THIRD WAY

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Giving Students a Better Shot at Graduating than Defaulting

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Would you attend a college or university if you knew you would have a better chance at defaulting on your student loans than graduating? Probably not. The number one reason students go to college is to get a job so they can earn a stable and secure life.[1] They enroll for the opportunity to reap the benefits of higher education—better wages, greater economic stability, and as research has even found, overall improved health outcomes.[2] They expect to not only graduate but to also gain the skills they need to get a good paying job that will provide them a return on their investment in higher education

Students who borrow to attend college certainly do not expect to default on their loans, a situation that can lead to long-term financial distress. Yet each year, too many students find themselves in the worst-case scenario: they take out loans to start college, but never finish—leaving them degreeless and in debt. And while graduation doesn't always guarantee financial success—as some poor-quality programs could give out degrees that mean little in the job market—data shows that students who enter college but do not graduate are three times more likely than graduates to default on their student loans. [3] Yet institutions that consistently leave their students with a better chance of defaulting than graduating bear no consequence for those poor outcomes—despite the fact that these same schools collect huge checks from taxpayer-funded grants and loans every year.

The Problem

While most students enroll in higher education for the economic benefits, far too many never see such returns. Recent Outcomes Measure federal survey data shows that 55% of all students who enrolled in higher education failed to graduate from that institution within eight years. [4] Even worse, hundreds of thousands of those who borrow to attend college end up defaulting on their loans soon after they leave. Today, there are approximately eight million student loan borrowers in default—with two-thirds of defaulters owing less than $10,000. [5] This is in large part because those defaulters weren't in school for very long—likely dropping out before they could accumulate greater loads of student debt. Yet current federal policy does nothing to improve *either* of these outcomes, including both a high number of defaults or dropouts.

CDR Only Catches the Worst of the Worst.

Congress created the Cohort Default Rate (CDR) in the 1980s as a tool to combat rising student loan defaults. The CDR is calculated as the percentage of an institution's student borrowers who default on their student loans within three years of entering repayment. Congress intended this metric to help ensure that taxpayer dollars were not being used at institutions where too many students have trouble repaying their loans after they leave. Currently, there are two situations in which an institution's CDR could cause them to lose federal funding:

1. The institution has a CDR of 30% or higher for three consecutive years; or

2. The institution has a CDR over 40% in any one year. [6]

Between these two situations, only 10 institutions failed this metric in the most recent cohort—and only 11 institutions have lost federal funding due to this sanction since 1999. [7] And CDR does nothing to catch millions of students who may not be in default but are unable to actually begin paying down their loans. The most recent data shows that over 500 institutions left more than three-quarters of their students unable to pay down even $1 of their loan principal within three years of leaving. [8]

There is No Federal Accountability for College Completion.

Under current law, despite the nearly $130 billion dollars that goes to institutions through taxpayer-funded grants and loans each year, there are no real sanctions or incentives for colleges to improve their retention and graduation rates. The closest thing we have in place today is the accreditation process. However, the current process focuses more on inputs than outputs—meaning that accreditors do not even consider graduation rates as a measure of success when providing colleges with their seal of approval. [9] That might explain why 140 institutions remain accredited even though they have graduation rates lower than 10%. [10] And we currently do nothing at a federal level to encourage institutions with low graduation rates to improve.

An analysis of student outcomes by institution reveals that last year alone, there were 64 institutions where students had an equal or greater chance of entering default than leaving with a certificate or degree. [11] Yet most of these schools would not be penalized by either their accreditor or CDR as is.

The Solution

To address these two problems, we propose that the federal government add a third prong to CDR that would cause an institution to lose access to federal funding: if an institution has a CDR that is greater than their graduation rate, then they should lose access to federal grants and loans. [12]

To determine a school's eligibility to remain in the Title IV student aid program under this new prong, the federal government would need to compare an institution's graduation rate with their current CDR. We would propose using the more generous Outcomes Measures graduation rate. This rate measures the percentage of students that graduate from an institution within eight years, including part-time and transfer students, and excludes "transfer out" students from the calculation altogether rather than counting them as non-graduates. Like the first prong of the existing CDR test, an institution would have three years to improve this measure before facing full sanctions. During this window, institutions facing ineligibility would be able to improve their status by either increasing their graduation rates *or* lowering their cohort default rates.

Critiques and Responses

This measurement may disproportionately affect community colleges, which serve a higher-proportion of low-income and non-traditional students.

To alleviate the impact on any one sector, this measure would use the most generous graduation rate possible for institutions that may have a large number of low-income or transfer students by excluding the transfer-out population and including the success of part-time and transfer students rather than the typical first-time, full-time cohort. This graduation rate also measures completion at eight years—meaning that community colleges would be measured on their success in helping students earn a two-year degree within 400% of the expected time. Additionally, we use multiple measures to encourage improvement in both graduation and default rates, giving institutions two opportunities to improve in order to stay in compliance. However, it is hard to argue that an institution of any kind (including a community college) where students are more likely to default than graduate is serving its students well, especially the students who are most at risk.

This wouldn't fix the fact that schools can game the Cohort Default Rate.

Currently, the CDR fails to capture students who may not be in default but struggle to repay their loans. This is because income-driven repayment plans—which are important to protect student borrowers from paying more than they are earning—allow borrowers to pay $0 towards their loans but remain out of default. In addition, borrowers can delay payment through deferment or forbearance, allowing students with difficulty repaying their loans to be excluded from any CDR calculation. [13] As a result, institutions have been able to game the current CDR metric by putting students into deferment or forbearance for a designated time in order to skirt the rule's sanctions. In fact, a recent study by the Government Accountability Office found that default consultants routinely encouraged students to enter forbearance over other more favorable repayment plans as a way to keep the institutions from failing CDR. [14] To mitigate this concern, Congress could put in place a process to review institutions with high rates of students entering deferment or forbearance to ensure honest interactions with students. In addition, we support policymakers moving toward a Cohort Repayment Rate, which would measure the number of students unable to begin repayment on their loans as opposed to looking only at students that have defaulted. [15]

Conclusion

When a student enrolls in college, they should have a better chance of getting a degree than a loan that ends up in default. Encouraging institutions to raise both their graduation rates and default rates is a win-win for students, especially as we know that students who don't graduate are three times as likely to default on their loans. [16] As Congress moves to reauthorize the *Higher Education Act*, they should protect students from attending institutions that make will them worse off. And a simple test for doing so: require institutions to have more of their students graduate than default.

ENDNOTES

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11. Author's analysis of Cohort Default Rates Outcomes Measures graduation rates. In addition to first-time, full-time students, this graduation rate includes part-time students and non-first-time students who transfer in to an institution. This calculation also excludes those students who transfer out of an institution rather than counting them as non-graduates.

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