INCOME-BASED REPAYMENT: MAKING IT WORK FOR STUDENT LOAN BORROWERS

July 2008

Student Loan Borrower Assistance

The Student Loan Borrower Assistance Project (SLBA)
is a program of the National Consumer Law Center (NCLC).

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July 2008

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A Policy Paper by the National Consumer Law Center's Student Loan Borrower Assistance Project

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EXECUTIVE SUMMARY

As of July 1, 2009, a new income-based student loan repayment program (IBR) will allow most federal student loan borrowers with economic hardships to repay their loans based on a formula that takes income and total indebtedness into account. The government will cancel any remaining balances after twenty-five years of repayment.

The program should bring much-needed relief to borrowers having trouble with student loan repayment. However, unless changes are made, IBR is not likely to reach many of the neediest borrowers. This paper presents recommendations to extend IBR to all who need it.

Access for Borrowers in Default

A borrower in default can choose IBR but will not get out of default simply by making this selection. This is tremendously important because as long as borrowers remain in default, even while making payments, they are still subject to collection agency tactics, income tax seizures, federal benefits offsets, administrative wage garnishments and possible lawsuits.

The current paths to get out of default through repayment are loan consolidation and rehabilitation. Access to both of these programs must be improved so that borrowers in default can get back into repayment through IBR. A general solution is to require loan holders to give borrowers the choice of selecting IBR before a default is declared.

Communicating Objective and Accurate Information to Borrowers

Collection agencies and loan servicers are delegated too much authority to resolve disputes with borrowers. In the federal loan programs, they are given authority to act on behalf of the loan holder in everything from rehabilitation to information about discharges to loan compromises. Yet dispute resolution is not their primary mission. They are not adequately trained to understand and administer the complex borrower rights available under the Higher Education Act and there is insufficient oversight of their activities. As a result, consumers are deprived of important options to which they are legally entitled. Even worse, some collectors misrepresent these rights or steer consumers into options more profitable for the collector.

In addition to improving Department of Education enforcement and oversight of private collection agencies, borrowers with cancellation or other options should be given proper advice so that they can pursue these options. The existing assistance network is insufficient. To help meet this need, we call on Congress to fund a pilot project that sets up a neutral non-profit entity to provide direct assistance to borrowers in trouble. Private funders could also offer assistance as long as there is no funding from conflicting interests, such as student lenders. This would be a borrower advocate program that would work in collaboration with ombuds, counseling and other mediation entities. The pilot project is a first step toward building a strong student loan borrower assistance network.

Assisting Borrowers to Find the Best Options and to Raise Defenses

There is a distinct category of borrowers who will not be able to benefit from IBR because they are disabled or otherwise unable to follow through or handle the paperwork required to apply for and maintain IBR. At a minimum, borrowers with cancellation or other options should be given proper advice so that they can pursue these options.

There will also be borrowers who do not choose IBR because they have already repaid the principal two or three times over, but still owe much more than what they initially borrowed. A solution is to cancel balances for borrowers who have repaid beyond a certain amount of principal.

Other borrowers will have defenses to repayment, such as claims based on deceptive practices of the school they attended. These borrowers must be given the opportunity to raise these defenses either in response to collection actions or affirmative litigation. From our experience, these cases often involve borrowers who attended for-profit vocational schools that failed to deliver as promised.

Assisting Private Loan Borrowers

IBR will not help the large numbers of borrowers financing their educations with private student loans. We wrote extensively about this issue in a separate paper.[1] Among other reforms, student loan creditors should be required to offer certain loss mitigation options, such as income-based and flexible repayment.

The keys to reform in this area should be based on the following principles:

- Eliminate unsustainable loans and develop fair underwriting standards;
- Eliminate incentives for schools and lenders to steer borrowers to abusive loans;
- Improve disclosures so that borrowers can know the true cost of private loan products and understand the difference between private and government loans;

[1] 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/uploads/File/Report_PrivateLoans.pdf.

- Require accurate and accountable loan servicing;
- Ensure effective rights and remedies for borrowers caught in unaffordable loans. This could include a mandatory flexible or income-based repayment plan, similar to the federal government plan;
- Preserve essential federal and state consumer safeguards; and
- Improve assistance to distressed borrowers, including mandatory loss mitigation.

Expanding the Safety Net

The government has collection powers far beyond those of most unsecured creditors. There is a cost to pursuing these most vulnerable members of society. In human terms, a consumer who became disabled later in life may find she simply cannot continue to pay back the student loan she took out thirty or forty years ago. Offsetting a portion of her Social Security may mean that she does not get all the food or prescription drugs she needs. In financial terms, the cost of trying to collect from those who simply do not have much is often greater than the meager amounts, if any, which ultimately come back to the government.

In addition to the recommendations described above, a number of critical reforms are needed, including:

- **Restore a reasonable statute of limitations for student loan collection.** The elimination of the statute of limitations for government student loans in 1991 placed borrowers in unenviable, rarified company with murderers, traitors, and only a few violators of civil laws.

- **Fix the disability discharge system**.

- **Restore bankruptcy rights.** Bankruptcy is meant to give individuals and families in trouble a second chance at organizing their lives and achieving financial stability. Students in trouble deserve a fair shot at this protection, too.

- **The government should cease collection when the costs clearly outweigh the potential revenues.**

- **Exempt certain borrowers from Social Security offsets, including those above age 75.**

- **Provide for cost of living increases in the amount protected from Social Security offset.**

- **Grant borrowers facing federal benefits offset the same right to hardship reductions and suspensions that exist in administrative wage garnishment cases.**

- **Exempt the Earned Income Tax Credit (EITC) from the tax refund offset program.**

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INTRODUCTION

Starting in July 2009, the new income-based repayment program (IBR) will allow most federal student loan borrowers with economic hardships to repay their loans based on a formula that takes income and total indebtedness into account. The government will cancel any remaining balances after twenty-five years of repayment.

The program should bring much-needed relief to borrowers having trouble with student loan repayment. However, unless changes are made, IBR is not likely to reach many of the neediest borrowers. There is a danger that just like the current Direct Loan income-contingent repayment plan (ICR), IBR will be underutilized, especially by borrowers in default. We must learn from the ICR experience in order to make the IBR as effective as possible for all borrowers.

This paper presents recommendations to expand the reach of IBR. Much of this analysis is derived from our experiences advising and representing borrowers through the National Consumer Law Center's Student Loan Borrower Assistance Project (SLBA). SLBA provides information about student loan rights and responsibilities to borrowers and advocates. SLBA also seeks to increase public understanding of student lending issues and to identify policy solutions to promote access to education, lessen student debt burdens and make loan repayment more manageable.[2]

THE STUDENT LOAN BORROWER "DEFAULT EXPERIENCE"

Introduction

The circumstances that lead to student loan defaults are often beyond a borrower's control. In a phone survey of student loan borrowers, the Texas Guaranty Agency found that repayers were likely to have jobs related to their training both during school and afterwards, while defaulters did not. Those who were predicted not to default but did faced the highest number of combined life traumas.[3]

In a June 2006 report, the Department of Education isolated other characteristics of borrowers facing the greatest student loan debt burdens. The report found that borrowers who

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[2] See http://www.studentloanborrowerassistance.org.
[3] Texas Guaranty Student Loan Corporation, "Predicting Which Borrowers Are Most Likely to Default" (1998), available at: http://www.tgslc.org/publications/reports/defaults_texas/ins_intro.cfm.

were still repaying loans after ten years were more likely to be female, black, from the lowest-income families, and have parents who did not go to college.[4]

The case of Joyce, a 63 year old Massachusetts woman, gives a window into the "default experience." Joyce worked sporadically when she was younger, but she mostly stayed home to raise her three children. After getting a divorce from an abusive husband, she was left with few assets and few marketable skills. When she was in her 50's, she took out federal student loans to finish her undergraduate education. After graduating, Joyce applied for many jobs, but received one rejection after another. She is an intelligent, capable woman, but she is overweight and in her late 50's. She is sure she faced discrimination in her job hunt. She finally settled for a $10/hour job with no benefits. She made sporadic payments on the loans during this time. Soon after she started this job, two major life events occurred. Her mother was diagnosed with Alzheimer's and needed someone to take care of her. Her son, who had a history of substance abuse, was in a horrible car accident which left him and his wife disabled and a young autistic son at home with no one to take care of him. The son moved closer to his mother and she now helps take care of her grandson. Unable to find a good job and unable to spend much time away from home due to her caretaking responsibilities, Joyce decided to start receiving Social Security retirement payments at age 62. She receives about $560/month and is able to get by only because she also gets food stamps and lives in subsidized housing. Due to interest accrual and collection fees, Joyce's student loan balance has grown to over $50,000. There is nothing the government can collect from her other than this years tax rebate, but they continue to send collection letters and calls. If her Social Security payments go up, they too could be vulnerable.

Joyce is a good candidate to consolidate with Direct Loans and get an income contingent repayment plan (ICR) plan with very low or even 0 payments. She will be working with SLBA to accomplish this goal. However, as has occurred with every client we have ever worked with, no one along the line, from the collection agency, guaranty agency or lender, mentioned this possibility. Joyce did not learn about ICR from the collection notices she received. And Joyce completed her degree! Those who drop out face greater potential for economic hardship. By 2001, nearly one-fourth of borrowers who dropped out had defaulted on at least one loan.[5]

Joyce's case also illustrates the problems of ballooning balances. Student loan balances that start low can increase very quickly, mainly due to interest accrual and exorbitant collection fees. The fees are added to the balance even in a case like Joyce's where there is nothing the collection agency can collect and nothing they can do other than call and write. This not only makes the problem objectively more difficult because the amounts are higher, but also takes a tremendous psychological toll on borrowers who see their balances continuing to increase even when they have made substantial payments. We often hear from borrowers who have paid two or three times the principal amount with virtually no impact on the balance.

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[4] Susan P. Choy, Xiaojie Li, U.S. Department of Education National Center for Education Statistics, "Dealing with Debt" at 27 (June 2006), available at: http://nces.ed.gov/pubsearch/pubsinfo.asp?pubid=2006156.

[5] Lawrence Gladieux and Laura Perna, "Borrowers Who Drop Out: A Neglected Aspect of the College Student Loan Trend" (May 2005) at 7, available at: http://www.highereducation.org/reports/borrowing/borrowers.pdf.

Joyce's case also highlights the gap in assistance resources for student loan borrowers. The importance of information and communication with borrowers is reinforced by a profile conducted by the University of Illinois, Chicago of student loan defaulters. The most commonly cited reason for defaults was lack of information.[6] In a phone survey of student loan borrowers, the Texas Guaranty Agency found that those who repaid their loans were generally more knowledgeable about their repayment options.[7]

Unfortunately for borrowers in default, the collectors are generally the front line providers of information. They are trained to push people to repay. They are notoriously ill-informed, poorly trained and rarely communicate in an effective, borrower-friendly way. As discussed below, this is a tremendous barrier to helping borrowers resolve problems and get back into repayment.

GETTING OUT OF DEFAULT

As of July 2009, a borrower in default will be able to choose IBR but will not get out of default simply by making this selection. The borrower must jump through some additional hoops to get out of default. This is tremendously important because as long as borrowers remain in default, even while making payments, they are still subject to collection agency tactics, income tax seizures, federal benefits offsets, administrative wage garnishments and possible lawsuits. No one is likely to stick with a payment plan for long if aggressive collection efforts continue while s/he is making payments.

The main ways in current law for a borrower to get out of default are consolidation and rehabilitation. The path to IBR for borrowers in default must first go through one of these programs. Each is discussed below.

1. **Consolidation**

Borrowers with non-consolidation loans in default can generally use consolidation as a path out of default. In the guaranteed loan program (also known as the Federal Family Education Loan programs or "FFEL"), these borrowers have the option of making three consecutive reasonable and affordable payments or arranging to repay under an income-sensitive repayment plan.[8] Direct Loan borrowers in default can choose to make three consecutive reasonable and affordable payments or arrange to repay under an income-contingent repayment plan.[9] As of July 1, 2009, Direct Loan borrowers will also be able to choose IBR.

There have historically been a number of practical barriers for borrowers seeking to get out of default through consolidation with the Direct Loan program. One of the key barriers, discussed in the next section, is that few borrowers are informed about this option. The situation

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[6] U.S. Department of Education, Office of Student Financial Assistance, "Ensuring Loan Repayment: A National Handbook of Best Practices" ch. 3 (2000).
[7] Texas Guaranty Student Loan Corporation, "Predicting Which Borrowers Are Most Likely to Default" (1998), available at: http://www.tgslc.org/publications/reports/defaults_texas/ins_intro.cfm.
[8] 34 C.F.R. §682.200 (satisfactory repayment arrangement); 20 U.S.C. §1078-3(a)(3)(A)(ii)(III); 34 C.F.R. §682.201(d)(1)(i)(3).
[9] 34 C.F.R. §685.220(d)(1)(ii)(C).

is exacerbated for borrowers in default as they generally are dealing with a collection agency that is focused on collecting money, not on advising the borrower about optimal strategies.

Another problem is that the Department of Education is often slow in processing Direct Loan consolidation applications. This would not be such a problem if collection ceased while the consolidation applications were pending. But this is not the case and in our experience, the Department rarely informs borrowers that they can place their loans in forbearance pending a decision on the applications. As discussed in the recommendations section below, these borrowers should automatically be granted forbearances after they have submitted completed consolidation applications. These delays are likely to get worse now that most, if not all, FFEL lenders are getting out of the consolidation business. It is likely that FFEL borrowers will soon have no choice but to consolidate with Direct.

Even if the consolidation application is approved, there can be a transition period while the Department collects the necessary information to approve an ICR. In these circumstances, the Department generally places the borrower in a standard repayment plan. This is devastating because these borrowers chose ICR because they could not afford standard plans. In our experience, many borrowers give up at this point and end up back in default.

There will also be problems that are likely to arise for student loan borrowers who are not in default and are seeking to repay their FFEL loans using IBR. We are concerned that many lenders and guaranty agencies will pressure borrowers to choose other repayment plans. In some cases, loan holders may do this for their own self-interested reasons. In other cases, we frequently hear from lenders that they believe it is in the best interest of borrowers to repay as much as possible each month so that their balances are reduced at the fastest rate. This is a good principle in theory, but not particularly practical for borrowers using IBR as a default management tool. For many of these borrowers, the ability to repay their loan balances is often secondary and will never be possible unless they experience dramatic improvements in their financial circumstances.

Income-based repayment is an imperfect default avoidance or default management tool, but one of the few that exist. Given the extremely harsh consequences of student loan defaults, it is critical that borrowers be offered this opportunity even if it means that they will never be able to pay off their balances. The 25 year write-off also offers these borrowers a light at the end of a tunnel, albeit a very long tunnel.

Among other issues, FFEL loans are frequently sold and borrowers often have to deal with successive servicers and loan holders. A borrower's previous loan history, including repayment plan selections, may get lost during the transition from lender to lender. Each lender must be prepared to honor the IBR agreement and keep track so that if necessary, the borrower is given the 25 year write-off. It remains to be seen whether this will occur.

There is precedent for these concerns given the self-interested (and illegal) way in which many FFEL lenders refused to certify borrower requests for Direct Loan consolidations during the heyday of loan consolidations in the late 1990's and early 2000s. The Department addressed and acknowledged this problem in numerous Dear Colleague letters.

Even if borrowers know about consolidation as a way out of default, not all student loan borrowers are eligible to consolidate with the federal programs. Private loan borrowers are in this category as well as certain federal borrowers. For example, borrowers with Perkins loans only are not eligible to consolidate with either FFEL or Direct Loans.

A final issue is with borrowers who have previously consolidated their loans. These borrowers are generally prohibited from reconsolidating. There is an exception for FFEL loan borrowers who are in default and are seeking to consolidate with Direct Loans for the purposes of obtaining an ICR. A similar option is not available to Direct Loan consolidation borrowers who have defaulted. They must first rehabilitate with the Direct Loan program. Problems with rehabilitation are discussed below.

2. **Rehabilitation**

Rehabilitation is an alternative to consolidation as a path out of default. Borrowers have the right to set up a repayment agreement where they are required to make nine reasonable and affordable timely payments within a ten month period. Under the FFEL program only, the loan must be resold at the end of this period.

In our experience, loan holders consistently refuse to follow the law and offer borrowers payments that are truly reasonable and affordable. This problem derives in part from a system established by the Department which provides compensation to collectors for setting up rehabilitation plans only if the plans require borrowers to make certain minimum payments.[10] Collection agencies may also have their own incentive systems that reward employees based on the number of debtors they are able to convince to commit to a particular type of repayment program, including rehabilitation.[11]

Some FFEL lenders and guaranty agencies claim that they cannot set up very low repayment plans because they will not be able to resell the loans. Some guaranty agencies claim that lenders will only purchase the rehabilitated loans if the balance is paid down sufficiently. However, others report that they very rarely have problems reselling the loans.

Regardless, these actions conflict with the statutory and regulatory provisions that afford borrowers the right to make reasonable and affordable repayments.[12] The FFEL regulations go even further by prohibiting the imposition of a minimum payment. Documentation is required if the payment is below $50, but these payments are clearly allowed if that is what is reasonable and affordable for a particular borrower.[13]

[10] See “Rehabilitation Minimum Payment Percentages” (July 7, 2006), available on the Department of Education’s Private Collection Agency support web site at: http://www.fsacollections.ed.gov/contractors/pca2004/rehab/070706.htm.
[11] See, e.g., Rumler v. General Revenue Corp. 2007 WL 1266747 (S.D. Ind. May 1, 2007).
[12] 34 C.F.R.§685.211(f)(1) (Direct), §682.405(b) (FFEL).
[13] 34 C.F.R. §682.405(b)(1)(iii)(B).

To compound the problem, collectors often assert that once a loan is successfully rehabilitated, borrowers must begin repaying the standard monthly payment amount rather than a lower, income-based amount. This is not true. Borrowers should be able to choose income-based repayment programs, such as the Direct Loan ICR, even if this requires them to first consolidate their loans with the Direct Loan program.

RECOMMENDATIONS FOR BORROWERS SEEKING TO GET OUT OF DEFAULT

1. **Automatic IBR**

A general solution is to require loan holders to give borrowers the choice of selecting IBR before a default is declared. Some borrowers may not want IBR. However, it should be straightforward to require loan holders to offer this option prior to declaring default and to explain the basic rights and responsibilities. If borrowers make this choice, they should be given a reasonable amount of time to submit the required paperwork before a default may be declared.

Even if this recommendation is adopted, there will still be some borrowers that do not make the IBR choice prior to default. Additional reforms are needed to help borrowers seeking to get out of default through consolidation or rehabilitation in order to access IBR.

With respect to consolidation, we recommend that:

A. Borrowers who send in completed applications for consolidation and request an ICR (and IBR once it is available) should be granted automatic forbearances for at least 90 days. This will help borrowers avoid getting back into default if they are told to repay under standard repayment plans even for a short period of time.

B. Just as in the FFEL program, borrowers in default on Direct consolidation loans should be able to reconsolidate with Direct Loans for the purposes of repaying through ICR or IBR.

With respect to rehabilitation, we recommend that:

A. The calculated monthly payment under IBR should be presumptively reasonable and affordable for purposes of establishing a reasonable and affordable repayment plan for rehabilitation. In the FFEL program, lenders argue that they cannot do this because it may jeopardize their ability to resell their loans. To the extent this is true, a solution is to eliminate the resale requirement. As an alternative, in cases where there are no purchasers of the rehabilitated loans, the Department should be required to accept these loans in the Direct Loan consolidation program. Borrowers with very low monthly payments could even be required at the outset of the rehabilitation plan to agree to consolidate their loans with Direct Loans at the end of the rehabilitation period. The Department of Education has indicated that it is taking steps in this direction.

B. Borrowers seeking repayment plans in lieu of collection actions should have the same rights described above in recommendation A.

With respect to FFEL lenders refusing to offer IBR or pressuring borrowers away from IBR:

A. There should be private remedies in the Higher Education Act (HEA) that allow borrowers to raise claims if they are unfairly denied IBR. Unfortunately, under current law, courts have found that there is no private right of action for borrowers to enforce the HEA. The Department should also have specific authority to penalize these lenders, including dropping them from FFEL participation for repeated violations.

B. A borrower's right to switch to Direct Loans to consolidate must be preserved both in and out of default. This gives borrowers an "out" if their FFEL lenders unreasonably block their access to IBR.

COMMUNICATING OBJECTIVE AND ACCURATE INFORMATION TO BORROWERS

Collection agencies and loan servicers are delegated too much authority to resolve disputes with borrowers. In the federal loan programs, they are given authority to act on behalf of the loan holder in everything from rehabilitation to information about discharges to loan compromises. Yet dispute resolution is not their primary mission. They are not adequately trained to understand and administer the complex borrower rights available under the Higher Education Act and there is insufficient oversight of their activities.[14] As a result, consumers are deprived of important options to which they are legally entitled. Even worse, some collectors misrepresent these rights or steer consumers into options more profitable for the collector.

From our experience, it is extremely difficult to get a guaranty agency or the Department to take a file away from a collection agency in order to help a borrower resolve a problem. In many years of representing borrowers, we have never been directed to a loan holder ombudsman or customer advocate by a collection agency. Borrowers that wish to repay or exercise other rights are often shut out because of problems with overly aggressive and often abusive collection agencies.

Private collectors have in some cases deliberately deceived consumers by misrepresenting themselves as the Department of Education. They have overcharged consumers for collection fees, used misleading tactics to track borrowers, browbeaten borrowers into unaffordable payment plans, threatened them with actions that they cannot legally take, and pressured consumers to borrow from relatives.[15]

Collectors often tend to push their "pet" options, regardless of whether they make sense for individual borrowers. For example, we often see letters from collection agencies that tout the

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[14] See U.S. Department of Education, Office of Inspector General, Final Audit Report, Control Number ED-OIG/A19-D0002 (December 23, 2003).

[15] See, e.g., Press Release, "Kennedy Questions Student Loan Lenders' Collection Tactics" (April 26, 2007). See generally National Consumer Law Center, Student Loan Law ch. 4 (3d ed. 2006 and Supp.).

benefits of loan rehabilitation. Figure 1 on the next page is one example of this type of letter. The collection agency informs the borrower that "The guarantee agency that is responsible for your defaulted loan strongly suggests you consider the benefits you will receive from Loan Rehabilitation." This may be a good idea for certain borrowers, but it is misleading to highlight this option and ignore others, such as consolidation with the Direct Loan program. The letter then goes on to state incorrectly that loan rehabilitation "...is a program that when a borrower of a defaulted student loan makes twelve consecutive on time monthly payments, their loans may qualify to be repurchased by a pre-determined lender." This letter, dated June 2008, is inaccurate in that the loan rehabilitation program, as of 2006, only requires borrowers to make nine payments within a ten month period. This is very typical of the types of errors we see regularly.

It is not just the private collectors that give out inaccurate information or mislead borrowers. We frequently run into this problem with the Department of Education collection staff as well as with guaranty agencies.

We cannot overstate this problem, yet it is almost never discussed in policy debates. We deal with collectors on behalf of clients all the time. The collectors are consistently wrong in interpreting student loan law and regulations. Our clients have us to fight for them, but most borrowers do not have this luxury. They are on their own, trying to get back into a system that is often treating them as "deadbeats." The collection agency personnel are not surprisingly bringing a collection mentality to a dispute resolution environment. It doesn't work. If this is the system we continue to use to get information to borrowers, the most vulnerable borrowers will either never learn about IBR or face extreme difficulty trying to get into the program. The problem is particularly acute for borrowers with special needs or language barriers.

FIGURE 1

Collection Technology, Inc.
P.O. Box 2017
Monterey Park, , CA 91754

PRIORITY NOTICE

June 5, 2008

[redacted]

Client : American Student Assistance

Account Number [redacted]
Balance Due : $8664.05

Take Advantage Of This Great Opportunity Today

The guarantee agency that is responsible for your defaulted loan strongly suggests you consider the benefits you will receive from **Loan Rehabilitation**.

The Advantages to you include:

- Your credit record pertaining to the defaulted FFEL Program Loan will be updated to clear the defaulted Status (there will be no history of it even going into default).
- You will have the restrictions from federal financial student aid removed.
- You will have all the opportunities of a current FFELP borrower reinstated (i.e. deferment, forbearance, additional loans, and etc…)
- There will be no more IRS tax offsets taken to collect this defaulted student loan.

Loan Rehabilitation is a program that when a borrower of a defaulted student loan makes twelve consecutive on time monthly payments, their loans may qualify to be repurchased by an pre-determined lender.

CTI is committed to helping you resolve this difficult situation. Please contact your loan counselor at 1-877-522-6898 today for more information about **Loan Rehabilitation**.

This notice has been sent from a collection agency. This is an attempt to collect a debt. Any information obtained will be used for that purpose. The balance due represents all moneys currently assigned to CTI. This may not include other amount due our client. Any payment in full will be verified by CTI and approved by our client.

IMPORTANT INFORMATION ON THE BACK OF THIS NOTICE

--Detach and Return with Payment--

P.O. Box 2017
Monterey Park, CA 91754
Return Service Requested

Account Number [redacted]
Balance Due : $8664.05
Amount Enclosed : $__________

PERSONAL & CONFIDENTIAL
[redacted]

Collection Technology, Inc.
P.O. Box 2017
Monterey Park, CA 91754

REHB 000643P 1 457 000553 157 062000 Z-CRE

RECOMMENDATIONS TO LIMIT COLLECTION AGENCY ABUSES AND IMPROVE COMMUNICATION WITH BORROWERS

1. **Borrowers with cancellation or other options should be given proper advice so that they can pursue these options.** The existing assistance network is insufficient. Legal aid and other programs are under funded and restricted in what they can do. Few assist student loan borrowers. To help meet this need, we call on Congress to fund a pilot project that sets up a neutral, non-profit entity to provide direct assistance to borrowers in trouble. Private funders could also offer assistance as long as there is no funding from conflicting interests, such as student lenders. This would be a borrower advocate program that would work in collaboration with ombuds, counseling and other mediation entities. Counselors in the borrower advocate project should be under the supervision of a lawyer who is knowledgeable about student loan law and keeps up with new developments. Depending on resources, the pilot project could begin in a few areas or it could be available more broadly. It should include an evaluation mechanism to measure borrower satisfaction and track borrower progress over time. The pilot project is a first step toward building a strong student loan borrower assistance network.[16]

2. **The Department of Education should limit the files it sends to collection agencies.** At a minimum, borrowers that are already subject to extreme collection programs such as offset and have no other assets should not be pursued by collection agencies and should not be charged collection fees. We also recommend in the "safety net section" below that the government cease collection all together when the costs clearly outweigh the potential benefits.

3. **The Department of Education must improve all aspects of enforcement and oversight of private collection agencies.** In addition, Congress should establish a set of mandatory penalties, including elimination from the government's program, for offenders.

4. **The Department and its agents should make publicly available its process for handling complaints against collection agencies and any disciplinary actions taken against those agencies.**

5. **Require collectors to develop a clear complaint escalation system and sanction those that fail to comply.** Borrowers should be able to easily work their way up the supervisory chain when problems arise and be able to lodge complaints about collectors.

[16] See generally National Consumer Law Center, "Finding A Way Out: Improving the Assistance Network for Financially Distressed Student Loan Borrowers" (December 2007), available at: http://www.studentloanborrowerassistance.org/uploads/File/REPORTDec07.pdf

ASSISTING BORROWERS TO FIND THE BEST OPTIONS AND TO RAISE DEFENSES

Even if all of the reforms discussed above are adopted, the reality is that IBR will not be appropriate for all borrowers. There is a distinct category of borrowers who will not be able to benefit from IBR because they are disabled or otherwise unable to follow through or handle the paperwork required to apply for and maintain IBR. The most severely disabled borrowers should, in theory, be able to get discharges of their loans through the total and permanent disability discharge program. Unfortunately, this program is a travesty as it is currently administered. Proposed reforms in this area are discussed below.

At a minimum, borrowers with cancellation or other options should be given proper advice so that they can pursue these options. The fact that most of these borrowers are dealing with aggressive collectors creates insurmountable barriers to relief for many borrowers. Only the most knowledgeable borrowers or those with effective representation can fight back, as discussed in the previous section.

There will also be borrowers who do not choose IBR because they have already repaid the principal two or three times over but still owe much more than what they initially borrowed. A solution, discussed below, is to cancel balances for borrowers who have repaid a certain amount beyond principal.

Other borrowers will have defenses to repayment, such as claims based on deceptive practices of the school they attended. These borrowers must be given the opportunity to raise these defenses either in response to collection actions or through affirmative litigation. From our experience, these cases often involve borrowers who attended for-profit vocational schools that failed to deliver as promised.

For example, we recently worked with John, a young man of 23 who attended a for-profit technical school in Massachusetts. He had worked hard to graduate from a vocational high school. The for-profit school's recruiters lured him to sign up with promises that he could study computer programming. When he enrolled, that particular course of study was not available. The staff told him to go ahead and start school and enroll in the program later. John withdrew when he found out later that the school had no plans to offer this course of study.

He was left with severe depression (which he had experienced even before he signed up for the school) and two student loans, one private and one federal. Sallie Mae has sued him to collect the private loan even though he lives solely on SSI income. He was able to get an economic hardship deferment of the federal loan, but this will expire after three years and must be recertified every year. He says that even if he had resources, he will never repay the loans because he believes he was ripped off. Yet he is not eligible for any of the existing and very limited school-related discharges. He is trying to raise the school-related claims as defenses to the Sallie Mae collection action, but this will be difficult to do given the complexities of the legal claims. He is in many ways the prototypical example of a young person who will most likely be lost to the higher education system. Bitter from his experience and saddled with debt, he says that he will never take out another student loan or go back to school.

RECOMMENDATIONS TO ASSIST BORROWERS WITH DEFENSES

1. **The government should cease collection and write-off balances for borrowers who have repaid a certain amount beyond principal and who have loans that are more than 10 or 15 years past due.**

2. **Limit collection charges to only those fees that are bona fide and reasonable and actually incurred in collecting against individuals.**

3. **Expand a borrower's ability to raise defenses in response to collection and school-related claims.** Even borrowers who are aware of their rights are often unable to enforce them. The main barrier to private enforcement is that courts have consistently held that there is no private right of enforcement under the Higher Education Act (HEA). Fair debt laws are an imperfect substitute for direct enforcement of borrower rights. Among other recommendations, we call on Congress to create an explicit private right of action to enforce the Higher Education Act.

4. **The Department and other relevant state and federal agencies, including the Federal Trade Commission (FTC), must ensure that lenders and schools that are required to do so are complying with the FTC Holder Rule**. Enforcement and oversight is especially important in the private student loan context.

ASSISTANCE FOR PRIVATE LOAN BORROWERS

IBR will not help the large numbers of borrowers financing their educations with private student loans. 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. The borrowing limits in the federal loan programs, the skyrocketing cost of higher education and aggressive lender marketing have fueled the growth of private student loans. Although still a smaller percentage of overall student loans, the yearly growth of private loans is outpacing that of federal loans. Private loans now comprise about 24% of the nation's total education loan volume.[17]

Private student loans are almost always more expensive than federal loans. This is especially true for borrowers with lower credit scores or limited credit histories. Private loans also do not have the same range of protections for borrowers that government loans have. Further, borrowers are more likely to borrow unaffordable amounts since, unlike most federal loans, there are no loan limits for private loans.

[17] College Board, Press Release, "Federal Student Aid to Undergraduates Shows Slow Growth, While Published Tuition Prices Continue to Rise" (Oct. 22, 2007).

We wrote extensively about this issue in a separate paper.[18] Among other reforms, student loan creditors should be required to offer certain loss mitigation options, such as income-based and flexible repayment.

The keys to reform in this area should be based on the following principles:

- Eliminate unsustainable loans and develop fair underwriting standards;
- Eliminate incentives for schools and lenders to steer borrowers to abusive loans;
- Improve disclosures so that borrowers can know the true cost of private loan products and understand the difference between private and government loans;
- Require accurate and accountable loan servicing;
- Ensure effective rights and remedies for borrowers caught in unaffordable loans. This could include a mandatory flexible or income-based repayment plan, similar to the federal government plan;
- Preserve essential federal and state consumer safeguards; and
- Improve assistance to distressed borrowers, including mandatory loss mitigation.

EXPANDING THE SAFETY NET

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

In addition to the recommendations described above, a number of critical reforms are needed, including:

1. **Restore a reasonable statute of limitations for student loan collection.** The elimination of the statute of limitations for government student loans in 1991 placed borrowers in unenviable, rarified company with murderers, traitors, and only a few violators of civil laws. Statutes of limitations are essential first because there are very serious problems associated with adjudicating old claims. For example, loan holders must keep records of government student loans for a borrower's entire life. Borrowers'

[18] 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/uploads/File/Report_PrivateLoans.pdf.

memories and records of payments made and other defenses to loan payment disappear over time. This leads to a second, key justification for time limits—bringing some peace of mind to borrowers and finality to the judicial system.

2. **Fix the disability discharge system**. Some reforms in this area will require Congressional action such as allowing borrowers to use evidence of a disability determination by another federal agency as presumptive proof for discharge. Other changes require administrative reform, including streamlining the application process and giving doctors reasonable guidelines and time to respond to requests for additional information.

3. **Restore bankruptcy rights.** The harsh treatment in bankruptcy for both federal and private student loan borrowers is based on two false assumptions: that higher education always leads to financial success; and that student loans are subsidized and thus, easier to pay. Unable to foreclose on a college education, banks have pressed Congress to place student borrowers in the same category as criminals and tax evaders. Excluding student loan debt from the possibility of bankruptcy protection is unrealistic and unfair. Bankruptcy is meant to give individuals and families in trouble a second chance at organizing their lives and achieving financial stability. Students in trouble deserve a fair shot at this protection, too.

4. **To better understand the true costs of collection, Congress should commission a study of all collection costs incurred in pursuing student loan debtors, including fees paid to collection agencies and paperwork costs.** Special attention should be paid to collection efforts against borrowers with little or no assets or income, including those living solely on Social Security payments.

5. **The government should cease collection when the costs clearly outweigh the potential revenues.** The limitless pursuit of vulnerable student loan borrowers has serious human and financial costs. Disabled and older consumers still face collection for loans they may have taken out thirty or forty years ago. Even if they have no other assets or property, the government may still take portions of their Social Security payments. The cost of collecting from those who simply do not have much is often greater than the meager amounts, if any, which ultimately come back to the government.

6. **Exempt certain borrowers from Social Security offsets, including those borrowers above age 75.**

7. **Provide for cost of living increases in the amount protected from Social Security offset.** The government cannot touch the first $750/month ($9,000/year) of a recipient's Social Security payments. The problem is that the limit is set in stone as of 1996, the year the law was passed.

8. **Grant borrowers facing federal benefits offset the same right to hardship reductions and suspensions that exist in administrative wage garnishment cases.**

9. **Exempt the Earned Income Tax Credit (EITC) from the tax refund offset program.** The EITC is based on income and household size and is only available to lower income working families with children.

CONCLUSION

If the changes discussed in this paper are not implemented, many at-risk borrowers will understandably be reluctant to finance higher education through loans, even federal loans. This chilling effect will continue to be a reasonable reaction to an overly harsh system. Unlike businesspeople and others in society who are encouraged to try new endeavors and given some cushion if they fail, there is no way out for most student loan borrowers who find that their educations are not paying off. The reforms proposed here will help extend IBR to all who need it.