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Testimony for the Senate Judiciary Committee/Subcommittee on Administrative Oversight and the Courts

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"The Looming Student Debt Crisis: Providing Fairness for Struggling Students"

Senator Durbin, Ranking Member Sessions, thank you for inviting me to testify before this subcommittee today. I appreciate your attention to this issue.

As Attorney General of the Commonwealth of Kentucky, the issue of students being unable to discharge private educational loans in bankruptcy is linked to my investigation into for-profit career colleges.

I first became aware of the tremendous debt burden carried by students at some proprietary colleges through the investigation into possible consumer protection violations by Decker College and subsequently my investigation into the closing of the for-profit American Justice School of Law in Paducah.

Eventually, Decker College closed and was forced into bankruptcy in 2005 following a loss of accreditation and its eligibility to receive Title IV funds. The students were left in a terrible situation. They had incurred thousands of dollars

in debt to pay for certifications as heating and air conditioning technicians, electricians, and plumbers. This was an education promised to secure them a higher paying job, but the school closed before the training was complete. And, to add insult to injury, the credits they had earned and paid for did not transfer to another school.

The American Justice School of Law and its successor, Barkley School of Law, failed to obtain accreditation from the American Bar Association, closed and also filed for bankruptcy. Most students had not completed their education when the school closed.

As you are aware, students with federal student loans who are unable to complete their degree because a school closes are entitled to have those federal loans discharged. However, the same protection is not available for private institutional loans or loans from other private lenders. Both Decker and Barkley students had millions of dollars in these institutional and private student loans that were not dischargeable in bankruptcy under the closed school discharge rule.

The Trustees in the Decker and Barkley bankruptcies began efforts to collect on the private loans the schools had extended to students. But, ironically, the students who were living on

the financial edge, saddled with tens of thousands of dollars in student loans, likely would not be able to discharge their student loans in personal bankruptcy.

In both instances, my office was able to successfully work with the Trustees to discharge loans owed directly to the schools. In the case of Decker College, the settlement negotiated by my office released the loans of 2,200 students that totaled $4.5 million dollars. Likewise, in the Barkley bankruptcy, after being contacted by my office, the Trustee released the student debts to the school.

With respect to other students at the law school, we were also able to secure a settlement with the private lender. We found that the school had a questionable relationship with a company called SLX. Further, notwithstanding the representations to students, these private loans didn't include the same consumer protections as federal student loans. Those protections include the ability to defer payment on the debt while still in school. We found evidence that the loan holder began requiring some students to repay their loans while they were still in school. Deferment for the entire time needed to complete a degree wasn't available under the terms of the loan.

So, students were forced into forbearance and into accruing significant amounts of capitalized interest.

My office was able to secure $3.6 million in debt reduction in the loan obligations for students who attended the law school. Students' loans were reduced by an amount equal to the amount of tuition paid for credits that did not transfer to another law school. The average loan reduction per student was $25,000.

We received calls, emails and letters from students thanking my office for its work. The reduction in these loans changed their lives. They were able to make a fresh start.

But, students at these schools had loans with other lenders. Decker College closed its doors in 2005, and my office still receives calls every week from students struggling to pay their school loans. One former student called because his tax refund had been taken to pay a student loan, but he needed this money to make a car repair. Another student needed the money to move her family into a safe apartment. Do we understand — really understand — how close to the line some of these borrowers are living? That working car means the difference between being able to get to work and keeping a job or losing

that job. That apartment means safety and security for a family.

Indeed, there are material differences between private loans and federal loans. The federal loans have important provisions protecting students. For example, as I mentioned earlier, the "closed school" discharge rule provides relief for students faced with a circumstance like Decker College. Some Decker students were able to get a "closed school discharge" for their federal loans. That remedy was not available for the students' private or institutional loans. Federal loans have other protections for borrowers too, including a fixed interest rate that is capped, an income based repayment plan, and the ability to defer repayment. Private lenders, on the other hand, are not required to offer any of these protections to borrowers.

After studying the cases of Decker College and the law school, in December 2010, I launched an investigation into seven other for-profit colleges operating in Kentucky. The students enrolled in most of these career schools are some of our most financially vulnerable citizens – they are Pell Grant recipients, they rely heavily on student loans to pay for their educations, and very often they are the first in their families to attend a college of any sort. According to most recent data

available from the Project on Student Debt, an estimated 96% of graduates from four-year proprietary schools have loans. Of great concern is that 42% of these students have private loans--without the protections of federal loans-- in contrast to the 14% of students at public four-year institutions and just 4% at public two-year institutions who have private loans.

An even more troubling statistic from the Senate HELP Committee is that while students at the for-profit schools are only 10% of the higher education body, they account for 47% of all defaults on federal loans. For the 2009-2010 year, according to the Institute for College Access & Success, students at these career colleges received approximately 25% of all Title IV Aid. Unfortunately, no comprehensive data on private loan defaults is available.

These schools receive a large portion of the funds intended for our veterans as well. A recent article in the Army Times reports that for-profit schools have received approximately 37% of the $17.2 billion cost for the GI Bill, and "almost 50% of the $563 million spent last year by the Defense Department on tuition assistance for active-duty troops went to for-profit schools."

My office has received hundreds of complaints since we commenced our investigation in 2010 ranging in topics from misrepresentations about financial aid, non-transferability of credits, and inability to get a job. Many of these students who took a chance on education are stuck with thousands of dollars in debt and no way to repay that debt.

In 2011, I filed suit against two colleges alleging they made false and misleading statements to consumers on matters including the rate of job placement, transferability of credits, and the students' financial aid. We are continuing our investigation into other schools.

I am now chairing a multistate working group looking into this issue with 23 other state attorneys general. In addition to the two suits my office has filed, Attorney General Madigan's Office has filed suit against Westwood College, the Colorado Attorney General has just reached a $4.5 million consumer protection settlement with Westwood College and other Attorneys General have active investigations.

The great tragedy is that students at some of these career schools, like Decker College, obtain these loans to go to school and change their lives--to get a higher paying job and improve their standard of living. Unfortunately, for many of these

borrowers, they are unable to complete their education or the school closes and they are left with no job and a mountain of debt that bankruptcy experts tell us is almost impossible to discharge.

The more we learn about the private student loan market, the more concerns we have. We have seen borrowers manipulated both by lenders and unscrupulous institutions that are in a fiduciary relationship with these borrowers.

Because of this dynamic, I must ask, why should we provide these students with no less than the same consumer protections that are available to federal student loan borrowers? Instead, current law provides private borrowers with none of the protections we've mentioned, and according to many experts, the law has made it almost impossible to get out of debt and get beyond the financial hardship that these private loans have caused.

With such harsh consequences for failure, these students are trapped in a cycle of dodging bill collectors, wage garnishment, and no meaningful path to financial recovery. This must not be the legacy of our efforts to provide an opportunity for education.