



May 7, 2015

Senator Lamar Alexander
Chairman
Committee on Health, Education, Labor and Pensions
United States Senate
428 Senate Dirksen Office Building
Washington, DC 20510

Dear Chairman Alexander:

On behalf of the National Association of College and University Business Officers (NACUBO), we submit the following comments to the HELP Committee's "Risk-Sharing/Skin-in-the-Game Concepts and Proposals" white paper. NACUBO represents chief financial officers and their staffs at more than 2,100 public and nonprofit colleges and universities. Our association is dedicated to promoting sound fiscal and administrative practices at campuses across the country.

NACUBO supports the positions presented by the American Council on Education (ACE) in response to the proposals presented in the risk-sharing white paper. However, we wanted to take this opportunity to submit additional observations and respond specifically with an accounting, financial reporting and auditing perspective on two specific components of the proposal, *Repayment of Federal Student Loans* and *Cost Structure*.

1. Repayment of Federal Student Loans: Colleges and universities assume a liability based on some factor related to their former students' repayment of federal student loans.

NACUBO's specific comments draw from knowledge of U.S. generally accepted accounting principles and auditing standards.

- As presented in the white paper, recording liabilities for assets (loans) that institutions do not own or make credit decisions on will result in unrealized losses that will (1) deflate unrestricted net assets and (2) negatively affect key balance sheet ratios calculated by analysts, investors, creditors, and the Department of Education.
- Further, there will be additional administrative burden in determining the veracity of liability estimates coupled with related financial statement disclosures. Liability estimates and credit disclosures will need to be audited, therefore, audit time and fees will increase.

Specifically, the liability and loan guarantee option would require colleges and universities to develop an accounting estimate (for the liability) and institutions would need significant amounts of timely data from the federal government on the student borrowers to develop the estimate. We believe the burden placed on the Department of Education to provide the necessary information will significantly escalate its administrative costs.

Loans outstanding for student borrowers can lead to various demographic and loan term changes over decades. Borrowers are mobile—they can change higher education institutions, enroll in graduate programs over unspecified time periods, change careers, and change residency. Default estimates and repayment time will need to consider these factors. Institutional estimates related to the liability for possible borrower defaults would require extensive information from the federal government that supports a probability-based analysis of how many or what dollar value of loans are likely to go into default. Independent auditors would routinely ask questions, seek confirmation, and request additional information to validate an institution’s measurement estimates that are used for financial reporting.

As noted in ACE’s response, which was endorsed by NACUBO, we must stress the social and financial unintended consequences. Institutions would be motivated under this proposal to control their financial destiny, and as such, may accept students with lower direct lending amounts. This will happen because a direct form of financial control an institution has over loan losses will be in the admissions decision. Such decisions will limit access to many higher education institutions for deserving students with financial needs.

We are also concerned that improvements in default rates could cause additional unintended financial consequences. It is possible that, colleges and universities can have a liability in one year, with improvement—or even substantial recovery—the following year. Yet, such improvements may be misunderstood by federal agencies and creditors when analyzing the school’s financial health. Meaning, succeeding performance improvements would be reflected as positive adjustments to loan loss reserve estimates. Such positive adjustments would improve the net asset (equity) position of the institution, giving a false impression of net income.

2. Cost Structure: Colleges and universities assume different liabilities based on the loan amount associated with some portion of an institution’s cost of attendance.

The “Cost Structure” proposal involves significant record-keeping changes to already complex student account records. Institutions will need to implement new account systems to track which dollars are applied to specific charges. In addition to federal aid, and student and family payments, other payments made to a student account can come from multiple sources, for example:

- Corporations or employers under third-party billing arrangements, including §127 plans.
- Institutional scholarships or other grants.

- State grants.
- State or local schools systems for K-12 dual enrollment.
- DoD Tuition Assistance.
- Veterans' benefits (Chapter 31, Chapter 33 and Yellow Ribbon).

Determining the formula to calculate the proportion of a loan amount associated with some portion of an institution's cost of attendance will necessitate a costly and complex regulatory system.

We are also concerned about steps that some institutions may take to circumvent additional administrative burden and audit verification. For example, the proposal creates an incentive to intentionally apply loan funds to housing or create a refund to the student in order to avoid application against tuition and related fees.

Skin-in-the Game

Higher education business officers across the country are keenly aware of the concerns you raise related to both excessive student borrowing and student success and completion, as well as the persistent gap in graduation rates between college students from different socioeconomic backgrounds. Our members have been tackling these issues, and sharing strategies to address these concerns, for many years. Some schools are taking in-depth looks at efforts to use analytics to increase student success and institutions nationwide are exploring the factors that influence student financial decisions and designing pathways to increase financial capability among students.

Not only are schools seeking best practices, they are investing in them. While the media are quick to label growth in spending at college campuses, "administrative bloat," a closer look at some of the spending reveals that schools are investing heavily in student services. A 2014 study by the Delta Cost Project at the American Institutes for Research found that, "Colleges and universities have invested in professional jobs that provide non-instructional student services, not just business support. Across all educational sectors, wage and salary expenditures for student services (per FTE staff) were the fastest growing salary expense in many types of institutions between 2002 and 2012." Non-faculty staff may include professionals in financial aid and academic advising, counseling and health services and other specialized areas from athletics to veterans affairs, where wise investments can have positive impacts on completion and student success.

We have no doubt that access will continue to be an important mission of many traditional public and private nonprofit higher education institutions. However, those institutions that continue to accept high need borrowers will likely choose to increase and dedicate administrative investments in student success as a way to mitigate future default risks of students who borrow. Such investments will increase student service expenses and the overall cost structure that tuition and fees will need to fund.

Rather than create a new punitive system, we raise a question we have been asking ourselves at NACUBO, how do we better demonstrate the investments colleges and universities are already making? Annual financial statements demonstrate the role that endowments, private fundraising, and auxiliary revenues play in lowering the pressure to increase tuition and forestall more drastic cuts in program offerings. While numbers speak volumes to business officers, our membership recognizes we need to do a better job translating balance sheets and enhancing the public understanding of how higher education institutions already have a vested interest in reducing excessive borrowing and prioritizing student success.

Institutional Authority to Manage Student Debt Levels

Our members strenuously agree with the white paper’s acknowledgement that, “Colleges and universities lack authority to manage student debt level.” College business officers support efforts to find more tools to help them limit over borrowing, and NACUBO agrees with the National Association of Student Financial Aid Administrators (NASFAA’s) position that a limited professional judgment authority for lowering loan amounts on an individual case-by-case basis is viable. We urge you to consider their recommendations. We also support NASFAA’s call for broader authority for schools to require additional counseling.

Recommendation

As students graduate, the repayment of student loans becomes a more multi-faceted responsibility and we urge you to consider additional stakeholders—including communities and employers, not just colleges and universities—as partners in meeting the committee’s goal of realigning federal incentives to reduce borrowing and promote completion. Just as investment managers mitigate risk by diversifying investment portfolios, are there federal policy mechanisms that can incentivize other parties to share the responsibility of student-to-employment success?

For example, at Portland Community College in Oregon, a city of Portland-sponsored program called Future Connect is invested in improving student outcomes. Students accepted into the program receive extra support in an effort to ensure degree completion and student retention and the program is funded through a variety of sources—about half of the funds come from the City of Portland (the City’s “skin-in-the-game”) with Portland Community College expected to match the amount with a combination of private and college resources.

The city’s interest stems from the basic fact that college-educated citizens are more likely to vote, volunteer in their communities, live healthier lifestyles, and are more likely to be employed and less likely to be dependent on federal, state and local income support programs. This program clearly recognizes that greater earnings power and lower unemployment rates result in increased productivity of the local economy—and beyond.

We very much appreciate the opportunity to provide comments and look forward to continuing the conversation as you work toward reauthorization of the Higher Education Act.

Sincerely,

A handwritten signature in black ink, appearing to read "John Walda". The signature is stylized with a large, looping initial "J" and a cursive "Walda".

John Walda
President and CEO