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**BUREAU OF CONSUMER FINANCIAL PROTECTION**

**12 CFR Part 1090**

**[Docket No. CFPB-2013-0005]**

**RIN: 3170-AA35**

# Defining Larger Participants of the Student Loan Servicing Market

**AGENCY:** Bureau of Consumer Financial Protection.

**ACTION:** Proposed rule; request for public comment.

**SUMMARY:** The Bureau of Consumer Financial Protection (Bureau or CFPB) proposes to amend the regulation defining larger participants of certain consumer financial product and service markets by adding a new section to define larger participants of a market for student loan servicing. The Bureau proposes this rule pursuant to its authority, under the Dodd-Frank Wall Street Reform and Consumer Protection Act, to supervise certain nonbank covered persons for compliance with Federal consumer financial law and for other purposes. The Bureau has the authority to supervise nonbank covered persons of all sizes in the residential mortgage, private education lending, and payday lending markets. In addition, the Bureau has the authority to supervise nonbank "larger participant[s]" of markets for other consumer financial products or services, as the Bureau defines by rule. The proposal (Proposed Rule) would identify a market for student loan servicing and define "larger participants" of this market that would be subject to the Bureau's supervisory authority.

**DATES:** Comments must be received on or before [**INSERT DATE 60 DAYS AFTER FEDERAL REGISTER PUBLICATION**].

**ADDRESSES:** Interested parties are invited to submit written comments electronically or in paper form. Because paper mail in the Washington, DC area and at the Bureau is subject to delay, commenters are encouraged to submit comments electronically. You may submit comments, identified by Docket No. CFPB-2013-0005 or RIN 3170-AA35, by any of the following methods:

- Electronic: http://www.regulations.gov. Follow the instructions for submitting comments. In general, all comments received will be posted without change to their content.
- Mail/Hand Delivery/Courier: Monica Jackson, Office of the Executive Secretary, Bureau of Consumer Financial Protection, 1700 G Street, NW, Washington DC 20552.

In addition, comments will be available for public inspection and copying at 1700 G Street, NW, Washington, DC 20552, on official business days between the hours of 10 a.m. and 5 p.m. Eastern Time. You can make an appointment to inspect the documents by telephoning (202) 435-7275.

All comments, including attachments and other supporting materials, will become part of the public record and will be subject to public disclosure. Submit only information that you wish to make available publicly. Do not include sensitive personal information, such as account numbers or Social Security numbers. Comments will not be edited to remove any identifying or contact information, such as name and address information, email addresses, or telephone numbers.

**FOR FURTHER INFORMATION CONTACT:** Christopher Young, Senior Counsel, (202) 435-7408, or Jolina Cuaresma, Attorney-Advisor, (202) 435-9212, Office of Supervision Policy, Bureau of Consumer Financial Protection, 1700 G Street, NW, Washington, DC 20552.

**SUPPLEMENTARY INFORMATION:**

## I. Overview

Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)[1] established the Bureau on July 21, 2010. Under 12 U.S.C. 5514, the Bureau has supervisory authority over all nonbank covered persons[2] offering or providing three enumerated types of consumer financial products or services: (1) origination, brokerage, or servicing of consumer loans secured by real estate, and related mortgage loan modification or foreclosure relief services; (2) private education loans; and (3) payday loans.[3] The Bureau also has supervisory authority over "larger participant[s] of a market for other consumer financial products or services," as the Bureau defines by rule.[4]

This Proposed Rule, if adopted, would be the third in a series of rulemakings to define larger participants of markets for other consumer financial products or services for purposes of 12 U.S.C. 5514(a)(1)(B).[5] The Proposed Rule would establish the Bureau's supervisory

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[1] Public Law No. 111-203 (codified at 12 U.S.C. 5301 *et seq*.).

[2] The provisions of 12 U.S.C. 5514 apply to certain categories of covered persons, described in subsection (a)(1), and expressly exclude from coverage persons described in 12 U.S.C. 5515(a) or 5516(a). "Covered persons" include "(A) any person that engages in offering or providing a consumer financial product or service; and (B) any affiliate of a person described [in (A)] if such affiliate acts as a service provider to such person." 12 U.S.C. 5481(6).

[3] 12 U.S.C. 5514(a)(1)(A), (D), (E). The Bureau also has the authority to supervise any nonbank covered person that it "has reasonable cause to determine, by order, after notice to the covered person and a reasonable opportunity . . . to respond . . . is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services." 12 U.S.C. 5514(a)(1)(C). In addition, the Bureau has supervisory authority over very large depository institutions and credit unions and their affiliates. 12 U.S.C. 5515(a). Furthermore, the Bureau has certain authorities relating to the supervision of other depository institutions and credit unions. 12 U.S.C. 5516(c)(1), (e). The Bureau notes that one of the Bureau's mandates under the Dodd-Frank Act is to ensure that "Federal consumer financial law is enforced consistently without regard to the status of a person as a depository institution, in order to promote fair competition." 12 U.S.C. 5511(b)(4).

[4] 12 U.S.C. 5514(a)(1)(B), (a)(2); *see also* 12 U.S.C. 5481(5) (defining "consumer financial product or service").

[5] The first two rules defined larger participants of markets for consumer reporting, 77 FR 42874 (July 20, 2012) (Consumer Reporting Rule), and for consumer debt collection, 77 FR 65775 (Oct. 31, 2012) (Consumer Debt Collection Rule).

authority over certain nonbank covered persons participating in a market for student loan servicing.[6]

The Bureau is authorized to supervise nonbank covered persons subject to 12 U.S.C. 5514 of the Dodd-Frank Act for purposes of: (1) assessing compliance with Federal consumer financial law; (2) obtaining information about such persons' activities and compliance systems or procedures; and (3) detecting and assessing risks to consumers and consumer financial markets.[7] The Bureau conducts examinations, of various scopes, of supervised entities. In addition, the Bureau may, as appropriate, request information from supervised entities without conducting examinations.[8]

The Bureau prioritizes supervisory activity at nonbank covered persons on the basis of risk, taking into account, among other factors, the size of each entity, the volume of its transactions involving consumer financial products or services, the size and risk presented by the product market in which it is a participant, the extent of relevant State oversight, and any field and market information that the Bureau has on the entity. Such field and market information might include, for example, information from complaints and any other information the Bureau has about risks to consumers.

The specifics of how an examination takes place vary by market and entity. However, the examination process generally proceeds as follows. Bureau examiners initiate an on-site

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[6] The Proposed Rule would describe one market for consumer financial products or services, which the Proposed Rule labels "student loan servicing." The proposed definition would not encompass all activities that could be considered student loan servicing. Any reference herein to "the student loan servicing market" means only the particular market for student loan servicing identified by the Proposed Rule.
[7] 12 U.S.C. 5514(b)(1).
[8] *See* 12 U.S.C. 5514(b) (authorizing the Bureau both to conduct examinations and to require reports from entities subject to supervision).

examination by contacting an entity for an initial conference with management, and often by also requesting records and other information. Bureau examiners will ordinarily also review the components of the supervised entity's compliance management system. Based on these discussions and a preliminary review of the information received, examiners determine the scope of an on-site examination and then coordinate with the entity to initiate the on-site portion of the examination. While on-site, examiners spend a period of time holding discussions with management about the entity's policies, processes, and procedures; reviewing documents and records; testing transactions and accounts for compliance; and evaluating the entity's compliance management systems. As with any Bureau examination, examinations of nonbanks may involve issuing confidential examination reports, supervisory letters, and compliance ratings.

The Bureau has published a general examination manual describing the Bureau's supervisory approach and procedures. This manual is available on the Bureau's website.[9] As explained in the manual, examinations will be structured to address various factors related to a supervised entity's compliance with Federal consumer financial law and other relevant considerations. On December 17, 2012, the Bureau released procedures specific to education lending and servicing for use in the Bureau's examinations.[10] If this Proposed Rule is adopted, the Bureau also plans to use those examination procedures in supervising nonbank larger participants of the student loan servicing market.

This Proposed Rule would establish a category of covered persons that are subject to the Bureau's supervisory authority under 12 U.S.C. 5514 by defining "larger participants" of a

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[9] CFPB Supervision and Examination Manual (October 1, 2012), *available at* http://www.consumerfinance.gov/guidance/supervision/manual/.

[10] CFPB Supervision and Examination Manual, Education Loan Examination Manual (December 17, 2012), *available at* http://files.consumerfinance.gov/f/201212_cfpb_educationloanexamprocedures.pdf.

market for student loan servicing.[11] The Proposed Rule pertains only to that purpose and would not impose new substantive consumer protection requirements. Nonbank covered persons generally are subject to the Bureau's regulatory and enforcement authority, and any applicable Federal consumer financial law, regardless of whether they are subject to the Bureau's supervisory authority.

## II. Summary of Proposed Rule

The Bureau's existing larger-participant rule, 12 CFR part 1090, prescribes various procedures, definitions, standards, and protocols that apply with respect to all markets in which the Bureau has defined larger participants.[12] Those generally applicable provisions, which are codified in subpart A, would also be applicable for the student loan servicing market described by this Proposed Rule. The definitions in § 1090.101 should be used, unless otherwise specified, when interpreting terms in this Proposed Rule.

As the Bureau has previously explained, it will include relevant market descriptions and larger-participant tests, as it develops them, in subpart B.[13] Accordingly, the Proposed Rule defining larger participants of the student loan servicing market would become § 1090.106 in subpart B.

The Proposed Rule would be the latest in a series of rules to define "larger participants" of specific markets for purposes of establishing, in part, the scope of coverage of the Bureau's nonbank supervision program. The Proposed Rule would define a student loan servicing market

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[11] The Bureau's supervision authority also extends to service providers of those covered persons that are subject to supervision under 12 U.S.C. 5514. 12 U.S.C. 5514(e); *see also* 12 U.S.C. 5481(26) (defining "service provider").
[12] 12 CFR 1090.100-103.
[13] 77 FR 42874, 42875 (Consumer Reporting Rule); 77 FR 65775, 65777 (Consumer Debt Collection Rule).

that would cover the servicing of both Federal and private student loans.[14] Under the Proposed Rule, "student loan servicing" would mean the collection and processing of loan payments on behalf of holders of promissory notes and, during periods when payments are deferred, maintaining of account records and communicating with borrowers on behalf of loan holders, as well as interactions with borrowers that facilitate such collection and processing of loan payments and maintaining of account records and communicating with borrowers. The Proposed Rule would also set forth a test that determines whether a nonbank covered person is a larger participant of the student loan servicing market.

To identify the larger participants of this market that would be subject to the Bureau's supervision authority, the Bureau is proposing a test based on the number of accounts on which an entity performs student loan servicing. The Proposed Rule would define the criterion "account volume," which reflects the number of accounts for which an entity and its affiliated companies were responsible as of December 31 of the prior calendar year.[15] An entity would be a larger participant if its account volume exceeded one million. As prescribed by existing § 1090.102, any nonbank covered person that qualified as a larger participant would remain a larger participant until two years after the first day of the tax year in which the person last met the applicable test.[16]

Pursuant to existing § 1090.103, a person would be able to dispute whether it qualifies as

[14] As discussed below, student loans include those under Title IV of the Higher Education Act of 1965, 20 U.S.C. 1070 *et seq.*, and those that are otherwise extended to a consumer in order to pay post-secondary education expenses.
[15] Although the Bureau proposes to use account volume as the criterion for the student loan servicing market, that criterion is not necessarily appropriate for any other market that may be the subject of a future rulemaking. As the Bureau explained in the Consumer Reporting Rule and the Consumer Debt Collection Rule, the Bureau expects to tailor each test to the market to which it will be applied. 77 FR 42874, 42876; 77 FR 65775, 65778.
[16] 12 CFR 1090.102.

a larger participant in the student loan servicing market. The Bureau would notify an entity when the Bureau intended to undertake supervisory activity; the entity would then have an opportunity to submit documentary evidence and written arguments that it was not a larger participant. Section 1090.103(d) provides that the Bureau may require submission of certain records, documents, and other information for purposes of assessing whether a person is a larger participant of a covered market; this authority would be available to the Bureau for facilitating its identification of larger participants of the student loan servicing market, just as in other markets.

## III. Legal Authority and Procedural Matters

### *A. Rulemaking Authority*

The Bureau is issuing this Proposed Rule pursuant to its authority under: (1) 12 U.S.C. 5514(a)(1)(B) and (a)(2), which authorize the Bureau to supervise larger participants of markets for consumer financial products or services, as defined by rule; (2) 12 U.S.C. 5514(b)(7), which, among other things, authorizes the Bureau to prescribe rules to facilitate the supervision of covered persons under 12 U.S.C. 5514; and (3) 12 U.S.C. 5512(b)(1), which grants the Bureau the authority to prescribe rules as may be necessary and appropriate to enable the Bureau to administer and carry out the purposes and objectives of Federal consumer financial law, and to prevent evasions of such law.

### *B. Proposed Effective Date of Final Rule*

The Administrative Procedure Act generally requires that rules be published not less than 30 days before their effective dates.[17] The Bureau proposes that the final rule arising from this Proposed Rule would be effective at least 60 days after publication.

[17] 5 U.S.C. 553(d).

## IV. Section-By-Section Analysis

*Subpart B—Markets*

Section 1090.106—Student Loan Servicing Market

Proposed § 1090.106 relates to student loan servicing. Servicing, in general, is the day-to-day management of loans on behalf of loan holders. Servicers' duties typically include, for example, maintaining account records, billing borrowers for amounts due, collecting and allocating payments, reporting to creditors or investors, and pursuing collection and loss mitigation activities with respect to delinquent borrowers. The student loan servicing market is comprised of entities that service Federal and private student loans that have been disbursed to pay for post-secondary education expenses.[18] Students may obtain Federal student loans to fund their own post-secondary education expenses; a parent or guardian of a student may also obtain certain Federal student loans to fund that student's post-secondary education expenses.[19] A private student loan may be available to any individual willing to help secure funding for post-secondary education expenses.

Servicers handle three main types of post-secondary education loans on which borrowers still have outstanding balances; only two of these categories of loans are still available for new originations. First, some outstanding loans were made under the Federal Family Education Loan Program (FFELP).[20] FFELP loans were funded by private lenders, guaranteed by State

[18] Throughout this notice of proposed rulemaking, the terms "student loan" and "post-secondary education loan" are used interchangeably.
[19] *See* 20 U.S.C. 1078-2 (describing the PLUS program which, among other things, permits parents to obtain loans to pay for the cost of their children's education). A borrower who has one or more outstanding student loans may sometimes take out a new loan to refinance and consolidate those existing student loans. For purposes of the Proposed Rule, such a refinancing would also be considered a student loan.
[20] 20 U.S.C. 1078(b), (c).

governmental or not-for-profit entities, and reinsured by the Federal government. These loans are either serviced by the loan holders themselves or serviced pursuant to contracts with the loan holders. FFELP loans constituted the vast majority of Federal student loans before 2010. Second, pursuant to the 2010 SAFRA Act, FFELP ended and the Department of Education became the primary lender for Federal student loans, providing loans directly to borrowers under the William D. Ford Federal Direct Loan Program.[21] Direct loans are serviced by entities that contract with the Department of Education pursuant to Title IV of the Higher Education Act.[22] These entities are known as Title IV Additional Servicers (TIVAS).[23] Third, the student loan market includes private student loans, made without Federal involvement. Private student loans are usually serviced by the originating institutions, by the TIVAS, or by other nonbank entities.

The student loan servicing market includes fewer than 50 nonbanks, and the market is heavily concentrated at the upper tier.[24] As measured either by unpaid principal balance or by

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[21] *See* Public Law 111-152, §§ 2101-2213, 124 Stat. 1071 (2010). The Direct Loan Program actually began in 1992, *see* Public Law 102-325, 106 Stat. 569 (1992), but Federal Direct loans constituted only a small portion of Federal student lending before the enactment of the SAFRA Act in 2010. Two additional Federal programs under Title IV also authorize student loans. One offers grants to those who pledge to become teachers. If the recipients do not become teachers, then the disbursed funds are converted from grants to loans. *See* 20 U.S.C. 1070g *et seq.* A second finances loans made directly by certain post-secondary education institutions through their financial aid offices. *See* 20 U.S.C. 1087aa *et seq.*

[22] 20 U.S.C. 1087f(b).

[23] Most of the initial Direct loan servicing business went to one entity: Affiliated Computer Services, Inc. (ACS). As the Department of Education began contracting with additional servicers, those additional servicers became Title IV additional servicers. In order to avoid confusion, when the Bureau uses the term TIVAS, the Bureau means to refer also to ACS, the original servicer of Federal Direct loans.

[24] The Bureau has estimated entity-level data for student loan servicers as of December 31, 2012, based mainly on the 2012 Student Loan Servicing Alliance (SLSA) Servicing Volume Survey, to which most servicers reported data as of December 31, 2011. To construct these estimates, the Bureau augmented the data from SLSA's Servicing Volume Survey in several ways. 1) For the servicers that elected not to report their servicing information to SLSA, the Bureau estimated their servicing volume using Department of Education reports, shareholder presentations, and other market information. 2) The Bureau forecasted the growth of the largest student loan servicers' portfolios of Federal Direct loans on the basis of the overall growth in Federal Direct loans of 11.8 percent in 2012. *See* U.S. Department of Education, Federal Student Aid Annual Report, p. 2 (2012). 3) The Bureau accounted for publicly reported market changes, including the Department of Education's borrower volume reallocations. 4) The Bureau also included in its estimate of a servicer's volume the borrowers for whose loans the servicer performs subservicing

number of borrowers with loans being serviced, five nonbanks, the TIVAS, account for between approximately 67 percent and 88 percent of activity in the market.[25] There are only a few nonbanks in the middle tier of this market, each with slightly greater than 1 percent market share. Many of these firms service loans placed with them by smaller nonbanks that are in the lowest tier of the market.[26] Finally, the lowest tier of the market has a few dozen smaller nonbanks, each of which has only a fraction of a percent in market share.[27] Many of these smaller nonbanks are not-for-profit entities run by States, and at least half of them contract to other firms the servicing of the loans for which they have servicing rights. Entities in the middle tier of the

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under contract with other servicers. The results of these calculations are entity-level estimates of total unpaid principal balance, borrower volume, and loan volume. These estimated data are cited hereinafter as "2012 SLSA Servicing Volume Survey, augmented by CFPB estimates." Depository institutions and credit unions also service student loans, although they would not be covered under this Proposed Rule.

[25] *See* 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates. As discussed below, the Bureau proposes to use account volume as the criterion that would determine whether an entity is a larger participant of the student loan servicing market. However, the Bureau does not have data directly on servicers' account volume, as the Proposed Rule would define the term. The Bureau has therefore estimated market share on the basis of both unpaid principal balance and number of borrowers.

For either method, the Bureau's data source presents potential uncertainties that make it difficult to produce precise market-share figures. Accordingly, the Bureau presents only a range of market-share estimates. The lower end of the range reflects the Bureau's estimate of market share on the basis of unpaid principal balance, using the Bureau's estimate of $1.1 trillion in outstanding student loan debt as the denominator. However, the Bureau believes SLSA's data may underestimate the amount of unpaid principal balance being serviced by the TIVAS. In particular, SLSA's data include the aggregate unpaid principal balance being serviced by both banks and nonbanks. For this reason, the actual market share of TIVAS, calculated on the basis of unpaid principal balance as a proportion of the balance serviced by nonbank participants in the student loan servicing market, may be larger than the lower end of the Bureau's range. The upper end of the presented range is the Bureau's estimate of market share on the basis of number of borrowers. The Bureau believes SLSA's data may underestimate the total number of borrowers in the market; the actual market share of the TIVAS may therefore be smaller than the Bureau's estimate. However, the Bureau does not expect these possible uncertainties regarding market structure to alter its conclusions about the operation of the Proposed Rule. As discussed below, the approximately seven entities that would qualify as larger participants under the Bureau's proposed test engage in substantially more market activity than the next largest participants, regardless of the details of how participation is assessed.

[26] *See* HCERA/SAFRA - Not-For-Profit (NFP) Servicer Program documentation, as of Dec. 6, 2012 (showing firms that contract servicing rights to other entities), *available at* https://www.fbo.gov/spg/ED/FSA/CA/NFP-RFP-2010/listing.html.

[27] *See* 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

market conduct most of this subcontracted servicing.[28]

Outstanding student loan debt—measured by unpaid principal balance at approximately $1.1 trillion as of the end of 2012—is the largest category of non-mortgage debt in the United States.[29] Published tuition and fees at public four-year institutions have increased on average at an annual rate of 5.2 percent per year above the general rate of inflation over the past decade.[30] In light of the rising cost of obtaining post-secondary education, American consumers have increasingly turned to student loans to bridge the gap between personal and family resources and the total cost of education. In fact, from the academic year 2001-2002 to 2011-2012, the average total borrowing per student increased by 55 percent.[31] The average student loan debt for 2011 graduates was $22,900.[32] During the last decade, a greater proportion of Americans than ever before pursued post-secondary education; from fall 2000 to fall 2010, the number of undergraduate students increased by 45 percent.[33] Thus, student loans are not only essential for

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[28] *See* HCERA/SAFRA - Not-For-Profit (NFP) Servicer Program documentation, as of Dec. 6, 2012 (showing firms that contract servicing rights to other entities), *available at* https://www.fbo.gov/spg/ED/FSA/CA/NFP-RFP-2010/listing.html.

[29] As of September 30, 2012, the total Federal student aid loan portfolio amounted to $948 billion. U.S. Department of Education, Federal Student Aid Annual Report, p. 2 (2012), *available at* http://www2.ed.gov/about/reports/annual/2012report/fsa-report.pdf. The Department of Education and the Bureau have together estimated that American consumers owe more than $150 billion in outstanding private student loans. Consumer Financial Protection Bureau & Department of Education, Private Student Loans, p. 17 (Aug. 29, 2012) (report to the Sen. Comm. on Banking, Housing, and Urban Affairs, the Sen. Comm. on Health, Education, Labor, and Pensions, the H. Comm. on Financial Services, and the H. Comm. on Education and the Workforce), *available at* http://files.consumerfinance.gov/f/201207_cfpb_Reports_Private-Student-Loans.pdf. The Federal Reserve Bank of New York, using different data and methodology, separately estimates that outstanding student loan debt was $966 billion at the end of 2012. *See* Federal Reserve Bank of New York, Quarterly Report on Household Debt and Credit, p. 3 (Feb. 2013), *available at* http://www.newyorkfed.org/research/national_economy/householdcredit/DistrictReport_Q42012.pdf

[30] College Board Advocacy & Policy Center Report, Trends in College Pricing 2012, p. 7 (Oct. 2012).

[31] College Board Advocacy & Policy Center, Trends in Student Aid 2012, p. 4 (Oct. 2012).

[32] As reported in *Number of the Week: Class of 2011, Most Indebted Ever*, Wall Street Journal, May 7, 2011.

[33] College Board Advocacy & Policy Center, Trends in College Pricing 2012, p. 4 (Oct. 2012).

many students to obtain post-secondary education; they are a significant part of the nation's economy.

Student loan servicers play a critical role in the student loan market. Student loan servicers manage interactions with borrowers on behalf of loan holders of outstanding student loans. Servicers receive scheduled periodic payments from borrowers pursuant to the terms of their loans and apply the payments of principal and interest and other such payments as may be required pursuant to the terms of the loans or of the contracts governing the servicers' work. Typically, student loan servicing also involves sending monthly payment statements, maintaining records of payments and balances, and answering borrowers' questions. When appropriate, servicers may also make borrowers aware of alternative payment arrangements such as consolidation loans or deferments.

Student loan servicers also play a role while students are still in school. A borrower may receive multiple disbursements of a loan over the course of one or more academic years. Repayment of the loan may be deferred until some future point, such as when the student finishes post-secondary education. A student loan servicer will maintain records of the amount lent to the borrower and of any interest that accrues; the servicer may also send statements of such amounts to the borrower.

In addition, student loan servicers may collect payments and send statements after loans enter default. They may also report borrowers' account activity to consumer reporting agencies.

In short, most borrowers, once they have obtained their loans, conduct almost all transactions relating to their loans through student loan servicers.[34] The Proposed Rule would enable the Bureau to supervise larger participants of an industry that has a tremendous impact on the lives of post-secondary education students and former students, as well as their families.

Section 1090.106(a)—Market-Related Definitions

Unless otherwise specified, the definitions in § 1090.101 should be used when interpreting terms in this Proposed Rule. The Proposed Rule would define additional terms relevant to the student loan servicing market. These terms would include "student loan servicing," the term that delineates the scope of the identified market; the terms "post-secondary education expenses" and "post-secondary education loan"; and "account volume," which the Proposed Rule would use as the criterion for assessing larger-participant status. The Bureau seeks comment on each of the definitions set forth in the Proposed Rule and any suggested clarifications, modifications, or alternatives.

Account volume. As discussed below, the Bureau proposes to use account volume as the criterion that would determine whether an entity is a larger participant of the student loan servicing market. Proposed § 1090.106(a) would define the term "account volume" as the number of accounts with respect to which a nonbank covered person is considered to perform student loan servicing, as calculated according to instructions set forth in the proposed regulation and as discussed below.

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[34] Activities of this type constitute "servicing loans," a consumer financial product or service pursuant to the Dodd-Frank Act. *See* 12 U.S.C. 5481(15)(A)(i) (definition of "financial product or service," including "extending credit and servicing loans"); *see also* 12 U.S.C. 5481(5)(B) (definition of "consumer financial product or service," including financial products or services provided in connection with consumer financial products, like education loans, that are provided to consumers).

Account volume, as an initial matter, would be based on the number of students or prior students with respect to whom a covered person performs student loan servicing. For example, a servicer might service a post-secondary education loan made to a student at the beginning of the student's time in college and paid back over a number of years after the student completed college. As another example, a servicer might service a post-secondary education loan made to a parent of a student to fund that student's education expenses.[35] In each of these cases, the student whose post-secondary education expenses a loan funded would represent at least one account.

However, the Bureau is aware that in some situations, a student or prior student may correspond to more than one account at a given servicer. For example, if a nonbank covered person is servicing a loan to a student and also a loan to that student's parent, the servicer will maintain separate accounts for the two loans. The student and the parent will each receive separate statements regarding their loans, and the servicer will remit payments on the loans to their respective holders. As another example, a student may receive loans from two different originators; or a given originator may securitize loans to the student through two different securitization vehicles. These different holders of the student's loans may all retain the same servicer, who may maintain separate accounts for the different loans.[36] The servicer may send

[35] For example, under the Federal PLUS loan program, a student's parent or guardian may take out a loan to pay the student's expenses. *See* 20 U.S.C. 1078-2. In the private lending market, the Bureau understands that, subject to underwriting criteria, post-secondary education loans may be available to any person who wishes to support a student's education.

[36] In some instances, student loans that have been securitized in the secondary market may have a single loan originator but a separate legal holder for each loan. The Bureau understands that a securitization sponsor will typically use the same servicer for multiple securitizations.

the student one consolidated statement or multiple statements, depending on the circumstances and its practices; and the servicer will remit payments on the loans to different loan holders.

To take account of such possibilities, the Bureau proposes to count, as an account, each separate stream of fees to which a servicer is entitled for servicing a post-secondary education loan with respect to a given student or prior student.[37] The Bureau believes that student loan servicers are generally compensated, on a monthly basis, at a fixed rate for each account they handle. For Federal Direct loans and Federally-owned FFELP loans, this compensation structure is determined by contract with the Department of Education, and the average fee rate for 2013 is \$1.68 per month per account.[38] For loans held by private entities (both private loans and FFELP loans), the rate may vary depending on the contracts governing a given servicer's business. But the compensation structure appears to be common throughout the student loan servicing market.[39] The Bureau therefore expects that counting the number of streams of fees a servicer receives for servicing loans with respect to a given student will be an appropriate way to represent the scope of the servicer's business with respect to that student. The Bureau requests comment on the proposed method of counting accounts and suggested alternatives.

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[37] Ancillary fees (such as a late payment fee or a disbursement fee) that a servicer may receive in particular circumstances would not constitute a distinct stream of fees for performing student loan servicing.

[38] *See* Title IV Redacted Contract Awards, pp. 12-13, *available at* https://www.fbo.gov/spg/ED/FSA/CA/FSA-TitleIV-09/listing.html. The contract fixes monthly compensation on a per-borrower basis, and the compensation depends on the repayment status of each borrower being serviced. *See also* Student Aid Administration Fiscal Year 2013 Request at p. AA-15, *available at* http://www2.ed.gov/about/overview/budget/budget13/justifications/aa-saadmin.pdf. The Student Aid Administration estimates the average cost per-borrower (which is equivalent to a servicer's per-account compensation for purposes of this Proposed Rule) to be \$1.68 per month, based on the contractual prices and the proportion of borrowers with different repayment statuses. *Id.*

[39] The Bureau recognizes that some covered persons may not receive servicing fees on a per-account or per-month basis. For example, a covered person may perform student loan servicing for loans it originated or holds and may receive no servicing fee or may receiving servicing fees on a different basis. For a person that does not receive fees on a per-account basis, each student or prior student would still count as one account under the proposed definition of "account volume."

The number of accounts generally would be counted as of December 31 of the prior calendar year. In general, a loan originator may open an account for a borrower at the beginning of an academic year and then disburse funds for the student's expenses at various points throughout the year. An originator may allocate the borrower's account to a servicer at the beginning of the academic year, even though the originator will be making further disbursements. If a servicer is responsible for servicing loans with respect to a student as of December 31, the corresponding account would be included in the calculation of account volume.

The proposed definition would attribute to a covered person the sum of the number of accounts of the person and its affiliated companies. Under 12 U.S.C. 5514(a)(3)(B), the activities of affiliated companies are to be aggregated for purposes of computing activity levels for rules—like this Proposed Rule—under 12 U.S.C. 5514(a)(1). In the consumer reporting and consumer debt collection markets, the Bureau implemented the aggregation called for by 12 U.S.C. 5514(a)(3)(B) by prescribing the addition of all the receipts of a person and its affiliated companies to produce the person's annual receipts. The Bureau proposes to use a similar calculation in the student loan servicing market. The account volume for each nonbank covered person would be the sum of the number of accounts serviced by that nonbank covered person and the number of accounts serviced by all affiliated companies.

The proposed calculation would add together each account on which any affiliated company was providing student loan servicing, even if two affiliated companies were servicing post-secondary education loans with respect to the same student. For example, if two affiliated companies each serviced the loans of the same 10 students, those companies' account volume would nonetheless be 20.[40] The Bureau recognizes that other methods of aggregation may also be appropriate for this market. One alternative would be to add, for a group of affiliated companies, only those accounts that correspond to unique students. Thus, the account volume of the affiliated companies in the example above would be 10, rather than 20. If one of the two affiliated companies also serviced the loans of an eleventh student, with respect to whom the other affiliated company was not servicing any loans, the account volume for the companies would be 11—the 10 common accounts plus the one additional account. The Bureau seeks comments on each of these alternatives as well as other methods of aggregation that might be appropriate for this market.

The proposed definition of number of accounts would establish that each person's number of accounts as of the prior calendar year's December 31 would be aggregated together where two persons become affiliated companies in the middle of a year. The Proposed Rule would also provide that, where two affiliated companies cease to be affiliated companies in the middle of a year, the account volume of each would continue to include the other's number of accounts until the succeeding December 31.

Post-secondary education expenses. Proposed § 1090.106(a) would define "post-secondary education expenses" to include any of the expenses that are included as part of the cost of attendance of a student as defined in 20 U.S.C. 1087*ll*.

Post-secondary education loan. Proposed § 1090.106(a) would define the term "post-secondary education loan" to mean an extension of credit (a) that is made, insured, or guaranteed

[40] This example assumes that each company is receiving only a single stream of fees for each of the 10 students.

under Title IV of the Higher Education Act of 1965 (20 U.S.C. 1070 *et seq.*); or (b) that is extended to a consumer with the expectation that the funds extended will be used in whole or in part to pay post-secondary education expenses. As noted above, a loan may be made to a parent or guardian, or to another consumer, to fund the post-secondary education expenses of a student who is not a borrower of that loan. Such a loan would be within the defined category of post-secondary education loans. Loans for refinancing or consolidating post-secondary education loans would also be considered post-secondary education loans.

The term would exclude any extension of credit under an "open-end credit" plan, as defined by the Bureau's Regulation Z, 12 CFR 1026.2(a)(20). The term would also exclude loans secured by real property (such as residential mortgages or reverse mortgages). The Bureau recognizes that students and their families may use credit cards or home equity lines of credit to finance post-secondary education. However, for several reasons, the Bureau believes it may be appropriate to exclude these two categories of credit from the defined category of "post-secondary education loan." First, such loans are typically serviced by entities that focus on servicing credit card accounts or mortgage loans, respectively. Nonbank entities with such a focus ordinarily do not more broadly service loans used for education expenses. Second, pursuant to 12 U.S.C. 5514, the Bureau has supervisory authority, independent of this Proposed Rule, over nonbank covered persons that offer or service loans secured by real estate, including home equity loans or lines of credit. The Bureau also has supervisory authority regarding large portions of the credit card market, through its supervision of very large banks and credit unions and their affiliates pursuant to 12 U.S.C. 5515. Third, post-secondary education loans differ from these other credit products in various ways that may affect the conduct of servicing activities. For example, payments on a post-secondary education loan might not be required until four or more years after a borrower first receives such a loan.  In addition, because a post-secondary education loan is not open-end, a servicer is not handling revolving balances.  And, unlike a home equity line, a post-secondary education loan is typically not secured.

Student loan servicing.  Proposed § 1090.106(a) would define the term "student loan servicing" to mean receiving any scheduled periodic payments from a borrower pursuant to the terms of any post-secondary education loan, and making the payments of principal and interest and other amounts with respect to the amounts received from the borrower as may be required pursuant to the terms of the post-secondary education loan or of the contract governing the servicing; or, during a period when payment on a post-secondary education loan is deferred, maintaining account records for the loan and communicating with the borrower regarding the loan, on behalf of the loan's holder.  The proposed definition would also make clear that student loan servicing includes interactions with a borrower to facilitate such activities.[41]

Among the interactions that would constitute student loan servicing are activities to help delinquent borrowers avoid or prevent default on obligations arising from post-secondary education loans.  For example, a servicer might negotiate a modified payment plan for a borrower who cannot afford the payments scheduled under the original terms of the loan.  The Bureau regards default prevention activities as closely connected to the core aspects of student loan servicing—collecting and remitting payments and maintaining account records and communicating with borrowers.  The Bureau believes that many student loan servicers perform or subcontract default prevention activities for loans that they are servicing.  Significantly,

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[41] Interactions to facilitate the collection of payment from a borrower who has defaulted on a post-secondary education loan would also constitute student loan servicing.

efforts to prevent default on post-secondary education loans can help save borrowers from the serious consequences resulting from default, which can include the accrual of thousands of dollars in penalties and fees. Default on a Federal student loan has an additional deleterious consequence: a loan in default cannot qualify for income-based repayment, an alternative plan under which a low-income borrower may be able to reduce his or her monthly payments. Conducted in accordance with applicable law, default prevention can help protect consumers from certain risks. The Bureau expects to assess those risks in its supervision of larger participants of the student loan servicing market.

Section 1090.106(b)—Test to Define Larger Participants

Criterion. The Bureau has broad discretion in choosing a criterion for determining whether a nonbank covered person is a larger participant of a market within which the Bureau will conduct supervision. For any specific market, there might be several criteria, used alone or in combination, that could be viewed as reasonable alternatives. For the student loan servicing market, the Bureau is considering a number of criteria, including the total amount of unpaid principal balance on student loans handled by a servicer; the number of student loans serviced; and account volume, which, as discussed in the preceding subsection, refers to the number of accounts on which a person is considered to perform servicing. The Bureau invites comment on all three possible criteria as well as suggestions for other criteria that commenters believe might be superior.

Among these three, the Bureau proposes to use account volume as the criterion that determines which entities are larger participants of the student loan servicing market. A discussion of the definition of "account volume" is set forth above. The Bureau expects that account volume will be an appropriate criterion because, among other things, it is a meaningful measure of a student loan servicer's level of participation in the market and of the servicer's impact on consumers. First, the number of accounts on which a person performs servicing reflects the magnitude of the student loan servicer's interactions with consumers.[42] Each account represents a regular series of interactions with at least one consumer. Second, because account volume is defined, in part, in terms of how many streams of fees a servicer receives with respect to a given student, the account volume criterion would correlate to the amount of compensation a person receives for its student loan servicing (and also to receipts and other comparable measures of market participation).

The Bureau anticipates that account volume would be a relatively straightforward quantity for a student loan servicer to calculate, as the occasion to do so arises. Most market participants already assemble data on the number of loans they service and the number of borrowers of those loans. Many student loan servicers are members of the Student Loan Servicing Alliance (SLSA), a trade organization, and report the sizes of their servicing programs to SLSA annually on both those bases.[43] The Bureau's proposed account volume criterion would not necessarily be the same, for any particular servicer, as its number of loans or number of borrowers. But in general, because any student with respect to whom a nonbank covered person is performing student loan servicing corresponds to at least one account, a nonbank

[42] Although student loan servicers may interact with co-signers as well as borrowers, the Bureau believes that the former interactions are less frequent compared to servicers' interactions with borrowers. A servicer typically deals with a co-signer only when the borrower has failed to make payments. The Bureau expects that a servicer's level of interaction with borrowers who are current with their payments is about the same regardless of the balance on a loan or whether the loan is Federal or private. Servicers may have more intensive interactions with borrowers who are in default or near or at risk of default. For such borrowers, the character and quality of servicers' interactions may depend in part on the amount and type of the loans involved. However, the Bureau has no information suggesting that the proportion of loans in default varies substantially among servicers. Account volume should therefore appropriately reflect the comparative amount of consumer impact of various servicers.
[43] *See e.g.*, 2012 SLSA Servicing Volume Survey.

covered person's account volume is at least as large as that person's number of borrowers. Thus, any student loan servicer whose number of borrowers is above the threshold can expect that its account volume will also exceed the threshold. As discussed above, the detailed calculation of account volume generally reflects the number of accounts for which the servicer is receiving fees. The Bureau expects that servicers will readily be able to ascertain the latter figure because servicers are presumably invoicing and expecting receipts on that basis.

The Bureau does not have data directly on servicers' account volumes, as defined in this Proposed Rule. However, the Bureau expects that the numbers of borrowers that servicers report to SLSA will be an adequate proxy to enable the Bureau to analyze the market and select a threshold for larger-participant status. The Bureau believes that for most firms the number of accounts may not differ substantially, for purposes of this analysis, from the number of borrowers; and in general the Bureau estimates that a firm's number of accounts is no more than 50 percent greater than the number of borrowers it reports.[44] In addition, the Bureau has no reason to think the relationship between the number of accounts and the reported number of

[44] To reach this estimate, the Bureau notes that for Federal loans (which include Federal Direct loans and Federally-owned FFELP loans), each borrower corresponds to exactly one account, because the Department of Education compensates servicers based on their number of unique borrowers, rather than on their number of loans. *See* Title IV Redacted Contract Awards, Attachment A-6-- Servicing Pricing Definitions, *available at* https://www.fbo.gov/spg/ED/FSA/CA/FSA-TitleIV-09/listing.html. According to SLSA's data, Federal loans account for 30 million borrowers at the seven largest firms and 31 million borrowers market-wide. The remaining borrowers received private loans (which include non-Federally-owned FFELP loans and any other loan originated privately). The Bureau believes that the number of accounts corresponding to those borrowers is unlikely to exceed the corresponding number of loans reported by the various servicers, because the Bureau is not aware of any servicer receiving a separate fee for a unit smaller than a single loan. (The Bureau recognizes that because SLSA has not established standards, servicers may adopt slightly different methods for counting private loans and their borrowers, but the Bureau does not expect the variations to be substantial.) Thus, the number of accounts at the seven largest market participants is unlikely to exceed 75 million, the sum of 30 million borrowers of Federal loans and 45 million private loans. That figure is roughly 50 percent greater than 49 million, the total number of borrowers reported by the seven largest market participants. Similarly, the number of accounts market-wide is unlikely to exceed 80 million, the sum of 31 million borrowers of Federal loans and 49 million private loans.

borrowers varies substantially among servicers, particularly among the seven largest market participants.

As additional data for the student loan servicing market become available to the Bureau, the Bureau may consider other criteria and potential revisions to the criterion used in the Proposed Rule.

Threshold. Under the Proposed Rule, a nonbank covered person would be a larger participant of the student loan servicing market if the person's account volume exceeded one million. The Bureau estimates the proposed threshold would bring within the Bureau's supervisory authority about seven student loan servicers. These seven servicers are responsible for between approximately 71 and 94 percent of activity in the nonbank student loan servicing market.[45]

As discussed above, the Bureau does not have precise data on market participants' account volumes calculated in accordance with the proposed definition. However, the number of a servicer's accounts, under the proposed definition of "account volume," cannot be smaller than the number of borrowers whose loans it is servicing. In addition, the Bureau believes that in general the number of accounts should be no greater than the number of loans a servicer reports to SLSA. These two figures therefore provide outer bounds for a given servicer's number of accounts. The Bureau notes that according to the 2012 SLSA volume survey, seven nonbank entities each serviced the loans of more than one million borrowers. Those seven nonbanks would presumably be larger participants under the Proposed Rule. The next largest market

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[45] 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

participants report servicing the loans of approximately 300,000 borrowers each, and are unlikely to reach the one million threshold on the basis of account volume.[46]

The Bureau anticipates that the proposed account-volume threshold of one million would be consistent with the objective of supervising market participants that represent a substantial portion of the student loan servicing market and have a significant impact on consumers. The seven student loan servicers that would likely be larger participants based on the Bureau's proposed threshold collectively service the loans of approximately 49 million borrowers.[47] At the same time, this threshold would likely subject to the Bureau's supervisory authority only entities that can reasonably be considered larger participants of the market.[48]

The Bureau is also considering a lower or higher threshold. For example, an account-volume threshold of 200,000 might allow the Bureau to supervise between 15 and 18 entities, representing between approximately 74 and 99 percent of activity in this market.[49] However, the additional entities that would be included using this lower threshold are only a fraction of the size of the middle tier market participants.[50] In comparison, an account-volume threshold of three million would likely allow the Bureau to supervise only the five very largest participants in

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[46] As discussed above, the Bureau expects the number of accounts at a given servicer to be less than 50 percent larger than the number of borrowers. A firm with 300,000 borrowers is therefore unlikely to have more than 450,000 accounts. However, the Bureau's estimates do not take account of any servicers that do not report data to SLSA. These estimates also do not reflect any affiliations that may exist among market participants. If two student loan servicers that appear to be below the threshold given their reports to SLSA are actually affiliated companies, their aggregated account volume might render them both larger participants.

[47] 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

[48] The median number of borrowers with loans being serviced by a given entity is approximately 250,000. The median number of loans being serviced is 800,000. The median outstanding principal balance being serviced by a given entity is approximately $3.5 billion. 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

[49] 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates. Three entities reported servicing the loans of between 133,000 and 200,000 borrowers. Although these entities would be below a threshold of 200,000 borrowers, they might qualify as larger participants using a threshold of 200,000 accounts. As discussed above, the Bureau expects a firm's number of accounts to be no less than its number of borrowers and no more than 50 percent greater.

[50] 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

the market, representing between approximately 67 and 88 percent of activity in this market based on unpaid principal balance and number of borrowers.[51]

The Bureau seeks comment, including suggestions of alternatives, on the proposed threshold for defining larger participants of the student loan servicing market.

## V. Request for Comments

The Bureau invites comment on all aspects of this notice of proposed rulemaking and on the specific issues on which comment is solicited elsewhere herein, including on any appropriate modifications or exceptions to the Proposed Rule.

## VI. Section 1022(b)(2)(A) of the Dodd-Frank Act

### *A. Overview*

The Bureau is considering potential benefits, costs, and impacts of the Proposed Rule.[52] The Bureau requests comment on the preliminary analysis presented below as well as submissions of additional data that could inform the Bureau's analysis of the costs, benefits, and impacts of the Proposed Rule. In developing the Proposed Rule, the Bureau has consulted with or offered to consult with the U.S. Department of Education, the Federal Trade Commission, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the National Credit Union Administration,

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[51] 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

[52] Specifically, 12 U.S.C. 5512(b)(2)(A) calls for the Bureau to consider the potential benefits and costs of a regulation to consumers and covered persons, including the potential reduction of access by consumers to consumer financial products or services, the impact on depository institutions and credit unions with $10 billion or less in total assets as described in 12 U.S.C. 5516, and the impact on consumers in rural areas. In addition, 12 U.S.C. 5512(b)(2)(B) directs the Bureau to consult, before and during the rulemaking, with appropriate prudential regulators or other Federal agencies, regarding consistency with objectives those agencies administer. The manner and extent to which the provisions of 12 U.S.C. 5512(b)(2) apply to a rulemaking of this kind that does not establish standards of conduct is unclear. Nevertheless, to inform this rulemaking more fully, the Bureau performed the analysis and consultations described in those provisions of the Dodd-Frank Act.

regarding, among other things, consistency with any prudential, market, or systemic objectives administered by such agencies.

The Proposed Rule would define a category of “larger participant[s] of other markets for other consumer financial products or services” that would be subject to the Bureau’s nonbank supervision program pursuant to 12 U.S.C. 5514(a)(1)(B). The proposed category would include “larger participants” of a market for “student loan servicing” that the Proposed Rule would describe. Participation in this market would be measured on the basis of account volume. If a nonbank covered person’s account volume (measured, per the proposed definition, as of December 31 in the preceding calendar year) exceeded one million, then it would be a larger participant. If a firm was deemed to be a larger participant in a given year, then it would remain a larger participant for at least the subsequent year as well, regardless of its account volume in that year.

*B. Potential Benefits and Costs to Consumers and Covered Persons*

This analysis considers the benefits, costs, and impacts of the key provisions of the Proposed Rule against a baseline that includes the Bureau’s existing rules defining larger participants in certain markets.[53] At present, there is no Federal program for supervision of nonbank student loan servicers of private student loans with respect to Federal consumer financial law. With respect to Federal student loans, there is no Federal program for supervision of nonbank student loan servicers with respect to Federal consumer financial law, but servicing of Federal student loans must be conducted in accordance with the Department of Education’s

[53] The Bureau has discretion in any rulemaking to choose an appropriate scope of analysis with respect to potential benefits and costs and an appropriate baseline. The Bureau, as a matter of discretion, has chosen to describe a broader range of potential effects to more fully inform the rulemaking.

performance standards.[54] With the Proposed Rule in effect, the Bureau would be able to supervise larger participants of the defined student loan servicing market.

The Bureau notes at the outset that limited data are available with which to quantify the potential benefits, costs, and impacts of the Proposed Rule. For example, although the Bureau has general quantitative information, as discussed above, on the number of market participants and their numbers of borrowers and loans and volumes of unpaid principal balances, the Bureau lacks detailed information about their rate of compliance or non-compliance with Federal consumer financial law and about the range of, and costs of, compliance mechanisms used by market participants.

In light of these data limitations, this analysis generally provides a qualitative discussion of the benefits, costs, and impacts of the Proposed Rule. General economic principles, together with the limited data that are available, provide insight into these benefits, costs, and impacts. Where possible, the Bureau has made quantitative estimates based on these principles and data as well as on its experience of undertaking supervision.

The discussion below describes three categories of potential benefits and costs. First, the Proposed Rule, if adopted, would authorize the Bureau's supervision in the student loan servicing market. Larger participants in the market might respond to the possibility of supervision by changing their systems and conduct, and those changes might result in costs, benefits, or other impacts. Second, when the Bureau undertook supervisory activity at specific student loan servicers, those servicers would incur costs from responding to supervisory activity,

[54] Department of Education, Federal Student Aid Annual Report, p. 2 (2012).

and the results of these individual supervisory activities might also produce benefits and costs.[55] Third, the Bureau analyzes the costs that might be associated with entities' efforts to assess whether they would qualify as larger participants under the rule.

In considering the costs and benefits of the Proposed Rule, it is important to note that Federal student loans differ from private student loans in various ways, including repayment options, terms and conditions; the treatment of delinquent accounts; and servicing standards, which for Federal loans are imposed by the Department of Education. Federal student loans are also much more prevalent than private student loans: Of the 39 percent of undergraduates who obtained education loans in the 2007-2008 academic year, 90 percent obtained Federal loans and only 39 percent obtained private student loans.[56]

1. Benefits and Costs of Responses to the Possibility of Supervision

The Proposed Rule would subject larger participants of the student loan servicing market to the possibility of Bureau supervision. That the Bureau would be authorized to undertake supervisory activities with respect to a nonbank covered person who qualified as a larger participant would not necessarily mean the Bureau would in fact undertake such activities regarding that covered person in the near future. Rather, supervision of any particular larger participant as a result of this rulemaking would be probabilistic in nature. For example, the Bureau would examine certain larger participants on a periodic or occasional basis. The Bureau's decisions about supervision would be informed, as applicable, by the factors set forth in

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[55] Pursuant to section 12 U.S.C. 5514(e), the Bureau also has supervisory authority over service providers to nonbank covered persons encompassed by 12 U.S.C. 5514(a)(1), which includes larger participants. The Bureau does not have data on the number or characteristics of service providers to the roughly seven larger participants of the student loan servicing market. The discussion herein of potential costs, benefits, and impacts that might result from the Proposed Rule generally applies to service providers to larger participants.

[56] National Postsecondary Student Aid Study 2008 (hereinafter NPSAS 2008).

12 U.S.C. 5514(b)(2), relating to the size and transaction volume of individual participants, the risks their consumer financial products and services pose to consumers, the extent of State consumer protection oversight, and other factors the Bureau may determine are relevant. Each entity that believed it qualified as a larger participant would know that it might be supervised and might gauge, given its circumstances, the likelihood that the Bureau would initiate an examination or other supervisory activity.

The prospect of potential supervisory activity could create an incentive for larger participants to increase their compliance with Federal consumer financial law. They might anticipate that by doing so (and thereby decreasing risks to consumers), they could decrease the likelihood of their actually being subjected to supervision as the Bureau evaluated the factors outlined above. In addition, an actual examination would likely reveal any past or present noncompliance, which the Bureau could seek to correct through supervisory activity or, in some cases, enforcement actions. Larger participants might therefore judge that the prospect of supervision increased the potential consequences of noncompliance with Federal consumer financial law, and they might seek to decrease that risk by curing or mitigating any noncompliance.

The Bureau believes it is likely that market participants would increase compliance in response to the Bureau's supervisory activities authorized by the Proposed Rule. However, because the Proposed Rule itself would not require any student loan servicer to alter its performance of student loan servicing, any estimate of the amount of increased compliance would be both an estimate of current compliance levels and a prediction of market participants' behavior. The data the Bureau currently has do not support a specific quantitative estimate or prediction. But, to the extent that student loan servicers increased their compliance in response to the Proposed Rule, that response would result in both benefits and costs.[57]

The Bureau notes that the existing levels of compliance with Federal consumer financial law may be different for the servicing of Federal and private student loans. The Department of Education's Office of Federal Student Aid (FSA) sets performance standards and oversees the operations of Federal student loan servicers.[58] FSA standards for systems, controls, and legal compliance may have the collateral consequence that entities comply more faithfully with some aspects of Federal consumer financial law with respect to their servicing of Federal student loans. To that extent, any increase in compliance that resulted from the Proposed Rule might be smaller for Federal than for private student loan servicing. Both the benefits and the costs of increased compliance might thus be smaller for Federal student loan servicing.

a. Benefits from Increased Compliance

Increased compliance would be beneficial to consumers that are affected by student loan servicing. As discussed above, the potential pool of consumers who are directly affected by student loan servicing is broad: In the 2007-2008 academic year, 39 percent of undergraduates and 43 percent of graduate students obtained new student loans.[59] Increasing the rate of compliance with such laws would benefit consumers and the consumer financial market by providing more of the protections mandated by those laws. The roughly seven larger participants of the student loan servicing market that would qualify as larger participants under the proposed

[57] Another approach to considering the benefits, costs, and impacts of the Proposed Rule would be to focus almost entirely on the supervision-related costs for larger participants and omit a broader consideration of the benefits and costs of increased compliance. As noted above, the Bureau has, as a matter of discretion, chosen to describe a broader range of potential effects to more fully inform the rulemaking.
[58] Department of Education, Federal Student Aid Annual Report, p. 2 (2012).
[59] NPSAS 2008.

threshold currently service the student loans of approximately 49 million borrowers.[60] A number of Federal consumer financial laws, including the Electronic Fund Transfer Act (EFTA) and its implementing regulation, Regulation E; the Fair Credit Reporting Act (FCRA) and its implementing regulation, Regulation V; the Equal Credit Opportunity Act (ECOA) and its implementing regulation, Regulation B; and Title X of the Dodd-Frank Act offer substantive protections to consumers regarding student loan servicing.[61] Increasing the rate of compliance with such laws would benefit consumers by providing more of the protections mandated by those laws.[62]

For instance, many student loan servicers receive loan payments through preauthorized electronic fund transfers. Among other things, EFTA establishes certain guidelines for ensuring that fund transfers are not sent without consumers' consent.[63] Increased compliance with EFTA might include a higher degree of fidelity to EFTA's consent process and could thereby decrease the risk that borrowers will suffer unauthorized transfers of their funds. Unauthorized transfers could adversely affect consumers by modifying the amount and timing of payments. Even if the amount of payments per period is anticipated, the timing of payments could constrain consumers

[60] *See* 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates. If a servicer were handling loans to an individual consumer for more than one holder the servicer might count that consumer as more than one borrower. Nonetheless, 49 million borrowers corresponds to a comparably large number of consumers with whom the anticipated larger participants interact.

[61] 15 U.S.C. 1693 *et seq.* (EFTA)*;* 12 CFR part 1005 (Regulation E); 15 U.S.C. 1681 (FCRA); 12 CFR part 1022 (Regulation V); 15 U.S.C. 1691 *et seq.* (ECOA); 12 CFR 1002 (Regulation B); 12 U.S.C. 5301 *et seq.* (Dodd-Frank Act).

[62] Among other things, EFTA is intended to establish basic consumer rights with regard to the use of electronic systems to transfer funds. 15 U.S.C. 1693. FCRA was enacted to improve credit report accuracy and protect consumer privacy. *See Safeco Ins. Co. of Am. v. Burr*, 551 U.S. 47, 52 (2007) ("Congress enacted the FCRA in 1970 to ensure fair and accurate credit reporting, promote efficiency in the banking system, and protect consumer privacy."). ECOA makes it unlawful for creditors to discriminate against applicants, with respect to any aspect of a credit transaction, on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract), the receipt of public assistance income, or the applicants' exercise of certain rights under Federal consumer financial protection laws. 15 U.S.C. 1691(a).

[63] 15 U.S.C. 1693e.

in the very short run. For example, a consumer might plan to make a student loan payment in one pay period and a car payment in the next pay period, but may have insufficient funds both to make payments in the same pay period and to meet his other financial obligations without incurring additional charges such as overdraft fees. Furthermore, the timing of anticipated payments may affect overall consumption for certain groups of consumers.[64]

As another example, many student loan servicers furnish information to consumer reporting agencies about borrowers' payment histories. Such servicers therefore have certain obligations under FCRA and Regulation V. FCRA prohibits the furnishing of information to a consumer reporting agency that the furnisher knows or has reasonable cause to believe is inaccurate.[65] A servicer that furnishes information to consumer reporting agencies must establish and implement reasonable written policies and procedures regarding the accuracy and integrity of the information furnished, considering applicable Federal guidelines, and must periodically review the policies and procedures and update them as necessary to ensure their continued effectiveness.[66] FCRA also gives consumers the ability to dispute information furnished to consumer reporting agencies by submitting disputes to the consumer reporting agencies or directly to furnishers.[67] A student loan servicer receiving a dispute must conduct a

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[64] Recent work by Mastrobuoni and Weinberg and by Shapiro and Slemrod demonstrated that the timing of payments to consumers can affect their consumption. Mastrobuoni, Giovanni and Weinberg, Matthew, 2009. "Heterogeneity in Intra-Monthly Consumption Payments, Self-Control, and Savings at Retirement," *American Economic Journal: Economic Policy*, American Economic Association, vol. 1(2), pp. 163-89; Shapiro, Matthew and Slemrod, Joel, 1995. "Consumer Response to the Timing of Income: Evidence from a Change in Tax Withholding," *American Economic Review*, American Economic Association, vol. 85(1), pp. 274-83. Consumers can also be expected to adjust their consumption in response to the timing of anticipated account debits such as automatic-debit student loan payments.

[65] 15 U.S.C. 1681s-2(a)(1)(A).

[66] 12 CFR 1022.42.

[67] 15 U.S.C. 1681i(a)(1), 1681s-2(a)(8); 12 CFR 1022.43.

reasonable investigation.[68] Increased compliance with these FCRA requirements would increase the accuracy of information that is furnished to consumer reporting agencies and thus of the information that is included in consumer reports. Given that student debt is a substantial proportion of total consumer debt in the United States, increasing the accuracy of reporting in this segment of the debt market could have a substantial positive effect on consumer report accuracy.[69] Because consumer reports are often critical in decisions regarding consumer financial products and services, more accurate information could lead to better economic decisions that would benefit both markets and consumers.[70]

More broadly, the Bureau will be examining whether larger participants of the student loan servicing market engage in unfair, deceptive, or abusive acts or practices (UDAAPs).[71] Conduct that does not violate an express prohibition of another Federal consumer financial law may nonetheless constitute a UDAAP.[72] Among the areas that the Bureau would examine with,

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[68] 15 U.S.C. 1681i (indirect); 12 CFR 1022.43 (direct). In 2011 approximately eight million consumer contacts with the three largest consumer reporting agencies resulted in approximately 32 to 38 million disputed items on consumers' credit files. CFPB, Key Dimensions and Processes in the U.S. Credit Reporting System, p. 4 (2012).

[69] As discussed above, the Bureau estimates that outstanding student loan debt was approximately $1.1 trillion at the end of 2012. This figure represents ten percent of total U.S. consumer debt at the end of the fourth quarter of 2012. *See* Federal Reserve Bank of New York, Quarterly Report on Household Debt and Credit, p. 3 (Feb. 2013), *available at* http://www.newyorkfed.org/research/national_economy/householdcredit/DistrictReport_Q42012.pdf (finding that total U.S. consumer debt was $11.31 trillion at the end of the fourth quarter of 2012).

[70] Inaccurate information, for example, could lead to a consumer's being denied a loan that the consumer could afford to and would be likely to repay. Several studies have identified the problems that inaccurate consumer reporting creates in credit markets. *See e.g.*, Avery, Robert B., et al., *Credit Report Accuracy and Access to Credit*, 2004 Federal Reserve Bulletin 297, pp. 314-15 (estimating fraction of individuals for whom inaccuracies in credit reports might affect credit terms); *see also id.* 301-02 (citing prior research). Inaccurate information could also lead to a consumer's being offered credit at an interest rate higher than would be available if the creditor knew the consumer's true credit history. Conversely, some inaccuracies, by exaggerating some consumers' credit worthiness, may enable such consumers to receive lower interest rates than they otherwise would but understate their risk of default. In all these cases, increasing the accuracy of consumer report information should improve the pricing and allocation of credit.

[71] 12 U.S.C. 5531.

[72] The CFPB Supervision and Examination Manual provides further guidance on how the UDAAP prohibition applies to supervised entities. That examination manual is available at http://www.consumerfinance.gov/guidance/supervision/manual.

in part, a view to preventing UDAAPs are repayment status processing, loan servicing transfers, general payment processing, application of prepayments and partial payments, and default prevention and avoidance. To the degree that any servicer is currently engaged in any UDAAP in these areas, the cessation of the unlawful act or practice would benefit consumers.[73] All of the previously listed areas could be reviewed during an examination and, therefore, student loan servicers might improve policies and procedures relating to these areas in order to avoid engaging in UDAAPs.

b. Costs of Increased Compliance

On the other hand, increasing compliance involves costs. In the first instance, those costs would be paid by the market participants that choose to increase compliance. Student loan servicers might need to hire or train additional personnel to effectuate any changes in their practices that would be necessary to produce the increased compliance. They might need to invest in systems changes to carry out their revised procedures. In addition, student loan servicers might need to develop or enhance compliance management systems, to ensure that they are aware of any gaps in their compliance. Such changes would also require investment and might entail increased operating costs.

An entity that incurred costs in support of increasing compliance might try to recoup those costs by attempting to increase servicing revenues.[74] Whether and to what extent such an

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[73] *See* CFPB Supervision and Examination Manual (October 1, 2012), *available at* http://www.consumerfinance.gov/guidance/supervision/manual/ for a more extensive discussion on the areas in which the Bureau intends to examine. Examiners will be reviewing these business lines for UDAAPs and for any other noncompliance with Federal consumer financial law.

[74] The Bureau uses the terms "revenues" and "receipts" interchangeably in the discussion that follows. The term "annual receipts," however, is used with specific meaning in the context of the Small Business Administration's size standards. How a participant receives its revenue depends on the participant's business model. Compensation for

increase occurred would depend on competitive conditions in the student loan servicing market. For example, larger participants in the student loan servicing market may be in competition with depository institutions or credit unions (or affiliates thereof) that are already subject to Federal supervision with respect to Federal consumer financial law. Assuming as a baseline Bureau supervision of depository institutions and credit unions with over $10 billion in assets (and their affiliates) and prudential regulator supervision with respect to these areas of other depository institutions and credit unions,[75] to the extent the Proposed Rule resulted in an increase in the costs faced by the roughly seven larger participants, that increase would be a competitive benefit to those other covered persons. And competition from those other covered persons might reduce the ability of the roughly seven larger participants to pass an increase in their costs through as an increase in the price of servicing.

Any increase that did occur could constitute a cost of the rule borne in part by originators and holders of student loans. Originators or holders might respond to such a cost by choosing to bear the higher servicing costs, by exiting the student loan market, or by servicing their portfolios of student loans in-house.

Whether and to what extent such an increase might occur would depend on market conditions. With respect to private student loans, origination and servicing are subject to the negotiation of terms, conditions, and prices; the Bureau lacks detailed information with which to predict what portion of any cost of increased compliance would be borne by loan originators or

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servicing Federal student loans is based on contracts with the Department of Education and assignments are dependent on a Department of Education Performance Score Card. *See* Title IV Redacted Contract Awards, *available at* https://www.fbo.gov/spg/ED/FSA/CA/FSA-TitleIV-09/listing.html. *See also* 2012 FSA Conference Session 14, Federal Loan Servicer Panel Discussion, p. 11. For private student loans, servicing contracts are negotiated between loan holders or guarantors and master servicers, and between master servicers and subservicers.

[75] *See* 12 U.S.C. 5515; 12 U.S.C. 5516.

holders, and what portion would be borne by consumers. For Federally-owned loans, the price of servicing is determined by contracts between servicers and the FSA.[76] Because the FSA, as a dominant purchaser of servicing, has great control over pricing, the Bureau expects that relatively little if any increase in the cost of servicing Federal student loans would be passed through as an increase in the price of servicing. With respect to consumers, Federal student loans "were authorized as entitlement programs in order to meet student loan demand."[77] Eligibility criteria, interest rates, and loan limits for Federal student loans are determined by Federal law, including the periodic reauthorization of the Higher Education Act of 1965.[78] Therefore, while the price of servicing Federal student loans might change, depending on market conditions, the pricing for and access to Federal student loans would likely not change substantially as a consequence of increases in servicers' compliance with Federal consumer financial law.

2. Benefits and Costs of Individual Supervisory Activities

In addition to the responses of market participants anticipating supervision, the possible consequences of the Proposed Rule would include the responses to and effects of individual examinations or other supervisory activity that the Bureau might conduct in the student loan servicing market.

a. Benefits of Supervisory Activities

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[76] *See* Title IV Redacted Contract Awards, *available at* https://www.fbo.gov/spg/ED/FSA/CA/FSA-TitleIV-09/listing.html.
[77] Department of Education Student Loans Overview: Fiscal Year 2013 Budget Request at p. R-28, *available at* http://www2.ed.gov/about/overview/budget/budget13/justifications/r-loansoverview.pdf.
[78] 20 U.S.C. 1070 *et seq*.

Supervisory activity could provide several types of benefits. For example, as a result of supervisory activity, the Bureau and the entity might uncover deficiencies in an entity's policies and procedures. The Bureau's examination manual calls for the Bureau generally to prepare a report of each examination, to assess the strength of the entity's compliance mechanisms, and to assess the risks the entity poses to consumers, among other topics. The Bureau would share examination findings with the entity, because one purpose of supervision is to inform the entity of problems detected by examiners. Thus, for example, an examination might find evidence of widespread noncompliance with Federal consumer financial law, or it might identify specific areas where an entity has inadvertently failed to comply. These examples are only illustrative of what kinds of information an examination might uncover.

Detecting and informing entities about such problems should be beneficial to consumers. When the Bureau notifies an entity about risks associated with an aspect of its activities, the entity is expected to adjust its practices to reduce those risks. That response may result in increased compliance with Federal consumer financial law, with benefits like those described above. Or it may avert a violation that would have occurred had Bureau supervision not detected the risk promptly. The Bureau may also inform entities about risks posed to consumers that fall short of violating the law. Action to reduce those risks would also be a benefit to consumers.

Given the obligations student loan servicers have under Federal consumer financial law and the existence of efforts to enforce such law, the results of supervision may also benefit student loan servicers under supervision by detecting compliance problems early. When an entity's level of noncompliance has resulted in litigation or an enforcement action, the entity must face both the costs of defending its actions and the penalties for noncompliance, including potential liability for statutory damages to private plaintiffs. The entity must also adjust its systems to ensure future compliance. Changing practices at this point can be expected to be relatively difficult, because a level of noncompliance that has attracted the attention of enforcement authorities or private plaintiffs is sometimes severe enough to represent a serious failing of an entity's systems. Supervision may detect flaws at a point when correcting them would be relatively inexpensive. And catching problems before they involve an entity in costly private litigation or administrative enforcement, and potentially the payment of legal penalties or other forms of relief, could save the entity substantial time and money. In short, supervision might benefit student loan servicers under supervision by reducing the need for other more expensive activities, like enforcement and private litigation, to achieve a given compliance rate. Accordingly, a shift of some amount of regulatory oversight from enforcement to supervision would be beneficial to market participants.[79]

b. Costs of Supervisory Activities

The potential costs of actual supervisory activities would arise in two categories. The first would involve the costs to individual student loan servicers of increasing compliance in response to the Bureau's findings during supervisory activity and to supervisory actions. These costs would be similar in nature to the possible compliance costs, described above, that larger participants in general might incur in anticipation of possible supervisory activity. This analysis

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[79] Further potential benefits to consumers, covered persons, or both might arise from the Bureau's gathering of information during supervisory activities. The goals of supervision include informing the Bureau about activities of market participants and assessing risks to consumers and to markets for consumer financial products and services. The Bureau may use this information to improve regulation of consumer financial products and services and to improve enforcement of Federal consumer financial law, in order to better serve its mission of ensuring consumers' access to fair, transparent, and competitive markets for such products and services. Benefits of this type would depend on what the Bureau learns during supervision and how it uses that knowledge. For example, because the Bureau would examine multiple covered persons in the student loan servicing market, the Bureau would build an understanding of how effective compliance systems and processes function.

will not repeat that discussion. The second category would be the cost of supporting supervisory activity.

Supervisory activity may involve requests for information or records, on-site or off-site examinations, or some combination of these activities. For example, in an on-site examination, generally, Bureau examiners would begin by contacting an entity for an initial conference with management. That initial contact is often accompanied by a request for information or records. Based on the discussion with management and an initial review of the information received, examiners would determine the scope of the on-site exam. While on-site, examiners would spend some time in further conversation with management about the entity's policies, processes, and procedures. The examiners would also review documents, records, and accounts to assess the entity's compliance and evaluate the entity's compliance management systems. As with the Bureau's other examinations, examinations of nonbank participants in the student loan servicing market might involve issuing confidential examination reports and compliance ratings. The Bureau's examination manual describes the supervision process and indicates what materials and information an entity can expect examiners to request and review, both before they arrive and during their time on-site.

The primary cost an entity would face in connection with an examination would be the cost of employees' time to collect and provide the necessary information. At this stage in its nonbank supervision program, the Bureau does not have precise estimates of the expected duration and frequency of its examinations and the resources that entities may expend to cooperate with such examinations. The frequency and duration of examinations of any particular entity would depend on a number of factors, including the size of the entity, the compliance or other risks identified, whether the entity has been examined previously, and the demands on the

Bureau's supervisory resources imposed by other entities and markets. Nevertheless, some rough estimates may be useful to provide a sense of the magnitude of potential staff costs that entities might incur.

The Bureau has engaged in multiple mortgage servicing exams. Because both mortgage servicing and student loan servicing involve collecting and remitting payments on long-term loans, examinations of mortgage servicers should be a reasonable analogue for the examinations the Bureau would conduct under the Proposed Rule.[80] Therefore, the Bureau intends to estimate duration and labor intensity of examinations using information from mortgage servicing examinations that have already been completed. The average duration of the on-site portion of a Bureau examination of a mortgage servicer is ten weeks.[81] The Bureau estimates the cost of an examination to a student loan servicer by assuming that, similarly, Bureau examiners might review materials and interview employees for ten weeks. An entity might devote the equivalent of one full-time employee during that time and for two weeks beforehand to prepare materials for the examination. The typical cost of an employee involved in responding to supervision can

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[80] Mortgage servicing examinations likely differ in detail from the supervisory activity the Bureau would undertake for student loan servicers. For example, mortgage servicers have certain obligations under the Real Estate Settlement Procedures Act, 12 U.S.C. 2601 *et seq.*, which does not apply to student loan servicing. As another example, mortgages are secured by real estate, and servicing activities may sometimes involve that security interest. The Bureau's examination manuals that relate to mortgage servicing and education lending reflect the differences between these two markets. Nonetheless, for the majority of borrowers, the core activities of the two types of servicers are comparable. The Bureau therefore expects that its experience supervising mortgage servicers can provide a useful guide for estimating the costs of examinations of student loan servicers.

[81] This estimate is based on confidential supervisory Bureau data on the duration of on-site mortgage servicing examinations at both depository institutions and nonbanks. For purposes of this calculation, the Bureau counts its mortgage servicing examinations for which the on-site portion has been completed. Additionally, the Bureau counts only the on-site portion of an examination, which includes time during the on-site period of the examination that examiners spent examining the entity while off-site for holiday or other travel considerations. However, the Bureau does not count time spent scoping an examination before the on-site portion of the examination or summarizing findings or preparing reports of examination afterwards.

be expected to be roughly $49 per hour.[82] Twelve weeks of such an employee's time would cost approximately $24,000.[83]

By comparison, the Bureau estimates that a student loan servicer with responsibility for one million accounts would receive at least $20.2 million per year in revenue from that activity.[84] Thus, the labor costs associated with an examination, as estimated above, would be no greater than 0.12 percent of the annual receipts of such a firm.[85] Note that $20.2 million is an estimated lower bound on the annual receipts of a larger participant as defined by the Proposed Rule, and the Bureau anticipates examining most larger participants in the student loan servicing market no more than approximately once every two years. For all these reasons, the costs associated with supervision are therefore likely to be a much smaller percentage of annual receipts for a given larger participant.[86]

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[82] Bureau of Labor Statistics, (BLS), Occupational Employment Statistics, *available at* ftp://ftp.bls.gov/pub/special.requests/oes/oesm11all.zip. BLS data for "activities related to credit information" (NAICS code 522300) indicate that the mean hourly wage of a compliance officer in that sector is $33.13. BLS data also indicate that salary and wages constitute 67.5 percent of the total cost of compensation. Dividing the hourly wage by 67.5 percent yields a wage (including total costs, such as salary, benefits, and taxes) rounded to the nearest dollar of $49 per hour.

[83] All figures assume 40 hours of work per week.

[84] The Bureau estimates this figure based on the 2013 average unit cost for loan servicing on Federal loans of $1.68 per month per borrower for for-profit servicers of Federal loans, as reported by the Department of Education. *See* Student Aid Administration Fiscal Year 2013 Request at p. AA-15, *available at* http://www2.ed.gov/about/overview/budget/budget13/justifications/aa-saadmin.pdf. The same source reports that not-for-profit servicers' average unit cost is $1.76 per month per borrower. The Bureau assumes, for the estimate, that servicing private student loans generates at least as much revenue per month per borrower as servicing Federal loans, and that a loan is serviced for 12 months per year. Note that since the number of accounts is no less than the number of borrowers, this approach may underestimate revenues.

[85] An entity may receive revenue from other sources.

[86] Assuming the Bureau examines each of the seven larger participants of the student loan servicing market once every two years, the expected annual labor cost of supervision per larger participant would be approximately $12,000. This would account for at most 0.06 percent of the annual receipts of an entity responsible for one million accounts. To put this in perspective, the Bureau estimates that the seven larger participants handle at least 49 million accounts, resulting in at least $984 million in annual receipts. The expected annual labor cost of supervision, collectively, at these seven larger participants is estimated to be $82,000, which is 0.01 percent of their estimated total annual receipts.

However, the Bureau declines to predict, at this point, precisely how many examinations in the student loan servicing market it would undertake in a given year. If the Proposed Rule is adopted, the Bureau will be able to undertake supervisory activity in the identified market; neither the Dodd-Frank Act nor the Proposed Rule specifies a particular level or frequency of examinations. The frequency of examinations would depend on a number of factors, including the Bureau's understanding of the conduct of market participants and the specific risks they pose to consumers; the responses of larger participants to prior examinations; and the demands that other markets make on the Bureau's supervisory resources. These factors can be expected to change over time, and the Bureau's understanding of these factors may change as it gathers more information about the market through its supervision and by other means.

3. Costs of Assessing Larger-Participant Status

Finally, the Bureau acknowledges that in some cases student loan servicers may incur costs in assessing whether they qualify as larger participants and potentially disputing their status. The rule is designed to minimize those costs.

Larger-participant status depends on the number of accounts for which a student loan servicer is performing servicing as of December 31 of the prior calendar year. This number should be readily extractible from administrative records, because account volume is, in general, derived from the compensation a servicer receives. In addition, all but one large nonbank student loan servicer reported to SLSA their number of borrowers and number of loans as of December 31, 2011.[87] These two figures should be lower and upper bounds for a servicer's number of accounts. Student loan servicers that service Federal loans should at a minimum

[87] 2012 SLSA Servicing Volume Survey.

know their Federal loan volumes as of December 31 because the Department of Education keeps up-to-date records of Federal student loan servicers in the National Student Loan Data System (NSLDS).[88]

To the extent that some student loan servicers do not already know their account volumes, such servicers might, in response to the Proposed Rule, develop new systems to count their accounts in accordance with the proposed definition of "account volume." The data the Bureau currently has do not support a detailed estimate of how many student loan servicers would engage in such development or how much they might spend. Regardless, student loan servicers would be unlikely to spend significantly more on specialized systems to count accounts than it would cost them to be supervised by the Bureau as larger participants. It bears emphasizing that even if expenditures on an accounting system successfully proved that a student loan servicer was not a larger participant, it would not necessarily follow that the student loan servicer could not be supervised. The Bureau can supervise a student loan servicer whose conduct the Bureau determines, pursuant to 12 U.S.C. 5514(a)(1)(C), poses risks to consumers. Thus, a student loan servicer choosing to spend significant amounts on an accounting system directed toward the larger-participant test could not be sure it would not be subject to Bureau supervision notwithstanding those expenses. The Bureau therefore believes it is unlikely that any but a very few student loan servicers would undertake such expenditures.

4. Consideration of Alternatives

[88] Department of Education. 2013, National Student Loan Data System (NSLDS) for Students, *available at* https://www.nslds.ed.gov.

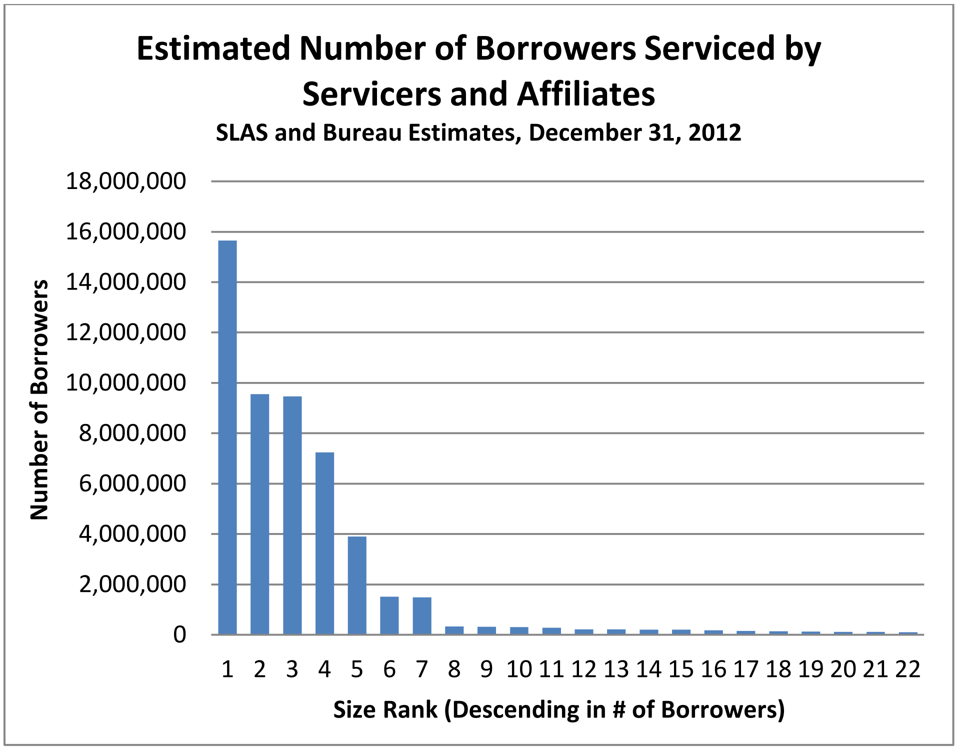
The Bureau is considering different thresholds for larger-participant status in the student loan servicing market. Figure 1 presents projections of the number of borrowers with loans being serviced by each servicer as of December 31, 2012.[89] Since the Bureau does not have specific data about the number of accounts, as defined in the Proposed Rule, in the discussion that follows the number of borrowers, as reported to SLSA, is treated as a proxy for the number of accounts at a given servicer.[90] These projections may underestimate the actual number of accounts for loans being serviced, because they do not account for the possibility of growth in the servicing of private student loans or the possibility of multiple accounts for a given borrower at a servicer. Note that there is a relatively large decline in number of borrowers between the seventh largest servicer, which services the loans of approximately 1.5 million borrowers, and the next largest servicers, each of which services the loans of approximately 300,000 borrowers. This drop is attributable in part to FSA's mechanism for allocating servicing contracts to the TIVAS and to the not-for-profit servicers (NFPs): Each NFP is limited to servicing at most 100,000 Federal accounts at a time.[91]

One possible alternative the Bureau is considering is a larger threshold, of, for example, three million in account volume. Under such an alternative, the benefits of supervision to both consumers and covered persons would likely be substantially reduced because firms impacting a large number of consumers and/or consumers in important market segments would be omitted. On the other hand, the potential costs to covered persons would of course be reduced if fewer

[89] *See* 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.
[90] For Federal Direct and Federally-owned FFELP loans, the concept of borrower and account are identical.
[91] SAFRA - Not-For-Profit (NFP) Servicer Program documentation, as of Dec. 6, 2012, *available at* https://www.fbo.gov/spg/ED/FSA/CA/NFP-RFP-2010/listing.html.

firms were defined as larger participants and thus fewer were subject to the Bureau's supervision authority on that basis.

**Figure 1: Estimated Number of Borrowers Serviced by Servicers and Affiliates**[92]




The Bureau is also considering various other criteria for determining larger-participant status, including number of loans and total unpaid principal balances. Calculating either of these metrics might be more involved than calculating total account volume for a given servicer. If so, then a given entity might face greater costs for evaluating or disputing whether it qualified as a larger participant. However, among the participants in the student loan servicing market these metrics correlate strongly with account volume. For each criterion, the Bureau expects that it could choose a suitable threshold for which the set of larger participants, among those entities

[92] 2012 SLSA Servicing Volume Survey, augmented by CFPB estimates.

participating in the market today, would be the same as the seven entities expected to qualify under the Proposed Rule. Consequently, the costs, benefits, and impacts of supervisory activities should not depend on which criterion the Bureau uses.

### *C. Potential Specific Impacts of the Proposed Rule*

#### 1. Depository Institutions and Credit Unions With $10 Billion or Less in Total Assets, As Described in Dodd-Frank Act Section 1026

The Proposed Rule would not apply to depository institutions or credit unions of any size. However, it might, as discussed above, have some impact on depository institutions that hold private student loans or that service private student loans or FFELP loans. The Proposed Rule might therefore alter market dynamics in a market in which some depository institutions and credit unions with less than $10 billion in assets may be active. To the extent such institutions may have less market power than larger institutions, the change in market dynamics could affect them differently. Although this affects all student loan holders that contract for servicing, loan holders that are depository institutions or credit unions with less than $10 billion in assets may have less negotiating power with respect to the price of servicing than larger institutions, so they may face larger price increases. However, the Bureau notes that asset size alone is not necessarily a good predictor of each institution's susceptibility to any changes in the student loan servicing market that might result from the Proposed Rule. An individual institution that focused on educational lending might, on its own or together with its affiliates, play a role in the market for originating student loans or for contracting for servicing that was disproportionate to its assets as a share of the overall banking market. And an individual institution might have contractual or other relationships with particular servicers that could insulate it from some of the potential impacts of the Proposed Rule or could make it especially vulnerable to those impacts.

2. Impact of the Provisions on Consumer Access to Credit and on Consumers in Rural Areas

If the costs of increased compliance increased the price of servicing, creditors might consider that increase in the underwriting and loan pricing process. Private student loan creditors might consider adjusting the terms and conditions of loans to pass some or all of the price increase through to consumers. In addition, creditors might be less willing to extend credit to marginal borrowers. Thus, it is possible that consumers' access to credit might decrease as a result of the Proposed Rule. As noted above, qualifying students are entitled to Federal Direct loans in amounts and on terms specified by statute.[93] An increase in the price of servicing Federal loans is therefore unlikely to reduce consumers' access to such loans.

Since the rule applies uniformly to the loans of a particular type of both rural and non-rural consumers, the rule should not have a unique impact on rural consumers. The Bureau is not aware of any evidence suggesting that rural consumers have been disproportionately harmed by student loan servicers' failure to comply with Federal consumer financial law. The Bureau would welcome any comments that may provide information related to how student loan servicing affects rural consumers.

## VII. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996, requires each agency to consider the potential impact of its regulations on small entities, including small businesses, small governmental units, and small

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[93] *See* 20 U.S.C. 1087e.

not-for-profit organizations.[94] The RFA defines a “small business” as a business that meets the size standard developed by the Small Business Administration pursuant to the Small Business Act.[95]

The RFA generally requires an agency to conduct an initial regulatory flexibility analysis (IRFA) of any proposed rule subject to notice-and-comment rulemaking requirements, unless the agency certifies that the proposed rule would not have a significant economic impact on a substantial number of small entities. The Bureau also is subject to certain additional procedures under the RFA involving the convening of a panel to consult with small entity representatives prior to proposing a rule for which an IRFA is required.[96]

The undersigned certifies that the Proposed Rule, if adopted, would not have a significant economic impact on a substantial number of small entities and that an initial regulatory flexibility analysis is therefore not required.

The Proposed Rule would define a class of student loan servicers as larger participants of the student loan servicing market and thereby authorize the Bureau to undertake supervisory activities with respect to those servicers. The rule adopts a threshold for larger-participant status of one million in account volume. As estimated above, a student loan servicer with one million accounts receives about $20.2 million in servicing revenue per year. By contrast, under the

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[94] 5 U.S.C. 601 *et seq*. The term “‘small organization’ means any not-for-profit enterprise which is independently owned and operated and is not dominant in its field, unless an agency establishes [an alternative definition after notice and comment].” *Id*. at 601(4). The term “‘small governmental jurisdiction’ means governments of cities, counties, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand, unless an agency establishes [an alternative definition after notice and comment].” *Id*. at 601(5). The Bureau is not aware of any small governmental units or small not-for-profit organizations to which the Proposed Rule would apply.

[95] 5 U.S.C. 601(3). The Bureau may establish an alternative definition after consultation with the Small Business Administration and an opportunity for public comment.

[96] 5 U.S.C. 609.

Small Business Administration's existing criterion, a servicer is a small business only if its annual receipts are below $7 million.[97] Thus, larger participants in the student loan servicing market would generally not be small businesses for purposes of this analysis. Indeed, using the estimate above that a servicer earns $1.68 per month per account, the Bureau believes that none of the larger participants under the Proposed Rule would have annual receipts below $30 million.[98] Moreover, the rule does not itself impose any obligations or standards of conduct on businesses outside the category of larger participants.

For these reasons, the Proposed Rule would not have a significant impact on a substantial number of small entities.[99]

Additionally, and in any event, the Bureau believes that the Proposed Rule would not result in a "significant impact" on any small entities that could be affected. As previously noted, when and how often the Bureau would in fact engage in supervisory activity, such as an examination, with respect to a larger participant (and, if so, the frequency and extent of such

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[97] 13 CFR 121.201 (NAICS code 522390). For the purposes of this analysis, the Bureau assumes that participants in the student loan servicing market will be classified in NAICS code 522390, "other activities related to credit intermediation." NAICS lists "loan servicing" as an index entry corresponding to this code. *See* http://www.census.gov/cgi-bin/sssd/naics/naicsrch?code=522390&search=2012 NAICS Search. The Bureau welcomes comment on whether this or any other NAICS code is most appropriate for this market. The Bureau is aware that a nonbank larger participant of the student loan servicing market could be classified in a NAICS code other than the one that includes loan servicing. For example, some entities may be in NAICS code 522291 for consumer lending, which is the index entry corresponding to student lending. The Small Business Administration's size standard for consumer lending is also $7 million in annual receipts. *See* 13 CFR 121.201 (NAICS code 522291).

[98] If one or more larger participants services loans it holds, such a firm might not receive monthly servicing compensation for such accounts. However, the Bureau is not currently aware of any small businesses that service student loans they originate or hold and that would meet the larger-participant threshold.

[99] A business might, hypothetically, be a larger participant of the student loan servicing market yet be a small business for RFA purposes, if the business lost a significant amount of account volume during the second year after qualifying as a larger participant. The Bureau expects such situations, if any, to be quite rare. In addition, if the Bureau aggregates the activities of affiliated companies in part by adding together numbers of accounts, two companies that are small businesses might, together, have an account volume over one million. The Bureau anticipates no more than a very few such cases, if any, in the student loan servicing market.

activity) would depend on a number of considerations, including the Bureau's allocation of resources and the application of the statutory factors set forth in 12 U.S.C. 5514(b)(2). Given the Bureau's finite supervisory resources, and the range of industries over which it has supervisory responsibility for consumer financial protection, when and how often a given student loan servicer would be supervised is uncertain. Moreover, when supervisory activity occurred, the costs that would result from such activity are expected to be minimal in relation to the overall activities of a student loan servicer.[100]

Finally, 12 U.S.C. 5514(e) authorizes the Bureau to supervise service providers to nonbank covered persons encompassed by 12 U.S.C. 5514(a)(1), which includes larger participants. Because the Proposed Rule would not address service providers, effects on service providers need not be discussed for purposes of this RFA analysis. Even were such effects relevant, the Bureau believes that it would be very unlikely that any supervisory activities with respect to the service providers to the approximately seven larger participants in the proposed student loan servicing market would result in a significant economic impact on a substantial number of small entities.[101]

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[100] As discussed above, the cost of participating in an examination might be roughly 0.12 percent of annual receipts for a firm near the threshold of one million in account volume. The proportion would be larger for a smaller firm, but the impact would still not be substantial.

[101] The Bureau reaches this judgment in light of the number of relevant small firms in the relevant NAICS codes. For example, many of these service providers would be considered to be in the industries with NAICS code 522390, "Other activities related to credit intermediation." According to the 2007 Economics Census, there are more than 5,000 small firms in the industry. The number of firms connected to the roughly seven larger participants of the proposed student loan servicing market is likely to be a fraction of this figure. Moreover, the impact of supervisory activities at such service providers would likely be no more intensive—and probably much less, given the Bureau's exercise of its discretion in supervision—than at the larger participants themselves. As discussed above, supervisory activities at larger participants would not be expected to give rise to a significant economic impact. Finally, because it is very unlikely that the Bureau would supervise many of such entities, a substantial number of entities would not likely be affected.

Accordingly, the undersigned certifies that the Proposed Rule would not have a significant economic impact on a substantial number of small entities.

## VIII. Paperwork Reduction Act

The Bureau has determined that this Proposed Rule would not impose any new recordkeeping, reporting, or disclosure requirements on covered entities or members of the public that would constitute collections of information requiring approval under the Paperwork Reduction Act, 44 U.S.C. 3501, *et seq*.

## List of Subjects in 12 CFR Part 1090

Consumer protection, Credit.

## Authority and Issuance

For the reasons set forth in the preamble, the Bureau proposes to amend 12 CFR Part 1090, Subpart B, to read as follows:

## PART 1090—DEFINING LARGER PARTICIPANTS OF CERTAIN CONSUMER FINANCIAL PRODUCT AND SERVICE MARKETS

1. The authority citation for part 1090 continues to read as follows:

**Authority:** 12 U.S.C. 5514(a)(1)(B); 12 U.S.C. 5514(a)(2); 12 U.S.C. 5514(b)(7)(A); and 12 U.S.C. 5512(b)(1).

2. Add a new § 1090.106 to subpart B to read as follows:

**§ 1090.106 Student loan servicing market**.

(a) Market-Related definitions. As used in this subpart:

Account volume means the number of accounts with respect to which a nonbank covered person is considered to perform student loan servicing, calculated as follows:

(i) Number of accounts. A nonbank covered person has at least one account for each student or prior student with respect to whom the nonbank covered person performs student loan servicing. If a nonbank covered person is receiving separate fees for performing student loan servicing with respect to a given student or prior student, the nonbank covered person has one account for each stream of fees to which the person is entitled.

(ii) Time of measurement. The number of accounts is counted as of December 31 of the prior calendar year.

(iii) Affiliated companies.

(A) The account volume of a nonbank covered person is the sum of the number of accounts of that nonbank covered person and of any affiliated companies of that person.

(B) If two persons become affiliated companies, each person's number of accounts as of the prior calendar year's December 31 is included in the total account volume.

(C) If two affiliated companies cease to be affiliated companies, the number of accounts of each continues to be included in the other's account volume until the succeeding December 31.

Post-secondary education expenses means any of the expenses that are included as part of the cost of attendance of a student as defined in 20 U.S.C. 1087*ll*.

Post-secondary education loan means an extension of credit (a) that is made, insured or guaranteed under Title IV of the Higher Education Act of 1965 (20 U.S.C. 1070 *et seq.*); or (b) that is extended to a consumer with the expectation that the funds extended will be used in whole or in part to pay post-secondary education expenses. A loan that is extended in order to refinance or consolidate a consumer's existing post-secondary education loans is also a post-secondary education loan. However, no extension of credit under an open-end credit plan (as defined in Regulation Z, 12 CFR 1026.2(a)(20)) or loan that is secured by real property is a post-secondary education loan, regardless of the purpose for the extension of credit.

Student loan servicing means receiving any scheduled periodic payments from a borrower pursuant to the terms of any post-secondary education loan, and making the payments of principal and interest and other amounts with respect to the amounts received from the borrower as may be required pursuant to the terms of the post-secondary education loan or of the contract governing the servicing; or, during a period when payment on a post-secondary education loan is deferred, maintaining account records for the loan and communicating with the borrower regarding the loan, on behalf of the loan's holder. Student loan servicing also includes interactions with a borrower to facilitate such receiving or making of payments or maintaining of account records and communicating with borrowers. Among the interactions that constitute student loan servicing are activities to help delinquent borrowers avoid or prevent default on obligations arising from post-secondary education loans.

(b) Test to define larger participants. A nonbank covered person that offers or provides student loan servicing is a larger participant of the student loan servicing market if the nonbank covered person's account volume exceeds one million.

**[THIS PAGE PERTAINS TO THE PROPOSED RULE TITLED "DEFINING LARGER PARTICIPANTS OF THE STUDENT LOAN SERVICING MARKET"]**

Dated: March 12, 2013.

**Richard Cordray,**

*Director, Bureau of Consumer Financial Protection.*