

Tug-of-War on Loan Servicing

As states become more active in regulating the companies that collect and handle student loan payments, servicers seek answer from Secretary DeVos on whether federal policy pre-empts new rules.

By [Andrew Kreighbaum](#)

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The Department of Education's announcement in May that it would rescind extensive requirements for loan servicers previously issued by the Obama administration was a red flag to skeptics who already doubted Education Secretary Betsy DeVos's commitment to protecting student borrowers.

Those requirements pressed servicers to be more active guides for borrowers seeking to pay off their student loan debt. And they said servicers would be judged based on outcomes for borrowers as well as the effectiveness of communications to borrowers, including special outreach to those at risk of default.

Despite assurances to the contrary from DeVos, many state lawmakers and regulators over the past year have responded by strengthening their own oversight regimes -- in one case, by largely adopting the Obama requirements. The drive for tougher oversight in many states has formed the backdrop to a dispute between servicers and regulators, with DeVos in the middle.

Now both sides are waiting for the secretary to weigh in one way or another -- to recognize that federal policy pre-empts state regulations or, if attorneys general have their way, to stay out of their oversight of the sector.

Unlike state laws governing campus policies, though, the new regulations of servicers affect entities operating across state lines, drawing complaints from entities that say they shouldn't have to comply with a patchwork of federal and state regulations.

In the first in a volley of letters to DeVos over the summer, the Education Finance Council, which represents nonprofit and state-based servicers, [called on](#) the secretary to make clear that federal law takes precedence in the event of a conflict with state law.

"We support any federal or state law that is protecting borrowers and is helping borrowers -- that we agree with 100 percent. Our specific concern is in the event of a conflict between federal and state law, servicers will have difficulty determining which to comply with," Debra Chromy, the president of EFC, said in an interview. "Additionally, we are concerned with a patchwork of 50 different state laws that not only servicers would have to comply with, but also that would require borrowers to figure out what their rights are from state to state, rather than having those rights clarified and encoded on a federal level."

Chromy said if states have concerns about regulatory standards for servicers, they should address those concerns at the federal level.

The National Council of Higher Education Resources in [a July letter](#) to DeVos offered even more detailed complaints about specific state laws and regulatory activity by state law enforcement officers.

But last month, a group of 32 Democratic and Republican state attorneys general [told DeVos](#) that the Higher Education Act, which authorizes Title IV federal aid programs, does not give the feds the power to pre-empt state consumer protections.

Colleen Campbell, associate director for postsecondary education at the Center for American Progress, said it's natural that state elected officials are taking a

hard look at loan servicers. Student loans are one of the top higher education issues when it comes to voter interest, she said.

The perception that the Department of Education has backed off oversight in the first months of the Trump administration likely fuels the push for tougher oversight by the states, Campbell said.

“If you’re running for office and you’re not seen as being tough on companies profiting off the student loan space, or you don’t really have a stance on student loans, it’s not a good look,” she said.

Several Democratic AGs have partnered with the Consumer Financial Protection Bureau to bring lawsuits against servicers such as Navient. While the CFPB has been active in oversight of loan servicers, Campbell said many consumers are not aware of the resources it provides. And many issues at the state level, she said, won’t be broad, systemic problems that can trigger federal involvement. “They’re kind of an easy boogeyman to go after,” she said. “At the same time, they’re probably not doing a great job. And we’re not compensating them in a way to incentivize them to do a better job. Servicing is a kind of new frontier to look to hold large entities accountable.”

Connecticut, California, Illinois, Massachusetts and Washington, D.C., have all added new requirements for servicers in the name of protecting student borrowers.

EFC said that the District of Columbia’s new emergency loan regulations created the most “heightened” sense of alarm because its fee schedule would mean servicers lose money by operating in the city.

Tanya Bryant, a spokeswoman for the D.C. Department of Insurance, Securities and Banking, said the fee schedule was based on similar regulatory regimes in California and Connecticut.

She said the department has met with student loan servicers to discuss issues with that fee schedule and is reviewing concerns raised through the public comment process. DISB will address any concerns over fees in a forthcoming final rule making.

The loan servicing group also said Connecticut's new servicing standards, issued in July, include requirements that would push servicers into loan counseling -- a much different activity than taking payments.

And NCHER complained to DeVos that Connecticut had largely adopted the servicing requirements of the "Mitchell memo" -- the Obama administration document issued by then Under Secretary of Education Ted Mitchell laying out new consumer requirements in the next federal servicing contract -- even though the department itself withdrew the document in May.

"This leads NCHER and its members to theorize that the 'Mitchell memo' is in effect, but just in certain states," said NCHER President James Bergeron in the letter to DeVos.

A Connecticut law requiring that student loan servicers apply for licenses to operate in the state went into effect last year. In July, the state issued the new set of student loan servicing standards, drawing the ire of the servicers.

Matt Smith, director of government relations and consumer affairs at the Connecticut Department of Banking, said those standards were required by statute. And they were largely based on standards already in place for industries like mortgage servicers.

There is growing evidence that more action is needed from federal and state regulators to rectify poor performance by servicers, said Ben Barrett, a program associate with the education policy program at New America, who follows servicing issues.

“There definitely needs to be some coordination between states and between the states and the federal government to ensure there aren’t any hiccups,” he said. “But they’re trying to protect servicers against having to comply with myriad state regulations.”