EYE ON ED

Episode 2—The OIG's Audit of FSA Oversight of Student Loan Servicing

[Introduction] This is Eye on Ed. Your source for information about audits, investigations, and other work by the U.S. Department of Education Office of Inspector General. Tune in for the latest news on our efforts to find and stop fraud, waste, and abuse in Federal education programs, operations, and funding.

[Stephanie Bloom] Hi, I'm Stephanie Bloom. Welcome to Eye on ED.

Today we're discussing an issue that has generated a lot of media and Congressional attention. It's the findings of our recent audit on the Department of Education's Federal Student Aid office's oversight of student loan servicing.

Here to discuss this audit with me are Howard Sorensen, Assistant Counsel to the Inspector General and Greg Bernert, an auditor from our Chicago office. Gentlemen thank you for being here today.

[Greg Bernert] Happy to be here.

[Howard Sorensen] Glad to be here.

[Stephanie Bloom] Howard, let me start with you. What is student loan servicing all about?

[Howard Sorensen] Stephanie, since 2011, the Department of Education and the Federal Student Aid office has been the sole source of Federal student loans. The Department has more than a trillion dollars in student loans spread over millions of individual borrowers. The Department can't make and collect these loans all by itself, so it has hired companies called servicers to do the work to collect the loans after students graduate from college. These are the companies that send a graduate the first letter, "Congratulations, you've graduated, you need to start paying your loans." They collect the payments, they send reminder notices to students, these are the companies that answer the phone to answer any questions students have about their loans. If they encounter financial difficulties and need to come up with a different payment plan, these are the companies they have to call to get answers on behalf of the Department of Education. So Federal Student Aid contracts with these companies, and because they contract with these companies, they need to make sure the companies do what they promise the Department they will do.

[Stephanie Bloom] Wow, that's really a lot of loans they have to service and a lot of customers they they're working with. Greg, how many companies is FSA contracting with to service these loans?

[Greg Bernert] Well, as of the end of our audit period in September 2017, there were nine servicers under contract to service Federal student loans, companies like Navient, Nelnet Servicing, and PHEAA.

[Stephanie Bloom] And what are some of the things FSA does to oversee those companies?

[Greg Bernert] Well, at the time of our audit, FSA had several procedures to oversee the work of the loan servicers to ensure that they were meeting all Federal requirements for servicing the loans. For example FSA listened to recorded telephone calls between the loan servicers and borrowers; they did their own reviews and reviewed audits of the servicers that were conducted by independent auditors. They had meetings with the servicers once or twice a month to go over issues FSA found or handle any other concerns. And they also surveyed borrowers and FSA employees twice a year to gauge their satisfaction with the servicers. And then FSA used those survey results to help determine how many new loans to allocate to each servicer.

[Stephanie Bloom] So Greg, what did your audit examine?

[Greg Bernert] We looked at whether steps taken by FSA to oversee the servicers lowered the risk of servicers not complying with laws and regulations.

To determine this, we had to first narrow FSA's oversight activities down to the ones that had the biggest impact on the effectiveness of FSA's oversight. Those key activities were listening to phone calls between borrowers and loan servicers, reviewing the servicers' records to assess compliance with laws and regulations, and reviewing independent auditor reports on servicers' operations. So after we identified those key activities, our audit examined FSA's records that were relevant to those activities.

[Stephanie Bloom] What were you looking for?

[Greg Bernert] We were looking for identified instances of noncompliance, that is, anything in the records that said the servicer wasn't doing what it was supposed to be doing. And once identified, we categorized each instance into groups based on the general subject area. For example, if the noncompliance was related to forbearance, repayment, or interest rates. We examined which noncompliance subject areas happened more than once at each loan servicer, and we looked at FSA's recommendations and the servicer's proposed corrective actions to determine whether those actions would likely lower the risk of similar instances of noncompliance reoccurring.

[Howard Sorensen] Right Greg. We were looking for, what did FSA do when it found that there was noncompliance? We were looking to see, what action did FSA take to lower the risk that that same thing might happen again in the future.

[Stephanie Bloom] Greg, what did your audit find?

[Greg Bernert] Overall we concluded that FSA's policies and procedures did not really lower the risk of noncompliance. We had two significant findings.

[Howard Sorenson] First, we found that FSA wasn't tracking all of the noncompliance they identified. In fact, if they found something wrong onsite, and the servicer promised to fix it, they didn't even enter that noncompliance into the database that they used to record noncompliance.

[Greg Bernert] And they weren't using the information they did have to identify trends or patterns of repeated noncompliance at each servicer or across servicers.

And second, we determined that FSA rarely held servicers accountable for the noncompliance they did identify.

[Stephanie Bloom] Alright, let's start by talking about those trends. Why does it matter that FSA wasn't tracking all instances of noncompliance?

[Greg Bernert] It matters because FSA might not be able to identify trends or repeated instances of the same type of noncompliance either at a single servicer or across all servicers. And that makes it harder for FSA to know when to take some additional action or hold servicers more accountable for repeated noncompliance.

[Howard Sorensen] And if I may, Greg, I sort of think about it like this. All these different reviews that FSA does, they're taking snapshots at different points in time in different activities of the servicers. They're not taking all those snapshots and putting them together for the big picture.

[Stephanie Bloom] Ok, so it sounds like FSA didn't really have all of the records and information it needed to get the big picture of what was going on at the servicers. But your audit also found that when FSA did identify problems at servicers, it rarely held them accountable. What are some of the things FSA could have done?

[Greg Bernert] Well, in FSA's contracts with the loan servicers, there are a couple provisions that allow FSA to penalize servicers for noncompliance. For example, FSA can require a servicer to return the fees it was paid to service an account, or FSA can assign fewer new loans to the servicer that did not comply with the law and regulations. But we found that FSA rarely did either of those two things.

[Stephanie Bloom] What is the impact of FSA not holding the servicers accountable?

[Greg Bernert] Well one impact is in terms of the taxpayer dollars that fund the Federal student aid programs: FSA might be paying the loan servicers more than the servicers are entitled to. If FSA doesn't recoup money from loan servicers for their noncompliance and doesn't adjust the number of loans noncompliant servicers are assigned, FSA ends up paying more than it should. Also, if FSA doesn't hold servicers accountable, the servicers have less incentive to follow all the rules.

[Howard Sorensen] And there could be a tremendous impact on borrowers, too. Unless the servicers give the borrowers correct information about the repayment options that they have under the law, they may be paying more than they need to under their financial circumstances. They could even end up defaulting on their loan.

[Stephanie Bloom] Your audit made six recommendations to address the issues you identified. Can you highlight a couple for us, Greg?

[Greg Bernert] Sure. FSA can and should do more to ensure that the loan servicers are complying with all Federal requirements to not only protect borrowers but also to ensure that taxpayer dollars are protected from improper payments. So we recommended that FSA track all instances of noncompliance that they identify during their oversight activities, and use that information to see if there are trends of noncompliance at each servicer or across all servicers. We also recommended that FSA use the information to evaluate the performance of the servicers and actually use the contract provisions to hold servicers accountable by requiring them to return money or by reducing the amount of loans they get in the future.

[Stephanie Bloom] Did FSA agree with your findings and recommendations?

[Greg Bernert] Well, FSA disagreed with our overall conclusion that they weren't mitigating the risk of servicers' noncompliance. They also disagreed with certain aspects of our finding about tracking noncompliance and stated that the wording of the finding implied a broader risk than our examples showed. But, as we pointed out, 61 percent of the reports we reviewed identified at least one instance of noncompliance, including some repeated noncompliance at some servicers.

FSA also disagreed that they weren't holding servicers accountable and said that they had taken action since the end of our audit period audit to recover more money from servicers for noncompliance, although what they have recovered is still a very small percentage of the money FSA pays loan servicers. But despite their disagreement with parts of our finding, FSA agreed with all of our recommendations and said they are already implementing the corrective actions.

[Stephanie Bloom] So Howard, what is the big takeaway from this audit?

[Howard Sorensen] Federal Student Aid is actually doing a lot of activity with the servicers. It's just not putting it all together, realizing exactly what's going on, and taking action to prevent further noncompliance in the future. We've given recommendations, it's agreed to carry out all of them. If it carries out the recommendations, it should be in a better place.

[Stephanie Bloom] And I understand we'll hear more about that on March 6 when the OIG will testify before Congress on the audit.

[Howard Sorenson] Yes, our Assistant Inspector General for Audit will be speaking to a House of Representatives Appropriations Subcommittee.

[Stephanie Bloom] We look forward to that! Thank you Howard and Greg for taking the time to join us today and break down this complex and very important issue.

[Greg Bernert] Absolutely—thanks for having me.

[Howard Sorensen] My pleasure.

[Stephanie Bloom] And thanks to our listeners for tuning in. You can read the full audit report and find more information about our office and our work on our website. Check back with us for additional podcasts and updates, including the March 6 testimony. I'm Stephanie Bloom with the U.S. Department of Education Office of Inspector General, and this has been Eye on ED.