This is US

How $10,000 of original student loan debt turned into a repayment scheme of 30 plus years

Between 1984 and 1987 Monica took out $10,000 in student loans. Over the next 30 years she made payments totaling over $24,000, yet she still owes more than $3,000 on her loans.

I first met Monica at a tax clinic in the early 2000s. As a CPA, I had been volunteering my time preparing tax returns pro bono on Saturdays during tax season. Monica and dozens of other taxpayers were waiting patiently to have their taxes prepared at this free clinic located at the Jersey Shore.

When it was her turn, Monica brought her completed interview/intake form to my workstation. I looked over the information she had provided and asked a few follow-up questions, including if she had any student loan debt.

She shifted in her seat and explained that she took out $10,000 in student loans when she was in college in the 1980s. She said that she has been doing her best to repay the loans since graduating, but wasn't really sure about how much she had repaid, how much of the principal she has knocked down, or how much she still owed. As a single person who rented, Monica needed all of the deductions to which she was entitled, so I encouraged her to get some specifics about her loans. She agreed to come back the following week with her student loan interest amount.

I've prepared Monica's taxes many times since that first meeting in the early 2000s. Each year, she provided statements from her loan servicers which reported student loan interest received. During the 2017 tax season, while preparing her return, I discovered that she was still paying down the original student loan debt she'd taken out 30-plus years earlier.

How could that be?

My curiosity piqued, and I asked Monica if I could perform a review of her student loan debt. A week later, she handed me a large and overflowing manila folder containing 30 years' worth of payments, loan documents, and servicer statements.

I dove into it with passion.

The following is a narrative on what I found (below narrative is summary recap of events by date, numbers are rounded):

1984 -1987: Origination of Student Loans

Monica attended a large public university outside New Jersey, graduating in the spring of 1987. In order to pay for tuition, housing, and other college costs, Monica obtained four (4) Federal Stafford FFEL loans for $2,500 each. All of the loans were fully subsidized.

What are FFEL Loans?

The Federal Family Education Loan program (FFEL) was a student loan program in which commercial bankers issued student loans directly to borrowers or colleges. FFEL loans are what the accounting industry calls "cash cows," a type of business investment which rewards investors beyond risk (initial investment costs) with liberal guaranteed payments and profitability. You see, FFEL loans were fully guaranteed by the government, including subsidized interest rates and administrative costs (called special allowance payments.)

FFEL loans issued to pay for qualified educational expenses began to earn interest from the date the loan was distributed to the borrower or school (date of origination). While the borrower is in college, interest accruing on subsidized FFEL loans is paid by the government directly to the lender. Since this interest is paid by the government, the borrower is only responsible for repaying the original principal balance upon graduation.

The FFEL program was terminated by President Obama effective July 2010. Federal student loans are now issued directly by the government to borrowers (or colleges) and are a part of the Direct Loan program.

December 1987: Graduation, Repayment Begins

Monica graduated from college in the spring of 1987. Once her six month grace period expired, her FFEL loans entered repayment.

Overview of Monica's student loan debt in 1987:

Term of note: 10 year, 120 monthly payments
Monthly payment: $127.00
Interest Rate: 9%
Principal: $10,000 (because interest while attending college was paid to the lender by the government)
Interest over loan term: $5,238.00.
Total repayment: $15,238.00
Grace period: 6 months
Repayment to begin: December 1987

Over the next two years, Monica made consistent monthly payments of <u>$127</u> directly to the commercial bank in New Jersey which originated the FFEL loans.

1989: Monica Gets a New Loan Servicer

In November 1989, the commercial bank notified Monica that the servicing of her loans was being transferred to the Student Loan Servicing Center (SLSC), effective January 1990. The principal loan balance at the servicing transfer date was $8,706.

The commercial bank reported student loan interest received for 1989 was $746.33.

1990 - 1992: Negotiating New Terms in Hard Times

Despite working two jobs, full-time for a local nonprofit during the day and waitressing at the local bar at night, Monica had problems meeting her repayment obligations. She fell behind on the $127 monthly payments and approached her servicer for help.

In July 1991, Monica signed a new note with SLSC (replacing her original loan note) for 90 monthly payments of her loans at 9% interest. Her new monthly payments were $136. The principal at note date was $8,148 plus accrued interest of $368 (for periods when she was unable to make payments interest was still being charged). With the interest capitalized (added to principal), her new principal balance totaled $8,516 ($8,148 plus $368.)

1993 - 1995: Struggles and Forbearance

Over the next three years, Monica continued to work at least two (and sometimes three) jobs. Despite her hard and tireless work, she still struggled to make her loan payments. During these years, Monica's housing and transportation costs accounted for more than 50% of her income. She had very little left for discretionary purchases and the payment of student loan debt.

In November 1994, SLSC accelerated the loan due to nonpayment. The principal balance at acceleration was $7,325 plus accrued interest of $375. The interest was capitalized, bringing the principal balance to $7,700.

In direct response to this move, Monica requested forbearance. Forbearance is a tool that allows student loan debtors to pause their payments for a short period of time. While payments are not due, the interest on the loan generally continues to accrue. As a result, the balance due will be greater after forbearance. SLSC agreed to grant a six-month forbearance, giving Monica a little bit of breathing room.

In January 1995, Monica signed a new note with SLSC. Under the new deal, Monica would be required to pay 63 monthly payments of $154 at 9% interest. The principal of the note at signing was $7,325 plus accrued interest of $495, which came to a grand total of $7,820. Monica would begin payments in April 1995.

1996 - 1998: Increased Cost of Living Leads to Default

Over the next two years Monica did her best to make payments each and every month. Unfortunately, her cost of living and transportation increased, continuing to swallow more than half of her monthly income. As a result, Monica skipped or delayed payments on her $154 plan.

By August 1997 - ten years after graduation - Monica's FFEL loans had been purchased by the NJ Higher Education Student Assistance Authority (NJHESAA). SLSC (the loan servicer) denied her request for economic hardship relief during forbearance which would have allowed the forbearance period to be interest free. Principal balance in August 1997 was $5,187.

[The NJ Higher Education Student Assistance Authority is a State agency which administers NJ CLASS loans (private student loan debt* originated through the sale of bonds to investors) and, as investments, maintains large quantities of purchased FFEL loans in their portfolio. As of 6/30/17, NJHESAA's FFEL-owned loans totaled almost $2 billion.]

*The Federal Reserve categorizes any loan that is not a Title IV loan as private. Title IV refers to the Higher Education Act of 1965 and amendments.

One month later in September of 1997, after SLSC granted forbearance through April 1998, Monica signed yet another note with SLSC. The terms of the new note included 38 monthly payments of <u>$173</u> at an interest rate of 9%. Principal balance was $5,187 plus accrued interest of $520 which was capitalized, bringing repayment of principal to $5,708. Payments were to begin May 1998.

1999 – 2003: Default and Rehabilitation

Over the next 2 years, Monica struggled to make the increased loan payments. Remember, her original monthly payment equaled $127. More than a decade later, her monthly student loan commitment had jumped to $173. Despite working 60 hours a week, Monica's yearly income rarely exceeded $25,000. In addition to struggling to keep up with the rising cost of living, Monica endured a series of medical catastrophes. As a result, she fell behind on her payments and defaulted in early 2000. NJHESSA told Monica that her only recourse was to "rehabilitate" the loans.

Default

Default of federal loans occurs when payment has not been made (or acknowledged by the lender) for more than 270 calendar days. Default causes the loan to be subject to higher interest rates, collection, and late fees. Collection costs for Monica's loans were 18.5%.

Rehabilitation

Rehabilitation is a process where the borrower must prove they can bring the loans current by making consecutive monthly payments over no less than a 10 month period. Most often payments are determined by calculating 15% of borrower's discretionary income. None of the rehabilitation payments are applied to reduce principal, but instead are used to pay for collection costs, fees, and interest.

In late 2000, Monica entered the rehabilitation program. After a year, she was notified by the guarantor, NJHESAA (who owned the FFEL loans), that her rehabilitation was completed and her loans had been referred to Sallie Mae for servicing. Principal at completion of rehabilitation was $5,282 plus accrued interest of $338 plus collection and late/collection fees of $1,076 (both of which were capitalized) brought the new loan principal balance to $6,697.

Monica signed a note with Sallie Mae for 104 monthly payments at <u>$86</u>.

By February 2003, Monica continued struggling to make payments on the latest note. She was still working on paying off medical debt including a lot of dental work. Housing and transportation costs exceeded 60% of income. She requested and was granted a forbearance of 12 months.

2004 - 2007: Request for Consolidation

Monica's most recent forbearance ended in early 2004. At this point in time, housing and transportation costs still accounted for more than 60% of Monica's income, and she was still trying to dig herself out of the debt caused by her medical catastrophes. Adding to this burden, she encountered large veterinary bills for her dog. As a result, Monica could not keep up with the new payment plan and became seriously delinquent.

In 2006, Monica contacted NJHESAA and requested to have her loans consolidated. She completed the Direct Loan Consolidation application, (complete with loan detail, personal information, and references) and submitted it to the Direct Loan Consolidation center. If the loan consolidation were approved, Monica's loans would only be subject to 8% interest. She received a postcard informing her that her application had been received on 06/22/2006. Loan balance at June 2006 was $9,436 (18 years after graduation, her principal balance was almost as much as the original loan amount of $10,000.)

There is no evidence her application for loan consolidation was ever processed and/or approved.

[If Monica's loans had been consolidated, they would no longer be the cash cow FFEL-guaranteed loans. This may have been a deterrent to consolidation by the loan holders.]

By February 2007, Monica was notified by NJHESAA that her loans had again defaulted. They threatened garnishment of her wages. Monica agreed to a voluntary repayment arrangement of <u>$112</u> a month over a 10 month period which required direct deduction of the payments from her bank account.

NJHESAA Form 1098-E for <u>2007</u> reported "defaulted FFELP loan" interest received of $972.87.

2008 – 2010: Struggling to Find a Solution

In March of 2008, after completing the second rehabilitation** program of her loans, and 20 years after graduating from college, Monica entered into another repayment agreement with loan servicer AES, agreeing to monthly loan payments of <u>$95</u>.

[**According to studentaid.ed, prior to 2008, defaulted federal loans could only enter rehabilitation once. After receiving the notice from NJHESSA reporting her loans in default and threatening wage garnishment, Monica "volunteered" to make 12 monthly payments of $112.]

NJHESAA Form 1098-E for <u>2008</u> reported "defaulted FFELP loan" interest received of $633.48.

Between 2008 and 2010, Monica attempted to make monthly payments of $95. She was granted several periods of forbearance. In September 2010, AES notified Monica that her most recent forbearance had ended.

NJHESAA Form 1098-E for <u>2009</u> reported "defaulted FFELP loan" interest received of $580.77.

In September 2010, principal balance was $6,211, plus accrued interest of $1,000 (during forbearance) which was capitalized, resulting in new principal balance of $7,209. Housing and transportation costs continued to hover around 55% to 65% of income. Old and new medical and dental bills exceeded $1,000.

NJHESAA form 1099-E for 2010 reported "defaulted FFELP loan" interest received of $225.86.

2011 – 2016:

Monica's income stabilized a bit, and she was able to make monthly payments of $95.

2017 – 30 Years After College Graduation

By January 2017, a statement issued by loan servicer AES reported principal balance at $3,208.

Postscript

As of January 2017, according to servicer statements, almost thirty years after college graduation, Monica still owed over $3,000 on her original student loans. Along the way, she'd made over $24,000 in payments. The loans were not consolidated, although she tried to do so to lock in a lower interest rate.

Her New Jersey refunds were levied for over a decade and seized by NJHESAA. Additionally, her tenant homestead rebates were also seized. Total amount of income tax refunds or homestead rebates taken by NJHESAA, exceeded $1,000.

Student loan payments are applied as follows:

1. First to late charges, fees, and collection costs,
2. Second to outstanding interest, and
3. Last to reduce principal.

During forbearance, because interest does not stop accruing, when payments were not made, or if payments were less than amount to pay accrued interest, the principal balance increased. When a borrower is seeking forbearance for FFEL subsidized loans claiming economic hardship, application must be made and approved by the loan servicer. Monica made application for economic hardship in 2007 but it was denied by the servicer.

Student loan borrowers should be aware of the daily interest cost of their loans. This is important because if payment is made for less than the daily amount, principal will never be reduced. At the beginning of Monica's repayment journey in 1987, her *daily* interest cost on the (4) FFEL loans with a principal balance of $10,000 at 9% was $2.50. Per day. So she needed to pay at least $75 ($2.50 times 30 days) per month in order to satisfy the interest accrued and due *before* payment would be applied to principal. The daily interest rate decreases with each payment, *assuming* interest has first been fully satisfied.

Federal student loans are exempt from most consumer protections (Fair Debt Collections Act, Truth in Lending, Statute of Limitations), are excluded, for the most part, from oversight by the Consumer Financial Protection Bureau, and are dischargeable in bankruptcy only under the most dire of circumstances (you have to meet the Brunner test proving harm and undue hardship). Collection costs are punitive and enormous and add to an already unbearable repayment burden.

Monica, like most students entering college right after high school, was a teenager when she signed her student loan contracts. It is apparent she had no idea what kind of indenture she'd "agreed to." This can be said for the majority of student loan borrowers.

Financial education at the high school level is seriously lacking, if existent at all. Student loans are originated between borrower (student) and lender without much scrutiny, oversight, awareness, or repayment considerations (seriously, what sane person could have thought up this repayment scheme?)

Over the past decade, through tax preparation work – both pro bono and paid - I've seen many student loan borrowers who, like Monica, have struggled not only to make ends meet, but also try to understand what's happening with regard to their student loans. I've watched as refundable credits in the thousands of dollars have been seized by federal and state agencies year after year to pay for student loan debt. Many low-income taxpayers who took out debt decades ago and who have tried to pay this debt back, find – with accrued interest and collection fees - they owe much more than the original loan amount. Those who qualify for tax credits earned for dependents, education, or economic qualifications (refundable child tax credit, education, and earned income tax credits), never see the refunds which could have helped with housing, utilities, and child care. Instead the money is siphoned off into a vat of pots to pay for bloated collection costs, fees, interest, and most likely never touching principal. It is a cycle that can last decades, is rarely broken, and often without any reconciliation of seized funds.

This past tax season I prepared the return for an 80 year old man who came into the tax clinic. He handed me his W-2 form which reported wages of $500 and a Social Security statement. He needed to file a tax return to obtain a refund of federal and state withholding reported on the W-2. While reviewing his Social Security statement, I noticed one-third of it was garnished. When I questioned him about this, he became very solemn, put his head down, and explained it was for an education loan taken out for his daughter "some time ago" to help her attend college. She had since died. Piecing together what he told me, I figured he took out a federal Parent Plus loan, had defaulted (before, during, or after his daughter's illness and death) and didn't know what to do. The default resulted in the garnishment of his Social Security, most likely without end for the rest of his life. There isn't even an accounting of what is taken each year.

Without basic consumer protections, financial education, understanding, or advocacy, and absent the ability to discharge in bankruptcy, the contracts Monica and other borrowers enter to secure loans to help fund higher education are heavily lopsided in favor of lenders, investors, and loan servicers.

I question, as required by the basic principles of contract law, whether there is even a meeting of the minds between borrower and lender. Additionally, there seems to be some amount of unconscionable favor on behalf of one party over the other.

Student loan debt has topped $1.3 Trillion. By entering into these cumbersome, confusing, complicated, non-transparent contracts, the US has been devouring its citizens- young and - old in a cruel system of endless servitude.

Recap of events by date

Notes	Original Principal	Principal paid	Principal after reduction	Accrued interest which was capitalized	FEES including REHAB fees	New Principal
Original Principal	**10,000**	-	-	-	-	**10,000**
11/15/89 Commercial bank contracted SLSC to process payments	-	1,294	8,706	-		**8,706**
07/05/91 signed repayment note with SLSC - 90 @ $136.06	-	558	8,148	368		**8,516**
11/26/94 SLSC accelerates loan	-	1,191	7,325	375		**7,700**
12/18/94 borrower requested forbearance 6/1/94 - 3/1/95						
01/06/95 signed repayment note with SLSC - 63 @ $154.36. Payments begin 04/01/95	-	375	7,325	495		**7,819**
08/08/97 NJHEAA reports loans delinquent						
08/12/97 SLSC denies economic hardship request						
08/12/97 SLSC statement of principal balances	-	2,632	5,187			**5,187**
08/17/97 SLSC reports forbearance expires 04/30/98						
03/03/98 signed repayment note with SLSC - 38 @ $173.38. payments begin 05/01/98	-	0	5,187	520		**5,708**

09/29/00 NJHEAA notice - statement of account	-	425	5,282	338	1,076	**6,697**
01/17/02 NJHEAA notice rehab is complete and loan has been purchased by Sallie Mae (who writes **"Congratulations!")**						
01/17/02 Sallie Mae notice change in payments - 104 @ $86.20	-	488	6,209	2		**6,211**
02/21/03 borrower requests forbearance 12 months						
06/16/06 Borrower requested direct consolidation of 4 loans at 8% interest, 120 mos @ $115.			6,211	2,076	1,149	**9,436**
03/20/07 NJHESAA signs note for auto debit from bank @ $115 month						
09/02/10 - AES statement	-	3,225	6,211	998		**7,209**
12/08/10 - AES statement	-	130	7,079			**7,079**
12/28/13 - AES servicing deduction of $95.21 per month	-	1,790	5,288			**5,288**
08/07/16 - AES statement	-	1,812	3,476			**3,476**
10/07/16 - AES statement	-	233	3,243			**3,243**
01/07/17 - AES statement	-	215	3,028			**3,028**

TOTALS		14,370		5,173	2,225

Original principal 10,000

Interest added to principal	5,173	
Collection fees added to principal	2,225	
Revised principal increase over 30 years		17,398
Principal paid	14,370	
Principal balance January 2017	**3,028**	

RECAP

Total paid over 30 years Dec 1987 thru Jan 1997

Paid toward principal	14,370
Paid toward interest	9,710
TOTAL PAID TOWARD LOAN	**24,080**

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