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# SHOULD WE FORGIVE STUDENT LOAN DEBT?

As the first female in my family to graduate from college (actually the 2<sup>nd</sup> person in my entire extended family tree to have done so, my dad being the first) I hold my college degree out as one of my greatest accomplishments as a young adult. Coming from a family of very simple means, there was no money for my college education, so I worked and I took out loans. At the time I graduated, I had \$10,000 in student loans – which was the maximum allowed at that point in time. I come from a time and place (good mid-west values!) where you accepted personal responsibility, you honored your commitments and you worked hard, so the thought of forgiving \$10,000 or \$50,000 in debt as though it were nothing ... well, that doesn't sit very well with me.

And yet, I think we need to give this topic some careful consideration.

Since I graduated from my state college some 30 years ago, the cost of tuition and fees has risen by 7% compounded annually; twice the inflation rate. During this time the average amount of student loan debt has risen from \$10,000 per student to \$30,000. That same college education that I received in the early 80's will now set a family back almost \$130,000 per student (includes tuition, fees, and living expenses). There is very little debate that higher education has gotten expensive and is placing a burden on so many of our young people who are effectively buying their first "house" but have no roof over their head to show for it!

So it is no wonder that Bernie Sanders and the rest of the Progressives have found an audience amongst those disenfranchised youth (or their parents) who now want us to wipe away a healthy amount of that debt so they can move forward into adulthood unencumbered, or at least have the burden lightened.

Here is my argument for why we shouldn't do that.

I want to start with a story (details are changed to protect privacy) to help illustrate my frustration with this whole idea.

We own rental property. In reviewing a couple of rental applications for a condo we had available, one credit report came back with a very low score. Looking further, I discovered it was due to the high amount of debt to income this young man had. Student loan debt totaling over \$300,000. There isn't a school on the face of this planet that costs \$300,000 for tuition, so what's obvious is that the loans were not just to cover school expenses, but also living expenses. We chose to not rent to this young man and when I explained the reason why, well, his response was ... interesting.

"Oh, yeah, I should have warned you that you might see that. But it's not a big deal – I mean, it's not like I'm going to actually pay back all that

money or anything." Really? And how, I asked him, was that supposed to work out (wondering all the time why anyone who was seeking to commit to a contract that required him to pay rent on time would think this was a reasonable response to their potential landlord!) – and he replied that he had entered into an IDR arrangement for repayment. IDR stands for Income Derived Repayment plan and it allows the borrower to consolidate their loans and pay a percentage of their income toward repayment of the loan. It carries with it a variable interest rate and, if executed to perfection – no late or missed payments – can be fully forgiven in 20 years. He thought that sounded like a great solution.

I couldn't help myself, after all, look what I do for a living ... so I asked him if he understood exactly what that meant for him and his new young family and their future. The interest rate on his loans was higher than the repayment rate, which meant he wasn't even covering the interest payments, which also meant that 20 years down the road, he wouldn't owe \$300,000 but probably quite a bit more. No reaction.

And then when that loan was forgiven, again if all went perfectly for tweekenty years, he was going to get a 1099 for the \$300,000 or more in loan forgiveness that was considered by the IRS as a gift (from us taxpayers to him) and he would owe taxes at ordinary income tax rates on that amount. A bit of a shocked look then. Oh, and that for the next tweekenty years, unless his income went up appreciably, that credit score wasn't getting any higher and good luck buying a house – shoot, I wouldn't even rent to him. Now he looked pretty depressed. I almost felt bad.

He wasn't the only candidate in the applicant pool with student loan issues. The other one about broke my heart. A young lady in her 70's also applied and had a similar credit score fail, but this one due to a combination of personal bankruptcy and debt. See, she had raised three children who also took out student loans that she co-signed for. When the financial crisis hit in 2008 and they all lost their jobs and couldn't make their loan payments, the loan companies came looking for the co-signer who guaranteed the payment – her. And when she, in retirement, could not also make the payments for them, she filed personal bankruptcy. Now student loans are generally not able to be discharged in bankruptcy (thanks to the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005) which means that, in order for her to be able to afford the student loan payments, she had to file bankruptcy in order to discharge all her other debt. Did you know that if you don't pay your student loan payments and you're retired, that they can garnish your Social Security check? But wait, there's a plan for this situation, too: when you die, your student loans are forgiven. How is that for golden years?

How did they and many others get into this position in the first place?

It was the perfect storm.

1. Escalating college tuition and expenses – 7% compounded increases over the past three decades.
2. The Financial Crisis of 2008 saw unemployment rates higher than 10% and many took this time to return to college and they used student loans to finance both classes and living expenses
3. Almost non-existent lending guidelines for student loans – remember the mortgage crisis anyone?
4. The inability to discharge student loans in bankruptcy – the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 made it nearly impossible to discharge student loans when filing for personal bankruptcy.

My examples are not the norm, but they were certainly real and do illustrate some of the challenges in fixing the college cost / student loan problem. If we look at the big picture, what we find is that the amount of debt has certainly gone up, but that for the most part, any forgiveness of debt is likely to help those with advanced degrees (higher earning potential) and over 60% of the total outstanding debt is owed by those making more than \$76,000 per year ([See our Graphs of the Month](#)).

President Biden made the comment recently that he didn't see any reason to forgive debt for someone who went to Harvard or Yale, or other Ivy-League school – and I have to agree with him!

At some level, these students are making a purchasing decision about their education. If they decide to buy a BMW rather than a Ford Taurus, shouldn't they expect to have to pay more money? And if they sign the loan documents to buy that vehicle, certainly they have an expectation of an obligation to pay off that loan and they understand that there are consequences if they fail in that obligation. What do we teach our young people if we always remove the discomfort of a bad decision?

There are obviously exceptions to every situation, things that fall outside of the norm. These students get student loans because universities and private lenders show them how easy it is to get them, with little or no credit counseling (and what does credit counseling even mean to an 18 year old?!) We replaced the mortgage crisis with the student loan crisis by making it easy to over-borrow at a time when some people were desperate to get ahead or simply put food on the table. Now they are paying the price, and we're all frustrated that they think it should be forgiven.

But I will also point out that we forgave a whole lot more debt following the mortgage crisis than we are talking about here. If you had the ill fortune to purchase a home at the peak of the market in 2007 and then lose your means of support, you had two options. You could 'short sell' your home – meaning you had a buyer for less than the amount of what you owed on the home. The bank would have to approve that transaction, but many of them did, understanding that something was better than nothing. That transaction would have normally resulted in a 1099 for the difference between what you owed the bank and what the bank was able to get from that sale as it represented a gift to you of the discharge of that debt, but we allowed for forgiveness of that obligation for several years following the mortgage crisis. The consequence of that transaction was a ding on your credit history for two years.

We also allow people to discharge their mortgage debt in filing for personal bankruptcy. When that happens, their credit record is impacted negatively for seven years. We allow businesses to file bankruptcy when they are unable to pay their debts. We discharge credit card debt in personal bankruptcy. You see where this is going. Why would we deny students or parents the same rights we provide under any number of other circumstances?

It is in society's best interests if we educate our young people and give them the means to that education. It is equally important that there is a cost to that education (sorry, Bernie) so that it is valued by our young people and they can feel proud, just like I did, of having accomplished this great thing that would launch them into a better life! Just forgiving student loan debt does not solve this problem. So here are a few ideas of how we begin to solve the big problem, not just the debt problem:

- Allow for student loans to be discharged in bankruptcy as we do every other type of unsecured debt
- Offer a 'short sale' type of option, forgiving up to \$10,000 in student loan debt if they can show need; forgive the taxation of that gift for the next two years, but negatively impact their credit report so there is a consequence to that decision.
- For future loans – certainly implement strict lending criteria that prevent excessive lending to students (some of this would self-resolve if creditors were no longer guaranteed that students could not default!)
- Make the universities responsible for the quality of their "product" – namely the education that they provide our children and the cost of that education. If they have to be responsible for some of the debt they encourage our students to incur, they might take more interest in helping students make smarter life decisions. I would love to see universities have to provide matching funds for federal loans – and then be responsible for collecting on those loans – just not certain we could ever get that to happen.
- The federal government does need to step up and fix the loan forgiveness they promised to certain professional degrees when those graduates satisfied the requirements of working in under-privileged communities. This was a program created during the Obama administration to incentivize teachers and medical and legal professionals to use their education and talents to help underserved communities in exchange for waiving their loans.
- State Universities need to remember the charters that established them and start making education affordable – or they no longer get funding from the state legislators. I believe there are currently few natural market forces being applied to colleges that would prevent them from continuing to increase costs excessively and at will – although the pandemic may just have given them a nudge.

Education of our young people is vital. That education has to include the education you get with a little bit of struggle and hard work and the consequences of sometimes making a bad decision. So for me, blanket forgiveness is a non-starter, but I think there is room for compromise. This has the attention of the press now, let's see where the current administration takes this.

*The views expressed here are my own and may not reflect the opinions of the other members of our team. Any constructive debate is welcome.*

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