



RESEARCH REPORT

Reshaping Parent PLUS Loans

Recommendations for Reforming the Parent PLUS Program

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Executive Summary

The use of Parent PLUS loans—federal loans for parents of dependent undergraduates—is increasing, even as student borrowing is declining. Parent PLUS loans were originally designed to provide liquidity to high-asset families who could not cover their expected family contributions (EFCs) with current income. But policymakers have pushed the Parent PLUS program past this original mission. Now, just 38 percent of Parent PLUS loans are equal to or less than the family’s EFC, and loans are too frequently issued to borrowers who cannot repay. Although Parent PLUS repayment outcomes are stronger than student repayment outcomes, some parents struggle with these loans. We argue that stopgap solutions, such as expanding income-driven repayment (IDR) for Parent PLUS borrowers, will only worsen the problem, providing large subsidies to affluent families. We propose returning to the program’s original intent, lending limited amounts to parents who can repay and providing additional financial aid directly to low-income students, rather than to their parents.

Policymakers must develop solutions for current parent borrowers who cannot afford their payments, while restoring stricter provisions for new Parent PLUS borrowers. We recommend that Congress revise the Parent PLUS program to do the following:

- **Limit Parent PLUS eligibility to the parents’ EFC.** PLUS loans should go only to parents who have the means to repay them and should be limited to the parents’ EFC. Other provisions, such as the required check for adverse credit history, should also remain in place.
- **Increase student loan limits for the lowest-income students, whose parents will not have access to PLUS loans.** Dependent students with \$0 EFCs should get automatic access to the independent student loan limits because their families have no ability to help pay for their education. This would provide an extra \$4,000 to \$5,000 a year in unsubsidized loans for undergraduate students and would be payable through IDR plans.
- **Exclude Parent PLUS borrowers from IDR.** Borrowers who use the Parent PLUS loan program moving forward should have access to standard, graduated, and extended repayment options, as well as consolidation. Parent PLUS borrowers should not have access to IDR plans or to forgiveness programs.
- **Hold institutions accountable for Parent PLUS lending.** Institutions that encourage both the parent and the student to borrow should be held accountable for the outcomes of both loans. We recommend that policymakers develop a cohort default rate (CDR) measure for Parent PLUS loans to discourage institutions from pushing parents to rely on PLUS loans and to ensure

that those who borrow repay their loans. The Parent PLUS loan CDR should be separate from the student loan CDR because they are based on different borrowers.

Lax Parent PLUS policies may have put some borrowers in a precarious financial position, and policymakers should provide some relief for these borrowers. We recommend that policymakers allow the following provisions for current Parent PLUS borrowers:

- **Ease restrictions on the discharge of Parent PLUS loans in bankruptcy.** A Parent PLUS borrower has likely reached his or her maximum earning capacity and is unlikely to see substantial increases in income or assets (unlike most student borrowers). Therefore, policymakers could lower the standard for the discharge of current Parent PLUS loans in bankruptcy—which is as stringent as the standard for student loans—without introducing the moral hazard some argue might be present for discharge of student loans.
- **Allow forgiveness of debt for Parent PLUS borrowers with long-term participation in social safety net programs.** Bankruptcy is more common among middle-class earners than among low-income households (Price and Dalton 2007). An additional way of offering relief to current Parent PLUS borrowers would be to allow the discharge of some or all of the debt for borrowers who have relied on a social safety net program, such as the Supplemental Nutrition Assistance Program, for a substantial period (e.g., five years) during repayment. These borrowers have already demonstrated significant financial need and inability to pay down the debt.
- **Permit continued use of income-contingent repayment, after consolidation, for those who borrowed under current rules.** Current Parent PLUS borrowers should not be cut off from their existing option to access income-contingent repayment, with payments set at 20 percent of discretionary income over 25 years, if they borrowed when that option was available. But once the EFC borrowing limit is imposed and ability to pay is added to the credit check, new Parent PLUS borrowers should not be permitted access to this plan.

Reshaping Parent PLUS Loans

Parents are borrowing more every year from the federal government, even as loans to undergraduate students have been declining. Parent PLUS loans rose from 14 percent of total federal lending for undergraduates in 2012–13 to 23 percent in 2017–18. Parents can borrow virtually unlimited amounts through the Parent PLUS program, passing only minimal credit checks. Because of concerns about parents struggling to repay these debts, some policymakers have proposed easing the repayment requirements for Parent PLUS loans. For example, House Democrats' proposed Higher Education Act reauthorization, the Aim Higher Act, would allow Parent PLUS loans to be repaid under generous income-based repayment plans.

In this report, we review the purpose of federal loans to parents of undergraduate students, examine borrowing patterns across parents in different financial circumstances, and consider options for reform. We argue that there should be stricter limits on borrowing and that students from low-income households should have more access to student loans and grants, for which parent loans are not an acceptable substitute. We also make suggestions for relieving the burden on existing parent borrowers who may be unable to support required payments.

Background on Parent PLUS Loans

The federal Parent PLUS loan program enables parents of dependent undergraduates—most students younger than 24—to borrow to help send their children to college.¹ Because federal grants and student loans are capped at specific annual and aggregate amounts, parents often borrow PLUS loans after their students have exhausted their loan eligibility but still face funding gaps. Parent PLUS loans are capped only at the student's cost of attendance, which is the full student budget set by the institution, including not only tuition and fees but room and board, books and supplies, transportation, and indirect expenses critical to academic success. As a result, parents frequently borrow more than students and can accumulate large amounts of debt. The interest rate on PLUS loans (7.6 percent in 2018–19) is higher than the rate for federal undergraduate student loans (5.05 percent in 2018–19). Parent loans also carry higher origination fees.

Unlike federal student loans, which are an entitlement once a student applies for federal aid, Parent PLUS loans require a check for adverse credit history. Parents are either approved or not depending on their credit history. The credit check does not look at a parent's ability to repay, and the absence of

credit history does not count against applicants. To pass the credit check, parent borrowers must not have had debts with a combined outstanding balance greater than \$2,085 (pegged to inflation starting in 2015) 90 or more days delinquent, charged off, or in collections in the past two years. They also cannot have been the subject of a default determination, bankruptcy discharge, foreclosure, repossession, tax lien, wage garnishment, or federal loan debt write-off in the past five years.²

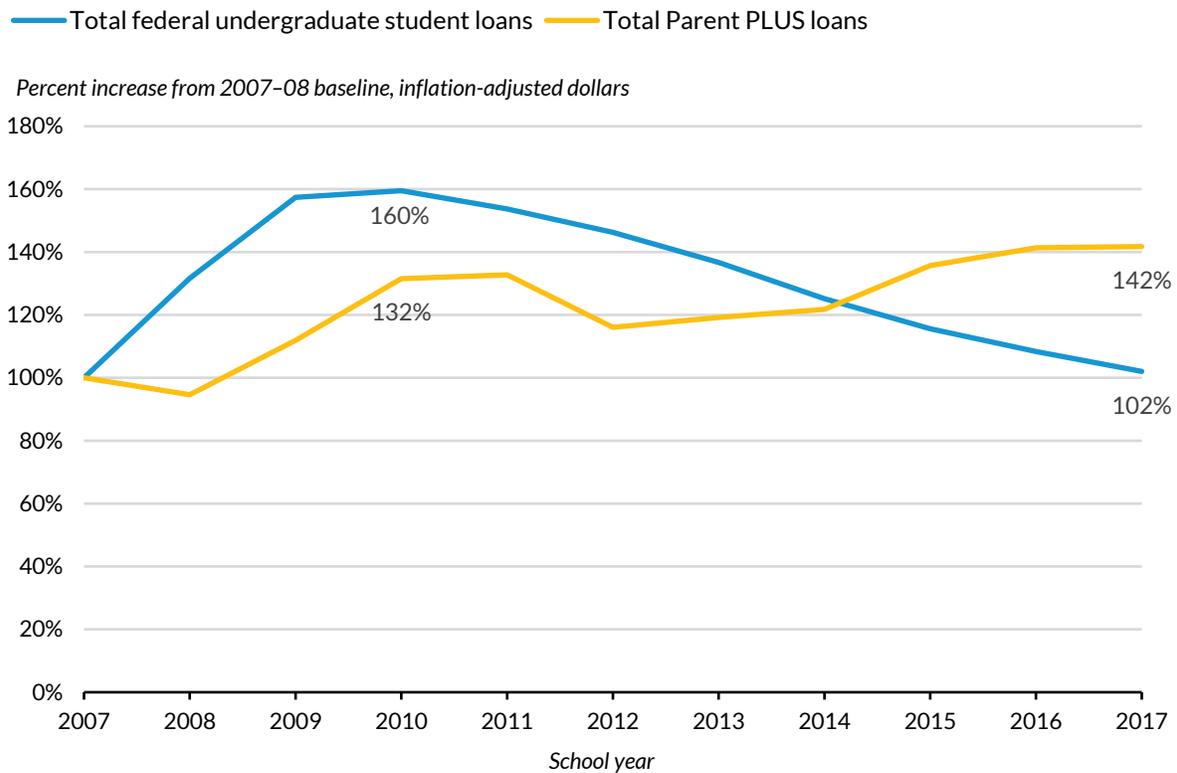
Parents who are rejected for a PLUS loan because of adverse credit history can either obtain an endorser to agree to repay the loan if they cannot or appeal the decision and provide the US Department of Education documentation of extenuating circumstances. If the parents take neither action, their children can borrow up to the independent student loan limit, an additional \$4,000 to \$5,000 a year depending on year of study (FSA 2015).

Like all federal higher education loans, PLUS loans are difficult to discharge in bankruptcy. The government can collect on defaulted debt through wage garnishment, as well as Social Security and tax refund offsets. Parent PLUS loans have traditionally been ineligible for income-driven repayment (IDR) plans. But a regulatory glitch creates an exception when parent loans are consolidated on their own into a federal direct consolidation loan, allowing repayment through one of the oldest IDR plans, income-contingent repayment. It is unclear how many Parent PLUS borrowers use this option.

In 2017–18, the parents of 779,000 undergraduates borrowed an average of \$16,452 in Parent PLUS loans. The total \$12.8 billion in loans under this program represented a 42 percent increase (in inflation-adjusted dollars) over the decade starting in 2007–08, a period during which federal loans to undergraduate students rose by only 2 percent, to \$43.3 billion (Baum et al. 2018).

FIGURE 1

Volume of Parent PLUS and Federal Undergraduate Loans, Relative to 2007–08



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Source: Urban Institute analysis of data from Sandy Baum, Jennifer Ma, Matea Pender, and CJ Libassi, *Trends in Student Aid 2018* (New York: College Board, 2018).

Note: Year indicates fall semester (e.g., 2007 is the 2007–08 school year).

Institutions and Middle-Income Parents Pushed for Parent PLUS Loan Expansion

The Higher Education Act of 1965 initially authorized financial aid, in the form of grants and low-interest loans, targeting low-income students who would otherwise be unable to afford higher education. Just over 10 years later, middle- and upper-income families pushed legislators to expand federal loans to all students. Faced with the squeeze of increasing tuition rates and high-interest loans in the private market, these families wanted access to low-interest financing to help send their children to college. Legislators responded to this need. The Middle-Income Student Assistance Act of 1978 expanded low fixed-interest federal loans to students regardless of their families’ incomes. The act was repealed in 1980 (Cervantes et al. 2005).

The expansion of financing did not stop with low-interest loans for students. The 1980 reauthorization of the Higher Education Act included a loan for parents of dependent students, known

today as a Parent PLUS loan.³ The conference report for the bill reveals that the goal of the parent loan program was to provide liquidity to parents who might not be able to pay tuition up front.⁴ The committee saw the parent loan program as a way to help parents cover their expected family contributions (EFCs), as determined by the federal formula measuring ability to pay. In the committee's words, the Parent PLUS loan "will encourage parents to bear more directly their expected share of a student's educational costs rather than transferring that burden to the student through student borrowing."⁵ The loan was capped at \$3,000 a year (approximately \$10,000 in today's dollars) and had a 7 percent interest rate, lower than prime bank loan interest rates at the time, which ranged from 15 to 20 percent.⁶

The 1992 reauthorization of the Higher Education Act removed the parent loan cap, allowing parents to borrow up to the full cost of attendance less grants and scholarships if they passed a check for adverse credit history.⁷ During various hearings for the reauthorization, many legislators called for increasing the cap on PLUS loans to meet the needs of middle-income families. The idea of removing the cap entirely seems to have originated from the American Council on Education, the head lobbyist for the higher education industry (Butts 1991).

These newly unlimited parent loans were not included in institutional accountability measures for Title IV eligibility, such as the cohort default rate (CDR). This omission made the PLUS loan a no-strings-attached revenue source for colleges and universities, with the risk shared only by parents and the government.

Parent PLUS Loans Carry Consequences for Borrowers, but Institutions Escape Accountability

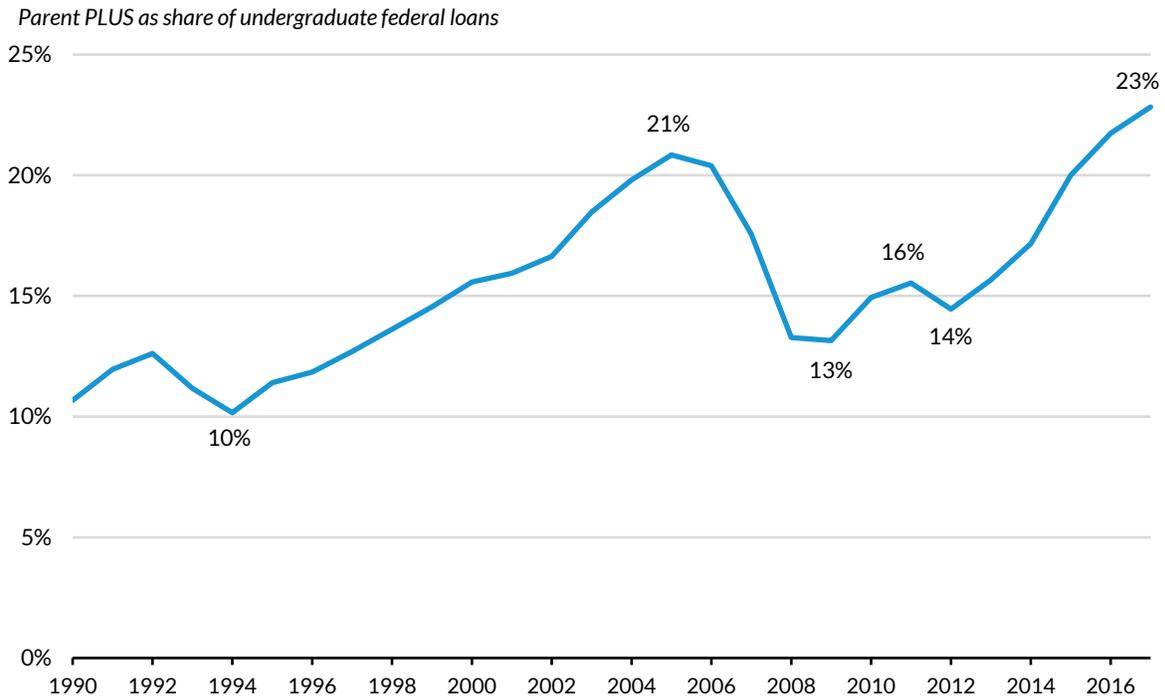
The structure of the Parent PLUS loan program remains largely the same today. Middle- and upper-income families remain the predominant users of Parent PLUS loans, which provide liquidity to pay for high-price institutions. One of the biggest institutional recipients of Parent PLUS loans, for example, is New York University.⁸

But some low- and middle-income students and families have started to rely on the program in ways Congress did not intend. As the Pell grant program has failed to keep pace with rising tuition prices and stagnant family incomes, and as families at all income levels have seen the importance of sending their children to college, low- and middle-income families, and the institutions their children enroll in, have sought alternative financing mechanisms.

In the wake of the 2008 recession, the US Department of Education found that some low-income parents and the institutions that serve them were relying heavily on the PLUS program because of an error in conducting the credit check. The department tightened the adverse-credit criteria in 2011, resulting in a sharp increase in the number of parents rejected for a PLUS loan.⁹ These loan rejections were especially hard on Historically Black Colleges and Universities (HBCUs) and the for-profit sector, which predominantly serve low-income students. The change sent students scrambling, causing enrollment declines and shortfalls in institutional budgets. HBCUs pushed for the Department of Education to loosen requirements for PLUS loans.

The department revisited the credit check for PLUS loans in 2013–14, weakening the eligibility criteria and opening the door for even less creditworthy parents to borrow.¹⁰ This change has contributed to the increase in disbursements of PLUS dollars relative to undergraduate federal loans (figure 2).

FIGURE 2
Parent PLUS Share of Federal Undergraduate Education Loan Disbursements over Time
Loans disbursed to parents as a share of all federal loans to undergraduate students and their parents



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Source: Urban Institute analysis of data from Sandy Baum, Jennifer Ma, Matea Pender, and CJ Libassi, *Trends in Student Aid 2018* (New York: College Board, 2018).

Notes: Year indicates fall semester (e.g., 1990 is the 1990–91 school year). The values for the 2017–18 school year are estimates.

In 2018, in response to concerns about the increase in PLUS borrowing and stories of struggling parent borrowers, the Democratic House bill to reauthorize Higher Education Act, as well as a student loan bill from Senator Jeff Merkley (D-OR), proposed extending the most generous IDR plans to parent borrowers. To better understand the potential distributional and fiscal impacts of such a change, we review the characteristics of parent borrowers in the following sections.

Background on Parent PLUS Borrowers

The characteristics of Parent PLUS borrowers can help us understand who might benefit from more lenient repayment policies and who might borrow more through the program if the rules or repayment plans for these loans were to change. In this section, we look at which parents borrow PLUS loans, the repayment outcomes for Parent PLUS loans, and the income and assets that these borrowers have as they repay these debts. We anticipate that the benefits of widespread access to more generous safety nets for repaying these debts would accrue primarily to parents in the upper half of the income distribution.

Parents Whose Students Maxed Out Their Loans Are Most Likely to Borrow PLUS Loans

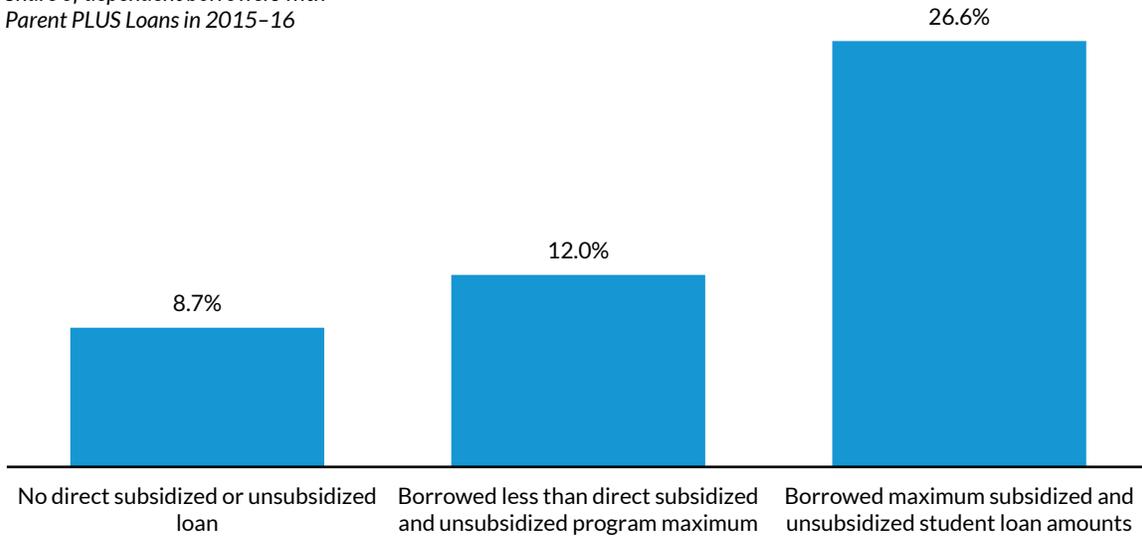
Dependent students who borrow the maximum amount of loans allowed are more likely than others to have parents who also borrow. Parents appear to use PLUS loans to help fill the gap between the aid a student receives (both grants and loans) and the cost of attendance. Of dependent first-year students who borrowed all they were eligible for in direct loans in 2015–16, 28 percent had parents who borrowed PLUS loans (figure 3).

FIGURE 3

Share of Dependent Students Whose Parents Borrow PLUS Loans

Among first-year students in the 2015–16 academic year

Share of dependent borrowers with Parent PLUS Loans in 2015–16



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Source: Urban Institute analysis of 2015–16 National Postsecondary Student Aid Study data using National Center for Education Statistics PowerStats table bkabmpabb.

Notes: Students are categorized as first-year for the purpose of applying for student financial aid. Our data exclude students who attended more than one institution in 2015–16 and those who are not citizens.

Parent PLUS loans are most common among families whose students are enrolled in private institutions. Eighteen percent of parents of dependent students starting at private nonprofit colleges and universities and 16 percent of those at private for-profit institutions took Parent PLUS loans in 2015–16, compared with 4 percent at public institutions.¹¹

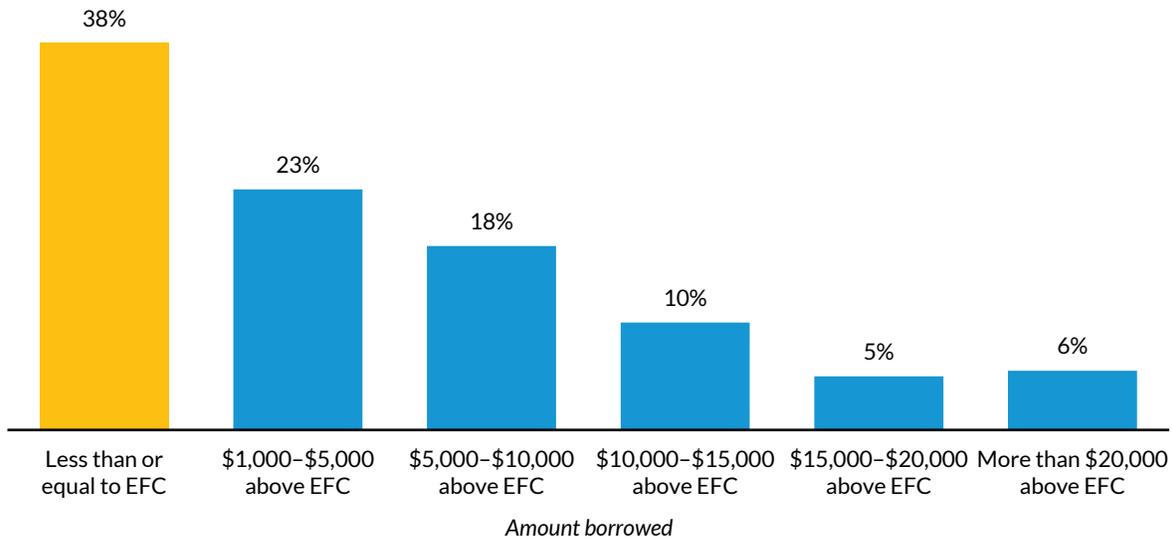
Although the program’s intent was to allow families liquidity to cover their expected family contributions, we estimate that 62 percent of Parent PLUS borrowers in 2015–16 borrowed more than their EFC. Twenty-three percent of Parent PLUS borrowers took out a loan that was less than \$5,000 above their EFC for the 2015–16 school year, but 11 percent of Parent PLUS borrowers in 2015–16 took out a loan that was more than \$15,000 higher than their EFC (figure 4). Households that are taking on these large debts—in a single year of their child’s education—are unlikely to be able to repay this debt.

FIGURE 4

Share of Parent PLUS Borrowers Borrowing More Than Their Calculated EFC

Among students in the 2015–16 academic year

Share of Parent Plus borrowers



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Source: Urban Institute analysis of 2015–16 National Postsecondary Student Aid Study data.

Note: EFC = expected family contribution.

Parent PLUS Borrowers Have Higher Incomes and More Assets than Nonborrowers

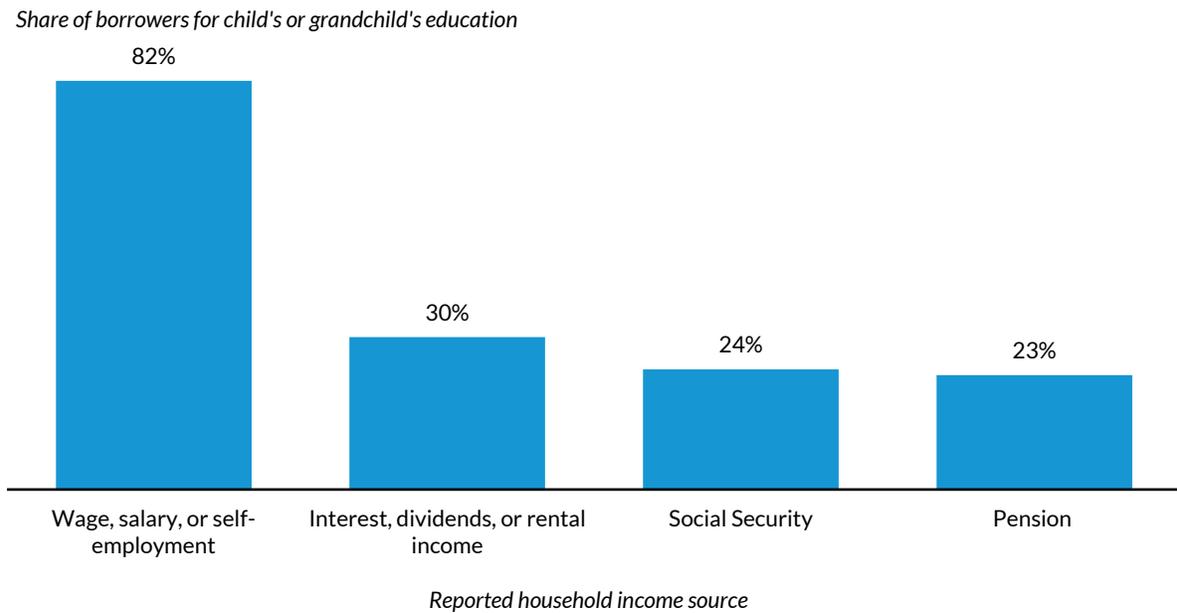
High-income, wealthy families are more likely than those with low incomes and less wealth to borrow Parent PLUS loans. Among the families of dependent first-year students in 2015–16, 30 percent of those with household incomes above \$100,000 took out Parent PLUS Loans, while just 16 percent of families with incomes below \$20,000 used these loans.¹² High-income families tend to take out larger loans as well. The median first-year PLUS loan amount was about \$7,000 for households with incomes below \$20,000 but \$17,850 for households with incomes above \$100,000.¹³ In 2015–16, about 40 percent of Parent PLUS dollars went to the 25 percent of parents in the highest income quartile.¹⁴

To understand the overall cohort of parent borrowers, we use data from the Survey of Household Economics and Decisionmaking (SHED) to look at the incomes and wealth of household heads who are currently paying off debt they took for children’s or grandchildren’s education. This debt includes not only Parent PLUS loans but private loans. If a parent borrower has a strong credit score, the interest rate on a private student loan may be lower than the rate on a Parent PLUS loan. But if the government

eases repayment requirements on Parent PLUS loans, parents who opt for a private loan may instead choose Parent PLUS loans to take advantage of additional borrower protections.

With the SHED, we observe the current sources of income for those who have borrowed for their children or grandchildren. Eighty-two percent of households report earning some money through employment, and 30 percent report additional income from investments. Roughly 22 percent of borrowers consider themselves retired, and a similar share report earning Social Security or pension income (figure 5). In other words, some parents in retirement are paying off debt they accrued for their children’s education.

FIGURE 5
Household Income Sources for Parent or Grandparent Borrowers
Share of adults with a student loan for child or grandchild reporting each source of income



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Source: Urban Institute analysis of 2016 and 2017 Survey of Household Economics and Decisionmaking data.

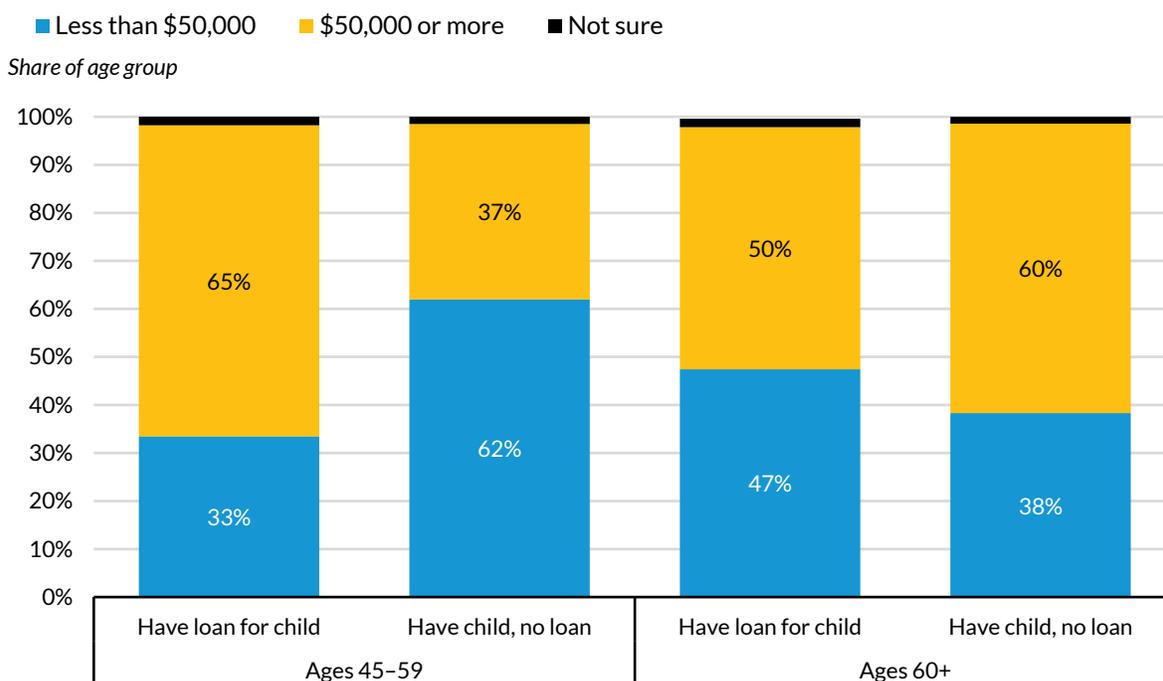
Note: Respondents were asked about any student loans owed from a child’s or grandchild’s education, which could include private or nonfederal loans.

About a quarter of borrowers who have not yet paid off their parent loans are close to or beyond retirement age. Sixty-one percent of those holding an education loan for a child or grandchild are ages 45 to 59, while another 25 percent are 60 or older.

Although we might assume that parents with minimal savings would take loans to pay for their children’s education, there is not a consistent relationship between savings levels and holding parent

loans. Parents ages 45 to 59 who hold parent loans are nearly twice as likely to have at least \$50,000 in savings and investments as parents who do not hold parent loans. But among parents 60 and older, those who hold debts for their children’s education have slightly less in savings and investments than parents without these debts; in 2016–17, half of these older borrowers still had at least \$50,000 in savings and investments (figure 6). The relatively high asset levels of the 45-to-59-year-old debt holders suggest that, in the aggregate, parents with the lowest asset levels are not the ones borrowing to fund their children’s education. The available data do not reveal whether those not holding education debt never borrowed or have already paid off the debt. The different pattern among older debt holders may indicate that parents with more resources are most likely to pay off their debts in a timely manner.

FIGURE 6
Savings and Investments Held by Parents with and without Parent Loans
Total savings and investments by age cohort



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Source: Urban Institute analysis of 2016 and 2017 Survey of Household Economics and Decisionmaking data.

Note: Respondents were asked about any student loans owed from a child’s or grandchild’s education, which could include private or nonfederal loans.

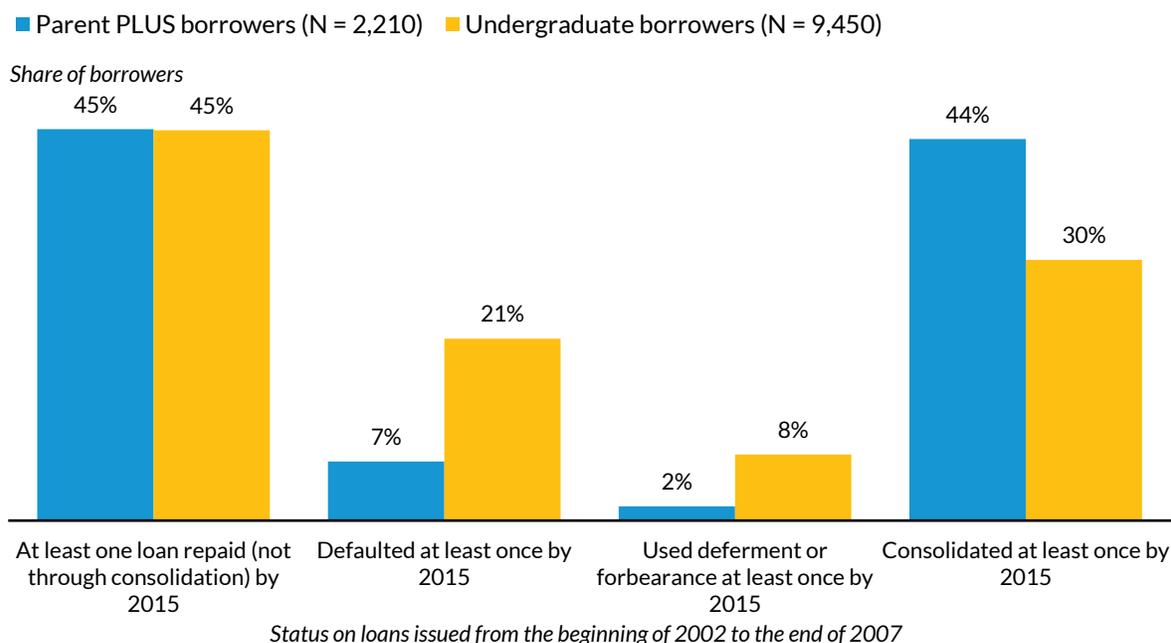
Parent PLUS Loans Have Lower Default Rates, but Gaps in Default Remain

Parents pay off their education loans more successfully than students. This pattern is not surprising because student loans do not require even the weak credit checks required for parent loans. Of Parent PLUS borrowers whose children started postsecondary education in 2003–04, only 7 percent defaulted on any of these loans by 2015. In contrast, the default rate of undergraduate students who first enrolled in 2003–04 was 21 percent. Parent PLUS borrowers are less likely to use deferment or forbearance but are more likely to consolidate their debt (figure 7). When parents consolidate—combine multiple student loans into a single loan to simplify payments, reduce interest rates, or access other repayment plans—we can no longer track repayment outcomes in the National Postsecondary Student Aid Study data. However, our estimated default rate is consistent with another study, based on data for students attending Texas institutions, which finds that the default rate for Parent PLUS loans over a similar period was 8.6 percent (Di, Fletcher, and Webster 2018).

FIGURE 7

Student Loan Outcomes for Parent PLUS and Undergraduate Borrowers

For undergraduate students who began college in the 2003–04 school year



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Source: Urban Institute analysis of 2004–09 Beginning Postsecondary Students Longitudinal Study data.

Notes: Weighted using WTA000, results show the share of borrowers who experienced a given outcome (e.g., a borrower who used forbearance and then defaulted would appear in both columns). “Undergraduate borrower” debt reports borrower status only on undergraduate loans.

But disparities in repayment of Parent PLUS loans echo disparities for loans issued to students. The default rate among parents of black students was 20 percent, compared with 5 percent for parents of white students. Similarly, parental wealth appears to play a role. Among those who owned a farm or business or had other investments worth more than \$10,000 combined, the default rate was lower (5 percent versus 8 percent). In addition, the default rate for Parent PLUS loans for private for-profit institutions was 16 percent, compared with 6 percent for private nonprofits and 5 percent for public institutions. The sectoral patterns in these data echo data published by the Department of Education for fiscal years 2005 to 2010 (Di, Fletcher, and Webster 2018) and highlighted in a recent Brookings Institution report.¹⁵

The Weak Logic for Easing Parent PLUS Repayment Terms

The data on current Parent PLUS borrowers and households holding education debt for their children reveal that affluent families disproportionately take advantage of parent loans for higher education. But some parents borrow through this program even though they are unlikely to be able to repay. Some parents may be close to retirement age when they take out PLUS loans. Others have low incomes and limited access to private student loans but are eager to expand their children's educational opportunities and see PLUS loans as their best or only option.

Calls to loosen repayment terms for parent loans, such as offering more generous IDR options, emerge from concern for parents facing repayment challenges. In this section, we focus on the logic behind the use of programs such as IDR for student borrowers and on the potential unintended consequences of applying this policy to parents, which may be wide reaching.

Student Loans Increase Access, and Parent Loans Provide Liquidity

Students are encouraged to borrow to invest in their futures. Because this is an investment with a high average rate of return, but with considerable risk, some students who would benefit from continuing their education may decide against it, limiting their future opportunities. Federal student loans and accompanying IDR options support access for underresourced students and improve the efficiency of the postsecondary education market, which is unlikely to provide them access to credit on good terms.

Parent loans, in contrast, were designed to increase the financing options available to parents whose assets and long-term resources will support the education payments they cannot immediately make out of pocket. These loans are not available to parents in the most precarious financial situations because they involve a minimal credit check. These education loans will not increase future earning opportunities for parents the way they do for students. Providing these loans to parents who are unlikely to be able to repay them is a poor substitute for providing the grant funding their children need to access meaningful educational opportunities.

Income-Driven Repayment Insures against Uncertain Returns from Education

For decades, economists from various ideological perspectives have advocated for basing student loan repayment obligations on borrowers' incomes, but this logic does not extend to parent loans. From the right, in 1955, Milton Friedman wrote in "The Role of Government in Education" about the underinvestment in human capital resulting from capital market imperfections and the lack of collateral to support loans for education. Friedman noted that despite the high expected return to investments in education, there is considerable variation across individuals.

Friedman's proposed solution was to "buy a share in an individual's earning prospects: to advance him the funds needed to finance his training on condition that he agree to pay the lender a specified fraction of his future earnings. In this way, a lender would get back more than his initial investment from relatively successful individuals, which would compensate for the failure to recoup his original investment from the unsuccessful" (Friedman 1955, 10). Of note for current IDR policy discussions, Friedman suggested that loan payment could easily be combined with payment of income taxes and so involve a minimum of additional administrative expense.

From the left, James Tobin, also a Nobel Prize-winning economist, was an architect of Yale University's experiment with income-based student financing (Buiter 2003). Australia, England, and New Zealand implemented income-based student loan programs in the 1980s and 1990s, and the US has had IDR schemes since 1994 (Barr et al. 2017).

Support for IDR for student loans also emerges from efforts to define manageable student debt levels. Evaluating potential approaches to setting benchmarks for how much former students can reasonably afford to repay, Baum and Schwartz (2006) argued that high-income borrowers can manage payments that are a higher percentage of their incomes than is reasonable for low-income borrowers. The parameters developed based on the evidence about manageable payments reviewed in this study contributed to the design of the original income-based repayment plan.

Some of the variation in higher education returns is predictable. Students studying early childhood education are not likely to earn as much as those majoring in engineering. Students with low high school grade point averages enrolling in open-access institutions are more vulnerable to not completing their programs than are high-achieving students attending selective colleges and universities. But even for individual students, outcomes are uncertain. Medical problems or other life circumstances derail plans. Some will find that economic realities have diminished opportunities in their chosen professions. IDR offers insurance against these unanticipated outcomes.

The goal of IDR and similar programs is to provide a safety net for students whose education does not work out as planned. For many, the problem is not inadequate earnings over their work lives but the timing of those earnings. If college graduates take time to settle into their careers, they may struggle with payments early on but have greater capacity to pay as they follow typical earnings paths. As advocates for a well-designed IDR program for student loans have noted, “We have a repayment crisis because student loans are due when borrowers have the least capacity to pay. Student borrowing is not excessive given the lifetime payoff to a college education, but current practice is for loans to be repaid during the first 10 years after college. It often takes years for college graduates to settle into a steady, higher-paying job that reflects the value of their education” (Dynarski and Kreisman 2013, 6).

The logic of student loans is that the investment in higher education leads, on average, to higher earnings. Students have limited resources before and during college but can use a portion of their future earnings to repay their loans.

Parent Borrowing Should Not Qualify for the Insurance IDR Offers

The logic for making payments based on income does not carry over from students to parents. Forgiving unpaid balances after a number of years of payments if incomes have not been high enough to support retirement of the entire debt is similarly inapplicable. Providing repayment insurance against low parent incomes in the future would be an ill-founded public policy.

Why should parents borrow to pay for their children’s education? Education is one of the largest expenditures families face. Just as they borrow for home purchases, it is reasonable for families to spread payment for education out over time, rather than financing it entirely from current income during the college years. Saving in advance for this predictable expense has clear advantages, but there is no reason that education payments should not include the postcollege years, especially because parents reasonably expect their expenses to decline once their children are financially independent.

The two components of IDR programs that are most helpful to borrowers are the flexibility of payment timing and the forgiveness of remaining balances after a fixed number of years. Parents' income paths are different from those of recent students. Parents' incomes are not interrupted by their children's college enrollment and do not increase because of that enrollment. All income paths are subject to unforeseen variation, and parents can run into difficulties with education loans just as they can with mortgages or car payments. But parents are better able to predict and plan for repayment than are students, and education loans are not in a separate category from any other debt these borrowers hold.

Most of the small share of parents who struggle with PLUS loan repayment likely could have predicted that struggle at the time they took out the loans. Although Parent PLUS loans were designed to help finance expected family contributions, these loans are often used to fill in the gaps left by financial aid packages. Some parents reasonably want to stretch their payments out over a longer period by making some of the payments after their children complete college. But it is probably wishful thinking for parents to expect that their incomes will increase dramatically after their children complete college, making payments that were somehow impossible before college feasible.

Promising Forgiveness for Unpaid Parent PLUS Loan Balances Will Yield Unintended Consequences

Allowing parents to take advantage of programs that involve reduced payments and forgiveness of unpaid balances after a fixed number of years has a clear problem of “adverse selection” into the program because of loosened repayment terms. Parents who plan to retire soon will be particularly drawn to loans that allow them to lower or avoid payments when their incomes predictably fall. In a market-based loan program, the problem here would be that the borrower would have information not available to the lender. But in the Parent PLUS program, even if this knowledge were available to the government, it would not change the loan's availability or terms. Parents who expect their incomes to remain steady or to increase will be less drawn to PLUS loans with the IDR option than those who expect their incomes to decline. Adverse selection into the program will lead to lower repayment rates than would prevail if all parents were equally likely to opt into the program.

There is also a “moral hazard” problem. Because such a system would protect parent borrowers against the risk of declining income that would make payments unaffordable, they would have less motivation to maintain their current incomes. They would have greater incentive to retire or otherwise allow their incomes to decline, in addition to seeking ways to shelter their income from the system. They

would not be at risk of becoming delinquent on their loans because of their diminished resources. And they would have the opportunity to benefit from the loan forgiveness provision of IDR, which would subsidize them only if their incomes were not high enough to support full repayment of their debts.

Unlike loans to low-income students who borrow, Parent PLUS loans do not support investments in parents' future earnings. If the government is going to subsidize low-income parents who are unlikely to repay their loans, it should do so through grants at the time of college entrance, not by forgiving loans later on.

Increasing the Generosity of Parent PLUS Repayment Plans Would Substantially Reduce Repayment

Parent PLUS borrowers do not have access to IDR. The exception is income-contingent repayment, which reduces payments to 20 percent of discretionary income, with any remaining balance forgiven after 25 years. Because of an oversight in developing the regulations, some Parent PLUS borrowers can access this plan after consolidating their loans.¹⁶ To understand how repayment could change under more generous IDR plans, we build a simple model of the optimal repayment choices for a representative cohort of Parent PLUS borrowers whose dependent students completed their education in the 2015–16 school year, estimating which parents would face lower lifetime repayment amounts under these plans.

We use data on actual PLUS borrowers to estimate the potential increase in program participation that might result from allowing parents to enroll in IDR, relying on a set of assumptions to obtain a lower-bound estimate for the number of parent borrowers who would benefit from IDR (box 1). For example, we assume that parents continue working and maintain their incomes for 20 years, rather than retiring or otherwise modifying their behavior. Because of data limitations, we can conduct this analysis only for students who are completing their degrees as dependent students. We exclude students who did not complete their degrees or who completed their studies as independent students. If parents of these excluded students are more likely to have higher debt relative to income, our estimate of the share who would benefit from IDR is likely lower than the actual amount.

BOX 1

Assumptions for Modeling Parent PLUS Repayment under Income-Driven Repayment

Repayment plan assumptions

- We model three generic income-driven repayment (IDR) plans, estimating repayment at 20, 15, and 10 percent of discretionary income, defined as adjusted gross income above 150 percent of the federal poverty level for the parents' household size.
- We compare total payments under each IDR plan with total payments under a standard 10-year plan. If the total repayment amount is lower under IDR than under a standard 10-year plan, we assume that the borrower will use the plan. We use undiscounted payment streams, reducing the calculated benefit of extending payments over a longer period (compared with discounted payment streams). This choice contributes to our underestimation of the benefits of IDR because borrowers facing the same total repayment amount over a longer period should opt into the longer period available under IDR.

Borrower assumptions

- We assume that the borrower maintains the adjusted gross income reported on the 2014 Free Application for Federal Student Aid. We inflate this income by 2 percent each year.
- We use the borrower's household size in 2014 and impute a decreasing household size for the next 20 years.
 - » We assume that the dependent student leaves the household in 2016.
 - » We assume that married couples stay married and that cohabitating unmarried couples file separately.
- Using imputed household size and adjusted gross income, we calculate income above 150 percent of the federal poverty level, using the actual poverty levels for 2014–19 and then inflating the 2019 levels by 2 percent each year.

Even under these lower-bound estimates of IDR take-up, we find that the share of Parent PLUS borrowers who would opt into an IDR plan would increase substantially as the program's generosity increased. We estimate that 16 percent would take up the 20 percent plan (which, with 20 rather than 25 years of repayment, is more generous than the current income-contingent repayment plan to which Parent PLUS borrowers have access). This increases to 18 percent at 15 percent of discretionary income and 22 percent at 10 percent of discretionary income. Again, although these estimates assume that all borrowers opt into the IDR plan if it results in lower total payments, these estimates could be

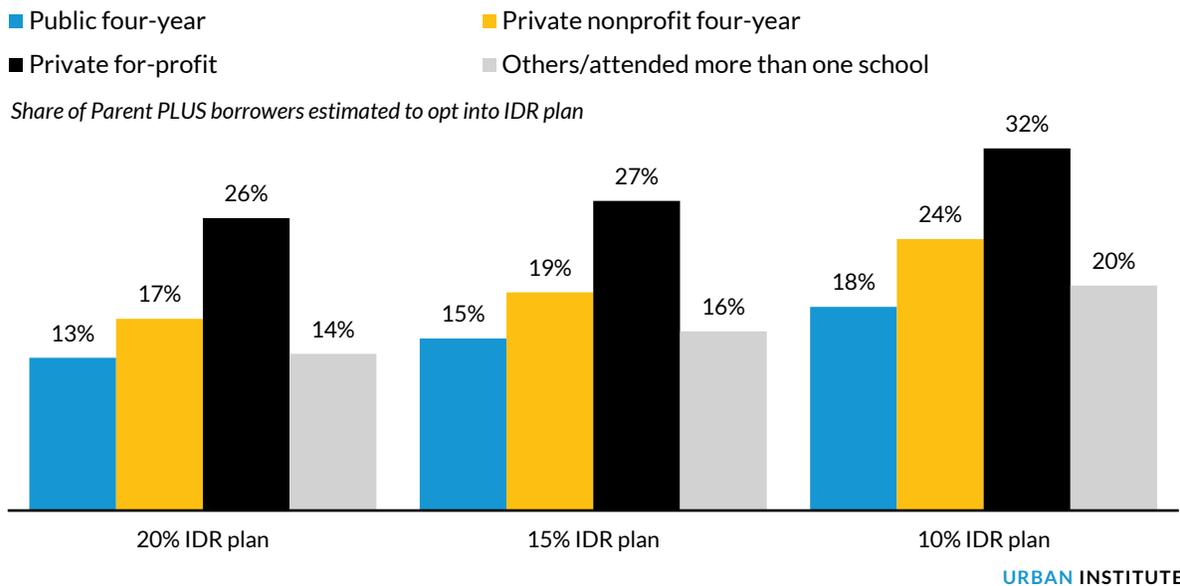
conservative estimates, as borrowers may modify both their borrowing and earning behavior to increase their eligibility for the benefits of these programs, particularly loan forgiveness.

One of the more striking results is the difference in the projected use of IDR by the type of school attended. Parents of students who attended for-profit schools would have the highest IDR use, with about a third of borrowers estimated to opt into a generic 10 percent IDR plan (figure 8). In contrast, 18 percent of parent borrowers with students attending public four-year schools and 24 percent of those who borrowed to send their children to private nonprofit four-year schools are estimated to take up the 10 percent IDR plans.

FIGURE 8

Estimated Use of Hypothetical IDR Plans

For Parent PLUS borrowers whose dependent children completed their degrees in 2015–16



Source: Urban Institute analysis of 2016 National Postsecondary Student Aid Study data.

Note: IDR = income-driven repayment.

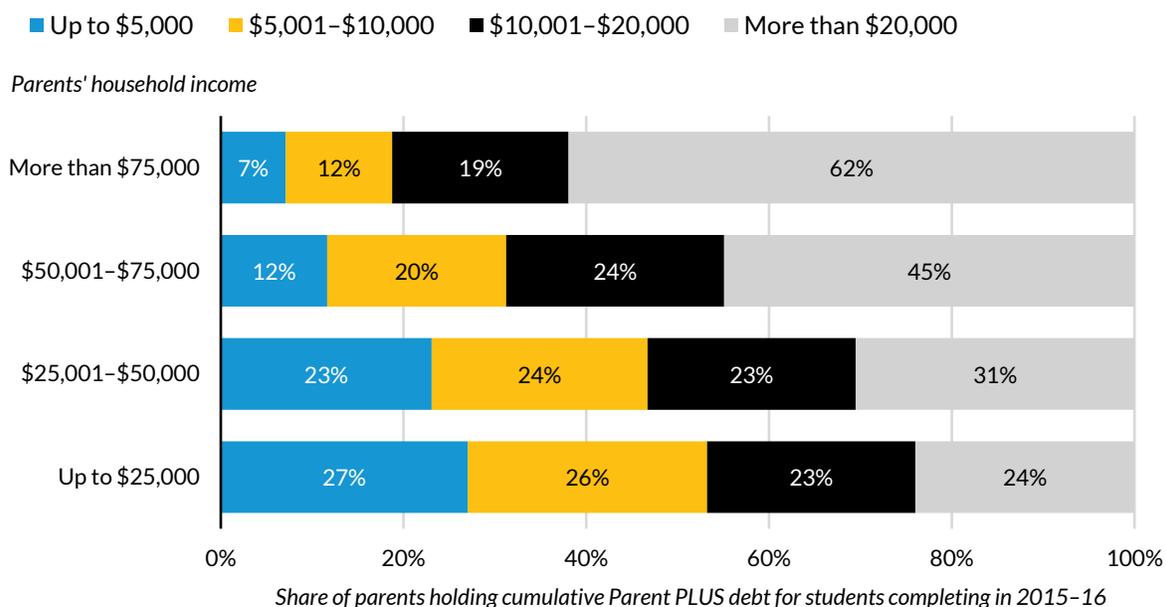
This back-of-the-envelope calculation is likely a substantial undercalculation of the true number of borrowers who would benefit from IDR for Parent PLUS loans. First, current Parent PLUS borrowers might change their earnings behavior if they could use this program, something we do not account for. Borrowers might choose to retire earlier or reduce their incomes through other means, such as part-time work. Because these parent borrowers likely have already reached their peak earning years (and are less likely to anticipate large expenses, such as buying a house or raising children), it is likely that some fraction could and would modify their behavior in this way.

Aside from the behavior of current Parent PLUS borrowers, policymakers should be concerned with future borrowers who may take out more debt because of IDR options. If parents know that their incomes will be low, they have an incentive to overborrow because under these plans, the total amount repaid before forgiveness is the same regardless of the amount borrowed. Some parents might even take on all the debt their children might otherwise incur. Under the current system, parent borrowing appears to be kept in check by the repayment requirements. Among parents who borrowed, 24 percent of those earning up to \$25,000 a year had more than \$20,000 in Parent PLUS debt when their children completed their credentials in 2015–16, while 62 percent of parent borrowers earning more than \$75,000 had more than \$20,000 in debt (figure 9).

FIGURE 9

Distribution of Parent PLUS by Parent Income

For Parent PLUS borrowers whose dependent children completed their degrees in 2015–16



URBAN INSTITUTE

Source: Urban Institute analysis of 2016 National Postsecondary Student Aid Study data.

The result of allowing Parent PLUS borrowers to enroll in IDR would likely be that many participants would receive large subsidies, creating an enormous cost to the government and imperiling the program’s long-term viability. Although expanding IDR to PLUS loans is meant to help low-income families, the high-income families who are already the predominant borrowers of the Parent PLUS program would be the main beneficiaries. Think, for example, of former Maryland governor Martin O’Malley, who borrowed over \$300,000 in PLUS loans to send his children to college. Under the

generous repayment terms of IDR, O'Malley would see a reduction in total payments and would likely receive forgiveness, even though his family is wealthy. Under the current system, with no fixed limit on borrowing, nothing would prevent wealthy families from borrowing the full cost of attendance for their children, increasing the chances that some of their debt would eventually be forgiven.

Institutions would be motivated to encourage low-income families to borrow the full amount because nonrepayment would no longer be an issue. The Parent PLUS loan would become a complicated grant for the families of dependent low-income students who could pass the credit check. Low-income students do not need a complicated backdoor grant that is really a loan. Instead, they need targeted grant aid.

Recommendations for Reform

As policymakers consider revising the Parent PLUS program under the reauthorization of the Higher Education Act, they must think about how to shape the program for the future and how to provide equitable and fair repayment options for those who already have Parent PLUS loans. We divide our recommendations by these two goals.

Revisions to Parent PLUS Lending Policy and Accountability

The principle underlying our recommendations is that aid should go primarily to the students enrolling in higher education. Federal financial aid programs, particularly grants and income-based loan forgiveness, increase overall investment in human capital and protect students when their individual investments do not work out. Loan forgiveness amounts to a grant after the fact. For students, the policy provides subsidies to students whose education did not pay off as planned. There is no reasoned argument for providing a similar subsidy for parents whose incomes do not support repayment of the entire amount they borrowed to help fund their children's education. We recommend that Congress revise the Parent PLUS program to do the following:

- **Limit Parent PLUS eligibility to the student's EFC.** This recommendation brings the Parent PLUS program back in line with its original intent of providing liquidity to families with high EFCs because of substantial asset accumulation. This limitation would ensure that PLUS loans go only to parents who have the means to repay the debt. Other provisions, such as the required check for adverse credit history, should also remain in place.

- **Increase student loan limits for the lowest-income students.** Dependent students with \$0 EFCs should get automatic access to the independent student loan limits because their families cannot help pay for their education. This would provide an extra \$4,000 to \$5,000 a year in unsubsidized loan for these students, which would be payable through IDR plans and for which other benefits would be available. In addition, Congress should expand the Pell grant program to meet the financing needs of low-income families, including those attending HBCUs and other institutions where parents currently rely disproportionately on PLUS loans.
- **Exclude Parent PLUS borrowers from IDR.** Borrowers who use the Parent PLUS loan program moving forward should continue to have access to standard, graduated, and extended repayment options. Parent PLUS borrowers should not have access to IDR plans, nor to specialized forgiveness programs (e.g., Public Service Loan Forgiveness).
- **Hold institutions accountable for Parent PLUS lending.** Institutions that encourage both the parent and the student to borrow should be held accountable for the outcomes of both loans. Parent PLUS loans are not tracked in the current measure used for assessing institutional eligibility for student loans, the cohort default rate (CDR). First, Congress and the Department of Education should produce and publish data on each institution's Parent PLUS default and repayment rates. These data will provide critical insights to Congress on how best to measure and hold accountable schools where parents borrow PLUS loans and discourage institutions from pushing parents to rely on PLUS loans. The PLUS loan CDR should be separate from the student loan CDR because they are based on different borrowers. Without the IDR option for parents, the default rate will be a more reliable benchmark for parent loans than for student loans.

Revisions for Current Parent PLUS Borrowers

Even as we recommend changes for the future of Parent PLUS lending, we cannot ignore existing Parent PLUS borrowers who are struggling to repay their loans. Current lax Parent PLUS policies may have put some borrowers in an untenable financial position, and policymakers should provide a measure of relief to these borrowers. We recommend that policymakers allow the following provisions for current Parent PLUS borrowers:

- **Ease restrictions on the discharge of Parent PLUS loans in bankruptcy.** The arguments for loosening the current limited options for discharging parents' education loans in bankruptcy proceedings are even stronger than the arguments for similar provisions for students. A Parent

PLUS borrower has likely reached his or her maximum earning capacity and is unlikely to see substantial increases in income or assets (unlike most student borrowers). Policymakers could lower the standard for the discharge of Parent PLUS loans in bankruptcy without introducing the moral hazard some argue might be present for discharge of student loans.

- **Allow forgiveness of debt for Parent PLUS borrowers with long-term participation in social safety net programs.** Bankruptcy is more common among middle-class earners than among low-income households (Price and Dalton 2007). An additional way of offering relief to current Parent PLUS borrowers would be to allow the discharge of some or all of the debt for those who have relied on a social safety net program, such as the Supplemental Nutrition Assistance Program, for a substantial period (e.g., five years) during repayment. These borrowers have already demonstrated significant financial need and inability to pay down the debt.
- **Permit continued use of income-contingent repayment, after consolidation, for those who borrowed under current rules.** Current Parent PLUS borrowers should be allowed access to income-contingent repayment, with payments set at 20 percent of discretionary income over 25 years, if they borrowed when that option was available. But once the EFC is added to the credit check, new Parent PLUS borrowers should not be permitted access to this or any other IDR plan.

Conclusions

A federal loan program for parents is designed to provide liquidity for parents who can afford the loan payments over time but have difficulty coming up with the money for college when it is due. Unlike grants and loans for students, Parent PLUS loans are not a tool for ensuring access to college for those with limited resources. Lending to these families, particularly in large amounts, only postpones and worsens their financial hardship.

As the federal government strengthens aid programs for students, increasing the resources available to them, it should reform the Parent PLUS program, reducing or eliminating loans made to parents who are unlikely to be able to repay and providing support for those currently facing insurmountable barriers to meeting their obligations. Policymakers should avoid provisions that direct subsidies to families with significant means, who are more likely than low-income parents to participate in the Parent PLUS program.

The current lax restrictions on Parent PLUS borrowing—both in terms of the financial strength required to access the program and the amounts parents can borrow—invite problems. Parents should not be able to borrow more than the amount they are expected to be able to contribute each year to their students' education. Students with limited family resources should receive more grant aid or increased access to student loans instead of parent loans. These changes should reduce the number of parents in the future who struggle with these loans. Meanwhile, it should be easier to discharge current parent loans in bankruptcy and eventually forgive the debts of those experiencing long-term financial difficulty.

Expanding IDR options to parents would be an illogical policy likely to increase program participation and cause a decline in repayment rates. Unlike students, parents are not investing in their futures when they pay for higher education. Many have good reason to believe their incomes will decline in the future, and the federal government should not take responsibility for their loans in the event of that predictable circumstance.

Notes

- ¹ Undergraduates younger than 24 are not considered dependent for financial aid purposes if they are married, have dependents of their own, are active-duty military or veterans, are orphans, or have been in foster care, wards of the court, emancipated minors, or unaccompanied homeless youth. See the “Am I Dependent or Independent?” section of “Dependency Status,” US Department of Education, Office of Federal Student Aid, accessed March 27, 2019, <https://studentaid.ed.gov/sa/fafsa/filling-out/dependency#dependent-or-independent>.
- ² Rachel Fishman, “Education Department Publishes Final Rule on PLUS Loans,” *EdCentral* (blog), New America, October 22, 2014, <https://www.newamerica.org/education-policy/edcentral/education-department-publishes-final-rule-plus-loans/>.
- ³ In most circumstances, a dependent student is a student younger than 24 who is pursuing an undergraduate credential. A student is usually considered dependent, regardless of whether a parent plans to help pay for college.
- ⁴ Education Amendments of 1980, S. 1841, 96th Cong. (1979–80).
- ⁵ Education Amendments of 1980, S. 1841, 96th Cong. (1979–80).
- ⁶ “Bank Prime Loan Rate Changes: Historical Dates of Changes and Rates,” Federal Reserve Bank of St. Louis, last updated October 23, 2018, <https://fred.stlouisfed.org/series/PRIME>.
- ⁷ Full cost of attendance includes not only tuition and fees but room and board, books and supplies, transportation, and other related educational expenses.
- ⁸ Nancy Pham and Susannah Snider, “Which Universities Burden Parents with the Most Federal Debt?” *US News and World Report*, February 13, 2018, <https://money.usnews.com/money/personal-finance/family-finance/articles/2018-02-13/data-which-universities-burden-parents-with-the-most-federal-debt>.
- ⁹ From Rachel Fishman, *The Wealth Gap PLUS Debt: How Federal Loans Exacerbate Inequality for Black Families* (Washington, DC: New America, 2018), 5: “The Department had discovered an error in the way the credit check had been implemented. This error was discovered after the federal loan program transitioned to full direct lending in July 2010. Before then, the federal student loan program made loans under two different programs: the Direct Loan program, where loans are issued directly through the Education Department, and the Federal Family Education Loan (FFEL) program, where loans were issued by private lenders and backed by the government. For all intents and purposes, the terms and conditions of the loans were the same. But the Department discovered a discrepancy between how the FFEL program implemented the credit check versus how it was done under Direct Loans. The Department had been, by mistake, making loans to parents with a history of accounts charged off to bad debt and accounts in collections.”
- ¹⁰ To read more about the rule change, see Fishman, “Education Department Publishes Final Rule.”
- ¹¹ PowerStats table bkabmp7b.
- ¹² PowerStats table bkabmafca.
- ¹³ PowerStats table bkabmc19.
- ¹⁴ PowerStats table dpbkhhp54.
- ¹⁵ Adam Looney and Vivien Lee, “Parents Are Borrowing More and More to Send Their Kids to College—and Many Are Struggling to Repay,” Brookings Institution, November 27, 2018, <https://www.brookings.edu/research/parents-are-borrowing-more-and-more-to-send-their-kids-to-college-and-many-are-struggling-to-repay/>.

¹⁶ Based on conversation with Robert Shireman (currently of the Century Foundation), who was an aide to Senator Paul Simon during the push by Simon for income-contingent repayment in the 1992 Higher Education Act reauthorization and 1993 expansion.

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