**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:

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

(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.

(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, --

(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) *Early Claim Resolution (ECR).* The ECR process facilitates the resolution of claims by providing an early opportunity for the borrower and the school to voluntarily resolve the borrower defense claims. The Secretary will consider whether a borrower defense claim is appropriate for ECR as early as possible upon the Department’s receipt of the borrower defense application and the school’s response. When the Secretary determines that a borrower defense claim is appropriate for ECR, it shall contact the borrower and the school to offer this resolution option.

(i) The Secretary’s designated representative as described in 685.206(d)(4)(iv) shall serve as an impartial, confidential facilitator between the parties. The Secretary’s representative shall:

(A) Inform the borrower and the school of ECR procedures, establish a constructive tone, and encourage the borrower and the school to work expeditiously and in good faith toward a mutually acceptable resolution.

(B) Review the allegations that the Secretary has accepted for investigation with the parties and assist both parties in understanding the pertinent legal standards and possible remedies.

(C) Facilitate a discussion between the borrower and the school regarding possible actions that the parties may consider in working toward a resolution.

(D) Offer assistance, as appropriate, with regard to reducing any resolution to writing. When an agreement is reached, the parties are informed that the Secretary will issue a closure letter reflecting the resolution of the borrower defense claim by agreement of the parties.

(ii) The borrower and school shall:

(A) Participate in the discussions in good faith.

(B) Consider offers or suggestions with an open mind and to work constructively toward a mutually acceptable resolution.

(C) Implement any agreement in good faith.

(iii) The Secretary does not sign, approve, endorse and monitor any agreement reached between the parties.

(iv) When the Secretary determines that ECR is appropriate and the borrower and the school are willing to proceed with this resolution option, the Secretary will designate a representative to facilitate an agreement between the borrower and school. To the extent possible, the representative assigned to conduct ECR of a borrower defense claim shall not be staff assigned to the investigation of that claim. An Agreement to Participate in ECR must be reviewed and either signed or verbally agreed to by the borrower and school. In circumstances where verbal agreement is obtained, the ECR representative shall send a letter or electronic mail to the parties confirming the Agreement. The Secretary has the discretion to suspend its investigation of the borrower defense claim for up to 45 calendar days to facilitate an agreement between the parties. If an agreement has not been reached, the Secretary will resume its investigation if it had been suspended.

(v) A Confidentiality Agreement must be reviewed and signed or verbally agreed to by the ECR facilitator and the parties to the ECR, (the borrower or borrower’s representative and the school or school’s representative). In circumstances where verbal agreement is obtained, the ECR facilitator shall send a letter or electronic mail to the parties confirming this Agreement. In order to maintain confidentiality of the ECR process, any notes taken during ECR by the facilitator and/or any records or other documents offered by either party to the facilitator during ECR will be kept in a separate file and will not be shared with the Department staff member(s) assigned to investigate the borrower defense claim.

(vi) At the conclusion of ECR, the Secretary will obtain a copy of a statement that the borrower defense claim has been resolved, signed by the borrower, or a copy of any agreement that has been signed by the parties. Once resolution of any borrower defense claim has been obtained, the Secretary will notify the parties in writing that the borrower defense claim has been resolved. A copy of the ECR agreement between the parties will be attached to the closure letter.

(vii) The Secretary will not monitor the agreement, but will inform the parties that if a breach occurs, the borrower has the right to file another claim. If a new claim is filed, the Secretary will not address the alleged breach of the agreement. Instead, the Secretary will investigate the original allegation. To be considered timely, the new complaint must be filed within \_\_\_ calendar days of the date the borrower obtains information that a breach occurred.

(viii) The Secretary will monitor the process of ECR to ensure adequate time for completion of the borrower defense claim investigation in the event that ECR is unsuccessful. Where ECR is unsuccessful, investigation shall proceed to ensure completion in accordance with claim processing procedures set forth herein.

(5) *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.

(6) *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.

(7) *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.

(8) *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.

(9) *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 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.

(10) *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.

(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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