Date of Hearing: April 17, 2012

ASSEMBLY COMMITTEE ON HIGHER EDUCATION
Marty Block, Chair
AB 1637 (Wieckowski) – As Amended: March 7, 2012

SUBJECT: Cal Grant Program: student default risk index score.

SUMMARY: Establishes the student default risk index (risk index) and limits institutional participation in the Cal Grant Program based on risk index scores. Specifically, this bill:

1) Requires an institution participating in the Cal Grant Program to calculate and certify its risk index to the California Student Aid Commission (CSAC) by October 1st annually.

2) Requires the risk index to be calculated by multiplying the percentage of undergraduate federal student loan borrowers at the institution, as reported to the United States Department of Education (USDE) for the academic year two years prior to the year of the risk index calculation, by the institution's three-year cohort default rate, as reported by the USDE in the annual release of cohort default rates in the same year as certification.

3) Specifies that for the 2013-14 academic year CSAC shall determine the risk index for each qualifying institution using the three-year cohort default rate, federal student loan borrower data, and student enrollment data provided by USDE for the 2009 fiscal year. Provides that for each year thereafter, institutions shall use the official three-year cohort default rate to calculate the risk index.

4) Requires, beginning with academic year 2013-14, institutions participating in the Cal Grant Program to have a risk index of less than 15.

5) Provides that an institution that becomes ineligible under the risk index requirements may regain eligibility in subsequent academic years upon certification to CSAC that the risk index threshold has been met.

EXISTING LAW establishes the Cal Grant Program, administered by CSAC, to provide financial aid to eligible students attending qualified institutions. Generally, accredited institutions with eligible programmatic offerings are authorized for Cal Grant participation. Recent legislation (SB 70, Chapter 7, Statutes of 2011) further requires the following:

1) Student Loan Default: Institutions with more than 40% of their undergraduate students borrowing federal loans must have a three-year cohort default rate of less than 24.6% to be eligible for new and renewal Cal Grant awards in the 2011-12 academic year and less than 30% for each subsequent year. A limited exception allows renewal Cal Grant A and B recipients to continue to use their Cal Grant awards at a newly ineligible institution, but their Cal Grant maximum award amounts are reduced by 20%.

2) Data Collection: As a condition for participation in the Cal Grant Program, institutions are required, beginning in 2012, to annually report to CSAC enrollment, persistence and graduation data for all undergraduate students, including aggregate information on Cal Grant recipients, and the job placement rate and salary and wage information for programs that are

designed or advertised to lead to a particular type of job or are advertised with any claim regarding placement.

3) Legislative Analyst's Office (LAO) Report: The LAO is required to report to the Legislature by January 1, 2013, regarding the implementation of SB 70 and include recommendations for appropriate measures of default risk and other direct or indirect measures of quality or effectiveness in institutions participation in the Cal Grant program.

FISCAL EFFECT: Unknown

COMMENTS: Purpose of this bill. According to the author, recent college graduates increasingly find themselves saddled with massive student loan debt they can't afford to pay off. At the same time, higher education funding (including the Cal Grant Program) is at risk of major budget cuts every year. The state is spending millions of dollars sending our students to schools that are not serving them well. This bill is designed to hold schools accountable to minimum standards, limiting the extent to which Cal Grant funding goes to schools where students get into unsupportable debt. Specifically, this bill provides a refinement on the current cohort default rate calculation by accounting for both the number of students who take out loans and the percentage of students who default on their loans.

Student borrowing. Many students rely on loans to finance their education. Nationally, two-thirds of 4-year undergraduate students graduated with a Bachelor's degree and some debt in 2007-08, and the average student loan debt among graduating seniors was $23,186 (including federal loans, state, college and private loans). The following table reflects 2007-08 national data on the percentage of students borrowing and the average debt per borrower at graduation according to the type of institution and degree program:

Institution Control and Degree Program	Percent Borrowing	Average Cumulative Debt
Bachelor's Degree	65.2%	$23,118
Public	61.2%	$20,040
Private Non-Profit	70.5%	$27,535
Private For-Profit	96.0%	$32,909
Associate's Degree	47.1%	$13,289
Public	38.9%	$10,574
Private Non-Profit	71.1%	$19,294
Private For-Profit	97.8%	$19,681
Certificate	63.2%	$11,302
Public	32.0%	$9,754
Private Non-Profit	49.5%	$15,071
Private For-Profit	89.9%	$11,573

According to data provided by The Institute for College Access and Success (TICAS), the percentage of borrowers and average debt amounts for students graduating from California institutions is somewhat comparable to the national figures, with a few notable exceptions. TICAS indicates that students graduating with associate's and bachelor's degrees from California's public institutions in 2007-08 were about 10% less likely to accumulate student loan debt and the average debt for bachelor's degree students at California's public colleges was about $4,500 less than that of their national counterparts. TICAS data also shows that the average debt for students graduating with bachelor's degrees from California for-profit institutions was $37,923; about $5,000 higher than the national average.

Student loan defaults. The USDE makes student loans widely available with an expectation that upon graduation students will be able to use the education and skills obtained to secure a job with sufficient earnings to cover loan payments. Large numbers of graduating students unable to repay their federal loans can signify several problems: students may have dropped out before graduating, the economy may not be supporting jobs in the field, or maybe the degree programs did not adequately train students for employment.

A cohort default rate is the percentage of an institution's borrowers that enter repayment status on federal loans during a particular fiscal year, between October 1 and September 30, and default within the cohort default period. Students are considered to have defaulted after at least 270 days of nonpayment. The USDE, which calculates and reports cohort default rates, is in the process of moving from a two-year to a three-year cohort default period. This change is in response to concerns that the two-year window allowed default numbers to be manipulated and did not provide a realistic indication of long-run loan repayment rates. USDE released preliminary 3-year cohort default rates to the public on December 14, 2009. The following table summarizes the increase in cohort default rates from two-year to three-year for FY2007 by institution type. The first official three-year rates are expected to be made public in September 2012.

Institution Type	2-Year Rate	3-Year Trial Rate	Percentage Increase
Public	5.9%	9.7%	64%
2-year	9.9%	16.2%	63%
4-year	4.4%	7.1%	64%
Private	3.8%	6.5%	71%
2-year	8.7%	16.2%	86%
4-year	3.7%	6.3%	70%
Proprietary	11.0%	21.2%	93%

Defaulted federal loans have significant consequences for both student borrowers and taxpayers. For borrowers, defaulting on a federal loan can devastate credit, making it difficult to rent an apartment or buy a car. Borrowers who default cannot get federal grants or loans to return to school, and the government can garnish wages, seize tax refunds and eventually dock Social Security payments. For taxpayers, defaulted federal loans cost money. It is estimated that the total defaulted loans outstanding are around $40 billion, when accrued but unpaid interest and late fees are included in addition to loan principal. Because of the risk to both students and taxpayers for defaulted loans, the USDE uses cohort default rate related sanctions and benefits as an incentive for institutions to work with their borrowers to reduce defaults and prevent institutions with high default rates from participating in federal financial aid programs.

Accounting for student population differences. Proponents of this bill argue that evaluating both the percentage of borrowers and the percentage of defaults provides a more nuanced metric by which to judge the performance of institutions. Opponents, generally for-profit colleges, argue that high percentages of borrowers and defaults results from serving at-risk populations. There appears to be some evidence that risk factors that affect persistence and attainment account for some of the difference in default rates between types of colleges. According to research by Finaid.org, 60.1% of the difference between for-profit and non-profit default rates and 38.6% of the difference between for-profit and public college default rates is attributable to various risk factors among student populations. However, as noted by FinAid.org, this research does not evaluate whether the greater prevalence of high-risk students at for-profit colleges is due to open enrollment policies and better service or the exploitation of a vulnerable population. Supporters of this bill argue that education programs should prepare all students for gainful employment and that it is unacceptable to suggest that low-income and minority students should expect lower salaries and higher debts upon graduation.

Impact on students. Opponents of this bill argue that this bill would potentially result in denying access to at-risk students. However, under this proposal, student eligibility requirements would not change. The degree to which new Cal Grant recipient students would be affected by changes in Cal Grant institutional eligibility would depend on a student's ability to gain admission to a Cal Grant eligible institution. Renewal Cal Grant recipients attending an institution that loses eligibility would be provided with the option of taking their Cal Grant award to an eligible institution or continuing at their current institution with a 20% reduction in their award amount.

Governor's budget proposal. As previously noted, institutions with more than 40% of their undergraduate students borrowing federal loans must have a three-year cohort default rate of less than 24.6% to be eligible for new and renewal Cal Grant awards in the 2011-12 academic year. Under current law this threshold increases to 30% for each subsequent year. The Governor's budget proposes to freeze the default rate limit at the current-year level. The Legislative Analyst's Office supported this proposal. The Assembly Budget Subcommittee No. 2 on Education Finance took action on March 7, 2012 to refer this proposal to policy committee.

Arguments in support. The Institute for College Access and Success supports this bill and argues that by using a metric, applied to colleges of all types, that better measures a student's risk of default, this bill better targets Cal Grant dollars to support student access and success and sends a strong message that access to an affordable and quality college education is a priority for the state.

Arguments in opposition. The California Coalition of Accredited Career Schools (CCACS) argues that loan default rates are not necessarily indicative of the quality of education that students receive, and ignores the risk factors of the nontraditional students this sector serves-students who are financially independent, single parents, first generation and full-time workers. CCACS argues that these risk factors affect persistence and attainment which ultimately elevates the risk of a student defaulting; accounting for 60% of the difference in default rates between for-profit and non-profit colleges and nearly 40% of the difference in default rates between for-profit and public colleges. CCACS raises concerns that this bill could have an unintended consequence of denying access to at-risk and nontraditional students.

Potential amendments. Through discussions with the author's office committee staff understands that it is not the intent of the author for this legislation to result in denying students access to quality postsecondary education. The author has indicated a desire to establish reasonable expectations and thresholds that encourage institutions to take proactive steps to reduce the debt burden amounts and loan default rates among their student populations. To that end, the author and Committee may wish to consider amending this bill to phase in the implementation over several years. One option would be to adopt the Governor's budget proposal to maintain the loan default rate at its current level of 24.6% until 2013-14. Then the bill could phase in the risk index over five academic years, beginning in 2013-14. The risk index could begin at a relatively high figure, and be reduced annually to the ultimate goal of a risk index of 15. This would allow high-quality institutions to prepare and respond to the requirements, with minimal impact on students. Additionally, the Committee may wish to consider amendments to ensure that students attending institutions that become ineligible are informed of their options, including their option to renew their Cal Grant at an eligible institution.

REGISTERED SUPPORT / OPPOSITION:

Support

California Civil Rights Coalition
California Federation of Teachers
California State Student Association
California Student Aid Commission
Consumer Federation of California
Consumers Union
The Education Trust - West
The Institute for College Access & Success
Public Advocates Inc.
University of San Diego School of Law's Center for Public Interest Law
University of San Diego School of Law's Children's Advocacy Institute

Opposition

American Career College/West Coast University
California Association of Private Postsecondary Schools
Carrington College California
DeVry University
Kaplan, Inc.
The California Coalition of Accredited Career Schools
University of Phoenix

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