Issue Paper 1
Session 2: January 8-11, 2018

Issue: Whether to establish a Federal standard for the purpose of determining if a borrower can establish a defense to the repayment of a Direct Loan or recover for amounts already paid on a Direct Loan based on an act or omission of an institution.

Statutory cite: §455(h) of the Higher Education Act of 1965, as amended

Regulatory cite: 34 CFR 685.206(c), 685.222, 685.300, 685.308

Summary of changes: Creates a regulatory section that establishes, for loans first disbursed on or after July 1, 2019, a new Federal standard applicable to borrower defense claims made by borrowers and for Department recovery actions against institutions. Under the proposed regulations, borrowers with an eligible Direct Loan would be entitled to a discharge (or recover amounts already paid) of all or a portion of the loan if the borrower establishes either: (1) an institutional misrepresentation, (2) a court judgment against an institution, or (3) a final judgment from an arbitrator against an institution. The proposed regulations would also describe in detail how a borrower establishes the basis for a claim.

Changes: See regulatory text below.

[Note to negotiators: §685.222 is a new section. For ease of readability and editing during negotiated rulemaking, the section is formatted as plain text, rather than redline.]

§685.222 Borrower defense and Department recovery actions against institutions

(a) *Introduction*.

(1) For the purposes of this section and § 685.206(c), a "borrower defense" refers to an act or omission of an institution at which the borrower enrolled that relates to the making of a Direct Loan for enrollment at the institution or the provision of educational services for which the loan was made, and includes one or both of the following:

(i) A defense to the repayment of amounts owed to the Secretary on a Direct Loan, in whole or in part; and

(ii) A right to recover amounts previously collected by the Secretary on the Direct Loan, in whole or in part.

(2) A borrower may assert a borrower defense of a Direct Consolidation Loan that repaid a Direct Loan, FFEL Program Loan, Federal Perkins Loan, Health Professions Student Loan, or Loan for Disadvantaged

Students under subpart II of part A of title VII of the Public Health Service Act; or a Health Education Assistance Loan, or Nursing Loan made under part E of the Public Health Service Act on which the borrower had a basis for a borrower defense claim prior to the consolidation.

(3) For loans first disbursed prior to July 1, 2019, the borrower may assert a borrower defense of a Direct Loan consistent with section 685.206(c).

(4) For loans first disbursed on or after July 1, 2019, the borrower may assert a borrower defense of a Direct Loan consistent with this section.

(5) The Department may initiate a recovery action against an institution consistent with paragraph (c) of this section.

(6) The Department administers this section consistent with the procedures described in section 685.206(c) and 34 CFR Part 668, Subpart G.

(b) *Borrower defense*.

(1) For loans first disbursed on or after July 1, 2019, the Secretary will discharge the borrower's obligation to repay a Direct Loan and will refund amounts paid on the loan, in whole or in part, less any amounts already refunded to the borrower from any source pursuant to section 685.206(d)(8), if the borrower establishes a defense by clear and convincing evidence that--

(i) The institution at which the borrower enrolled acted with an intent to deceive, knowledge of the falsity of a misrepresentation, or a reckless disregard for the truth in making a misrepresentation of material fact, opinion, intention, or law upon which the borrower reasonably relied in deciding to obtain a Direct Loan to enroll or continue enrollment in a program at the institution, and which resulted in financial harm to the borrower;

(ii) The borrower has obtained, from a court of competent jurisdiction, a nondefault contested State or Federal judgment and was awarded monetary damages against the institution relating to the loan or the provision of educational services for which the loan was obtained; or

(iii) The borrower has obtained, from an arbitrator or a hearing official in a State or Federal administrative tribunal agreed to by the borrower and the institution, a nondefault contested judgment, or equivalent final determination, and was awarded monetary damages against the institution relating to the loan or the provision of educational services for which the loan was obtained.

(2) For the purposes of this section—

(i) A misrepresentation is a statement, act, or omission by an institution that would mislead a reasonable person regarding the nature of the educational program, the nature of financial charges, the employability of graduates of an educational program, the eligibility of the educational program for licensure or certification, the State agency authorization or approval of the educational program, or an accreditor approval of an institution or educational program. Evidence that a misrepresentation described in paragraph (b)(1)(i) of this section has occurred includes, but is not limited to:

(A) Actual licensure passage rates materially different from those included in the institution's marketing materials, website, or other communication made to the student;

(B) Actual job placement rates materially different from those included in the institution's marketing materials, website, or other communication made to the student;

(C) The inclusion in the institution's marketing materials, website, or other communication made to the student of specialized, programmatic, or institutional certifications or approvals not actually obtained or the failure to remove within a reasonable period of time such certifications or approvals from marketing materials, website, or other communication when invalidated or withdrawn;

(D) The inclusion in the institution's marketing materials, website, or other communication made to the student of representations regarding the widespread or general transferability of credits that are only transferrable to limited types of programs or institutions or the transferability of credits to a specific program or institution when no reciprocal agreement exists with another institution or such agreement is materially different than what was represented;

(E) A representation regarding the employability or specific earnings of graduates without an agreement between the institution and another entity for such employment or sufficient evidence of past employment or earnings to justify such a representation;

(F) A representation regarding the availability, amount, or nature of any financial assistance available to students from the institution or any other entity to pay the costs of attendance at the institution that is not fulfilled following the enrollment of the borrower;

(G) A representation regarding the amount of tuition and fees that the student would be charged for the program that is materially different in amount, method, or timing of payment from the actual tuition and fees charged to the student;

(H) A representation that the institution, its courses, or programs are endorsed by vocational counselors, high schools, colleges, educational organizations, employment agencies, members of a particular industry, students, former students, or governmental officials when no such endorsements exist as stated;

(I) A representation regarding the institution's size, location, facilities, training equipment or the number, availability, or qualifications of its personnel that are materially different from the institution's actual circumstances at the time the representation is made;

(J) The nature or extent of prerequisites for enrollment in a course or program; or

(K) Any other circumstances as determined by the Secretary.

(ii) A violation by the institution of a requirement of the Higher Education Act or the Department's regulations is not a basis for a borrower defense claim unless the violation would otherwise give rise to a successful borrower defense claim under this section or section 685.206(c), as applicable. The Secretary will not approve a borrower defense claim under this section or section 685.206(c) of this Part when the borrower submits a claim based on—

(A) Personal injury;

(B) Sexual harassment;

(C) A violation of civil rights;

(D) Slander or defamation;

(E) Property damage claims;

(F) Educational malpractice, which is a tortious claim about the general quality of the student's education or the reasonableness of an educator's conduct in providing educational services; or

(G) Academic disputes and disciplinary matters.

(iii) Financial harm to the borrower has occurred when the borrower suffers monetary loss as a consequence of a misrepresentation described in paragraph (b)(1)(i) of this section or as found by a court, arbitrator, or hearing official pursuant to a judgment as described in paragraphs (b)(1)(ii) and (b)(1)(iii). Financial harm does not include damages for nonmonetary loss such as inconvenience, aggravation, emotional distress, pain and suffering, punitive damages, or opportunity costs. Financial harm is such monetary loss that is not predominantly due to intervening local, regional, or national economic or labor market conditions. Evidence of financial harm includes, but is not limited to the following circumstances:

(A) A significant difference between the borrower's earnings after completing the program and the earnings listed for the borrower's program of study in the institution's marketing materials, website, or other communication made to the student;

(B) A significant difference between the borrower's earnings after completing the program and the earnings for similar borrowers employed in the program's intended occupational field, determined by, for example, earnings below the lowest income quintile for the program of study's intended occupational field according to the Standard Occupational Classification (SOC) code as published by the U.S. Bureau of Labor Statistics;

(C) Lower or lost wages, extended periods of involuntary unemployment, or the cost of obtaining nontransferable credits;

(D) A significant difference in the amount or nature of the tuition and fees charged by the institution for which the Direct Loan was disbursed and the amount or nature of the tuition and fees the borrower reasonably believed the institution would charge or was charging;

(E) The borrower's inability to secure employment in the field of study for which the institution expressly guaranteed employment; or

(F) The borrower's inability to complete the program because the institution no longer offers a requirement necessary for completion of the program in which the borrower enrolled.

(3) The Secretary may determine at any time that a borrower defense claim should not be approved based on evidence that rebuts the borrower's claim, including any evidence provided by the institution at which the borrower enrolled. Such evidence may include, but is not limited to--

(i) For a claim based on licensure exam passage rates, the institution or program has a licensure exam passage rate associated with the program in which the borrower enrolls that, at a minimum, reasonably approximates the passage rates included in the institution's marketing materials, website, or other communication made when recruiting the student;

(ii) For a claim based on the inability of the borrower to obtain the necessary certification or licensure for employment in the program's intended field of employment, the borrower has obtained a certification or licensure related to the program in which the borrower enrolled without needing to complete additional coursework after completing the program;

(iii) The institution provided information to the borrower to correct the misrepresentation prior to the borrower enrolling in the program; or

(iv) The institution demonstrated that its representative or agent made a misrepresentation that was inconsistent with or prohibited by the institution's policies, procedures and training at the time it was made.

(4) For purposes of this section, the term "institution" includes an eligible institution, its representatives and agents, or any institution, organization, or person with whom the eligible institution has an agreement to provide educational programs, or to provide marketing, advertising, recruiting or admissions services.

(c) *Department recovery actions against institutions*. The Secretary may initiate a recovery action against an institution when the Secretary determines that the borrower has asserted a successful borrower defense against the institution as described in this section or section 685.206(c) of this Part.

(d) *Limitations period*. A borrower must file a claim under paragraph (b)(1) of this section within three years of the date the borrower discovered, or reasonably should have discovered, the misrepresentation.

§685.300 Agreements between an eligible school and the Secretary for participation in the Direct Loan Program.

(a) *General*. Participation of a school in the Direct Loan Program means that eligible students at the school may receive Direct Loans. To participate in the Direct Loan Program, a school must—

* * *

(8) Accept responsibility and financial liability stemming from its failure to perform its functions pursuant to the agreement;

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* * *

(11) Accept responsibility and financial liability stemming from losses incurred by the Secretary for repayment of amounts discharged by the Secretary pursuant to sections 685.206, 685.214, 685.216, and 685.222;

§685.308 Remedial actions.

(a) *General*. The Secretary may require the repayment of funds and the purchase of loans by the school if the Secretary determines that the school is liable as a result of-- --

Deleted: the unenforceability of a loan or loans, or the disbursement of loan amounts for which the borrower was ineligible, resulted in whole or in part from

(1) The school's violation of a Federal statute or regulation;

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(2) The school's negligent or willful false certification under section 685.215; or

(3) The school's actions that gave rise to a successful claim for which the Secretary discharged a loan, in whole or in part, pursuant to sections 685.206, 685.214, 685.216, and 685.222.

Issue Paper 2
Session 2: January 8 -11, 2018

Issue: Developing a regulatory framework for the process of submitting and evaluating a borrower defense (BD) to repayment claim.

Statutory cite: §455(h) of the Higher Education Act of 1965, as amended

Regulatory cites: 34 CFR 682.211, 682.410, 685.205, 685.206, and 685.212

Summary of change:

Establishes a regulatory framework for processing BD claims for Direct Loans first disbursed on or after July 1, 2019, including provisions for:

- Forbearance
- The application process
- Adjudication of a BD claim
- Notification of the borrower and school of the Department's decision
- Reconsideration of denials
- Relief that a borrower may receive if a BD claim is approved

Changes: See regulatory text below.

§682.211 Forbearance

(i) *Mandatory administrative forbearance.*

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(7) The lender must grant a mandatory administrative forbearance to a borrower upon being notified by the Secretary that the borrower has made a borrower defense claim related to a loan that the borrower intends to consolidate into the Direct Loan Program for the purpose of seeking relief in accordance with section 685.212(k). The lender must grant mandatory administrative forbearance in yearly increments or for a period designated by the Secretary, until the loan is consolidated or the lender is notified by the Secretary to discontinue the forbearance.

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§682.410 Fiscal, Administrative, and Enforcement Requirements

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(b) * * *

(6) *Collection efforts on defaulted loans.*

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(viii) Upon notification by the Secretary that the borrower has made a borrower defense claim related to a loan that the borrower intends to consolidate into the Direct Loan Program for the purpose of seeking relief in accordance with section 685.212(k), the guaranty agency must suspend all collection activities on the affected loan for the period designated by the Secretary.

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§685.205 Forbearance

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(b) *Administrative forbearance.* In certain circumstances, the Secretary grants forbearance without requiring documentation from the borrower. These circumstances include but are not limited to—

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(6) Periods necessary for the Secretary to determine the borrower's eligibility for discharge—

(i) Under §685.206

(ii) Under §685.214;

(iii) Under §685.215;

(iv) Under §685.216;

(v) Under §685.217;

(vi) Under §685.222; or

(vii) Due to the borrower's or endorser's (if applicable) bankruptcy;

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§685.206 Borrower responsibilities and defenses.

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(c) *Borrower defenses for loans first disbursed prior to July 1, 2019* (1) In any proceeding to collect on a Direct Loan first disbursed prior to July 1, 2019, the borrower may assert as a defense against repayment any act or omission of the school attended by the student that would give rise to a cause of action against the school under applicable State law. These proceedings include, but are not limited to, the following:

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(i) Tax refund offset proceedings under 26 U.S.C. 6402(d), 31 U.S.C. 3716 and 3720A.

Deleted: 34 CFR 30.33.

(ii) Wage garnishment proceedings under section 488A of the Act or under 31 U.S.C. 3720D and regulations at 34 CFR part 34.

(iii) Salary offset proceedings for Federal employees under 34 CFR part 31, 5 U.S.C. 5514 and 31 U.S.C. 3716.

(iv) Consumer reporting agency reporting proceedings under 31 U.S.C. 3711(f).

(2) If the borrower's defense against repayment claim is successful, the Secretary notifies the borrower that the borrower is relieved of the obligation to repay all or part of the loan and associated costs and fees that the borrower would otherwise be obligated to pay. The Secretary affords the borrower such further relief as the Secretary determines is appropriate under the circumstances. Further relief may include, but is not limited to, the following:

(i) Reimbursing the borrower for amounts paid toward the loan voluntarily or through enforced collection.

(ii) Determining that the borrower is not in default on the loan and is eligible to receive assistance under title IV of the Act.

(iii) Updating reports to consumer reporting agencies to which the Secretary previously made adverse credit reports with regard to the borrower's Direct Loan.

(3) The Secretary may initiate an appropriate proceeding to require the school whose act or omission resulted in the borrower's successful defense against repayment of a Direct Loan to pay to the Secretary the amount of the loan to which the defense applies in accordance with 34 CFR 668 subpart G.

Deleted: However, the Secretary does not initiate such a proceeding after the period for the retention of records described in §685.309(c) unless the school received actual notice of the claim during that period.

(d) *Borrower defenses for loans first disbursed on or after July 1, 2019*.(1) To assert a borrower defense under § 685.221, a borrower must submit an application on a form approved by the Secretary—

(i) Certifying that the borrower received the proceeds of a loan to attend the named school;

(ii) Providing documentation that supports the borrower defense claim; and

(iii) Indicating whether the borrower has made a claim based on the information underlying the borrower defense with any third party, such as the holder of a performance bond or a tuition recovery program, and, if so, the amount of any payment received by the borrower or credited to the borrower's loan obligation.

(2) *Forbearance and suspension of collection activity*. (i) Upon receipt of a borrower's application and at the request of the borrower the Secretary

(A) Grants forbearance if the borrower is not in default on the loan for which a borrower defense has been asserted; or

(B) Suspends collection activity on a defaulted loan until the Secretary issues a decision on the borrower's claim.

(ii) Interest that accrues during the forbearance period or during the suspension of collection activity is not capitalized.

(iii) If the borrower's claim is denied, the forbearance or suspension of collection activity will not be reinstated if the borrower resubmits that claim, unless the resubmission meets the eligibility criteria in paragraph (e)(5) of this section.

(3) *Adjudication of borrower defense claim.* The Secretary determines whether the borrower has presented a qualifying borrower defense claim in accordance with the standards in § 685.222.

(i) Within 60 days of the date of the Department's receipt of the borrower defense application, the Secretary provides written notice of the submission of the borrower defense application and a copy of the application to the school. The notice to the school provides the school with the opportunity to submit a response to the borrower defense claim, including any relevant documentation or information, to the Department.

(ii) In resolving the borrower defense claim the Secretary will consider relevant evidence, including, --

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(A) Department records;

(B) The borrower defense application and any supporting documentation submitted by the borrower; and

(C) Any response or information submitted by the school.

(iii) In resolving the borrower defense claim, the Secretary may also consider other relevant information obtained by the Secretary.

(4) *Written decision.* The Secretary issues a written decision--

(i) Notifying the borrower and the school of the decision;

(ii) Providing the reasons for the decision;

(iii) Informing the borrower of the relief, if any, that the borrower will receive; and

(iv) Informing the borrower and the school of their opportunity to request reconsideration of the claim based on newly discovered evidence pursuant to paragraph (d)(5) of this section.

(5) *Reconsideration of denials*. The decision of the Secretary is final as to the merits of the borrower's claim and any relief that may be granted on the claim. Notwithstanding the foregoing—

(i) If the borrower defense application is denied in full or in part, the borrower may request that the Secretary reconsider the borrower defense upon the submission of newly discovered evidence which supports the borrower's claim.

(ii) If the borrower defense is granted in full or in part, the school may request that the Secretary reconsider the borrower defense upon the submission of newly discovered evidence in support of the school's defense.

(iii) If the Secretary accepts a borrower's request for reconsideration, the Secretary follows the procedures in paragraph (d)(2) of this section for granting forbearance or suspending collection activity, as applicable, and also notifies the borrower and the school that the Secretary has taken such action.

(iv) A request for reconsideration must be submitted within 60 days of the date the written decision under paragraph (d)(4) of this section is issued.

(v) "Newly discovered evidence" is relevant evidence that the borrower or the school, with reasonable diligence, could not have discovered prior to the Secretary's decision on the borrower defense claim and was not relied upon by the Secretary in determination of the borrower defense claim.

(6) *Relief.* If the Secretary grants a borrower's application for a discharge based on the borrower's claim of a borrower defense, the Secretary notifies the borrower and the school that the borrower is relieved of the obligation to repay all or part of the loan and associated costs and fees that the borrower would otherwise be obligated to pay. The Secretary affords the borrower such further relief as the Secretary determines is appropriate under the circumstances. Further relief includes, if applicable:

(i) Reimbursing the borrower for amounts paid toward the loan voluntarily or through enforced collection;

(ii) Determining that the borrower is not in default on the loan and is eligible to receive assistance under title IV of the Act; and

(iii) Updating reports to consumer reporting agencies to which the Secretary previously made adverse credit reports with regard to the borrower's Direct Loan.

(7) *Cooperation by the borrower.* The Secretary may revoke any relief granted to a borrower who fails to cooperate with the Secretary in any proceeding under paragraph (d) of this section or under § 685.222. Such cooperation includes, but is not limited to--

(i) Providing testimony regarding any representation made by the borrower to support a request for discharge; and

(ii) Producing, within timeframes established by the Secretary, any documentation reasonably available to the borrower with respect to those representations and any sworn statement required by the Secretary with respect to those representations and documents.

(8) *Transfer to the Secretary of the borrower's right of recovery against third parties.* (i) Upon the granting of any relief under this section, the borrower is deemed to have assigned to, and relinquished in favor of, the Secretary any right to a loan refund (up to the amount discharged) that the borrower may have by contract or applicable law with respect to the loan or the provision of educational services for which the loan was received, against the school its principals, its affiliates, and their successors or its sureties and any private fund. If the borrower asserts a claim to, and recovers from, a public fund, the

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Secretary may reinstate the borrower's obligation to repay on the loan an amount based on the amount recovered from the public fund, if the Secretary determines that the borrower's recovery from the public fund was based on the same borrower defense and for the same loan for which the discharge was granted under this section.

(ii) The provisions of this paragraph (d)(8) apply notwithstanding any provision of State law that would otherwise restrict transfer of those rights by the borrower, limit or prevent a transferee from exercising those rights, or establish procedures or a scheme of distribution that would prejudice the Secretary's ability to recover on those rights.

(iii) Nothing in this paragraph (d)(8) limits or forecloses the borrower's right to pursue legal and equitable relief arising under applicable law against a party described in this paragraph (d)(8) for recovery of any portion of a claim exceeding that assigned to the Secretary or any other claims arising from matters unrelated to the claim on which the loan is discharged.

(9) *Recovery from the school.* The Secretary may initiate an appropriate proceeding to require the school whose act or omission resulted in the borrower's successful defense against repayment of a Direct Loan to pay to the Secretary the amount of the loan to which the defense applies in accordance with 34 CFR 668 subpart G.

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§685.212 Discharge of a Loan Obligation

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(k) *Borrower defenses*. (1) If a borrower's application for a discharge of a loan based on a borrower defense is approved under the standards set forth in §§ 685.206(c) or 685.222, the Secretary discharges the obligation of the borrower, in whole or in part, in accordance with the procedures described in §§ 685.206(c) or 685.206(d) respectively.(2) In the case of a Direct Consolidation Loan, a borrower may assert a borrower defense under the standards set forth in §§ 685.206(c) or 685.222 with respect to a loan that was repaid by the Direct Consolidation Loan.

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(i) The Secretary considers a borrower defense claim asserted on a Direct Consolidation Loan by determining--

(A) Whether the act or omission of the school with regard to the loan described in paragraph (k)(2) of this section, other than a Direct Subsidized, Unsubsidized, or PLUS Loan, establishes a borrower defense under § 685.206(c) for a Direct Consolidation Loan made before July 1, 2019, or under the standard set forth in § 685.222, for a Direct Consolidation Loan made on or after July 1, 2019; or

(B) Whether the act or omission of the school with regard to a Direct Subsidized, Unsubsidized, or PLUS Loan made on or after July 1, 2019 that was paid off by the Direct Consolidation Loan, establishes a borrower defense under § 685.222.

(ii) If the borrower defense claim is approved, the Secretary discharges the appropriate portion of the Direct Consolidation Loan.

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Issue Paper 3

Session 2: January 8-11, 2018

Issue: Financial Responsibility and Administrative Capability

Statutory cite: §498 of the Higher Education Act of 1965, as amended

Regulatory cite: 34 CFR 668.171, 668.175

Summary of changes: For institutions that are not financially responsible, we propose to expand the types of financial protection those institutions may provide. In addition, we propose to recalculate the composite score for institutions that incur debts and liabilities from borrower defense claims.

Changes: See regulatory text below.

§ 668.171 General.

(a) Purpose. To begin and to continue to participate in any title IV, HEA program, an institution must demonstrate to the Secretary that it is financially responsible under the standards established in this subpart. As provided under section 498(c)(1) of the HEA, the Secretary determines whether an institution is financially responsible based on the institution's ability to--

(1) Provide the services described in its official publications and statements;

(2) Meet all of its financial obligations; and

(3) Provide the administrative resources necessary to comply with title IV, HEA program requirements.

(b) General standards of financial responsibility. Except as provided under paragraph (c) of this section, the Secretary considers an institution to be financially responsible if the Secretary determines that--

(1) The institution's Equity, Primary Reserve, and Net Income ratios yield a composite score of at least 1.5, as provided under § 668.172 and appendices A and B to this subpart;

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(2) The institution has sufficient cash reserves to make required returns of unearned title IV, HEA program funds, as provided under § 668.173;

(3) The institution is current in its debt payments. An institution is not current in its debt payments if—

(i) It is in violation of any existing loan agreement at its fiscal year end, as disclosed in a note to its audited financial statements or audit opinion; or

(ii) It fails to make a payment in accordance with existing debt obligations for more than 120 days, and at least one creditor has filed suit to recover funds under those obligations;

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(4) The institution is otherwise able to meet all of its financial obligations and otherwise provide the administrative resources necessary to comply with title IV, HEA program requirements. An institution may not be able to meet its financial or administrative obligations if it is subject to an action or event described in paragraph (c) of this section. The Secretary may consider those actions or events in determining whether the institution is financially responsible; and

(5) The institution or persons affiliated with the institution are not subject to a condition of past performance under § 668.174(a) or (b).

(c) Other factors or events. The Secretary may determine that an institution is not able to meet its financial or administrative obligations under paragraph (b)(4) of this section if—

(1) After the end of the fiscal year for which the Secretary has most recently calculated an institution's composite score, the institution incurs a debt or liability from borrower defense claims adjudicated by the Secretary, and as a result of that debt or liability the institution's recalculated composite score is less than 1.0, as determined by the Secretary under paragraph (d) of this section;

(2) For a proprietary institution whose composite score is less than 1.5, there is a withdrawal of owner's equity from the institution by any means, including by declaring a dividend. This

provision does not apply if the withdrawal is a transfer to an entity included in the affiliated entity group on whose basis the institution's composite score was calculated;

(3) For a publicly traded institution, the institution is currently subject to one or more of the following actions or events—

(i) The SEC warns the institution that it may suspend trading on the institution's stock;

(ii) The institution failed to file a required annual or quarterly report with the SEC within the time period prescribed for that report or by any extended due date under 17 CFR 240.12b-25; or

(iii) The exchange on which the institution's stock is traded notifies the institution that it is not in compliance with exchange requirements, or its stock is delisted; or

(4) For its most recently completed fiscal year, a proprietary institution did not derive at least 10 percent of its revenue from sources other than title IV, HEA program funds, as provided under § 668.28(c).

(d) Recalculating the composite score. As specified in Appendix C of this subpart, the Secretary recognizes and accounts for the actual debt or liability incurred by an institution for borrower defense claims under paragraph (c)(1) of this section and based on that accounting, may recalculate the institution's most recent composite score using the financial statements on which the institution's composite score has been calculated under § 668.172.

(e) Reporting requirements. (1) In accordance with procedures established by the Secretary, an institution must notify the Secretary of the actions or events identified in paragraph (c) of this section no later than--

(i) For a withdrawal of owner's equity described in paragraph (c)(2), 10 days after the withdrawal is made. In its notice to the Secretary, the institution must identify whether the reported withdrawal of owner's equity was used exclusively to meet tax liabilities of the institution or its owners for income derived from the institution;

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(ii) For the SEC and stock exchange provisions for publicly traded institutions described in paragraph (c)(3), 10 days after the SEC or exchange warns, notifies, or takes an action against the institution, or 10 days after any extension granted by the SEC; or

(iii) For the non-title IV revenue provision in paragraph (c)(4), 45 days after the end of the institution's fiscal year, as provided in § 668.28(c)(3).

(2) The Secretary may take an administrative action under paragraph (h) of this section against the institution if it fails to provide timely notice of the actions or events under this paragraph.

(f) Public institutions. (1) The Secretary considers a domestic public institution to be financially responsible if the institution--

Deleted: (ii) Repayments to the Secretary for debts and liabilities arising from the institution's participation in the title IV, HEA programs ... [2]

(i)(A) Notifies the Secretary that it is designated as a public institution by the State, local, or municipal government entity, tribal authority, or other government entity that has the legal authority to make that designation; and

(B) Provides a letter from an official of that State or other government entity confirming that the institution is a public institution; and

(ii) Is not subject to a condition of past performance under § 668.174.

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(2) The Secretary considers a foreign public institution to be financially responsible if the institution--

(i)(A) Notifies the Secretary that it is designated as a public institution by the country or other government entity that has the legal authority to make that designation; and

(B) Provides documentation from an official of that country or other government entity confirming that the institution is a public institution and is backed by the full faith and credit of the country or other government entity; and

(ii) Is not subject to a condition of past performance under § 668.174.

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(g) Audit opinions. Even if an institution satisfies all of the general standards of financial responsibility under paragraph (b) of this section, the Secretary does not consider the institution to be financially responsible if, in the institution's audited financial statements, the opinion expressed by the auditor was an adverse, qualified, or disclaimed opinion, or the auditor expressed doubt about the continued existence of the institution as a going concern, unless the Secretary determines that a qualified or disclaimed opinion does not significantly bear on the institution's financial condition.

(h) Administrative actions. If the Secretary determines that an institution is not financially responsible under the standards and provisions of this section or under an alternative standard in § 668.175, or the institution does not submit its financial and compliance audits by the date and in the manner required under § 668.23, the Secretary may--

(1) Initiate an action under subpart G of this part to fine the institution, or limit, suspend, or terminate the institution's participation in the title IV, HEA programs; or

(2) For an institution that is provisionally certified, take an action against the institution under the procedures established in § 668.13(d).

§ 668.175 Alternative standards and requirements.

(a) *General.* An institution that is not financially responsible under the general standards and provisions in §668.171, may begin or continue to participate in the title IV, HEA programs by qualifying under an alternate standard set forth in this section.

(b) *Letter of credit alternative for new institutions.* A new institution that is not financially responsible solely because the Secretary determines that its composite score is less than 1.5, qualifies as a financially responsible institution by submitting an irrevocable letter of credit or other surety described under paragraph (h)(1)(i) of this section, that is acceptable and payable to the Secretary, for an amount equal to at least one-half of the amount of title IV, HEA program

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funds that the Secretary determines the institution will receive during its initial year of participation. A new institution is an institution that seeks to participate for the first time in the title IV, HEA programs.

(c) Letter of credit alternative for participating institutions. A participating institution that is not financially responsible either because it does not satisfy one or more of the standards of financial responsibility under § 668.171(b) or (c), or because of an audit opinion described under § 668.171(g), qualifies as a financially responsible institution by submitting an irrevocable letter of credit or other financial protection described under paragraph (h) of this section, that is acceptable and payable to the Secretary, for an amount determined by the Secretary that is not less than one-half of the title IV, HEA program funds received by the institution during its most recently completed fiscal year.

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(d) Zone alternative. (1) A participating institution that is not financially responsible solely because the Secretary determines that its composite score under § 668.172 is less than 1.5 may participate in the title IV, HEA programs as a financially responsible institution for no more than three consecutive years, beginning with the year in which the Secretary determines that the institution qualifies under this alternative.

(i)(A) An institution qualifies initially under this alternative if, based on the institution's audited financial statement for its most recently completed fiscal year, the Secretary determines that its composite score is in the range from 1.0 to 1.4; and

(B) An institution continues to qualify under this alternative if, based on the institution's audited financial statement for each of its subsequent two fiscal years, the Secretary determines that the institution's composite score is in the range from 1.0 to 1.4.

(ii) An institution that qualified under this alternative for three consecutive years, or for one of those years, may not seek to qualify again under this alternative until the year after the institution achieves a composite score of at least 1.5, as determined by the Secretary.

(2) Under the zone alternative, the Secretary--

(i) Requires the institution to make disbursements to eligible students and parents, and to otherwise comply with the provisions, under either the heightened cash monitoring or reimbursement payment method described in § 668.162;

(ii) Requires the institution to provide timely information regarding any of the following oversight and financial events--

(A) Any event that causes the institution, or related entity as defined in Accounting Standards Codification (ASC) 850, to realize any liability that was noted as a contingent liability in the institution's or related entity's most recent audited financial statement; or

(B) Any losses that are unusual in nature or infrequently occur, or both, as defined in accordance with Accounting Standards Update (ASU) No. 2015-01 and ASC 225;

(iii) May require the institution to submit its financial statement and compliance audits earlier than the time specified under § 668.23(a)(4); and

(iv) May require the institution to provide information about its current operations and future plans.

(3) Under the zone alternative, the institution must--

(i) For any oversight or financial event described in paragraph (d)(2)(ii) of this section for which the institution is required to provide information, in accordance with procedures established by the Secretary, notify the Secretary no later than 10 days after that event occurs; and

(ii) As part of its compliance audit, require its auditor to express an opinion on the institution's compliance with the requirements under the zone alternative, including the institution's

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(4) If an institution fails to comply with the requirements under paragraph (d)(2) or (3) of this section, the Secretary may determine that the institution no longer qualifies under this alternative.

(e) [Reserved]

(f) Provisional certification alternative. (1) The Secretary may permit an institution that is not financially responsible to participate in the title IV, HEA programs under a provisional certification for no more than three consecutive years if, as determined annually by the Secretary--

(i) The institution is not financially responsible because it does not satisfy the general standards under § 668.171(b), its recalculated composite score under § 668.171(d) is less than 1.0, is subject to an action or event under § 668.171(c), or because of an audit opinion described in § 668.171(g); or

(ii) The institution is not financially responsible because of a condition of past performance, as provided under § 668.174(a), and the institution demonstrates to the Secretary that it has satisfied or resolved that condition; and

(iii) The institution provides to the Secretary an irrevocable letter of credit that is acceptable and payable to the Secretary, or other financial protection described under paragraph (h) of this section, for an amount determined by the Secretary that is not less than 10 percent of the title IV, HEA program funds received by the institution during its most recently completed fiscal year.

(2) Under this alternative, the institution must comply with the provisions of the zone alternative, as provided under paragraph (d)(2) and (3).

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Deleted: (e) *Transition year alternative.* A participating institution that is not financially responsible solely because the Secretary determines that its composite score is less than 1.5 for the institution's fiscal year that began on or after July 1, 1997 but on or before June 30, 1998, may qualify as a financially responsible institution under the provisions in §668.15(b)(7), (b)(8), (d)(2)(ii), or (d)(3), as applicable.

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(3) If at the end of the period for which the Secretary provisionally certified the institution, the institution is still not financially responsible, the Secretary--

(i) May permit the institution to participate under a provisional certification, but--

(A) May require the institution, or one or more persons or entities that exercise substantial control over the institution, as determined under § 668.174(b)(1) and (c), or both, to provide to the Secretary financial protection for an amount determined by the Secretary; and

(B) May require one or more of the persons or entities that exercise substantial control over the institution, as determined under § 668.174(b)(1) and (c), to be jointly or severally liable for any liabilities that may arise from the institution's participation in the title IV, HEA programs; and

(ii) May permit the institution to continue to participate under a provisional certification but requires the institution to provide, or continue to provide, the financial protection resulting from an event described in § 668.171(c) until the institution meets the requirements of paragraph (f)(5) of this section.

* * * * *

(h) Financial protection. (1) In lieu of providing a letter of credit for the amount determined by the Secretary under this section, the Secretary may permit an institution to—

(i) Provide the amount required under this section in the form of other surety or form of financial protection as specified by the Secretary in a notice published in the Federal Register;

(ii) Provide cash for the amount required under this section; or

(iii) Enter into an arrangement under which the Secretary offsets the amount of title IV, HEA program funds that an institution has earned in a manner that ensures that, no later than the end of a nine-month period, the amount offset equals the amount of financial protection the institution is required to provide. The Secretary uses the funds to satisfy the debts and liabilities owed to the Secretary that are not otherwise paid directly by the institution, and provides to the

Deleted: may again permit the institution to participate under a provisional certification, but the Secretary—

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Deleted: g) *Provisional certification alternative for persons or entities owing liabilities.* (1) The Secretary may permit an institution that is not financially responsible because

Deleted: persons or entities that exercise substantial control over the institution owe a liability for a violation of a title IV, HEA program requirement,

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Deleted: (iii) The institution submits to the Secretary an irrevocable

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Deleted: that is not less than 10 percent of the title IV, HEA program funds received by the institution during its most recently completed fiscal year.

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Deleted: to be sufficient to satisfy any potential liabilities that may arise from the institution's participation in the title IV, HEA programs; and institution any funds not used for this purpose during the period covered by the agreement, or provides the institution any remaining funds if the institution subsequently submits a letter of credit or other surety under this paragraph.

Deleted: (iii) May require one or more of the persons or entities that exercise substantial control over the institution to be jointly or severally liable for any liabilities that may arise from the institution's participation in the title IV, HEA programs.

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Administer properly the title IV, HEA programs in which it participates; and

(3)

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(ii) Repayments to the Secretary for debts and liabilities arising from the institution's participation in the title IV, HEA programs

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—

(1) In

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(2) As provided under the past performance provisions in §668.174 (a) and (b)(1), the institution violated a title IV, HEA program requirement, or the persons or entities affiliated with the institution owe a liability for a violation of a title IV, HEA program requirement.

(e) *Administrative actions.*

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Any adverse action, including a probation or similar action, taken against the institution by its accrediting agency;

(B)

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violation by the institution of any loan agreement;

(D) Any failure of the institution to make a payment in accordance with its debt obligations

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results in a creditor filing suit to recover funds under those obligations;

(E) Any withdrawal of owner's equity from the institution by any means, including by declaring a dividend;

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(F) Any extraordinary losses

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must—

(i) Submit

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(ii) Demonstrate that it was current on its debt payments and has met all of its financial obligations, as required under §668.171 (b)(3) and (b)(4), for its two most recent fiscal years; and

(iii) Comply

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only if—

(i)(A) The persons or entities that exercise substantial control, as determined under §668.174(b)(1) and (c), repay or enter into an agreement with the Secretary to repay the applicable portion of that liability, as provided under §668.174(b)(2)(ii); or

(B) The institution assumes that liability, and repays or enters into an agreement with the Secretary

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repay that liability;

(ii) The institution satisfies the general standards and provisions of

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this section;

(ii) May require the institution,

Issue Paper 4
Session 2: January 8-11, 2018

Issue: **Pre-dispute Arbitration Agreements, Class Action Waivers, and Internal Dispute Processes**

Statutory cites: §§455(a)(6) and 455(h) of the Higher Education Act, as amended

Regulatory cites: §§ 668.41 and 685.304

Summary of Changes: To facilitate transparency and fully inform prospective, enrolled, and departing students:

- Amend "Reporting and disclosure of information" [§ 668.41] to (1) require schools that use pre-dispute arbitration agreements and/or class action waivers to disclose that information in an easily accessible format for students, prospective students, and the public, and (2) require these schools to provide an annual notification of this information to enrolled students.
- Amend 'Counseling borrowers' [§ 685.304] to include a requirement (similar to the current requirement that schools provide information regarding the FSA Ombudsman) that the school review with the student borrower information on the availability of the school's internal dispute resolution process and provide to the student a written disclosure explaining any internal dispute process;
- Amend 'Counseling borrowers' [§ 685.304] to include a requirement for schools using pre-dispute arbitration agreements and/or class action waivers, that the school review with the student borrower the pre-dispute arbitration and/or class action waiver process.

Changes: See regulatory text below.

§668.41 Reporting and disclosure of information.

(a) Definitions. The following definitions apply to this subpart:

* * * * * *

Undergraduate students, for purposes of §§ 668.45 and 668.48 only, means students enrolled in a bachelor's degree program, an associate degree program, or a vocational or technical program below the baccalaureate level.

(b) Disclosure through Internet or Intranet websites. Subject to paragraphs (c)(2), (e)(2) through (4), or (g)(1)(ii) of this section, as appropriate, an institution may satisfy any requirement to disclose information under paragraph (d), (e), or (g) of this section for—

(1) Enrolled students or current employees by posting the information on an Internet website or an Intranet website that is reasonably accessible to the individuals to whom the information must be disclosed; and

(2) Prospective students or prospective employees by posting the information on an Internet website.

(c) Notice to enrolled students. (1) An institution annually must distribute to all enrolled students a notice of the availability of the information required to be disclosed pursuant to paragraphs (d), (e), (g), and (h) of this section, and pursuant to 34 CFR 99.7 (§ 99.7 sets forth the notification requirements of the Family Educational Rights and Privacy Act of 1974). The notice must list and briefly describe the information and tell the student how to obtain the information.

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(2) An institution that discloses information to enrolled students as required under paragraph (d), (e), (g), or (h) of this section by posting the information on an Internet website or an Intranet website must include in the notice described in paragraph (c)(1) of this section—

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(i) The exact electronic address at which the information is posted; and

(ii) A statement that the institution will provide a paper copy of the information on request.

(d) General disclosures for enrolled or prospective students. An institution must make available to any enrolled student or prospective student through appropriate publications, mailings or electronic media, information concerning—

(1) Financial assistance available to students enrolled in the institution (pursuant to §668.42).

(2) The institution (pursuant to §668.43).

* * * * * *

(h) *Enrolled students, prospective students, and the public—disclosure of an institution's use of pre-dispute arbitration agreements and/or class action waivers for students receiving Title IV Federal student aid*. (1) An institution of higher education must make available to enrolled students, prospective students, and the public, information regarding any class action waiver or pre-dispute arbitration agreement in agreements between the institution and students receiving Title IV Federal student aid. The school must make the information easily accessible to students, prospective students, and the public. The institution may not use an Intranet website for the purpose of providing this notice to prospective students or the public.

(2) The institution must provide an annual notice to all enrolled students, pursuant to paragraph (c)(1) of this section of the information described in paragraph (h)(1). If the institution chooses to make the disclosure available by posting the disclosure on an Internet website or an Intranet website, such disclosure must include the exact electronic address at which the disclosure is posted, a brief description of the disclosure, and a statement that the institution will provide a paper copy of the disclosure upon request.

(3) For the purposes of this paragraph (h), the following definitions apply:

(i) *Class action* means a lawsuit or an arbitration proceeding in which one or more parties seek class treatment pursuant to Federal Rule of Civil Procedure 23 or any State process analogous to Federal Rule of Civil Procedure 23.

(ii) *Class action waiver means any agreement or part of an agreement, regardless of its form or structure,* between a school, or a party acting on behalf of a school, and a student that prevents an individual from filing or participating in a class action lawsuit.

(iii) *Pre-dispute arbitration agreement* means any agreement or part of an agreement, regardless of its form or structure, between a school, or a party acting on behalf of a school, and a student requiring arbitration of any future dispute between the parties.

(Authority: 20 U.S.C. 1092)

§685.304 Counseling borrowers.

(a) Entrance counseling. (1) Except as provided in paragraph (a)(8) of this section, a school must ensure that entrance counseling is conducted with each Direct Subsidized Loan or Direct Unsubsidized Loan student borrower prior to making the first disbursement of the proceeds of a loan to a student borrower unless the student borrower has received a prior Direct Subsidized Loan, Direct Unsubsidized Loan, Subsidized or Unsubsidized Federal Stafford Loan, or Federal SLS Loan from that school.

(2) Except as provided in paragraph (a)(8) of this section, a school must ensure that entrance counseling is conducted with each graduate or professional student Direct PLUS Loan borrower prior to making the first disbursement of the loan unless the student borrower has received a prior student Direct PLUS Loan or student Federal PLUS Loan from that school.

(3) Entrance counseling for Direct Subsidized Loan, Direct Unsubsidized Loan, and graduate or professional student Direct PLUS Loan borrowers must provide the borrower with comprehensive information on the terms and conditions of the loan and on the responsibilities of the borrower with respect to the loan. This information may be provided to the borrower—

(i) During an entrance counseling session, conducted in person;

(ii) On a separate written form provided to the borrower that the borrower signs and returns to the school; or

(iii) (A) Online or by interactive electronic means, with the borrower acknowledging receipt of the information.

(B) If a standardized interactive electronic tool is used to provide entrance counseling to the borrower, the school must provide any elements of the required information that are not addressed through the electronic tool:

(*1*) In person; or

(*2*) On a separate written form provided to the borrower that the borrower signs and returns to the school.

(4) If entrance counseling is conducted online or through interactive electronic means, the school must take reasonable steps to ensure that each student borrower receives the counseling materials, and

participates in and completes the entrance counseling, which may include completion of any interactive program that tests the borrower's understanding of the terms and conditions of the borrower's loans.

(5) A school must ensure that an individual with expertise in the title IV programs is reasonably available shortly after the counseling to answer the student borrower's questions. As an alternative, in the case of a student borrower enrolled in a correspondence, distance education, or a study-abroad program approved for credit at the home institution, the student borrower may be provided with written counseling materials before the loan proceeds are disbursed.

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(6) Entrance counseling for Direct Subsidized Loan and Direct Unsubsidized Loan borrowers must—

(i) Explain the use of a Master Promissory Note (MPN);

(ii) Emphasize to the borrower the seriousness and importance of the repayment obligation the student borrower is assuming;

(iii) Describe the likely consequences of default, including adverse credit reports, delinquent debt collection procedures under Federal law, and litigation;

(iv) Emphasize that the student borrower is obligated to repay the full amount of the loan even if the student borrower does not complete the program, does not complete the program within the regular time for program completion, is unable to obtain employment upon completion, or is otherwise dissatisfied with or does not receive the educational or other services that the student borrower purchased from the school;

(v) Inform the student borrower of sample monthly repayment amounts based on—

(A) A range of student levels of indebtedness of Direct Subsidized Loan and Direct Unsubsidized Loan borrowers, or student borrowers with Direct Subsidized, Direct Unsubsidized, and Direct PLUS Loans depending on the types of loans the borrower has obtained; or

(B) The average indebtedness of other borrowers in the same program at the same school as the borrower;

(vi) To the extent practicable, explain the effect of accepting the loan to be disbursed on the eligibility of the borrower for other forms of student financial assistance;

(vii) Provide information on how interest accrues and is capitalized during periods when the interest is not paid by either the borrower or the Secretary;

(viii) Inform the borrower of the option to pay the interest on a Direct Unsubsidized Loan while the borrower is in school;

(ix) Explain the definition of half-time enrollment at the school, during regular terms and summer school, if applicable, and the consequences of not maintaining half-time enrollment;

(x) Explain the importance of contacting the appropriate offices at the school if the borrower withdraws prior to completing the borrower's program of study so that the school can provide exit counseling, including information regarding the borrower's repayment options and loan consolidation;

(xi) Provide information on the National Student Loan Data System and how the borrower can access the borrower's records;

(xii) Provide the name of and contact information for the individual the borrower may contact if the borrower has any questions about the borrower's rights and responsibilities or the terms and conditions of the loan;

(xiii) Provide a description of the school's internal dispute resolution process, including the name and contact information for the individual or office at the school that the borrower may contact if the borrower has a dispute relating to the borrower's Federal student loans or to the educational services for which the loans were provided;

(xiv) If the school requires borrowers to enter into a pre-dispute arbitration agreement, as defined in § 668.41(h), to enroll in the institution, explain how and when the agreement applies, how the borrower enters into the arbitration process, and who to contact if the borrower has any questions;

(xv) If the school requires borrowers to sign a class-action waiver, as defined in § 668.41(h), to enroll in the institution, explain how and when the waiver applies, alternative processes the borrower may pursue to seek redress, and who to contact if the borrower has any questions; and

(xvi) For first-time borrowers as defined in § 685.200(f)(1)(i), explain the limitation on eligibility for Direct Subsidized Loans and possible borrower responsibility for accruing interest described in § 685.200(f), including—

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(A) The possible loss of eligibility for additional Direct Subsidized Loans;

(B) How a borrower's maximum eligibility period, remaining eligibility period, and subsidized usage period are calculated;

(C) The possibility that the borrower could become responsible for accruing interest on previously received Direct Subsidized Loans and the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan during in-school status, the grace period, authorized periods of deferment, and certain periods under the Income-Based Repayment and Pay As You Earn Repayment plans; and

(D) The impact of borrower responsibility for accruing interest on the borrower's total debt.

(7) Entrance counseling for graduate or professional student Direct PLUS Loan borrowers must—

(i) Inform the student borrower of sample monthly repayment amounts based on—

(A) A range of student levels or indebtedness of graduate or professional student PLUS loan borrowers, of student borrowers with Direct PLUS Loans and Direct Subsidized Loans or Direct Unsubsidized Loans, depending on the types of loans the borrower has obtained; or

(B) The average indebtedness of other borrowers in the same program at the same school;

(ii) Inform the borrower of the option to pay interest on a PLUS Loan while the borrower is in school;

(iii) For a graduate or professional student Direct PLUS Loan borrower who has received a prior Direct Subsidized Loan, Direct Unsubsidized Loan, Subsidized Federal Stafford Loan, or Unsubsidized Federal Stafford Loan from that school, provide the information specified in § 685.301(a)(3)(i)(A) through (a)(3)(i)(C); and

(iv) For a graduate or professional student Direct PLUS Loan borrower who has not received a prior Direct Subsidized Loan, Direct Unsubsidized Loan, Subsidized Federal Stafford Loan, or Unsubsidized Federal Stafford Loan from that school, provide the information specified in paragraph (a)(6)(i) through paragraph (a)(6)(xiii) of this section.

(8) A school may adopt an alternative approach for entrance counseling as part of the school's quality assurance plan described in § 685.300(b)(9). If a school adopts an alternative approach, it is not required to meet the requirements of paragraphs (a)(1) through (a)(7) of this section unless the Secretary determines that the alternative approach is not adequate for the school. The alternative approach must—

(i) Ensure that each student borrower subject to entrance counseling under paragraph (a)(1) or (a)(2) of this section is provided written counseling materials that contain the information described in paragraphs (a)(6)(i) through (a)(6)(v) of this section;

(ii) Be designed to target those student borrowers who are most likely to default on their repayment obligations and provide them more intensive counseling and support services; and

(iii) Include performance measures that demonstrate the effectiveness of the school's alternative approach. These performance measures must include objective outcomes, such as levels of borrowing, default rates, and withdrawal rates.

(9) The school must maintain documentation substantiating the school's compliance with this section for each student borrower.

(b) Exit counseling. (1) A school must ensure that exit counseling is conducted with each Direct Subsidized Loan or Direct Unsubsidized Loan borrower and graduate or professional student Direct PLUS Loan borrower shortly before the student borrower ceases at least half-time study at the school.

(2) The exit counseling must be in person, by audiovisual presentation, or by interactive electronic means. In each case, the school must ensure that an individual with expertise in the title IV programs is reasonably available shortly after the counseling to answer the student borrower's questions. As an alternative, in the case of a student borrower enrolled in a correspondence program or a study-abroad program approved for credit at the home institution, the student borrower may be provided with written counseling materials within 30 days after the student borrower completes the program.

(3) If a student borrower withdraws from school without the school's prior knowledge or fails to complete the exit counseling as required, exit counseling must, within 30 days after the school learns

that the student borrower has withdrawn from school or failed to complete the exit counseling as required, be provided either through interactive electronic means, by mailing written counseling materials to the student borrower at the student borrower's last known address, or by sending written counseling materials to an email address provided by the student borrower that is not an email address associated with the school sending the counseling materials.

(4) The exit counseling must—

(i) Inform the student borrower of the average anticipated monthly repayment amount based on the student borrower's indebtedness or on the average indebtedness of student borrowers who have obtained Direct Subsidized Loans and Direct Unsubsidized Loans, student borrowers who have obtained only Direct PLUS Loans, or student borrowers who have obtained Direct Subsidized, Direct Unsubsidized, and Direct PLUS Loans, depending on the types of loans the student borrower has obtained, for enrollment in the same school or in the same program of study at the same school;

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(ii) Review for the student borrower available repayment plan options including the standard repayment, extended repayment, graduated repayment, income-contingent repayment, and income-based repayment plans, including a description of the different features of each plan and sample information showing the average anticipated monthly payments, and the difference in interest paid and total payments under each plan;

(iii) Explain to the borrower the options to prepay each loan, to pay each loan on a shorter schedule, and to change repayment plans;

(iv) Provide information on the effects of loan consolidation including, at a minimum—

(A) The effects of consolidation on total interest to be paid, fees to be paid, and length of repayment;

(B) The effects of consolidation on a borrower's underlying loan benefits, including grace periods, loan forgiveness, cancellation, and deferment opportunities;

(C) The options of the borrower to prepay the loan and to change repayment plans; and

(D) That borrower benefit programs may vary among different lenders;

(v) Include debt-management strategies that are designed to facilitate repayment;

(vi) Explain to the student borrower how to contact the party servicing the student borrower's Direct Loans;

(vii) Meet the requirements described in paragraphs (a)(6)(i), (a)(6)(ii), and (a)(6)(iv) of this section;

(viii) Describe the likely consequences of default, including adverse credit reports, delinquent debt collection procedures under Federal law, and litigation;

(ix) Provide—

(A) A general description of the terms and conditions under which a borrower may obtain full or partial forgiveness or discharge of principal and interest, defer repayment of principal or interest, or be granted forbearance on a title IV loan; and

(B) A copy, either in print or by electronic means, of the information the Secretary makes available pursuant to section 485(d) of the HEA;

(x) Review for the student borrower information on the availability of the Department's Student Loan Ombudsman's office;

(xi) Review for the student borrower the school's internal dispute resolution process, including the name and contact information for the individual or office at the school that the borrower may contact if the borrower has a dispute relating to the borrower's Federal student loans or to the educational services for which the loans were provided;

(xii) If the school required the borrower to enter into a pre-dispute arbitration agreement, as defined in § 668.41(h), to enroll in the institution, explain how and when the agreement applies, how the borrower enters into the arbitration process, and who to contact if the borrower has any questions;

(xiii) If the school required the borrower to sign a class-action waiver, as defined in § 668.41(h), to enroll in the institution, explain how and when the waiver applies, alternative processes the borrower may pursue to seek redress, and who to contact if the borrower has any questions;

(xiv) Inform the student borrower of the availability of title IV loan information in the National Student Loan Data System (NSLDS) and how NSLDS can be used to obtain title IV loan status information;

(xv) Explain to first-time borrowers, as defined in § 685.200(f)(1)(i)—

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(A) How the borrower's maximum eligibility period, remaining eligibility period, and subsidized usage period are determined under § 685.200(f);

(B) The sum of the borrower's subsidized usage periods, as determined under § 685.200(f)(1)(iii), at the time of the exit counseling;

(C) The consequences of continued borrowing or enrollment, including--

(1) The possible loss of eligibility for additional Direct Subsidized Loans; and

(2) The possibility that the borrower could become responsible for accruing interest on previously received Direct Subsidized Loans and the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan during in-school status, the grace period, authorized periods of deferment, and certain periods under the Income-Based Repayment and Pay As You Earn Repayment plans;

(D) The impact of the borrower becoming responsible for accruing interest on total student debt;

(E) That the Secretary will inform the student borrower of whether he or she is responsible for accruing interest on his or her Direct Subsidized Loans; and

(F) That the borrower can access NSLDS to determine whether he or she is responsible for accruing interest on any Direct Subsidized Loans as provided in § 685.200(f)(3);

(xvi) A general description of the types of tax benefits that may be available to borrowers; and

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(xvii) Require the student borrower to provide current information concerning name, address, social security number, references, and driver's license number and State of issuance, as well as the student borrower's expected permanent address, the address of the student borrower's next of kin, and the name and address of the student borrower's expected employer (if known).

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(5) The school must ensure that the information required in paragraph (b)(4)(xvi) of this section is provided to the Secretary within 60 days after the student borrower provides the information.

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(6)(A) If exit counseling is conducted through interactive electronic means, a school must take reasonable steps to ensure that each student borrower receives the counseling materials, and participates in and completes the exit counseling.

(B) If a standardized interactive electronic tool is used to provide exit counseling to the borrower, including the electronic interactive exit counseling offered by the Secretary, the school must provide any elements of the required information that are not addressed through the electronic tool:

(*1*) In person; or

(*2*) On a separate written form provided to the borrower that the borrower signs and returns to the school.

(7) The school must maintain documentation substantiating the school's compliance with this section for each student borrower.

(8)(i) For students who have received loans under both the FFEL Program and the Direct Loan Program for enrollment in a school, the school's compliance with the exit counseling requirements in paragraph (b) of this section satisfies the exit counseling requirements in 34 CFR 682.604(a) if the school ensures that the exit counseling also provides the borrower with the information described in 34 CFR 682.604(a)(2)(i) and (ii).

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(ii) A student's completion of electronic interactive exit counseling offered by the Secretary satisfies the requirements of paragraph (b) of this section and, for students who have also received FFEL Program loans for enrollment in the school, 34 CFR 682.604(a).

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(Authority: 20 U.S.C. 1087a et seq.)

Issue Paper 5
Session 1: January 8 - 11, 2018

Issue: Closed School Discharge

Statutory cites: §437(c) of the Higher Education Act of 1965, as amended

Regulatory cites: 34 CFR 674.33(g), 682.402(d), and 685.214

Summary of change:

Amends the application requirements for closed school discharges to reflect current practice, which requires that a borrower applying for a closed school discharge submit a completed application form, rather than a sworn statement. The proposed regulations also would expand the window for closed school discharges from 120 days to 150 days.

Changes: See regulatory text below.

§ 674.33 Repayment.

* * * * *

(g) *Closed school discharge*—(1) *General.*

* * * * *

(4) *Borrower qualification for discharge.* Except as provided in paragraph (g)(3) of this section, in order to qualify for discharge of an NDSL or Federal Perkins Loan, a borrower must submit to the holder of the loan a written request on an application approved by the Secretary, and the factual assertions in the application must be true. The application need not be notarized but all statements made therein must be made by the borrower under penalty of perjury. The application explains the procedures and eligibility criteria for obtaining a discharge and requires the borrower to—

(i) Certify that the borrower—

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(A) Received the proceeds of a loan to attend a school;

(B) Did not complete the program of study at that school because the school closed while the student was enrolled, or the student withdrew from the school not more than 150 days before the school closed. The Secretary may extend the 150-day period if the Secretary determines that exceptional circumstances related to the school's closing justify an extension. Exceptional circumstances for this purpose may include, but are not limited to: revocation or withdrawal by an accreditation agency of the school's institutional accreditation; the school's discontinuation of the majority of its academic programs; the State's revocation or withdrawal of the school's license to operate or to award academic credentials in the State; or a nondefault, contested Federal or State court judgment issued by a court of competent jurisdiction, or an adjudication by a Federal or State administrative agency that the school violated State or Federal law; and

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(C) Did not complete and is not in the process of completing the program of study through a teach-out at another school as defined in 34 CFR 602.2 and administered in accordance with 34 CFR 602.207(b)(6), by transferring academic credit earned at the closed school to another school, or by any other comparable means;

* * * * *

(v) If the borrower fails to submit the application described in paragraph (g)(4) of this section within 60 days of the holder of the loan's mailing the discharge application, the holder of the loan resumes collection and grants forbearance of principal and interest for the period during which collection activity was suspended.

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§ 682.402 Death, disability, closed school, false certification, unpaid refunds, and bankruptcy payments.

* * * * *

(d) *Closed school*—(1) *General.*

* * * * *

(6) ***

(ii) ***

(B) If a guaranty agency determines that a school appears to have closed, it shall, within 30 days of making that determination, notify all lenders participating in its program to suspend collection efforts against individuals with respect to loans made for attendance at the closed school, if the student to whom (or on whose behalf) a loan was made, appears to have been enrolled at the school on the closing date, or withdrew not more than 150 days prior to the date the school appears to have closed. Within 30 days after receiving confirmation of the date of a school's closure from the Secretary, the agency shall—

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(*1*) Notify all lenders participating in its program to mail a discharge application approved by the Secretary to all borrowers who may be eligible for a closed school discharge; and

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(*2*) Review the records of loans that it holds, identify the loans made to any borrower (or student) who appears to have been enrolled at the school on the school closure date or who withdrew not more than 150 days prior to the closure date, and mail a discharge application to the borrower. The application informs the borrower of the procedures and eligibility criteria for obtaining a discharge.

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(F) If the guaranty agency determines that a borrower identified in paragraph (d)(6)(ii)(C) or (D) of this section does not qualify for a discharge, the agency shall notify the borrower in writing of that determination and the reasons for it within 30 days after the date the agency—

(*1*) Made that determination based on information available to the guaranty agency;

(*2*) Was notified by the Secretary that the school had not closed;

(*3*) Was notified by the Secretary that the school had closed on a date that was more than 150 days after the borrower (or student) withdrew from the school;

(*4*) Was notified by the Secretary that the borrower (or student) was ineligible for a closed school discharge for other reasons; or

(*5*) Received the borrower's completed application.

* * * * *

(G) Upon receipt of a closed school discharge claim filed by a lender, the agency shall review the borrower's completed application in light of information available from the records of the agency and from other sources, including other guaranty agencies, state authorities, and cognizant accrediting associations, and shall take the following actions—

(*1*) If the agency determines that the borrower satisfies the requirements for discharge under paragraph (d) of this section, it shall pay the claim in accordance with § 682.402(h) not later than 90 days after the agency received the claim; or

(*2*) If the agency determines that the borrower does not qualify for a discharge, the agency shall, not later than 90 days after the agency received the claim, return the claim to the lender with an explanation of the reasons for its determination.

(H) If a borrower fails to submit the completed application described in paragraph (d)(3) of this section within 60 days of being notified of that option, the lender or guaranty agency shall resume collection and shall be deemed to have exercised forbearance of payment of principal and interest from the date it suspended collection activity. The lender or guaranty agency may capitalize, in accordance with § 682.202(b), any interest accrued and not paid during that period.

* * * * *

§685.214 Closed school discharge.

* * * * *

(c) *Borrower qualification for discharge.* (1) In order to qualify for discharge of a loan under this section, a borrower must submit to the Secretary a completed application, and the factual assertions in the application must be true. The application explains the procedures and eligibility criteria for obtaining a discharge and requires the borrower to—

(i) Certify that the borrower (or the student on whose behalf a parent borrowed)—

(A) Received the proceeds of a loan, in whole or in part, on or after January 1, 1986 to attend a school;

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(B) Did not complete the program of study at that school because the school closed while the student was enrolled, or the student withdrew from the school not more than 120 days before the school closed. The Secretary may extend the 150-day period if the Secretary determines that exceptional circumstances related to a school's closing justify an extension. Exceptional circumstances for this purpose may include, but are not limited to: the revocation or withdrawal by an accreditation agency of the school's institutional accreditation; the school's discontinuation of the majority of its academic programs; revocation or withdrawal of the school's license to operate or to award academic credentials in the State; or a nondefault, contested Federal or State court judgment issued by a court of competent jurisdiction or adjudication by a Federal or State administrative agency that the school violated State or Federal law; and

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(C) Did not complete the program of study through a teach-out at another school or by transferring academic credits or hours earned at the closed school to another school;

* * * * *

(f) *Discharge procedures*.(1) After confirming the date of the school's closure, the Secretary identifies any Direct Loan borrowers (or students on whose behalf a parent borrowed) who appears to have been enrolled at the school on the closure date or to have withdrawn not more than 150 days prior to the closure date.

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(4) If a borrower fails to submit a completed application described in paragraph (c) of this section within 60 days of the Secretary's mailing the discharge application, the Secretary resumes collection and grants forbearance of principal and interest for the period in which collection activity was suspended. The Secretary may capitalize any interest accrued and not paid during that period.

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Issue Paper 6
Session 2: January 8 -11, 2018

Issue: False Certification

Statutory cites: §437(c) of the Higher Education Act of 1965, as amended (HEA)

Regulatory cites: 34 CFR 685.215

Summary of change: Amends application requirements for false certification discharges to reflect current practice, which requires that a borrower applying for a false certification discharge submit a completed application form, rather than a sworn statement. The proposed regulations also update the regulatory requirements regarding false certification of eligibility of non-high school graduates for Direct Loans.

Changes: See regulatory text below.

§ 685.215 Discharge for false certification of student eligibility or unauthorized payment

(a) *Basis for discharge*—(1) *False certification.* The Secretary discharges a borrower's (and any endorser's) obligation to repay a Direct Loan in accordance with the provisions of this section if a school falsely certifies the eligibility of the borrower (or the student on whose behalf a parent borrowed) to receive the loan. The Secretary considers a student's eligibility to borrow to have been falsely certified by the school if the school—

(i) Certified the student's eligibility for a Direct Loan with the knowledge that the student did not have a high school diploma or its recognized equivalent and did not meet the alternative eligibility requirements described in 34 CFR part 668 and section 484(d) of the Act applicable at the time the loan was originated;

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(c) *Borrower qualification for discharge.* In order to qualify for discharge under this section, the borrower must submit to the Secretary an application for discharge on a form approved by the Secretary, and the factual assertions in the application must be true and made under penalty of perjury. In the application, the borrower's responses must demonstrate to the satisfaction of the Secretary that the requirements in paragraphs (c) (1) through (6) of this section have been met.

(1) *High school diploma or equivalent*. In the case of a borrower requesting a discharge based on not having had a high school diploma and not having metthe alternative eligibility requirements, the application requires the borrower to certify that the borrower (or the student on whose behalf a parent borrowed)—

(i) Received a disbursement of a loan, in whole or in part, on or after January 1, 1986, to attend a school; and

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(ii) Received a Direct Loan at that school, did not have a high school diploma or its recognized equivalent, and did not meet the alternative to graduation from high school eligibility requirements described in 34 CFR part 668 and section 484(d) of the Act applicable at the time the loan was originated;

* * * * *

(d) *Discharge procedures.* (1) If the Secretary determines that a borrower's Direct Loan may be eligible for a discharge under this section, the Secretary providesthe borrower an the application described in paragraph (d), which explains the qualifications and procedures for obtaining a discharge. The Secretary also promptly suspends any efforts to collect from the borrower on any affected loan. The Secretary may continue to receive borrower payments.

(2) If the borrower fails to submit a completed application described in paragraph (c) of this section within 60 days of the date the Secretary suspended collection efforts, the Secretary resumes collection and grants forbearance of principal and interest for the period in which collection activity was suspended. The Secretary may capitalize any interest accrued and not paid during that period.

(3) If the borrower submits the completed application described in paragraph (c) of the section, the Secretary determines whether to grant a request for discharge under this section by reviewing the application in light of information available from the Secretary's records and from other sources, including but not limited to guaranty agencies, State authorities, and cognizant accrediting associations.

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Issue Paper 7
Session 2: January 8-11, 2018

Issue: Guaranty Agency Collection Fees

Statutory cites: §§428F(a) and 484A(a) of the Higher Education Act, as amended

Regulatory cites: 34 CFR 682.202(b), 682.405(b), and 682.410(b)(2)

Summary of Changes: Prospectively bars guaranty agencies from charging collection costs to a defaulted borrower who enters into a repayment agreement with the guaranty agency within 60 days of receiving notice of default from the agency.

Prospectively bars guaranty agencies from capitalizing interest on a loan that is sold following the completion of loan rehabilitation.

Changes: See regulatory text below.

§ 682.202 Permissible charges by lenders to borrowers.

[* * *]

(b) Capitalization. (1) Except as provided in §682.405(b)(4), a lender may add accrued interest and unpaid insurance premiums or Federal default fees to the borrower's unpaid principal balance in accordance with this section. This increase in the principal balance of a loan is called "capitalization."

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§682.405 Loan rehabilitation agreement.

[* * *]

(b) Terms of agreement. In the loan rehabilitation agreement, the guaranty agency agrees to ensure that its loan rehabilitation program meets the following requirements at all times:

[* * *]

(4)(i) An eligible lender purchasing a rehabilitated loan must establish a repayment schedule that meets the same requirements that are applicable to other FFEL Program loans of the same loan type as the rehabilitated loan and must permit the borrower to choose any statutorily available repayment plan for that loan type. The lender must treat the first payment made under the nine payments as the first payment under the applicable maximum repayment term, as defined under § 682.209(a) or (e). For Consolidation loans, the maximum repayment term is based on the balance outstanding at the time of loan rehabilitation.

(ii) The purchase of a rehabilitated loan is not considered a borrower's entry into repayment or resumption of repayment for the purposes of interest capitalization under § 682.202(b).

[* * *]

(vi) Within 15 business days of its determination of the borrower's loan rehabilitation payment amount, the guaranty agency must provide the borrower with a written rehabilitation agreement which includes the borrower's payment amount calculated under paragraph (b)(1)(iii), a prominent statement that the borrower may object orally or in writing to the payment amount, with the method and timeframe for raising such an objection, and an explanation of any other terms and conditions applicable to the required series of payments that must be made before the borrower's account can be considered for repurchase by an eligible lender or assignment to the Secretary (i.e., rehabilitated). To accept the agreement, the borrower must sign and return the agreement or accept the agreement electronically under a process provided by the agency. The agency may not impose any conditions unrelated to the amount or timing of the rehabilitation payments in the rehabilitation agreement. The written rehabilitation agreement must inform the borrower—

(A) Of the effects of having the loans rehabilitated (e.g., removal of the record of default from the borrower's credit history and return to normal repayment); and

(B) That the rehabilitation agreement is null and void if the borrower fails to provide the documentation required to confirm the monthly payment calculated under paragraph (b)(1)(iii) of this section.

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§682.410 Fiscal, administrative, and enforcement requirements.

[* * *]

(2) Collection charges. (i) Whether or not provided for in the borrower's promissory note and subject to any limitation on the amount of those costs in that note, the guaranty agency shall charge a borrower an amount equal to reasonable costs incurred by the agency in collecting a loan on which the agency has paid a default or bankruptcy claim unless, within the 60-day period following the initial notice described in paragraph (b)(6)(ii) of this section, the borrower enters into an acceptable repayment agreement, including a rehabilitation agreement, and honors that agreement, in which case the guaranty agency shall not charge a borrower any collection costs.

(ii) An acceptable repayment agreement may includes an agreement described in §682.200(b) (Satisfactory repayment arrangement), §682.405, or paragraphs (b)(5)(ii) of this section. An acceptable repayment agreement constitutes a repayment arrangement or agreement on repayment terms satisfactory to the guaranty agency, under this section.

(iii) The costs under this paragraph (b)(2) include, but are not limited to, all attorney's fees, collection agency charges, and court costs. Except as provided in §§682.401(b)(18)(i) and 682.405(b)(1)(iv)(B), the amount charged a borrower must equal the lesser of—

(A) The amount the same borrower would be charged for the cost of collection under the formula in 34 CFR 30.60; or

(B) The amount the same borrower would be charged for the cost of collection if the loan was held by the U.S. Department of Education.

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(4) *Capitalization of unpaid interest.* The guaranty agency shall capitalize any unpaid interest due on the loan at the time the agency pays a default claim to the lender, but shall not capitalize any unpaid interest thereafter.

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Issue Paper 8
Session 2: January 8-11, 2018

Issue: Whether to recalculate a borrower's Subsidized Usage Period and interest accrual, if applicable, when the borrower receives a discharge of a loan for which he or she has not received all or part of the educational benefit of the loan

Statutory cite: § 455(q) of the Higher Education Act of 1965, as amended (HEA)

Regulatory cite: 34 CFR 685.200(f)

Summary of Change: To eliminate or recalculate the subsidized usage period and, if applicable, restore interest subsidy associated with the Direct Subsidized Loan(s) fully or partially discharged based on school closure, false certification, unpaid refund, or borrower defense, amend 34 CFR 685.200(f)(4)(iii) and 34 CFR 685.200(f)(3)(v).

Changes: See regulatory text below.

§ 685.200 Borrower eligibility.

[* * *]

(f) Limitations on eligibility for Direct Subsidized Loans and borrower responsibility for accruing interest for first-time borrowers on or after July 1, 2013

[* * *]

(3) Borrower responsibility for accruing interest.

(i) Notwithstanding any provision of this part that provides for the borrower to not be responsible for accruing interest on a Direct Subsidized Loan or on the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan, and except as provided in paragraphs (f)(6)(v) and (f)(7)(iv) of this section, a first-time borrower becomes responsible for the interest that accrues on a previously received Direct Subsidized Loan or on the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan beginning on the date—

(A) The borrower has no remaining eligibility period; and

(B) The borrower attends any undergraduate program or preparatory coursework on at least a half-time basis at an eligible institution that participates in the title IV, HEA programs.

(ii) The borrower continues to be responsible for the interest that accrues on the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan for which the borrower previously became responsible for accruing interest in accordance with paragraph (f)(3)(i) of this section.

(iii) For any loan for which the borrower becomes responsible for accruing interest in accordance with paragraph (f)(3)(i) of this section, the borrower is responsible for only the interest that accrues after the borrower meets the criteria in paragraph (f)(3)(i) of this section and unpaid interest is capitalized in the same manner as for a Direct Unsubsidized Loan.

(iv) A borrower who completes an undergraduate program and who has not become responsible for accruing interest on Direct Subsidized Loans as a result of attendance in that program does not become responsible for accruing interest under paragraph (f)(3)(i) of this section on any Direct Subsidized Loans received for attendance in any program prior to completing that undergraduate program and for which the borrower has not previously become responsible for accruing interest, regardless of subsequent attendance in any other program.

(v) A borrower who receives a closed school, false certification, unpaid refund, or borrower defense discharge that results in a remaining eligibility period greater than zero is not responsible for the interest that accrues on a Direct Subsidized Loan or on the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan unless the borrower once again becomes responsible for the interest that accrues on a previously received Direct Subsidized Loan or on the portion of a Direct Consolidation Loan that repaid a Direct Subsidized Loan, for the life of the loan, as described in paragraph (f)(3)(i) of this section.

(4) Exceptions to the calculation of subsidized usage periods.

(i) For a first-time borrower who receives a Direct Subsidized Loan in an amount that is equal to the full annual loan limit for a loan period that is less than a full academic year in length, the subsidized usage period is one year.

(ii) For a first-time borrower who is enrolled on a half-time or three-quarter-time basis, the borrower's prorated subsidized usage period is calculated by multiplying the borrower's subsidized usage period by 0.5 or 0.75, respectively.

(iii) For a first-time borrower who receives a closed school, false certification, unpaid refund, or borrower defense discharge on a Direct Subsidized Loan or a portion of a Direct Consolidation Loan that is attributable to a Direct Subsidized Loan, the Subsidized Usage Period is reduced. If the Direct Subsidized Loan or a portion of a Direct Consolidation Loan that is attributable to a Direct Subsidized Loan is discharged in full, the Subsidized Usage Period of those loans is zero years. If the Direct Subsidized Loan or a portion of a Direct Consolidation Loan that is attributable to a Direct Subsidized Loan is discharged in part, the Subsidized Usage Period may be reduced if the discharge results in the inapplicability of paragraph (f)(4)(i) of this section.

(Authority: 20 U.S.C. 1087a *et seq.*)