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NATIONAL CONSUMER LAW CENTER®
Advancing Fairness in the Marketplace for All

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Response to the Consumer Financial Protection Bureau's Request for Information Regarding an Initiative to Promote Student Loan Affordability
78 Fed. Reg. 13327 (February 27, 2013)
Docket No. CFPB-2013-0004
Submitted April 8, 2013

The following comments are submitted on behalf of the National Consumer Law Center's low-income clients. The nonprofit National Consumer Law Center® (NCLC®) works for economic justice for low-income and other disadvantaged people in the U.S. through policy analysis and advocacy, publications, litigation, and training. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness.

Our comments on private student loans are based on our expertise and our experiences representing low-income consumers. NCLC's Student Loan Borrower Assistance Project provides information about student rights and responsibilities for borrowers and advocates and provides direct legal representation to student loan borrowers.[1] We also work with other advocates across the country representing low-income clients. In addition, we seek to increase public understanding of student lending issues and to identity policy solutions to promote access to education, lessen student debt burdens, and make loan repayment more manageable.[2]

I. Summary of Comments

Large and growing numbers of private student loan borrowers are falling behind on their loans. Data is not publicly available on precisely which lenders, loan features and borrowers are most at risk of defaulting. However, the available data strongly suggests that a large portion of private student loan (PSL) defaults is attributable to irresponsible lending practices that became particularly widespread during the period leading up to the credit crisis, roughly from 2006-2008. The loans were characterized by high volume,

[1] *See* the Project's web site at www.studentloanborrowerassistance.org. Most of the clients we represent are low-income borrowers living in Massachusetts, although we also receive e-mails from thousands of borrowers each year from other states.
[2] NCLC regularly conducts research and publishes reports on student loan issues. *See, e.g.*, National Consumer Law Center, The Student Loan Default Trap: Why Borrowers Default and What Can Be Done (2012), *available at* http://www.studentloanborrowerassistance.org/legal-policy/. NCLC also publishes and annually supplements practice treatises that describe the law currently applicable to all types of consumer transactions, including *Student Loan Law* (4th ed. 2010 and Supp.). These comments were written by Arielle Cohen, Deanne Loonin, Robyn Smith and Persis Yu.

lax underwriting, heavy use of Direct to Consumer (DTC) lending, loan amounts higher than Cost of Attendance, and variable interest rates with very high margins.

The Request for Information focuses on options for creating a loan modification program, as do these comments. Given rising default rates and borrower distress, providing payment relief for borrowers is essential. However, loan modifications, while important, should be combined with other policies to provide relief to borrowers and prevent defaults in the future. These policies include:

- Restoring bankruptcy rights for all student loan borrowers;
- Mitigating the impact of negative credit reporting on borrowers' ability to access housing, employment opportunities and other basic needs;
- Eliminating predatory student lending, including development of sound underwriting standards ensuring ability to pay;
- Including provisions for flexible repayment and death and disability discharges in new originations;
- Improving the availability and accuracy of information provided to students before they borrow; and
- Vigorously enforcing federal and state laws to protect borrowers from origination and collection abuses and for-profit school abuses.

With regard to loan modifications, because of the lack of important data, these comments are structured as a discussion of the potential trade-offs of different approaches, rather than as a recommendation of one particular model. However, any proposed modification program, no matter how it is structured, should meet the following essential criteria to ensure it helps the borrowers most in need of assistance.

1. **Affordability**: Loan modifications must provide a real financial benefit to borrowers and must be linked to the borrower's realistic ability to repay. This is essential not only to providing real relief to borrowers in distress, but also to prevent high re-default rates which would make the program not worth the expense from the servicers' and investors' perspective.

2. **Preservation of Borrower Protections**: Participation in a loan modification program or acceptance of a loan modification offer should not result in a borrower losing any rights or protections she would otherwise have. This includes forbidding any waivers of rights as a condition of modification and also structuring the program in such a way that previously exempt income or assets of the borrower are not placed at risk (for example, through the expanded collection powers available for federal loans) and time limits for collection are not lengthened beyond previously applicable statutes of limitations.

3. **Enforceability**: Borrowers must have the ability to enforce their rights under the modification program, including the ability to dispute and appeal denials of eligibility and mistakes in the terms offered and to raise claims and defenses related to the program in legal proceedings.

4. **Efficiency and Scale**: The program must be designed to reach as many as possible of the borrowers in or at risk of default, both in order to assist those borrowers directly and in order to have a positive impact on the broader economy. Eligibility criteria must be broad enough to encompass all borrowers in need of assistance and the program must be efficient in reaching those borrowers and in minimizing the barriers to uptake. Reaching scale will require either mandating loan modification offers or providing effective incentives sufficient to induce servicers and lenders to modify a large number of eligible loans.

5. **Fairness**: Any program, particularly one that relies on incentives to servicers or on purchase of loans from existing servicers and lenders, must not be a bailout or giveaway to lenders. This is essential to avoid moral hazard on the part of lenders and servicers. The industry should not be allowed to externalize the costs of the shortsighted and destructive lending decisions it made, particularly between 2005 and 2008. Furthermore, the program must be structured to prevent servicers and lenders from "creaming" or selecting particular loans for modification in order to maximize their own finances and from receiving credit or incentive payments for modifications or other actions they would have taken anyway. Finally, the program must have protections to prevent a disparate impact on borrowers of color or other protected groups.

We urge the CFPB to evaluate any proposed loan modification program to determine whether it will – at a minimum – satisfy these five essential criteria. We further urge the CFPB to gather any additional necessary information about industry practices and incentives and about the characteristics of borrowers in distress as quickly as possible so that it can choose the most appropriate of the available policy options and implement it without delay.

II. Introduction

Predatory private student lending shattered the dreams of many individuals seeking to better their lives through education. These loans have become a curse, not an opportunity, for all too many borrowers. Those harmed by lenders' predatory practices are now stuck trying to get those same lenders to provide relief.

Large and growing numbers of private student loan borrowers are falling behind on their loans. Data is not publicly available on precisely which lenders, loan features and borrowers are most at risk of defaulting. However, the available data strongly suggests that a large portion of private student loan (PSL) defaults is attributable to irresponsible lending practices that became particularly widespread during the period leading up to the credit crisis, roughly from 2006-2008. Private student loan origination during these boom years was driven by the demand for student loan asset backed securities (SLABS). The loans were characterized by high volume, lax underwriting, heavy use of Direct to Consumer (DTC) lending, loan amounts higher than Cost of Attendance, and variable interest rates with very high margins.

Some borrowers who were targeted for these loans have also faced the difficulty of entering the workforce during the Great Recession. The poor economy has had a huge impact on the job prospects of these borrowers and exacerbated student loan burdens, but is only part of the story. Getting to the bottom of the default problem requires an understanding of the diversity of students. The majority of college students are non-traditional, meaning that they did not enroll in college after high school, they work part-time or full-time as they attend school, or they support dependents.[3] These student borrowers tend to default at higher rates, during good or bad economic cycles.

Aggressive marketing of PSLs impacted some borrowers more than others. Low-income and non-traditional students were particularly hard hit. While there was an overall increase of the percentage of undergraduates with PSLs from 5% in 2003-04 to 14% in 2007-09,[4] increases were even larger among students at for-profit colleges (from14.1% in 2003-04 to over 40% in 2007-08)[5], and among students of color (increasing from 4.1.% and 4.6% to 17.3% and 13.2% for African-Americans and Hispanics, respectively).[6]

Not surprisingly, default rates are high for all PSLs originated during the boom period, and get higher with each vintage of loan originations. Loans that are part of SLABS have particularly high default rates, with some pools of loans expected to experience lifetime default rates higher than 50%.[7]

While it is important to improve loan origination, servicing and loss mitigation for all student borrowers going forward, there is good reason to pay special attention to the cohort of borrowers who were harmed by predatory lenders and the financial market's huge appetite for SLABS. The impact of payment unaffordability and default on these borrowers is huge and has a negative impact on the overall economy. The burden on low-income borrowers is even worse, since these borrowers, as discussed below, are faced with the Catch-22 of forgoing essential needs in order to stay current or risking loss of employment, housing and other opportunities because of the negative credit impact of default and other adverse consequences.

The goal of these comments is to explore options for providing relief to borrowers harmed by what will hopefully prove to be a short period of unusually aggressive and inappropriate lending activity. If future loan originations are properly regulated, there should be diminished need for loan modification options.

Because of the unusual conditions and serious hardships faced by this group of borrowers, the need for assistance is great, and the risk of moral hazard is low – investor demand drove the origination of these loans, and with appropriate regulation, private lenders will hopefully not return to these bad practices.

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[3] U.S. Dep't of Education, Findings from the Condition of Education 2002: Nontraditional Undergraduates, Nat'l Ctr. for Education Statistics (2002); Center for Law and Social Policy, Yesterday's Nontraditional Student is Today's Traditional Student (June 29, 2011).
[4] Consumer Financial Protection Bureau, Private Student Loans: Report to the Senate Committee on Banking, Housing, and Urban Affairs, the Senate Committee on Health, Education, Labor, and Pensions, the House of Representatives Committee on Financial Services, and the House of Representatives Committee on Education and the Workforce, 39 (August 29, 2012) [hereinafter "CFPB: Private Student Loans Report"].
[5] CFPB: Private Student Loans Report, Table 6.
[6] CFPB: Private Student Loans Report, Table 4.
[7] CFPB: Private Student Loans Report, 64.

The CFPB should be aggressive and creative in seeking solutions for these borrowers, including but not limited to creation of a loan modification program. Just as in the mortgage industry, there seem to be institutional barriers to finding the win-win situation that puts borrowers back on the track of repaying their loans. Laws and regulations that require private student lenders to have workable repayment programs for those who have gotten in trouble may be necessary to jump start this process. We discuss these options in these comments.

Mandatory loss mitigation can be justified both as a matter of ability to repay and as a safety and soundness issue. From a safety and soundness perspective, institutions need to anticipate the possibility that the loan debt may prove unsustainable for some borrowers and to put in place programs to turn those loans into performing loans rather than write-offs.

The Need for More Information. Throughout these comments, we note gaps in the publically available data on the private student loan industry. Information on the existing incentives of lenders, servicers and collectors, the terms of loans and on the payment, default and re-default patterns of borrowers will be helpful to creating an effective loan modification program. The lack of this type of information in the private student loan context is a major impediment to understanding the scope of the problem and helping borrowers. To the extent that any necessary information has not been provided in response to this request for comments, the CFPB should use its broad research and supervision authority to collect such information.[8] As part of its efforts to improve loan modification options for student, the CFPB should increase its data collection and analysis. It should collect and analyze data about existing loan modification programs and new ones that it might establish, to evaluate how they are working.

III. Scope of Borrower Hardship

A. What are the primary drivers of private student loan borrower distress?

The agency asked about the characteristics that might predict distress at loan origination and during repayment.

There is very little empirical research on the causes of student loan distress. What research is available is based mainly on federal student loan data. The CFPB's own research is one of the richest existing data sources for possible predictors of default in private student loans. Research based on federal loans has limited relevance to determining which features of PSLs at origination predict default. However, the federal data is helpful in considering what circumstances lead borrowers to default later.

[8] The CFPB should collect data not only for its own purposes but to improve the availability of information for borrowers and policy makers. One important step the CFPB could take would be to require reporting of private student loan information to the National Student Loan Data System (NSLDS), which currently has data only on federal student loans. Consumers would then be able to see all their loans, both federal and private, in one place and receive counseling based on their total student loan debt. In addition, colleges would be able to assess the usage of private loans among their students and craft policies to better encourage the use of federal loans first. Researchers and policy makers would be able to analyze patterns of borrowing and determine if consumers are receiving the information they need to make informed decisions.

1. Loan Features and Origination Practices That Lead to Default

Based on default rates of PSLs, it is clear that certain loan features and origination practices result in higher default rates. These features were hallmarks of the lending boom leading up to the crisis and were the result of lenders pushing the origination of loans that would produce the most profit when they were sold on the secondary market, rather than offering products that met the needs and repayment abilities of borrowers. The factors discussed below were known to lenders at the time of origination. Not all lenders engaged in all these practices to the same extent. For example, non-profit lenders generally have much lower default rates as a result of better policies, such as choosing not to make loans to students at for-profit schools.

Loan features and origination practices that are associated with high default rates include:

Predatory Terms and Fees

Unlike federal loans, there are no limits on the interest rates that can be charged for private student loans. There are also no limits on origination and other fees. We surveyed a number of private loan products in our 2008 report, "Paying the Price."[9] All of the loans in our survey had variable rates. The lowest initial rate in our sample was around 5% and the highest close to 19%. The average initial disclosed annual percentage rate (APR) for the loans in our survey was 11.5%. Our results are confirmed by the CFPB's research, which showed private lenders charged most borrowers interest rates higher than federal loans, and charged particularly high rates to borrowers in certificate and continuing education programs.[10]

Some of the margins in our survey were shockingly high. Multiple loans in our survey had margins of close to 10%. This means that the variable rates for those loans were set at the prime rate plus nearly 10%. The average margin was about 4.8%. A review of Sallie Mae loans found that rates for products targeted to supposedly higher-risk borrowers, such as community college students and adults returning to school, could be as high as prime plus nine percent.[11]

These high cost loans failed at very high rates. According to the CFPB, default rates on private student loans spiked following the financial crisis of 2008 as the recession "…exposed the weakened underwriting standards that were fueled by the capital markets during the securitization and lending boom."[12]

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[9] National Consumer Law Center, Paying the Price: The High Cost of Private Student Loans and the Dangers for Student Borrowers (March 2008) [hereinafter "NCLC: Paying the Price"], *available at* http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/Report_PrivateLoans.pdf.
[10] CFPB: Private Student Loans Report, Appendix Fig. 2.
[11] Christopher Mazzeo, *Private Lending and Student Borrowing*, *in* Footing the Tuition Bill 74, 81 (Frederick M. Hess ed., 2007).
[12] CFPB: Private Student Loans Report, 63.

Lending to Borrowers at Inferior Schools

A number of studies affirm that the type of institution attended is correlated with default.[13] For-profit colleges consistently have the highest federal student loan default rates, with a 15% federal student loan cohort default rate for borrowers entering repayment in 2009.[14] Borrowing rates are also highest in the for-profit sector.[15]

Both Sallie Mae and Citi's Student Loan Corporation have identified lending to students attending schools with lower graduation rates and lower earning potential as the main source of private student loan credit deterioration.[16] These loans represented about 14% of Sallie Mae's private education loan portfolio, but accounted for 54% of charge-offs in the company's portfolio in 2008. [17] Even Sallie Mae's then-CFO Jack Remondi admitted that this is "… [o]bviously, a business model that does not make sense."[18]

Direct to Consumer Loans

Particularly during the heyday of predatory lending, many lenders aggressively marketed their student loan products directly to consumers. Another feature of lending in the years leading up to the crisis, and related to the use of Direct to Consumer lending, was an increase in loan amounts that exceeded the "Cost of Attendance" calculated by schools.[19] By marketing loans directly to students, these lenders bypassed school financial aid offices, which, when they assist borrowers in putting together a financial aid package of grants, federal loans and private loans, cap the total amount borrowed at the cost of attendance.

Among other findings, the CFPB noted that from 2005-2007, lenders increasingly marketed and disbursed loans directly to students, reducing the involvement of schools in the process. The CFPB concluded that the credit quality of loans that were not school-certified was materially worse than average.[20]

Lack of Information or Counseling

The Consumer Financial Protection Bureau's collection of complaints about private student loans indicates high levels of confusion among borrowers regarding their loans and the financial aid process. Many borrowers did not know the rules for federal aid eligibility and some could not identify whether they had federal or private loans.[21] The increase in Direct to

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[13] *See, e.g.*, Mary Nguyen, Degreeless in Debt: What Happens to Borrowers Who Drop Out, Education Sector at 1 (Feb. 2012), *available at* http://www.educationsector.org/publications/degreeless-debt-what-happens-borrowers-who-drop-out.
[14] The Project on Student Debt, Sharp Uptick in Federal Student Loan Default Rates (Sept. 12, 2011).
[15] *Id.*
[16] Fitch Ratings, Private Education Loans: Time for a Re-Education, 7 (Jan. 28, 2009). Citi sold Student Loan Corp. to Discover in 2010.
[17] Alejandro Lazo, *Sallie Mae Forecasts Surge in Defaults*, Washington Post (Jan. 23, 2009).
[18] SLM Corporation Q4 2007 earnings Call Transcript (Jan. 23, 2008).
[19] CFPB: Private Student Loans Report, Figs. 7 and 7a.
[20] CFPB: Private Student Loans Report, 25.
[21] Rachel Fishman, What Borrowers Don't Understand About Student Loans May Hurt Them, *Higher Ed Watch* (June 18, 2012).

Consumer lending, discussed above, contributes to borrower confusion by eliminating the school financial aid office from the transaction.

Various studies have found a relationship between knowledge about student loans and likelihood of default.[22] It is possible that more comprehensive information and counseling prior to a borrower incurring the loan debt would prevent some instances of financial distress down the road. Regardless, disclosures and counseling are never enough to provide substantive protection for borrowers. In a market full of securitized, complex products often made for Wall Street, not Main Street, borrowers cannot rely on disclosures to ensure they get the loan they want and can afford.

Failure to exhaust federal loan options.

At least in part due to the confusion between federal and private loans, and perhaps also due to the increase in Direct to Consumer lending, the majority (52%) of private student loan borrowers in 2007-08 borrowed less than they could have in federal Stafford loans.[23] This is borne out by the experiences of borrowers who contact NCLC. A first generation college and law student and member of the Air National Guard told us:

> The [law] school gave me a partial scholarship. I took out loans to make up the rest of the tuition and living expenses. These loans were confusing – somehow I ended up taking out a lot of private loans instead of taking out the max of my federal loans.

He couldn't find a job after graduating and went into default. He now worries that he won't be able to pass the moral character portion of the bar exam because of the default.

In its July report, the CFPB found that 40% of private loan borrowers who also obtained a Stafford loan did not exhaust the total amount of Stafford loans for which they were eligible. The agency refined this analysis and released new information in August 2012. The new analysis includes private student loan borrowers who chose to borrow 0 in Stafford loans, regardless of whether they applied for federal aid or not. Based on this approach, the proportion of students who borrowed a private student loan but did not exhaust the individual Stafford maximum is 54.5%.[24]

Borrowers that fail to exhaust federal student loan eligibility are likely to borrow higher amounts from private student lenders. This increases the possibility of financial distress primarily because federal loan borrowers have access to flexible and affordable repayment and postponement options if they are unable to make standard payments on their loans. As discussed in detail below, private loan borrowers do not have these options.

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[22] *See generally* National Consumer Law Center, The Student Loan Default Trap: Why Borrowers Default and What Can Be Done (2012) [hereinafter "NCLC: The Student Loan Default Trap"], *available at* http://www.studentloanborrowerassistance.org/legal-policy/.
[23] The Project on Student Debt, Private Loans: Facts and Trends (July 2011).
[24] CFPB: Private Student Loans Report.

2. Borrower Circumstances That Predict Default

The limited data on drivers of student loan defaults after origination is based mainly on federal loan data. However, these same predictors apply to private student loan borrowers, since they are essentially factors that reduce borrower income or ability to withstand financial shocks.

It is difficult to predict a particular individual's future income at the time of origination or even at the time she completes school. Lenders can, however, detect useful patterns by examining data such as institutional job placement rates and average starting salaries. However, some of this data, particularly job placement rates used by unscrupulous schools, is notoriously unreliable. Despite problems with the federal student loan default rate calculation, this information can also be useful in predicting the likelihood of borrower distress after completion or during repayment.

Nearly all of the predictors discussed in the preceding paragraph relate to institutional qualities and performance data. There are also some studies that cite individual characteristics that may be risk factors for default, including lower parental education attainment and high incidence of life traumas, including health crises. The latter category, including health and family problems, is nearly impossible to predict.

These factors should be used with a measure of caution. For example, the CFPB noted in its August report that private student lenders' use of cohort default rate data to make underwriting decisions may present fair lending concerns because racial and ethnic minority students are disproportionately concentrated in schools with higher cohort default rates.[25] This does not mean that high cohort default rates and other measures should not be considered. Instead, care should be taken that all borrowers have access to affordable higher education options, and that lenders are not given free rein to gouge the most vulnerable consumers under the guise of "equal opportunity."

Some of the most commonly cited causes of federal student loan defaults are:[26]

Low Incomes and Unemployment

It should not be surprising that in studies of federal student loans, one of the strongest predictors of default is whether the borrower has sufficient income to pay back the loans. Researchers compiling a 2009 review of the literature on student loan defaults stated simply that most students default because their personal income is inadequate to keep up with their payments.[27] This is likely magnified among students from lower-income families because the unavailability of a family safety net makes it more difficult to make payments during fluctuations in income.[28]A study using Department of Education data found that the percentage of borrowers

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[25] CFPB: Private Student Loans Report, 80.
[26] For additional discussion of these factors, *see* NCLC: The Student Loan Default Trap.
[27] *See generally* Jacob P.K. Gross *et al.*, *What Matters in Student Loan Default: A Review of the Research Literature*, Journal of Student Financial Aid (2009).
[28] *Id*.

who still owed student loans after ten years was related to the borrowers' salaries.[29] Unemployment is another risk factor and clearly connected with lower incomes.

Lack of Completion

Lack of completion was the most commonly cited risk factor for default in the studies NCLC reviewed.[30] In a 2008 Power Point presentation, the Department of Education stated that of the borrowers who defaulted on their Direct Loans (6-7 million borrowers), 70% withdrew before completing their program.[31]

Completion rates are low in all sectors of higher education. According to the Department of Education, 58% of first-time full-time students who started college in 2004 completed a bachelor's degree within six years. Students at four-year for-profit colleges had only a 28% graduation rate.[32]

This does not necessarily mean that graduation causes lower default rates. Though there is a strong correlation between completion rates and default, the cause and effect is less clear, largely because failure to complete is associated with other characteristics. Whether they borrow or not, those who do not complete are more likely to come from low-income backgrounds and their parents are more likely to have lower levels of education than those who complete.[33] Borrowers who fail to complete generally have higher unemployment rates and lower incomes.[34]

Type of Institution

For-profit colleges consistently have the highest two-year default rates, with a 15% cohort default rate for borrowers entering repayment in 2009.[35] The Institute for Higher Education Policy found that borrowers who attended four-year public or private nonprofits saw only a third or fewer borrowers become delinquent or enter default. In contrast, more than half of the students attending for-profit schools and two-year public institutions became delinquent or defaulted.[36] Another study, by the Institute for Higher Education Policy found that borrowers who *graduated* with a certificate had a similar default rate as those who *dropped out* from public four year schools. [37]

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[29] Susan P. Choy & Xiaojie Li, Dealing with Debt: 1992-93 Bachelor's Degree Recipients 10 Years Later, U.S. Dep't of Educ. National Ctr. For Educ. Statistics (June 2006).
[30] *See generally* NCLC: The Student Loan Default Trap.
[31] John Pierson & Mark Walsh, Promote Student Success, Manage Delinquency and Prevent Defaults, U.S. Dep't of Education (2008), Slide 31.
[32] National Center for Education Statistics, Postsecondary Graduation Rates, U.S. Dep't. of Education (2012). Note that these official completion rates only track first time full-time students.
[33] Lawrence Gladieux & Laura Perna, Borrowers Who Drop Out: A Neglected Aspect of the College Student Loan Trend, National Center for Public Policy and Higher Education, 6-7 (May 2005).
[34] Nguyen, *supra* note 13 at 1.
[35] The Project on Student Debt, Sharp Uptick in Federal Student Loan Default Rates (Sept. 12, 2011).
[36] Alisa F. Cunningham & Gregory S. Keinzl, Delinquency: The Untold Story of Student Loan Borrowing, Institute for Higher Education Policy, 21 (March 2011).
[37] *Id*. at 24.

While not all research reaches the same conclusion, a number of studies have concluded that even after controlling for student demographics and completion rates, default rates are still much higher at for-profit institutions.[38]

Loan Amount

There have been contradictory findings regarding whether the amount of debt has a strong impact on default. According to a few studies, the amount of debt is not a good predictor of default when other characteristics are considered.[39] The Institute for Higher Education Policy found, for example, that borrowers who defaulted had fewer loans and lower loan amounts that those who did not default.[40] This may be because those who drop out generally have lower balances, but are otherwise at risk for default.

However, in a 2006 report, the Department of Education followed a group of federal student loan borrowers for ten years and found a correlation between the amount borrowed and default.[41] Twenty percent of the borrowers in the study with $15,000 or more in Stafford loans defaulted at some point, compared to 7%-8% of those who borrowed less than $10,000.[42]

Race and Ethnicity

Some researchers have found a correlation between race and higher default rates, mainly among African American and in some cases Latino and Native American student borrowers.[43] However, the researchers generally acknowledge that relatively little is known about the factors that contribute to this difference. Among other issues to consider, these students tend to borrow more. According to some studies they are also more likely to be unemployed and less likely to be satisfied with their educational experiences. Discrimination after leaving school may also play a role.[44]

3. Debt-to-Income Ratios of Borrowers in Distress

The agency asked about typical debt-to-income ratio of borrowers in distress. Although there is little empirical evidence on this point, we do have information from the borrowers who contact us through the Student Loan Borrower Assistance Project and from the clients we represent.

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[38] *See, e.g.*, David J. Deming, Claudia Goldin, Lawrence F. Katz, The For-Profit Postsecondary School Sector: Nimble Critters or Agile Predators? Nat'l Bureau of Economic Research (Dec. 2004); Mamie Lynch, Jennifer Engle, & José L. Cruz, Subprime Opportunity: The Unfulfilled Promise of For-Profit Colleges and Universities, The Education Trust, 28 (Nov. 22, 2010).
[39] *See, e.g.*, Robin McMillion, Student Loan Default Literature Review, TG Research and Analytical Services, 13-14 (Dec. 22, 2004).
[40] Alisa F. Cunningham & Gregory S. Keinzl, Delinquency: The Untold Story of Student Loan Borrowing, Institute for Higher Education Policy, 22 (March 2011).
[41] Susan P. Choy & Xiaojie Li, Dealing with Debt: 1992-93 Bachelor's Degree Recipients 10 Years Later, U.S. Dep't of Educ. National Ctr. for Educ. Statistics (June 2006).
[42] *Id.* at vii.
[43] *See* NCLC: The Student Loan Default Trap at 14.
[44] *Id.*

Most of our clients originally incurred private loan debt under about $35,000. By the time they seek legal assistance, this balance has usually ballooned considerably. We also have some clients with much higher levels of debt and hear from borrowers through our web site with higher balances, particularly graduate students.

For our low-income clients, the debt-to-income ratios are extremely high. Many of our clients are living solely on public assistance or Social Security income. In those cases, the standard private loan monthly payments can be as much as 80% of their income or even more. Even for employed borrowers, the debt-to-income ratios of our clients are extremely high. An example is Rachel, who graduated with a degree in fashion marketing, but has been unable to find work in her field. Her monthly take home pay is less than the monthly payment due on her student loans.

B. What is the impact on borrowers of being unable to afford private student loan payments and/or of going into default?

The focus of NCLC's advocacy is on assisting low-income borrowers. For these borrowers, the impact of unaffordable private student loans is to force borrowers to choose between going without essentials or facing the severe negative consequences of default, including collection efforts and harm to credit, leading to difficulty finding housing and employment. The result is a downward spiral: instead of helping students better their lives, bad educational programs and bad student loans make it ever harder for students to find employment or even survive.

1. Staying Current by Going Without

There is very little empirical research on how borrowers stay current. The information below is based mainly on our experiences with clients and on information from borrowers contacting us through our web site.

Most of our clients seek assistance after struggling for years to stay current on both federal and private loans. Most have had to cut back on all but the most essential expenses in order to try to pay private student loans.

For example, we had a client last year with significant private loan debt. A citizen immigrant from South America, he did not have parents or other relatives in this country to help counsel him when he applied to college to study to become an airline pilot. He ended up with only a few federal loans and substantial private loans. Although he ultimately completed school, he was unable to find employment as an airline pilot. His work as an administrative assistant at an airline company pays barely more than minimum wage. This client was unable to even rent his own apartment, instead sleeping at various friends' houses. He borrowed clothes and other items from friends.

Another borrower who contacted us through our website reported that he was current on his student loan payments, but after paying those and his rent, he had only $80 left each month for other expenses. These examples are unfortunately typical of many of our clients.

A recent report by the Institute on Assets and Social Policy illustrates not only how burdensome student loan debt lowers borrowers' ability to make purchases, but also how it impedes asset building for the future. This inability to save for the future and for future generations fuels the growing wealth inequality in our country, ultimately harming individual and family well-being and blocking economic growth.[45] This problem affects everyone, but is particularly destructive for low-income communities and certain communities of color.

2. Confusion and Efforts to Prioritize Debts

The confusion about the type of loan a borrower has and the difference in repayment options leads many private loan borrowers to prioritize these payments over federal loans even though the consequences of federal student loan default are much more severe and there are flexible options available for most federal loan borrowers.

We have counseled many clients who had stopped paying federal loans, but were still making payments on private loans. In most cases, we are able to help those borrowers obtain affordable repayment plans for their federal loans. However, this can be a complicated process if the borrower has already defaulted on federal loans and significant damage has already occurred.

We find that private loan collection efforts are very aggressive. As one borrower told us:

> AES [American Education Services] calls me between 5-30 times A DAY requesting a payment that I told them I cannot afford, they refuse to work with me on lowering my payments to an affordable or manageable amount… Further, the amount owed after interest is now nearly three times the amount I borrowed and growing everyday!

Private loan collectors also often exploit borrower confusion. It is particularly common for collectors of private student loans to claim that they can use collection tools unique to federal loans, such as Social Security offsets.[46] Borrowers may feel compelled to pay more to a private loan collector in these cases even though it is only the federal government that has the most extreme collection powers.

3. Severe Negative Consequences of Default

Credit Reporting

Though many have noted the relationship of student loan debt to inability to qualify for a mortgage,[47] the credit reporting implications of student loan debt, especially for low-income

[45] Thomas Shapiro, Tatjana Meschede, Sam Osoro, The Roots of the Widening Racial Wealth Gap: Explaining the Black-White Economic Divide (The Institute on Assets and Social Policy, February 2013).
[46] *See, e.g.*, *Strom v. National Enterprise Systems, Inc.*, 2011 WL 1233118 (W.D.N.Y. March 30, 2011) (alleging that collector of private student loan advised that it would seize plaintiff's SSDI funds in bank account).
[47] *See, e.g.*, Janet Lorin, *Rising Student-Loan Delinquencies Hurt Young Homebuyers*, Bloomberg (Feb. 28, 2013), http://www.bloomberg.com/news/2013-02-28/rising-student-loan-delinquencies-hurt-young-homebuyers.html; Jen Mishory and Rory O'Sullivan, Denied? The Impact of Student Debt on the Ability to Buy a House (Young

borrowers, is much broader. Credit reports are currently used for many purposes beyond basic lending, such as employment, housing, and insurance.

Unaffordable private student loans may place borrowers in a "Catch-22" where delinquency on their private loans prevents them from obtaining jobs necessary to afford the payments. Nearly half of all employers do credit checks on some or all of their employees when hiring.[48] A recent study by Demos found that these positions were not limited to high management positions, but also to "jobs as diverse as doing maintenance work, offering telephone tech support, assisting in an office, working as a delivery driver, selling insurance, laboring as a home care aide, supervising a stockroom and serving frozen yogurt."[49]

Additionally, poor credit can affect a consumer's ability to secure affordable housing. All three of the major credit bureaus offer products targeted specifically at residential landlords. If they are willing to rent to someone with a negative credit history, many landlords will require an additional security deposit – making housing more unaffordable. However, many landlords are simply not willing to rent to someone with a negative credit history. The use of credit reports is not limited to market rate housing. In fact, many public housing authorities also run credit checks on its housing applicants.

Finally, both the delinquency on the credit report and a high debt amount will likely make insurance premiums, especially car insurance, more expensive. Most automobile insurance companies use credit reports to generate an insurance score that determines a consumer's rates. In fact, Progressive Insurance's website explicitly states that past-due payments will result in higher rates for its customers.[50] A safe and reliable car is essential to the success of most working families. Childcare, jobs, groceries, medical appointments, and so many other everyday tasks are often out of reach for families without a car. Therefore, it is essential that consumers are able to afford their car insurance.

These difficulties are illustrated by the experience of one of our clients. Pat owes approximately $90,000 in student loans, half of which is private loans to three different private lenders. Pat has developmental disabilities and currently works full time as a waitress. She is currently on the income-based repayment plan for her federal loans, and has worked out a payment arrangement with two of her three private lenders. Unfortunately, her third lender refused to accept any amount less than the full monthly payment of $200 – which she cannot afford. Because the lender refused to work out a payment arrangement with Pat, she is now three years past due on this account.

Pat has a long credit history. Though not perfect, the biggest drag on her credit score is this past due private loan. Her other accounts are currently in good standing and helping her build a positive credit history. Unfortunately, because she cannot get up to date on this one

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Invincibles 2012), http://younginvincibles.org/wp-content/uploads/2012/08/Denied-The-Impact-of-Student-Debt-on-the-Ability-to-Buy-a-House-8.14.12.pdf.

[48] Society for Human Resources Management, SHRM Survey Findings: Background Checking – The Use of Credit Background Checks in Hiring Decisions (July 19, 2012).

[49] Amy Traub, Demos, Discredited: How Employment Checks Keep Qualified Workers Out of a Job (Feb. 2013).

[50] Progressive, Insurance Scores: What You Should Know, http://www.progressive.com/shop/car-insurance-credit-scores.aspx.

private loan, it will continue to report a past due balance until it is obsolete. Furthermore, although this lender sends Pat one bill with one monthly payment, because she took out the loan in 3 separate disbursements, it is reported on her credit reports as three separate past due accounts.

Six months ago, Pat was in a car accident and her car was totaled. She needed to buy a used car on credit in order to get to work. Due to her bad credit score, the best interest rate that she could get on a car loan was 19.7 percent. Over the life of her loan, Pat will pay thousands more dollars for her car, due in large part to the refusal of the private student lender to offer her an affordable payment plan.

Collection Abuses

One reason loan holders have little incentive to modify the terms of private student loans for financially distressed borrowers is the ease with which such holders can obtain default judgments without showing that they actually own and have a right to collect on the loans. Because many of the private student loans that were made prior to 2008 are reaching the end of their statute of limitations periods, we are seeing increasing numbers of collection actions filed against borrowers all over the country. We have noticed a disturbing trend in these cases, very similar to the "robo-signing" scandal in foreclosure actions, based on reports from legal services attorneys who are defending these actions on behalf of low-income and financially distressed borrowers. Like a plaintiff in a foreclosure action, the plaintiff in a private student loan action should prove that it is the real party in interest and has a right to collect on the loan by documenting an unbroken chain of assignment from the original creditor to itself.[51]

In these cases many private loan plaintiffs – who are usually securitization trusts, insurance companies who have guaranteed the loans, or entities that have acquired the loans after multiple transfers – have been unable to provide such documentation. The plaintiffs typically rely upon the promissory note, which only documents an agreement between the original lender and the borrower, and one or more documents (which often appear to be downloaded from the SEC's publicly available EDGAR database) that purport to show the transfer of the promissory note between a few parties involved in the chain of ownership. The transfer documents, however, are deficient in a number of ways – some do not identify the individual student loan promissory notes being transferred, others do not reflect any transfer to the plaintiff or between intermediary parties, and there are questions about whether the employees who sign the affidavits to support the collection actions have any personal knowledge about these documents.

While we are concerned about this practice whenever it occurs, we are especially concerned about borrowers who do not contest the actions because they do not know where to go for help or are not able to find an attorney they can afford. In such cases, courts have entered default judgments without ensuring that the plaintiff actually owns and has the right to collect on the debt. Once it obtains a judgment, the plaintiff will have the right to, among other things, garnish wages and seize non-exempt residential property that is essential to the economic well-being of the borrower and her family. If private student loan holders are able to obtain easy

[51] *See, e.g.*, *United States v. Elliott,* 2006 WL 3759857 (N.D. Tex. Dec. 19, 2006); *Educap v. Smith*, 362 S.W.3d 451 (Mo. Ct. App. 2012); *Student Loan Mktg. Ass'n v. Holloway*, 25 S.W.3d 699, 704 (Mo. Ct. App. 2000).

default judgments without showing actual ownership, there is little incentive for them to modify loans and work with the most financially distressed borrowers.

IV. Current Options for Borrowers with Hardship

The agency asked what options currently exist for borrowers to permanently or temporarily lower their payments on private student loans. Unfortunately, although individual borrowers are sometimes able to negotiate temporary payment relief, voluntary efforts by lenders are not widespread or transparent. Furthermore, student loan creditors have pushed hard to limit the safety net for borrowers who get in trouble. One of the most notable examples is the 2005 Congressional decision to make private student loans as difficult to discharge in bankruptcy as federal loans. Borrowers trying to manage unaffordable PSL payments face a number of barriers.

Lack of Long-Term Repayment Relief

The bankruptcy policy might not be so harsh if borrowers had ample non-bankruptcy alternatives to address student loan problems. In NCLC's experience representing borrowers through the Student Loan Borrower Assistance Project, we have found private lenders to be inflexible in granting long-term repayment relief for borrowers. Lenders that had no problem saying "yes" to risky loans have no problem saying "no" when these borrowers need help. The CFPB likewise found that the lenders in its sample did not currently offer loan modification programs.[52]

Most of our clients simply cannot pay the onerous lump sums or monthly payments that the lenders demand. This is despite the fact that in some cases, our clients have borrowed money from friends and family and offered as much as 25-35% of their balances as settlement. We do not understand why a creditor would reject substantial funds from a low-income consumer, particularly since the creditor is unlikely to recover much if anything from these consumers.[53]

Based on discussions with other advocates and our experiences trying to get relief for our clients, we know that lenders will offer settlements in some cases. However, the lenders generally require very large lump sums to settle debts even from borrowers with low incomes. Most lenders will not even consider an offer that is less than 70% of current principal and interest balance, but this varies considerably by lender.

Most lenders will not even discuss settlement or modification until the loan is in default or written off. At this point, the borrowers' main point of contact is usually a collection agency. Interestingly, the collection agencies working on behalf of the lenders will often settle for smaller amounts than the originating lenders. Many collectors agree to these settlements without requiring financial documentation. In general, most will offer more favorable settlements to borrowers who have been in default for longer periods of time.

[52] CFPB: Private Student Loans Report, 66.
[53] In some cases, we hear from servicers that they do not have the authority to accept a settlement offer.

It may seem to make business sense for the lenders to wait until a borrower defaults to allow settlements, but this is hardly in the best interests of borrowers. It may also not be in the best interests of investors. With respect to borrowers, a default negatively impacts the borrower's credit score and subjects a borrower to collection.[54] Yet we find that few lenders offer work-outs, modifications, or other programs to help borrowers who are struggling while staying current on their loans.

Even in cases of severe distress, the creditors we have contacted have offered no more than short-term interest-only repayment plans or forbearances. Short-term interest-only payment options in most cases only prolong inevitable defaults, particularly for borrowers with large loan balances. In a recent article, for example, Sallie Mae described options available to private loan borrowers as reduced payment plans, lower rates or extended terms and temporary suspension of payments. The company did not even mention principal reduction and did not specify the specific criteria to qualify for the various options.[55]

This experience holds true for both for-profit and non-profit lenders although some non-profit lenders claim to offer more flexible options. Even those non-profit lenders that offer relief, however, rarely describe options in loan agreement, web sites, or other descriptive materials. A borrower generally must know to ask for particular programs. However, there are some lenders, particularly non-profit lenders, that proactively reach out to delinquent borrowers. We urge the CFPB to make sure it has whatever information is available about these programs and their effectiveness.

Uncertainty as to the Availability of Death or Disability Discharges

Some private student lenders offer cancellation programs, generally for death of an obligor or disability. The federal student loan programs provide death and disability cancellations. Similar programs are only available at lender discretion for private loans.

Sallie Mae announced in 2010 that it had hired a company to administer claims for a new total and permanent disability provision for private education loans.[56] This program, however, does not necessarily apply to all of the company's private loan products. Wells Fargo announced a similar program in December 2010, stating that it would require verbal or written notification of a student's death or permanent and total disability followed by receipt of acceptable documentation. The forgiveness, according to Wells Fargo, covers the death or disability of the student, leading to forgiveness of not only the student's obligation, but also the obligation(s) of

[54] *See* Section III. B. 3, above.
[55] Janet Lorin, *Students Pay SLM 9.25% on Exploitive Loans for College*, Bloomberg (June 5, 2012), http://www.bloomberg.com/news/2012-06-05/students-pay-slm-9-25-on-exploitive-loans-for-college.html.
[56] *See* Securian Company News Release, Securian Wins Contract for Administering Total and Permanent Disability Claims on Private Student Loans (March 8, 2010), http://www.reuters.com/article/2010/03/08/idUS190074+08-Mar-2010+PRN20100308.

any co-signers.[57] Discover also announced a cancellation program due to death or permanent disability.[58]

We have found that the lenders that do have these programs have different standards in some cases within the same company. Some lenders will automatically allow a private loan discharge if the borrower obtained a federal disability discharge. They will also in some cases use the criteria for federal loan discharges. In other cases, the lenders use criteria that are completely different than the federal programs. The Sallie Mae private loan disability discharge application, for example, requires the borrower to answer different questions and meet different standards than the federal program and requires separate certification from a physician.

The companies to date have not provided public information about eligibility and application requirements. We do not know of any investigation as to whether these programs are described in writing in loan agreements or elsewhere and whether the lenders are following up on their promises.

Refusal to Offer School-Related Cancellations

Under the Higher Education Act, borrowers are able to discharge federal loans if the borrower was unable to complete the program due to the school's closure[59] or if their eligibility to borrow was falsely certified by the school.[60] These administrative discharges are critical, but provide relief for only a small fraction of borrowers. Borrowers may also be able to raise other claims against the school as defenses to payment.[61]

The right to assert defenses to repayment of the loan when the school fails to deliver on its promises is especially important when private lenders have close ties to for-profit schools that promote, package or help the lender market their private loan products. In these cases, borrowers are often limited in the relief directly available from schools, many of which are out of business or insolvent by the time borrowers seek redress. Even borrowers who successfully obtain damages from an unscrupulous school are often left with significant loan debt.

There is a strong argument that claims against the schools can be raised against private student lenders, either because the lenders have close relationships with the school, because of the FTC Holder Rule or other assignee liability arguments.[62] However, private student lenders have sought numerous ways to avoid this type of liability, including hiding behind preemption

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[57] *See* Wells Fargo, News Release, Wells Fargo Enhances Student Loan Products to Include Loan Forgiveness (Dec. 17, 2010), https://www.wellsfargo.com/press/2010/20101217_EFS.
[58] *See* https://www.discover.com/student-loans/schools/student-loan-products.html?gcmpgn=0809_ZZ_srch_gsan_txt_2&srchQ=permanent%20disability%20death&srchS=internet_cm_corp&srchC=internet_cm_fe&srchP=0.
[59] 20 U.S.C. § 1087(c)(1).
[60] *Id*.
[61] *See* National Consumer Law Center, Student Loan Law § 12.7 (4th ed. 2010 and Supp.)
[62] *See* National Consumer Law Center, Student Loan Law § 11.9 (4th ed. 2010 and Supp.). Under the FTC holder provision (more accurately referred to as the Federal Trade Commission Preservation of Claims Rule), students who have claims or defenses that they could have raised against the school can raise them against the lender. The lender's liability is capped; at most the student can recover any payments made and have the remaining indebtedness canceled.

arguments. Many fail to include the holder notice in the loan notes. Nearly 40% of the loans in NCLC's 2008 survey followed this potentially illegal approach.[63] Other lenders include the notice but attempt to deny borrowers its benefits by placing contradictory clauses in the notes. In our survey, 90% of the notes that included the FTC notice undermined it in some way by attempting to prohibit borrowers from raising defenses.

In light of their general practice of denying any legal responsibility for school closure or misconduct, it is no surprise that private student lenders appear also to be unwilling to provide voluntary loan workouts for borrowers that experience these problems.

An example of a typical response can be seen in letters from Chase and AES, the lender and servicer of the private student loan for one of our clients. According to AES, "We are unable to cancel the debt incurred. Pursuant to Section L. Additional Agreements of the Credit Agreement, it states, 'If I fail to complete the education program paid for with this loan, I am not relieved of any obligation within or pursuant to this Application/Promissory Note.' Your client may wish to seek resolution from the school itself.'" When we contacted Chase about this client, Chase wrote back stating that we should contact the school regarding any practices in regards to their education. According to Chase's letter, "We are only a lender and servicer. Funds are disbursed upon the school's certification. Once certified, we have no further correspondence with the school."

Refusal to Negotiate or Denial of Authority

Borrowers are often told by loan servicers that the servicer does not have the authority to accept a settlement offer.[64] In the mortgage context, servicers sometimes claim that pooling and servicing agreements constrain their ability to modify loans, although in reality, most securitization documents give broad authority to servicers to service loans in accordance with customary standards, often also stating that the servicers must act in the best interests of investors.[65] In any case, we have not heard creditors or servicers use this excuse in the student loan context. In fact, Sallie Mae and VSAC assert that loan servicing is the same whether the loans are securitized or not.[66] NCLC has reviewed pooling and servicing agreements from several private student lenders and did not find any explicit barriers to modifications in any of those agreements. Most of the agreements are explicit that servicers <u>can</u> reschedule, revise, defer

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[63] NCLC: Paying the Price.

[64] *See*, *e.g.*, Janet Lorin, *Students Pay SLM 9.25% on Exploitive Loans for College*, Bloomberg (June 5, 2012), http://www.bloomberg.com/news/2012-06-05/students-pay-slm-9-25-on-exploitive-loans-for-college.html (describing Chase's refusal to negotiate with a PSL borrower, despite public statement by spokesperson that "[w]e continue to encourage customers to contact us if they have questions about paying back their loans,")

[65] Testimony of Stephen S. Kudenholdt, U.S. House of Representative, Committee on Oversight and Government Reform, Domestic Policy Subcommittee, "Is Treasury Using Bailout Funds to Increase Foreclosure Prevention as Congress Intended" (Nov. 14, 2008).

[66] *See* National Consumer Law Center, Too Small to Help (April 2009), *available at* http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/TooSmalltoHelp.pdf.

or otherwise compromise payments due on any student loan, as long as the servicer uses the same standards it uses for its own loans.[67]

Lender Evaluation of Borrower Qualifications is Not Transparent

The agency asked how lenders evaluate borrowers for affordable repayment options and whether lenders work directly with co-signers to modify loan terms. In general, lenders do not share their criteria for evaluating borrower requests for assistance. Therefore, we have very little information regarding these questions, limited to the experiences of our clients or those of other advocates. As one borrower with loans from graduate school told us:

> I wish Sallie Mae would provide realistic payment options. I asked for assistance prior to the account becoming past due… Every time I speak with a representative, they have a new payment option… The representatives tell me that repayment options change on a daily basis – *a daily basis*! This does not make sense as my paycheck does not change on a daily basis.

We have not been able to obtain copies of lender standards for evaluating borrowers for loan workouts, but a number of lenders and servicers have told or us or other advocates that they have standard criteria for settlements. In general, we have found that the longer the loan has been in default, the lower the lump sum required. There may be typical criteria or even standardized criteria, but we have no knowledge of this.

We have not had cases in which lenders negotiate directly with co-signers, but we have heard from other advocates that they are able at times to negotiate releases of co-signer obligations. The lenders vary considerably in requirements. They will often accept a lower lump sum because they can still pursue collection from the co-obligor that remains on the loan. As with the settlements discussed above, most lenders will only consider co-signer settlements or "buy-outs" if the loan is in default. Some lenders will also release co-signers when the loans are current, but we have not had direct experience with this.

V. Options for Addressing Unaffordability and Default

The agency asked for examples of loan modification programs and asked about features of those programs that might be applicable to a student loan affordability program. The comments below are structured as a discussion of the potential trade-offs of different approaches, rather than as a recommendation of one particular model. However, <u>any proposed modification program, no matter how it is structured, should meet certain essential criteria to ensure it helps the borrowers most in need of assistance</u>. These essential elements and borrower protections are discussed in Section V.A, below. We urge the CFPB to evaluate any proposed loan modification program to determine whether it will – at a minimum – satisfy these five essential criteria.

<u>Given rising default rates and borrower distress, providing relief for borrowers is essential</u>. We urge the CFPB to gather any additional necessary information about industry practices and incentives and about the characteristics of borrowers in distress as quickly as

[67] *Id*.

possible so that it can choose the most appropriate of the available policy options and implement it without delay.

The Request for Information focuses on options for creating a loan modification program, as do these comments. However, <u>loan modifications, while important, should be combined with other policies to provide relief to borrowers and prevent defaults in the future</u>. These policies include:

- Restoring bankruptcy rights for all student loan borrowers;
- Mitigating the impact of negative credit reporting on borrowers' ability to access housing, employment opportunities and other basic needs;
- Eliminating predatory student lending, including development of sound underwriting standards ensuring ability to pay;
- Including provisions for flexible repayment and death and disability discharges in new originations;
- Improving the availability and accuracy of information provided to students before they borrow; and
- Vigorously enforcing federal and state laws to protect borrowers from origination and collection abuses and for-profit school abuses.

A. Essential Program Features and Borrower Protections

In evaluating proposals for PSL modification programs, the agency should evaluate whether the proposal will – at a minimum – satisfy the following essential criteria.

1. **Affordability**: Loan modifications must provide a real financial benefit to borrowers and must be linked to the borrower's realistic ability to repay. This is essential not only to providing real relief to borrowers in distress, but also to prevent high re-default rates which would make the program not worth the expense from the servicers' and investors' perspective.

2. **Preservation of Borrower Protections**: Participation in a loan modification program or acceptance of a loan modification offer should not result in a borrower losing any rights or protections she would otherwise have. This includes forbidding any waivers of rights as a condition of modification and also structuring the program in such a way that previously exempt income or assets of the borrower are not placed at risk (for example, through the expanded collection powers available for federal loans) and time limits for collection are not lengthened beyond previously applicable statutes of limitations.

3. **Enforceability**: Borrowers must have the ability to enforce their rights under the modification program, including the ability to dispute and appeal denials of eligibility and mistakes in the terms offered and to raise claims and defenses related to the program in legal proceedings.

4. **Efficiency and Scale**: The program must be designed to reach as many as possible of the borrowers in or at risk of default, both in order to assist those borrowers directly and in order to have a positive impact on the broader economy. Eligibility criteria must be broad enough to

encompass all borrowers in need of assistance and the program must be efficient in reaching those borrowers and in minimizing the barriers to uptake. Reaching scale will require either mandating loan modification offers or providing effective incentives sufficient to induce servicers and lenders to modify a large number of eligible loans.

5. **Fairness**: Any program, particularly one that relies on incentives to servicers or on purchase of loans from existing servicers and lenders must not be a bailout or giveaway to lenders. This is essential to avoid moral hazard on the part of lenders and servicers. The industry should not be allowed to externalize the costs of the shortsighted lending decisions it made, particularly between 2005 and 2008. Furthermore, the program must be structured to prevent servicers and lenders from "creaming" or selecting particular loans for modification in order to maximize their own finances and from receiving credit or incentive payments for modifications or other actions they would have taken anyway. Finally, the program must have protections to prevent a disparate impact on borrowers of color or other protected groups.

B. Loan Modification Policy Options and Examples

PSL lending in the years leading to the financial crisis bears many similarities to subprime mortgage lending in the same period and has produced similar results. Accordingly, the various efforts to modify large numbers of home mortgages provide a source for potential program designs and some indication of what the advantages or pitfalls of particular policy decisions might be. These policy decisions include whether to structure the program as a mandate, incentive or purchase program; determining which loans or borrowers are eligible for assistance; and setting the terms of the loan modifications themselves.

While the CFPB will be in a better position to evaluate these options once it reviews the information submitted in response to this request for comments and gathers any additional information that is necessary, some options appear more promising than others, and more likely to satisfy the five essential criteria for a loan modification program. Mandating loan modifications or purchasing loans out of existing pools is more likely to reach large numbers of eligible borrowers than relying on incentives. Automatically offering modifications to eligible borrowers, rather than requiring borrowers to apply, is also likely to improve the reach of the program to the borrowers who are most in need of assistance. Because student loans are generally smaller than home mortgages, it may be necessary to strictly limit the administrative costs of evaluating borrowers for and implementing modifications in order to make the program cost-effective. Some ways of doing this include determining eligibility based on features of the loan or school attended, rather than on the borrower's current financial circumstances, taking advantage of information gathered in applications for IBR, ICR and other aid programs, and setting uniform terms for modifications (although the last will reduce affordability for some borrowers).

There are also non-modification options that could assist borrowers in addition to any loan modification program, outlined in section V. D, below.

1. Mandates, Incentives or Purchase of Loans

There are three basic models for creating a PSL loan modification program. 1) Mandate modification of certain loans by the existing lenders or servicers; 2) pay incentives to the existing lenders or servicers for loan modifications; or 3) purchase loans at a discount from the existing owners and then modify them. Examples or hybrids of all three approaches can be found in the mortgage market, and each has advantages and potential pitfalls.

Mandates

Mandates to modify loans are generally found in the context of settlements of enforcement actions by federal or state regulators. Examples include the National Mortgage Settlement[68] and the Massachusetts Attorney General's settlements with Fremont, Option One and other predatory lenders.[69] HAMP (the Home Affordable Modification Program) also includes a partial mandate in addition to incentives, since once a servicer agrees to participate, it must consider all eligible borrowers for loan modifications and offer modifications to all borrowers who satisfy the program requirements.[70] All other things being equal, a mandate should result in the maximum number of eligible borrowers receiving assistance at the least cost to taxpayers.

However, a mandate is only effective if it is adequately enforced. HAMP has reached only a fraction of eligible borrowers because of servicer non-compliance, the U.S. Treasury's failure to enforce the rules, and barriers to private enforcement by homeowners.[71]

Another limit to the HAMP 'mandate' is that it does not override restrictions on loan modifications in the contracts between investors and servicers. Thus, servicers are only required to modify loans if the investor permits it.[72] It is not clear to what extent there are similar contractual barriers to loan modification in the PSL industry. In any case, a loan modification program should require servicers to provide documentation in any instance where investor restrictions are asserted as a barrier to modifications.

[68] The settlement requires servicers to provide up to $17 billion in principal reductions and other loan modification relief. *See* settlement documents available at http://www.nationalmortgagesettlement.com.
[69] *See* press release and supporting documents available at http://www.mass.gov/ago/news-and-updates/press-releases/2009/ag-coakley-reaches-10m-settlement-with.html.
[70] U.S. Dep't of the Treasury, MHA Handbook v4.1, *Making Home Affordable Program: Handbook for Servicers of Non-GSE Mortgages* (Dec. 13, 2012) [hereinafter "MHA Handbook"], at ch. II § 2.2, *available at* https://www.hmpadmin.com/portal/programs/docs/hamp_servicer/mhahandbook_41.pdf ("Servicers must pre-screen all first lien mortgage loans where two or more payments are due and unpaid to determine if they meet…basic criteria for consideration under HAMP").
[71] National Consumer Law Center, At a Crossroads: Lessons from the Home Affordable Modification Program (HAMP), 26 – 40 (January 2013) [hereinafter "NCLC: At a Crossroads"], *available at* http://www.nclc.org/issues/at-a-crossroads.html; *See also* Paul Kiel, *Secret Documents Show Weak Oversight of Key Foreclosure Program,* Pro Publica (Nov. 8, 2012), http://www.propublica.org/article/secret-documents-show-weak-oversight-of-key-foreclosure-program; Paul Kiel, *Secret Docs Show Foreclosure Watchdog Doesn't Bark or Bite*, ProPublica, Oct. 4, 2011, http://www.propublica.org/article/secret-docs-on-foreclosure-watchdog/single.
[72] NCLC: At a Crossroads, 32.

A third potential difficulty is that, since participants in the PSL industry are not all subject to supervision by the same agency, it may be challenging to craft or enforce a mandate that reaches all the relevant entities or loans. This has been another weakness of HAMP; different rules (and sometimes no rules at all) apply depending on which servicer is servicing the mortgage and whether the loan is insured or guaranteed by a GSE or other government program. This has led to a complicated patchwork that is difficult for borrowers to navigate and probably more expensive for servicers to implement.[73] The National Mortgage Settlement simply relies on existing loan modification standards, and so does not create a uniform mandate.[74] The Massachusetts Attorney General negotiated settlements with individual lenders, based on the specific practices of each lender.[75] Enforcement actions against individual lenders or schools, with the goal of reaching a settlement mandating loan forgiveness or modifications, might be an appropriate way to direct assistance to borrowers who were harmed by abusive school operators or subjected to unfair or deceptive marketing by lenders.

Incentives

The largest example of a modification program based on offering incentives to lenders and servicers is HAMP. Under HAMP, participating servicers receive a payment of up to $1,600 for each permanent loan modification they complete according to program rules.[76] Investors also receive compensation for reducing borrowers' principal (up to $0.63 for each dollar of principal forgiven), reducing the interest rate, or accepting a short sale or deed in lieu of foreclosure.[77] As of December 31, 2012, Treasury has paid out approximately $1.4 billion in incentives to servicers and $2.2 billion in incentives to investors, as well as expending funds to administer the program. As of the same date, there were 417,419 active permanent first-lien modifications under the TARP-funded portion of HAMP, 68,921 active permanently modified second liens and 80,178 short sales and deeds-in-lieu.[78] Borrowers have received principal reductions totaling approximately $9.2 billion and see monthly payment reductions averaging about $550.[79] However, HAMP has reached only a fraction of the 4 million borrowers originally projected, despite being extended for an additional year.[80]

While incentives have been moderately successful in the mortgage context, it may be challenging to price servicer incentives high enough to encourage modification of PSLs while still producing a net benefit to taxpayers. PSL balances are much lower than mortgage balances (so the savings to borrowers will necessarily be lower), yet the administrative costs to servicers

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[73] NCLC: At a Crossroads, 9-10.
[74] *See* www.nationalmortgagesettlement.com, particularly the document entitled "Servicing Standards Highlights" (https://d9klfgibkcquc.cloudfront.net/Servicing%20Standards%20Highlights.pdf).
[75] *See* press release and supporting documents available at http://www.mass.gov/ago/news-and-updates/press-releases/2009/ag-coakley-reaches-10m-settlement-with.html.
[76] MHA Handbook ch.II, 13.1.1.
[77] MHA Handbook ch.II, 13.3.4.
[78] *See* Special Inspector Gen. for the Troubled Asset Relief Program, Quarterly Report to Congress: Jan. 30, 2013, 52-53 (2012), *available at* http://www.sigtarp.gov/Quarterly%20Reports/January_30_2013_Report_to_Congress.pdf.
[79] *See* U.S. Dep't of the Treasury, Making Home Affordable: Program Performance Report Through January 2013, 25 (2013) *available at* http://www.treasury.gov/initiatives/financial-stability/reports/Documents/January%202013%20MHA%20Report%20Final.pdf.
[80] NCLC: At a Crossroads.

of contacting borrowers, collecting current financial information and modifying servicing platforms may be similar.

Purchase of Loans

Several proposals have been made that involve purchasing distressed PSLs from the existing investors and either placing them in a new pool, where they can be modified, or "swapping" the borrowers into government loans with less onerous repayment terms.[81] The FDIC's modification of IndyMac mortgages is a useful recent point of reference, although it was a result of receivership of a failed institution, rather than purchase of particular loans. The advantage of the FDIC program or a purchase program is that it eliminates any investor restrictions on modification (such as limits in the pooling and servicing agreements) and theoretically solves the problem of different investor tranches having conflicting incentives with regard to modifications; once a price has been agreed, the new owner has a clean slate to modify the loan. Moreover, more consumers receive the modifications for which they are eligible.

If a purchase program is created or subsidized by the federal government, care should be taken that it satisfies the criteria of Affordability, Preservation of Borrower Protections and Fairness, discussed above. In terms of Affordability and Fairness, loans should be purchased at a discount sufficient to ensure that the original lenders are not receiving a windfall from taxpayers and that the loan payments can be reduced enough to be truly affordable to the borrower. Some private student loans in default have already been sold to debt collection companies. In our experience assisting individual clients, we find that collection agencies are willing to settle for smaller amounts than originating lenders, and will offer more favorable settlements to borrowers who have been in default for longer periods of time. The CFPB should collect information on the extent to which lenders sell distressed PSLs, and the prices they are willing to accept for them.

Any proposal to swap PSLs for government loans should be structured to ensure that borrowers would not become subject to the more draconian collection powers generally available for federal loans; for example, a borrower unable to pay a federal loan can face the loss of tax refunds and public benefits—even Social Security—that are protected from collection by private lenders. At the very least, borrowers should receive full information about potential consequences and have the option to decline to participate in such a swap.

2. Loan Selection and Borrower Eligibility

A second essential question for designing a PSL modification program is to decide which loans or borrowers will be the target of the program, and how participation will be structured. Options (which may be combined) include 1) targeting borrowers based on financial hardship; 2) targeting certain loans based on features such as high interest rates or questionable underwriting practices; or 3) directing relief to borrowers who attended schools that engaged in deceptive marketing or other abusive practices. If the program is aimed at particular loans or schools, eligibility may be limited to borrowers who are already experiencing payment difficulties or could be extended to all borrowers with loans that fit the program criteria. Finally, the program

[81] *See*, *e.g.* Private Student Loan Debt Swap Act of 2009, S.1541, 111th Cong. (2009).

could be structured to require borrowers to apply for assistance, or it could be structured so that all eligible borrowers are identified based on servicer or lender records and receive a modification offer.

Again, examples or hybrids of these approaches can be found in the mortgage market, and each has advantages and potential pitfalls.

Borrower Eligibility and Application Requirements

HAMP uses a combination of loan-based and borrower-based eligibility requirements. For example, loans must have been originated before January 1, 2009, must have an unpaid principal balance below a certain cap and must be a first-lien loan secured by the borrower's primary residence.[82] At the same time, the *borrower* must satisfy certain criteria, including being in default or at imminent risk of default and having a current monthly payment greater than 31% of current gross monthly income.[83] HAMP also requires borrowers to complete a lengthy and complicated application process in order to receive a modification.[84]

Two of the greatest disappointments of HAMP have been its failure to reach large numbers of apparently eligible borrowers and the very high numbers of borrowers who start the application process but are denied due to missing documentation. As of October, 2012, 4.35 *million* borrowers had started the application process for HAMP, but only 1.9 million reached the next stage (starting a trial modification).[85] The single largest category of HAMP denials is "failure to submit documents," which is often the result of servicer mishandling of documents, rather than borrower failure to submit.[86] Whether the fault of borrowers or servicers, fewer modifications have been achieved in part because the application process is complicated and document-intensive and the financial incentives have not resulted in servicers improving their handling of applications.[87]

Another emerging problem with HAMP appears to be access for non-English speaking borrowers.[88] Any program that relies on borrower outreach or requires borrowers to respond to requests for information must be made accessible to non-English speakers.

[82] MHA Handbook ch.II, 1.1. HAMP Tier 2, which was introduced in 2012, allows modifications on rental properties. *Id.*
[83] *Id*.
[84] MHA Handbook ch.II, 4.1 – 5.7. HAMP requires servicers to conduct outreach to all eligible borrowers, but the borrower must still respond to the outreach and provide extensive documentation of hardship and current income in order to qualify. MHA Handbook ch.II, 2.1.
[85] NCLC: At a Crossroads, 26.
[86] *Id.* at 31.
[87] The Fremont settlement, discussed below, while providing automatic temporary protection from foreclosure for large numbers of borrowers, still required borrowers to respond to outreach efforts and provide documentation to receive a loan workout, and uptake of the program was not very high.
[88] Cal. Reinvestment Coalition, Race to the Bottom: An Analysis of HAMP Loan Modification Outcomes by Race and Ethnicity for California 2-3, 27 (2011), http://www.calreinvest.org/ publications/crc-reports; Nat'l. Cmty. Reinvestment Coal., HAMP: Mortgage Modification Survey 2010 3 (2010), *available at* http://www.ncrc.org/images/stories/mediaCenter_reports/ hamp_report_2010.pdf.

As discussed above, because the loan amounts are lower in the PSL context than in the mortgage market, the administrative costs of determining borrower eligibility (both for borrowers and servicers) will be higher relative to the amount of payment relief and may be cost-prohibitive. One way of reducing these costs would be to piggyback the eligibility determination on the documentation process for IBR, ICR or receipt of public benefits, so that borrowers do not have to go through more than one income-documentation process. In other words, private lenders could be required to provide loan modifications for borrowers who qualify for IBR or ICR (or perhaps for need-based programs outside the student loan context) and to use the same documentation of income and expenses.

Another option, as discussed below, is to avoid basing eligibility on the borrower's current financial circumstances, and instead base it on features of the loan or school attended. This would not necessarily mark a departure from current practice; in our experience working with individual clients, we have found that many debt collectors will agree to settlements without requiring financial documentation from borrowers, particularly where borrowers have been in default for long periods of time.

Loan-Based Eligibility

The Massachusetts Attorney General's agreement with Fremont focused on loan features at origination. Fremont was forbidden from foreclosing on loans with a combination of features including teaser rates, high debt-to-income ratios and prepayment penalties unless it first took steps to work out the loan *and* received the approval of the court or Attorney General's office.[89] This was a clear, bright-line rule which provided automatic protection to thousands of borrowers. This approach was justified because a court found such loans to be "presumptively unfair."[90]

Certain features of PSLs, particularly those made during the years leading up to the crisis, might justify automatic borrower protections. For example, a large number of loans were made "Direct to Consumer," rather than through the school channel. Especially when combined with a loan balance that is higher than the cost of attendance, such a loan is completely unlinked from the borrower's likely future income and ability to repay and was probably made in order to meet secondary market demand rather than to meet the credit needs of the individual student. PSLs also frequently have higher interest rates than federal loans – when such loans are made to borrowers who have not exhausted their federal loan eligibility, there may be a presumption of unfairness that justifies requiring modification.

[89] *Com. v. Fremont Inv. & Loan*, 452 Mass. 733 (2008) (where mortgage loan terms include four identified factors, they are "presumptively unfair" and Fremont must explore alternatives to foreclosure and seek court approval for proceeding with the foreclosure).

[90] The four characteristics that render the Fremont loans presumptively unfair are: (1) the loans are ARMs with an introductory period of three years or less; (2) the loans have an introductory or "teaser" rate 3 percentage points lower than the fully indexed rate; (3) the borrowers have a debt-to-income ratio that would have exceed 50 percent if the lender had measured the debt by the fully indexed rate, not the teaser rate; and (4) the LTV is 100 percent, or the loans carry a substantial prepayment penalty, or the prepayment penalty extends beyond the introductory period. *Id.*

School-Based Eligibility

Linking eligibility for relief to the school attended does not have a clear counterpart in the mortgage market, but is similar to the cancellation of federal loans available to students who attend a school that closes before they can complete the program. In light of the very close links between some for-profit schools and PSL lenders, requiring cancellation of private loans not only for school closures but in cases where the school has engaged in deceptive marketing or other wrongful practices is justified.[91] While individual borrowers may already be able to get relief by raising school-related claims and defenses,[92] this avenue is only available to those borrowers sophisticated and lucky enough to find aggressive legal representation. Agencies with enforcement authority over particular schools or lenders could bring enforcement actions with the goal of securing payment relief for all affected borrowers.

3. Modification Terms

The third essential question for designing a PSL modification program is to decide what form of relief will be available to borrowers, and how the terms of modified loans will be determined. One option is to link the loan modification terms to the borrower's income, on an individualized basis. IBR and ICR, available for federal student loans, use this approach, as does HAMP "Tier 1." Another option is to modify loans based on uniform rules that do not vary by borrower. HAMP "Tier 2" modifications use this approach, although they still require a cross-check with borrower income. Loan modification terms may also vary depending on whether they focus on interest rate reductions, principal reductions, forgiveness over time, or other changes in the original terms.

Income-Based Modifications

The benefit of tying the modification terms directly to the borrower's income is that the resulting payment is likely to be affordable. HAMP "Tier 1" modifications have resulted in much greater payment reductions and much lower re-default rates than non-HAMP modifications in part because of the requirement that monthly payments be reduced to 31% of the borrower's gross monthly income.[93] However, getting an accurate picture of a borrower's current financial circumstances is time and labor-intensive for the borrower and the servicer. One way to reduce the burden, at least for borrowers with both private and federal loans, is to "piggyback" on the IBR or ICR application process.

Uniform Modifications

Modifications with fixed terms are less labor intensive at the application stage, but not as narrowly targeted to borrowers experiencing hardship, or to achieving affordability. Some borrowers will end up paying less than they could afford, while others will not receive deep enough payment reductions and may re-default. HAMP "Tier 2" provides standardized modification terms that result in payments anywhere from 25%-42% of the borrower's gross

[91] *See* National Consumer Law Center, Student Loan Law § 12.7 (4th ed. 2010 and Supp.)
[92] *Id.*
[93] NCLC: At a Crossroads, 18.

monthly income.[94] HAMP Tier 2 has not been in place long enough to provide a comparison of re-default rates with HAMP Tier 1, however.

Modification Terms

In order to ensure affordability and fairness for borrowers, it is not enough to simply reduce the current monthly payment on a loan. It makes a difference how the reduction is achieved. For example, extending the repayment period of a loan without changing any other terms will result in a lower payment, but greatly increases the total amount the borrower must repay. Similarly, allowing reduced payments or deferrals that result in negative amortization is harmful to borrowers in the long term.

In the mortgage context, there is strong evidence that the best way to reduce payments and also prevent re-default is to reduce principal.[95] Borrowers who are "underwater" on their homes have reduced incentives to keep paying, even if the monthly payment is currently affordable, since there is very little prospect of building equity. In the student loan context, it should theoretically make very little difference to the borrower whether payment reduction is achieved through interest rate reduction or through principal forgiveness. If the monthly payment amount and the total number of remaining monthly payments are the same, the share of repayment that is interest versus the share that is principal should not matter. In fact, the borrower may prefer an interest rate reduction to forgiveness of principal, since the latter may result in increased income tax liability. If the data submitted in response to this request for comments does not already address the question, the CFPB should determine the extent to which servicers and lenders in the PSL market prefer interest rate or principal reduction as a mechanism for reducing borrower payments and the impact on borrowers of different terms.

C. Regulatory and Systemic Barriers to Addressing Affordability and Default

The agency asked about potential impediments to providing relief to borrowers, including mismatched incentives among lending industry participants, servicing infrastructure weaknesses, and restrictive accounting guidelines.

There is very little publicly available information on these issues. Our experience with the mortgage industry suggests that mismatched incentives may indeed be a serious problem.[96] Similarly, there is reason to fear that servicing platform limitations – and more importantly, unwillingness to invest in necessary staff or technology – may delay and complicate implementation of an effective loan modification program.[97] The responses to this request for information should help shed light on the incentives and capacities of PSL servicers.

In our conversations with Sallie Mae and other private lenders, accounting guidelines are always raised as a barrier to providing relief to borrowers. In particular, lenders reference CNBE

[94] MHA Handbook, ch. II, 6.3.4.
[95] NCLC: At a Crossroads, 22.
[96] Diane E. Thompson, *Foreclosing Modifications: How Servicer Incentives Discourage Loan Modifications*, 86 Wash. L. Rev. 755 (2011).
[97] NCLC: At a Crossroads, 31.

Policy Guidance 2010-02, issued by the Office of the Comptroller of the Currency in August 2010. This guidance provides that "practices for working with distressed borrowers that mirror federally-guaranteed student loan programs…[are] not appropriate for student loans not backed by a federal guarantee."

Our discussions with the Office of the Comptroller of the Currency suggest that lenders may be misinterpreting this guidance or using it as a convenient excuse for refusing to assist distressed borrowers. First, the guidance impacts only accounting practices; it dictates what lenders may do without recognition of an "impairment of credit" on a loan, but does not actually forbid any action. For loans that are already in default, the guidance should have little or no impact, since such loans are already 'impaired' assets. Second, the guidance is a companion to the Uniform Retail Credit Classification and Account Management Policy, which governs the accounting treatment of modifications of consumer loans more generally. The special guidance for student loans is intended to provide *more* flexibility (by allowing grace periods and in school deferments) than lenders have with other types of credit (such as credit cards).

Whether rightly or wrongly, however, lenders and servicers do refer to the CNBE document as a barrier to providing loan modifications. It may also contribute to lenders' reluctance to provide any kind of payment relief before borrowers are in default. The CFPB should work with the OCC to provide updated guidance to lenders that more clearly indicates the range of workout options available and how such actions must be indicated for accounting purposes, and encourages lenders to work with borrowers, since performing loan modification agreements are beneficial from a safety and soundness perspective as well as for individual borrowers.

D. Other Relief Options

The Request for Information focuses on options for creating a loan modification program, as do these comments. However, loan modifications, while helpful, should be combined with other policies to provide relief to borrowers and prevent defaults in the future. These policies include:

Restoring bankruptcy rights for all student loan borrowers. Restoring bankruptcy rights is the single most important action that Congress can take to provide relief to these borrowers. Restoration of bankruptcy rights would not only provide relief to the individual borrowers who have no other options for addressing their financial circumstances, but it would alter the incentives of lenders for all PSL borrowers to encourage more voluntary loan modification efforts. Moreover, it would deter irresponsible lending, as lenders would know that borrowers had a safety valve if their education proves worthless and their loans unaffordable.

Mitigating the impact of negative credit reporting on borrowers' ability to access housing, employment opportunities and other basic needs. Credit reports are now used in many contexts unrelated to lending, including employment and apartment rental applications and various forms of insurance. Borrowers having difficulty paying their PSLs – and especially borrowers who are making modified payments per an agreement with their lenders – should not have to struggle against the damaging effects of negative credit reporting. The HAMP rules, while not ideal, do provide some mitigation of credit reporting consequences for borrowers with loan modifications. Even without changes in law or regulation, more relief for borrowers is possible; in NCLC's conversations with lenders, some appear to *mistakenly* believe that the Fair Credit Reporting Act prevents them from providing less negative credit reporting for borrowers making modified payments. The CFPB and other agencies should provide guidance on this issue so that lenders will not feel chilled in removing trade lines or otherwise removing derogatory information to borrowers making affordable payments and seeking a fresh start.

Encouraging voluntary loan modification efforts. Lenders and servicers assert that they are willing to provide assistance to struggling borrowers and regularly do so. NCLC's experience with low-income borrowers is that such programs are very hard to access. Nevertheless, voluntary efforts by the industry should be encouraged,[98] and any barriers to such efforts (such as unnecessarily restrictive accounting guidelines) should be removed or modified.

Eliminating predatory student lending, including development of sound underwriting standards ensuring ability to pay. Controls on future originations are *essential* to prevent a repetition of the lender-driven over-borrowing that characterized the years leading up to the crisis. There is already evidence that investors' appetite for high-risk private student loans has recovered.[99] NCLC and our allies elsewhere have shared recommendations for preventing abusive or unaffordable origination of new loans.[100]

Including provisions for flexible repayment and death and disability discharges in new originations. Future PSL originations should contractually provide for loss mitigation in appropriate circumstances. One mechanism is to mandate school certification of private loans and the inclusion of such options as a condition of this certification.

Improving the availability and accuracy of information provided to students before they borrow. As the CFPB has noted, many students fail to apply for federal financial aid or fail to exhaust their federal loan limits before taking out PSLs. Further, many PSL borrowers are confused about the nature of their loans, and the differences between federal and private educational loans. While disclosure and borrower counseling are not sufficient by themselves to prevent lending abuses, they are necessary and should be improved and expanded.

Vigorously enforcing federal and state laws to protect borrowers from origination and collection abuses and for-profit school abuses. Enforcement of existing borrower protections is just as important as creating new protections and additional repayment options for borrowers in

[98] In other industries, voluntary efforts have reached meaningful scale. For example, the credit card industry cooperated in the creation of Consumer Credit Counseling Services programs to offer debt management plans to borrowers in distress. *See* National Consumer Law Center, Credit Counseling in Crisis: The Impact on Consumers of Funding Cuts, Higher Fees and Aggressive New Market Entrants (April 2003), http://www.nclc.org/images/pdf/credit_counseling/report_creditcounseling_crisis.pdf.

[99] *See, e.g.* Ruth Simon, Rachel Louise Ensign and Al Yoon, "Student-Loan Securities Stay Hot: Investors' Hunger for Returns Is Driving Demand Even as More Borrowers Fall Behind on Their Payments" *Wall Street Journal* March 4, 2013 (noting that demand for the *riskiest* portion of a $1.1 billion sale of new private student loan securities by Sallie Mae was 15 times higher than the available supply), *available at* http://online.wsj.com/article/SB10001424127887323293704578334542910674174.html.

[100] *See generally* policy documents available at http://www.studentloanborrowerassistance.org/legal-policy/.

distress. NCLC and others have witnessed abuses by for-profit schools, loan servicers and debt collectors.[101] The CFPB should use its supervision and enforcement authority to identify and address such practices.

VI. Conclusion

Large and growing numbers of private student loan borrowers are falling behind on their loans. We applaud the CFPB for taking steps to examine and address this problem. A number of policy options, including mandating or encouraging loan modifications, are available for assisting current borrowers and preventing future defaults. In designing a loan modification program, the CFPB should focus on ensuring affordability for borrowers, preservation of borrower rights and protections, availability of enforcement mechanisms, reaching meaningful scale, and selecting policies that are fair to borrowers and to the lending industry.

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[101] *See, e.g.*, Written Testimony of Deanne Loonin, Director of National Consumer Law Center's Student Loan Borrower Assistance Project in Response to the May 5, 2011 U.S. Department of Education Notice of Establishment of Negotiated Rulemaking Committees and Notice of Public Hearings (May 20, 2011), *available at* http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/2007/03/neg-rulemaking-may2011.pdf; National Consumer Law Center, Comments in Response to Federal Trade Commission Request for Public Comments: Vocational School Guides Review, Matter No. P097701 (Oct. 16, 2009), *available at* http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/policy_briefs/FTCguides1009.pdf.