To: The US Department of Education
From: The Informal Working Group on Repayment Rates
Date: September 30, 2013

Proposal for a Repayment Rate Trigger in the Gainful Employment Metric

Introduction

When the Department of Education published the first Gainful Employment rules in 2011, repayment rates were an important metric, part of a test to determine whether or not a program has adequately prepared a student for employment in a recognized occupation.[1]

The repayment rate calculation supplemented the debt-to-earnings ratios by capturing outcomes of all students who had enrolled in a program, not just those who completed it. By measuring students' financial wellness – whether they were paying down their loans – the repayment rate added important context to the debt-to-earnings ratios, which measure relative debt burden regardless of whether it is practicably manageable.

Secondly, repayment rates act as a mirror to cohort default rates, which, as the 2012 Senate H.E.L.P committee report extensively detailed, are easily manipulated by unscrupulous institutions. For example, with loan default rates 25% higher than proprietary schools across the sector, Kaplan Higher Education Corporation hired an internal default management staff and contracted with third party companies in order to try and reduce their student default rates. Default managers were paid a fee for each default they successfully "cured" – which in practice almost always meant putting students in deferment or forbearance, not actually getting students back into repayment.[2] Cohort default rates, therefore, are an unreliable metric without repayment rates to capture the students whose loans are growing ever larger in forbearance.

Finally, as this proposal envisions it, a high repayment rate would act as a "safe harbor" for well-performing programs, exempting them from further regulation. High repayment rates among all former borrowers allow us to assume that unreasonable debt burdens are not a problem for program graduates.

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[1] 34 U.S.C §668.7 (a)(1)
[2] United States Senate Health, Employment, Labor, and Pensions Committee, *For Profit Higher Education: The Failure to Safeguard the Federal Investment and Ensure Student Success (2012).*

The Repayment Rate

In the DC District Court's decision last summer, the Court took no issue with the repayment rate calculation itself, but made it clear that the Department needs to "make rational and informed decisions about how the relevant thresholds are determined."[3] This is not a particularly high bar for the Department to meet. This memo does not include recommendations for specific thresholds, but rather proposes that the Department task an expert panel to determine appropriate thresholds and the best definition of repayment rate to use. Given the longstanding statutory precedent for measuring students' ability to repay loans (CDRs) and well established lending industry risk standards, there are clearly models for the Department to rely upon in crafting the gainful employment rule. By convening an expert panel to explore such models, the Department should be able to articulate a reasoned, rational, and defensible basis for the repayment thresholds that is established.

The Repayment Thresholds

The repayment proposal creates three thresholds that sort programs into various bands of regulation. This model serves several purposes. First, it allows well-performing programs "safe harbor" from the debt-to-earnings analysis, lessening the administrative burden on the Department of Education and creating an incentive for moderately performing programs to improve. Secondly, it allows the Department to almost immediately eliminate the worst performing programs, protecting students from languishing in poor programs. Finally, it creates clear, simple expectations for those programs whose repayment rates place them in the moderate band and allows the Department to focus its attention on those programs that demonstrate a willingness to improve their student outcomes.

Under this proposal, programs with a median debt burden of zero will be exempted from the regulation. This exemption continues the spirit of the 2011 rule, which noted in its executive summary that:

> … we are revising the regulations to provide that programs with a median loan debt of zero are meeting the measures. This clarification is a logical extension of the debt measures since programs with a median loan debt of zero are not placing any debt burden on the majority of their students. Program Integrity: Gainful Employment Debt-Measure Rules, 76 Fed. Reg. at 3440176.

As this rulemaking session is primarily concerned with the effect that a high debt burden has on the graduates of Gainful Employment programs, incorporating this exception into the final rule is serves the mission of both protecting students and well-performing, affordable institutions.

[3] *Ass'n of Private Colleges & Univs. v. Duncan*, 870 F. Supp. 2d 133, 165, 2012 U.S. Dist. LEXIS 90434 (D.D.C. 2012)

High Repayment Threshold Triggers a Safe Harbor

Programs with a "high" repayment threshold (to be determined by an expert panel) will be given a safe harbor from further regulation. As discussed above, a high repayment rate demonstrates that students are able to reasonably manage their loan debt and, therefore, allows for the assumption that the debt-to-income ratio is reasonable.

As the Department opined in the 2011 Notice of Proposed Rulemaking, the repayment rate can provide regulatory flexibility for "programs that may have high debt-to-income ratios for completers but enroll prepared and responsible students who understand their financial obligation."[4]

Moderate Repayment Threshold Triggers a Closer Look

When programs fall between the high and low repayment rates, they will be subject to further scrutiny from the Department. In order to continue receiving Title IV funds, programs will need to demonstrate the following:

1. <u>Programs in the Moderate Repayment Rate Must Meet Both Debt-to-Earnings Ratios</u>

   The annualized and discretionary debt to earnings ratios introduced by the Department (herein DTE) in the proposed rules are an important measure of the affordability of student loan debt, appropriateness of graduate job placement, and the success of a programs education goals. This proposal does not seek to change their structure, but rather to pair them with an analysis of programmatic repayment rates.

   Programs falling in the median repayment band would be required to meet both DTE ratios, because they are most informative when read together. Annual DTE ratios provide the most protection to upper income borrowers, while discretionary DTE ratios provide protection to low income borrowers. A bivariate formula like the one currently proposed fails to provide a complete picture of the borrower's financial health.

2. <u>Programs in the Moderate Repayment Rate May Have Their Job Placement Rates Audited</u>

   A high job placement rate, when coupled with a mediocre repayment rate and a high DTE ratio, should be a red flag to regulators. If students are working in the jobs the program is designed to train them for (or jobs with a comparable pay scale), then that employment should be reflected in both the repayment rate and the DTE ratios. An audit of the placement rate is an appropriate tool to assist regulators in determining the veracity of the programs placement claims and, possibly, adjust the Gainful Employment rules to be a more accurate measure of student success.

[4] Program Integrity: Gainful Employment Debt-Measure Rules, 75 Fed. Reg. 43618.

Job placement rates are one of the most helpful disclosures for students, but the lack of a standard definition for what constitutes a job – not to mention what constitutes placement – means that they can be one of the most deceptive disclosures. The authors of this proposal fully support the proposal for a standardized job placement rate in order to make the disclosure more meaningful to the students who rely on it.

3. <u>Institutions with programs in the Moderate Repayment Band Must Apply for Upfront Approval of New Programs</u>

Upfront qualification of programs has been a contentious issue of discussion by Gainful Employment negotiators, and Barmak Nassirian and Margaret Reiter are submitting full proposals on the issue. Targeting new program approval requirements at institutions with mediocre program repayment rates makes sense because these institutions may have institution-wide issues with debt and repayment. In contrast, institutions where repayment rates are all high should be given the benefit of the doubt that they can create new programs of high value for students.

Approaching upfront approval of new programs in this manner solves two of the problems that were most widely cited in the discussions surrounding the issue. First, it provides the Department with a targeted analysis, relieving regulators of the cumbersome task of reviewing every programmatic evaluation. Secondly, it ensures that well-performing institutions are not burdened by overregulation, and that their new programs are not delayed by additional and unnecessary scrutiny.

Low Repayment Rate

In the first year, programs with a low repayment rate (to be determined by an expert panel) will be subject to all of the additional scrutiny described above. However, in the second year, programs with a low repayment rate would no longer be eligible for Title IV.

To ensure that the burden of due process is met, a program would be able to appeal the loss of Title IV funds for one year if they can show that both of their DTE ratios meet the Departments required thresholds and that at least 70% of their students go on to graduate the programs they enroll in.

Conclusion

The proposed repayment thresholds create a workable solution to reward well-performing programs, focus regulatory action on programs with the ability to improve, and eliminate programs that fail to serve students.