Southern Indebtedness:
Reports for the Southern Partnership to Reduce Debt

These are highlights from 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 full reports are linked to the titles of each paper.

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Key findings

Paper 1: How Structural Inequities and Flawed Systems Keep People in Debt

We need a nuanced understanding of how consumer debt is propping up the economy so we can focus on more effective interventions and employ the more accurate measures to evaluate those interventions. Acknowledging the reality of the consumer debt crisis is a prerequisite to identifying accurately policies and practices to address the structural causes of increased debt burden among the most disadvantaged. Evidence missing from popular narratives include:

- Forty percent of Americans had trouble paying for food, medical care, housing, or utilities in the last year
- Seventy percent of low- and middle-income households surveyed by the Center for Responsible Lending reported relying on credit cards for basic living expenses, medical expenses, or car and house repairs.
- The personal savings rate of the average American household is below 10 percent, even accounting for personal savings of wealthier families. Nearly half of Americans have no retirement savings and more than 60 percent do not have $500 of cash on hand for emergencies.
- Average incomes of the top five percent of households grew by 13.2 percent in 2018. In comparison, average incomes in the bottom fifth fell by 3.2 percent during the same time period; incomes in the fourth quintile grew at less than half the rate of the top earners, just 5.6 percent.

For a significant share of Americans, it is practically impossible to live debt-free in the United States. Debt is the often way to meet daily needs—the only means keeping them financially afloat and a mode of survival that is fraught with risk.

As in the case of mortgages and student loans (depending on the degree type and marketability in the local economy), debt can be an accelerator for wealth-building opportunities. Detrimental debt such as credit card debt, student loans for degrees with low ROI, and predatory loans can threaten economic security.

While young adults are accumulating debt at the same *rate* as their peers in earlier generations, they are accumulating debt *earlier* in life and most often in the form of student loans, auto loans, and credit card debt, and at a time when they are likely to be the most financially insecure. Increased debt burdens are altering lifestyles of younger generations.

Borrowers of color are more likely to have higher interest rates across the board—varying from mortgage loans, student loans and auto loans—and are more likely to fall victim to predatory borrowing. Black borrowers do not possess more total debt, but they are more likely to be rejected by private financial institutions and more likely to acquire debt with higher interest rates, which result in more limited buying power in the future

The rising costs of tuition coupled with the lack of savings often means students of color are more likely to take out higher student loan amounts to attain a postsecondary credential than their white counterparts. This puts them at a greater disadvantage later when workplace and wage discrimination limit their ability to earn incomes that allow them to thrive and repay student debt. People of color are more likely to default on their loans because of wage stagnation, higher interest rates, lower pay (even with credentials), and their increased likelihood to take jobs to meet immediate financial needs with a low raise rate.

The South saw the largest growth in the number of self-employed individuals (27 percent), followed by the West (21 percent). Gig workers, as independent contractors, do not receive benefits like health insurance; rather, they must procure them on their own

Trends in consumer debt show striking differences between the South and that of the rest of the nation:

- Student loan debt comprises the largest percentage of non-mortgage debt held by Southerners, likely because of the rising cost of education, unrestricted loan borrowing, and low returns to credentials in the labor market.
- Southern states account for 9 of the 10 states most burdened by credit card debt and penalties associated with this type of debt. In many Southern states, the burden is so high that families making the median household income would need more than 18 months to pay off the balance in some states.
- Auto loan debt in Southern states increased by more than 50 percent between 2003 and 2017. Families take on loans with longer repayment terms, sometimes more than six years, and end up owing more on their vehicles than they are worth.
- Income inequality and inadequately-funded systems in the region are the culmination of policies focused on privileging debt options for the wealthy rather than providing the supports for those most in need—who often use high-cost debt to create a safety net.
    - Mortgage interest deduction
    - Property tax deduction
    - Employee sponsored retirement plans

Families are most prone to punishing debt accumulation when emergencies happen, which is most evident for the uninsured or during medical emergencies. Uninsured individuals who are hospitalized experience a host of financial setbacks—including reduced access to credit, a 170 percent increase in unpaid medical bills, and a more-than-double likelihood of bankruptcy.

Only five Southern states have expanded Medicaid, as permitted by the Affordable Care Act (ACA). According to studies, Medicaid expansion results in lower medical debt, reduced personal bankruptcies, increased financial well-being, and freed-up resources to be spent elsewhere—including for basic goods and services like groceries, rent, education, and savings. States that forfeited federal

Medicaid expansion dollars left millions of people nationwide in the coverage gap: they earn too much to qualify for Medicaid, but not enough to qualify for ACA Marketplace premium tax credits. Roughly 90 percent of those in the coverage gap live in the South.

Climate change
Living in a community hit by a medium-sized natural disaster leads to a five percentage-point increase in the share of people with debt in collections after one year, this negative effect doubles to 10 percentage points after four years.

Paper 2: How Society Uses Debt to Restrict the Economic Mobility of Youth and Young Adults

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.

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.

About half of parental income advantages are passed on to their children. 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.

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 grandchild

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. 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. 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.

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.

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.

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.

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.

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.

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.

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.

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.

The default rate for non-graduates is three times higher than for those who earned a degree.

Paper 3: An equity-driven policy agenda to reduce debt

Student Debt

While many borrowers are struggling with the weight of student loan debt, recent data show the disproportionate impact on students of color:

- African-American students take on federal student loans at a rate 25 percentage points higher than their white peers (87 percent versus 60 percent)
- Twelve years after taking out their first loan, African-American borrowers still owe 114 percent of the original loan
- Moreover, 20 years after entering repayment, the median white student borrower has paid back 94 percent of their student debt. The median black borrower, meanwhile, still owes 95 percent of their student loans, or roughly $18,500
- Nearly half of African American borrowers have defaulted on a student loan.
- Three quarters of African American dropouts from for-profit colleges have defaulted

While the federal government does have a lead role in financing higher education (through the Pell Grant and subsidized and un-subsidized loans), states are on the front lines of determining the actual cost of education. While postsecondary education costs have risen, public investment has decreased. With some variation, Southern states have been shifting financial responsibility away from state general funds toward postsecondary institutions. Those institutions in turn secure a greater share of funding from net-tuition revenue. Per FTE appropriations for each state dropped by more than 10 percent from 2008 to 2018, with some states cutting funding by nearly 40 percent.

Student Loans: Status of In-Advance Solutions

Though states must abide by federal policies under the Higher Education Act (HEA), the William D. Ford Federal Direct Loan Program, and the Federal Family Educational Loan Program (FFELP), there are steps that they can take to support students. Aspen offers two “in-advance” solutions, and we add a third for consideration:

- *Implement debt-free public college programs targeting low-income students.*
- *Regulate tuition rates at public colleges and universities.*
- *Expand and strengthen child savings accounts and/or 529 plans with matching state resources, and/or allow these contributions to be tax deductible at a capped income level.*

Student Loans: Front-end Solutions

- *Establish new or shift existing loan-forgiveness programs from merit-based towards need-based determinations and expand eligibility to address critical workforce needs and occupations with limited racial and ethnic diversity.*
- *Provide low-interest and no-interest loans.*
- *Strengthen borrow protections through adoption of the Borrower’s Bill of Rights*
- *Allow students and borrowers to deduct interest and tuition payments on their tax returns or provide a refundable credit.*

Medical Debt: In-advance Solutions

- *Require greater cost pricing transparency to equip consumers with critical information about their medical care.*
- *Fully implement Medicaid expansion.*
- *Establish single-payer healthcare systems.*
- *Establish rules that limit or eliminate surprise medical billing.*

Fines and Fees: In-advance Solutions

- *Reform state and municipal laws and regulations that enable frivolous or unfair civil fines and fees and automatic suspension of a driver’s license for failure to appear or pay.*
- *Explore alternative public funding models to reduce need to rely on fines and fees for revenue.*

Fines and Fees: Front-end solutions

- *Fines and fees are assessed at levels proportional to the seriousness of the offense and ability to pay.*

Fines and Fees: Back-end Solutions

- *Implement new strategies for states and municipalities to collect fines and fees designed to meet consumer's needs.*
- *Eliminate imprisonment or violation of parole because of unpaid debt.*
- *Eliminate punishments that reduce ability to repay and impeded people's livelihoods.*

High-cost lending: Front-end solutions

- *Apply more stringent regulation to products and services that incorporate excessively expensive and/or harmful features.*
- *Use local zoning ordinances to limit the geographic concentration of brick-and-mortar payday loan stores.*