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WPRI Commentary

Moral Hazard in Wisconsin Universities

by Benjamin Artz

When chief executive officers use corporate funds to buy company jets for family vacations, we cry foul. When a firm's top executives drive up the stock price by secretly displacing debt from the books and then sell their options before it all comes crashing down, we are furious. These situations arise because managers are hired by firm owners to make decisions for them in their best interest. But managers tend to make decisions in their own best interest rather than the owners'. This sort of activity is known as moral hazard and is commonplace in corporate America; but no one really expected to uncover moral hazard in our very own public universities.

In a recent *Milwaukee Journal Sentinel* story, evidence of moral hazard was discovered at UW-Oshkosh, UW-Eau Claire, UW-La Crosse and UW-Green Bay. In Oshkosh, a student loan provider reportedly paid the university $10,000 to be listed as a preferred lender. This is a prime example of moral hazard if, in fact, this lender does not deserve to be a preferred lender and uses bribery to get onto the list. If this is the case, then the student borrowers are getting a raw deal, while the university and the sub-preferred lender are earning dishonest profits. Of course the university sees nothing wrong with this and may be right, but only if it assumes that that all lenders are created equal. Recent events, particularly in California, prove otherwise.

The lender supposedly offered the same deal to UW-Eau Claire, but was turned down by the chief financial aid officer. It turns out however, that the same financial aid officer owns almost $10,000 worth of stock in Citigroup, the parent company of Citibank, one of UW-Eau Claire's preferred lenders. Although pushing students to borrow from Citibank to raise Citigroup's profits and stock price is clearly moral hazard, it is naïve to assume this relatively small amount of activity would positively impact the stock price of the world's biggest financial conglomerate in a noticeable way. No matter how small though, the incentive is still there and should be taken away. The students' best interest should be looked after and in no way should the chief financial officer's personal income impede that objective.

UW-La Crosse and UW-Green Bay are also at fault for allowing a lender to give their respective financial aid officers all-expense-paid trips to the lender's loan processing center. This of course was done in the hope that the officers would push that particular lender's services rather than others, once again keeping the interest of the students out of the equation.

In all fairness, this type of bribery is done all the time across America. Maybe it is the universities' faults for being swayed by the lenders' kind offers. Better yet, maybe it is the lenders' faults for tempting universities to commit moral hazard and act in their best interest rather than the students'. This might not even be a big deal because the impact on the student may not even be perceivable. But why risk it? Maintaining student solvency is of utmost concern if our universities are to remain competitive with the rest of the world. With education prices rocketing upward, students are using financial aid more than ever. They need to be unafraid and confident in the borrowing process, especially when borrowing for education, possibly one's most important investment. The universities must resist the temptation of moral hazard to keep students borrowing funds so they can afford to attend college. If they cannot, I fear what might happen to the future of this country.