



Automatic for the Borrower:

How Repayment Based on Income Can Reduce Loan Defaults and Manage Risk

March 2014

By



Table of Contents

Consortium Description	3
Acknowledgments	3
Glossary	3
Introduction and Executive Summary	4
Repayment Terms for Auto-IBR	7
The Principles of a Successful Auto-IBR Formula	7
Applying the Principles to Current IBR Terms	7
Examining Alternative Terms for Auto-IBR	9
Three Examples of Auto-IBR Plans	10
Simplifying Repayment through an Employer Withholding Scheme	14
The Current Repayment Process	14
Challenges of the Current IBR Repayment Process	15
Employer Withholding: A Possible Solution	16
How Would Employer Withholding Work?	17
Rethinking Institutional Accountability	20
Possible Unintended Consequences of Auto-IBR	20
Improving Consumer Information and Counseling	21
Loan Limits in Auto-IBR	21
Redesigning Federal Accountability Measures under an Auto-IBR System	23
The Stakes and Application of Accountability in Auto-IBR	32
Conclusion	35
Endnotes	36

Consortium Description

This paper is the culmination of work by a consortium of five student-aid advocacy and research organizations – HCM Strategists, the Institute for Higher Education Policy (IHEP), the National Association of Student Financial Aid Administrators (NASFAA), New America (NA), and Young Invincibles (YI) – with assistance from the Association of Public and Land-grant Universities (APLU), Committee for Economic Development (CED), the National Campus Leadership Council (NCLC), and the National College Access Network (NCAN). The proposals contained in this paper reflect research conducted by and discussions between members of the consortium. However, not all proposals included in this paper are supported by all groups in the consortium. Financial support for this research was provided by a grant from the Bill & Melinda Gates Foundation through the Reimagining Aid Design and Delivery (RADD) project.

Acknowledgments

We would like to thank the Bill and Melinda Gates Foundation for their generous support of this important research.

A number of higher education experts served as advisors to our consortium, and we would also like to thank them for this invaluable feedback on during the research and writing process. Thanks to: Sandy Baum; Diana Carew; Jacob Fraire; Kay Jacks; Kevin James; Daniel Madzellan; Scott E. Miller; Barry Simmons; and Jessica Thompson. Note that the final content of this paper is reflective of the authors, not the advisors.

Glossary

- **Auto-IBR** – refers to the consortium’s proposed single, auto-matic repayment plan based on income for all new federal student loan borrowers.
- **Current IBR** – refers to the Pay As You Earn Repayment Plan (PAYE), available to new borrowers as of October 1, 2007 who took out a loan after October 1, 2011) and the new Income-Based Repayment Plan (IBR), available to new borrowers for new loans as of July 1, 2014). Under both plans, a borrower’s monthly payment amount is 10 percent of his or her adjusted-gross income (AGI) above a specified exemption with forgiveness of the remaining balance after 20 years.
- **Repayment plans based on income** – refers to the current menu of federal loan repayment plans that are based on a borrower’s income, including Income-Based Repayment, Income-Contingent Repayment (ICR), and Pay As You Earn; also refers to the general concept of calculating borrowers’ monthly payments based on their income.

Introduction and Executive Summary

When borrowers default on a federal student loan, it can have catastrophic consequences. Their credit scores drop dramatically, severely curtailing their ability to afford a home or a car, and even limiting their ability to sign up for utilities. The cost of their loan rises as late fees pile up. Moreover, the federal government can garnish borrowers' wages, withhold taxes, and sue them in order to obtain the money owed. It can take years for borrowers' credit and finances to recover.

You might assume that relatively few individuals suffer through this experience, but you would be wrong. In 2011, 1 in 10 borrowers defaulted in the first two years after entering repayment¹ – that is nearly double what it was five years earlier.² Lifetime dollar default rates for the 2014 cohort are expected to range from 9.15 to 23.24 percent (depending on the type of Direct Loan).³ Delinquency rates have also jumped, a sign that more students are struggling to manage their loan payments than ever before.⁴

This is alarming not just for the financial hardship it visits on borrowers, but also because students borrowing a reasonable amount to obtain a quality postsecondary credential is often in the best economic interest of students and taxpayers. A person with a bachelor's degree earns about 80 percent more on average than someone with a high school diploma earns.⁵ At the same time, rising college costs have driven up the amount that students borrow and the number of students borrowing. Now, roughly two-thirds of graduating college seniors leave college with debt.⁶ From 2008 to 2012, debt at graduation among undergraduate borrowers who earn a degree increased an average of six percent each year.⁷ The path to economic security now runs through the doors of a postsecondary institution, but it has become a risky road for far too many students.

A variety of factors contribute to the repayment crisis, but the faulty design of the federal student loan program is a key culprit. Complexity is major problem. Federal loan borrowers experiencing a financial hardship can choose among several plans that lower their payments.⁸ However, with nine different repayment options, too few borrowers understand all of their options or know how to enroll. Therefore, enrollment in repayment plans based on income remains low – at about 11 percent.⁹ Instead, the majority of students end up on a standard repayment plan amortized over 10 years.

This leads to a second problem: timing. The standard repayment plan under which all borrowers automatically begin repayment works well for students who graduate, quickly find a well-paid job, and can begin repaying their debt. For borrowers whose careers do not take off as quickly or pay as well, the consequences can be disastrous. Even in the best economic periods, it often takes time for borrowers to earn the higher salaries commanded by their education level. However, their first federal student loan payment often comes due within six months of leaving school – the point in their career when they may be least able to afford it. The great recession has exacerbated the problem. In 2011, the unemployment rate for recent bachelor's degree graduates ages 20 to 29 was 13.5

percent.¹⁰ While the evidence is clear that, on average, a college degree pays off, the payoff may not be realized immediately upon graduation. Students who take out loans but do not complete their programs fare even worse.

Our consortium's members have come together around an idea that we believe will fix the student repayment process and reduce the risk of unaffordable loan payments and default. We call it "auto-IBR." The plan would:

- Automatically enroll all federal student loan borrowers in a repayment plan based on income (hereafter "auto-IBR") upon leaving school;
- Automatically deduct student loan payments through employer withholding; and
- Implement institutional accountability measures based on borrowers' ability to repay their debt.

We do not believe auto-IBR will solve the problem of college affordability or stem growing student debt levels. Nor do we fully agree on the details of the formula. However, we do believe that an auto-IBR system would have several advantages for students and taxpayers.

First, auto-IBR would act as a form of insurance against tough economic times for federal student loan borrowers, particularly those who experience unexpectedly low incomes at any point during repayment. Students would know going into school that, if they must borrow, their monthly loan payments will meet a minimum level of affordability, which could encourage college enrollment. Second, having a single repayment plan will dramatically simplify the federal student loan repayment system, making it easier for students to navigate. Third, automatic enrollment in a repayment plan based on income will make the system more fair by ensuring that all borrowers can benefit, not just those who are financially savvy and persistent enough to discover and navigate the program. Fourth, automatically enrolling borrowers in a repayment plan based on income where they repay their loans through employer withholding will virtually eliminate defaults.

Implementing an auto-IBR scheme would require significant administrative changes. Currently, borrowers repay through multiple private loan servicers. For repayment plans based on income, servicers set the amount of monthly repayments according to each borrower's most recently documented income (typically documented through prior-year tax returns). This prior-year methodology contradicts one of the primary benefits of auto-IBR – the safety net aspect of having payments adjust automatically, and in real-time, as income fluctuates. Instead, collecting student loan repayment through employer withholding not only makes auto-IBR more feasible, but may also provide advantages over the current repayment process. Automatically collecting payments through employer withholding, coupled with a system whereby the government automatically reconciles annual payments and amounts owed, would reduce the need for borrowers to document

changes to income each year and get rid of the “lag” in reflecting a borrower’s true income.

Apart from its benefits, auto-IBR risks unintended consequences without proper safeguards. Enrolling all borrowers in the current IBR scheme would reduce payments and provide forgiveness to many borrowers capable of paying back their loans in full. Moreover, a system where the federal government ensures a minimum level of affordable payments could alter the current incentives for setting tuition at institutions of higher education.

Further, although repayment plans based on income currently exist, few students take are aware of or access them. Auto-IBR would increase awareness and participation dramatically. Knowing that the federal government would ensure a minimum affordable payment and forgive outstanding debt could reduce incentives for institutions and states to hold down tuition or improve outcomes for graduates. In addition, students would face greater incentives to borrow more. Taxpayers could end up footing the bill for high tuition, low-quality programs, and excess borrowing.

We believe that a package of reforms including modification to the current repayment formula and institutional accountability metrics can avoid the unintended consequences of auto-IBR. Schools that consistently fail to graduate students capable of paying back their debt should not receive federal student aid. Any new accountability measures should be phased in to give institutions time to adjust their behavior and respond to the new auto-IBR system. We do not recommend specific cut-offs, though we explain why we would favor some measures over others.

We also propose the possibility of pairing minimum cutoffs with a risk-sharing mechanism to incorporate institutional responsibility among more than just the poorest performers. However, the consortium did not agree on whether student loan limits should play a role in that effort. Consortium members also vary in our ideal methods for formula changes, though we do agree that we would increase payments for higher-income borrowers compared to the current IBR terms, which would reduce the number of high-debt, high-income borrowers who reach forgiveness.

In this report, we discuss the details of our proposal in three major parts. First, we discuss the mechanics of the repayment formula and some possible options for adjusting it to accommodate an auto-IBR system. Second, we propose administrative changes required to implement employer withholding for student loans. Finally, we discuss options for ensuring institutional accountability under an auto-IBR system. As noted previously, the consortium did not fully agree on the details of implementation, particularly in the case of the formula and loan limits. This paper clearly describes our differing views where they occur.

Repayment Terms for Auto-IBR

This section outlines the principles the consortium believes an auto-IBR system should advance, measures the current IBR terms against these principles, and discusses the reasons for altering the current IBR formula when implementing auto-IBR. It also examines the options for formula changes, their merits, and their drawbacks. Whatever the chosen formula, we favor streamlining borrowers' ability to prepay through an "accelerated option." Importantly, though our members agree on the overall shortcomings of the current IBR formula for an auto-IBR system, individual members value the principles and policy alternatives differently.

The Principles of a Successful Auto-IBR Formula

An ideal auto-IBR repayment formula would align with several principles:

- 1. Safety Net:** The terms should provide a safety net to borrowers who unexpectedly find their loan balances temporarily or permanently unaffordable. The terms should not, however, create an expectation that debt can rise unchecked and be accommodated through loan forgiveness or extended loan terms. Auto-IBR should not aim to cover a portion of the cost of a postsecondary credential; that is the role grants should play in the federal aid system. Grant aid, such as the Pell Grant, more effectively targets federal tuition assistance and should remain the primary tool for offsetting tuition for low-income students.
- 2. Sustainability:** The auto-IBR terms should be fiscally sustainable.
- 3. Unintended Consequences:** The auto-IBR terms should minimize incentives students might have to engage in unnecessarily risky borrowing (i.e. moral hazard), and limit the incentives schools might have to charge higher prices than they otherwise would.
- 4. Fairness:** Auto-IBR should be designed to benefit borrowers who most need it, in a fair and equitable manner.
- 5. Simplicity:** The ideal terms should be simple and straightforward, so borrowers can understand them and employers can easily administer them through employer withholding.

Applying the Principles to Current IBR Terms

Under current IBR, borrowers pay 10 percent of their discretionary income each month (dependent on the family-size exemption), and monthly payments are capped at the 10-year repayment amount. In other words, if a borrower's monthly payment under current IBR would be more than the 10-year monthly repayment amount, the borrower pays the 10-year monthly repayment amount. Any remaining balances are forgiven after 20 years.

How would the current IBR terms measure up to the five principles just outlined?

- 1. Safety Net:** Generally, the current IBR terms provide a sufficient safety net to mitigate risks for borrowers. However, automatically enrolling all borrowers in current IBR could consistently deliver forgiveness to high-income, high-debt earners. Taxpayer dollars would be much better spent helping low-income students afford the up-front cost of higher education.
- 2. Sustainability:** Providing loan forgiveness to high- and upper-middle-income borrowers undermines fiscal sustainability in an automatic system. Under auto-IBR, many high-income, high-debt borrowers who are not enrolled in the current IBR system would be automatically enrolled in the new system, which would likely reduce their payments. The federal government could end up forgiving significant portions of the debt of otherwise successful borrowers, making it too costly compared with current policy.¹¹
- 3. Unintended Consequences:** Consortium members generally agreed that implementing auto-IBR under the current IBR terms could risk prompting schools to charge more, and thus students to borrow more. Although school administrators consider a variety of factors in setting tuition, they might have less concern about raising prices when they know students would be able to borrow to make up the difference and have any remaining debt forgiven after 20 years. Students, too, might have less incentive to weigh costs and value when choosing a school. These pricing and borrowing concerns exist primarily at the graduate level, as loan limits at the undergraduate level would mitigate these risks by limiting the amount of debt eligible for forgiveness.
- 4. Fairness:** Implementing auto-IBR with the current IBR terms would violate notions of fairness. High-income borrowers would receive significant and unnecessary benefits in lower payments and forgiven debt. The exemption for pre-tax, employer-provided benefits would worsen regressivity, as many high earners would qualify for lower monthly payments simply by taking advantage of these exclusions. Moreover, by providing the same loan forgiveness terms to all borrowers regardless of loan amount, the program provides the largest benefits to those who borrow the most. This feature can poorly target benefits and make the program inequitable.
- 5. Simplicity:** The current IBR terms are fairly simple, but may need to be simplified further to implement employer withholding. It is easy to administer one repayment percentage at 10 percent of discretionary income and one term for forgiving loans at 20 years. However, the current terms require borrowers to document their household size according to a hard-to-understand set of criteria (to calculate their income exemptions) and opt for a certain filing status for federal income taxes to fully utilize current IBR benefits. Accounting for a

borrower's family size would make employer withholding more complex and difficult.

Although our consortium identifies challenges to implementing auto-IBR under the current IBR terms, different individuals, organizations, or constituencies may weight these concerns differently. Nevertheless, our members agree that implementing auto-IBR with the current IBR formula would not work, because the policy would be poorly targeted, costly, and unfair. Auto-IBR, therefore, requires adjustments to the current terms in order to work effectively.

Examining Alternative Terms for Auto-IBR

The consortium weighed the relative merits of a variety of different auto-IBR terms. No single plan aligns perfectly with the consortium's principles for auto-IBR because many of the principles are in tension with one another. For example, effectively targeting the benefits to further fairness can make the system more complex. Furthermore, not all members of the consortium support any one set of alternative repayment terms, given members' differing perspectives and values.

Yet by providing valuable insight on the advantages and disadvantages of potential auto-IBR terms compared with current IBR, the consortium's work can help guide policymakers and stakeholders in designing an auto-IBR formula. The next section of this paper presents the trade-offs inherent in this policy, using three potential auto-IBR plans, each with a slightly different set of terms.

Importantly, consortium members did agree that auto-IBR terms should have some common features. All three of the plans discussed here share these characteristics, as they represent trade-offs we believe policymakers should make in designing any auto-IBR plan. The terms of any plan should include the following elements:

- **Loan Forgiveness:** The plan should include some form of loan forgiveness for those borrowers who repay for a given amount of time but do not fully repay what they owe (principal, interest, or both). Loan forgiveness provides a safety net to borrowers whose incomes are unexpectedly low for a long time.
- **Income Exemption:** All borrowers should be able to exempt some amount of their incomes from the payment calculation (consortium members have varying perspectives on how much). The exemption ensures that the lowest-income borrowers can make very low or no payments on their loans, or that they can exclude from loan payments income needed for basic "cost of living."
- **No Repayment Cap:** The plan should not include a cap on payments based on something other than income. Under current IBR terms, borrowers' payments stop increasing regardless of their incomes once their payments reach what they would have been under a 10-year repayment plan. That type of provision

allows high-income borrowers (or borrowers with small loan balances) to pay a smaller share of their incomes than lower-income borrowers, and therefore distributes benefits regressively, particularly as it interacts with the loan-forgiveness terms.

- **No Compounding Interest/Interest Capitalization:** Interest on the loans should accrue while borrowers repay, but it should not compound (or capitalize). That provision helps reduce the rate at which borrowers' loan balances grow when their income and/or payments are low – an important advantage over loans provided in the private market.
- **Targeted Benefits:** Compared with current IBR, the plan should reduce benefits to borrowers who have high incomes. However, each plan presented below does so to varying degrees. This reflects the consortium's range of views on the definition of a high-income borrower and on the relative weight of total interest paid over the life of a loan versus forgiveness of some of the principal.

Three Examples of Auto-IBR Plans

Note: All examples in this section are calculated using an IBR calculator developed by New America. The calculator is available from Alex Holt and Jason Delisle at New America upon request.

1. High-Exemption, High-Rate Plan

Income Exemption	•First \$25,000 of total income for all household sizes
Payment as Share of Income Above Exemption	•18%
Loan-Forgiveness Terms	•20 years of payments for all borrowers regardless of initial loan balance

This is the simplest of the three examples because it includes only one exemption, one rate, and one loan-forgiveness term, making it the easiest for borrowers to understand and for employers to administer under an employer-withholding scheme. It also maintains administrative simplicity by using a standard income exemption for all borrowers, regardless of family size. The plan may require some explanation to borrowers, as the 18 percent rate may cause borrowers to believe they are paying a far higher portion of their income than they actually are, given the exemption. Under this plan, employers would only need to know that an employee had federal student loans to determine the amount of withholding and would not need to collect any additional information from the employee – a plus for employers concerned with administrative simplicity.

The plan has the highest exemption, and therefore is the most generous for low-income

borrowers. This high exemption – 45 percent higher than current IBR for single borrowers – means this plan would assist a larger share of borrowers than the other two plans discussed here, through smaller or zero payments on student loans and substantial levels of forgiveness. The high exemption also means that more interest will accrue for borrowers with lower incomes, because they will be paying less per month than under current IBR or, in some cases, less than under the standard 10-year plan. These low payments and the accompanying interest accrual could significantly lengthen repayment periods.

This high exemption is more generous than current IBR for borrowers with a family size of two or less, but less generous for borrowers with a family size of more than two. While a fixed exemption makes the program simple, it risks providing unnecessarily large exemptions for single borrowers and not providing enough of an exemption for a borrower with multiple dependents.

For borrowers with income levels above the threshold, the relatively high repayment rate of 18 percent causes payments to rise more rapidly than the other two plans. As a result, borrowers could see notable increases in their monthly payments as their incomes rise. This high rate forces middle and high earners to pay back at a faster rate, which will help prevent high earners with high debt from receiving substantial amounts of loan forgiveness. However, it also results in monthly payments for some middle-income borrowers that are higher than what they would be under current IBR. Nevertheless, the payments are still low enough that when combined with the 20-year forgiveness term, it is the most likely of the three plans discussed to provide loan forgiveness to middle-income borrowers with large debts, and does so in the largest amounts.

2. Low-Exemption, Low-Rate Plan

Income Exemption	•First \$10,000 of total income for all household sizes
Payment as Share of Income Above Exemption	•10%
Loan-Forgiveness Terms	<ul style="list-style-type: none"> •20 years of payments for borrowers who begin repayment with ≤ \$50,000 in debt •30 years of payments for borrowers who begin repayment with > \$50,000 in debt

This plan is also administratively simple, with only one exemption and one repayment rate, although the two loan-forgiveness terms make it more difficult for a borrower to understand than the first plan. (The dual-forgiveness term would not add complexity for employers, as they would not administer the loan forgiveness provision – only ED would track that.) As with the first plan, employers would only need to know that an employee had federal student loans to determine the amount of withholding and would not need to collect any additional information from the employee.

This plan has the lowest payment rate for all borrowers and therefore avoids the more rapid increase in payments that arises in the other plans discussed here for borrowers whose incomes grow. However, this plan also has the lowest exemption (about 40 percent lower than current IBR for a single individual), making it the least generous to low-income borrowers, who would have to begin paying back as soon as they earned above \$10,000. Payments would therefore be significantly higher compared with current IBR for the lowest-income borrowers, especially those with larger household sizes. The lower exemption and resulting higher monthly payments mean that less interest would accrue, making it less likely that borrowers would significantly extend their term – as compared with the two other plans or current IBR.

The extended loan-forgiveness term and the higher monthly payments for middle-income borrowers mean this plan is unlikely to provide loan forgiveness to middle-income borrowers with moderate to high levels of debt. However, the low repayment rate of 10 percent means that, even after 30 years, those with extremely high debt would be more likely to receive loan forgiveness than if they were enrolled in example 3 (discussed below). Nevertheless, the extended loan-forgiveness term means that borrowers with more than \$50,000 in student loan debt would pay based on their incomes for 10 more years than with current IBR before becoming eligible for forgiveness, even if they had perpetually low incomes.

The single repayment rate of 10 percent, combined with a low exemption, makes the system less progressive than the other plans, as high-income borrowers would pay less under this plan than under example 1 with its 18 percent rate and high exemption, or example 3, which includes a higher rate for higher-income borrowers. However, all borrowers earning more than \$10,000 would pay more per month under this plan than under current IBR because the exemption is lower than current IBR.

A combination of factors – a low repayment rate, a payment cap, and a 20-year forgiveness term – in the current IBR system allow high- and middle-income borrowers with high-debt levels to receive loan forgiveness. All three example formulas discussed here propose removing the payment cap, but this formula addresses the issue of loan forgiveness for high-income borrowers further by implementing an extended loan forgiveness term for high-debt borrowers.

3. Multiple-Rate, Multiple-Exemption Plan

Income Exemption	<ul style="list-style-type: none"> •\$12,000 of total income for individual •\$18,000 for households of two or larger
Payment as Share of Income Above Exemption	<ul style="list-style-type: none"> •10% for borrowers earning \leq \$40,000 •12.5% for borrowers earning $>$ \$40,000 but \leq \$70,000 •15% for borrowers earning $>$ \$70,000
Loan-Forgiveness Terms	<ul style="list-style-type: none"> •20 years of payments for borrowers who begin repayment with \leq \$60,000 in debt •25 years of payments for borrowers who begin repayment with $>$ \$60,000 in debt

On all measures except simplicity, this is effectively a middle-ground plan relative to current IBR and the other plans discussed here. The two exemptions, three repayment rates based on income, and two loan-forgiveness terms add substantial complexity. The two different exemption levels are simpler than current IBR, which uses a sliding scale that accounts for each additional household member, but more complex than examples 1 and 2. This binary exemption complicates the calculation for employers and requires the borrower to submit additional information on family size to the employer.

The multiple rates in this plan would require employers to withhold at one of three rates, introducing complication into employer calculations. Borrowers with more than one job could also face challenges withholding the correct monthly amount. For example, if a borrower holds two part-time jobs that earn \$22,000 per year, then each employer might decide to hold 10 percent of her income. However, the borrowers' total income would require her to withhold at a rate of 12.5 percent. She would need to predict this in advance and inform each employer to withhold a greater amount. As a result, borrowers under this plan would face a greater chance of underpaying (or overpaying) their loans in a year, triggering large lump-sum payments (or account credits) at the end of the year.

The low exemption for single borrowers makes it less generous for low-income borrowers than the current IBR. This likely makes the program less costly and slows interest accrual, as low- and moderate-income borrowers just above the exemption would consistently make small payments. Households with more than one person would have a higher \$18,000 exemption, approximately equivalent to the exemption for single individuals under current IBR. A \$10,000/\$18,000 binary exemption would be less generous, but more fiscally sustainable than implementing auto-IBR with the current IBR formula. However, this exemption structure is more generous than example 2.

The progressive, stepped-rate increases attempt to further target the generosity of

the program towards low- to middle-income borrowers, while expecting higher-income borrowers to pay at a higher rate and decreasing the likelihood that these higher-income borrowers receive loan forgiveness. Of the three plans proposed, middle- and high-income borrowers are least likely to receive loan forgiveness if they were enrolled in example 3. However, these progressive rates also create moderate cliff effects for borrowers.

Finally, under this plan, borrowers with graduate school debt would repay for five more years before becoming eligible for loan forgiveness, compared with current IBR and example 1. The \$60,000 threshold is set near the independent undergraduate loan limits (higher than example 2) to ensure that undergraduate borrowers do not face a longer repayment, unless they also have graduate debt.

Simplifying Repayment through an Employer Withholding Scheme

The current repayment process is rife with administrative burdens on borrowers and loan servicers. Because making the current IBR option automatic would magnify the administrative challenges, we considered ways to simplify and streamline the enrollment and repayment process. Ultimately, we believe that an employer withholding system should be the default repayment mechanism for borrowers.

The Current Repayment Process

Currently, if a borrower does not affirmatively select a repayment plan, the loan servicer will assign the borrower to the standard, 10-year repayment plan and will bill the borrower accordingly with no required upfront action by the borrower. To enroll in a repayment plan based on income, the borrower must affirmatively indicate that preference to the loan servicer and then take further steps to document income so the servicer can determine the monthly payment. The current process sets a borrower's repayment obligation based on their most recently documented income. The borrower provides a hard copy of their federal income tax return, or shares tax return information electronically with the loan servicer by participating in the electronic IBR request process.¹²

Borrowers who did not file a federal income tax return for the two most recently completed tax years or whose current income is not accurately reflected by the Adjusted Gross Income (AGI) from their most recently filed federal income tax return (most likely due to a loss of or change in employment) instead complete an Alternative Documentation of Income (ADOI) form. In such cases, the repayment obligation is based on current taxable income if that amount is high enough to require filing of a US tax return. Every 12 months, borrowers must submit updated income documentation via a federal tax return or the ADOI form with supporting documentation. The loan servicer then recalculates the repayment obligation for the next 12-month period based on the updated income documentation. Borrowers who fail to submit updated income documentation are forced to make the

monthly payment they would have had if they had entered the standard repayment plan at the time when they entered IBR. In addition, accrued interest will capitalize. If such borrowers subsequently provide updated income documentation, they can resume making income-based monthly payments. Borrowers who experience a significant change in income between the annual “renewal” dates and wish to have the IBR repayment obligation recalculated must complete the ADOI form and submit supporting documentation to their loan servicer. The loan servicer then recalculates the repayment obligation based on current income rather than using the tax return, which reflects prior-year income.

Challenges of the Current IBR Repayment Process

The current process generally calculates the repayment obligation based on prior-year income. While prior-year income is easy to document, it does not always correspond to the borrower’s current ability to pay. Although the ADOI process is intended to address this time lag, it has two major problems—it’s burdensome, and its design almost guarantees that only those borrowers whose current income is lower than their prior-year income will use it.

The use of prior-year income and the ADOI process can also lead to similarly-situated borrowers having very different monthly repayment amounts according to the dates they apply for IBR and whether they file a tax return. Consider this example of how calculating IBR payments using prior-year income and the ADOI process may have very different effects on three classmates.

Similar Borrowers, Different Repayment Amounts		
ALI	BO	CY
<p>Ali had never been employed or filed a federal tax return. She graduated in June and began her job with an annual salary of \$35,000 in September. In December, after prompting by her loan servicer, she selected IBR as her repayment plan. Because she had never filed a federal tax return, she used the ADOI process and submitted a current pay stub. Ali received a monthly payment amount of \$119 based on her \$35,000 salary. <i>Her monthly payment amount is \$119.</i></p>	<p>Bo’s circumstances were identical to Ali’s, except that he applied for IBR in August, before beginning his post-graduation, full-time job in September making \$35,000 annually. He answered “No” to the question “Do you have taxable income?” on the ADOI, and received a monthly repayment amount of \$0 based on his zero income. <i>His monthly payment amount is \$0.</i></p>	<p>Cy worked sporadically while in school, filing income tax returns every year with AGIs ranging from \$2,000-\$3,000. He graduated in June and began a full-time job in September with an annual salary of \$35,000, just like Bo and Ali. When he chose IBR, he submitted a copy of his prior-year tax return and received a monthly repayment of \$0 based on his prior-year AGI. <i>His monthly payment amount is \$0.</i></p>

All three borrowers had the same taxable income when they entered the first year of repayment, yet they had very different monthly repayments. When these same students enter the second year of repayment, the servicer will calculate their monthly payment using the prior-year tax return, which will reflect eight months of little to no income during enrollment and four months of full-time work. While all three borrowers will face the same minimum payment at this point, due to the prior-year basis used in the current IBR system, the second year of loan repayment still will not accurately reflect the borrowers' current ability to pay.

Borrowers who have a change or loss of employment must initiate contact with their loan servicer to adjust their monthly repayment through the ADOI process. This process is time-consuming, administratively difficult, and an added burden during an already stressful time for the borrower. Once the servicer adjusts the monthly repayment amount, if an unemployed borrower subsequently finds employment, the monthly repayment amount remains unchanged for the year unless the borrower initiates that process.

In short, the current process is complicated, somewhat arbitrary, and does not reflect a borrower's current ability to pay. Despite increased public awareness of the availability of repayment plans based on income, current IBR enrollment rates remain below 10 percent¹³ and default rates continue to rise.¹⁴ Clearly something needs to change.

Employer Withholding: A Possible Solution

If designed well, employer withholding as an auto-IBR repayment mechanism would advance the principles of fairness and simplicity. By drastically reducing the burden of enrolling in a repayment plan based on income and making monthly payments, the process would prevent many borrowers from falling into delinquency and default. For these reasons, all groups in our consortium support pursuing employer withholding with the ability to opt out, although we did not discuss at length the detailed mechanics of such a process.

Under this approach, employers would withhold loan payments from paychecks in the same manner that they withhold Social Security (FICA), making the process automatic, simple, and based on current income rather than prior-year income. Self-employed borrowers would make quarterly estimated payments in the same way that they currently pay federal income and payroll taxes. By using the existing mechanisms for withholding a certain percentage of a borrower's income, payments would be regular, automatic, and most importantly, would self-adjust as current earnings begin, end, or fluctuate. This withholding mechanism eliminates the need for the ADOI, the annual income documentation processes, and the associated paperwork burden. Self-adjusting payments also could eliminate the need for some of the currently available student loan deferments and forbearances, which are based largely on circumstances connected with lower earnings (e.g., economic hardship, inability to find employment, postsecondary enrollment). It would treat all borrowers equitably by basing payments on current income

for everybody. This basic process has been proposed by Rep. Thomas Petri (R-WI) in the Earnings Contingent Education Loans (ExCEL) Act of 2013.¹⁵

How Would Employer Withholding Work?

The first step in an employer withholding process would be to notify the employer that the employee is a federal student loan borrower. Under no circumstances would an employer need to know the amount of the borrower's total loan debt, since loan debt does not dictate the amount of IBR payments. This should alleviate some of the privacy concerns about employer withholding.

Either the employee or an outside party would be responsible for notifying the employer of the borrower's status. For example, the employee could self-identify as a federal student loan borrower by checking a box on the W-4 form while selecting other withholding and deduction options. However, while employee self-identification has the benefit of using the existing W-4 process, it may be error-prone. For example, employees may not self-identify, misunderstand the check-off box, or not realize that the check-off box applies to them.

A less error-prone alternative would be for ED to notify the employer of their employee's borrower status. To obtain this information, ED would run a database match between its National Student Loan Data System (NSLDS) and the National Directory of New Hires (NDNH), which includes all employees except the self-employed.

Once the borrower has been identified, the employer would withhold a certain percentage of the borrower's income based on the auto-IBR formula authorized in law. A relatively simple auto-IBR formula that requires withholding a certain percentage of earnings, without considering household size, would be less complicated and would reduce burden on employers. However, some complexity within the IBR formula would not necessarily preclude employer withholding. The precedent of employers collecting information about dependents for health care and dependent care purposes and offering individualized options for retirement and transportation benefits shows that such nuances are possible within an employer-based system. The system for withholding Social Security (FICA) is a model to aim for; the system for withholding child support, which is individualized, often manual, and frequently requires communications back and forth with an outside agency, is not.

Employers could direct the withheld funds to one of two entities: the Internal Revenue Service (IRS) or the Department of Education (ED). If the IRS is the recipient, the employer would simply include the withheld loan repayment funds with other federal withholding, reporting these amounts for each employee through its annual W-2 process. Because this method uses an existing process, it is less burdensome for employers. However, due to existing IRS policies, the reconciliation of payments would only occur on an annual basis.

Sending funds to ED on a quarterly basis could be timelier, but would require employers

to send funds to a new entity. ED, through its servicers, could apply payments to borrower accounts as if they were made in equal monthly increments throughout the year, so that interest accrues equally for all borrowers even if employers submit funds on different schedules.

Regardless of the flow of funds, a reconciliation process at the end of the year would compare a borrower's yearly loan obligation with the yearly withholding, plus any other payments. The Internal Revenue Code would need to be modified to permit the IRS to share the tax return information with ED without an individual authorization from the borrower. ED would complete the reconciliation and send an annual statement to the borrower. If reconciliation shows the borrower has overpaid, we propose automatically applying the overage toward the loan balance unless the borrower requests a refund of the overage. If the borrower has underpaid, the borrower would be required to pay the difference that exceeds a certain *de minimis* amount within a set period or arrange a longer-term payment plan with the loan servicer. Borrowers who participated in employer withholding, or who opted out of withholding but made payments determined with some type of income verification, should not be penalized if they have underpaid but paid the difference within the set period or arranged a payment plan." We recommend that the "late" payments be credited to the borrower's account as if they were made on time, so the borrower is not assessed additional accrued interest.

Ideally, the amount withheld would closely align with the borrower's yearly repayment obligation, so any overpayments or underpayments would be small. In order to achieve this precision, the auto-IBR formula should be driven largely by wage income, since that is the basis for the withholding. An auto-IBR formula based on AGI rather than total income or wage income would create greater discrepancies between the amounts withheld by employers and the total yearly repayment obligation. Our consortium is in general agreement that an auto-IBR formula based on income rather than AGI is preferable.

Opting Out of Employer Withholding

Consortium members raised the concern that subjecting loan repayments to employer withholding elevates student loan payments to a higher priority in the list of a borrower's monthly financial obligations. That is, required employer withholding removes a borrower's discretion not to make a loan payment on time if more urgent financial obligations must be met instead. To address this, we recommend that any employer withholding system allow a borrower to stop withholding in emergency situation by notifying ED. ED would either not notify the employer to initiate withholding, or would notify the employer to stop withholding.

Borrowers may also have privacy concerns with their employers knowing their borrowing status and may prefer to repay their debt through a traditional servicer. As a result, we recommend that ED notify borrowers of the opt-out provision well in advance of its correspondence with employers, giving borrowers sufficient time to opt out. Once

that deadline has passed, a borrower can still choose to opt out of withholding but the employer may have already been notified of the employee's borrowing status. The servicer would then determine a repayment amount based on current-year income, which could be collected via the National Directory of New Hires, depending on timing, or another intermediate verification option. The borrower would then make monthly payments using the payment processes available today.

Self-Employment

In an employer withholding system, self-employed workers would need to take more initiative to make their auto-IBR payments than workers who are not self-employed. They would make their loan payments on a quarterly basis, at the same time that they pay their estimated federal income and payroll taxes. Since the quarterly payment process is already in place, the added burden to the self-employed should be minimal. Alternatively, self-employed borrowers could opt out of quarterly loan payments and instead make monthly payments like those who opt out of employer withholding.

Married Borrowers

Current IBR rules use combined income to establish the repayment obligation of married borrowers who file joint tax returns. For single borrowers and married borrowers who file separate tax returns, repayment obligation is based on only the borrower's income. These current rules would present challenges in an employer withholding system: the employer might know an employee's marital status, but may not know if a married employee files a joint return or if the married employee's spouse is a borrower. If the employee is not a borrower, the employer would not be instructed by ED to initiate withholding, even if the employee's spouse is a borrower. Unless the repayment rules were changed to treat loan debt of married borrowers who file jointly as an individual, rather than joint, obligation, a married employee who files a joint tax return and whose spouse is a borrower would need to self-identify to the employer.

Loan Prepayment

The consortium agreed that borrowers should always have the ability to make higher payments than those required under auto-IBR, even in an income withholding system. The embedded option discussed earlier in this paper would provide information to help borrowers make that decision. A borrower who chooses to withhold more than the minimum auto-IBR payment would simply notify her employer of the additional amount to be withheld. ED could develop a standard form to serve this purpose, and the request could be included on the same form that married, non-borrowing employees with borrowing spouses would use to self-identify to their employers. Or, borrowers who wish to make additional payments could use a separate online system; however, the extra step of going to a separate website may reduce usage of the prepayment option.

Rethinking Institutional Accountability

Moving toward an auto-IBR scheme and repayment through employer withholding will reduce the administrative hurdles and other complexities that plague current income-driven options and lead to the underutilization of these programs. However, auto-IBR does not inherently lower the cost of college, nor does it eliminate the need for students to borrow. Previous research has shown that upfront costs simply need to be lower, through moderate tuition levels or targeted grant aid, to effectively improve college access and completion for the neediest students.¹⁶ Keeping costs low is the best way to minimize borrowing and, in effect, protect students against burdensome loan repayment. Awareness and accessibility are important benefits of moving to an auto-IBR system, but without appropriate protections in place this “system reset” could also have unintended consequences.

In this section we review potential unintended consequences of a switch to an auto-IBR system as well as possible solutions. These include better consumer information, loan limits, and institutional accountability measures. Though the consortium members bring different perspectives to these areas, we do broadly agree that the federal government should implement a system of outcomes-based institutional accountability as part of the federal student loan system.

Possible Unintended Consequences of Auto-IBR

By vastly simplifying the system for students, auto-IBR could inadvertently provide incentives for states and institutions to increase, rather than decrease, upfront costs by raising tuition, or limiting need-based aid, or both, exacerbating current negative trends.¹⁷ With no checks in place on college prices or student outcomes, debt-averse students may continue to undermatch into colleges that are less selective than those to which they could be admitted based on their academic qualifications, enroll part-time, or forgo college despite the auto-IBR safety net.¹⁸ Other students who are less debt-averse may react to higher costs by incurring more debt, remaining in repayment for longer, and paying more as they approach federal borrowing limits¹⁹ – even though their monthly payments will not become more burdensome under auto-IBR.

Worse, if costs rise above borrowing limits, students – particularly dependent undergraduates who face lower limits – could be forced to rely on Parent PLUS loans or private financing options, leaving them outside the protections of repayment plans that are based on income. If states and institutions disinvest further, a larger percentage of students may be faced with debt balances high enough to reach forgiveness under auto-IBR, with the federal government picking up the tab. In short, while auto-IBR represents a compelling option for solving our nation’s loan repayment crisis, it is important to consider which student and taxpayer protections should accompany this system redesign. These protections are necessary to prevent further exacerbating the access and affordability problems that must also be addressed if we are to achieve higher rates of college

attainment in this country.

Improving Consumer Information and Counseling

To be sure, the shift from our current repayment system – which includes nine options for students to weigh (including deferment and forbearance) – to auto-IBR presents an opportunity to combine simplicity in repayment with simplicity in consumer information and counseling. Minimally, third-party consumer information and counseling should be enhanced to make sure borrowers understand the full obligations and benefits of the new loan repayment scheme, including how to become eligible for loan forgiveness. Counseling also should aim to help borrowers understand new concepts, such as the “accelerated option,” so that they may offload debt on a faster schedule if desirable.

In this shift, ED will need to create tools that help students understand the mechanics of auto-IBR and make informed choices about where to attend college and how much to borrow. These tools should help students understand their monthly payments and loan terms at certain earnings levels and compare their likely debt levels and employment prospects (the two factors that underpin their payments in auto-IBR) by institution and/or program.

However, given the substantial investment in federal student grants, loans, and education tax benefits – nearly \$170 billion per year²⁰ –better consumer information alone will not mitigate some of auto-IBR’s potential unintended consequences. While auto-IBR simplifies repayment, it may not simplify the complex system of college choice, and it may not be sufficient to rely on consumer behavior to prevent larger-than-necessary costs to both students and the federal government.

Loan Limits in Auto-IBR

Another option for mitigating potential unintended consequences of an auto-IBR system is to institute stricter loan limits, particularly at the graduate level. Loan limits, by their nature would limit the amount the federal government would forgive in an auto-IBR system. As a result, loan limits could reduce incentives for institutions to charge more and students to borrow more. On the other hand, instituting loan limits at the graduate level could restrict access for low- and moderate-income students. Consortium members value these trade-offs very differently so there was no consensus policy on graduate loan limits under auto-IBR. This section will examine both the benefits and drawbacks of making loan caps for graduate students part of the transition to an auto-IBR system.

The Pros and Cons of Loan Limits under Auto-IBR

Currently, undergraduates may borrow Direct Subsidized and Unsubsidized Loans up to specified limits depending on their dependency status and financial need.²¹ Although the

parents of dependent undergraduates can take out Parent PLUS Loans up to the cost of attendance, these caps limit the amount of federal money undergraduate students themselves can borrow. In contrast, there is currently no cap on Grad PLUS loans for graduate and professional students, as students can borrow up to the cost of attendance (determined by the school) less any other financial assistance the student has received, regardless of financial need.²²

Limiting the amount graduate students can borrow could allow for lower payments and earlier loan forgiveness terms for everyone in an auto-IBR system, because the system would spend fewer resources forgiving graduate student debt. As discussed in our formula section above, various levers can be used to target benefits to certain borrowers. For example, a formula with a lower repayment rate and shorter forgiveness term could benefit low-income, low-debt borrowers. However, a repayment formula with these terms would benefit high-income, high-debt borrowers, who could pay back less over the life of the loan and receive larger amounts of forgiveness. Adding loan limits would cut off the potential benefit that high-debt borrowers could receive, allowing more targeted benefits to low-income borrowers without threatening the fiscal sustainability of the program.

Further, loan limits could reduce potential counterproductive incentives under auto-IBR. As discussed previously, under auto-IBR there is a risk that graduate institutions could increase tuition with few consequences, as the federal government would guarantee a minimum level of affordable payments. Loan limits could help protect against this, because above a certain level of tuition, students would need to take out private loans to finance their education. If institutions can no longer rely on unlimited federal loans to fund their high-tuition programs and if the private market is responsive to the ability of borrowers to repay (these loans must be made dischargeable in a regular bankruptcy proceeding), then graduate schools may have to set their pricing based, in part, on students' expected earnings.

That said, research on loan limits at the undergraduate level suggests they have little effect on tuition. The GAO has examined the question twice in recent years, finding that tuition and fees grew consistently before and after loan limit changes took effect.²³ On the other hand, the new incentive structure presented under the auto-IBR scheme could both change tuition incentives for schools and make loan limits more effective at curbing incentives for schools to raise tuition and for students to borrow.

Moreover, implementing loan limits at the graduate level would also come with potential downsides, particularly related to access for low- and moderate-income students. Many professional schools, such as medical or law schools, are expensive, but also consistently allow their graduates to earn very high incomes. Limiting access to federal loans for these programs could put them out of reach for students who do not have the out-of-pocket money to cover unmet need – even if they are likely to earn higher incomes after they graduate. Although private student loans are available, these loans come with a reduced repayment safety net (e.g. they may not be eligible for repayment based on income,

deferment, or forbearance). Additionally, low-income students without a credit history and/or a co-signer may face higher interest rates on these loans, or may be unable to take them out altogether. Low- and moderate-income students would then either take out loans with fewer consumer protections or be effectively barred from certain professional degree programs.

The consortium members value these competing interests differently and therefore reach different conclusions about the role loan limits should play in an auto-IBR program. However, an effective consumer protection scheme designed to ensure institutions have a stake graduating borrowers who earn incomes that offer a high likelihood that they can repay the debt they incurred alleviates some of the concerns regarding loan limits.

For YI's perspective on loan limits and institutional accountability under auto-IBR, see YI's paper, [Loan Limits and Auto-IBR](#).

Redesigning Federal Accountability Measures under an Auto-IBR System

Note: Some of the recommendations below do not reflect NASFAA's views. In particular, NASFAA recommends that any accountability system include institutional flexibility and discretion to limit borrowing for categories of students if the institution believes that level of borrowing is against the students' interest. For more on NASFAA's views, see their 2013 RADD paper, [Reimagining Financial Aid to Improve Student Access and Outcomes](#). Also see HCM's report, [Doing Better for More Students](#).

Another option for limiting the unintended consequences of auto-IBR involves implementing accountability measures for institutions. Some may suggest leaving it to states to ensure that institutions share adequately in the responsibility to provide value to students. However, relying solely on states may leave an oversight vacuum. For instance, while 31 states have established or are in the process of instituting outcome-based metrics as part of a performance-based funding (PBF) policy, not a single state has included student debt or student loan repayment measures as part of their PBF system. Moreover, the stakes for an institution's benefit or loss in these PBF policies are too low in almost all of these states to be meaningful. Some states are beginning to measure graduate earnings using dashboards, which are more transparency and management tools than accountability instruments. Six (AR, CO, FL, TN, TX, VA) of the ten states that developed state dashboards for higher education have included measures of graduate earnings and three (AZ, FL, MN) feature measures of graduate employment, but only one features measures of student debt (FL) and none include measures of repayment. Other states have implemented eligibility standards in their state grant programs, but in all but California and Colorado, those eligibility criteria involved additional standards for students rather increased accountability for institutions. For more details on these state efforts, see HCM's paper, [State 'Shared Responsibility' Policies for Improved Outcomes: Lessons Learned](#).

Furthermore, the federal government issues grants and loans directly, justifying its oversight. Currently, the federal government uses Cohort Default Rates (CDRs) as a minimum bar for institutional eligibility for federal financial aid.²⁴ However, precisely due to the projected benefits of auto-IBR (that is, fewer defaults), a move to auto-IBR would render CDRs nearly obsolete. As such, the federal government should minimally accompany a move to auto-IBR with a repayment measure that replaces CDRs, as a way of protecting the federal investment in loan forgiveness and ensuring that institutions and states provide a reasonable return on investment for students.²⁵

What follows is a discussion of the stringency and feasibility of various debt and repayment metrics under consideration by the consortium. For example, debt-to-earnings ratios provide an indirect measure of potential success in repayment, while repayment rates provide a more direct measure, but set a low minimum performance standard. A repayment progress measure could provide a more nuanced picture of student loan repayment, although there are measurement issues to consider. Any new accountability structure also should be phased in, allowing institutions ample time to prepare.²⁶

Debt-to-Earnings Ratios: An Indirect and Incomplete IBR-Accountability Measure

Debt-to-earnings ratios measure student loan debt as a proportion of students' income or discretionary income (that is, income above a poverty exemption) at a given point in time. The purpose of debt-to-earnings ratios is to reflect the "return on investment" of higher education – whether or not a program prepares a student to earn an income that aligns with the debt they must incur to receive the degree. Proposed regulations for programs designed to prepare students for gainful employment in a recognized occupation included two debt-to-earnings metrics: debt-to-income (which included all income), and debt-to-discretionary income (which included income above a poverty exemption).²⁷ Through the 2011 Gainful Employment (GE) regulations, ED collected and reported debt-to-earnings data for GE programs through the National Student Loan Data System (NSLDS), institutional reporting, and a partnership with the Social Security Administration. These data have not been collected or calculated since a U.S. district court opinion overturned the GE regulation, but such measures could be mandated statutorily.

Debt-to-earnings ratios attempt to measure whether borrowers' debts are in line with their earnings after college. In this sense, the underlying components of the ratios (debt and earnings) are fairly intuitive for institutional administrators to understand and develop plans to impact (e.g., by lowering prices and need to borrow or enhancing career placements). While understandable for institutions and students, these ratios are only indirectly related to successful repayment in an auto-IBR system, so likely are not the best choice for a stand-alone auto-IBR-based accountability metric. Similarly problematic is the lack of distinction in outcomes provided by debt-to-income ratios, under which a high-income/high-debt borrower could appear the same as a low-income/low-debt borrower, despite the low-income/low-debt borrower being more likely to struggle during repayment. Further, debt-to-earnings ratios have previously only included graduates in order to demonstrate

the value of credentials produced by the program in the workforce, which may be appropriate for purposes of the GE regulations. However, omitting the outcomes of non-graduates, who are more likely to struggle to repay loans,²⁸ is not appropriate if only one measure is to be used. If debt-to-earnings ratios are the only accountability measure, they should be disaggregated by completion status and reported and incorporated separately for completers and non-completers.

Repayment Rate: A Bare-Minimum Auto-IBR Accountability Measure

Repayment rates represent the ability of borrowers to make minimum progress against the principal of their loan balance. Repayment rates have been defined and calculated by the U.S. Department of Education through proposed regulations in several ways. These variations on repayment rates can help guide decisions about using repayment measures in a system of checks and balances under auto-IBR.

The final GE rules, released in 2011, defined repayment rate as the percent of federal loan dollars, borrowed to attend a program, that are “in repayment” (i.e., in which principal is reduced by at least \$1).²⁹ In other words, if a student pays at least \$1 toward principal over the course of a year, then that full loan balance is considered “in repayment.” If the balance increased – due to, for example, small payments accompanied by interest accrual – then the loan balance was counted as not “in repayment.” In 2013, ED proposed for discussion a new definition of repayment rate related to whether a GE program’s loan portfolio is negatively amortized, with programs at risk of sanction if the principal of their entire loan portfolio does not decrease in a given year.³⁰ In other words, a passing GE program’s total loan portfolio would need to decrease by at least \$1 over the year to avoid sanctions.³¹ Under both definitions, repayment rates included both program completers and non-completers.

While repayment rates were calculated as part of GE negotiations and regulations for reference purposes (using the 2011 definition noted above), ED does not currently calculate and report them on a regular basis. However, the data to do so do exist in NSLDS, and ED has released repayment rates in the past. For example, ED calculated program-level repayment rate data for gainful employment programs in 2011 under regulations in place at the time.³² Also, in 2009, they calculated institution-level repayment rates for all schools (not just those subject to GE regulations) in order to model the impact of proposed regulations. The 2009 data, shown in Table 1, suggest that public and private non-profit four-year, private nonprofit two-year, and public less-than-two-year institutions tend to have higher repayment rates than for-profit institutions and public community colleges.³³

Table 1: Average Repayment Rates by Sector									
Sector	Public 4-Year	Public 2-Year	Public Less Than 2-Year	Private Non- Profit 4-Year	Private Non- Profit 2-Year	Private Non- Profit Less Than 2-Year	For- Profit 4-Year	For- Profit 2-Year	For- Profit Less Than 2-Year
Average Repayment Rate	54%	44%	53%	57%	60%	51%	37%	39%	42%
Source: IHEP calculations based on the U.S. Department of Education <i>Negotiated Rulemaking for Higher Education 2009-10: Data Used to Model the Effects of the Program Integrity (Gainful Employment) Notice of Proposed Rulemaking</i> (Washington DC: 2010). Repayment Rate calculations include all institutions, including those not subject to GE regulations. FAQs about these repayment rate data are available here: http://www2.ed.gov/policy/highered/reg/hearulemaking/2009/ge-repayment-faq.pdf .									

Repayment rates, which reflect the ability of students to make more than interest-only payments on their loans, offer a number of advantages as an option for replacing CDRs in an auto-IBR system. While auto-IBR helps mitigate risk for students who cannot afford to pay down the principal of their loans, repayment rates would hold institutions accountable for students who do not earn enough to do so, requiring institutions to share some of the risk with the federal government. Further, by including non-completers in the calculation, repayment rates incentivize completion, since borrowers who earn a credential are more likely to be able to pay off loans. In fact, non-completion is consistently the best predictor of student loan default.³⁴

Furthermore, unlike under CDRs, the loan balances of borrowers in deferment or forbearance may count as negative outcomes in repayment rate calculations per the 2011 definition.³⁵ When students enter deferment or forbearance, their loan balances are unlikely to decline, so those balances will be counted as not “in repayment.” Because the balances of most loans in deferment or forbearance do not decline, repayment rates would capture more borrowers who are struggling to repay than are captured by CDRs. Similarly, a well-designed repayment measure would not count as “in repayment” those borrowers who are paying through auto-IBR but earning so little that their minimum monthly payments are not enough to reduce their principal.

During various GE negotiations, some argued that borrowers in income-driven repayment plans should not negatively affect an institution’s repayment rate, even if those borrowers are not decreasing their loan principal.³⁶ In developing a repayment measure as a check on auto-IBR, most members of the consortium³⁷ agreed that all borrowers who are not reducing loan principal must be included in the measure and count as not “in repayment,” even if they maintain good standing through auto-IBR. In fact, an accountability measure

How to Measure Accountability: Institution vs. Program

The consortium debated whether the proposed auto-IBR-based system of checks and balances should measure institutional or program-level performance.

On one hand, holding programs accountable for their performance would offer a more targeted system of checks and balances, assuring that failing programs cannot persist. However, implementing a program-level accountability system would require far more in-depth data collection than currently exists. Program-level data on debt and repayment were collected under GE rules, but expanding these types of accountability measures to all programs and institutions would require substantially more robust data systems.

Also, program-level repayment measures may encourage the use of differential tuition, in which majors with high expected earnings would cost more or majors with low expected earnings would cost less. Extreme program-level tuition differentiation could stratify program access based on family income levels, making it more difficult for low-income students to access high-paying fields.

Finally, program-level measures would require minimum sample sizes, limiting performance measures to those programs with sufficient numbers of students. Ultimately, the consortium recommends first implementing the system of checks and balances based on institution-level performance for all undergraduate programs combined and institution-level performance for all graduate programs combined.

Using institution-level measures also will allow schools flexibility in meeting benchmarks, though. It could allow institutions to mask poor performance in some programs with strong performance in others. More modeling is necessary to determine whether high-performing programs mask poor performance of other programs or *balance out* performance of moderately performing programs that fulfill a social good. If the former is true, institutional level measures could later be applied to programs.

is intended to capture just that: borrowers who are unable to make a dent in their loan balances through affordable monthly payments.

Despite the advantages of repayment rates, they also face some limitations as an accountability tool, primarily related to their lack of comprehensiveness in identifying struggling borrowers. Without making a distinction between those paying back \$1 of principal and those making a sizeable dent in their debt, borrowers could be considered in repayment while not making substantial progress to pay off loan balances. This is a particular concern in an auto-IBR system offering loan forgiveness. Paying off \$1 of principal should be a bare minimum expectation, but truly successful borrowers should be able to make more progress. For example, a borrower may decrease her loan balance by \$5 over the course of the year, but have income low enough and debt high enough that she is projected to repay for 20 years and generate a substantial forgiveness cost for the federal government. While auto-IBR is designed to protect just this type of borrower, an accountability mechanism should be designed to identify institutions or programs that are producing many borrowers who fall into this situation, which a repayment rate would not do.

Also, repayment rate definitions have not traditionally accounted for PLUS loans for parents or Federal Perkins Loan borrowing (or private borrowing, for that matter). As a result, repayment rate measures do not hold institutions accountable for the full amount of debt students incur and their ability to repay it. Perkins loans could and should be included in repayment measures. Data on repayment of private loans are not easily available, although some institutions reporting to the Common Data Set do provide data on private loans, and

many private lenders now require school certification, warranting further discussion about the feasibility of obtaining such information from colleges or lenders. Incorporating parent PLUS loans into the repayment metric, while technically feasible, would require more discussion about their applicability in this context since students do not take out these loans for themselves.

Repayment Progress Measure: A More Comprehensive (but More Complicated) Solution

A third option could provide a more complete and nuanced picture of student loan repayment than either the repayment rate or debt-to-income measures. A repayment progress measure involves calculating patterns of progress on loan repayment for cohorts of students.³⁸ This measure could be structured in a number of ways, such as:

- The proportion of borrowers on track to repay loans on time (which might be defined as 10-12 years), based on the ratio of outstanding balance to original balance in the initial years (which might be defined as three or four years) after entering repayment;
- The average predicted number of years in repayment for a cohort, based on repayment in the first several years;
- The amount or proportion of the loan portfolio on track to be forgiven, based on the first several years in repayment;
- The percentage of borrowers with negative interest accrual on loans, at a period after entering repayment. (This would be similar to the portfolio repayment rate proposed by ED, reflecting the ability of borrowers to pay principal on their loans); and
- The percentage of borrowers making a \$0 monthly payment under the auto-IBR formula (or in deferment or forbearance) at a period in time after entering repayment. (This would reflect the number of borrowers with low-incomes but would not reflect their level of indebtedness, as would the other options).

The major benefit of this type of measure is that it is more stringent than current repayment rates, capturing students who are struggling with burdensome debts, even if they are making bare minimum progress (\$1 in principal) against those debts. It is also directly related to repayment success and loan forgiveness, presenting a clear tie to the federal government's costs associated with auto-IBR.³⁹

Perhaps the biggest drawback of a measure of repayment progress is that it is more complicated than a repayment rate. Also, some may interpret it as a pure prediction tool and argue that it will be inaccurate for students in some programs who may have uncommon income trajectories. It is true that the prediction may not be precise, especially because

student ability to pay likely increases over time, possibly at different rates for different fields of study. In short, a borrower's balance at years three and four of repayment might look as if he or she will receive forgiveness even if she ultimately experiences income growth and does not reach forgiveness. Despite this lack of precision, the measure could be useful in judging loan repayment progress. While public data are unavailable to model these types of repayment progress measures, ED should use its internal data systems, such as NSLDS, to examine the full impacts and implications of these measures in more detail, including using historical data to model repayment trends by sector and level to determine the appropriate number of years at which to measure progress and the appropriate benchmarks for judging adequate progress.

Regardless of the measure used, any repayment measure should be disaggregated by income or financial aid status, so that institutions can be held accountable for meeting performance standards for both Pell Grant recipients and non-Pell Grant recipients, protecting against the potential for inequitable outcomes. This disaggregation will help ensure that institutions prepare all students – especially those with the least family resources on which to fall back – to be able to repay their debts. To ensure the new measure is fair to institutions, adjustments or exemptions could be considered for institutions with low prices and/or low borrowing rates. And, just as ED has phased in changes to CDRs in the past, these new accountability measures should be phased in, allowing time for institutions to adjust.

Comprehensive Accountability in Auto-IBR: Completion, Access, and Price Measures

Repayment measures offer a minimum level of accountability required under an auto-IBR scheme. However, they are not the only set of measures that ED could use for determining Title IV eligibility. Measures of price and completion could be worth including in a system of checks and balances, and an access measure could guard against institutions limiting enrollment to underserved populations in order to perform well on repayment and other accountability measures.

Repayment metrics do proxy price and completion indirectly, but more direct measures of price and completion rates may be worthwhile. Though high prices certainly correlate with high borrowing, non-borrowers are not captured in repayment metrics. A more comprehensive accountability system may aim to protect all students, including students who pay for college out-of-pocket or through mechanisms other than federal loans, especially credit cards. Price measures would be particularly important in protecting students who avoid borrowing by making substantial sacrifices in terms of time-to-degree and hours worked.

How to Distinguish Accountability: Graduate vs. Undergraduate Programs

The measures outlined in this paper are primarily designed to measure institutional performance with undergraduate students – not because graduate students are less important, but rather because data on graduate students are severely lacking. However, the stakes may be even higher with graduate borrowing, considering that graduate students represent about 15 percent of all Stafford Loan borrowers, but more than 30 percent of all Stafford Loan dollars.⁴⁵ In addition, graduate students can borrow up to the full cost of attendance now with the introduction of GRAD PLUS loans in 2007. This raises concerns about the impact on prices for graduate programs as a result of auto-IBR.

Better data on the institutional performance for graduate students is critical, then – even for existing CDR measures. Current CDRs combine undergraduate and graduate students into the same cohort, making it impossible to parse out different outcomes for students pursuing different levels of education. The system of checks and balances outlined in this paper could apply to all undergraduate programs at an institution, combined, *and* to all graduate programs at an institution, combined. In essence, each institution would be judged twice: once as an undergraduate institution and once as a graduate institution. However, to measure the performance of institutions at the graduate level, ED will need to collect additional data. Because these data will be new, their link to Title IV eligibility should be phased in over time, allowing institutions to adjust to the new results and performance standards for graduate programs. Also, any new reporting requirements should be considered carefully and designed to minimize burden. For example, in cases where accurate data can be compiled from ED's existing data sets, new institutional reporting would be unnecessary.

Repayment: ED can calculate a repayment measure using existing data in NSLDS. The graduate school calculation should parallel the undergraduate calculation, and both should be disaggregated by socioeconomic status (e.g., Pell Grant receipt while an undergraduate).

Access: While advocates, policymakers, and institutions have placed a great deal of attention on access to undergraduate programs for underserved students, they have devoted less attention to access to graduate programs for these populations. Identifying the socioeconomic background of graduate students can be difficult because they are no longer considered dependents of their parents. However, NSLDS could identify graduate students who come from low-income backgrounds by flagging which graduate students received Pell Grants for their undergraduate studies.

Completion: Institutions are not required to report graduation rates for graduate students. IPEDS should begin collecting data on the success rates of students in graduate programs, including disaggregation by race/ethnicity, gender, and socioeconomic status (as measured by Pell Grant receipt as an undergraduate).

In addition, an access metric is critical in any accountability system to protect against institutions trying to meet performance benchmarks by cutting access for students who are less likely to complete or more likely to borrow substantial amounts. In fact, in conversations with higher education experts conducted as part of the research process for this paper, multiple commenters emphasized the importance of protecting access alongside any other outcomes-based accountability measures.

Ensuring access for low-income, underrepresented students is essential in any high stakes institutional accountability scheme. To promote access for these populations and to mitigate incentives for institutions to reduce access, HCM proposed the creation of an

“Institutional Eligibility Index” for federal Title IV programs in RADD 1.0. This proposal integrated measures of access, loan repayment and completion rates. Under HCM’s recommendations, institutions would not need to perform strongly on all components of the index to participate in Title IV, but neither could they get by with weak performance on all or most components. This proposal represents one type of institutional accountability system, which is endorsed by HCM but not necessarily by all members of this consortium. Using multiple measures rather than a single one – like CDRs – makes it more difficult to improve performance on one measure by performing worse on another.

Table 2 outlines the various alternate metrics ED could use to protect the federal investment in higher education, and how each might add value in any regulatory structure. ED could choose multiple metrics within each category (such as measuring institutions both by overall graduation rates as well as graduation rates of Pell Grant recipients). It also might consider using the non-repayment measures as secondary indicators that offer a supplemental level of accountability for institutions that are close to failing on the primary measure(s). For example, repayment measures could be used to determine passing and failing thresholds for institutions, with those on the verge of failure facing a second level of scrutiny based on secondary measures, including price and completion. An access measure should accompany any accountability measure, including repayment measures. Further analysis and modeling is necessary to determine the appropriate benchmarks on the various metrics, including whether to allow for any adjustments based on the type and mission of the institution. When used to determine basic Title IV eligibility, however, minimum cutoffs may not require any adjustments.

Table 2. Non-Repayment Institutional Accountability Measures in Auto-IBR		
Measure Category	<i>Rationale</i>	<i>Recommended Metrics (Measures available in Integrated Postsecondary Education Data System (IPEDS) shown in BOLD)⁴⁰</i>
Completion	Research suggests that not completing a postsecondary program is the strongest single predictor of struggling to repay student loans. ⁴¹ As such, it is important to understand which institutions perform well at graduating their students.	<p>Overall (150%) Graduation Rate</p> <p>Overall On-Time (100%) Graduation Rate</p> <p>Pell Grant Recipient Graduation Rate</p> <p>Note: IPEDS graduation rates should be improved to include part-time and transfer students and to disaggregate by type of credential (bachelor’s, associate’s, or certificate) sought and income/financial aid receipt.⁴²</p>

<p>Price</p>	<p>As all students gain automatic access to income-based repayment, institutions and states could raise tuition or reduce need-based grant aid at faster rates with the knowledge that students will still have affordable monthly loan payments and, for some, eventual loan forgiveness. Repayment metrics are influenced by price in so far as borrowers accrue more debt, but they are an indirect price measure. It may be more appropriate to hold institutions accountable for the price students must pay, whether through borrowing, family contributions, or student work. Research indicates that non-traditional students tend to avoid or minimize borrowing for college, even if they have remaining financial need,⁴³ so a price measure would protect these students more fully than a repayment measure.</p>	<p>Average Net Price</p> <p>Net Price for Low-Income Students</p> <p>Net price data should be revised to include prices for continuing and transfer students, instead of only freshmen</p>
<p>Access (Essential Protectionary Measure)</p>	<p>An access measure would act as a protection to ensure that institutions do not seek to perform well on repayment (and/or completion) metrics by excluding populations who tend to experience less favorable outcomes in higher education. Without such standards – which could be implemented as minimum benchmarks or limitations on decreases in Pell access over time – potential price increases and institutional concerns about meeting the other benchmarks may lead to exclusion of low-income, price-sensitive students. Pell enrollment data are readily available from the Office of Federal Student Aid and IPEDS to populate this metric.</p>	<p>Percent of Students Receiving Pell Grants⁴⁴</p>

The Stakes and Application of Accountability in Auto-IBR

Title IV Eligibility

Traditionally, the strongest accountability mechanism at ED's disposal has been Title IV aid eligibility. Loss of Title IV aid eligibility eliminates the ability of a school to receive money from grant and loan programs, thus cutting off the primary source of aid that students use to cover college costs.⁴⁶ Perhaps because of the stringency of this penalty, Congress and ED have set very high thresholds for eligibility loss. For example, in the most recent release of two-year CDRs, only eight total schools were subject to sanctions based on the 25 percent threshold, and 218 must develop "default prevention plans" for having a three-year rate of at least 30 percent.⁴⁷ In short, the "all-or-nothing" nature of Pell Grant and Direct Loan eligibility is harsh enough to be used sparingly, but also makes almost no distinction between a school with a two-year CDR of 0 percent for three years and a school with a two-year CDR of, for example, 39 percent for two consecutive years, if the third year is below 25 percent. Under an auto-IBR system, a repayment measure floor will need to be instituted to determine Title IV eligibility and protect students from the worst-of-the-worst outcomes. More empirical research is necessary to identify this performance floor. We also recommend exploring ways to broaden accountability beyond the current all-or-nothing approach.

Risk Sharing

Risk sharing could create an interim accountability system for institutions, while limiting

loss of Title IV eligibility to only the absolute lowest performers. Some members of the consortium think a risk-sharing approach, in conjunction with an eligibility floor, could incentivize institutions on the cusp of failure to improve, while also protecting student and taxpayer investments. Risk sharing has gained new attention recently, but is not a new idea. The Institute for College Access and Success, for example, has proposed risk sharing for some institutions based on their performance.⁴⁸ Another proposal recently introduced in the Senate would require risk sharing for institutions at which at least 25 percent of students borrow federal loans.⁴⁹ And, risk sharing is already built into the Federal Family Education Loan (FFEL) Program, under which lenders can recover a proportion of the outstanding loan balance when a borrower defaults on a FFEL loan. That proportion is determined based on the guarantee agency's default rate.⁵⁰

In the auto-IBR context, such a system could hold institutions liable for some portion of the school's total loan balance based on their performance on a repayment measure. Since loan defaults would decrease under auto-IBR while loan forgiveness would most likely increase, risk-sharing could, for instance, hold institutions responsible for a portion of their total loan portfolio projected to be forgiven after 20 (or 25) years for a given cohort.⁵¹ This scheme could be structured a number of ways. For example, an institution at which 30 percent of the total loan portfolio is projected to be forgiven based on the initial years of student repayment under auto-IBR could be required to contribute the equivalent of, say, 15 percent of its total loan portfolio into this fund (or less stringently, 15 percent of the dollars expected to be forgiven), which would help the federal government finance loan forgiveness. As discussed earlier, this projection would not provide a precise estimate of loan forgiveness because borrower incomes will change – likely increase – throughout repayment. However, it can serve as an early indicator of successful repayment and a useful estimator in a risk-sharing scheme.

Using the risk-sharing model in place for the guarantee agencies as a guide, a potential risk-sharing structure could be constructed as follows:

- If 0 percent of an institution's borrowers are on track for forgiveness at year 4 (assuming average income increases over time), the institution will contribute 0 percent of that cohort's loan portfolio to the risk-sharing fund.
- If 1-10 percent of an institution's borrowers are on track for forgiveness, the institution will contribute 5 percent of that cohort's loan portfolio to the risk-sharing fund.
- If 11-20 percent of borrowers are on track for forgiveness, the institution will contribute 10 percent of that cohort's loan portfolio to the risk-sharing fund.
- If 21-30 percent of borrowers are on track for forgiveness, the institution will contribute 15 percent of that cohort's loan portfolio to the risk-sharing fund.

- If more than 30 percent of borrowers are on-track for forgiveness, the institution will fail the repayment progress metric and risk losing Title IV eligibility in part or full.

The risk-share could be determined by a sliding scale instead of cut-offs for varying levels of performance on the repayment progress metric. Also, the system could waive the risk-sharing payment for institutions meeting certain benchmarks. As another alternate example, institutions could be required to pay – either into the risk-sharing fund or directly to students to prevent ballooning debt – a portion of any negative interest that accrues on loans in their portfolio. In the November 2013 GE negotiations, ED proposed a similar measure: institutionally provided debt relief for programs likely to lose Title IV eligibility in the following year.⁵²

As with all accountability schemes, risk sharing brings concerns about unintended consequences. Institutions might, for instance, shift costs onto students by folding the risk-sharing payment into increased tuition and fees, or by increasing prices for students who do not borrow in order to fund the pool. However, a carefully designed system can avoid these unintended results. For example, if risk-sharing payments are based on repayment measures (and especially if they are tied to price measures), then tuition increases may simply increase debt and eventual forgiveness – requiring institutions to contribute even more to the risk-sharing fund. Also, protections could be put in place to protect against price increases, either for all institutions or for low-performing institutions required to pay into the risk-sharing pool. Furthermore, it may be difficult to determine an institution's risk share for a student who has attended more than one institution. One option could be to require a proportional risk share for each institution a borrower attended based on the amount borrowed at each institution.

Positive Incentives for Improvement

ED could also develop a system that rewards schools that perform well (or better than expected) or improve on certain measures. For an incentives-based system, ED could divide a set amount of funds among institutions similar to the way performance-based systems currently are being utilized to distribute appropriations in a growing number of states. Colleges could demonstrate outcomes on a variety of measures, such as the number of Pell recipients who persist beyond freshman year and graduate, or those whose repayment metrics for low-income students exceed a certain threshold. The awards would need to be sizeable enough to incentivize change, and if they are, a competitive effort of this nature could drive positive institutional or state behavior.

Interim Stakes: Campus-Based Aid, Tax-Exempt Status, and Incentive Fund Eligibility

Another way to structure interim accountability is to change the stakes. For example, schools that do not fail the bare minimum benchmark for Title IV eligibility, but that are projected to have a subpar percentage of loans forgiven, could be deemed ineligible for all

campus-based aid (including Perkins Loans, Federal Work Study, and FSEOG) or higher education tax credits, such as the American Opportunity Tax Credit. These options are feasible but less than ideal because the sanctions could hurt students by restricting their access to aid that does not need to be repaid (with the exception of Perkins Loans). They also may not be sizable enough to impact institutional behavior. Instead of using student aid as a lever, performance standards also could be tied to eligibility for and/or amounts of research funding, federal competitive grants, or institutional tax-exempt status. Each of these stakes will have distinct effects on different types of institutions, so identification of the most appropriate stake would be well informed by further analysis of the institutions that are likely to struggle to meet benchmarks.

Alternately, Parent and Grad PLUS loan limits could be implemented for institutions that are close to failing the repayment rate or other measure. If an institution is struggling to prepare its students to graduate and/or repay student debt, then ED might be justified in restricting borrowing levels at that institution.⁵³ Allowing PLUS loans up to the cost of attendance should provide low- and moderate-income students with access to high-performing institutions. Restricting PLUS for poor-performing institutions may limit the negative effects on families borrowing loans that are not eligible for auto-IBR at schools that do not serve students particularly well.

Conclusion

A postsecondary degree pays off for the vast majority of students attending the vast majority of colleges across the country. That, despite this, many borrowers end up delinquent or in default on their student debt drives us to propose the reforms above. We believe that an overly complex and poorly designed federal student loan repayment system results in needless financial hardship for borrowers.

In contrast, automatically enrolling borrowers in a repayment plan based on income and administering it through employer withholding would virtually eliminate delinquencies and defaults. Doing so would require adjustments to the current repayment formula. A new formula must strike a balance with the sometimes-competing principals of fairness, fiscally sustainability, simplicity, and provision of an adequate safety net. Our discussion of the trade-offs should make clear that there is no perfect solution, though we do agree on a number of elements that any reform should contain.

Finally, we believe that in order for its students to obtain federal student loans, an institution should meet a minimum standard in showing its borrowers can pay off their debt. That concern is all the more heightened in an auto-IBR system that guarantees a minimum level of affordable payments and forgives the remaining debt after a certain number of years. Policy-makers have a number of options in this regard and we offer several possible alternatives above. Auto-IBR, implemented in conjunction with these accountability mechanisms, would make the current repayment system fairer and more effective.

End Notes

1. "Two-year Official Cohort Default Rates for Schools," U.S. Department of Education. Retrieved from <http://www2.ed.gov/offices/OSFAP/defaultmanagement/cdr2yr.html>.
2. Based on the overall two-year default rate for the 2006 cohort found in: "Default Rates Two-Year Cohort Default Rate," U.S. Department of Education. Retrieved from <http://www.ifap.ed.gov/eannouncements/attachments/DefaultRates.pdf>.
3. U.S. Department of Education, *Student Loans Overview: Fiscal Year 2014 Budget Proposal* (Washington, DC: 2014), 32, accessed February 20, 2014, <http://www2.ed.gov/about/overview/budget/budget14/justifications/s-loansoverview.pdf>.
4. See, e.g., Bill Hardekopf, "More Than Half of Student Loans Are Now in Deferral or Delinquent," *Forbes*, February 1, 2013. Retrieved from <http://www.forbes.com/sites/moneybuilder/2013/02/01/alarmed-number-of-student-loans-are-delinquent/>.
5. Anthony P. Carnevale, et al., *The College Payoff: Education, Occupations, Lifetime Earnings* (Washington, DC: The Georgetown University Center on Education and The Workforce, 2011), 1. Retrieved from <http://www9.georgetown.edu/grad/gppi/hpi/cew/pdfs/collegepayoff-complete.pdf>.
6. See, e.g., Project on Student Debt, *Student Debt and The Class of 2012* (Washington, DC: The Institute for College Access & Success (TICAS), 2013), 1. Retrieved from <http://projectonstudentdebt.org/files/pub/classof2012.pdf>.
7. Ibid.
8. See, e.g., "Repayment Plans," Federal Student Aid, U.S. Department of Education. Retrieved from <http://studentaid.ed.gov/repay-loans/understand/plans#direct-and-ffel>.
9. Data derived from: "Direct Loan Portfolio by Repayment Plan," Federal Student Aid, U.S. Department of Education. Retrieved from <http://studentaid.ed.gov/about/data-center/student/portfolio>. (Percent of Direct Loan recipients in Income-Based, Income-Contingent, or Pay As You Earn Repayment Plans in the first quarter of 2014).
10. Bureau of Labor Statistics, U.S. Department of Labor, "The Job Market for Recent College Graduates in the United States," *The Editor's Desk*, April 05, 2013. Retrieved from http://www.bls.gov/opub/ted/2013/ted_20130405.htm.
11. Susan Dynarski, "Improving College Outcomes: A Modern Approach to Financing Higher Education," panel discussion sponsored by the Hamilton Project (Washington, D.C.: Brookings Institution, October 21, 2013), [http://www.hamiltonproject.org/multimedia/audio/improving_college_outcomes_a_modern_approach_to_financing_higher_education/\[begins at 54 minutes\]: "Obama's Pay As You Earn... is simply not sustainable... we do not propose that it become the default. There is nervousness about making this program the default because the program is so expensive, it should not be made the default because it is not designed in such a way that it will be self-sustaining."; Cooper Howes, *Student Loans: An Educated Mess* \(New York, NY: Barclays Economic Research, December 2012\). The report finds that more than half of federal student loan borrowers would qualify for a reduced payment under IBR available to new borrowers as of 2007, posing a](http://www.hamiltonproject.org/multimedia/audio/improving_college_outcomes_a_modern_approach_to_financing_higher_education/[begins%20at%2054%20minutes]:%20%22Obama's%20Pay%20As%20You%20Earn...%20is%20simply%20not%20sustainable...%20we%20do%20not%20propose%20that%20it%20become%20the%20default.%20There%20is%20nervousness%20about%20making%20this%20program%20the%20default%20because%20the%20program%20is%20so%20expensive,%20it%20should%20not%20be%20made%20the%20default%20because%20it%20is%20not%20designed%20in%20such%20a%20way%20that%20it%20will%20be%20self-sustaining.%22%3B%20Cooper%20Howes,%20Student%20Loans:%20An%20Educated%20Mess%20(New%20York,%20NY:%20Barclays%20Economic%20Research,%20December%202012).%20The%20report%20finds%20that%20more%20than%20half%20of%20federal%20student%20loan%20borrowers%20would%20qualify%20for%20a%20reduced%20payment%20under%20IBR%20available%20to%20new%20borrowers%20as%20of%202007,%20posing%20a)

- “significant financial risk” to the federal government, and that the U.S. Department of Education had underestimated the impact of the cost of the program by \$225 billion between 2012 and 2020. “Federal Perkins Loan Program, Federal Family Education Loan Program, and William D. Ford Federal Direct Loan Program; Notice of Proposed Rulemaking,” *77 Federal Register* 137 (July 17, 2012): pp. 42122, <http://www.gpo.gov/fdsys/pkg/FR-2012-07-17/pdf/FR-2012-07-17.pdf>. ED estimates that one-quarter of borrowers using IBR will receive loan forgiveness worth an average of \$41,000 on original loan balances of \$39,500; The president’s Fiscal Year 2014 budget shows that the subsidy rate on a loan issued in 2014 and repaid through IBR has a subsidy rate of 10 percent, while a loan repaid through the standard repayment plan has a subsidy rate of -29 percent. <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2014/assets/edu.pdf>.
12. U.S. Department of Education, “Income-Based (IBR)/Pay As You Earn/Income-Contingent Repayment Plan Request Form,” (Washington DC: 2012). Retrieved from: <http://www.ifap.ed.gov/dpcletters/GEN1222.html>; U.S. Department of Education, “Loan Servicing Information - Availability of Pay As You Earn Repayment Plan and Electronic IBR/Pay As You Earn/ICR Repayment Plan Request,” (Washington DC: 2013). Retrieved from: <http://www.ifap.ed.gov/eannouncements/122112LSIPayAsYouEarnPlanIBRnICR.html>.
 13. “Despite previous attempts by the administration to promote the income-based programs and ease the application process, enrollment remains low. Fewer than 7 percent of federal direct loan borrowers whose loans were in repayment had enrolled in an income-based repayment plan by June 30 of this year.” Michael Stratford, “You’ve Got Mail,” *Inside Higher Ed*, November 4, 2013. Retrieved from: <http://www.insidehighered.com/news/2013/11/04/education-dept-will-email-35-million-student-loan-borrowers-about-income-based#ixzz2pujAyQJX>.
 14. U.S. Department of Education, “Default Rates Continue to Rise for Federal Student Loans” (Washington DC: September 30, 2013). Retrieved from: <http://www.ed.gov/news/press-releases/default-rates-continue-rise-federal-student-loans>.
 15. *ExCEL Act of 2013*. HR 1716. 113th Cong., 1st sess. Congressional Record 159, no. 57, daily ed. (April 24, 2013): H 2298.
 16. Susan Dynarski, “Does Aid Matter? Measuring the Effect of Student Aid on College Attendance and Completion.” *The American Economic Review*, vol. 93, no. 1 (2003), p. 279–288; Donald E. Heller, “Making College a Priority: Promising Practices and Strategies.” Testimony before the U.S. Senate Committee on Health, Education, Labor and Pensions, (2012). Retrieved from: <http://www.help.senate.gov/imo/media/doc/Heller.pdf>; Benjamin L. Castleman and Bridget Terry Long, “Looking Beyond Enrollment: The Causal Effect of Need-Based Grants on College Access, Persistence, and Graduation,” (Cambridge, MA: Harvard Graduate School of Education, 2012); Eric P. Bettinger, “How Financial Aid Affects Persistence.” In *College Choices: The Economics of Where to Go, When to Go, and How to Pay for It*, ed. C. Hoxby (Chicago: University of Chicago Press, 2004), 207-233.
 17. Appropriations per full-time equivalent student (in real terms) were lower in 2012 than at any time since 1980. State Higher Education Executive Officers (2013). *State Higher Education Finance FY 2012*. Retrieved from: <http://www.sheeo.org/sites/default/files/publications/SHEF%20FY%2012-20130322rev.pdf> and Stephen Burd, “Undermining Pell How Colleges Compete

- for Wealthy Students and Leave the Low-Income Behind.” New America Foundation (2013). Retrieved from: http://education.newamerica.net/sites/newamerica.net/files/policydocs/Merit_Aid%20Final.pdf.
18. Alisa F. Cunningham and Deborah A. Santiago, “Student Aversion to Borrowing,” Institute for Higher Education Policy and *Excelencia* for Education (2008). Retrieved from <http://www.ihep.org/assets/files/publications/s-z/StudentAversiontoBorrowing.pdf>.
 19. Loan limits can keep federal debt from rising, up to a point. Dependent undergraduates can borrow up to \$31,000 in Stafford loans, independent undergraduates can borrow up to \$57,500, and graduate and professional students can borrow up to \$138,500 (including undergraduate loans). Federal Student Aid, U.S. Department of Education. Retrieved from: <http://studentaid.ed.gov/types/loans/subsidized-unsubsidized>.
 20. College Board, *Trends in Student Aid 2013* (Washington, DC: 2013). Retrieved from: <http://trends.collegeboard.org/student-aid/figures-tables/total-student-aid-and-nonfederal-loans-current-dollars-over-time>.
 21. See “How much can I borrow?” Federal Student Aid, U.S. Department of Education (Washington DC: December 16, 2013). Retrieved from: <http://studentaid.ed.gov/types/loans/subsidized-unsubsidized#how-much-can-i-borrow>.
 22. See “PLUS Loans How much can I borrow?” Federal Student Aid, U.S. Department of Education. Retrieved from: <http://studentaid.ed.gov/types/loans/plus#how-much-can-i>.
 23. See Government Accountability Office (GAO), “What GAO Found,” in *Federal Student Loans: Impact of Loan Limit Increases on College Prices Is Difficult to Discern* (Washington, DC: 2014). Retrieved from: <http://gao.gov/assets/670/660991.pdf>; Government Accountability Office “Federal Student Loans: Patterns in Tuition, Enrollment and Federal Stafford Loan Borrowing Up to the 2007-2008 Loan Limit Increase” Washington, DC, 2011), p.3, Retrieved from: <http://www.gao.gov/assets/100/97510.pdf>.
 24. Institutions with two-year cohort default rates greater than 40 percent (starting in 2014, this will change to three-year CDRs greater than 40 percent) in one year lose eligibility to participate in the Direct Loan program. Institutions with two-year CDRs greater than 25 percent in three consecutive years (in 2014, this will change to three-year CDRs greater than 30 percent in three consecutive years) lose eligibility to participate in the Direct Loan and Pell Grant programs. 34 CFR 668.187, 34 CFR 668.206. U.S. Department of Education. “Default Rates Continue to Rise for Federal Student Loans” (Washington, DC: 2013) [Press Release]. Retrieved from: <http://www.ed.gov/news/press-releases/default-rates-continue-rise-federal-student-loans>. Some have argued that CDRs are easily gamed under the current system. For more, see: The Institute for College Access and Success (August 21, 2012). [Memo] “Steps the Department Should Immediately Take to Curb Default Rate Manipulation.” Retrieved from: http://www.ticas.org/files/pub/TICAS_memo_on_CDR_evasion_082112.pdf. Even absent a shift to auto-IBR, some, but not all, consortium members would support a shift to another measure that captures students who are struggling in repayment, but not defaulting.
 25. The majority of consortium partners, advisory panel members, and other experts in the field consulted about this project agreed that an auto-IBR system should include new accountability measures.

26. HCM Strategists, "Doing Better for More Students" (Washington, DC: 2013). p. 25. Retrieved from: http://hcmstrategists.com/wp-content/themes/hcmstrategists/docs/Technical_report_fnl.pdf
27. U.S. Department of Education *Final Regulations: Program Integrity: Gainful Employment-Debt Measures*. 76 FR 34385 (Washington DC: 2011). Retrieved from: <https://www.federalregister.gov/articles/2011/06/13/2011-13905/program-integrity-gainful-employment-debt-measures>.
28. Jacob P. K. Gross, Osman Cekic, Don Hossler, and Nick Hillman "What Matters in Student Loan Default: A Review of the Research Literature." *Journal of Student Financial Aid*, 39:1 (2009). Retrieved from: <http://content.lib.utah.edu/utills/getfile/collection/uspace/id/5348/filename/image>.
29. U.S. Department of Education *Final Regulations: Program Integrity: Gainful Employment-Debt Measures*. 76 FR 34385 (Washington DC: 2011). Retrieved from: <https://www.federalregister.gov/articles/2011/06/13/2011-13905/program-integrity-gainful-employment-debt-measures#h-26>.
30. U.S. Department of Education *DRAFT Regulatory Language, Subpart Q: Gainful Employment (GE) Programs* (Washington DC: 2013). Retrieved from: <http://www2.ed.gov/policy/highered/reg/hearulemaking/2012/draft-regs-session2-11813.pdf>.
31. Ben Miller from New America has proposed a similar repayment measure. See: Ben Miller, "Improving Gainful Employment: Suggestions for Better Accountability." New America Foundation (Washington DC: 2013). Retrieved from: <http://www.newamerica.net/sites/newamerica.net/files/policydocs/Improving%20Gainful%20Employment%20FINAL.pdf>.
32. U.S. Department of Education *Negotiated Rulemaking 2013-2014 -- Gainful Employment*. (Washington DC: 2013) Retrieved from: <http://www2.ed.gov/policy/highered/reg/hearulemaking/2012/gainfulemployment.html>.
33. IHEP calculations based on the U.S. Department of Education *Negotiated Rulemaking for Higher Education 2009-10: Data Used to Model the Effects of the Program Integrity (Gainful Employment) Notice of Proposed Rulemaking* (Washington DC: 2010). Repayment Rate calculations include all institutions, including those not subject to GE regulations. FAQs about these repayment rate data are available here: <http://www2.ed.gov/policy/highered/reg/hearulemaking/2009/ge-repayment-faq.pdf>.
34. Gross, et al. "What Matters in Student Loan Default: A Review of the Research Literature." *Journal of Student Financial Aid*, 19-29.
35. In the 2011 Gainful Employment rule, three percent of loan balances could count as "in repayment," even if they were negatively amortizing under a repayment plan based on income. For more on the relationship between repayment plans based on income and repayment rates, see: Ben Miller "Do Income-Based Payment Plans Really Ruin Repayment Rates?" New America Foundation (Washington DC: 2013) Retrieved from: <http://inthe tank.newamerica.net/blog/2013/12/do-income-based-payment-plans-really-ruin-repayment-rates>
36. Ben Miller, "Gainful Employment Liveblog Session 2: Day 1." New America Foundation (Washington DC: 2013). Retrieved from: <http://www.edcentral.org/gainful-employment-liveblog-session-2-day-1/>

37. According to NASFAA, unless institutions have discretion over borrowing levels, the threshold would need to account for some IBR loans negatively amortizing through no fault of the school.
38. The concept of a repayment progress ratio arose from discussions between IHEP and Mark Kantrowitz, senior vice president and publisher of Edvisors Network.
39. Repayment progress measures also could be used to quantify the amount that institutions would need to contribute to a risk-sharing scheme. See the more detailed discussion of risk sharing in auto-IBR in a subsequent section of this paper.
40. For more detail on data availability, see M. Voight, A. Long, M. Huelsman, J. Engle "Mapping the Postsecondary Data Domain: Problems and Possibilities." Institute for Higher Education Policy (Washington DC: 2014) Retrieved from: http://www.ihep.org/assets/files/publications/M-R/mapping_postsecondary_data_part_1_final_march_2014-v2.pdf.
41. Gross, et al. "What Matters in Student Loan Default: A Review of the Research Literature." *Journal of Student Financial Aid*, 19-29.
42. For detailed recommendations on improvements to IPEDS Outcome Measures, see the Institute for Higher Education Policy's November 2013 comments to the U.S. Department of Education on IPEDS outcome measures: http://www.ihep.org/assets/files/radd/comment_on_ipeds_outcome_measures.pdf
43. Institute for Higher Education Policy and *Excelencia* in Education, "Student Aversion to Borrowing: Who Borrows and Who Doesn't." (Washington DC: 2008). Retrieved from: <http://www.ihep.org/assets/files/publications/s-z/studentaversiontoborrowing.pdf>; Pamela Burdman, "The Student Debt Dilemma: Debt Aversion as a Barrier to College Access." Project on Student Debt, The Institute for College Access and Success (Berkeley, CA: 2005). Retrieved from: <http://cshe.berkeley.edu/publications/docs/ROP.Burdman.13.05.pdf>; National Center for Educational Statistics (NCES), "Borrowing at the Maximum: Undergraduate Stafford Loan Borrowers 2007-2008," (Washington DC: October 2011). <http://nces.ed.gov/pubs2012/2012161.pdf>.
44. While this measure is a proxy for the percent of the student population that is low-income, it is an imperfect measure of the overall income distribution because not all low-income students apply for or receive Pell Grants, particularly at low-price institutions such as community colleges. Alternative metrics (e.g., income ranges rather than financial aid status) would require additional data collection by institutions.
45. IHEP calculations using College Board *Trends in Student Aid 2013* (New York: 2013). Tables 6a and 6b Retrieved from: <http://trends.collegeboard.org/student-aid/figures-tables/loans#StudentLoans>.
46. Schools could theoretically still participate in campus-based aid programs even when facing sanctions on grant and loan programs for high CDRs.
47. 2013 was also the first year schools were subject to action using three-year default rate calculations. Schools with a three-year default rate of 30 percent or more must establish a default prevention task force to create a default prevention plan. Federal Student Aid, U.S. Department of Education "Two-Year Official Cohort Default Rates for Schools" (Washington DC: 2013). Retrieved from: <http://www.ifap.ed.gov/eannouncements/attachments/2013OfficialFY112YRCDRBriefing.pdf>; Rachel Fishman, "Shape Up or Lose Out:

- The 218 Institutions that Must Develop Default Prevention Plans” New America Foundation, October 2, 2012). Retrieved from: http://higheredwatch.newamerica.net/blogposts/2012/shape_up_or_ship_out_the_218_institutions_that_must_develop_default_prevention_plans-.
48. The Institute for College Access and Success (TICAS), “Aligning the Ends and the Means: How to Improve Federal Student Aid and Increase College Access and Success.” (Berkeley CA: 2013) p.40, Retrieved from: http://projectonstudentdebt.org/files/pub/TICAS_RADD_White_Paper.pdf.
49. *Protect Student Borrowers Act – S. 1873*. (2013). 113th U.S. Congress. Retrieved from: <http://beta.congress.gov/bill/113th-congress/senate-bill/1873>.
50. Under the Federal Family Education Loan (FFEL) Program, lenders can recover a substantial portion of the outstanding loan balance when a borrower defaults on his or her FFEL loan by filing a claim with a guarantee agency, which reimburses the lender for the loss. The Department of Education then reimburses guarantee agencies in an amount based on the guarantee agency’s default rate, with high default rate agencies receiving smaller reimbursement from the Department of Education. If an agency’s default rate is below 5 percent, they are reimbursed at 95 percent of the costs; if the rate is 5 percent or higher but lower than 9 percent, they are reimbursed at 85 percent; and if the rate is 9 percent or higher, they are reimbursed at 75 percent. *34 CFR 682.404 - Federal Reinsurance Agreement. Title 34 - Education. Subtitle B - Regulations of the Offices of the Department of Education.* Retrieved from: <http://www.gpo.gov/fdsys/pkg/CFR-2012-title34-vol4/xml/CFR-2012-title34-vol4-sec682-404.xml>
51. Because state policies largely impact prices at public institutions, states will need to be involved with helping public institutions meet accountability benchmarks.
52. Miller, “New Gainful Employment Language is Out and it’s Tougher Than Before.” Washington, DC: New America Foundation, November 11, 2013). Retrieved from: <http://www.edcentral.org/ed-may-have-just-released-the-strongest-gainful-employment-proposal-yet/>.
53. Alternately, NASFAA has suggested that institutions be allowed to use discretion to restrict student borrowing.