March 20, 2012

The Honorable Richard Durbin
United States Senate
Washington, DC 20510

Dear Senator Durbin:

The undersigned organizations are writing to express our opposition to S. 1102. This legislation would revise the federal bankruptcy law to make it easier for borrowers to discharge some educational loans.

S. 1102 is unnecessary because under current law, any borrower may discharge student loans if repayment would constitute an undue hardship. In enacting this into law, Congress intended to create a necessary and well-balanced safety valve for borrowers.
S. 1102 undermines this balance and is unfair to lenders who have relied on current law when extending credit to students with little or no credit history. It is also unfair to students because it will have the effect of restricting the availability of student loans and raising the cost of loans when they are available. For these and other reasons, S. 1102 should not be reported by the Committee or passed by the Senate.

There is no question that the ever increasing cost of education is making it harder for students to afford college. Between 1986 and 2011, inflation increased by 115% but college tuition increased by over 498% - outpacing inflation by more than 4 times the rate. Although federal Pell Grant assistance has increased significantly during this period, reliance on student loans—in particular federal student loans—has increased dramatically. The Department of Education projects that over 25 million Federal Direct Student Loans will be made this year totaling over $124 billion. In addition to these Direct Loans to students and parents, private sector lenders will make approximately $8 billion in loans—or about 6 percent of the overall total.

Rising education costs are the reason students and families continue to take out student loans over and above the direct lending programs provided by the Federal government. Yet, nothing in this bill attempts to address the root problem of rising education costs. Instead, it seeks to amend the Bankruptcy Code in a way that encourages defaults and that ensures that student loans will become even harder to obtain for deserving students. Moreover, the changes made by the bill do not apply to federal or student loans made by other governmental entities, which are the vast majority of student loans, and thus S. 1102 would not even help most borrowers.

For the small subset of loans that are covered, the bill changes the Bankruptcy Code in a way that will add uncertainty and additional risk to student lending. This will further restrict the availability of credit at a time when students are already finding it harder to find loans due to the credit crunch.

Current law allows student loans to be discharged in bankruptcy if "undue hardship" to the borrower or their dependents can be shown. This policy protects truly unfortunate borrowers while at the same time preserving the integrity of the bankruptcy system. This balanced federal policy is designed to ensure that a sufficient volume of loans are available to meet the financial needs of students across the country, and it has worked.

The proposed legislation would undermine this policy by allowing private sector student loans to be discharged without a showing of "undue hardship." Under the bill, federally funded loans and

loans made or guaranteed by governmental entities could still be discharged only upon a showing of undue hardship. In contrast, students taking out other private loans could run up thousands of dollars in private loans, carry them without having to pay interest while in school and then walk away without making a single payment even if the student in the future should be able to repay the loans in full. Moreover, it is retroactive and will apply to existing as well as future student loans. As a result, the bankruptcy system would be opened to abuse.

Enactment of S. 1102 will discourage lenders from making private student loans or force them to find some way to offset the increased risk. These risk management effects could mean raising interest rates and fees, or reducing the term of the loan (perhaps to 5 years) which would increase monthly payments, further increasing monthly debt service costs. None of these effects would benefit students.

We strongly urge the Committee to reject the S. 1102.

American Bankers Association
American Financial Services Association
Consumer Bankers Association
The Financial Services Roundtable

cc: Members of the Judiciary Committee