About Young Invincibles

Young Invincibles is a non-partisan, non-profit organization that seeks to amplify the voices of young Americans and expand opportunity for our generation. Young Invincibles engages in education, policy analysis, and advocacy around the issues that matter most to this demographic, focusing primarily on health care, education and economic opportunity for young adults, and working to ensure that the perspectives of young people are heard wherever decisions about our collective future are being made.

Acknowledgements

We would like to thank the Bill and Melinda Gates Foundation for their generous support of this important research. We would also like to thank Healey Whitsett and NERA Economic Consulting for their invaluable partnership in developing and analyzing surveys, and the dozens of national and state partners who helped us reach so many students.

A number of members of the Young Invincibles team contributed to the research and drafting of the report over several months, and we are grateful for their efforts. Thanks to Brian Burrell, Erin Hemlin, Jasmine Hicks, Karen Hu, Nick Kelly, Amy Lin, Adaku Onyeka, Christina Postolowski, Katherine Schaller, Reid Setzer, Aaron Smith, Dustin Summers, Tzion Tesfaye, Samuel Wappel, and Ashley Young.
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Executive Summary

The coming months and year could be a turning point for students, their families and for the future of higher education in this country. The long-term trends of state disinvestment and increased student enrollment have brought student debt to unprecedented levels, and with it, public agreement that something must be done. At the same time, the federal government is facing enormous financial decisions in the near-term, with Washington debating choices around expiring tax cuts, automatic discretionary cuts known as sequestration, a Pell grant funding shortfall, and the fast-approaching reauthorization of the Higher Education Act. It is an understatement to say that large-scale decisions as to the future of investment in higher education in this country could be right around the corner. Now is the time for reform.

Unfortunately, the perspectives of students and young people have traditionally been an afterthought in these key debates in Washington. As a result, improvements to the federal aid system take years to accomplish, and never go quite far enough. Cuts, on the other hand, come quickly and hit hundreds of thousands of students at once. This project seeks to put an end to that. With the impending decisions in mind, Young Invincibles set out to capture the experiences and perspectives of a variety of students. We first analyzed existing polling, engaged in our own survey data collection, interviewed and held roundtables with hundreds of students and non-students from all backgrounds, and took note of the unique role and ideas of student leaders. We found that:

Key Research Findings

- Young people, and particularly students, broadly support investments in federal financial aid, even in the face of federal deficits. Nationally, three-quarters oppose cutting Pell grants for deficit reduction. In a survey of high debt borrowers, a large majority supported ending tax breaks for universities in order to sustain funding for Pell grants.

- Students overwhelmingly lack information and strong counseling about federal loans, federal grants, and private loans. About 40 percent of high debt borrowers responding to a survey reported never receiving federally mandated loan counseling.

- Students and student leaders value the connection between their school and jobs, and support measures that would increase that connection.

- When it comes to school accountability, students prefer incentives for driving improved outcomes to more punitive alternatives, likely worrying that other mechanisms will unfairly punish individuals. Student leaders in particular support strong accountability measures for schools, but seem to hold similar concerns.

Clearly, major reforms are needed to ensure that low- and middle-income students have access to school, that students graduate with a good job and minimal debt, and that all stakeholders – including students and schools – are held accountable for these goals. With the re-
Key Policy Solutions

- Fully fund and invest in Pell grants as a centerpiece of our financial aid system, protecting a critical tool for giving low-income students access to college. Invest in 2 new Pell programs, PellWorks and PellPlus, by reforming existing funding streams. 1) Pell Works: Use the Pell formula to re-target federal work study, sending work study dollars to schools that best connect school to work. 2) PellPlus: Instead of sending FSEOG dollars to schools that have been in the program longest, send dollars to the lowest-income students and to schools doing a better job of helping the lowest-income students graduate.

- Overhaul our student loan system with a single, simple federal loan. Provide automatic enrollment into the Income-Based Repayment as a form of insurance against tough economic times. Increase transparency with an online hub incorporating new and existing data, improve existing online counseling tools, and increase access to counselors for students in desperate need of guidance.

- Rethink and simplify tax incentives for higher education. Contemplate consolidation of credits like the American Opportunity Tax Credit and Lifetime Learning Credit, and consider redirecting expenditures for tax-exempt bonds that help private institutions and high-income investors to fill the Pell grant shortfall and fund expansions like PellWorks during reauthorization of the Higher Education Act.

These reforms take bold action on the part of all actors: President Obama, Congress, the Department of Education, schools, and importantly, students. But such action is necessary if we are to provide the same economic opportunities to this generation as we have to every previous one.
The Student Perspective

Introduction

Paying for college is a radically different proposition than it was even a generation ago, as any parent or student thinking about college knows well. A college degree was once so affordable that a student could work for a summer and pay for their next year’s tuition. No longer. Today, getting a degree is becoming increasingly essential to growing our economy and providing individual economic stability – yet getting that degree is dramatically more expensive. Moreover our country has fallen from 1st to 12th in the world in educational attainment.1 If we fail to address college access and completion, the economic consequences will be significant. Indeed, experts estimate that our country will be 3 million degrees short by 20182, and discussion about the skills gap facing employers is pervasive.3

This generation understands that the economy has changed: about four in five young adults believe that getting an education is more important to their generation than it was to their parent’s generation.4 As a result, about 80 percent of high school students who graduated in 2004 enrolled in college within two years after high school.5 Encouragingly, students from communities of color also go to college more than they did previously - though still not as often as Caucasians.6

But despite the increasing importance of education and the economic returns on public investment in higher education,7 state appropriations have fallen. Between 2000 and 2010, enrollment increased 37 percent, from 15 million to 21 million,8 but state and local funding per pupil for public higher education fell by 21 percent.9 This plummet followed several decades of declining investment and has fueled tuition hikes.

To view this drastic change through the lens of a student trying to pay for school:

- In 1980, at the average four-year school, a student who worked full-time over the summer at a minimum wage job could cover tuition the next year and have the 2012 equivalent of $1,923 leftover.

- In 2012, a student who works full-time over the summer at a minimum wage job covers 42% of tuition at an average 4-year school, leaving them $4,764 short.10

Most students simply cannot afford this cost without taking on significant debt.11 And while economists agree that a degree is still worth it, the economic gain is not always so clear to students. Although young adults believe that getting an education is important to their success,12 when life circumstances catch up, student aid cannot keep up, students drop out. In a recent survey by Young Invincibles, about one-third of high-debt borrowers said that federal aid did not cover tuition, and about 55 percent said that it did not cover additional costs beyond tuition.13 As a result, those who do make it through school often face a slow crawl through monthly debt bills, collection calls, and postponed life choices.

Young Invincibles will continue to work with its state partners to fight for state prioritization of higher education. But with a dramatic reversal in state appropriations unlikely in the next several years, today’s students will continue to face higher costs than prior generations. Federal aid, then, becomes increasingly important in filling the gap for students and ensuring that they graduate with economic opportunity and manageable debt.
Principles for Reform

In our surveys and conversations with students across the country, they voice concerns over rising costs, complicated financial aid systems, little guidance, and the uncertain job prospects after school. Students want change, and their experiences should guide these changes. If reform is done wrong -- without student input, for example -- it could hurt the very students we are trying to help. But higher education is too important to settle for the status quo. As Congress faces vital budgetary decisions, the reauthorization of the Higher Education Act, and a looming fiscal cliff, we offer policymakers a student-centered guide to reforms in federal financial aid.

Financial aid must provide meaningful access to all students and families.

With more students relying on higher education as a way to achieve financial stability, federal aid can and should provide access to that stability. About 84 percent of young adults state that making college more affordable should be a priority for Congress. Ensuring that federal aid works to make higher education accessible for all students, particularly students coming from communities with historically low enrollment and completion rates, including low-income students, should be a guiding tenet of the program. This generation understands that federal aid is a pathway to economic success, regardless of background. Policymakers should too.

Promote a transparent system that allows students and their families to act as well-informed consumers.

Academic research consistently shows that access to grant aid increases enrollment. Yet too few individuals fully understand the types of grants available to them. At the same time, when students do apply for aid, they find the process complicated and confusing. There are several similar types of loans and repayment options, but students often report that they are not even clear on the differences between loans and grants. It is unsurprising, then, that over 90 percent of the respondents to a large survey of high-debt borrowers support the creation of a model financial aid award letter with simple, easy-to-understand terms. Literacy gaps and an opaque marketplace lead not only to decisions not to attend or complete college, but also to more costly choices. Our federal aid system must be transparent and must prepare students to make good decisions.

Hold all stakeholders accountable for the goal of graduating students with jobs, not debt.

Encouraging students to enroll in higher education without a clear pathway to graduation and employment is not enough. About 40 percent of students who enter school do not graduate within 6 years, and completion rates are particularly low at many for-profit and community colleges. In a recent study, about four in five Pell grant recipients said that their grants increased the likelihood of completing school. Aid should help students complete their education, and schools benefiting from aid must be accountable for that goal as well.

Yet even for some who do graduate, a fuzzy loan marketplace and lack of protections mean that students too-often face difficulties in managing their debt. Attending college is only truly a pathway to economic security if students can leave school with a level of debt that they can pay down. All stakeholders must ensure that this aid money is going toward achieving that end.
The Student Perspective

- Make smart, innovative investments to prepare this generation for tomorrow’s economy.

This generation needs policymakers to make robust, smart financing decisions in higher education. Congress faces a large deficit, and recent legislation such as the Budget Control Act calls for across-the-board cuts of discretionary spending. Yet when asked whether Congress should cut Pell grants – the quintessential access program in federal aid policy – in order to address the growing national deficit, a full three-quarters of young people state that Pell grants should not be cut.

Indeed, young people understand that investing in higher education is crucial; 88 percent of young people and over 9 in 10 students agree that increasing financial aid and making loans more affordable for post-secondary education and training helps make the economy stronger. With limited resources, this means that policymakers must 1) invest adequate dollars in aid, and 2) efficiently distribute limited dollars.

Applying Student-Centered Principles to Reform

Changes to federal financial aid should systematically follow policy proposals that stem from the principles laid out above, and to best do that, policymakers must incorporate student voices. We have seen too many instances where student voices are ignored, and the consequences can be very harmful. For example, when policymakers in Washington faced a budget hole in Pell grant funding in 2011, they chose a quick fix that ultimately hurt students. Congress decided to make an immediate and retroactive change to the lifetime limit on Pell grants, from nine years to six years. Instead of a prospective or phased-in lower limit, the six-year cap was imposed immediately. A Pell grant recipient who was one semester away from graduating was nonetheless cut off if they hit the cap. More than 100,000 Pell recipients, including those only months from graduation, began losing Pell eligibility starting with the 2012-2013 academic year. Another quick change came when policymakers removed summer Pell grants right after implementing the new program, even before having a chance to determine how successful summer Pell grants could be in facilitating faster completion.

As one student told us, “I started my second stint of college in 2009, but my first go-around was in 1999, when I was forced to quit due to family circumstances. I’m now thirty-four years old and I’m able to attend school largely thanks to the Pell grant ... The current changes in the Pell grant regulations penalize those who realize their mistakes and return to college when their life is more stable.” This student was going to lose her summer Pell grant, and also expressed concern about having enough grant aid available to finish her degree in time due to the new cap.

To avoid these consequences, students must be included in the conversation from the beginning, and changes must follow the clearly articulated principles provided above. This paper lays out Young Invincibles’ research into what students are experiencing on the ground with the federal financial aid system, and what changes they want to see. We use this perspective as the basis and guiding force behind key policy recommendations to reform the federal aid system.
Surveying the Student Voice

Enhancing the voice of students in the nationwide conversation about financial aid reform is critical. Without a clear understanding of the complex ways in which policies impact students on the ground, Washington will never be able to craft effective reforms. And without student leaders and activists making calls to Washington, talking to their friends, and becoming an integral part of the policymaking process, Congress may lack the motivation to overcome the status quo and pass those reforms.

Over the past year, Young Invincibles has performed some of the most significant and comprehensive research in the country on the student perspective on financial aid. We conducted a national telephone poll and two online surveys with students from a range of backgrounds to understand attitudes on financial aid and options for reform. We launched a national bus tour in the spring of 2012, going to 20 states, 42 cities, and 43 campuses to host 100 roundtables on the economic challenges facing this generation. Unsurprisingly, much of the conversation focused on access to higher education and post-secondary skills. We engaged in a number of student roundtables this fall, talking specifically about federal financial aid issues. We performed one-on-one interviews with students, parents and counselors of all backgrounds, allowing them to share their stories and experiences. We also led an online survey of student leaders from across the country – the voices that play an important role in translating policy to their peers and can help to lead the movement for change with the public and policymakers. This report summarizes the findings from that research, including the following key points:

- Young people strongly support investments in higher education, even in the face of broad fiscal deficits. Nationally, three-quarters of those surveyed opposed cutting Pell grants for deficit reduction. In a survey of high debt borrowers, large majorities supported ending tax breaks to sustain funding for Pell grants.

- Students lack a great deal of information about federal loans, federal grants, and private loans.

- Students strongly support simplifying the financial aid system by reducing the types of loans and automatically enrolling graduates in IBR.

- Our processes of explaining financial aid to students need significant reform. The Free Application for Federal Student Aid ("FAFSA"), financial aid award letters, and federal student loan counseling require changes to make them simpler and more effective.

- Student leaders prefer incentives to improve school performance to more punitive approaches, likely worrying that those harsher mechanisms will unfairly punish individuals.
Surveying Students

In order to best understand the challenges in the current federal financial aid system and options for reform, Young Invincibles has conducted extensive quantitative and qualitative research into the student perspective on financial aid. Our research includes three major student and young adult surveys in the last year alone. In the fall of 2011, we worked with TICAS and Demos to commission a broad national telephone poll of 18 to 34 year-olds with a bipartisan set of pollsters. The poll produced significant data on the young adult perspective on financial aid and levels of support for federal programs like Pell grants. Importantly, this poll included large samples of Latinos and African-Americans, allowing us to look at the views of diverse young adult cohorts both individually and collectively. In the spring of 2012, we administered an online survey of 12,000 student loan borrowers to better understand borrowers’ level of awareness about their own financial aid.

This fall, we worked with NERA Economic Consulting to administer an online survey with over 27,000 largely high-debt respondents to delve more deeply into the problems and potential solutions for financial aid reform. The high debt student and former student population were a key target of our research because these borrowers often have the greatest interaction with federal financial aid and can speak well to its problems. This fall, we also conducted an online survey of 72 student leaders from around the country, and about 35 in-depth phone interviews with a diverse sample of those interacting with the financial aid system, from high school students to college students to parents. Our research includes the perspectives of students in four-year public and private colleges and universities, community colleges, for-profit colleges, non-traditional students, high school students, recent graduates, college drop-outs, as well as young adults who never went to college. We report the results of this extensive research below.

Young People Value Investments in Higher Education

Congress may be debating cuts to discretionary funding, but for young people, there is no debate.

- Eight in ten current students oppose cutting Pell grants or loan subsidies to reduce the deficit.
- The top priorities for young adults are #1) jobs and #2) college affordability. Among young African-Americans, the order is reversed - college affordability is #1.1

Though young people are a voice to be reckoned with in the voting booth, few public polls actually ask them about their perspectives on the issues. Without more information, policymakers have
trouble keeping pace with the views of students and young Americans. To help close that gap, YI conducted a broad telephone poll of nearly 900 young people, ages 18 to 34, about their thoughts on the affordability and necessity of a college education, strengthening the economy, and Congress’ top priorities.

Young people sent a clear message in this poll: this generation highly prioritizes higher education and financial aid. The top priorities for young adults for their leaders in Washington are #1) jobs and #2) college affordability. Among young African-Americans, the order is reversed. For example, 82 percent of 18 to 34 year-olds felt that some kind of education or training beyond high school is more important today than it was for their parents’ generation. This generation also clearly understands that the economy has changed, placing new demands on their careers.

Not surprisingly, the recognition of education’s growing importance influenced young American’s perspective on federal funding priorities. For example, respondents felt strongly about not cutting Pell grants. Even when it was suggested that cutting Pell grants could reduce the deficit, three-quarters of respondents still answered that Pell grants should not be cut. Those results were even higher for current students - eight in ten opposed cutting Pell grants or loan subsidies to reduce the deficit. The findings are particularly relevant in the current fiscal climate.

Overall, the poll demonstrated that young people are the most concerned with access to higher education and their job prospects. Eighty-four percent of respondents wanted Congress to make the affordability of a college education a priority, even when also asked about reducing the federal debt by cutting spending on entitlements. Furthermore, when respondents were asked about their feelings on making the economy stronger, 88 percent supported increasing financial aid and making loans more affordable for college and post-high school education and training. Education, it is safe to say, is a top investment priority for this generation, even in the current fiscal climate.

The Student Experience With Federal Financial Aid

Student respondents to another survey sent a clear message when it came to their experience with financial aid: they need more help.

- 40 percent of student and recent graduates reported that they did not receive loan counseling from their school, as required by federal law.
- About two-thirds of private loan borrowers, including those with private and federal loans, did not understand the major differences between their private and federal loan options.
- 81 percent of students and recent graduates felt that a school’s job placement rate was “important” or “very important” in deciding on where to attend and send their federal aid dollars.

Despite the broad support for public investment in higher education, young people still struggle with the federal aid status quo. This fall, Young Invincibles released a report, “Lost Without a Map: A Survey about Students’ Experiences Navigating the Financial Aid Process.” The underlying survey showed that students are woefully under-informed about the financial aid system and need more reliable and simpler information regarding their student loans.
While we released some of the data in our September 2012 report, this white paper contains previously unreleased results on additional financial aid issues and student responses to proposed policy fixes.

The survey was e-mailed to over 1.5 million high-debt borrowers and targeted to those most likely to be affected by financial aid policy. Of the 27,000 responses received, the analysis focuses on about 13,000 respondents, about 5,000 current students and about 8,000 recent graduates. Although the results of the survey cannot be generalized to the larger population of current students and recent graduates, the students included in the survey were more likely to be affected by and concerned about financial aid policy. These facts made the students surveyed the ideal sample to study in gaining perspective on issues related to student financial aid.

The Importance of Aid

The survey results demonstrate the importance of financial aid for students to access higher education. For instance, 98 percent of federal borrowers and 87 percent of grant recipients reported that receiving financial aid allowed them to attend school. Additionally, after beginning a program of study, 96 percent of federal loan borrowers, 87 percent of private loan borrowers, and 78 percent of grant recipients reported that the aid they received made it more likely that they would or did complete their degree. These statistics make it clear that students view financial aid as essential to getting a degree.

Despite the necessity of financial aid, about one-third of respondents reported that they did not receive enough federal financial aid to cover their tuition costs. Of that population, about one-third, reported taking on private loans to cover the additional tuition, and about 21 percent reported working part-time to make payments. In addition, about 54 percent of respondents reported not having enough financial aid to cover living expenses beyond tuition. To pay for living expenses, most of these students worked part-time, and about one-third reported working full-time or using credit cards to make up the difference. In other words, the vast majority of students whose financial aid did not cover living expenses took time away from their studies to work, or took on more debt using credit cards or private loans, in order to stay in school.

Views on College Choice

We also asked respondents about what they looked for when choosing a school to find out what additional information students would find most valuable during the financial aid counseling
process. In particular, we wanted to know what kinds of information about outcomes mattered to students, and how those data points compared to other characteristics. For example, 81 percent of students and recent graduates felt that a school’s job placement rate was “important” or “very important” in deciding on where to attend. Three-quarters felt that way about the graduation rate.

In contrast, only a little more than a third thought that the student loan default rate of recent graduates was important. Even though default rates are an important metric from a federal policy perspective, the technical terminology may not adequately communicate information to students. Our data suggests students respond better to straightforward measures such as completing a degree or finding a job, and that some accountability metrics like default rates do require enforcement by the Department of Education.

However, a handful of other factors ranked ahead of these outcomes. Strikingly, 97 percent of respondents felt academic majors/fields of study were an important or very important characteristic. Academic rigor came in as the second most popular trait with over 90 percent of participants identifying it as important. By contrast, less than half of respondents felt athletic teams, social life, or extracurricular activities were important in deciding where to go.

While most students responded that they relish information like job placement rates, others did not spend time reviewing those statistics before enrolling. Lisanne H., a massage therapist who holds a bachelor’s in Italian Studies, shared with us that her priority was to get a degree, but wished she had examined information on job placement statistics about the school she chose: “I was more hungry to just get a degree of some kind, and at that time that’s what everyone was doing; in hindsight, it definitely would have helped.” Many students intuitively care about outcomes, but others will not go looking for them when making decisions. For the latter students, if federal aid dollars go to the better-performing schools, it is imperative that they have easy-to-understand data available for consumption.

**Understanding Aid**

Students also made clear that they lacked information and proper counseling during the financial aid process. An alarming number of respondents to the survey reported that they did not receive adequate or accurate financial aid information. Only about 60 percent of grant and federal loan recipients and 40 percent of private loan borrowers answered that they had received accurate information. Mike H., who attended the for-profit college New England Institute of Art in 2006, said he felt like he was being sold a product rather than being provided with information, stating: “I wouldn’t use the word ‘counseling.’”

Additionally, survey respondents lost confidence after graduation in the information that they had previously received. For instance, recent graduates with either federal loans or private loans were about 10 percentage points less likely than current students to report that they got accurate information about their loans. This difference in respondents’ perception of information accuracy could indicate that borrowers only learn about the details of their student loans upon graduation, when they enter repayment. The hypothesis fits with our earlier findings that nearly two thirds of high debt borrow-
ers reported being surprised by terms of their loans or the student loan process. Even before loans come due, students are confused. Jacqueece M., a young woman we interviewed who is waiting to take her nursing boards, told us that she still lacks understanding about the different loans she took out: “I am not that confident. To be totally honest ... I have so many different loans, with different interest rates, they are all on different schedules and it’s a lot to keep up with.”

It is unsurprising, then, that survey respondents considered federal student loan counseling to be lacking. Over 40 percent reported that they had not received federal loan counseling at all, despite the federal mandate that all students taking out federal loans receive counseling. For those respondents who remembered receiving counseling (about 55 percent), 59 percent found it somewhat or very informative, while 41 percent found it somewhat or very uninformative or had no opinion. When the respondents were asked to provide a substantive answer as to what they would change about the federal student loan counseling system, most tended to comment on the format of the counseling or the content of the counseling. Specifically, 15 percent said they would make the counseling more personal, and nearly 50 percent said more or better information on interest rates, repayment options and timelines, consolidation options, and information on the total amount owed and estimated monthly payments should be included.

Generally, respondents were only moderately satisfied with their current and/or previous sources of financial aid information and would have preferred more information earlier in the financial aid process. They typically received most of their information from financial aid offices and government websites. When asked where they preferred to get their information from, students re-emphasized those two sources. However, a sizable minority of respondents would have preferred to receive additional information from their high school counselors, suggesting some students want to have more information earlier in the process. Moreover, nearly 40 percent of private loan borrowers would have preferred more information from a governmental website, suggesting they did not receive enough from the loan companies themselves.

We also asked respondents about the how they preferred to receive financial aid information. Although we expected this media savvy generation to desire information through the newest avenues, few respondents would wanted to learn about financial aid via informal media, such as text messages and social media. They preferred traditional high quality digital sources like e-mail, grant/loan specific databases, and grant/loan specific websites. Also of note, most respondents filled out financial aid applications for themselves. This finding argues for focusing information dissemination on the students themselves, and only secondarily on those who provide guidance to the students, like their parents.

The September 2012 survey builds upon a similar Young Invincibles report in the spring 2012 called “High Debt, Low Information: A Survey of Student Loan Borrowers,” analyzing a similar sample of high-debt borrowers owing more than $76,000 and falling into the top 5 percent of borrowers by student debt volume. As noted above, the survey found that 65 percent of
respondents misunderstood or were surprised by aspects of their student loans or the student loan process. Moreover, about two-thirds of private loan borrowers, including those with private and federal loans, did not understand the major differences between their private and federal loan options.

The survey population also demonstrated low comprehension of basic financial aid terminology. About 20 percent of respondents found repayment terms confusing, 20 percent mentioned the amount of their monthly payments as confusing, and 15 percent thought that their loans’ interest rates were confusing. Even older, more experienced students do not fully grasp the complexities that they face. Erica Z., currently a law student at the University of Maryland, told us she feels more confident in her understanding of financial aid now that she is in graduate school: “Haven’t had too many horrific experiences, still learning, but now confident I understand 50-60% of what goes on.”

Student feedback consistently tells us that policy reformers must not assume that students will be able to seamlessly translate data and information into good decisions without an accompanying investment in better counseling and financial literacy.

Reactions to Policy Reform

Because students struggle in the current system, they overwhelmingly support mechanisms to simplify the system.

- 89 percent of respondents strongly agreed or agreed with being automatically enrolled in the income-based repayment plan.

- Three-quarters of respondents agreed with reforming federal financial aid to include one grant, one loan, and one subsidized work program.

- Over 90 percent of respondents agreed with standardizing the format content and terminology of financial aid award letters.

- 70 percent agreed with eliminating tax breaks that reduce tuition costs for upper-income families in order to sustain funding for Pell grants for lower-income students.

- Six in ten supported eliminating tax breaks that make it cheaper for private universities to improve their facilities in order to maintain funding for Pell grants.

- 87 percent of respondents agreed with giving students a reduction in their federal loan interest rate for graduating on time.

The financial aid system is unnecessarily complicated and confusing for most students. To inform our ideas around improving the financial aid system, we asked students a number of questions about specific reforms.

In general, respondents strongly supported reforms that would simplify the financial aid system and our process for explaining it to a student. Most notably, 89 percent of respondents strongly agreed or agreed with being automatically enrolled in the income-based repayment plan, a loan repayment program allowing them to pay only what they could afford based on their income. Another three-quarters agreed with reforming federal financial aid to include one grant, one loan, and one subsidized work program. Evidently, students strongly support a more straightforward structure to federal aid.
Respondents also feel that financial aid forms should be simplified. Over 90 percent agreed with standardizing the format content and terminology of financial aid award letters.\textsuperscript{23} Three quarters agreed that a one-time FASFA application would be ideal, and about two-thirds of borrowers agreed with eliminating non-financial questions from the FAFSA.\textsuperscript{24} The feedback strongly suggests that whatever reforms go into effect, the federal government and schools must make changes to the process for applying and receiving financial aid.

We also asked participants about a number of accountability reforms, which led to mixed feedback. Typically, students supported positive incentives for students to reach goals. For example, 87 percent agreed with giving students a reduction in federal loan interest rate for graduating on time. Over 70 percent support making more loans available to students on track to graduate. On the other hand, when asked if students should receive more financial aid if they attended schools with better track records, only 40 percent supported sending more financial aid dollars to schools with higher graduation or job placement rates. The number does not necessarily translate into disagreement: about one-third of students responded neutrally to the proposals.

This evidence combined with our interviews suggests two main reasons for the trends. First, institutional accountability is an abstract concept that many students do not intuitively grasp. This became clear in our interviews, because as we spelled out the accountability mechanisms for schools in more depth, students were supportive, after initial concern that institutional accountability mechanisms would hurt an individual’s ability to achieve his or her educational goals. They might ask, for example, “why should I be punished if my school is the one who is failing?” The feedback suggests any institutional accountability mechanism must adequately protect the aspirations of individual students, and that students as a whole need more information about proposals to hold schools accountable.

Finally, we asked about priorities in higher education spending. Most relevant to this paper, 70 percent agreed with eliminating tax breaks that reduce tuition costs for upper income families in order to sustain funding for Pell grants for lower-income students. Six in ten supported eliminating tax breaks that make it cheaper for private universities to improve their facilities in order to maintain funding for Pell grants. The responses suggest students favor distributing tax benefits that go to high-income families or private institutions to fund programs that help those who need it most.

These national and self-selected surveys are key to understanding the student experience.
The Student Voice: Student Leaders Speak Up

Young Invincibles, in conjunction with several national and state partners, conducted a survey of student leaders to gauge their views on the costs of college, the financial aid process, and observations of their peers’ experiences. The survey asked respondents about their views on how their universities prepared their peers for employment, their general understanding of the grant and loan system, the importance of federal aid in completion, and ways in which they believe schools should be held accountable for the aid that they receive. These 72 leaders provided some important feedback:

- **Accountability:** Student leaders see value in holding schools accountable for the federal aid that they receive: about 80 percent of respondents agreed the federal government should hold schools that take federal money accountable for strong student outcomes. However, they are wary of what pulling aid away from schools might do to students, and are more supportive of positive incentives.

The voice of student leaders is important for several reasons. First, while typical students and borrowers give insight into how the federal aid system is working, the views of student leaders give insight into how campuses may be responding systemically to those issues. Student leaders are more likely to listen to their peers, interact with their school administration, and understand the financial workings of a campus. Second, the views of student leaders can give policymakers some indication as to how the more active student voices will speak up. Leaders on a campus or in an organization working on behalf of students are the ones leading campaigns and shaping the work of their fellow students. Their leadership experience gives them a nuanced perspective on financial aid issues, and increases the likelihood that they will be actively engaged in advocating for or against proposed policy changes.

- **Job placement** rate was a top factor for student leaders in choosing a school, and those surveyed strongly support measures that will improve that connection, including reforms to work-study. Yet, they also value the ability to choose an area of study without having financial aid impacted.

- **Simplify:** There is a clear consensus among the student leaders that students have a poor understanding of the financial aid process. Three-quarters of student leaders thought that simplifying the system and in-depth counseling were key tactics to helping their peers.
The Student Perspective

Methodology & Demographic Information

The survey was distributed online through national and state networks. Those networks included: Young Invincibles, National Campus Leadership Council, Campus Progress, United States Student Association, the Illinois Education Foundation, the Minnesota State University Student Association, the Campaign for College Opportunity in California, and several other organizations connected to student leader listservs. Those who responded were more likely to be active and well-connected to networks that work on financial aid issues. While this is small and self-selected sample, it is an important voice to capture – these leaders often take action and leadership roles on financial aid questions, talk to the media, call their members of Congress, and lead campus-based campaigns.

A total of 72 student leaders of various backgrounds participated in this survey concerning their experiences and opinions on college affordability, and job prospects post-graduation. The majority were student leaders seeking a bachelor’s degree. Most respondents attend a public university (70 percent) followed by 17 percent who attend a private not-for-profit university, almost 9 percent who attend community college, and 4 percent who attend a for-profit institution. Every respondent did not answer every question; percentages reported on each question refer to the percentage who responded to that particular question.

The category of “student leaders” is characterized by a variety of positions held on campus by the respondents. The majority of respondents, 55 percent, identify as a leader in an active student organization on campus, such as a fraternity or sorority. Over one-quarter are student body presidents of their campuses. The nearly 8 percent who chose “other” included roles such as athletic team captains, leaders of campus projects, student representatives-at-large, and student trustees.

Number of Respondents

![Table 1.1: Percentage of students in various leadership roles.]

- Student Body President: 27.5%
- SGA Member: 47.1%
- Student Council: 3.9%
- Student Organization Leader: 54.9%
- Student Advocate Organization: 21.6%
- Other: 7.8%
Analysis of Responses

Student leaders are looking for change in the federal aid system. Despite this desire among student leaders to see changes in financial aid at their school, 63 percent of students said their school did not seek their advice in potential financial aid reforms. Only 9 percent answered that they have been consulted in efforts for change. Should policymakers and campuses begin to listen more closely, here is some of what they may hear.

Help Wanted: Connecting School to Work

Student leaders value the role of colleges and universities in helping students find jobs after graduation. When asked to rate the important factors when picking a school, the “job placement rate” of the institution was ranked second, just behind the “graduation rate.” Some of the more commonly cited reasons for picking a school, such as academic prestige and the program’s US News and World Report Ranking, were rated far lower. A total of 81 percent of respondents who value the job placement rate of a school is a show of overwhelming support.

Respondents attend, or have attended, the following schools:

- Brandeis University
- California State University
- California State University at Northridge
- Colby College
- Community College at Forest Park
- Florida International University
- Georgetown University
- George Washington University
- Howard University
- Hunter College
- Iowa State University
- Macaulay Honors College at CUNY Hunter
- Mankato State University
- Minnesota State University
- Minnesota State University at Moorhead
- Modesto Junior College
- Occidental College
- Purdue University
- Quinnipiac University
- Rivier University
- St. Louis University
- SUNY Binghamton University
- Southwest Minnesota State University
- Texas Southmost College
- University of California - Santa Cruz
- University of Maine
- University of Richmond
- University of Texas at Brownsville
- Virginia Commonwealth University
- Virginia Tech University
- Winona State University
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Top Student Factors in Picking Colleges, In-Depth

Table 1.2

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<tr>
<th>Factor</th>
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<th>Somewhat Important</th>
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<td>Job Placement Rate</td>
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<td>Recent Grad Loan Default Rate</td>
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<td>Income of Graduates</td>
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<td>US News &amp; World Report Ranking</td>
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<td>Social Life</td>
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<td>Academic Rigor</td>
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<td>Quality of Facilities</td>
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<td>Quality of Athletic Teams</td>
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Table 1.3

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<td>52.2%</td>
<td>26.1%</td>
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<td>32.6%</td>
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<td>34.8%</td>
<td>15.2%</td>
<td>4.3%</td>
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Interestingly, in our broader survey, students ranked choice of major above job placement and graduation rates. Student leaders often are keen observers of their peers, both older students who have graduated, and younger ones entering their programs. The fact that the respondents chose to rate factual data like job placement rates and graduation rates higher than reputation and prestige shows the priorities that student advocates will have when fighting for changes in their campus’ behavior. Importantly, this survey result could foreshadow future trends of more data-driven decision-making by students in picking their schools, particularly as that information becomes more accessible to less-informed students.

Indeed, some of the graduate students we interviewed believed this information is important, but are not convinced they would have given it much weight at the time they applied to colleges. Katie H., who completed her bachelor’s degree in business administration from Suffolk University, told us, “I think those are good questions to ask, but I don’t remember if I looked at that or not.” Student leaders could be key players in moving the ball to fight for and successfully disseminate better information for their peers.

Unfortunately, a majority of respondents agreed that their school is doing an insufficient job in helping students find a job after graduation. Fifty-three percent of respondents answered that their school either did not provide students help, or that the help came too late. In contrast, about 34 percent answered that their school provides sufficient support in helping students find jobs post-graduation.

Young Invincibles knew that connecting coursework to jobs was important to students, and wanted to test various policy solutions. For example, the survey tested whether student leaders might support a measure that provided financial incentives to students who work to graduate quickly and choose majors based on high-demand jobs. Students who choose to major in mechanical engineering and follow a degree plan that allows them to graduate in three years instead of four would be offered opportunities for financial aid that aren’t available to all students.

We found, however, that such an approach was not popular among those surveyed. Only 11 percent of respondents agreed strongly with this policy, whereas 46 percent of respondents either disagreed or disagreed strongly. Another 30 percent answered neutral or had no opinion. These responses made it clear: student leaders value strong job placement rates in schools, but also value the ability to choose areas of study. The question must also be distinguished from support for loan incentives that provide assistance to students who choose majors that pay less, which students see as an expansion of choice, rather than narrowing options such as the survey question suggested. Any policy push in the direction of spending more aid on high-demand fields would have to maintain that freedom and would need to convince student leaders of the value of such a policy.

Lastly, the survey asked respondents for their opinions on a policy recommendation being considered by Young Invincibles called “Pell Works.” Pell Works would reform federal work study by tying the program to federal Pell grants and retargeting work study funding to students most in need, and encouraging jobs related to a student’s field of study. Respondents overwhelmingly supported this reform: 81 percent
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answered that this would benefit students at their school. That being said, 60 percent of respondents feel that their school does a good job of providing “real world experience” through work study jobs, paid internships, and coursework connected to local and regional employers. Certainly, high-achieving students who become leaders on campus are more likely to personally land quality job placements like sought after paid internships and top work study positions. However, the overall support for work-study and current programs make it clear that an aid-based program is popular among students, but that these leaders agree that there is room for improvement.

Navigating the Federal Aid Process

Student leaders were in agreement with overall survey respondents, stating that the current system is too confusing and that schools could be more proactive in providing information and in-depth counseling to students around financial aid. For an open answer question, the student leader respondents mostly replied that making financial aid information more accessible, lowering the student-to-counselor ratio, and providing information that is clearer and easier to understand were all critical.

When asked about the accuracy of information that is provided to them by their own financial aid offices, about half of respondents, 47 percent, believe that information their peers receive about financial aid is either “very accurate” or “mostly accurate,” while the other half of respondents, stated that the information that is provided to them and other students is only “somewhat accurate.” Similarly, 57 percent of respondents do not believe that the information that their peers receive about grants and loans were “clear and understandable.” Only 14 respondents believe that information is presented in a clear and understandable way.

Compensation of Grants and Federal Loans

Table 1.4

Student leaders were asked what they thought would help students make more informed decisions about grants and loans; the top two responses chosen by about three-quarters of student leaders were a simplified process and more in-depth counseling.

When asked what could be done to improve federal student loan counseling, respondents answered their schools should “be more proactive,” “advertise [information on loans] around campus, and hold workshops that help students navigate the system.” Other respondents asked for more aggressive advertising of loans and repayment programs. These changes could be made without having to take legislative action altering federal aid.

The survey asked student leaders a few questions on interest rates and their views on repay-
ment options, especially for recent graduates who are struggling to find work. Regarding interest rates, there was significant support for lowering rates that would ease payments for recent graduates who are low-income. About 43 percent of respondents “strongly agree” that borrowers should be automatically enrolled in a loan repayment program that allows them to pay only what they can afford based on their income. An additional 38 percent agree with this policy reform. In sum, 81 percent of respondents showed support for automatic enrollment in income-based repayment programs.

Respondents found automatic enrollment favorable even when asked in comparison to other repayment options. About two-thirds of student leaders said that they favored a repayment plan where borrowers are enrolled in a program where their loan payment was a fixed percentage of their income, versus based on the amount owed. These results signify the potential for significant student leader support for revamping the student loan repayment system.

**Completion**

Student leaders who participated in our survey see their peers dropping out of school for financial reasons as a serious issue. Almost 80 percent answered that dropping out of school for financial concerns was a “very big problem” or “somewhat of a problem.” They stated that more financial aid will allow their peers to stay in school instead of dropping out in order to work full time, and allow students to concentrate more on their classes while in school. Almost 70 percent believe that more financial aid will allow their peers to focus more on school and encourage completion. Only 13 percent of respondents answered that most students at their school received enough aid to stay in school and not stress about their finances.
Similarly, 80 percent of respondents agreed with the statement “the amount of grant(s)/federal student loan(s)/private student loan(s) that students at my school receive make it more likely that they will complete their degree.” Student leaders supported measures for rewarding students who graduate on time, however, respondents generally did not agree that financial aid should be contingent to finishing a degree plan.

That being said, when asked if federal financial aid should be used to encourage students to graduate on time and participate in programs that will get them work experience, 80 percent of respondents either strongly agreed or agreed with this statement. Respondents were asked if financial incentives should be offered to their peers who take on more coursework to graduate quicker, given the fact that at the average 4-year public school, only about 50 percent of full-time students graduate within 6 years, student leaders agreed that those who strive to finish on time should be rewarded with access to additional financial aid like bigger Pell grants or lower interest rates. While student leaders seem wary of pulling existing financial aid from those who take longer to complete a degree, there does seem to be interest in added incentives to encourage a quicker trajectory.

School Accountability

Student leader respondents had interesting answers about how to hold schools accountable for their success in providing adequate education. Respondents did agree that schools have a responsibility to do better—keeping tuition down, helping students graduate, and connecting students to jobs. Specifically, about 80 percent of respondents agreed the federal government should hold schools that take federal money accountable for strong student outcomes.

But student leaders were wary of reform proposal to take away federal dollars for Pell grants and student loans from students who attend schools with very low graduation rates, such as a rate below 15 percent. About 54 percent of respondents do not believe federal financial aid should be limited at these institutions despite their poor records of degree completion. Stu-
dent leaders seem to hold similar concerns as the more general survey respondents, worrying that students will be harmed.

In line with keeping tuition down, student leaders also shared opinions on how federal dollars allocated to universities should be spent. About 76 percent of respondents either agreed strongly or agreed that tax breaks for private universities for amenities, such as new dorms, should be eliminated in favor of maintaining funding for Pell grants for low-income students. Only 12 percent disagreed or disagreed strongly with this elimination for private universities. This is consistent with the views of student leaders that federal dollars should be concentrated in academics and used as investments in students, rather than general university improvements. Certainly, most respondents to the survey attended public schools – but this breakdown is largely reflective of the student body as a whole.

Respondents also felt that in order to keep tuition down, help more students graduate, and connect their peers to jobs, the government should incent schools to perform well by providing greater financial support to the school: almost 60 percent answered either in agreement or strong agreement. Again, the positive wording of this question may account for stronger support than similar questions that asked if financial aid should be taken away from low-performing schools. When asked if financial aid dollars should be taken away from very low-performing schools, the most often chosen answer was neutral at 34 percent. This likely stems from a) a fear that current students would be unfairly harmed, and b) a need for more concrete understanding of what these penalties would entail.

This dichotomy is significant, particularly as policymakers in Washington consider accountability metrics, and reflects the concern cited by students more generally: a reluctance to punish schools that do not perform well so as not to unfairly harm students who attend those schools, but a general agreement that it is reasonable to reward students and schools who perform well. Any accountability recommendations should adequately address those valid concerns, ensuring that if schools lose funding, current students would not be harmed; policymakers should also adequately convey this to student leaders who would otherwise support such measures.

Student leaders have a unique and critical position in the higher education landscape, serving as a connection point between the general student body, policymakers, and administrations. Importantly, student leaders, like other students, are often personally impacted by policy decisions, good and bad, made by our leaders in Washington. The student leader voice is a powerful one, and one that must be heeded as decisions about financial aid reform are considered.

**Conclusion: A Desire for Reform**

Though America’s students are very diverse and hold a variety of different views, our surveys and interviews have revealed clear trends of opinion. For example, our generation strongly supports investment in higher education and wants Congress to protect Pell grants from deficit cuts. Moreover, students feel that financial aid is overly complex and poorly explained. They support a variety of reforms that would improve information delivery and simplify the system itself. Finally, students tend to support accountability, but only if accountability measures do not unfairly punish students for their schools’ mistakes. These takeaways shape our ideas for reform.
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Reimagining Federal Financial Aid

After nearly a year of research into the tone of the student voice on federal financial aid, we set about to develop principles for reform, and ultimately, specific solutions to meet the needs of our generation. Our analysis demonstrates that federal financial aid plays a crucial role in educating this generation, but needs change to truly live up to the values we set forward. Too few students can afford college. Too few students and families can make sense of a complicated system. Too few institutions are held accountable for poorly serving students. We set forward solutions below that address each of these concerns consistent with the values of our generation:

- Fully fund Pell grants and tie innovative reforms to this foundational program.
  - Convert Federal Work Study to PellWorks, a grant program that rewards schools that create opportunities for low-income students to find job experience related to their field of study.
  - Convert Federal Supplemental Educational Opportunity Grants to PellPlus, a funding stream that rewards schools who enroll higher numbers of Pell students and graduates the highest percentage of students with high risk factors.
- Create a system of student loan insurance where all federal borrowers take out a single type of federal loan and automatically enroll in Income-Based Repayment upon graduation.
- Provide students with more information about school outcomes, simplify the FAFSA, standardize financial aid award letters, and scale up efforts to counsel students about federal financial aid.
- End or reform tax breaks that subsidize private schools to build expensive buildings and use savings to fund Pell grants.

Implementing these changes would dramatically improve the federal financial system from the perspective of students. In the sections below, we offer up specific details on how to put these reforms into practice.

Bolstering Grant Aid

The foundation of the federal financial aid system is the Pell grant, a 40 year-old program that has sent millions of students to college. Grants are distributed to students based on a sophisticated need-based formula, and between 9 and 10 million students qualify for some amount of aid. The program is well-targeted to students and families who need it most, and academic research shows us that need-based grant aid like Pell is responsible for enrolling more low-income students. Making college truly affordable able requires a multi-faceted approach, including a dramatic reversal in state appropriations. At the federal level, Pell grants are the single most powerful tool that we have to enroll students and keep debt levels low.

The Importance of Pell

Pell grants increase enrollment of lower-middle and lower income individuals. Initially
established under the Higher Education Act (HEA) of 1972, Pell grants are available to students seeking undergraduate degrees and who have limited means with which to pursue higher education. During the 2010 - 2011 academic year alone, more than 9.5 million students relied upon Pell grants as a primary source of funding for their pursuit of a college degree.\(^2\)

Currently, Pell grants are mostly funded as a discretionary line item within the federal budget, with a portion of funding coming from mandatory spending: each grant is 12% mandatory and 88% discretionary.\(^3\) The grants are made available to anyone who qualifies. In 2007 through 2010, Congress increased funding for Pell and restructured the way in which it is funded, creating and then altering the mandatory funding side of the equation.\(^4\)

Those increases were too good to last. With a tough economy and an increase in college enrollment, Congress failed to keep funding at the levels needed. In April 2011, Congress passed the Department of Defense Full-Year Continuing Appropriations Act, which repealed the newly instated summer Pell grant. Then, in August 2011, Congress passed the Budget Control Act, which appropriated an additional $17 billion in mandatory funding needed to keep Pell almost level for 2011 – 2013, but also left a shortfall in Pell grant funding that had to be filled by appropriators. The law also included mandatory caps on discretionary spending, as well as sequestration, or additional automatic cuts, that would effect Pell starting in 2014.

In December 2011, Congress passed the Consolidated Appropriations Act of 2012, a bill that filled the gap leftover by the Budget Control Act through a variety of cuts. For example, Congress cut the ability of a student to access Pell grants from 18 semesters to 12 semesters, but made that cut retroactive. As a result, more than 100,000 Pell recipients, including those nearing completion, began losing their access to grants. Those cuts disproportionately hurt minority students.\(^5\) That round of cuts also cut off access to Pell grants for students without a high school diploma or GED to receive federal aid if they a) passed a federal test; or b) completed 6 credit hours of postsecondary education.\(^6\) Several innovative career pathways programs across the country relied on the “Ability to Benefit” (ATB) provision to help disadvantaged students complete post-secondary credentials by curtailing remedial education and co-enrolling participants in adult education with courses leading to a job in a high demand field. The cuts eliminated ATB for an estimated 90,000 students.

As it stands now, each new budget cycle threatens Pell. Looming mandatory shortfalls threaten to leave the program underfunded by $8 billion in 2014, with additional gaps in subsequent years.

This constant battle harms students’ ability to access a college degree. Academic literature clearly demonstrates that access to grant aid increases enrollment again low-income students. A recent study by Bridget Terry Long and Benjamin J. Castleman found that being eligible for $1,000 in grant aid increased enrollment by 4.1 percentage points.\(^7\) In a 2006 study, Sarah Turner and John Bound found that less public resources to subsidize education meant lower degree attainment.\(^8\) Another study found that a 10% increase in the maximum Pell award is associated with a 15% increase in revenues received at the average institution, meaning that “low-income students appear sensitive to the level of aid conditioned on the decision to
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enroll."9 Another recent study found that Pell grants served as significant factor in encouraging lower income students to enroll in rural community colleges.10

Opponents of Pell grants sometimes raise the prospect that additional grant aid fuels tuition increase, but study after study has clearly demonstrated that this is not the case. As leading higher education economist Sandy Baum put it, “There is no convincing evidence that increases in Pell Grants feed tuition increases in either public or private not-for-profit institutions. Increases in federal grant funding for low- and moderate-income students are critical to assuring educational opportunities for students with the most limited ability to pay and critical to the future of our economy.”11

Indeed, Pell grants increase access for those who need it most. Almost three-quarters of of Pell recipients had family incomes less than or equal to $30,000.12 But this is not just a matter of equity. Our country also needs more students going to school and graduating. Along with increasing state investment, a key component of making college affordable again is a large-scale investment in the Pell grant. Ideally, Pell grants would increase at the pace of tuition inflation. Even with the federal deficit looming, we can at least ask in the near-term for a commitment from Congress and the Administration to fund Pell grants and halt the constant threat of cuts.

Use Pell to Guide Other Campus-Based Aid

Pell grants increase access, and in a recent Young Invincibles survey, about four out of five Pell grant recipients in a recent survey stated that access to grants made it more likely that they would complete/completed school.13 The program utilizes a well-targeted14 formula that pinpoints students who most need the help. Given the goal of increased access to students of all income backgrounds, we propose that the Pell grant program become the guiding basis for other, less-targeted campus-based aid.

Convert Federal Work Study into PellWorks

The Federal Work Study program (FWS) allocates $1 billion a year to colleges who in turn subsidize jobs for 1.5 million students.15 But the funding formula gives more money to schools that have been in the program longer, not necessarily those with students of greater need. Moreover, even though institutions can only provide subsidies to students with “financial need,” the method for calculating that need favors students with higher tuition costs. Many private schools spend their allotment by deeming high-income families needy because they still cannot pay their soaring tuition out-of-pocket. In fact, because higher income students tend to go to pricier schools,16 students from families making over $100,000 receive higher average awards than families making less than $40,000.17

Even if funding ends up at schools with high-need students, the funding choices left to schools do not always lead to funding going to those who need it most. It also allows schools to pull funding from students, perhaps as an upfront incentive to enroll. Kesha T., who attended a private college told us, “work study was only offered during my freshman and sophomore year. . . seems to be offered more to new students.

FWS also does not guarantee valuable experience: universities must align FWS and course-
work “as much as practicable,” a vague standard that does not ensure useful experience.\textsuperscript{18} As Kesha T. added: “It wasn’t really valuable besides getting to know other students.”

While many students have a positive experience with federal work study, we did hear a strong interest in improvements. For example, one student who completed her bachelor’s degree in business administration from Suffolk University found it to be difficult juggling a work-study program on top of an internship, and believed it would have been better if work-study was part of her internship instead of trying to do both. Indeed, in order to gain experience, students pile on unpaid internships on top of work study in order to afford school. Another stated that a work-study option related to her major “would have been much more valuable… part of my program … I had to do work study in the morning at the gym, then go to classes, and then do my internship in the evening.”

We propose to revamp FWS to create Pell-Works, a program that connects students to local employers. Schools would submit a Pell-Works proposal to the Department of Education, or potentially the state’s Department of Education or Department of Labor, who would receive an allocation of work study dollars based on the number of Pell students in each state. The application would request funding for the estimated number of PellWorks slots created and associated administrative costs. Most slots would need to be filled with Pell students, though schools could make the case for non-Pell students with significant need.

Each proposal would include a description of business partnerships where students can gain experience in their field through subsidized work. The state entity will show preference in allotting funds to community colleges, and schools with high Pell enrollment and a demonstrated ability to place students in high-need skills areas - though funds could still be used for on-campus work that builds skills or provide students with opportunities to increase campus involvement, particularly given the rural location of some campuses. Students could then choose to attend a PellWorks school, knowing that attending would avail themselves of relevant, subsidized work, and the PellWorks money. The grant could be available over the summer to help students who cannot afford an internship and no longer have access to summer Pell.

Given the value that students place in connecting their field of study to getting a good job, it is unsurprising that the vast majority of student leaders stated support for this specific proposal. The potential for this program could be enormous. With federal work study funding only providing a limited amount of money to test this program, we envision a long-term scaling up as the model proves its success.

**Convert FSEOG to PellPlus**

The Federal Supplemental Educational Opportunity Grant (FSEOG) program provides need-based grants to very low-income undergraduate students. However, the allocation formula is based on longevity in the program and cost of attendance. We instead propose converting FSEOG to PellPlus, a funding stream given to schools that enroll higher numbers of Pell students and graduates the highest percentage of students with high risk factors.

Currently, FSEOG grants can be used to pay for the costs of higher education, such as tuition and books. Using a statutory formula, ED allo-
icates funds based on the institution’s previous funding level and the aggregate need of eligible students in attendance in the prior year. The Federal government’s share of FSEOG funds cannot exceed 75 percent of the award amount; schools must allocate the rest. The Secretary of Education allocates FSEOG funds based on both base funding for schools that have participated in the program, and based on cost of attendance.

The institution makes the award determination once it has been allocated funds from the Federal government. The institution must give priority to students who are considered to have “exceptional need,” but must prioritize first those students who qualify for Pell grants. First the institution will award funds to students with the lowest expected family contribution AND who also receive Pell grants. Then, if the institution has funds left over, it will award the extra funds to eligible students with the lowest EFC, but who do not receive Pell grants. Once the full amount of the school’s FSEOG funds has been awarded to students, no more FSEOG awards can be made for that year. In other words, FSEOG funds are first come, first served. The average award is $716, though students can receive up to $4,000. While FSEOG grant programs are generally well-targeted, with 93.4 percent of its funding to students with total incomes under $50,000 schools with higher costs of attendance have access to a larger pool of aid.

Rather than basing allocation on longevity in the program or rewarding higher costs, this grant aid should be converted to PellPlus, to serve as the foundation for reward schools who 1) maintain a base percentage of Pell students and 2) achieve an increasing graduation rate for the lowest-income Pell students. Once the funding gets to campuses, it could be used to increase the Pell grant awards for recipients. A similar plan was proposed in the President’s 2012 budget request. If such as plan proves successful in bringing up graduation rates among those with the lowest graduation rates, larger investments into the program would be warranted.

By attaching these funding streams to Pell eligibility and ability to connect school to work, not cost of attendance or longevity, financial aid dollars will better follow students who need the help the most. Funding the Pell shortfall and revamping federal work study and FSEOG to better serve students will help increase access for those who need it most, fuel stronger relationships between schools and employers, and foster completion.

Reimagining Federal Student Loans

Grant aid used to pay for a much larger share of tuition, but that is no longer the case. As college tuition prices skyrocketed over the past three decades, student debt levels trailed closely behind. With few other options to cover rising costs, most students turn to loans to finance their education. In 1993, one in three graduating college seniors borrowed to pay for school, leaving with an average of $9,200 in debt. Now, two-thirds of students graduate with an average of $26,600 in debt. As a country, we hold one trillion dollars in student loans. Although the debt may be worth it for many, rising default rates and persistent delinquency make it clear that student loans do not pay off for everyone.

The past few years have brought significant changes to the student loan system. Interest
rates have fluctuated, new repayment plans have appeared, and Congress cut out middleman banks giving the Department of Education sole responsibility for issuing federal loans. There were also new disclosure requirements and a push to create easily navigable online comparison tools like the “College Navigator.”

Although many of the changes improved life significantly for students, the federal student loan system still does not meet important metrics. Recent adjustments notwithstanding, the Free Application for Federal Student Aid remains overly complex, and students frequently report trouble with the process. Student loan counseling falls seriously short of properly educating students about their options. Changes to student loan terms and conditions have created a system of more choice in repayment, but the system is too complicated for students to fully take advantage of that choice. It is no wonder that in a Young Invincibles survey of high debt borrowers, two-thirds reported that they misunderstood or were surprised by aspects of their student loans or the student loan process. As a student succinctly told us in a recent interview: “The information is too fragmented and complex. The system needs to be streamlined and simplified.”

We propose to do exactly that: dramatically simplify the federal student loan system and better prepare students to make important financial choices. We first detail how the status quo does not meet the principles of a successful financial aid system. Next, we outline steps to better serve the needs of this population by 1) overhauling our information and counseling system to ensure that students make good choices, and 2) converting the federal student loan system into a student loan insurance system, requiring that students repay no greater than what a graduate can afford, and that stakeholders meet certain metrics in order to access such a program.

The Status Quo: Good Policy, Weak Implementation

The federal government has made several positive changes to the student loan system over the past five years. Income-Based Repayment ensures that more students have an opportunity to make affordable payments on their federal loans. Cutting banks out as middlemen in the FFEL program created a simpler process where students would borrow federal loans from a single source through the Direct Loan system. The Department also now has a single website where borrowers can apply for repayment options, like Income-Based Repayment. Outside the federal realm, private lenders responded to the credit crunch by limiting their previous predatory practices. Consequently, more students now take out federal loans that typically have better terms over private loans. Each of these changes has helped students access financing options at a time when states are pulling back on investments in higher education.

Nevertheless, our federal student loan system is not yet where it needs to be. The inherent risks in taking out loans dissuade students who stand to benefit. Too few students receive clear information about their options, leading to disastrous financial consequences. Schools can enroll entire student bodies financed by federal loans, with no accountability mechanism to ensure that their degree earns enough to pay back their debt. As a result, we do not use our resources to best help students. Students cannot wait for state budget investments in higher education to stop shrinking, or for the federal government to ramp up grant aid; those bigger trends will take...
longer to reverse. Amidst this era of budgetary belt-tightening, the federal student loan system must function at its full potential.

**Loans Increase Access, Maybe Completion - But Could Do Better**

Intuitively, student loans increase access to college: with rising tuition, many, if not most, students would have no other way to finance their education. However, teasing out the size of the loans’ impact proves difficult. Many factors contribute to college enrollment, meaning that researchers cannot account for all the possible variables. Nor is there an easy way to conduct a randomized experiment to determine which factors matter most.  

There is little academic research on the impact of different loan terms; in fact, there is minimal research on the impact of loans themselves. The research that does exist on the impact of student loans on access turns up a mixed bag. For example, in a recent literature review commissioned by College Board, Donald Heller concludes that loans have little impact on college access and completion for most students. However, this analysis notes several major limitations to these existing studies, including the dramatic increase in borrowing in recent years to cover a greater percentage of tuition. Relatedly, loans have become a necessary part of college financing for even relatively low-cost institutions, rather than a way to pay for expensive private colleges. Given the dynamic changes, loans may have a far bigger impact on college access than they once did, and so it is not surprising that other studies suggest that financial aid has a positive effect on college enrollment and postgraduate studies. Our survey and interviews support this trend.

The relationship between student loans and completion also remains unclear. A study from the University of Alabama found no conclusive impact on college completion in a 2010 survey conducted at two universities. Specifically, the authors observed that students with loans of $10,000 to $30,000 were more likely to reduce hours or drop out than students with no debt. However, the trend did not apply to students with $30,000 or more in debt. One possible explanation is that when students took out enough loans to cover all expenses, they were more able to complete their degree.

In contrast, Rachel Dwyer from the University of North Carolina found that debt may have some effect on completion at a lower threshold amount. Their study compared the amount of student debt that private and public university students carry to the rate of graduation. Student loans appeared to have little impact on the graduation rate in private institutions, but students at public institutions show both positive and negative impacts. Specifically, college debt shows positive impacts on the graduation rate up to an amount of $10,000, after which the higher amounts of debt starts to show a negative impact on graduation rate.

On the other hand, there is more evidence that debt effects break down along socioeconomic lines. Studies show that Hispanic and low-income families are more debt-averse than higher-income families. Class-based perceptions of money and education impact a low-income family’s willingness to take on debt. Specifically, low-income families are less likely to borrow for education, and when they do, they tend to borrow less than the full amount. Students from such families are also more debt-averse than other students. Moreover, all socioeconomic
levels benefit from student loans, but the negative effects of debt are more apparent among students from lower-middle classes.\textsuperscript{51} Borrowers who had positive experiences with loans may also be more likely to borrow for college than those who did not have a positive experience.\textsuperscript{52} The direction of the research indicates that student loans do not help inexperienced, low-income, or Latino students access college as much as they could - a worrying sign in a system that increasingly relies on loans to finance higher education.

There is also data showing that loan repayment options may help overcome access barriers to student loans. Felicia Ionescu at Colgate University compares the 1986 implementation of federal loan consolidation and the income contingent repayment option to the 1992 changes in eligibility requirements that allowed more high-income families to qualify for federal loans; her model suggests that a student’s ability to consolidate loans into a single predictable interest rate or switch from standard payments to income contingent repayment increases the likelihood of college enrollment.\textsuperscript{53} These repayment options also decreased default rates. However, the change in eligibility requirements did not have a significant impact on college enrollment or default rates.\textsuperscript{54} She thus argues that a policy accounting for payment flexibility is more effective in promoting college enrollment and reducing default rates than a policy that targets eligibility requirements.\textsuperscript{55} The repayment options appear to reduce the risk of borrowing particularly for low-income families.\textsuperscript{56}

Ionescu’s findings have particular importance for our current financial aid system. A primary strategy to increase access through student loans comes in the form of subsidized loans for low-income students and families. Yet these products arguably increase access less effectively than favorable repayment plans. Although we have repayment plans, few people know about or take advantage of them.\textsuperscript{57} Our choice to favor eligibility requirements over repayment options may therefore hamper our ability to use student loans to increase access to higher education.

With rising tuition eclipsing college savings and the ability of a student to pay for school through work alone, student loans are increasingly becoming a key college access tool for students. But the evidence suggests that students of lower socioeconomic status fail to benefit from loans as much as others, and that we fail to use the most efficient methods to increase access. Additionally, too many students enroll and take out loans, but fail to complete school. We need a system that better utilizes our resources to help students to enroll in and complete higher education.

A Complicated Web

Because even astute higher education experts can get lost when navigating student loans, we first describe the system. Below is a short summary of current federal student loan options and their repayment plans.

Types of Federal Loans

**Stafford Loans**

Direct Stafford loans are federal student loans available through the U.S. Department of Education.\textsuperscript{58} To receive loans, students must be enrolled in a postsecondary institution for at least half-time. Unsubsi-
dized Stafford loans have an interest rate of 6.8%, accrue interest while in school, and capitalize when the student enters repayment. On the other hand, subsidized Stafford loans have an interest rate of 3.4% (though it will double without congressional action on July 1st, 2013) and do not accrue interest while in school. Repayments generally begin six months after graduation or six months after the student borrower stops enrolling at least half-time. Stafford loans may be included in a Federal Direct Consolidation Loan and are eligible for Income-Based Repayment and Public Service Loan Forgiveness programs.

Students face a cap on the amount of each type of loan they can take out each year.

PLUS Loans

For students and families that require additional financing beyond Stafford loans, the Department of Education offers PLUS loans to graduate or professional degree students (Grad PLUS loans) and to parents of dependent undergraduate students (Parent PLUS loans). PLUS loans have a fixed interest rate of 7.9%. A parent borrower may not transfer his or her Parent PLUS Loan to the child. The maximum amount of PLUS loans equals the student’s cost of attendance minus any other financial aid received. PLUS loans also require a minimum credit check to ensure that the borrower—either the student or the parent—does not have an adverse credit history. Parent PLUS loans are not eligible for Income-Based Repayment, and cannot be consolidated into a Consolidation loan to then reap those benefits.

Perkins Loans

Perkins loans are low-interest federal loans for undergraduate and graduate students with financial need. The loans run through the school, which means that a school that chooses to participate becomes the lender—not the federal government. The amount of awards depends on the school’s available funding and the students’ needs. Perkins loans carry a fixed interest rate of 5% and have a 9-month grace period, though that can differ for less than part-time students. Interest does not accrue while the student is enrolled. Perkins Loans can be a part of a Federal Direct Consolidation Loan, and then can use the Income-Based Repayment and Public Service Loan Forgiveness programs. These loans are also eligible for a number of other types of debt cancellation for working in fields such as policing, firefighting, or teaching.

Federal Loan Repayment Plans

Student borrowers can choose from 7 different repayment plans for their federal student loans: Standard, Graduated, Extended, Income-Based, Pay As You Earn, Income-Contingent, and Income-Sensitive. Each plan has different benefits and drawbacks. The table below from the U.S. Department of Education summarizes these repayment plans.
Standard Repayment

Under the Standard Repayment plan, student loan borrowers make a fixed monthly payment on their loans until the loans and interest are paid in full. There is a minimum monthly repayment amount of $50, and a maximum loan repayment period of 10 years. Standard Repayment is beneficial to higher-income borrowers who can afford to make potentially larger monthly payments, because these borrowers could pay off their loans more quickly and pay less in interest on the loans as a result.70

Graduated Repayment

Under Graduated Repayment, the borrower’s monthly payments start off low and increase every two years. The minimum monthly payment is the amount of interest that accrues between payments. As with Standard Repayment, the maximum repayment period is 10 years. Although monthly payments increase under this plan, no payment can be more than three times the amount of the previous payment. Graduated Repayment may make sense for a borrower whose income is low but who expects her income to increase steadily over time.71 As with Standard Repayment, borrowers in Graduated Repayment may pay their loans off more quickly and accrue less interest, but may need to make larger monthly payments as their repayment period progresses than they would under other plans.

Extended Repayment

Under Extended Repayment, borrowers make lower monthly payments over a longer period of time. The monthly repayment amount can be fixed or graduated, and the maximum repayment period is 25 years. The borrower must meet certain requirements to qualify for Extended Repayment on their Direct Loans and FFEL Program loans.72 Extended Repayment is good for borrowers who need to make lower monthly payments. However, because the repayment period is longer, borrowers in Extended Repayment will likely pay more in interest.73

Income-Based Repayment (IBR)

Under Income-Based Repayment (IBR), a borrower’s monthly payment amount is based on his income and family size. The monthly repayment amount is 15 percent of the borrower’s discretionary income, and is adjusted each year to reflect changes in the borrower’s income and family size. The monthly repayment is never more than the borrower’s repayment amount under the 10-year Standard Repayment plan, and will likely be lower than the repayment amounts under other plans.74 The borrower’s repayment period can be more than 10 years but is capped at 25 years, and the borrower’s remaining loan balance is forgiven after 25 years of qualifying repayment (10 years if the borrower is in public service).75
Starting in 2014, IBR will look more like Pay as You Earn, with a 20-year repayment cap and monthly payments capped at 10 percent of income. Because the borrower’s monthly payments are based on income and adjusted to reflect changes in the borrower’s financial situation, a borrower will not be required to pay more than he can afford each month. Moreover, there is a limit on the capitalization of interest when a borrower is in IBR. The drawbacks to IBR are that the borrower may pay more in interest because the repayment period is longer and may have to pay taxes on the amount of the loan that is forgiven.

Pay As You Earn Repayment Plan

Under the new Pay As Your Earn plan, monthly payments are also based on the borrower’s income and family size, and are usually lower than they are under the other plans. The monthly repayment amount is 10 percent of the borrower’s discretionary income, and is adjusted each year to reflect changes in income and family size. The monthly payment is never more than the borrower’s repayment amount under the 10-year Standard Plan. The borrower’s repayment period is capped at 20 years, and the borrower’s remaining loan balance is forgiven after 20 years of qualifying repayment. The Pay As You Earn plan is only available for Direct Loans. The borrower “also must be a new borrower as of Oct. 1, 2007, and must have received a disbursement of a Direct Loan on or after Oct. 1, 2011.”

Otherwise, the plan is similar to IBR, except that if you no longer have a partial financial hardship, interest capitalization will be limited to 10 percent of the original balance.

Income-Contingent Repayment

Income-Contingent Repayment (ICR) is for borrowers who “need to make lower Direct Loan payments, but . . . do not qualify for the IBR or Pay As You Earn plans.” Monthly payments are calculated based on the borrower’s adjusted gross income (AGI), family size, and total amount of Direct Loans. The maximum repayment period is 25 years, after which any remaining loan balance is forgiven. Borrowers in ICR benefit from lower monthly payments and loan forgiveness after 25 years. In addition, borrowers receive a “ten percent capitalization benefit;” if the borrower’s payment amount is less than the amount of interest that accrues, the interest is capitalized once each year until the balance is 10 percent higher than the original loan balance – after that, the “interest continues to accrue but is not capitalized.”

Income-Sensitive Repayment

Income-Sensitive Repayment (ISR) is available to borrowers with FFEL Loans who need to make lower monthly payments. Monthly payments are adjusted based on the borrower’s income, and the maximum repayment period is 10 years.
Untangling the Web

These varying loan and repayment programs are, to say the least, bewildering for students. The interest rates, interest accrual, capitalization requirements, eligibility, loan limits, repayment options, and debt cancellation programs vary dramatically, creating a complicated web of cost permutations that a typical student struggles to unravel.

Unfortunately, students rarely receive a helpful explanation of their options. Some of the challenge is inherent in the task, stemming from the population being served. By nature, graduating college students have less experience with basic financial decisions than older adults. Nevertheless, they must make a series of choices about how to pay for school that could leave them with loan payments for decades. Moreover, many teenagers lack information about their future careers. Some may know exactly what they want to do, but often students will change their major before they graduate. The lack of information increases the risks of taking on large amounts of debt. As one interviewee said “it’s a balance of finding what you like, versus what will make you money; ... for me trying to figure out that balance - I started out as a pre-med student from pressure ... I later dropped that for political science because that’s where my interest was, and my plan was to go to law school - I ended up in business school.”

The age-related challenges are solvable, but our financial aid system makes things harder than necessary on students, particularly with private lender options also on the table. As a recent report from the Federal Reserve Bank of Kansas City notes, “[t]he market for student loans is complex, with a wide range of institutions, products and relationships.” It is no surprise that in a Young Invincibles survey of high debt borrowers, about two-thirds of private loan holders said that they did not understand the major differences between their private and federal options. Shockingly, the responses included those who took out both private and federal loans.

A convoluted system compounds the problem at every step. The student aid process begins with the FAFSA, a document with around 120 questions that students must fill out to receive aid. It is even more difficult for students who are new to the process, or families who speak English as a second language. Further, nearly 35% of post-secondary students are the first in their family to go to college and therefore lack a natural guide. A Sallie Mae backed survey among low-income students and families found that 86% of Latino parents did not name grants as a source of financial aid, as compared to 62% of all parents. An estimated 2.3 million students in 2007-2008 who would have qualified for financial aid failed to file the FAFSA.

Following completion of the FAFSA, students receive their award letters. The mixture of scholarships, grants and loans can be difficult to compare across schools. Sometimes it appears deliberately misleading, with students accepting debt that has been packaged as ‘aid’. Award letters are so complicated that over 90% of federal financial aid recipients in our survey support standardizing their format, terminology and content.

Unfortunately, students receive too little help navigating the maze. In our recent survey, we asked students and recent graduates with high levels of debt whether they thought they had received accurate information about their grants...
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and loans. Four in ten federal loan borrowers answered “no” or “don’t know.” Recent graduates reported receiving accurate information roughly ten percentage points less than current students, suggesting that when loans came due, students discovered terms and conditions that surprised them. Thus, even when transparent facts are made available, students may still find themselves lost without a helping hand.

Worse still, although federal law mandates that federal borrowers receive counseling, four in ten high-debt borrowers reported that they had not had such counseling. Some schools may be out of compliance, though this statistic likely points to the inadequacy of student loan counseling itself. Technically, schools may mail a paper description of the loan process to students who must sign and return the form, or send a mass email with a link to the federal student exit counseling website. While that may qualify as “counseling” under an overly broad interpretation of federal law, few students would recognize it as such. The information requirements appear ill-designed to ensure students receive and understand what they need to successfully apply for loans. In short, the combination of complexity and poor information provision undermines transparency in the student loan system.

Without adequate counseling, many students navigate the system solo. But the information that students look for can be hard to find. Karen H., who studied at Columbia University is a good example. She filled out her FAFSA alone and isn’t confident in her understanding of the financial aid process telling us that “[i]t can definitely be confusing, very overwhelming and ... it’s hard to keep up with.” A litany of confusing sources makes it difficult for students to put together information, even when they can find it. US News and World Report, Department of Education federal aid sites, College Navigator, Department of Labor career search engines, state labor statistics site, college websites, and scholarship search engines are just a few of the information sources that a student may try to navigate to make more informed decisions about schools and college financing.

Accountability

Finally, the federal student loan system does not do enough to ensure that stakeholders who benefit from receiving federal dollars promote student success. In one sense, the federal student loan system is among the most accountable of institutions, in that borrowers face severe consequences if they fail to pay back what they owe; loans are not dischargeable in bankruptcy. More so than most any loan, students are held to a higher standard in repayment.

On the other hand, the institutions that educate students often face a much lower performance bar. Each year, higher education institutions receive billions of dollars of grants and loans in the form of tuition payments. However, there is little consequence for schools that fail to graduate most of their students or leave others with degrees that have little value in the job market.

Recently, the Department of Education instituted an accountability mechanism known as the gainful employment regulations. The Department focused on for-profit colleges due to their graduates’ extremely high debt levels and disappointing history of paying back their loans. The rule set a minimum standard for these schools to achieve based on the ability of students to pay back their loans. The rule set a minimum standard for these schools to achieve based on the ability of students to pay back their loans. For schools to comply, in at least 2 out of 4 consecutive years they must at
least meet 1 of the following 3 standards related to recent graduates: 1) 35% are paying back their loans; 2) they have a debt to earnings ratio of 12% or less; 3) or they have less than 30% of discretionary income going to student loans.\textsuperscript{102} Failing to meet this test disqualifies a for-profit institution from receiving most federal financial aid.

In a recent court case, Association of Private Sector Colleges and Universities v. Duncan\textsuperscript{103}, the court vacated and remanded the regulation. While the court agreed the Department of Education has the proper authority to regulate gainful employment\textsuperscript{104}, one of the three standards, the loan repayment rate lacked a “reasonable basis.”\textsuperscript{105} It is unclear what will happen next with the regulation, but even without the troubles of a lawsuit over these regulations, the federal student loan system still lacks a significant level of accountability. First, the gainful employment regulations set a low bar. Schools can pass the test with 60 percent of graduates not in repayment, regardless of the amount of income recent graduates have compared to their debt levels. Second, the rule only applies to a slice of the higher education sector. Most students attend public or private not for profit institutions that, although perform better in aggregate, should still be held accountable for student success.

Finally, students themselves have little means to hold institutions accountable. Weak disclosure requirements in the Higher Education Act mean that information provided by school on graduation and job placement is meager at best.\textsuperscript{106} The Department of Education fails to collect enough data that would allow students across the country to compare schools based on the career outcomes of their graduates. With the right information in hand – and enough counseling aid to interpret that data - students would have the opportunity to reward good schools and punish poor ones by attending the highest performers. Solving these problems is essential for successful financial aid reform because, while good policy is crucial, it becomes far less effective if students do not know how to take advantage of it.

\section*{Solutions: Inform and Insure}

To address the shortcomings described above, we call for two major changes to the federal loan system. First, we must revamp the on-ramp to federal loans so that new borrowers can make smart, informed choices. To do so, we must simplify the application process, bolster counseling, and streamline online information sources. Second, we propose converting the federal student loan system into student loan insurance, creating a simpler, singular loan with automatic income-based repayment and straightforward cancellation options. The new paradigm would serve as an insurance plan so that students know going into school that they will be able to afford to pay back their loans.

\section*{I. Invest in Information}

Students will not be able to take advantage of college financing options if they are not made aware of them. Nor will they be able to make smart college choices with that aid if they are not provided with and counseled on important data points. Among those who left school with the highest amount of debt, 65\% experienced misunderstandings and surprises about aspects of their own loans and the loan process in general.\textsuperscript{107} At the same time, 40\% of those borrowers reported not receiving accurate information or being unsure of whether or not the information they received about their loans was accurate.\textsuperscript{108}
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The dearth of information can be devastatingly expensive. We owe it to students to give them the tools to make good decisions.

In order to bring greater accountability and transparency to the process, we propose 1) bolstering federal loan counseling as well as the number of well-trained high school counselors, 2) creating a centralized web tool that provides students with all the relevant data they need in choosing a school that is right for them, and 3) simplifying the FAFSA and award letters. The sum of these reforms would offer not only greater transparency, but also access for students who are often lost and intimidated by the complexity of the financial aid process.

Student Loan Counseling

The Young Invincibles student survey shows that students want more from federally mandated student loan counseling. Over half of respondents surveyed want better information about interest rates, repayment options and timelines, consolidation options, and information on the total amount owed and estimated monthly payments. Two overarching themes emerged from these responses. First, many students want more information about the terms they are already federally mandated to receive - suggesting existing counseling is inadequate. Second, students want more personalized information about their student loans. As one respondent put it: “What I didn’t really understand was how much I would be having to pay back per month. I wish that there could have been a simulator – i.e. here’s what’s available to you. If you do this option with this repayment plan, here’s how much you’ll be on the hook for in a given month...”

Our research suggests that students are hungry for personalized feedback to help them better plan for their financial futures, and that the quality of online student loan counseling must improve. It is currently too easy for students to “click through” pages of information and answer online quizzes, without actually absorbing the information. A more interactive and challenging online counseling process could be one option to help students better retain information. Certainly, individual students should do more to educate themselves, but the problems are so systematic and widespread that it is incumbent upon school financial aid offices and the Department of Education to aim higher.

A sizable minority of students also expressed a desire for more personal contact with their financial aid office. One respondent commented that “I would have a financial professional employed for the purpose of walking people through the process step by step... To help explain the system of interest and payment especially for students with little real life experience coming from high school.” What is striking about comments like these is that colleges already have financial aid administrators employed for this very purpose. Yet too many students appear not to have interacted with them.

Below are three ways to bolster the financial aid counseling system for students.

A. Enforcement

First, the Department of Education must enforced the federal counseling requirements. The intent of the law was to ensure students were meaningfully informed about their student loans. Counseling in name only is unacceptable. The Department of Education must act immediately to set more clear and strict standards.
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for counseling, and then audit school counseling procedures to ensure they are adequate. Schools should also be held accountable for providing both highly-trained and an adequate number of counselors to address the needs of their student population.

B. New Counseling Tools

The Department of Education federal student aid counseling can also be improved significantly by creating an interface that allows counselors to walk through the process with students step-by-step, and give personalized attention to the unique situation of each student. This would give students a more tangible idea about the process, the actual size of their loan, and what it will really mean for their future.

C. Strengthen High School Counseling

One possibility to improve personal interaction is to start early. High school counselors occupy a potentially pivotal position in impacting a student’s college, financial aid, and career choices, particularly for low-income and minority students. As another expert puts it: “Research clearly shows that counselors, when consistently and frequently available and allowed to provide direct services to students and parents, can be a highly effective group of professionals who positively affect students’ aspirations, achievements, and financial aid knowledge.”

However, the system is far too stressed to expect counselors to take on financial aid counseling. The recommended student to counselor ratio is 250:1, but state budget cuts mean that nationally we average a dismal 476:1. The lack in personnel forces counselors to spend time dealing with behavior emergencies, and not enough on the college and career planning. Not surprisingly, few students in our survey report receiving financial aid information from counselors, although between one-fifth and one-quarter of respondents wanted more information from their counselors.

Counselors want to provide more help with financial aid, but find themselves badly understaffed and under-resourced. In a recent national survey of high school counselors, half reported that they would spend more time counseling on financial aid if they had the time. The survey noted that the counselors “are eager to receive professional development, and that these trainings can, and should, be targeted at critical levers like college and career readiness, financial aid and the use of technology to promote these goals.”

The federal government could incentivize states to invest in and take innovative approaches to high school counseling. For example, the Obama Administration’s Race to the Top (RTT) program incentivized states to implement education reforms and set student achievement goals. However, RTT contained no language regarding school counseling services. Future efforts to expand or develop RTT-like programs should include legislative or regulatory incentives that challenge schools to increase the number of counselors, promote professional development, and improve the effectiveness of their programs.

There is also an enormous opportunity to supplement school counselors with help from paid or volunteer college students or recent graduates. These young people can by no means replace trained school counselors, but they can provide academic advice, career planning, help with college applications, student intake and
follow-ups, and organize student activities. Several promising non-profits across the country already implement some form of this model in low-income high schools. Moreover, Senator Durbin has introduced legislation that would help fund similar post-secondary coaching programs. Scaling up an effort like this could go a long way toward supporting the work of school counselors across the country. The use of AmeriCorps funds to send more counselors into schools could also help bolster the number of counselors.

**DegreeLink**

The Department of Education should take the lead on creating a web tool, DegreeLink, that would provide consumer information for prospective students about the performance of colleges of interest, post-graduate employment rates, financing options, labor market data, and credentials needed to perform a specific job or career. This site would better integrate aid and loan applications with college search tools and employment statistics by major and region. Essentially, federal and state education agencies would create a one-stop shop for students looking to pursue a degree. This includes coordinating existing information portals to provide information on federal grants, loans, state aid programs, student outcomes within the same system, combining College Navigator, FAFSA, Net Price Calculators, CareerOneStop, and Direct Loans into one dynamic online system. A student looking to apply for financial aid should be able to go into DegreeLink, search for schools with high graduation rates or net price for students with similar backgrounds, and review a school’s placement rates for careers in high-need fields in their region – while also filling out information needed to obtain federal aid.

Importantly, by connecting this site to FAFSA, we could ensure huge traffic and that millions of students would access the types of information they need to make sound educational and financial decisions. In that sense, DegreeLink would function like health care exchanges set up by the Affordable Care Act. Prospective or current students should also be able to use the site to search for careers that are in high demand in their region, which will help them as they choose a postsecondary path. The site should incorporate existing data available through CareerOneStop and other forums, and even provide tax breaks for employers who post job openings and hiring data through DegreeLink. The site would then aggregate state and local opportunities, allowing future students to search through growing fields in their region. DegreeLink would also be a way to incorporate new data that the Department receives from a consolidated loan program described below.

Lacking knowledge about the true cost of college is a double-edged sword that not only causes some students to underestimate cost but also causes others, nearly six in ten families, to rule out certain colleges based on sticker price alone without considering the substantially cheaper net cost. College Navigator was a step in the right direction, but its maze of information and interface does not quite get students to the place they need to go, and the back-end information such as employment rate by school does not exist. In order for students to make the most of their federal aid, we need a system like DegreeLink that provides them the data they need, when they need it.

**FAFSA & Award Letter Simplification**

Finally, the on-ramp to the financial aid process
needs further simplification. FAFSA should be streamlined beyond its 2009 improvements, removing unnecessary questions to ensure that all eligible students are able to wade through the process. With over one hundred questions, many having nothing to do with financial aid, it came as no surprise that our survey respondents frequently described it as “complex” and “confusing.”

Financial aid award letters also have room for improvement. Recognizing this, the Department of Education recently released the model Financial Aid Shopping Sheet that includes standardized estimates of cost of attendance, grants, scholarships, and loans across schools. At this point, over three hundred schools have adopted this standard format. Over 90% of the students in our survey supported scaling up a proposal to standardize form, content, and term definitions of financial aid award letters for colleges across the country. Taken together, the proposals above could go a long way toward increasing transparency, and ultimately access to higher education.

II. Student Loan Insurance

In order to overhaul the current loan system, we propose simplifying the current student loan program by converting it to one type of loan, with automatic enrollment in an insurance-like income based repayment system that protects graduates against short-term economic distress. The system would function like insurance: students would effectively be adding an insurance policy to their loans that protects them against low incomes and unemployment after school. Currently, complicated administrative processes and limited outreach cause too few people to take advantage of income-based repayment despite the clear benefits. Automatic enrollment in income-based repayment would fix the income-based repayment enrollment problem that currently exists and dramatically reduce defaults, while at the same time increasing post-graduation data and facilitating a mechanism for the public to hold schools accountable.

A single loan with an income-based repayment system would better address our goals for federal financial aid than the status quo. First, borrowers would benefit tremendously from a simplification of the financial aid process. They would have an easier time comparing financial aid awards, students would be able to calculate future monthly payments, and counselors would have a simpler time explaining the process. When they graduate, students would skip the current complex consolidation and IBR selection process altogether, immediately enrolling in IBR with their one loan. Far more people will pay an affordable amount of their student loans, avoiding defaults and the disastrous personal financial consequences that come with it. As Bruce W., a second year student at Harold Washington College who didn’t know about IBR until we spoke with him remarked: “students should be automatically enrolled; they might be struggling to pay their loans and not know that this is an option.”

The federal government would also save on pricely collection fees and administrative expenses associated with signing people up for one of the six or seven repayment plans. A simpler system has less administrative expense.

Second, improving repayment terms for all borrowers is likely a more cost-effective and better-targeted way to increase access than offering a lower interest rate for more middle-income borrowers. As recent research suggests, policies
that improve loan repayment options appear to have more positive affect on enrollment among low-income students than those that lower interest rates. A single student loan with income-based repayment as insurance reduces the risk that college will not pay off, alleviating a major fear of students and parents, and thereby could increase enrollment. It reduces the post-college debt burden by subsidizing payments for graduates who are struggling to find decent work in a bad economy.

Income based repayment does more to match the federal dollars to those who need it the most. For example, a borrower who leaves school with a high-income job pays more, which in turn subsidizes payments for struggling graduates who temporarily cannot find a job after school. That is the essence of insurance. It is also a more progressive system than one that lowers interest rates across the board, and thereby spends that government subsidy on a high-income graduate who does not need it.

Third, borrowers would still retain the freedom to pay back their loans as quickly as they choose, or to apply to the Department of Education to take into account special circumstances on their payments. As discussed previously, almost 90 percent of respondents strongly agreed or agreed with being automatically enrolled in the income-based repayment plan. Students who did have hesitation generally wondered about staying in a loan repayment program for such a long period of time. To address those concerns, higher earners would be encouraged to pay as much as they were able to avoid the longer pay-out of accrued interest. However, with a more progressive IBR formula at the higher income levels, the required payments should be able to incorporate that enhanced ability to pay.

Finally, the automatic IBR allows for a simpler message to students about college affordability. It still incentivizes students to borrow wisely and frugally, or else face a long term of repayment. But it also ensures that students will no longer face the disastrous consequences of a recession full of debt collectors and joblessness. In essence, loan repayment insurance simplifies the system and sends the message to all students: our economy needs college degrees and the federal government has an interest in ensuring that you get that degree. Student loan insurance can help calm growing fear among students of un-supportable debt, fear that could deter students from enrolling.

Any remaining skeptics should take note that this proposal has been tried before – and worked. Peer countries such as the United Kingdom, Australia, and New Zealand already implement similar systems effectively. In New Zealand, graduates pay back their student loans through their tax returns, paying back 10 cents of every dollar above a baseline threshold. Similar to the payroll tax in the United States, employers simply make student loan repayment deductions on their paychecks. New Zealand’s system dramatically reduces the administrative burden for students, schools, and the government. Moreover, the system ensures that all students can pay back their loans. Although New Zealanders take out much smaller amounts than their American counterparts, they typically pay back their loans within 6 years. The major downside to New Zealand’s plan is its cost: loans are interest free for graduates who stay in the country, which requires the government to heavily subsidize loans. However this poses little problem to the United States, because our student system essentially pays for itself, and
we do not propose changing that dynamic.\textsuperscript{130}

### A Single Interest Rate Plus Automatic IBR: Pros and Cons

A student loan insurance plan would necessarily shift resources from subsiding interest rates to ensuring student loan repayment. However, given that all students would automatically enroll in a plan that allows them to pay back their loans based on their income, it would obviate the need for subsidized interest rates up front. The federal government would be able to set a single interest rate for all students. Given current fiscal constraints, we propose setting that rate at a point that would ensure the program would be budget neutral over the long run.

Skeptics of a single interest rate might argue that it prevents targeting affordable options to low-income students. Interest subsidies do further affordability - particularly for students who end up in lower wage jobs after graduation, and certainly for this who do not complete but must still pay back the debt. But, as explained above, they are not always well-targeted. A student from a low-income background who goes on to a high salary job would have no trouble paying a sizeable monthly payment while a middle class student moving to a rural area to work as a teacher would have more trouble. Federal dollars would be better spent on those who made the right decision to go to college but are struggling to repay during an economic downturn. As the economy improves, they will have a better ability to repay.

Another counter argument might follow that we are forcing high-income graduates to subsidize low salary students. This ignores the basic principles of insurance. Student loan insurance asks students before they take out the loans to borrow at a rate that will allow them to pay back their college education based on their income thereafter. For the vast majority of 18-year-olds, there is little certainty about their future. They may end up with a high salary, or fall short of the competitive position they seek. They may end up in a field with lay-offs, or graduate during a recession. The lack of information about outcomes justifies an insurance scheme that, rather than collect premiums during school, does so after graduation.

The focus on post-graduation targeting would be less convincing if there was more evidence that lower interest rates based on family income improves college access or completion. But in fact, the little research that does exist favors repayment plans as a preferred policy for increasing college access.\textsuperscript{131} Interest rate subsidies only further access to the extent that such a borrower understands upfront that he or she would pay less, and that it would have changed the students mind on whether to attend college (or where to attend college). Given the low levels of information among loan applicants and inherent uncertainty in predicting future earnings, federal loan subsidies, unlike straightforward grant aid, appear ill-designed to further college access for low-income students.

For now, however, interest rate subsidies are the only comprehensive mechanism that we have to attempt to target these loans based on ability to pay. Thus, we would only support consolidating interest rates if it was accompanied by the comprehensive insurance plan described above. We also support further research to determine how much interest rate subsidies further college access. Such requirements would ensure that borrowers pay back their loans as quickly as possible, helping to keep costs down for the loan program, while ensuring that low-income struggling borrowers are protected.
There are a variety of potential options to set the interest rate. Having a single, fixed interest rate set by Congress has some advantages. Most importantly, it is simpler for students. Right now students with multiple types of loans face multiple types of rates. Moreover, those rates can change on the same loans from year to year based on changes in the law. This adds unnecessary confusion. On the other hand, a fixed interest rate fails to respond to market conditions. While students taking out fixed interest rate Stafford loans did well before the market crashed, many now pay far more than the market rate for loans. Some Grad PLUS loans are now fixed at 8.6% are likely far higher than necessary when the Federal Open Market Committee interest rates hover close to 0.

Another option is to choose a fixed interest rate that varies with market conditions. This option mirrors the advantages and disadvantages of a single fixed interest rate. Namely, a variable interest rate responds to the market, ensuring that students get a competitive deal on the loans they take out. However, the rate will fluctuate year-to-year, meaning that students will again have a variety of interest rates on the loans that they hold. It will also favor some generations of students who are lucky enough to attend school when interest rates are low. One way for Congress to reduce risk to borrowers would be to choose a variable interest rate, but impose a cap so that students are never caught paying exorbitant amounts.

Finally, Congress could also choose a truly variable rate that responds to market conditions over the life of then loan. In this way, all borrowers would face the same rate no matter when they attended school. An individual borrower’s interest rates from loans taken out in different years would be the same as well. However, the interest rate would fluctuate from year to year dramatically increasing risk in the long run. This option would make it unnecessarily difficult for students to plan ahead.

**Debt Cancellation**

The student loan insurance system also offers a way to streamline debt cancellation options. Currently, federal Perkins loans offer low interest rates and cancellation for a number of different professions including teachers at low-income schools, nurses, child or family services workers, Head Start employees, law enforcement officers, military service-members, childcare workers, and firefighters among others. Federal loans also offer cancellation generally for those who join the income-based repayment program for 20 or 25 years. People with federal loans who work in public service for 10 years will also receive full forgiveness on their loans. However, the system lacks a clear signal to students about which tracks offer forgiveness. Many borrowers, if not a majority, are unaware that they are eligible for cancellation.

Having a single student loan and automatic IBR provides a natural avenue to alert students to their cancellation options, because they will all continue to receive IBR updates and notifications after college, and will not have to reconcile different cancellation options among different types of loans. Borrowers will no longer be “lost,” but remain part of a central information pathway. Creating such a system is essential. As debt levels grow, we risk discouraging high-skilled workers from pursuing the public good. We need quality doctors, nurses, and teachers in rural areas, but high debt levels may prevent them from
moving there. Currently, the complex system of debt cancellation makes it difficult for students to understand their benefits. A single loan system will allow the country to send a clear signal that certain career paths and the pursuit of the public interest will receive incentives. Generally, we support maintaining current features that allow full cancellation for public service after 10 years and for all other loans after 20 years.

**Holding Schools Accountable**

As described above, the current federal student loan system lacks accountability. Schools may enroll students almost entirely funded by federal loans and grants with little consequence for low graduation or job placement rates. The one exception applies only to the very worst performers in the for-profit sector. The lack of accountability would present a problem if the federal government chose to implement student loan insurance. Students would pay back only what they can afford, defaults would plummet, there would be even less incentive on the part of institutions to ensure that their students graduate into decent paying jobs: schools would never look bad. *As a result, a conversion to student loan insurance is only feasible if it is accompanied by significant accountability metrics.*

The most straightforward option would be to model an accountability mechanism similar to the gainful employment regulations, but apply them to all schools, and enforce stricter standards. However, the gainful employment rule would need modifications to adjust to a student loan insurance system. In the latter, defaults would not exist, so it would make little sense to grade schools on their default rate. Moreover, if students pay based on their income, their debt to income ratios would also never rise to levels that cause alarm, even if the total debt level skyrockets.

Instead, the government could set a minimum standard for the dollar amount of loans students are able to pay back. For example, if too few students made progress paying down their principal, a school could face penalties. Given that all students would automatically enroll their federal loans in the same repayment plan, the federal government would have income and debt information about every school’s former students. This would allow the government to easily make calculations about a school’s success rate without forcing institutions to collect and submit data through a costly process. Such accountability metrics would incentivize schools to:

1. **Better connect students to high-paying jobs;**
2. **Reduce the overall debt burden on students by providing more grant aid;** and,
3. **Reduce the overall cost of the college.**

There are certainly unintended consequences of accountability mechanisms that policy reform must avoid. Typically, disadvantaged students have the lowest graduation rates. Faced with penalties for failing to graduate students into higher-paying jobs that require a degree, schools might decide to give fewer low-income students a chance to enroll. As our survey and interview findings above report, students have an intuitive grasp of this objection. In the interviews and survey questions respondents expressed concerns that punishing institutions would unfairly hurt students at those schools. In fact, they preferred incentives for success rather than accountability mechanisms targeted at the schools they attend.

Their feedback caused us to rethink how to
structure institutional accountability mechanisms targeted at institutions, and prevent any negative consequences for students. We propose three possible ways for doing so. First, the scheme could use regression analysis to take the characteristics of a particular school’s student body into account when applying accountability mechanisms. It could consider attributes such as household income, race, ethnicity, sex, SAT scores, high-school GPA and any other accessible, relevant variables to ensure that schools that focus on accepting the least-advantaged students are not punished for doing so. The Department of Labor Employment and Training administration already uses regression models in its performance system; there is no reason why the Department of Education cannot do the same.

Second, the accountability formula would need to take into account the type of institution. Community colleges for a variety of reasons have lower rates of graduation, some of which a regression model based on demographics may not be able to capture. They should not be held to the same standard as four-year schools.

Finally, the federal government could implement penalties on a rising scale to avoid shutting down schools that might still be able to benefit students. For instance, rather than take away all federal aid to a school that missed a yearly target, the Department of Education would limit total federal grants and loans to that institution for the entering class the following year, or charge a public fine to the school. This would provide schools a chance to improve their graduation rates rather than losing all financial aid which would effectively shut them down, as well as alleviate concerns of students who worry that draconian penalties would unfairly harm students. The right balance of accountability mechanisms and safeguards for the least-advantaged students would improve accountability and ensure access to those who need it most.

As students and families navigate the complex web of financial aid, they need more help, better information, and a loan system devoid of the harsh punishments that it currently holds. An overhaul of our entry way into federal aid, a remodeling of the loan repayment system, and a requirement that schools make good use of federal money are all important tools to achieve those goals.

Reform Higher Education Tax Benefits to Increase Access, Lower Debt

Tax credits for families who send their kids to college improve affordability, often by several thousands dollars a year. The benefits are particularly useful for middle-income families to reduce costs and limit the debt that a student must take on. But while the higher education tax benefits system makes college more affordable for some families, the current system has flaws, failing to increase access to college for low-income students and providing loopholes for schools at a time when Pell grants face a shortfall. Though there are 18 total higher education-related tax credits, we examine two of the most expensive ones: tax-exempt bonds for institutions and tax credits for educational expenses. Both of these tax expenditures should be better targeted, particularly at time of budgetary belt-tightening. Low-income students receive fewer benefits from these programs than middle- and high-income students, tax benefits come too late and are too complex, and
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schools rather than students benefit from some. Money is spent on indirect tax incentives that could instead be directly invested into the Pell grant program, which has been show to increase access to higher education among the neediest students. We propose the following:

- First, policymakers should eliminate or reform tax-exempt qualified 501(c)(3) bonds for private educational institutions and invest the federal savings into the Pell grant program to fill at least half of the impending shortfall. At a minimum, more research should be done on ways to modify the bond program, which currently gives a windfall to high-income bond purchasers.

- Second, policymakers should consider consolidating the higher education tax credits for individuals into one improved American Opportunity Tax Credit (AOTC) that is easier to understand and can be better used by low- and middle-income students.

The tax benefits discussed in this paper are part of a larger federal expenditure program intended to help families pay for higher education. Using tax expenditures to pay for spending may not be feasible during an appropriations process, but rather should be implemented during a comprehensive reform to the Higher Education Act. Higher education funding has been slashed enough over the last few years; eliminating any higher education-related budgetary costs must be used to pay for higher education expenditures that benefit students more efficiently.

**Tax-Exempt Qualified 501(c)(3) Bonds**

This section will examine the tax-exempt qualified 501(c)(3) bonds, a higher education tax program that benefits institutions. Private colleges and universities can issue tax-exempt bonds, called qualified 501(c)(3) bonds, to raise capital for building construction or repay previously issued bonds. State and local governments issue these bonds to higher education institutions, which then sell the bonds to private bond purchasers. The tax-exempt status of these bonds saves schools money because the schools can pay lower interest rates to bond buyers; and bond purchasers are willing to accept a lower return because they do not have to pay taxes on the bond interest. The exclusion of interest on the bonds for private non-profit educational facilities are expected to cost the federal government close to $3.7 billion in 2013.

In practice, most tax-exempt bonds issued by colleges and universities are used to raise capital for building construction and to refinance or refund earlier bonds issued. Though it is difficult to find sector-wide information, an examination of the financial statements of colleges and universities and the statements of conduit issuers show consistency in use: repayment of prior bonds coming due and capital improvements. For example Boston University used $117 million in proceeds “to fund a partial redemption of Series H variable rate bonds.” Mount Ida College relied on $26 million in proceeds “to refund previous debt and to replace its main athletic field with a new artificial turf and expand its existing practice field into a regulation-size grass playing surface.” These purposes certainly provide value to the universities, but raise questions about priorities in the use of federal funds.

Tax-exempt qualified 501(c)(3) bonds are inefficient because rather than the government providing a direct payment to schools for qualifying projects, schools indirectly raise money from...
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private bond buyers at a government-subsidized interest rate. The primary beneficiaries of this government subsidy are not students or their families, but instead the private colleges and universities that issue the bonds and bondholders at the highest marginal income tax rate who purchase them. While schools may argue that students reap the benefits indirectly through nicer facilities, it is difficult to argue that a nicer basketball arena is a more important government investment than subsidizing the tuition of a low-income student through a Pell grant.

Although many schools may argue that they need funding for essential buildings, many have shown the ability to raise substantial resources in the form of endowments. A National Association of College and University Business Officers survey of 823 schools found that in FY2011, endowments returned an average of 19.2%, while the average endowment spending rate was 4.6%. The total value of the endowments examined was $408.1 billion, and of the 615 institutions that carried debt, the average debt amount was $189 million and the median amount was $56.2 million. This endowment wealth is not distributed evenly. As the College Board points out, “ten private doctoral universities hold about 45% of the total endowment assets of all private four-year institutions.” However, the statistics do demonstrate that schools can raise a lot of capital, and that many of them have enough endowment resources to help finance major capital projects.

One major concern about tax-exempt qualified 501(c)(3) bonds is that private colleges and universities are using tax-exempt bonds to commit indirect tax arbitrage. Tax arbitrage is “the use of proceeds from lower-cost tax-exempt bonds to directly finance the purchase of higher-yield securities” and is prohibited by law. In 2010, the Congressional Budget Office examined whether colleges and universities are engaging in an indirect form of tax arbitrage, wherein the schools issue less costly tax-exempt bonds to finance capital improvements while holding onto other investments, like stocks and other financial instruments purchased with endowment funds, that earn a greater return than what the schools pay out in interest rates on their tax-exempt bonds. The CBO concluded that “[to the extent that colleges and universities earn an untaxed return on investments that exceeds the interest they pay on tax exempt debt, they are benefiting from a form of indirect tax arbitrage.” Giving tax-exempt bonds to schools that could pay for these capital improvements with their other higher-yield investments is an inefficient use of a higher education expenditure.

Tax-Exempt Bonds Provide a Windfall to High-Income Bond Purchasers

Purchasers of qualified 501(c)(3) bonds in the highest tax bracket gain a windfall in tax advantages that outstrip the difference in interest rates between taxable and tax-exempt bonds. This windfall to high-income bond purchasers is estimated to be 20 percent. With federal tax expenditures on tax-exempt bonds issued by non-profit educational facilities projected to cost almost $18 billion from 2012-2016, this adds up to about $3.6 billion accruing to these investors rather than subsidizing borrowing the costs of schools. The interest rates for tax-exempt bonds are set lower than the interest rates for taxable bonds, because bond purchasers do
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not have to pay taxes on the interest they earn. Bond issuers set the interest rate at the level needed to ensure that they sell all of the bonds, known as the market-clearing rate. The market-clearing rate is typically higher than the interest rate needed to make tax-exempt bonds as attractive as taxable bonds to buyers in the highest tax bracket, because they pay a higher tax rate and thus get a larger tax exemption. Bond purchasers in the highest tax bracket earn more in interest from tax-exempt bonds set at the market-clearing rate than other bond purchasers, resulting in a windfall for these high-income investors.

**Spend Tax Expenditure on Pell, Not Gyms**

Tax-exempt qualified 501(c)(3) bonds are not an efficient use of federal investment into higher education. Instead of directly benefitting students or increasing college enrollment, these bonds provide direct financial benefits to private universities and investors. At least some schools that issue tax-exempt bonds have other higher-yield investments that they could use to finance the relevant construction projects instead. Harvard University, for example, has $3.705 billion in outstanding tax-exempt bonds and notes compared to $2.477 billion in outstanding taxable bonds and notes. Harvard is paying an average of 4.0% in interest on its tax-exempt bonds versus an average of 5.4% on its taxable bonds. Boston University has $917 million in outstanding tax-exempt bonds and $292 million in taxable bonds. Boston University pays an average of 2.53% on its tax-exempt bonds and 3.13% on its taxable bonds. These low interest rates appear to be due to the use of variable rates; about half of Boston University’s bonds have variable rates—including one that currently costs them 0.03%. The investors who benefit most from the tax-exempt status of the bonds are those in the highest income brackets.

Moreover, tax-exempt qualified 501(c)(3) bonds do not directly contribute to college access and affordability. Instead, the tax-exemption for qualified 501(c)(3) bonds results in a significant loss of revenue for the federal government that disproportionately benefits private colleges and universities and investors in the highest income tax bracket. These institutions, particularly those currently issuing these types of bonds, have other affordable avenues to raise capital. Therefore, we recommend converting expenditures on tax-exempt bonds going to private colleges into mandatory funding for the Pell grant program during Higher Education Act Reauthorization. Practically, that would require a new subsection added to 26 USC 145 stating that qualified 501(c)(3) bonds can only be used by public, not private, 501(c)(3) higher education organizations. Students would benefit more directly and colleges and universities would still end up as the recipients of this federal money. By re-investing the recouped funding into Pell grants the federal government would prioritize enrollment and completion for low-income students rather than spending money on capital projects. There would also be a dramatic increase in efficiency, as 100% of the federal dollars would go into higher education; now, studies estimate that about 20% of the federal investment in tax-exempt bonds end up in the pockets of high-income investors. Finally, it is important to note that public colleges and universities who face greater financial challenges would continue to enjoy the ability to issue tax-exempt bonds.
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Options for Modifying Tax-Exempt Bonds

Short of eliminating private colleges’ tax-exemption for 501(c)(3) bonds entirely, the bond program could be modified, so non-profit schools could still raise money for capital improvements, but the federal government could also recoup money to support low-income students. Alternative ways to provide support for school borrowing might be: (1) direct payment bonds, wherein the tax-exemption is eliminated in favor of a direct payment from the federal government to the school at some established share of the bond’s interest payment; (2) tax credit bonds, wherein a federal tax credit is provided to the bond holder in lieu of tax-exemption; and (3) restricted-use qualified 501(c)(3) bonds, wherein the tax-exemption is preserved but capital raised from the sale of the bonds could only be used by schools for the construction of academic buildings.

Direct Payment Bonds

One potential alternative might be to replace the tax-exemption for these bonds with a direct payment from the federal government to the school to cover a portion of the bond’s interest payment. For example, direct payment bonds made available to state and local governments through the 2009 Build America Bonds had a federal subsidy of 35% of the interest payment costs that was paid directly to the bond issuers. During the April 2009 to December 2010 period that these bonds were available, states and local governments issued $181 billion worth of them, and the US Treasury Department estimates that issuers saved $20 billion in borrowing costs compared to tax-exempt bonds. States and local governments found the bonds attractive to investors with no tax liability (such as pension funds) and more investors outside of the highest marginal tax rate, expanding the market of municipal bond buyers. Similarly, the educational bond subsidy would go directly to the school so that every federal dollar spent would be a dollar that would lower the borrowing costs of the college or university, but could subsidize less than the tax exempt bond.

Tax Credit Bonds

Another potential alternative might be to replace the tax-exemption for qualified 501(c)(3) bonds with a tax credit. The level of the federal tax credit could be set at an amount that equals the difference of the return between taxable and tax-exempt bonds, and could be provided to the bondholder on top of a taxable interest rate payment from the issuer – allowing 501(c)(3) organizations to issue taxable bonds at tax-exempt-level interest rates. By making the tax credit itself taxable, as they are in the current range of tax credit bonds, investors at all marginal income tax rates could receive an equivalent tax benefit. And as with direct payment bonds, the entire amount of the subsidy for tax-credit bonds would go toward lowering the issuer’s borrowing costs instead of being diverted to high marginal tax rate bondholders.

Restricted-Use Bonds

Finally, further restrictions could be placed on the use of funds from qualified 501(c)(3) bonds. Currently, schools can use the proceeds from these bonds to finance property they own, and in some cases can use the proceeds for working capital or for intangible property. Instead, the use of the proceeds from the bonds could be limited to financing academic buildings owned by a qualifying organization. This way, tax-exempt bonds would still be available to colleges...
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and universities to help finance the construction of buildings used for teaching, learning, and research. However, the overall amount of tax-exempt bonds issued would decrease, allowing the federal government to recoup some money from the tax-exemption and devote it to need-based financial aid.

AOTC, Hope, & Lifetime Learning Credits

This section will examine tax credits and tax-advantaged savings programs for higher education. Over the last decade, there have been three different tax credits for higher education expenses – the Hope Credit, American Opportunity Tax Credit (AOTC), and Lifetime Learning Credit (LLC). Each of these credits have had different requirements and provided different benefits. The credits are summarized in Appendix 1 and discussed in more detail below.

Hope Credit and American Opportunity Tax Credit (AOTC)

The Hope Credit and Lifetime Learning Credit (LLC) were established in 1997 in part with the goal “to enable students who could not otherwise afford to attend college to do so.” The Hope Credit is non-refundable, and may be claimed for tuition and fees during the first two years of postsecondary education. The maximum credit that may be claimed is $1,800 for each eligible student in a household. But due to the manner in which the credit is calculated, in order to claim the maximum amount of the Hope Credit, a minimum of $2,400 in tuition and fees must be paid per eligible student. Finally, the amount a taxpayer may claim is gradually reduced and phased out for higher-income taxpayers.

In 2009, the American Recovery and Reinvestment Act modified and replaced the Hope Credit with the American Opportunity Tax Credit (AOTC) for tax years 2009-2012. The maximum credit was increased to $2,500 per eligible student. The qualified education expenses for which the credit can be used were expanded to include “course-related books, supplies, and equipment” as well as tuition and fees, and the credit can be used for the first four rather than just the first two years of postsecondary education. Significantly, 40 percent of the AOTC – or $1,000 per eligible student – is refundable, and the income range at which benefits phase out was also increased. It is estimated that the AOTC cost a total of $14.4 billion in FY2011. Meanwhile, the AOTC is set to expire in 2012, and the Hope Credit is expected to cost $5.4 billion in its place. With the fiscal cliff guiding many of the tax credit discussions, it is unclear what will happen to the AOTC as it exists today.

Lifetime Learning Credit (LLC)

Like the Hope Credit, the LLC is non-refundable. However, it can be claimed for some required books as well as tuition and fees, like the AOTC. In contrast with both the Hope Credit and AOTC, there is no limit on the number of years of postsecondary education for which the LLC may be claimed, and the LLC can be used for courses to acquire or improve job skills as well as undergraduate or graduate programs. The maximum credit is $2,000, but may only be claimed once per tax return – rather than per student, like the Hope Credit and AOTC. In addition, “[i]f a taxpayer is claiming a Hope/AOTC for a particular student, none of that student’s expenses may be applied to the LLC.” As with the Hope Credit and AOTC, the amount a taxpayer may claim as a LLC is gradually reduced and phased out as income increases. The total cost of the LLC was estimated to be $3.88 billion.
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in FY 2011, and is expected to be $5.53 billion in FY 2012.179

**Tax Credits Ease the Burden on Middle-Income Families**

Higher education tax credits have helped make higher education more affordable for middle-income families, reducing debt for students and families. As a report by the Congressional Research Service explains, “the incentives provide needed relief for the middle class, many of whom may not qualify for any other source of financial aid.”180 However, these tax incentives are less useful to low-income students: low-income students and their families often do not have enough tax liability and/or net tuition costs to claim the credits.

Moreover, these tax benefits are complex. Students and their families may not even know about the benefits available to them, let alone which higher education tax incentive would be best for them.181 Ideally, the current system should be modified so that it is more transparent and benefits are available to low- as well as middle-income students, and bring up the benefits of low-income students to reduce debt levels.

**Distribution of Tax Credits**

Middle-income households receive both the largest percentage and amount of higher education tax credits, while low- and high-income households receive less of these credits. For example, a 2005 (pre-AOTC) study found that only 4.1 percent of total expenditures for the Hope Credit went to “students in tax units with cash incomes of less than $20,000,” while almost 60 percent of total went to “students whose family cash incomes exceed $50,000.”182 The study also found that “[l]ess than 5 percent of the LLC benefit accrue[d] to students in tax units with cash income of less than $20,000, and over 50 percent accrue[d] to tax units with cash income above $50,000.”183

Similarly, a 2011 (post-AOTC) report on higher education tax credits found that households with an adjusted gross income (AGI) of $30,001 or more comprised 49.8% of tax filers but accounted for 65.6% of tax returns that claimed credits.184 However, households with an AGI of $20,000 or less accounted for 34.4% of tax filers but made up only 16.6% of returns claiming education tax credits.185

The AOTC has increased the number of low- and high-income families who can claim higher education tax credits by making the AOTC partially refundable and larger than the Hope Credit.186 However, tax credits still largely do not go to low-income families.

**Tax Credits, Enrollment, and Debt**

Education tax credits do not benefit low-income families enough; for some, families must have positive tax liability to benefit from the credits, and for most, the timing of the benefit comes too late.187 Tax credits are subtracted from the amount of taxes owed,188 and the Hope Credit and LLC are nonrefundable.189 However, even now that there is a partially-refundable AOTC, tax credits may not increase enrollment or completion among low-income students due to the timing of the benefits.190 For most tax credits, this means that if a student or her family do not owe any in taxes, or owe less in taxes than the full credit amount, the student or her family will not be able to receive the full benefit of the tax credit.191 The Congressional Research Services
asserts that “[t]his limit on the ability to benefit lower income individuals may limit the incentive effects of education tax provisions (at least with respect to college enrollment) if lower income individuals are more sensitive to price than higher income individuals (who are likely to send their children to college in any case).” In other words, tax credits provide less incentive for low-income students to enroll as compared to a benefit like grant aid.

Families receive the financial benefit of the credits when their taxes are due, which may be up to a year after the student’s tuition is due. One study that found no evidence that higher education tax credits affected attendance behavior attributed at least part of this disconnect the timing of the benefit and college enrollment. The study explained that “[i]f the primary reason individuals do not enroll in college is due to liquidity constraints—the inability to secure present-day funding—then this aid is unlikely to increase access;” and that is why “critics have suggested that the credits would only benefit students expected to attend college regardless of aid rather than individuals on the margin of enrolling.”

Tax credits keep debt levels down for students who already anticipate attending college - a worthy goal - but do not provide that important incentive to enroll in the first place.

Low-income families may also benefit less from education tax credits than middle-income families because they generally have lower net tuition costs. Higher education tax credits cannot be claimed for tuition covered by grants (like Pell grants), scholarships or fellowships, or veteran’s benefits. Low-income households “typically spend less on education than other households,” and therefore have less tuition to use tax credits on overall. For example, “[o]nly students who pay tuition and fees over $10,000 a year get the full Lifetime Learning Credit”; however “[o]ver 80 percent of college students attend schools with tuition and fees under $10,000.”

One 2010 study did find that tax incentives increase college enrollment. This empirical study looked at the Hope Credit, LLC, and tuition and fees deduction (which has since expired), and found that these tax incentives “increase[d] full-time enrollment in the first two years of college by about 2.2 percentage points (6.7 percent).” However, the study noted that this increase came at a heavy price: “[b]etween 7 and 13 inframarginal youths are subsidized for each marginal youth that is induced to enroll in college” by the credits.

If the goal of higher education tax benefits is to increase enrollment, subsidizing approximately 10 students who would have gone to college anyway to get one more student who would not have attended college to enroll is not as good as we can do. And if grant aid were doing enough to keep college costs down and enrollment up among low-income students, then having a tax credit system entirely focused on the middle class might be ideal. But while these credits may not spur enrollment as much as we would like, with Pell covering far less than it used to, both low- and middle-income students need this help to keep debt levels down. Better targeting tax credits to low-income students would make them more efficient, while preserving these credits could still help middle-income families keep debt levels low. Greater transparency, however, is key to making the credits beneficial to all students.

Lack of Transparency in Tax Credits Hurts Enrollment

The current tax benefits system may be too
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complex and confusing to affect college enrollment. The Internal Revenue’s Service’s publication explaining higher education tax benefits to taxpayers is 87 pages long; it’s no wonder that students and their families, particularly those with less financial literacy, have trouble navigating the system. With respect to tax credits specifically, there are three different credits that can be used for different years of postsecondary education, which can be claimed for different numbers of students in a household, are calculated in different ways, and have different maximum credit amounts, and phase out at different income levels.

As several studies note, these complex interactions “undoubtedly discourage some taxpayers from taking advantage of tax provisions that could benefit them.” For example, the Government Accountability Office (GAO) found “that 237,000 of the 588,000 filers [(40 percent)] who claimed the tuition [and fees] tax deduction in 2009 would have been better off claiming the lifetime learning tax credit instead,” and as a result, “these filers forfeited about $67 million in tax benefits.” Additionally, “there is evidence that a significant share of eligible students and families never claim federal tax credits for higher education.” The GAO concluded that in 2008, “almost 20 percent of eligible students or families never filed for their benefits.” Moreover, college financial aid offices are not set up to help students and their families navigate the higher education tax benefits system.

Recommendations for Reform: Consider Consolidation, Expansion

A tax deal looms large at the end of this year, tax reform seems imminent, and the Higher Education Act comes up for reauthorization, policymakers should:

- Maintain AOTC instead of the Hope Credit when they strike their deal on tax extenders. Several tweaks have been discussed to address the issues raised above.
- Some experts have suggested expanding the definition of “qualified educational expenses” to which the tax credits can be applied to include room and board.
- In order to increase both the number of low-income families eligible for the credit and the amount of the credit these families can receive, several studies have suggested that the higher education tax credits be made fully refundable. While the cost of the credit would increase, opportunity for a full refund would better extend help for low-income students.
- Other experts have suggested making the tax credit more progressive, phasing the benefit out more quickly on the upper end in order to better fund the credit on the lower end. Policymakers should consider all of these possibilities as they face the expiration of AOTC and contemplate a tax deal at the end of the year.
- Consider simplifying the tax system by consolidating AOTC and LLC. Having only one credit, with one set of rules and requirements, would make it easier for families to learn about, understand, and take advantage of the higher education tax credit. Before making this change Congress should consider a number of issues:
  - LLC can be used for non-college job training while the AOTC cannot. The AOTC could be modified to preserve the use of the tax credit for job skills rather than just college studies. Expanding the types of education for which the
credit is available will presumably increase the number of people claiming the credit and thus the cost of the program.

- There is no limit on the number of years of postsecondary education for which the LLC is available, while the AOTC is only available for the first four years. This means that if the LLC were to be replaced with the AOTC, older individuals who go back to school to get job skills training might no longer be able to take advantage of a higher education tax credit. The AOTC could be modified, though, to remove the limit on the number of years of postsecondary education for which the credit can be used, and replace it with a dollar cap on the amount of credit an individual could use over his or her lifetime.

As Washington faces the task of renewing expiring tax credits at the end of 2013, tax reform proposals, the Pell grant shortfall, discretionary caps that come as a result of the Budget Control Act, and sequestration, policymakers must begin to view our higher education financing system more holistically. Subsidizing private school gyms might make sense if revenue is increasing, but when budgets are tight and result in year after year of harmful cuts to successful programs, a more comprehensive review of spending priorities is in order.

**Conclusion**

Change is never easy, and some of the reforms that we propose may take years. Many of the policies laid out must also come as part of a comprehensive overhaul of higher education financing, lest we face a familiar situation where simplification and streamlining are code words for “cut.” For federal financial aid to work well in an environment of ever increasing importance of higher education, it will need all stakeholders involved to dedicate themselves to the goals of increasing access for low-income students; keeping debt levels down; graduating more students and getting them into good jobs; and ultimately, to making the decisions necessary to fully invest in this generation’s success.
### Appendix 1 – Higher Education Tax Credits

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>Available to X student(s) in household</td>
<td>Any</td>
<td>Any</td>
<td>1</td>
</tr>
<tr>
<td>Years of postsecondary education</td>
<td>1st and 2nd</td>
<td>First 4</td>
<td>Any</td>
</tr>
<tr>
<td>Level(s) of education</td>
<td>Undergraduate and graduate</td>
<td>Undergraduate and graduate</td>
<td>Undergraduate and graduate Courses to acquire or improve job skills</td>
</tr>
<tr>
<td>No. of tax years available</td>
<td>2</td>
<td>4</td>
<td>No limit</td>
</tr>
<tr>
<td>Covered expenses beyond tuition and fees</td>
<td>None</td>
<td>Course-related books, supplies, and equipment</td>
<td>Required books, etc. that must be purchased from institution as condition of enrollment (considered fees)</td>
</tr>
<tr>
<td>Annual limit</td>
<td>$1,500 (100% of first $1,000 plus 50% of next $1,000)</td>
<td>$2,500 (100% of first $2,000 plus 25% of next $2,000)</td>
<td>$2,000 (20% of $10,000)</td>
</tr>
<tr>
<td>Income phase-out range (MAGI)</td>
<td>$48,000-$58,000 single $96,000-$116,000 married (2008)</td>
<td>$80,000-$90,000 single $160,000-$180,000 married</td>
<td>$51,000-$61,000 single $102,000-$122,000 married</td>
</tr>
<tr>
<td>Refundable?</td>
<td>No</td>
<td>Partially - $1,000 (40% of credit)</td>
<td>No</td>
</tr>
<tr>
<td>Cannot be claimed with</td>
<td>Pell Grants LLC</td>
<td>Pell Grants LLC</td>
<td>Pell Grants AOTC/Hope Credit</td>
</tr>
<tr>
<td></td>
<td>Coverdell ESA Section 529 QTP</td>
<td>Coverdell ESA Section 529 QTP</td>
<td>Coverdell ESA Section 529 QTP</td>
</tr>
<tr>
<td>Est. Total Expenditure – FY 2010</td>
<td>$0</td>
<td>$15.11 billion</td>
<td>$3.49 billion</td>
</tr>
<tr>
<td>Est. Total Expenditure – FY 2011</td>
<td>$540 million</td>
<td>$14.4 billion</td>
<td>$3.88 billion</td>
</tr>
<tr>
<td>Est. Total Expenditure – FY 2012</td>
<td>$5.41 billion</td>
<td>$0</td>
<td>$5.53 billion</td>
</tr>
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</table>

*AOTC = American Opportunity Tax Credit; LLC = Lifetime Learning Credit; MAGI = Modified Adjusted Gross Income; ESA = Education Savings Account; QTP = Qualified Tuition Program; FY = Fiscal Year*
Introduction: End Notes


6. Ibid.


19. Ibid.
The Student Perspective

Surveying the Student Voice: End Notes


2. Ibid.

3. Ibid.

4. Ibid., 3-4.

5. Ibid., 5-6.


7. Ibid., 1-2, 4-5.

8. Ibid., 2-3.

9. NERA/YI Survey: [Do you/Did you] receive enough federal financial aid to cover your tuition costs? Do not include private loans. How [do you/did you] cover additional tuition costs?

10. NERA/YI Survey: [Do you/did you] receive enough financial aid to cover your additional expenses beyond tuition (e.g. room & board, books)? How [do you/did you] cover these additional expenses?

11. NERA/YI Survey There are many pieces of information that affect students’ decisions to attend a particular college or university. In general, when evaluating a college or university, please indicate the level of importance you would place on the following characteristics of that institution.

12. Ibid.


14. Ibid.


16. Ibid., 15-16.


18. Ibid., 14.

19. Ibid., 4, 10-11.


21. Ibid.

22. Ibid.


24. Ibid.
Reimagining Federal Financial Aid: Endnotes


11. The Institute for College and Access, “Pell Grants Not Linked to Higher College Costs,” last modified on April 7, 2011.


18. Ibid.


20. Ibid.


23. Ibid., 4.


33. Ibid.


35. Healey C. Whitsett and Rory O’Sullivan, Lost Without a Map, 17.


38. Ibid., 48.


43. Ibid.

44. Ibid., 1148.

45. Ibid, Figure 2.

Financial Aid Reform


50. Ibid.


52. Heller, 58.

53. Ionescu, 31.

54. Ionescu, 34-35.

55. Ionescu, 38.

56. Ionescu, 3.


63. Ibid.


66. Ibid.

67. Ibid.


72. Direct Loan borrowers “must have had no outstanding


74. In order to qualify for IBR, a borrower must have partial financial hardship, which is defined to mean that her monthly payment amounts under standard payment would be more that 15% of her discretionary income.

75. Borrower’s employed full-time for a public service organization who make 120 on-time, full monthly payments under IBR may also qualify to have their remaining loan balance forgiven after 10 years through the Public Service Loan Forgiveness Program. Ibid.

76. Ibid.

77. Ibid.


79. In order to qualify for IBR, a borrower must have partial financial hardship, which is defined to mean that her monthly payment amounts under standard payment would be more that 15% of her discretionary income. Ibid.

80. Borrower’s employed full-time for a public service organization who make 120 on-time, full monthly payments under IBR may also qualify to have their remaining loan balance forgiven after 10 years through the Public Service Loan Forgiveness Program. Ibid.

81. Although FFEL Program loans cannot be repaid under Pay As You Earn, some FFEL Program loans are counted in determining whether a borrower has partial financial hardship (Subsidized and Unsubsidized Federal Stafford Loans, Federal PLUS Loans made to graduate or professional students, and Federal Consolidation Loans that did not repay any Parent PLUS loans). Ibid.

82. New borrowers are defined as those borrowers who “had no outstanding balance on a Direct Loan or FFEL Program loan as of Oct. 1, 2007, or had no outstanding balance on a Direct Loan or FFEL Program loan when [they] received a new loan on or after Oct. 1, 2007.” Ibid.

83. Benefits: lower monthly payments; loan forgiveness after 25 years (10 years for employees of public interest organizations); interest that is not covered by the borrower’s loan payments does not capitalize; and “the government will pay [the borrower’s] unpaid accrued interest on [his] Direct Subsidized Loans (and on the subsidized portion of [his] Direct Consolidation Loans) for up to three consecutive years.” Drawbacks: the borrower may pay more in interest because the repayment period is longer; has to submit annual documentation of income and family size; and may have to pay taxes on any loan amount that is forgiven. Ibid.

84. Ibid.


86. Ibid.


88. Ibid.


98. Ibid., 17 - 18.

99. Ibid.

100. Ibid.

101. See 20 USC §1092(l).


104. Ibid. at 17.

105. Ibid. at 31.


109. Ibid.


113. Ibid.


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140. The other three tax benefits that are among the most expensive but will not be discussed in this paper are: the deduction for charitable contributions to educational institutions; the personal exemption for dependent students age 19 to 23; and the deduction for student loan interest. Office of Management and Budget (OMB), “Federal Receipts,” in Analytical Perspectives (2012): 243. There are currently 18 tax credits for higher education, including tax benefits for donations, financing, and bonds associated with educational institutions; tax credits, deductions, exclusions, and exemptions for current and past educational expenses; and tax breaks for educational savings plans and programs. Joint Committee on Taxation, “Background and Present Law Relating to Tax Benefits for Education” (July 2012), i, https://www.jct.gov/publications.html?func=startdown&id=4474.


142. See Pike, "No Wealthy Parent Left Behind," 1245.


152. Ibid.


158. This would be consistent with the current structure of section 145, which contains limitations on nonhospital bonds and restrictions on bond used for residential housing.


Financial Aid Reform

167. Ibid., 3.

168. Ibid. “For tax year 2008, the amount of credit that may be claimed is equal to 100% of the first $1,200 of the taxpayer’s out-of-pocket expenses for each student’s tuition and fees, plus 50% of the next $1,200 of the taxpayer’s out-of-pocket expenses for each student’s qualified tuition and related expenses.”

169. Ibid. In 2008, the amount a taxpayer may claim is gradually reduced for “taxpayers who have modified adjusted gross income between $48,000 ($96,000 for married taxpayers filing jointly) and $58,000 ($116,000 for married taxpayers filing jointly). Taxpayers with modified adjusted gross income over $58,000 ($116,000 for married taxpayers filing jointly) may not claim the Hope credit.”

170. “The credit covers 100% of the first $2,000 of tuition, fees, and course materials expenses, plus 25% of the next $2,000 of tuition, fees, and course materials expenses” (Ibid., 3).

171. Ibid., 3.


173. Ibid. For tax year 2011, benefits phase out for taxpayers with modified adjusted gross incomes (MAGIs) between $80,000-$90,000 ($160,000-$180,000 for joint returns).

174. OMB, “Federal Receipts,” 243. See also: Clare McCann, “Education Tax Credits Set to Expire at Year’s End Await Congressional Action,” Ed Money Watch, New America Foundation (August 2, 2012) http://edmoney.newamerica.net/blogposts/2012/education_tax_credits_set_to_expire_at_year_s_end_await_congressional_action-70187 (asserting the AOTC will “cost taxpayers $14.3 billion in fiscal year 2012, and is expected to cost another $13.7 billion [in fiscal year 2013]”).

175. IRS, “Tax Benefits for Education,” Appendix B.


178. Ibid. For tax year 2011, benefits phase out for taxpayers with MAGIs between $51,000-$61,000 ($102,000-$122,000 for joint returns). IRS, “Preparing 2011 Returns,” Appendix B.


181. Households with adjusted gross incomes (AGIs) less than $20,000 received about 50% of the total benefits from Pell Grants, the Hope Credit and LLC. In comparison, households with AGIs of $50,000 or more received only 12% of these combined benefits. Leonard E. Burman, Elaine Maag, Peter Orszag, Jeffrey Rohaly, and John O’Hare, “The Distributional Consequences of Federal Assistance for Higher Education: The Intersection of Tax and Spending Programs,” Urban-Brookings Tax Policy Center Discussion Paper No. 26 (2005), 10. Similarly, low-income households realized a 26% reduction in the price of college from nonfederal and federal aid, veteran’s benefits, and tax benefits, compared to the 21% and 18% reductions realized by low-middle- and upper-middle-income households respectively. Alexandria Walton Radford and Lutz Berkner, “Federal Education Tax Benefits: Who Receives Them and to What Extent Do They Shape the Price of College Attendance?” National Center for Education Statistics (NCES), U.S. Department of Education (2011), 5-6, http://nces.ed.gov/pubs2012/2012212.pdf.


183. Ibid.


185. Ibid.


187. Keightley, “Overview of Tax Benefits,” 12. Since the AOTC was made partially-refundable, some taxpayers with no or lower tax liability can receive a benefit from this tax credit as well. While high-income families generally have enough tax liability to benefit from the credits, as previously noted, the credits are reduced and
phased out beyond certain income ranges.


190. See, e.g., Pike, “No Wealthy Parent Left Behind,” 1255-56.


192. Ibid.


200. Ibid., 3.

201. Ibid., 23.

202. Ibid., 1.


205. E.g. Dynarski and Scott-Clayton, “Simplify and Focus,” 1291 (“Each credit, deduction, and savings plan has a different income limit and phase-out. They even differ in how income is defined for the purposes of eligibility.”).


209. Ibid.

210. Ibid. (Noting that “college financial aid offices are set up to help students get federal grant aid and student loans, but not tax benefits”).

211. IRS, “Preparing 2011 Returns,” Appendix B. The LLC can also be used for required books and other expenses.

212. Ibid., 3.


214. Burman et. al., “Distributional Consequences,” viii. Even though this study points out that while “refundability adds substantial cost to the proposal,” it is “mostly because it provides large increases in the benefits to lower-income households” (Ibid., 12).

215. E.g. Dynarski and Scott-Clayton, “Simplify and Focus,” 1291. Some have even proposed repealing all of the higher education tax provisions and replacing them with one, expanded federal grant program. Pike, “No Wealthy Parent Left Behind,” 1256.
