Comment for the Record
Hearing on Financial Products for Students: Issues and Challenges

Maura Dundon and Leslie Parrish[1]
Center for Responsible Lending
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The Center for Responsible Lending (CRL) is pleased to provide a comment for the record on some of the issues covered in the Senate Banking Committee's hearing, "Financial Products for Students: Issues and Challenges" held on July 31, 2014. Students must make important choices related to how much they borrow and from what source, as well as how to conduct every day financial transactions and receive financial aid funds. In addition, standards should be enacted to ensure borrowers' loans are serviced in a fair and appropriate manner, and to safeguard a borrower's ability to seek redress when wronged. We detail our concerns related to these issues, and recommendations to protect students from predatory and unfair practices, in the sections below.

1. PRIVATE STUDENT LOANS

Still Risky for Legacy Subprime Borrowers, For-Profit College Students, and Servicemembers

Private student loans should be closely monitored by Congress and regulators. Although origination practices by some lenders do appear to have improved in recent years, the private student lending market historically engaged in lending with risky underwriting standards. Current practices, especially at for-profit colleges, may still place borrowers at risk.[2]

Many borrowers are still struggling today with the consequences of subprime private student loans. Spurred by an expanding market for asset-backed securities, private student lending grew rapidly in the early- to mid-2000s.[3] Just as with mortgages, credit standards weakened and lenders made increasingly aggressive loans. Many borrowers ended up with high, variable rate loans, when they could have chosen much safer federal loans. This resulted in defaults with far-reaching harmful consequences for borrowers, who are usually unable to discharge this type of loan in bankruptcy.

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[1] Maura Dundon is Senior Policy Council and Leslie Parrish is Deputy Director of Research.
[2] *See* Consumer Financial Protection Bureau, *Private Student Loans* (Aug. 29, 2012), http://www.consumerfinance.gov/reports/private-student-loans-report/ [hereinafter *CFPB Private Student Loan Report*].
[3] *Id.*

Private student loans are especially risky for for-profit college students.[4] This risk stems from the intrinsic features of the loan product (e.g., high, variable rates, and the lack of bankruptcy protection for most borrowers); deceptive practices when originating the loans (e.g., false claims about the school's job placement rate); and the low value of the education and high drop-out rates, which can negate the return on a student's loan investment. Since students of color enroll disproportionately in for-profit colleges, these financial practices also impact them disproportionately.[5]

As the Consumer Financial Protection Bureau (CFPB)'s recent complaint against ITT illustrates, banks partnered with for-profit colleges to offer students abusive private student loans that they know they would never be able to repay.[6] The Senate Committee on Health, Education, Labor and Pensions report on for-profit colleges also details the harmful private student loans made to for-profit college students, some with the cooperation of financial institutions.[7]

In addition to for-profit college students, servicemembers have also been vulnerable to private student loan problems. As demonstrated by the recent enforcement actions by the Department of Justice and FDIC against Sallie Mae Bank and Navient, Sallie Mae's servicing spin-off, private student loan owners and servicers have failed to ensure that active-duty servicemembers receive the benefits due to them under the Servicemembers Civil Relief Act, and have engaged in other unfair practices.[8]

School Certification Needed to Ensure Borrowers Exhaust Federal Loans

Although some students may appropriately use private student loans, private loans lack essential consumer protection features of federal student loans – namely, relief for distressed borrowers. For this reason, most borrowers should exhaust their federal options before turning to private loans. But over half (54%) of private student loan borrowers fail to exhaust their Stafford loan options first.[9] Improved loan counseling practices by schools, as well as improved federal school

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[4] *See* National Consumer Law Center, *Piling It On* (Jan. 2011), http://www.studentloanborrowerassistance.org/wp-content/uploads/2013/05/proprietary-schools-loans.pdf.

[5] *See* Leslie Parrish and Peter Smith, *For-Profit Colleges Saddle African-American and Latino Students with Crushing Debt and Poor Employment Prospects*, Center for Responsible Lending, http://www.responsiblelending.org/student-loans/research-policy/2014-CRL-Policy-Brief-For-Profit-Colleges-and-Students-of-Color-Summary-April.pdf.

[6] *See CFPB v. ITT*, No. 14-292 (S.D. Ind. filed Feb. 26, 2014), http://files.consumerfinance.gov/f/201402_cfpb_complaint_ITT.pdf; *see also*

[7] *See* Senate HELP Committee, *For Profit Higher Education: The Failure to Safeguard the Federal Investment and Ensure Student Success* (Jul. 30, 2012), http://www.help.senate.gov/imo/media/for_profit_report/Contents.pdf (click on chapters about individual schools to read details on private student loans).

[8] *See* Statement of Holly Petraeus, Consumer Financial Bureau (May 13, 2014), http://www.consumerfinance.gov/newsroom/statement-by-cfpbs-holly-petraeus-on-doj-fdic-enforcement-actions-against-sallie-mae/.

[9] *CFPB Private Student Loan Report*, *supra note TK*, at 10, 50-51.

certification requirements, could help ensure that students chose the best option for their financial situation.

Relief to Struggling Borrowers

Borrowers struggling to repay private student loans, particularly those originated under abusive standards, deserve a comprehensive package of relief. This includes a restoration of bankruptcy rights, which is a crucial backstop of consumer protection; increased refinancing options; enforcement actions by federal and state authorities to obtain restitution where appropriate; and protection against "robosigning" and other illegal debt collection practices.

Refinancing Federal Loans into Private Loans

Some financial institutions are currently refinancing federal student loans into private student loans, or have expressed interest in potentially doing so in the future. But refinancing a federal loan into a private loan would expose some consumers to higher risk, since they would lose their rights to federal income-based repayment plans and to rehabilitate defaulted loans. We are unaware of any private lender who contractually guarantees access to equivalent relief options. Thus, even if consumers receive an interest rate reduction via refinancing, refinancing into a private loan may in some cases leave them worse off. These emerging loan products should be developed and monitored with caution to ensure that only those borrowers who can truly benefit from refinancing out of federal loans receive such loans.

2. SERVICING

Student loan servicers can play an essential role in helping to prevent default. By identifying and counseling distressed borrowers, servicers can help enroll them in appropriate repayment plans before they default. Preventing default benefits the borrower, who avoids a negative credit report, and it also benefits the taxpayer, who continues to receive some payment on the loan.

We appreciate the recent efforts of the White House and Department of Education to reach out to distressed borrowers to enroll them into repayment plans.[10] But stronger and more decisive measures are needed. As long as servicing is outsourced to contractors, the Department of Education must draft and administer contracts in a way that achieves the goal of responsive and fair servicing.

Student loan servicing (both federal and private) should also conform to the high standards of consumer protection and customer service so that borrowers can responsibly manage their obligations. Servicers must provide easy, online access to account information and payment history. They must allow consumers to easily designate how to apply additional payments in

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[10] *See, e.g.,* Fact Sheet: Making College Affordable (Jun. 9, 2014), http://www.whitehouse.gov/the-press-office/2014/06/09/factsheet-making-student-loans-more-affordable.

order to minimize interest and fees, or to facilitate repaying their loans more quickly if they desire.

Finally, servicers must refrain from engaging in unfair and deceptive practices. For example, the FDIC sanctioned Sallie Mae Bank and Navient for applying payments in a way that maximized late fees.[11]

3. ARBITRATION

Forced arbitration clauses with class action bans are a common feature of consumer financial products, including private student loans.[12] These clauses in some cases purport to extend to the student loan servicer as well, even though the borrower never entered into a contract with the servicer.[13] Arbitration and class action bans serve to dampen consumers' ability to obtain redress and reform abusive practices. They compound the harm faced by students with predatory loans or faced with other illegal or unfair practices, especially servicemembers and for-profit college students. Accordingly, Congress and regulators should restrict the use of arbitration agreements in student loans and student loan servicing.

4. PARTNERSHIPS TO OFFER BANK ACCOUNTS AND/OR DEBIT CARDS

Schools often partner with financial institutions to offer bank accounts or prepaid debit cards as a way to facilitate students' receipt of financial aid funds and need to conduct everyday transactions. A recent study by US PIRG found that almost 900 of these partnerships exist, affecting over 9 million students.[14]

Unfortunately, even though schools may provide an implicit endorsement of these products by allowing co-branding, on-campus marketing, or other activities, the CFPB has concluded that these accounts do not have better features than accounts readily available in the broader marketplace.[15] For example, many of these accounts come with unique fees, such as a fee for a debit PIN transaction, or include abusive overdraft features, such as the ability to overdraw an account through a debit card transaction that could simply be declined for no fee; multiple and sustained overdraft fees; and the re-ordering of transactions to artificially generate more overdrafts. CRL's overdraft research has found that young adults are particularly vulnerable to

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[11] *See In the Matter of Sallie Mae Bank*, FDIC-13-0366b and 13-0367k (May 13, 2014), https://www5.fdic.gov/EDOBlob/Mediator.aspx?UniqueID=5007e0b4-911a-435c-9a0a-9d984ec5f53f.

[12] Public Citizen, *Between a Rock and a Hard Place: Courthouse Doors Shut for Aggrieved Private Student Loan Borrowers* (Jul. 2012), http://www.citizen.org/documents/private-student-loans-predatory-lending-arbitration-report.pdf.

[13] *See, e.g., Fensterstock v. Education Finance Partners,* 2012 WL 3930647 (S.D.N.Y. Aug. 30, 2012).

[14] U.S. PIRG, *The Campus Debit Card Trap: Are Bank Partnerships Fair to Students?* (May 2012), http://www.uspirg.org/sites/pirg/files/reports/thecampusdebitcardtrap_may2012_uspef.pdf.

[15] Consumer Financial Protection Bureau, *Perspectives on Financial Products Marketed to Students*, (March 26, 2014), http://files.consumerfinance.gov/f/201403_cfpb_presentation-to-department-education-rulemaking-committee.pdf.

accruing high overdraft fees generated by small, frequent debit card transactions.[16] Similarly, an FDIC study found that young adults were more likely to incur overdraft fees than accountholders generally.[17] These features are especially problematic since schools often enter into revenue sharing agreements with banks, creating a potential conflict of interest between doing what is in their students' best financial interest or maximizing the income generated from the students' adoption and use of these products.

Similar issues related to steering students to certain loans or credit cards have been addressed in the past; Congress and regulators now need to take action to also ensure students are not improperly steered into sponsored checking accounts or debit cards. In the case of financial aid disbursements, students should be encouraged to have funds directly deposited into their existing checking account, and any alternative account or debit card facilitated by the school should be presented in a neutral manner. Sponsored accounts marketed to students should be free of abusive features such as overdraft fees assessed on debit card and ATM transactions that could otherwise be declined at no cost. While some may argue that incorporating basic consumer protections into these accounts may mean that they are no longer attractive for a bank to offer (thus causing students to turn to expensive check cashers for their transaction needs), a CFPB analysis found that less than 0.5% of all students would be unable to secure their own checking account if a sponsored account was unavailable.[18]

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[16] *See* Center for Responsible Lending, *High-Cost Overdraft Practices* (July 2013), http://www.responsiblelending.org/state-of-lending/reports/8-Overdrafts.pdf.

[17] Federal Deposit Insurance Corporation, *FDIC Study of Bank Overdraft Programs* (November 2008), http://www.fdic.gov/bank/analytical/overdraft/FDIC138_ExecutiveSummary_v508.pdf.

[18] Consumer Financial Protection Bureau, *Perspectives on Financial Products Marketed to Students*, (March 26, 2014), http://files.consumerfinance.gov/f/201403_cfpb_presentation-to-department-education-rulemaking-committee.pdf.