

# INSOLVENCY, CREDITORS' RIGHTS & FINANCIAL PRODUCTS

>>ALERT

## CLAIMS AGAINST NAVIENT ECHO PROBLEMS WITH SUBPRIME MORTGAGE LOAN SERVICERS

Just as industry-wide litigation and investigations targeting subprime mortgage servicers began with lawsuits against the industry's largest players, the lawsuit filed recently by the Consumer Financial Protection Bureau (CFPB) against Navient Corporation, the nation's largest student loan servicer, may serve as a springboard for lawsuits against student loan servicers. In addition to providing a glimpse into potential trends in the industry, subprime mortgage litigation could provide a roadmap for student loan borrowers seeking to recover damages for potential servicer misconduct.

### THE NAVIENT SUIT

As discussed in more detail in our Alert, "[Recent Actions Against Navient May Expose Problems Contributing to the Student Loan Debt Crisis](#)," the CFPB alleges that Navient broadly (1) steered struggling borrowers toward paying more than necessary on their loans, (2) obscured information needed by borrowers to maintain lower payments, (3) deceived borrowers regarding requirements to release co-signers and (4) failed to properly process payments. According to the CFPB, Navient's conduct of misguiding and misleading borrowers with respect to their repayment options unnecessarily increased borrowers' debt burden, resulting in violations of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Fair Credit Reporting Act and the Fair Debt Collections Practices Act. On the same day Navient filed suit, the Attorneys General of Illinois and Washington commenced separate actions against Navient, alleging deceptive and predatory loan servicing and collection activities.

### THE BOTTOM LINE

The allegations in the recent CFPB action against Navient are reminiscent of the abusive tactics that the CFPB alleged subprime mortgage servicers employed against struggling borrowers, which ultimately led to record-setting settlements. Unlike mortgage loan servicers that have had an opportunity or were required to adjust their policies and procedures in response to the subprime mortgage era litigation, student loan servicers are just now entering the crosshairs. If, under the Trump Administration, the federal government is viewed as soft on enforcing consumer protections, there is the potential for substantial private litigation. As student loan servicers have not been challenged to date, such litigation may seek to reveal vulnerabilities in their procedures that may be said to have contributed to the mounting student debt crisis. Based on the extensive battery of actions that ensnared the mortgage industry for years, it appears the student loan servicing industry may be on the verge of following a similar course.

### THE POTENTIAL FOR FURTHER LITIGATION TO FOLLOW THE NAVIENT SUIT

Given that the Trump Administration and the Republican controlled Congress seem intent on disarming the CFPB and rolling back the Dodd Frank Act (as widely reported in the press), it is uncertain whether and how aggressively the CFPB will pursue the case against Navient. In the event the government

fails to pursue Navient or to investigate or pursue other student loan servicers, private litigation (*i.e.*, class actions and individual complaints by borrowers) may become the main means of recovery for any student borrowers that have been harmed by similar servicer misconduct. Although there are presently two class actions pending against Navient, they do not prohibit additional actions against Navient, either individually or by way of class action.

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In any event, the actions against Navient could be just the first in the industry. There are a number of student loan servicers in the United States, with Navient servicing the loans of more than 12 million borrowers, or roughly 30% of the market. Other large players include Great Lakes Education Loan Services, Nelnet and the Pennsylvania Higher Education Assistance Agency. Of the \$1.3 trillion in outstanding student loan debt held by more than 44 million student loan borrowers in the United States, the New York Fed estimates that over 11% is 90+days delinquent or in default (see The Federal Reserve Bank of New York's Quarterly Report on Household Debt and Credit (February 2017)). Moreover, of the amount actually in repayment, the New York Fed estimates that roughly 22% is 90+ days delinquent or in default. If the loan servicers for these loans engaged in or are engaging in similar practices as Navient or other conduct that may have contributed to defaults, more lawsuits could follow. Although one would hope for some degree of self-correction in the industry in response to the actions against Navient, it is not clear such correction happened during the litigation cycle in the mortgage industry, and in any event, any actionable conduct by student loan servicers may have already occurred. Ultimately, if student loan servicers are engaging in deceptive practices, they may not be willing to take corrective action until they are facing a lawsuit and the threat of real exposure.

## TRAJECTORY OF MORTGAGE LOAN SERVICER LITIGATION

Whether further litigation is pursued by the government or borrowers, there is precedent in the subprime mortgage space for litigation to spread from larger to smaller servicers. One of the earliest and most prominent actions against mortgage servicers was by the federal government and state attorneys general involving the five largest mortgage servicers – Bank of America Corporation, JPMorgan Chase & Co., Wells Fargo & Company, Citigroup Inc. and Ally Financial Inc. (formerly GMAC), which resulted in a \$25 billion settlement. This was followed by charges by the CFPB, attorneys general of 49 states and the District of Columbia against Ocwen Financial Corporation, the largest nonbank mortgage servicer in the country, alleging violations of state laws and the Dodd-Frank Act, which resulted in a \$2 billion settlement. The CFPB thereafter moved against smaller servicers, such as Flagstar Bank, which agreed to pay a \$37.5 million settlement, and Residential Credit Solutions, Inc., which paid \$1.5 million in restitution and a \$100,000 civil money penalty.

## CLAIMS AGAINST NAVIENT ECHO MORTGAGE SERVICING COMPLAINTS

The CFPB's allegations in the Navient action are similar to allegations that subprime mortgage servicers engaged in servicer misconduct in the years leading up to the financial crisis. Although the list of sins allegedly committed by mortgage servicers often related to mortgage foreclosure procedures, as with the allegations

against Navient, they were nevertheless premised on the servicers' allegedly misguiding and misleading struggling borrowers in connection with loss mitigation options. For example, the allegations against mortgage servicers included claims that they failed to offer non-foreclosure alternatives before foreclosing on borrowers (Bank of America), deceived consumers about foreclosure alternatives and improperly denied loan modifications (Ocwen), failed to advise borrowers of incomplete loan modification applications and denied modifications to qualified borrowers (Flagstar). As the allegations in the Navient action suggest that student loan servicers may be engaging in a pattern of similar deceptive conduct, the prior subprime mortgage loan servicer actions will be instructive for plaintiffs and defendants in the student loan space going forward.

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