Center for American Progress

AP PHOTO/PAUL SAKUMA

# Increasing Postsecondary Attainment Through Smarter Student-Loan Repayment

By Elizabeth Baylor and David Bergeron March 26, 2015

# Introduction and summary

By the year 2020, nearly two-thirds of U.S. job openings will require postsecondary education, according to workplace projections by Georgetown University's Center on Education and the Workforce. Those projections show that 35 percent of jobs in 2020 will require a bachelor's degree and 30 percent will require an associate's degree or other education credential.[1] Based on current postsecondary education attainment levels, this data means that the U.S. economy will soon face a shortfall of 5 million college-educated workers.[2]

Meeting future workplace demand means significantly boosting the share of Americans who have attained high-quality postsecondary education degrees and credentials. According to the most recent data from the Organisation for Economic Co-operation and Development, or OECD, 43 percent of Americans have earned a postsecondary degree or credential, and of those same Americans, 32 percent have attained a bachelor's degree or higher.[3]

Today, the U.S. economy has $1.3 trillion in outstanding student-loan debt; $1.1 trillion of that debt is the result of federal loan programs with the remaining $200 billion in student-loan debt coming from private lenders.[4] Outstanding federal student-loan debt equaled $27,800 per borrower in 2014, which is up from $18,300 per borrower in 2007.[5] The system of collecting federal student loans relies on servicers and collection agencies that have little incentive to prioritize the financial well-being of students because the cost of providing the service and the amount of loan debt collected drive the allocation of the portfolio. In addition, choosing a repayment plan is complicated because new plans have been layered upon each other over time.

The federal government must play a crucial role in increasing postsecondary education attainment, specifically by ensuring that American students have the financial resources needed to go to college and by minimizing the amount of debt they are required to take on. To address these challenges, the Center for American Progress recently released a new plan for the U.S. higher-education system, College for All. College for All would guarantee that every high school graduate would be able to attend four-year, public institutions without having to incur any tuition or fees while enrolled. Students attending private schools would receive support equivalent to the cost of a public institution's tuition and fees. Graduates would be required to repay the cost of their tuition and fees, but repayment would be based on their income. Pell Grants and American Opportunity Tax Credits would be retained and targeted at the most at-risk students in order to cover the full cost of attendance or support their attendance at private institutions.

This proposal calls for modernizing the way student loans are repaid in order to promote affordability, eliminate default and its detrimental economic consequences, and reduce taxpayer costs. Ultimately, CAP proposes the creation of a new system that utilizes the Internal Revenue Service's, or IRS's, wage-withholding system to repay student loans automatically. This modern system would make all borrowers eligible for simple, affordable repayment terms based on income and employ modern data exchanges and smart strategies to help students proactively manage student-loan debt. Automatic loan repayment would be the default method of repayment under the new system; it would offer incentives to student borrowers to boost participation.

This report describes the elements of the universal wage-withholding system for student-loan repayment and outlines an implementation process that would allow the Obama administration to begin to pilot the system to ensure it works well. The pilot would begin by allowing federal workers with student-loan debt to repay some loans automatically and expand the pilot to workers in the private sector. If College for All were adopted, this model could be further streamlined to manage postsecondary education financing. Even without the expanded benefits of College for All, this new system of repayment would help borrowers by streamlining the process for repayment and expanding access to affordable repayment terms, minimizing their risk of default.

CAP proposes the following elements of the program:

- **Use the IRS's wage-withholding system to automatically repay student loans:** Congress should enact legislation to allow all borrowers with outstanding student-loan debt—including those with private loans and Federal Family Education Loan, or FFEL, Program loans—and new borrowers to automatically repay their loans using the IRS's wage-withholding system.

- **Provide simple, affordable repayment terms for all borrowers:** Ultimately, all federal student-loan borrowers who participate in this new system would be eligible for a single, simple income-based plan. Terms would be similar to today's Pay As You Earn, or PAYE plan, which caps monthly payments at 10 percent of discretionary income and allows for the elimination of any remaining debt after 20 years. Individuals who earn enough would amortize the amount owed in order to finish repaying their loans after 10 years, similar to today's standard repayment plan.

- **Share the savings:** Once phased in, automatic loan repayment through wage withholding would be the standard repayment method for workers with student loans, but existing borrowers would have the ability to opt out of the system if they preferred to retain their current repayment to servicers. Since wage withholding would be less expensive for the U.S. Department of Education to run than the current system of using third-party servicers and collectors, a portion of that savings could be shared with borrowers to create an incentive for them to participate.

- **Build a smarter system that proactively helps borrowers manage their debt:** The modern loan repayment system would optimize affordable loan repayment. It would use modern data exchanges within the federal government and private-sector partnerships to proactively help students manage their debt. In order to eliminate default and its grim economic consequences, borrowers with economic hardship would be proactively reassigned a monthly payment based on income in order to ensure affordable repayment. For example, if a borrower applied for unemployment insurance, information communicating this status could be shared between the U.S. labor and education departments, and the student would be reassigned a monthly payment—likely very low—based on the new income level.

This program would require legislative action in order to provide all borrowers with access to its wage withholding and to create incentives in the form of shared savings. Streamlining repayments terms would also require legislative action. The U.S. Department of Education could move forward with a pilot of the wage-withholding mechanism through the following:

- **Create a smooth transition to the new repayment system beginning with the federal workforce:** The Obama administration should use its executive authority to pilot an automatic student-loan repayment program within the federal workforce. The federal government would use existing payroll systems to calculate monthly payments and automatically credit student-loan accounts held by employees. Federal workers with bank-based FFEL loans could consolidate into the new program structure in order to take advantage of the wage-withholding system.

- **Partner with private-sector employers to allow borrowers to pay their federal direct loans through wage withholding:** Once the U.S. Department of Education has developed the capacity to direct wages to outstanding federal loans, it could engage private employers that would like to provide this service to their employees.

Together, these changes would make student loans more affordable and ensure that student borrowers are in repayment plans that promote both economic wellness and stability.

The Center for American Progress is a nonpartisan research and educational institute dedicated to promoting a strong, just and free America that ensures opportunity for all. We believe that Americans are bound together by a common commitment to these values and we aspire to ensure that our national policies reflect these values. We work to find progressive and pragmatic solutions to significant domestic and international problems and develop policy proposals that foster a government that is "of the people, by the people, and for the people."

Center for American Progress

1333 H STREET, NW, 10TH FLOOR, WASHINGTON, DC 20005 • TEL: 202-682-1611 • FAX: 202-682-1867 • WWW.AMERICANPROGRESS.ORG