

POLICY BRIEF

How to Reinvigorate Higher Education for the 21st Century

13 Recommendations for Reauthorizing the Higher Education Act (HEA)



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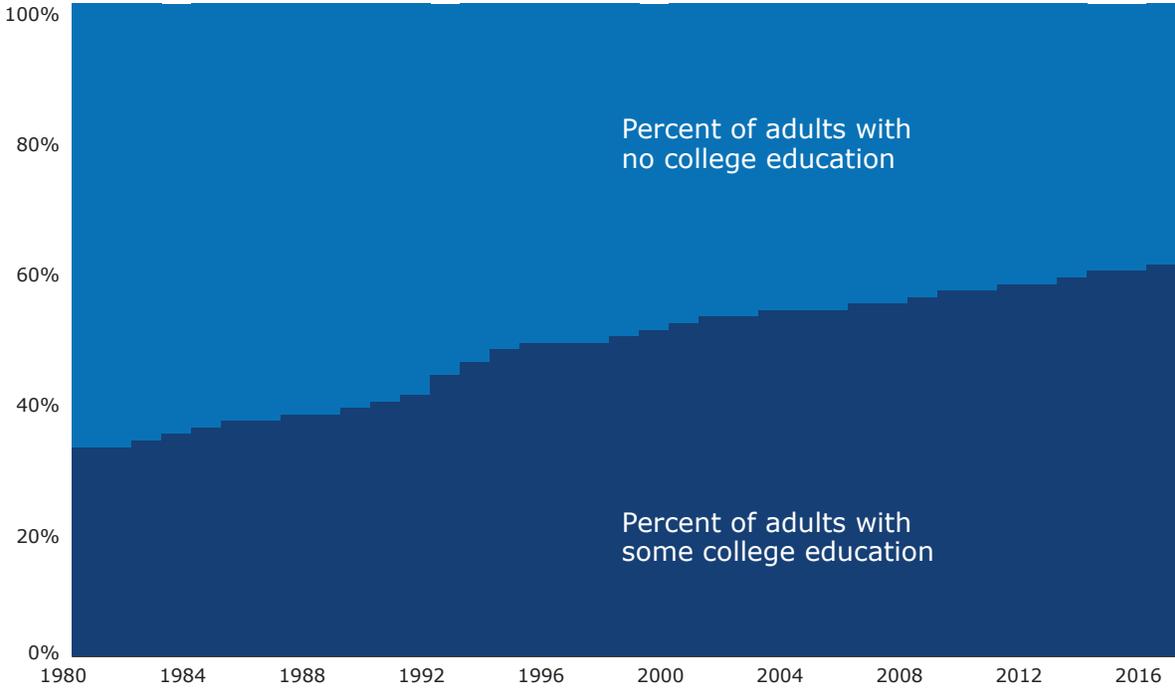
Today education and training beyond high school are more essential to our success as individuals and as a nation than ever before. Experts estimate that approximately two-thirds of American jobs will require some postsecondary education or training by 2020.¹ Of the jobs created since the last recession, almost all have gone to workers with at least some college education.²

Americans have responded to these new realities, and education beyond high school is now the norm in the US. As of 2016, 60 percent of adult

Americans have completed some coursework or training beyond high school.³ Nearly 70 percent of the high school class of 2016 continued directly to college the following fall.⁴

These trends make the federal Higher Education Act (HEA), which governs federal student aid programs and accreditation rules for colleges and universities, more important than ever. First passed in 1965, the HEA was most recently reauthorized in 2008 and has been due for reauthorization since 2013.

Chart 1
Percent of US adult population with at least some college, 1980-2016



Note: Adult population = Noninstitutionalized population age 25 and older.

Source: U.S. Census Bureau, Current Population Survey, Historical Time Series Tables, Table A-1. Years of School Completed by People 25 Years and Over, by Age and Sex: Selected Years 1940 to 2015; Educational Attainment in the United States: 2016, Table 1. Educational Attainment of the Population 18 Years and Over, by Age, Sex, Race, and Hispanic Origin: 2016 (<https://www.census.gov/data/tables/time-series/demo/educational-attainment/cps-historical-time-series.html>)

Recommendations for HEA Reauthorization:

Innovation:

1. Allow new models of higher learning to emerge
2. Fully authorize competency-based education and allow student-centered models of higher education
3. Federally fund research on improving access, affordability, and better student outcomes in higher education

Affordability:

4. Increase Pell grant funding
5. Create Lifetime Learning Accounts for every American that will serve as the “bank account” for all student aid, including grants, scholarships, and student loan lines of credit
6. Transfer management of federal student aid to the Department of Treasury from the Department of Education
7. Move the origination of student loans to the private sector. Provide federal guarantees for those student loans where such guarantees are necessary for affordability
8. Limit the amounts of some types of federally-guaranteed student debt that individuals can accrue
9. Allow borrowers to refinance their federal student loans
10. Pilot-test alternative funding models for higher learning, such as income-share agreements
11. Test increased risk-sharing by having postsecondary institutions pay a small percentage of the value of loans defaulted on by their former students

Accountability:

12. Improve the information available to students and families by having higher education institutions publish standardized cost and outcome measures
13. Enhance today’s accreditation system with a set of quality assurance entities, which would certify the providers of higher learning that are eligible to receive individuals’ payments from their Lifetime Learning Accounts

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Higher Education Today

Postsecondary education in the US functions as much more of a free market than the K12 sector does. Postsecondary education has never been a “free” public entitlement for individuals (although some now propose this). And while public colleges and universities such as land-grant institutions are key providers of postsecondary education, non-profit and increasingly for-profit colleges and universities have always played a much larger role than private schools do in the K12 sector.

Despite the federal government’s smaller direct role in providing postsecondary education, its impact on the sector is arguably greater than its impact on K12 education, thanks to its role in the student loan market. The value of outstanding loans in the federal student loan portfolio has now reached \$1.3 trillion.⁵

Nearly 7 out of 10 undergraduates take out student loans, and since 2010 the federal government has originated most of these loans. Other important

types of loans include Parent PLUS loans, taken out by parents on their children’s behalf, and student loans for graduate degrees.

Members of the undergraduate class of 2015 who borrowed to pay for their education (68 percent of them) owed \$30,100 on average by the time they left.⁶ Most will repay these loans. But those who failed to complete a degree or certificate (or who majored in fields that are unlikely to lead to well-paying jobs) are at risk of default. As of 2015, 10.6 percent of borrowers were in default and 5.4 percent were over 90 days delinquent.⁷ Even for those who can and do repay their loans in full, years of debt and interest payments loom over their early adult years—times when young Americans traditionally started families, bought houses, and launched businesses.

The college wage premium remains high: those with a BA can expect to earn wages 70 percent higher on average than those with a high school

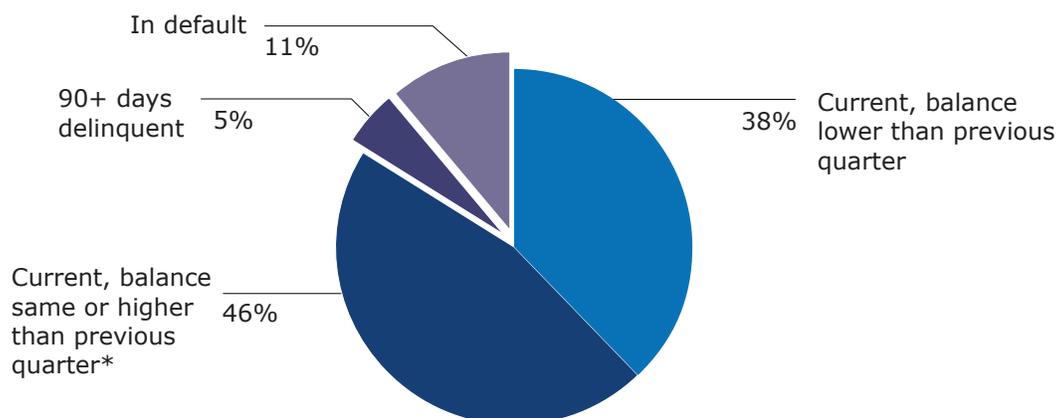
Chart 2
\$1.3 trillion federal student loan portfolio (in billions), 2017



Note: Consolidation Loans allow borrowers to combine multiple federal education loans into one loan, allowing them to make single monthly payments. Most federal student loans can be consolidated, with the exception of parent PLUS loans.

Source: U.S. Department of Education, Office of Federal Student Aid, Federal Student Loan Portfolio, “Federal Student Aid Portfolio by Loan Type” (<https://www.studentaid.ed.gov/sa/about/data-center/student/portfolio>)

Chart 3
Student loan borrowers by repayment status in 2015



Source: Federal Reserve Bank of New York, Center for Microeconomic Data, 2016 Student Loan Update, "Number of Borrowers by Repayment Status" (<https://www.newyorkfed.org/microeconomics/databank.html>)

*There are several reasons borrowers are classified as current on payments and not reducing loan balances. For example, federal student loan programs have generous deferment and forbearance provisions for certain borrowers to defer payments (re-enrolled in school, economic hardship, etc.) or to pay interest only (forbear payment of the principal). Also, the federal student loan balance could increase for a borrower with low income and high debt if he or she is enrolled in an income-driven repayment plan where the calculated monthly payment does not reduce principal balance nor cover interest owed. In those cases, the unpaid interest is added to the existing loan balance (i.e., negative amortization).

diploma. Yet this wage premium rose only slowly from 2000 and 2010 and was then unchanged from 2010 to 2015, suggesting that the returns to a college education are not growing as quickly as they once did.⁸ Finally, employers assert that job applicants at all levels, including recent college graduates, lack job-relevant skills.

Postsecondary education in the US needs to be restructured and reimagined to meet the needs of Americans and the American economy in the 21st century. Today Americans need education and training throughout their adult lives—education that they can afford, that fits into their lives (not just when they can devote full time to a degree that takes years), and that helps them obtain and retain work that supports them and their families. By the same token, the American economy and businesses need a system of higher learning that

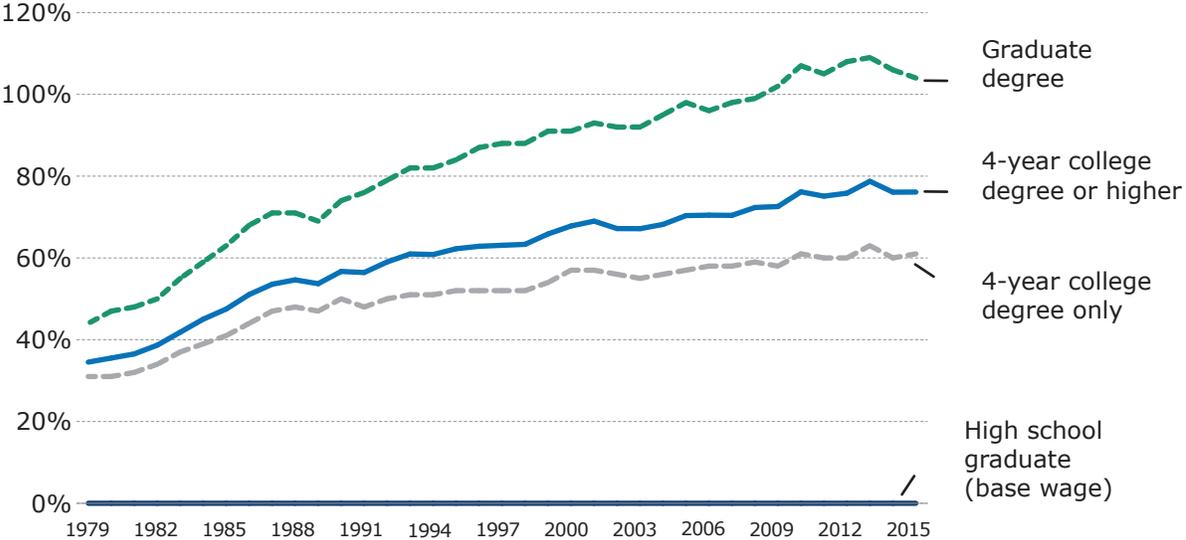
can prepare and reskill Americans throughout their lives to fill the rapidly changing jobs of the future.

Any reauthorization of the Higher Education Act (HEA) should aim at nothing less than reinvigorating the promise of higher education for the 21st century. Higher education should be recast as higher learning that helps Americans throughout their lifetimes to expand their opportunities and to lead sustaining and productive lives. In short, any HEA reauthorization must:

- Foster innovation in higher learning
- Improve affordability
- Increase accountability and transparency

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Chart 4
Estimated college wage premium (relative to high school graduates), 1979-2015



Note: Restricted to workers ages 25-64. Wages measured as hourly earnings.

Source: Valletta, Robert G. 2017. "Recent Flattening in the Higher Education Wage Premium: Polarization, Skill Downgrading, or Both?" Forthcoming in the National Bureau of Economic Research Studies in Income and Wealth conference volume, Education, Skills, and Technical Change: Implications for Future U.S. GDP Growth, edited by Charles Hulten and Valerie Ramey. Chicago: University of Chicago Press. Available as FRBSF Working Paper 2016-17 (<http://www.frbsf.org/economic-research/files/wp2016-17.pdf>). Graph reconstructed based on author's calculations using CPS MORG data.

I. Foster innovation in higher learning: more, better, and at lower cost

Higher learning in the 21st century needs to help *more* Americans from more diverse backgrounds and age groups develop *better* abilities and knowledge, and it needs to do so at *lower cost* per individual to make the system affordable both for individuals and for American society overall. Meeting these goals will require innovation and the emergence of new approaches to higher learning, including some we cannot even imagine today.

Recommendation 1: Ensure that any new (or existing) federal law or regulations allow new models for fostering higher learning (such as competency-based education) to emerge, while still providing accountability for taxpayer dollars.

The HEA should provide substantial latitude for innovation to occur. In cases where there are reasonable concerns that an innovation may be harmful to the interests of students or taxpayers, then the Secretary of Education should embark on time-limited demonstrations of the innovation that include evaluations of the quality

of the program. For example, the Secretary of Education might select particular postsecondary institutions or other organizations for voluntary participation in a pilot program of an innovative model. Congress should authorize the Secretary to waive particular regulatory requirements for these programs as appropriate, while also requiring the aforementioned outcome evaluation.

Recommendation 2: Fully authorize competency-based education and ensure that the definition of distance education accommodates student-centered models of higher education.

Competency-based models promote educational quality by tying credentials earned to actual knowledge acquired, rather than the time devoted to study. The current HEA looks at “seat time”—whether students complete a certain number of courses and credit hours within a defined academic period. The new HEA, while retaining traditional measures of credit hours, should also create alternative measures focused on evidence of student learning—what students actually know and can do.

Recommendation 3: Maintain and enhance federal funding for applied research on how to improve access, affordability, and student outcomes (including learning and employment) from higher learning.

Support for basic and applied research that the private sector (and states and localities) are unlikely or unable to fund has always been a key federal role. Findings from applied educational research can lead to greater innovation in how we educate more students of different ages and backgrounds to higher levels of skills, and how to do so more efficiently.

II. Improve affordability

Learning in the 21st century is a lifetime endeavor. So any solution for making higher learning affordable must also serve Americans across their lifetimes.

Education is a public good: living in a society and economy with a more highly skilled population benefits all of us indirectly in ways that go beyond the already substantial direct benefits that individuals obtain from higher education, such as increased earnings. In addition, education has been an important path to upward mobility in the US. For both these reasons, government has an appropriate role to play in making higher learning affordable, especially for lower-income Americans.

“Learning in the 21st century is a lifetime endeavor”

Currently the federal student aid system consists of grants for low-income students—known as Pell grants—and federally guaranteed student loans. Pell grants serve approximately a third of American college students and are capped at a maximum of \$5,920 for the 2017–18 academic year.⁹ This amount covers tuition and fees at most 2-year community colleges but only 60 percent of the average tuition and fees at a 4-year public college.¹⁰ The vast majority of Pell grants—83 percent in 2014–15—go to students in households earning less than \$40,000.¹¹

In terms of number of students served, federal student loans are the largest federal student aid program. Over two-thirds of undergraduate students take out student loans—either because they do not qualify for Pell grants or because their Pell grant does not cover their educational costs.¹²

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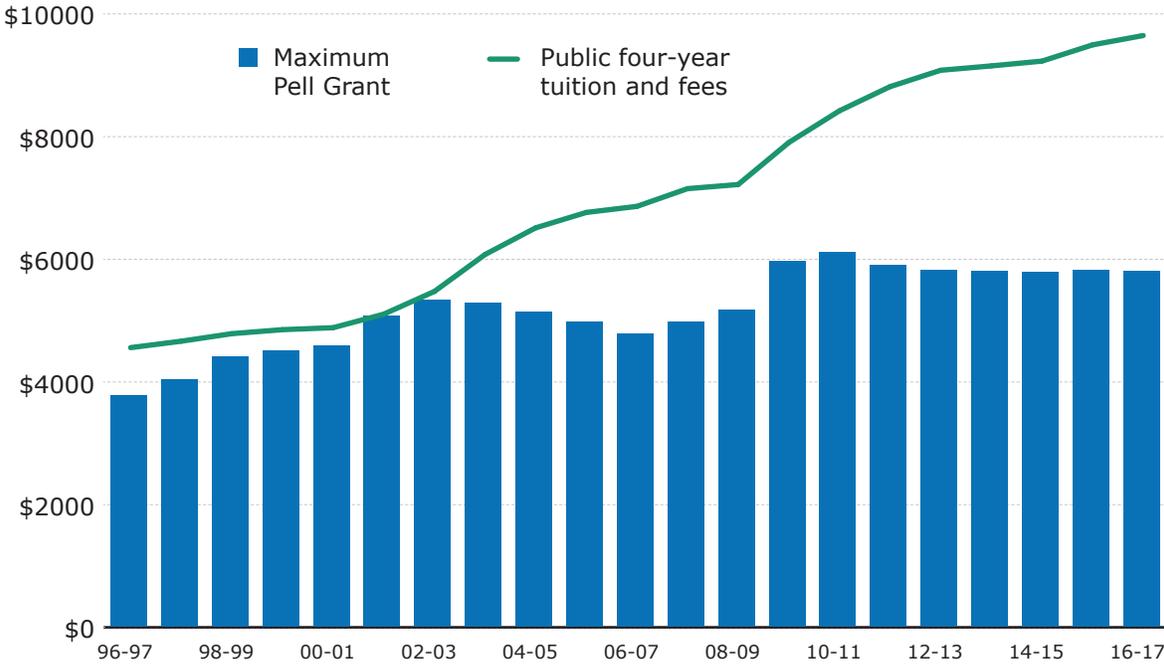
From a public policy perspective, student loans serve two purposes:

- They provide *liquidity* to households for a large expense that 1) is truly an investment that pays benefits throughout the person’s lifetime in the form of increased earnings, and 2) occurs relatively early in a person’s life (and so is hard to save for in advance). As one example, the net annual cost of approximately \$14,000 for tuition, room, and board at a public 4-year college¹³ represents almost a quarter of the median income of \$68,011 for US families with children in 2016.¹⁴ Most American households do not have sufficient income or savings when their children finish high school to self-finance this expense.

- When loans are subsidized (such as by the federal government waiving interest on the loans while the student is in school), they make postsecondary education more affordable by lowering the overall cost to the student. To the extent that supporting upward mobility for Americans is a goal of our federal student aid system, any reforms to student loans should keep in mind their effect on college *affordability*, especially for lower-income students.

For most large household purchases, such as cars, houses, or other consumer goods, private lenders generally do a good job of assessing the borrower’s creditworthiness and offering appropriate loan terms. So if simply providing households liquidity to pay for college was the only problem

Chart 5
Inflation-adjusted maximum Pell Grant and published tuition and fees at 4-year public colleges (2016 \$)



Source: The College Board, Trends in Higher Education, "Maximum Pell Grant and Published Prices at Four-Year Institutions over Time" (<https://trends.collegeboard.org/student-aid/figures-tables/maximum-pell-grant-and-published-prices-four-year-institutions-over-time>)

to be solved, one could argue that the private lending market could provide this service without government intervention, just as it does for many other consumer purchases.

A fully privatized student loan market would work for financially independent adult students with good credit and for younger students (e.g., under the age of 22) who come from families with good credit who will cosign for them.¹⁵ However, the private loan market is less likely to serve the needs of *lower-income* students (and their parents), who are more likely to lack the credit history necessary to access student loans in a purely private market, except at relatively high interest rates.

For this reason, if affordability is a goal, a government role in guaranteeing student loans will be required, at least for students who could not otherwise obtain loans at affordable rates. In fact, the federal government has guaranteed student loans, including those originating in the private market, since 1958 (for select students studying science, engineering, or education) and since 1965 more broadly.

“Our central recommendation for improving affordability is Lifetime Learning Accounts”

Given the necessary and appropriate government role as a guarantor for at least some student loans, a final criterion for any reform of the student loan system as part of HEA reauthorization should be *appropriately balancing risk* among lenders, borrowers, taxpayers, and providers of higher learning.¹⁶

The following recommendations aim to strike a balance among these goals of providing *liquidity*, enhancing *affordability* and upward mobility, and appropriately *balancing risk*.

Recommendation 4: Maintain the Pell Grant program and increase the annual maximum award. Fund these increases in Pell Grants through explicit statutory language that eliminates both in-school interest subsidies on federal student loans and federal income tax incentives for higher education expenses. Index Pell Grant awards to overall inflation (not inflation in college costs).

Pell grants are the part of the federal student aid system that most directly enhances affordability (and therefore upward mobility) for our lowest income students. Total savings from the proposed changes would increase Pell grant funding, thereby allowing a broader base of middle-income students to receive some funding and high-need students to receive larger grants. Indexing increases in the grant awards to overall inflation (rather than to inflation in college prices) supports affordability by reducing the incentive of institutions to raise prices to capture higher Pell grant funding.

Our central recommendation for improving affordability is Lifetime Learning Accounts, which will allow Americans to access the funding they need for higher learning throughout their lives.

Recommendation 5: Deliver student aid—grants, scholarships, and loans—through a new system of Lifetime Learning Accounts. Individuals could use the funds in their personal Lifetime Learning Account for postsecondary education or training from any provider of higher learning accredited by a quality assurance entity.¹⁷

Lifetime Learning Accounts would be tax-free accounts, similar to health savings accounts, which every American would have and which they could use for education, study, training, or coursework at any eligible provider of higher learning. For each individual, the account

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would serve as the depository of funds from a wide range of sources, including grants (e.g., Pell Grants, grants from other sources, Forever GI Bill Veterans Benefits, and military and employer tuition assistance) and loans, from both governmental and private sources. The funds would belong to the individual, could be used for education or training from any eligible provider, would grow at a tax-free rate, and could be rolled over to other family members, thereby encouraging cost-conscious use of the funds.

Individuals could use their Lifetime Learning Accounts for a wide range of higher learning, including coding boot camps, badges, credentials, and other relatively short education and training opportunities, as long as the provider was accredited by a quality assurance entity.

Lifetime Learning Accounts would simplify how Americans access student aid. For example, the government and employers could directly deposit whatever gifts, grants, and access to loans (as a line of credit) an individual is eligible for into his or her account. Government or private funds to support retraining or upskilling for workers who have been displaced from their jobs by technology or trade could be deposited in the accounts. Similarly, savings for future education and training could be deposited into the accounts where it would grow tax-free, like today's 529 accounts. Americans would be able to easily understand and access the combined total aid that is available to them. The accounts would be designed to deplete grant and gift aid first, before tapping available lines of student loan credit. For Americans enrolled in a degree or training program (e.g., a bachelor's degree), timely completion of the program could be incentivized by tying eligibility for additional grant and loan increments to completion of program milestones.

“Lifetime Learning Accounts would simplify how Americans access student aid”

Lifetime Learning Accounts would require a *student-level record system* that included each student's coursework, payments, and outcomes (e.g., grades, certificates, or degrees earned) at eligible institutions, since subsequent infusions of federal grant and student loan line-of-credit increases to an individual's account would be tied to both need and adequate progress towards a certificate, degree, or other appropriate end goal. Aggregated and de-identified information from this system regarding institutions attended, coursework, and outcomes (e.g., degrees or certificates attained) will provide another source of institutional transparency and accountability and can drive improvements in outcomes over time.

Recommendation 6: Transfer management of the federal student aid programs (including the proposed Lifetime Learning Accounts) from the Department of Education to the Department of Treasury.

The US Department of Education currently serves as both the originator and guarantor of most student loans, and some question whether an agency devoted to developing education policy and programs has the expertise to manage a loan portfolio larger than those of most banking institutions. The Treasury, with its expertise in managing US government debt and collecting revenue, could be better able to manage this vast loan portfolio. Specifically, moving student loans to Treasury would facilitate the following improvements:

- **Simplify student aid eligibility determination**
The already complex Free Application for Federal Student Aid (FAFSA) is further complicated by the difficulties of safely sharing sensitive tax data across agencies. Since the Internal Revenue Service (IRS) is part of the Department of Treasury, transferring responsibility for determining eligibility for student aid to Treasury should vastly improve

the process of linking family tax data to aid applications. Directly linking tax data to the aid application could also help simplify FAFSA by basing eligibility on multi-year tax data and family size.

- **Implement income-based repayment plans through employee withholding**

Income-based repayment plans are one method ensuring that student debt is manageable, but they are underused. The Treasury, which oversees payroll tax collections, could make it an option for employers to withhold (through payroll deductions) the appropriate percentage from borrower’s wages for employees participating in income-driven repayment plans.

- **Streamline and improve debt collection**

Standard repayment plans could be administered through a single platform, which would improve borrowers’ user experience. Through this single interface, multiple loan servicers would be awarded contracts based on performance to ensure better quality service for borrowers.

- **Improve how families plan and save for college**

One way to reduce the burden of student loans is to encourage families to begin saving for college early. Beginning when a student enters the seventh or eighth grade, the IRS could report estimated student aid eligibility to families that file 1040s, based on their three-year income averages. Along with the report, the agency could provide information to these families on saving for college through tax-deferred 529 Savings Plans or through the Lifetime Learning Accounts described above.

Recommendation 7: To the extent possible, move the *origination* of student loans to the private sector. Determine which types of loans for which types of borrowers require federal guarantees to make the market work. For those student loans that are federally guaranteed, the federal government will need to create adequate safeguards to protect taxpayers from excessive default rates and perverse incentives on the part of lenders.

Private-sector lenders have the expertise and incentives to determine credit risk and appropriate debt limits for different borrowers. To the extent that loans to low-income students (or to their families in the case of dependent students) require federal guarantees to “make” the market, the guarantees should be for less than 100 percent of the loan amount to ensure that lenders undertake reasonable collection efforts.¹⁸ These steps will more adequately balance risk among borrowers, lenders, and taxpayers, while ensuring access to liquidity for low-income households that would not otherwise qualify for student loans in the private market.

Recommendation 8: To limit students (and their parents) from accruing levels of *federally-guaranteed* student debt they may struggle to repay:

- Cap Parent PLUS loans¹⁹ at \$20,500 per year per dependent student, with an aggregate cap of \$138,500.
- Eliminate Graduate PLUS loans.²⁰
- Students (and the parents of undergraduates) who need or want to borrow more than these amounts should go to private lenders for non-federally guaranteed loans.
- Allow institutions to limit individual students’ federally guaranteed borrowing to amounts that are less than the federal limits (in ways that do not discriminate against protected groups).

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The improvements outlined in recommendation 8 (see box on previous page) are intended to protect both borrowers and taxpayers from instances in which borrowers take on large amounts of federally guaranteed debt that they may struggle to repay (and that taxpayers will be liable for in case of default).

Currently under the Parent PLUS program, any parent without an adverse credit history who has a dependent, undergraduate child can borrow up to a college's total "cost of attendance" (including direct and indirect costs) minus other financial aid. These loans are federally guaranteed. The student does not co-sign with the parent and is not liable for repayment. Because there are no annual or aggregate limits on the amount borrowed, it is possible for parents who have large families or whose children attend expensive undergraduate institutions to borrow well beyond their ability to repay. These loans are difficult (though not impossible) to discharge in bankruptcy. They are essentially a blank check for parents to pay any level of tuition and expenses that a college asks.

We would not end federally guaranteed Parent PLUS loans. We would simply limit them to parental borrowers who otherwise could not qualify for loans in the private market. And we would place annual and aggregate limits on them corresponding to current limits on unsubsidized undergraduate student loans. These limits (together with the amounts students can borrow on their own behalf) should be sufficient to pay for the cost of attending public colleges and universities. If parents felt they needed additional funds, we would leave it to private lenders to determine the appropriate limits and terms for such loans. These limits will protect parents and taxpayers from excessive borrowing that may lead to defaults. It will support affordability by limiting the availability of "blank checks" to pay whatever cost of attendance institutions choose to put forward.

As for graduate degrees beyond a four-year undergraduate degree, it is hard to argue that such degrees are necessary to find meaningful, important, and well-paying work in the US today. Many professions—medicine, law, business—either require or benefit from advanced graduate training. But in most cases, the earnings premium from obtaining an MD, JD, or MBA is more than sufficient to repay a student loan. Again, private lenders are well-equipped to judge the credit risk of particular borrowers and programs of study, and to extend commensurate loan terms and amounts.

We suggest that postsecondary institutions be allowed to limit individual students' borrowing to amounts less than the federal limits. These institutions often have close knowledge of the true cost of attendance and of their students' individual financial situations. Further, if they are to share in the risk of student loan defaults, as we advocate in Recommendation 11 below, then they should be given some means of preventing students from borrowing more than they are likely to be able to repay.

Recommendation 9: Permit borrowers to refinance their student loans should interest rates decline.

This would increase affordability by permitting individuals (both current students and former students who have left school) who took out loans at higher interest rates to receive the same low interest rates that benefit contemporary cohorts of students.

The complexity of federally guaranteed student loans

	Stafford Direct Loan (subsidized)*	Stafford Direct Loan (unsubsidized)*			Federal Perkins Loan	Parent PLUS Loan	Grad PLUS Loan	
Who is eligible?	Undergraduate students only	Undergraduate & graduate/professional school students			Undergraduate & graduate/professional school students	Parents of <i>dependent</i> undergraduates	Graduate/professional school students	
Other eligibility requirements	Students with "financial need"	None			<ul style="list-style-type: none"> Financial need Availability of funds at the school 	Parent must not have "adverse credit"	Student must not have "adverse credit"	
Who is the borrower?	The student	The student			The student	The parent	The student	
Who is the lender?	US Dept. of Education	US Dept. of Education			The school	US Dept. of Education	US Dept. of Education	
Origination Fee** (for loans disbursed on or after Oct.1, 2017)	1.066%	1.066%			0%	4.264%	4.264%	
Interest rate (for loans disbursed in 2017-18)	4.45%	Undergrad 4.45%	Grad/Prof 6%	5%		7%	7%	
Maximum amount (annually)	\$3,500-\$5,500 (depending on the student's year in school)	\$20,500 (less any subsidized loan amounts)			Undergrad \$5,500	Grad/Prof \$8,000	"Cost of Attendance" minus the student's other financial aid	"Cost of Attendance" minus the student's other financial aid
Maximum amount (lifetime)	\$23,000	Dependent \$31,000 (less any subsidized)	Independent \$57,500 (less any subsidized)	Grad/Prof \$138,500 [†]	Undergrad \$27,500	Grad/Prof \$60,000	None	None

* For subsidized loans, the federal government pays the interest while the student is in school. For unsubsidized loans, interest accrues while the student is in school (although repayment is deferred until the student leaves school).

** The origination fee is a mandatory fee charged for each federal loan a borrower receives (excluding Perkins). The fee is a percentage of the total loan amount borrowed (gross amount) and is deducted proportionately from each loan disbursement.

† This \$138,500 maximum includes the total of all federally guaranteed subsidized and unsubsidized loans for undergraduate and graduate study

Source: US Department of Education, Office of Federal Student Aid, "Types of Aid: Loans" (<https://studentaid.ed.gov/sa/types/loans#types>); "Subsidized and Unsubsidized Loans" (<https://studentaid.ed.gov/sa/types/loans/subsidized-unsubsidized>); "Federal Student Loan Programs" (<https://studentaid.ed.gov/sa/sites/default/files/federal-loan-programs.pdf>)

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Recommendation 10: Create a government-sponsored experimental/pilot program of “alternative funding models” for higher learning which would test the feasibility and effectiveness of such alternatives to benefit at least some students and learners. For example, income-share agreements (ISAs) could be one possible alternative model to be evaluated.

Income-share agreements are contracts under which students receive money to pay for education expenses in exchange for paying back a set percentage of their future earnings over a fixed period. ISAs typically include caps on the total dollar amount repaid and a maximum time limit on the payments. As an alternative to loans, ISAs help ensure that borrowers will not be saddled with unmanageable debt loads, as the amount they pay for their education varies with their salary.

Recommendation 11: Test having higher education institutions share in the risk of student loan defaults by charging them amounts based on the value of defaulted student loans for students attending their institution.

Colleges, universities, and other providers of postsecondary education and training arguably are best able to predict which students are likely to benefit from and succeed in their programs. Almost all operate with their students’ best interests in mind. However, the option that students have to take out relatively large federally-guaranteed student loans (at taxpayer expense if they default) creates a potential moral hazard. Unscrupulous institutions bear little cost if they encourage students who are unlikely to succeed to enroll using student loans (or to enroll in programs that are unlikely to lead to employment).²¹

Increasing institutions’ “skin in the game” if their students subsequently default on their student loans will incentivize colleges and universities to take a more proactive approach to ensuring better student outcomes in terms of completion and subsequent employment. Colleges and universities can proactively identify their enrolled students who are at risk of dropping out and provide them with guidance and supports to help them complete courses of study that are likely to allow them to repay their loans.

“For markets to work optimally, consumers...need a clear understanding of what they are buying, for what price, and how that compares to other alternatives”

Some argue that requiring higher education institutions to participate in student loan risk sharing would make them responsible for their students’ repayment behavior, which they cannot control. This might cause institutions to “cherry pick” and not admit students whom they assess to be repayment risks. That would disproportionately affect disadvantaged students and their chances for upward mobility.

On the other hand, if all providers of higher education face a small but non-trivial penalty based on the value of their students’ subsequent loan defaults, it may become a cost of doing business that helps align institutions’ incentives more closely with the outcomes that students, lenders, and taxpayers care about—namely, degree completion and employment. The cherry-picking problem can be limited by charging institutions that serve high proportions of disadvantaged or first-generation students somewhat lower rates.

III. Increase accountability and transparency

Where they exist, free markets provide one of the best mechanisms for accountability—that is, for ensuring that providers give consumers the outcomes that consumers want at the lowest price. In this sense, one of the great strengths of America’s system of higher education is that it has always been a diverse marketplace with a variety of public, non-profit, and for-profit providers.

However, for markets to work optimally, consumers—in this case, students and their families—need a clear understanding of what they are buying, for what price, and how that compares to other alternatives available to them. Transparency and relevant information make markets work better.

Recommendation 12: Improve access to consumer information for students and their families by recommending that higher education institutions publish standardized key performance indicators related to cost and student outcomes. Require that each institution participating in Title IV put a link on the homepage of its primary website that goes directly to a report of a standard set of key performance indicators.

When it comes to higher learning, it is hard for Americans to know what they are buying (in terms of learning and later employment outcomes) and how much it will cost them (both immediately and when their loan payments come due). Better information presented in standard formats that the average American can understand will help the market play its role. Measures should focus on 1) student outcomes, 2) cost to the student, and 3) loan outcomes.

Potential types of indicators could include:

Student Outcomes:

1. Graduation rate – four-year and six-year rates for all students (not just first-time, full-time students), disaggregated by age (25+), income (Pell-eligibility), ethnicity, and first-generation college status

2. Employment outcomes

- a. Average salary of a graduate (3 years after graduation).

This outcome is clearly among the most important to students and yet it varies more with field of study or major (e.g., engineering versus English) than by institution. Careful thought should be given to how best to balance standardization and ease of comparability. Ease of comparability argues for reporting salary outcomes for a relatively limited number of broad categories of study,²² rather than for the full range of majors and fields of study that are available.²³

- b. Percentage of graduates employed (180 days after graduation): full-time, part-time, in or out of their field. *If “gainful employment” is kept as a performance indicator, all institutions, not just for-profit institutions, should be required to report it.*

3. Student satisfaction rate. Institutions could annually survey all students and recent alums with two questions using a five-point Likert scale:

- a. How satisfied are you with your educational experience at _____ ?
- b. If you were making the decision today, how likely would you be to choose to attend _____ again?

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4. One-year retention rate (the percentage of students who continue past the first year at the school)

Cost of the Investment:

5. Average cost of a degree for the institution's most recent cohort of graduates
6. Average annual cost for full-time attendance, broken out by tuition, fees, living costs, and other (indirect) costs
7. Median time to degree completion

Loans:

8. Percentage of current students with student loan debt
9. Average student loan debt at time of graduation for the most recent cohort of graduates who borrowed money
10. Percentage of graduates (who graduated within the last five years) with loans in repayment and the percentage of those in default

Informed choice by students and their families who have access to a wide array of postsecondary options and providers in a robust marketplace is the strongest source of accountability. As with all markets, consumers voting with their feet (and their wallets) is the best way to ensure that providers of postsecondary education deliver outcomes that students and their families value.

However, the purchase of postsecondary education does differ from other consumer purchases in important ways. As mentioned above, it represents a very large investment in both time and money. Like healthcare, individuals making choices about postsecondary education, such as 18-year high school seniors and their families, may not have sufficient expertise to assess the quality of potential providers and options. As with healthcare, mistakes can be highly costly and

may not be evident for years. Finally, at least some higher education spending comes from taxpayers in the form of grants or federally guaranteed loans. For all these reasons, we believe there is still a role for some form of accreditation to ensure basic levels of quality and to protect consumers (and taxpayer dollars) from “bad actors.”

Accreditation has always played a central role in higher education. Today accreditation is especially important since students can only use federal student aid at accredited Title IV institutions. Moving, as we propose, to Lifetime Learning Accounts that can be used at a wider range of eligible providers, will make the definition of “eligible provider” only more significant.

Recommendation 13: Supplement today's accreditation system for higher learning with a set of quality assurance entities (QAEs), which would certify providers of higher learning that are eligible for individuals to spend their Lifetime Learning Accounts. Reform the current accreditation system so that accreditors would be assigned based on the type of school, institution, or provider of higher learning being reviewed, rather than the current geographically-based accreditation system.

The quality assurance entities (QAEs) will enhance the current accreditation system. They will serve a much broader range of providers of postsecondary education, training, retraining, and workforce development. In assuring provider quality, the new QAEs should focus on student outcomes rather than inputs to the extent possible. As with all regulations or accreditation systems, the key challenge will be simultaneously 1) allowing innovative providers to arise, and 2) preventing accreditation from serving as a barrier to entry, while 3) still protecting the public from truly “fly-by-night” providers.

Modifying the existing basis for assigning accreditation agencies (and QAEs) from one based on geography to one focused on school type will foster more meaningful specialization of the accreditors and QAEs. The current geographically-based system for determining who accredits different schools has had the potential to create differences in quality and standards across regions.

HEA reauthorization can restore confidence in accreditation's role in quality assurance by requiring accreditors to:

- Include employers on their commissions and on their visiting teams.
- Communicate with state regulators.
- Make public all final team reports, commission actions, and institutional responses.
- Harmonize accrediting actions and terms so they mean the same across regions and accrediting bodies.
- Evaluate an institution's key performance indicators for accuracy and against benchmarks (set by accreditors), while taking into account institutional mission, student characteristics, and other relevant factors. These key performance indicators should be included and addressed in the accreditor's evaluation of institutional and program quality.

Moving Education Forward in the 21st Century

We believe that this set of principles for HEA reauthorization will increase innovation, affordability, and transparency in higher education, while ensuring accountability for students and taxpayers. These recommendations will provide necessary access to grants and loans for Americans seeking postsecondary education and training, while appropriately balancing risk among borrowers, higher education institutions, and taxpayers. Taken together, we believe that these recommendations will help ensure that in the 21st century, Americans will once again lead the world in the quality and attainment of our higher learning.

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Endnotes

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- 5 This figure is as of 2017, Q2 and includes Direct, Perkins, and FFEL. Direct loans account for \$1 trillion of the balance. Office of Federal Student Aid, US Department of Education, Federal Student Loan Portfolio Summary. <https://studentaid.ed.gov/sa/about/data-center/student/portfolio> In contrast, the federal government provides only 9 percent of government funding for K12 education. National Center for Education Statistics, US Department of Education, The Conditional of Education: Public School Revenue, March 2017. https://nces.ed.gov/programs/coe/indicator_cma.asp Funding, provision, and regulation of K12 education is primarily handled by states and localities.
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- 7 2015 figures come from the Federal Reserve Bank of New York's "2016 Student Loan Data Update," and measure the percentage of borrowers in default or 90+ days delinquent. When measured in terms of the value of the underlying loans, the 90+ day delinquency rates are even higher. Thus in 2015 Q1, loans representing 11.1 percent of all outstanding loans were 90+ days delinquent. Federal Reserve Bank of New York, Center for Microeconomic Data, 2016 Student Loan Data Update. <https://www.newyorkfed.org/microeconomics/databank.html>. As of 2017 Q2, 11.2 percent of the aggregate student loan debt was 90+ days delinquent. Federal Reserve Bank of New York, Quarterly Report on Household Debt and Credit, August 2017. <https://www.newyorkfed.org/microeconomics/hhdc.html>
- 8 Anthony P. Carnevale, Ban Cheah, and Andrew R. Hanson, The Economic Value of College Majors, The Georgetown Center on Education and the Workforce, May 2015. <https://cew.georgetown.edu/cew-reports/valueofcollegemajors/> Roger G. Valletta, "The Recent Flattening in the Higher Education Wage Premium: Polarization, Skill Downgrading, or Both?" NBER Working Paper # 22935, December 2016. <http://www.nber.org/papers/w22935>
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- 10 Trends in Higher Education: Maximum Pell Grant and Published Prices at Four-Year Institutions over Time, The College Board, 2017. <https://trends.collegeboard.org/student-aid/figures-tables/maximum-pell-grant-and-published-prices-four-year-institutions-over-time>
- 11 The College Board, Trends in Student Aid 2016, Figure 20B: Distribution of Pell Grant Recipients by Dependency Status and Family Income, 2014-15, p. 28, 2016; CED calculations. https://trends.collegeboard.org/sites/default/files/2016-trends-student-aid_0.pdf
- 12 According to the National Center for Education Statistics (NCES), during the 2011-12 academic year, 68 percent of undergraduates age 18 to 24 in their fourth (senior) year or above had ever received a student loan. US Department of Education, National Center for Education Statistics, Digest of Education Statistics: 2016, Table 331.9. https://nces.ed.gov/programs/digest/d16/tables/dt16_331.95.asp
- 13 Trends in Higher Education: Average Net Price over Time for Full-Time Students, by Sector, The College Board, October 2016. <https://trends.collegeboard.org/college-pricing/figures-tables/average-net-price-over-time-full-time-students-sector>
- 14 US Census Bureau, American Community Survey, 2016 American Community Survey 1-Year Estimates, Table B19125: Median Family Income in the Past 12 Months (in 2016 Inflation-Adjusted Dollars) by Presence of Own Children Under 18 Years, using American FactFinder, https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=ACS_16_1YR_B19125&prodType=table
- 15 Few lenders would be willing to extend large loans directly to 18-year-olds, who typically lack significant assets, income, and work histories.
- 16 Risk tends to be appropriately balanced for loans without an outside guarantor, since both borrower and lender have an incentive to balance the benefits and risks they are receiving from the loan. However, in cases where a third party, such as the government, guarantees a loan, perverse incentives can arise for borrowers, lenders, and the suppliers of the item in question for the borrower to consume more of the item (and at higher prices) than would otherwise be the case since all three parties (borrowers, lenders, and suppliers) are at least partially protected if the loans go unpaid. So, for example, federal guarantees of home mortgages helped drive inflation in housing prices prior to the 2008 financial crisis. Some argue that a similar situation is occurring with regard to postsecondary education and student loans.
- 17 See Recommendation 13 for our proposals regarding quality assurance entities
- 18 When private student loans were guaranteed at 100 percent of their outstanding balance, it was more profitable for private lenders to simply turn them over to the federal government than to attempt to collect in the case of late payments.

- 19 Parent PLUS loans are federally guaranteed loans that allow any parent without an adverse credit history who has a dependent undergraduate student to borrow unlimited amounts up to the “cost of attendance” at an eligible school minus other financial aid awarded. There are no annual or lifetime limits on the amount borrowed.
- 20 Grad PLUS loans are federally guaranteed loans available to any US citizen without an adverse credit history to pay for his or her graduate school. There are no limits on the amount borrowed.
- 21 This is analogous to other situations where the existence of a third-party payer or guarantor leads to “over-consumption” of a good or service. Some argue that third-party payment and fee-for-service medicine leads to more testing and treatment in US healthcare, without better outcomes. Federal mortgage guarantees have been identified as one cause of Americans buying “more home” than they could afford before the 2008 financial crisis.
- 22 As one example, the Georgetown CEW reports undergraduate employment outcomes for seven broad categories of undergraduate majors. Carnevale, Cheah, and Hanson, The Economic Value of College Majors. <https://cew.georgetown.edu/cew-reports/valueofcollegemajors/>
- 23 We note that reporting these data may have a negative impact on the number of individuals going into occupations that our society needs and benefits from—such as early care and education positions, some health care support positions, and some teaching positions—that do not pay well.

POLICY BRIEF

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