

PROMOTE INCOME SHARING AGREEMENTS IN HIGHER EDUCATION

With higher education debt at record levels, income sharing agreements (ISAs) protect students and incentivize higher education institutions to invest in students beyond their college years.

BACKGROUND

Student loan debt in higher education has developed into a financial crisis for far too many American families. According to *Forbes*, “Student loan debt in 2019 is the highest ever,” with over 44 million borrowers owing over \$1.5 trillion in debt in the United States.¹ On average, Class of 2017 borrowers owe \$28,650.²

Higher education is a massive economic enterprise. Combined spending of all degree-granting institutions of higher education (IHE) for the 2016-2017 academic year reached \$608 billion or 3.1 percent of U.S. gross domestic product (GDP).³ The Department of Education estimates that approximately 26 percent of federal undergraduate student loans in 2018 will default, nearly half of student borrowers will negatively amortize⁴ within five years, and a plurality of student loan borrowers will never repay their loans.⁵

As student loan debt has exploded, so has federal spending on higher education. In Fiscal Year (FY) 2017, the Federal Government spent \$69.7 billion on postsecondary education, and an additional estimated \$35.9 billion on research at educational institutions.⁶

ISAs are increasingly common across states and universities. ISAs allow students to receive funds upfront to cover the cost of college. In return, students with an ISA contract agree to pay the investor a percentage of their future monthly earnings for a set number of years. The investor is only successful if the student is successful. ISAs are similar to federal income-driven repayment (IDR) plans offered to federal student loan borrowers, which tie monthly payments to the borrower’s monthly discretionary income. While approximately 7.8 million federal loan borrowers are enrolled in some type of income-driven repayment plan,⁷ there is no federal ISA program.⁸

Under an ISA program, “the investor takes an ownership stake in the [asset, student or program participant], and [the investor’s] return rises and falls with the asset’s performance,” which transfers risk from the student to the investor. Unlike traditional student loans, where a student repays a fixed amount, the student’s payments to the investor are based on the student’s earnings over the course of their career.⁹ This provides students and investors with a safety net, as high-earning students cross-subsidize investor losses to lower earning student recipients, and differs from traditional private student loans that “require the average student to pay a high interest rate.”¹⁰

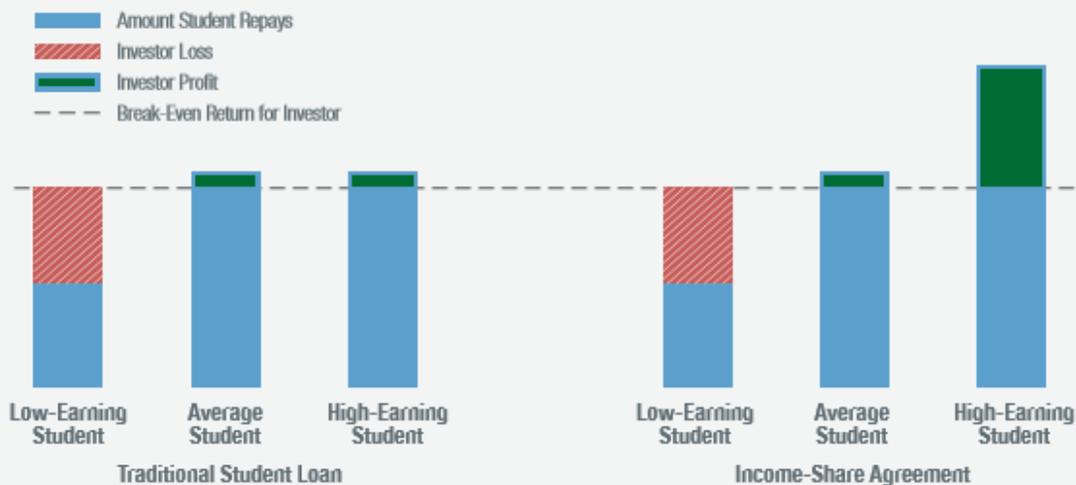
Quick Take

Student loan debt in higher education is the highest in our nation’s history.

Congress should expect recipients of higher education dollars or federally guaranteed loans to offer financing options which ensure continued interest in student financial success.

FIGURE 1.

Cross-Subsidization, Traditional Student Loans vs. ISAs



Source: Manhattan Institute¹¹

These plans also provide borrowers with certainty about their payment window, the percentage of their income they must pay towards the loan, and, ideally, the maximum repayment amount. Because ISAs protect students whose postsecondary education bets do not pay off, students graduating with lower income levels may ultimately pay less than the cost of their degrees. Students with higher incomes may pay more if they find early financial success once leaving college.

CONSTITUTIONAL AUTHORITY AND REPUBLICAN PRINCIPLES

The Constitution gives Congress the authority to tax and spend for the general welfare.¹² IHEs receiving federal funds and disbursing federal student loans should offer financing options to students which ensure continued interest in the financial success of graduates. Congress should encourage alternative college financing options, such as ISAs, by creating the regulatory framework necessary for their continued existence.

POLICY SOLUTIONS

The Institute for College Access and Success notes several areas of bipartisan consensus regarding the broader category of IDR plans which may also apply to ISAs:

- IDR is provided as an option to borrowers rather than mandated or universal;
- All borrowers in IDR make payments based on their income; and
- Married borrowers are treated consistently, regardless of how they file their taxes¹³

Transparency is critical to any loan program, especially with respect to more novel loan products such as ISA plans. The “Back a Boiler” program at Purdue University requires prospective student borrowers to “read about the ISA and take a quiz about the cap and the downsides so they fully understand [the program].”¹⁴

The President's FY2020 budget request for the U.S. Department of Education, contain options for streamlining IDR plans. One legislative solution to encourage ISAs is H.R. 1810, the "Kids to College" Act, which was introduced by Rep. Mark Green (R-TN).

Please contact Cameron Smith or Kelsey Wall with the Republican Policy Committee at (202) 225-4921 with any questions.

¹Zack Friedman, *Student Loan Debt Statistics in 2019: A \$1.5 Trillion Crisis*, Forbes (Feb. 25, 2019), <https://www.forbes.com/sites/zackfriedman/2019/02/25/student-loan-debt-statistics-2019/#75b0854b133f>.

²*Id.*

³National Center for Education Statistics, 2020-009, *Digest of Education Statistics 2018, Table 106.10* (December 2019), https://nces.ed.gov/programs/digest/d18/tables/dt18_106.10.asp.

⁴Negative amortization occurs when the net loan balance increases during repayment due to interest charges larger than loan payments.

⁵Sheila Blair and Preston Cooper, *The Future of Income-Share Agreements Policy and Politics* 6, The Manhattan Institute (Mar. 2019), <https://www.manhattan-institute.org/future-income-share-agreements-to-finance-higher-education>.

⁶National Center for Education Statistics, *supra*, note 3.

⁷Federal Student Aid, *Federal Student Loan Portfolio: Income-Driven Portfolio by Borrower Age* (2019), <https://studentaid.ed.gov/sa/sites/default/files/fsawg/datacenter/library/IDRPortfolio-by-Age.xls>.

⁸Blair and Cooper, *supra*, note 5 at 9.

⁹Blair and Cooper, *supra*, note 5 at 7.

¹⁰*Id.*

¹¹Blair and Cooper, *supra*, note 5 at 7.

¹²U.S. Const. art. I, sec 8, cl. 1.

¹³Lindsay Alhman, *The Debt is in the Details: A Review of Existing Proposals to Streamline Income-Driven Repayment*, The Institute for College Access and Success (July 2019), https://ticas.org/sites/default/files/pub_files/debt_is_in_the_details.pdf.

¹⁴Sydney Johnson, *So You Want to Offer an Income-Share Agreement? Here's How 5 Colleges Are Doing It.*, EdSurge, Feb. 15, 2019, <https://www.edsurge.com/news/2019-02-15-so-you-want-to-offer-an-income-share-agreement-here-s-how-5-colleges-are-doing-it>.