A MAGIC MIRROR FOR STUDENT LOANS

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Early in 2013, the University of Michigan Law School created and published an online tool designed to allow current and prospective students to compare student loan repayment outcomes under a variety of potential postgraduate conditions. The idea came from a student. In a conversation with an admissions officer, a student said that she wished that she had a visual presentation of her student loan amortization schedule so that she could see what her repayment obligations would look like month-to-month. That simple idea led to more discussion with students and law school administrators, and the Law School's admissions office launched a far more ambitious project: the Debt Wizard.[1] The Debt Wizard helps students to visualize their postgraduate personal finances by balancing multiple factors and helps them anticipate the potential consequences of various career choices on their ability to manage educational debt.

I. BACKGROUND AND MOTIVATION

In the last two years, prospective students have begun asking for more, and more detailed, information about funding, and they do so progressively earlier in the admissions process. Students are in-

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[1] *See Welcome to Michigan Law's Debt Wizard!*, UNIV. OF MICHIGAN LAW SCHOOL, www.law.umich.edu/financialaid/debtwizard (last visited Aug. 8, 2013).

creasingly told by a variety of sources that they should eschew all other criteria and focus exclusively on choosing a law school with the lowest cost of attendance; minimizing debt is often touted as the most risk-averse course. With the national media providing nightmare scenarios of unemployed graduates[2] who will "never fully pay off their law school debt,"[3] it is no wonder that prospective students shrewdly consider finances. In the current economic climate, it is the rare candidate for whom cost is not a central factor in choosing a law school, and our conversations with prospective students almost always touch upon themes of educational debt and the impact of debt upon careers. Yet, despite the increased awareness of the importance of funding, many students tell us that they feel anxious about navigating their finances. Some students come to law school with a fair degree of financial sophistication, but many lack the experience, information, or propensity to vigorously investigate their options.

Although our primary concern was developing the Debt Wizard for prospective and current students of Michigan Law, the Debt Wizard is equally usable by students who are considering other law schools. As a public institution, with a broad mission of public service, we were committed to making the Debt Wizard available and accessible. And in an effort to achieve maximum transparency, the underlying data model relies on publicly available datasets, and all underlying assumptions are disclosed and discussed in detail in the Debt Wizard's instructions.

II. MODEL DATA

To provide information that could be individually tailored to a student's personal choices, we used three main data sets: income, housing, and debt repayment. As a student adjusts the Debt Wizard's variables, the display updates to show how her choices for career type, location, salary, and repayment interact. Based on the user's selections, the Debt Wizard calculates and displays estimated

[2] John J. Farmer Jr., *To Practice Law, Apprentice First*, N.Y. TIMES, Feb. 18, 2013, at A17.
[3] Brian Z. Tamanaha, *How to Make Law School Affordable*, N.Y. TIMES, June 1, 2012, at A27.

monthly housing and student debt expenses, as well as after-tax income. Because almost 90% of Michigan Law graduates leave the state following graduation, we sought data with a national scope so that we could present accurate regional cost-of-living comparisons that were relevant for the cities where our graduates most commonly go.

A. Income

We assumed that our user was single, without dependents, and took standard income tax deductions and exemptions. We used an online paycheck calculator to calculate net income after federal and state income taxes (and city taxes for New York).

We used twelve income intervals ranging from $40,000 to $160,000, which approximate what a new lawyer is likely to earn. We chose the specific intervals based on the National Association for Legal Career Professionals ("NALP") salary survey for the class of 2010.[4] We attempted to simulate realistic salaries through interpretation of NALP's data. For example, when "public interest" is selected as the entry-level postgraduate employment option, the Debt Wizard "grays out" salaries of more than $75,000, making them unselectable in the interface, because there were virtually no entry-level public interest lawyers anywhere in the country in 2010 making more than $75,000.[5]

B. Housing

We used the Department of Defense's Basic Allowance for Housing ("BAH") as the starting point for our housing budget values. Service members receive BAH as a tax-exempt supplemental payment to account for rent in civilian areas, renter's insurance, and utilities, calculated according to service grade.[6]

We assumed that a lawyer with a high salary may spend more on housing than a lower-salaried attorney, so we settled on two levels of

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[4] *Starting Salaries - What New Law Graduates Earn - Class of 2010*, NATIONAL ASSOCIATION FOR LAW PLACEMENT, INC. (Nov. 2011), www.nalp.org/starting_salaries_-_what_new_law_graduates_earn_-_class_of_2010.

[5] A future update to the Debt Wizard will include a customizable salary field.

[6] *Basic Allowance for Housing (BAH)*, DEFENSE TRAVEL MANAGEMENT OFFICE, DEPARTMENT OF DEFENSE, www.defensetravel.dod.mil/site/bah.cfm (last visited August 18, 2013).

housing allowances corresponding to the BAH for service members who make $60,000 and $80,000. Military service grade increments do not correspond exactly with the round numbers that we selected, so we had to recalculate some of the values for an approximation.

The Debt Wizard's calculations suggest that some graduates – those with very low salary and very high debt – simply cannot afford to pay for both their monthly debt and housing allowance if they live in New York City. And yet we know that in actuality, our graduates are able to find housing in New York City and pursue public interest work even at low salaries: anecdotal information suggests a number of strategies for reducing living expenses, including sharing housing costs with a spouse, partner, or roommate. We considered trying to account for various living arrangements, but including them would have excessively complicated our tax and Income-Based Repayment ("IBR") calculations.[7]

We considered but ultimately rejected including living expenses other than housing (along with taxes and debt repayment) in our income calculations. Food, clothing, transportation, and medical costs are obvious recurring expenses, but we had trouble finding reliable and locally calibrated data for these costs. Plus, these costs are highly variable between individuals, so adding expenses might have had the perverse effect of making our model less accurate and more difficult to interpret. Likewise, the addition of spouses, partners, and children, and the modeling of salary increases, would have made our tax and IBR calculations far more complex. We ultimately decided in favor of simplicity, and excluded these additional factors in order to focus on the most reliably determinable expenses and repayment options.

C. Debt Service

The Debt Wizard includes debt intervals between $60,000 and $250,000. We chose these intervals based on typical amounts that

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[7] Under IBR, a graduate's monthly debt payment is limited to a percentage of her income with certain allowances for basic living expenses. *See* 34 C.F.R. § 685.221 (2013). Currently, monthly IBR payment is calculated as follows: 15% ([Adjusted Gross Income] - 150% [Poverty Rate]).

are borrowed by Michigan Law students. Among graduates with law school educational debt, the lowest total at graduation that our financial aid office typically sees is $60,000, while the highest amount that a hypothetical student could borrow is about $250,000, based on the current student budget. The average law school debt for a recent Michigan Law graduate was $117,000.[8] The Debt Wizard displays the four debt repayment options that Michigan Law alumni most commonly choose from: standard, 10-year repayment; extended, 25-year repayment; IBR; and Michigan Law's Debt Management Program.

The default repayment schedule for federal student loans requires equal monthly payments over 10 years. Graduates with more than $30,000 in student loan debt can elect an extended repayment schedule with a fixed, monthly payment for 25 years. Under both the 10-year schedule and 25-year schedule, the monthly payment amount is a fixed amount based on the graduate's debt balance.

IBR allows a graduate to cap her monthly payment at 15% of her disposable income.[9] The graduate must reapply for IBR annually and, in order to qualify, she must demonstrate a "partial financial hardship" – essentially, the IBR payment must be lower than her payment would be under the 10-year repayment schedule. We used gross income as an approximation for Adjusted Gross Income ("AGI") and plugged that figure into a nonprofit website's online IBR calculator to determine monthly IBR payment.[10] Since we used an approximation for AGI, the resulting calculations are just estimates, but we think that our model provides a more precise and accurate estimate than many students are likely to calculate on their own.

Recent Michigan Law graduates can receive repayment assistance

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[8] Average debt at Michigan Law compares favorably to the average debt incurred by law students at peer schools and is among the lowest average debt loads at graduation for the Top 14 law schools according to data reported to the American Bar Association. In 2012, only 5 of the Top 14 law schools (including Michigan Law) reported average debt between $110,000 and $120,000. The lowest average debt in the Top 14 was $110,000, while the highest was $157,000.

[9] *See supra* note 7.

[10] *Income-Based Repayment Calculator (15% version)*, FINAID, www.finaid.org/calculators/ibr.phtml (last visited Aug. 18, 2013).

through the Michigan Law Debt Management Program.[11] Michigan Law covers all or a portion of the student's IBR payments on a sliding scale based on income for up to 10 years. Other law schools offer similar school-sponsored loan repayment programs, but some school-sponsored programs have significant barriers to entry or exit, are restricted to lawyers in qualifying public interest careers, only cover a fraction of law school loans, or have other qualification requirements. Qualification under the Michigan Law program is straightforward: any recent graduate with relatively low-income and legal employment is eligible to participate.[12] We used the monthly IBR payment generated by our IBR calculations to estimate the Michigan Law Debt Management Program payment.

The 25-year repayment and IBR options both reduce a graduate's monthly payment while extending the term of repayment. However, graduates who pursue qualifying public service employment and make on-time monthly payments for 10 years can apply for Public Service Loan Forgiveness from the federal government.[13] So, for graduates who are pursuing public service careers, it might make sense to minimize the monthly payment while waiting for forgiveness. For graduates in the private sector, loan forgiveness occurs at 25 years.[14]

III.
FUTURE DEVELOPMENTS

Although we have detailed cost-of-living information from the BAH rate data, we were unable to find career data of comparable breadth. Anecdotally, of course we know that a recent graduate in a secondary legal market probably has a lower income than her

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[11] Michigan Law first implemented a Debt Management Program in 1985, and it has been through several iterations. Our current income-based Debt Management Program replaced a prior version that is still utilized by graduates of earlier years. *See Debt Management/Loan Repayment Assistance Program*, UNIVERSITY OF MICHIGAN LAW SCHOOL, www.law.umich.edu/alumniandfriends/giving/Pages/DebtManagementProgram.aspx (last visited Aug. 18, 2013).

[12] Graduates must first enter the program within five years of graduation. *See id.*

[13] *See* 34 C.F.R. § 685.221 (2013).

[14] *Id.*

counterpart in a larger city. But, to what extent are salaries lower in secondary markets? What is the degree of variation? While many law firms report salary data, comprehensive market-based salary data is hard to come by outside of the private legal practice context. The only distinction that we were able to derive from the available data was national, not market-specific: virtually no recent graduates find a public interest job making more than $75,000. However, beyond this basic distinction for public interest salaries, the Debt Wizard cannot tell a student how likely she is to receive a particular salary in a particular market. Unfortunately, NALP does not publish comprehensive salary data broken down by job type and location. This means that although the BAH data shows that, for example, students should expect housing in New York City to be more expensive than in Detroit, the available data does not tell us whether public interest lawyers are paid more in New York than in Detroit. The trend toward law schools publishing comprehensive, transparent graduate employment reporting[15] may well lead to the availability of more refined data in the future.

One challenge for maintaining the relevance of an undertaking like the Debt Wizard is the constantly evolving regulatory framework. New loans issued after July 1, 2014, will be eligible for a lower, monthly IBR payment capped at 10% of disposable income as opposed to the current 15% calculation. Additionally, debt forgiveness for graduates in the private sector will occur after 20 years instead of 25 years.[16] As a stopgap measure for 2012 and 2013, President Obama issued an executive order creating a new Pay As You Earn ("PAYE") program, which uses a 10% income-based monthly payment similar to the expected changes to IBR.[17] But, PAYE is a temporary program and, for future law students, it is unclear whether PAYE will be available as a separate program or be

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[15] *See*, *e.g.*, Kyle P. McEntee & Patrick J. Lynch, *A Way Forward: Transparency at American Law Schools*, 32 PACE L. REV. 1 (2012); Kyle P. McEntee & Patrick J. Lynch, *Take This Job and Count It*, 2 J. of L. (1 J. LEGAL METRICS) 309 (2012).

[16] Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029, § 2213 (2010); *see also* 20 U.S.C. § 1098e(e).

[17] *See* Tamar Lewin, *President to Ease Student Loan Burden for Low-Income Graduates*, N.Y. TIMES, Oct. 26, 2011, at A15.

merged into the existing IBR program after the statutory changes take effect in 2014. Many current law students appear to be eligible for lower monthly payments under these two programs, but the details of how these programs will be administered in the long-term are not settled. Once the government promulgates new regulations governing these changes, we will update the Debt Wizard to include a 10% option.

IV. CONCLUSION

Students have long had difficulty visualizing how student loan payments will affect their post-graduate financial outlook. Many students are planning to move to a new city after graduation, and compounding that uncertainty, a professional lifestyle is totally unfamiliar territory: some are expecting to be financially independent for the first time in their lives. This issue is not exclusive to law students, either. The U.S. Consumer Financial Protection Bureau has an initiative to educate student borrowers about their loan options and to encourage colleges and universities to provide plain-language counseling information precisely because some students have a hard time understanding their options.[18] Certainly many financial aid offices, including Michigan Law's, offer individual counseling to address concerns about budgets and funding, but the Debt Wizard creates a self-service option that allows students to grapple with the issues in fairly simple terms from the earliest stages of the process.

Still, while the financial outlay for tuition and living expenses is without question a key factor, it is but one aspect of a complicated picture. Focusing exclusively on the outlay ignores the opportunities of law school. Even from a purely financial perspective, many law school graduates come out ahead, because lawyers tend to earn more money than workers without law degrees. Of course, graduates of highly regarded law schools have higher earning potential: the median salary for a 2011 Michigan Law graduate was $147,500

[18] Richard Cordray, *Prepared Remarks in a Press Call about the "Financial Aid Shopping Sheet"*, CONSUMER FINANCIAL PROTECTION BUREAU (July 23, 2012), *available at* www.consumerfinance.gov/speeches/prepared-remarks-by-richard-cordray-in-a-press-call-about-the-financial-aid-shopping-sheet/.

for the first year of employment, compared to the national median starting salary for any law school graduate of $60,000.[19] However, even this relatively low median starting salary for all law school graduates is greater than $55,432, which is the national median for full-time, salaried workers with a bachelor's degree at *any experience level*.[20] Simply put, the outlay for law school can be daunting, but law school graduates potentially earn a lifetime of higher earnings.[21]

Further, an exclusive focus on the worst case financial scenario ignores important considerations for prospective students choosing whether to go to law school. A career in the law can be stimulating and fulfilling in a way that few fields can challenge – and for a student attracted to the relatively unique work of lawyering, the necessary first step is to attend law school. We encourage students to consider finances when making their decisions along with postgraduate career outcomes, student culture, fit, academic reputation, strength of alumni network, and other criteria which affect students' success in law school and in their future careers.

The Debt Wizard is only one tool for students to use in envisioning their futures. And, given the inherent uncertainties, the best that we can offer is an estimate of how we think things will look in those students' futures. However, we created the Debt Wizard because, despite its flaws, we think that it provides a more accurate and reliable model of debt repayment than other online tools that are currently available to students.

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[19] *Salaries for New Lawyers: An Update on Where We Are and How We Got Here*, NATIONAL ASSOCIATION FOR LAW PLACEMENT, INC. (Aug. 2012), www.nalp.org/august2012research.
[20] *Earnings and unemployment rates by educational attainment*, BUREAU OF LABOR STATISTICS (May 22, 2013), *available at* www.bls.gov/emp/ep_table_001.htm.
[21] For a more robust discussion on this point, *see* Michael Simkovic & Frank McIntyre, *The Economic Value of a Law Degree* (Apr. 13, 2013) (working paper), *available at* ssrn.com/abstract=2250585.