Final Cut_Student Loan Episode

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SPEAKERS

Steven Valentino, Introductory Voice, Prof. Brooks

I

Introductory Voice 00:05

Welcome to A Hard Look, the Administrative Law Review podcast from the Washington College of Law. We'll discuss how administrative law impacts your daily life for regulatory actions by agencies and the litigation over them to the balance of power among branches of the government. This is A Hard Look.

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Steven Valentino 00:30

Everybody welcome back to another edition of a hard look. On today's episode, we're going to be looking at the student debt crisis and executive authority related to the issue. This episode will also take an academic approach to how educational expenses could take the form of attacks. We'll also talk about some of the regulatory and administrative law questions around loan cancellation and related issues. But before we dive in, let me take a brief moment to introduce our guests for today's episode. Professor John Brooks is presently a professor of law at Georgetown University Law Center and a visiting professor at Fordham Law School, where he will be joining them permanently in the fall. Professor Brooks received his JD from Harvard Law School. After receiving his JD, Professor Brooks worked as a tax associate for Ropes & Gray, and then proceeded to clerked for Judge Norhan H. Stahl on the US Court of Appeals for the First Circuit. He spent 10 years on the faculty of Georgetown University Law Center before moving to Fordham. His research and writing focuses on both tax law and the federal student loan program. And as a disclaimer to our listeners, the views of our guests today are his own and are not a reflection of his employer, organization firms or other individuals in which his opinions can be imputed. Professor Brooks, welcome to A Hard Look.

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Prof. Brooks 01:40

Thanks for having me.

S Steven Valentino 01:41

Let's get started. Student loans are obviously a very common thread amongst a lot of students in today's age, and a very crucial part for the educational experience. Many students are familiar with the annual FAFSA application myself included Stafford loans Grad PLUS, and the light for federal financial aid options for school. Some sources estimate that the total cost of debt is near $1.7 trillion. Before we dive into model alternatives, let's explore the logistics of the current system itself. So the system dates back to the Higher Education Act of 1965. And then there were some subsequent pieces of legislation that have augmented and modified this process. I was wondering what sort of framework was crafted based on these pieces of legislation?

P Prof. Brooks 02:23

So the student loan program has a long history that goes back even before the Higher Education Act. But the the main system that started in 1965 was a system of guaranteed student lending. So they said, We want to get money into the student into into the higher education program to help fund student tuition payments, let's set it up as get private lenders to lend the money but we'll guarantee their lending well subsidize the interest to make sure that they can make enough money. And we'll promise that we'll make them whole if the if the student doesn't pay or or isn't able to pay all of all of it back. And that was rate basically the system for a very long time. But it gradually expanded more and more lending was allowed. Students can borrow more and more there's introductions of subsidies to students to lower some of their interest payments. But the big change that happened in the 1990s was the introduction of direct lending. So instead of just having guaranteed private lending, they introduced in the 1990s direct loans from the Department of Education. So that was a pretty big change. An additional change around that time. That was really important, especially for for law students and other grad students was the introduction of the PLUS loans, which was available to graduates and also to parents. The reason that's really important for the overall thinking about the overall student loan program is that those loans allow for borrowing the full cost of attendance, your typical undergrad loan is actually pretty limited. Your typical four year student can only borrow a total of about $27,000 from the federal student loan program for an undergraduate degree. But the a grad student or a parent can borrow the full full cost of attendance, which includes not only tuition, room and board but also living expenses for for a law student, for example, that can approach $100,000 a year. So that was a huge change in terms of the amount of student lending in the system. And then what you see in the 90s is the creation of the first Income Based Repayment income driven repayment program that's called income contingent repayment. It was a pretty minimal program, but then in the in the late 2000s, and especially in 2010. those programs were expanded and made more types of loans were eligible for these income driven repayment programs. And then we had the next big change, which is super important, which is in 2010, the guaranteed student loan program was was essentially nationalized, was completely was abolished, so that all and all student, federal student lending was brought inside the Department of Education. So there was all loans would now be direct loans from the federal government, there wouldn't be no longer any subsidized private loans through the student loan program, there is some residual truly private lending, where you just go to a bank and ask for money. But through the federal student loan program, all of that is now loans from the federal government, you can borrow a lot because of the expansion of the PLUS loans, and almost all that can be run through one of these income driven repayment programs.

S Steven Valentino 05:57

Awesome. So then, obviously, on the flip side, you know, getting access to a loan is one thing and getting the capital to then go to school is critical. But on the other side of that equation is you have to repay that at some point. So can we talk through like, what are the current repayment models and structures that currently exist for students who have borrowed to go to school from the government?

P Prof. Brooks 06:17

Yeah, so these these, you know, there's the standard loan payment, which is like any other loan, you pay, you know, what is it? How do we amortize this loan over 10 or 20 years, just like you're paying off a mortgage or something like that. And that's always been kind of the baseline program, just pay it back. Like it's like it's any other loan. But these income driven repayment programs, which, as I said, started in the 90s, expanded a little bit in 2008, and then 2010, and then really blew up after that have created a whole new system of, of how to repay a student loan that is income driven, that's based not on amortizing the loan over a fixed amount of time, but it's based on a person's income. And so all these programs, there's four in particular, income contingent repayment, Income Based Repayment, pay as you earn, or and then revised Pay As You Earn or repay the big ones being IVR Pay As You Earn and repay all of these allow for somebody to pay or not pay as a percentage of their income. And typically, it's to paying, they vary a little in their terms, but the most common arrangement is to pay 10% of your discretionary income, which is actually a tax based measure of income, it's your adjusted gross income for tax purposes, minus 150% of the applicable federal poverty level, you pay 10% of that discretionary income for 20 years, sometimes it's 25 years. If you're in public service, loan forgiveness, it might be 10 years, but you know, that sort of typical would be 10 years. So what that's done then is created a system where where you, instead of just paying off your loan, like it's a mortgage, you instead pay a percentage of your income for a fixed amount of time. And then if any loan balance after that still exist, the loan would be cancelled at that point. I should know one thing that's all these programs have. They have important differences in terms of the payment period. A really important one is the treatment of interest accrual, which is complicated in a way, that's probably part hard to lay out in a podcast. But I encourage people to kind of unpack that if they're looking at different repayment options. But most of the programs except for repay, if you once your income gets high enough, you default back to paying a standard loan payment, just like you're paying off a mortgage or a car loan or something. With repay the revised pay as you earn, you actually keep paying a percentage of your income even if you have very high income. So that's and that I think, is particularly interesting, because it basically means that it's become much more like a, like a sort of an income surtax. Like you opt into this program and then you just pay a percentage of your income for a number of years and that's it and no matter what your income is. So so it's a collection of different programs, all with some important differences among each other. But the key element is that you can choose to pay your loan just as a function of your income.

S Steven Valentino 09:36

So one of the more subtle things that maybe not a lot of people like think about all the time but it's definitely a presence in this structure is that there are tax implications for payment and I'm curious what how does it typically impact somebody?

curious what how does it typically impact somebody?

P **Prof. Brooks** 09:53

The tax stuff is is really is complicated and and troubling because A standard doctrine in tax law is that any cancellation of indebtedness is assumed to be taxable. It's taxable income. If somebody, if you cancel a debt, it's as if I just gave you that money and the income tax system treats that as income and taxes it accordingly. It unless there are a lot of excluded unless an applicable exclusion, and there are many, there are many that apply to borrowers generally, like if you're insolvent, for example, then then debt cancellation isn't taxable. But there's also some that particularly apply to student loans. And it's a it's a messy area that, you know, we can unpack but but the upside is that not all student debt cancellation is is taxable, some is and some isn't some, and it's, and there's some debate about it, and it shifts over time, and depending on when the loan is cancelled, and why it's canceled. But the upshot is that some people when a loan is cancelled under an income driven repayment program, you know, after the 20 year repayment period, it's possible that they would get hit with a tax bill for that amount, which if you think about it is as if the loan isn't fully canceled. Let's say you're subject to a 25% tax rate. It's the means instead of canceling 100% of the loan, it's actually only canceling 75% of the loan, because the government's going to turn right around and say now give us 25% of that canceled loan amount right back in terms of taxes.

S **Steven Valentino** 11:30

It's really interesting. So and I think so let's let's shift gears a bit and to an area of subject or a subject area that you are you do a ton of work in this in this field is the Congressional Budget process, which is a very core part to the loan process itself. And I'm curious if you could, one illustrate the Congressional Budget process for us and then talk about afterwards the impact on the student loan process and how that affects student loans.

P **Prof. Brooks** 11:57

Yeah, I mean, the the budget process in generally generally is is really complicated and and in some ways, budget rules and and scoring rules and things like that have a huge amount of explanatory power in terms of thinking about you know, why? Congress does what it does, it explains a lot of things like the Affordable Care Act, for example, what I want to talk about is the budget rules as applied to student loans, because there's some really interesting wrinkles here that have to do with all federal credit all federal lending programs, including student loans, which is that it's very cheap for the federal government to lend money. The reason is that you'd think alone would look like an outlay, we're spending the we lend the government lends about $100 billion in federal student loans every year. But that's not treated as an outlay for budget purposes, it is not $100 billion dollar cost on the on the federal government's national budget. Instead, the way the rules work is they say, well figure out what you think you're likely to get repaid on that loan. So do an analysis of kind of expected profit, essentially, you've made you've lent out $100 billion. But you're also going to receive repayment of that plus interest, but also with some percentage likelihood of default. And it's a complicated, you know, model to figure out, you know, what is the likely amount that you'll get repaid over time and then also do a discounted present value analysis of that back to the year the the actual loan. And then and then all it's only that net cost or income, typically, that's recorded for

budget purposes. So that's complicated to explain. But the end result is that if if the government lends $100 billion, and is expected to get repaid $100 billion with interest, that has no net cost on the budget, or for appropriations purposes, and in fact, might actually even look like a profit. And this explains a ton of stuff really, I mentioned earlier that the there's a shift in the 90s from guaranteed student lending to the first introduction of direct lending of direct loans. And then later we saw a shift in the in 2010 to entirely direct lending and the end of the guaranteed student loan program. That can actually be explained in large degree by a law that was passed in the 90s. The Federal Credit Reform Act, which said said that the the accounting that I just described would apply not only to guaranteed lending, but also to direct lending. It used to be that guaranteed lending, did this kind of netting of outlays and receipts but direct lending was just treated as a as a cost. And then you had revenue when the loan was repaid that made direct lending very on on it. tractive, but for budgetary purposes, that accounting was changed in 1990. And now direct lending is cheap for budget purposes, in fact, and in fact, it's a profit center, because because the interest rates are so high on student loans, so you end up with a situation where making student loans is actually very cheap. And until recent years, it was actually a profit center for the government for budget purposes, every loan, they made, actually added revenue for budget purposes. And the government has spent that money, right, that's money that allows them to not raise as much money in taxes, they can spend that money on, you know, on roads, and fighter jets and food stamps and what have you. So each, you know, each each time a student loan is made, the government puts the money in its pocket, if that wasn't true until a couple of years ago, although it still is it still is a pretty cheap form of government spending.

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Steven Valentino 16:05

Super interesting. And then, so we have Congress, on the one hand with its budget procedures, sort of, I think hinting into its crystal ball to its policy thinking to some degree, depending on how they like to do things. But on the other hand, too, they've amended the tax code a few times. And I think that sort of tees up a question that I'm sure a lot of law students have. And students generally too is student debt cancellation. Is it a taxable event? Sort of like what's going on here? Like what what does the tax code really say on this issue? In addition to the question that's on a lot of people's minds, I guess even thinking income driven repayment to like public service loan forgiveness to is like its own little subset.

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Prof. Brooks 16:49

Yeah, the tax question, as I said, is really messy. And it's shifted a lot over time. And, and one of the weird things about this is that the, the IRS has taken the position that, let me talk about let me talk about the world before Before 20, before 2018, but even really, before 2021. Before 2018, the only type of student loan cancellation that was explicitly excluded from taxation in the tax code was for public service, loan forgiveness. And so reasonably, the IRS and any tax lawyer would look at that and say, Well, okay, debt cancellation is taxable unless there's an exclusion. The tax code tells me that only Public Service Loan Forgiveness is excluded, therefore, all other student loan cancellation must be taxable. That's another that's a standard way to, you know, just do a little bit of a little bit of tax lawyering, right? It turns out, though, that it's much more complicated than that, because there's another provision of the tax code that is relevant here, which is that scholarships are not taxable. And if you think about what a student loan is, it's just an ex post scholarship, right? It's saying instead of, you know, you pay

the loan, we'll pay your tuition. But if we then cancel some of the loan, that's in effect, a form of a scholarship, that's a form of tuition grant, it's just that it's a tuition grant that's happening kind of after you, you attend rather than than before or during. And for that reason, the IRS actually, if you go back to the 50s and 60s, the IRS said explicitly that that if a student loan was forgiven, and there were forgiveness programs back in those days, particularly for like teachers and medical students, if a loan was forgiven, that was a form of the scholarship and therefore not taxable, but then things got kind of messed up and for for reasons that I'm not sure are going worth going into, but there's a Supreme Court case that related to something that was not about student loans, but that the IRS got kind of confused about and they changed their mind. And they said, Well, wait a minute, if you if you do, if you get your loan forgiven, because you're doing something like you're working in a rural medical clinic, well, that looks more like employment income. And so that's not a scholarship and it should be taxable. And then Congress said, Well, no, that's not right. That's, we want that too. We want that to be excluded as well. And so that's why they added this public service loan forgiveness provision of the tax code, it wasn't to make public service loan forgiveness, the only kind of excluded debt cancellation. It was to correct a problem in in a bad IRS ruling and return the status quo to all student loans should be treated as scholarships, all student loan cancellation should be treated as scholarships. So the history here is really that it should all be excluded, but it's gotten all messed up and confused and the laws changed in the meantime, so that we end up With this weird patchwork where some people instead think well wait, some student loan cancellation shouldn't be taxable, because they're misinterpreting kind of the history of of provision of the tax code. Now, in current year there right now is a provision that they've passed, the Congress passed in 2021, that says, well, for the next five years, all student debt cancellation is not taxable is excluded from cancellation. But that, that expires at the end of 2025. And we go back to this crazy patchwork quilt of confusion and so on. So it's an area of the law that's unclear and shifting constantly. The current interpretations are based on I think, some serious errors in interpreting the tax code. You know, I hopefully Congress will say, well, we'll fix this cleanly by just saying all debt cancellation should be not taxable, regardless of whether it's before 2026 Or after 2026. But we'll see.

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Steven Valentino 21:02

So I think it's important to think to what that sunset date in the future, I mean, thinking between now from the date when all this initiated, like what are the effects that we see as a result of this sort of tinkering with the revenue code?

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Prof. Brooks 21:15

I've heard anecdotally that students are afraid of some students are afraid of income driven repayment because of this potential tax bill, that they think, you know, even if they get the debt cancellation, the tax bill that I'll get hit with will be will be punitive. And if you think about it, most of the people who are going to have the their debt canceled after 20 years of income driven repayment are probably people with not a lot of assets or income, which is why they're in the program in the first place. And even though the debt the tax bill will be less than the dead. You got hit with that all at once. And you have to pay it right now. Right? So it's, it's scary for some people, it's some people have referred to it as a tax bomb, because it like, you know, it just hits all at once in a way that that could be really financially devastating for some people. Now, as I said, there are other ways around it. If you're insolvent at that time, then you won't

be taxed on it. But you know, who can predict that for certain? How would you know, and and maybe you won't be insolvent, but you will be after you pay the tax bill. So there's that, you know, that that I think uncertainty about what's going to happen, right, right now, the debt cancellation is only excluded for certain for the next few years, but most student loan payments will go on well past that. So there's a lot of uncertainty. And I think that creates some problems. Now, there's an interesting question here about the interaction between the tax code and higher education, finance, the tax code is full of small provisions to help pay for college. There's tax credits, and there's tax deductions, both for tuition and for student loans, and student loan interest and things like that. Although that one has been removed recently, there's some little ton of economic work to sort of figure out how does this affect things? I know we provide all these these tax credits for tuition and so on, do they drive enrollment and things like that? And that most of the evidence shows that no, that has no, it has no effect on college related metrics, you're putting some more money in people's pockets, maybe, but you're not actually driving people to go to school or to go to school for longer or anything like that. So you have a bunch of stuff in the tax code that probably does nothing. And then you've got the potential taxation and student debt cancellation, which might do active harm. And it does raise this question of whether, you know, we use the tax code for a lot of social policy, but this is one area where it's not clear that it's doing any good and might actually be doing harm.

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Steven Valentino 24:00

So, thinking about that too, or taking it to the next step. If we think about the key provisions that are sort of at play here, what what are like actual amendments that we could see that might actually alleviate some of these potential impending harms?

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Prof. Brooks 24:13

Yeah, so there's a lot of stuff that I think we need to do. I mean, the the student loan program, I think we can all pretty much agree it's a bit of a mess. I think the idea of income driven repayment is is good, just say let everybody pay a percentage of their income for a certain number of years. And if you have a lot of income, you pay more if you have less income, you pay less, there's a certain kind of insurance built into that. And it also reflects frankly, the overall values of the income tax system generally that you know, we pay people who have received more benefits from you know, from society or everything else in the form of having higher income, pay a higher share of that back to the collective. And so I think that's a that's a good Would ideal to drive higher ed finance and student loan payments. But the the system itself is having a lot of problems in terms of its administration, in terms of some of the terms in terms of how you effectuate your rights to these things, it kind of breaks down. So really leaning into the theory that this is like an income tax. I have suggested that really, why don't we just literally implement this, as you know, through the tax system, right now, to get an income driven repayment program, you have to go to a private loan servicer, and we can talk about the servicing industry and the problems there. But you have to go to a private loan servicer to try to get in get into income driven repayment. Their incentives are not great to help, you know, you have to go through a system where they ask the IRS what your income is, but it was what your income is last year, and then you know, do you qualify and so on. And so it's as complicated, so then you have to do this every year. So it's this complicated system to prove your income, we have to go through a bunch of steps. And it's not even totally accurate, because it's last year's income. And then you have to do that every year. Well, the tax system

is pretty good at knowing what your income is, right? Now, if you have a paycheck, the tax system withholds money from that paycheck based on your current income, and for that week, or month or pay period, and we could do the same for student loans, you know, we could, if we implemented it through tax withholding, we could say, you know, gotta pay 10% of whatever your paycheck is this week, or whatever, you know, and that's how we're going to collect our loan payments, you don't have to deal with the service or you don't have to deal with recertifying your income every year, you don't have to deal with connecting to the IRS, it's based on your current income, not last year's income, there's going to be no problems with you know, collection, and so on. And in fact, we should probably make that the the automatic way loans are paid, you don't have to like opt into an income driven repayment program, just make that the rule for everybody. By the way, what I've just described is how most other countries implement their student loan programs, particularly the UK and Australia. And in Australia, they've been doing this since the 80s. And it's works really well. The other change that I think would be really important is, again, if we're leaning into this idea that it's sort of just like another income tax, why charge interest student loans, we all know, student loan interest is really high way above market interest rates, that the reason for that goes back to the guaranteed student lending program was a way to make sure banks had profit from doing this. But when you're talking about now that the government is the lender, why, you know, why have these really high interest rates? So that's another area that I think need some reform. Now, the upshot of all this is that this has got to be statutory. I mean, this is all stuff that's baked into the Higher Education Act. I don't and I think there's only, you know, this would take a pretty big reform of of higher education, finance, it would have to come from Congress. But those are some of the changes that I think would be needed to really, really make the true goals of of income driven repayment. Come to thee.

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Steven Valentino 28:04

So now, like shifting from branches of government, this time thinking we've talked a lot about congressional action, talk about administrative action, that I mean, there's a lot of discussion, even in the news today about whether or not the President can unilaterally cancel it. And I'm sure we'll reach that question in a moment. But sort of thinking broadly here, what sorts of general administrative authority do we have up at agency or presidential that can sort of begin to manifest or implement some of the changes that we sort of discussed earlier?

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Prof. Brooks 28:37

Yeah, I mean, some of the stuff I just mentioned, I think, would probably need to be statutory, for example, the interest rates are set by statute. I mean, it's, it's really sort of hard coded into the Higher Education Act. And by the way, that that's been something that's, you know, the budget scores and legislative drafters have have always kind of tweaked those numbers to to get the budget score they want. Going back to what I said earlier about how student loans actually score as generating profit for the government. In many cases, there's an interaction there where drafters kind of fiddle with the interest numbers in the legislation to get a good to get a good budget score. So that's one area where I think there's limited work that limited power at the just at the agency level. But there's, you know, going to the to the income driven repayment programs. There's an interesting history here, which is that in 2010 22,008, and in 2010, which was the sort of introduction and expansion of income, the income based repayment program, that program allowed for much more generous terms are income driven

repayment, but they realized there were a couple problems. It wasn't going to apply to any loan prior to 2014. And there were some problems with how the interest capitalisation. Rules worked as well. And so they almost immediately said, well, we need to do better. And they went into a rulemaking process with the Department of Education. But the statutory authority under under Income Based Repayment, as I said, only applied to to current, you know, later loans loans after 2014. what they realized is that there's this earlier provision of the Higher Education Act for income contingent repayment, something that was introduced in the 90s, but never really caught on. But that added allow them to have much more flexibility in terms of setting the terms like what loans applied and repayment periods and percentage of income and interest accrual and capitalization rules and all this stuff that they wanted to do better on. So they said, Well, you know, we can go back to that older authority, all this work we did in 2010, to expand the Income Based Repayment Program, in a way was actually not really necessary, because they already had the power under the income contingent repayment portions of the Higher Education Act. And that's what they used to develop the Pay As You Earn program and the revised Pay As You Earn programs, which are today really the big one. So Income Based Repayment right now has there's about $195 billion in repayment in debt that's currently in the Income Based Repayment Program. But there's about 320 or so billion dollars that's in either pay as you earn or revised pay as you earn. So so that move actually really expanded the availability of income driven repayment to a lot of people. And by the way, almost half of all debt and repayment is in one of these, one of these income driven repayment programs, it's about $550 billion of debt that's in repayment, and applies to about 9 million borrowers. It's about half of all debt, and about a third of all bar borrowers. So this isn't this is not just a set of plans that applied as a limited set of borrowers and a limited set of circumstances this is becoming central to the student led student loan program, which is one reason why I think we need to lean into some of the changes. But to reform a lot of the income driven repayment programs, they have a wide amount of authority under the income contingent repayment portions of the Higher Education Act. And there actually is a rulemaking processes that's been going on to even try to improve or reform what's existing. So there's a lot of legislative authority in that area. But for some of these bigger changes, I was talking about, like, for example, lowering or wiping out interest rates entirely or shifting collection to the to the tax system. I think that's that that's a job for Congress,

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Steven Valentino 32:51

I think it's really important to think about the scale and the amount of money and the amount of people that are actually affected by it. I think it illustrates really, that this is a very integral part of the education process that needs to be addressed in some capacity. So I think the big question the big ticket, one that a lot of people be at news, be it students, be it, you know, Congress, people that are actively lobbying the president to do this unilateral student debt cancellation? Is it possible? Are there tools? Is this one of those delegable authorities to the Secretary of Education? How does it work? If it could? Or does?

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Prof. Brooks 33:30

Yeah, this is a big one, this is a big one. So there are a number of ideas out there, the ones that you see most common are cancel everything, cancel some amount of money. And then it's the two numbers you see most common are maybe something like 50,000 of debt for everybody, or maybe $10,000 of debt for everybody. So the, you know, some degree of unilateral debt

cancellation that would be across the board and apply to everybody. And so the question is, you know, is this is their legal authority to do this administratively for just the you know, the executive branch to do this unilaterally? And this is really interesting question that actually overlaps with some of the complicated budget, stuff I mentioned earlier. So the first cut at it is that the Higher Education Act gives the Secretary of Education, settlement and compromise authority, it says you can you can adjust the amount of debt that borrower owes. And that's pretty reasonable thing to have. I mean, this often it was it was because you can imagine there lots of situations where the unique circumstances of a borrower just requires you know, some degree of negotiation about what's going on and, and the higher education access to the you know, to the Department of Education that you to the degree that you need some authority to do that kind of negotiation. You've got it. If you think it's just like a bank, they're a lender and a bank. Like as another lender could decide to cancel some of your debt if they want to. That's just a you know, as a lender, you can decide to do that and the Higher Education Act gives the department that authority. Now, the Department of Education is not a bank. They are an agency of the government. And so it's it's complex. It's more complicated than that. There's a question of what type of authority did Congress intend to give? It's most likely that Congress was thinking of this as there's something wrong with an individual's data and you need to work it out. Or there's some unique circumstances related to their situation that makes you need to need to have some degree of negotiation. did Congress intend this this settlement and compromise authority to apply to broad based student loan cancellation? Maybe not. But maybe that also doesn't matter? Because that is power they granted nonetheless. So that's one area of question. Right? Okay. They have the power to revise the amount of debt. But But is that really how Congress intended that power to be used? And so that would be one sort of question to work out. Another related question is that, again, because this is not a bank, but a government? If if they're spending money if the if the agency if the Department of Education would in effect be spending money? by canceling debt, did Congress appropriate that money under the you know, constitutional, a congress, you know, any appropriation of money, any spending of money has to come from, from Congress? Now, this is where it interacts? Interestingly, I think with the budget stuff I talked about, because it's not totally clear that they wouldn't be spending money by canceling debt because of this weird way in which the, in which loans are accounted for if all of the spending all the outlays and potential spending has already been accounted for in the year of the loan, what does it mean, when you cancel that loan later? The way it would work out is that there would be there is already a process where every year the department has to revise its estimates of the net subsidy for each loan cohort. Sorry, that sounds really technical, but basically they say, Okay, we got to, we made a guess about how much money we're going to make from a loan. And we got to, we got to revise, I guess, every year is there a broad based loan cancellation, and that's where that would take place is they'd say, You know what we thought we're going to collect X dollars from this loan. Now we know we're only going to collect x minus 10,000. And that would affect their calculation of the net subsidy rate. So to the degree that there's any cost from loan cancellation, that's where it would be reflected in a change in the net subsidy rate for a particular loan cohort. Now, it turns out that Congress has given the department permanent and indefinite budget authority for those net subsidy recalculations. Every time there's a net subsidy, count recalculation, there has already been a sort of permanent appropriations for that. So this is kind of like the layers here get really interesting, right? It's like they can cancel debt if they want to, because they're a lender. Well, what Wait a minute, Congress has to appropriate that money. But wait a minute, maybe Congress has already appropriated that money. It's it's ends up being a pretty complicated legal question when you get into the interaction between broad based loan cancellation and where the money is and where it would come from.

S

Steven Valentino 38:19

No need to add to the sort of competing tensions and factors but we mentioned loan servicers earlier, and as also, as we are aware from earlier that the education department is the agent of the governor. It's an agency it's not a bank, it's not its own private institution. Does the servicing program add any sort of competing layer to this or their appropriation problems, their tax administration problems?

P

Prof. Brooks 38:43

Yeah, this is another complication, both in terms of the success of the loan program, but also from the sort of legal and administrative issues. The loan servicers used to be the direct lenders used to be the guaranteed lenders under the the old guaranteed student loan program, when they were all put out of the lending business in 2010. Part of the compromise and it's mostly really a political compromise to not wipe them out entirely, was to say, Well, okay, we'll contract with you to service the loans. And they also, they also had some residual loan portfolio, they sold a lot of their loan portfolio portfolio to the government during the financial crisis, but they a lot of them have some residual loans, that they're also, you know, actually managing. And then the government sort of said, well, we'll also contract with you to manage the loans that we're going to make now in a normal consumer lending context, like mortgage loans. A loan servicer is collecting the payments and then distributing that money to the lenders and therefore has some skin in the game you know, like if they're not able to collect that actually kind of hurts them a little bit. Even though they're not the direct lender, they bear some risks. In the student loan context, that's not the case. The payments are always made directly to the Department of Education. None of that goes through the loan servicer. So you got to deal with the loan servicer administratively to sort of figure out, I don't know what your loan balance is. And can you get deferment or forbearance or income driven repayment or dealing with the repayment pause right now, there's a lot of stuff that you have to do with the servicer, but they're not going to see any of the money, they just get paid a flat fee from the government to kind of manage the process. And furthermore, those contracts are poorly drafted and poorly designed in a way that doesn't give them the right incentives to get you into the right programs, especially the income driven repayment programs. And so there's a lot of tension and problems there. And so the question is, well, if you're if your rights under the terms of your loans are not being effectuated, because of the way the because of things the student loan servicer is doing, what do we do about that? How are they regulated? How are they overseen now? And as contractors for the Department of Education, are they an arm of the Department of Education? Or are they a, you know, a private regulated entity, and that's not totally clear, this is a complicated area and student loan servicers and student loans in general are don't seem to be subject to the same set of regulations that apply to in a lot of other consumer lending contexts, like the Truth in Lending Act and some other related regulations and consumer protection laws. States have had some success in litigation and settlements and so on with the these private loan servicers, but some of the loan servicers have tried to claim sovereign immunity as an arm of the Department of Education, because they're under contract. And to the degree that their main regulator is essentially the Department of Education. It's a complicated relationship, because it's more that they're actually under contract with them. Not just that the department's coming in and making sure that they're, you know, acting appropriately. So there's some conflicts of interest there a little bit where the Department of Education is both kind of the main regulator, but also hiring them to do stuff, the Consumer Financial Protection Bureau has had some success in dealing with the worst parts of the student loan servicing market. But it's limited and they were almost entirely non active during the

Trump administration, they really, really, really didn't do much of anything during those years. So. So it's complicated. Now, as I said, all the money is going to the Department of Education anyway. And these guys were basically, given this con these contracts just to ease the pain of nationalizing the guaranteed student loan program. There's no real reason why they're necessary. I mean, they're just, they're just sending sending paperwork and running call centers, the department could do that themselves more directly. And I think, certainly, if the collection moved through the tax system, and if we made income driven repayment, the default program, it would mean that there was much less than you even even the small amount of need for the for a private servicing company would would go away.

S Steven Valentino 43:25

Professor Brooks, thank you for this really insightful and illuminating discussion on how this the student loan crisis is actually more than just an administrative question. There are congressional implications here and budget appropriations that are relevant. Any parting comments for our listeners?

P Prof. Brooks 43:41

I guess I would say, you know, this is this is a really massive area of both government activity and and economic activity. Generally, it's 100. As I said, it's $100 billion of lending that goes out every year that's well more than Pell Grants, for example, or other direct support. We're talking about $1.7 trillion or more of outstanding debt or maybe 40 million borrowers. And as I think we've scratched the surface of today some some really complicated and messy legal questions. So I you know, I've tried over a lot of years to bring more attention to the to the some of the interesting and complicated legal and financial and budgetary and so on issues raised by the student loan program. And I encourage, I encourage more people to dig in and look under the hood and figure out what's what's really going on here.

S Steven Valentino 44:44

Thank you so much. And as always, I want to thank our guests for his substantial and important contributions to the discussion today, the American Bar Association's Administrative Law Section, the Administrative Law Review, and of course, the podcasts own Kubra Babaturk for their continued support resources and work on making this podcast a continued contributor to the important discussions that are happening in the world of Administrative Law. Thank you and see you on the next episode.