STUDENT BORROWER PROTECTION CENTER

Background on income share agreements, alternative data, and educational redlining

Income share agreements may perpetuate educational redlining

Income share agreements (ISAs) are consumer credit contracts wherein a student pledges a portion of his or her future income in exchange for money used to pay for college. Over $250 million in ISAs were originated in 2019, and market participants expected $500 million in ISAs to be originated in 2020 before the COVID pandemic began. Though industry-wide data are unavailable, the association between ISAs and the types of for-profit career training programs known to take advantage of economic downturns implies that the volume of ISAs originated in 2020 may have ultimately been much larger.

ISA providers often charge students more based on the school they attend or the major they select. Given that income, college selection, and students' choice of major are all closely associated with race, there is a substantial risk of educational redlining inherent to the ISA product. As described in an analysis published by the American Enterprise Institute, "there is a significant risk that evaluating students on [educational] factors tends to generate disparate impact on protected classes. Because some of the best predictors of student performance and future income are familial factors, such factors will disparately affect traditionally underserved communities."

A recent analysis by two fair lending experts substantiates these claims. In examining public pricing quotes for an ISA offered at the University of Utah, the authors noted that the advertised price of an ISA was thousands of dollars higher for students in majors with relatively more female students and students of color.

Alternative data poses fair lending risks

Financial services firms have long touted the use of nontraditional or "alternative" data, including data related to credit applicants' educational background (referred to as "educational criteria") as a purported method to expand access to credit. In recent years, however, regulators, lawmakers, civil rights organizations, and consumer advocates have all expressed concern that the use of educational criteria such as the school attended, major, or SAT score of a credit applicant in underwriting can lead to discriminatory outcomes. These risks can have a particularly outsized effect on communities of color, reinforcing systemic barriers to financial inclusion for Black and Latino consumers. Advocates refer to the damaging practice of denying members of protected classes equal access to financial products based on their educational backgrounds as "educational redlining." The salience of the risks associated with using educational criteria in underwriting is heightened by the critical role that MSIs—HBCUs, HSIs, tribal colleges, and more—play in expanding access to higher education for students from underrepresented communities of color. MSIs have a long legacy of serving as a pipeline for educational opportunity and upward mobility in communities of color.

Consumer protection and fair lending laws apply to ISAs, including Stride Funding's ISAs

A defining feature of the marketing of ISAs is industry's insistence that the contracts are not student loans or not even a form of credit and that they therefore fall outside of the legal structures that may be used to address the potential disparate impacts described above. Legal experts have rejected these arguments and instead agree that ISAs are simply another form of consumer credit that falls squarely within the purview of ECOA, the Truth in Lending Act, the Fair Debt Collection Practices Act, the Fair Credit Reporting Act, and the Consumer Financial Protection Act of 2010. Further, civil rights lawyers have already begun charting a course for challenges to ISAs under civil rights laws.