Federal Regulators Shine a Spotlight on Private Student Loan Servicers

By David Elliott and Parris Bell Winter 2018

Uptick in Private Student Loan Litigation

The private student lending market is experiencing a surge in consumer litigation and enforcement actions. This is largely due to the Consumer Financial Protection Bureau's elevated interest in enforcing consumer protection statutes against private student loan servicers. Loan servicers – rather than loan originators – remain the target of the bulk of student loan litigation. Once originators provide the funds, they commonly fade into the background in terms of consumer interactions. As such, this article will primarily focus on litigation and enforcement actions surrounding private student loan servicing.

After the mortgage loan-servicing crisis, federal regulators, such as the Consumer Financial Protection Bureau ("CFPB" or "Bureau"), began cracking down on private student loan originators and servicers, hoping to avoid similar industry-wide devastation. In a 2016 study, the CFPB found that more than 8 million borrowers were in default on more than $130 billion in student loans. In an effort to stifle this trend, federal regulators are responding by closely examining student-lending practices in the federal and private student loan markets.

The Basics: Private Student Loan Lending

The private student loan market is a $108 billion dollar industry. Private education loans are primarily offered by banks, non-profits, and higher education institutions (including for-profit schools). The originating institution often bundles multiple private educational loans and sells them to a depositor. The depositor, in turn, sells the loans to various trusts, which employ student loan servicers. Private student loan lenders do not have the enforcement mechanisms that federal lenders have (i.e. wage garnishment) and are left with filing suit against the borrower as their only recourse for a defaulted student loan.

Private loan servicers are the bridge between originators and borrowers. Servicers communicate with borrowers, manage their accounts, process their monthly payments, and are generally responsible for loan collections. Correspondingly, servicers are the ripest targets for litigation when borrowers have grievances regarding student loan accounts.

Enter the Consumer Financial Protection Bureau

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") created the CFPB and gave it specific authority to examine and supervise private loan servicers and originators engaging in unfair, deceptive, or abusive acts, or practices that otherwise violate consumer financial laws. In 2013, the CFPB issued a larger participant rule that extended its supervisory authority to large market participants in the student loan servicing industry (i.e. those servicing over one million accounts). The CFPB estimates that the new rule captures between 71 percent and 94 percent of all student loan servicers under its supervisory purview. Since then, the Bureau has prioritized taking action against student loan servicers engaging in illegal servicing practices.

In October of 2017, the Bureau released its Annual Report of the CFPB Student Loan Ombudsman 2017 – highlighting the servicing failures reported by borrowers of private student loans.[1] From September 1, 2016 through August 31, 2017, the Bureau handled approximately 7,700 private student loan complaints. 61% of those complaints concerned consumers' experiences in dealing with lenders and servicers.

The leading reasons borrowers submitted private student loan complaints included:

- Limited options for payment relief during periods of financial stress;
- Difficulty accessing advertised loan benefits and protections;
- Inadequate explanations of how borrowers can successfully qualify for a cosigner release when servicers deny applications for cosigner release; and
- Servicers' failing to allocate payments according to borrowers' instructions when borrowers submit one payment intended to cover multiple private loans.

Common Types of Litigation Faced by Private Student Lenders and Servicers

Actions by consumers against private loan servicers and originators typically arise as: (1) counterclaims in collections actions by private lenders over defaulted payments, or (2) as consumer lawsuits (brought individually or as a class) alleging that servicers violated various federal and state consumer protection statutes through their loan servicing practices. The most common claims brought by borrowers against private loan originators and servicers are commenced under the Fair Debt Collection Practices Act and the Fair Credit Reporting Act.

Recently the CFPB has been using its enforcement authority to sue large actors in the private student lending industry in enforcement actions as well. Every publicly announced enforcement action by the CFPB relating to student loans has included counts pleading illegal unfairness, deception, or both.[2]

On November 27, 2017, President Donald Trump named Mick Mulvaney, current White House Office of Management and Budget Director, as acting director of the CFPB. Mulvaney's nomination was met with opposition. Challengers argued that the CFPB's deputy director, Leandra English, should have been named as acting director instead. Despite attempts to thwart his nomination, a U.S. District Judge ruled in favor of Mulvaney's service as the acting director on November 28, 2017, one day after his appointment. That same day, Mulvaney instituted a 30-day freeze on hiring, rulemaking, regulations, guidance, and payments to consumers out of the CFPB's civil penalties fund.

On January 10, 2018, a U.S. District Judge ruled for the second time against Leandra English's request to block Mulvaney's appointment. The CFPB has not experienced obvious changes to its policy or focus to date and only time will tell what impact Mulvaney's leadership will have on federal consumer protection measures, oversight, and the goals of the Bureau, but his appointment undoubtedly signals a less robust enforcement effort by the CFPB.

[1] www.consumerfinance.gov/data-research/research-reports/annual-report-cfpb-student-loan-ombudsman-2017/

[2] To read the full Student Loan Servicing Report, click here.

This section lists the most commonly litigated claims against private student loan originators and servicers, and addresses the most frequently asserted statute-specific defenses.

The Consumer Financial Protection Act (CFPA)

The CFPB typically brings enforcement actions under a combination of the applicable federal consumer protection statutes listed below and Dodd-Frank's Consumer Financial Protection Act of 2010 (CFPA).[3] The CFPA's prohibition on unfair and deceptive acts and practices ("UDAAP") is its chief enforcement mechanism.[4] In its revised Education Loan Exam Procedures, the CFPB explains how examiners review student loan servicers' compliance with federal consumer financial law. The CFPB listed the following as potentially unfair, deceptive, or abusive acts or practices with respect to lenders and servicers interactions with consumers:

- An act or practice is **deceptive** under the CFPA, if: [1] there is a representation or omission likely to mislead consumers acting reasonably under the circumstances; and [2] the representation or omission is material.
- An act or practice is **unfair** when: (1) it causes or is likely to cause substantial injury to consumers, (2) consumers cannot reasonably avoid the injury; and (3) the injury is not outweighed by countervailing benefits to consumers or to competition.
- An **abusive act or practice** is one that: (1) materially interferes with a consumer's ability to understand a term or condition of a consumer financial product or service; or (2) takes unreasonable advantage of: [a] a consumer's lack of understanding of the material risks, costs, or conditions of the product or service, [b] a consumer's inability to protect its interests in selecting or using a consumer financial product or service, or [c] the consumer reasonably relies on a covered person to act in the consumer's interest.[5]

The Bureau's Winter 2016 Supervisory Highlights includes the following examples of practices the CFPB considers unfair or deceptive in the student lending industry: the use of ambiguous "auto-default" clauses; failing to inform borrowers about the costs of forbearance agreements for co-signers; misrepresenting the borrower's ability to discharge student debt in bankruptcy; obscuring the applicability of late fees; and failing to provide borrowers with correct information required on tax filings to deduct student loan interest payments.[6]

Fair Debt Collection Practices Act (FDCPA)

The FDCPA protects consumers against abusive and deceptive practices by debt collectors.[7] FDCPA claims often arise in student loan litigation when servicers (or their agents) attempt to collect on debts that are time-barred, harass defaulted borrowers through their collections efforts, or fail to provide validation of debts.

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[3] 12 U.S.C. § 5531(a), 5536(a), 5564, and 5565.

[4] Sections 1036(a)(1) and 1036(a)(1).

[5] To read the CFPB's Education Loan Examination Procedures, click [here]().

[6] To read the Winter 2016 Supervisory Highlights, click [here]().

[7] Some states have adopted their own debt collection statutes providing additional protections to debtors with broader definitions that apply to creditors.

DEFENSES

Servicers: Courts have consistently held that when a loan servicer takes over an account before the loan is in default, the servicer is not a debt collector and is thereby exempt from FDCPA liability. In this situation, the servicer becomes a creditor collecting on its own debt. Accordingly, a plaintiff's failure to allege that an entity serviced a loan before default is fatal to a claim under the express language of the FDCPA. Servicing companies can, however, be subject to FDCPA liability if the loan was already in default at the time the servicing company acquired the account.[8]

Originators: A lender which originates a student loan is not a debt collector when it attempts to collect on a loan from the consumer if the lender originated the loan and the loan was not in default when the lender obtained it.[9]

Spokeo Standing: In *Lyshe v. Levy*, the Sixth Circuit examined Plaintiff's standing to bring an FDCPA claim in light of Spokeo.[10] The Court noted that the goal of the FDCPA is to eliminate abusive debt collection practices. The Sixth Circuit held that the harm alleged by Plaintiff – that he would have been required to visit a notary and contact the opposing party to obtain electronic copies of discovery – was not the type of harm the FDCPA was designed to prevent. Because this was not the type of abusive debt collection practice contemplated by the FDCPA, Plaintiff failed to allege a concrete harm and lacked Article III standing to sue.

Statute of Limitations: Actions not brought within one year of the last violation are time-barred.[11]

Fair Credit Reporting Act (FCRA)

The FCRA requires entities that furnish information to consumer reporting agencies (i.e. private student loan originators and servicers) to have reasonable written policies and procedures to ensure the accuracy of the information they provide to the agencies. When a consumer reporting agency notifies a furnisher of a consumer dispute, the FCRA requires the furnisher to perform a reasonable investigation of the dispute. FCRA claims frequently arise in student loan litigation when borrowers allege that servicers furnished inaccurate information to credit reporting bureaus, or that servicers failed to conduct the required investigation once notified of the borrower's dispute of information furnished to the credit bureaus.

DEFENSES

No Private Right of Action: The FCRA permits an individual to bring a claim under § 1681s-2(b) against a furnisher of information for failing to perform certain duties imposed on furnishers after they receive notice from a credit reporting agency. For a consumer to have a private right of action under the FCRA against a furnisher of information, it is a threshold requirement that the consumer must first notify a credit reporting agency of a dispute. Private lenders and servicers have a strong defense when the

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[8] *Mondonedo v. Sallie Mae, Inc.*, No. 07-4059-JAR, 2009 WL 801784, at *3 (D. Kan. Mar. 25, 2009).

[9] 15 U.S.C. § 1692a(6)(F); *Hudson v. Babilonia*, 192 F. Supp. 3d 274 (D. Conn. 2016).

[10] *Lyshe v. Levy*, 854 F.3d 855, 861 (6th Cir. 2017).

[11] 15 U.S.C. § 1692 *et seq*.

consumer brings a claim under the FCRA without first notifying the credit reporting agencies.[12] Notifying the servicer alone of the dispute is insufficient to trigger a private right of action. Once the borrower notifies the credit reporting agency of the dispute, the servicer's duty to conduct a reasonable investigation is then triggered by notice from one of the credit reporting bureaus. It is only upon a showing that the servicer failed to investigate and modify the inaccurate information that a servicer can potentially face FCRA liability.[13]

Spokeo Standing Defense to Negligent Noncompliance Claim: 15 U.S.C. § 1681o authorizes an award of "actual damages" sustained by the consumer as a result of the negligent failure to comply with the FCRA, however, a plaintiff cannot show "actual damages" if he was not harmed by a failure to conduct a reasonable investigation. The statute does not require a showing of actual damages to obtain punitive damages for willful FCRA violations, but regardless of the statute's scope, under *Spokeo*, a plaintiff must show some harm that is "fairly traceable" to the violation in order to have standing to sue under Article III of the Constitution.[14]

Statute of Limitations: A claim under the FCRA must be brought within the earlier of: (1) two years after the date the plaintiff discovers the violation that is the basis for FCRA liability, or (2) five years after the date on which the violation that is the basis for FCRA liability occurs.[15]

Truth in Lending Act (TILA)

The Truth in Lending Act imposes requirements on private educational loan lenders, including disclosure in writing of interest rates, repayment terms, fees, cost estimates, consumer rights, and information about federal student loan alternatives.[16] TILA claims often arise in student loan litigation when borrowers claim originators failed to provide them with the required disclosures at the time of signing the private loan agreements.

DEFENSES

Statute of Limitations: Any action brought under TILA must be brought within one year from the date of the occurrence of the violation.[17] In *Consumer Financial Protection Bureau v. ITT Educational Services*, Inc., the court declined to read an exception into the one-year statute of limitations imposed under TILA's civil liability provision for enforcement actions brought by the CFPB.[18]

Telephone Consumer Protection Act (TCPA)

Consumers frequently file suit or a counterclaim under the TCPA alleging that the servicer or its agent called them on their cell phones using an automatic telephone dialing system ("ATDS") and prerecorded or artificial voice, without their consent. Because phone calls are often the primary method of contact

[12] *See* 15 U.S.C. § 1681s-2.

[13] *Flax v. Navient Sols., Inc.*, No. CV MJG 16-1209, 2017 WL 1153889, at *5 (D. Md. Mar. 28, 2017).

[14] *Spokeo, Inc. v. Robins*, 136 S. Ct. 1540 (2016), *as revised* (May 24, 2016).

[15] 15 U.S.C. § 1681(p).

[16] 15 U.S.C. § 1601 *et seq.*; 12 C.F.R. § 1026.46-47 (2014).

[17] 15 U.S.C. § 1640(e).

[18] *Consumer Fin. Prot. Bureau v. ITT Educ. Servs., Inc.*, 219 F. Supp. 3d 878, 923 (S.D. Ind. 2015).

when an account falls behind, TCPA claims typically arise in student loan litigation when the servicer (or its agent) places a high volume of calls to the borrower. The TCPA provides for $500 per statutory violation (per call) and for up to $1,500 per violation if the violations were willful or knowing.

DEFENSES

Consent Defense: Student loan servicers and originators often obtain a borrower's cell phone number at various points throughout the life of the loan, including on credit applications and through consent-to-be-called provisions.[19] Prior express consent to call the number in connection with a particular debt, given by a person with authority to consent before calls are placed, is an affirmative defense to TCPA liability.[20] Having said this, special attention should be paid to a consumer's revocation of consent – as this could destroy a prior express consent defense.

Statute of Limitations: Actions not brought within four years from the date of the last violation are time-barred.[21]

Lack of Standing: In order to have standing to bring a claim under the TCPA, the plaintiff must be the subscriber or non-subscribing customary user of the called number.

Calls Were Not Placed by an ATDS: The TCPA defines an ATDS as equipment with "the capacity to store or produce telephone number to be called, using a random or sequential number generator and to dial such numbers.[22] Since the Federal Communications Commission issued its 2015 Declaratory Ruling and Order on the TCPA concerning autodialers, courts have consistently focused on the degree to which human intervention is involved at the time the call is launched in determining whether a calling system is an ATDS.[23] There is currently no bright line rule and the ATDS analysis is done on a case-by-case basis.

Breach of Contract

Consumers occasionally bring breach of contract claims against private loan servicers for failing to apply payments properly and timely, for failing to give proper notice of a servicing transfer, or for any other reason relating to the underlying contract.

DEFENSES

Consumers face two main obstacles when asserting a breach of contract claim against their loan servicer: *First*, there is a lack of privity between the servicer and the student borrower, as the servicer contracts with the lender, and the lender is the entity in privity with the borrower and the servicer. *Second*, the

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[19] *See In the Matter of Rules & Regulations Implementing the Tel. Consumer Prot. Act of 1991*, 23 F.C.C. Rcd. 559 (2008) (providing the listing of a number on the consumer's credit application as an example of prior express consent to be called).

[20] The Second Circuit has held that a party who provides their number as part of a contractual bargained-for-exchange cannot unilaterally revoke that consent. *Reyes v. Lincoln Auto. Fin. Servs.*, 861 F.3d 51, 56 (2d Cir. 2017), *as amended* (Aug. 21, 2017).

[21] 28 U.S.C. § 1658.

[22] 47 U.S.C. § 227.

[23] *See In the Matter of Rules & Regulations Implementing the Tel. Consumer Prot. Act of 1991 Am. Ass'n of Healthcare Admin. Mgmt. Am. Bankers Ass'n Coal. of Mobile Engagement Providers Consumer Bankers Ass'n Direct Mktg. Ass'n Paul D. S. Edwards Milton H. Fried, Jr., & Richard Evans Glide Talk, Ltd. Glob. Tel*link Corp. Nat'l Ass'n of Attorneys Gen. Prof'l Ass'n for*, 30 F.C.C. Rcd. 7961, 7974 ¶ 55, 64 (2015).

contract itself might not forbid the complained of practices, even though they may be considered deceptive, unfair, or abusive, and thus violative of consumer protection statutes.

Other General Defenses Private Student Lenders and Servicers Can Assert

Preemption

Federal statutes will preempt many statutory state law claims. This has proven a particularly effective defense when state law claims are predicated on conduct that could also underlie a FCRA action.

Standing

In *Spokeo, Inc. v. Robbins*, the Supreme Court considered the requirements for FCRA standing and concluded that a plaintiff cannot satisfy the standing requirements of Article III by alleging a "bare procedural violation that results in no harm."[24] Since *Spokeo*, defendants have successfully used the case's reasoning to defeat a plaintiff's standing under various consumer protection statutes.

RECENT CASES

Consumer Litigation

Humphrey v. Navient Solutions, Inc., No. 16-CV-370-JDP, 2017 WL 4083593, at *2 (W.D. Wis. Sept. 13, 2017).

Humphrey ("Plaintiff") filed suit alleging that Navient furnished inaccurate information that Plaintiff's accounts were past due to consumer reporting agencies. Plaintiff sued Navient under the Fair Credit Reporting Act 15 U.S.C. § 1681s-2(b), which requires a furnisher of credit information to take various actions when it receives notice from a consumer reporting agency of a consumer dispute about the accuracy of information the furnisher provided. At issue in *Humphrey* was the FCRA requirement that the furnisher must "conduct an investigation" about the dispute upon receipt of notice of the dispute from a consumer reporting agency.[25] A number of courts have held that a prerequisite to a 15 U.S.C. § 1681s-2(b) claim is a showing that the defendant provided false, misleading, or incomplete information. The courts so held because the FCRA's purpose is to protect consumers from the results of the compilation and dissemination of inaccurate credit information. In light of the statute's purpose, the credit information would necessarily first have to be inaccurate in order to establish an FCRA claim.

Plaintiff's Claim Failed for Lack of Standing: Navient argued that Plaintiff could not prevail on his claim unless he first showed that Navient furnished inaccurate information. In *Spokeo, Inc. v. Robbins*, the Court provided as an example of a bare procedural violation that results in no harm, a situation in which, "[A] consumer reporting agency fails to provide the required notice to a user of the agency' consumer information [but] that information [is] entirely accurate." In *Humphrey*, the Court held that pursuant to the reasoning in *Spokeo*, Plaintiff lacked standing to maintain a claim that Navient failed to conduct a reasonable investigation under the FCRA in the absence of showing that the failure to conduct an investigation harmed him. Each of Plaintiff's theories of harm were contingent upon a showing that

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[24] *Spokeo, Inc.*, 136 S. Ct. at 1547.

[25] 15 U.S.C. § 1681s-2(b)(1)(A).

Navient furnished inaccurate information, and in the absence of harm that could be traced to a failure to conduct a better investigation, the Court granted summary judgment to Navient.

Valletta v. Navient Corp., No. CV-16-01934-PHX-DGC, 2017 WL 1437563, at *1 (D. Ariz. Apr. 24, 2017).

James Valletta ("Plaintiff") filed a complaint alleging that Navient improperly reported his debt to credit bureaus resulting in a negative credit history, and that Navient harassed him regarding a student loan that he had already paid off. Based on these allegations, Plaintiff sought damages under the FDCPA. It is a threshold for FDCPA liability that the defendant qualifies as a debt collector under the statute. Because Navient became the loan servicer before the Plaintiff's loan was in default, it was not a "debt collector" under the FDCPA. The Court granted Navient's motion for summary judgment on Plaintiff's FDCPA claims.

Flax v. Navient Sols., Inc., No. CV MJG 16-1209, 2017 WL 1153889, at *5 (D. Md. Mar. 28, 2017).

Joshua Flax ("Plaintiff") alleged that Navient violated the FDCPA, FCRA, and several state consumer protection statutes in its servicing of three private educational loans originated by Navient. Plaintiff alleged that his father took out the loans in his name without his knowledge. The Court granted Navient's motion to dismiss Plaintiff's FCRA claim, finding that Plaintiff failed to present factual allegations establishing that he notified a credit reporting agency of a dispute or that a credit reporting agency provided notice to Navient to trigger an investigation of the account. Absent notification by the credit reporting agency, Navient's duty to investigate was not activated, and Plaintiff's FCRA claim failed accordingly. Plaintiff also alleged that Navient violated the FDCPA by failing to send him verification of the student loan debt pursuant to 15 U.S.C. § 1691(g), which requires written notice containing the details of the debt. The Court granted Navient's motion to dismiss Plaintiff's FDCPA claim as well, finding that Navient was a creditor collecting on its own debt without the aid of a third party, and was thereby not a debt collector under the statute. Plaintiff's statutory state law claims were premised on Navient's alleged disclosure of information in connection with the consumer transaction. The Court dismissed Plaintiff's state law claims after determining they were each preempted by the FCRA.

Somlar v. Nelnet Inc., No. 4:16-CV-01037-AGF, 2017 WL 35703, at *1 (E.D. Mo. Jan. 4, 2017)

Stuart Somlar ("Plaintiff") filed suit alleging that Nelnet violated provisions of the FDCPA and FCRA in its servicing of his student loans.[26] Plaintiff argued that Nelnet violated the statutes by failing to send validation that Plaintiff was disputing the accounts to any credit agency. Nelnet filed a motion to dismiss the complaint, arguing that Plaintiff failed to state a claim under either consumer protection statute. In response to the FDCPA claim, Nelnet argued that Plaintiff failed to adequately allege: (a) that Nelnet is a debt collector, (b) that Plaintiff timely disputed his debt, or (c) that Nelnet engaged in any collection activities in violation of the FDCPA. Because Plaintiff did not allege that his loans were in default at the time they were obtained by Nelnet, Plaintiff failed to make the required threshold showing that Nelnet was a debt collector for FDCPA liability. In response to Plaintiff's FCRA claim, Nelnet argued that Plaintiff lacked a private right of action under section 2(a) of the statute and failed to allege that he notified any consumer reporting agencies of a dispute. In order to create a private right of action against the furnisher of information (i.e. the loan servicer) under the FCRA, the consumer must first notify the credit reporting agency of a dispute. The Court dismissed Plaintiff's FCRA claim finding that he lacked a private right of action against Nelnet since he failed to allege that he notified a credit reporting agency of the dispute.

[26] 15 U.S.C. § 1692g(b); 15 U.S.C. § 1681s-2.

CFPB Enforcement Actions

Navient, the largest student loan servicer in the country, has been the prime target of numerous recent enforcement actions filed by the CFPB alleging that it obscured borrowers' rights in repaying their student debt. Navient, formerly part of Sallie Mae, services more than $300 billion in federal and private student debt, servicing the loans of more than 12 million borrowers. In the Bureau's October 2017 Report, Navient accounted for 4,030 (61%) of the 7,700 complaints against private student lenders and servicers submitted to the Bureau between September 1, 2016 and August 31, 2017.

Consumer Financial Protection Bureau v. Navient Corp., No. 3:17-CV-101, 2017 WL 3380530, at *1 (M.D. Pa. Aug. 4, 2017).

The Complaint

On January 18, 2017, the CFPB filed suit against Navient accusing the entity of taking shortcuts and deceiving consumers to save on operating costs throughout the repayment process. The CFPB charged that Navient obscured important information regarding income-based loan repayment plans, incorrectly applied and allocated payments, failed to act when borrowers complained, deceived borrowers regarding requirements to release loan co-signers, harmed the credit of disabled borrowers, and directed struggling borrowers into forbearance (an option that allows a borrower to stop making payments temporarily while interest continues to accrue). Specifically, the Bureau alleges that Navient violated the Dodd-Frank Act, the FCRA, and the FDCPA through its servicing activities. The CFPB estimates that Navient added up to $4 billion in interest charges to the principal balances of an "immense number of borrowers" who were enrolled in "multiple consecutive forbearances."[27]

Navient's Motion to Dismiss

In an attempt in March of 2017 to get the lawsuit dismissed, Navient alleged that the CFPB's structure – an independent agency with a director who can only be removed for cause – was unconstitutional. Navient also argued that the Bureau did not have the statutory authority to act against servicers under the CFPA because it was first required to engage in a rulemaking before initiating an enforcement action, and as such, Navient lacked fair notice of what the CFPA proscribes.

On September 4, 2017, a U.S. District Judge for the Middle District of Pennsylvania ruled that the CFPB can act against loan servicers without first adopting rules defining specific practices as unfair, deceptive, or abusive, pursuant to the Dodd-Frank Act. The judge noted that the Bureau was free to use litigation as its vessel to determine what practices are prohibited. The judge also rejected Navient's argument that the organizational structure of the Bureau was unconstitutional, citing to a 1935 U.S. Supreme Court ruling that an almost identical for-cause removal provision for members of the Federal Trade Commission was constitutional.[28] This case is the most recent addition to the lineup of U.S. District Court opinions affirming the Bureau's constitutionality.

Consumer Financial Protection Bureau v. National Collegiate Student Loan Trusts

[27] To read the Complaint, click here.

[28] *Humphrey's Ex'r v. United States*, 295 U.S. 602 (1935).

On September 18, 2017, National Collegiate Student Loan Trusts entered into a consent judgment with the CFPB over illegal student loan debt collection lawsuits.[29] The Trusts are one of the largest holders of private student-loan debt in the nation, made up of 15 trusts that hold $12 billion in private student loans originated by banks. According to court filings, at least $5 billion of that debt is in default. The Trusts were accused of suing consumers over private student loan debts that the Trusts either could not prove were owed or were time-barred from suit, and filing false and misleading affidavits to that effect in violation of the Dodd-Frank Act. The Trusts agreed to pay at least $19.1 million in redress to harmed consumers and civil money penalties in addition to temporarily halting much of its collection activity. The CFPB also ordered an independent audit of each of the 800,000 student loans in the Trusts' portfolio. Going forward, the Trusts and any company they hire will not be permitted to collect on any loan that they cannot first prove the borrower legally owes. Transworld Systems, the debt collector hired by the Trusts, will pay an additional $2.5 million pursuant to a separate consent order it entered into with the CFPB on September 18, 2017. The Trusts are having difficulty proving in court that they have legal paperwork showing ownership of the loans which were originally made by banks before being sold to investors. If loans end up needing to be written off as a result of the Trusts' inability to affirmatively prove the debts are owed, it could end up costing far more than the initial $21.6 million assessment.

One to Watch: Student Lending Industry Giant Fights Back

Navient Solutions, LLC. v. Krohn & Moss, LTD et al, 1:17-CV-01178

Navient filed a groundbreaking lawsuit against several Plaintiff's firms and their affiliated attorneys ("Defendants") on October 18, 2017, alleging that the entities engaged in RICO violations, fraud, and tortious interference with contract by recruiting borrowers to bring TCPA claims against it. In its Complaint, Navient charges that the Defendant attorneys have operated as an association to carry out a "scheme" seeking to defraud Navient out of millions of dollars and to inhibit its debt collecting operations. Navient alleges that Defendants executed the scheme through a "network of referral and fee-sharing arrangements," and have conspired to manufacture federal lawsuits while fraudulently concealing their scheme. Navient contends that the Defendants recruited borrowers in search of "debt-relief counseling" by misleading them into stopping payments on their loans and instead paying Defendants in an attempt to misuse the TCPA and other laws offensively to avoid their loan obligations. Once a consumer was recruited, Navient alleges that Defendants instructed the consumer to follow a script intended to induce calls from Navient in the hopes that the calls would form the basis for a TCPA claim. After the Defendants determined that Navient had made a sufficient number of calls, Navient claims that Defendants referred consumers to Krohn & Moss, Ltd. or the Law Offices of Ryan Lee, PLLC, which would then initiate legal actions in federal court or through arbitration. Navient further alleges that Defendants sent fraudulent communications to Navient, including forged letters, and instructed their clients to lie under oath to improve settlement leverage.

Navient declares that it has incurred substantial losses as a result of the scheme, including direct settlement payments, cancellation of hundreds of thousands of dollars in student loan debt, and the cost of attorneys' fees. Navient avers that the scheme also victimized consumers who followed Defendants' instructions to cease payments and suffered significant and lasting damage to their credit as a result. Navient contends that Defendants were motivated by the tremendous potential statutory damages under the TCPA, which provides for $500 in statutory damages per call placed, and up to $1,500 per call if the

[29] To read the Proposed Consent Judgment, click here.

violations were willful or knowing. Navient noted that attorneys frequently bring such claims in the form of class actions against large defendants and use the threat of potentially crippling damages as leverage to extract settlements for suits that may be of questionable merit. Navient claims that the Defendants in this case took the common practice a step further by actually manufacturing claims where none existed.

Each of the Defendants filed separate motions to dismiss Navient's Complaint for failure to state a claim upon which relief can be granted pursuant to Federal Rule of Civil Procedure (FRCP) 12 (b)(6). Defendants Michael Biancone & MB Investments moved to dismiss the Complaint on one additional ground, asserting that the Court lacks personal jurisdiction under FRCP 12(b)(2). In response, Navient filed a consolidated opposition to Defendants' motions to dismiss on December 22, 2017, restating the grounds for each of its claims against Defendants. On January 12, 2018, the Court denied each of the Defendants' motions to dismiss Navient's Complaint.

The case is still in the preliminary stages and is sure to bring added attention to Navient, which has recently been the primary target of consumer litigation and CFPB enforcement actions alike. It has the potential to drastically change the landscape of student loan litigation, by providing student lenders and servicers with an additional defense where Plaintiff's attorneys employ similar practices to those alleged in order to drum up litigation.

Preventative Measures Loan Servicers and Originators Can Take to Avoid Becoming Targets of Litigation

How to Avoid Litigation:

- **Management:** Have a system in place to ensure that loan servicers (and any hired third party collectors) comply with applicable federal laws and regulations, including: FCRA (Regulation V), FDCPA, "Privacy of Consumer Financial Information" (Regulation P), TILA (Regulation Z), Telephone Consumer Protection Act, USA PATRIOT Act, Equal Credit Opportunity Act (Regulations B and Z), Electronic Funds Transfer Act (Regulation E), and Servicemember's Civil Relief Act.
- **Respond to consumer complaints:** As a private loan originator or servicer, the client is the borrower. When the client does not feel heard, the client will complain to an entity that will listen: the CFPB. Servicers should implement robust quality assurance and compliance management functions to guarantee that individual issues identified by borrowers are evaluated, and to the extent related problems exist for other borrowers, servicers should have the information necessary to proactively identify and address issues.
- **Arbitration provisions:** Arbitration provisions should be included in originating documents for the consumer to sign. Should a dispute arise, arbitration is an effective way to efficiently litigate the case while avoiding the possibility of a protracted federal lawsuit.
- **General release and consent provisions:** Loan modifications and settlements present companies with an opportunity to negotiate favorable terms with the consumer. To limit exposure contractually, companies should add a general release of past claims provision for the consumer to sign at these negotiation stages.[30] These points of renegotiation are also an appropriate time

[30] Release provisions that unambiguously encompass all past claims relating to the parties' contractual relationship are regularly upheld. *See Baker Hughes Inc. v. S&S Chem., LLC*, 836 F.3d 554, 557–58 (6th Cir. 2016) (upholding release of claims provision in settlement agreement, finding the provision was "plainly broad enough" to encompass plaintiff's claims); *Sherrod v. Sch. Bd. of Palm Beach Cty.*, 550 F. App'x 809, 811 (11th Cir. 2013) (upholding release of claims provision in settlement

for companies to include consent-to-be-called provisions in the accompanying documents for the customer's signature.

- **Maintain good policies**: Companies should regularly review their policies and institute employee training each time a new policy is rolled out. The possibility of becoming involved in a class action can be avoided by having policies in place to catch mistakes when they occur. Class actions form when issues go unnoticed and impact multiple consumers.
- **Report account status accurately to credit reporting agencies:** Review policies and procedures to ensure accuracy and integrity in reporting of information furnished to consumer reporting agencies. If an error in reporting a borrowers' failure to satisfy payment obligations to a credit reporting agency occurs, make sure that the error is quickly corrected. It is essential that companies refrain from reporting any negative credit information without having proper documentation.
- **Document, document, and then document some more:** Maintaining solid documentation practices is the easiest preventative measure loan servicers and originators can take to prevent becoming the subject of a CFPB enforcement action or the defendant of a class action or of a counterclaim in a collections action. Judges have already dismissed dozens of lawsuits by private loan originators against former borrowers wiping out their debt because the originators lacked the proper documentation to prove ownership of the loans. An internal audit should be conducted to identify holes in the chain of title, and to attempt to procure the documentation showing the debt is outstanding. This will result in a net savings, enabling the servicer to collect on debts rather than having to write them off for failing to show the debt is actually owed.[31]
- **Bring collections actions within the statutory period:** There are time limits on how long private student lenders can sue to collect on the underlying debt. These time limits vary by state, but are usually between three and six years. One of the most common defenses in lawsuits filed by lenders to collect on outstanding debt is that the lender waited too long to sue. Verifying the timeliness of the collections action prior to commencing suit will preclude consumers from asserting a time-barred defense.
- **Keep records current and up-to-date to reflect payments received.** A common defense in suits by private lenders to collect on delinquent accounts is that the consumer paid the amount on the loan and it was never credited to their account. Consumers may also defend themselves on the ground that the private lender miscalculated the amount due. Implementing and maintaining a system of internal controls to ensure that loans are taken out of repayment as soon as they are paid off by the student can refute such a claim, avoiding costly litigation.
- **Delinquency prevention:** Engage in delinquency prevention to avoid having to sue to collect down the road. Examples of this include: allocating payments in a way that will keep the borrower from incurring late fees, contacting borrowers prior to the start of the repayment period to counsel them on repayment options and due dates, and keeping the borrower's contact information current in the system.

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agreement, finding that plaintiff entered into the agreement in exchange for consideration and the provision barred all claims arising out of the settled employment termination matter); *Beck-Ford Constr., LLC v. TCA Glob. Credit Master Fund, LP*, 240 F. Supp. 3d 1256, 1278–79 (S.D. Fla. 2017) (holding that plaintiff released and waived any claims based on conduct occurring prior to the execution of a credit card agreement containing an "all-encompassing" release of claims provision).

[31] Any affidavits to be used to show ownership must be signed by a witness with personal knowledge of the consumer's account records and debt. The CFPB has brought enforcement action alleging that affidavits were "false and misleading" where affiants claimed personal knowledge of the student loan debt that they did not actually have.

- **Use indemnity agreements:** Originators using third-party servicers should use indemnification agreements in which the servicer agrees to hold the originator harmless from liability for any deficiency in originating or servicing student loans.

Takeaway - Be Proactive

If originators and servicers of private student loans proactively take steps to protect themselves they can significantly reduce the risk of involvement in enforcement actions and consumer litigation. Steps:

- Regularly conduct internal audits to evaluate all of the risks and controls in the companies' student lending operations.
- Ensure compliance with applicable laws for all key areas, including: loan origination, account management, collections, and customer service.
- Monitor the CFPB's announcements for guidance on compliance and enforcement that might impact the companies' operations.

To discuss this further, please contact:

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