Understanding America's student debt crisis: Diverging paths in higher education financing, access, and outcomes

Outcome Group Inc.

White Paper Series, No. 1

April 10, 2020

Jim Courtland, CEO
Nora Delaney, Quantitative Social Scientist
Alison Fredman, Senior Consultant

Executive Summary

For many Americans student debt is a growing crisis, placing an extraordinary burden on enrolling students and stymying the financial and material development of an emerging generation of professionals. For many of us, student loans are a profoundly personal topic, carrying our own stories of the commitment, costs, and rewards of higher education. Yet, higher education financing is also a pressing policy issue as America weighs its role in social mobility against skyrocketing levels of outstanding student debt and the burden it places on American students and taxpayers. And, as the COVID-19 pandemic upends our economy and the livelihoods of millions of Americans, it is crucial that we examine the role of education, student debt, and career development in financial wellbeing.

In our globalized economy, those that miss out on a college degree earn less, experience greater unemployment, live shorter lives, and gather less social capital on average than peers with bachelor's degrees. Yet, a college degree is far from a golden ticket to a bright future, as a growing proportion of borrowers struggle to pay down educational debt and stave off the threats of default and insolvency. Higher education experiences in the United States are as diverse as our communities, challenging our assumptions about who holds student debt, which schools it flows to, and why it is difficult to repay. As Americans seek skills and career development and non-traditional degrees rise in popularity and importance, it is crucial that educators remain accountable to post-graduation outcomes.

Mounting student debt, and the costs of repayment stress in our society and economy, are the result of misaligned incentives between schools, students, and loan providers. With more than $1.6 trillion in outstanding federal student loan debt, the federal government has made clear its commitment to financing higher education. However, once student loan dollars are transferred to higher education providers, there are few mechanisms in place to ensure that schools honor tuition dollars as a commitment to equip students for successful careers. Rising tuition costs and uncertain labor market outcomes conspire to place tremendous risk on students, calling for a realignment of responsibilities in the relationships between schools, their students, and their funding sources.

Ballooning Debt

Tuition costs have risen by 538% since 1985, pushing federal student debt levels to more than $1.6 trillion. Education debt is growing faster than any other consumer finance product as students pile on loans to cover the cost of attendance.

Uncertain Returns

Estimates place the internal rate of return (IRR) of college tuition at 14% for earners of a bachelor's degree. Yet, college graduates in the bottom quarter of earnings see zero or negative returns to tuition dollars, calling into the question the safety of higher education as an investment.

Diverse Student Experiences

Just more than a quarter of American college students are enrolled full-time in 4-year degree programs at public and non-profit schools. In fact, most degree seekers are non-traditional students who enroll in 2-year degrees and access coursework online or at commuter campuses. Focusing on the programs that serve minority and low-income groups provides clues into a disconnect between higher education investment and labor market outcomes.

The Destruction of Default

Defaulting student borrowers face punitive consequences, including restricted professional opportunities and access to social services and financial assistance. Despite the devastating costs, 38% of borrowers who took out federal student loans in 2004 are projected to default by 2023.

Calling for Accountability

With skyrocketing federal student debt, educators have a responsibility to demonstrate to students and taxpayers that they are preparing students for a competitive labor market. Asking schools to take a financial stake in students' futures can realign the relationship between schools and their students.

The Magnitude of the Student Debt Crisis

College access has held a key role in American social mobility and human capital development. It's no mistake that higher education financing has played an outsized role in discourse surrounding the 2020 presidential election. In the emerging period of globalization and automation, graduating high schoolers and labor force veterans alike are eager to invest in education rather than risk being left behind in an economy demanding increasingly specialized skills.

As of 2019, outstanding federal student loans totaled an all-time high of $1.6 trillion. Accumulating student debt corresponds to increases in cost of attendance; tuition expenses increased by 538% from 1985 to 2013, far outpacing a 121% increase in the Consumer Price Index (CPI) over the same period. Considering other consumer finance products can help put the scale of student debt accumulation in perspective. With the exception of home mortgages, student debt represents the largest class of consumer debt and continues to grow rapidly. Between 2007 and 2018, the amount of outstanding student debt in the US grew by 157%, relative to 53% growth in auto loans and negative growth, if any, in mortgage and credit card debt. But the rate of growth isn't the only significant difference between student debt and other consumer finance products. While mortgages and auto loans finance tangible assets providing shelter and transportation, student borrowers receive no guarantee of a job—or even a diploma. Student borrowers must choose to invest in higher education without knowing the value of their degree in an evolving labor market.

Uncertainty over post-graduation outcomes, coupled with skyrocketing costs of attendance, places considerable risks on students. The cost of attendance has risen by an average of 3.4% each year at public universities since 1995. As of 2016, the average cost of yearly attendance at private and public four-year institutions constituted 64% and 30% of median household income respectively. In turn, financial distress stemming from student debt has the potential to derail or destabilize other crucial areas of personal finance, including home ownership, family planning, entrepreneurship, and healthcare. Yet the consequences of unsustainable student debt are not constrained to individual borrowers. Depressed human capital development has the potential to inform not only how the American workforce will adapt to challenges of the 21st century, but also the extent of mobility and equity our citizens can expect.

Why Statistics Don't Matter

At face value, official data paints a rosy picture of the benefits of higher education. Figures released by the Federal Reserve Bank of New York place average returns to a 4-year college degree at an all-time high since 1970. The internal rate of return on investment in a college degree is roughly 14%, meaning that dollars invested in higher education vastly out-perform average returns in the stock market, which hover around 7%.[1] Recent graduates holding a bachelor's degree earn an average salary of $78,000 annually, compared to $45,000 for workers without a degree. College attendance is also associated with lower rates of unemployment. Data from the Bureau of Labor Statistics places the unemployment rate for high school graduates at 4.1% in 2018, compared to just 2.2% among college graduates. However, the benefits of higher education extend far beyond a competitive edge in the labor market. Princeton economists Anne Case and Angus Deaton

[1] Abel & Deitz, 2019

find that a 4-year bachelor's degree doesn't just boost overall earnings outcomes but also sharply demarcates quality of life indicators such as life span, marriage, likelihood of drug and alcohol abuse, and suicidal behavior. Their research indicates that American 50-year-olds who lack a 4-year degree are nearly 3.5 times more likely to die prematurely than those with a bachelor's degree.[2]

While this data indicates that a bachelor's degree holds a clear net-positive effect for the average graduate, it does little to express the diversity of demographics, educational programs, and labor market outcomes that American college students experience. In fact, outcomes for individuals enrolling in higher education are widely dispersed, varying by region, industry, educational institution, and individual characteristics.

Using broad statistics to inform our understanding of the costs and risks of higher education offers an incomplete picture of higher education and its consequences. After all, who is the "average" graduate? How does the average graduate vary by demographics, school, professional field, and financial background? What about students who don't graduate at all, but still carry the costs of an incomplete degree? While statistics play a crucial role in measuring the role of education in our labor force, we should be careful not to let a central tendency draw our attention away from the diverse set of higher education experiences and outcomes in the US today. For example, the same study by the Federal Reserve Bank of New York that is cited above finds that returns to higher education *are zero or less for the bottom 25% of earners*, confirming that the well-documented benefits to higher education for those earning at or above the average level are counterbalanced by substantial downside risk for roughly 1 in 4 seekers of a higher degree.

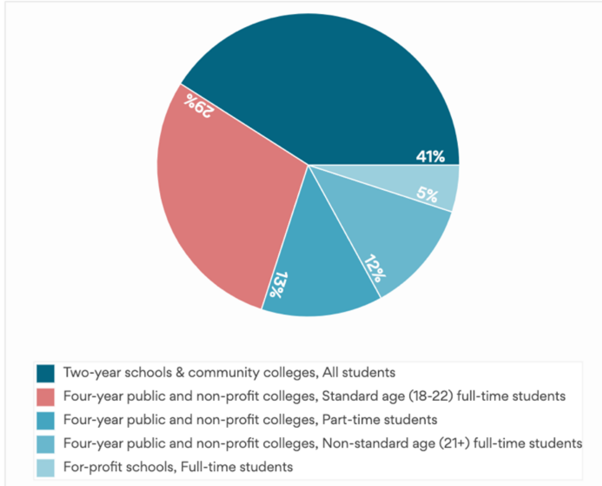
Acknowledging the dispersion of outcomes among higher education seekers can help us reconcile earnings statistics with alarming data surrounding student debt burden. The U.S. Department of Education estimates that 38% of the cohort of students who first took out federal student loans in 2004 will default by 2023. Roughly half of borrowers fail to make a principal payment within five years of graduation. The scale of debt distress calls for a close examination of the diverse risks and benefits of higher education programs in the United States, which students they impact, and how we can move towards a more equitable and affordable higher education system.

Challenging the Myth of the College Experience

In movies, TV shows, and popular culture, the word "college" tends to recall 18- to 22-year-olds studying, living, and partying on or near suburban campuses. Yet this picture only describes roughly a quarter of the nation's 18 million undergraduates, according to data from the US Department of Education. In fact, this figure is overstated as it doesn't include the more than half a million students who are enrolled in certificate programs or online and commuter students who don't attend colleges with traditional residential campuses. A student's higher education experience, including school of attendance and financing characteristics, are highly stratified by demographics including age, race, and overall socioeconomic status. These factors form the basis for school-based marketing and outreach campaigns, career and vocational advice, and cultural and community norms.

[2] Leonhardt & Thompson, 2020

Figure 1: Diversity of Students Enrolled in Higher Education



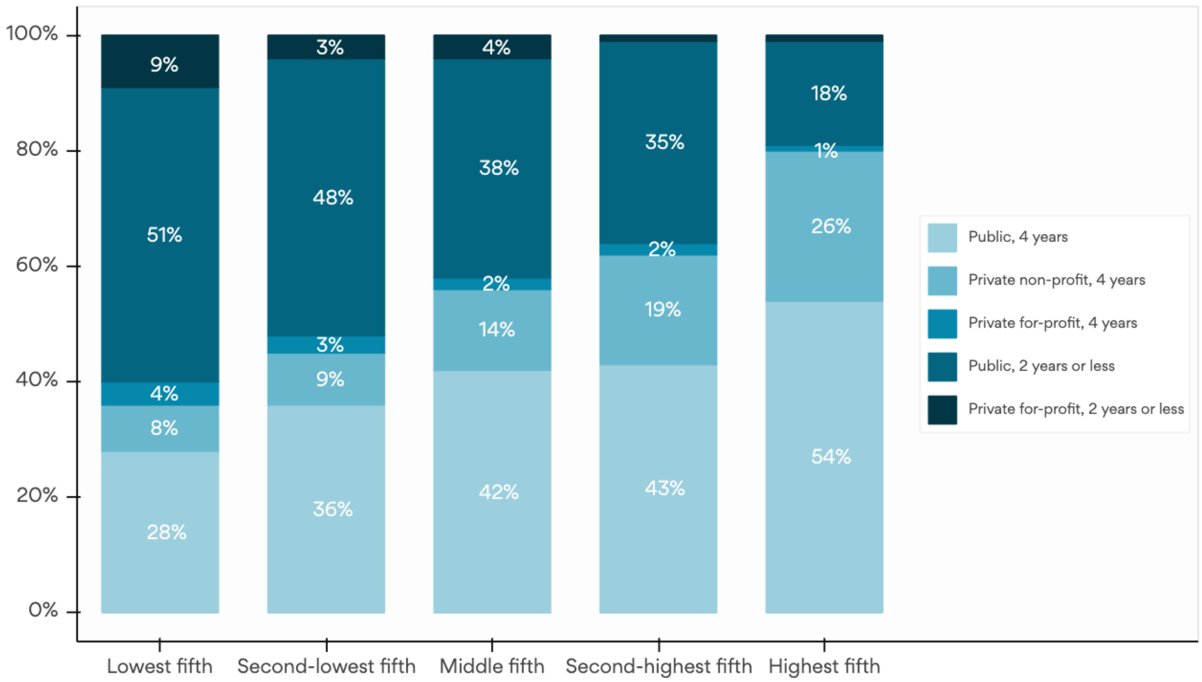
Source: National Center for Education Statistics, Digest of Education Statistics

Understanding how the so-called "college experience" varies among diverse American communities is key to understanding the tradeoffs facing students in higher education. According to the US Department of Education, family wealth plays a big role in which colleges and levels of degree programs students choose. Students from the lowest 20% of parental earnings are not only more likely to pursue an associate degree, but also to enroll in a less selective institution than their peers from the highest 20%. By contrast, students from wealthier families overwhelmingly enroll in more selective 4-year institutions while seeking bachelor's degrees (Figure 2).[3] Those from lower socioeconomic strata are not only far less likely to enroll in a college degree program but also less likely to have access to informational resources about college, financing, and the substantial upfront costs required for positive financial return. Many students and their families lack trustworthy information sources as they approach high-risk decisions in higher education financing, especially as they seek to identify which institutions are likely to help them achieve a positive return on their investment.

Over the last several decades, the cost of college has outpaced inflation, wages, and Federal grants, causing student borrowing to become the primary way people pay for college. Even with the increase in overall borrowing rates, there is still significant variation depending on the type of school a given graduate attended. Table 1 shows that debt accumulation at private institutions exceeds that at public institutions for every degree type. A near constant majority of students at for-profit private schools accumulate debt, regardless of the degree type. For students of for-profit and non-traditional schools, issues of financial resources and educational access are driven largely by complex issues of socioeconomic status and pre-college educational preparation. In addition, debt accumulation does not take into account degree completion rates, leaving students who fail to finish their degrees or require additional time in school in adverse circumstances.

[3] U.S. Department of Education, National Center for Education Statistics, 2019

Figure 2: Enrollment in postsecondary education by socioeconomic status in 2016



Source: National Center for Education Statistics

Similarly, labor market outcomes within a given degree program vary wildly by program of study. While debt accumulated towards a bachelor's degree should yield higher post-graduate earnings relative to shorter degrees, diverse labor market outcomes raise questions over whether the value of the degree justifies the debt. While students pursuing two-year degrees are more likely to study technical and career-oriented fields such as health care, students pursuing bachelor's degrees are more likely to study liberal arts topics such as English and history. Among students in four-year colleges, age plays a role in determining area of study as older and more experienced students are more likely than their peers to study business, computer science, and engineering.

Table 1: Percentage of Graduates Holding Debt

	Certificate Program	Associate's Degree	Bachelors' Degree
Public	36%	42%	64%
Private, non-profit	N/A	N/A	74%
Private, for-profit	0.86	0.88	0.87

Source: The Student Debt Review Policy Brief, Ben Miller

Students' choices in school of attendance—and the associated debt load—fracture along demographic lines and go far to explain racial wealth gaps. We know that demographic factors are associated with not only the amount of loans that students acquire, but also the institutions they attend. Inequities in college preparation, admissions, and the dearth of information available mean that students of color are far more likely to enroll in less selective, and often under-resourced colleges that have lower overall college graduation rates. Black and Hispanic students are far more likely to attend for-profit colleges than white students and, reciprocally, are less likely to attend public four-year colleges.[4] Yet simply examining attendance rates at for-profit colleges is insufficient to explain racial differences in student debt and lifetime wealth accumulation. Intergenerational wealth dynamics lead black students to borrow at higher rates than white students, with black students in fact borrowing higher amounts than white counterparts even after controlling for the sector of educational institutions. This suggests that black students carry a heavier debt burden relative to the value of their degree in the labor market. Heavy debt burden combined with high dropout rates at for-profit institutions places outsized financial burden on students of color, leading roughly 75% of African American borrowers who drop out of for-profit schools to eventually default on student loans. And, unlike other demographic groups, the debt crisis is not limited to dropouts and for-profit entrants among African Americans. Over 20% of African American college graduates default, a rate that is five times as high as white bachelor's recipients, and a higher rate than white students who drop-out of college with debt.[5]

Understanding the complex relationships between socioeconomic status and education access, including the perverse penalization of under-resourced students, goes a long way towards understanding profound disconnects in the modern economy. Social mobility and financial stability are undermined by underserved populations struggling to pay down college degrees. With roughly 40% of college students enrolled in non-traditional educational tracks, the value of these degrees relative to their cost remains uncertain. Yet, while under-resourced populations stand to lose the most in a globalized and technologized economy, they face tough choices in navigating the pitfalls of private vocational and technical programs. Removing barriers to success for students across the demographic spectrum not only has the potential to reduce outsized financial strain on low-income and minority students, but also to spur investment in crucial skills throughout our modernizing economy.

Debt Burden: Focusing on Smaller Borrowers

Most importantly to our focus on the student debt crisis, we must understand who holds the most perilous debt burden. As student debt has swelled into the trillions, the public conversation has focused on those who hold the most debt. While students holding more than $100,000 in student debt are struggling under the weight of the obligation, they represent only a small fraction of borrowers. In fact, smaller borrowers have more trouble repaying student debt than peers with large loan balances and the professional degrees that accompany them.

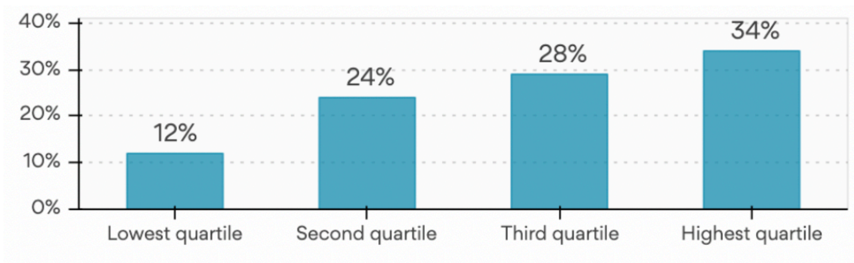
As figure 3 shows, the largest portion of outstanding student debt is held by people with relatively high incomes ($97,001 and above). Households in the lowest income quartile (incomes of $27,000 or less) hold only 12% of student debt. Education debt is indeed

[4] Libassi, 2018

[5] Scott-Clayton, 2018

disproportionately concentrated among the well off, but this can be explained by the fact that, while the top US universities are expensive, they offer the best career prospects and the highest earnings. The education those in the top-income quartile borrowed to pay for is what helps them rise towards the top of the income distribution. Demonstratively, 48% of outstanding student debt is owned by households with graduate degrees.[6] However, well-off students enrolling in elite colleges represents a tiny fraction of students in the US, suggesting that the experiences of borrowers with large debts distort our assumptions about the amount of debt held across all student types, and the ease of its repayment.

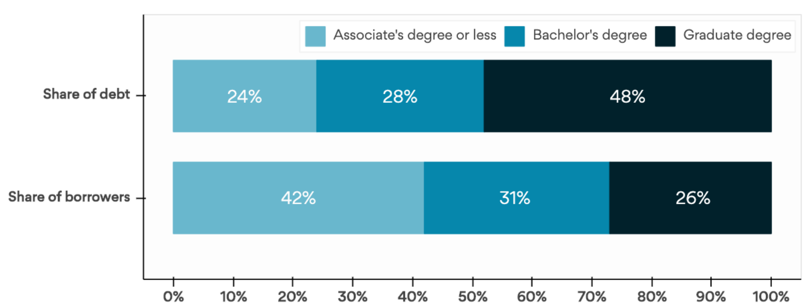
Figure 3: Percent of education debt held by income quartile of households age 25 and older, 2016



Sources: Survey of Consumer Finances, Urban Institute

Yet, the fact that a relatively small share of outstanding student debt is held by low-income households does not mean these households have not borrowed—or that they are not burdened by student debt obligations. Figure 4 illustrates that borrowers with an associate degree or less account for a larger share of overall borrowers than of student debt in dollar terms. Even though they may not hold a large amount of debt, 42% of those with student debt have an associate degree or less. Simply, the students facing the most problems with loan debt are those who enroll in college but leave without completing a credential or those who complete programs at institutions that don't prepare them to find good jobs. According to the College Board, two-thirds of those who defaulted owed $10,000 or less.

Figure 4: Proportions of Borrowers and Total Outstanding Debt by Education Level, 2016



Source: The Urban Institute, Which Households Hold the Most Student Debt

[6] Baum, 2018

Additionally, 18% of borrowers across all degree types were in default on their loans, but these borrowers accounted for only 12% of total debt owed.[7] This disparity is explained by the disproportionate number of borrowers in default with small amounts of debt. The issue is low earnings, not high debt. Students who borrow less than $5,000 default at a rate of 34%, compared to 18 % for those who borrow more than $100,000.[8]

For-Profit Colleges

Earlier, we discussed the diversity of higher education cohorts and how wealth and race disproportionately affect students enrolling in for-profit colleges. For-profit institutions correct a gap in the higher education market by serving nontraditional students that other post-secondary schools haven't reached. Their students are heavily weighted toward students of color, veterans, older students, the disabled, single mothers, and people who are already employed but seeking new jobs in new fields.

Today these institutions enroll over a million people ranging from traditional degree programs to alternative vocational programs, often with flexible schedules, online options, and targeted skills-based training. Budget cuts and tuition hikes at to state and community colleges boost the attractiveness of for-profit colleges among nontraditional students looking for programs that give them an educational opportunity.

When properly administered and regulated, for-profit schools can offer a valuable educational option. In New York State, for instance, a many for-profit schools boast above-average student outcomes, with graduation rates outpacing other higher-education sectors.[9] Nationally, however, this is not the case as the majority of students have a low return on investment and high default rates. For-profit borrowers default at twice the rate of public two-year borrowers (52% versus 26% after 12 years), but because for-profit students are more likely to borrow, the default rate among all for-profit entrants is nearly four times that of public two-year entrants (47% versus 13%).[10] The rise in default rates has been strikingly concentrated among for-profit entrants, and projections suggest that default rates in this sector could ultimately approach 70%.[11] Additionally, as figure 5 shows, for-profit institutions increasingly account for the largest amounts of federal student loan debt among all educational institutions, with some institutions individually accounting for more than $35 billion in 2014.[12] With a lack of oversight, targeted recruiting practices, and business models focused on profits instead of student outcomes, the for-profit higher education industry is disproportionately contributing to the student debt crisis and would benefit greatly from reform.

[7] College Board, 2020
[8] Dynarski, 2016
[9] Bellin, 2016
[10] Scott-Clayton, 2016
[11] Scott-Clayton, 2016
[12] Jackson, 2015

Figure 5: Colleges with highest debt loads, 2000 vs 2014

2000

Institution	Total Debt (bn)
New York University	2.18
University of Phoenix-Phoenix Campus	2.10
Nova Southeastern University	1.74
Pennsylvania State University-Main Cam	1.71
University of Southern California	1.61
Ohio State University-Main Campus	1.53
Temple University	1.53
Arizona State University-Tempe	1.39
Michigan State University	1.32
University of Minnesota-Twin Cities	1.29

2014

Institution	Total Debt (bn)
University of Phoenix-Phoenix Campus	35.53
Walden University	9.83
Nova Southeastern University	8.75
DeVry University-Illinois	8.25
Capella University	8.04
Strayer University-Global Region	6.69
Kaplan University-Davenport Campus	6.66
New York University	6.31
Argosy University-Orange County	6.18
Ashford University	5.89

For-profit Non-profit or Public

Source: Adam Looney and Constantine Yannelis, Brookings Institution

In the next several decades, there is no doubt that for-profit institutions will be an important vehicle for non-traditional students and workers looking for career development and retraining, especially for students of color and those from low-income backgrounds. Government can (and should) hold for-profit schools accountable, while, for its own part, the higher education industry has the opportunity to redesign the incentives between students and schools. With a mixed record of student outcomes across for-profit schools, competitive actors in the industry will need to demonstrate a commitment to preparing students for a skills-focused labor market.

The Costs of Default

It is difficult to overstate the transformative and destructive impact of default on the prosperity and livelihoods of struggling borrowers. A history of default has long-term implications for borrowers' quality of life, influencing access to rental housing, credit cards, mortgages, and auto loans and restricting a borrower's safety net to facilitate family planning, career changes, and geographic mobility.

Defaulting on student loans opens the door to a range of punitive remedial action on the part of public institutions and remains on a borrower's credit history for up to seven years. The US Department of Education can garnish up to 15% of defaulting borrowers' disposable income, while the US Treasury can divert retirement and disability benefits, income tax returns, and even lottery winnings towards loan repayment. Defaulted borrowers are unable to access mortgages through federal agencies, deferment or forbearance options to repay student loan debt, and further student aid funding. Not only do borrowers face truncated financial streams and social services—potentially compounding financial distress—but also reduced financial and professional opportunities in the future. Defaulted borrowers are prevented from taking jobs with the US Armed Forces. Adding to the sting of default, the Department of Education can prevent renewal of professional licenses held by defaulted borrowers, compounding the financial penalty to professionals requiring licenses to work in their field of expertise.[13] Many employers require credit checks for job applicants working with money, locking defaulted borrowers out of opportunities as cashiers, accountants, clerks, and store managers.

[13] FinAid, 2020

Evidence suggests that the costs of default far outweigh the monthly drain of loan repayments, even for borrowers on the margin of default who are struggling to make loan payments. A group of researchers examined two groups of defaulting student loan borrowers, publishing their findings in a working paper for the National Bureau of Economic Research. The authors find that one group, who experience an exogenous debt-forgiveness event, enjoy greater geographic and professional mobility and higher incomes after their defaulted student debt was erased relative to similar peers who were not released from student debt obligations.[14] Importantly none of the defaulted borrowers in the study were making loan payments either before or after the loan forgiveness event, indicating that the financial burden of monthly payments alone is insufficient to explain the wide-ranging effects of student debt burden.

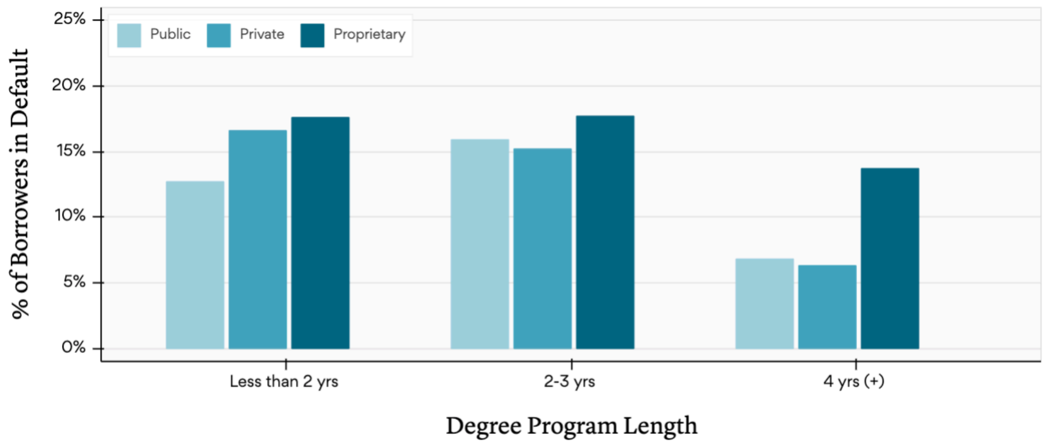
The extraordinary costs of default—financial, professional, and psychological—are undoubtedly designed to deter willful non-payment by student borrowers. However, cohort default rates on federal student loans have hovered around 10% since 2015, suggesting that, for borrowers struggling to make payments, the punitive consequences of default are not a choice but an inevitability. As cost of attendance at US colleges and the national balance of outstanding federal student loans continues to rise, the penalties of default appear increasingly misplaced, amplifying discrepancies in outcome between the winners and losers of the higher education lottery.

As with many aspects of the higher education system, students from low-income and minority backgrounds shoulder a larger share of the costs of default, as they are more likely to enroll in for-profit schools and non-traditional degree programs which are less likely to deliver a positive return on investment compared to their traditional counterparts. While federal grants, financial aid, and scholarships exist to assist these populations, access is concentrated among well-resourced public and private non-profit institutions, and thus out of reach for many non-traditional students. Moreover, we know that students at for-profit institutions are likely to come from low-SES and minority backgrounds and to take out more debt than peers at non-profit schools, indicating that existing student aid is insufficient to service these groups. As Figure 6 shows, default rates in shorter, non-traditional degree tracks are higher than those at 4-year institutions after controlling for institution type. While graduates from 4-year institutions are expected to earn more on average than peers in non-traditional degree tracks, higher education seekers without a 4-year degree are disproportionately likely to experience the financial strain of default.

A student loan financing system that places a disproportionate burden on lower earners results in a regressive redistribution, rewarding those at the top of the earnings spectrum and compounding the financial woes of those at the bottom. The increase in the average returns to a college degree and their variance across individual earners, combined with climbing tuition costs, raises the stakes for all students in a gamble to achieve a high standard of living and professional success. However, the current student loan financing mechanisms place the greatest risk on vulnerable students, converting the pursuit of higher education into an unsuitable investment that can lead to unacceptable losses.

[14] Di Maggio, Kalda, & Yao, 2020

Figure 6: Default Rates by Institution and Degree Type



Source: US Department of Education, Office of Federal Student Aid

Accountability in Student Financing

Higher education financing represents a key gateway in educational access and labor market mobility. Yet, the status quo has failed to serve students and, in many cases, punish vulnerable groups. As students seek out education as a pathway to career development and economic opportunity, it is crucial that we develop financing mechanisms that engage schools as active stakeholders and link the quality of education to the value of student debt. For-profit programs are incentivized to maximize enrollments, often relying on federal student loan dollars to pay tuition. In March 2020, the Department of Veteran Affairs suspended enrollment of new students under the GI Bill at a slate of for-profit institutions, including the University of Phoenix and Temple University, on the grounds of inadequate provision of educational services. However, in many cases where educational provision falls short of employment promises, for-profit programs may not be subject to censure, leaving program alumni and—in many cases—US taxpayers holding the bag. Even public and non-profit programs' finances are largely disconnected from student employment outcomes. While colleges rely on tuition dollars to cover operational costs, they do not take a stake in the debt that students took out to pay their tuition. Aligning the incentives of higher education providers with their students in terms of quality of education, cost of attendance, and post-graduation employment outcomes is the single most crucial step in addressing the distortions of our current higher education financing system.

To realign the interests of students and higher education providers, we must innovate the financial relationship tying students to schools. Instead of characterizing the relationship between students and colleges as an exchange of tuition dollars for educational services, we could ask colleges to quite literally invest in their students. After all, if a degree is really worth its tuition, why shouldn't a college reinforce their commitment to educational and career attainment with a tangible stake in student outcomes? Income-share agreements (ISA) are a financial tool that allows schools to do just this, providing funds towards tuition costs in return for a share of student earnings after graduation if—and only if—those earnings fall above a predetermined level. Under ISAs, graduates pay a fixed percentage of their income above a given threshold, say $35,000. Unlike conventional student loans, ISAs have neither an interest rate nor an outstanding balance; borrowers are released from the obligation at the end of the repayment term regardless of how much or how little they have paid.

Under an ISA, the higher education provider loans tuition funds to the student. More importantly, the amount that borrowers repay is linked to the school's ability to prepare those borrowers for success in the labor market. If a borrowing student finds that their degree is of little value in the labor market, the school may be unable to recoup the value of the loan. Conversely, if the student is successful, the school is rewarded and the student continues on to a fruitful and remunerative career, rewarding both parties. Schools that provide ISAs must take a stake in their student body, sharing both risks and rewards with their graduates.

Under ISAs, schools front tuition costs in return for ISA repayments from students once they enter the workforce months or years in the future. This can present a challenge for schools that derive a large portion of operating revenues from tuition payments, since the implementation of ISAs may lead to a shortage of cash on hand to cover the provision of educational services. While some elite schools may be able to self-finance ISA costs by drawing on endowments or donations, ISAs should not—and need not—be limited to this relatively select group of institutions. Instead, schools may share the up-front costs of providing ISAs with third party investors, who can provide operating capital to schools before students enter repayment. With both schools and investors jointly taking a stake in students' outcomes, the incentives between students and their financing providers under an ISA remain intact.

While ISAs ensure that educators' and investors' interests are aligned with student outcomes, ISAs are also a tool to assist schools in helping a larger proportion of students successfully complete degrees. For students who drop out due to financial constraints, low-risk student financing has the potential to cover tuition gaps and alleviate financial pressures while in school, increasing the probability of graduation and in turn, rewarding post-graduate labor market outcomes. While federal student aid and loans will continue to play a critical role in higher education financing, ISAs can cover financing gaps with a flexible financial tool. For borrowers with both conventional federal loans and an ISA obligation, the insurance offered by the ISA's repayment threshold can dampen the financial strain of overall loan repayments during periods of low earnings, reducing the probability of default and its consequences.

Final Remarks

From the GI Bill to Pell grants and federal student loan provision, US policymakers have sought to marry access to student financing with the principles of meritocracy, rewarding those who invest in education with the potential of upward mobility and the pursuit of the American Dream. While the $1.6 trillion in outstanding federal student loan debt demonstrates commitment to these principles on an unprecedented scale, the benefits of higher education—and its costs—are perversely distributed across our society. Simply financing education isn't adequate to ensure social mobility and skill development; we must reform the structure of incentives underpinning the relationships between higher education providers and their students. A lack of alignment between the interests of taxpayers, higher education providers, and students from diverse backgrounds leaves the most vulnerable students among us carrying a heavy burden. However, we should not forget that, in a globalized and technologized economy, we all benefit from a competitive, skilled, and inclusive workforce. It's time to innovate the rules of student financing, to level the playing field, and to ensure that all students have a fair chance at post-graduation success.

Resources

Abel, J., & Deitz, R. (2019, June 5). Despite Rising Costs, College Is Still a Good Investment Liberty Street Economics. Retrieved from https://libertystreeteconomics.newyorkfed.org/2019/06/despite-rising-costs-college-is-still-a-good-investment.html

Baum, S. (2019, May 2). Which Households Hold the Most Student Debt? Retrieved from https://www.urban.org/urban-wire/which-households-hold-most-student-debt

Bellin, J. (2016, January 27). A Gateway to the Working World. Retrieved from https://www.city-journal.org/html/gateway-working-world-13724.html

College Board. (2020, February 7). The Student Loan Crisis Is More Complicated Than a Number. Retrieved from https://elective.collegeboard.org/student-loan-crisis-more-complicated-number

Di Maggio, Marco and Kalda, Ankit and Yao, Vincent. (2020, March 2). Second Chance: Life without Student Debt. Retrieved from SSRN: https://ssrn.com/abstract=3376245

Dynarski, S. M. (2016, October 18). The trouble with student loans? Low earnings, not high debt. Retrieved from https://www.brookings.edu/research/the-trouble-with-student-loans-low-earnings-not-high-debt/

FinAid. (n.d.). Defaulting on Student Loans. Retrieved April 7, 2020, from https://www.finaid.org/loans/default.phtml

Jackson, A. (2015, September 11). This graphic perfectly sums up who's being pummeled by America's student loan crisis. Retrieved from https://www.businessinsider.com/the-student-loan-crisis-hurts-for-profit-and-community-college-borrowers-2015-9?international=true&r=US&IR=T

Leonhardt, D., & Thompson, S. (2020, March 6). How Working-Class Life Is Killing Americans, in Charts. Retrieved from https://www.nytimes.com/interactive/2020/03/06/opinion/working-class-death-rate.html

Libassi, C. (2018, May 23). The Neglected College Race Gap: Racial Disparities Among College Completers. Retrieved from https://cdn.americanprogress.org/content/uploads/2018/05/22135501/CollegeCompletions-Brief1.pdf

Looney, A., & Yannelis, C. (2016, September 13). A crisis in student loans? How changes in the characteristics of borrowers and in the institutions they attended contributed to rising loan defaults. Retrieved from https://www.brookings.edu/bpea-articles/a-crisis-in-student-loans-how-changes-in-the-characteristics-of-borrowers-and-in-the-institutions-they-attended-contributed-to-rising-loan-defaults/

Miller, B. (2014, February 18). "The Student Debt Review." New America: http://education. newamerica.net/sites/newamerica.net/files/policydocs/TheStudentDebtReview_2_18_14.pdf.

Scott-Clayton, J. (2018, May 15). The looming student loan default crisis is worse than we thought. Retrieved from https://www.brookings.edu/research/the-looming-student-loan-default-crisis-is-worse-than-we-thought/

U.S. Department of Education, Center for Education Statistics. (2019, May 1). The Condition of Education - Spotlights - 2019 Spotlights - Young Adult Educational and Employment Outcomes by Family Socioeconomic Status - Indicator May (2019). Retrieved from https://nces.ed.gov/programs/coe/indicator_tbe.asp

U.S. Department of Education, National Center for Education Statistics. (2012, September 1). Total fall enrollment in all postsecondary institutions participating in Title IV programs, by degree-granting status and control of institution: 1995 through 2011. Retrieved from https://nces.ed.gov/programs/digest/d12/tables/dt12_222.asp

U.S. Department of Education, Office of Federal Student Aid. (2019, August 4). Official Three-year Cohort Default Rates for Postsecondary Schools. Retrieved from https://www2.ed.gov/offices/OSFAP/defaultmanagement/cdr.html