



UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

February 29, 2016

The Honorable Patty Murray
United States Senate
154 Russell Senate Office Bldg.
Washington, D.C. 20510

The Honorable Elizabeth Warren
United States Senate
317 Hart Senate Office Bldg.
Washington, DC 20510

The Honorable Richard Blumenthal
United States Senate
706 Hart Senate Office Bldg.
Washington, DC 20510

Dear Senator Murray, Senator Warren, and Senator Blumenthal:

Thank you for your August 4, 2015, letter requesting that the U.S. Department of Education (Department) Office of Inspector General conduct an independent examination of the adequacy and accuracy of the Department's review of student loan servicers' compliance with the Servicemembers Civil Relief Act, specifically its requirement to provide eligible servicemembers with an interest rate reduction on certain Federal student loans. The enclosure to this letter provides the results of our review.

If you have any questions or if you need any additional information, please do not hesitate to contact me directly at (202) 245-6900 or have a member of your staff contact our Congressional Liaison, Catherine Grant, at (202) 245-7023.

Sincerely,

Kathleen S. Tighe
Inspector General

Enclosures

cc: The Honorable Lamar Alexander, Chairman, Committee on Health, Education, Labor, and Pensions, United States Senate
Dr. John King, Acting Secretary, U.S. Department of Education

Servicemembers Civil Relief Act

Congressional Request

On August 4, 2015, Senators Warren, Murray, and Blumenthal requested that the Office of Inspector General conduct an independent examination of the adequacy and accuracy of the Department of Education's (Department) reviews of student loan servicers' compliance with the Servicemembers Civil Relief Act (SCRA) requirement to provide eligible servicemembers with an interest rate reduction on certain Federal student loans. Concerns were raised about the Department's conclusion contained in a May 26, 2015, press release that "in less than 1 percent of cases, borrowers were incorrectly denied the 6 percent interest rate cap required by the laws." Along with the request, we were provided an August 2015 Staff Analysis Report critiquing the SCRA program reviews that the Department performed.

Work Performed

To respond to this request, we reviewed the Staff Analysis Report, obtained and reviewed the SCRA program reviews that the Department performed, obtained and reviewed supporting documentation, and interviewed Department officials involved in planning and conducting the program reviews and preparing the May 2015 press release. We did not conduct this review as an audit or inspection.

Summary of Results

We identified flaws in the Department's sampling design that resulted in the Department testing few borrowers eligible for the SCRA benefit, errors in the program reviews it conducted, and inconsistent and inadequate corrective actions for the errors it identified for the period reviewed. As a result, the press release of May 26, 2015, is unsupported and inaccurate. In response to the results of our review, the Department stated that it was a management decision to not require further corrective actions for periods reviewed due to limited servicing errors identified and that the decision was not primarily based on a statistical analysis. To address the issues with servicemembers' SCRA benefits, the Department designed new procedures that, if properly implemented, should provide for all eligible borrowers to receive the SCRA benefit as of July 2014.

Background

Congress enacted the SCRA in December 2003 as a modernized version of the Soldiers' and Sailors' Civil Relief Act of 1940. The SCRA, among other benefits, provides for an interest rate cap of 6 percent for active duty servicemembers on certain loans, including mortgages, credit cards, and automobiles acquired before active duty status. In 2008, an amendment to the Higher Education Act of 1965 provided for the SCRA interest rate cap on Federal student loans meeting the requirements of the SCRA.

According to the SCRA, to receive the 6 percent interest rate cap, the loan must have been made before the servicemember was called to active duty; the active duty servicemember must also provide the creditor a written notice of the servicemember's eligibility for the interest rate cap and a copy of the service member's military orders. Under the SCRA, the Secretaries of each military service and the Secretary of Homeland Security have the primary responsibility for ensuring that servicemembers receive information on their SCRA rights and protections.

Department of Justice Complaint Filed

In May 2014, the Department of Justice filed a complaint against Navient¹ alleging multiple violations of the SCRA, including that Navient failed to provide servicemembers the 6 percent interest rate to which they were entitled under SCRA for both private and Federal student loans. The Federal student loans Navient serviced included Federal Family Education Loans, Federal Direct Loans, and Federal Family Education Loans held by the Department. In September 2014, Navient entered into a consent order that required it to correct its practices going forward and make eligible servicemembers with private and Federal student loans whole from the point they became eligible for the SCRA interest rate cap in the past and to compensate borrowers for other violations of the SCRA.²

Federal Student Aid Reviews Initiated

In response to the Department of Justice complaint, the Secretary of Education announced that the Department would review each of the four Title IV Additional Servicers (TIVAS)³ for compliance with their contracts and the requirements of the SCRA. In June 2014, Federal Student Aid's (FSA) Financial Institution Oversight Service (FIOS) began its program review of Navient. The program reviews of the remaining three TIVAS began in July and August 2014. The objective of the reviews was to determine whether borrowers of eligible Federal Family Education Loans and Direct Loans received the benefit of the 6 percent interest rate cap provided by the SCRA in accordance with applicable status and the Department's regulations and guidance. The purpose and scope of the reviews were to

- determine whether the TIVAS complied with all Department statutes, regulations, and guidance in determining whether borrowers were eligible to receive the interest rate cap provided by the SCRA and
- ensure that eligible borrowers who met the requirements for the interest rate cap under the SCRA were granted the benefit on all of their eligible Federal student loans.

In September 2014, the Department decided to perform a second review of Navient,⁴ and FIOS conducted the review in January 2015. FIOS modified and strengthened the procedures for identifying the universe of potential eligible borrowers and expanded the sample size designed for testing to 300. FSA also

¹ The complaint and related September 2014 consent order covered Navient (a company that services loans for the Department, as a Title IV Additional Servicer, and other entities), and Sallie Mae Bank (a company that holds private student loans and Federal Family Education Loans).

² In May 2015, the Department of Justice disclosed that 77,795 borrowers would receive benefits under a settlement with Navient to resolve allegations of SCRA violations. The Department of Justice later disclosed that the settlement included 18,191 borrowers with Department-owned loans serviced by Navient. We confirmed with Justice that it does not have data showing which of the three types of SCRA violations alleged in its complaint occurred with respect to a servicemembers' Department-owned loans. All servicemembers receiving benefits under the settlement had military service dates that qualified them for the 6 percent interest rate cap and had a military code in Navient's computer system. According to the consent decree implementing the settlement, the parties agreed that, to resolve the matter efficiently and expeditiously, compensation Navient provides under the settlement may go beyond the SCRA benefits and may be to servicemembers who may not have been eligible for SCRA benefits. As a result of the information we received from Justice, we concluded that we could not use the Justice data to assess the adequacy and accuracy of the Department's program reviews.

³ The four TIVAS are Navient, Pennsylvania Higher Education Assistance Authority, Great Lakes, and Nelnet.

⁴ The Department did not make the results of the first Navient review public, and neither the Department's nor our conclusions were based on the sample included in the first Navient review.

engaged a contractor, Ernst & Young, to review the same sample of loans serviced by Navient and to corroborate the FIOS review.

Limitations on the Universe FIOS Used in Its Program Reviews

For its reviews of Pennsylvania Higher Education Assistance Authority, Great Lakes, and Nelnet, FIOS relied on data in the National Student Loan Data System to identify potentially eligible SCRA borrowers. This approach identified loans or borrowers in a military deferment or grace period status⁵ with an interest rate exceeding 6 percent. FIOS used military deferment and grace status to identify potentially eligible borrowers because the National Student Loan Data System did not have information on borrowers requesting the SCRA benefit. FIOS did not attempt to determine whether the TIVAS had information in their own servicing systems that it could have used to identify a complete universe of military borrowers who had requested the SCRA benefit, which may have allowed for a better estimate of the extent of compliance by the TIVAS. Instead, FIOS relied on the National Student Loan Data System, which restricted its universe to only borrowers in a military deferment or grace period.

For the second Navient program review, FIOS used the results of a match with the Defense Manpower Data Center, which is a Department of Defense database, to identify potentially eligible servicemembers. The match identified active duty servicemembers and the time periods of active duty.

Sampling Methodology Flaws

FIOS designed and used what is called an “acceptance” sampling methodology to evaluate three of the TIVAS for compliance with the SCRA requirements. This type of sampling establishes a threshold for drawing conclusions concerning a population. If the number of errors found in the sample is below the established threshold, then the population is deemed acceptable. If the number of errors found in the sample is above the threshold, the population is rejected.⁶ For example, if an acceptance sample were taken from a shipment, the results of the inspection would be used to decide whether to accept or reject the entire shipment. The reported sampling design was based on statistically valid random samples of 99 loans, representing 99 distinct borrowers, and established a threshold that if FIOS identified no instances of noncompliance during testing, FIOS would conclude that the servicer met the population’s tolerable deviation rate of 3 percent or less, with 95 percent confidence.⁷ Therefore, the FIOS sampling design defined compliance with SCRA as deviation rates up to 3 percent. Under the acceptance sampling design, when FIOS found incorrect denials or other instances of noncompliance, FIOS could not estimate

⁵ Military grace periods and deferment periods are available for servicemembers for Federal loans. For subsidized loans, during these periods, the borrowers do not make payments on their loans and interest does not accrue on the loan balance. For unsubsidized loans, the borrower has the option to defer payments on the loans; however, interest does accrue.

⁶ The Government Accountability Office’s guide, “Using Statistical Sampling,” states that acceptance sampling is a variation of attribute sampling, but it does not permit the estimation of the rate of occurrence of the deficiencies. Acceptance sampling provides us with the decision of whether to accept or reject a specific population.

⁷ FIOS tested whether the TIVAS complied in four areas: (1) granting SCRA benefits, (2) denying SCRA benefits, (3) using the correct active duty military service dates, and (4) adjusting accounts based on service dates. The reviews for the four servicers covered periods through April or May 2014 and were designed to test servicer compliance with the requirements in place at the time, which required a servicemembers to request the SCRA benefit and provide supporting documentation.

the extent of noncompliance by the TIVAS; under its approach, FIOS should have “rejected” the population if noncompliance in the sample exceeded 3 percent. Therefore, the program reviews were not designed to form statistical estimates for the percentage of eligible applicants incorrectly denied the SCRA benefit, but were designed to provide information on areas of noncompliance for management to address through corrective actions. We determined that FSA did not consult with or use a statistician to assist with designing the sample it used in its program reviews.

Sampling Errors

We identified sampling errors with the FIOS program reviews of all four TIVAS. Examples of the errors include the following.

- The samples for 3 program reviews were not random for either loans or borrowers because FIOS selected cases from a list of servicing actions. For each of these program reviews, FIOS selected the samples from a universe comprising National Student Loan Data System records of military deferments and military grace for borrowers. FIOS did not filter the dataset to remove duplicate records or to create a loan-level or borrower-level dataset. After selecting each sample, FIOS confirmed that each sampled borrower was selected only once. As a result, borrowers and loans with multiple military deferments and military grace records were more likely to be selected, and each borrower or loan did not have an equal chance of selection. The program reviews did not disclose that FIOS drew the samples from servicing actions.
- When preparing the dataset from which FIOS drew the sample for the Pennsylvania Higher Education Assistance Authority review, FIOS failed to exclude military deferment and grace records associated with loans with an interest rate of 6 percent or less. As a result, 51 of the 99 selected records were associated with loans with interest rates of 6 percent or less, and the borrowers of those loans would not benefit from the SCRA interest rate cap.
- In its second Navient program review, FIOS included servicing actions that occurred outside of the review period of June 19, 2009, through May 31, 2014. Specifically, FIOS reviewed some servicing actions even though the servicing actions were posted after May 31, 2014, as long as they had an effective date prior to June 1, 2014. FIOS explained that “the nature of FFEL [Federal Family Education Loans] and DL [Direct Loan] processing is retroactive and entities must be able to record both an effective date and a posting date on any transaction.” The program review report states that, of the 23 borrowers who requested the interest rate cap, Navient correctly granted the SCRA interest rate cap to 10 borrowers. However, these 10 borrowers included 3 borrowers for whom Navient granted the interest rate cap based on new procedures (the Defense Manpower Data Center match) that took effect after the review period end date of May 31, 2014, but for whom the effective dates for the SCRA benefit fell within the review period. For these three borrowers, Navient did not grant the SCRA benefit during the review period, and FIOS should not have included these borrowers as part of the program review.

As a result of these errors, we cannot render an opinion on the accuracy of the results that FIOS reported.

Second Navient Program Review Methodology Not Disclosed

From the limited documentation available, we could not determine whether the FIOS selected the sample for the second Navient review at the loan or borrower level. FIOS did not specify the rationale, expected deviation rate, tolerable deviation rate, or expected precision for the sample design. To allow readers to properly interpret the results of the program review, FIOS should have disclosed this information and any limitations on the sample results.

Universe and Sampling Identification of Few SCRA Applicants

For the program reviews of Pennsylvania Higher Education Assistance Authority, Great Lakes, and Nelnet, FIOS selected samples of 99 loans, representing 99 distinct borrowers, for testing. For the second Navient review, FIOS selected a sample of 300 borrowers for testing. This resulted in FIOS testing 597 borrowers across the four TIVAS. However, out of the 597 borrowers tested, only 55 borrowers requested SCRA benefits, of which FIOS deemed 37 to be eligible.⁸ Because the number of borrowers that requested and were eligible to receive SCRA benefits was small, FSA's ability to draw conclusions on TIVAS compliance was limited to the few instances of noncompliance that FIOS identified.

Noncompliance by TIVAS

For three of the program reviews, FIOS identified one instance in each review that resulted in a failure to provide the SCRA benefit to an eligible borrower. For two of the program reviews, FIOS also determined that the TIVAS improperly granted the benefit, used incorrect active duty dates, and made incorrect adjustments based on service dates. FIOS reported noncompliance with SCRA and recommended corrective actions, which included correcting the instances that were identified for specific borrowers that the program reviews covered. FIOS also recommended that two TIVAS review the portfolio of borrowers granted the SCRA benefit to ensure that the TIVAS granted the benefit only to eligible borrowers, used the correct service dates, and made correct adjustments based on actual service dates. However, FIOS did not recommend that the TIVAS review the portfolio of borrowers to identify and correct all potential instances of incorrect denial of the SCRA interest rate cap. For the program review of Nelnet, FIOS drew no conclusion on whether Nelnet was in compliance because FIOS found no errors for the four SCRA eligible servicemembers it tested.

Press Release Inaccurate

We found that the overall conclusion in the May 26, 2015, press release was not supported by the program reviews. Specifically, the press release concluded that "The reviews, which looked at active-duty servicemembers' SCRA eligibility between 2009 and 2014, show that in less than 1 percent of cases, borrowers were incorrectly denied the 6 percent interest rate cap required by the laws." FIOS based that calculation on 3 incorrect denials out of a total of 597 servicemembers it sampled. However, FIOS could not review TIVAS compliance with SCRA requirements for all 597 servicemembers: only 55 servicemembers requested the benefit, and only 37 were actually eligible. Therefore, FIOS could not test whether the TIVAS complied with SCRA requirements for 542 of the servicemembers in its sample

⁸ FIOS determined that 18 borrowers were not eligible to receive the SCRA benefit, including 11 borrowers who were correctly denied the benefit by the TIVAS and 7 who were incorrectly granted the benefit. Of the 37 who were eligible, 3 were incorrectly denied the benefit.

because those servicemembers had not requested SCRA benefits. To be eligible for the SCRA benefit and subject to review by FIOS, servicemembers had to request the benefit and provide supporting documentation (a copy of military orders). Although the results of the four program reviews should not have been combined, following the approach FIOS used in the program reviews would result in 3 incorrect denials for 37 eligible borrowers it tested, which would equate to an 8 percent incorrect denial rate. However, due to the acceptance sampling design and the few eligible borrowers tested, it was not appropriate to report an aggregate incorrect denial rate.

FSA Revised Procedures for Ensuring Eligible Servicemembers Receive SCRA Benefits

In May 2014, FSA waived the documentation requirement (that is, a request for SCRA benefits and a copy of military orders) for its loans and required the TIVAS to match their loan portfolios to the Defense Manpower Data Center database. The match identifies potentially eligible servicemembers and grants them the SCRA benefit.⁹ TIVAS are required to provide the SCRA benefits to a borrower with an active duty status end date that is no more than 180 days in the past according to the Defense Manpower Data Center database. The TIVAS were required to implement this database match on loans as of July 2014 and are to be reimbursed for their efforts to conduct the match and provide the benefit, as well as for outreach activities to servicemembers.

Conclusion

Based on our review, our overall conclusions are (1) the sampling designs were not adequate to project the extent of SCRA compliance or noncompliance, (2) we cannot render an opinion on the accuracy of the Department program reviews due to errors we identified, and (3) the Department's press release is not supported by the work the Department performed and is inaccurate. However, the control requiring the TIVAS match with Defense Manpower Data Center, if implemented properly, should have corrected this problem as of July 2014. FSA did not make any effort to require the TIVAS to identify and correct all potential instances of incorrect denials of the SCRA interest rate cap.

⁹ This requirement was not initially applied to Navient because at the time it was still under investigation by the Department of Justice, but was implemented effective October 31, 2014.