



PROPOSED ACTION
MEMORANDUM

The Role of State Laws to Police and Regulate
Student Loan Servicing Companies

Department of Education
November 2020

I. Summary

On March 18, 2018, the Department of Education issued a Notice of Interpretation (Notice) in the *Federal Register* regarding the preemption of state laws as applied to student loan servicing companies.¹ The Notice, promulgated at the advice and suggestion of the student loan servicing industry, interpreted the Higher Education Act (HEA) and federal law to limit the role of state consumer protection laws, regulations, and oversight over student loan servicing companies.² Under the interpretation advanced by Secretary DeVos in the Notice, if a student loan servicing company provides affirmatively false information to a borrower, that borrower is without judicial recourse. Similarly, under the Notice, a state attorney general is preempted from bringing a state law enforcement action against a servicing company if that servicing company acts deceptively, unfairly, untruthfully, or otherwise violates state consumer protection laws. Finally, under the Notice, state laws that “impose requirements” on servicers (through state law licensing, registration, or supervision regimes) “may conflict with legal, regulatory, and contractual requirements,” and are therefore preempted. The Notice was widely rebuked by a bipartisan group of state attorneys general, the National Governors Association, and consumer-protection advocacy organizations.³

This memorandum proposes that the Department immediately revoke the Notice and issue revised interpretations (one on state consumer protection laws; one on state regulations and oversight) after an opportunity for public comment.

II. Background and Current State

The Notice has been raised in litigation and has been relied upon by student loan servicing companies seeking to avoid liability in attorney general enforcement actions and consumer class actions.⁴ The Notice has also been relied upon by industry organizations seeking to invalidate state efforts to regulate the student loan servicing industry, and by student loan servicing companies seeking to avoid oversight by state regulators and licensors.

The Notice has been widely and expressly rejected as unpersuasive, and federal courts have refused to defer to the Notice or adopt the interpretations stated therein.⁵ And in other cases that post-date the Notice, courts

¹ See Federal Preemption and State Regulation of the Department of Education’s Federal Student Loan Programs and Federal Student Loan Servicers, 83 Fed. Reg. 10,619 (March 12, 2018).

² See Michael Stratford, *How the student loan industry lobbied DeVos to fight state regulations*, POLITICO, (Aug. 15, 2019), <https://www.politico.com/story/2019/08/15/student-loan-devos-lobbying-1464926>.

³ See Office of the Attorney General of New York State, Letter to Secretary of Education Betsy DeVos, (Oct. 23, 2017), https://www.marylandattorneygeneral.gov/news%20documents/DeVos_10_24_17.pdf; see also National Governors Association, *Governors Voice Concerns Over New Student Borrower Proposal*, (Mar. 12, 2018), <https://www.nga.org/news/press-releases/governors-voice-concerns-over-new-student-borrower-proposal/>.

⁴ See National Student Legal Defense Network, Preemption Project, (accessed Jun. 16, 2020), <https://www.defendstudents.org/work/preemption-project>.

⁵ See, e.g., *Nelson v. Great Lakes Educ. Loan Servs., Inc.*, 928 F.3d 639, 651 (7th Cir. 2019) (“We also agree that the Preemption Notice is not persuasive because it is not particularly thorough and it ‘represents a stark, unexplained change’ in the Department’s position.”); *Lawson-Ross v. Great Lakes Higher Educ.*, 955 F.3d 908, 921 n.13 (11th Cir. Apr. 10, 2020) (finding the Notice “unpersuasive”). See also, e.g., *Hyland v. Navient Corp.*, No. 18CV9031(DLC), 2019 WL 2918238, at *7 (S.D.N.Y. July 8, 2019) (agreeing with *Nelson*); *Pennsylvania v. Navient Corp.*, 354 F. Supp. 3d 529, 552 (M.D. Pa. 2018) (declining to defer to the Notice) *aff’d* ___ F.3d ___ (3rd Cir. 2020); *Student Loan Servicing All. v. District of Columbia*, 351 F. Supp. 3d 26, 50 (D.D.C. 2018) (hereinafter “SLSA”) (finding that the Notice is not “persuasive guidance” in part because it “represents a stark, unexplained change in the DOED’s position”); *id.* at 70 (noting that the Notice is due “no deference whatsoever”); *People of the State of New York v. Pennsylvania Higher Educ. Assistance Agency*, No. 19 CIV. 9155 (ER), 2020 WL 2097640, at *17 n.14 (S.D.N.Y. May 1, 2020) (hereinafter “NY v. PHEAA”) (agreeing with “nearly every other court to have considered the Preemption Notice: it is entitled to little weight,” and acknowledging that the “only” decision to find the Notice persuasive was vacated by the Eleventh Circuit in *Lawson-Ross*); *Reavis v. Pennsylvania Higher Educ. Assistance Agency*, 2020 WL 3969887, ___ P.3d ___ (Mt. 2020) (declining to defer).

have rejected the interpretation contained in the Notice, albeit without expressly opining on the persuasive value of the interpretation.⁶

Indeed, we are aware of *only* two federal court opinions that squarely adopted the position espoused in the Notice, both of which have now been vacated by respective U.S. Courts of Appeal.⁷

III. Proposed Action

Immediately publish a statement in the *Federal Register* withdrawing the Notice, in light of both the policy expressed in the Notice and its wide rejection by federal courts, and establish a thirty-day comment period for interested members of the public to comment on the preemptive effect of the HEA vis-à-vis student loan servicing companies. The withdrawal notice and request for comments should recognize, discuss, and seek comment upon: (a) the salient legislative history of 20 U.S.C. § 1098g, and its connection to the Truth in

⁶ See, e.g., *Pennsylvania v. Navient Corp.*, ___ F.3d ___ (3rd Cir. 2020); *Travis v. Navient*, No. 17-cv-4886, 2020 WL 2523066, at *5-9 (E.D.N.Y., May 18, 2020) (citing, with approval, *Nelson*, *Pennsylvania v. Navient* (district court), and *Hyland v. Navient*); *Minner v. Navient Corp. & Navient Solutions, LLC*, No. 18-CV-1086S, 2020 WL 906628, at *9 (W.D.N.Y. Feb. 25, 2020) (implicitly declining to defer to the Notice of Interpretation); *Olsen v. Nelnet, Inc.*, 392 F. Supp. 3d 1006, 1021 (D. Neb. 2019) (same); *Chery v. Conduent Educ. Servs., LLC*, No. 1:18-CV-75, 2019 WL 1427140, at *4 (N.D.N.Y. Mar. 29, 2019) (same).

⁷ See *Nelson v. Great Lakes Educ. Loan Servs., Inc.*, 928 F.3d 639, 651 (7th Cir. 2019) *vacating Nelson v. Great Lakes Educ. Loan Servs., Inc.*, No. 317CV00183NJRSCW, 2017 WL 6501919 (S.D. Ill. Dec. 19, 2017); *Lawson-Ross v. Great Lakes Higher Educ.*, 955 F.3d 908 (11th Cir. Apr. 10, 2020) *vacating Lawson-Ross v. Great Lakes Higher Educ. Corp.*, No. 1:17-CV-253-MW/GRJ, 2018 WL 5621872 (N.D. Fla. Sept. 20, 2018). The now-vacated district court opinion in *Nelson* pre-dates the Notice. The Notice, meanwhile, was published shortly *after* the district court issued its decision, but before that decision was vacated, and expressly relies on that now-vacated opinion.

The Southern District of New York recently took a nuanced approach to preemption. See *NY v. PHEAA*, 2020 WL 2097640, at *15–*16. In that case, the State of New York had made a series of claims regarding PHEAA’s servicing of federal student loans. After concluding that PHEAA was not entitled to so-called “*Yearsley* immunity” (*i.e.*, derivative sovereign immunity) or intergovernmental immunity, the court turned to issues of preemption. First, as noted above, the court declined to defer to the Notice. *Id.* at *17 n.14. Second, with respect to most of the claims in the case, the court agreed with the courts of appeal in *Nelson* and *Lawson-Ross* that state law claims for affirmative misrepresentations were not preempted by 20 U.S.C. § 1098g. *Id.* at *15. Third, however, the court concluded that claims premised on an allegation that PHEAA “steer[ed] borrowers into less favorable repayment options,” such as, for example, forbearance, were preempted under § 1098g. This holding, however, appears to be rooted in the specifics of how the claim was alleged—*i.e.*, that a steering claim was about what borrowers were “told” about repayment options and/or that PHEAA “misrepresents the options . . . by often failing to mention the option to enter [income driven repayment]” instead of forbearance. *Id.* Perhaps recognizing the limited nature of its holding, the Court also expressly noted that it did “not find that amendment would be futile” and permitted NY, “if it so chooses, to replead the claims dismissed here.” *Id.* at *16. The *PHEAA v. NY* holding, therefore, is entirely consistent with both *Nelson* and *Lawson-Ross*, *i.e.*, that if the HEA mandates certain disclosures, and the state law claim is premised on—and alleged in terms of a—failure to make such a disclosure, such a claim is a preempted state law “disclosure requirement” under 20 U.S.C. § 1098g.

Lending Act,⁸ (b) the court opinions discussing the preemption issue, *see supra*, and (c) the 2018 Notice, other departmental pronouncements on preemption,⁹ and judicial opinions discussing those pronouncements.

⁸ Section 1098g was codified in the same provision in which Congress exempted federal student loans from the disclosure requirements of the Truth in Lending Act (“TILA”) and state disclosure requirements. Pub. L. 97-320, § 701, 96 Stat. 1538 (1982). Section 701(a) of Pub. L. 97-320 exempted HEA Title IV loans from coverage under TILA, while § 701(b) provided that “Loans made, insured, or guaranteed pursuant to a program authorized by title IV of the Higher Education Act of 1965 ... shall not be subject to any disclosure requirements of any State law.” Pub. L. 97-320, § 701, 96 Stat. 1538.

At the time, TILA and its implementing regulation required a creditor to make certain disclosures for each transaction, including the creditor’s identity, the amount being financed, any finance charges, the annual percentage rate, any variable rate, the payment schedule, the total amount of payments to be made, any demand features, and additional information about prepayment, late payments, and assumption. *See* Truth in Lending; Revised Regulation Z, 46 Fed. Reg. 20,848, 20,902-03 (April 7, 1981) (codified at 12 C.F.R. § 226.18, effective April 1, 1981). Congress was concerned about lenders and servicers being required to provide duplicative disclosures, since TILA’s coverage overlapped with comparable disclosures required under the HEA for federal student loans. *See* S. Rep. 97-536, at 42, *reprinted in* 1982 U.S.C.A.N. 3054, 3096.

When § 701 was enacted, TILA permitted states to apply to the Federal Reserve Board (“Board”) for a determination of whether a state law disclosure is “substantially the same in meaning as disclosure required under this subchapter.” 15 U.S.C. § 1610(a)(2) (1982). If the Board determined that the state-required disclosure was substantially the same in meaning as a disclosure required by TILA, “then creditors located in that State may make such disclosure in compliance with such State law in lieu of the disclosures required by” TILA. *Id.*; *see also* 12 C.F.R. § 226.29 (1982). Accordingly, if Congress had stopped at § 701(a), and had not adopted § 701(b), now codified as § 1098g, creditors in states that had adopted disclosures approved by the Board as substantially the same as those in TILA would likely have been subject to both the state law disclosure requirements and the HEA disclosures, resulting in precisely the confusion and duplication the legislative history indicates Congress sought to avoid.

There are several indications that Congress was concerned about state truth-in-lending disclosures when it enacted § 1098g. For example, during the legislative process, one senator stated that “[s]ome 23 States have enacted their own truth-in-lending provisions. As is true with respect to the Federal [TILA], State disclosure laws serve no useful purpose in connection with loans made under title IV of the Higher Education Act of 1965. It is therefore appropriate that the proposed exemption apply as well to State laws.” 97 Cong. Rec. 19,897, 19,916 (daily ed. Aug. 9, 1982) (statement of Sen. Heinz). Further, the civil liability provision in TILA authorizes liability for failure to comply with state law “disclosure requirements” that have been determined to be “substantially the same” as those imposed by TILA, 15 U.S.C. § 1640, adding to the inference that “disclosure requirements” in § 1098g similarly meant to refer only to state truth-in-lending act requirements.

⁹ Prior to the issuance of the Notice, the Department had generally affirmed the role of state consumer protection laws. For example, as recently as 2016, the Department’s Office of General Counsel explained that “the Department does not believe that the State’s regulation of [loan servicers or private collection agencies] would be preempted by Federal law.” Letter of Vanessa A. Burton to Jedd Bellman, Assistant Commissioner, Maryland Dep’t of Labor, Licensing, and Regulation at 2 (Jan. 21, 2016), <https://goo.gl/J1KB3e>. Moreover, in a Statement of Interest filed in *Sanchez v. ASA College, Inc.*, No. 14-5006, 2015 WL 3540836 (S.D.N.Y. June 5, 2015), “the United States declared that “[n]othing in the HEA or its legislative history even suggests that the HEA should be read to preempt or displace state or federal laws. Nor is there anything in the HEA or the regulations promulgated thereunder to evince any intent of Congress or [ED] that the HEA or its regulations establish an exclusive administrative review process of student claims brought under state or deferral law, even if the conduct alleged may separately constitute an HEA violation.” *SLSA*, 351 F. Supp. 3d at 50 (quoting the Statement of Interest).

In addition, in 1990, the Department issued a Notice of Interpretation regarding the preemptive scope of regulations setting out the steps that entities collecting student loans guaranteed by the federal government must take to attempt to collect defaulted student loans (“GSL Notice”). Notice of Interpretation: Stafford Loan, Supplemental Loans for Students, PLUS, and Consolidation Loan Programs, 55 Fed. Reg. 40,120 (Oct. 1, 1990). In the GSL Notice, the Department expressly “stresse[d] the limited nature of this action in displacing State rules and authority,” stating, consistent with the views espoused in 2015 and 2016, that “the preemptive effect of [the GSL] regulations extended no farther than is reasonably necessary to achieve an effective minimum standard of collection action.” 55 Fed. Reg. at 40,121.

Even further, a 2015 amicus brief submitted to the Seventh Circuit, the Department took the “opportunity to make clear that the [HEA] does not preempt breach-of-contract claims that are premised on violations of the Act,” Brief of the United States as Amicus Curiae, *Bible v. United Student Aid Funds, Inc.*, Case No. 14-1806, 2015 WL 3403631 (7th Cir. May 21, 2015). These statements are consistent with how the Department has viewed preemption of claims against other actors involved in the Title IV programs. *Cf.* Program Integrity Issues, 75 Fed. Reg. 66,832, 66,865 (Oct. 29, 2010) (“States should retain the primary role and responsibility for student consumer protection against fraudulent or abusive practices by some postsecondary institutions.”).

This is not to say that the Department has been uniform and absolute. Indeed, in its briefs in the district court and Ninth Circuit in *Chae v. SLM Corp.*, 593 F.3d 936 (9th Cir. 2010), the Department asserted that certain of the claims were preempted by federal law. But in *Chae*, as the Eleventh Circuit summarized in the Lawson-Ross case, the claims at issue challenged how the servicer communicated information that the HEA required it to disclose. Thus, the pronouncements with respect to the claims at issue in *Chae* were fundamentally different than the sorts of claims being made now against student loan servicing companies. *See, e.g., NY v. PHEAA*, 2020 WL 2097640 at *16 n.13 (“As two different appellate courts and one court in this District have noted, *Chae* concerned disclosures that were compelled by federal law and which were disclosed in a manner that comported with federal law, and therefore the Ninth Circuit found that plaintiffs were simply seeking to impose additional disclosure requirements.”). Additionally, as noted *infra*, shortly after the issuance of the Notice, on March 26, 2018, the Department’s Office of the General Counsel cited the Notice to support its position that “[s]tate laws regulating Direct Loan servicing are preempted by Federal law.” *See* Letter from S. Dawn Scaniffe, Dep’t of Educ. Office of Gen. Counsel to Carmen Costa, Director, Consumer Credit Division, Connecticut Department of Banking (March 26, 2018) (filed in *PHEAA v. Perez*, No. 3:18-cv-01114 (D. Conn. Dec. 19, 2019) at Dkt. 67-14).

By providing a period for public comment, the Department will increase the extent of the deference ultimately afforded to a new interpretation of the preemption issue.¹⁰ After reviewing submitted comments, absent compelling evidence to the contrary, the Department should quickly publish two separate notices of interpretation: one regarding state regulation of affirmative misstatements and material omissions, and one regarding state regulation, licensing, or monitoring of loan servicer operations.

State laws governing affirmative misstatements and material omissions

The first notice will consider the role of state UDAAP (unfair, deceptive, or abusive acts or practices) laws, and forcefully affirm the importance of state law to both misrepresentations and material omissions (*i.e.*, failures to provide information). Although the final interpretation must grapple with the express preemption language in 20 U.S.C. § 1098g, the Department can interpret the word “disclosure” in that section to be co-extensive with the federally mandated “disclosures” that must be provided under 20 U.S.C. § 1083 and Department regulations. Such a notice can ensure the primacy of state laws of general applicability that police and provide remedies for unfair, deceptive, and abusive acts and practices of student loan servicing companies.

State laws requiring licensing or registration regulation of student loan servicing companies that contract with the federal government

The second notice can address the role of state law in regulating and/or licensing student loan servicing companies. We believe the precise preemptive scope of the HEA in this regard to be a more difficult question than would be addressed in the first notice. For this reason—in addition to the difficulties that some district courts have had distinguishing between the various types of preemption—we think there are strategic advantages to separating the notice (largely to ensure the primacy of consumer protection laws).

At one end, the Department needs to take seriously the opinions of two district courts that have held that state law licensing regimes create “duplicative and additional” requirements for loan-servicing companies and therefore can be seen as “second-guess[ing] the federal government’s decisions to contract” with the servicers. *SLSA*, 351 F. Supp. 3d. at 62; *Pennsylvania Higher Educ. Assistance Agency v. Perez*, No. 3:18-CV-1114 (MPS), 2020 WL 2079634, at *9 (D. Conn. Apr. 30, 2020) (hereinafter *PHEAA v. Perez*). In both of these cases, the courts have held that federalism principles bar state licensing regimes, because such regimes could give a state agency “virtual power of review over the federation [contracting] determination.” *SLSA*, 351 F. Supp. 3d at 62 (citing, *inter alia*, *Leslie Miller, Inc. v. Arkansas*, 352 U.S. 187, 190 (1956)); *PHEAA v. Perez*, 2020 WL 2079634, at *9 (same).

But neither *SLSA* nor *PHEAA v. Perez* restrict the role of state oversight beyond licensing regimes that provide states with an effective veto power over federal student loan servicers operating in a state. Indeed, the core issue in *PHEAA v. Perez* was whether or not PHEAA could be forced to comply with document demands made by the Connecticut Department of Banking (CT DOB), which is the state regulator over—and licensor of—student loan servicing companies. As part of an examination of PHEAA, the CT DOB

¹⁰ *Christopher v. SmithKline Beecham Corp.*, 567 U.S.142, 159 (2012) (observing that the Department of Labor’s interpretation of a regulation articulated in a series of amicus briefs “plainly lack[ed] the hallmarks of thorough consideration” because “there was no opportunity for public comment”); *Vulcan Const. Materials, L.P. v. Fed. Mine Safety & Health Review Comm’n*, 700 F.3d 297, 316 (7th Cir. 2012). Ultimately, any the extent of judicial deference to any interpretation published by the Department “will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control.” *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944). See also, e.g., *United States v. Mead Corp.*, 533 U.S. 218, 228 (2001).

sought the production of a series of records. The Department, meanwhile, restricted PHEAA from turning over those records. After striking down the licensing rule as preempted, the District Court then held that the document demands at issue in that case were also preempted because those demands were premised on Connecticut’s licensing authority, which the District Court had found preempted. The District Court expressly reserved for another day whether CT DOB (or another state agency) could subpoena PHEAA records as part of a separate authority. *PHEAA v. Perez*, 2020 WL 2079634, at *11 & n.7.¹¹

As it relates to state law *licensing* regimes (as distinct from registration or supervision regimes, or document demands), the formulation expressed in *SLSA* and *PHEAA v. Perez* appears likely to win the day—*i.e.* a state cannot functionally *veto* the use of a contractor selected by the federal government to perform activities in that state. But state law can still require registration and supervision of the student loan servicing companies and enforce compliance with state laws that do not conflict with federal obligations and limitations.¹² Courts may also look favorably on state licensing regimes that grant licenses as a matter of course to federal contractors acting in their capacity as such. And, as the *Nelson* and *Lawson-Ross* courts have made clear, state consumer protection laws regarding affirmative misrepresentations are not preempted. Thus, even if certain licensing regimes are preempted, state investigations into violations of state consumer protection laws are not preempted insofar as the underlying law is not preempted. We suggest that the Department work within that structure—rather than try and avoid the *Student Loan Servicing Alliance* and *PHEAA v. Perez* holdings—in order to draft a new interpretation that continues to give state regulatory agencies appropriate authorities to protect the interests of student loan borrowers.¹³

IV. Justification

As written, the Notice espouses an interpretation of federal law that limits the abilities for state-enforcement agencies and individual borrowers to sue student loan servicing companies. The Notice also espouses an interpretation of federal law that limits the ability of state regulators to supervise the conduct of student loan servicing companies. In light of the well-documented failures of student loan servicing companies, revoking and replacing the Notice will increase the extent to which state actors can oversee the student loan servicing industry and provide recourse to student loan borrowers that have been harmed.

¹¹ The *PHEAA v. Perez* decision was made without any deference to the Notice. See *PHEAA v. Perez*, 2020 WL 2079634, at *7 n.1 (“I need not determine whether Education’s interpretation of the preemptive effect of its regulations and the HEA is entitled to *Skidmore* deference”).

¹² As noted *supra* at n.3, in the lead-up to *PHEAA v. Perez*, the Department’s Office of the General Counsel interpreted the scope of preemption perhaps even more broadly than it did in the Notice, flatly asserting that “[s]tate laws regulating Direct Loan servicing are preempted by federal law.” See Letter from S. Dawn Scaniffe, Dep’t of Educ. Office of Gen. Counsel to Carmen Costa, Director, Consumer Credit Division, Connecticut Department of Banking (March 26, 2018) (filed in *PHEAA v. Perez*, No. 3:18-cv-01114 (D. Ct. Dec. 19, 2019) at Dkt. 67-14. In that same letter, the Office of the General Counsel also stated that because the document request at issue “cites to a state law that purports to license Direct Loan servicers and to regulate Direct Loan servicing,” the Connecticut state law is “inapplicable” under the routine use exception to the Privacy Act. See *infra* at n.6 (discussing the Privacy Act).

¹³ *PHEAA v. Perez* highlights a separate issue that merits consideration. Prior to the litigation, the Department maintained that PHEAA could not provide CT DOB with the requested records because of the Privacy Act of 1974, 5 U.S.C. § 552a. One exception to the restrictions under the Privacy Act is known as the “routine use” exception, which is defined as “the use of [a] record for a purpose which is compatible with the purpose for which it was collected.” 5 U.S.C. § 552a(a)(7). Each agency that maintains records in a “system of records” must publish in the Federal Register a notice regard its system of records (known as a “system of records notice” or “SORN”), which specifies “each routine use of the records contained in the system, including the categories of users and purpose of such use.” *Id.* § 552a(e)(4)(D). The Department claimed that the CT DOB request was not subject to the “routine use exception.” Although the SORN at issue in *PHEAA v. Perez* was published by the Department in September 2016, the Department revised the SORN in June 2018. See Notice of a Modified System of Records, Privacy Act of 1974, 83 Fed. Reg. 27,587 (June 13, 2018). As part of the process of revisiting the preemption issues discussed above, the Department should separately consider changes to the SORN and servicing contracts to ensure that state regulatory and law enforcement agencies have sufficient access to information. See generally *PHEAA v. Perez*, 2020 WL 2079634, at *12–*13 (same).

