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More on Oil Patch Jobs …

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Desperately seeking workers in the oil patch

Jobs go begging in booming western North Dakota and northeastern Montana

By PHIL DAVIES
Senior Writer

Rick Tofte doesn't try to hire workers for his Williston, N.D., construction business anymore. They're difficult to find, and even harder to keep—starting wages at oilfield service firms in the area far exceed what he can pay for the services of carpenters, roofers and electricians. The 30-year-old firm has a full slate of building projects, including upscale housing and facilities for expanding oilfield companies. Yet Tofte Brothers Construction employs only six people; as the oil boom has taken hold in the region, Tofte and his brother Terry have increasingly relied on subcontractors to do most of their work.

"We have changed our structure in how we [operate]," Rick Tofte said. "We used to do it all ourselves; now we sub[contract] out 75 percent of it, just because we can't find the employees."

Such adaptations by employers to a tight labor market go with the territory in western North Dakota and northeastern Montana, where rapid oil and natural gas development has transformed the economic landscape. Extraordinary demands are being made on the labor supply in the oil patch.

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PHOTOGRAPHS BY KEVIN CEDERSTROM

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THE QUICK TAKE

Rapid oil and gas development in the "oil patch" of western North Dakota and northeastern Montana has created huge demand for workers—not just in the oilfields, but also in a range of non-oil industries. But so far, the supply of labor—from within and outside the region—has responded slowly to demand. In recent years, job openings have soared and unemployment has dropped to very low levels—below 3 percent in a number of counties.

The Bakken oil play is drawing job seekers from other Ninth District states and the rest of the country, but they're not coming in sufficient numbers to keep up with continued job growth. There are several obstacles to the flow of labor into the oil patch, among them low unemployment in eastern North Dakota, the area's frigid winters and—most important—a scarcity of housing.

The region faces an awkward period of adjustment, but labor conditions are likely to loosen within a few years as rising wages and improved living conditions for migrants increase the workforce.

From Minot, N.D., west to Sidney, Mont., and on down to Dickinson, N.D., few workers are available to fill thousands of job openings in a range of industries, from oil and construction to health care and food service. Last December, the unemployment rate in the Williston area was 1 percent, and job openings outnumbered the jobless 10 to one. "If you're not working right now, you don't want to be working," said Shawn Wenko, assistant director of economic development for the city of Williston.

In the oil patch, labor supply constantly plays catch-up with demand—setting it apart from most areas of the Ninth District and the nation, where unemployment rates remain high in the wake of the Great Recession. Oil country is a place where finding a job typically takes less than a day, unskilled laborers can make over $60,000 per year and restaurants offer sign-on bonuses and prize drawings to attract workers.

As local pools of available labor have drained, job seekers have poured into the oil patch from other parts of the district, from distant states and even from other countries. But still there aren't enough outsiders arriving to satisfy rising demand for labor in a white-hot regional economy driven by ongoing oil and gas exploration, drilling and production.

Markets are rising to the workforce challenges of the oil boom. For example, employers have raised wages to lure workers in a variety of industries, not just oil and gas. But when jobs are plentiful and wages high, yet employers still go begging for workers—especially in this national economy—it's clear there are barriers to the free flow of labor into the oil patch. One obstacle is external to the region—low unemployment in eastern North Dakota that discourages migration from that area.

Communities and employers also face a variety of internal and place-specific factors that prevent or limit more labor recruitment, including a scarcity of housing and other critical infrastructure and services, and increasing crime. Hit by a massive economic stimulus that has attracted thousands of newcomers, many cities and towns are feeling growing pains. For many prospective workers, there's another type of pain—the region's notoriously harsh winters.

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One of the Minneapolis Fed's congressionally mandated responsibilities is to gather information on the Ninth District economy. The *fedgazette* is published quarterly to share that information with the district, which includes Montana, North and South Dakota, Minnesota, northwestern Wisconsin and the Upper Peninsula of Michigan.

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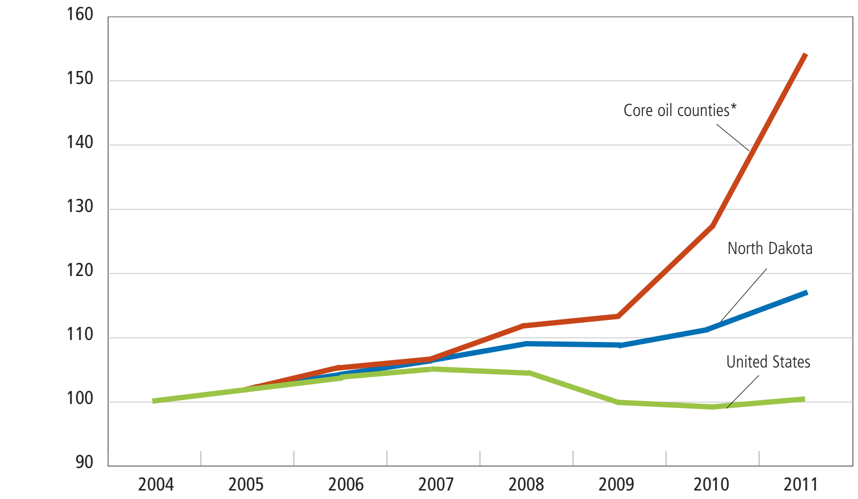
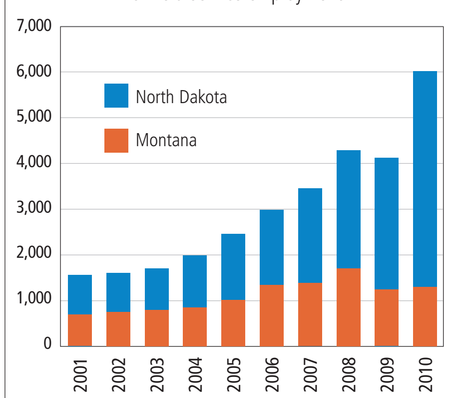
Chart 1 **Surging employment in the Bakken**
Index (2004 = 100)



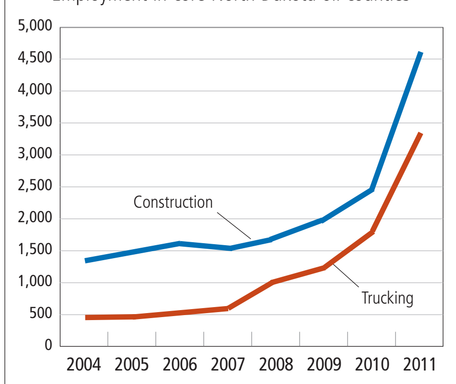
* Dunn, McKenzie, Mountrail, Stark, Williams, N.D.; Richland, Mont.
Source: Bureau of Labor Statistics, Local Area Unemployment Statistics

Chart 2 **More work in the oilfields**
Oilfield service employment



Source: Bureau of Labor Statistics, Quarterly Census of Employment and Wages

Chart 3 **Build it, move it**
Employment in core North Dakota oil counties*



*Dunn, McKenzie, Mountrail, Stark, Williams
Source: Bureau of Labor Statistics, Quarterly Census of Employment and Wages

Businesses and local governments can't do much about the weather. But they're striving to make the oil patch a more hospitable place to live and work; for instance, the pace of housing construction has picked up over the past two years, despite lingering fears of a 1980s-style oil bust. These and other community-building efforts are critical to helping the oil patch continue its remarkable run of economic growth.

An employment gusher

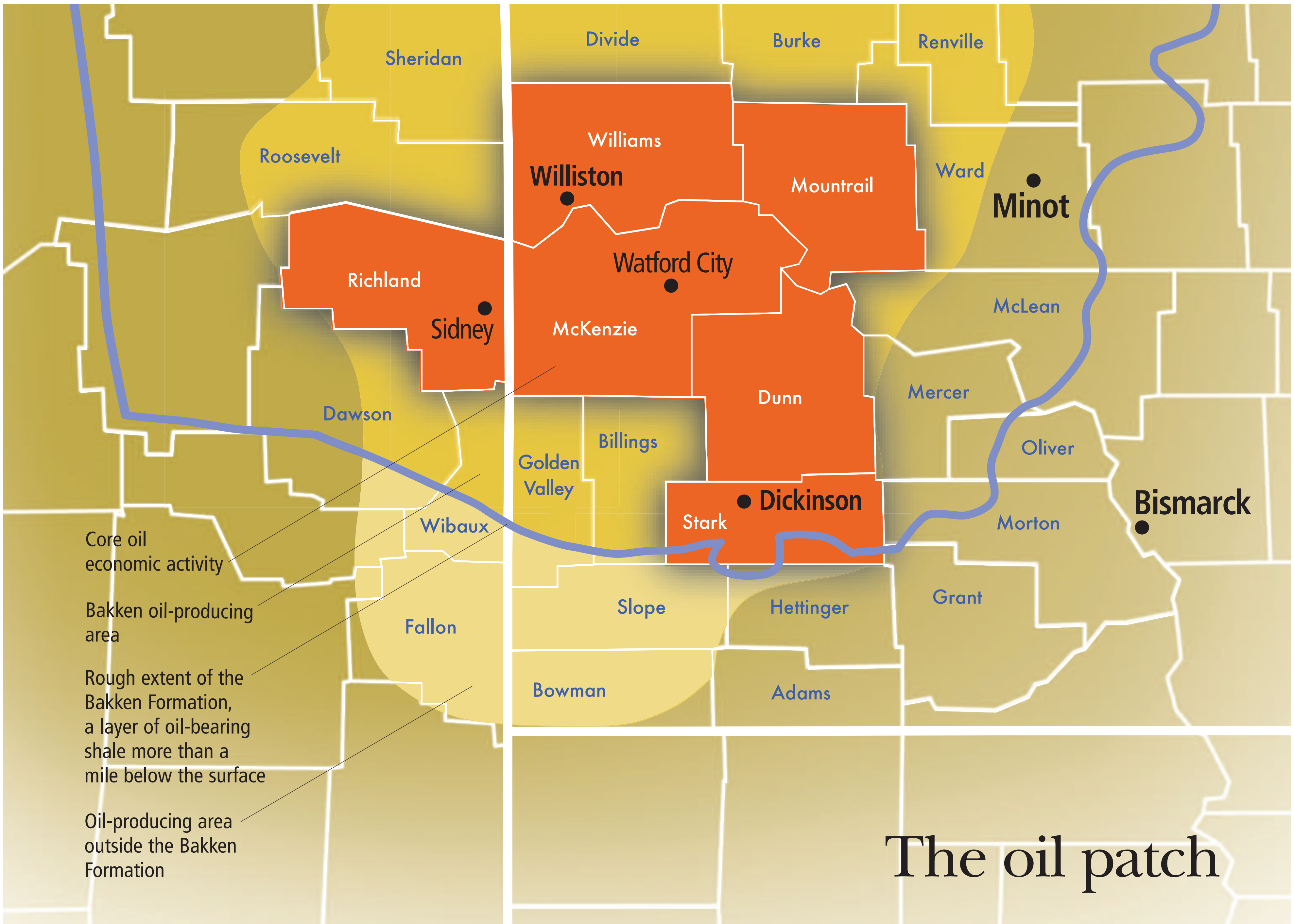
The full impact of oil and gas development on the regional economy becomes evident in springtime, when the easing of road restrictions gives full rein to trucks headed out to drilling and well sites in the oilfields. The already high level of activity in communities such as Williston, Dickinson and Sidney rises to a fever pitch; restaurants are packed, long lines form at the post office, traffic jams main thoroughfares.

Total employment has exploded in the region since the early 2000s (see Chart 1), thanks to new horizontal drilling techniques that allow energy companies to tap the Bakken Formation, a deep layer of oil-bearing shale underlying 200,000 square miles of the northern Great Plains.

Employment in Williams County (home to Williston, a bustling oilfield hub) and Mountrail County more than doubled between 2004 and 2011, according to figures from the U.S. Bureau of Labor Statistics (BLS). Employment growth in six Bakken counties with either major oil production or oilfield service centers far outstripped average growth in North Dakota—a state which led the country in job gains.

Not surprisingly, many new jobs in this core Bakken zone and other nearby counties are in oil and gas (oil wells produce natural gas as a byproduct). From 2003 to 2010—the latest year for which BLS data are available—the industry added at least 5,500 net new jobs in eastern North Dakota and western Montana. Most of the new positions were at North Dakota oilfield service firms that provide petroleum and drilling companies with everything from truck hauling to crane services to derrick and well components (see Chart 2).

Continued on page 4



Sidney
The center of oil activity and home construction in Montana's portion of the Bakken

Williston
The hub of the region's petroleum industry, home to 200-odd oilfield service firms

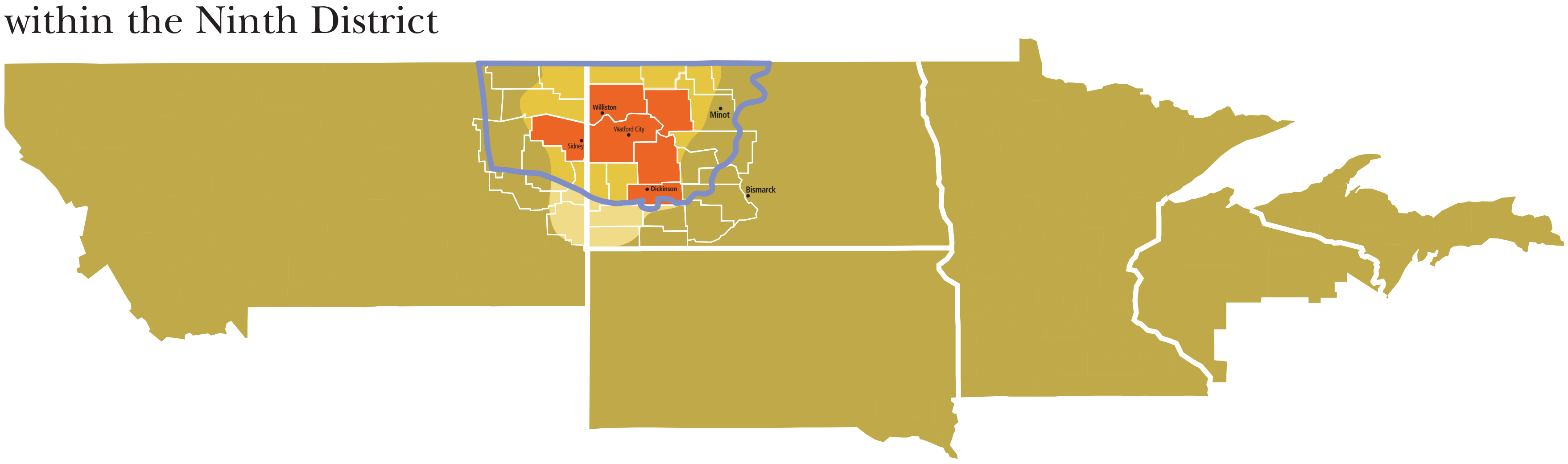
Watford City
Community has annexed land and extended sewer lines to accommodate a burgeoning population

Dickinson
A farming, manufacturing and university community developing into an oilfield service center

Minot
A gateway to the oil patch for oil companies, construction firms and other businesses doing business in the oilfields

Bismarck
State capital becoming a bedroom community for oil and construction industry managers and their families

Location of the oil patch within the Ninth District



Jobs from page 2

With the exception of a short slowdown during the recession (see the September 2009 *fedgazette*), oilfield activity and employment have grown at breakneck pace, especially in North Dakota. In February, over 180 drilling rigs were operating in the state—triple the number active three years before, according to Baker Hughes, an oilfield technology firm that compiles drilling statistics.

Oil and gas development has also created jobs in other industries that feed on energy spending rippling through the regional economy (see Chart 3 on page 2). Builders in core Bakken counties have thrived on expansion projects—new offices, workshops and temporary housing for workers—for oilfield companies such as Baker Hughes, Halliburton and Brigham Exploration. In the second quarter of 2011, Williams County construction jobs more than doubled year over year.

Transportation employment has increased too. Together, Williams County and Stark County (home to Dickinson) gained over 700 trucking jobs from 2010 to 2011, an increase of 58 percent.

And as truck traffic has risen, so have crashes, increasing demand for ambulance crews, emergency room doctors and other health care workers. Oilfield trauma—falls, burns, explosions, crushed limbs—have added to the workload and strained capacity at hospitals in the region. Last fall, Mercy Medical Center in Williston broke ground on a 40,000-square-foot addition to accommodate expanded outpatient services, including new surgery suites.

Everywhere in the oil patch, new enterprises have opened to cash in on the boom—machine shops, restaurants, extended-stay motels, appliance stores. In the Williston area alone, almost 500 net new businesses have formed since 2004, according to BLS figures. All need labor, a commodity that has become more precious than oil itself.

Jobs chasing people

Rising demand for labor has severely taxed supply in a region that before the oil boom was an economic backwater compared with fast-growing western Montana and North Dakota's Red River Valley. Ranching and dry-land farming were the mainstays in what is now the oil patch, supporting a relatively small, dispersed workforce; in 2005, about 100,000 people lived in 11 North Dakota counties west of Minot and four border counties in Montana.

In a mere half-dozen years, oil has turbocharged that regional economy, driving down unemployment rates to the lowest levels in a generation. In December 2011, a swath of counties in western North Dakota and two in northeastern Montana had unemployment rates at or below 3 percent (see map on page 5). By comparison, North Dakota's average unemployment rate was 3.2 percent that month, and the equivalent figure in Montana was 6.7 percent. Rates were relatively higher in Montana's portion of the Bakken—though still low in most counties compared with the state and U.S. average—because of lower and declining oil production.

Data on job openings paint an even starker portrait of demand chasing supply in the oil patch. Job openings have climbed in the region as more jobs go unfilled for longer periods. According to Job Service North Dakota, job openings in most oil counties increased at least 80 percent in December 2011 compared with the year before; in Williams County, vacant positions more than doubled year over year.

A large share of openings are for oilfield jobs—petroleum engineers, roustabouts, crane operators, heavy-truck drivers. In January, there were over 1,100 oilfield positions open within a 50-mile radius of Williston. But there were also hundreds of other job openings in a range of occupations, including construction, office administration and sales.

Job Service data show that last December, job openings outnumbered unemployed people in many oil counties—an indication that labor pools were nearing rock bottom. In Williams County, there were 10 openings for every unemployed person, and five openings per jobless worker in Stark County.

Oil and gas development is also putting pressure on labor supplies in Minot and Bismarck, N.D., cities on the periphery of the oil patch. Petroleum isn't the only factor driving demand for workers in these relatively large communities, which have diverse economies based on agriculture, health care, retail trade and other industries. Bismarck is the state capital, with thousands of government jobs. But Minot and the Bismarck-Mandan metro area are becoming centers for oil companies, engineering, land leasing agencies and other firms doing business in the oilfields to the west.

Last December, the Bismarck-Mandan unemployment rate stood at 3.2 percent, a year-over-year drop of almost 1 percentage point. In the Minot area, average weekly wages rose 12 percent in the second quarter of 2011 compared with the same period the previous year. And in both cities, percentage increases in job openings over that period mirrored those seen in oil-producing counties.

High wages and big-screen TVs

With labor supplies stretched tight as a drum, recruiting and holding onto workers is a daily battle for many firms, from the oilfields to Main Street. "The labor shortage situation is so serious that there are incredible accommodations being made by employers; everything from hours of the work shift to the wage rate," said David Flynn, director of the Bureau of Business & Economic Research at the University of North Dakota (UND).

Raising wages is the most obvious tactic to lure scarce workers, and indeed average private wages have risen dramatically in the oil patch. Since 2004, wage increases in core Bakken counties have dwarfed increases in the state and nation (see Chart 4).

Some of the increase in oil counties is due to a rising proportion of well-paid workers in oil-related industries. (The average annual wage for North Dakota oilfield service workers was over $76,000 in 2010.) But most of the rise in average wages stems from increases across the spectrum of industries. For example, in McKenzie County, N.D., average wages for motel and food service workers increased 66 percent from 2010 to 2011. In the Sidney area, the locus of oil activity in the western part of the Bakken, average construction wages rose 10 percent from 2009 to 2010.

Business at Johnson Hardware & Furniture in Sidney was booming in January on the strength of increased sales of household goods to new residents and farmers flush with oil royalty income. "Things are fantastic," said owner Phil Johnson. "We've posted 18 consecutive record months [in sales]; we've just put to bed the biggest month ever in the history of our store." But costs have increased as well; to compete with rising wages in the area, Johnson has increased average pay at the store 40 percent to 50 percent over the past two years, to about $12 per hour.

In Watford City, the seat of McKenzie County, auto dealership S&S Motors has doubled its wage rates over the past five years. Owner Brent Sanford—who also is city mayor—said via email that the firm has also sweetened health benefits, paying 100 percent of employees' medical, dental and vision coverage.

Employers have tried other ways of attracting and retaining workers, including offering flexible or part-time hours, paying sign-on bonuses and enlisting current employees in recruitment efforts. Last winter, a Williston restaurant ran a promotion in which workers who referred new hires were entered in a prize drawing for a large-screen television.

But no matter how diligently they pursue workers and strive to keep them

Big trucks hauling materials and equipment to the oilfields take a toll on roads throughout the Bakken region.

Low unemployment in the oil patch

December 2011 unemployment rates

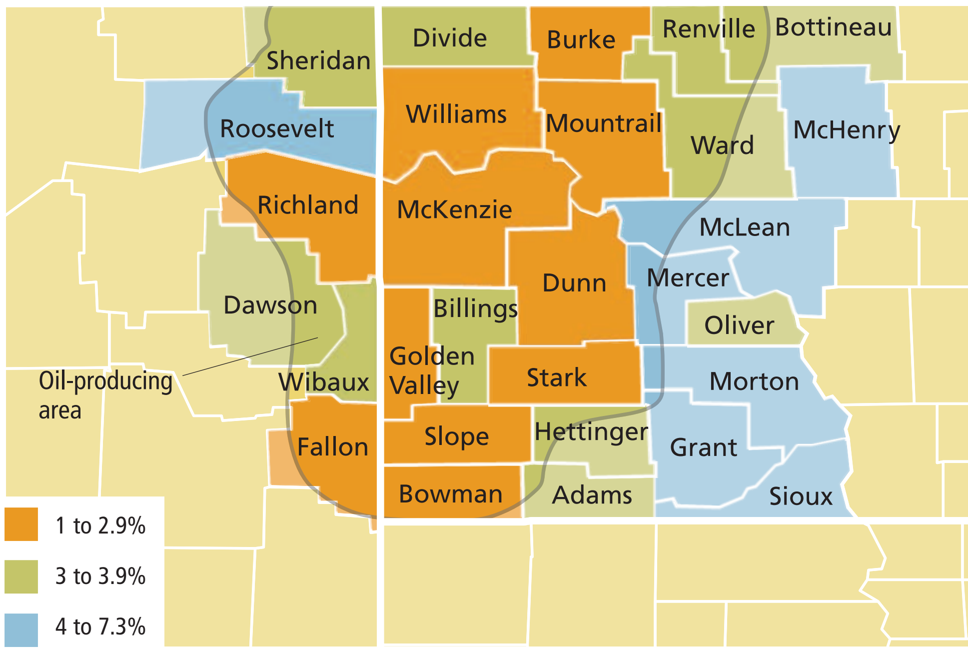
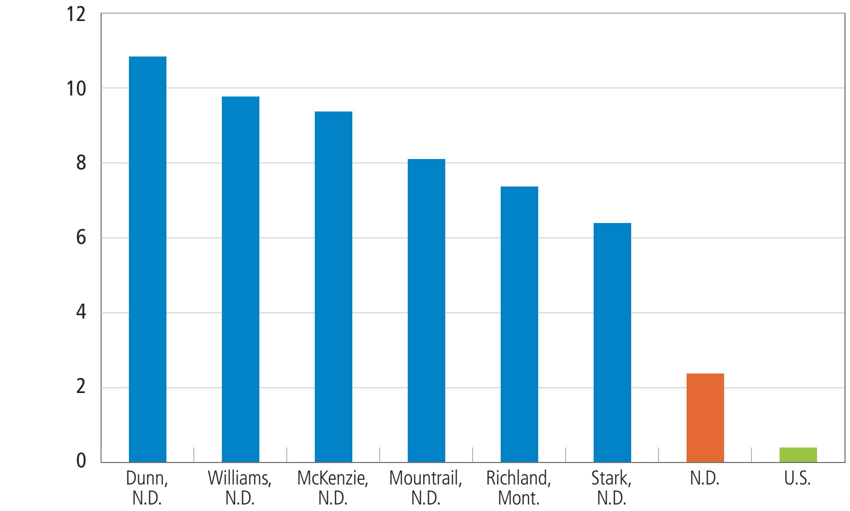


Chart 4 **Higher pay in the Bakken zone**

Average annual percentage wage growth* (Q2 2004–Q2 2011)



*Private weekly wages, inflation-adjusted
Source: Bureau of Labor Statistics, Quarterly Census of Employment and Wages

happy, many businesses in the oil patch inevitably lose employees to the oilfields. Not everybody is cut out to work on an oil rig, or an oilfield service crew—the work is physically demanding and the hours long. But the lure of high wages can be irresistible, particularly for young men. Tofte, Johnson and other employers interviewed for this article said workers had quit to take jobs in the oil and gas industry.

Tofte said he stopped trying to compete with oil wages years ago. "We've lost some to the oilfields and never really tried to retain them, either," he said. "It wasn't like, 'What will it take to keep you here,' that type of thing. We've found that you can't get into a bidding war."

Powerful attraction

With unemployment rates in the abyss, the oil patch depends on workers from outside the region to supplement homegrown help, "whether they're commuters or migrants that move there," said Michael Ziesch, manager of the North Dakota Labor Market Information Center in Bismarck. "They're important to us; the youngsters aren't going to grow up and hit 18 quick enough."

The oil patch is a black hole for labor, sucking in workers from near and far. The Bakken's gravitational pull is strongest in adjacent areas such as western Montana, Wyoming, eastern North Dakota and Minnesota, but its influence extends across the continent and overseas.

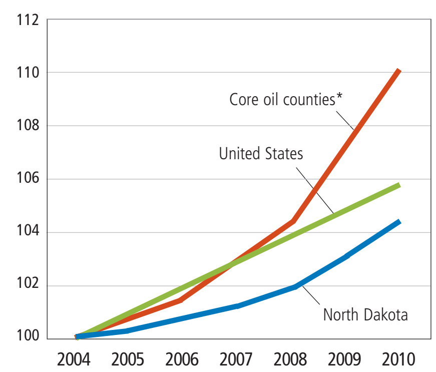
Extensive construction in the region—new commercial facilities, housing, roads, utilities—has created opportunities for businesses based elsewhere to provide skilled labor. A number of contractors and engineering firms in Fargo and Grand Forks, N.D., regularly dispatch work crews west, putting them up in motels, apartments or other temporary housing. They come home on weekends, completing a 600-mile roundtrip commute.

"It's attractive to do business out there, because labor is so scarce," said Barry Wilfahrt, president of the Grand Forks-East Grand Forks chamber of commerce. "[Oil patch firms] are paying a very significant premium to get people to come out." Other contractors commute from Bismarck and Billings, Mont., and housing developers based in western Montana maintain work crews in the oil patch for part of the year.

This transient labor is difficult to track; most itinerant contractors draw their paychecks from firms based outside the oil patch. What can be quantified is migration to oil country—people from other places coming to take jobs and settle in.

Chart 5 **More people in the oil patch**

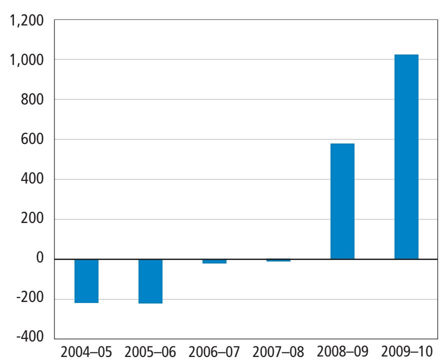
Population growth index (2004 = 100)



*Dunn, McKenzie, Mountrail, Williams, Stark, N.D.; Richland, Mont.
Source: U.S. Census

Chart 6 **The lure of oil**

Net migration of tax filers in core Bakken counties*



*Returns filed by taxpayers who lived in a different county the previous year
Source: Internal Revenue Service

Between 2004 and 2010, after minimal growth earlier in the decade, the combined population of six counties in the heart of the oil patch increased markedly (see Chart 5). Census data show that the population of Williams County increased at more than three times the state average from 2005 to 2010, for a gain of about 2,700 people.

The region's torrid economy has surely accelerated population growth over the past two years, which has yet to show up in the census. Williston officials in January estimated the city's population at about 20,000, based on building activity and water consumption; that's far higher than the official 2010 census of less than 15,000.

A *fedgazette* analysis of federal tax return data provides further evidence of in-migration. The numbers are

Continued on page 6

"Help wanted" signs are as ubiquitous as gas flares and packed restaurants in the oil patch.

Jobs from page 5




Daily bustle pervades the oil patch, both in the oilfields and on Main Street.

small—tax data documenting household moves miss newcomers who filed returns from their previous hometowns—but the data (see Chart 6 on page 5) show a net inflow of taxpayers into core Bakken counties since 2008, reversing an opposite trend before the oil boom.

Talk to oil patch employers, and the wide sweep of the region's labor net becomes clear. Every business contacted for this article employed people from outside the area, some of whom had traveled hundreds of miles to find work. In January, Johnson Hardware had six workers on its payroll who had recently moved to Sidney, including three men from Montana's Flathead Valley, where home building has been slow. "We've seen a large influx of fellow Montanans moving from the mountains to the plains because of the opportunity that exists out here," Johnson said.

At Mitchell's Oil Field Service, a Sidney-based construction and trucking company with facilities in Watford City and other communities in the region, applicants from western Montana and other states such as Minnesota, Idaho and Arizona far outnumber those from area residents. "Pretty much all the local people have been snatched up by somebody, either by our company or other companies around here," said Human Resources Director Andrea Davidson.

A half-open gate

Despite the inflow of workers, there's no sign of loosening labor conditions in the oil patch.

Throughout 2011, unemployment rates across the Bakken remained very low and ratios of job openings to unemployed kept rising, with increasing numbers of jobs available to those who somehow had managed to avoid employment.

Clearly, not enough people are moving to the oil patch to keep up with the pace of job creation in the region. Or perhaps it isn't attracting enough of the right types of workers—those with the aptitudes and skills sought by employers.

Ziesch sees a structural "imbalance" in the region's workforce: a dearth of teenagers, mothers of young children and other part-time workers to fill positions in offices, retail stores, restaurants and motels. A large proportion of workers who come to the area to work in the oilfields are men who are either single or choose to live apart from their families for weeks or months at a time.

Many newcomers are people down on their luck without the necessary skills to work in the oil industry, construction and other fields, said Wenko of Williston economic development. "It's unfortunate we have people showing up off the bus, off the train," he said. "We're looking for skilled labor up here; we're not looking for lost souls."

There are a number of obstacles to increased migration to the region, some more easily surmounted than others.

One is strong economic growth and low unemployment in other parts of North Dakota. The Red River Valley, the most populous part of the state, is the closest large source of potential workers for the oil patch. Many residents of Fargo, Grand Forks and other communities along the Minnesota border are familiar with the oil patch and may have relatives or friends living there. But the job market in eastern North Dakota gives them little incentive to pull up stakes. Last December, the Fargo area had over 6,000 open positions, twice the number available a year earlier. Most counties in the eastern half of the state had unemployment rates below 4 percent—enviably low compared with the nation as a whole.

In Grand Forks, most people are content to stay put for now, said Keith Reitmeier, customer service area manager for the Grand Forks Job Service office. "They like the communities where they live," he said. "There are a lot of opportunities in eastern North Dakota, and people are aware of that. There's no gate swung open and people heading west."

Strains on the physical capacity of the oil patch to absorb more people are another impediment to migration. Public and private resources necessary to support a burgeoning workforce are being stretched to their limits in cities at the epicenter of the oil boom, such as Williston and Watford City. "You're getting communities that are just completely overwhelmed with this influx of people," said Flynn of UND.

A housing shortage—a major reason why more nuclear families aren't moving to the region—has driven up rents and forced many workers to sleep in trailers, tents and vehicles (see "No room at the inn," page 7).

A related problem: maxed out sewage systems in some communities. In 2011, the flow of wastewater into the city of Williston's treatment plant exceeded its design capacity; this year, the city plans to spend $5 million to $6 million in state grants funded by impact fees on oil companies to upgrade the plant—a stopgap measure until a bigger facility can be built.

Other strains on infrastructure and public services make life stressful and unpleasant, discouraging some people from moving to the oil patch. Truck traffic clogs highways and ravages county roads, lengthening commutes; small police and sheriff's departments struggle to respond to increased crime.

Finally, there's the weather, an issue for migrants from warmer climes. Flynn noted that North Dakota's bracing winters give pause to workers considering moving anywhere in the state, not just its western reaches. "The fact that it's North Dakota doesn't help," he said. "There's a perception of North Dakota being cold, and it happens to be true."

In time, they will come

This year is likely to set new records in oil drilling and production in the oil patch. Petroleum companies are exploring promising new areas of the Bakken, like Montana's Roosevelt County, and refining their drilling techniques to tap even deeper shale-oil deposits. Unless global oil prices fall or regulators intervene—drilling processes that inject water and chemicals into the earth have drawn federal scrutiny—economic growth tied to oil and gas development will continue to strain the region's labor supply.

Any further tightening in the job market could retard economic development in the region if some employers search in vain for workers, forcing them to delay or cancel new initiatives and facility expansions.

That possibility concerns Gaylon Baker, executive vice president of Stark Development Corp., the economic development arm for Stark County. "Our workers are hard to find, and our wage scales are up there," he said, making it hard for the Dickinson area to attract manufacturers and other non-oil employers.

Williston is being eyed by restaurant and retail chains for new locations, Wenko said. But they're worried about ultra-low unemployment, and the scarcity and expense of housing for workers. "We understand that it's going to take significant investment for them to come in here," he said. "It comes down to the workforce and housing."

Not every business is a winner in an oil boom; over the next few years, many employers, especially non-oil firms, will continue to struggle to hire and retain workers, at least at wages they want to pay. A surfeit of job openings in the region will keep unemployment rates in the basement.

However, down the road, labor supplies are likely to increase in the oil patch as state and local governments invest in sewers, highways and other infrastructure, and developers build more housing for workers and their families.

Rising wages in a range of industries should encourage more local residents to enter the workforce and attract more workers from outside the region willing to brave frigid winters. "We're catching up with the rest of the world," Baker said. "We were a low-wage environment prior to [the oil boom], and thank goodness we're no longer famous for that."

Instead, western North Dakota and northeastern Montana are known for having jobs—more jobs than anyone could have imagined before oil lit a fire under the region's economy. f

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Photography by Kevin Cederstrom

A wintered-in RV near Watford City, N.D.

No room at the inn

For newcomers to oil country, their first job is finding a place to live

By PHIL DAVIES
Senior Writer

Scarce, expensive housing is the biggest impediment to the flow of labor into the oil patch from other parts of the district and the nation. Newcomers looking for digs in Williston and Dickinson, N.D., Sidney, Mont., and other communities find slim pickings, and the few available places often are priced beyond the means of many non-oil workers earning low to moderate wages.

Mention the large number of job openings to anyone in western North Dakota and northeastern Montana, and the conversation quickly turns to the housing crunch. "Everybody's looking for people," said Williston Mayor Ward Koeser, "and I think it would be easier to fill these jobs if there was housing available. But there's just no place to live."

Said Gaylon Baker, an economic development official in Dickinson: "To create jobs, all you have to do is build an apartment; two people will move into that apartment, and they'll have no trouble finding jobs."

Last winter, many workers slept in their cars or in campers parked at the local Walmart without water or sewer hookups; bitter cold forced an unknown number to quit their jobs and return to where they had come from.

New housing isn't being built fast enough to satisfy mounting demand from workers in the oilfields and related industries. Constraints on the region's housing supply include rising construction costs and a cautious approach to residential planning and financing by local governments and lenders. However, the pace of home construction has quickened across the Bakken in recent years, and in time housing stocks should increase and prices moderate.

Gimme shelter

Oil country would be a real estate agent's dream, if only there were more homes to sell. Housing prices and rents have escalated over the past five years as workers have flooded the region, competing for a limited housing stock. Prices in some communities have risen to levels typical of the nation's biggest cities. In Williston, simple trailer homes were selling for over $100,000 last winter, and modest, two-bedroom apartments were renting for over $2,000 per month—triple the rate landlords were charging three or four years ago.

Shelter was less expensive in Dickinson, but average home prices have increased about 25 percent over the past two years, according to a recent report by engineering firm Kadrmas, Lee & Jackson.

Oil companies and large oilfield service and construction firms often rent entire apartment buildings, trailer courts and motels for their employees. Other workers, including those earning lower wages, must find their own accommodations—an increasingly iffy proposition in an area where virtually everything but the henhouse is already rented out.

"If you're new to the area, and you don't have a family member who says, 'Hey, stay in my basement,' it's going to be a significant challenge," said Phil Johnson, owner of Johnson Hardware & Furniture in Sidney. "You can find a job in 10 minutes; it might take you 10 months to find a place to live."

Instances of workers roughing it until something better comes along abound in the Bakken. One of Johnson's employees from outside the area was "couch surfing" with friends, he said. In Williston, a restaurant worker was paying $1,400 per month to park a camper outside town; two co-workers were sleeping in their pickup truck.

Crew camps—dormitory-style, prefab settlements built for oilfield and construction employees—are one option for workers living on their own; some "man camps" are open to individual renters. But the camps' small, one-bedroom units aren't suitable for families, and some counties have imposed moratoriums on the construction of new camps because of sanitation concerns and complaints by area residents.

The high price of shelter is hard on public employees whose paychecks don't cover the cost of a place in town. In a bid to retain police officers, street maintenance crews and other workers, the city of Williston started paying its workers a $350 per month housing allowance this year. And sharply rising rents have displaced residents on fixed incomes, such as the elderly and disabled. Faced with rents that consume most of their income, many seniors have had no choice but to leave their hometowns.

Demand for housing in the region is also driving up housing prices and rents in Minot and Bismarck, N.D., cities that serve as gateways to the oil patch. In Minot, an influx of oil and construction workers has further taxed housing supplies decimated by last year's flooding (see the October 2011 *fedgazette*), raising prices for both surviving and replacement housing. The average price of single-family homes increased 8 percent from 2010 to 2011, according to the Minot Board of Realtors.

In Bismarck, demand for homes and apartments has increased as families whose incomes are tied to oil and gas development move into the city. Because housing in the state capital is inexpensive relative to shelter in western North Dakota, many managerial workers with families choose to live in Bismarck and commute on a weekly basis to the oilfields, said Michael Ziesch, manager of the North Dakota Labor Market Information Center in Bismarck. "We're kind of becoming a bedroom community for the oil patch," he said.

Continued on page 8

Kevin Cederstrom

Improvised housing in Alexander, N.D.

Housing from page 7

'What if we fall off the cliff?'

Just as there are barriers to migration into the oil patch, the region's housing market has its own issues that curb the capacity of builders to meet demand for new homes. These obstacles are rooted in building costs and a long-standing conservative approach to financing housing construction—a legacy of the oil bust of the early 1980s, which left local banks and other investors financially exposed when demand for housing evaporated overnight.

The same forces driving housing demand are also increasing construction costs. Land purchases by expanding oil and oilfield service firms in recent years have bid up the price of residential lots in many communities. Lots developed for a new housing subdivision in Minot sold for about $60,000 apiece last fall, said Joel Feist, a Minot home builder who heads the North Dakota Builders Association. "We used to think that a $30,000 lot was a pretty premium lot," he said.

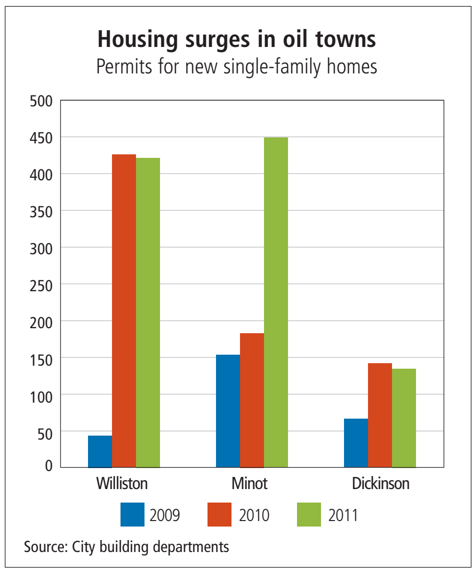
Oil-driven demand has also increased costs of construction materials such as concrete, copper and electrical supplies—much of which must be trucked into the region at high rates. And to compete with oilfield wages, builders must pay their workers more; Feist anticipates a 7 percent to 10 percent increase in labor costs at his firm this year.

To meet these additional expenses, developers must either draw upon their own capital or borrow the money—a challenge for smaller builders that rely on local bank financing. As a rule, banks based in the region try to minimize their exposure on loans for housing construction, insisting on lower loan-to-value ratios than is the norm in other parts of the country.

"We require housing developers to bring a lot of their own capital to the table; that's pretty much the way we've always done it," said David Hanson, CEO of American State Bank and Trust Co. in Williston. Like other financial institutions in the oil patch, the bank is especially careful about lending for large developments such as tract housing or apartment complexes—it considers the risk of default high.

Lenders in the region haven't forgotten the early 1980s, when a drop in oil prices led to widespread home foreclosures in former boomtowns such as Williston and Sidney. Despite growing institutional confidence that this boom is more sustainable than the last one in the 1970s—industry experts predict at least 20 years of intensive oil drilling—"there's always that concern about the cliff out there; what if we fall off the cliff?" Hanson said.

Local governments also worry about getting burned in the event of a bust. Williston was saddled with millions of dollars in bond debt for infrastructure when developments planned during the last oil boom were never built. Today, Williston "shares the risk" of residential development, Mayor Koeser said, using local tax revenue and state grants to extend trunk sewer and water lines, but making developers foot the bill for improvements within subdivisions. This philosophy, shared by other oil communities, increases upfront costs for developers.



Because of high development costs and credit constraints, local contractors typically build a few units at a time, slowing the overall pace of housing construction in the oil patch. Most housing projects with 20 or more units have been built by large, deep-pocketed developers from outside the region.

Pouring concrete, pounding nails

Despite these obstacles, the pace of home building has picked up; over the past two years, new subdivisions and apartment buildings have sprung up throughout the oil patch. Soaring home prices and rents have spurred development, said Mike Marcil, a Fargo, N.D., real estate developer who is involved in an apartment project near Stanley, a burgeoning town between Minot and Williston.

Marcil notes that other developers based outside the region are breaking ground on housing projects, and he sees increased investment in housing. "I think the mentality has started to change," he said via email. "The economics are so staggering, it has silenced some of the biggest skeptics. I see more locals getting involved and a lot more lenders starting to chase the opportunity."

Approvals for new homes and apartments have surged, in stark contrast with sluggish building activity nationwide. In Williston, permits for new single-family homes and townhouses increased more than 10-fold between 2009 and 2011 (see chart). Last year, permits were issued for over 400 homes, almost matching a city record for annual home permits set the previous year.

Above: New crew camps near Williston, N.D.

> *"You can find a job in 10 minutes; it might take you 10 months to find a place to live."*
> —Phil Johnson, owner of Johnson Hardware & Furniture

Koeser estimates that by this fall, roughly 1,200 new dwellings, including hundreds of apartment units—the most efficient way to house people on increasingly expensive land—will be ready for occupancy.

Home construction has also shot up in Minot and Dickinson, and in smaller oil communities such as Stanley and Watford City, N.D., and Sidney. In Watford City, a community south of Williston, two housing developments to be built on annexed land will double the number of dwellings in the city, said Mayor Brent Sanford in an email.

Sidney added more than 100 living units last year, and construction was slated to start this spring on a massive mixed-use development on the town's outskirts. Preliminary plans by a Bozeman, Mont., developer called for more than 150 houses and 60 apartments—one of the biggest subdivisions ever proposed in the city.

Visions of spreading rooftops

Despite the increased activity, a lot more of the same has to occur for housing supply to catch up with demand in the Bakken. "The effort is there … but [home building] doesn't move as quickly as we'd like it to move," said Shawn Wenko, Williston's assistant director of economic development.

A 2010 analysis of Williston's housing market by Ondracek, Witwer & Bertsch, a Minot research firm, estimated that the city's permanent housing stock would have to swell by 50 percent over the next 15 years—to more than 11,000 units—to accommodate new households. Similar proportional increases in housing demand were projected for Watford City, Stanley and other communities.

Those projections are probably outdated, and low; Watford City officials estimate that the community's population already exceeds the 2,700 people the study anticipated would live there in 2030.

At least in the near term, many non-oil workers will struggle to find lodging at a price commensurate with their earnings in Watford City and other boomtowns. Government efforts to provide "affordable" housing are ramping up—the 2011 North Dakota Legislature provided $15 million in tax credits to encourage construction of inexpensive apartments in high-rent areas—but it remains to be seen how many workers will benefit from state and federal housing subsidy programs aimed mainly at low-income households.

Current housing prices in the region reflect the huge impact of thousands of new workers on communities ill prepared for their arrival. But, as Marcil observed, there's nothing like high prices to encourage more home building. Given time—two years, five years, nobody really knows—housing stocks should increase to the point where prices plateau.

Extraordinary demand for housing in the oil patch "will eventually be met," said David Flynn, an economist at the University of North Dakota. "It's just taking time; it's taking adjustments on the part of builders and other local market participants." f

College Finance 101: Not all their (de)fault?

Student default rates are rising and likely to continue until the economy sees strong job growth

By RONALD A. WIRTZ
Editor

Many Americans hold a soft place in their heart for college. It's a place for intellectual freedom, for expanding personal horizons, for gaining new friendships, experiences and perspectives.

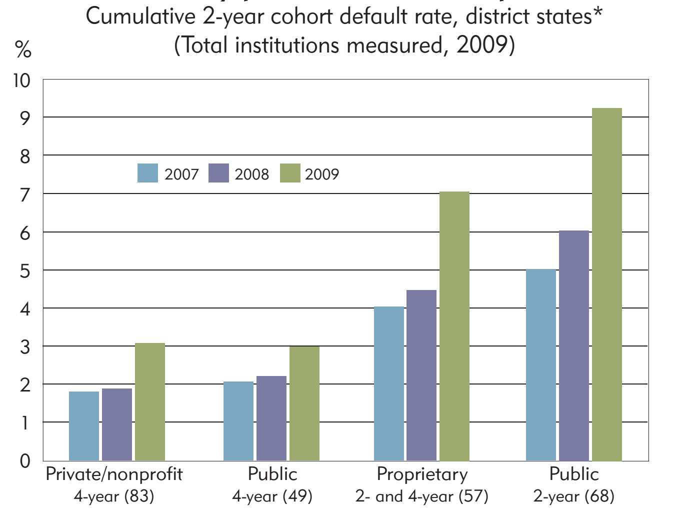
But many college-goers are ringing up a small fortune in debt, and a growing number of graduates across the Ninth District are earning a big, fat D—as in default—on their student loans, according to a *fedgazette* analysis of default rates at more than 250 public and private higher education institutions in district states.

Rising student debt and related defaults have been gaining national attention, in part through the Occupy Wall Street movement and its evolution. Facebook and other outlets are brimming with stories about students facing 5-, even 6-figure debts, accompanied by calls for loan forgiveness, temporary waivers for unemployed graduates and other efforts to address debt that OccupyStudentDebt.com says "is slowly suffocating us."

Myriad factors influence student loan defaults in the short and long term. Two of the biggest causes behind the recent spike in defaults are rapidly rising student debt and a tough job market for graduates since the recession. Current default rates are also a fairly crude financial measure, and additional information about student borrowers suggests that their financial condition after graduation is worse than current default rates imply.

At the same time, default rates were much higher in the early 1990s, before changes made to the financial aid system helped to bring them down. Further changes made by Congress this time around should help struggling graduates. But rather than reducing incentives for schools and students to borrow (as in the 1990s), recent changes make it easier for borrowers to delay or dilute loan repayments on record-level debt. Though debt counseling and training in financial literacy have proven useful in helping borrowers to avoid delinquency, only strong job growth is likely to reverse the overall upward course of loan default rates.

Chart 1
Money problems not all equal
Cumulative 2-year cohort default rate, district states*
(Total institutions measured, 2009)



*Minnesota, Montana, North Dakota, South Dakota, Wisconsin and Upper Peninsula of Michigan
Source: U.S. Department of Education

The dog ate my payment

Student default rates are measured in cohort groups—in essence, the percentage of student borrowers due to begin repaying a federal loan during a federal fiscal year (Oct. 1 to Sept. 30) who default by the end of the following fiscal year. Borrowers who are more than 270 days delinquent by the end of the second fiscal year are considered in default unless special arrangements are made with the lender, which is fairly common. (This and other caveats to default rates are discussed later in this article and in the sidebar on page 12.) This official measure is called the 2-year cohort default rate.

Virtually any way the data are sliced, default rates got significantly worse after the recession for the large majority of higher education institutions in Ninth District states (including those in the Upper Peninsula of Michigan and all of Wisconsin). Though default rates vary considerably by institution type, the biggest increases were seen at public 2-year and for-profit schools of any program length, according to data from the U.S. Department of Education. But defaults also rose among public and private 4-year schools. (See Chart 1. These data concern only defaults on federal student loans; there are no public data on privately financed student loans.)

Neither is it a case of a few large schools running off the rails. Rather, increased default rates are widespread within institution types and sizes. For example, among 68 2-year public community and technical colleges in district states, only three saw default rates improve from 2007 to 2009 (the most recent data year available).

Default rates for most district states (all schools, all borrowers entering repayment) have climbed significantly over this period (see Chart 2). The biggest exception to the overall rise is the Upper Peninsula of Michigan, where student default rates actually declined. However, that region had comparatively high default rates to begin with and has just seven higher education institutions; four of them are 4-year institutions, which historically have had more stable default rates.

There is good news. Default rates in the district are generally—and significantly—lower than those for their

Continued on page 10

College finance from page 9

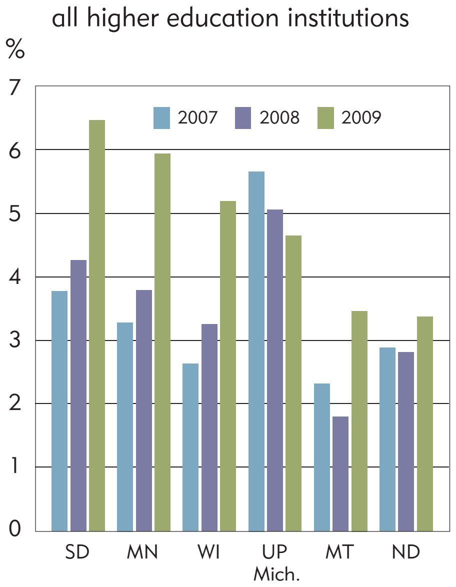
national peers across institution types (see Chart 3). That's particularly the case with proprietary (aka for-profit) schools, where the district default rate is about half the national rate and lower even than the district average for public 2-year schools.

Part of that advantage, however, is a quirk of data. Default rates are generally lower for 4-year programs offering bachelor's degrees, and the district is home to a few 4-year, for-profit schools with a nationwide footprint whose respectable default rates are attributed solely to their home states. Minnesota, for example, is home to Walden University and Capella University, two online universities with tens of thousands of student borrowers throughout the country. The two schools had a total of 18,000 students begin repaying loans in 2009, and their combined default rate was less than 5 percent. All those borrowers were treated as though they attended college in Minnesota.

Chart 2

Class dismissed

Cumulative default rate, all higher education institutions



Source: U.S. Department of Education

Pop quiz: Why?

Some of the culprits behind rising default rates are not particularly hard to identify. Like millions of other people, graduates are struggling to find jobs, and those are important as a means to pay off debt.

National American University (NAU) was founded in 1941 in Rapid City, S.D., and offers mostly secretarial and accounting classes. Today, the for-profit school offers a range of 2-year, 4-year and advanced degrees catering mostly to nontraditional, working adults (70 percent of them women), who can choose online courses or attend one of 35 campuses in 11 states, including 10 in South Dakota and Minnesota.

Of course, higher debt would be manageable if wages for new graduates were increasing as well. But adding insult to a tough job search are stagnant wages for newly minted grads fortunate enough to find a job.

NAU's default rate has typically been in the single digits, and it was 8.2 percent as recently as 2007. But the school's default rate spiked to 14 percent by 2009. "The number one reason is the economy," said Ron Shape, NAU chief executive officer. "There's no doubt that plays a role here" because in a sluggish economy, graduates are not able to find jobs as quickly as they have in the past. Shape said that until recently, 92 percent of NAU students found jobs within five years of graduation. The 5-year job placement rate is now about 83 percent, "and it's tied directly to the economy," Shape said.

North Dakota is a good—if contrary—example of the relationship between economic performance and the ability to repay debt. With the economy booming, default rates at the state's higher education institutions have risen only slightly of late (see Chart 2). At 3.4 percent, the Peace Garden State has the lowest statewide default rate in the district, and a sliver of the national rate of 8.9 percent.

The state's handful of proprietary schools are a good example. Their cumulative default rate was 4.9 percent in 2009—one-third the national rate and well below the district average for such schools. Josef's School of Hair Design is a for-profit vocational school with programs in cosmetology, skin aesthetics, massage therapy and nail technology. With locations in Fargo and Grand Forks, the school's cumulative default rate was just 4.4 percent.

"There are more positions available than we have graduates," said Heather Ostrowski, company recruiter and manager. And that's despite strong growth in similar vocational schools in the eastern part of the state. "I think [graduates] can find jobs, and if not locally, then for certain in [other areas of] North Dakota."

The connection between default rates and the job market is evident at many community colleges in other states. For example, annual job placement rates at Minneapolis Community and Technical College declined from 89 percent for 2007 graduates to 63 percent last year, according to Angela Christensen, MCTC financial aid director. Default rates rose by 50 percent from 2007 to 2009, to more than 12 percent.

Hibbing Community College and Mesabi Range Community Technical College, located about 10 miles from each other on the Iron Range of northeastern Minnesota, have both watched default rates for graduates reach 15 percent and 16 percent, respectively, in 2009, while rates of employment related to graduates' studies have fallen significantly, particularly since 2006 (see Chart 4), according to data from the Minnesota System of Colleges and Universities. (Financial aid officials at both schools declined to comment.)

It's not just the economy, stupid

But there's more to the default trend than a sputtering economy. In recent years, more students have taken out loans, and total debt levels have been ramping up to keep pace with steeply rising tuition. At 2-year public schools in Minnesota, the percentage of graduates incurring school-related debt rose from 54 percent in 2004 to 68 percent four years later, according to the National Postsecondary Student Aid Study. Over the same period, median total debt rose 40 percent (inflation-adjusted) to $11,000.

Debt levels are heading further north. In 2008, Congress increased limits for federal student loans to keep up with the rising cost of going to college. Students have responded by significantly upping their borrowing. Among all undergraduate students attending Minnesota postsecondary institutions, borrowing from 2007 to 2009 increased by 39 percent (inflation-adjusted) to $1.54 billion, according to a 2010 report by the Minnesota Office of Higher Education (MOHE). The majority of those borrowers are still in school and have not yet entered repayment.

And unlike other holders of consumer debt, student debtors are on the hook indefinitely for those loans. "It's extraordinarily difficult to discharge student loans in bankruptcy," said Tricia Grimes, a policy analyst with MOHE.

Of course, higher debt would be manageable if wages for new graduates were increasing as well. But adding insult to a tough job search are stagnant wages for newly minted grads fortunate enough to find a job. A study of college graduates by Rutgers University last year found that wages for a nationally representative sample of college graduates in 2009 and 2010 were 10 percent lower than wages for graduates in 2006 and 2007. An analysis of entry-level wages for college graduates (using the Current Population Survey) by the Economic Policy Institute found that inflation-adjusted wages through 2010 had been flat for five years (and lower than wages in 2000).

As such, student borrowers have hit the trifecta of debt woes—students are more likely to take out loans and have higher debt, they're having difficulty getting jobs and, even for those finding jobs, starting wages are not growing on pace with debt.

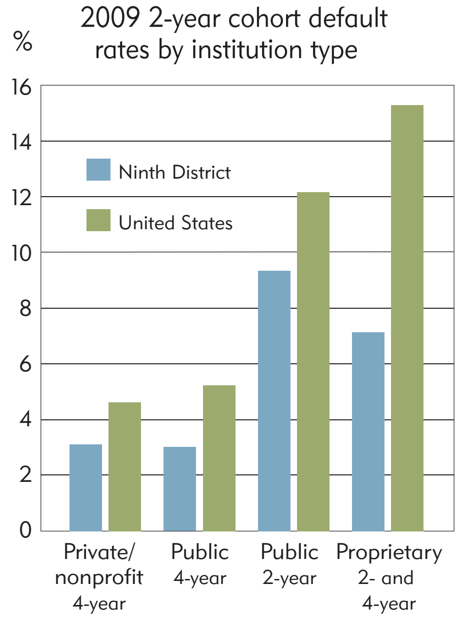
Default rates at Wisconsin's 16 public technical colleges reached almost 10 percent in 2009, more than double the 2007 rate. Comparing the graduating classes from those years shows that 2009 grads found fewer jobs (86 percent compared with 93 percent), fewer found jobs in their field of study (73 percent to 77 percent) and median graduate wages had actually fallen by 13 cents per hour (to $14.46) after adjusting for inflation.

These data don't count students who go to college but never graduate—unlucky winners of the double-whammy trifecta, if you will, because many of these students incur debt without earning the credentials that typically lead to higher-wage jobs (or any jobs) that help borrowers repay education loans. These students are particularly at risk for default. Though there are exceptions,

Chart 3

District defaults lower than nation

2009 2-year cohort default rates by institution type



Source: U.S. Department of Education

college completion rates in the district have fortunately been moving in the right direction.

If you think this is bad …

Gauging the seriousness of this default trend depends a bit on the context. Current default rates are in many ways a poor measure of the financial health of students and their ability to repay education loans. More careful accounting suggests that student loan repayments are more troubling than current default rates imply (see sidebar on page 12).

But it's not as though student borrowers have broken through some fundamental, edge-of-the-abyss barrier for defaults. While rates have risen considerably, they are still well below rates of the early 1990s (see Chart 5). Rates as high as 20 percent were not uncommon, particularly among public and for-profit, 2-year institutions.

There are a number of reasons for

the higher default rates back then, including much higher interest rates on loans. But a bigger reason is simply that they could be higher—there were no penalties on institutions whose students defaulted. That changed in 1991, when Congress required that colleges keep cohort default rates below a particular threshold—35 percent initially, 25 percent eventually. Failure to comply over a 3-year period meant their students would no longer be eligible for federal student aid. By 1997, more than 1,000 educational institutions nationwide had lost eligibility.

In the Ninth District, the Department of Education listed 333 colleges whose students were eligible for financial aid in 1991; by 2001, that number was down to 278, and in 2009 it was 257. The eliminated institutions were typically small, for-profit schools. Though default rates are rising today, all schools are a considerable distance from sanctions. In Minnesota, for example, the highest default rate in 2009 was 16.9 percent, at the Duluth Business University, a 4-year, for-profit school.

What, me worry?

The outlook on defaults is uncertain, because various factors could influence movement in either direction. Most sources agreed that faster economic (and thus job) growth is the best cure for ailing student borrowers. Said Grimes, at MOHE, "As the economy gets better, it would be surprising if rates didn't settle down a little bit."

On that front, things should get better, though not quickly or dramatically. In its annual forecast, the Minneapolis Fed predicted faster-than-average employment growth in 2012 across all district states, but unemployment is expected to decrease only moderately and remain above historical averages, in part because an improving economy is expected to pull more people who stopped looking for work back into the job market.

"Overall, I'm not very concerned about the cohort default rates," said Mark Kantrowitz, a leading researcher on student debt and default, and founder of FinAid, an online resource for financial aid. "I expect them to start decreasing in a few years, especially as unemployment rates return to pre-credit-crisis norms over the next four years."

In the near term, however, default rates are guaranteed to increase by bureaucratic quirk. That's because starting in 2014, schools will be required to track 3-year cohort default rates, rather than the current standard of two years. That means default rates will rise almost by definition, and in most cases quite steeply. (See sidebar on page 12 for more discussion and a 2-year versus 3-year cohort comparison of 2008 graduates.)

Interest rates are also a compounding factor. Rates on federal student loans were steadily lowered by Congress to 3.4 percent in response to the recession and slow recovery, but are scheduled to reset up to 6.8 percent for federal loans originated this summer unless Congress intervenes. Kantrowitz said that a 1 percent increase in the interest rate on a federal student loan corresponds to about a 5 percent increase in the monthly payment on a 10-year repayment term, and more as the loan term increases.

A penny borrowed …

Until the economy improves and job openings increase, many sources pointed to financial education as the best hedge against rising default rates. Suffice it to say, there's a lot of room for better grades in this department.

For example, Ostrowski, from Josef's School of Hair Design, said it's rare for prospective students to ask basic questions about average debt or starting wages. "It's a very smart question," said Ostrowski, who's been at the school for 13 years. "I'm never asked that question."

In a report last year on the financial outlook for private (nonfederal) student loans, Moody's Investors Service projected future charge-off rates at more than 20 percent by 2014, in part because "there is increasing concern that many students may be getting their loans for the wrong reasons, or that borrowers—and lenders—have unrealistic expectations of borrowers' future earnings. Unless students limit their debt burdens, choose fields of study that are in demand, and successfully complete their degrees on time, they will find themselves in worse financial positions."

"The thing that bothers me is that some people are borrowing every penny they can" to support a certain lifestyle, said Grimes, "and then they are really surprised later" that they owe so much money. "Buyer beware has to enter at some point. … But I believe financial literacy is beginning to creep in."

Montana offers a case study on how default rates can be corralled—at least to some degree—by lenders and higher education institutions. The state's default rate increased only modestly in recent years. It was previously the district's best at less than 2 percent and remains well less than half the national default rate.

"The secret to our success is fairly simple. We have committed significant resources in the form of employees who work with delinquent borrowers to keep them out of default," said Bruce Marks, director of student financial services for the Montana Office of the Commissioner of Higher Education. "We believe that if we can talk to a borrower, we can keep that borrower from defaulting. … Individually contacting each delinquent borrower is expensive and time consuming, but we have done exactly that in recent years."

That might sound like a simple bullet with too much silver in it, but financial counseling works. Kantrowitz, from FinAid, pointed out that many student borrowers are simply unaware of their options. Currently, borrowers can limit loan payments to 15 percent of their discretionary income, and all debt is forgiven after 25 years. Last year, Congress sweetened the terms even more, lowering the income-based payment to 10 percent and shortening loan forgiveness to 20 years, changes that are expected to go into effect this year.

The introduction of income-based repayment means "there's absolutely no reason why anybody should default on their federal student loans," said Kantrowitz. A borrower losing his or her job or earning less than 150 percent of the poverty line "has a zero monthly payment under income-based repayment. Yet borrowers still default on their federal loans. This demonstrates the need for improved communication with borrowers."

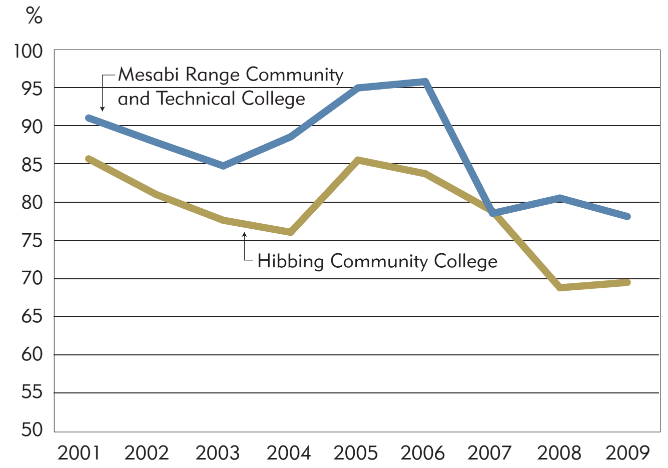
Sources widely agreed that communication has to start when students first consider taking on education debt. According to Grimes, schools and aid programs are introducing financial literacy tools to make sure students understand what they are getting into when they take out loans.

But even then, a school's hands can be tied if a student simply wants whatever federal loan money is available—money that comes without credit checks or other considerations. Aid formulas determine how much a student can borrow, and it might amount to several thousand dollars more than the student technically needs to cover tuition, books and other college expenses. But that extra money is hard for a student on a shoestring budget to turn down.

"If a check shows up in your mailbox for $2,500, would you send the check back, saying 'I don't want the excess money?'" asked Shape, from NAU.

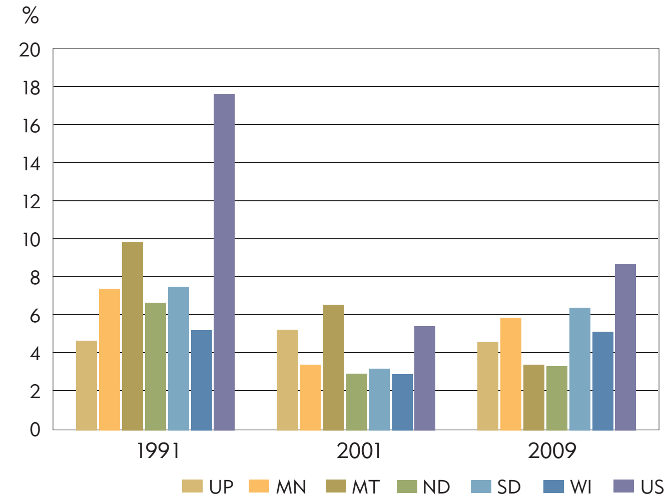
He believes giving schools the ability to deny excess loan money would help in the fight against high loan debts and defaults. He added that getting students to borrow more frugally "would be the best option, but I don't see it," because students have gotten used to borrowing with few strings attached. "That train has left the station." f

Chart 4
Graduate to unemployment?
Related employment rate of graduates



Source: Minnesota State Colleges and Universities

Chart 5
Bad, but not the worst
2-year cohort default rates



Source: U.S. Department of Education

The fine print on student default rates

There's a lot of information missing in today's official measure

When it comes to student loans, "default" is a word with a simple meaning, but many social connotations. Technically speaking, default occurs when borrowers are more than 270 days late on their loan payments. But it carries many negative implications about financial responsibility and maturity.

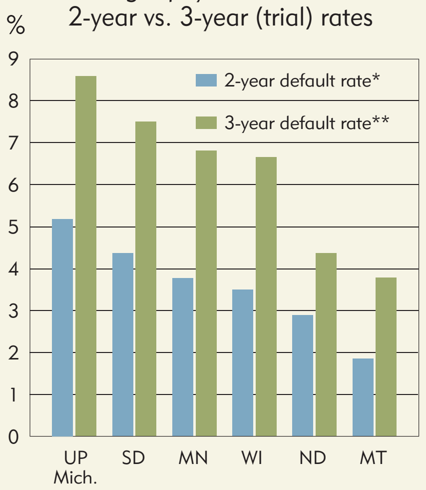
It turns out that the measurement of student loan defaults is similarly nuanced. Even the term "default" is a bit misleading. Many assume it refers to people who have skipped out on their debt, or will eventually, as happens with personal bankruptcy.

But as many borrowers have come to learn, student loans (federal or private) are virtually impossible to discharge, even in bankruptcy. Funds for repayment can be garnished from the wages of student debtors and from Social Security benefits. Even long-term defaulters "pay something," according to Tricia Grimes of the Minnesota Office of Higher Education. "If you earn some money, [lenders] are going to get some of it."

So while virtually all student loans must be repaid, default rates tell us nothing about the state of student debt—whether, or how soon, borrowers will make good on repayment and to what extent taxpayers foot the bill for loans gone bad. Plenty of other caveats exist, suggesting that current default rates do not offer a very clear picture of the financial wherewithal of students after graduation.

Chart 1 **Uphill battle**

Default rates for those entering repayment in FY2008
2-year vs. 3-year (trial) rates



*The percentage of students who entered repayment in federal fiscal year 2008 (between Oct. 1, 2007, and Sept. 30, 2008) and defaulted by Sept. 30, 2009.
**The percentage of students who entered repayment in federal fiscal year 2008 (between Oct. 1, 2007, and Sept. 30, 2008) and defaulted by Sept. 30, 2010.
Source: U.S. Department of Education

For example, default rates reflect the repayment status only of federal student loans—those originated through either the Direct Loan or the Federal Family Education Loan (FFEL) program (both administered through the U.S. Department of Education). A third source of loans is financed privately by financial institutions. These loans skyrocketed from about $6 billion in 2000 to $22 billion in 2007, or about one-quarter of all student loans that year. (Due to the recession, private lending pulled back to $6 billion in 2010, or less than 6 percent of all student loans.) These loans typically carry higher interest rates—a significant factor in monthly repayments. Students taking on private loans are also more likely to come from low-income families, go to a for-profit school and attend on a part-time basis—subgroups that tend to have higher-than-average default rates. Yet there are no default data on private student loans.

Current default rates also supposedly gauge repayments over two years, but that window is narrower than it might appear. The rate measures those entering repayment in one federal fiscal year (Oct. 1 to Sept. 30) and defaulting by the end of the following fiscal year. So ex-students entering repayment have just 12 to 24 months to fall more than 270 days (9 months) behind in loan repayments. So default rates capture loan performance of students who fall almost immediately and deeply into repayment problems.

Time out

Loan repayments typically start within six months of when a student graduates, has credit loads fall below required thresholds or drops out. But borrowers can postpone loan payments—through deferment or forbearance—based on economic hardship and other situations, such as continuation to graduate school. Though technically different, deferment and forbearance both provide relief from loan payments for up to several years. Once qualified, loans in deferment or forbearance are also considered current and thus counted (only) in the denominator of default rates, regardless of any underlying financial difficulty.

Surprisingly, very little is known about deferments and forbearance. The Department of Education publishes no public data on these categories, and institutional and other sources had little insight into the use of these tools over time.

A few studies shed some light on the matter. A July 2010 investigation of student loans by the *Chronicle of Higher Education* found that the percentage of those postponing their loan repayments grew from 10 percent in fiscal 1996 to 22 percent in fiscal 2007.

There are financial consequences to deferment and forbearance, because interest on outstanding debt continues to accrue on the loan balance for most loans in deferment or forbearance (the exception is for subsidized student loans in deferment). That typically adds up to thousands of dollars of additional debt—increasing the burden on students who delayed repayment because of financial hardship.

A study last year by the Institute for Higher Education Policy looked at a 4-year repayment window on 1.8 million FFEL loans originated in 2005. It found that 23 percent of borrowers used deferment or forbearance to avoid any delinquency on their loans. But another 21 percent became delinquent by 2009 and then applied for forbearance or deferment. Finally, 15 percent defaulted altogether by that year, and 4 percent were delinquent at some point but made payments to become current again on loans. Just 37 percent of borrowers managed to make timely payments without postponing payments or becoming delinquent or defaulting during the 4-year repayment period.

The widespread use of deferment and forbearance also means that the repayment performance of many student loans is effectively never measured because payments are postponed beyond the official 2-fiscal-years window. So in 2008, Congress responded by moving to a 3-year cohort rate, effectively extending the measurement window by an additional fiscal year. The new rates won't have regulatory teeth in terms of student aid sanctions until fiscal year 2014, but preliminary data from the Department of Education show a big jump in default rates in the district. (See Chart 1; note that the comparison uses the 2008 cohort, because 3-year data are not yet available for the 2009 cohort.)

A lifetime of default

What happens to loans after this comparatively short—and early—repayment window is mostly guesswork. Unlike other consumer borrowers, a student's likelihood of repaying an education loan actually goes up over time as he or she latches onto employment and builds a work history, which typically leads to higher wages in the long run.

The Department of Education does not technically track lifetime default rates. But its Federal Student Aid office has started estimating a so-called budget lifetime default rate that reflects rates over a 20-year period for a particular pool of loans (based on when loans originate, rather than when they go into repayment). Not surprisingly, those estimates have been rising for recent loan cohorts (see Chart 2). The *Chronicle of Higher Education* estimated in 2010 that one of every five government loans that entered repayment in 1995 had gone into default.

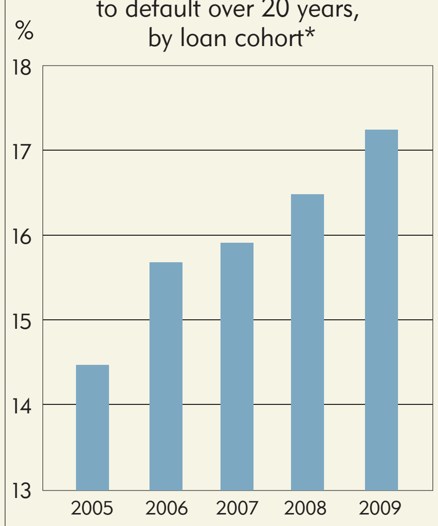
Critics of the current system say government should move away from nonpayment measures and instead track repayments, which would give policymakers a better idea of how many use financial aid as intended: Borrow money to go to college and improve skills, which should lead to a better job with higher income that makes it easier to repay loans.

In fact, a controversial pilot program that takes this approach was implemented last year. Congress imposed "gainful employment" regulations on for-profit schools intended to quash questionable recruiting practices by some schools and push institutions to pay more attention to job placement and wages earned after graduation.

—Ronald A. Wirtz

Chart 2 **Lifetime default estimates rising**

Percent of outstanding federal loan value estimated to default over 20 years, by loan cohort*



*Cohort groups are based on year of loan origination
Source: Federal Student Aid, U.S. Department of Education, memo dated Jan. 5, 2012

A prescription for better health outcomes: Electronic health records

Ninth District states lead in EHR adoption, but challenges abound to patient data sharing

By FRANK JOSSI
Contributing Writer

In the future, advocates hope to make health care a keystroke away for all patients. But for some, it's already a reality, even if their doctor is eating lunch—in Estonia.

Christopher Tashjian, a doctor with the Ellsworth (Wis.) Medical Clinic, was one of the first physicians in the country to have his practice recognized by the federal government for using electronic health records (EHRs). While checking his email in a McDonald's during a vacation in Estonia, Tashjian read an urgent message from a patient whose blood pressure medication had run out. After accessing the patient's medical record from his mobile phone, he sent off an electronic refill notice to a nearby pharmacy.

"I didn't want her to go without medication or have to come into the clinic to get one," said Tashjian. "The whole thing took about a minute to get done."

That's precisely the promise of EHRs, which digitize health records, allowing health care organizations to more easily share information among many necessary users, including patients and various health care providers, with the expectation that doing so will improve health care outcomes.

"The question consumers are asking is, 'We use technology to pay bills and to stay in touch with family and friends, so why shouldn't providers use technology to improve the care they deliver?'" said Parmeeth Atwal of the Office of the National Coordinator for Health Information Technology, which oversees EHR implementation. "Increasingly, I think it's an expectation."

In fact, it's becoming a reality in district states, which are ahead of most states in EHR implementation. But the nirvana of seamless and sophisticated data sharing is still a considerable distance away, both in the district and elsewhere. Research suggests that, when done properly, EHRs can deliver benefits to patient outcomes and an organization's bottom line. EHR implementation, however, is rife with technical complications and high startup costs.

Enter the federal government, which has made heaps of money available to encourage EHR installation and help train medical staff in its use, especially those in rural or disadvantaged communities without the financial assets to purchase digital records. While this assistance appears to help medical organizations make the EHR leap, money alone cannot untangle the many transitional challenges that come with electronic health records.

EHRs: Coming to clinic near you?

The National Center for Health Statistics released a report last year that showed that 34 percent of the nation's office-based physicians used basic but fully functional EHR systems. This includes things like patient history and demographics, clinical notes, medication and allergy lists, and computerized prescriptions. The NCHS report also noted that an additional 23 percent of physicians were using at least some EHR functions, meaning that most physicians are ankle-to-hip deep in digital records.

"That's huge. … All points say yes to electronic health care records," said Atwal.

And that's important because digital records, say advocates, will improve care by giving doctors access to a patient's history, helping them to determine necessary care and testing through best practices and ensuring that checkups are not missed. E-prescribing eliminates bad handwriting and pharmacy phone calls to double-check the scrawl.

Tashjian, one of the first doctors to meet federal guidelines for meaningful EHR use, is convinced that electronic records provide better care for patients. "You can get a longitudinal view of a patient's health history as opposed to a snapshot you often get using paper records."

Existing research on EHRs supports that view. Of the 154 peer-reviewed studies on EHRs from 2007 to 2010, 92 percent found better patient outcomes and other positive results from EHRs, according to a study done by the Office of the National Coordinator for Health Information Technology. In a *New England Journal of Medicine* 2008 study, physicians reported that EHRs improved patient communication, enhanced decision support with alerts and reminders, improved billing accuracy and prescribing, reduced paperwork and made referrals simpler.

Continued on page 14

Health records from page 13

"Just think of diabetics losing their limbs because of the disease and how improved care could allow them to avoid that fate," said Tashjian. In fact, a study of 27,000 diabetics in the September 2011 *New England Journal of Medicine* found that "EHR sites were associated with significantly higher achievement of care and outcome standards and greater improvement in diabetes care." And saving patients from surgery and a challenging recovery should translate into savings for patients and insurance plan sponsors, whether private employers or government.

Ninth District: Leaders, not laggards

But EHRs are exceedingly complex because of the sheer quantity of data generated by the many health care providers (even within a single health care organization) and their propensity for having different—and incompatible—information technology systems.

As a result, EHR development and implementation is geographically lumpy. Most of the country trails the progress of Ninth District states. Minnesota, North Dakota and Wisconsin are considerably ahead of the national average in terms of EHR penetration (see chart). Montana and South Dakota lag behind those states, but exceed the national average of doctors using fully functional EHRs.

That shouldn't necessarily be a surprise. Most of the region's patients are served by "integrated delivery systems"—health-speak for large hospital and clinic networks. Becky Schierman, manager of quality improvement for the Minnesota Medical Association, said having an EHR in those settings makes economic sense because physicians within the system can more easily share data on patients who go to one clinic for primary care and another for specialized treatment. "You probably don't find [high] adoption rates in states where there are still a large number of small, independent practices."

Schierman added that Minnesota was an early adopter, thanks to a state law—passed prior to similar federal legislation in 2009—that called for all practitioners to be using EHRs by 2015 and to be e-prescribing by 2010. Minnesota also offers incentives to providers for EHR adoption in addition to federal incentives.

The situation is largely the same elsewhere in the district. Sheldon Wolf, North Dakota's health information technology director, said that more than 70 percent of the state's population is served by a half-dozen regional health care systems, such as Sanford and Essentia Health. North Dakota also has a $10 million loan fund to help providers pay for costs associated with EHRs.

Most South Dakota residents receive care through large systems like Avera and Sanford Health, which have had EHRs for more than a decade, according to Kevin DeWald, the state health information technology coordinator. "Our integrated delivery networks were early adopters of EHRs."

How high can you jump?

But obstacles abound to faster EHR integration and development of more sophisticated applications. For example, despite the promise of data sharing, concerns over privacy and control of patient data have cropped up, adding to the complexity—and cost—of EHRs.

Research from a variety of sources, including the Congressional Budget Office, suggests that an EHR requires an upfront investment of $25,000 to $45,000 per physician and does not include annual operations and maintenance. In Wisconsin, many small clinics are considering selling themselves to integrated delivery networks to save the cost of having to buy their own EHR, according to Jesi Wang, project director for the Wisconsin Health Information Technology Extension Center in Madison.

Presumably, the long-term benefits of EHRs outweigh the costs, but it's not yet a slam-dunk, at least on paper. For example, it can be challenging to monetize improved care outcomes when payments are based on patient visits and procedures—or to capture the financial benefits of greater operational efficiency when reimbursements (particularly from government) are often based on the documented cost of that care. A survey last summer of 500 U.S. health practitioners by athenahealth, a web-based health care management company, found that three-quarters of physicians think EHRs can improve patient care, but 88 percent said that cost remains a big issue for implementation.

"I think one of the biggest challenges and one of the biggest barriers is money for buying the systems," said Jeff Pickett, who works with many rural providers in South Dakota as marketing and training coordinator for the nonprofit consultancy HealthPOINT. "In addition to the software and hardware costs, there's a fear that whatever they buy might have to be purchased again [for upgrades] in the future."

To encourage more EHR investment, in 2009 Congress passed the Health Information Technology for Economic and Clinical Health Act (HITECH), part of the federal stimulus bill at the time, offering providers both carrots and castor oil for adopting more seamless and integrated health record keeping.

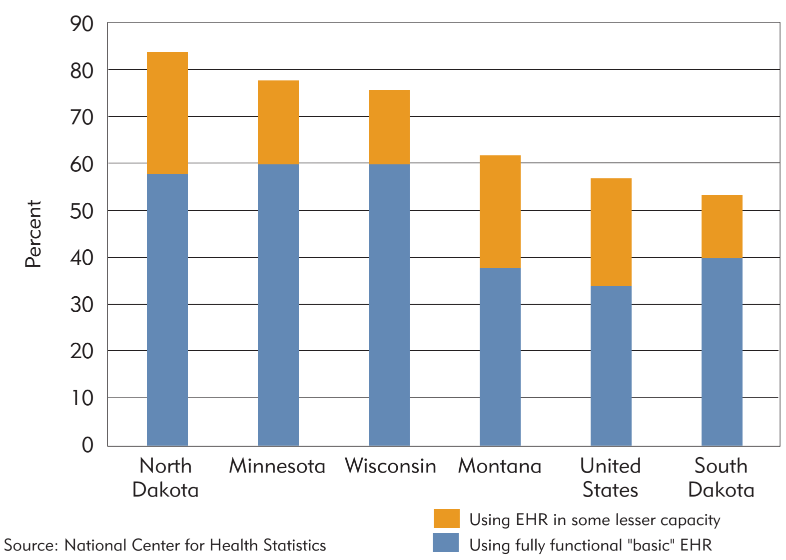
For starters, HITECH created a $27 billion EHR incentive fund to help clinics, hospitals and physicians pay for an EHR or upgrade one over the next decade. In tandem with this money, the Centers for Medicare and Medicaid Services established an initial set of 25 EHR guidelines for so-called meaningful use, which includes things like e-prescriptions and electronic access to laboratory and imaging results. Medicare and Medicaid providers (physicians and other eligible professionals, as well as hospitals) implementing at least 20 of these guidelines receive payments to defray EHR costs.

Incentive payments began in January 2011, and $1.3 billion had been disbursed as of December. Eligible Wisconsin providers received more than $76 million, and Minnesota $33 million; those in South Dakota have received $1.3 million, Montana $949,000 and North Dakota just $18,000. Sources said the large payment disparity among states is partly a function of when individual states got their EHR-based reimbursement programs for Medicaid and Medicare providers in place.

And for those lagging in implementation, there are consequences. Hospitals and clinics that do not have an EHR under way by 2015 could see their Medicare reimbursements dinged by 1 percent, and by an additional 1 percent every subsequent year.

EHRs: Coming to a clinic near you

Doctors' reported use of electronic health records, 2011



Source: National Center for Health Statistics

Reaching rural providers

Proper training is also a constant drag on integration. EHR training at small, rural clinics and hospitals often goes begging "because getting staff out there from a vendor to answer their questions is very expensive," said Paul Kleeberg, a doctor who heads up Key Health Alliance, a regional assistance center for Minnesota and North Dakota. "Distance creates big challenges."

In response to that challenge, the HITECH act set aside $677 million for the creation of nonprofit regional extension centers like Key Health Alliance. These organizations help health care providers—and particularly small, primary care offices and rural hospitals—select EHR vendors and train staff. Modeled on agricultural extension centers found throughout the country, the health-care-related centers hoped to help 100,000 primary care physicians within two years, a goal it achieved in mid-November. The program is designed to make the centers self-funded after a few years, drawing on consulting fees from providers.

Centers located in the district report that they have met or are approaching their recruiting goals for physician training. HealthPOINT, the regional extension center at South Dakota State University, has a goal of helping 800 health care providers and is nearly there, according to Pickett. Many clients are clinics with one to 10 doctors, he said, which constitute the majority of the state's physician population.

Wang, head of the Wisconsin Health Information Technology Extension Center, said her organization works with a lot of small practices in the northwestern part of the state and has signed up more than 1,700 small clinic physicians, nurses and staff at 45 of the state's 59 smaller hospitals, defined as 50 beds or fewer. "I think we see broadband challenges and less ability to see best practices from their neighbors because they're fewer and far in between," she said. Thanks in part to training, providers "are learning they can get [EHRs] done, and it will improve their care."

Though Montana's official EHR measures are ahead of the national average, the state "is a little bit behind the rest of the country," conceded Dan Maronick, marketing and outreach manager for Helena-based Health Technology Services, the regional extension center that covers Montana and Wyoming. One reason is because the state does not have many integrated medical networks.

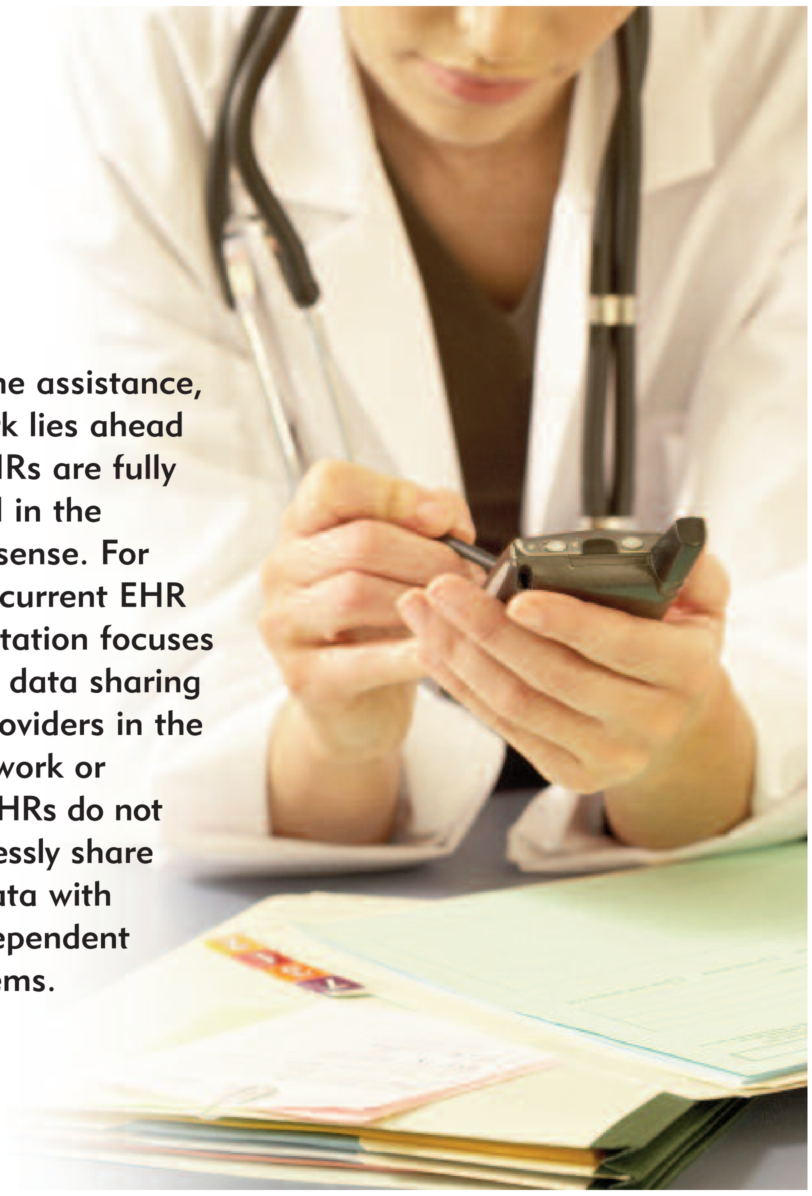
Maronick said the majority of hospitals and clinics in Montana are installing EHRs, "but some are saying they don't care about incentive money and that their paper system works fine. Some of the physicians are about to retire and don't want the bother."

But momentum for EHRs appears to be growing in the state. Maronick said his organization has attracted 900 physicians, just 100 short of its goal. About 80 percent of the region's 60 critical access hospitals—defined as 25 beds or more—have signed up for services, said Maronick. Many clients already have EHRs, but need help with training and adding functions to reach meaningful use. "We come in with IT experts and people who know 'meaningful use,' and we help them get up to speed so they can get their EHR incentive money," said Maronick.

Take two aspirin and boot up in the morning

Despite the assistance, much work lies ahead before EHRs are fully functional in the broadest sense. For example, current EHR implementation focuses mostly on data sharing among providers in the same network or system; EHRs do not yet seamlessly share patient data with other independent care systems (also called interoperability).

Avera Medical Group and the Brookings Health System hospital stand next to each another in Brookings, S.D. Both have an EHR from the software vendor Meditech, but the two systems don't automatically exchange data because different companies own each institution, said Brian Sterud, the hospital's information management director. Clinic physicians now simply log on to Brookings' Meditech EHR to enter data on patients they have seen at the hospital rather than use their office's EHR.



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To address interoperability, every state has to create a health information exchange (HIE) to enable noncompatible platforms to send and receive health data to and from each other. Wang sees it as a "network of networks" allowing physicians to use a state exchange to move patient data among Wisconsin care providers now, and later with other HIEs nationally. No state has an HIE up and running, although the federal government has contributed $400 million toward their creation.

Not all institutions are waiting for HIEs to be created. Several large hospitals in the Twin Cities collectively selected Epic as their EHR vendor in part because they believed one platform was a better way to quickly share health records.

Technical and bureaucratic obstacles also abound for both small and large providers. For instance, meaningful use standards—and the financial incentives they bring in tow—have introduced some unexpected problems. Kleeberg said that some large Minnesota hospitals and clinics already had sophisticated digital records for a number of years, but failed to meet federal criteria for meaningful use.

"We have been slow as a state to become meaningful users in our larger, more established facilities because we're already doing well beyond what's required, and it's harder to change a battleship than a boat," Kleeberg said. "Many of these places have built these great systems, but now they have to change the battleship."

If the move toward EHRs sounds complex, confusing and expensive, well, it is. Martin LaVenture, director of the Center for Health Informatics at the Minnesota Department of Health, calls EHRs a "multistep" journey that will improve as "gaps and barriers" are overcome and best practices inform new capabilities and assist in their implementation.

"We have adoption, but we have a long ways to go on effectively using electronic health records, including the exchange," LaVenture said. "The exchange represents the next wave of what we think needs to be achieved." f

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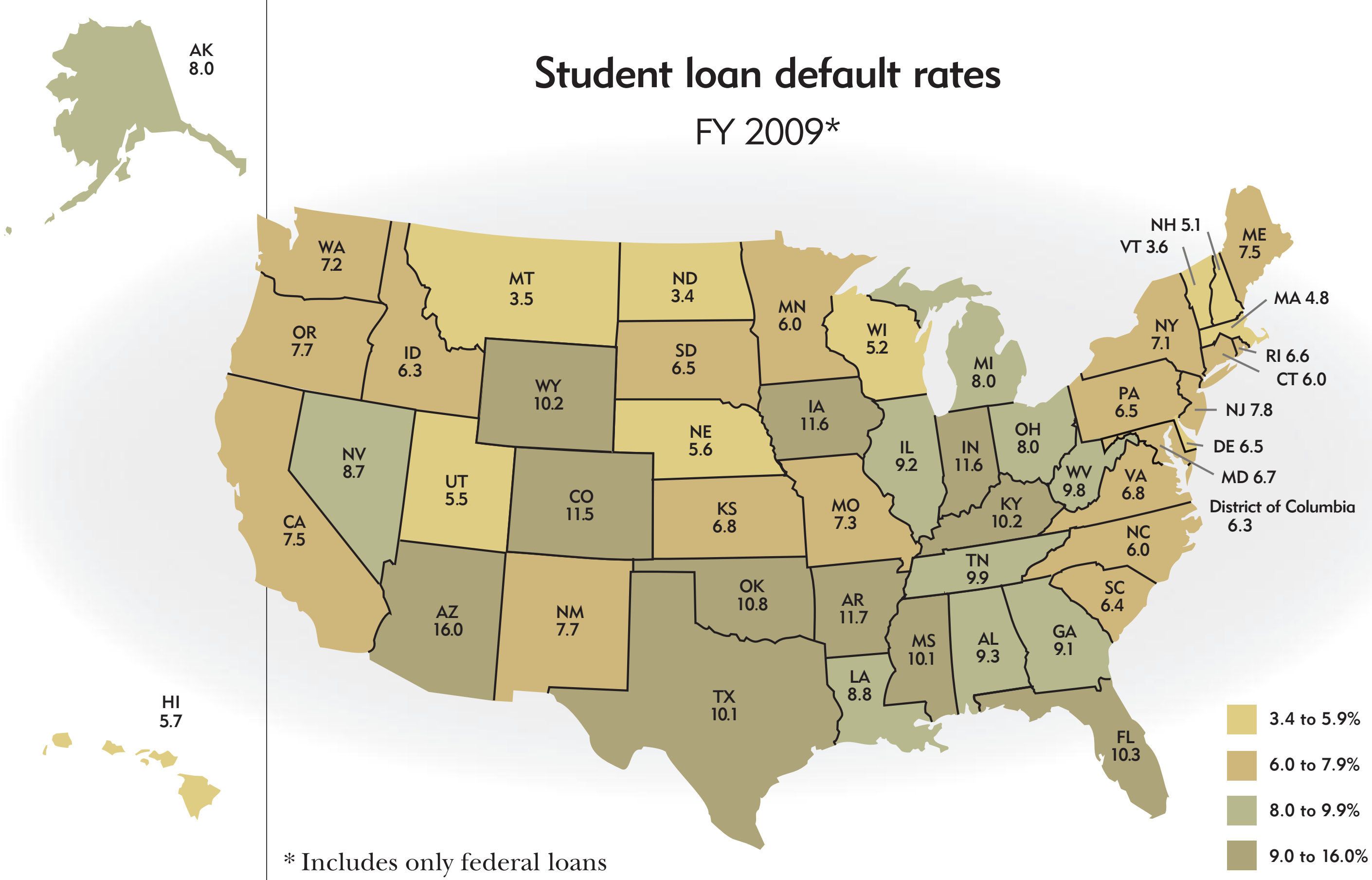
April 2012

Student loan default rates

FY 2009*



* Includes only federal loans

Source: U.S. Dept. of Education