CFPB Report Shows Student Loan Rehabilitation Fails Many Borrowers

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More than One-Third of Borrowers Who Rehabilitate Federal Loans Will Default Within Two Years

(BOSTON) Today, the Consumer Financial Protection Bureau (CFPB) Student Loan Ombudsman released a report estimating that more than one-third of borrowers who rehabilitate their federal student loans will re-default within the first two years. It also found that over 220,000 borrowers who re-default on their loans could have had a $0 payment in an income-driven repayment plan.

“The CFPB report confirms one of our greatest fears – that the implementation of programs designed to help student loan borrowers may actually put them in a worse position,” said attorney Persis Yu, director of National Consumer Law Center’s Student Loan Borrower Assistance Project.

Loan rehabilitation is a program by which a federal student loan borrower is able to cure a loan default by making nine reasonable and affordable payments in a ten-month period. The catch is that, since 2008, borrowers are only able to rehabilitate their loans once. Therefore, borrowers who re-default will often be stuck in default indefinitely—with no further chance to get back on track and in good standing. These borrowers will experience the draconian consequences of default, such as wage garnishment, seizure of their tax refund (including their Earned Income Tax Credit), and offset of their Social Security benefits, potentially for the rest of their lives.

As NCLC wrote its 2014 report, Pounding Student Loan Borrowers, the U.S. Department of Education’s compensation system rewards its debt collectors for maximizing the dollars collected and for loan rehabilitations. In fact, when the Department fired five of its debt collectors last year for lying to student loan borrowers, it was for exaggerated claims about the benefits of loan rehabilitation.

“Debt collectors working for the Department of Education are paid a lot of money. The CFPB’s data suggests that the Department is paying over $1 billion to put a lot of borrowers in a worse position then when they started. That seems like a bad deal for the American taxpayer,” said Yu.

Debt collectors are required to provide borrowers with counseling about income-driven plans while rehabilitating their loans. Unfortunately, we do not have any data about the success rate of that counseling, nor will the Department release an unredacted version of the Private Collection Agency Manual so that we can see how it has instructed its debt collectors.

In a blog post released today, NCLC advocates renew their call on the Department to eliminate the use of private collection agencies and move toward a comprehensive and individualized counseling model for student loan borrowers in default.