

**Issue Paper 2**

**Session 3: February 12 – 15, 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 borrower defense claims, claims for Direct Loans first disbursed on or after July 1, 2019,~~ including provisions for:

- Forbearance;
- The application process;
- Adjudication of a ~~BD borrower defense~~ claim;
- Notification of the borrower and school of the Department’s decision;
- Reconsideration of denials;
- Relief that a borrower may receive if a ~~BD borrower defense~~ 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 or loans 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;

(iv) Under §685.217; ~~or~~

(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 ~~34 CFR 30.33-26~~ 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~~ (fe).

(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. However, the Secretary does will not initiate such a proceeding more than three years after the date of the final determination of the borrower's defense against repayment claim; 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 § 685.2224, a borrower must submit an application under penalty of perjury 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~~ evidence that supports the borrower defense claim; and

(iii) Indicating whether the borrower has made a claim based on the same act or omission of the school on which the borrower defense claim is based 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) If the borrower’s claim is denied, the Secretary ends the forbearance or resumes collection 60 days after the date of the denial-, unless a request for reconsideration under paragraph (d)(5) -of this section is accepted.

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

(iv) If the borrower’s claim is denied, the forbearance or suspension of collection activity will not be reinstated if the borrower resubmits that claim and , unless the resubmission submits a revised borrower defense claim request for reconsideration that -meets the eligibility criteria in paragraph (e)(d)-(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) If the Secretary determines that the borrower’s claim -does not meet at the minimum threshold for consideration of a borrower defense claim, the Secretary provides a written notification to the borrower denying the claim.

(ii) A borrower meets the minimum threshold for consideration of a borrower defense claim if—

(A) The borrower’s application provides the information specified in paragraph- (d)(1) of this section;

(B) The claim alleges a misrepresentation on the part of the school as described in 685.222(b)(1)(i) or establishes that the borrower has obtained a judgment as described in 685.222(b)(1)(ii) or (iii); and

(C) Provides minimum supporting evidence to corroborate the borrower defense claim.

(iii) Within 60 days of the date of the Department’s receipt of the borrower defense application, tlf the Secretary determines that the borrower meets at the minimum threshold for consideration of a borrower defense claim as described in- paragraph (d)(3)(ii) of this section, the Secretary provides written notification of the -determination to the borrower and the school. submission of the borrower defense applicatio The notification to the school provides the school with a -copy of the borrower’s application and any supporting evidence submittted with the application. The school may submit a response to the borrower’s claim as described in (d)(3)(iv)(C) of this section. 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.

(iv) The borrower and the school may provide the Secretary any additional relevant evidence within 45 days of the date of the notification specified in paragraph (d)(3)(iii) of this section.

(v) 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 evidence submitted by the borrower; and

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

(vi) In resolving the borrower defense claim, the Secretary may—

(A) Consider other relevant information obtained by the Secretary; and

(B) Request additional relevant information from the borrower or the school.

(vii) Upon request, the Secretary provides the borrower any information submitted by the school and provides the school any additional information provided by the borrower. The Secretary further provides the borrower and the school with any other relevant information obtained by the Secretary in resolving the borrower defense claim.

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

(i) Notifying the borrower and the school of the decision on the borrower's borrower defense claim;

(ii) Providing the reasons for the decision;

(iii) Informing the borrower and the school of the relief, if any, that the borrower will receive, consistent with paragraph (d)(6) of this section; 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) The borrower or the school may request reconsideration from the Secretary by submitting newly discovered evidence within 60 days of the date of the written decision in paragraph (d)(4) of this section.

(i) If the borrower defense is denied in full or in part, the borrower may request that the Secretary reconsider the borrower defense new evidence support the borrower's claim.

(ii)

~~(iii)~~ If the Secretary accepts a 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)~~ The borrower or the school may request reconsideration from the Secretary by submitting newly discovered evidence within 60 days of the date of the written decision as outlined in paragraph (d)(4) of this section. 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.

~~(iii)~~ “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 that the Secretary did not rely upon in determination of the borrower defense claim.

(6) *Relief.* (i) 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. In determining the appropriate amount of relief to be provided to the borrower, the factors the Secretary will consider, in a practicable manner, include but are not limited to—

(A) The value of the education that the borrower received from the school; and

(B) The borrower’s earning potential.

(ii) The Secretary affords the borrower such further relief as the Secretary determines is appropriate under the circumstances. Further relief includes, if applicable:

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

~~(ii)~~ (B) 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)~~ (C) 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)(9) of this section or under § 685.222 Subpart G. Such cooperation includes, but is not limited to--

(i) Providing testimony regarding any representation made by the borrower to support a request for discharge successful borrower defense claim; 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 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. –(i) The Secretary may initiate an appropriate proceeding to require the school whose ~~act or omission~~misrepresentation resulted in the borrower's successful borrower defense ~~against repayment claim of~~ with respect to ~~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.

(ii) The Secretary initiates a recovery action against a school no later than three years after the date of the final determination of the borrower's defense to repayment claim.

(iii) The school must repay the Secretary for the amount of the loan which has been discharged and amounts refunded to a borrower for payments made by the borrower to the Secretary unless the school demonstrates that the Secretary's decision to approve the borrower defense claim was clearly erroneous.

(iv) The school may present relevant evidence in the recovery proceeding.

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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 and affords the borrower further relief, as applicable, in accordance with § 685.206(c)(2) or 685.206 (d)(6)(ii).

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

(a) \* \* \*

(b) Program participation agreement. In the program participation agreement, the school must promise to comply with the Act and applicable regulations and must agree to--

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(8) ~~Provide that the school will a~~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, 685.215, 685.216, and 685.222 and for which the institution has been determined to be liable as described in Subpart G;

**Section 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 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; ~~or~~

(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

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