Improving Program Administration by Promoting Better Loan Servicing for Student and Parent Borrowers

Since 2009, the U.S. Department of Education has used not-for-profit (NFP) and for-profit servicers to provide important services to student and parent borrowers with loans made under the William D. Ford Federal Direct Loan Program. Many nonprofit and for-profit servicers also service loans made under the federal guaranteed student loan program and through private education loan programs.

The Department has contracts with 10 for-profit and NFP providers who service the Direct Loan portfolio of over 31 million borrowers. Four of the servicers, the Title IV Additional Servicers or TIVAS, signed their original contracts in 2009 and signed renewal contracts in 2014. The six NFP servicers signed their contracts in 2011 and 2012. The Department is currently in the process of re-competing all of its student loan servicing contracts and has stated publicly that it anticipates major changes to its system, which will impact millions of borrowers across the country. In addition, the Consolidated Appropriations Act, 2014, required the Department to establish common performance metrics across all student loan servicers. The Consolidated Appropriations Act, 2016, requires the Department to allocate new Direct Loan accounts among the student loan servicers on the basis of their performance and capacity. The Act also directs the Department to ensure the participation of a sufficient number of servicers to promote high-quality customer service in the servicing of consolidation loans. The current competitive structure – using a mix of state-based and national, and nonprofit and for-profit, organizations - promotes high levels of customer service; establishes a benchmark for quality servicing; protects the interests of the federal government while providing important localized services to borrowers; encourages innovation; and saves taxpayers money.

The student loan servicing system is <u>not</u> broken. The nation's student loan servicers provide an array of important, high-quality services to student and parent borrowers, at minimal costs to the federal government. Besides handling general billing and payment processes, student loan servicers:

- Are the primary contact point for borrowers regarding their Direct Loans. For students that are in-school or in their 6-month grace period before beginning repayment, the servicer may be their first contact with anyone who helps them with their loan. Student loan servicers spend millions of dollars locating and educating students on their financial obligations and how to balance their student loan payments with other bills.

- Assist students and parents that are in repayment on their student loans, including working with these borrowers to identify and enroll in the most appropriate repayment and loan consolidation plans to meet their unique and individual financial situations. Student loan servicers have helped more than 4.5 million Direct Loan borrowers successfully enroll in the program's income-driven repayment plans.

- Assist servicemen and women in understanding and signing-up for the benefits under the Servicemembers Civil Relief Act (SCRA). Each servicer has a dedicated person with expertise who has been specially trained to respond to inquiries on all aspects of the military entitlements, forms, regulations, and military repayment options as they relate to federal student loans. All student loan servicers review the borrowers in their portfolio against the U.S. Department of Defense (DOD) database monthly and apply the benefit based on that match.

- Help borrowers who are delinquent in repaying their Direct Loans, including ensuring they are aware of the various options under the law to get their loans back in good standing.

Student loan servicers are highly-supervised and regulated, both by the U.S. Department of Education and the Consumer Financial Protection Bureau (CFPB). They must comply with all statutory, regulatory, and contractual requirements, including compliance with the Federal Information Security Management Act (FISMA), and have highly-specialized systems for handling the unique requirements for servicing federal student loans. The Department evaluates each servicer quarterly based on a common set of performance metrics: (1) the percentage of borrowers in current repayment status (defined as making their loan payment within 5 days of the established due date) – 30 percent weighting; (2) the percentage of borrowers more than 90 but less than 271 days delinquent – 15 percent weighting; (3) the percentage of defaulted borrowers (over 270 days and less than 361 days delinquent) – 15 percent weighting; (4) borrower survey results – 35 percent weighting; and (5) Federal Student Aid (FSA) employee survey results – 5 percent weighting. The resulting competitive structure is designed to incentivize servicers to help all borrowers select the best repayment option for them and provide enhanced customer service for student and parent borrowers at all stages of the student loan life cycle.

NCHER Reform Proposals

The National Council of Higher Education Resources (NCHER) supports the important and successful work of the nation's student loan servicers in helping student and parent borrowers repay their loans. We urge Congress to promote better loan servicing for student and parent borrowers by:

- <u>Continuing its oversight of the Department's management of student loan servicing to prevent adoption of disruptive proposals that will harm students.</u> As noted above, the Department is currently in the process of developing a Request for Proposals that it anticipates will include major changes to student loan servicing, including potentially moving to a single servicer or a single servicer platform aimed at improving the borrower experience. These ideas are not advisable and would not improve student loan servicing. This approach failed previously and would undermine the current structure that promotes competition among state, nonprofit, and for-profit entities with decades of experience in assisting student and parent borrowers. It would also prevent the Department from allocating additional loan volume to high-performing servicers or pulling loan volume from low-performing servicers; and magnify risk, stemming from both system and security failures. Through the use of a group of decentralized providers, the risk to the federal government is diversified, and competition and innovation are encouraged. NCHER believes it is fundamentally unfair to artificially reduce the number of current servicers as long as they continue to meet the performance metrics. Another proposal reportedly being considered is the creation of a single student and school portal or point of contact, leveraging the existing National Student Loan Data System for Students (NSLDS). While this idea shows promise and could help students and parents contact their servicers and make them aware of which servicers are responsible for their student loans, Congress should ensure that any final plan does not make student loan servicing more complex and confusing for borrowers and servicers.

- <u>Ensuring there are common performance metrics across all servicers, and allocating loan volume to the highest performers.</u> Over the last two years, the House and Senate Appropriations Committees have directed the Department to establish common performance metrics across all student loan servicers, and then allocate new student loan volume based on performance and capacity. Congress should include language in the reauthorization of the Higher Education Act providing for an open competition between multiple servicers, where higher-performing servicers receive more loan allocations. This is critical to improving the quality of servicing for all borrowers. Congress should also authorize all student loan servicers to originate and service consolidation loans. The unfortunate result of the Department's current action preventing the NFP servicers from offering consolidation loans is that borrowers interested in obtaining a consolidation loan are required to switch to a new servicer who they have had little or no contact with throughout their postsecondary education career, even if they are happy with the performance of their NFP servicer, and thereby denied consumer choice.

- <u>Promoting the use of smaller state and nonprofit organizations with expertise in helping student and parent borrowers.</u> With federal student loan debt totaling more than $1.2 trillion and with unacceptably high delinquency and default rates, it is clear that students, borrowers, and families need access to more specialized support services to help them understand their postsecondary education options. State-based and state-affiliated nonprofit higher education assistance agencies, including lenders, servicers, and guaranty agencies, have been highly successful in providing these important services for decades. Congress should direct the Department to require its student loan servicers to work with these organizations as subcontractors to provide state and local personalized financial education and debt management services to struggling borrowers. As part of this effort, Congress should make clear that the definition of 'small business' in the student loan servicing context includes state and not-for-profit entities so that student loan servicers receive credit for subcontracting for services with these organizations.

- Encouraging more innovation. Similar to the "Experimental Sites" program for schools, the Department should widely expand the ability of servicers to utilize their expertise and experience to test and create best practices that can improve the borrower experience and protect the taxpayers' investment. Congress should also look at targeting more intensive services to borrowers who need it most. For example, the Department could build and expand upon its work around specialty servicing and late-stage delinquency. The Department could also test the use of data analytics to target servicer resources.

If you have questions or need more information, contact Sean Deverey, Vice President for Government Relations at the National Council of Higher Education Resources (NCHER), at sdeverey@ncher.us or (202) 822-2106.

Legislative Language

Section 456(b) of the Higher Education Act (20 U.S.C. 1087f) is amended by inserting the following:

"(5) IMPROVEMENTS TO STUDENT LOAN SERVICING.

(A) IN GENERAL. The Secretary shall establish and carry out common, performance-based metrics and methodology when allocating newly originated loans among student loan servicers with which it has entered into servicing contracts under paragraph (2).

(B) PRE-EXISTING LOANS FOR BORROWERS. The Secretary shall ensure that additional loans to borrowers whose loans are being serviced by the Secretary under this subsection are assigned to the servicer of the pre-existing loans.

(C) TRANSITION TO COMPARABILITY. Until such time as the portfolios assigned to each student loan servicer are comparable, the Secretary shall employ performance metrics and methodology that take into account the differences in the portfolio composition of loans being serviced. Each loan servicer shall, no later than July 1 of each year, provide a certification to the Secretary as to its servicing capacity for the following fiscal year, and shall immediately notify the Secretary should there be a change in the servicer's capacity. The Secretary shall not allocate additional loan volume to any servicer if such allocation would result in the servicer being assigned more loans than its certified capacity.

(D) INNOVATION. The Secretary is authorized to carry out demonstration projects to promote innovation in the servicing of the federal student loan program. Such projects may include

(i) Approaches that test and create best practices that can improve the borrower experience and protect the taxpayers' investment.

(ii) Approaches that promote specialty servicing that provides more intensive services to struggling borrowers and late-stage delinquency.

(E) REPORT. On a quarterly basis, the Secretary shall submit a report to the Committee on Education and the Workforce and the Committee on Appropriations of the House of Representatives and the Committee on Health, Education, Labor and Pensions and the Committee on Appropriations of the Senate that:

(i) describes the performance methodology used by the Secretary under paragraph (A) or (C) in evaluating servicer performance;

(ii) contains the results under the performance methodology used by the Secretary under paragraph (A) or (C) for each servicer for the prior quarter;

(iii) contains the number of borrower accounts being serviced by each servicer at the end of the prior quarter;

(iv) contains the number of new accounts assigned to each servicer during the prior quarter (broken out by whether the accounts are for new borrowers or constitute additional loans to borrowers whose loans were previously assigned to the servicer); and

(v) describes and reports on the results of the demonstration projects undertaken under paragraph (D)."