

## **LOWERING STUDENT LOAN DEFAULT RATES:**

What One Consortium of Historically Black Institutions Did to Succeed

By Erin Dillon and Robin V. Smiles



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# Colleges across the nation are struggling to confront a growing problem in higher education: student debt. As more students borrow more money than ever before, and recent graduates enter the worst job market in a generation, students are increasingly unable to pay back their loans.

At a recent conference in Austin, TX, financial aid officers representing a wide variety of institutions shared secrets to combating this problem. Some of the tactics were unorthodox: perfumed envelopes, colored Easter bunnies and Valentine's Day hearts, brightly colored paper with the words "CHECK INSIDE" stamped on the outside. But they worked—helping colleges successfully reach out to delinquent student borrowers.

For some of the conference participants, the discussions had a familiar ring. Just over 10 years ago, a small group of historically black colleges and universities (HBCUs) in Texas confronted a similar crisis, one in which student loan defaults threatened the existence of the institutions. The steps they took to solve that problem have suddenly become relevant to a much broader set of colleges and universities today.

The problem, then and now, starts with a number called the "cohort default rate," which is calculated annually by the U.S. Department of Education for every college and university in the country that participates in the federal student aid program. The rate is the percentage of student borrowers who default (defined by the department as not making loan payments for 270 days) within two years of leaving school.<sup>1</sup> The federal government uses the cohort default rate to sanction colleges where too many students don't pay back their loans. Any college with a rate higher than 25 percent for three consecutive years or above 40 percent in any one year risks losing eligibility for federal student aid. Without access to federal grant and loan funds to help students pay tuition, a school's very survival is at risk.

The average default rate has hovered around 5 percent since 2001, leaving most colleges far below the danger zone. But a number of things have happened in recent years to put substantially more colleges at risk. Rising college costs have forced students to borrow increasingly large amounts of money, sums that are more difficult to pay back. The latest cohort default rates, which track students who left school in 2007, showed the largest increase since 1989, with 6.7 percent of students

defaulting on their federal loans.<sup>2</sup> The classes of 2008 and 2009 face bleak job prospects, putting more students at risk of defaulting and suffering its consequences—ruined credit and mounting debt from accumulated collection fees and unpaid interest.

At the same time, Congress has raised the bar for institutions. 2008 saw the reauthorization of the massive federal Higher Education Opportunity Act (HEOA). Provisions in that legislation mandate that, starting in 2014, colleges will be held accountable for the percentage of students who default within the first *three* years of leaving school instead of just two years. A recent Department of Education analysis found that 2007 cohort default rates jumped from 6.7 percent over two years to 11.8 percent over three years, a 76 percent increase.<sup>3</sup> And despite the fact that the legislation increased the default threshold from 25 percent to 30 percent, the extended time frame will put many more schools at risk of facing sanctions. In 2009, only two schools faced sanctions under the existing two-year calculation.<sup>4</sup> But under the proposed three-year calculation, over 50 schools would be at risk.<sup>5</sup>

Most at risk are those schools that serve large numbers of first-generation and low-income students. These populations, which are at a higher risk of dropping out and are less likely to have family resources to rely on, are more likely to default.<sup>6</sup> As such, those schools that serve them will find it harder to keep their cohort default rates below the federally mandated cut-offs, rendering them at greater risk of crossing the default rate threshold and losing eligibility for financial aid. Among for-profit institutions, for instance, default rates nearly doubled, growing from 11 percent to 21.2 percent. HBCUs as a whole saw a 60 percent increase, from an 11.6 percent average default rate to an 18.5 percent default rate, with 10 institutions having default rates above 30 percent and several more coming close.

But the experience of the Texas HBCUs, along with a new statistical analysis of cohort default rates, suggests that dangerously high default rates for institutions that serve at-risk students are not inevitable. From the initial financial

aid package to providing individual counseling on loan repayment when students leave, institutions can take steps to help students avoid default. Schools can also maintain contact with students after they leave campus, communicating with them about when they need to begin repayment and where they should send their repayment checks. And for some schools, personal tactics like perfumed envelopes and holiday-themed mailings are especially effective in keeping students out of default.

Such “default aversion” strategies helped a number of HBCUs significantly lower their loan default rates and avoid losing eligibility for federal financial aid the last time the federal government imposed tough new default rate standards. Their story is one of teamwork, collaboration, and relationship-building and proves that when institutions are armed with the tools, resources, support, and commitment needed to lower default rates, they can do so successfully. With the recent HEOA amendment and a worsening economic outlook, all colleges can learn from the efforts of these schools. Their success is not only applicable to other similar institutions, but to all schools that serve those students most at risk for default and who are committed to helping them succeed.

Default aversion strategies, moreover, are just one part of the solution. Institutions that make increasing graduation rates a priority will also help their students repay their student loans. Put simply, students who graduate are less likely to default.<sup>7</sup> As institutions face the next default rate challenge, those that combine default aversion strategies with strategies for degree completion will be in the best position to not only reduce their default rates now and in the future, but to improve the overall success of their institutions and their students.

## THE STORY

The default rate sanctions were established in 1990 to crack down on fraudulent, fly-by-night schools that left students with no legitimate degree and a lot of debt. At that time, student loan defaults were a much more widespread problem than they are today. In 1990, the cohort default rate hit an all-time high of 22.4 percent.<sup>8</sup> Despite earlier efforts by the U.S. Department of Education to encourage, and sometimes force, repayment through wage garnishment, negative credit reports, and increased efforts to contact borrowers, default rates remained high. In a

time of growing budget deficits, the high default rates were costing taxpayers more than \$3 billion a year, increasing pressure on Congress to clamp down on loan defaults.<sup>9</sup> In response, Congress began sanctioning schools—and not just students—for student loan defaults. In the years following the enforcement of the default rate thresholds, more than 1,000 schools have been denied participation in the federal student aid program and default rates have dropped precipitously. (See sidebar “Cohort Default Rates” for explanation of calculations and sanctions process.)

When the default rules were first put into place, many HBCUs had default rates above the legislated cut-offs. Recognized as playing a unique and valuable role in higher education, these schools were at first exempted from the default rate cut-offs and allowed to continue participating in the federal loan program. (See sidebar “About HBCUs.”) But this exemption ended with the 1998 Higher Education Act reauthorization, and HBCUs with default rates above the cut-off were given until 2004 to lower them. Those institutions unable to do so would be at risk of losing eligibility to participate in the federal loan program.<sup>10</sup> In 1999, 14 historically black institutions were at risk of losing eligibility. By 2002, 12 of these schools had successfully lowered their default rates below the threshold through default management plans that included improving student retention and graduation, better loan counseling, partnerships with outside financial aid experts, and improved financial aid packaging.<sup>11</sup>

### *In Texas: ‘We’re Not Going Down Like This’*

Seven of the 14 colleges identified as having high default rates in 1999 were located in Texas—Texas Southern University, Huston-Tillotson College, Jarvis Christian College, Paul Quinn College, Southwestern Christian College, Texas College, and Wiley College. With the exception of Texas Southern, one of the nation’s largest HBCUs and a public university, these schools are all private four-year colleges and represent some of the smallest and least wealthy among their peers. Enrollments average around 600 students, and the average endowment per student is \$8,600, well below the median endowment of \$16,000 per student among private four-year institutions.<sup>12</sup>

For such schools, losing federal student aid money would be disastrous, likely forcing them to shut their doors. The mission of these institutions is to serve first-generation, low-

## COHORT DEFAULT RATES

The two-year cohort default rate is the percentage of a school's borrowers who enter repayment on a federal Stafford student loan in one fiscal year and who default in that fiscal year or the next. The 2007 two-year cohort default rate, for example, calculated the percentage of borrowers at a school who entered repayment between October 1, 2006, and September 30, 2007, and who subsequently defaulted on or before September 30, 2008.

The three-year cohort default rate calculation tracks the number of students who default for an additional year, but does not change the denominator—the number of students entering repayment. The three-year 2007 cohort default rate, for example, calculates the percentage of borrowers who enter repayment between October 1, 2006, and September 30, 2007, and who default on or before September 30, 2009. Because the numerator in this equation will almost certainly go up—tracking students for an additional year will catch more defaulters—the three-year calculation will result in higher default rates for nearly every institution.

Schools, however, won't face sanctions for the new three-year default rate calculation until 2014, at which time the threshold for sanctions will also increase. Currently, a school loses eligibility for federal financial aid if it has a two-year cohort default rate above 25 percent for three consecutive years or above 40 percent in any one year. In addition, there are benefits to schools with two-year default rates below 10 percent. These schools are allowed to deliver loan funds in one payment and can disburse funds immediately to first-year undergraduate students. When sanctions for the three-year calculations take effect in 2014, schools will risk losing federal student aid for having default rates above 30 percent over three years, or 40 percent in one year, and will receive benefits for having default rates below 15 percent.

In the spring before official cohort default rates are released, the U.S. Department of Education notifies each school of its draft cohort default rate. Schools have the opportunity within 45 days of the release of the draft rates to challenge the accuracy of the default rate data under an "incorrect data challenge." The success rate on incorrect data challenges typically exceeds 40 percent.\* Schools with a low percentage of borrowers can also file a "participation rate index challenge" to avoid sanctions. The participation rate index is calculated by multiplying the school's cohort default rate by the total number of borrowers over a 12-month period divided by the total number of students enrolled over that 12-month period. Schools with a cohort default rate of 25 percent or more over three years can qualify for the participation rate index exemption by having a participation rate index of .0375 or less in any of the three years. Schools with a cohort default rate of 40 percent or more must have a participation rate index of .06015 or less to qualify for the exemption.

If schools still face sanctions after exhausting their challenges, there are still data adjustment and appeal options available:

**Uncorrected Data Adjustment, New Data Adjustment, or Erroneous Data Appeal:** Schools can appeal official cohort default rates based on incorrect or new data. If data was not corrected after a successful incorrect data challenge to the draft default rates, schools can submit an "uncorrected data adjustment" to correct the default rate data.

**Loan Servicing Appeal:** Schools can file a "loan servicing appeal," which alleges that a defaulted loan was not properly serviced by the borrower's lender or, under the Direct Loan program, by the loan servicer. Improper servicing appeals are successful if the school can provide evidence that a borrower never made a payment and the lender or servicer failed to take action in contacting the borrower, including failing to send at least one letter urging the borrower to make payments or failing to attempt at least one phone call to the borrower.

**Economically Disadvantaged Appeal:** Schools can file an "economically disadvantaged appeal" if they enroll a high number of low-income students and can prove high graduation or job placement rates. Degree-granting schools must submit an independent auditor's written opinion that the school's low-income rate is two-thirds or more and that the school's completion rate is 70 percent or more. Non-degree granting schools must submit a written opinion that the low-income rate is two-thirds or more and the job placement rate is 44 percent or more.

**Average Rates Appeal:** For schools with fewer than 30 borrowers in any one year, cohort default rates are calculated as an average of the prior three years. This avoids large fluctuations from year to year because of small cohorts. Under an "average rates appeal," a school with default rates greater than 25 percent over three years can avoid sanctions if at least two of those years were averaged default rates, but would have been less than 25 percent had the rate not been averaged. A school with a default rate above 40 percent in any one year will not face sanctions if the cohort default rate was an averaged rate, regardless of what the rate would have been without averaging.

**Participation Rate Index Appeal:** If a school does not file a participation rate index challenge based on draft default rates, the school can file a "participation rate index appeal." If the school meets the requirements described above for the participation rate challenge, it will not be subject to sanctions. A school facing sanctions because of a 25 percent or higher default rate over the prior three years may file a participation rate index appeal for any of the prior three years.

**Thirty-or-Fewer Borrowers Appeal:** If a combined total of 30 or fewer borrowers entered repayment over the prior three years, the school is not subject to sanctions.

For more details on cohort default rates, see the U.S. Department of Education's *Cohort Default Rate Guide*, available at: <http://ifap.ed.gov/DefaultManagement/finalcdrg.html>

\*Note: Mark Walsh, U.S. Department of Education, Special Initiatives Services, in discussion with author, January 2010.

## ABOUT HBCUS

The Higher Education Act defines an HBCU as “any historically black college or university that was established before 1964, whose principal mission was, and is, the education of black Americans...” Today there are more than 100 HBCUs in the country, most of which were founded immediately after the Civil War in order to educate newly freed blacks who were denied access to predominantly white institutions.

Although HBCUs share a historic mission, they are very diverse. They include public and private universities, two-year and four-year schools, single-sex and coeducational institutions, research universities, and small liberal arts colleges. Overall, these schools educate close to 300,000 students. And four-year HBCUs enroll about one out of every five black students attending a four-year institution and grant a similar proportion of all bachelor’s degrees awarded to black students.\*

\*Steven Provasnik and Linda Shafer, *Historically Black Colleges and Universities, 1976 to 2001* (Washington, DC: U.S. Department of Education, National Center for Education Statistics, 2004).

income students—the students who rely most heavily on federal grant and loan funds for college. Among the seven Texas HBCUs that risked losing access to federal student aid funds, 80 percent of the students receive Pell grants (the federal aid money that goes to the lowest-income college students), and 78 percent borrow to pay for their education.<sup>13</sup> Without access to this money, few of the students enrolled in these seven colleges would be able to pay tuition.

Bronte Jones, former assistant dean of financial services at Huston-Tillotson in Austin, remembers being in “crisis mode” in the summer of 1999, just months before the new rules were to go into effect. During a number of meetings held to discuss the issue and bring together administrators from the “at-risk” campuses, it was clear, Jones says, that no one really knew how to get started. Although schools had until 2004 to lower their default rates, the new regulations became effective July 1, 1999, requiring all of the HBCUs with high default rates to submit a “default management plan” to the secretary of education for approval. The department also required schools to hire an independent third-party consultant to help with implementing the plan, as well as provide evidence to the secretary that the rate had improved and that the plan was being successfully implemented.

The department provided assistance to schools in designing and implementing the plans, hosting a meeting at Paul Quinn in February to review the new requirements and outline what was expected. Over the next few months, a number of outside groups stepped in to offer

their assistance as well, sponsoring training sessions on default prevention, technical help, and on-site review of the default management plans.<sup>14</sup> The Department of Education also reached out to Texas Guaranteed, a loan guarantee agency based in Austin with experience working with Texas HBCUs, and asked the company to dedicate resources to addressing the issue. In response, Texas Guaranteed launched a new initiative, “Achieving Systemic Default Aversion,” which included creating a new position, a default aversion consultant, who would travel to the individual schools and work directly with them and make sure they stayed on track. Texas Guaranteed also provided \$15,000 in grant assistance to help the schools pay for the independent third-party consultant.

As the July 1 deadline approached, however, it was clear that some schools were still behind, prompting Jones and others to decide to pool their resources in order to ensure that all the schools would be successful. As a result, six of the schools joined together and formed, with the assistance and leadership of Texas Guaranteed, the Texas Historically Black Colleges and Universities Default Management Consortium.<sup>15</sup> The consortium committed to quarterly meetings and sharing best practices. And the leadership from Texas Guaranteed gave them a partner with expertise in loans and default prevention.

According to Jones, who served as the consortium’s first chairwoman, the team approach is what ensured that all of the schools met the new requirements. “The partnership gave us a lot of power,” she says, pointing to the process of hiring a third-party consultant as a good example of how collaborating made a difference. Alone, she suggests, the schools would not have been taken seriously by the vendors, but by interviewing the candidates together, they were able to find a vendor that met all of their needs, including professional development for financial aid staff, new technology, and an understanding of the unique mission and nature of their institutions. “You have to understand our campuses. Our staff was not well-trained or savvy in the area of default management,” she explains. “To not have partnered would have meant failure.”

Failure would have not only been disastrous for the individual schools affected, but it would have had a broader impact on their peer institutions across the nation, says Jones, who left Huston-Tillotson in 2006 to become treasurer at St. John’s College in Annapolis, Md. “There is a sentiment in the HBCU community that others feel they are no longer relevant; that some want to do away

with HBCUs.” In response to this sentiment, the tagline of the group became “We’re not going down like this.” This determination coupled with the teamwork, collaboration, and partnership worked. Sharing best practices and tweaking them to fit their individual campuses, each school reduced its default rate in the first year. The success of the Texas consortium approach is apparent when default rates for these six institutions are compared with the six HBCUs that did not participate in the consortium.<sup>16</sup> While both groups of colleges successfully lowered their default rates, the six consortium schools did so faster and more dramatically. (See Figure 1)

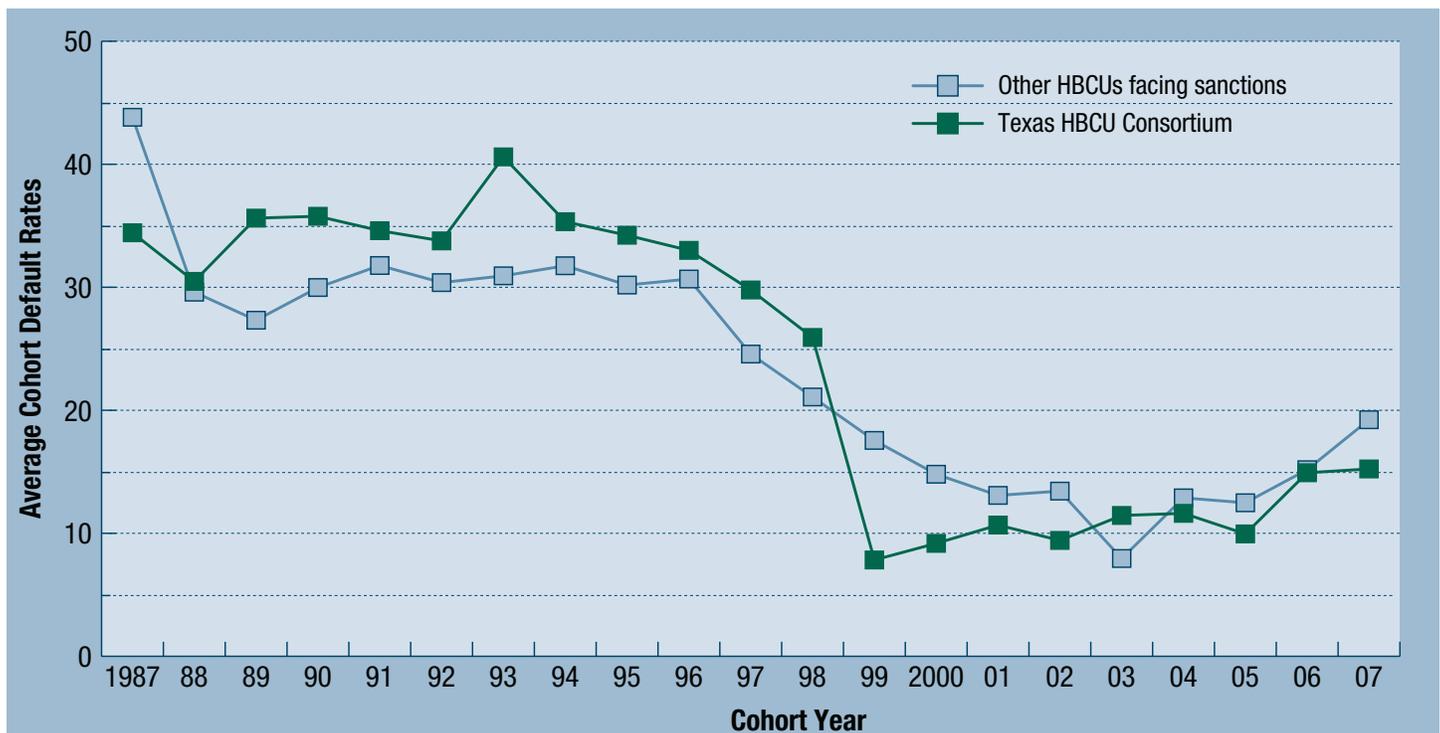
## DEFAULT AVERSION 101

Much of what worked for the Texas consortium schools appears to be default aversion 101. Before the new regulations, the consortium schools were doing minimal default aversion work, says Shelia Dunlap, assistant vice president for default prevention at Texas Guaranteed, who helped lead the effort. “Once the schools started doing the things they were required to do, they found success,” she says.

## A Campuswide Concern

One of the first steps toward that success was to create institutional buy-in and support, endorsed by the president and top leadership. Successful default management required the interest and commitment of those not traditionally concerned with financial aid issues. Yet, it was a challenge, Dunlap says, “to get the administration and faculty to see that it was not just the responsibility of the financial aid office.” The initial lack of institutional support was due to a lack of understanding of the issue, Dunlap says. But once the leadership understood the consequences of inaction both to the students and to the institution, “they were on board, making everyone reliable and accountable.” At one school, Dunlap recalls, the president brought in the entire faculty and staff on a holiday to discuss default management and ensured they had a plan by the end of the day. Dwight Fennell, now president of Texas College, was provost at Paul Quinn College in the late 1990s, when the school was faced with bringing down its default rate. He remembers it as a “top-down driven assignment,” where default prevention efforts were “internal to the institution’s organization,” meaning they were the responsibility of the entire institution, not just confined to one office.

Figure 1. Average Cohort Default Rates Among HBCUs Facing Sanctions, 1987–2007



Source: U.S. Department of Education Office of Federal Student Aid, Debt Prevention and Management.

To ensure that default management was a campuswide concern, school officials created a default management team. Teams brought together administrators and staff from all aspects of the school, i.e., from admissions to alumni affairs. As such, default prevention efforts covered as much of a student's on-campus interactions as possible. The team approach was particularly effective in helping schools deal with students who "stopped out," meaning they left school for a semester or more to work or deal with family obligations but intended to return, and also with students who dropped out entirely. These students are much more likely to default. According to the Department of Education, 70 percent of the defaults in the department's loan program come from students who dropped out.<sup>17</sup> And research has shown that whether a student earns a degree is one of the most important predictors of whether that student will eventually default.<sup>18</sup>

By involving a variety of campus departments, officials at the Texas consortium colleges could intervene before a student made the decision to leave. Academic affairs staff, for instance, would alert the financial aid office when a student's grades dropped significantly, a sign that a student might be about to drop out. And faculty members were prepared to alert both academic affairs and the financial aid office when a student stopped showing up to class, another sign of impending drop out. Finally, the registrar's office would signal a warning when a student failed to enroll or withdrew from classes. (See sidebar "The Default Management Team.")

Once students left campus—whether they dropped out, transferred, or graduated—they were more difficult to keep track of, making it harder for financial aid staff to locate students and inform them of their repayment obligations. Again, the team approach was effective for the consortium schools. The registrar's office would issue a hold on students' transcripts, forcing students to contact the financial aid office before their transcripts could be released. And since alumni affairs staff made it a priority to keep track of students after they graduated, they were often in a position to help default prevention managers locate hard-to-find students.

### ***Default Management 'Superstars'***

Schools created a default management team, pulling together administrators from all across campus to

tackle the issue. Another important first step for the consortium schools was to appoint a default prevention manager, a sole person responsible for coordinating team efforts and executing a school's approved default management plan. A 1998 General Accounting Office study on student loan defaults at HBCUs found that creating a "default rate manager position or retain[ing] a consultant to track and contact delinquent borrowers" was commonly cited as a default reduction measure by administrators at HBCUs that formerly had high default rates.<sup>20</sup>

Many of the Texas consortium schools brought in an additional staff person to serve in this role, either by reallocating resources within institutions' operating budgets or by using federal funding provided through HEOA's Title III, which supports HBCUs and other minority-serving institutions. Jones, Fennell, and others emphasized the need for the default manager to be a full-time position, someone with a considerable amount of his or her time dedicated to the role's many tasks. They were the ones who served as a liaison between the financial aid office and other on-campus departments; worked closely with third-party consultants, guarantors, and lenders to keep track of students who were near default; analyzed data to create profiles of students most likely to default and to identify early warning signs of students at risk of dropping out or defaulting; raised awareness among students, faculty, and staff of the default problem; and developed programs to educate borrowers about loans and improve financial literacy.

Given the importance of the default rate problem at the time, default managers became, according to Jones, "superstars overnight" on many of the campuses. And successful default prevention managers worked to develop a personal relationship with the students, showing interest in and concern about students' futures and how the consequences of defaulting on student loans can hinder their future options. "Mentoring and close relationships are key," says Eric King, who worked in the financial aid office at Jarvis Christian College during what he calls the "big panic." "If you're not willing to have those, then the default rate will go through the roof." King, who is now director of financial aid at Wiley College, says he treats the students "like they are my own kids." Similarly, Fennell likened the internal default manager to a "surrogate parent." It is no surprise then to see highly personal tactics on the Texas consortium's list of "25 Best Practices." Among the most personal are sending

student borrowers birthday cards, calling them during special holidays, and planning default prevention visits in conjunction with special events (e.g., social gatherings and athletic events).<sup>21</sup>

The small, intimate nature of the seven HBCUs in the Texas consortium made this kind of personal contact a natural extension of the institutions’ familial atmosphere and frequent interactions between faculty and staff and students.<sup>22</sup> But personal contact does not need to be limited to small colleges. Research has shown that fostering high student engagement and encouraging frequent interactions between faculty and students are two successful strategies for improving student academic performance and retention, both of which ultimately lead to lower loan default rates.<sup>23</sup>

## Outside Partnerships

Partnerships with outside entities—all with experience in skip tracing, the process of finding and successfully contacting borrowers, collections, and personalized customer service—proved as important to successful default management as on-campus relationships. Working closely with independent third-party consultants, lenders, and guarantee agencies allowed the consortium schools to increase their capacity to locate, keep track of, and communicate with former students. The third-party consultant that worked with the consortium schools was “actively involved,” says Jones. “They came to our campuses, uploaded software, trained our staff, and worked closely with them. They were concerned about us getting out of this.”

DEFAULT MANAGEMENT TEAM		
The chart below is taken from the “Breaking New Ground” report published by the Texas HBCU Default Management Consortium. The chart outlines the departments that should be represented on an institution’s default management team, their contribution to the team, and what the campus gains from their participation. By including personnel from each of these areas, the default management team can be most effective in implementing a default management plan.		
Office	Contribution	Knowledge gained
Academic Affairs	Informing team of academic standards and student progress	Educating faculty members on their role in default aversion
Student Affairs	Voicing the concerns and suggestions of the student body and campus areas designed specifically to meet the needs of the students	Creating an environment to support the efforts of default aversion
Fiscal Affairs	Providing budgetary information including endowment and institutional funds, student costs and administering Title III funds	Incorporating current default trends to assist in making adjustments within the budget
Alumni Affairs	Updating the team on changes in demographic and employment statuses of graduates	Communicating successful repayment and default aversion measures for former students
Financial Aid	Education of college community on the packaging philosophy and promoting gift aid	Utilizing information in revising and updating office procedures and packaging philosophy
Career Planning/ Placement	Informing the team of expected salaries of the graduates based on fields of study and their placement success rates	Providing an outlet to disseminate unemployment and economic hardship deferment options
Institutional Research	Analyzing data to assist in identifying potential defaulters	Incorporating new variables into current research and statistical models
Registrar	Reporting of enrollment status, withdrawals, course load adjustments, and classification	Developing a new understanding of how they play a major role in proactive default measures and tactics to increase retention and student success
Admission	Reporting of special academic needs based on transcript evaluation	Enhancing recruiting techniques to identify high-risk defaulters
Administration	Allocating funds for the support of default aversion measures and providing atmosphere for campus commitment	Promoting a campuswide approach to proactive default aversion

Source: Breaking New Ground: The Texas Historically Black Colleges and Universities Default Management Consortium, (Round Rock, TX: Texas Guaranteed, 2004).

Outside partnerships also helped the consortium schools improve the technology they were using to track students. At the same time that Texas Guaranteed was working with the Texas consortium, another loan company, Sallie Mae, began its HBCU Default Management Project, a yearlong study of the HBCUs that were at risk of losing access to loan funds. The final report from the Sallie Mae study found that, “many of the HBCUs lack the types of technology-driven resources that might help reduce default rates.”<sup>24</sup> In light of this finding, the institutions that participated in the Sallie Mae study, including the consortium colleges, shared a \$275,000 grant from Microsoft to upgrade the colleges’ technology and ability to track student borrowers.

With the new investments in technology, institutions were able to get more accurate, real-time information on students’ repayment statuses. As a result, default prevention managers could get students on the phone early, when they first missed payments, and explain options for deferment or forbearance that could keep students out of default. In some cases, schools moved to track students who were in loan repayment as often as daily or weekly. Texas Guaranteed’s Integrated Default Assistant (IDA) system, for instance, allows schools to access customized reports on which students are behind on payments and find out the institution’s projected three-year cohort default rate on Texas Guaranteed loans. Institutions can also target their default prevention activities to students most at risk by generating reports of students based on whether they graduated or their academic standing when they were last enrolled. This type of targeted outreach can be effective in reducing loan defaults. A 2004 study published in the *NASFAA Journal of Student Financial Aid* found, for example, that the Advocate Unit, a program that contacted borrowers during their six-month grace period and targeted those students at the highest risk of falling behind on loan payments, was effective in reducing defaults. According to the study, the simple task of contacting borrowers and informing them of their repayment responsibilities and options was enough to reduce the default rate among this high-risk population.<sup>25</sup>

Moreover, by tracking which students default and coordinating databases from across the campus, default managers and financial aid offices were able to understand which students were most likely to default, which, according to Jones, “made a difference in decisions about financial aid packages, advising students,

## CONSEQUENCES OF DEFAULTING ON STUDENT LOANS

Defaulting on student loans has serious consequences for the borrower. “The U.S. Department of Education is responsible for recovering those funds for the taxpayers, and we have a variety of tools to use in accomplishing that,” says Mark Walsh, who recently moved from the department’s Default Prevention office to the Special Initiatives team. Walsh lists wage garnishment, federal and state tax refund seizure, and seizure of any federal payment among those tools. He also says that borrowers may be sued in Federal District Court, and students who default lose eligibility for additional federal education funding.

Defaulting also affects a student’s future job prospects and quality of life. In some states, Walsh says, defaulting may prohibit a borrower’s occupational license from being issued or renewed. And since defaulted loans are reported to credit bureaus, borrowers sustain long-term damage to their credit rating. Damaged credit ratings, in turn, make it difficult to get a mortgage or rent a house, or even to purchase a car. Borrowers with poor credit are also subject to paying higher interest rates on many forms of credit.

For more information, visit the department’s Web site “Facing Loan Default,” <http://www.ed.gov/offices/OSFAP/DCS/default.html>.

and tutoring students.” Financial aid offices could then direct grant and work study aid to those students least able to manage debt, particularly in their first years in college, and the academic and student affairs offices could target academic and social support services to those students most likely to drop out. Coordinating data across campus also improved financial aid offices’ ability to maintain up-to-date contact information and keep track of students’ academic progress.

## Packaging Philosophy

Knowing which students were likely to default was an important step, empowering schools to make changes early in the student loan process. Miles College, a private HBCU in Fairfield, Ala., was also on the list of schools at risk of losing federal financing in 1998. And like the Texas consortium schools, Miles brought its default rate down significantly, and it has kept its rate below the federal threshold ever since. Diana Knighton, chief fiscal officer for Miles College, helped implement the school’s default management plan and remembers that a big component of the school’s success was changing the way financial aid officers “packaged” students, the process of deciding how much aid students receive and how that aid will be divided among loans, grants, and/or work-study. “We were like many schools,” Knighton says,

“out of control with our packaging ... meeting students with more than their direct costs.” Miles moved quickly to change its packaging philosophy to minimize borrowing, so that students were only given loans that amount to a small percentage above their direct costs, which included allowances for things like basic transportation and books.

This philosophy is still in place at Miles, says Knighton, and remains key to the school’s ability to manage its default rate. But it has gotten harder for schools like Miles to keep students from taking on too much debt. Limits on federal loans have recently increased in an effort to keep pace with rising college costs, allowing undergraduate students to accumulate \$31,000 in federal loans by graduation. And private student loans, which are not guaranteed by the federal government and have none of the safeguards of federal loans, grew steadily through 2008—offering students ever-easier access to student loan debt.<sup>26</sup> These higher debt levels make it more difficult for students to keep up with payments after graduation and can increase the likelihood of default. In a 10-year follow-up study of students who graduated from college, the Department of Education found that default rates steadily increased with debt levels—20 percent of students with the highest debt levels defaulted within 10 years, compared with 7 percent of students with the lowest debt levels.<sup>27</sup> The growing availability of debt also makes it more difficult for financial aid officers to ensure students aren’t borrowing too much. Colleges don’t always know when students have taken out private loans, and aid officers may even need to counsel students away from taking on the maximum federal loan amount.

Cecilia Jones, financial aid director at Texas College, says they only include in an aid package the amount of loans absolutely necessary for a student to attend. But students might be eligible for additional federal loans beyond that amount, which the financial aid office must give them if they request it. When students request additional loan money, Jones says that gives the financial aid office the opportunity to counsel students about the consequences of taking on more debt. They also reach out to parents and educate them on the consequences of students taking on too much debt in college, hopefully gaining an ally in the effort to keep students out of excessive debt. At Wiley College, King is implementing a similar strategy. When students request more loan money than they need, King sits down with them and shows them how the additional debt will translate into higher monthly payments

after graduation, and how much more they’ll need to earn to make those payments.

“One of the worst things an institution can do,” Fennell says, “is to package to the point where the student, when they graduate, can’t get a job to meet their repayment obligations.” Fennell points to students who live off campus, but don’t really need to, and who often become saddled with high housing and transportation costs. “They find themselves as working adults with debt, so that effort becomes full-time and the education becomes part time.”

## *Enrollment and Retention*

Educating themselves on which students were likely to default also forced schools to look more closely at the students they were enrolling. Looking back to the changes some HBCUs made in 1998, Bronte Jones noted that schools faced pressure to keep enrollment numbers up and sometimes would “enroll high-risk students.” This led to many students dropping out and failing to repay their loans. While some schools tightened admissions standards, most schools just became more realistic about the deficiencies among their students. “It was a wake-up call,” says Jones. “Schools revisited their satisfactory academic progress policies and got more serious about support services—they looked at who they were bringing in and what they needed to be successful.”

As a result, schools recognized that retention efforts worked in concert with default prevention. In describing the default prevention efforts at Miles College, which has maintained an open-enrollment policy, Knighton highlighted the school’s tutorial and remedial labs, where students can get additional help in math, reading, and English. Even in the collections phase, Knighton says, the focus is on getting students back into school. Miles financial aid staff advises students against dropping out, but if they do find that Miles is not a good fit, they encourage students to complete the semester and then transfer to another institution. In so doing, students will at least earn credits for the semester and avoid wasting loan money on incomplete courses.

This philosophy mirrors recommendations from the U.S. Department of Education. Mark Walsh, who recently moved from the department’s Default Prevention office to the Special Initiatives team, which works specifically with minority-serving institutions, recommends that schools

“aggressively reach out to students who withdraw to try and help them overcome obstacles to continuing their education.” Says Walsh: “Many borrowers have the misconception that by leaving school they are somehow relieved of their loan responsibilities. Once they learn they must still repay a loan, some elect to come back.” He also points out that students who abruptly withdraw from school not only lack a degree, but also miss out on loan exit counseling and job placement assistance, putting them at an even higher risk of default.

Under Fennell’s leadership, Texas College hired a retention coordinator to improve graduation rates. The retention coordinator, akin to the default prevention manager, is responsible for aligning retention efforts across campus. Both positions are under the “enrollment services” umbrella, with the retention coordinator working closely with faculty to ensure they report student absences and academic problems. These early warning signs are critical to the college’s early alert system, intended to catch students before they leave campus and provide them with the support they need to stay.

Early alert systems have the added benefit of ensuring that students who do drop out get repayment notifications about their loans during the full six-month grace period. According to the Department of Education, 91 percent of borrowers who defaulted did not receive their full grace period because of late or inaccurate notification by the school.<sup>19</sup> During the grace period, loan servicers, the companies that process students’ loan payments, establish contact with borrowers and notify them of their repayment options—those six months are an important time for students to learn of their repayment obligations and for servicers to determine if there is a problem contacting a borrower. Institutions that keep close tabs on students—by taking attendance at classes, monitoring grades, and communicating across campus—are in a better position to know as soon as a student has stopped attending and can notify the lender promptly, allowing the student to receive his or her full six months of services.

Student retention was an important focus of default prevention in 1998. The Texas consortium’s recommended strategies for lowering default rates included improving “academic persistence and retention” as a key strategy.<sup>28</sup> But institutions also used many other strategies, such as improved communication with students and better tracking of borrowers, to target the “low hanging fruit,” including students who didn’t know their loans needed to be repaid,

who lost communication with their school, or who needed a deferment because of unemployment. It appears that these other strategies, and not a focus on retention, explain most of the institutions’ success in lowering default rates. The data available from 1999 forward do not indicate dramatic increases in graduation rates among this group of HBCUs.<sup>29</sup> As institutions face the next default rate challenge, though, the low-hanging fruit has already been picked, and improving graduation rates holds the biggest potential for reducing default rates in the future.

## *Financial Literacy*

In many ways, the default prevention process for these schools and its success came down to the schools doing what they are charged to do—educate their students. “There was a heightened need to make sure students understood the consequences of not taking this seriously,” says Bronte Jones. “We served a lot of first-generation college students who only heard about loans and debt in negative terms, so we did things to help them understand debt. There’s debt when you buy that new car so you can be cute on campus, and there is student loan debt that is leading you somewhere. Colleges need to help students understand financial decisions and the implications of financial decisions,” says Jones. One of the things the consortium did was to produce their own student loan guide, with fellow students, Jones, and others talking about their positive experiences with student loan debt.

Overall the Texas consortium schools worked to do a better job of educating students about the pros and cons of borrowing. They instituted financial literacy courses and hosted financial aid awareness fairs. Some schools also required loan counseling as often as each semester or quarter, which is much more frequent than the federally mandated “entrance” counseling when students first take out a loan and “exit” counseling when students leave school. In-person entrance and exit counseling was also identified as a valuable strategy. Many of the HBCUs, rather than have students watch a presentation on the computer or in a large lecture room when they take out loans and prepare to leave college, sit down with students one-on-one to discuss their repayment schedule, the consequences of default, and the options students have if they’re struggling with payments. These sessions build students’ awareness of their debt and also reinforce that the financial aid office is a resource they can turn to if they

run into trouble. A study conducted in 1987 of borrowers at California community colleges and proprietary schools highlights the importance of good information, finding that some financial aid practices, including providing financial aid services on site, informing applicants of total costs, providing applicants with repayment information, and

informing applicants of the consequences of default, were significantly associated with lower default rates.<sup>30</sup>

Counseling sessions also give financial aid officers a chance to make sure students understand the difference between grant aid, which does not need to be repaid, and

## INSTITUTIONS' BEST PRACTICES

Students who graduate are less likely to default; thus, emphasizing retention and student success tops any list of best practices in default prevention and management. Yet, there are specific strategies that institutions can take to help prevent and lower their default rates and ultimately help their students avoid the consequences of loan default.

### **Create and Implement a Default Management Plan**

The U.S. Department of Education recommends that all schools implement a default prevention and management plan and provides a sample one on its Web site, available at <http://www.ifap.ed.gov/dpcletters/attachments/GEN0514Attach.pdf>. Those HBCUs identified as having high default rates in 1999 were required to submit a plan to the secretary of education for approval in order to maintain Title IV eligibility.

### **Create a Default Management Team**

Successful default management requires the interest and commitment of those not traditionally concerned with the issue. To make sure default management was a campuswide concern, school officials brought together staffers from a variety of departments; thus creating a team to tackle the problem.

### **Institute Early Alert Systems**

According to the U.S. Department of Education, 70 percent of the defaults in the department's loan program come from students who dropped out. Identifying students who might drop out as early as possible (for example when they withdraw from several classes, or accumulate a high number of absences) can go a long way toward preventing loan default. Early alert systems also help schools target their outreach to students most at risk of defaulting.

### **Appoint a Default Prevention Manager**

An important first step for the Texas consortium schools was to appoint a default prevention manager, a sole person responsible for coordinating team efforts and executing the school's default management plan. These individuals worked closely with third-party consultants, guarantors, and lenders to keep track of students who were near default and led efforts to communicate with students both on and off campus.

### **Encourage Personal Contact With Students**

On the Texas consortium schools' small campuses, personal contact was inherent in each school's culture. But default prevention managers and other financial aid staffers still made it a priority to have direct contact with students, for instance, conducting in-person entrance and exit loan counseling even when online versions were available.

### **Establish Partnerships With Outside Entities**

Working closely with independent third-party consultants, lenders, and guarantee agencies allowed the consortium schools to increase their capacity to locate, keep track of, and communicate with former students. These companies provided experience and expertise in skip tracing, the process of finding and successfully contacting borrowers, collections, and customer service.

### **Improve Technology**

Better technology helped schools improve their ability to track student borrowers. In some cases, it helped them track students more frequently—as often as weekly or daily. Schools were also able to get real-time information on a student's repayment status. As a result, default prevention managers could move quickly to contact students when they first missed payments and explain their repayment options.

### **Avoid Giving Students More Than Their Direct Costs**

Schools took a closer look at the way their financial aid officers packaged students, the process of deciding how much aid students receive and how that aid will be divided among loans, grants, and/or work-study. Schools then moved to make sure they only included in an aid package the amount of loans absolutely necessary for a student to attend their school.

### **Educate Students About Debt and Its Consequences**

Schools worked to educate students about the pros and cons of borrowing, instituted financial literacy courses, hosted financial aid awareness fairs, and mandated entrance and exit counseling each semester or quarter. The personal counseling sessions were particularly effective, building students' awareness of their debt and also reinforcing that the financial aid office is a resource they can turn to if they run into trouble.

loans, and also help students understand the process of repaying their loans, including where to send repayment checks. The multitude of grant and loan programs can easily be confusing, particularly for students who are the first in their family to attend college, and this confusion can lead to students defaulting on their loans. A 1998 analysis of a national survey of students who defaulted on their loans found, for example, that nearly one in four students reported being confused by the repayment process.<sup>31</sup> Another study, which interviewed students who defaulted on their loans, found that these students were less knowledgeable about their loan options and reported that their loan counseling was unclear.<sup>32</sup>

“Financial literacy is important. You can never do enough,” says King at Wiley College. Educating students about finances starts when a student arrives on campus, he says. “We cascade information ... just keep giving information and sitting down and talking to students.” But King also says that they often need to correct misinformation that students have received. For example, “students think Pell grants will cover tuition,” he says. High schools, he suggests, need to “create an awareness of loans and the reality of needing loans to finance college.”

## INSTITUTIONS MATTER

The experiences of the 12 HBCUs we studied and the success of the strategies they used to lower default rates offers powerful evidence that institutional practice can make a difference in determining a school’s default rate, even for schools that enroll high percentages of low-income and first-generation students. And it disputes two arguments often used by colleges, particularly for-profit institutions, to lobby against the default rate measure: (1) the cohort default rate is primarily a reflection of the demographics of students enrolled and *not* institutional practice, and (2) the rate unfairly punishes schools that enroll high numbers of low-income students.

For-profit higher education institutions, while different from HBCUs in mission and programs, have also struggled with high cohort default rates, and the Career College Association, which lobbies on behalf of for-profit colleges, is one of the most vocal opponents to sanctions based on default rates. In lobbying against the 2008 HEOA amendment, for example, CCA President Harris Miller stated, “We object to the singling out of schools that take on the risk

and accept lower-income students, and saying the failure of those students to pay is an indicator of institutional quality.”<sup>33</sup>

To bolster its argument, the CCA commissioned a review of existing research on causes of default rates, conducted by the Project on Academic Success at Indiana University. The report was critical of sanctions based on default rates and concluded the “default rate is not a good vehicle for assessing the quality of institutions.”<sup>34</sup> But the research reviewed in the report suffers from two critical shortcomings that limit its ability to evaluate federal policy. First, the research considers whether or not a student graduates to be solely a “student” characteristic. Graduation is consistently one of the strongest predictors of whether a student defaults; therefore, it is not surprising that this same research concludes that student characteristics are far more powerful than institutional characteristics in predicting loan default. But research on graduation rates clearly illustrates that institutional practices and programs can moderate, and in some cases overpower, the role of income, race, or prior education in determining students’ outcomes.<sup>35</sup> By categorizing graduation as only a student characteristic, the existing research overstates the influence of student background on a student’s likelihood to default.<sup>36</sup>

Second, along with categorizing graduation as solely a student characteristic, much of the existing research on causes of loan defaults uses data on the likelihood of an *individual* student to default in order to evaluate the appropriateness of federal policy.<sup>37</sup> Using the research in this way assumes that federal policy sanctions institutions for *each* student who defaults. But that is not an accurate reflection of federal policy. The policy actually holds schools responsible for an *entire cohort of students*, and assumes that extremely high default rates—not each individual default—are a reflection of the institution’s quality: That a school where one in four students defaults almost immediately after leaving school over three consecutive years or where nearly half of students default in any one year is not providing an education worth the cost that students—and taxpayers—are paying.

In contrast with the existing research that examines the likelihood of an individual student to default, we evaluated the actual cohort default rate (CDR) data that is used to determine sanctions under federal policy. We examined the 2007 CDR data for 1,778 four-year institutions and 1,336 two-year institutions to determine how much of a school’s default rate could be explained by the

characteristics of the students it enrolls and how much could be attributed to institutional characteristics.<sup>38</sup>

Consistent with previous research, we found that student demographics are a significant predictor of cohort default rates. But we did not find that they are the *sole* predictor of an institution's CDR or even the primary predictor. Instead, institutional characteristics, or in some cases unmeasured factors, are important to predicting whether an institution has a high or low default rate and potentially whether it runs afoul of federal sanctions.

Among four-year institutions, the combination of student characteristics, institutional success in student retention and graduation, and other institutional characteristics did a good job of predicting which schools will have high or low cohort default rates. Overall, we were able to account for 62 percent of the variation in institutions' default rates. The story was different among two-year institutions, however. We were able to account for only 15 percent of the variation in default rates among public two-year institutions and 21 percent among for-profit two-year institutions. This leaves the vast majority of variation in default rates among two-year institutions unexplained. It also leaves a substantial portion, 38 percent, of the variation among four-year institutions unexplained. While student characteristics and institutional success matter, other unmeasured variables are clearly still important to consider. Some of these unmeasured variables may be student characteristics, such as first-generation status, or local economic conditions, but many are also likely to be institutional, especially given the paucity of good data available to measure institutional quality and practice. Many of the successful practices used by the Texas consortium, for example, are not measured in a federal data set, such as whether a school has a default prevention team or manager.

Despite the role of these unmeasured variables, a few measurable student and institutional characteristics did emerge as significant in predicting default rates. Among student characteristics, a higher percentage of students receiving Pell grants, a measure of low-income student enrollment, significantly predicted higher cohort default rates among all types of institutions we analyzed: public four-year; private not-for-profit four-year; public two-year; and for-profit two-year.

Race was another significant student characteristic in predicting institutions' cohort default rates, but it varied depending on the type of institution, an indication that

race was merely a stand-in for other factors. Among four-year schools, the percentage of African-American students enrolled emerged as one of the strongest predictors of an institution's default rate, with higher enrollment predicting a higher default rate. Among public two-year institutions, though, the percentage of African-American students enrolled was not significant and instead the percentage of Hispanic students enrolled predicted a higher default rate. Once data from the Community College Survey of Student Engagement was included, however, no race variables emerged as significant. (See discussion of CCSSE data in "More Institutional Characteristics" sidebar.) And among for-profit institutions, neither Hispanic nor African-American enrollment was significant. Instead, the percentage of white and Asian students enrolled predicted *lower* default rates. This variation in the influence of race across institutions indicates that race is likely a proxy for other student risk factors that influence institutions' cohort default rates, which would be consistent with prior research.<sup>39</sup> It is important, therefore, to interpret these results with caution. If the race of a student was what mattered, one would expect the same racial group or groups to consistently predict default rates across institution types, but this is not the case.

Even after controlling for these student characteristics, though, an institution's ability to retain and eventually graduate its students emerged as an important factor in determining that institution's cohort default rate, regardless of the types of students it enrolls. Both a higher retention rate and a higher graduation rate predicted lower default rates among four-year institutions, and higher retention rates predicted lower default rates among public two-year institutions. Surprisingly, though, neither retention rate nor graduation rate were significant predictors among for-profit colleges.<sup>40</sup>

While a higher retention rate was a significant predictor of lower default rates among public two-year institutions, an even stronger variable was the type of degrees students earned. To assess the effect of the types of degrees earned at two-year institutions, we divided the degrees awarded at each institution into four categories according to expected earnings after graduation, and included the percentage of students receiving degrees in the lowest earning category as a variable.<sup>41</sup> A higher percentage of students earning degrees in fields with the lowest salaries after graduation predicted higher cohort default rates.

## MORE INSTITUTIONAL CHARACTERISTICS—PREDICTING COHORT DEFAULT RATES

- Selectivity was significant in predicting an institution's default rate among four-year schools: Institutions that maintained the basic criteria of requiring students to submit a high school GPA for admission had lower default rates, and institutions admitting a higher percentage of applicants had higher default rates.
- Among both not-for-profit four-year institutions and for-profit two-year institutions, a higher student-faculty ratio predicted higher cohort default rates. This indicates that among these institutions, more opportunity for student and faculty interaction may contribute to lower default rates.
- Higher per-student expenditures predicted lower default rates among public two-year institutions, but were not significant among four-year or for-profit two-year schools.
- Among the public two-year institutions reporting results from the Community College Survey of Student Engagement (CCSSE), a higher score on the measure of academic challenge at an institution predicted lower cohort default rates, indicating that institutions at which students rated their school highly on measures of the quantity and rigor of the academic work had better outcomes in terms of loan repayment. In prior research on CCSSE results, the academic challenge measure has been most strongly related to academic outcomes rather than persistence or graduation, indicating that academics in school may affect students' loan repayment behavior outside of school.\*
- A higher score on the CCSSE measure of supportive learning, though, predicted *higher* default rates. This result runs counter to our research with HBCUs, which found that supporting students and establishing personal contact was an effective strategy in reducing loan default rates. But the CCSSE measure of supportive learning may confound institutional practice with student characteristics—those institutions that score highest on this measure may also have student populations with the highest needs, which could impact the outcomes of this analysis.
- Among the public and private four-year institutions reporting results from the National Survey of Student Engagement (NSSE), another surprising outcome emerged. The only NSSE variable that was significant in predicting cohort default rates was the measure of student-faculty interaction among seniors, with higher scores predicting *higher* default rates. Much like the results for the supportive learning measure in CCSSE, this result runs counter to what we know about the positive impact of student-faculty interaction on graduation rates and student persistence. More research is clearly needed on how CCSSE and NSSE results predict student outcomes in terms of loan repayment.

\*Kay McClenney, C. Nathan Marti, and Courtney Adkins, *Student Engagement and Student Outcomes: Key Findings from CCSSE Validation Research*, (Austin, TX: Community College Leadership Program, The University of Texas at Austin).

Other institutional characteristics also emerged as important variables in predicting cohort default rates. HBCU status, for example, predicted higher default rates among four-year institutions. This result may be because we were not able to control for the percentage of first-generation students enrolled at institutions. Prior research has indicated that whether or not a student's parents attended college is an important predictor of whether a student will default.<sup>42</sup> HBCUs enroll, as part of their mission, a high percentage of first-generation students, and this may be reflected in the results of this analysis.

Borrowing also mattered in predicting default rates, but not always as one might expect. For instance, higher average debt levels at four-year institutions actually predicted *lower* default rates. This indicates that higher debt may indicate some level of institutional quality—more prestigious institutions are often the most expensive, but this higher price seems to pay off in a student's ability to repay his or her debt. Among for-profit two-year institutions, a higher average amount of loan debt also predicted *lower* cohort default rates. This may be because some of the schools with the highest average debt levels include schools with a clear career-oriented focus and good job prospects for those students, such as culinary schools. The same is not true, however, for the percentage of students borrowing. A higher percentage of students taking out loans predicted higher cohort default rates among for-profit two-year institutions. (For more factors, see sidebar “More Institutional Characteristics—Predicting Cohort Default Rates.”)

No one expects institutions that serve a large number of low-income or first-generation students to have the same 0.4 percent default rate as Harvard University, but our analysis suggests that it is appropriate to hold all schools accountable for consistently keeping loan default rates below 25 percent. The wide variation in results among institutions serving similar student populations is evidence of the influence institutions have over whether students stay in good standing on their loans. We ran an additional analysis comparing each institution's actual default rate with a predicted default rate we calculated based on the institution's student characteristics, HBCU status, and selectivity. Figure 2 presents the results for four-year institutions, with each institution's actual and predicted default rate plotted.

The diagonal line indicates the point at which an institution's predicted and actual default rates match

perfectly. Institutions above the line have default rates that are better than expected, and institutions below the line have default rates that are worse than predicted. As the chart shows, no institution has a predicted default rate as high as 20 percent, much less the 25 percent federal threshold for sanctions, and institutions with similar predicted default rates can vary widely in their actual default rates. Institutions with a predicted default rate between 10 and 11 percent, for example, had actual default rates ranging from 3.3 percent to 13.2 percent.

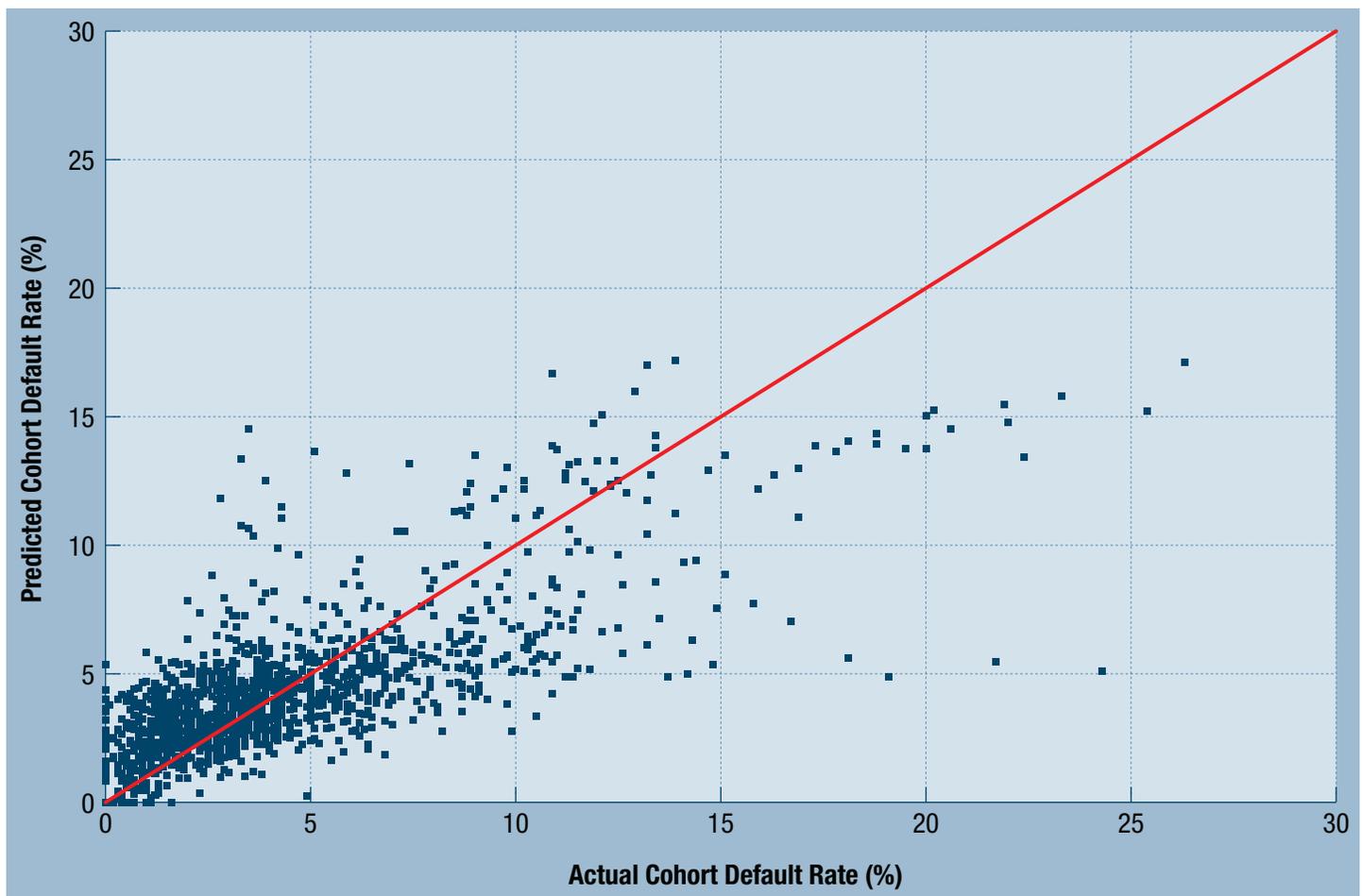
While the HBCUs we studied faced unique challenges 10 years ago, their lessons are clearly still applicable today and are relevant to a much wider group of institutions than just HBCUs. As Figure 2 shows, many institutions could do better in helping their students avoid default, a task that will become more urgent as an increasing number of schools face sanctions for high default rates in the next five years.

## ON THE HORIZON

Ten years after the “big panic,” schools are no longer in crisis mode. Thus, it is no surprise that the Texas consortium is less active and campus awareness of default prevention is less acute. Inactivity is, on one hand, a clear sign of success. Once the rates were brought down, attention and resources were allocated elsewhere. But without concentrated default prevention efforts, the rate has come back up at some schools. This is perhaps the most compelling evidence of the effectiveness of institutional measures to lower default rates—not that default rates declined so quickly at first, but that for colleges that diverted resources and attention away from default management, the rates began to climb back up.

The new three-year calculation of cohort default rates will result in even higher increases in default rates across all institutions. Combined with the current economic climate

**Figure 2. Predicted vs. Actual Cohort Default Rates Among Four-Year Institutions, 2007**



Source: Author analysis of 2007 cohort default rates, available from the U.S. Department of Education Office of Federal Student Aid, Default Prevention and Management at <http://www.ed.gov/offices/OSFAP/defaultmanagement/cdr.html>.

and high unemployment rates, schools of all types may be facing the big panic once again. Institutions, however, will not be held accountable for the new three-year calculations until 2014, providing schools with valuable time to implement default prevention measures and reduce default rates before they face sanctions. The next few years represent a critical time for schools to understand why their default rates are high and how they can lower them.

Recognizing this, Texas Guaranteed held a special session during its 2009 conference focused on rising college costs and debt levels and the new three-year cohort default rate calculation. Texas Guaranteed staff informed schools of when the new calculation will go into effect and also provided examples from real schools on how this will have an impact on institutions. They also allowed schools to find out what their three-year default rates were before the Department of Education began releasing the numbers publicly. Jacob Fraire, assistant vice president of educational alliances at Texas Guaranteed, says that this communication

is key. “Now that the law is passed, it is important to get the word out that there is time to make changes.”

The U.S. Department of Education is also working to get the word out to institutions and held multiple sessions at its December 2009 Federal Student Aid conference focused on the implications from the change to a three-year calculation. The Department of Education’s Special Initiatives Branch in the Office of Federal Student Aid is developing a strategy to work closely with minority-serving institutions to help them avoid getting caught by the new three-year calculation. As part of this work, the Special Initiatives team is holding meetings at HBCUs around the country, bringing nearby institutions together for a day of intensive default prevention training. Reminiscent of the Texas consortium, the Special Initiatives team recently gathered many of the same institutions together at Jarvis Christian College to discuss strategies for reducing default rates once again. Walsh from the Special Initiatives team describes the meetings as a combination of presentations

## HOW THE FEDERAL AND STATE GOVERNMENTS CAN HELP

The lesson from the 12 HBCUs that successfully lowered their default rates a decade ago, along with the results from our analysis of cohort default rates, is that institutions can successfully lower default rates and avoid federal sanctions without changing the students they enroll. While student background characteristics do influence default risk, there are specific steps institutions can take to reduce that risk. Some of these steps are the same as those that increase graduation rates—improving student engagement and student support on campus can help students persist, be academically successful, and ultimately succeed after graduation. And some strategies are specific to reducing default rates, such as hiring a default prevention manager and improving students’ financial literacy skills and knowledge of student loans.

But to implement these steps effectively requires dedicated financial resources and dedicated attention from campus leadership, faculty, and staff—two things that are difficult to maintain long-term for institutions that operate on tight budgets, with small staffs, and experience frequent leadership and staff turnover. The attention from the Department of Education and large guarantors like Texas Guaranteed increased the awareness of the default rate problem among faculty and administrators and made lowering the default rate a priority among consortium schools. As importantly, financial resources from TG and others went a long way toward helping the schools hire additional staff, invest in new technology, and employ the expertise of third-party consultants.

Schools or students, however, are not the only ones who can help prevent loan defaults. There are steps that the federal

government and state governments can take to reduce default rates:

- **Focus on need-based aid for low-income students:** The past 10 years have seen a growing reliance on debt and a shift away from need-based aid, particularly at the state level. By requiring low-income students to take out loans to attend public four-year, and in some cases two-year colleges, states and the federal government are putting these students at increased risk of defaulting on their loans. By reorienting grant aid to those students who most need it, and away from merit-based programs that reward middle- and upper-class students, institutions, states, and the federal government can reduce the amount of debt low-income students incur and help prevent students from defaulting on loans.\*
- **Require ‘default aversion’ to include working directly with colleges:** Congress is currently debating the Student Aid and Fiscal Responsibility Act, or SAFRA, which allows part of the \$3 billion in funds to be awarded to third-party agencies, most likely guarantee agencies, for default prevention work. The legislation also includes assessing the effectiveness of loan servicers’ default aversion work as part of the annual review of loan servicing contracts. As our research shows, default prevention is most effective when third-party agencies work closely with colleges to build capacity and expertise among the administration, staff, and financial aid office, and help institutions to develop institution-specific plans for reducing default rates. Default aversion activities should be clearly defined to include this type of collaborative work with institutions as an essential element of any successful default prevention initiative.

\*See Kevin Carey, *Colleges Giving More Financial Aid to Wealthy Students*, (Washington, DC: Education Sector, January 2006), Erin Dillon and Kevin Carey, *Drowning in Debt: The Emerging Student Loan Crisis*, (Washington, DC: Education Sector, July 2009).

on the three-year change and conversations with the schools about their challenges. According to Walsh, the meetings focus on “successful prevention strategies, which include identifying ‘at-risk’ borrowers and providing them with the support they need to be successful.” Special Initiatives asks the schools to bring their default prevention plans so that Walsh and other team members, along with fellow schools, can help create more effective plans.

But the Special Initiatives team is looking to push schools beyond just enhancing default prevention plans. Joel Harrell, the director of the Special Initiatives Branch, says the ultimate goal is to focus schools on improving student retention and student success. “When we say defaults, we want the thing that comes to mind to be student success—how do we get students to be academically successful? That’s where the action has to be.”

And it isn’t just HBCUs that need to focus on student success. Most institutions concerned with the new

change will likely be those like the 12 HBCUs that faced sanctions after 1998—small, under-resourced and serving a primarily low-income and first-generation student population. But good default management practices and a commitment to preventing students from defaulting should not be limited to these institutions. Many colleges across the country, particularly large public universities, have “HBCUs” within them—groups of students who are at a higher risk of defaulting and who need the attention and resources that institutions like HBCUs dedicate to serving these students. Recent research has documented large racial gaps in student success at many institutions, and given the connection between graduation and defaults, it’s likely that those gaps persist in institutions’ default rates. Institutions can find out which of their students are at a higher risk of defaulting and have a moral obligation—even in the absence of federal pressure—to do all they can to help these students avoid the financially disastrous results of defaulting on student loans.

## HOW THE FEDERAL AND STATE GOVERNMENTS CAN HELP (Continued)

- **Investigate the potential of front-loading grant aid:**

Financial aid officers at the schools we spoke with mentioned the value of front-loading grants, meaning that students receive more grant aid in their first and second years. Front-loading grants reduces the debt students take on early in their academic careers and allows financial aid officers to increase the ratio of loans to grants as students successfully progress through their education. This reduces the financial burden on students in their first years, and limits the amount of debt students have if they drop out early in their college career. The idea of front-loading Pell grants has gained attention in the past, although opponents object that it might appear to be a “bait and switch” for students who come to rely on the higher grant amounts, or that it could encourage students to leave mid-way through their education because of reduced grant aid in later years.\*\* Unfortunately, there is inadequate research on the topic to inform policy decisions. Congress should consider funding a demonstration project to provide greater grant aid to students in their first two years of college, with lower amounts provided in students’ final years. The results from this project would help inform policymakers about the value of front-loading grant aid as a strategy for reducing debt loads and encouraging student retention.

- **Promote the New Income-Based Repayment (IBR) Program:**

Financial aid officers we spoke with expressed enthusiasm for the new IBR program and its potential to help students who are struggling with repayment because of low salaries and high debt levels. IBR allows students to limit loan payments to 10 percent of their income, thereby allowing borrowers to make payments within their means and also stay in good standing on their loans. But the implementation

of the new program has been off to a rocky start, with a technical glitch that makes it difficult for borrowers to enroll.\*\*\* This glitch, along with different forms spread across multiple lenders, may have resulted in fewer students than expected enrolling in this program, thereby limiting its ability to help struggling borrowers. While financial aid officers are the front-line in providing students with the necessary information about IBR and the forms to enroll, the Department of Education can help by improving the ease with which students can enroll in the program and by communicating aggressively with schools and students about the availability of this new repayment option and who is eligible to take advantage of it.

- **Help colleges and states develop early alert systems:**

Having an early alert system on campus was consistently identified by financial aid officers as an important strategy for keeping track of students and intervening before students drop out. But developing the data systems needed to monitor student progress effectively and training staff on using those systems requires expertise and resources, which are not equally available to all institutions. In addition, states could use these systems across institutions to track students who transfer between schools and from two-year to four-year institutions. The federal government can encourage institutions to develop and implement early alert systems and can promote their use at the state level through targeted grants. The College Access and Completion Innovation Fund, a \$600 million program in the proposed SAFRA legislation, is intended to support effective programs for student retention and should include developing early alert systems as an authorized use of both state and institutional grant funds.

\*\*See, for instance, *Restructuring Student Aid Could Reduce Low-Income Student Dropout Rate* (Washington, DC: General Accounting Office, March 1995).

\*\*\*Kelly Field, “Glitch May Block Student Borrowers from Enrolling in Income-Based Repayment,” *The Chronicle of Higher Education*, October 8, 2009.

## APPENDIX: Methodology and Results of Our Analysis of Cohort Default Rates

### Methodology

We used a multivariate linear regression to isolate the impact of student and institutional characteristics on two-year cohort default rates. The dependent variable was the 2007 two-year cohort default rate, which measures the percentage of students who entered repayment on their loans in fiscal year 2007 and subsequently defaulted by the end of the following fiscal year. To keep the data consistent with the 2007 cohort of students, we used 2007 data on student and institutional characteristics from IPEDS, the Integrated Postsecondary Education Data System compiled by the federal government.<sup>i</sup> For institutions with fewer than 30 borrowers, we used a weighted average of the past three years of cohort default rates as the dependent variable. This is consistent with the calculation the U.S. Department of Education uses to determine whether a school faces sanctions for high default rates in a particular year. We excluded from analysis all schools with fewer than 30 borrowers total over the past three years. This eliminates schools that are likely to see wide fluctuations in default rates from year to year and is also consistent with U.S. Department of Education regulations.

We included only institutions that grant an associate's or bachelor's degree in the 50 states and the District of Columbia. Nearly 600 institutions in the cohort default rate database were excluded because they report one default rate for several campuses. For example, Pennsylvania State University reports the same default rate for its more competitive University Park campus as it does for its 19 regional campuses. Rather than aggregate the data on student and institutional characteristics for these campuses, which vary widely on these variables, we excluded all campuses that did not have a unique cohort default rate.

Because of their different missions and educational programs, we analyzed four-year institutions separately from two-year institutions. We analyzed public and private not-for-profit four-year institutions, and public and for-profit two-year institutions. The sample sizes for four-year for-profit institutions and non-profit two-year institutions were too small to yield reliable results.

### Independent Variables

Among four-year institutions, we first needed to control for graduate student enrollment. Cohort default rates include both undergraduate and graduate students who default on their loans. Research has shown that graduate-level students are less likely to default; therefore, an institution with a large graduate program, such as a law school or medical school, might have lower default rates simply because of the types of programs it operates. To control for this, we included the percentage of students receiving graduate-level degrees first in the analysis of four-year institutions.

To determine the impact of student characteristics, we included data on the racial distribution of students enrolled at each school (percentage of white, African-American, Hispanic, and Asian students), the percentage of Pell grant recipients (as a measure

of income), the percentage of female students enrolled and the percentage of adult students enrolled. We also did a separate analysis of the 1,186 four-year institutions that reported SAT score data to determine the impact of students' academic preparation on default rates.

While IPEDS collects a large amount of institutional data, very few variables can be directly attributed to institutional quality or student outcomes. Based on prior research showing the importance of student academic success on default risk, we included institutional retention rates (the percentage of students who remain after their first year) and graduation rates as measures of how well institutions are doing in promoting student success. By first controlling for student characteristics, we were able to measure the independent effect of retention and graduation rates on default rates.

We also included information on the percentage of students taking out loans and the average loan amount to determine if borrowing patterns influenced cohort default rates. Other institutional variables included in the analysis were: total enrollment, student-to-faculty ratio, expenditures per student, institutional control (e.g., public private not-for-profit, and private for-profit), and among four-year schools, whether the institution is a historically black college or university. We also included two variables when analyzing four-year institutions related to the selectivity of the institution: the percentage of students admitted and whether the institution requires students to submit a high school GPA for admission.

To assess the impact of the types of degrees students earned at two-year institutions, we divided the degree types into four categories according to expected earnings after graduation.<sup>ii</sup> We included the percentage of students receiving degrees in the lowest earning category as a variable. Similarly, to determine if degree type influenced default rates at four-year institutions, we included the percentage of students receiving degrees in liberal arts majors as a variable.

Because IPEDS data includes little information on what is happening at institutions in terms of institutional practice, we included data from the National Survey of Student Engagement and the Community College Survey of Student Engagement. We analyzed these data separately because they were provided for a smaller subset of institutions—367 four-year institutions reported NSSE data and 486 community colleges reported CCSSE results.

See Tables A1 and A2 for a listing of all the variables included in the analysis for four-year and two-year institutions.

### Results

#### Four-Year Institutions

We first analyzed four-year public and private not-for-profit institutions together. The model explained 62 percent of the

variance in default rates. The percentage of graduate students earning degrees explained 5 percent of the variance in cohort default rates, with, as expected, a higher percentage of graduate degrees predicting a lower cohort default rate. Each of the student characteristics was then entered into the regression equation using a stepwise analysis to see which characteristics accounted for a significant proportion of the variance in cohort default rates.

The percentage of Pell grant recipients and the percentage of African-American students enrolled were the two strongest predictors of cohort default rates of the student characteristics, with higher enrollments of both types of students predicting a higher CDR. The percentage of women enrolled predicted lower

default rates. Adult enrollment and the percentage of Asian students enrolled were both included in the final model, although neither variable was significant.

After all student characteristics were entered, institutional characteristics explained an additional 8.7 percent of the variance in cohort default rates. One of the strongest predictors was whether or not an institution was an HBCU, with HBCU status predicting higher default rates. Higher retention rates and graduation rates both were strong and significant predictors of lower cohort default rates.

Institutions that maintained the basic admissions criteria of requiring students to submit a high school GPA for admission also had lower default rates, indicating that minimal selectivity does impact an institution's CDR. The percentage of students admitted—another more nuanced measure of selectivity—also significantly predicted cohort default rates, with a higher percentage of students admitted predicting higher default rates.

Two additional institutional characteristics were also significant: A higher student-faculty ratio predicted higher default rates, and a higher average amount of annual loan debt predicted lower default rates (see Table A3).

When SAT scores were added to the model, they explained an additional 1 percent of the variance in cohort default rates for the 1,186 schools that reported SAT data. Higher SAT scores predicted lower cohort default rates. Once SAT scores were added, student-faculty ratio and average loan amount were

**Table A1. Four-Year Institutions**

<i>Control</i>	Percentage of degrees awarded to graduate-level students
<i>Student Characteristics</i>	Percentage of students receiving Pell grants Percentage white enrollment Percentage African-American enrollment Percentage Hispanic enrollment Percentage Asian enrollment Percentage female enrollment Percentage adult undergraduate enrollment
<i>Student Success</i>	Retention rate (full-time, first-time students) Six-year graduation rate (full-time, first-time students)
<i>Institutional Characteristics</i>	Percentage of students receiving loans Average loan amount Student/Faculty ratio High School GPA required for admission Percentage of students admitted Expenditures per student Percentage of students receiving liberal arts degrees HBCU status Non-profit status
<i>Additional Analysis: Average SAT Score</i>	Average SAT score
<i>Additional Analysis: National Survey of Student Engagement</i>	Academic challenge - 1st year students Academic challenge - Seniors Active & Collaborative Learning - 1st year Active & Collaborative Learning - Seniors Student-Faculty Interaction - 1st year Student-Faculty Interaction - Seniors Enriching Education - 1st year Enriching Education - Seniors Supportive Campus - 1st year Supportive Campus - Seniors

**Table A2. Two-Year Institutions**

<i>Student Characteristics</i>	Percentage of students receiving Pell grants Percentage white enrollment Percentage African-American enrollment Percentage Hispanic enrollment Percentage Asian enrollment Percentage female enrollment Percentage adult undergraduate enrollment
<i>Student Success</i>	Retention rate (first-time, full-time students) Three-year graduation rate (first-time, full-time students)
<i>Institutional Characteristics</i>	Percentage of students receiving loans Average loan amount Student/Faculty ratio Expenditures per student Percentage of students earning degrees in the lowest earning category (public institutions only)
<i>Additional Analysis: Community College Survey of Student Engagement</i>	Active & Collaborative Learning Student Effort Academic Challenge Student-Faculty Interaction Supportive Learning

**Table A3. Final Model: Four-Year Not-for-Profit and Public Institutions**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of degrees awarded to graduate-level students	-2.059	0.377	-0.096	<.01	0.052	0.053	<.01
Percentage of students receiving Pell grants	0.039	0.006	0.177	<.01	0.456	0.404	<.01
Percentage African-American enrollment	0.04	0.007	0.229	<.01	0.524	0.068	<.01
Percentage adult undergraduate enrollment	-0.008	0.005	-0.038	ns	0.529	0.005	<.01
Percentage female enrollment	-0.017	0.005	-0.056	<.01	0.536	0.007	<.01
Percentage Asian enrollment	0.001	0.011	0.002	ns	0.538	0.003	<.01
Retention Rate	-0.063	0.008	-0.215	<.01	0.59	0.051	<.01
Graduation Rate	-0.032	0.006	-0.163	<.01	0.603	0.014	<.01
HBCU status	2.803	0.561	0.179	<.01	0.611	0.008	<.01
High School GPA required for admission	-0.649	0.148	-0.076	<.01	0.618	0.007	<.01
Student/Faculty ratio	0.031	0.011	0.048	<.01	0.62	0.003	<.01
Average loan amount	-9.08E-05	0	-0.045	<.01	0.621	0.002	<.05
Percentage of students admitted	0.009	0.004	0.049	<.05	0.623	0.002	<.05

R<sup>2</sup> = .623, n = 1,386 schools ns = not significant

no longer significant. Instead, non-profit status emerged as a significant predictor of lower default rates (see Table A4).

We also did a separate analysis with the 367 institutions that publicly report data from the National Survey of Student Engagement. Only one NSSE variable was significant in the final model: Higher scores on the measure of student-faculty interaction in a student's senior year were related to *higher* cohort default rates. This result is surprising in light of our research showing that student-faculty interaction can be helpful in communication with students about their loan responsibilities. More research is needed on the relationship between NSSE scores and student loan default rates to understand why

student-faculty interaction predicts higher default rates (see Table A5).

#### Four-Year Institutions by Institution Type

While institutional control was not a significant variable in the overall model, we analyzed public and private not-for-profit institutions separately to determine if there were important differences between institution types in which variables predicted default rates.

The model predicted a larger amount of the variance in default rates, 64 percent, among private not-for-profit institutions,

**Table A4. Final Model: Four-Year Not-for-Profit and Public Institutions With SAT Score Analysis**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of degrees awarded to graduate-level students	-1.405	0.331	-0.077	<.01	0.028	0.029	<.01
Percentage of students receiving Pell grants	0.032	0.006	0.156	<.01	0.458	0.43	<.01
Percentage African-American enrollment	0.037	0.007	0.228	<.01	0.529	0.071	<.01
Average SAT score	-0.003	0.001	-0.11	<.01	0.582	0.054	<.01
Percentage female enrollment	-0.016	0.005	-0.065	<.01	0.59	0.008	<.01
Retention Rate	-0.063	0.01	-0.228	<.01	0.617	0.027	<.01
Graduation Rate	-0.025	0.007	-0.142	<.01	0.623	0.007	<.01
HBCU status	2.136	0.551	0.151	<.01	0.628	0.005	<.01
Non-profit status	-0.387	0.127	-0.062	<.01	0.63	0.003	<.01
Percentage of students admitted	-0.008	0.003	-0.047	<.05	0.632	0.002	<.05
High School GPA required for admission	-0.316	0.149	-0.038	<.05	0.633	0.001	<.05

R<sup>2</sup> = .633, n = 1,186 ns = not significant

**Table A5. Final Model: Four-Year Not-for-Profit and Public Institutions With NSSE Results Analysis**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of degrees awarded to graduate-level students	-0.341	0.514	-0.025	ns	0.002	0.005	ns
Percentage of students receiving Pell grants	0.047	0.01	0.248	<.01	0.396	0.395	<.01
Percentage African-American enrollment	0.059	0.008	0.289	<.01	0.463	0.068	<.01
Average SAT score	1.00E-03	0.002	0.045	ns	0.487	0.025	<.01
Percentage female enrollment	-0.016	0.007	-0.088	<.05	0.499	0.013	<.01
Graduation Rate	-0.034	0.012	-0.211	<.01	0.552	0.053	<.01
Retention Rate	-0.062	0.019	-0.235	<.01	0.562	0.011	<.01
Non-profit status	-0.872	0.22	-0.168	<.01	0.569	0.008	<.01
Faculty-Student Interaction, Seniors	0.073	0.019	0.166	<.01	0.585	0.017	<.01

R<sup>2</sup> = .585, n = 367 ns = not significant

HBCU status was excluded because there were only 7 HBCUs included in the sample.

compared with 59 percent among public institutions. For both types of institutions, the percentage of Pell recipients and African-American enrollment were significant and strong predictors of default rates. Among private not-for-profit institutions, Hispanic student enrollment also predicted higher default rates, while female enrollment predicted lower default rates.

Retention rates predicted lower default rates across both types of institutions, but graduation rates emerged as significant only among public four-year institutions. Both HBCU status and whether an institution required students to submit a high school GPA for admission remained significant predictors for both types of institutions, with HBCU status predicting higher default rates and requiring a GPA predicting lower default rates.

Among private not-for-profit institutions, a higher student-faculty ratio remained significant as a predictor of higher default rates and a higher average loan amount was significant in predicting lower

default rates. Admission rates were also significant, with a higher percentage of students admitted predicting higher default rates.

Among public institutions, a higher graduation rate and a higher percentage of students earning liberal arts degrees predicted lower default rates (see Tables A6 and A7).

### Two-Year Institutions

Our regression model explains just 15 percent of the variance in cohort default rates among two-year institutions, and many of the significant variables were different when compared with four-year institutions.

Consistent with our analysis of four-year institutions, Pell enrollment significantly predicted higher default rates. Race still mattered among two-year institutions, but white enrollment and Asian enrollment emerged as significant, with higher enrollments

**Table A6. Final Model: Not-for-Profit Four-Year Institutions**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of degrees awarded to graduate-level students	-1.561	0.398	-0.083	<.01	0.054	0.055	<.01
Percentage of students receiving Pell grants	0.042	0.007	0.203	<.01	0.497	0.443	<.01
Percentage African-American enrollment	0.047	0.009	0.262	<.01	0.575	0.079	<.01
Percentage female enrollment	-0.024	0.006	-0.091	<.01	0.582	0.007	<.01
Percentage Hispanic enrollment	0.036	0.011	0.073	<.01	0.584	0.003	<.01
Percentage Asian enrollment	-0.004	0.019	-0.005	ns	0.589	0.005	<.01
Retention Rate	-0.075	0.008	-0.273	<.01	0.626	0.038	<.01
HBCU status	3.326	0.747	0.193	<.01	0.633	0.007	<.01
Percentage of students admitted	0.012	0.004	0.067	<.01	0.636	0.004	<.01
Average loan amount	-8.56E-05	0	-0.047	<.05	0.638	0.002	<.05
Student/Faculty ratio	0.031	0.013	0.052	<.05	0.640	0.002	<.05
High School GPA required for admission	-0.386	0.185	-0.044	<.05	0.642	0.002	<.05

R<sup>2</sup> = .642, n = 879 ns = not significant

**Table A7. Final Model: Public Four-Year Institutions**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of degrees awarded to graduate-level students	-2.79	0.953	-0.093	<.01	0.05	0.052	<.01
Percentage of students receiving Pell grants	0.034	0.011	0.148	<.01	0.39	0.341	<.01
Percentage African-American enrollment	0.029	0.011	0.182	<.01	0.461	0.071	<.01
Retention Rate	-0.042	0.016	-0.132	<.05	0.486	0.026	<.01
HBCU status	3.375	0.789	0.255	<.01	0.5	0.015	<.01
High School GPA required for admission	-0.497	0.245	-0.063	<.05	0.557	0.058	<.01
Percentage adult enrollment	-0.014	0.012	-0.05	ns	0.567	0.01	<.01
Percentage white enrollment	0.012	0.007	0.081	ns	0.582	0.016	<.01
Graduation Rate	-0.069	0.012	-0.311	<.01	0.589	0.008	<.01
Percentage of students receiving liberal arts degrees	-0.017	0.006	-0.085	<.01	0.592	0.003	<.05

R<sup>2</sup> = .592, n = 507 ns = not significant

of both predicting lower default rates. Higher adult enrollment predicted higher default rates.

Surprisingly, neither retention rate nor graduation rate were significant predictors of default rates in the final model. A higher student-faculty ratio, however, predicted higher default rates, while a higher average loan amount predicted lower default rates. Contrary to many news reports of the large difference in default rates among for-profit and public two-year institutions, when other student and institutional characteristics were controlled, for-profit status was not significant in predicting an institution's default rate (see Table A8).

among public two-year institutions. The percentage of Hispanic students enrolled also predicted a higher CDR.

Among public institutions, a higher percentage of students earning degrees in the lowest earning subjects significantly predicted higher cohort default rates. Retention rate was also a significant predictor of lower default rates, although graduation rate was not. Finally, higher expenditures per student predicted lower cohort default rates.

Community College Survey of Student Engagement results were analyzed for 486 public community colleges. With CCSSE

**Table A8. Final Model: Public Two-Year and For-Profit Two-Year Institutions**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of students receiving Pell grants	0.068	0.008	0.278	<.01	0.106	0.107	<.01
Percentage white enrollment	-0.028	0.007	-0.141	<.01	0.121	0.015	<.01
Percentage Asian enrollment	-0.057	0.02	-0.098	<.01	0.127	0.007	<.01
Percentage adult enrollment	0.028	0.012	0.075	<.05	0.129	0.004	<.05
Retention Rate	-0.021	0.012	-0.057	ns	0.135	0.007	<.01
Student-Faculty ratio	0.089	0.02	0.136	<.01	0.15	0.016	<.01
Average loan amount	-1.75E-4	7.80E-5	-0.073	<.05	0.154	0.004	<.05

R<sup>2</sup> = .154, n = 965 ns = not significant

### Two-Year Institutions by Institution Type

We analyzed public institutions and for-profit institutions separately to determine if there were differences in which variables were significant and how much variance the model explained. We also included the percentage of students receiving low-earning degrees in the analysis of public institutions. There was not enough variance in this measure to include it in the analysis of for-profit institutions (see Table A9).

As with four-year institutions, the percentage of Pell grant recipients was one of the strongest predictors of default rates

variables included, the model explained 19 percent of the variance in default rates. Retention rates were no longer a significant predictor of default rates in the analysis with CCSSE results. Instead, graduation rates significantly predicted lower default rates. Among CCSSE variables, two were significant. A higher score on the measure of academic challenge at an institution predicted lower cohort default rates, while a higher score on the measure of supportive learning predicted higher default rates (Table A10).

The model varied substantially for for-profit two-year institutions, although it still only explained a small amount—21 percent—

**Table A9. Final Model: Public Two-Year Institutions**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of students receiving Pell grants	0.07	0.01	0.253	<.01	0.055	0.056	<.01
Percentage Hispanic enrollment	0.033	0.01	0.114	<.01	0.076	0.023	<.01
Retention Rate	-0.063	0.016	-0.145	<.01	0.095	0.02	<.01
Percentage students receiving low-earning degrees	3.904	0.649	0.218	<.01	0.143	0.049	<.01
Expenditures per student	-3.81E-4	1.42E-4	-0.108	<.01	0.153	0.011	<.01

R<sup>2</sup> = .153, n = 731      ns = not significant

**Table A10. Final Model: Public Two-Year Institutions With CCSSE Scores**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of students receiving Pell grants	0.08	0.012	0.298	<.01	0.083	0.085	<.01
Percentage white enrollment	-.010	0.008	-0.054	ns	0.102	0.021	<.01
Graduation Rate	-0.043	0.014	-0.13	<.01	0.112	0.011	<.05
Percentage of students receiving low-earning degrees	3.752	0.786	0.205	<.01	0.155	0.044	<.01
Academic Challenge score	-0.241	0.052	-0.213	<.01	0.173	0.02	<.01
Supportive Learning score	0.173	0.048	0.176	<.01	0.193	0.022	<.01

R<sup>2</sup> = .193, n = 486      ns = not significant

**Table A11. Final Model: For-Profit Two-Year Institutions**

Variables	B	SE B	Beta	Sig.	R <sup>2</sup>	Change R <sup>2</sup>	Sig. Change
Percentage of students receiving Pell grants	0.067	0.02	0.217	<.01	0.114	0.117	<.01
Percentage Asian enrollment	-0.19	0.068	-0.173	<.01	0.13	0.02	<.05
Percentage white enrollment	-0.035	0.014	-0.164	<.05	0.151	0.024	0.01
Percentage adult enrollment	0.047	0.021	0.136	<.05	0.164	0.017	<.05
Average loan amount	0	0	-0.167	<.01	0.181	0.02	<.05
Percentage of students receiving loans	0.051	0.022	0.143	<.05	0.196	0.018	<.05
Student-faculty ratio	0.074	0.033	0.132	<.05	0.21	0.016	<.05

R<sup>2</sup> = .21, n = 234      ns = not significant

of the variation in default rates. The percentage of Pell grant recipients remained a powerful predictor of default rates. The percentage of African-American or Hispanic enrollment was not significant; however, higher enrollment among white or Asian students predicted lower default rates. The percentage of adult students enrolled predicted higher cohort default rates.

Borrowing patterns were also significant in predicting default rates. A higher average amount of loan debt at for-profit institutions predicted *lower* cohort default rates. The same is not true, however, for the percentage of students borrowing—a higher percentage of students taking out loans predicted higher cohort default rates among for-profit two-year institutions. A higher student-faculty ratio also predicted higher cohort default rates. Neither retention rate nor graduation rate were significant in predicting default rates (see Table A11).

## Endnotes

<sup>1</sup>The exception to this is data on Pell grant recipients, which was only available for the 2008–09 school year.

<sup>2</sup>Diana Furchtgott-Roth, Louis Jacobson, and Christine Mokher, *Strengthening Community Colleges' Influence on Economic Mobility*, (Washington, DC: Pew Charitable Trusts Economic Mobility Project, October 2009). The authors identified health care as the highest return field; the second highest return fields were agriculture, business, computer science, education, engineering, environmental science, marketing, and math; the third highest return fields were building trades, English, legal services, machinery repair, protective services, and technical support for business and industry; and the lowest return fields were communications, consumer services, fine arts, humanities, human services, performing arts, personal services, public services, and social studies.

## Endnotes

- <sup>1</sup> Excluding students that qualify for loan deferment, a short-term suspension of loan payments granted for situations including re-enrollment in school, unemployment or economic hardship; loan forbearance, a postponement or reduction in payments due to economic hardship; or loan forgiveness, under which loans may be paid off in exchange for volunteer work, public service, or military service.
- <sup>2</sup> The most recent two-year cohort default rate was released September 14, 2009. "Student Loan Default Rates Increase," U.S. Department of Education Press Release, September 14, 2009.
- <sup>3</sup> Doug Lederman, "Defaults Nearly Double," Inside Higher Ed, December 14, 2009. Paul Basken, "New Measure of Student Loan Defaults Could Threaten Hundreds of Colleges," *The Chronicle of Higher Education*, December 14, 2009.
- <sup>4</sup> Under the two-year calculation, the two schools faced sanctions for having a two-year default rate above 40 percent in one year. No schools faced sanctions for having a two-year default rate above 25 percent over three years. "Student Loan Default Rates Increase," U.S. Department of Education Press Release, September 14, 2009.
- <sup>5</sup> Under the three-year calculation, 40 schools had default rates above 30 percent for three consecutive years, and more than 50 had default rates above 40 percent in any one of the past three years. Author analysis of three-year cohort default rate data released by the U.S. Department of Education in December 2009. Data available for download at <http://federalstudentaid.ed.gov/datacenter/cohort.html>. Analysis excludes schools with fewer than 30 borrowers in any year, since those schools are not subject to sanctions.
- <sup>6</sup> Robin McMillion, *Student Loan Default Literature Review* (Round Rock, TX: TG Research and Analytical Services, December 2004); Laura Greene Knapp and Terry G. Seaks, "An Analysis of the Probability of Default on Federally Guaranteed Student Loans," *The Review of Economics and Statistics*, vol. 74 (3), August 1992; Mark Dynarski, "Who Defaults on Student Loans? Findings from the National Postsecondary Student Aid Study," *Economics of Education Review*, vol. 13 (1), 1994.
- <sup>7</sup> Robin McMillion, *Student Loan Default Literature Review*; Laura Greene Knapp and Terry G. Seaks, "An Analysis of the Probability of Default on Federally Guaranteed Student Loans"; J. Fredericks Volkwein, Bruce P. Szelest, Alberto F. Cabrera, and Michelle R. Napierski-Prancl, "Factors Associated with Student Loan Default Among Different Racial and Ethnic Groups," *The Journal of Higher Education*, vol. 69 (2), March/April 1998; Michael Podgursky, Mark Ehlert, Ryan Monroe, and Donald Watson, and John Wittstruck, "Student Loan Defaults and Enrollment Persistence," *Journal of Student Financial Aid*, vol. 32 (3), 2002; Mark Dynarski, "Who Defaults on Student Loans? Findings from the National Postsecondary Student Aid Study."
- <sup>8</sup> *Student Loans: Default Rates Need to Be Computed More Appropriately*, (Washington, DC: Government Accountability Office, July 1999).
- <sup>9</sup> *Student Loans: Default Rates Need to Be Computed More Appropriately*, (Washington, DC: Government Accountability Office, July 1999), and Jim Killackey, "Default Rates Place 11 Schools on Federal Loan Hit List," *Daily Oklahoman*, August 29, 1993.
- <sup>10</sup> William A. Blakey, "The Progress of Historically Black Colleges and Universities in Reducing Student Default and Improving Default Management of the Federal Student Loan Programs: A Critical Examination," *Journal of Student Financial Aid*, Winter 2000.
- <sup>11</sup> Charles Devarics, "HBCUs Making Progress on Loan Default Rate," *Black Issues in Higher Education*, October 2002. Two of the 14 schools eventually lost accreditation and one subsequently closed. As a result, there were no cohort default rates reported for these schools beyond the 2000/2001 cohorts. We limited our research to the 12 schools that are still accredited and in operation, and that reported cohort default rates through the 2007 cohort.
- <sup>12</sup> Author analysis of 2008 IPEDS data on private not-for-profit four-year institutions.
- <sup>13</sup> Author analysis of 2008 IPEDS data on private not-for-profit four-year institutions.
- <sup>14</sup> *Breaking New Ground: The Texas Historically Black Colleges and Universities Default Management Consortium*, (Round Rock, TX: Texas Guaranteed, 2004).
- <sup>15</sup> Although Texas Southern was among the seven schools at risk of losing eligibility, it did not join the consortium. In 2001, however, Prairie View A&M joined the consortium, although it was not a part of those institutions facing sanctions.
- <sup>16</sup> Prairie View A&M University joined the consortium in 2001 and was never subject to sanctions; therefore, it is excluded from the group of consortium schools represented in Chart 1.
- <sup>17</sup> Mark Walsh, John Pierson, and Cynthia Battle, *Default and Delinquency Management*, U.S. Department of Education (conference presentation at the 2009 Federal Student Aid Conference, Nashville, TN., December 2009).
- <sup>18</sup> Robin McMillion, *Student Loan Default Literature Review*; Laura Greene Knapp and Terry G. Seaks, "An Analysis of the Probability of Default on Federally Guaranteed Student Loans"; J. Fredericks Volkwein, Bruce P. Szelest, Alberto F. Cabrera, and Michelle R. Napierski-Prancl, "Factors Associated with Student Loan Default Among Different Racial and Ethnic Groups"; Michael Podgursky, Mark Ehlert, Ryan Monroe, Donald Watson, and John Wittstruck, "Student Loan Defaults and Enrollment Persistence"; Mark Dynarski, "Who Defaults on Student Loans? Findings from the National Postsecondary Student Aid Study."
- <sup>19</sup> Mark Walsh, John Pierson, and Cynthia Battle, *Default and Delinquency Management*.
- <sup>20</sup> *Student Loans: Characteristics of Students and Default Rates at Historically Black Colleges and Universities*, (Washington, DC: Government Accountability Office), April 1998, p. 22.
- <sup>21</sup> *Breaking New Ground: The Texas Historically Black Colleges and Universities Default Management Consortium*.
- <sup>22</sup> Adrianna J. Kezar, "The Impact of Institutional Size on Student Engagement," *NASPA Journal*, 43 (1), 2006.
- <sup>23</sup> See George D. Kuh, Jillian Kinzie, Jennifer A. Buckley, Brian K. Bridges, and John C. Hayek, *What Matters to Student Success: A Review of the Literature*, (Washington, DC: National Postsecondary Education Cooperative, July 2006); George D. Kuh, Ty M. Cruce, Rick Shoup, Jillian Kinzie, and Robert M. Gonyea, *Unmasking the Effects of Student Engagement on College Grades and Persistence*, (Bloomington, IN: Center

- for Postsecondary Research, April 2007); Robin McMillion, *Student Loan Default Literature Review*.
- <sup>24</sup> *Supporting the Historically Black College & University Mission: The Sallie Mae HBCU Default Management Program*, (Reston, VA: Sallie Mae, 1999).
- <sup>25</sup> Charles F. Seifert and Lorenz Worden, "Two Studies Assessing the Effectiveness of Early Intervention on the Default Behavior of Student Loan Borrowers," *NASFAA Journal of Student Financial Aid*, 34(3), 2004.
- <sup>26</sup> Erin Dillon and Kevin Carey, *Drowning in Debt: The Emerging Student Loan Crisis* (Washington, DC: Education Sector, 2009).
- <sup>27</sup> Susan P. Choy and Xiaojie Li, *Dealing with Debt: 1992–93 Bachelor's Degree Recipients 10-years Later* (Washington, DC: U.S. Department of Education, National Center for Educational Statistics, June 2006).
- <sup>28</sup> *Breaking New Ground: The Texas Historically Black Colleges and Universities Default Management Consortium*.
- <sup>29</sup> Author analysis of graduation rate data from IPEDS.
- <sup>30</sup> Wellford Wilms, Richard Moore, and Roger Bolus, "Whose Fault is Default? A Study of the Impact of Student Characteristics and Institutional Practices on Guaranteed Student Loan Default Rates in California," *Educational Evaluation and Policy Analysis*, Vol. 9 (1), Spring 1987. See also, Matt Steiner and Natali Teszler, *Multivariate Analysis of Student Loan Defaulters at Texas A&M University*, (Round Rock, TX: TG Research and Analytical Services), January 2005.
- <sup>31</sup> J. Fredericks Volkwein, Bruce P. Szelest, Alberto F. Cabrera, and Michelle R. Napierski-Prancl, "Factors Associated with Student Loan Default Among Different Racial and Ethnic Groups"
- <sup>32</sup> *Student Loan Defaults in Texas: Yesterday, Today and Tomorrow*, (Austin, TX: Texas Guaranteed Student Loan Corporation, 1998).
- <sup>33</sup> Kelly Field, "For-Profit Colleges Lobby Against Proposed Change in Calculating Student-Loan Default Rates," *The Chronicle of Higher Education*, January 30, 2008.
- <sup>34</sup> Don Hossler, Jacob P.K. Gross, Osman Cekic, and Nick Hillman, *What Matters to Student Loan Default*, (Bloomington, IN: The Project on Academic Success, Indiana University), 2008.
- <sup>35</sup> Jennifer Engle and Colleen O'Brien, *Demography is not Destiny: Increasing the Graduation Rates of Low-Income College Students at Large Public Universities*, (Washington, DC: The Pell Institute, May 2007); Kevin Carey, *Graduation Rate Watch: Making Minority Student Success a Priority*, (Washington, DC: Education Sector, April 2008).
- <sup>36</sup> A 1995 study, for example, concluded that, "campuses can best assist their student borrowers by creating a climate that promotes good academic performance, encourages study in both pure and applied scientific disciplines, and ensures student degree completion." But the study also concluded that the national policy sanctioning schools for high cohort default rates, "assumes that default rates are under institutional control, but our results show that personal factors substantially outweigh institutional ones." The researchers made this conclusion, though, without differentiating between the impact of demographics such as race or income, and "student" characteristics that can be influenced by the institution, such as academic success in college and graduation, both of which have a strong impact on a student's likelihood to default. J. Fredericks Volkwein, Alberto F. Cabrera, Bruce P. Szelest, and Michelle Napierski, *Characteristics of Student Loan Defaulters Among Different Racial and Ethnic Groups*, (Boston, MA: AIR Forum), May 1995.
- In comparison, a 2005 study by Texas Guaranteed of students at Texas A&M University took a more nuanced approach to the question of student vs. institutional characteristics. Researchers organized the student and institutional characteristics into more precise categories such as demographics, loan counseling, financial aid, and college success. Student characteristics were separated into "performance variables," such as persistence and graduation, and demographic characteristics, including ethnicity and family income. The study found performance variables had the strongest relationship with default risk, transcending ethnicity and socio-economic status. Matt Steiner and Natali Teszler, *Multivariate Analysis of Student Loan Defaulters at Texas A&M University*, (Round Rock, TX: TG Research and Analytical Services), January 2005.
- <sup>37</sup> See, for example, Mark Dynarski, "Who Defaults on Student Loans? Findings from the National Postsecondary Student Aid Study"; Laura Greene Knapp and Terry G. Seaks, "An Analysis of the Probability of Default on Federally Guaranteed Student Loans"; J. Fredericks Volkwein, Bruce P. Szelest, Alberto F. Cabrera, and Michelle R. Napierski-Prancl, "Factors Associated with Student Loan Default Among Different Racial and Ethnic Groups."
- <sup>38</sup> See the Methodology and Results Appendix for more details on which institutions were included in the analysis.
- <sup>39</sup> J. Fredericks Volkwein, Bruce P. Szelest, Alberto F. Cabrera, and Michelle R. Napierski-Prancl, "Factors Associated with Student Loan Default Among Different Racial and Ethnic Groups."
- <sup>40</sup> We used six-year graduation rates for four-year institutions and three-year graduation rates for two-year institutions. The federal IPEDS database only reports graduation rates for full-time, full-year students, which may explain why graduation did not emerge as a significant variable for two-year institutions—a smaller portion of students at those schools are enrolled full-time, compared with four-year institutions. Retention rates for full-time students, though, were more predictive of default rates than retention rates for part-time students among public, two-year institutions. Therefore, we limited our analysis to retention rates for full-time students among public, two-year institutions. Among for-profit, two-year institutions, too many institutions were missing retention rates for part-time students to include them in the analysis.
- <sup>41</sup> Diana Furchtgott-Roth, Louis Jacobson, and Christine Mokher, *Strengthening Community Colleges' Influence on Economic Mobility*, (Washington, DC: Pew Charitable Trusts Economic Mobility Project, October 2009). The authors identified health care as the highest return field; the second highest return fields were agriculture, business, computer science, education, engineering, environmental science, marketing, and math; the third highest return fields were building trades, English, legal services, machinery repair, protective services, and

technical support for business and industry; and the lowest return fields were communications, consumer services, fine arts, humanities, human services, performing arts, personal services, public services, and social studies.

<sup>42</sup> *Student Loans: Characteristics of Students and Default Rates at Historically Black Colleges and Universities*, (Washington, DC: United States General Accounting Office, April 1998), J. Fredericks Volkwein, Bruce P. Szelest, Alberto F. Cabrera, and Michelle R. Napierski-Prancl, “Factors Associated with Student Loan Default Among Different Racial and Ethnic Groups.”