CENTER FOR RESPONSIBLE LENDING

June 4, 2013

The Honorable Arne Duncan
Secretary
Department of Education
c/o Wendy Macias
1990 K Street NW, Room 8017
Washington, D.C. 20006

Re: Docket No. ED-2012-OPE-0008, Negotiated Rulemaking Committee

Dear Secretary Duncan,

Thank you for the opportunity to comment on the Department of Education's proposed topics for a negotiated rulemaking committee addressing federal student aid programs under Title IV of the Higher Education Act (HEA).

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. Our work grows directly from our affiliation with Self-Help, one of the nation's largest nonprofit community development financial institutions. For over 30 years, Self-Help has worked to create ownership and economic opportunity in underserved communities through responsible loans and financial services. Self Help has provided $6 billion in financing to help more than 75,000 low-wealth borrowers buy homes, start and build businesses, and strengthen community resources across the country, and serves more than 88,000 mostly low-income families through 30 retail credit union branches. We look forward to sharing our perspective with the Department.

This comment focuses on two areas of the proposed negotiated rulemaking agenda: gainful employment and the "adverse credit" standard for Parent PLUS loans.

Gainful Employment

We commend the Department for continuing its efforts to require for-profit colleges to prepare their students for gainful employment. For-profit colleges have engaged in some of the worst practices in higher education, saddling many students with high debts they have little ability to repay, often on the basis of deceptive representations.[1]

The Department should continue to use its two original tests to measure gainful employment: the debt-to-income measurement (DTI), and loan default rates.

DTI is an appropriate measure of whether an institution has prepared its graduates for gainful employment. DTI is commonly used by lenders as one factor in measuring an individual's ability to repay credit. A high debt-to-income ratio could indicate that the graduate's debt burden is incommensurate with his or her earning capacity. This lack of earning capacity indicates that the student had not been prepared for gainful employment.

Student loan default rates are also a reasonable measure of gainful employment. A high default rate may indicate poor educational quality and a resulting lack of income -- i.e., a failure to prepare a student for gainful employment. While a default rate cutoff lower than 35% could be justified, the Department's original 35% default rate by any measure indicates a failure of gainful employment. If *one in three* students defaults on student loans, the school is failing to prepare students for gainful employment. Seen from another angle, if potential students were informed that they had a one in three chance of defaulting on their loans after enrolling, many would likely agree that the school fails to provide an education that leads to gainful employment to its student body.

Furthermore, high default rates may have a spillover effect harming the gainful employment of students who do not default.   Defaults by a significant proportion of students could harm the school's reputation with employers in the community. High default rates could also spur sanctions by states and accreditation organizations.   These consequences of high default rates could reduce the value of the credential for students who do manage to graduate and avoid default, and hurt their chances at gainful employment.

Parent PLUS Loans Underwriting and "Adverse Credit"

We agree that the rulemaking committee should re-examine the interpretation of "adverse credit" for approval of Parent PLUS loans. The Department should take this opportunity to institute more appropriate overall underwriting standards for these loans. Good underwriting can help ensure that parents do not take up unmanageable debt, while preserving access to education for those who do qualify. No family should be saddled

1 *See, e.g.,* U.S. Gov't Accountability Office, GAO-10-948T, *Undercover Testing Finds Colleges Encouraged Fraud and Engaged in Deceptive and Questionable Marketing Practices* (Aug 4, 2010) (finding that all 15 of for-profits investigated engaged in deceptive practices); Staff of Senate Health, Education, Labor, and Pensions Committee, 112th Congress, *Report on For Profit Higher Education: The Failure to Safeguard the Federal Investment and Ensure Student Success* (Jul. 30, 2012) (identifying a "wide range of problems that run deep within the for-profit sector").

with Parent PLUS loans – which are not dischargeable in bankruptcy and do not enjoy the same repayment and forgiveness benefits as other federal loans – unless they can repay it.

Good underwriting has two components: an assessment of the borrower's objective ability to repay, and an assessment of their propensity or likelihood of actually repaying. Ability to repay should be assessed by looking at the borrower's complete financial life, which may include assets, debts, income, and the debt-to-income ratio. Propensity to repay can be assessed by the borrower's credit history or credit score.

The Department's existing regulations only perform half of the underwriting equation. The assessment is limited to a rudimentary credit check for "adverse credit history," such as delinquencies and charge-offs. 34 C.F.R. § 685.200(c)(I)(vii)(A)(1) and (c)(I)(vii)(B). Although the regulations also allow consideration of "extenuating circumstances" if the parent has an adverse credit history, § 685.200(c)(I)(vii)(A)(3), this screening may not properly identify the borrowers who can and cannot repay their loans.

The Department should formulate a comprehensive underwriting standard for Parent PLUS loans that includes both ability to repay and an appropriate credit history test. The HEA gives the Department broad authority to perform such underwriting. It requires screening for an "adverse credit history," but does not define the meaning of "adverse" to be limited to a traditional credit report. 20 U.S.C. § 1078-2(a)(1)(A). In addition, the HEA allows the Department to institute other "eligibility criteria" in awarding PLUS loans. § 1078-2(a)(1)(C). These statutory provisions give the Department leeway to consider a Parent PLUS applicants' entire financial history to assess ability to repay, including total debt and income, and to perform a fair evaluation of propensity to repay through a credit check that reflects the applicants' current propensity to repay. For low-income consumers, this credit history or score could include nontraditional items indicating a likelihood of repaying, such as rent and utility payment records. The rulemaking committee should also consider what kind of negative items on credit reports constitute truly "adverse credit" that demonstrate a *current* propensity not to repay a loan.

While we believe the Department's Parent PLUS underwriting standards should be improved, we recommend that the Department inform schools and students in advance about any changes. Students should not face a last minute crunch from unexpected Parent PLUS denials. Although the Parent PLUS program must not saddle parents with unmanageable debt, changes in eligibility should not needlessly disrupt students' education. With enough advance notice about eligibility changes, students and schools may be able to fill in the gaps and minimize disruptions to enrollment.

Sincerely,

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