Causes Consequences and Policy Responses to the Student Loan Crisis

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Introduction

Receiving a college degree and going for higher education has become one of the most popular choices among students and parents in the United States of America. It has become an integral part of the American dream. Most parents and students believe that a college degree from a prestigious institute can secure the future and land a job that pays off the bills, as well as increase the chances of living a quality life. Hence, they believe that the dramatically increasing tuition fees of colleges and universities are worth every penny. The number of people financing their college education through federal and private loans has proliferated, which makes it the second largest source of consumer debt after house mortgages. The $1.3 trillion and 44 million figures describe the 2017 source period. Federal Student Aid reported that, as of March 31, 2026, the outstanding federal student-loan portfolio included approximately 42.6 million recipients and totaled about $1.7 trillion. These federal figures do not include the entire private student-loan market, and individual graduate debt varies widely by program and borrower. The major contributor to this increase in the national student debt crisis is the rapid growth of college tuition fees. According to Bloomberg (2012), the cost of attending college has increased by 1,000 per cent in the past three decades. Another reason for student loans is the economic recession of 2008, which boosted college tuition and people's dependence on loans to attain a college degree. Higher education has become crucial in the American economy, as it helps people get decent employment and secure a quality life. Hence, the percentage of the American population enrolling in colleges and graduating with a bachelor's degree has increased.

Since universities' tuition is increasing each year massively and the possibility of borrowing student loans from a federal or private lender is limitless, this has put many young Americans who are pursuing higher education in major debt. Even though there are some student loan forgiveness programs, this doesn't solve the root of the student loan crisis in America, which begs us to find a better solution. One way to help reduce this problem is to repeal or revise [11 U.S.C 523 (a) (8)] amendment and evaluate individual borrowers depending on their future ability to repay their student loan.

Types of Student Loans

The majority of the population of the United States of America depends on loans to attain higher education. There are two types of major student lenders, which include federal loans and private

loans. However, the dominant student loan lender is the federal government since they are available to everyone.

Federal Loans

The United States Department of Federal Education offers three types of student loans: the William D. Ford Federal Direct Loan (Direct Loan) Program, Stafford Loans, and Perkins Loan. Each type of loan serves the purpose of providing financial help to students who can't afford a college degree, which covers a majority of the American population.

Stafford Loans

Stafford loans are the most popular type of student loan offered to American students today. The eligibility requirement for a Stafford loan is to be a citizen of the United States of America pursuing a college degree, which, in other words, means almost anyone can apply for the loan and receive it without any effort. Moreover, this also requires the applicant to have no outstanding debts to the federal government of the United States of America. These loans have a grace period of six months from the time the student who has borrowed the loan finishes school or drops below the requirement for at least half-time enrollment in a college, university or an educational institute until they are legally required to pay back their loans. Stafford Loans had fixed interest rates, and loans first disbursed from October 1, 2017, to October 1, 2018, carried a 1.066% origination fee. That figure is historical and should not be treated as a current fee. The Stafford loans have two general categories, i.e., subsidized and unsubsidized loans.

Subsidized Loans

Subsidized Loans are the ones that are covered by the government for interest payment while the student is in college. These types of loans are only offered to undergraduate students who require financial assistance since they are entirely need-based. The government is responsible for paying the loans while the student is enrolled in the educational institute for at least half-time, during the grace period of six months and during the time of deferment.

Nevertheless, subsidized loans are limited to certain amounts that can be borrowed per year and for the number of academic years that the student is enrolled. Students are permitted to borrow up to $3,500 for the first year and increase to the maximum amount of $5,500 in the third and fourth years, with a total amount borrowed of no more than $23,000 in the four academic years.

Since July 1, 2013, first-time borrowers are not eligible to receive subsidized loans for more than 150 per cent of the length of their college degree program, which is known as the "maximum eligibility period."

Subsidized Loans

Unsubsidized Loans are not limited to undergraduates but are also available to graduates and professional students. These loans are not based on the financial needs of the applicant. The interest on an unsubsidized loan is added to the student's loan balance while they are enrolled in the educational institute, as well as during the grace period of six months and the time of deferment. Similar to subsidized loans, unsubsidized loans are limited in the amount the student can borrow per year, with up to $31,000 in total for dependent students, $57,500 for independent undergrad students, and $135,500 for graduate and professional students.

Perkins Loans

The Perkin's Loans are more selective than the Stafford Loans. The Perkins loans are a type of federal loan that is directly offered by the educational institute in which the student is studying. About eighteen hundred colleges are registered in the Perkins loan program. The purpose of the loan is to provide financial aid to students whose financial circumstances do not allow them to attend college. The loan program is strictly need-based, and students who face serious financial issues are eligible for the federal loan. Similar to the other federal student loans, students require to sign up for the FASFA (Free Application for Federal Student Aid) that determines the eligibility of the student for the loan.

Private Loans

Private student loans, also known as alternative education loans, serve as the second option for students whose financial circumstances do not permit them to attain a college education after they have received federal loans and aid. The cost of attending college is too high to be covered entirely by federal government loans. Private loans are mostly used by students who are attending for-profit educational systems.

Private loans are similar to personal loans as they are not need-based or allowed to students because the lender believes in securing their future. Private loans are offered based on the credit history of the student and their parents. Similarly, the interest rates are flexible and higher than the interest rates on federal loans. Private loans are not helpful to most students because they require repayment even while the student is enrolled in college. Moreover, the deferment and forbearance options in private loans are limited.

Student Loans: the Unsolved Problem

The question is, when did a simple form of loan for education become a major problem in the United States? Higher education is considered the doorway to opportunities and securing a bright future and a high standard of life. Hence, the number of education loan borrowers has increased to 44 million,

who've collectively borrowed more than $1.3 trillion from federal and private lenders. There are several factors that contributed to the dramatic increase in student loans in the United States of America (Best, n.p.). The primary reasons are the increasing cost of college, aggressive lending practices in the States, and the recession of 2008, which cut off family savings and earnings and the government's priorities, which do not accommodate higher education in the annual budgets (Thompson, 660-677).

Bankruptcy [11 U.S.C 523 (a) (8)]

The legal system of the United States of America states the amendment of Bankruptcy [11 U.S.C 523 (a) (8)], which includes several factors that encourage the high number of lending and borrowing of educational loans. Section 523(a) (8) consists of a presumption that qualified student loans will not be discharged. The presumption can be overcome by the debtor who shows "undue hardship" to the court; however, bankruptcy courts often prefer that debtors take benefit of the federal programs in order to delay payments rather than grant a discharge (Hennessy, 71-93). Nevertheless, when a debtor is unable to pay back, and there is no way to repay the loans in the given period, the legal system allows them a discharge. The discharge ability of loans has been restricted since the amendments of 2005, which requires evidence of "undue hardship" that proves that the debtor is in more than just a financial crisis to be unable to pay back their loans (Pashman, 605–621)

Since student loans are not discharged easily by the borrowers, private lenders give out loans very easily with the incentive of profits and interest without worrying about the payback. This has increased the lenders to an infinite level for higher education (Hennessy, 71-93). Before the amendment of the Bankruptcy Code in 2005, private student loans were dischargeable. However, since the dischargeability of these loans is rare, private lenders have granted $6.6 billion of student loans to students and parents seeking higher education. This was followed by a dramatic increase of $7.8 billion in the second year, and by 2008 it reached $10 billion (Thompson, 660-677).

This increase in lending can be blamed on the amendments to the Bankruptcy Code of 2005, which has given private lenders a free hand. Moreover, Congress meant to decrease the abuse of the discharge ability and bankruptcy codes, which would allow students to discharge their loans due to their irresponsibility and waste their grants on social activities. However, this has led to private lenders exploiting the market for higher education loans.

Tuition Increase

Higher education tuition rates have proliferated since the 1980s, with a growth rate of 1,000 per cent. The astonishing increase in educational bills, which has a direct impact on students and parents, has exceeded the rates of inflation for other products and services, such as gasoline and healthcare (Watson, 315). Meanwhile, hourly wages and compensations have remained flat for the past four decades, which shows that the majority of the population of the United States can't afford significant

and increasing college costs that result in the application for loans.

There are various factors that contribute to the rise in tuition fees, which include professors' salaries, campus extra-curricular activities, increased faculty charges and other maintenance charges, and one of the major reasons is the cutting of funds to these non-profit colleges that depend on student fees to run the institute (Best). The annual federal budget gives less priority to educational funding to public colleges and schools. This has resulted in colleges relying on tuition fees as the major source of revenue. Hence, tuition fees are rising at a high rate, which has contributed to the rise in student loans from both federal and private lenders.

Lenders Benefits

Another major contributor to the student loan crisis is the practice of aggressive lending by federal and private lenders. Federal loans are extremely easy to get but are not enough to pay for the entire cost of college (Watson, 315). Hence, students and parents shift to private lenders who follow the lending practice in similar patterns of personal loans. The loans have skyrocketed in a short period. Private lenders charge high interest rates to students who desperately need the loans to attain a college education, and the borrowers aren't able to discharge them easily.

Student Loan Forgiveness Programs

Public Service Loan Forgiveness

The Public Service Loan Forgiveness (PSLF) program allows forgiveness over the remaining balance of the loan the student owes to the federal government after making 120 qualified monthly payments while they are working full-time for a public service employer. The program is helpful for students in managing their debts while they are pursuing a career in the public service department.

Teacher Loan Forgiveness

The Teacher Loan Forgiveness is offered to students who pursue a teaching career and work in the sector for at least five academic years, teaching at elementary and secondary schools or any form of educational institute or agency. Teachers can get up to $17,500 of forgiveness on their federal loans.

Closed School Discharge

The Closed School Discharge allows a 100 per cent forgiveness of student loans if the student's school or educational institute shuts down or closes while the student is enrolled or within 90 days of their graduation, which affects their degree completion.

Total and Permanent Disability Discharge’

A Total and Permanent Disability Discharge eliminates all loans for students who are unable to pay back their federal loans due to some form of disability, which might include extreme poverty, physical disability, inability to achieve employment, etc. The U.S. Department of Education is responsible for deciding if the student deserves the discharge.

Propose Solution

Repeal or revise [11 U.S.C 523 (a) (8)]

The major contributor towards the increase in the student loan crisis is the 2005 amendments to the Bankruptcy Code in section 523(a) (8). Hence, Congress is required to reconsider the policy and improve the student loan crisis. There needs to be control over aggressive lending, which can be solved with the introduction of the dischargeability of private loans.

Evaluate Student Credibility, Field Of Study and Future Earnings before Offering Loan

The aggressive lending practices should be reduced, and loans should not be easily offered to all applicants. While it is essential for everyone to pursue higher education, student credibility, field of study, and future learning should be evaluated by both federal and private lenders before they offer their financial services. This will decrease the exploitation of loans, and students will be more focused on opening up opportunities and improving their profiles.

Effect on Federal Government and Private Lenders

The changes in the amendment of Section 523 (a) (8) will improve the matters and impact the Federal and private lenders and their practices of offering loans. Federal loans are available to everyone, but not enough to cover the entire cost of a college education. Hence, people apply for private lenders who grant loans easily due to the new policies which do not allow the discharging of loans without evidence.

Returning Result

The changes in the lender’s practices will impact the student loan crisis and the number of people who rely on loans from federal and private sources. This will lead people to save up more and focus on employment opportunities that will contribute to the growth of the economy. Moreover, the tuition

fees might decrease due to the decrease in the demand for private profit institutes. The student loan crisis will improve due to the effective application of the suggested changes.

Opposition

Congress Opposition to Repealing [11 U.S.C 523 (A) (8)]

One of the most common reasons that Congress opposes the repealing of Section 523 (a) (8) and not allowing discharge on all student loans is to prevent the abuse of the bankruptcy system. Legislators feared that students wasted their loans on social activities and took advantage of the discharge and being free of any debts, which proved to be unfair to the economy and the government that spent money on them. Moreover, post-graduates were blamed for discharging their loans while they still could pay and seek better employment options. However, such cases have proven to be reported in only 1 per cent of all filings. This shows that the claim is baseless.

Private Lenders Opposition to Evaluating Individual Borrowers

On the other hand, private lenders believe that evaluating individual borrowers can be a long process that might not always be accurate. There is no guarantee of how the student will perform or if they will be able to get a decent job that pays off the loans.

Conclusion

It is concluded that the student loan crisis is a major problem in the United States. The number of student loan borrowers has increased dramatically, which can be blamed on the rising costs of attending college and the increase in federal and private lending. The Bankruptcy Code of Section 523 (a) (8) proves to be a major contributor to the increase in lending. Revising the amendment will decrease the private sector lending practices and improve the student loan crisis. Federal and private lenders will require looking into every individual borrower to evaluate them for repaying the loans to attain college. This will put a restriction on the private lending practices.

The evidence discussed in the paper shows that increasing tuition and the costs of attaining college and higher education have made student loans a necessity for the majority of the American population. Furthermore, with the addition of limitless student loans granted by federal and private lenders, the market for higher education has faced a student loan crisis. The student loan forgiveness programs do not seem to be helpful in solving the issue that is caused by other factors such as the amendments of [11 U.S.C 523 (a) (8)] and private lending practices.

Works Cited

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