Date of Hearing: April 24, 2017

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Matthew Dababneh, Chair
AB 38 (Mark Stone) – As Amended March 23, 2017

SUBJECT: Student loan servicers: licensing and regulation: Student Loan Servicing Act

SUMMARY: Changes the Student Loan Servicing Act (Act) authorizing the Commissioner of the Department of Business Oversight (DBO) to implement licensee requirements under the Act, as specified. Specifically, **this bill**:

1) Defines the term "Nationwide Multistate Licensing System and Registry" to mean certain systems of records, and the requirements of licensees, as specified.

2) Authorizes the Commissioner of DBO, for purposes of participating in the licensing system and registry, to waive or modify rules, regulations, orders and other requirements reasonably necessary.

3) Permits the Commissioner of DBO to use the registry to request information from the Department of Justice and other sources, as specified.

4) Requires the Commissioner of DBO to report on violations of the Act and other enforcement actions, as specified.

5) Includes within that category of electronic records a surety bond, rider, or endorsement.

6) Extends the time for a licensee to acknowledge the receipt of a qualified written request from five days to 10 days.

7) Increases the circumstances in which a person may be required to take an oath, thereby expanding the crime of perjury, imposing a state-mandated local program.

EXISTING LAW: AB 2251 (Stone), Chapter 824, Statutes of 2016, enacts the Student Loan Servicing Act, operative July 1, 2018, which establishes a new licensing law applicable to student loan servicers, administered by DBO.

FISCAL EFFECT: Unknown

COMMENTS: The Student Loan Servicing Act is intended to increase protections for student loan borrowers and allow for greater transparency of the actions of student loan servicers. The changes in the Act contained in this bill allow the Commissioner of DBO to implement the requirements of the Act more efficiently and effectively. According to the author's office:

> The Student Loan Servicing Act gave California the power to regulate student loan servicers and protect student loan borrowers. With its passage, California has provided national leadership in the student loan servicing arena with many states introducing similar bills after the act found success in California.
>
> AB 38 continues the last year's goals of increased transparency and protection for student loan borrowers. AB 38 allows for easier implementation for [DBO] and

increases transparency within an industry that often lacks readily available information.

With the amount of student debt quickly becoming a national crisis, California must continue to lead and protect its student loan borrowers.

Student loan options: There are four types of postsecondary education loans.

1) Direct Loans are federal loans made directly to borrowers by the Department of Education through the William D. Ford Federal Direct Loan Program.

2) Federal Family Education Loan Program (FFELP) loans were originated by private lenders and guaranteed by the federal government. Federal law ended new originations of FFELP loans in 2010 but many remain outstanding.

3) Federal Perkins Loans are co-funded by higher education institutions and the federal government and are originated and administered by the education institutions.

4) Private student loans are made by depository and non-depository financial institutions, states, institutions of higher education, and other entities. These loans and their servicing come with varying levels of consumer protections.

Student loan debt: Student loan debt is the second highest outstanding consumer debt in the United States, second only to mortgage debt. Nationwide student loan debt is $1.2 trillion with an average debt balance of $29,000. California ranks relatively well compared to the other states on the average student loan debt per student. However, even with a low ranking on the debt scale a California student will rack up an average of $21,383 in public education institution debt. Data is unclear on how much private education debt may add to the average per student but private education debt overall is on the rise from a $55.9 billion in 2005 to $140.2 billion in 2011 and, in large part, fueled by the reselling of loans on the secondary market in a system very similar to mortgage funding and asset backed securities (*The High Economic and Social Costs of Student Loan Debt*, CNBC. June 15, 2015). According to the Wall Street Journal, *Congratulations, Class of 2015: You're the Most Indebted Ever*, May 2015, not only is average debt rising but the number of students taking out loans is also on the rise with 71% of bachelor's degree recipients taking out loans, double the number two decades ago.

This growing trend toward increasing the use of loans for education financing is taking a toll on graduates. For example, homeownership rates are dropping among people under the age of 35. Some of this may be related to the fact that mortgage lenders must look at all sources of debt, including student loans and this debt can either delay homeownership or require the borrower to reduce their housing expectations. The National Association of Realtors has found that over half of potential first time buyers that are having trouble saving for a down payment for a house have trouble due to student loan debt. According to CNBC, student loan default rates stand around 13-15% with the average amount of default at $14,000 while the default rates for some private-for profit schools is at 30%. A recent report from the Wall Street Journal, *More Than 40% of Student Borrowers Aren't Making Payments*, April 7, 2016, found:

1) Forty percent of Americans who borrowed from the Government's main student-loan program aren't making payments or are behind on more than $200 billion owed.

2) One in six borrowers (3.6 million) were in default on $56 million in student debt.

3) Three million borrowers owing almost $110 billion were in forbearance or deferment.

The cost of education is obviously on the rise and loans are filling a greater portion of the financing options. As the use of loans increases the levels of student financial literacy remain for the most part, dismal. A decade ago the biggest obstacle for students entering college was the potential draw of credit card offers that could lead to thousands of dollars in debt. With rising college costs the addition of more student loans is adding tens of thousands of dollars in debt. Twenty somethings reaching for the dream of a bachelor's degree are able to run up massive debt with little understanding of how to even balance a checkbook. A survey on student loans by Citizens Bank reveals that recent college graduates are lacking in basic details about their loan debt. For example, 45% didn't know what percentage of their salary went to paying off their loans; another 37% were unaware of the interest rate on their loan; and 59% did not know how long it would take to pay off their loans.

Student loan servicing: The Consumer Financial Protection Bureau (CFPB) released a report, *Student Loan Servicing: Analysis of Public Input and Recommendations for Reform,* in September of 2015.

1) The report indicated that consumers with federal and private student loans report a range of problems around servicers making mistakes, records getting lost, payments being processed too slowly, or servicer personnel not having the latest information about a consumer's account. Borrowers report that these issues include:

   a) Poor customer service and bad information causing borrowers distress: Borrowers report problems accessing basic account information, receiving conflicting information about repayment programs and loan features, and receiving inaccurate billing statements. When errors occur, borrowers report problems getting them resolved and a lack of recourse.

   b) Servicing transfers leading to surprise fees and lost benefits: More than 10 million borrowers have had their servicer change in the past five years. Consumers and industry report, however, that servicing transfers can create confusion when companies have different policies and procedures related to payment posting, allocation, and processing, as well as the administration of certain borrower benefits. When servicers change, payments may be lost, consumers may incur surprise late fees, and processing problems and missing account records can knock borrowers off track on repaying their loans.

   c) Roadblocks to refinance keeping borrowers tied to high-rate loans: Borrowers seeking to refinance student loans often depend on their current servicer to provide accurate and timely information about how to pay off their student loans. Public comments from borrowers and from student loan refinancing companies describe payoff problems, including inaccurate payoff statements, surprise bills demanding extra payments, and customer service confusion that increases costs for borrowers, lenders, and servicers.

   d) Co-signer policies causing auto-defaults and borrower distress: Private student loan borrowers continue to report serious financial distress when a company unexpectedly puts their loan in default status. These borrowers report paying on time each month, only to discover that their loan has been placed into default and sent to a debt collector following the death or bankruptcy of a co-signer, causing damage to their credit.

e) Payment processing practices increasing fees and penalizing borrowers: Borrowers expect servicers to process monthly payments and apply them to the loans in their account correctly, in a timely manner and without needlessly increasing costs.

Technical problem: This bill creates confusion because it establishes conditions where the Commissioner of DBO decides who is exempted from the division by requiring special reports or answers in writing. The Commissioner of DBO can then decide an entity is not exempted and the burden of proof is then on the entity to prove the exemption. If an entity is refused an exemption, then all the requirements under the Student Loan Servicing Act would then apply to that entity (i.e. a bank). The author may wish to work with effected parties to clarify.

REGISTERED SUPPORT / OPPOSITION:

Support

California Association of Nonprofits

Opposition

None on file

Analysis Prepared by: William Herms / B. & F. / (916) 319-3081