NEW AMERICA
FOUNDATION

Comments of Benjamin Miller and the Education Policy Program at the New America Foundation

Prepared for the Negotiated Rulemaking Public Meeting at the U.S. Department of Education
October 8, 2008

Thank you for the opportunity to share our thoughts today on issues to be addressed during the negotiated rulemaking process for Public Law 110-315, the Higher Education Opportunity Act (HEOA). As the first major reauthorization of the Higher Education Act in a decade, HEOA raises a number of issues and concerns that the New America Foundation would like to bring to your attention.

The New America Foundation is a nonprofit, nonpartisan public policy institute that invests in new thinkers and new ideas to address the next generation of challenges facing the United States. The foundation's mission is animated by the American ideal that each generation will live better than the last. To this end, we are especially interested in issues of access, quality, and affordability as it relates to higher education.

We at New America support a number of provisions in HEOA that are designed to protect students from unscrupulous private lenders, shame colleges for excessive price hikes, and curb the increasing costs of university textbooks. We also believe that there are a number of provisions that have the potential to be beneficial but only if they are executed with careful consideration by the Department. What follows is a list of our concerns related to current provisions in the law. We are here today to make you aware of these issues as you pursue the negotiated rulemaking process.

Guaranty Agencies

Guaranty Agency Default Reduction Activities: Title IV, Part B, Sec. 433A. Consumer Education Information

Guaranty agencies are currently tasked with helping to prevent defaults among borrowers holding loans from the Federal Family Education Loan (FFEL) Program. To carry out this role, guaranty agencies may use their operating funds to pay for "default aversion activities," activities which they often cite to justify their existence within the FFEL program. Though operating funds are not government assets (as opposed to federal funds,

which are) the money deposited in them comes from several federal sources of reimbursement.

The HEOA expands the mission of guaranty agencies by enlarging the definition of default reduction activities to include "high-quality educational programs and materials to provide training for students and families in budgeting and financial management." While budgeting and financial management are important issues for students and their families, we would caution against allowing guaranty agencies to appropriate operating funds for these purposes without putting mechanisms in place to measure whether such activities are useful or effective. We suggest that when implementing the expanded definition of default reduction activities, the Department also include requirements for guaranty agencies to demonstrate the effectiveness of their activities in reducing both their cohort and lifetime default rates. Given that these operating funds are largely aided by taxpayer contributions and are supposed to benefit students, it does not make sense to continue dedicating dollars toward programs or initiatives that have not been evaluated to determine whether they are having substantial positive effects on those they are intended to help.

Exit Counseling by Guaranty Agencies, Non-Profit Lenders, and For-Profit Lenders: Title IV, Part B, Sec. 422 Federal Payments to Reduce Student Interest Costs and Title IV, Part C, Sec. 493 Program Participation Agreements

While the HEOA explicitly prohibits guaranty agencies and student lenders from performing student aid functions required of a college or university, it does allow an exemption for borrower exit counseling. The lenders' exemption, however, states that college staff must maintain control of the counseling and that companies cannot promote specific loan companies during the course of the counseling. Despite these protections, we are concerned that the legislation does not sufficiently protect students from being exposed to lender marketing during exit counseling.

We have two main concerns: 1) Lenders participating in counseling will find a way around restrictions by branding their names across materials that are incorporated into the sessions, and 2) the legislation contains less stringent regulations for guaranty agencies, even though many are closely linked to non-profit lenders.

To counteract these concerns, we propose that the Department include strong language requiring increased school oversight of exit counseling. Specifically, none of the counseling materials should be branded with the name of any lender, nor should counselors mention any loan company or guaranty agency during counseling. To additionally allay concerns about the crossover between guaranty agencies and non-profit lenders, we propose that guaranty agencies engaging in counseling activities be subject to the same limitations as student loan companies. Finally, school officials overseeing counseling activities by electronic methods should have to do so in real-time, ensuring that they are actively overseeing the sessions.

Guaranty Agency Involvement in pilot PLUS loan auction program, Title IV, Part I, Sec. 499 Competitive Loan Auction Pilot Program Evaluation

The pilot PLUS loan auction program represents an exciting opportunity to harness market forces in determining the ideal subsidy companies should receive in exchange for originating student loans. The HEOA improves on this by including penalties that would be imposed on winning lenders that fail to meet the terms of the auction—such as not making loans for all eligible individuals in a given state. These penalties create incentives to ensure that winning lenders will provide PLUS loans in a state, which should ease concerns about federal loan availability that have cropped up during the credit crunch. However, we are concerned that the introduction of guaranty agencies into the pilot auction will increase complexity and the potential for conflicts of interest—all without providing tangible benefits to parents and students.

For these reasons we propose that the Department of Education be allowed to be designated as the pilot's guaranty agency. The pilot PLUS auction is designed to be a partnership between the Department and winning lenders. It is up to the Secretary of Education to enforce and monitor lender compliance—a main role of guaranty agencies in the FFEL program. Since the Department is already handling the compliance role, it seems inefficient to introduce an outside party solely to guarantee against losses.

We are also concerned that the close ties between several guarantors and non-profit lenders could lead to conflicts of interest if certain non-profit lenders were to win PLUS auctions. Some of these agencies share the same office building, require a vote of both boards in order to issue tax-exempt bonds, and even have the same websites. This is problematic because guaranty agencies are supposed to have an oversight role in the FFEL program. It is questionable that this role would be properly carried out if a non-profit lender connected to a guaranty agency were to win one of the two spots to exclusively make loans in a state. We suggest the Department handle this issue by serving as the guarantor on all loans in a state if one of the winning lenders is closely connected with the designated guarantor for that state.

For-Profit Colleges and Universities

Incentive Compensation Rules, Title IV, Part G, Sec. 493 Program Participation Agreements

In 1992, Congress added a provision to the Higher Education Act prohibiting colleges from giving "any commission, bonus, or other incentive payment based directly or indirectly on success in securing enrollments." The ban on incentive compensation for college recruiters was included as part of a broader effort by lawmakers to crack down on fly-by-night trade schools that had been set up to reap profits from the federal student aid programs. With reports rampant that trade schools were enrolling unqualified low-income individuals simply to get access to federal student aid funds, policymakers believed it was important to bar postsecondary-education institutions from paying recruiters on the basis of how many students they enrolled.

A decade later, in November 2002, the Department of Education issued new regulations that significantly weakened this prohibition. As part of these rules, which were enacted over the objections of the negotiated rulemaking panel that had been assembled to consider them, the Department created 12 safe harbors to the ban on incentive payments.

The Department created these exemptions even though some of them clearly appear to violate the law —such as ones that allow commission-based recruiting for non-Title IV programs at colleges participating in the federal student aid programs and that allow colleges to provide commission-based payments to managerial or supervisory employees who are not directly involved or do not supervise those involved in recruiting. At the very least, these provisions can be easily gamed to provide school officials with the type of incentives the statute is trying to prevent.

Over the last six years, some of the largest publicly-traded for-profit higher education companies have come under intense scrutiny from federal and state regulators and have faced numerous lawsuits by former employees, shareholders, and students over allegations that they have engaged in misleading recruiting and admissions tactics to inflate their enrollment numbers. In 2004, for example, the Department reached a $9.8 million settlement agreement with the University of Phoenix after the agency concluded that the school had knowingly violated the incentive compensation ban. Last year, the U.S. Supreme Court allowed a False Claims lawsuit to proceed against the University of Phoenix over allegations by former recruiters who say they were compensated solely on their success in enrolling students.

In light of these controversies, the Department of Education should use the upcoming negotiated rulemaking sessions to reconsider the rule changes it made in 2002 to weaken the compensation ban. The Department should eliminate loopholes that have made it harder for the agency to ensure the integrity of the federal student aid programs and safeguard students.

Prevent Gaming of 90-10 Rule: Title IV, Part G, Section 493 Program Participation Agreements

As part of the reauthorization legislation, Congress made significant changes to a key consumer protection provision that aims to protect students from unscrupulous trade schools. This provision, which is known as the "90-10 rule" requires proprietary institutions to receive at least 10 percent of their revenue from sources other than federal student aid in order to participate in the aid programs. The HEOA expands the sources of funds that trade schools can count toward the 10 percent threshold, including institutional scholarships and tuition discounts. We worry that these changes are open to wide interpretation and can be easily gamed by institutions. As our colleagues at The Institute for College Access and Success pointed out in their testimony, unless the Department is careful, schools could inflate their published tuition by $5,000 and then give all students a $5,000 "grant," and claim it as a discount that qualifies as non-Title IV revenue. We would urge the Department to define qualifying discounts that prevents this form of gaming.

Private Student Loans

Private Student Loan Self Certification, Title X, Subtitle B, Sec. 1021 Private Education Loan Disclosures and Limitations

Private student loans have undergone exponential growth over the last decade—increasing by 894 percent in the last 10 years, according to the College Board. We are concerned that one reason for this jump in private loan volume is confusing and misleading marketing practices

by loan companies that lead students to take out expensive private loans before exhausting their federal loan eligibility. Another contributing factor is that students can obtain direct-to-consumer private loans without contacting their schools' financial aid offices. School officials have a wealth of knowledge about how to help defray the cost of college and could point students toward substantially cheaper financing opportunities. In fact, both Barnard College and Colorado State University saw substantial decreases in the volume of private student loans taken on by their students following the induction of a policy that requires students to meet with financial aid officials before private loans are certified.

While the HEOA does not contain a requirement for school certification, it does contain a provision that requires students taking out private loans to first obtain a self certification form from their schools. Without careful regulation, the self-certification requirement will do little to curb private loan borrowing or better inform students of their financing options.

First, we are concerned that colleges will simply mail these forms to all students, absolving themselves from taking an active role in students' considerations of private loans. Certainly, an item mailed en masse is less likely to be carefully read by a consumer, which lessens the potential beneficial effect. To counter this, we suggest that the Department consider requiring schools to provide a certification form only following a direct request from a student. This personal level of contact is more likely to result in counseling and follow-up on the parts of both the financial aid officer and the student.

Second, we are concerned that the model form to be developed by the Secretary of Education and the Board of Governors of the Federal Reserve System will not contain enough personalized information to fully demonstrate to borrowers their alternative financial aid options. We propose that the Department require schools to provide students with additional information that is more detailed than what is currently in legislation. Institutions should make use of the National Student Loan Data System to determine how much, if any, federal student aid students have used. This form should then inform students how much of their federal financial aid eligibility has been exhausted and how much more is available. For dependent and graduate students, this figure should include the availability of PLUS loans. Moreover, when listing these items the forms should provide a side-by-side comparison of federal options and private loans, including loan limits based upon the school's cost of attendance, interest rates, deferment, forbearance, and income-related repayment opportunities.

For federal aid, the form should also contain information on the estimated cost of repaying the entire loan so that students can compare it to private loan materials that lenders are now required to provide. The form should also disclose the difference between the estimated cost of attendance and the total amount of federal aid (grants and loans) available to students. Additionally, it should contain information about how students can find out more about federal aid sources, including the number for the school's financial aid office and the Department's Federal Student Aid Information Center.

Thank you again for this opportunity to share our thoughts on the negotiated rulemaking process, and we look forward to the Department's implementation of the HEOA.