STUDENT BORROWER PROTECTION CENTER

MEMORANDUM

DATE: January 27, 2023

TO: Interested Parties
FROM: Student Borrower Protection Center

RE: **Defaulted Borrowers Must Be Included in the Income-Driven Repayment Account Adjustment**

This memorandum urges the U.S. Department of Education (ED) to reconsider its exclusion of periods of time in default from the one-time Account Adjustment, which ED announced as a remedy for borrowers who have been steered into forbearance or otherwise knocked off course from IDR cancellation. While we applaud ED's clarification in its January 2023 Notice of Proposed Rulemaking (NPRM) that the IBR statute permits borrowers in default to make payments under that plan, the Account Adjustment itself must be expanded to include periods of time in default. As is detailed below, ED's remedy to a decade of servicer misconduct is incomplete as long as the defaulted borrowers most harmed by forbearance steering are excluded from the Account Adjustment. ED's failure to fully remedy these harms would be an unforced error as the Secretary's discretionary authority to compromise and modify federal student loan debt is expansive enough to bring periods of default within the scope of the Account Adjustment and existing IDR statutory authority is broad enough to include time in default.

Background

On April 19, 2022, the Biden Administration announced that it would remedy decades of student loan servicer misconduct and administrative failures through a one-time Account Adjustment for borrowers improperly placed into forbearance instead of an IDR plan or otherwise denied cancellation due to inaccurate IDR tracking. In its announcement, ED admitted, and sought to remedy, that its agents—the loan servicing companies charged with providing borrowers with clear and accurate information about options for staying out of delinquency—had steered borrowers in financial distress into periods of forbearance when they were eligible for IDR plans with monthly payments as low as zero dollars.[1] The Department further admitted that "[a] borrower advised to choose forbearance—particularly long-term consecutive or serial uses of

[1] Press Release, U.S. Dep't of Educ., *Department of Education Announces Actions to Fix to Longstanding Failures in the Student Loan Programs* (April 19, 2022), https://www.ed.gov/news/press-releases/department-education-announces-actions-fix-longstanding-failures-student-loan-programs.

forbearance—can see their loan balance and monthly payments grow due to interest capitalization and lead to delinquency or default."[2]

For thirty years, borrowers with federal student loans have been entitled to pursue debt cancellation through IDR. While 4.4 million borrowers have been in repayment for 20 years or longer, half had loans that were delinquent or in default,[3] and as of 2022, only 132 had received the promised cancellation.[4] As the Government Accountability Office found in 2022, this discrepancy is due in part to failures by ED and its servicers to communicate IDR forgiveness eligibility requirements to borrowers, including that periods of time in forbearance do not count.[5] Notably, 2 million of these borrowers who have been in repayment long enough to qualify for IDR forgiveness are in default and thus ineligible for the Account Adjustment.[6]

ED's decision to implement its Account Adjustment plan is based on FSA reviews finding that "loan servicers placed borrowers into forbearance in violation of Department rules."[7] ED also found that FSA's reviews were consistent with concerns raised by state attorneys general who, mere months before the Account Adjustment was announced, reached a $1.85 billion settlement agreement with Navient, the ED-contracted student loan servicer alleged to have steered IDR-eligible borrowers into financially-devastating periods of forbearance and, ultimately, default.[8] A lawsuit by the Consumer Financial Protection Bureau (CFPB) similarly alleging that ED's servicer steered borrowers' away from IDR plans and into higher-interest forbearances is ongoing.[9]

Despite the clear and recognized link between servicers steering borrowers into forbearance and those borrowers inevitably falling into default on their student loans, ED has decided that periods of time in default will not be credited with time towards IDR forgiveness under the Account Adjustment. By excluding time in default, the Account Adjustment falls short of its stated goal

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[2] *Id.*

[3] OFFICE OF U.S. SEN. ELIZABETH WARREN, Education Department Responses to Data Request by Senator Elizabeth Warren, April 2, 2021, https://www.warren.senate.gov/imo/media/doc/Education%20Department%20Response%20to%20Sen%20Warren%20-%204-8-21.pdf.

[4] Gov't Accountability Office, GAO-22-103720, *Federal Student Aid: Education Needs to Take Steps to Ensure Eligible Loans Receive Income-Driven Repayment Forgiveness* at 10 (2022), https://www.gao.gov/assets/gao-22-103720.pdf.

[5] *Id.* at 19.

[6] *Supra* note 3.

[7] *Supra* note 1.

[8] *Id.; See* 39 State Attorneys General Announce $1.85 Billion Settlement with Student Loan Servicer Navient, Navient AG Settlement, https://navientagsettlement.com/Home/portalid/0?portalid=0?portalid=0.

[9] Consumer Fin. Prot. Bureau, *CFPB Sues Nation's Largest Student Loan Company Navient for Failing Borrowers at Every Stage of Repayment*, Consumer Fin. Prot. Bureau (Jan. 18, 2017), https://www.consumerfinance.gov/about-us/newsroom/cfpb-sues-nations-largest-student-loan-company-navient-failing-borrowers-every-stage-repayment/.

of remedying the harms caused by servicers' forbearance steering and ignores the very borrowers ED has admitted were harmed by its servicers' violation of Department regulations.

<u>There are Sound Equitable Principles Supporting Inclusion of Time in Default in the Account Adjustment</u>

The Secretary asserts that the Account Adjustment will "begin to remedy" the harms suffered by federal student loan borrowers swept up in ED's administrative failures and its servicers' forbearance steering practices.[10] To do this, ED must credit borrowers' time in default towards IDR forgiveness through its Account Adjustment plan. As it stands, this initiative only just begins to remedy the historical failures of IDR that ED purportedly seeks to address. For the millions of borrowers with periods of time in default due to administrative failure and servicer forbearance misconduct, ED's attempt to redress that harm is no remedy at all.

Black's Law Dictionary defines "remedy" as "[t]he means of enforcing a right or preventing or redressing a wrong; legal or equitable relief."[11] In *Marbury v. Madison*, Chief Justice Marshall established that where a legal right exists, it is "a general and indisputable rule" that there is also a legal remedy for its violation.[12] The Supreme Court has elaborated on this principle throughout its history, holding generally that the nature of a remedy should be determined according to the nature of the injury suffered.[13] Expanding further on the appropriate scope of a remedy, the Court found that "the remedy does not 'exceed' the violation if the remedy is tailored to cure the 'condition that offends [the law].'"[14]

ED recognizes that its own findings of forbearance steering are "consistent with concerns raised by the Consumer Financial Protection Bureau and state attorneys general" which resulted in Navient's multi-state settlement, including $95 million in restitution payments to an estimated 357,000 federal student loan borrowers who were improperly placed in long term forbearances.[15] The Account Adjustment is a response to the same abuses that spurred the lawsuits seeking to remedy borrowers steered into forbearance. ED has also acknowledged that borrowers improperly placed in long-term or serial periods of forbearance can ultimately fall into default on their student loans. It follows that any complete answer to the problem of forbearance steering must include borrowers with periods of time in default.

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[10] *Supra* note 1.
[11] <u>Remedy</u>, Black's Law Dictionary (11th ed. 2019).
[12] *Marbury v. Madison*, 5 U.S. 137, 163 (1803).
[13] *Milliken v. Bradley*, 433 U. S. 267, 280 (1977).
[14] *Id*. at 282.
[15] *Supra* note 1.

<u>It is Legally Permissible for ED to Include Defaulted Borrowers in the Account Adjustment</u>

The law does not require ED to limit the Account Adjustment to this inadequate remedy. There are multiple paths ED can take to bring borrowers with periods of default due to administrative failure and servicer misconduct into the scope of the Account Adjustment. First, the Secretary's discretionary authority to compromise and modify federal student loan debt is broad and flexible enough to bring periods of time in default into the scope of the Account Adjustment. Further, under the IDR statutes and implementing regulations, time in default is analogous to borrowers' time in IDR-ineligible plans, such as extended repayment plans, or in forbearance, that have already been included in the Account Adjustment. Second, the Secretary has existing statutory authority to include borrowers' time in default in the Account Adjustment. If ED chooses not to exercise these authorities, the scandal of forbearance steering will continue to overshadow IDR's promise.

Compromise and Modification Authority

Although ED has not published the legal justification for the Account Adjustment, time that borrowers have spent in default is analogous to other time that the Secretary has temporarily modified to count towards cancellation. Through the Account Adjustment, ED will count borrowers' time in any repayment plan and in certain forbearances and deferments as IDR plan payments, qualifying for IDR cancellation after 20 or 25 years. Additional modification of time spent in default pursuant to the Secretary's authority at 20 U.S.C. § 1082(a)(4) is both legally permissible and consistent with the Account Adjustment's other modifications to statutory and regulatory provisions.

Defaulted borrowers can be brought within the scope of the Account Adjustment through the Secretary's broad statutory authority to compromise and modify federal student loan debts pursuant to the HEA.[16] The only limitation on this authority is that the Secretary must request review by the Attorney General of a settlement that exceeds $1,000,000.[17] The Secretary has promulgated regulations regarding his authority to compromise a debt, which were amended in 2016.[18] These specify that, "under the provisions of [the FCCS found at] 31 CFR part 902 or 903," the Secretary may "compromise a debt in any amount, or suspend or terminate collection of a debt in any amount" if these arise under the Title IV program.[19] While this provision contains a cross reference to the FCCS, this provision seems to clarify that the Secretary is not

[16] 20 U.S.C. § 1082(a)(4), (6).
[17] 20 U.S.C. § 1082(b).
[18] 34 C.F.R. § 30.70.
[19] 34 C.F.R. § 30.70(e)(1).

required to follow procedures outlined in the FCCS, which generally limits amounts that an agency can compromise without seeking approval from the Attorney General to $100,000.[20]

The Secretary may also "consent to modification, with respect to rate of interest, time of payment of any installment of principal and interest or any portion thereof, or any other provision of any note or other instrument" of any loan made under the Title IV program.[21] This authority is not limited by Congress' appropriations power, nor by the FCCS.[22] The Secretary has previously exercised this authority to modify borrowers' federal student loan balances to zero dollars.[23]

In the wake of the litigation and settlement agreement arising out of the multistate lawsuits against Navient's years of forbearance steering and ED's admission that its servicers ratcheted up borrowers' balances through this practice, the Secretary should use this expansive and discretionary authority to modify periods of default to count towards IDR cancellation during the Account Adjustment.

To the extent that ED recognizes any litigative risk in the matter of its servicers' forbearance steering practices, the Secretary's compromise and modification authority could be particularly appropriate as a means of fully resolving the issue of forbearance steering and making whole all of those borrowers harmed, including those with periods of time in default.

Exercising this authority, the Secretary can modify each month that a borrower has been in default to count as a qualifying month for the purposes of IDR cancellation. Under the Account Adjustment, ED has already modified the payment histories of borrowers with periods of time ineligible to count towards cancellation because of repayment plan type, periods of forbearance or deferment, and loan type. Extending this modification to include periods of time in default would make borrowers whole and restore the progress towards cancellation they would have accrued had they not been harmed by illegal or improper loan servicing.

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[20] The FCCS outlines procedures for compromise of loans above a certain dollar amount, while section § 30.70 provides that the Secretary has authority to compromise debts in "any amount." Additionally, § 30.70 was amended to reflect the Secretary's broader authority -- not to limit it, meaning a limiting reading would contract the regulation's underlying purpose. *See* Letter from Eileen Connor et al., Legal Servs. Ctr. of Harv. L. Sch., to Senator Warren (Jan. 13, 2020), https://static.politico.com/4c/c4/dfaddbb94fd684ccfa99e34bc080/student-debt-letter-2.pdf.pdf at 5.

[21] 20 U.S.C. § 1082(a)(4)

[22] *Supra* note 20 at 6.

[23] *Id*. at fn 21, citing *Carr et al. v. DeVos*, Case No. 19-cv-6597 (S.D.N.Y.), Dkt. No. 15-1 (Decl. of Cristin Bulman), 16 (Stipulation of Dismissal) (Secretary modified DLP and FFELP loans of Plaintiffs pursuant to 20 U.S.C. § 1082(a)(4) resulting in balances of $0.00).

The Secretary has existing statutory authority to include borrowers' time in default in Account Adjustment.

Neither the IBR or the ICR statute prohibits defaulted borrowers from benefiting from and enrolling in either plan. The IBR statute states that "a borrower . . . who has a partial financial hardship (whether or not the borrower's loan has been submitted to a guaranty agency for default aversion or had been in default) may elect, during any period the borrower has the partial financial hardship, to [pay the amount in the IBR formula]."[24] Regarding ICR, the HEA goes on to state that "[t]he Secretary may require any borrower who has defaulted on a loan made under this part to . . . repay the loan pursuant to an income contingent repayment plan."[25]

Further, the IBR statute allows time in default to count towards cancellation. This flexibility is most apparent in contrast to ICR language which explicitly excludes time in default from the calculation of time that counts towards cancellation and reads, "[i]n calculating the extended period of time for which an income contingent repayment plan under this subsection may be in effect for a borrower, the Secretary shall include all time periods during which a borrower of loans under part B [FFEL], part D [Direct], or part E [Perkins] [was not in default on any loan included in the ICR plan and made qualifying payments]."[26] In light of this early choice to address how time in default should be credited towards ICR cancellation, Congress' later silence on the issue in the IBR provisions suggests a legislative choice to clearly include time in default for IBR borrowers.

ED has acknowledged the flexibility inherent in the statute in its January 2023 Notice of Proposed Rulemaking, proposing to "[m]odify the IBR plan regulations in § 685.209 to clarify that borrowers in default are eligible to make payments under the plan."[27] And although the ICR statute may not permit time in default to count towards cancellation as clearly as its IBR counterpart, the language does not necessarily prevent a defaulted borrower enrolled in ICR from counting payments made prior to default and ICR enrollment towards cancellation.[28]

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[24] 20 U.S.C. § 1098e(b)(1)

[25] 20 U.S.C. § 1087e(d)(5)(B). The regulation goes further to allow the secretary to require a borrower repay a defaulted loan pursuant to IBR as well. 34 C.F.R. § 685.211(X)(X).

[26] 20 U.S.C. § 1087e(e)(7)

[27] 88 Fed. Reg. 1913 (Jan. 11, 2023) https://www.govinfo.gov/content/pkg/FR-2023-01-11/pdf/2022-28605.pdf

[28] 20 U.S.C. § 1087e(e)(7) reads that "the Secretary shall include all time periods during which a borrower of loans. . . is not in default on any loan that is included in the income contingent repayment plan" — this language does not necessarily exclude payments made on defaulted loans *outside* of the ICR repayment plan from counting towards cancellation.

The IBR and ICR statutes offer much more flexibility for defaulted borrowers than the implementing regulations would suggest.[29] Through the Account Adjustment, ED can and should use that flexibility to count defaulted time as IBR time qualifying for cancellation.

Conclusion

While the Adjustment offers an important lifeline to millions of borrowers, it will be incomplete as long as it denies credit to those who have spent time in default, particularly those borrowers inevitably driven to default by forbearance steering. That ED has declined to include periods of time in default in the Account Adjustment is perplexing given the appropriate modifications it has already made to eligibility requirements for IDR cancellation. The Secretary has already temporarily modified statutory or regulatory prohibitions on IDR for borrowers enrolled in improper repayment plans or with otherwise ineligible payment histories. He can and must waive the bar against periods of time in default counting towards IDR cancellation if the Department is to fully effectuate the Account Adjustment as a remedy to forbearance steering.

[29] Delivering on Debt Relief: Proposals, Ideas, and Actions to Cancel Student Debt on Day One and Beyond, Student Borrower Prot. Ctr. (Nov. 2020) at 86-87, https://protectborrowers.org/wp-content/uploads/2021/02/Delivering-on-Debt-Relief-Final.pdf#page=74.