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Integrity versus access? The effect of federal financial aid availability on postsecondary enrollment☆

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ABSTRACT

It is generally believed that access to financial aid will increase the likelihood that students will attend and graduate from college. There is a surprising lack of research, however, on the consequences when postsecondary institutions lose eligibility to disburse financial aid. This paper provides among the first causal estimates of institution-level financial aid funding loss on enrollment and composition of student bodies. I implement a dynamic regression discontinuity design using a multi-year rule that restricts institutions' eligibility to offer federal aid such as Pell Grants and subsidized loans when alumni's loan repayment rates are below allowed thresholds. Results suggest that financial aid loss discourages enrollment at for-profit institutions and institutions that offer programs of two years or less. The decline in enrollment appears to be driven by fewer new enrollees, particularly at for-profit colleges. I find less conclusive evidence that ineligibility to disburse federal financial aid substantially alters student body composition. This research is particularly relevant considering recently proposed federal rulemaking that will further limit the number of institutions eligible to disburse financial aid based on additional student loan debt repayment requirements. Restrictions such as these are intended to protect students and the integrity of federal aid programs, but may also have implications for access to higher education.

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1. Introduction

A robust economics literature examines the effect of financial aid on students' likelihood of enrolling in and graduating from college. Little is known, however, about the consequences for students and schools when postsecondary institutions lose the ability to disburse financial aid. Recently, spurred by government and media reports of federal aid fraud and abuse at some for-profit colleges (e.g., GAO, 2010; Lewin, 2010), the US Department of Education ("ED") proposed controversial additions to requirements that determine which institutions are eligible to disburse federal financial aid. These regulations attempt to further limit the number of postsecondary institutions disbursing federal financial aid, including Pell Grants, Stafford Loans, and other aid.

This type of rulemaking endeavors to protect students, taxpayers, and the "integrity" of federal aid programs by holding institutions accountable for the use of federal student aid funds. Opponents, however, allege that such regulations are discriminatory, unnecessarily burdensome, disproportionately harm at-risk and underserved students, and have potentially negative implications for access to postsecondary education (ED, 2011a). Regulatory initiatives of this type are not uncommon. In the past 20 years, the ED has implemented a number of policies that determine which institutions are allowed to disburse federal aid. Key components of recently proposed program integrity regulatory efforts were vacated because of the lack of empirical evidence available to support requirements. Because of ongoing concern about the value of educational experiences at certain institutions, however, there will likely be significant contentious policy proposals related to institution-level financial aid disbursement eligibility considered in the future.

In this study, I present the first causal estimates to my knowledge of the effects on institution-level enrollment and student body composition when postsecondary institutions lose eligibility to disburse federal financial aid. Certain federal financial aid program integrity regulations aim to safeguard students by discouraging their attendance at schools that allegedly provide little return to human capital investments or result in unmanageable debt. The rules also attempt to protect taxpayers by limiting publicly subsidized enrollment at institutions where former students do not or cannot repay student loans. As a result, institutions that lose aid disbursement eligibility may experience decreases in the matriculation of financially and/or geographically constrained students. As well, the lack of debt repayment by former students may serve as a negative signal to prospective students about the returns to education at ineligible schools. Over time, aid disbursement ineligibility may also affect the management and survival of institutions, leading to closure

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or an operations overhaul. Alternatively, if losses of institutional aid eligibility have no impact on schools' enrollments or student body compositions, such findings would suggest that institutions can compensate for the loss of federal aid or that this aid is not critical to operations.

The challenge with isolating causal estimates of institutional aid eligibility loss is that ineligibility is possibly correlated with a number of institutional strategies or problems, such as poor management or lack of viable program offerings that could also affect enrollment and student body composition. To isolate the loss of federal aid eligibility as the source of enrollment changes, I take advantage of one of the existing federal requirements that renders schools ineligible to disburse funds if the rate at which former students default on student loan obligations (the yearly cohort default rate or “CDR”) exceeds 40% in a single year or 25% for three consecutive years.

These thresholds are used to implement a dynamic regression discontinuity (“DRD”) design. In the DRD, I identify differences in institution-level outcomes by comparing the enrollment and student body composition of institutions that are just over the eligibility cutoffs against the outcomes of institutions that are just under. Schools cannot precisely select themselves into ineligible (treatment) and eligible (control) groups and therefore variation in treatment near the cutoff can be considered as good as randomized (Lee and Lemieux, 2010). I use a relatively new variation of a regression discontinuity design to dynamically take into account the multiple year conditionality of one of the thresholds. Institutional data comes from the National Center for Education Statistics Integrated Postsecondary Education Data System (“IPEDS”) and is combined with institution-level cohort default rate data available from the ED.

The primary findings provide evidence that program integrity rules are effective in discouraging enrollment at schools with alumni who default on student loans at a high rate, with eligibility loss due to CDR threshold violations resulting in lower annual overall enrollment of approximately 12–16% at for-profit and two-year institutions. The results appear driven by declines in first-year students, particularly at for-profit institutions, and observed medium-to-long run consequences are larger than immediate ones. Reduced enrollment at institutions that fail student loan debt measures might be considered a favorable outcome if these schools produce a large number of students with unaffordable debt burdens. Further research is needed, however, to directly assess whether students who forgo education at ineligible schools transfer to other programs or drop out of higher education altogether. In addition to lower enrollment, I observe that completions declined at for-profit institutions after eligibility loss, though this result is not robust to all sensitivity tests. I find little conclusive evidence that the composition of student bodies at ineligible schools changes substantially because of loss of eligibility.

The paper is organized as follows. Section 2 provides context on federal financial aid. Section 3 reviews existing literature on the effects of financial aid and discusses why institutional federal financial aid program ineligibility has consequences for enrollment and student body composition. Section 4 presents identifying assumptions and empirical research design. Sections 5 and 6 provide an overview of data and a discussion of results. Section 7 concludes and provides policy implications.

2. Background on federal financial aid and cohort default rates

Title IV of the Higher Education Act of 1965 and subsequent amendments (“Title IV”) govern the primary set of federal programs providing financial assistance for postsecondary students. Title IV authorizes a number of well-known federal grant and loan programs, such as Pell Grants, federal student aid work–study, and Stafford and PLUS loans through the William D. Ford Federal Direct Loan Program (“FDLP”).[1] Table 1 lists Title IV grant and loan programs, along with related expenditures for the 2009–2010 school year. Concerns persist that some of this public investment is wasted by generating revenue for certain schools that do not offer a high-quality education (GAO, 2010). Indeed, much of the consternation about alleged abuses by for-profit schools concerns claims that some schools commandeer federal funds by having students pay for tuition using public money and provide very little in return.

Table 1
Title IV federal student aid, 2009–2010 academic year.

Program	Total aid ($MM)	10-Year change in total aid
Grants		
Pell	$28,213	203%
Supplemental Educational Opportunity (SEOG)	$758	−5%
Leveraging Educational Assistance Partnership (LEAP)	$63	95%
Academic Competitiveness (ACG)	$503	n/a
Science and Mathematics Access to Retain Talent (SMART)	$361	n/a
Loans		
Perkins	$1106	−22%
Subsidized Stafford — Federal Direct (FDLP)	$14,190	105%
Subsidized Stafford — Federal Family Education (FFELP)	$22,551	61%
Unsubsidized Stafford — Federal Direct (FDLP)	$16,721	251%
Unsubsidized Stafford — Federal Family Education (FFELP)	$27,968	155%
PLUS — Federal Direct (FDLP)	$5934	309%
PLUS — Federal Family Education (FFELP)	$8231	195%
Federal Work Study	$1417	20%

Source: Baum et al. (2010). ACG and SMART grants started within the past 10 years and therefore 10 year change is not displayed.

Institutions lose Title IV eligibility for a number of reasons: voluntary withdrawal from the program; change in status (e.g., school opening/closure, change in ownership, or merger); failure to comply with program requirements (e.g., gain or loss of accreditation, financial responsibility, or administrative capability); federal policy changes; and subject to loss because of high student loan cohort default rates (Congressional Research Service, 2007). For this study, I focus on Title IV eligibility changes due to the final reason, subject to loss because of high student loan cohort default rates.

The main empirical identification strategy in this study examines loss of Title IV eligibility because of high institution-level student loan CDRs. CDRs are calculated as the percentage of a school's former students who, within a two year period after starting repayment of particular FFEL and FDLP loans, default on student loan obligations.[2] Institutions with CDRs greater than or equal to 25% for three consecutive years or exceeding 40% for one year are subject to loss of Title IV program eligibility for the remainder of the year in which the ED notifies the institution of its violation and the ensuing two fiscal years.[3] In order to regain Title IV fund disbursement eligibility, institutions need to prove compliance with regulations. There is some additional flexibility in disbursement afforded to schools with extremely low CDRs, though they are not likely to be generous enough to substantially influence institution behavior.[4]

[1] Prior to July 1, 2010, the Federal Family Education Loan (“FFEL”) program allowed private lenders to offer federally subsidized student loans.

[2] PLUS, Grad PLUS, Insured Student Loans, and Perkins loans are not included in cohort default rate calculations. For schools with less than 30 borrowers entering repayment in any fiscal year, the ED calculates default rates as an average repayment rate over a three year period.

[3] Starting in 1992, institutions lose Title IV eligibility if they have cohort default rates exceeding 25% for 3 consecutive years or 40% for 1 year. The thresholds were 35 and 30% in for the multiple year cut-off and 45 and 40% for the single year cut-off in 1990 and 1991 respectively. In this study, I use the threshold value to which they were subject for each year.

[4] For example, in some years, schools with cohort default rates less than five percent gain some privileges associated with disbursing loan proceeds to students studying abroad, and schools with cohort default rates less than ten percent earn flexibility with the timing and number of installments for loan disbursements.

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