THE REPUBLICAN STUDY COMMITTEE
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Legislative Bulletin……April 27, 2012

Contents:

H.R. 4628 – Interest Rate Reduction Act
(Biggert, R-IL)

Order of Business: The bill is scheduled to be considered on April 27, 2012, under a closed rule with one hour of debate.

Summary: This legislation amends the Higher Education Act of 1965 to keep the Stafford loan rates to undergraduate students from an automatic rate increase scheduled for July 1, 2012 of this year. The rates were to go from 3.4% to 6.8%, but this legislation would push that increase back for one more year until June 30, 2013. Rates were originally pushed to these levels for five years under H.R. 5 from 2007 (read our Legislative Bulletin). H.R. 4628 would also repeal the Prevention and Public Health Fund from the Patient Protection and Affordable Care Act, which is an advanced-appropriated pool of funds, to offset this spending.

Maintaining the lower, taxpayer subsidized loan rate will cost taxpayers $5.9 billion for a one-year extension. Those new borrowers who apply for the loans this year will save about $7 a month after they graduate.

Background: While the cost of attending college has risen rapidly in the last decade even as federal aid has also increased sharply. 65% of students who got a bachelor's degree in 2010 graduated in debt. The federal government's aid is part of the problem.

College costs are increasing faster than the cost of living, over the past 10 years the cost of private college has jumped more than 60%, nearly three times as much as incomes over the same period, and will now set you back $42,000 a year on average.

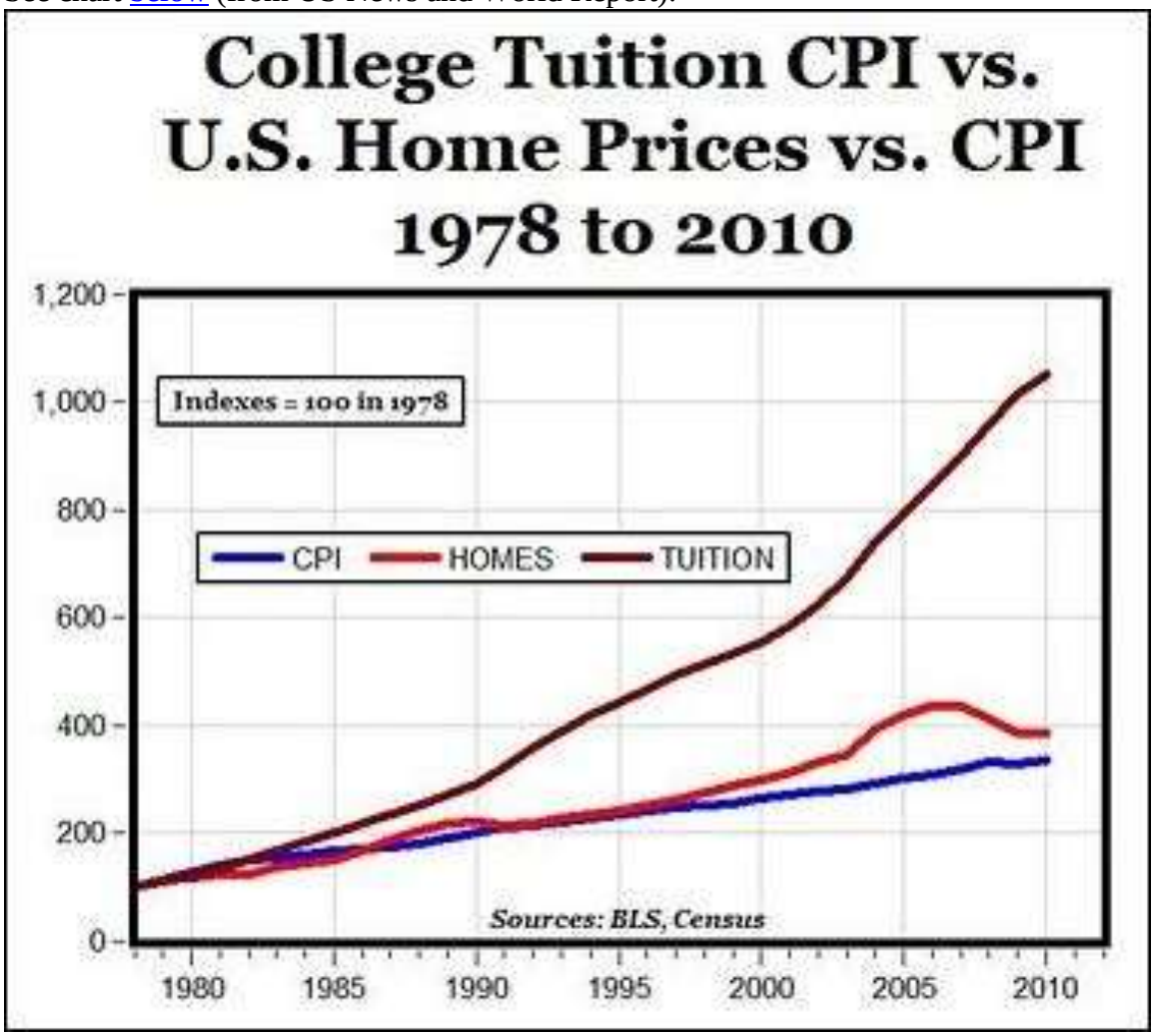
Prices at public colleges have shot up even more, nearly doubling to $21,000 for in-state students. By 2020, at a four-year bill is likely to top $240,000 for private schools and $155,000 at public universities.

This increase is the problem, and many conservatives would argue that hiking student aid is not the solution; in fact, that may be the underlying reason for this increase.

When determining the cost of higher education, colleges and universities know they are guaranteed a certain amount from students based on the amount of aid the student receives from the government. The cost of attending college has increased 439 percent since 1982 (after adjusting for inflation). Since 1980, Pell grant funding has increased 475 percent (after adjusting for inflation). *Continuing to increase federal subsidies hasn't helped reduce college costs and has likely exacerbated the problem.*

As federal involvement has increased and the maximum grant/loan amounts have increased, this has allowed colleges and universities to respond by increasing the cost of education expenses, creating an upward spiral of cost and federal involvement. Also, by inflating the demand for higher education through government intervention, basic economics suggests this has the effect of increasing costs. Cato has written extensively on this subject here.

See chart below (from US News and World Report):



What are some of the drivers of this increase in cost?:
Over the 10 years that ended in 2009, spending by large public universities on instruction rose about 10% in real terms (over ten years), reports the Delta Cost Project, a nonprofit that analyzes college expenses. Meanwhile, spending on student services jumped 19% (over ten years), and outlays for operations shot up 20% (over ten years), as the bills for everything from maintaining lavish dorms and spa-like gyms to salaries for the legions of administrators it takes to run large universities these days took their toll (read rest of report for a very thorough analysis of this question).

Spending on athletics has accelerated at twice the pace of spending on academics, according to the Knight Commission on Intercollegiate Athletics, even though most programs lose money. Of the top 120 Division I football teams, for example, only 22 showed a profit last year. Defenders say those programs are still valuable because they can lead to a spike in admissions applications and alumni donations.

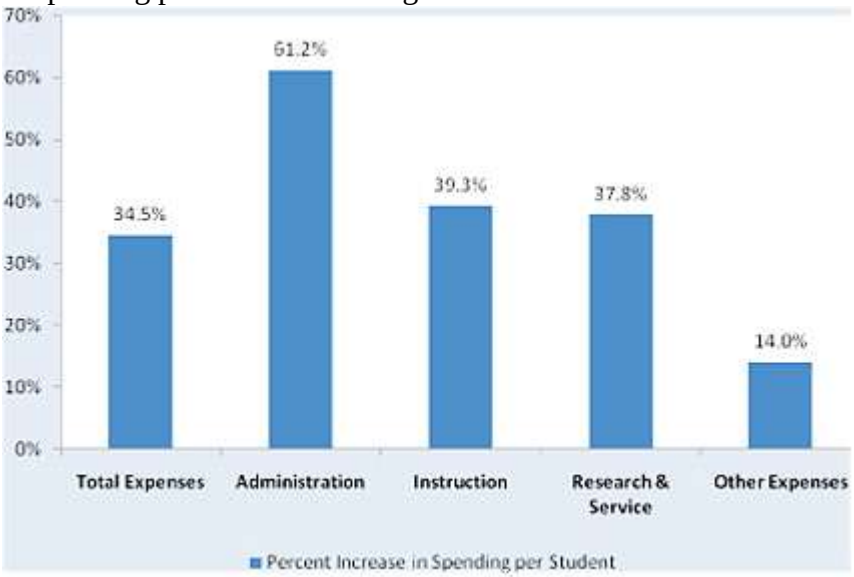
See their chart below:

Private institutions: Average expenditures per FTE student, AY1998–2008 (in 2008 dollars)

1998	2003	2004	2005	2006	2007	2008	Private bachelor's sector	
$7,232	$7,972	$7,963	$7,986	$7,936	$8,062	$8,172	Instruction	Standard expense categories
$746	$715	$747	$729	$731	$740	$725	Research	
$2,845	$3,352	$3,381	$3,442	$3,542	$3,660	$3,740	Student services	
$588	$748	$710	$699	$679	$692	$628	Public service	
$1,692	$1,953	$1,948	$1,953	$1,958	$1,994	$2,017	Academic support	
$4,548	$4,854	$4,807	$4,783	$4,957	$4,973	$5,091	Institutional support	
$1,923	$1,932	$1,929	$1,992	$2,035	$2,070	$2,110	Operations and maintenance	
$3,159	$2,692	$2,668	$2,685	$1,687	$1,529	$1,692	Net scholarships and fellowships	
$19,894	$21,170	$21,122	$21,150	$21,136	$21,397	$21,676	**Education and general**	
$4,349	$4,943	$4,863	$4,851	$4,929	$4,989	$4,953	Auxiliary enterprises, hospitals, independent and other operations	
$24,150	$26,050	$25,912	$25,898	$25,961	$26,270	$26,503	**Total operating expenditures**	
$17,909	$19,705	$19,665	$19,804	$20,090	$20,407	$20,750	Education and related	Grouped expense categories
$1,263	$1,223	$1,285	$1,262	$1,260	$1,279	$1,232	Research and related	
$1,002	$1,307	$1,233	$1,191	$1,148	$1,162	$1,048	Public service and related	
$3,159	$2,692	$2,668	$2,685	$1,687	$1,529	$1,692	Net scholarships and fellowships	
$19,894	$21,170	$21,122	$21,150	$21,136	$21,397	$21,676	**Education and general**	
$4,349	$4,943	$4,863	$4,851	$4,929	$4,989	$4,953	Auxiliary enterprises, hospitals, independent and other operations	
$24,150	$26,050	$25,912	$25,898	$25,961	$26,270	$26,503	**Total operating expenditures**	

Source: Delta Cost Project IPEDS database, 1987–2008, 11-year matched set.

This is another chart from a Goldwater Institute Study analyzing the percentage increase in spending per student in colleges and universities from 1993-2007:



Is federal aid promoting inefficiency?:

Colleges don't have to cut into academic programs to keep rising costs in check, as shown by a report last year from McKinsey on highly efficient colleges. Among the easier-to-implement ideas: shifting some services online and outsourcing dining and IT. Many of the practices actually improve the educational experience for students (McKinsey's study is a good resource).

This study found that high-performing institutions are achieving degree productivity up to 60% better than their peer group average demonstrating that certain choices can have a large increase in efficiency. The study consolidated these choices into five strategies that increase productivity:

1. **"Systematically enabling students to reach graduation.** Graduation rates vary widely between institutions, even within peer groups. Among community colleges, graduation rates typically range from 19 percent to 45 percent and from 37 percent to 62 percent among four-year institutions. Reforms to enable students to persevere through to graduation include providing structured pathways to graduation, effective student supports and effective placement and college preparation, as well as preparing students for post-study work."

2. **"Reduce nonproductive credits.** Analysis of state data suggests 14 percent of the credits earned by degree completers are over the threshold required by their degree. Such "excess crediting" may constitute up to 10 percent of total credits taken by all students. Failed credits and credits from which students withdraw constitute another 7 percent. Although excess crediting may give students extra

educational benefit, it adds to the cost of a degree and so diminishes degree productivity. The latter can be improved by 4 percent to 26 percent by initiatives to prevent such redundant efforts. Measures include better developmental education and tutoring, policies for tracking and intervening to support student progress and completion, transfer policies that conserve credits, and innovative delivery methods."

3. **"Redesigning instruction.** On average, institutions spend $7,000 on instructional costs per full-time student equivalent (FTSE), ranging from $4,000 for associate-granting institutions to $22,000 for elite research institutions. By redesigning the way they deliver instruction the eight institutions that we visited achieved degree productivity 17 to 26 percent better than the average without compromising degree quality."

4. **"More efficient core supports and services.** Core support services include institutional supports (such as HR, IT, and finance,), student services (such as financial aid, counseling, and enrollment), academic support services (including libraries, museums, and audio/visual services) and plant operations. On average, institutions spend about $9,000 per FTSE on core supports and services—ranging from about $4,000 for associate-granting institutions to $21,000 for the most competitive research institutions."

5. **"Optimize non-core services and other operations.** Top-performing institutions also carefully assess the non-core services and other operations they must offer to fulfill their mission, to ensure they are run efficiently. In our sample, non-core services and other operations included research, public services, and auxiliary enterprises. Institutions spend an average of $3,500 per FTSE on non-core services, ranging from $500 for associate-granting institutions to $21,000 for the most competitive research institutions. Competitive bachelor's-granting institutions spend $2,500 per FTSE on non-core services."

The McKinsey study found that the most efficient institutions were able to accomplish these strategic goals because they were supported by:

1. "Efficient and effective operations processes supported by appropriate technology and tools.
2. Effective management systems to ensure progress, build capabilities, and manage implementation
3. Leaders and staff who are committed to achieving degree productivity gains alongside high-quality educational outcomes.
4. Support from state and institutional policies that allow them to choose how to achieve their quality and efficiency goals."

Many of these practices actually improve the educational experience for students:

> "A mentoring program at Southern New Hampshire University in Manchester, for example, keeps costs per student low by helping ensure students are not wasting money on unnecessary credits. And a shift to a year-round calendar at Brigham Young University in Idaho has led to a 32% drop in costs per student, with extra tuition revenue more than off-setting a rise in faculty costs."
>
> A bigger, bolder move to hold down costs: Boost the number of hours professors teach. Using data from the University of Texas at Austin, Richard Vedder, head of the nonprofit Center for College Affordability and Productivity, concluded that the average public research university could reduce its faculty size at least 25% by requiring professors to teach one or two more classes a year. While some faculty argue that heavier teaching loads would impede research -- and could spur some teachers to flee to private colleges -- Vedder's data show that many UT professors successfully juggle large teaching loads and research." (from CNN)

Increasing student aid by subsidizing student loans does nothing to further incentive any of these types of behavior by universities. It has the perverse incentive of making students less savvy customers in choosing their education. Some students are effectively putting their education on their credit card, because of this incredible growth in the costs of colleges, and when they are taking out a large amount of debt they are less likely to be price discerning in their decisions. Loans at 3.8% interest rate are almost as low as a mortgage rate for someone with excellent credit (but without the collateral); this interest rate is a few percentages off from the rate of inflation.

Behavioral economics has demonstrated that, in reality, economic assumptions of people being rational actors are fundamentally incorrect in many situations, and this is a core demonstration. Taking online courses, summer courses or attending a cheaper college may be a rational economic behavior that benefits students in the long run, but student loans may create a psychological "credit card" like mentality that effectively treats an education that costs $60,000 per year as economically comparable to one that cost $20,000 per year. In the realm of other purchasing decisions the price disparity is clear, but in the context of education, purchasers often approach it with a different mentality, and student loans may accentuate that psychological lapse in judgment.

The true costs to the middle class – paying through debt:

Subsidizing student loans benefits graduates who earn higher than average incomes after their education concludes. The effect of government involvement in higher education, in part, imposes taxes on blue-collar workers, who are more likely not to have attended college, in order to pay for the higher education of future white-collar workers.

Not only do the subsidies fail to stem the rising cost of a college education, the loans are also easily attained, increasing the likelihood taxpayers will be left on the hook when students default. There are no limitations on these loans for overall student performance.

Subsidizing loans without regard to what college students choose, or what major they choose (like frisbying), and however they choose to apply themselves (getting A's or F's) creates perverse market incentives. If a student is failing out of college, many conservatives would argue that taxpayers should not continue to give him or her student loans, because they are likely to never get a job that can pay those loans back.

While many credit card companies won't give students their own credit card without a co-signer, the federal government is willing to back $10,000s of dollars in subsidized loans without due diligence into the potential risk of default, this lack of proper underwriting could ultimately put tax-payers on the hook for much more than the expected costs.

The true costs to the middle class – paying out of pocket:
While many students take out student loans, other students are able to save up money or receive money through others to pay their way through part or all of college. These other students may take out private loans. In many colleges and universities, most student aid is provided on the basis of diversity or income level, rather than merit. There is a two-priced system of education. Today millions of Americans pay one price for college education, and other millions of Americans, at the same college, pay significantly more money for the same education. Across the country, instances of this are increasing, where tuition increases by $1500, but financial aid grants increase by $1000 per person. This means that some students have to pay $1500 vs. and some students will be paying $500 for the tuition hike.

The report, Trends in Student Aid 2009, shows that financial assistance is contributing to a widening gap between the published price of college and the amount students actually pay. On average, undergraduates received $10,185 in grants and loans during the 2008-09 academic year, the latest data available. That sum has risen sharply in the past decade, in inflation-adjusted dollars. In the 1998-99 academic year the average was $6,688.

Merit based aid is increasingly disfavored, reducing part of the normal positive incentive structure for students. *Why should public policy disfavor using scarce public resources to incentive high performance?*:

Case Study - UMASS Amherst:

Massachusetts instituted a policy of free tuition in publicly funded state Universities for students who score in the top quartile in their state assessment exam (MCAS). The change in costs for highly performing students at the top public school in Massachusetts, UMASS Amherst, has been stark. In the previous year, before the free tuition policy went into effect, fees (in addition to tuition but not including room/board) were under $4,000 in addition to the tuition, but fees for the current year are $10,898, nearly a 300% increase in under 10 years in the costs for highly performing students. At the same time student aid has increased. During the same time, the financial aid commitment of UMASS Amherst has increased by 444%, going from $35.6 million to $158 million (this analysis was created by the RSC, not from any study).

This student aid policy was created in 2007 be a Democratic led Congress, and 71 Republicans voted against it at the time:

- In 2006, as part of their "6 for '06" campaign agenda, Democrats promised to cut student loan interest rates in half.

- However, once gaining control of Congress in 2007, Democrats realized it was too costly to cut all student loan interest rates in half. Instead, Education & Labor Committee Chairman George Miller (D-CA) and then-Speaker of the House Nancy Pelosi (D-CA) proposed temporarily reducing interest rates for undergraduate students receiving subsidized Stafford loans.

- The College Cost Reduction and Access Act incrementally phased down interest rates for subsidized Stafford Loans made to undergraduate students over four academic years from 6.8% to 3.4%. Per the law, interest rates are scheduled to return to 6.8% on July 1, 2012.

- As the expiration date crept closer, Democrats did nothing to address the impending interest rate increase during the 111th Congress, despite taking action to terminate the private sector federal loan program to help pay for Obamacare.

Potential Conservative Concerns:

Using agreed upon deficit reduction to pay for new spending:
This legislation is paid by a $15 billion PPHF "slush" fund for the President's health care law. All conservatives agree that Obamcare should be repealed, and that the "savings" should be used to pay down the debt. Further, repealing Obamcare was part of the RSC FY 2013 budget and the House-passed FY 2013 budget.

One choice is to save $12 billion over ten years by repealing this without new spending. This bill uses a portion of the savings for new spending.

As Frederick Hess of AEI argues, "Newsflash: we're borrowing a trillion bucks this year. None of this is paid for. Any cuts we find could trim that debt. We need all those cuts *and* to let the 3.4% rate expire."

If one of the problems with Obamacare includes spending too much money, many conservatives would argue that we can't simply take that money and re-direct it to new spending.

One year spending with a ten year pay-for:
Many conservatives would argue that one-year spending with a ten year pay-for is a problematic. Pairing that new spending with a ten year savings pays for it, but over a ten year horizon.

Sometimes these out year savings never materialize in practice (e.g. Doc fix).

Partially repeals Obamacare:
Taking apart Obamacare piece by piece, as opposed to wholesale, may create an impression that this legislation is severable.

It is not severable. The vast majority of conservatives believe in repealing this legislation in its entirety.

Hurting the private sector and potentially hurting the consumer:
By increasing the federal government's role in student loans we are discouraging private loan providers who often can provide more competitive products than that offered by the federal government (not including subsidization). The solution is to allow the private sector to provide competitive student loans. If we allow for private loan providers to base their products upon several factors, similar to how car insurance works, then someone with a 4.0 in Chemical Engineering would likely have a substantially lower student loan rate than anything offered by the federal government (even including the subsidized loans).

Let the private sector provide better products then the public sector can offer.

Process Concerns:
Student loan reform is an important issue for the House to address. There are many major issues to address:

- There is a large amount of student debt.
- The federal loan program does a poor job underwriting these loans.
- There is a lack of flexibility in utilizing these loans.
- The FAFSA forms are too long and complicated.
- There was a federal take-over of the private federal loan market industry.

- Freeing the private student loan market to make rates more competitive to actually help students.
- Transitioning to an aid program mainly based upon merit.

The legislation was introduced on April 25, 2012, referred to the House Committee on Education, Committee on Energy and Commerce, and Committee on Budget. There was no mark-up or committee hearing. The Rules Committee met at 6:30 PM, on April 25, 2012, and announced a floor vote on Friday.

There is still time for the House to consider this issue in depth and to reform the many problems with the federal student loan program.

Supporting Arguments:

Reduces net federal spending:
This legislation reduces federal spending on *net* by $6 billion over ten years.

Repeals an Obamacare program.
This legislation gets rid of the Prevention and Public Health Fund, a slush fund for the Patient Protection and Affordable Care Act

Committee Action: The bill was introduced on April 25, 2012, and referred to the House Committee Education and the Workforce, the House Committee on Energy and Commerce, and the House Committee on the Budget.

Administration Position: The White House has not released a Statement of Administration Policy at this point.

Cost to Taxpayers: CBO estimates that this legislation will reduce net spending by $6 over ten years in estimated outlays.

Does the Bill Expand the Size and Scope of the Federal Government?: This legislation contains provisions that increase the size of the federal government

Does the Bill Contain Any New State-Government, Local-Government, or Private-Sector Mandates?: No.

Does the Bill Contain Earmarks/Limited Tax Benefits/Limited Tariff Benefits?: Yes.

Constitutional Authority: Rep. Biggert's statement reads: "Congress has the power to enact this legislation pursuant to the following: Article I, section 8 of the Constitution of the United States."

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