



# S.332: AN ACT RELATING TO STUDENT LOAN SERVICERS

Jill Rickard, Director of Policy

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## NATIONAL STUDENT LOAN DEBT

- 43 million borrowers have outstanding federal student loan debt of over \$1.4 trillion.
- This figure has tripled since 2007.

Source: U.S. Dept. of Education Office of Federal Student Aid (as of second quarter 2019).

## VERMONT STUDENT LOAN DEBT

- 63% of 2018 Vermont college graduates had student loan debt.
- The average debt load was \$31,431.
  - Does not include for-profit college graduates, but they are more likely to have high student loan debt levels and struggle with repayment.

Source: 14<sup>th</sup> Annual Report: "Student Debt and the Class of 2018." The Institute for College Access & Success. September 2019.

# FEDERAL STUDENT LOAN PROGRAMS

- Federal Family Education Loan Program (“FFELP”)
  - Student loans originated by private sector and state-based lenders and guaranteed by the federal govt.
- Federal Direct Loan Program (“FDLP”)
  - Student loans directly issued, owned, and administered by the federal govt.
- FFELP and FDLP created by the Higher Education Act of 1965; coexisted until 2010, when the Student Aid and Fiscal Responsibility Act essentially eliminated new FFELP loans.
- Today:
  - All new federal student loans are issued under the FDLP.
  - Most outstanding FFELP loans are owned by private lenders; some were purchased by the U.S. Department of Education.

## PRIVATE STUDENT LOANS

- Made directly to students by (1) state- or college-based lenders or (2) banks, credit unions, or other lending institutions.
- Typically subject to higher interest rates than federal student loans, without the same repayment options or consumer protections.

# WHAT IS A STUDENT LOAN SERVICER?

- The Dept. of Education and private lenders contract with private student loan servicers to aid in the administration of student loans.
- Servicers act as middlemen between lenders and borrowers, performing functions such as:
  - Communicating with borrowers about repayment;
  - Disclosing info about loan terms;
  - Collecting and processing loan payments; and
  - Processing requests for loan forgiveness, forbearance, and deferment.
- A servicer is often the sole point of contact for a borrower about their federal student loans.

# FEDERAL REGULATION OF STUDENT LOAN SERVICERS

- The Higher Education Act of 1965 governs FDLP and FFELP and empowers the Secretary of Education to enter into servicing contracts with qualified entities and prescribe regulations applicable to servicers.
- For all FDLP loans and FFELP loans owned by the Dept. of Education, servicers enter into contracts directly with the Dept. of Education, which govern servicer obligations.
  - For privately-owned FFELP loans, servicers enter into contracts with the private lenders.
- Under Dodd-Frank, CFPB has supervisory and enforcement authority over student loan servicers with more than one million accounts.
- In 2017, the Dept. of Education terminated its MOU with the CFPB and claims it has full responsibility for oversight of federal student loan servicers.

## REPORTS OF SERVICER MISCONDUCT

- In recent years, student loan servicers have been accused of a range of misconduct, such as:
  - Steering borrowers away from favorable repayment plans;
  - Misleading or failing to provide borrowers material information regarding their loans' terms, status, and repayment options; and
  - Misallocating or misapplying payments.



## REPORTS OF SERVICER MISCONDUCT

- According to a 2017 report, the Inspector General found that the Dept. of Education's Office of Federal Student Aid failed to adequately supervise student loan servicers.
- Servicers repeatedly placed borrowers into costly forbearance without offering them other, more beneficial options.
- One large servicer had a "call fail rate" greater than 10% - on more than 10% of calls, they failed to give borrowers good information on repayment options.

## REPORTS OF SERVICER MISCONDUCT: FORBEARANCE STEERING

- Allegations of forbearance steering (to avoid lengthy consumer interactions).
- In 2017, the CFPB filed a complaint against a large federal student loan servicer, alleging the servicer actively encouraged borrowers to enter forbearance (in which interest continues to accrue and is capitalized), rather than enroll in an income-driven repayment plan (which would avoid fees).
- Alleged to cost borrowers \$4 billion in interest from January 2010 to March 2015.

## REPORTS OF SERVICER MISCONDUCT: PSLF ELIGIBILITY

- In 2007 Congress created the Public Service Loan Forgiveness program, designed to encourage graduates to taking lower-paying jobs in government or with a nonprofit.
- Forgives the remaining federal student loan debt of qualified public servants after ten years of on-time, qualifying payments.
- Allegations that the program's complex requirements were not adequately understood or explained by servicers.
- In 2017 (the first year of accepting PSLF applications), 28,000 borrowers applied for forgiveness and only 96 were approved.

## STATE EFFORTS TO REGULATE STUDENT LOAN SERVICERS

- In response to a perceived lack of oversight by the Dept. of Education, many states have passed laws regulating student loan servicers.
  - Laws enacted in 12 jurisdictions: California, Colorado, Connecticut, DC, Illinois, Maine, Maryland, Nevada, New Jersey, New York, Rhode Island, and Washington
  - Pending legislation in 9 jurisdictions: Iowa, Massachusetts, Minnesota, Missouri, New Hampshire, North Carolina, Oregon, Pennsylvania, and South Carolina

## S.332: LICENSURE

- Any person servicing loans in Vermont must be licensed with DFR.
  - Excludes depository institutions, public and nonprofit secondary institutions, VSAC, and the U.S. government.
- \$1000 annual license fee + \$500 one-time application and investigation fee.
- **Automatic license** given to any person who performs servicing under a contract with the Dept. of Education.
  - Attempts to avoid federal preemption issues.
  - If federal servicer also conducts servicing outside of its contract with the Dept. of Education, it must comply with the application procedures.

## S.332: SERVICER DUTIES

- Required disclosure to student borrowers
- Promptly respond to inquiries from borrowers and ombudsperson
- Request borrower instruction on the application of overpayments
- Apply partial payments in a manner that minimizes late fees and negative credit reporting
- Notify borrower of default within 30 days
- Safeguard and account for borrower's money and act with reasonable skill, care, and diligence

## S.332: SERVICER DUTIES (CONT.)

- In the event of the sale or transfer of servicing:
  - Require the new servicer to honor all borrower benefits (and new servicer must do so)
  - Within 45 days, transfer all borrower records
  - Seven days before the next payment is due, provide borrower with notice of the sale or transfer, including contact info for the new servicer
- Upon request of DFR, provide a report on its activity in Vermont
- Properly evaluate borrower's eligibility for an income-based repayment plan or loan forgiveness program before placing the borrower in forbearance or default

## S.332: SERVICER PROHIBITED PRACTICES

- Defraud, mislead, harass, or intimidate a borrower
- Misstate any material fact, or misrepresent or omit a material fact concerning a student loan
- Misapply or recklessly apply payments
- Refuse to communicate with a borrower's authorized representative
- Make a false statement or misrepresent or omit a material fact concerning information or reports to be filed with a state or federal agency or an investigation or examination conducted by DFR or another state
- Violate applicable state or federal laws or regulations



## S.332: STUDENT LOAN OMBUDSPERSON

- A single knowledgeable point of contact to assist and educate student borrowers, work with colleges and servicers to resolve borrower complaints, collect and analyze data, and educate the public.
- Currently borrowers may contact VSAC, DFR, the AGO, the Dept. of Education student loan ombudsman, the FTC, or the CFPB.
- Effective assistance requires deep knowledge of the intricacies and differences between varying federal loan programs, which current state contacts may lack.