Reauthorizing the Higher Education Act: Strengthening Accountability to Protect Students and Taxpayers

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Chairman Alexander, Ranking Member Murray, and Members of the Committee, thank you for the opportunity to testify today.

Lending money to someone to attend an educational program with a demonstrated record of failure is doing the student no favor. Unpayable loan burdens not only cost taxpayers, but they haunt borrowers for years.

Poor student outcomes are caused by low-quality institutions and programs. At any given college, students from low- and high- income families have similar earnings and repayment outcomes. As a result, colleges level the playing field across students with different socioeconomic backgrounds—often lifting all boats, but sometimes sinking them. While disadvantaged students are concentrated in programs with poor outcomes, the research is clear about the direction of causality. The problem is the schools, not the students.

When it provides financial aid, the federal government has a responsibility – to students, to their families, and to taxpayers – to direct those resources to successful programs and to sanction or limit aid at poor-performing institutions.

Accountability policies are an appropriate response to protect to taxpayers' investments in students, increase the economic value of those investments, and to protect students from economic harm. Federal accountability policies were effective in the past. They remain familiar features of the educational policy landscape today. But they are no longer effective because of legislative and regulatory changes, because of expansions of federal financial aid that falls outside of current accountability systems, like graduate lending, and because of the unintended effects of borrower protections like forbearances or income-based repayment plans, which, by helping students avoid default, shielded their institutions from accountability.

Federal accountability policies should focus on student outcomes after they separate from an institution or a program. For instance, an institution's repayment rate–how much a cohort of borrowers has repaid several years after leaving school–would be a better indicator of student success, institutional quality, and the return on federal investments, than the measures we use now.

Early repayment outcomes are predictive of long-run loan success, easy to understand, and practical to measure with existing data. Because successful loan repayment results from the culmination of many incremental milestones—degree completion, finding a job, earning enough to pay down the loan—it summarizes in a simple way a complex series of achievements.

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The repayment rate could form the basis for the simple, familiar systems we have today, like the Cohort Default Rate rule or the Gainful Employment rule, in which institutions or programs are assessed relative to a threshold and lose eligibility if their performance falls below a minimum level. Or, the repayment rate could be used as the basis for risk-sharing systems in which institutions bear a portion of the financial consequences that students and taxpayers face from poor outcomes. In either case, the performance benchmarks and sanctions must be sufficient to drive real change, and the rules should apply broadly, including to graduate and parent borrowers, not just undergraduates. Outcome-based accountability measures could complement other federal rules, like the so-called 90/10 rule, and other elements of the accountability triad.

Before adopting a new regime, we need to address several unknowns and potential short comings. Loan-outcome-based systems don't necessarily provide accountability for institutions that receive federal funds but don't participate in loan programs. And Congress and the public should see the data underlying proposed repayment metrics, to understand how they vary across colleges or demographic groups, before drawing bright lines.

But those unknowns pale in importance to what we know is happening to students today. We are doing students no service by sending them to programs with demonstrated records of failure and encouraging them to take federal loans we know they cannot repay. The evidence shows that accountability measures that close poor-quality programs don't limit access to college, only access to poor-quality colleges: students move on to attend lower-cost, higher-value institutions. And there are thousands such institutions across the U.S. that regularly propel low-income, disadvantaged students up the income ladder. Redirecting federal dollars to those institutions would protect taxpayers and improve student outcomes.

The Consequences of Federal Aid and Existing Federal Accountability Rules

Federal loans and grants play a central role in financing valuable investments in education, especially for low- and middle-income families. In the labor market, workers with bachelor's degrees typically earn roughly $500,000 more over the course of their careers than individuals with high school diplomas. Beyond the traditional BA, many career-oriented programs offer degrees and certificates that boost their students' job prospects.[i]

College is therefore a key pathway to economic opportunity. Children from the bottom fifth of the income distribution have a 41 percent chance of reaching the top two quintiles if they earn a college degree, but only a 14 percent chance if they do not.[ii] Society as a whole benefits, as well, when more people go to college–from better health, lower crime rates, a more productive workforce, less dependence on public benefits, and a more informed electorate.

The educational workhorses responsible for most of the upward mobility of students are mid-tier, nonselective, and mostly public institutions, rather than elite or selective schools. [iii] Indeed, research identifies thousands of institutions across the U.S. that regularly propel low-income, disadvantaged students up the income ladder. Federal aid facilitates access to those institutions.

But not all institutions or programs lead to success. Too many students enroll in programs that they can't or don't finish, that don't lead to a job, or, that don't lead to a job that pays well enough to justify the cost or loan burden incurred. These problems are salient in the high rates of default among borrowers. Nearly 40 percent of borrowers who left school in 2004 may default on their student loans by 2023.[iv] When student loan borrowers default—as nearly 1.2 million direct loan borrowers did in 2016—the consequences are particularly severe because of interest and collection costs, credit reporting, tax refund offsets, wage garnishment, and ineligibility for future aid.[v]

A larger economic problem is that many students leave educational programs without having improved their earnings and employment prospects, wasting time, effort, and financial resources that could have been invested more productively. Many career-oriented programs leave students worse off because students' earnings and employment rates are lower than what they were prior to school entry, or their job prospects were little changed but they now owe new loan burdens.[vi] Looking across the country's 671 cosmetology programs, for instance, only six programs produced graduates whose earnings average more than $20,000 a year; at one typical school, the program costs $17,700, only 29 percent of students graduate, the average student leaves with $10,702 in debt, but earns an average of $12,487 after leaving school.[vii] Most online programs don't appear to increase the earnings of enrollees, despite enrolling millions of aid-dependent students over the past several years.[viii] And other programs that do improve outcomes sometimes still leave their students with debt burdens that exceed their ability to pay back the loans.[ix]

The weight of those failures falls most heavily on the most disadvantaged students. Pell Grant recipients comprise nearly 90 percent of students defaulting on undergraduate loans.[x] Black BA graduates default at five times the rate of white BA graduates.[xi] And low-income students disproportionately enroll at institutions whose graduates struggle in the labor market and are unable to repay their loans.[xii]

Taxpayers are on the hook for the costs of loans that will never be repaid and for grants squandered on educational opportunities that don't pay off. Aid recipients give up opportunities for higher income by enrolling in programs they can't finish or that don't lead to a good job, hurting them and weakening our economy. In some cases, the only winners are the schools.

Lending money to someone to attend a program with a demonstrated record of failure is doing the student no favor. Defaults not only cost the taxpayers (with little harm to the school), but they harm the borrower for years.

The Role and Responsibilities of Institutions and Institutional Accountability Policies

Poor student outcomes are caused by low-quality institutions and programs. While disadvantaged students are concentrated in programs with poor outcomes, the research is clear about the direction of causality.

The problem is the schools, not the students. At any given college, students from low- and high- income families have very similar earnings and repayment outcomes, even at institutions without selective admissions.[xiii] As a result, colleges level the playing field across students with different socioeconomic backgrounds—often lifting all boats, but sometimes sinking them.[xiv] The outcomes of students at different institutions reflect the quality of the school not just the backgrounds of their students.[xv] Systematic differences in outcomes across schools can be observed in default rates, loan repayment rates, post-college earnings, or callback rates of job applicants.[xvi]

The federal government has a responsibility – to students, to their families, and to taxpayers – to sanction or limit aid to poor-performing institutions and programs, and to direct resources to successful programs. To do otherwise is wasteful and unprincipled. Such accountability policies are an appropriate policy response to protect to taxpayers' investments in students, increase the return on human capital investments, and to protect students from economic harm.

Accountability policies were effective in the past. After a crisis in the student loan market in the 1980s, rigorous institutional accountability measures implemented in the early 1990s drove default rates down to the single digits.[xvii] The imposition of the Cohort Default Rate regulations exposed 1,200 institutions to sanctions, causing the official cohort default rate to plunge from 21.4 percent in 1989 to 10.4 percent in 1995 and 5.6 percent in 1999. Enrollment shifted to better-performing programs, students borrowed less, and default rates declined.[xviii] More recently, while no programs were sanctioned under the Gainful Employment rule, some institutions closed poor performing programs or changed academic guidelines in anticipation of their effect. Of 767 failing programs, 500 (65 percent) are now closed. About half of those are because the institution itself closed, but more than 200 were selectively closed or changed by their institutions.

Gaps and weaknesses in the current accountability system

But our current accountability system is no longer effective. After enacting effective measures in the early 1990s, Congress subsequently defanged key accountability provisions, like the 85/15 rule, which limited the share of revenues that a for-profit institution could receive from federal aid programs to 85 percent, and distance learning rules, which prohibited institutions from enrolling more than 50 percent of students in distance (or online) programs. The Gainful Employment rule and other regulations are being eliminated by the current administration. Congress expanded federal aid eligibility and the amount of aid to new markets, like exclusively online education, and through new or expanded aid programs like graduate and parent PLUS and new GI Bill benefits that fall outside of the oversight of existing accountability systems.[xix] Congress also enacted important borrower protections like forbearances, deferments, and income-based repayment plans, which helped struggling students avoid default, but which had the unfortunate unintended consequence of shielding the institutions they attended from accountability under the Cohort Default Rate rules, which bars schools with high default rates from federal aid eligibility. At many institutions, borrowers still default at high rates, but only after the three-year testing period has ended.[xx] As more borrowers enroll in income-based plans, default rates will fall—and that's a good thing. But it also means that the Cohort Default Rate rule is increasingly obsolete.

One consequence of the erosion in federal accountability and recent expansions in aid eligibility is the entry and expansion of low-quality, high-risk institutions, mostly in the for-profit sector, and disproportionately targeting older, non-traditional undergraduate students. A majority of the increase in default rates since 2000 resulted from federal policies that expanded aid to institutions that would not be eligible previously.[xxi] In contrast, student borrowers who attended so-called traditional programs—full-year, full-time undergraduate degree-seeking students at long-established brick-and-mortar public and private non-profit colleges—accumulate modest levels of debt, succeed in the job market, and rarely struggle with their loans.[xxii]

Today's problems also arise from gaps in oversight in other areas of the student loan program—particularly loans to graduate students and to parents of college students. Graduate-school and parent borrowers are exempt from outcome-based accountability rules, like the Cohort Default Rate rules. Such loans now represent more than 45 percent of all new student loan volume.[xxiii] Almost all borrowers with the cripplingly large loan balances highlighted in the media are either graduate student or parent borrowers.[xxiv] While default rates were historically low in these groups, loan performance is deteriorating.

Graduate students' average annual borrowing amount has almost doubled over the past 30 years, more than 20 percent of graduate borrowers entering repayment in 2014 owed more than $100,000, up from 8 percent in 2000. While borrowers with such large balances are rare, they account for a growing share of all student loans; the 5.5 percent of all borrowers who owe more than $100,000, owe a third of all student loan debt. While those borrowers rarely default, when they do financial consequences for students and taxpayers are outsized. Borrowers owing more than $50,000 accounted for almost 30 percent of all dollars in default, but only about 17 percent of student borrowers in 2014. Unlike associate or bachelor's degree students, graduate students pursuing masters, professional or doctoral degrees can take out federal loans for the entire cost of tuition, fees, books, and living expenses; the college itself decides those costs. Institutions have taken the bait: The University of Pennsylvania offers a master's in "Applied Positive Psychology"—a course with no prerequisites where applications are accepted from anyone with a minimum 3.0 grade point average—for $66,000; Columbia University offers a $64,595 online engineering degree, and tuition for USC's online master of social work degree is $107,484—the same as the on-campus version.[xxv] Few institutions could charge such large amounts or attract students to pay it without uncapped federal aid.

Enrollment trends suggest new risks in graduate lending. In 1990 1 percent of active graduate borrowers attended for-profit schools. By 2014, the for-profit share of graduate students had increased to 17 percent. Among graduate student borrowers who leave school owing more than $50,000, the for-profit share increased from 3 percent to 21 percent. Just as for undergraduate education, institutional quality matters, and the variation in graduate borrower outcomes across institutions is just as large as the variation in undergraduate outcomes, suggesting that not all graduate schools or programs lead to successful careers and successful loan repayment.[xxvi]

For parent borrowers, the story is similar. The average annual borrowing amount for parent borrowers has more than tripled over the last 25 years, from $5,200 per year in 1990 (adjusted for inflation) to $16,100 in 2014. Because of increasing borrowing amounts, more parents owe very large balances: 8.8 percent of parent borrowers entering repayment on their last loan in 2014 owed more $100,000, compared to just 0.4 percent in 2000. Parent default rates have increased and repayment rates have also slowed. Repayment rates have declined with increases in borrowing at for-profit institutions and at minority-serving institutions. Parent borrowers' repayment outcomes vary widely across institutions that students attend, and repayment rates at the worst-performing institutions are alarmingly slow.[xxvii] It's not surprising that some parent borrowers struggle; PLUS loans are offered without regard to parents' ability to pay and in uncapped amounts. According to data from the Federal Reserve Bank of New York, the cumulative 8- year default rate among the least credit worthy parent PLUS borrowers exceeds 30 percent. Among Pell-eligible students, 8 percent of their parents take out PLUS loans.[xxviii] For the hundreds of thousands of low-income borrowers in these circumstances, the result is near certain financial catastrophe. Because parent borrowers are generally ineligible for the borrower protections and income-based loan plans available to student borrowers, the consequences are severe, especially when borrowers default. In those cases, federal authorities are required to garnish wages and Social

Security benefits and confiscate tax refunds—a particular burden on low- and middle-income families. In 2017, the Treasury offset $2.8 billion, mostly in tax refunds, for delinquent student-loan debtors including both students and parents.

How to Improve Federal Accountability Policies

All these problems are solvable. Federal accountability policies that focus on student outcomes, encourage success, and sanction institutions and programs that systematically fail their students would improve students' labor-market and financial outcomes, reduce the burden on taxpayers, and retain access to high-quality programs for low-income students.

An institution's repayment rate–defined as the fraction of a cohort's initial loan balance that is repaid within a period of time after leaving school–would be a better indicator of student success, institutional quality, and the return on federal loan dollars than default-based measures we use now. The repayment rate is practical to measure because the Department of Educational already collects and retains most of the necessary data to measure loan repayment at the institution or program level. The repayment rate is difficult to for institutions to game or manipulate. The repayment rate bears a direct relationship to the federal costs of a loan. And the success students have repaying their loan is a good indicator of their own employment success and of the value of the program, especially when a rising share of students are enrolled in income-based repayment plans. Because successful loan repayment results from the culmination of incremental achievements from completing a valuable degree, finding a job, and earning enough to pay down the loan, it summarizes in a simple way a complex set of inputs.

Early-stage repayment outcomes are highly predictive of long-run loan outcomes. Nearly more than 90 percent of loans that are performing early on will still be performing at Year 15. Similarly, loans that are not being paid down after 3 or 5 years are unlikely to be performing at Year 15. And it's likely that the value of the measured repayment rate could be improved by accounting for in-school or military-deferments, or by incorporating anticipated forgiveness under teacher or public sector loan forgiveness programs.

Repayment rates (measured as the percent of a cohort's balance repaid) are closely related to other institutional outcomes of interest. The cohort repayment rate is strongly correlated with existing institutional metrics, including historical default rates, measures of repayment rate used in the College Scorecard, measures of loan burdens like debt-to-earnings ratios, and other outcomes like completion rates, post-college employment and earnings, and the earnings of low-income students. (Note, measures like whether a borrower is simply enrolled in or in good standing in an income-driven plan is not a good indicator of economic success.)

As more students enroll in income-based repayment plans, in which borrowers pay a fixed fraction of their discretionary earnings each month, repayment rates will more closely reflect fundamental economic outcomes like employment, earnings, and accumulated debt burdens. As a result, repayment rates will be a stronger indicator of post-college success and more closely related to debt-to-earnings ratios used as the basis for the Gainful Employment rules.

The repayment rate could form the basis of a range of practical accountability systems. First, it could be used as the basis for simple systems like the Cohort Default Rate rules or the Gainful Employment rules, in which institutions are assessed relative to a threshold or benchmark on a specified outcome metric (e.g., the default rate, the debt-to-earnings ratio, or the repayment rate), and lose eligibility if their performance falls below a minimum level of quality. Such a system could be applied at the institution level, like the Cohort Default Rate Rules, or at the program level with an institutional backstop, as in Gainful Employment. (Because some students separate before selecting a program and because institutions would have incentives to manipulate enrollment in failing programs, an institution-level repayment rate as a backstop is necessary.) The performance benchmark matters, and a lax standard would not encourage institutions to improve student outcomes. Consider the existing Cohort Default Rate system. Only 10 institutions were in danger of failing the standard in 2014; for most schools the rules were irrelevant.[xxix] To be effective, the repayment rate benchmark should be applied at a level that corresponds indicates real success and which requires institutions to quickly shutter failing programs. Students not in school or in the military should already be making progress repaying their loans three or five years after leaving school. If they're not, we should not send new students down the same path.

The repayment rate could also be used as the basis for a broader risk-sharing system, in which institutions bear a portion of the financial consequences that students (and taxpayers) face from poor outcomes. In broad terms, risk-sharing proposals identify socially valuable outcomes — as measured by loan repayment or post-college employment — and set targets for schools. If an institution's students fall below target, financial penalties proportional to the failure apply. Some plans would utilize carrots as well as sticks: revenues collected from failing schools would be used to finance bonuses for institutions that exceeded the target. For instance, the funds could be used to provide extra grant support to schools that have a superior record of outcomes for low-income students.[xxx] If institutions were financially liable to reimburse taxpayers for a sizable portion of their students' unpaid loan balances, institutions would have stronger incentives to maximize the long-term financial outcomes of their students.

Such accountability systems could be expanded to incorporate other outcome measures, particularly outcomes associated with financial aid recipients not taking federal loans, who might otherwise be excluded from accountability oversight. For instance, one could incorporate outcomes like post-enrollment labor market outcomes or cumulative financial costs. More elaborate systems could provide accountability over grant-funded students and more precisely target low-performing institutions. But they would be more complicated to administer and comply with, and some outcome measures, like educational outcomes or completion, would be harder to administer and easy to manipulate relative to market-based outcomes.

And outcome-based institutional accountability could continue to operate alongside other elements of our existing system, such as an improved 90/10 rule.

To be sure, before adopting a new regime, we first need to solve several unknowns and acknowledge potential short comings. Loan-outcome-based systems don't necessarily provide accountability for institutions that receive Title IV funds but don't participate in loan programs. We need more data and more transparency on student loan outcomes, to understand the properties of repayment metrics, how they vary across colleges, how they would be affected by adjustments for in school or military deferments or for rising enrollment in income-based plans, and how they would affect different demographic groups. Congress and the public should see those data before drawing bright lines. The analysis of a new accountability system should also take into account other features of the current system or other reforms undertaken in HEA reauthorization to forestall unintended consequences or costs. For instance, we should consider incorporating credit for public sector or teacher loan forgiveness programs, so that the loan relief policymakers intend to provide to students also benefit the programs or institutions that lead to public service. We should consider the impact of increased participation in income-based plans on loan outcomes. And it's important that the Congressional Budget Office get the scoring right: federal loan programs are not uniform monoliths but are comprised of thousands of different institutions and programs with widely varying costs or surpluses depending on the quality and cost of the program and the success borrowers repaying loans after enrollment. Reforms that eliminate poor outcomes should produce substantial budget savings.

Stronger Accountability is Needed Today

A reinvigorated accountability system would have many benefits. Federal oversight and accountability systems have a successful track record of improving student outcomes and reducing waste in federal aid programs.[xxxi]

Shifting aid eligibility away from the worst-performing institutions and programs to better ones will increase the average earnings and employment of students, and reduce the debt burden of students. For instance, the Department of Education estimated that the gainful employment rule would lead to lifetime earnings gains between $11 billion and $36 billion, as programs improve quality and students transfer to better performing programs.[xxxii]

As programs close or admissions criteria change, an important concern is that some students could lose access to certain programs. First, lending money to students to attend a program with a demonstrated record of failure does them no service. Second, the evidence suggests that students in sanctioned schools do not lose access to college. Rather, students respond to sanctions by moving on and attending other, better institutions. We need not ask students to choose between going to college and taking out a loan that they would be unable to repay. During the 1990s, when colleges lost access to federal student aid due to cohort default rate regulations, enrollment losses in sanctioned institutions were entirely offset by enrollment gains in local public institutions.[xxxiii]

Today, there are many institutions that offer admission to most or all candidates that lead to good earnings outcomes; many of these serve substantial numbers of low-income students. At "average" American colleges—the ones ranked in the middle (between the 40th and 60th percentiles) based on the post-enrollment earnings of their students in the College Scorecard, 26 percent of student borrowers come from low-income families. Compared to the lowest-ranked 10 percent of schools, low-income borrowers in this middle-opportunity range are 70 percent more likely to earn more than $25,000 a year, four times as likely to achieve earnings of $50,000 or more, likely to be making progress repaying their loans. And almost all institutions in this middle range admit more than 75 percent of applicants or are open enrollment.[xxxiv] Redirecting federal dollars to those institutions that offer economic mobility to their low-income students would improve student outcomes and protect taxpayers. A well-designed accountability system for federal aid would do just that.

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