Center for Responsible Lending

The Center for Responsible Lending (CRL) is a nonprofit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, one of the nation's largest nonprofit community development financial institutions.

National Consumer Law Center

Since 1969, the nonprofit National Consumer Law Center (NCLC) has worked for consumer justice and economic security for low-income and other disadvantaged people in the U.S. through its expertise in policy analysis and advocacy, publications, litigation, expert witness services, and training.

STUDENT BORROWER PROTECTION CENTER

The Student Borrower Protection Center is a nonprofit organization focused on alleviating the burden of student debt for millions of Americans. The SBPC engages in advocacy, policymaking, and litigation strategy to rein in industry abuses, protect borrowers' rights, and advance economic opportunity for the next generation of students.

Department of Financial Protection and Innovation, Legal Division

Invitation for Comments on Proposed Rulemaking under the California Consumer Financial Protection Law
FILE NO: PRO 01-21
March 15, 2021
Submitted electronically to regulations@dfpi.ca.gov.

Introduction

On September 25, 2020, Governor Newsom signed AB 1864 (Chapter 157, Statutes of 2020), establishing the California Consumer Financial Protection Law ("CCFPL") under Division 24 of the Financial Code. The undersigned consumer advocates are encouraged to see that the Department of Financial Protection and Innovation ("DFPI" or the "Department") is seeking input from stakeholders in developing regulations to implement the CCFPL.[1]

We write this comment in response to the following questions regarding registration requirements that the DFPI posed in 3(a)-(b):

> For what industries should the DFPI first establish registration requirements under Financial Code section 90009, subdivision (a)? What consumer protection risks do those industries present to consumers that would make it appropriate to prioritize the registration of those industries over others?
>
> For each industry that a stakeholder states should be a priority for registration, what rules should the DFPI establish to facilitate oversight of the industry, what records should the DFPI require those registrants to maintain, and what requirements should the DFPI impose to ensure that covered persons are legitimate? (Fin. Code § 90009, subd. (b).) What data should the DFPI require registrants to submit in annual or special reports to the DFPI? (Fin. Code § 90009, subd. (f)(2)). Why should the DFPI collect this data?[2]

The focus of this comment will be on providers of private financing to students and families when paying for college ("Student Financing Providers"), including lenders providing so-called Income Share Agreements (ISAs). These firms often attempt to evade oversight from state regulators on the basis that their so-called innovative nature renders them unique financial products that, they argue, are not providing credit.

Under 90009(a), the DFPI is authorized "to prescribe rules regarding registration requirements applicable to a covered person engaged in the business of offering or providing a consumer financial product or service[.]"[3]

We urge the DFPI to register Student Financing Providers, including ISA lenders, using DFPI's authority under the CCFPL over credit.[4] Registration would further the stated intent of the DFPI: to promote nondiscriminatory access to responsible, affordable credit that reflect consumers ability to repay; to promote products that are not unfair deceptive, or abusive; and to promote consumer-protective innovation.[5]

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[1] DFPI, Invitation for Comments on Proposed Rulemaking Under the California Consumer Financial Protection Law (Feb. 4, 2021), available: https://dfpi.ca.gov/wp-content/uploads/sites/337/2021/02/2021-02-04-Invitation-for-Comments.pdf.
[2] *Id*.
[3] https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201920200AB1864
[4] Cal. Fin. Code § 90005(g).
[5] Assem. Bill 1864, 2019-2021 Reg. Sess. (Cal. 2020).

I. The Consumer Protection Risks Unique to Student Financing, Particularly ISAs, Render it Appropriate for the DFPI to Prioritize Regulating the Student Financing Marketplace, Including the ISA Industry.

Over the course of the past decade, a class of financing firms has emerged purporting to offer so-called innovative financing options to students and families seeking to pay for higher education. These firms often use alternative underwriting tactics and novel credit features when marketing products to students and families. These Student Financing Providers may offer financing structured to resemble a traditional, amortizing consumer loan. Or they may adopt alternative structures for repayment of the loans, including terms that tie monthly payments to borrowers' post-graduate earnings, known as ISAs.

ISA lenders use alternative criteria, such as a student's major and projected future income, to make private loans to fund a portion of educational costs in exchange for a percentage of the student's earnings over time.[6] Despite industry-touted benefits of innovation, ISAs can be especially dangerous because they allow private investors to put a super lien on a borrower's future income without, in many cases, guardrails against unfair practices.

While about 90% of student loan debt is held by the federal government, the reliance on debt to finance higher education has attracted private investors. ISAs are one emerging and increasingly prevalent form of student financing, marketed as an alternative to federal student loans. For-profit schools may also seek to use student financing, including ISAs, in the coming years to make up for lost revenue due to the federal government's tightening of the 90/10 loophole through the passage of the $1.9 trillion coronavirus relief bill.[7] As a general matter, we urge state governments to exhaust all public and philanthropic funding options to make higher education

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[6] *See*, *e.g.* Rustin IV, Dowse B. (Brad), Grayson, Neil E., & Degroote, Kiersty, M. (2017, February). Pricing Without Discrimination: Alternative Student Loan Pricing, Income-Share Agreements, and the Equal Credit Opportunity Act. American Enterprise Institute. Retrieved from https://www.aei.org/research-products/report/pricing-without-discrimination-alternative-student-loan-pricing-income-share-agreements-and-the-equal-credit-opportunity-act/ (discussing ISA's use of alternative, nontraditional lending factors, such as Alternative Finance (AltFinance), which prices loans based on a student's perceived likelihood of repayment).

[7] The "90/10 rule" or loophole is a constraint that for-profit colleges can receive no more than 90% of their total revenues from Title IV sources; this means that students must turn to other options, such as obtaining other grants or loans or using their own income or savings to pay for at least a portion of their education. The "90/10 rule," was put into place with the rationale that programs of sufficient quality should be able to attract students willing to invest some of their own funds towards their education. However, aid received by recent veterans as part of the new Post-9/11 GI bill does not count towards the 90% limitation on federal aid, since it is not a Title IV program. As a result, for-profit colleges target their recruitment efforts toward current and former members of the military, whose additional grant aid can be counted towards the 10% of funds that are intended to come from private sources. See generally Smith, P. & Parrish, L. (2014, Oct.). Do Students of Color Profit from For-Profit College? Poor Outcomes and High Debt Hamper Attendees' Futures. Center for Responsible Lending. Retrieved from https://www.responsiblelending.org/student-loans/research-policy/CRL-For-Profit-Univ-FINAL.pdf. On March 6, 2021, Congress passed the 1.9 trillion coronavirus relief bill that tightened the 90/10 loophole by changing how GI Bill dollars are counted such that GI Bill dollars would begin to be counted as federal money. Murakami, K. (2021, Mar. 2). Tightening the 90-10 Rule. Inside Higher Ed. Retrieved from https://www.insidehighered.com/news/2021/03/02/provision-covid-19-relief-bill-would-ease-incentives-profits-target-veterans; Murakami, K. (2021, Mar. 8). $40 Billion for Colleges. Inside Higher Ed. Retrieved from https://www.insidehighered.com/news/2021/03/08/senate-approves-40-billion-colleges.

affordable for their students, and we exercise great skepticism of predatory "novel" student financing products like ISAs to fund higher education, given the heightened consumer protection risks. While there may be some carefully constructed ISA programs that are relatively safe and provide a benefit to students, especially for programs where public funding and financing are unavailable, all programs must be subject to oversight and regulated as credit, and rules must be in place to prevent unfair, deceptive or abusive practices.

In addition to risks generally prevalent in the marketplace for private student loans and other student financing, ISAs present unique risks driven by the practices of existing ISA lenders and by the structure of this form of student financing. Amid the COVID-19 pandemic, ISAs are being touted by industry as a fix for financing education during uncertain economic times, but policymakers and institutions need to beware of the significant potential harm they could involve. During the pandemic, we have observed the following:

- unaccredited schools positing that "[d]uring economic instability, income share agreements can be a great tool to make higher ed more accessible & lower risk" for borrowers;
- traditional schools steering students toward these problematic financial products in an attempt to "future-proof . . . enrollment and revenue strategies" in anticipation of diminished state aid;
- direct-to-consumer ISAs masquerading as low-cost, non-debt alternatives for those who "can't obtain emergency grant funding," when in reality these products can be extremely high-cost with harmful borrower terms; and
- companies that facilitate investment in ISAs promising Wall Street an "attractive monthly cash return" well into the double digits, pointing to job re-training needs caused by the coronavirus pandemic.[8]

It is also important to note that ISAs are not limited to the education space. Companies – including one that has entered into a memorandum of understanding (MOU) with the Department of Business Oversight (DBO), DFPI's predecessor – are offering ISAs to pay for weddings or other types of consumer expenses. ISAs pose similar risks in this context and a similar danger of evasion of the protections of credit laws.

As these companies ramp up to capitalize on a national emergency, the players in the emerging ISA market are poised to repeat many of the higher education finance scandals that followed the 2008 financial crisis. Many ISA lenders echo the worst of these practices by peddling high fees and predatory loan terms under a veneer of so-called "innovation." ISAs can cost borrowers as much as 40 percent[9] of their pre-tax income and frequently include unconscionable contract

[8] Habash, T. & Kaufman, B. (2020, May 5). As Coronavirus Crisis Rages, ISA Companies Ramp Up to Reap the Rewards. Student Borrower Protection Center. Retrieved from https://protectborrowers.org/coronavirus-isa/.
[9] Morgan, Julia M., Farr, B. & Hornung, D. (2019, Jan. 10). Income Share Agreements: A Student Debt Promise Falling Short of Reality. Roosevelt Institute. Retrieved from https://rooseveltinstitute.org/2019/01/10/income-share-agreements-a-student-debt-promise-falling-short-of-reality/.

terms like mandatory arbitration agreements[10] or unfettered access to borrowers' bank accounts.[11] Moreover, the programs that these ISAs prop up often have a poor track record of student success,[12] including a history of actively misrepresenting students' academic and employment outcomes.[13]

ISA lenders also argue they should be able to operate wholly outside of basic consumer protection laws.[14] Because ISA lenders have asserted that they are not credit, they argue that federal consumer protection laws, such as the Equal Credit Opportunity Act (ECOA), which would protect against lending discrimination,[15]or the Truth in Lending Act (TILA), are inapplicable.[16] By denying that they are not "credit" and not "loans" ISA lenders also seek to evade state usury laws.[17] Despite their baseless claims, these laws are necessary to protect students.

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[10] *See, e.g.*, Back a Boiler Program ISA Sample Contract (Academic Year), Purdue Univ., Retrieved from https://www.purdue.edu/backaboiler/disclosure/contract.html (stating that the "Arbitration Agreement shall survive the termination of this ISA, your fulfillment or default of your obligations under this ISA and/or your or our bankruptcy or insolvency to the extent permitted by applicable law. In the event of any conflict or inconsistency between this Arbitration Agreement and the administrator's rules or other provisions of this ISA, this Arbitration Agreement will govern) (internal parentheticals omitted)).

[11] *See, e.g.*, Leif. ISA Agreement. Retrieved from https://leif.org/api/products/5b5b8bd0e59b743f9a086ed9/pdf (stating that as the ISA borrower "you agree that, prior to receiving any Earned Income, you have or will establish a bank account with a financial institution designated in writing with Leif ("Designated Bank Account") and also will permit integration of the Designated Bank Account with Leif's Platform as necessary to permit Leif to track your Earned Income, monitor account activity and balances, perform reconciliations and, if elected by you, process and withdraw your Monthly Payments from your Designated Bank Account. You further agree to provide details of the Designated Bank Account as Leif may reasonably request from time to time.").

[12] Schiffer, Z. & Farokhmaneh, M. (2020, Feb. 11). The High Cost of a Free Coding Bootcamp. The Verge. Retrieved from https://www.theverge.com/2020/2/11/21131848/lambda-school-coding-bootcamp-isa-tuition-cost-free.

[13] Woo, V. (2020, Feb. 19). Lambda School's Misleading Promises. NY Magazine: Intelligencer. Retrieved from: https://nymag.com/intelligencer/2020/02/lambda-schools-job-placement-rate-is-lower-than-claimed.html.

[14] Pearl, J. & Shearer, B. (2020, Jul.). Credit by Any Other Name: How Federal Consumer Financial Law Governs Income Share Agreements. Student Borrower Protection Center. Retrieved from https://protectborrowers.org/wp-content/uploads/2020/07/Pearl.Shearer_Credit-By-Any-Other-Name.pdf.

[15] Rustin IV, Dowse B. (Brad), Grayson, Neil E., & Degroote, Kiersty, M. (2017, February). Pricing Without Discrimination: Alternative Student Loan Pricing, Income-Share Agreements, and the Equal Credit Opportunity Act. American Enterprise Institute. Retrieved from https://www.aei.org/research-products/report/pricing-without-discrimination-alternative-student-loan-pricing-income-share-agreements-and-the-equal-credit-opportunity-act/.

[16] *See* AFR Statement on the ISA Student Protection Act: Income-Share Agreements are Just Student Debt with a Fancy Name. (2019, Jul. 17). Americans for Financial Reform. Retrieved from https://ourfinancialsecurity.org/2019/07/statement-income-share-agreements-just-student-debt-fancy-name/ (expressing concern for ISA Student Protection Act by Senators Mark Warner (D-VA), Todd Young (R-IN), Chris Coons (D-DE) and Marco Rubio (R-FL) for, *inter alia*, "preempt[ing] existing state usury laws, and any future usury laws that do not specifically target ISAs."); *see also* Kantrowitz, M. (2019, Dec. 1). History of Income Share Agreements. Saving for College. Retrieved from https://www.savingforcollege.com/article/history-of-income-share-agreements (arguing "[i]ncome-share agreements have been less successful in the U.S., in part because of state usury laws. This has [led] to caps on the total payments under an ISA and limits on the ratio of total payments to the amount originally received. Some proponents of income-share agreements have sought federal legislation to exempt income-share agreements from state usury laws.").

[17] *See* AFR Statement on the ISA Student Protection Act: Income-Share Agreements are Just Student Debt with a Fancy Name. (2019, Jul. 17). Americans for Financial Reform. Retrieved from

The risks posed by ISAs are illustrative of broader risks posed by emerging and incumbent providers of student financing. To the extent that Student Financing Providers, including ISA lenders, are operating in California, we urge the DFPI to regulate these firms and these products like other private financing products on the market.[18]

II. The DFPI Should Establish Registration Requirements under Financial Code section 90009(a) to Achieve the Stated Intent of the DFPI: to Protect Students from Unfair, Deceptive, or Predatory Practices.

The plainly stated intent of the legislature in passing the CCFPL was to expand DFPI's ability to "protect consumers from abusive financial practices, while prioritizing the prevention of unethical businesses from harming the most vulnerable populations including . . . students, low- and moderate-income individuals, and new Californians."[19] By focusing on regulating Student Financing Providers, including ISA lenders, the DFPI will achieve its stated intent.

Companies across the student financing industry, including ISA lenders, have been accused of a shocking range of abuses over the past two years alone. For example, these firms have faced credible allegations of:

- **Deceptive marketing by ISA lenders to students at large public universities.** In 2020, NCLC and SBPC filed a complaint with the Federal Trade Commission alleging that ISA provider Vemo undertook an illegal marketing scheme that made Vemo-backed ISAs appear cheaper than certain federal student loans, deceiving students at University of Utah and Purdue University about the cost of its products.[20]

- **Illegal lending by unlicensed coding bootcamps providing ISAs.** In October 2020, the California Bureau of Private Postsecondary Education issued the unaccredited coding bootcamp Lambda School a $50,000 fine for operating in California without a license, despite a prior warning by the state regulator about Lambda's noncompliance.[21] As part of this action, the state regulator uncovered that Lambda

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https://ourfinancialsecurity.org/2019/07/statement-income-share-agreements-just-student-debt-fancy-name/ (expressing concern for ISA Student Protection Act by Senators Mark Warner (D-VA), Todd Young (R-IN), Chris Coons (D-DE) and Marco Rubio (R-FL) for, *inter alia*, "preempt[ing] existing state usury laws, and any future usury laws that do not specifically target ISAs."); *see also* Kantrowitz, M. (2019, Dec. 1). History of Income Share Agreements. Saving for College. Retrieved from https://www.savingforcollege.com/article/history-of-income-share-agreements (arguing "[i]ncome-share agreements have been less successful in the U.S., in part because of state usury laws. This has [led] to caps on the total payments under an ISA and limits on the ratio of total payments to the amount originally received. Some proponents of income-share agreements have sought federal legislation to exempt income-share agreements from state usury laws.").

[18] The undersigned organizations do not endorse or support legislation enabling predatory ISAs. We believe state and federal consumer protection laws are strong and broad enough to regulate ISAs. However, we do believe consumer protections can be considered in the form of limiting which schools can offer ISAs, specifying prohibited acts, and establishing state reporting, licensing and/or registration requirements

[19] Cal. Fin. Code § 90000(a)(4).

[20] National Consumer Law Center and Student Borrower Protection Center, *In re: Vemo Education* (2020), https://www.nclc.org/media-center/advocates-file-complaint-with-ftc-urge-enforcement-action-against-vemo-education-for-its-deceptive-marketing-of-income-share-agreements-to-students.html

[21] California Bureau of Private Postsecondary Education, MODIFIED CITATION: ASSESSMENT OF FINE AND ORDER OF ABATEMENT (October 30, 2020); https://www.bppe.ca.gov/enforcement/actions/lambda_mod.pdf

misrepresented its authorization to operate in California to students taking Lambda-backed ISAs.

- **Educational redlining by Student Financing Providers.** February 2020, an SBPC investigation into fintech and banking products uncovered cases where a prospective borrower may be hit with thousands of dollars in additional credit costs if he or she attended a community college, an Historically Black College or University (HBCU), or a Hispanic-Serving Institution (HSI).[22] A subsequent investigation by members of the U.S. Senate exposed evidence of these practices at a wider range of student financing providers.[23]

- **Financing predatory schools by FinTech Student Financing Providers.** In August 2020, SBPC, Allied Progress, Americans for Financial Reform Education Fund, and Student Debt Crisis petitioned federal consumer protection and banking regulators to take action against PayPal Credit for online lending to students attending hundreds of for-profit schools, programs that are almost exclusively unaccredited, unproven, and lightly or wholly unsupervised.[24]

- **Deceptive marketing by third-party Student Financing Providers.** In October 2020, SBPC petitioned the CFPB to take action against Climb Credit, a fintech lender that offers loans students can use to finance attendance at job training programs ranging from coding bootcamps to teacher training courses.[25] As part of its underwriting model, Climb purports to have carefully vetted—and lends in part based on—the institution and program the borrower is looking to attend. SBPC warned that Climb's advertising appears to deceive borrowers, tricking them into taking out loans that are more expensive than represented for programs that may be of lower quality than Climb assures.[26]

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[22] Student Borrower Protection Center, *Educational Redlining* (2020); https://protectborrowers.org/new-report-finds-educational-redlining-penalizes-borrowers-who-attended-community-colleges-and-minority-serving-institutions-perpetuates-systemic-disparities/

[23] Senate Committee on Banking, Housing, and Urban Affairs, *Use of Educational Data to Make Credit Determinations* (2020); https://www.banking.senate.gov/imo/media/doc/Review%20-%20Use%20of%20Educational%20Data.pdf.

[24] Student Borrower Protection Center, Allied Progress, Americans for Financial Reform Education Fund, and Student Debt Crisis, *Advocates Sound Alarm on PayPal's Education Financing Partnerships with Over 150 For-Profit Schools* (2020); https://protectborrowers.org/advocates-sound-alarm-on-paypals-education-financing-partnerships-with-over-150-for-profit-schools/.

[25] Student Borrower Protection Center, *Advocates Warn Specialty Student Lender Climb Credit May be Deceiving Borrowers and Engaging in Pervasive Consumer Protection Violations* (2020), https://protectborrowers.org/advocates-warn-specialty-student-lender-climb-credit-may-be-deceiving-borrowers-and-engaging-in-pervasive-consumer-protection-violations/

[26] Student Borrower Protection Center, *The CFPB Must Investigate Climb Credit and Protect Borrowers Across the Dangerous, High-Cost Shadow Student Debt Market* (2020); https://protectborrowers.org/the-cfpb-must-investigate-climb-credit-and-protect-borrowers-across-the-dangerous-high-cost-shadow-student-debt-market/

Other documented and potential problems specific to ISAs include:

- **Unaffordable payments**. The payments required by ISAs may be far higher than under federal income-based repayment programs. The percentage of income to repaid may not include additional student loan payments on top of the ISAs**.**

- **Onerous terms and mechanisms that may make early repayment costly**. Though not styled as prepayment penalties, the structure of ISA loan repayment may effectively front-load high interest that could be avoided with early repayment of a traditional loan, resulting in extremely high effective APRs.

- **Inability to compare cost to traditional loans**. The lack of APR and total cost of credit disclosures make comparisons difficult.

- **Long loan terms that may be extended for years**.

- **Potential liability for breach of representations about finding work**. Disputes may arise about why a student is unemployed or underemployed.

- **Loan stacking**. ISA loans are usually not offered as a replacement for traditional education financing, like federal student loans, but are offered on top of other student financing sources, compounding student debt even further.

Furthermore, at least one ISA lender has created an ISA fund aimed at undocumented students, who are ineligible to receive financial aid, including Dreamers who are eligible for the Deferred Action for Childhood Arrivals program.[27] Given the potential for unfair practices, particularly against vulnerable populations, we urge the DFPI to regulate ISA lenders in a way that does not exacerbate the existing, deep racial wealth gap.

Student loan debt disproportionately impacts students of color. The results of historic and current segregation in higher education, as well as the existing racial wealth gap, makes the burden of student loan debt particularly heavy for Black and Latino communities, and ISAs are positioned to make this burden worse, particularly without proper regulation.[28] ISA lenders are likewise exploiting the failures of our state-funded education system for their own gain, and without adequate guardrails, the debt load will fare worse for our students of color.

Families of color are likely to have less income and family wealth to pay for college, are more likely to borrow for higher education, and typically have less of a cushion to withstand future financial shocks, thus contributing to a higher likelihood of delinquency and default on student loan debt. Black graduates are more than three times as likely to default on their student loans

[27] https://www.insidehighered.com/quicktakes/2018/09/20/income-share-agreements-undocumented-students
[28] Center for Responsible Lending and the National Association for the Advancement of Colored People. (2019, July). Quicksand: Borrowers of Color and the Student Debt Crisis. Retrieved from https://www.responsiblelending.org/research-publication/quicksand-borrowers-color-student-debt-crisis.

within four years as white borrowers, and Latino graduates are more than twice as likely to default as white graduates.[29] In California, for-profit college enrollees with far worse educational outcomes, are 15% African American compared to 5.4% African American in all nonprofit undergraduate institutions in the state.[30] Black students, and Black women especially, are targeted and recruited by schools that "exploit the failures of the non-profit higher education system—from the byzantine financial aid processes to recruitment practices that rarely reach high schools where the majority of students are people of color—for their own gain."[31]

Without critical rules to protect borrowers, ISAs targeted at this population will result in the same problems. Indeed, they will likely make those problems worse, as students may take out ISAs on top of other student debt. For-profit colleges, for example, target low-income students, women students, and students of color, who are already disproportionately enrolled in for-profit schools as nontraditional students struggling to manage family and work obligations to make better lives for their families. Such students are targeted with aggressive marketing, persuading them to invest heavily in the future with promises of successful careers and financial stability that ultimately do not materialize.[32] Often, these same students borrow more for college and struggle more with debt, and ISAs may exacerbate their debt burden.[33]

Thus, unless bold, regulatory action is taken by the DFPI with respect to Student Financing Providers, including ISA lenders, a generation of low-income students and students of color will be further ensnared in debt undertaken in an effort to advance their lives.

III. The DFPI Should Establish Registration Requirements for Student Financing Providers, including ISA lenders, under Financial Code section 90009(a).

i. The DFPI should establish registration requirements for Student Financing Providers, including ISA lenders, because they are engaged in the business of offering or providing a consumer financial product by extending credit and collecting debt under the CCFPL.

The CCFPL applies to all "covered persons," who are engaged in "offering or providing a consumer financial product or service to a resident of this state."[34] A "[c]onsumer financial product

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[29] Scott-Clayton, J. & Li, J. (2016). Black-white disparity in student loan debt more than triples after graduation. Brookings Institution. Retrieved from https://www.brookings.edu/research/black-white-disparity-in-student-loan-debt-more-than-triples-after-graduation/.

[30] https://www.responsiblelending.org/map/pdf/ca.pdf

[31] Jen Mishory, Mark Huelsman, and Suzanne Kahn, "How Student Debt and the Racial Wealth Gap Reinforce Each Other, The Century Foundation, September 2019, https://tcf.org/content/report/bridging-progressive-policy-debatesstudent-debt-racial-wealth-gap-reinforce/?session=1.

[32] In California, for-profit students are more likely to be low-income (54.3%), African-American (15%), and women (63%) compared to enrollment at California's public and private nonprofit four-year institutions. *See* Center for Responsible Lending, State of For-Profit Colleges: California. Retrieved from https://www.responsiblelending.org/map/pdf/ca.pdf.

[33] Morgan, Julia M., Farr, B. & Hornung, D. (2019, Jan. 10). Income Share Agreements: A Student Debt Promise Falling Short of Reality. Roosevelt Institute. Retrieved from https://rooseveltinstitute.org/2019/01/10/income-share-agreements-a-student-debt-promise-falling-short-of-reality/ ("ISAs like Back a Boiler exist *on top of* federal student loan debt often after students have exhausted their federal student loan eligibility, rather than as a replacement for it. ISAs that are stacked on top of existing debt can lead to excessively burdensome education financing payments after graduation.") (internal punctuation omitted).

[34] Cal. Fin. Code. §§ 90002(d); 90005(f).

or service" is defined as a "financial product or service that is delivered, offered, or provided for use by consumers primarily for personal, family, or household purposes."[35] The term "financial product or service" is further defined as including:

> Extending credit and servicing extensions of credit, including acquiring, purchasing, selling, brokering extensions of credit, other than solely extending commercial credit to a person who originates consumer credit transactions[;] [and]
>
> Collecting debt related to any consumer financial product or service.[36]

And, "credit" and "debt" are again further defined under the CCFPL as follows:

> "Credit" means the right granted by a person to another person to defer payment of a debt, incur debt and defer its payment, or purchase property or services and defer payment for those purchases.
>
> "Debt" means any obligation of a person to pay another person money regardless of whether the obligation is absolute or contingent, has been reduced to judgment, is fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured and includes any obligation that gives rise to right of an equitable remedy for breach of performance if the breach gives rise to a right to payment

Many so-called "innovators" in the marketplace for student financing provide traditional, amortizing consumer loans that may have some exotic features (e.g. alternative underwriting). Typically, the providers of this student financing acknowledge that their offerings are credit and a "consumer financial product," as defined in the CCFPL. However, as described above, other participants in the student financing market, particularly ISA lenders, may seek to sidestep regulation by disputing their classification as "credit" or "loans" or whether the collection of an ISA constitutes the servicing or collection of a debt.

By breaking ISAs down into their essential components, it becomes clear that ISA lenders are extending credit and collecting debt, such that they are covered by the CCFPL and should fall squarely within the purview of the DFPI.[37]

A growing body of research and analysis supports application of credit laws to ISAs.[38] We have appended this letter with a copy of one such analysis, *Credit By Any Other Name: How Federal Consumer Financial Law Governs Income Share Agreements*,

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[35] Cal. Fin. Code. § 90005(e).
[36] Cal. Fin. Code. §§ 90005(k)(1), (k)(10).
[37] Below we discuss the impact of the Consumer Financing Law (CFL) on ISAs.
[38] *See* Pearl, J. & Shearer, B. (2020, Jul.). Credit by Any Other Name: How Federal Consumer Financial Law Governs Income Share Agreements. Student Borrower Protection Center. Retrieved from https://protectborrowers.org/wp-content/uploads/2020/07/Pearl.Shearer_Credit-By-Any-Other-Name.pdf; Hayes, S. & Milton, A. (2020, Jul.). Solving Student Debt or Compounding the Crisis?: Income Share Agreements and Fair Lending Risks. Student Borrower Protection Center. Retrieved from https://protectborrowers.org/solving-student-debt-or-compounding-the-crisis-income-share-agreements-fair-lending-risks/; Roesch, B. (2020, Aug.). Applying State Consumer Finance and Protection Laws to Income Share Agreements. Student Borrower Protection Center. Retrieved from https://protectborrowers.org/applying-state-consumer-finance-laws-to-income-share-agreements/.

authored by two former senior regulators at the Consumer Financial Protection Bureau. In this analysis, the authors demonstrate that an ISA is an agreement in which:

- A lender promises to pay a sum to a student (usually distributed to a third party, the school);

- In exchange for the student's promise to repay the lender at a later time, by either:
    i. Paying a fixed Payment Cap that is higher than the sum the student received (in cases of early payoff or default); or

    ii. Making payments, calculated according to a formula in the agreement that is based on the student's income, over a period determined in the agreement.[39]

To this end, the authors argue:

> ISAs are functionally equivalent to student loans with income-driven repayment options. Both ISAs and student loans provide financing for higher education. They both require the borrower to repay with a set number of payments calculated as a percentage of income. In both circumstances, the monthly payments can be as low as $0. And student loans with income-driven repayment options are subject to federal consumer financial law governing credit, unless explicitly exempted. The fact that ISA lenders claim they do not extend credit to student borrowers does not change this analysis. In the consumer law context, courts consistently look to the substance of agreements over conclusory claims of the parties to determine whether an arrangement is an extension of credit. When faced with contracts that purport not to be "credit," courts will interpret the nature of the parties' agreement "after peeling away . . . labels from these transactions."

The authors conclude, and our undersigned organizations agree, that these components are sufficient to render ISAs "credit" under the CCFPL and to provide the DFPI with sufficient authority to regulate ISA lenders as part of any comprehensive effort to oversee the student financing market.[40]

It is worth noting that the definition of "credit" under the CCFPL is similar to – but even broader than – the ECOA definition. Under Regulation B implementing ECOA,, the term "credit" means "the right granted by a creditor to an applicant to defer payment of a debt, to incur debt and defer

[39] Pearl, J. & Shearer, B. (2020, Jul.). Credit by Any Other Name: How Federal Consumer Financial Law Governs Income Share Agreements. Student Borrower Protection Center. Retrieved from https://protectborrowers.org/wp-content/uploads/2020/07/Pearl.Shearer_Credit-By-Any-Other-Name.pdf.

[40] *Id*. (The authors further explain that "[w]ith this framing in mind, we turn to the analysis of why Income Share Agreements are "credit" under federal consumer financial law. ISAs typically claim, in the agreement, that they are not loans or extensions of credit. ISA lenders market these products as alternatives to traditional education loans55 and debt.56 The first words in the sample ISA contract Purdue makes available on its website are: "THIS IS NOT A LOAN OR CREDIT." Lenders contend that, even though students will have to later repay the money they have borrowed, ISAs present an opportunity to complete school "without worrying about interest rates or decades of student loan payments." The compliance bar has similarly taken the position that ISAs do not constitute extensions of credit and should not be subject to federal consumer protection regulation.")

its payment, or purchase property or services and defer payment therefor."[41] The CCFPL definition is similar with two important differences: It applies to the right granted by "a person to another person" – not just the right granted by a "creditor" – and CCFPL has a broad definition of "debt" that is lacking in ECOA (or TILA). Courts liberally construe the ECOA to achieve the statute's goal of eradicating credit discrimination – also a large part of the stated intent of the CCFPL.[42] Thus, the persuasive analysis that ISAs are credit under ECOA provide compelling reasons to view them as credit under the CCFPL.

The broader aspects of the CCFPL definition make it especially compelling to view ISAs as credit under California law. In particular, the CCFPL definition of "credit" incorporates the term "debt," and CCFPL gives "debt" a broad interpretation:

> "'Debt' means any obligation of a person to pay another person money regardless of whether the obligation is absolute or contingent, has been reduced to judgment, is fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured and includes any obligation that gives rise to right of an equitable remedy for breach of performance if the breach gives rise to a right to payment."[43]

Importantly, this definition extends to debt that is contingent, not fixed, or unsecured. ISAs certainly create an obligation to pay another person money, even though that obligation may be contingent, not fixed, or unsecured. Thus, ISA lender arguments touting that their agreements do not create debt or that they are nonrecourse fail in light of this broad California definition.

Moreover, the CCFPL definition of "debt" is essentially the same as the definition of "debt" under the federal Bankruptcy Code.[44] Congress intended the terms "debt" and "claim," which are coextensive,[45] to have "the broadest available definition,"[46] and they reach even to rights to payment that are unenforceable.[47]

Separate comments submitted by the National Consumer Law Center and Center for Responsible Lending regarding earned wage access programs ("EWAs") discuss additional reasons, also applicable to ISAs, as to why claims that products are not "credit" or "loans" under California law should be rejected.

As the DFPI is considering how to interpret the definitions of "credit" and "debt" as they apply to ISA lenders, it should also heed the advice of consumer legal experts who have rightly raised the alarm on ISA lender claims that their agreements are not subject to existing federal consumer

[41] 12 C.F.R. § 1002.2(j).
[42] Cal. Fin. Code. §§ 90000(b); 90019(a).
[43] Cal. Fin. Code § 90005(h).
[44] The Bankruptcy Code defines "debt" as a "liability on a claim." 11 U.S.C.§ 101(12). The Code defines a "claim" to mean "(A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured." 11 U.S.C. § 101(5). The Supreme Court has noted that Congress intended "that the meanings of 'debt' and 'claim' be coextensive." Pennsylvania Dep't of Public Welfare v. Davenport, 110 S.Ct 2126, 2130 (1990).
[45] Pennsylvania Dep't of Public Welfare v. Davenport, 110 S.Ct 2126, 2130 (1990).
[46] Johnson v. Midland Funding, LLC, 137 S. Ct. 1407, 1412 (2017).
[47] *Id.*

protection law because they— unlike private student lenders—do not extend credit. Accepting industry's arguments would leave ISA borrowers without the critical protections of ECOA, the FCRA, and TILA, among other laws.

ii. ISAs are consumer loans under the CFL, although this licensing regime would not be suited to ISAs.

If another California statutory scheme does not apply, such as one regulating retail installment sales or mortgage loans applies, credit then generally falls under the California Financing Law (CFL).

The CFL covers "finance lenders," defined as "any person engaged in the business of making consumer loans."[48] It is important to note, that in the definition of "finance lenders," the statute further defines "the business of making consumer loans," in relevant part:

> The business of making consumer loans . . . may include lending money and taking, in the name of the lender, or in any other name, in whole or in part, as security for a loan…any lien on . . . salary, earnings, income, or commission.[49]

Another provision of the CFL makes clear that a sale or assignment of a consumer's unearned, future salary in exchange for any payment is a loan:

> The payment by any person in money, credit, goods, or things in action as consideration for any sale or assignment of, or order for, the payment of wages, salary, commissions, or other compensation for services, **whether earned or to be earned**, is, for the purposes of regulation under this division, a loan secured by the assignment. The amount by which the assigned compensation exceeds the amount of the consideration actually paid is interest and charges upon or for the loan, calculated from the date of payment to the date the compensation is payable.[50]

ISA lenders are lending money, and taking a lien on salary, earnings and income. In addition to basic elements of ISAs, as discussed in the preceding section III(i) above, it is worth noting also, that in the case of some ISAs, including many coding "bootcamp" ISAs, students are also required to pay an initial deposit as consideration for the loan, in addition to the student's promise to repay the lender at a later time.[51]

Thus, the Department may determine that ISAs are providing consumer loans within the meaning of the CFL. The undersigned organizations support the analysis provided and conclusion stated in the comments regarding EWAs discussing that, for debits above $300, as well as all employer-based advances that do not debit bank accounts and thus are outside the California Deferred Deposit Transaction Law ("CDDTL") governing payday lenders, the CFL applies. And, that

[48] Cal. Fin. Code § 22009.
[49] Cal. Fin. Code § 22009.
[50] Cal. Fin. Code § 22335 (emphasis added).
[51] Crispe, I. (2021, Feb. 13), All About ISAs: Income Share Agreements and Deferred Tuition at Coding Bootcamps. Course Report. Retrieved from https://www.coursereport.com/blog/all-about-isas-income-share-agreements-and-deferred-tuition-at-coding-bootcamps.

EWAs should be required to obtain finance lender licenses and to comply with the CFL usury caps.

However, ISAs are typically large loans, over $10,000. For these larger loans, the CFL lacks any meaningful protection within its regime applicable to regulate Student Financing Providers, including ISA lenders that largely provide education financing to student borrowers.

Consumer loans subject to the CFL must comply with CFL's usury provisions. For small loans of the size typical of payday advances, CFL caps the rate at 2.5% per month (30% APR) for loans up to $225 and 2% per month (24% APR) for amounts over $225 up to $900. Larger installment loans between $2,500 and $10,000 are now capped at 36% plus the federal funds rate thanks to the passage of AB 539 in 2019. Loans above $10,000 made by licensed consumer finance lenders remain uncapped by CFL.[52]

Given that ISAs are intended to cover the cost of tuition and living expenses, those comparing the cost of ISAs measured against the cost of other higher education financing options assume a repayment amount that is comparable to the amount borrowed through either federal or private student loans to cover such costs.[53] This amount will very typically be much greater than $10,000, rendering the CFL—with no usury caps above $10,000—inappropriate to cover ISA lending.[54]

To the extent that loans are protected by the CFL's usury limits, DFPI does not have the authority to authorize lenders to evade those limits by giving them an alternative registration regime under the CCFPL without similar limits. For that reason, NCLC and CRL have explained in the comments on earned wage access products that the smaller loans offered by EWA providers must comply with the CFL usury limits (or, in the alternative, the constitutional 10% usury limit).

But for loans unprotected by CFL, CCFPL registration would not facilitate usury evasions. Therefore, DFPI should register them under CCFPL and adopt protections to prevent unfair, deceptive or abusive practices and address the risks of ISAs.

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[52] The 38% to 40% rate permitted by CFL is also quite high for loans at the upper $10,000 range, especially for student loans that may be outstanding for a number of years. These rates are simply too high for higher education financing, and out of step for even the most costly private financing options. We believe that the 10% constitutional usury limit is the more appropriate one for ISAs. If, however, DFPI rejects that view, it must apply the CFL limits to the extent that they apply. Otherwise, CFPI will be sanctioning usury evasions.

[53] *See*, *e.g*., Helhoski, A. & Lane, R. (2020, May 5). Income Share Agreements vs. Student Loans: Which Costs Less? NerdWallet. Retrieved from https://www.nerdwallet.com/article/loans/student-loans/how-income-share-agreements-stack-up-against-college-loans (comparing the cost of a $20,000 ISA at 10% of income over a 10-year term with a $20,000 PLUS loan with an APR of 7%, repaid over 10 years and a private loan of $20,000 with an APR of 9% with that same repayment period.)

[54] *See generally* Helhoski, A. & Lane, R. (2020, May 5). Income Share Agreements vs. Student Loans: Which Costs Less? NerdWallet. Retrieved from https://www.nerdwallet.com/article/loans/student-loans/how-income-share-agreements-stack-up-against-college-loans (comparing the cost of a $20,000 ISA at 10% of income over a 10-year term with a $20,000 PLUS loan with an APR of 7%, repaid over 10 years and a private loan of $20,000 with an APR of 9% with that same repayment period).

We additionally argue that the State's constitutional usury cap will apply and that while DFPI does not have the authority to adopt a usury cap, it also does not have the authority to exempt providers from a usury cap, as discussed below.

iii. ISA lenders should not be exempt from the California Constitution's usury limit.

In its request for comments, the DFPI asks whether it should issue regulations clarifying the applicability of state credit cost limitations, including rate and fee caps, to consumer financial products and services offered by covered persons.[55] If DFPI decides to register ISA lenders as covered persons CCFPL, it should clarify that the constitutional usury limit of 10% applies to them.

ISAs are a "loans … of money" under the California Constitution for similar reasons to their coverage under the other credit laws discussed in these comments. Further discussion of the meaning of "loan" under the Constitution can be found in the earned wage access comments of NCLC and CRL.[56]

We are cognizant that section 90009(a)(3) of the CCFPL shall not "be construed to give the department authority to establish a usury limit applicable to an extension of credit offered or made by a covered person to a consumer, except as otherwise provided for by statute." However, neither does the CCFPL exempt lenders from our state constitutional usury limit of 10%. Our Constitution provides a number of specific exemptions and authority for the legislature to exempt "any other class of persons authorized by statute."[57] But, DFPI does not have authority to create new exemptions by regulation.

The California Constitution renders any amount that an ISA lender charges that goes beyond a 10% interest rate be void and uncollectable. Any more is simply too high for higher education financing.

In addition, the history of the regulation of payday loans and high-cost installment loans illustrates the dangers of viewing ISAs as something different from traditional credit. Historically, usury and small loan laws helped rein in abusive lending. Within the past several decades, many states granted payday lenders exemptions from usury and small loan laws. Since then, payday lenders have used these exemptions to gouge borrowers with triple-digit interest

[55] Cal. Fin. Code § 90009(f)(3).
[56] The CFL does not include a definition for the term "loan," but in DBO's legal opinion letter issued on December 30, 2019, the DBO concluded that the definition of a "loan of money" found in Civil Code § 1912 should be used in defining the term "loan" for purposes of the CFL. See OP 7667 – Deferred payment products subject to CFL. (2019, Dec. 20). Department of Financial Protection and Innovation. Retrieved from https://dfpi.ca.gov/wp-content/uploads/sites/337/2019/12/Deferred-Payment-Products-cfl.pdf. While ISA lenders may claim that ISA borrowers do not agree to return an equivalent sum, their underwriting methods and the terms of the ISA contracts make it highly unlikely that the borrower will not be obligated to return at least as much as, and likely far more than, they borrow. Certainly, ISA lenders would not make loans to students on terms that they did not expect would be handsomely repaid. Thus, theoretical claims that the borrower is not committing to return the sum borrowed should be met with a high degree of skepticism.
[57] Cal. Const., art. XV. § 1.

rates.[58] Once abusive financial product lenders convince regulators that that products are different from traditional credit and deserve a different statutory scheme with different price limits, the Constitution exempts them from its usury cap through the exemption for any "class of persons authorized by statute." That exemption covers payday lenders licensed under the CDDTL that put people in a well-documented, unaffordable cycle of debt. That exemption also covers lenders licensed under the CFL even though the California Supreme Court deemed their rates "unconscionable" until the passage of AB 539 that capped rates on loans between $2,500 and $10,000.

ISA lenders are not licensed by CFL. There are no other constitutional or statutory exemptions from the constitutional usury cap that would be applicable to ISAs. Only the legislature "by statute" can authorize additional exemptions, not DFPI by regulation. Thus, the Constitutional usury cap of 10% should apply to ISA lenders. Indeed, capping the rates of ISAs at 10% makes public policy sense.

Among all households with student debt, the average interest rate is 5.8%, which includes both federal loans that make up 90% of all student loans, and private student loans.[59] Given that the Federal Reserve has cut rates to near-zero in response to the COVID-19 crisis, student loan rates are lower now than they have ever been to help students reeling from the economic devastation the pandemic has caused. Today, the "interest rate for all new federal direct undergraduate student loans decreased to 2.75%, down from 4.53% in 2019-20. Unsubsidized direct graduate student loan rates decreased to 4.30%, down from 6.08%. Rates for PLUS loans, which are for graduate students and parents, dropped to 5.30%, down from 7.08%."[60]

The Consumer Financial Protection Bureau (CFPB) has also long recommended that "public policy should emphasize the choice of a federal student loan" over a private student loan given that they are often more expensive, because rates are often variable, and repayment options are limited.[61] Publicly available data on private student loan interest rates is hard to find. But, at least one source states that among the sixteen best private student loans of March 2021, even variable rates—across all lenders, including those that did not disclose the minimum credit score required to qualify—ranged between 1.02% at the low end to 12.37%. Ascent, for example, provides a variable rate of 2.14%-12.37% for those with minimum credit scores of 540.[62]

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[58] https://www.responsiblelending.org/sites/default/files/uploads/modern-day-usury-the-payday-loan-trap.pdf

[59] Dancy, K. & Holt, A. (2017, Jun. 20). In the Interest of Few: The Regressive Benefits of Federal Student Loan Refinancing. New America. Retrieved from https://www.newamerica.org/education-policy/policy-papers/interest-of-few/.

[60] Helhoski, A. (2020, Sep. 3). Current Student Loan Interest Rates and How They Work. NerdWallet. Retrieved from https://www.nerdwallet.com/article/loans/student-loans/student-loan-interest-rates.

[61] Consumer Financial Protection Bureau. Private Student Loans: Report to the Senate Committee on Banking, Housing, and Urban Affairs, the Senate Committee on Health, Education, Labor, and Pensions, the House of Representatives Committee on Financial Services, and the House of Representatives Committee on Education and the Workforce. (2012, Aug. 29). Retrieved from https://files.consumerfinance.gov/f/201207_cfpb_Reports_Private-Student-Loans.pdf#page=16; Consumer Financial Protection Bureau. Student Loans: Choosing a Loan That's Right for You. Retrieved from https://www.consumerfinance.gov/paying-for-college/choose-a-student-loan/#o1.

[62] Helhoski, A., Clark, C. & Lane, R. 16 Best Private Student Loans of March 2021. NerdWallet. Retrieved from https://www.nerdwallet.com/best/loans/student-loans/private-student-loans.

As such, the constitutional usury cap of 10% that applies to ISA lenders in the absence of an exemption, is more in line with average interest rates for student financing.[63] The DFPI has an opportunity to act decisively to ensure that the regulation of ISA lenders does not follow the same pattern of oversight evasion that leaves the industry without any meaningful rate cap guardrails, and which leave consumer advocates playing whack-a-mole to curb their predatory practices.

IV. We Urge the DFPI to Impose the Following Minimum Requirements for Student Financing Providers, including ISA lenders, to operate in California to ensure their Legitimacy.

In DFPI's consideration of whether it should register Student Financing Providers, including ISA lenders, under CCFPL, and to prevent unfair, deceptive or abusive practices against students, we urge the Department to render void and unenforceable any student financing, including a student loan or an ISA, under the following non-exclusive conditions:

- The borrower's work authorizations changes (i.e. the borrower loses deferred action for childhood arrival authorization);
- The borrower dies;
- The borrower suffers from total and permanent disability;
- The school closes; or
- The university misled them or engaged in misconduct (i.e. UDAAP violations).

Moreover, we urge the following requirements to prevent unfair, deceptive or abusive practices against students specifically with respect to student financing that has an income-contingent repayment structure, including ISAs:

- Earnings disclosures in marketing should be based off actual earnings of graduates' starting median salary or, if it is a new degree program, based off of historical state workforce statistics or similar location specific data; disclosures should not be based on salaries that differ from the lender's internal assessments for business planning or accounting purposes or from those use to estimate profits for investors or potential investors.

- Impose reasonable initial term limits for repayment. Students should not be signing up for extended periods of indentured servitude. Disclosures should conspicuously warn students of the potential longer extended time period.[64]

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[63] *See generally* Helhoski, A. & Lane, R. (2020, May 5). Income Share Agreements vs. Student Loans: Which Costs Less? NerdWallet. Retrieved from https://www.nerdwallet.com/article/loans/student-loans/how-income-share-agreements-stack-up-against-college-loans (comparing the cost of a $20,000 ISA at 10% of income over a 10-year term with a $20,000 PLUS loan with an APR of 7%, repaid over 10 years and a private loan of $20,000 with an APR of 9% with that same repayment period).

[64] Banard, J., Darcus, Joanna K., Harrington, A., Howarth, R., Shafroth, A., Taylor, K., Yu, P. Road to Relief: Supporting Federal Student Loan Borrowers During the COVID-19 Crisis and Beyond. CRL & NCLC. Retrieved from https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/nclc-crl-road-to-relief-23nov2020.pdf (finding "CFPB research using credit reporting data for a large sample of student loan borrowers

- Deferments for financial distress or other specified events should be allowed as long as there is a reasonable hard cap on term that is not extended due to these paused payments. Deferments should not result in negative reports to credit bureaus.

- DFPI's supervision of the servicing of any student financing with an income-contingent repayment structure, including ISAs, should include close oversight of the process for asserting claims that a borrower has violated the agreement by failing to seek work. Financing agreements that give lenders too much discretion to claim breach of contract for those who cannot find work or are unable to work for various reasons post risks to borrowers.

- The cost of repaying any student financing with an income-contingent repayment structure, including an ISA early should be capped to prevent an inappropriate prepayment penalty or a usurious loan. That cost should be calculated to ensure that the student does not pay an effective interest rate of more than the constitutional 10% limit and that the loan does not violate the prohibition on prepayment penalties under TILA.

V. Required Disclosures Should be Required and Should at a Minimum Require APR Disclosures per DBO's Align MOU and Mirror California's Private Student Loan Disclosures.

On February 9, 2018, Department of Business Oversight (DBO) entered into a Memorandum of Understanding (MOU) with Align Income Share Funding ("Align"). Align states that while "other companies offer ISAs as a way to pay for education, Align offers ISAs to use for any cash need, whether it's consolidating debt, paying a medical bill, or planning your wedding."[65]

The MOU does not resolve competing arguments about whether the ISAs are loans or whether Align is covered by CFL. But, as part of the MOU, the DBO required that Align modify its ISA agreement to require that on the first page, and before offering its product to California consumers, Align disclose the effective APR "assuming funds were provided to the consumer as a loan rather than pursuant to an ISA."[66] The DBO also required the APR disclosure to be based on a calculation of the Federal Reserve Board's APR method as set forth in Regulation Z, and delineated scenarios for when the APR should be calculated.

We urge DFPI to require APR disclosures for all student financing, including ISAs, as well as disclosures of the finance charge and total of payments in a similar fashion as required to be disclosed under TILA. However, we urge that the DFPI seek input from the public prior to determining a calculation method. We urge that the disclosures for Student Financing Providers, and ISA lenders specially, must include an APR calculated based on the assumptions currently in Regulation Z for fixed and variable rate credit for private student loans and based on

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shows that for the longest-studied cohort, the proportion of borrowers fully paying off their loans begins to flatten out after 8 years in repayment. At 14 years, 20% of borrowers have an outstanding balance on their loans, and additional years of repayment appear to yield little to nothing towards the achievement of full repayment.").

[65] Align. Income Share Agreements. Retrieved from https://www.helloalign.com/products/income-share-agreement.
[66] Align also argued that its ISA product was not a "loan" under California law, such that it triggered a requirement to be licensed under the CFL. DBO did not make a determination as to whether its ISA product was a loan, and whether it would trigger an obligation to get a license under the CFL.

assumptions established by the DFPI for ISAs' variable payment and other features. ISA lenders must provide consumers with the cost of comparable federal and private student loans at the time of application.

Furthermore, we urge that additional disclosures for any student financing with an income-contingent repayment structure, including ISAs, must be required. These disclosures should largely mirror what is at minimum required for private student loans in California, and should also include:

- a statement that the transaction creates debt and is a loan;
- the loan term;
- the interest rate;
- whether the interest rate is variable or fixed;
- the minimum salary level required for repayment to begin;
- under what conditions the ISA will be terminated;
- information communicating that if a graduate anticipates working at a Public Service Loan Forgiveness program-qualifying job, and/or anticipates that their debt-to-income ratio will be high, then subject to underwriting and other considerations, federal student loans may be a much better option due to loan forgiveness and other flexible repayment options; and
- a warning that any ISA loan will stack upon any outstanding federal student loan and private loan obligations, and that this should be considered by the student prior to taking out an ISA loan.

VI. The DFPI Should Require Registrants to Submit Annual Reports to Prevent against Student Financing Provider Abuse and to Promote the Intent of the CCFPL.

Student Financing Providers, including ISA lenders, should adhere to comprehensive reporting requirements, especially as new forms of student financing, including ISAs, are emerging and there is not enough data to fully understand the harm these loans could bring to borrowers. At a minimum, we urge the following to be provided to the Commissioner at the time of registration and not less than once per year thereafter:

- a list of all schools at which the student financing company or lender has provided loans to a borrower residing in this State;
- the volume of loans made annually to borrowers residing in California;
- the volume of loans made annually at each school;
- the default rate for borrowers obtaining loans from the student financing company or lender;
- the rate of borrowers that have payment terms extended and the extent by which they have been extended;
- actual borrower salaries and how they compare to the estimates and disclosures at time of origination;

- any debt collection or other activities in which the ISA lender or its agents engage to collect payments;
- any complaints received;
- a copy of each model promissory note, agreement, contract or other instrument used by the student financing company during the previous year to substantiate that a private education loan has been extended to a borrower or that a borrower owes a debt to the student financing company; and
- the name and address of the student financing provider and any officer, director, partner or owner of a controlling interest of the student financing provider.

We also encourage the Commissioner to create a publicly accessible website that includes the following minimum information about Student Financing Providers registered in California to promote transparency for borrowers:

- the name, address, telephone number and website for all registered Student Financing Providers, including ISA lenders;
- a summary of the information as discussed in the reporting requirements above; and
- copies of all model promissory notes, agreements, contracts, or other instruments provided to the Commissioner as described above.

Finally, DFPI should create a publicly available complaints database for all consumer financial products and services, similar to the database published and maintained by the CFPB. That database should include publicly available complaint narratives, appropriately redacted to protect the complainant's privacy.

VII. Conclusion.

Thank you for the invitation to comment and for your thoughtful consideration of our collective feedback on the regulation of ISAs herein. If you have questions, please contact Marisabel Torres marisabel.torres@responsiblelending.org; Mike Pierce mike@protectborrowers.org; or Lauren Saunders at lsaunders@nclc.org.

Sincerely,

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