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Revisiting the College Default Rate

Working Group Initiative held May 1, 2000 Southern Illinois University Carbondale

Presented by the Public Policy Institute

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The Challenge

Low-income people of all backgrounds – including students – live on the financial edge. We frequently worsen their financial problems by forcing them to take loans for an education. We know that a significant percentage of people in this group will face critical problems of a personal or family nature, such as health care, either as students or in the period immediately following their schooling. These problems often cause students to drop out and ex-students to default on their loans. In admitting low-income students who have the needed aptitude for education, we cannot identify specific individuals who will have critical personal problems, though we know that a significant percentage of the low-income group will, and that pushes up dropout rates and defaults. The only way for a school to avoid this is to deny admission to low-income students. There are no public announcements of such a policy, but when schools shift their location or their emphasis from the central city to the suburbs, this is part of a pattern that a well-intentioned but flawed policy encourages.

A decade ago the federal student loan program was a program in crisis. Years of neglect at the Department of Education had loosened the administrative and fiscal controls. The most obvious barometer of a problem was the soaring student loan default rate and the costs that the federal government incurred to pay off defaulted student loans.

Congress and the Executive Branch took strong action. A student loan default rate cut-off was instituted. Schools with a default rate above a specified threshold were eliminated from the federal student aid program. One whole class of schools – correspondence schools – was eliminated from eligibility. Standards to participate in the loan program – academic and financial – were tightened.

The harsh medicine worked. During the same decade that the amount of money borrowed increased from 12 billion to 30 billion, the default rate fell. The amount spent by the federal government to pay off student loan defaults plummeted.

Today we face a different problem. Some schools, including excellent institutions that provide a high quality education, have found themselves losing federal student aid, or coming close to it, because of the mechanical application of student aid rules.

It is time for the federal government to revisit the default rate trigger issue and to look for ways to ensure

Paul Simon

that good schools that provide excellent education and training are not threatened by rules and regulations put in place to solve a problem that existed a decade ago. This is not to call for the opening of doors to shady schools. To the contrary – improved oversight of the program by the Department of Education has made it possible for us to think about ways to selectively loosen some of the restrictions put in place a decade ago without running the risk that the student loan default rate will, once again, spiral out of control.

The Recommendations

The following are recommendations of a small group assembled at Carbondale, Illinois, by the Southern Illinois University Public Policy Institute. A list of the participants follows the recommendations. Not every recommendation is necessarily supported by each of the participants nor by the groups or institutions with which they are affiliated.

Long-Term

- The shift from heavy reliance on student grants to heavy reliance on student loans needs to be reversed. Gradually increasing the Pell Grants is in the nation's interest and will lessen the prospect that students from low-income families will accumulate unmanageable debt. Increasing funding for Pell Grants will encourage more students from families of limited income to attend post-secondary institutions and remain in school through graduation. Lowering debt burden would also allow students to choose the lower-paying service professions. Congress should expand eligibility for Pell Grants to more students and increase the amounts of Pell Grants to fund a greater portion of the student's financial need.

- The Pell Grant should be shifted to a year-around program for students who pursue summer studies. The traditional student, ages 18 – 22, who takes the summer off is a shrinking segment of the post-secondary education student population. Frequently an older student or one from a low-income family wants to get through school quickly. That need should be accommodated. Students should not be required to assume a larger debt burden due to the unavailability of Pell Grants for the summer session. Congress should fund Pell Grants for any period of student attendance.

Andrew Sund and Cheryl Fields

- Eliminate the Pell Grant tie-in to the default rate cut-off. Schools need to provide Pell Grants to enable low-income students to attend and remain in school. The increased Pell Grant will be partially off-set by reduced loan subsidies and accelerated placement of the student into the workforce.

Short-Term

- If a school has 30% of its full time enrollment receiving a Pell grant and has a default rate of 33% or less, the school should be permitted to remain eligible for federal student aid provided it prepares and implements a default management plan satisfactory to the Secretary of Education and there are no outstanding audits or limit, suspend or termination agreements pending against the school.

"Bud" Blakey and William Gray

- Immediate research is needed assessing the total debt burden that students are assuming when they end their schooling and how that burden impacts a student's career choices. It should include a look at the amounts that students borrow by field of study and the burden this will impose on them in light of income they are likely to earn. This study should also look at successful repayment plans and the effectiveness of exit counseling. Congress needs to appropriate adequate funding to conduct this study authorized in part during the last reauthorization of the Higher Education Act. Results can be used to make necessary policy changes. Congress should authorize the study and appropriate funds for the study. The amount of funding needed for this research is a tiny fraction of one percent of what we now spend for student loans.
- At present, all student loan borrowers receive exit and entrance counseling to make certain that they understand the obligations they face by borrowing under the student loan program. Such counseling is often done in a routine fashion. The Department should conduct research into the most effective practices and should promulgate the results to campuses.
- The default rate threshold mechanism for continued eligibility for federal financial aid programs has served as a means for the Department of Education to eliminate low-quality schools from the federal programs, but it has also decreased educational opportunities for many students from low-income families. Good-quality schools have changed locations away from the inner cities and poor rural areas to avoid default rate problems that are inherent to serving at-risk populations. The Department of Education should explore means other than default rates to assess and enforce accountability for the quality of schools.
- Effectively informing the public of educational opportunities and particularly reaching the minority communities is a need. The Department of Education, schools and other agencies should improve communication to the public and more effectively utilize the media outlets that serve the minority communities, often composed of low-income families.
- Many students need advice after receiving loans. Involving people in the community to assist these students often can be helpful.
- Students should be given a sheet of recommendations to avoid financial difficulties. Having a bank account is one example of a recommendation. Students carrying cash are less likely to be cautious with the money than if the same amount is in a bank account.

Omer Waddles, Dr. Terry Hartle and Dr. Marshall Grigsby

- Financial counseling, including financial planning, budgeting and debt management should be provided to all students and families, and particularly to low-income students, before and during college and through repayment of student loans after leaving school. Financial counseling should include responsible credit card management, utilization of banking resources, savings and investments, as well as the traditional financial aid and student loan counseling. The banking industry and guarantee agencies as well as the Department of Education should be required to partner with schools to provide direct financial services to students and families including printed and web-based financial planning

William Carson

resources, and financial training for school personnel to develop counseling skills to assist students. Whenever possible, schools should follow through with students after they leave school — either upon graduation or when dropping out — to encourage debt payment and offer counsel and assistance when necessary.

- The Department of Education's "Plain Language" warning on student loan disclosure statements is not written in plain language. Improve the accurate but difficult to understand legalese.
- The Department of Education should examine the possibility of having training opportunities for student financial counselors in the area of debt management and debt counseling. The typical aid officer at traditional institutions does not have much understanding or training in this specialty area.

Pam Britton