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ABSTRACT

This document reports oral testimony and prepared statements of persons who testified at hearings on the financial difficulties confronting the Higher Education Assistance Foundation (HEAF) and the impact that situation has on the Stafford Student Loan Program of the Department of Education. Witnesses included: Lauro F. Cavazos, U.S. Department of Education; Jean S. Frolicher, National Council on Higher Education; Stephen J. Blair, National Association of Trade and Technical Schools; Charles B. Saunders, Jr., American Council on Education; and A. Dallas Martin, National Association of Student Financial Aid Administrators. Their testimonies focused on the administration, structure, stability, and integrity of the Stafford Loan Program and program reform. Prepared statements were also submitted by Senators Edward M. Kennedy, Paul Simon, and Dave Durenburger; and by Richard C. Hawk, Stephen C. Biklen, Lawrence A. Hough, Bruce F. Vento, Samuel M. Kipp, and Muriel Johnson Murray. (LPT)

HC

S. HRG. 101-951

PROBLEMS CONFRONTING THE HIGHER EDUCATION ASSISTANCE FOUNDATION

HEARING

BEFORE THE

SUBCOMMITTEE ON EDUCATION, ARTS, AND HUMANITIES

OF THE

COMMITTEE ON LABOR AND HUMAN RESOURCES UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

ON

EXAMINING THE FINANCIAL DIFFICULTIES CONFRONTING THE HIGHER EDUCATION ASSISTANCE FOUNDATION AND THE IMPACT THAT SITUATION HAS ON THE GUARANTEED STUDENT LOAN PROGRAMS OF THE DEPARTMENT OF EDUCATION

AUGUST 3, 1989

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PROBLEMS CONFRONTING THE HIGHER EDUCATION ASSISTANCE FOUNDATION

FRIDAY, AUGUST 3, 1990

U.S. SENATE,
SUBCOMMITTEE ON EDUCATION, ARTS, AND HUMANITIES,
COMMITTEE ON LABOR AND HUMAN RESOURCES,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:05 a.m., in room SD-430, Dirksen Senate Office Building, Senator Claiborne Pell (chairman of the subcommittee) presiding.

Present: Senators Pell, Kennedy, Simon, Kassebaum, Hatch, Jeffords, and Durenberger.

OPENING STATEMENT OF SENATOR PELL

Senator PELL. The Subcommittee on Education, Arts, and Humanities will come to order.

We will focus this morning on the financial difficulties confronting the Higher Education Assistance Foundation (HEAF) and the impact that situation has on the Stafford Student Loan program.

I very much appreciate the fact that the Secretary has agreed to appear before the subcommittee this morning. He really is a great friend of education, and I look forward to his testimony.

Before we hear from you, I would like to stress, though, that this hearing has two primary purposes: First, we want to address the specific problems raised by HEAF's financial difficulties and the department's efforts to address those problems. Second, we want to take a careful look at the overall health and stability of the Stafford Student Loan program in light of the crisis brought on by HEAF's difficulties.

I think we should be clear on one point from the outset. It is vitally important that all of us who are involved in the loan program—the students who borrow, the schools they attend, those who lend, those who guarantee, or any interested party, for that matter—know from the outset that the program is stable and that the Federal guarantee is in place.

That is not to say that the program is not without problems. Defaults in the Stafford Student Loan program constitute an extremely serious problem. They will cost the Federal Government more than $2 billion this year. As I have said time and time again, that is an intolerable situation that must not continue unabated. If it does, it will threaten the viability not only of the student loan program but of all Federal student aid programs.

For several years, I have sought strong measures to crack down on student loan defaulters. My proposal to report defaulters to credit bureaus, where the question of getting a credit card comes, is now, I am glad to say, law. The proposal that Bob Stafford and I advanced to withhold income tax refunds from defaulters is now law. And my idea that no student should receive Federal student aid unless they make satisfactory academic progress is also law.

Further, on at least four separate occasions, the Senate has taken strong action to curb defaults. We passed legislation that enabled a guarantee agency to stop doing business with any school that had a default rate in excess of 25 percent. We twice passed legislation that required schools, lenders, and guarantee agencies to implement stringent default management plans.

I believe it very important that we include in the hearing record today a summary of the action the Senate has taken in this area. In addition, I am including in the record a summary of the default reduction measures that were a part of the 1986 Higher Education Act Amendments.

While I am very glad that the department, when it implemented the new default regulations last year, drew extensively on the Senate-approved legislation, I remain disappointed to date that the House has not—I repeat, not—acted on the Senate legislation.

This hearing cannot proceed, however, without an acknowledgment of the fact that the problems we face in the loan program would be far less serious if our grant programs had been adequately funded. We would not need a large loan program, and we would not have had a huge increase in borrowing had our grant programs kept pace with the increase in borrowing and costs of a college education.

There is a crisis in student aid today. It is the crisis brought about by a Reagan administration that cared very little about the educational opportunities of needy, deserving students. Not only did it try to completely cut out, to eliminate the Pell Grant program by as much as 40 percent, but it also sought to wipe out entirely our supplemental grant, College Work Study, and State Student Incentive Grant programs.

We are fortunate the Reagan administration did not succeed, but their efforts took a toll. In Congress, we had to spend days, weeks, and months fighting just to keep programs in place. That was valuable time that could have been put to good use pushing for increases instead of staving off cutbacks. To my mind, that is the crisis that should be grabbing headlines today.

Mr. Secretary, as you know, I had hoped that the department would have been able to offer the details of its plan to remedy the HEAF crisis to the subcommittee this morning. I regret this is not the case, but I do look forward to your testimony and to your report on the department's efforts to resolve this crisis and maintain the public confidence in this student aid program.

Finally, there is one question that I am sure is in everyone's mind. I must ask you, Mr. Secretary, and every other person who testifies this morning: Is this or could this become another S&L crisis? I appreciate so much your being here.

[The information Senator Pell refers to follows:]

SUMMARY OF SENATE DEFAULT ACTION, 1987 TO PRESENT

1. S. 1448 Introduced June 1987; passed August 1987: Would have allowed guaranty agencies to withdraw their guaranties from any school with a default rate in excess of 25%. Added to Omnibus Trade bill. House would not accept in conference.

2. S. 2647 Introduced June 1988; passed September 1988: Major default bill based upon extensive review of problem including two hearings in December 1987. Provisions highlighted in the accompanying summary. House took no action.

3. S. 568 Introduced and passed March 1989: Same as S. 2647 in 100th Congress. Reintroduced and passed under unanimous consent. Bill still pending in House.

   (Spring 1989, Department issued new default regulations which borrowed heavily from Senate bill.)

4. S. 695 Introduced April 1989; passed February 1990: Includes many default provisions from S. 2647. This is the President's education initiative and may go to Conference in September.

Note: When the Higher Education Act was reauthorized in 1986, default reduction was a major topic and the legislation contained several provisions in this area. Those provisions are highlighted in the accompanying summary.

S.2647 Summary

"Stafford Student Loan Default Prevention and Management Act of 1988"

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1. Default Management Plan: Title I of the bill requires any school, lender or guaranty agency with a default rate in excess of 25% to develop a default management plan. The plan would be developed and administered in cooperation with the state guaranty agency, in the case of schools and lenders, and the Department of Education, in the case of guaranty agencies. The purpose of the default management plan would be to direct institutional resources towards a default reduction plan that takes into consideration the unique needs of each institution.

   If, after three years under a default management plan, a school or lender has not reduced its default rate below 25%, the guaranty agency administering the plan may recommend that the Secretary of Education begin the implementation of limitation, suspension and termination proceedings. The Secretary must implement such proceedures.

   Title I also outlines how defaults are to be measured for the purposes of this plan. The Secretary will publish an annual default rate for each lender, school and guarantor which shall be based on the average of three previous years. Each of the three year's rates will include any recoveries made during the first two years such loans were in repayment and will be credited to the school the student attended when the loan was made.

2. Improved Collection Provisions: Title II provides for batter information collection and communication amoung guarantors, schools, lenders and students. Included in this title are credit checks for PLUS loans, credit bureau reporting at 90 days of delinquency, additional borrower information, notification to schools of defaulting students, withholding of academic transcripts for defaulters and notice of loan sales by lenders.

   This title also prohibits the use of commissioned sales people in admissions.

3. Responsibilities: Title III outlines new responsibilities for the Department of Education including greater restrictions on schools that have had their accreditation revoked and mandating the establishment of the national student loan data system.

4. Needs Analysis: The bill also addresses several of the more severe problems created in the needs analysis system by the Higher Education Amendments of 1986. Specifically the bill would reduce dependent student contributions from 70 to 50% of earnings, would remove home, farm and business equity from consideration in needs analysis for families with adjusted gross incomes of under $30,000 and make several minor adjustments suggested in the first report of the Student Aid Advisory Commission.

Summary of Default Provisions in 1986 HEA REAUTHORIZATION

Guaranteed Student Loan

o Reaffirms mandated multiple disbursement of loans.

o Mandates universal need analysis.

o Limits borrowing by first and second year students to $2625.

rohibits loan agencies from offering inducements to education insti ons or employees to secure applications for loans.

o Allows any guaranty agency to request information from any other agency on borrowing by students in its State.

o Allows the Secretary of Education to reimburse loan agencies for the cost of supplemental preclaims assistance under reinsurance.

o Establishes a reinsurance fee based on default rates to be paid to the federal government by guaranty agencies; agencies with a default rate less than 5% will pay a fee equal to .25% of the total principal amount of loans on which they issued insurance during the fiscal year and agencies with rates equal to or greater than 5% will pay a fee equal to .5% of such amount.

o Requires guaranty agencies to submit proof that reasonable attempts were made to locate the borrower, in the case of a defaulted loan when the borrower's location was unknown, and proof of contact with the borrower when the location was known.

o Allows guaranty agencies to permit forbearance on defaulted loans.

o Allows guaranty agencies to retain 30% of collections to cover agency costs without proof of such incurred costs to the agency.

o Allows disposable pay to be garnished up to 10% if adopted by the State. Requires notice to the borrower and an opportunity to respond; provides the borrower with an opportunity to review existing information; provides the borrower the opportunity to establish a repayment schedule with the guaranty agency; sets penalties for employers' non-compliance after notice; and prohibits the employer from firing or taking disciplinary action against an employee whose wages are garnished.

o On a three-year pilot project basis, allows guaranty agencies or the Secretary to sell defaulted loans which have been in repayment status for 12 months and allows the borrower having such a rehabilitated loan to be eligible to receive additional loans.

o Allows guaranty agencies to provide information to eligible institutions on former students of the institution who are in default, including the names and addresses of such students. Public dissemination of such information is not authorized. Activities performed by educational institutions to relating to delinquent or defaulted borrowers must be clearly supplemental to the due diligence required to be performed by guarantors and lenders.

o Provides for graduated or income-sensitive repayment in the case of consolidated loans.

o Requires guaranty agencies to submit proof that attempts were made to locate the borrower in case of a default.

o Requires guaranty agencies and lenders, as appropriate, to make reports to credit bureaus on current balances, default date, and collection and cancellation of the loan through repayment. Holders of loans are to report on loans in good standing and guaranty agencies on loans in default status.

o Requires the Secretary to limit, suspend, or terminate lenders who engage in fraudulent or misleading advertising that may have led to making loans or the making of loans that violate the certification for eligibility.

o Authorizes the Secretary to sell defaulted loans (assigned to the United States) to collection agencies, lenders, or other parties if those loans are in default status and only as a last recourse after all other collection efforts have failed and the loan has been in default for at least one year.

o Requires that lenders inform student borrowers of the total cumulative balance owed, the projected level of indebtedness of the student based on a four-year college career and an estimate of the projected monthly repayment for those loans held by the lender.

o Requires the lender, each time a loan is disbursed, to provide the borrower with a separate paper summarizing his rights and responsibilities in plain English, including a statement of consequences of default and a statement that defaults will be reported to a credit bureau.

o Prohibits the use of commissioned salesmen to promote the availability of supplemental loans.

o Prohibits unsolicited mailings of student loan application forms to students unless the students have previously received loans from that lender.

Perkins Loans (formerly NDSL)

o Provides that for the 1987-88 award year, institutions with a default rate in excess of 20% will receive no new federal capital contributions and that institutions with default rates between 7.5% and 20% will have their FCC reduced. Further provides that for the 1988-89 and other subsequent award years, institutions with a default rate in excess of 15% will receive no new FCC and institutions with default rates between 5% and 15% will have their FCC reduced.

o Requires loan information be provided to student borrowers by education institutions both prior to disbursement and prior to repayment and including the same required in the GSL program above.

General Provisions

o Prohibits students who are in default under the GSL or NDSL programs or owing any refund on any federal grant program, from receiving any form of federal assistance while they remain in default.

o Requires exit counselling of student loan borrowers which provides general information on the average indebtedness of students, the average anticipated monthly repayments and the available repayment options. Such counselling can be provided to either individuals or groups of students.

o Requires the Secretary to make available to institutions and lenders information on debt burdens and total and monthly repayment obligations that students may incur as a result of borrowing under the GSL programs.

o Creates a National Student Loan Data System which will maintain computerized student loan data on GSL and NDSL programs. Access to information in the system is restricted to individuals and federal agencies specifically authorized by the Secretary to have such access and may be used only for research, improvement of federal debt collection practices, and furnishing information in response to an official request by a committee of the Congress.

Senator PELL. I will turn to the chairman of our full committee who has honored us with his presence.

OPENING STATEMENT OF SENATOR KENNEDY

The CHAIRMAN. Thank you very much. I want to at the outset commend Senator Pell for having these hearings and for the oversight that he has been providing on this extraordinary, challenging situation facing millions of families and millions of young people in this country; that is, the stability of the student loan program. I join in welcoming the Secretary here this morning, and we are looking forward to his commendation.

I want to make just a couple of brief observations. One is to reinforce what the chairman has said about the dramatic shift from the grant program to the loan program. I think when we developed the higher education programs in the early 1960's, it was with the idea that any talented young person in America that had the intellectual skills and the ability and gained entrance into an institution of higher learning, would have available to them the matching of either loans or grants or work study or employment of the resources of their families, and match them together in order to be able to obtain the best education that they desired and that they had a capability of achieving. And as the chairman has just pointed out, what has happened in the interim during the period of the 1980's is that we have put the dollar sign right back on the doors of every one of our institutions of higher learning and denied millions of young people the opportunities to go to institutions that they desired. The real reason for that is the very dramatic cutback in the grant programs and other programs which the Chair has outlined. I think the real challenge for us as a country, as a Nation, is to restore that balance. We will be dealing with that at another time, but I think it is worthwhile at the outset of these hearings to underline that point.

Student loans are an indispensable part of Federal student aid. The problems confronting the Higher Education Assistance Foundation have undermined confidence in that program, and we intend to work closely with the administration to see that confidence is restored.

The most important short-term priority is to assure the stability of the Stafford Loan program. This means two things. First, the loan guarantees made by the Higher Education Assistance Foundation must be honored. Second, students and their families must be assured that Federal loans will be available on schedule to meet this fall's tuition bills. All of us understand that this is the critical time. July and August are the times when there is the greatest demand for these programs.

If lenders know that the guarantees will be honored, loans will be widely available to students, and the access to loans that has been the hallmark of the program will be preserved.

But we also need to address long-term issues about the structure and integrity of the program. The HEAF problem and its negative publicity reinforce the perception that this program is poorly designed and administered. The continuing negative publicity about the program makes all its other problems worse.

Under the leadership of Senator Pell, the Labor Committee has taken numerous steps to address these problems. On several occasions, the Senate has enacted legislation to reduce loan defaults. Earlier this year, for example, the Senate approved the Educational Excellence Act of 1990, and we intend to do all we can to see that the default reduction provisions in this legislation are enacted into law before Congress adjourns.

Last year's Budget Reconciliation Act contained specific provisions to reform the Supplemental Loans to Students program. We acted in response to evidence compiled by the General Accounting Office suggesting that too many student loans were being made, especially to students at proprietary schools, and that student loan defaults were increasing sharply.

The actions we took had a substantial effect. In a report released just today, the GAO finds that among the nine largest guarantee agencies, borrowing in the SLS program was 46 percent lower in the first 4 months of this year than in the comparable period in 1989. Borrowing by students at proprietary schools dropped by 65 percent.

Last year's reforms, coupled with the pending default reduction legislation, demonstrate that these problems are being addressed. Similar action will also be a prominent part of our proposals next year for reauthorizing the Higher Education Act.

Today's hearing is the next step in a series of efforts to ensure that these vital reduction programs do the job they are supposed to do.

[The prepared statement of Senator Kennedy follows:]

Prepared Statement of Senator Kennedy

I commend Senator Pell for his commitment to the student loan program, and for scheduling this timely hearing on the financial problems of the is Higher Education Assistance Foundation.

Student loans are an indispensable part of Federal student aid. The problems confronting the Higher Education Assistance Foundation have undermined confidence in that program, and we intend to work closely with administration to see that confidence is restored.

The most important short-term priority is to assure the stability of the Stafford Loan program. This means two things. First, the loan guarantees made by the Higher Education Assistance Foundation must be honored. Second, students and their families must be assured that Federal loans will be available on schedule to meet this fall's tuition bills.

These two goals are interrelated. If lenders know that the guarantees will be honored, loans will be widely available to students, and the access to loans that has been the hallmark of the program will be preserved.

But we also need to address long-term issues about the structure and integrity of the program. The HEAF problem and its negative publicity reinforce the perception that this program is poorly designed and administered. The continuing negative publicity about the program makes all its other problems worse.

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Today's hearing is the next step in a series of efforts to ensure that these vital reduction programs do the job they are supposed to do.

Senator PELL. Thank you very much, Senator Kennedy.

Senator Hatch, the ranking minority member of the full committee.

OPENING STATEMENT OF SENATOR HATCH

Senator HATCH. Thank you, Senator Pell. I appreciate it. Welcome, Dr. Cavazos, Mr. Stringer, and other witnesses here today.

The problem before us today is a very serious one. It threatens a program which is of vital concern to our future as a Nation, the Guaranteed Student Loan program. It is essential that both the short- and long-term solutions to this problem ensure the ability of students to obtain loans and the ability of banks to have those loans guaranteed by the Federal Government. I am a strong supporter of the student loan program and the opportunity it provides for students in all socioeconomic classes to attend the school of their choice. I am confident that Secretary Cavazos knows the importance of the decision that he must make within the next few days and will work for the best solution possible.

I want to commend you, Dr. Cavazos, for the way in which you have handled this emergency. As soon as this evolved into a crisis situation, you immediately alerted us up here in Congress. At the same time, you took steps to resolve the crisis and to protect the integrity of the student loan program by ensuring that all loans would be guaranteed and that all eligible students would continue to have access to these loans. I appreciate the kind of leadership you have shown.

I also appreciate the cooperation of Dr. Roberta Dunn, who was formerly on my staff, and I think she has done an excellent job in these areas as well.

The student loan program is very different from a normal customer loan program. It requires different handling. The element of risk is much higher because the borrowers do not have credit histories, and the borrower puts up no collateral. That particular element of the program makes it risky. It also ensures access to students from all backgrounds in our society and gives them all a chance to be able to go to school. We cannot eliminate the risk without reducing that access.

I hope that in the process of resolving this crisis we can find better ways to handle and share the risks inherent in this program. We will have to deal with the systemic problems that have become even more apparent as a result of the HEAF crisis during the upcoming reauthorization of the Higher Education Act. I hope our experience with HEAF will result in a stronger and better student loan program.

As I have said, I look forward to hearing the testimony of the witnesses today. I can only be here for a short part of this meeting, but I again want to express appreciation to you, Dr. Cavazos, and those who are working with you, and hope that working together we can help solve this problem, as I think Senator Kennedy and Senator Pell have indicated, before the end of this Congress. I intend to work hard to get that done, and hope all of us will.

Thank you, Mr. Chairman.

Senator PELL. Thank you very much.

Senator Simon.

Senator SIMON. Thank you, Mr. Chairman. I thank you for holding the hearing and your leadership on this issue. Obviously, we want to deal with the problem.

I would just like to underscore, however, the point made by Senator Kennedy that we have in this past decade had a very substantial shift from grants to loans in the Federal student aid portfolio. I think it has not served the Nation well. It first of all costs us more, believe it or not, as the Grace Commission report has pointed out, because we end up subsidizing interest and paying for defaults. We will spend more money this fiscal year for student loan defaults than for the Head Start program. That is really an appalling situation.

In addition, it distorts things. First of all, it is a barrier to families of limited income. For a family of limited income to owe $10,000, or more, after completing college is a barrier. It distorts occupational choices. Do you go into business or do you become a social worker? Well, if you are going to face $10,000 to $15,000 in loans, you tilt the answer on that. It postpones dreams that people have.

I talked to a young couple paying $711 a month on student loans. They would like to buy a home and have a family. They are postponing that because of their student loan debt.

We also know from studies that those who are in school on loans are much less likely to stay than those who are on grants. So we are not utilizing the human capital of this Nation as we should.

Finally, there is a clear discriminatory factor. We have made a lot of progress in our country, and I am proud of the progress that we have made. But the reality is those of us who are white males, when we graduate from college, on the average are going to earn more than those who are female and those who belong to minority groups. So it is easier for us to repay loans.

I hope, as we re-examine the Higher Education Act next year—not that we are going to do away with the student loan program—we have a shift back to the grant program. I think it is extremely important for the future of this country.

Thank you, Mr. Chairman.

[The prepared statement of Senator Simon follows:]

PREPARED STATEMENT SENATOR SIMON

Mr. Chairman, I commend you for holding this hearing to address the financial problems facing the Higher Education Assistance Foundation (HEAF)—the largest guarantee agency in the Federal Stafford Student Loan Program. It is imperative that we obtain more information about the precise nature and the magnitude of the problems facing HEAF, the potential liabilities of the Federal Government, and how the Department of Education plans to deal with these issues.

Mr. Chairman, it is critical that the department act swiftly to reach a solution to HEAF's problems that will maintain the full faith in and integrity of the Stafford Student Loan Program. Millions of students and their families across the country will soon be preparing to enter or return to school this fall. Both the students and their families, and lenders who actually make the loans to them, must be assured that loans will continue to be issued and guaranteed this fall. Timely action on this issue is of the utmost importance.

Mr. Chairman, public confidence in the Federal student loan programs has already been shaken by the intolerable student loan default costs that taxpayers are subsidizing. As you are well aware, this subcommittee, in particular, has carefully monitored these issues and developed legislation to address them. We have moved aggressively and in a creative fashion to reduce student defaults. I have introduced legislation, as have other members of this panel. In the 1986 Higher Education Act amendments, and in every year since then, this committee has moved forward with legislative measures designed to get control of the Federal student loan programs.

Much more can and should be done to reduce student loan default costs. One major action that we can take to reduce these costs is to reduce the number of students who are forced to take out these loans in the first place, because there is insufficient financing of the Pell Grant Program. I have made no secret of the fact that I believe that our priorities in student aid policies are wrong. We have shifted from a primary emphasis on loans, rather than grants. Now, even needy, at-risk students must borrow to finance their education. And, offering low-income students the opportunity to acquire $10,000 or more in debt over 4 or 5 years is no real offer at all.

But, Mr. Chairman, the immediate issue at hand is the crisis facing the Higher Education Assistance Foundation. I look forward to hearing the testimony of our distinguished witnesses and their suggestions for addressing the short- and long-term problems facing the Stafford Student Loan program.

Senator PELL. Thank you very much.

Senator Kassebaum, the ranking minority member of our subcommittee.

Senator KASSEBAUM. Thank you, Mr. Chairman. I made an opening statement last week in the Banking Committee. I think I will save my remarks for questions.

Senator PELL. Thank you, Senator, very much.

Senator Jeffords.

OPENING STATEMENT OF SENATOR JEFFORDS

Senator JEFFORDS. Thank you, Mr. Chairman. I certainly appreciate this hearing today. I think it is very important. I certainly want to welcome the Secretary as well.

The matter at hand is the financial stability of HEAF, the Higher Education Assistance Foundation. The solvency of one of the largest guarantors within the Federal student financial assistance programs brings with it both short-term concerns as well as a number of essential policy questions and ramifications. In the short term, we must ensure that students will continue to have access to the loan program; that the viability and public confidence within the program is resumed; and that participants in the program will not be adversely affected. But I believe in the long run it is the long-term effects that we must focus on.

The proverbial "sins of the past" may be coming back to haunt us. When we established a system of using guarantors, did we recognize and understand the full ramifications of our actions? Did we put in enough safeguards against such a situation and monitor it properly? Did we anticipate such an occurrence? Now that this situation has arisen, are there other guarantors in a similar situation?

The question is not solely of control over the guarantee agency. It is just as much a question of control over school eligibility within the student loan program. As its root, this is basically a question of defaults. I firmly believe that all students must have access to student aid. However, not all schools should be able to participate within the program. We must be very careful not to point the finger solely at proprietary schools nor imply that all proprietary schools are unscrupulous. But we can no longer afford to turn a blind eye to these schools—whether they be 4-year institutions, community colleges, or proprietaries—that are using a publicly financed program for their own financial benefit.

Investigation and auditing of schools must be increased, and controls on new schools coming into the program must be adequately monitored. I am not confident this has been the case in the past few years. There are numerous questions that must be answered, and I will have some for our witnesses. I don't want to ignore the short-term resolution of this problem for I believe we have a responsibility to ensure that it is the best solution. However, I believe even more vehemently that we must begin to look at the long-term effects of this situation and take a careful look at our overall policy intent of the student aid program. We cannot afford to lose public confidence in a program that has been successful and that has provided increased opportunity to many individuals.

I look forward to the testimony of the witnesses here today.

Senator PELL. Thank you very much.

We have been joined by Senator Durenberger of the full committee.

Senator DURENBERGER. Mr. Chairman, let me begin by thanking you for holding this hearing. I thank all of you on the Education Subcommittee for your commitment to higher education issues and for your inviting me to join you here today.

I am here because I have a long-term interest in education and higher education, but I am also here, Mr. Chairman, because I was an original member of the board of HEAF, the Higher Education Assistance Foundation, back in my pro bono days in Minnesota before the thought ever occurred to me to get anywhere near politics, to say nothing of running for the U.S. Senate. So I have a familiarity, with HEAF and certainly with Dick Hawk, which goes way back into the 1960's when he served as the chairman or the president and executive director, whatever we called it in those days, of the Higher Education Coordinating Commission in the State of Minnesota, and then in his capacity as the chief executive of HEAF.

We all know it is the largest guarantor agency in the country. We should know by now that over the past 3 years HEAF has guaranteed $14 billion in loans, and in 1988 made 815,000 people's lives richer by providing the means of access to higher education. And I don't think we should lose sight of that fact over a period of time.

I am not here to defend the condition that the agency is in. I am here to learn, like everybody else. What I have learned over the last few weeks is that there is enough blame for the condition HEAF is in to go around, that includes the department, we here in Congress, educational institutions who have failed to provide quality education to its students, HEAF, and a lot of other people. Just like every other situation, there is no single source of blame. But I trust that is not what my colleagues are here to do. As several of you have indicated in your opening statements, I think this ought to look at how we can learn from mistakes. This ought to be part of dealing with the issue of access to higher education in America, and it also ought to do something with the quality of education in America.

We have differing philosophical views on the approach to the acquisition of public services. I couldn't disagree more with my colleague from Illinois on the subject of grants versus loans. I think a free access to anything in America today has an impact on the quality of the service that is delivered. And whether it is a Pell grant or it is a totally subsidized elementary, secondary system, or whatever the case may be, there is no question in my mind that there is some value attached to earning access to a system. And one of those values is that you get to be a little bit more concerned about what it is you are acquiring—whether you go to college or a trade school or whatever.

I think one of the benefits of the loan system in America has been that it has made it possible for people to participate in making sure we have quality education in this country. I for one believe that those who advocate moving in the direction of financing more and more access through the loan system but changing the way we do it is a much preferable course. The campaign of Governor Dukakis in 1988 on this subject excited me. The notion that financial aid ought to be part of the social insurance system in America, for example, that people can borrow against their hopes and their dreams, can take the financing into an institution and make a difference when they get there in the quality of what they are getting, and then through their earnings make a repayment, is one I believe in very strongly.

I would assume around this table we have differing views on that subject, and I would hope, Mr. Chairman, that I will be permitted as a member of the full committee to participate at various times in your debate on the Reauthorization of the Higher Education Act and as you continue to review the problems facing HEAF and learn from this experience how best to shape public policy and the approach to higher education, postsecondary education in America by the Federal financing guarantees for that access.

Thank you.

Senator PELL. Thank you.

[The prepared statement of Senator Durenberger follows:]

PREPARED STATEMENT OF SENATOR DURENBERGER

Mr. Chairman, I want to thank you for holding this hearing today and for allowing me to sit in on this hearing, even though I am not a member of this subcommittee. As you know, not only have I had a long interest in trying to increase access to higher education for all Americans, but because of this interest, I was an original member of the board at HEAF and have followed its progress closely as it has operated over the years in St. Paul.

HEAF is the largest guarantor agency in the country. Over the past 3 years it has guaranteed $14 billion in loans and has given 815,000 the opportunity to pursue their dreams through higher education.

So it is with deep regret that we are here today under these circumstances. Not only because I do not like to see Dick Hawk and the 800 people in Minnesota on the low end of the free enterprise system in this country, but more importantly for the implications this has on the whole student loan program and the access for the thousands of kids going off to college this fall.

As I have followed the issue over the past 3 weeks I have found that there is plenty of blame to go around—among HEAF, the department, the institutions, and here in Congress. But there is also a lot to be learned from this situation and I have a deep interest in finding out the answers behind the reason we are here today, and also to find out how the problems at HEAF will effect access to the student loan program for all Americans in the future.

I believe we need to look first at a short term solution to the situation surrounding HEAF, and then we need to look closely at the system as a whole to find a lrng-term solution for the future. I hope that this hearing today will be a first step in that direction.

I look forward to hearing from all the distinguished group of witnesses here today, but I would especially like to welcome my good friend Dick Hawk. Dick has been a friend of mine for many years. I only wish that I were welcoming him here under better circumstances.

Mr. Chairman, I want to thank you for the opportunity to be here today and look forward to working with you on a solution to this problem in the future.

The CHAIRMAN. Mr. Chairman, just one point. I just want to indicate to the Secretary and to other witnesses that I understand their testimony wasn't available until this morning. We have had long hours, but I am one who takes time generally on a matter of this importance to try and prepare myself for these hearings. There is a rule on this committee in terms of having testimony 24 hours prior. Regardless of whether it was there last night, we have a rule about 24 hours having testimony. I just want to underline that point in terms of the administration, not only in this hearing but every other hearing. It is a matter of importance that people take time, and I think it is important just to have it underlined.

Senator PELL. I appreciate the suggestion of the Senator, and he is quite correct. We did not get the Secretary's testimony until this morning. I think we had other testimony as of close of business last night. That was also a bit late.

Secretary Cavazos, I think the respect that we all have for you is tremendous. We know you are a friend of education, and we will be very interested in your testimony. Would you proceed please?

STATEMENT OF HON. LAURO F. CAVAZOS, SECRETARY, U.S. DEPARTMENT OF EDUCATION, WASHINGTON, DC, ACCOMPANIED BY EDWARD C. STRINGER, GENERAL COUNSEL, AND LARRY OXENDINE, DIVISION OF POLICY AND PROGRAM DEVELOPMENT, OFFICE OF SECONDARY AND POSTSECONDARY EDUCATION

Secretary CAVAZOS. Thank you very much, Mr. Chairman. I have submitted for the record a rather lengthy statement already so that will go in there, but I am going to read another statement that in itself is lengthy because of the complexity of this issue, if I may, sir.

Mr. Chairman and members of the subcommittee, we are here this morning, of course, to discuss a very serious situation, and that is the vicarious financial condition of one of the Nation's largest guarantors of the Guaranteed Student Loan programs. The department's highest priority at this time is to resolve this immediate problem and to take steps to ensure the stability of these important student aid programs. We must also review what caused this guarantor's failure and learn the lessons that will help us avoid such problems in the future.

With me this morning is my general counsel, Dr. Ed Stringer, whom I have asked to walk us through very, very quickly the general structure of the Guaranteed Student Loan program. With your permission, Mr. Chairman, I would like to proceed in that direction.

Senator PELL. Certainly.

Dr. STRINGER. Mr. Chairman and members of the subcommittee, at the risk of oversimplifying a very complex structure, I thought it might be helpful to take you through this just to see the flow of paper and funds starting from the point where a student decides to seek a postsecondary education through a loan down through the Federal Government.

It starts when the student decides to make that loan and to attend an institution. That student goes to a lender, obtains the loan. The lender then either retains the loan or sells it into the secondary market.

If the student defaults on that loan, the loan is submitted by the lender to the guarantee agency. That is the level that HEAF operates at. If the guarantee agency determines that the loan has been properly administered with due diligence, the guarantee agency will pay that loan on that guarantee 100 percent.

The guarantee agency will then turn to the Federal Government as a reinsurer of the loan, and if again the due diligence has been done on that loan in the collection efforts, the Federal Government will pay the guarantee agency the amount of that loan, depending upon the guarantee agency's then default rate. As the Secretary will explain in his testimony in just a minute, that default rate can penalize that guarantee agency up to 20 percent of that loan.

That is a very simple overview of how the system works.

Senator PELL. Thank you very much, indeed.

Mr. Secretary.

Secretary CAVAZOS. Now, let's take a look at HEAF's situation and why is it failing. Under the Guaranteed Student Loan program administered by the department, HEAF operates as, of course, the designated guarantor for Minnesota, West Virginia, Kansas, Nebraska, Wyoming, and the District of Columbia. It also operates as national guarantor insuring loans in other States where a different agency is the designated guarantee agency. In 1989, HEAF insured loans worth $1.8 billion made by 1,147 lenders.

It is clear that HEAF sought to be a large volume, national guarantor of student loans. In the mid-1980's, HEAF held a large percentage—almost 65 percent—of its portfolio in loans to proprietary school students. These loans have a higher default rate than loans to students in other sectors. Thus, the portfolio of loans guaranteed by HEAF has a proportionately high default rate.

Under current law, at the beginning of a fiscal year, a guarantee agency is reimbursed at 100 percent, and the rate declines to 90 percent or 80 percent, depending upon the agency's annual default rate. With its high default rate loan portfolio, HEAF was paying out 100 percent for its lender claims but was receiving only 90 percent or 80 percent reimbursement from the Federal Government. This, of course, ultimately caused a serious cash flow problem for HEAF.

HEAF realized the problems with its portfolio mix and tried to correct it. It discussed with us a number of options to alter its portfolio. However, these options would have violated the Higher Education Act. Finally, in 1988, HEAF withdrew as a guarantor in 18

States. The proportion of proprietary school loans in its annual portfolio dropped from 59 percent of its annual loan volume in 1988 to 35 percent in 1989. Despite the attempts to reshape its portfolio, HEAF still hits the 80 percent reinsurance trigger—as a result of the earlier portfolio mix still being presented as default claims. Also, we now know that when HEAF withdrew from the 18 States, it lost a significant proportion of its loan volume, for which it receives guarantee fees from its lenders. Thus, while its costs were still high, HEAF lost substantial revenue. Four weeks ago, the Department of Education was notified by HEAF that it was facing serious financial problems and soon would be unable to pay default claims presented by lenders.

The Department of Education, in conjunction with OMB and with the assistance of outside consultants, is closely monitoring the situation and is developing options to resolve the matter. Last week we sent a nine-member team to HEAF's headquarters in St. Paul for a firsthand assessment of HEAF's operation. HEAF was cooperative throughout the review, and we anticipate the continued cooperation. This week, staff from the department's inspector general's office are on site at HEAF headquarters conducting an independent review of the agency's operation. We are intensely involved in sensitive discussions with other organizations that have an interest in and capacity for assuming all of HEAF's guarantee functions. I am not at liberty to disclose specifics about HEAF's deliberations, but I want to assure you that we are committed to putting in place a solution that will ensure that new loans are made and insured without interruption and that the existing HEAF portfolio is properly serviced, collected, insured, and reinsured.

The department has made its position clear in a public statement and with the Congress. Let me repeat our position here. HEAF's problems do not threaten the integrity of the Guaranteed Student Loan program. While we take these problems seriously, analogies of this situation—your question, sir—to the savings and loan crisis are quite simply inappropriate. They just don't apply. We do not expect that HEAF's problems will be replicated, and I see no need for a Federal rescue of guarantee agencies in general or HEAF in particular.

We expect to resolve this matter in a manner that: one, minimizes the cost to the taxpayers; two, assures orderly management of the HEAF portfolio; and, three, contributes to a stronger student loan program. As I have indicated previously, this situation will not affect the ability of students to obtain loans, of lenders to make those loans, or guarantors to insure those loans. The department is also monitoring other guarantee agencies with a particular focus on their financial strength. This, too, is being done to ensure the long-term stability of the GSL program.

In the larger sense, HEAF's current situation is related to and is a particularly accurate example of the nationwide problem of student loan defaults and the high concentration of defaults in the proprietary school sector. It is possible that HEAF acted imprudently by aggressively pursuing guarantees in that sector. But it is HEAF's view that it was acting consistently with the purposes and requirements of the Higher Education Act. We are carefully examining whether there also may have been other practices that contributed to HEAF's problems.

In order to understand better the serious problems that massive loan defaults yield in a case like HEAF, we must take a look at the individuals behind those defaults. Who defaults? What do we know about student defaulters? We know that borrowers from low-income families are more likely to default than high-income borrowers. We know that many borrowers default because they do not enter jobs with incomes high enough to repay their loans. This is especially true for students in short-term programs who drop out before completing the programs but still have that debt to repay. Far too many students are not academically prepared for postsecondary education. Too many, particularly in short-term programs, drop out before completing their program.

In the future, our Federal student aid programs must continue to serve students in both long- and short-term programs. I have said that repeatedly. But we must reduce the possibility that students will drop out or default. In doing so, we will ensure access to educational opportunity, shield the student borrower from the serious consequences of default, and protect the Federal taxpayer from the escalating costs of defaults. This must be done to restore public confidence in all of our Federal aid programs.

We have already begun this task. Shortly after becoming Secretary in 1988, I sought the views of the entire postsecondary community—this is within the first month after I was on the job—on the best way to reduce student aid loan defaults. I believe that the public should have a full opportunity to comment on default programs. I believe that before we proceed, the public should have final regulations, and I received over 1,200 responses.

These regulations were published June 5, 1989. They carefully balance the responsibility of educational institutions for reducing defaults with the reality that we cannot make the problem disappear overnight. We must acknowledge that a large percentage of student loan defaults are concentrated in a relatively small number of schools. For example, in 1988, of the 2,143 proprietary schools, 20, only 20, were responsible for $175 million in defaults, or 25 percent of all proprietary school defaults that year. That shows you the narrowness of that problem.

The department is also taking other regulatory and administrative steps to address abuses. We have increased staff devoted to monitoring schools as well as a number of program reviews. Regulations are being proposed to deal with schools that inflate their estimate of the quality of education provided and address the conditions under which branch campuses may be eligible for the student aid program. In addition, by Monday, regulations will be published authorizing emergency actions to revoke the eligibility of schools for serious abuses. I expect that these regulations will be effective in late September, and we will promptly move to suspend any institution that we have good reason to believe is in substantial violation of the program requirements. In addition, we will shortly take action to strengthen procedures for eligibility, accreditation, certification, and licensure.

While these provisions cannot be expected to produce instant results, I believe that in combination with our legislation proposals, they represent a solid foundation that will not only protect the taxpayer but will protect the student from the unfair consequences of default.

In conjunction with the default initiative regulations, on June 30, 1989, the department submitted to Congress its legislative proposal, the "Student Loan Default Reduction Amendments of 1989." This legislation is designed to strengthen accountability in student aid programs, both for individuals and institutions. Two of the provisions of the department proposal—clarifying the Secretary's emergency action authority in denying Title IV eligibility for 24 months to an institution that has lost its accreditation—have been enacted due directly to the efforts of this subcommittee. In addition, S. 695, the Educational Excellence Act which was passed by the Senate earlier this year, contains provisions from our initiating prohibiting the employment of commissioned recruiters. We deeply appreciate your support in that area.

Our default initiative, however, is just the beginning. We have an opportunity to accomplish much with our objectives.

For the past 13 months, the department has been carefully evaluating the Higher Education Act in order to propose a comprehensive reauthorization. And we have received a lot of testimony, public comment, and we have identified problems within the act, within our postsecondary education programs, and within the system of postsecondary education.

We know that studying problems is not going to take them away. We must do far more than just simply ensure access. We must ensure and provide quality education. This means the States, accrediting agencies, and the Federal Government must do more, individually and together, to make sure that only truly high quality programs participate in Federal student aid. We must ensure that students do not enter low quality programs only to drop out, or graduate from poor quality programs to enter low paying job carrying a large loan debt. We are looking at a package of new authorities for the department that will give us stronger power to act in the case of a guarantee agency failure, as well as addressing some of the underlying cause of the HEAF situation. These may include closer oversight of financial structure of the guarantee agency, a system of providing reinsurance and other authority to address the cause of high default. In our reauthorization proposal, you will see a package of measures addressing licensure, accreditation, and eligibility.

Perhaps in the pursuit of our worthy goal of providing our neediest students "access" to educational opportunity, we have not fully faced the more difficult tasks of promoting retention, graduation, and achievement. As a result, many students have had access only to academic failure and default. We should open doors of educational opportunities only if they lead to achievement and a quality education. If this is the hard lesson that we have learned because of the problems of HEAF and what is happening there, we could not be learning them at a more propitious time as we approach the Higher Education Act reauthorization. I look forward to working with you, and I certainly will be pleased to answer questions. I understand, of course, that you have to go vote.

Senator PELL. Thank you very much, indeed. We have to recess the committee for about 15 minutes to participate in a roll call vote. The hearing is in recess.

[Recess.]

Senator PELL. The Subcommittee on Education, Arts, and Humanities will come to order again.

We will limit ourselves on the Senate side to the 10-minute rule. I will start out the questioning, if I may.

Reiterating the question I asked earlier, is there a relationship between the S&L crisis and this? I realize they are different areas, but I think in people's minds, there may be a similarity. I was wondering what your thought was, again. I recognize you touched on it in your testimony, but I think it would be helpful if you once again let us know whether you thought this was another S&L crisis.

Secretary CAVAZOS. Mr. Chairman, there is no way in the world that one can compare this situation with the savings and loan crisis. There absolutely is minimal risk to the taxpayer here. We are guaranteeing the loans. So we can't compare it in any way at all. I would like to dispel that notion at this moment.

Senator PELL. I agree with you from a substantive viewpoint there is no comparison. But some of the elements of the lack of faith in the Government guarantee could creep into it, and that is what we are worried about here.

Secretary CAVAZOS. Well, I think certainly here the guarantee that has been built in is one that provides for a good loan system to get these moved out and assures the students who perhaps have an excellent credit rating or have no history of credit rating will have loans made to them. As part of that, of course, is that loan guarantee, and I think that that is an important component of this effort. Certainly, even the loan guarantee is structured so that it spends down in terms of the amount of repayment to the Federal Government if due diligence is not pursued or the job is not getting done. So there is absolutely no comparison at all.

Senator PELL. I am very concerned about the process by which the schools become eligible to participate in the programs. Clearly, too many bad schools are seeping through the cracks. Do you believe you need stronger legislative language to crack down on the accreditation, eligibility, and certification purposes?

Secretary CAVAZOS. Mr. Chairman, you have hit exactly in the area that I intend to put a lot of emphasis, higher ed reauthorization. I think that, to me, the approach has to be in that direction. I have had a lot of people say right off the bat, well, you need to exclude the proprietary schools, then you wouldn't have the problem, or you need to move the proprietary schools to another unit.

I have consistently maintained that proprietary schools provide, in many cases, excellent education and a greater opportunity. The problem is, of course, that there are some bad ones out there that we need to get rid of. And my tactic has been and will be—and I will be working with the Senate when we come through here with our higher ed reauthorization next year—to look at the whole issue of accreditation, licensure, and certification. I think that is the key. Part of our problem is we have some accrediting agencies out there that are not doing the job, and the States are going to have to work with us because certainly the States also do licensure and then we certify. So that I must say that, to me, the best approach is not to say, well, let's just eliminate all the proprietary schools. I feel very strongly about not doing that, but I think that what we can do is approach it, therefore, through the accreditation issue.

I have put the accreditation community on notice to that effect that we are going to be coming in there pretty hard.

Senator PELL. I agree with your thoughts. Proprietary schools are what are called taxpaying schools. Many of them do an excellent job, indeed, and fulfill a very real need. But as I understand your reply, your thought is there is further legislative language that would be necessary.

Secretary CAVAZOS. Yes, it is. There is quite a bit necessary, and we will be working with you people to work that through and make sure that we have something that is operative. I think that is the obvious approach to me. We talk about access. The key is access to what? Access to a quality education. And if you have good accreditation systems in place, then that will happen. But at the present time, we cannot be looking at them in terms of quality, only in terms of resources.

Senator PELL. For the shortfall, from now, today, until this new legislation is enacted, which will probably be about a year—looking at the normal course of events—do you feel that the resources of the Government are adequate to prevent the complete breakdown of HEAF?

Secretary CAVAZOS. Oh, no question about it. We will continue on in a very positive sense. What we are doing now, of course, is assuring that those lenders will be repaid, that loans will be properly serviced, so that I am not concerned about that aspect of it at all. However, I expect that we will be able to resolve the instant problem that we have in front of us now, designating a successor guarantee agency without needing new legislation. So that I think that we have that in place. I want to get back a little bit, of course, to the issue of accreditation again. Because of the new authority that you granted in terms of suspension, we will be able to be looking at that. So we have a variety of things we can do between now and reauthorization.

Senator PELL. Actually, I remember pressing at the time that we should knock out automatically schools with higher than a 25 percent default rate, and I was in too much of a minority.

In 1987, when your predecessor testified before us, you had gone from 1,977 program reviews, in 1981 to about a half by 1986. What have you done to turn the situation around now so we have more departmental reviews?

Secretary CAVAZOS. I am trying to find my numbers on that. We are doing more in that entire area. For example, in program reviews by the guarantee agencies, the lenders, we did in 1990 already to this time 505. Last year it was 919. In terms of the lenders, we have done a total across the last 3 years 1,300.

I must also point out, though, that we have continued to fight the battle of more S and E as we get more programmatic responsibility in the department. We now have about 207 discretionary programs that we have to operate. We have not seen an increase—significant increase, I might add—in S and E's, and we really need to continue to get those out there. I have been quite vocal in trying to get more support for our people in that area. I am optimistic we are going to turn that around.

Senator PELL. Without objection, I will insert in the record an analysis of the program review activities showing how the number of reviews conducted declined just as the need increased. I look forward to that being reversed.

[The report follows:]

PROGRAM REVIEW ACTIVITIES

Institutional Reviews

Fiscal Year	Reviews Conducted	Recoveries
1981	1,058	$16,412,694
1982	510	4,387,280
1983	648	5,877,265
1984	721	11,661,319
1985	763	6,955,832
1986	417	2,505,485

PROGRAM REVIEW ACTIVITIES

Lender/Guarantee Agency Reviews

Fiscal Year	Reviews Conducted	Recoveries
1981	919	$9,276,325
1982	812	10,612,995
1983	783	6,919,392
1984	773	7,506,799
1985	685	3,274,784
1986	473	1,696,217

Senator PELL. My time has expired. I have some questions I will ask for the record.

I will now turn to the ranking minority member, Senator Kassebaum.

Senator KASSEBAUM. Mr. Secretary, first, I would just like to share with you a letter that I received yesterday from a banker in Kansas, which reads in part: "There have been a number of questions which have risen lately concerning student loans at the Leavenworth National Bank, which the Leavenworth National Bank holds. My board is desirous of receiving some type of documentation showing that these loans, while guaranteed by HEAF, are, in fact, in the event of their default or bankruptcy, guaranteed by the Federal Government."

I guess I would wonder how I should answer that letter.

Secretary CAVAZOS. Actually, the guarantee that we have from the Federal Government is to the guarantee agency. The guarantee agency has a guarantee, of course, to that loan, the person who has put out the loan. And I would really be—in my job you have to be optimistic, that we will have in place in a short period of time, Senator Kassebaum, the mechanism to make sure that those loans that have been guaranteed will continue to be guaranteed and, therefore, repaid should they come into jeopardy. So I would respectfully suggest that when you write back that these things will be fulfilled.

Senator KASSEBAUM. Thank you very much.

I have a lot of confidence, as a matter of fact, that, indeed, that will be the case. There have been a lot of comparisons with the student loan default situation and the savings and loan situation, and that is just not a good comparison. But, as you have expressed, there are some changes that need to be made.

There has been a lot of talk in some of the opening testimony about grants versus loans. I think the Senator from Minnesota made a good point regarding loans. But 10 years ago, grants made up two-thirds of the student aid package. Today, loans comprise from about two-thirds to three-fourths of a student's package. So it is a greater responsibility, of course, that a student has. I don't know what the figures are as far as comparable costs to the Government, and perhaps those figures might be available. Either way, my guess is it is almost a tradeoff.

Secretary CAVAZOS. I suspect it is very, very close to that.

Senator KASSEBAUM. I think that what one gains from recognizing that there is a responsibility. What I think it is most unfortunate is that we have encouraged students many times to assume an indebtedness that they should never have really assumed in the first place.

Secretary CAVAZOS. That is right.

Senator KASSEBAUM. I know that you are concerned about this. I think there are things that are being recommended or that are already in place that eventually will make a difference. Regarding the system itself, I find it troubling, as it exists right now, that a guarantee agency such as HEAF really becomes the lender of last resort. They cannot turn down loans in which there might be a question. So immediately they are placing themselves in some jeopardy. Is that not correct?

Secretary CAVAZOS. That is correct. That is correct, Senator.

Senator KASSEBAUM. When they have that responsibility and when we have required them by law to assume it, then it seems to me we do have a responsibility for resolving the situation—at least by recognizing that we have to look at the "open sesame" situation we have today. I think we do a disservice to students, as a matter of fact, if we saddle them with a debt which either they are just simply going to ignore or which hangs over them for years, and on the other hand if we require a guarantee agency to take on the questionable loans.

I would also say that I am troubled by the fact that institutions with high default rates which have received notice and/or are denied by the guarantee agency further loans can go elsewhere. There is nothing at this point, other than your closing them down, that really means the practice stops. Is that not correct?

Secretary CAVAZOS. Well, I think we are putting in place a variety of mechanisms that will help close them down earlier, or to certainly address it. Part of the problem that we have done in the past is that we have not involved the school in some effort in terms of the student loan. They have always said, well, that is between the lenders, the guarantee agency, and the student. The school has no responsibility.

When I came into the job a couple years ago, I took quite the opposite tack, that the school does have the responsibility to counsel those students and to let them know what they are getting themselves into relative to the issue of loans. And so last year we published new regulations targeted at each level that really involved the schools. And we were able to cut off some funding into some of these schools. They now have default management plans and how they have to pull those numbers down. And for the first time, we have gotten one of the key players back into—not back into it, it was never in it—into the loops, and that is going to make a difference because then that will let us get at those bad schools that you talked about, Senator, that we can close down.

Senator KASSEBAUM. Well, but some of them just keep coming right back.

Secretary CAVAZOS. They have moved down the street and changed their name and start over again.

Senator KASSEBAUM. I guess, then, I would ask: What responsibility and oversight does the Department of Education have? And what, as a matter of fact, have you done to assure that a situation such as HEAF will not happen again?

Secretary CAVAZOS. I think basically the main thing that—there are two parts to that question. One, what do we do about schools that close down and move about and change? And I talked earlier about the whole issue of accreditation, how that whole system needs to be tightened down so we can get rid of the bad schools through the accreditation system and licensure and certification.

The second one that we did, we can get rid of our bad schools, unless they pull down their default plans in terms of support to the guarantee agencies, certainly I think that the main thing we can do there is to help them through audits and management plans. We have been doing that, I believe with some diligence within the department.

Senator KASSEBAUM. Well, I think so, and sometimes these results are slow in coming.

If I may just ask one further question, Mr. Chairman, it is one that I asked at last week's hearing of the Banking Committee on this issue. HEAF had requested permission from the Department of Education to drop some of their questionable loans.

Secretary CAVAZOS. Yes.

Senator KASSEBAUM. Some of the things that they had requested, I assume would have made their portfolio a more solvent portfolio but were denied by the Department of Education?

Secretary CAVAZOS. Yes.

Senator KASSEBAUM. Can you explain that?

Secretary CAVAZOS. Yes, I will point that out, Senator, because HEAF proposed to, one, stop guaranteeing loans for certain schools. That proposal would violate actually one of the laws on this. It is required to do that by law. They also proposed requiring cosigners on student loans for students at some school. That proposal also violates another one of our laws. Finally, they want to stop guaranteeing loans for certain lenders, and that also is in violation of our laws. I can go into great detail about those, but actually that is the way that the law is written, and we had to respond negative. I want to make that point. That is a very important point, and I am pleased that you brought it up.

Senator KASSEBAUM. Again, because of being the lender of the last resort, they really have no recourse.

Secretary CAVAZOS. They have no recourse at all.

Senator KASSEBAUM. I think we need to take another look at some of the laws and the way they are written.

Thank you, Mr. Chairman.

Senator PELL. Thank you very much, Senator Kassebaum.

Senator Kennedy.

The CHAIRMAN. Thank you very much, Mr. Chairman.

Secretary, can you give an ironclad guarantee to every eligible student and their family and assure them that those that are eligible to receive the loans will receive them this fall?

Secretary CAVAZOS. Yes.

The CHAIRMAN. Are you requesting any additional legislation here at this hearing to permit you to deal in a responsible way with the financial difficulties of HEAF?

Secretary CAVAZOS. Mr. Chairman, at the present time, we are not seeking legislation. We think we can resolve this issue within the next couple of weeks. It is imperative that we do that. We want to get it done, and we will do it.

However, that doesn't mean that in the higher ed reauthorization we are not going to come back in here with a lot of changes to this whole system. I must point out to everyone here that that act now is 25 years old. I looked at it, and, very frankly, it has so many components to it that perhaps have some issues in there that need to be readdressed.

What I did 14 months ago, I started the department working in this whole area. I said just get yourself a clean piece of paper and start all over again. Forget the current one. What would be the ideal one? And we have been working with the people at Dupont Circle, and in the administration to get this worked out. We have had field hearings so that subsequently, yes, Mr. Chairman, we will have to be coming back with new legislation.

The CHAIRMAN. I know Chairman Pell and others look forward to working closely on this with me, and we can't get started too early on it.

How often did you audit HEAF?

Secretary CAVAZOS. It is audited every 3 years. It was audited in 1988. The 1988 audit showed that they were not in serious problem at that time.

The CHAIRMAN. Just every 3 years?

Secretary CAVAZOS. Yes.

The CHAIRMAN. The last audit was 3 years ago? Was it prior to the time that we understood that there is a crisis?

Secretary CAVAZOS. December of 1988 was the last audit.

The CHAIRMAN. Have you formed any opinion whether there ought to be closer oversight to not only HEAF but to the other guarantee agencies?

Secretary CAVAZOS. I guarantee you, Mr. Chairman, that if I can find at least one silver lining out of the problems that we have in front of us, it is the fact that we are going to have to work much harder to make sure that this doesn't happen again. There are a lot of guarantee agencies out there, and in terms of having the personnel to audit extensively, we find when you are dealing with the number of guarantee agencies that we have, it is not easy to get it done soon. But we are going to put a hard press on it to make sure it doesn't happen again.

The CHAIRMAN. Given the financial difficulties at HEAF, have you ordered an auditing of all the other guarantee agencies?

Dr. STRINGER. Senator, we have in place now a team that is going to be doing intensive audit work on all other guarantee agencies.

The CHAIRMAN. Is it the same policy for the other agencies to be audited every 3 years?

Dr. STRINGER. Yes, that is the policy. It should be kept in mind that the department does not have financial oversight authority with respect to the guarantee agencies.

The CHAIRMAN. But you can certainly audit those, can you not? You have the authority to be able to audit those?

Dr. STRINGER. That is right.

The CHAIRMAN. I am trying to get some feel as to what is being done. Can you give us the financial conditions of these other agencies?

Secretary CAVAZOS. If I may, Mr. Chairman, I could ask Larry Oxendine from our staff, who deals with that specific area, to address that.

The CHAIRMAN. Fine.

Mr. OXENDINE. Thank you, Mr. Secretary.

The CHAIRMAN. Give me your name and position.

Mr. OXENDINE. Yes, sir. I am Larry Oxendine, and I am the director of the Division of Policy and Program Development within the Office of Postsecondary Education. I am in the office that is responsible for regulating the guarantee agencies.

We do perform audits of guarantee agencies, program reviews of guarantee agencies. The last one that was performed of HEAF was in 1988. We have a policy in place right now where we will be performing these reviews every 2 years, but in addition to the reviews that are performed by the Department of Education, we also receive independent audits of the guarantee agency CPA firms every 2 years. In addition, we receive extensive financial information and programmatic information from the guarantee agencies on a quarterly basis, a former we refer to as the guarantee agency quarterly report. And then at the end of each year, we receive even more extensive information from the guarantee agencies in the annual reports. We receive a great deal of information from the guarantee agencies which we can use to determine the condition of the agency.

The CHAIRMAN. And what assurance can you give us this morning, with all that information, about the condition of the other guarantee agencies?

Mr. OXENDINE. I can give you an assurance that all of that information is reviewed within the department of——

The CHAIRMAN. I am asking about their financial stability. What can you tell us about it?

Mr. OXENDINE. I can give you an assurance that there is no other agency in existence at the moment that is having financial troubles that are similar to the HEAF financial problems.

The CHAIRMAN. Similar? Let's leave the word "similar" out. Do I gather from what you are saying that the other agencies are financially stable?

Mr. OXENDINE. Yes, they are.

The CHAIRMAN. How many people do you have in your department that are reviewing this information on the various agencies? How many people in the Department of Education?

Mr. OXENDINE. The information that is submitted to the Department of Education, we have approximately nine people reviewing that information.

The CHAIRMAN. Excuse me. Could I hear that again? How many people?

Mr. OXENDINE. The people in the department to review the reports that are submitted, we have approximately nine people.

The CHAIRMAN. As I understand it, last week at the Banking Committee there was indication that five to seven of the other agencies were in some financial difficulty.

Mr. OXENDINE. There are five to seven other agencies that we are watching closely. I would not say that they have financial difficulties. They are in a position where they are able to pay their bills. We don't expect any serious problems from those agencies, but they are being watched closely.

The CHAIRMAN. Well, I hope that you share that information with the chairman of the committee and others as to the progress that is being made.

Thank you very much, Mr. Chairman.

Senator PELL. Thank you.

Senator Jeffords.

Senator JEFFORDS. Thank you, Mr. Chairman.

Mr. Secretary, I would like to ask you about your testimony as to your assurances that you were capable of taking care of the HEAF matter. In 1988, I included a provision in the House student default initiative to mandate that the Secretary conduct a study relative to appropriate actions to take in the event that a guarantee agency becomes insolvent, and clearly defined the Federal Government's role in such an event. I did that; of course, this bill was never enacted, but it seems to me the law is rather unclear on these issues.

I would like you to clarify for me as to what you can do in the event of a default of the guarantor agency and whether or not the Government is a backup. I don't believe there is any full faith in the Government which assures that money would be forthcoming. How do you anticipate taking care of that? And what responsibility, if any, or authority do you have with respect to the lenders in that event?

Secretary CAVAZOS. First of all, let me point out that the department has no legal responsibility for HEAF's guarantees. However, we are acting to ensure that HEAF's guarantee functions are continued and that the department will continue to reinsure both existing and expected loans. We are looking at all of that. But if HEAF is failing to meet its responsibility as a guarantee agency, the department can terminate its agreement and enter into another agreement with another agency. We expect cooperation from HEAF in arranging for a smooth transition to a new guarantor if that opinion becomes necessary. The department is not, as a matter of law, responsible for paying lenders' claims. Our legal responsibility is only to pay reinsurance to the guarantee agency if it pays insurance to a lender on a defaulted loan.

However, the department is pursuing options to ensure that existing and new loans continue to be insured, and the department continues to pay reinsurance. So our entire efforts will be devoted over the next week or two, therefore, to putting in place that mechanism for someone to take over, if necessary.

Senator JEFFORDS. I think the question that we have, and I guess the taxpayers would, is: What authority or what responsibility does the lender bear in these circumstances? And is this a situation where there could be a requirement for a taxpayer bailout in the sense of any legal authority for that? And, third—I shouldn't add a third one so quickly, but what power do you have to reassign defaulted loans to other agencies, or loans to other agencies that may or may not be in default?

Secretary CAVAZOS. In terms of the legal aspect of that, Ed.

Dr. STRINGER. Senator, your first question relating to the lenders, what are the responsibilities of the lenders, the responsibility of the lenders relate to doing due diligence on any loans that they have issued to the students, and to timely submit those loans to the guarantor agency if they go in default. The lender has no direct responsibility to the Federal Government, and the Federal Government has no direct responsibility to the lender.

Senator JEFFORDS. But what happens if they don't use due diligence? What is the authority?

Dr. STRINGER. Then the guarantor agency is not authorized to guarantee that loan.

Senator JEFFORDS. Well, isn't the loan already guaranteed at the time where due diligence might be a part, or not?

Dr. STRINGER. If a loan goes in default, it remains in default with the lender for some period of days, 180 days I believe it is, and it is then submitted to the guarantee agency. There must be evidence that that lender has done due diligence in attempting to collect on that loan during that time period.

Senator JEFFORDS. And if he has not?

Dr. STRINGER. If he has not, then the guarantee agency does not guarantee that loan. That is the lender's loan at that point.

Senator JEFFORDS. Thank you. And the other questions?

Dr. STRINGER. As to the third—I remember your third question.

Senator JEFFORDS. Well, try that one.

Dr. STRINGER. Having to do with the authority of transferring loans and guarantees.

Senator JEFFORDS. Yes.

Dr. STRINGER. That can be done only at the consent of the Federal Government.

Senator JEFFORDS. Not the agency to which you are transferring it? Do they have a consent——

Dr. STRINGER. Well, certainly the agency—I would assume that the agency that is receiving the transfer would have agreed to it. But the transfer cannot be done without the department's consent.

Senator JEFFORDS. And then presuming also that it can't—you can't order it to be done then, is what I am getting at.

Dr. STRINGER. That is correct.

Senator JEFFORDS. Thank you.

Senator PELL. Thank you very much.

Senator Simon.

Senator SIMON. Thank you, Mr. Chairman.

First, when we talk about defaults—and I don't like them any more than anyone else—what we are saying is there are no short-term payoffs. For example, someone who obtains 2 years of college education may not be able to pay that loan right now doesn't mean that in the long-term society hasn't benefited from this investment.

Second, and I realize the problem you face here, Mr. Secretary, I do think there is a difference in the default rate, if I may pick on my colleague from Massachusetts here, for a Harvard and, say, a privately controlled community college on the Pine Ridge Indian Reservation where there is a 73 percent unemployment rate.

Secretary CAVAZOS. Yes, sir.

Senator SIMON. You cannot expect to apply the same standard across the board. It seems to me that a uniform standard does not make an awful lot of sense.

Now, in your statement, Mr. Secretary, you say, "We all must do far more to ensure that the institutions to which students take their Federal student aid dollars will provide a quality education." In response to Senator Pell and Senator Kassebaum, you talked about accrediting. Is this how we do this? And if I can be more specific, you mentioned a startling statistic I hadn't heard before; 20 out of more than 2,000 proprietary schools——

Secretary CAVAZOS. It is 2,140 proprietary schools.

Senator SIMON. Twenty out of 2,140 proprietary schools are responsible for 25 percent of the defaults by the proprietary schools.

Secretary CAVAZOS. Yes.

Senator SIMON. Are those 20 schools providing quality education?

Secretary CAVAZOS. Part of the issue here comes back to the accreditation thing. If they are accredited—that means accredited by a recognized accrediting agency, and there are, very frankly, some pretty bad accrediting agencies out there. They are given a license by a State; we certify them.

Now, what I am going to try to do is to tighten up that whole sequence there, and I am going to have to have the States' cooperation to do that because this is not just a Federal part. We have been able to get into legislation—and it has been passed—that one of the problems we would have is a school would lose its accreditation. Well, now you won't be able to get a guaranteed student loan, but they go down the street and find themselves another accrediting agency to accredit them. There are some startling numbers of just some of these accrediting agencies, a number of the proprietary schools that they accredit.

To put it into view here, Senator Simon, it is that about 35 percent of the loans that are out there now are to students in proprietary schools, but they account for 70 percent of the defaults, approximately, that we have out there. I want to get back to your other point when you were comparing Harvard to the community college. You are right, there is a tremendous difference between that when we talk about the percentages of default. That is why I was being very, very sensitive to the issue that you just now brought up.

Last year, when we proposed our new regulations, we did a step procedure on it requiring certain activities. We don't require anything as long as the school's default rate is below 20 percent. But once it goes over 20 percent, say to 30 percent, default management plans, and we have now 1,200 default management plans that have been submitted to our department that we are reviewing at the present time. Going to that into the next step, 30 to 40 percent, we can now delay disbursement of the loans to first-time buyers, which is very, very handy because we have to wait 30 days, and by that time they have dropped out, unfortunately; and also require a pro-rata refund from the proprietary schools up to a certain level of time.

Being sensitive to the issue that you brought up, rates for schools above 40 to 60 percent, people came to me and said, well, we just ought to cut them off at some point. Well, what we have done here is we have delayed certification, a pro-rate refund policy, and they have to bring their levels down at a given rate. We even go as far as 60 percent and require all of these default reduction measures I have mentioned—refund policy, we could delay disbursement. In other words, even at 60 percent, we don't just say you can't——

Senator SIMON. I think I understand.

Secretary CAVAZOS. And I think that these regulations are the best regulations that we have ever had in place and will get the job done, because I was being very sensitive to the issue that you raised. There are some excellent colleges out there that have very similar troubles. We don't want to shut them down.

Senator PELL. Could we insert that information in the record?

Secretary CAVAZOS. Yes, sir. We will be glad to include that.

[The information referred to follows:]

RATES OF SCHOOLS

Rates that are 20 percent or below:

No action related to default reduction measures is required. All other regulatory requirements apply.

Rates that are above 20 percent but not above 30 percent:

DMP submission by 10/1/89 to the Secretary and principal guarantee agency.

Rates that are above 30 percent but not above 40 percent:

DMP submission by 10/1/89 to the Secretary and principal guarantee agency.

Delayed certification of loan applications and delayed disbursement of loan proceeds to first-time borrowers for loans certified after 10/1/89.

Pro rata refund policy for Stafford, SLS, and PLUS recipients whose last recorded date of attendance occurs on or after 11/21/89.

Rates that are above 40 percent but not above 60 percent:

Implementation of all Appendix D default reduction measures as defense to LST action in 1992. In effect, Appendix in school's DMP.

Delayed certification and delayed disbursement for first-time borrowers.

Pro rata refund policy.

Reduction of fiscal year 1990 rate by 5 percent from fiscal year 1989 default rate as a defense to LST action in 1992.

Rates above 60 percent:

Implementation of all Appendix D default reduction measure as defense to LST action in 1991. In effect, Appendix D is the school's DMP.

Pro rata refund policy.

Delayed certification and delayed disbursement for first-time borrowers.

Schools with fewer than 30 Borrowers:

Default rate will be calculated as a 3-year average. No action related to default management plan (DMP), *pro rata* refund, and delayed certification is required at this time. All other regulatory requirements apply.

Senator SIMON. And it does seem to me that if you see 20 proprietary schools that are responsible for 25 percent of the default problem, there ought to be a good look at these schools. Perhaps they are good schools. I just don't have any idea.

Secretary CAVAZOS. We have closed down a number of them already just this year.

Senator SIMON. Forgive me for not remembering your name, sir.

Mr. OXENDINE. Larry Oxendine.

Senator SIMON. You mentioned you have nine people to review the reports.

Mr. OXENDINE. Yes, sir.

Senator SIMON. Do you just assume that the reports that you get are accurate? How much do you feel it will cost, in terms of HEAF and other guarantee agencies that may have some problems?

Mr. OXENDINE. No, we do not assume the reports are accurate. As a matter of fact, we have a computer program that we run the reports through to do various edits for us and to make comparisons between the current quarter's reports and previous quarter's reports to make sure that there is consistency among the reports.

The reports that I am referring to are also used to make payments to the guarantee agencies, and we, of course, have to make sure that the information is accurate before we can authorize the payments. The administrative cost of loans, for example, we pay the guarantee agencies an allowance of 1 percent of loan volume, and we use these reports. So we do various edit checks, both through a computer system and manually to determine the accuracy of the reports. And we frequently have discussions back and forth with the agencies in correcting the data.

I didn't fully follow your second question, Senator Simon.

Senator SIMON. The second question is: What are we talking about in terms of losses to the guarantee agencies right now?

Secretary CAVAZOS. We would estimate less than $100 million, Senator.

Senator SIMON. If I may follow through, Mr. Secretary on the accredition issue, I remember when I was back in the House we had hearings on the accrediting process. Do you have a timetable for looking at this and saying here is what we are going to do?

Secretary CAVAZOS. Yes. I have already formed a task force within the department itself—in fact, I started that about a year ago—to work and to give us guidelines that we will have to have in our higher ed reauthorization to be very specific about improving the accrediting and licensure and certification procedure. I believe that all of us, very frankly, all of us share in the responsibility. It is a tough thing to say. I think that the whole Nation shares in that, that we have not done the kind of job that we should have done over the years. There are some excellent accrediting agencies out there. Don't misunderstand me.

Last year, at a major speech that I gave at the Southern Association of Secondary Schools and Colleges, which is one of the very finest accrediting agencies, I put them all on notice that I wanted their cooperation nationwide of the accrediting agencies to participate in this; because if they didn't participate, we were going to do it alone, and they would see some very, very tough rules coming down the road.

I remarked earlier that I have had people come to me and say, well, it is very, very simple, I know how to clean this up, why don't you just get rid of the proprietary schools, don't give them student loans. I don't agree with that. I have testified to that issue repeatedly over the last couple of years. I really believe that the best way to do this is to get rid of the bad ones. As you point out, there are only a handful of them, and we are going to go after them.

Senator SIMON. My time has expired. Thank you.

Senator PELL. Thank you very much.

I am getting a little bit nervous because we have Mr. Hawk, the head of HEAF, and also two panels of public witnesses. So we will have to roll on a little faster.

Senator Durenberger.

Senator DURENBERGER. Mr. Chairman, I will be as quick as I can.

Mr. Secretary, I want to begin with your answer to Senator Kassebaum's question regarding the Leavenworth banker. I understand that the Government has no obligation by law to pay the lender.

Secretary CAVAZOS. That is correct.

Senator DURENBERGER. But you have stated today that the Department of Education is going to insure the lender.

Secretary CAVAZOS. I am very, very confident, Senator, that in the next couple of weeks we will have a new guarantee agency or resolve this issue so that those loans will be serviced and they will be paid off. What I was talking about was the optimism that I really believe we are making progress.

Ed, you have been the main negotiator in that area.

Dr. STRINGER. We are optimistic, Senator, that we are going to reach a conclusion.

Senator DURENBERGER. That means that every banker, Leavenworth and all others, need not have to worry.

Secretary CAVAZOS. If they do due diligence on those loans.

Dr. STRINGER. I think that if I were the banker in Leavenworth, I would have a high level of confidence that their loans would be honored; at least the loans that follow through to the Federal Government level. What happens, obviously, on the due diligence side is their responsibility.

Senator DURENBERGER. Where does the figure $100 million in losses come from? Is that an estimate the Secretary gave in response to Senator Simon's question?

Dr. STRINGER. Yes, Senator, that is a top side number that we estimate at this time. There are a lot of unanswered questions, but in answer to the Senate Banking Committee question last week, that was the answer we gave.

Senator DURENBERGER. And the bulk of that comes from what source?

Dr. STRINGER. Costs of transferring the loan portfolios to the substitute guarantee facility.

Senator DURENBERGER. Is there any factor in there for the publicity implications of this? I don't want to draw a direct comparison between the reaction of a depositor in a savings and loan to the news that the savings and loan is in trouble, and the reaction here of a person who has an obligation under a loan saying, I think I will default on mine, too, and all of a sudden she starts spinning and we have a much larger problem than we anticipated. Is there some factor in your optimism and your figure $100 million for the potential of that happening?

Dr. STRINGER. No, there is no factor for that.

Senator DURENBERGER. I represent 800 people who have been working for HEAF in Minnesota, largely in the city of St. Paul. To the degree that the process of guaranteeing the stability of the guarantee behind the HEAF portfolio, might imply an arrangement with another guarantor, and that that arrangement might imply at some point in time the servicing of those loans somewhere other than St. Paul, I have a deep concern.

It seems to me that those loans having been generated out of St. Paul, and having been serviced by people in that city, that there is some value not only to the consumers involved but also to the acquiring guarantee agency of keeping that system in St. Paul. What can you say, Mr. Secretary, right now about what I can tell the 800 folks in St. Paul about the way in which the negotiation of HEAF's future might affect them. What can I say to the 800 folks in St. Paul?

Secretary CAVAZOS. I think that certainly the main thrust that we would do is we will work with them to do the best we can to make sure that it doesn't collapse. But if it does, then we have to provide and make sure that those loans are serviced. And so at this time, very frankly, it is a question certainly that I am sure that you are going to be getting into more and more as we worry about this issue. But our major job right now is to make sure that those lenders are back and those loans get out there to the students. The guarantee agencies, we have got to put in place the best mechanism that we have that will do that.

Senator DURENBERGER. But do you have a view right now, Mr. Secretary, in trying to determine the cost of servicing these loans, do you have a view that says that it is quite clear from your experience, that those loans can be serviced, even though you may change the management——

Secretary CAVAZOS. Yes, sir.

Senator DURENBERGER. Do you have the view that those loans can be serviced at a lower dollar cost by leaving them in St. Paul to be serviced rather than by lifting them up and moving them some place else?

Dr. STRINGER. I don't think we know that at this time, Senator. The proposals that we are looking at each provide for keeping those loan portfolios and those guarantee records in the HEAF organization for some time. Obviously, that is a decision to be made by whatever successor guarantee agency there is. There is a high level of sophistication in their computer program systems, but as far as cost of administering those in St. Paul versus another city, I don't know.

Senator DURENBERGER. Thank you.

Senator PELL. Senator Kassebaum.

Senator KASSEBAUM. Excuse me. I would just like to ask a follow-up question if I might, to perhaps clarify my own thinking and an answer I heard questions by both Senator Jeffords and Senator Durenberger. It seemed to me, Mr. Secretary, you indicated that there could be a new guarantee agency. I guess I am not sure why a new guarantor would solve the problem if you are moving bad loans, which at this point are only getting 80 percent reinsurance, 80 cents, say, on the dollar. Who is going to want that kind of loan?

Secretary CAVAZOS. When they come back on as a new guarantor, they will be back at a hundred percent for a 5-year period by law.

Senator KASSEBAUM. Well, Mr. Secretary, I don't understand that. Why would they do that? That seems to me certainly to be a bad credit risk.

Secretary CAVAZOS. That is the way the law provides for that.

Senator KASSEBAUM. That if it is moved to a new guarantee agency, it comes back on as a hundred percent?

Dr. STRINGER. That is what the law provides, Senator. But under the proposals that we are negotiating now, that is not the way it would work out. We are getting into some of the refinements of negotiation at the moment, so I would like not to get too far into this. But the proposals we have show out over time a very healthy loan portfolio of the successor agencies that we are dealing with. So from the standpoint of the illness of the HEAF portfolio at this point, blending it with a stronger portfolio can get them through this time period that HEAF cannot get through, given their situation at the moment.

Senator KASSEBAUM. I guess I will have to accept that answer, but I think it raises many questions about future problems.

Dr. STRINGER. It does, indeed. And that is one of the reasons why we are taking probably more time than a lot of people would have wished, because we want to be sure that whatever we do doesn't create another problem down the line.

Senator KASSEBAUM. Thank you.

The CHAIRMAN. Could I ask just one question?

You mentioned that part of the difficulty is with these accrediting associations. Can you tell us how many have been approved in the last 3 years?

Secretary CAVAZOS. I don't know that number, but we will get that number of how many have been approved in the last 3 years. There are 60 accrediting agencies in the United States. But I want to point out, though——

The CHAIRMAN. What I am interested in, Mr. Secretary, is how many have been rejected. Do you know how many have been rejected in the last 3 years? Could you get the information for the last 3 years, regarding how many have been approved and how many have been rejected? Have any been rejected?

Secretary CAVAZOS. I am not aware of any, Senator.

The CHAIRMAN. That is what the problem is. None have been rejected. It creates a concern. Why? I don't want to take more time, but if that is the problem, and you don't know any that have been rejected, why haven't they been? Why haven't some been rejected if they are the problem?

Secretary CAVAZOS. Because the accreditation element is one that involves the State level. They approve these accrediting agencies.

We recognize those accrediting agencies in turn. They give licensure, and we certify.

The CHAIRMAN. But you have power to approve them ultimately, don't you?

Secretary CAVAZOS. We can remove that, and that is exactly the point that I was making. I looked at this list and——

The CHAIRMAN. But none have been rejected?

Secretary CAVAZOS. None have been to date.

The CHAIRMAN. Thank you.

Senator SIMON. Mr. Chairman, just one brief comment. First, I think Senator Kennedy's question and the question that follows I think is clearly an area the Secretary and his staff ought to be taking a good, hard look at. And if you need additional powers, you ought to come to us and ask for those additional powers.

Second, all of us regret the kind of default costs—the $100 million—we are talking about. If the average default is $3,000—and I don't know what it is—that means 30,000 students have been helped. We are talking about $100 million or one-eighth of a B-2 bomber. We get nothing back from the B-2 bomber. Thirty thousand people have been helped, presumably, in the process. So we are not talking about complete losses for this country.

Thank you, Mr. Chairman.

Senator PELL. I just want to also understand one thing. Are you suggesting the creation of a new guarantee agency with a 5-year, 100 percent reinsurance to succeed HEAF?

Secretary CAVAZOS. No.

Senator PELL. You are not. OK.

Senator SIMON. But you can just shift these loans to a new agency and all of a sudden they are a hundred percent guaranteed?

Secretary CAVAZOS. By law you could.

Dr. STRINGER. We can do that, Senator, but this is a process that we are deep in negotiation on. We have the authority to do that.

Senator SIMON. I sure didn't know about that.

Secretary CAVAZOS. It is the way it is written.

Senator PELL. Thank you very much, indeed, gentlemen, for being with us.

Secretary CAVAZOS. Thank you, Mr. Chairman.

[The prepared statement of Secretary Cavazos (with attachments) follows:]

U.S. DEPARTMENT OF EDUCATION

Statement of

Dr. Lauro F. Cavazos

Secretary of Education

Before the

Subcommittee on Education, Arts and Humanities

August 3, 1990

Mr. Chairman and Members of the Subcommittee:

We are here this morning to discuss a very serious situation, the serious financial condition of one of the Nation's largest guarantors in the Guaranteed Student Loan programs. The Department's highest priority at this time is to resolve this immediate problem, and to take steps to ensure the stability of these important student aid programs. We must also take a very hard and serious look at what caused this guarantor's problems and learn the lessons that will help us avoid such problems in the future.

First, I would like to provide a brief history of the Guaranteed Student Loan (GSL) programs. The GSL programs include a number of different programs. The two most important of those programs for our purposes this morning are the Stafford Student Loan Program and the Supplemental Loans for Students, or SLS, Program.

Both are student loan programs in which private financial institutions provide capital that is loaned to student borrowers. In return, these institutions receive a subsidy from the Government to bring the interest they receive closer to a market rate, and the borrower's interest may be paid, or subsidized, by the Government at certain times. If properly serviced by the lender, these loans are guaranteed by State and private non-profit guarantee agencies against default and a borrower's death, disability, or bankruptcy.

As you know, the GSL programs began with the enactment of the Higher Education Act (HEA) of 1965. Prior to that time, a number of States had established their own loan programs to assist their residents with postsecondary education costs. All of these early programs were need-based, had various academic requirements for students, and had a variety of eligibility requirements for educational institutions.

Many students did not qualify for these loans, and these loan programs were available only in certain States. For these reasons and because of the increasing costs of postsecondary education, a nationwide guaranteed student loan program was enacted in the HEA. A separate, but similar, loan program for vocational students was consolidated into the HEA in 1968.

By the summer of 1966, the GSL program was operational throughout the country. A direct Federal Insured Student Loan (FISL) program served those States not served by an intermediary guarantee, or insurance, agency. Under the FISL program, the Federal Government directly insured the student's loan. The HEA did not provide enough incentives to encourage the creation of State and private non-profit guarantee agencies, and the FISL program covered most of the loans at this time. This situation continued until enactment of the Education Amendments of 1976, which made major changes to the HEA. Those amendments placed renewed emphasis on both the existing guarantee agency programs and the formation of new guarantee agency programs, through incentives such as new Federal advances, supplemental reinsurance, and administrative cost allowance payments, and by limiting the circumstances under which the FISL program could operate in a State.

The HEA now relies almost exclusively on private nonprofit and State guarantee agency programs. If a borrower defaults on a loan, the guarantee agency pays the amount of the defaulted loan to the lender. After paying the default claim, the guarantee agency comes to the Federal Government for reinsurance of the insured amount paid to the lender. Once the Federal Government pays reinsurance to the guarantee agency, the guarantee agency tries to collect on the defaulted loan and, if successful, keeps some amount of the money collected and sends the larger proportion to the Federal Government. The Federal Government, under a guarantee agency program, does not directly insure loans made by a lender.

In the 1976 Higher Education Amendments, an important provision, relevant to our discussion this morning, was added. This provision increased the rate at which guarantee agencies are reimbursed by the Federal Government for the insurance claims which they pay to lenders for defaulted student loans from a fixed rate of 80 percent. Now, a guarantee agenc·'s reimbursement, or reinsurance, from the Federal Government declines from 100 percent to 90 percent or 80 percent depending on the agency's annual default rate. If the yearly default rate on these loans reaches 5 percent, the Federal Government reimburses an agency for only 90 percent of the amount of reinsurance claims paid during the remainder of that year. If the default rate on the loans in repayment goes over 9 percent, the agency is reimbursed for only 80 percent of the amount of reinsurance claims paid during the remainder of the year. Each guarantee agency's reimbursement rate starts again at 100% at the beginning of each fiscal year.

The 1986 Amendments to the HEA authorized the SLS program. An SLS loan receives a Federal reinsurance guarantee, but no interest subsidies, as do Stafford Loans. Finally, in the Hawkins-Stafford Elementary and Secondary School Improvement

Amendments of 1988, the GSL program was renamed the "Robert T. Stafford Student Loan Program."

Since the inception of the GSL programs, over $114 billion has been loaned to students. In fiscal year 1990, almost $12.5 billion will be loaned to 4.7 million borrowers, and $53 billion of the total amounts loaned in the program will still be outstanding.

We are here today to discuss concerns raised by the financial problems of the Higher Education Assistance Foundation (HEAF), one of the Nation's largest guarantors of student loans. We are here to tell you what we are doing to solve that particular problem, and of the actions being taken by the Department of Education to ensure the continuation and stability of the GSL programs.

The Department of Education -- in conjunction with the Office of Management and Budget, and with the assistance of the investment banking firm of Kidder, Peabody, Inc. -- is closely monitoring the situation and is developing options to resolve the matter. We sent a nine-member team to HEAF's headquarters in St. Paul, Minnesota last week. That group included accounting and computer specialists who administer our student loan programs. They monitored HEAF's operations and assessed the situation first-hand to assist us in making informed decisions about HEAF's existing loan portfolio and its prospective guarantee functions. HEAF was cooperative throughout the review and we anticipate their continued cooperation in resolving this situation. This week, the Department's Inspector General's Office has staff on site at HEAF headquarters conducting an independent review of the agency's operations.

In addition, we are intensively involved in sensitive discussions with other organizations that may have an interest in and capacity for assuming all of HEAF's guarantee functions. While we are not at liberty to disclose specifics about these deliberations, I want to assure you that we are committed to putting in place an appropriate solution.

The Department has made its position clear in public statements and with the Congress. Let me repeat our position here. HEAF's problems do <u>not</u> threaten the integrity of the nationwide Guaranteed Student Loan program. While we take these problems very seriously, analogies of this situation to the savings and loan crisis are quite simply inappropriate. We expect no "domino effect" from HEAF's problems, and see no need for a federal "bailout" of guarantee agencies in general or HEAF in particular. We expect to resolve this matter in a manner that: (1) minimizes costs to the taxpayer; (2) assures orderly management of the HEAF portfolio; and, (3) contributes to a stronger student loan program. As I have indicated before, this situation will <u>not</u>

affect the ability of students to obtain loans, of lenders to make those loans, or of guarantors to insure those loans.

The Department is also taking steps to continue and enhance monitoring of other guarantee agencies with particular focus on their financial strength. This, too, is being done with the objective of ensuring the long term stability of the Guaranteed Student Loan programs.

We also need to consider the reasons for HEAF's financial problems, and the implications of this situation for program-wide improvement.

Under the Guaranteed Student Loan programs administered by the Department, HEAF operates as the designated guarantor in Minnesota, West Virginia, Kansas, Nebraska, Wyoming, and the District of Columbia. It also operates as a national guarantor insuring loans in other states where a different agency is the designated guarantee agency. In 1989, HEAF insured loans worth $1.8 billion made by 1,147 lenders. HEAF insures loans made by lenders to students, pays lenders their insurance claims on defaulted loans, and services and collects these defaulted loans.

It is clear that HEAF sought to be a large volume, national guarantor of student loans. In the mid 1980's HEAF held a large large percentage -- almost 65% -- of its portfolio in proprietary school students' loans. These loans have a higher default rate than loans of students in other sectors of postsecondary education. Thus, the portfolio of loans guaranteed by HEAF has a proportionately high default rate.

With a portfolio of student loans with a high default rate, HEAF was paying out 100 percent for a default claim made by a lender, but receiving only 90 percent or 80 percent reimbursement from the Federal government. This, of course, can ultimately cause a cash flow problem. That is what happened to HEAF.

HEAF realized the problem with its portfolio mix and tried to correct it. It discussed with us a number of options to alter its portfolio. However, the options it originally wanted to pursue would have violated the HEA. Finally, HEAF withdrew as a guarantor in 18 States in 1988. As a result, the proportion of proprietary school loans in its annual portfolio dropped from 59 percent of its annual loan volume in 1988 to 35 percent of annual loan volume in 1989. We expected that this adjustment of its portfolio mix would prevent financial difficulties for HEAF in the future. Indeed, despite its loss in fiscal year 1989, HEAF's last annual report was extremely optimistic about its prospects. However, despite the attempt to reshape its portfolio, HEAF still hits the 80 percent reinsurance trigger -- as a result of the earlier portfolio mix still being presented as default claims. Also, we now know that when HEAF withdrew from the 18 States, it lost a significant proportion of its loan guarantee volume, for which it receives guarantee fees from lenders. Thus, while its costs were still high, HEAF lost substantial revenue. Four weeks ago, the Department was notified by HEAF that it was facing serious financial problems and soon would be unable to continue to pay default claims presented by lenders.

In the larger sense, HEAF's current situation stems from the nationwide problem of defaults on student loans and the disproportionate concentration of that problem in the proprietary school sector. It is possible that HEAF acted imprudently in aggressively pursuing guarantees in that sector, but it is HEAF's view that it was acting consistently with the purposes and requirements of the HEA. We are carefully examining whether there also may have been other HEAF practices that may have contributed to its problems.

In order to understand better the serious problems that massive loan defaults yield in a case like that of HEAF, we need to take a look at the individuals behind these defaults. Who defaults? What do we know about student defaulters? We know from numerous recent studies that borrowers from low-income families are more likely to default than higher income borrowers. We know that many borrowers default because they do not enter jobs with incomes high enough to support the repayment of their educational costs. This is particularly true for students in short-term programs, especially those who drop out before completing the program but, unfortunately, not before they are saddled with a debt to repay. As the borrower progresses through school and the length of the program increases, the likelihood of default drops. But far too many students are not academically prepared for postsecondary education; too many, particularly in short-term programs, drop out before completing their program. Looking at the projected workforce need in the Twenty-first Century, we know that almost half of all new jobs created will require some education beyond high school, and almost a third will be filled by college graduates.

In the future, our Federal student aid programs must continue to serve students in both long- and short-term programs. But we must reduce the possibility that students, especially the needy, minorities, and those in shorter term programs, will drop out or default on their Federal student loans. In reducing these possibilities, we will both ensure continuing access to educational opportunity, shield the student borrower from the serious consequences of default, and protect the Federal taxpayer from the escalating costs of defaults. This must be done to restore public confidence in all of our Federal student aid programs: grant, loan, and work-study.

We have already begun this task. Shortly after becoming Secretary in 1988, I sought the views of the entire postsecondary education community on the best ways to reduce student loan defaults. Through a "Dear Colleague" letter and a Federal Register publication, I raised a list of detailed questions respecting the relative roles and responsibilities of lenders, guarantee agencies, educational institutions, and students. I did so because I believed that the public should have a full opportunity to comment on the costly and persistent default problem before we proceeded to publish final regulations based on proposed rulemaking, issued shortly before I took office, that had generated over 1,200 responses.

Our final regulations, published on June 5, 1989, carefully balance the responsibility of educational institutions for reducing defaults with the reality that we cannot make the problem disappear overnight.

Among the major provisions of our June 1989 regulations were the following:

-- Schools with default rates above 60 percent may be subject to limitation, suspension, or termination (L,S&T) from the Federal student financial aid programs, with the highest allowable default rate decreasing five percent a year over four years to 40 percent

-- Schools with a 40-60 percent default rate must reduce the default rate by five percent per year or face LS&T action

-- Schools with default rates above 30 percent must delay disbursing loans to first-time borrowers until 30 days after the first day of class and must provide pro-rata tuition refunds to borrowers who drop out before the halfway point of a course of study, or in the first six months, whichever is earlier

-- Schools with default rates above 20 percent must develop and submit default management plans to be approved by the Department to address causes of default by their students

-- All schools must provide entrance counseling o first-time borrowers, and

-- All non-baccalaureate vocational programs that make a claim about their job placement rate, regardless of default rate, must compile and disclose consumer information to all prospective students, including program completion and job placement data.

The Department also is taking other regulatory and administrative steps to address abuses by schools that contribute to high default rates. Thus, we have increased the number of program staff devoted to monitoring schools and the number of program reviews of schools. By Monday, regulations will be published authorizing emergency actions for revoking the eligibility of schools for serious abuses. Regulations also are being proposed to address inflated estimates by schools of the quantity of education provided, and to address the conditions under which branch campuses may be eligible to participate in student aid programs. In addition, we are developing a plan to strengthen procedures for eligibility, accreditation, certification, and licensure under existing law.

While these provisions cannot be expected to produce instant results, I am confident that, in combination with our legislative proposals, they represent a solid foundation for making significant inroads toward saving the taxpayers considerable losses occasioned by defaults. These provisions will also help ensure that students will not unfairly suffer the consequences of default.

In conjunction with the default initiative regulations, on June 30, 1989, the Department submitted to Congress its legislative proposal, the "Student Loan Default Reduction Amendments of 1989." This legislation, introduced in the Senate as S. 2029, is designed to strengthen our ability to hold individuals and institutions accountable for responsible performance of their duties under the student aid programs, thus helping to ensure the integrity of these programs.

This bill includes provisions to require lenders to offer graduated repayment schedules to student borrowers, require high-default schools to use a pro-rata tuition refund policy for all student aid recipients, prohibit institutions from employing commissioned recruiters, and require that, in order to receive Federal student aid, any student admitted on the basis of "ability to benefit" (i.e., a student lacking a high school diploma or a GED) must pass a test developed, administered, and graded by an independent organization. These provisions are designed to reduce defaults by protecting the student and by removing the incentive for abuse of the aid programs. Another provision of S. 2029 would enhance collection efforts by providing guaranty agencies with uniform, Federal authority under which to garnish the wages of student loan defaulters.

Only two of the provisions in the Department's proposal have been enacted. The Omnibus Budget Reconciliation Act of 1989 included both the Department's provision clarifying the Secretary's authority to take emergency action against a lender or an institution when such action is necessary to prevent the misuse of Federal funds; and the Department's provision making an institution that loses its accreditation ineligible to participate in the student aid programs for 24 months (with some exceptions). In addition, S. 695, the Educational Excellence Act which was passed by the Senate earlier this year, contains a provision from our initiative prohibiting the employment of commissioned recruiters. We deeply appreciate your action on these provisions.

Our Default Initiative, as comprehensive and as important as it is, however, is just the beginning of our efforts to maintain educational opportunity while simultaneously reducing defaults and their consequences for both defaulters and taxpayers. We have an opportunity to accomplish these objectives on an even broader scale in the upcoming HEA reauthorization.

For the past thirteen months, the Department of Education has been carefully evaluating the HEA in order to propose a comprehensive scheme of amendments. We have held public hearings across the country and solicited and read reams of public comments. We have been seeking to identify problems within the Act, within our Federal postsecondary education programs, and within our system of postsecondary education, of which HEAF's problems are only one extreme example.

Studying problems will not be enough to reduce defaults, however. We all must do far more to ensure that the institutions to which students take their Federal student aid dollars will provide a quality education. Students and taxpayers both deserve no less. This means that States, accrediting agencies, and the Federal Government must do more, individually and together, to make sure that only truly high quality educational institutions will be able to open their doors to students who need Federal student aid. We must ensure that students do not enter low quality programs only to drop out, or graduate from poor quality programs to low paying jobs, with a large loan debt that they cannot repay. We must also ensure that Federal grant monies are wisely spent at our postsecondary institutions. You will see in our reauthorization proposals a package of measures addressing State licensing, accreditation, and Federal program eligibility.

Perhaps in the pursuit of our worthy goal of providing our neediest students "access" to educational opportunity, we have not fully faced the more difficult tasks of promoting retention, graduation, and achievement. As a result, many students have had access only to academic failure and default. We should open doors of educational opportunity only if they can lead to achievement and a quality education; we should open those doors to all students, without at the same time increasing the risk and cost of defaults. If this is the hard lesson that we are meant to learn from the problems that HEAF is facing, we could not be learning them at a more propitious time, as we approach the HEA reauthorization. I look forward to continue working with you to achieve these objectives.

I will be pleased to answer any questions Members of the Subcommittee might have at this time.

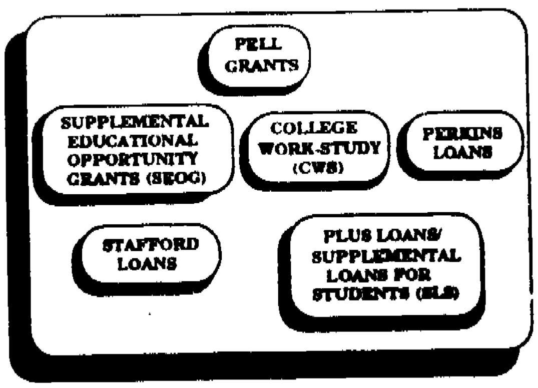
FEDERAL STUDENT AID FACT SHEET 1990-91

Published by the U.S. Department of Education

This *Fact Sheet* offers some information about Federal student aid for students who want education or training beyond high school. But the *Fact Sheet* can't cover everything you need to know. For more information, contact the financial aid administrator at the school(s) you want to attend. You should also check your local public library for additional sources of financial aid.

GENERAL INFORMATION

The U.S. Department of Education offers the following major student financial aid programs:



Grants are financial aid you don't have to pay back. **Work-Study** gives you the chance to work and earn money to help pay for school. **Loans** are borrowed money that you must repay with interest.

Eligibility Requirements

To be eligible to receive aid, a student must meet the following requirements:

- Generally, have financial need.
- Have a high school diploma, a GED, or demonstrate the ability to benefit from the program or training offered. See your financial aid administrator for more information.
- Be enrolled as a regular student in an eligible program. A regular student is one who is enrolled in an institution to obtain a degree or certificate. An eligible program is a course of study that leads to a degree or certificate at a school that participates in one or more of the student aid programs described in this *Fact Sheet*.
- Be enrolled at least **half-time***—except for the campus-based programs (see page 6).
- Be a U.S. citizen or eligible non-citizen. Check with your financial aid administrator for categories of "eligible non-citizen."
- Make **satisfactory academic progress.***
- Sign a **statement of educational purpose/certification statement on refunds and default.***
- Sign an **Anti-Drug Abuse Act Certification.***
- Sign a **statement of updated information.***
- Sign a **statement of registration status.***

Financial Need

Aid from most of the Federal student aid programs discussed in this *Fact Sheet*—except for PLUS and SLS loans (see page 10)—is awarded on the basis of financial need. The amount of aid you receive if you meet the eligibility requirements listed on this page depends on whether you and your family are considered to have financial need.

The information you report on an aid application (see "Applying," page 2) is used in the formulas that calculate your need and eligibility.

*See "Important Terms," pages 11 to 12 for a definition of this term.

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Eligibility for the Pell Grant Program is determined by a formula and depends on a number called the "Pell Grant Index (PGI)." If this number is low enough, you're eligible for a Pell Grant. And the lower the number, the larger your award will be. If your PGI is higher than a certain number, you're not eligible. For more information on Pell Grants, see page 5.

There isn't a minimum or maximum number in determining eligibility for the "campus-based" and Stafford Loan programs (see pages 6 and 8 for information on these programs). Instead, your financial need is determined by the following subtraction:

COST OF EDUCATION
— FAMILY CONTRIBUTION (FC)
= FINANCIAL NEED

COST OF EDUCATION—your educational expenses such as tuition, fees, room, board, books, supplies, transportation, child care, costs related to a handicap, and miscellaneous expenses.

FAMILY CONTRIBUTION (FC)—the amount you and your family are expected to pay toward your education. This amount is determined by a standard formula somewhat different from that used for the Pell Grant Program. However, as is true for the Pell Grant Program, factors such as taxable and non-taxable income, assets (such as savings and the value of a home), and benefits (for example, unemployment or Social Security) are all considered in the calculation. You can get a booklet describing the FC formula in detail by writing to—Congressional Methodology, Department M-11, Pueblo, Colorado 81009-0015.

Note that although need is determined by formula, the financial aid administrator can adjust—up or down—your Family Contribution (FC) or your cost of education, if he or she believes your family's financial circumstances warrant it. However, the aid administrator does not *have* to make such an adjustment. For more information on adjustments, see "Special Circumstances," page 3, or contact your financial aid administrator.

Applying

You can use any one of a number of forms if you'll be applying for need-based Federal student aid *other than* a Pell Grant. Check with your school to find out which form to use. However, if you want to be considered for a Pell Grant as well, you must use one of the six forms listed in the next column.

Your school may specify which of these forms you should complete if you also want to be considered for aid from **non-Federal** sources. You can get the application you need from your school.

The following four forms are free:

• The U.S Department of Education's "Application for Federal Student Aid" (AFSA)

• The Pennsylvania Higher Education Assistance Agency's (PHEAA's) "Application for Pennsylvania State Grant and Federal Student Aid"

• CSX Technology's "Application for Federal and State Student Aid (AFSSA)"

• United Student Aid Funds' (USAF's) "Singlefile Form"

The two forms listed below collect extra information used in applying for non-Federal aid and charge for processing that information:

• The American College Testing Program's "Family Financial Statement" (FFS)

• The College Scholarship Service's "Financial Aid Form" (FAF)

If you apply using a form other than the U.S. Department of Education's AFSA and you want to be considered for Federal student aid, you must check a box to have your information forwarded to the Federal processing center. The box is in the middle of the form.

For the Stafford Loan, PLUS, or SLS programs, there are some additional steps you must take to apply. (See pages 8 and 10 for information on these programs.)

Certain questions on your student aid application will determine whether you're considered dependent on your parents and must report their income and assets as well as your own (and your spouse's, if you're married), or whether you're independent and report only your own income (and that of a spouse). **So be sure to answer the questions on your student financial aid application carefully.** You may have to prove later that what you reported is correct.

☞ NOTE: If you want to apply to more than one school, and those schools use different student aid applications, you may not have to fill out more than one application. Instead, you may be able to use a short form called a "Request for Information Transfer" (RIT) and have the information from the ***Federal*** portion of one application sent to another school of your choice. Check with the schools you're interested in to see if you can fill out a RIT.

Apply as soon as possible after January 1, 1990. Send your application to the address given in your application booklet. It will take 4 to 6 weeks for your application to be processed, and you may have to confirm or correct information and return it for reprocessing. (See "Student Aid Report" below.) Reprocessing takes another 2 to 3 weeks. Also, you may have to prove the information you reported is correct. You need to complete each step in the process promptly, so that you don't miss any deadlines (see "Deadlines," page 4). **Missing a deadline means you will lose out on student aid.**

If it's been more than 6 weeks since you applied and you haven't heard anything, you can check the status of your application by writing to the Federal Student Aid Information Center, P.O. Box 84, Washington, D.C. 20044.

When you write, make sure you include in your letter your full name, permanent address, Social Security Number, date of birth, and signature.

Or, you can call the number for status checks given on page 4.

☞ NOTE: Aid from Federal programs is not guaranteed from one year to the next. You must reapply every year. Also, if you change schools, your aid doesn't automatically go with you. Check with your new school to find out what steps you must take.

Student Aid Report

After you apply for Federal student aid, you'll receive a Student Aid Report (SAR) in 4 to 6 weeks. The SAR will contain the information you gave on your application plus your Pell Grant Index (PGI) number, which determines your Pell Grant eligibility, and your Family Contribution (FC) number, used in determining your eligibility for the campus-based and Stafford Loan programs.

Make sure you review the information that's printed out on the SAR. This information must be correct before you can receive any Federal student aid. If you need to make any changes, make them on Part 2 of your SAR, which will be called either the Information Review Form or the Information Request Form. Sign the Certification statement on the back of Part 2 and **return Part 2 only** to the address given on the back of Part 2. You'll receive a new SAR in 2 to 3 weeks.

If all the information on your SAR is correct as it is, and you're eligible for a Pell Grant, **submit all three parts** of the SAR to your financial aid administrator right away. Your aid administrator will use the information on your SAR to determine the amount of your Pell Grant.

Even if your SAR says you're not eligible for a Pell Grant, contact your financial aid administrator. He or she may use the Family Contribution (FC) number on the SAR in determining whether you're eligible for other Federal student aid.

If you have any trouble understanding what you're supposed to do after you get your SAR or how you're supposed to make corrections, your financial aid administrator can help you and can answer any questions you have.

To request a copy of your SAR or to correct your address for the records, write to the agency where you sent your student aid application or write to the Federal Student Aid Information Center, P.O. Box 84, Washington, D.C. 20044. When you write, make sure you include in your letter your full name, permanent address, Social Security Number, date of birth, and signature.

You can also request a copy of your SAR by calling the number for duplicate requests given on page 4. However, you can correct your address only by writing a letter.

Special Circumstances

Some students may have special financial considerations that can't be described adequately on an application. If you feel you have special circumstances that might affect the amount you and your family are expected to contribute toward your education, see your financial aid administrator. Remember, for the campus-based and Stafford Loan programs, the aid administrator may adjust your cost of education or your Family Contribution (FC) if he or she feels your circumstances warrant it. For example, if you believe the amount you and your family are expected to contribute toward your

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education is too high, you can ask your aid administrator to review your case. But remember, the aid administrator does not *have* to make any of these changes—there have to be very good reasons for doing so. Also remember that the aid administrator's decision is ***final*** and cannot be appealed to the U.S. Department of Education.

☞ **NOTE:** The Pell Grant Program does not allow for *individualized* adjustments. However, there are certain special conditions that would make the family's financial circumstances worse in 1990-91 than they were in 1989. If one of these conditions applies to you or your family, **estimated 1990** income information will be used to calculate your Pell Grant eligibility, instead of 1989 income. The conditions are death of a parent or spouse, separation or divorce, loss of a full-time job, or loss of nontaxable income or benefits such as Social Security, child support, Aid to Families with Dependent Children (AFDC or ADC), welfare, or unemployment benefits.

If you think you meet one of the special conditions, see your financial aid administrator. If you qualify, the aid administrator will explain what steps to take so that estimated 1990 income will be used.

Deadlines

MAY 1, 1991—Your student aid application must be *received* by this date. The application you fill out will contain the address where your application must be sent. **THERE ARE *NO EXCEPTIONS* TO THIS DEADLINE.**

You should apply as soon after January 1, 1990, as you can. Schools often set deadlines early in the calendar year that students must meet in order to receive certain types of funds, including those from the campus-based programs (see pages 6 through 8 for information on these programs).

JULY 1, 1991, or your last day of enrollment in 1990-91, whichever comes first. This is the deadline for submitting your SAR to your school's financial aid office. Be sure you know your last day of enrollment in 1990-91—it may be earlier than July 1. The earlier you can submit your SAR, the better, but you must turn it in by the deadline.

Telephone Numbers

There may be times when you have questions about your application, your SAR, or other Federal student aid matters, and you need an answer right away. If so, you may call one of the numbers below at the **Federal Student Aid Information Center** between the hours of **9:00 a.m.** and **5:30 p.m.** (Eastern Standard Time), Monday through Friday:

1-(800) 333-INFO (a ***toll-free*** number)
The Information Center provides the following services at the toll-free number:

- Helping you file an application or correct a SAR
- Explaining the Request for Information Transfer (RIT) process
- Checking on whether a school takes part in Federal student aid programs
- Explaining student eligibility requirements
- Mailing publications

1-(301) 722-9200
You must call this number at the Information Center if you want to find out if your application has been processed, or if you want a duplicate Student Aid Report (SAR). **Please note that you will have to pay for this call.** The Center cannot accept collect calls.

1-(301) 369-0518
If you are hearing-impaired, you may call this TDD number at the Information Center for help with any Federal student aid questions you may have. This number is not toll-free, and the Center cannot accept collect calls.

If you have reason to suspect any fraud, waste, or abuse involving Federal student aid funds, you may call the following ***toll-free*** number:

1-(800)-MIS-USED
This number is the hotline to the U.S. Department of Education's Inspector General's office. You may remain anonymous, if you wish.

Student Rights

Education after high school costs you time, money, and effort. It's a big investment, and you should carefully evaluate the school you're considering. You have the *right* to know certain things about a school you're considering. To find out about a school, you need to—

Check the school's accreditation. Ask for the names of the school's accrediting and licensing organizations. You also have the right to ask for a copy of the documents describing the institution's accreditation or licensing. But don't assume that if a school is accredited that's all you need to know. . .

Find out about the school's programs for yourself. You have the right to ask a school about its programs, its faculty, and its instructional, laboratory, and other physical facilities (including what special facilities and services are available to the handicapped).

Find out about financial aid. You have the right to ask the school the following:

• What financial assistance is available, including information on all Federal, State, local, private, and institutional financial aid programs. You also have the right to know how a school selects financial aid recipients.

• What the procedures and deadlines are for submitting applications for each available financial aid program.

• How the school determines your financial need. This process includes how costs for tuition and fees, room and board, travel, books and supplies, and personal and miscellaneous expenses are considered in your cost of education. It also includes the resources considered in calculating your need (such as parental contribution, other financial aid, assets, etc.). You also have the right to know how much of your financial need, as determined by the school, has been met and how and when you'll receive your aid.

• How the school determines each type and amount of assistance you'll receive. You also have the right to ask the school to reconsider your aid "package" if you believe a mistake has been made, or if your enrollment or financial circumstances have changed.

• How the school determines whether you're making **satisfactory academic progress,*** and what happens if you're not. Whether you continue to receive Federal financial aid depends, in part, on whether you're making satisfactory progress.

• What the interest rate is on any student loan you may receive, the total amount you must repay, the length of time you have to repay, when you must start repaying, and what cancellation or deferment (postponement) provisions apply.

• If you're offered a College Work-Study job (see page 7 for information on this program)—what kind of job it is, what hours you must work, what your duties will be, what the rate of pay will be, and how and when you'll be paid.

• Who the school's financial aid personnel are, where they're located, and how to contact them for information.

Understand your school's refund policy. You have the right to know what your school's policy is. If something happens and you never register for classes, or if you drop out of school within a short time after you start, you may be able to get a part of your educational expenses returned to you. But after a certain date, you won't get any money back. Check with your school to find out what expenses you may have to pay if you drop out. Keep in mind that if you receive Federal student aid from any of the programs mentioned in this *Fact Sheet*—other than College Work-Study—some or all of that aid will be returned to those programs.

If you have a Stafford Loan or a Supplemental Loan for Students (SLS), or if your parents have a PLUS loan for you (see pages 8 and 10 for information on these programs), the school must explain its refund policy, in writing, to you and to all prospective students. The school must also make its refund policy known to students who are currently enrolled. The school must include examples of how its policy applies and must explain the procedures you must follow to obtain a refund. If the school changes its refund policy, it must make sure all students are made aware of the new policy.

GRANTS, WORK-STUDY, AND LOANS

Pell Grants

A Pell Grant helps undergraduates pay for their education after high school. For the Pell Grant

*See "Important Terms," pages 11 to 12, for a definition of this term.

program, an undergraduate is one who has not earned a bachelor's or first professional degree. (A professional degree would include a degree in such fields as pharmacology or dentistry, for example.)

Eligibility for those who receive a Pell Grant for the first time is generally limited to 5 to 6 years of undergraduate study. For more information, see your financial aid administrator.

For many students, Pell Grants provide a "foundation" of financial aid, to which aid from other Federal and non-Federal sources may be added. Unlike loans, grants don't have to be paid back.

How do I qualify?

You must be attending school at least **half-time.***

To determine if you're eligible, the Department of Education uses a standard formula, passed into law by Congress, to evaluate the information you report on your student aid application. The formula produces a Pell Grant Index (PGI) number. Your Student Aid Report (see page 3) contains this number and will tell you whether you're eligible.

The formula used to determine your Pell Grant Index (PGI) is too long to be included here. However, you can get a booklet that describes it in detail by writing to—Formula Book, Department M-11, Pueblo, Colorado 81009-0015.

How much money can I get?

Awards for the 1990-91 academic year (July 1, 1990 to June 30, 1991) will depend on program funding. The maximum award for the 1989-90 academic year was $2,300. How much you actually get will depend not only on your Pell Grant Index (PGI) number, but on the cost of education at your school, whether you're a full-time or part-time student, and whether you attend school for a full academic year, or less than that.

When should I apply?

The sooner, the better. Your 1990-91 application must be ***received*** at the address given on your application ***no later than*** May 1, 1991. **THERE ARE *NO EXCEPTIONS* TO THIS DEADLINE.**

*See "Important Terms," pages 11 to 12, for a definition of this term.

How will I be paid?

You must submit all parts of your Student Aid Report (SAR) to your school by the deadline noted on page 4. Your school will then credit your award to your account, pay you directly, or use a combination of these methods.

The school must tell you in writing how and when you'll be paid and how much your award will be. You should acknowledge the school's notification in writing, for the school's records. Schools must pay at least once per term (semester, trimester, or quarter). Schools that do not use formally defined, traditional terms must pay at least twice per academic year.

Campus-Based Programs

Supplemental Educational Opportunity Grants (SEOG)
College Work-Study (CWS)
Perkins Loans

The three programs you'll read about next are called "campus-based" programs because they're administered by the financial aid administrator at each participating school. Even though each program is different—SEOG offers grants, CWS offers jobs, and Perkins provides loans—they have these characteristics in common:

• You can go to school less than **half-time*** and still be able to receive aid.

• How much aid you receive from the campus-based programs depends on your financial need (see page 1), the amount of other aid you'll receive, and the availability of funds at your school. Unlike the Pell Grant Program, which provides funds to every eligible student, each school participating in any of the campus-based programs receives a certain amount of funds for each program. When that money is gone, there are no more awards from that program for that year.

• There's no one deadline for applying as there is for the Pell Grant Program—each school sets its own. But most deadlines are quite early in each calendar year. Be sure to check with the financial aid administrator at your school to find out what its deadlines are. **You'll probably miss out on receiving aid from the campus-based programs if you don't apply early!**

Supplemental Educational Opportunity Grants (SEOG)

What is an SEOG?

A Supplemental Educational Opportunity Grant (SEOG) is for undergraduates with exceptional financial need (with priority given to Pell Grant recipients), and it doesn't have to be paid back.

How much can I get?

You can get up to **$4,000 a year**, depending on the restrictions noted on the preceding page.

What's the difference between an SEOG and a Pell Grant?

The Department of Education guarantees that each participating school will receive enough money to pay the Pell Grants of its eligible students. As noted on the preceding page, there's no guarantee every eligible student will be able to receive an SEOG.

How will I be paid?

Your school will credit your SEOG to your account, pay you directly, or use a combination of these methods. Schools must pay students at least once per term (semester, trimester, or quarter). Schools that do not use traditional terms must pay at least twice during the academic year. (There's one exception: If the total SEOG aid you receive is $500 or less, the school may pay you just once during the year, if it chooses.)

College Work-Study (CWS)

What is College Work-Study?

The College Work-Study (CWS) Program provides jobs for undergraduate and graduate students who need financial aid. CWS gives you a chance to earn money to help pay your educational expenses.

How much can I make?

Your pay will be at least the current Federal minimum wage, but it may also be related to the type of work you do and the skills required. Your total CWS award depends on the restrictions noted on the previous page.

How will I be paid?

If you're an undergraduate, you'll be paid by the hour. If you're a graduate student, you may be paid by the hour or you may receive a salary. No CWS student may be paid by commission or fee. Your school will pay you at least once a month.

Are College Work-Study jobs on campus or off campus?

Both. If you work on campus, you'll usually work for your school. If you work off campus, your job will usually involve work that is in the public interest, and your employer will usually be a private or public non-profit organization, or a local, State, or Federal agency. However, some schools may have agreements with private sector employers for CWS jobs.

Can I work as many hours as I want?

No. Your school sets your work schedule. In arranging a job and assigning work hours, your financial aid administrator will take into account your class schedule, your health, and your academic progress. And remember, the amount you earn can't exceed your total CWS award.

Perkins Loans

What is a Perkins Loan?

A Perkins Loan is a low-interest (5 percent) loan to help you pay for your education after high school. These loans are for both undergraduate and graduate students and are made through a school's financial aid office. Your school is your lender. You must repay this loan.

How much can I get?

Depending on the restrictions noted on the previous page, you may borrow up to—

- $4,500 if you're enrolled in a vocational program, or if you have completed less than 2 years of a program leading to a bachelor's degree.

- $9,000 if you're an undergraduate student who has already completed 2 years of study toward a bachelor's degree and has achieved third-year status. (This total includes any amount you borrowed under Perkins [or under the National Direct Student Loan Program, its former name] for your first 2 years of study.)

• $18,000 for graduate or professional study. (This total includes any amount you borrowed under Perkins/NDSL for your undergraduate study.)

How will I be paid?

After you sign a **promissory note*** **agreeing** to repay the loan, your school will either pay you directly or credit your account. You'll receive the loan in at least two payments during the academic year. (There's one exception: If the total Perkins Loan you receive is $500 or less, the school may pay you just once during the year, if it chooses.)

When do I pay back this loan?

If you're attending at least **half-time,*** you have a "grace period" of 9 months after you graduate, leave school, or drop below **half-time.*** If you're a less-than-**half-time*** student, your grace period may be different. Check with your financial aid administrator.

If you borrowed under the old National Direct Student Loan (NDSL) Program ***on or after*** October 1, 1980, your grace period is 6 months. If you borrowed under that program ***before*** October 1, 1980, your grace period is 9 months.

At the end of your grace period, you must begin repaying your loan. You may be allowed up to 10 years to repay.

How much will I have to pay each month?

The amount of each payment depends on the size of your debt and on the length of your repayment period. Usually, you must pay at least $30 per month. In special cases—for example, if you're unemployed or ill for a long period of time—your school may allow you to make payments that are less than $30 per month or may extend your repayment period.

The following chart shows typical monthly payments and total interest charges for three different 5 percent loans over a 10-year period.

Total Loan Amount	Number of Payments	Monthly Payment	Total Interest Charges	Total Repaid
$ 4,500	120	$ 47.73	$1,227.60	$ 5,727.60
9,000	120	95.46	2,455.20	11,455.20
18,000	120	190.92	4,910.40	22,910.40

*See "Important Terms," pages 11 to 12, for a definition of this term.

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Can I defer (postpone) repayment of my Perkins Loan after I leave school?

Under certain conditions, yes—as long as you're not in **default.*** However, deferments aren't automatic. You have to apply for one through your school, using a deferment request form that you must get from your school.

For information on what deferments are permissible under the Perkins Loan Program, see your financial aid administrator.

☞ NOTE: Even though you may have ***applied*** for a deferment, you still must continue to **make payments** until your deferment is processed. If you don't, you may end up in **default.***

Are there ever any cases where repayment of a Perkins Loan can be cancelled?

Yes, a few. For example, your loan will be cancelled if you die or become totally and permanently disabled. Your loan can be cancelled if you're a teacher (under certain circumstances), or if you're a Head Start or a Peace Corps or VISTA volunteer. For more information, read your **promissory note*** or contact your financial aid administrator.

Stafford Loans

What is a Stafford Loan?

Stafford Loans are low-interest loans made to students attending school at least **half-time.*** Loans are made by a lender such as a bank, credit union, or savings and loan association. Sometimes a school acts as a lender. These loans are insured by a guarantee agency in each State and reinsured by the Federal Government. You must repay this loan.

For **new borrowers*** who receive loans for periods of enrollment beginning ***on*** or ***after*** July 1, 1988, the interest rate is generally 8 percent for the first 4 years of repayment and 10 percent after that. For **new borrowers*** who took out a loan ***between*** July 1, 1987, and June 30, 1988, the interest rate is 8 percent. Students who are ***not*** **new borrowers*** should check their **promissory note*** for the interest rate.

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How much can I borrow?

Depending on your financial need (see page 1), you may borrow up to—

- $2,625 a year, if you're a first- or second-year undergraduate student.
- $4,000 a year, if you have completed 2 years of study and have achieved third-year status.
- $7,500 a year, if you're a graduate student.

The total debt you can have outstanding as an undergraduate is $17,250. This includes any amount you may have borrowed under the Guaranteed Student Loan (GSL) Program—the former name for the Stafford Loan Program. The total for graduate or professional study is $54,750, including any Stafford Loans and GSL's made at the undergraduate level.

☞ **NOTE:** You can't borrow more than the cost of education at your school, minus any other financial aid you receive.

How do I apply?

You can get an application from a lender, a school, or your State guarantee agency. After you fill out your part of the application, the school you plan to attend must complete its part, certifying your enrollment, your cost of education, your academic standing, any other financial aid you'll receive, and your financial need.

When the school's portion of the application is completed, you or your school submits it to the lender you've chosen. If the lender agrees to make the loan and gets the approval of the guarantee agency, the lender will send the loan amount to your school.

When should I apply?

Since not every lender participates in the Stafford Loan Program, you should begin looking for one as soon as you're accepted by your school. After you submit your application to a lender and the lender agrees to make the loan, it usually takes 4 to 6 weeks to get your loan approved by the guarantee agency, so give yourself as much time as possible to complete the application process.

How will I be paid?

Your lender sends your loan proceeds to your school. Your loan proceeds will be made payable either to you or to both you and your school. Your school will issue your loan proceeds to you in one or more payments. (In general, for longer periods of enrollment, the loan will be divided into two or more installments.)

How can I find out who the lenders are in my State?

Contact your State guarantee agency. It's the best source of information on the Stafford Loan Program in your State. To find out your State guarantee agency's address and phone number and to find out more information about borrowing, call the Federal Student Aid Information Center (toll-free): **1-(800) 333-INFO**.

Is there any charge for making a Stafford Loan?

Yes, there is an "origination fee" of about 5 percent, which will be deducted proportionately from each loan disbursement made to you. The money is passed on to the Federal Government to help reduce the Government's cost of subsidizing these low-interest loans.

Your lender may also charge you an insurance premium of up to 3 percent of the loan principal. This premium must be deducted proportionately from each disbursement.

When do I pay back this loan?

After you graduate, leave school, or drop below **half-time,*** you have a certain period of time before you have to begin repayment, called a "grace period." The length of this period depends on when you took out your loan, but it is usually 6 to 12 months. Check your **promissory note*** or ask your lender what your grace period is.

How much will I have to pay each month?

The amount of each payment depends on the size of your debt and on the length of your repayment period. Usually, you'll have to pay at least $50 per month or $600 per year. Ask your lender what your monthly payments will be before you take out the loan, so you'll know what to expect.

*See "Important Terms," pages 11 to 12, for [illegible] term.

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The chart below shows ***estimated*** monthly payments and total interest charges for 8 percent/10 percent loans of varying amounts, with typical repayment periods.

TYPICAL REPAYMENT PLANS

Total Indebtedness	Number of Payments	Monthly Payment	Interest Charges	Total Repaid
$ 2,600	64	$ 50.00	$ 614.60	$ 3,214.60
4,000	119	50.00	1,972.48	5,972.48
7,500	120	93.52	3,722.07	11,222.07
10,000	120	124.68	4,961.77	14,961.77
15,000	120	187.01	7,441.17	22,441.17

Source: National Council of Higher Education Loan Programs, Inc. (NCHELP), 1989

Your school must give you a loan repayment schedule, which lets you know the due date of your first payment, and the number, frequency, and amount of all payments.

Can I defer (postpone) repayment of my Stafford Loan after I leave school?

Yes, under certain conditions, and as long as your loan is not in **default.*** However, deferments are not automatic. For information on what deferments are permissible under the Stafford Loan Program, contact your financial aid administrator, your lender, or the guarantee agency in your State. If you believe you qualify, submit a written request for deferment to your lender.

☞ NOTE: Even though you may have ***applied*** for a deferment, you still must **continue to make payments** until your deferment is processed. If you don't, you may end up in **default.***

Are there ever any cases where repayment of a Stafford Loan can be cancelled?

Only if you become totally and permanently disabled, or if you die. However, if you serve as an enlisted person in certain selected specialties of the U.S. Army, the Army Reserves, the Army National Guard, or the Air National Guard, the Department of Defense will, as an enlistment incentive, ***repay*** a portion of your Stafford Loan. If you think you may qualify, contact your recruiting officer.

*See "Important Terms," pages 11 to 12, for a definition of this term.

PLUS Loans Supplemental Loans for Students (SLS)

What are PLUS and SLS loans?

PLUS loans are for **parents** who want to borrow to help pay for their children's education; Supplemental Loans for Students (SLS) are for **student** borrowers. Like Stafford Loans, both these loans are made by a lender such as a bank, credit union, or savings and loan association.

PLUS and SLS loans have variable interest rates, adjusted each year. For the 1989-90 award year, the interest rate was 12 percent. The interest rate for the 1990-91 award year will be determined in June 1990. The interest rate for each loan is shown on the **promissory note,*** signed by the borrower when the loan is made.

Who can get a loan, and how much can they borrow?

PLUS enables parents to borrow up to $4,000 per year, to a total of $20,000, for each child who is enrolled at least **half-time*** and is a dependent student. (See page 2 for a discussion of dependent vs. independent students.)

Under SLS, graduate students and independent undergraduates may borrow up to $4,000 per year, to a total of $20,000. This amount is **in addition** to the Stafford Loan limits. (In exceptional circumstances, the financial aid administrator may authorize dependent undergraduates to apply for an SLS.)

How does a PLUS or SLS borrower apply?

The same way as for a Stafford Loan (see page 9). Unlike Stafford Loan borrowers, however, PLUS and SLS borrowers do not have to show need. However, like all borrowers, they may have to undergo a credit analysis.

☞ **Note to SLS borrowers:** Before you can receive an SLS, your school must determine your eligibility for a Stafford Loan and for a Pell Grant (if you're an undergraduate and your school participates in the Pell Grant Program). If you're eligible for aid from either or both of those programs, the amount you're eligible for may affect the amount you can borrow under SLS: Under SLS—as under the Stafford Loan Program—you can't borrow more than the cost of education at your school minus *any other financial aid* you receive.

How will I be paid?

If your parent(s) takes out a PLUS loan for you, the lender sends the full amount of the loan proceeds in the form of a check directly to your parent(s). If you take out an SLS, the lender sends the loan proceeds to your school. Your loan proceeds will be made payable either to you or to both you and your school. Your school will issue your loan proceeds to you in one or more payments. (In general, for longer periods of enrollment, the loan will be divided into two or more installments.)

Is there any charge for making a PLUS or an SLS?

Your lender may charge an insurance premium of up to 3 percent of the loan principal. This premium must be deducted proportionately from each loan disbursement made to you. There is no origination fee for these loans.

When do my parents or I have to begin repaying these loans?

PLUS and SLS borrowers generally must begin repaying both **principal** and **interest** within 60 days after the last loan disbursement. However, if a deferment applies (including a deferment for being in school), borrowers do not begin repaying any ***principal*** until the deferment ends.

☞ **NOTE:** You must continue to pay the ***interest*** during a deferment period, unless the lender allows you or your parents to wait until the deferment ends to repay it.

What are the deferments?

SLS borrowers get the same deferments as Stafford Loan borrowers except that, as mentioned above, under SLS the deferments apply only to loan ***principal***. PLUS deferments are much more limited and also apply only to principal. For information about specific repayment and deferment conditions, contact your financial aid administrator, your lender, or the guarantee agency in your State.

☞ **NOTE:** Unlike Stafford Loans (see page 9), there are no grace periods for PLUS and SLS loans.

Are there any cancellation provisions?

They're the same as for Stafford Loans—only for death or permanent and total disability after the loan is taken out.

If I borrow under more than one of the loan programs mentioned in this *Fact Sheet*, can I combine payments so I won't have to make several different ones?

Yes, except for PLUS loans, all of the loans described in this *Fact Sheet* are eligible for "loan consolidation." This is a plan that allows certain eligible lenders to pay off your existing student loans and to create one new loan. You're eligible for loan consolidation if you have loans totalling at least $5,000. You must be in repayment (or have entered your grace period) before your loans can be consolidated. The interest rate on the consolidated loan will be 9 percent or more, depending on the interest rates of the loans consolidated. The repayment period will be from 10 to 25 years, depending on the amount to be repaid.

IMPORTANT TERMS

Anti-Drug Abuse Act Certification: To receive a Pell Grant, you must sign a statement certifying that you will not make, distribute, dispense, possess, or use drugs during the period covered by the grant. Your 1990-91 Student Aid Report (SAR) will contain this certification statement although, in some cases, your school may ask you to sign instead a separate statement it has prepared.

☞ **NOTE:** Your eligibility for ***any*** of the programs covered in this *Fact Sheet* may be suspended or terminated by a court as part of a conviction for possessing or distributing drugs.

Default: Failure to repay a student loan according to the terms agreed to when you signed a **promissory note.*** If you default on a student loan, your school, lender, State, and the Federal Government all can take action to recover the money, including notifying national credit bureaus of your default. This may affect your future credit rating for a long time. Also, you may be liable for expenses incurred in collecting the loan. If you decide to return to school, you're not entitled to receive additional Federal aid or a deferment of your loan repayments. Finally, the Internal Revenue Service may withhold your income tax refund. The amount of your refund will be applied toward the amount you owe.

Half-Time: At schools measuring progress by credit hours and academic terms (semesters, trimesters, or quarters), "half-time" means at least 6 semester hours or quarter hours per term. At schools measuring progress by credit hours but not using academic terms, "half-time" means at least 12 semester hours or 18 quarter hours per year. At schools measuring progress by clock hours, "half-time" means at least 12 hours per week. Note that schools may choose to set higher minimums than these. Also, Stafford Loan, PLUS, and SLS requirements may be slightly different.

You must be attending school at least half-time to be eligible to receive a Pell Grant, Stafford Loan, a PLUS, or an SLS. Half-time enrollment is not a requirement to receive aid from the Supplemental Educational Opportunity Grant, College Work-Study, and Perkins Loan programs.

New Borrower: A term that applies to the Stafford Loan, PLUS, or SLS programs. You're a "new borrower" under these programs if you had no outstanding (unpaid) Stafford Loans, PLUS, SLS, or consolidation loans on the date you signed your promissory note, ***and*** if your loan was either disbursed on or after July 1, 1987, or was for a period of enrollment that began on or after July 1, 1987. Once you qualify as a new borrower, the loan conditions that apply to "new borrowers" automatically apply to any future Stafford Loans, PLUS loans, or SLS loans you may receive.

Promissory Note: The legal document you sign when you get a student loan. It lists the conditions under which you're borrowing and the terms under which you agree to pay back the loan. It's very important to **READ AND SAVE** your copy of this document because you'll need to refer to it later when you begin repaying your loan.

Satisfactory Academic Progress: To be eligible to receive Federal student aid, you must be maintaining satisfactory academic progress toward a degree or certificate. You must meet your school's written standard of satisfactory progress. Check with your school to find out what its standard is.

If you received Federal student aid **for the first time** on or after July 1, 1987 ***and*** you're enrolled in a program that's **longer than 2 years**, the following definition of satisfactory progress ***also*** applies to you: You must be maintaining a "C" average by the end of your second academic year of study, or have an academic standing consistent with your institution's graduation requirements. You must continue to maintain satisfactory academic progress for the rest of your course of study.

Statement of Educational Purpose/Certification Statement on Refunds and Default: You must sign this statement in order to receive Federal student aid. By signing it, you are stating that you do not owe a refund on a Pell Grant or SEOG, and you are not in default on a Perkins Loan, Stafford Loan, PLUS, or SLS. You're also agreeing to use your student aid only for education-related expenses. Part 1 of the 1990-91 Student Aid Report (SAR) contains such a statement. You must sign either this one or a similar one prepared by your school.

Statement of Registration Status: If you're required to register with the Selective Service, you must sign a statement indicating you have done so before you can receive any Federal student aid. This requirement applies to males who were born on or after January 1, 1960, are at least 18, are citizens or eligible non-citizens, and are not currently on active duty in the Armed Forces. (Citizens of the Federated States of Micronesia, the Marshall Islands, or the Trust Territory of the Pacific [Palau] are exempt from registering.)

Part 1 of the 1990-91 Student Aid Report contains a statement of registration status. If you are required to register, you must sign either that statement or a similar one prepared by your school. (Some schools require all students to sign a statement, indicating that they either have registered with the Selective Service or are not required to do so.)

Statement of Updated Information: You must sign a statement certifying that certain Student Aid Report (SAR) items are correct *at the time you submit your SAR to your school*. If information for any of those items changes after you submit your application, you must update the information so that it's correct on the date you sign your SAR. Otherwise, you won't be able to receive Federal student aid. Read the Statement of Updated Information on the back of Part 1 of your SAR for the information that must be updated.

☞ **NOTE:** The only exception to the requirement to update is when changes occur because your marital status changes. In that case, you cannot update.

QUESTIONS ABOUT STUDENT AID?

call the

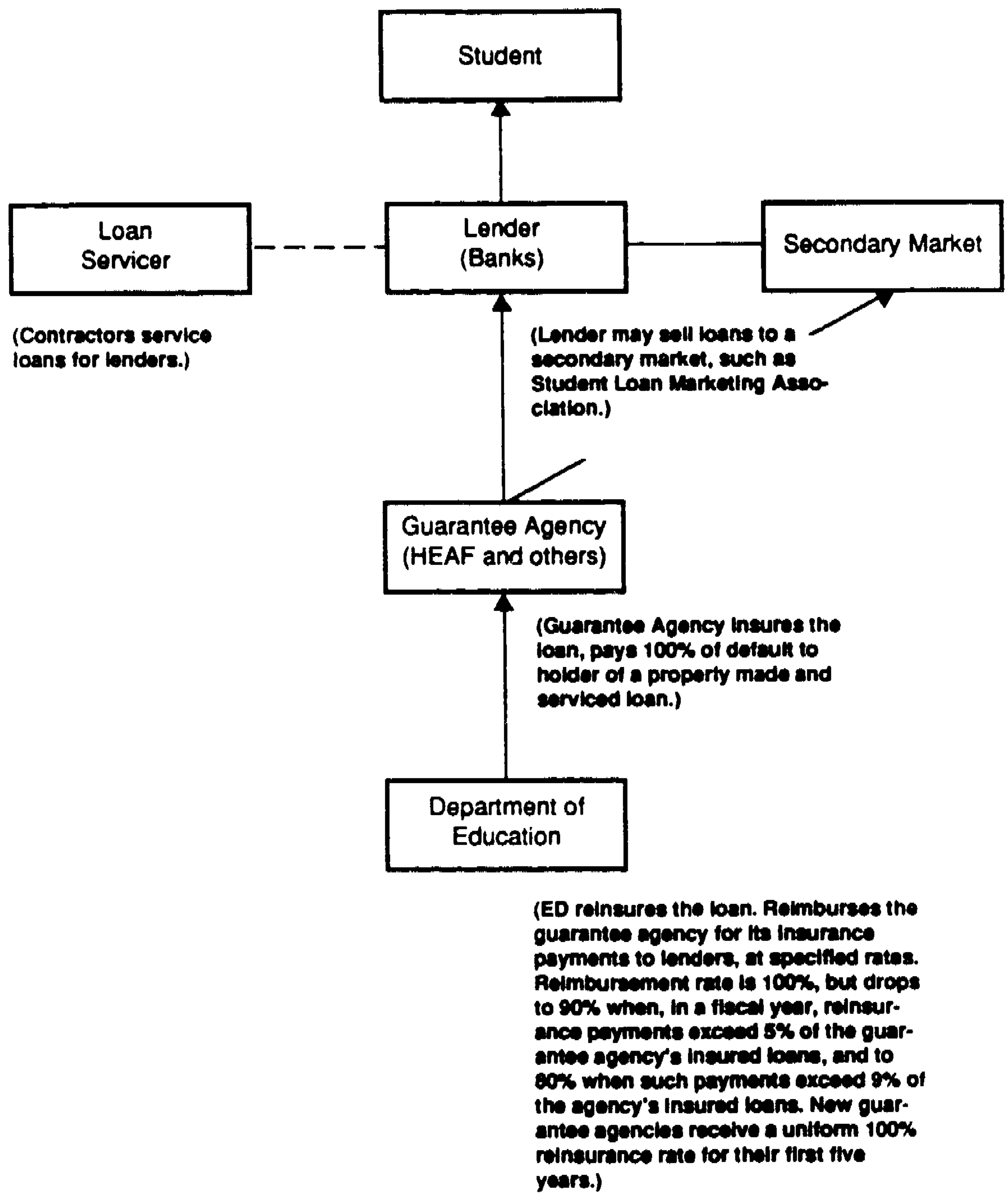
FEDERAL STUDENT AID INFORMATION CENTER

TOLL-FREE

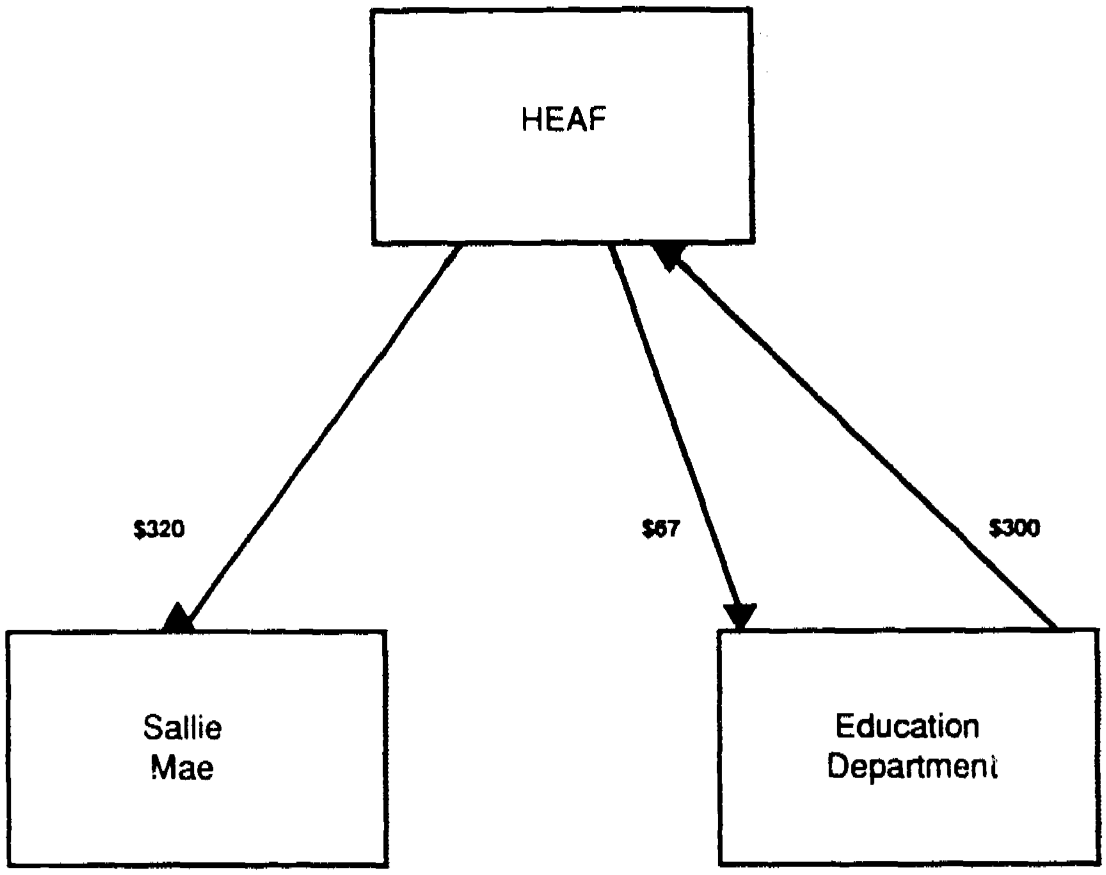
1-(800)-333-INFO

9:00 a.m.—5:30 p.m.
Eastern Time
Mon.— Fri.

ROLE OF GUARANTOR IN GSL PROGRAM



HEAF INDEBTEDNESS
(Estimates as of September 30, 1990, $ in millions)



Senator PELL. We now come to Mr. Richard Hawk, who is the chief executive officer of the Higher Education Assistance Foundation, HEAF. Thank you very much for being with us.

There is a roll call vote going on, so I would suggest that we go off to that and come right back. Mr. Hawk, if you could place yourself at the table, we will be back.

[Recess.]

Senator PELL. The subcommittee will come to order. I regret these interruptions, but there is no avoidance of them with the roll call votes going on.

Our next witness is Mr. Richard Hawk, the chairman of the board and CEO of HEAF, the Higher Education Assistance Foundation. We welcome you here and look forward to hearing from you.

STATEMENT OF RICHARD C. HAWK, CHAIRMAN, HIGHER EDUCATION ASSISTANCE FOUNDATION, OVERLAND PARK, KS

Mr. HAWK. Thank you very much, Mr. Chairman.

As you know very well, the Higher Education Assistance Foundation has been a participant in the effort to meet the needs of students through loans to assure access to postsecondary education for the past dozen years. That has been a distinct privilege for us to participate in that process. After all, it is through access to postsecondary education in this Nation that we provide for social mobility, that we provide for individual opportunity, that we transmit the cultural heritage, that we create the opportunity for individuals to make the most of themselves and live richer, fuller lives. And it has been a distinct pleasure for us to participate with you in some small way in making that educational opportunity available to the citizens of this Nation.

I must also say that throughout this process we have been absolutely delighted with the support of the Congress, the leadership of this committee, the commitment of the chairman of this committee. I know you have had a long-standing ideal in terms of making 14 years of postsecondary education generally available to the population. We have shared that goal with you.

I think you know, Mr. Chairman and Senator Kassebaum, that the Higher Education Assistance Foundation has been committed to full access, that the Foundation has done more than that, even, in that the Foundation has made a special effort to meet those needs of those populations who have had a particular problem in obtaining access to postsecondary education. And you will recall our special efforts to provide assured access to programs for the United Negro College Fund institutions where there was a problem, to the LULAC organization, to a number of geographical areas, and certainly to the Nation's vocational schools where access to loans has not always been generally available as it has been to students attending 4-year institutions.

Unfortunately, Mr. Chairman, as we have sought diligently to meet the needs of those students and to cover and fulfill the obligation with respect to those pockets of access difficulties, we have been the victim of an adverse selection or an imbalance in portfolio which is difficult for an organization to manage, given the limitations on a guarantee agency with respect to sources of revenue to obtain reserves to cover defaults on loans.

As you know, the Higher Education Assistance Foundation experienced a loss of some $54 million in fiscal year 1989. We experienced a budget deficit. As you also know, the Higher Education Assistance Foundation has continued to take heavy losses during fiscal year 1990, and those losses are as a result of the high concentration of trade school loans which emerged in the Foundation's portfolio during the past several years.

In 1986, we recognized that as our total volume continued to increase, vocational loans were increasing at a more rapid rate than other types of loans. That is a problem for a guarantor because the default rate on borrowers in vocational and trade schools is higher than the default rate among students who attend 4-year institutions.

I want to be quick to add, Mr. Chairman, that that does not necessarily mean that there is something wrong with the Nation's vocational and trade schools. There have been some abuses. But I think there is an inherent difference in the default rate which will be with us probably forever, as we move from one category of borrower to another category of borrower.

It is a fact that trade schools serve a larger segment of low-income students than do 4-year colleges and universities. It is a fact that a number of trade schools are located in inner cities where the problem is particularly difficult, and there are a number of circumstances which causes there to be an inherent difference in the default rate among types of institutions. But the point is the Higher Education Assistance Foundation, having achieved a peak in volume in 1987 of $3.3 billion annual volume, got into a situation where 70 percent of that volume was not to students attending 4-year institutions but was to students attending shorter-term school. With only 30 percent of the loans being originated going to students attending 4-year institutions, we experienced the kind of portfolio imbalance which a guarantor cannot handle given the limitations on a guarantor with respect to sources of revenue.

As you know, Mr. Chairman, for good reason, there is a limit of three percent on the guarantee fee which a guarantor may charge for guaranteeing a loan. That serves a good purposes. It stops guarantors from charging an exorbitant fee. It has a negative ramification, however, for a guarantor which has an imbalance in its guarantee portfolio. One cannot collect three percent, guarantee loans which default at the rate of 50 percent, and stand 20 percent of the cost of those 50 percent defaults. I don't care what kind of arithmetic you use. The three percent that you charge is not sufficient to cover the defaults which you have to bear under that kind of circumstance.

Now, if there is adequate mutualization in the Guaranteed Student Loan program—that is, if all guarantors have a balanced portfolio with the same proportion of 4-year borrowers—community college borrowers, vocational school borrowers, the program works pretty well. The three percent then is adequate to cover the risk.

When you get into a situation where there is maldistribution, where there is adverse selection, or where there are differences in the mix of the portfolio guaranteed by individual guarantors, problems are created. Some guarantors with a profitable portfolio come out very well. They become profitable organizations and accumulate excess funds. Other organizations which serve a higher proportion of higher risk loans have great difficulty. They end up with a shortfall. You have in that situation an absence of the mutualization of the risk which is necessary in order for the program to function effectively when you have a limitation on the amount which the insurer can charge in order to cover the risk.

Now, there are a number of possible solutions to this problem. One obvious possible solution simply is to remove the limitation on the guarantee fee so that the guarantor has the opportunity to charge whatever is necessary in order to cover the risk for the kind of portfolio which is being guaranteed. That obviously has some disadvantages.

There are other kinds of alternatives in terms of changing the reinsurance formula. As you know, Mr. Chairman, reinsurance formula penalizes an organization which serves a high-risk population. If you serve a low-risk population, you get 100 percent reinsurance. If you serve a high-risk population, you get only 80 percent reinsurance. You have to figure out some way to make up the shortfall.

Well, Mr. Chairman, those are the kinds of problems that the Higher Education Assistance Foundation have been grappling with in attempting to continue with respect to its responsibility to assist you in providing access for the Nation's youth with respect to postsecondary education. If I may say, Mr. Chairman, I am, indeed, proud of the way in which our staff has performed in managing this very difficult situation, and I want to commit to you that we will continue to do everything that we can to come to a satisfactory resolution. We are paying default claims, and we will make every effort to continue to provide the highest level of service that we can possibly provide.

But I think you now understand that it is that maldistribution, it is that portfolio mix, it is that adverse selection, the lack of opportunity to modify revenue to cover defaults which creates the problem which we are experiencing.

Thank you.

Senator PELL. But you mentioned, Mr. Hawk, the maldistribution. That was a question of judgment. How did you come to make the judgment that you would accept 70 percent proprietary or taxpaying schools?

Mr. HAWK. Mr. Chairman, Senator Kassebaum, the guarantor does not on an individual basis make a decision with respect to which loans are going to be guaranteed. A guarantor has a relationship with lenders. It is the lender who decides which loans should be made. The guarantor has an obligation to make every loan which is presented to it under a legitimate lender agreement, provided that that loan is eligible under the terms of the program. The guarantor does not make an individual decision with respect to individual loans to be guaranteed.

I will say to you, Mr. Chairman, that the Higher Education Assistance Foundation is guilty of having been responsive to providing the guarantee for populations which are high-risk populations. The Higher Education Assistance Foundation I think also made an error in judgment because the Higher Education Assistance Foundation did not understand at the outset that once we started guaranteeing loans for students attending a particular institution that there was no circumstance under which we could stop guaranteeing loans for students attending an institution, unless we found some program violation at that institution. We learned that when we attempted to withdraw.

I must say for the benefit and defense of the actions of the Department of Education that the Department of Education was responsive in coming up with the plan under which by withdrawing from an entire State we then could stop guaranteeing loans for some high-default institutions located in those States. But that solution was a bit long in coming, and that is, in my judgment, if I may, Mr. Chairman, a very cumbersome way in which for a guarantor to have the opportunity to deny guaranteeing some types of loans, to have to withdraw from an entire State in order not to——

Senator PELL. I still don't think you answered my question, which is, to simplify it, why did HEAF take in so much more high-risk paper than did other similar guarantee agencies around the country?

Mr. HAWK. Mr. Chairman, HEAF does not have an opportunity, as loans come in, to make a decision as to whether or not the individual loans should be guaranteed unless the loan is ineligible under the criteria established under the program. It is the lender who decides which loans should be originated. HEAF had agreements with a number of lenders who, at their choosing, elected to originate high volumes of loans to students attending vocational schools.

I must say, Mr. Chairman, at some points in time, we in effect aided and abetted that. We encouraged lenders to meet the needs of all students, to provide total access, and to serve all segments of the population. So we are not without guilt with respect to that.

We did not anticipate that the volume of loans to trade school students would increase at the very rapid rate which it increased in our portfolio. We didn't, in all honesty, frankly, at the time we were doing it quite understand that when it began to increase so much and we wanted to slow it down, that there were no mechanisms at our disposal to do it.

Senator PELL. But why would this same phenomenon not have occurred in other parts of the country? Why is it HEAF is the one that stands out as being most in trouble?

Mr. HAWK. Well, Mr. Chairman, I should point out that it is not a geographical difference. As you know, the Higher Education Assistance Foundation guarantees nationwide. So it is not something peculiar to a geographical area.

The answer as to why we have a higher concentration of vocational loans than other guarantors is a complex one, indeed. There is competition, frankly, for the more profitable guarantees, guarantees to students attending 4-year institutions. There is not the same kind of competition for students attending trade schools where the default rate is higher. Because the default rate is higher, trade school loans are not very attractive loans for a guarantor to receive. So that competition doesn't exist there. So I think we suffered from a lack of competition for trade school loans.

Second, I am not at all bashful about saying I think the quality of service provided by the Higher Education Assistance Foundation is superior. We provide good turn-around time. We are very dependable for institutions, and I think there were a lot of institutions and a lot of vocational schools and lenders serving vocational schools who wanted to take advantage of the services which the Foundation can provide.

Senator PELL. In 1987, I attached a measure to the education part of the trade bill that would have permitted guarantee agencies to withdraw their guarantees for any schools, educational institutions with default rates in excess of 25 percent; in other words, knock them out completely. Had the House agreed to this provision, would we be in this situation we are today?

Mr. HAWK. Mr. Chairman, had the House agreed to that provision, we would have been in a position to withdraw our guarantee from institutions more easily than we certainly can under the present rules. That certainly would have eased the situation. Whether or not it would have completely solved the problem depends upon the timing when it was actually implemented. But it certainly would have gone a long way.

Senator PELL. As pointed out in the earlier testimony, of the 2,000-odd institutions, only 20 have been responsible for a high proportion of the defaulted loans, and those, it would seem to me, would have been knocked out by this 25 percent rule. Wouldn't that be correct?

Mr. HAWK. I agree with that, Mr. Chairman.

Senator PELL. Do you see a comparison between this and the S&L crisis?

Mr. HAWK. I do not, Mr. Chairman. The only similarity that I see is that there is an institution, the Higher Education Assistance Foundation, that has had two fiscal years now of experiencing losses. That does not create the kind of nationwide industry crisis that we see in the S&L program. I think this is a manageable problem, and I don't think there is any reason for any kind of panic or automatic suggestion that somewhere this has something to do with the S&L crisis.

Just the fact that S&L's are having difficulties, everybody automatically now, when they see some kind of problem, assumes or is fearful that might be similar. I don't think it is.

Senator PELL. Are you keeping up your due diligence standards at this time in this period of crisis?

Mr. HAWK. Indeed, we are, Mr. Chairman.

Senator PELL. Is it correct that you cut and mailed $37 million in checks before Sallie Mae afforded you the $200 million loan?

Mr. HAWK. I am sorry, Mr. Chairman.

Senator PELL. Did you cut and mail $37 million in checks before Sallie Mae agreed to forward up to $200 million to you last week?

Mr. HAWK. Mr. Chairman, we did not. If I understand what you are referring to, we did put in the mail checks for payment of default claims in approximately that amount—I think it was $35 million, something like that—after having signed a new lending agreement with the Student Loan Marketing Association for the advance of the funds equal to that. Those funds had not as yet been advanced on the day that we put those checks in the mail, but we checked very clearly under Minnesota law—because it was Minnesota where they were mailed from—and it was very clear under the law of that State that you are entitled to go ahead and mail checks under that circumstance where you have a definitive agreement for funds to be provided immediately thereafter.

Senator PELL. Thank you.

Senator Kassebaum.

Senator KASSEBAUM. Thank you, Mr. Chairman.

Mr. Hawk, I would like to walk through some of this a bit to further my understanding. When you get from a bank, say, or a lender a request to cover their loans, if it is a Kansas lending institution, you are required to take those loans; is that correct?

Mr. HAWK. Senator Kassebaum, as the designated guarantor, the Higher Education Assistance Foundation has a legal obligation to guarantee all loans in the State of Kansas, in the State of Minnesota, in the State of Wyoming, in the State of West Virginia, and in the District of Columbia. That is correct.

Senator KASSEBAUM. Because you are the designated guarantee agency in the District of Columbia?

Mr. HAWK. That is correct. In addition to that, Senator Kassebaum, if I may, once we enter into a lender agreement with a lender, even if they are outside of those States, once we have the lender agreement in place we are obligated to guarantee loans made by the lender, as long as the individual loan is eligible under the rules of the program.

Senator KASSEBAUM. But you just recently—I don't know how long ago—removed yourself from 18 States.

Mr. HAWK. That is correct, Senator.

Senator KASSEBAUM. Because you weren't the designated agency in those states?

Mr. HAWK. We were not the designated guarantor there, and the only way that we could stop guaranteeing for some high default institutions, where we were getting a dramatic imbalance in loans from some States, was to withdraw entirely from those States. And we did that in July of 1988.

Senator KASSEBAUM. Now, any agency that is not a designated guarantor has greater latitude as far as what they can accept or reject?

Mr. HAWK. Senator, I have to be very careful here because we have had differences of interpretation with the Department of Education, and over time, we have come to have a different conception of how much flexibility a guarantor has. My present understanding is that once a guarantor has started guaranteeing loans or providing service to any lender or any school, the guarantor may not withdraw service from that lender or school unless it withdraws completely from the State in which that lender or school is located.

As I understand the rules, prior to beginning to provide service to any lender or a school, the guarantor has full discretion so long as they are not the designated guarantor. My understanding based on the department interpretation of the law is that once a guarantor agrees to guarantee loans for any lender or any school any place, the guarantor has to continue with that service unless, through LS&T procedure—limitation, suspension, and termination procedure—the agency is able to identify program violations which permits a termination, or unless the guarantor withdraws completely from that, as the department calls it, area of service, which means withdraws completely from that State.

So in the first instance, if you are the designated guarantor, you have an obligation to guarantee all loans in that State which are eligible. In the second instance, outside of the State in which you are the designated guarantor, once you begin guaranteeing for a school or for a lender, you are obligated to continue doing so in the absence of a program violation unless you withdraw completely from the State in which that lender or school is located. That is my understanding of the current interpretation of the Federal law.

Senator KASSEBAUM. What is the advantage in being the designated guarantor?

Mr. HAWK. Senator Kassebaum, at one time there was the advantage that some Federal Reserve advances were made available to the guarantor. The Higher Education Assistance Foundation did receive some Federal Reserve advances in States where it was the designated guarantor, as every other guarantee agency does. The Higher Education Assistance Foundation voluntarily returned all those Federal advances in I think 1983. Subsequent to that, all guarantors have been required to return Federal Reserve advances. Once there are no longer any Federal Reserve advances, the only advantage to being the designated guarantor that I know is purely cosmetic.

Senator KASSEBAUM. Now, a lender must take all student loans within their lending State. Let's say a bank in Kansas would be required to take all student loans from Kansas students?

Mr. HAWK. Senator, I do not think that is true of an individual lender. I think individual lenders have some discretion with respect to the volume of loans that they wish to originate, and they have some discretion with respect to individual loans. They have to be a little careful about discrimination. But aside from that, there is no requirement that a commercial lender make all of the loans for which applications are presented to it.

There is a requirement that every State have a last resort guarantor. In the State of Kansas, that is the higher education loan program of Kansas. There is a requirement that if the last resort lender does not make all loans which are not made by commercial lenders, then the guarantee agency must not only guarantee but also make loans to students remaining in need.

Senator KASSEBAUM. Well, for instance, it is my understanding that Chase Manhattan Bank does not make any student loans for proprietary schools; is that correct? Or do you know?

Mr. HAWK. Senator Kassebaum, there are a number of lending institutions which have elected not to make loans to trade school students.

Senator KASSEBAUM. That is right. That is just one example.

Mr. HAWK. That is one example.

Senator KASSEBAUM. So what that means is, of course, there is a greater burden of loans which may or may not be necessarily the blue ribbon loans that have to be taken care of somewhere?

Mr. HAWK. That is correct.

Senator KASSEBAUM. Let me ask you what happens in your situation or in any of the other guarantee agencies, with the paper that you hold at the beginning of the new fiscal year. What happens then in the evaluation of one's default ratio? Does that stay the same year after year, or is it recalculated?

Mr. HAWK. Senator, at the beginning of every year, there is a recalculation. The formula is loans which default in a year divided by the original principal amount of loans in repayment at the end of the previous year. So at the beginning of each fiscal year, a guarantor starts over with 100 percent reinsurance until the defaults, based on that formula, equal 5 percent. Then it goes to 90 percent for the next 4 percent, then to 80 percent thereafter. So the higher the number of defaults, the less the Federal reinsurance.

Senator KASSEBAUM. Well, I understand that, but right now you are getting about 80 percent reinsured.

Mr. HAWK. That is correct.

Senator KASSEBAUM. I assume your loan situation won't change a lot between now and October 1. Certainly, it is a difficult situation which the Department of Education said will be resolved. But if it isn't resolved, by October 1, the beginning of the new fiscal year, you start all over again with 100 percent reinsurance? Would that not be correct?

Mr. HAWK. That is correct, Senator. Right now, for the State of Kansas, we are not submitting any default claims to the Department of Education for reimbursement. The reason we are not is because we would suffer the 20 percent shortfall which we couldn't handle right now. October 1, or actually before October 1, after about the middle of September, we will submit those claims, and they will be counted toward the next fiscal year. And for a brief period of time, we then will have 100 percent reinsurance again.

Senator KASSEBAUM. Mr. Chairman, if I may follow this line just a moment.

Senator PELL. Please.

Senator KASSEBAUM. I suppose on paper you could make the argument, then, if you can just sit on this until October 1, you are okay.

Mr. HAWK. That is true, Senator.

Senator KASSEBAUM. Am I misreading that?

Mr. HAWK. That is true, Senator, temporarily. But then, of course, we very soon will get back into less than 100 percent again.

Senator KASSEBAUM. Well, I know. I am not arguing that solves the problem. I am just saying it seems to me that it confuses the issue.

Mr. HAWK. It confuses the issue.

Senator KASSEBAUM. Particularly in any guarantee agency right now that may be in an uncertain situation.

Mr. HAWK. Senator, it does confuse the issue. I would like to say for the benefit of the peace of mind of those who are concerned about paying default claims, as long as we have in place a credit facility which we now have with the Student Loan Marketing Association—they have just agreed to provide some additional funding in their credit facility. As long as we have in place a credit facility to help us with liquidity, we are not in any jeopardy of not paying default claims between now and the end of the fiscal year. Certainly, as you suggest, at the beginning of the fiscal year, then on some portion of those claims we hold we will once again get 100 percent reinsurance.

If we had sufficient liquidity and opportunity to work through this thing where we have this large bulge of higher-risk, high-default paper moving through the Foundation's portfolio, long-term we would have a pretty good situation because, as we withdrew from 18 States and took some other steps in order to change the mix in our portfolio—which unfortunately meant denying access to some students. But as we did that, we turned the mix around completely. So right now in the volume which we are generating, 70 percent is to students attending 4-year institutions. That is quite a viable situation long-term, but we still have the bulge of defaults from that high concentration of trade schools which we guaranteed particularly 1986, 1987, and 1988.

Senator KASSEBAUM. Thank you very much.

Senator PELL. Thank you. Thank you very much for being with us, Mr. Hawk.

[The prepared statement of Mr. Hawk follows:]

STATEMENT

Richard C. Hawk, Chairman,
Higher Education Assistance Foundation

Before the
Senate Subcommittee on
Education, Arts and Humanities

August 3, 1990

Mr. Chairman and Members of the Subcommittee:

Thank you for inviting me to appear before you today. Although the circumstances surrounding this hearing are difficult at best, I am pleased to be able to set the record straight about the Higher Education Assistance Foundation (HEAF) and the challenges and difficulties it faces. In my testimony today, I intend to provide you with a candid description of how our current difficulties evolved, the nature of those difficulties, what we have done to date to remedy the situation and what we have proposed to do to resolve the problem. Additionally, I will comment on the implications of the Foundation's situation for the entire student loan program and suggest some measures that may forestall future problems.

The origins of HEAF's difficulties

HEAF's current circumstances are the direct result of several factors:

- HEAF's historic commitment to assure all eligible students -- regardless of their past educational achievements, economic circumstances, state of residence or the kind of school they were attending -- of equal access to the guaranteed student loan programs.

- The changing demographics of student borrowers in the loan program as grant support declined.

- The development of state-of-the-art services for students, schools and lenders that proved most attractive to trade schools.

- The limited ability of guarantee agencies to finance the risk in their portfolios.

- The extraordinary abuses in the program by some schools and lenders, abuses that directly affected HEAF's financial strength.

The result of these events is that HEAF guaranteed an extraordinary proportion of trade school loans, half of which will default. This large proportion of trade school loans, about 31% of its current, outstanding portfolio, was insured by HEAF because of its commitment to assure all eligible, under-served students access to loans and its state-of-the-art computerized services. This began in the Spring of 1982 when Citibank, the Student Loan Marketing Association, HEAF and the United Negro College Fund jointly established a special loan program for students attending member institutions of the United Negro College Fund. A similar program for the League of United Latin American Citizens was established. Shortly thereafter the Hawkeye BanCorporation sought HEAF's services because of its dissatisfaction with the quality of services being provided by their guaranty agency and HEAF agreed to provide those services. Within a relatively short period of time, the major four-year institutions in South Carolina asked HEAF to serve their students because many could not obtain loans from the South Carolina agency and lender although the denied students were eligible to obtain loans under federal eligibility criteria. As representatives of under-served students and lenders approached HEAF for help, HEAF responded. Meanwhile, HEAF developed computerized processing systems that reduced the time required for students to obtain loans from nine to twelve weeks to a few days to provide improved services to students and schools. This advance in processing combined with HEAF's commitment to equal access proved most attractive to trade schools and, beginning in 1986, resulted in a skyrocketing volume of trade school loans.

As a consequence of its own efforts to provide state-of-the-art services to students, schools and lenders, HEAF guaranteed far more than its share of high-risk, high-default trade school loans. Furthermore, as it attempted to limit the eligibility of trade schools that wanted to begin using the HEAF services, it found that the law prohibited HEAF from imposing eligibility and certification criteria on schools more onerous that the Department's criteria.

Consequently HEAF deferred to the Department's judgement about the eligibility of institutions to participate in the student loan programs. Moreover, large pockets of under-served students were created when other agencies did not honor this provision. Furthermore, the "antidiscrimination provisions" of the law, as interpreted by the Department of Education, stated that once a lender or school had established a relationship with HEAF, program requirements that were intended to assure equal access and due process made it almost impossible for HEAF to reduce the flow of high-risk loans it was required to guarantee.

These provisions and HEAF's state-of-the-art services resulted in adverse selection in HEAF's portfolio. Let me explain what I mean by adverse selection. In an effort to serve all its customers well, HEAF developed state-of-the art services for students, schools and lenders that, as it developed, proved particularly attractive to trade schools. HEAF simply provided better, more timely service than other guarantors. The quick turnaround HEAF provided to all its customers was particularly attractive to trade schools for cash flow reasons. Hence, they directed their students toward HEAF instead of to other guarantors. Also, in an effort to avoid these higher risk loans, certain state guarantors encouraged trade schools in their states to utilize HEAF instead.

The flow of high-risk loans to HEAF was further increased as several national lenders with whom HEAF had an existing relationship began making massive numbers of loans to trade school students. Those lenders used the HEAF guarantee because it was available nationwide, and because it was administratively more convenient and more efficient to use a single guarantor who could guarantee loans for students in nationwide. Banks no longer are constrained to lend only in a limited geographic area and larger lenders serve customers in many states. Since profit margins on student loans are narrow, many lenders seek to reduce expenses by using a single source of guarantees for students in many states. HEAF met that lender need but the nationwide scope of HEAF's operations left us vulnerable to increased risk when some of our customers began to send us large volumes of high-risk loans.

HEAF did *not* seek to guarantee high-risk, high-default loans as a way to generate fee income. That would have been reckless and self-destructive, since the fees we are allowed to charge are not sufficient to cover the risk on high-default loans. By a change in law in 1986, a guaranty agency may charge a guarantee fee no greater than 3% of the loan amount. Hence, a guaranty agency has limited flexibility to charge a fee that is commensurate with the risk of the loan. It would have made no sense whatsoever to deliberately seek to increase our fee income by guaranteeing high-risk loans, and that was in fact not our strategy.

We did seek to honor the equal-access requirements of the program, thus making the HEAF guarantee available to students at trade schools as well as four-year schools. Our intentions were honorable, and we believe they were consistent with what Congress intended. However, because market forces directed a high volume of high-risk loans our way, HEAF guaranteed a disproportionate share of loans that default at a high rate, and the results were financially very detrimental to us. If the loans guaranteed by HEAF to students at trade schools were more evenly divided among guarantee agencies, all our agencies would jointly have the financial resources to cover all default expenses.

Why didn't HEAF simply stop issuing guarantees on the higher risk loans? The answer is that we tried, but that the options we believed were available to us were denied us by the Department's interpretation of the law and regulation.

Chronology of management action to reduce the volume of high-risk loans

The percentage of high-risk trade school loans in HEAF's guarantee portfolio began to rise in the early 1980s, from 8% in 1981, 10% in 1982 and 13% in 1983, to 22% in 1984. By 1985, when this trend began to threaten the health of our guarantee portfolio, HEAF began to take steps to correct the disproportionate number of trade school loans in the portfolio. Our first step was to encourage lenders to attempt to generate more balanced loan portfolios. At the same time, we encouraged secondary market organizations to stop paying premiums to acquire trade school loans.

By late in 1986, it was apparent that additional, more drastic measures would be needed if HEAF was to curtail the growing imbalance in its portfolio. Hence, management took several actions to deal with this emerging trend. These actions included:

1. In a departure from the industry standard, the Foundation revised its guarantee fee structure in April, 1987 to charge the maximum rate permitted by law (3%) for loans to students attending trade schools and offered its guarantee at no charge to borrowers attending four-year colleges and universities. Unfortunately, this rate structure had no discernible impact on the portfolio mix.

2. Also in April, 1987, the Foundation adopted a policy that required borrowers attending schools with a historical default rate of 40 percent or more to secure cosigners for their loans. This requirement had to be rescinded after the U.S. Department of Education advised us that such a policy might be interpreted to be "discriminatory".

3. Early in 1988, the Foundation moved to cancel its agreements with several major lenders who were bringing the Foundation $1.5 billion per year in loan portfolios which were more than 90% high risk paper. This effort was chilled by the Department of Education's expressed view that the Foundation would need to proceed under so-called "Limitation, Suspension, and Termination" procedures to cancel those agreements. In HEAF's view, it could not use L,S and T actions in the absence of violations of law or regulations, so it began searching for another approach.

4. The Foundation then proposed to review the eligibility of each school to continue use of the Foundation's guarantee after a future date. Again, the Department of Education determined that full "Limitation, Suspension, and Termination" procedures would need to be followed for each of the hundreds of schools which might not be approved under this approach. Again, no timely results could be obtained.

5. Fortunately, the Department of Education came up with an effective solution in June, 1988. The Department agreed that a guarantor may restrict access to its guarantee by geographic region. This ruling allowed us to evaluate our business on a state-by-state basis. Eighteen states were identified whose 1987-88 loan volume consisted of more than 80% high risk paper, and we announced our intent to withdraw from those states as of July 15, 1988.

6. Between Marcn, 1988 and July, 1988 HEAF guaranteed about $500 million in loans from the lenders who were subjected to the actions in 3. above, which resulted in a unrecoverable cost to HEAF of $50 million.

In withdrawing from the 18 states, the Foundation gave up more than $1 billion per year in loan volume, with 93% of that volume representing other than four-year institutions. The objective sought by management was to restore a balance portfolio mix where no more than 40% of new guarantee volume came from trade schools.

The decision to withdraw was made difficult by three major considerations:

1. The loan volume abandoned represented at least $30 million per year in cash receipts as well as at least $10 million per year in Federal Administrative Cost Allowance. The Foundation would experience two years of reduced cash receipts before it began to realize the benefits of substantially reduced default expense.

2. Some valued customers would be inconvenienced, particularly regional and national lenders who simply did not want to deal with a variety of local guarantors.

3. Even though management was confident that the withdrawal strengthened the Foundation's long term viability, it was felt that others in the industry--primarily competitors--would draw attention to the short term negative financial impact.

The actual results secured by our action were dramatic and even more beneficial than anticipated. The proportion of trade school loans in our insured portfolio is rapidly dropping because the proportion of trade school loans which we are now insuring is less than 30% of all insured loans. Today our portfolio contains about $3 billion in insured loans for trade school students, $400,000 million of which are in "in-school or grace." The remainder are in repayment.

As you have seen, HEAF has been endeavoring to resolve the rapidly growing imbalance in its portfolio for five years now, but we have been hampered by unfortunate interpretations of the regulations and the inflexibility that has been built into the program. Even a guarantee agency with extremely vigilant management such as HEAF's is limited in the steps it can take to control the lenders or schools that are the source of the high-risk paper.

Current situation

An additional issue I want to address forthrightly is the view that HEAF's growth necessarily was at the expense of quality, and that thus excessive default rates were an inevitable byproduct. The facts simply do not support this view. While HEAF has indeed achieved significant economies of scale, such economies have not come from diminished effort.

- HEAF subjects each loan application to over 500 of edit criteria before issuing a guarantee. Even so, applications are typically processed within 24 hours.

- HEAF's default-aversion programs "cure" more than 60% of delinquencies reported to us by our lenders.

- By utilizing more than 200 in-house collectors, 12 collection agencies and a national network of law firms, HEAF will collect more than $100 million in defaulted loans this fiscal year.

- HEAF's dedicated compliance staff has identified program violations and imposed liabilities problems and imposed penalties that returned $2 million to the program during the past fiscal year and resulted in "L,S and T actions against 35 schools.

- HEAF's claims examiners reject almost 15% of submitted claims as a result of detecting violations of due diligence requirements and impose interest limitations that save the program an average of $750,000 per month.

- Despite this thoroughness, our cost efficiency, according to Department of Education data (defined as operating expense less collection costs, divided by the number of loans guaranteed) is greater than all but four other guaranty agencies.

A dozen representatives of the Department of Education and the Office of Management and Budget spent last week critically examining HEAF operations on site. We are confident that they will confirm the high standards of performance to which HEAF adheres.

Mr. Chairman, my remarks in this regard are designed to meet two objectives:

First, I believe that the management and staff of the Foundation deserve to have me respond to the comments of recent weeks that reflect on their competence and dedication. Their performance is now, and has always been, the finest of any guaranty agency participating in the program. HEAF is one of the most efficient agencies in the country, with an exceptional record of developing innovative and needed services for students and schools, of recovering defaulted student loans and of uncovering and ending abuses in the Guaranteed Student Loan Program. Second, HEAF's demonstrated efficiency and effectiveness suggests that its technological resources and its experienced and dedicated staff are valuable to the continued stability and viability of the loan program.

Despite the immediate difficulties we face, our situation can best be summarized as follows:

- HEAF's action of July 1988 to curtail a growing portfolio imbalance was indeed successful, and our current-year guarantee volume consists primarily of highly desirable college and university loans. In other words, the required corrective action was taken two years ago, and it has clearly succeeded.

- The financial stress now faced by the Foundation is not part of a continuing downward trend. Rather it is the tail-end of a period of reduced revenues and expanded costs as we digest the last of the high-risk loans guaranteed before corrective action was taken in 1988.

- An additional burden on our reserves in the short term is posed by the imminent resolution of a long-standing matter relating to the Bank of America. This matter surfaced in June of 1988, when HEAF's compliance team discovered major irregularities in the servicing of a loan portfolio for which the Bank of America serves as trustee on behalf of the California Student Loan Finance

Corporation. HEAF immediately reported its findings to the Inspector General of the Department of Education. Following a joint review, the Department directed HEAF to suspend all claim payments from this portfolio. Over the past two years, intensive negotiations have taken place between the Department, the Bank of America, HEAF and the two other guarantors involved to identify a fair and mutually acceptable resolution of this situation. HEAF guaranteed $565 million of this $1.1-billion portfolio, and the default rate is expected to be between 60% and 75%. Under the proposed settlement agreement, these figures pose extraordinary potential cost and cash flow consequences for HEAF.

- HEAF was in the process of pursuing a plan to transfer certain loans to, and ultimately to merge with, the Nebraska Student Loan Program (NSLP). Because it is a new guaranty agency, Nebraska temporarily receives 100% reinsurance from the federal government regardless of the percentage of default claims which it submits to the Department. The merger would have allowed HEAF to receive 100% reinsurance for the next year, which should have been enough time for the last of the extremely high-default portfolio to work its way through the system. At that point in time, the long-term correction created by the new portfolio mix would have taken effect, and the problem would have been solved. However, the Department raised objections to our proposal.

We disagree with the Department on the legality and viability of our proposed transfer of loans to, and merger with NSLP, and we do not believe it is necessary for the Department to seek an alternative solution. Having said that, we will continue to provide our full cooperation as they explore other options. Our goals in those deliberations will be to ensure that the long-term viability of the Guaranteed Student Loan Program is protected and that the Foundation's employees who have served so expertly and diligently will be treated with fairness.

Implications for the future of the program

The Higher Education Assistance Foundation was created nearly a decade and a half ago out of a belief in the goals of the Guaranteed Student Loan Program. We all share a wish that the program continue meeting its laudable goals. As you view HEAF's situation today, it is essential that you consider its implications for the future success of the entire program.

Preserving assets

A central goal in the resolution of the situation we face is the protection and preservation of two great assets--our staff and our technological resources. We are proud beyond measure of the manner in which, under the most trying of times, our loyal, dedicated and incredibly talented team has managed its responsibilities. It is a reaction we knew we could expect, since they are the ones who have made us one of the most respected and efficient guaranty agencies in the country. Their dedication to our mission, and to the students, schools and lenders we serve, has been unwavering.

Our computer system is unparalleled in the industry. We have invested a great deal of effort in the development, construction and implementation of this system over the past three years, and that investment has paid huge returns in the form of service that is both responsive and responsible. It is responsive in that it conforms easily and efficiently to the needs of lenders, both large and small, permitting easy customizing; it is responsible in that it has built-in checks and edits that virtually eliminate programmatic violations and data inconsistencies. It has allowed the Foundation to issue guarantees quickly, while eliminating compliance errors. These technological and human resources, combined with our infrastructure, procedures and operating standards, form a highly effective and efficient operating unit that would be time-consuming, expensive and difficult to replicate.

If the Guaranteed Student Loan Program continues at approximately its present level of activity--and there is every reason to believe that it will--the nation will continue to need the Foundation's capacity if we are to ensure continued service levels. The long-term cost of re-establishing this pool of experience, expertise and dedication would be high, not to mention altogether unnecessary.

Creating new opportunities

If the growing number of high-risk trade school loan guarantees is at the root of HEAF's financial woes, then the solution may seem obvious to some: reduce or eliminate the federally backed guarantee for loans to students at such schools. Yet to take such a step would be to deny thousands of students the opportunity to improve their standard of living and make a greater contribution to society as a whole.

If a student wishes to study to be a court reporter, a diesel mechanic or a computer technician, he or she has as much right to federally sponsored student lending as a student who wishes to study physics, English or sociology. Society values both categories of students equally, and the Guaranteed Student Loan Program must continue to do likewise. Clearly, additional steps will need to be taken to weed out the illegitimate trade schools that prey upon taxpayers and students alike. Yet the program must at the same time continue to allow for the legitimate interests of post-secondary students whose needs are not met by four-year colleges and universities.

Providing flexibility for guarantors

Another lesson of HEAF's experience over the past several years is that, while a great deal of risk is laid at the feet of the nation's guaranty agencies, little control over the level of that risk is placed in their hands. Unlike a typical insurance program, or for that matter a typical lending program, the risks and the rewards are not distributed in a way that provides an incentive both to serve a broad cross-section of students and, at the same time, to remain in viable financial condition. Some possible improvements:

- The existing trigger formula, which was designed for a different era, could be replaced with a formula that provides greater, rather than lesser, reinsurance to agencies that bear the burden of an unfavorable mix of loans. Rigorous controls could be instituted to discourage lack of diligence in weeding out fraudulent and irresponsible lending practices.

- The ceiling on the guarantee fee could be eliminated, granting each guarantor the opportunity to establish a fee at the level necessary to cover losses.

- Another possible solution would be to prohibit guarantors from guaranteeing loans for students who are neither residents nor attending school in a state in which they are the designated guarantee agency. The disadvantage of this alternative is the inconvenience it offers to lenders doing business across state lines, yet it would help avoid the high concentration of trade school loans from disparate sources from being guaranteed by a single agency.

Closing

Thank you for giving us this opportunity to present our perspective on this important matter. As always, you may expect our full cooperation and assistance as you seek to resolve issues for the benefit of the schools, students and lenders the Program serves.

Senator PELL. Now we will turn to our first panel: Mrs. Jean Frohlicher, executive director of the National Council of Higher Education Loan Programs; Stephen Biklen, vice president of Citibank Student Loan Business; Mr. Lawrence Hough, president and chief executive officer, Student Loan Marketing Association.

We welcome you here, particularly Mrs. Frohlicher, who has been used to being on this side of the dais, not that side. She did a wonderful job when she was on this side of the dais.

Mrs. Frohlicher, you know the rules. The bells are set up for 5 minutes, and we will try to roll along as much a we can.

STATEMENTS OF JEAN S. FROHLICHER, EXECUTIVE DIRECTOR, NATIONAL COUNCIL OF HIGHER EDUCATION LOAN PROGRAMS, INC., WASHINGTON, DC; STEPHEN C. BIKLEN, VICE PRESIDENT, CITIBANK STUDENT LOAN BUSINESS; ROCHESTER, NY; AND LAWRENCE A. HOUGH, PRESIDENT AND CHIEF EXECUTIVE OFFICER, STUDENT LOAN MARKETING ASSOCIATION, WASHINGTON, DC

Mrs. FROHLICHER. Thank you, Mr. Chairman. I must confess it was more comfortable on that side of the table.

My name is Jean Frohlicher, and I am executive director of the National Council of Higher Education Loan Programs, which represents State and nonprofit private guarantee agencies and secondary markets involved in the Guaranteed Student Loan program, as well as major lenders, servicers, collectors, and other organizations involved in the provision of credit to students.

I think the committee is well aware of the magnitude of this program. Last year it made available nearly $13 billion in private credit to more than 4.7 million borrowers. We are the second largest source of credit for postsecondary education in the country after parental contributions themselves.

Much press has been given to the difficulties encountered by the Higher Education Assistance Foundation, and I think that I would like to reinforce the statements that have been made here this morning. It is our belief the program is fundamentally sound. Guarantees are going forward as we speak, in Rhode Island, in Kansas, and in all the other States in the country, and we have no belief that any student will be denied access to credit this fall.

Senator PELL. Could you move the mike a little closer?

Mrs. FROHLICHER. Certainly, sir.

There has been discussion about the 4 to 5 agencies that might be in trouble. I don't know who those are. I think that this may be because of cash flow the agencies must, as has been discussed here this morning, work due diligence on the paper after they purchase the claim from the lender, and there may be as much as 90 days between when they have paid the lender and when they are able to seek reimbursement from the Federal Government.

Currently 7 agencies are operating under some kind of reduced reinsurance because they have hit the basic trigger. The Department of Education, in enforcing the reconciliation spend-down legislation, was extremely enthusiastic in doing that enforcement and has already collected the $250 million in agency reserves that otherwise would be used to pay default claims, even though the litigation is still proceeding on that law.

A little over 2 weeks ago, the NCHELP board of directors adopted a reauthorization proposal to present to this committee next year in the regular cycle. We recognized that we were very early in the timing of the Higher Education Act reauthorization, but as we all thoroughly discussed, this was a living, breathing, and ongoing effort, and we expected ramifications and changes to make changes in our position.

I hadn't expected it to twitch within 8 hours of its adoption. But I would like to assure the committee that we are going to, as a result of this problem, be taking a new and very critical look at the entire underlying questions of agency solvency, how the various cash flows in the program do work, and try to make some solid recommendations as part of your regular reauthorization process next year, so that we can assure that this situation is not possible.

There are a number of policy-oriented things that the committee may want to do that we recommend that you do and you have discussed today: the redress of what is now a critical imbalance between grants and loans; perhaps tightening up of eligibility of various kinds of schools and their participation in the program. All of these lead to an essential downsizing of the loan program in general as it becomes less relied upon for basic access. And we need to make sure that the program sources of funding to guaranty agencies and to uses by them do not impair your ability to make those kinds of policy decisions.

Right now funds flowing into agencies derive from current year volume. Funds flowing out of agencies in the form of claim payments are based on past practice. And this is what we will be addressing specifically so that with it as part of your recommendations, our recommendations to you, you will have freedom to do conscious downsizing if that is what you decide to do, and not have a similar kind of cash flow based on the downsizing affect on agency stability.

This committee, Mr. Chairman, has been very active in taking strong anti-default measures. I wanted to report a few things that you would credit to your actions and your leadership in providing agencies with at least clear authority to take emergency suspension actions. California has already taken 31 actions; Texas has done 7 limitations, 12 suspensions, 4 terminations, 92 program reviews. Colorado has, within the past year, done terminations on 3 schools, one of which operated in 3 States. The list of sub-schools of one school covered almost 3 pages of single-spaced typing, and they are pursuing criminal activities again, actions against school officials. They already have had one guilty plea, and one goes to the grand jury next week. So within the limited authority agencies have to take action, they are taking action.

Finally, your restriction on the SLS program in high-default schools is already showing substantial impact. California projects if their efforts are mirrored nationwide we could expect to save in defaults nearly $120 million in the upcoming fiscal year 1991 and as much as potentially $885 million in fiscal year 1992 from that one change alone.

So we are grateful for the opportunity to appear, and I would be happy to answer any questions.

[The prepared statement of Mrs. Frohlicher follows:]

PREPARED STATEMENT OF JEAN S. FROHLICHER, EXECUTIVE DIRECTOR, NATIONAL COUNCIL OF HIGHER EDUCATION LOAN PROGRAMS, INC.

Mr. Chairman and Members of the Subcommittee.

My name is Jean Frohlicher, and I am the Executive Director of the National Council of Higher Education Loan Programs. The Council represents State and nonprofit private guaranty agencies and secondary markets involved in the Guaranteed Student Loan Program, as well as major lenders, servicers, collectors, and other organizations involved in the provision of credit to students attending postsecondary educational institutions.

As you know, last year the Guaranteed Student Loan Program provided nearly $13 billion in loans to millions of students and their parents for postsecondary education. Next to parental assistance, the Program is the biggest source of aid for college students. We are proud of our track record -- while much attention has been focused on default problems over the last few years, more than 90% of our borrowers repay their loans on a regular basis.

Much has been written in the past couple of weeks concerning the financial difficulties encountered by one of the Nation's largest guarantors, the Higher Education Assistance Foundation. I would like to assure the Subcommittee that the fundamental structure of the Guaranteed Student Loan Program remains sound. Lenders and guaranty agencies are prepared to meet the capital needs of borrowers across the country for this coming academic year, and I do not believe that any eligible borrower will experience difficulty in obtaining a Guaranteed Loan.

Departmental officials have been quoted as saying that another handful of guaranty agencies have financial difficulties, although not on the scale of those experienced by HEAF. I do not know which guaranty agencies the Department is referring to. Every agency experiences cash-flow problems at some point, as lender claims are paid as much as 90 days before the agency can file for Federal reinsurance. In any given fiscal year, several guaranty agencies experience default claims in excess of 5% of their outstanding loans in repayment and trip the reinsurance "trigger." It may have been this circumstance that led to the comment. The Department's enthusiasm in enforcing the 1987 Reconciliation bill's spend-down mandate by withholding payments for default claims until an agency's reserves were thoroughly spent-down (despite litigation which is still continuing) has also undoubtedly contributed to the current situation.

Changes in the Guaranteed Student Loan Program made both in the 1986 Reauthorization as well as in several subsequent Budget Reconciliation bills have affected the basic nature of the Program. The 1986 Reauthorization instituted needs analysis for all GSL borrowers. The net result of converting what had formerly been a middle-income cash-flow program into a needs-based program was obviously an increase in the number and costs of defaults in the

GSL program. Middle income borrowers, who could be counted on to repay their loans were no longer eligible for subsidized Stafford Loan borrowing. Shortages of available grant funds led poor students increasingly into GSL debt, and studies show that the primary reason borrowers today are not repaying their loans is their financial inability -- not their unwillingness -- to do so. Spend-down provisions of the 1987 Reconciliation Bill reduced guaranty agency reserves (used to pay lender claims) by $250 million.

Reauthorization of the Higher Education Act in the next Congress will give this Subcommittee an appropriate forum for an in-depth look at the current structure of the Guaranteed Loan Program. The Program has been in existence for 25 years; it needs the critical examination that this Subcommittee and the community can provide to assure its strength and viability for the next quarter century.

The HEAF experience has led the Council to plan a thorough analysis of the underlying structure of guaranty agency funding in the GSL Program as part of its Reauthorization effort. In essence, the way the Program is currently structured, funds flowing into an agency through Administrative Cost Allowances (paid by the Federal government) and through Insurance Premiums (paid by borrowers) are both dependent on loan volume in the current fiscal year. However, guaranty agency expenditures--primarily in the form of claims payments to lenders for defaulting, disabled, deceased, and bankrupt borrowers--are based on past volume. In HEAF's case, a calculated down-sizing of its portfolio (through its cessation of business in 18 States) meant substantially reduced income through fees but continued obligations to pay lender claims on previously-guaranteed high-risk paper.

This dichotomy in financing will need to be considered in Reauthorization if the Congress is to have the freedom to make policy decisions which may result in a lowered volume of loans. The decision in the 1989 Reconciliation bill, which was strongly supported by the Council, to deny Supplemental Loans to borrowers in high-default schools, is already having a significant effect in stopping the run-away abuse of the SLS Program. In its Reauthorization Paper, the NCHELP Board of Directors has already strongly endorsed redress of the grant-loan imbalance which has accumulated over the past decade. The Board has also gone on record against continued GSL eligibility for courses of study of less than 600 clock hours in duration, on the grounds that students in extremely short (300 hour) courses which probably lead only to minimum-wage jobs should not be saddled with debt they are patently unable to repay. Concern about agency finances, because of reduced income from a lower-volume Guaranteed Student Loan Program, should not deter Congress from making needed policy changes in the Reauthorization process.

Many of the anti-default measures enacted by this Subcommittee are beginning to show significant results. Guaranty agencies are taking aggressive actions against bad schools under the recently-authorized emergency L, S, & T procedures. SLS loan volumes in high default schools are dropping significantly, and there has been a concomitant drop in Stafford Loan volume in those schools which had artificially pegged their tuitions to the maximum Stafford/SLS loan limits. In fact, if California's experience during the first six months of 1990 is typical of the Nation's loan program as a whole, Fiscal Year 1991 default claim savings from the SLS change alone could reach $179 million, and the FY 1992 savings could be as much as $885 million.

Today, and for the foreseeable future, the Guaranteed Student Loan Program remains strong and vital. Guaranty agencies have indicated to the Secretary their willingness to consider assumption of HEAF loans made to borrowers from their designated States. The Council sees no basis for the Secretary to make the finding required by law that borrowers lack access and existing guaranty agencies are unable to serve such borrowers -- a precondition of recognizing Sallie Mae as a loan guarantor. Rather, guaranty agencies are discussing with the Department the outlines of a speedy, community-wide resolution of the current problem.

I appreciate the opportunity to appear before the Subcommittee. I would be happy to respond to any questions you might have.

Senator PELL. Thank you very much, Mrs. Frohlicher.

Mr. Biklen.

Mr. BIKLEN. Thank you, Mr. Chairman, members of the subcommittee. I am Steve Biklen, vice president of the Citibank Student Loan Business, and I am here today representing the Consumer Bankers Association, which is made up of more than 800 banks, thrifts, credit unions, and other organizations involved in providing consumer credit.

Throughout the last 3 weeks, CBA has supported the actions and statements of Secretary Cavazos indicating a commitment to ensure the integrity of the HEAF-guaranteed loans. When the Secretary indicated on July 24 that "HEAF-guaranteed loans will continue to be guaranteed"——

Senator PELL. Could you put the mike a little closer?

Mr. BIKLEN [continuing]. Sure. That "HEAF-guaranteed loans would continue to be guaranteed," lenders across the country participating in the program interpreted this remark to mean that the Secretary would ensure that a facility would be in place to meet the financial obligations represented by the HEAF guarantees, and he talked earlier about that. Even so, however, there is growing concern and unrest in the lender community that is evidenced by the fact that a number of lenders have ceased disbursing HEAF-guaranteed loans pending a resolution of this problem.

CBA believes that a speedy resolution to the problem is imperative. Such a resolution should protect against any disruption in the processing of claim payments. Similarly, any change in guarantee arrangements should be announced and formalized as early as possible so the making of student loans this fall can proceed without interruption.

CBA believes the preferred resolution to the HEAF problem is one that involves little or no disruption to existing guarantee arrangements. To this end, the financial arrangements that would enable HEAF to meet its current financial responsibilities should be fully explored. If it is necessary to transfer responsibility of HEAF guarantees to another party, CBA believes that the best approach is one involving multiple existing guarantee agencies.

It is important to emphasize, Mr. Chairman, that any handling of the HEAF situation that does not allay existing lender fears regarding the reliability of guarantees on guaranteed student loans could severely undermine the program. If HEAF guarantees are not fully honored, the following would occur:

Virtually all lenders would immediately cease placing new guarantees with any agencies that they felt had any difficulty. The Secretary has talked about 5 to 6 agencies. Clearly, there may be some that may have a problem. But the point is, if there was any doubt about it, they would cease placing guarantees there.

These weaker agencies would then experience an immediate drop in their cash flows, and that would only hasten their decline. And I think the ultimate result would be that lenders would establish very low limits with respect to the level of risk they were willing to take with any agency.

The cumulative impact of these developments would be the creation of access problems for borrowers, and particularly those from low-income backgrounds.

There has been considerable speculation regarding the circumstances contributing to the HEAF situation. As we heard earlier, clearly the high defaults cause this. And we do think that the legislation and regulation that has been put in place, which you referred to earlier, has had a definite positive impact and will, over time, significantly reduce defaults.

CBA does support changes to the program that will reduce the level of these defaults, and in this regard we certainly want to work with you in the future to establish more legislation. We do believe that additional legislation could help prevent a repeat of this situation. First, we think there are some changes that could be made with respect to improvements in the quality of education provided by schools and requiring that schools provide students with more consumer-related information related to the outcome of the educational program offered.

Second, the Department of Education should develop procedures for addressing the contingency of another guarantee agency experiencing financial difficulty. We were pleased that the Secretary earlier did reference this and noted the fact that they would be looking into this. And we are also pleased hearing Mrs. Frohlicher's testimony that NCHELP is looking into that.

In closing, CBA would like to emphasize its belief that with an appropriate resolution of the HEAF problem, the Guaranteed Student Loan program will continue to meet the educational credit needs of students and their families.

Thank you.

[The prepared statement of Mr. Biklen follows:]

PREPARED STATEMENT OF STEPHEN C. BIKLEN, VICE PRESIDENT OF CITIBANK STUDENT LOAN BUSINESS

Mr. Chairman, Members of the Subcommittee on Education, Arts and Humanities, my name is Stephen C. Biklen, Vice President of Citibank Student Loan Business headquartered in Rochester, New York. Thank you for the opportunity to appear before you today on behalf of the Consumer Bankers Association[1]. CBA represents more than 800 banks, thrifts, credit unions, and other organizations involved in providing consumer credit. The Association's policies regarding the student loan programs are set by an Education Funding Committee consisting of representatives from 18 financial institutions involved in the Guaranteed Student Loan Programs.

CBA has followed with great interest the financial problems experienced by the Higher Education Assistance Foundation (HEAF). Throughout the last three weeks, CBA has supported the actions and statements of Secretary Cavazos indicating a commitment to ensure the integrity of the HEAF-guaranteed loans. When the Secretary indicated on July 24th that "HEAF-guaranteed loans will continue to be guaranteed," lenders across the country participating in the program interpreted this remark to mean that the Secretary would ensure that a facility would be in place to meet

[1]The Consumer Bankers Association was founded in 1919 to provide a progressive voice for the retail banking industry. CBA represents approximately 800 federally insured banks, savings and loans and credit unions that hold more than 80 percent of all consumer deposits, and more than 70 percent of all consumer credit held by commercial institutions. It is estimated that CBA's membership also accounts for more than 80 percent of the total student loan volume in the U.S.

the financial obligations represented by the HEAF guarantees. This commitment to constructively resolve the HEAF problem is much appreciated by lenders participating in the program, and will help ensure that the availability of student loans to students this Fall will not be adversely affected in any way by the HEAF problem. Notwithstanding the statements of the Secretary, however, there is growing concern and unrest in the lender community evidenced by the fact that a number of lenders have ceased disbursing HEAF-guaranteed loans pending a resolution of the problem.

CBA believes a speedy resolution to the problem is imperative. Such a resolution should protect against any disruption in the processing of claim payments. Similarly, any change in guaranty arrangements should be announced and formalized as early as possible so the making of student loans this Fall can proceed without difficulty or interruption. CBA has every confidence that these objectives will be met and has offered its assistance to the Department to help ensure that this is the case.

CBA believes the preferred resolution to the HEAF problem is one that involves little or no disruption to existing guaranty arrangements. To this end, financial arrangements that would enable HEAF to meet its current financial responsibilities should be fully explored. If it is necessary to transfer responsibility for HEAF guaranties to another party, CBA believes that the best approach is one involving multiple existing guaranty agencies.

It is important to emphasize, Mr. Chairman, that any handling of the HEAF situation that does not allay existing lender fears regarding the reliability of guarantees on GSLs could severely undermine the program. If HEAF guarantees are not fully honored, the following would occur:

o Virtually all lenders would immediately cease placing new guarantees with the five or six agencies considered to be financially troubled.

o Weaker agencies would experience an immediate sharp decline on reserves from guaranty fees, hastening their decline.

o Lenders would establish a very low level of risk exposure to any single agency.

The cumulative impact of these developments could be the creation of access problems for borrowers, particularly those from low-income backgrounds and attending short-term courses of study. Obviously, the interests of the federal government and the students relying on the student loan program require that this scenario not be allowed to occur.

In recent weeks, there has been considerable speculation regarding the causes and circumstances contributing to the HEAF situation. It is worthwhile to note that the high level of defaults experienced on the HEAF-guaranteed student loan portfolio played a significant role in creating HEAF's current financial difficulties. In this regard, we should not lose sight of the fact that default reduction measures recently implemented by law and regulation will reduce the default problem. These measures include:

o Curtailment of SLS borrowing to students attending high default rate schools.

o Imposition of a need analysis on SLS borrowing to prevent unnecessary borrowing.

o Pro-rata tuition refund policies.

o Required default reduction plans for high default schools.

o Delayed certification for SLS for first-year students.

o An increase in the number of audits and program reviews of schools and lenders by the Department and guaranty agencies.

o Required disclosure of placement and completion rates by schools offering non-baccalaureate vocational training programs.

o Enhanced counselling requirements to ensure that students know their student loans must be repaid.

CBA also notes that the trade associations and accrediting commissions for the proprietary school sector have taken a greater interest in reducing defaults by looking at educational outcomes and administration of the loan programs on the campus.

As we trust this Subcommittee is aware, CBA supports changes to the Stafford Loan Program that will reduce the level of defaults. In this regard, CBA intends to work actively with the Congress on identifying additional measures that may complement those already in place. CBA is proud of its past role in default reduction legislation. It was CBA that in 1989 proposed the enactment of multiple disbursement requirements on student loans and the modification of SLS eligibility. These two measures by themselves have substantially reduced the flow of likely-to-default student loans being processed through the Program.

CBA believes that additional legislation could help prevent a repeat of the current situation. First, the default reduction initiative regulations issued by the Secretary need to be complemented with additional legislation that encourages improvements in the quality of education provided by schools, and requires that schools provide students with more consumer-related information relating to the outcome of the educational program offered. Schools, accrediting agencies, State licensing boards and guaranty agencies, along with the Department of Education, need to work together to improve the educational quality and to make sure students receive appropriate counselling and screening prior to admission.

Second, the Department of Education should develop procedures for addressing the contingency of another guaranty agency experiencing financial difficulty. Although we all hope that this circumstance will not arise again, we understand that at least five or six guaranty agencies, according to the Department of Education, have financial problems. CBA, in 1987, 1988 and 1989 proposed to the Congress the enactment of provisions to establish procedures for the merger or termination of guaranty agencies that experience serious financial difficulty. For a variety of reasons, this legislation has not been enacted. We recommend that the Subcommittee work with the Department of Education to establish a process through which financial problems at guaranty agencies might be uncovered early enough for corrective measures to be implemented to avoid situations like the one presently before this Subcommittee. We also believe, however, that in the event that financial problems are sufficiently severe to make the continued viability of the individual guaranty agency unlikely, Congress should take steps to ensure that a financially capable entity would assume the financial responsibility for the guarantees of the agency

In closing, CBA would like to emphasize its belief that with an appropriate resolution of the HEAF problem, the Guaranteed Student Loan Program will continue to meet the educational credit needs of students and their families.

The HEAF problem points out inherent difficulties with a loan program that is guided by the important social objective of creating educational opportunity. With appropriate modifications, the program can be better designed to serve the students who are its true beneficiaries well into the twenty-first century.

Mr. Chairman, thank you for the opportunity to be with you today. I would be happy to respond to any questions that you or other Members of the Subcommittee may have.

Senator PELL. Mr. Hough.

Mr. HOUGH. Mr. Chairman, members of the committee, I am Lawrence A. Hough, president and chief executive officer of the Student Loan Marketing Association. Sallie Mae is a federally chartered, stockholder-owned corporation which provides the Nation's largest single source of financing for postsecondary education. To foster our public mission, assuring the availability nationwide of education credit, Sallie Mae is expected to provide responsive leadership to ensure the continuation of private capital for student loans. In carrying out that business mission, our shareholders expect us to achieve a reasonable return on investment and not to assume risks which would adversely affect our ability to do so.

Since 1973, Sallie Mae has provided over $50 billion in funds and commitments for educational loans. This represents funding for more than 20 million student loans.

Sallie Mae is one of a very small number of financial corporations that hold a AAA credit rating from the rating agencies. This rating does not rely on our status as a Government-sponsored enterprise, but, rather, it reflects "on our strong financial fundamentals." In 1981, when Sallie Mae's obligations were guaranteed by the Department of Education—that is, the full faith and credit of the United States—our credit rating was only an A.

In general, Sallie Mae is doing everything possible to identify and minimize the various types of risk to which it is subject. With the advent of the new due diligence requirements in 1988, and the overall climate of risk-shifting to the private lending sector, the potential cost of error now has certainly increased.

Last year, the Treasury Department studied the financial risks posed by various Government-sponsored enterprises. They concluded that Sallie Mae is essentially not exposed to a large degree of business risk, credit risk, or interest risk. The report stated that "Sallie Mae is a well-managed enterprise with adequate controls to manage and monitor its operations."

Mr. Chairman, recently the Department of Education announced that one of the largest guarantors in the Federal Guaranteed Student Loan program, the Higher Education Assistance Foundation, is experiencing financial difficulties.

HEAF is the guarantor of a portion of the guaranteed student loans which Sallie Mae owns. Our share of HEAF loans is about the same as the share of HEAF loans in the total Guaranteed Student Loan program. The large majority of loans in our HEAF portfolio are already in repayment and, hence, can be expected to experience only insignificant default rates. The default experience on the smaller, newer portion of the HEAF-guaranteed portfolio can be reliably predicted based on our lending experience. The projected impact on Sallie Mae's balance sheet and earnings will not be material. This is true since, like all guaranteed student loans, HEAF-guaranteed loans are reinsured by the Department of Education. Irrespective of HEAF's financial situation, Sallie Mae believes its claims on these loans will be honored. In fact, last week the Secretary publicly stated, "Loans now guaranteed by HEAF will continue to be guaranteed."

Sallie Mae also extends collateralized loans to participants in the student loan program in addition to purchasing. Consistent with this activity, since 1984 Sallie Mae has extended collateralized advances to HEAF and its affiliates totaling $800 million. Of that amount, $200 million has been lent to HEAF itself. These advances are more than 100 percent collateralized with guaranteed student loans and Federal obligations.

Earlier this week, as a result of discussions with the Department of Education, Sallie Mae agreed to extend additional credit for HEAF of up to $200 million. An initial disbursement of $38 million was made on Tuesday of this week. As was the case with our earlier loans, this obligation is fully collateralized. We agreed to extend this loan to permit the development of a longer-term resolution of HEAF's difficulties.

Finally, Mr. Chairman, there has been much speculation in the press about what role Sallie Mae may have in any permanent resolution of HEAF's problems. Early on, the department asked us to provide our preliminary thinking on a "what if" basis. We have done so. I can assure you that were we to participate in a resolution, it would only be if so requested by the Secretary and only to the extent it is consistent with our traditional sound business practices.

Mr. Chairman, Sallie Mae is proud of the role it has played in supporting the Federal student loan programs. We have fostered and encouraged student credit as Congress intended. And we have accomplished this task by prudently managing a well-financed, strongly capitalized corporation. Students, colleges, universities, lenders, and our shareholders have all benefited. I look forward to working with you and this committee to strengthen educational opportunity, and I would be happy to answer any questions.

Thank you.

[The prepared statement of Mr. Hough follows:]

PREPARED STATEMENT OF LAWRENCE A. HOUGH, PRESIDENT AND CHIEF EXECUTIVE OFFICER, STUDENT LOAN MARKETING ASSOCIATION (SALLIE MAE)

Mr. Chairman, Members of the Committee, I am Lawrence A. Hough, President and Chief Executive Officer of the Student Loan Marketing Association, perhaps better known as Sallie Mae. I am accompanied by Timothy G. Greene, Executive Vice President and General Counsel to Sallie Mae.

Sallie Mae is a federally chartered, stockholder-owned corporation which provides the nation's largest single source of financing for postsecondary education. Sallie Mae was created by the Congress in the Education Amendments of 1972. To foster our public mission, assuring the availability nationwide of education credit, Sallie Mae is expected to provide leadership in the education credit markets to ensure the continuation of private capital availability for student loans. We also serve the interests of our investors -- commercial lending institutions, educational institutions and the general public; it is their continued confidence -- and investment -- in Sallie Mae that enables us to accomplish our mission. In carrying out that business mission, our shareholders expect us to achieve a reasonable return on investment and not to assume risks which would adversely affect our ability to do so.

Since 1973, Sallie Mae has provided over $50 billion in funds and commitments for educational loans; this represents funding for more than 20 million student loans. Today the corporation, both by buying student loans and by providing collateralized warehousing loans to lenders to finance student loans they own, funds about four in ten of all student loans outstanding.

Sallie Mae is one of a very small number of financial corporations that has been given a AAA credit rating from the rating agencies. This rating does not rely on our status as a government-sponsored enterprise (GSE), but reflects our "strong financial fundamentals." In 1981, when Sallie Mae's obligations were guaranteed by the Department of Education (i.e., by the full faith and credit of the United States), our credit rating was only an A.

In general, Sallie Mae is doing everything possible to identify and minimize the various types of risk to which it is subject. With the advent of the new due diligence requirements in 1988, and the overall climate of risk-shifting to the private sector, the potential cost of error has certainly increased.

Last year the Treasury Department studied the financial risks posed by various government-sponsored enterprises. They concluded that Sallie Mae is essentially not exposed to a large degree of business risk, credit risk, or interest risk. The report stated that "Sallie Mae is a well-managed enterprise with adequate controls to manage and monitor its operations."

Mr. Chairman, recently the Department of Education announced that one of the largest guarantors in the federal guaranteed student loan program, the Higher Education Assistance Foundation (HEAF), is experiencing financial difficulties.

HEAF is the guarantor of a portion of the guaranteed student loans which Sallie Mae owns. Our share of HEAF loans is about the same as the share of HEAF loans in the total Guaranteed Student Loan Program. The large majority of loans in the Sallie Mae portfolio are already in repayment and, hence, can be expected to experience insignificant default rates. The default experience on the smaller, newer portion of the HEAF-guaranteed portfolio can be reliably predicted based on experience. The projectable impact on Sallie Mae's balance sheet and earnings will not be material. This is true since, like all guaranteed student loans, HEAF-guaranteed loans are reinsured by the Department of Education. Irrespective of HEAF's financial situation, Sallie Mae believes its claims on these loans will be honored. In fact, last week the Secretary of Education publicly stated that:

> "While HEAF's problems are serious to that organization, they do not threaten the integrity of the nationwide Guaranteed Student Loan Program or the loans now guaranteed by HEAF. Loans now guaranteed by HEAF will continue to be guaranteed."

Sallie Mae also extends collateralized loans to participants in the student loan program in addition to purchasing loans. This activity increases liquidity to lenders and other loan program participants. Consistent with this activity, since 1984 Sallie Mae has extended collateralized advances to HEAF and its affiliates totaling about $800 million. Of that amount, $200 million has been lent to HEAF itself. These advances are more than 100% collateralized with guaranteed student loans and federal obligations.

Earlier this week, as a result of discussions with the Department of Education, Sallie Mae agreed to extend additional credit for HEAF of up to $200 million. An initial disbursement of $38 million was made on Tuesday of this week. As with our earlier loans, this obligation is fully collateralized. We agreed to extend this loan to permit the development of a longer term resolution to HEAF's difficulties.

Finally, Mr. Chairman, there has been much speculation in the press about what role Sallie Mae may have in any permanent resolution of HEAF's difficulties. Early on the Department asked us to provide our preliminary thinking on a "what if" basis. We have done so. I can assure you that we would participate in a resolution only if requested to do so by the Secretary and only to the extent it is consistent with our traditional sound business practices.

Mr. Chairman, Sallie Mae is proud of the role it has played in supporting the federal student loan programs. We have encouraged and fostered student credit as Congress intended. And we have accomplished this task by prudently managing a well-financed, strongly-capitalized corporation. Students, colleges and universities, lenders, and our shareholders have benefitted. I look forward to working with you and this Committee to strengthen educational opportunity.

I would be happy to answer any questions you have.

Senator PELL. Thank you very much.

I have to be here, anyway, so I am going to defer my questions, and I believe the ranking minority member will not be coming back.

Senator KASSEBAUM. I am sorry. Are you coming back?

Senator SIMON. I am going to vote and come back.

Senator KASSEBAUM. All right. Let me just ask briefly each of you, if you had to give one recommendation on how future problems of this sort could be avoided, what recommendation would you make? Mrs. Frohlicher.

Mrs. FROHLICHER. I am not sure I have a recommendation at this point. I think that the guarantee agencies that exist across the country have indicated to the Department of Education their willingness to do their share in helping out with this program. I think that work is very strong. I don't have an instant solution, and we will be looking at this problem, too.

Mr. BIKLEN. First of all, as I said, I do think that the legislation and the regulatory changes that have been put in place will have a big impact on defaults, and hopefully that will help lessen problems of this nature going forward.

However, if this type of situation did come about in the future, I think it is imperative that there be a mechanism, whether it be 100 percent is supplied, if that is not possible at least there be a mechanism so that other agencies could step in and take over the guarantee function and honor the existing liabilities.

Senator KASSEBAUM. The figures show, as you know, that the legislative changes have meant a significant drop in the volume of loans. So perhaps this is going to work its way through the system in a positive way.

Mr. Hough.

Mr. HOUGH. I believe these events point up the need for much greater clarity in just exactly what the combined approach will be of the Federal Government in the guarantor structure to immediately dissolve, eliminate completely any questions relative to the position that lenders and holders are put in as a result of the underlying elements of the law itself. The sooner that can be done, the better off the program will be.

Senator KASSEBAUM. Thank you very much. Unfortunately, I will have to go vote, Mr. Chairman.

Senator PELL. I will ask my questions. Thank you very much, Senator Kassebaum.

Do any of you think there is any relationship, in appearance, in perception, between this crisis and the S&L? Mrs. Frohlicher.

Mrs. FROHLICHER. Oh, no. I know that various press reports have even gone so far as to categorize Federal payments for defaults, which is one of the two things the Federal Government does as bailouts. This is not in any way similar to the S&L.

Senator PELL. Mr. Biklen.

Mr. BIKLEN. No, I don't think it is similar to the S&L crisis. But I do think that if this is not resolved, it could lead to a crisis for guaranteed student loans.

Senator PELL. Mr. Hough.

Mr. HOUGH. I concur with Mr. Biklen. The problem is not a run on the treasury. The problem is the total deficiency of credit availability to students who depend on such for going to school this fall.

Senator PELL. I am going to have to leave, so I will recess the committee. Senator Simon will be right back, and he will resume. And I will be back in a few moments.

[Recess.]

Senator SIMON [presiding]. The subcommittee will resume its hearing.

As I listened to your statement, Mr. Hough, I didn't hear any recommendations for change. Maybe things ought to just stay as they are. Do you have any recommendations?

Mr. HOUGH. Senator, there are a series of elements within the statute that the HEAF situation points up. Let me just touch on a couple of them.

The ability of the guarantee agency to quickly establish the reserves necessary to meet its responsibilities as it sees situations develop, as HEAF saw back in 1987 or 1988, clearly the outcome that we have in front of us today suggests that we don't have everything in the present program that allows the guarantee agency to quickly move in and make the kinds of adjustments to protect its reserves. So I think that warrants some attention.

The second area deals with——

Senator SIMON. And when you say it warrants some attention, are you willing to give us a specific recommendation before 1991?

Mr. HOUGH. Yes, sir. We would happily work with the staff of this committee.

Senator SIMON. Good.

Mr. HOUGH. I should also point out that there is a history, as I spoke last Friday—there are, indeed, strange bedfellows together in this program, but the pattern has been that with NCHELP and CBA and the schools together, we have fine tuned this program over the years. And it is a tribute to that effort on our part and the committee's part that we have only had one incident such as we unhappily have in front of us over a very long history in a program that is very complex.

The second possible area of attention would be in looking again, as I mentioned to Senator Pell, at what the holders and lenders have ahead of them in the event we get into these situations where insolvency looms as a possibility. As the vice president of Citibank, Steve Biklen, indicated clearly, it is the CBA's view and it is our view that there is a full commitment of the Government that strengthens the participation by lenders and holders in this program.

A lot of the stir we have in front of us today is because some are questioning whether that commitment is complete. There is no question in my mind and I don't think there is any question in CBA's mind that there is a full commitment. But if there is a way of reassuring that—there has been an expression in several instances that the whole area of "what happens if" might well be addressed in the statute, and it has not been, although it has been raised before.

Senator SIMON. Mr. Biklen, you say, "We recommend that the subcommittee work with the Department of Education to establish a process through which financial problems at guarantee agencies might be uncovered early enough for corrective measures to be implemented."

Can you be more specific in what you think ought to be done?

Mr. BIKLEN. Well, I couldn't lay out for you this afternoon all of the specifics with respect to that, but I think given some time I could probably come up with some suggestions in terms of what the department might be looking at to enable it to ascertain whether or not an agency might have some problems. And I think that if a full understanding was had, we might be able to correct the situation before it became a crisis, which we are discussing today.

Senator SIMON. Well, if at any point you have more specific suggestions, we would welcome them.

If I could just underscore one of the points Mrs. Frohlicher mentioned in her statement, "Studies show that the primary reason borrowers today are not repaying their loans is their financial inability, not their unwillingness to do so," I think the public image is quite to the contrary. I think what you State here is the fact.

In your testimony, you also state, "The board has also gone on record against continued GSL eligibility for courses of study of less than 600 clock hours in duration." I should know this, but I don't: Is that a common practice? Are there a lot of courses that are less than 600 clock hours in duration?

Mrs. FROHLICHER. Yes, there are. I don't have any number of them, but the Guaranteed Student Loan program is the only Federal financial aid program that enrolls—eligibilizes students in courses of 300 clock hours. The standard for Pell grants and for all the campus-based program is a minimum academic years of 600 hours. So what this leaves the Guaranteed Student Loan program with is students who are probably the neediest students going into very short courses—these could be 8- to 15-week courses—which are probably leading them to minimum wage jobs. And the only Federal aid they have available under Title IV is guaranteed loans.

We are extremely concerned that the incomes that they can anticipate in the bulk of these courses are simply not the kinds of things that would sustain debt. We are not saying to the committee that the needs of those students not be met. But speaking for the loan community, we feel it is very bad public policy to have it be met by a loan.

Senator SIMON. And by implication, you are suggesting that students attending the shorter courses are much more likely to be default-prone?

Mrs. FROHLICHER. Again, because of the difficulty of what they train them for. They are entry-level jobs, nursing aides or sorts of things that are department store retail clerks, which are primarily minimum wage, noncareer ladder types of curricula. Those courses appeal to students to whom speed in getting into the job market is important. A welfare mother who wants to get off welfare doesn't have the time to take the same course for free in a community college. But she can't sustain the debt with the job she would get afterward.

Senator SIMON. If I can use this example, in our society today, the fact that she is off welfare is not counted against the default.

Thank you, Mr. Chairman.

Senator PELL [presiding]. Thank you very much, Senator Simon. Senator Jeffords.

Senator JEFFORDS. Just a couple of questions. First of all, Mrs. Frohlicher, is there some advantage perhaps to having only guarantors within a State rather than nationwide? Is there a problem with nationwide guarantors not being able to better understand those institutions that the lenders are guaranteeing?

Mrs. FROHLICHER. I think we have a mix of strong State-based guarantors. We have national guarantors. As the banking community begins to move beyond individual State borders, they often want to stay with the same guarantor. I think obviously—and history proves this. The reason that the Congress went to a State-based guarantee system in 1976 was the obvious strength of State-guaranteed—State of nonprofit private guarantors within specific States as far as better default records than the Federal program that was in about half the States, much greater lender participation. I think that as an organization we favor a strong guarantor system, and I think we have it in this country.

Senator JEFFORDS. Thank you. I know we have worked hard to try and reduce the monthly payments through spreading them out and consolidating. Have we done enough in that area, or is the problem with the term of the loans are too short? Or what do you feel would help in getting a better situation for reducing defaults?

Mrs. FROHLICHER. Well, we run into budgetary problems, as you are too well aware, with great extensions of term of the loan. Right now we are still operating on the same 10-year term we did 25 years ago although loan limits have increased geometrically from the potential for an individual to borrow.

I think that we need to take another look at the consolidation program. We need to look at how the interest rate to the student works in relation to the current market. As I say, our organization is going to be proposing to the community that we essentially go to an annually set market rate for interest payment by the borrower in repayment, which would ease the budgetary crisis and allow us in consolidation situations to effect longer terms without greater Federal budget costs as a result.

Senator JEFFORDS. Mr. Biklen or Mr. Hough, would you have any comment on that last question from your own experience?

Mr. BIKLEN. As I said in my testimony, I think that a number of the things that have been legislated or regulated with respect to default reduction, we have yet to see their full impact. I do think a lot of those things are going to have a very positive impact. There are probably a few other things that can be done, but I am really hopeful that the things that happened are going to help a lot. I just think that there were a lot of people getting loans that never should have gotten them in the first place. And I think a lot of those things have been corrected.

Senator JEFFORDS. Mr. Hough.

Mr. HOUGH. The specific question as to whether an extension of term will have a positive impact in reducing default, my immediate reaction to that is no. I don't believe it will. I think the default problems we face today are not as aptly dealt with by merely extending the repayment term. We have the ability to use graduated repayment, and that, in effect, can give relief on the front end. And

10 years is a long time in which to build up the income and the ability to pay off a loan. So I think the mechanism is in place.

That would be my answer, sir.

Senator JEFFORDS. Thank you.

Thank you, Mr. Chairman.

Senator PELL. Thank you very much. The record will stay open for a few days in case any of our colleagues want to direct any questions to you.

Thank you very much, indeed, for being with us. You are excused.

We now come to our second panel: Mr. Stephen Blair, president, National Association of Trade and Technical Schools; Charles Saunders, senior vice president, American Council on Education; and Dr. Dallas Martin, president of the National Association of Student Financial Aid Administrators, an old friend of the committee and of the chairman.

Senator SIMON. Mr. Chairman, I am going to have to leave for another meeting before their testimony is over. But these three witnesses have contributed immensely to this Nation, and I wish I could stay here to hear all three of them.

Senator PELL. Thank you, Senator Simon.

Mr. Blair.

STATEMENTS OF STEPHEN J. BLAIR, PRESIDENT, NATIONAL ASSOCIATION OF TRADE AND TECHNICAL SCHOOLS, WASHINGTON, DC; CHARLES B. SAUNDERS, JR., SENIOR VICE PRESIDENT, AMERICAN COUNCIL ON EDUCATION, WASHINGTON DC; AND A. DALLAS MARTIN, JR., PRESIDENT, NATIONAL ASSOCIATION OF STUDENT FINANCIAL AID ADMINISTRATORS, WASHINGTON, DC

Mr. BLAIR. Mr. Chairman and the subcommittee, my name is Stephen Blair, and I am the president of the National Association of Trade and Technical Schools, which represents some 1,300 private postsecondary trade and technical institutions attended by some 650,000 students nationwide.

Senator PELL. Hold the mike a little closer if you would.

Mr. BLAIR. Yes, sir. I appreciate the opportunity to testify before you.

NATTS is extremely concerned about the problem currently experienced by the Higher Education Assistance Foundation, and we must maintain public confidence in the guarantees found in the Stafford Loan Program. In creating the Federal student assistance programs, Congress' clear intention was to ensure that all Americans, especially the poor, have access to postsecondary education. By specifically including trade and technical schools, Congress wanted to ensure that students would have access to the kind of education that best meet their interests, their needs, and their abilities.

Today, more than ever, Congress should reaffirm its commitment to the access to our schools for the job market increasingly demands a skilled and educated workforce. Our schools provide half of the trained workers entering the job market today, and over the next decade 70 percent of all jobs will require some level of technical education beyond high school. And only 20 percent of that will require a traditional degree.

NATTS schools will help the Nation meet that challenge of the 1990's and the 21st century. In considering the default problem, we cannot lose sight of the congressional commitment to protect the opportunity of all students to get the kind of assistance and the training they need. Blame for HEAF's problems are not the fault of trade school students or our schools. HEAF's problems are due to the costs everyone faces who serves high-risk students and many other complicated issues. However, I would like to point out the special lessons that can be learned about the pitfalls of risk-sharing because the trigger is a form of risk-sharing.

We are dealing with the problems that there are no incentives, only penalties, for dealing with high-risk students. While loan defaults are serious problems, we should not exaggerate the magnitude of the problem. The dollars in default is a function of the volume of borrowing. The default percentages remain constant, as the chart attached to my testimony points out.

Student loan programs are extremely cost-effective. For every $10 going to students, the Government has only paid out 92 cents in defaults. Student loan programs have a lower default rate than Small Business Administration loan programs and many other Federal programs. The student loans have been a cost-effective way to open doors for millions of Americans of all economic backgrounds. They have helped millions pursue the American dream and become productive, economic contributors to society.

Part of the default problem is due to the dramatic shift in aid. As Senator Kassebaum pointed out, in 1980 two-thirds of the typical aid package consisted of grants, while today only one-quarter is grant aid. We have created a brutal imbalance between loans and grants that means that our poorest students must incur the crushing burden of debt to finance their education.

The default problem is not so much because of our schools but because of the population we serve. We serve in trade schools the full range and economic spectrum of the citizens of this country, and our schools also educate a higher percentage of low-income, women, and minorities than any other sector. These individuals are more likely to default on loans no matter what kind of school they attend. We recognize that there is a problem, and we are working with the Congress to make sure that the schools and their abuses are identified and routed out.

NATTS has undertaken numerous reforms that have already produced concrete results. Private trade schools have experienced the largest decrease in default rates of any sector. The U.S. Consumer Information Center is now making available for free our book called "Getting Skilled, Getting Ahead," which is consumer information on how to be sure the consumer picks a good school.

In NATTS accrediting, we are aggressively policing our own ranks to eliminate bad business and recruiting practices and ensure quality of education. We are trying to send a clear message to the Nation that our schools have standards that are as stringent and exceed the stringency found in any other sector. NATTS is committed to ensuring that all of our schools offer high quality education for the students we teach and the businesses we serve.

We have been aggressive in supporting legislation which has banned the jumping of accreditation bodies from one another, and a bill that would require disclosure of completion rates for everyone. While the current situation with HEAF is a serious one, it is not a condemnation of the entire student aid program. The remedies that exist in the program to address student loan defaults are already in place and must be given the opportunity to demonstrate their effectiveness. However, the mission of the Federal assistance program must be maintained, and the needs of the students it serves must be protected.

In order to ensure access to Federal student aid for a high-risk population that needs the aid most, there must be a coordinated effort to operate effective lender of last resort program. Furthermore, Congress must look into the current fee structure in the loan program, recognizing the higher costs of serving a high-risk student.

The brutal imbalance between Federal grants and loans must be remedied to prevent this Nation's neediest from incurring overwhelming debt burdens to finance their postsecondary.

Finally, the issue before us today has not to do with HEAF or, more importantly, the students they serve, but rather how are we effectively going to fund the critically needed postsecondary education for all of our citizens. This country is in crisis. We must regain our competitive edge in the world marketplace. To do this, we must have the skilled professionals, artisans, craftsmen, and technicians. We cannot turn our backs on the citizens at this critical time.

Thank you, sir.

[The prepared statement of Mr. Blair follows:]

PREPARED STATEMENT OF STEPHEN J. BLAIR, PRESIDENT, NATIONAL ASSOCIATION OF TRADE AND TECHNICAL SCHOOLS

Mr. Chairman, Members of the Subcommittee: My name is Stephen Blair. I am the President of the National Association of Trade and Technical Schools which represents some 1,300 private postsecondary institutions attended by 650,000 students nationwide. I appreciate the opportunity to testify before you today.

NATTS is extremely concerned about the problems currently being experienced by the Higher Education Assistance Foundation (HEAF) for three reasons. The first is that access to student aid for individuals regardless of socio-economic status is the basic premise upon which the federal student loan programs were founded. The current situation raises concerns about continued access for high risk students. Second, it places undue strain on the participants in the programs and threatens the delicate balance between students, schools, lenders, and guarantee agencies. Finally, the disruption in the flow of student aid sets a bad precedent.

The primary purpose of federal student financial assistance programs is to provide the necessary funds to ensure equal access to postsecondary education for all students. The 1972 amendments to the Higher Education Act of 1965 permitted greater access for high-risk students to the federal student aid programs. In addition to allowing private career school students to participate in federal aid programs, the Basic Educational Opportunity Grant Program, now known as the Pell Grant Program, was established.

Both of these initiatives represented a commitment by Congress that the very poorest of students would have access to the necessary funds to pursue the type of education that best suits their interests and personal needs. The inclusion of proprietary schools and technical and vocational education in the Title IV programs marked a conscious effort to expand the traditional concept of "higher" education to one of "postsecondary" education. By providing access to federal student aid to students of all ages and career interests, the 1972 amendments enabled every citizen to pursue the postsecondary educational opportunity of his or her choice.

PROBLEMS WITH THE HIGHER EDUCATION ASSISTANCE FOUNDATION

To ensure that the mission of the Higher Education Act is preserved, the current financial situation with respect to HEAF must be resolved. The problems with HEAF have been evident for some time. The problems are not a result of HEAF's coverage of trade and technical school students' loans, but due to the cost to everyone who serves high risk students, as well HEAF's ineffective servicing. Higher default rates than other cc able guarantee agencies are indicators of this.

Based on a sample of all records on the Fiscal Year 1986 "State Tape Dump," we find that the two-year cohort default rate experienced by HEAF was 32.6 percent. This compares to 12.5 percent for United Student Aid Funds (USAF), and 12.4 percent for all state agencies combined. For loans to students attending proprietary schools that year, HEAF had a default rate of 43 percent, USAF had a rate of 28.9

percent, and the state guarantee agencies had a rate of 26.4 percent. HEAF also had higher default rates for other sectors of postsecondary education than did the other guarantee agencies. For public postsecondary institutions, HEAF's rate was 13.8 percent, USAF's rate was 9.3 percent, and the state agencies' rate was 10.3 percent. For private, non-profit schools, HEAF's default rate was 14.4 percent, USAF's was 9.7 percent, and the state agencies' was 6.9 percent.

The difference between the HEAF default rates and those of other guarantee agencies in all educational sectors is significant because it indicates that HEAF, or its servicer, the Higher Education Management and Resources Corporation (HEMAR), experienced difficulties in loan servicing. The Department of Education is currently examining the financial situation at HEAF. Other guarantee agencies were able to keep their default rates lower while serving similar populations of students. The USAF and state agencies' default rates are in keeping with the national average default rate for proprietary schools, which is around 27 percent, while HEAF's rate is significantly higher.

What is important to note here is that trade and technical schools are not the only players involved in student aid. Students, schools, servicers, and guarantee agencies all must play a role in reducing defaults. While some defaults are expected, it is our responsibility to ensure that these are kept to a minimum. HEAF's difficulties in this area cannot be blamed on trade and technical schools who relied on HEAF and HEMAR to service their students' loans.

THE COST EFFECTIVENESS OF THE STUDENT LOAN PROGRAM

Since the inception of the federal student loan programs in FY66, over 50 million students have received $106 billion in loans. While the dollars in default have grown, the percentage of loans in default has remained relatively constant. This direct corollary between dramatic increases in loan volume and dollars in default is shown on the chart taken from the Department of Education, Office of Postsecondary Education's FY88 GSL Program Data Book that is included in my written comments.

In FY89 alone, the program provided 4.7 million students with over $12.4 billion in loans. In fact, the student loan programs have provided three dollars in assistance for every dollar from the federal treasury. Defaults average less than 30 percent of the program cost over the long run (28.75 percent). For every $10 going to students, the government has paid $.92 in defaults. Interest subsidies make up the bulk of the remaining cost.

According to an analysis of the federal budget conducted by the Department of Education, the student loan programs have a lower default rate than many other federally guaranteed loan programs, including the Small Business Administration Loan Program, Commodity Credit Corporation, and the Economic Development Fund.

Finally, the true cost of defaults can only be measured by looking at defaults after collections, or net defaults. Department of Education data from FY88 indicates that of all student loan money, $17.5 billion is in school, $27.6 billion is in repayment, and $45.1 billion is outstanding. At that time, $89.2 billion had been loaned cumulatively. Of that total, only 9.2 percent or $6.6 billion were in default after collections. Nearly half of all loans made in the program have been totally repaid, and an additional 40 percent are in successful repayment.

The federal student loan programs represent a 25-year commitment to postsecondary education. By every measure, it has been a cost effective method to provide a wide range of students and their families with the necessary funds to pursue postsecondary education.

SHIFTS IN STUDENT AID FROM POOR TO MIDDLE INCOME STUDENTS

A recent report issued by American College Testing (ACT) indicates that from 1978 to 1990, there has been a dramatic shift in student financial assistance programs from poor to middle-income and affluent students. Since the passage of the federal Middle Income Student Assistance Act in 1978, most institutional, state, and federal student aid programs have been expanded to include a greater percentage of the middle- and high-income students.

Limited funding and an ever-increasing federal deficit further decrease the assistance that trickles down to the neediest of students. While needs analysis originally provided very poor students with a significant portion of their federal assistance in the form of grant aid, this is no longer the case. Eligibility of middle- and high-income students for basic grants has added to this strain on the available grant aid to the neediest students. Now, even the poorest students must incur debt to finance their education.

The brutal imbalance between loans and grants that has forced our neediest students to rely upon loans to finance postsecondary education must be remedied. In 1980, grants constituted 40 percent of the typical aid package, with loans making up most of the remainder. Now, grants comprise only 29 percent of the typical package. Coupled with other changes in student aid, such as a cap on borrowing under the Stafford Student Loan program and restrictions on Supplemental Loans for Students (SLS), people are increasingly hard-pressed to pay for the education required for many of the jobs currently available.

The grant loan imbalance and increased eligibility of middle-income students has limited available aid for poor students who were the intended benefactors of the federal student assistance programs. This also means the students graduating from most postsecondary educational institutions embark on their career path carrying a crushing debt burden. Clearly, the original mission of the Higher Education Act of 1965, and Amendments of 1972, for need-based federal student assistance programs is not being met.

THE CRITICAL NEED TO SERVE NON-COLLEGE STUDENTS

Private trade and technical schools provide the forum for the non-college bound to pursue a postsecondary education. Furthermore, the need for skilled workers increases the demand on this country to educate and produce a more technically capable workforce.

The Department of Labor estimates that over the next decade, 70 percent of all jobs will require some form of technical education beyond high school. Only 20 percent of these jobs will require a traditional college degree. Only 50 percent of all high school graduates will go on to college, and 42 percent of those students do not obtain a college degree. However, federal, state, and local governments and private entities spend $45 billion a year subsidizing college students, yet barely $7 billion a year on postsecondary education for non-college bound youth. Continued access to federal student aid is the only option for many of these individuals to finance their future.

The proprietary sector continues to provide quality education and outcomes to the full economic spectrum of our citizens while at the same time serving a disproportionate percentage of low income individuals, women and minorities. The following statistics demonstrate a dedication to serving the high risk and a commitment to quality education:

- Sixty-one percent of private career school students graduate, compared to 43 percent of students in public community colleges, 58 percent in four-year colleges, and 33 percent in Job Corps.

- The placement rates for graduates of trade and technical schools is 81 percent.

- Forty-three percent of private career school students have an income of less than $11,000.

- Private career schools educate a higher proportion of women ([illegible] percent) than any other postsecondary sector.

- Forty percent of private career school students are minorities.

All of the current studies on America's ability to compete in the world economy clearly indicate two things: 1) the critical need for skilled artisans, craftspersons, and technicians; and, 2) minorities, women and immigrants will make up a significant portion of the future workforce.

NATTS REFORM MEASURES

While we are concerned about the problems with HEAF, we also recognize that some schools have abused students and the student aid programs. We are working with the Congress and the Department of Education to curb these abuses. NATTS recommended and fully supported the provision in the Omnibus Budget Reconciliation Act of 1989 that prohibits federal financial aid to students attending schools which have voluntarily withdrawn while under a show cause order from an accrediting body or whose accreditation has been revoked. Such schools are now prohibited from participating in the Title IV programs for at least two years.

NATTS also supports the legislation now being considered by Congress which would require that all schools disclose completion rates, as well as placement rates and pass rates on licensure exams where applicable, to prospective students. We believe that arming students with this information will help to reduce defaults. Students should be able to make sound consumer decisions about where to attend school.

In addition to these efforts, NATTS commissioned a consumer guide book in 1989 called Getting Skilled, Getting Ahead. The book tells students what questions to ask and what to look for before enrolling in a private career school. Its is endorsed by both Department of Education and the U.S. Consumer Information Center. It is the most requested publication in the U.S. Consumer Information Center's history. This free consumer information tool helps students make sound educational choices, thereby decreasing their potential for default.

The NATTS Accrediting Commission effectively evaluates schools and rigorously enforces its high standards. In 1988, 9.3 percent of schools seeking initial accreditation or reaccreditation were denied. A number of other schools seeking reaccreditation voluntarily withdrew. Schools removed from accreditation frequently sought remedies in the courts. To date, NATTS has generally been successful in these court decisions. Since April 1990, court costs for NATTS have exceded $70,000.

Regarding initial accreditation, many schools express an interest in NATTS accreditation. Of every 100 schools attending our pre-application workshop, at which potential applicant schools learn about the NATTS standards of accreditation and the rigorous review process, about 50 actually apply.

The NATTS Accrediting Commission has recently instituted several changes to its standards of accreditation which will further ensure good management and education practices in NATTS accredited schools. Among these are the following changes:

Recruitment: The standards now require that commissions be given to recruiters only upon the earlier of the student's completion of the program or 30 days after the start of the program, rather than on enrollment.

Branching: The procedure for starting branch campuses has been tightened to include multiple visits beginning prior to the establishment of the branch. The NATTS Accrediting Commission believes that while the Department of Education does not specifically require such extensive oversight of branching, it is in the best interests of both the students and the schools to monitor branching closely.

Tuition refund policy: The Commission voted to extend the refund policy to students terminating their education within 75 percent of the program from the previous level of 50 percent.

Associate degree programs: To ensure public confidence in the value of an associate degree from NATTS-accredited institutions, the Commission voted to require a high school diploma or recognized Occupational Studies degree.

DEFAULTS AND NATTS SCHOOLS

While any abuses or mismanagement are a serious concern, it is important to note that they are not the root of the default problem. All research demonstrates that the default rate of a postsecondary institution, lender, or guarantee agency is primarily a function of the population served. The cost of educating "at-risk" students, and making and administering loans for them, are greater regardless of the type of postsecondary institution the students attend.

Because trade and technical schools serve a significantly higher proportion of low-income individuals, women, minorities, and at-risk students than any other postsecondary sector, our default rates tend to be higher. In spite of this high-risk population, trade and technical schools are successful, as demonstrated by our completion and placement rates. While trade and technical schools have higher completion rates than other sectors, we are continually striving to improve.

With regard to defaults, we launched a major Default Management Initiative over three years ago in conjunction with other groups in the proprietary sector. This program has been adopted, in whole or in part, by seven state guarantee agencies. We are currently conducting a second series of workshops for this initiative, which includes an emphasis on "economic life skills."

The results of this effort are already evident. The Secretary of Education reported that trade and technical schools posted the largest decrease in loan defaults of any sector of postsecondary education from Fiscal Year 1986 to Fiscal Year 1987. Although the Department of Education has chosen this year not to report the data by sector, our analysis shows that trade and technical schools have experienced the largest drop in defaults in Fiscal Year 1988. These declines can be attributed to various efforts, but the private career school sector's Default Management Initiative has played a significant role.

We are proud of our reduced default rates because we recognize that every dollar in default that is collected can then be redistributed to other needy students. However, we also recognize that if too much emphasis is placed on low default rates, schools, lenders, and guarantors will be less inclined to serve at-risk students who have a higher propensity to default, those people perhaps most in need of educational opportunity. We must take care to address properly the default problem without compromising the access of these students to the education they need.

NEED FOR EFFECTIVE OVERSIGHT

While we continue to take effective steps toward lowering default rates, all participants in the program must accept their share of the responsibility for serving high risk populations. This responsibility includes effective oversight and enforcement of existing laws designed to maintain access to the programs.

In the face of the rapid growth in the student loan programs, the level of oversight from the Department of Education was decreased. The staff levels and number of program reviews during the past decade declined significantly, while the number of schools participating in the student loan programs escalated. Serving high risk students and limited oversight increase the potential for defaults and program abuses.

PRESERVING ACCESS FOR THE HIGH RISK

Many of the students who are served by the federal student loan program could not possibly obtain a loan from any other source. In many instances, these individuals do not have a credit history, or have a very poor credit history, and have not maintained the same address or the same job for an extended period of time throughout their entire life. Many of these people are products of a variety of federal assistance programs, and will continue to rely on such programs if they are not given the opportunity to obtain the necessary education and skills to become employable.

Great caution must be exercised in the consideration of restrictive policy designed to "tighten up the program," such as credit checks and co-signers. We cannot deny these loans to the students who most need them, and those upon whom society will rely heavily for its workforce in the near future. Currently, the return on investment is great. Every tax-dependent person using a Stafford Loan to enable them to become a tax-paying person pays for 65 defaults.

The Department of Education is required to ensure that the very high risk are served by the federal student loan programs. The policy established to serve these populations is the lender of last resort provision. While each state has a designated guarantee agency that serves as the lender of last resort, the policy has not been consistently implemented. In order to ensure that all students have access to federal student assistance, the Department of Education must not only see to the implementation of this policy by each state agency, but also must provide the appropriate guidance and oversight to the designated guarantee agencies to assure effective and financially stable management of the programs.

REMEDIES PROPOSED BY THE DEPARTMENT OF EDUCATION

The Administration has proposed several changes which it maintains will help avoid future situations similar to what HEAF is experiencing. Among these are lender risk sharing, credit checks for loan applicants, required co-signers, and linking some loans to high school performance. Some of these proposals are receiving support from some Members of Congress.

Lender risk sharing: The Administration proposes that lenders be required to share in the risk of serving high risk students by reducing the reinsurance rate from 100 percent to a lower percentage if the lender has a certain default rate. Given that a shortage of lenders willing to lend to high risk students already exists, reducing the reinsurance would only serve to exacerbate this problem. Lenders would likely "red-line" institutions serving academically and financially at-risk students. This would cause a further decline in the ability of high risk students to obtain postsecondary education. More importantly, the real effects of cost sharing are seen in the collapse of HEAF.

Credit checks for borrowers and required co-signers: Requiring credit checks and co-signers for borrowers in the federal student loan programs would directly contradict the mission of these programs. The federal student loan programs, as previously noted, were originally created to provide assured access to federal student assistance for all people, regardless of their socio-economic status or credit history. The programs were developed using a need-based system of providing varying degrees of grant and loan assistance to all eligible students. The aforementioned proposals fly in the face of the basic premise of guaranteed need-based federal student assistance.

CONCLUSION

The federal student loan programs celebrate their silver anniversary of continual service in providing students with access to postsecondary education. The student loan programs that have effectively served over 50 million students, providing them with $106 billion in loans and boasting an average net default rate of approximately ten percent. The growth in the dollars in default is directly related to rapid growth in the volume of the student loan programs, while percentage of loans in default has remained relatively constant.

While the current situation with HEAF is a serious one, it is not a condemnation of the entire student loan program. The remedies exists in the program to address student loan defaults and must be given the opportunity to demonstrate their effectiveness. However, the mission of the federal assistance program must be maintained, and the needs of the students it serves must be protected.

In order to ensure access to federal assistance for the high risk population that needs it the most, there must be a coordinated effort to operate an effective lender of last resort program. Furthermore, Congress must look into the current fee structure in the loan programs, recognizing the higher costs of serving high risk students. The brutal imbalance between federal grants and loans must be remedied to prevent this nation's neediest students from incurring overwhelming debt burdens to finance the postsecondary educational opportunity of their choice.

Finally, the issue before us today is not what to do with HEAF or more importantly the students they have served, but rather how are we effectively going to fund the critically needed postsecondary education for all of our citizens. This country is in a crisis - we must regain our competitive edge in the world marketplace. To do this, we must have skilled professionals, artisans, craftspeople, and technicians. We cannot turn our backs on any of our citizens at this critical time.

Thank you very much for your attention. I would be happy to answer any questions at this time.

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Senator PELL. Thank you very much, Mr. Blair. Mr. Saunders.

Mr. SAUNDERS. Mr. Chairman, thank you very much for holding these hearings to explore the dimensions of the problems HEAF is having and the reasons they came about.

I think in the short run it is obvious it is very important that the Education Department restore lender confidence in the program, and assure all eligible students that they will be able to continue to borrow. I think we heard some assurances from the Secretary this morning, and I find his statement encouraging.

For the long run, though, it is essential to address some of the larger problems in student aid that have brought these problems about. And we are counting on your continued leadership, Mr. Chairman, as we go into the reauthorization process to explore some of these problems.

The first basic problem, it seems to me, is the rising tide of defaults caused by over-reliance on loans as a primary form of assistance. The decline in the value of grant aid is well known. This issue has already been commented on this morning. I would just like to say that a primary goal of reauthorization should be to assure that regular inflation adjustments are made to the Pell award and to minimize borrowing by needy students, particularly at-risk students. And I am happy to note, Mr. Chairman, that this is one of your stated priorities, if not your highest priority, in reauthorization.

The second basic problem is the need to strengthen the fraud and abuse provisions in existing law and regulations. I note in my testimony the NCS study of defaulters which notes that something like 88 percent of defaulters, or 83 percent of defaulters either have not completed a bachelor's degree or received a lesser degree. Half of all defaulters were enrolled in vocational programs, and almost half have incomes after they get out of less than $6,000.

Such statistics underline the need to give the Department of Education more flexible authority to distinguish between schools that do a good job of educating or training high-risk students and those that don't. It is also vital to strengthen the process for determining institutional eligibility. Accreditation and licensing procedures must be tightened. The Secretary should have authority to decertify accrediting agencies which are not doing an adequate job.

Accrediting agencies need limited protection from damage suits and authority to use arbitration as an alternative to court action. The Secretary should be required to make a determination that a State has established adequate licensing standards as a condition for any institution within its borders to continue to receive Federal aid. The States should also assure that proprietary school programs demonstrate the need for courses and the quality of the instruction before they are approved, just as collegiate programs are scrutinized. State guarantee agencies should be given authority to refuse guarantees when they have clear evidence that a potential for fraud and abuse exists.

My statement contains a number of other suggestions, Mr. Chairman. I will close by saying we look forward to working with you and the committee on these problems in the months ahead.

[The prepared statement of Mr. Saunders follows:]

PREPARED STATEMENT OF CHARLES B. SAUNDERS, JR., SENIOR VICE PRESIDENT, AMERICAN COUNCIL ON EDUCATION

Mr. Chairman and Members of the Subcommittee:

On behalf of the American Council on Education, the national coordinating body for higher education, I appreciate this opportunity to comment on the recently reported financial problems of the Higher Education Assistance Foundation, and their implications for all of postsecondary education.

Just last week, ACE President Robert Atwell wrote to Secretary of Education Lauro Cavazos to express support for his efforts "to avert a crisis in the lending community which could jeopardize the availability of loan capital to students entering college this fall."

The letter emphasized: "it is vital that the Department take the necessary steps to assure that the integrity of the program will be maintained. In this regard...it is important to end press speculation that the federal government may not have the necessary authority to resolve (HEAF's) current financial problems. I believe that the statute is very clear in giving the Department full authority to assure lenders that 100 percent of the guarantee on loans held by HEAF and other guarantors is backed by the federal government."

I want to underscore the importance of assuring that all eligible students will continue to be able to borrow through the Stafford Guaranteed Student Loan program. This can best be accomplished by maintaining lender confidence in the program, through assurances that lenders who follow prescribed rules will continue to receive full payment on the default claims they submit. Anything the Congress can do to elicit such assurances would be of tremendous assistance in stemming the recent erosion of confidence in the program.

In the longer term, the HEAF situation serves as a warning that the present reinsurance structure of the Stafford Loan program needs to be thoroughly examined during the reauthorization of the Higher Education Act. But the reauthorization process must also address a number of larger and more basic problems with the student aid system that contribute to HEAF's current financial difficulties. These problems include: the growth in defaults caused in large part by overreliance on loans as the primary form of federal student assistance, and the lack of adequate regulations and incentives to prevent fraud and abuse of the student aid programs.

Defaults and the Grant-Loan Imbalance

The disturbing growth in defaults over the past decade is one of the more obvious consequences of the substantial decline in grants as a proportion of all aid which has taken place during that same period of time. Although appropriations for student aid have increased significantly, the value of student benefits has sharply eroded. The maximum Pell Grant declined 16 percent in constant dollars between 1980 and 1989; funding for Supplemental Educational Opportunity Grants declined 25 percent; College Work-Study 29 percent; Perkins Loans 58 percent, and State Student Incentive Grants 39 percent.

As a result, access to higher education and the ability of low-income students to choose the college or university that best meets their needs has become a more serious problem. As Guaranteed Loans were converted from loans of convenience for middle-income students to a need-based program, the number of low-income students borrowing and defaulting has grown alarmingly: annual net default costs, after collections, have risen from less than $200 million in FY 789 to over $1 billion in FY 89.

A primary goal of federal policy should be to provide regular, reliable inflation adjustments to the Pell Grant award and other grant assistance for all needy students. Federal policy should also minimize borrowing by needy students--especially academically at-risk students. This would restore a more appropriate balance of grant and loan funds and would substantially reduce the level of defaults.

A recent NCES study of defaulters demonstrates the result of the current grant/loan imbalance: 50 percent of defaulters never completed a degree program, and another 33 percent earned less than a BA degree. Half of all defaulters were enrolled in vocational programs, and almost half of defaulters had incomes after leaving school of less than $6,000.

The Need to Strengthen Fraud and Abuse Provisions

Such default statistics underline the need to distinguish between institutions which provide effective education and training programs for high-risk students, and those which do not. The Department currently lacks adequate authority to differentiate between institutions and target its actions to those with serious management problems: instead, it must issue blanket regulations which impose unnecessarily restrictive regulations on institutions which manage the federal funds properly in order to regulate those who do not.

It is also vital to strengthen the process for determining institutional eligibility for student assistance programs. As the Department's Inspector General pointed out in his recent semi-annual report to Congress, specific institutional policies and practices contribute directly to the incidence of loan defaults.

Accreditation and licensure procedures and controls must be tightened. The Secretary should have authority to decertify accrediting agencies which are not doing an adequate job, and to remove from eligibility schools whose accreditation has been withdrawn. Accrediting agencies should be given limited protection from damage suits, and authority to use arbitration as an alternative to court action. They should be required to establish standards for minimum length of programs, and to determine whether courses are needed to provide minimum skills for entry-level employment.

States should be required, as a condition for any of their postsecondary institutions to receive Title IV HEA assistance, to assure the Secretary that they have established adequate licensing standards. Such standards should govern the ethical and business practices of all postsecondary institutions, prohibit misleading advertising and solicitation, and establish the rights and remedies of the consuming public. They should also assure that proprietary programs are subject to the same requirements as collegiate programs to demonstrate the need for the course and the quality of instruction.

State guarantee agencies should be given authority to refuse guarantees when they have clear evidence of a potential for fraud and abuse. State education agencies should also be empowered to stay the review, processing, or issuance of any license in cases where officers of the institution have been convicted or are under investigation for violation of state or federal statutes or the regulations of any recognized national accrediting agency.

Further restictions are needed to deal with related issues such as recruiting practices, the eligibility of new branch campuses, the definition of ability to benefit, and the sale of stock in proprietary institutions.

We look forward to working with the Subcommittee in the months ahead to address these and other problems during the reauthorization process, to ensure that the current situation is not repeated.

Senator PELL. Dr. Martin

Mr. MARTIN. Thank you, Mr. Chairman, Senator Jeffords.

Once again, we have the Nation student loan programs in the spotlight, and I guess that has heightened somewhat in the past few weeks as it has become public knowledge that the Higher Education Assistance Foundation had sought permission from the Education Department to transfer some of its loan guarantees to the Nebraska Student Loan program. That was turned down, and I would say that it is my opinion that the refusal of the Department of Education to allow that transfer was a mistake. And had it been permitted, it seems to me that we would not only have minimized Federal costs, but we would have avoided most, if not all, of the public uncertainty that currently is focused upon this important program.

I think it is unfortunate that many people have tried to focus the attention of this as speculation, that it is caused by greed or mismanagement. I can say to you clearly, Mr. Chairman, that I do not believe that that is the case. To the contrary, I think most informed individuals who understand the student loan programs and the functions that are performed by all of the guarantee agencies would judge HEAF's internal operations as some of the best in the Nation.

While the revelation of HEAF's difficulties have caused many to—again, unfairly—criticize the student aid programs and the Guaranteed Student Loan program in particular, I am pleased to sit before you to say that at least on behalf of all of our members, we feel that the program has been and is working very well. The vast majority of students that are served by this program are not only responsibly repaying their loans, but as has been pointed out, they would have been denied opportunity to have successfully benefited from postsecondary education if we had not made these loans available.

If I may, Mr. Chairman, to help illustrate this point, I would like to enter into the record a copy of one of our most recent publications. It is called "Student Aid Success Stories: Celebrating 25 Years of the Higher Education Act." This publication highlights the accomplishments of 46 Americans who have been recipients of Federal student aid since 1965 when that historic legislation was adopted. It shows that the investment that we have made in this country is worthwhile and that clearly these programs, while not perfect, have been a wise investment on the part of the Congress and the United States into its people.

Still, I think there are several factors that need some additional attention, and so let me touch upon some items that I think are important to the discussions before us. First, I think it is important to remember that the Stafford Student Loan program has become the ultimate access program for many students for whom it was not intended. As originally enacted, Mr. Chairman and Mr. Jeffords, we know that the program was designed to assist students from middle-income families who were encountering cash flow problems in meeting their educational expenses.

Today, it is a strict means-tested program for which most moderate income families cannot qualify. As such, the financial characteristics of the current cohort of borrowers are much different today than they were five, six, or even 7 years ago. As we have testified before to this committee, this means that we are dealing with a higher risks portfolio than we were previously.

Second, the proportion of Federal grant moneys available to enable a high-need student to meet educational costs has declined over the past decade, while reliance upon student loans has increased. This increased reliance on student credit programs to initially finance many low-income, disadvantaged, and often poorly prepared students has certainly helped to maintain access to postsecondary education, but it is also resulting in additional default costs and, I might add, the destruction of many students' future credit when they do not successfully persist in their academic careers.

Third, legislative actions to constrain Federal costs in the Part B programs, influenced primarily, again, because of our budget deficits, have imposed unanticipated revenue reductions on all guarantee agencies while simultaneously we have imposed upon them and asked them to perform additional administrative tasks.

If you look at some of the things that we have done—the imposition of the multimillion-dollar spend-down, the recall of agency advances, the limits on the three percent fixed cap on the borrower insurance premium, the reduction from one percent to one-half a percent on the administrative allowances that the guarantors get now when they get the 90 or 80 percent reinsurance figures—these are all examples of how we have squeezed the program financially, at the same time we have increased the risk. And what has occurred during this, Mr. Chairman, is that we have basically eroded reserves, we have disrupted anticipated cash flows, and as a result we have perhaps put more at risk the obligations that the entities are responsible for. Simultaneously, we have asked them to do more.

Fourth, I would make the notice that the primary oversight responsibility for the operation of the Guaranteed Student Loan program with lenders and schools has primarily been shifted from the Education Department to the guarantee agencies without adequate reimbursement to perform such tasks or proper authority to undertake what is sometimes needed, and that is decisive action.

There are many other things that I could say about the program, but I think it is important to recognize that guarantors cannot suddenly terminate its school or lender agreements without going through a defined due process route. And in many cases, the department is responsible for giving that permission, and that permission often comes too slowly.

There is more we could say, Mr. Chairman, but in closing, let me just make three quick points.

First, I believe that the coverage in the popular press and the furor that has resulted from HEAF's problems is resulting in many students and parents who are now calling our institutions and asking whether or not these occurrences will negate their loans for the coming year. While we are trying to assure these students and parents that this will not negatively impact them, people still are unnecessarily concerned. This is, indeed, unfortunate and is causing doubts. We need assu nces as soon as possible that everything is okay.

Second, let me say that I think that the department needs to move very quickly to resolve this in order to alleviate these kind of concerns.

Third, any associated Federal costs that may be incurred as a result of addressing the current problems, we believe very strongly should not come out of the limited dollars that are currently being allocated for the other Title IV programs, either for this year or for next. The money in turn should come first from the funds that are being collected by the department from its IRS offsets, which are doing very well, their other collection activities, or from their own student insurance fund. If additional moneys are then needed, Mr. Chairman, I would suggest that we do it through a supplemental appropriation.

Thank you very much.

[The prepared statement of Mr. Martin (with attachments) follows:]

PREPARED STATEMENT OF A. DALLAS MARTIN, JR., PRESIDENT, THE NATIONAL ASSOCIATION OF STUDENT FINANCIAL AID ADMINISTRATORS

Mr. Chairman, members of the Subcommittee, over the past several months, the operation of the nation's federal student loan programs has been a topic of review by several legislative committees. The scope of this review, however, has become heightened in the past three weeks after it became public knowledge that the Higher Education Assistance Foundation (HEAF) had sought permission from the Education Department to transfer some of its loan guarantees to the Nebraska Student Loan Program, to overcome its intermediate financial difficulties and to meet its financial obligations. The refusal by the Education Department to allow this transfer, in my opinion, was a mistake, and had the transfer been agreed to, it would have minimized federal costs and avoided most, if not all, of the public uncertainty that since has been focused upon the Guaranteed Student Loan programs.

In spite of unwarranted assumptions on the part of some who assumed that HEAF's financial difficulties were caused by greed and mismanagement, the fact is that this is not the case. To the contrary, I believe that most informed individuals who understand the student loan programs and the functions to be performed by the guaranty agencies would judge HEAF's internal operations as some of the best in the nation. In reality, the problems that HEAF is encountering are due: first, to the percentage of higher risk loan paper that comprises its portfolio; second, to the changes that have occurred over the past several years in the financial assurances that undergird the student loan system's structure; and third, to the lack of flexibility afforded to any guarantor to limit its exposure from assuming questionable paper when it discovers that the party with which it is doing business is performing unsatisfactorily.

While the revelation of HEAF's difficulties has caused many to again unfairly attack the student loan programs and to question the worth of the nation's investment in them, I am pleased to appear before you on behalf of the National Association of Student Financial Aid Administrators and our 3,400 members to clearly state that the overall structure of the

Guaranteed Student Loan programs has and is working well, and that the vast majority of students who are served by it not only are responsibly repaying their loans, but would have been denied the opportunity to have successfully benefitted from postsecondary education without such loans. To help illustrate this point, with your permission I would like to have entered into the record a copy of one of our Association's most recent publications entitled *Student Aid Success Stories...Celebrating 25 Years of the Higher Education Act*. This publication highlights the accomplishments of 46 Americans who have been recipients of federal student assistance since 1965.

The enactment of the Higher Education Act of 1965 created the legislation that began the Part B student loan programs, and those programs in concert with the other Title IV student assistance programs have since enabled millions of our citizens to secure the needed education and training to make them productive members of our society. The programs are certainly not without their faults, but overall, they have been, and continue to be, one of the wisest and best investments that America has ever made in its people. That is why NASFAA members and many others who know the facts become very concerned when some people and the popular press focus almost entirely upon the problem areas of the program or on the actions of a few irresponsible people and try to assert that the whole system is flawed and not worthy.

Any responsible evaluation would show that the overall system of student assistance has been, and continues to be, a great success. Still, it is appropriate that this Subcommittee, which has jurisdiction and oversight responsibilities for the programs, monitor them carefully and make changes as needed. There are several factors, however, that need additional attention, and other facts that need to be communicated.

1. *Today, the Stafford Student Loan program has become the ultimate access program for many students for whom it was not intended.* As originally enacted, the program was designed to assist students from middle-income families who were encountering cash flow problems in meeting education expenses. It was also conceived to be a loan program that would only be used to assist students from low-income families as a last resort, and then only after those students had exhausted their eligibility for other grant, work, and more highly- subsidized loan programs.

Since the early 1980s, however, the focus, use, and eligibility criteria for the program have changed dramatically. Today, it is a strict means tested program for which most moderate income families cannot qualify. As such, the financial characteristics of the current cohort of borrowers are much different than they were even five or seven years ago. As we have testified before, these eligibility changes have made the Stafford Student Loan paper "higher risk" than it was before the restrictions were adopted.

2. *The proportion of federal grant monies available to enable a high-need student to meet educational costs has declined over the past decade, while reliance upon student loans has increased.* This shift in funding priorities has resulted in the necessity to award higher than desirable amounts of student loans to nearly all students from low income families, and to many who are not as academically well prepared as some of their counterparts, to pursue postsecondary education. Increased reliance on student credit programs to initially finance poorly prepared students has helped maintain access to postsecondary education, but is resulting in additional default costs and the destruction of many students' future credit when they do not successfully persist in their academic endeavors.

3. *Legislative actions to constrain federal costs in the Part B programs, influenced primarily by overall budget deficits, have imposed unanticipated revenue reductions on guaranty agencies while simultaneously requiring them to perform additional administrative tasks.* Actions primarily precipitated by budget reconciliation over the past few years have resulted in decreased sources of revenues for all guaranty agencies. These actions have made those who have higher than normal amounts of high risk paper, or those who have experienced a significant decline in loan volume to be at greatest risk. The imposed multi-million dollar spend-down, the recall of agency advances, the three percent fixed cap on borrower insurance premiums, and the reduction from one percent to one-half of one percent in administrative allowance paid to guarantors who hit the ninety or eighty percent reinsurance triggers, are examples of revenue changes that have affected the guaranty agencies. In isolation, these changes may appear to be minimal, but taken together, they have reduced incoming funds in a given year, eroded reserves, and disrupted anticipated cash flows needed to meet previously incurred obligations. Simultaneously, additional legislated and regulated responsibilities have been imposed on the agencies which, in turn, have increased their operating costs. The combination of these factors though perhaps well intended, has certainly weakened the overall financial viability of the agencies.

4. *Primary oversight responsibility for the operation of the GSL programs with lenders and schools has been shifted from the Education Department to the guaranty agencies without adequate reimbursement to perform such tasks or proper authority to undertake sometimes needed decisive action.* Over the past several years, the Education Department has significantly reduced the number of program reviews and audits it has performed. In large part, this has been caused by reductions in Departmental salary and expense requests, but also by administrative allocation priorities within the Department. The result has been that the program review and audit responsibility, without reasonable resources or compliance

authority, has shifted to the guarantors. While I believe the agencies have performed this function fairly well given the circumstances, it does not, in my mind, relieve the Education Department of their administrative responsibilities for overseeing and managing the programs. While nobody wants to talk about it, the fact remains that there have been several circumstances in which unsatisfactory performance on the part of some individual schools or lenders was uncovered, and should have been stopped. But the authority for taking this corrective action or initiating the process to terminate these parties rested within the Department. As such, corrective actions to address problem areas have often dragged on for several months, and losses due to these occurrences have been greater than necessary. While we all believe in insuring due process for all parties involved, somebody should have "turned the faucet off" when these circumstances arose rather than allowing the "money to flow" while we performed an investigation to determine who was right. I realize that the Education Department felt it needed additional authority to take some of this corrective action, but I would observe that the Administration has not been as aggressive in making the case for expanding such authority or fully utilizing the authority it has to properly manage the program as well as it could.

It should also be noted that under current statutes and regulations, a guarantor cannot suddenly terminate its school or lender agreements without going through the defined due process route, nor can it limit or define its area of service without concurrence from the Department of Education. Yet, the guarantor has to assume the liability, while the Department resolves the issue. The result is that when problems begin to arise, the guarantor is unfairly penalized because it cannot properly respond in a timely manner to the changing environment in which it finds itself. In large part this is what occurred in the HEAF case. Perhaps it is time we all take anothe look at whether or not this is the way we want the program to operate.

There is much more that could be said in regard to the current circumstance that has necessitated this hearing, but let me close my remarks by making three points.

First, the coverage in the popular press and the furor that has resulted from HEAF's problems is resulting in many students and parents calling schools and asking whether or not these occurrences will negate their loans for the coming year. While we are trying to assure students and parents that it will not negatively impact them, people are unnecessarily concerned, and this is indeed unfortunate and only adds doubts about the programs.

Second, the Department and the Administration can and should take responsible action to resolve the HEAF situation as soon as possible, without compounding the problems or costs that will be incurred.

Third, any associated federal costs that may be incurred as a result of addressing this current problem should not come at the expense of limited dollars that are currently being allocated for the other Title IV programs for the current or the next fiscal year. The Department should first be required to use the funds it is collecting from its IRS off set, its other collection activities, and its own current student loan insurance fund. If these are not sufficient, then additional funds should be requested through a supplemental appropriations bill.

Again, I appreciate the chance to appear before you, and can assure you that our Association will be more than happy to lend any assistance we can in helping to resolve this issue.

TGSLC

Texas Guaranteed Student Loan Corporation

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August 1, 1990

The Honorable Claiborne Pell
Chairman, Senate Subcommittee on
Education, Arts and Humanities
United States Senate
Washington, DC 20510-3901

Dear Senator Pell:

The Department of Education is currently considering several options with regard to the disposition of the current financial difficulties of the Higher Education Assistance Foundation (HEAF). One of the proposals now under consideration would involve the Secretary making Sallie Mae a national guarantor under the provisions of Section 439(d)(1)(D) of the Higher Education Act. This section, in part, calls for:

> "the Secretary determines that (i) eligible borrowers are seeking and unable to obtain loans under this part, and (ii) no guaranty agency is capable of or willing to provide a program of loan insurance for such borrowers...."

The current situation surrounding the HEAF financial crisis in no way creates a situation described in (i) or (ii) above. The network of state guarantee agencies nationwide is most adequate to continue loan access to students in all areas formerly served by HEAF. Furthermore, several guarantee agencies are prepared to assist the Department of Education in a viable solution to the HEAF problem.

Dr. Joe Cronin of the Massachusetts Higher Education Assistance Corporation has offered the Department of Education a most workable alternative involving several major guarantee agencies who would be willing to accept responsibility for the student loans within the HEAF portfolio from their respective states. A copy of the "Massachusetts Solution" is enclosed for your review.

I urge you to express to the Department of Education strong support for this solution. No single entity in the Guaranteed Student Loan Program, including Sallie Mae, is in a financial position to accept the entire HEAF portfolio without incurring a potentially seriously unacceptable future liability. No alternative should be

The Honorable Claiborne Pell
August 1, 1990
Page 2

pursued that would weaken the relative financial position of the respective entities in the GSLP marketplace.

Whatever solution the Department of Education ultimately chooses must restore public confidence in the integrity of the GSLP and reaffirm the time-honored policy of the federal government to stand behind the guarantee on the student loans. Access to guaranteed student loans must be maintained. TGSLC and its several state guarantee agency colleagues stands ready to cooperate with the Department of Education in that effort.

Your attention to this most serious matter is greatly appreciated.

Sincerely,

Joe L. McCormick

Joe L. McCormick
President

JLM/alg

Enclosure

cc: Members, Senate Subcommittee on Education,
Arts and Humanities

Joseph M. Cronin
President

Berkeley Place at 330 Stuart Street
Boston, Massachusetts 02116

Telephone 617 426-9434

Massachusetts
Higher
Education
Assistance
Corporation

July 25, 1990

Edward C. Stringer
General Counsel
U.S. Department of Education
Room 4091
400 Maryland Avenue, SW
Washington, DC 20202

Dear Mr. Stringer,

The Department of Education has asked for suggestions on how to deal with the education loan guarantee function of a multi-state guarantee agency.

First we recommend:

1. broad consultation with major players who have a strong record of participation in the program. The Department is entitled to the best thinking of members of the National Council of Higher Education Loan Programs and of the Consumers Bankers Association. Education loans are made possible by a public-private partnership and problems ought to be addressed with the assistance and advice of large stakeholders and partners.

2. solutions that strengthen the state-based nature of the program. It is very difficult for the Department or for any one guarantor to deal with 8,000 schools and 14,000 lenders. These relationships can be better maintained at a state level. A major solution would be to assign responsibilities, including for career schools, back to the states in which the schools exist or the students live so that the schools (and lenders) can be properly reviewed and assisted.

The Higher Education Assistance Foundation has assisted national organizations as well as the several states for which they are the designated guarantor. The proper solution is to ask each of the other fifty guarantors to assume responsibility for all of the schools in their state. This was and remains federal policy, one preferred by the vast majority of state public and private guarantors.

You have requested our assistance in offering solutions to the current HEAP situation. We are pleased to respond. Attached please find a concept paper which we hope addresses the major concerns.

Please feel free to contact me should you have any questions.

Sincerely,

Joseph Cronin

Joseph M. Cronin
President

MHEAC CONCEPT PAPER

The U.S. Department of Education and Congress must address two aspects of the problem should any guarantor cease to be financially viable.

1. how best to make new loans available, and;
2. how to handle the existing portfolio of loans.

1. Making new loans available is the easier problem. Each school, lender, and state could pick a guarantor which is either geographically proximate or which could establish an affinity with that state, territory or district. It would be prudent to encourage multiple guarantors to offer new loans rather than let any one guarantor make one billion dollars of additional student loans. Bigness carries heavy risks, a potential neglect of preclaims assistance, a lack of familiarity with lenders and schools, and some serious diseconomies of scale. Also, any guarantor growing more than 100 percent in one year could find themselves broken by the additional burden one year later.

   The Department should assist guaranty agencies in developing capacities to take on an additional state if necessary. Some of this has taken place in the past on a voluntary basis such as when Pennsylvania (PHEAA) assumed new guarantees for South Dakota after Congressional mandates to spend down reserves. Other guarantors have assisted other states with loan processing or servicing function on a contract basis.

   Most student loan programs are and should continue to be operated on a state basis. During the 1970's there was concern that minority students did not have access to student loans. Citicorp, Sallie Mae and HEAF pledged support to United Negro College Fund colleges and to Hispanic parents in the League of United Latin American Citizens to make student loans available. Subsequently several states properly have assumed this responsibility, found lenders, and provided capital to all students and their colleges. That is the basic format provided for in the Higher Education Amendments; to ask one guarantor to do that which is presumably required of all guarantors may perpetuate inequality of service and concentrate risks of service to low income students on one guarantor. In fact, each state has signed an agreement to serve the students in that state.

The Department should convene a meeting to seek collaboration among guarantors to provide access to new loans. The staffs of NCHELP and CBA will provide support and leadership in obtaining commitments. Each of these associations has elected leaders who are major participants in the education loan program. They are pledged to maintain access for students and to ensure conscientious administration of programs.

2. The assumption of responsibility for approximately $9 billion in existing student loans is a heavy burden. It should be shared among three or more agencies.

The Department might be concerned that a large portfolio be "broken up" in the process of being parcelled out. However, HEAF loans are currently in many places -- with HEMAR in Minneapolis, in Texas agency, also in Ohio, and with Sallie Mae and elsewhere. Responsibility or ownership of loan portfolios can transfer well when they are kept with the same servicer. They can be sold and divided into parcels as, indeed they often are, either before or after going into default.

The existing $9 billion in guarantees could be divided into bundles of $1 billion, $2 billion, or $3 billion and apportioned among three, four, five or even nine guarantors. Each would be assured 100 percent guarantees for loans already approved. This reinsurance provision would be necessary for a period of time.

The cost to the federal government for this reinsurance is reasonable -- about one cent on the dollars of total loans for year one, one half cent the second year, and half that for year three.

The Department will be obligated to pay 100 percent on HEAF claims now held and to be submitted in October 1990, first month of the new fiscal year.

No existing guarantors would be able to pledge existing reserves to do anymore than pay claims promptly. For this purpose agencies might require assurances of expedited payments to reinsure one million dollars in claim payments a day, $20 million a month (but above the $3 million a day and $60 million a month now paid by HEAF). Again it would be more manageable for the Department to ask three or more guarantors to process and pay these claims.

Also, three agencies might have more success in claims aversion. The effective guarantors in 1990 do not rest with the minimum phone calls but rely heavily on computerized services and auto dialers to make as many as twenty or thirty calls to delinquent or pre-default borrowers. On a huge portfolio these efforts become extremely cost-effective. The Department of Education should require the guarantors give evidence of their performance in using pre-claims aversion techniques.

There are additional measures the Department should take. The Inspector General and several guarantors have taken aggressive action to identify schools which violate federal regulations, which short change students and spoil the program.

A team of fifty federal program reviewers, Inspector General staff, and FBI agents should visit those 250 schools which have the highest incidence of cancellations and defaults and the lowest rate of program completions and placement. These are ineffective schools and chains of schools. They should be suspended from the programs. The weakest will then fold. This will save money for the government and preserve the career aspirations and credit capacity of prospective students. Access to inferior educational programs is no access at all.

The existing collection of schools, and a few lenders, need aggressive policing. Again, multiple guarantors could handle this function better than any single guarantor. The advantages to the federal government will include substantial cost-savings from subsidies on loans not made and improvement of program integrity.

We are pleased to offer additional details (below) which adhere to the above fundamental position. MHEAC is also willing to accept a leading role in coordinating participating guarantee agencies.

I. Management and Systems Integration

While this is one of the most critical aspects in formulating a plan for the transfer of HEAF's various functions and responsibilities, we feel seriously hindered in addressing specifically management and system issues without obtaining some essential data. We would hope, that the selection process would allow for the Department of Education to provide, or, at a minimum, facilitate the delivery of appropriate data prior to selection. Section V of this proposal addresses a number of related data requests.

In addition, the ability of any guarantor to effect a smooth transition is predicated on the assistance and support of appropriate and skilled HEAF staff. We would want to gain the confidence of individuals who are dedicated and knowledgeable in each HEAF student loan area. For this purpose we would review performance records and conduct personal interviews with staff. At any rate, we would want to minimize personnel disruption and to assure key individuals of our intention to provide a continuing positive working environment.

In order to ascertain proper placement of functions and necessary system enhancements to support the transition, we would conduct a comprehensive review of computerized and manual support systems. Various individual guarantors may be best equipped to handle specific functions, while other components may be most effectively maintained on current HEAF systems through a coordinated servicing arrangement with the participating guarantors. Again, this can only be determined after full review.

II. Distribution Process

As a general concept, of the HEAF portfolio and guarantee functions should be distributed amongst the participating guarantors. Distribution would be based on management and risk assessments, financial and system capacity, expertise, and geographical reach of the various guarantors. For purposes of discussion, the portfolio is divided into four functional areas:

- o new loan volume,
- o loans guaranteed prior to distribution, but not delinquent,
- o delinquent loans and default claims pending,
- o defaults paid prior to distribution.

1. New Loans

New loans may be defined as those loans which are currently pending, or may be generated, by schools or lenders who would generally use the HEAF guarantee. These may fall into three categories:

- o Loans to be guaranteed in HEAF designated states (D.C., Kansas, Minnesota, Nebraska, West Virginia, Wyoming),
- o Special programs such as MedLoans, LawLoans, MBALoans, UNCF, Assured Access, etc.
- o Guarantees from other sources (specialized school programs, FastFile, etc.)

For the first category, our proposed approach would be to review in detail the various HEAP programs in each state. The review will require disclosure and thorough analysis of information in response to questions noted in Section V of this proposal. In general, however, we would recommend the redesignation of guarantor for each of these states amongst the participating guarantors. This will insure that uninterrupted support and access to student loan funds for students, schools, and lenders in these states is matched with the ability of the designated guarantor to absorb and guarantee this new loan volume.

Special programs will be reviewed in the same manner and assigned to participating guarantors based on fit with existing guarantee agency programs. For example, MHEAC currently supports the Law Access Loan Program, which may be compatible with the current HEAF LawLoans portfolio, minimizing disruption and facilitating the transition to the new guarantor.

In general, for the third group, a state by state review would be conducted
and, where possible, these guarantees would be assigned, after some transition period, to local guarantors . If we are unable to convince all state guarantors to assume guarantee responsibilities, then the participating guarantors would recommend distribution based on an appropriate fit with their existing portfolios. In the event that the portfolio mix is unable to support integration of some of these programs, we would recommend the adoption of lender of last resort criteria.

In all cases we would want to ensure consistency of guarantor for students with prior HEAP guarantees so that prior and future loans are not split between participating guarantors.

2. Loans guaranteed by HEAF but not delinquent

Loans already guaranteed by HEAF would be subject to review and analysis, again based on questions posed in Section V of this document. While these loans are all part of the current HEAF portfolio, actual servicing may be handled by a number of different lenders and servicers. We recommend the following:

- Immediately identify significant holders and servicers,
- Gather data specifically related to holder and servicer portfolios, e.g. volume, delinquency rates, status (in-school, deferment, repayment, etc.),

- o Establish appropriate communication with these entities for purposes of facilitating transfer of the guarantee without jeopardizing due diligence, timely filing, or pre-claim aversion support.
- o Assign various holder/servicer groupings among the participating guarantors.
- o Any transfer made would take into account geographic location, system capacities and specific guarantor portfolio mix.

3. Delinquent loans and default claims pending

Loans which have already moved into stages requiring pre-claim assistance or claim processing and payment would be analyzed separately to ascertain immediate action requirements. Such action would include:

- For delinquent loans not yet in default, participating guarantors would work with holders and servicers to assure immediate pre-claims claims aversion activities.
- Depending on our review and assessment of HEAF's internal systems capacities, we may elect either to use HEAF's systems to support these activities or to transfer activities to those guarantors most able to step in immediately; in either case, a focused management program would be established in order to minimize default activity.

- For claims already in process at HEAF, we would assess the capacity of the HEAF system to conduct review and process claims for payment. If necessary, these claims would be transferred to one or several of the participating guarantors for claim payment processing.

4. Defaults paid by HEAF prior to distribution

We understand that the Department of Education may be interested in assuming this portion of the HEAF portfolio. However, in order to ease administrative burden on the Department, to support continued timely due diligence, and, where possible, to improve on HEAF recoveries, participating guarantors would be willing to step in and assume portions of the portfolio that fit most closely with their current default recovery activities. In this case, distribution, for example, might be appropriate by current residence of defaulted borrowers.

Additionally, the guarantors would deliver information for IRS offset, federal employee match programs, perform credit bureau reporting requirements, and work with external agencies and law firms for appropriate pursuit of these accounts.

III. Guarantees and Administrative Costs

While we obviously need to obtain more information before defining a proposal, we would propose, in general, the following:

- The Department of Education would fully reinsure all claims that are pending with HEAF at the point of transfer.
- This full reinsurance would be extended for some period of time probably 12-18 months) to loans that have been guaranteed by HEAF prior to the point of transfer; the specific length of this "grace period" would be determined based on further analysis of the HEAF portfolio.
- We would require an arrangement with the Department whereby participating guarantors would be reimbursed for claim payments on an accelerated basis for a period of time to be mutually determined.
- At the end of the "grace period", each participating guarantor would incorporate all transferred loans into their individual loan portfolios for purposes of federal reporting, including trigger rate calculations.
- We would expect that the Department would hold harmless the participating guarantors from any violations prior to transfer, including gaps in guarantee agency due diligence, improper review of accounts for claim payment, or any errors or omissions by the guarantor in making or servicing the loans.
- The effective date of transfer shall be mutually agreed to by the Department of Education and the participating guarantors.
- The participating guarantors will assume full responsibility for complying with federal guidelines for all activities after the agreed-to transfer date.
- The Department of Education and the participating guarantors will mutually agree on an appropriate reimbursement for expenses incurred by the participating guarantors in relation to this activity for the period up to the effective transfer date.

V. Data Requirements

To the extent possible, the data on HEAP requested should cover at least a three year period.

- Most recent audited financial statements.
- Most recent biennial compliance report.
- Federal quarterly reports.
- Copies of manuals of internal procedures, school and lender procedures.
- Computer system documentation, including user manuals, functional specifications, flowcharts, description of computer hardware, etc.
- Copies of most recent federal audits or reviews.
- Copies of contracts with external vendors or servicers.
- Copies of lender and school agreements.
- Description of portfolio by program (Stafford/PLUS/SLS). Details to be discussed with appropriate individuals.
- Monthly pre-claim and claim activity reports, including pre-claims received and cured, claims received, rejected and paid.
- Management reports for recovery activity, including recoveries and placements for outside vendors.
- Internal budget income and expense reports.
- Internal financial projections or planning models.

Timing and Support

Speedy action is required.

1. Within 48 hours ten of the leading student loan experts in the nation could be summoned to a meeting in Washington, D.C.

2. The Department must be perceived by state guarantors as a leader, a convener, a problem-solving partner not simply a passive and reluctant regulator or inspector. For an effective, low cost solution in 1 percent of the total liability, everyone must come together and provide mutual assurances.

3. Three professional associations can provide positive, constructive logistical communication, and public information support:

   The Consumer Bankers Association, the largest education lender.
   The National Council of Higher Education Loan Programs, the 56 guarantors, secondary markets, and others.
   The National Association of Financial Aid Administrators, the campus aid officers.

   Each of them know about the problem, as does Sallie Mae, and can assist in promoting a speedy consensus and legitimizing any constructive action.

4. There must be assurances that the loans will remain in existing locations. It is not possible even with tape transfers, to shift batches of $100 million in student loans from one servicer to another. This means that Sallie Mae, HEMAR and other services must be assured of a continued flow of fee revenue for the first year. They, too, must be involved in meetings and consultations.

NORWEST BANKS

Norwest Student Loan Center
101 North Phillips Avenue
Post Office Box 1028
Sioux Falls, South Dakota 57117-1028
605/339-7300
1-800-658-3567

July, 1990

I looked up the definition of "Success" the other day. The dictionary says it is "The achievement of something desired, planned, or attempted." That's true, as far as that definition goes. However, the definition is too passive, too austere, when you're talking about Student Aid Success Stories. It doesn't speak of the incredible effort many of these former students have made, and the obstacles they had to overcome, to achieve their success.

Obtaining a post-secondary education is never easy. For those without adequate financial resources, it becomes close to impossible. Financial aid is the great equalizer, allowing those students who lack resources to have the same access to college or trade schools as those who are financially well off.

It is for this reason that Norwest is proud to sponsor NASFAA's Student Aid Success Stories book. We want to spread the word that if a student has the determination and energy to seek a post-secondary education to help him or her become a success, financial hardship will not stand in the way.

Sincerely,

Jon A. Veenis
Vice President
Student Loan Manager

JAV:dms

Introduction

Many of the Student Aid Success Stories profiled in this book would not be here if not for an event that occurred nearly twenty-five years ago, on November 8, 1965. Sitting at a desk at Southwestern Texas State College, his alma mater, President Lyndon B. Johnson signed into law the Higher Education Act of 1965. In so doing, he opened the doors of the nation's schools, colleges, and universities to all academically qualified citizens, regardless of race or socioeconomic status.

The genesis of this historic legislation goes back to January 12, 1965, when President Johnson sent Congress a special message on education. "Toward Full Educational Opportunity" stated that "every child must be encouraged to get as much education as he has the ability to take." Specifically, President Johnson said that "four major tasks confront us:

- To bring better education to millions of disadvantaged youth who need it most;
- To put the best educational equipment and ideas and innovations within the reach of all students;
- To advance the technology of teaching and the training of teachers; and
- To provide the incentives for those who wish to learn at every stage along the road to learning."

Ten months after his challenge to Congress, President Johnson signed into law the Higher Education Act, which addressed the postsecondary goals of his education message. The Act included Educational Opportunity Grants, the first program of scholarships to undergraduates ever passed by Congress; federally insured student loans, which evolved into today's guaranteed student loan programs (Stafford, PLUS, and Supplemental loans); and a continuation of the National Defense Student Loans and College Work-Study programs. Over the years, the Act became the comprehensive umbrella for all federal programs (other than research programs) supporting higher education.

Looking back, we see that the promises held out by the Act have been fulfilled for millions of our citizens. The Success Stories featured in this book are representative of those who have been afforded the opportunity that President Johnson envisioned and who had the opportunity to succeed because of the nation's investment in them. As we read the stories of these Student Aid Successes, let us remember the words of President Johnson as he signed the Higher Education Act:

"When we leave here, I want you to go back to your children and to your grandchildren.... Tell them we have made a promise to them. Tell them that the truth is here for them to seek. And tell them we have opened the road and pulled the gates down and the way is open, and we expect them to travel it."

Kathleen Hogan McCullough
NASFAA National Chair

Dallas Martin
NASFAA President

Public Law 89-329
89th Congress, H. R. 9567
November 8, 1965

An Act

79 STAT. 1219

To strengthen the educational resources of our colleges and universities and to provide financial assistance for students in postsecondary and higher education.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Higher Education Act of 1965". Higher Education Act of 1965.

TITLE I—COMMUNITY SERVICE AND CONTINUING EDUCATION PROGRAMS

APPROPRIATIONS AUTHORIZED

SEC. 101. For the purpose of assisting the people of the United States in the solution of community problems such as housing, poverty, government, recreation, employment, youth opportunities, transportation, health, and land use by enabling the Commissioner to make grants under this title to strengthen community service programs of colleges and universities, there are authorized to be appropriated $25,000,000 for the fiscal year ending June 30, 1966, and $50,000,000 for the fiscal year ending June 30, 1967, and for the succeeding fiscal year. For the fiscal year ending June 30, 1969, and the succeeding fiscal year, there may be appropriated, to enable the Commissioner to make such grants, only such sums as the Congress may hereafter authorize by law.

DEFINITION OF COMMUNITY SERVICE PROGRAM

SEC. 102. For purposes of this title, the term "community service program" means an educational program, activity, or service, including a research program and a university extension or continuing education offering, which is designed to assist in the solution of community problems in rural, urban, or suburban areas, with particular emphasis on urban and suburban problems, where the institution offering such program, activity, or service determines—

(1) that the proposed program, activity, or service is not otherwise available, and

(2) that the conduct of the program or performance of the activity or service is consistent with the institution's over-all educational program and is of such a nature as is appropriate to the effective utilization of the institution's special resources and the competencies of its faculty.

Where course offerings are involved, such courses must be university extension or continuing education courses and must be—

(A) fully acceptable toward an academic degree, or

(B) of college level as determined by the institution offering such courses.

ALLOTMENTS TO STATES

SEC. 103. (a) Of the sums appropriated pursuant to section 101 for each fiscal year, the Commissioner shall allot $25,000 each to Guam, American Samoa, the Commonwealth of Puerto Rico, and the Virgin Islands and $100,000 to each of the other States, and he shall allot to each State an amount which bears the same ratio to the remainder of such sums as the population of the State bears to the population of all States.

1965 1965

Stanley Koplik
Board of Regents Executive Director
B.A. State University of New York, College at New Paltz
M.P.A. New York University
Ph.D. The University of Kansas

Stanley Koplik, Executive Director of the Kansas State Board of Regents, was appointed by the Senate to serve a three year term on the Advisory Committee on Student Financial Assistance. According to Stanley, it provides "an objective view of current financial aid mechanisms and procedures with an eye towards improving the student aid system, from both philosophical and mechanical perspectives."

The Committee makes recommendations to Congress and the Department of Education on how to work with the $20 billion financial aid programs. "Being on the Committee gives me a great opportunity to visit with some of the best minds on student aid issues. Coincidentally, I am then able to bring back to Kansas many new thoughts."

The Kansas State Board of Regents oversees the organization, management, and control of the state's universities and colleges. Stanley is the principal liaison between the Board and the campuses.

Before accepting his current job, Stanley was the Commissioner of Higher Education in Missouri and a Budget Analyst for the state of Kansas. He also worked for the U.S. State Department as Chairman of the Department of Social Sciences at a diplomatic high school in Pakistan. In 1985, Stanley was Chairman of the Kansas Public Television Board. "We distributed funding to the public radio and television stations. It was exciting since I had a hand in directing the course of public broadcasting in Kansas.

"I worked throughout college, but I reached a point where I needed a little help to pay all of the bills. Financial aid allowed me to complete my education on schedule."

Rod Bartlett
Chemistry and Physics Professor
B.S. Millsaps College, MS
Ph.D. University of Florida

Today Rod Bartlett is an accomplished author, lecturer, scientist, and professor at the University of Florida's Quantum Theory Project, the largest institute of its kind in the world. When Rod entered college 25 years ago, he wasn't sure whether he wanted to be a poet or a scientist. "The decision was made when I finally realized I never knew what T.S. Eliot was trying to say.

"I was just a 'B' student in high school, but there was never any doubt about going to college, even though I was the first in my family to go. We just weren't sure how the bills would be paid."

Rod is a Graduate Research Professor of chemistry and physics at the University of Florida, a rank that is held by only two percent of the university's professors. He has written more than 175 research papers in quantum chemistry. Aside from his more serious articles, Rod injects trivia questions and humor into his writing—like an article entitled, "Theoretical Chemistry: or how to do chemistry with mathematics and computers instead of test tubes and smelly laboratories."

Since his Phi Beta Kappa collegiate days, Rod has been lecturing, teaching, and researching around the world. Earlier in his career he was awarded a National Science Foundation Fellowship, which he used to study in Denmark. While there, he played in the Danish version of the National Basketball Association. He has been a Guggenheim Fellow and a visiting scientist in Germany, and has lectured at conferences around the world.

"The U.S. *has* to have federal financial aid to educate our young. The 1965 Higher Education Act was so crucial because it attracted people to teaching."

"My education gives me the opportunity to influence the federal direction of student financial aid."
Stanley Koplik

"Federal financial aid was essential in enabling me to achieve my academic and scientific goals."
Rod Bartlett

1967

"Without financial aid, I could not have paid the bills. It's that simple."
William Ebbeling

William Ebbeling
Head of Allergy and Immunology
B.S. Wheaton College, IL
M.D. The Bowman Gray School of Medicine, Wake Forest University, NC

Dr. William Ebbeling knew at a very early age that he would attend college. He also knew it would take a long time for his family to save enough money to help pay his way.

It has been a long journey to the National Naval Medical Center where he is Head of Allergy and Immunology. He also serves as allergy advisor to President Bush's personal physician.

"When I was 12, my uncle bought a bakery truck to deliver bread, doughnuts, pies, pastry, and soda from house to house. On Saturdays I went to his house at 7 a.m. to help him deliver. At the end of the day he paid me, and about 80 percent of my money went into the bank. I saved about $1,000 for college."

During college William worked as a secretary. Summers he worked in factories making textile parts for machinery "I really needed those jobs, so I'd finish school on a Friday, be home on Monday, get the job on Tuesday, and work through the summer until the day before I left to go back to college.

"The school expected parents to pay everything they could. My father worked, but without more than a high school education, he only made minimum wage. At thirteen, his parents signed him out of school so he could work on a farm to help support the family through the Depression. When he was old enough to be out on his own, it was the World War that intruded.

"My father returned home and he and my mother were married. I was their first anniversary present. To support our family, he had to work at the factory. In fact, it was his job I worked one summer. My dad was a brilliant man and his job frustrated him. Throughout my younger life he always told us 'if you don't want to have to work at the factory, get an education.' Books were always encouraged. Because I knew I would go to college, when I was a kid I started working.

"It took me ten years to pay my loans back, but I was able to do so because I had the education. Medical school became a 52 weeks-per-year training program. Again, financial aid picked up what I couldn't pay. Student aid really made a difference. Every week in the mail I got a letter with $5 from my parents. They were contributing everything they could. The 1965 Higher Education Act provided the loans. I wouldn't conceive of not paying them back. I hope that money now goes to someone else to go to college."

Margaret Workman
State Supreme Court Justice
B.A., J.D. West Virginia University

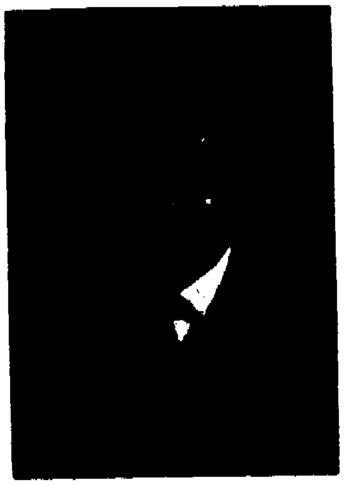
The daughter of a coal miner, Margaret Workman became the first woman elected to a statewide office in West Virginia when she became a Justice of the State Supreme Court of Appeals in 1988. At one time she was the youngest circuit court judge in the state. She also was the first in her family to go to college.

"I never thought about going to college, yet I always assumed I would graduate from high school." Then a ninth-grade teacher approached her about attending college and the whole world opened up for Margaret. Financial aid permitted her to explore that world.

"Without financial aid, I could never have gone to college and then to law school. Receiving financial aid added to my life as the education that I've received has.

"I would encourage legislators, when they are addressing federal financial aid, to consider financial aid legislation that provides those who have the capabilities the chance to go to college. Not only is the pragmatic return to society great, but the financial return through contribution to society is also great, and must be considered."

1968



Norman Rice
Mayor
B.A., M.P.A. University of Washington

Norman Rice won 57 percent of the vote in 1989 to become the first black mayor of Seattle even though he entered the race just a half-hour before the filing deadline. In 1962, though, Norman was not having the same kind of luck. He flunked out of college and didn't return until six years later, when he spent a year at Highline Community College in Washington getting back on his feet. "I had a family to support and I really needed assistance to get a degree. The availability of financial aid is critical because it is an investment in the future," Norman says.

He went on to a successful career as a radio and television reporter, writer and editor, and Assistant Director of the Seattle Urban League. Norman also served three terms on the Seattle City Council, where he promoted neighborhood anti-crime teams, assistance programs for low-income families and seniors, and the addition of 100 more officers to the Seattle Police Force.

Among the Mayor's top priorities for Seattle are strengthening the public school system, creating partnerships between police and the communities they serve, and restructuring city government to be more responsive and accessible to citizens.

Frank Kuss
High School Science Teacher
B.S. Valley City State University, ND

"The way our economy is going, 'middle-income' is eroding to the point that there will be no real middle-income families soon. Those families will become lower-middle-income, making it increasingly difficult for students to depend on their parents' contributions for higher education funding. Without financial aid in the picture, these students won't be able to go to college."

Frank Kuss and his six siblings grew up in a small farming community in North Dakota. Neither of his parents advanced beyond eighth grade yet they encouraged their children to attend college with the hope of contributing what little they could. To help cover his college costs, Frank worked at varied places such as the student center, a cheese factory, a gas station, and a lumber yard.

"If financial aid hadn't been there, I might be a truck driver, or working with equipment or something similar because I'm mechanically inclined." Instead, Frank is leaving his mark on Minnesota high school students by teaching earth, life, and physical chemistry.

Frank's sister Betty, Financial Aid Director at Valley City State University, also benefitted from Frank's financial aid. "Our folks never had anything to give for our educations," she says. "I got a job working in Valley City State's financial aid office because Frank knew about it and the good work they did. If it weren't for him, I wouldn't be where I am today."

"I would not be the Mayor of Seattle if it weren't for the student aid I received."
Norman Rice

"Without financial aid, how can students make it? In small communities, the number of jobs for teens is limited so it is hard for them to work to earn money for college."
Frank Kuss

1969

Frank Candalisa
Director of Financial Aid
B.A. St. Mary's Seminary and University, MD

"There were four of us children born within the span of six years, so there were two in college at one time or another. Needless to say, this was a strain on my family's finances," says Frank Candalisa, Director of Financial Aid at Our Lady of Holy Cross College in Louisiana.

"If financial aid is not there for those who need it, the 'thousand points of light' will burn out. We cannot afford to let education become accessible only to the rich."
Frank Candalisa

In his first year of college, Frank had to have a colon resection, which increased the financial burden on his family. During his undergraduate career, he was hospitalized four more times, and in graduate school he suffered two heart attacks. His family's resources were quickly depleted. "I was able to continue my education through the help of financial aid. Having worked with financial aid at a proprietary school, a four-year public, and a four-year private institution, I can more clearly see how it enables people to complete their education. I have seen first-hand what can be accomplished that would not be possible if it weren't for the federal student aid programs."

Cornelius Davis
Soil Conservationist
B.S. North Carolina A&T State University

Cornelius Davis began studying agriculture 25 years ago. Soon after, he was married and had two children to support. "Both my wife and I dropped out of school to raise our children. It later became more important that she finish school, so she went back to get her degree."

While his wife, Dolores, was studying, Cornelius had some really "dead-end" jobs. He worked in a police records office, but there was only one supervisory position and the man who had it showed no signs of retiring. He worked at a gas station, where the owners felt so sorry for him that they gave him up to 44 hours of work between Thursday evening and Sunday night. "It wasn't much," he says, "but it paid the light and the water bills."

Cornelius went back to school in 1981 with the help of financial aid and earned his degree. He now works for the U.S. Department of Agriculture. "We help citizens preserve natural resources, like soil, water, wildlife, and forestry. From a technical standpoint, I assess situations and give advice. Some of the projects that the soil conservation service advises on range from the installation of a farm pond, creating a grass waterway, and suggesting good crop rotations.

"While a consultant might cost up to $400, my services are free. We also go to schools to educate kids about conservation, enhancing wildlife around homes, and the effects of littering. We sponsor poster and essay contests to get the kids thinking. I really love my job."

Cornelius's roots go back to his Granddaddy's farm. "Being born and raised on a farm increased my appreciation for life. It isn't complete until we've been on a farm. After all, that is where the essence of life lies."

1970

Linda Pelzer
English Professor
B.A. Ball State University, IN
M.A., Ph.D. University of Notre Dame

"My family was from the working class. I was the oldest of six, and the first in my extended family to go to college. Our mother never worked outside of the home and our father worked for 20 years as the manager of an auto parts store and a service station."

With financial aid, Linda began her academic career at Ball State, where she was graduated magna cum laude. She was also able to study for one term at the school's London Centre. In the summers she worked to save money for school.

"The first summer I worked in a factory where, for eight hours a day, I taped wires together that were put into washing machines and dishwashers." During the other summers she found work through the College Work Study Program that was more in tune with her life aspirations, in a hospital for developmentally delayed children. "The work was fascinating! It gave me a great sense of humility, making me patient, tolerant, and accepting in ways I would not otherwise be. I hope I've carried that over in my teaching."

Linda, an expert on American literature, is an assistant professor at Wesley College in Delaware. She teaches composition and is currently working to establish a new English major and minor program for the school.

Linda was able to take advantage of a provision of the old NDSL program that allowed for the partial cancellation of her school loan (up to 50 percent) for each year she taught. "Some students these days are so saddled with their loan debt after college that it is hard for them to repay if they go into a field with lower salaries."

"Ultimately, federal financial aid made possible my degrees and the advancement in my career."
Linda Pelzer

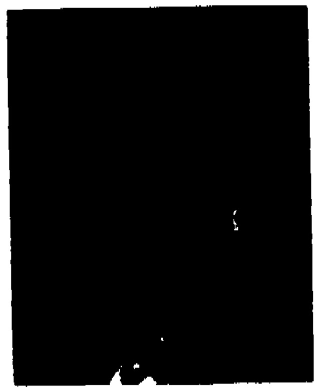
Joe Anderson
Personnel Relations Manager
B.S. North Carolina A&T University

As the third oldest of nine children, Joe Anderson had no family income to rely on to pay for college. "My father was a janitor most of his life, and my mother, with nine kids, didn't work outside of the house. My two older siblings set an example for me to follow by attending college, so college also became a goal for me. All nine of us have gone through college with some kind of aid. I *had* to have financial aid to go to college."

Joe has been with the Eastman Kodak Company since graduation 20 years ago except for two years spent in the Army. In college he had joined the ROTC program and he is still in the Army reserves. Joe was just promoted to Lt. Colonel.

Joe is in charge of Kodak's Pacific Northern area personnel relations department which services about 800 people. After the big earthquake last year, Joe arranged for counseling for some of the families of Kodak employees who were having trouble after the disaster.

1971



Victoria de la Garza
Elementary Instruction Specialist and Language Arts Teacher
B.A., M.A. Our Lady of the Lake University, TX

Fourteen years ago, Victoria de la Garza returned as a teacher to the Texas school district where she'd grown up. Since then, she has been inducted into the school district's Hall of Fame and named Teacher of the Year on her campus.

"The opportunity that was given to me during my college years is still opening doors for me. The fact that I was able to pursue a higher level of education when my parents had not completed high school is an achievement I wouldn't have thought possible. The cost of one year's tuition was half the amount my father was making in a year at the time. Financial aid opened doors for me that I otherwise would not have been able to go through."

Victoria applied for the Teacher in Space program through NASA. "I would still go in a minute if I were to be chosen," she says. She is involved with the Young Astronaut Program at her school and is the state curriculum coordinator for the program. Participants meet once a week to go star gazing, launch model rockets, and take field trips. She serves as the aerospace education officer at a local Air Force base in her capacity as a senior member of the Civil Air Patrol.

"I often talk to my students, neighbors, and parents about financial aid. If I didn't have it, I would probably be doing clerical work." Victoria is serving as the summer school principal for her school. "It's my first time in this position. It is a little more demanding as far as making decisions, but I am really enjoying it."

"College would have been completely out of the question without financial aid."
Victoria de la Garza

"There should never be a chance that someone can be denied an education due to a lack of funds. It almost happened to me. It is necessary to provide money to educate our future leaders, otherwise, they will all be from the elite class."
Andrew McGuire

Andrew McGuire
Foundation Executive Director
B.A. Sonoma State University, CA

"My parents had no money to send me to college. At that time, I didn't have the skills to even go looking for financial aid." To pay for college, Andrew McGuire started the rocky routine of working, then attending school, then working again. It proved to be too much and ended when he flunked out. After getting married, he ultimately transferred to Sonoma State where, with financial aid, he became a full-time junior. He became the first in his family to graduate, and went on for teaching certification.

"Receiving financial aid so that I could go full-time and then finally graduate was extremely helpful to me and my family."

On the morning of Andrew's seventh birthday, the hem of his bathrobe caught fire as he was warming himself next to the open oven door. What resulted were second and third degree burns on his body and admittance to the hospital four times for skin grafts. Twenty-one years later, he read about a little girl who was badly burned when her sleepwear caught on fire. At the time there were standards for sleepwear that protected little children, but not those who wore sizes 7 or larger, as was the case of this little girl. A group of citizens banded together to fight for extended regulations to sizes 7-14 for fire retardant children's sleepwear, and Andrew joined them as a volunteer. He later moved back to California to open a West Coast chapter of this organization.

Today Andrew is the Executive Director of the Trauma Foundation at San Francisco General Hospital, a nonprofit health policy organization working to prevent injuries through stronger regulations. One issue the Trauma Foundation tackled was banning assault weapons in California. He served on the Board of Directors for Mothers Against Drunk Driving and won an Emmy for a film he directed and produced "Here's Looking at You Kid," which aired on public television's NOVA series. Andrew has also been the recipient of prestigious Kellogg and MacArthur Foundation Fellowships.

Nicholas Moscalink
Elementary School Principal
B.S. Baldwin Wallace College, OH
M.S. Cleveland State University, OH

"The rewards of my education have opened up opportunities for teaching, getting into management as a principal, and most importantly, the chance to help kids, to give them guidance so they can grow up to have opportunities from which they can choose what to do with their lives," says Nicholas Moscalink, Principal of Lodi Elementary School in Ohio.

Nicholas is the oldest child of a factory worker with six children. "I had to get through school without the help of my parents. Financial aid allowed me to do that."

In Nicholas's opinion, "it is hundreds of times more costly to give money for prisons or welfare than to put it into financial aid. The return on the investment says it all. Democracy cannot run with illiterate citizens. Only through literacy can people strive to make the world better for those around them."

Elmer Yazzie
Teacher/Artist
B.A. Calvin College, MI

Elmer Yazzie, whose Navajo name means "Little Cottonwood Tree," believes that "every one of us has special talents that are unique. It is important to set goals based on those talents, and decide what you want to do with your life."

Elmer had help in deciding what to do from his high school teachers, who were whites in a predominantly Indian school in New Mexico. They explained to him how wonderful it would be for the community if he were to return to teach after attending college in Michigan. Elmer understood the customs and the culture of the students; his teachers had struggled to learn and understand.

" 'Put your energy into your own community,' " they told me. "Now I tell my students that story and encourage them to return. I didn't come from a wealthy family. Without financial aid I would not have been able to complete my education at Calvin College and return to teach in this way."

Elmer teaches art to students from first grade through twelfth. He is also the cross country track coach and has run in the Boston Marathon. In 1984 Elmer was one of the 50 finalists in a contest for amateur athletes to be on the cover of a Wheaties cereal box. Through the contest he earned $11,000 for his school.

When Elmer was growing up, his father was an interpreter for a white missionary. Now he is the pastor of a small, mostly Indian church. His mother worked as a teacher's aid but went back to college. She is now a kindergarten teacher. "I'm so proud of her. She has such a strong and beautiful inner spirit."

During the summer Elmer paints. His major artistic accomplishments include three murals in New Mexico that total 7,600 square feet. One tells stories of the Bible from a traditional Navajo viewpoint.

"I'm thankful I've had the opportunity to be a role model to our community."
Elmer Yazzie

1973

Laura Adkins
Founder LA Communications and MAGIK Inc.
B.A. George Washington University

Laura Adkins started building her self-esteem the day she quit her job as a window dresser. Her salary was so low that she was living below the poverty line. "I was standing in Safeway with $11.25 to my name when it hit me. I can't live this way anymore."

She quit her job, went on welfare, and enrolled in college. With the help of financial aid, Laura studied art psychotherapy. She worked as an art therapy intern in a hospital and at a psychiatric institute, where she helped place outpatients from a mental health clinic in housing, job training, education, and therapy groups. "I began to see that I could contribute to easing the harrowing journey mentally ill patients make as they reenter the real world."

"Education changed me, it made me brave. I learned how to think on my own, to believe my ideas were okay. It taught me to take risks."
Laura Adkins

One project led to another and Laura found herself with a wealth of knowledge about homeless people and shelters. It became obvious to her that no service existed that matches corporations directly with nonprofit organizations. Thus her concept of 'benevolent waste management' was born.

Laura, a single mother of two, started two companies in Washington, D.C. One, LA Communications, produces books and workshops that address housing-related problems that evolve from homelessness. The second is MAGIK, which stands for Movement and Acquisition of Gifts in Kind. MAGIK is a nonprofit organization that takes in massive donations of goods, like furniture no longer needed by companies, and gives them to nonprofit groups who have a need for them. To move the goods, she hires homeless people who are participating in self-help programs at shelters to get off of the streets and into permanent jobs.

"The word education comes from the Latin root 'educo' to lead out. To educate is to lead out of ignorance, poverty, prejudice, and limitations. To educate is to lead one to be a contributing member of society, one who can make a difference to one's children or one's country."

1974

Phoenix Sinclair
Professor of Dentistry
B.S., D.D.S. University of California, San Francisco
M.P.H. University of California, Berkeley

"I was born in North Carolina and lived on a farm with my grandparents and lots of aunts, uncles, and cousins. We had no money and no knowledge of anything but perpetual sharecropping year after year. I had no one in my family to turn to for information about college, or for financial help, even if I got the information elsewhere."

So Phoenix Sinclair went to live with an aunt in New York City and graduated from high school there with the idea of becoming an engineer. He worked odd jobs for a while, at the post office, in restaurants, and in the garment industry. At 21, he joined the Air Force and was trained as a medical corpsman.

With the idea of being an engineer still in his head after being discharged, he moved to the San Francisco area, worked in a hospital, and went to school part-time. He became an apprentice electronics technician for the Naval Shipyard. That knowledge, plus his medical experience, lead him to a job in the research and development office at the University of California at San Francisco, where he was exposed to dentistry. His interests peaked, so he began to take some pre-dental classes.

In 1972, at the age of 32, married with one child, Phoenix changed his focus and entered dental school. He graduated and joined the dentistry teaching staff at UCSF. Phoenix has since received a master's degree in public health. He has served as Co-Director of the Recruitment and Retention Program, Director of a community dental clinic for the poor and disadvantaged, teacher at the University of Nairobi in Kenya, and is now Coordinator of Alumni Affairs.

Nelson Artiga
Professor of Dentistry
A.A. City College of San Francisco
B.A. San Francisco State University
B.S., D.D.S. University of California, San Francisco
M.P.H. Univ. of California, Berkeley

Dr. Nelson Artiga is the star of a recent television commercial, a parody that plays off the fact that the University of California, San Francisco does not have sports teams. In the commercial, Nelson is notably unsuccessful on the field; but off the field, he is very successful at his mission to return some of his good fortune to his community.

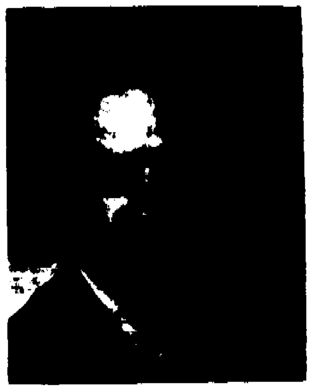
A professor of dentistry, Nelson also holds a master's degree in public health and feels a call of duty above and beyond dentistry. He is actively involved in humanitarian issues on local, regional, and international levels. Nelson was the announcer in a public service announcement about AIDS prevention that aired on a Spanish television channel in the San Francisco area.

Nelson was born in El Salvador, where his father was an attorney. As children, he and his brother came to the United States to live with an aunt when his father was killed. Later, while in dental training, his family received food stamps. "It was not possible for my wife and me to raise children and meet basic living needs without financial aid. Receiving financial aid for schooling was absolutely, fundamentally essential.

"People in the health care professions have a great impact on decreasing total health care costs. We go back to our communities, provide patient care and health education. We research. The return on the financial aid money invested has multiplier effects."

"To decrease financial aid funding is tantamount to unethical behavior towards underserved communities, as well as the nation on the whole."
Nelson Artiga

1975



David Irwin
Speech and Language Pathologist
B.S., M.S. Central Missouri State University
Ph.D. University of Oklahoma

"Fortunately, I was familiar with the financial aid process. My brother and sister had received it. Our parents were farmers most of their lives. Three years in a row the crops flooded. They tried investing in a chicken house, but ran into financial difficulties."

To help defer college costs, David Irwin returned to his high school every summer as a maintenance man through the College Work-Study Program. During school he had a part-time job, making "about $10 to $15 a week which was enough to cover my very basic needs."

"It is so important for us to educate our children. We need to be able to count on the availability of financial aid for those who need it."
Mary Fischer

After graduation with honors, David worked as a public school speech pathologist for three years. He also worked part-time doing progressive speech therapy with juvenile delinquents. After conducting some research, he concluded that there is a high incidence of communicative problems with the juvenile delinquent population that most likely contributes to the delinquents' behavioral problems.

Today David is the head of the Department of Communicative Disorders at Northeast Louisiana University. He is in charge of a clinic where students learn to assess and solve the communicative problems of the clinic's patients. He is also the editor of the Louisiana Speech-Language-Hearing Association and Chairman of the Editors of the State Association Publications Committee for the American Speech-Language-Hearing Association.

Mary Fischer
Director, Public Library
B.S. Valley City State University, ND

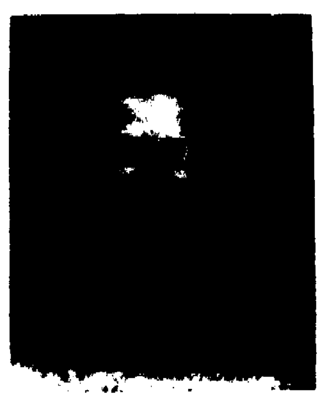
Mary Fischer and her husband had always talked about how she would get an education when the kids were grown. But when she became a widow, she had to support her eight still growing children on her own. With the help of financial aid, Mary entered college to study English, biology, and library science for her education degree.

"I had a problem because I felt I should be home taking care of the children. But at that time I had two in college on financial aid. I figured, if they can do it, so can I! Once there were five of us enrolled at Valley City at the same time. I had classes with four of my girls; two of us were chemistry lab partners. One of my daughters went on to become a librarian too.

"It is fascinating to go through school with your children. I got to know them in a way I could not have in any other situation." Without financial aid, it would have been impossible for Mary, who graduated summa cum laude, to complete her education plus maintain her family responsibilities.

Mary has been Director of the Valley City/Barnes County Public Library for a year and a half. During that time, she established a friends' group for the library and has summer readings for the children.

"With eight children and 15 grandchildren, my horizons are really broadened. Every one of them is into different things that I then get to discover."



1976

Elva Aguilar de Villarreal
Job Corps Representative
B.A. Boise State University, ID

Born in Mexico, Elva Aguilar de Villarreal moved with her family to the U.S. when she was two years old. They didn't settle in one location, migrating as their jobs moved from one crop to another. Because she did not speak English, Elva was not allowed to enter school until the family settled in California where school attendance was mandatory. She was eight years old, too old for the first grade where she belonged. Elva entered the second grade and has flourished ever since, overcoming tremendous hardships.

During her last two years of high school in Idaho, Elva worked full-time on the graveyard shift in a potato processing plant to help support her parents and their six other children. Despite her grueling schedule, she was graduated and got a summer job with the Migrant Education Program as a teachers' aid. There Elva found encouragement to go to college, something she had never considered because there was no way her family could afford to send her. But she had another barrier that she considered even bigger.

"My father didn't think women should attend college. He was really against me going. He was sure I was only interested in finding a husband, and not starting a career. But I had to prove myself, and with the help of financial aid, I was able to enter Boise State with a friend. At the time, we were two of the first Hispanics to attend the school. My friend left after the first 40 days. Many nights I cried, asking myself, 'Should I have gone against my father's wishes?' But if I returned to my family, I would be doomed to continue at the processing plant. So I stayed and things improved."

In the summers, Elva returned to her family to work, eight hours a day with the school district, as well as eight hours at night in the potato plant. All of the money went to her family.

In 1975, Elva was hit by a train. Her injuries required hospitalization for a month, which meant dropping out of some classes. But she persevered and was graduated in the normal four-year period.

Since then, Elva has spent 10 years with the Job Corps in Idaho managing an office that covers eleven counties. She works with 16 to 24 year olds, helping them get their GEDs, vocational training in any of 30 different trades, and admittance to college. "I preach about education to everyone. I want to go on and get my Master's, but right now I have four kids ranging from ages one to twelve who need me. My evenings with them and my husband are precious."

Although she is short on spare time, Elva is active in her community. She is the Vice President of Image de Idaho, a Hispanic organization committed to enhancing education and employment opportunities. "In my day-to-day dealings with youth, I'm continuously surprised at the talent that is going to waste because these kids don't get an education. No one will discover that talent unless we reach out. I'm just trying to return what someone gave to me. I get so many emotional and spiritual rewards from my job."

"Once I entered school, if I had been denied financial aid, I would have had no recourse but to return home to the potato processing plant. Financial aid was my only hope to escape and make something of myself."
Elva Aguilar de Villarreal

1977

"If a child really wants to be something, but can't because of a shortage of funds, it is a tremendous waste."
David Williams

David Williams
Circuit Court Judge
A.S. Patrick Henry Community College, VA
B.S. Virginia Tech
J.D. Campbell University, NC

"A lack of education is the common denominator in the majority of the criminal cases I see," says Judge David Williams of Virginia's 21st Circuit Court. "How much is the person's fault and how much belongs to society? We're not doing a very good job of educating our people."

David is an only child who was raised by his mother, a nurse. "We weren't destitute, but college was expensive. If my mother had to pay the total cost of my education, I could not have gone. Receiving financial aid really took the strain off of our family." At the very young age of 30, David was selected to serve as the local Commonwealth's Attorney after being in private practice for three years. He was appointed later to the circuit court.

David is well aware of the value of education as the difference between success and failure. His concern for the future begins well before the point where financial aid becomes a factor, however. "It is frightening that some of these defendants cannot read or write."

Mary Kay Incandela
Financial Administrator
B.S. Otterbein College, OH

"My parents could not afford to send me to college. I probably would not have gone if it had not been for the help of financial aid," says Mary Kay Incandela, the second youngest of six children. Her father was a steel worker and her mother, who had worked as a Kelly Girl when the children where young, was no longer working when it was time for Mary Kay to enter college.

Even with her College Work-Study job in the library for four years, and the money she made from working extra hours for the business department or tutoring, Mary's financial situation was still tight. "There were many times I had to decide if I should split my laundry into three loads and do it properly, or if I should save it for something else. I have a greater appreciation for the value of my education." Mary Kay figured out exactly how much each of her classes cost so she would resist the urge to skip lectures.

Her calculations paid off. She is now the financial administrator of the Sapirstein-Stone-Weiss Foundation in Ohio, which was established by the founder of American Greetings, Jacob Sapirstein, to support Jewish heritage through grants given to Jewish educational institutions and community organizations.

Mary Kay and her husband have two young girls. To be prepared for whatever post high school plans the girls may have, every month they get a $100 bond. "At 3½ and almost 2 years old they're better off than I was when I went to college," Mary Kay says.

15/8

Theopolis Williams
Physician
B.A. Whitman College, WA
M.D. Howard University, DC

When Dr. Theopolis Williams was a teenager, he did what other teenagers do. He was on the cross country track team, played football, and was even a three-time All-American, all-conference wrestler. He was also the Vice President of his junior class. The one thing that really differentiated Theopolis, the second youngest of five children, from all of his peers was that he didn't live at home. Theopolis was placed in his first foster home when he was three (each of his siblings were placed in different homes). From there the road became even rockier. After surviving a series of homes, a court intervention removed him from one family because he had been beaten.

The picture started to brighten when he was 5 because his mother regained custody of her children. But a few years later, life again became unstable for him, due in part to the addition of a stepfather to the family.

The problems continued at age 11. While on a visit to see his natural father, Theopolis was essentially kidnapped by his father, who kept him for a year before he was allowed to return to his mother.

Unbeknownst to most of his peers, Theopolis lived in foster homes during most of his high school years. He immersed himself in his studies and sports in an attempt to escape. "I liked school and stayed there late just about every day. It meant I didn't have to think about my home life," Theopolis said.

It has been a long and difficult road to success for Theopolis, who is currently a family practice physician at the Yakima Indian Health Center, a low-income facility in rural Washington (he will soon leave that position to work for Kaiser Permanente). He credits his success to involvement in sports, support from his community, and access to higher education.

"I was one of the dirt-poor people. The financial aid opportunities I had in the '70s allowed me to get a higher education. I'm looking at the future thinking 'how will I pay for my kids' education?' I know it's going to be hard for me, but it will be even harder for people who are in the social strata where I came from."

Glenn Patterson
Design Engineering Supervisor
B.S., M.S. DeVry Institute of Technology, IL

To make money while going to college, Glenn Patterson worked many different part-time jobs: in a fast food restaurant, at a manufacturer of scales; in a market research firm interviewing consumers about products; and as a receptionist.

"My father drove a bus and my mother did domestic support work. There just wasn't enough money for college," Glenn recalls. "I would have had to attend college on a part-time basis while working full-time if I hadn't received aid. I'm not sure where I'd be if I didn't have a degree. I would definitely be making less than half of what I do now, with fewer benefits. Financial aid gave me the opportunity to prove myself. Financial aid is sometimes the only answer people have to move on to a better life."

Since he was graduated, Glenn has been promoted three times at AT&T, where he supervises about 30 people on four different projects. His job concentrates on product and design verification and testing products to ensure quality and reliability.

Glenn is involved with AT&T's summer intern program. High school students and college freshmen have the opportunity to work for 10 weeks with the company. "I think they get motivated to stay in school. They learn that the work is worth the effort." He also judges science fairs and has worked with high school mentor programs.

"The educational system can shape youth, in spite of any social disadvantages."
Theopolis Williams

"I have friends who couldn't afford college and didn't know enough to apply for financial aid. They really aren't doing very well now without an education."
Glenn Patterson

1979

Theresa Burbey
President, Accounting Firm
B.A. Silver Lake College, WI

" Life begins at 40 is more than an interesting phrase. I started an exciting career in my life at 40 when I received my degree. The financial aid program made this possible."
Theresa Burbey

Theresa Burbey was interviewing for a part-time position in a financial aid office when she became aware of the assistance programs available to nontraditional students. "My marriage of 17 years had ended and my career goals seemed out of reach," she recalls. Instead of taking the position, Theresa, who had been out of school for 20 years, enrolled as a full-time student in business administration. "Without the assistance of financial aid, obtaining a degree would never have become a reality.

"Through financial aid assistance in completing my academic degree, I was able to start my own accounting and tax services business to serve the 'Mom and Pop' businesses of America with 50 or fewer employees. We're not out to over take the huge accounting firms, but we've been in business for six years, and I love it! Nobody ever told me you don't go out and start accounting practices. I'm glad they never did, I might have listened. Right now I have four full-time degreed accountants and a CPA, all of whom are Silver Lake graduates. We also have an on-going internship program with the school."

Theresa is the mother of three grown sons and is working on her Master's degree, but that hasn't slowed her down. She is currently a part-time instructor at her alma mater and the immediate Past Chairperson of the Board of Directors of the Manitowac/Two Rivers Area Chamber of Commerce. Theresa is also Past President of her alumni association and the Board of Directors of the local Big Brothers/Big Sisters chapter. "If you plant the good seeds of community service in our young people, it is amazing how much our communities can grow and prosper."

1980

Carlos Murguia
Attorney
B.S., J.D. University of Kansas

Janet Murguia
Legislative Assistant
B.S., B.A., J.D. University of Kansas

Mary Murguia
Assistant District Attorney
B.S.,B.A., J.D. University of Kansas

Ramon Murguia
Attorney
B.A. University of Kansas
J.D. Harvard University

The Murguias have a very strong message they want to share with fellow Hispanics. It comes from their parents, Janet Murguia says. "They believe if you do a good job raising your family, good things will happen." The children are carrying that philosophy to their communities in the hope that each will become more tightly knit and better educated.

"Our father was a steel worker for 37 years, and our mother never worked outside of our home. With seven kids — four in college at the same time — financial aid directly affected my position today," says Mary Murguia. "I tell Hispanic kids about the importance of education. I know they can get an education, because we did. We're not geniuses, just hard workers."

Ramon Murguia is thankful that their mother made them speak Spanish at home. "It helped preserve our sense of culture." Mary jokes that her Mom would be happier "if we knew how to make flour tortillas."

Janet performs volunteer work with a mentoring program for Hispanic teens in Washington, D.C. She traveled recently with her boss, U.S. Representative Jim Slattery, to Central America as official observers of the Nicaraguan election for the Organization of American States.

Mary recently was named an Assistant U.S. Attorney for the District of Arizona. She leaves a position as Assistant District Attorney for Wyandotte County in Kansas, where she prosecutes primarily those accused of sex crimes and child molestation. She took an active civic role in Kansas City as Vice President of an advancement group for Hispanic women, and as Assistant Treasurer for the United Way. "I want to help stop the high drop-out rate of Hispanic kids. They need self-esteem and self-respect that only education can give. I didn't go to law school to make money, I went so that I can make a difference."

Ramon works for Armstrong, Teasdale, a large Midwestern law firm in Kansas City, Missouri. "I benefitted from people who helped me get a college education, which put me in a position to help others," Ramon says. One of his reasons for returning to Kansas was to get more people to work together in the community, in the spirit of cooperation. To do so, Ramon took a leadership role in the Kansas City community. As Chairman of the Greater Kansas City Hispanic Development Fund, he oversees an endowment of over $1 million. Ramon also serves on the Board of Directors of the Greater Kansas City Community Foundation.

Carlos Murguia is an attorney with a private practice in Kansas, but also serves as a judge pro tem for Wyandotte County. He is active with the Hispanic Scholarship Fund, a subgroup of the Development Fund, and also serves on the Board of Directors of the local Hispanic community organization El Centro. "Whatever success we have is primarily owed to our parents, Alfred and Amalia, and our older brother, Alfred Jr. because of the good example they set and the values they instilled. Our other sisters, Rosemary and Martha, and Alfred Jr. have always been very supportive and encouraging," says Carlos.

Ramon says what they've achieved is a family success. "All of the credit for the thought that we might be able to make it goes to Alfred Jr. We made the leap of faith because he took the risk of being the first to go to college," Ramon says. He believes he can help more people through his education. "It is a vehicle for giving back to the community. Now I'm in a position to raise funds for scholarships, which takes some of the burden off the local and federal government. We can see a positive future only if we have an educated society. We're trying to send a clear message to Hispanics: work hard, stay out of trouble, and do work for the community, not just for yourself."

"The fact that the four of us, children of a steel worker, have law degrees confirms for our parents what people say about America. It really is the land of opportunity."
Janet Murguia

1981

Thomas LaVeist
Faculty Member
B.A. University of Maryland, Eastern Shore
Ph.D. University of Michigan

Thomas LaVeist grew up in a Brownsville housing project in Brooklyn, New York. "There were gangs and Girl Scouts, PTA and prostitution. Crime, drugs, church picnics, and Little League were all elements of my community. Amidst the contrasts was one sustaining constant. In Brownsville lived the poor.

"Education was the opportunity for me and my family to escape. You could say it saved my life. As a black male in that society, it's common to turn to crime, drugs, or both. Without financial aid I could never have gone to college and who knows where I'd be now."

Except for his senior year, Tom's high school grades were low, as were his SAT scores. He was admitted into a remedial program at the University of Maryland, Eastern Shore, however, and went on to graduate with honors. He then enrolled in the sociology Ph.D. program at the University of Michigan, and finished a seven-year program in an amazing four years. Thomas's 1989 dissertation was awarded the "Best Dissertation in Medical Sociology" by the American Sociological Association. He recently finished a research fellowship at the School of Public Health at the University of Michigan and is joining the faculty of The Johns Hopkins University.

"I did as well as I did because I didn't have to be constantly worrying about where I would get the money I needed to continue my education."
Tammy Lomax

Tammy Lomax
Writer/Editor
B.S. University of Maryland, Eastern Shore

"My parents are factory workers at a Campbell Soup plant. They had some money to help me, but I come from a large family and they could not pay all of my fees. My oldest sister went to college with financial aid assistance. I was very thankful that I was able to receive it too."

To save money for school, Tammy Lomax worked during the summers as a secretary for a law enforcement agency. That position lead her to the Drug Enforcement Administration (DEA), in Washington, D.C. She plans and prepares oral and written communications aimed at all levels of the DEA and the general public.

Tammy writes reports, articles, and testimony, and responds to congressional inquiries to the DEA on drug-related matters. She also writes speeches for the DEA Administrator and program management.

Tammy was graduated cum laude. "The financial responsibilities of a college education were overwhelming to me, and while I was scholastically inclined to attend college, I was not financially equipped. I was able to overcome this one obstacle through federally funded financial assistance."

1982

Carol Sasaki
Founder, HOME Network
A.A. Bellevue Community College, WA
B.A., M.A. Washington State University

Once she was a young victim of incest and rape who was lost to the streets with a baby and a welfare check. Today, Carol Sasaki is the founder and leader of a dynamic national network that connects people to resources that help them get out of poverty, into college, and on to a better life. The HOME network (Helping Ourselves Means Education) started when Carol realized she needed to share the information she had collected on becoming self-sufficient.

Carol's first step towards that freedom came during an unexpected encounter with a college administrator who had been a welfare mother. She told Carol there were two ways to get out of the welfare system: get some skills to sell by getting an education, or sell yourself as a prostitute. Carol discovered that welfare would pay for one year at a technical college, but she wanted more. She hounded the local welfare agency, which finally said yes to two years. She entered Bellevue Community College and went on to Washington State University. When Carol attempted to cram four years worth of school into two, she was hospitalized for exhaustion.

Then another former welfare mother who was studying for a graduate degree showed Carol how to get college credit for independent projects and paid internships. With that income, federal financial aid, low-cost day care, and low-rent housing, Carol was finally able to get off welfare. "It was the most wonderful moment in my life. For the first time I felt in control."

Carol took the opportunity near the end of her final year to express her philosophies about welfare when she received an award for outstanding academic achievement. "I told them I knew 50 other welfare mothers smarter than I am, who would get an education if they knew how. People assume that welfare mothers are stupid and lazy. They're not. They're stuck."

She began to hold small workshops to tell people what she had learned. HOME was born and what emerged was a "buddy network." More than 150,000 people have been part of the HOME network, which is now headquartered in Worthington, Ohio. They are committed to helping themselves and each other escape poverty and dependency through education.

To spread HOME's message, Carol is invited to speak to universities, government agencies, and private groups around the country. She has told her story on national television shows and in several national publications. A very strong part of Carol's message is her belief that "it is better to give people the means to support themselves rather than simply give them the means to exist. Financial aid is access to the American dream and must be a priority. The financial aid office is a must in disseminating that information to the community. By working together with agencies, a communications channel is created to find information and build creative bridges."

"When I was young I thought high school was a prison. By quitting school at 13, I went into the prison of life without an education. Financial aid helped me change that."
Carol Sasaki

1983

Tina Huyck
Environmental Chemist
B.S., Ph.D. Colorado School of Mines

Doug Huyck
Computer Programmer
B.S. Colorado School of Mines

"There would be one less Ph.D. chemist and one less programmer in the U.S., if it weren't for financial aid."
Tina Huyck

"We got married after my first semester in college, and had two children during my undergraduate career. Doug and I were both full-time students during the first year and a half of our marriage. If not for the financial support available to us, one or both of us would have had to sacrifice our education. We lived on about $6,000 a year of loans which meant we ate a lot of rice, but we were committed to our education and our marriage." To make ends meet, Tina Huyck had a full-time job in the afternoon. She attended classes in the morning.

Both Tina and Doug feel very strongly about the importance of getting a higher education. "I'm very worried about my kids and how they will deal with the problems of a generation that is uneducated. Education must be the foundation of a strong America, and investing in the education of young Americans must be a top national priority."

Doug, Tina, and their two daughters, K.T. and Maggie, are moving to Texas so Tina can begin her career with Radian Corporation. She will be consulting with companies on how to prevent or correct environmental problems. "It is the ideal job for me. I think our environmental well being is absolutely crucial. This position will allow me time to publish. That way I won't be far from academia when I'm ready to teach."

"Through education, I learned the skills to compete and to be a problem solver," Doug Huyck says. He graduated with a degree in geophysics and worked in the field until the oil industry crunch hit the Denver area and his company went under. He was able to secure his current position because of his degree.

The Huycks are very active in their community. Tina volunteers with Expanding Your Horizons, a program aimed at exposing girls ages 9 to 14 to nontraditional careers for women. She also works with Odyssey of the Mind, whose focus is to develop young people's problem solving abilities in a group setting. There is an international competition in which the participants compete. Both Doug and Tina are involved with their PTA. Doug is on the Board of Directors of their homeowners association, and helped to establish a computer users group in the Denver area.

1984

Kay Kapeloff
Licensed Practical Nurse
LPN Community College of Rhode Island

"I was frightened to death to go to college! I'd been out of school for over 20 years. My husband was very ill and had to be hospitalized. Later he was put in a nursing home. I had no skills or work experience other than odd factory jobs, none of which could support us without my husband's income."

Kay enrolled at the Opportunity Industrialization Center, a community agency where she took pre-nursing classes. "I had to take biology, chemistry, and algebra for the first time, but I did graduate and enrolled in the LPN certificate program. Every Friday, I drove with the boys in the back seat from Rhode Island to New York where my husband was hospitalized, returning late on Sunday night. I finished with good grades and even made the Dean's List. Now I tell everyone to 'go to college and make something of yourself.' I'm really a big mouth about education changing your life."

After graduation, Kay became an LPN in the same nursing home where her husband was a patient until this spring when he passed away. "He always tried to teach me lessons in a gentle way so that I would be able to take care of myself when he was gone. One day in the nursing home I was extremely busy. He was one of my patients, but because he was also my husband, I asked him to wait a minute. He reported me to my supervisor and I got in trouble! When I questioned him about it, he said, 'Today your husband, tomorrow your other patients.' I'm very thankful he was that way."

Victor Vasquez
Director of State Community Services
B.S. University of Oregon
M.A. Harvard University

Victor Vasquez was one of four children being raised by his father. They were farm workers who lived in migrant labor camps and traveled wherever the crops needed to be harvested. From those experiences Victor learned a lesson he would carry with him forever. "When you're in a position like that, other people make all of the decisions for you. People deserve the opportunity to make their own decisions."

In his position as Director of State Community Services for Oregon, Victor is helping people move into positions where they can make their own decisions. He manages 14 federal grants, coordinates state community services with 36 community action agencies and local nonprofit organizations, and is a liaison to the state legislature.

"The fulfillment of basic needs gives people stability. People don't want to fail, but if they have no hope to achieve a goal and no role models, then achieving those goals is not a top priority. Kids just need a person who believes in them, someone to be a role model for them."

Victor, who was Phi Beta Kappa at the University of Oregon, is on the Board of the Oregon Council for Hispanic Advancement, and is a member of the Portland Political Action Committee, and the Hispanic organization Image de Oregon. "Originally I asked myself, 'Where can I have the greatest impact?' On the state level. Now I'm beginning to ask if I can have a *greater* impact on the national level.

"Without the help of financial aid, I would probably be working in a food processing plant, maybe I'd be a supervisor by now. I wouldn't be on the state level making a difference."

"It's something out of a dream to go to college on loans. This one step of going to college was as big for me as going to the moon. Financial aid moved the mountains I never could have moved on my own."
Kay Kapeloff

"I always knew what I wanted to do. The deciding point was whether or not I would receive financial aid."
Victor Vasquez

1985

Zna Portlock

Labor Relations Counsel
B.A. Pepperdine University, CA
J.D. Pepperdine University School of Law

"My parents had enough money to pay for a roof over our heads, clothes, food, and my undergraduate degree They didn't have $30,000 for law school. The cost of getting such a degree can be debilitating. Very few students can afford that cost."

After completing her double-major undergraduate degree in 2½ years at the age of 20, Zna Portlock (pronounced ZEE-nah) finished law school at 23, and passed the bar at 24. An internship with the television show Entertainment Tonight lead her into entertainment law Her work as counsel to 20th Century Fox Film Corporation concentrates on the arbitration of labor grievances on behalf of the company. "I like my position because it allows me the opportunity to actively participate in structuring settlements and facilitating communications between disputing parties, before the final resort of arbitration."

In her previous job, Zna once had to cross a Teamsters picket line to seek declarations. "I really did not enjoy that," she says. Zna now deals with more than 150 different unions at the studio lot and at the seven television stations within the Fox family.

To support black law students, Zna makes herself available to answer questions and help with job searches. She is on the Board of Black Women Lawyers of Los Angeles and is involved in numerous community projects. This L.A. lawyer believes "there is no hope for many Americans to get an education without financial aid. I would never have completed law school without it."

"How can students even compete for a piece of the American pie without an education?"
Zna Portlock

"I have always wanted to help others who are less fortunate to succeed in life. I hope that one day these people I have helped will do the same for others."
Bernadette Mendez

Bernadette Mendez

Foster Care Placement Specialist
B.A. Allentown College, PA

"I was one of seven children raised only by my mother," says Bernadette Mendez. "My mother was on welfare since she was about 15. In high school, a counselor prompted me to apply for financial aid and go to college. I would never have been able to attend college without financial aid."

Bernie is a foster care placement specialist whose caseload currently consists of 11 children between the ages of 2 and 16 years. Although the children do not live with her, she plays the role of the parent while they are in her care by arranging for medical and dental treatment, working out school problems, enrolling kids in social activities, and assisting in psychotherapy.

In some cases, Bernadette acts as an interpreter for Spanish-speaking children. She also serves as a sounding board for parents and appears at court hearings on behalf of the children.

"I am totally responsible for the children when they are in my caseload I love my job."

1986

Mary Ihns
Speech-Language Pathologist
B.S., M.S. Purdue University, IN

Mary Ihns' family is like so many other families in the U.S.—hard working, lower-middle-class, yet full of love and encouragement. With four children, they just didn't have the resources to pay for college. "Without financial aid, I would not have been able to go to college at all. I am so thankful for the money. I don't know what I'd be doing now if I hadn't gone. I'd probably be an unskilled laborer."

Mary is a speech and language pathologist who provides therapy to adults with head injuries, stroke victims, and children with speech, language, or cognitive skills problems. She loves her work: "It is so exciting to see them get back to things that are important to them, things they had planned on accomplishing.

"This job is just like watching a movie. We strategize about patients' treatments and then work to correct the problems. The amount of tears shed in this office is amazing. The work is exciting and very rewarding. I wouldn't be in this position helping people if it weren't for financial aid.

"The importance of having an educated society can not be stressed enough. The U.S. is built on the notion of opportunities for all. Better funding for financial aid programs is one way for us to prove this is still true today."

Mary is also active in her community. She volunteers with the Special Olympics and at a residence for developmentally delayed children. She has also been a counselor for four summers at a very special camp for autistic children. "It is a whole new experience for these kids to do such a 'normal' thing—to go to camp. The camp also allows the parents to have a respite. And it reminds us that no matter how difficult the kids' behavior is to understand sometimes, they are real human beings."

Cindy Swim
Surgical Nurse
A.A. Indiana University East

Cindy Swim and her husband Dennis just bought their first house. "It's a medium-sized farm house on 18 acres. The roof leaks in a spot or two, but it's ours!" Not long ago Cindy was working on a factory assembly line putting the finishing touches on top-of-the-line caskets. "I hated that job," Cindy recalls. She now works as a surgical nurse in an Indiana hospital. "I love what I'm doing now so much. There is a lot of psychology involved in nursing. I like being able to make someone who has just returned from surgery feel better. It sort of seems I've gone from one extreme to the other."

Cindy and Dennis, who is a truck driver, had just gotten married when he suggested that she go back to school. "He put the idea in my head, but I wasn't sure I could since I'd been out so long. People at the factory encouraged me too. We were going to try to make the costs on our own, but reality set in when we looked at our bills for basic living expenses and decided there was no way.

"When I got the loans I used them only for books and tuition, nothing else. Those loans really saved me. I don't think I would have been able to make the dramatic switch in careers without the financial aid, especially as a nontraditional student. We aren't living with a family who can support us. *We* have to pay the electric and food bills. I swear by college as the means to a job you like. After all, there is nothing more important in life than having a job you enjoy because *everything* stems from that."

"Intelligence and wealth don't always go hand in hand."
Mary Ihns

1987

Boyd Clark
Math Teacher
B.S. Northwestern Oklahoma State University

Louise Clark
Accountant
B.S. Northwestern Oklahoma State University

When competition from larger firms forced their family's meat packing business to close, Boyd and Louise Clark were left with no permanent place to work. "We went from job to job with no security," Louise remembers. Boyd went to work in a gold mine in Alaska, yet they never knew whether he would continue to have a job from one summer to the next. The Clarks decided they desperately needed some job security.

The Clarks moved back to Oklahoma and Boyd began his studies at Northwestern Oklahoma State University. Louise thought she would work and put him through school, but she couldn't find a job. That opened an opportunity for her to go to college. "It was only possible through financial aid," Louise said. For four years they both worked in the summer, with Boyd returning to the Alaskan gold mine.

"They only access we have to education is through financial aid. It helped us realize our goals."
Louise Clark

Louise graduated summa cum laude from Northwestern Oklahoma State University this spring and started a job with Amoco as an accountant. "I've never had a job where someone wanted me so much they'd pay to move us!" Louise says. "I'm marketable now. Before I had to beg, 'Please, take me!' Now I say, 'Look at my transcript.'"

For Boyd, going back to college was a fresh start. He had wanted to be a chemical engineer, but dropped out of school and entered the National Guard. "It was my first failure in life. Going back to school righted the wrong," he said. "When we went to Alaska it kept nagging at the back of my mind—failure. I worked with the local school board up there and tutored math and science, which made me interested in going back to school." Boyd is now a high school math teacher.

"It would not have been possible to do what we've done without financial aid. Not at the same time. I think we've proven we are worth the financial aid we were given. By increasing our earning income, we should be able to help fund financial aid for others through an increased tax base. I get kind of teary-eyed. We're seeing our hopes and dreams realized because of financial aid," Boyd said.

1988

Carolyn Mercer Bowers
Vice President/Physical Therapist
B.S. The University of Maryland, Eastern Shore

Carolyn Mercer Bowers came from Texas as an independent student to The University of Maryland, Eastern Shore to get a degree in physical therapy. Her parents were able to provide minimal initial assistance for a portion of her tuition. After high school, she had worked for a doctor as a receptionist, but felt extremely unchallenged. "The doctor and I would talk about what I wanted to do. He was an important influence behind my pursuing higher education."

Since she was graduated from UMES, Carolyn and her husband have started their own physical therapy practice in the Maryland/District of Columbia area. "With the help of financial aid, I achieved one of my long-term goals by becoming Vice President of our own company. It would have taken longer if I had to sit out some semesters to work full-time. You need to retain the information and carry it over to the following class."

Thanks to student aid, Carolyn was able to concentrate on absorbing new information for her studies instead of worrying about how she would pay the next semester's tuition.

Jesus "Jessie" Camacho
City Chamber of Commerce Manager
B.A. University of Hawaii
M.A. Golden Gate University, CA

Just when Jessie Camacho was really beginning to climb the marketing ranks in Silicon Valley, the firm where he was a vice president merged with another company, leaving him out of a job. "My wife was pregnant with our third child and I was on unemployment. We soon depleted our savings, the compensation expired, and I was compelled to apply for Aid to Families with Dependent Children."

Shortly thereafter Jessie was admitted into a one-year master's program. "The Welfare Department allowed me to borrow through the Guaranteed Student Loan Program because I was making a concerted effort to better myself and remove my family from public assistance."

Upon graduation, Jessie became Assistant Director of Economic Development for the city of Delano, California, as well as Manager of the City Chamber of Commerce. "I am very happy about my new career in the public sector. Sure, I get disgruntled, but that's life. Had it not been for the financial aid I received, my dreams would not have been realized. I had no money, and no contacts to borrow money."

"My admission to the graduate program was valueless without financial aid."
Jessie Camacho

1989-1990

"Companies used to hire on a handshake. Now you have to have a degree."
Roger Dean

"Without the help of financial aid, it was not practical to go to school on a full-time basis, work, and take care of my three children."
Michael Andrews

Roger Dean
Mechanical Designer
A.A. Southwest Wisconsin Technical College

A motorcycle accident in 1986 permanently altered Roger Dean's life. He was working as a machine tool operator but due to a crushed foot and substantial leg injuries, he was prevented from standing and operating the machine.

"I was forced to establish a new life and a new career in a field where I had no real educational background. I was out of a job and had depleted my savings on health care insurance and hospitalization," Roger remembers. "My only choice was to get an education. Financial aid made that possible. I lived 24 miles from school, I couldn't afford a social life, but I had a great grade point average."

Roger is a mechanical designer for the Beloit Corporation, a company that designs and builds paper manufacturing machines. "I've worked with people who only have experience. Today, however, a company will ask, 'what education do you have beyond high school?'. If the industry dries up, what will those people without an education do? Financial aid gave me the opportunity to put my best foot forward and get the education."

Michael Andrews
Student
Hinds Community College, MS

Twelve years ago Michael Andrews went to school to study music education, but he dropped out to get married and ended up working at a job with no future. A recent divorce propelled Michael, a single parent of three, to return to get a degree. He says, "all of that math and science are really a burden on this older mind!" But he is expected to perform well because his children are A and B students and they expect he should be too. All of their encouragement must have an effect; he has maintained a 3.6 grade point average.

As part of his education to be an electronics technician, Michael participated in a co-operative education program at the Waterways Experiment Station of the Department of Defense's Corps of Engineers. The program allows a student to work one semester full-time and then study the next, alternating until its completion. Michael is currently working and will finish his last semester of school this fall. Upon graduation, Michael will have a permanent job with the Corps of Engineers.

Because Danielle, Bobby, and Jonathan are involved in the extended-day program through their school, Michael has more time to fulfill his educational responsibilities, while the children are involved in computer and music classes, drama, art, and gymnastics. "The kids can operate computers better than I can. It's number one on their Christmas list to get one of their own. They also like the Teenage Mutant Ninja Turtles. I think watching the show is their prerequisite for going to school every morning.

"We talk a lot about the importance of an education. They know those who aren't educated can't be competitive. They already have a good start."

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Senator PELL. Thank you. I find myself in pretty broad agreement with you, Dr. Martin.

Turning to Mr. Blair, when we have kids who don't repay their loans, who default, doesn't that have a bad psychological effect on them for the rest of their lives?

Mr. BLAIR. Very much so, sir. What we are trying to do is, we began a major initiative over 3½ years ago so that the students would know what they are getting into, that it is a loan, what their responsibilities are. We created a video that is given to the students to watch which declares a very simple message: You default, you die.

The idea is that they are very clear that it is a loan and those responsibilities will be with them, but, more importantly, we teach them of that responsibility, if they run into trouble, if they lose a job or they become sick, how to get the deferments that will allow them not to go into default. Our schools are also setting up extensive support systems so that the students, if they run into trouble or can't understand the complexities of the problem, will have technical assistance to help get it straight.

Senator PELL. I think that the proprietary, the taxpaying schools that I call them, serve a very real role in education. When you hear, as we heard earlier this morning, that 20 out of the 2,000-odd schools are responsible for 25 percent of the defaults, then you realize there is something wrong, and these institutions, I would think, should be kicked out of the program. What would be your view?

Mr. BLAIR. I agree. We have moved very aggressively to also work with the department. NATTS has put into place a whole series of processes that will strengthen the review as well as the more intensive screening process as schools come in to apply. We are also very much involved in our own tightening of the standards. In this last year, some 21 schools have lost their accreditation who have come up for renewal. It is a very extensive process that is controlled in large part by due process, but it represents a commitment on our part to make sure that those schools that do not meet the standards or become financially weak are removed from their eligibility.

We also supported the legislation which was in the budget reconciliation bill which stopped schools who were under negative action by one accrediting body to jump to another, so that we have been able to stop the accreditation jumping.

In addition, we have also put together a series of major proposals and remedies that are now in place on NATTS accreditation which will ensure the public's confidence can be there, that if it is a NATTS-accredited school it is a quality educational experience.

Senator PELL. I would like to ask each of you what you believe can be the benefit derived from this experience we are going through now—or what we can learn from it. That is a better way of phrasing it.

Mr. BLAIR. In my mind, the single most major impact that we have learned is that we have over the past several years made borrowing the way people pay for their education, and we have made poor people use borrowing; and we have not addressed the fact that as we have had more and more poor people have to borrow, we need to recognize there are additional costs in servicing them, there is additional costs in serving the short-term programs, and those must be addressed if we are to continue to have access for everyone in this country.

Senator PELL. Thank you.

Mr. Saunders.

Mr. SAUNDERS. Mr. Chairman, I would agree with that generally. I think the opportunity this whole issue has brought to our attention is the very real need to make substantial changes in the law in reauthorization. And I am encouraged, as I say, by what I have heard from the Secretary this morning about some of their plans for recommendations in the reauthorization process. It is encouraging to hear you and others in the Congress talk about the need for major changes. And over the last couple of reauthorizations, the starting assumption has been nothing much is going to be done, we are just holding the programs in place. I think we have an entirely new opportunity to really make some progress this time around.

Senator PELL. Thank you.

Dr. Martin.

Mr. MARTIN. Senator Pell, first of all, I agree with my colleagues. I think there are a couple of points that I would like to make.

One is I think the thing we have learned out of this is that it has been foolish and short-sighted to have the shift that we have seen in the last decade to expect very low-income disadvantaged students, many who are poorly prepared, to have to primarily finance postsecondary education, at least starting off, with high amounts of indebtedness. We should have been providing these students grants and work opportunities to give them a chance to be successful, and then give them loans to move on. That has worked, and it has proven it has worked before. So that is the first point.

The second thing I think we have learned out of this is that it is unfortunate that the program has gotten, I think, some of the bad press. I have been appalled by the stories that I have read across the country about comparing this to the S&L debacle.

Let me give you an example. First of all, the S&L debacle was caused in part because of deregulation. We have not had deregulation in this program. Quite the contrary.

Second, by the very structure of the S&L programs, these were entities with shareholders that shouldn't have been making bad loans that they did so. By the very nature of this program, we are supposed to take risks with people that don't have the means to give them opportunity. And I think we get apples and oranges here in terms of it all being mixed up. But they are not the same, Mr. Chairman. I think the fallacy of this is that we have used short-sighted programs because people thought it would be cost-effective to use loans to create opportunity. And if we are going to do that, then we are going to have some costs. And somewhere we are going to have to be willing to stand up and say that there is going to be more risk and the Government is going to have to pay for it.

I think it would be better to change the policies as you have proposed, to use programs like the Pell grant program to give those students the opportunity for that, and only use loans as a last resort and for people who maybe aren't as poor that have credit experiences, and then it is an appropriate vehicle.

Senator PELL. Wouldn't a simple approach to this be the idea that has been bandied about of having the first 2 years being grants and then the next 2 years being loans? In other words, the first 2 years, one would not be eligible for a loan.

Mr. MARTIN. I think, Mr. Chairman, that for a lot of students, and particularly low-income and disadvantaged students, that model would make a great deal of sense, and I think it would be supportive. I also think that there are students, however—and, obviously, there are differences in cost of education. I don't know that we could give a Pell grant of the magnitude to ensure that a student had the full choice of an institution that he or she would like to attend. And yet I don't want to deny them that. And if a student was willing to take out some loan for that choice, then I think that is appropriate. So we need to look at that carefully, but fundamentally I would concur with the direction that you are going and I think that you have always believed.

Senator PELL. Mr. Saunders.

Mr. SAUNDERS. Mr. Chairman, if I could express a reservation about that proposal, to have grants for the first 2 years, it seems to me one of the things we need to do is build into the system more incentives for retention and graduation. And it seems to me that that specific proposal goes just counter to that idea. It may discourage people or force people into shorter-term programs if the aid isn't going to be available in the junior and senior year.

So I think one of the things we need to do is look at ways to provide incentives and a bonus in student aid for retention in college and graduation.

Senator PELL. Mr. Blair, you mentioned actions being taken to reduce defaults, both by your accrediting agency and the trade associations. What would be some of those actions?

Mr. BLAIR. In addition to the elements that I have mentioned, we have held a whole series of workshops. We have developed a manual. We have developed training aids. We have held workshops across the United States in concert with the Guaranteed Student Loan agencies.

We have gone through now two rounds of training workshops, and we are about to commence our third. The third also provides additional materials for the students to understand their responsibilities and what they are to do. But, more importantly, we are finding that a lot of people simply have no experience with credit. So we are also putting together a series of videos that will help people understand what it means to have credit, what it means to make sure that they maintain a good credit rating. So it is all designed to support the student in knowing, if they have to have a loan, what their responsibilities are and how to correctly carry those out.

Senator PELL. Thank you very much.

I turn now to Senator Jeffords.

Senator JEFFORDS. Thank you, Mr. Chairman. You have covered many of the areas I was going to cover.

Mr. Blair, let me pursue a little bit further the 20 institutions that have the 25 percent. You mentioned that 21 had recently lost their accreditation. Were any of those 20 in that group?

Mr. BLAIR. I don't know which that 20 are that the Secretary had. We are going to secure that list and see what the match is.

The ones that were in reference to the very large money ones, to my knowledge, no. Those have already been identified in the past, and they have been either removed or substantially reduced in their borrowing efforts.

Senator JEFFORDS. In other words, most of the defaults are relatively old defaults when you look at that 25 percent?

Mr. BLAIR. Yes, sir. We went through a period of time when there was rapid growth in the student loan programs. One of the dilemmas that has always been there is the role distinction, and accreditation has always been firm in its belief that its focus has been on the quality of the educational experience, not upon the administration of student aid programs.

What we are pleased to see now is that Secretary Cavazos and the Department of Education is reinstituting the very critical oversight that was lax for a number of years, so that we are able to both target very quickly and together on schools where we see aberrant behavior, either in loan volume, student complaints, or concerns by the press or anyone else. So we have intensified our monitoring system so that those kinds of problems simply, we are convinced, will not take place again.

Senator JEFFORDS. I am also concerned from the other aspects. I know, of course, that proprietary schools try to service, in many cases, a group from the area of the economically disadvantaged, and I would be concerned that we do concentrate on the accreditation rather than necessarily just on defaults, with the expectation that we are going to have perhaps larger defaults in the groups that we are talking about. So I would hope we kind of separate those things out so that we don't create a problem which really is adverse to social interest.

Mr. BLAIR. Yes. We are working very closely with the department. We are very pleased, for example, with Secretary Cavazos' staging that he has so that you don't simply reach a cutoff point of default. We intensify what is required. We intensify the oversight.

We at the same time are looking to those schools that say that they wish to serve the high risk. We fully support that. However, when they accept that responsibility, they accept the responsibility of additional efforts. They are going to have to provide the counseling and training that that very vulnerable population has. We have entered into an agreement with the American Council on Education to make sure that the tests that are used for ability to benefit students are sound and viable tests, they are administered in effective and controlled fashions, and that people who fall below certain ranges are not admitted to the programs because the probability of their success is so low.

So we are trying to do what we can in working with the Department of Education and others to ensure that the high-risk population is served, but served well.

Senator JEFFORDS. My next question is to all three of you. I have to take primary responsibility for the reform of the SLS and the PLUS programs, and I know that the immediate response was dramatic, to say the least, which did give me some concern. However, I note that with reforms that went through in reconciliation, we have seen almost a 50 percent drop in the number of loans.

I would like your comments, as I look toward the future, first, whether what we did by making them more accessible and lower cost loans was good; and, second, did the reforms we made cause any negative problems or were the results mostly positive?

Mr. SAUNDERS. I think those were good reforms, Senator. I am not aware of any major negative reactions to it.

Senator JEFFORDS. Before you go on, is the 50 percent cutback bad, then, or unnecessary? Did we create problems with that cutback?

Mr. SAUNDERS. Well, Steve has already mentioned it has created problems in the proprietary sector. I am not aware of any serious problems in the collegiate sector.

Mr. BLAIR. In the proprietary sector, there were very adverse impacts of it. One of the things that has happened is with the very serious concerns that people do not engage in too great of borrowing. Caps were placed upon the Guaranteed Student Loan program. People generally think that all proprietary schools simply serve is the downtrodden masses of this country. That is simply not the case. We serve the full range of the economic spectrum.

Senator JEFFORDS. I certainly understand that.

Mr. BLAIR. The dilemma that we face is that there are a lot of people who are not eligible for Pell, that the cap on the GSL reduces what they had as access, and so what we faced were a large number of single heads of households who were looking to the SLS program to meet the additional costs, not only of the tuition and fees but also for the support they needed so desperately for child care.

So what has happened is we have seen the most devastating effect take place particularly in the high-risk areas, the urban areas; schools in the city of New York have closed simply because the cost of the education cannot be reached with the availability of the current student aid configuration. So it did do damage.

It also stopped some abuses, and so it did serve a good purpose. But the inability to make the distinctions between those truly deserving and needy and where there were abuses meant that a lot of good people were seriously harmed.

Mr. MARTIN. Mr. Jeffords, I might just add that I think generally from our membership, I would agree that we have had some schools that have relayed to us some of the very concerns that Steve has expressed. On the other hand, I think that we have had a lot of institutions that have basically applauded those changes. Unfortunately—I hate to say this—but I think there were a few people that were abusing the program, people that were clearly—I don't think we anticipated when we created the SLS as a backup that people would not work through the process, that you would first try to give a student a guaranteed student loan first of all. In some cases, we found that even though students would have qualified for a guaranteed student loan, the institution did not offer the guaranteed student loan first but went directly to the SLS because it was a little more money and you also could disburse it in a single disbursement.

Now, that was clearly not what was intended with that program. It was to be an additional backup. Those kind of events—not many—did occur. And I think I agree with Steve. I think that we have weeded out that kind of abuse because of the legislation that has been put in place. The unfortunate thing when we cast a broad net like that is that there were some well-deserving people that fall through the cracks, that don't qualify even for the GSL as we have made it more restrictive. They are just slightly over, or they can only qualify for a small amount. And the SLS really made the difference for them. Some of those people now are not getting it.

So as we move forward in reauthorization and so on, again, I think it gives us an opportunity now to see how do we do that but ensure a proper control so it won't be abused.

Senator JEFFORDS. I guess you know how interested I am in the program. I would like to work with you so that we can ensure that we don't deny people an education because of the nuances of the law or whatever, but that we also don't allow abuses which previously occurred.

Thank you, Mr. Chairman.

[Additional statements and material submitted for the record follow:]

Responses to questions submitted by the Committee from Mrs. Frohlicher

1. **Your testimony states that guaranty agencies have been cracking down on bad schools. Could you please elaborate?**

Section 428(b)(1)(T) authorizes guaranty agencies to limit, suspend, or terminate an eligible institution "pursuant to criteria issued under the student loan program which are substantially the same as regulations with respect to such eligibility issued under the Federal student loan insurance program...." Section 432(h)(3) of the Education Amendments of 1986 sought to prohibit "agency shopping" by institutions which had been subjected to L, S, & T procedures by an individual guaranty agency by requiring the Secretary of Education, within 60 days of receipt of notice from the guaranty agency of imposition of a limitation, suspension, or termination, to "disqualify" such institution from participation in the GSL Program as a whole unless he determines that the agency had not followed the law in imposing such penalty. The Department of Education has upheld agency terminations (in instances where the school has appealed an agency's action, rather than closing its doors), but has refused to enforce agency limitations and suspensions of school eligibility, due to its General Counsel's opinion that the statutory term "disqualify" would require the Secretary to terminate the institution's eligibility, a penalty more severe than that imposed by the guarantor. NCHELP disagrees with this interpretation of statutory intent, and will seek clarification in reauthorization, if necessary, to assure that the law is carried out.

Attached are reports from three guaranty agencies which have been especially diligent in undertaking actions against "bad institutions." As you can note, a number of these actions have involved limitations or suspensions (which have not been enforced by the Secretary) or have led to the closing of an institution, thereby not requiring Secretarial action. It should be stressed that current law requires an agency to find and prove program violations in order to L, S, or T an institution; high default rates, in and of themselves, are not grounds for termination, as the Department made clear to HEAF in 1987 when it sought to cease guarantee activity with a handful of extremely high-default institutions.

While *Continental Training Services, Inc. d/b/a/ Superior Training Services v. Lauro Cavazos, Secretary of Education, et. al.* called into question the Secretary's authority to take emergency action with regard to limitation, suspension, or termination of schools, the Congress in the Student Loan Reconciliation Amendments of 1989 made such authority statutory. Regulations implementing this authority were published in the *Federal Register* on August 7, 1990. As the enclosed charts make clear, guaranty agencies continued to utilize emergency actions even during the period that the "parent" Federal authority was unclear.

Section 682.411 of the Regulations governing the Guaranteed Student Loan Program, which became effective in December 1986 (implementing the Education Amendments of 1980) shifted major responsibility for program reviews of eligible institutions from the Department of Education to the guaranty agencies. The regulation requires that an agency conduct biennial reviews of its 10 largest schools (by annual loan volume) and of any school whose students received 2% or more of the loans guaranteed by that agency for the preceding year. These required reviews of large schools have limited many agencies' ability to devote staff time and attention to "problem schools." However, as program abuses have proliferated, especially with regard to the SLS program, many agencies, such as the ones whose reports are enclosed, have substantially increased the size of their review and enforcement staffs to deal with the problems. In addition, some

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States, such as California and Georgia, have by State law given guarantors increased authority over State licensure of trade schools, thus increasing guaranty agency ability to deal with the problems of "bad schools."

2. By your testimony, are you saying that other guaranty agencies are not facing serious financial difficulties?

I am saying unequivocally that no other guaranty agency is in financial difficulties of the magnitude of those experienced by the Higher Education Assistance Foundation.

All guaranty agencies may experience temporary cash flow problems, as lenders are entitled to file default claims 180 days after delinquency occurs (which the guaranty agency must pay within 90 days), while agencies are precluded by law from filing reinsurance claims with the Department of Education until the 270th day. (In the interim, the agency performs required due diligence, which may bring the defaulted loans into repayment, and obviate the need for a reinsurance claim.)

In addition, agencies may suffer higher-than-anticipated default claims, resulting in such claims' being paid at 90, or even 80, cents on the dollar. However, "tripping the trigger" should not be interpreted as a sign of financial difficulty. Rather, an agency's "trigger rate" is highly dependent upon the characteristics of the schools which are in its area of service. Research has shown that borrowers at four-year institutions are significantly less likely to default than borrowers attending proprietary institutions or two-year colleges. A State with a high percentage of community colleges and trade schools is, therefore, much more likely to receive reduced reinsurance for at least a portion of the fiscal year--and to plan for such expenditures--than is a New England State whose institutional mix is heavily tilted toward four-year and graduate-level institutions.

Finally, the spend-down legislation enacted as part of Budget Reconciliation in 1988 has served to reduce the amount of agency reserves, which are used to pay lender default claims. In enforcing the statute, the Department of Education withheld payments for reinsurance until the amount sought had been reached, even though the statute clearly vested in the agency the right of election on how to pay the money, and even though litigation over the constitutionality of the statute is still continuing in more than 20 States.

However, it cannot be stated strongly enough--HEAF's difficulties do NOT represent a problem in the Guaranteed Student Loan system in this country. Other guaranty agencies are strong and healthy and fulfilling their responsibilities to students in postsecondary education across the Nation.

3. How severe an impact has the guaranty agency spend down had upon your member agencies?

It is difficult to say, since the impact of spend-down fell unevenly across the guaranty agency community. Long-established agencies with prudent management and low default rates felt the burden most heavily, since they were the most likely to have accumulated substantial reserves. The Department of Education did grant full or partial waivers to several agencies, although it is difficult to understand the basis for their decisions on agencies' obligations since none of the appeals process was conducted on the record.

The fallacy of GAO's spend-down criteria, challenged by NCHELP in its response to the 1986 report, was that GAO assumed that no program rules would be changed and that future loan volume would be available to underwrite the costs of dealing with defaults and other expenses associated with loans already guaranteed by the agency. This approach is inconsistent with accepted accounting principles, which would dictate sufficient reserves to cover the existing portfolio, even if no new loans were made.

Of course, GAO's underlying assumption of no changes in the program to affect loan volume (and concomitant agency income) has not proven out. Recent GAO studies have documented the substantial decline in SLS volume which has resulted from Congressional action (fully supported by NCHELP) to deny SLS availability to borrowers in high-default schools. Although HEAF's spend down liability was not as high as that of other agencies, it did have its reserves reduced by that legislation, thereby aggravating the difficulties it encountered when the Department of Education required it to withdraw from 18 States in order to reduce the level of high risk loans in its loan portfolio.

Spend-down's effects have not been limited to its financial consequences. The line of current Circuit Court decisions (currently being appealed to the Supreme Court) holding that it is constitutional for the Federal government to revise its contractual relationships with guaranty agencies and to claim their assets has contributed to lender uneasiness about the fiscal stability of the program. Some lenders have even withdrawn from the GSL program, and credit markets which provide backing for State secondary markets are much more restrictive in their willingness to provide credit, as a result of spend-down.

4. **Have lenders begun to restrict lending to certain segments of the population?**

Some lenders have. One national lender announced several years ago that it would no longer make loans to students attending proprietary institutions. Other large lenders have modified their lending policies with regard to students attending high-default institutions. However, most lenders are still willing to make loans to all eligible borrowers under the statute. NCHELP knows of no instance today where loan availability is such that a significant Lender of Last Resort effort has had to be undertaken by a guaranty agency.

As noted above, credit providers and credit enhancers are also becoming more cautious about protecting bondholders of secondary markets from acquisition by the markets of a disproportionate proportion of high-risk loan paper. Increasingly, bond indentures contain limitations on the type or amount of such paper that may be purchased with the proceeds of a bond issue. Such limitations, if carried to extremes, could further limit lending, since many lenders do not choose to hold student loans but rather sell them after origination or before they enter repayment, to obtain capital to make new student loans.

5. **Will HEAF's problems cause lenders to further restrict their area of service?**

There is no question that HEAF's problems have raised questions in the lending community about their ability to be assured that claims will be paid in the event of a guarantor's financial difficulty. A lender's agreement is with the guaranty agency, after all, not with the Federal government.

However, Secretary Cavazos has been very clear in his statements that "all HEAF loans will remain guaranteed," and this assurance has done much to allay these concerns. NCHELP knows of no instances where lenders have announced more restrictive lending policies as a result of the current situation. However, lender attrition from the Program, attributable to the rising costs of servicing loans and the increasing cost of capital to make them, is a continuing concern.

6. **Is any preventive action being taken to avoid another situation of this magnitude?**

There is little possibility of another situation *of this magnitude*. HEAF is the largest guaranty agency in the country, in terms of total portfolio. A smaller guaranty agency's financial difficulty would not cause the GSL system such problems, as other guarantors would be able to absorb the portfolio without difficulty.

As I noted in my testimony, NCHELP is examining alternatives designed to prevent the recurrence of this problem, which will be part of the Council's proposals to the Subcommittee during reauthorization of the Higher Education Act in the next Congress.

7. **This crisis has raised many questions concerning the viability of the student loan program. Do you feel the program remains sound?**

Yes. This problem has arisen in August, traditionally the month in which the demand for student loan funds is highest. However, students across the country are apparently applying for, and receiving, Guaranteed Student Loans without difficulty. Certainly, given the extent of press coverage of the HEAF situation, any decline in GSL availability would have been thoroughly chronicled.

However, NCHELP is undertaking an analysis of all of the elements of the GSL Program, with a special emphasis on guaranty agency solvency, so that the Council can make appropriate recommendations for strengthening the viability of the program, if any are needed, during Reauthorization.

8. **In last year's budget reconciliation, we eliminated SLS Loans for first-year students at schools with default rates in excess of 30%. The General Accounting Office is issuing a report today showing that this action has dramatically reduced loan volume. Do you agree that this action will help loan defaults?**

Yes. GAO's study confirms reports NCHELP has received from guaranty agencies about the substantial drop in SLS volume in high-default schools.

In California alone, SLS loan volume at high-default community colleges, private 2-year, and proprietary schools declined by $83.89 million (64%) for the first six months of 1990, when compared with the first six months of 1989. In addition, GSL borrowing for these schools declined by $49.87 million (25%), probably attributable for the most part to the SLS limitation.

Based on a 17-month lag between guarantee and claim in SLS loans, the SLS default claim savings for fiscal year 1991, for California alone, will be $22.45 million for these high-default schools. In fiscal year 1992, California estimates that its SLS claims for Federal reinsurance will decline by $60.4 million, while concomitant GSL claims will be reduced by $26.9 million, for a total savings to the Federal government--*in California claims alone*--of $87.3 million.

If California's experience during the first six months of 1990 is typical of the nation's loan program as a whole, then the FY 1991 default claim savings could reach $179 million and the FY 1992 savings could be as high as $885 million.

9. **What are the lessons to be learned from the HEAF crisis?**

I am not sure that anyone can know the answer to this question until the crisis has been resolved. Some of the lessons we knew intuitively--that maintenance of lender confidence in the fiscal strength of the program is essential for its continued effective functioning, as withdrawal of lender participation would spell the program's demise; that some populations are more prone to default than others, and the costs of making, administering and collecting their loans, and paying for their defaults, is much higher than similar costs involving lower-risk populations; that the GSL program, which began 25 years ago as a middle-income cash-flow program has been transformed over the years into an open-access program which has become the primary vehicle for financing the postsecondary education of the most needy; that the almost-annual process of budget reconciliation has reduced the funding available to lenders, guaranty agencies, borrowers, and schools, as their responsibilities have been increased by Federal regulation and statute; that much more attention needs to be paid to the front end of the process--how institutions are admitted into the program--than has been paid in the past.

There may be other lessons that become clearer as the process moves forward. Reauthorization of the Higher Education Act in the next Congress will provide an excellent forum for making whatever statutory changes may become necessary.

10. **During the 1980s, we had a dramatic shift from grants to loans. Our student aid programs have also failed to keep pace with the cost of a college education. Could you please comment on how this policy change is affecting student loan defaults?**

The fact that grant and other campus-based aid funds did not keep pace with college costs during the past decade, resulting is a substantially-increased reliance on loans for postsecondary education financing has undoubtedly had a substantial effect on the cost, if not the rate, of student loan defaults. The Administration has repeatedly publicized Federal expenditures for default costs, giving the impression that borrowers were not repaying their loans in ever-greater percentages. Actually, the *rate* of Guaranteed Student Loan defaults has not increased significantly over the last ten years. Costs have increased, reflecting the jump in annual GSL lending from $2.984 billion in FY 1979 to $12.434 billion in FY 1989--an almost direct result of the failure of other aid programs to keep pace. As conceived, the Pell Grant was to be the foundation of student financial aid, with other campus-based programs serving to augment a student's aid package, and with GSL as the "last resort" program for high-cost institutions. Instead, today the GSL Program is the second-largest source of aid for college, ranking behind parental contribution, and to many students it is the <u>only</u> source of aid.

It is imperative that the grant-loan imbalance be rectified next year in Reauthorization, so that all aid programs can function as Congress intended.

11. **What do you see as the primary causes of student loan defaults?**

Studies have consistently shown that the primary reason that borrowers do not repay their Guaranteed Student Loans is that they do not have the money to do so.

Changes made by the Congress over the past several years have virtually eliminated the stereotypical "doctor with a Corvette" who is thumbing his nose at collection efforts. All defaults are now reported to credit bureaus, thereby thwarting defaulters' efforts to obtain other credit for home mortgages, cars, or credit cards. Most States participate in the Federal IRS Offset program, which applies any tax refund due the borrower to his outstanding loan indebtedness. In addition, many States have enacted similar State tax offset programs. Guaranty agencies have been extremely creative in developing other relationships to assist them in collecting loans--agreements with trade and professional licensure agencies which will not issue the necessary license to a defaulter; cross-checks with Motor Vehicles Departments and other State agencies for current borrower addresses to pursue collection activities; authority to confiscate lottery winnings to satisfy defaulted GSL debt.

Other factors also contribute to defaults. If a borrower does not receive a quality education, he often feels under no obligation to repay, although the debt is owed to a lender which has no control over the educational program provided by the school. Tightened eligibility criteria for educational institutions and active monitoring and termination of "bad schools" by guarantors and the Department of Education should reduce the incidence of default caused by inadequate instructional programs. Similarly, if a school closes while the borrower is enrolled, he often defaults on the amount of his loan for which he is still liable, since he did not receive the educational credential necessary for obtaining the job which would enable him to repay. NCHELP will be making recommendations to the Subcommittee concerning treatment of "closed schools" as part of the Reauthorization process.

1989-90
L, S, & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F Notification Date	 Effective Date	Status/Comments
LAB Radio, Television, Inc., dba Los Angeles Broadcasters 1717 North Highlan Avenue, 2nd Floor Los Angeles, CA 90028	Initial Compliance audit conducted 1/2-4/90	Certified students' eligibility for attendance in ineligible program, improper ATB assessment, failed to make required refunds.	At least $296,000 in unpaid refunds	Case on verge of review by General Counsel for filing, when CELP Official learned of school's closing and Bankruptcy, and loss of accreditation.	Case on verge of review by General Counsel for filing, when CELP Official learned of school's closing and Bankruptcy, and loss of accreditation.		School's owner filed Chapter 7, Bankruptcy 12/4/89. Accreditation (NATTS) withdrawn 2/90.
The Word Processing & Computer School 350 West Cerritos Avenue Anaheim, CA 92805	Initial Compliance audit conducted 4/6-8/88 School non-responsive to report issued 6/2/88	Non-response to outstanding issues, per Compliance letter of 10/6/89 regarding required student-consumer information, refund to provide students and unpaid refunds, AGI/EFC issues and factors of financial responsibility.	$3,702 in unpaid refunds plus $4,000 in school federal subsidies.	In process of serving documents to Suspend to be followed by Termination if continuing non-response when information received (1/31/90) school being sold.	In process of serving documents to Suspend to be followed by Termination if continuing non-response when information received (1/31/90) school being sold.		School placed in "S" status because of change in ownership resulting in change in control on 1/31/90. Sale finalized effective 2/7/90 and, three weeks later, new owner closed the school. Closure confirmed 3/21/90 and audit closed 4/9/90.
Delena's Colleges of Beauty 895 Fulton Mall Fresno, CA 93721	Compliance reviews conducted 10/25-28/83, 9/3-4/86, 2/17-19/88, and 6/20-22/89	Failure to make refunds, impaired factors of financial responsibility and administrative capability, certification of ineligible loans, improper ATB assessment, excessive charges to students, inadequate use of need analysis, certifying loans in excess of annual aggregate limits, and failure to provide required student-consumer information.	At least $30,844 plus repayment of associated federal subsidies.	Will not be used in this case.	5/11/90	(T) 5/31/90	Failed to respond to Notice of Intent to Terminate. ID inactivated on the system effective 6/1/90. On 6/8/90 received letter dated 5/30/90 from lawyer stating Chapter 11, Bankruptcy was filed. This precluded the college from termination. Letter was sent 6/27/90 withdrawing termination. School is again eligible.
Travel and Trade Career Institute 3635 Atlantic Avenue Long Beach, CA 90807, and 12451 Brookhurst Boulevard Garden Grove, CA 92640	Compliance reviews conducted 10/31-11/2/89, and 1/16-18/90	Maintaining "two sets of student records." Failed to establish financial need, ability to benefit, certified loans for students with prior defaults. Failed to determine correct dependency status, granted improper leaves of absence, and failed to make proper and timely refunds.	At least $70,895 plus repayment of associated school subsidies.	Will not be used.	6/29/90	7/20/90	Consent Agreement executed 7/20/90 to be in place one year and requiring payment of unpaid refund liability of $100,000 and provide quarterly reports of withdrawals and refunds, plus other fiscal and administrative requirements.
CA Institute of Dental Technology 4365 Atlantic Avenue Long Beach, CA 90807							Now exclusively a fraud investigation. Arrest warrant issued for school's owner.

1989-90
L, S, & T ACTIONS

Report Issue Date 8/3/90

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F: Notification Date	Notice of Intent to L, S, T or F: Effective Date	Status/Comments
United Education & Software, Inc., dba National Technical School 4000 S. Figueroa Street, and Martin Luther King Blvd. Los Angeles, CA 90037	OIG Audits conducted 4/88 - 3/89 for the period 8/87 - 9/88	Certified loan applications for ineligible program and students; failure to make proper/timely refunds; used unfair refund policy; misrepresented financial charges, improperly administered ATB testing; ineffective academic progress policies used and evidenced severely impaired administrative capability.	$21.9 million ineligible loans $1.7 million unpaid refunds	Effective 10/16/89	10/13/89	(T) 11/2/89	School to placed in "suspense" on 10/16/89. Posted $250,000 bond. School's code restored to "active" status on 10/24/89. Hearing on "Preliminary Injunction" 11/9/89. UES filed for Chapter 11 Bankruptcy on 12/4/89. UES says it must sell or close 12 of its 28 schools.
American Video Repair Institute, Inc., dba American Video Repair Institute 601 South Brand Boulevard San Fernando, CA 91340	Compliance initial review 5/2-3/89	Ineligible loans; failed to meet standards of administrative capability and factors of financial responsibility.	$69,580 in ineligible loans $20,831 in unpaid refunds from audit sample	Effective 7/14/89	7/12/89	(T) 8/1/89	School failed to request hearing or indicate in writing the reason not to terminate. Termination effective 8/1/89. National disqualification sought from USDE on 8/2/89.
City Business Colleges, Inc., dba Metropolitan Technical Institute 2300 Pacific Avenue Long Beach, CA 90806	Compliance reviews conducted 8/27-29/85 and 11/7-9/89	Ineligible loans, ineligible programs, improper administration of ATB assessment, failure to obtain financial aid transcripts, improper retention of loan proceeds, failure to make refunds properly.	$70,281 in ineligible loans $4,282 unpaid refunds - both from audit sample	Effective 3/23/90	3/23/90	(T) 4/12/90	Consent Agreement finalized 7/9/90; school to pay unpaid refund liability of $74,543.32 and withdraw from participation in Part B, HEA, loan programs.
Beta Technical Schools, Inc., dba Beta Technical Schools 6606 Paramount Boulevard Long Beach, CA 90805	Received final audit report(s) from Compliance. CA Attorney General conducted investigation 12/89 - 3/90 and filed civil complaint 3/21/90.	Ineligible loans, ineligible programs, enrolled students in ineligible school, used unqualified instructors, substantial misrepresentation of the nature of its educational program and of its financial charges.	CA Attorney General prays for $1 million civil penalty from each of 53 defendants and restitution for each student enrolled in ineligible programs.	Will not be used.	7/10/90	(T) 7/31/90	Termination documents served 7/10/90, effective 7/31/90 unless, by 7/27/90, hearing is requested.
Golden State Institute, Inc., dba Reseton College 18330 Sherman Way Reseda, CA 91335, and 3200 Wilshire Boulevard Los Angeles, CA 90010	Awaiting final audit report from Compliance, initial audit conducted 1/2-4/90	Improper certification of SLS loans, substantial misrepresentation of school's financial charges, failure to correctly determine students' dependency status, failure to obtain financial aid transcripts, improperly granted leaves of absence.	To be quantified by Compliance and verified by the CELP Official	Filed after school's 30-day response period has elapsed.	Filed after school's 30-day response period has elapsed.		1st draft, based on draft audit report completed - may be modified if final report differs significantly from draft report. School closed on 5/3/90.

1990-91
L, S, & T ACTIONS

Report Issue Date 8/3/90 - (latest revisions italicized)

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F: Notification Date	Notice of Intent to L, S, T or F: Effective Date	Status/Comments
San Diego College of Medical & Dental Careers 5952 El Cajon Boulevard San Diego, CA 92115	*Compliance Review conducted 1/30-31 and 2/1/90*	*Failure to assess ATB, no documentation of eligibility of non-citizens, failure to perform required verification, improper retention of students loan proceeds, failure to make timely and proper refunds, and failure to provide required consumer information.*	At least $43,781 plus excess federal subsidies.	Emergency Action not imposed.	8/1/90	*6/21/90*	Intent is to terminate participation and impose $50,000 in civil penalties based on specific violations.
Universidad Autonoma de Guadalajara 10999 IH-10 West Suite 355 San Antonio, Texas 78230	Compliance Review conducted 5/2-4/89	n/a	n/a	n/a	n/a		*To General Counsel for review on 7/19/90.*
United College of Business, 3 campuses: Downey, Pico Rivera, and Hollywood	Compliance Review conducted 3/6-8/90	n/a	n/a	n/a	n/a		Received from Compliance week of 7/16/90; this school is next in queue. Information about Emergency Action and L, S, T or F not yet available.
University of Sound Arts 1645 North Vine Street Hollywood, CA 90028	Compliance Review conducted 6/5-7/90	Enrolling students into an ineligible program, failure to assess ability to benefit, failure to document eligibility of non-citizens, severely impaired standard of administrative capability, substantial misrepresentation to prospective students, and impaired factors of financial responsibility.	At least $88,813 plus repayment of associated federal subsidies and other liabilities discovered in the course of implementing corrective action.	n/a	n/a		Currently preparing case from draft audit report. Information about Emergency Action and L, S, T, or F not yet available.
Cases known to be forthcoming to the CELP Official, but not yet received from Compliance: . Wilshire computer Colleges							

1988-89
L. S. & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F — Notification Date	Notice of Intent to L, S, T or F — Effective Date	Status/Comments
Dental Technology College for the Handicapped, Inc., dba National Technical College 1201 Victory Blvd. N. Hollywood, CA 91606 600 S. Spring Street Los Angeles, CA 90014	Initial review conducted 6/26-27/88	n/a	Restitution for 3100 students X $2650 = $8,215,000 or $8.2 Million	Effective 6/24/89	(T) 6/24/89	8/13/89	Action commenced based upon information (dispositions and declarations) developed by CA Attorney General resulting in filing of 6/14/89 "Complaint for Injunction, Civil Penalties and Other Equitable Relief." Case No. C727570. Requested administrative hearing being scheduled for May/June 1990.
First Independent Trust Co.	Compliance audits conducted 1/88 and 2/27 - 3/24/89	Failure, through quarter ended, 6/30/88, to remit origination fees owed USDE. Failure to: evidence billing and payment at fair market value for computers and software placed in schools as inducement to obtain students loans; make timely refunds to borrowers' accounts; make any origination fee adjustments; timely manifest loan transaction thereby insurance premiums due the Commission to remain in guaranteed but non-disbursed status.	Major issues - failure through quarter ended 6/30/88, to remit some $4.6 million in origination fees owed USDE. Failure to: make timely refunds ($1.35 million and $684 thousand from 9/88) to borrowers' accounts; make any .5% (10/87-12/87) origination fee adjustments covering some 12,000 loans worth $25.5 million and representing some $680,000 in insurance premiums due the Commission to remain in guaranteed but non-disbursed status.	Emergency Action not taken	(T) 4/21/89	5/12/89	As of 5/12/89 awaiting finalization of hearing dates. Institution "seized" by Superintendent of State Banking Department on 5/19/89 - Liquidation of the company to be forthcoming, all assets frozen.

1988-89
L, S, & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F — Notification Date	Notice of Intent to L, S, T or F — Effective Date	Status/Comments
ABC Colleges, Inc., dba ABC Colleges, 2213 Kern Street, Fresno, CA 93721	Compliance review conducted 10/24-26/88	Failure to: establish Ability to Benefit; incomplete applications and incomplete when certified; improper need analysis procedures; maintain proper loan check transaction records; inadequate SSCR processing; and inadequate provision of consumer information.	$81,630 potential; since need analysis not used since inception (10/17/86) through 12/88. $582,000 & interest & special allowance in both cases.	Effective 2/24/89	(T) 2/24/89	3/17/89	Entered into Consent Agreement 4/3/89 - 3/31/90. 1) $10,000 civil penalty payable by 5/5/89, in lieu of termination; 2) respond to remaining issues in audit report by 6/5/89; 3) conduct (and pay if liability found) refund portfolio analysis by 6/5/89; 4) develop default reduction and retention and placement enhancement plan and report on progress on 9/30/89 and 2/28/90; 5) good faith effort to resolve student complaints in 30 days and enter documentation on same in students' files; and 6) put internal processing controls to preclude CSAC commencing action to terminate due to violation of Consent Agreement. Authorized [illegible] to again obtain CSLP guarantees effected [illegible] of 4/7/89.
American Microcomp Systems, Inc. AMS College 11015-A Bloomfield Avenue Santa Fe Springs, CA 90670	Compliance last review 8/83	Found via discussion with HEAF, had certified loans for 27 CA GSLs for attendance at Computer Training School (an ineligible school) using AMS ID#.	Ineligible loans total $58,800	Effective 7/21/88.	(T) 7/21/88	8/10/88	ID # inactivated 7/21/88. Consent Agreement executed 9/1/88, see AMS L,S & T file for its terms/conditions.

1987-88
L, S, & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F: Notification Date	Notice of Intent to L, S, T or F: Effective Date	Status/Comments
Fashion Careers International, dba Plaza Three Academy 973 Market Street San Francisco, CA 94103	Compliance review conducted 12/28-29/87.	Failure to: make proper Pell grant eligibility determinations; maintain complete, accurate GSL applications; improper certification of independent student status (2 orphans); establish correct student budgets; make proper refunds when due; inadequate provision of consumer information; and process SSCR of 9/87.	Not quantified until refund calculation listing prepared and remitted to CSAC, per direction of Compliance-Audits Supervisor.	Effective 5/13/88	(T) 6/10/88	6/30/88	Emergency Action based on refund problems and failure to respond to request for specific refund portfolio calculation and listing. Owner failed to: respond to demand for payment of $180,789 in unpaid refunds made on 3/31/88 as evidenced by the "Enrollment and Refund Analysis" dated 5/19/88; request a hearing or a prehearing conference; and provide written materials to show termination should not take place. Owner notified of termination by letter on 7/1/88. On same day USDE requested to consider "national disqualification." USDE followed up by letter on 7/28/88.
M & C Beauty Colleges, Inc., dba Continental BC, Sacramento	Compliance review conducted 7/87	Failure to make refunds, retention of unearned student funds, potentially ineligible loans.	$20,000 unpaid refunds/credit balances $13,000 ineligible loans	n/a	n/a		Consent Agreement negotiated 8/13/87; school in compliance with agreement as of 12/24/87. Lost NACCAS accreditation at 2/88 NACCAS meeting. CSAC inactivated ID # for further guarantees on 3/28/88.
Dolores's Colleges of Beauty all located in Fresno, CA 3241 North Cedar Street 4060 E. Kings Canyon Road 3125 West Shaw Avenue 805 Fulton Mall	Compliance reviews conducted 10/83, 9/86, and 2/88.	Failure to make timely and proper refunds, provision of inaccurate monthly withdrawal and refund information, and failure to implement program of exit counseling for students.	$16,000 in refund checks returned to CELP lender (1/88 and 3/88) because of non-sufficient funds. Subsequently, "covered" via cashier's check(s).	Effective 3/15/88	(T) 4/13/88	5/2/88	Consent Agreement executed 4/26/88, to continue through 6/30/89.
Mesa, Inc., dba Cabrillo School of Nursing	Compliance review conducted 5/86	Failure to: make refunds; maintain proper, current, complete student academic and financial records.	$330,000 in unpaid refunds	n/a	(T) not available in the file	9/11/87	Consent Agreement executed 12/5/86; violated 4/27/87 by failure to provide responses to unresolved issues. Schools closed 10/19/87 and lost accreditation and eligibility to participate in Title IV programs. Filed 11 USC Chapter 7 Bankruptcy on 12/1/87. First meeting of creditors scheduled for 12/30/87. CSAC inactivated ID# for further guarantees effective 10/19/87.

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1987-88
L, S, & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F: Notification Date	Notice of Intent to L, S, T or F: Effective Date	Status/Comments
M & C Beauty Colleges, Inc., dba Broadway BC, LA Continental BC, Van Nuys Continental BC, Pico Rivera Continental BC, Hawthorne Continental BC, Rancho Cordova	Compliance review conducted 8/87	Failure to make refunds, retention of unearned student funds, potentially ineligible loans.	$180,000 unpaid refunds/credit balances $41,000 ineligible loans	Effective 9/24/87	(T) 10/7/87	10/27/87	Attempting to negotiate Consent Agreement at $25,000 per month 1/88 - 8/88. Lost NACCAS accreditation at 2/88 NACCAS meeting. CSAC withdrew EA and Notice of Intent to Terminate without prejudice on 3/30/88. Schools inactivated by USDE via "B-washline" during 1st week of 8/88; CSAC inactivated schools ID's for further guarantees on 3/30/88.
University of Cosmetology	Compliance reviews conducted 8/19-20/86 and 2/24-26/87	Failure to make refunds.	$33,000	Effective 8/27/87	n/a		Reached Consent Agreement 9/10/87; see letter dated 9/22/87 acknowledging payment of refunds totaling + $25,000. Emergency Action lifted and school remains in compliance with Consent Agreement.
Cal West College	Compliance reviews conducted 8/86 and 1/87	Failure to: make refunds; timely return checks to lenders; establish ability to benefit; obtain selective service registration status; improper granting of leaves of absences; make available required consumer information; and improper recruitment and check endorsement practices.	$46,000 by sampling; but since records are a "shambles", could be several hundred thousand dollars. $786,180 GSL cumulatively at time of termination.	Effective 7/30/87	(T) not available in the file	8/19/87	Notice of Intent to Submit Written Materials to CSAC dated 8/13/87, received 8/1/87. CSAC reviewed written materials and responded 8/14/87; not found mitigating. School terminated 8/19/87. CSAC inactivated ID# for further guarantees, same date. USDE Notice of Review of CSAC's termination sent to school 11/25/87; USDE Notice of Disqualification from GSL, SLS, and PLUS to (Cal West) 2/8/88, signed by Secretary Wm. Bennett and effective on the date of letter.
Future Technical Institute, Inc., dba Future Technical Institute	Compliance review conducted 7/7-10/87	Violations range from failure to establish ability to benefit to failure to use need analysis methodology through failure to document citizenship status.	$15,000 in unpaid refunds, BUT records so flawed, if ineligible loans not "cured", whole portfolio of $800- 680,000 could be at risk.	Effective 7/28/87	(T) not available in the file	9/8/87	No hearing requested or written materials presented. Schools closed by owner - terminated 9/8/87 by inactivating ID# for further CSAC guarantees.

1986-87
L, S, & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F: Notification Date	Notice of Intent to L, S, T or F: Effective Date	Status/Comments
North County College	Compliance review conducted 1/87	Placed on one-year monitoring due to concerns over attrition/default rates, timeliness of refunds, administration of CBSLP, student complaints, and conduct of fiduciary responsibility.	not quantified	Effective 6/29/87	n/a		On 3/24/87, IRS seizes school's assets. CSAC administratively suspends processing new GSL's on 3/25/87. On 5/13/87, AICS accreditation expires and school does not renew and has no plans to do so. On 6/11/87, CSAC notifies school that since loss of accreditation, school no longer eligible to participate in Title IV programs. (i.e., ED# inactivated for further guarantees)

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1985-86
L, S, & T ACTIONS

Corporate/School Name & Address	Basis for Action	Types of Violations	Potential Liability	Notice of Emergency Action	Notice of Intent to L, S, T or F: Notification Date	Notice of Intent to L, S, T or F: Effective Date	Status/Comments
Super Shapes College of Cosmetology	Compliance reviews conducted 10/83 and 3/86	Failure to: make refunds; assess ability to benefit; accurately record and retain check transaction dates; use of commissioned salespersons to promote GSL's; accurately and timely process SSCR's; and maintain proper complete, current student academic and financial records.	$200,000	Effective 6/28/86	(T) not available in the file	7/17/86	USDE withdrew school's eligibility to participate in GSLP, therefore, CSAC withdrew termination action without prejudice, and cancelled the administrative hearing on 9/25/86, and inactivated ID# for further guarantees.
Sierra College of Business	Compliance review conducted 6/19-22/86 HEAF review conducted 3/26-28/86, our action, in part, based on findings of HEAF.	Failure to: make refunds; establish ability to benefit; maintain records; accurately report AGI; maintain records on check transaction dates; document continued half-time enrollment; and verify satisfactory academic progress.	$100-150,000 by sample, but inaccuracy of records suggests liability could be greater.	Effective 6/16/86	(T) not available in the file	7/7/86	School lost AICS accreditation effective 7/14/86, therefore, lost eligibility to participate in the Title IV programs. On 8/17/86 CSAC withdrew termination action (without prejudice) on the basis of lost accreditation. ID# inactivated for further guarantees.
Dinary, Inc., dba Academy of Stenographic Arts	Compliance review conducted 7/85	Failure to: make refunds; establish ability to benefit; accurately certify applications; accurately report AGI; document satisfactory academic progress; and maintain proper current, complete student academic and financial records.	$170,000 in unpaid refunds	Effective 1/29/86	(T) not available in the file	2/19/86	Parties (CSAC, via Attorney General, and Dinary, Inc.) have failed as of 12/22/87, to negotiate an acceptable Consent Agreement. Emergency Action remains in place. ID# inactivated for further guarantees by CSAC. No new CSGLP loans being made since 1/29/86; think school has obtained new loan guarantees from HEAF since that date.

MEMO

TO: Ms. Laurie Quarles, Staff Associate, NCHELP
Mr. Robert Fomer, Director, CSLP
Ms. Carmen Piekenbrock, Manager of CTI, CSLP

FROM: Marschall S. Smith, Lead Program Officer, CSLP

DATE: 1 August 1990

RE: CSLP Program Reviews

The Colorado Student Loan Program (CSLP) performed approximately 25 reviews in the time frame of 07-01-89 to 06-30-90. This number reflects official program reviews and does not take into account technical assistance, trainings and "unofficial" reviews. CSLP's Compliance, Training, and Investigations Department (CTI) employs five (5) program officers; one lead, two school specialists, two lender specialists; to do the program reviews and an investigator. The CTI Department has, as its responsibility, performing a program review at each lender and school approved by CSLP at least every three years. Institutions with high default rates and in CSLP's top ten are reviewed every two years. This type of review schedule can only be accomplished by a guarantee agency with a focused area of responsibility, like CSLP.

CSLP has taken restrictive action (Limitation, Suspension, or Termination) against three (3) institutions in the past year and a half. Two (2) of the actions were taken as a result of CSLP's program reviews. The most recent action involved a school with campuses in Colorado, New Mexico and Arizona, and involved over 300 students. I have attached a copy of the liability assessment letter sent to the president of the corporation with regard to only one of the campuses involved. The actions were a result of the schools' failure to make refunds, admitting ability to benefit students improperly and problems with other areas of administrative capability--issues that could best be discovered by a program audit or review.

Criminal action has or is being taken against the officials of these three schools. A school official has already plead guilty to criminal activity, another case will go to a grand jury next week, and the others are still under investigation. CSLP's investigator also works on fraud and abuse by students and financial aid personnel, both on the state and federal levels. Many cases have been successfully tried, and the guilty parties have paid fines or served time in prison.

Of the schools where restrictive action has been taken, the statistics look like this:

Total Loans Guaranteed:	school #1 = 395 school #2 = 1,378 school #3 = 8,397 (comb)
Total Dollar Amount Guaranteed:	school #1 = $1,001,221 school #2 = $3,687,780 school #3 = $25,198,203 (comb)
Cohort Default Rates:	school #1 = not listed school #2 = 39.9% (FY 88) school #3 = 34.6% (FY 88 av)

The amounts listed here are cumulative amounts of loans guaranteed by CSLP and include Stafford, SLS and PLUS. School #3 includes 11 campuses.

STATE OF COLORADO

Department of Higher Education
COLORADO STUDENT LOAN PROGRAM

Denver Place
999 18th Street, Suite 425
Denver, CO 80202-2440
Phone (303) 294-5050
FAX (303) 294-5076

Roy Romer
Governor
Dr. David A. Longanecker
Executive Director
Robert Fomer
Director

July 5, 1990

Dear

The administration of your policies and procedures for the Guaranteed Student Loan Program at , was reviewed The findings of that review were disclosed to you in a report dated . Because of the seriousness of those findings, file reviews were required in a number of areas. You were instructed to answer the report and submit documentation of your findings to the Colorado Student Loan Program by

Due to the failure by your institution to adequately respond to the report, the following liabilities have been assessed in the areas indicated:

VIOLATION	% OF LOANS	LIABILITY ASSESSED
Missing Ability-to-Benefit Tests	94%	$ 3,512,689.76
Missing Financial Aid Transcripts	34%	$ 1,270,547.36
Incomplete Verification	27%	$ 1,008,964.08
Unresolved Discrepancies (Verification)	27%	$ 1,008,964.08
Funds Released to Students Not Maintaining Satisfactory Progress	20%	$ 747,380.08

July 5, 1990
Page Two

The percentage of loans is based on the number of files reviewed with the violation, compared with the total number of files reviewed. The percentage was then extrapolated to the number of loans guaranteed since September 1, 1988, excluding cancelled loans. Many of the loans have more than one violation; therefore, the institution need only satisfy the liability assessed as a result of the Missing Ability-to-Benefit Tests violation to be considered in compliance with this demand. If the institution decides, however, to perform the required file reviews rather than paying the assessed liabilities, the institution must perform all of the file reviews as indicated in the original program review report.

If you have any questions, please contact me by calling (303)294-5050 extension 310. Immediate payment of the liabilities is expected and must be received by CSLP no later than August 10, 1990.

Sincerely,

Patti Swisher

Patti Swisher
Program Officer

cc: Kristie Hanson, CSLP
Carmen Piekenbrock, CSLP
Harry Shriver, USDE

TGSLC

Texas Guaranteed Student Loan Corporation
P.O. Box 15996 • Austin, Texas 78761-5996 • 512-835-1900 • 800-252-9743

July 31, 1990

Summary of TGSLC's Program Compliance Activities: FY87-90
(As Requested for Jean Frolicher)

	FY87	FY88	FY89	FY90 (10/01/89-06/30/90)	Total
Limitations	0	0	3	4	7
Emergency Suspensions	0	0	7	4	11
Suspensions	0	0	1	0	1
Terminations	0	0	2	2	4
Administrative Hearings:					
Emergency Suspension	0	0	0	1	1
Termination	0	0	2	2	4
Program Reviews	0	22	39	31	92
Default Reduction Agreements:					
Executed	0	0	10	15	25
Pending	0	0	0	8	8

Fiscal year dates: October 1 - September 30

UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF LEGISLATION AND CONGRESSIONAL AFFAIRS

September 5, 1990

Senator Claiborne Pell
Chairman
Subcommittee on Education, Arts and Humanities
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Enclosed are Secretary Cavazos' responses to HEAF-related questions you submitted in follow-up to his August 3 appearance before the Subcommittee on Education, Arts and Humanities.

I hope you find them satisfactory, and I appreciate your support as the Department attempts to reach a solution to the HEAF situation.

Sincerely,

Nancy Mohr Kennedy
Assistant Secretary

Attachment

RESPONSES BY SECRETARY CAVAZOS

TO QUESTIONS SUBMITTED BY SENATOR PELL

1. Will the transfer of HEAF's loans cause financial difficulties for whoever assumes their responsibilities? How will this be avoided?

A. We have retained the services of a financial management firm to analyze the various options which are being considered. That firm is also analyzing the financial impact that the assumption of the HEAF portfolio would have on the various entities being considered. Our own staff are also analyzing the financial and operational burdens. We are determined to select the option that will ensure that the HEAF portfolio is properly serviced, and causes no disruption to the loan guarantees. In addition, we want to ensure that HEAF's problems are not simply transferred to another entity or entities, and that we do not face another HEAF-type collapse. To this end, we are analyzing the financial and operational impact on a successor entity or entities.

2. Will the problems confronting HEAF affect the ability of students to obtain loans for the upcoming school year?

A. No. Problems confronting HEAF should have no effect on the ability of students to obtain loans. Currently, United Student Aid Funds is, and other State guarantee agencies are, able to guarantee loans in the five HEAF-designated States and the District of Columbia if they have agreements with lenders in those States. Furthermore, all options to address the HEAF problem that we are contemplating will ensure that students continue to have access to the GSL programs.

3. Over the past two years, the Department has put into effect regulations to reduce defaults, many of which are based upon my Senate-passed default bill. Can you give us any early indication of how these regulations are working?

A. It is still too early to estimate with any certainty the impact of the Department's default reduction regulations, which were finalized in June 1989, as part of the Department's Default Reduction Initiative -- a package of regulatory, administrative and legislative measures designed to address the default problem.

Although schools are currently undertaking steps to address the default problem in accordance with the Initiative, changes in institutional default calculations and significant program savings will not be reflected for a number of years. This is because borrowers in school at the time of the implementation of the Initiative will not be reflected in default statistics until the calculation of the FY 91 cohort default rates, which will be collected and published early in 1993. However, we believe the delayed delivery of loan proceeds to first-time borrowers and the use of a pro rata refund policy are having a positive impact on reducing defaults attributable to early dropouts.

Some of the regulatory measures in the Default Reduction Initiative include:

- o requiring participating schools to provide initial counseling with first-time GSL borrowers to ensure that they have a clear understanding of their rights and obligations under the program and where they may turn if they encounter problems in repaying their loans;

- o requiring schools offering certain types of vocational programs to provide detailed consumer disclosures to prospective students on the completion, job placement, and state licensing pass rates of former students in those programs; this information will be gathered and used to evaluate programs and schools, and be published as consumer information to help students make informed choices; and,

- o requiring participating schools at certain levels of default to implement comprehensive default management programs on their campuses, delay loan delivery to first-time borrowers at their schools, and implement a pro rata refund policy for student borrowers who drop out or withdraw early in their programs.

Also, as part of the Initiative, guarantee agencies have been required to conduct program reviews of schools with default rates that exceed 40 percent so that we may closely monitor schools that we believe are having problems. Finally, lenders have been required to enlist the assistance of schools in tracking former students and encouraging them to repay by providing schools with a notice of the borrower's delinquency.

Schools participating in Title IV programs were required to implement these actions shortly after the regulations were published in 1989. The strongest measures in the regulations, which allows for Limit, Suspend and Termination (L,S & T) actions against schools with over a 40 percent default rate, will take effect in FY 1991.

4. What are the lessons to be learned from the HEAF situation and what needs to be done to prevent further crises like this in the Stafford Student Loan Program?

A. We are continuing to review the HEAF situation to determine what lessons can be learned and to develop proposals designed to avoid further crises of this type. Upon our initial review, the HEAF situation appears to indicate a need for closer management of guarantee agencies; the collection and analysis of audited and unaudited financial statements for all guarantee agencies; and more stringent accreditation process monitoring and eligibility reviews to determine the eligibility of schools and their students. One thing is certain--we need to pursue additional steps to reduce the default rate. The Department is considering legislative, regulatory, and administrative proposals to this end, many of which will be included in the Department's Higher Education Act reauthorization proposals to be submitted in February, 1991. We are also considering proposals to strengthen Federal oversight of guarantee agencies and postsecondary institutions.

5. Can you tell us if there are other entities in the Student Loan Program facing problems similar to HEAF's? (And if so, who are they?)

A. As we indicated previously, there are a few guarantee agencies experiencing what we now believe are short term cash flow problems. We have engaged the services of a financial management firm to assist ED staff in reviewing the financial aspects of the guarantee agencies. These reviews will be completed within 60 days.

The Department is reviewing the financial solvency of all guarantee agencies. Indicators such as reserve ratio, default rate, and mix of loans by postsecondary sector will help us identify guarantee agencies for in-depth review. In addition, we are reviewing audited financial statements of all guarantee agencies. Site visits are being conducted at 15 guarantee agencies to be completed by September 28, 1990.

6. How much will it cost the American taxpayer to solve this problem?

A. Given the various options we are pursuing, the final cost to the American taxpayer is unknown at this point. Various options to address the situation are under consideration and each has its own cost. It would be premature at this point to indicate which cost level presents the best overall solution. We will inform the Subcommittee as soon as we know what the cost will be.

7. I have been told that in court cases regarding the guarantee agency spend down reserves, the Administration has contended that guarantee agencies need not worry about their reserve level because their assets are backed by the Federal Government? Is this correct?

A. No. The Department's response to the court challenges to the recovery of guarantee agency excess cash reserves required by Section 422(e) of the HEA has not included an argument that agencies need not worry about the level of their reserves. Instead, the Department has argued that the reserve funds are dedicated to the GSL program.

8. What, if any action, did the Department take with HEAF to stem their financial difficulties and prevent the problem from escalating?

A. HEAF proposed to stop guaranteeing loans for certain schools; stop guaranteeing loans for certain lenders; and require co-signers on student loans for students at some schools. These proposals violated either section 428(c)(2)(F) or section 428(b)(1)(T) or (U) of the Higher Education Act of 1965. In discussions with us, HEAF also suggested that it withdraw its guarantee from entire states as a way to adjust the proportion of proprietary school loans in its portfolio. The Department approved the request in the expectation that adjustments to HEAF's loan mix would improve its financial situation. HEAF announced its withdrawal from 18 states in April 1988.

9. Is any consideration being given to providing a mechanism for HEAF to continue their operations?

A. No. Continuation of HEAF as a guarantee agency is not one of the options under consideration.

10. Is any preventive action being taken to avoid another situation of this magnitude?

A. Yes, with the assistance of a financial management firm, we are reviewing the financial strength of all guarantee agencies and are considering strategies for addressing guarantor solvency issues.

We are also engaged in preventive activities. Although it will take several years for default rates to reflect the full effect of the Department's Default Reduction Initiative, we are confident that we can significantly reduce the incidence of default, thus helping to avoid HEAF-like problems in the future. Restrictions on access to SLS loans enacted in the 1989 Omnibus Reconciliation Act will also reduce defaults. In addition, we will continue to seek enactment of default-related provisions of the Department's "Student Default Reduction Amendments" and other legislative proposals. These proposals include the following:

- authorize guarantee agencies to garnish defaulter's wages. This proposal would authorize guarantee agencies to garnish a defaulter's wages, up to 10% of disposable pay, after the defaulter is provided a notice and an opportunity for a hearing;

- require lenders to offer graduated repayment schedules to student loan borrowers, thus easing the terms of repayment in the early years, and reducing the risk of default;

- delay loan disbursement to all first-time borrowers for 30 days from the student's first day of classes. This would help reduce the inordinately high rate of defaults by students who withdraw within the first few weeks of class; and,

- tighten "ability to benefit" criteria by requiring students without a high school diploma or GED to pass a test given by an independent third party.

11. One of the most difficult problems in tackling the default problem is obtaining accurate default data. Could you please comment on what progress, if any, the Department is making in this regard?

A. The Department receives its default data via computer tapes, known informally as "tape dumps," provided by the guarantee agencies. From these tapes, we also obtain default data needed to administer the Secretary's Default Reduction Initiative. Over the past several years, we have been working closely with the guarantee agencies to improve our data bases, and to ensure the most accurate data possible. We believe that the information that we are currently receiving reflects a very high level of accuracy. The accuracy of this data is demonstrated by the fact that, even though a large number of schools request "back-up data" from the Department to support the default rates we publish, very few schools (74 for the 1987 cohort, 13 for the 1988 cohort) appeal their default rates once this data is received. Of these appeals, only 12 schools in the 1987 cohort had their default rates reduced, and in the 1988 cohort, seven schools have had their rates reduced and four appeals are still pending.

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Congress of the United States
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Washington, DC 20515

HOUSE COMMITTEE ON
INTERIOR AND INSULAR AFFAIRS

CHAIRMAN
SUBCOMMITTEE ON NATIONAL PARKS
AND PUBLIC LANDS

HOUSE COMMITTEE ON
BANKING, FINANCE AND
URBAN AFFAIRS

HOUSE SELECT COMMITTEE
ON AGING

August 8, 1990

Honorable Claiborne Pell
Chairman
Subcommittee on Education, Arts,
and Humanities
648 Dirkson Senate Office Bldg.
Washington, D.C. 20510

Dear Chairman Pell:

I was extremely pleased to see your quick response to the current crisis facing the Higher Education Assistance Foundation (HEAF).

It is vitally important that this issue be addressed responsibly and without undue hesitation. As I am sure you are aware, some lending institutions have already begun to slow down the processing of new loans for students pending action of the Department of Education. One of Minnesota's major lenders, Twin City Federal -- which accounts for almost a third of the loans in the Minneapolis/ St. Paul area -- has declared that it will stop both its current and pending disbursements until a resolution is reached. This is of great concern to me, since other lending institutions might be tempted to follow this example. This is a serious consequence for students and educational institutions during the busiest season for the origination of new loans. Hopefully, the attention given this matter by your Subcommittee will move the Department of Education towards a timely resolution.

I would also like to express my appreciation for being permitted to submit the enclosed statement for the record of last Friday's hearing. The future of HEAF is of great concern to the people of my district and state and I am pleased to have been able to share some of their concerns with you.

Thank you for your timely attention to this matter. If I can be of any assistance, please feel free to contact me.

Warm regards.

Sincerely,

Bruce Vento

Bruce F. Vento
Member of Congress

BFV:evc

STATEMENT OF REPRESENTATIVE BRUCE F. VENTO

BEFORE THE

SENATE SUBCOMMITTEE ON EDUCATION, ARTS, AND HUMANITIES

August 3, 1990

Mr. Chairman, I would like to thank you and the other Members of the Subcommittee for calling this hearing in such a timely fashion. Clearly, the crisis now facing the Higher Education Assistance Foundation (HEAF) must be addressed in a prompt manner.

I would also like to express my appreciation for being allowed to share a few thoughts with you on this matter. I am deeply concerned about the current negotiations which will determine the future of HEAF and its employees.

As the Representative of St. Paul, Minnesota, where the bulk of HEAF's operations are located, and one of the states in which HEAF serves as the designated guarantee agency, I would like to share a few important issues which should be part of your consideration and your debate on the future of HEAF.

While it is clear that HEAF's financial difficulties are of such magnitude that a transfer of its portfolio to another guarantor is inevitable, I think it is significant that these difficulties are not attributable to HEAF's workforce. These workers are highly trained and very productive. While the quality of the actual paper that was guaranteed may be questioned, this was beyond the control of the workforce. It was their job to process the paper, which they did with great efficiency.

In fact, it is my understanding that the Department of Education's own team of evaluators, in conjunction with the Office of Management and Budget, found this to be the case. Although there has been no official report of which I am aware, individuals within the Department have stated publicly that even before their visit to St. Paul they had no expectation of finding any fraudulent behavior or mishandling of the portfolio by this highly capable workforce.

With over 800 employees, and contract obligations that involve as many as 800 additional workers in supportive services, HEAF is a vital contributor to St. Paul's economy. Thus, I am very concerned and hold out hope that the Department of Education will consider the impact of any decision upon these workers and our St. Paul community. While I do not intend in any way to impede the prompt resolution of this matter, it is clear that the track record of efficiency compiled by HEAF's workforce in St. Paul, its familiarity with the current loans and the regions in which it operates, and the resources available to it in its present location suggest that these workers could make a significant contribution towards regaining payment to the maximum extent possible and maintaining the future health of the existing portfolio entrusted to their care.

I have significant concerns about the effect any resolution of this matter will have upon the students in Minnesota and across this nation. Some of the distinguished panelists that you will hear today will undoubtedly express similar concerns in more depth.

For several years now Minnesota has had the lowest default rate on guaranteed student loans of any state. HEAF has always recognized this and, consequently, did not assess Minnesota's students the maximum allowed guarantee fee of 3%. This has been beneficial and appropriate in recognition of the lower risk earned by Minnesota loans. However, I am concerned that a new guarantor taking over for HEAF may well disregard this positive Minnesota performance and increase these charges. This would add an additional cost and unfairly tax the students of Minnesota. I hope that the Department of Education would carefully review this potential change and ensure that procedures are in place to avoid or limit such action.

The students in Minnesota have complied faithfully with the requirements of the insurance fund from the beginning. They have always paid a slightly higher premium than their risk level warranted, helping to lower the costs to other students around the country who may have provided a greater risk, but without the lower fee may not have had the opportunity to attain a post-secondary education. This is a national benefit for other students, especially for those in lower income or higher risk states. Yet after all these years of having demonstrated consistently low default rates, Minnesota's students could be forced to pay significantly more because of the overall defalut rates experienced by the guarantor.

While there may be no doubt that HEAF shares liability for the current problem. the principle which governed their loan guarantee actions were commendable. This principle was that access to loan markets should be equal for all students who were eligible under federal policy guidelines established in law. Many regions throughout the country, such as Washington D.C., would very likely have gone underserved without HEAF. Our guiding values as a nation embrace a philosophy of opportunity and that a higher education should be within the grasp of all who can perform without regard to income. Unless Congress and the Administration intend to discard such basic values, I suggest that regardless of who assumes the HEAF portfolio, assurances should require that accessibility to the guaranteed student loan market be maintained to the maximum extent feasible. Certainly this must include additional safegaurds and oversight, but not an abandonment of certain areas or the academically qualified students in those environments.

I believe that these concerns can be addressed within the broader context of addressing the current problem without presenting a significant departure from the overall objective of the student loan programs.

Again, I appreciate your prompt attention to this crisis and the opportunity to share my concerns with you.

STATEMENT OF
DR. SAMUEL M. KIPP III
EXECUTIVE DIRECTOR, CALIFORNIA STUDENT AID COMMISSION
TO THE
SUBCOMMITTEE ON EDUCATION, ARTS, AND HUMANITIES
UNITED STATES SENATE
AUGUST 3, 1990

Mr. Chairman and Members of the Committee:

Thank you for this opportunity to comment on the important issues resulting from recent developments concerning participation of the Higher Education Assistance Foundation (HEAF) in the federal Guaranteed Student Loan program. It is a matter of public record that HEAF, the single largest guarantor in the program with some $9.6 billion in student loans, faces grave financial problems.

It is certain that HEAF will continue to have great difficulty paying the staggering flow of default claims on loans it guaranteed--estimated to be some $3 million per day. With a vocational school default rate reported to be approaching 70 percent, HEAF's troubles are compounded because it is being reinsured at less than 100 cents on the dollar for most of its estimated $900 million claim volume for this year.

The potential insolvency of HEAF has given rise to several critical questions which strike at the heart of the federal educational loan program. No answers are provided in the statutes or regulations that explain what is to be done in the event a guarantee agency fails. Yet the choices that are made now will have a profound impact on the very shape and long-term health of the loan program.

HEAF's present situation magnifies some of the fundamental structural contradictions inherent in the loan program which attempts to maintain low program costs while also providing unlimited borrower access, but which insists on maintaining an unacceptably weak set of school eligibility standards. If, within this framework, a guarantor actively guarantees a disproportionate amount of loans from borrowers who are attending the highest-risk schools in the segment with the highest overall default rate--the worst of the very bad; such "reverse skimming" produces disastrous financial and educational results which can be, and in HEAF's case were, predicted. As the largest state guarantee agency in the nation with more than $7 billion in total loan guarantees, the California Student Aid Commission is vitally concerned with the manner in which this matter is resolved. The course selected will have a profound effect on the educational loan program and, more importantly, upon millions of students and their families who depend on the program to make access to higher education and a better life a reality.

Present Guarantee Agency Structure Sound

The California Student Aid Commission and others in the educational loan program have long maintained, with a good deal of supporting evidence, that the present guarantee agency structure is a sound, cost-effective way to deliver student loans.

However, this is only true when the guarantor invests the resources necessary to properly administer the program by providing workshops and training for lenders and schools; protecting the integrity of the program by carrying out regular and thorough compliance reviews and audits (then taking the necessary administrative steps, including limitation, suspension, or termination when warranted); and by providing borrowers with default prevention and debt management information.

Background: HEAF's Rapid Loan Volume Expansion

It is important to examine how HEAF arrived at its current circumstances. If a guarantor allows the indiscriminate generation of new loan volume to take precedent over prudent administration, the bill will eventually come due for payment. That is exactly the case with HEAF. Its dramatic mid-1980's expansion throughout the country reached far beyond those states where HEAF was the designated guarantor to other regions and to schools that were often afraid of the more diligent oversight and compliance review activities of the state designated guarantee agency. This was certainly true for most of the business HEAF did in California.

When, during the past two years, HEAF attempted to correct the imbalance in its portfolio by retreating from 18 states and by implementing an insurance fee structure designed to discourage vocational school borrowing, the resulting drop in loan volume and accompanying reduction in ACA payments, together with the contingent liabilities HEAF had guaranteed already, combined and compressed to produce the current crisis situation.

Little responsibility for HEAF's present circumstances should be attributed to the 1988 United Education and Software/California Student Loan Finance Corporation loan-servicing problem. If anything, HEAF's liability was reduced substantially when many of its worst loans in that portfolio lost their guarantee and never materialized as claims.

Suggested Solutions

While this is a strong argument in support of student loan guarantors maintaining a balanced portfolio and an active compliance program, it does not resolve the issue at hand. It has been suggested by the Department of Education that such a resolution will in no way either adversely affect students' access to loans, increase taxpayer liability, affect the soundness of the HEAF guarantee or compromise the ability of the lenders to be fully paid. Achieving all these simultaneously would require some sort of alchemy; a magic formula not possible within the confines of the loan program's current regulations and statutes.

Making the lenders with HEAF-guaranteed loans whole raises a number of important questions:

- How can this be accomplished at no cost to the taxpayer?
- What are the implications for other guarantors which may be receiving reimbursement less than 100 cents on the dollar?
- If the issue of lender liability has been eliminated, why move the portfolio to another/other guarantors?

There are reports that the Student Loan Marketing Association (Sallie Mae) has made a bid to become a guarantor in exchange for taking over the troubled HEAF portfolio. The Student Aid Commission believes that this step is both illegal and unnecessary. Current circumstances, while serious, do not meet the legal test for such an action as set forth in the Higher Education Act. The California Student Aid Commission and other state guarantee agencies have provided, and will continue to provide, sound guarantees to lenders in the student loan program.

Furthermore, as a new guarantor, Sallie Mae would be entitled to 100 percent reimbursement for five years no matter how high its default claim level. The potential cost to taxpayers would be very high. The California Student Aid Commission opposes allowing Sallie Mae to become a guarantee agency. The present partnership between lenders, guarantee agencies, and the federal government must be preserved and strengthened so that the nation's students are assured of continued access to essential funds for higher education.

Allowing Sallie Mae to become a guarantor would have grave implications for the educational loan program. As a guarantee agency, Sallie Mae would combine all of the functions of separate program participants in a single organization--guarantor, lender, and servicer--and would have to determine the acceptability of its own claims for defaulted loans. Without the current checks and balances, the potential for conflict of interest would be immense. This concern has already been expressed by the GAO and the Inspector General.

Equally concerning is the suggestion that all or a large portion of the HEAF portfolio might be taken over by United Student Aid Funds, thereby creating a new giant. As in the case of Sallie Mae, there are a whole variety of terms and conditions being proposed as part of any such arrangement that would also involve substantial cost to the taxpayer. Further concentration in the loan program is likely in the future, but is no excuse for creating a monopoly.

Any short-term solution to HEAF's problems must be consistent with the loan program's long-term goals. Resolution plans must consider the policy, legal and operational implications for all program participants--students, lenders, guarantors--and the taxpayers.

Among the questions which should be addressed when examining each potential solution are the following:

- Would the present environment--in which students, lenders and guarantors are held accountable for responsible compliance with loan program regulations and policies--be altered?
- Will there be significant alteration of the present loan program environment which draws a distinction between guarantors, lenders and secondary markets?
- What is the legal mechanism for transferring guarantees between guarantee agencies?
- What oversight role does the Department have in the instance of such a transfer?
- Will the viability of other guarantors be maintained?
- Operationally, is it practical or desirable to move the HEAF portfolio to another/other location(s)?

Budget Reconciliation Producing Results

Resolving the current HEAF situation should not divert attention from the fact that the dramatic and bold steps taken by Congress in the last Budget Reconciliation Act are, by addressing the issues of institutional quality and eligibility, producing the kind of long-term results that will help restore balance to the Guaranteed Loan Program. By eliminating SLS loan eligibility for students to attend schools with default rates of 30 percent or more, the new SLS loan volume at the very high-risk California institutions has gone from over $131.4 million dollars in the first six months of 1989 down to $47.5 million dollars in the first six months of 1990, a decline of nearly 64 percent.

In the same period for those same institutions, the Stafford loan volume has dropped over 25 percent from $195.3 million down to $145.5 million. Using projection techniques based on the average length of time between guarantee, or in this case nonguarantee, to default for different types of institutions and the different loan programs, the first impact of this declining loan volume will occur in the last four months of federal fiscal year 1991. (Overall default claim levels are likely to rise until then.)

The likely impact for California alone in fiscal year 1991 will be a decline of more than $22 million dollars in the level of default claims that otherwise would have been paid. In fiscal year 1992, tha impact for California for a full 12 months of the decline in SLS borrowing plus the accompanying decline in Stafford borrowing, will be an estimated total default claim savings of more than $87 million.

Potential Savings of $885 Million in Fiscal Year 1992

If California's experience in the first six months of 1990 is in fact typical of the nation's--a rough extrapolation because patterns vary widely among states--a savings in the range of $179 million dollars can be expected in federal fiscal year 1991 and savings of $885 million in federal fiscal year 1992. This does not count savings in interest and special allowance payments that will accrue as a consequence of the lower loan volume at high-risk schools and does not count potential Pell Grant savings of awards that were, in many respects, wasted at some of those institutions that will either be scaling back or departing the program.

An $885 million dollar savings represents over 20 percent of the total federal expenditure for the loan programs. It would, if redirected and utilized, make available a substantial amount of additional resources that could be and should be put into other areas like the Pell Grant program to bring about some rebalancing of federal aid. The California Student Aid Commission believes that, to the extent that this kind of savings can in fact be realized, it could help restore public confidence in the integrity of the student loan program while making much-needed monies available to students attending institutions that can deliver the education or training they promise. It will also help to restore balance among the sources of aid.

The implications of Budget Reconciliation are clear: institutional eligibility is the key to a healthy educational loan program. By allowing only quality schools to be eligible for the program, students are provided consumer protection and lenders, guarantors and taxpayers are protected financially. There is no evidence that the provisions of the Budget Reconciliation Act limit access to quality education.

As always, the California Student Aid Commission will continue to work toward making the loan program a realistic means by which students and their families can fulfill their educational dreams. Please do not hesitate to call upon me or my staff if we can be of assistance. Thank you.

TGSLC

Texas Guaranteed Student Loan Corporation

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August 14, 1990

The Honorable Claiborne Pell
Chairman, Senate Subcommittee on
Education, Arts and Humanities
United States Senate
Washington, DC 20510-3901

Dear Senator Pell:

Enclosed is written testimony concerning the recent hearings conducted by your committee with regard to the recent financial difficulties of the Higher Education Assistance Foundation. I appreciate the opportunity to submit written testimony to discuss some of the more vital issues surrounding this matter.

I'm hopeful upon the committee's return from the current recess that this matter will be given appropriate attention during the remaining portion of this session of Congress.

If there are any questions concerning the points raised in my testimony, I will be glad to respond.

Sincerely yours,

Joe L. McCormick

Joe L. McCormick
President

JLM/alg

Enclosure

cc: Members, Senate Subcommittee on Education, Arts and Humanities
Senator Lloyd Bentsen
Senator Phil Gramm

PREPARED STATEMENT OF JOE L. McCORMICK, PRESIDENT, TEXAS GUARANTEED STUDENT LOAN CORPORATION (TGSLC)

INTRODUCTION

The current uproar over the financial situation at the Higher Education Assistance Foundation (HEAF) presents the Higher Education community with the much needed opportunity to evaluate the operation of the Stafford student loan program among all players -- schools, lenders, guarantors, servicers, secondary markets and the Department of Education.

The easiest explanation is to infer that the HEAF situation is due to poor financial management based on an over aggressive marketing ploy. However, as I hope to show in my testimony, the HEAF situation, while magnified, is not a problem peculiar to one agency and is not a temporary problem, but rather a problem within the GSL program itself.

The problems facing HEAF are symptomatic of a systemic crisis. A 'quick fix' solution will only be treating symptoms. The underlying causes of HEAF's financial problems, and the impact these same causes will have on other sectors of the financial aid industry, can only be addressed by fundamental changes in the financing structure of the program.

In 1965, when President Lyndon B. Johnson signed the Higher Education Act into existence, it was clear that he intended the mission of this act was to provide access to all American students to assist them in pursuing the educational goals of their choice.

"To thousands of young men and women, this Act means the path of knowledge is open to all that have the determination to walk it."

This equal access philosophy remains today and must be preserved if we are to honor the promise unveiled in 1965. But, philosophy must be backed up by policy --- and reality. And access must become access to quality education, not just access to debt.

CHANGES TO THE GSLP IN THE '80'S

The Stafford Loan Program that operates today is a far different animal than the program that began the decade of the 80's. A major change during the past decade has been the student loan portfolio shift from the traditional middle income family to an overwhelming majority of "high risk" borrowers from low income families. Other significant changes have been:

- the availability of grants to pay college costs has not kept pace with increasing costs and students now rely heavily upon loans. In 1977-78, the average student had close to 40% of their financial aid package composed of grants and 50% of loans. Ten years later, the average student's financial aid package consisted of 71% of loans and 25% of grants.

- a dramatic increase in the number of participating proprietary schools since 1985 and their proportion of GSL and SLS loans. In Texas alone the number of proprietary schools increased from 167 schools in 1986 to almost 400 in 1990.

- rapidly rising attendance at non-traditional proprietary schools, particularly enrollments in less than 600 clock hour courses such as bartending, security guard and nurse aid training.

- the introduction in 1986 and rapid volume growth of the Supplemental Loans for Students (SLS) loan program. In 1986 TGSLC did $15,966,604 in SLS/PLUS volume. That number had increased to $219,260,760 in 1989.

- responsibility for program compliance was shifted to individual states and guarantors. As a result, the Department of Education dramatically reduced their number of program reviews. In 1980, the Department conducted over 2,000 reviews; in 1988 only about 300 reviews were done.

- certification of schools by the Department of Education occurred at a "rubber-stamp" level with only 63 schools denied out of 2,087 applying for certification during a three year period.

GUARANTOR FINANCING AND STUDENT LOAN RISK

While the philosophy of the Guaranteed Student Loan Program promotes access for all students to all types of education, program administration penalizes guarantors who provide access to "high-risk" borrowers.

Guarantee agencies are financed through a combination of revenue sources including the guarantee fee charged to each loan, administrative cost allowance paid for administration by the federal government, a certain percentage of collections of defaulted loans, and, most importantly, the reinsurance of 80% to 100% on defaulted claims.

Given the federal law limiting to 3% the guarantee fee that can be charged to borrowers combined with the reinsurance regulations which impose a possible 20% loss on that same loan, it's not difficult to conceive a scenario where a high defaulting loan portfolio can financially break a guarantor. The revenue to the guarantor is not always compatible with the risks involved.

GUARANTEE FEE CAP

Student loan guarantors are the only insurance business forbidden to charge a fee that is commensurate with the risk involved in making the loan. Federal guidelines have capped the guarantee fee at 3%, regardless of the inherent risk of each loan.

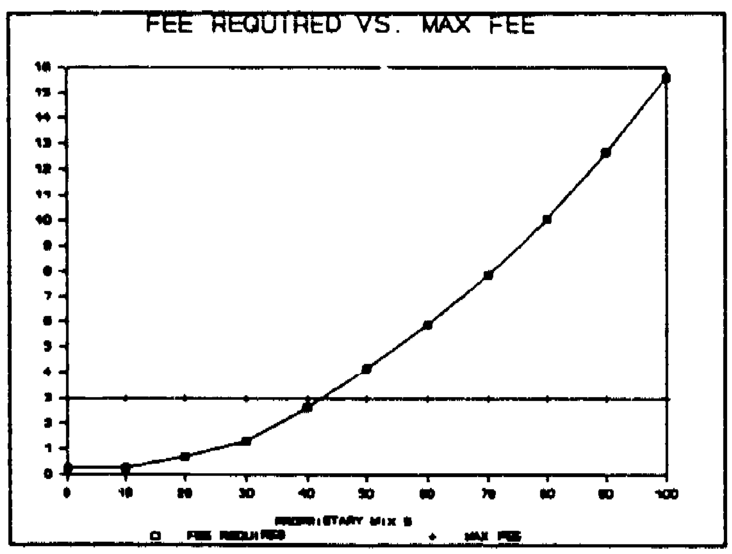

Figure 1

A 3% fee is sufficient when the guarantor has a favorable portfolio mix of low default loans. However, as Figure 1 shows, the 3% maximum can quickly become inadequate given a guarantors limited ability to control their portfolio mix. In essence, any guarantor whose portfolio mix exceeds 41% proprietary school loans over an extended period of time, is simply not collecting sufficient guarantee fee income to cover the high defaults.

REINSURANCE METHODOLOGY

The existing reinsurance method works as a penalty against guarantors with high default rates. Originally devised as an incentive for proper program administration, the formula today serves only to increase the risk of guarantors that are providing the loan access the program mandates. Active community awareness, compliance, preclaims assistance and collection programs are not enough to avoid "hitting the trigger" when the portfolio has an unusually high percentage of high-risk loans.

This trigger mechanism in reinsurance payments should probably be modified in some way to compensate guarantee agencies who serve a high percentage of low income, high risk students.

This clash between the open access philosophy and a guarantor's potential risk is a fundamental flaw in the GSL program.

CAPITAL REQUIREMENTS

Minimum capital requirements that incorporate the long term risk of student loans would allow a more financially stable program. An actuarially sound financing structure, stricter eligibility criteria for schools, active compliance functions and portfolio management tools are needed for guarantors to maintain minimum capital requirements and protect the integrity of the GSLP.

The federal government contributed to the weakening of reserves by following guidelines from the August 1986 General Accounting Office report: GSL's -- Guidelines for Reducing Guarantee Agency Reserves. The report recommended that Congress establish maximum reserve levels for guarantee agencies and return excess reserves to the U.S. Treasury.

As a result, Congress enacted the spend-down provisions in the Budget Reconciliation Act that reduced agency reserves by $250 million. This action was based solely on historical portfolio data and did nothing to take into account the current financial condition of guarantee agencies nor their potential future risk -- a most serious flaw in the decision to require agencies to "spend down" reserves.

In addition, COBRA directed the Secretary to seize $75 million and $30 million in federal advances for 1988 and 1989. These arbitrary actions dealt severe blows to the adequacy of required reserve levels at the same time that federal policies were not responding to situations that were straining those levels through increased claim payments.

THE HEAF EXPERIENCE

Knee-jerk responses to the HEAF financial situation that take all the blame, wrap it in a pretty package with a shiny red ribbon and hand it back to HEAF are irresponsible. This hypocrisy of the program that champions equal access for all students at all schools, yet severely penalizes guarantors who fulfill their equal access mandate must be exposed.

The HEAF financial crisis is the fulfillment of a hypothesis that most of the higher education establishment has ignored. Unlimited access to loans + limited program oversight + inadequate revenue related to risk = an unworkable formula.

Proposed options for solving the HEAF problem have so far ignored the most practical, reasonable and less costly proposal -- keeping HEAF intact and leaving the portfolio where it is. A merger, as proposed by HEAF, and as clearly allowable by law, is the most realistic proposal. The failure of the Department of Education to approve that option has caused much of the panic and alarm we are now experiencing from lenders.

Converting the HEAF portfolio to United Student Aid Funds (USAF) would not save the government money, and would alternately buoy up, and then burden, another national guarantor.

Creating a new national guarantor under the control of the Student Loan Marketing Association (Sallie Mae) would empower Sallie Mae to the detriment of the independent guarantors and the students they serve. This proposal also clearly contradicts recent Department of Education policy that emphasized the separation of student loan responsibilities within agencies.

THE TEXAS EXPERIENCE

The financial difficulties of HEAF have generated concern among the financial community as to the financial viability of other guarantee agencies and as to whether or not the federal government will stand behind the 100% guarantee on HEAF loans. HEAF described its financial difficulties as due primarily to the large percentage of trade school loans in its portfolio, approximately 65% at the end of FY89. While states such as California, New York, Florida and Texas had experienced significant increases in trade school loans during 1988 and 1989, several steps have been taken both at the federal and state levels to control the level of trade school participation in the GSLP to acceptable levels.

While the concern for the financial viability of a guarantor such as TGSLC is understandable, it is important not to draw conclusions from the unfortunate experience of a national guarantor. There are vital and important differences in the manner TGSLC has conducted its affairs over its ten years of existence as compared to HEAF:

1. TGSLC is a state guarantee agency and has never attempted to serve as a national guarantor, as such, TGSLC has always been in a better position to manage its portfolio, its policies & procedures, and its ability to control defaults.

2. TGSLC has always charged the most appropriate guarantee fee allowable in relation to its portfolio in order to always have sufficient guarantee reserves to pay claims. Other guarantee agencies, including HEAF, have at times yielded to market pressures and charged a lower fee insufficient to cover future loan losses.

3. TGSLC's Guarantee Reserve levels have always been maintained at levels well above the level required by contract and/or the level required to cover future loan losses. As of June 30, 1990 TGSLC had over $43.5 million in the Guarantee

Reserve representing 2.46% of outstanding loans. See Figures 2, 3, 4 and 5.

4. TGSLC was one, if not the first, guarantee agency to point out some of the fraud and abuse among trade schools participating in the GSLP. TGSLC has taken the lead in implementing "Default Reduction Agreements", credit checks for SLS borrowers, and an aggressive program of program compliance reviews of both lenders and schools. Since TGSLC began in 1988 to actively review schools and lenders, 92 program reviews have been conducted, 7 limitations have been imposed, 11 emergency suspensions invoked, and 4 terminations have been enforced.

5. TGSLC has aggressively pursued legislation and regulations at both the federal and state level to protect the integrity of the GSLP and to prevent further fraud and abuse. Several improvements have been made in recent months to restore public confidence in the GSLP in Texas:

   a) The Texas Legislature passed default reduction measures in the 1989 session to require state agencies to work with TGSLC to control defaults and prevent fraud & abuse.

   b) Congress enacted more restrictions on school participation in the SLS program.

   c) The Department of Education has recently implemented its default reduction regulations.

As a result of these combined efforts, the first ten months of 1990 reflect an impressive reduction in SLS borrowing and overall trade school loan volume. Total loan volume is down approximately 20% as of July 31, 1990 over the same period a year ago ($390,412,000 now as compared to $503,645,000 a year ago). See Figure 6.

SLS volume for the first ten months of this year is at $67,933,000 as compared to $143,748,000 a year ago. This represents a 53% reduction in SLS volume. Trade school volume is at $148,383,000 so far this year as compared to $262,068,000 a year ago. This is a 43% reduction in trade school volume. See Figure 7.

TGSLC's current portfolio mix has shifted to less high-risk trade school volume as a result of our successful efforts to control defaults and protect the integrity of the GSLP as the following percentages indicate:

	FY89	FY90(TD)	JULY 90
FOUR-YEAR	50.0%	55.0%	75.0%
TWO-YEAR	8.0%	7.0%	3.0%
TRADE SCHOOL	42.0%	38.0%	22.0%

TGSLC has always aggressively pursued the collection of defaulted student loans. Texas has, since 1981, sought court judgments against defaulted borrowers when all other collection attempts fail.

As seen in Figure 8, our total dollars collected from defaulted borrowers continue to rise at impressive amounts for the next several years.

The Guaranteed Student Loan Program and most assuredly, the Texas Guaranteed Student Loan Corporation, is financially sound and stable. The continued support and confidence of the financial community in TGSLC and the GSLP is vital to assure that loans are available this Fall and throughout the coming year for students.

THE IMMEDIATE ISSUES

Again, the HEAF crisis being symptomatic of a broad, system-wide problem, a fast resolution is possible, but limiting in what it will accomplish. However, there are some steps that should be taken immediately:

o Regardless of the outcome, the confidence of lenders in this program must be maintained. This will only be achieved by honoring the guarantee on all HEAF loans at 100%. Without lender confidence, this program will not survive. This commitment to the lenders must be made known as soon as possible in order to avoid an unnecessary loss of loan access for students this Fall. Congress should act immediately to pass legislation requiring the

Department of Education to honor loan guarantees at 100% for lenders in cases where a guarantor may be financially insolvent.

o The integrity of this program is more important than the profits of an individual school owner. The Department must allow guarantee agencies to further restrict school eligibility until improvements in program eligibility and certification are implemented, as suggested by the Inspector General himself in his most recent Report to Congress dated April 30, 1990.

o No more schools should be approved in this program by the Department of Education until they have fully responded to the Inspector General's audit.

ISSUES FOR REAUTHORIZATION

Reauthorization will allow the many players in the Guaranteed Student Loan Program to re-examine the successes and challenges of this program. Let us not waste this mandate by glossing over problems and relying on platitudes. Much will be written and discussed later about Reauthorization, however, the outcome must include:

o an ability to provide access to loans for high-risk borrowers and at the same time reasonably manage defaults

o reaffirmation of the decentralized, state guarantor administration of the GSLP and its importance to decentralize in order to more realistically apportion the risk

o a definition of access that insists on a quality program of instruction appropriate to provide meaningful outcomes for students

o provide "performance based" incentives for lenders and guarantee agencies to encourage low default rates, while still providing loan access to low income students attending eligible schools of all types

o provide necessary federal incentives to guarantee agencies to insure adequate reserves are maintained against future loan loss without the threat of "spend-down"

CONCLUSION

My message to all of you is that HEAF is not a lone wolf. Other guarantors, including TGSLC, have been asking for appropriate program related action for several years. We supplemented our pleas with the strongest internal actions that the Department of Education would allow. We believe that the HEAF phenomenon is a consequance of this program's failure to enforce program standards for schools and yet force guarantors to insure loans from all schools.

This federal lack of diligence has created the perception that the Guaranteed Student Loan Program is not working. On the contrary, the Guaranteed Student Loan Program is a viable and successful student loan program that delivers $12 billion annually to students seeking postsecondary education. Behind all those dollars are millions of students who are achieving their personal dreams. We must take the time now to correct any problems in this program. We must not abandon our commitment to serve all of America's students.

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Stephen C. Biklen
Vice President

August 15, 1990

The Honorable Claiborne Pell
Chairman
Subcommittee on Education, Arts,
and Humanities
United States Senate
335 Russell Senate Office Building
Washington, DC 20510

Dear Senator Pell:

Thank you for your letter of August 6th. I am pleased to enclose my responses to additional questions you had as a result of my appearance before your committee on August 3.

Please do not hesitate to contact me if I can be of additional assistance regarding the Student Loan Program.

Sincerely,

Stephen C. Biklen

Enclosure

(Reference: 8/6/90 Letter from Senator Pell)

ANSWERS TO QUESTIONS REGARDING PROBLEMS CONFRONTING THE HIGHER EDUCATION ASSISTANCE FOUNDATION

1) I am not aware of any crises with respect to any lenders in the Student Loan Program similar to that facing HEAF. However, depending upon how the HEAF situation is resolved, and, as noted in the answers to several questions below, lenders could significantly vary their activities within the Student Loan Program depending upon the resolution of this issue.

2) The answer to this question depends upon how the problem is resolved. If the problem is resolved such that the guarantee on loan insurance remains at 100%, I would expect that there will be no significant change in Citibank's approach to the program, although individual limits per guarantee agency may be revised downward.

If, however, a resolution of the problem results in less than 100% guarantee to lenders, Citibank most certainly would restrict its guarantee activities to those agencies either backed 100% by the State in which they resided or those agencies which are an integral part of the State government. In addition, Citibank would probably establish significantly lower exposure limits with respect to each of the guarantee agencies that insured its originations. I would expect other lenders to react in a manner similar to Citibank.

3) Yes. CBA has noted that lenders have restricted lending in geographic terms, by school type, and according to default rates.

4) Yes. We believe that lenders have already begun to restrict their areas of service. However, the impact of this could be minimized if the HEAF situation is resolved favorably, i.e., 100% insurance is maintained. In addition, if procedures are developed to cover future situations similar to the current HEAF situation, and those procedures ensure 100% guarantees, this impact will be further minimized.

5) Some action has been taken to avoid another HEAF situation to the extent that significant default reduction legislation and regulation has been put in place. We have not yet seen the full impact of these changes.

In addition, CBA would support the following measures:

- Additional legislative change as outlined in my testimony at the hearing.

(2)

- Implementation by the Department of Education of an early warning system, also mentioned in my testimony, and further discussed in my letter dated August 14 to Senator Simon.

- Legislation implementing a process to ensure the absorption of a financially troubled agency by one or more other guarantee agencies with maintenance of 100% guarantees to lenders.

6) The Guaranteed Student Loan Program will remain sound as long as the current situation is resolved and 100% guarantees to lenders are maintained.

7) There is no question that SLS loan volume has decreased significantly, and CBA believes that the majority of this decrease is due to the elimination of SL loans for first year students at schools with default rates in excess of 30%. Based upon this, the action should have a very positive impact on reducing loan defaults.

8) Lessons to be learned include the following:

- We need an early warning system to identify agencies that may have future problems.

- Legislation is needed to provide a mechanism for dealing with financially troubled agencies without any loss of guarantee.

9) CBA believes that the shift from grant aid to loans probably has had a negative impact on loan defaults, particularly for lower income borrowers. In addition, however, CBA believes that the impact of legislation and regulations aimed at schools which have abused the program needs to be assessed before making a final judgment. Also, additional legislation that could be considered. This could include the requirements that schools provide students with more consumer related information relating to the outcome of the educational program offered.

10) CBA believes the primary causes of defaults are as follows:

- In many cases low completion and placement rates reflect poor educational quality, inappropriate admissions, or abuse of the student aid programs.

- High debt burdens, particularly for those borrowers from low income families.

8/15/90

N·A·S·F·A·A

August 15, 1990

The Honorable Claiborne Pell
Subcommittee on Education, Arts and Humanities
428 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Pell:

On behalf of the more than 3,400 institutional members of the National Association of Student Financial Aid Administrators (NASFAA), I am pleased to respond to the questions in your letter dated August 6, 1990.

Question 1. In last year's budget reconciliation, we eliminated SLS Loans for first-year students at schools with default rates in excess of 30 percent. The General Accounting Office is issuing a report today showing that this action has dramatically reduced loan volume. Do you agree that this action will help loan defaults?

The Omnibus Budget Reconciliation Act of 1989 made several changes to the Supplemental Loans For Students (SLS) Program that have significantly reduced the SLS eligibility of some students and, subsequently, seem to have reduced SLS loan volume in the first four months of calendar year 1990. As you know, this action was taken by the Congress as a cost-saving measure in response to the dramatic increase in SLS loan volume from FY-87 to FY-89, and the corresponding increase in SLS loan defaults during this time. Because proprietary institutions were seen as largely responsible for the increase in loan volume and defaults, the reconciliation action targeted its provisions to affect students attending those types of institutions. Proprietary school students tend to be low-income, high-risk students who are often less well prepared to persist academically than students attending more traditional postsecondary institutions. The effects, then, of the reconciliation provisions will most probably reduce student loan defaults in the SLS program because these types of students are more likely to default on their loans.

Although the actions taken in the reconciliation legislation were aimed at those institutions who were perceived to be abusing the system, I submit that the legislation may be incomplete and, in some cases, unfair. In particular, if high default rates are an accurate indication that a particular school is weak, then additional action may be necessary to address the participation of those schools in the other federal student aid programs. Using high default rates as the only criteria to determine an institution's eligibility for federal programs, however, may be unfair to those institutions who are providing quality education or training services but serve mostly low-income, high-risk student who are more likely to default on their loans. I look forward to working with you to develop some additional criteria in this area during the reauthorization process.

NATIONAL ASSOCIATION OF STUDENT FINANCIAL AID ADMINISTRATORS
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The Honorable Claiborne Pell
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Question 2. What are the lessons to be learned from the HEAF crisis?

(1) The shift in the primary oversight responsibility of the GSL programs from the Department of Education to the guaranty agencies has resulted in a less efficient oversight mechanism. Over the past several years, the Education Department has significantly reduced the number of program reviews and audits it has performed. In large part, this has been caused by reductions in Departmental salary and expense requests, but also by administrative allocation priorities within the Department. The result has been that the program review and audit responsibility—without reasonable resources or compliance authority—has shifted to the guarantors. In the future, the Administration needs to be more aggressive in making the case for expanding the corrective authority of the Department or fully utilizing the authority it has to properly manage the programs as well as it could.

(2) In addition, as I noted in my testimony, a guarantor cannot suddenly terminate its school or lender agreements without going through the defined due process route, nor can it limit or define its area of service without concurrence from the Department of Education. Yet, the guarantor has to assume the liability, while the Department resolves the issue. The result is that when problems begin to arise, the guarantor is unfairly penalized because it cannot properly respond in a timely manner to the changing environment in which it finds itself. It appears that—given the HEAF situation—this policy should be reviewed.

(3) Traditionally, the Department has advanced that competition among guaranty agencies would strengthen the operation of the entire guaranty agency community. Competition in this particular instance created an environment for HEAF to amass a large proportion of high-risk student loan paper in its portfolio. Clearly—through its quarterly and annual reports—the Department was aware of HEAF's weakening financial situation, but no action was initiated. Perhaps this is not a wise way to allow the system to operate without more supervision by the Department.

Question 3. During the 1980s, we had a dramatic shift from grants to loans. Our student aid programs have also failed to keep pace with the cost of a college education. Could you please comment on how this policy change is affecting student loan defaults?

Although total program cost for the Pell Grant Program has increased considerably, what we have seen in the past several years were really just expansions in eligibility. Some of them were very conscious expansions such as extending eligibility to less than half-time students or to somewhat higher income students. Some of the cost increases resulted from an increase in participation of independent students or students from vocational, short-term programs, particularly proprietary institutions. However, the lowest income college student who is receiving the maximum award has seen a real erosion in purchasing power because the maximum award has remained fairly constant. A panelist at a recent NASFAA forum expressed that during the past several years it seems as though "we have been throwing half a life jacket to many students rather than a full life jacket to the ones we can save."

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In order to counterbalance this decrease in purchasing power, more and more low-income, high-risk students have had to rely on student consumer credit programs to finance their postsecondary education. As originally enacted, however, the Guaranteed Student Loan Program was designed to assist students from middle-income families who were encountering cash flow problems in meeting educational expenses. It was conceived to be a loan program that would only be used to assist students from low-income families as a last resort, and then only after those students had exhausted their eligibility for other grant and work programs. What has evolved is a loan program whose participants are mostly low-income, high-risk students who statistically are often less well prepared—relative to their counterparts—to pursue a postsecondary education. In effect, it has become the access program for many of these students.

Several recent studies have shown the relationship between family income and default rates. In particular, the Pennsylvania Higher Education Assistance Authority's recent report entitled *A Decade of Growth, Pennsylvania Cumulative Stafford Loan Debt, 1980-1989* shows the relationship between family income and default rates for Pennsylvania borrowers. Students with family incomes of less than $6,000 were shown to be twelve times as likely to default on their loans as students with a family income of $42,000 or more. While some of the problems associated with increased student loan defaults are clearly related to program quality and other issues, the current federal policy—which ultimately requires students from low-income families to borrow in order to meet their educational financing needs—has contributed significantly to the default problem. The student grant/loan balance is certainly an issue that deserves more attention during reauthorization.

Question 4. What do you see as the primary causes of student loan defaults?

To pinpoint the exact causes of student loan defaults is a difficult task given the complexity of the program and the diversity of institutions, lenders, and students who participate in it. Quite clearly, however, the large increase in low-income, high-risk students participating in student consumer credit programs has contributed to the increase in defaults. The Congress simply must realize that turning the GSL programs into access programs and giving unsecured loans to high-risk borrowers will lead to defaults.

Most disturbing, however, are the defaults caused by inadequate education or training services provided by a few institutions. Although the vast majority of proprietary institutions provide valuable services to millions of students, anecdotal evidence and press reports suggest that there are some schools who employ shady recruiting methods to entice students into programs that will not lead them to productive employment. The students targeted by these schools are mostly low-income, disadvantaged students who are looking for ways to become productive, contributing members of society. Unfortunately, they often find themselves heavily in debt, without employment after having participated in these types of programs, and often have no other choice but to default on their loans.

I can assure you that NASFAA will work with the Subcommittee to address these and other issues surrounding student loan defaults during the reauthorization process.

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Question 5. What more should be done to rid the student loan programs of bad schools?

It has long been NASFAA's belief that maintaining and ensuring the integrity of the student aid programs is central to their success and, perhaps, to their existence. Abuse of the federal student aid programs can be curtailed if disreputable schools are prevented from participating in the programs. Current standards require that—before an institution can participate in the programs—it must be licensed to provide postsecondary education in the state in which it operates, accredited by an accrediting agency sanctioned by the Department of Education, and certified by the Department as to its financial responsibility and administrative capability to participate in the programs.

These mechanisms, however, have been criticized by some because they do not provide assurance that accrediting bodies are reliable authorities to sanction schools and because many states differ in their authority to regulate schools, revoke licenses, and license branch campuses. As a result, many schools are currently participating in the federal student aid programs who—under more stringent supervision—would not be allowed to do so.

To address this issue, NASFAA is in the process of developing recommendations that will be presented to the Congress and the Administration during the forthcoming reauthorization of the Higher Education Act of 1965. We look forward to sharing these recommendations with you and to working with you and your staff on these and other issues as we seek to improve and expand educational opportunity for our nation's students.

Thank you for inviting me to testify and for soliciting additional comments on these important matters. If I can be of any further assistance to you, please do not hesitate to let me know.

Sincerely,

Dallas

Dallas Martin
President

STUDENT LOAN MARKETING ASSOCIATION
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202-298-2600

LAWRENCE A HOUGH
President and
Chief Executive Officer

August 14, 1990

The Honorable Claiborne Pell
Chairman, Subcommittee on Education,
Arts and Humanities
Committee on Labor and Human Resources
United States Senate
Senate Russell Office Building
Washington, DC 20510-3901

Dear Senator Pell:

Enclosed please find our responses to the additional questions you have posed in connection with the hearing before the Subcommittee on August 3, 1990. Although some of the questions posed fall somewhat outside of our familiar area of expertise, we have nevertheless given our response to them.

We are appreciative of the Subcommittee's attention to the need to address the issues which led to the problems of the Higher Education Assistance Foundation.

Sincerely,

Lawrence A. Hough

1. If Sallie Mae were to take over HEAF, would you gain the ability to issue tax-exempt bonds?

No. To our knowledge, HEAF as a guarantor has no tax-exempt financing authority. In any event, the authority to issue tax exempt bonds is one that is granted by the Internal Revenue Code and is not an authority that can be simply transferred by one entity to another. Moreover, the Code provides that the purpose of issuing tax exempt bonds is to raise money for either the making of student loans or the acquisition of student loans in the secondary market. We would not expect to acquire any authority with respect to loan making and loan acquisition functions in connection with any loan guarantee authority that might be agreed to with the Secretary.

2. If you were a guarantor, what would prevent you from directing the best loans to your guarantee agency and sending more high-risk loans to others?

Guarantors are not in a position to direct loan guarantees to themselves or to others. Their only ability is to conduct their own activities in such a way so as to attract the "best loans" and to restrict their guarantee of the "high risk" loans to the extent permitted by the statute. A guarantee agency's ability to do so effectively is, of course, limited by similar activities of its competitors.

3. How could you assure an arm's-length review of your efforts as a servicer if Sallie Mae was to become a guarantor of the HEAF portfolio?

Many state agencies have a guarantee function coupled with a secondary market or direct lender--often with the same senior management. Steps have to be taken, of course, to appropriately separate the functions of loan collector and loan guarantor--a Chinese wall, so to speak--which we believe we can readily accomplish. This is a common occurrence in the program today. Guarantors are, of course, subject to audit by independent auditors and by the federal government in the context of reinsurance. In this way the independent guarantee function is subject to review and oversight.

4. Have lenders begun to restrict lending to certain segments of the population?

We do not have any statistical studies but our experience would indicate that many lenders are restricting the amount of loans they make or acquire from segments of the student population they perceive to be high risk. This pattern preceded the problem at HEAF since loans that default are much more costly for a lender to administer. Moreover, they are on the lender's books for a shorter period of time and, therefore, have shorter earning streams than other student loans, and statistically are smaller balance loans with higher per unit costs. Perhaps most importantly, loans submitted for claim to a guarantor are subject to extreme scrutiny in which every program requirement, no matter how minute or immaterial to the default, is a potential basis for claim rejection. This creates significant insurance risk for lenders leading to their avoidance of loans that have a high risk of default.

5. Will HEAF's problems cause lenders to further restrict their area of service?

HEAF's problems may well result in a number of lenders feeling insecure as to whether they will, in fact, be paid off 100% on defaulted loans which they have properly administered. The insurance is, of course, the only basis on which a lender can prudently make a loan under the program since the loans are not collateralized and the borrowers have no income, and little or no credit experience.

6. Is any preventive action being taken to avoid another situation of this magnitude?

We expect that, in light of this serious situation regarding HEAF and the Department's concern about the financial condition of several other agencies, the Congress and the Department are considering actions that would stabilize the guarantee in the program so as to provide lenders with the necessary assurances to go forward with program lending and secondary market purchases.

Hopefully, in plotting their strategy in this regard, policymakers will take a more measured approach to the regulation of guarantor reserves, including federal financial support of them, and reject the concept of using these financial underpinnings as a means for helping to meet shortfalls in federal revenues or reducing the federal deficit. Guarantors need to be able to meet unforseen circumstances that may arise in the future; without a viable reserve pool, the future stability of guarantors and lenders reliance on them will remain in doubt.

7. This crisis has raised many questions concerning the viability of the student loan program. Do you feel the program remains sound?

Yes. While there are problems that need to be faced up to and dealt with appropriately, we believe the program as a whole is sound and can continue to make a vital contribution to the financing of higher education. It cannot, however, be overemphasized that lenders must be assured that the loans they make will be repaid.

8. In last year's budget reconciliation, we eliminated SLS Loans for first-year students at schools with default rates in excess of 30%. The General Accounting Office is issuing a report today showing that this action has dramatically reduced loan volume. Do you agree that this action will help loan defaults?

Yes, the reduction of abuses in the SLS program will result in fewer defaults.

9. What are the lessons to be learned from the HEAF crisis?

There are a number of lessons to be learned. One is that unless lenders can be assured that their loans are, in fact, guaranteed against default at 100% without regard to the financial condition of the federally sponsored guarantor, the ability of this program to achieve the purposes for which it was created are indeed limited. There must be general recognition that making good to banks as distinguished from the guarantor for the credit they have extended to borrowers on the basis of a guarantee of repayment, is fundamental. Indeed, this is the basic design of the program. Were it not for the guarantee, very few loans would be made since very few borrowers would qualify on the basis of lenders normal standards and prudent practices for making loans. Another lesson is that very little is known about the financial condition of each of the guarantee agencies, and therefore little influence brought to bear on their activities by either the public or private sector.

10. During the 1980s, we had a dramatic shift from grants to loans. Our student aid programs have also failed to keep pace with the cost of a college education. Could you please comment on how this policy change is affecting student loan defaults?

Clearly, as the Report of the Belmont Task Force suggests, the program of guaranteed student loans, which was designed for the middle class, is under severe strain as a result of being pressed into service as a major form of assistance for students from financially needy families. This is especially so during periods when the costs of education are increasing, thus requiring even larger loans. The disposable income of this group of borrowers cannot sustain the repayment of increasingly larger loans. As was pointed out in the Belmont Report and has been reiterated by all major studies on student loan defaults, the major cause of default is the borrower's inability to pay, rather than a decision to avoid his obligations.

11. What do you see as the primary causes of student loan defaults?

There are, no doubt, multiple reasons for student loan defaults. We doubt whether the default rate is any greater, however, than would be the case with respect to consumer loans generally in the populous if banks made loans to borrowers who have no credit experience, no employment history, no assets and have provided no security on the loan. In addition to the foregoing, a number of borrowers do not receive the benefit of their borrowing. This is so because they were not adequately prepared to benefit from the program for which they borrowed, or the program did not provide them with the employment they expected, or the program was simply of poor quality. However, it cannot be overlooked that this may be for most students their first significant experience with debt financing. There are, of course, many competing demands for what may be limited resources and there is no lack of marketers of goods and services who are competing for the dollars borrowers earn after leaving school. In this connection, it may be useful to reflect upon the fact that while the repayment period on student loans (except for consolidation loans) has not essentially changed since the inception of the program, the amount of aggregate possible borrowing as a result of increases in the cost of education have risen quite dramatically. Nevertheless, studies indicate, and our own experience would confirm this, that the default rate declines as the size of the borrowing increases. This appears to be associated with the coincidence of large size borrowings for students who undertook four-year or advanced degree programs, a fact which has a positive correlation to the ability of the borrower and his family to support the debt.

STUDENT LOAN MARKETING ASSOCIATION
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LAWRENCE A. HOUGH
President and
Chief Executive Officer

August 23, 1990

The Honorable Edward M. Kennedy
Chairman, Committee on Labor and Human Resources
United States Senate
315 Senate Russell Office Building
Washington, DC 20510-2101

Dear Senator Kennedy:

Enclosed please find a copy of our response to the additional questions you have posed in connection with the August 3, 1990 hearings before the Subcommittee on Education, Arts and Humanities on the HEAF situation. As you have requested, the original copy of the response has been submitted to the Subcommittee.

We agree, as is indicated in our response to your inquiries, that our corporate involvement with HEAF and our recent response to its financial problems affords an interesting context for the consideration of the Treasury Department's proposed safety and soundness provisions for GSEs.

Sincerely,

Lawrence A. Hough

Lawrence A. Hough

35-069 0 - 90 - 9

1. There have been some suggestions that, in light of the HEAF situation, Sallie Mae should be subject to safety and soundness regulations regarding government sponsored enterprises that were recently proposed by the Treasury Department. What would be the impact on the Sallie Mae if the Treasury proposal is adopted?

This question suggests several lines of inquiry. Initially, what business risk does HEAF's situation present for Sallie Mae? Had the Treasury proposed regulations been in place, what effect might that have made on Sallie Mae's HEAF related business? And, aside from special HEAF issues, what other effect might the Treasury proposals have on Sallie Mae's ability to carry out its statutory mission?

At the outset, we reiterate that the impact on Sallie Mae's balance sheet and earnings as a result of our financial exposure to HEAF will not, in our judgement, be material. As we indicated in our testimony before the Subcommittee on Education, Arts and the Humanities, our exposure falls into two basic classes. First, HEAF is a guarantor of a significant portion of the guaranteed student loans which Sallie Mae owns. And second, HEAF is a borrower of funds from Sallie Mae.

A large majority of HEAF guaranteed student loans, which we own, are already in repayment and hence, can be expected to experience insignificant default rates. The default experience on the smaller, newer portion of our HEAF guaranteed student loan portfolio can be reliably predicted based on experience and is of course higher. The composition of this newer portfolio of loans, however, is not skewed in favor of trade school loans or any other group.

In any event, our mandate is to provide liquidity through the purchase of guaranteed student loans on a national basis and without regard to which of the guarantee agencies--either the federal government itself or one of the 47 government sponsored state or non-profit, private guarantors--may have been the insurer of the loan under the program. Like all the rest of the lenders and holders of guaranteed student loans, we have to rely on, and at least until now had no reason not to rely on, the fact that these loans were insured fully against the default, death and disability of the borrower.

Under another essential part of our mission, over the last six years and prior to our most recent extension of credit to it, we have extended collateralized advances to HEAF and its affiliates totaling about $800 million: $200 million of which was lent to HEAF itself. The remaining $600 million was lent to the HEAF/HELP organizations which provide direct lending and secondary market services in D.C., Kansas, Tennessee and West Virginia. All of these advances are more than 100 percent collateralized with guaranteed student loans and federal obligations.

Recently, as a result of discussions with the department of education, we have agreed to extend additional credit for HEAF of up to $200 million. Any advances made under this new commitment of credit will, in our judgement, be adequately secured. Our decision to provide interim financing for HEAF to permit the government time to arrange for a permanent solution, was made on the basis of our evaluation of the circumstances and risks involved, consistent with prudent business practice. One can only speculate at this juncture as to what might have happened had the Treasury's proposed financial safety and soundness policies been in place. On the one hand, Sallie Mae currently enjoys a AAA rating currently without regard to our agency status. On the other hand, if irrespective of that status, Treasury determined as our regulator of financial safety and soundness to provide oversight with respect to our HEAF transactions, we have no way to know whether they would have reached the same conclusion with respect to the further extension of credit to HEAF. In any event, it seems clear that it is unlikely that we would have been in as good a position to take decisive action in the timely manner that we did. Given the coverage in the public press we betray no confidence in sharing with you the fact that, without our prompt assistance, HEAF might well have been forced to default on its obligations to lenders. The consequence of that occurrence, we believe, could have severely jeopardized the program at the height of the annual lending season.

The HEAF situation, we believe, emphasizes the need to assure the existence of a financially strong, national secondary market, subject to the disciplines imposed on publicly held corporations and appropriate congressional oversight, but possessing the ability to take actions without governmental clearances.

2. What would the the impact on the student loan program if the Treasury proposal is adopted?

We believe the Treasury proposed use of private rating agencies for the purpose of determining safety and soundness; the AAA rating standard proposed; the establishment and supervision of business plans by the Treasury; the imposition of risk premiums and/or recovery rate fees, and the withdrawing of particular agency benefits; and, the ability to replace our Board of Directors and/or officers, would adversely affect our ability to raise equity capital and finance ourselves in a cost effective manner. We do not believe that there is any added value to Treasury Department regulation in the management of Sallie Mae. We already enjoy a AAA rating without regard to our GSE status. Investors in our debt and, by and large, in our common stock are large sophisticated financial institutions. There is no comparison between them and individual depositors in a bank or S and L.

In short, we think the Treasury already has an adequate statutory role in the conduct of our business and that role, together with the presidential appointment of a third of our Board of Directors and it's Chairman and the oversight of the congressional committees, more than adequately forms a basis for reflecting public interest in our financial well being. Further intrusion by government into the management of Sallie Mae, in our view, risks the possibility of poor performance for which, we believe, the government would properly be held responsible by our investors.

Since its inception, Sallie Mae has supported approximately $50 billion in student loans to approximately 20 million student borrowers and their parents. This means that over the course of years we have provided support for approximately 49 per cent of all student loans made. Any significant limitation on our activities would constrain the willingness of lenders to extend credit to borrowers in the program unless the slack is made up for by other secondary markets or financial institutions. Virtually all of the other secondary markets operate at the local level or, if not, in certain particular markets through arrangements with a limited number of lenders. No one, to our knowledge, holds itself open to providing liquidity to virtually every eligible lender across the nation as does Sallie Mae and few, if any, offer warehousing advances collateralized by student loans to lenders who do not wish to sell their loans. In addition, secondary markets generally rely on the undependable availability of tax exempt financing, and financial institutions that acquire and hold student loan portfolios are in and out of the marketplace depending on the attractiveness of alternative uses of their funds. The most damaging program consequence may be a perceived concern that there might not be liquidity at reasonable cost for those who make student loans or that a competitive market for their student loans would not be available to them. Any such perception would be bound to dampen lender participation in the program.

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NATTS

August 15, 1990

The Honorable Claiborne Pell
Chairman, Subcommittee on Education,
Arts, and Humanities
648 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Pell:

Thank you very much for providing me the opportunity to testify before the Subcommittee on Education, Arts, and Humanities during its hearing on the Higher Education Assistance Foundation (HEAF) held August 3, 1990.

I am happy to provide to you the additional information which you requested in your letter to me dated August 6, 1990. Enclosed are responses from the National Association of Trade and Technical Schools to the questions you raised.

Again, thank you for inquiring about the concerns of trade and technical students and schools regarding the HEAF situation. Please let us know if we may be of service to you again.

Sincerely,

Stephen Blair

Stephen J. Blair
President
National Association of Trade
and Technical Schools

Enclosure

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NATTS

RESPONSE TO SENATOR PELL'S REQUEST FOR ADDITIONAL INFORMATION ON THE PROBLEMS CONFRONTING THE HIGHER EDUCATION ASSISTANCE FOUNDATION

August 15, 1990

1. Aren't proprietary schools at the root of HEAF's problem?

No. Proprietary schools are not at the root of HEAF's problem. Schools do not default, borrowers do. High risk students, no matter where they go to school, have a harder time repaying their loans than those students with more advantages. Trade and technical schools enroll more low-income, minority, and generally higher-risk students than other sectors of postsecondary education. These student characteristics are related to the probability of default. Any school enrolling a significant proportion of high risk students will experience a higher default rate than a school enrolling more advantaged students. Any agency which guarantees a large number of loans for high-risk borrowers is going to have a higher default rate than one that excludes or minimizes loans to high risk borrowers. HEAF was very supportive of trade and technical school students when other guarantee agencies were hesitant to support them.

However, evidence suggests that HEAF's default experience has been higher for borrowers in all sectors compared with either USAF or an average of state guarantee agencies. In Fiscal Year 1986, HEAF's two-year cohort default rate was nearly fifty percent greater for borrowers in every sector of education compared to USAF, the other national guarantor. This suggests that even several years ago, HEAF was having trouble controlling its default rate.

Anecdotal evidence exists that demonstrates that HEAF's rapid growth taxed its administrative ability to do the best possible job of managing its portfolio. From 1977 to 1988, the loan volume guaranteed by HEAF increased from approximately $15 million to $3.3 billion. By FY 1987, HEAF was paying more to lenders than it was collecting from the federal government. According to Department of Education (ED) reports, HEAF had a $32 million short-fall in FY 1988. HEAF took steps in FY 1988 to shift itself away from loans with a high risk of default. Part of that effort was to balance its portfolio by aggressively pursuing loans of students attending four-year institutions.

To secure this lower-risk paper, HEAF offered zero percent insurance fees. This had a negative impact on its income. As recently as February 1990, HEAF reported it had solved its problem and was well on the way to long-term profitability. Clearly, HEAF was overly optimistic. HEAF was not able to improve its default rate even after excluding as many high risk borrowers as possible.

While schools have little to do with loan repayment, there is a great deal that schools can do to prevent defaults. They must first admit only those students who, in the schools' best judgement, are capable of completing the education and of being placed in a job for which they have been educated. Schools can help borrowers understand their rights and obligations regarding the loan programs before they receive loans and as they leave school. The private career school Default Management Initiative, launched more than three years ago, has assisted over 5,000 schools with the development of counseling such as entrance and exit videos which improve student graduation rates.

Again, the default rate is primarily a function of the population served. Within trade and technical schools, as well as all postsecondary schools, there are wide ranges of default rates. They range from low single-digit default rates to some above 30 percent. These variations reflect the percentages of high risk students served by each of the respective schools.

The significant differences in the default rates among lenders and guarantee agencies, independent of the level of risk represented in their student loan portfolio, indicates that guarantee agency and lender servicing and collection activities make a difference in successful repayment.

2. In last year's budget reconciliation legislation, Congress eliminated Supplemental Loans for Students (SLS) for first-year students at schools with default rates in excess of 30 percent. The General Accounting Office is issuing a report today showing that this action has dramatically reduced SLS volume. Do you agree this action will help loan defaults?

There is no question that the most effective way to eliminate defaults is to stop making loans. Defaults can be reduced by limiting access by high risk students. The resulting problem is the long-term cost of limiting access for these students. According to Jerry Jasinowski, President of National Association of Manufacturers, these long term costs include the following:

- Productivity losses caused by poorly trained workers cost U.S. business about $25 billion last year.
- One out of every four ninth graders drops out of high school each year at an estimated cost to the nation in lost earnings of $240 billion during their lifetimes
- If private business is to close the "skills gap" between workers and labor market needs, America's private sector will have to expand its training efforts from $30 billion to $88 billion a year.

Saving money today by keeping high risk students out of loan programs will increase social costs in the future. Excluding these students from the loan program does not solve any problem or reduce society's cost of an under-educated work force. Short-term savings in default reduction will be spent many times in the cost of welfare, unemployment, health benefits, administration of justice, and loss of productivity. Margaret Beyer stated the problem succinctly in the current issue of Youth Policy on delinquency,

"James plans to sell drugs when he is released form the institution -- it is the only entry-level job where his lack of skills does not disqualify him."

The loan programs are a key part of the financial assistance package many students require to attend a postsecondary institution. Given that funding for the Pell Grant program has not kept pace with inflation over the past decade, even the very poorest individuals must rely on federal student loans to finance their education. The following example indicates their need for Pell Grants, Stafford Student Loans, and Supplemental Loans for Students (SLS).

A single welfare mother 25 years of age with a child decides to attend a private career school for nine months. The school charges a tuition of $5,000 . Her budget will be a minimum of $4,000 for child care, room and board, and other incidental expenses. A full Pell Grant and Stafford Loan would cover roughly half the $9,000 it will take to attend school. Even with an SLS, this student will be shy several hundred dollars of the minimum cost. Without the SLS, she cannot afford to attend the school. Granted, this student is at risk of defaulting, but without an appropriate postsecondary education she is at risk of a lifetime on welfare.

3. What are the lessons to be learned from the HEAF crisis?

The first lesson is that the threat of financial punishment for high defaults will result in a reduction of opportunity for the neediest students. Lenders, guarantee agencies, and schools increasingly are unwilling to serve students with the most need who also have the highest chance of defaulting because the institution will be punished for doing so. HEAF tried to exclude high risk borrowers as the way to solve its cash problem.

An incentive system built on punishment, such as risk-sharing, will result in the exclusion of those students who need help most. Banks have always known that the highest risk borrower is one who does not have any resources. Contrary to its original mission of helping middle income families finance postsecondary education, the federal student loan programs now serve even the poorest students to compensate for inadequacies in federal grant assistance. Further, the purpose for providing a federal guarantee is to ensure access to loans for students regardless of their credit history and to provide assurance that lenders' investments are protected.

The second lesson is that the Department of Education needs to take responsibility for oversight and enforcement of regulations. In the long run, anticipation of school, lender, and guarantee agency problems before they escalate to disaster proportions will be more effective. Prevention is the best way to solve problems and protect taxpayers from unnecessary financial losses.

The third lesson is that positive, not negative, incentives are needed for schools, lenders, and guarantee agencies to serve high risk students. The government needs to ensure that lenders and guarantee agencies obtain a return on their investment that is high enough to make serving high risk students worthwhile.

4. During the 1980's we had a dramatic shift from grants to loans. Our student aid programs have also failed to keep pace with the cost of a college education. Could you please comment on how this policy change is affecting student loan defaults?

The biggest loss in federal support came with the conclusion of the Vietnam Veterans education benefits and the loss of Social Security education benefits. These two programs provided $3.6 billion in grant aid to students in 1980. These programs were not need-based, but in practice, helped low income students.

According to the College Board, the federal government provided about 56 percent of the 1980 student aid awards in grants, 40 percent in loans, and the rest in College Work Study. In 1989, 48.5 percent of the awards were in grants, 49 percent in loans, and 2.5 percent in College Work Study. The amount of all federal award dollars has declined slightly from $19.8 billion in 1980 to $19.4 billion in 1988 (in constant 1988 dollars), while costs of education significantly increased during the 1980's.

The other way to calculate the erosion caused by inflation is to calculate how much the maximum award has declined. The maximum Pell Grant ($2,300), which affects the neediest students, has slipped a little over six percent since 1980. The maximum Pell Grant should be about $2,450 if it were to have the same purchasing power as it had in 1980. Recognizing this need, the Pell Grant currently is authorized to have a $3,100 maximum award, but is only appropriated at a level of $2,300. This forces the needy to rely heavily on loans to finance their postsecondary education.

The maximum Stafford Loan has not done well relative to inflation either. If the maximum loan were to have the same purchasing power now for a lower division undergraduate as it did in 1980, it would have to be $3,100 instead of the current $2,650. There has been a loss of about 17 percent in the maximum loan available to a first or second year student.

What this means is that there has been a modest shift in federal student aid from grants to loans with overall award dollars remaining nearly constant. Again, one must remember the $3.6 billion loss in Vietnam Veterans and Social Security education benefits. In that same time, collegiate enrollment has gone from 12.1 million with an estimated 1 million in non-collegiate schools to 12.9 million with another 1.7 million in non-collegiate schools. There has been a modest 11.5 percent enrollment increase over the decade. Much of the percentage increase is found in part-time and non-collegiate school enrollments. The amount of federal aid per student has eroded slightly over the decade.

Students today are not as well served by federal student aid as were students in 1980. Today's students are more likely to rely on loans because the maximum grant awards do not go as far. There are more students in school with fewer award dollars available. We estimate that if the correction were made for the increased enrollment (11.5 percent or $2.2 billion) and the $400 million lost to inflation, it would take $2.6 billion in new appropriations for grant programs to regain the relative position held in 1980.

Using this money to replace loans with grants for high risk students certainly could reduce defaults. The increased cost of a larger grant program to the Treasury would be partially recouped in default savings in future budget years. If the $2.6 billion were used to provide grants instead of loans to a high risk population with a default rate of 30 percent, the default savings would exceed $750 million.

5. **What do you see as the primary causes of student loan defaults?**

The evidence is clear that the main reason for defaulting is borrowers do not have the money to make the payments. Based on information on borrowers collected by the Department of Education, we have identified several factors related to default. They include: being a disadvantaged minority, being divorced or separated, and not completing a program. It does not matter in what type of institution the student is enrolled.

When those students who defaulted were asked why they defaulted, they were most likely to say it was because they were unemployed or under-employed. In short, they did not have the money they needed to make payments. Interfering personal problems also play a big part in propensity to default. Getting a divorce, spells of illness, or unexpected moves play a role in defaults.

One of the most disturbing results was that a large number of borrowers who defaulted did not know about deferments even though they might have been eligible to take advantage of the option to head-off default.

Over half the borrowers who defaulted indicated they had entered repayment at some time after defaulting. A majority of these repayments fall outside the default cohort. Even if repayment begins during the cohort window, the school is not credited with the repayment. Default is a temporary status for the majority of defaulters who repay at a later date. Defaults, as they are reported by ED, do not represent a total loss to the Treasury but a gross dollar figure before repayments are made.

6. What more should be done to rid the student loan program of bad schools?

We need to be careful not to equate high defaults with "bad schools." Many schools are trying to help students who have not been well served by the public school system. According to the National Assessment of Education Progress (NAEP), many 17 year-old students cannot summarize a newspaper article, write a good letter requesting a job, solve a real-life math problem, or follow a bus schedule. It is no wonder that these students, who are eligible borrowers in a very short time after this test is given, have trouble making loan payments. Many borrowers are not well prepared to deal with the administrative requirements that come with a loan. One way to solve the default problem is to improve students' basic life skills in high school. If they have not been well served by the secondary education system, then incentives must be given for postsecondary schools to include basic life skills their curricula. This makes more sense than trying to close trade and technical school that are trying to help these high risk students become more productive members of the workforce.

At the same time, there have been a few schools which have abused the student aid programs, defrauding the taxpayers and leaving students with debts they cannot repay. These schools must be identified and stopped, and the NATTS Accrediting Commission is taking strong measures to ensure that any school with the NATTS seal of approval meets the high standards required. While our Accrediting Commission is doing its job to prevent abuses, until recently, it has received little help from the Department of Education.

Prior to the Reagan administration, the Department of Education had an effective program in place to provide student financial aid program oversight. ED was able to identify potential student financial aid problems early and stop them before they cost taxpayers a great deal of money. During the period of greatest growth in the GSL program, the Administration reduced regulatory staff and the number of oversight visits to schools, lenders, and guarantee agencies.

One result of this reduced oversight has been an increase in problems in local administration of student financial aid programs. The current Administration has encouraged the Department to do more program reviews, and the outcome has been more effective oversight. However, increased oversight of all participants in the guaranteed student loan programs is essential to preserve the integrity and restore public confidence in a program that has served over 50 million students since its inception.

Many of the overtly fraudulent schools have been closed or currently are under investigation. Even if a school has been closed for as long as three years, it still had a cohort default rate reported by the Secretary of Education for Fiscal Year 1988. Thus, some of the recently reported default numbers are "ghosts of the past." Hundreds of private career schools have gone out of business in the last two years. Some have been forced to close because of legal problems or mismanagement, but many more have closed because of their students' reduced access to student aid.

The changes in default rates resulting from new federal regulations and restrictions which were implemented last year will not be known until next year at the earliest. It is too early to decide that these efforts have not been successful. However, the decline in private school default rates is largely attributed to our sector's Default Management Initiative. The default rate has been declining since FY 1986 and will continue to decline in future years.

If there is fraud in the operation of federal student aid programs, the responsible parties should be prosecuted. If accrediting commissions are lax in the enforcement of appropriate standards, the Department of Education should not recognize them. If guarantee agencies are experiencing financial difficulties, the Department of Education should carefully monitor them to ensure that they do not become insolvent. The means of enforcement are available to the federal government. Additional restrictions could further undermine the mission of the GLS programs -- to provide needy students with financial assistance to obtain access to their choice of postsecondary education. We must take care to ensure that this mission is accomplished.

Responses by Richard C. Hawk
to additional questions submitted by letter dated
August 6, 1990 by Chairman Claiborne Pell
in connection with the
Subcommittee on Education, Arts and Humanities Hearing of August 3, 1990

1. What effect would the closing of HEAF have on HEMAR, your for-profit servicing agency?

   HEMAR Service Corporation of America (HSCA) services student loan portfolios of 340 lenders and other holders of student loans throughout the nation. The volume of loans serviced by HSCA s more than $3 billion and includes loans guaranteed by 20 different guarantors. The servicing of these loans under the Federal student loan programs constitutes the primary business of HSCA. In addition, HSCA services privately insured loans which are not part of any Federal program in an aggregate volume of $394,000,000. Closing HEAF could affect future volume of loans serviced by HSCA. Predicting the magnitude of any such effect is difficult, but HSCA probably would need to intensify marketing for servicing of portfolios guaranteed by other guarantors, if HEAR should be closed.

   In order to achieve economics of scale and maximize computer utilization, HSCA provides data processing services both for itself and for HEAF. If HEAR were to close, this cost sharing would cease and HSCA would have to find other parties interested in similar cost sharing or would have to reduce expenses to compensate for the loss of cost sharing.

2. Has the Bank of America situation in California contributed to HEAF's difficulties, and if so, how? Could this have been avoided?

   The Bank of America portfolio in question consists of more than one-half billion dollars in student loans of which more than 95% are loans to proprietary trade school students. Loans to proprietary trade school students normally default at four times the rate of students attending four year colleges and universities. Many of the loans in the Bank of America portfolio, were originated by First Independent Trust Company (FITCO) which used some questionable origination procedures before selling loans very quickly and which now has been closed as a result of problems relating to student loans.

   The FITCO originated loans were sold to California Student Loan Financial Corporation (CSLFC) a secondary market which relied on United Education and Software (UES) for servicing most of its loans. Servicing by UES was grossly inadequate and generally not in compliance with diligance regulations. Fraud in the servicing of some of those loans has been admitted.

Responses by Richard C. Hawk
Page two

As the trustee for CSLFC, Bank of America was the owner of loans purchased from FITCO and was a party to the contract under which UES serviced the loans. The problem of high defaults normally expected to be associated with a portfolio of high risk trade school loans has been exacerbated by poor origination and grossly inadequate servicing. Current delinquencies suggest an ultimate default rate of 60 - 75% on the portfolio.

The Department of Education has entered into an indemnification agreement with Bank of America which will permit the bank to receive claim payments on loans in the contaminated portfolio and which obligates the Department to pay reinsurance to HEAF for defaulted claim payments on those loans, the majority of which would not otherwise be eligible for claims payment. Because HEAF will receive only 80% reinsurance, the cost to HEAF covering losses on a portfolio of more than one-half billion dollars with a default rate of 60 - 75% is unbearable. The burden on HEAF is intensified by the prospect of most of those defaults being paid in a single year.

HEAF entered into a settlement agreement with Bank of America for payment of claims in the contaminated portfolio. The settlement agreement was contingent on an acceptable arrangement under which the Department of Education would provide relief for HEAF on the inordinate cost to HEAF of the portfolio. HEAF proposed that the problem be solved by combining the HEAF guarantee program with the Nebraska Student Loan Program which has automatic 100% reinsurance through fiscal year 1991, thereby permitting defaults from the Bank of America portfolio to be paid with 100% reinsurance. The proposed combination also would have solved the problem of the cost for the inordinate concentration of other trade school loans in the HEAF portfolio and would have combined the programs of the two designated guarantors in Nebraska, giving Nebraska the strength of a single designated guarantor. The Department rejected the Nebraska proposal, but announced that HEAF has severe financial problems. Although the problem of inordinate concentration of trade school loans for the Foundation exists without the Bank of America portfolio, the magnitude of the liability existing with the portfolio contributes to HEAF's difficulties.

Determing how the situation could have been avoided is more complex. HEAF uncovered the problems at UES and in the course of conducting a program review of that operation, notified, and requested assistance from the Department of Education Inspector General. Obviously the situation could have been minimized if HEAF had uncovered the UES problems sooner but the cost of conducting program reviews frequently enough in order to have uncovered the problem sooner is probably prohibitive. Although CSLFC acquired substantial volume, it did so in a relatively brief period of time. The UES servicing operation was reviewed by another guarantor and by a major public accounting firm not long before HEAF uncovered the problem, but neither of those reviews indicated significant deficiencies. The situation also could have been minimized if HEAF had not been required to rescind its action cancelling lender agreements with FITCO and several other lenders which were generating high volumes of predominately trade school loans. The Department ruled that the 30 day cancellation provision in HEAF lender agreements does not permit cancellation without applying formal limitation, suspension, and termination procedures for identifying program violations and providing due process for the lenders. Advantages of providing the protection of limitation, suspension and termination and due process for the lender are obvious and some unfortunate program abuse may be the inevitable price to be paid for achieving those advantages. The problem is partially the result of deficiencies in some of the trade schools which were utilized FITCO as a source of student loans for their students. More careful screening and monitoring eligibility of these schools for Federal programs could have partially alievated the situation.

Muriel Johnson Murray
Executive Director

Sharrye A. Ward
Deputy Executive Director

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August 15, 1990

The Honorable Claiborne Pell, Chairman
Subcommittee on Education, Arts
and the Humanities
Room 648 Dirksen Senate Office Building
Washington, D.C. 20510-6306

Dear Senator Pell:

The Virginia State Education Assistance Authority and the Virginia Education Loan Authority are greatly interested in legislative actions which may be taken to address the financial difficulties encountered by the Higher Education Assistance Foundation. I have enclosed a statement on behalf of the two authorities which describes our concerns.

I would greatly appreciate your including the enclosed testimony in the record of the August 3, 1990 hearing before the Subcommittee on Education, Arts and the Humanities.

Thank you for your consideration of this request. If you have questions or if you would like additional information, please give me a call.

Sincerely,

Muriel Johnson Murray
Executive Director

MJM/lh

Statement of

Muriel Johnson Murray

to the

Senate Subcommittee on

Education, Arts and Humanities

August 10, 1990

Mr. Chairman and Members of the Committee:

I am submitting comments on behalf of the Virginia State Education Assistance Authority and the Virginia Education Loan Authority. As the recent difficulties of the Higher Education Assistance Foundation (HEAF) have shown, student loan guarantors and secondary markets are subject to financial failure as a result of the risks associated with participating in the federal student loan programs. However, we believe that a closer partnership between the federal and state governments can reduce the risks for taxpayers and students alike.

I am the Executive Director of Virginia's designated student loan guarantor and secondary market. While the Virginia State Education Assistance Authority has always received 100% reinsurance due to our comparatively low default rate, we are increasingly concerned about our ability to control the use of our guarantee, given lax federal oversight of school certification for participation in Title IV programs.

The Virginia SEAA and VELA have welcomed recent restrictions on the participation of some schools in the Title IV student loan programs. We have implemented the restrictions included in last year's budget reconciliation measure in the most stringent measure possible. If we were permitted greater latitude in our certification of schools to use our guarantee, we would implement more stringent restrictions.

Virginia has not experienced problems with proprietary vocational schools of the magnitude encountered by other states. Nevertheless, student complaints and school closings are affecting our student loan programs with increasing frequency.

As the recent financial difficulties of HEAF have highlighted, the student loan programs are a curious combination of free market enterprise and government sponsored activities. In order to make student loan funds available to individuals who cannot provide collateral, have no credit record and are sometimes poor credit risks, the federal government, through several state and national guarantors, guarantees loan repayment. If student loan guarantees were unavailable, it is doubtful that commercial lenders would make loans to such a high risk population as college students.

The government has assumed the financial risks of lending to students in the interests of preparing a skilled workforce. It is inevitable that some of these loans will prove to be a poor investment. However, even considering the cost of defaults, student lending is considerably less expensive to the government than funding education solely through grants and is far less expensive to industry than providing equivalent education in the form of on-the-job training.

The greatest default risk in the student loan programs is presented by low-income students attending shorter education programs. Virtually every default study has shown that such students are those most likely to default their repayment obligations. However, these students also are those most likely to need student financial aid if they are to have the benefit of postsecondary education. They are also the cohort most likely to need public assistance if they are inadequately educated.

In recent years, it appears that the U.S. Department of Education has lost sight of these inherent conflicts. Guarantee agencies, such as the Virginia State Education Assistance Authority, are required to guarantee high-risk loans in the interest of preserving education access for students who are, frankly put, poor credit risks. Changes in loan eligibility during the last reauthorization have eliminated the cohort of students most likely to repay their loans, thus increasing the proportion of students likely to default. Lender-of-last-resort provisions require guarantee agencies to make loans to students who are turned down by commercial banks, further increasing our potential liabilities.

Default reduction provisions punish guarantee agencies for the defaults incurred by the students we are mandated to serve by reducing federal reinsurance rates if our default rate exceeds five percent. Despite our accountability for keeping defaults below five percent, guarantors have very little authority to limit the use of our guarantees by high default schools. Finally, the above mentioned risks are exacerbated by extremely lax school accreditation and certification standards on the part of the U.S. Department of Education.

A recent Wall Street Journal article reported that the Congress is considering a number of options to reduce student loan defaults as a result of HEAF's difficulties, including requiring that banks perform credit checks and obtain cosigners before lending to students. But requiring credit checks and cosigners does not address the root of the problem. Most student loan defaulters have defaulted for one simple reason -- they are too poor to repay their loans.

Stafford loans are limited to lower-income students, many of whom lack a credit history. In most instances, a credit check will merely confirm this fact.

Similarly, requiring cosigners for student loans would be counterproductive to the goal of promoting broad access to education. Heads of low-income families are more likely to have poor credit histories and may not be willing to take on the additional liability of cosigning their children's loans. Older independent students, including displaced workers and displaced homemakers, could also be denied education if they cannot secure a cosigner.

Changes in the administration of the student loan programs have made it increasingly difficult for borrowers to escape their repayment responsibilities. The consequences of default are sufficiently burdensome and well publicized to discourage borrowers from treating their repayment obligations lightly. Additional default reduction measures targeted at borrowers are likely to reduce defaults only to the extent that they reduce access to higher education.

But there is another deserving target for the Congress to consider--poor quality education programs. Mounting evidence compiled by the Office of the Inspector General, the Senate and by our own program reviews suggests that some schools view their students as an inconvenient but necessary conduit to student aid funds. We have all heard about computer institutes which lack computers, cosmetology schools whose "classes" consist of using paying students as unpaid hairdressers, and business schools whose main order of business consists of processing student loan and grant applications. We feel that the goal of the Higher Education Act does not include enriching the proprieters of such schools at the expense of our borrowers.

Such school prey on those most in need of education -- highschool dropouts, the unemployed and recipients of public assistance. These schools return little of educational value in return for the tuition they charge. Their students too often are left with little but debt.

The SEAA would like to take a greater role in policing the schools which use our loan guarantee. However, with the loss of a large portion of our trust funds, which were confiscated by the U.S. Department of Education according to the provisions of the 1987 Budget Reconciliation Act, we lost our financial ability to bear the costs of extensive program reviews, particularly for out-of-state campuses. Similarly, in order to reduce its own operating costs, the U.S. Department of Education has curtailed federal level program reviews. We view this policy as penny wise and dollar foolish.

Before the loss of our financial reserves, the Virginia Education Assistance Authority performed program reviews every two years for every school and lender using our guarantee. Due to the loss of interest income from our trust fund investments, we have been forced to reduce our program reviews to those mandated by the federal government.

Our program reviews have been helpful in halting abuses among schools certified by the U.S. Department of Education. However, the requirement for reviewing only the top schools by dollar volume causes us to review primarily large state institutions which are generally well-run and responsible participants in the Title IV programs. The schools which we have found abusing the programs account for a relatively small portion of our overall loan volume, but a larger proportion of defaults.

The Virginia SEAA continues to perform program reviews for in-state schools when we receive complaints from students or when we detect a possibility of irregularities. This reactive approach to oversight it is not as effective as reviewing every school on a regular basis. It is far less effective than eliminating schools of questionable merit during the federal certification process.

Low-income borrowers are inherently at risk of default because they are less likely to complete their education programs. The default risk is compounded if the programs are of little educational value. Borrowers who attend shorter term programs are complaining with increasing frequency that such is the case.

Student loan defaults carry a significant cost to the federal budget. They carry an even greater cost to the many low-income students involved. These students have already tasted failure in their chosen school. By defaulting their student loans, borrowers loose the opportunity to try again while taking on the burden of a poor credit record. These costs, both human and budgetary, can be reduced if we do a better job of school oversight.

Guarantee agencies with ties to state departments of education are well positioned to evaluate the merits of schools operating within our state borders. However, we are provided with very little discretion in determining which schools located within our states are eligible to use our guarantee. Our influence is even more limited when we guarantee loans for out-of-state schools in order to accomodate regional lenders. In these instances, we have no influence over state legislatures or regulators to protect the interests of students and taxpayers. The increasingly regional banking environment will require that we expand our guarantee activities beyond the borders of our state if we are to maintain broad-based lender participation.

The SEAA and VELA urge the Department of Education to increase scrutiny of proprietary schools participating in Title IV programs. Should the Department decline this responsibility, we urge the Congress to provide us with greater latitude in withholding the use of our guarantee.

The collapse of HEAF also calls into question the wisdom of the 1987 Budget Reconciliation provisions which required some guarantee agencies to "spend down" their guarantee reserves. While the issue of establishing an adequate proportion of guarantee reserve funds to outstanding loans has taken on greater urgency, it is glaringly apparent that the GAO formula did acheive that goal.

The accounting firm of Touche Ross (now Deloitte & Touche) has developed a model which considers a number of variables in determining the adequacy of guarantors' reserve funds. The model considers the composition and default history of the existing portfolio, the operating expenses required to service new and previously existing loans, and the guarantee fees which should be charged in order to cover the default risks of the guarantor's present loan volume. Unlike the GAO formula, which was devised to reach a pre-determined budgetary savings of $250 million, the Deloitte Touche model is concerned with establishing the necessary reserves to operate a fiscally sound guarantee agency.

Mr. Chairman, the problems encountered by HEAF are not an indictment of the student loan programs. These programs are generally sound and provide a valuable service by financing the higher education of our nation. HEAF's downfall does point out some programmatic weaknesses that need to be resolved during the upcoming reauthorization of the Higher Education Act.

Thank You.

CITIBANK

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Stephen C. Biklen

August 14, 1990

The Honorable Paul Simon
United States Senate
462 Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Simon:

At the hearing before the Senate Subcommittee on Education, Arts, and Humanities on August 3rd regarding the Higher Education Assistance Foundation, you asked me for specific proposals regarding how the Department of Education might establish a process through which financial problems at guarantee agencies could be uncovered at an early date. The purpose of this letter is to provide you with our ideas regarding this subject.

CBA believes it would be relatively easy for the Department of Education to construct a computer model (several lenders already have these in existence) that could be used to forecast a guarantor's financial state based upon the input of key indicators from each agency. We would envision the process to work as follows:

- The Department of Education constructs or adopts a computer model to forecast the future financial state of each agency (both income statement and balance sheet).
- The Department of Education identifies key pieces of information to be collected from each agency on a quarterly basis. These would include such items as actual and projected volumes (broken down by school type), default rates, expenses, recovery rates, insurance premiums, etc.
- The Department of Education forecasts the projected results of an agency based upon the data received. At least two scenarios should be projected, one based upon a normal course of events and one based upon a worse case situation if no additional guarantees were made. (This would allow one to evaluate whether or not an agency could cover today's existing liabilities even if it closed down).

The Honorable Paul Simon
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Beyond establishing the above process, CBA believes it is important for the Congress, in conjunction with the Department of Education, to establish an orderly process to be followed in the event an agency does become insolvent. It is extremely important that this process include 100% guarantees for the holder of the loans.

I hope that the above information is helpful to you. We would be happy to work with either your staff or the Department of Education in implementing the above suggestions. If you or your staff have any questions or need additional information, please do not hesitate to contact me.

Sincerely,

Stephen C. Biklen

cc: Senator Claiborne Pell
Senator Nancy Kassebaum
Cheryl Smith
Craig Ulrich, CBA

Senator PELL. Thank you very much, indeed. I thank the panel very much for being with us. This winds up today's hearing. The hearing is adjourned.

I should add the record will be kept open for 5 days for questions.

[Whereupon, at 1:55 p.m., the subcommittee was adjourned.]

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