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April 8, 2013

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Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street NW., Washington, DC 20552
Via: http://www.regulations.gov

RE: Docket No. CFPB-2013-0004

INTRODUCTION

Public Citizen, a national nonprofit consumer advocacy organization with more than 300,000 members and supporters, appreciates the opportunity to offer comments concerning the Consumer Financial Protection Bureau's (Bureau) notice and request for information to determine options that would increase the availability of affordable payment plans for borrowers with existing private student loans. A myriad of obstacles and difficulties exist for student loan borrowers. We commend the Bureau for its effort over the last two years in seeking to catalogue those issues and identify potential solutions.

While there are many challenges facing students in this arena, we are using this comment opportunity to highlight two issues that are critical for student borrowers, particularly when they are at their most vulnerable point in dealing with their loans: the shrinking access to legal remedies to recover for losses caused by predatory lending and other harmful industry practices, and the lack of reasonable repayment options. Allowing borrowers to hold lenders accountable for abuses and providing them with meaningful, long-term repayment relief will make student loans more affordable and, on the whole, make the market work better for consumers.

BACKGROUND

The last year has brought justified attention to the plight of private student loan borrowers and the state of the private student loan market. According to the Bureau's own data, private student loan borrowers have more than $150 billion in debt, and in the last decade, hundreds of thousands of borrowers have defaulted on their loans. Meanwhile, creditors who have benefited from students' ballooning debt are doing little to assist financially distressed borrowers.[1] Public officials have raised concerns about the lack of protections for private borrowers. Even the minimum protections of federal loans—forbearance, deferment and loan forgiveness options—are absent from private loans.

The dangers that impact private student loans affect all Americans, and led Sen. Dick Durbin (D-Ill.) to say last year: "It's not only young people facing this crisis, it is parents, siblings and even grandparents who co-signed private loans long ago and are still making payments decades later."[2]

As Public Citizen discussed in our report on student loans issued in July 2012,[3] private lenders have been accused of a wide range of abuses that have harmed borrowers. They include charging credit-card interest rates, excessive and unreasonable fees and penalties, providing high-cost loans to borrowers despite knowing that those borrowers are likely unable to repay, and misrepresenting the quality of educational programs that their loans finance.

The 2012 Annual Report of the Bureau's Student Loan Ombudsman confirmed that lenders have engaged in predatory lending practices, poor underwriting standards with risky loan terms, and have trapped students in debt with few remedies.[4] The Bureau continues to document borrower complaints with an important new online database, which has provided further evidence of many harmful practices of the private student loan industry. The majority of the currently 4,600-plus complaints relate to problems with repaying loans, such as fees, billing, lack of deferment and forbearance options, fraud, and credit reporting.[5]

The Bureau and the Department of Education have compared the student loan market to the subprime mortgage lending industry practices that led to the 2008 financial crisis and brought financial ruin to millions of homeowners.[6] As Education Secretary Arne Duncan

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[1] *See*, National Consumer Law Center, *Comments to the Consumer Financial Protection Bureau on Request for Information Regarding Private Education Loans and Private Educational Lenders*, 76 Fed. Reg. 71329, Docket CFPB-2011-0037, Jan. 17, 2012, http://bit.ly/YQPxa9.

[2] Press Release, Sen. Dick Durbin (D-Ill.), "As Student Loan Debt Surpasses $1 Trillion, Senators Introduce Legislation to Address Crisis," Jan. 23, 2013, http://1.usa.gov/WxsVYM.

[3] Public Citizen, *Between a Rock and a Hard Place: Courthouse Doors Shut for Aggrieved Private Student Loan Borrowers*, July 2012, http://bit.ly/O5zJMI.

[4] Consumer Financial Protection Bureau, *Annual Report of the CFPB Student Loan Ombudsman*, October 16, 2012, http://1.usa.gov/SYH4dF; *See also*, Mandi Woodruff, He*re's How Private Student Loan Debt Became a $150 Billion Burden*, BUSINESS INSIDER, July 20, 2012, http://read.bi/NNDwy4;

[5] Consumer Financial Protection Bureau, *Consumer Response: A Snapshot of Complaints Received*, March 2013, http://1.usa.gov/WZ9N8Q.

[6] Consumer Financial Protection Bureau and the Department of Education, *Private Student Loans*,

observed: "Subprime-style lending went to college and now students are paying the price."[7]

While there are notable differences between the mortgage and student loan markets, lenders in both markets had misplaced incentives to give loans to consumers they knew or should have known would not be able to afford them. In its Private Student Loan Report, the Bureau detailed the extent to which student loan originations were driven by asset-backed securities (ABS) investors' search for yield.[8] And while the student loan ABS market experienced a contraction following the 2008 financial crisis, investors' appetite for these risky financial products appears to have returned despite borrowers falling behind on their payments.[9] We all experienced the economic damage which resulted from these practices in the mortgage market and must be wary of similar practices in the student loan market.

FORCED ARBITRATION PRESENTS "A SERIOUS FAIRNESS ISSUE."

Another common characteristic of pre-crisis mortgage lending and private student loan terms is the widespread use of mandatory binding (or forced) arbitration clauses, an increasingly prevalent tool used by some lenders to avoid accountability and hide bad practices. Indeed, as far back as 2003, the federal government associated forced arbitration clauses in mortgages and other loan contracts with abusive and predatory lending.[10] Fortunately for residential homeowners, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act barred pre-dispute binding mandatory arbitration clauses outright from residential mortgages and home equity line of credit transactions.[11] The Dodd-Frank Act also granted authority to the Bureau to take similar action and ban arbitration clauses from all other financial services contracts under its jurisdiction, including student loan promissory notes and other lending contracts.

Arbitration clauses are typically inserted in take-it-or-leave-it loan terms with boilerplate language drafted solely by lenders and other financial institutions. Borrowers generally

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Report to the Senate Committee on Banking, Housing, and Urban Affairs, the Senate Committee on Health, Education, Labor, and Pensions, the House Committees on Financial Services, and Education and the Workforce, at 18, Aug. 29, 2012, http://1.usa.gov/NVvBcz.

[7] Carter Dougherty & Janet Lorin, *CFPB Says Students Victimized by 'Subprime-Style' Lending,* BLOOMBERG, July 20, 2012, http://bloom.bg/NOl1JJ.

[8] Consumer Financial Protection Bureau and the Department of Education, *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 Committees on Financial Services, and Education and the Workforce, at 21, Aug. 29, 2012, http://1.usa.gov/NVvBcz.

[9] *See* Ruth Simon et al., *Student-Loan Securities Stay Hot*, THE WALL STREET JOURNAL, March 3, 2013, http://on.wsj.com/WD1nWZ.

[10] Office of the Comptroller of the Currency, Administrator of National Banks, *Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices*, OCC Advisory Letter, AL 2003-2, Feb. 21, 2003, http://1.usa.gov/12boMkb.

[11] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-2013 § 1414(e) (codified at 15 U.S.C § 1639c).

have no opportunity or ability to negotiate the terms. Arbitration clauses block borrowers with valid claims from seeking redress in court for alleged wrongs. In the event of a dispute, a borrower's claims must be heard in a private proceeding, which is often accompanied by unpredictable costs and fees. The arbitration provider, designated by the lender, then decides the outcome of the dispute, which can rarely be appealed.

The growing lack of access to court leaves private student loan borrowers vulnerable to numerous practices and acts that violate state and federal laws, such as:

- The Truth in Lending Act (TILA), by advertising false and misleading loan terms and failing to make required disclosures in appropriate ways;
- The Equal Credit Opportunity Act (ECOA), by discriminating against borrowers based on certain protected characteristics, including race, color, religion, national origin, sex, marital status, age, and disability;
- The Fair Debt Collection Practices Act (FDCPA), by harassing borrowers in seeking payment;
- The Telephone Consumer Protection Act (TCPA), by placing harassing calls to borrowers' through auto-dialer systems, without borrowers' consent;
- The Servicemembers Civil Relief Act (SCRA), by impeding the ability of borrowers on active duty to access the SCRA interest rate cap.

In our student loan report, we highlighted the ongoing cases of two private student loan borrowers who had initiated court actions against their lenders and other financial institutions seeking redress for alleged wrongdoing.[12] In both cases, the borrowers sought to represent themselves and other similarly situated borrowers in class actions. And in both cases, the promissory note terms contained an arbitration clause and also prohibited borrowers from banding together in collective actions against the lenders. The cases of the former students, Joshua Fensterstock and Justin Kuehn, have since resulted in unsurprising but disappointing outcomes, as they were unable to get their claims heard in court and were forced to either present their claims in individual arbitration or not at all.

Fensterstock had alleged that the financing company and lender on his private loans were applying an improper method to determine how much of a loan payment to apply to the loan principal, rather than to interest, and that the method amounted to a hidden penalty. He asserted claims under California law, including breach of contract, fraud, unfair business practices, and false and deceptive advertising practices.[13] The lenders, citing the loan terms, sought to force Fensterstock into arbitration on an individual basis. A New York district

[12] Public Citizen, *Between a Rock and a Hard Place: Courthouse Doors Shut for Aggrieved Private Student Loan Borrowers*, at 10, 13-14, http://bit.ly/O5zJMI.
[13] *Fensterstock v. Educ. Fin. Partners*, 611 F.3d 124 (2d Cir. 2010) cert. granted, judgment vacated sub nom. *Affiliated Computer Services, Inc. v. Fensterstock*, 131 S. Ct. 2989, 180 L. Ed. 2d 818 (U.S. 2011).

court and the Second Circuit Court of Appeals had agreed with Fensterstock that the arbitration clause was unconscionable and therefore unenforceable under California law.[14] However, the dispute over Fensterstock's arbitration clause reached the U.S. Supreme Court.

The Supreme Court had just issued *AT&T Mobility v. Concepcion*,[15] a far-reaching opinion that continues the Court's expansive interpretation of the Federal Arbitration Act (FAA). The Court held that the FAA preempted state laws that sought to preserve the class action tool for consumers where an arbitration clause was present. The *Concepcion* decision in effect permitted corporations to insert class action bans within forced arbitration clauses in their one-sided adhesion contracts with consumers and employees. In light of *Concepcion*, the Supreme Court vacated the Second Circuit's decision and remanded it to the appellate court for further consideration,[16] which in turn remanded the case to the trial court.[17] Ultimately, Fensterstock was required to resolve his claim against his lenders in individual arbitration.[18]

Justin Kuehn had alleged that the financial institutions that held his consolidated private loans had deceived him and other borrowers into believing that a monthly payment reduction was a result of an interest rate reduction when in fact it was attributable to a reduction in the amount of principal being repaid each month. According to his complaint, the alleged practice resulted in prolonged loan payment terms and additional interest paid by borrowers.

Kuehn argued that the arbitration clause in the promissory note was unconscionable, or unfair on its face, and should not be enforced. However, the arbitration clause dictated that the arbitrator—and not a court—must decide on any questions about the fairness of the arbitration clause. Consequently, the arbitration provider picked by the lender would get to decide the fairness of the arbitration terms in Kuehn's promissory note.

"The fact that an arbitrator gets to decide whether the arbitration clause is enforceable gives him or her the power to decide on an issue that benefits the arbitrator financially," Kuehn said. "With companies' widespread use of forced arbitration in contracts, our only option as consumers is to challenge the validity of the arbitration clause itself in court. But that option is also gone."[19]

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[14] *Id*.
[15] *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 179 L. Ed. 2d 742 (2011).
[16] *Affiliated Computer Services, Inc. v. Fensterstock*, 131 S.Ct. 2989 (Mem) (2011).
[17] *Fensterstock v. Educ. Fin. Partners*, 426 Fed.Appx. 14 (2011).
[18] *Fensterstock v. Educ. Fin. Partners*, 2012 WL 3930647 (S.D.N.Y. Aug. 30, 2012).
[19] CitizenVox, *Student Loans and Forced Arbitration*, Dec. 10, 2012, http://bit.ly/TR06Hv.

The impact of forced arbitration clauses in lending contracts is also felt by students who take out loans to attend for-profit institutions. The Bureau's own analysis found that students at for-profit schools add private student loans to their "debt mix at roughly twice the rate of students in comparable non-profit programs."[20] We applaud the Bureau for investigating certain for-profit schools to determine whether they are "engaging in unlawful acts or practices relating to the advertising, marketing, or origination of private student loans."[21] A number of legal actions have been initiated by students against for-profit schools, alleging misrepresentations and other fraud that induced them to take out significant student loans for their courses. However, many attempts to get students' claims heard in court have been blocked by forced arbitration.[22]

Recently a federal court in Tennessee enforced the arbitration clause against students seeking redress against a for-profit school, but the court also noted that "a serious fairness issue"[23] existed for consumers and opined that change was needed. The court was concerned that the students in the lawsuit "will not be able to afford the out-of-pocket costs to arbitrate, even under conservative cost assumptions." The court observed that their right to recovery under the state law was "essentially extinguished," and that ultimately the decision, while made pursuant to the law, was "manifestly unjust and, perhaps, deserving of legislative attention."[24]

We agree with the court's assessment. Forced arbitration clauses are being used both as a sword to slash the rights of student loan borrowers and other consumers, and a shield for corporations to evade accountability for misconduct. Fortunately, Congress has already given the issue attention for the benefit of financial services consumers. It is now up to the Bureau to take the necessary corrective action and require the elimination of arbitration clauses from these contracts.

DISTRESSED BORROWERS NEED MEANINGFUL, LONG-TERM REPAYMENT RELIEF.

Since the mortgage crisis, the federal government has initiated various loan modification programs for troubled homeowners to avoid foreclosure. While those programs have proven far less effective at providing homeowners sufficient relief to facilitate timely and

[20] Consumer Financial Protection Bureau and the Department of Education, *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 Committees on Financial Services, and Education and the Workforce, at 33, Aug. 29, 2012, http://1.usa.gov/NVvBcz.

[21] *See, e.g.* Corinthian Colleges, Inc. Form 10-Q, Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, For the Quarterly Period Ended March 31, 2012, at 18, http://bit.ly/QcusU4.

[22] *See, e.g.*, *Anderson v. Virginia Coll., LLC*, 2012 WL 4052198 (S.D. Miss. Sept. 13, 2012); *Daymar Colleges Group, LLC v. Dixon*, 2012 WL 4335393 (Ky. Ct. App. Sept. 21, 2012)

[23] *Dean v. Draughons Junior College, Inc.*, 2013 WL 173249, at 12 (M.D. Tenn. Jan. 16, 2013).

[24] *Id*.

reasonable repayment on their mortgage loans, the government's actions are, nonetheless, a step in the right direction.

A similar issue in the private student loan market warrants the Bureau's attention. Private student lenders are largely unwilling to provide borrowers with meaningful, long-term repayment relief when they get into trouble repaying their debts. Unlike federal student loans, private student lenders are not required to—and, by and large, do not—offer flexible repayment options. If anything, private lenders usually offer short-term interest-only or forbearance options, which fall short of remedying borrowers' repayment distress. As a result, private student borrowers are more likely to default on their loans. And when private student loan borrowers default, private student loan creditors do not provide rehabilitation programs that would allow borrowers to get out of default and back into repayment.[25]

Members of Congress have expressed grave concerns about the lack of flexible repayment options for private student loan borrowers. Last month, Senators Jack Reed (D-R.I.), Durbin, Tom Harkin (D-Iowa), Al Franken (D-Minn.), Elizabeth Warren (D-Mass.), and Sherrod Brown (D-Ohio), signed a letter, calling on thirteen major banks to work with regulators and student borrowers to reduce the number of students in default on their private student loans. Reed stressed the importance of such an endeavor, saying, "We need the public and private sector to work together to prevent a calamity for middle-class students."[26]

The Student Loan Ombudsman report also confirmed the lack of meaningful, long-term repayment relief for borrowers. According to one of the report's major findings, distressed borrowers who make good-faith attempts to service their debts or renegotiate the terms of their loans, are often rebuffed by their lenders. As an unfortunate consequence, those borrowers are trapped in loans that they cannot afford and suffer the resulting damage when they inevitably do not make their payments.[27]

The dearth of repayment options is compounded by the nearly impossible hurdles of discharging private student loans in bankruptcy. Because creditors can squeeze out small amounts of money from private student loan borrowers for the rest of their lives, creditors conceivably can profit even if the loans are never repaid fully. As an unfortunate consequence, private student loan creditors have no financial incentive to modify loan terms, and borrowers are held in debt peonage indefinitely, making it even more difficult to

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[25] *See*, National Consumer Law Center, *Comments to the Bureau on Request for Information Regarding Private Education Loans and Private Educational Lenders*.
[26] Press Release, Sen. Jack Reed (D-R.I.), "Senators Call on Banks to Work With Regulators and Students Who Are Trying to Pay Back Loans," (March 1, 2013), http://1.usa.gov/YuadoQ.
[27] Press Release, Consumer Financial Protection Bureau, "Consumer Financial Protection Bureau Finds Private Student Loan Borrowers Face Roadblocks to Repayment," Oct. 16, 2012, http://1.usa.gov/PEvHgf.

buy a home, save for retirement, or start a business. Such a dynamic reinforces the private student loan market's drag on our economy.

Because it is not in industry's short-term interest to repair this short-sighted, pernicious business model, the Bureau must step in where appropriate to ensure that creditors' loss mitigation practices and borrowers' repayment options are reformed. Doing so is imperative because, while industry may profit in the short-term, a precipitous—and not entirely unpredictable—increase in defaults and charge-offs could create safety and soundness issues for market participants, which could in turn proliferate threats to financial and economy stability.

Sincerely,

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