Testimony of Bryon Gordon, Assistant Inspector General for Audit
U.S. Department of Education, Office of Inspector General, before the
Subcommittee on Labor, Health and Human Services, Education, and Related Agencies
Committee on Appropriations, U.S. House of Representatives
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Chairwoman DeLauro, Ranking Member Cole, members of the Subcommittee:

Thank you for inviting me here today to discuss the U.S. Department of Education (Department) Office of Inspector General's (OIG) recent audit of the Federal Student Aid office's (FSA) oversight of student loan servicing. Through FSA, the Department awards more than $122 billion in student aid to some 13 million students each year. It also manages a loan portfolio of more than $1 trillion, making the Department one of the largest financial institutions in the country.

To help manage the Department-owned student loan portfolio, as of September 30, 2017, FSA contracted with 9 companies, called "servicers." The largest 4 servicers are responsible for about 93 percent of the $1 trillion in loans. The servicers collect payments on loans, advise borrowers on resources and benefits to manage their Federal student loan obligations, respond to customer service inquiries, and perform other administrative tasks associated with maintaining a loan on behalf of the Department. The servicers must comply with all requirements for servicing federally held student loans. For example, servicers must correctly record the borrowers' interest rates and calculate the borrowers' balances, properly grant forbearances and deferments to borrowers, properly process borrowers' applications for income-driven repayment plans, and correctly calculate borrowers' monthly payments under income-driven repayment plans.

Audit of FSA's Oversight of Loan Servicing Summary

The objective of our audit was to determine whether 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.

At the time of our audit, FSA had several processes in place to oversee the work of the loan servicers to ensure that they were meeting Federal requirements for servicing the loans. FSA had teams conducting four types of periodic reviews, including listening to recorded telephone calls between the loan servicers and borrowers. FSA also reviewed the annual audits of the servicers' independent auditors for findings related to internal controls. FSA met with the servicers once or twice a month to go over issues FSA found or handle any other concerns. It also surveyed borrowers and FSA employees twice a year to gauge their satisfaction with the servicers. Our audit examined whether these activities, as well as FSA's policies and procedures, provided reasonable assurance that the risk of servicers not servicing federally held student loans in accordance with Federal requirements was mitigated or reduced.

Our audit found that FSA's oversight policies, processes, and activities collectively did not provide reasonable assurance that the risk of servicer noncompliance with requirements for servicing federally held student loans was being mitigated or reduced. Our audit found that FSA's oversight activities regularly identified instances of servicer noncompliance. Specifically, we found that FSA identified servicer noncompliance in 210 (about 61 percent) of the 343 monitoring reports that we analyzed. FSA management routinely tracked the instances of noncompliance when servicers did not remediate them before FSA issued a final monitoring report. However, FSA did not track the identified instances of noncompliance if servicers remediated them. For example, if during the course of a review, FSA found 5 instances of noncompliance in a sample of 30 borrower accounts, and the servicer corrected 4 of them during the course of the review, FSA tracked only the single uncorrected instance of noncompliance. Further, FSA management did not analyze the information it did have to track and identify trends and recurring instances of noncompliance at each servicer and across all servicers.

We concluded that FSA management has information that FSA could use to identify recurring instances of and trends in noncompliance. For example, FSA's monitoring reports disclosed recurring instances of noncompliance primarily in two areas: consumer protection (representatives not informing borrowers of the available repayment options) and income-driven repayment (servicers incorrectly calculating income-driven payment amounts). The monitoring reports also disclosed that some servicers had noncompliance rates that were higher than average.

Additionally, we found that FSA management rarely used available contract provisions to hold servicers accountable for instances of noncompliance and did not incorporate a performance metric relevant to servicer compliance into its methodology for assigning loans to servicers. FSA uses metrics (such as percentage of borrowers who are current in repaying their loans, the percentage of borrowers who are delinquent, and customer satisfaction scores based on surveys of borrowers and FSA staff) to measure the performance of each servicer. It then allocates the volume of new loans to servicers based on a formula that considers each of the metrics. Our audit also found that FSA employees did not always follow policy when evaluating the quality of servicer representatives' interactions with borrowers. FSA also did not provide servicers with reports of failed calls during a 10-month period, from June 2016 through March 2017, because FSA was revising the report format.

Because FSA's oversight policies, processes, and activities collectively did not provide reasonable assurance that the risk of servicer noncompliance was being mitigated, FSA management did not have reasonable assurance that servicers were complying with Federal loan servicing requirements when handling borrowers' inquiries. Additionally, borrowers might not have been protected from poor services, and taxpayers might not have been protected from improper payments. Because it was not holding loan servicers accountable for instances of noncompliance, FSA did not provide servicers with incentive to take actions to mitigate the risk of continued servicer noncompliance that could harm borrowers. For example, a borrower might not have received the most favorable repayment terms available to them. Or, if a borrower was enrolled in an income-driven repayment plan and the servicer incorrectly calculated the affordable monthly payment, the borrower could be negatively affected.

We recommended that FSA (1) track all instances of noncompliance identified during its oversight activities; (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; (3) use the contractual provisions available to hold servicers accountable for instances of noncompliance; (4) verify that call monitors are completing all necessary data fields before submitting call evaluation scoresheets; (5) ensure that FSA management has implemented a quality control process and is evaluating call monitors' completed work each month; and (6) regularly share the results of any FSA loan servicing oversight activities with servicers.

In its December 7, 2018, comments on a draft of our report, FSA responded that it already had or will implement all six recommendations, and it described improvements it has made to its oversight activities since September 2017. However, 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 stated that the wording of our first finding implied a much broader risk than indicated by the examples included in the report. FSA also disagreed that it rarely held servicers accountable, stating that enforcement actions since September 2017 have resulted in about $2 million in recommended recoveries.

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 did not discuss them in our audit report. However, and as we stated in our audit report, the improvements as described are aligned with our recommendations. 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 our report based on FSA's comments.

This concludes my remarks on our audit of FSA's oversight of student loan servicing. As you know, the Federal student aid programs are exceptionally large, complex, and inherently risky because of the numerous entities involved in administering the programs and the characteristics of student populations. Accordingly, FSA management needs to improve its oversight to provide reasonable assurance that its contractors are complying with all applicable laws, regulations, and guidance, and serving the interests of students. In addition to the audit covered in this testimony, we have a number of ongoing and planned audits involving the Federal student aid programs, as outlined in our FY 2019 Annual Plan. In addition to a copy of our audit, I have attached a copy of our FY 2019 Annual Plan for your review. We look forward to working with FSA, the Department, this Subcommittee, and the 116th Congress to help improve Federal student assistance programs and operations so they meet the needs of America's students and families, and ensure that the vital tax dollars that fund these programs are protected from waste, fraud, and abuse. I'm happy to answer any of your questions.