Providing Quality Postsecondary Education: Access and Accountability
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Testimony
Mr. Chairman and Members of the Committee:

Thank you for allowing me the opportunity to testify regarding the federal role in promoting college access and success. Through the Higher Education Act, the federal government plays a critical role in making postsecondary education financially within reach for millions of Americans. But more than just serving individual students, the programs help to drive the economy. As Federal Reserve Chairman Alan Greenspan said in testimony last year, our versatile higher education system serves "the practical needs of the economy by teaching and training and, more significantly, by unleashing the creative thinking that moves our economy forward."

With some urgency, Chairman Greenspan called for a more aggressive effort to expand educational opportunity. "As history clearly shows, our economy is best served by full and vigorous engagement in the global economy. Consequently, we need to increase our efforts to ensure that as many of our citizens as possible have the opportunity to capture the benefits that flow from that engagement. . . [O]ne critical element in creating that opportunity is the provision of rigorous education and ongoing training to all members of our society. This proposal is not novel; it is, in fact, the strategy that we have followed successfully for most of the past century and a strategy that we now should embrace with renewed commitment."

More recently, Chairman Greenspan has also warned of the dangers of the large federal deficit. As I will testify today, this committee has the opportunity to address both of these critical economic concerns: to significantly expand Americans' opportunities for postsecondary education and training, and to do so without adding to the budget deficit.

The Debt Generation

Over the past 20 years, the way Americans pay for college has changed dramatically. A system once based primarily on subsidized tuition and need-based grants is now dominated by student loans. For students from all socioeconomic backgrounds, debt has become a primary method of financing higher education:

• Just 15 years ago, only one in six full-time freshmen at four-year public universities took out a federal student loan; now more than half do.

• By the time they graduate, nearly two-thirds of all undergraduate students have accumulated debt, up from less than one-half just seven years earlier.

• Between 1993 and 2000, the average student debt for recent graduates from four-year colleges increased by 60 percent, to $19,300; the proportion of parents taking out loans to help pay for their children's education also rose.

• In the baccalaureate graduating class of 2000, more than one-fourth had in excess of $25,000 in loans. That is triple the proportion just seven years earlier, when only seven percent carried that much debt (adjusted for inflation).

• Borrowers who go to graduate and professional school carry even larger debt loads. A 2002 Nellie Mae survey found average debt of $45,900; for those who attended law and medical schools, the average is $91,700.

Today's young adults are the first generation in American history to experience college debt on such a mass scale. How does this new reality affect the educational opportunities and outcomes that we want and need in this country?

At the Institute for College Access & Success, we have been exploring the perceptions that students, counselors, teachers, financial aid administrators, and education policy experts have about borrowing for college. We are finding an enormous amount of confusion and anxiety. It shows in the conflicting messages that people hear when they are thinking about continuing their education:

Message 1: Invest in yourself. "Student loans are a good investment. Your education will empower you to earn far more than you borrow."

Message 2: Protect yourself. "Student loans can destroy your life. If you default, your credit is ruined, and you can't get any more student aid. To avoid default, you might have to work two jobs, or forego the career you most want, just to keep up with your loan payments."

So, are student loans good, or bad? The real answer is, "it depends," which is why even college financial aid officials struggle with how to counsel students about loans. For example, Ohio State University has made a valiant effort with its financial counseling web site (http://sfa.osu.edu/basic/debt.asp). It provides tools for budgeting college costs and offers guidance for figuring out how much borrowing is too much.

The American Council on Education and others recommend that student loan repayments not exceed eight percent of a borrower's earnings. They call anything higher than 10 percent the "Red Zone"—the danger zone for default, diminished savings, and other risks associated with too much student debt.

But how many high school or even college students can predict with any level of certainty what job they are going to have, much less what their income is going to be? The only thing they can say for sure is that if they don't graduate, or they don't get the kind of job they want, or they don't get the salary they expect, then they risk defaulting

and undermining their own financial future and possibly their families' as well.

Some observers criticize families who are more reluctant to borrow for college than to take on other types of debt. After all, postsecondary training is an investment that pays off handsomely in future earnings. But there are understandable reasons for such reluctance. If you have a mortgage, then you have a house. If you have an auto loan, then you have a car. But if you have a student loan, you do not necessarily have the increased income that you need to pay it off. While education does boost earnings in society in general, there is much variation around that average. And you can't return your education to the store for a refund in order to pay off the loan.

Student loans do offer real opportunities for millions of students. But with the promise comes real peril as well. This reality affects the behaviors and attitudes of students and potential students and their families—and thus has an impact on our educational outcomes as a nation. For Americans from all backgrounds, the looming threat of high loan payments—the Red Zone—has potential negative effects well before high school and long after a borrower completes—or fails to complete—a postsecondary program. These effects include:

Diminished college access and¬ completion. Some students of limited means are extremely reluctant to take out loans. This leads them to forego college altogether, or to engage in behavior that reduces their chances of completing a degree (such as attending part-time, enrolling at less supportive institutions, or working excessively while in school).

Disincentive for service careers. Recent graduates who want to¬ go into teaching, social work, religious service, and other helping professions find that their college debt pushes them in other directions.

Delay of¬ marriage, family, and home ownership. Student loan debt makes it more difficult for young adults to afford a home mortgage. Borrowers also report that it has delayed their plans for marriage and children.

Reduced ability to save¬ for retirement—and for their own children's college education. Increasingly, borrowers are extending student loan repayment across 20 or even 30 years. This reduces their ability to save for their own retirement, and to help pay for their own children's higher education expenses.

In my testimony today I will focus mostly on how college students and potential college students and their families think about loans. I will touch briefly on some of the other key issues, and then turn to what can be done about the problems.

Aid, Loans and College-Going Behavior

"I didn't get any financial aid. I got a loan"

--Disappointed Student

One of the great attributes of our postsecondary education system is that there are so many different ways to enroll in so many different types of institutions. There are traditional residential colleges, commuter campuses, community colleges, career-focused night programs, intensive weekend courses, and on-line courses. This diverse array of options is a positive feature of our system. It means that people who would not enroll in one type of program have other options to consider. The problem is that financial considerations prevent too many students from choosing the approach that is the best fit for their qualifications, interests, and needs. This reduces their likelihood of enrolling in any program; and for those who do enroll, it diminishes their likelihood of success.

In the traditional model, high school graduates who cannot cover the full costs of college take loans and other aid, enroll full-time in a four-year school, and keep their work to less than 20 hours a week. By focusing on their studies, these students are the most likely to graduate and to play productive roles in the economy and as citizens. Research consistently shows this is the most certain route to significant upward mobility.

The image we like to have of our system is of the hard-working student from a tough background who leaps far beyond his parents' educational and income levels. But this American dream doesn't come true as often as it should. It is students from high-income families who are most likely to take the four-year-college route.

Set aside all of the students who drop out of high school, and set aside the high school graduates who are not qualified for college—two factors that disproportionately affect low-income families. There is still a large gap in college-going by family income. Among high school graduates who are from higher income families and are college-qualified, 83 percent enroll in four-year colleges. But among low-income families, only 52 percent enroll in four year colleges within two years of graduating high school.

Where do the other college-qualified low-income students go? Twenty-one percent enroll at community colleges and may be as successful as they would have been at a comparable four-year institution. But more of them—22 percent—do not enroll in any type of postsecondary program at all. The comparable figure for high-income recent high school graduates is only four percent. In other words, almost every college-qualified, high-income high school graduate enrolls within two years, while more than one in five qualified low-income students does not go at all.

For lower income students, affordability – perceived and actual – plays a major role in whether and where they go to college. It also affects how they approach their studies and, therefore, how likely they are to graduate. Research has found that if a young adult sees herself as a student, she is more likely to persist. And it is much more difficult to maintain that self-perception as a student if you are enrolled part-time while working, a pattern that is more common for students of modest means.

For full-time students, work is a factor, too. Up to around 15 hours a week, work is a

positive contribution to achievement and college completion. But much more than that and it becomes an impediment. Nearly a third of full-time dependent students work more than 20 hours a week on top of their schooling. The lower your income, the more likely you are to be in this group. Of these full-time and hard-at-work students, 60 percent did not take out a student loan. In other words, 60 percent could have reduced their work burden with a student loan, but chose not to. Should they be congratulated for their commitment? Or pitied because they are more likely to drop out, or graduate with lower grades than they are capable of? How many talented students turn away from tough majors like science and engineering because the courses don't leave enough time for the work hours required to pay the bills?

Financial aid is certainly not the only factor behind these gaps in the quality and intensity of enrollment between lower and higher income students. But it is a contributing factor. Here is a taste of what we are hearing from college officials in interviews conducted for an upcoming report by researcher Pamela Burdman:

"Parents are very leery about loans. Sometimes it filters down to a student. . . For some, it seems that they weren't optimistic about their future. It's more acceptable if you were going to borrow money to purchase a car. It's more tangible. It can get you back and forth to work. They've seen people before them who have cars. Nobody before them has borrowed money to go to school."
--Jennifer Roller, GEARUP director, Youngstown State University, Ohio

"Retention has been a problem at Carbondale. We did quite a few studies and we started to see that working over 20 hours a week started to disintegrate academic performance. Those students who were working a lot just to be able to go to school were not academically successful. They were defeating the purpose. There clearly seemed to be an issue that finances were affecting academic performance for some students."
--Dan Mann, former financial aid director, Southern Illinois University at Carbondale.

"I have actually had students tell me they aren't going to school because they can't get any grant money and they refuse to take on any loans."
--Bill Nowlin, Dean of Enrollment Management, Northeastern
State University, Oklahoma

"How can we better explain this process, what it means and why it might be good to take out the loan when we all wish they wouldn't have to take out the loan?. . . Even though we wish that these students weren't having to take out these loans and graduate in debt, lacking other choices, we want our students to enroll, and do well and we don't want them working 25 hours a week."
--Karen Rice, financial aid administrator, University of California, Berkeley

After College: Staying Out of the Red Zone.

While in college, the borrower's student loan experience is brief and relatively painless.

The truly meaningful relationship with a student loan begins about six months after leaving college. That's when the bills start coming in.

College is an excellent investment. On the average, it pays off in additional earnings far more than it costs. But for the graduating class of 2000, it certainly didn't feel that way. A year out of college, a large proportion—36 percent—were making payments that represented more than eight percent of their income. These borrowers are not all doomed to a long-term struggle with student debt. Many of them will see their incomes rise substantially over time, and they will be able to pay off their loans without great difficulty.

But untold numbers make enormous life and career sacrifices to pay their student loan bills. They forego a career as a teacher or community health worker. They take a higher-paying job "for a few years to pay off the loans," then find themselves stuck in a career path that does not represent the best contribution that they can make to their community. Or they work two jobs, too tired to excel at either, and miss out on promotions that would ease their debt burden, or on time with their children during the critical early years. They delay buying a home, and then watch as prices rise for the home they could have had. They forego adequate health insurance, delay saving for retirement, and make other tradeoffs with potentially devastating consequences.

Millions of borrowers have gotten some relief because the recent low interest rates in the economy meant lower rates on student loans. Hundreds of thousands of them have taken the opportunity to lock in low rates through consolidation; more will do so prior to a rate increase scheduled for July1. While some observers are concerned that the rate is "too low," it is the only real relief that struggling borrowers can currently get.

In the refinancing frenzy, it is easy to forget that there are many borrowers who are currently prisoners of their lenders, stuck with high fixed interest rates because of federal rules that prohibit them from consolidating more than once. President Bush proposed granting them the right to refinance. Congress should follow up on his recommendation.

The borrower relief offered by refinancing opportunities is important. But there is a dark side of the refinancing boom. Many borrowers are being placed in the longest repayment plan for which they are eligible. In the first six months of 2003, Sallie Mae reported that half of the company's new consolidations were for 20 years or longer. This reduces the borrower's monthly payments, providing many with the help they need. But total interest costs are higher over the life of the loan, and extending repayment into most borrowers' 40s interferes with the need to save for retirement and for their own kids' college education.

Solutions

Congress can address these problems by using the federal government's current investments more effectively. It is not necessary to spend additional taxpayer dollars or to

reduce student benefits as long as Congress takes the steps to make the loan program more efficient. This section focuses on how to spend the money; the next section focuses on where to get it. On the spending side, I recommend two strategies: (1) grant aid with accountability; and (2) loans that hurt less.

1. Grant aid with accountability. Elite universities are abandoning loans in order to recruit high-achieving students from low-income families. In the last few years, Harvard, Princeton, the University of North Carolina at Chapel Hill, and the University of Virginia all have launched new programs that promise students from low-income families that they will not have to take out any loans to pay for college. Initial reports indicate that low-income students, and minority students in particular, respond favorably to these programs.

Of course, most colleges and universities cannot afford to make blanket no-loan promises. They don't have the large endowments of more elite schools, and they enroll many more students from low-income families. But the strategy that high-status institutions are using suggests that increasing grants may be the most effective way to get more low-income students onto the college track.

What gets measured, gets done, and currently colleges and universities do not have enough reason to pay attention to their enrollment and retention of students from modest backgrounds. By attaching some campus funding to higher levels of Pell Grant enrollment campuses would be more likely to implement and improve programs to increase those numbers all the way through to the baccalaureate. The federal government should provide some funding for grant aid to colleges—either directly or through states—in proportion to the number of low-income students that the institutions enroll and/or graduate.

This policy would have different positive effects at two different types of colleges. At higher-priced and more selective institutions, it would create incentives both to recruit high-achieving students from low-income families and to offer the financial aid that they need to enroll. To some degree, this has already begun to happen. Three years ago, with the help of Don Heller at Pennsylvania State University, I wrote articles in the New York Times and the Los Angeles Times that pointed out the low proportion of Pell Grant recipients at some colleges and universities. Others then started drawing the comparisons between colleges, and the leaders of elite colleges are now paying closer attention to the economic diversity of their student bodies.

Low-cost institutions have a different problem. Too many of their students who likely qualify for aid are not getting it because there is no one to tell them that aid is available or to help them fill out the application. These are students who, if they had more aid, might attend full-time instead of part-time, or might enroll at a different institution, or might be able to get the child care they need in order to attend class consistently. At low-cost colleges right now, more students applying for aid just creates additional administrative work for the college. By providing some institutional funding with each Pell Grant, the campus has an incentive to help all the students who are eligible.

This funding could be provided directly to colleges by the federal government. Another, probably better, option has been suggested by the Advisory Committee on Student Financial Assistance, on which I serve as a congressional appointee. This approach would create a federal-state partnership, providing states with matching funds for policies and programs that improve college affordability, enrollment, and completion for their residents.

2. Loans that hurt less. Fifty years ago, the economist Milton Friedman said that the creation of a government student loan program would "do much to make equality of opportunity a reality, to diminish inequalities of income and wealth, and to promote the full use of our human resources." He suggested income-based repayment so that people could more safely take out the loans. Let's finally put his idea into meaningful practice.

Public policy should help hard-working borrowers stay away from Red Zone of burdensome debt without forcing them to spend half their working lives paying off their student loans. Past approaches, as well as the current income-sensitive and income-contingent repayment options, fail this test. They are better than nothing, but they provide inadequate relief, and they can extend repayment for too long.

We need a simpler, more effective design for income-based loan repayment assistance. This is critically important for two reasons. First, we need to be able to provide some assurance to students and families that a student loan will not ruin them. Our economy suffers when they decide against postsecondary education or when they work excessively during school. The purpose of the student loan program, after all, is to get people to give postsecondary education the old college try.

Second, we need to minimize the negative life and career effects that student debt can have on borrowers. A system that assists borrowers who are working but are still facing excessively burdensome loan payments will let graduates consider the best use of their skills and interests, even if it is not the career choice with the highest starting salary. It will make room for homeownership, entrepreneurship, retirement savings, and commitment to family, and reduce economic insecurity across the spectrum of student loan borrowers.

Improving Efficiency

There are a variety of ways that Congress could improve the efficiency of the student loan programs, and use those savings to ease the burdens of student loan debt.

A. According to President Bush's FY06 Budget, "the Federal Government assumes almost all of the risk for the [student] loans, while Federal subsidies to intermediaries—lenders and guaranty agencies—are set high enough to allow the less efficient ones to generate a profit. These problems lead to unnecessary costs for taxpayers and prevent the

program from achieving the efficiencies the market is designed to provide." To address this problem, the Bush Administration identified $25 billion in savings over 10 years. Some of those savings negatively affect borrowers. But at least half are positive improvements in efficiency, freeing up funds you could use to help borrowers when their payments are excessively burdensome.

B. Colleges have no incentive to keep taxpayers costs down in the loan programs; those costs are invisible to the institutions. Bipartisan legislation has already been introduced that would address this problem. Under the provisions of the Student Aid Rewards Act, the Secretary of Education would give colleges a share of the taxpayer savings when they utilize the loan program that the Secretary determines is "the most cost-effective for taxpayers." By aligning a college's incentives with taxpayer costs, this proposal, according to the Congressional Budget Office, would generate an additional $17 billion in grant aid for low-income students over 10 years.

C. Taxpayers are currently spending $240 million every three months to subsidize a guaranteed 9.5 percent interest rate for some student loans. Congress tried to fix this problem last October, but the payments have actually increased. Part of the problem with the new law is that it did not ban the "recycling" of loans carrying the excess subsidies. Recycling allows the loan companies to create new loans carrying the 9.5 percent guarantee by using collections and profits from prior 9.5 percent loans as capital. The lure of such large, taxpayer-assured returns is an invitation to abuse and the reason for the ballooning taxpayer costs over the last two years. I join with the Congressional Budget Office in recommending that this recycling be ended.

D. Congress should take a serious, independent look at all of the efficiencies that could be tapped in the government student loan programs without harming those the program was designed to help. First identify more cost-effective ways of providing students with the same loans and terms that they receive today. Then consider any changes in the design or distribution of student benefits. Compare them to the reforms proposed by President Bush. Compare them to other options. And give taxpayers the return they have every right to expect: real educational opportunity and a better educated workforce.

Fighting for efficiency is not easy. Those who benefit from the inefficiencies will resist change. Identifying improvements, particularly in a program that is financially complex like student loan systems, inevitably leads to competing and confusing interpretations of the data. Rely on the experts who work for taxpayers: CBO, OMB, GAO, the Education Department, and the Treasury Department.

We have a real opportunity to advance the education and training of our population, improving our economic competitiveness and making good on the American dream. Thank you for providing me with the opportunity to share my views. I look forward to working with you in the months to come.