Insight

SCOTUS Blocks the Biden Administration's Blanket Student Loan Forgiveness

TOM LEE | JUNE 30, 2023

On June 30, 2023, the Supreme Court of the United States (SCOTUS) ruled to block the Biden Administration's blanket federal student loan forgiveness plan. The plan, first announced in August 2022, called for forgiving $10,000 in outstanding balances for borrowers of federal student loans who make less than $125,000 per year and for married borrowers whose combined spousal income is less than $250,000 per year. The amount of forgiveness would have increased to $20,000 for borrowers who had received a Pell Grant while as an undergraduate student.

SCOTUS' decision ruled the Secretary of Education does not have the authority under the Higher Education Relief Opportunities Act to forgive federal student loans. Borrowers will not receive student loan forgiveness under the administration's blanket forgiveness plan.

This primer walks through the timeline of the Biden Administration's blanket forgiveness plan and its other forgiveness initiatives to date.

The Blanket Forgiveness Plan – Distorted Incentives and a Moral Hazard

Blanket loan forgiveness in any amount is unlikely to increase educational attainment or lower costs. It simply would shift the burden to taxpayers. As a result, blanket loan forgiveness would create a moral hazard by introducing a new set of disincentives for future borrowers to pay back what they owe. This would also reduce institutional incentives to find ways to lower tuition rates since they know students could receive blanket forgiveness again in the future. Blanket loan forgiveness may very well exacerbate high post-secondary education costs. Future students entering post-secondary education in 2023 and beyond would still take out loans as before – if not in greater volume. Even if the blanket forgiveness plan had been approved, outstanding federal student loan debt would have likely bounced right back to current levels by the end of 2030.

Cost Saver Becomes Huge Liability

In 2010, Congress passed a law to have all federal student loans issued directly by the federal government. This became known as the Direct Loan program, which covers most outstanding federal student loans today. The Direct Loan program was intended to be a cost saver for the federal government and taxpayers, as well as a pay-for to offset the costs of the Affordable Care Act. It has, nevertheless, already become a major taxpayer liability due to lack of repayment by borrowers, a feature largely of the Department of Education's (ED) design. The administration's blanket forgiveness proposal would have dramatically exacerbated this taxpayer liability.

Thinly Veiled Blanket Forgiveness Through Income-driven Repayment

In January 2023, ED proposed new regulatory changes to income-driven repayment (IDR) plans for federal student loans – particularly the Revised Pay As You Earn Repayment Plan, or REPAYE. These proposed changes have been finalized and will go into effect this July. The changes to the REPAYE plan at least halve the monthly required payments on outstanding balances and in some cases reduce the number of payments needed until the borrower is eligible to receive automatic forgiveness. While the blanket forgiveness plan would have provided forgiveness up front all at once, IDR provides forgiveness spread out over years.

As with the administration's blanket loan proposal, expanding forgiveness through IDR does nothing to lower the cost of college. Dispersing loans and requiring borrowers to pay back only a fraction simply shifts the rising costs of college tuition – and thus, student loans – to taxpayers who did not take the loans. This policy, like blanket forgiveness, also introduces a moral hazard in which future students are incentivized to take large loans with the expectation of having the loan partially or fully forgiven. Further, the proposed changes reduce universities' incentives to control costs, since they expect their students to be bailed out at some point in the future.

Targeted Forgiveness and Expanded Eligibility

In October 2022, ED released final regulations on five federal targeted student loan forgiveness programs. These regulations are slated to go into effect in July 2023. The five programs codify certain standards under which the federal government can cancel borrowers' outstanding federal student loan balances. The final rules mainly ease the programs' eligibility requirements, allowing the Biden Administration to forgive the loans of more borrowers, namely those who currently attend or have attended for-profit colleges.

The final rule also eliminates all instances where interest capitalization is not required by the Higher Education Act. This means, as the rule holds, that "interest will no longer be added to a borrower's principal balance when a borrower first enters repayment, after periods of forbearance, and upon leaving all IDR plans except for IBR [income-based repayment]." This includes the Pay As You Earn (PAYE) and REPAYE plans. These specific changes to interest capitalization provide student debt "relief" by reducing the rate at which outstanding balances can grow due to borrowers not paying interest but does not entail forgiveness and its associated issues.

Repayment Begins in October

As part of the debt-ceiling deal struck in May, Congress has ordered the ongoing three-year pause on repayments of federal student loans to end. This prevents the Biden Administration from once more extending the current payment pause on federal student loans that was originally set in March 2020 as part of COVID-19 pandemic economic relief. Borrowers of federal student loans will need to begin repaying their loans again in October 2023.[1]

[1] https://studentaid.gov/