NASFAA ISSUE BRIEF
INSTITUTIONAL RISK-SHARING

MAY 2018

KEY TAKEAWAYS

1. LAWMAKERS SHOULD DESIGN A RISK-SHARING SYSTEM THAT ENCOURAGES INSTITUTIONS TO CONTINUE TO COMMIT RESOURCES TO UNDERSERVED STUDENTS.
2. INSTITUTIONS ALREADY TAKE ON SIGNIFICANT RISK WHEN UTILIZING SCARCE RESOURCES ON STUDENTS WHO HAVE BEEN DEEMED AT-RISK.
3. THE CAMPUS-BASED PROGRAMS ARE AN EFFECTIVE, SELF-SUFFICIENT EXAMPLE OF SKIN-IN-THE-GAME PROGRAMS THAT HELP MILLIONS OF STUDENTS EACH YEAR. LAWMAKERS SHOULD THINK ABOUT THE VALUE OF THESE PROGRAMS AND THE INHERENT RISK-SHARING THEIR STRUCTURE PROVIDES.

SHARING THE RISK IN HIGHER EDUCATION

As Congress and the higher education community work toward the reauthorization of the Higher Education Act (HEA), broad themes and proposals have emerged. One underlying concept is accountability, with a particular focus on the federal government and institutions of higher education sharing the "risk" in the federal student aid programs. A number of proposals have sought to tie institutions more closely to the loan repayment success of their former students, such as by requiring institutions to pay back a share of defaults by former students.

> *"We are concerned that the emphasis on risk-sharing* ***does not take into account the responsibilities that institutions who enroll at-risk students already assume"***

Incentivizing creative and effective ways to improve success and completion is a positive step—far preferable to negative and punitive measures, such as monetary fines. However, we are concerned that the emphasis on risk-sharing, as shown in proposals thus far, does not take into account the responsibilities that institutions who enroll at-risk students already assume, and that the risk-sharing measures proposed to date would provide more disincentives than incentives to serve these students.

While policymakers continue to emphasize the need for additional "skin-in-the-game" for institutions, many fail to recognize that schools already take on significant risk when dedicating scarce resources to students who have been deemed at-risk. Institutions admit at-risk students and provide remediation for students who need extra investment to benefit from higher education. In addition, colleges and universities provide—whenever possible—generous grant aid and participate in the campus-based aid programs, which entail risk-sharing in the form of institutional contributions and administrative expenses.

> *"Institutions have a vested interest in the success of their graduates,* ***but to tie an institution's eligibility for federal aid dollars to the repayment behavior of its former students can be problematic."***

Institutions have a vested interest in the success of their graduates, but to tie an institution's eligibility for federal aid dollars to the repayment behavior of its former students can be problematic. Some institutions, particularly community colleges, have "open enrollment" policies and do not select which students are admitted. Their mission is to serve their communities by providing unconditional access, and affording support services to students with insufficient academic preparation. At all institutions there can be many reasons why a student leaves school, many times having nothing to do with their experience with the institution and more to do with external factors in their lives. Not having a degree significantly increases the chances of repayment difficulty. Further, once a student leaves an institution, schools have little influence on the actions or inactions a borrower takes regarding repayment, including the relationship between a loan servicer and borrower.

In sum, what is lost and overlooked in the conversation about risk-sharing is that many schools already assume risk by committing seats and resources to at-risk populations. Lower completion/graduation rates, higher need for preparatory coursework, more personal attention, more need for all forms of aid (including loans that may increase the school's default rates), and loss of revenue if a student drops out are all existing risk factors that schools assume.

WHAT CONGRESS CAN DO:

Consider the impacts of poorly designed risk-sharing models on low-income students.

*"**A poorly designed risk-sharing system could increase the number of institutions (most likely community colleges) that choose not to participate in the federal loan programs,** as some institutions have already chosen to do since high cohort default rates (CDR) can put institutions at risk for losing all federal student aid funding."*

A poorly designed risk-sharing system could increase the number of institutions (most likely community colleges) that choose not to participate in the federal loan programs, as some institutions have already chosen to do since high cohort default rates (CDR) can put institutions at risk for losing all federal student aid funding. This could result in reduced access for students and/or a greater reliance on private borrowing where consumer protections are inconsistent and borrowing is credit-based thereby further restricting access. Even worse, schools that have traditionally served at-risk students may choose to admit less-risky students, which would have a devastating impact on access. Instead, Congress should consider "carrot" versus "stick" approaches to accountability if developing new models. These approaches should also utilize "input-adjusted metrics"; metrics that take into account inputs such as student risk level, when evaluating the outcome.

Provide institutions with the tools to curb student indebtedness.

*"By enhancing a school's authority to limit excessive loan borrowing or require additional counseling, **schools can better serve their students and mitigate risk to the federal government** in the federal student loan programs."*

As it stands now, institutions have little control over the borrowing behavior of their students, even though they are held responsible for their cohort default rates (CDR). Financial aid administrators want to be good stewards of federal funds, but more importantly, they want to ensure their students avoid accruing unnecessary or excessive debt and are able to repay their loans. Because of the entitlement nature of the Direct Loan program, a school cannot impose across-the-board restrictions on borrowing institution-wide or even by program, enrollment status, dependency status, or any other parameters. On a case-by-case basis a school can deny a loan to a student, but financial aid offices are reluctant to exercise this authority to deny or restrict borrowing because they may be subject to legal action. Furthermore, institutions do not even have the authority to require additional loan counseling or documentation supporting a request for loan funds. Providing institutional authority to mandate additional counseling allows institutions to tailor counseling requirements to the unique characteristics of their students. By enhancing a school's authority to limit excessive loan borrowing or require additional counseling, schools can better serve their students and mitigate risk to the federal government in the federal student loan programs.

Support or Model the Campus-Based Aid Programs.

*"Calls for consolidation and elimination of some of the campus-based aid programs **miss the inherent risk-sharing components of the campus-based aid programs."***

Under the three federal campus-based aid programs, which include the Federal Work-Study (FWS) Program, the Federal Supplemental Educational Opportunity Grant (FSEOG) Program, and the soon-to-expire Federal Perkins Loan Program, institutions match at least one-third of federal contributions they receive with their own funds. These programs stretch federal investment further and represent true risk-sharing in that institutions put their own dollars on the line to support needy students. Over the years, funding for these programs has remained relatively flat as the cost of higher education increases. Calls for consolidation and elimination of some of the campus-based aid programs miss the inherent risk-sharing components of the campus-based aid programs. At the very least, campus-based programs provide a good model for risk-sharing proposals.

NASFAA RESOURCES

Sen. Alexander White paper on Accountability and NASFAA Reply

Sen. Lamar Alexander's (R-TN) February 2018 accountability white paper proposes eliminating three key federal accountability measures: the cohort default rate, the 90/10 rule, and gainful employment. While each was created with the intent to protect student and taxpayer money, according to the paper, each could be improved to better measure student success in repaying loans and educational quality. The paper also suggested replacing the cohort default rate with a programmatic-level loan repayment rate, which Alexander said could provide a more accurate representation of overall progress toward student loan repayment.

In response, NASFAA outlined its principles on accountability in a letter to the Senator:

1. Congress should acknowledge, and try to work within, existing institutional risk- sharing.
2. Congress should give great attention to the potential unintended consequences on the most vulnerable students.
3. Congress should consider a "carrot" versus "stick" approach to accountability.

2015 Sen. Alexander White Paper on Risk-Sharing and NASFAA Reply

The second of three HEA reauthorization white papers released by Sen. Lamar Alexander in 2015 calls for a realignment and improvement of federal incentives "so that colleges and universities have a stronger vested interest and more responsibility in reducing excessive student borrowing and prioritizing higher levels of student success and completion." In response, NASFAA outlined its priorities and perspectives on accountability in a letter to the Senator.

NASFAA Editorial: Calls for 'Skin in the Game' in Higher Education Ignore an Existing, Effective Program

NASFAA President Justin Draeger published an op-ed in The Hill newspaper on legislative proposals around accountability and the inherent risk-sharing components of the Federal Perkins Loan Program.

NOTABLE RISK-SHARING LEGISLATION

Several notable pieces of legislation have been introduced that seek to address accountability and risk-sharing. The quality and accountability page of NASFAA's Legislative Tracker includes summaries of these legislative proposals and others that look to hold institutions or individuals responsible for their actions or performance, including several risk-sharing proposals.

- PROSPER Act
- Protect Student Borrowers Act
- Student Protection and Success Act
- ASPIRE Act

OTHER RISK-SHARING RESOURCES

Designing Higher Education Risk-Sharing Proposals (summary of several proposals), Published by Center for American Progress on 5/22/17

Risk-Sharing Proposals Would Have Negative Consequences for Student and Institutions, Published by American Council on Education on 4/29/15

Proposing a Federal Risk-Sharing Policy by Robert Kelchen, Published by Lumina Foundation on 9/9/15

Share the Risk on Student Loans by Andrew Kelly, Published by American Enterprise Institute on 9/7/16

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