**Comments to the Consumer Financial Protection Bureau on Request for Information Regarding Private Education Loans and Private Educational Lenders, 76 Fed. Reg. 71329 (November 17, 2011)**

**Docket # CFPB-2011-0037**

**January 17, 2012**

## Introduction

These comments are submitted on behalf of the National Consumer Law Center's low-income clients.[1] 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.[2] Our comments on private student loans are based on our experiences representing low-income consumers. We also receive e-mails from thousands of borrowers each year through our Student Loan Borrower Assistance web site.

The way in which the private student loan market evolves in the future has far-reaching implications for our clients and others seeking to better their lives through education. Our comments focus on the CFPB's authority to regulate the market going forward and to help provide relief to financially distressed borrowers.

In brief, our comments are:

- The critical context for private student loan issues is that, due to the lack of a bankruptcy option or any federally mandated relief, students with little experience in financial matters can incur tens and even hundreds of thousands of dollars of completely unaffordable debt that will follow them and damage their credit for their entire lives.

- Little data is available on the private student loan market and is sorely needed.

- Private student loans have high default rates that are likely to climb.

- Too many students take out private students without having exhausted cheaper and safer federal financial aid.

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[1] The National Consumer Law Center (NCLC) is a nonprofit organization specializing in consumer issues on behalf of low-income people. NCLC works with thousands of legal services, government and private attorneys and their clients, as well as community groups and organizations that represent low-income and older individuals on consumer issues.

[2] Most of the clients we represent are low-income borrowers living in Massachusetts. We work with other advocates across the country representing low-income clients. We also 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. See the Project's web site at www.studentloanborrowerassistance.org. NCLC also publishes and annually supplements practice treatises which 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 Deanne Loonin.

- Some for-profit schools are making predatory institutional loans that they know, at the outset, students cannot repay.

- Private student lenders have failed to adopt any meaningful policies, such as long-term repayment options or loan modifications, to help students who are buried in debt.

- Despite receiving disclosures, co-signers often do not realize they are liable for loans and lenders often refuse to cancel loans even in the event of the student's death.

**Financially Distressed Private Student Loan Borrowers Have Nowhere to Turn**

The student loan market is unique in that the government is the primary supplier of loans through the federal student loan program. Private student loans are almost always more expensive over the long term than federal loans. This is especially true for borrowers with lower credit scores or limited credit histories.

Federal loans come with a range of borrower protections that are mandated in the federal Higher Education Act, including income-based repayment, deferment and cancellation rights. In contrast, private lenders are not required to offer any particular relief.

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. Since 2005, nearly all student loan borrowers must prove "undue hardship" in court in order to discharge their loans. Courts have been very restrictive in applying this standard.[3]

Private student loan borrowers seeking to prove undue hardship often encounter judges who do not understand the difference between federal and private loans. The judges may deny hardship cases based on a mistaken belief that the borrowers have the same flexible repayment and other options as federal student loan borrowers.

Collectors often tell our clients that they have nowhere to go because they cannot get bankruptcy relief. The lenders and collectors therefore use the limited bankruptcy relief as a weapon to pressure financially distressed borrowers.

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[3] See generally National Consumer Law Center, "No Way Out: Student Loans, Financial Distress and the Need for Policy Reform" (June 2006), available at: http://www.studentloanborrowerassistance.org/uploads/File/nowayout.pdf; Testimony of NCLC and NACBA before the U.S. House of Representatives Committee on the Judiciary, "Undue Hardship? Discharging Educational Debt in Bankruptcy" (September 23, 2009), available at: http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/policy_briefs/testimony_bankruptcy_sept09.pdf.

Creditors argue against restoring bankruptcy rights for student loan borrowers, claiming that treating student loans the same as other debts in bankruptcy would create greater risk for them. This is far from obvious. If most borrowers who file for bankruptcy cannot afford to repay their debts, a more restrictive bankruptcy policy is not going to make them more able to pay.

The private student loan industry grew rapidly during the pre-2005 period when these loans were fully dischargeable in bankruptcy. The industry has contracted in recent years even with a restrictive bankruptcy policy. The recent tightening of the credit market has helped eliminate loans that never should have been made. This has forced schools and lenders to think twice before pushing these high-priced products. We believe that this is a welcome market correction.

There is simply no good evidence that bankruptcy policy affects creditor behavior. Interest rates, for example, were largely the same before and after the 2005 bankruptcy law which made private student loans more difficult to discharge in bankruptcy. Sallie Mae steadily increased the average margin on private student loans above the prime interest rate from 2002 through 2007, both before and after bankruptcy became less available to students.[4] The business of private lending has expanded and contracted based on market opportunities, not based on bankruptcy.

Bankruptcy is not and should not be the entire safety net, but it is the most organized, recognized, and effective system available offering relief to those who most need it. It is never an easy decision for a consumer to choose bankruptcy. This choice comes with many costs and consequences, including damaged credit that lasts for years. However, it was a choice that was available to private student loan borrowers before 2005, but is now available only through the random, unfair, and costly "undue hardship" system. Effectively, it has become no choice at all for those who most need it.

We see and hear the human toll of the eviscerated student loan safety net every day from the low-income borrowers we represent. Some are so traumatized by collection calls and skyrocketing debt loads that they vow never to try education again. These choices not only impact these individuals and their families, but also harm our society.

**Lack of Reliable Data about Private Student Loans**

There is no comprehensive database on private loans, comparable to the government's National Student Loan Data System. Lenders do not publish proprietary data on their loans. The national data that is available is based on various estimates or infrequent surveys. The College Board, for example, uses data from an informal pool of the largest non-federal loan sponsors.[5] Recently, the Department of Education began posting on CollegeNavigator.gov private loan data for schools, but these data are for first-time, full-time students only and appear to be highly

[4] Sallie Mae, "Private Credit ABS Investor Presentation" (September 2008).
[5] See generally College Board, "Trends in Student Aid 2011" (2011).

unreliable and inconsistent.[6] 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.

**High Default Rates and Financial Distress**

The clients we represent and most of the borrowers contacting us through our web site cannot afford to pay their private student loans. This persistent financial distress can be seen in the skyrocketing levels of private student loan defaults and write-offs.

The private student loan industry began to crash in 2008 as defaults ballooned and overall economic conditions deteriorated. For example, in the last quarter of 2011, Sallie Mae posted a loss of $47 million and charged off $272 million in its private education loan portfolio. Over the past three quarters of the year, the company charged off $809 million worth of private education loans.[7] Fitch Ratings in 2009 stated that, from a net-charge-off perspective, the rates had been deteriorating for the main private student lenders since 2006.[8] Fitch Ratings reported in July 2011 that losses for private student loans continue to increase. [9]

Sallie Mae and others have attributed much of the poor performance to their "nontraditional" loan portfolio. These loans are described as loans to borrowers who are expected to have a high default rate due to numerous factors, including a lower-tier credit rating or low program completion and graduation rates usually at "nontraditional schools." Even when the borrower is expected to graduate, nontraditional loans tend to go to borrowers with low expected incomes relative to the cost of attendance.[10] 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 credit deterioration.[11] Overall, Sallie Mae executives noted in 2010 that, of the $6 billion in non-traditional private loans they had made, a projected 40% would default. These loans, they claim, made up about 11% of their private student loan portfolio.[12]

**Scope and Use of Private Education Loans**

**(Question #1: Extent of reliance on non-federal student loans)**

The private student loan industry grew throughout the 1990's and early 2000's. During this time, many private lenders steered borrowers to these products even if they were eligible for federal student loans. Unfortunately, many lenders targeted low-income borrowers with predatory loans. Too many of these risky, high cost loans were destined to fail and have been failing at astronomical rates, especially since the credit crisis began.

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[6] Project on Student Debt, "Student Debt and the Class of 2009" at 10-11 (October 2010), available at http://projectonstudentdebt.org/files/pub/classof2009.pdf.
[7] The News Journal, "Sallie Mae Posts 3rd-quarter loss of $47M", (Oct. 21, 2011); Sallie Mae Corp, 10-Q at 11, 13 (Nov. 4, 2011).
[8] Fitch Ratings, "Private Education Loans: Time for a Re-Education" at 7 (Jan. 28, 2009).
[9] Fitch Ratings, "The Student Loan Report Card "(July 2011).

[10] Fitch Ratings, "Private Education Loans: Time for a Re-Education" at 7 (Jan. 28, 2009).
[11] Id. Citi sold Student Loan Corp. to Discover in 2010.
[12] Student Lending Analytics Blog, "The $5.4 Billion Private Student Loan Problem" (May 16, 2010).

The majority (52%) of private student loan borrowers in 2007-08 borrowed less than they could have in federal Stafford loans.[13] In 2007-08, 25% of private loan borrowers took out no Stafford loans at all and 13% did not apply for federal financial aid.[14] Interestingly, the majority of private loan borrowers (57%) attended schools charging $10,000 or less in tuition and fees. The percentage of African Americans who took out private loans quadrupled between 2003-04 and 2007-08, from 4% to 17%.[15]

The GAO found in 2009 that a slightly higher percentage of dependent undergraduate students borrowed private loans compared to independent students and a higher percentage of dependent students from middle and high income families borrowed private loans compared to dependent students from low income families.[16]

We began to see a growing number of low-income clients with private student loans about ten years ago. Many clients had multiple loans with large balances. Most of these loans were third party loans.

A high percentage (about 70 -75%) of our clients attend for-profit schools. These schools have had the largest proportion of students taking out private loans and the largest increase in private loan borrowing. Forty-two percent of all for-profit school students had private loans in 2007-08, up from 12% in 2003-04.[17] In contrast, 25% of students at private non-profit four year schools, 14% of students at public four year schools and 4% of students at public two year schools had private student loans in 2007-08.[18] In 2007-08, for-profit school students comprised about 9% of all undergraduates, but 27% of those with private loans.[19]

Since the credit crisis in 2008, we have noticed a steady decline in third party private student lending to our clients. The College Board reports that after peaking at 26% of total education loan volume in 2006-07, nonfederal loans declined to 12% of the total in 2008-09, 8% of the total in 2009-10 and 7% of the total in 2010-11.[20] More recently, lenders have reported increased growth and competition.[21]

The decline in predatory student lending is a welcome respite for our clients; yet significant damage has already occurred. Further, we have started to see more clients with institutional loans from for-profit schools. (See Questions 5 and 6 below).

In addition to third party and institutional loans, some states offer their own private loan programs. In New York, for example, the New York Higher Education Financing Authority

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[13] The Project on Student Debt, "Private Loans: Facts and Trends" (July 2011).
[14] Id.
[15] Id.
[16] U.S. Government Accountability Office, "Higher Education: Factors Lenders Consider in Making Lending Decisions for Private Education Loans", GAO-10-86R (Nov. 17, 2009).
[17] The Project on Student Debt, "Private Loans: Facts and Trends" (July 2011).
[18] Id.
[19] Id.
[20] College Board, "Trends in Student Aid 2011" at 13 (2011) .
[21] Fitch Ratings, "Private Education Loans: Time for a Re-Education" at 7 (Jan. 28, 2009).

issues private bonds to purchase loans made by private lenders that participate in the program.[22] Participating lenders must sign agreements to make loans in accordance with the program guidelines. Loan rates are set by the New York State Education Department and are determined by credit score. Interest rate maximums cannot exceed 16.5%.[23]

**Reasons for Private Student Loan Usage**

**(Question #2: Explanations for private student loan use)**

From our clients and those who contact us on our web site, we hear the following explanations for using private student loans:

1. **Borrowers are confused and mistakenly select private loans instead of federal.**

   Based on our experience, borrowers rarely understand the difference between private and government loans.

2. **Schools or lenders push private loans on borrowers**.

   In the worst cases, school financial aid officers or other school staff provides inaccurate information in order to lure borrowers into private loans or otherwise pressure borrowers to take out these loans. Particularly during the heyday of predatory lending, many lenders aggressively marketed their student loan products directly to consumers and schools promoted "approved" lenders that gave kickbacks to the school. Private student lending, particularly prior to the credit crisis, became very much a push market in which products were offered not only in response to consumer need but also to fulfill investor demand.[24]

   Though creditors have ceased some of these practices, the debt remains with the students. In addition, since the decline in market abuses occurred due to market changes rather than aggressive new legislation or enforcement actions, there is nothing to prevent the resurgence of abuses in the future. This is why it is so important for the CFPB to act precipitously and preemptively to ensure that the market that reemerges is fair, efficient and devoid of predatory practices.

3. **Non-students, including parents and friends, co-sign private loans.**

   Some of our clients and even more of the borrowers contacting us through our web site co-signed private student loans. Most are confused about the scope of their obligations. For example, we very frequently hear from parents who believe that their children should be liable for the loans even though the parents co-signed. In

[22] N.Y. Educ. Law § § 690-694-b; N.Y. Comp. Codes R. & Regs. Tit. 8, § § 2231.1-2213.28. See also New York Higher Education Loan Program Underwriting Manual (August 25, 2010).
[23] N.Y. Comp. Codes R. & Regs. tit. 8 § 2213.9.
[24] *See generally* National Consumer Law Center, "Paying the Price: The High Cost of Private Student Loans and the Dangers for Borrowers" (Mar. 2008), *available at* http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/Report_PrivateLoans.pdf.

most cases, when we review the documents, we find that lenders provided the co-signer disclosures if required. However, as with most disclosures, few borrowers read or are given time to read the fine print and fail to understand that they are equally liable for the debts.

In one case, a monolingual Spanish speaking client earning minimum wage co-signed multiple private loans for her daughter's education. Her daughter attended a private non-profit college in the Boston area with a tuition of over $25,000/year. She attended for only about 1 ½ years, dropping out because of concerns about affordability. The client had previously taken out a PLUS loan and thought the private loan was another PLUS loan.

**4. Perception that private loans have better terms.**

Shopping for student loans can be very confusing for parents in particular because the comparison between parent PLUS loans (the federal loan option for parents) and private loans is not as clear as for other loans. Parent PLUS loans have higher fixed interest rates than other federal student loans. Further, many of the most attractive federal student loan options, such as income based repayment, are not available for parent PLUS borrowers. With the possible exception of PLUS loans, however, federal student loans are almost always a better deal than private student loans for borrowers.

**5. Perception that the private loan process is easier and faster.**

Some lenders and financial aid office staff tout private loans as an easier alternative to federal loans. In a 2006 report, the Institute for Higher Education Policy noted that students may perceive private loan borrowing to be more convenient than federal loans. Among other reasons, borrowers do not have to fill out the Free Application for Federal Student Aid (FAFSA) form to get private loans.[25]

**6. Borrowers cannot obtain sufficient funds through federal loans.**

Some students may understand the difference between federal and private loans, but may still choose private loans because of the borrowing limits in the federal loan programs. For example, a recent client attended UMass Amherst. He had to withdraw due to severe emotional problems. He exhausted his federal aid, but his parents did not want to take out PLUS loans. The client was not eligible at the time for Pell grants. The loan limits for undergraduates capped the amounts this client could borrow. The funds available were not enough to cover even a public university education and so the client took out smaller amounts of private loans as well. The lender extended this credit without requiring parental co-signers.

[25] Institute for Higher Educ. Policy, "The Future of Private Loans: Who is Borrowing, and Why?" at 22 (Dec. 2006).

**Information and Shopping for Private Loans**

**(Question #3: Sources of information about private education loans and effectiveness of existing disclosures)**

Most of our clients with private loans report that they got the information about the loans directly from their schools, usually from financial aid officers. In cases where we are able to obtain the original loan agreements and disclosures, we generally find that the lender provided the required Truth in Lending Act (TILA) disclosures. However, the information in the disclosures is not always accurate. Further, most borrowers tell us that they do not recall having seen or having been shown the disclosures.

Effective February 14, 2010, lenders making private student loans are required by TILA to provide special disclosures.[26] There are three sets of required disclosures: 1) application and solicitation; 2) loan approval; and 3) final disclosures. Each is subject to special timing rules and detailed form and content requirements.

The new disclosure rules are a significant improvement for consumers. Among other changes, the disclosures must be given prior to consummation and include more detailed information about cost and repayment options.

However, the new disclosures still leave much to be desired. For instance, the disclosures focus on interest rates, rather than APRs that include fees. Moreover, there has been limited enforcement and investigation to determine whether private lenders are complying with the new regulations and if they need to be improved. This is a critical role for the CFPB as it has full authority to write rules and enforce TILA.

The CFPB should also write rules to ensure that the TILA student loan disclosures apply more broadly. The current scope is too narrow, primarily because it excludes open-end credit. This is problematic particularly as lenders create new products, in many cases offered as open-end credit or disguised as open-end credit.

The CFPB's "Know What You Owe" campaign is a very promising step in improving the information available for prospective borrowers. We urge the CFPB to expand these efforts and work to create greater standardization in financial aid offers and other documents provided to prospective students and their families. In addition, the Student Debt Repayment assistant site is an excellent tool for borrowers seeking to understand the differences between federal and private loans.

We recommend that the CFPB link the Repayment Assistant tool to the CFPB ombuds office so that borrowers have a central resource to report problems with private student loans and seek resolutions.

[26] 15 U.S.C. § 1638(e); Reg. Z § 226.46.

A common complaint we hear from borrowers is that they are unable to obtain even basic information, such as amounts owed and paid, from their private student lenders or servicers. A borrower from Franklin, NY contacting us through our web site summarized this problem concisely: "I have a private loan that has been passed around and I can't seem to get ahold of anyone about it."

Unfortunately, private loan borrower rights to fair billing and accounting statements are not as clear or strong as for federal loans. For example, federal student lenders are required to respond within thirty days to any inquiry from a borrower on a loan. There are also dispute resolution procedures set out in the Higher Education Act.[27] These are essential rights for borrowers that need basic information about what they owe on loans, how much they have paid, and how they can dispute possible errors.

**Institutional Loans**

**(Questions 5 and 6)**

As the third party student loan market crashed, many for-profit schools began to develop their own products. Institutional loans have become a major component of financial aid. While exact numbers are difficult to come by, the College Board attributes much of the growth to lending by for-profit schools."[28] Overall, the College Board estimates that institutional loans have grown from about $600 million in 2007-08 to $720 million in 2010-11.[29]

As documented in NCLC's January 2011 report, the planned default rates on these school loan products are shockingly high.[30] For example, at the beginning of FY 2009, Corinthian Inc. expected a loan default rate on its school loan product of 50% -- before it even made the loans.[31] Corinthian adjusted this estimate to 55% for FY 2009 and predicted a range of 56 to 58% in 2010. [32] At nearly one-third of Corinthian campuses, more than half of all first year students took out high-cost private student loans in 2009.[33]

Despite the dismal performance of these loans, Corinthian executives told investors in summer 2011 that they planned to double the volume of private loans made through the institutional loan program to $240 million.[34] In June 2011, Corinthian announced a new private

[27] 34 C.F.R. § 682.208(a).
[28] College Board, "Trends in Student Aid 2011" at 13 (2011).
[29] Id.
[30] National Consumer Law Center, "Piling It On: The Growth of Proprietary School Loans and the Consequences for Students", (January 31, 2011), available at: http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/proprietary-schools-loans.pdf.
[31] The amount discounted against revenue (the discount rate) is the estimated loan default rate. See generally Corinthian Colleges Q2 2009 Earnings Conference Call Transcript (Feb. 3, 2009).

[32] Q42009 Corinthian Colleges Earnings Conference Call (Aug. 25, 2009).

[33] Stephen Burd, "Updated: New Data on Private Loan Borrowing at Corinthian Colleges Should Raise Alarms", New America Higher Ed Watch (June 17, 2011).
[34] Id.

loan facility with ASFG, an existing for-profit education student lender. As with its prior institutional loan program, Corinthian will be obligated to purchase any of the new private student loans that are delinquent for more than ninety days. Further, ASFG was supposed to purchase a portfolio of Corinthian's institutional loans at a discount.[35]

DeVry has ramped up its institutional lending program, lending $13,360,000 more in 2011 than 2010 as of September 30, 2011. Even as DeVry increased the amount available to students, the company charged off a high proportion of these loans. DeVry set aside 36.8% of the total value of the loans to offset expected delinquencies.[36]

Other schools have also made school loans with exorbitant default rates. Analysts have estimated that ITT may assume close to a 45% loss rate or even higher on institutional loans.[37] However, ITT is phasing out its PEAKS program and has not originated new loans through the program as of July 2011.[38]

The schools seem to view these loans more as "loss leaders" to keep the federal dollars flowing. Among other reasons, for-profit schools must show that at least 10% of revenues come from sources other than federal student aid provided by the U.S. Department of Education. Since many of these schools generate revenues and profits almost exclusively from federal funds, compliance with the 90-10 rule is a lifeline of the schools and its investors. The school can comply with this rule by inflating their tuition and loaning the amount not covered by federal loans and grants, even if many of these loans get written off as bad debt. As CFPB's Assistant Director for Military Affairs Holly Petraeus has highlighted, this has also led to aggressive targeting of the military service member market as Department of Defense education funds are not included in the 90% category.

However, the growth of institutional lending is not only about the 90-10 rule. It is also a way for schools to keep revenues of all types flowing so that profits remain high and the companies remain attractive to investors.

Each charge-off represents an individual who cannot repay a debt and who may be facing aggressive collection tactics. These student borrowers generally face numerous collection calls, lawsuits and negative entries on their credit reports that can last for extended periods of time. Many schools require students to make payments on institutional loans while in school. In contrast, most third party private and all federal loans can be deferred during school. Interest may accrue, depending on the type of loan, but payment is not required. This places many

[35] Corinthian Colleges, Inc., 10-Q at 8, 9 (November 3, 2011); See also PAA Research, "COCO: ASFG Arrangement a 90/10 Workaround? Maybe. A Real Private Lending Program Most Definitely Not, Cutting FY12 Estimates" (June 30, 2011).
[36] DeVry, Inc., 10-Q at 12, 13 (November 4, 2011).
[37] PAA Research LLC, "ESI: Connecting the Dots on ESI's Increasingly Worrisome Off-Balance Sheet Exposure-The Potential 'Daisy Chain' of Events" (June 21, 2011).

[38] ITT Educational Services, Inc., 10-Q at 10 (October 21, 2011).

students in a trap. Many cannot pay the monthly payments on institutional loans while they are in school and as a result are often terminated from the schools or are denied transcripts.

The CFPB should examine these loans closely for unfair, deceptive and abusive acts or practices (UDAAP). The Bureau should also consider whether there are any fair lending concerns and develop and enforce sound underwriting standards. We particularly support Director Cordray's recent comments that the CFPB will be looking closely at these loans and the tactics by which they are marketed.[39] Among other unfair practices, Director Cordray noted that schools are making loans even when they anticipate default rates as high as 50%. This is not only harmful to borrowers as described above, but also a safety and soundness issue for financial regulators, including the CFPB, to investigate. Among other tools, the CFPB has supervisory authority over nonbanks that can be used to investigate the scope of abusive institutional loans, potential accounting abuses, and other unfair or abusive practices.

**Repayment and Lack of Relief**

**(Question #11: Alternative repayment plans, modifications, default reduction and rehabilitations)**

Unfortunately, private lenders have been generally inflexible in trying to assist financially distressed borrowers.[40] Unlike the federal student loan programs, there is no federal law requiring private student lenders to offer particular types of relief or flexible repayment. Private student loan borrowers are generally at the mercy of their creditors.

Many lenders have also increased collection activity. Sallie Mae, for example, has announced steps to resolve higher risk accounts, including a more aggressive use of collection efforts.[41]

The most common complaint we hear is that the lenders do not offer meaningful relief. Here are a few voices (e-mails reprinted verbatim) from borrowers contacting us through our web site.

> **Borrower in Ohio**: "I have a private loan with Sallie Mae that allowed me to defer due to economic hardship. All of a sudden it would not allow me to do so and my loan went into default... They have told me to stop paying other bills and to do what I have to do to get the money..They have also told me to take other loans or sell my belongings to get the money., I have nothing except too much debt to income at this time to be able to do so. They tell me to make an offer, but what I can do at this time never works for them…it's their way or no way and it doesn't matter if I'm put out on the street or left to starve."

[39] Edward Wyatt, "Some Lenders to Students Face Greater U.S. Scrutiny", The New York Times (Jan. 12, 2012).
[40] *See generally* National Consumer Law Center, "Too Small to Help: The Plight of Financially Distressed Private Student Loan Borrowers" (Apr. 9, 2009), *available at* http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/TooSmalltoHelp.pdf.
[41] Paul Basken, "Sallie Mae Reports $159-Million Loss and More Delinquencies by Borrowers", The Chron. of Higher Educ. (Oct. 23, 2008).

**Borrower in Sacramento, CA**: "I need an income-based refinance plan, but I haven't found one available for my private loan…Please help me find, or create a solution!!!"

**Borrower in Cudahy, WI**: "I have many student loans with Sallie Mae, Great Lakes and Citi Bank. They will all become current this month and I am having a hard time figuring out how to pay over $800 a month in just loans. I just signed up for the IBR repayment plan, but it doesn't work for the $57,000 I owe in private loans…I, of course didn't know how bad private loans were when I signed up for them. So, i still have to pay about $600 in loans a month on top of rent and bills, on a bartender's salary. (I obviously can't find a job in my profession. Although I'm interning for free in the field...doesn't help on bills...)"

**Borrower in Turner Falls, MA**: "I'm writing to support: H.R. 2028: Private Student Loan Bankruptcy Fairness Act of 2011.

"I graduated with a Bachelors degree in 2008. After graduation I could not find a job because of the poor economy. I searched for jobs daily; I had sent out hundreds of resumes to no avail. I ended up having to pay Sallie Mae $150.00 (that I didn't have) every 3 months for them to grant me a forbearance! That money did NOT go to the principal balance of the loan, it was theirs to keep as well as interest that was accruing due to my involuntary hardship.

"After 2 years of being unemployed I finally obtained a part-time job as a Network Technician, making $13.00 an hour. I struggled to pay bills and old debt (not including student loans). At this time I was forced to continue the forbearance on my education loans; both Federal and Private. I did not make enough money to keep Sallie Mae satisfied. I tried to work out payment plans, but they wanted too much money that I couldn't afford. The payment went up as the interest piled up.

"As of today, I have accrued more than $30,000 in interest with Sallie Mae. My loan went from roughly $90,000 to $120,000 during the years I was unemployed. I continued the $150.00 forbearance "bribes" until late June 2011 when Sallie Mae told me that I had exhausted my forbearance period. I still cannot pay $1000 a month to them.

"I've tried numerous times to work things out with Sallie Mae; they will not work with me on this issue. Needless to say, the phone calls from Sallie Mae are endless and harassing. I have been yelled at, degraded, and verbally abused by their debt collectors, but I see no end to this downward spiral of college debt. (I'm not even working in my field of study).

"I want to live the "American Dream." I want a small house with a picket fence; a golden retriever; a decent job. I do not see the "American Dream" in my future at all."

**Borrower in Oregon**: "My husband and I got a US Bank no fee student loan for the duration we were in undergrad because federal loans did not cover everything. It was great until they came out of deferment. Now, my husbands student loan is $600 a month and mine is $474 a month. We have tried talking with US Bank about consolidating or refinancing, but they have been no help. We tried to get them to offer a graduated payment plan, extend it to a 30 year pay-off instead of 15, but nothing. The company that "owns" the loan is Great Lakes and they offer those programs, but because we have a US Bank student loan, we can't use any of them. They wouldn't even let us change the payment date so we could get caught up on payments until the payments were completely caught up. It makes no sense and is extremely frustrating. No one said it would be so hard with a student loan that wasn't a federal loan. We can't save and put money aside for a house, travel or kids. We don't know exactly what we are going to do. We are current for now (never were in default) and are still trying to figure out a way to get this resolved."

**Private Loan Deferments and Forbearances**

Unlike federal loans, there is no federal law requiring private student loan creditors or servicers to offer deferments or forbearances. In a 2008 study, the National Consumer Law Center surveyed private loan notes and found that most lenders provided an in-school deferment option.[42] However, interest generally accrued during this period, and borrowers were given the choice of paying the interest while in school or approving capitalization once they entered repayment. Since the economic crisis of 2008/2009, many lenders that are still offering private student loans are now requiring borrowers to pay interest while in school.

No forbearance rights were specified in nearly half of the loans in the NCLC survey.[43] Creditors may offer these plans, but they do not inform borrowers about available choices ahead of time in the loan notes. A number of lenders in the survey disclosed that they would charge fees to process forbearance and deferment requests. The fees were generally up to $50 for forbearances.

Most creditors have sharply restricted forbearance availability since 2008. In a 2009 report, Fitch noted that lenders began to impose more restrictive forbearance criteria starting in 2008 after realizing that the economic downturn would have a more prolonged impact on a borrower's ability to repay.[44]

**Repayment Relief**

Private loan creditors may offer flexible arrangements, but they are not required to do so. None of the loan notes we surveyed in our 2008 report specifically provided for income-based repayment. A few stated that borrowers would be able to choose alternative repayment plans in certain circumstances. However, the specific criteria and circumstances were not spelled out in the agreements. Only a few mentioned that graduated repayment was possible. In these cases, the loan contract stated that these plans would be offered only <u>if available</u>. There is no information provided about when such plans are available.

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[42] National Consumer Law Center, "Paying the Price: The High Cost of Private Student Loans and the Dangers for Student Borrowers"(Mar. 2008).
[43] *Id.*
[44] Fitch Ratings, "Private Education Loans: Time for a Re-Education" at 6 (Jan. 28, 2009).

In our experience representing borrowers through the Student Loan Borrower Assistance Project, we have found private lenders to be universally inflexible in granting long-term repayment relief for borrowers. Even in cases of severe distress, the creditors we have contacted have offered no more than short-term interest-only repayment plans or forbearances. This experience holds true for both for-profit and non-profit lenders. Some offer short-term interest-only payment options that merely prolong inevitable defaults, particularly for borrowers with large loan balances.

For example, we recently had a client with six private student loans from National Collegiate Trust (serviced by AES) with a total balance of about $232,000. He has private student loans from other lenders as well.

AES provided the client with summaries of his repayment options, including a Modified Graduated Repayment Schedule (MGRS), Reduced Payment (RP) and Temporary Hardship Forbearance. The MGRS programs offers three levels of repayment starting with an initial 12 month period of reduced payments equal to 50% of the regular monthly principal and interest payment amount. By the third year, the monthly payment returns to a level repayment schedule to satisfy principal and interest. AES acknowledges that, due to the reduced payments during the first two years of the MGRS, the payment amount by the third year may be higher than the monthly payment before the borrower selected MGRS.

Our client had already exhausted available hardship forbearances. His MGRS payment would have been $823.46/month. Earning a salary of about $10/hour and facing payments on other private student loans, even the supposed flexible plan payment of over $800/month was far beyond his budget.

In all of our efforts working with many borrowers and many lenders, we have not encountered <u>any</u> private student lender with a rehabilitation program or any other program to allow borrowers to get out of default and back into repayment.

**Modifications and Settlements**

In our experience representing borrowers in financial distress, most lenders, including non-profit lenders, have not been willing to cancel or modify loans or offer reasonable settlements. We have found that the lenders require very large lump sums to settle debts even from borrowers with very low incomes.

A lender’s failure to have a loan modification program and other practices to help distressed borrowers is an element or sign of unfair origination and underwriting practices. Speculative projections of future income made as part of determining ability to pay also require a plan for contingencies if the student’s income is not – either temporarily or permanently – as projected. Loan modifications that enable a student to make payments on a loan rather than completely defaulting are in both the students’ and the lenders’ best interests, but as we have seen in the mortgage market, sometimes industry needs the push of a regulator to come up with a win-win solution.

Modifications may lead to lost revenues for servicers, but in many cases the losses will be much greater if the servicer refuses assistance. Many borrowers are financially destitute with little or no future earnings prospects. Some are severely disabled or otherwise unable to work. Yet servicers remain largely unaccountable for their dismal performance in making modifications.[45]

In some cases, we hear from servicers that they do not have the authority to accept a settlement offer. A recent letter from AES to a client states that "AES is unable to accept a settlement offer in lieu of the total amount that is owed. Accordingly, the terms of the original Credit Agreement remain in effect. Your client will remain responsible for the repayment of the loans until they are paid in full with a zero balance." Servicers that claim to lack authority to modify loans should put the borrower in touch with the owner or entity that does have such authority.

Some lenders and servicers have discussed settlement with us. In every case, the lender has requested at least 80% of the total balance as settlement. This is far beyond an amount our clients can afford. In rare cases, we have represented low-income clients who have been able to raise significant funds to settle debts. Even these offers have been rejected. 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.

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. 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.

Regulations requiring loss mitigation can be justified both as a matter of ability to repay and as a safety and soundness issue. Because a student's future income cannot be known at the time of loan origination, responsible lending requires safety valves that ensure that the loan will be affordable even if initial projections turn out wrong. From a safety and soundness perspective, as well, 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.

We recommend that the CFPB focus on ways to incentivize lenders to modify loans and in some cases require modifications. This may involve addressing barriers in accounting or other safety and soundness standards to facilitate modifications. For example, Student Loan Corporation announced in public filings that the Office of the Comptroller of the Currency reviewed forbearance polices on private student loans and recommended a number of proposed changes including more rigorous requirements for participation in forbearance and loss mitigation programs, shorter forbearance periods and the requirement for minimum periods of payment performance between forbearance grants.[46]

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[45] For a discussion of this problem in the mortgage context, see National Consumer Law Center, "Why Servicers Foreclose When They Should Modify and other Puzzles of Servicer Behavior" (Oct. 2009).
[46] See Student Lending Analytics Blog, "OCC Tightens Forbearance Policies on Private Student Loans" (Jan. 19, 2010).

## Loan Cancellations

## Outside of Bankruptcy

The federal student loan programs provide death and disability cancellations. Similar programs are only available at lender discretion for private loans. A number of loans in a 2008 NCLC study stated explicitly that there will be no cancellation if the borrower or co-signer dies or becomes disabled.[47]

A few lenders have said they will cancel loans in very rare circumstances. For example, at least two lenders, Wells Fargo and Sallie Mae, recently announced programs to provide cancellations in cases of death and disability, but only on a small percentage of their outstanding private loans. Sallie Mae announced in 2010 that it had hired a company to administer claims for a new total and permanent disability provision on private education loans.[48] This program, however, applies only to the Smart Option Student Loans. The company also announced that it would forgive any unpaid balance in the event of a primary borrower's death. It is unclear whether this policy is being administered consistently.

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 any co-signers.[49]

However, 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.

As with loan modifications, the presence of a program for disability and death discharges is part of assessing whether lending is designed at the outset to be based on ability to pay. Discharges in case of the student's death are particularly important to prevent deception and unfairness for parents who do not expect to be liable, and should not be, for a loan after the student dies.

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[47] National Consumer Law Center, "Paying the Price: The High Cost of Private Student Loans and the Dangers for Student Borrowers" (Mar. 2008).

[48] See Securian Company News Release, "Securian Wins Contract for Administering Total and Permanent Disability Claims on Private Student Loans" (March 8, 2010).

[49] See Wells Fargo, News Release, "Wells Fargo Enhances Student Loan Products to Include Loan Forgiveness" (Dec. 17, 2010)

**School-Related Cancellations**

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.

A key to lender liability in many cases is the FTC holder rule. The holder rule (more accurately referred to as the Federal Trade Commission Preservation of Claims Rule), puts lenders on the hook when they have "referring relationships" with schools that defraud students or shut down unexpectedly.[50] The holder rule gives lenders an incentive to scrutinize the schools with which they have close relationships and to originate loans only with upstanding schools. This helps promote responsible lending. Under the FTC holder provision, 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, though: at most- for example, if the educational program was worthless or the school closed before the borrower attended - to the student's recovery of any payments made and to have the remaining indebtedness canceled.

Similar relief is available for most federal loans. Yet, private student lenders have sought numerous ways to avoid this type of liability, including hiding behind preemption arguments.[51] Many simply do not include the holder notice in the loan notes. Nearly 40% of the loans in our 2008 survey followed this potentially illegal approach.[52] 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.

Because the FTC does not have jurisdiction over banks, the holder rule only applies to schools, not depository lenders. That is, the FTC rule obligates only the schools, not the lenders, to include the holder notice in the contract. In general, the school must insert the notice in consumer credit agreements whenever the school is the originating lender and must arrange for the lender to insert the notice in the lender's credit agreement whenever the school refers the consumer to the lender or otherwise has a business arrangement with the lender.

An example of this concern can be seen in a recent letter from AES servicing one of our client's Chase private student loans. AES states that it understands that the client is seeking the possibility of a settlement and that it empathizes with the client's situation in regards to the alleged misrepresentation made by the school. However, 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

[50] 16 C.F.R. §433.2.
[51] See, e.g., Kilgore v. Keybank, 712 F. Supp. 2d 939 (N.D. Cal. 2010).
[52] National Consumer Law Center, "Paying the Price: The High Cost of Private Student Loans and the Dangers for Student Borrowers" (March 2008).

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."

The CFPB, with its broader jurisdiction over the lender, can remedy this problem by requiring all lenders that have close relationships with a for-profit school to include the holder rule in the contract and to prohibit clauses and other measures that undercut the rule.

**Conclusion and Policy Recommendations**

As the CFPB reviews the student loan market for unfair, deceptive or abusive practices, it must consider the full lifespan of a student loan. Specific policy recommendations to protect borrowers and ensure fair lending include:

**Origination of Private Student Loans**

- Develop and enforce sound underwriting standards ensuring ability to pay.
- Define and act against unfair, deceptive and abusive marketing practices.
- Improve and broaden scope of Truth in Lending Disclosures (TILA) and enforce TILA requirements.
- Require school certification of loans, including notifying borrowers of any untapped federal student loan eligibility.

**Servicing**

- Encourage and, where appropriate, require loan modification standards for distressed borrowers and discharges in case of death or disability.
- Extend Fair Credit Billing Act rights to private student loan borrowers.

**Collection**

- Enforce fair debt collection laws for the entire student loan collection market, both federal and private student loans.
- Prohibit deceptive, unfair and abusive default triggers, such as universal default clauses.
- Ban collection actions in inconvenient forums.

**Additional Relief for Borrowers and Measures to Promote Responsible Lending**

- Enforce the FTC Holder rule giving borrowers defenses against lenders with close relationships with unscrupulous schools.

- Ban mandatory arbitration clauses.

- Promptly create an effective private loan ombudsman office.

- Push restoration of bankruptcy rights for student loan borrowers.

**Data Collection and Research**

- Collect data on private student lending, including loan defaults, lender responses to borrower distress as well as campus level loan volume and pricing.

- Work with the Department of Education and other lenders to make this information available to borrowers and advocates as well as policymakers.

Thank you for your consideration of these comments. Please feel free to contact Deanne Loonin if you have any questions or comments. (Ph: 617-542-8010; E-mail: dloonin@nclc.org).