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Promoting Higher Education Access and Success

Higher Education Act (HEA) Reauthorization Recommendations

SLBA Student Loan Borrower Assistance

The Goals of Federal Student Aid

Despite all of the government money spent on financial aid, the difference in college graduation rates between our country's top and bottom income groups has widened by nearly 50% over two decades. In the past thirty years, the gap between students from low-and high-income families who earn bachelor's degrees has grown from 31% to 45%.[1]

The stakes are high as we search for ways to thrive in a competitive global economy and to keep our democracy alive. It is essential to focus on the original goals of federal student aid of making higher education more accessible and helping the neediest students succeed.

Times are Changing: Understanding Current College Students

Most students do not follow a straight line from high school to a four year college to graduation. Only 15% of undergraduate students live on campus. Three in 10 works full-time and one in four have their own children.[2] Low-income students in particular are less likely to enroll and complete higher education for many reasons, including real and perceived cost barriers as well as lack of academic and social supports. Federal student aid policy must reflect and accommodate the reality that "non-traditional" students are now the majority of college students.

Policies tailored to the needs of current college students include:

- Ensuring smooth transfer of credits,
- Providing aid for part-time students,
- Funding for support services such as TRIO and Gear Up, and
- Giving returning students the opportunity for a fresh start (see section below on a new Fresh Start for Students program).

Recommended Federal Aid Policy Priorities for HEA Reauthorization

These priorities focus on changes to the Higher Education Act. Comprehensive reform will also require amendments to other key legislation including the Truth in Lending Act (mainly for private student loans), Debt Collection Improvement Act, the Internal Revenue Code to ensure

[1] Institute on Assets and Social Policy, "The Roots of the Widening Racial Wealth Gap: Explaining the Black-White Economic Divide" (Feb. 2013). See also Advisory Committee on Student Financial Assistance, "Inequality Matters" (June 2013).
[2] HCM Strategists, "The American Dream 2.0" (2013).

equal tax treatment of borrowers, and the Bankruptcy Code. These recommendations highlight areas that will likely require legislative change. In some cases, however, legislative action is not necessary, but will be helpful to clarify existing authority. Congress should also use its powers to urge the administrative agencies to enforce existing regulations and laws and to create new regulations.

1. **Target assistance to the neediest students and their families.**

This general goal should include incentives for schools to admit low-income students and help them succeed. There are a number of suggested reforms that tie government aid to institutional records in admitting low-income students and helping them succeed, including Pell grant matching for underperforming colleges. As New America outlined in a recent paper, under this plan, four-year public and private non-profit colleges at which Pell grant recipients make up less than 25% of the student body would have to match a share of the Pell Grant disbursements they receive if they charge higher prices for these students.[3]

There may also be ways to incentivize completion and success, such as a system of loan forgiveness for on-time completion for Pell-eligible students.[4] This forgiveness programs closely tracks the goals of federal aid as opposed to other forgiveness programs, such as public service forgiveness, which disproportionately benefit graduate students and other higher income borrowers.

We urge Congress to use the HEA reauthorization process to target benefits to the neediest students. As discussed in detail below, we also recommend creating a "Fresh Start" program to eliminate barriers for students who fail to complete education after the first try.

2. **Reduce reliance on student loans and increase grant aid for those with the most financial need.**

   A. **Reducing reliance on loans.**
   This can be done in a number of ways include targeting grants and scholarships to the neediest students. Borrowers should also be encouraged to limit borrowing as much as possible.

   B. **Reduce burdens for those who borrow.**

   Key policies include:
   - **Setting a time limit on repayment,**
   - **Ensuring access to flexible, affordable repayment options, and**
   - **Creating a Fresh Start for Borrowers program (discussed below).**

[3] Stephen Burd, Kevin Carey, Jason Delisle, Rachel Fishman, Alex Holt, Amy Laitinen, and Clare McCann, New America Foundation, "Rebalancing Resources and Incentives in Federal Student Aid" (Jan. 2013).

[4] This proposal is discussed in Institute for Higher Education Policy, "Making Sense of the System" (Jan. 2013).

3. Fresh Start for Borrowers Program

Current federal aid practices and policies hammer students that do not succeed the first time around. Draconian collection and default policies prevent individuals from getting a fresh start. It also impedes economic productivity by preventing many students from returning to school, succeeding, entering repayment on their loans, and entering the labor force.

This section outlines a multi-faceted "fresh start" program including the following components:

- Preventing defaults,
- Reforming the current "get out of default" options including removing the one-time limit on programs to get out of default and allowing borrowers multiple consolidation opportunities,
- Restoring a student loan safety net, including bankruptcy rights for student loan borrowers,
- Eliminating adverse tax consequences for borrowers that receive administrative discharges for death and disability,
- Eliminating private collection agency involvement in federal student loan collections and other reforms to the collection process, and
- Creating a comprehensive relief program for borrowers harmed by predatory school practices and "collection proof" borrowers.

A. Preventing Defaults

1) Counseling and Education

Counseling and education can help some borrowers and should be improved. However, counseling and disclosures should not be substitutes for substantive reform.

2) Simplify Federal Aid

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.[5]

3) Automatic IBR Enrollment

To help catch borrowers before they fall into default, we recommend instituting an automatic entry process so that loan holders can evaluate borrowers for presumptive eligibility for income-based repayment and place borrowers temporarily in IBR during late stage delinquency.

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[5] Rachel Fishman, "What Borrowers Don't Understand About Student Loans May Hurt Them" Higher Ed Watch (June 18, 2012).

IBR provides many benefits for borrowers. Most important, automatic placement into IBR will allow borrowers to avoid the draconian costs of collection and extraordinary government collection powers. Current participation in IBR is low due mainly to lack of awareness and operational barriers. Creating an automatic entry, especially during late stage delinquency, would allow more to benefit. This could involve automatic debiting from borrower paychecks if borrowers choose this option.

However, not all borrowers are working and the automatic system should allow these borrowers entry as well. Borrowers receiving means-tested public assistance benefits should be automatically placed in a presumptive IBR program. They should be allowed to stay in this program by proving continued receipt of public assistance benefits. This should be a straightforward form, similar to the economic hardship deferment form. Borrowers applying for this deferment need only check the box that they are receiving public assistance payments and provide documentation.

In the meantime, Congress should increase oversight over Department of Education operations to ensure that borrowers are able to access IBR and that borrowers coming out of default can easily transition into income-based or income-contingent repayment.

4) Research the Causes of Default and Effectiveness of Post-Default Programs

Unfortunately, there are many holes in the existing research on the causes of student loan defaults. [6] Congress should require targeted study of the current "get out of default" programs as well as study of the costs of collections. Researchers should use longer-term default data rather than relying mainly on the limited cohort default rate (CDR) data, and they should study delinquency, not just default rates. While studying rates at a particular school may be useful, it is preferable to broaden the research and use the most comprehensive data possible.

The Texas guaranty agency has done some insightful studies in this area. It acknowledges the limits to its data and has recommended numerous topics for future study, including:

- The impact of servicer behavior on default rates,
- Servicer trends by type of institution to determine if forbearances or other types of cures dominate in particular sectors,
- Whether particular tools, such as forbearance, are associated with higher default rates, and
- Tracking a sample of borrowers whose loans are cured from entering repayment, through a cured delinquency, to a period of successful repayment.[7]

[6] See generally National Consumer Law Center, "The Student Loan Default Trap: Why Borrowers Default and What Can Be Done" (July 2012).

[7] Texas Guaranteed Student Loan Corporation, "Crisis averted or merely postponed? Examining long-term cohort default rates, resolving defaults, and curing delinquencies" (2005); The Institute for Higher Education Policy published this type of study in a March 2011 report, following a particular cohort of borrowers over time to evaluate whether they became delinquent or availed themselves of various options to postpone or delay repayment during their first five years in repayment. See Alisa F. Cunningham & Gregory S. Kienzl, "Delinquency: The Untold Story of Student Loan Borrowing." Institute for Higher Education Policy (March 2011).

As the Texas agency recommends, different cohorts of borrowers should be tracked after rehabilitation, reinstatement, and consolidation to assess re-default rates. It is not sufficient, however, to look only at success rates over time for the programs. Researchers must also take operational problems into account and quantify their effects. From our experience, for example, many borrowers re-default because of confusion or servicer error in submitting paperwork or other operational barriers. This is a major reason why the one-time limit on both consolidation and rehabilitation is so unfair to borrowers.

It is particularly important to research whether making payments is the reason why re-default rates may be lower under the rehabilitation program. It may seem intuitive that individuals are more invested in programs when they put money on the line, but this is a controversial topic in social science literature.[8]

Based on objective research, Congress should consider comprehensive reforms to the two main ways borrowers can currently get out of default, consolidation and rehabilitation. In the meantime, Congress should also reform these two programs so that they allow borrowers to truly get fresh starts.

B. Reform Existing "Get out of Default" Programs

1) Eliminate the one-time limit on rehabilitation.

Borrowers should be given more chances to get out of default. Because of this policy, borrowers who are desperately trying to get out of default into repayment are left with no options.

Suggested legislative language:
Section 428F(a) of the HEA (20 U.S.C. § 1078-6(a) is amended by striking paragraph (5).

2) Eliminate the FFEL program resale requirement.

Because of this "requirement," borrowers who make the necessary payments can get stuck with no possibility of completing the rehabilitation simply because their guaranty agencies cannot find buyers. At a minimum, agencies that cannot find buyers should be required to assign the loans to the Department of Education.

Statute: If Congress chooses to retain the requirement, at a minimum, Congress should extend the provision limited to loans from September 30, 2011 or earlier requiring assignments to the Department of Education if sales are not possible. 20 U.S.C. § 1078-6(a)(1)(A)(ii).

3) Provide full credit reporting benefits.

Lenders should be required to erase all negative history in the borrower's credit report, not just the default notation. This is a much more complete "credit clearing" benefit. This can be done without amending the Fair Credit Reporting Act.

[8] See, e.g., Christopher Shea, "A handout, not a hand up" The Boston Globe (Nov. 11, 2007).; Nava Ashraf, James Berry, & Jesse M. Shapiro, "Can Higher Prices Stimulate Product Use? Evidence From a Randomized Experiment in Zambia" Poverty Action Lab (2006).

Statute: 20 U.S.C. § 1078-6(a)(1)(C).

4) Reduce Collection Fees for Rehabilitation

Collectors should not be making so much profit in excess of the costs of collection. Currently the HEA allows collectors to charge up to 18.5% of the outstanding loan balance at the time of sale without regard to whether those charges are actually earned.

Suggested language: 20 U.S.C. § 1078-6(a)(1)(D)(i)(II)(aa)
(aa) charge to the borrower **reasonable and bona fide fees** ~~an amount~~ not to exceed 18.5 percent of the outstanding principal and interest at the time of the loan sale;

5) Reduce Collection Fees for Consolidation.

Collectors should not be making so much profit in excess of the costs of collection.

Suggested language: 20 U.S.C. § 1078(c)(6)(B)(I).
(I) not charge the borrower **reasonable and bona fide** collection costs in an amount in excess of 18.5 percent of the outstanding principal and interest of a defaulted loan that is paid off through consolidation by the borrower under this subchapter and part C of subchapter I of chapter 34 of Title 42;

6) Eliminate the 45% "Excess Consolidation Proceeds" Standard

The HEA (20 U.S.C. § 1078(c)(6)(C) requires guaranty agencies to remit the entire amount of the collection costs charged borrowers when a defaulted loan is paid off with excess consolidation proceeds. Excess proceeds are defined as the proceeds of consolidation loans received to pay defaulted loans that exceed 45% of the agency's total collections in that year.

This standard was created to prevent agencies from pressuring borrowers into consolidation. Times have changed and the policy now harms borrowers by discouraging agencies from counseling borrowers about consolidation.

C. Restore a safety net for ALL student loan borrowers

Key reforms include:

1) Eliminate offset of earned income tax credits (one of the most important programs that help working families keep working)

2) Eliminate Social Security offsets. Social Security helps give aging and disabled Americans peace of mind. Offsetting this lifeline is an extraordinary collection tool that should be eliminated. In the meantime Congress should increase the exempted amount from a flat $9,000/year to an amount that is sufficient for basic survival and tied to an annual index. The $9,000 limit has not been raised since the legislation was passed in the mid 1990's. It is even below the current poverty level for a single person of $11,490.

These recommendations require amendment of the Debt Collection Improvement Act, 31 U.S.C. § 3716 for Social Security offsets and 31 U.S.C. § 3720A for tax offsets.

3) Eliminate the three year reinstatement period for borrowers in the Social Security Medical Improvement Not Expected category.

The Department of Education recently amended the HEA regulations to allow borrowers to provide certain SSA determinations as presumptive proof of disability discharge. However, the Department did not eliminate the reinstatement period for these borrowers. This is in contrast to the V.A. process in which certain veterans may receive discharges without a three year reinstatement period.

This amendment is critical because based on Department reports and our experience representing borrowers, many disabled borrowers are not able to keep up with the paperwork requirements during the three year reinstatement period. Reinstating their loans denies them the opportunity to reapply for disability discharge and subjects them to potential tax consequences. Eliminating the reinstatement period for these most disabled borrowers will also save money by reducing unnecessary bureaucratic requirements and oversight.

Statute: Section 437(a) of the HEA, 20 U.S.C. § 1087(a))
Rename section 1087(a)(2), "Determination by the Secretary of Veterans Affairs" and add a new section (a)(3) and (4)

(3) Determination by the Social Security Administration-A borrower who has been determined by the Social Security Administration to be disabled and who provides documentation of such determination to the Secretary of Education, shall be considered totally and permanently disabled for the purpose of discharging such borrower's loans under this subsection, and such borrower shall not be required to present additional documentation for purposes of this subsection unless the Social Security Administration has determined that the borrowers medical condition is expected to improve and will review the borrowers medical condition not less than 6 months and not more than 30 months from the such of such determination.

(4) Reinstatement provisions—Borrowers who are discharged under paragraphs (2) and (3) (V.A. determination and SSA medical improvement not expected category) shall not be subject to any reinstatement provisions created by the Secretary.

4. Restore Bankruptcy rights for all student loan borrowers. This requires amendments to the Bankruptcy Code.

5. Restore a statute of limitations for federal student loans

The elimination of the statute of limitations for government student loans in the early 1990's placed borrowers in unenviable, rarified company with murderers, traitors, and only a few violators of civil laws. Despite the governmental and social interest in pursuing criminals, statutes of limitations apply to nearly all federal criminal actions. Among other reasons, statutes of limitations are essential because of the serious problems and abuses associated with adjudicating old claims. Further, the limitless pursuit of vulnerable student loan borrowers has serious human and financial costs.

D. Eliminate adverse tax consequences for Borrowers Receiving Administrative Discharges

Under current law, borrowers obtaining discharges due to disability or death (e.g. for parents surviving their children) face potential tax consequences while most other borrowers obtaining discharges do not. The current insolvency system is insufficient to protect many vulnerable borrowers. This likely requires amendments to the Internal Revenue Code. (See information sheet attached at Appendix A).

E. Create a more Efficient and Equitable Collection System

1) Eliminate private collection agencies from the dispute resolution role. Dispute resolution is not the primary mission of loan collection agencies. Debt collectors are not adequately trained to understand and administer the complex borrower rights available under the Higher Education Act, and the government does not provide sufficient oversight of their activities. There are certainly times when a borrower is uncooperative or has exhausted all options. In those cases, the loan holder may have no choice but to focus on collection efforts. Yet there are many borrowers who want to find a solution, but are stymied because they cannot get past the rude, harassing, and often abusive behavior of a collection agent.

Until such time as the government identifies viable alternatives to private collection agencies, we call on the Administration to issue a moratorium on using private collection agencies for student loan dispute resolution. Congress should also act to prohibit use of private debt collectors and create a pilot program to study the effectiveness of other debt collection techniques.

2) **Collection charges should be limited to only those fees that are bona fide and reasonable and actually incurred.**
As long as collection agencies are still employed to collect student loan debts, Congress should act to limit the profits they earn on the backs of borrowers. The government pays an estimated $1 billion in commissions to private collection agencies annually.[9]

The HEA currently provides only that collection fees must be reasonable. 20 U.S.C. § 1091a(b)(1). At a minimum, the statute should be amended to require that fees also be bona fide. Reasonable collection fees should be charged only when actual costs are incurred and in no case for government offsets or wage garnishments**.**

6. **Prohibit delegation of inherently governmental functions, such as conducting fair hearings, to third party debt collectors**

There is an inherent conflict of interest in allowing collection agency officials to conduct and make hearing decisions. The hearing judges must be neutral and independent. Congress should prohibit agencies from using their own personnel as judges in collection hearings for borrowers.

F. Relief for those harmed by predatory schools.

Through our work consulting with legal services and other attorneys across the country, as well as our direct representation work, we have seen a continuous stream of student loan borrowers who are struggling to pay 10, 20, and even 30-year old loans. The vast majority of these borrowers, including single parents, veterans, non-English speakers, first-generation students, and seniors – enrolled in for-profit schools in order to earn higher wages and improve the lives of themselves and their families. Too many of these schools, however, preyed on these borrowers' dreams by falsely promising high quality educations that would lead to high paying careers. By the time our clients reach us, their hopes and dreams have been shattered. Unable to find the employment promised, they face aggressive debt collection tactics for student loan debts they cannot afford to repay. Many of them have no way out.

A July 2013 *New York Times* article describes hundreds of borrowers (and maybe more) in New York City facing financial devastation due to loans incurred at a number of cosmetology schools that have been closed for years.[10] One of the borrowers summed up the trap she is in, "It would have been worth it", she said "for a school that gave me a future."

Although the Department of Education has recently worked at creating regulations designed to curb future abuses, these regulations do nothing to provide relief for the countless number of borrowers who have been harmed by fraudulent schools. The three main types of existing cancellations (or "discharges") that are intended to address fraud – closed school, false

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[9] John Hechinger, "Obama Relies on Debt Collectors Profiting from Student Loan Woe", Bloomberg (March 26, 2012).
[10] Emily S. Rueb, "Beauty School Students Left with Broken Promises and Large Debts", The New York Times (July 28, 2013).

certification, and unpaid refund cancellations – are narrowly defined and provide relief to only a small subset of harmed borrowers. These cancellations are not available to borrowers harmed by other kinds of deceptive practices, including those that are prohibited by federal regulation. For example, a school may routinely pay admissions officers by commission, fail to provide educational materials or qualified teachers, or misrepresent a student's likelihood of finding a job or earning a particular salary after completion.[11] All of these violations harm students, but none of them are currently included as grounds for student loan discharges.

Congress and the Department of Education can fill in these gaps by creating a fresh start relief program. For too long, the risk of predatory school practices has fallen almost entirely on individual borrowers, who were not in a position to discover fraud and police schools before they enrolled.

This approach has the twin virtues of relative simplicity and equity. Congress can authorize the Department to identify groups of borrowers eligible for relief by evaluating existing evidence regarding the deceptive and illegal practices of for-profit schools. In most cases the school practices, not the experiences of each individual borrower, would be the focus of the evaluation – thus creating a more efficient and less burdensome process for the government and a fairer process for the borrowers, who typically do not have access, outside of their own experiences, to evidence regarding their schools' fraudulent practices. In addition, a fresh start approach would reach borrowers who cannot benefit from the existing narrow discharge provisions, but who were subjected to illegal practices and likely did not receive the quality education they were promised. This approach would (1) benefit the maximum number of harmed borrowers; (2) save administrative time and therefore cost; and (3) free up governmental resources to more aggressively enforce existing regulations that would help curb deceptive practices and pursue parties with deeper pockets, to the extent that they still exist, i.e. problem schools, school owners, and related parties.

The Department currently has the authority to create this program AND to seek reimbursement for costs from violators. Existing authority includes:

- False certification and closed school discharge statute, 20 U.S.C. § 1087(c),
- Breach of contract actions based on contracts signed by school officials certifying compliance with the HEA,
- Violations of program participation agreements,
- Broad settlement and compromise authority in the HEA, particularly 20 U.S.C. § 1082(a) and other statutes including "Collection and Compromise" (31 USC § 3711).

The authority exists, but is not being used. We urge Congress to act through the reauthorization process to ensure that the Department creates this Fresh Start program.

[11] See 34 C.F.R. §§ 668.14(b)(22) (prohibiting the payment of incentive compensation for securing enrollments);); and 668.71(b) (prohibiting substantial misrepresentations, including about the nature of a schools' educational programs and the employability of its graduates).

The program should include tiers of discharges, including some that will occur automatically without borrower application. Others may require basic documentation from borrowers. In these cases, the Department could identify all borrowers in the eligibility category and send them a simpler, user-friendly application form.

In most cases, the Department would identify and automatically discharge the loans for all borrowers, without any need for the borrowers to submit applications or other information. In all likelihood a significant number of the low-income borrowers intended as primary beneficiaries of the fresh start may be difficult to locate. In addition, due to comprehension difficulty and years of harassment from collection agencies, many of these borrowers may not open yet another envelope from a government agency or respond to an application for discharge.

Below is a non-exhaustive list of "fresh start" categories:

1. Discharges Due to Pattern and Practice of Falsely Certifying Borrower or Program Eligibility

   Ability-to-Benefit (ATB) Violations: School had a pattern of enrolling students who did not have a high school diploma or equivalent and who did not demonstrate an ability to benefit as required by the HEA or regulations. All borrowers who enrolled in those programs while the school was violating ATB requirements should be deemed falsely certified.

   Falsifying Academic Progress, Disqualifying Status and Forgery Violations: Whenever there is evidence that a school engaged in any of these practices, students enrolled in the affected programs at the time of the violations should be deemed falsely certified if they provide a statement under oath of relevant facts.

2. Fresh Start for Collection Proof Borrowers and for Very Old Debts

   At a minimum, borrowers should be given a fresh start if they are of advanced age (to be determined, but possibly 75 years old or older) or if the debt is 20 years old or older. The program could include other relevant factors in other cases

   The program should also include an across-the-board standard to terminate collection activity and/or grant discharges on the ground of uncollectability, against borrowers who have no more than a certain income level or who have a particular income sources, such as public benefits – for example, if the borrower's adjusted gross income is at or below 150% of the federal poverty level or borrower receives public benefits, including food stamps, general relief, SSI, social security disability benefits, EITC.

3. Incentive Compensation Ban Violations:

   For time periods for which there is credible evidence that a school was paying its recruiters in violation of the incentive compensation ban, all programs offered by that school should be deemed ineligible and all borrowers who enrolled in those programs in that time period should receive discharges.

4. Substantial Misrepresentations:

Schools that engaged in a pattern of making substantial misrepresentations regarding transferability of credits, quality of instruction, facilities, or equipment, cost to complete the program, or future conditions of employment.

All students who enrolled at the time the substantial misrepresentations were occurring should qualify for a fresh start. Borrowers should be presumptively eligible if they certify under oath basic elements and there is no evidence contradicting the borrower's sworn statement or disputing their credibility.

5. Closed Schools or Discontinued Programs

All borrowers should automatically qualify for a fresh start if they were in attendance within one year prior to a school closure or, when there are multiple branches or campuses that close on different dates, one year prior to their branch or campus closure. In addition, if a program is terminated before students have completed, then all students in attendance at the time of program termination should qualify for discharge.

Closure and/or program termination is usually preceded by an extended period of decline and diminished services. In anticipation of closing, financially troubled schools most often cut back on equipment, maintenance, teacher salaries, and living expense "stipends" to the students, over a period of time prior to actually padlocking the school doors. Often in an effort to scale back operations and cut costs, certain programs may be eliminated before the school terminates all programs.

The Department should identify all borrowers who were attending within the established time period and discharge their loans.

6. Judgments and State Law Violations

Students who have secured judgments against schools based on HEA, regulation or state law violations, but who are unable to collect from the school or other sources (such as state student tuition reimbursement funds), should qualify.

G. Ensure Access to Justice for Borrowers

1) Private Right to Enforce the HEA

As the recent U.S. Senate HELP committee investigations show, federal and state enforcement of HEA requirements has been generally lax. While government enforcement is important, borrowers cannot rely on public actions to get relief. Congress must act to ensure that borrowers have private enforcement rights, not only to challenge predatory school practices, but also servicer and collector abuses. This requires amending the HEA to create an explicit private right of action.

Congress has created many new and improved options for borrowers. The Department of Education also signs numerous contracts with servicers and collectors to provide essential services. Theoretically, these entities could lose their contracts if they do not comply with the law. Even if this occurs, there are no provisions requiring relief for borrowers harmed by these practices. For example, what happens if the lender, guaranty agency or school refuses to discuss loan rehabilitation even when a borrower clearly has a right to such a plan? Currently the borrower can complain to the Department of Education. Given documented problems with the Department's oversight, this is less than a complete solution even for those borrowers who persist and manage to speak to someone. Beyond complaining, it is virtually impossible for a borrower to enforce her rights.

The lack of private enforcement shuts the door on borrowers seeking to access programs that they are entitled to under the Higher Education Act. This glaring problem also undermines the effectiveness of new borrower-friendly programs because loan holders and servicers are not held accountable when they fail to comply with the law.

2) Ban Mandatory Arbitration Clauses

Another barrier to justice is the widespread use in school enrollment agreements of mandatory arbitration clauses. Congress can ban such clauses for schools receiving federal aid funds.

3) Amend Direct Loan Claims and Defenses Statute

To provide Direct Loan borrowers the same rights to bring school-related claims and defenses against the government as FFEL borrowers have. We recommend amending the Direct Loan statute to clarify that borrowers can bring affirmative claims as well as defenses and that claims may be brought under federal and state law. This is critical to ensure that borrowers do not have to wait for collection actions to raise these claims. The change also addresses the current situation in which it is extremely difficult for borrowers to raise violations of the federal HEA in their state law claims. In effect, this means that a borrower has no legal recourse if she is harmed by a recruiter violation of incentive compensation regulations or by a school misrepresentation. The school may suffer some consequences, but the borrower is left with no relief. The administrative discharges, such as false certification, only provide relief for a limited number of these borrowers.

Suggested Statutory Change

20 U.S.C. § 1087e

h) Borrower claims and defenses

Notwithstanding any other provision of State or Federal law, the borrower may assert as an affirmative claim or defense against repayment, any act or omission of the institution of higher education attended by the borrower that would give rise to a cause of action against the institution under the Higher Education Act, other federal laws, or applicable state law, except that in no event may a borrower recover from the Secretary, in any action arising from or relating to a loan made under this part, an amount in excess of the amount such borrower has repaid on such loan.

H. Mandate Research and Innovation

One way to improve efficiency is to conduct more empirical research and pilot projects to find out what works. According to New America, higher education generally suffers from a lack of rigorous experimentation, both in terms of practice and policy.[12]

In addition to research mandates, Congress should require the Department of Education to release data about key federal aid metrics including extensive default rate information, effectiveness of post-default programs, costs of collection, commissions to collectors and servicers, and other critical information. .

Giving borrowers a chance to get back in good standing may be less costly in many cases than the relentless gauntlet of collection tactics. We particularly need more information about the costs of the Department's collection programs.

Some cynically argue that default rates should not be a major concern because government collection rates are so high that there is no cost to taxpayers. Nexus Research, an organization funded by Apollo Group (owner of University of Phoenix) stated in a 2010 presentation that there is no net loss to the government from their students' defaulted loans.[13] Among other problems, this view ignores the extraordinary human costs of default. Further, the premise that there is no financial cost to defaults is highly debatable. By most accounts, the government has an extraordinarily high collection rate, but does not profit from collection if the costs are taken into account.[14]

I. Create counseling assistance resources for financially distressed borrowers that are not tied to lenders or guaranty agencies and get rid of collection agency involvement in collecting federal student loans.

[12] Stephen Burd, Kevin Carey, Jason Delisle, Rachel Fishman, Alex Holt, Amy Laitinen, and Clare McCann, New America Foundation, "Rebalancing Resources and Incentives in Federal Student Aid" (Jan. 2013).

[13] Jorge Klor de Alva, "For-Profit Colleges and Universities: America's Least Costly and Most Efficient System of Higher Education: Case Study--University of Phoenix" Nexus Research & Policy Center (August 2010), Slide 39.

[14] See generally Jason Delisle, "President's Budget Shows Student Loan Defaults Cost Taxpayers." New America Ed Money Watch (Feb. 16, 2012).

The current patchwork of complex student loan programs leaves many borrowers feeling bewildered when they try to resolve student loan problems. In too many cases, they are stuck dealing with a collection agency that does not have the borrower's best interests in mind. At the same time, precious government resources are funneled to collection agencies.

This should include using all available tools to crack down on unscrupulous student loan debt relief companies.[15]

J. Use HEA Authority to Provide Relief for Private Loan Borrowers

Much of the statutory authority for private lending is outside of the HEA. However, the government can use the HEA as an oversight tool to protect private loan borrowers attending schools that receive Title IV funds. We recommend using this tool to require private loan certification. As part of the certification process, schools should be prohibited from certifying loans that fail to provide basic consumer protections such as death and disability discharges.

Thank you for your consideration of these recommendations. Please contact Deanne Loonin (dloonin@nclc.org;617-542-8010) with questions or comments.

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[15] See generally National Consumer Law Center, "Searching for Relief: Desperate Borrowers and the Growing Student Loan 'Debt Relief' Industry" (June 2013).

Appendix A

Ensuring that Student Loan Death and Disability Discharges Do Not Result in a Tax Penalty

Exempting federal student loans discharged because of death or total and permanent disability from cancellation of debt income would ensure fairer tax treatment for some of the most vulnerable student loan borrowers.

1. **Borrowers should not be worse off after a total and permanent disability or death discharge than they were before.**

2. **The budgetary impact of exempting death and disability discharges from income is likely negligible.** A relatively small number of borrowers have their student loans discharged for death or disability each year. Most have little or no resources to pay these unexpected tax bills. Thus, the government gains little by trying to collect taxes from these borrowers. Yet, the impact to those who will be taxed will likely be profound.

3. **There is no evidence to suggest that borrowers who receive these discharges are hiding (or even own) significant assets.**

4. **Insolvency is insufficient to protect many vulnerable borrowers.** In general, the Internal Revenue Code allows taxpayers to exclude canceled debt from their income to the extent that the taxpayer was insolvent immediately prior to the discharge. The amount of canceled debt that is excludable is calculated by finding the excess of liabilities (total debts owed) over the fair market value of any assets. However, the insolvency provision does not distinguish between assets that are essential (such as a primary residence or transportation) and other assets. Borrowers get disability discharges because they have no future earning potential. We should not require them to give up the assets necessary to maintain basic necessities. In addition, many vulnerable borrowers are not aware of the insolvency exception.

Examples of the impact of tax consequences:[1]

Borrower 1: Helen

Helen is a single mom. Her 20 year old son died in a car accident in 2012. Helen has three surviving children under the age of 18. She took out $40,000 in ParentPLUS loans so that her son could go to the state university. Helen works in a call center making $35,000 per year and receives no child support from the father of her children. She owns a home that she purchased with her ex-husband 15 years ago. It is now worth $100,000 and has $30,000 remaining on

[1] These examples assume that the amount reported on the 1099-C is for the full amount of the principal, interest, and fees. It also assumes that each of these borrowers claims the full $2500 student loan interest deduction.

mortgage. She also owns a car worth $5,000. (Total assets: $100,000 (home) + $5,000 (car) = $105,000).

Because of Helen's assets, she does not qualify for the insolvency exception. Without the cancellation of debt (COD) income, Helen would have qualified for approximately $2,110 in the Earned Income Tax Credit. She would not owe any taxes and would have received a refund of approximately $1,247. With the COD income, she no longer qualifies for the EITC and must pay $6,801 to the IRS.

	Loan Balance Discharged	Total Asset Value	Total Debt	Extent of Insolvency *(Debt – Assets)*	Amount of loan to be included in income *(Debt – Insolvency)*	Estimated AGI	Estimated Tax Liability	Tax Liability w/o Cancellation of Debt Income
Helen	$40,000	$105,000	$70,000	0	$40,000	$72,500	$6,801	-$1,247 (refund)

Borrower 2: Linda

Born in 1946, Linda receives $831 per month in SSI/SSDI. She has a small single family house valued at $115,000 in a low-income suburb of Boston, Massachusetts that she inherited from her father in 1985. She originally borrowed $25,000 in 1990 to attend a trade school.

A spinal injury in 1998 left her totally and permanently disabled. Struggling to pay off her student loan, her balance has ballooned to $58,450. In 2012, her loans were canceled.

After paying for her living expenses (utilities, co-pays and prescriptions, transportation, groceries, and incidentals) Linda has $20 left at the end of the month.

Because of the value of her home, Linda will not qualify for the insolvency exception and will owe $7,586 to the IRS.

	Loan Balance Discharged	Total Asset Value	Total Debt	Extent of Insolvency *(Debt – Assets)*	Amount of loan to be included in income *(Debt – Insolvency)*	Estimated AGI	Estimated Tax Liability	Tax Liability w/o Cancellation of Debt Income
Linda	$58,450	$115,000	$58,450	0	$58,450	$55,950	$7,586	$0

Borrower 3: Paul

Paul is a 50 year old disabled veteran. He has a service-connected disability that is 100% disabling. He receives $800 per month in VA disability benefits. He purchased a home in Rochester, New York in 1989 that is now paid off. It is currently valued at $50,000. Before entering the service, he attended a small private college, but never finished. His student loan debt was $60,000 when it was discharged.

Although Paul is insolvent, the extent of his insolvency is only $10,000 ($60,000 - $50,000) and does not relieve him of the tax consequences of his loan cancellation.

	Loan Balance Discharged	Total Asset Value	Total Debt	Extent of Insolvency *(Debt – Assets)*	Amount of loan to be included in income *(Debt – Insolvency)*	Estimated AGI	Estimated Tax Liability	Tax Liability w/o Cancellation of Debt Income
Paul	$60,000	$50,000	$60,000	$10,000	$50,000	$47,500	$5,474	$0

For all of these borrowers, the cancellation of debt income will likely have collateral consequences. In order to pay the tax liability, these borrowers may need to sell their homes. Borrowers with loans canceled due to death or disability are already vulnerable. This added tax burden threatens their limited stability and resources.