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Southern Indebtedness

How Society Uses Debt to Restrict the Economic Mobility of Youth and Young Adults

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Introduction

This paper is the second in a three-part series on debt in the American South written by MDC with support from the Annie E. Casey Foundation and its Southern Partnership to Reduce Debt initiative. The first paper focuses on the root causes of Southern debt. This piece addresses the impact of debt on talent development for youth and young adults. The third paper outlines policy options to reduce debt across Southern states.

The three papers were written before the Coronavirus pandemic. The pandemic has further illuminated and underscored gaps in our economic and societal fabric that can push people further into debt. Lost employment and a lack of a coordinated response by federal and state governments to halt private and public debt collections have left people in debt without protections from wage garnishment and judgments that will leave families in disparate financial conditions.

We know that advancing the upward economic mobility of young people—the foundation of the "American Dream"—is highly dependent upon strengthening local talent development systems. However, for far too many young people, the systems put in place to educate, protect, and support them may, in fact, also become the very systems that leave them over-indebted in ways that impede their economic security and upward mobility.

Background

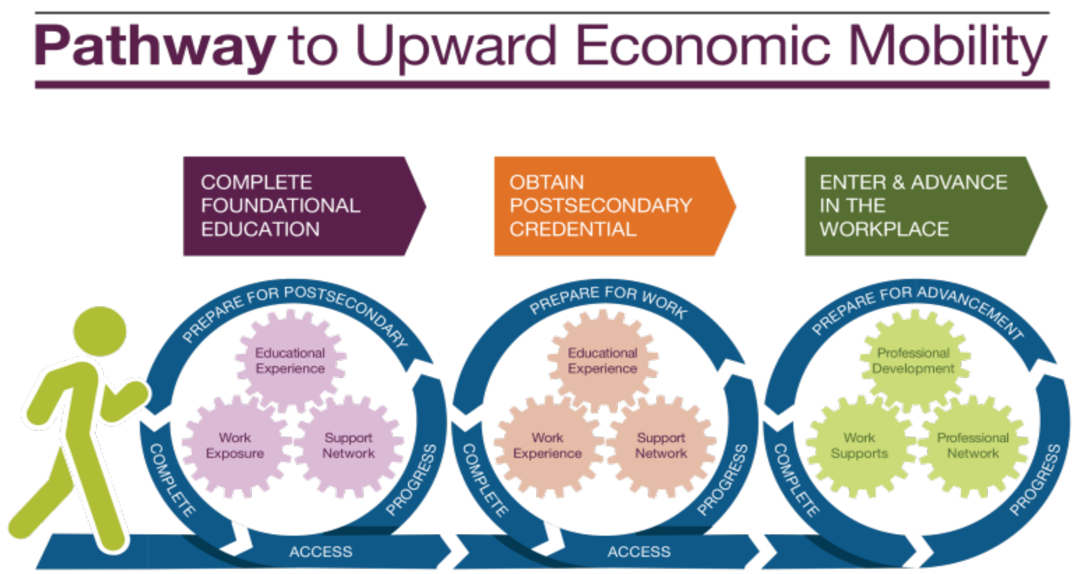
Our idealized view of debt is that it is an optional and calculated financial strategy that aligns with long-term planning and well-being. Underlying this idealized view is the assumption that people have control over the amount of debt they take on at any given time. While that assumption may be true for some, debt is also involuntarily imposed on others—disproportionately low-income families and communities of color—through predatory policies and practices used by businesses and governments. Such practices create financial insecurity that sometimes begins at birth and persists into adulthood.

Debt can be used to build long-term wealth and improve the economic mobility of one's family. However, too often indebtedness occurs not as a result of intentional choices, but because our current financial systems are not designed to manage the complications of daily life for low-wealth households in under-resourced communities. Indebtedness is a major contributor to the lack of mobility among families in the South and perpetuates cycles of intergenerational poverty that are difficult to break.

Debt and the talent development system

As explained in Part I of this series, growing up in a low-income household in the South exposes individuals to stagnant mobility odds. Even in the most prosperous Southern communities, economic mobility is stalled, especially for low-income families. The chance of a child moving from the bottom to top quintile in Atlanta is 4.5 percent; chances in Raleigh and New Orleans are only slightly better at 5 percent. Racial and social exclusion in the South have created a legacy of young people facing multiple barriers to earn an education, secure a living wage job, and enjoy an economically stable career—a cycle that often repeats itself through multiple generations.

One of the primary pathways to improve economic security and upward economic mobility is the talent development system—the interconnected network of institutions, practices, and relationships that facilitate progression from a foundational education to an industry-recognized credential or degree, and, finally, to a job that pays a family-sustaining wage, with potential for career advancement. Although this system provides opportunities for economic security and mobility, progression through the talent development system and its institutions does not happen in a vacuum; success can be impeded or supported by community context, including access to resources and exposure to excessive amounts of debt.[1] Debt accrued in one phase can inhibit progression to the next phase and the ability to become economically secure and upwardly mobile.



A high debt burden restricts access to the necessary financial resources to invest in the next generation and build social capital that connects people to opportunity. Starting out with excessive debt leaves youth and young adults at significant disadvantage at the beginning of this pathway and creates increasingly larger divides between low-income households and their less-indebted counterparts. At each step, the highly-indebted are forced to make decisions that sacrifice long-term goals for more immediate needs, making achievement of those long-term goals more difficult, if not impossible. Short-term consequences are too immediate and severe to consider forgoing in exchange for future rewards.

Effects start early in life

Research shows that parents' economic circumstances not only affect the ability to provide fully for their families' current needs and investments in their children as they navigate education, but their financial resources have an outsized effect on their children's economic mobility in adulthood. About half of parental income advantages are passed on to their children.[2] Family income can shape the social networks, education, and employment opportunities their children are able to access, which can influence future matrimonial prospects and, ultimately, future household income for their families.[3]

In many contexts, debt, as a result of access to credit, is an important wealth-building tool. However, the over-extension of credit by lenders, often with excessive fees and punitive lengthy repayment structures, can have profound effects on a young person early on in life. These effects result from pressures families face when dealing with high indebtedness to achieve economic mobility. For example, certain types of "good" debt (e.g., home mortgages) are associated with greater socioemotional well-being for children. Other types, especially unsecured and high levels of debt, are associated with significant declines in socioemotional development and behavioral issues. This relationship holds true even after controlling for such factors as the mother's marital status and education level, household size, and household income.[4]

Excessive debt leaves families and young people feeling stressed, anxious, and depressed. Children living in families struggling with debt are five times more likely to be unhappy than children in families who do not have difficulty with debt.[5] Living in poverty during childhood can lead to higher levels of toxic stress and is now considered an Adverse Childhood Experience (ACE), one of the factors linked to serious health problems in adulthood.[6] Consumer debt, then, is a double-edged sword for many low-income families—often necessary to make ends meet, but with potential long-term negative effects on children.

As children progress into formal institutions within the talent development system, they face new challenges to access, persistence, and completion of educational credentials that can position them to secure living-wage work. Financial and legal pressures on low-income families divert precious few resources away from supports for these students, including the time and energy needed to focus on educational goals. As a result, young people often lack the confidence that pursuing their future goals will pay off.

Debt and the school-to-prison pipeline: Fines and penalties

Higher rates of entanglement with the criminal justice system among low-income households can compromise progression through the talent development system. Families often get trapped in debt cycles perpetuated by court-related fines and fees they cannot pay. Truancy is just one of a host of minor infractions that criminalize the behavior of young people—often those who are poor, have learning disabilities, or face abuse at home or bullying in school—only to be funneled out of public schools and into the juvenile and criminal justice systems.

The No Child Left Behind (NCLB) Act solidified the link between criminal justice systems and educational systems in many states. Strict school attendance laws commonly lead to fines, loss of custody, and probation for both juveniles and parents. This “school-to-prison” pipeline places families in precarious financial situations that can often lead to them choosing between basic needs and paying criminal justice fees and fines. Research by the Juvenile Justice Center finds that “the imposition of costs, fees, and fines is widespread and poses significant problems for youth and their families. Approximately one million youth appear in juvenile court each year. In almost every state and the District of Columbia, youth may be charged for multiple court-related costs, fines, and fees. Across the country, the inability to make these payments subjects youth and families to possible incarceration, suspension of driver’s licenses, an inability to expunge or seal records, and economic and social stress, among other consequences.”[7]

For example, Alabama and Georgia impose strict truancy laws that can result in jail and court costs for parents. Under the compulsory education laws in Georgia, children between the ages of 6 and 16 must attend school or a home study program until they graduate (although 16- and 17-year-old students must meet certain requirements before they can legally drop out of school). If they are not eligible to leave school, students who miss too many classes could end up in juvenile court, with parents receiving fines or jail time if they are found to be negligent.[8] Alabama parents also face significant fines that, if unpaid—even with demonstrated inability to pay—can result in exorbitant interest and additional fees. In some cases, they may be sentenced to jail time, which means missed work and reduced paychecks—devasting blows to low-income families already struggling to make ends meet.

Young adults with interactions with the criminal justice system that have resulted in convictions for drug offenses, misdemeanors, or felonies are not eligible for federal financial aid.

Even for states that have done away with fines or penalties for truant students, states may file a juvenile justice complaint for “habitual” truancy. Doing so puts the student under the court’s supervision with all the consequences and fees associated with the juvenile court system. For example, about 15,000 truants are placed on juvenile probation in North Carolina each year, with probation violations such as breaking curfew or missing additional days of school leading to detention or out-of-home placement, further disengaging already struggling students and reducing their odds of graduating high school.[9]

The school-to-prison pipeline limits students’ ability to progress through the talent development system. Student interactions with the criminal justice system jeopardize postsecondary aspirations. Access to federal financial aid is often a determining factor for access to and completion of a postsecondary credential. However, young adults with convictions related to driver’s license suspensions or drug offenses—whether misdemeanors or felonies—are not eligible for federal financial aid. Students of color are most impacted by this barrier to education financing because of they are disproportionately charged with drug-related offenses even though research shows they use illicit substances at comparable rates to white counterparts.[10]

The odds are not much better for young people with criminal records seeking employment—especially with changes in state licensure requirements for certain occupational classifications. States are increasingly requiring labor force participants to meet minimum requirements before they can be attached to an employer. These new requirements have significant costs for individuals with criminal records, society, and the economy, in the form of lost hours of labor, the social cost of higher crime rates, and the lost potential of the individual.

The occupational licensing statutes in more states now have blanket prohibitions on awarding of licenses to those with a criminal record. Some laws contain an automatic disqualification which prohibits a person with a felony conviction from obtaining an occupational license, regardless of whether the offense is directly related to the practice of the occupation or poses a substantive risk to public safety.

In addition, licensing laws often contain “good-character” or “good moral character” provisions that grant licensing boards broad discretion to deny applications based on criminal history, including convictions for minor offenses and sometimes arrests that never led to a conviction. Moreover, the costs associated with licensure can be a barrier for people with criminal records, particularly those who are formerly incarcerated. The fees related to training, education, acquisition, and maintenance of a license are all challenges for the formerly incarcerated who often have limited income and other court-ordered monetary sanctions that further inhibit their economic standing.[11]

ABOUT STUDENT DEBT

- More than 44 million graduates hold student debt
- Average undergraduate debt at graduation is $37,000
- Average monthly payment is more than $350
- In 2014, nearly 40 percent of student debt belonged to people owing between $1 and $10,000.
- Student loan debt for people 65 years and older exceeded $18.2 billion in 2013, more than half of which are education loans on behalf of a child or

Education is often *not* the great equalizer

Despite these challenges, if a young person can complete foundational education (i.e., a high school diploma or equivalent credential) and is accepted into a postsecondary education or training program, financial support is still needed. The availability of student loans has increased access to postsecondary degrees and credentials for many, making them important vehicles for economic security and upward mobility. In many ways, access to student loans has resulted in more equitable access to the talent development system, and to postsecondary education and training for those most disconnected from opportunity. This benefit comes at a cost, though, and the potential risks of student loan use are far greater for low-income and minority students. This reality compromises the blanket assertion that a postsecondary education is the “great equalizer” because degrees and credentials must be *affordable* to be accessible.[12]

The importance of a college degree is a widely held American value, but it is not a new one. Upon signing the Higher Education Act of 1965 into law, which provided, among many things, federally subsidized student loans for low-income families, President Lyndon B. Johnson publicly affirmed this sentiment, remarking that:

> *So to thousands of young people education will be available. And it is a truism that education is no longer a luxury. Education in this day and age is a necessity…And in my judgment, this Nation can never make a wiser or a more profitable investment anywhere.*[13]

This public vision for the nation produced higher college enrollment and graduation rates. Today, prospective students have greater access to education that can propel them toward a satisfying career with family-sustaining wages and opportunities for advancement. The funding and supports for education pathways that lead to greater financial security can range from career and technical certifications to an associate degree, and beyond.

However, given the multitude of postsecondary paths available today, it can be difficult to calculate the return on investment (ROI) of student loans, especially for people with little experience navigating postsecondary education systems. Any analysis of student loan debt and the inequities it perpetuates must acknowledge the tension between the increasingly mandatory postsecondary credential required for living-wage work and the reliance on debt among the most vulnerable in their pursuit for economic security and upward mobility. If real wage stagnation continues, the ROI of using student loan debt to gain entry to living-wage jobs will get riskier and become a more significant barrier to upward economic mobility. Failure to address the threat of excessive debt to postsecondary education will also undermine the goals of increasing numbers of states to reach ambitious postsecondary attainment goals.

College attendance and completion can secure credentials needed for specialized jobs and professional occupations with high salaries. It can also broaden one's marriage market, increasing the chances of marrying someone in a higher income or wealth bracket and making one become upwardly mobile.[14] Perhaps the most well-known perceived benefit is the boost to one's lifetime earnings.[15] Despite the strong relationship between postsecondary credentials and lifetime earnings, the use of student loans to earn that credential changes the calculation. Student debts can shape career choices and serve as a deterrent to pursue entrepreneurship[16] or a public service job,[17] although the Public Student Loan Forgiveness program[18] may change the latter depending on how it is implemented.

Some research has found that student loan use is associated with higher starting salaries,[19] but lower wage growth.[20] This could be an indication that student loan users, who are more financially constrained, feel more pressure to accept a job with more initial financial rewards to relieve the immediate burden of student loan debt repayment at the expense of a job that offers more opportunities for development and growth, but a smaller starting salary—a luxury available to their counterparts with significantly lesser student debt.

In the fall semester of 2019, there were 250,000 fewer students enrolled nationwide in postsecondary education than the year before. While part of the reason for this decline is the stronger economy at the time, the cost of college is also a factor. As states reduce their investments in higher education, public colleges and universities are more reliant on tuition, making the sticker prices of college less affordable for families, even when financial aid is applied to the bill.[21] This means more student loans and higher debt burdens.

A Catch-22 of the student loan debt is the high cost of default for those with professional licenses. As a way to stem the rising default in student loans, the federal government encouraged states to revoke occupational licenses of people who defaulted on their student loans. Today, 13 states still have some form of this law in place, including Arkansas, Florida, Georgia, Tennessee, Texas, Louisiana, and Mississippi. It is difficult to determine exactly how many licenses are actually revoked since most states do not track this information. In Tennessee, an estimated 5,000 professionals were reported to occupational boards for loan default between 2012 and 2017. And in Texas, more than 4,200 professionals, including nurses and teachers, were in danger of losing their licenses in 2017 because of unpaid student loan debt.[22] Nationwide, laws related to professional licensure revocation due to student loan default affects 25 percent of the workforce. This issue greatly affects Southerners, because most of the states with such laws are concentrated in the Deep South.

Race, gender, debt, and education

High student loan debt burdens disproportionately affect minorities. About 87 percent of Black students take out student loans at four-year colleges, while 65 percent of Latino students take out student loans, according to the National Center for Education Studies. Black students average $7,400 more in debt than White students when they graduate, and that gap widens over time due to higher default rates.[23]

Any analysis of student loan debt and the inequities it perpetuates must acknowledge *the tension between the increasingly mandatory postsecondary credential required for living-wage work and the reliance on debt by the most vulnerable in their pursuit of upward mobility.*

Gender, race, and other factors shape structural inequities that make student loan debt a poor investment for some. According to the *2015-16 National Postsecondary Student Aid Study*, women make up 56 percent of enrolled college students and hold 65 percent of student loan debt. On average, Black women leave undergraduate study $30,400 in debt, compared to $22,000 for White women.[24]

Women working full-time earn 25 percent less than men, according to a Georgetown University Study and, at the highest education levels, African Americans and Latinos could expect to earn close to a million dollars less than their White and Asian counterparts over a lifetime.[25] Of course, all of this assumes a person completed their program of study. The fact is that many do not. From mid-2014 to mid-2016, 3.9 million undergraduates with federal student loan debt dropped out, according to an analysis of federal data by The Hechinger Report, a nonprofit news organization.[26] The cost of college and the increased demands of life have resulted in many students dropping out of school to meet work and family obligations. Students with some college, debt, and no degree are doubly impacted by the monthly cost of student loans and the lack of credential to boost wages in an environment where real wages have remained stagnant for some time.

The default rate for non-graduates is three times higher than for those who earned a degree. Students at for-profit colleges are in a particularly tough spot. More than half of students who drop out of a for-profit college default on their loans within 12 years, according to one analysis from The Institute for College Access and Success.[27] People in default lose access to Federal student loans that can help them complete their degrees and secure wage increases—another cycle that keeps people isolated from economic opportunity.

The high cost of an over-indebted society

The connection to the talent development system is becoming more tenuous for young people, leading to higher debt burdens, social isolation, and lower educational attainment outcomes—which ultimately reduces economic security and mobility for low-income youth and young adults and people of color. Reducing debt and thus improving the financial security of vulnerable families is a next-generation approach to a better society—it leads to increased educational opportunity which often begets higher wages, a more robust tax base, and a larger share of people who can weather economic storms without reliance on social welfare programs.

A strong talent development system—that works for everyone while creating and sustaining conditions for people to thrive—requires close alignment of the institutions that support a strong economy and vibrant local communities. This system requires attention to reducing debt burdens, especially among those most disconnected from opportunity. While this paper underscores the need for action because of the negative impact of excessive debt on talent development for youth and young adults in the South, the third paper in the series outlines policy options to reduce debt across the Southern states.

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