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BACKGROUNDER

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Americans Deserve Bold Policy Reforms in the Reauthorization of the Higher Education Act

Mary Clare Amselem

KEY TAKEAWAYS

The federal government has a near-monopoly over the student loan market, which has distorted the market of tuition prices.

The Congressional Budget Office determined that loan forgiveness programs are expected to cost taxpayers $108 billion over the next 10 years.

In order to reverse the trend of perpetually increasing college tuition, policymakers must first address the problematic federal aid programs.

The Higher Education Act (HEA) of 1965 was meant to unlock the secret to upward economic mobility by granting more Americans the chance to obtain a college degree. Upon signing the HEA, President Lyndon Johnson remarked,

> The President's signature upon this legislation passed by this Congress will swing open a new door for the young people of America. For them, and for this entire land of ours, it is the most important door that will ever open—the door to education. And this legislation is the key which unlocks it.[1]

President Johnson's remarks were aspirational but failed to recognize how this dramatic shift in federal higher education policy would affect generations to come. Today the federal government originates or distributes roughly 89 percent of all student loans

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through its various loan programs.[2] The federal government also distributes Pell Grants, which cost Americans $28.2 billion in 2017–2018.[3] This largesse has meant that the federal government has a near monopoly over the student loan market, which has distorted the market of tuition prices. Evidence continues to mount that federally subsidized student loans have enabled colleges and universities to raise their tuition prices without fear of losing students.

Until Congress addresses the problem of tuition inflation fueled by the overly generous federal student aid programs, skyrocketing college cost increases will continue unabated. Student loan delinquencies reached record highs of $166.4 billion last year.[4] According to Bloomberg, "Delinquencies continued to climb even as the unemployment rate fell below 4 percent, suggesting the strong U.S. job market hasn't generated enough wage growth to help some people manage their outstanding obligations."[5] Indeed, for too many students, college fails to equip them with the skills and knowledge needed to be successful in the job market—despite saddling them with considerable debt burdens, leaving students with insufficient resources to pay back American taxpayers. As Congress considers reauthorization of the Higher Education Act, measures to curb federal spending and subsidies must be included in order to lower costs for students and unburden American taxpayers.

Debt Burdens Continue to Mount

Since 2010, the federal government has originated and serviced the vast majority of student loans. Today the federal government originates approximately 89 percent of all student loans, meaning taxpayers, for their part, bear the burden of paying for student loan defaults when they occur. Nearly 20 percent of borrowers enrolled in a standard 10-year loan repayment plan are in delinquency,[6] and 10.8 percent of the 2015 student borrow cohort—representing some 531,000 borrowers—defaulted on their student loans.[7] An analysis by the Brookings Institution found that, if current trends continue, nearly 40 percent of student loan borrowers are expected to default by 2023.[8]

These debt burdens do not just affect young borrowers. Americans over 60 years old owe $86 billion in student loan debt cumulatively, either because they took out Parent PLUS loans for their children to attend college and have not yet repaid them or because they took out loans for themselves to go back to school.[9] Student loan debt among Americans in their sixties increased 161 percent from 2010 through 2017, with older borrowers bearing an average debt burden of $33,800 according to an analysis by the *Wall Street Journal*.[10] More than 40,000 of those borrowers had their social security benefits or tax refunds garnished by the federal government in 2015 due to student loan defaults, according to the same source.[11]

The Bennett Hypothesis, which argues that easy access to federal loans encourages colleges to raise tuition, can hardly be characterized as a hypothesis in light of recent studies. In 2017, economists from the Federal Reserve Bank of New York found that every dollar that an institution receives in subsidized federal loans led to an estimated 58 cent increase in the sticker price of tuition. Similarly, every dollar an institution received in Pell Grants led to a tuition increase of 38 cents.[12] Additionally, in 2014, Cellini and Gordin found that tuition at for-profit schools that participate in federal aid programs is 78 percent higher than comparable programs that do not accept federal aid.[13] In order to reverse the trend of perpetually increasing college tuition, policymakers must first address the problematic federal aid programs.

The Prosper Act: Necessary Reforms—and A Missed Opportunity

In December 2017, the House Committee on Education and the Workforce introduced the Promoting Real Opportunity, Success, and Prosperity through Education Reform (PROSPER) Act. The Prosper Act proposed a mix of substantive reforms with a few reforms that missed the mark. Notably, the Prosper Act proposed eliminating loan-forgiveness programs. Currently, students who have an outstanding balance on their loan after 20 years of payments can have the remainder of their balance discharged. Public service employees are eligible to have their loans discharged after just 10 years of payments. Although student loans should not mean a life sentence of monthly payments, simply discharging such loans and passing that cost to American taxpayers does not solve the issue. The Congressional Budget Office determined that loan-forgiveness programs are expected to cost taxpayers $108 billion over the next 10 years.[14] Proposed elimination of loan forgiveness in PROSPER is a much-needed policy reform that should be mirrored in any HEA reauthorization proposal.

Although the Prosper Act would have ended some loan forgiveness, it went in the wrong direction on overall lending by *raising* lending caps on the federal loan programs. Under current law, dependent undergraduate students can borrow $31,000, while the Prosper Act proposed that dependent undergraduates be able to borrow $39,000.

Nonetheless, the Prosper Act wisely would have eliminated the PLUS loan program, which allows parents of undergraduate students and graduate students to borrow up to the cost of attendance. However, this proposal would have raised the amount graduate students can borrow under the graduate Stafford program, mitigating much of the positive step in the right direction of eliminating PLUS.

Signals from the Senate

Senator Lamar Alexander (R–TN), who chairs the Senate Committee on Health, Education, Labor and Pensions, has indicated several policy priorities he wishes to address as Congress considers the reauthorization of the Higher Education Act. In a speech at the American Enterprise Institute, Senator Alexander outlined three top policy priorities:

1. **Simplifying the FAFSA.** Students must complete the Free Application for Federal Student Aid (FAFSA) in order to apply for federal loans or grants to attend college. Politicians and students alike have often bemoaned the long and complex form and even called its complexity a barrier to college access. The Urban Institute's Kim Reuben stated in a 2017 congressional testimony,

   > Further simplification is a low-cost way of increasing the effectiveness of the federal commitment to broadening educational opportunities. And it is especially important for low-income students, who are least likely to attend college and who could benefit the most from an improved student aid application system.[15]

   While it could be the case that the FAFSA application may deter students from pursuing available federal loans and grants, encouraging more students to partake in the federal aid programs should not be a priority for conservative lawmakers. Reinstating the private lending market and diversifying higher education options could unlock the door to career access for all Americans. Simplifying the FAFSA would certainly help streamline the application portion of the federal aid program; however, the inefficient bureaucracy surrounding the federal loan program extends far beyond the FAFSA. Policymakers should focus on solving the college affordability crisis and career readiness—deeper systemic issues—rather than tinkering around the edges of the paperwork required to apply for aid.

2. **Consolidating Loan-Repayment Options.** Senator Alexander has also proposed simplifying the current loan-repayment options. Indeed, many students find it difficult to navigate what their repayment options are once they are in the workforce. Students currently have nine repayment options to choose from, which Senator Alexander proposes to consolidate into just two—one income-based repayment plan and one standard 10-year repayment plan with equal monthly payments, which he compares to a mortgage. Streamlining the loan-repayment options could certainly help address student loan repayment issues. However, it is critical that policymakers couple this consolidation with the elimination of loan-forgiveness programs. Hardworking American taxpayers should not be left with the tab after students qualify for loan forgiveness.

3. **Establishing a New Accountability System for Colleges.** The third component of Senator Alexander's priorities for reauthorization of the HEA is to create a new system to hold colleges accountable for student loan repayment rates. According to *Inside Higher Ed*, "Rather than measuring a ratio of students' debt to income, as gainful employment did, Alexander's proposal would measure borrowers' progress repaying their debt. And it would apply to every program at every college, regardless of the type of institution."[16] Gainful employment was indeed a poor accountability measure that singled out one sector—the proprietary college sector—penalizing for-profit colleges while ignoring bad outcomes in the rest of the sector.

If policymakers are to place regulations on colleges, they should indeed be sector-neutral as Senator Alexander suggests. However, student loan repayment rates are merely one piece of the puzzle needed to determine whether a college is serving students well. A better approach to increasing accountability for colleges is to reduce federal lending, reform the accreditation system, and highlight schools that are innovating in areas such as income-share agreements.

What Should Be Included

Policymakers should pursue bold reforms to bring financial solvency back to higher education policy. The reauthorization of the Higher Education Act presents an opportunity to reform the federal student aid program as well as the inefficient accreditation system.

Stricter Lending Caps on Federal Student Loans. In order to reverse the detrimental trend of tuition inflation, Congress must reduce the amount that students may borrow to attend college. The federal government now originates or distributes 89 percent of all student aid. The private market has been all but eliminated from the marketplace, substantially raising taxpayer exposure due to defaults and generous loan-forgiveness policies. Easy access to federal loans has encouraged colleges and universities to raise tuition prices, confident that students will be able to make up the difference through federal aid programs. Placing an annual per student cap on federal lending at $7,500 and a lifetime cap of $40,000 (inclusive of undergraduate and graduate school borrowing) would save taxpayers an estimated *$33 billion* over the next 10 years.[17] This would also achieve the goal of disincentivizing colleges and universities from raising their cost of attendance, significantly reduce strain on federal lending programs, and allow private lenders to once again serve students in a competitive marketplace.

Elimination of Loan Forgiveness. Federal loan forgiveness programs are simply a backdoor pathway to "free college." Although many students do successfully pay down their debts, the current system would enable certain borrowers to spend 20 years paying off the *interest* on their loans (while never paying a dollar down on the principle) before the balance is forgiven. For public service employees, they can qualify to have their loans forgiven after just 10 years of payments, leaving American taxpayers (the majority of whom did not attend college) to absorb the remaining loan balance. This is a wildly inefficient system that simply places a band-aid on the student loan problem. Instead, legislative reforms should address the cost of college at its source—easy access to federal student loans. The aforementioned reforms to the federal aid system would improve college affordability and encourage students and families to make the best financial decisions for them.

Accreditation Reform. In addition to placing downward pressure on tuition inflation, HEA reauthorization should reform the accreditation system to encourage innovative higher education models to compete with the status quo. In today's highly competitive and diverse job market, Americans are doing themselves a disservice by syphoning all future employees through the same bachelor's degree track. Instead, high school graduates should have access to a variety of educational options to help them achieve career success. For many, a bachelor's degree is a great way to experiment with different courses of study and achieve a well-rounded education. But for students who simply want to make a cost-effective decision and learn exactly the skills they need in a reasonable amount of time, high-quality vocational and technical training programs should be readily available.

Unfortunately, our current accreditation system offers inadequate quality assurance for students and makes it extremely difficult for start-up higher educational models to gain accreditation and compete with well-established universities. A meaningful step forward would be to allow states, rather than the Department of Education, to determine who can be an accreditor. This would enable the business community or other entities with industry-specific knowledge to create a relationship with universities and offer their stamp of approval on curricula or programs.

At a time when many college graduates of accredited universities find themselves lost in the job market with skills that do not match the needs of the business community, a pipeline between education and work would make a significant difference. For example, the Higher Education Reform and Opportunity Act would break the link between the *de facto* federal accreditation regime and student aid. It would enable students to take piecemeal classes and courses of study and to customize their higher education experience.

Income-Share Agreements. Americans want to know that colleges and universities have some "skin in the game"—and bear some responsibility for the consequence of their performance. Income-share agreements (ISAs) increase college accountability and add much needed transparency for students.[18] If a student enters into an ISA with either a private entity or a school itself, the student does not pay for the cost of their education up front, but rather agrees to pay back a percentage of their future earnings.

When the school is the lender, as is the case with Purdue University, for example, the school is heavily motivated to prepare students for a profitable post-graduation career. Additionally, students enter into higher education with a very good idea of what their starting salaries will be. This information could help students greatly at a time when graduates are struggling with debt and enrolling in majors such as women's studies or sociology—which have a very poor return on investment.[19]

It Is Time for Meaningful Reform

American students and taxpayers deserve bold reforms that will dig our country out of the $1.5 trillion student debt hole. While streamlining the student aid program by simplifying the FAFSA and consolidating repayment options will make it easier to borrow more money from the federal loan system, these reforms ignore the overwhelming problem of runaway tuition inflation.

Shrinking the size of the federal loan programs should be a top priority for policymakers, along with inserting alternative accreditation options into the higher education sphere. The American economy would vastly benefit from meaningful reforms that bring college costs down while creating more efficient pathways to career success.

Mary Clare Amselem is a Policy Analyst in the Center for Education Policy, of the Institute for Family, Community, and Opportunity, at The Heritage Foundation.

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