What Was the Impact of Borrowing on Borrowers?

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July 13, 1999

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Executive Summary

This paper examines the effect of borrowing on the lives of the borrowers after they leave school. It is the third in a series of three papers on undergraduate borrowing. The first paper, titled *Undergraduate Borrowing* (December 1998) examined national and state trends in the aggregate dollar volume of borrowing and looked at the percentage of students who borrow. The second paper was *How Much Did Undergraduates Borrow?* (February, 1999). Most of the data in this paper and both earlier papers was national data.

The Effect of Borrowing on the Lives on the Borrowers

The ratio of debt payments to income determines the effect of borrowing on the lives of borrowers. Even small amounts of debt were a problem if the borrower had little income. Typical student loan defaulters owed less than $3,600.

Student loan payments averages $136 per month April 1994 according to the National Center for Education Statistics (NCES) study of 1993 bachelor's degree recipients. Payments averaged $76 per month for associate degree or certificate recipients and students who did not complete any post-secondary degree according to the NCES study of 1989-90 beginning post-secondary students whose last enrollment ended by December 1992.

As salary increased, the number of borrowers with payments of 15 percent (or more) of their salaries decreased. Among the 1993 bachelor's degree recipients who had salaries less than $15,000, 41 percent had payments that were 15 percent (or more) of their salaries. Among those who had salaries of $35,000 or more, 2 percent had payments that were 15 percent (or more) of their salaries. About 10 percent of borrowers who did not complete their post-secondary program and those who received associate degrees or certificates had payments that were 15 percent (or more) of their salaries.

About 50 percent of borrowers said they felt burdened by their student loan payments, 18 percent said they did not feel burdened, and 32 percent were neutral according to the NellieMae 1997 study.

About 36 percent of borrowers said that their student loans caused more financial hardship than anticipated in the NellieMae 1997 study. About 41 percent disagreed that their loans had caused more hardship than anticipated. About 23 percent were neutral.

Federal Pell Grant recipients did not report feeling more burdened than other borrowers.

Half of borrowers said they would borrow about the same amount if they could begin again in the NellieMae 1997 study. Nearly half (45 percent) said they would borrow less. About 5 percent were neutral. Responses to this variable differed by race/ethnicity. About 60 percent of black borrowers said they wished they had borrowed "a little less" or "much less." Black borrowers in the study had similar incomes and debt levels to others, but they were more likely to say that their loans caused them problems. About 44 percent of Hispanic and Asian borrowers said they wished they had borrowed less. Approximately 43 percent of white borrowers said the same thing.

Non-education debt also effected borrowers. The NellieMae 1997 study asked borrowers about other debt (including car loans, mortgages, and credit cards). About 97 percent of respondents had non-education loan debt, with a median monthly payment of $700. Borrowers had higher average non-education loan debt than average student loan debt. Borrowers felt equally burdened by both kinds of debt. Most borrowers who felt extremely burdened by student loan payments gave the same response for non-education loan payments.

Borrowers could choose to reduce their monthly student loan payments even though it would increase their interest costs. Approximately18 percent of borrowers said they would opt for reduced monthly student loan payments even though it would increase interest costs according to the NellieMae's 1997 National Student Loan Survey.[1]

In a USA Group study of borrowers who entered repayment in Fiscal Year 1998 more than 90 percent chose level payment plans. About 9 percent chose graduated payment plans and less than 1 percent chose income sensitive repayment plans. Even among borrowers who were consolidating their loans to reduce their monthly payments, more than 80 percent chose level payments plans and very few chose income sensitive options. Thus, 80 to 90 percent of borrowers expected to be able to pay the standard monthly amount.

Delinquency rates, deferment rates, forbearance rates and default rates can be indicators of borrowers who have trouble making their payment. When borrowers obtained deferments, no payments were due during the deferment. About 8 nine percent of USA Group borrowers with Subsidized Stafford Loans and 9 percent of those with Unsubsidized Stafford Loans were in deferment in July 1998. About 12 percent of subsidized and unsubsidized Stafford Loan borrowers had payments that were at least 30 days overdue. About 14 percent of USA Group borrowers with Subsidized Stafford Loans and 19 percent of those with Unsubsidized Stafford Loans were in forbearance in July 1998.

The national cohort default rate on federally guaranteed student loans for 1996 was 9.6 percent. Minnesota's cohort default rate for 1996 was 7.6 percent.

In many studies of the characteristics of borrowers who default on student loans there are two primary characteristics of defaulters. The borrowers did not complete their post-secondary studies and the borrowers had low incomes. Usually borrowers who completed more years of post-secondary education and those who borrowed larger amounts had lower default rates.

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1 NellieMae is a non-profit student loan lender and secondary market.

Some borrowers repaid their loans early. The NCES Baccalaureate and Beyond study showed that by 1994, 17 percent of 1993 bachelor's degree recipients who had borrowed as undergraduates no longer owed any money on their student loans. The NCES Study of 1989-90 Beginning Postsecondary Students showed that by 1994, 23 percent of noncompleters and associate degree or certificate recipients who had borrowed no longer owed any money.

Overall, 58 percent of borrowers said that they knew how much total debt they were accumulating when they signed for their education loans according to the NellieMae 1997 study. About 20 percent disagreed that they understood.

Approximately 69 percent of borrowers said that loan repayment became easier over time, in the NellieMae 1997 study. About 31 percent said that it had not gotten easier at all.

Some borrowers received help in paying their student loans from relatives or friends. The NCES Survey of 1989-90 Beginning Postsecondary Students showed that in 1994, 13 percent of noncompleters, associate degree and certificate recipients who were making payments were receiving help from relatives or friends. In the NellieMae 1997 study, 23 percent of borrowers received help from their parents.

Borrowers were just as likely to move out of their parents home, get married, have children and buy a home as non-borrowers, according to the NellieMae 1997 study. There was a difference between perception and behavior on these variables. More than 20 percent in the NellieMae 1997 study said that their debt was important or extremely important in causing them to delay moving out of their parents' home or to delay having children. About 40 percent said that their debt caused them to delay purchasing a house. However, their behavior differed from this perception. When the analysis controlled for other factors related to each variable (such as age and income) borrowers with higher debt and higher payment to income ratios were no more likely than other borrowers to delay these behaviors.

In the NellieMae 1997 study, 31 percent said that their student loan debt was important or extremely important in causing them to delay purchasing their own car. Among those whose payments were more than 15 percent of income, 30 percent said their student loan debt was extremely important in causing them to delay purchasing a car. Among those whose payments were less than 10 percent of income, 10 percent expressed this opinion.

Most borrowers were also saving for the future. In the Baccalaureate and Beyond survey, among 1993 bachelor's degree recipients making loan payments, 71 to 77 percent of those working full time said they were saving. Those paying 15 percent (or more) of salary in education loan payments were more likely to be saving than those paying less than 5 percent.

About half of borrowers who left school before completing their programs said that concern over borrowing prevented them from staying in school, according to the NellieMae 1997 study. About 31 percent of these borrowers said that this factor was not an important factor in preventing them from staying in school. Responses to this variable varied by racial/ethnic group. About 69 percent of black borrowers who did not complete a degree said that loans prevented them from staying in school and completing a degree. About 71 percent of Hispanic borrowers and 70 percent of Asian borrowers who did not complete a degree said the same thing. Approximately 43 percent of white borrowers who did not complete a degree said that concern over borrowing was an important factor in preventing them from staying in school.

Borrowing appears to affect enrollment in graduate school. The 1993 bachelor's degree recipients who borrowed were slightly less likely than nonborrowers to apply to graduate school by spring 1994. About 27 percent of borrowers applied to graduate school. About 30 percent of nonborrowers applied. In the NellieMae 1997 study, 43 percent of respondents said their undergraduate debt was important in preventing them from going to graduate school. About 28 percent said this was not important. Half the Federal Pell Grant recipients in the NellieMae study said that their undergraduate debt had prevented them from attending graduate school, compared to 38 percent of those who did not receive Federal Pell Grants.

Most (66 percent) borrowers said they thought the loans were worth the trouble of repayment. (NellieMae, 1997) About 76 percent of respondents said that student loans were extremely or very important in allowing them to continue their education after high school. About 76 percent of borrowers said that the education they"invested in" with student loans was worth it for personal growth. About 64 percent said that the investment they made in their education through borrowing was worth it for the career opportunities it provided.

About 66 percent of borrowers in the NellieMae 1997 study said that loan payments were unpleasant but the benefits of the education loans were "worth it." About 10 percent disagreed. The rest were neutral.

About 64 percent of respondents said that student loans were extremely or very important in allowing them to attend the school of their choice, 13 percent said that loans were not important in this regard. (NellieMae, 1997)

About 82 percent of Federal Pell Grant recipients who borrowed reported that loans were important for continuing education after high school, as compared to 72 percent of those who did not receive Federal Pell Grants.

About 37 percent of the borrowers in the NellieMae 1997 survey said that the student loan/debt counseling they received prepared them for repayment. About 40 percent disagreed. About 23 percent were neutral.

Introduction

This paper examines the impact of undergraduate debt on borrowers. The paper includes information on:

- Was student debt hard to repay?
- Did the debt affect major life decisions and career choices?
- Did borrowers think the debt was a good way to finance post-secondary education?

This is the third in a series of three papers on undergraduate borrowing:

1. ***Undergraduate Borrowing***, December 28, 1998.

    A) National and state trends in the aggregate dollar volume of borrowing.

    B) What percentage of students borrowed?

2. ***How Much Did Undergraduates Borrow***?, February 16, 1999.

3. ***What Was the Impact of Borrowing on Borrowers?***

Summary of Findings Reported Earlier

- ***Undergraduate Borrowing***, December 1998
    - The aggregate dollar volume of borrowing increased in Minnesota and nationally, particularly since 1992.
    - In 1992, the federal government increased the amounts students could borrow and made all students eligible to borrow.
        - The increase in borrowing was greater than the increases in both tuition and inflation from 1987 to 1997.
        - The rate of increase in the aggregate dollar volume of borrowing by Minnesota undergraduates was less than the rate of increase in national borrowing from 1987 to 1997.

- What percentage of students borrowed?
  - Most of the data included was for post-secondary students across the U.S.A.
  - 38 percent of all undergraduates had borrowed in 1995-96.
  - The more time students spent on post-secondary education, the more likely they were to borrow.
  - As the price of attendance increased, the percentage of students with debt increased.

- *How Much Did Undergraduates Borrow*, February 1999.
  - Most of the data included was for post-secondary students across the U.S.A.
  - Most borrowers borrowed $10,000 or less - 63 percent of borrowers at four-year institutions.
  - About 9 percent of borrowers at four-year institutions borrowed $20,000 or more.
  - The amounts borrowed by full-time, full-year students were similar to the amounts borrowed by part-time students or students who attended only part of the year. However, more full-time, full-year students borrowed.
  - The amounts borrowed by students who worked different numbers of hours per week were similar. However, the more hours students worked each week, the less likely they were to borrow.
  - The amounts borrowed by students from families in different income groups were similar. However, as income increased, the percentage of students who borrowed decreased.
  - First and second year students borrowed less than third and fourth year students.
  - Price of attendance explained more of the variation in amounts borrowed than the other variables, but the amount borrowed increased more slowly than the price increased.

This paper examines how undergraduate debt affected borrowers.

Sources of Information

Much of the information in this paper came from national surveys conducted by the National Center for Education Statistics (NCES) at the U.S. Department of Education. These surveys collected information on borrowing by students across the United States. The surveys were:

- *National Postsecondary Student Aid Study, 1993* - During the 1992-93 academic year, the National Center for Education Statistics conducted a comprehensive study of how students and their families finance post-secondary education. It included nationally representative samples of undergraduates attending all types of public and private institutions. The study included students who received financial aid and those who did not receive financial aid.

- *National Postsecondary Student Aid Study, 1996* - During the 1995-96 academic year, the National Center for Education Statistics repeated the survey described above.

- *Baccalaureate and Beyond Study, 1994* - During Spring 1994, the National Center for Education Statistics surveyed 11,000 1993 bachelor's degree recipients who were part of the National Postsecondary Student Aid Study for 1993.

- *Beginning Postsecondary Students, 1990/1994* - During Spring 1994, The National Center for Education Statistics surveyed students who started post-secondary education for the first time in 1989-90 and whose last enrollment ended by December 1992.

An additional important source was the *1997 National Student Loan Survey*, often called the NellieMae 1997 survey. The results discussed in this paper are based on the 1,098 usable responses to the survey that NellieMae sent to 2,500 borrowers. Borrowers in the population had loans owned by Nellie Mae and serviced by USA Group Loan Services. Nellie Mae is a nonprofit student loan originator and secondary market. The population in the survey is not nationally representative. It is concentrated in Massachusetts, New York and California. These states have about 23 percent of the post-secondary students in the U.S.A. The borrowers surveyed began repayment of their loans between 1993 and 1996. They responded to the survey in 1997.

What Was the Impact of Undergraduate Debt on Borrowers?

This paper presents the following information on the impact of undergraduate borrowing on those who had student loans:

- Was the amount of debt the problem?
- Was student debt hard to repay?
- Did the debt affect major life decisions and career choices?
- Did borrowers think the debt was a good way to finance post-secondary education?
- Discussion - what do we make of the information on student borrowing?

Data presented in this report include only those with loans.

The statistics reported in this paper are for ***borrowers who had undergraduate loans***. Some undergraduates did not borrow.

Was the Amount of Debt the Problem?

- Many people assume that a larger amount of debt always has more impact on the borrower than a smaller amount of debt.

- However, small amounts of debt can be a problem if the borrower has little income.

  - Typical student loan defaulters owe less than $3,600.

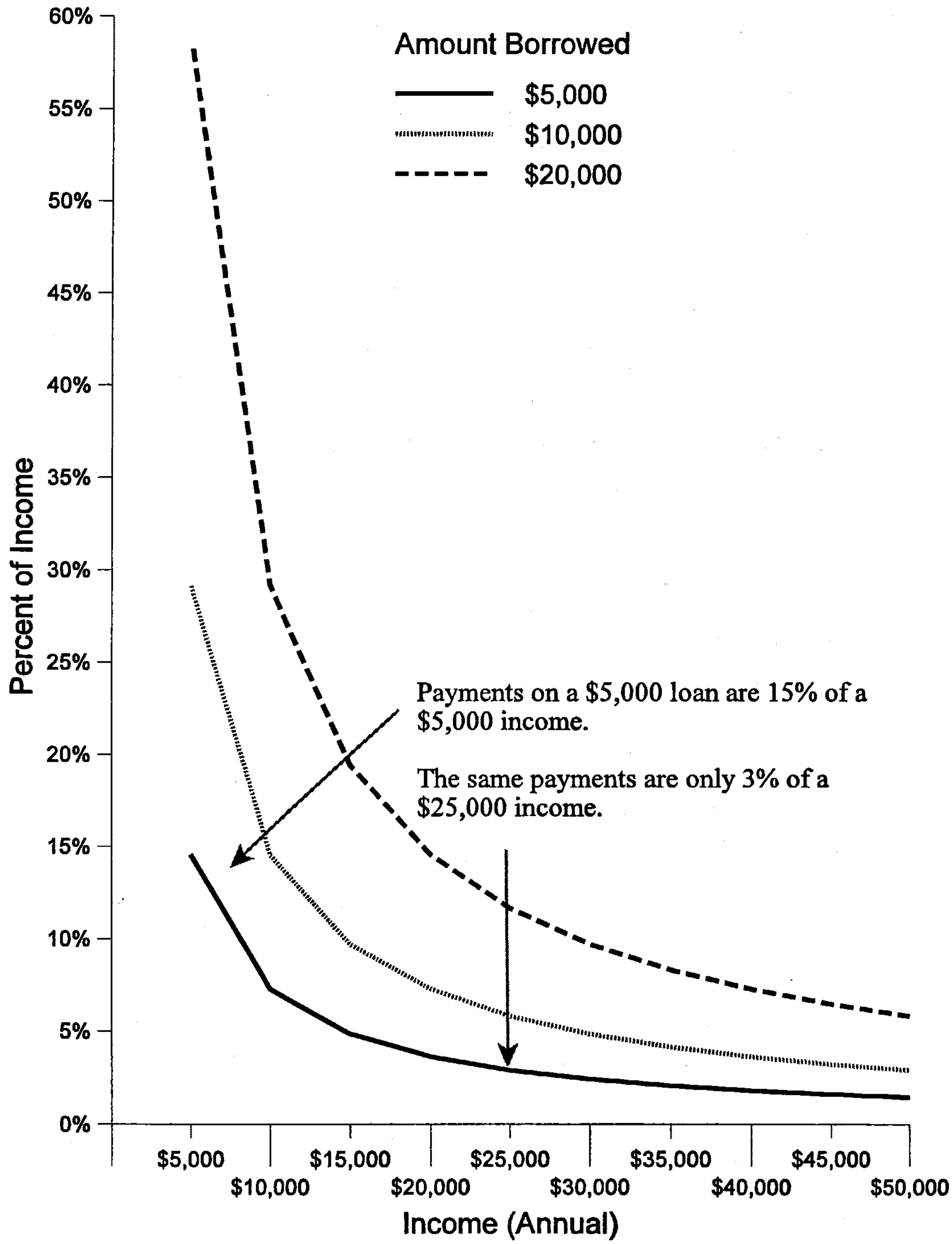
- The effort required of borrowers to make their debt payments can be expressed as the ratio of payments to income.

  - The ratio of payments to income decreases as income increases for any given loan amount, as shown in Figure 1.

  - For example, payments on a $5,000 loan are about $728 per year, which is 15 percent of a $5,000 annual income.

  - The same payments are only 3 percent of a $25,000 income.

Figure 1. The Impact of Loan Payments Depends on Income and the Amount Borrowed



Source: Minnesota Higher Education Services Office

Were Student Loans Hard to Repay?

This section examines indicators of payment stress. The indicators are choice of repayment plans, delinquency, deferment, forbearance and default rates. In addition, this section looks at student attitudes about how hard it was to repay.

How Much Were the Monthly Payments?

1993 Bachelor's Degree Recipients (NCES)

- The NCES study of 1993 bachelor's degree recipients who were making payments in 1994 showed that borrowers paid $136 per month on average.

- About 39 percent of 1993 bachelor's degree recipients who were making payments paid less than $100 per month, as shown in Figure 2.

    - 11 percent paid $250 or more.

Noncompleters, Associate Degree or Certificate Recipients (NCES, 1990/1994)

- Those who were in repayment among associate degree or certificate recipients and students who did not complete any post-secondary degree paid an average of $76 per month.

- The distribution of monthly payments for these borrowers is also shown in Figure 2.

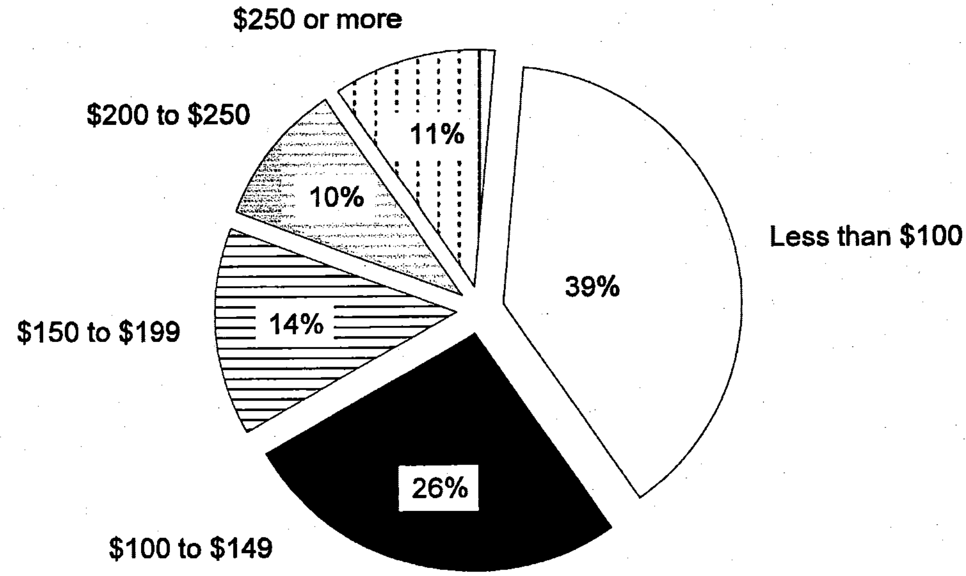
    - 72 percent paid less than $100 per month.

    - 3 percent paid $200 or more per month.

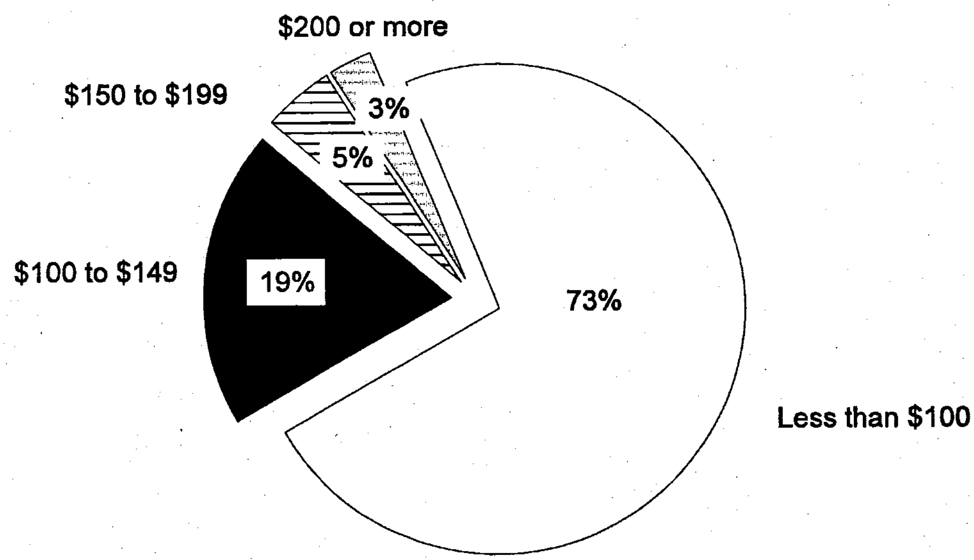
Monthly Student Loan Payments in 1994		
	1993 Bachelor's Degree Recipients	Noncompleters, Associate Degree & Certificate Recipients
Less than $100	39 %	72 %
$100 to $149	26 %	19 %
$150 to $199	14 %	5 %
$200 to $249	10 %	2 %
$250 or more	11 %	1 %

Figure 2. Monthly Payments in 1994

1993 Bachelor's Degree Recipients



Noncompleters & Associate Degree or Certificate Recipients



Source: National Center for Education Statistics

Monthly Payments As a Percent of Salary

1993 Bachelor's Degree Recipients (NCES)

- As salary increased, the number of borrowers with payments of 15 percent (or more) of their salaries decreased.

  - Salary was annualized based on the respondent's primary job in April 1994.

  - Among the 1993 bachelor's degree recipients who had salaries less than $15,000, 41 percent had payments that were 15 percent (or more) of their salaries, as shown in Figure 3. (28 percent of 1993 bachelor's degree recipients had salaries less than $15,000.)

  - Among those who had salaries of $15,000 to $19,999, 12 percent had payments that were 15 percent (or more) of their salaries.

  - Among those who had salaries of $20,000 to $24,999, 9 percent had payments that were 15 percent (or more) of their salaries.

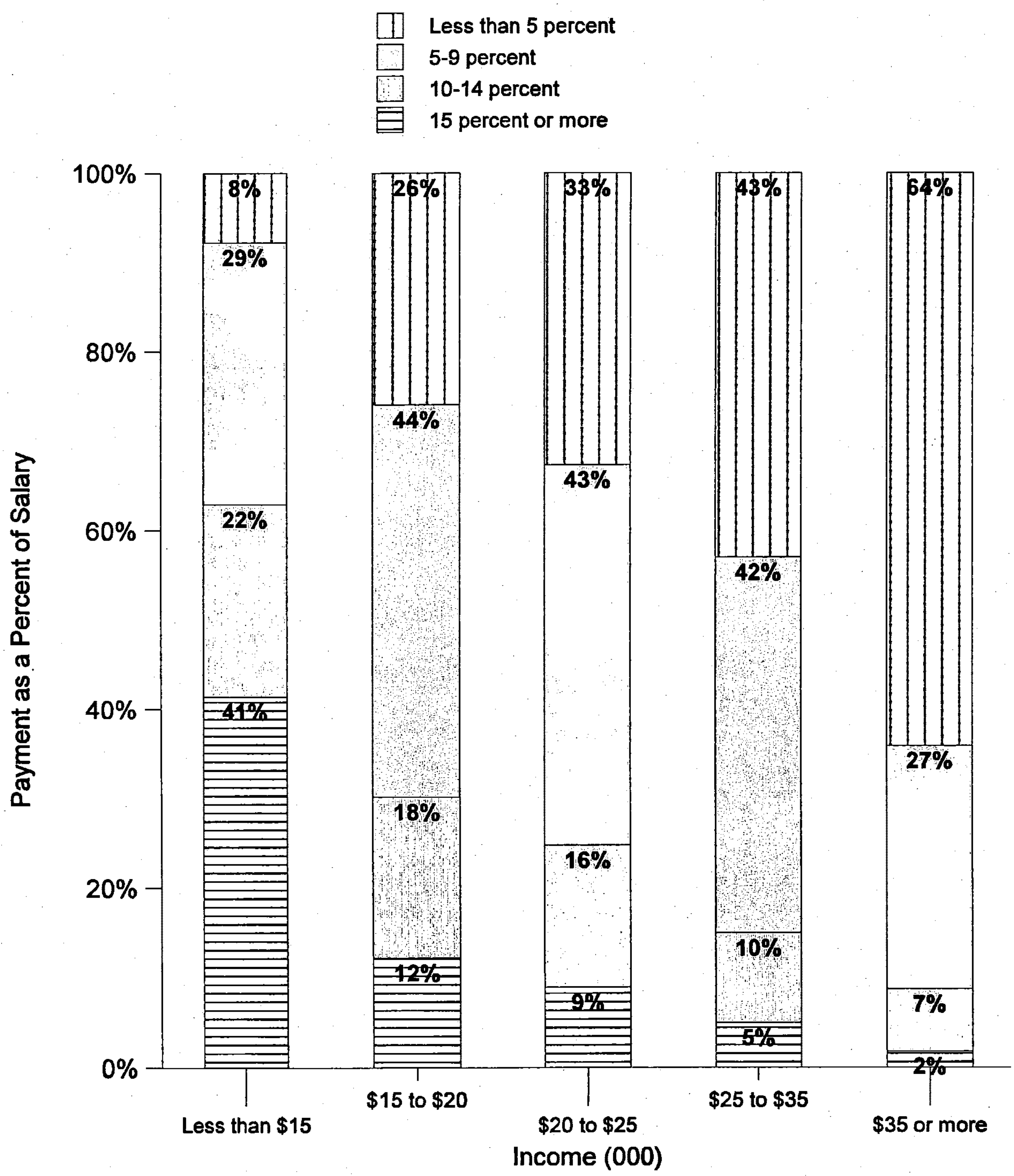
  - Among those who had salaries of $25,000 to $34,999, 5 percent had payments that were 15 percent (or more) of their salaries.

  - Among those who had salaries of $35,000 or more, 2 percent had payments that were 15 percent (or more) of their salaries.

Distribution of Payments as a Percent of Salary

Salary (000)	*Payments That Were Less than 5% of Salary*	*Payments That Were 5-9% of Salary*	*Payments That Were 10-14% of Salary*	*Payments That Were 15% or more of Salary*
Less than $15	8%	29%	22%	41%
$15 to $20	26%	44%	18%	12%
$20 to $25	33%	43%	16%	9%
$25 to $35	43%	42%	10%	5%
$35 or more	64%	27%	7%	2%

Figure 3. Monthly Payments As a Percent of Salary in 1994 for
1993 Bachelor's Degree Recipients



Source: National Center for Education Statistics

Noncompleters and Associate Degree or Certificate Recipients (NCES, 1990/1994)

- About 10 percent of borrowers who did not complete their post-secondary program and those who received associate degrees or certificates had payments that were 15 percent (or more) of their salaries, as shown in Figure 4.
  - Small sample sizes precluded making statistically reliable comparisons by salary groups.

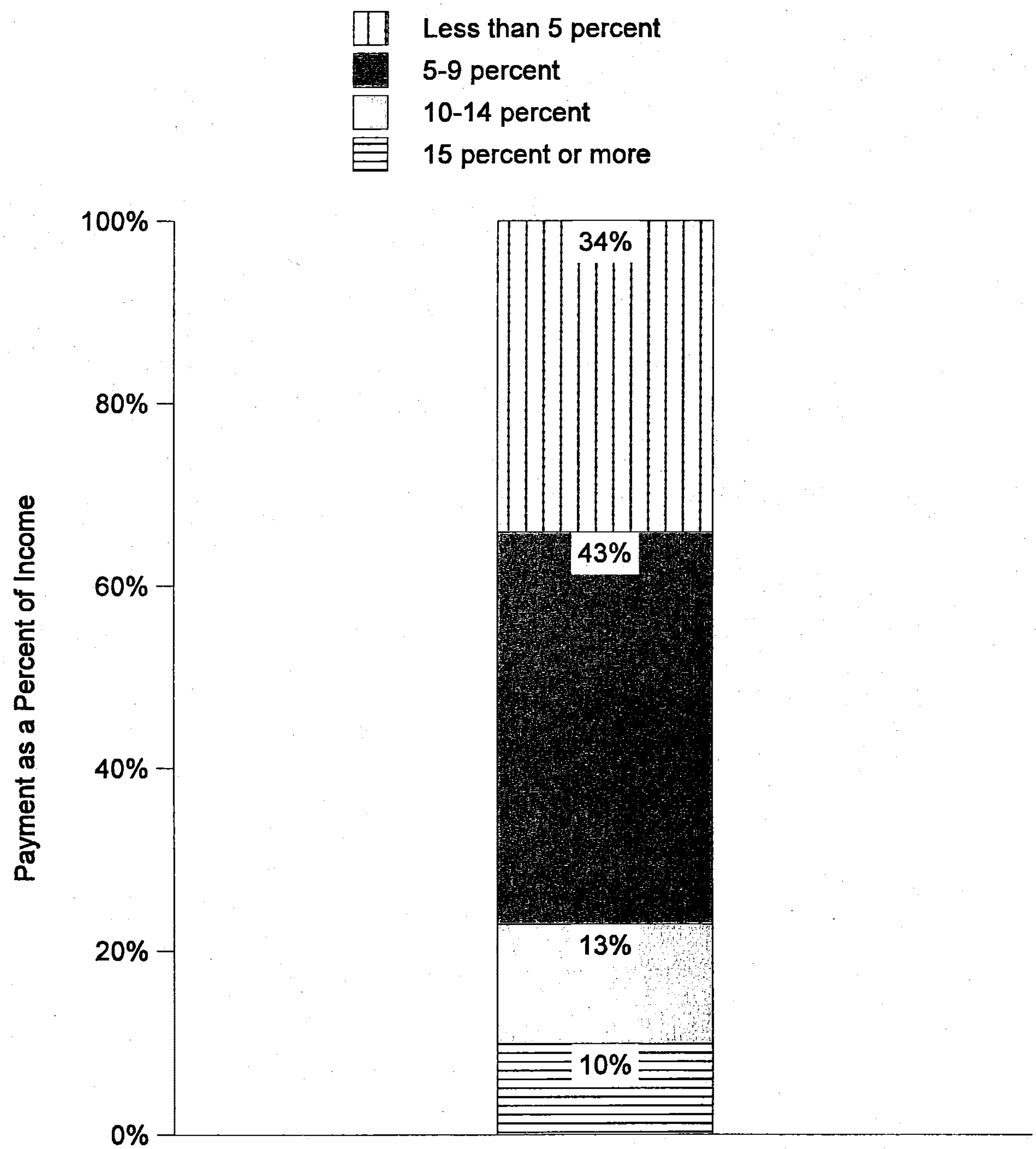
The Choice Between Lower Monthly Payments and Increased Cost

- The NellieMae 1997 study asked borrowers whether they agreed with the following statement:

  "If I could, I would opt for reduced monthly student loan payments even though it would increase my repayment period and the interest costs over the life of the loan."

  - Overall 18 percent of the respondents said they "strongly agreed" or "agreed" with the statement.
  - Borrowers with incomes of $20,000 or less were more likely to agree.
  - Responses to this question differed by racial/ethnic group:
    - 32 percent of black borrowers said say they would opt for lower payments even at higher overall cost.
    - 23 percent of borrowers from other minority groups said they would opt for lower payments.
    - 17 percent of white borrowers said the same thing.

Figure 4. Payments As a Percent of Salary in 1994 for Noncompleters and Associate Degree or Certificate Recipients



Source: National Center for Education Statistics

Perceived Burden

- The NellieMae 1997 study asked how borrowers perceived the burden of repayment, as shown in the top panel of Figure 5.

"To what extent do you feel burdened by your student loan payments?"				
Extremely Burdened				Not at All Burdened
1	2	3	4	5
22%	28%	32%	14%	4%

- 43 percent of borrowers who used more than 15 percent of their monthly salary for loan payments felt extremely burdened.
- 77 percent of borrowers who were delinquent reported they felt "significantly" burdened by their student loan payments.
    - 47 percent of those who were not delinquent reported they felt "significantly" burdened.

Perceived Hardship

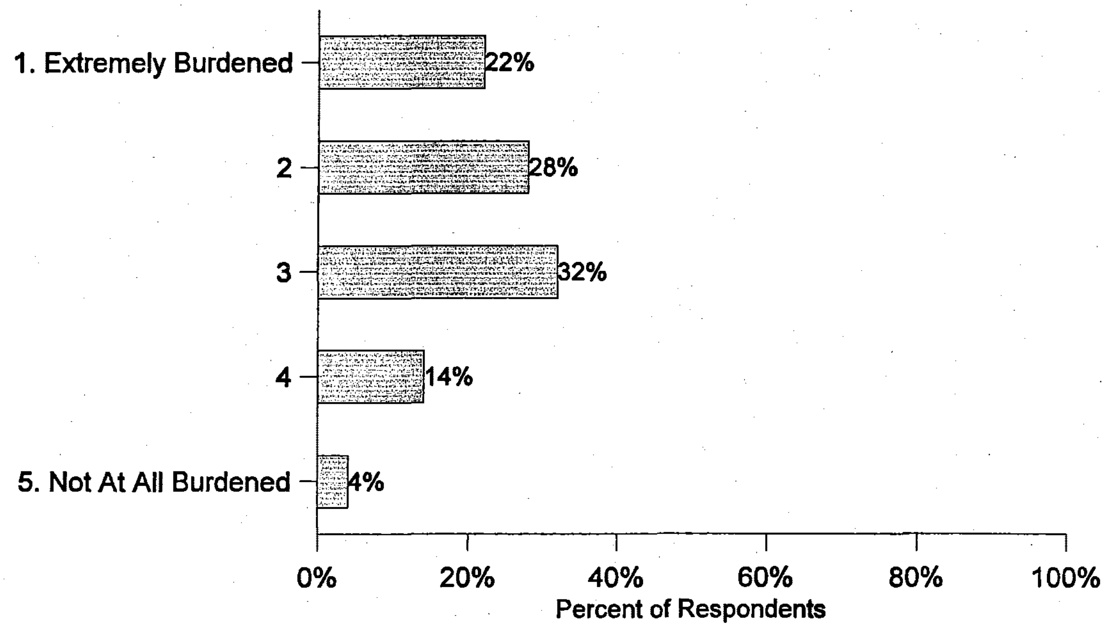
- The NellieMae 1997 study asked borrowers to respond to the statement:

    "Since leaving school my student loans have caused me more financial hardship than I had anticipated at the time I took out the loans."

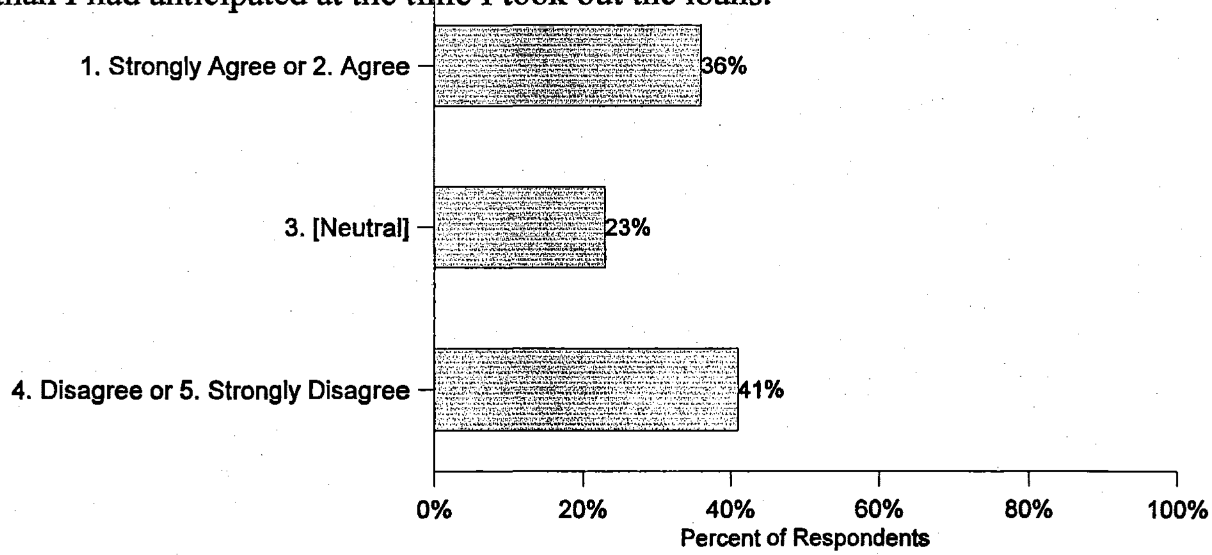
- About 36 percent of borrowers agreed with the statement and 41 percent disagreed, as shown in the bottom panel of Figure 5. About 23 percent were neutral.
- Federal Pell Grant recipients did not report feeling more burdened than other borrowers.

Figure 5. Repayment Perceived as Burden and Hardship

"To what extent do you feel burdened by your student loan payments?"



"Since leaving school my student loans have caused me more financial hardship than I had anticipated at the time I took out the loans."



Source: National Student Loan Survey, NellieMae 1997

- Debt burden is defined differently by different people. A study of 2,000 borrowers in Iowa in 1990 measured two indicators of debt burden. (Greiner, *Journal of Student Financial Aid*, Winter 1996.)

  - About 33 percent of borrowers perceived their student debt as a burden.

    - These borrowers answered yes to the question:

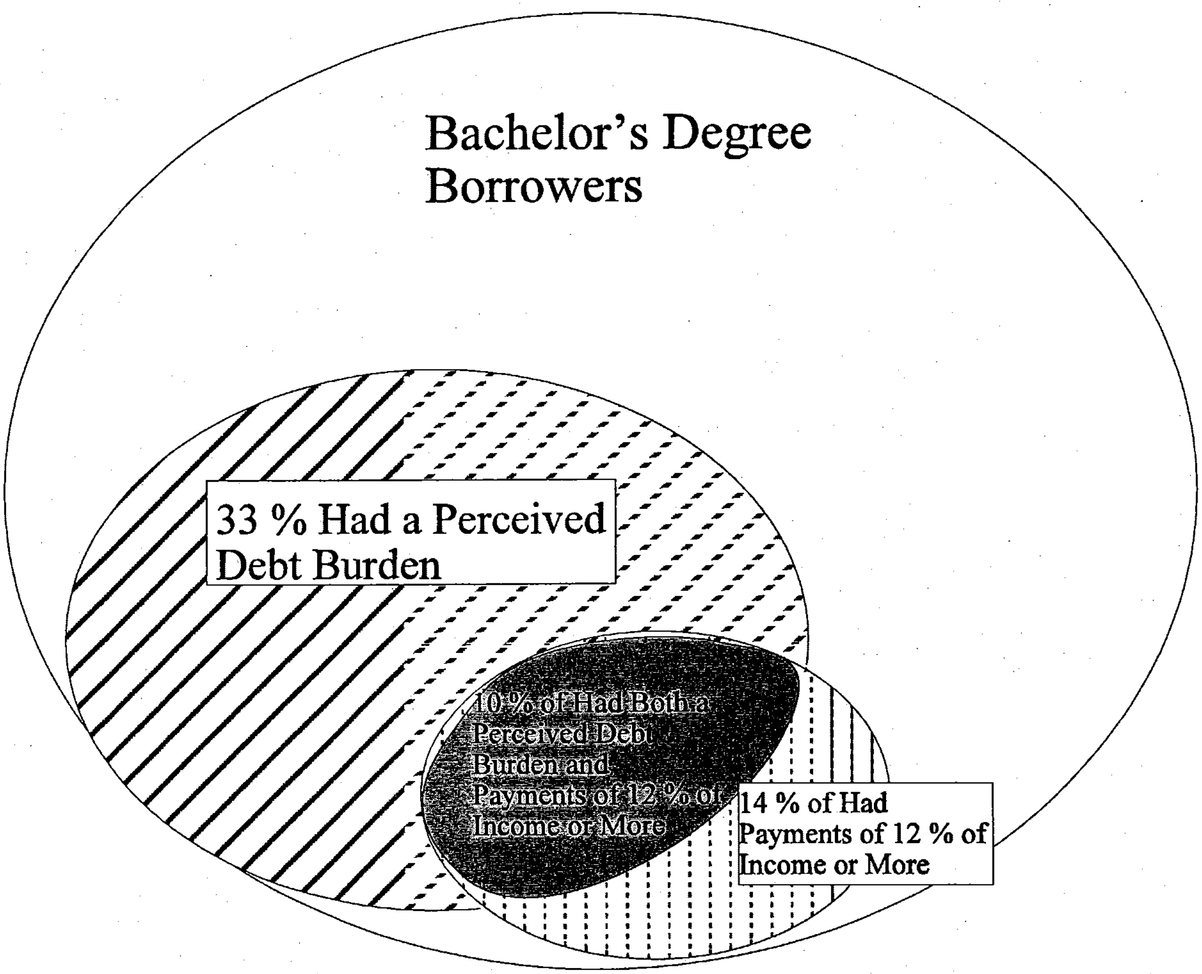
    "My student loans have caused me more financial hardship than I anticipated."

    - 29 percent of those who said their loans were a hardship also had payments that were 12 percent (or more) of income.

  - Approximately 14 percent of borrowers had payments of 12 percent or more of income.

  - Thus 10 percent of borrowers had both indicators of burden, as shown in figure 6.

Figure 6. Borrowers With Two Indicators of Hardship



Source: Iowa Student Aid Commission, 1990

If You Had to Do It Over, How Much Would You Borrow?

- The NellieMae 1997 study asked borrowers:

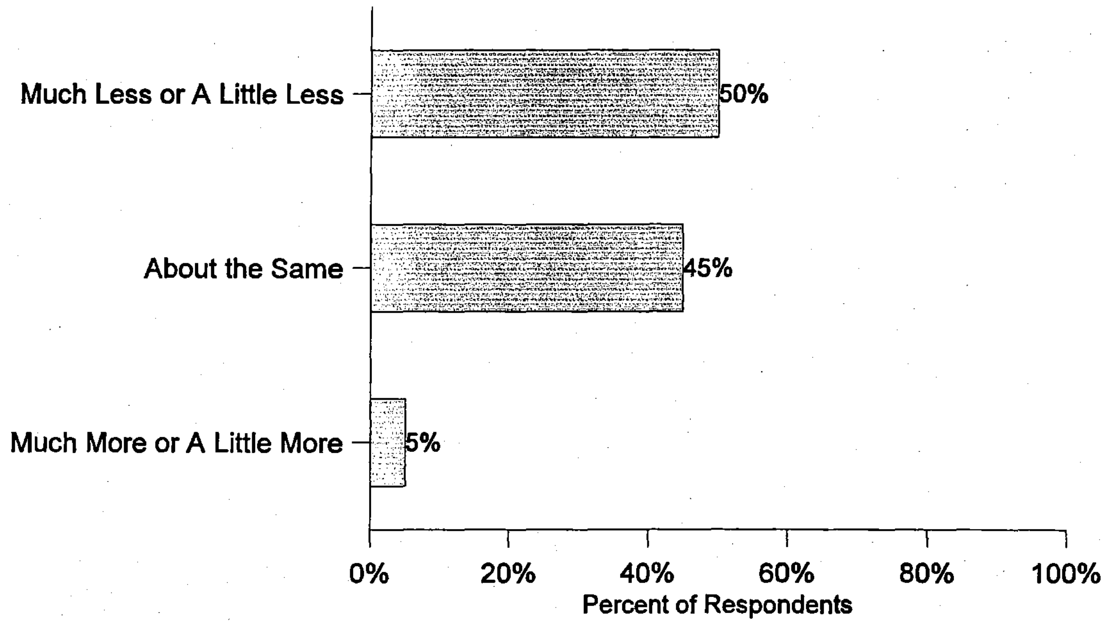
  "Think back to the time when you first started your education after high school. If you could begin again at that point in time, and taking into account your current experience, would you borrow much less, a little less, about the same amount, a little more or much more?"

  - Half of borrowers said they would borrow "about the same amount" - 50 percent, as shown in Figure 6.
    - Nearly half said they would borrow "much less" or "a little less" - 45 percent.
    - About 5 percent said they would borrow "a little more" or "much more."
  - Responses to this question varied with the ratio of payments to salary.
    - 60 percent of borrowers whose payments are more than 20 percent of salary said they would borrow less.
    - 33 percent of those whose payments were 5 percent of salary or less said they would borrow less.
  - There were no significant differences in the responses to this question from borrowers who received Federal Pell Grant and borrowers who did not receive Federal Pell Grants.

- Responses to this question differed by race/ethnicity.
  - 60 percent of black borrowers said they wished they had borrowed "a little less" or "much less."
    - Black borrowers in the study had similar incomes and debt levels to others, but they were more likely to say that their loans caused them problems.
  - 44 percent of Hispanic and Asian said they wished they had borrowed less.
  - 43 percent of white borrowers said the same thing.

Figure 7. If Borrowers Could Do It Over, Would They Borrow Less?

"If you could begin again . . . would you borrow much less, a little less, about the same amount, a little more or much more?"



Source: National Student Loan Survey, NellieMae 1997

Affect of Other Debt

Student loan debt was not the only debt that affected borrowers. Other debt also had impact.

- The NellieMae 1997 study asked borrowers about other debt:

  "How much do you (and your spouse/partner combined, if applicable) pay each month for all your *non-education loan debts* combined (including car loans, personal loans, mortgage, credit lines, charge cards and credit cards)?"

  - 97 percent of respondents had non-education loan debt, with a median monthly payment of $700.

  - Borrowers had higher average non-education loan debt than average student loan debt.

  - Borrowers with high student loan debt were also more likely to have high non-education loan debt.

    - 22 percent of borrowers with student loan debt over $30,000 had non-education loan payments of more than $2,000 a month.

    - 13 percent of borrowers with $10,000 or less in student loans had monthly non-education loan payments of more than $2,000.

  - Borrowers felt equally burdened by both kinds of debt.

    The NellieMae 1997 report said: "Responses to the question of how burdened they feel by these loans . . . were almost identical to the student loan responses with borrowers who said they felt extremely burdened by student loan payments giving the same response for non-education loan payments."

    "Student loans are often a relatively small part of the debt burden faced by many of these recent graduates, and they do not appear to differentiate between the impact of the two forms of debt on their lifestyles."

- The Higher Education Research Institute conducted a study of student credit card use in the spring of 1998.

  - Nearly 2/3 of the students had at least one credit card.

  - 59 percent of students with credit cards paid off their balances each month.

  - Of the 41 percent who carried balances from month to month, 81 percent paid more than the minimum amount due.

- 86 percent of credit card users paid their own bills, and 14 percent received help from parents or spouses.

- The Higher Education Research Institute study concluded that student credit card use is not very different from credit card use in the general population.

  - In the Federal Reserve Board Survey of Consumer Finances for 1997, 67 percent of families had a "bank-type" credit card.

  - 44 percent of the cardholders carried a balance from month to month.

Repayment Plans Provide Information About Payment Stress

When they went into repayment, borrowers of federally guaranteed loans could choose three types of repayment plans:

1. Level payments - payment of a fixed amount each month for the term of the loan (usually 10 years). Minimum monthly payments were $50.

2. Graduated payments - the monthly payment started low and then increased gradually during the repayment period. Graduated plans had initial monthly payments that were 10 to 40 percent less than level payment plans.

3. Income sensitive payments - payments were based on income. For example, a single borrower with $15,000 in student loans and $15,000 in income paid about $105 per month in the first year of repayment (as compared to about $180 per month on level payments). Income sensitive plans typically had a term of 25 to 30 years. Income sensitive plans had initial monthly payments that were 40 to 50 percent less than level payment plans.

- In a USA Group study of 77,000 borrowers who entered repayment in Fiscal Year 1998, borrowers made the following choices, as shown in the top panel of Figure 8.

    - 91.0 percent chose level payment

    - 8.5 percent chose graduated payments

    - 0.5 percent chose income sensitive payments.

- Thus, in the USA Group study, more than 90 percent of borrowers who began repayment in Fiscal Year 1998 expected to be able to pay the standard monthly amount.

Consolidated Loans

Borrowers were also eligible to consolidate their loans to reduce their monthly payments and to make all of their payments to one servicer. The consolidated loans reduced monthly payments by extending the years of repayment. Consolidated loan borrowers could also choose level payments, graduated payments, or income sensitive payments. Borrowers who were consolidating their loans with level payments did so for periods ranging from 12 to 30 years.

- Borrowers who consolidated their loans through USA Group in Fiscal Year 1998 made the following choices, as shown in the bottom panel of Figure 8.

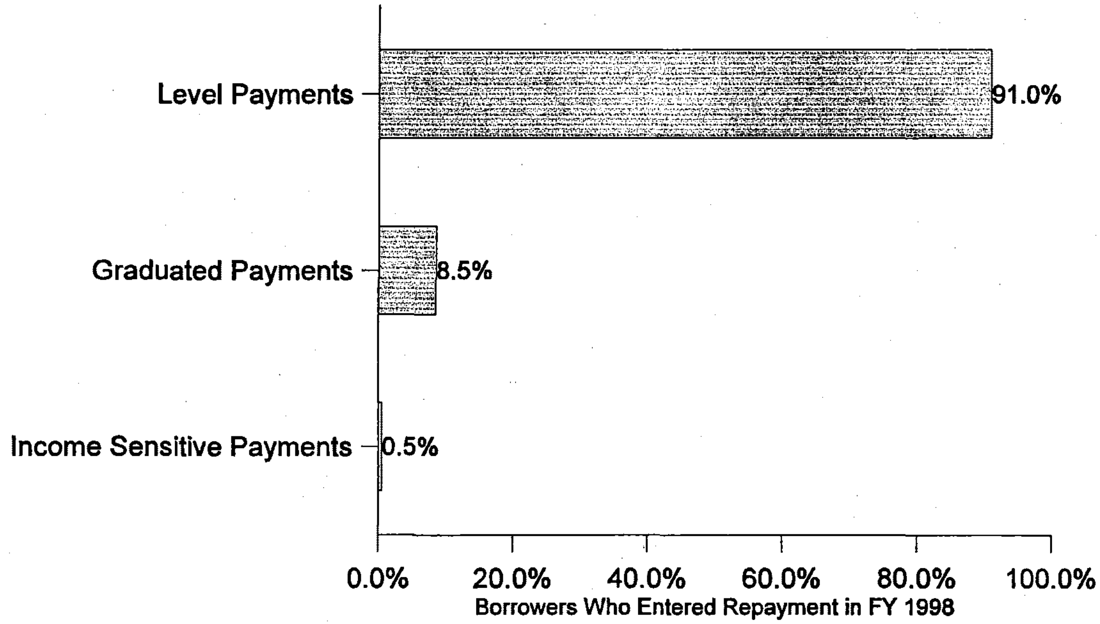
    - 81.5 percent chose level payment plans. Usually the payment plans extended the time of repayment to more than 10 years.

- 18.0 percent chose graduated payments
- 0.5 percent chose income-sensitive payments

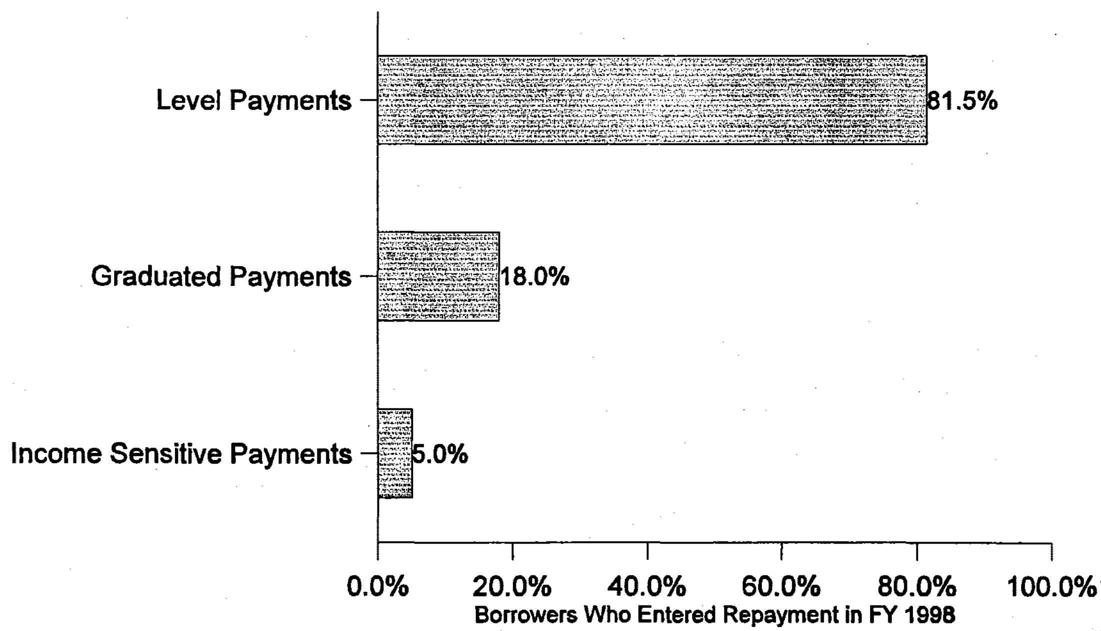
- Thus, more than 80 percent of borrowers who consolidated their payments through USA Group expected to be able to pay the monthly amount in the level payment plans.

Figure 8. Repayment Plans Selected by Borrowers

Borrowers Entering Repayment For the First Time



Borrowers Consolidating Their Loans



Source: USA Group

- It is not surprising that more borrowers who consolidated their loans chose graduated repayment plans. Their motive for consolidating was to lower their monthly payments.

Selection of Repayment Plans	Borrowers Who First Entered Repayment in 1998	Borrowers Who Consolidated Their Loans in 1998
Level payments	91.0%	81.5%
Graduated payments	8.5%	18.0%
Income-sensitive payments	0.5%	0.5%

Deferment, Delinquency, and Forbearance

Lenders use deferment, delinquency, and forbearance to measure the performance of loans.

Deferment

- When borrowers obtained deferments, no payments were due during the deferment.
  - The federal government paid the interest during periods of deferment for Subsidized Stafford Loans.
  - Borrowers owed interest on Unsubsidized Stafford Loans during periods of deferment.
- Deferments were available to borrowers who were:
  - Enrolled in post-secondary education at least half time.
  - Unemployed.
  - Participating in a qualified service program such as the Peace Corps.
  - Had a recognized medical or financial hardship.
- About 8 percent of USA Group borrowers with Subsidized Stafford Loans were in deferment in July 1998, as shown in Figure 9.
- About 9 percent of borrowers with Unsubsidized Stafford Loans were in deferment, as shown in Figure 9.

Delinquency

- Lenders measured delinquency rates to manage potential losses on many kinds of loans.

- USA Group said that about 12 percent of subsidized and unsubsidized Stafford Loan borrowers had payments that were at least 30 days overdue. (Scherschel, 1998)

- In the NellieMae 1997 study, delinquent borrowers had lower incomes than borrowers who were not delinquent.

    - 65 percent of delinquent borrowers reported incomes below $20,000, compared to 35 percent of those who were not delinquent.

    - 18 percent of delinquent borrowers reported incomes over $30,000 compared to 38 percent of those who were not delinquent.

Forbearance

- Borrowers who had trouble making their monthly payments could apply to lenders for forbearance.

    - Forbearance was an agreement between the lender and the borrower for the lender to accept less than the standard monthly payment.

    - Often, borrowers in forbearance made interest-only payments on their loans each month.

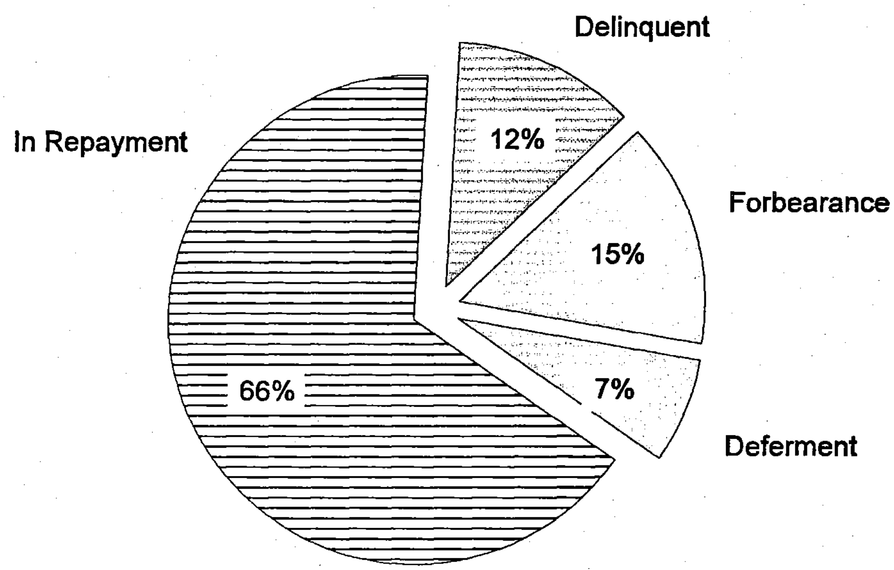
    - Forbearance usually started when the lender or guarantee agency noticed that payments were late on a loan and contacted the borrower with a forbearance proposal to prevent default.

- About 14 percent of USA Group borrowers with subsidized Stafford loans were in forbearance in July 1998.

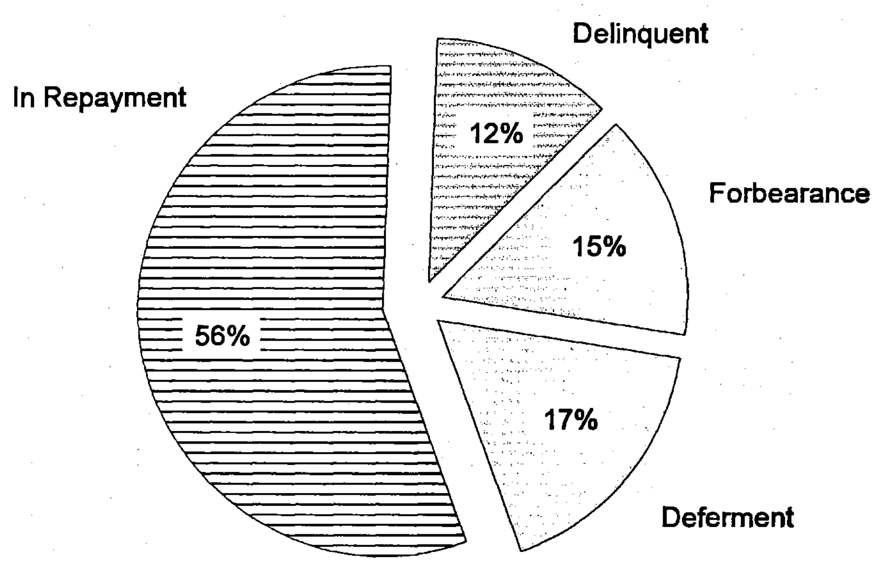
- About 19 percent of borrowers with unsubsidized loans were in forbearance.

Figure 9. Borrower Repayment Status, 1998

Subsidized Federal Stafford Loans



Unsubsidized Federal Stafford Loans

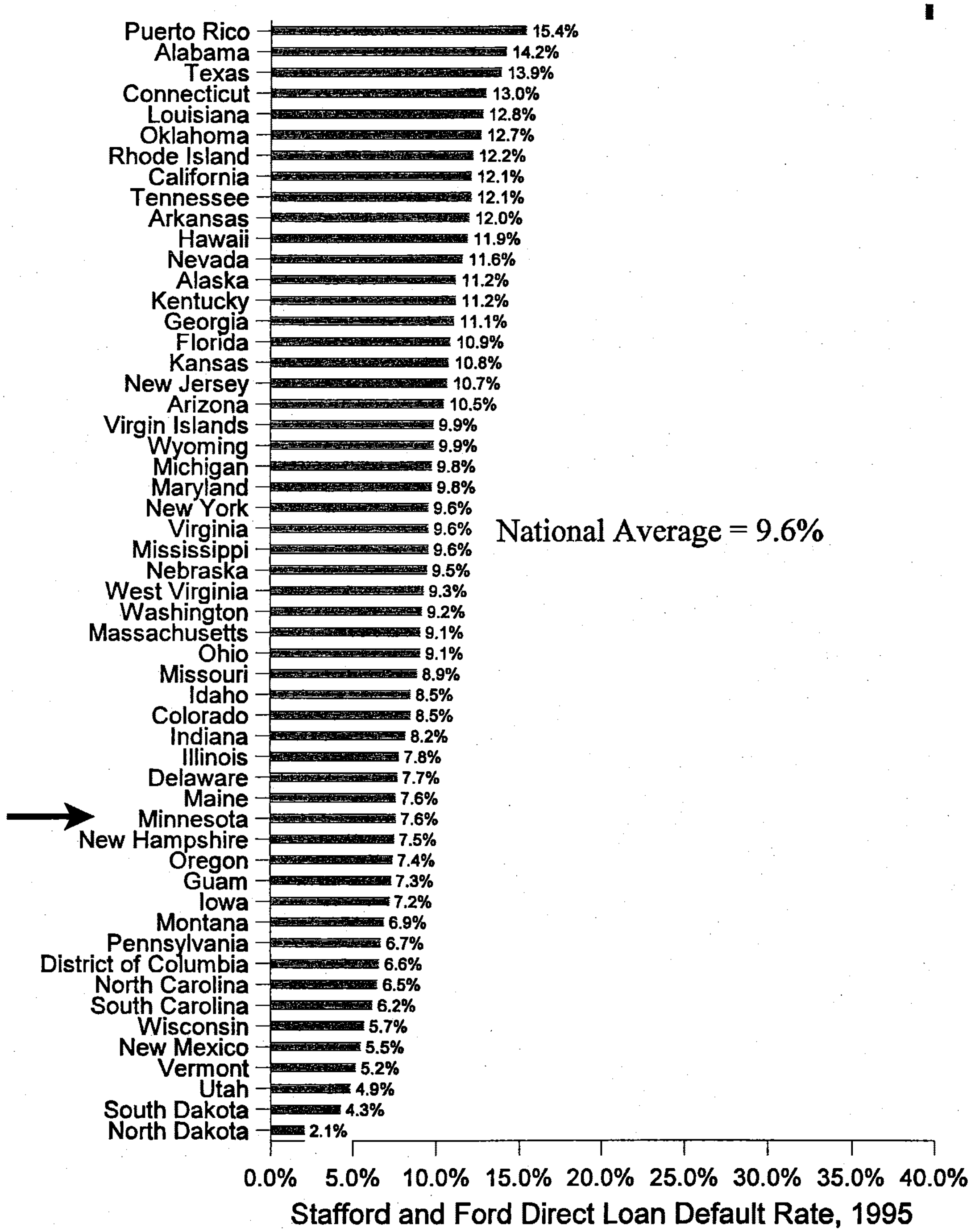


Source: National Center for Education Statistics

Default Rates

- The U.S. Department of Education calculated default rates on federally guaranteed student loans.
    - The federal government reports the most recent available default rates as rates for Fiscal Year 1996.
        - They represented the cohort of borrowers whose first loan repayments were due in Fiscal Year 1996 and who defaulted before October 1, 1997.
- The national cohort default rate for 1996 was 9.6 percent.
- Minnesota's cohort default rate for 1996 was 7.6 percent.
    - Minnesota's default rate is the 16th lowest among the 54 states and territories, as shown in Figure 10.

Figure 10. State Cohort Default Rates on Federal Subsidized and Unsubsidized Stafford and Ford Direct Loans



Source: U.S. Department of Education

Factors Associated With High Default Rates

- In the many studies of the characteristics of borrowers who default on student loans there are two primary characteristics of defaulters.
  - The borrowers did not complete their post-secondary studies.
  - The borrowers had low incomes.
- Usually borrowers who completed more years of post-secondary education had lower default rates.
- Usually borrowers who borrowed larger amounts had lower default rates.

Cohort Default Rates by Sector in Minnesota

- The median default rates among the institutions in each sector were:
  - MnSCU two-year institutions - 11.5 percent
  - Private two-year institutions - 9.7 percent.
  - MnSCU four-year institutions - 5.3 percent.
  - University of Minnesota campuses - 4.3 percent.
  - Private four-year institutions - 3.8 percent.

Some Borrowers Repaid Early

- The NCES Baccalaureate and Beyond study showed that by 1994, 17 percent of 1993 bachelor's degree recipients who had borrowed as undergraduates no longer owed any money on their student loans.
- The NCES Study of 1989-90 Beginning Postsecondary Students showed that by 1994, 23 percent of noncompleters and associate degree or certificate recipients who had borrowed no longer owed any money.

Understanding of How much Debt They Were Accumulating

- The NellieMae 1997 study asked borrowers whether they agreed with the statement "I knew how much total debt I was accumulating when I signed for my education loans."

- Overall, 58 percent of respondents strongly agreed or agreed that they knew how much debt they were accumulating while in school.

  - 20 percent strongly disagreed or disagreed that they understood.

- Responses to this question were strongly correlated with age:

  - 52 percent of those age 24 or younger agreed.

  - 54 percent of those aged 25 to 29 agreed.

  - 70 percent of borrowers who were 30 and older agreed.

- Borrowers who reported that they did not understand how much they were accumulating were also more likely to say they felt burdened by their student loan payments.

  - 46 percent of those who said they did not understand how much they were accumulating said they felt burdened by their student loan payments.

  - 21 percent of those who said they did understand what they were undertaking said they felt burdened by their student loan payments.

Ease of Repayment Over Time

The NellieMae 1997 study asked borrowers:

> "If you have been paying your loan back for three or more years, has it gotten easier to make payments than it was in the first year or two?"

- The survey asked the respondents to choose from four categories: "Much Easier, Somewhat Easier, Not at All Easier, Not Applicable to Me."

- 66 percent of respondents had been in repayment for 3 years or more.

  - Of these, 21 percent said that repaying had gotten much easier over time.

  - 48 percent said that it had gotten somewhat easier to repay.

  - 31 percent said that it had not gotten easier at all.

- 47 percent of borrowers who use over 15 percent of their monthly income to repay student loans said it had not gotten easier at all.

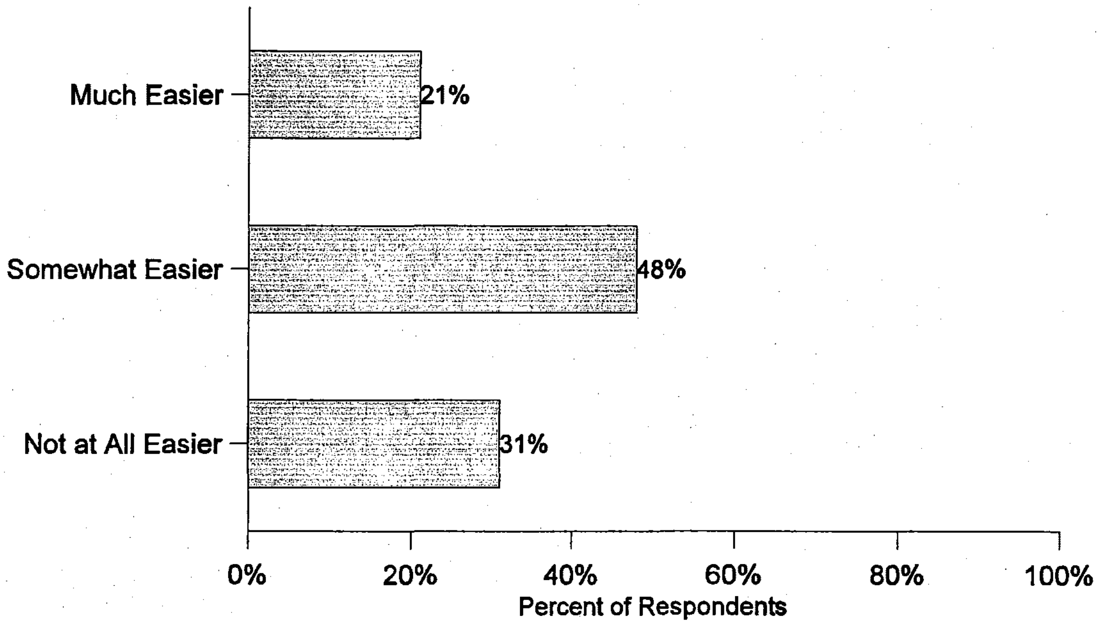
- 24 percent of borrowers who use 10 percent or less of their monthly income to repay student loans said it had not gotten easier at all.

Some Borrowers Received Help From Parents

- The NCES Survey of 1989-90 Beginning Postsecondary Students showed that in 1994 13 percent of noncompleters, associate degree and certificate recipients who were making payments were receiving help from relatives or friends.
  - 7 percent of those from families in the lowest salary quartile
  - 17 percent of those from families in the two middle salary quartiles.
- In the NellieMae 1997 study, 77 percent of respondents said they received no help from parents in repaying.
  - Among the 23 percent of borrowers who received help, the amount of help varied.
    - 9 percent said their parents paid 10 percent or less of their loan payments to date.
    - 5 percent said their parents paid 10 to 20 percent
    - 3 percent said their parents paid 20 to 40 percent
    - 4 percent said their parents paid 40 to 60 percent
    - 2 percent said their parents paid 60-90 percent
    - 3 percent said their parents paid 90-100 percent

Figure 11. Did Repayment Become Easier With Time?

"If you have been paying your loan back for three or more years, has it gotten easier to make payments than it was the first year or two?"



Source: National Student Loan Survey, NellieMae 1997

Did the Debt Affect Major Life Decisions and Career Choices?

The Effect of Borrowing on Type of Work

- The Baccalaureate and Beyond Longitudinal Study asked 1993 bachelor's degree recipients whether various factors were important to them in determining the type of work they (the bachelor's degree recipients) planned to do in the future.

  - The responses provided no evidence that borrowers were making career choices differently than nonborrowers.

    - For example, 45 percent of borrowers and 45 percent of nonborrowers said that "good income potential" was important to them in determining the type of work they (the bachelor's degree recipients) planned to do.[2]

    - 76 percent of borrowers said their job in April 1994 was closely related or somewhat related to their degree. 74 percent of nonborrowers said the same thing.

- The NellieMae 1997 study asked borrowers to respond to the statement:

  "Because of my education loan debt, I significantly changed my career plans."

  - About 17 percent "strongly agreed" or "agreed" with this statement.

  - 70 percent of respondents disagreed.

Job Security

- When NCES surveyed of 1989-90 beginning post-secondary students in 1994, job security was very important to nearly all of the students who were noncompleters, associate degree, or certificate recipients.

  - However, job security was even more important to borrowers than it was to nonborrowers.

    - 92 percent of borrowers said that job security and permanence was very important in determining the kind of work they planned to be doing for most of their lives.

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2 This compares to 75 percent of freshmen who gave the desire to "make more money" as a reason for attending college in The *American Freshmen: National Norms for Fall 1998*, by Alexander Astin, of UCLA..

- 86 percent of nonborrowers said the same thing.

Marriage

- In the NCES Baccalaureate and Beyond survey, the 1993 bachelor's degree recipients with loans were just as likely to marry between graduation and 1994 as those without loans.

- In the NellieMae 1997 study, debt also did not appear to have an impact on whether borrowers were married.

- In the NellieMae study, 16 percent of respondents had spouses with undergraduate debt.

    - 7 percent had spouses with undergraduate debt of more than $10,000.

    - "In other words, the phenomenon of borrowers with high education debt levels marrying others with high debts does not seem pervasive."

Living With Parents

- The NCES Baccalaureate and Beyond Study showed that in 1994, living with parents was more related to age than indebtedness. Older bachelor's degree recipients were more likely to be living separately from parents.

    - However, borrowers with education loan payments that were a higher percent of salary were more likely to be living with parents.

        - When education loan payments were less than 5 percent of salary, 22 percent of graduates lived with parents in April 1994.

        - When payments were 5 to 9 percent of salary, 26 percent lived with parents.

        - When payments were 10 to14 percent of salary, 29 percent lived with parents.

        - When payments were 15 percent of salary or more, 35 percent lived with parents.

- 21 percent in the NellieMae 1997 study said that their debt was important or extremely important in causing them to delay moving out of their parents' home.

    - However, their behavior differed from this perception. When the analysis controlled for other factors related to living apart from parents (age, being married, having children), borrowers with higher debt and higher payment to income ratios were no more likely than other borrowers to be living with parents.

Having Children

- 22 percent of borrowers in the NellieMae study said that their student loans had caused them to delay having children. The amount of the loans did not appear to have impact.
    - However, this perception was not reflected in actual behavior. When the analysis controlled for other factors related to having children (such as age and being married), those with higher debt or higher payment to income ratios were no less likely to have children.

Major Purchases

- In the NellieMae 1997 study, 31 percent said that their student loan debt was important or extremely important in causing them to delay purchasing their own car.
    - Among those whose payments were more than 15 percent of income, 30 percent said their student loan debt was extremely important in causing them to delay purchasing a car.
    - Among those whose payments were less than 10 percent of income, 10 percent expressed this opinion.
- 40 percent said that their student loans caused them to delay buying a house.
    - However, this perception was not reflected in actual behavior. When the analysis controlled for other factors related to home ownership (age, being married, having a higher income, having children), those with higher debt or higher payment to income ratios were no less likely to own a home.

Saving

- In the Baccalaureate and Beyond survey, among 1993 bachelor's degree recipients making loan payments, 71 to 77 percent of those working full time said they were saving.
- Those paying 15 percent (or more) of salary in education loan payments were more likely to be saving than those paying less than 5 percent.
    - Among those with education loan payments of 5 percent or less, 16 percent said they were saving for further education.
    - Among those with payments of 5 to 9 percent, 22 percent said they were saving for further education.

- Among those with payments of 10 to 14 percent, 19 percent said they were saving for further education.

- Among those with payments of 15 percent or more, 28 percent said they were saving for further education.

Borrowing and Further Education

Withdrawing Without Completing an Undergraduate Program

- The NellieMae 1997 study asked borrowers the following question:

  "If you left school before completing your program, how important was concern over borrowing in preventing you from staying in school?"

  - 50 percent of borrowers who did not stay in school to complete their degrees chose "extremely important" or "very important" in response to this question.

    - 31 percent of these borrowers chose "not important."

  - Responses to this statement varied by racial/ethnic group.

    - 69 percent of black borrowers who did not complete a degree said that loans prevented them from staying in school and completing a degree.

    - 71 percent of Hispanic borrowers who did not complete a degree said the same thing.

    - 70 percent of Asian borrowers who did not complete a degree said that loans preventing them from completing.

    - 43 percent of white borrowers who did not complete a degree said the same thing.

Enrolling in Graduate School

- Borrowing appears to affect enrollment in graduate school.

  - 1993 bachelor's degree recipients who borrowed were slightly less likely than nonborrowers to apply to graduate school by spring 1994.

    - 27 percent of borrowers applied to graduate school.

    - 30 percent of nonborrowers applied.

  - Bachelor's degree recipients who said they had considered applying to graduate school but then had not applied were asked the primary reason they had not applied.

  - 10 percent of those who had borrowed as undergraduates said that having too much undergraduate debt was their main reason for not applying.

    - ■ 5 percent of those who borrowed less than $5,000 gave this reason.

    - ■ 20 percent of those who borrowed $20,000 or more gave this reason.

- In the NellieMae 1997 study, 43 percent of respondents said their undergraduate debt was extremely or very important in preventing them from going to graduate school.

  - o 28 percent said this was not important.

- Half the Federal Pell Grant recipients in the NellieMae study said that their undergraduate debt had prevented them from attending graduate school, compared to 38 percent of those who did not receive Federal Pell Grants.

- In the NellieMae 1997 study, 39 percent of those who borrowed for undergraduate education said that concern over borrowing was extremely important or very important in preventing them from attending a more expensive graduate school, compared to 33 percent who said it was not important.

What a Borrower Can Do If He or She Has Defaulted and Wants to Return to School

If a borrower who defaulted later wants to return to school, federal rules prohibit that borrower from getting another federally guaranteed loan.

- However, if the borrower has made satisfactory arrangements to repay the defaulted loan, then the borrower is eligible to apply for federally guaranteed loans.

  - o The phrase "satisfactory arrangements to repay" means a set of payments that show to the lender's satisfaction that the borrower is sincere about repaying.

    - For example when a lender has received six months or more of steady payments, the default is considered "cured."

    - A borrower with a cured default is usually eligible to apply for additional loans.

  - o Default statistics do not reflect the defaulted loans that borrowers later repay.

Do borrowers think the loans were worth it?

Most borrowers said they thought the loans were worth the trouble of repayment.

Continuing Their Education

In the NellieMae 1997 study, 76 percent of respondents said that student loans were extremely or very important in allowing them to continue their education after high school.

Personal Growth

The NellieMae study asked:

> "To what extent are you satisfied that the education you "invested in" with your student loan(s) was worth the investment for personal growth?"

- 76 percent said that the investment they made in their education through borrowing was worth it for personal growth.
  - This was true even for borrowers who were delinquent - 57 percent of delinquent borrowers said it was worth it for personal growth, and 78 percent of borrowers who were not delinquent said it was worth it.

Career Opportunities

About 64 percent said that the investment they made in their education through borrowing was worth it for the career opportunities it provided.

- Delinquent borrowers were less likely to agree with this statement.
  - 35 percent of delinquent borrowers disagreed compared to 17 percent of those who were not delinquent.

Loans Are Unpleasant, but Worth it

The NellieMae 1997 study asked borrowers whether they agreed with the statement:

> "Making loan payments is unpleasant but I know that the benefits of the education loans are worth it."

- About 66 percent of borrowers agreed or strongly agreed, as shown in Figure 12.

- 10 percent disagreed with this statement. The rest were neutral.

- Borrowers with debt above $30,000 were the most likely to agree that while repaying student loans is unpleasant the benefits were worth it.

  - 29 percent with debt of $10,000 or less strongly agreed.

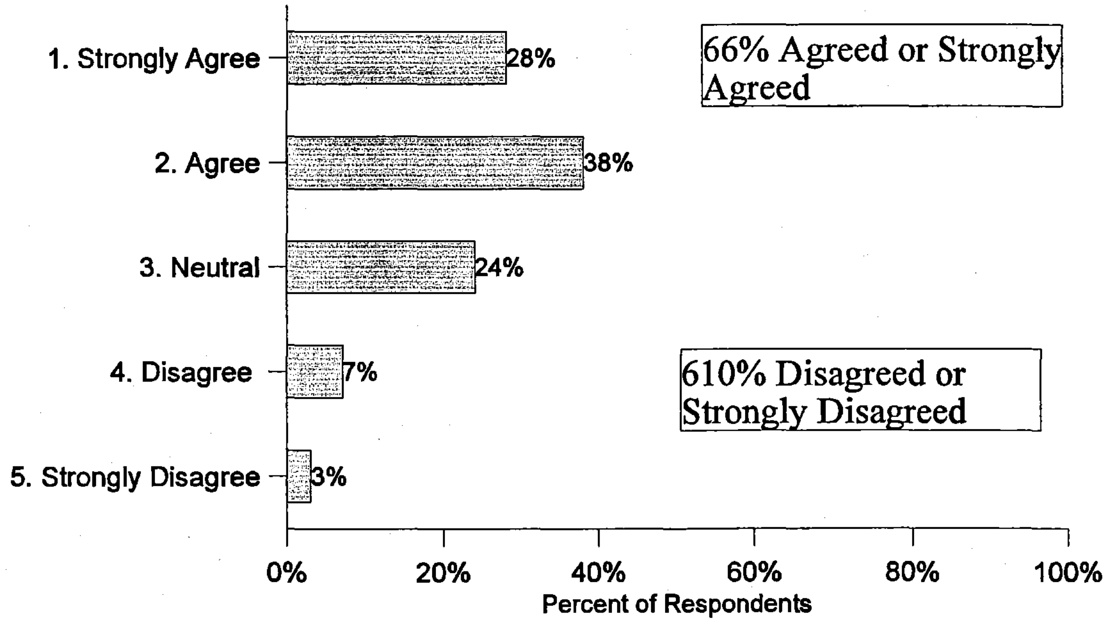
  - 27 percent with debt between 10,001 and $20,000 strongly agreed.

  - 24 percent with debt between $20,001 and $30,000 strongly agreed.

  - 35 percent with debt above $30,000 strongly agreed.

Figure 12. Repayment Was Unpleasant, But Worth It

"Making Loan payments is unpleasant but I know that the benefits of the education loans are worth it?"



Source: National Student Loan Survey, NellieMae 1997

Allowing Students to Attend the School of Their Choice

About 64 percent of respondents said that student loans were extremely or very important in allowing them to attend the school of their choice, 13 percent said that loans were not important in this regard.

Continuing Education After High School

Most Federal Pell Grant recipients reported that loans were extremely or very important for continuing education after high school - 82 percent agreed with this statement as compared to 72 percent of those who did not receive Federal Pell Grants.

Did Debt Counseling Help?

Federal rules required borrowers who received federally guaranteed loans to receive loan counseling when they first took out a student loan (entrance counseling) and before leaving school (exit counseling).

- In the NellieMae 1997 survey asked whether they agreed with this statement:

  "The student loan/debt counseling I received from my school informed and prepared me for repayment."

  - 37 percent strongly agreed or agreed that loan counseling had prepared them to repay their loans.
  - 40 percent strongly disagreed or disagreed.
  - 23 percent were neutral.

- Sentiment about whether loan counseling had prepared them varied by the type of institution attended.

  - Among those who last attended public four-year, private four-year, and private two-year institutions, 42 to 48 percent of borrowers disagreed with the statement that loan counseling had prepared them to repay their loans.
    - 31 to 42 percent of these borrowers agreed with the statement.
  - Among those who last attended vocational/technical institutions and public two-year institutions, about 50 percent agreed with the statement.

- 27 to 32 percent disagreed with the statement.

Discussion

Is Borrowing a Valid Way of Financing Post-Secondary Education?

- Attitudes toward borrowing as a policy issue reflect different beliefs about who should pay for post-secondary education.
  - These attitudes also reflect the historical changes in financing post-secondary education.
  - Many people discussing borrowing today remember financing their own post-secondary education with little or no borrowing.
- The following belief underlies many discussions of student borrowing:
  - Those who pursue post-secondary education should not have to borrow to do so.
    - Part of this belief is an attitude that loan repayment is a problem if it has *any* impact on the standard of living of the borrower.
    - Sandy Baum, professor of Economics at Skidmore College said: "Much of the concern over borrowing levels emerges from the sense that because access to higher education should be a right for all who can benefit from it, it somehow should not involve sacrifice. But every choice we make about how to spend our money involves sacrifice." (*Education Record,* Winter 1996)
  - Media reports are often based on borrowers with unusual circumstances.
  - Baum also said: "Few firms assume they should finance their capital investments entirely out of retained earnings and current income. Few families feel compelled to finance their homes entirely out of savings and current income." (*Educational Record,* 1996)
- Some people think borrowing is an acceptable to finance post-secondary education.
  - Perhaps the complainers speak up and those who do not see it as a big problem remain quiet.

Borrowing Represents a Shift in Financial Responsibility

- Borrowing represents a shift in financial responsibility from parents to students.
  - Minnesota's Design for Shared Responsibility assigns students the primary responsibility in paying the recognized price of attendance.

- The assigned student responsibility is the amount that students are expected to invest in themselves.

- Students can make this investment with past income (savings), current income, or future income (loans).

- Families are second in line in assigning responsibility.

  - The assigned family responsibility is the amount that families are expected to invest in the post-secondary student.

  - Families can also make this investment with past income (savings), current income, or future income (loans).

    - Few parents borrow to finance a dependent student's post-secondary education.

- Most of the savings used for post-secondary education come from parents.

- Most of the money used to repay student loans comes from students.

Many Borrowers Say That Loans Were Necessary to Attend

- Most borrowers say that the loans were very important to their ability to attend.

- William Chance, in *Essay on the Contours of a New Partnership: Reconsideration of the Federal Student Loan Program* (1995) made an interesting observation:

  - "Student loans have become a way for unequaled numbers of people to afford a college education at a lighter load of indebtedness than the cost of a moderately equipped car."

Repayment Is a Problem for Some Borrowers

- Borrowers with low incomes after leaving school are at greater risk of having repayment problems.

  - If the low income persists for several years, the impact of the debt on the borrower is likely to be very negative.

  - For many borrowers, incomes increase over time, while debt payments remain constant.

    - Thus, many borrowers find that the impact of their student loans declines with time.

- Even if debt burdens are manageable over time, they may look unmanageable in advance, and thus deter attendance (Baum, 1996).
    - There is more uncertainty and risk associated with debt than there is with savings or current income.

Most Borrowers Say that Repayment Is Unpleasant, but Worth It

- Most borrowers said they would borrow about the same amount if they had it to do again.
- Most borrowers said that repayment was unpleasant, but worth it.

Many Borrowers Think Loans Are a Good Way to Pay for Post-secondary Education

- Most borrowers have seen an increase in earnings because of attending post-secondary education.
    - In 1997, workers with a high school diploma earned an average of $23,250. Workers with a bachelor's degree earned an average of $41,106. This is a 77 percent difference in earnings. (U.S. Census Bureau, Current Population Survey)
    - Those with some college but no degree earned 15 to 20 percent more than those with a high school diploma.
    - Those with associate degrees earned 20 to 30 percent more in 1997.
- Some financial advisers told parents that could pay for college out of savings and income to have their child borrow.
    - In a *St. Paul Pioneer Press* article on May 16, 1999, Gail MarksJarvis quoted Ray Loewe, a consultant with College Money in Marlton, NJ:
        - "It's good for the child to contribute something toward their education. It helps them establish credit and feel vested."
        - In addition, "rates on federal Stafford loans are so attractive parents who have money in stocks or stock mutual funds may want to let the investments build while having their child borrow money. After college . . . parents can help their children pay off the loans."
        - Loewe "advises his clients to borrow the maximum $17,000 for undergraduate education."

  - Loewe thinks borrowing is generally preferable to using retirement money. "Anyone will loan you money for college, but I haven't seen anyone willing to loan people money for retirement."

  - Loewe gives this example for a family that is "getting financial aid but still struggling . . . A family receiving $15,000 in aid [grants] for a college that charges $30,000 a year, decides it's nervous about taking on more debt. Instead of borrowing $30,000 the couple cashes in stock that's worth $40,000 – one they originally purchased for $10,000. The family's income, because of that transaction, just went up substantially. And next year that will probably cost them about $11,000 in financial aid [grants]."

- In the same Pioneer Press article Mick Endersbe, of American Express Financial, "tells his clients to borrow, and likes Minnesota SELF Loans because they currently carry only a 5.75 percent interest rate."

  - Ken Richard, a Roseville financial planner also says "the Minnesota Self loans are more attractive than the federal ones" right now.

- Gail MarksJarvis said: ""Parents sometimes turn to PLUS loans so they don't burden the children. But advisers tell parents to take the lower rates available on Stafford Loans, and simply help the child with the payments."

- In addition she says "One attraction of borrowing . . . would be to get an immediate tax advantage. . . . They can deduct a portion of the interest on college loans from their taxes.

Borrowing Is Here to Stay

- Before the start of federal student loans in 1965, it was generally believed that private lenders would not provide loans for post-secondary education because there was no collateral.

- With the creation of federally guaranteed loans in 1972, lenders became willing to provide loans for post-secondary education.

- In 1999, not only is there a large volume of federally guaranteed borrowing, but private lenders also offer uninsured education loans.

- After more than 25 years of federally guaranteed student loans it may be too late to stop students from borrowing, even if the government decided to do so.

- If the government closed down student loan programs, it is likely that private lenders would move into the market.

Who Decides What Level of Debt Is Appropriate?

- One borrower may find payments of 8 percent of income to be too much of a sacrifice. Another borrower may find payments of 15 percent of income to be very worthwhile.

- The role of government in borrowing is ambiguous.

  - Some borrowers are likely to feel the government (or the institution) encouraged them to borrow "too much."

  - Other borrowers are likely to feel the government should have a limited role in the decision of how much they can repay, unless they are delinquent.