
MEMORANDUM

February 10, 2022

TO: Interested Parties
FROM: Center for Responsible Lending
Student Borrower Protection Center

RE: One Door Closes & Others Remain: Institutional Loans and the 90/10 Formula

I. Introduction/ Non-federal Funding Under the 90/10 Rule and Closing the GI Bill Loophole

The “90/10 Rule” is meant to ensure that for-profit schools are, in fact, competitive in the marketplace and are not relying only on taxpayers to survive. In other words, the rule is based on the principle that a viable educational program should be funded in part by students or employers who are willing to pay cash to invest in career training for themselves or their employees, respectively. Although a small percentage of proprietary schools have failed the 90/10 test in recent years, between 11 and 20 percent of schools derive over 85 percent of their revenues from Title IV sources.¹

Because so many proprietary institutions’ revenue distribution falls so close to the 90/10 Rule threshold, it is important to pay close attention to the sources that for-profit colleges rely on as revenue. In some instances, schools rely on other forms of public funding, such as the GI Bill

¹ Hegji, A. April 26, 2021. “The 90/10 Rule Under HEA Title IV: Background and Issues.” *Congressional Research Service*. Available at https://www.everycrsreport.com/files/2021-04-26_R46773_ec4183000b224becae3d99e1b47610d95725cfbc.pdf.

or state funding, to pass the 90/10 test by the letter of the law, if not the spirit.² Other times, institutions draw funding from sources such as venture capital and private investors, unlike public and non-profit institutions which rely on charitable donations and state appropriations. Some of this revenue may represent tuition paid directly by students or their employers, but students often turn to private loans to finance their education after they have reached the limit of available Title IV funding.

Predatory institutions have sought out loopholes in the regulations in order to continue to extract federal and other public funding for programs that would not otherwise be capable of meeting 90/10 requirements. Historically, the 90/10 regulation's failure to include GI Bill benefits alongside Title IV funding as federal funding has created a major loophole that has enabled predatory practices that prey on student veterans and their dependents.³ As a result, tens of thousands of our nation's veterans have been lured into for-profit schools that have exhausted their educational benefits while leaving them with little to show for the time and money they invested.

In response to for-profits' disgraceful treatment of veterans, Congress directed the Department of Education to close this loophole in 2021 on a bipartisan basis with the passage of the American Recovery Act. The proposed regulations expand the coverage of the 90/10 rule to include federal funding beyond Title IV sources and include other federal sources, including the GI Bill.⁴ The draft language is an improvement on current regulations and meaningfully protects veterans and their dependents from exploitation.

² Public funding sources such as grants provided by nonfederal public agencies (such as states) or contracts (such as funding from the Workforce Innovation and Opportunity Act, or WIOA) are not counted in the numerator of the 90/10 formula. See: Hegji 2021.

³ Halperin, D. 2017. "Military-Branded Websites Push Veterans to Troubled For-Profit Colleges." *Huffington Post*. Available at https://www.huffpost.com/entry/military-branded-websites_b_9131742.

⁴ See proposed 34 CFR 668.28(a)(1).

II. Institutional Loans: Problematic in Principle

In addition to closing the GI Bill funding loophole, the Department's most recent proposed language to amend the 90/10 Rule allows annual repayment revenue on institutional loans to be counted as non-Federal sources of revenue.⁵ In particular, 34 CFR 668.28(5)(i) is amended to provide that an institution may include as revenue "the amount of payments made on [loans made to students and credited in full to the students' account at the institution] by current or former students." These loans must be "evidenced by standalone repayment agreements between the students and the institution that are enforceable promissory notes; issued at intervals related to the institution's enrollment periods; subject to regular loan repayment and collections by the institution; and separate from the enrollment contracts signed by the students."⁶ Additionally, the proposed regulations exclude as revenue institutional loans sold off to third-parties, or "any amount from the proceeds of the factors or sale of accounts receivable or institutional loans, regardless of whether the loans were sold with or without recourse."⁷

The Department's inclusion of payments on institutional loans may have the unintended consequence of incentivizing burdensome debt and unscrupulous practices by schools as lenders and debt collectors. While the proposed language's exclusion of the sale of receivables from revenue derived from institutional loans is a critical protection that could prevent institutions from issuing junk loans to students and profiting from a sale to third-party buyers, this change only partially protects students and, overall, the proposal threatens to leave open a significant loophole.⁸ Under the current proposal, consumer protections are sorely lacking to ensure that schools are not encouraged to issue risky and expensive loans to students and to use predatory

⁵ See proposed 34 CFR 668.28(a)(5).

⁶ Proposed 34 CFR 668.28(a)(5)(i).

⁷ Proposed 34 CFR 668.28(a)(6)(iv).

⁸ See proposed 34 CFR 668.28(a)(6)(iv).

debt collection debt tactics. Furthermore, institutional loans are often a bad deal for borrowers *because* their terms do not include benefits afforded to federal student loan borrowers, such as the right to income-driven repayment plans, an array of discharge opportunities, and an in-school deferment period.⁹

Discussions of non-federal aid have often conflated the role of private loans and institutional loans. Bona fide third-party private loans evince the belief not only among students, including those from low income households who do not have immediate access to cash, but also among lenders, of a worthwhile investment. On the other hand, institutional loans could incentivize an unscrupulous institution to put its own interests above those of its students. In this way, it is unsurprising that malfeasance on the part of for-profit schools has entailed both allegations of investor fraud following the failure to collect on such loans and predatory debt collection tactics (discussed further below) when for-profits do collect on institutional loans.¹⁰

III. Institutional Loans: Problematic in Practice

These objections are not purely theoretical and are, unfortunately, based on a troubled history of institutional loans offered by proprietary schools. As documented by the National Consumer Law Center, institutional loans emerged as a tactic by schools to issue loans to students when outside credit dried up during the 2008 credit crash.¹¹ While these loans have incredibly high default rates, schools keep issuing them because they “are recognized as loss leaders that keep the federal dollars flowing. There is so much profit reaped from federal student

⁹ Butrymowicz, S. & Kolodner, M. March 25, 2021. “Left in the Lurch by Private Loans From For-Profit Colleges.” *New York Times*. Available at <https://www.nytimes.com/2021/03/25/business/for-profit-colleges-private-loans.html>.

¹⁰ <https://www.sec.gov/litigation/complaints/2015/comp-pr2015-86.pdf>

¹¹ Loonin, D. 2011. “Piling On: The Growth of Proprietary School Loans and the Consequences for Students.” *Student Loan Borrower Assistance Program at the National Consumer Law Center*. Available at <https://www.studentloanborrowerassistance.org/wp-content/uploads/File/proprietary-schools-loans.pdf>.

aid funds that the massive losses experienced from these institutional loans are simply a cost of doing business.”¹²

There is evidence that schools are indeed not relying on these loans being paid back in full: a New York Times report from March 2021 revealed that one school with \$33 million in institutional loans expected that at least \$13 million of the total would never be repaid.¹³

Additionally, these loans could also be used by unscrupulous schools to artificially lower critical and high-stakes accountability metrics such as the cohort default rate, which is defined only by the repayment outcomes of a specific cohort of an institution’s *federal* student loan borrowers.

The Consumer Financial Protection Bureau’s (CFPB) recent announcement that it will investigate school’s institutional lending practices recognizes yet another concern regarding institutional loan practices that is especially prevalent among for-profit institutions: aggressive debt collection.¹⁴ As stated by CFPB Director Rohit Chopra, “schools that offer students loans to attend their classes have a lot of power over their students’ education and financial future.” Schools have been known to restrict enrollment for students who are late on their payments, withhold transcripts, accelerate payments for students who withdraw, and fail to issue refunds, among other abusive tactics such as pulling students out of class in front of their classmates until they pay off their debts.

IV. Recommendations

Given the troubled history of deception and aggressive debt collection involved in the making and collecting of institutional loans, respectively, the Department of Education should:

¹² Loonin 2011.

¹³ Butrymowicz & Kolodner, March 25, 2021.

¹⁴ Jan 20, 2022. “Consumer Financial Protection Bureau to Examine Colleges’ In-House Lending Practices.” *Consumer Financial Protection Bureau*. Available at <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-to-examine-colleges-in-house-lending-practices/>

1. Simply exclude the counting of revenue from institutional loans as a non-federal source of funding.
2. Short of not including institutional loans as a source of revenue, the Department could also consider discounting the value of institutional loans in the 90/10 formula calculation.