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AUTHOR Blanchette, Cornelia M.

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ABSTRACT

This report examines the effectiveness of recent federal government efforts through amendments to the Higher Education Act (1993) to reduce student loan defaults. Key measures to curb defaults had been to make schools with high student loan default rates ineligible for federal student loan programs. However, many institutions have challenged Department of Education ineligibility decisions arguing that such decisions were based on inaccurate data. Recent amendments have attempted to address these concerns by changing Department processes. In evaluating the effectiveness of these changes a study evaluated Department information on schools filing administrative appeals and court documents. The study found that, as of September 30, 1994, 250 schools had administrative appeals pending with the Department challenging the accuracy of their default rates. In the appeals the main issues under contention were that the Department had used erroneous data in the default rate calculation or that the Department had failed to follow the law by including defaulted loans that had not been properly serviced by lenders in the default rate calculations. Overall the study found that 1993 amendments have not eliminated abuses in the student loan program. Possible ways to address this concern include: (1) holding schools liable for the costs associated with defaults on loans that their students receive during the appeal process; and (2) making schools post a performance bond as a condition of filing an appeal. Appendixes contain scope and methodology and Federal Family Education Loan Program eligibility status of schools with default rates over the statutory thresholds (fiscal years 1991-94). (JB)

GAO

Report to the Ranking Minority Member,
Subcommittee on Human Resources and
Intergovernmental Relations, Committee
on Government Reform and Oversight,
House of Representatives

June 1995

ED 385 184

STUDENT LOAN DEFAULTS

Department of
Education Limitations
in Sanctioning Problem
Schools



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GAO/HEHS-95-99

Health, Education, and
Human Services Division

B-255079

June 19, 1995

The Honorable Edolphus Towns
Ranking Minority Member
Subcommittee on Human Resources
and Intergovernmental Relations
Committee on Government Reform
and Oversight
House of Representatives

Dear Mr. Towns:

Some schools, particularly proprietary for-profit trade schools whose profits come from student tuition payments, have enrolled students whose tuition is heavily financed by federally guaranteed student loans. Some of these schools are not overly concerned about their students completing an educational program or the frequency of their students defaulting on student loans. Although annual federal costs for defaulted student loans have begun to decline from their high of \$3.6 billion in 1991, in 1994 the federal government paid out \$2.4 billion to make good its guarantee on these defaulted loans.

In 1991, the Department of Education, under its Default Reduction Initiative, which implemented the Student Loan Default Prevention Initiative Act of 1990 (P.L. 101-508), began to bar postsecondary schools from federally guaranteed student loan programs if their students had exceptionally high loan default rates. Congressional hearings in 1990 had shown that some for-profit trade schools with high loan default rates received substantial proceeds from such loans while providing students with little or no education in return. Under this new initiative, the Department could stop a school from participating in federal loan programs if the school's default rate exceeded statutory thresholds in 3 consecutive fiscal years—in general, about a 25-percent default rate. However, once the initiative was under way, many schools complained that the Department was not using accurate information in setting default rates. A number of schools filed administrative appeals or took court action to block the Department's denial of their participation in federal loan programs.

You asked us to determine whether sufficient steps were being taken to resolve these issues. These steps included the Department's implementation of certain amendments to the Higher Education Act,

enacted in 1993, that were designed to address the schools' concerns. As agreed with your office, we focused our work on the following questions:

- How many schools have contested the Department's decisions, and what are the main points of their contention?
- To what extent are the schools' concerns addressed by the 1993 amendments and the Department's efforts to implement them?
- What more, if anything, may need to be done to resolve problems with the default reduction initiative?

We examined Department information on defaulted student loans to determine the extent to which schools were filing administrative appeals challenging the accuracy of the Department's default rate data. We also examined documents filed in the courts by the schools and the Department to determine the nature and outcomes of the lawsuits that the schools have filed against the Department over default rate issues.

Results in Brief

As of September 30, 1994, 250 schools had administrative appeals pending with the Department challenging the accuracy of their default rates. The 250 schools constituted about one-third of all schools identified by the Department as being above the statutory default thresholds in fiscal years 1991 to 1994. In addition, 111 schools and their trade associations filed 22 lawsuits over default rate issues. In the appeals and lawsuits, the main issues under contention were that the Department (1) used erroneous data in the default rate calculations or (2) failed to follow the law by including defaulted loans that had not been properly serviced by lenders in the default rate calculations.

In our view, the 1993 amendments will not eliminate challenges to the Department's default rate determination, but should reduce the likelihood of such challenges. The amendments require that schools be given an opportunity to verify the accuracy of loan data and examine loan servicing records. This access to information should help resolve misunderstandings on matters of fact and allow a clearer focus in those areas in which disagreements remain. Regulations issued in November 1994 to implement these amendments should make adjudication of appeals more straightforward and less time-consuming.

These recent changes, while addressing schools' concerns, did not contain measures to fully protect the government's interest in such disputes. Current policies and practices leave open the possibility that unscrupulous

schools can saddle the government with additional loan default costs by continuing their same pattern of operation during the appeals process. Possible ways to address this concern include (1) holding a school liable for costs associated with defaults on loans made to its students during the appeals process and (2) requiring that a school post a performance bond as a condition of filing an appeal. The first alternative was used in an earlier federal student loan program; the second alternative has been ordered by a court in one of the lawsuits against the Department.

Background

In 1990, the Senate Permanent Subcommittee on Investigations conducted a series of hearings on fraud and abuse in the Federal Family Education Loan Program (FFELP).¹ Evidence provided to the Subcommittee showed that operators of some for-profit trade schools made substantial amounts of money by taking payments from students in the form of federally guaranteed student loans while providing little or no education in return. Faced with large debts and no marketable training, these students often defaulted on their loans. Based on this and other evidence, the Subcommittee concluded that high default rates were both a warning sign of potential abuse and a common thread of actual abuse in problem schools.

In response to this information and to loan defaults that increased from \$1.4 billion in fiscal year 1988 to over \$2.6 billion in fiscal year 1990, the Congress enacted the Student Loan Default Prevention Initiative Act of 1990. This legislation, together with the Department's Default Reduction Initiative, established a process for discontinuing participation in FFELP for postsecondary institutions with default rates over certain statutory thresholds.

Under this process, the Department annually computes a default rate (known as the cohort default rate) for all participating schools. In general, the default rate is the percentage of a school's borrowers who enter repayment in one fiscal year and default by the end of the next fiscal year. For example, if 100 former students from a school were scheduled to begin repaying their loans in fiscal year 1990 and 25 defaulted on their loans by the end of fiscal year 1991, the school's fiscal year 1990 default rate would be 25 percent.

¹FFELP comprises several types of federally guaranteed student loans: Stafford loans, Parent Loans for Undergraduate Students, and consolidated loans. These loans are made by private lenders, but the federal government—through a network of guaranty agencies—repays the loan in the event of a default.

To compute default rates, the Department uses data submitted annually on computer tapes by guaranty agencies that administer FFELP at the state level. This database, commonly called the tape dump, contains information showing the status of the program at the end of each federal fiscal year (September 30). Guaranty agencies, which use information provided by lenders, schools, and borrowers, are required to certify that the annual data tapes are complete and accurate. The Department checks the data tapes for missing or erroneous entries and returns tapes to the agencies for correction if it finds what it considers to be a significant number of errors.

To remain eligible for participation in FFELP, schools must have default rates that are lower than the statutory thresholds, which vary depending on the fiscal year or years covered. For example, if a school's annual default rate was 25 percent or greater in fiscal years 1990, 1991, and 1992, it was subject to the loss of its eligibility in FFELP beginning in fiscal year 1994.² According to federal requirements, schools with default rates over statutory thresholds can file an appeal with the Department (or seek relief through litigation) if they believe that

- their default rates were calculated using erroneous data,
- their default rates were calculated using loans that fell into default as a result of improper loan servicing or collection procedures, or
- exceptional mitigating circumstances exist.³

Department's Default Rates Have Been Challenged

During fiscal years 1991 to 1994, 890 schools became subject to the loss of FFELP eligibility because their default rates were over the statutory thresholds for at least 3 successive years. As of September 30, 1994, 601 of these schools were no longer eligible for FFELP participation. However, another 250 schools had appealed the Department's calculation of their default rates and their appeals were still pending. Appendix II provides

²Schools with a single year default rate of 40 percent or higher (for fiscal year 1992 or later) are also subject to limitation, suspension, or termination actions that can result in the schools' loss of eligibility for all federal student aid programs authorized under title IV of the Higher Education Act of 1965, as amended.

³A school is considered to have exceptional mitigating circumstances if it can demonstrate that (1) either 15 percent or fewer of its at least half-time students received Stafford or Supplemental Loans for Students (SLS) in a recent 24-month period or two-thirds or more of its at least half-time students in a recent 24-month period were economically disadvantaged; and (2) two-thirds of its full-time students complete their course of study and two-thirds or more of its graduating students find jobs or were transferred to higher levels of education for which the school's program provided substantial preparation.

more details on the results of the Department's Default Reduction Initiative.

In addition to filing administrative appeals, some schools and their trade associations have filed suit over the default rate issue. In total, 22 lawsuits have been filed, with 111 schools as parties to one or more of them. As of September 30, 1994, 10 of the lawsuits (involving 17 of the schools) had been either dismissed by the courts or had been terminated by agreements between the schools and the Department. The 12 other cases were pending, and the 94 schools involved were continuing to participate in the program.⁴

The appeals and lawsuits have centered on two allegations: that the Department used erroneous data in its computations and that it failed to follow the law's requirement to exclude improperly serviced loans when making its calculations. The schools filing lawsuits have also alleged that the loan servicing problems were aggravated by the schools' lack of access to information.

Data Accuracy Issues

The accuracy of the Department's data has been an issue raised in at least 236 of the schools' administrative appeals and 17 of the 22 lawsuits. In general, the schools' concerns have been based in part on well-documented inaccuracies in the Department's loan database. For example, after releasing school default rates for fiscal year 1988, the Department learned that guaranty agencies for California, Florida, and Washington had reported erroneous date-entered-repayment dates to the Department.⁵ This mistake contributed to the Department's having to recompute rates for about 5,000 schools. Similar mistakes were subsequently found in the data of three other guaranty agencies, leading to recomputations of default rates for affected schools for fiscal years 1989 to 1991.

Problems were also discovered in Department reviews of guaranty agencies' data tapes for the period from March 1992 to January 1993. These reviews were undertaken to address problems like those described above, and they disclosed inaccuracies in data supplied by several guaranty agencies for such matters as the date-entered-repayment, student

⁴One of these cases also involved an association representing proprietary schools. This lawsuit was subsequently withdrawn.

⁵The date-entered-repayment data element is significant because that date determines the year that a borrower's loan is included in the default rate calculation.

enrollment status, and defaulted loan amount. The Department found that inaccuracies occurred in part because guaranty agencies were estimating certain data elements instead of using the most current information received from lenders or schools.

We have reported before on problems with the accuracy of the Department's student loan data. For example, in 1990 we reported that the loan database often contained information that was suspect or incomplete.⁶ In an audit of the internal controls of FFELP, we reported that none of the 10 guaranty agencies included in our review routinely researched and corrected erroneous data before submitting data tapes to the Department.⁷ Most recently, in a joint financial audit conducted with the Department's Office of Inspector General (OIG), we found that some of the tape data were clearly wrong; for example, data showing that borrowers defaulted before the date that a loan was made.⁸

Loan Servicing Issues

Disagreements About What Constitutes Improper Servicing

Servicing of loans has been the more contentious issue. Section 435(m)(1)(B) of the Higher Education Act requires the Department to "... exclude any loans which, due to improper servicing or collection, would result in an inaccurate or incomplete calculation of the cohort default rate"⁹ (emphasis added). In nearly all the lawsuits filed against the Department, schools contended that the Department failed to exclude many improperly serviced loans as required by this provision and thus erroneously inflated the school's default rate. Most schools (198 of the 270 with appeals pending as of September 30, 1994) have also based their appeals on the grounds that the Department did not exclude loans that were improperly serviced by lenders.

Part of the controversy has involved the definition of what constitutes improperly serviced loans. The schools have generally contended that an improperly serviced loan is one in which lenders or loan servicing agencies have violated the Department's procedures for servicing and collecting loans (referred to as due diligence procedures) as specified in

⁶Stafford Student Loans: Millions of Dollars in Loans Awarded to Ineligible Borrowers (GAO/IMTEC-91-7, Dec. 12, 1990).

⁷Financial Audit: Guaranteed Student Loan Program's Internal Controls and Structure Need Improvement (GAO/AFMD-93-20, Mar. 16, 1993).

⁸Financial Audit: Federal Family Education Loan Program's Financial Statements for Fiscal Years 1993 and 1992 (GAO/AIMD-94-131, ACN 17-30302, June 30, 1994).

⁹This section of the law was subsequently amended by the Higher Education Technical Amendments of 1993 and is discussed on pages 8-9.

federal regulations (34 C.F.R. 682.411).¹⁰ An example of these procedures is the requirement that a lender must send at least one written notice or collection letter to a borrower during the first 10 days of a delinquency. If this effort fails, the lender must initiate a series of at least four telephone calls and send at least four additional collection letters in an attempt to bring the borrower back into repayment status. Most of the lawsuits contended that many loans were improperly serviced under these procedures, in that lenders made insufficient attempts to telephone borrowers or failed to use the proper series of letters.

To support their position, schools have provided a number of examples of studies conducted by their own consultants, the Department's OIG, and others that have alleged significant deficiencies in loan servicing. For example, a consultant hired by some of the schools examined approximately 7,000 loans from six guaranty agencies and alleged that loan servicing errors (such as improper telephone contact) occurred at rates ranging from 87 percent for one guaranty agency to 42 percent for another agency.

In rebuttal, the Department has contended that its improper loan servicing determinations are based on additional factors beyond violations of due diligence procedures. It said that certain modest violations of due diligence procedures are not significant for claims payment purposes and loans with these types of violations should not be construed to be improperly serviced for purposes of determining a school's default rate. Also, for a defaulted loan to be excluded from its calculations, the Department believes that a clear cause-and-effect relationship must exist between improper servicing and a loan's default—a relationship it maintains the schools have failed to show.

In one court ruling on this matter, an appellate court concluded that the law requires a link between the violation and the default. The judge said that because the statute did not provide any guidance on the extent to which schools must demonstrate the causal link between the violation and the default, the court would defer to any reasonable interpretation of the statute by the Secretary of Education.

Schools' Access to Loan Servicing Records

In about one-half of the lawsuits, the schools contended that the lack of access to loan servicing records limited their ability to identify possible loan servicing problems. They noted that guaranty agencies were required

¹⁰The regulations require that lenders follow the due diligence procedures for default claims to be paid; failure to follow the procedures may be cause for default claims to be rejected.

to provide loan servicing records for only those loans that the schools believed had loan servicing deficiencies. The Department took the position that granting schools wider access to hundreds or thousands of guaranty agency loan records would be administratively infeasible and that the statutory deadlines for the appeals process were not set up to allow schools to conduct "fishing expeditions" through the voluminous records of the guaranty agencies.

1993 Amendments and Implementing Regulations Should Make Conflict Resolution Less Contentious

Access to Default Rate Information

The Higher Education Technical Amendments of 1993 contained provisions that, among other things, address schools' concerns about access to default rate and loan servicing data. Also, the implementing regulations, which were issued in November 1994, appear to make the adjudication of appeals more straightforward and less time-consuming.

Regarding the accuracy of data used in computing default rates, the amendments established a requirement that schools be allowed a reasonable opportunity to verify the accuracy of data before the Department uses them to compute default rates. The new requirements are effective for default rates issued in fiscal year 1995. Also, for use in computing fiscal year 1995 default rates, Department officials said that they intend to begin using data collected through the Department's National Student Loan Data System.¹¹ The Department plans to update the data in this system on a monthly basis, which should provide more current information for computing default rates.

Access to Loan Servicing Information

The amendments contain a provision requiring guaranty agencies to provide loan servicing records to those schools filing appeals based on improper loan servicing. More specifically, the provision allows schools with default rates above 20 percent for the most recent year for which data are available to have access to a representative sample of the loan servicing and collection records. If a school provides evidence to support its claim that improper loan servicing resulted in an incorrect or incomplete calculation of the default rate, the Department is to reduce the

¹¹This system is designed to be a national database of information on individual student loans that can be used to prescreen students' aid applications and to support a variety of research and program management functions, such as computing school default rates.

school's default rate by the percentage of defaults caused by improperly serviced loans found in the sample.

Department's Implementing Regulations

In April and November 1994, the Department issued regulations for implementing the default rate provisions of the 1993 amendments. The regulations specify that, before annually computing and issuing final default rates, the Department will provide draft default data to all schools with rates equal to or in excess of 20 percent. The Department will also provide draft default data to schools with rates lower than 20 percent upon request.

The schools must notify the guaranty agencies within 30 calendar days of any information that they believe is incorrect. The guaranty agencies, in turn, must respond to any such challenges within 30 calendar days. The final default rates will reflect any adjustments made as a result of this process. If a school continues to disagree, it can file an appeal with the Department after the final rates have been computed and made public.

The final regulations also establish procedures for appeals based on allegations of improper loan servicing and define which loans the Department considers to be improperly serviced for the purposes of the default rate calculations. The Department will exclude loans from the default rate calculation based on improper loan servicing if the school can prove that after the borrower did not make a payment on the loan the lender failed to perform one or more of the following loan servicing and collection procedures (if such procedures were required for that loan):

- send at least one letter (other than the final demand letter) urging the borrower or endorser to make payments on the loan,
- attempt at least one telephone call to the borrower or endorser,
- submit a request for preclaims assistance to the guaranty agency,¹²
- send a final demand letter to the borrower, and
- submit a certification (or other evidence) that skip-tracing¹³ procedures were performed.

¹²Regulations require guaranty agencies to provide collection assistance to lenders, such as sending letters to borrowers, if requested by the lenders.

¹³Skip-tracing is a term to describe the procedures used to locate a borrower that the lender has lost contact with. Such procedures may include checking telephone directories, motor vehicle registration or driver's license records, or seeking assistance from the Internal Revenue Service.

These regulations will be effective July 1, 1995. However, the Department will apply the new procedures to schools that had appeals pending at the time the regulations were issued. Also, the Department will allow schools that previously filed loan servicing appeals but did not have access to at least a representative sample of the relevant loan servicing records to refile their appeals under the new procedures.

Government's Interests Are Not Fully Protected

The recent legislative changes should help address the concerns of schools that believe they have become inadvertent victims in the Department's attempt to minimize abuses in the student loan program. However, neither the 1993 amendments nor the Department's implementing regulations contain measures for protecting the government's interest against operators who may take advantage of these additional due process provisions by using them to continue unscrupulous operations.

Schools have due process rights allowing them to continue participating in FFELP during the resolution of their appeals. Their participation assures students attending these schools continued access to FFELP loans and protects schools from being denied program eligibility on the basis of erroneous default rates. However, to help guard against the possibility that a school may simply continue to abuse the program until its administrative appeals are exhausted, some additional form of accountability may be necessary.

The risk of loss from additional defaults accrued by schools filing appeals could be significant if the appeal is unsuccessful. For example, there were 88 schools with appeals pending for 1 year or more as of September 30, 1994. If these schools' students continued to receive loans and default on them at the same pace as they did during the preceding years, we estimate that the additional defaults through September 30, 1994, could have cost the government about \$50 million.¹⁴

Possible ways to address this concern include (1) holding schools liable for the costs associated with defaults on loans that their students receive

¹⁴More specifically, our estimate is based on the following assumptions: (1) the schools continue to enroll students at the same rate as before the appeal, (2) students continue to enter repayment at the same rate as they did in fiscal year 1992 (the latest year for which the related default rate data were available), (3) the schools continue to experience the same default rate they had in fiscal year 1992 (the latest year for which the related default rate information was available), and (4) the average loan for students at these schools is equal to the average Stafford loan at all schools across the country (\$2,815 in fiscal year 1992).

during the appeal process and (2) making some schools post a performance bond as a condition of filing an appeal. Both of these options have some precedence in earlier loan programs or in rulings by the courts. Either option would allow a school to continue exercising its due process rights and to enroll students with guaranteed loans as the school's appeal is being reviewed by the Department or the courts.

Making Schools Liable for Costs on Defaulted Loans Made During the Appeals Process

One approach for reducing the government's risk of loss would be to require that if a school is unsuccessful in its default rate appeal, it must reimburse the government for the costs associated with defaults on loans that the school certified during the appeals process. The Department had such a policy in place for SLS loans, but without specific legislation it had to request relief from the courts on a case-by-case basis.

Under such an arrangement, the Department would continue to incur costs as it does for other guaranteed loans by paying interest subsidies on loans while students are in school and by paying claims for loans that default. If a school wins its appeal, the government would bear the costs attributed to loans that may eventually go into default. If a school loses its appeal, it would share in the risk of loss; it would be responsible for the cost of any loan that was made and defaulted on after the default rate appeal was filed.

Such an arrangement might also deter schools from filing frivolous appeals. A reduction in the number of appeals filed would free up the Department's resources to more quickly adjudicate appeals that were filed. Department officials said that they have asked the courts for such arrangements on occasion, and have been granted them in a few instances. They said that if the Department was given the legislative authority, it could use it more uniformly and not be required to ask the courts for it.

Requiring a Performance Bond

Another approach would be for the Department to require some schools to post a performance bond as a condition of filing an appeal if the school has default rates that far exceed the statutory thresholds and in the Department's view may be unlikely to succeed in an appeal. For example, about one-third of the 88 schools with appeals pending for 1 year or more had default rates of 40 percent or higher, compared with the statutory threshold of 25 percent.

The amount of a bond could be established on the basis of a school's most recent default rates and loan volume experience. For example, in one of the lawsuits against the Department, the court ordered the schools to post a bond each month for a percentage of the face amount of student loans certified during that period. The percentage was established as the schools' average historic default experience, and at the end of each month the schools were required to increase the bond amount by the additional volume of loans certified during that month. Under such an arrangement, a school with a 3-year average default rate of 30 percent and \$100,000 in new loans each month would have to post a \$30,000 bond at the end of the first month, a \$60,000 bond at the end of the second month, and so on until the appeal was finalized. If the school's appeal took 3 months to adjudicate and the school was unsuccessful in its appeal, the Department could demand a forfeiture of the bond, which would amount to \$90,000 at the end of the third month. If, on the other hand, the school was successful in its appeal, the bond would be cancelled and the school would be allowed to continue participating in FFELP.

The Department does not have statutory authority to place bonding requirements on schools that are appealing their default rates. A Department official said that a bonding provision would help the Department deal with frivolous appeals, while at the same time allow schools that have more legitimate concerns the opportunity to appeal the Department's actions.

Conclusions

Data accuracy problems and loan servicing issues have hampered the Department's efforts to eliminate schools with high default rates from FFELP participation. If designed and implemented properly, the National Student Loan Data System and new statutory requirements established by the 1993 amendments to allow schools to review the quality of its loan database should contribute to the Department more accurately determining schools' default rates. However, the defaults associated with new loans made by schools filing unsuccessful appeals could be very costly to the government. Requiring schools to pay for the default of subsequent student loans if their appeals are unsuccessful could help reduce the government's costs.

Matters for Consideration by the Congress

In those instances in which schools appeal a Department action to eliminate their FFELP eligibility because their default rates exceed a statutory threshold, the Congress may wish to consider giving the Secretary of Education authority to require schools to reimburse the

government for the cost of loans that are made and that may subsequently default, in the event that the schools' appeals are unsuccessful.

As a measure of further protection of the government's interests, the Congress also may wish to consider granting the Secretary the authority to require schools to post a performance bond as a condition of filing an appeal as well as the discretion in determining under which circumstances a bond would be required of schools.

Agency Comments and Our Evaluation

We requested comments on a draft of this letter from the Secretary of Education or his designee. On May 19, 1995, we received verbal comments from representatives of the Department's Offices of General Counsel and Postsecondary Education. They generally agreed with the results of our findings. They suggested several technical changes, which we incorporated in the letter, as appropriate.

Copies of this report are being sent to the Ranking Minority Member, Permanent Subcommittee on Investigations, Senate Committee on Government Operations; the Chairman, Senate Labor and Human Resources Committee; the Chairman, House Economic and Educational Opportunities Committee; the Director, Office of Management and Budget; the Secretary of Education; and other interested parties. Please call me at (202) 512-7014 if you or your staff have any questions about this report. Major contributors include Joseph J. Eglin, Jr., Assistant Director; Charles H. Shervey; and Jonathan H. Barker.

Sincerely yours,

Cornelia M. Blanchette

Cornelia M. Blanchette
Associate Director, Education
and Employment Issues

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Abbreviations

| | |
|-------|---------------------------------------|
| FFELP | Federal Family Education Loan Program |
| OGC | Office of General Counsel |
| OIG | Office of Inspector General |
| SLS | Supplemental Loans for Students |

Scope and Methodology

We examined the provisions of the Higher Education Act of 1965, as amended, pertaining to the use of student loan default rates. We also examined federal requirements and other documentation the Department of Education issued to implement the Student Loan Default Prevention Initiative Act of 1990.

We obtained and examined default rate statistical information from the Department to identify schools with rates exceeding statutory thresholds. We focused our analysis on data pertaining to schools subject to the loss of FFELP eligibility, that is, schools with default rates exceeding statutory thresholds for three successive years.

To determine the extent that problems with the Department's default rate data have been previously identified, we reviewed prior reports and other documentation prepared by GAO and the Department's OIG and program offices. We discussed the data accuracy problems with OIG staff and program offices. We also discussed with Department officials the National Student Loan Data System—the first of its three phases became operational in November 1994—to determine whether it will address data accuracy problems associated with existing data bases.

To determine the nature and status of court cases relating to the accuracy of default rates, we reviewed and analyzed various documents filed in the courts by schools filing the lawsuits and the Department. We also discussed the issues and status of each case with officials of the Department's Office of General Counsel (OGC).

We reviewed the Higher Education Technical Amendments of 1993 and the Department's regulations implementing these amendments to determine the extent to which the amendments and regulations address the data accuracy and other issues being litigated by the schools and the Department. We discussed the amendments and regulations with attorneys from the Department's OGC and officials from the Default Management Section.

Our work was conducted from September 1993 through March 1995 in accordance with generally accepted government auditing standards.

FFELP Eligibility Status of Schools With Default Rates Over the Statutory Thresholds (Fiscal Years 1991-94)^a

| | |
|--|------------------|
| Schools with default rates over thresholds | 890 |
| Schools losing eligibility ^b | 601 |
| Schools retaining eligibility | 289 |
| Schools filing successful appeals | 19 ^c |
| Schools with pending appeals | |
| Erroneous data and/or loan servicing appeals | 250 ^d |
| Mitigating circumstances appeals | 20 ^e |

^aIncludes schools with default rates exceeding thresholds for 3 successive years. Excludes schools subject to limitation, suspension, and termination action with a single-year default rate over statutory thresholds.

^bThese schools lost eligibility because they did not file appeals, filed unsuccessful appeals, or closed and went out of business.

^cAn additional 26 schools filed successful appeals. However, they had default rates over the thresholds in a subsequent year and either (1) had appeals pending for default rates over the thresholds in subsequent years (8 schools), (2) lost eligibility because they failed to file a successful appeal in a subsequent year (15 schools), or (3) closed and went out of business after filing their successful appeals (3 schools).

^dIncludes 25 schools that also filed mitigating circumstances appeals.

^eThese schools' appeals did not challenge the accuracy of the Department's default rates through erroneous data and/or loan servicing appeals.

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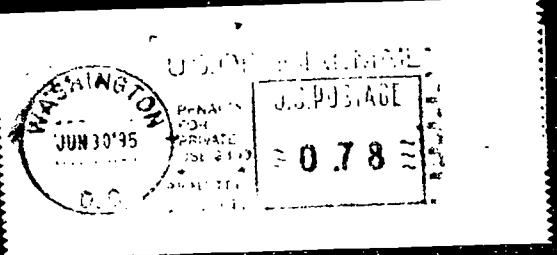
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Penalty for Private Use \$300

Address Correction Requested



SHIP TO:
GAIL MATHEWS
1301 PICCARD DR. S-300
ROCKVILLE MD 20850

Request # 3433682 27 3

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