the institute for college access & success

PROTECTING THE COHORT DEFAULT RATE FROM FORBEARANCE ABUSE

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Holding colleges accountable for unacceptably high default rates through the cohort default rate (CDR) has successfully driven down student loan defaults. However, evasion of CDR accountability through abuse of forbearance options – which temporarily suspend payments but may serve to delay rather than prevent defaults – harms borrowers and undermines the meaningfulness of the CDR metric. Policymakers must take action to strengthen the CDR against forbearance abuse.

The CDR has worked to reduce student loan default.

The CDR is the federal government's most longstanding student debt outcome measure, tracking how often students experience the single most devastating student loan repayment outcome: default. By tying high rates of default to schools' eligibility for federal financial aid, the CDR remains critical for ensuring schools do not consistently leave significant shares of their students at high risk of default shortly after leaving school. Holding colleges accountable for their CDRs has effectively reduced students' risk of default, as colleges take steps to meaningfully lower their CDRs without limiting access to federal loans.

Forbearance is a valuable repayment relief option for federal student loan borrowers, but when misused it can increase the cost of a loan and delay rather than prevent default.

Forbearance allows federal student loan borrowers to temporarily postpone loan payments without becoming delinquent, an important protection for borrowers facing temporary financial hardship. However, misuse of forbearance through consecutive or long-term periods in forbearance, during which financial hardship persists, is at odds with the purpose of forbearance in providing short-term relief. Interest continues to accumulate on loans in forbearance, and any accrued interest is capitalized (added to the principal loan balance on which future interest is calculated) upon exiting forbearance. Under the Higher Education Act, forbearance is intended for the benefit of the borrower, as balances can grow unnecessarily and put borrowers at risk of defaulting in the future on an even larger loan balance. A related problem of loan servicers allegedly overusing forbearance demonstrates that the cost of forbearance can add up: A 2017 Consumer Financial Protection Bureau complaint filed against the loan servicer Navient identified a collective $4 billion in interest charges arising from borrowers' multiple consecutive periods of forbearance over the course of five years.[1]

Some colleges evade CDR accountability by exploiting forbearance options.

The CDR holds schools accountable for borrowers who default within three years of leaving the school and entering repayment. It is widely documented that some default management firms employed by some schools steer borrowers at risk of default into extended periods of forbearance during this three-year window.[2] Although longer-term repayment relief options like income-driven repayment would meaningfully reduce struggling borrowers' default risk,[3] long-term forbearance can increase risk to borrowers and permit schools to evade the established system for holding colleges accountable for leaving students at high risk of default.

Although default rates among a group of students can be expected to increase over time, a particularly large spike shortly after the three-year CDR window may indicate troubling patterns of forbearance abuse, as attempts to place borrowers in forbearance are abandoned after the measurement period ends. Longer-term default rate data suggest concentrations of forbearance abuse among a subset of colleges.

- 50 schools had default rates that increased more than threefold between three and five years after their borrowers entered repayment in fiscal year 2012. At these 50 schools alone, the default spikes represented an additional 9,100 defaulting borrowers.
- More than two-thirds (70%) of these 50 schools saw rates increase by at least 20 percentage points between the third and fifth year of repayment.[4]

How to protect the CDR from forbearance abuse:

Ensure that forbearance is for the benefit of the borrower, not the schools.

Section 428(c)(3)(B) of the Higher Education Act specifies that contracts with student loan servicers "may, to the extent provided in regulations of the Secretary, contain provisions that permit such forbearance *for the benefit of the student borrower* as may be agreed upon by the parties to an insured loan and approved by the insurer" (emphasis added). The Department of Education should strengthen regulations by specifying that certain types of forbearance patterns — such as back-to-back forbearances — are rarely to borrowers' benefit, and should require that schools and servicers document the reasons why an additional forbearance is the best solution for the borrower. This rule modification recognizes the importance of forbearance as short-term relief but prioritizes solutions better suited for longer-term periods of financial hardship.

Publish five-year default rates in the interest of transparency, in addition to the three-year rates used for accountability.

Although the government has a strong interest in holding colleges accountable for high risks of default occurring relatively quickly after entering repayment, longer-term default rates are critical for identifying where forbearance abuse may be delaying, rather than preventing, defaults. However, these data are not routinely publicly available. The Department of Education should routinely calculate, review, and publish five-year cohort default rates.

Target program reviews or other investigations at colleges with significant increases in default rates after the three-year window closes.

Spikes in a college's default rate outside the three-year accountability window should trigger enhanced federal oversight. As part of a program review or investigation prompted by these data, the Department of Education should determine whether the school has promoted the use of forbearance and, if so, whether it has documented that forbearances are provided for borrowers' benefit. Investigations could also be triggered by high rates of borrowers enrolled in consecutive forbearances, as identified through more routine data analysis, program reviews, and audits.

For more information on forbearance, see the Department of Education's information page.

For more on who defaults and why, read *Casualties of College Debt*.

For more on how to strengthen the cohort default rate, read *Driving Down Default*.

Endnotes

1. Consumer Financial Protection Bureau. January 18, 2017. "CFPB Sues Nation's Largest Student Loan Company Navient for Failing Borrowers at Every Stage of Repayment." https://bit.ly/2PiZ0Ic.

2. Velez, Erin Dunlop, Austin Lacy, and Johnathan Conzelmann. March 2019. "Are For-Profits Manipulating Cohort Default Rates? How Student and School Characteristics Are Related to the Timing of Default." RTI International. http://bit.ly/2qoNfWD; United States Government Accountability Office (GAO). 2019. Federal Student Loans: Actions Needed to Improve Oversight of Schools' Default Rates (GAO-18-163). http://bit.ly/2NMEhux; United States Senate Committee on Health, Education, Labor and Pensions. 30 July, 2012. "For Profit Higher Education: The Failure to Safeguard the Federal Investment and Ensure Student Success." http://bit.ly/2NPbsxA; United States Department of Education Office of Inspector General (ED-OIG). 2003. Audit to Determine if Cohort Default Rates Provide Sufficient Information on Defaults in the Title IV Loan Programs (ED-OIG/A03-C0017). http://bit.ly/34xDLaf.

3. See, for example, Holger M. Mueller and Constantine Yannelis. 2017. "Students in Distress: Labor Market Shocks, Student Loan Default, and Federal Insurance Programs." NBER Working Paper No. 23284. http://bit.ly/32iqKjm.

4. TICAS analysis of data obtained by the Center for American Progress through a Freedom of Information Act request. Data are available at https://ampr.gs/2JUowjM. Calculations exclude four schools where five-year default rates remained below five percent.