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Financing Graduate Education: Next Steps for Federal Policy

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Key Points

- In the interest of students and taxpayers, it is time for bipartisan and commonsense graduate financing policy reform.
- This issue's complexity and importance demand a comprehensive solution that balances protecting students and taxpayers from low-value programs with ensuring equitable access to high-value ones.
- Doing so will require additional support to students and institutions that have need and provide significant value and a system with sufficient data transparency to understand the effects of the policy changes.

This report is a follow-up to our organizations' joint 2023 report,[1] which introduced five foundational pillars needed to address crucial issues in federal graduate financing: (1) setting reasonable loan limits, (2) providing targeted grant aid to students and institutions, (3) ensuring sufficient value and return on investment for students and taxpayers, (4) enhancing the regulatory structure and consumer protections for private lending, and (5) improving data disclosure and transparency.

This report further examines key issues and questions raised in our initial report and explores the breadth of specific policies that could achieve what is needed in each pillar. These policies need to be thoughtfully balanced across the pillars. For instance, binding loan limits would have serious implications for access, which should be addressed with targeted increases in grant funding. At the same time, constraints on federal lending would likely spur growth in private education lending, which should be met with appropriate reforms to the regulations that protect borrowers from usurious terms. We offer these policies as examples of potential approaches, but we are not specifically recommending them—nor do we believe that the following is a comprehensive list of possibilities.

Pillar One: Set Reasonable Loan Limits

The cost of graduate education has steadily increased over the past several years, placing significant financial strain on students and creating growing alarm among stakeholders in higher education. In 2004, the typical graduate student cumulatively borrowed an average of approximately $34,500 in federal loans. With the elimination of loan caps, that total doubled to $70,300 by 2020.[2]

The rise in the cost of graduate degrees is particularly concerning when examined in conjunction with the returns some students receive following the completion of their degree. Federal data show that roughly 10 percent of graduate students, or about 72,000

students each year, attend programs that typically leave students earning less than if they had never attended.[3] The higher costs of a graduate degree combined with insufficient returns have left an increasing number of students across programs and institutions with loans they cannot reasonably afford to repay after graduation.

Under current law, student borrowers face no restrictions on the amount of tuition that can be financed with Grad PLUS loans. They are allowed to borrow up to the full cost of attendance minus any other financial aid received. The lack of any loan limits, coupled with institutions' ability to determine the cost of attendance, creates a negative feedback loop: Institutions continuously raise prices unchecked,[4] knowing they can simply rely on students accessing unlimited federal graduate loans. In turn, students borrow more to keep pace with the skyrocketing charges. The harm of this policy is not limited to the almost half of graduate students who borrow: All students, even those who do not rely on loans or receive financial aid, are affected by rising prices.

Graduate borrowing levels could be constrained to more reasonable and appropriate levels in several ways. One of the most simple and straightforward would be to establish an annual maximum and an aggregate lifetime maximum for the Grad PLUS program (as exist for other federal student loans), but policymakers could also consider some combination of the following.

Replace Grad PLUS with Increased Stafford Loan Limits for Graduate Students. The Grad PLUS program could be eliminated, while the loan limits in the Stafford loan program could be increased to some extent. This would simplify federal student lending and allow students to rely on less expensive Direct Unsubsidized Loans (which carry a lower interest rate and lower origination fees), but it would likely further complicate unsubsidized loans by having differential loan terms for certain graduate students (e.g., medical students).

Establish Differentiated or Flexible Limits in Grad PLUS. While continuing the Grad PLUS program, the loan amounts could be capped, but the caps could differ by the credential length and type. The high costs of providing physician training programs, along with the high earnings of most graduates of these programs, might justify annual limits of $50,000 and aggregate limits of $250,000. However, a yearlong graduate certificate might not be eligible for Grad PLUS at all, given the program's relatively low costs, and masters programs might be limited to $20,000 annually and $50,000 overall, respectively. A slightly more complex version would provide different loan limits for individual programs based on factors such as demonstrated earnings sufficient to repay the loans or success in graduating disadvantaged students.

Allocate Loan Funds to Institutions Based on Outcomes. In this approach, colleges would be granted access to loan amounts they could allocate across programs and students, up to a total dollar amount the institution has earned. The amount of additional loan funds would be allocated to the institution based on performance factors such as graduation of Pell Grant recipients, job outcomes, and loan repayment.

Like in the former Perkins loan program, the institution would decide which programs to fund and how much to offer particular students, within certain parameters. Unlike the Perkins program, the loan funds would be managed as Federal Direct Loans (not a separate revolving fund managed by the school). Rather than having an incentive to establish more programs and charge higher prices, as in the current Grad PLUS program, this approach would reward positive student outcomes and encourage institutions to prioritize quality and affordability, including among their own programs.

Pillar Two: Award Grant Aid to Students and Institutions to Address Equity and Social-Good Considerations

The first pillar of our joint proposal, limiting the availability of federal loan dollars, would necessarily have major implications for many low-income students' ability to access graduate and professional degree programs. That's because the private marketplace would not replace all the loans that would have been made under the existing federal program, particularly concentrated at programs leading to lower-paying occupations and at institutions that overwhelmingly serve historically marginalized students.

Some of the lost opportunities for enrollment in graduate study would leave the nation further from our collective goals of ensuring equitable access to

opportunity. Therein lies the potential for bipartisan policy action on grant aid for graduate students.

By eliminating the blanket subsidies inherent in unlimited access to graduate student loans, resources could be freed up to focus on one of the challenges we tend to collectively see as most dire: ensuring that the most disadvantaged people and communities have access to the resources they need to succeed. Examples of targeted, explicit subsidies could include providing grants to the neediest students (such as those who received maximum Pell Grants or whose families have few assets), subsidizing programs of study in fields that are socially valuable but less lucrative, supporting academic pipeline initiatives, and keeping high-quality programs available in rural communities that otherwise would be likely to close.

A new policy for graduate-level subsidies could mimic the ways in which the existing federal aid programs essentially offer student-level subsidies, but lawmakers could also reallocate the savings from constrained borrowing into institutional, community, or even state-level subsidy programs. The nature of the subsidy should be designed to address the nature of the challenge it's trying to solve. Examples of grant aid could include the following.

New Grant Programs for Students. Reducing student loan availability would likely have immediate and predictable impacts on access, persistence, and completion, particularly for economically disadvantaged students. Constraints on federal borrowing paired with an unavailability of credit from private lenders based on lack of credit history, collateral, or cosigners would severely limit graduate opportunities for many students.

While this might be desirable in cases where outcomes after graduation—economic or otherwise—are poor, there may be instances in which policy should provide subsidies that keep certain opportunities within reach. These subsidies could be targeted to students based on their personal situations, such as having received a Pell Grant previously and having low income at present.

Institutional Aid for Socially Valuable Programs of Study. In the same way that some individual students would have their opportunities limited by the constraint on borrowing, some institutions could struggle to maintain sufficient enrollment and revenues with this change. Direct subsidies to institutions could offset this effect, enabling programs that offer social value not necessarily recognized by the private loan marketplace or the labor market to continue to operate. Examples of this include support for institutions serving historically disadvantaged students, such as Historically Black Colleges and Universities or Hispanic-Serving Institutions. Alternatively, subsidies could support programs specialized in training students to work in socially valuable professions.

Aid for Communities Facing Unique Educational-Opportunity Challenges. It is also possible that some portion of the grant-aid offset to constrained borrowing could be delivered to state and local governments, earmarked for use in combating specific educational and workforce challenges facing their population or a specific geography. One example would be government support of programs in rural areas that might not otherwise have the revenue to support continued enrollment. Another would be a state or community using grant aid to build a pool of workers qualified for local jobs that are going unfilled.

Pillar Three: Ensure Sufficient Value and Return on Investment for Students and Taxpayers

In addition to a lack of loan limits, our existing system of graduate financing has effectively no quality-control mechanism. This means that graduate programs that consistently leave their students worse off—deep in debt with insufficient earnings to repay it—can continue participating in the federal loan programs at taxpayer and student expense with no consequences or incentives to improve. For this reason, federal student loans should be available only to students attending programs in which they are generally getting a good return on their investment and there isn't a consistent pattern of taxpayers being on the hook to cover unpaid balances.

Recent research provides strong evidence that there is little relationship between the price of a program and its graduates' lifetime earnings. About 15 percent of graduate programs (1,459 of 9,877) leave students earning less than $50,000 per year, the average annual earnings of bachelor's degree holders four years after graduation. Some institutions leave students owing

debt that most research agrees is unaffordable (more than 20 percent of discretionary income), including 39 percent of nonprofit and 44 percent of for-profit professional degree programs.[5]

At the programs in which this consistently occurs, students are left with insufficient earnings while also being on the hook for huge debt. This debt can significantly limit their economic mobility, preventing them from starting a family or business, hampering wealth accumulation, and creating a financial burden that harms their mental health. When students cannot repay federal loans, taxpayers can be stuck holding the bag. Institutions face no policy incentives to improve and are never held responsible for these unpaid balances. This is a problem that must be addressed at its source by preventing students from taking on loans for graduate programs with consistently poor returns on investment.

There are several ways policymakers could ensure students are not consistently being left worse off.

Establish Minimum Earnings Thresholds for Program Loan Eligibility. The minimum earnings thresholds for students who enrolled in graduate programs, as outlined in the Senate Republican Streamlining Accountability and Value in Education (SAVE) for Students Act,[6] and minimum earnings thresholds for graduates like the Biden administration's gainful employment rule reflect a recognition that students attend graduate school in major part to improve their earnings. The SAVE for Students Act's use of the median earnings of bachelors' degree holders four years after graduation (about $50,000) recognizes that if most students who have enrolled in a graduate program aren't making as much as the average college graduate who never attended postgraduate education, that program is not providing significant financial value to those students.

Ensure Graduate Program Earnings Are Sufficient to Repay Debt, or Lower Program Costs. Similarly, a debt-to-earnings limit (like in the gainful employment rule) would place limits on the amount of unaffordable debt programs are allowed to disburse to their students. Consistently leaving students unable to make enough money to repay five- or six-figure debts should call the value of that program into question.

A price-to-earnings limit would operate by a comparable mechanism, limiting exposure of prospective students to graduate programs that charge exorbitant tuition in exchange for degrees that don't provide solid wages. An advantage of both measures is that institutions can improve their performance by simply lowering the price they charge students.

Apply Consequences Appropriate to Improve the Program and Protect Students and Taxpayers. Depending on the measures included in a return-on-investment system, appropriate consequences would have to apply to provide incentives for improvement. For example, a program with strong earnings but an abysmal completion rate for low-income students might have three years to improve those rates before being limited in the total volume of graduate aid it can disburse. Policymakers could choose among other possible return-on-investment measures (such as minimum completion rates, loan nonpayment rates, and rates of income improvement) and would have to decide how many should be applicable. Choosing more than one measure would prevent gaming an accountability system (a significant problem with the current cohort default rate measure), but each additional measure would add administrative complexity.

Regardless of which measures are chosen, various incentives and consequences could apply to programs that consistently fail such measures. There could be limits on the total number or percentage of federal aid recipients that could enroll in a program, requirements that the institution is responsible for some portion of students' unpaid debt, limits on institutions' grant funding, or discontinuation of the program's eligibility to make federal loans to students. Enforcement of these responsibilities could lie with the Education Department but also with institutional and programmatic accreditors and states.

Pillar Four: Enhance the Regulatory Structure and Consumer Protections for Private Lending

A major goal of introducing borrowing limits in federal loans for graduate study is reducing the incentives that contribute to tuition inflation. Even as states have implemented tuition freezes and caps for undergraduates at public institutions, graduate tuition inflation has increased significantly in recent years to the detriment of students and taxpayers.

Because there are currently no caps on federal graduate loans or graduate program tuition, federal loans for graduate school cover whatever tuition price the institution has established, on top of other student expenses, leaving private lending with a limited role. The lack of any tuition caps has invited administrative bloat and high promotional budgets, spurring the creation and expansion of programs with little to no academic or workforce value.

Targeted grant aid is far preferable to loans for providing access to graduate programs for disadvantaged populations. Traditional credit instruments are generally a poor match for financing graduate program tuition because any anticipated future income that the education may enable is uncertain and often not in the student's control. However, until we refine the graduate financing system and address the need for individual and institutional grant support, students will continue turning to loans and other financial products to fund their education. Our continued overreliance on a debt-financed education system is the reason a safety net is so important in the federal student loan program. Nevertheless, to ensure private lending can provide equitable access to high-value programs, policy could take the following steps to protect students and help provide market certainty.

Allow for Bankruptcy Protections. Even with the expansion of grant aid, restrictions on federal lending will inevitably lead to some increase in private lending activity, necessitating strong consumer protections for private student loan borrowers. First on that agenda should be reclassifying student loans in bankruptcy so they are treated like other consumer debt rather than being in the same difficult-to-discharge category as unpaid child support and taxes.

Prohibit Products that Mislead Students. A second area of attention should be to guard against loan products that create a false impression that they are somehow free or "not a loan," if their repayment is contingent on future income or other factors such as job placement. Financial instruments that falsely claim they are not debt, penalize borrowers for prepayment, or have widely variable or unstated interest can do considerable harm to students. Except in rare circumstances, such products are quite complicated and therefore difficult for students to assess accurately, creating the potential for harm.

Protect Against Insider Lender Arrangements. A third area of attention is the need to guard against institutions and programs funneling students into overpriced financial products. Federal law and, in some localities, state law and regulation prohibit certain types of pay-to-play arrangements between schools and lenders, mandating that institutions with preferred lender arrangements provide certain public disclosures. These rules help protect student borrowers from being steered toward risky, expensive private education credit products. As more students turn toward the private market to finance their graduate education, these protections should be expanded.

One potential benefit of greater private lender involvement in graduate and professional education would be the additional accountability it can provide. A lender is in a better position to analyze the job market in a particular field and judge whether the educational institution is enrolling students who are likely to complete and benefit from the program. However, these factors can create access gaps that may be of concern to policymakers and school officials. Those gaps are best addressed with targeted aid; the lender reactions can assist schools in determining which programs and students might need more grant aid to reduce their need for private loans.

Pillar Five: Improve Data Disclosure and Transparency

Despite recent improvements to the publication of graduate-level data, students still lack basic information about comparable program costs and outcomes. Institutions, accreditors, researchers, and policymakers lack the information needed to understand program outcomes and inform decisions related to graduate programs.

Effective implementation of the targeted policy solutions in the other four pillars is predicated on access to improved data. For example, better program-level data would allow policymakers to set effective loan limits that consider the average costs of programs, ensuring that borrowing is aligned with actual educational expenses. Additionally, more robust data that are disaggregated by

factors such as race, age, and Pell Grant–recipient status would allow for the identification and targeting of financial aid to students and institutions that may be disproportionately affected by new loan limits.

Lastly, increasing transparency on student outcomes will help students make informed decisions about which program is right for them before they enroll, empowering them to optimize their academic and career paths. Therefore, policy must ensure that researchers and policymakers have access to student-level data on important aspects of graduate programs like outcomes, data on tuition costs, enrollment patterns, and more.

Policy changes can promote better understanding of graduate programs, including their cost and outcomes. To do this, policymakers should consider the following strategies.

Collect Additional Data to Ensure the Accuracy of Price and Aid Data. Currently reported data are insufficient to provide students with accurate information on the listed price or the average net price they can expect to pay at each graduate program. These data limitations also make return-on-investment mechanisms that rely on price or aid unworkable.

Increase Access to Existing Data. One substantial improvement to transparency would be wider access to the National Student Loan Data System (NSLDS). NSLDS is administered by the Federal Student Aid Office and contains extensive records on Title IV loans and Pell Grants throughout their life cycle, from administration through repayment. However, access to this information is largely restricted to federal agencies and entities like institutions of higher education and lender agencies. Wider use of the NSLDS by researchers and policymakers would allow for more targeted policy to improve the graduate federal lending system in two ways: A more in-depth understanding of repayment trends among different populations of students would allow for more targeted aid, and insight into trends in loan amounts would aid in the creation of effective loan caps.

Improve Data Collection. As it stands, policymakers, institutions, and researchers lack practical information on important trends such as graduation rates and earnings data. For example, the primary sources of widely available information on graduation rates are the Integrated Postsecondary Education Data System Completions Survey and the National Center for Education Statistics Sample Surveys.

While these surveys provide important data, both have limitations that affect their usability. Most crucial is the inability to compare cohorts of students at specific programs or evaluate outcomes data disaggregated by race or income, rather than making generalized conclusions based on national surveys. In contrast, the College Transparency Act, which is a bipartisan and bicameral bill, would create a privacy-protected student-level data network that would provide comprehensive, publicly available disaggregated student-level data on trends like enrollment and completion, all while lowering the burden on institutions by streamlining the reporting process.

Conclusion

Policymaking is a process that requires compromise, as opportunities to improve a system are designed to balance different values, priorities, and ideologies. This report reinforces the importance of approaching much-needed reforms to the federal graduate student aid programs with an eye to reducing inflated costs, avoiding unpayable debt, and not restricting access and opportunity while also illustrating that a variety of policies could be combined to advance those goals.

Regardless of the specific combination of policy approaches policymakers take with respect to each of the five pillars, policy reform must account for their interdependence. Reforming the graduate financing programs to better serve students and taxpayers requires a balancing of interests. Doing so will necessitate additional support to students and institutions that have need and provide significant value and a system with sufficient data transparency to understand the effects of the policy changes.

The problems with the current federal graduate financing policies are immense, and the opportunity to improve the return on the government's investment in students is significant. It would be prudent for policymakers to address these problems using any number of options within this balanced framework rather than let the current policies continue to create negative incentives.

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Notes

1. Beth Akers et al., *A Framework for Reforming Federal Graduate Student Aid Policy*, American Enterprise Institute, Education Counsel, and Century Foundation, December 8, 2023, https://www.aei.org/research-products/report/a-framework-for-reforming-federal-graduate-student-aid-policy.
2. Tomás Monarrez and Jordan Matsudaira, *Trends in Federal Student Loans for Graduate School*, US Department of Education, August 2023, https://sites.ed.gov/ous/files/2023/08/OCE_GraduateDebtReport202308.pdf.
3. Calculations by the authors using data from US Department of Education, College Scorecard, June 13, 2024, https://collegescorecard.ed.gov/data.
4. See Akers et al., *A Framework for Reforming Federal Graduate Student Aid Policy*, Figures 5 and 6.
5. Monarrez and Matsudaira, *Trends in Federal Student Loans for Graduate School*.
6. Streamlining Accountability and Value in Education for Students Act, S. 1971, 118th Congress, 1st sess. (2023).

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