Comments submitted by
Center for American Progress and Campus Progress
To the Consumer Financial Protection Bureau

RE: Request for Information Regarding an Initiative to Promote Student Loan Affordability
Docket No. CFPB-2013-004
April 8, 2013

Thank you for the opportunity to submit comments to the Consumer Financial Protection Bureau (CFPB) concerning student loan affordability.

This comment is submitted by the Center for American Progress (CAP), a progressive, nonpartisan think tank dedicated to improving the lives of Americans through ideas and action, and Campus Progress, the Center's youth outreach arm. As part of its activities in developing policies to reduce poverty and ensure a stable middle class, CAP considers public issues that concern the financial well-being of low- and moderate-income households, and promotes a financial system that works for all Americans.

Since student loan debt affects millions of individuals of all ages and backgrounds, we commend the CFPB for turning its attention to this issue. We believe that the growing student loan burden could make it more difficult for families to achieve future financial security and, if unchecked, could negatively affect the housing market and the broader economy. In our comment, we will explore key characteristics of the growing student debt burden and its potential impact on borrowers and the broader economy. We will also offer recommendations to help contain the amount of student loan debt and make student loan debt more manageable.

I. The Rise in Student Loan Debt Affects Americans of All Ages

According to the 2010 Survey of Consumer Finances, 45 percent of all American families hold outstanding student loan debt, an increase from 33 percent in 2007.[1] Education debt outpaced vehicle debt for the first time in the history of the Survey of Consumer Finances as well.

Over time, young Americans have increasingly turned to student loans to finance education. Of the $1 trillion in national student loan debt, more than $600 billion has been borrowed by families with household head under 35 years of age. In 2004, 30 percent of heads of household under 30 held student loan debt; by 2010, this figure rose to 41 percent.[2] For younger workers, this debt threatens their long-term financial security, including the ability to make asset purchases such as homes and vehicles.

Yet the rise in student loan debt also affects older Americans. Thirty-six percent of families with household head age 45 to 54, and 29 percent of families with household head age 55 to 64, hold student loan debt.[3] Even among families in which the household head is in the 65 to 74 age range, 13.3 percent hold outstanding student loan debt. For these families, the ability to retire is at risk, as student loans and housing debt combine to undermine financial security.

While the number of borrowers has increased over the past decade, the size of the average student debt obligation has also risen significantly, increasing by close to $3,000 for those under 30 and $6,000 for households between the ages of 30-39.[4] For heads of household under 30, the number of borrowers who owe more than $50,000 in student debt obligations doubled from 5 percent to 10 percent between 2004 and 2010.[5] The number of 30 through 39-year-old heads of household with more than $50,000 in student debt increased from 14 percent to 19 percent.[6] And most notably, total private student loan debt more than doubled from 2005 to 2011, jumping from $55.9 billion to $140.2 billion.[7]

As the CFPB's 2012 report on private student loans noted, following the financial crisis of 2008, delinquency rates increased considerably. More than $30 billion of the $140 billion Sample Lender Portfolio was either deferred or in forbearance, while just $97 billion – less than 7 in 10 student loan dollars – was in an on-time repayment status.[8] Banks wrote off $3 billion in student loan debt during January and February of 2013, and an estimated 850,000 former students have defaulted on loans.[9] While borrowers with federal student loans have a variety of repayment options, including Income Based Repayment and Pay As You Earn, those with private student loans do not, exacerbating borrowers' inability to repay.

Student debt delinquency poses a serious risk to the short- and long-term financial health of borrowers. Those who fall behind on their payments can face poor credit ratings and wage garnishment, and the federal government and private lenders incur further expenses as they attempt to recover the loans. Addressing these challenges is both vital to the economic health and future of individual borrowers as well as the country as a whole.

II. Student Loan Debt Particularly Affects Borrowers of Color

Looking broadly at the student debt picture and its impact, 66 percent of all students take out loans to help pay for college.[10] Sixty-five percent of white students and 67 percent of Latino students, take out loans, which is close to the national average. Asian students take out loans at a somewhat lower rate of 60 percent. But among African-American students, 81 percent take out loans.[11] And African-Americans' federal student debt burdens—$30,000 on average—are far higher than other groups.[12] Twenty-seven percent of African-American graduates hold more than $30,500 in student debt, compared to 16 percent of whites.[13]

Not only do African-Americans and Latinos more frequently take out loans, but they are increasingly likely to rely on private loans rather than federal loans, which typically carry lower rates and better protections. From the 2003-04 to 2007-08 school years, there was a 16 percent increase among African American students and 12 percent increase among Latino students taking out private loans.[14] This use of private student loans often translates into higher overall student debt, with the private loans typically bearing higher interest rates. A study conducted by the CFPB found that interest rates for private student loans could reach as high as 19 percent.[15]

For borrowers of color, taking out student loans may be a necessary strategy to close educational achievement gaps. For example, although the number of Latinos with bachelor's degrees jumped 80 percent between 2001 and 2011, 20 percent more white Americans over 25 still hold bachelor's degrees than Latinos.[16] As the cost of college continues to rise and more students are taking on debt to keep up, existing educational and economic disparities will likely persist, if not worsen.

III. Economic Obstacles for Borrowers Cause a Ripple Effect for the Broader Economy

The increase in student debt is part of a perfect storm for adults in their twenties and thirties. In recent years, young Americans have faced high unemployment rates and declining wages. In fact, young Americans may lose more than $20 billion in earnings over the next ten years due to delayed entry to the workforce, according to a new analysis by the Center for American Progress.[17]

Meanwhile, rents increased more than 5.4 percent in 2012, requiring many young workers to dip deeply into their salaries in order to afford housing.[18] In fact, about half of all renters are "rent impoverished," meaning they spend over 30 percent of their income on housing, and one in four renters spends over half of their monthly income on housing.[19] Between 2009 and 2011, the number of "worst case needs" renters—those who earn below 50 percent of Area Median Income and who pay more than half their income on rent or live in severely inadequate conditions—increased by 43.5 percent to nearly 8.5 million households.[20]

Not surprisingly, declining incomes, rising housing costs, and student debt are having a ripple effect across the broader economy. First, these factors may be delaying household formation. Two million more adults aged 18–34 live in a household headed by their parents than before the recession, an increase from 28.2 percent in 2007 to 31.0 percent in 2011.[21] The situation is even worse for young people of color, with 38 percent delaying moving out on their own.[22] Moody's Analytics estimates that each new household formed leads to $145,000 of economic activity, suggesting that this delay in household formation could be slowing broader economic growth.[23]

Moreover, the delay of household formation and the financial challenges of adults in their twenties and thirties may alter the future of the U.S. housing market. The Bipartisan Policy Center estimates that Echo Boomers—those born between 1981 and 1995—will drive 75 to 80 percent of owner-occupied home acquisition before 2020 as baby boomers sell off their homes.[24] Yet, homeownership rates for young people are among the lowest in decades.

In other words, the future of the housing market is reliant on Echo Boomers buying homes, but despite attractive home prices, they face tremendous obstacles in doing so. While home prices and mortgage interest rates are both at historically low levels, the tightening of credit resulting from the housing crisis poses a double obstacle to young people with significant debt.

First, due to the implementation of new mortgage regulations under the Dodd-Frank Act, lenders are often requiring that homeowners have a 43 percent “back end” debt-to-income ratio to get a loan. In other words, combined monthly housing costs and monthly debt payments must not exceed 43 percent of one’s monthly income in order to qualify. For those with significant student debt, this debt-to-income ratio cap may well put homeownership out of reach.

Second, even young borrowers who successfully meet debt-to-income ratios may not be able to set aside enough savings for a down payment. The Center for Responsible Lending calculates that median-income families of all ages take nearly 20 years to save enough for a 10 percent down payment and closing costs for a moderately priced home.[25] Younger workers may take even longer to save for a down payment, given other immediate financial obligations, or they may simply never reach this goal.

Student loan debt will likely pose even more formidable challenges to homeownership and long-term financial security for borrowers of color. As families of color are expected to represent more than 70 percent of net household growth between 2010 and 2020, the excessive student debt burden may not only undermine these households’ financial stability but could also lead to a weaker housing market with lower homeownership rates. [26] By 2020, California real estate brokerage Movato.com predicts that half of all new homebuyers nationwide will be Latino—assuming Latino families are able to get mortgages.[27]

As a result of the factors described above, young families are likely to be discouraged by their economic prospects. A 2011 survey commissioned by Demos and Young Invincibles found that approximately half of young adults anticipate that the next generation of American families will be worse off than their parents.[28] These sentiments are echoed by statistics. While average household wealth approximately doubled between 1983 and 2010, average wealth among those in their 20s and 30s is now 7 percent less than their counterparts a generation ago.[29]

IV. Effects on Retirement Security

High student debt also threatens retirement security. According to the Center for Retirement Research at Boston College, 62 percent of workers aged 30-39 are projected to have insufficient resources in retirement. This is a far higher concentration than older age groups (55 percent of workers aged 40-49, and 44 percent of workers aged 50-59), and it has increased by nine percentage points between 2007 and 2010.[30]

Consider two workers: one who begins contributing 5 percent of her income to a retirement account, such as a 401(k) or an IRA, beginning at age 30, and another who waits to contribute 5 percent until age 40 due to continued student loan obligations. The 30-year-old earns $40,000 per year when she starts contributing, and earns a modest 5 percent return on her savings, net of inflation. At age 65, assuming modest growth in her income, she will have about $250,000 in her 401(k)—or an annuity of $1,321 per month for the rest of her life. Her counterpart who begins saving at age 40 is not as lucky: even if we assume he earns more when he starts to save —$50,000—he will only have about $160,000 in his 401(k) at age 65, or about $846 per month as an annuity.[31] Losing ten years of compounding interest reduces his overall retirement benefits by over one-third.

The combination of inadequate retirement savings and the continued existence of housing debt or rent payments in retirement is particularly damaging. Historically, families have sought to pay off their mortgage by retirement, freeing them up from shelter payments, and providing a source of funding if the home needs to be sold to finance a nursing home or assisted living.

However, post-crisis, forty percent of families with a household head aged 65-74, and 24 percent of families with a household head age 75 or older, held housing debt in 2010, according to the Federal Reserve Board's Survey of Consumer Finances.[32] In fact, families in the 65-74 age range with housing debt carry a median debt load of $70,000. What's more, nearly twenty percent of households headed by someone age 65 or older are still renting.[33] In short, more than half of families with a household head of retirement age are still dealing with rent or mortgage payments.

V. Recommendations

Giving borrowers fair and realistic options for repayment is essential to ensure that a college education is within reach for middle class families and that a college degree continues to be a ladder of opportunity – rather than a stumbling block – for students striving to reach the middle class. The following recommendations would equip households with tools to better manage student debt so that they have the flexibility to invest in their future financial stability.

1. **Develop a well-designed refinancing program for student loan borrowers.** The Center for American Progress strongly advocates refinancing options for student loan borrowers. Please see the comment submitted by Campus Progress (CFPB-2013-0004-0078) for more about the potential impact of a refinancing program.

2. **Promote broader access to Income-Based Repayment (IBR).** Borrowers of private student loans typically don't benefit from the same level of protection as those borrowing directly from the government. They should have access to options like the federal Income-Based Repayment plan. Borrowers who took out federally-backed loans before 2008 are eligible for this plan, through which they make monthly payments based on 15 percent of their discretionary income if they face financial hardship. For example, a borrower with a starting balance of $25,000 at 6.8 percent interest, for example, who earns $22,000 in his or her first year of repayment, would make monthly payments of $38. This plan provides borrowers with manageable payments when their incomes are low and loan forgiveness after 25 years of payments.

Even with attractive repayment plans, too few borrowers are aware of the options available to them to help manage their student loan debt, including reducing their monthly payment through IBR. Additionally, too many borrowers have had difficulties navigating and completing the IBR application process once they have started it. As outlined in the Center for American Progress report "Making Our Middle Class Stronger," the income-based repayment system should become an "opt-out" rather than "opt-in" program, and this change should be combined with meaningful counseling that would help students understand whether IBR is right for them.[34] Placing all new graduates on an income-based plan ensures a seamless transition to affordability.

More recently, the federal government introduced Pay As You Earn, a program that helps those who took out student loans during the recession. This new initiative improves on IBR by allowing borrowers to repay their loans at a rate of ten percent of their monthly income rather than 15 percent. Additionally, it gives borrowers who continue to make payments to have their loans forgiven after 20 years, or ten if they go into public service careers. The CFPB should continue collaborating with the Department of Education to ensure that eligible borrowers are aware of these critical opportunities.

3. **Consider including private student loans under bankruptcy protection.** We strongly support the CFPB's request for Congress to "examine the appropriateness of the bankruptcy discharge standard" with respect to private student loans.[35] The difference between private and federal student loans is stark. Private student loans often have reduced consumer protections, less flexible repayment plans, and fewer deferral and forbearance options than federal loans.

   The inability of bankruptcy judges to restructure mortgages on primary residences during the foreclosure crisis was a missed opportunity, with disastrous consequences. In the six years since, numerous government and private efforts have been made – and sweeping legal settlements have been reached – that essentially mimic the operations of bankruptcy court through "loan modifications" and "principal reduction." Yet these efforts have largely fallen short. Loan servicers are neither motivated nor equipped to do the kind of case-by-case restructuring that takes place every day in our nation's bankruptcy courts..

   Giving bankruptcy courts the power to restructure these mortgages would have potentially resulted in a shorter and less severe financial crisis for two reasons. Bankruptcy courts would have been able to address mortgage debt, and the very possibility of bankruptcy would have changed servicers' behavior from the outset. While the student loan issue is much smaller in scope, student debt touches almost as many American families, and in many cases, since borrowers in trouble often are quite young and vulnerable, the resulting harm can be more difficult to overcome.

   The bankruptcy code must be carefully examined to ensure that distressed borrowers have access to reasonable relief options and to prevent a repeat of the types of servicing challenges that emerged during the foreclosure crisis should the student debt crisis worsen.

4. **Require school certification for private student loans.** One contributor to the student debt crisis is the fact that many students borrow far more money than necessary from private sources to pay for college. Often, borrowers do so before exhausting their options for federal loans that carry lower interest rates. It seems that many students don't have a complete understanding of the various loan options available to them. We support efforts to require that a lender obtain a certification of enrollment and financial need from the borrower's school before issuing a private student loan. We also urge the CFPB to work together with the Department of Education to encourage institutions of higher education to provide counseling to students as they assess their student loan options.

5. **Encourage broader adoption of the college scorecard by post-secondary institutions, in concert with the Department of Education.** Providing students with the appropriate information and tools to help decide which school to attend is vital to their future success. A standardized college scorecard would provide consistency across a student's prospective institutions. The CFPB should work with the Department of Education to encourage schools to include a scorecard, like the one recently unveiled by the Department of Education, in all acceptance packets; the schools should also post the scorecard on school websites and on enrollment forms. Given the CFPB's student outreach mission and its role in promoting improved disclosures across the spectrum of financial products, this partnership can help ensure prospective students have the information they need to make the best decisions about their educational and financial futures.

Conclusion

Thank you again for the opportunity to comment on this notice. If you have any questions or would like to discuss anything in this letter in more detail, please contact Tobin Van Ostern, Deputy Director of Campus Progress, at tvanostern@americanprogress.org or 202-481-8144, or Sarah Edelman, Policy Analyst, Housing Finance and Policy, at sedelman@americanprogress.org or 202-481-8158.

Sincerely,

The Center for American Progress and Campus Progress

ENDNOTES

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