The $555,000 Student-Loan Burden

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As Default Rates on Borrowing for Higher Education Rise, Some Borrowers See No Way Out; 'This Is Just Outrageous Now'

By MARY PILON

When Michelle Bisutti, a 41-year-old family practitioner in Columbus, Ohio, finished medical school in 2003, her student-loan debt amounted to roughly $250,000. Since then, it has ballooned to $555,000.

It is the result of her deferring loan payments while she completed her residency, default charges and relentlessly compounding interest rates. Among the charges: a single $53,870 fee for when her loan was turned over to a collection agency.

"Maybe half of it was my fault because I didn't look at the fine print," Dr. Bisutti says. "But this is just outrageous now."

To be sure, Dr. Bisutti's case is extreme, and lenders say student-loan terms are clear and that they try to work with borrowers who get in trouble.

But as tuitions rise, many people are borrowing heavily to pay their bills. Some no doubt view it as "good debt," because an education can lead to a higher salary. But in practice, student loans are one of the most toxic debts, requiring extreme consumer caution and, as Dr. Bisutti learned, responsibility.

Unlike other kinds of debt, student loans can be particularly hard to wriggle out of. Homeowners who can't make their mortgage payments can hand over the keys to their house to their lender. Credit-card and even gambling debts can be discharged in bankruptcy. But ditching a student loan is virtually impossible, especially once a collection agency gets involved. Although lenders may trim payments, getting fees or principals waived seldom happens.

Yet many former students are trying. There is an estimated $730 billion in outstanding federal and private student-loan debt, says Mark Kantrowitz of FinAid.org, a Web site that tracks financial-aid issues—and only 40% of that debt is actively being repaid. The rest is in default, or in deferment, which means that payments and interest are halted, or in "forbearance," which means payments are halted while interest accrues.

Although Dr. Bisutti's debt load is unusual, her experience having problems repaying isn't. Emmanuel Tellez's mother is a laid-off factory worker, and $120 from her $300 unemployment checks is garnished to pay the federal PLUS student loan she took out for her son.

By the time Mr. Tellez graduated in 2008, he had $50,000 of his own debt in loans issued bySLM Corp., known as Sallie Mae, the largest private student lender. In December, he was laid off from his $29,000-a-year job in Boston and defaulted. Mr. Tellez says that when he signed up, the loan wasn't explained to him well, though he concedes he missed the fine print.

Loan terms, including interest rates, are disclosed "multiple times and in multiple ways," says Martha Holler, a spokeswoman for Sallie Mae, who says the company can't comment on individual accounts. Repayment tools and account information are accessible on Sallie Mae's Web site as well, she says.

Many borrowers say they are experiencing difficulties working out repayment and modification terms on their loans. Ms. Holler says that Sallie Mae works with borrowers individually to revamp loans. Although the U.S. Department of Education has expanded programs like income-based repayment, which effectively caps repayments for some borrowers, others might not qualify.

Heather Ehmke of Oakland, Calif., renegotiated the terms of her subprime mortgage after her home was foreclosed. But even after filing for bankruptcy, she says she couldn't get Sallie Mae, one of her lenders, to adjust the terms on her student loan. After 14 years with patches of deferment and forbearance, the loan has increased from $28,000 to more than $90,000. Her monthly payments jumped from $230 to $816. Last month, her petition for undue hardship on the loans was dismissed.

Sallie Mae supports reforms that would allow student loans to be dischargeable in bankruptcy for those who have made a good-faith effort to repay them, says Ms. Holler.

Dr. Bisutti says she loves her work, but regrets taking out so many student loans. She admits that she made mistakes in missing payments, deferring her loans and not being completely thorough with some of the paperwork, but was surprised at how quickly the debt spiraled.

She says she knew when she started medical school in 1999 that she would have to borrow heavily. But she reasoned that her future income as a doctor would make paying off the loans easy. While in school, her loans racked up interest with variable rates ranging from 3% to 11%.

She maxed out on federal loans, borrowing $152,000 over four years, and sought private loans from Sallie Mae to help make up the difference. She also took out two loans from Wells Fargo & Co. for $20,000 each. Each had a $2,000 origination fee. The total amount she borrowed at the time: $250,000.

In 2005, the bill for the Wells Fargo loans came due. Representatives from the bank called her father, Michael Bisutti, every day for two months demanding payment. Mr. Bisutti, who had co-signed on the loans, finally decided to cover the $550 monthly payments for a year.

Wells Fargo says it will stop calling consumers if they request it, says senior vice president Glen Herrick, who adds that the bank no longer imposes origination fees on its private loans.

Sallie Mae, meanwhile, called Mr. Bisutti's neighbor. The neighbor told Mr. Bisutti about the call. "Now they know [my dad's] daughter the doctor defaulted on her loans," Dr. Bisutti says.

Ms. Holler, the Sallie Mae spokeswoman, says that the company may contact a neighbor to verify an individual's address. But in those cases, she says, the details of the debt obligation aren't discussed.

Dr. Bisutti declined to authorize Sallie Mae to comment specifically on her case. "The overwhelming majority of medical-school graduates successfully repay their student loans," Ms. Holler says.

After completing her fellowship in 2007, Dr. Bisutti juggled other debts, including her credit-card balance, and was having trouble making her $1,000-a-month student-loan payments. That year, she defaulted on both her federal and private loans. That is when the "collection cost" fee of $53,870 was added on to her private loan.

Meanwhile, the variable interest rates continue to compound on her balance and fees. She recently applied for income-based repayment, but she still isn't sure if she will qualify. She makes $550-a-month payments to Wells Fargo for the two loans she hasn't defaulted on. By the time she is done, she will have paid the bank $128,000—over three times the $36,000 she received.

She recently entered a rehabilitation agreement on her defaulted federal loans, which now carry an additional $31,942 collection cost. She makes monthly payments on those loans—now $209,399—for $990 a month, with only $100 of it going toward her original balance. The entire balance of her federal loans will be paid off in 351 months. Dr. Bisutti will be 70 years old.

The debt load keeps her up at night. Her damaged credit has prevented her from buying a home or a new car. She says she and her boyfriend of three years have put off marriage and having children because of the debt.

Dr. Bisutti told her 17-year-old niece the story of her debt as a cautionary tale "so the next generation of kids who want to get a higher education knows what they're getting into," she says. "I will likely have to deal with this debt for the rest of my life."

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