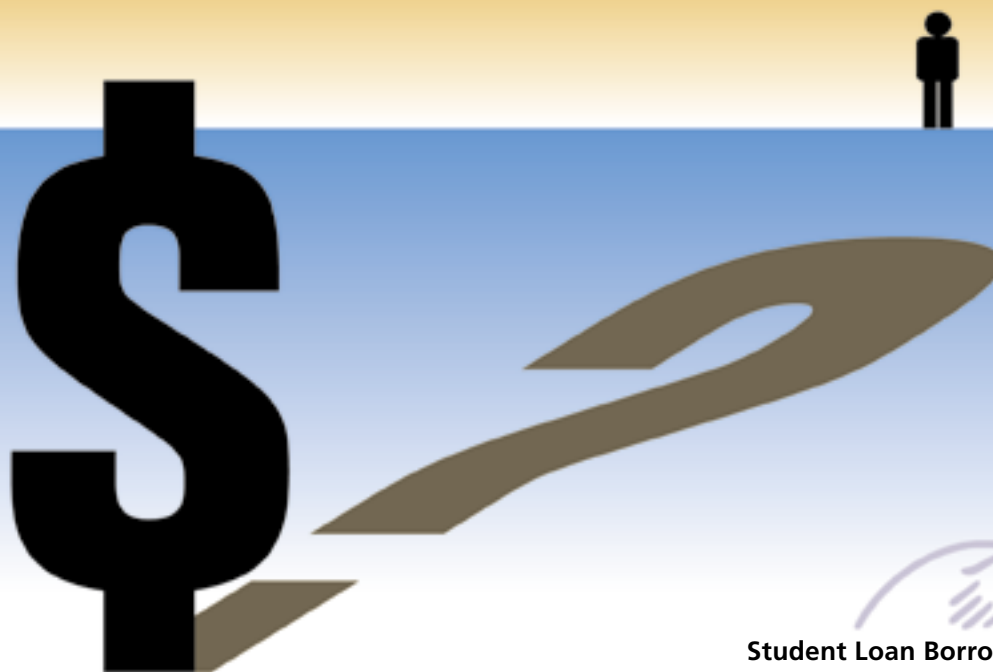


PILING IT ON

THE GROWTH OF PROPRIETARY SCHOOL LOANS AND THE CONSEQUENCES FOR STUDENTS



Student Loan Borrower Assistance



January 2011

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The findings and conclusions presented in this report are those of the author alone.



ABOUT THE NATIONAL CONSUMER LAW CENTER

The National Consumer Law Center[®], a nonprofit corporation founded in 1969, assists consumers, advocates, and public policy makers nationwide on consumer law issues. NCLC works toward the goal of consumer justice and fair treatment, particularly for those whose poverty renders them powerless to demand accountability from the economic marketplace. NCLC has provided model language and testimony on numerous consumer law issues before federal and state policy makers. NCLC publishes an 18-volume series of treatises on consumer law, and a number of publications for consumers.

EXECUTIVE SUMMARY

GROWTH OF INSTITUTIONAL LOANS AFTER THE CREDIT CRASH

Before the credit crash in 2008, many proprietary schools partnered with third party lenders to provide private student loans to their students. Private student loans are made by lenders to students and families outside of the federal student loan program. They are almost always more expensive than federal student loans. High rate private student loans were made to many proprietary school students during this time, often with little or no underwriting criteria. When these loans started to fail at devastating rates, nearly all of the third party lenders exited the subprime student loan business and terminated their partnerships with proprietary schools.

Proprietary school executives faced a dilemma when the credit crisis hit. This report is about the way they responded, focusing on the schools that created their own student loan products.

The proprietary school executives could have viewed the pull-out of the third party creditors as a warning sign that lending without regard to repayment caused significant harm to their students. Instead, many proprietary school executives chose to create or expand institutional loan products. They did this even though their students were already struggling with student loan debt, both federal and private, and even though most knew that a majority of their students would not be able to repay the new loans.

All of the large companies, except for Apollo Group, the largest of all, have

increased institutional lending in some way. The size of the institutional lending varies considerably as do funding sources.

PROBLEMS WITH INSTITUTIONAL LOANS AND CONSEQUENCES FOR STUDENTS

High Default Rates

As documented in this report, the default rates on most institutional loans are shockingly high. The schools seem to view these loans more as “loss leaders” to keep the federal dollars flowing. Among other reasons, proprietary schools must show that at least 10% of revenues come from sources other than Department of Education federal student assistance. This is known as the “90–10” rule. Schools make unaffordable loans as a way of filling up the 10% category with vapor revenues derived from loans that will never be repaid.

The growth of institutional lending is not only about “90–10.” It is also more simply a way for schools to keep revenues of all types flowing so that profits remain high and the companies remain attractive to investors.

However, the view from the student perspective is much different. 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.

High Costs

Many of the institutional loan products have high interest rates and origination fees, particularly for less credit worthy borrowers.

Predatory Terms

The problems with these products are not confined to cost. In our review of the institutional loans, we found many other problems and predatory terms. For example, many include mandatory arbitration clauses. Many also include hair-trigger default clauses, providing that a student who misses just one payment, files for bankruptcy (even if the student loan is not discharged), or, in some cases, leaves school without graduating is in default.

Schools Often Deny Transcripts or Terminate Students who Cannot Pay

Many of the 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 federal loan, but payment is not required. Many students 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.

Lack of Regulation

There has been substantial confusion in many cases about who is regulating institutional products or who should be regulating the products. Regulatory authority at the federal level will be clearer as of July 2011 when the Consumer Financial Protection Bureau (CFPB) comes into being. The CFPB has authority over all private student loans made by non-banks.

However, confusion and gaps still exist, particularly at the state level. Schools may claim that the institutional loans they offer are not really “loans” and so are not within the jurisdiction of state banking agencies. This is presumably an effort to evade disclosure requirements such as the federal Truth in Lending Act, but also to avoid application of certain state laws.

State regulators do not appear to be focusing on this issue. We contacted a number of state regulators and with one exception were told that they do not specifically track school institutional lending programs.

Accounting Tricks and Traps

Many schools have developed accounting systems that hide the true loss rates of the institutional loans and how these loans impact their companies. For example, many have used the institutional products as a way to make the company’s bad debt situation look better, at least on the surface.

Overall, these accounting tactics not only lower the booked bad debt expense, but also understate leverage. All of this makes the companies more attractive investments, but in many cases these accounting methods obscure real problems with the companies.

RECOMMENDATIONS FOR REFORM

1. Strengthen the 90–10 Rule and Study Its Effects

In its present form, the 90–10 rule is easily gamed by schools. The rule even creates perverse incentives for schools to make loans without regard to ability to pay and to increase tuition.

Any study of the rule in its present form is unlikely to be a true measure of its usefulness. It is essential to strengthen the rule in order to assess whether it helps improve quality outcomes at proprietary schools.

There are many ways to put some teeth back into the 90–10 rule and reduce the perverse incentives that it creates in its current form. These include:

- Including all federal funding in the 90% category.
- Prohibiting schools from counting in the 10% category loans in which the school has a substantial portion of the credit risk.
- Ending the temporary relief for schools that allows them to temporarily count increased federal loans revenues as part of the 10% of non-federal revenues and to count in the 10% category the net present value of any institutional loans made before July 1, 2012. These are incentives for schools, at least in the short-term, to make institutional loans regardless of whether students repay them.
- Changing the required ratio depending on a school's federal and private loan default rates. For example, a default rate of more than 15% would require an 85-15 ratio. A default rate of less than 10 to 15 would permit a 90–10 ratio and so on.

2. *Regulators Must Provide Aggressive Oversight of Institutional Loans*

Institutional loan products have generally fallen through regulatory cracks. Regulators, both state and federal, must evaluate institutional

loan programs and enforce relevant laws. Among other actions, we recommend:

- The FTC (and in July 2011 the CFPB) should immediately request that the schools provide detailed information about the various loan programs so that the agencies can take appropriate enforcement actions.
- Bank regulators should review the involvement of entities within their oversight responsibility that are partners in institutional loans and credit unions that have begun to offer their own school loan products, in some cases in affiliation with schools.
- State education and banking departments should review and enforce banking licensing and substantive laws.
- The Federal Reserve Board (FRB) (and in July 2011 the CFPB) and the FTC using its authority under the FTC Act should pass comprehensive unfairness standards applicable to private student loans, including institutional loans.
- Students should be able to raise as defenses to student loans, the breach of these unfairness standards described above.
- The FRB (and in July 2011 the CFPB) and the FTC should review whether the schools are complying with Truth in Lending Act (TILA) disclosure requirements.
- Federal and state regulators should review institutional loan programs for possible violations of unfair and deceptive consumer protection laws.

3. *Ensure That Schools are Held Accountable Even if they Sell Institutional Loans or Use Other Entities to Make the Loans*

4. *The Department of Education Must Examine Institutional Loan Programs and the Impact on Federal Student Aid*

The Department of Education should be particularly concerned about the ways in which schools are using institutional loan programs to evade 90–10-related sanctions. As both a legal and policy matter, schools should face sanctions for taking actions that are clearly not in the best interests of students. In particular, the Department should investigate schools that are setting tuitions school by school and even program by program in order to ensure compliance with 90–10.

5. *Track Private Loan Default Rates*

There is no comprehensive set of data about private student loan default rates, including institutional loans. A key way to improve information about private student loans,

including institutional loans, is to include private loans in the National Student Loan Data System (NSLDS). Consumers would then be able to see all their loans, both federal and private, in one place and receive counseling based on their total student loan debt.

6. *Provide Relief for Financially Distressed Students*

If enacted, many of the recommendations discussed above will improve quality at proprietary schools, benefitting future students. In the meantime, there are countless student borrowers buried in debt with nowhere to turn. A key barrier to relief is that both third party and institutional student loans are nearly impossible to discharge in bankruptcy.

A major first step is to reform the bankruptcy laws so that student borrowers can discharge private student loans without having to go through the complex and nearly impossible “undue hardship” process. Other non-bankruptcy loss mitigation strategies should also be considered. There are also ways to expand relief through the federal student loan programs.

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I. INTRODUCTION

Before the credit crash in 2008, many proprietary schools partnered with third party lenders to provide private student loans to their students.¹ Private student loans are made by lenders to students and families outside of the federal student loan program. They are almost always more expensive than federal student loans. High rate private student loans were made to many proprietary school students during this time, often with little or no underwriting criteria. When these loans started to fail at devastating rates, nearly all of the third party lenders exited the subprime student loan business and terminated their partnerships with proprietary schools.

Proprietary school executives faced a dilemma when the credit crisis hit. This report is about the way they responded, focusing on the schools that created their own student loan products. This report explores the growth of institutional loans products and the harm they have caused to students and taxpayers.

The proprietary school executives could have viewed the pull-out of the third party creditors as a warning sign that lending without regard to repayment caused significant

harm to their students. The schools could have reacted in many ways such as lowering tuitions or reducing their often excessive executive compensation. For example, the Chairman and CEO of the for-profit education company Strayer Education was paid \$41.9 million in 2009, 26 times the compensation of the highest-paid president of a traditional university.² At least some of these savings could have been used to fund more scholarships and grants for students.

Instead, many proprietary school executives chose to create or expand institutional loan products. They did this despite the additional debt piled on students already struggling with student loans, both federal and private, and even though most knew that a majority of their students would never be able to repay the new loans.

Reading only insider Wall Street accounts, one might think the schools had no other choice but to create new loan products in response to the exodus of third party lenders. Referring to announcements that Sallie Mae and other loan providers would stop providing private loans to many proprietary schools, FBR Capital Markets issued a report stating that “. . . several institutions such as Corinthian Colleges and Career Education were forced to make loans directly to students.”³ This misses the mark because the schools deliberately chose to make the loans. It was a purposeful decision that may have benefited the companies and their investors, but was not

¹ The terms “proprietary” and “for-profit” schools are used interchangeably throughout this report. Proprietary institutions range from small vocational and technical schools to large accredited colleges and universities offering “traditional classroom experiences” and online degrees. The main difference between proprietary institutions and traditional public and private nonprofit institutions relates to control, operation and mission. See generally Daniel L. Bennett, Adam R. Lucchesi and Richard K. Vedder, Center for College Affordability and Productivity, “For-Profit Higher Education: Growth, Innovation and Regulation” (July 2010).

² John Hechinger and John Laueran, “Executives Collect \$2 Billion Running U.S. For-Profit Colleges”, Bloomberg, (Nov. 10, 2010).

³ FBR Capital Markets, “Proprietary Schools 101: Coverage Initiation” at 13 (Jan. 14, 2010).

in the best interests of their students. We know that this was not the only option available as not all proprietary schools took this route.

Harris Miller, the President of the Career College Association (now Association of Private Sector Colleges and Universities), stated in a 2009 article, “We’re not lenders. We’re educators,” but “if it’s a question of not going to school at all or covering the gap, they [the schools] cover the gap.”⁴ As documented in this report, “covering the gap” is not as innocuous as it seems. It means that students who are already burdened with high levels of federal student loans will now be saddled with additional private loans that they cannot repay and that damage their credit reports. In many cases, the loans have high interest rates and include predatory terms.

As documented in this report, the default rates on the institutional loans are shockingly high. Given the acknowledged failure rates of these loans, why did the schools create or expand institutional loans? The only way this appears to make sense is if these loans are recognized as loss leaders that keep the federal dollars flowing. There is so much profit reaped from federal student aid funds that the massive losses experienced from these institutional loans are simply a cost of doing business. As explained in a 2009 AP article, “Consider, for example, a school charging \$10,000, hoping to enroll a student who has lined up \$9,000 in aid from the government and elsewhere. Even if the school loses half of the \$1,000 it lends to get the student in the door, it comes out \$9,000 ahead.”⁵

⁴Justin Pope, “For-Profit Colleges Boost Lending”, AP Impact (Aug. 14, 2009).

⁵Id.

This report focuses on how many proprietary schools have responded to government and investor interests by creating institutional loan products. The first section reviews the responses of the largest for-profit higher education companies and a number of smaller companies as well. This section is followed by a review of the main problems with institutional loans. The final sections discuss the various rationales for the schools’ actions and recommendations for reform.

II. METHODOLOGY

We gathered information for this report in a number of ways. We sent the questionnaire attached at Appendix 1 to six of the largest proprietary school companies. Two did not respond at all. Two responded by telling us to review their publicly filed information. Only representatives from Apollo and DeVry provided substantive responses. The balance of the information in this report is from publicly available data, such as S.E.C filings and media reports as well as information gathered from NCLC’s clients.

We were able to gather at least some information about the following larger companies and schools: Alta Colleges (Westwood Colleges), Apollo Group (University of Phoenix), Career Education Corporation, Corinthian Colleges, DeVry, Education Management Corporation (EDMC), ITT Educational Services and Kaplan Education. We also include information about lending at some of the smaller schools.

All of the large companies, except for Apollo, the largest of all, have increased institutional lending in some way. The size of the institutional lending varies considerably as do funding sources.

Largest For-Profit Institutions

INSTITUTION	2008-09 ENROLLMENT	% OF TOTAL FOR-PROFIT ENROLLMENT
Apollo Group	395,361	21.2
Education Management	104,547	5.6
Career Education Corp.	97,645	5.3
Corinthian Colleges	85,029	4.6
DeVry	78,544	4.2
Kaplan Education	67,897	3.7
ITT Educational Services	60,890	3.3

Source: U.S. Department of Education, IPEDS as calculated in Daniel L. Bennett, Adam R. Lucchesi and Richard K. Vedder, Center for College Affordability and Productivity, “For-Profit Higher Education: Growth, Innovation and Regulation” at 15 (July 2010).

The schools highlighted in this report make up a significant share of revenues and students at for-profit schools. The table above shows a comparison of enrollment numbers for the largest for-profit schools.

III. HOW WE GOT HERE: THE ROAD TO INSTITUTIONAL LENDING/FEDERAL FUNDS FUEL GROWTH AND PROFITS

The proprietary (or “for-profit”) higher education industry has experienced unprecedented growth in recent years. Between 1998 and 2008, enrollment in higher education generally increased 31%. Among for-profit schools, enrollment increased by 225% over that same period.⁶

⁶ U.S. Senate, Health, Education, Labor and Pensions Committee, “Emerging Risk?: An Overview of Growth, Spending, Student Debt and Unanswered Questions in For-Profit Higher Education” at 2 (June 24, 2010).

This growth has paid off for the schools and their investors. The average operating profit in FY 2005 among publicly traded for-profit higher education companies was \$127 million. The same number in FY 2009 was \$229 million, an increase of 81%.⁷

This rapid growth is fueled by federal dollars. In 2009, proprietary schools received almost one-quarter of all Pell grants, up from just 13% in 1999.⁸ Federal dollars going to proprietary schools continues to increase. For example, eight of the sixteen for-profit schools analyzed in a September 2010 U.S. Senate report more than doubled the amount of Pell grant dollars they received just between 2006 and 2009 and three nearly doubled Pell funding.⁹ The U.S. Senate Committee on Health,

⁷ Id. at 5.

⁸ Id. at 3.

⁹ U.S. Senate Comm. on Health, Educ., Labor & Pensions, “The Return on the Federal Investment in For-Profit Education: Debt Without a Diploma” at 10 (Sept. 30, 2010).

Education, Labor and Pensions (HELP) found that the percentage of school revenues comprised of all federal dollars (generally in the form of assistance to students) ranges as high as 93.1% for many proprietary schools. Many also receive state funds that bring the dependence on government funds closer to 95%.¹⁰ The flow of federal dollars drives the profits that make the companies attractive to investors.

This may seem on the surface like a typical business success story, but there are very serious down sides for students and taxpayers. Students at these schools default on their federal students loans at disproportionate rates. Further, there are many serious concerns about poor quality and consumer fraud at these schools.¹¹

“Default rates are sky high, taxpayer money is being squandered, top executives walking away with fortunes. You might think I am talking about the subprime mortgage industry,

which came crashing down 2 years ago, because that does describe it. But what I have just described is also the situation created by many for-profit colleges. Just as in the subprime mortgage crisis, countless thousands of ordinary Americans are being harmed by the reckless pursuit of profits by a few.”

—Excerpt from Senator Tom Harkin’s December 14, 2010 speech on the Senate floor about the Senate’s investigation of for-profit education.

In response to the many problems with the industry over the years and the huge stakes for taxpayers and students, Congress passed legislation in 1992 limiting the share of revenues schools can receive from the federal Department of Education student assistance funds. Originally, schools were limited to 85% of revenues from federal student assistance funds. This was changed to 90% and is now known as the “90–10 rule.”

Before the crash in 2008, third party private student loans helped many schools fulfill the 10% “no federal student assistance” category. During this time, many schools encouraged and even pressured their students to take out student loans with third party lenders.¹² This also allowed the schools to keep charging high tuitions even though they generally enroll students who have little or no ability to pay out of their own pockets. The private loan boom may have boosted the school’s enrollment and profits, but it took a terrible toll on these students, as described below.

¹⁰ U.S. Senate Committee on Health, Education, Labor and Pensions “The Return on the Federal Investment in For-Profit Education: Debt Without a Diploma” at 10 (Sept. 30, 2010).

¹¹ These problems have been documented in numerous investigations and media reports, including U.S. Health, Education, Labor and Pensions Committee reports: “Emerging Risk?: An Overview of Growth, Spending, Student Debt and Unanswered Questions in For-Profit Higher Education” (June 24, 2010), and “The Return on the Federal Investment in For-Profit Education: Debt Without a Diploma” (Sept. 30, 2010). See also National Consumer Law Center, Public Advocates and U.S. PIRG, “Comments to the FTC on Vocational School Guides” (Oct. 16, 2009), available at: http://www.studentloanborrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/policy_briefs/FTCguides1009.pdf. A summary of media reports on these issues can be found at: <http://protectstudentsandtaxpayers.org>.

¹² See generally, 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.

IV. FOR-PROFIT EDUCATION AND STUDENT LOANS

Students at for-profit schools on average take on more debt and default on this debt at higher rates than students in other sectors.¹³ Proprietary school students are much more likely to default on federal student loans. Based on Department of Education data released in 2010, nearly half of all federal student loan defaulters (43%) attended for-profit schools even though these schools enrolled only about ten percent of all students during this time period.¹⁴ According to data released by the Department of Education in December 2010, 46.3 percent of all Stafford loans to students at two and four year proprietary schools in 2008 will eventually go into default. This is compared to an overall “lifetime” default rate for all higher education sectors of 15.8%.¹⁵

The high default rates indicate that many students are experiencing financial problems after leaving school. The full scope of problems is illustrated by the poor academic completion rates and poor job placement rates at many of these schools. The debt issues are closely connected to the lack of quality outcomes

because students who do not complete school and do not find employment are generally less likely to be able to repay their loans.

For an industry that is fueled almost exclusively by federal funds, particularly federal loans and grants, it may come as a surprise that many of the students at these schools have had high rates of private loan borrowing, particularly during the credit boom. Private student loans are made by lenders to students and families outside of the federal student loan program. They are not subsidized or insured by the federal government and may be provided by banks, non-profits, or other financial institutions. Institutional loans are a type of private student loan.

In theory, private student loans may have some advantages over federal loans in terms of flexibility and less restrictive collection tactics. Yet in reality private loans are almost always more expensive than federal student loans. This is especially true for borrowers with lower credit scores or limited credit histories. The key differences between federal and private student loans are summarized in the table on page 11.

During the heyday of easy credit and subprime lending in the mid-2000s, an alliance developed between a number of lenders and many proprietary schools to market private loans to their students. After making loans in many cases with little or no underwriting standards, the lenders turned around and, like subprime mortgage providers, enjoyed enormous profits by securitizing the loans and selling risky debt to investors.

Many of these loans were recourse loans, meaning that the school took on full or partial financial responsibility if the borrower was unable to repay. In most of their arrangements with private lenders such as Sallie Mae, the

¹³ About 95% of students at two year for-profits and 93.4% at four year for-profits took out federal student loans in 2007-08. This is compared to 16.6% of students at community colleges and 44.3% at four year public schools. U.S. Senate Comm. on Health, Educ., Labor & Pensions, “The Return on the Federal Investment in For-Profit Education: Debt Without a Diploma” at 6 (Sept. 30, 2010).

¹⁴ The Project on Student Debt, “Federal Student Loan Default Rates on the Rise” (September 13, 2010).

¹⁵ These rates are calculated based on Stafford loan dollars originated in FY 2008 that may default during a twenty year life of the loan period. See U.S. Department of Education, “Default Rates for Cohort Years 2004-2008” (Dec. 20, 2010).

DIFFERENCES BETWEEN FEDERAL AND PRIVATE STUDENT LOANS

- **Underwriting.** With the exception of PLUS loans, federal loan borrowers do not have to meet creditworthiness standards to obtain federal loans. Private loans, in contrast, are priced according to credit worthiness standards.
- **Pricing.** All federal loans have interest rate caps, in most cases with fixed rates set at 6.8% or lower. In contrast, most private loans have variable interest rates with no upper limits.
- **Loan Limits.** There are loan limits for the various federal loan programs. The only exception is PLUS loans. Parents or graduate students may take out PLUS loans equaling the cost of attendance minus any other financial aid received. For private loans, there are no regulations setting a maximum dollar amount on how much a student can borrow. Generally, lenders allow students to borrow up to the cost of attendance minus other aid.
- **Borrower Protections.** 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 or repayment options and generally do not offer such options.
- **Application Process.** Private loan borrowers are not required to fill out the complicated federal application form, known as the “FAFSA.” Many companies tout the simplicity of the private loan application and approval process.
- **Regulation.** Federal loans are regulated through the Higher Education Act (HEA). Private loans, in contrast, are regulated (or not) in much the same way as other types of private credit, such as credit card installments or mortgage loans. This will begin to change at the federal level in July 2011 when the new Consumer Financial Protection Bureau (CFPB) will take over rule writing and enforcement authority over most private student lending.
- **Information and Data Collection.** Significant data about federal student loan borrowing is available through the National Center for Education Statistics and other related resources. Borrowers are also able to access information about their federal loans through the National Student Loan Data System (NSLDS). There is no similar comprehensive data base for private loans.
- **Collection.** Both federal and private lenders use third party collection agencies to pursue delinquent and defaulted borrowers. Private student lenders have fewer collection powers than federal collectors. This gap is closing, however, as private lenders have fought to obtain many of the same collection rights as the government. They succeeded in persuading Congress in 2005 to make private 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.

schools were required to repurchase loans originated by the lenders after a certain period of time or otherwise mitigate the risk to the lenders. Despite the schools’ willingness to cover losses, nearly all third party lenders cut off ties with proprietary schools after the credit crash, starting in 2008.

The subprime private student loan market showed signs of weakness by 2007 and then dried up by 2008. The losses on these loans were staggering. In May 2010, Sallie Mae projected that of the \$6 billion in non-traditional private student loans in its portfolio, 40%

would default. The company also stated that these loans made up about 11% of their private loan portfolio.¹⁶ First Marblehead reported in 2010 that almost 50% of the loans it securitized into trusts would fall into the worst performing category, with default rates of nearly 50%. According to Student Lending Analytics, that would mean that of approximately \$6 billion in First Marblehead’s

¹⁶ Student Lending Analytics, “The \$5.4 Billion Private Student Loan Problem” (May 16, 2010).

high risk loans, there would be \$3 billion in defaults.¹⁷

Sallie Mae and others have attributed much of the poor performance to their “non-traditional” loan portfolio. These loans are described as loans to borrowers who are expected to experience high default rates because of factors such as having lower tier credit ratings or attending schools with low program completion and graduation rates. These inferior outcomes are typical for “non-traditional schools”, including many proprietary schools.¹⁸

When the market crashed in 2008, the alliance between lenders and for-profit schools came to a fairly sudden and almost complete stop. Sallie Mae ended its relationships with most for-profit schools in early 2008. For the most part, these partnerships have not yet been renewed.

V. THE GROWTH OF INSTITUTIONAL LOANS

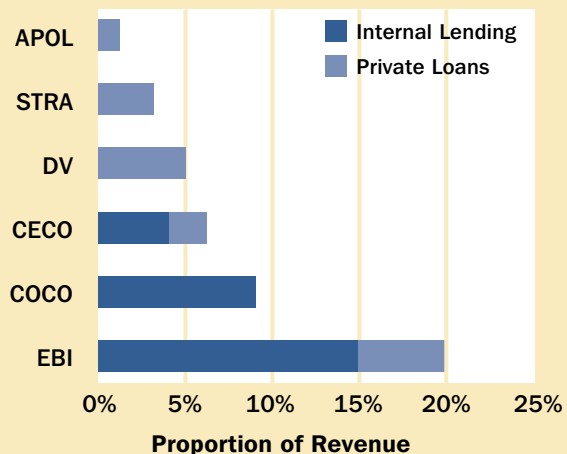
The graph below shows how the largest proprietary schools have responded to the demise of third party private student lending. With the exception of Apollo, the largest of them all, most have expanded their institutional lending.

Apollo’s main brand is the University of Phoenix. Apollo students were not heavy users of any type of private student loans before the market crash. As of early 2010, the company reported that private student loans accounted for only about 1% of its

¹⁷Id.

¹⁸Fitch Ratings, “Private Education Loans: Time for a Re-Education” at 7 (Jan. 28, 2009).

Internal Lending: Proportion of Revenue from Private Loans and Internal Lending, FY 2009



Source: UBS Investment Research: Education Update (March 4, 2010).

revenues.¹⁹ Perhaps because its students had not previously relied much on private loans, the school has not increased institutional lending since the crash to any measurable degree. Other than a small pilot project, the company says that it has not developed institutional loan products. An Apollo spokesperson stated that the company made the deliberate decision not to engage in private lending because “. . . quite simply, we believed it was not in the best interests of our students.”²⁰

Among the schools shown in the graph above, **ITT (ESI)** had the highest percentage of both institutional and private loans in FY 2009. The company had 15% of revenues from

¹⁹FBR Capital Markets, “Proprietary Schools 101: Coverage Initiation” at 67 (Jan. 14, 2010).

²⁰David A. Graham, “An Education in Institutional Loans”, Newsweek (Nov. 20, 2009).

internal lending with another 5% from other private loans.²¹

In January 2010, ITT announced a new institutional loan program called PEAKS. A trust was established that issued \$300 million in senior debt to a group of investors. Deutsche Bank facilitated the purchase of ITT loans by the PEAKS trust.²² ITT guarantees payment of principal, interest and certain premiums on the Senior Debt and administrative fees and expenses of the trust.²³ Some or all of the holders of the Senior Debt could require ITT to purchase the Debt in certain circumstances.

The company says that only students in their second academic year at ITT are eligible for PEAKS loans. The company has also said that it will still offer institutional loans to first year students, with some credit requirements for eligibility.²⁴ Second year students are eligible to take out PEAKS loans for current and future expenses as well as to refinance prior institutional loans.²⁵ The company says that it does have credit standards and that borrowers must be of majority age and have completed a minimum of 20 quarter credit hours or the equivalent of credit for college level courses.

The company did not provide substantive responses to our request for information and has generally not disclosed much detail about

the PEAKS program. It did, however, provide some additional disclosures in third quarter 2010. Total disbursements in the third quarter under its private student loan programs, it said, were \$64 million, the vast majority through PEAKS.²⁶

The ITT catalog provides additional details about the program. An excerpt from a May 2010 catalog is attached at Appendix 2. The information in the catalog includes a sample Truth in Lending disclosure for PEAKS. Through the PEAKS program, students are eligible to borrow from \$1,000 up to the cost of the education, less other aid, not to exceed:

- \$35,000 in total for an associate degree program
- \$60,000 in total for a bachelor degree program (including any amount for an associate degree program); and
- \$25,000 for a graduate degree program.

Corinthian Colleges also expanded institutional lending considerably. Corinthian operates Everest, WyoTech and Heald College. Many analysts view Corinthian as one of the most troubled of the for-profit higher education companies.²⁷ In November 2010, Chief Executive Peter Waller resigned at the request of the board of directors. The Wall

²¹ For a summary and graph of internal lending, see UBS Investment Research “Education Update” (March 4, 2010).

²² Alison Damast, Deutsche Bank and ITT Team Up for New Loan Program”, Business Week (Jan. 25, 2010).

²³ ITT Educational Services Inc (ESI), 10-Q (Filed April 22, 2010).

²⁴ ITT Educational Services, Inc. “Q4 2009 Earnings Call Transcript” (Jan. 21, 2010).

²⁵ Id.

²⁶ Please Act Accordingly, “Please Help Us Answer a Few Questions, Examining ESI’s Leverage” (Oct. 26, 2010), referencing ITT’s FY 2010 third quarter conference call.

²⁷ In January 2010, FBR Capital Markets called Corinthian the most likely of the for-profit education companies to “get detention.” This is a “cautious” investment rating, stemming from expectations of decelerating enrollment growth, regulatory changes, and concerns about student defaults and 90–10 compliance. FBR Capital Markets, “Proprietary Schools 101: Coverage Initiation” at 75 (Jan. 14, 2010).

Street Journal reported that he received a \$1.55 million lump sum severance payment.²⁸

Corinthian students were heavy users of private loans. In 2007, private loans represented 13% of Corinthian's total revenues, with Sallie Mae providing about 90% of these loans.²⁹ Sallie Mae notified the company in 2008 that it would no longer provide private loans to its students.

In an August 2009 conference call, Corinthian management referred to the company's internal lending program as the Genesis Discount Lending Program. Corinthian described Genesis as a company that specializes in subprime credit. Genesis has described itself as a company that serves the most credit-challenged applicants.³⁰ This program replaced the prior institutional loan program called STAR.

Corinthian described a process of "ramping up" internal lending throughout 2008 and 2009. In order to increase the amount of loans funded, the company was focused on decreasing the amount of time needed to fund the loans. Among other actions, this involves shortening the funding cycle so that more loans can be funded.³¹ Corinthian lent about \$120 million in institutional loans for both of the years ending June 30, 2009 and 2010. It expected to lend about \$150 million in FY 2010.³²

²⁸ Melissa Korn, "Corinthian College CEO Waller Resigns, Massimino Retakes Helm", Wall Street Journal (November 30, 2010).

²⁹ FBR Capital Markets, "Proprietary Schools 101: Coverage Initiation" at 83 (Jan. 14, 2010).

³⁰ Business Wire, "Genesis Lending Services Expands Options for Credit-Challenged Students in Educational Programs" (May 21, 2008).

³¹ Corinthian Colleges Q2 2009 Earnings Conference Call Transcript (Feb. 3, 2009).

³² Corinthian Colleges, Inc. Form 10-K (FY 2010, filed Aug. 20, 2010); Corinthian Colleges FY10Q2 Earnings

The Genesis program has some similarities to previous Corinthian institutional loan programs. Under the Genesis program, Corinthian pays a discount to Genesis, the origination and servicing provider, as a reserve against future defaults. Corinthian records the discount as a reduction to revenue. However, unlike the previous private loan programs, under the Genesis program, Corinthian has both the right and an obligation to acquire the related loans, except in very limited circumstances. Corinthian bears the risks of collections. Since initiating the program in 2008, Corinthian says it has acquired all of the loans that have been originated.³³

Career Education Corporation (CEC) also expanded institutional lending. The company has 90 campuses with a total enrollment of about 116,000 students worldwide. The company has a number of brands including American InterContinental University, Colorado Technical University, International Academy of Design & Technology and Le Cordon Bleu North America.

CEC has had a high percentage of students borrowing private loans. CEC's private loan funding traditionally came from third parties such as Sallie Mae. Sallie Mae shut off the faucet in early 2008, notifying the company that it would no longer provide any recourse private student loans and would curtail the funding of nonrecourse loans.³⁴ CEC also previously had recourse loan agreements with Stillwater National Bank and Trust Company. These programs required CEC to repurchase loans originated by the lenders after a certain

Call Transcript (Feb. 2, 2010).

³³ Corinthian Colleges, Inc. Form 10-K at 37 (FY 2010, filed Aug. 20, 2010).

³⁴ Career Education Corp., 10-Q (Filed May 5, 2010).

period of time.³⁵ The Stillwater agreement ended in April 2007.

Total private loans, including recourse and non-recourse, accounted for about 10% of CEC's cash flows in 2008, 17.6% in 2007 and 22.1% in 2006.³⁶ These percentages declined significantly as the third party student lending market dried up. The percentage of cash receipts from private loans decreased to just 2.3% during the first three quarters of 2009.³⁷

After the end of these affiliations with third party lenders, CEC began increasing its institutional lending, mostly through loans referred to as extended payment plans. According to an analysis by FBR Capital Markets, this was a conscious effort by management to loosen credit standards to accommodate more students.³⁸ Through June 30, 2010, CEC had committed to about \$87.7 million of funding through extended payment plans.³⁹

According to CEC, the extended payment plans have lower in-school payments and are generally paid back over a seven year period following graduation.⁴⁰ The company has said that the interest rate on these products is 8% for most students, although it says that online students pay no interest.⁴¹

DeVry University also expanded institutional lending. DeVry University is the parent organization of Advanced Academics, Becker Professional Education, Carrington

College and Carrington College California, Chamberlain College of Nursing, DeVry Brasil, DeVry University, and Ross University.

Private student loans represented about 5% of revenues in 2008, with the majority of the loans provided by third party lenders. In FY 2009, 3% of DeVry's revenues were from private loans.⁴²

Due to contraction in lending by third party lenders in 2008 and 2009, the school began funding more loans on its own and retaining credit risk on those loans.⁴³ Much of this involved an expansion of the company's existing Educard program. DeVry also has other institutional loan programs, including Chamberlain, Apollo/Western Career College and Ross Institutional Loan Programs. DeVry says that it does not pull credit information for any of the institutional loan products except for the Apollo/Western Career College Program.

The company said that it has not offered other loan products in the past and that it does not have arrangements with banks or other entities to offer loan products. DeVry provided this information in response to our questionnaire in spring 2010. It was the most transparent of the companies we surveyed about their loan products.

DeVry started offering the Educard product in the early 1970's to enrolled students. The terms are 12% annual interest and 0 fees. Students must pay in monthly installments, with the first monthly payment due at registration. Delinquent payment may prevent future registration. The loan amount is calculated to pay out within one year of graduation with no deferments or forbearances. It is

³⁵ Id.

³⁶ Career Education Corp., 10-K (Filed Feb. 20, 2009).

³⁷ FBR Capital Markets, "Proprietary Schools 101: Coverage Initiation" at 34 (Jan. 14, 2010).

³⁸ FBR Capital Markets, "Proprietary Schools 101: Coverage Initiation" at 35 (Jan. 14, 2010).

³⁹ Career Education Corp., 10-Q (Filed Aug. 4, 2010).

⁴⁰ Career Education Corp., 10-Q (Filed Aug. 4, 2010).

⁴¹ Justin Pope, "For-Profit Colleges Boost Lending", AP Impact (Aug. 14, 2009).

⁴² DeVry Inc., Form 10-Q (Filed May 6, 2010).

⁴³ FBR Capital Markets, "Proprietary Schools 101: Coverage Initiation" at 54 (Jan. 14, 2010).

a revolving credit account while the student is in school that becomes an installment loan when the student leaves or completes school. A copy of the Educard loan agreement is attached at Appendix 3.

At one point, a student finance checklist for Chamberlain School of Nursing stated that all students must have an Educard account, regardless of their financing plans. However, this requirement was deleted from the checklist as of late 2010. This is a positive development if it means that students are not forced to set up a credit card arrangement with the school.

Other schools not depicted in the graph above also expanded institutional lending, including:

Education Management Corporation (EDMC)

Education Management Corporation (EDMC) is the second largest for-profit company as measured by total enrollment. Its four brands are the Art Institutes, Argosy University, Brown Mackie College and South University. Goldman Sachs and two other firms bought EDMC in 2006 and took it public in 2009.⁴⁴

EDMC created its Education Finance Loan (EFL) program with a private lender in August 2008. Under this program, EDMC purchases loans that are originated by a private lender.⁴⁵ According to Art Institute web sites, at least some of these loans are originated by PNC Bank.

⁴⁴ Along the way, Goldman and the other firms shared at least \$70 million in advisory, management, and other fees. Goldman also became EDMC's biggest stockholder. John Hechinger, "Goldman Schools Students on Debt", Bloomberg Business Week (Aug. 5, 2010).

⁴⁵ Education Management Corp. (EDMC), 10-Q (filed September 30, 2010).

During FY 2010, loans to students under the EFL program represented about 2.6% of the company's net revenues and only about 1% in FY 2009.⁴⁶ The company projected total loans awarded under the program in FY 2010 to be nearly \$70 million.⁴⁷ EDMC has said that it does not anticipate awarding loans under this program in FY 2011 to students who had not received loans under the program as of June 30, 2010. It estimates that total loans awarded under the program during FY 2011 will be about \$15 million and that it will purchase about \$25 million in loans under the program in all of FY 2011.⁴⁸ Despite cutting back on institutional lending in 2011, the company has said that it will continue to support students through in-school payment plans.⁴⁹

Other private loans comprised about 4.5% of EDMC's net revenue for FY 2010.⁵⁰ This compares to about 13% in FY 2009 and 22.3% in FY 2008.⁵¹ In FY 2010, about 43% of private loans were Sallie Mae loans. The company's agreement with Sallie Mae to provide loans to certain students who already had private loans expired in June 2010.⁵²

Kaplan

Kaplan's U.S. based higher education division includes Kaplan University, specializing in on-line education, and Kaplan Higher Education

⁴⁶ Education Management Corp. (EDMC), 10-K (filed September 1, 2010).

⁴⁷ Education Management Corp., Q32010 Corporation Earnings Conference Call Transcript (May 5, 2010).

⁴⁸ Education Management Corp. (EDMC), 10-Q (filed Sept. 30, 2010).

⁴⁹ Education Management Corp., Q32010 Corporation Earnings Conference Call Transcript (May 5, 2010).

⁵⁰ Education Management Corp. (EDMC) 10-K (filed Sept. 1, 2010).

⁵¹ Id.

⁵² Id.

campuses, consisting of 73 schools in 19 states. Kaplan, one of the largest for-profit higher education companies, did not respond to our questionnaire and has not provided much public information about its internal lending. Public information about Kaplan, to the extent it is available, is mainly through the Washington Post's filings. The Post owns Kaplan, Inc. In fact, Kaplan accounts for about 62% of the Post's total revenue. In November 2010, the Post reported that overall revenue from its Kaplan division rose to \$743 million, up 9% over the same period last year.⁵³

The company estimates that funds received from students borrowing under third party private programs comprised about 1% of its higher education net revenues in 2009. According to the Post's SEC filings, as the private loan market deteriorated, Kaplan provided loans directly to some students under a third party institutional loan program.⁵⁴

Alta Colleges (Westwood)

Headquartered in Denver, Colorado, Alta College, Inc. (Alta) is the parent organization for Westwood College. According to its web site, Westwood College, founded in 1953, now has 17 campuses across California, Colorado, Georgia, Illinois, Texas and Virginia and an online campus. They have more than 15,000 students enrolled in degree programs ranging from business, design, technology, industrial services, justice and healthcare.

Westwood has an institutional loan product called Apex. The loan program was

⁵³ Stephen Burd, "The Washington Post and the Perils of For-Profit Colleges", New America Foundation (Nov. 8, 2010).

⁵⁴ The Washington Post Company Form 10-K (filed March 2, 2010).

the subject of at least one lawsuit filed in 2009 alleging various unfair and deceptive practices and violations of state banking laws. At the time the suit was filed in 2009, about 30% of Westwood's students used the Apex loan program.⁵⁵ The lawsuit alleged that the Apex product had no credit limit, was not credit-based and had an interest rate of 18%. In addition, the complaint alleged that the school representatives were instructed not to tell students about the 18% interest rate.⁵⁶ Westwood denied the allegations in the lawsuit. It was filed with an arbitration association, which refused to certify a class action. Since the lawsuit was filed, Westwood says that it has lowered the interest rate on the Apex loan to 10% for incoming students and 0 for existing students and graduates.⁵⁷

Anthem Education Group

Another school, Anthem Education Group describes on its web site an institutional loan program with no fee but with a 0 to 18% interest rate depending on the length of the loan.⁵⁸ Anthem Education Group, formerly known as High-Tech Institute, Inc. is the parent company of a collection of for-profit college campuses around the country.

⁵⁵ Justin Pope, "For-Profit Colleges Boost Lending", AP Impact (Aug. 14, 2009).

⁵⁶ Mensch v. Alta Colleges, Before the American Arbitration Association, Denver Colorado (Nov. 19, 2009).

⁵⁷ David A. Graham, "An Education in Institutional Loans", Newsweek (Nov., 20, 2009). See also <http://www.westwood.edu/facts/#Q3> (last checked December 2010).

⁵⁸ See <http://anthem.edu/institutional-loans.php>. (last viewed December 2010).

Tennessee Schools

Tennessee regulators sent questionnaires to the schools in their states requesting information about internal lending. The regulators told us that they collect this information and look at terms, but as of summer 2010, had not made the information public. There is no prohibition against internal lending in the state, but reporting is required. The information sent upon request by Tennessee regulators shows a wide range of internal lending products.

One school stated that its interest bearing loan was meant to be a last resort. The loan extended to 24 months from the start date and students had to be denied by an alternative lender in order to be eligible for the institutional loan. The interest rate is 15%.

Most of the information we received from the Tennessee regulators is from smaller schools. An exception is the Wyotech school (Corinthian). According to the Tennessee Higher Education Commission's summary, the Wyotech campus (Corinthian) requires students to pay the entire loan off during the period they are enrolled.

The information from the Tennessee regulators gives a sense of the wide range of institutional lending by schools of all sizes. Only a few of the schools reviewed were affiliated with large corporations. Many were small vocational schools, offering courses in vocations such as dog grooming, truck driving, and massage. These "in-school loan" products are often more complex and costly than they appear at first glance. For example, many of the Tennessee loans were interest free while the student is in school, but accrue interest on balances carried over after school. One of these products begins to accrue interest after graduation at 8% for students who are living out of state and 7% for those living in Tennessee.

The aggregate loan limit is \$15,000 in this case. Most require some payments while the student is in school.

VI. PROBLEMS WITH INSTITUTIONAL LOANS AND CONSEQUENCES FOR STUDENTS

High Default Rates

Although it is often difficult to obtain public information about the terms of institutional loans and credit performance, the information that is available regarding failure rates is shocking.

Corinthian states that it reports expected defaults on institutional loans as a discount to revenue. At the beginning of FY 2009, the company expected a loan default rate of about 50%.⁵⁹ After nearly 18 months of data in 2010, Corinthian announced an even higher discount rate, noting that the shift was toward students with lower credit quality. They adjusted the rate to 55% for FY 2009 and predicted a range of 56 to 58% in 2010.⁶⁰ The management noted that when Sallie Mae was making private student loans to Corinthian's students, the discount was about 25%.⁶¹

Despite the difficulties and financial distress that defaults generally mean for the students, the company still viewed these loan products as profitable and good business practices. In a February 2010 conference call,

⁵⁹ 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).

⁶⁰ Q42009 Corinthian Colleges Earnings Conference Call, Aug. 25, 2009.

⁶¹ Id.

Corinthian management said after describing the high write-offs, that they were "...feeling frankly good about what we're offering to our students."⁶²

ITT has been more secretive about its PEAKS and other institutional lending programs, but when asked in a January 2010 conference call about loan performance, the company acknowledged that it is not immune to what others are seeing in terms of difficulties with collections.⁶³ An analysis by the independent research firm Please Act Accordingly (PAA) uses the level of credit enhancement provided by ITT for PEAKS to conclude that those that graduate default at much higher rates than management has indicated. According to PAA, if the 30% subordination is meant to represent the actual loss experience, this would imply about a 37.5% default rate.⁶⁴ Analysts have estimated that ITT may assume close to a 45% loss rate on some institutional loans.⁶⁵ CEC stated that it expects default rates on institutional loans to approach 48%.⁶⁶

These are astronomical write-off rates. As discussed in greater detail below, the schools seem to view these loans more as "loss leaders" to keep the federal dollars flowing. However, the view from the student perspective is much different. Students do not care if the high default rates help the companies maintain high tuitions and present a more

attractive front 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.

While many students complain about aggressive collection tactics, we have found at least in some cases that the schools and servicers abandon the collection of institutional loans, particularly after a student withdraws from school. Many of the clients we see through the Student Loan Borrower Assistance Project face collection from the government or from third party lenders, but not necessarily from the institutional loan servicers once they have left school. This is further evidence that the schools view these as loss leaders, not worth the cost of collecting.

We have heard from many students that they are called into financial aid offices while they are in school to discuss why they are not making payments on institutional loans. The students are often confused about how these loans are different than the federal loans or private loans they may have taken out through companies such as Sallie Mae.

The confusion is compounded because so many schools use third party lenders to make or service the loans. Corinthian's relationship with Genesis is an example of this type of affiliation. Corinthian retains the risk, but Genesis is usually the company that collects. One student in an on-line complaint said he only found out long after he left the school that despite Genesis's aggressive collection efforts, "... Genesis is just a service center, not the owner of my loan."⁶⁷

⁶⁷ Complaint posted on "Everest Complaints Forum" (Sept. 12, 2010).

⁶² Corinthian Colleges Q2 2010 Earnings Conference Call Transcript (Feb., 2, 2010).

⁶³ ITT Educational Services, Inc. "Q4 2009 Earnings Call Transcript" (Jan. 21, 2010).

⁶⁴ Please Act Accordingly, "ESI Please Help Us Answer a Few Questions, Examining ESI's Leverage" (Oct. 26, 2010).

⁶⁵ Rolfe Winkler, "For-Profit Schools Put in Detention", Wall Street Journal (Aug. 21, 2010).

⁶⁶ FBR Capital Markets, "Proprietary Schools 101: Coverage Initiation" at 35 (Jan. 14, 2010).

Students face harm and confusion even if the schools choose not to pursue collection. The loan and subsequent default is reported on credit reports. Negative entries on credit reports bar many individuals from renting a home or even obtaining employment.

High Costs

Many of the products described above have high interest rates and origination fees, particularly for less credit worthy borrowers. For example:

- **Anthem Education Group:** No origination fee but with a 0 to 18% interest rate depending on the length of the loan.
- **DeVry Educard:** No origination fees, but 12% interest rate.
- **ITT PEAKS:** Origination fees ranging from 0 to 10% based on creditworthiness. Interest rates are variable ranging from the prime rate plus 11.5% for the least creditworthy borrowers to the prime rate plus 1.5%, not to exceed 25%.
- **CEC:** The company has said that the interest rate on institutional products is 8% for most students, although it says that online students pay no interest.⁶⁸

ITT has said that it does not direct the terms of the PEAKS trust loans. However, the company did say that underwriting is established by the lender and is similar to previous institutional loan programs.⁶⁹ According to ITT representatives, this “. . . should work for our student profile based upon where we set expectations for that demographic that we

⁶⁸Justin Pope, “For-Profit Colleges Boost Lending,” AP Impact (Aug. 14, 2009).

⁶⁹ITT Educational Services, Inc. Q4 2009 Earnings Call Transcript (Jan. 21, 2010).

know how to serve very well.”⁷⁰ This appears to be corporate language for “trust us.”

For comparison purposes, most federal student loans have fixed interest rates that are no higher than 6.8%. Private student loans generally have variable rates. As of mid-2010, the costs of institutional loans generally were higher than the range of rates for private student loans. The chart below compiled by Student Lending Analytics shows low and high interest rates for a number of large private student lenders.

Private Student Loan Interest Rates: July 2010

LENDER NAME	LOW RATE	HIGH RATE
Chase	4.14%	9.79%
Citibank	3.63%	11.38%
Citizens	3.35%	11.60%
Sallie Mae	2.88%	11.25%
SunTrust	4.13%	11.63%
Wells Fargo	3.50%	9.99%

Source: Student Lending Analytics, “Rates They Are A Changing . . .” (July 1, 2010).

This information undermines the credibility of institutions that claim that they offer institutional loans because they are less expensive for their students than third party loans. The reality is that the schools profited from the partnerships with third party lenders. Most schools did not end these programs because of concerns about students. Rather, they ended them because they had no choice when the third party lenders terminated the partnerships.

⁷⁰Id.

Predatory Terms

The problems with these products are not confined to cost. We found many other problems and predatory terms described below.

Mandatory Arbitration Clauses

Mandatory arbitration provisions are buried in many kinds of consumer contracts, including many proprietary school enrollment and loan agreements. These provisions require consumers to waive their right to use the court system, and instead limit consumers to resolving their disputes with the lender through a binding arbitration process. This constraint puts the lender in a stronger position. Under arbitration, little discovery is available. The lender can choose the arbitration service provider, and repeat players bring more business, leading to an incentive for the arbiter to rule for the lenders.

Mandatory arbitration clauses are controversial as they are hallmarks of predatory loans. The Center for Responsible Lending lists mandatory arbitration clauses as one of the seven signs of predatory lending.⁷¹ The 2010 Dodd-Frank legislation banned forced arbitration in mortgages and gives the new Consumer Financial Protection Bureau (CFPB) the authority to prohibit or impose conditions on other forced arbitration provisions involving consumer financial products or services.⁷²

⁷¹ Center for Responsible Lending, “Common Abuses: Seven Signs of Predatory Lending”, available at: <http://www.responsiblelending.org/mortgage-lending/tools-resources/seven-signs-of-predatory.html> (last checked December 2010)..

⁷² Pub. L. No. 111-203, signed into law on July 21, 2010.

Problematic Default Triggers

The loan agreements in many cases specify that a borrower will be considered in default with even one missed payment. Many also trigger default if a borrower files for bankruptcy, even if the student loan is not discharged in the bankruptcy. This is a provision, for example, in the DeVry Educard loan. The 2009 Westwood loan agreement triggers default if the student leaves school for any reason other than for graduation. Although most studies show that students who drop out are more likely to default, this provision ensures that this will be the case. The Westwood loan agreement also states that no notice of default is required.

Waiver of Defenses such as Infancy

The DeVry Educard agreement in Appendix 3 includes a clause that the agreement will be considered valid even if the borrower signed when she was under 18 years old. Essentially, the school is requiring borrowers to waive the traditional contract defense of infancy. Although the defense is well entrenched in the American legal system, it is not allowed for federal student loans. It is unclear why this should be the case for federal loans, but at least federal loans have a range of other borrower protections, loan limits, and fixed interest rates.

Schools Often Deny Transcripts or Terminate Students who Cannot Pay

Many of the schools such as DeVry require students to make payments on institutional loans while in school. According to the Tennessee Higher Education Commission’s summary, the Wyotech campus (Corinthian) requires students to pay the entire loan off during the period they are enrolled.

The problem is that many students 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. 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.

Lack of Regulation

There has been substantial confusion in many cases about who is regulating institutional products or who should be regulating the products. This will be clearer at the federal level as of July 2011 when the Consumer Financial Protection Bureau (CFPB) comes into being. The CFPB has authority over all private student loans made by non-banks.

Under the current federal regulatory scheme, federal regulators have oversight over credit products originated by most banks and federal credit unions. Institutional loan products do not fall in this category. The Federal Trade Commission, however, has authority over proprietary schools and should also have oversight and enforcement responsibility over these products. However, we do not know of any FTC enforcement in this area.

The Truth in Lending Act (TILA) should also apply to institutional loan products. There is no distinction for TILA coverage purposes based on whether the loan is originated by the educational institution or a third party creditor.⁷³ The only exclusions are if the loans are open-end credit or secured by real property. The schools should be considered private educational lenders as long as they regularly extend consumer credit that is subject to a

⁷³ 15 U.S.C. § 1650(a)(7).

finance charge or is payable by written agreement in more than four installments (not including a down payment).⁷⁴

School loans are clearly covered by TILA. The only exceptions are if the term of the extension of credit is ninety days or less or an interest rate is applied to the credit balance and the term of the extension of credit is one year or less.⁷⁵

Most of the products we reviewed should be covered by TILA. This means that the schools must provide required disclosures at three important points in time: 1) when students apply for credit, 2) when the credit is approved and 3) when the loan is consummated.

As of July 2011, the new Consumer Financial Protection Bureau will have rule writing and enforcement authority for TILA. The CFPB will also have more general authority to write rules related to the institutional loan products. Further, the agency will have enforcement authority over school lenders. In addition, the CFPB will have new federal supervisory authority over nonbank institutions, including school lenders.

The S.E.C is another federal agency that should have an interest in this issue. The S.E.C.'s mission is to protect investors. It should have learned from the subprime crisis that protecting investors and examining company filings more closely will often uncover serious problems also affecting consumers.

The creation of the CFPB should clarify the regulatory confusion and help protect consumers at the federal level. However, there is still confusion about state regulation.

⁷⁴ Reg. Z, 12 C.F.R. § 226.2(a)(17).

⁷⁵ Reg. Z, 12 C.F.R. § 226.46(b)(5)(iv). The second of these exceptions is applicable even if the credit is payable in more than four installments.

Schools may claim that the institutional loans they offer are not really “loans” and so are not within the jurisdiction of state banking agencies. Some label such loans “consumer financing” rather than student loans.⁷⁶ This is presumably an effort to evade disclosure requirements such as the federal Truth in Lending Act, but also to avoid application of certain state laws.

Most of these companies acknowledge that they could be subject to state banking laws. Corinthian, for example, noted in its August 2010 public filing that states might require it to get licenses or registrations.⁷⁷

If subject to state control, depending on the state, there are often usury limits and other substantive regulation of terms that apply to credit products. The schools would likely be required to comply with licensing laws in all states where they deliver education, including on-line education.

In a typical state, there may be a dozen or more statutes each intended to address a different kind of credit transaction. There are small loan laws that generally apply to loans of \$25,000 or even higher amounts in some states. There are also installment loan laws and retail installment sales acts (RISA). The substance of the RISA laws varies considerably, but most require disclosures and an itemization of charges. Many set maximum rates and also limit late charges, prepayment rights and other terms.

We contacted a number of state regulators and with one exception were told that they do not specifically track school institutional lending programs. New York regulators with the Bureau of Proprietary School Supervision, for

⁷⁶Justin Pope, “For-Profit Colleges Boost Lending”, AP Impact (Aug. 14, 2009).

⁷⁷Corinthian Colleges, 10-K (Filed Aug. 20, 2010).

example, told us in spring 2010 that they do not have responsibility under the state education law to research or report on student lending in the proprietary school sector. They said that Attorney General Cuomo had lobbied for a bill to create transparency in the student lending field. The bill passed and responsibility and authority was placed with the Office of Higher Education. However, as of early 2010, it was unfunded and the staff necessary to carry out those tasks could not be hired. As a result, institutional lending, they said, is not tracked.

Accounting Tricks and Traps

Many schools have developed accounting systems that hide the true loss rates of the institutional loans and how these loans are impacting their companies. For example, many have used the institutional products as a way to make the company’s bad debt situation look better, at least on the surface.

This is a major reason why most proprietary school companies do not put the institutional loans in the bad debt category. Instead, they subtract the amount of institutional loans from sales so that it is treated as if the company never received the revenue. Revenues are lower, but given that federal dollars are still flowing, the companies are generally still profitable. Corinthian, for example, reports expected defaults on institutional loans as a discount to revenue.

ITT is using the PEAKS program in a similar way. If ITT had used its own funds for institutional loans, it would have likely had to use its own balance sheet to do so. Instead, by setting up the PEAKS trust, the loans are not originated by the school and the school can delay recognizing the loans as bad debt. According to PAA, bringing PEAKS “on

balance sheet” would likely increase disclosure requirements and make investors more aware of the inherent leverage on ITT’s balance sheet.⁷⁸

Much of the prior bad debt from institutional loans was taken off the books because ITT used the new PEAKS financing to offer refinancing of prior institutional loans that students took out before their second year.⁷⁹

Nevertheless, as many analysts have pointed out, the PEAKS trust is not really a private loan arrangement since ITT retains all of the credit risk associated with the loans. According to PAA, when it created the PEAKS trust, ITT kicked the can down the road by pushing the recognition of credit losses on private loans out a few years.⁸⁰ This reduces bad debt in the short-term, but it does not decrease eventual credit exposure for the loans. It is unclear what will happen when the current PEAKS structure is tapped out. ITT has said that it expects that the current capacity of the PEAKS trust will hold into 2011, although it is not sure how far into 2011.⁸¹

Overall, these accounting tactics not only lower the booked bad debt expense, but also understate leverage.⁸² All of this makes the companies more attractive investments, but in

many cases these accounting methods obscure real problems with the companies.

The S.E.C. has begun to take notice of some of these issues, although we do not know of any formal investigations to date.⁸³ For example, the S.E.C. has asked ITT to justify its conclusion that it is not the primary beneficiary of the PEAKS trust. The agency requested information about the nature and extent of the company’s involvement in the activities of the trust, among other questions.⁸⁴

The S.E.C. also asked about ITT’s arrangements in which it guarantees repayment of charged off loans above a certain percentage of the loans made. Among other responses, ITT agreed to expand certain disclosures. Hopefully the SEC’s inquiry will penetrate the smokescreen of the trust, the recourse, the originators, and other troubling issues.

VII. UNDERSTANDING SCHOOL MOTIVES FOR INSTITUTIONAL LENDING

The 90–10 rule is critical to understanding why companies have created institutional loan programs. The rule was modeled after a

⁷⁸ Please Act Accordingly, “ESI: SEC Correspondence Suggests Heightened Scrutiny of Accounting Treatment of PEAKS” (Nov. 30, 2010).

⁷⁹ ITT Educational Services, Inc. “Q42009 Earnings Call Transcript” (Jan. 21, 2010).

⁸⁰ Please Act Accordingly, “ESI Reports a Solid Quarter, New ‘Private student Loan’ Program ‘Optically Looks good, Economically Kicks the Can Down the Road” (March 12, 2010).

⁸¹ ITT Educational Services, Inc. “Q42009 Earnings Call Transcript” (Jan. 21, 2010).

⁸² See generally Please Act Accordingly, “ESI: SEC Correspondence Suggests Heightened Scrutiny of Accounting Treatment of PEAKS” (Nov. 30, 2010).

⁸³ The S.E.C. has also investigated proprietary schools for other matters, including an investigation of the Apollo Group for allegedly misrepresenting income by failing to account for losses resulting from student withdrawals. State officials in Oregon filed a securities fraud lawsuit against Apollo based on similar allegations. See, e.g., Bill Graves, *The Oregonian*, “Oregon Sues University of Phoenix Parent Apollo Group Alleging Fraud that Hurt PERS” *OregonLive.com* (Oct. 18, 2010).

⁸⁴ These letters are described and analyzed in Please Act Accordingly, “ESI: SEC Correspondence Suggests Heightened Scrutiny of Accounting Treatment of PEAKS” (Nov. 30, 2010).

similar safeguard enacted during the Korean War. The provision was designed to ensure that schools were of sufficient quality to attract some students who would pay tuition.⁸⁵ According to a 1978 U.S. Supreme Court decision upholding the veterans “85–15” rule, “The requirement of a minimum enrollment of students not wholly or partially subsidized by the Veterans’ Administration was a way of protecting veterans by allowing the free market mechanism to operate.”⁸⁶

Another important rationale for the current rule is that outcomes are worse at schools that rely heavily on government assistance. A 1997 GAO study reached this conclusion, finding that proprietary schools that rely more heavily on student assistance tend to have poorer student outcomes, including lower completion and placement rates and higher default rates.⁸⁷ The GAO also found that these schools are also more likely to push students into taking out loans that they will not be able to repay.

The current version of the 90–10 rule requires proprietary schools to show that at least 10% of their revenues come from a source other than Department of Education student assistance.⁸⁸ The 90% category includes only Department of Education federal assistance. This means that other types of federal student aid, such as Department of Defense tuition

assistance and Veterans Department G.I. Bill assistance, is not counted toward the 90%. The chart on the next page from the U.S. Government Accountability Office summarizes how the 90–10 calculation should work.

The 90/10 rule was previously an institutional eligibility requirement. Due to Congressional changes in 2008, it is now part of the program participation agreement (PPA) that schools must sign to participate in the federal aid programs.⁸⁹ As a result of this change, an institution that does not meet the 90/10 requirement no longer loses its eligibility to participate in the federal assistance programs. Instead, the institution’s participation becomes provisional for two fiscal years. If the institution does not satisfy the requirement for two consecutive fiscal years, it will then lose its eligibility for at least two fiscal years. Despite these lesser penalties, schools desperately try to avoid having to tell investors that they are jeopardizing federal funds by getting too close to the 90% line.

The industry has pushed hard to include more revenue sources in the 10% category and to dilute the potential penalties for violations. For example, when loan limits were raised in 2008, Congress allowed increased federal loan revenues to be temporarily counted as part of the 10% category. In 2008, Congress also allowed schools to count in the 10% category the net present value of any institutional loans made before July 1, 2012. After that, only the value of actual payments received counts. This is yet another incentive for schools, at least in the short-term, to make these loans regardless of whether students repay them. The school industry is fighting hard to extend these “temporary” relief measures beyond 2011.

⁸⁵ See U.S. Senate Health, Education, Labor and Pensions Committee, “Benefitting Whom? For-Profit Education Companies and the Growth of Military Educational Benefits” at 8 (Dec. 8, 2010).

⁸⁶ *Cleland v. National College of Business*, 435 U.S. 213 (1978).

⁸⁷ U.S. Gen. Accounting Office, *Proprietary Schools: Poorer Student Outcomes at Schools That Rely More on Federal Student Aid*, GAO/HEHS-97-103 (June 1997).

⁸⁸ 34 C.F.R. § 668.28.

⁸⁹ 20 U.S.C. § 1094 (a)(24); 34 C.F.R. § 668.14(b)(16), 668.28.

Background: 90/10 Calculation



No More than 90 Percent of a For-Profit School's Total Revenues May Be Obtained from Federal Student Aid

- Only revenues received for a school's educational and institutional charges, such as tuition, fees, and certain required course materials, are included in its 90/10 calculation.*
 - Other revenues, such as those from vending machines and parking lots, are excluded from the calculation.**
- The 90/10 rate must be calculated using a cash basis of accounting.***

NO MORE THAN 90 PERCENT	AT LEAST 10 PERCENT
<p>Only revenues from federal student aid programs authorized by Title IV of the Higher Education Act are included, such as:</p> <ul style="list-style-type: none">• Pell Grants,• Stafford Loans, and• Federal Work Study funds.	<p>Revenues counted include:</p> <ul style="list-style-type: none">• cash payments from students,• private student loans (including payments for loans made by schools),• state educational grants,• federal education assistance payments for military personnel and veterans, and• federal and state job training grants.

*Federal student aid revenues in excess of a school's educational and institutional charges must be excluded from a school's calculation.

**For more information, see 20 U.S.C. §1094(d) and 34 C.F.R. § 668.28.

***On a cash basis of accounting, revenues are recorded when they are received regardless of when they are earned. Outside of the 90/10 calculation, schools generally track revenues on an accrual basis of accounting, where revenues are recorded when they are earned.

Source: U.S. Government Accountability Office, "For-Profit Schools: Large Schools that Specialize in Healthcare are More Likely to Rely Heavily on Federal Student Aid," GAO-11-4 (October 2010).

The third party loan boom was critical for schools seeking revenues to fill up the 10% side of the equation. When the third party lending market fell apart, many companies crept much closer to the 90% line. Other factors also contributed to the growth of federal student assistance to proprietary schools, including the elimination of a rule

that limited federal aid for schools that offered primarily distance (or online) education courses.

The chart on the next page shows how the percentage of the school revenues from Department of Education aid has grown at many proprietary school companies since the death of most third party loan programs.

90–10 Calculations

	FY06	FY07	FY08	FY09
Apollo Group	64.0%	69.0%	82.0%	86.0%
Career Education	59.3%	62.7%	69.2%	80%
Corinthian Colleges	75.3%	75.2%	81.0%	88.9%
DeVry	62.0%	65.0%	71.0%	80.0%

Source: FBR Capital Markets, “Proprietary Schools 101: Coverage Initiation” at 18 (Jan. 14, 2010). Career Education’s 90–10 calculation is year to date as of September 30, 2009. DeVry’s calculation is for undergraduate students only. The FY09 DeVry figure is an estimate.

Industry analysts and the schools are generally up-front about their motives and strategies. A 2009 AP article quotes an industry analyst saying that financially it makes sense to make the institutional loans, even if you write off the loan right away.⁹⁰ FBR Capital Markets analysts note that the expected loss rate on institutional loans makes them unprofitable from the start.⁹¹ However, the analysts state that they view this rate more as a discount to revenues than as a true loss. They state further that this discount is necessary not only to help students fund their tuition payments, but also to help schools comply with 90–10.⁹²

Corinthian executives announced in 2010 that unless the 90–10 rule is amended, the company’s primary alternative for staying in

compliance is to charge higher tuitions. They said they would increase tuition only to the level needed to meet 90–10 and that this could mean a price increase at various schools of up to 20%.⁹³ They said that the increase in tuition would be funded “fundamentally” from institutional loans and that they might even raise the amounts students can borrow.⁹⁴ The company executives described a “sophisticated” model that allows them to increase pricing only to the level that is needed to meet 90–10. They do this by checking program by program within schools and then increasing tuition as needed.⁹⁵

This is from a company that is projecting up to 58% default rates for institutional loan products. When asked about alternatives to price increases, Corinthian executives said the list is pretty short. They also acknowledged that tuition increases are not in the best interests of students.⁹⁶

“To increase the likelihood that the last institutions will stay below the 90% threshold in fiscal 2012 we are calmly evaluating whether to institute a substantial price increase in the third quarter of fiscal 2011. We do not believe such a price increase is in the best interest of our students.”

—Corinthian Colleges Former CEO Peter Waller, Q1 2011 Earnings Conference Call Transcript (Nov. 2, 2010).

The Corinthian announcement correlates with a fiction spread by the industry that compliance with 90–10 necessitates tuition

⁹⁰ Justin Pope, “For-Profit Colleges Boost Lending”, AP Impact (Aug. 14, 2009).

⁹¹ FBR Capital Markets, “Proprietary Schools 101: Coverage Initiation” at 35 (Jan. 14, 2010).

⁹² Id. (referring to CEC institutional loans).

⁹³ Corinthian Colleges Q1 2011 Earnings Conference Call Transcript (Nov. 2, 2010).

⁹⁴ Id.

⁹⁵ Id.

⁹⁶ Id.

increases. For example, the Association of Private Sector Colleges and Universities has referred to a “90–10” problem that can only be fixed with a dramatic increase in tuition.⁹⁷ Yet the costs of attending most proprietary schools already soar above those at public institutions.⁹⁸

This supposed connection between tuition and the 90–10 rule distorts the intent of the rule. The rule does not in any way require schools to charge students more than the amounts available through federal aid. Rather, as discussed above, it is intended to ensure that a school can prove itself in the private market. The idea is that there should be some students who can pay for the schools other than with federal grants and loans, including not only through student contributions, but also from employers or other private sources such as private scholarships.

The more appropriate response for schools having trouble complying with 90–10 is to reduce tuition in order to attract some students who can or will pay without federal aid. There are proprietary schools that have followed this route and continued to grow. American Public Education, for example, has seen enrollment increases of 31% each year even though its CEO says that it has not increased undergraduate tuition in almost ten years.⁹⁹

⁹⁷ Association of Private Sector Colleges and Universities, “Legislative Issues” (last checked in December 2010).

⁹⁸ The Education Trust, “Subprime Opportunity: The Unfulfilled Promise of For-Profit Colleges and Universities” (Nov. 23, 2010).

⁹⁹ Hilary Kramer, “For-Profit Ed Goes to the Head of the Class”, *Forbes.com* (Dec. 1, 2010).

“We have not increased our undergraduate tuition in almost 10 years, unlike some schools that regularly increase tuition to drive incremental revenue growth and margins.”

—American Public Education CEO Dr. Wallace E. Boston Jr., quoted in Hilary Kramer, “For-Profit Ed Goes to the Head of the Class”, *Forbes.com* (Dec. 1, 2010).

The growth of institutional lending is not only about 90–10. It is also more simply a way for schools to keep revenues of all types flowing so that profits remain high and the companies remain attractive to investors. In September 2010, Senator Richard Durbin of Illinois asked the question in a Senate floor speech why Corinthian is willing to lend money to students when they know these students are already defaulting on their government loans. He answered the question by saying, “The company is willing to take this loss of \$75 million in private student loan defaults because these loans help ensure the Federal loans and Pell grants will keep coming in to these students, despite the fact they are in over their head in debt and have nowhere to turn.”¹⁰⁰

VIII. RECOMMENDATIONS

1. Strengthen the 90–10 Rule and Study Its Effects

There are many rationales for the 90–10 rule as described above. Ultimately, the rule is useful only if it helps promote higher quality outcomes for students. A 1997 GAO study reached this conclusion, finding that proprietary schools that rely more heavily

¹⁰⁰ Cong. Record S7587-90 (Sept. 28, 2010).

on student assistance tend to have poorer student outcomes. As indicators of school performance, the GAO used data on program completion, training-related job placement and student loan default rates.¹⁰¹ The GAO also found that these schools are more likely to push students into taking out loans that they will not be able to repay.

We urge policymakers to study this issue further, focusing on whether the 90–10 rule is useful in improving outcome measures. The GAO study from 1997 is the type of study that is most needed.

In its present form, however, the rule is easily gamed by schools. Schools make unaffordable loans as a way of filling up the 10% with vapor revenues derived from loans that will never be repaid. The rule in its present weak form even creates perverse incentives for schools to make loans without regard to ability to pay and to increase tuition. When a school subverts the rule in one of these ways, the rule no longer ensures that the school is actually attracting some students who will pay tuition.

An evaluation of the rule in its present form is unlikely to be a true measure of its usefulness. It is essential to strengthen the rule in order to ascertain whether it helps improve quality outcomes at proprietary schools.

There are many ways to put some teeth back into the 90–10 rule and reduce the perverse incentives that it creates in its current form. These include:

- Including all federal funding in the 90% category.

¹⁰¹ U.S. Gen. Accounting Office, *Proprietary Schools: Poorer Student Outcomes at Schools That Rely More on Federal Student Aid*, GAO/HEHS-97-103 (June 1997).

- Prohibiting schools from counting in the 10% category loans in which the school has a substantial portion of the credit risk. These loans should either be in the 90% category if this is meant to represent school-related funding or not counted at all.¹⁰²
- Ending the temporary relief for schools that allows them to temporarily count increased federal loans revenues as part of the 10% of non-federal revenues and to count in the 10% category the net present value of any institutional loans made before July 1, 2012. These are incentives for schools, at least in the short-term, to make these loans regardless of whether students repay them.
- Changing the required ratio depending on a school's federal and private loan default rates. For example, a default rate of more than 15% would require an 85–15 ratio. A default rate of less than 10 to 15 would permit a 90–10 ratio and so on.

If the 90–10 rule, even once it is strengthened, is not shown to meet its intended purpose, or if the perverse incentives created by the rule cannot be eliminated and are found to outweigh the benefits, Congress should rethink whether additional or different policies should be adopted. Regardless of whether 90–10 is in place, stronger, more targeted outcome measures, such as the proposed “gainful employment” standard, are essential, as the 90–10 rule has been insufficient to ensure the quality of proprietary school programs.

¹⁰² See generally Ben Miller, “Fuzzy Math in the 90/10 Rule”, *Quickanded.com* (Nov. 1, 2010).

2. Regulators Must Provide Aggressive Oversight of Institutional Loans

Institutional loan products have generally fallen through regulatory cracks. Regulators, both state and federal, must evaluate institutional loan programs and enforce relevant laws. Among other actions, we recommend:

- **The FTC (and in July 2011 CFPB) should immediately request that the schools provide detailed information about the various loan programs so that the agencies can take appropriate enforcement actions.** The agencies should focus not only on the high rates and fees, but also problems with unfair or abusive default triggers, mandatory arbitration clauses, and waiver of important rights such as infancy defenses. A key issue is developing an “ability to pay” standard and mandatory underwriting guidelines so that entities will face penalties for making loans that they know will fail at very high rates.
- **Bank regulators should review the involvement of entities within their oversight responsibility that are partners in institutional loans and credit unions that have begun to offer their own school loan products, in some cases in affiliation with schools.**
- **State education and banking departments should review and enforce banking licensing and substantive laws.**
- **The Federal Reserve Board (FRB) (and in July 2011 the CFPB) and the FTC using its authority under the FTC Act should pass comprehensive unfairness standards applicable to private student loans, including institutional loans.**

The unfairness standards should prohibit student loans to students who do not have a reasonable expectation of 1) completing the requirements to obtain the certification necessary to obtain a paying job for which the schooling is provided, or 2) repaying all of the student loan debts incurred for that schooling because of either i) the insufficiency of the reasonably expected income from the job for which the schooling to allow the student to repay all of the loans according to their terms, or ii) some other reason reasonably foreseeable at the time the loan was originated.

- **Students should be able to raise as defenses to student loans, the breach of these unfairness standards described above.**
 - **The FRB (and in July 2011 the CFPB) and the FTC should review whether the schools are complying with TILA disclosure requirements. Federal and state regulators should review institutional loan programs for possible violations of unfair and deceptive consumer protections laws.** Possible violations include failure to disclose the nature and terms of loan programs.
 - The S.E.C. and other agencies, along with investors, need to ask more questions about these products and the extent to which they are masking serious problems at many proprietary education companies.
- ## 3. Ensure That Schools are Held Accountable Even if they Sell Institutional Loans or Use Other Entities to Make the Loans

The FTC 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 for-profit trade schools that defraud students or shut down unexpectedly.¹⁰³ The regulation requires a private student loan provider to include a clause in the loan documents making the lender responsible for any fraud or breach of contract by the school, up to the amount of the loan. Some providers of private student loans have violated this regulation and failed to include the clause in the loan documents.¹⁰⁴ To help prevent this problem from surfacing again, all lenders, including school lenders, must be required to include the FTC Holder notice in their products going forward. Further, for those receiving government funds, the term should be implied in all contracts previously made.

This is especially relevant for institutional loan programs where the schools are using third parties to originate the loans.

In other cases, the schools may originate, but then sell the loans. To help provide relief for harmed borrowers, we recommend that there be full assignee liability for all institutional student loans and all other consumer loans as well.¹⁰⁵

¹⁰³ 16 C.F.R. §433.2.

¹⁰⁴ See generally 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.studentloan-borrowerassistance.org/blogs/wp-content/www.studentloanborrowerassistance.org/uploads/File/Report_PrivateLoans.pdf.

¹⁰⁵ For more details on extending assignee liability and other recommendations to protect consumers, see National Consumer Law Center, “Time to Update the Credit Practices Rule” (Dec. 2010), available at: http://www.nclc.org/images/pdf/debt_collection/credit-practices-rule-update.pdf.

4. The Department of Education Must Examine Institutional Loan Programs and the Impact on Federal Student Aid

The Department of Education should be particularly concerned about the ways in which schools are using institutional loan programs to evade 90–10-related sanctions. As both a legal and policy matter, schools should face sanctions for taking actions that are clearly not in the best interests of students. In particular, the Department should investigate schools that are setting tuitions school by school and even program by program in order to ensure compliance with 90–10.

5. Track Private Loan Default Rates

There is no comprehensive set of data about private student loan default rates, including institutional loans. The rates cited in this report are disclosed only by public companies in their public filings. Schools that create these programs must be required to provide students not only with the loan term information required under TILA, but also with information about default rates and other performance indicators. This information should be easily available to students. Better information alone will not solve the problem, but it may deter some students from taking out these loans and it will also help generate information for policymakers and enforcement agencies.

A key way to improve information about private student loans, including institutional loans, is to include private loans in the National Student Loan Data System (NSLDS). Consumers would then be able to see all their loans, both federal and private, in one place and receive counseling based on their total student loan debt.¹⁰⁶

¹⁰⁶ This recommendation and related recommendations

6. Provide Relief for Financially Distressed Students

If enacted, many of the recommendations discussed above will improve quality at proprietary schools, benefitting future students. In the meantime, there are countless student borrowers buried in debt with nowhere to turn. A key barrier to relief is that both third party and institutional student loans are nearly impossible to discharge in bankruptcy.

A major first step is to reform the bankruptcy laws so that student borrowers can discharge private student loans without having to go through the complex and nearly impossible “undue hardship” process.

Other non-bankruptcy loss mitigation strategies should also be considered. For example, schools with very high institutional loan default rates could face elimination from participation in federal student loan programs. This would be a program similar to the current federal student loan default rate sanction program.

There are also ways to expand relief through the federal student loan programs. This does not directly address institutional loans. However, most students with institutional loans also have federal loans. Therefore we recommend that the Department and Congress if necessary expand the existing statutory discharges so that broad relief is available

to victims of proprietary school abuses. Even without additional action, the Department currently has general authority to compromise loans.¹⁰⁷ This is critical to ensure not only that future abuses are deterred, but also so that those already harmed can get relief.

CONCLUSION

It is unconscionable that schools that claim to serve low-income students are piling these students with even more debt that they cannot repay. Although the companies repeatedly talk about ways in which the institutional loans are in the best interests of the companies and their investors, the most important question for students is whether these new products are in their best interests.

Until the companies can show that their students are completing their educations at high rates, getting good jobs, and repaying these loans, the answer has to be that these products are not in the best interest of students. They are just another way that companies, enabled by government funds, are piling more debt on vulnerable members of our society. This is not only unconscionable, but ultimately self-defeating as these individuals not only fail to get ahead through education as promised, but are buried in debt.

are discussed in greater detail in The Project on Student Debt, “Student Debt and the Class of 2009) (Oct. 2010).

¹⁰⁷ 31 U.S.C. § 3711 (General authority to compromise government debts); 34 C.F.R. § 30.70.

APPENDIX 1

Questions for Schools from NCLC's Student Loan Borrower Assistance Project

Name of School/Company:

Your Name and Contact Information:

Date of Response:

1. Please describe any institutional credit products you currently offer to your students (this should include all products that your school originates, including loans and revolving credit accounts).
2. When did you start offering these products? (Please specify for each product)
3. Did you offer other products in the past that you no longer offer to your students? If so, please specify and describe why you no longer offer these products.
4. Do you have an arrangement or arrangements with other entities, such as banks or other financial institutions, to offer credit products to your students? If so, please describe.
5. Is information about the products described above publicly available? If so, please specify location of such information, including preferred lender lists.
6. Please send a sample credit agreement for each product described above.
7. For each product described above, please provide the following information:
 - a. Eligibility requirements
 - b. Summary of credit profiles (including average credit scores) of borrowers
 - c. Summary of basic terms, including interest rates and fees
 - d. Summary of repayment provisions including when repayment starts, availability of deferment and forbearance etc.
8. Do you use in-house or third party collectors to collect from delinquent borrowers? Please explain if you use both.

APPENDIX 2

From ITT Albany, NY 2010 Catalog, May 11, 2010

Private Loan Programs

PEAKS Private Student Loan Program

Loans under the PEAKS Private Student Loan Program (the "PEAKS Program") are made available to eligible students by Liberty Bank, N.A. The PEAKS Program was designed to help eligible students fill the funding gap when federal and state student financial aid sources do not fully cover the students' cost of education. PEAKS Program loans are not guaranteed by the federal government and may cost an eligible student more than federal loans. Under the PEAKS Program, an eligible student may borrow from \$1,000 up to the cost of the student's ITT Technical Institute education, less all federal and state grant and loan aid received by the student and his or her parents for the student's ITT Technical Institute education, not to exceed:

- \$35,000 in total for an associate degree program;
- \$60,000 in total for a bachelor degree program (including any amount for an associate degree program), and
- \$25,000 for a graduate degree program.

A student borrower can defer payments of principal and interest on his or her PEAKS Program loans during the student's enrollment. A student borrower must begin repaying his or her PEAKS Program loans:

- six months after the student graduates, unless he or she enrolls in another program at an ITT Technical Institute or Daniel Webster College on at least a half-time basis;
- three months after the student ceases to be enrolled at least half-time for any reason other than graduation, unless he or she enrolls in a program at an ITT Technical Institute or Daniel Webster College on at least a half-time basis; and
- in any event, 48 months following the first disbursement of his or her first PEAKS Program loan.

The maximum repayment period for PEAKS Program loans is 10 years. To qualify for a PEAKS Program loan:

- ITT Technical Institute must have received an Institutional Student Information Report ("ISIR") from the DOE for the borrower, which ISIR has been approved for Title IV federal student financial aid eligibility by the DOE;
- the borrower must have a U.S. address and a U.S. Social Security number, and must successfully meet Office of Foreign Asset Control screening requirements;
- the borrower must meet the lender's creditworthiness requirements;
- the borrower must be of majority age in his or her state of residence;
- the student must be accepted for enrollment or enrolled on at least a half-time basis at, or have graduated from, an ITT Technical Institute; and
- the student must have completed by the loan application date a minimum of 20 quarter credit hours (or the equivalent) of credit for college-level courses.

As of the date this catalog was published:

- an origination fee ranging from 0% to 10% of the loan amount was charged on a PEAKS Program loan, based on the creditworthiness of the borrower;
- the interest rate charged on a PEAKS Program loan was a variable rate that ranged from the prime rate plus 11.5% for the least creditworthy eligible borrowers to the prime rate plus 1.5% for the most creditworthy eligible borrowers, not to exceed 25% per annum; and
- the interest rate charged on a PEAKS Program loan adjusts monthly based on the prime rate that is in effect on the 17th day of the immediately preceding month (or if not published on that day, the next day on which the prime rate is published).

The following model disclosure form for loans under the PEAKS Program contains information that the Federal Reserve Board requires to be disclosed to students and their families:

PRIVATE EDUCATION LOAN APPLICATION AND SOLICITATION DISCLOSURE

CREDITOR:
LIBERTY BANK, N.A.
 25201 Chagrin Blvd. #120
 Beachwood, OH 44122

Loan Interest Rates & Fees

Your starting interest rate will be between

4.75% and 14.75%

After the starting rate is set, your rate will then vary with the market.

Your Starting Interest Rate (upon approval)

The starting interest rate you pay will be determined after you apply. It will be based on your credit history. If approved, we will notify you of the rate you qualify for within the stated range.

Your Interest Rate during the life of the loan

Your rate is variable. This means that your actual rate varies with the market and could be lower or higher than the rates on this form. The variable rate is based upon the U.S. Prime Rate, as published by *The Wall Street Journal*. For more information on this rate, see Reference Notes.

Although the rate will vary after you are approved, **it will never exceed 25%** (the maximum allowable for this loan).

Loan Fees

Loan Origination Fee: The fees that we charge to make this loan range from 0% to 10% of the total loan amount.

Late Charge: \$10.00 for each payment that is more than 15 days late.

Loan Cost Examples

The total amount you will pay for this loan will vary depending upon when you start to repay it. This example provides estimates based upon two (2) different repayment options available to you while enrolled in school and during your six-month grace period.

Repayment Option (while enrolled in school)	Amount Provided (amount provided directly to your school)	Interest Rate (highest possible starting rate)	Loan Term (how long you have to pay off the loan)	Total Paid Over 10 Years (includes associated fees)
1. DEFER PAYMENTS Make no payments while enrolled and during grace period. Interest will be charged and added to your loan.	\$10,000.00	14.75%	10 years Starting after the deferment period	\$30,432.72
2. PAY ONLY THE INTEREST Make interest payments but defer payments on the principal amount while enrolled in school.	\$10,000.00	14.75%	10 years Starting after the deferment period	\$25,150.83

About this example

The repayment example assumes that you remain in school for 2 years and have a 6-month grace period before beginning repayment. It is based on the **highest starting rate and the highest origination fee currently charged**. Repayment will last 10 years, starting once the initial principal payment is made.

PKS 2010 A

Federal Loan Alternatives

Loan program	Current Interest Rates by Program Type	
PERKINS For Students	5.0% fixed	
STAFFORD For Students	5.6% fixed	Undergraduate subsidized
	6.8% fixed	Undergraduate unsubsidized and Graduate
PLUS For Parents and Graduate/Professional Students	8.5% fixed	Federal Family Education Loan
	7.9% fixed	Federal Direct Loan

You may qualify for Federal education loans. For additional information, contact your school's financial aid office or the Department of Education at:

www.federalstudentaid.ed.gov

Next Steps

- Find out about other loan options.**
Some schools have school-specific student loan benefits and terms not detailed on this form. Contact your school's financial aid office or visit the Department of Education's web site at: www.federalstudentaid.ed.gov for more information about other loans.
- To apply for this loan, complete the application and the self-certification form.** You may get the certification form from your school's financial aid office. If you are approved for this loan, the loan terms will be available for 30 days (terms will not change during this period, except as permitted by law and the variable interest rate may change based on the market).

REFERENCE NOTES

Variable Interest Rate:

- This loan has a variable Interest Rate that is based on a publicly available index, the U.S. Prime Rate as published in *The Wall Street Journal*. Your rate will be calculated each month by adding a margin between 1.5% and 11.5% to the current index, rounded up to the nearest one-eighth of one percent (0.125%).
- The rate will not increase more than once a month, but there is no limit to the amount that the rate could increase at one time.

Borrower Eligibility Criteria

- Must be a U.S. citizen/national or eligible noncitizen with a U.S. address and a valid U.S. Social Security number.
- Must be a returning student as defined by the school
- Must be enrolled or accepted for enrollment at least half time as defined by the school at, or have graduated from, either an ITT Technical Institute or a Daniel Webster College campus
- Must be the age of majority in your state of residence at the time of application

Bankruptcy Limitations

This is an education loan. If you file for bankruptcy, you may still be required to pay back this loan.

More information about loan eligibility and repayment deferral or forbearance options is available in your loan application and loan agreement.

PKS 2010 A

APPENDIX 3

EDUCARD is DeVry Inc.'s interest bearing installment loan program that is available only to students attending DeVry University, DeVry Institute of Technology, or Chamberlain College of Nursing ("the school"). The objective of EDUCARD is to provide a loan for students to pay tuition and book costs for attendance at DeVry or Chamberlain. It offers students a monthly payment plan that is worked out in accordance with the students' financial circumstances. The EDUCARD Plan requires students to apply financial aid and monthly cash payments to their account to reduce any outstanding EDUCARD balance while enrolled. The school acts as an agent for DeVry Inc. in receiving payments and appropriately transferring credit balances to reduce the EDUCARD balance.

Upon graduation or other termination of enrollment, a student may have a remaining balance on his/her EDUCARD account. In that case, the DeVry Inc. EDUCARD account converts to an installment loan and requires that the student pay any outstanding balance on the EDUCARD account within twelve months of the time attendance discontinued.

Any questions relating to the completion of this form or the EDUCARD plan should be directed to the school's Student Finance Office.

EDUCARD Plan Application and Contract

RETAIL INSTALLMENT APPLICATION

TO BE COMPLETED BY ALL STUDENTS STUDENT INFORMATION	STUDENT'S NAME:		FIRST	MIDDLE	LAST	DATE OF BIRTH		
	HOME ADDRESS:		STREET	CITY	STATE	ZIP CODE	(AREA CODE) HOME PHONE ()	
	YEARS AT PRESENT ADDRESS	LIVE WITH PARENTS YES <input type="checkbox"/> NO <input type="checkbox"/>	SOCIAL SECURITY NUMBER / /		DRIVER'S LICENSE # AND STATE			
	FIRM NAME OR EMPLOYER'S NAME						YEARS THERE	
	EMPLOYER'S ADDRESS:		STREET	CITY	STATE	ZIP CODE		
	(AREA CODE) BUSINESS PHONE ()	POSITION OR TITLE			NATURE OF BUSINESS			
	PRESENT ANNUAL EARNINGS		OTHER INCOME: INCOME FROM ALIMONY, CHILD SUPPORT OR MAINTENANCE PAYMENTS MAY BE EXCLUDED UNLESS RELIED UPON FOR CREDIT.					
	\$		SOURCE		\$ AMOUNT			
	PARENT'S NAME: (ALL STUDENTS MUST COMPLETE INFORMATION)							
	FATHER			AGE	MOTHER			AGE
	PARENT(S) HOME ADDRESS:		STREET	CITY	STATE	ZIP CODE		
	(AREA CODE) HOME PHONE ()	YEARS AT PRESENT ADDRESS	OWN HOME <input type="checkbox"/> RENT <input type="checkbox"/>	NO. OF DEPENDENTS	SOCIAL SECURITY NUMBER / /			
	PREVIOUS ADDRESS (IF LESS THAN 5 YEARS):		STREET	CITY	STATE	ZIP CODE		
	STUDENT'S PERSONAL REFERENCES:		ADDRESS	CITY	STATE	ZIP CODE	TELEPHONE #	
	1. NAME (RELATIVE OTHER THAN PARENT)							
2. NAME (OTHER THAN RELATIVE)		ADDRESS	CITY	STATE	ZIP CODE	TELEPHONE #		
3. NAME (OTHER THAN RELATIVE)		ADDRESS	CITY	STATE	ZIP CODE	TELEPHONE #		
TO BE COMPLETED BY COSIGNER, IF NO COSIGNER, PROVIDE PARENT INFO. COSIGNER INFORMATION	NAME OF COSIGNER: (IF NO COSIGNER, GIVE PARENT INFORMATION)					SOCIAL SECURITY NUMBER / /		
	ADDRESS OF COSIGNER:		STREET	CITY	STATE	ZIP CODE	(AREA CODE) HOME PHONE ()	
	COSIGNER'S EMPLOYER/FIRM NAME						YEARS THERE	
	EMPLOYER'S ADDRESS:		STREET	CITY	STATE	ZIP CODE		
	(AREA CODE) BUSINESS PHONE ()	POSITION OR TITLE			NATURE OF BUSINESS			
	PRESENT ANNUAL EARNINGS		OTHER INCOME: INCOME FROM ALIMONY, CHILD SUPPORT OR MAINTENANCE PAYMENTS MAY BE EXCLUDED UNLESS RELIED UPON FOR CREDIT.					
	\$		SOURCE		\$ AMOUNT			

I give this information for the purpose of obtaining credit and authorize the obtaining of information concerning any statements made therein.

**EDUCARD PLAN
RETAIL INSTALLMENT CONTRACT
DEVRY INC.**

1. **General Definitions.** The student signing this application for loans ("Loans") applies for an Account with DeVry Inc., a Delaware corporation with its principal place of business at One Tower Lane, Oakbrook Terrace, Illinois. As used in this Agreement, the words "you" and "yours" refer to the student applicant and the co-signer, if any, and the words "we," "us" and "our" refer to DeVry Inc.

2. **Use of the Account.** You may use this Account to purchase educational services, pay for tuition costs, books and equipment that DeVry University, DeVry Institute of Technology, or Chamberlain College of Nursing (the school) may sell you from time to time. You represent that you have exhausted all avenues of student financial aid, including, if eligible, both grants and government assisted, insured or guaranteed student loans (Financial Assistance). Further, you authorize the school to use any credit balances that may result from the receipt of any financial assistance that you, or your parents, receive to credit your outstanding EDUCARD Plan balance to reduce said balance.

3. **Promise to Pay.** You agree to pay us in United States dollars for all purchases and applicable Finance Charges and any other fees that may be imposed in connection with this Agreement.

4. **Monthly Billing Statement.** We will send you a billing statement after each monthly billing period in which you have a balance in excess of \$1.00. This statement will show your New Balance, your Average Daily Balance, the applicable daily periodic rate, and the amount of the Finance Charge.

5. **Finance Charge.** You may avoid the imposition of a Finance Charge if you pay the New Balance on or before the Payment Due Date as shown on your monthly statement. If you do not pay the New Balance in full, you may pay the deferred purchase price for each purchase consisting of the cash price plus a Finance Charge.

5.1 A Finance Charge will be computed on the Average Daily Balance in your Account in each monthly billing period. The Average Daily Balance is determined by dividing the sum of the balances outstanding for each day of the monthly billing period by the number of days in the monthly billing period. The balance outstanding each day is determined by adding purchases (but not unpaid Finance Charges or current purchases made during that monthly billing period) and other debit adjustments to, and subtracting payments and other credits from the previous day's balance. The Finance Charge is determined by multiplying the daily periodic rate times the Average Daily Balance times the number of days in the billing period.

5.2 The daily periodic rate is .03287% (equivalent to a monthly rate of 1% and a corresponding ANNUAL PERCENTAGE RATE of 12%).

5.3 You may pay at any time all or any part of the New Balance owed by you under this Agreement.

6. **Minimum Payment Required.** Your initial minimum payment is due at registration. Thereafter, each month you will be required to make a minimum payment toward the New Balance that is shown on your monthly billing statement. The New Balance represents purchases made or charges incurred by you less payments or credits received by us during the previous billing period. Your payment will be due on the Due Date as shown on your monthly billing statement. If you pay your New Balance on or before the Due Date, no additional Finance Charge will accrue on your Account. The amount of the minimum monthly payment for the first eight months after you begin school will be determined after you submit your financial aid application and all required verification documents. The payment will be based on your expected charges and the financial assistance we expect to credit to your account. The monthly payment will be approximately one-fourth of the difference between your expected charges and the assistance ready to disburse at the beginning of the term. In addition to the minimum payment, you agree to make mandatory principal payments equal to (i) the amount you owe us in excess of the Credit Limit, plus (ii) any Financial Assistance received by you after the date of the Agreement.

After this first eight (8) months, your Minimum Payments will be adjusted for each subsequent eight month period to more accurately reflect the charges we expect you will incur and the financial assistance we expect to credit to your balance during that period. This adjustment may also consider the accumulated balance from previous periods of enrollment at the school.

7. **Credit Limit.** You agree not to let the Account balance, including Finance Charges, exceed any Credit Limit that we may establish for you.

8. **Other Charges.** If any check or payment instrument that you send to us is dishonored for any reason, you agree to pay a returned check fee in the amount that is imposed on us by the depository bank and in any event at least \$15.00.

9. **Default.** You will be in default of this Agreement if (a) you fail to make a payment when due, (b) you die or are declared incompetent, (c) you become the subject of bankruptcy or insolvency proceedings or an attachment or garnishment is entered against you which is not bonded over within ten days, (d) you supply us with false information, (e) you otherwise do not comply with the terms of this Agreement, including declining all or part of the financial aid for which you are eligible, failing to comply with financial aid requirements, or being in default on a prior government loan.

In the event of default, we may declare the entire outstanding balance, including all accrued Finance Charges and other fees due to us hereunder immediately due and payable.

If you are in default and we accelerate the loan balance to maturity, we may charge you collection costs incurred by us, including, without limitation, reasonable attorneys' fees and court costs to the extent permitted by applicable law.

10. **Credit Authorization.** We may require prior authorization for certain purchases each time you request placing those charges on your Account. We are not responsible in the event we refuse to honor such request for additional credit.

11. **Change in Terms.** We may at any time, subject to applicable law, terminate this Agreement or change your Credit Limit, increase advances to correspond to increases in tuition fees and other costs established by the school, and change other terms and conditions of this Agreement relating to your Account. If we change the terms of your Account, we will send you a notice describing those terms, as required by applicable law. We may, subject to applicable law, apply such change to the outstanding balance of your Account on the effective date of the change and to any new purchases or charges made after that date. Use of your Account following the effective date of the change will constitute your acceptance of these new terms.

12. **Delay.** We will not lose any rights under this Agreement if we delay taking action for any reason. You agree not to send us a check marked paid in full or similar legend if you have a dispute regarding our services. Disputes regarding the quality of the service may only be raised at the address shown in the billing error notice attached to this Agreement. By sending a paid in full check to us, to an address other than that address, you agree that we may cash the check and that you will remain liable for the remaining balance.

13. **Applicable Law.** This Agreement and the Account will be governed by Illinois law and applicable Federal law.

14. **Conversion to Installment Loan.** You agree that, when you complete or otherwise terminate your course with the school, you will no longer have credit privileges under the Account. At that time, you agree to pay us the then outstanding balance in the Account, including all Finance Charges in twelve consecutive monthly installments or less in substantially equal amounts sufficient to pay the principal balance in full, together with finance charges accruing on the unpaid balance of such account. If the minimum monthly payment indicated in paragraph 6 shall not serve to pay the outstanding balance, including finance charges, in a maximum of twelve monthly installments, your minimum monthly payment will be adjusted upward to the lowest minimum monthly payment which results in payment in full within twelve months. If the minimum monthly payment indicated in paragraph 6 shall serve to fully pay the outstanding balance, including all finance charges, in less than twelve monthly installments, we shall not be required to lower your minimum monthly payments. Your payments may vary over this twelve month (or less) period and we shall send you a monthly notice of the amount then due and owing. You have the right to prepay this amount in full at any time without penalty. We will provide you with a disclosure statement setting forth the material terms of this installment loan prior to your first payment becoming due under such terms.

15. **Additional Provisions.** You agree that the proceeds of this Loan will be used solely for purchasing educational services and books from the school. You agree that you must repay the amounts owing under this Agreement even though you may be under 18 years of age at the time you sign it. This Agreement is not effective until it is accepted by us in Illinois. You agree to notify us of any change in your name, address, or applicable school enrollment status within ten (10) days of such occurrence. You represent that you have not made any false written statement with respect to this Loan. If any provision of this Agreement is determined to be unenforceable or is prohibited by law, such provision shall be considered ineffective without invalidating the remaining provisions of this Agreement.

NOTICE TO STUDENTS

Do not sign this Agreement before you read it or if it contains any blank spaces. You are entitled to an exact copy of the Agreement you sign. Execution of this Agreement by you shall constitute your acknowledgment of receipt by you of a fully completed copy of this Agreement. You have the right to pay in advance the full amount due. The acceptance of this Agreement by DeVry Inc. shall be presumed and confirmed by the first extension of credit by DeVry Inc. pursuant to and after your signing of this Agreement.

STUDENT'S RIGHT TO CANCEL

YOU, THE STUDENT MAY CANCEL THIS TRANSACTION AT ANY TIME PRIOR TO MIDNIGHT OF THE FIFTH BUSINESS DAY AFTER THE DATE OF THIS TRANSACTION. SEE THE NOTICE OF CANCELLATION FORM FOR ANY EXPLANATION OF THIS RIGHT.

Executed at _____
STUDENT'S SIGNATURE _____ DATE _____
CITY STATE

COSIGNER (TO BE EXECUTED BY PARENT OR GUARDIAN)

The undersigned hereby agrees to and accepts the terms and conditions of this Agreement, and guarantees payment of the installments due hereunder if the Student does not pay said installments when due, and that the undersigned will pay said installments including all applicable Finance Charges, according to the tenor of this instrument and without resort by DeVry Inc., to and against the student. (Note for Illinois residents: DeVry Inc. cannot pursue you until it has attempted through the use of the court system to collect this amount from the student.) The undersigned further acknowledges that the "Notice to Cosigner" and a completely filled in and exact copy of all pages of this Agreement have been received and consents to be bound hereby.

COSIGNER'S SIGNATURE DATE _____
ADDRESS _____
Executed at _____ CITY STATE _____
Cosigner's relationship to student _____

ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL NOT EXCEED AMOUNTS PAID BY THE DEBTOR HEREUNDER.

EDUCARD PLAN AGREEMENT (continued from Page 3)

STATE LAW REQUIRES US TO GIVE YOU THE FOLLOWING NOTICES:

California Residents: The applicant, if married, may apply for a separate account. After credit approval each applicant shall have the right to use this Account to the extent of any credit limit set by the creditor and each applicant may be liable for all amounts of credit extended under this Account to any joint applicant. Delaware and Pennsylvania Residents: Finance Charges will be made in amounts or at rates not in excess of those permitted by law, and will be computed on the outstanding balances from month to month. Illinois Residents: Residents of Illinois may contact the Illinois commissioner of banks and trust companies for comparative information on interest rates, charges, fees, and grace periods. State of Illinois — Cap. P.O. Box 10181, Springfield, IL 62791 (1-800-634-5452). New York Residents: We may request a consumer report from consumer reporting agencies in considering this application and for the purpose of an update, renewal or extension of credit. Upon applicant's request,

we will inform applicant of the name and address of each consumer reporting agency from which we obtained a consumer report, if any, relating to applicant and co-applicant. Ohio Residents: THE OHIO LAW AGAINST DISCRIMINATION REQUIRES THAT ALL CREDITORS MAKE CREDIT EQUALLY AVAILABLE TO ALL CREDITWORTHY CUSTOMERS, AND THAT CREDIT REPORTING AGENCIES MAINTAIN SEPARATE CREDIT HISTORIES ON EACH INDIVIDUAL UPON REQUEST. THE OHIO CIVIL RIGHTS COMMISSION ADMINISTERS COMPLIANCE WITH THIS LAW. Wisconsin Residents: Marital Agreement Notice — No provision of a marital property agreement, unilateral statement under Section 766.59 Wis. Stats., or court decree under Section 766.70 Wis. Stats., will adversely affect our rights unless we are furnished a copy of the agreement, statement of decree, or we have actual knowledge of its terms, before credit is granted or the account is opened.

**FAIR CREDIT BILLING DISCLOSURE STATEMENT
— TO DEVRY INC. EDUCARD PLAN ACCOUNT HOLDERS —**

This notice contains important information about your rights and our responsibilities under the Fair Credit Billing Act. Notify Us In Case Of Errors Or Questions About Your Bill.

If you think your bill is wrong, or if you need more information about a transaction on your bill, write to us on a separate sheet at the "Billing Address" listed on your statement. Write to us as soon as possible. We must hear from you no later than 60 days after we sent you the first bill on which the error or problem appeared. You can telephone us, but doing so will not preserve your rights. In your letter, give us the following information:

- i. Your name and account number.
- ii. A description of the error and an explanation (to the extent you explain) why you believe it is an error. If you only need more information, explain the item you are not sure about and, if you wish, ask for evidence of the charge such as a copy of the charge slip. Do not send in your copy of a sales slip or other document unless you have a duplicate copy for your records.
- iii. The dollar amount of the suspected error.
- iv. Any other information (such as your address) which you think will help us to identify you or the reason for your complaint or inquiry.

We must acknowledge all letters pointing out possible errors within 30 days of receipt, unless we are able to correct your statement during those 30 days. Within 90 days after receiving your letter, we must either correct the error or explain why we believe the statement was correct.

Your Rights And Our Responsibilities After We Receive Your Written Notice:

After we receive your letter, we cannot try to collect any amount in question, or report you delinquent. We can continue to bill you for the amount in question, including finance charges, and we can apply any unpaid amount against your credit limit. You do not have to pay any questioned amount while we investigate, but you are still obligated to pay the parts of your bill that are not in question. If we find that we made a mistake on your bill, you will not have to pay any financing charges relating to any questioned amount. If we didn't make a mistake, you may have to pay finance charges, and you will have to make up any missed payment on the questioned amount. In either case, we will send you a statement of

the amount you owe and the date it is due. If you fail to pay the amount that we think you owe, we may report you as delinquent. However, if our explanation does not satisfy you and you write to us within 10 days telling us that you still refuse to pay, we must tell anyone we report you to that you have a question about your bill. And, we must tell you the name of anyone we reported you to. We must tell anyone we reported you to that the matter has been settled between you and us when it finally is.

If we do not follow these rules, we can't collect the first \$50 of the questioned amount, even if your bill was correct.

NOTICE TO WISCONSIN RESIDENTS

If you fail to make, when due, two minimum payments within any 12 month period, such event will constitute a default hereunder. Upon such default, the full amount of your account shall be payable if such default is not cured within 15 calendar days after mailing notice of this default to you.

NOTICE TO NEW JERSEY RESIDENTS

In the event that the outstanding balance reflected on the EDUCARD Plan Contract signed by you and your cosigner shall be in default and referred to an attorney not on our staff for collection, New Jersey law provides that the assessment of such attorney's fees to be charged you shall not exceed 20% of the first \$500 of the outstanding balance, and 10% of the excess due and payable when the account is referred to such attorney.

NOTICE TO IOWA, KANSAS AND WISCONSIN RESIDENTS

In the event that you default in the payment of any of the installments due under this EDUCARD Plan Contract, and we sue you or your cosigner to enforce any of its rights under the Agreement, we shall not be authorized to collect from you or your cosigner attorney's fees incurred by us in bringing such action. Wisconsin law further provides that when you complete or terminate your course of study with us and if you have an outstanding balance in your account, before your minimum monthly payment will be adjusted upward to the lowest minimum monthly payment alternative as indicated in paragraph 6 which will permit payment in full within twelve months as set forth in the Agreement, you will be notified in writing and your written authorization will be required, as to the new minimum monthly payment to be made by you.

EQUAL OPPORTUNITY ACT

The Federal Equal Credit Opportunity Act prohibits creditors from discriminating against credit applications on the basis of race, sex, or marital status. The Federal agency which administers compliance with this law is the: Federal Trade Commission, c/o Equal Credit Opportunity, Washington, D.C. 20530.

NCLC[®]

NATIONAL
CONSUMER

LAW
CENTER[®]

Advancing Fairness
in the Marketplace for All

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