

SCHOOL OF HARD KNOCKS: FEDERAL STUDENT LOAN SERVICING AND THE LOOMING FEDERAL STUDENT LOAN CRISIS

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With an estimated one in four borrowers struggling to repay their federal student loans or already in default, the federal student lending program is on the precipice of collapse. Rates of delinquency and default are continuing to rise due to the fractured statutory and regulatory framework enacted by the federal government. Although critics are quick to blame federal student loan servicers for the failings inherent within the federal student loan program, such misplaced blame obfuscates the true problems underpinning the federal student loan program as a whole: the Department of Education’s convoluted regulations and contractual obligations, the unnecessarily complex statutory and regulatory framework, and competing oversight exercised by multiple federal agencies and the individual states.

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INTRODUCTION

Nearly forty-three million Americans collectively owe \$1.5 trillion in outstanding student loan debt.¹ Of that, approximately ten percent of student loan debt is over ninety days delinquent or in default,² while the actual delinquency rate is estimated to likely be double this amount due to the fact

1. *Federal Student Aid Portfolio Summary*, U.S. DEP'T OF EDUC., <https://studentaid.ed.gov/sa/sites/default/files/fsawg/datacenter/library/PortfolioSummary.xls> [hereinafter *Student Aid Portfolio*] (last visited May 11, 2020).

2. CTR. FOR MICROECONOMIC DATA, FED. RESERVE BANK OF N.Y., QUARTERLY REPORT ON HOUSEHOLD DEBIT AND CREDIT (2019), https://www.newyorkfed.org/medialibrary/interactives/householdcredit/data/pdf/HHDC_2019Q2.pdf [hereinafter FED. RESERVE QUARTERLY REPORT].

that half of all federal student loans are not in the repayment cycle.³ This equates to one in four student loan borrowers who are struggling to repay or already in default.⁴ In total, student loan borrowers are at least ninety days behind on repayment of \$160 billion worth of federal student loans.⁵ By way of comparison, the worst performing residential mortgage portfolio on which the federal government is ultimately responsible is the Federal Housing Administration single family loan program, and only two percent of those loans are ninety days or more delinquent.⁶ To give these staggering numbers perspective, there are nearly as many people receiving retirement benefits under the United States Social Security program as those who owe federal student loans, and the volume of outstanding student loan debt outweighs the total volume of credit card and automobile debt combined.⁷ Many characterize the federal student loan program as a system on the verge of collapse due to the soaring rates of default and predictions that defaults will only continue to rise.

If these headline numbers were not intimidating enough, they are thought to be having real-world ramifications on student loan borrowers. Increasingly, borrowers are putting off major life decisions on account of their federal student debt. According to the Federal Reserve, federal student debt prevented 400,000 young Americans from purchasing homes between 2005 and 2014.⁸ Not only is federal student debt affecting decisions related to the type of housing the borrowers' purchase, but at least one study has identified

3. *Id.* at n.2.

4. CFPB *Concerned About Widespread Servicing Failures Reported by Student Loan Borrowers*, CONSUMER FIN. PROT. BUREAU (Sept. 29, 2015), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-concerned-about-widespread-servicing-failures-reported-by-student-loan-borrowers/>.

5. See FED. RESERVE QUARTERLY REPORT, *supra* note 2 (detailing the repayment status and composition of student loan debt, among other forms of household credit).

6. Robert Carnevale, *Mortgage Loan Delinquency Rate Hits 13-Year Low*, VALUEPENGUIN (Mar. 4, 2019), <https://www.valuepenguin.com/news/mortgage-delinquency-rate>.

7. Teddy Nykiel, *2019 Student Loan Debt Statistics*, NERDWALLET (Dec. 20, 2019), <https://www.nerdwallet.com/blog/loans/student-loans/student-loan-debt/> (43 million federal student loan borrowers); *Policy Basics: Top Ten Facts About Social Security*, CTR. BUDGET & POLICY PRIORITIES (Aug. 14, 2019), <https://www.cbpp.org/research/social-security/policy-basics-top-ten-facts-about-social-security> (63 million Social Security beneficiaries); FED. RESERVE QUARTERLY REPORT, *supra* note 2.

8. See Alvaro Mezza et al., *Can Student Loan Debt Explain Low Homeownership Rates for Young Adults?*, 1 FED. RES., CONSUMER & CMTY. CONTEXT 1, 2, 5 (2019), <https://www.federalreserve.gov/publications/files/consumer-community-context-201901.pdf> (crediting federal student loan debt for the upwards of twenty percent decline in homeownership).

student debt burdens as influencing the geographical location in which borrowers choose to live and causing educated rural residents to move to urban areas.⁹ Unable to pay their federal loans and unable to discharge them in bankruptcy, these borrowers are postponing key wealth-building activities such as saving for retirement and building equity in real property. Due to the student loan market's scale, these issues not only impact individual borrowers in the short term but appear to be having macro effects on the economy as a whole that will continue to magnify as time goes on. In some senses, obtaining federal financing for a postsecondary education—previously thought to be an entry ticket into the middle class or upper-middle class—may look more like a game of chance to some borrowers.

Seeking someone to blame, politicians, attorneys general, regulators, and distressed borrowers are increasingly scapegoating federal student loan servicers, since borrowers must interact with servicers to manage their student loan debt.¹⁰ These servicers are private companies hired by the Department of Education (DoE) to administer and collect outstanding federal student loan debt.¹¹ State politicians have noticed this trend: several states have passed or are in the process of passing legislation regulating federal student loan servicers,¹² and state attorneys general are bringing enforcement actions against

9. PJ Tabit & Josh Winters, “*Rural Brain Drain*”: *Examining Millennial Migration Patterns and Student Loan Debt*, 1 FED. RES., CONSUMER & CMTY. CONTEXT 1, 7, 9 (2019), <https://www.federalreserve.gov/publications/files/consumer-community-context-201901.pdf> (studying the correlation between the amount of borrowers' student loans and their residential geographic choices in relation to urban and rural environments).

10. See, e.g., Nicholas Fandos, *Elizabeth Warren Calls Out Education Department over Student Loans*, N.Y. TIMES (June 10, 2015, 4:01 PM), <https://www.nytimes.com/politics/first-draft/2015/06/10/elizabeth-warren-calls-out-education-department-over-student-loans/> (describing Senator Elizabeth Warren's criticisms of federal loan servicers); *An Examination of State Efforts to Oversee the \$1.5 Trillion Student Loan Servicing Market: Hearing Before the Subcomm. on Oversight & Investigations of the U.S. H. Comm. on Fin. Servs.*, 116th Cong. (2019), <https://financialservices.house.gov/uploadedfiles/hrg-116-ba09-wstate-thomana-20190611.pdf> (testimony of Arwin Thoman, Director, Student Loan Assistance Unit) (discussing the failings of the federal student loan program as due to the federal student loan servicers); *CFPB Concerned About Widespread Servicing Failures Reported by Student Loan Borrowers*, *supra* note 4 (quoting Richard Cordray, who stated “[w]ith one out of four student loan borrowers struggling to repay their loans or already in default, cleaning up the servicing market is critical . . .”).

11. *Who's My Loan Servicer?*, U.S. DEP'T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/understand/servicers> (last visited May 11, 2020).

12. Michael Stratford, *More States Pass Student Loan Servicer Laws*, POLITICO (May 15, 2019, 10:00 AM), <https://www.politico.com/newsletters/morning-education/2019/05/15/more-states-pass-student-loan-servicer-laws-436952>.

servicers.¹³ Moreover, private litigants are filing actions in droves, citing their servicers as the reason for their defaults.¹⁴

Federal student loan servicers did not create this crisis, however, and blaming the messenger only serves to obscure the complex system underpinning the federal student loan program as a whole. As a threshold matter, one of the key contributors to federal student loan defaults is the government's policy decision to fund a wide variety of unsecured student loans. The principal form of underwriting—the process by which a lender assesses a potential borrower's ability to repay and creditworthiness and adjusts the terms of the loan to align with the risk of repayment—in the student loan program is simply whether the student attends a Title IV-approved school.¹⁵ Unlike virtually every other extension of consumer credit, there is no underwriting of the student's assets, preexisting creditworthiness, prospects for graduation, area of study, or any other factor. And while the DoE has voluminous data regarding the cohort default rates based upon individual schools—data which demonstrate that graduates of some schools have a historically markedly higher probability of being able to repay their federal student loan debt—DoE explicitly does not take this loan data into account when approving loans, deciding how much to lend, or setting interest rates for individual borrowers. Thus, it is not surprising that many students find themselves unable to repay the loans to which they have committed themselves.

After federal student loan borrowers enter repayment, the complicated universe of federal financial assistance options pose another set of challenges

13. See generally Stacy Cowley, *New York Sues Student Loan Servicer for 'Abusive' Acts*, N.Y. TIMES (Oct. 3, 2019), <https://www.nytimes.com/2019/10/03/business/student-loans-forgiveness-pheaa.html> (detailing the alleged failures of a servicer proffered in a suit by New York's Attorney General); Nate Raymond, *Massachusetts Can Sue Federal Student Loan Servicer, Judge Rules*, REUTERS (Mar. 1, 2018, 1:04 PM), <https://www.reuters.com/article/us-massachusetts-education-law-suit/massachusetts-can-sue-federal-student-loan-servicer-judge-rules-idUSKCN1GD602> (presenting a ruling that allows the Attorney General of Massachusetts to proceed with a suit against student loan servicers).

14. Dena Aubin, *7th Circuit Revives Lawsuit Against Student Loan Servicer Great Lakes*, REUTERS (Jun. 28, 2019, 5:56 PM), <https://www.reuters.com/article/greatlakes-student-appeal/7th-circuit-revives-lawsuit-against-student-loan-servicer-great-lakes-idUSL2N23Z1T7>; Dena Aubin, *Penn. Student Loan Servicer Accused of Fraud in New Lawsuit*, REUTERS (Jan. 9, 2018, 4:21 PM), <https://www.reuters.com/article/pheaa-lawsuit/penn-student-loan-servicer-accused-of-fraud-in-new-lawsuit-idUSL1N1P41RN>; Chris Dunker, *Judge: Class-Action Suit Against Nelnet Can Move Forward*, LINCOLN J. STAR (July 13, 2019), https://journalstar.com/news/local/crime-and-courts/judge-class-action-suit-against-nelnet-can-move-forward/article_6d518f52-37f5-5946-a4f7-bb7acf97ea1c.html.

15. *Private Student Loans for Every Type of Student*, SALLIE MAE, <https://www.salliemae.com/student-loans/private-student-loans/> (last visited May 11, 2020) (discussing the role of credit in private student loans).

for borrowers. The current repayment assistance framework has been cobbled together over several decades and is governed by DoE's voluminous federal student loan servicing regulations and the overlapping—and at times conflicting—regulatory oversight splintered among both federal and state actors. Competing incentives within the federal loan sphere have resulted in a federal loan program rife with burdensome filing requirements for both borrowers and servicers which, in combination with the administrative complexities inherent in the regulatory framework, have contributed to borrower difficulties and increased operational costs for servicers. Despite these administrative challenges, the compensation for servicers has not increased in accordance with the increases in operating costs, and several mechanisms have actually reduced the resources federal student loan servicers have to help those borrowers most in need of assistance. This leaves student loan servicers in the difficult position of administering an evermore complicated student loan regime with ever-fewer resources.

Politicians and the public hold federal student loan servicers responsible for serving two competing constituencies. Federal student loan servicers are supposed to work with student loan borrowers to place them into the best repayment plan for their unique situations, all while collecting debts owed by these very same borrowers to the servicers' actual contractual client: the federal government. With such high rates of default and the corresponding increased costs involved with assisting delinquent debtors, the administrative system falls short of its goal to address the growing student loan crisis and help borrowers who are struggling with their payments find relief.

Overall, federal student loan servicers find themselves—often unfairly—in an untenable position as they are held responsible for systemic issues related to federal priorities in originating federal student loans, DoE's complicated servicing regulations, and the inherent economic challenges that arise from the federal student loan program. This Article will begin by describing the original goals of the federal student loan program, how historical changes in the governing statutory and regulatory framework have reconfigured the contours of the federal student loan servicing industry, and how that continues to influence the current, and very different, federal student loan regulatory ecosystem. Next, this Article will discuss the laws and regulations governing the modern federal student loan program, paying particular focus on the requirements for servicers and an analysis of the problems that result from such a complicated regime. This Article will conclude by recommending options that may alleviate the burden on servicers and allow them to operate more efficiently to the betterment of borrowers, the federal government, and the American taxpayers.

I. HOW WE GOT HERE: THE LEGAL FRAMEWORK GOVERNING FEDERAL STUDENT LENDING

A. *The Uniqueness of Federal Student Debt: How Much Would You Lend on an Unsecured Basis to a Twenty-Year-Old with Neither a Credit History nor a Job?*

Every class of consumer debt—mortgages, installment federal loans, credit cards—has its own nuances, but all of these forms of debt have one thing in common that does not exist for federal student loans: underwriting.

For federal student loans, the student picks the school, the school sets its own tuition rate without oversight from the federal government, and the federal government originates the loan for tuition—plus reasonable costs for fees, books, and room and board—all without regard to the student’s credit history, income, assets, or ability to repay. No other major creditor issues debt without any analysis of whether the borrower will actually be able to pay the loan back. In fact, both investors and prudential regulators demand that private sector lenders engage in safe and sound practices that take into account consumers’ ability to repay their debts.¹⁶ Even government and quasi-government entities tasked with expanding homeownership (including Fannie Mae, Freddie Mac, and the Department of Veterans Affairs) all have robust underwriting guidelines.¹⁷

Underwriting serves two critical purposes. First, underwriting serves to protect a creditor’s overall balance sheet from losses. It allows the creditor to fully analyze the level of risk involved in the loan and craft the terms and conditions to account for that level of risk—and in so doing helps the creditor remain solvent so it can continue to serve as a source of funding for other consumers. Just as importantly, however, underwriting also protects borrowers. It provides a check on unrestricted borrowing to reduce the likelihood that borrowers take on more debt than they can reasonably repay. While not a panacea for loan defaults, the underwriting process provides critical

16. See, e.g., NAT’L RISK COMM., OFFICE OF THE COMPTROLLER OF THE CURRENCY, SEMIANNUAL RISK PERSPECTIVE ii, 1 (2018), <https://www.occ.gov/publications-and-resources/publications/semiannual-risk-perspective/files/pub-semiannual-risk-perspective-spring-2018.pdf>.

17. FANNIE MAE, SELLING GUIDE: FANNIE MAE SINGLE FAMILY 283–529 (2019), <https://www.fanniemae.com/content/guide/sel100219.pdf> (outlining Fannie Mae’s underwriting requirements); FREDDIE MAC, SELLER/SERVICER GUIDE (2019), https://guide.freddiemac.com/ci/okcsFattach/get/1002095_2_series_5000 (outlining Freddie Mac’s underwriting requirements); U.S. DEP’T OF VETERANS AFFAIRS, VA PAMPHLET 26–7, ch. 4 (rev. Apr. 10, 2009), https://www.benefits.va.gov/WARMS/docs/admin26/pamphlet/pam26_7/ch04.pdf (outlining VA’s underwriting guidelines).

information to both the lender and borrower so that both parties can responsibly enter into a credit decision.¹⁸

We should hardly be surprised, then, when a class of consumer loans issued without any form of underwriting results in high default rates. Of all of the various types of household debt—mortgage loans, auto loans, unsecured personal loans, and credit card debt—federal student loans consistently have the highest rate of delinquency.¹⁹ All other forms of consumer debt declined during and after the Great Recession—in significant part because of investor and prudential financial regulators insisting on more careful underwriting to protect both creditors and borrowers—but federal student debt has steadily risen.²⁰ This is due in part to individuals electing to obtain additional credentials with the hope of reentering a recovered job market in a better position,²¹ and in part due to the tuition and fees required to obtain a college or advanced degree increasing faster than the rate of inflation.²² This combination of unlimited funds, a growing numbers of borrowers, increasing loan amounts, and climbing delinquency rates is placing an unprecedented strain on the federal student loan financing and servicing system.

And while many assume that the effect of the federal student debt crisis is limited only to those in their twenties and thirties, the modern student loan market is far more diverse. In fact, one of the fastest growing segments of consumers with student debt is individuals over sixty years old that otherwise would be on the threshold of retirement.²³ Nearly 870,000 borrowers

18. This Article should not be read as a criticism of the federal government's policy decision to provide federal student loans to students without regard for their ability to repay. Quite the opposite—we see great value in the government encouraging individuals to learn about a wide variety of topics, engage in critical thinking, and enrich both themselves and their communities. However, we appreciate that higher education is not free, and policymakers and students would do well to consider how we treat federal student loan debt once repayment begins.

19. META BROWN ET AL., MEASURING STUDENT DEBT AND ITS PERFORMANCE 9–10 (2014), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr668.pdf.

20. *Id.* at 4.

21. See Beth Pinsker, *Grad School Can Be Worth It if You Pick Wisely: Study*, REUTERS (Jan. 10, 2018, 10:06 PM), <https://www.reuters.com/article/us-money-education-gradstudents/grad-school-can-be-worth-it-if-you-pick-wisely-study-idUSKBN1F009O> (weighing returns on investment for areas of secondary education).

22. Camilo Maldonado, *Price of College Increasing Almost 8 Times Faster than Wages*, FORBES (July 24, 2018, 8:23 AM), <https://www.forbes.com/sites/camilomaldonado/2018/07/24/price-of-college-increasing-almost-8-times-faster-than-wages/#303894e466c1>.

23. See U.S. GOV'T ACCOUNTABILITY OFF., GAO-17-45, SOCIAL SECURITY OFFSETS: IMPROVEMENTS TO PROGRAM DESIGN COULD BETTER ASSIST OLDER STUDENT LOAN BORROWERS WITH OBTAINING PERMITTED RELIEF 1–2 (2016) [hereinafter 2016 GAO], <http://www.gao.gov/assets/690/681722.pdf>.

age sixty-five or older owed federal student loans as of 2015.²⁴ There is a growing set of data showing that student loan debt impacts the most vulnerable segments of society the hardest, including military families, women, people of color, and rural communities.²⁵ Moreover, on average the borrowers with the highest rates of default are those with the smallest amount of outstanding debt.²⁶

B. The Evolution of Federal Student Loans: From World War II to Underwater Basket Weaving

The federal student loan program began with the passing of the Servicemen's Readjustment Act in 1944, more commonly known as the GI Bill, which allowed veterans of World War II to attend college using federal benefits.²⁷ As a result of the GI Bill, the number of adults attending college more than tripled.²⁸ The National Defense Education Act, enacted in 1958, created the first federal student loans backed by the federal government which

24. See *id.* at 8–9.

25. *Soldiers as Consumers: Predatory and Unfair Business Practices Harming the Military Community: Hearing Before the Comm on Commerce, Sci., and Transp.*, 113th Cong. 4 (2013), <https://www.govinfo.gov/content/pkg/CHRG-113shrg89464/pdf/CHRG-113shrg89464.pdf> (testimony of Admiral Mike Mullen) (“A sailor’s financial readiness directly impacts unit readiness and the Navy’s ability to accomplish its mission . . .”); *Women’s Student Debt Crisis in the United States*, AM. ASS’N OF UNIV. WOMEN, <https://www.aauw.org/research/deeper-in-debt/> (last updated May 2019); *Report: Defaulted Federal Student Loan Borrowers in Communities of Color Are Disproportionately Sued*, NAT’L CONSUMER LAW CTR. (Apr. 24, 2019), <https://www.nclc.org/media-center/report-defaulted-federal-student-loan-borrowers-in-communities-of-color-are-disproportionately-sued.html>; PJ Tabit & Josh Winters, *supra* note 9, at 7. See, e.g., HOLLISTER PETRAEUS & SETH FROTMAN, CONSUMER FIN. PROT. BUREAU, OVERSEAS & UNDERSERVED: STUDENT LOAN SERVICING AND THE COST TO OUR MEN AND WOMEN IN UNIFORM 3–5 (2015), https://files.consumerfinance.gov/f/201507_cfpb_overseas-underserved-student-loan-servicing-and-the-cost-to-our-men-and-women-in-uniform.pdf.

26. See FED. RESERVE QUARTERLY REPORT, *supra* note 2.

27. CHARMAINE MERCER & REBECCA R. SKINNER, CONG. RESEARCH SERV., RL33281, MONTGOMERY GI BILL EDUCATION BENEFITS: ANALYSIS OF COLLEGE PRICES AND FEDERAL STUDENT AID UNDER THE HIGHER EDUCATION ACT 2 (2007); Servicemen’s Readjustment Act of 1944, Pub. L. No. 78-346, 58 Stat. 284, 287–89 (codified as amended in scattered sections of 38 U.S.C.).

28. Jennifer Wadia, *Rising Tuition Costs and the History of Student Loans*, STUDENT DEBT RELIEF (Oct. 21, 2019), <https://www.studentdebtre relief.us/news/rising-tuition-costs-and-the-history-of-student-loans/>.

were offered to encourage students to pursue math and science degrees during the Cold War's focus on aerospace.²⁹ The program set up by the National Defense Education Act is still in existence today, albeit in a slightly different form, as the Federal Perkins Loan Program.³⁰

Although we often take for granted the federal government's financial support for the availability of higher education for all, it is a relatively recent development. The Higher Education Act (HEA) was enacted in 1965 to solidify and expand the federal government's involvement in higher education.³¹ First signed into law by President Lyndon B. Johnson, the HEA was a part of his education message to improve access to higher education for middle and lower income families.³² This message continued to gain traction in American culture such that beginning in the 1970s, more students from various socioeconomic backgrounds began attending college.³³ Around this time, the Student Loan Marketing Association, also known as Sallie Mae, was created as a government-sponsored enterprise dedicated to administering both federal and private federal loans for college students.³⁴ Just thirteen years later, in 1978, the

29. See National Defense Education Act of 1958, Pub. L. No. 85-864, 72 Stat. 1580, 3702-03 (codified as amended in scattered sections of 20 U.S.C.).

30. *Id.* at 3702, 3706-08 (forming the loan program for qualifying students studying science and engineering, later relabeled the Perkins Loans Program); Higher Education Amendments of 1992, Pub. L. No. 102-325, § 461, 106 Stat. 448, 576 (codified as amended at 20 U.S.C. § 1087a (2018)).

31. Higher Education Act of 1965, Pub L. No. 89-329, 79 Stat. 1219 (codified as amended in scattered sections of 20 U.S.C.); see also 20 U.S.C. §§ 1070-1099e (2018) (increasing the availability of funding for secondary education). See generally ANGELICA CERVANTES ET AL., TG RES. & ANALYTICAL SERVS., OPENING THE DOORS TO HIGHER EDUCATION: PERSPECTIVES ON THE HIGHER EDUCATION ACT 40 YEARS LATER (2005), <https://files.eric.ed.gov/fulltext/ED542500.pdf> (articulating the purpose and impact of the Higher Education Act).

32. CERVANTES, *supra* note 31, at 1, 17-18.

33. See NAT'L CTR. FOR EDUC. STATISTICS, U.S. DEP'T OF EDUC., 120 YEARS OF AMERICAN EDUCATION: A STATISTICAL PORTRAIT 66 (Thomas D. Snyder ed., 1993), <https://nces.ed.gov/pubs93/93442.pdf> (noting enrollment rose by 45% in the 1970s).

34. See CERVANTES, *supra* note 31, at 24; ERIN DILLON, AM. INSTS. FOR RESEARCH, LEADING LADY: SALLIE MAE AND THE ORIGINS OF TODAY'S STUDENT LOAN CONTROVERSY (2007), <http://www.educationsector.org/sites/default/files/publications/SallieMae.pdf> [<http://perma.cc/WJK9-3TEX>] (noting benefits received by Sallie Mae as GSE). Beginning in 1991, discussions regarding privatizing Sallie Mae began circulating in Congress. U.S. DEP'T OF THE TREASURY, OFFICE OF SALLIE MAE OVERSIGHT, LESSONS LEARNED FROM THE PRIVATIZATION OF SALLIE MAE 1-2, 7-8 (2006), <https://www.treasury.gov/about/organizational-structure/offices/Documents/SallieMaePrivatizationReport.pdf>. The Clinton Administration supported the privatization and worked out a proposal for Congress that would either provide for privatization if the shareholders approved, or Sallie Mae's dissolution if such approval was denied. *Id.* at 27, 49. This legislation picked up traction and in 1996, Congress

Middle Income Student Assistance Act eliminated the income requirement for federal student loans, allowing middle and high income students to qualify for federal loans.³⁵ Although this Act was repealed in 1981,³⁶ it represented a significant shift in attitudes towards higher education and in favor of the then-novel position that all Americans should have the chance to attend college.

The HEA has been reauthorized a handful of times over the past few decades, all with the purpose of offering borrowers greater access to the federal student loan program. These reauthorizations have created various borrower protections in the form of additional repayment plans, deferment, and forgiveness options, adding depth and complexity to the federal student loan program. The HEA created the Federal Family Education Loan Program (FFELP), which was the primary source of federal loans from 1965 through 2010, when the Student Aid and Fiscal Responsibility Act terminated the authority to make new FFELP loans.³⁷ Because in 1965 the government did not have a mechanism in place to issue thousands of federal student loans, FFELP loans were originated by private lenders but were guaranteed by the federal government.³⁸ Although FFELP loans are no longer being made, outstanding FFELP loans will continue to be repaid over the coming years.³⁹

The 1993 Student Loan Reform Act created the William D. Ford Direct Loan Program, which—since the end of FFELP in 2010—is the primary federally subsidized student loan program.⁴⁰ The government shifted from the FFELP/guarantor model to the Direct Loan/originator model with the hopes of streamlining delivery of federal student loans to students and saving

enacted amendments to the Higher Education Act (HEA) providing for the reorganization and dissolution of Sallie Mae. *Id.* at 49. Resultantly, in 1997, Sallie Mae incorporated as SLM Corporation under the laws of Delaware and the government-sponsored entity became a subsidiary of SLM Corporation. SLM Corp., Annual Report (Form 10-K) 1 (Mar. 1, 2018). On November 3, 2005, SLM Corporation formed Sallie Mae Bank, a Utah industrial bank subsidiary to fund and originate private education loans on behalf of SLM Corporation. *Id.* at 3. On April 30, 2014, SLM Corporation legally separated into two distinct entities: Navient Corporation (“Navient”), an “education loan management, servicing, and asset recovery business,” and a consumer banking business, named SLM Corporation. *Id.*

35. Middle Income Student Assistance Act, Pub. L. No. 95-566, 92 Stat. 2402 (1978).

36. Omnibus Budget Reconciliation Act of 1981, Pub. L. No. 97-35, 95 Stat. 357 (codified at scattered sections and titles of U.S.C.)

37. CERVANTES, *supra* note 31, at 24; ALEXANDRA HEGJI, CONG. RESEARCH SERV., R43351, THE HIGHER EDUCATION ACT (HEA): A PRIMER 13–14 (2018), <https://crsreports.congress.gov/product/pdf/R/R43351>.

38. *See* HEGJI, *supra* note 37, at 13–14.

39. *Id.* at 14.

40. *See* 20 U.S.C. § 1087a (2018) (authorizing the creation of the William D. Ford Direct Loan Program).

costs for the federal government.⁴¹ Under the Direct Loan program, the federal government, through DoE, as the lender of record, provides federal loans to students and their families using funds from the United States Treasury, and retains ownership of the Direct Loans. As of September 30, 2019, Direct Loans make up over eighty percent of outstanding federal student debt.⁴² In recent years, many changes have been made to the terms and conditions of Direct Loans, including the College Cost Reduction and Access Act of 2007,⁴³ the Ensuring Continued Access to Student Loans Act of 2008,⁴⁴ and the Bipartisan Student Loan Certainty Act of 2013.⁴⁵ As described in Section IV *infra*, contrary to their legislative titles that suggest these laws had addressed the weaknesses in the federal student loan program, these statutes added new facets to the program without simplifying the repayment puzzle that borrowers face.

In addition to creating the overall federal student loan program, federal law also mandates the creation of borrower assistance programs.⁴⁶ These programs have taken three primary forms, with several variations within each: (1) repayment plans, which focus on reducing borrowers' monthly payments to ensure that borrowers are able to stay current; (2) deferment and forbearance programs, which provide for the temporary cessation of payments altogether due to unstable financial conditions; and (3) forgiveness and cancellation plans, which terminate any outstanding student loan balance after a certain repayment period.

These borrower assistance laws and their implementing regulations are driven by two important yet competing priorities. On the one hand, Congress and DoE want to provide assistance to borrowers and their families who

41. CONG. RESEARCH SERV., R40122, FEDERAL STUDENT LOANS MADE UNDER THE FEDERAL FAMILY EDUCATION LOAN PROGRAM AND THE WILLIAM D. FORD FEDERAL DIRECT LOAN PROGRAM: TERMS AND CONDITIONS FOR BORROWERS 1–3, 14 (2013), <https://crsreports.congress.gov/product/pdf/R/R40122>.

42. *Student Aid Portfolio*, *supra* note 1 (FSA Portfolio Summary for Q3 2019).

43. See College Cost Reduction and Access Act, Pub. L. No. 110-84, 121 Stat. 784 (2007) (codified as amended in scattered sections of 20 U.S.C.) (establishing the Public Service Loan Forgiveness program and a new Income-Based repayment plan, among other appropriations and amendments to the HEA).

44. See Ensuring Continued Access to Student Loans Act of 2008, Pub. L. No. 110-227, 122 Stat. 740 (codified as amended in scattered sections of 20 U.S.C.) (increasing the maximum allowable amounts of certain types of federal loans).

45. See Bipartisan Student Loan Certainty Act of 2013, Pub. L. No. 113-28, 127 Stat. 506 (establishing set interest rates for federal student loans).

46. See 20 U.S.C. ch. 28, subchapter IV, pt. G.

are facing temporary or permanent financial hardships such as the temporary loss of a job, medical emergencies, permanent disability, or death.⁴⁷ However, as with all government assistance programs, Congress and DoE want to protect these programs—and to ensure, to the greatest extent possible, that the \$1.5 trillion which has been lent is repaid by the borrowers who borrowed (and thus hopefully benefitted from) the funds and not the taxpayers.⁴⁸ Like all Great Society federal benefit programs from the Great Society era and since, federal student lending programs have been attacked as being rife with fraud and waste and those that administer the programs work to allay claims of such abuses.

II. CONTRACT AND CODE: LAWS GOVERNING THE SERVICING OF FEDERAL STUDENT LOANS

Combined, these various programs have created a massive portfolio of federal student loans that are guaranteed or were issued outright by the federal government. Today, DoE is—by more than an order of magnitude—the largest student loan holder in the country and effectively “the largest special purpose consumer bank in the world,”⁴⁹ with a portfolio of nearly \$1.5 trillion.⁵⁰ Because of DoE’s unique position as both a creditor and a federal agency, there are two main bodies of law that govern federal student loan servicers’ day-to-day interactions with borrowers: servicers’ contracts with DoE and federal regulations promulgated by DoE.

Unlike most creditors, Congress has directed DoE to enter into contracts for the servicing of its loan portfolio.⁵¹ To collect federal student loan debt,

47. ALEXANDRA HEGJI ET AL., CONG. RESEARCH SERV., R43571, FEDERAL STUDENT LOAN FORGIVENESS AND LOAN REPAYMENT PROGRAMS (2018), <https://crsreports.congress.gov/product/pdf/R/R43571>.

48. See *Student Aid Portfolio*, *supra* note 1; Zack Friedman, *These 76,000 People May Have Committed Student Loan Fraud*, FORBES (July 29, 2019, 8:32 AM), <https://www.forbes.com/sites/zackfriedman/2019/07/29/student-loan-repayment-fraud/#1c5244a63aff> (quoting Department of Education (DoE) Secretary Betsy DeVos on student loan repayment fraud: “[m]isrepresenting income or family size is wrong, and we must have a system in place to ensure that dishonest people do not get away with it”).

49. Press Release, U.S. Dep’t of Educ., Secretary DeVos Announces Intent to Enhance FSA’s Next Generation Processing and Servicing Environment (Aug. 1, 2017), <https://www.ed.gov/news/press-releases/secretary-devos-announces-intent-enhance-fsas-next-generation-processing-and-servicing-environment>.

50. See *Student Aid Portfolio*, *supra* note 1 (totaling the third quarter of 2019); Ben Miller et al., *Addressing the \$1.5 Trillion in Federal Student Loan Debt*, CTR FOR AM. PROGRESS (June 12, 2019, 5:00 AM), <https://www.americanprogress.org/issues/education-postsecondary/reports/2019/06/12/470893/addressing-1-5-trillion-federal-student-loan-debt/>.

51. 20 U.S.C. § 1087f(b)(4) (2018).

DoE has contracts with fifteen different student loan servicers, but the majority of its portfolio is allocated to three servicers: Navient Corporation (Navient), Nelnet, Inc. (Nelnet), and Pennsylvania Higher Education Assistance Agency (PHEAA). For these servicers, DoE is their largest client, and they are required to work cooperatively with DoE in collecting debt and protecting federal funds.⁵²

These servicing relationships are governed by highly complicated contracts. The vast majority of requirements for federal student loan servicers are contained within the contracts, as opposed to in the statutes governing the federal student loan program or DoE regulations. As a result, federal student loan servicing contracts span more than 600 pages and make federal student loan servicers responsible for every single aspect of servicing federal student loans and collecting debt. These contracts address in detail such broad topics as sending borrowers statements, collecting payment, applying payments to outstanding loan balances, processing applications for enrollment in repayment plans, evaluating borrowers' applications for loan forgiveness or discharge, responding to borrowers' requests for loan forbearance or deferment, disclosing information about student loan terms to borrowers, and communicating with borrowers regarding their loan repayment, deferment, forbearance, and forgiveness options.⁵³ These contracts make clear that the servicers are responsible for all supplies, services, and other costs involved in administering the federal student loans.⁵⁴

Compared to the magnitude of the tasks facing these servicers, DoE's payments to its student loan servicers are meager. DoE compensates its servicers with a fixed monthly payment per loan with slight variations in compensation depending on the status of the loan. For example, federal loans that are in grace or current repayment status are paid a premium, at \$2.11 per loan.⁵⁵ Loans in deferment or forbearance are paid slightly less than current federal loans, at \$2.07 per loan.⁵⁶ However, delinquent federal loans possess an even lower unit price dependent on the amount of

52. *Servicer Performance Metrics and Allocations*, OFFICE OF FED. STUDENT AID, <https://studentaid.ed.gov/sa/about/data-center/business-info/contracts/loan-servicing/servicer-performance> (last visited May 11, 2019).

53. See Great Lakes Educational Loan Services, Inc. Servicing Contract No. ED-FSA-09-D-0012, OFFICE OF FED. STUDENT AID, Attach. A-3, 3-4 (2009), <https://www2.ed.gov/policy/gen/leg/foia/contract/greatlakes-061709.pdf> [hereinafter Great Lakes Servicing Contract].

54. *Id.* at Attach. A-2, 10-11; see OFFICE OF INSPECTOR GEN., U.S. DEP'T OF EDUC., FED. STUDENT AID: ADDITIONAL ACTIONS NEEDED TO MITIGATE THE RISK OF SERVICER NONCOMPLIANCE WITH REQUIREMENTS FOR SERVICING FEDERALLY HELD STUDENT LOANS 6-7 (2019), <https://www2.ed.gov/about/offices/list/oig/auditreports/fy2019/a05q0008.pdf>.

55. Great Lakes Servicing Contract, *supra* note 53, at 13.

56. *Id.*

time that the loan has been delinquent.⁵⁷ For example, a loan that is between thirty-one and ninety days delinquent is worth \$1.62, while servicers with federal loans that are between 151 and 270 days delinquent are only compensated at \$1.37 per loan.⁵⁸

Through this compensation structure, DoE attempts to incentivize servicers to keep borrowers out of delinquency by paying a modest premium for federal loans that are in a current status. While this may intuitively make sense, this structure fails to take into account the costs imposed on servicers when federal loans are on the brink of or already in delinquency in the form of increased efforts to contact the delinquent borrower and interactions with the borrower to help ease them into a more feasible repayment option. In 2015 alone, DoE reported that federal student loan servicers placed and received more than 250 million phone calls and sent out 687 million emails and correspondence; to keep their costs in check, federal student loan servicers placed this burden on fewer than 9,500 servicing employees.⁵⁹ These costs and the compensation structure do not reflect the effort required to contact delinquent borrowers—phone calls, mailing letters, and sending emails cost servicers significant money that easily outstrips the \$1.37 monthly payment that DoE is willing to pay to servicers for these federal student loans.

The combination of these two contractual features—the low price point at which DoE compensates federal student loan services and their inability to shift certain increased and/or non-bargained for costs associated with servicing—is unique among the other forms of consumer debt. The mortgage servicing industry serves as a useful analogue in understanding the novelty of the federal student loan servicing compensation structure. Like federal student loan servicers, in the mortgage servicing industry private companies also contract with the federal government (the Federal Housing Authority, the Veterans Administration, etc.) to service loans that the federal government originated, insured, or guaranteed.⁶⁰ However, mortgage servicers that contract with the federal government are compensated at much higher rates than federal student loan servicers, despite the similarities in the forms of debt

57. *Id.*

58. *Id.*

59. Lisa Oldre & John Brooks, Office of Fed. Student Aid, U.S. Dep't of Educ., Presentation at the 2015 FSA Training Conference for Financial Aid Professionals: Servicing Update 5 (Dec. 2015), <https://fsaconferences.ed.gov/conferences/library/2015/2015FSAConfSession17.ppt>.

60. *Servicers of VA Loans*, U.S. DEP'T OF VETERANS AFFAIRS, <https://www.benefits.va.gov/homeloans/servicers.asp> (last updated Nov. 30, 2015); VETERANS BENEFITS ADMIN., U.S. DEP'T OF VETERANS AFFAIRS, VA SERVICER GUIDE (2009), https://www.benefits.va.gov/HOMELOANS/documents/docs/va_servicer_guide.pdf.

and that both forms of servicers must expend greater resources in communicating with borrowers, whether delinquent, defaulted, or current.⁶¹ To further monitor and incentivize efficiency among its student loan servicers, DoE uses a metrics-based performance evaluation system to assess servicers' performance.⁶² This evaluation system incorporates customer satisfaction ratings, as well as the percentage of a servicers' borrowers who are (i) current on their loan repayment, (ii) in default, or (iii) more than ninety, but less than 270, days delinquent.⁶³ When student loan servicing contracts are up for renewal, these metrics are a critical part of contract negotiations between servicers and DoE.⁶⁴ In an attempt to encourage ongoing competition among its student loan servicers, in 2014⁶⁵ DoE introduced a new performance metric that on a biannual basis reallocates assignments of federal loans based upon servicer performance.⁶⁶

III. THE REPAYMENT PUZZLE: FEDERAL BORROWER ASSISTANCE PROGRAMS

Under the rulemaking authority vested in the DoE pursuant to Title IV of the HEA, DoE has promulgated numerous regulations governing the servicing of FFELP loans, and to a lesser extent Direct Loans.⁶⁷ These regulations

61. See, e.g., *A2-3-01: Servicer Compensation*, FANNIE MAE (Dec. 14, 2016), <https://www.fanniemae.com/content/guide/servicing/a2/3/01.html> (describing the servicing fees for mortgage servicers and generally linking the amount of compensation to the interest collected on the loan).

62. DEANNE LOONIN ET AL., *STUDENT LOAN LAW* 63–64 (5th ed. 2015).

63. OFFICE OF FED. STUDENT AID, DEP'T OF EDUC., *Explanation of Allocation and Performance Measure Methodology* (2016), <https://studentaid.gov/sites/default/files/ExplanationQuarterEnd093015.pdf>.

64. *Id.*

65. STUDENT AID ADMIN., DEP'T. OF ED., *FISCAL YEAR 2016 BUDGET REQUEST 9* (2015), <https://www2.ed.gov/about/overview/budget/budget16/justifications/z-saa.pdf>.

66. *Explanation of Allocation and Performance*, supra note 63, at 1. The renegotiation also called for delinquency to be surveyed on a quarterly basis. *Id.* at 3.

67. 34 C.F.R. §§ 682.100–682.713 (2018). There remains some uncertainty whether and to what extent DoE's Federal Family Education Loan Program (FFELP) regulations apply to the servicing of Direct Loans. The majority of DoE regulations governing the terms of student loan servicing are found in Part 682 of the Code of Federal Regulations, governing the administration of FFELP loans. The Ninth Circuit, using the text of the HEA as a guide, ruled that DoE's FFELP regulations should apply equally to Direct Loans. See *Chae v. SLM Corp.*, 593 F.3d 936, 945 (9th Cir. 2010) (“Congress’s instructions to [DoE] on how to implement the student-loan statutes carry this unmistakable command: Establish a set of rules that will apply across the board.” (citing 20 U.S.C. § 1087e(a)(1))). However, the issue is not conclusively resolved since courts considering whether FFELP regulations apply to Direct Loans outside the loan servicing context have come down on both sides of the question. Compare *Won v. Nelnet Servicing, LLC*,

impose a variety of disclosures that servicers must issue before repayment begins, during repayment, and when borrowers are facing difficulty in making their monthly payments.⁶⁸ When actually collecting borrower payments, DoE regulations prescribe a number of actions that a servicer must take when servicing a FFELP loan, including “responding to borrower inquiries, establishing the terms of repayment, and reporting a borrower’s enrollment and loan status information.”⁶⁹

Specific DoE regulations govern the calculation of monthly payment obligations for federal student loans, based upon the wide variety of repayment schedules available to borrowers.⁷⁰ Elsewhere, DoE’s regulations establish administrative and financial responsibility standards that servicers must satisfy, in addition to the separate requirements contained within the servicing contracts.⁷¹ Should a servicer violate any of these federal requirements, DoE’s regulations establish a variety of procedures for addressing such violations, including administrative proceedings to limit, suspend, or terminate a servicer’s eligibility to enter into servicing contracts.⁷² Because of the relative paucity of promulgated regulations, a substantial majority of the guidance for servicers of Direct Loans lies within the servicing contracts, rather than the regulations.

While DoE’s contractual and administrative requirements pose challenges to several aspects of federal student loan servicers, perhaps the most obvious area of regulatory difficulty is assisting borrowers who are delinquent or in default.⁷³ The number of similar-sounding options, the particularized requirements that a borrower must meet to qualify for each one, and the

No. 18-00381 ACK-RLP, 2019 WL 1548572, at *3 n.7 (D. Haw. Apr. 9, 2019) (concluding that FFELP regulations pertaining to loan rehabilitation agreements do not apply to Direct Loans), *with* Weber v. Great Lakes Educ. Loan Servs., Inc., No. 13-cv-00291-wmc, 2013 WL 3943507, at *2 n.2, *3 (W.D. Wis. July 30, 2013) (crediting defendant’s position that FFELP loan collection regulation applied equally to Direct Loans). As seen in the case law, the uncertainty as to the application of FFELP regulations to the servicing of Direct Loans is an additional element contributing to the difficulties of servicing federal student loans.

68. 34 C.F.R. § 682.205 (2018).

69. *Id.* § 682.208.

70. *See id.* § 682.209 (laying out the repayment schedules based upon the repayment plan).

71. *Id.* § 682.416.

72. *Id.* § 682, subpart G.

73. The DoE defines default as the “failure of a borrower . . . to make an installment payment when due, or to meet other terms of the promissory note, if the Secretary finds it reasonable to conclude that the borrower . . . no longer intend[s] to honor the obligation to repay, provided that this failure persists for 270 days.” 34 C.F.R. § 685.102(b). Although “delinquent” is not defined in the Code of Federal Regulations, FSA provides that loans be-

unique servicing demands that these impose on federal student loan servicers all contribute to dissatisfaction with the current system. Since 1990, the number of repayment options have increased from two to fifteen, each with different eligibility criteria.⁷⁴ There are currently thirteen different forgiveness programs and over thirty-five deferment and forbearance options.⁷⁵

Repayment—the most straightforward of these categories—covers federal loans on which borrowers are making payments as agreed to by the servicer and where the loan is treated as being current. Even within this category, a non-exhaustive list of the repayment plans available for federal student loans includes Standard Repayment, Graduated Repayment, Extended Repayment, Pay As You Earn, Revised Pay As You Earn, Income-Based Repayment, Income-Contingent, and Income-Sensitive Repayment.⁷⁶ For borrowers seeking to qualify for these plans and the servicers trying to administer them, federal regulations impose strict income limits, documentation requirements, and requalification demands that must be met.⁷⁷

Loan forgiveness options—where the servicer agrees to excuse the borrower from having to repay the outstanding balance on a federal student loan—are a patchwork targeting specific borrowers and careers where Congress and DoE have decided that a public benefit outweighs the loss of revenue for the federal government. The most popular federal student loan forgiveness programs are Public Service Loan Forgiveness, certain types of Perkins Loan cancellations, Teacher Forgiveness Program, NURSE Corps Loan Repayment Program, National Health Service Corps Loan Repayment Assistance, Indian Health Services Loan Repayment Program, Active

come delinquent “the first day after [a borrower] miss[es] a payment.” *Understanding Delinquency and Default*, DEP’T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/default> (last visited May 11, 2020).

74. CONSUMER FIN. PROT. BUREAU, *STUDENT LOAN SERVICING: ANALYSIS OF PUBLIC INPUT AND RECOMMENDATIONS FOR REFORM 20* (2015), https://files.consumerfinance.gov/f/201509_cfpb_student-loan-servicing-report.pdf [hereinafter PUBLIC INPUT ANALYSIS].

75. Dori Zinn, *The Complete List of Student Loan Forgiveness Programs and Options*, STUDENT LOAN HERO (Jan. 2, 2019), <https://studentloanhero.com/featured/the-complete-list-of-student-loan-forgiveness-programs/>; *Deferment and Forbearance*, DEP’T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/deferment-forbearance> (last visited May 11, 2020).

76. *Repayment Plans*, DEP’T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/understand/plans> (last visited May 11, 2020). While these repayment plans apply to Direct and FFELP Loans, there is an entirely different set of repayment plans that apply specifically to federal Perkins loans. *Perkins Loans*, DEP’T OF EDUC., <https://studentaid.ed.gov/sa/types/loans/perkins> (last visited May 11, 2020).

77. See, e.g., 34 C.F.R. § 682.215 (mandating the eligibility criteria for Income-Based Repayment); *id.* § 685.209 (mandating the eligibility criteria for Pay as You Earn repayment and Revised Pay as You Earn repayment).

Duty Health Professionals Loan Repayment Program, and the Attorney Student Loan Repayment Program.⁷⁸

Finally, deferment and forbearance give federal student loan borrowers a temporary reprieve from making payments. In deferment, interest typically does not accrue on the loan balance during the period when the borrower is not making payments. Some of the deferment options include: In-School Deferment, Cancer Treatment Deferment, Unemployment Deferment, Economic Hardship Deferment, and Military Service and Post-Active Duty Student Deferment.⁷⁹ Forbearance—where the borrower need not make payments, but accruing interest will increase the overall loan balance—includes Medical or Dental Internship/Residency, National Guard Duty, Student Loan Debt Burden, AmeriCorps, and the Teacher Loan Forgiveness Forbearance.⁸⁰

DoE's regulations regarding these various repayment programs place student loan servicers in an unenviable position. On one hand, DoE has specifically tasked federal student loan servicers with explaining these programs to borrowers and assisting borrowers in making an informed decision.⁸¹ At the same time, DoE also requires its student loan servicers to enforce these programs' requirements, and the strict qualification criteria for each program means that many borrowers who believe that they are entitled to enter a certain program may not qualify or may not be able to produce the required documentation to demonstrate that they are eligible for the program. This leaves borrowers unsatisfied with their outcome, and federal student loan program servicers—who have no control over the regulations they are required by law to enforce—are left to answer complaints from borrowers and regulators alike.

For example, forbearance is a way for a borrower who encounters a short-term financial hardship to obtain temporary relief from his or her obligation to repay a federal student loan. In forbearance, interest will continue to accrue during the forbearance period and is then added to the loan principal when the forbearance period ends (a process known as capitalizing interest).⁸² Income-driven repayment plans (IDR), on the other hand, are designed to help borrowers stay in good standing on their federal student loans when a standard ten year repayment plan would not be affordable based upon the borrower's monthly income. This is achieved by calculating the monthly payment amount as a portion of the borrower's monthly disposable income

78. *Forgiveness, Cancellation, and Discharge*, DEP'T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/forgiveness-cancellation> (last visited May 11, 2020).

79. *Deferment and Forbearance*, *supra* note 75.

80. *Id.*

81. 34 C.F.R. § 682.205.

82. *Deferment and Forbearance*, *supra* note 75.

as opposed to a percentage of the overall loan amount.⁸³ However, when a borrower's income falls below a certain threshold, the monthly payment may not be large enough to cover the interest that is accruing, resulting in negative amortization, or a growing balance in the outstanding debt.⁸⁴ While some borrowers may view this as a harmful outcome, other borrowers can benefit from IDR, such as those who are planning on having their federal loans forgiven through another federal program, are in a graduate program that will increase their earning capacity in a few years, or those who are working to pay down higher interest debts (such as credit card debt) first.⁸⁵

The forbearance versus IDR puzzle is magnified when the borrower is delinquent, because a delinquent borrower is not eligible for IDR unless they bring their federal loans current. This is typically done through forbearance because it allows borrowers a short period of time to repay late payments. According to Navient, nearly seventy percent of IDR borrowers needed to enter a brief forbearance period to bring their accounts current to be eligible for IDR and time to complete the mandatory IDR application.⁸⁶ Nevertheless, regulators have targeted federal student loan servicers for improperly "steering" borrowers toward forbearance over IDR.⁸⁷ Such actions fail to take into account the reality that forbearance is often the only option for a delinquent borrower to become eligible for IDR; such actions effectively serve to punish servicers for following federal law.

Based upon the borrower's reason for hardship, expected future income, current interest rate, other financial obligations, and other factors, either forbearance or IDR (or a combination of the two) might be the right decision for a particular borrower. However, it is difficult for a federal student loan servicer

83. See 34 C.F.R. § 685.221(b)(1) (mandating that a borrower's aggregate monthly payment under Income-Based Repayment is "limited to no more than fifteen percent or, for a new borrower, ten percent of the amount by which the borrower's [adjusted gross income] exceeds 150 percent of the poverty guideline applicable to the borrower's family size, divided by 12").

84. See *id.* § 685.221; see also *Income-Driven Plans Questions and Answers*, DEP'T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/understand/plans/income-driven/questions> (last visited May 11, 2020).

85. See *Deferment and Forbearance*, *supra* note 75.

86. *Fact Sheet on Legal Action*, NAVIENT (June 29, 2018), <https://news.navient.com/static-files/52a18ce6-7313-434c-81f8-0f30609b1963>.

87. Complaint for Permanent Injunction and Other Relief at 50–52, *Consumer Fin. Prot. Bureau v. Navient Corp.*, No. 3:17-cv-00101-RDM (M.D. Pa. Jan. 18, 2017), ECF No. 1 (Consumer Financial Protection Bureau (CFPB) bringing action against Navient for improper steering into forbearance); see also Complaint for Permanent Injunction and Other Relief at 49–52, *Pennsylvania v. Navient Corp.*, No. 3:17-cv-1814-RDM (M.D. Pa. Oct. 5, 2017), ECF No. 1 (PA Attorney General bringing action against Pennsylvania Higher Education Assistance Agency (PHEAA) for improper steering into forbearance).

to understand fully each borrower's unique circumstances. DoE regulations requiring servicers to aid borrowers in enrolling in the right payment plan for them pose great practical difficulties to servicers given their lack of knowledge of the borrower's future plans and the fact that borrowers on the verge of delinquency are the least likely to respond to servicers' informational outreach.⁸⁸

Not only is it important for borrowers to understand the full consequences of enrolling in a certain repayment plan, it is vital for borrowers to understand the interplay between the different plans and the impact that enrolling in a plan may have on eligibility for further plans down the road. For example, a Direct Consolidation Loan allows a borrower to combine multiple federal student loans, each with a different monthly payment, into a single loan with one monthly payment.⁸⁹ Because a Direct Consolidation Loan is a new loan, the repayment term starts over which usually increases the period of repayment overall—and may increase the total amount the borrower will have to pay to the government over the life of the loan. This may also negatively affect a borrower who is otherwise eligible for Public Service Loan Forgiveness; as a new loan, a Direct Consolidation Loan resets the 120-month period under the federal public service loan forgiveness and the borrower loses credit for any payments already made towards this goal. As a result, a borrower who consolidates his or her federal loans after making nine years of qualifying payments would have to make another ten years of qualifying payments to be eligible for forgiveness. Therefore, making an informed and correct decision in the first instance is critical.⁹⁰

88. 20 U.S.C. § 1083(e)(2) (2018) (requiring lenders and servicers to provide struggling borrowers with descriptions and the requirements of repayment plans and forbearance options to help avoid default); 34 C.F.R. § 682.205(a)(4) (dictating the procedures for such disclosures). For a further discussion of the challenges that emerge when creditors are tasked with determining the best approach for borrowers, see Jeffrey P. Naimon et al., *Caveat Emptor or Caveat Vendor? The Evolution of Unfairness in Federal Consumer Protection Law*, 132 BANKING L.J. 3, 18–20 (2015).

89. *Loan Consolidation*, DEP'T OF EDUC., <https://studentaid.ed.gov/sa/repay-loans/consolidation> (last visited May 11, 2020). At various points, the federal government has incentivized borrowers to enter into consolidation loans by offering interest rate reductions on the new loan's overall balance. See, e.g., OFFICE OF FED. STUDENT AID, DEP'T OF EDUC., BULL. NO. 00-51, NEW REPAYMENT INCENTIVE BENEFITS—SECOND QUESTION AND ANSWER DOCUMENT: INTEREST RATE REDUCTION FOR DIRECT CONSOLIDATION LOANS (2000), <https://ifap.ed.gov/dlbulletins/attachments/dlb0051.pdf> [<http://web.archive.org/web/20170428051613/https://ifap.ed.gov/dlbulletins/attachments/dlb0051.pdf>] (outlining the interest rate reductions for Direct Consolidation Loans in 2000).

90. Further complicating matters, if a borrower has unpaid interest when entering into a Direct Consolidation Loan, that interest is added to the new loans' principal, further increasing the amount the borrower will have to repay. 34 C.F.R. § 685.220.

As if consolidation was not complicated enough, the need for informed decisionmaking is magnified when a borrower consolidates several different types of federal loans, particularly Perkins Loans. A borrower with Perkins Loans is not eligible to enroll in an IDR plan unless the borrower consolidates the Perkins Loans with other federal student loans.⁹¹ However, by consolidating the Perkins Loans to access IDR, the Perkins Loans lose eligibility for cancellation under the federal Perkins Loan cancellation programs.⁹²

Due to the complexities regarding eligibility and the application processes for various assistance programs, student borrowers have often found it difficult to avail themselves of available federal repayment benefits. For example, in the first year of eligibility for the Public Service Loan Forgiveness program, 28,000 borrowers applied for forgiveness.⁹³ Only ninety-six borrowers (0.3%) had their loans forgiven.⁹⁴ Because the situation was so dire for borrowers who were rejected for forgiveness, Congress created and funded the Temporary Expanded Public Service Loan Forgiveness to help borrowers who were found to be ineligible because they were enrolled in an ineligible repayment plan.⁹⁵ Although Congress set aside \$700 million in appropriations for this temporary program in 2018, only one percent of applicants were approved for forgiveness; ninety-nine percent of applicants were rejected for forgiveness by the federal government *for a second time*.⁹⁶

Unsurprisingly, requiring federal student loan servicers to counsel delinquent borrowers and rigorously enforce DoE's labyrinthine repayment program qualification requirements on a loan portfolio facing high rates of default has created frustration. Borrowers and politicians have blamed federal student loan servicers for problems arising from DoE's regulations—regulations that servicers are contractually and administratively bound to enforce.⁹⁷ Support

91. *See id.* § 685.209 (noting that only Direct Loans, FFELP loans, and certain Direct or Federal Consolidation Loans are eligible for income-contingent and income-based repayment plans); *see also id.* § 674.33 (mandating the standard repayment options for Federal Perkins loans).

92. 34 C.F.R. § 674.56 (noting that only outstanding Federal Perkins Loans are eligible for cancellation for full-time employment as a nurse, medical technician, public or private nonprofit child or family service agency, librarian, firefighter, *inter alia*).

93. *Federal Student Aid Posts New Reports to FSA Data Center*, DEP'T OF EDUC. (Sept. 19, 2018) (on file with author).

94. *Id.*

95. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-19-595, PUBLIC SERVICE LOAN FORGIVENESS: IMPROVING THE TEMPORARY EXPANDED PROCESS COULD HELP REDUCE BORROWER CONFUSION 22 (2019), <https://www.gao.gov/assets/710/701157.pdf>.

96. *Id.* at 11.

97. JASON D. DELISLE & LEXI WEST, AM. ENTERPRISE INST., STUDENT LOAN SERVICES: SCAMMERS OR SCAPEGOATS? 4 (2019), <https://www.aei.org/wp-content/uploads/2019/10/Student-Loan-Servicers.pdf>.

ing this view, the American Enterprise Institute (AEI) recently examined a sample of complaints against federal student loan servicers from the Consumer Financial Protection Bureau's (CFPB) complaint database.⁹⁸ AEI found that only "44 percent of complaints referenced something under loan servicers' control. In other words, fewer than half of the complaints filed under student loan servicing are about student loan servicing."⁹⁹ Of these fifty-six percent of complaints outside of the servicers' control, AEI determined thirty-five percent of the complaints related to the terms and regulations of the federal loan program, which the servicers have no role in setting.¹⁰⁰ The remaining nonservicing complaints cited practices by "institutions of higher education, debt relief companies, or some other matter."¹⁰¹

A. Case Study: Income-Driven Repayment

One of the primary foci of regulators and litigants is how federal student loan servicers enroll students in IDR plans. In creating IDR plans, Congress evinced an intent to provide borrowers with flexibility in their repayment options because a flat fixed payment fee stretched over ten years was not feasible for borrowers who did not earn enough monthly income to cover their living expenses in addition to the loan payments.¹⁰² Not only do borrowers who earn enough income to cover both their necessary expenses and the ten-year monthly payment not need the protections of an IDR plan, but the plan could actually hurt such borrowers in the long run. This is because

98. *Id.*

99. *Id.*

100. *Id.* As with most other federal benefits programs, the application processes are document heavy and require borrowers to show documentation attesting to their eligibility in the program. Given that a major source of borrower complaints relate to the administrative difficulties involved in proving one's eligibility for the repayment benefit, the data suggests that these middle-class borrowers are reluctant to prove their continued eligibility for a government benefit, despite the fact that most federal benefits programs, including welfare, unemployment, and food assistance programs, have required the same since the New Deal.

101. DESLISLE & WEST, *supra* note 97, at 4. According to the United States Government Accountability Office, fifteen percent of Direct Loan borrowers participated in income-based or pay-as-you-earn repayment plans as of September 2014. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-15-663, FEDERAL STUDENT LOANS: EDUCATION COULD DO MORE TO HELP ENSURE BORROWERS ARE AWARE OF REPAYMENT AND FORGIVENESS OPTIONS 13–14 (2015) [hereinafter GAO EDUCATION].

102. 153 CONG. REC. 23916–19 (2007) (statement of Rep. Andrews) (stating that upon the creation of an income-driven repayment plan, "[t]his is a loan repayment program that works the way life does. You start out with a low income and a lot of obligations, and hopefully your income grows. When it does, your payments do; but if it doesn't, then your payments stay reasonable.").

the IDR plan's monthly payments may not reduce the principal of the loan, therefore trapping the borrower into paying more for the loan over time. With respect to both borrowers, Congress wanted to encourage the borrower to make wise financial choices over the long term.¹⁰³

To solve the quandary of encouraging the borrowers who will benefit from IDR while disallowing borrowers who do not need the protection from making an unsound financial decision, Congress requires those who wish to enroll in an IDR plan to verify their income to DoE and to recertify their income on an annual basis to prove their continued entitlement to the IDR plan.¹⁰⁴ For most borrowers, income is documented based on the submission of a federal tax return.¹⁰⁵ For those who do not file federal tax returns, verification is shown by alternative documentation of income such as pay stubs.¹⁰⁶ A borrower who fails to comply with the annual recertification requirement may experience an increase in both monthly loan payments and total loan balance, due to the capitalization of the unpaid interest. Moreover, to enroll in the program, DoE requires borrowers to print, sign, and return the IDR application to DoE.¹⁰⁷

Studies have shown that only a small fraction of borrowers eligible for an IDR plan are actually enrolled in such plan.¹⁰⁸ This stems from the administrative barriers put in place by Congress and DoE regulations. The barriers to entry and continued enrollment obligations are often too high for borrowers, despite the federal student loan servicers' outreach efforts to contact eligible borrowers. Not only are servicers regularly sending out written information and placing calls to eligible borrowers, but also servicers are

103. See 145 CONG. REC. 23861–65 (2007) (statement of Sen. Kennedy) (discussing the importance of the income-driven repayment (IDR) plans).

104. Federal Family Education Loan (FFEL) Program – Income-based Repayment Plan, 34 C.F.R. § 682.215(e) (2018) (“The loan holder determines whether a borrower has a partial financial hardship to qualify for the income-based repayment plan for the year the borrower elects the plan and for each subsequent year that the borrower remains on the plan. To make this determination, the loan holder requires the borrower to – (i) provide documentation, acceptable to the loan holder, of the borrower’s AGI . . .”).

105. *Id.* § 682.215(a)(1) (defining “adjusted gross income” as “the borrower’s adjusted gross income as reported to the Internal Revenue Service”).

106. *Id.* § 682.215(e)(1)(ii) (stating that if the borrower is unable to provide documentation on his or her adjusted gross income, alternative documentation may be provided).

107. See, e.g., *id.* § 682.215(e) (requiring the borrower to provide documentation to the loan holder, the DoE).

108. GAO EDUCATION, *supra* note 101, at 13–14 (highlighting that a September review of DoE student loan data from September 2014 found that only fifteen percent of eligible borrowers were enrolled in an IDR plan).

increasingly searching for innovative solutions to streamline the IDR application process to better serve their borrowers.

For example, Navient conducted a study in 2017 to determine whether borrowers were more likely to complete the IDR application if Navient provided the borrowers with a pre-populated application with their earnings and family information, as well as the option to electronically sign the application.¹⁰⁹ To do so, Navient “[a]gents contacted the borrowers, gathered salary and family information over the phone, and used this [information] to pre-populate [DoE’s IDR] application.”¹¹⁰ Navient found that the number of borrowers who were given a pre-filled application that could be electronically signed were two-and-a-half times more likely to complete and submit their application.¹¹¹ This study shows that merely reducing the administrative hassles involved with the government-required IDR application has a palpable positive impact on the enrollment rate.¹¹²

Overall, then, Congress’s borrower assistance programs for federal student loan borrowers—and the DoE regulatory and contractual provisions implementing them—demonstrate the tension between making borrower forgiveness available and protecting against those borrowers who may abuse the system. As a result, federal student loan borrowers often struggle with confusing requirements, and servicers are charged with administering a program that contains conflicting directives.

B. Case Study: Paid Ahead Status

A common example of this misplaced borrower frustration with federal student loan servicers is DoE’s paid ahead status regulation (Paid Ahead Status). This regulation requires servicers to credit any extra loan payments to the next month’s bill, which results in advancing the borrower’s next due date.¹¹³ For example, if a borrower owes \$1,000 per month and pays her servicer \$1,500 on January 1st, the bill for February 1st will only show the amount due as \$500. By the same token, if the borrower instead makes a \$6,000 payment of her \$1,000 bill on January 1st, the borrower will not have

109. Holger Mueller & Constantine Yannelis, *How a Simple Tweak to a Federal Form Could Help Borrowers Potentially Avoid Defaulting on Student Loans*, PROMARKET (Oct. 2, 2019), <https://promarket.org/how-a-simple-tweak-to-a-federal-form-could-help-borrowers-potentially-avoid-defaulting-on-student-loans/>.

110. *Id.*

111. *Id.*

112. *Id.*

113. William D. Ford Direct Loan – Miscellaneous Repayment Provisions, 34 C.F.R. § 685.211(a)(3) (2018).

to make another student loan payment until July 1st.¹¹⁴ While borrowers can request that a servicer not advance the due date, the default approach mandated by DoE regulations requires the servicer to advance the due date.¹¹⁵ Generally, Paid Ahead Status does not cause borrowers to pay more on their federal loans than they would if they had made their originally scheduled minimum payment amounts (although they do miss out on reducing the amount of interest they would otherwise pay through accelerated repayment of principal).¹¹⁶

However, Paid Ahead Status can conflict with DoE's popular Public Service Loan Forgiveness program. As discussed above, this program forgives federal student loans for borrowers who work in qualifying public service occupations and make 120 on-time qualifying payments. Under the Public Service Loan Forgiveness program, a qualifying payment means a full payment based on the borrower's repayment plan. If the borrower does not make a *full payment*, that payment will not constitute a qualifying payment towards the requirement of 120 qualifying payments.

In practice, when a borrower pays extra in a given month, the next bill is credited with the amount of the extra payment, and the borrower's next bill is reduced correspondingly. Therefore, if a borrower pays \$1,500 for a \$1,000 monthly bill, the next month's invoice will be reduced to only \$500.¹¹⁷ If the borrower pays just the \$500 on the invoice, that month's payment will not qualify towards the Public Service Loan Forgiveness program because it was not a full payment—even though the borrower has paid exactly what they were required to under DoE regulations. Both the Public Service Loan Forgiveness program and Paid Ahead Status were designed to protect borrowers, but when combined it can appear to borrowers as if their federal student loan servicer is cheating them out of loan forgiveness. In reality, the servicer is merely following DoE regulations as required by law.

Separate and apart from the conflict between Paid Ahead Status and Public Service Loan Forgiveness, Paid Ahead Status conflicts with another government directive. A Presidential Memorandum signed in March 2015 instructs

114. *See id.* (calculating repayments based on the instructions in the Code of Federal Regulations).

115. *Id.*

116. *See* Seth Frotman, *You Have a Right to Pay Off Your Student Loan as Fast as You Can, Without a Penalty*, CONSUMER FIN. PROT. BUREAU (Sept. 26, 2016), <https://www.consumerfinance.gov/about-us/blog/you-have-right-pay-your-student-loan-fast-you-can-without-penalty/>.

117. For a further explanation of this contradiction, as well as exploration of its absurd application in real-life borrower examples, see Robert Farrington, *Be Careful With Student Loan Pay Ahead Status and Loan Forgiveness*, COLLEGE INVESTOR (Feb. 11, 2020), <https://thecollegeinvestor.com/19797/pay-ahead-status-loan-forgiveness/>.

DoE to require Direct Loan servicers to apply prepayments to the loan balance with the highest interest rate unless they receive explicit instructions from the borrower to apply payments otherwise.¹¹⁸ Thus, a borrower with several federal loans with total monthly payments of \$1,000 who sends in a check for \$2,000 in January may reasonably believe that she need not make a payment in February. She would be wrong, however; the servicer would be required to apply the second \$1,000 entirely to her loan with the highest interest rate, leaving the other federal loans unpaid. If the borrower failed to make a February payment to cover these lower interest rate federal loans, the borrower would end up delinquent—resulting in negative credit reporting and possibly harming her ability to qualify for other federal student loan assistance programs.¹¹⁹ In this situation, the federal student loan servicer’s strict adherence to DoE’s requirements serves as the true cause of borrower frustration, yet borrowers almost always blame the servicers themselves for their dissatisfaction with this outcome.¹²⁰

118. See *Federal Family Education Loan Programs: Federal Stafford Loans, Federal PLUS, and Federal Consolidation Loan Programs, Award 1996–1997*, DEP’T OF EDUC., <https://ifap.ed.gov/federal-student-aid-handbook/06-17-1998-federal-family-education-loan-programs-federal-stafford-5> (last visited May 11, 2020) (dictating that “[i]f the borrower submits a payment amount that exceeds the normal monthly payment amount and does not provide instructions for the handling of the [excess] payment” the servicer must credit the payment in the order dictated in 34 C.F.R. § 685.211); Presidential Memorandum on Student Aid Bill of Rights to Help Ensure Affordable Loan Repayment, 80 Fed. Reg. 13,475, 13,476 (Mar. 10, 2015) (instructing DoE to require Direct Loan servicers to apply prepayments to the highest interest rate loan balance).

119. See PUBLIC INPUT ANALYSIS, *supra* note 74, at 38, 81–82.

120. In addition to the regulations discussed in this Section, DoE also periodically issues guidelines for servicers outside of the rulemaking process. For example, in 2016, DoE issued a memorandum titled “Policy Direction on Federal Student Loan Servicing” that articulated standards expected of servicers. See Memorandum from Ted Mitchell, Under Sec’y, U.S. Dep’t of Educ., on Federal Student Loan Servicing to James Runcie, Chief Operating Officer, Office of Fed. Student Aid 2 (July 20, 2016), https://files.consumerfinance.gov/f/documents/20160620_US-Department-of-Education_loan-servicing-policy-memo.pdf (outlining “a list of directives federal student loan borrowers can expect their servicer to follow, including specific baseline standards when providing customer service to ‘at-risk’ borrowers”); see also Addendum to July 20, 2016 Memorandum on Policy Direction on Federal Student Loan Servicing from Ted Mitchell, Under Sec’y, U.S. Dep’t of Educ., to James Runcie, Chief Operating Officer, Office of Fed. Student Aid (Oct. 17, 2016), https://files.consumerfinance.gov/f/documents/20160620_US-Department-of-Education_loan-servicing-policy-memo.pdf. DoE later withdrew this memorandum in 2017, further adding to the inconsistencies and uncertainty plaguing the field of student loan servicing. See Memorandum from Betsy DeVos, Sec’y, U.S. Dep’t of Educ., on Student Loan Servicer Recompete to James W. Runcie, Chief Operating Officer, Off. of Fed. Student Aid 1 (Apr. 11, 2017), <https://www2.ed.gov/documents/press-releases/student-loan-servicer-recompete.pdf> (withdrawing the July 20, 2016 memorandum “to

IV. TOO MANY COOKS: OTHER ENFORCEMENT AGENCIES

While increasing borrower delinquency and regulatory confusion are the main challenges in the federal student loan servicing space, they are far from the only challenge. The DoE and its servicers generally resolve their issues under their existing contracts, but a variety of federal and state administrative agencies—to say nothing of private and class action plaintiffs—have shown interest in regulating, examining, and filing suit against federal student loan servicers.

A. *The Consumer Financial Protection Bureau*

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Congress granted the then-new CFPB supervisory authority over both nonbanks in the private student lending market, as well as nonbank “larger participant[s]” of markets for other consumer financial products or services, as the CFPB defines through administrative rulemaking.¹²¹ In its March 1, 2014 rule, the CFPB used its “larger participant” authority to extend its supervisory authority over the three main servicers of federal student loans.¹²²

Although the CFPB does not have administrative authority under the HEA or DoE regulations, Congress nevertheless tasked the CFPB with enforcing a variety of consumer protection statutes that apply to all forms of consumer lending, including federal student loans.¹²³ The CFPB is empowered to regulate and initiate enforcement actions against federal student loan servicers for violations of the Electronic Funds Transfer Act, Equal Credit Opportunity Act, Fair Credit Billing Act, Fair Credit Reporting Act, Fair

negate any impediment, ambiguity or inconsistency in the approach needed to accomplish th[e] critical mission” of “acquiring new federal student loan servicing capabilities” and “provid[ing] high quality customer service to federal loan borrowers in a cost-efficient and effective manner”).

121. 12 U.S.C. § 5514(a)(1)(B), (a)(2) (2018); *see also* 12 U.S.C. § 5481(5) (defining “consumer financial product or service”).

122. Defining Larger Participants ff Certain Consumer Financial Product and Service Markets, 12 C.F.R. pt. 1090 (2017). The CFPB defines “student loan servicing” as (1) receiving loan payments or notifications thereof and “applying payments to the borrower’s account pursuant to the terms of the post-secondary education loan or of the contract governing the servicing;” (2) “[d]uring a period when no payment is required on a post-secondary education loan, . . . [m]aintaining account records for the loan and . . . [c]ommunicating with the borrower regarding the loan, on behalf of the loan’s holder; or” (3) “[i]nteractions with a borrower, including activities to help prevent default on obligations arising from post-secondary education loans, conducted to facilitate” the aforementioned activities. 12 C.F.R. § 1090.106(a).

123. 12 U.S.C. § 5481(12) (2018).

Debt Collection Practices Act, and the Truth in Lending Act.¹²⁴ In addition, the CFPB has broad authority to examine institutions and file suit to prevent unfair, deceptive, and abusive acts or practices (UDAAP).¹²⁵

The CFPB has acted aggressively in enforcing the provisions of the Consumer Financial Protection Act against federal student loan servicers. For example, in 2019 the CFPB brought an enforcement action against Conduent Education Services, LLC, formerly conducting business as ACS Education Services (ACS), for failing to process FFELP loan adjustments in a timely manner, resulting in errors in borrowers' principal balance amounts in violation of § 1031 and § 1036 of the Dodd-Frank Act.¹²⁶ Because ACS could not automatically process all principal balance adjustments, processors had to manually enter certain adjustments, which caused queues of adjustments to form.¹²⁷ While adjustments were queued, the affected loans showed inaccurate principal balances, misleading borrowers as to the actual balance of their federal student loans.¹²⁸

According to the CFPB, over 200,000 packets of loans were backlogged in queues for adjustment for a period of several years, which impacted borrowers' eligibility for consolidation, IDR, and other assistance programs.¹²⁹ The CFPB alleged that the practice of untimely processing principal balance adjustments caused harm to borrowers and constituted an unfair practice, in violation of the Consumer Financial Protection Act.¹³⁰ ACS entered into a Consent Order with the CFPB in which ACS agreed to review all affected loans, adjust the loans as appropriate, and pay a civil money penalty of \$3.9 million to the CFPB.¹³¹

B. *The Department of Justice and False Claims Act Liability*

While there is no private cause of action against servicers for violations of DoE regulations,¹³² the threat of private enforcement under the False Claims Act (FCA) has the capacity to dominate the federal loan servicers. Although

124. *Id.*

125. 12 U.S.C. § 5531.

126. Conduent Educ. Servs., LLC, File No. 2019-BCFP-0005, Fed. Banking L. Rep. (CCH) ¶¶ 156-093, 2019 WL 5104426 (Consumer Fin. Prot. Bureau May 1, 2019) (consent order).

127. *Id.* ¶ 11.

128. *Id.* ¶¶ 28, 31.

129. *Id.* ¶ 14.

130. *Id.* p. 1.

131. *Id.* ¶¶ 35–36.

132. See KEVIN M. LEWIS & NICOLE VANATKO, CONG. RESEARCH SERV., LSB10302, PREEMPTIVE STRIKE: DOES FEDERAL LAW DISPLACE STATE REGULATION OF STUDENT LOAN SERVICES? 2 (2019), <https://crsreports.congress.gov/product/pdf/LSB/LSB10302>.

no court has imposed liability on student loan servicers under the FCA yet, the threat of a potential action casts a shadow over the federal student loan servicing industry.

The FCA prohibits a person or corporation from knowingly submitting a false claim for payment to the government.¹³³ The government can initiate FCA suits directly, although often they arise when a whistleblower or other individual who has identified a false claim files a *qui tam* action under seal on behalf of the government.¹³⁴ The Department of Justice (DOJ) will then review the *qui tam* suit and decide whether to take over the case; even if the government decides not to intervene, the individual who identified the false claim may proceed with the case and can receive up to thirty percent of any award, plus attorneys' costs and fees.¹³⁵ In addition, a court may impose civil penalties and treble damages, leading to major exposure for companies dealing with the federal government.¹³⁶

Although the FCA provides multiple theories of liability, the false certification theory is the most relevant to federal loan servicing. Under this theory, persons or entities can be held liable for knowingly making a false statement that is material to the submission of a claim for payment from the United States.¹³⁷ Because federal student loan servicers are constantly making representations to the government in exchange for payment under their servicing contracts—e.g., submitting claims for payment, providing performance data for analysis, certifying compliance with various statutes, regulations, and contractual requirements—there are numerous ways that a federal student loan servicer can run afoul of the FCA. Moreover, several of the primary federal student loan servicers explicitly recognize that they may be subject to FCA liability, even though the federal government has not yet spoken on the issue.¹³⁸

133. See 31 U.S.C. § 3729 (2018).

134. *The False Claims Act: A Primer*, U.S. DEP'T OF JUSTICE, https://www.justice.gov/sites/default/files/civil/legacy/2011/04/22/C-FRAUDS_FCA_Primer.pdf (last visited May 11, 2020).

135. *Id.*; 31 U.S.C. § 3730(d)(2).

136. See 31 U.S.C. § 3729.

137. Michael Murray, *Seeking More Scienter: The Effect of False Claims Act Interpretations*, 117 YALE L.J. 981, 983 (2008).

138. Navient Corp., Annual Report (Form 10-K) 20 (Feb. 26, 2019), https://www.sec.gov/Archives/edgar/data/1593538/000156459019004187/navi-10k_20181231.htm (“If improper or illegal activities are found in the course of government audits or investigations, the contractor may become subject to various civil and criminal penalties, including those under the civil U.S. False Claims Act.”); Nelnet, Inc., Annual Report (Form 10-K) 24 (Feb. 27, 2019), <https://www.sec.gov/ix?doc=/Archives/edgar/data/1258602/000125860219000022/wfx-20181231.htm> (employing the same FCA language as Navient).

While this theory has not been used successfully against federal student loan servicers in particular, it has been used in similar areas. In the past several years, courts have held colleges and universities liable for false certifications in originating student loans.¹³⁹ For example, in *United States ex rel. Main v. Oakland City University*,¹⁴⁰ a university compensated its admissions personnel based on commission, rather than a salary basis as required to receive Title IV funds from DoE.¹⁴¹ Even though the primary contract at issue was the employment agreement between the university and its recruiting personnel, the Seventh Circuit found that the university violated the FCA because the university incorrectly certified to DoE that it complied with all Title IV requirements.¹⁴² Similarly, in the federally-backed home mortgage lending context, several servicers have faced FCA litigation arising out of inaccurate representations made to the Department of Housing and Urban Development.¹⁴³

Although FCA lawsuits against federal student loan servicers are not currently an active area of litigation, this may be changing. In at least one case, *United States ex rel. Jackson v. University of North Texas*,¹⁴⁴ a student athlete tried to hold federal student loan servicer Nelnet liable under the FCA.¹⁴⁵ When the student borrower applied for federal student loans, the university failed to take into account the value of his athletic scholarship in calculating his costs of attendance, which caused the loan amount that the school certified on his behalf to be larger than the amount he should have received.¹⁴⁶ Nelnet certified that the federal loans complied with federal law and, when the borrower defaulted on the federal loans, Nelnet submitted the default claim to DoE as the guarantor on these federal loans.¹⁴⁷ Based on this inaccurate certification, the student borrower filed an FCA action against Nelnet (as well as the university and loan

139. See *United States ex rel. Main v. Oakland City Univ.*, 426 F.3d 914, 916 (7th Cir. 2005).

140. 426 F.3d 914 (7th Cir. 2005).

141. *Id.* at 916.

142. *Id.*

143. See, e.g., *United States v. Bank of Am. Corp.*, 753 F.3d 1335 (D.C. Cir. 2014) (addressing potential FCA claims based upon alleged false certifications made by mortgage servicers in connection with home mortgage loans insured by the Federal Housing Administration, a division of the Department of Housing and Urban Development); *United States ex rel. Szymoniak v. Am. Home Mortg. Servicing, Inc.*, 679 Fed. App'x 299 (4th Cir. 2017) (upholding the district court's grant of a motion to dismiss an action alleging that mortgage servicers, among other entities, made false certifications to apply for payments from the Department of Housing and Urban Development under the Federal Housing Administration's mortgage insurance program).

144. 673 Fed. App'x 384 (5th Cir. 2016), *cert. denied* 138 S. Ct. 59 (2017).

145. *Id.* at 386.

146. *Id.*

147. *Id.*

originator).¹⁴⁸ Although the Fifth Circuit upheld the dismissal of the FCA claim against Nelnet on statute of limitations grounds, this case shows that borrowers can and are bringing claims against servicers under the FCA—with its crippling potential for treble damages and fees.

C. State Attorney General Enforcement

Until this point, this article has focused exclusively on federal oversight over the federal student loan servicers. But there is a growing debate taking place in classrooms, legislatures, and courtrooms across the country concerning whether federal student loan servicers are subject to regulation by the individual states, in addition to the oversight exercised by the federal government through DoE and FSA.

As a threshold matter, most federal statutes in the student loan space do not provide a right of action for either attorneys general or private borrowers. For example, the HEA addresses the relationship between servicers and the federal government but does not provide other litigants with a private cause of action against a federal student loan servicer.¹⁴⁹ Without a federal cause of action, borrowers and state attorneys general have turned to state law to provide a cause of action against federal student loan servicers.¹⁵⁰ Although the state unfair competition statutes and common law doctrine of *parens patriae* generally empower state attorneys general to sue on behalf of aggrieved citizens in court because such actions are based in state law, the issue of state law preemption by the federal student loan serving program often dominates the course of the litigation.¹⁵¹

Following the direction of DoE, federal student loan servicers have argued that federal law preempts any state laws that purport to regulate federal student loan servicing.¹⁵² In March 2018, DoE published an interpretation announcing its position that federal law preempts a wide range of state laws that regulate federal student loan servicers.¹⁵³ Specifically, the guidance document

148. *Id.*

149. See 20 U.S.C. §§ 1001–1019 (2018); LEWIS & VANATKO, *supra* note 132, at 2–3.

150. See LEWIS & VANATKO, *supra* note 132, at 2–3.

151. Importantly, 20 U.S.C. § 1098g expressly exempts certain federal student loans made, insured, or guaranteed pursuant to the HEA from “any disclosure requirements of any [s]tate law.” LEWIS & VANATKO, *supra* note 132, at 2–3.

152. See, e.g., *Pennsylvania v. Navient Corp.*, No. 19-2116, 2019 WL 1052014 (M.D. Pa. Mar. 5), *appeal docketed*, No. 19-2116 (3d Cir. filed July 23, 2019).

153. Federal Preemption and State Regulation of the Department of Education’s Federal Student Loan Programs and Federal Student Loan Services, 83 Fed. Reg. 10619, 10619 (Mar. 12, 2018) (to be codified at 34 C.F.R. pt. 6).

claimed that federal law displaces state laws that impose regulatory requirements on servicing, state licensing requirements, and state disclosure requirements.¹⁵⁴ This theory was based upon conflict preemption, field preemption, and express preemption as contained in 20 U.S.C. § 1098g.¹⁵⁵ In response to these challenges, state attorneys general—in addition to challenging the overall basis for preemption—have turned to the federal Consumer Financial Protection Act (CFPA) as a basis for filing their own lawsuits against federal student loan servicers. The CFPA expressly allows state attorneys general to undertake enforcement actions for alleged UDAAP violations; because this is a federal statute, state attorneys general have seen this as a way to avoid preemption arguments by student loan servicers.¹⁵⁶ While courts continue to rule on these issues, the question of whether federal law preempts actions grounded in state law will continue to dominate courtrooms for the foreseeable future.

D. State Student Loan Servicer Licensing

Finally, some states are taking a different approach to regulating student loan servicers by requiring them to obtain licenses to service federal student loans owed by borrowers within the state. For example, in May 2019 the Colorado Student Loan Servicers Act established a licensing requirement for student loan servicers.¹⁵⁷ The Colorado Student Loan Servicers Act requires servicers of federal student loans owed by Colorado borrowers to be licensed by the designated Assistant Attorney General responsible for enforcing the Colorado Consumer Credit Code, as well as prohibits servicers from a myriad of activities that range from fraudulent to negligent, requires servicers to keep records of each student loan transaction, grants the designated Assistant Attorney General the authority to conduct investigations, and makes any violation of the Act a deceptive trade practice.¹⁵⁸ While servicers of federal student loans are exempted from the requirement to submit a license application by virtue of their federal regulation, they must comply with the remainder of the Act's various requirements.¹⁵⁹

154. *Id.*

155. *Id.* at 10620–21.

156. 12 U.S.C. § 5552(a) (2018) (authorizing “the attorney general (or the equivalent thereof) of any State” to bring a “civil action . . . to enforce a provision of [the Consumer Financial Protection Act]” or regulations issued thereunder). *See id.* § 5552(a)–(b) (including limits on such authority and enumerating the conditions that a state must satisfy to exercise such authority. The CFPB retains the right to intervene in any state attorney general lawsuit brought under the Consumer Financial Protection Act. *Id.* § 5552(b)(2).

157. S.B. 19-002, 2019 Gen. Assemb., Reg. Sess. (Colo. 2019).

158. *Id.*

159. *Id.*

Connecticut has similarly passed a student loan servicer licensing requirement that applies to federal student loan servicers.¹⁶⁰ Connecticut imposes a number of requirements upon student loan servicers operating in the state, including licensing requirements, recordkeeping requirements, prohibitions on false statements or omissions to borrowers, and enforcement of these provisions by the Connecticut Banking Commissioner.¹⁶¹ Unlike the Colorado law, Connecticut does not exempt the servicers of federal student loans from any of its licensing-related provisions.

State laws that impose licensing requirements upon federal student loan servicers appear to directly conflict with DoE's desire for a uniform, nationwide approach to student loan servicing. In DoE's view, "[a] requirement that Federal student loan servicers comply with fifty different state-level regulatory regimes would significantly undermine the purpose of the Direct Loan Program to establish a uniform, streamlined, and simplified lending program managed at the federal level."¹⁶² Further, federal student loans are meant to be an affordable means for all students to fund higher education, but these state licensing regimes will impose additional registration, compliance, and disclosure costs upon federal student loan servicers—costs that, combined with other requirements, can eclipse the revenue from student loan servicing in a particular state.

E. Confusion and Convolutions: The Impact of the Complex Federal Student Loan Program

Combined, these laws, regulations, servicing contracts, and multiple enforcement agencies create a complicated and (in some ways) conflicting environment for both borrowers and federal student loan servicers.

Through decades of well-intentioned legislation and regulation—from Congress, the DoE, and other federal agencies—the current universe of borrower assistance programs is so complicated that borrowers can struggle to get the assistance they otherwise deserve. In enacting such protections, Congress intended to provide borrowers with flexibility in their repayment options and to account for varying financial situations, whilst simultaneously encouraging behavior associated with future borrower success.¹⁶³ Unfortunately, these repayment assistance programs were created, not as a holistic set of borrower assistance options, but rather over several different administrations and

160. H.B. 6915, 2015 Gen. Assemb., Reg. Sess. (Conn. 2015).

161. *Id.*

162. Federal Preemption and State Regulation of the Department of Education's Federal Student Loan Programs and Federal Student Loan Services, 83 Fed. Reg. 10619, 10621 (Mar. 12, 2018) (to be codified at 34 C.F.R. ch. VI).

163. PUBLIC INPUT ANALYSIS, *supra* note 74, at 1, 17–18.

in response to various external repayment concerns. For these reasons, the repayment, forgiveness, and cessation benefits come in a variety of forms, stemming from entitlements created by federal law and regulations, contractual features in the student loan promissory notes, and contractual features in the servicing contracts. Additionally, informational programs initiated by the servicers in response to this complexity that strive to aid borrowers in selecting and applying for the correct student loan assistance program based upon their specific needs. Selecting the appropriate repayment assistance program is made much more difficult by the fact that some of these benefits are mutually exclusive or make a borrower ineligible for a different benefit or program in the future. While there is value in providing borrowers with the needed flexibility to adjust to a difficult job market and tough economy, the multitude of repayment options can result in borrowers enrolling in a benefit that does not suit their particular needs due to information asymmetry.

Not only is it a challenge for struggling borrowers to select the appropriate repayment assistance program, but once the borrower selects a program even the threshold application process can discourage an otherwise qualified borrower from obtaining assistance. Each of the various repayment options available to borrowers contains its own paperwork requirements, mandating the collection and submission of various income, asset, and employment documents along with regular recertification of eligibility. By complicating the administration of these repayment programs with various barriers to entry, DoE may unwittingly create burdens for borrowers that outweigh the benefits they would expect to see from filing for borrower assistance. As a result, this contributes to the narrative that federal student loan servicers are thwarting borrowers seeking relief under these programs; in reality, much of the criticism should lie with the larger federal student loan system.

In addition to creating barriers for borrowers, this complexity also increases the challenges and costs facing student loan servicers. As an initial matter, this increased complexity requires servicers to invest significant time into understanding various repayment programs and their unique requirements. Servicers must then build controls to ensure that they implement each program accurately for thousands of individual customers, and regulators and enforcement agencies further expect that federal student loan servicers will steer each individual borrower to the best repayment option based on the borrower's unique financial situation. As these regulations grow more complex, servicers must expend greater resources in contacting borrowers and explaining the benefits and costs of each program. As a result, the current federal borrower assistance programs necessitate a large number of contacts from the servicers to the borrowers through letters, emails, phone calls, etc.—and in practice, borrowers who are delinquent or in default are less likely to respond to any form of outreach, further compounding the efforts

servicers must expend. Separately, when the CFPB or a state legislature imposes additional requirements on servicers above and beyond those contemplated by the servicers when bidding for DoE contracts, the servicer has to find a way to address these unanticipated costs on a contract that already pays federal student loan servicers limited margins. This lack of financial recourse places the servicers in an economically unsustainable position.

Even when the rules governing federal student loan servicing appear to be set, an overlapping universe of regulatory entities enforce such rules and their conflicting enforcement priorities can add to the uncertainty and confusion that federal student loan servicers face. With DoE, CFPB, state attorneys general, state financial regulators, and potential *qui tam* litigants under the FCA all creating potential liability for student loan servicers, a servicer cannot rely upon the guidance of any single entity. Put differently, one regulator could hold a servicer liable for violating a law or regulation simply because the servicer was following the reasonable direction of another regulator. This is not merely an academic concern; these tensions between DoE, DOJ, the CFPB, and state attorneys general arose over the past several years and, in the face of increasing complexity, these inter-regulatory tensions will only increase.

To illustrate, the CFPB and DoE have for years tried to coordinate their oversight of federal student loan servicers, only to see tensions arise between these two agencies. In the early 2010s, the two agencies entered into a Memorandum of Understanding (MOU) which provided for interagency sharing of information pertaining to complaints about student loan servicers, among others, and coordinated supervisory and oversight activities with respect to federal student loans.¹⁶⁴ However, DoE terminated this MOU in a letter dated August 31, 2017, on the asserted basis that the CFPB had “unilaterally expand[ed] its oversight role to include the Department’s contracted federal loan servicers” in derogation of DoE’s claimed “full oversight responsibility for federal student loans.”¹⁶⁵ While the decision to terminate the MOU may have been driven in part by partisan politics, it

164. Letter from Kathleen Smith, Acting Assistant Sec’y, Office of Postsecondary Educ., & Dr. A. Wayne Johnson, Chief Operation Officer, Fed. Student Aid, Dep’t of Educ., to Richard Cordray, Director, Consumer Fin. Prot. Bureau (Aug. 31, 2017), <https://buckleyfirm.com/sites/default/files/Buckley%20Sandler%20InfoBytes%20-%20Department%20of%20Education%20Letter%20to%20CFPB%20Terminating%20MOUs%202017.08.31.pdf> (describing the Memorandum of Understanding (MOU) between the CFPB and the DoE “Concerning the Sharing of Information” entered into on October 19, 2011 and the MOU “Concerning Supervisory and Oversight Cooperation and Related Information Sharing” between the DoE and the CFPB entered into on January 9, 2014).

165. *Id.*

nevertheless highlights the tension between the ostensibly independent CFPB and the administration-bound DoE.

After DoE's unilateral termination of the information-sharing MOUs, the CFPB represented to Congress in April 2019 that student loan servicers had declined to produce information requested by the CFPB for supervisory examinations related to federal loans.¹⁶⁶ In February 2020, less than a year later, the CFPB and DoE reversed course again and announced that the two agencies had signed a new MOU to coordinate the sharing of complaint information from student loan borrowers for private and federal loans.¹⁶⁷ The 2020 MOU expressly contemplates the CFPB's role in collaborating with DoE to resolve complaints arising from the application of federal consumer financial law to federal student loans (i.e., federal student loan borrowers whose complaints allege potential issues based upon non-HEA/non-DoE laws and regulations).¹⁶⁸ In addition, the new MOU outlines a process for the two agencies to share information in response to subpoenas and other legal requests.¹⁶⁹ It remains to be seen how the 2020 MOU will affect the relationship between the CFPB and DoE, and just as importantly, the relationships between federal student loan servicers and the federal government. Nevertheless, these internecine disputes have left student loan servicers trapped between two federal agencies, which can have differing policy agendas and priorities. In some ways, conflict between the two agencies is inherent in their differing missions: DoE has a statutory obligation to protect taxpayers by vigorously collecting loans that it has made or guaranteed, while the CFPB is not similarly obligated to take into account whether servicing and collection efforts will be effective for the U.S. government.

We agree with the CFPB that many of the issues related to federal student loan servicing are created by the lack of an "existing, comprehensive federal statutory or regulatory framework providing consistent standards for the servicing of all federal student loans."¹⁷⁰ This piecemeal regulatory regime, in combination with interdepartmental conflicts, complicated ser-

166. Letter from Kathleen L. Kraninger, Director, Consumer Fin. Prot. Bureau, to Elizabeth Warren, Senator, United States Senate (Apr. 23, 2019), https://www.warren.senate.gov/imo/media/doc/2019.04.23%20KK%20to%20Warren_student%20loan%20industry.pdf.

167. Memorandum of Understanding between the Consumer Fin. Prot. Bureau and the U.S. Dep't of Educ. Concerning Coordination in Resolving Borrower Complaints (Feb. 3, 2020), https://files.consumerfinance.gov/f/documents/cfpb_ed-memorandum-of-understanding_student-loan-borrowers_2020-02.pdf [hereinafter Borrower Complaints Memorandum].

168. *Id.* at 2.

169. *Id.* at 3.

170. PUBLIC INPUT ANALYSIS, *supra* note 74, at 11.

vicings contracts, and limited servicer compensation, has created challenges for servicers and—by extension—for federal student loan borrowers.

V. RECOMMENDATIONS

While most scholars agree that the federal student loan program is facing significant financial and legal challenges, there is little consensus on how best to address the problems inherent in the program's administration. Some of the loudest advocates focus such efforts on the federal student loan servicers. But such proposals fail to address the root of the problem: the statutory and regulatory framework governing the servicing of federal student loans. Recognizing that the problem is more complicated than the standard narrative would lead one to believe, we recommend several changes that may improve federal student loan servicing.

A. *Streamline the Number of Federal Student Loan Assistance Programs*

The federal student loan program will struggle until the federal government simplifies it. Although Congress has attempted to provide concrete benefits to borrowers facing specific financial hardships, the overall web of borrower benefits has become so complicated and confusing for individual borrowers that the student loan servicing regime is impairing the ability of some borrowers to obtain the help they need.

To address this, the HEA should be amended to completely overhaul the existing loan assistance programs and, in their stead, implement a *limited* number of programs that are designed to achieve the same goals. For instance, instead of having four different IDR plans with minor variations, Congress should establish a single IDR plan with one set of interest rates and one set repayment period. Implementing this would require both amendments to the HEA and new implementation regulations from DoE establishing rules and providing guidance on how to carry out this new program. Streamlining the complicated web of borrower assistance programs will provide needed clarity, reduce the information asymmetry between the borrowers and the administrators, reduce costs for both the borrowers and servicers, and provide transparency to the entire federal lending program.

B. *Simplify the Application Process for Federal Student Loan Assistance Programs*

Second, the application processes for borrower assistance programs has been a source of frustration for both borrowers and loan servicers. Currently, borrower assistance programs require rigorous application processes to ensure that applicants do not defraud or abuse the system and unfairly benefit from an assistance program to which they do not qualify. While

ensuring that only eligible individuals benefit from borrower assistance programs is laudable, the barriers to entry are not only keeping away the underserving, but also those who need and deserve such programs the most.

Instead, the application process should be re-examined to focus on ease of access and reducing unnecessary barriers to entry, while maintaining appropriate protections against abuse. To this end, federal loan servicers are already experimenting with creative ways to simplify the application process to better ensure that borrowers can enroll in an IDR plan. As previously mentioned, Navient has already had great success in experimenting with prepopulated IDR applications that include electronic signatures.¹⁷¹ DoE should encourage such innovation, especially when such approaches prove effective. And more generally, the IDR application should be rewritten so that it is shorter and easier to comprehend by borrowers.

Potentially, DoE could develop an online tool that would allow a student loan borrower to input his or her information and have the software predict for the borrower which repayment programs the borrower might qualify for and which would be the most beneficial in different scenarios (e.g., steady income, rising income, dropping income, continued public service income, etc.). Such software, provided by DoE as the federal agency that administers these programs, would give borrowers and their servicers a critical and trustworthy tool that would facilitate loan repayment.

Most importantly, DoE should revisit the annual recertification process for IDR plans. Requiring borrowers to recertify their income every single year is not only a hassle for borrowers but can result in them losing their IDR status and defaulting on their federal loans, even though nothing has changed in their financial status. DoE could lengthen the recertification period, for example, by requiring recertification every two or five years. Alternatively, DoE could work with the IRS to create a streamlined recertification process based upon DoE automatically obtaining federal tax filings from the IRS. These efforts will help borrowers avail themselves of the benefits that Congress and DoE have created while reducing unnecessary red tape that can lead to delinquency and default.

C. Preempt Certain State Lawsuits Against Federal Student Loan Servicers

The federal student loan program was purposely housed within the federal government and contemplates exclusive supervisory authority by the federal government for the stated purposes of ensuring uniformity and the efficient administration of federal student loans across the nation. “Uniformity not

171. See *supra* section III.A.

only reduces costs but also helps to ensure that borrowers are treated equitably State-level regulation subjects borrowers to different loan servicing deadlines and processes depending on where the borrower happens to live, and at what point in time.”¹⁷² Subjecting federal student loan servicers to actions grounded in state law not only subverts the stated objectives of uniformity, equity, and cost-savings in the administration of federal loans, but also threatens the safety and soundness of the federal servicers by subjecting them to money judgments that could serve to reallocate taxpayer dollars into the coffers of a select few.

Increasingly, challengers have filed private actions against federal student loan servicers in courts across the country seeking to hold federal student loan servicers financially liable for perceived wrongdoing. These actions are commonly grounded in a state-specific consumer protection law, such as the Connecticut Bill of Rights or the Colorado Student Loan Servicers Act, as well as in tort for issues such as negligent misrepresentation. Often, the state consumer protection statutes impose additional and conflicting requirements on federal student loan servicers, such as disclosure requirements, deadlines to respond to borrower inquiries, and required specific procedures to resolve borrower disputes.¹⁷³

Allowing private borrowers to sue for violations of these state requirements forces the servicers to reallocate resources from borrower assistance towards litigation expenses. By imposing costs in addition to those contemplated by the federal student loan servicers during the bidding period for DoE contracts, the federal student loan servicers are bearing the lion’s share of the defense costs, as well as the additional resources necessary to comply with fifty different state requirements.

Moreover, these actions against federal student loan servicers fail to target the party that is often the most accountable for the shortfalls in the federal student loan program: DoE. Instead of bringing actions against federal student loan servicers, borrowers and state attorneys general should focus their efforts—in both litigation and lobbying—on those entities that write the rules that servicers must follow: DoE and Congress. This approach has already proven effective at changing the underlying statutory and regulatory framework governing federal student loan servicers. In fact, a coalition of nineteen states, the District of Columbia, and student borrowers obtained a successful ruling against the DoE in September 2018 regarding DoE’s delay in imple-

172. Federal Preemption and State Regulation of the Department of Education’s Federal Student Loan Programs and Federal Student Loan Services, 83 Fed. Reg. 10619, 10621 (Mar. 12, 2018) (to be codified at 34 C.F.R. ch. VI).

173. *Id.* at 10620.

menting loan forgiveness protections for borrowers designed to “protect student loan borrowers from misleading, deceitful, and predatory practices.”¹⁷⁴ This action was one example of litigation that properly targeted the entity that has the authority and capability to make meaningful changes—DoE—as well as the resources and expertise to address the alleged deficiencies nationwide. In addition to the practical problems created by private enforcement of state laws against federal student loan servicers, subjecting servicers to state regulation undermines the federal interests of uniformity, simplicity, efficiency, and costs-savings to the federal taxpayers.

The most obvious and practical solution to this emerging issue is to preempt actions grounded in state law—including consumer protection statutes (and state UDAP) and common law tort actions—to federal law under the Supremacy Clause. This position is supported by a plain reading of the HEA, as well as by DoE guidance. As the Ninth Circuit has recognized, “Congress’s instructions to the [DoE] on how to implement the student-loan statutes carry this unmistakable command: Establish a set of regulations that will apply across the board.”¹⁷⁵ Actions against federal student loan servicers based upon state law clearly conflict with this congressional directive, and therefore must be subverted to the federal objectives.

D. Require DOE and CFPB to Coordinate Oversight of Federal Student Loan Servicing

As this article has already addressed, federal student loan servicers are not only subjected to conflicting regulation by the individual states, but also by different federal agencies. Within the servicing industry, unclear directives from the CFPB and DoE have created uncertainty and confusion regarding the concurrent enforcement authority. As these two agencies attempt to resolve their conflicts through rulemaking, public letters, information-sharing MOUs, and litigation, servicers face uncertainty operating under the authority of these two agencies. When DoE’s and CFPB’s directives conflict, servicers are left in the difficult position of wondering whether compliance with a DoE policy may subject them to criticism by the CFPB.

To address these interagency conflicts, Congress should require the CFPB and DoE to coordinate their concurrent oversight of federal student

174. *Bauer v. DeVos*, 325 F. Supp. 3d 74, 78 (D.D.C. 2018) (quoting William D. Ford Federal Direct Loan Program, 81 Fed. Reg. 75,926, 75,926 (Nov. 1, 2016)). In this action, the District Court for the District of Columbia granted summary judgment in favor of the coalition of states finding that DoE’s purposefully delayed implementation of the borrower defense regulations was arbitrary and capricious, and therefore in violation of the Administrative Procedure Act. *Id.* at 109.

175. *Chae v. SLM Corp.*, 593 F.3d 936, 945 (9th Cir. 2010).

loan servicers. While the two agencies have found common ground in coordinating the resolution of borrower complaints through their newly signed 2020 MOU, these efforts do little to address the practical issues posed by the concurrent and conflicting enforcement authority.¹⁷⁶ Rather than impose duplicative and potentially conflicting regulatory oversight, the agencies should coordinate their efforts so that servicers are not forced to navigate between the two.

E. Increase Servicer Compensation for Moving Delinquent Borrowers into Assistance Programs

Under the current compensation structure, federal student loan servicers are paid decreasing amounts for federal loans that are delinquent or in deferment or forbearance. This system is meant to discourage servicers from allowing borrowers to enter into delinquency and other nonpayment plans. However, this structure fails to appreciate that borrowers end up in these programs for a myriad of reasons—family issues, economic challenges, employment market shifts, etc.—all of which are exogenous to the actions of loan servicers. Further, the current compensation structure fails to reward servicers for their successful efforts in helping borrowers qualify for IDR plans.

We propose two fundamental changes to the compensation structure to properly align congressional incentives with the realities of student loan repayment. First, servicers should be paid a premium for federal student loans that are successfully enrolled in an IDR plan. This would serve a twofold purpose: (1) incentivize federal student loan servicers to enroll borrowers in IDR plans, and (2) properly account for the increased costs to servicers to assist borrowers into an IDR plan, as well as manage borrowers in IDR plans. Helping borrowers enroll in an IDR plan involves increased costs in terms of borrower outreach to inform them of the deadlines, the time and costs involved in explaining the eligibility criteria to borrowers over the phone, and the resources involved in actually assisting borrowers successfully complete the IDR application. It is important to recognize that the costs to the servicers do not end once the borrower is enrolled in an IDR plan. Instead, the servicers must continue to expend additional resources in reminding borrowers of their annual recertification and increased borrower outreach to ensure that borrowers remain in the proper repayment plan based on their particular financial circumstances.

Second, the current compensation structure punishes servicers for every loan that is in deferment or forbearance by paying almost twenty percent less

176. Borrower Complaints Memorandum, *supra* note 167.

for such federal loans compared with federal loans that are in current repayment status.¹⁷⁷ By compensating servicers less for federal loans that are in deferment or forbearance, DoE is implying that deferment and forbearance are not sound decisions for borrowers—in direct contrast to other DoE and federal guidance encouraging needy borrowers to take advantage of these programs. In fact, forbearance is the right choice for many borrowers who have a better sense of their current and projected financial and personal situation than the government or a servicer (e.g., only the borrower would know “I am about to quit my job,” “I am about to start to a new job with better pay,” or “my expenses are about to go up with a new child”). As a result, the legal framework should encourage servicers to communicate program benefits and requirements, but generally allow individuals to make an informed choice on that basis. Moreover, participating in a brief period of forbearance can help borrowers become current on their loan obligations and make them eligible for an IDR plan. Therefore, the compensation structure fails to appreciate the material benefits involved in forbearance and deferment.

Instead of fiscally punishing servicers for assisting borrowers based upon their particular financial circumstances, DoE should expend greater efforts to ensure that borrowers fully comprehend the potential positive and negative consequences of entering into forbearance so that borrowers can make a knowing, informed decision on that basis. This goal is not achieved by compensating servicers less for each loan in forbearance or deferment. By making these minor changes to servicer compensation, DoE will better align fiscal incentives with the realities of federal student loan servicing, to the betterment of both servicers and borrowers.

F. *Preempt State Requirements to License Federal Student Loan Servicers*

Licensing laws exist to ensure that those providing a good or service to the public do so in a safe and professional manner. DoE goes to great lengths to ensure that federal student loan servicers can effectively service federal loans: DoE requires federal background checks for all servicer personnel, mandates training for all employees, audits servicers’ systems and facilities at regular intervals, continually monitors the performance of its servicers, and censures servicers who fall short of these standards through both contractual and administrative means.¹⁷⁸ While DoE’s oversight cannot guarantee that federal

177. See Great Lakes Servicing Contract, *supra* note 53, at 13.

178. Nelnet, Inc. Servicing Contract No. ED-FSA-09-D-0013, DEP’T OF EDUC., Attach. A-1, 11 (2009), <https://www2.ed.gov/policy/gen/leg/foia/contract/nelnet-061709.pdf>.

student loan servicers will never make a mistake, no licensing regime promises perfection; as it stands, DoE has created a comprehensive set of standards that provides a high degree of reliability for servicing personnel.

Additional state licensing requirements for federal student loan servicers do little to add to this. Instead, these state licensing requirements merely increase the operating costs for the servicers to service federal loans in that particular state. This is fundamentally unfair since “[a] servicer does not have the choice to refrain from operating in a particular state to avoid licensing fees and other costs imposed by the state. Rather, the states are using the servicers’ compliance with federal law and contracts to extract payments that benefit the state at the expense of the federal taxpayer.”¹⁷⁹ Moreover, these additional requirements were not contemplated by the federal student loan servicers or by DoE at the time the contracts were negotiated. Therefore, the servicers are forced to shoulder the unexpected, increased operating costs arising from state licensure requirements—servicers cannot renegotiate an existing contract or push their costs onto the federal government or borrowers. Thus, state licensing regimes increase the costs involved in administering the federal student loan program without providing any corresponding safeguards or additional benefits to the borrowers.

To address this issue, Congress should amend the HEA to expressly preempt all state licensure requirements for federal student loan servicers if the servicer is a DoE-approved servicer. This would ensure that Congress’s stated interests of uniformity, efficiency, and cost-savings are carried out and that such objectives remain free from unwarranted intrusions by the individual States. Such preemption would further protect the federal taxpayers from taking on the burden of incessant and duplicative litigation, as well as ensure that federal contracts are not subverted.

CONCLUSION

The federal student loan program was designed to increase access to higher education for Americans across all socioeconomic classes and was housed within the federal government to ensure that borrowers were treated uniformly across the nation, but the statutory and regulatory framework cobbled together over decades falls short of this goal. As a result, neither federal student loan servicers nor borrowers can thrive, causing the rise of delinquency and default rates which will only increase over time.

179. Federal Preemption and State Regulation of the Department of Education’s Federal Student Loan Programs and Federal Student Loan Services, 83 Fed. Reg. 10619, 10621 (Mar. 12, 2018) (to be codified at 34 C.F.R. ch. VI).

Increasingly, those looking to place the blame for the clear failings of the federal student loan program have been pointing their fingers at federal student loan servicers, as the servicers are often the most visible party operating within the federal student loan sphere. Painting the servicers as scapegoats for the student lending crisis not only misplaces the blame but obfuscates the true problem giving rise to the crisis: the unwieldy and complicated framework of statutes and regulations governing the federal student lending program. Further, the lack of any underwriting during federal student loan origination necessarily means a greater number of loans will end up in default. And as the government continues to issue loans without regard for how students' ability to repay, it is unsurprising that a significant number of these loans go into default—as a complete underwriting review presumably would have indicated.

The current student lending crisis was created by a piecemeal statutory and regulatory framework. As a result, DoE has enacted extensive, overlapping, and contradictory regulations imposing federal student loan servicing requirements that can lead to borrower confusion. With rising defaults from a lack of underwriting, and borrower assistance programs that are falling short of their stated goals, there is an urgent need for legislative and regulatory action to address the rising increase in student loan defaults.

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