Testimony before the

U.S. Senate Judiciary Subcommittee on Administrative Oversight and the Courts

"The Looming Student Debt Crisis: Providing Fairness for Struggling Students"

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The National Consumer Law Center (NCLC) thanks the Committee for holding this hearing and inviting us to submit this testimony on behalf of our low-income clients. The National Consumer Law Center is a nonprofit organization specializing in consumer issues on behalf of low-income people. We work with thousands of legal services, government and private attorneys, as well as community groups and organizations that represent low-income and older individuals on consumer issues.[1] NCLC's Student Loan Borrower Assistance Project provides information about student loan rights and responsibilities for borrowers and advocates. We also seek to increase public understanding of student lending issues and to identify policy solutions to promote access to education, lessen student debt burdens and make loan repayment more manageable.[2]

In my work as the Director of NCLC's Student Loan Borrower Assistance Project, I provide training and technical assistance to attorneys and advocates across the country representing low-income student loan borrowers. I have written numerous reports on student loan issues as well as NCLC's *Student Loan Law* publication. I also provide direct representation to low-income borrowers through Massachusetts-based legal services and work force development organizations. Many of these borrowers seek assistance because they are trying to rebuild their lives after escaping domestic violence or homelessness. The non-profit work force development organizations help them get G.E.Ds if necessary and hopefully move on to higher education. However, many cannot take this next step because of prior student loan debt. I also have daily contact with a wide range of borrowers through our student loan web site. Because of my extensive experience representing student loan borrowers and working on student loan matters, I have served as the legal aid representative at a number of Department of Education negotiated rulemaking meetings, including the current "Loans team" session. My testimony is based on this work and previous work representing low-income consumers at Bet Tzedek Legal Services in Los Angeles.

Introduction

Investment in education can be one of the best financial decisions consumers make. Unfortunately, it can also be the beginning of a lifetime of burdensome debt. As college costs

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[1] In addition, NCLC 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.).
[2] *See* the Project's web site at http://www.studentloanborrowerassistance.org.

rise in a tight economy, a growing number of student borrowers end up with staggering debt burdens that they can never escape.

Students go to college to improve their lives. Unfortunately, not everyone succeeds, especially not financially. Far too many never graduate. Many who do graduate are unable to find work to repay burdensome debt loads.

It is increasingly difficult for students to figure out how to pay for college. Tuition keeps growing while scholarship and grant aid shrinks. A growing number of students must rely on loans to finance their educations. The increased borrowing is not only from federal loans. The borrowing limits in the federal loan programs, the skyrocketing cost of higher education and aggressive lender marketing have fueled the growth of private student loans, which are almost always more expensive than federal loans.

Despite the growing perils of trying to pay for college, Congress has consistently weakened the safety net, including bankruptcy, for those who try, but end up unable to repay their education debts. Our experience working with low-income borrowers is that bankruptcy is almost never their first choice. Most express a desire to avoid bankruptcy because it feels like a failure. They also fear the stigma and the resulting difficulties of finding employment and housing. However, for many, bankruptcy is the only way to get a fresh start in life.

Bankruptcy is not and should not be the entire safety net, but it is the most organized and effective system we have to offer relief to those who 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 and is still fully available to nearly all other unsecured debtors. For student loan debtors, however, bankruptcy relief 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.

The New York Federal Reserve Board reported in March 2012 that outstanding student loan debt stands at about $870 billion, higher than total credit card balances ($693 billion) and total auto loan balances ($730 billion).[3] The Board noted that student loan balances are expected to continue this upward trend.

It is not just the amount of outstanding debt that causes concern, but the growing delinquency and default rates. Our testimony focuses on the social, economic and human toll of these staggering debt burdens and defaults. Just as college costs are increasing and grant aid has declined, policymakers have chosen over time to punch major holes in the safety net for borrowers. Congress has eviscerated bankruptcy rights for federal and private student loan borrowers. On the federal loan side, Congress and various Administrations have instituted tax refund intercepts (including EITC seizures), eliminated the statute of limitations, initiated administrative wage garnishment and Social Security offsets, and expanded use of private collection agencies. This conscious destruction of the safety net has occurred just as enrollment in higher education continues to skyrocket, college costs are rising exponentially and the income gap in this country continues to grow.

[3] Federal Reserve Bank of New York, "Grading Student Loans" (March 5, 2012).

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 society as well. Beyond the benefits for individuals, there are a broad range of social gains from a more educated population. The College Board publishes research on the benefits of higher education, including not just higher earnings for individuals, but also less reliance on public benefits among those with more education, better health, and higher voting and volunteering rates.[4]

As evidenced by the Obama Administration's higher education goals, it is in our national interest for more people to get post-secondary education or training. If public policies only encouraged safe choices, few would borrow to go to college. Few would start businesses either. Most businesses fail, even those started by those who have previously run successful businesses. Yet we have decided as a society that we want people to start businesses even if this means writing off some bad debt. The same principle should apply to education.

Student Loan Defaults and Delinquencies Harm Borrowers, Society and the Economy

Private Student Loans

There are limits on how much students can borrow through most of the federal student loan programs. However, some students and their families borrow more by taking out private student loans. Some take out private loans because they are not aware of the federal student loan programs or incorrectly believe they are not eligible for federal loans or that the private loans are better deals. This often occurs because of aggressive private student loan marketing or borrower confusion about loans. The Project on Student Debt found that the majority (52%) of private loan borrowers in 2007-08 borrowed less than they could have in Stafford loans.[5]

The College Board reports that after peaking at 25% of total education loan volume in 2006-07, nonfederal loans declined to 8% of the total in 2009-10 and 7% in 2010-11. [6] More recently, however, lenders have reported a return to growth and increased competition.

Unfortunately, many private student loans are high cost loans that borrowers cannot repay or are in amounts far in excess of the student's ability to repay with anticipated income. Many of the most expensive private student loans are made to for-profit school students. These loans default at staggering levels.

A high percentage (about 70 -75%) of the clients we represent through NCLC's Student Loan Borrower Assistance Project 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.[7] 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

[4] College Board, "Education Pays 2010" (2010).
[5] The Project on Student Debt, "Private Loans: Facts and Trends" (July 2011).
[6] CollegeBoard, "Trends in Student Aid 2011" (2011).
[7] The Project on Student Debt, "Private Loans: Facts and Trends" (July 2011).

in 2007-08.[8] In 2007-08, for-profit school students comprised about 9% of all undergraduates, but 27% of those with private loans.[9]

The private student loan industry generated huge profits for lenders and investors for many years. The private loan market was profitable largely because originators sold the loans with the intention of packaging them for investors. Prior to the credit crisis, private student lenders engaged in many of the same predatory practices as occurred in the subprime mortgage market. Not surprisingly, the industry began to crash once it could no longer rely on passing off dubious loans through the securitization process. Defaults and delinquencies ballooned during this time and continue to be a major problem.

Moody's acknowledged in early 2010 that the high default rates for private loan securitizations reflected weak underwriting, referring in this case to the 2006-07 period.[10] "Non-traditional" students or those attending "non-traditional" schools had a large portion of the defaulted loans, but many students graduating from traditional colleges and universities have also struggled under unsustainable loan burdens.

Fitch Ratings reported in July 2011 that losses for private student loans continue to increase. [11] According to Moody's, the private student loan default rate in the most recent quarter was about 5.1%, double what it was before the recession.[12]

To compound the pain for borrowers, as the subprime student loan market contracted, many for-profit schools began to develop their own products. As documented in NCLC's January 2011 report, the default rates on these school loan products are shockingly high.[13] Corinthian Colleges, for example, has told investors that it expects its students will not be able to repay 56-58% of its institutional private loans.[14] 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.[15]

As has occurred with the failed mortgage lending market, high student loan write-off and default rates block economic recovery. This is a particularly critical time for policymakers to provide relief for student borrowers <u>and</u> ensure that the private student loan market that emerges from the credit crisis is fair and efficient.

Federal Student Loans

There has also been a steady increase in federal student loan default rates in recent years. Even using the limited official cohort default rate, which only tracks borrowers for a few years,

[8] Id.
[9] Id.
[10] Student Lending Analytics Blog, "Moody's Outlook for Student Loan Securities: Expect Negative Credit Trends for Private Loans in 2010" (Jan. 29, 2010).
[11] Fitch Ratings, "The Student Loan Report Card "(July 2011).
[12] Don Lee, "Report on College Loan Delinquency Rate Raises Alarms," Los Angeles Times (March 5, 2012).
[13] National Consumer Law Center, "Piling It On: The Growth of Proprietary School Loans and the Consequences for Students," (January 31, 2011).
[14] Id.
[15] Id.

default rates are growing. According to the most recent data, 8.8% of federal student loan borrowers who entered repayment in 2009 had defaulted by the end of 2010, up from 7% for those entering repayment in 2008. For-profit colleges continue to have the highest two-year default rates, with a 15% cohort default rate for borrowers entering repayment in 2009. [16]

These rates only show loans that went into default. The full scope of student loan problems is more accurately portrayed by examining delinquency rates as well. In a 2011 report, the Institute for Higher Education Policy found that more than one-fourth of the borrowers in their study who entered repayment in 2005 became delinquent on their loans at some point, even though they did not default. [17]

The consequences of federal loan default are particularly severe. The government has extraordinary powers to collect student loans, far beyond those of most unsecured creditors. The government can garnish a borrower's wages without a judgment, seize his tax refund, even an earned income tax credit, seize portions of federal benefits such as Social Security, and deny him eligibility for new education grants or loans. Even in bankruptcy, most student loans must be paid. Unlike any other type of debt, there is no statute of limitations.

Borrowers who are current on their loans suffer from high debt burdens as well. Flexible repayment programs such as income-based repayment allow federal loan borrowers with limited incomes to make very low payments. This is extraordinarily helpful in preventing the worst consequences of default, but many of these borrowers are not making much if any progress toward paying off their loans. In some cases, payments do not even cover the interest that accrues monthly. Among other problems, this can impede asset building since creditors avoid lending to consumers with high debt-to-income ratios. Those in default face even graver credit reporting consequences.

The Diverse Student Borrower Population

The debate about student loan debt generally spotlights the struggles of young college graduates. There is no question that the problems faced by these "traditional" students are critical and should be addressed in policy reform. However, focusing exclusively on this population ignores the fact that the majority of students are "non-traditional," meaning that they are working adults over 25 or otherwise financially independent.

Despite the term "non-traditional," these students greatly outnumber traditional students. Low-income students are even more likely to fit the non-traditional profile and more likely to rely on student loans than their high or middle income traditional student peers.[18]

[16] The Project on Student Debt, "Sharp Uptick in Federal Student Loan Default Rates" (Sept. 12, 2011).
[17] Alisa F. Cunningham, Gregory S. Keinzl, Institute for Higher Education Policy, "Delinquency: The Untold Story of Student Loan Borrowing" (March 2011).
[18] U.S. Dep't of Educ., Nat'l Center for Educ. Stat., "Characteristics of Undergraduate Borrowers: 1999–2000" at 13-14 (Jan. 2003).

The population of student loan borrowers is diverse. Our low-income clients, for example, include very young individuals who are often in financial trouble because they were unable to complete school or completed a program that did not prepare them for employment. We also represent single parents in their 30's and 40's as well as borrowers in their 80's or 90's. Many come to us for assistance because they want to go back to school and improve their employment prospects. Some of our clients are severely disabled or otherwise cannot work. The government is still hounding these borrowers, in many cases taking away portions of their Social Security lifelines.

Non-traditional borrowers are at high risk of default for a variety of reasons, including lower completion rates.[19] Many individuals delayed enrolling in school and worked to save money to finance education. Others worked during school to defray costs. These well-intended decisions unfortunately are correlated with higher withdrawal rates. In addition, students who attend for-profit or two year community colleges are more likely to default as well as those who do not have high school diplomas. Older students are also more likely to default as well as some borrowers of color. Low parental educational attainment is another risk factor. Most of these risk factors closely track the defining characteristics of non-traditional students.

We must reset our policy priorities so that these borrowers are given the opportunity for a fresh start, to finish school, and hopefully climb the economic ladder.

Restore Bankruptcy Rights for Student Loan Borrowers

Current bankruptcy law treats students who face financial distress the same severe way as people who are trying to discharge child support debts, alimony, overdue taxes and criminal fines. The current undue hardship system is arbitrary and unfair and denies relief to the most vulnerable student loan borrowers.

This harsh treatment of students in the bankruptcy system was built on the false premise that students were more likely to "abuse" the bankruptcy system. Yet there is no evidence and has never been any evidence to support this assumption.

When first considering this policy, Congress commissioned a Government Accountability Office (GAO) study on the topic which found that only a fraction of 1 percent of all matured student loans had been discharged in bankruptcy. The House report summarized the GAO's findings:

> First, the general default rate on educational loans is approximately 18%. Of that 18%, approximately 3-4% of the amounts involved are discharged in bankruptcy cases. Thus, approximately ½ to ¾ of 1% of all matured educational loans are discharged in

[19] See generally Mary Nguyen, "Degreeless in Debt: What Happens to Borrowers Who Drop Out", The Education Sector (February 23, 2012).

bankruptcy. This compares favorably with the consumer finance industry. [20]

Congress acknowledged the pressure from the anecdotal reports of abuse. For example, a 1977 House Report on this issue stated that:

> The sentiment for an exception to discharge for educational loans does not derive solely from the increase in the number of bankruptcies. Instead, a few serious abuses of the bankruptcy laws by debtors with large amounts of educational loans, few other debts, and well-paying jobs, who have filed bankruptcy shortly after leaving school and before any loans became due, have generated the movement for an exception to discharge. In addition, a high default rate has been confused with a high bankruptcy rate, and has mistakenly led to calls for changes in the bankruptcy laws.[21]

Despite the shaky foundation, Congress ignored the study and instead chose to make it more and more difficult for student loan borrowers to get a fresh start through bankruptcy. As Representative O'Hara noted in fighting student loan nondischargeability in the 1970's, "No other legitimately contracted consumer loan, applied to a legitimate undertaking is subjected to the assumption of criminality which this provision applies to every educational loan."[22]

After a series of changes which eliminated borrower rights, the final blow to students came in 2005 when Congress included private student loans in the non-dischargeability category. Congress made this change even though private student loans are not part of the federal financial aid system, which was created to promote equal access to higher education.

Even those who insist without evidence that students are more likely to file bankruptcy should be able to agree that the general changes made to the bankruptcy laws in 2005 address this issue. Congress added a number of new elements to the personal bankruptcy system in 2005, such as a means test and counseling requirements that make it more difficult for all consumers to file bankruptcy, especially those who have assets to pay their debts. In any case, the Bankruptcy Code has always included safeguards to prevent discharge in cases where a debt is obtained through false pretenses or fraud.

People who borrow to pay for education are trying to improve their financial situations, not ruin them. There is simply no evidence that less restrictive bankruptcy policies will lead to borrowers "irresponsibly" taking out loans that they know they cannot repay. Default is not something that anyone seeks out. Financial distress is also not something that anyone seeks out, but it happens. In this difficult economy, we know that people are struggling, including many who had been entrenched in middle class jobs. Bankruptcy may be the only option for many of these individuals.

In addition, bankruptcy provides the most complete relief for financially distressed borrowers. For example, borrowers who discharge debt in bankruptcy are not liable to pay any

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[20] H.R. Rep. 95-595, 1st Sess. 1977, 1978, 1978 U.S.C.C.A.N. 5963, 6094, 1977 WL 9628.
[21] Id.
[22] H.R. Rep. No. 94-1232 (1976) and H.R. Rep. No. 95-595 at 149 (1977), quoted in John A.E. Pottow, "The Nondischargeabilty of Student Loans in Personal Bankruptcy Proceedings: The Search for a Theory" (March 2007).

taxes for the amounts written off. This is in sharp contrast to many of the federal student loan discharge programs, including the disability discharge, which come with potential tax consequences. The income-based repayment program for federal loans is a very useful program, but unlike bankruptcy, there are potential tax consequences and under current law, borrowers do not obtain discharges until 25 years have passed. During this time, borrowers face numerous operational barriers that may prevent them, in some cases through no fault of their own, from staying on these relief programs. These barriers arise, among other reasons, because the government delegates dispute resolution authority to private collection agencies.

"Undue Hardship" and Lack of Relief

The current "undue hardship" system is random, arbitrary and unfair. Under current law, most federal and private student loans can only be discharged if the debtor can show that payment will impose an undue hardship on the debtor and the debtor's dependents. The student must seek the hardship determination in court through a separate proceeding.

The system is strikingly arbitrary. Judges are granted extraordinary discretion to make these decisions, especially since the Code provides no definition of "undue hardship." Professors Pardo and Lacey have studied this issue and found a high degree of randomness in the application of the undue hardship test.[23] They also found that students seeking bankruptcy relief were in fact suffering financial distress, concluding that judicial discretion has come to undermine the integrity of the undue hardship system.[24]

At this point, nine circuits use the so-called *Brunner* test to evaluate hardship.[25] This test requires a showing that 1) the debtor cannot maintain, based on current income and expenses, a "minimal" standard of living for the debtor and the debtor's dependents if forced to repay the student loans; 2) additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and 3) the debtor has made good faith efforts to repay the loans.

In recent years, many judges have recognized the random and unfair application of this "test." According to the Tenth Circuit, many courts have "…constrained the three *Brunner* requirements to deny discharge under even the most dire circumstances."[26] The court further noted that this overly restrictive application fails to further the Bankruptcy Code's goal of providing a "fresh start" for the honest but unfortunate debtor.[27] In criticizing the test, another judge noted that *Brunner* was "…made up out of whole cloth anyway."[28] Among other nearly

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[23] See Rafael I. Pardo & Michelle R. Lacey, "Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt," 74 U. Cin. L. Rev. 405 (2005); Rafael I. Pardo, Michelle R. Lacey, "The Real Student-Loan Scandal: Undue Hardship Discharge Litigation," 83 Am. Bankr. L.J. 179 (Winter 2009).
[24] Id.
[25] *Brunner v. New York State Higher Educ. Servs. Corp.*, 831 F. 2d 395 (2d Cir. 1987).
[26] *ECMC v. Polleys*, 356 F. 3d 1302 (10th Cir. 2004).
[27] Id.
[28] *In Re Cummings*, 2007 WL 3445912 (Bankr. N.D. Cal. Nov, 13, 2007).

impossible barriers, the test forces borrowers to prove a negative—they must somehow prove that their future is as hopeless as their present.

Other courts have taken the *Brunner* test to the extreme of requiring that a borrower show a "certainty of hopelessness." In rejecting this analysis, some courts have blamed its widespread use on an erroneous reading of *Brunner*.[29]

The current system is stacked against the most financially distressed borrowers. These borrowers have few, if any, resources to pay for legal assistance to prove to judges that they suffer from undue hardship. Yet competent legal assistance is one of the key factors in determining whether a borrower will successfully get a discharge.[30]

Most bankruptcy courts are even unmoved by borrowers who went to fraudulent schools. Judges have struggled to fit the concept of "educational benefit" into the undue hardship analysis even in cases where the school closed while the borrower was in attendance or was otherwise a sham school.[31]

The Business Impact of Student Loan Bankruptcy Policy

Many creditors argue 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.

It is certainly true that private student loans, made without government guarantees, can be risky for both creditors and borrowers. Many students are young, with little or no credit history. Their earning power is mostly speculative. Yet responsible underwriting of student loans is not impossible. Recent trends in the industry show that creditors know how to sell less risky products and still generate profits.

The fact is that the private student loan industry grew rapidly during the pre-2005 period when these loans were fully dischargeable in bankruptcy. This should not be so surprising. During the past decades of irresponsible lending, creditors threw credit around like candy even where the credit was dischargeable in bankruptcy (such as credit cards) and those where it was harder to write off debts in bankruptcy.

The private student loan industry has contracted in recent years even with a restrictive bankruptcy policy. The more restrictive 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, a welcome market correction.

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[29] *In re King*, 368 B.R. 358 (Bankr. D. Vt. 2007).
[30] Rafael I. Pardo, Michelle R. Lacey, "The Real Student-Loan Scandal: Undue Hardship Discharge Litigation," 83 Am. Bankr. L.J. 179 (Winter 2009).
[31] *See, e.g., In re Gregory* 387 B.R. 182 (N.D. Ohio 2008) (relief on the basis of fraud can be had only against those who are shown to be parties to the fraud).

There is simply no good evidence that bankruptcy policy has much impact on 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.

The business of private lending has expanded and contracted based on market opportunities, not based on bankruptcy policy. Some lenders continue to make high rate, risky loans even during the current economic climate. While some of the larger lenders have at least temporarily tightened criteria, other, less selective lenders have stepped into the market. In some cases, for-profit schools are making private loans knowing that the majority of their students will not be able to repay. Corinthian Colleges, for example, has told investors that it expects its students will not be able to repay 56-58% of its institutional private loans.[32] Yet it keeps making these loans, even with a restrictive bankruptcy policy, presumably because the loans lure students to its schools and gives it access to federal student aid dollars.

Further, there is no evidence that restoring bankruptcy rights will negatively impact college enrollment by limiting access to funds. In fact, enrollment is at record highs even though the private student loan industry has contracted after the credit crisis.

Lack of Non-Bankruptcy Alternatives: Private Student Loans

The current bankruptcy policy might not be so harsh if borrowers had ample non-bankruptcy alternatives to address student loan problems. Given their role in creating the recent economic crash, it is reasonable to expect lenders to do everything possible to help borrowers with unaffordable loans. Distressingly, this has not occurred. In NCLC's experience representing borrowers through the Student Loan Borrower Assistance Project, we have found private lenders to be inflexible in granting long-term repayment relief for borrowers. Lenders that had no problem saying "yes" to risky loans are having no problem saying "no" when these borrowers need help. [33] These lenders rarely cancel loans or offer reasonable settlements. We found that the lenders require very large lump sums to settle debts even from borrowers with very low incomes.

Fundamentally, lenders who make private student loans are not <u>obligated</u> to offer repayment modification or relief under any circumstances, leaving borrowers truly at the mercy of their lenders. We have found that even when lenders do offer some flexibility, these are usually short-term interest-only payments plans that do not extend loan terms.

The options are particularly limited for borrowers in default. We are told again and again that once a loan has been written off, there is nothing the lenders can do. 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.

[32] Consumer Law Center, "Piling It On: The Growth of Proprietary School Loans and the Consequences for Students," (January 31, 2011).
[33] National Consumer Law Center, "Too Small to Help: The Plight of Financially Distressed Private Student Loan Borrowers" (April 2009), aavailable on-line at: http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/TooSmalltoHelp.pdf.

Yet these are generally the borrowers most desperate for assistance. This is also in sharp contrast to the federal student loan programs where borrowers in default have various ways to select affordable repayment plans and get out of default.

Private student loan creditors may offer flexible payment arrangements to borrowers not yet in default, but they are not required to do so. None of the loan notes we surveyed in s 2008 report specifically provided for income-based repayment.[34] 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.

For example, we recently had a client with six private student loans from National Collegiate Trust (serviced by AES). He has private student loans from other lenders as well. Our client had already exhausted available hardship forbearances. His modified repayment plan option required a payment of $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.

These are just a few e-mails we have received through our web site helping to illustrate the human toll of the “no relief” policy:

> **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.”
>
> **Borrower in Turner Falls, MA**: “I’m writing to support: H.R. 2028: Private Student Loan Bankruptcy Fairness Act of 2011.
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> “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…
>
> “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).

[34] See National Consumer Law Center, “Paying the Price” The High Cost of Private Student Loans and the Dangers for Student Borrowers” (March 2008), available at: http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/Report_PrivateLoans.pdf.

> "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."

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 or Congress to come up with a win-win solution.

The recent private student loan complaint system established by the Consumer Financial Protection Bureau (CFPB) is a promising development. [35] This system, among other benefits, will help policymakers track the most common types of complaints and borrower responses. The CFPB has committed to reporting to Congress about the complaints it receives and to provide recommendations to improve relief for borrowers.

Appendix A, attached to our testimony includes recommendations we recently submitted to the CFPB in response to a request for comments. The recommendations focus on protecting borrowers and ensuring fair lending in the private student loan market.[36]

Lack of Non-Bankruptcy Alternatives: Federal Student Loans

The good news for federal student loan borrowers is that there are numerous options available if they are having trouble repaying student loans, including limited cancellation rights. The bad news is that these programs are underutilized and not well publicized. There are many operational barriers to access. For example, in the case of defaulted borrowers, collection agencies often provide inaccurate information about borrower rights.

Improving relief requires additional legislation as well as improved operations at the Department of Education. The Department of Education can go a long way toward providing greater relief by making sure that existing programs such as income-based repayment are implemented fairly and efficiently. The Department must make similar changes to improve rehabilitation and consolidation, the two main ways for borrowers to get out of default through repayment. Both programs are flawed in design and in execution.[37]

It is also critical to strengthen the various federal student loan cancellation/discharge programs and enact targeted legislative change as needed. The three cancellations (or "discharges") intended mainly to address fraud are closed school, false certification, and unpaid refunds. It is important to emphasize that not one of these programs provides general remedies

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[35] Rohit Chopra, Consumer Financial Protection Bureau, "Our Student Loan Complaint System is Open for Business" (March 5, 2010).

[36] See also National Consumer Law Center, "Comments to the Consumer Financial Protection Bureau on Request for Information Regarding Private Education Loans and Private Educational Lenders" (Jan. 17, 2012).

[37] See, e.g, Kelly Field, "Department's New Debt Management System Leaves Some Students Stuck in Default," The Chronicle of Higher Education (Dec. 9, 2011).

for borrowers who attended a fraudulent school. For example, a school may routinely pay admissions officers by commission in violation of incentive compensation rules, fail to provide educational materials or qualified teachers, and admit unqualified students on a regular basis. None of these violations is a ground for cancellation. Instead, each cancellation offers relief for a narrow set of circumstances. We recommend that Congress and the Department consider new loan cancellation criteria that will afford relief to all borrowers who attend schools that violate key Higher Education Act (HEA) regulations and for borrowers who have secured judgments against schools based on HEA violations but are unable to collect from the schools or other sources. We also urge creation of a fair and equitable disability discharge process. [38]

Restore an Adequate Safety Net for Student Loan Borrowers

Some former students will never recover financially, often due to disability or related health problems. There comes a point of no return where the government's ceaseless efforts to collect make no sense, monetarily or otherwise.

S. 1102, the "Fairness for Struggling Students Act of 2011" is a critical first step in restoring bankruptcy rights which will help students get back on their feet. The legislation would allow private student loan borrowers the same relief afforded to other unsecured debtors.

In addition to restoring bankruptcy rights, we urge the following reforms:

- Re-impose a reasonable statute of limitations on federal student loan collections. The elimination of the statute of limitations for student loans in 1991 placed borrowers in unenviable, rarified company with murderers, traitors, and only a few violators of civil laws. Even rapists are not in this category since there is a statute of limitations for rape prosecutions, at least in federal law and in most states.

- Eliminate Social Security and federal benefit offsets. At a minimum, increase the $9,000 annual exemption amount. This "floor" has not been amended since the mid 1990's.

- Eliminate offset of earned income tax credits.

Reining in collection abuses is a key component of a viable safety net. Unfortunately, there are serious collection abuses in both the federal and private student loan industries. In the private student loan industry, many violations occur due to collectors' inaccurate claims about their collection powers. It is particularly common for collectors of private student loans to claim that they can use collection tools unique to federal loans, such as Social Security offsets. These types of deceptive or false claims can be the basis of state or federal debt collection or other legal violations.

[38] See generally National Consumer Law Center, "Written Testimony of Deanne Loonin in Response to the May 5, 2011 U.S. Department of Education Notice of Establishment of Negotiated Rulemaking Committees and Notice of Public Hearings" (May 20, 2011), available at: http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/2007/03/neg-rulemaking-may2011.pdf.

With respect to federal loan collection, the Department of Education has turned over almost all student loans it holds to private collection agencies. In a 2009 report, the Treasury Department stated that the Department of Education uses private collection agencies heavily to collect defaulted student loans and refers every eligible debt to these agencies as quickly as possible.[39]

Student loan debt collection contacts, both by private collectors and guarantors, involve a remarkable amount of deceptive, unfair, and illegal conduct. There are several reasons for the extent of these abusive collection actions, including:

- Remedies available to collect on student loans are often both unique and misunderstood (for example, federal tax refund offsets, federal benefits offsets, and non-judicial garnishments), and collectors often misrepresent the exact nature of these remedies when they send collection letters.

- Private collection agencies are delegated the responsibility for determining the size of a reasonable and affordable payment plan for rehabilitation. In addition, these collection agencies help determine if students have defenses to wage garnishments, tax refund offsets and other collection actions, even though the collection agencies' financial incentive is not to offer reasonable and affordable plans or to acknowledge defenses.

We urge the Department of Education to eliminate the use of private collection agencies.[40] In the meantime, there are ways to improve the system so that private collection agencies follow the law and better serve borrowers, including:

- ➢ Developing a rigorous, public training process for collection agencies that includes information about all student loan rights as well as fair debt collection rights,

- ➢ Improving all aspects of enforcement and oversight of private collection agencies, and

- ➢ Only charging collection fees that are bona fide and reasonable and actually incurred in collecting against individuals.

Conclusion

Restricting relief for student loan borrowers gives lenders some additional peace of mind and potentially more profits. These goals reflect industry interests, not the key policy goals of improving access to education and making college more affordable for students and their families.

[39] U.S. Dep't of the Treasury, "U.S. Government Receivables and Debt Collection Activities of Federal Agencies: Fiscal Year 2008 Report to the Congress" at 14 (July 2009).
[40] See Deanne Loonin, New America Higher Ed Watch, "Get Rid of Student Loan Collection Agencies" (Jan. 6, 2010), available at: http://higheredwatch.newamerica.net/node/25940.

There are many ways to close the education achievement gap, but at a minimum, we must ensure that those who do not succeed the first time can try again if they are ready and able. A first attempt at higher education should not be the final attempt. We must also create an adequate safety net for financially distressed borrowers.

Appendix A

Recommendations to Protect Private Student Loan Borrowers and Ensure Fair Lending

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.