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May 27, 2014

The Honorable Arne Duncan
Secretary of Education
U.S. Department of Education
400 Maryland Avenue, SW
Washington, DC 20202Re: Program Integrity: Gainful Employment
Docket ID ED-2-14-OPE-0039

Dear Secretary Duncan,

Thank you for the opportunity to comment on the proposed rule governing Program Integrity: Gainful Employment. Woodstock Institute is concerned about unscrupulous career education programs, often at for-profit schools, that encourage students to take out high amounts of debt and provide little benefit to the student in return. Many of these programs seem to target low-wealth students and students of color.

The Department of Education's rules that require career education programs to "prepare students for gainful employment in a recognized occupation" or risk losing eligibility for receiving Title IV federal loans and other aid play a crucial role in holding institutions accountable for the quality and the costs of their programs. Woodstock Institute applauds the Department for moving forward with issuing proposed rules for determining whether students are being adequately prepared for a career. The rules in their current form are not rigorous enough to provide meaningful protections for student borrowers, however, and should be strengthened. Given Woodstock Institute's more than 40 years of experience with a broad range of consumer credit issues, this letter will focus on the portion of the rule determining the debt-to-earnings standards. In particular, we recommend that:

- The debt-to-earnings calculation should consider other types of debt and a realistic amortization period in order to generate a more accurate picture of a borrower's debt burden.
- The interest rate used to calculate payment amounts should use the highest interest rate over the six-year period preceding the cohort year, rather than the average interest rate.
- The debt-to-earnings metric should clarify that program performance is evaluated on an absolute basis, rather than relative to other programs.
- Language regarding the inclusion of private student loans should be strengthened to define how a school should determine a student's private student debt load.
- The minimum number of graduates required for a program to be evaluated on its debt-to-earnings metric should be reduced from 30 graduates to 10 graduates.

In addition to the concerns raised in this letter, we support the letter submitted by the Center for Responsible Lending and the letter submitted by the coalition of advocates led by the Institute for College Access and Success.

About Woodstock Institute

Woodstock Institute is a leading nonprofit research and policy organization in the areas of fair lending, wealth creation, and financial systems reform. Woodstock Institute works locally, statewide, and nationally to create a financial system in which lower-wealth persons and communities of color can safely borrow, save, and build wealth so that they can achieve economic security and community prosperity. We conduct research on financial products and practices, promote effective state and federal policies, convene a coalition of community investment stakeholders working to improve access to credit, and help people use our work to understand the issues and develop and implement solutions.

Background

Abusive and predatory practices in the for-profit college sector create barriers to economic security, particularly for low-wealth people and people of color. There is significant evidence that some for-profit colleges make false promises about employment prospects to their students, fail to adequately prepare them for their career of choice, and encourage students to take out excessive debt to pay for exorbitant tuition and fees. The easy access to credit, strong financial incentives for institutions to hype student loans, and deceptive and aggressive marketing tactics are reminiscent of the abuses that led to the collapse of the housing market. As with the mortgage crisis and other examples of predatory lending, people of color and low-wealth people bear the brunt of the worst practices.

Poorly performing for-profit colleges are not responsible stewards of public funds. These schools can receive up to 90 percent of their revenues from federal loans and aid, but are not producing skilled graduates that the economy needs to grow. As the Department pointed out in a recent analysis, 72 percent of for-profit college graduates make less than high school dropouts.¹ For-profit college students comprise 13 percent of all college students, but nearly half of all defaults on federal student loans.²

For-profit colleges target low-income students and students of color. More than half of dependent students at for-profit colleges in 2007-2008 come from families with incomes below \$40,000, compared to 35 percent of dependent students at public two-year schools.³ Even worse, for-profit colleges are an expensive option for low-income students. Net tuition and fees at for-profit colleges for dependent students with family incomes below \$32,000 in 2007-2008 was \$8,360, which is higher than public two-year schools (where the net tuition and fees was \$0), public four-year schools (\$0), and the lowest and second-lowest cost quartiles of private nonprofit colleges (\$1,630 and \$6,250, respectively).⁴

Students of color disproportionately enroll at for-profit colleges, with African American students representing 13 percent of all college students but 22 percent of for-profit college students.⁵ While the industry heralds this fact as a sign of their commitment to underserved communities, low-income students and students of color are simply gaining access to a system that sets them up to fail. Just 22 percent of for-profit college students who began a four-year degree in 2002 graduated within six years, compared to 55 percent of public college students and 65 percent of private nonprofit students. For African American students, the figures are more stark—just 16 percent of African American students who started a four-year degree at for-profit colleges in 2002 graduate within six years, compared to 39 percent of African American students at public colleges and 45 percent of African American students at private nonprofit

¹ Ritsch, Massie. "Fact: Too many career-training programs lead to low wages, high debt." Homeroom: The Official Blog of the U.S. Department of Education. March 2014.

² Ibid.

³ Baum, Sandy and Kathleen Payea. "Trends in For-Profit Postsecondary Education: Enrollment, Prices, Student Aid and Outcomes." CollegeBoard Advocacy & Policy Center. April 2011.

⁴ Ibid.

⁵ Deming, David, Claudia Goldin, and Lawrence Katz. "The For-Profit Postsecondary School Sector: Nimble Critters or Agile Predators?" *Journal of Economic Perspectives* 26.1 (Winter 2012): 139-164.

colleges.⁶ The Department must take action to correct an industry that targets those who historically have been poorly served by the education system and can least afford the high costs and low rewards of for-profit colleges.

Representatives of the for-profit college industry claim that the gainful employment rules will penalize them for enrolling high numbers of low-income students and students of color.⁷ This claim suggests that the fact that the students are low-income or people of color is the reason for the poor loan performance at for-profit colleges rather than the excessive debt burden and poor quality of the education they provide. Research shows, however, that for-profit college students are more likely to default on their loans than students at other schools, even controlling for demographic characteristics like race.⁸ Woodstock's experience working to reform predatory products and practices in the mortgage, payday lending, and other consumer credit markets shows that providing access to debt that produces poor outcomes for borrowers reduces, not expands, opportunities for people of color and low-income people to build wealth. Although subprime mortgage lenders argued that they provided access to credit for borrowers of color, research shows that those mortgages were much more likely to go into default than soundly-underwritten, fixed-rate mortgages to low-income borrowers and people of color.⁹ Woodstock's research found that subprime mortgage lending substantially increased the number of foreclosures in a neighborhood even after controlling for demographics like race,¹⁰ and other research demonstrates that those subprime loans increased foreclosures even among neighboring borrowers with good mortgages.¹¹ Providing students with debt for an education that sets them up to fail cannot be rationalized by arguing that the borrowers fail because they are students of color and will harm their ability to improve financial outcomes in the future.

Federal and state law enforcement agencies are investigating claims that for-profit colleges are aggressively steering students into high-cost loans and making deceptive claims about job placement and graduation rates. In Illinois, where Woodstock Institute is based, Attorney General Lisa Madigan sued Westwood College in 2012 for deceiving students by claiming that their criminal justice program would prepare them for jobs in law enforcement. In reality, the degree was not accepted by many law enforcement agencies because Westwood is not regionally accredited. Students often accrued \$50,000-70,000 for a degree that could not land them a relevant job. Nearly 95 percent of the 1,300 complaints about colleges received by General Madigan's office in 2012 concerned unfair practices at for-profit colleges.¹² Other state Attorneys General are investigating for-profit college abuses across the country as well.¹³ The Consumer Financial Protection Bureau (CFPB) launched an investigation into ITT Educational Services for steering students into high-cost private student loans with few consumer protections and misleading students about the loan terms.¹⁴ Each new investigation adds to the evidence

⁶ Baum *op. cit.*

⁷ Blumenstyk, Goldie. "For-Profit Colleges Decry Gainful-Employment Rule as 'Arbitrary and Biased'." *The Chronicle of Higher Education*. May 27, 2014. See also: Fain, Paul. "Nowhere to Go." *Inside Higher Ed*. May 27, 2014.

⁸ Hillman, Nicholas. "College on Credit: A Multilevel Analysis of Student Loan Default." *The Review of Higher Education* 37.2 (Winter 2014): 169-195.

⁹ Ding, Lei, Roberto G. Quercia, and Janneke Ratcliffe. "Risky Borrowers or Risky Mortgages? Disaggregating the effects using Propensity Score Models." *Journal of Real Estate Research* 33. 2 (2011): 245-277.

¹⁰ Immergluck, Dan and Geoff Smith. "Risky Business: An Econometric Analysis of the Relationship Between Subprime Lending and Neighborhood Foreclosures." Woodstock Institute. March 2004.

¹¹ Ding, Lei, Roberto G. Quercia, and Janneke Ratcliffe. "Neighborhood Subprime Lending and the Performance of Community Reinvestment Mortgages." *Journal of Real Estate Research* 32. 3 (2010): 341-376.

¹² "Madigan Sues National For-Profit College: Westwood College Used Deceptive Marketing to Lure Students into Thousands in Debt, Limited Job Opportunities." Office of Illinois Attorney General Lisa Madigan. January 18, 2012.

¹³ "Attorney General Kamala D. Harris Files Suit in Alleged For-Profit College Predatory Scheme." Office of California Attorney General Kamala Harris. October 10, 2013. See also: Lauerman, John. "For-Profit Colleges Face New Wave of State Investigations." *Bloomberg News*. January 29, 2014.

¹⁴ "CFPB Sues For-Profit College Chain ITT For Predatory Lending." Consumer Financial Protection Bureau. February 26, 2014.

that for-profit colleges are engaging in many of the same deceptive practices that subprime mortgage lenders used to trap borrowers in a cycle of unaffordable debt.

It is evident that for-profit colleges are targeting historically underserved groups, such as low-income students and students of color, with aggressive marketing tactics that hide the truth about the benefits of their programs and the high costs students incur. The result is that many students who can least afford it leave school—often without a degree—and are unable to find jobs that pay them enough to repay staggering debt loads. The consequences can be severe, including being subject to the government’s extraordinary debt collection powers (such as garnishment of wages and benefits); the near-impossibility of discharging student debt in bankruptcy; and limited ability to build wealth through homeownership, entrepreneurship, and retirement savings. There is a clear and pressing need for the Department to enact strong gainful employment rules that protect students from the damage poorly performing for-profit colleges cause their finances and life prospects.

The Debt-to-Earnings Metric

The Department defined two debt-related metrics that evaluate whether schools are adequately preparing students for gainful employment. This strategy sensibly assesses students’ financial outcomes after they leave school, which is a reasonable indicator of whether the education provided adequately equipped the students to find employment.

The proposed rule includes two metrics, the debt-to-earnings (D/E) ratio and program cohort default rate (pCDR), that must both be met in order for the program to pass. This letter will focus its recommendations on the D/E measures.

A program passes the D/E measures if the average debt service of a cohort of its graduates is less than or equal to 20 percent of graduates’ discretionary income, or if the average debt service of the program’s graduates is less than or equal to eight percent of graduates’ total income. A program would be “in the zone” if the average debt service of a cohort of its graduates was greater than 20 percent but less than 30 percent of their discretionary income or if the average debt service is greater than eight percent but less than 12 percent of total income. A program would fail under the D/E measures if the average debt service of a cohort of its graduates was at least 30 percent of discretionary income and at least 12 percent of total income. A program would only have to pass the D/E metrics if 30 or more students complete the program in a year. A program loses eligibility for Title IV aid if it fails for two out of three consecutive years, or if it is failing or in the zone for four consecutive years.

The reasoning behind the D/E measures is sound: if graduates, on average, cannot find employment that allows them to afford their student loan payments, then they have not been prepared for gainful employment. It also follows the principle of assessing borrowers’ ability to repay their debt, which has been accepted as a sound underwriting standard across many types of consumer credit because it reduces a borrower’s likelihood of defaulting on his or her loan. Although this proposed rule does not govern student loan originations, the ability to repay standards of other financial products can provide useful lessons—such as how to define “affordability” for different classes of debt—to the Department as it determines how to assess whether graduates earn enough income to repay the debt they incurred for their education. Woodstock has advocated for implementing ability to repay standards for a variety of debt products, and many of them have been enacted:

- **Payday lending.** In Illinois, Woodstock engaged in a ten-year campaign to enact consumer protections for high-cost short term loans, such as payday and installment loans. These loans were often made without regard to borrowers’ ability to repay them, and borrowers were regularly trapped in a cycle of expensive debt. Now, short-term lenders in Illinois cannot extend credit

where the payments exceed 22.5 – 25 percent of a borrower’s monthly income (depending on the loan term).¹⁵

- **Bank payday, or deposit advance, lending.** Some banks offered high-cost, short term loans called “deposit advance” loans that posed similar threats to consumers as do payday loans. In May 2013, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation released regulations that, among other provisions, required banks to determine borrowers’ ability to repay their loans by examining six months of inflows and outflows from borrowers’ bank accounts.¹⁶
- **Mortgage lending.** The Dodd-Frank Act charged the CFPB with drafting rules that require mortgage lenders to consider a borrower’s ability to repay before extending credit. The “qualified mortgage” rules, finalized in January 2013, require lenders to consider a borrower’s ability to repay by documenting employment status, income and assets, non-mortgage debt, credit history, and other factors.¹⁷
- **Credit cards.** The Credit CARD Act of 2009 requires credit card issuers to consider borrowers’ ability to make payments on their accounts before approving a new credit line or extending a credit limit. Issuers must take into account income, assets, and existing debt obligations.

These ability to repay rules reflect a growing consensus among federal and state regulatory and legislative bodies that lenders should verify whether the credit product is affordable to the borrower. Many of these rules require lenders to include in the debt-to-income calculation not only the credit they are offering borrowers, but their other debt obligations as well. A person with zero other debt will have a very different ability to afford new credit payments than another person with the same income and a high level of other debt.

Woodstock Institute applauds the Department for including an assessment of the affordability of the debt incurred for an education in its gainful employment rules. The provision needs to be further strengthened, however. Our recommendations include:

The debt-to-earnings calculation should consider other types of debt and a realistic amortization period in order to generate a more accurate picture of a borrower’s debt burden.

We appreciate the Department’s desire to include in its calculations of D/E ratios “the most complete picture of the indebtedness a student has incurred to enroll in a GE program.” Appropriately, the calculation includes not only federal loans, but private and institutional loans as well. There is evidence that students use methods other than federal, private, and institutional loans to finance their college educations, however. Fourteen percent of all undergraduates and eight percent of undergraduates who are citizens or resident aliens and who attended for-profit colleges in 2011-2012 reported that they used credit cards to pay tuition and fees.¹⁸ Students may use other types of credit to pay for the cost of attendance as well, such as home equity lines of credit or payday loans.

Students may have college-related costs, such as housing costs, over which they have little control in addition to the costs already included in the debt calculation (tuition, fees, books, equipment, and supplies). Schools may steer students towards on-campus housing options if the institutions have a financial interest in placing students in their on-campus housing and arrange housing through the financial

¹⁵ Monsignor John Egan Campaign for Payday Loan Reform. “Governor Quinn signs landmark payday loan reforms.” Woodstock Institute. June 21, 2010.

¹⁶ Eccles, Courtney. “Regulators finalize rules to protect consumers from predatory “bank payday loan” products.” Woodstock Institute. November 25, 2013.

¹⁷ Buitrago, Katie. “New CFPB rules crack down on irresponsible mortgage lending.” Woodstock Institute. January 10, 2013.

¹⁸ Woodstock Institute analysis of National Postsecondary Student Aid Survey Data, 2011-2012. This analysis is limited because half of the survey respondents skipped the question, but it does indicate that some students are relying on credit cards to pay the cost of attendance.

aid process, even though off-campus housing options may be more affordable to students. The Department should include housing costs in the debt metric as well.

Additionally, we are concerned that the D/E measure may not actually portray what is an affordable level of debt for low-income workers. The eight percent of discretionary income threshold was derived from established mortgage underwriting standards that recommend restricting housing debt to 28 percent of income and total debt to 36 percent of income. If graduates have other kinds of consumer debt, spending eight percent of their income on student debt payments may be unaffordable to them, particularly if they have low incomes. The Department should consider ways of examining other types of debt in its D/E measures.

Finally, the amortization period used by the Department to calculate annual debt burden should accurately reflect how long it takes students to repay their loans. The Department proposes an overly long amortization schedule: 10 years for certificates and associate degrees, 15 years for bachelor's and master's degrees, and 20 years for doctoral or professional degrees. Since "the substantial majority of borrowers entering repayment in 2012, regardless of credential level, are in the standard repayment option of 10 years,"¹⁹ the Department should use an amortization period of 10 years for all borrowers so that they reflect the payments that students are most likely to make. Failing to examine other types of credit used to cover college expenses, overlooking graduates' other consumer debt obligations, and using overly long amortization periods may understate borrowers' total debt burdens and overstate how well their schools prepared them for gainful employment that will allow them to earn enough to repay their loans.

The interest rate used to calculate payment amounts should use the highest interest rate over the six-year period preceding the cohort year, rather than the average interest rate.

The proposed rule calculates borrowers' student debt payments using the average interest rate in the six years prior to the cohort year. The Department states that the rationale for using the average interest rate is that it "helps minimize year-to-year fluctuations in the interest rate that would be applied to the D/E rates calculations and therefore would lead to more predictability for institutions."²⁰ While using the average interest rate may benefit colleges, it does not accurately capture how student debt payments may strain graduates' budgets. Borrowers should be able to afford their loan in periods of high interest rates as well as low interest rate periods, and using the average rate could obscure periods of particularly high interest. The Qualified Mortgage rules governing ability to repay for mortgage borrowers instructs lenders to calculate ability to repay based on the highest interest rate the loan could reach in a five-year period.²¹ Similarly, we recommend that the Department calculate payments based on the highest interest rate observed in six years prior to the cohort year, rather than the average interest rate over six years.

The debt-to-earnings metric should clarify that program performance is evaluated on an absolute basis, rather than relative to other programs.

In several places in the proposed rule, the Department makes reference to the "worst" programs. The Notice mentions that the debt metrics will "identify the worst performing programs"; the "lowest performing programs"; and "the very worst performers."²² It is critical that the Department clarify that the programs will not only be judged relative to the performance of other institutions, but that programs will be evaluated on their own ability to meet the gainful employment standards. For example, if all for-profit colleges performed poorly on the D/E and pCDR tests, the Department should sanction all of them, not just the worst performers of a bad group.

¹⁹ Program Integrity: Gainful Employment. 34 CFR Section 668.404: Amortization.

²⁰ Program Integrity: Gainful Employment. 34 CFR Section 668.404: Interest Rate.

²¹ 12 CFR Section 1026.43: "Minimum standards for transactions secured by a dwelling."

²² Program Integrity: Gainful Employment. 34 CFR Section 668.403

Language regarding the inclusion of private student loans should be strengthened to define how a school should determine a student's private student debt load.

Students' private student loan debt is an important component of determining the total debt loads incurred at a particular program. According to the CFPB's report to Congress, for-profit college students are more likely to use private student loans than students at other types of colleges.²³ The proposed rule requires schools to include the "total amount the student received from private student loans for enrollment in the program that the institution is, or should reasonably be, aware of." We are concerned that this statement provides an opportunity for ill-intentioned institutions to circumvent the D/E measure. Institutions could intentionally fail to record students' private student loan usage and claim that they could not have been reasonably expected to know about the loans. Private student lenders are not required to notify schools that they are providing credit to their students, and some market directly to students. The Department should explore ways to close this loophole, perhaps by requiring institutions to survey students about their methods of financing their education.

The minimum number of graduates required for a program to be evaluated on its debt-to-earnings metric should be reduced from 30 graduates to ten graduates.

We are concerned that institutions could evade evaluation on the D/E measure by gaming the enrollment in their programs so that they fall under the 30-graduate threshold. The Department's analysis indicates that they could lower the minimum program size to as few as ten graduates and still achieve statistical accuracy. We urge them to do so. Expanding the universe of programs that are evaluated on how well they prepare students for gainful employment means that more students will be protected from unscrupulous practices.

Conclusion

Thank you for the opportunity to comment on the proposed rules regarding gainful employment. We applaud the Department for moving forward with this rulemaking that is critically important to the financial security of students across the country. We urge the Department to revise the D/E metrics so that they accurately depict graduates' debt burdens, clarify how performance will be measured, and limit opportunities for exploiting loopholes.

Sincerely,



Dory Rand
President, Woodstock Institute

²³ "Private Student Loans." Consumer Financial Protection Bureau Report to Congress. August 2012.