November 6, 2017

California Department of Business Oversight
Attn: Mark Dyer, Legal Division
1515 K Street, Suite 200
Sacramento, CA 95814

RE: PRO 01/17

Dear Mr. Dyer:

The National Council of Higher Education Resources ("NCHER") is writing to provide comments on the proposed regulations (the "Proposed Rule") released by the California Department of Business Oversight ("DBO") on September 15, 2017, implementing the Student Loan Servicing Act (Chapter 824, Statutes of 2016 - the "Act") enacted last year. NCHER is a national, nonprofit trade association representing state, nonprofit, and private organizations that administer education programs that make grant and loan assistance available to students and parents to pay for the costs of postsecondary education. Our membership includes organizations under contract with the U.S. Department of Education (the "Department") to service loans made under the William F. Ford Federal Direct Loan Program, servicers and guaranty agencies fulfilling their respective roles in the legacy Federal Family Education Loan Program ("FFELP"), and organizations that service private education loans. Seven of the organizations included in the group of larger participants in the student loan servicing market, as such term is defined by the Consumer Financial Protection Bureau ("CFPB"), are members of NCHER.

NCHER understands that, with all the attention being devoted to the cost of college and how to pay for it, states are looking to identify their role in postsecondary education. Our organization agrees that more can be done at both the federal and state levels to increase college affordability, the real problem underlying most of the concerns addressed in the media. Borrowers are overburdened with student loan debt not because of decisions made by their federal and private servicers, but because the cost of college continues to rise as states reduce their investment in higher education and colleges and universities continue to shift the burden of paying tuition and fees to students and their families. To address this challenge, NCHER supports the establishment of state-based student loan ombudsman offices that can serve as a local advocate for student loan borrowers. Under FFELP, this important role is provided by state and nonprofit guaranty agencies, such as Educational Credit Management Corporation ("ECMC"), the designated guarantor for California. With the elimination of new FFELP originations in 2010, the Department's Federal Student Aid Ombudsman Group and the CFPB Student Loan Ombudsman now largely handle this responsibility for loans made under the Federal Direct Loan Program. Despite the existence of multiple federal agencies involved in this effort, NCHER sees benefit in having state-based borrower advocates as long as the costs of running such offices are borne by state governments and not the student loan industry.

The Proposed Rule requires federal and private student loan servicers to obtain a license to operate in the state of California, and requires such servicers to meet certain minimal standards for student and parent borrowers. NCHER offers the following comments on each respective part:

I. Federal and Private Student Loan Licensing

The Initial Statement of Reasons issued by the DBO states that “All servicing of federal student loans is contracted out to and performed by just nine entities,” implying that these are the only organizations subject to the Act. While it may be reasonable to expect that the federal student loan servicers employed by the U.S. Department of Education, which owns more than 75 percent of all outstanding borrower accounts, to obtain a license, the law would also apply to guaranty agencies and small state-based servicers. As detailed below, these organization should be exempted from the Act’s licensing requirements.

Guaranty agencies. Under section 428(b) of the Higher Education Act of 1965 (“HEA”), codified at 20 U.S.C. §1078(b), every FFELP loan is insured by a guaranty agency. There are currently 25 guaranty agencies (though through consolidation, this number is gradually shrinking as the legacy FFELP program winds-down its operations); each is either one of the 19 state agencies or the six private, nonprofit organizations. A guaranty agency’s duties are spelled out in the HEA, and includes working with loan servicers and institutions of higher education to lower student loan default rates, promoting financial literacy, and providing resources that help borrowers to successfully repay their federal student loans. Under the law, they perform limited delinquency and default prevention activities consistent with their agreements with the Department and Departmental regulations. But guaranty agencies do not perform any of the traditional servicing activities such as maintaining student records and processing payments. Nonetheless, the Proposed Rule defines “servicing” to include “interacting with borrowers to prevent defaults,” potentially classifying guaranty agencies as servicers, even though they do not perform the functions generally considered to be part of servicing and it would be impossible for them to comply with many of the requirements of the Proposed Rule. For example, guaranty agencies do not maintain account records for the loans they guarantee and would not be able to provide secure access to account records, including loan balance and status information, and loan histories through the servicer’s website, which section 2049 of the Proposed Rule would require of a servicer. In fact, due to the Federal Information Security Management Act (FISMA), it is certain that federal student loan servicers would not be able to provide guaranty agencies with access to account records on a general basis. NCHER urges the DBO to clarify that guaranty agencies are not “servicers” under the Proposed Rule. For further information on why the Proposed Rule should not classify guaranty agencies as servicers, we draw your attention to the response of the Proposed Rule filed by ECMC.

Finally, contrary to the assertion in the state’s Purposes discussion that “there are no consistent, market-wide federal standards for student loan servicing,” there *are* consistent, market-wide standards for guaranty agencies performing default prevention activities on FFELP loans that have been in existence for decades.

Smaller State-Based Servicers. Over the last few decades, many states have created state-based student loan authorities with the public mission to expand college access and success to residents in their state, including making, acquiring, and then servicing state financed private education loan programs to student and parent borrowers in order to supplement federal financial aid programs. The Proposed Rule would require these state-based student loan organizations to obtain a license even if they service a relatively small number of California accounts. Under the federal tax code, these organizations can only originate and service loans to students and parents of students who, at the time the loans were originated, resided in their state or who attended a school within their state. However, recent graduates are mobile, and a certain percentage move to states throughout the country, including California. The cost of licensure and regulatory compliance in multiple states could be prohibitive for these state organizations. The result may very well be that they exit the servicing business, leaving only a handful of large national servicers active in the program. NCHER recommends that state-based servicers, who are already regulated by the federal government and their individual states, be exempt from the licensure requirement of the bill.

Other States That Have Explored Exemptions. Earlier this year, NCHER worked with the Illinois State Legislature and the Attorney General's office to exempt guaranty agencies and small student loan servicers from its pending licensing legislation. After making many of the same arguments included in this letter to state policymakers, they agreed to include the exemptions in Senate Bill 1351, the Student Loan Servicing Rights Act, which is currently awaiting a veto override in the state house. The final language would exempt the 25 guaranty agencies and those nonprofit private organizations designated by a government entity to make or service student loans, provided the organization services fewer than 20,000 student loan accounts for borrowers who reside in Illinois. NCHER is having similar conversations with representatives from the District of Columbia Department of Insurance, Securities, and Banking responsible for implementing the District's new statute.

Licensing Fees. NCHER does not necessarily object to a requirement that large federal and private student loan servicers obtain a license to operate in the state and the Proposed Rule's application fee and investigative fee of $300 and $100, respectively, seem consistent with other state licensing regimes. But the payment of an annual assessment under section 2057 is unreasonable. This fee is based on DBO's cost of administering the Act, and should be shouldered by the state of California if it has been deemed to be in the public interest, and not by federal and private student loan servicers.

II. Federal and Private Student Loan Servicing Requirements

NCHER opposes the creation of state rules that impose state-specific servicing routines, thus creating significant differences between the servicing of borrowers residing in one state and borrowers residing in other states. The additional regulatory burden of complying with a patchwork quilt of differing state rules would create a regulatory maze confusing to student loan borrowers and servicers alike. The costs could also be prohibitive to all but the very largest federal and private student loan servicers. As noted above, the Department owns more than 75 percent of all student loans today, and that percentage is expected to rise over time since the federal government originates more than 90 percent of all new student loans. The Department pays its servicers a fixed fee of around $2.00 per account per month. The costs of complying with individual state rules means there would be less revenue left over to assist all student and parent borrowers but especially those struggling borrowers who are delinquent or close to defaulting on their student loans.

Given this background, some comments on the specific servicing requirements in the Proposed Rule are as follows:

- State-based, nonprofit organizations – either servicers or guaranty agencies - are chartered and structured to carry out the interests of their public missions. Many of these entities have Board of Directors composed of state officials, including legislators and executive branch officials, and their senior executives who are public employees. Any requirement that these public officials be finger printed and undergo background checks, as would be the case under the Proposed Rule, would be intrusive and could discourage qualified, reputable individuals from serving in these capacities.

- Section 2049(d) of the Proposed Rule states that a servicer must follow instructions provided by a student loan co-signer regarding the application of co-signer payments or, in the absence of instructions, to apply the payment only to co-signed loans. While servicers generally strive to apply payments as directed, instructions are not always clear. Further, loan payments can be made by a number of parties: the borrower, a family member, a cosigner, a government agency (e.g. the Department of Defense) or an employer. A servicer has no means to specifically identify co-signer payments until specifically advised.

- The Proposed Rule would require a servicer to maintain certain account information on its website, accessible to borrowers through a secure log in, including a consolidated report and loan history, as described in sections 2052 and 2053(d) of the Act. In some cases, these requirements are overly prescriptive while, in others, it may not be available to a servicer or is overly vague. For example, the Proposed Rules include a requirement that "loan terms" be provided to borrowers even though it is unclear how such term is defined. Depending on the detail expected, the required information could be lengthy and unhelpful.

- Section 2053(b) of the Proposed Rule requires a servicer to maintain monthly reconciliations of trust account balances. The purpose and meaning of this requirement are unclear.

III. Impact of the Proposed Rule on Federal Servicing Rules, and Federal Preemption

Given the limited revenue to service federal student loans, and the potential conflict between Department requirements and those that would be imposed by the Proposed Rule, a compelling argument can be made that the servicing requirements included in the Proposed Rule are subject to preemption. Current federal regulations "preempt any state law, including state statutes, regulations, or rules, that would conflict with or hinder satisfaction of the requirements or frustrate the purposes of the federal servicing rules" (See 34 CFR 682.411(o)1)). While this regulation applies to the servicing of FFELP loans, the principle logically applies equally to the servicing of federally-owned Direct Loans. Further, federal regulations covering those duties of guaranty agency contains a similar preemption provision (See 34 CFR 682.410(b)(8)).

Thank you again for the opportunity to comment on the Proposed Rules implementing the Student Loan Servicing Act. NCHER would like to work together with the DBO on all of the identified issues discussed above, in support of student borrowers in the State of California. If you have any questions, please contact me at jbergeron@ncher.us or at (202) 822-2106.

Sincerely,

James P. Bergeron
President