Executive Summary

This report provides background and context for the proliferating Pay It Forward, Pay It Back (PIF) legislation seen across the country. It explains what a PIF program is, describes the mechanics of these programs, outlines the conditions that would need to be met for a program to be viable, and identifies the issues and questions that require resolution before a program could be implemented. It is written in response to House Bill 5323 – the Pay It Forward, Pay It Back Act - that requires the Illinois Student Assistance Commission to "undertake a study to determine the practical and fiscal impacts of adopting a program in Illinois similar to Pennsylvania's Pay It Forward Pay It Back program." The bill further requires that the "study shall focus on the particular intricacies, details, and mechanics of funding with specific regard to the proposal contained in the language of House Bill 5323 [the Pennsylvania Model] from the 98th General Assembly, as introduced." The report also must include the results of a survey of similar programs in other states "with specific regard to funding and programmatic practicality and feasibility." The important points of the report are detailed below.

- At least 24 states have proposed some form of PIF legislation within the past two years. At the core of these legislative initiatives is a desire to reduce the financial barriers to college attendance that potential students face by implementing a state-funded loan program in which payment size is adjusted according to the borrower's income, or a contract for income sharing that allows students to defer paying for college until they join the workforce. These PIF programs usually tie the amount students ultimately pay for their education to the income they receive for a specified number of years after graduation. *To date, however, no state has implemented a PIF, even as a pilot program.*

- While actual program implementation has not occurred in any state, states' interest in the idea has accelerated. The astonishing number and speed of these legislative proposals, despite some very serious design hurdles and cost barriers yet to be overcome by any state, is likely the result of a combination of factors: the rapidly rising cost of higher education in all sectors; the necessity of pursuing higher education to help insure a middle-class standard of living; the decline in the ability or inclination of the states to fund higher education; and the uncertain job market for college graduates which leaves students wondering if they ever will be able to pay off their student loans. PIF programs appear to provide a path to acquiring a postsecondary credential for those who are now finding paying for college difficult or impossible.

- Although PIF programs have generated much interest by legislators, there are many in the higher education community opposing PIF programs. While some critics offer up logistical problems and student to student cost shifting as reasons for their dislike, the most prevalent and fundamental reason for the considerable opposition to these programs is the belief that they will mask declining state support for higher education and hasten the march toward the complete privatization of higher education. *These outcomes are not inevitable with a PIF program but any successful PIF program would have to provide safeguards to address these concerns*.

- The report describes the mechanics of a PIF program and the substantial political, legal and investment hurdles associated with these types of programs that must be overcome for a successful program to be implemented. PIF programs need to have an efficient financial instrument, either an Income Share Agreement (ISA) or an Income Based Repayment (IBR) Loan, and a workable set of program parameters that define eligibility requirements, identify the costs that can be deferred, detail an accounting methodology for tracking the deferred costs, develop repayment and collection procedures and identify a source or sources of initial funding.

- The issue of funding is critical. PIF programs require huge up-front costs by the state. To offer a PIF option to most public university and community college students in Illinois would require *billions of dollars in up-front costs from the state*. Under generous assumptions, it would be 20 years before the net revenue stream turns positive and many more years after that to recoup the initial investment. While other funding sources may be available at some point, such as public/private partnerships and utilizing a prepayment program for parents – a parent's PIF - these types of resources would take years to develop and may never develop. In the short run, reallocation of existing funds, new tax revenues and bonds are the only reasonable options available. Bonding out the cost seems the most likely option but that would add additional costs to an already expensive program.

- The report describes some safeguards that would need to be in place to prevent some of the widely perceived negatives of a PIF program, specifically that it would increase the movement toward the privatization of public institutions and that it would shield schools from the impacts of further raising their tuition and fees. Assuming those safeguards are in place, a program was modeled using a consistent set of assumptions to illustrate how a PIF program might work in Illinois. The analysis indicates that it is possible in Illinois to design a PIF program with a 20-year break even point (the point at which the state no longer has to make *additional* contributions) and keep the PIF repayment percentages on income under 5%. It also provides a description of a pilot program that could be implemented to test the financing mechanism and determine the accuracy of some of the assumptions concerning school and student behavior that need to be made when forecasting participation in this type of program. It would also establish the workability of participant tracking and collection processes. However, it is critical that additional work be done with outside professionals in the areas of legal, tax, actuarial and systems development to understand all of the issues and to accurately determine the cost of implementing a PIF program.

- The start up costs associated with a pilot program would be very high on a per participant basis since all of the operations necessary to run a full-scale PIF program would have to be in place. While the pilot program is only six years in length (the period of time where students are actually receiving a PIF), a least a year's lead time and more likely two years would be needed. Since services of attorneys, actuaries and other professionals would have to be procured and that procurement process can take nearly a year, the lead time needed could easily stretch to two years. A higher education trust fund would need to be set up to collect the payments from PIF participants and tracking and collecting methodologies would need to be developed. Payments from participants would need to be tracked and collected for twenty years after the project officially ends. In addition, the process of interacting with the schools related to making payment for students would have to be developed. *Adding the preparation time and the collection period to the actual PIF running time yields a "pilot" program that would take close to 30 years to complete.* While much of the information needed from that pilot would be obtained during the first ten years of operation, the program would still have to function until the last participants make their last payments.

- The protracted nature of a PIF pilot and the costs associated with it make running it only feasible if the intent is to institute the full-scale program. The biggest hurdle to running a full scale program is funding it. *Until a source of funding for a full-scale program has been identified, a pilot PIF program would appear to make little sense.*

- Policymakers should also take note that there are significant risks and uncertainties associated with the creation of a precedent-setting PIF pilot. The lack of any legal antecedents for a state-level PIF means that there are substantial questions unanswered regarding critical factors—such as taxation, bankruptcy, and collectability—affecting a PIF plan's ultimate success. Without clarity in these areas, there is real risk that a program could run into stumbling blocks in attracting program participants, securing adequate initial funding, attracting private investment (if using a public/private funding model), and ultimately achieving a self-sustaining system. Federal legislation that has been proposed but not yet passed in the current Congress could address a number of these issues, but as yet PIFs must be said to occupy a legal gray area.

- Finally, PIF programs have been billed in the media as essentially providing a way to make college "free." *PIF program are not the path to free higher education. They are deferred income payment plans that require repayments by participants that extend decades into the future.* The up-front costs that are being deferred by students have to be paid initially by the state at a cost of billions of dollars in addition to the state funding already provided. PIF programs may ultimately turn out to be a better way to pay for college, but they do not make college free for anyone.

In addition to the report, there is an appendix containing the origins and history of what are now called Pay It Forward programs (Appendix II), an appendix containing frequently asked questions (FAQs – Appendix I) about these programs, appendices describing other state initiatives (Appendix III) and federal legislation (Appendix IV), and a bibliography of all materials consulted (Appendix X). ISAC has established a PIF resources web page that contains the bibliography with links to the materials used. We also have encouraged comments and suggestions from those in the higher education community, existing private income share agreement providers and other interested parties. We have incorporated some of their comments into the report and all comments can be found in Appendix IX.

The legislation requiring us to produce this report did not ask for recommendations. There are strong opinions, both positive and negative, about PIF programs. This report attempts to describe the issues of concern and to show a pathway to the establishment of PIF program if funding can be found. Although a selection of program components had to be chosen to develop the fiscal estimates and address the mechanical issues (through a pilot program), the report does not recommend any particular course of action.