Income Share Agreements: A Student-Centric Alternative to Loans

Problem: student debt burdens recent graduates

As of June 2016, public universities in the U.S. had a default rate of 11.3% on student loans, and approximately 8.1 million students had not made a payment on $128 million of debt for at least nine months[1]. While legislative measures have alleviated some of the student debt burden in the U.S., a problem clearly persists and begs an alternative to the traditional loan model.

A major concern with the current system is that students entering a volatile job market have little option to alleviate their debt load if they are unable to secure well-paying work. The result is a large portion of U.S. youth faced with seemingly insurmountable debt that can ultimately burden them for decades.

Solution: shift down-side risk from the student to the investor

When a venture capital firm chooses to fund a start-up, it assumes essentially all down-side risk: if the firm fails, the investor faces the loss of his or her investment. Conversely, the success of the firm benefits both the investor and the firm itself. The result of this model is twofold: first, more individuals are encouraged to start new businesses with minimal risk in the case of failure. Second, investors have every incentive to aid in the success of the firm, as a positive return on their investment is contingent upon it.

The idea of Income Share Agreements is to extend this model to the funding of undergraduate education. Rather than banks offering loans to students—in which case the down-side risk (i.e. not finding a job) is placed solely on the student, who is responsible for the repayment of the loan regardless of financial success—investors fund students' education and in return receive a fixed share of their future earnings. In this way, the down-side risk is placed on the investor: students aren't burdened with a fixed loan amount, but rather with a repayment amount proportional to their income. In turn, then, investors are likely to provide guidance and mentorship to students, as the investor's return is tied directly to the students' success.

Why ASU?

Arizona State University has long been touted as the world's premier innovator in the education space. Indeed, there is hardly an issue in higher education more yearning for an innovative solution than the conundrum of student debt. Having designed a program connecting students with investors eager to see them succeed, the University will be able to better fulfill its mission of giving more people access to quality education, and do so with limited financial burden placed on the shoulders of students.

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[1] https://www.washingtonpost.com/news/grade-point/wp/2016/09/28/student-loan-default-rate-dips-but-considerable-work-remains-education-secretary-says/

How would the program work?

In the Fall of 2016, Purdue University piloted the first-ever Income Share Agreement program[2] at a major American university, achieving national recognition for its innovation[3,4]. While Purdue's program has seen preliminary success, securing funding for over 150 students in its first semester, ASU has the potential to innovate the idea further into something truly revolutionary. To do this, we propose three major advancements from the Purdue framework:

1. *Make the program student managed* – We propose selecting a board of student advisors to drive and oversee the implementation of the Income Share program, giving top undergraduate students experience working first-hand with investors, while helping their peers secure funding for their education.
2. *Leverage ASU's large network in the business world* - Through the University's commitment to innovation in education technology, ASU has forged tremendous relationships with many international firms whose goals align with those of the proposed program. These relationships will serve as a useful baseline from which to begin to find potential investors.
3. *Utilize ASU's relationship with the global community to reach the broadest possible range of students* - ASU is a global leader in educational outreach, offering quality education to a wide array of students from across the world each year. As such, the University has the unique opportunity to offer income-sharing options to students most liable to benefit from them.

Conclusion and next steps

If the University chooses to move forward, we propose implementing a small pilot of the program as soon as Fall of 2017. To make this possible, the University would first need to connect with potential investors interested in participating in the pilot. From here, a student board can be formed and begin to work with investors and third-party legal and financial entities to build the framework for the program, and ultimately advertise the pilot to potential student benefactors.

Once initial planning is underway, Luminosity will begin to develop new technologies around the program: first, we will use advanced data visualization to build tools to help students better understand their financing options and decide whether income-sharing is a viable funding option. Second, we will create an elegant, online framework for students and investors to connect and ultimately make finding funding as simple and intuitive as possible.

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[2] More information about Purdue's program can be found at http://purdue.edu/backaboiler/overview/index.html

[3] https://www.washingtonpost.com/news/grade-point/wp/2016/04/11/at-purdue-student-aid-based-on-future-earnings-could-revolutionize-college-debt/

[4] http://www.nytimes.com/2016/04/09/business/dealbook/getting-a-student-loan-with-collateral-from-a-future-job.html?_r=0