March 5, 2019

TO: Mark A. Brown
Chief Operating Officer
Federal Student Aid

FROM: Bryon S. Gordon /s/
Assistant Inspector General for Audit

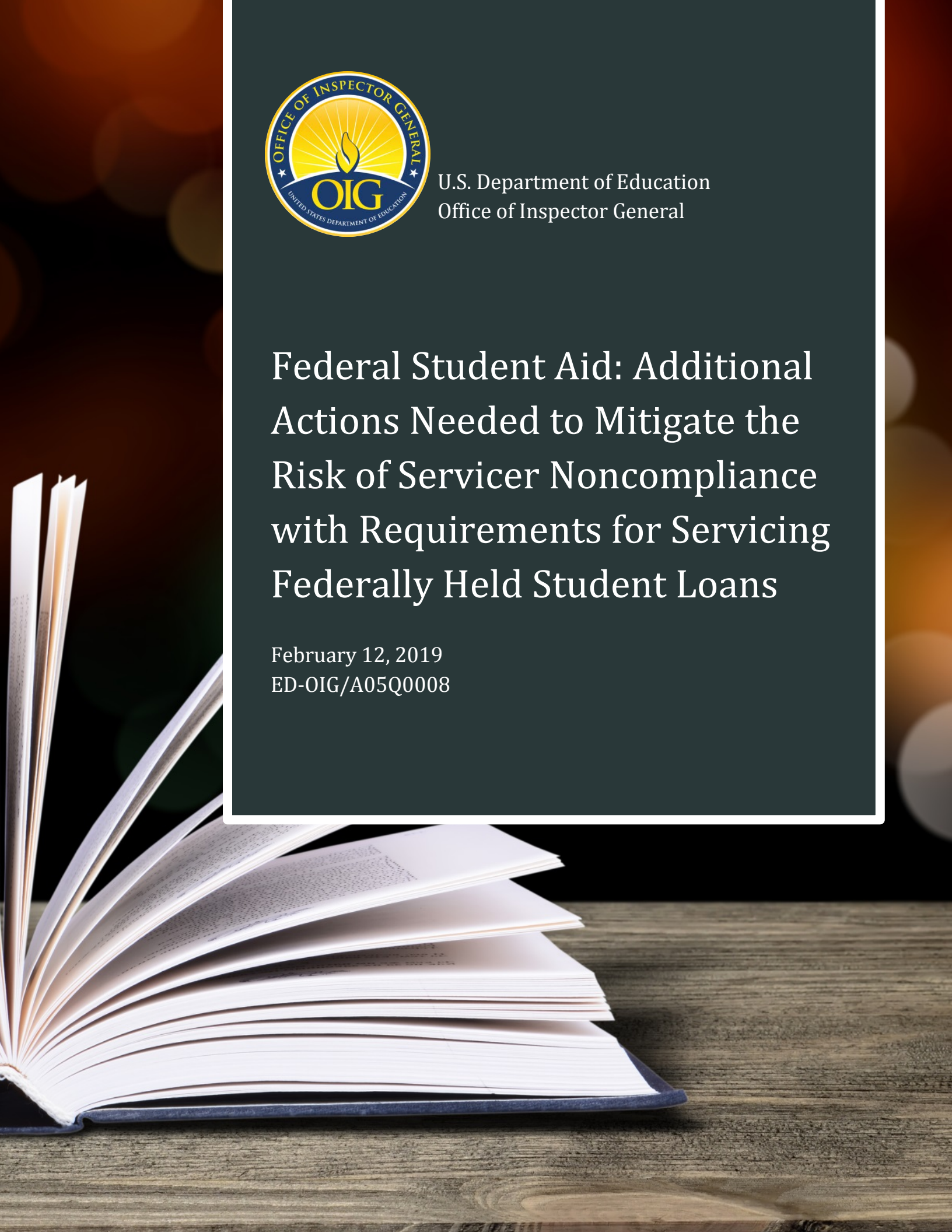
SUBJECT: Reissuance of Final Audit Report, "Federal Student Aid: Additional Actions Needed to Mitigate the Risk of Servicer Noncompliance with Requirements for Servicing Federally Held Student Loans," Control Number ED-OIG/A05Q0008

The attached final audit report, originally issued on February 12, 2019, was reissued on March 5, 2019. After we issued our final audit report on February 12, 2019, we became aware of one instance where a statement made in the report did not reflect supporting audit documentation. We were also provided with additional documentation after the issuance of the audit report that required clarification of a second statement made in the audit report. Once these items were brought to our attention, we conducted a full review of the supporting documentation for the entire report and identified one additional statement that warranted clarification. This review identified no additional issues with the quality of the audit report. We consider these items to be minor corrections. They do not have an effect on our conclusions or recommendations.

First, on page 15, we reported: "In 2017, FSA reduced payments to Great Lakes by $1,260, New Hampshire by $37,438, and Oklahoma by $42,550 because the three servicers billed FSA for borrower accounts despite not complying with administrative forbearance requirements." Although the amounts of the reduced payments are correct, the reason for the reduced payments is not. FSA reduced payments to these three servicers because the servicers did not comply with the requirements of an interest rate reduction program. The report now identifies the correct reason for the reduced payments.

Second, in our response (page 19) to FSA's comments about FSA's May 2017 report on its March 2017 review of Navient, we stated that FSA's comments did not: ". . . accurately reflect the FSA review team's work and observations. The review team's sample did not include only short-duration calls. The review team's report clearly stated that all calls were included in the review team's universe." On February 19, 2019, Navient provided a copy of the instruction from the FSA review team and informed us that FSA had requested that Navient provide only short-duration calls for the review. We revised our response to FSA's comment.

Finally, in the Scope and Methodology Appendix (page 25), we stated that the five components of internal control apply to four categories of the objectives for internal control. The GAO Standards for Internal Control divide the objectives for internal control into three categories, not four. We revised the report to reference only three categories of internal control objectives under the GAO standards.



U.S. Department of Education
Office of Inspector General

Federal Student Aid: Additional Actions Needed to Mitigate the Risk of Servicer Noncompliance with Requirements for Servicing Federally Held Student Loans

February 12, 2019
ED-OIG/A05Q0008

NOTICE

Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report, represent the opinions of the Office of Inspector General. The appropriate Department of Education officials will determine what corrective actions should be taken.

In accordance with the Freedom of Information Act (Title 5, United States Code, Section 552), reports that the Office of Inspector General issues are available to members of the press and general public to the extent information they contain is not subject to exemptions in the Act.

February 12, 2019

TO: James F. Manning
Acting Chief Operating Officer
Federal Student Aid

FROM: Bryon S. Gordon /s/
Assistant Inspector General for Audit

SUBJECT: Final Audit Report, "Federal Student Aid: Additional Actions Needed to Mitigate the Risk of Servicer Noncompliance with Requirements for Servicing Federally Held Student Loans," Control Number ED-OIG/A05Q0008

Attached is the subject final audit report that consolidates the results of our audit of Federal Student Aid's oversight of servicers. We received your written comments disagreeing with the overall conclusion presented but agreeing with the recommendations in our draft audit report and have included those comments at the end of this report.

U.S. Department of Education policy requires that you develop a final corrective action plan within 30 days of the issuance of this report. The corrective action plan should set forth the specific action items and targeted completion dates necessary to implement final corrective actions on the findings and recommendations contained in this final audit report. Corrective actions that your office proposes and implements will be monitored and tracked through the Department's Audit Accountability and Resolution Tracking System.

In accordance with the Inspector General Act of 1978, as amended, the Office of Inspector General is required to report to Congress twice a year on the audits that remain unresolved after 6 months from the date of issuance.

We appreciate your cooperation during this review. If you have any questions, please contact me at (202) 245-6900 or Bryon.Gordon@ed.gov or Gary D. Whitman, Regional Inspector General for Audit, at (312) 730-1620 or Gary.Whitman@ed.gov.

Table of Contents

Results in Brief

What We Did

The objective of our audit was to determine whether Federal Student Aid (FSA) had established policies and procedures to mitigate the risk of servicers not servicing federally held student loans in accordance with Federal requirements. We assessed FSA's operations as of September 2017.

To answer the objective, we first gained an understanding of the five components of a system of internal control relevant to FSA's oversight of the servicing of federally held student loans.[1] We concluded that the control activities component of FSA's system of internal control was most relevant to our audit objective.[2] Next, we identified the control activities that FSA had established to mitigate the risk of servicers not servicing federally held student loans in accordance with Federal requirements. We then assessed the adequacy of the design of the following control activities that we determined had the greatest impact on the effectiveness of FSA's oversight:

- monitoring telephone calls between servicer representatives and borrowers and providing feedback about the monitoring to servicers,
- conducting reviews of servicers' compliance with requirements for servicing federally held student loans, and
- reviewing independent auditors' reports on audits of servicers' systems of internal control.[3]

Finally, we evaluated whether the policies and procedures provided reasonable assurance that the risk of servicers not servicing federally held student loans in accordance with Federal requirements was mitigated.

---

[1] "Standards for Internal Control in the Federal Government" (Government Accountability Office, September 2014) sets the internal control standards for Federal agencies. The standards are organized into five components—control environment, risk assessment, control activities, information and communication, and monitoring.

[2] Control activities are the actions management establishes through policies and procedures to achieve objectives and respond to risks.

[3] Audits of service organizations' systems of internal control completed by independent auditors following "Statement on Standards for Attestation Engagements," No. 18, issued by the American Institute of Certified Public Accountants.

What We Found

FSA had not established policies and procedures that provided reasonable assurance that the risk of servicer noncompliance with requirements for servicing federally held student loans was mitigated.

FSA's oversight activities regularly identified instances of servicers' not servicing federally held student loans in accordance with Federal requirements. From January 1, 2015, through September 30, 2017, 61 percent (210) of 343 reports on FSA's oversight activities disclosed instances of servicer noncompliance. FSA management routinely tracked the instances of noncompliance that servicers did not remediate before FSA issued a final review report. However, it did not track the identified instances of noncompliance that servicers remediated, even though FSA management could have used such information to identify patterns of noncompliance. FSA management also had not analyzed the information it did track to identify trends and recurring instances of noncompliance at each servicer and across all servicers.

FSA management rarely used available contract accountability provisions to hold servicers accountable for instances of noncompliance. It also did not incorporate a performance metric relevant to servicer compliance with Federal requirements into its methodology for assigning loans to servicers (see Finding 1).[4] By not holding servicers accountable for instances of noncompliance with Federal loan servicing requirements, FSA did not provide servicers with an incentive to take actions to mitigate the risk of continued servicer noncompliance that could harm students. Further, FSA's not holding servicers accountable could lead to servicers being paid more than they should be (the contracts with servicers allow FSA to recover amounts paid for loans not serviced in compliance with requirements).

Additionally, FSA employees did not always follow policy when evaluating the quality of servicer representatives' interactions with borrowers, and FSA did not provide reports of failed calls to servicers during a 10-month period, from June 2016 through March 2017 (see Finding 2). As a result, FSA management did not have reasonable assurance that servicers were complying with Federal loan servicing requirements when handling borrowers' inquiries, borrowers might not have been protected from poor services, and taxpayers might not have been protected from improper payments.

[4] FSA's contracts with the servicers allowed FSA to take certain actions, such as withholding payment or reducing loan volume, to hold servicers accountable when they failed to comply with Federal loan servicing requirements.

What We Recommend

We recommend that the Chief Operating Officer for FSA—

- track all instances of noncompliance identified during FSA oversight activities, regardless of whether servicers remediated the specific instances before FSA issues a final review report, and use the records to identify trends and recurring noncompliance for each servicer and across all servicers;
- use the contractual accountability provisions available, such as requiring the return of funds or reducing future loan volume, to hold servicers accountable for instances of noncompliance; and
- regularly share the results of any FSA loan servicing oversight activities with servicers.

FSA Comments

FSA provided written comments on the draft of this report on November 2, 2018. FSA neither agreed nor disagreed with the findings but agreed with all six recommendations. It did not comment on the overall conclusion presented in this report. On November 20, 2018, the Deputy Chief Operating Officer for FSA notified OIG that FSA would revise its comments on the draft audit report.

On December 7, 2018, FSA provided its revised written comments. FSA strongly disagreed with the overall conclusion that it did not establish policies and procedures that provided reasonable assurance that the risk of servicer noncompliance with Federal requirements was mitigated. FSA also stated that it already had or will implement all six recommendations and described improvements it has made to its oversight activities since September 2017.

FSA stated that the wording of Finding 1 implies a much broader risk than indicated by the examples included in the report. It also disagreed that FSA rarely held servicers accountable, stating that enforcement actions since September 2017 have resulted in about $2 million in recommended recoveries. FSA stated no disagreement with Finding 2.

We include the full text of FSA's revised comments in the FSA Comments section at the end of this report. We also summarize FSA's revised comments at the end of each finding.

OIG Response

Because the post-September 2017 improvements that FSA described in its comments did not occur during our audit period, we did not evaluate them and do not discuss

them in this report. However, as described, the improvements are aligned with the recommendations in this report. Other than providing further emphasis that we based our overall conclusion and findings on an assessment of FSA's control activities as of September 2017, we did not make any changes to the report based on FSA's comments.

We acknowledge that reasonable assurance of risk mitigation is a matter of management's risk appetite and risk tolerance. However, FSA's revised comments did not explain, and FSA did not provide any evidence showing, the level of noncompliance that is acceptable to FSA management or the level of noncompliance that would compel FSA to take enforcement actions against a servicer. Without such policies, employees conducting FSA's oversight activities cannot consistently know when it would be appropriate to recommend servicers take actions beyond correcting the specific instances of noncompliance identified by FSA's review teams.

Further, we do not agree that the risk of servicer noncompliance as described in Finding 1 is not broad. From January 1, 2015, through September 30, 2017, 61 percent (210) of 343 reports on FSA's oversight activities identified instances of servicer noncompliance with Federal loan servicing requirements. These reports disclosed noncompliance by all nine servicers and recurring instances of noncompliance by some servicers. These instances included noncompliance with requirements relevant to forbearances, deferments, income-driven repayment, interest rates, due diligence, and consumer protection. In most cases, FSA only required servicers to correct the accounts of borrowers affected by the noncompliance specifically identified by FSA.

In most cases before October 2017, FSA did not take actions stronger than correcting the accounts of those affected by FSA-identified noncompliance; rarely did FSA require the servicer to conduct a full file review. FSA also rarely penalized servicers for recurring noncompliance. In the 5 years that ended September 2017, FSA had required only three servicers to return about $181,000 to FSA for four instances of failure to service loans in compliance with Federal loan servicing requirements. Additionally, FSA's methodology for assigning new loans to servicers was not adjusted to take into account servicers' compliance with Federal loan servicing requirements. Therefore, servicers with more frequent instances of noncompliance experienced no reduction in the amount of new loans that FSA assigned to them. Although FSA stated that enforcement actions since September 2017 have resulted in about $2 million in recommended recoveries, the amount represents less than 0.12 percent of $1.7 billion that FSA budgeted for its loan servicing contracts in 2018 and 2019. While increased use of enforcement actions by FSA aligns with our recommendation, it will be important for FSA to track all instances of noncompliance and to assess the effect that its increased enforcement actions have on reducing noncompliance by the servicers.

Introduction

Background

The U.S. Department of Education (Department) is the nation's largest provider of student financial aid for education beyond high school. Within the Department, FSA is responsible for servicing all loans originated through the William D. Ford Federal Direct Loan (Direct Loan) Program and Federal Family Education Loan (FFEL) Program loans purchased from nonfederal entities.[5] As of September 30, 2017, the outstanding federally held student loan debt was more than $1.1 trillion.

Servicing Federally Held Student Loans

In 2009, FSA contracted with four servicers: (1) Great Lakes Educational Loan Services (Great Lakes); (2) Navient, LLC (Navient);[6] (3) Nelnet Servicing, LLC (Nelnet); and (4) Pennsylvania Higher Education Assistance Agency (PHEAA). From 2011 through 2013, FSA contracted with 11 more servicers: (1) Aspire Resources, Inc.; (2) College Foundation, Inc.; (3) Council for South Texas Economic Progress; (4) Educational Services of America, Inc. (EdFinancial Services); (5) Kentucky Higher Education Student Loan Corporation (Kentucky); (6) Missouri Higher Education Loan Authority (Missouri); (7) New Hampshire Higher Education Loan Corporation (New Hampshire); (8) Oklahoma Student Loan Authority (Oklahoma); (9) South Carolina Student Loan Corporation; (10) Utah Higher Education Assistance Authority (Utah); and (11) Vermont Student Assistance Corporation.[7] These 15 servicers have been responsible for collecting payments on federally held student loans that are not in a default status,[8] advising

[5] From September 2008 through September 2010, the Department purchased a portion of the outstanding FFEL program loans, as authorized under the Ensuring Continued Access to Student Loans Act of 2008 (Public Law 110-227). In this report, we refer to Direct Loan and the purchased FFEL loans as federally held student loans.

[6] In 2009, FSA contracted with SLM Corporation. In 2014, SLM Corporation split into two corporations; the second corporation—Navient, LLC—assumed the loan servicing responsibilities.

[7] As of September 2017, five of these 11 servicers (EdFinancial Services, Missouri, Oklahoma, New Hampshire, and Utah) were still servicing federally held student loans.

[8] A borrower who is more than 270 days delinquent in making payments is considered in a default status. However, FSA's policy is to not have the servicer transfer such loans to FSA's Default Management Collection System for assignment to a private collection agency until 360 days pass without payment being received.

borrowers on available resources to better manage their loan obligations, responding to borrowers' inquiries, and performing other administrative tasks associated with collecting and servicing federally held student loans on behalf of the Department.

The contracts with the servicers stated that: "The contractor(s) will be responsible for maintaining a full understanding of all federal and state laws and regulations and FSA requirements and ensuring that all aspects of the service continue to remain in compliance as changes occur." The contracts also specified certain activities that servicers were required to address through their policies and procedures. For example, all the contracts required servicers to report financial and other information to FSA and provide FSA access to their loan servicing information. Additionally, the contracts with Great Lakes, Navient, Nelnet, and PHEAA required the servicers to provide the Department with a copy of any lawsuit within 10 days of the complaint being served.

The contracts with the servicers also stated that FSA will assign loans based on the performance of each servicer in relation to the other servicers (as determined twice a year). Since September 2014, FSA has assigned new loans to servicers by calculating performance scores based on five attributes. The five attributes (and corresponding weights) for calculating servicer performance scores were as follows:

- satisfaction surveys of borrowers (35 percent),
- percentage of borrowers who were not more than 5 days delinquent (30 percent),
- percentage of borrowers who were more than 90 days but less than 271 days delinquent (15 percent),
- percentage of borrowers who were more than 270 days but less than 361 days delinquent (15 percent), and
- satisfaction survey of FSA employees who interacted with the servicers (5 percent).

As of September 30, 2017, FSA was responsible for about $1.147 trillion of federally held student loans. Of the $1.147 trillion, about $1.026 trillion was assigned to servicers,[9] of which $950 billion (93 percent) was assigned to four servicers—PHEAA ($319 billion), Great Lakes ($236 billion), Navient ($215 billion), and Nelnet ($180 billion). FSA had

[9] About $120 billion (10 percent) of the $1.147 trillion in outstanding federally held student loan debt was in default. Defaulted loans were assigned to private collection agencies, not to servicers.

assigned the remaining $76 billion (7 percent) to EdFinancial Services, Missouri, Oklahoma, New Hampshire, and Utah.

Ensuring Servicer's Compliance with Requirements

FSA is responsible for ensuring servicers comply with all requirements for servicing federally held student loans, including requirements relevant to income-driven repayment plans, forbearances and deferments of loan payments, consolidations of loans, and principal and interest payments. Among the many requirements with which they must adhere, servicers must

- correctly record the borrowers' interest rates and calculate the borrowers' balances;
- correctly apply payments to borrowers' accounts;
- properly grant forbearances and deferments to borrowers;
- appropriately capitalize loan interest;
- follow guidelines for delinquency notice letters, telephone calls, and skip tracing activities as they pertain to the collection of loans;
- properly process borrowers' applications for income-driven repayment plans;
- correctly calculate borrowers' monthly payments under income-driven repayment plans; and
- maintain complete and accurate records to support borrower's repayment plans.

See Appendix C for a list of significant Federal laws and regulations with which servicers must comply.

Employees from three FSA offices—Business Operations, Program Compliance, and Finance—performed oversight activities that FSA management established to provide reasonable assurance that servicers complied with the requirements for servicing federally held student loans. These procedures included

- listening to recorded telephone interactions between servicer representatives and borrowers,
- conducting reviews of servicers' compliance with loan servicing requirements,
- reviewing independent auditors' reports on audits of servicers' systems of internal control,

- meeting with servicers, and
- conducting surveys of borrowers and FSA employees.

For a description of these oversight activities , see Appendix B.

Finding 1. FSA Did Not Track All Identified Instances of Noncompliance and Rarely Held Servicers Accountable for Noncompliance with Requirements

FSA

- did not track all instances of noncompliance that FSA identified during its oversight activities,
- did not analyze the records relevant to identified instances of noncompliance to identify trends and recurring noncompliance for each servicer and across all servicers,
- rarely used available contract accountability provisions to hold servicers accountable for instances of noncompliance, and
- did not incorporate a performance metric relevant to servicer compliance with Federal requirements into its methodology for assigning loans to servicers.

As a result, borrowers might not have received the most favorable repayment terms available to them, and servicers might have been paid more than they should have been under their contracts.

FSA Did Not Track All Information Necessary to Identify Trends in Servicer Noncompliance with Federal Requirements

FSA used a database to track instances of servicer noncompliance with Federal loan servicing requirements. The database included instances of servicer noncompliance that required further action to be taken by either the servicer or FSA.

However, the database did not include instances of noncompliance that FSA identified during its review but considered the actions that the servicer proposed to be sufficient to remedy the specific instance of noncompliance. For example, an April 2017 report on a servicer liaison team review of EdFinancial Services' inbound and outbound calls disclosed that servicer representatives did not always provide interest capitalization information to borrowers. EdFinancial Services agreed to take the action as recommended by FSA; therefore, according to FSA's practice, the instances of noncompliance were not recorded in FSA's database.

In addition to the information in the database being incomplete, FSA management was not using the information it did have to identify trends and recurring noncompliance for each servicer and across all servicers. Instead, FSA relied on the memories of the

employees responsible for the oversight activities to recognize recurring instances of noncompliance.

We concluded that FSA had the information needed to identify recurring instances of and trends in noncompliance. We analyzed all 343 monitoring reports that FSA completed from January 1, 2015, through September 30, 2017. The 343 reports included those on FSA's monitoring of calls between servicer representatives and borrowers (73 reports), reviews of servicers' compliance with Federal requirements (210 reports), and reviews of independent auditors' reports on audits of servicers' systems of internal control (60 reports).[10] About 61 percent (210) of these reports disclosed instances of servicer noncompliance with various areas of Federal loan servicing requirements. These instances included noncompliance with requirements relevant to forbearances, deferments, income-driven repayment, interest rates, due diligence, and consumer protection. The reports disclosed recurring instances of noncompliance primarily in two areas: consumer protection (servicer representatives not informing borrowers of the available repayment options) and income-driven repayment (servicers incorrectly calculating income-driven payment amounts). The reports also disclosed that the noncompliance rates at some servicers were significantly higher than the average noncompliance rate of all servicers.

Servicer Representatives Not Sufficiently Informing Borrowers of Available Repayment Options

When a servicer is notified that a borrower is having difficulty making payments, the servicer is required to provide the borrower with information about her or his options for avoiding default status.[11] The servicer must explain the repayment plans available to the borrower. The servicer also must explain how the borrower may request a change in her or his repayment plan, provide the borrower with a description of the requirements for obtaining forbearance on the loan and any costs associated with forbearance, and provide the borrower with a description of the options available to avoid default and any fees or costs associated with those options. From January 2015 through September 2017, monthly reports on FSA's monitoring activities disclosed recurring instances at all servicers of servicer representatives not sufficiently informing borrowers about available repayment options.

[10] For a description of these control activities, see Appendix B.

[11] Title 34, Code of Federal Regulations (C.F.R.), § 682.205(a)(4). Where there was no comparable Direct Loan regulation, the FFEL program regulation was effective.

Monthly, FSA listened to a sample of recorded telephone calls between servicer representatives from all nine servicers and borrowers. For each call, FSA call monitors completed a scoresheet. FSA failed all calls receiving a score under FSA's established standard.[12] From January 2015 through September 2017, FSA provided 73 monthly reports on individual servicers. Nearly 92 percent (67) of the monthly reports included at least 1 instance of the servicer representative not sufficiently informing borrowers about available repayment options. For the April 2017 reports, FSA listened to 4,440 telephone calls. The monthly reports showed that FSA failed 193 calls (4.3 percent of the 4,440 calls). Of those failed calls, FSA failed 26 percent (50 calls) because the servicer representatives did not provide the borrowers with sufficient information about the repayment options available to them. The failed-call rates for two servicers (Utah, 8.9 percent, and PHEAA, 10.6 percent) were significantly higher than the 4.3 percent average failed-call rate for all servicers (see Table 1).

Table 1. April 2017 Calls That FSA Monitored and Failed

Servicer	Number of Calls Evaluated	Number of Calls That Failed	Percentage of Calls That Failed	Number Failed Because Borrower Not Provided Sufficient Information
Utah	158	14	8.9	2
EdFinancial Services	492	15	3.0	4
PHEAA	997	106	10.6	25
New Hampshire	261	3	1.1	2
Great Lakes	206	3	1.5	3
Missouri	568	29	5.1	9
Navient	834	6	0.7	2
Nelnet	466	7	1.5	2
Oklahoma	458	10	2.2	1
Total	4,440	193	4.3	50

[12] See Appendix B. FSA's Oversight Activities, Call Monitoring Team Reviews.

For the May 2017 reports on FSA's call monitoring, FSA listened to 6,070 telephone calls between servicer representatives from all 9 servicers and borrowers. The monthly reports showed that FSA failed 151 calls (2.5 percent of the 6,070 calls). Of those failed calls, FSA failed 20 percent (30 calls) because the servicer representatives did not provide the borrowers with sufficient information about the repayment options available to them. The failed-call rates for two servicers (Missouri, 4.9 percent, and PHEAA, 8.8 percent) were significantly higher than the 2.5 percent average failed-call rate for all servicers (see Table 2).

Table 2. May 2017 Calls That FSA Monitored and Failed

Servicer	Number of Calls Evaluated	Number of Calls Failed	Percentage of Calls Failed	Number Failed Because Borrower Was Not Provided Sufficient Information
Utah	735	11	1.5	1
EdFinancial Services	481	4	0.8	0
PHEAA	853	75	8.8	8
New Hampshire	488	5	1.0	1
Great Lakes	369	11	3.0	7
Missouri	699	34	4.9	9
Navient	1,112	3	0.3	0
Nelnet	871	6	0.7	4
Oklahoma	462	2	0.4	0
Total	6,070	151	2.5	30

From January 2015 through September 2017, FSA issued 5 other reports (4 on reviews conducted by the servicer liaison team and 1 on a review conducted by Financial Institution Oversight Service) that covered the area of consumer protection.[13] Of the

[13] During this period, FSA issued 33 reports on reviews conducted by the servicer liaison team and 25 reports on reviews conducted by Financial Institution Oversight Service.

five reports, three identified instances of servicer representatives not sufficiently informing borrowers about available repayment options.

The April 2017 report on a servicer liaison team review of EdFinancial Services' inbound and outbound calls disclosed that servicer representatives did not always provide interest capitalization information to borrowers. The servicer representatives provided interest capitalization information when discussing a forbearance or deferment but not when discussing different repayment plans.

The May 2017 report on a servicer liaison team review of Navient's call center disclosed that servicer representatives did not offer alternative or potentially beneficial options when attempting to assist borrowers with bringing their account current or managing repayment. Instead, Navient representatives placed the borrowers' accounts into forbearance statuses.[14] For this review, FSA listened to 2,388 calls and determined that, for 220 calls (9.2 percent), servicer representatives did not provide the borrowers with all of their available repayment options. Navient offered only forbearance as an option during all 220 calls. The 9.2 percent rate of noncompliance was significantly higher than the 0.3 percent rate disclosed in FSA's failed-call report for the same month.

The May 2017 report on a review conducted by Financial Institution Oversight Service disclosed that PHEAA representatives placed borrowers' accounts into forbearance statuses to resolve delinquencies without discussing all available options with the borrowers. For this review, FSA listened to 99 borrower calls. It determined that, for 24 (24.2 percent) of the 99 calls, servicer representatives did not provide the borrowers with sufficient information regarding their available options. PHEAA granted forbearances to 17 borrowers when they might have benefitted from a different option, such as possible deferment or income-driven repayment. PHEAA either provided the other seven borrowers with inaccurate information regarding their options or did not follow internal procedures regarding the order of delinquency resolution options. The 24.2 percent rate of noncompliance was additional evidence (to the 8.8 percent rate disclosed in the failed-call report for the same month) of a pattern of noncompliance at PHEAA.

Income-Driven Payment Amounts Not Correctly Calculated

Income-driven repayment plans set a borrower's monthly payment at an amount that is intended to be affordable based on the borrower's income and family size. Any errors in

[14] Forbearance status results in a temporary cessation of the borrower's required payment, providing the borrower an extension of time for making payments or to temporarily make smaller payments than previously scheduled. However, interest continues to accrue on the borrower's account.

the calculation of the affordable payment amounts could negatively affect borrowers or taxpayers. From January 2015 through September 2017, reports on FSA's monitoring activities (Financial Institution Oversight Service reviews, process monitoring team reviews, servicer liaison reviews, and reviews of audit reports on servicers' systems of internal control) disclosed recurring instances of servicers not correctly calculating borrowers' monthly payment amounts under income-driven repayment plans. FSA identified such noncompliance at seven servicers—at four more than once.

From January 2015 through September 2017, FSA issued 25 reports on reviews conducted by Financial Institution Oversight Service, 152 reports on reviews conducted by the process monitoring team, and 33 reports on reviews conducted by the servicer liaison team. These 210 reports disclosed the following:

- Twenty-two of the 25 Financial Institution Oversight Service reviews covered the calculation of income-driven repayment amounts. Five (23 percent) of those 22 reviews disclosed instances of servicers not correctly calculating borrowers' repayment amounts.

- Ten of the 152 process monitoring team reviews covered the calculation of income-driven repayment amounts. Two (20 percent) of the 10 reviews disclosed instances of servicers not correctly calculating borrowers' repayment amounts.

- Nine of the 33 servicer liaison team reviews covered the calculation of income-driven repayment amounts. Six (67 percent) of the 9 reviews disclosed instances of servicers not correctly calculating borrowers' repayment amounts.

In total, 13 (32 percent) of the 41 reports on FSA reviews that covered the calculation of income-driven repayment amounts disclosed instances of servicers not correctly calculating borrowers' repayment amounts.

In addition to its own reviews, FSA reviewed independent auditors' reports on audits of servicers' systems of internal control, tracked the instances of noncompliance disclosed in those reports, and considered the noncompliance during planning for FSA's following year's compliance review work. Reports on 60 audits of servicers' systems of internal control that FSA reviewed from January 1, 2015, through September 30, 2017, disclosed that 1 servicer did not correctly calculate the income-driven monthly payment amounts during 2 consecutive audit periods. The report on the Utah audit covering July 1, 2016, through December 31, 2016, disclosed that Utah incorrectly calculated the payment amounts for 2 of 45 borrower accounts. The report on the Utah audit covering January 1, 2017, through June 30, 2017, disclosed that Utah incorrectly calculated the payment amounts for 6 of 45 borrower accounts.

Contractual Accountability Provisions Rarely Used

FSA provided us with evidence of only four instances, affecting three servicers, in the past 5 years in which it required a servicer to return funds to the Federal government for failure to service loans in compliance with Federal requirements. In 2013, FSA reduced payments to Great Lakes by $99,836 because the servicer improperly billed FSA for borrower accounts placed in administrative forbearance. Great Lakes automatically placed delinquent accounts in administrative forbearance, which did not comply with the forbearance requirements. In 2017, FSA reduced payments to Great Lakes by $1,260, New Hampshire by $37,438, and Oklahoma by $42,550 because the three servicers did not comply with the requirements of an interest rate reduction program. FSA has not adjusted the number of new loans assigned to a servicer or transferred a noncompliant servicer's current loan volume to another servicer because of a servicer's noncompliance with Federal loan servicing requirements.

FSA's contracts with all servicers state that the servicers are required to follow all applicable Federal laws and regulations, or they will be required to return any fees that they billed to the Department from the time of noncompliance. The "Invoicing and Non-Compliance" section of every servicer's contract states the following:

> Borrowers whose loans are not being serviced in compliance with the Requirements, Policy and Procedures for servicing federally held debt due to the fault of the servicer (i.e. correct interest calculations, correct balances, interest determination and calculations, notices sent properly, proper due diligence, etc.), will not be billable to the Government from the initial point of non-compliance. Any funds that have been invoiced for these borrowers and paid shall be returned to the Government via a credit on the next invoice.

According to the contracts, servicers are responsible for all supplies, services, and other costs to service borrower accounts. This includes costs for bringing contractor systems into compliance for handling federally held debt and costs for legislative, regulatory, or policy changes that affect the servicing of borrower accounts. For all other costs, the Department and the servicer may come to an agreement via change order process or negotiation, as necessary.

All contracts also allowed FSA to penalize the servicers for noncompliance by reallocating new loan volume to other servicers or transferring all or part of the noncompliant servicer's current loan volume to another servicer until the noncompliant servicer comes back into compliance. Servicers bill the Department for each individual borrower account serviced. The billing amount is based on the number of borrower accounts serviced (a set amount per account) and the status of each borrower account.

The contracts include a pricing structure for in-school, grace or repayment, deferment or forbearance, and delinquent borrower account statuses.

As of September 2017, FSA's methodology for assigning new loans to servicers did not take into account servicers' compliance with Federal loan servicing requirements or FSA's requirements for servicer representatives' interactions with borrowers. Servicers with more instances of noncompliance experienced no reduction in the amount of new loans that FSA assigned to them, even though some borrowers might be experiencing poor service. All contracts required FSA to assign loans based on the performance of each servicer in relation to each of the other servicers (as determined two times a year). Since September 2014, FSA has assigned new loans to servicers by calculating servicer performance scores based on the following five attributes and weights:

- satisfaction surveys of borrowers (35 percent),
- percentage of borrowers who were not more than 5 days delinquent (30 percent),
- percentage of borrowers who were more than 90 days but less than 271 days delinquent (15 percent),
- percentage of borrowers who were more than 270 days but less than 361 days delinquent (15 percent), and
- satisfaction survey of FSA employees who interacted with the servicers (5 percent).

None of the contracts allowed FSA to establish performance metrics relevant to each servicer's compliance with loan servicing requirements and evaluate individual servicer's performance against such performance metrics.

Agencies Should Evaluate and Modify Control Activities

"Standards for Internal Control in the Federal Government" states that management should design appropriate types of control activities to address risks, including those risks relevant to service organizations. The standards also state that management retains responsibility for monitoring the effectiveness of internal control over the assigned processes performed by service organizations and should hold service organizations accountable for their assigned internal control responsibilities. When issues are identified, management should evaluate them to determine whether any of the issues rise to the level of an internal control deficiency. Management should consider whether current controls address the identified issues and modify controls, if necessary. Management should also determine appropriate corrective actions and oversee remediation of deficiencies.

In addition to the standards for internal control, FSA's own strategic plan emphasizes that FSA's control activities should focus on ensuring that servicers fulfill their responsibilities. FSA's strategic plan for fiscal years 2015–2019 included a strategic goal to "Proactively manage the student aid portfolio to mitigate risk." One of FSA's objectives for this goal stated: "This will include the implementation of processes, tools, and methods that serve to protect the interests of students, and support FSA in making service providers accountable." The objective further stated that FSA would "ensure that its processes for resolving student issues are simple for customers to use and sophisticated enough to capture insights that can be used to refine student aid operations."

The Harm of Not Holding Servicers Accountable for Compliance with Federal Requirements

In its 2007 report on proposed amendments to the Higher Education Act, the Senate Committee on Health, Education, Labor, and Pensions stated: "[t]he committee believes strongly that lenders, guaranty agencies and institutions of higher education must act with honesty and integrity at all times to ensure that the financial aid programs under title IV serve the best interests of students." In its December 2007 report on the Higher Education Opportunity Act of 2008, the House of Representatives Committee on Education and Labor stated: "[t]he nation's financial aid system exists for a single purpose: to serve students and their families."

By rarely holding servicers accountable for instances of noncompliance with Federal loan servicing requirements, FSA is not providing servicers with incentive to take actions to mitigate the risk of continued noncompliance that harms students and their families. Failure by servicers to take appropriate corrective actions could lead to borrowers not receiving the most favorable repayment terms that should have been available to them. Additionally, FSA's not holding servicers accountable could lead to servicers being paid more than they should be (the contracts with servicers allow FSA to recover amounts paid for loans not serviced in compliance with requirements).

By not holding servicers accountable, FSA could give its servicers the impression that it is not concerned with servicer noncompliance with Federal loan servicing requirements, including protecting borrowers' rights.

Recommendations

We recommend that the Chief Operating Officer for FSA—

1.1 Track all instances of noncompliance identified during FSA reviews, regardless of whether the specific instances were corrected and did not require further action to be taken by either the servicer or FSA.

1.2 Analyze the records relevant to noncompliance, identify trends and recurring noncompliance for each servicer and across all servicers, and use the information as a basis for assessing servicer performance.

1.3 Use the contractual accountability provisions available, such as requiring the return of funds or reducing future loan volume, to hold servicers accountable for instances of noncompliance.

FSA Comments

FSA disagreed with certain aspects of the finding (see FSA Comments). FSA stated that the wording of the finding implies a much broader risk than indicated by the examples described. According to FSA, it devotes significant resources to its servicer oversight and monitoring efforts. FSA and third parties, including the OIG, conduct regular audits of servicers' internal control processes. Neither Finding 1 nor these oversight activities have identified material instances of servicer noncompliance. FSA also disagreed that it rarely held servicers accountable for identified instances of noncompliance, stating that, since September 2017, it has required servicers to return more than $2 million for noncompliance.

FSA also provided its explanation regarding the servicer liaison team review of Navient's call center (see page 13 of this report). FSA stated that the review was part of a larger review initiated by FSA in response to a lawsuit filed against Navient by the Consumer Financial Protection Bureau. FSA stated that the review only targeted short-duration calls because those would most likely include improper use of forbearances. According to FSA, the review team concluded that Navient was not improperly steering borrowers into forbearance, and nothing in the review report indicated that Navient improperly applied forbearances. FSA further stated that the review supports a conclusion that Navient followed standard practice and acted consistent with the requirements of its contract.

Finally, FSA stated that it has made improvements to its oversight and monitoring policies and procedures since the end of the audit period (September 2017). According to FSA, some of the improvements align with the recommendations of this report. FSA asked that we revise the report to reflect these improvements.

OIG Response

We did not revise the finding based on FSA's comments. We agree that FSA devotes significant resources to its oversight activities. However, we disagree with FSA's statement that the risk of servicer noncompliance is not broad. As stated in this finding, from January 1, 2015, through September 30, 2017, 61 percent (210) of 343 reports on FSA's servicer oversight activities identified instances of servicer noncompliance with Federal loan servicing requirements. These reports disclosed noncompliance by all nine servicers and recurring instances of noncompliance by some servicers. These instances included failure to comply with requirements relevant to forbearances, deferments, income-driven repayment, interest rates, due diligence, and consumer protection. FSA usually concluded that the error rate was low (1, 2, or 3 instances of noncompliance in a sample of about 30 borrower accounts) and did not expand its samples of borrower accounts or require the servicer to conduct a review to determine the extent of the noncompliance. Instead, FSA only required the servicer to correct the borrower accounts that FSA identified as in error.

However, the noncompliance that FSA has repeatedly identified could affect a much larger population of borrowers than those specifically identified by FSA's reviews of samples of borrower accounts. Those risks include increased interest or repayment costs incurred by borrowers, the missed opportunity for more borrowers to take advantage of certain repayment programs, negative effects on borrowers' credit ratings, and an increased likelihood of delinquency or even default.

Our audit evaluated FSA's control activities as of September 2017, and we found that FSA's control activities disclosed instances of noncompliance across all servicers and recurring instances of noncompliance at some servicers. Those results suggest that a more concerted effort to enforce accountability on the part of servicers is necessary. The approximately $2 million in recommended recoveries since September 2017 that FSA described in its comments represents a significant increase in recommended recoveries during the 5 years ended September 2017. However, $2 million represents less than 0.12 percent of the approximately $1.7 billion that FSA budgeted for loan servicing contracts in fiscal years 2018 and 2019. While increased use of enforcement actions by FSA aligns with our recommendation, it will be important for FSA to track all instances of noncompliance and to assess the effect that its increased enforcement actions have on reducing noncompliance by the servicers.

FSA's explanation of its conclusions regarding the Navient review did not cause us to change our discussion of FSA's May 2017 review report. The report did not state that Navient improperly or properly steered borrowers into forbearance. Instead, the report stated that Navient used forbearances instead of sufficiently informing borrowers about available repayment options. FSA's review report stated:

> For 220 of the calls, Navient [Customer Service Representatives] neglected to offer the borrower an option other than forbearance. . . While this isn't a contractual requirement, these borrowers were not given the opportunity to decide if another option (like one of the Income Driven plans or a deferment) would have been more favorable. And in some instances, interest was capitalized when another option may have prevented it.

FSA's comments do not change the finding of the May 2017 report that Navient did not always notify borrowers of their repayment options. The report's finding could still have been used to identify noncompliance rates at one servicer that were higher than the average noncompliance rate of all servicers.

Because the post-September 2017 improvements that FSA described in its comments did not occur during our audit period, we did not evaluate them and do not discuss them in this report. However, the described improvements are aligned with the recommendations for Finding 1.

Finding 2. Information Necessary to Ensure Servicer Compliance Not Always Complete

The information that FSA collected and FSA's communications with servicers were not always sufficient to ensure servicers complied with requirements for servicing federally held student loans. We found that FSA did not ensure that the call monitoring team completed scoresheets for all calls that it monitored. As a result, FSA's call monitoring database could not generate a score for more than 8 percent of the calls that FSA monitored from March 2017 through May 2017, and FSA management was unable to determine whether the servicers complied with FSA's established standards for interaction with borrowers. We also found that FSA's call monitoring team did not provide failed-call reports to servicers for a 10-month period, from June 2016 through March 2017. As a result, servicers were not receiving feedback about their telephone interactions with borrowers.

FSA Did Not Always Collect Information Necessary to Evaluate Servicer Interactions with Borrowers

We found that FSA employees did not always follow policy and complete a scoresheet for every monitored call. FSA used these scoresheets to assess the quality of customer service provided by servicers and to determine whether the servicers were complying with FSA's established standards for handling borrowers' inquiries. FSA provided us with a list of 10,237 inbound calls that it monitored for the months of March, April, and May 2017. Of those 10,237 calls, 838 (8.2 percent) did not have a system-generated score.

According to FSA policy ("Call Center Monitoring – Improved Process for Call Entry"), call monitors must complete a scoresheet for each monitored call. The scoresheet contained 2 sections and had a possible overall score of 100 points. The first section was worth 25 points and evaluated the servicer representatives' introduction and greeting of the borrower, verification of the borrower's identity and contact information, and overall professionalism. The second section was worth 75 points and evaluated the method of resolution used by the servicer representative to address the borrower's concerns. To score the second section, the call monitor first selected the method of resolution from a list and the scoresheet was automatically populated with metrics for that method. The call monitor then answered the questions applicable to the call. One of the options that the call monitor could select was a miscellaneous option ("Unknown/Misc/Other"). This option did not have any metrics associated with it. Instead, the call monitor could only select "Yes" or "No" to indicate whether the servicer representative properly addressed the borrower's concerns. However, we found that call monitors did not always follow procedures and make a "Yes" or "No" selection, and the call monitoring database did not automatically reject incomplete scoresheets.

FSA management was not aware that call monitors did not follow policy because, in part, it had not implemented a quality control process. In addition, FSA management did not design the call monitoring database to reject scoresheets that could not be scored.

After we raised our concerns about the completeness of its call monitoring data, FSA management acknowledged that the call monitoring database was not capturing enough information to score all monitored calls. FSA management also informed us that, as of November 2017, it had implemented a quality control process to evaluate about 4 percent of each call monitor's scoresheets each month. Further, FSA management informed us that it ordered system programming changes. The changes are intended to ensure that all fields in a scoresheet are fully populated when the monitor submits it or the scoresheet will be rejected and the call monitor will be prompted to complete the blank fields and resubmit it. We have not verified whether FSA has implemented these corrective actions.

FSA Did Not Provide Servicers with Feedback about Failed Calls During a 10-Month Period

From June 2016 through March 2017, FSA did not communicate the results of its call monitoring to servicers. Providing reports of failed calls to servicers was an oversight activity that FSA used to give servicers feedback about servicer representatives' interactions with borrowers. FSA did not provide the reports because it was revising the report format. However, without this feedback, servicers were unaware of whether their call operations were meeting FSA's expectations and whether they needed to correct potential deficiencies in their call operations.

Agencies Should Design Processes to Identify and Communicate Quality Information

"Standards for Internal Control in the Federal Government" states that management should design appropriate types of control activities for the entity's internal control system. These include reviews by management at the functional or activity level and controls over information processing, such as edit checks of the data entered and comparing file totals with control accounts. Management also should design a process to identify the information needed to address risks, obtain relevant data in a timely manner so the data can be used for effective monitoring, and process the data it obtains into quality information that supports the internal control system. Quality information means information that is appropriate, current, complete, accurate, accessible, and timely provided. Management should communicate that quality information to the necessary external parties so that external parties can help the entity achieve its objectives and address related risks.

Without complete call monitoring data, FSA management did not have reasonable assurance that servicers were complying with Federal loan servicing requirements when handling borrowers' inquiries. When FSA does not identify and communicate noncompliance by servicers, borrowers are not protected from poor services and taxpayers are not protected from improper payments.

FSA stated that it did not provide servicers with reports of failed calls from June 2016 through March 2017 because it was revising the report. According to FSA, the revised report improved the information provided to servicers by including detailed information by category of failed calls. The revised report took months to create because it needed to be acceptable to FSA and all parties involved. While the report was being revised, FSA still could have shared the results of any oversight activities with servicers.

Recommendations

We recommend that the Chief Operating Officer for FSA—

2.1 Verify that programming corrections ensure the system prompts call monitors to complete all necessary data fields before submitting scoresheets.

2.2 Ensure that FSA management has implemented its new quality control process and is evaluating a management-determined percentage of each call monitor's completed work each month.

2.3 Regularly share the results of any oversight activities with servicers, regardless of whether management is making changes to existing processes.

FSA Comments

FSA neither agreed nor disagreed with the finding but agreed with all three recommendations (see FSA Comments). FSA stated that it implemented a new database on June 14, 2018. The new database requires completion of all data fields before a call monitoring submission will be accepted. FSA also stated that it has implemented a quality control measure for the call monitoring team. Each day, a quality control analyst will review from 10 to 14 of the calls between borrowers and servicers that FSA monitors. The review will include the monitoring conducted by each call monitoring team member. Finally, FSA stated that it resumed providing all servicers with the results of FSA's call monitoring activities as of April 2017.

OIG Response

Because the improvements that FSA described did not all occur during our audit period, we did not confirm that the improvements were operating as FSA management intended. However, as described, the improvements are aligned with the recommendations for Finding 2.

Appendix A. Scope and Methodology

We evaluated FSA's system of internal control over loan servicing as of September 2017. We obtained and reviewed information relevant to FSA, the servicers with whom FSA had contracted, the terms of the contracts between FSA and the servicers, and prior reports relevant to FSA's oversight of the servicers. The information included the following:

- data covering the portfolio of federally held student loans;
- FSA's annual report for fiscal years 2015, 2016, and 2017 and strategic plan for fiscal years 2015–2019;
- contracts between FSA and Aspire Resources, Inc.; College Foundation, Inc.; Council for South Texas Economic Progress; EdFinancial Services; Great Lakes; Kentucky; Missouri; Navient; Nelnet; New Hampshire; Oklahoma; PHEAA; South Carolina Student Loan Corporation; Utah; and Vermont Student Assistance Corporation;
- two Office of Inspector General reports relevant to FSA's oversight of loan servicing—"Federal Student Aid's Award and Administration of the Title IV Additional Servicers Contracts" (A02L0006) and "The U.S. Department of Education's Administration of Student Loan Debt and Repayment" (A09N0011);
- three Government Accountability Office (GAO) reports relevant to FSA's oversight of loan servicing—"Federal Student Loans: Better Oversight Could Improve Defaulted Loan Rehabilitation" (GAO-14-256); "Federal Student Loans: Education Could Do More to Help Ensure Borrowers Are Aware of Repayment and Forgiveness Options" (GAO-15-663); and "Federal Student Loans: Education Could Improve Direct Loan Program Customer Service and Oversight" (GAO-16-523);
- the transcript of one GAO congressional testimony relevant to FSA's oversight of loan servicing—"Federal Student Loans: Key Weaknesses Limit Education's Management of Contractors" (GAO-16-196T);
- three Consumer Financial Protection Bureau reports relevant to loan servicing—"Student loan servicing: Analysis of public input and recommendations for reform" (September 2015); "Annual report of the Consumer Financial Protection Bureau Student Loan Ombudsman: Transitioning from default to an income-driven repayment plan" (October 2016); and "Staying on track while giving back: The cost of student loan servicing breakdowns for people serving their communities" (June 2017); and

- independent auditors' reports on audits of nine servicers' systems of internal control covering July 1, 2015, through December 31, 2015, and one servicer's systems of internal control covering January 1, 2015, through December 31, 2015.

We then gained an understanding of the system of internal control relevant to FSA's oversight of servicers. After gaining that understanding, we concluded that the control activities component of internal control was the most significant to our audit objective and assessed the adequacy of the three most significant activities FSA used to oversee the servicers: (1) reviewing servicer's compliance with Federal loan servicing requirements, (2) listening to recorded telephone calls between servicer representatives and borrowers, and (3) reviewing independent auditors' reports on audits of servicers' systems of internal control.

Understanding of FSA's System of Internal Control

Standards for internal control are organized into five components (control environment, risk assessment, control activities, information and communication, and monitoring). The five components apply to employees at all organizational levels (entity, division, operating unit, and function) and to all categories of objectives (operations, reporting, and compliance). To gain an understanding of the five components of FSA's system of internal control over loan servicing, we identified and interviewed FSA managers and employees from the office of the Chief Operating Officer, Finance, Program Compliance, Customer Experience, Acquisitions, Risk Management, and Business Operations who were responsible for the oversight of loan servicing. In total, we interviewed 26 managers and 34 employees. We also reviewed the following:

- FSA's organization charts and a list of employees involved with the oversight of servicers;

- documents describing the elements covered by Financial Institution Oversight Service reviews during fiscal years 2016 and 2017, and Financial Institution Oversight Service's "FY 2016 Review Program Methodology" and "FY 2017 Review Program Methodology," which established the policies and procedures employees were supposed to follow when conducting Financial Institution Oversight Service reviews during fiscal years 2016 and 2017;

- "Process Monitoring Team Policy and Procedural Manual," which established the policies and procedures employees should follow when performing process monitoring team reviews of servicers;

- call monitoring standards, which established the scoring methodology used to determine whether calls passed or failed;

- "Site Visit Review Procedures Guide," which established the policies and procedures employees were to follow when conducting servicer liaison reviews of a servicer;

- FSA's "OMB [Office of Management and Budget] Circular A-123, Appendix A FY16 Implementation Plan;"

- the A-123 assessment of FSA's system of internal control for fiscal year 2016 and the A-123 assessment of FSA's servicer oversight activities for fiscal year 2016;

- "Explanation of Allocation and Performance Measure Methodology," which describes the methodology FSA used to assign new borrower accounts to servicers and the performance measures included in the allocation methodology;

- examples of meeting notes from internal FSA meetings relevant to overseeing servicers and FSA meetings with servicers;

- flowchart of the process FSA used to revise the requirements that servicers' need to follow;

- examples of change requests that FSA issued to revise the requirements that servicers must follow; and

- Financial Institution Oversight Service, process monitoring, and servicer liaison review reports, call monitoring failed-call reports, and reports on audits of servicers' systems of internal control.

After gaining an understanding of the five components of FSA's system of internal control over loan servicing, we concluded that control activities was the component most significant to our audit objective.

Assessing the Adequacy of Control Activities

To assess the adequacy of FSA's control activities, we first identified the following processes that we considered having the most significant impact on the effectiveness of FSA's oversight of loan servicers:

- listening to recorded telephone calls between servicer representatives and borrowers;

- reviewing servicer's compliance with Federal loan servicing requirements, completed by process monitoring teams, servicer liaison teams, and Financial Institution Oversight Service; and

- reviewing reports on audits, completed by independent auditors, of servicers' systems of internal control.

We then determined whether these processes were operating as FSA management intended and whether these processes were likely to mitigate the risk of servicer noncompliance with Federal loan servicing requirements.[15]

To determine whether a particular process was operating as intended, we reviewed records showing FSA's implementation of the process.

- *Listening to recorded telephone calls between servicer representatives and borrowers.* During March, April, and May 2017, FSA monitored 10,237 calls that borrowers made to the 9 servicers.[16] We grouped the 10,237 inbound calls by servicer. We then randomly selected 45 calls and judgmentally selected 1 additional recorded call for each servicer. Using the same system and audio files that FSA employees used, we listened to each selected recording. Following FSA's processes and using FSA's scoring rubric, we calculated a score for each call. We then compared our score with FSA's scoring records.

- *Reviewing servicer's compliance with loan servicing requirements.* We reviewed 6 of 27 process monitoring team review reports that FSA issued from June 1, 2016, through May 31, 2017. We selected the reports on reviews of the four largest servicers (Great Lakes, Nelnet, Navient, and PHEAA) and the reports on reviews of two of the five other servicers to ensure that our evaluation helped us ensure that FSA consistently implemented its activities regardless of the type of servicer. We also reviewed 5 of 13 servicer liaison team review reports that FSA issued from June 1, 2016, through May 31, 2017, ensuring that we selected recent reviews, reviews of different servicers, and reviews that covered different topics. In addition, we reviewed all nine Financial Institution Oversight Service review reports that FSA issued from July 11, 2016, through June 27, 2017. We reviewed the records that FSA employees created to show the work performed and conclusions reached about the servicer's compliance with the requirements within the scope of each review. We compared FSA's

[15] FSA designed and implemented other processes, such as regular meetings with servicers and satisfaction surveys of borrowers and FSA employees. However, we did not evaluate the effectiveness of these other processes because we did not consider them as significant as the three that we evaluated.

[16] At the time we were conducting our audit, these were the most recent months for which FSA had completed its monitoring.

reports and records of the review processes to the documents describing FSA's processes and the processes explained to us during interviews.

- *Reviewing reports on servicers' systems of internal control*. We reviewed the most recent reports on audits of all nine servicers' systems of internal control.[17] We then reviewed the records that FSA's reviewers created to show whether the audits tested all required control activities. We compared FSA's records to the documents describing FSA's processes and the processes explained to us during interviews.

We also reviewed the instances of noncompliance that FSA identified through its oversight activities and how FSA addressed those instances of noncompliance. We obtained and reviewed all call monitoring reports of failed calls; all reports on process monitoring team, servicer liaison team, and Financial Institution Oversight Service reviews; and all independent auditors' reports on audits of servicers' systems of internal control that FSA issued or reviewed from January 1, 2015, through September 30, 2017. We then categorized all of the instances of noncompliance identified in those reports into groups based on the general subject area of the noncompliance. Next, we listed the noncompliance subject areas that occurred more than once. For noncompliance that occurred more than once, we assessed FSA's recommended actions and the servicer's proposed actions to determine whether the actions taken would likely mitigate the risk of similar instances of noncompliance occurring.

Use of Computer-Processed Data

We relied, in part, on inbound call monitoring data that FSA retained for the months of March, April, and May 2017. We analyzed the data to ensure that all fields included the correct type of information (for example, the date fields included only dates) and no fields were blank. Based on our analysis, we concluded that the computer-processed data were sufficiently reliable for the purposes of our audit.[18]

We also used data on federally held student loans that we obtained from FSA's website. We used this data to identify the volume of loans serviced by FSA and the allocation of those loans to the servicers. We did not use the data to assess FSA's processes or to support our conclusions. Accordingly, we did not assess the reliability of this data.

[17] The audits covered either January 1, 2016, through December 31, 2016, or July 1, 2016, through December 31, 2016.

[18] Not all calls were scored (see Finding 2). However, the lack of a score for some calls did not affect the overall reliability of the data for use in achieving our audit objective.

Compliance with Auditing Standards

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We conducted our audit at FSA's offices in Washington, D.C.; Dallas, Texas; Kansas City, Missouri; and Chicago, Illinois; and our offices from June 2016 through December 2017. We discussed the results of our audit with FSA officials on June 26, 2018.

Appendix B. FSA's Oversight of Servicers

Managers and employees from three FSA offices—Business Operations, Finance, and Program Compliance—conducted the following oversight activities:

- monitoring of telephone calls between servicer representatives and borrowers (completed by Business Operations call monitoring team);
- conducting reviews of servicers' compliance with requirements for servicing federally held student loans (completed by the Business Operations process monitoring team, Business Operations servicer liaison team, and Program Compliance, Financial Institution Oversight Service);
- reviewing audit reports on servicers' systems of internal control (completed by independent auditors and reviewed by Business Operations);
- meeting with servicers (facilitated by Business Operations servicer liaison team); and
- conducting surveys of borrowers' satisfaction with their interactions with servicers and surveys of FSA employees (developed by a vendor through consultation with the Office of the Chief Operating Officer and completed by the vendor).

Reviewing Servicer Compliance

Five separate teams (call monitoring team, process monitoring team, servicer liaison team, Financial Institution Oversight Service, and A-123A team) from three FSA offices (Business Operations, Finance, and Program Compliance) evaluated servicers' compliance with contractual and Federal loan servicing requirements.

Call Monitoring Team Reviews

Monthly, the Business Operations call monitoring team listened to a sample of recorded telephone calls between servicer representatives and borrowers.[19] The purpose of this process was to determine whether borrowers received complete and accurate information in an efficient, polite, and professional manner in compliance with FSA's standards for servicer interactions with borrowers. Every month, each servicer provided the call monitoring team with multiple lists of inbound and outbound telephone calls. FSA asked each servicer to provide a list and recordings of all specialty line calls (for example, military-related and consolidation calls). FSA did not ask each servicer to

[19] The call monitoring team is part of the Operations Services Group under Business Operations.

provide recordings of all other inbound and outbound calls. Instead, FSA asked each servicer to provide a list of up to 10,000 inbound and 5,000 outbound calls. From each list, the call monitoring team selected a random sample of 200 to 400 calls. The call monitoring team provided the servicer with a list of the selected calls, and the servicers provided recordings of the selected calls to FSA.

Call monitors listened to the recordings and completed a scoresheet for each call in FSA's call monitoring database. The scoresheet included sections for various subject areas, such as income-driven repayment plans, forbearances, and loan discharges. For each subject area, call monitors were required to answer questions by applying FSA's established standards for handling such calls. FSA's call monitoring database would then calculate a score for each call based on how the call monitor answered all the questions. A call could receive a score up to 100 points. As many as 25 points could be received based on the servicer representatives' introduction and greeting of the borrower, verification of the borrower's identity and contact information, and overall professionalism. As many as 75 points could be received based on the servicer representative's handling of the call in relation to the subject of the call. Calls receiving a score less than 85 failed FSA's established standards.

Each month, the call monitoring team prepared a failed-call report for each servicer.[20] The failed-call report listed each call that received a score less than 85 and an explanation of why FSA considered the call to be substandard. The call monitoring team asked each servicer receiving a failed-call report to review the calls and provide comments and proposed actions. After the servicer provided comments or proposed actions to remediate the noncompliance relevant to the failed calls, or both, the call monitoring team reviewed and either approved or disapproved the proposed corrective actions.

Process Monitoring Team Reviews

Each year, the process monitoring team completed five to six reviews of each servicer.[21] For a typical review, the team members selected samples of borrower accounts (usually 30) and reviewed the servicer's records for those accounts. Examples of records included payment histories, servicing histories, and system screen shots. The team members reviewed the records to determine whether the servicer complied with

[20] FSA did not provide any servicers with failed-call reports during a 10-month period, from July 2016 through March 2017.

[21] The process monitoring team is part of the Servicers Oversight Division within the Operations Services Group under Business Operations.

Federal loan servicing requirements relevant to the special topic of the review and a set of standard topics. Since January 2015, the special topics of the reviews have included determining whether servicers

- appropriately capitalized loan interest,
- correctly applied payments to borrowers' accounts,
- properly processed borrowers' applications for income-driven repayment plans, and
- correctly calculated borrowers' monthly payments under income-driven repayment plans.

Standard topics have included determining whether servicers

- properly granted forbearances and deferments to borrowers;
- correctly recorded the borrowers' interest rates and calculated the borrowers' balances;
- appropriately applied military benefits to eligible borrowers;
- followed guidelines for delinquency notice letters, telephone calls, and skip tracing activities as they pertain to the collection of loans;
- maintained complete and accurate records to support borrower's repayment plans; and
- properly handled borrowers' claims for death, closed-school, or other discharges.

After conducting each review, the process monitoring team prepared a report for each servicer to review. The team asked each servicer for comments and any technical corrections. After a servicer provided comments, the team combined the individual servicer reports into one consolidated report. The consolidated report included the methodology followed during the reviews of all the servicers, the instances of noncompliance identified at each servicer, the team's recommended corrective actions (if any), and comments (if any) from each of the servicers.

The process monitoring team provided the consolidated report to Business Operations management for review. Once approved, Business Operations management provided the consolidated report to the servicer liaisons (employees who served as the primary

point of contact between FSA and servicers), who provided individual reports to their assigned servicers.[22]

Servicer Liaison Team Reviews

At least once each year, FSA sent a team of employees to each servicer. Each review team typically consisted of one member of the Business Operations servicer liaison team and at least one member of the process monitoring team.[23] A servicer liaison team review could be either a comprehensive review or a targeted review. A comprehensive review covered multiple loan servicing processes and operations. A targeted review covered a specific area of concern. Since January 2015, specific areas of concern have included call center operations, forbearances, and income-driven repayment plan processing and approval. After completing a site visit, the review team prepared a draft report describing the instances of noncompliance identified and the team's recommended actions for remediating the instances of noncompliance. The review team provided the report to Business Operations management for review.

After Business Operations management reviewed the report, the review team held a meeting with the servicer to discuss the information included in the draft report. This meeting provided the servicer an opportunity to raise any concerns with the information included in the draft report and to provide additional information. If the servicer provided additional information, a member of the review team researched the information to determine whether it changed the results of the review as presented in the draft report. After the review team made any necessary changes to the draft report, it issued a final report to the servicer and requested the servicer's official written response and proposed actions.

The review team compared the servicer's written response and proposed actions to determine whether the proposed actions would sufficiently address the identified instances of noncompliance. If not, the review team required the servicer to reconsider its proposed actions. Once the review team determined that the actions would likely remediate the FSA-identified instances of noncompliance, a team member monitored the servicer until the proposed actions were implemented.

---

[22] The consolidated report is not provided to the servicers because it contains information on all the servicers reviewed.

[23] Servicer liaisons are part of the Operations Services Group under Business Operations.

Financial Institution Oversight Service Reviews

Financial Institution Oversight Service annually reviewed all servicers.[24] Financial Institution Oversight Service conducted a risk analysis to determine the requirements to test during the coming fiscal year. For example, for fiscal year 2017, the risk analysis identified three areas of risk that applied to Great Lakes, Navient, Nelnet, and PHEAA and three areas of risk that applied to the other five servicers. Based on the risk analysis, Financial Institution Oversight Service designed its 2017 reviews of Great Lakes, Navient, Nelnet, and PHEAA to determine whether they

- timely processed borrowers' requested loan consolidations and correctly calculated the interest rates for the consolidated loans,
- properly processed applications for income-driven repayment plans and correctly calculated the payment amounts for those repayment plans, and
- properly granted an interest rate cap to borrowers eligible under the Servicemembers Civil Relief Act.

Financial Institution Oversight Service designed its 2017 reviews of the other servicers to determine whether they

- properly processed new loans received for servicing,
- properly processed applications for income-driven repayment plans and correctly calculated the payment amounts for those repayment plans, and
- properly granted an interest rate cap to borrowers eligible under the Servicemembers Civil Relief Act.

To determine whether a servicer complied with the selected requirements, Financial Institution Oversight Service reviewed the records for a sample of borrower accounts (usually 29).

After completing its review of the records, Financial Institution Oversight Service prepared a report describing the review objective, review scope, and any instances of noncompliance identified. Financial Institution Oversight Service provided the report to Business Operations management for review. (Financial Institution Oversight Service did not include recommendations in its reports to Business Operations.) After review, Business Operations provided the report to the servicer and worked with the servicer to resolve the instances of noncompliance included in the report.

[24] Financial Institution Oversight Service is part of Program Compliance.

A-123A Team Reviews

FSA's A-123A team reviewed reports on audits of servicers' systems of internal control.[25] These audits were conducted once or twice a year by independent auditors. Such audits are intended to provide a description of a service organization's system of internal control over areas that are likely to be relevant to the service organization's customers' internal control over financial reporting. Although these audits are primarily intended to cover internal control over financial reporting, customers may request that the service organization have the independent auditors cover other key areas of its operations.

Annually, the A-123A team identified key controls over compliance with loan servicing requirements that each servicer was required to have the independent auditor review during the next audit cycle. For example, for fiscal year 2017, the A-123A team identified the following key controls: reporting information to credit bureaus, processing income-driven repayment plans, adding new loans to the financial system, and applying correct interest rates to loans.

The A-123A team reviewed the audit reports to ensure that the independent auditors reviewed all of the servicers' key controls. If the report indicated that the auditor did not test a required key control, the A-123A team would decide whether it needed to conduct its own review of that servicer. If the report disclosed noncompliance, the A-123A team recorded the noncompliance and the servicer's proposed action plan in a summary of aggregated deficiencies. The A-123A team tracked the status of all actions to ensure that the controls relevant to those actions would be tested during the next audit.

Meeting with Servicers

Each servicer liaison held calls once or twice a month with her or his assigned servicer (once a month with EdFinancial Services, New Hampshire, Oklahoma, and Utah and twice a month with Great Lakes, Missouri, Navient, Nelnet, and PHEAA). Each call typically included discussions about (1) noncompliance that FSA identified through its oversight activities; (2) corrective actions to address noncompliance that FSA identified; (3) a report on call center statistics, such as call volume, average call length, average amount of time to answer a call, number of calls that the caller hung up; (4) questions or concerns relevant to loan servicing; and (5) areas that need improvement according to the quarterly satisfaction survey results.

[25] The A-123A Team is comprised of employees from Finance and an audit firm contracted to assist with planning the audits.

Surveying Borrowers' and FSA Employees' Satisfaction with Servicers

FSA contracted with a third-party vendor to conduct surveys of borrowers' and FSA employees' satisfaction with their interactions with servicers.[26] The purpose of the surveys was to help FSA with loan allocation methodology and to identify areas in which servicers might need improvement.

For the July 2017 through December 2017 borrower survey, the vendor sent the survey to about 23,500 borrowers for each servicer.[27] According to FSA's Office of the Chief Operating Officer, about 3 or 4 percent (700 to 900 responses) of the borrowers typically responded to the surveys. For the July 2017 through December 2017 FSA employee survey, the Deputy Chief Business Operations Officer provided the vendor a list of employees who had interactions with servicers. Each employee was to complete a separate survey for each servicer with which he or she worked during the past 6 months. Of the 28 FSA employees receiving the survey, about 60 percent (17) responded.

Both surveys included three general questions.[28]

- The respondent's overall satisfaction with the servicer.
- The extent to which the servicer fell short of or exceeded expectations.
- How the respondent's interactions with the servicer compared to what the respondent thought would be an ideal interaction.

The borrower survey also included questions covering multiple areas, such as the clarity and usefulness of letters and emails received from the servicer, ease of making payments, accuracy and understandability of billing statements, ease of navigating the servicer's website, and quality of service received from the servicers representatives. In addition to the three general questions, the FSA employee survey included questions about their experiences with the servicer's data system; work products, reports, or other servicer-generated deliverables; information received during communications with the servicer; interactions with the servicer; and general working relationship with the servicer.

[26] Before calendar year 2017, the survey was conducted four times a year. Effective for calendar year 2017, the survey was conducted twice a year.

[27] Borrowers were selected using data from the National Student Loan Data System.

[28] FSA and the vendor jointly developed the survey questions.

Those surveyed were asked to answer questions using a scale of 1 through 10 to indicate their level of satisfaction. All of the questions included a comment area in which those surveyed could provide additional information or explain questions assigned a score below seven.

Appendix C. Federal Requirements that Apply to Loan Servicing

Law	Subject	Statutory Citation	Summary of Loan Servicing-Relevant Provisions	Regulatory Citation
Dodd-Frank Wall Street Reform and Consumer Protection Act	Consumer protection	12 United States Code § 5531	Prohibits unfair, deceptive, or abusive acts or practices.	-
Fair Debt Collection Practices Act	Debt collection	15 United States Code §§ 1692d-1692f	Prohibits the use of abusive, deceptive, and unfair debt collection practices and prohibits the threatening or harassing borrowers.	-
Higher Education Act of 1965, as amended (HEA)	Borrower eligibility and consolidation loan eligibility	§§ 428, 428B, 428C, 428H, and 455	Specifies eligibility requirements for borrowers to receive Federal loans and requirements with which servicers must comply when determining borrower eligibility for loan consolidation.	34 C.F.R. §§ 682.201, 682.412, 685.200, 685.211(e), and 685.220
HEA	Deferment	§§ 428, 428B, 455(f), and 493D	Establishes requirements servicers must follow when determining whether a borrower is eligible for a deferment of loan payments.	34 C.F.R. §§ 682.210, and 685.204
HEA	Loan discharge and forgiveness	§§ 428J, 428K, 428L, 437, 455(h), 455(m), and 460 Public Law 109-292 § 6	Establishes requirements for determining whether a borrower is eligible for loan discharge and forgiveness.	34 C.F.R. §§ 682.209, 682.402, 682.407, 685.206-685.219, and 685.222
HEA	Due diligence	§ 432	Sets requirements for reporting certain information to consumer reporting agencies, responding to borrower inquiries, establishing terms of repayment, and reporting a borrower's enrollment and loan status information.	34 C.F.R. §§ 682.208 and 682.411

Law	Subject	Statutory Citation	Summary of Loan Servicing-Relevant Provisions	Regulatory Citation
HEA	Forbearance	§§ 428(c)(3), 428(c)(10), 428H(e)(7), and 430(c)	Allows the granting of forbearance to borrowers meeting certain requirements.	34 C.F.R. §§ 682.211 and 685.205
HEA	Interest rates	§§ 427A, 428C, and 455(b)	Sets the applicable interest rate on the borrower's loan.	34 C.F.R. §§ 682.202 and 685.202
HEA	Loan limits	§§ 428 and 428H	Sets limits on the amounts students may borrow.	34 C.F.R. §§ 682.204 and 685.203
HEA	Repayment plans	§§ 428(b), 428(b)(9), 428C(c)(2), 455(d), 455(e), and 493C	Establishes the repayment plans for a borrower (based on eligibility): • Standard (10-Year and Consolidation) • Extended • Graduated (10-Year and Consolidation) • Income-Contingent • Income-Based • Pay As You Earn • Revised Pay As You Earn • Alternative	34 C.F.R. §§ 682.209, 682.215, 685.208, 685.209, and 685.221

Note: Table is not inclusive of all requirements that must be followed when servicing federally held student loans.

Appendix D. Acronyms and Abbreviations

A–123	Office of Management and Budget Circular A–123
C.F.R.	Code of Federal Regulations
Department	U.S. Department of Education
Direct Loan	William D. Ford Federal Direct Loan
EdFinancial Services	Educational Services of America, Inc.
FFEL	Federal Family Education Loan
FSA	Federal Student Aid
GAO	Government Accountability Office
Great Lakes	Great Lakes Educational Loan Services
HEA	Higher Education Act of 1965, as amended
Kentucky	Kentucky Higher Education Student Loan Corporation
Missouri	Missouri Higher Education Loan Authority
Navient	Navient, LLC
Nelnet	Nelnet Servicing, LLC
New Hampshire	New Hampshire Higher Education Loan Corporation
OMB	Office of Management and Budget
Oklahoma	Oklahoma Student Loan Authority
PHEAA	Pennsylvania Higher Education Assistance Authority
Utah	Utah Higher Education Assistance Authority

FSA Comments

December 7, 2018

TO: Bryon S. Gordon
Assistant Inspector General for Audit

FROM: James F. Manning
Acting Chief Operating Officer
Federal Student Aid

SUBJECT: Draft Audit Report, "Federal Student Aid: Actions Needed to Mitigate the Risk of Servicer Noncompliance with Requirements for Servicing Federally Held Student Loans," Control Number ED-OIG/A05Q0008

Thank you for the opportunity to review and comment on the Office of Inspector General's (OIG) draft audit report "Federal Student Aid: Actions Needed to Mitigate the Risk of Servicer Noncompliance with Requirements for Servicing Federally Held Student Loans," dated September 28, 2018. The purpose of the audit was to determine whether Federal Student Aid's (FSA's) has established policies and procedures to mitigate the risk of servicers not servicing federally held student loans in accordance with federal requirements.

We take our responsibility to provide high-quality service to federal student loan borrowers very seriously. We strongly disagree with your report's statement that "FSA did not establish policies and procedures that provide reasonable assurance that the risk of servicer noncompliance with requirements for servicing federally held student loans was mitigated" and disagree that we rarely hold servicers accountable. We also are concerned that the wording of your findings implies a much broader level of risk than is indicated by the specific examples identified in your report. FSA devotes significant resources to vendor oversight and monitoring efforts – which include extensive call and process reviews, control audits, complaint monitoring, and contractual accountability measures – and has established performance-based contracts focused on driving improvements in customer satisfaction and outcomes related to reduced borrower delinquency and default. In addition, FSA and third parties—including the OIG's financial statement auditor—conduct regular audits of FSA's and our vendors internal control processes. Neither your report nor any of these other extensive oversight efforts have identified material instances of noncompliance by our vendors.

Further, your report is based on fieldwork performed between Jan. 1, 2015, and Sept. 30, 2017. As such, your report fails to reflect significant ongoing improvements we have made to our oversight and monitoring policies and procedures, some of which directly align with the recommendations included in your report. A discussion of some of these efforts, as well as clarifications on some of the specific issues discussed in the report, is provided below.

We appreciate OIG's review and agree that there always is room for improvement in policies, processes, and procedures, particularly in a program as large and complex as federal student loans. That said, we believe that the scope and scale of issues identified in your report, as well as the fact that most of them

have been addressed since the fieldwork was completed, does not support the broad negative characterization of FSA's overall oversight efforts.

Before addressing the report's recommendations in detail, I am providing additional context and updated information related to OIG's federal loan servicer oversight findings. In some cases these activities were in their early stages during the latter part of OIG's fieldwork, while others have been put in place since September 2017.

- FSA currently is tracking 17 Corrective Action Plans (CAPs) involving our federal loan servicers. Five of those CAPs have been closed because the servicers carried out all of the corrective actions, and 12 are in the process of being fully implemented. In general, we have identified and are correcting primary issues that include proper application of forbearance, income-driven repayment (IDR) selection and annual certification, Public Service Loan Forgiveness (PSLF) payment counting, and interest capitalization. All CAPs include making affected borrowers whole, when appropriate, and determining the monetary amount a servicer must reimburse the Department because the contracted fee we paid them to perform a service was not performed appropriately.

  The total amount of contracted fees identified to be reimbursed since the end of the audit period in September 2017 as a result of closed CAPS and work plan completion is approximately $2,055,000. In one example, a servicer was not capitalizing unpaid interest on borrower accounts due to negative amortization. That resulted in a revenue loss for the government totaling approximately $940,000, which the servicer has repaid to the government. In addition, approximately $1,004,000 in fees paid to a servicer for the performance of a contracted service will be reimbursed to FSA upon final determination that the service was not performed. In most cases, amounts owed are credited to FSA on the next monthly invoice after a determination of non-performance has been made.

- In addition to initiating, tracking, and completing CAPs, FSA has restructured one component of the three federal loan servicer oversight resources described in the report. The restructuring involves FSA's Servicer Liaison Team (SLT). Instead of having each member of the SLT assigned to cover one (or sometimes more than one) servicer exclusively, each SLT member now is assigned to monitor one or more specific oversight areas across all servicers. This change in structure allows a more holistic, objective, and cohesive approach to identifying and remediating issues. Once we identify an issue with one servicer, we immediately expand our assessment to all servicers. Oversight areas include, but are not limited to, forbearance and deferment, discharges and forgiveness, repayment plans, delinquency and default, and day-to-day work in process. We also have added a separate team focused only on PSLF, and our call monitoring team remains in place.

- It should be noted that the Financial Institution Oversight Service (FIOS) has completed testing at all of the TIVAS/NFPs during FY 2018. In doing so, we have found that there has been improvement in the servicers' performance overall. In fact, there were several servicers that had no failure during our testing.

- The OIG report discusses a May 2017 SLT report summarizing the results of a site visit review on Navient's use of forbearances. This SLT report was one element of a significantly larger review of

Navient activities in the wake of a lawsuit filed against the company in January 2017 by the Consumer Financial Protection Bureau (CFPB). While ongoing contract oversight and monitoring activities had given no indication of widespread compliance issues with Navient, FSA senior management requested the additional review to obtain supplementary information given the issues raised in the CFPB's lawsuit, which included accusations of widespread efforts to direct borrowers to obtain forbearances when other repayment options could be more beneficial.

Based on our own due diligence, our review of case-specific information provided by Navient, and our analysis of Navient as compared to other servicers, the Department concluded that Navient was not improperly steering borrowers into forbearance, a conclusion supported by FSA's May 2017 site visit report and the data provided in response to the report. Nothing in the report indicates forbearances were applied inappropriately; the observations noted focused on suggested improvements regarding how to best counsel borrowers on a small minority of calls. In fact, a subsequent review of the borrower-level data provided by Navient in response to the site visit report confirmed that, in most cases, forbearances were used as intended to resolve short-term issues related to delinquency consistent with the borrower's circumstances.

Other elements of FSA's review included an assessment of data across all federal servicers to determine whether there were any indications of excessive forbearance use or other noncompliant behavior. Program data indicated that Navient's overall use of forbearance was consistent with that of other servicers, while the duration of forbearances for Navient borrowers was actually among the lowest of the Department's nine servicers. Further analysis by FSA determined that Navient also had among the highest "take-up" rates for income-driven repayment plans, as well as longer-than-average call durations in comparison to all servicers. Calls on which borrowers only were offered forbearance without discussing other options would be expected to be shorter than average, rather than longer.

Across the federal and commercial student loan industry, forbearance originally was developed and appropriately is used as a tool to help borrowers cover temporary periods of financial hardship during which they are unable to make timely payments. For example, if borrowers are laid off from work, suffer an injury, or have their life disrupted by a natural disaster or family crisis, they may fail to make payments for a number of months without needing to permanently change their repayment plan. Forbearance can be used as a tool to bring these borrowers current without the need for a lump-sum payment to cover the months of delinquency. Even in cases where a change in repayment plan to an income-driven repayment plan is the best solution, short-term administrative forbearances must be applied to cover the period when income documentation is being provided and reviewed to ensure the borrower enters the new repayment plan in a "current status."

Page 12 of the OIG report notes that the May 2017 review identified 220 instances—out of 2,388 calls reviewed—where the servicer's call center staff placed borrower accounts into forbearance status without offering alternative or potentially beneficial options to bring accounts current or manage repayment. We should note that the site visit call review was specifically targeted on short-duration calls, as those would be the cases most likely to include improperly truncated interactions of the type cited by CFPB. More

specifically, while the 220 instances observed represent 9.2 percent of the short-duration calls sampled, those results cannot be extrapolated to Navient's overall portfolio. If longer-duration calls had been included in the sample, we would expect this percentage to be significantly reduced.

Also, as noted above, upon subsequently analyzing case-by-case detail about the 220 calls noted in the review, and considering the ultimate outcome of the borrower's situation, FSA determined that that in virtually all cases there was a clear reason for the application of those forbearances and the servicer was following standard practice as discussed in the previous paragraph. In addition, the OIG report does not note that the May 2017 report specifically states that in these instances the servicer acted consistent with the requirements of their contract.

- With respect to the issue concerning FIOS testing as it relates to IDR (see page 13), the OIG addresses the FIOS review of IDR as if it was a comprehensive review of IDR. In fact, FIOS testing was directed at subsets of IDR during specific fiscal years.

  For example, during FY 2013 and 2014, FIOS focused on the granting of income-based repayment (IBR) and income-contingent repayment (ICR).
  - During FY 2015, FIOS testing focused on the implementation of the Pay As You Earn (PAYE) repayment plan.
  - During FY 2016, FIOS testing focused on the renewal process across the IDR plans.
  - During FY 2017, FIOS testing focused on the renewal process and the implementation of the Revised Pay As You Earn (REPAYE) plan.
  - During FY 2018, FIOS testing focused on IDR plans granted when the borrower submitted alternative documentation of income (ADOI) instead of using an Adjusted Gross Income (AGI) from a federal tax return.

  Applying the results of the portions of IDR that FIOS considered at the highest risk during each year would skew the results of that subset when comparing it to the universe of borrowers granted IDR. In about half the cases where the servicer miscalculated the AGI during FY 2018, there was no impact to the monthly payment amount (MPA), because the borrower's recalculated income still resulted in a zero-dollar MPA. For lower-income borrowers, incorrect calculation of AGI did not result in an incorrect MPA or repayment amount.

As noted above, FSA is committed to ensuring that students, parents, and borrowers receive world-class service throughout the student aid life cycle. While we strongly believe that our current oversight and monitoring environment includes policies and procedures that provide reasonable assurance that the risk of servicer noncompliance with requirements for servicing federally held student loans was mitigated and a reasonable assurance that our vendors are generally complying with the requirements of their contracts, we recognize that we can do better still. Accordingly, we have launched the Next Gen FSA initiative, which is focused on fundamentally transforming the way we interact with our customers. A key element of Next Gen FSA will be restructuring our systems, processes, and contracts to introduce even greater accountability based on more target standards, metrics, and incentives and disincentives to drive outstanding performance. We believe that this effort also directly addresses a number of the

issues underlying the findings and recommendations within the OIG report and will lead to even better outcomes for the customer and taxpayer alike.

FSA Response to Recommendations

Finding No. 1: FSA Did Not Track All Identified Instances of Noncompliance and Rarely Held Servicers Accountable for Noncompliance with Requirements.

Recommendation 1.1: Track all instances of noncompliance identified during FSA reviews, regardless of whether the specific instances were corrected and did not require further action to be taken by either the servicer or FSA.

Response: FSA agrees with this recommendation to track all instances of noncompliance and has implemented the suggested improvement. FSA has developed procedures to ensure that all instances of non-compliance are tracked in an internal tracking database, including non-compliance that does not require further action by either the servicer or FSA. This tracking mechanism has been in place for several years and has been enhanced to ensure that all instances are tracked regardless of resolution classification. All instances are followed through to resolution. In instances where there is no resolution, the items remain in the tracking database as data points for trending and other analytical purposes. Thus, FSA is already implementing this recommendation to track all instances of noncompliance.

Recommendation 1.2: Analyze the records relevant to noncompliance, identify trends and recurring noncompliance for each servicer and across all servicers, and use the information as a basis for assessing servicer performance.

Response: FSA agrees with the recommendation and is using analysis and trending information gleaned from servicer noncompliance tracking as a basis for assessing servicer performance. The information collected in the internal tracking database (see 1.1 above) allows FSA to perform that analysis and trending for use in assessing servicer performance. We also use the noncompliance tracking information to evaluate the effectiveness of guidance FSA provides to servicers and issues inherent in the *Title IV* program regulations. Thus, FSA is already implementing this recommendation to use data on noncompliance to analyze and use trending information to assess servicer performance along with the other processes mentioned above.

Recommendation 1.3: Use the contractual accountability provisions available, such as requiring the return of funds or reducing future loan volume, to hold servicers accountable for instances of noncompliance.

Response: FSA agrees with the recommendation and, as we previously discussed, is using these tools to ensure accountability of the servicers through the use of contractual provisions and CAPs to servicers that must be implemented. As appropriate to the instance of noncompliance, some actions taken have included review and approval of corrective work plans, as well as imposing penalties. Examples of penalties have included reducing the loan volume allocation for a one-month period for a servicer that had call statistics outside the acceptable range and requiring multiple servicers to reimburse FSA in

cases where fees were paid related to contracted services that were not performed. Thus, FSA is already implementing this recommendation.

Finding No. 2: Information Necessary to Ensure Servicer Compliance Not Always Complete.

Recommendation 2.1: Verify that programming corrections ensure the system prompts call monitors to complete all necessary data fields before submitting scoresheets.

Response: While FSA agrees that there were programming errors that resulted in scores not being recorded fully in the system previously used to generate Call Monitoring Reports, FSA corrected these errors and subsequently implemented an improved system. On June 14, 2018, FSA implemented a new database that requires the completion of all data fields and all selections before a submission can be accepted into the database. This enhancement helps to reduce the chances of inadvertent completion errors by the Call Monitoring Team. Thus, FSA has already implemented this recommendation.

Recommendation 2.2: Ensure that FSA management has implemented its new quality control process and is evaluating a management-determined percentage of each call monitor's completed work each month.

Response: FSA agrees with this recommendation and has implemented a Quality Control measure for the Call Monitoring Team. Each day, the team's quality control analyst reviews between 10 and 14 calls, which is three to four percent of the total calls monitored. This equates to quality control being conducted on 220–300 calls per month in an even distribution across all Call Monitoring Team members.

Recommendation 2.3: Regularly share the results of any oversight activities with servicers, regardless of whether management is making changes to existing processes.

Response: FSA agrees with the recommendation and since April 2017 has provided federal loan servicers with the results of all oversight activities related to call monitoring. OIG observed a period of time (June 2016 to March 2017) during which call monitoring reports were not issued directly to servicers; however, during that period FSA did provide alternative relevant feedback to servicers through regular meetings and issue escalation. Starting with the April 2017 Monthly Call Monitoring Report, servicers have received and continue to receive reports on a monthly basis. In addition, servicers have the opportunity to provide feedback on each Call Monitoring Report before the report is made final.

Again, we thank you for the opportunity to review and comment on this draft report. As noted above, we strongly disagree with the report's characterization of FSA's overall monitoring and oversight efforts, and respectfully suggest that the final report be revised to reflect the information provided above,

which we believe would provide a more accurate and complete picture of our efforts to mitigate the risk of servicers not servicing federally held student loans in accordance with federal requirements. Please let me know if you have any questions or need further information.

Sincerely,

James F. Manning
Acting Chief Operating Officer