



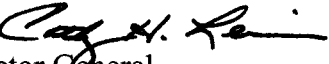
UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF INSPECTOR GENERAL

**ALERT MEMORANDUM**

AUG 1 2003

TO: Sally Stroup  
Assistant Secretary  
Office of Postsecondary Education

FROM: Cathy H. Lewis   
Assistant Inspector General  
Evaluation, Inspection and Management Services

SUBJECT: Review of Lender Inducements (ED/OIG I13C0003)

This alert memorandum provides information from our review of lender inducements. The Office of Inspector General received an allegation that Sallie Mae was offering schools illegal inducements in return for Federal Family Education Loan Program (FFELP) loan volume. The allegation, from an anonymous source, did not include any specific information or evidence regarding illegal inducements.

The governing anti-inducement legislation, found in Section 435(d)(5)(A) of the Higher Education Act of 1965, as amended (HEA), prohibits a lender from offering, directly or indirectly, points premiums, payments, or other inducements, to any educational institution or individual in order to secure applicants for FFELP loans. Since the enactment of the legislation in 1986, the FFELP market has changed significantly with increasing demands for benefits or services by schools, the rising cost of education, and escalating competition for FFELP loans.

The Department's interpretive guidance to the community through Dear Colleague Letters has not been updated since 1995. Informal guidance provided in letters and e-mails has not resolved the concerns of the FFELP participants as to what constitutes an inducement. Formal administrative enforcement action has been limited to one case, involving Sallie Mae's agreement with Dr. William M. Scholl College of Podiatric Medicine. Federal Student Aid has never performed reviews of lenders for the specific purpose of reviewing compliance with the anti-inducement provision.

The Department held a series of meetings with the FFELP community in the spring and summer of 2001 to discuss anti-inducement issues, but no consensus was reached. In November 2001, the Consumer Bankers Association (CBA) and the Education Finance Council (EFC) issued a joint statement on their view of the applicability of the anti-

inducement statute to the private credit offerings of FFELP lenders. In the statement, CBA and EFC declared that they believe it is illegal for a lender to require a school to refer FFELP loan applicants (including placing a lender on a preferred lender list) to the lender in exchange for private credit. A FFELP lender, however, could offer private credit in hopes of FFELP loan referrals from a school, and could subsequently alter the terms of any private loan agreement with a school, or cease to provide private credit if the FFELP loan volume was less than expected.

Sallie Mae and the National Council of Higher Education Loan Programs did not sign the statement. The Department has not taken a position on the joint statement and has not offered guidance on the growing market for private loans.

We met with representatives from Federal Student Aid (FSA), the Office of the General Counsel, the Office of Postsecondary Education (OPE), and the Office of the Deputy Secretary. We also interviewed representatives from Sallie Mae and other FFELP participants, including lenders, guaranty agencies, a school financial aid officer participating in the William D. Ford Federal Direct Loan Program (Direct Loan Program) and a lawyer with the legal aid community representing student interests. Although the parties we interviewed were knowledgeable and provided useful information on current practices in the FFELP market, none provided specific information regarding improper inducements provided by lenders at specific institutions.

We selected two schools for review based on an increase in Sallie Mae loan volume. We found evidence that one of these schools and Sallie Mae negotiated preferred lender status in exchange for a specified dollar amount of private loans.

Our review concluded there are bargaining practices between schools and lenders for FFELP preferred loan status and private loan volume that should be addressed through statutory and regulatory changes or further Department guidance. Given the current marketing practices by schools and lenders, the Department should examine the roles and responsibilities of schools, as well as lenders and lender affiliates in the inducement issue.

We recommend that in recognition of the current market realities in the FFELP, the Assistant Secretary for OPE:

- Provide guidance on the growing market for private loans by clarifying the application of the anti-inducement provision to private loans; and
- Reevaluate the anti-inducement provision of Section 435(d)(5)(A) of the HEA and determine if statutory changes should be proposed in the upcoming reauthorization to include schools, lender affiliates and other necessary changes.

cc: John Danielson  
Harold Jenkins