

Students crushed by high interest rates

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Should student debt really be categorized on the same level as money owed because of criminal behaviour?

Rules put in place about 13 years ago under changes to the Bankruptcy and Insolvency Act put student debt on par with unpaid child support and court settlements based on crimes you may have committed.

“They are putting student loans up there with criminal behaviour,” says Carleton University professor Saul Schwartz, who has studied the issue for years and says about 12% to 15% of student loans will never get repaid. That’s about double the rate of the general population, he says.

It’s no easy route for a student to go bankrupt because of changes to the act in 1998. Up until then, student debt was no different from any other kind of debt and completely forgiven once there was a bankruptcy discharge.

But the act was changed to say you had to wait 10 years after leaving school before you could apply to have your student debt forgiven. That was lowered to seven years in 2008.

“There is no good reason why student loans should be treated differently than any other loan,” says Prof. Schwartz, adding that even taxes are forgiven by the government in a bankruptcy. “That’s the basic point that should be made.”

Others will point to jurisdictions like the United States where student debt is not forgiven in any bankruptcy situation. They will also suggest the loans are taxpayer money and should therefore be paid back.

Through the Canada Student Loans Program, the federal government with the provinces provides financial assistance. Ottawa provides 60% of the assessed need to a maximum of \$210 in loans per week of study. About 4.3 million students have received almost \$32-billion in student loans since the program was created in 1964.

There are two key points students need to remember as part of bankruptcy, says Melanie Wengel, trustees in bankruptcy at A. Farber and Partners Inc.

For starters, no student debt is cleared if you declare bankruptcy less than seven years after you leave school. “Unless you wait seven years that debt will not be forgiven at the end of the process,” Ms. Wengel says.

Sometimes students will go ahead with declaring bankruptcy before the seven-year period because by clearing debt such as credit-card balances they are better able to deal with knocking down their expensive student debt.

But even if you wait the full seven years, there is no guarantee your student debt will be erased.

“I do most of the court work here and what I’m seeing is where student loans comprise the majority of the debt in the bankruptcy, [the Canada] Student Loans [Program] will oppose the bankruptcy,” Ms. Wengel says.

If no agreement on repayment can be reached, a court may be asked to rule on an application and that former student can be forced to pay a certain amount into a bankruptcy estate.

“Sometimes the court says debts are 20 years old and have no bearing on the profession the individual chose, and discharge the debt on the spot,” Ms. Wengel says.

One of the biggest hurdles in Canada is convincing the government to not pursue you.

“I’ve heard that,” says Margaret Johnson, president of Solutions Credit Counselling Services Inc. in Vancouver, about the government refusing to go along with bankruptcy agreements in which the student debt is more than 50% of the amount of debt outstanding.

She says part of the reason so many students are struggling is the high rate of interest on loans. The prime-lending rate is 3% at most financial institutions but students pay as high as 8.5% interest, says Ms. Johnson.

Payments on a student loan don't start until six months after you leave school but interest begins accumulating right away and it can add up pretty quickly. The Canadian Federation of Students said that in 2009, the average debt for university graduates was \$26,680 — making a strong case for declaring bankruptcy even if it does mess up your credit rating for six years.

“The government needs to come to terms with the interest on these student loans, that’s what’s killing them,” Ms. Johnson says. “It’s so high compared to other types of debt.”

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