the institute for college access & success

Balancing Risk and Rewards: A Proposal for Enhancing College Accountability

February 2016

The Need to Improve Institutional Accountability and Reward Colleges for Quality

Students are held accountable for studying and making progress toward a credential, but there are few consequences for schools that fail to graduate large shares of students or consistently leave students with debts they cannot repay. The current federal aid eligibility system uses a blunt, all-or-nothing strategy that provides little incentive for colleges to improve unless they are on the verge of losing eligibility for federal funds. We recommend a comprehensive federal policy that supplements existing accountability measures like the Gainful Employment and 90-10 rules, ties federal aid eligibility to the actual financial risk students take by enrolling and the risk taxpayers take by subsidizing the school, and rewards schools that serve low-income students well. Such a policy will not only increase accountability to better protect students and taxpayers, but also provide incentives for schools to improve and reward performance.

Proposal for Risk Sharing and Rewards

The U.S. Department of Education currently uses cohort default rates (CDRs) to assess college eligibility for federal student aid funding (Title IV funding). However, the meaning and utility of CDRs are limited because they fail to account for the number of students at an institution who take loans. A better indicator is the Student Default Risk Indicator (SDRI), a school's three-year CDR multiplied by the share of the school's students who borrow. By incorporating the share of students who borrow, the SDRI more accurately conveys a student's risk of default at a given school. Our proposed framework replaces the current CDR thresholds with risk sharing and rewards based on the SDRI, providing incentives for colleges to enroll low-income students and help students graduate and avoid default. The proposal below would begin rewarding colleges based on their SDRIs in the 2017-18 school year, and introduce risk sharing and SDRI-based eligibility determinations in 2020 in order to provide schools adequate time to prepare. The figures below are based on fiscal year 2012 CDRs (the most recent available), and represent the share of schools in each category if their SDRIs remained the same when rewards and risk sharing are implemented.

Offer Rewards: Schools where students have the lowest risk of default would be eligible for financial and non-financial rewards, providing incentives for colleges with low risk to innovate and enroll more low-income students.

1. Schools with SDRIs at or below 2% would receive additional, flexible, need-based grant funding based on their low-income student enrollment. Currently, 21% of colleges have an SDRI of 2% or lower (enrolling 34% of all students).
2. Schools with SDRIs at or below 5% would receive additional flexibility, such as bonus points in funding competitions or preferential treatment for Experimental Sites, to help foster innovation. Currently, 51% of schools have an SDRI of 5% or lower (enrolling 67% of all students).

Require Risk-reduction Plans: Schools with an SDRI of 10% or greater would be required to adopt a risk reduction plan to lower their risk. Currently, schools are not required to adopt a plan until their CDR reaches 30%.

End Eligibility for Schools with Unacceptable Performance: Unacceptably risky schools would lose eligibility for federal aid. Schools with SDRIs at or above 20% (where one in five students is expected to default within three years of entering repayment) would not be eligible for federal funding. Currently, 3% schools have an SDRI of 20% or higher (enrolling fewer than 1% of students).

Implement Risk Sharing: Schools with SDRIs between 10% and 20% would be required to make risk-sharing payments. The level of risk sharing would increase as the risk to students and taxpayers increases, as measured by the school's SDRI and by the extent of the school's reliance on federal aid. The Education Department would use payments to supplement funding for student financial aid, improving loan counseling, and enforcing laws designed to protect students and taxpayers from waste, fraud and abuse. Currently, 17% of schools have an SDRI at or above 10% and below 20% (enrolling 9% of students); these schools have a median SDRI of 13%.

For more details on our proposal see http://ticas.org/content/pub/comments-senate-help-committee-white-paper-college-risk-sharing.