May 22, 2018

NASFAA Bankruptcy Comments

On behalf of the National Association of Student Financial Aid Administrators (NASFAA), I submit these comments in response to the Request for Information (RFI) published February 21, 2018, concerning the Department's guidance pertaining to bankruptcy filings. NASFAA represents nearly 20,000 financial aid professionals who serve 16 million students each year at approximately 3,000 colleges and universities of all sectors throughout the country. NASFAA member institutions serve nine out of every ten undergraduates in the U.S. These comments are supported by the American Council on Education.

We appreciate the Department's request for comment on the efficacy of current guidance for treating bankruptcy filings. In this response, we:

- Caution against loosening undue hardship requirements for federal student loans, except in the absence of strong borrower defense of repayment;
- Contend that private student loans warrant less stringent bankruptcy requirements;
- Encourage steps to improve access to existing alternatives to bankruptcy discharge, with emphasis on income-driven repayment.

Please reach out with any additional questions. We look forward to working with the Department on this important issue.

Best regards,

Justin Draeger
NASFAA President

Opening Doors of Educational Opportunity

Evaluating Undue Hardship

NASFAA supports the Department's expressed desire to ensure that the congressional mandate to discharge student loans in bankruptcy only in cases of undue hardship does not inadvertently discourage borrowers in such straits from filing for relief. We are, however, unclear as to what deficiencies in the current procedures may have prompted the Department to request comment. As the Department points out, it has no authority to define undue hardship, and, absent congressional definitions, must rely on case law.

Specifically, the Department requests feedback on:

1. Factors to be considered in evaluating undue hardship claims;
2. Weight to be given to any such factors;
3. Whether the use of two tests results in inequities among borrowers;
4. Circumstances under which loan holders should concede an undue hardship claim by the borrower; and
5. Whether and how the 2015 Dear Colleague Letter should be amended.

NASFAA claims no particular experience or expertise in the resolution of bankruptcy claims, and thus leaves specific input on the efficacy of the current process and adequacy of current guidance to those commenters who do. Nevertheless, we have general observations to put forward, relating to program integrity and reasonable access to alternatives to bankruptcy.

We note that the Department does not distinguish between private and government-backed education loans in its request for comment. We understand that the bankruptcy code encompasses both in the same undue hardship requirement, but we have been troubled by this parallel treatment since it was instituted in 2005. Private education loans are more parallel to other consumer debt than to government-backed education loans, especially in that the latter overlook absence of positive creditworthiness, and offer far more safeguards and options to deal with borrower hardship before resorting to bankruptcy filing.

Regarding federal loans, we believe a stringent test of undue hardship is justified. These loans extend taxpayer dollars to individuals who, in most circumstances, accrue a lifelong benefit in terms of personal advancement and higher earnings potential. The benefits of higher education cannot be repossessed, and borrowers should honor their obligation to repay except in circumstances already defined and accommodated in the loan programs, and truly exceptional situations not otherwise so addressed. The integrity and continued existence of these programs, which are vital to access to higher education, rest on expectations of repayment. To this end, generous repayment terms—including deferment rights, forbearance standards, income-driven repayment plans and discharge or forgiveness provisions—distinguish federal

student loans from private education loans.

Conversely, we have previously noted that the discharge of private student loan debt in bankruptcy is critical to ensuring fairness for American consumers and to provide a way for some struggling private student loan borrowers to establish financial stability. Private student loans are offered *after* a lender has established the creditworthiness of borrowers, and as such, should take on a reasonable amount of risk associated with those underwriting standards. However, much like the federal government, private lenders cannot repossess a postsecondary credential in cases of default, so it may make sense to require some good faith effort at repayment prior to allowing a bankruptcy discharge on private education loans. While the law treats both similarly with regard to undue hardship, ED can establish guidelines that recognize inherent, real differences between private and federal loans. We caution, however, that stringent requirements for bankruptcy discharge are justifiable only if borrowers have reasonable access to other program discharge provisions.

If a borrower's education was of questionable value, a stronger case should be made for federal student loan bankruptcy relief, if the federal government does not implement reasonable borrower defenses against repayment. A balance between bankruptcy relief and borrower defense discharge must be struck: ease of achieving one should be predicated on reasonable access to the other. If a fair system of borrower defenses against repayment is available, taken together with standardized discharges (such as disability and closed schools), deferment for temporary economic hardship, and income-driven repayment plans for longer term economic disadvantage, bankruptcy discharge should be warranted only in limited circumstances.

Regarding the factors used to evaluate undue hardship, which is a highly individual, case-by-case proposition, we recommend that the Department make as much flexibility as possible available. The tests of hardship should accommodate variations in individual circumstances, and the judgment of those responsible for assessing hardship should be supported by a broad range of possible considerations. The current ability to compromise the amount of debt to be repaid to avoid full discharge, and current bankruptcy case law tests that consider how long the debt has been in repayment, evidence of the borrower's desire to repay (as opposed to borrowing with the intent to evade repayment), and personal choices that unnecessarily inhibit repayment, are all important general factors, but other factors may be equally weighty in individual cases, in the judgment of the assessor.

Alternatives to Bankruptcy

We believe that the Department needs to be equally focused on ensuring that federal loan borrowers understand their other options under the provisions of the loan programs; there is

work to be done in this area that the Department must undertake. The Department should ensure that borrowers take reasonable steps to access those options before turning to—or being granted—bankruptcy discharge. Borrowers may believe that discharge or reduction of debt in bankruptcy may "wipe the slate clean," but that failure to honor their debts will follow them for up to 10 years in their credit history, and it can take several of those years to rebuild good credit. In the meantime, they will likely pay a cost in higher interest rates and fees, lower credit limits, exacerbated ill effects of late payments, and the need to use some of their limited assets as security for subsequent credit cards or loans. They will be considered to have an adverse credit history for 5 years for purposes of student or parent PLUS loans.

Concomitant with keeping a high bar for discharge of federal student loans in bankruptcy is the need to simplify current provisions and procedures so that borrowers who are already stressed by their extenuating circumstances can meet repayment requirements prior to acceding bankruptcy discharge. Measures to improve access to alternatives to bankruptcy include the following considerations.

Income-Driven Repayment

Income-driven repayment (IDR) is a powerful tool, both for preventing default and avoiding discharge in bankruptcy. However, it is underutilized and prohibitively confusing and complicated, and it appears that the most at-risk borrowers are least likely to avail themselves of IDR. An Update issued by the Bureau of Consumer Financial Protection (CFPB) in May 2017 found that borrowers who had rehabilitated defaults but who did not enroll in IDR were five times more likely to redefault than those who did, and yet fewer than 2% were enrolled in IDR in their first billing cycle after rehabilitation, and less than 10% had accessed IDR by their ninth billing cycle. By contrast, borrowers who cure default through consolidation are required to use IDR and the consolidation process facilitates that enrollment; the CFPB study suggests that, even though other factors may be in play, these borrowers are significantly more likely to begin and remain in repayment.

We wonder how much the national default rate (at 11.5% for 2017) could be reduced with more effective use of IDR. A 2015 Government Accountability Office (GAO) report said that fewer than 1% of borrowers who entered repayment between 2010 and 2014 and enrolled in one of two income-driven repayment plans defaulted on their loans, compared to 14% of borrowers on standard 10-year repayment plans. Although enrollment in IDR plans has increased to 28% of all borrowers in repayment as of the end of 2017[1], their use still falls

[1] These numbers are based on NASFAA's calculations using data downloaded from the Federal Student Aid Data Center on 5/14/2018

short of their potential for helping borrowers.

While the most effective use of IDR would be before a borrower defaults, accessing IDR on their own may be confusing or intimidating even for borrowers who are not at risk. Current

IDR plans are:

- Revised Pay As You Earn Repayment Plan (REPAYE Plan) for Direct Loans
- Pay As You Earn Repayment Plan (PAYE Plan) for Direct Loans
- Income-Based Repayment Plan (IBR Plan) for Direct and FFELP loans
- Income-Contingent Repayment Plan (ICR Plan) for Direct Loans
- Income-Sensitive Repayment Plan for FFELP loans only (not eligible for PSLF)

These plans differ in eligibility requirements, calculation of repayment amount, covered loans, length of repayment period, amount forgiven at the end of the repayment period, impact of increasing borrower income, and consequences of missing recertification deadlines. Recertification itself remains a stumbling block; a poll conducted by the Department in November 2014 showed that almost 57% of borrowers did not recertify their IDR plans on time. A chart excerpted from Federal Student Aid's publication "Repaying Your Loans" comparing the various IDR plans, other than the FFELP-only income-sensitive plan, is attached to this response.

Every effort should be made to provide one comprehensive income-driven repayment (IDR) plan instead of the proliferation that now exists. As much cooperation as possible between the Departments of Education,Treasury, Social Security, and other federal and state agencies should facilitate enrollment in, documentation for, and recertification of income-driven repayment.

Enrollment in an income-driven repayment plan should be required wherever it can (1) deflect need for discharge in bankruptcy, (2) prevent default, or (3) help borrowers transition out of default. Enrollment in an income-driven plan could be automatic under more circumstances. A number of bills have been introduced to simplify or automate enrollment in income-driven repayment, such as the SIMPLE Act (HR 3554 / S. 1712) and the Dynamic Repayment Act (S. 799). Simplification and enhanced cooperation among government agencies to assist borrowers with income-driven repayment could improve low enrollment rates and avoid more desperate measures, such as filing for bankruptcy.

Borrower Defenses

Borrowers who were harmed by demonstrable and systemic fraudulent practices or substantial misrepresentation should be given maximum consideration for discharge, in as

streamlined, efficient, and timely a process as possible. The Department is still finding its way in the area of borrower defenses, but victimized borrowers should not suffer further harm by a discharge process that is confusing or untimely. We appreciate the need for balancing due process for all parties, but we encourage the Department to employ

approaches, including a group process, that forestall the need to consider bankruptcy a viable option.

Communication with Borrowers

Early monitoring of borrowers having problems with repayment should trigger vigorous outreach activities by the loan holder, motivated by the best interests of the borrower and including understandable, standardized information about income-driven repayment plans. Rather than directing borrowers to forbearance, for example, servicers should explain the benefits of income-driven repayment and assist borrowers in enrolling.

NASFAA commissioned a task force to examine loan servicing issues, identify problems, and recommend improvements. The task force conducted a survey of the NASFAA membership, which garnered responses from over 2,200 aid administrators at more than 1,500 institutions. The task force issued its report in February 2015, which included several recommendations focused on improving communication with borrowers in repayment. One of those recommendations encouraged the Department to permit the use of innovative technologies that would allow servicers to more efficiently and effectively communicate with borrowers, in lieu of certain prescribed requirements. A more flexible, targeted communication framework can be designed to enable servicers to use their data analytics to put time, resources, and efforts into borrowers identified as truly being at-risk of default.

Those cases that result in bankruptcy discharges because they cannot be resolved by existent loan program provisions and that rise to the level of undue hardship beyond the borrower's control should also not result in any penalty or adverse effect to the institution.

NASFAA understands that some improvements might require legislative change, and we would be pleased to work with the Department to identify and advocate for such changes. In the meantime, periodic review of processes such as treatment of bankruptcy petitions is an important way to ensure their effectiveness and relevance to current trends and circumstances. Any changes, however, should be made in the context of program integrity and only after full consideration of all available alternatives. We believe rigorous requirements for bankruptcy discharge of federal student loans is still in the best interests of program integrity, and should be supported by equal attention to improving access to, and use of, existing alternatives.