

January 26, 2023

Via Email to Regulations@dbo.ca.gov

Araceli Dyson, Regulations Coordinator

CC: Senior Counsel Mary Tomé at mary.tome@dfpi.ca.gov

California Department of Financial Protection and Innovation

RE: PRO 06-21 - Notice of Modifications to Proposed Regulations Under the Student Loan Servicing Act

Dear Ms. Dyson:

We appreciate the opportunity to submit comments related to PRO 06-21 - Notice of Modifications to Proposed Regulations Under the Student Loan Servicing Act.

We also appreciate the continued efforts by the California Department of Financial Protection and Innovation (“DFPI” or the “Department”) to provide additional legal clarity for those groups providing funding to students utilizing income-contingent, income-indexed forms of financing, such as ISAs. We are confident that the DFPI is well suited to balance student protection concerns with the need for innovative financial tools to assist students in financing post-secondary education.

The following are suggestions related to the revised proposed regulations:

Clarify PEL reference in definition of “education financing product”

In the definition of "education financing product", there is a reference to "private education loans" without further definition or a citation. Based on the definition of "private student loan" later in the definitions, we believe “private education loan” in this context is meant to be defined using the Truth in Lending Act (TILA) definition for “private education loan”. However, it would be helpful to clarify that the use of “private education loan” within the rule should be interpreted based on the TILA definition.

Defining income for reporting purposes

The regulation lays out a definition of income and then requires ISA providers to report income based on that definition. There are two issues we wish to raise with this approach:

(1) Some programs have a definition of income that is narrower than what is provided in this definition, so they may not have data on all the sources of income specified here.

(2) It is unclear if the definition of income includes income derived by an individual from any trade or business carried on by such individual where compensation is in the form of dividends, profits, or rental income.

With these two issues in mind, we suggest a definition that does not specifically define “income”:

“Income’ means a Borrower’s income (or that portion of the borrower’s income that is less than the full income) that is used by the licensee in calculating the borrower’s obligations under the income share agreement.”

However, if DFPI is concerned about making sure that certain types of income are excluded from coverage under an ISA, we would prefer that DFPI use the language above but separately articulate the types of income to be excluded.

Finally, if DFPI would prefer to keep a prescribed definition of income, we suggest the following:

“Income’ means a borrower’s gross compensation from all sources, including but not limited to salary, wages, bonuses, commissions, vacation pay, gratuities, and self-employed earnings, but excludes passive income that is not derived as a result of borrower’s active participation in any trade or business. To the degree an ISA provider excludes certain types of income within this definition, those exclusions would not be considered income for the purpose of those private student loans.”

This distinction mirrors how the IRS Topic No. 425 (Passive Activities) handles passive income.

Include payment contingency and a maximum duration as part of the definition of an ISA

We appreciate the Department’s revision of the definition of an ISA to capture contracts that may have a payment obligation that is not structured as a percentage of an individual’s income. We suggest that the Department also incorporate two additional elements critical to capturing and distinguishing ISAs from traditional student loans.

First, payment contingency is an important element of an ISA. Even if an individual’s payment obligation is not calculated as a percentage of income, it is critical that the amount be determined by the individual’s income – at a minimum through the inclusion of an income threshold. This is a critical element of the contingency and protection afforded by an ISA. But the existing text (“agrees to... an amount of the student’s future income”) fails to explicitly state that the payment is contingent on income. To address this, we suggest the following revision to the definition in the proposal:

*“Income share agreement” or “ISA” means an agreement between a student and a school or an income share agreement provider under which the student agrees to **make payments calculated based upon and determined by** ~~pay a percentage or amount of~~ the student’s future income for the payment term, in exchange for the school or income share provider advancing, covering, crediting, deferring, or funding the cost of some or all of the student’s postsecondary education and costs of attendance at a postsecondary institution, including but not limited to tuition, fees, books and supplies, room and board, transportation, and miscellaneous personal expenses.*

Second, we believe a maximum duration is a fundamental component of a contingent contract because it creates an end point after which a student’s obligation is complete regardless of the

amount paid. We suggest that DFPI add an additional requirement to the ISA definition stating that *“there is maximum payment duration after which the student’s obligation is complete regardless of the amount paid by student to the income share agreement provider or school (as long as the student has paid any prior amounts due).”*

Because the ISA definition references a “payment term,” it is possible to include such language in the “payment term” definition, if DFPI would prefer that approach:

*“Payment term’ means the payment window or maximum period of repayment obligations under an income share agreement or other written agreement evidencing an education financing product, **after which the student’s obligation is complete regardless of the amount paid by student to the income share agreement provider or school (as long as the student has paid any prior amounts due).**”*

Where a loan has a fixed principal balance plus interest that accrues—but is still payable based on earnings but without a maximum duration—we believe that is a traditional loan. In contrast, an ISA creates a payment obligation that is contingent on future income and provides students with a maximum duration that does not require them to pay back a fixed amount to end the obligation.

Clarify payment cap definition to explicitly include caps based on an APR

The definition of "payment" cap" says "the maximum amount payable under an income share agreement, which may be expressed as an amount or a multiple of the amount advanced, covered, credited, deferred, or funded, excluding charges related to default." Some ISA providers use a cap that is based on an APR. We would suggest that the definition states explicitly that a payment cap can be expressed as an APR cap as these can provide material student protections.

Clarify “contract and delivery schedules” language

In section 2043, for clarity, are the "contract and delivery schedules" a single series of schedules as opposed to requiring the retention of the contracts themselves and separately the delivery schedules? We are also unclear what the term "contract" is referring to and would appreciate DFPI providing additional guidance.

Thank you again for this opportunity to comment. We welcome any questions you may have regarding this submission.

Sincerely,

Better Future Forward, Inc.
Jobs for the Future
Stride Funding Inc.
Social Finance, Inc.