

KEEPING STUDENTS AWAY FROM THE PRECIPICE OF STUDENT LOAN DEFAULT

DON'T FALL!

By Justin Draeger

While climbing a narrow trail in Arches National Park, my wife and I found ourselves alone, staring up at a huge, rounded rock. The rock was longer than it was high and extended well beyond our view – and directly in our path. After a brief search we found a spot in the rock where weathering had created a natural staircase. Scrambling to the top we were rewarded with a beautiful view of a canyon lit with the late afternoon sun. We walked out as far as we could safely to absorb the beautiful vista.

Before long I found myself so transfixed by the view that, without thinking, I approached the edge of the rock to gaze down on the seemingly endless abyss. Only one wrong step, slip of the foot, or distraction separated me from certain death. When my wife took a step in my direction to join me, I quickly came to

my senses and pulled us both away.

A couple of years older now and hopefully a little wiser, I look back on that day and think of the foolishness of placing myself in a situation where I was so close to calamity and had so few options. But how different is my experience from the nearly three million people who enter student loan default each year?

Life on the Edge

Students focused on the beautiful vista that a postsecondary education provides can sometimes find themselves at the edge of a cliff, dangerously close to the precipice of student loan default that can sour even the best college experiences. Among the students who entered repayment in Cohort Year 2004, over 144,000 eventually fell off of that cliff into student loan default. Sure, some did not intend



to repay, but how many simply found themselves too close to the edge with so few options that only one miscalculated step made them tumble into default?

We have come a long way in helping students avoid the consequences of student loan default. The latest U.S. Department of Education figures show the average cohort default rate at 5.1 percent, 77 percent lower than the highest cohort rate 14 years ago. But by adapting our default aversion efforts to meet the specific needs of our students, and practicing them effectively and efficiently, we may see even more success and lower default rates.

Keeping Students Away from the Cliff

Once a trucking company owner began a search for a suitable driver for one of his toughest routes. It was a dangerous road with many curves, dips, and sharp corners, and required a high degree of skill.

He asked his three top candidates the same question: “How close to the edge of a cliff could you drive my truck without going over?”

“I could drive within two feet of the edge of a cliff without losing any of my cargo” said the first with pride.

“I could drive within one foot of the edge of a cliff without losing any of my cargo,” boasted the second.

“I’m not really sure,” the third applicant said. “I would keep as far away from the edge of that cliff as possible to keep your cargo safely away from any type of danger.”

Who do you think got the job?

Many of today’s default aversion tactics do not kick into full gear until the student is on the verge of default. Late-stage delinquency tactics can be very effective in keeping students from defaulting, at least within a certain cohort year. But how confident are we that a student who is saved from default through a late-stage delinquency strategy today will avoid default in the future? Cohort default rate statistics only cover students who enter repayment in one fiscal year and default before the end of the next fiscal year.

There is little information on what happens after that.

Sometimes with all of the talk about late-stage delinquency tactics and last-minute deferments and forbearances, we lose sight of the real opportunity that exists for financial aid professionals to reach the students with default aversion strategies while they are still within the institution’s own walls.

Curing the Problem, Not the Symptom

Sometimes default aversion is practiced like 19th century medicine: it treats the symptoms, not the illness. Student loan default is often the symptom of a larger underlying problem, such as financial illiteracy, poor money management, or unmanageable debt levels. Effective default aversion requires a head-on attack on the underlying problems *before* delinquency occurs. Getting students the financial tools to combat these problems early in their college careers gives them a better chance of keeping their loans in good standing after leaving school.

The Right Tools for Your Students

Financial aid administrators can develop effective tools by knowing their student population, allocating their resources effectively, and exchanging ideas with others in the profession.

1. Know your student population.

Extensive studies have been conducted on student populations that can give financial aid administrators insight into student characteristics (see *Student Data Resources* on page 16 as a research starting point). But what is unique about *your* student population? For example, graduates of which majors in your school tend to have high debt but lower salaries upon completion of their schooling? Are certain students at your school more likely to withdraw? How well do your students understand basic financial terms such as compounding interest, deferment, forbearance, or amortization? Are there any significant differences between students in certain programs in regard to

their credit card use, debt levels, expected salary levels, likelihood of using deferments or forbearances, or even default?

While a multivariate analysis may sound daunting, you may want to collaborate with other offices (such as the admissions or institutional research offices) or departments in your school to study these questions, perhaps as part of an overall student retention study, or possibly as part of a student's masters or doctoral project. Besides your institutional research office, schools of business, social sciences, statistics, or education would be good starting places to look for help with research projects. Almost any information about your student population can be helpful. You cannot prescribe a cure for an illness that you do not fully understand.

2. Allocate resources effectively. Once you understand more about your students, default aversion resources should be allocated according to their unique needs. Instead of blanketing all of your students with the same default aversion strategy, give the most attention to the students who are more likely to need it most. Perhaps your accounting students only require basic information and exit counseling while your social work students require additional information on the availability of deferments and forbearances until their salaries are sufficient to begin successful loan repayment. Perhaps something extra should be done for students you identify as more likely to withdraw, or maybe certain freshmen (e.g., those with a certain debt level, those in certain majors, those with lower family incomes) should receive additional encouragement to enroll in a special college success series.

The point is that everyone works with finite resources, and targeting them to the students who are most at risk may go a long way to maximizing your default aversion strategies. One guarantor did a simple analysis on their default population and found that a majority of defaulters had one common characteristic: more than 90 percent were students who had

withdrawn. The guarantor allocated resources accordingly to focus additional attention on withdrawn students. They created a customized exit packet that could be sent directly to the withdrawn students and began calling all withdrawn students during their grace period to remind them of their impending first student loan payment. During the phone campaign, if the borrower balked in any way about the impending payment, the guarantor would remind the borrower of additional deferments or forbearances. The guarantor would then add the lender into a conference call with the borrower to ensure that everything was taken care of immediately. Since the guarantor began reallocating these resources based on their analysis six years ago, their default rate has decreased by more than 40 percent.

3. Exchange ideas. We all have the students' best interests at heart. When we find a successful default aversion tactic, it should be shared with others in the financial aid community. Whether through state, regional, or national association meetings, listservs, newsletters, or even through an article submitted to *Transcript*, keep others informed of your successes.

Also, keep your eyes and ears open. Too often scarce time and resources are spent developing programs that have already been created at other schools. When you hear of a good idea, ask questions, learn more, and consider whether a similar approach would be effective on your campus. Although some default aversion

activities, courses, and materials may be proprietary, there are often ready-made materials or programs available that may be used as-is or adapted to meet the needs of your students.

Don't just dump piles of default literature on your students, though. Choose carefully according to your students' characteristics. Given students' competing priorities, a few exceptionally informative or powerful pieces or programs are better than a crate of mediocre materials or a presentation that doesn't suit your population

Making a Difference

Financial aid administrators do vital work that largely goes unrecognized. If everything goes right, you often receive no thanks or spotlight; if anything goes wrong, you get too much spotlight! But default aversion can be a bright spot in the financial aid process, giving you the chance to educate students and give them the financial tools that will help them well into the future.

Default aversion has evolved quite a bit in the last two decades with great success. Now it is time to improve on all we have learned. It is worth the effort. Little is more satisfying than helping students to experience the vistas that accompany a postsecondary education, knowing they are safe from the precipice of student loan default.

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STUDENT DATA RESOURCES

The following resources are a good starting point for financial aid administrators who want to know how their students' borrowing behavior compares to other students nationally.

- *NASFAA Annotated Bibliography of Student Financial Aid*
- MGA Default Aversion Database
- US Dept. of Education's National Center for Education Statistics
- The College Board: *Trends in Student Aid, Trends in College Pricing, Annual Survey of Colleges*
- Pell Grant End of Year Report (DOE - OPE)
- Federal Loan Volume Update (DOE - OPE)
- Survey Report (NASSGAP)