

Statement of Senator Charles E. Grassley of Iowa
Senate Committee on the Judiciary,
Subcommittee on Administrative Oversight and the Courts,
Hearing on “The Looming Student Debt Crisis:
Providing Fairness for Struggling Students”
Tuesday, March 20, 2012

Today’s hearing fails to address why college graduates are struggling to find jobs while faced with burdensome student loan debt due to ever increasing tuition rates. Instead we’re examining how to “provid[e] fairness for struggling students.” This title is misleading because all the bill being discussed today does is give some college graduates or even college dropouts a bailout at the expense of others. Nothing being considered today helps students, unless you think telling them to take out a loan and then file bankruptcy when you either graduate or tire of school is help. We’re not seriously considering how to help out students just now preparing to enter college or a trade school, primarily because that subject isn’t within this Committee’s jurisdiction. Rather, we’re examining whether Congress should reconsider the way it overwhelmingly voted to treat private student loans, a small subset of all student loans, in bankruptcy. It seems to me that what’s on the table for discussion will not help students find jobs nor will it address the rising cost of college tuition. Unfortunately, allowing private student loans to be unconditionally dischargeable in bankruptcy will contribute to the rising cost of college tuition.

Regardless, today’s hearing intends to examine the treatment of private student loans in bankruptcy. Specifically, Senator Durbin has introduced S. 1102, “The Fairness to Struggling Students Act of 2011,” which amends 11 U.S.C. § 523(a)(8) so that private student loans are unconditionally dischargeable in bankruptcy. We’re told that this change will serve as an incentive for lenders to work out flexible repayment plans with their borrowers. However, while this may be one consequence of the bill, there may be other consequences, such as encouraging people to file bankruptcy.

In considering why student loans are treated as conditionally dischargeable debt in bankruptcy, it’s important to recognize the unique characteristics of student loans and why Congress treats them differently in bankruptcy. Unlike other unsecured loans, student loans are often long-term extensions of credit, with repayment options of up to 30 years. These are loans made to student borrowers with no assets and basically no way of demonstrating their creditworthiness, let alone demonstrating any ability to repay the loan. In how many other situations would a lender extend credit to someone in this kind of financial situation? Why do the lenders extend credit to these risky borrowers? Because student loans are essentially an investment in the student’s education, which has the promise that the borrower will eventually achieve a higher earning capacity than he or she had at the time of the loan. For other unsecured consumer loans, lenders are willing to extend credit even if those debts can be discharged in bankruptcy because borrowers have other assets that can be used to satisfy the debt in the event of default. Thus, there is a legitimate reason the bankruptcy code treats student loans differently from other unsecured consumer loans.

Today’s hearing will likely make a point that the Bankruptcy Code has not always treated private student loans as conditionally dischargeable. The Bankruptcy Abuse Prevention and Consumer

Protection Act of 2005 made private student loans subject to the same requirements as federally guaranteed student loans. This change was the result of efforts starting in the late 1990s to treat all student loans the same in bankruptcy. With the treatment of student loans as, essentially, non-dischargeable unless a debtor can show that payment would impose an undue hardship, Congress sought to limit instances where a borrower can obtain the benefit of higher education without ever having to pay for it. And individuals in the 1970s did strategically file bankruptcy just to get their student loans discharged before Congress changed the way student loans were treated in bankruptcy. Abuse was real, not just perceived as some may say. As a result of limiting discharge of student loans in bankruptcy, students can now obtain student loans at more affordable rates than ever before.

As mentioned at the outset, the proposed bill fails to provide any help to students facing high tuition costs when enrolling in college. We should be discussing how to treat the real problem, which is the outrageous cost of tuition. Congress should be considering other, substantial reforms to the market for financial aid that could provide true relief, and fairness, to student loan debtors.

One possible reform I would like to highlight is that lenders could do a better job of educating borrowers as they prepare for higher education. There are studies that show borrowers of private student loans often fail to exhaust their eligibility for federal student loans. This could be due to several reasons, but borrowers must be educated as to the consequences of these decisions. Perhaps borrowers of private student loans are not always well-informed of their repayment responsibilities, and improved disclosure requirements or educational tools could prevent students from taking out more private loans than they need.

On this point, I note an initiative by Iowa Student Loan back in my home state. Iowa Student Loan is a private, nonprofit corporation, with a mission to help Iowa students and families obtain the resources necessary to succeed in postsecondary education. Currently, Iowa Student Loan helps more than 220,000 students pay for college. As part of its work in educating borrowers before they take on student loan debt, Iowa Student Loan has in place an online counseling program that requires all borrowers of private student loans to complete. The program requires borrowers to input their college major and other data, and it shows them how much they are likely to earn after graduation and estimates how much of their income will go towards their loan payments. Iowa Student Loan has found that by going through this counseling program, students actually reduce the amount of private student loans they take out. We must address the issue on the front end, when students take on the loans, rather than years down the road through the bankruptcy code.

Incentivizing individuals to file bankruptcy in order to discharge student loan debt is a short sighted option for young debtors. This is not the purpose of the Bankruptcy Code. Moreover, when an individual files for bankruptcy protection there will be a host of consequences flowing from that decision. If Congress really wants to help provide fairness to students, then let's do so with a comprehensive review of federal higher education policy that looks at how well our current programs address the rising costs of tuition and provide value for the taxpayers' money in terms of graduates with greater employment prospects.