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SLBA
Student Loan Borrower Assistance

MAKING STUDENT LOAN SERVICING WORK FOR BORROWERS

June 2014

FEDERAL STUDENT LOAN SERVICING IN A NUTSHELL

From the beginning of the government's Direct Loan program in 1994 until 2008, the Department of Education ("Department") contracted with a single Direct Loan servicer. In 2009, just before the switch to 100% Direct Lending, the Department contracted with four student loan servicers, Great Lakes Educational Loan Services, Nelnet, FedLoan Servicing (PHEAA), and Sallie Mae (now Navient). These four servicers are referred to as TIVAS (Title IV Additional Servicers).

The Department's initial contract with the TIVAS was for five years, expiring in June 2014, with an option to extend for an additional five years at the government's discretion. The Department has said that it intends to "exercise the option" and extend the contracts with all of the TIVAS. The Department has also said that it "…intends to refine the contract terms and conditions through negotiations in its on-going efforts to drive efficiency and enhance performance." [i]

In addition to the contracts with the TIVAS, the Department currently has contracts with seven non-profit student loan servicers representing thirty-four non-profit entities. In fact, Congress passed legislation in 2010 requiring the Department to contract with non-profit servicers. This mandate was eliminated in 2013. The Department announced that it would continue the existing non-profit servicer contracts through fiscal year 2014.

The four TIVAs currently service about 25 million borrower accounts.

The government pays millions of dollars to each servicer:

Just one servicer, Sallie Mae, received about $109 million in 2013 to service loans.[ii]

The non-profits currently service about 3 million borrower accounts.

THE NEED FOR REFORM AND OVERSIGHT

The Department of Education is not providing sufficient oversight to ensure that all student loan borrowers receive quality service. [iii] For years, National Consumer Law Center staff members have sent examples of poor service and legal violations to the Department of Education and more recently to the Consumer Financial Protection Bureau (CFPB). Only recently has the Department admitted to finding numerous problems with the performance of servicers such as Sallie Mae. For example, the Department responded to a request for information from Senator Elizabeth Warren in December 2013 with a long list of "issues" identified by the Department in audits and reviews of Sallie Mae. These issues with Sallie Mae's servicing of federal loans include defects in conversion to repayment, incomplete adjustments to borrower accounts when transferred from a previous servicer, and incorrect calculation of income for the income-based repayment program (IBR). However, the Department said that compliance issues have not risen to the level where "penalties were considered appropriate."[iv]

The Department decided that these problems were not serious, but other federal agencies have come to different conclusions. For example, the FDIC and Department of Justice announced settlements with Sallie Mae in May 2014 based on allegations of a pattern and practice of violating the Service Members Civil Relief Act and other consumer laws.

QUALITY SERVICE AND PROTECTING BORROWERS AND TAXPAYERS

There are few laws specifically governing student loan servicer conduct. There are some protections in the contracts that the Department signs with the servicers. However, borrowers rarely know about those rights. Even borrowers who find out about their rights have virtually no way to enforce them. To make matters worse, there is little or no government oversight.

The system must work for borrowers, not just for private profit. At a minimum, borrowers must have the following rights:

1. **Right to timely and accurate information about loan balances, payment histories and other important account information.**
2. **Right to timely and accurate information about affordable repayment, deferment, and other options.**
3. **Right to holistic counseling and information about the options that work best for borrowers.**
4. **Right to switch servicers.**
5. **Right to dispute errors and challenge abuses.**
6. **Right to receive timely responses to appeals and inquiries.**
7. **Right to obtain comprehensive performance information about all servicers.**
8. **Right to relief for harm caused by servicer misconduct.**

REFORM PRIORITIES

Do Not Renew Current Contracts

There is ample evidence of non-compliance and legal violations among the current servicers. Yet the Department has already said that it will renew the contracts. Borrowers and taxpayers deserve better than five more years of the same old system.

Department leaders have said they cannot terminate the contracts among other reasons because it would be too onerous to find new servicers. It will certainly be necessary to ensure a smooth transition if servicers are removed from the government payroll, but this is not an excuse to let them linger.

> **In testimony before the U.S. Senate in March 2014, Federal Student Aid Chief Operating Officer James Runcie said that the Department has considered the potential dislocation of borrowers if they did not continue the TIVAS contracts. Chairman Harkin responded, "It sounded like your answer, Mr. Runcie, was that they're too big to fail." Senator Warren added: "I'm very concerned about re-upping a multimillion –dollar contract with Sallie Mae, when Sallie Mae has demonstrated time and time again that it's not following the rules."[v]**

Limit the Number of Servicers and Create a Single Point of Entry

The goal of the system should be to provide quality service to borrowers. The current system is not meeting this goal because, among other reasons, there are too many servicers and too much variation in service. As a result, many borrowers do not understand who is servicing their loans.

Current servicers co-brand all correspondence, leading to confusion among borrowers as to why they are hearing from an unknown agency. This confusion has serious consequences leading to communication breakdowns and sometimes to defaults.

We agree with the Department that competition among a small group of highly qualified servicers will likely drive improved performance for borrowers and taxpayers. Limiting the number of servicers is important, but not enough. The Department must also eliminate co-branding and create a single point of entry for borrowers to communicate with servicers. We agree with the Direct Loan Coalition that federal contractors servicing the loans should be "…invisible agents of the federal government with identical processes and policies."[vi]

Under this system, all borrowers will receive communications that are clearly from the government, not from a private servicer or contractor that the borrower may or may not know and may not even associate with student loans. Borrowers should be able to find out the identities of servicers as necessary.

Compensate Servicers Based on Comprehensive Default Prevention and Quality Service Metrics

The current performance metrics for the TIVAS that are used to allocate accounts are based on customer satisfaction, school and federal personnel surveys, and the number of borrowers and amounts of loans in default. The metrics for the non-profit servicers are more expansive, considering not only the total numbers of borrowers in default and the amounts in default, but also the percentage of borrowers in current repayment, 90 days delinquent and resolution of borrower accounts greater than 180 days delinquent.

At a minimum, the Department should evaluate all servicers based on the additional default prevention statistics that currently apply only to non-profit servicers. Counting only the numbers of borrowers in default is incomplete because it does not consider whether the servicers steered borrowers to short-term options such as forbearances or other ways that servicers temporarily keep borrowers out of default to make their numbers look more attractive. This keeps the accounts flowing to the servicers, but too often at the expense of comprehensive, long-term relief for borrowers.

Provide Public Information about Servicer Performance

Public information should include detailed information about the current performance metrics and other investigations and evaluations of servicer performance.

Conduct Rigorous Oversight and Penalize Servicers that Do Not Perform

The Department has authority to terminate contracts or otherwise penalize servicers that violate program requirements. Under existing authority, in addition to terminating contracts, the Department can:

- Choose not to assign further accounts or transfer existing accounts to other servicers based on non-compliance with the contract,
- Unilaterally shift borrowers to other servicers,
- Decide not to reimburse servicers for loans that were not serviced in compliance with the contracts, and
- Terminate contracts if conflicts of interest arise or if necessary to avoid the appearance of a conflict of interest.

The Department must use these tools to protect borrowers and taxpayers. Other regulators must be part of the solution too. The CFPB's announcement in December 2013 that it will begin supervising large student loan servicers is a promising sign for borrowers.[vii] The CFPB can help fill the gaps caused by a long history of lax federal oversight. The CFPB, the Department of Education and other agencies must work together to ensure that servicers are doing their jobs properly. State Attorney General Offices also have an important role in protecting consumers in their states.

Solicit Borrower Input

The Department of Education has severely restricted access to contracts and important servicing instructions. We fear that the Department of Education is moving toward a model in which it justifies withholding basic information about private servicers because of supposed proprietary contract arrangements. For example, the Department has said that it is in the final stages of developing revised performance metrics and other reforms. Yet this appears to be a closed process.

Relying on private contracts may work well if the Department is seeking to avoid accountability, but it does not work best for borrowers and taxpayers. Schools may be profiting as tuition continues to rise and private servicers and collectors may be profiting due to borrower misfortune, but we should not be growing our student loan system on the backs of defaulted borrowers or measuring success by private profit rather than student success.

We can and must do better for student borrowers and taxpayers.

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[i] U.S. Department of Education, Letter to Chairman John Kline, Committee on Education and the Workforce, U.S. House of Representatives (March 31, 2014).

[ii] Shahien Nasiripour and Zach Carter, "How Arne Duncan is Undercutting Senate Democrats on Student Loan Reform", Huffington Post (May 7, 2014).

[iii] See, e.g., U.S. Department of Education, Office of Inspector General, "Federal Student Aid's Award and Administration of the Title IV Additional Servicers Contracts", Final Audit Report ED-OIG/A02L0006 (August 2013).

[iv] Senator Warren's letter and the Department of Education's response are available in attachments to NCLC's report: "The Sallie Mae Saga: A Government-Created, Student Debt Fueled Profit Machine" (January 2014).

[v] Quoted in Michael Stratford, "Ed Dept. Defends Loan Servicing", InsideHigher Ed (March 28, 2014).

[vi] See, e.g, Statement of Nancy Hoover, Director Financial Aid, Denison University, before the U.S. Senate Banking Subcommittee on Financial Institutions and Consumer Protection (June 4, 2014).

[vii] Consumer Financial Protection Bureau, "CFPB to Oversee Nonbank Student Loan Servicers" (Dec. 3, 2013).