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STUDENT LOAN SERVICING ALLIANCE

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Senate Information Hearing on "The Changing Face of Student Loan Servicing in California"
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Thank you, Chairman Dodd, Vice Chairman Vidak, and other honorable Members, for your invitation to speak today. I am executive director of the Student Loan Servicing Alliance, or SLSA, a non-profit membership organization of federal student loan servicers. SLSA has approximately 25 servicer members, and together we service about 95 percent of all outstanding student loans. On behalf of our members, I am proud to tell you about the work student loan servicers perform to help borrowers manage repayment.

The Committee staff was kind enough to make copies of a PowerPoint presentation that provides a lot of background information on student loans and student loan servicing. There are approximately $1.4 trillion in outstanding student loans, with the lion's share being federal loans -- $1.3 trillion. More than $1 trillion (and the fastest growing piece) is made up of loans that are made and/or held by the U.S. Department of Education. I will therefore focus on federal loans in my testimony today, but I am happy to take questions on any element of servicing.

To begin, I'd like to share a few insights and trends related to student loans.

Most students who graduate from college have both reasonable loan balances and the income to support repayment. That fact is often lost when reports focus only on anecdotes.[1] According to the College Board, however, nearly 40 percent of students don't borrow at all. Those who do borrow graduate with an average of $28,100 in debt.[2]

We should also review the latest trends in delinquencies and defaults. If you simply read the stories, you would think that defaults are increasing at an alarming pace. But the facts tell a different story. From Federal Student Aid data, serious delinquency (90+ days) rates are down 24 percent in three years.[3]

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[1] Matt McDonald and Pat Brady, "Media Coverage of Student Debt," Hamilton Place Strategies: www.hamiltonplacestrategies.com/insights/media-coverage-student-debt/
[2] College Board, Trends in Student Aid: https://trends.collegeboard.org/student-aid
[3] FSA Data Center, "Direct Loan Portfolio by Delinquency Status"

There are reports that point to the fact that the cumulative number of defaults continues to rise. Of course they do, as the federal government never write offs a defaulted loan. Some of these defaults are decades old. The fact is: the rate at which student loan borrowers defaulted has dropped for a second consecutive year. The actual number of direct loan borrowers defaulting declined by five percent last year, even though the number of borrowers repaying their loans increased.

That said, there are some borrowers who struggle to repay their loans. The borrowers who struggle most are often those who did not finish college. A White House report published last year by the Obama administration showed that two-thirds of defaults came from borrowers with less than $10,000 in balances. One third had a balance of less than $5,000.[4] At these levels, it is clear these are borrowers who went to college, borrowed, but did not complete their degree. Those who did not complete are three-times as likely to default as those who achieved their degree.

I provide this context because I think it's important to understand the issue and how the borrowers facing the most challenges are not necessarily the ones you hear about or read about. We need to have better information to these borrowers *before they borrow* to stress the importance of completion and its relationship to borrowing success.

The decision to borrow, and how much, is not part of the servicing system. Servicers do not have anything to do with where a student choses to go to college or how much they borrow to pay for that education. In the federal student loan process, the borrower decides to attend a specific college or university, is awarded financial aid (including loans) by the college, signs a promissory note provided by the Department of Education, and undergoes loan counseling mandated by the Higher Education Act through the college. The student loan servicer only becomes involved after the borrower has taken all of those steps, and has already incurred the debt.

The federal student loan program is too complex. The federal student loan program is highly and specifically regulated in terms of borrower treatment. There are both statutory and regulatory requirements for loan servicing. These include specific disclosures and notices at various points in the loan cycle, due diligence requirements in terms of how often delinquent borrowers must be contacted, and how they must be contacted, including by telephone. There are certain deferments to which borrowers are entitled under the terms of the Higher Education Act, and discretionary forbearances which are administered in accordance with the lender's written policy and Department of Education regulations and guidance. In addition, the federal loan servicers who service loans on behalf of the Department of Education are contractors, and must follow detailed and proscriptive sub-regulatory guidance issued by the Department.

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[4] : President's Council of Economic Advisors, "Investing In Higher Education: Benefits, Challenges, and The State Of Student Debt," July 2016

There are multiple types of federal loans and 16 repayment plans, including nine possible versions of plans in which the monthly payment amount is based on income. There are eight forgiveness programs, and 32 deferment and forbearance options. All of these plans have different statutory and regulatory requirements in terms of eligibility. The form for signing up for an income-driven repayment plan is 10 pages long.

An examination of the student loan complaints filed to date with the Consumer Financial Protection Bureau bears out this complexity – more than 85 percent of all student loan complaints with the CFPB have been resolved and "closed with explanation." A recent analysis by one of SLSA's larger servicers found that only 10 percent of federal loan complaints and 1 percent of private student loan complaints were related to an actual servicing error. The majority of issues raised in connection with federal loans involved a consumer disagreeing with federal law or policy, including federal requirements on credit reporting, repayment options, and loan forgiveness. The most common issue for private loans involved requests for lower payments, including requests for repayment options that are unique to federal loans (i.e., income-based repayment).

We have concerns about how state regulation of federal loan servicers will work, and whether it will increase the complexity. The entire $1 trillion in federal loans issued and/or held by the U.S. Department of Education is serviced by nine entities acting as contractors for the federal government on multiple servicing platforms or systems. The Department is currently in the midst of a contract solicitation that will radically change the servicing of federal loans. Under the new contract, all Department-owned loans will be serviced on a single platform/servicing system. The contract procurement contains very detailed specifications for what the servicer must do in all situations. The contract was expected to be awarded early this year, but has been held up by a bid protest. Once the contract is in place, it is hard to imagine how state laws would apply in many instances. Many of the practices that the CFPB criticizes the servicing industry for are things that are hard-wired into the servicing system, and automatic. For example, if a state disagrees with the way that payments have been processed under the federal contract, and withdraws the servicer's license, it means that no borrower in that state will be able to have their federal student loans serviced at all. This result is unimaginable.

Many FFELP and private student loan servicers are relatively small, state-based entities created by the legislature of a state to serve the students and families of that state. They are only permitted to make student loans to residents of their state or students attending colleges and universities in the state. Given that recent graduates are a very mobile population, however, it is likely that some of their borrowers will end up moving to another state, a fact that is beyond the servicer's control. The costs of licensure and examination in multiple states will be prohibitively expensive for these small entities. They will be forced to transfer the loans to another servicer, which will be very disruptive to the borrower, or they may be pushed to exit the servicing business entirely. The latter is not an empty threat; two of SLSA's members exited the servicing business altogether in the last year because of the increased costs of servicing student loans.

Federal loan servicers under the current contract to the Department of Education can be paid no more than $34.20 per borrower per year, regardless of the number or type of loans the borrower may have. That is for a loan in repayment. As a loan becomes increasingly delinquent, the servicer is paid less and less. These fees are far lower than mortgage servicing fees. The money to pay for licensing and examination fees in various states has to come out of this same fee, and will take away from servicers' ability to do more to help struggling borrowers.

With respect to California and other states considering regulating student loan servicers, our concern is assuring that the legislation does not impose requirements that conflict, directly or indirectly, with federal requirements. Further, we have great concerns over the breadth and vagueness of regulatory structure that the new statute imposes. We are anxious to work with you and other states to eliminate these conflicts and create increased clarity around the statute's requirements.

Student loan servicers help millions of consumers repay their education loans, and avoid the negative consequences of default. Servicers help ensure student loan borrowers, many of whom have limited financial experience, know about and can take advantage of the various repayment options available to them. Borrowers rely upon the consistent, even application of federal regulations by student loan servicers in order to navigate the ocean of benefits and requirements that surround student loans. Servicers work tirelessly on behalf of borrowers to enroll them into the right payment plan for their individual circumstance, while helping them avoid delinquency and default. Since June 2013, the number of Direct Loan borrowers in income-driven repayment plans has grown from 1.58 million to 5.58 million.[5]

Imposing conflicting information, or additional procedural requirements, on borrowers who can immediately obtain assistance with their student loans directly from their servicer, is bound to cause confusion for borrowers. They may then fail to seek help from their servicer and delay a satisfactory resolution to their concerns.

Bottom line: there are better solutions to address the real problem of student loan debt. Congress is expected to reauthorize the Higher Education Act during this Congress, and SLSA is working hard to urge legislators to simplify the federal student loan programs, including the number of repayment plans, and the complex rules governing their terms and conditions. In addition, the counseling provisions must be strengthened, and more counseling needs to take place before the borrower takes out a loan.

On the state level, some legislatures have adopted or are considering legislation that requires colleges and universities to provide the borrower with better information about the loans they are about to take out, including the monthly payment amount that the borrower can be expected to pay, and the cumulative cost of borrowing for the next several years. In Indiana, for example,

[5] FSA Data Center, "Direct Loan Portfolio by Repayment Plan"

the legislature required public colleges and universities to send borrowers an annual letter with information on the amount they have borrowed to date; as a result of these letters, students in Indiana are borrowing less.

Several states are considering the creation of a new position of student loan ombudsman to work with borrowers in the state to answer their questions and deal with their complaints. We already work closely with the Office of the Ombudsman at the U.S. Department of Education. Servicers would be more than happy to work with ombudsmen financed and operated by the state, and to share our knowledge of the complexities of federal student loans, to help them better serve borrowers in the state. We think that having a neutral and trusted third party deliver the same facts as the servicer would be helpful to borrowers.

As indicated above, the vast majority of complaints from student loan borrowers tend to arise from a misunderstanding of the terms of their loans, which are statutory or regulatory, and cannot be waived or changed by a loan servicer. Ensuring that student loans are treated the same for borrowers across the country ensures that borrowers can be confident in their understanding of their opportunities to succeed in repayment and maintain a healthy financial history.

I would be more than happy to take questions and to provide additional information about student loan servicing.