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TESTIMONY
U.S. Senator Jack Reed
Institutional Risk-sharing

Committee on Health, Education, Labor, and Pensions
Reauthorizing the Higher Education Act: Exploring Institutional Risk-sharing

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I would like to thank Chairman Alexander, Ranking Member Murray, and the members of the Committee for inviting me to testify on what I believe is a critical area of needed reform for our student aid programs and higher education more broadly – requiring our colleges and universities to bear greater responsibility for student loan debt. Chairman Alexander has taken a very thoughtful approach to looking at this issue – as have others on this Committee, and I thank you all for your leadership.

We all know that postsecondary education is required for most family-sustaining, middle-class jobs, and that an educated workforce is essential to a modern, productive economy.

Yet, just as there is growing recognition that postsecondary education is indispensable in the modern economy, families are being required to shoulder growing debt burdens that severely impact the lives of borrowers to the point of threatening access to college and restricting our nation's economic growth potential.

According to a recent analysis of student loan debt by the Federal Reserve Bank of New York, between 2004 and 2014, there was an 89 percent increase in the number of student loan borrowers and a 77 percent increase in the average balance size. Today, over 40 million Americans have student loan debt, with the outstanding balance exceeding $1.2 trillion.

This is a growing drag on our economy. As student loan debt has grown, young adults have put off buying homes or cars, starting a family, saving for retirement, or launching new businesses. They have literally mortgaged their economic future.

We know that student loan borrowers are struggling. And defaults are on the rise. The Federal Reserve Bank of New York reported that the number of borrowers who default each year has increased from about half a million 10 years ago to 1.2 million annually in 2011 and 2012. Only 37 percent of borrowers are current on their loans and actively paying down their debt.

We cannot tackle the student loan debt crisis without states and institutions also stepping up and taking greater responsibility for college costs and student borrowing.

Institutions of higher education can take action to reduce the likelihood that a student will default on a loan. However, under current law there is little incentive for them to do so until default rates reach excessive levels such as their three-year cohort default rate exceeding 30 percent for three years. In other words, nearly one in three students would have to default by their third year in repayment before an institution would be obligated to take action.

The financial crisis showed us what happens when certain players in the system can reap the rewards of easy credit without having to bear any of the consequences of making reckless, risky decisions. The players that created and sold exotic financial products got rich while middle income families lost their homes and taxpayers had to bail out the financial system.

We only have to look at the collapse of Corinthian Colleges to see that we face a similar problem in the higher education sector. Students have been left in the lurch and taxpayers on the hook because of a business model based on maximizing enrollments and student loan revenue – with little responsibility for outcomes.

I introduced the Protect Student Borrowers Act with Senators Durbin, Warren, and Murphy to ensure that institutions take greater financial responsibility when it comes to student loan debt by setting stronger market incentives for colleges and universities to provide better and more affordable education to students, which will in turn help put the brakes on rising student loan defaults.

We introduced this legislation to move the conversation forward – beyond whether institutions should bear greater responsibility for student loan debt to how to design a system that puts the right market incentives in place for them to assume such responsibility.

The Protect Student Borrowers Act would hold colleges and universities accountable for student loan defaults by requiring them to repay a percentage of defaulted loans. Only institutions that have 25 percent or more of their students borrow would be included in this risk sharing based on their cohort default rate. Risk-sharing requirements would kick in when the default rate exceeds 15 percent. As the institutional default rate rises, so too would the institution's risk-share payment. These payments would be invested in helping struggling borrowers, preventing future default and delinquency, and reducing shortfalls in the Pell Grant program.

We need to tackle student loan debt and college affordability from multiple angles. And we need all stakeholders in the system to do their part. With the stakes so high for students and taxpayers, it is only fair that institutions bear some of the risk in the student loan program.

I commend Chairman Alexander and Senator Murray for putting this topic on the reauthorization agenda. I look forward to working closely with this Committee and our colleagues on refining the risk-sharing concept and including tough, fair, and workable provisions in the Higher Education Act to ensure that we truly have shared responsibility for student success.

Thank you.