Improving Gainful Employment

Suggestions for Better Accountability

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President Barack Obama took to the Northeast in late August to unveil a new plan for college affordability. Standing before raucous crowds at several universities, he laid out a reform agenda, which included the idea that "it is time to stop subsidizing schools that are not producing good results, and reward schools that deliver for American students and our future."[1] Obama would do this by having the U.S. Department of Education (Department) produce a rating of colleges and asking Congress to tie the results of those ratings to aid eligibility.

While the ratings plan received widespread attention from the mainstream media, the Administration released another higher education accountability plan a week later that drew little notice outside the trade press. If enacted, the proposal would accomplish the first half of what the President called for, directly targeting the parts of higher education with some of the worst results for students. Even better, the plan can be carried out without any congressional involvement. All it requires is defining a six-word phrase.

That phrase is "gainful employment in a recognized occupation." It's a clause that has been in the Higher Education Act in one form or another since the law was first enacted in 1965. Today, all programs offered by for-profit colleges, as well as many non-degree programs at public and private nonprofit colleges, must show they are preparing their students for gainful employment in order to maintain eligibility for federal student aid.[2] Despite being in statute for nearly 50 years, there was never an attempt to formally define that phrase until the Obama Administration took office.

The proposal released in August would define what it means to prepare students for gainful employment by judging programs' performance on several outcome measures.[3] These metrics try to measure what students are getting for their educational investment by looking at how much they are earning three and four years after they graduate compared to the amount of debt they took on to pursue a program. Programs that repeatedly fail to meet or exceed these performance standards would have their access to federal financial aid limited and eventually revoked.

The late-August proposal has a long way to go before it can become a regulation. First, the Department has to hold "negotiated rulemaking" sessions, in which a group of stakeholders with vested interests (such as students, college representatives, accreditors, etc.) come together to discuss the regulatory text. If the negotiating panel can reach unanimous consensus on a proposal, the agreed-upon language becomes the final rule. If the group does not, then the Department can propose its own rule, take public comment, and then publish a final rule that incorporates feedback. It's an arduous process that can take over a year to finish.

The first meeting of the negotiating committee took place in early September with a wide-ranging discussion that showed just how many decisions must go into crafting a good rule. It also left a number of unanswered questions about how to address potential loopholes in the Department's proposal, balance second chances for failing programs with the need to protect students from expensive, poorly-designed programs, and make sure the suggested metrics are an accurate measurement of how well a program serves students. How these issues get solved will have significant ramifications for the for-profit higher education sector and a significant number of programs at community colleges. The development of the rule will also be critical for informing how all of postsecondary education could be held accountable in the future, whether through a ratings system or some other mechanism.

Recognizing those difficulties, this policy brief addresses some of the thorniest challenges within the gainful employment rule by offering clear, simple, and actionable policy suggestions, backed up where possible by impact estimates.

In total, these recommendations propose the following accountability system:

- Programs' performance and ability to maintain federal student aid eligibility would first be tested on three minimum performance standards that a program would have to meet or exceed. The standards are:

1. A repayment rate test of whether the cumulative principal owed on federal student loans for all borrowers in a program was reduced by at least $1 from the time the cohort entered repayment until four years after.
2. A student withdrawal rate test of whether no more than 33 percent of students left school between the start and end of an award year—a regulatory standard that has existed in some form for over three decades.
3. A minimum income test of whether graduates' average income at programs with student debt is at least equal to or greater than the annual income of someone making the federal minimum wage.

- Programs would be labeled as "passing," "struggling," or "failing based upon their results on these tests. A passing program meets or exceeds all the requirements on all performance tests, while a failing program does not meet any of the requirements. A struggling program meets only one or two of the requirements.

- Next, programs would be judged on an annual debt-to-earnings rate that measures the average income of graduates three and four years after leaving school compared to their average annual payments on federal and private student loan debt. Programs' performance on this measure would also be judged as "passing," "struggling," or "failing" as follows:
    - A passing program is one in which average annual debt payments make up 8 percent or less of graduates' average annual income.
    - A struggling program is one in which average annual debt payments make up more than 8 percent, but no more than 12 percent of average annual income.
    - A failing program is one in which average annual debt payments are greater than 12 percent of average annual income.

- A program can be no better than the worst level achieved on either the minimum performance tests or the annual debt-to-earnings rate. So a program that fails the minimum performance tests cannot be "saved" and categorized as passing by having a low debt-to-earnings rate. This means a program can pass if it meets or exceeds all the requirements on the minimum performance tests and has a debt-to-earnings rate of 8 percent or less.

- Programs would lose eligibility for federal student aid under any of the following circumstances:
  - Not pass at least once in a four-year period.
  - Fail twice in a three-year period.
  - Programs with excessively poor results on the debt-to-earnings rate—defined as 200 percent above the failing threshold, which is over 24 percent of annual earnings—would lose eligibility immediately.

- Both failing and struggling programs would have to commit to improving in order to maintain aid eligibility.

While data do not exist yet to model all the items in this proposal, estimates of the effects modeled with available data show that 67 percent of programs would pass under the New America proposal versus 78 in the Department's version. The programs that pass under the Department's proposal but not New America's would instead be struggling. Both proposals have the same failure rates, but New America's would have the worst 1 percent of programs lose eligibility immediately. (See table 6 on page 16 for the full effects estimate.)

The Department's Proposal

The Department's new proposal is the Obama Administration's second stab at defining gainful employment. During a regulatory process that ran from 2009 through 2011, the Department worked with stakeholders to propose a set of accountability tests for judging whether programs subject to the gainful employment requirement are preparing their students in a way that meets the law's intent.

The regulation finalized in 2011 would have held programs accountable using three outcomes-based tests. Two measures were debt-to-earnings rates, a comparison of the average income of graduates three and four years after leaving school to their average annual student debt payments, including federal and private loans. The "annual" debt-to-earnings rate compared loan payments to all income. The "discretionary" debt-to-earnings rate looked at debt payments compared to remaining income after subtracting out some funds for basic expenses. The third metric looked at whether federal student loan dollars were being repaid by students after three and four years in repayment, regardless of whether or not they finished their program.

Each measure had an acceptable performance threshold. A program failed the debt-to-earnings rates if the average annual debt payments of graduates were more than 12 percent of annual income and over 30 percent of discretionary income. A program failed the repayment rate if less than 35 percent of the loan dollars borrowed by students had declining balances. Failure to meet at least one of these thresholds three times in a four-year period would have resulted in a program losing access to federal student aid funds. Though programs that lost federal student aid eligibility could still operate at schools' discretion, most programs that lost access to these funds would likely shut down because federal aid is often their predominant source of revenue. This is particularly true at for-profit colleges, where federal student aid dollars can easily exceed 70 to 80 percent of revenue.[4]

The final regulation survived an intense public and behind-the-scenes lobbying campaign from the for-profit college sector, which had the most programs likely to fail the metrics and risk losing federal aid eligibility. Those efforts did win several concessions from the Department that made it easier for more programs to avoid penalties and gave those that failed more time before harsher consequences would kick in.[5] Despite these changes, the main trade association representing for-profit institutions sued the Department to challenge its legal authority to issue the rule. Hours before the rule was supposed to take effect in 2012, a federal judge struck down the entire regulation except for a few disclosure requirements. U.S. District Court Judge Rudolph Contreras ruled that while the Department had the legal authority to provide a definition for gainful employment, it had not sufficiently justified how it chose the 35 percent threshold for failure on the repayment rate.[6] Because Contreras found that benchmark did not show reasoned decision-making—a standard applied to regulations promulgated by the executive branch—he ruled that the repayment rate was invalid. In addition, he ruled that since the repayment rate was inextricably intertwined with the other measures, eliminating it invalidated the entire accountability system.[7]

As a result of the judge's decision, the Department has to restart the entire regulatory process around gainful employment. The general framework of the Department's latest proposal is not radically different from the struck-down regulation. Rather, it keeps most of the same measures, but includes tweaks that would make the accountability system both tougher on colleges and easier for the Department of Education to implement.

There are three main changes between the final rule and the 2013 proposal. First, the Department would exclude the repayment rate as an accountability measure, meaning a program's results would be based only upon the two debt-to-earnings rates. Doing so presumably reduces the rule's legal risk since the repayment rate threshold proved to be the problematic component of the previous rule.

Second, the Department created an additional performance tier between passing and failing, which it calls the "zone," but for the purposes of clarity is identified in this brief as "struggling." This tier acknowledges that experts recommend borrowers should not spend as large a percentage of their income on student loan payments as the threshold for failing rates allows. As summed up in a 2006 College Board report, multiple studies have argued that student loan payments should not constitute more than 8 percent of someone's annual income or 20 percent of his or her discretionary income—a figure that's derived by looking at the maximum amount of debt service an individual should have and how much of that should be consumed by housing expenses.[8] But a program is only failing to prepare students for gainful employment in the Department's proposal if its average debt payments are above 12 percent of average annual income or 30 percent of average discretionary income. This means a program could have a level of debt relative to income up to 150 percent above the recommended maximum, but still not be considered failing to provide gainful employment. The struggling designation thus fills in the gap between the passing and failing debt-to-income levels. In terms of numerical thresholds, this means a struggling program has debt payments that are above the passing thresholds of 8 percent of annual income and 20 percent of discretionary income but has an annual rate no more than 12 percent, a discretionary ratio no more than 30 percent, or both.

Finally, the Department reduced the number of failures allowed before a program loses federal student aid eligibility. The suggested rule would remove a program's aid eligibility if it fails twice in any three-year period. This is one year shorter than the 2011 rule, in which a program would lose eligibility if it failed three times in a four-year period. In addition, struggling programs would lose eligibility if they do not pass at least once in a four-year period. The result is that the worst performers must improve more quickly and middling actors now also risk losing aid eligibility.

If implemented, the Department's new proposal would likely increase the number of programs that are labeled failing compared to the rule it published in 2011. Data released following the publication of the 2011 rule showed that about 5 percent of programs failed all three tests. By contrast, estimating the 2013 proposal on newly released data indicates that 9 percent of programs would fail and another 13 percent would be struggling. That means over one-fifth of programs could potentially be in trouble if their results did not change over multiple years.[9] (See "The Data Used to Measure Effects" on page 10 for more on the figures behind these estimates.)

Many elements of the Department's plan are sensible. The repayment rate as defined in the 2011 regulation is a legal risk, and it would be hard to set a clear threshold based upon available data. A faster ineligibility time period reflects the fact that these rules have already been issued once, and the concepts they capture are no longer new. And adding the struggling label is important for strengthening a message of continuous improvement, rather than targeting only the worst performers.

But some elements of the Department's proposal have potential weaknesses. First and foremost, the accountability metrics under consideration would only deal with graduates, meaning a program in which only 10 percent of students finish could still end up passing, provided that small group has sufficient income relative to its debt. The debt-to-earnings ratio construction also means programs could pass with income levels that are leaving graduates impoverished as long as the debt amounts are not too high. For example, the average income of graduates from the certificate program in medical insurance coding at the Pittsburgh branch of the Everest Institute was just $14,614—less than what someone working full time at the minimum wage makes in a year. But students graduating from that program had average annual student loan payments of just $809, giving it an annual debt-to-earnings rate of 5.5 percent that easily met the standards to pass. Focusing only on income relative to debt ignores the investment of time, grant aid, or out-of-pocket money students spend on programs in addition to what they borrowed for attending. The final concern is that the timing of consequences may still be too lenient, giving even the worst-performing programs many chances to keep receiving financial aid and harm students.

Repayment Rates and Program Level Cohort Default Rates

The student loan repayment rate threshold proved to be the original gainful employment rule's fatal flaw. The Department now proposes that programs only disclose repayment rates and would not attach consequences to

Table 1. Comparing the U.S. Department of Education and New America Foundation Gainful Employment Regulation Proposals

Element	U.S. Department of Education	New America Foundation
Accountability Metrics	Two: both based on debt and income	Four: one based on debt and income and one each on loan repayment, dropouts, and minimum income
Performance Categories	Passing Struggling Failing	Same
Passing	Meet one of the two debt and income tests	Meet all four tests
Failing	Fail both debt and income tests	Fail either the debt and income test and/or the repayment, dropouts, and minimum income tests
Struggling	In between passing and failing	Same
Value test	Debt and income tests	Same but with repayment test
Non-completion test	None	Dropouts and repayment tests
Low income test	None	Minimum Income
Loss of federal aid eligibility	After two to four years	Same, but after one year for lowest-performing programs

Source: New America Foundation.

their performance. Though legally safer, the absence of a repayment rate as an accountability measure leaves a potentially significant loophole in the regulation. Without the repayment rate, gainful employment programs would only be judged on the economic success of their graduates. That means programs with high rates of non-completion would not be accountable for having lots of students drop out without a credential. For example, a program could still pass the debt-to-earnings measures if only 10 of its 1,000 students graduate, so long as that small group has sufficiently high income and low debt.

During the first negotiation session in September, the Department suggested addressing this issue by judging programs based upon their cohort default rates. These measure the percentage of student loan borrowers from an institution who enter repayment in a given year and default on their loans by the end of the third fiscal year (e.g., those who entered repayment in fiscal year 2010 and defaulted by the end of the 2012 fiscal year). Congress introduced penalties for schools with high cohort default rates in the early 1990s after the national student loan default rate hit 20 percent.[10] For-profit colleges, which accounted for 80 percent of defaults at that time, were a major driver of these high figures and were also accused of engaging in unscrupulous practices, including operating fly-by-night operations that took student aid dollars and left students with nothing to show for their investment.[11] In the most recent set of cohort default rate data, for-profit colleges represented 31 percent of borrowers in repayment and 46 percent of those who had defaulted.[12]

The Department provided few details about its program-level default rate proposal, but said it would build off the existing institutional rate, only applied separately to each program within a school. That suggests it would likely use the same performance thresholds that colleges are currently held to—a loss of eligibility for federal student aid if their default rates are above 30 percent for three consecutive years or 40 percent in one year. The Department also indicated the program default rates would be administered separately from the debt-to-earnings rates, meaning passing the programmatic default rate could not be a way to avoid penalties associated with failing the debt-to-earnings tests.

A program-level cohort default rate has the advantage of drawing on statute to establish thresholds and calculations. But it also has some drawbacks. First, cohort default rates require at least 30 borrowers over three years to be measured. By contrast, the Department had suggested holding programs accountable under the debt-to-earnings rate if income data can be obtained on at least 10 graduates. Establishing different minimum program sizes creates confusion. Second, there are a decent number of institutions that offer only a single program. For these institutions, there is no distinction between a programmatic and institutional cohort default rate. In other words, it would be a completely duplicative measure for these schools that adds no value. Finally, several groups have raised concerns that cohort default rates can be manipulated by getting borrowers to take advantage of deferment or forbearance options that prevent them from defaulting within the measurement window.[13] A programmatic measure would not fix that issue.

Recommendation: Reinstate the repayment rate

One reason the judge's ruling on the repayment rate threshold invalidated the entire gainful employment accountability system is that he found that measure to be inextricably intertwined with the other metrics. The program-level cohort default rate discussed by the Department of Education would presumably avoid that problem by judging its results separately from the debt-to-earnings ratios. If the Department is confident that this separation could avoid a legal risk that could jeopardize the overall rule, then the Department should use the repayment rate, but calculate it in a different way, as suggested below. Setting up a separate accountability regime will already be difficult and time-consuming, so it would make more sense to use the more meaningful repayment rate.

Recommendation: Use a pooled repayment rate

The version of the repayment rate the Department proposes disclosing to prospective students would measure the rate at which individual borrower outcomes occurred. In other words, each borrower had his or her own outcome—he or she did or did not repay—and the rate is the percentage of borrowers who can be described as repaying. But this approach requires making a judgment as to the percentage of borrowers that has to be successful or unsuccessful before sanctions kick in—a determination that is nearly impossible with currently available data.

Instead of continuing to seek out standards based upon rates of individual performance, a program's repayment rate should be measured by treating all loan dollars borrowed and payments made on them as if they were a single debt. In other words, a program would be judged on whether the total amount of outstanding principal owed at the end of the fourth year of repayment is at least $1 less than the outstanding principal amount owed at the time those debts entered repayment. Alternatively, the calculation could be made by seeing whether the total amount of outstanding principal at the end of the fourth year is at least equal to what the total amount of outstanding principal would be if that combined debt was one loan on a standard 10-year repayment plan. Any program that does not meet this pooled repayment rate test would become either a struggling or failing program, depending on whether it failed the other minimum performance tests.

Either formulation benefits from the fact that it does not have a threshold—either the total loan debt owed is reduced or it is not. This simpler formula approaches the program the way someone investing in it might: Is the total amount of funds lent to that school being retired in a timely manner? It also avoids the problems associated with the manipulation of cohort default rates, since usage of deferment or forbearance will increase the amount owed through interest accrual and make it harder to pay down principal owed.

This proposal has some potential drawbacks. First, students who make significant prepayments or retire their debts in full can reduce the overall amount owed substantially, potentially masking a larger number of struggling students that are not making large enough payments to reduce their balance owed. Relatedly, this formula attaches greater weight to larger debt balances, since their potential for reduction from the balance owed upon entering repayment to the outstanding balance four years later is greater than that of smaller debts. That said, larger loans that are not being repaid can also accumulate more interest, making it harder to reduce the overall principal balance. Finally, students on income-based payment plans in a way that make payments less than the amount they accrue in interest will have their balances grow and make it harder for a program to repay its loans overall. But looking at all loan dollars pooled together means borrowers not on these income-based plans could outweigh the negative effects of those who need these plans by making larger payments.

Non-Completers

Broadly speaking, the Department's original gainful employment regulation targeted two main issues that policymakers are concerned are too common in vocationally oriented sectors of higher education: (1) programs may cost too much compared to the benefits students receive from them and (2) programs may have too few students completing. The debt-to-earnings ratios measured the concept of value in strictly economic terms—if we assume that completing a program gave an individual some level of improved financial standing, is the income they receive sufficient enough that the continued costs a graduate pays for a program through loan debt do not make up too much of his or her income?

But the Department's latest proposal does not contain any provisions that would address high rates of non-completion. The debt-to-earnings rates only look at graduates. And the measure that did include non-completers in the 2011 rule—the repayment rate—would not be used as an accountability metric. Many consumer groups are concerned that not holding programs accountable for high dropout rates will create a loophole that would allow a program to pass even if only a small fraction of its students ever earn a credential.[14] After all, a program that only sees one out of every 10 students through to completion is certainly not preparing its students for gainful employment in a recognized occupation.

Debt-to-earnings rates are not the solution to this problem. They measure whether students who did everything that was expected of them by completing a program are getting sufficient benefits relative to their costs. That proposition makes less sense for a non-graduate, since there may be reasons outside of a school's control for why someone does not finish. Non-graduates are also likely to have less debt than a graduate, since they were not enrolled as long.

While loan repayment measures provide some accountability for non-completion, it's still a fairly indirect measure. To better address dropout concerns, a proposal for gainful employment should incorporate existing measures of non-completion that have been in regulation for nearly 40 years.

Recommendation: Adopt a 33 percent withdrawal rate standard based off existing regulations

Current regulations state that institutions seeking to participate in the federal student aid programs for the first time have to show that no more than 33 percent of their undergraduate students withdrew during the college's most recent award year.[15] Students who withdraw and still receive a full refund of their tuition and fees are excluded from the calculation and not counted as withdrawals. The withdrawal provision in its current form dates back to 1994, when it was addressed by regulations following the 1992 reauthorization of the Higher Education Act.[16] But the idea of high withdrawal rates as a sign of insufficient administrative capability to participate in the federal loan programs has existed in regulations since 1975, including a threshold of 33 percent since 1979.[17]

From 1975 to 1994, the Secretary or Commissioner of Education could decide on a case-by-case basis whether high withdrawal rates were an indicator that an institution lacked sufficient administrative capability to continue participating in the student aid programs. Regulations promulgated in 1994 aimed to strengthen this provision. In a proposed rule issued in February 1994, the Department suggested making a withdrawal rate above 33 percent an automatic sign that a school lacked sufficient administrative capability to administer the aid programs, which could carry immediate consequences that would limit, suspend, or terminate a college's participation in the student aid programs. Recognizing that some institutions would fail to meet this standard, the Department said existing colleges that had too high a withdrawal rate could be provisionally certified for the student aid programs as they worked to improve. In response to comments, the Department ultimately decided to restrict the withdrawal requirement only to institutions seeking approval for the first time and removed it as a potential sign of insufficient administrative capability for all other colleges. That provision has not been changed since and the underlying language in the Higher Education Act that allows the Secretary to define financial and administrative capability standards for institutions participating in the student aid programs remains.

The Department justified its 1994 decision to apply the withdrawal standard only to new institutions on the grounds that it would be duplicative of non-federal oversight that does not exist today. In its commentary on the final rule, the Department noted that the problems identified with the 33 percent standard should be caught by a set of newly authorized agencies known as State Postsecondary Review Entities (SPREs).[18] The SPREs were supposed to be the state part of a new oversight triad, which would also be composed of the federal government and accreditation agencies. But these entities never really came to fruition and were defunded by Congress in 1995, thus taking away the main rationale advanced by the Department for removing the withdrawal requirement from not just institutions with gainful employment programs, but all colleges and universities.

Recognizing that no set of state agencies across the country has appeared to fulfill the role in the triad that SPREs were supposed to perform, the Department should reinstate the withdrawal requirement for at least gainful employment programs, and potentially all institutions of higher education. A program with a withdrawal rate above 33 percent would become either a struggling or failing program depending on whether it also failed the other minimum performance tests.

Debt-to-Earnings Rates

The concept of annual and discretionary debt-to-earnings rates introduce an important new concept of accountability into how we think about colleges and universities. Holding a program responsible for the amount its graduates earn compared to their debt levels provides an automatic check on the claims of well-paying and in-demand jobs that dominate so much of the marketing around vocational programs.

But these measures are not perfect. The annual debt-to-earnings rate, for instance, allows a program that's utterly unsuccessful in terms of an economic return to graduates to still pass, as long as debt levels are not too high. For example, Table 2 below shows that of the 8,506 programs that had annual debt-to-earnings rates of 8 percent or less for 2008-09 graduates, 2,962 (35 percent) had average incomes below 150 percent of the poverty level for a single individual ($17,235).[19] And 1,033 of those programs actually had average incomes below 100 percent of the poverty line. Programs in the other performance categories showed similar results. Among the 1,501 programs in the struggling zone of neither passing nor failing the annual measure, 46 percent have average incomes below 150 percent of poverty. By contrast, 33 percent of the programs that fail the annual debt-to-earnings test had average incomes below 150 percent of the poverty line.

It's arguable whether allowing programs whose graduates have low income and debt to pass is a problem. From the standpoint of judging only the return on the federal loan investment, low levels of debt mean policymakers do not need to care as much about the income those graduates earned. But such a stance ignores the substantial investment of other forms of federal grant aid that is also occurring, not to mention the opportunity cost that students incurred to complete a purportedly postsecondary program that is leaving them essentially impoverished. For example, initial gainful employment data released by the Department of Education in 2012 had data on four certificate programs at the South Florida Institute of Technology, a for-profit college in Miami: computer and information sciences support services; electronics equipment installation and repair; heating, ventilation, air conditioning, and refrigeration technician; and medical assisting. All of these programs easily pass because students graduating from these programs had annual debt payments of between $69 and $96 and annual debt-to-earnings rates well below 1 percent. But 100 percent of the students at the school received Pell Grants, representing over $3 million in federal dollars funds.[20] That substantial investment in grant aid has not resulted in particularly good outcomes for students—graduates from the four programs had average incomes ranging from just $11,508 for medical assisting to $16,652 for the electronics equipment installation and repair.[21]

A focus on relative and not absolute income also ignores the importance of debt levels in context. A student who is earning $30,000 a year is likely less burdened by $2,400 in annual loan payments than another student who earns $10,000 a year and pays $800, even though both are spending 8 percent of their income on student loan payments. For extremely low-income individuals, even a debt burden of 8 percent may be

Table 2. Programs with average incomes below 150% of the poverty line, by category

Category	# Programs	# Below 150% of poverty	Percent
Passing	8,506	2,962	35
Struggling	1,501	684	46
Failing	1,043	345	33
Total	**11,050**	**3,721**	**34**

Source: New America Foundation analysis of U.S. Department of Education data.

too burdensome. Statistics from the government-based Direct Loan program underscore how low amounts of loan debt can still lead to default. As of June 2013, the average student loan balance for borrowers in default was $14,500. By contrast, the average balance for borrowers in repayment was $21,300, about 47 percent greater.[22]

The Data Used to Measure Effects

The estimated effects presented in this paper are all based upon actual income and student loan figures for 11,050 gainful employment programs, which were released in August 2013 by the U.S. Department of Education. The average income information is from the Social Security Administration and reflects the higher of the mean or median income in calendar year 2011 of students that completed a gainful employment program in the 2008 or 2009 federal fiscal years (October 1, 2007 through September 30, 2009). Average student loan debt payments include all sources of loans, including federal, private, and institutional. Only students that received any form of federal student aid—Pell Grants, Stafford Loans, etc.—are included. For more on the data and methodology, see: http://www2.ed.gov/policy/highered/reg/hearulemaking/2012/2013-methodology.pdf

Some instances in the text refer to results at specific institutions. Because the data released in 2013 did not include the name of the school offering the program, any data point that names an institution is from a separate 2012 data release. In those cases, the data are based upon all students, regardless of whether they received federal student aid, who completed a program in the 2007 or 2008 federal fiscal years (October 1, 2006 through September 30, 2008). For more on these figures, see: http://studentaid.ed.gov/about/data-center/school/ge

In theory the discretionary debt-to-earnings rate allows programs with higher average incomes to have a larger percentage of their incomes go to debt payments after, making a deduction for necessary expenses. But in practice, the discretionary debt-to-earnings measure helps almost no programs earn a better performance designation. Programs that pass the discretionary measure almost universally also pass the annual measure. The reverse is not true—a large number of programs that pass the annual measure fail the discretionary one. A few programs identified as struggling on the annual rate would pass thanks to the discretionary rate. But half of the programs in that position are within 1 percentage point of passing the annual rate anyway and could end up being a passing program during the four-year period are granted before losing eligibility.

Table 3 below shows the distribution of programs by how they fared on each of the two debt-to-earnings rates based on actual income data provided by the Department. Of the 11,050 programs with income data for 2008 and 2009 graduates, 8,763 pass at least one debt-to-earnings measure. Overall, 53 percent of programs pass both measures. Another 2,630 (30 percent) pass the annual measure but not the discretionary one. But just 167 programs pass the discretionary debt-to-earnings rate and not the annual one. This includes just 12 that fail the annual rate and pass the discretionary one. And the discretionary rate helps move just 60 programs from failing to struggling. That's 2.6 percent of programs positively affected by the discretionary rate, including 0.8 percent saved from failing because of the discretionary measure, versus 34.5 percent helped by the annual measure alone.

Table 3. Comparing program results on the two debt-to-earnings tests (%)

N = 11,050		Annual		
		Passing	Struggling	Failing
Discretionary	Passing	53	1	0
	Struggling	3	1	<1
	Failing	21	11	9

Source: New America Foundation analysis of U.S. Department of Education data

Though programs pass or fail the discretionary debt-to-earnings metric, it's important to understand that sometimes that failure is due to excessive levels of debt;

other times it's because incomes are very low. For example, a program with average income below 150 percent of the poverty line will have $0 in discretionary income, meaning it will fail the discretionary debt-to-earnings test as long as its graduates have at least $1 in average student debt payments. While this may seem harsh, it reflects that someone living in or close to poverty is probably struggling to afford food and housing, let alone making student loan payments. Table 4 below breaks down the number of programs that fail the discretionary measure, showing how much debt 30 percent of their discretionary income represents on a monthly basis, compared to their average actual monthly loan payments.

As Table 4 shows, nearly three-quarters of programs that fail the Department's discretionary measure do so because their graduates have so little income that making the minimum student loan payment of $50 each month ($600 a year) would be more than 30 percent of their discretionary income on an annual basis. This includes 2,671 programs (59 percent of those that fail) in which graduates had average discretionary income of $0 and thus could not support any debt at all.

Restricting the analysis to just the 2,344 programs that pass the Department's annual measure but fail its discretionary one shows how low-return programs are not being held accountable under the Department's proposal. The mean annual income for these programs is $15,020—$2,215 below the 150 percent of poverty threshold and about $60 less than someone making minimum wage working full-time for a year. But these programs are still able to pass because their average annual debt is $789—about $66 a month or a total loan balance of approximately $5,710.

Acknowledging that programs with low income should still pass due to small debt levels arguably runs counter to the way Congress and the Obama Administration have designed the student loan safety net. The Income-Based Repayment program created by legislation in 2008, and the more generous Pay as You Earn program enacted by regulation in 2012, tie borrowers' student loan payments to no more than 10 or 15 percent of their income. But that 10 or 15 percent is not of total income; it is income remaining after deducting 150 percent of the poverty line for a family of the borrower's size in his or her state.[23] For a borrower with a household size of one, this calculation is nearly identical to the way discretionary income is calculated for gainful employment purposes.[24] So borrowers with incomes below 150 percent of the poverty line for their family size would have an expected payment of $0, regardless of whether they owed $1,000 or $100,000. These individuals have been determined by the safety net to be so poor that they should not have to contribute anything to their loan payments.

Table 4. The average monthly payments graduates at programs that fail the discretionary debt-to-earnings test would make if their debt were 30% of income, versus the actual average payments (n = 4,498)

Discretionary Income	% of programs that fail the discretionary-debt-to-earnings test	Maximum monthly payment if student loan debt were 30% of discretionary income	Actual average monthly student loan payment
$0	59	$0	$84
$1 - $2,000	15	$50	$122
$2,001 - $4,000	10	$100	$168
$4,001 - $6,000	7	$150	$234
$6,001 - $8,000	4	$200	$305
$8,001 - $10,000	2	$250	$376
Over $10,000	3	$250+	$499

Source: New America Foundation analysis of U.S. Department of Education data.

But the Department's proposed gainful employment language would allow programs to pass if their average debt levels are sufficiently low. This is a contradictory stance—average incomes so low that the safety net would absolve borrowers for all their monthly obligations should not pass.

Recommendation: Drop the discretionary debt-to-earnings rate

The discretionary rate provides little to no relief for programs. It also plays no meaningful role in holding programs accountable, since they can pass even if they only pass the annual debt-to-earnings rate. As a result, there is no reason to continue using it as an accountability metric.

Recommendation: Set a minimum income standard

Instead of using a discretionary income test, a program should be judged on whether the average graduate's income is equal to or greater than the annual income of someone working full time for a full year at the federal minimum wage. This minimum level better aligns the gainful employment regulations with income-based repayment plans. It also sends a strong message about how there must be some degree of economic return for a program to be considered acceptable. A program where the average income of graduates fell below the minimum recommended level would be either struggling or failing depending on whether it failed the other minimum performance tests.

The minimum wage is the suggested threshold because it is the minimum income that Congress has determined a worker must earn. Table 5 below shows the potential results of this proposal, along with outcomes for two other possibilities, both based upon well-understood thresholds. It also shows that using minimum wage as a threshold is a middle option. The highest bar would be to require all programs to have average income at least equal to 150 percent of the poverty line for a single individual in the contiguous United States, or about $17,235.[25] The lowest would be to require all programs to at least produce average income above the poverty line for a single person—$11,490. Though an easier standard than the others, it still conveys the idea that programs should not be producing graduates that on average are impoverished. The minimum wage requirement fits in between at $15,080.

Table 5 also shows that regardless of the level chosen, a minimum income cutoff would move a number of programs from passing to struggling or failing status. It could also significantly increase the rate of programs being subject to sanctions. But it does so while reflecting the reasonable principle that a postsecondary education program should at the bare minimum not leave its graduates, on average, in poverty or close to it.

Consequences of Not Passing

The consequences applied to a program with unsatisfactory results should incorporate assumptions about the likelihood of improvement, balanced with the need to protect students from bad programs. Programs where results fall just short should be given opportunities to meet the threshold. A program that is far off the mark should be given significantly fewer chances on the

Table 5. Programs where the average graduate has student debt and the average income is below recommended thresholds

			Current result on annual debt-to-earnings test (%)		
Average Income Threshold	Income	# Programs	Passing	Struggling	Failing
100% of poverty for a single individual	$11,490	696	56	27	18
Full-time at the minimum wage	$15,080	1,860	58	28	13
150% of poverty for a single individual	$17,235	2,671	61	26	13

Source: New America Foundation analysis of U.S. Department of Education data.

grounds that it has farther to go and is less likely to improve to the point where it can pass. But there should be a limit to this tolerance—a program with results so far from acceptable levels that it is obviously damaging to students does not deserve additional chances to improve because the likelihood it will cause continued harm far outweighs the odds that it will get better.

The types of consequences also matter. Failing programs that are close to avoiding that label should face penalties that encourage them to improve but do not shackle them in such a way that they cannot hope to do so. But with extremely poor-performing actors, the consequences should focus on orderly movement toward shutting down and trying to protect students. In all cases, the threat of losing eligibility for federal student aid must always be present because it is the most meaningful sanction and will be far more effective at driving change than anything else. All types of penalties should strive for simplicity in implementation to avoid bureaucratic headaches. This requirement means taking off the table theoretically attractive, but actionably complicated ideas, such as only making aid payments to programs for credits earned by students.

An additional consideration is whether programs should get a year of rates that serve only an informational purpose and have no consequences attached to the results they show. The logic for these informational rates is that programs may not know where they stand until the first figures come out, and so institutions want a chance to see results before their programs potentially face sanctions. However, by the time the gainful employment regulation under discussion is published, the metrics will have been around for nearly four years.[26] Many programs will have already had an initial shot at knowing how they are doing, and the Department could possibly release informational rates based upon voluntary reporting in the interim.

There is also little likelihood of programs improving following the release of one year of informational rates because these data are capturing outcomes of students three and four years after leaving a program. One year of informational rates would mean the first set of results with consequences would be based upon students who were two and three years out when the informational rates were released. While colleges could potentially do things to help the results of those students compared to those measured under the informational rates, the prospects for improvement over a year or two are likely modest. At this point, requests that the Department provide another year of informational rates serves as little more than a delay tactic aimed at running out the clock in the hopes that the Obama Administration ends before sanctions can occur.

Recommendation: Keep the Department's general framework

The framework laid out by the Department in its latest proposal is generally solid. Taking away student aid eligibility from programs that fail twice in any three-year period and never pass once in a four-year period successfully balances the need for better programs to be given more time and worse ones less, while still giving all parties multiple opportunities to improve. Nevertheless, some important tweaks are still necessary, as outlined below.

A program should be grouped into one of three performance categories: passing, struggling, or failing. The default consequence for a struggling or failing program should be loss of aid eligibility unless the program agrees to certain conditions: A struggling or failing program is not producing results for its students that research suggests it should. Accordingly, the default assumption for non-passing programs should be that they will lose access to federal student aid. This framework does not necessarily mean that a struggling or failing program automatically loses eligibility. It means that the program will lose eligibility unless it immediately agrees to subject itself to other consequences. An accountability system set up this way ensures that programs that have no desire to take concrete steps toward improvement are immediately removed instead of being allowed to hang around.

Recommendations for struggling programs

Upon being told it is struggling, a program should agree to be subject to some combination of the following consequences. Refusal to do so should result in ineligibility, as should not passing at least once in four years, as suggested by the Department.

> Struggling programs are teetering between passing and failing. So while they might get better and avoid trouble, they also could get worse.

Restrict student aid growth

The Department's proposal would subject only failing programs to this requirement, but a struggling program should also face this penalty. These programs are teetering between passing and failing. So while they might get better and avoid trouble, they also could get worse. Accordingly, steps should be taken to protect students by restricting the amount of federal financial aid struggling programs may receive to no more than what they took in during the prior year.

Offer a one-month trial period for new students

One problem a struggling program may face is that students drop out after a short period of time. A one-month trial period ensures that students have sufficient time to see if they like a program before making a financial commitment. A number of institutions have already implemented similar programs, showing that the idea is workable.[27]

Seek programmatic accreditation, where applicable

One reason a program may struggle to have its graduates succeed is they are not eligible to receive the state licensing or third-party certifications needed to work in the profession in which they trained. Therefore, a struggling program must agree to seek programmatic accreditation if it is either required by the state in which its graduates live or widely used for that profession and not currently held. Failure to seek programmatic accreditation or denial of an attempt to receive it would be grounds for immediate expulsion from the student aid programs.

Publicly release a performance improvement plan

After being a struggling program for one year, the institution would be required to put together a plan describing how it would improve the program to become passing. This plan would not be subject to Department approval, since the metrics themselves will serve as a check on the program's effectiveness, but it would have to be publicly posted on the school's website.

Recommendations for failing programs

Failing programs should be subject to the same consequences as struggling programs, but also:

No longer market that program

Failing programs may be forced to shut down before a student is able to complete his or her studies. Thus, it is unwise to advertise that program to future students. Accordingly, the institution would no longer be allowed to mention the program in any advertising materials.

Most failing programs should lose eligibility after two failures in any three-year period

Instead of offering informational rates, programs should be allowed to fail once before being at risk of losing eligibility. Requiring a second failure before loss of eligibility serves the same purpose as a set of informational accountability metrics in giving a program more time. It also presents an opportunity to show that a program can change, regardless of the likelihood of improvement. For example, just 10 of the 247 programs that would have failed the annual debt-to-earnings test in 2007-08 would have passed it in 2008-09. Another 53 would have moved from failing to struggling.

The lowest-performing programs should lose eligibility after one failure

Giving failing programs one free pass before losing eligibility reflects a chance at improvement. But the gainful employment rule should recognize that there is some degree of low performance so far removed from acceptable standards that ending a program's eligibility for federal financial aid is better for students and the larger world of postsecondary education than giving it a chance to improve.

The concept of minimum expected performance is already incorporated into accountability metrics like the cohort default rate, which terminates an institution's eligibility for federal student aid after just one year if it has a rate above 40 percent. In that framework, the immediate ineligibility threshold is set at 133 percent of the other penalty level. A similar standard is worth adopting here. In this case, the automatic ineligibility threshold would be set at 300 percent of the passing level. This 24 percent threshold (or 60 percent if the discretionary test is kept) culminates a logical sequence, in which programs at or below 100 percent of the maximum recommended level are passing; those between 100 and 150 percent of that mark are struggling; those between 150 and 300 percent are failing; and those above 300 percent are failing so badly that they should lose immediate eligibility. Based upon available data, the 24 percent immediate ineligibility threshold would affect 137 programs, or about 1 percent of all programs.

Measuring Effects Using Current Data

Available data on 11,050 programs measured using 2008 and 2009 graduates make it possible to gauge how many programs would be classified as passing, struggling, and failing for the minimum income test and annual debt-to-earnings rate in one year. Table 5 shows the estimated effects of this proposal compared to what the Department released. According to those figures, 67 percent of programs would pass under this proposal. An additional 23 percent would struggle and 9 percent would fail. Within the failing category, 1 percent of programs, or 137, would lose eligibility immediately.

The nearly one-quarter of programs that would be struggling includes 10 percent that earned that designation solely because graduates on average had both some student debt and income below the minimum level. Since the data do not make it possible to model the effects of the repayment or withdrawal rate tests, it is possible that some share of that 10 percent could end up failing if they did not pass either of those tests too. It is also possible that more of 67 percent could end up struggling if they did not pass both of the withdrawal and repayment tests.

Table 6. Estimated effects of the U.S. Department of Education and New America Foundation proposals (n = 11,050)

Result	U.S. Department of Education Proposal	New America Foundation Proposal
Passing	78	67
Struggling	13	23
(Due to low Income)	—	(10)
(Due to debt-to-earnings rate)	(13)	(14)
Failing	9	9
(Non-immediate eligibility loss)	—	(8)
(Immediate eligibility loss)	(9)	(1)

Note: Totals may not add up due to rounding.

Source: New America Foundation analysis of U.S. Department of Education data.

Conclusion

Though the overall numbers have decreased in recent years, a significant share of college students are still enrolled in programs that statue requires prepare students for gainful employment, particularly at for-profit colleges. With their explicit focus on specific jobs, these programs can be the ticket to a better life, more stable income, and all the other benefits that come with postsecondary education. But for too many students, the return received on their education has not come close to the time and money they invested in it, leaving them with toomuch debt and too little income to handle it. It's clear that market pressures and voluntary efforts are not sufficient to solve this problem, since the same companies keep on getting in trouble for the same issues year after year.

The Department's new proposal for gainful employment is a generally solid way to leverage governmental oversight to encourage these programs to improve. But it's only a start. The suggestions presented here would close some important loopholes and ensure that students enrolling in programs can expect at least some minimum returns for their investments. The result would be a stronger vocational training system that can truly fulfill those promises of access to a better life through gainful employment.

Notes

[1] Barack Obama, "Remarks by the President on College Affordability," Buffalo, N.Y., August 22, 2013, http://www.whitehouse.gov/the-press-office/2013/08/22/remarks-president-college-affordability-buffalo-ny.

[2] "Gainful Employment Frequently Asked Questions," U.S. Department of Education, last accessed October 31, 2013, http://ifap.ed.gov/GainfulEmploymentInfo/2011GEFAQ.html#G-Q16.

[3] "Subpart Q--Gainful Employment (GE) Programs," U.S. Department of Education, August 29, 2013, http://www2.ed.gov/policy/highered/reg/hearulemaking/2012/2013-draft.pdf.

[4] Data released by the U.S. Department of Education show that 64 percent of for-profit colleges received over 70 percent of their revenue from the federal student aid programs in 2011-12. This includes 40 percent of for-profit colleges that received more than 80 percent of their revenue from these programs. See "Proprietary School 9/10 Revenue Percentage," U.S. Department of Education, last accessed October 30, 2013, http://studentaid.ed.gov/about/data-center/school/proprietary.

[5] Libby Nelson, "Concessions or a Cave-In?" Inside Higher Ed, June 2, 2011, http://www.insidehighered.com/news/2011/06/02/new_gainful_employment_rules.

[6] Association of Private Sector Colleges and Universities v. Arne Duncan, Civil Action 11-1314 (D.D.C. 2012), https://ecf.dcd.uscourts.gov/cgi-bin/show_public_doc?2011cv1314-25 31.

[7] *Ibid* 32.

[8] Sandy Baum and Saul Schwartz, "How Much Debt is Too Much?" College Board, 2006, http://research.collegeboard.org/sites/default/files/publications/2012/9/researchinreview-2006-12-benchmarks-manageable-student-debt.pdf; Sandy Baum and Marie O'Malley, "College on Credit: How Borrowers Perceive Their Education Debt," *NASFAA Journal of Student Financial Aid,* Vol. 33, No. 3, 2003, http://www.immagic.com/eLibrary/FIN_AID/SALMAEUS/N030225B.pdf.

[9] "Gainful Employment Negotiated Rulemaking Informational Data Analysis," U.S. Department of Education, August 29, 2013, http://www2.ed.gov/policy/highered/reg/hearulemaking/2012/2013-calculations-chart.pdf. The Department figures differ slightly from the estimates presented in the text because it includes results for approximately 300 programs at public and private nonprofit institutions that appear to have been incorrectly included and would not in fact be subject to the gainful employment requirements because they are degree programs.

[10] "Federal Student Loan Default Rates," New America Foundation, (last accessed October 29, 2013), http://febp.newamerica.net/background-analysis/federal-student-loan-default-rates.

[11] "Supplemental Student Loans: Who Borrows and Who Defaults," U.S. General Accounting Office, GAO-HRD-90-33FS, October 1989, http://gao.justia.com/department-of-education/1989/10/supplemental-student-loans-hrd-90-33fs/HRD-90-33FS-full-report.pdf, 13. For more on questionable practices by for-profit colleges in the 1980s, see the 1991 reporrt by the Senate Permanent Committee on Investigations called "Abuses in Federal Student Aid Programs," which was overseen by Sen. Sam Nunn (D-Ga.)

[12] "Comparison of 3-year FY2010 Official Cohort Default Rates to Prior Official Calculation," U.S. Department of Education, July 28, 2013, http://www2.ed.gov/offices/OSFAP/defaultmanagement/cdrschooltype3yr.pdf.

[13] "Steps the Education Department Should Immediately Take to Curb Default Rate Manipulation," The Institute for College Access and Success, August 21, 2012, http://www.ticas.org/files/pub/TICAS_memo_on_CDR_evasion_082112.pdf.

[14] "Background for the September 9-11 Negotiated Rulemaking Meeting," The Institute for College Access and Success, August 19, 2013,

http://www.ticas.org/files/pub/TICAS_memo_re_upcoming_neg_reg_issues_Aug_19_2013.pdf, 4.

[15] "Standards of Administrative Capability," 34 C.F.R. §668.16(l), 2013, http://www.gpo.gov/fdsys/pkg/CFR-2003-title34-vol3/pdf/CFR-2003-title34-vol3-sec668-16.pdf.

[16] "Institutional Eligibility; Student Assistance General Provisions; Federal Family Education Loan Programs; Final Rule," Federal Register 59:228, November, 29, 1994, http://www.gpo.gov/fdsys/pkg/FR-1994-11-29/html/94-29048.htm.

[17] A maximum withdrawal rate as a sign of administrative capability was first introduced in 1975 regulations, which stated that institutions participating in the student loan programs had to have less than 20 percent of their students withdraw from the start to the end of the academic year. In 1979, the withdrawal rate requirement as a sign of administrative capability became an ineligibility requirement for participation in all of the federal student aid programs, not just loans. During that change, the Office of Education within the Department of Health, Education, and Welfare, decided to make the threshold beyond which a withdrawal rate might be a sign of a lack of administrative capability to 33 percent. See "Guaranteed Student Loan Program: Proposed Requirements and Standards," Office of Education, Department of Health Education and Welfare, Federal Register: 39-202, October 17, 1974, 37158 and "General Provisions Relating to Student Assistance Programs," Office of Education, Department of Health, Education, and Welfare, Federal Register 44-190, September, 28, 1979, 56283,56296-56297.

[18] November 29, 1994 59 Federal Register 228, http://www.gpo.gov/fdsys/pkg/FR-1994-11-29/html/94-29048.htm.

[19] "2013 Poverty Guidelines," U.S. Department of Health and Human Services, last accessed October 29, 2013, http://aspe.hhs.gov/poverty/13poverty.cfm.

[20] "South Florida Institute of Technology," National Center for Education Statistics, U.S. Department of Education, last accessed October 29, 2013, http://nces.ed.gov/collegenavigator/?q=south+florida+institute+of+technology&s=all&id=443252.

[21] "Information About the Gainful Employment Downloadable Spreadsheet," U.S. Department of Education, last accessed October 30, 2013, http://studentaid.ed.gov/about/data-center/school/ge/data.

[22] Rohit Chopra, "A Closer Look at the Trillion," Consumer Financial Protection Bureau, August, 5, 2013, http://www.consumerfinance.gov/blog/a-closer-look-at-the-trillion/.

[23] "Federal Student Aid: Income-Based Repayment Plan for the Direct Loan and FFEL Programs," U.S. Department of Education, last accessed October 29, 2013, http://studentaid.ed.gov/sites/default/files/income-based-repayment.pdf.

[24] The income-based repayment calculation is slightly more generous, since it deducts 150 percent of the poverty level from a borrower's adjusted gross income, which is lower than their annual income, but the calculation concept is basically the same.

[25] 2013 Poverty Guidelines.

[26] The concept of debt-to-earnings rates has been under discussion since 2009, the first regulations were finalized in 2011, the first rates were also published that year. The new regulation will likely go into effect on July 1, 2015.

[27] For example, see the Kaplan University Commitment at http://www.kaplanuniversity.edu/about/kaplan_commitment.aspx or the University of Phoenix Orientation Workshop at http://www.phoenix.edu/students/how-it-works/student_experience/orientation-workshop.html.

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