Insight

The Biden Administration's New REPAYE Plan: Thinly Veiled Blanket Student Loan Forgiveness

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Executive Summary

- On January 11, the Department of Education proposed new regulatory changes to income-driven repayment (IDR) plans – particularly the Revised Pay As You Earn Repayment Plan, or REPAYE – for federal student loans that focus on lowering repayment and expanding forgiveness under IDR plans.
- If finalized, IDR would become a form of blanket loan forgiveness, as it would dramatically reduce or eliminate the amount federal loan student borrowers would have to pay back.
- As with earlier blanket loan forgiveness, these changes to IDR would do nothing to lower the rising costs of higher education, and instead simply shift students' loan balances to taxpayers.
- The proposed changes to IDR would be made through the negotiated rulemaking process, and as such, they would become a permanent part of the federal student loan system.

Introduction

On January 11, the Department of Education (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 – that would greatly reduce repayment under IDR and allow borrowers to have their loans completely forgiven after a period of successful payments. If finalized, IDR would become a form of blanket loan forgiveness, as it would dramatically reduce or eliminate the amount federal loan student borrowers would have to pay back.

Currently, IDR plans set monthly payments on outstanding federal student loan balances to a certain percentage of a borrower's discretionary income, usually 10 percent, regardless of their total outstanding federal student loan balance. ED provides four different types of IDR plans. Depending on the specific type of loan and IDR, borrowers who make 20–25 years of successful payments receive forgiveness on any remaining debt owed.

The proposed changes under the REPAYE plan would at least halve the monthly required payments on outstanding balances and in some cases shorten the number of payments needed until receiving automatic forgiveness. A Penn Wharton Budget Analysis found the forgiveness associated with the new REPAYE plan, into which most forms of IDR would be consolidated, could cost between $333–$361 billion over 10 years.[1] The same model found the Biden Administration's one-time blanket loan forgiveness plan would cost $469 billion.[2]

As with the administration's earlier blanket loan proposals, 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 also introduces a moral hazard in which future students 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. Finally, as the proposed changes to IDR would be made through the negotiated rulemaking process, if finalized, they will become a fundamental and permanent part of the federal student loan system.

Proposed Changes to IDR

There are currently four types of IDR plans administered by ED[3]:

1. Revised Pay As You Earn Repayment Plan (REPAYE);
2. Pay As You Earn Repayment Plan (PAYE);
3. Income-Based Repayment Plan (IBR); and
4. Income-Contingent Repayment Plan (ICR).

Under the newly proposed regulatory changes, ED would phase out PAYE and ICR while limiting the circumstances under which borrowers may enter IBR, thereby requiring most borrowers who enter IDR to enroll in REPAYE. The more specific changes focus on lowering repayment and therefore expanding forgiveness under the REPAYE plan[4]:

1. Lower the current required monthly repayment rate from 10 percent of discretionary income to 5 percent for undergraduate loans, effectively halving borrowers' monthly payments.
2. For borrowers with graduate and undergraduate loans, pay between 5 to 10 percent using the weighted average "of their original principal balances attributable to those different program levels."
3. Increase the threshold of calculating discretionary income from 150 percent of federal poverty guideline to 225 percent, thus significantly reducing the amount of income that can be used to calculate monthly payments and lowering or eliminating monthly payments for borrowers who enroll in REPAYE.
4. Borrowers whose discretionary income is below 225 percent of the federal poverty guideline would have $0 monthly payments but still receive credit toward forgiveness.
5. If a borrower enrolled under the new REPAYE plan becomes unemployed, their monthly payment would drop to $0 but they would still receive credit toward forgiveness.
6. Borrowers in REPAYE owing $12,000 or less would receive forgiveness after 10 years of payments instead of the current 20-year level for undergraduate loans and 25-year level for graduate loans.

For every $1,000 borrowed above the $12,000, one year of monthly payments would be added to the total time before receiving forgiveness until reaching the 20-year mark for undergraduate loans or 25-year mark for graduate loans. For example, a borrower owing $13,000 in undergraduate loans, would receive forgiveness after 11 years, while under the current plan they would have received forgiveness after 20 years. A borrower owing $21,000 would receive forgiveness after 19 years. A borrower owing more than $21,000 would receive forgiveness after 20 years.

Borrowers making monthly payments that are not enough to cover accrued interest would no longer be charged on that accrued interest.

REPAYE Would Offer a Form of Blanket Forgiveness

According to ED, under the newly proposed changes to REPAYE, “any individual borrower who makes less than roughly $30,600 annually and any borrower in a family of four who makes less than about $62,400” would have $0 monthly payments and still receive credit toward forgiveness.[5] Even if a borrower’s income exceeds these amounts, ,their monthly payments would still be cut in half on undergraduate loans, since their required monthly payment would decrease from 10 percent of discretionary income to just 5 percent. ED also has stated “future cohorts of borrowers would see their total payments per dollar borrowed decrease by 40%. Borrowers with the lowest projected lifetime earnings would see payments that are 83% less, while those in the top would only see a 5% reduction.”[6]

The proposed changes to IDR would essentially render the plan another form of blanket student loan forgiveness. A Penn Wharton Budget Analysis found the forgiveness associated with the new REPAYE plan could cost between $333–$361 billion over 10 years.[7] The same model found the Biden Administration’s one-time blanket loan forgiveness plan would cost $469 billion.[8]

Rising Costs and Bad Incentives

Student loan forgiveness in any amount does nothing to lower the cost of higher education and may even produce higher costs for students by removing universities’ incentives to lower tuition because they expect their current and former students will be bailed out. This presents a moral hazard with the expectation that future forgiveness will persist into the future. Current and prospective students will pay the same if not higher tuition rates, but they will enter with the assumption that they will receive large amounts of forgiveness if they eventually enroll in REPAYE. These proposed changes to IDR are going through the negotiated rulemaking process. If finalized, the expanded forgiveness under IDR would become a fundamental and permanent part of the federal student loan system.

[1] https://budgetmodel.wharton.upenn.edu/issues/2023/1/30/budgetary-cost-of-proposed-income-driven-repayment

[2] Ibid

[3] https://studentaid.gov/manage-loans/repayment/plans/income-driven

[4] https://www.federalregister.gov/documents/2023/01/11/2022-28605/improving-income-driven-repayment-for-the-william-d-ford-federal-direct-loan-program

[5] https://www.ed.gov/news/press-releases/new-proposed-regulations-would-transform-income-driven-repayment-cutting-undergraduate-loan-payments-half-and-preventing-unpaid-interest-accumulation

[6] https://www.ed.gov/news/press-releases/new-proposed-regulations-would-transform-income-driven-repayment-cutting-undergraduate-loan-payments-half-and-preventing-unpaid-interest-accumulation

[7] https://budgetmodel.wharton.upenn.edu/issues/2023/1/30/budgetary-cost-of-proposed-income-driven-repayment

[8] Ibid