

## John Pierson Presentation Transcript

### Opening – Diane Todd Sprague

It is my pleasure to introduce John Pierson; who has joined us today from Atlanta, Georgia. **John** works with the U.S. Department of Education Federal Student Aid Default Prevention. His career with the Department started in the area of civil rights, working on school desegregation in the south in the 1970s. In addition to his work with the Department, John has also worked in radio and has had a private practice as a psychotherapist for many years. John has a wonderful significant other named Theresa and a good dog named Betty. (John Pierson response “Thank you”).

**John Pierson** – I’ve always liked that “a good dog”. I like “a good dog”. Thanks for inviting me. I have to tell you that this is an amazing event, the fact that we are all here talking about Default Prevention within this framework is proof that some of the conversations that are happening in the Default Prevention community are beginning to change. We are going to talk a little bit about that as we go forward today. I’m really pleased to be here to listen to Justin and Drew. These are really going to be the guys who will be leading you into that “New Place”, what I think is the “Promised Land”, of Default Prevention.

Think about this; if we are all successful in five years, or today, what happens when you’re Chancellor or the President of your school wants to know about “What’s going on with loan default on our campus?” Who do they call? Who do they call now? They call the financial aid office, right? Five years from now, ten years from now (what we hope is) thinking changes about where does loan default come from? That they’ll call Enrollment Management, they’ll call the people who are involved in Retention, and Graduation, and Placement (Job Placement), and Career Placement because we know what?

We know that students who are successful tend not to default on their loans. And; so partially what we are going to talk about today; is that intersection between Student Success and Loan Default. If we only ever talk about Loan Default as something that occurs after somebody leaves school, and they go into repayment; we’ll only ever have what we’ve always had, which is a raft of people who go into default every year. So; let’s go ahead. We’re not going to be able to hit all these slides because we only have a couple of minutes; but we’ll look at some data, talk briefly about the changing landscape, talk about the two different ways we can think about Default Prevention, and then I’m going to hand it off.

So; let’s go ahead. As you can see the draft rates went up in 2004 (and that’s a portfolio view picture). This is the contribution of the number of accounts that go into default by school type or school sector. One of the things that is interesting to me; is that default is dynamic over time within the community. (within the higher education community). So that what we’re seeing is the growth of career schools over the last five to ten years, and there is a corresponding increase in their contribution to the loan default. And, so we are beginning to work with the career schools in a different way than we’ve done before. There is still a hefty proportion of default in the four year public, and four year private sector; and as you can see; there is a growing amount of Loan Default in the Community College sector.

So; this is always changing. I think it reflects the students who are entering college, the objectives that they have; and how colleges are responding to them. Now, the data we’re going to look at (and this is a snap shot) this is our disclaimer; this is a snap shot on a particular date and time, July 29, 2006 when the department calculated the 2004 Cohort Default Rates. So; here’s

some data. The National Cohort Default Rate went up; the National Dollars and Default (which is something that we've started tracking, and I'll explain why in a second), went up; almost mirroring the National increase; and the number of defaulters in Michigan also went up by about a quarter. Why do we talk about dollars in default?

Anybody want to venture a guess? Well; Cohort Default Rates are in regulation, right? 25 percent three years in a row, or 40 percent from one year, puts you at risk of what? Losing eligibility to participate in Title IV; and very few schools could continue to operate if you didn't have Title IV participation. But, when people who go into default they also take a defaulted loan that somebody has to deal with; and the number of accounts and the number of dollars represents to the department a cost. Because, the department is the collector of last resort. And, so we're looking out (in effect), looking out for the taxpayers. And, what you're looking at here is that nationally in the portfolio, we've increased 23 percent year over year from 2003-2004.

Let's go to the next slide. Now for the 2005 Cohort; I cannot share with you today what the numbers are, I know what they are, but I can't share them with you because the "Official Rate" will not come out until September, so there are some things I can't say. But let me say this; I haven't seen anything which would lead me to believe that the number of dollars between 2004-2005 will not have gone up, let's say roughly in the same trajectory that they went up between 2003-2004. So, if we're looking at that data that you have on that slide, what would you guess it might be? Could somebody do a quick calculation in the number of dollars?

What would be a 25 percent increase over eight hundred million be? Could be a billion, (could be a billion), and if it were; it would be the first time we had a billion dollars worth of default loans in one year. And remember, that's only a small slice of the loans that are in repayment, that's a subset, that wouldn't capture all the default in the portfolio in a given year.

That's all that we publicized. But, that's real money; and what we're hoping is that by (there are a lot of threads here for us), and some of the threads have to do with trying to manage the risk within the portfolio (The Stafford Portfolio) from the department's stand point; and by doing that; we're hoping that there's no call to change the program in some way. That if Congress were to say, "Well, this is getting out of hand, we need to do something about it". Well, it might not be better than it is now. So; what we're looking at is collaboration between all the parties in the Stafford Loan community to say; "What can we do to muddle through (given what we're going to look at in the next slide). (But not yet).

See where I say anomalies. Who had a draft rate that went up this year? Who had a draft rate that went down? (Ok) so, it's not an even picture from state to state. And actually, Michigan has more schools doing more about loan default, so I'm not surprised that there were some schools that had some draft rates that went down. But, in September; (and some of you may have already seen some statements in the community about the 2005 rates are going down; the rate of default is going down). (Have you seen some of that in the paper?) What happened; what BIG natural event occurred during the 2005 Cohort period?

A HUGE natural event; how about a BIG HURRICANE; because of that series of hurricanes, the department took some steps in some states that pulled a bunch of loans out of the cohort calculation. What was a non-natural event that occurred during that period which might have had a similar effect? Remember, when there was a big rush to consolidate loans? That pulled a bunch of loans out of the calculations as well. So, what we think is; that when you look at the 2005 "Official Rates" in September, you need to think about what some of the events that occurred that might have impacted them. So; that when you see the first slide (where you saw

that the rates were going up again), that there **might be**, (I'm only saying **might be** because all of this is embargoed information.) **could be** factors behind the numbers that you see; that might have created a one time only event where the rates **could** go down.

**Might, could** that's all I can say about that. (Let's go ahead, ok). These are the things we know. Education costs are going up. This is the environment that we're operating in for the loans. It's not what it was ten years ago; so we have education costs that are going up; and those are costs to borrowers; then our dollars going into default is going up; and our borrowers are entering into default is going up. Total indebtedness is going up, (and that's a **BIG ONE**). So; from a loan repayment stand point; we think that the environment is more hostile for everybody. How many of you have borrowers who are using both Stafford and Private Loans now? Almost everybody is now; and either through programs that are "generally overseen" by schools (not through the schools), but "generally overseen" by the schools where you know about them; and loans that people are getting where you don't know about them; because people are being solicited from an extra educational stand point.

This is a concern that I've had; that we don't talk about to much; and it has to do with Institutional Liability. And, I'm just thinking because the rules are different between the Stafford Loan Program and the Private Loan Programs; that what you have is one set of rules that are fairly obvious, very flexible, and you know that within the Stafford Loan Program, as long as you have a default rate that's below 25 percent (you know what the interest rate is going to be from year to year to calculate it. It does change, but you know what it's going to be). And so; you sort of know what the rules are, and you know how to play the game. Then you have another set of loans that are increasing (we think that probably in 2011, 2012 the number of private loans will **exceed** the number of Stafford Loans, nationally, and over the next decade it will probably **dwarf it**).

And that's partially because the federal share will never keep up with the cost of education. (I think we're way behind that curve now, because I don't think it's going to matter who is in Congress and who the President is. I just don't think the Federal Government is going to be able to pony up that much). And so; there may always be a need for Private Loans. (And so, it's kind of like; there are fleas that come with this dog). And if I'm a school; I need to be careful about that because; what happens to the Stafford Loan Program if your loan default rates goes up 5 percent from 10 percent to 15 percent? Nothing, nothing happens to you right? There is no adverse impact on any of your students; there is no adverse impact on your school.

But; if you have a Private Loan Portfolio; what happens if your default rate in that Private Loan Portfolio goes from 10 percent to 15 percent? What **could** happen? (It's a commercial loan). Can anybody venture a guess? (I'm not saying it **would**; I'm just saying it **could** happen). Increase risk to the lender. And how do they deal with the risk? They raise the interest rate, right? And that's an additional cost to the students. It's not a cost that the school imposes, but it's an additional cost to the student. And, let's suppose it goes up another couple percent; what might your lender do? They **might** say; "I'm sorry; the risk is too great; and we can't lend anymore money to your student". Now, remember, this money that's coming in (flowing in) is because there's a need for it.

**YOU** have a need for it; to continue operating your schools. To keep the lights on; to keep the heat on in the dorms, library books, and paying salaries. If there was no need for it people wouldn't be borrowing as much as they are. So; what happens if there's a possibility that you could have this flow of loan capital cut off at anytime? That's what I'm talking about; a threat to institutional viability. It's a different world. And so; I'm running a school, I need to be

conscious about how we can manage loan default, not just in the Stafford Loan Program; but all loan default; because there is greater risks to students, there is greater risk to schools, (and from our point of view), more risk to the tax payer who supports the Stafford Loan portfolio.

Because you know; if your risk goes up, so does ours (so does ours). (Let's go forward). (You know about that, you know about this; that's partly why we're here today.

71 percent student's who did not complete their academic programs, defaulted on their loans. (That's in the Direct Loan Portfolio; we know that, that's a fact); and so, what we think about and what we're trying to begin; is to shift the conversation about default prevention. I actually; the first time had a conversation with Stewart, (Drew's colleague) about a year ago February; I went to the National Conference. I sought her out and said "Look; we think we have a conversion of interest here, that we know that people who default, are people who do not succeed in school (by in large), and if we can deal with loan default at that level; then I think we're going to have a more fruitful set of options that schools can embrace when we talk about default prevention."

Historically, when we talk about default prevention; we're talking about the borrower's relationship to the loan, right? That's what Entrance Counseling is about; Exit Counseling is about, the Grace Period is for; to help the borrower's have a healthy relationship with that loan. They go into repayment; they continue making the payments, that's what due diligence is for on the part of lenders and servicers. We always want to support people; that's what financial literacy is for; late stage delinquency assistance is for; and supporting the borrower's to have a good and vital relationship with the loan until it's repaid. But that'll only get you so far, because; seven out of ten people end up in trouble; that you've expended all the energy for; are people who didn't succeed in school.

So; what we are trying to do is go back to the beginning of the educational process and say; "How can we deal with this before they become people who are in repayment; troublesome people in repayment?" And so, what we're trying to do is then create a second option for schools supporting the borrower's relationship to their educational programs. Now; are there any people in the room from the "other side" of the aisle? The "Enrollment Management Side?" (Other than Drew?). So; there are some people here. I know that's partly what the holistic view is; and we need the holistic view in schools to deal with the issue of default and default prevention. There's only so much that the people in financial aid can ever do; there's only so much that the Lenders can ever do; and so much that the servicers can ever do; once you have a problem borrower.

How can we keep people from becoming "problem borrowers" to start with? And; that's about Student Success (from our point of view). That involves analysis and being strategic. It involves being able to anticipate who your "problem students" are going to be. That's exactly what Drew does; and Justin does; they will help you identify who your "problem students" are likely to be; and to think strategically; "Who do we need to pull together on campus to help these students become more successful; so they are able to then become "more successful borrowers?" (Why don't we go ahead? I know that this is a generalization), but I think we've found this to be true wherever we've gone; that there are "core functions" that every school engages in; Admissions, Recruitment, Education, Student Services, Retention, Graduation, Job Placement or Career Placement.

If schools do all of these things really, really, really well; then you'll have diminished loan default in your student population. You'll have the absolute lowest amount that your school population can have. And when you start doing the analysis that these guys will be talking about; what you'll see is that there's a problem in one of those areas; one of those general areas, and who do

you need to work with on those areas? You can't do it in financial aid. So; who do you have to have at the table? (Anybody?) You need people from those areas. Enrollment Management, Faculty, etc. (Just as a general question) are there teams working on campuses right now? Do you have teams working on this issue that involve all of those folks? (John observing and responding) "So; you have these people at the table". (John observing and responding) "You're beginning to do that".

(John observing and responding); "You have a retention team; a retention team is a Default Prevention Team; it's the same thing when you're talking about it from this point of view." You'll still have people maybe on campus who are working to support the borrower's relationship to the loan, but when you're talking about the "**PRO**"spective way of addressing the problem, it's a retention team. So; my job; and Eileen's job (and Eileen is working with your advisory team more closely than I am). But; our job is to go around the country, (Let's go ahead); we've kicked off projects so far in all of these states. Our message is the same with all schools; whether we're working on a state project in a given state; or we're addressing some other group, is to let people know that in order to solve the problem (and we think that there'll be a growing problem, going back to Al Gore, that the waters will be rising for everybody; that loan default; as you have this confluence of private loans and Stafford Loans; that the amount of loan default is going to be startling in the next decade).

And what we're trying to do; is create the capability in **every** institution across the country; to do something about it from their own unique "**PRO**"spective. And that not only involves supporting borrower's relationship to the loan; but helping institutions understand that if they do their core missions better; (or as well as they possibly can), that they're making a default prevention contribution. That educational piece; that "Student Success Piece". There are the states that we're working in so far. We have several others teamed-up in Texas and Arizona. There are ten states that have more than half of the loan default in the whole portfolio; and we're engaging all of those states once we've teamed-up with Texas and Arizona.

That's it! I hope you have a really great day today; and this Holistic View of Loan Default is where we need to be; where we need to go; and the professionals who will help you deal with that. Really have those conversations on your campuses; so that you begin to move away from a "Financial-Aid Solution" to a "Campus-Wide Solution"; to a "Student Success Solution". That's what we have to do if we're not to be engulfed by a flood of loan defaults.

Thank you and Good Luck today – (Clapping)