who are grappling with the process of repayment. This massive amount of outstanding debt also represents a tremendous liability to taxpayers. This is the result of President Biden's efforts to cancel student loans, which—if allowed to be implemented—will transfer that enormous liability away from the borrowers who took on the debt and onto taxpayers, many of whom never enrolled in college.

In contrast, private student loans make up just a small share of that outstanding debt. At present, 133 billion dollars of that total amount were borrowed from private lenders.

The federal student loan program and the associated portfolio of outstanding loans are in complete disrepair due to MacGyver-esque efforts from the Biden Administration to cancel student loans despite no legal pathway to do so. But the private student loan industry is a well-functioning consumer credit market.

Borrowers with private student loans are largely successful in repaying their debts. Recent reports from the industry suggest that the vast majority (97%) of borrowers are in good standing on their loans. And about three-quarters (72.5%) of them are successfully making payments. (About one-fifth of borrowers are not making payments because they are still enrolled and working toward their degrees.)[ii]

Even before the COVID-19 pandemic and the subsequent modifications to student loan repayment that have undermined borrowers' likelihood of repaying their loans, repayment on federal student loans was poor. In the ten years preceding COVID-19—which fundamentally upset trends in repayment—during an average month in repayment status there was a 52 percent chance of payments being made.[iii]

A loan program that fails to collect on the debt it issues should hardly be considered a loan program. Instead, it functions as a convoluted and opaque system of subsidies that encourages inflationary pricing from institutions and discourages thrift among borrowers.

Private student loan origination and servicing, both for federal and private loans, hasn't been perfect. Lending institutions and those that service loans are fallible. But private entities supporting student lending, in any capacity, don't deserve the ire of lawmakers looking for a quick fix—or even a scapegoat—for what is happening more broadly in student lending. In fact, there are many ways in which the private loan market could offer a model for how the federal loan program could be reformed to operate more effectively and efficiently.

The private student loan market is highly regulated, as it should be. Young people, who use student loans at high rates, can be naïve to the trade-offs involved in different financial instruments, so it is imperative that lenders comply with high standards when it comes to consumer education and disclosure requirements. Private lenders are currently held to standards that exceed the disclosure requirements that are mandated in the federal lending program. This likely contributes to the success in repayment seen among private student loans.

That said, there is room for improvement. For example, we should reconsider the treatment of private student loans in bankruptcy. Student loans are somewhat remote from eligibility for discharge during bankruptcy. Discharge of student loans does happen during some bankruptcy proceedings, but the standards for eligibility are opaque and too strict.

Lenders should face the liability of loans they originate not being repaid. This will encourage them, even more than they currently are, to only make loans in instances when they expect the borrower to be able to repay. This accountability is good for both the sector and student borrowers, even those who subsequently lose access to credit as a result.

I anticipate that the tone of the hearing today will reflect a general skepticism about private sector participation in student lending. There seems to be a persistent sense among left-leaning observers that profit seeking has no place in education at any level. In contrast, I believe that growing the role of the private sector could offer a solution to many of the challenges we are currently facing and have written as much, particularly in the arena of graduate student lending in a recent report.[iv]

While the focus of the hearing today is on the subject of private student loans and servicers, I would be remiss not to voice my concern about the state of federal student lending.

Servicers of federal student loans are often villainized by those concerned with the plight of borrowers holding federal student debt. But the actions taken in recent years by the Biden Administration have taken a difficult job and made it practically impossible. Like all of us, servicers of federal student loans make mistakes; some more than others. But if our goal is to put in place a lending program that is likely to succeed administratively, then the steps taken to complicate and manipulate the lending program, often on short notice, are steps in the wrong direction.

I am also deeply concerned, on behalf of taxpayers, about the exorbitant expense of these recent interventions. And concerned on behalf of Americans at the lawless nature in which the Administration is attempting to enact them. But I am most deeply concerned about the trajectory for higher education in the United States more generally.

The way that the Biden Administration has intervened in the marketplace for higher education has effectively deteriorated any incentives that colleges and universities previously had to charge prices that are in line with the value they provide. Likewise, students, who were previously incented only to borrow what they needed and expected to repay, would be wise to exploit the taxpayer funded subsidies that are, unfortunately, free for the taking.

I am grateful that the subcommittee has taken the time to delve into these important issues facing higher education and look forward to future action taken by members of this committee to pass legislation that would rectify the challenges we face. I thank you again for the opportunity to be here today to share my testimony and look forward to answering any questions.

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[i] Federal Reserve Board. (2024). Consumer Credit – G.19 Historical Data. https://www.federalreserve.gov/releases/g19/HIST/cc_hist_memo_levels.html

[ii] Enterval. (2024). Private Student Loan Semi Annual Report Ending Q1 2024. *Enterval Analytics, LLC*. https://www.enterval.com/#reports

[iii] Alsalam, N., Ash, E., & Pierce, B. (2024). Student Loan Repayment, 2009 to 2019. *Congressional Budget Office*. https://www.cbo.gov/system/files/2024-09/58963-student-loan.pdf

[iv] Akers, B., Cooper, P., & Pitts, J. (2024). How Private Student Lending Can Repair Higher Education. *American Enterprise Institute.* https://www.aei.org/research-products/report/how-private-student-lending-can-repair-higher-education/