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TESTIMONY

UNITED STATES HOUSE OF REPRESENTATIVES

COMMITTEE ON EDUCATION AND LABOR

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I thank Chairman Miller, Ranking Member McKeon, and the members of the Committee on Education and Labor for inviting me to speak this morning.

Background

Over the last few months my office has conducted an investigation into the student loan industry. In just the short time that the investigation has been ongoing, we have uncovered several significant, deceptive and illegal practices. Unfortunately, these practices are widespread throughout the country and throughout the many segments of the industry. These practices have affected hundreds of thousands of student borrowers and their parents.

It is easy to see why the results of this investigation have struck such a chord with the public. As the members of this Committee are well aware, the costs of higher education are soaring and have been for some time. Grant and scholarship funds have not kept pace with rising tuition. Accordingly, a significant and growing number of students and their parents turn to loans to cover what they otherwise could not afford. This is not just a problem in my state. Nationwide, two-thirds of all four year college graduates have loan debt. The student loan industry has swelled to become a greater than $85 billion per year industry.

In spite of the large number of students and families that the student loan industry affects, the procedures of applying for and receiving loans are enormously complex and confusing. Students and their parents are faced with a dizzying array of loan possibilities and hundreds of potential lenders from which to choose.

These parents and students, not surprisingly, often look to the educational institutions they are attending for advice. They trust that the institutions will give them unbiased guidance as to how to best finance their education. In response, many institutions of higher education have created lists of recommended lenders. In some instances, these Apreferred lender lists@ contain dozens of lenders that meet certain minimal requirements. In other cases, educational institutions use the lists to recommend a handful of lenders, or even a single lender, as Apreferred.@ The benefits to the lenders of being included on these lists are considerable. Lenders on preferred lender lists typically receive up to 90% of the loans borrowed by the institutions= students and parents. With this loan volume come vast profits for included lenders.

I am angered and saddened to say that our investigation has revealed an unholy alliance between lenders and many trusted institutions of higher education. The best interests of the lender and the institution, rather than the interests of the student, all too often have become paramount.

I will take the next few minutes to elaborate on a few of the troubling, deceptive and often illegal practices that we have uncovered.

Problems Uncovered

Revenue Sharing

What I believe to be the most egregious practice that we have uncovered so far is a form of kick-back scheme often referred to as Arevenue sharing.@ Revenue sharing is an arrangement under which a lender pays an institution of higher education a percentage of the principal of each loan taken out by a borrower at the institution. The practice of revenue sharing creates a potential conflict of interest on the part of the institutions of higher education. When and if the institutions direct students to lenders, the direction should be based solely on the best interests of the student and parents who may take out loans from the lenders. Because of these revenue sharing arrangements, however, the institutions have a financial interest in the student or parents selecting the revenue sharing lender, regardless of whether that lender offers the best rates and service for that borrower. The advice the students and parents sought from a trusted source may not be so impartial after all.

Preferred Lender Lists

As I mentioned before, many schools maintain preferred lender lists and encourage students to borrow from the lenders whose names appear on the lists. Despite the significant role that these lists play in determining the lenders from which students and parents borrow, many institutions have chosen not to inform their student and parent borrowers about the criteria used to formulate the lists of recommended or preferred lenders. In some instances, they have even gone so far as to actively conceal the methods by which their recommendations derive. Worse, some

institutions fail to disclose the potential and all too often actual conflicts of interest on the part of their financial aid offices B the same offices which compile the preferred lender lists. These conflicts of interest may arise from the revenue sharing arrangements I just described or from other perks or consideration granted to schools and financial aid employees, some examples of which I will describe in greater detail.

Improper Relationships Between Lenders and Financial Aid Offices and Administrators

Our investigation has uncovered potential conflicts of interest created by financial aid administrators who have held stock in a lender, having been encouraged to purchase the stock by a lender executive. In other cases, financial aid administrators have received payment for consulting with a lender. In several of these cases, the implicated lenders succeeded in getting themselves placed on the implicated administrators= schools= preferred lender lists.

Not all of the improper perks have been so egregious, but many have been exceptionally widespread. Many lenders have paid travel expenses and honoraria for financial aid officials to attend meetings and seminars in attractive locations often as part of an appointment of the institutions= financial aid officials to Aadvisory boards@ or Acommittees@ sponsored by the lenders.

We have also uncovered many examples of lenders paying hundreds of thousands of dollars for printing services at the request of financial aid officers. Some lenders have also sent their own staff to assist schools= financial aid staff on the schools= campus. The lenders did not offer

these services out of the goodness of their hearts. Similar to the revenue sharing arrangements, lenders granted institutions of higher education these types of benefits in an effort to encourage the institutions to steer students to the lenders.

In a related problem, lenders have agreed with institutions of higher education to staff Acall centers@ that answer students= telephoned or emailed questions regarding financial aid, loans and lenders. Often the call center employees have not only failed to identify themselves as employees of a lender, but have been instructed to answer the phone in the institutions= name. The student calling or emails their questions rightfully expected to receive disinterested advice and information regarding lenders. These lender call center employees, however, have an interest in advocating on behalf of the lender that pays them.

Denial of Choice of Lender

Our investigation has also brought to light a failure of some institutions of higher education to make clear that borrowers have a right to select the lender of their choice, irrespective of whether the lender appears on any preferred lender lists. In the most egregious cases, institutions have gone so far as to abrogate this right, by stating or strongly implying that the student and parents were limited to the lenders on the list, or even to a single lender. In this way the educational institutions steer borrowers to certain lenders, as with the other examples, not necessarily because that lender is best for the borrower.

Undisclosed Sales of Loans to Another Lender

Further, in many instances, institutions of higher education place several lenders on the institutions= lists of preferred lenders causing the potential borrower to think that the lender list represents a real choice of options. However, the choice is illusory when, as sometimes occurs, all or a number of the lenders on a lender list have arranged with each other to sell any loans to one of the lenders immediately after one of the other complicit lenders disburses a loan.

Quid Pro Quo AOpportunity Loans@

Deeply disturbing, too, was our discovery that lenders and colleges had, in many instances, entered into *quid pro quo* high risk, high interest loans that hurt students. Under these undisclosed agreements, often referred to as Aopportunity loans programs@ lenders agreed to make loans up to a specified aggregate amount to students with poor or no credit history, or international students, who the lender claimed would otherwise not be eligible for the lender=s alternative loan program. In exchange for the lender=s commitment to make such loans, however, the institution provided concessions or promises that prejudice other borrowers.

Solutions

Code of Conduct

Over the last few weeks, as my office exposed many of these practices to the light of day, I was pleased to see many lenders and schools that had engaged in some of the questionable and even illegal practices agree to change course and set a new standard for the industry. To that end, we have entered into numerous settlement agreements B with major lenders and schools alike B in which the schools and lenders agreed to adopt a new landmark Education Loan Code of Conduct, which will now govern those institutions= student loan practices going forward. The Code of Conduct offers institutions the guidelines many schools and lenders have actively sought and by which all schools and lenders should be willing to abide.

The Code of Conduct remedies the troubling and illegal practices we have uncovered. Specifically, the Code of Conduct prohibits revenue sharing and kickbacks in other forms, including printing services. It prohibits lenders from funding gifts and trips for institutions' financial aid employees. The Code prohibits lender staffed call centers. Our Code also lays out strong but fair guidelines concerning, among other things, preferred lender lists, advisory board compensation, and loan resale.

My office will continue to pursue lenders, schools, and other players in the student loan industry that fail to put students= interests first. In cases where the law has been broken, we will continue to demand that the responsible entity agree to cease the illegal practices, reimburse wronged

borrowers or pay into our education fund as appropriate, and agree to abide by the Code or Conduct. If not, we will sue.

State Legislation

But, to most effectively reform the student loan industry B and to restore most fully the broken trust between universities and lenders on the one hand and students on the other Blegislation is necessary so that these types of reforms come to **all** lenders and schools. I respectfully submit that it is crucial that Congress act promptly to end the conflicts, perks and revenue sharing that have been costing our students dearly. I ask you to move quickly to ensure that, as another group of high schools students look toward beginning their college educations in the fall, we have reform in place that will keep the students= interests paramount.

That is why I was so pleased to stand on April 16 alongside my state=s legislative leadership when we announced the introduction of state legislation that will codify and lend additional enforcement strength to the Code of Conduct. Our legislation addresses, on an industry-wide basis, the problems exposed as a result of my office=s ongoing investigation into the widespread conflicts of interest throughout the student loan industry.

National Action

The settlements into which we have entered in New York will affect millions of students and thousands of schools around the country. Recently, my office has entered into settlements involving other states= attorneys general. Most notably because of the leadership of Illinois

Attorney General Lisa Madigan and Missouri Attorney General Jay Nixon, we have been able to broaden the impact of our investigation by entering into settlements with multiple states simultaneously. The legislation we have proposed in New York will continue the reforms we began through our investigation and I hope other states will follow suit. We have certainly taken a major step in cleaning up a system laden with conflicts of interest.

Congressional Action Needed

Yet there is much more that needs to be done C and we must move without delay. That is where this Congress can play a significant role.

Part of the reason the practices we have uncovered have been able to flourish nationwide over the past several years is because the U.S. Department of Education has been asleep at the switch. The practices we have uncovered were not undiscoverable until now. Rather, the entity charged with maintaining the integrity of the student loan market failed. The failure of the Department to pass adequate regulations is disappointing and irresponsible.

Now is the time for Congress to act to affect change in this industry; an industry that until very recently has functioned without proper oversight. Congressman Miller and Senator Kennedy have both been extraordinary leaders on this issue for years. I believe that Chairman Miller=s Student Loan Sunshine Act will go a long way toward bringing the much needed disinfectant of sunlight to this tainted industry. I would encourage the Committee to ensure that the bill is ultimately brought to the floor of the House soon.

Conclusion

In closing, I urge Congress to enact the Student Loan Sunshine Act. Further, this Congress must ensure that the trust placed in educational institutions is warranted and that we end the pernicious effects of financial gain through the misleading of students and their families. The stakes are too high for too many Americans= futures for Congress not to act. I look forward to providing any assistance the Committee may require of my office to help achieve these goals.