



## **STUDENT LOAN PROGRAM COMPLEXITY, UNCERTAINTY, AND ADMINISTRATIVE CHALLENGES**

**Statement of  
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**before the  
Committee on Banking, Housing, and Urban Affairs  
Subcommittee on Economic Policy  
United States Senate**

## **MOHELA's PERFORMANCE AS A STUDENT LOAN SERVICER**

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\* The views expressed are my own and should not be attributed to the Urban Institute, its trustees, or its funders.

## Introduction

Chair Warren, Ranking Member Kennedy, and members of the subcommittee, thank you for the opportunity to testify about servicing in the federal student loan program. The views expressed are my own and should not be attributed to the Urban Institute, its trustees, or its funders.

I am a nonresident senior fellow at the Urban Institute's Center on Education Data and Policy, where I conduct research and analysis on higher education policy. Much of my work at the Urban Institute and throughout my career has focused on improving the design and operation of the federal student loan program. I have published numerous analyses that examine the Income-Driven Repayment program and the Public Service Loan program to help policymakers understand the strengths and weaknesses of these benefits and how they can be improved. My testimony focuses on these two programs as they are at the center of many complaints about loan servicing. I also draw on research I conducted in 2019 at the American Enterprise Institute that examined the loan servicing system in relation to borrowers' complaints filed with the Consumer Financial Protection Bureau.<sup>1</sup>

As you are aware, nearly all student debt is issued through the federal government's student loan program. However, the government does not service the loans itself. Instead, it contracts with private companies ("servicers") to handle most interactions with borrowers.<sup>2</sup> Borrowers with federal student loans are unlikely to interact much with the US Department of Education (the Department) when repaying their loans. Loan servicing companies collect payments, staff call centers, maintain websites, send account statements, and inform borrowers of repayment options.

Despite loan servicing companies' important role play in administering the program, the Department and Congress are also responsible for how the federal student loan program operates. The Department plays a key role the program's administration by maintaining loan records, designing forms, and establishing contracts and guidelines for servicers, among many other functions. Congress also plays a role in how the program operates by defining terms and benefits for borrowers in statute.

Although today's hearing is primarily focused on loan servicing, the role of Congress and the Department are also integral to a well-functioning student loan program. The policy and administrative decisions they make contribute to the program's success. Still, they both can also work at cross purposes with that success. Moreover, it is often difficult to disentangle the interaction of all three entities when identifying the source of administrative problems in the loan program. To automatically blame loan servicing companies for concerns of borrowers not being treated fairly may obscure other factors contributing to the program's challenges.

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<sup>1</sup> Jason Delisle and Lexi West, *Student Loan Servicers: Scammers or Scapegoats? An Analysis of the Consumer Financial Protection Bureau Complaint Database*, (Washington, DC: American Enterprise Institute, October 2019), <https://www.aei.org/research-products/report/student-loan-servicers-scammers-or-scapegoats-an-analysis-of-the-consumer-financial-protection-bureau-complaint-database/>.

<sup>2</sup> "Who's My Student Loan Servicer." Office of Federal Student Aid, US Department of Education, <https://studentaid.gov/manage-loans/repayment/servicers>.

In my testimony, I will discuss some of the other factors I believe contribute to borrowers' frustration and dissatisfaction with how the loan program operates and the quality of customer service they receive. I will put forth some principles for reform and related policy solutions that could improve how the loan program operates.

## **Program Complexity Creates Servicing and Administrative Challenges**

The federal loan program has become extremely complex in its required terms and the benefits it provides borrowers. The more complicated the student loan program becomes, the more challenges loan servicers and the Department will have in administering it, and there will be more confusion and frustration for borrowers. To be sure, complexity often stems from providing benefits and options to borrowers. This is an inherent tradeoff that should be carefully balanced.

The most complicated part of the loan program is, by far, the Income-Driven Repayment (IDR) system. This program started as a single repayment option in the 1990s and now includes several options. Note that the IDR options are in addition to other repayment options such as consolidation, extended repayment, and graduated repayment.

The latest IDR option, Saving on a Valuable Education or SAVE, was added by the Biden administration in 2023<sup>3</sup>. Each of the IDR plans has different terms that are optimal for different groups of borrowers depending on their loan balances, interest rates, career paths, future income trajectories, and whether they borrowed for an undergraduate education or a graduate education. Although the creation of the SAVE plan simplifies this somewhat by generally providing the largest benefits, this is only true for undergraduate borrowers.<sup>4</sup>

For example, a graduate borrower might benefit most from enrolling in the Pay As You Earn (PAYE) plan, because it provides loan forgiveness after 20 years of payments. But they must consider that the SAVE plan offers lower monthly payments than PAYE and forgives unpaid interest each month. The tradeoff is that loan forgiveness occurs after 25 years of payments, which might negate SAVE's other benefits relative to PAYE. Further complicating matters, graduate borrowers who expect to use Public Service Loan Forgiveness program will always be better off in SAVE because of the lower monthly payments. Borrowers are likely to be frustrated and need support to understand these differences and choose a plan that is best for them. Loan servicers will be challenged to help them understand these differences as well. As a matter of policy, servicers do not counsel borrowers on which plan is best for their individual circumstances.

The IDR system provides important benefits to borrowers, but it is always going to add complexity to the loan program. The SAVE plan goes even further in that direction. It is arguably the most

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<sup>3</sup> Improving Income Driven Repayment for the William D. Ford Federal Direct Loan Program and the Federal Family Education Loan (FFEL) Program: Final Regulations, 88 Fed. Reg. 43820 (Jul. 10, 2023).

<sup>4</sup> Jason Delisle and Jason Cohn, *The SAVE Plan for Student Loan Repayment: Which Fields and Colleges Benefit Most?* (Washington, DC: Urban Institute, 2023), <https://www.urban.org/research/publication/save-plan-student-loan-repayment>.

complicated of the IDR options and will likely be prone to more confusion and servicing challenges. In other words, the system is set to become more complicated with the creation of SAVE.

For example, unlike other IDR plans, borrowers' payments in SAVE are calculated based on a prorated share of their debts for graduate versus undergraduate studies. Debts from undergraduate studies will be repaid at 5 percent of income (over an exemption) and debts for graduate school will be repaid at 10 percent of income. A borrower with an even split in their loan balances will, therefore, repay 7.5 percent of their income. Even though this policy serves a worthwhile purpose (it targets lower payments to undergraduate borrowers), it is complicated and requires the Department and servicers to process more information about borrowers' loans and make more calculations to arrive at a monthly payment, which increases the risk for errors and confusion.

Loan forgiveness benefits in SAVE are also more complicated than past plans. Prior IDR plans provided one or two loan forgiveness terms: 20 years of payments or, in some cases, 25 years for graduate borrowers. The SAVE plan sets loan forgiveness durations by the amount borrowed, but only for undergraduate borrowers. Under this approach, borrowers qualify for forgiveness after 10 years if they borrowed \$12,000 or less, and the term increases by 1 year for each additional \$1,000 borrowed, up to 20 years for undergraduates. Here again, the policy has a strong rationale—it links the loan forgiveness duration to amount borrowed—but it requires the Department and servicers to process more information about borrowers' loans and make more calculations to arrive at a forgiveness term, which increases the risk for errors and confusion among borrowers.

The Public Service Loan Forgiveness (PSLF) program is another major source of frustration and confusion among borrowers and a significant source of accusations of loan servicing failures. I do not want to excuse poor student loan servicing or management by the Department, but it is important to acknowledge that the PSLF program poses an enormous administrative challenge for both entities because of its design.<sup>5</sup> Some loans are ineligible (but can be converted to become eligible), and only payments made in specific plans and statuses count toward the 120 cumulative qualifying payments. Borrowers must make those payments while they are employed full-time in a qualifying job. They must submit paperwork certified by each employer they had during the repayment term, complete with accurate starting and ending dates that collectively span a decade or longer. Servicers and the Department must ensure borrowers have met all eligibility terms (loan type, repayment plan, repayment status, payment count, employment terms), and that they were met during the periods of qualifying employment before forgiving any loans. Given the extreme number of eligibility requirements and their complexity, it is not a coincidence that the program is the source of so many complaints. Note that both Congress and the Biden administration have taken steps to temporarily waive the original rules of PSLF to allow borrowers qualify more easily and address what some say were servicing and administrative failures.

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<sup>5</sup> "Public Service Loan Forgiveness," US Department of Education, Office of Federal Student Aid, accessed April 3, 2024, <https://studentaid.gov/manage-loans/forgiveness-cancellation/public-service#qualify>.

Evidence shows that borrower frustration over programs such as IDR and PSLF is related to the terms of the programs, not simply loan servicing failures. In a 2019 study for the American Enterprise Institute, my coauthor Lexi West and I analyzed a random sample of 1,200 out of 12,113 complaints borrowers had submitted to the Consumer Financial Protection Bureau's database and classified as complaints against federal student loan servicers.<sup>6</sup> We found that over a third of the complaints were about the terms and rules of the federal loan program, which servicers do not set.

## **Loan Program Instability and Uncertainty Create Administrative Challenges**

In addition to complexity, the federal student loan program has been subject to enormous uncertainty and instability in recent years, largely owing to the Biden administration's changes to its rules and regulations. Some of these changes were direct responses to pausing loan payments in the early days of the COVID-19 pandemic. Still others reflect a large-scale reform agenda the Biden administration has sought to execute outside the legislative process. These changes, which I will discuss below, will likely contribute to servicing and administrative challenges along with borrower frustration. All will require servicers and the Department to develop new processes, rules, guidance, forms, and communications on short timelines, creating instability and uncertainty in the loan program and setting the stage for errors and delays.

The most prominent of these efforts include the administration's student loan forgiveness program developed under the HEROES Act of 2003, which was struck down by the Supreme Court in 2023.<sup>7</sup> Even though the plan was immediately put on hold by court challenges in 2022 and ultimately invalidated, the Department and servicers had to plan and prepare for the possibility that this new program would take effect. The administration also sought to tie the end of the pandemic-era payment pause to the launch of the new loan forgiveness program, potentially creating a complicated administrative bottleneck in the program. Servicers and the Department would have to simultaneously manage two major new events (return to repayment and loan forgiveness). Congress ultimately intervened and mandated a restart to repayment in August of 2023.<sup>8</sup>

The administration is now developing a follow-on loan forgiveness program using a different statute that will again fall on the Department and servicers to implement.<sup>9</sup> The details of that plan have yet to be made available, but are expected any month now. The rulemaking process has suggested so far that the plan will be more complicated than the initial plan struck down by the

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<sup>6</sup> Jason Delisle and Lexi West, *Student Loan Servicers: Scammers or Scapegoats?* (2019); At the time we downloaded complaints for analysis, there were 12,113 complaints with narratives, which is the universe of complaints from which we drew our sample, and roughly 9,000 more complaints without narratives. In complaints without narratives, the borrower selected complaint topics from the CFPB's menus, but did not further explain the issue with a written description. Because we rely on the narratives for our analysis, we sampled only from the complaints with narratives.

<sup>7</sup> Biden, President of the United States et al., v. Nebraska et al., 22-506 (2023), [https://www.supremecourt.gov/opinions/22pdf/22-506\\_nmip.pdf](https://www.supremecourt.gov/opinions/22pdf/22-506_nmip.pdf).

<sup>8</sup> The Fiscal Responsibility Act of 2023, FRA; P.L. 118-5 (2023).

<sup>9</sup> "Negotiated Rulemaking for Higher Education 2023-2024," US Department of Education, accessed March 12, 2024, <https://www2.ed.gov/policy/highered/reg/heardulemaking/2023/index.html>.

Supreme Court, increasing servicing and administrative challenges.<sup>10</sup> The new plan may also be subject to court challenges that will create further uncertainty and instability in the loan program.

The SAVE plan is also a significant new policy the Biden administration has implemented through the regulatory process. As discussed earlier, this new program entails new work for servicers and the Department due in part to the complicated benefits it will provide. In addition, the SAVE plan will allow many borrowers to become immediately eligible for loan forgiveness because it will grandfather in borrowers' past loan payment histories.<sup>11</sup> Servicers and the Department must have the necessary administrative structure to execute those benefits.

In addition to the SAVE plan, the Biden administration has also made significant changes to the terms of the IDR and PSLF programs from 2021 through 2023, which it says are to assist borrowers in response to the pandemic. These policies retroactively made past payments in any loan repayment plan and specific time spent in deferment and forbearance eligible toward the loan forgiveness payment count required under IDR and PSLF.<sup>12</sup> These policies effectively re-wrote the rules for IDR and PSLF retroactively, as the statute states that only income-based payments and those under a 10-year plan count toward loan forgiveness (and payments made in the Direct Loan program for PSLF).

These retroactive changes required a significant administrative undertaking for both servicers and the Department as they had to update and restate payment counts for borrowers and identify and notify borrowers newly eligible for loan forgiveness in IDR. In the case of PSLF, borrowers had to apply for the benefits by October 31, 2022, which created the conditions for a surge of applications that the Department and servicers both had to process.

Amidst all of these changes, the Department and loan servicers must also manage the return to normal repayment for federal student loan borrowers that began in late 2023. That process requires massive new outreach efforts to borrowers and other servicing tasks. Although the resumption of normal payments following the pandemic payment pause was always going to be challenging, the Department and servicers are having to conduct it while simultaneously implementing the Biden administration's many changes to the loan program.

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<sup>10</sup> US Department of Education, "Issue Paper: Student Loan Debt Relief, Session 1: October 10 and 11, 2023," <https://www2.ed.gov/policy/highered/reg/hearulemaking/2023/session-1--issue-paper-student-loan-reliefom-committee.pdf>.

<sup>11</sup> US Department of Education, "Biden-Harris Administration to Shorten Path to Debt Cancellation for Some SAVE Borrowers," January 11, 2024, <https://www.ed.gov/news/press-releases/biden-harris-administration-shorten-path-debt-cancellation-some-save-borrowers>.

<sup>12</sup> US Department of Education, "Announces Actions to Fix Longstanding Failures in the Student Loan Programs," April 19, 2022, <https://www.ed.gov/news/press-releases/department-education-announces-actions-fix-longstanding-failures-student-loan-programs>; US Department of Education, "Fact Sheet: Public Service Loan Forgiveness (PSLF) Program Overhaul," October 6, 2021, <https://www.ed.gov/news/press-releases/fact-sheet-public-service-loan-forgiveness-pslf-program-overhaul>.

## Policies to Improve Servicing and Program Administration

Based on the issues outlined above, I highlight three areas where lawmakers could help promote a federal loan program that is less prone to borrower confusion, frustration, and administrative challenges.

### *Streamline and simplify loans, terms, and benefits*

A more streamlined loan program would likely be less prone to servicing and administrative challenges. The program can be simplified in many ways, but I list those I believe are directed most at improving loan servicing.

- Establish one income-driven repayment plan in statute and sunset all other income-driven repayment plans, as well as authority for the Secretary of Education to create new plans.
- Establish one default fixed-payment plan with a 20-year repayment term to replace all other nonincome-driven repayment plans, such as the standard, consolidation, extended, and graduated plans.
- Tie loan forgiveness benefits to total repayment time, not the number of payments or loan status during repayment; this will eliminate the need for complicated payment counts that have been a source of servicing problems and administrative complexity.<sup>13</sup>
- Eliminate forbearance and deferment benefits and use income-based repayment to allow borrowers to postpone payments.
- Eliminate interest and charge one large origination fee added to the initial loan balance; borrowers will know how much they owe immediately and their balance cannot grow, and there is no need to track and tally interest accrual.
- Use grants, direct payments, or tax benefits to subsidize public service employment instead of loan forgiveness benefits like Public Service Loan Forgiveness; income-driven repayment will allow these borrowers to make affordable loan payments.
- Reclaim congressional control over the major design, terms, and benefits in the loan program.

As outlined above, much of the recent uncertainty and instability in the loan program stems from the Department of Education seeking to establish new programs and policies within the federal loan program through its interpretation of the underlying statutes. Lawmakers could limit such activities and create a more stable loan program less prone to administrative friction by writing more specific language in the statute and not granting broad discretion to the Secretary of Education to set important program features. For example, the statute that the administration used to create the SAVE plan leaves all major decisions about the plan's terms, such as the income-based repayment formula and the loan forgiveness term, up to the Secretary.<sup>14</sup> The statute could instead specify the terms that

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<sup>13</sup> "Education Needs to Take Steps to Ensure Eligible Loans Receive Income-Driven Repayment Forgiveness," GAO-22-103720 (Washington, DC: GAO, 2022), <https://www.gao.gov/assets/d22103720.pdf>.

<sup>14</sup> 20 U.S.C. §1087e(d)(1)(D) & (e).

Congress believes are appropriate, thereby avoiding successive administrations inventing new plans with new terms whenever and however they see fit.

Of course, it may be necessary in some cases to defer to the Secretary to refine broad terms of a statute and incorporate the agency's administrative expertise. To prevent the Department from taking extreme liberty with this authority, Congress could consider including provisions like one in the College Cost Reduction Act, H.R. 2669 (118th Congress) that restricts the Secretary from promulgating regulations that will increase the subsidy cost of the federal student loan program or that is "economically significant."<sup>15</sup> To ensure this language has its intended effect, it should also be more specific about what constitutes an "economically significant" rule and what baseline will be used to judge whether it would increase the subsidy cost of the loan program.

### *Consider tax withholding as an alternative to loan collection and servicing*

This reform would require major changes to the terms and benefits of the loan program, but collecting loan payments through the federal income tax system has major advantages over the current repayment system. The main one: payments track income as it is earned, so there is no annual certification process that borrowers must complete. Another advantage is that it eliminates the need for loan servicing and servicers. It could also reduce delinquency and defaults.

Under this approach, borrowers would elect additional withholding on their Internal Revenue Service Form W-4 or estimated quarterly tax filings, and then those amounts would be reconciled with the correct amount owed annually through the income tax filing process. In other publications,<sup>16</sup> I have written about how such a system would work in detail.

Note that the income-based repayment formula and forgiveness terms of the loan program would need to be simplified for this system to function well. Policymakers would also need to develop alternatives to charging monthly interest, such as a one-time origination fee, because the tax collection system is an annual process that operates with a timing lag. These issues are detailed in my other publications.<sup>17</sup>

Thank you, Chair Warren, Ranking Member Kennedy, and members of the subcommittee. This concludes my testimony, and I look forward to answering any questions you may have.

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<sup>15</sup> College Cost Reduction Act, H.R. 6951, 118th Cong. (2024), <https://www.congress.gov/bill/118th-congress/house-bill/6951/cosponsors?s=1&r=39>.

<sup>16</sup> Jason Delisle, "How to Make Student Debt Equitable and Affordable," Manhattan Institute, July 23, 2019, <https://manhattan.institute/article/how-to-make-student-debt-affordable-and-equitable>.

<sup>17</sup> Jason Delisle, "How to Make Student Debt Equitable and Affordable," <https://manhattan.institute/article/how-to-make-student-debt-affordable-and-equitable>.