

The First Marblehead Corporation

**Statement of Peter B. Tarr
Chairman of the Board of Director and General Counsel**

**The First Marblehead Corporation
Opening Statement**

**Washington, DC
June 6, 2007**

The First Marblehead Corporation is pleased to have the opportunity today to appear before the Senate Committee on Banking, Housing and Urban Affairs on the subject of private education loans. I'm here today on behalf of First Marblehead. My name is Peter Tarr and I serve as the Chairman of the Board of Directors and General Counsel for the company. We thank Chairman Dodd, Ranking Member Shelby and the Committee for inviting us here and congratulate them for bringing additional focus on these important issues.

We support recent efforts made by Congress to ensure that all Americans have access to higher education and affordable student financing. It is critical that students and families have a broad range of quality financing options to meet the rising cost of college education as well as transparent and accurate information about those choices.

First Marblehead provides outsourcing services for private, non-governmental education lending in the U.S. Founded in 1991, First Marblehead today employs more than 1000 people working primarily in the Boston area.

First Marblehead helps meet the growing demand for private education loans by providing financial institutions with an integrated suite of private loan services - from program design through application processing and customer support to the ultimate disposition of the loans through securitization transactions that we structure and administer. Over the past 16 years, First Marblehead has helped our lender clients deliver more than one million loans, in the process assisting more than 600,000 students and families in the pursuit of their educational goals.

Enrollment in higher education in the U.S. has grown dramatically over the past several decades, with approximately 18 million students currently attending college versus 12 million in 1980.¹ Over the same period, the cost of education has increased rapidly. Today, the average annual cost of attending a public university is approaching \$15,000, while the average cost of private colleges exceeds \$30,000.² At the same time, the availability of student aid from federal, state and institutional sources has grown at a much slower rate – creating a large and growing gap between the cost of attendance and traditional financial aid.

The annual funding gap between the cost of education and traditional funding sources such as federal student loans, scholarships and grants continues to widen and today we estimate that gap at traditional two and four-year public and private institutions to be \$122 billion.³ In fact, recent estimates indicate that federal and institutional aid covers only 20% of average total need at public four year universities, and 12% at private institutions.⁴

To address this huge funding gap and to meet the growing demand for long-term, supplemental financing for education, First Marblehead and other reputable companies have over the past 16 years created innovative products that provide reasonable, market-based pricing and attractive features for borrowers. In the upcoming academic year, we estimate the total private education loan market will exceed \$20 billion.⁵ Today, private loan providers are competing vigorously on the basis of price, product features, customer service and borrower benefits. The result is better choices for students and their families seeking financing options that work best for their circumstances.

Private education loans are funded by financial institutions and are not guaranteed against default by the federal government. Many private education loans have features similar to federally-guaranteed student loans, including no pre-payment penalties, in-school payment deferment and forbearance. Many programs also offer borrower rewards for on-time and electronic payment just like in the federal programs.

Because they are not federally guaranteed, the risk of default on private education loans is borne by the lender or loan holder. This most fundamental difference is a key limiting factor as to who might qualify for a private student loan. Private loan borrowers must typically qualify for the loan by meeting certain credit criteria. Not all applicants for private loans are approved for the loans: approximately one half of the applicants for First Marblehead-facilitated private loans are declined due to insufficient credit. In fact, few if any undergraduates can meet our strict underwriting criteria on their own so they enlist their parents or another experienced borrower to co-sign the loan. As a result, the “typical” private loan borrower in the programs we administer is an undergraduate student with a 50-year-old parental cosigner with an average FICO score in excess of 700.⁶ Approximately 80% of the loans we process are co-signed. The remainder are generally to older students or non-traditional students –who have the requisite credit history.

The interest rates on First Marblehead-facilitated private loans are determined by a borrower's credit quality. Again because of the absence of a federal guarantee, rates are typically higher than those on federal student loans. For private loan products facilitated by First Marblehead, interest rates are based on the London Interbank Borrowing Rate – an internationally-recognized money rate index. Also, many private loans include an origination or guarantee fee which provides a reserve against potential loan default. While these may result in higher rates than federal student loans, these rates are in most cases better than those offered on credit cards or other unsecured debt, which are frequently utilized by students to pay some portion of education expenses.

Private education loans are offered by providers through two distinct channels. Historically, most private loans have been originated via the school financial aid office, similarly to how Federal Stafford Loans are administered. An increasing percentage of private loans are originated directly between the borrower – typically a student and an adult cosigner – and the loan provider. The growing range of product types, features and providers allows borrowers to choose private loan products and providers based upon their own personal preferences and selection criteria, which may include customer service quality, price, convenience, speed of disbursement, brand/provider preference and privacy concerns.

Postsecondary education is a large and highly impactful investment for students and families. With the cost of college continuing to rise at a rate far exceeding inflation⁷, it is critical that students make sound financial decisions in determining how to pay for college. No one benefits – not the student, the school, the lender nor First Marblehead - when a borrower struggles to repay their private education loan. To foster smart borrowing, First Marblehead initiated a borrower information program in mid-2006 to encourage students and families to carefully consider the full range of financial aid options available to them, including federal student loans, prior to taking private loans. In the web pages and call scripts we develop with our lender clients, we have integrated language recommending that loan applicants carefully consider the full range of financial aid options available to them before turning to private loans. In these materials we inform prospective borrowers that private loans are typically used to supplement rather than supplant federal loans when the latter are not sufficient to cover the full cost of education, which is increasingly the case.

Industry data demonstrate that the vast majority of private education loan borrowers already know about, and avail themselves of, federal aid. A recent industry report cites statistics from the Department of Education indicating that nearly 9 out of every 10 private loan borrowers have applied for federal aid.⁸ And in the case of First Marblehead loan programs, private loan borrowing is typically a family decision involving both students and parents. More than 80% of the students taking loans facilitated by First Marblehead have creditworthy cosigners.⁹

Regarding the regulation of private education loan programs, all First Marblehead-facilitated loans are originated by financial institutions that are subject to oversight and examination by one or more of the following regulatory agencies: the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve Bank (FRB), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS). By regulation and contract, these agencies' oversight powers extend into First Marblehead as agents for our client lenders. Additionally, both First Marblehead and our lender clients are subject to Federal Trade Commission (FTC) jurisdiction with regard to general commercial consumer protection regulations involving marketing and advertising practices, telecommunications rules and collection activities.

Private education loans are subject to the same Federal consumer lending regulations applicable to more familiar consumer-purpose loans such as installment loans and credit cards. The most significant of these regulations are:

- Truth in Lending Act (TILA, Regulation Z), which requires that creditors clearly and conspicuously disclose interest rates and borrowing costs to borrowers, using a specified disclosure format that allows comparison shopping between loan products. TILA also imposes certain advertising and billing dispute resolution requirements.
- Equal Credit Opportunity Act (ECOA, Regulation B), which prohibits discrimination on the basis of race, color, religion, national origin, sex, marital status, age, or receipt of public assistance income. ECOA establishes rules for taking and evaluating applications and sets adverse action notification requirements.
- Title V of Gramm-Leach-Bliley Act (GLBA, Regulation P), which requires institutions to notify customers about privacy policies and practices, describes how the institutions intend to share non-public personal information with third parties, and allows consumers to prevent that sharing if desired.

In closing, First Marblehead again appreciates the opportunity to participate in this discussion and thanks the committee and Chairman Dodd for the invitation to testify today. The employees of First Marblehead are deeply committed to working with our lender clients to provide attractive, high-value financial solutions for students and families pursuing their educational goals. We firmly support product innovation and the objective of making the process of financing higher education more efficient, transparent and understandable for students and families.

-
- ¹ National Center for Education Statistics (NCES) – *Projections for Education Statistics to 2014*
- ² College Board – *Trends in Student Loan Pricing, 2006*
- ³ NCES - *Projections*
- ⁴ College Board – *Trends in Student Aid, 2006*, College Board – *Trends in College Pricing, 2006*
- ⁵ College Board - *Trends in Student Aid, 2005*
- ⁶ The First Marblehead Corporation – *Risk Management Update, March 2007*
- ⁷ United States Census Bureau – *Statistical Abstract of the United States: 2007*, College Board – *Trends in College Pricing, 2006*
- ⁸ U.S. Department of Education – *National Post-Secondary Aid Survey (NPSAS), 2004*
- ⁹ The First Marblehead Corporation – *National Collegiate Student Loan Trusts 2004-1 through 2007-2 Static Pool Data*