

Solutions for the Student Loan Debt Crisis

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Abstract

Our team conducted research on student loans and the cause of the student loan crisis. We determined that there are many factors that come into play that determine if a student can pay for college, as well as many reasons why the student loan crisis is occurring. Among these reasons are poor education, the lure of loan forgiveness, and a poor system of giving our financial aid, to name a few. Because our team believes that the system for funding higher education needs change, our solution is to change the way financial aid is calculated to allow students to be able to receive more aid.

Introduction

Students in the U.S. are no stranger to debt. By the time they graduate college, the average college student has about \$29,000 in student loan debt (College Board, n.d.). Students don't know how to avoid these massive loans. For many, there is an expectation that if they participate in college, they will have to go into debt to pay for it. In the United States, the total amount of student loan debt currently exceeds \$1.6 trillion. This figure is higher than the collective credit card and auto loan debts and is second only to mortgage loans (Friedman, 2019). Based on these disturbing figures, it is clear that the system for funding higher education needs massive reformation so college students can elevate their Financial Capability upon attaining their desired degree. The reason this subject is important is that if it is not addressed, the collective student loan debt will continue to increase, potentially causing severe problems for the US economy. At an individual level, this subject is important because no person or family should have to live with crippling student loan debt.

Background Information

Paying for college is a big deal and when they do not have the money, college students have different options at their disposal that can help them to pay for college. The main options available for college students to fund their higher education are loans, grants, and scholarships. The first option, loans, is an amount of money that is lent to someone and is expected to be paid back at a later date, usually with an interest. There are two main types of loans: Federal and private. Federal loans are funded by the government and usually offer many benefits, like fixed interest rates and income-driven repayment plans. These loans are usually paid after the student has graduated. Private loans are made by private organizations such as credit unions, banks, and state-affiliated institutions; and have terms and conditions that are defined by the lender, which is why they may not offer as many benefits as federal loans. These loans may be paid while the student is in school, although some allow the student to pay back after graduation. The second option, grants, are money that is given to a student based on financial need and are not expected to be paid back. The third option, scholarships, are similar to grants except that these are given based on merit, meaning they are awarded to students with high academic or athletic achievements.

Literature Review

The Reimagining Aid Design and Delivery (RADD) project which seeks to identify and develop innovative postsecondary financial aid solutions that ensure continued access while also increasing success for low-income students. The RADD project was created by the Institute for Higher Education Policy (IHEP), a non-profit organization that aims to foster access and success in postsecondary education through public policy research and other activities that inform and influence the policymaking process.

The Higher Education Tax Reform, a publication that discusses different proposals for reforming higher education tax benefits. This publication was carried out by a consortium between the Center for Postsecondary and Economic Success at CLASP, Young Invincibles, the New America Foundation's Education Policy Program, and The Education Trust.

Terms and Definitions

Expected Family Contribution (EFC): It is a measure of your family's financial strength and is calculated according to a formula established by law.

Free Application for Federal Student Aid (FAFSA): It is a form completed by current and prospective college students in the United States to determine their eligibility for student financial aid.

Cost of Attendance (COA): It is the amount it will cost a student to go to school.

Federal Loans: These are loans made by the government, with terms and conditions that are set by law.

Private Loans: These are loans made by private organizations such as banks, credit unions, and state-based or state-affiliated organizations, and have terms and conditions that are set by the lender.

Subsidized Loans: These loans are based on financial need and the interest does not accrue while the student is in college, as the interest is paid by the federal government.

Unsubsidized Loans: These loans are not based on financial need and the interest starts to accrue when the student is studying.

Research Design and Design Thinking

Research Design

For our research design, we dividend the work evenly into sections between the 3 of us. We used a chart to organize our research citings with the person's name to the left following with the information they found from the article. The chart was split into three parts with the sub-topics “Causes of the student loan debt crisis”, “Methods for funding higher education”, and “Methods to avoid student loan debt”. Each person was assigned a sub-topic and had to find the required information.

Research Materials

There aren't many ways to save money and avoid student debt when it comes to college. Not many websites can help you calculate how much money you will spend by depending on your dream college, but Student Loan Hero will help your student loan by comparing options to save money on the cost of borrowing. They can help you find the top private student loan lenders to help you make an informed decision.

payout

Education and Financial Literacy

There are many reasons the collective student loan debt is at its whopping \$1.6 trillion figure today. For starters, many college students just aren't knowledgeable enough to make hefty financial decisions such as taking out 5 and 6 figure loans. Without this critical information, it is easy to see how students can exhibit poor judgment when it comes to funding their higher education. According to the National Association of Student Financial Aid Administrators, a survey from EverFi showed that on a six-question test on basic Financial Literacy concepts, the average score out of over 100,000 students was a two (Bidwell, 2018). How can college students

be expected to make smart financial decisions when the average score on a basic Financial Literacy test was 33%? The statistics in Florida are especially damning; Survey data shows that 69% of people are unable to answer three or more questions right on a five-question Financial Literacy test. The same survey from just two years ago showed that 58% of Floridians don't even compare credit card information between different companies, instead most people just sign up with the first company that they stumble upon (Financial Industry Regulatory Authority, n.d.). The disturbing part about these last statistics is that this survey was not given to strictly college students. This means that grown adults were among this group of people who couldn't pass a simple Financial Literacy test. A lack of education is one of the driving factors as to why there are trillions of dollars of collective student loan debt in America.

Loan Forgiveness

Another reason why student loan debt may be so high is because of loan forgiveness. Loan forgiveness is a plan where you don't have to pay for a portion of your student loans if you meet certain requirements after you have graduated. According to the Federal Student Aid Office of the Department of Education, "[Public Service Loan Forgiveness (PSLP)] forgives the remaining balance on your Direct Loans after you have made 120 qualifying monthly payments under a qualifying repayment plan while working full-time for a qualifying employer" (n.d.). On the surface, this might seem like a good deal for college students because they won't have to pay for a portion of their debt. The problem with loan forgiveness, however, is that in a lot of cases it can make college students more lenient to take out larger loans, with the expectation that they will qualify for loan forgiveness and not have to pay it all back. If the loan forgiveness program is modified or outright removed, or if a college student is unable to qualify for the program, they will end up worse than they would if they had simply taken out a cheaper loan. Rebecca Lake

puts it like this: “[Loan forgiveness is] a tempting prospect, which may lead students to lean on loans more heavily, with the expectation that they'll be forgiven later. But, the program isn't permanent and could be altered or canceled, making it risky for borrowers to count on loan forgiveness” (2020). Although loan forgiveness might sound like a great way for students to fund their higher education, when you consider what percentage of students are even eligible for loan forgiveness, you quickly find that it is not worth it to take out a larger loan. Data from the Federal Student Aid Office Department of Education from May 2020 showed that out of 187,053 applications, only 3,697 qualified for Public Service Loan Forgiveness (2020). College students take out larger loans thinking they won't have to pay all of it because of loan forgiveness, not realizing that less than two percent of applications even qualify in the first place. Yes, loan forgiveness is a way for a small percentage of graduates to be relieved from some of their debt, but it's also a way for college students to justify taking out massive loans, only to realize that their lack of research into PSLP acceptance rates will inevitably cause them thousands of dollars.

Financial Aid

Financial aid is one way that college students can get help paying for their tuition fees. It can come in many forms, such as grants and scholarships, work-study jobs, and of course, federal and private loans. These four main groups can be split into need-based and merit-based financial aid. According to professional researcher Alice Garnett, “The primary difference between these two types of financial aid is that merit-based scholarships, unlike need-based financial aid, are awarded to students based on academic or other merits rather than demonstrated financial need” (n.d.). Merit-based financial aid includes academic grants or the Bright Futures Scholarship here in Florida. In both cases, a student has to work or meet a certain requirement to receive a pre-set amount of money. Need-based financial aid is based on

individual needs and is determined by your information filled out on your Free Application for Federal Student Aid (FAFSA). An example of this is the Pell Grant, which is a grant that focuses on giving money to students from lower-income families. The money you will receive from this type of aid is determined by calculating your Expected Family Contribution (EFC) and subtracting it from your Cost Of Attendance (COA) for the school you are applying to (Federal Student Aid, n.d.). The main factor in this calculation is your EFC because students taking the same classes and living in the same dorms or type of housing will have similar COAs. According to the official formula for calculating EFC, your EFC is based almost entirely on your family's income. Simplified, the actual amount of EFC is calculated by taking your parents' total income minus their tax allowances and dividing that number by the number of their kids that are in college. This number is summed with the individual student's income minus their allowances, to get their actual EFC (Federal Student Aid, n.d.). Private and Federal Student Loans can also be considered need-based because the amount that you take out is dependent on what you are already able to pay. Federal Work-Study, as described by the Federal Student Aid Office, "provides part-time jobs for undergraduate and graduate students with financial need, allowing them to earn money to help pay education expenses" (n.d.). This can be useful for students who are still unsure what career they want to focus on, or those who are simply struggling to find a job to start paying off student loan bills.

Automation and Its Role in the Job Industry

A lot of people aren't paying their student loans because they're losing their jobs. Many company employers are handing out pink slips to their employees because of automation. Automation is one of the main causes of student debt. According to Student Loans Advice, Automation will replace millions of blue-collar jobs but it doesn't stop there. Many white-collar

jobs are at risk such as accountants, airline pilots, and pharmacists, and with the wave of automation replacing jobs, more people are pushed into advancing their education. Over 2% of Americans - 7 million people - lost their jobs in mass layoffs between 2004-2009. Workers without a college degree are, particularly at risk. As production met automation and moved overseas, the broader citizenry enjoyed cheaper products while large sectors of the workforce were left with a loss of livelihood. Harvard Fellow in Technology and Public Purpose Susan Winterberg shared that laid-off workers typically see a permanent 17-30% reduction in wages when they return to the workforce.

Unused Financial Aid Funds

Even though need-based aid such as the Pell Grant can help pay a large sum of tuition fees, a great amount of this money goes unused every year. In Florida alone, high school graduates missed out on over \$100 million in Pell Grants in 2013. Completing the Free Application for Federal Student Aid, or the FAFSA is a critical step to be considered eligible to obtain financial aid from the \$150 billion in federal grants, loans, and work-study funds that help students pay for their college. However, not all students take advantage of this opportunity, with only 55% of all Florida high school graduates completing the FAFSA during the 2012-13 school year. Nationwide, the class of 2018 missed on \$2.6 billion in Pell Grants. All this amount was unclaimed since about 661,000 high school graduates didn't complete their FAFSA.

Data Analysis

The collective student loan debt in the US is \$1.6 trillion today. According to the National Association of Student Financial Aid Administrators, a survey from EverFi showed that the average score out of over 100,000 students was two on a six-question test on basic Financial Literacy concepts. Survey data shows that 69% of people are unable to answer three or more

questions right on a five-question Financial Literacy test. The same survey from just two years ago showed that 58% of Floridians don't even look at and compare credit card information from different companies, instead, signing up with the first company that they stumble upon. Data from the Federal Student Aid Office Department of Education from May 2020 showed that only 3,697 out of 187,053 applications qualified for Public Service Loan Forgiveness. High school graduates missed out on over \$100 million in Pell Grants in 2013, in Florida alone.

Personal Stories

Barbara J. Allen

Our Virtual Mentor, Barbara J. Allen, stated she was awarded a full-ride academic scholarship to attend college. It was not renewed after her first year because she did not meet the terms of the scholarship. Barbara was one of the fortunate ones who graduated without any student loan debt. Her daughter graduated as a Nurse Practitioner in 2019. She amassed over \$80,000 in student loan debt and had a hard time paying it back. The situation was very stressful for her and her family. Barbara is now a member of a business association who awards scholarships and this year we had less than 10 students apply for four scholarships. Creativity and persistence are key.

Nadja Rivera

Nadja Rivera, our second mentor, stated she incurred a lot of student loan debt because nobody oriented her as to how those loans work. She took them and was able to complete her Bachelor's (undergraduate) degree. When she went on to Graduate school for her Master's degree, she had grown and wasn't as naive. Her strategy was: pay out of pocket even if it takes you longer to finish, and that's exactly what she did and she finished in 3 years because she paid as she went and only by what she could afford semester after semester. Nadja completed the Master's in 3

years instead of the usual 2 yrs because of it, but Nadja says it was the smartest decision she made.

Edna Forero

Edna Forero, our third mentor, says she was much like others who used their student loan refunds to fund household expenses. She was paying for my apartment and trying to work while going to college in Houston, TX. When she graduated she had \$21,000 in debt and 2 bachelor's degrees. When she got married, her husband's military career took them all over the country. Edna moved 13 times and had 4 children. She had only paid off \$15,000 and paid about \$13,000 of her husbands. Years later, Edna and her husband created their own home business and took in extra hours at work. Her original debt was \$21,000, twenty-three years later she owed \$37,000. Edna knew her original loans were necessary for her to graduate but small minimum payments cost so much more.

Research Outcomes

There are many things to take away from our research, as well as many problems that we have identified on an individual level and a federal level. For one, there seems to be a severe lack of education on an individual level. College students simply don't have the financial capability to make smart financial choices and to fund their higher education. This, coupled with the fact that college loans can be confusing and sometimes purposefully misleading, makes it obvious why so many students struggle with student loans and help explain why the collective student loan debt is so high. As discussed earlier, loan forgiveness is also a contributing factor as to why so many students end up with massive amounts of student loan debt. Loan forgiveness encourages students to take out higher amounts of student loans, with the expectation that they will be able to be "forgiven" for them later. The problem is students don't realize that because so few

students qualify for loan forgiveness, it is in no way worth it to take out a larger loan with the hopes that the government will excuse it later. Financial aid also has problems in the way that it's calculated and distributed. Because a student's Expected Family Contribution (EFC) is based almost entirely on income, their financial aid will not be based on their actual wealth, in terms of income and expenses. This is a problem because a family with a higher income but equally high expenses from debt payments from student loans or costlier house payments because of the area they live in is less wealthy than a middle-class family who doesn't have all these expenses and has more money to spend at the end of the day. But because the current formula only takes into account family income, the middle-class family with more wealth will receive more financial aid, despite being able to contribute more to a college education.

Solution

Our solution is to change the way financial aid is calculated and given out. Since the formula for EFC for calculating financial aid mainly only takes into account income, our solution would include changing the way this formula is written out. Our team would propose that this formula also takes into account expenses for families as well. These expenses would include previous loan payments such as mortgages and student loan payments. This updated formula would also take into account utilities and rent for a family before deciding what their EFC is. Essentially, expenses would be calculated along with income to get a better sense of that family's wealth. This formula would make it so that families with high incomes who aren't wealthy because they have high expenses would still be able to obtain a decent amount of financial aid. Families who have higher mortgages or car payments than the median expenses in their area will default to these median values on the calculation sheet. In other words, families whose expenses are higher in their local area for these categories would default to the median on the EFC. The idea is that if

someone goes out and buys an expensive house or car because they have a lot of excess money, we wouldn't want to give that person more financial aid because that wouldn't be fair to someone making the same income who chooses to live more frugally. The implementation plan would be as simple as updating the formula that the financial aid staff at colleges use to calculate your EFC. This solution would inevitably cause the amount of financial aid to rise because most students' EFC would be lower under this calculation. This extra money would come from financial aid that is not used up, such as the hundreds of millions of dollars that go unused every year. Excess funds from these grants would go towards making sure this new method of calculating financial aid is properly financed. The next step to get this solution implemented would be to pitch it to our local government to try to gain support for this issue. It would hopefully then gain enough support to be considered by the state government, and then would be passed on to the federal government to turn it into some sort of law or act. This solution would help to make sure that less of this money is wasted and that more students can receive the financial aid they need to fund their higher education.

Conclusion

College students had amassed a massive loan debt when trying to pay for their higher education, making it a main issue in the United States. The system for funding higher education clearly needs a massive reformation to help college students pay for their college while avoiding debt and elevating their Financial Capability upon they attain their desired degree. We have identified that part of the problem is due to how financial aid is calculated, specifically how the Expected Family Contribution (EFC) is calculated. Financial aid is determined by calculating the student's EFC and subtracting it from their Cost Of Attendance (COA) for the school they are applying to. The EFC is determined by the total income of the student's parent's minus their tax allowances,

divided by the number of children they have in college, and finally added to the individual student's income minus the student's tax allowance. The problem with this is that the EFC only takes into account income, leaving out family's expenses. Determining how much financial aid a family needs to be based only on their income can misrepresent the amount of money they are available to spend on college. Our proposal attempts to solve this problem by including family expenses when determining the EFC. When taking into account a family's expenses, they may receive more financial aid if their expenses are higher than another family with the same income. The problem with this is unnecessary expenses like buying an expensive car, eating out every day, or buying fancy clothes, which can increase a family's expenses and give them more financial aid. To prevent this we would only take into account main expenses like car payments, utilities, mortgages, etc. to exclude unneeded expenses. Also, if these expenses are higher than the median expenses of families living in the same area, these expenses value would default to the median values of families in that area when calculating the EFC. Changing how financial aid is calculated, we expect more of this aid would be correctly given to students who need it the most.

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