



- Difficulty in obtaining employment upon graduation.
- Low quality education and services.
- Lack of adequate OE staff to review participating schools and lenders.

We are currently conducting a survey of proprietary vocational-technical school participation in OE's Guaranteed Student Loan program. We also plan to examine OE's policies and procedures for recognizing accrediting agencies.

The Guaranteed Student Loan program consists of a State or private nonprofit agency insurance program and a Federal Insured Student Loan program. The latter provides loan insurance for students or lenders who do not have access to State or private nonprofit programs. Colorado students and lenders are insured under the Federal Insured Student Loan program.

Our responses to your specific questions follow:

"(1) Are the above-mentioned lending institutions exercising 'due diligence' in collecting loans?"

OE has not issued specific criteria for determining "due diligence" in collecting loans and, therefore, it is largely a matter of individual judgment. Both the Labor Finance Industrial Bank and the Denver Industrial Bank essentially follow the same collection procedures. (See enc. II for a detailed description of these procedures.) There was no evidence that any loans had been made by the Denver Automotive Institute, now known as the Denver Automotive and Diesel College, Inc., and all loans made by Parks School of Business, Lear Siegler, Inc., had been transferred to the Labor Finance Industrial Bank before April 1971.

We selected several collection files for default claims from both banks and reviewed the collection procedures followed. With the exception of requesting preclaims assistance, 1/ both banks were following

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1/OE provides lenders with collection assistance on delinquent loans after the lenders have exhausted their own collection procedures but before the lenders' submit a claim to OE. Such preclaims assistance normally consists of sending a mailgram to the student borrower.

their stated procedures and appeared to be making a reasonable effort in collecting loans. Our response to question 4 discusses the banks' use of preclaims assistance.

Both OE headquarters and regional office officials believed that the banks were making a reasonably adequate effort to collect defaulted loans before filing claims. One official stated that these banks appeared to be making more of an effort to collect loans than some other lenders.

"(2) Are the default rates for the above-mentioned lending institutions higher than average for this program? If so, why?"

Applicable records at the two banks showed a claims rate <sup>1/</sup> of 16.6 percent for the Labor Finance Industrial Bank and 15.1 percent for the Denver Industrial Bank. The records did not distinguish between claims arising from defaults and those due to bankruptcy, death, or disability. These rates are based on the total dollar volume, as of October 31, 1973, of loans in repayment status and claims for reimbursement which have either been collected or are pending. All loans by both banks were made to students attending vocational-technical schools.

Because of certain reporting problems, comparable default or claim rates for the total Guaranteed Student Loan program or for all participating vocational-technical schools were not available from OE. Therefore, we could not make a realistic comparison. OE officials stated that the best estimate available as of June 30, 1973, for the overall default rate for all participating institutions was about 5.7 percent and that this figure was probably understated. Information provided by OE indicates that default and claim rates for vocational-technical school students are higher than the overall estimate.

"(3) Is there any indication that the default rate is higher because the drop-out or attrition rate is higher?"

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<sup>1/</sup>Includes reimbursement to lenders for bankruptcy, death, and disability, as well as payment defaults.

The banks' records generally did not indicate whether or not a student, on whose loan a claim for reimbursement was filed, had completed a course, nor did they identify the student's school. Information obtained from the three schools named in your letter showed the following percentage of dropouts among those students with federally insured loans and those without such loans:

	<u>Insured Loans</u>	<u>Non- insured Loans</u>
	(percent)	
Airline Training School, Inc. (now the Airlines School of Travel and Tourism)	23	35
Denver Automotive Institute (now the the Denver Automotive and Diesel College, Inc.)	31	16
Parks School of Business	27	60

The Airlines Training School percentages are based on student enrollment in courses offered between June 1972 and June 1973; the other percentages are based on classes graduating in August and September 1973. Information was not available for comparing average dropout rates nationwide for all schools or for a particular category of schools, such as vocational-technical.

Records maintained by the Labor Finance Industrial Bank showed that, from the start of its student loan program on April 1, 1971, through April 30, 1972, the claims rate for the above three schools was as follows:

Airlines Training School, Inc.	1.6%
Denver Automotive Institute, Inc.	7.8%
Parks School of Business	9.8%

The Denver Industrial Bank had not made any insured student loans as of that date. Because of the banks' subsequent changes in recordkeeping, it was impracticable to determine more recent default or claim rates for individual schools.

We cannot conclude, on the basis of the above information, whether or not a correlation exists between default and dropout rates. OE and other Federal and non-Federal groups studying the program have concluded that such a correlation exists where schools do not make timely and adequate refunds to students who fail to complete their courses.

"(4) With what frequency, if at all, are the above lending institutions making use of the HEW/OE preclaims collection assistance?"

Historically, OE has not maintained records on individual lenders' use of preclaims collection assistance, and this information was not available at the banks. During our review of a selected sample of lender default claim files, however, we noted that preclaims assistance had been requested by Labor Finance Industrial Bank and Denver Industrial Bank on 50 percent and 65 percent of the sampled claims, respectively.

An official who represented both banks informed us that, unless otherwise instructed by OE, preclaims assistance is always requested. He stated that OE had, at times, temporarily suspended this service when it fell behind in its work. We reported such a suspension to the Secretary of HEW in a letter dated November 30, 1973. OE quickly responded to our report and restored this service. Additionally, OE is testing a system modification which should enable it to determine which lenders are requesting preclaim assistance.

"(5) Are the above-mentioned lending institutions following applicable procedures in pledging, transferring or discounting loans?"

OE's manual and contracts of insurance with lenders provide that the restrictions on pledging and discounting student loan notes apply only to educational institutions who are also lenders. The only educational institutions you mentioned that were also eligible lenders were the Denver Automotive Institute (now Denver Automotive and Diesel College, Inc.) and Parks School of Business, Lear Siegler, Inc. As previously mentioned, neither of these institutions had loans outstanding or were making loans at the time of our review.

OE's manual also prohibits educational institutions from paying points, premiums, or additional interest to an eligible lender for (1) securing funds for loans or (2) inducing lenders to make loans to students of a particular category or attending a particular institution. According to the manual, prohibitions include, but are not limited to, outright dollar payments for each loan made, compensating balances as a condition to making loans, and any kind of secondary financing involving the sale of services to the school.

After arranging for a loan students may acknowledge receipt of loan proceeds by signing a voucher instructing the bank to pay the proceeds directly to the school. Neither of the banks we visited were remitting total

proceeds to the schools at the time a loan was made. Instead, the proceeds were recorded on the banks' records as unremitted voucher proceeds due the schools (accounts payable). Payments were made periodically or when the school requested them. The approximate average balances in the unremitted voucher proceeds accounts for the 10-month period ended October 31, 1973, were as follows:

Labor Finance Industrial Bank	\$10,317,000
Denver Industrial Bank	\$ 788,000

OE, in a letter dated October 31, 1973, informed HEW's Office of General Counsel of this practice and questioned the legality of OE paying interest to the banks on these loans before the funds were disbursed. The Office of General Counsel replied March 21, 1974, that, on the basis of facts reported in the memorandum, these billing practices per se did not appear to violate applicable regulations pertaining to interest. It said, however, that it would seem appropriate to treat these procedures as a prima facie violation of the prohibition of the payment of points, premiums, or additional interest by a school to a lender. The General Counsel's reply further stated that the schools would appear to have no reason to allow funds to which they are supposedly entitled on demand to remain in non-interest-bearing limbo for long periods of time except to induce the banks to make loans to their students.

We were informed that, as of August 5, 1974, both banks were still following this practice. OE plans to take corrective action and will inform us of the results.

OE's manual for lenders states that student loan notes may be sold or otherwise transferred only to other eligible lenders and only at par value. Our tests showed that both banks were adhering to this requirement.

"(6) Are the above-mentioned lending institutions' practices of pledging, transferring, or discounting loans in keeping with the letter or the intent of the law?"

The legislation which authorizes and governs the Federal Insured Student Loan program does not contain specific restrictions on pledging, transferring, or discounting loans. The restrictions on these practices, which are described under question 5, are based on regulations established by the Commissioner of Education pursuant to authority in the Higher Education Act of 1965, as amended.

"(7) What tuition rebate policies are followed by the above-mentioned education institutions for students who dropout

of the institution prior to completion of their school semester, quarter or year?"

The organizations which accredit the schools involved recommend refund policies for their member institutions. (See enc. III.) The Airlines School of Travel and Tourism, the Denver Automotive and Diesel College, Inc., and, as of about March 1973, the medical-dental assistance courses at Parks School of Business were accredited by the National Association of Trade and Technical Schools. All other courses at Parks School of Business were accredited by the Accrediting Commission of the Association of Independent Colleges and Schools (formerly United Business Schools Association).

Our tests of refund practices showed that all three institutions had adopted and had been following the recommended refund policies since September 1972.

"(8) What effect, if any, does an educational institutions' tuition rebate policy have on the loan default rate?"

On the basis of prior work by this Office and by others, we believe that inequitable refund policies are one of the factors that cause loan defaults.

Our December 30, 1971, report <sup>1/</sup> to the Congress, said that an important deficiency in the entire Federal Insured Student Loan program was the absence of a uniform policy setting forth the conditions under which participating schools will make tuition refunds and to whom such refunds should be made. In addition, a 1972 OE task force study of the Guaranteed Student Loan program concluded that the practice of many public as well as proprietary schools of billing students by the semester, course, or year with no refund to dropouts or students who do not complete their education is one of several factors that cause default claims. The task force also recommended that OE encourage accrediting associations to establish uniform refund policies. Other Federal and non-Federal groups that have studied this program have reached similar conclusions.

"(9) What was the finding and follow-up to HEW's September 14, 1971, audit of the Lear Siegler, Inc., Educational Division?"

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<sup>1/</sup>"Office of Education Should Improve Procedures to Recover Defaulted Loans Under the Guaranteed Student Loan Program (B-117604(7))."

The principal finding in HEW's audit was the need for Lear Siegler schools to make refunds, in accordance with the schools' refund schedules, to borrowers no longer attending school and without the borrower having to specifically request the refund.

OE's internal correspondence dated October 31, 1973, stated that the audit has remained open to verify the effectiveness of corrective action allegedly taken and the amount of refunds due students. The letter stated that, until OE published definitive standards for examining appropriate records, legal counsel for the Education Division of Lear Siegler was denying HEW access to the materials necessary to settle the audit items.

Appropriate regulations were expected to be in force by the third quarter of fiscal year 1974, but as of August 1974, OE had not finalized the regulations.

Two of the Lear Siegler schools included in the HEW audit apparently have corrected their refund practices. Our tests of the refunds made by the Denver Automotive and Diesel College, Inc., and Parks School of Business since September 1972 showed that they were following their stated refund policies.

"(10) What is the status of HEW's current audit on the Labor Finance Industrial Bank?"

On September 29, 1972, the HEW region VIII Audit Director reported to the Assistant Director, Division of University and Nonprofit Audits, Washington, D. C., the results of the audit of selected aspects of the Guaranteed Student Loan program at Labor Finance Industrial Bank. We were told that you have a copy of this report.

Labor Finance Industrial Bank was one of 108 lender and guarantee agencies throughout the country selected for audit. At the conclusion of these audits, 18 lenders and agencies, including Labor Finance Industrial Bank, were selected for a followup review. HEW officials informed us that the fieldwork at Labor Finance Industrial Bank has been completed and that a final report will be issued around September 1974. The report will address the adequacy of determining student eligibility and the propriety and accuracy of interest charged. We were informed that the audit did not reveal any significant problems at the bank.

"(11) Is HEW's position in response to questions (3), (4), and (6) of my letter of June 4, 1973, in violation of the Freedom of Information Act?"

The Freedom of Information Act provides that exemptions from disclosure in section 552(b) do not apply to the Congress; however, the legislative history <sup>1/</sup> indicates that individual Members of Congress were intended to have no greater right of access than "any person." Our Office is not responsible for determining what information must be disclosed by a Government agency under the act. Therefore, in view of the above, we cannot disagree with OE's refusal to disclose information, considered proprietary, to an individual Member of Congress.

With respect to the specific information you requested, HEW officials subsequently held that such information was not proprietary and, to the extent that it was available, provided us with the necessary data to respond to your questions.

"(12) John O'Connor, until February 29, 1972, the Student Financial Aid Chief in the Regional HEW/OE in Denver is presently a director of the Denver Industrial Bank and an officer with the Labor Finance Industrial Bank. Did his transfer of positions and subsequent activities in any way involve a conflict of interest in violation of 18 U. S. C. 206 or any other statute or government regulation? While employed in the Denver HEW/OE did he engage in activities in violation of 18 U. S. C. 206 or any other statute or government regulation?"

Until February 29, 1972, Mr. John O'Connor was employed as senior program officer, Guaranteed Student Loan program, region VIII, Denver. He submitted his resignation to the Denver office on November 15, 1971, to be effective February 29, 1972. Before the effective date of his resignation, he was made Executive Vice President of the Labor Finance Industrial Bank, through the sponsorship of Mr. Donald E. Leonard, president of the Bank.

Because of possible conflict-of-interest, OE referred this matter to HEW's Office of Investigations and Security for review and investigation. In a December 17, 1973, report the Office of Investigations and Security stated that there was neither criminal violation nor evidence of a conflict of interest. We understand that HEW has provided you with a synopsis of its investigative report.

Our review indicated possible violations of Federal laws. Accordingly, we referred this matter to the U. S. Attorney in Denver for his consideration. He subsequently advised us that, in his opinion, further action was not warranted.

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<sup>1/</sup>H. Rept. 1497, 89th Congress, 2nd Session, Public Law 487, pp. 11 and 12.

"(13) Donald E. Leonard is the President of the Denver Industrial Bank, a director of the Labor Finance Industrial Bank, and a partner in the Denver law firm of Nelson, Harding, Marchetti, Leonard, & Tate which is general counsel for Lear Siegler and the Labor Finance Industrial Bank. Mr. Leonard is also the chairman of the Committee on Higher Education. Does his position on the Committee involve a conflict of interest with his positions with the industrial banks?"

Mr. Leonard was chairman of the National Commission on the Financing of Postsecondary Education, established by section 140(b) of the Education Amendments of 1972, Public Law 92-318. Members of the Commission were selected from, among others, financial experts of the private sector under section 140(g)(1)(c)(v) of the Education Amendments of 1972. Mr. Leonard's service on the Commission while an officer or director of a private financial institution dealing in Federal insured student loans would not, in itself, be a conflict-of-interest violation.

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As instructed by your office, we did not seek formal comments on this report from OE. The report contents, however, were discussed informally with OE officials.

We do not plan to distribute the report unless you agree or publicly announce its contents.

Sincerely yours,



Deputy Comptroller General  
of the United States

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**Congress of the United States**  
**House of Representatives**  
**Washington, D.C. 20515**

July 25, 1973

Honorable Elmer B. Staats  
Comptroller General  
General Accounting Office  
441 G Street, NW  
Washington, D. C. 20548

Dear Mr. Staats:

I am writing to you concerning the administration of the Federal Insured Loan Program in Colorado.

I recently wrote to the Department of Health, Education and Welfare requesting information concerning this same subject. (See enclosures)

The information from the HEW Office of Education, along with information independently uncovered by my staff, leads me to question whether the legislative objectives of Title IV-B of the Higher Education Act of 1965, as amended, are being fulfilled or whether the program is being used primarily for private commercial gain at the expense of the students.

Specifically, I am interested in the practices of and the relationships between the following Denver eligible lenders: Denver Automotive Institute, Denver Industrial Bank, Labor Finance Industrial Bank, and Parks School of Business Lear Siegler, Inc.; and the following Denver eligible educational institutions: Airlines Training School, Inc., Denver Automotive Institute, Inc., and Parks School of Business.

I am concerned about present or potential abuses in the loan program when, as I believe is the case with the above-named institutions, a group of lending and educational institutions are all owned by the same corporation or controlled by interlocking directorates. Also there are persons in positions of authority in these institutions who are currently associated with, or were associated with, the government agencies responsible for the program.

Honorable Elmer B. Staats  
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The General Accounting Office has recently published a report on the loan program, "Improvements Needed in Administration of the Guaranteed Student Loan Program." This report considers the administration of the program with particular attention to the problem of increased loan defaults. In the instant case, I am concerned about intentional misuse of the program as well as administrative deficiencies. Therefore, I would appreciate a letter report from the GAO which responds to the questions set forth below as well as treats the broader problem of the misuse of the program.

- (1) Are the above-mentioned lending institutions exercising "due diligence" in collecting loans?
- (2) Are the default rates for the above-mentioned lending institutions higher than average for this program? If so, why?
- (3) Is there any indication that the default rate is higher because the drop-out or attrition rate is higher?
- (4) With what frequency, if at all, are the above-mentioned lending institutions making use of the HEW/OE "preclaims collection assistance?"
- (5) Are the above-mentioned lending institutions following applicable procedures in pledging, transferring, or discounting loans?
- (6) Are the above-mentioned lending institutions' practices of pledging, transferring or discounting loans in keeping with the letter or the intent of the law?
- (7) What tuition rebate policies are followed by the above-mentioned educational institutions for students who drop out of the institution prior to completion of their school semester, quarter or year?
- (8) What effect, if any, does an educational institutions' tuition rebate policy have on the loan default rate?
- (9) What was the finding and follow up to HEW's September 14, 1971, audit of the Lear Siegler, Inc., Educational Division?

Honorable Elmer B. Staats  
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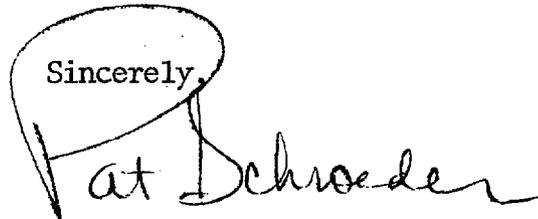
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- (10) What is the status of HEW's current audit on the Labor Finance Industrial Bank?
- (11) Is HEW's position in response to questions (3), (4) and (6) of my letter of June 4, 1973, in violation of the Freedom of Information Act?
- (12) John O'Connor, until February 29, 1972, the Student Financial Aid Chief in the regional HEW/OE in Denver is presently a director of the Denver Industrial Bank and an officer with the Labor Finance Industrial Bank. Did his transfer of positions and subsequent activities in any way involve a conflict of interest in violation of 18 U.S.C. 206 or any other statute or governmental regulation? While employed in the Denver HEW/OE did he engage in activities in violation of 18 U.S.C. 206 or any other statute or governmental regulation?
- (13) Donald E. Leonard is the President of the Denver Industrial Bank, a director of the Labor Finance Industrial Bank, and a partner in the Denver law firm of Nelson, Harding, Marchetti, Leonard & Tate which is general counsel for Lear Siegler, and the Labor Finance Industrial Bank. Mr. Leonard is also the chairman of the Committee on Higher Education. Does his position on the Committee involve a conflict of interest with his positions with the industrial banks and his law firm?

If you have any questions or need further information about my inquiry, please contact Lawrence A. Wright, Jr., in my Denver District Office.

With kind regards.

Sincerely,

A handwritten signature in cursive script that reads "Pat Schroeder". The signature is written in black ink and is positioned below the word "Sincerely,".

Patricia Schroeder  
Member of Congress

PS:db:r  
Encls.

X COLLECTION PROCEDURES FOR DENVER INDUSTRIAL BANK  
AND LABOR FINANCE INDUSTRIAL BANK

1. Prior to graduation or drop out, the school is to prepare and send to the bank an exit interview checklist, based on consultation with the student whenever possible, for the purpose of

- indicating any refund due the student,
- documenting his current address,
- documenting the repayment agreement, and
- reminding him of his responsibility to promptly repay the loan.

2. About 30 days before the first payment is due, a coupon payment book is to be sent to the student with a letter reminding him when the first payment is due.

3. When a student is more than 5 days late in making his first, second, or third regular installment payment, personal contact is to be made by telephone or telegram immediately.

4. After the first three payments have been made, a student who defaults commencing 5 business days after the due date is to be contacted by telephone, telegram, payment notice, or letter.

5. When the loan becomes 30 business days past due, the account is to be turned over to a trained member of the collection staff for appropriate action. Several form letters have been developed for the collector's use.

6. When the loan becomes 60 days past due, pre-claim assistance is to be requested of the HEW Office of Education.

7. When the loan is 90 days past due, a registered letter is to be sent to the student's last known address requesting payment of the loan in full within 30 days and cautioning the student that failure to comply will result in the loan being referred to the Federal Government for collection.

8. When the loan is 120 days past due, the entire collection history is to be reviewed by a member of the bank to determine whether additional collection efforts should be undertaken. If not and 30 days have elapsed since the letter in item 7 was sent, the loan is to be declared in default and a claim filed with the HEW Office of Education.

RECOMMENDED REFUND POLICIES OF CERTAIN  
VOCATIONAL SCHOOL ACCREDITING ORGANIZATIONS

NATIONAL ASSOCIATION OF TRADE  
AND TECHNICAL SCHOOLS

1. All money paid will be refunded if cancellation is requested within 3 days after signing an enrollment agreement.
2. A registration fee of 15 percent of the contract price, but not more than \$100, may be retained by the school if cancellation is requested after 3 days, but before the scheduled starting date for classes.
3. A tuition charge of not to exceed 10 percent of the contract price plus \$100 limited to a total of \$300 may be retained by the school if a student terminates his training during the first week of his course.
4. A tuition charge of not to exceed 25 percent of the contract price plus \$100 may be retained by the school if the student terminates his training after 1 week, but within the first 25 percent of his course.
5. A tuition charge of not to exceed 50 percent of the contract price plus \$100 may be retained by the school if the student terminates his training after completing over 25 percent but within 50 percent of his course.
6. The school shall make a settlement which is reasonable and fair to both if prolonged illness or accident, death in the family, or other circumstances make it impracticable for the student to complete his course.

The policy of the Association does not provide for any refund of tuition after a student completes more than 50 percent of a course.

ACCREDITING COMMISSION OF THE ASSOCIATION  
OF INDEPENDENT COLLEGES AND SCHOOLS  
(FORMERLY UNITED BUSINESS SCHOOLS ASSOCIATION)

1. Not more than \$100 may be retained by the school if tuition is collected in advance and the student does not begin classes.
2. The following refund policy will be acceptable after commencement of classes for programs of more than 3 months (or 1 quarter) in length up to 12 months:
  - a. The school may retain 10 percent of the stated course price during the first week of classes.

b. The school may retain 20 percent of the stated course price during the next 3 weeks of classes.

c. The school may retain 45 percent of the stated course price during the first 25 percent of the course.

d. The school may retain 70 percent of the stated course price during the second 25 percent of the course.

e. The school may retain 100 percent of the course price thereafter.

3. The school will refund 100 percent of the stated course price attributable to the period of a course beyond 12 months in length.

4. The school should establish an equitable refund policy for course of 3 months (or 1 quarter) or less.