Making & Disbursing Loans

CHAPTER 3

A Perkins Loan (or NDSL) is made when the borrower has signed the promissory note for the award year and the school makes the first disbursement of loan funds under that promissory note for that award year. The student is required to sign the note only once each award year. The borrower must sign before the school disburses any loan funds to him or her under that note for that award year. However, a school may choose to require a borrower to sign for each advance.

After a student files a FAFSA and the Department determines an official Expected Family Contribution for the student, the school must award financial aid based on the student's maximum loan eligibility and the maximum loan amounts for each loan program. For a complete explanation of awarding financial aid, see *Volume 1 - Student Eligibility* and *Volume 4 - Campus-Based Common Provisions.*

LOAN MAXIMUMS

The maximum amount an eligible student may borrow is $4,000 per award year for a student who has not successfully completed a program of undergraduate education or $6,000 per award year for a graduate or professional student.

The aggregate loan limits now include only unpaid principal. (Previously, a student who had borrowed the maximum cumulative amount for a graduate or professional student would not be eligible for another loan even if the student had repaid part or all of the amount he or she had borrowed.) The maximum aggregate amount an eligible student may now borrow is: (1)$20,000 for an undergraduate student who has completed two academic years and is pursuing a bachelor's degree; (2)$40,000 for a graduate or professional student, including loans borrowed as an undergraduate student; and (3)$8,000 for any student who has not completed two academic years of undergraduate work.

The annual maximums and aggregate maximums include any amounts borrowed previously under the Federal Perkins Loan Program.

Because previous aggregate loan maximums were not tied to the completion of two academic years of undergraduate work, schools may have inadvertently created an overaward by awarding more than $8,000 to borrowers who had not completed two undergraduate years. The Department will not require schools to resolve such overawards if they were made prior to the publication of the revised statutory

Maximum Loan Eligibility Calculation

	Financial Need
(-)	Other resources
=	Maximum Perkins Loan

Loan limits cite
34 CFR 674.12

Annual maximum loan:
Undergraduate: $4,000
Graduate: $6,000

Aggregate maximum loan:
Undergraduate: $20,000
Graduate: $40,000

Overaward resolution cite
FR Vol. 64, No. 145, pg. 41235

maximums. (The proposed rule for the revised statutory maximum was published on July 29, 1999.)

A school may disburse a Perkins Loan to a student engaged in a program of study abroad if the student meets all eligibility requirements and is enrolled in an eligible program at the school that will accept credits earned abroad. If the reasonable costs of the foreign study program exceed the cost of attending the home school, the awarded Perkins Loan may exceed the annual and/or aggregate loan limits by up to 20%.

A student enrolled in a teacher certification program may be considered either an undergraduate or a graduate student as determined by the school. A teacher-certification student who is considered to be a graduate student and who has already borrowed the maximum aggregate allowed for an undergraduate is eligible to receive an additional Perkins Loan or NDSL. A teacher-certification student who is considered to be an undergraduate student and who has already borrowed the maximum aggregate allowed for an undergraduate is not eligible to receive an additional Perkins Loan or NDSL.

DISCLOSURE TO STUDENTS

Disclosure cite
34 CFR 674.16(a)

Before making the first Perkins Loan or NDSL disbursement, the school must have the student sign the promissory note. (Promissory notes are discussed later in this chapter.) The school must inform the student of her rights and responsibilities under the Federal Perkins Loan Program. The school must also remind the student that the loan may be used only for educational expenses and that the loan must be repaid. The school should also inform the student that the **school** holds the promissory note.

The school must disclose all information to the student **in writing**—as part of the application material, as part of the promissory note, or on a separate form. Although the information can be mailed to a student, it is preferable for the aid administrator to meet with the student to answer any questions and to emphasize his or her responsibility to repay the loan.

The school must review all of the repayment terms in the promissory note. In addition, the school must give the following information to the student:

- the name and address of the school to which the debt is owed and the name and address of the official or servicing agent to whom communications should be sent;
- the maximum annual and aggregate amounts the student may borrow;
- the effect that accepting the loan will have on the borrower's eligibility for other types of student aid;

- a statement of the total cumulative balance owed by the student to that school and an estimate of the monthly payment amount needed to repay that balance;
- options the borrower may have to consolidate or refinance;
- a brief notice about the Department of Defense program for repaying loans based on certain military service;
- a complete list of charges connected with making the loan, including whether those charges are deducted from the loan or whether the student must pay them separately; and
- a notice that the school will report the outstanding balance of the loan to a national credit bureau **at least annually**.

The school should also update the identification and contact information in the promissory note and collect the following additional contact information:

- the name, address, and telephone numbers of the borrower's parents and spouse;
- the spouse's employer; and
- the names and addresses of two or three of the student's personal acquaintances.

The additional contact information gained during loan counseling could be valuable later for use in collection procedures, and it will help the school locate a student who leaves school without notice or who does not attend the exit interview. However, this counseling may not be used to satisfy the requirement for an exit interview. (See chapter 7 of this volume.)

PROMISSORY NOTE

Promissory note cite
34 CFR 674.31

The promissory note is the legally binding document that is evidence of a borrower's indebtedness to a school. A student must sign this note before he or she can receive any Perkins Loan funds and must receive a copy of the note at (or before) the exit interview. The note includes information about the loan's interest rate, repayment terms, and minimum rates of repayment; deferment, forbearance, and cancellation provisions; credit-bureau reporting; late charges, attorney fees, collections costs, and consequences of default.

If the school does not have a valid note or other written evidence that would be upheld in a court of law, the school has no recourse against a borrower who defaults. Two examples of invalid notes are notes that have been changed after they were signed and notes without proper signatures or dates for loan advances. In such cases, the school would have to repay to its Perkins Loan Fund any amounts loaned, whether recovered from the borrower or not, as well as any Administrative Cost Allowance (ACA) claimed on those amounts.

Master Promissory Note

The following new definitions will take effect when the Department issues an approved Master Promissory Note.

A **Master Promissory Note(MPN)** is a promissory note under which the borrower may receive loans for a single award year or multiple award years.

The **making of a loan** occurs when the school makes the first disbursement of a loan to a student.

You must ensure that each Perkins Loan is supported by a legally enforceable promissory note.

You can no longer make a loan under an MPN:

- more than 10 years from the date the borrower signed the MPN or the date you received the MPN (schools can still disburse a remaining portion of a loan after this date);
- more than 12 months after the date the borrower signed the MPN, if you make no disbursement under that MPN;
- after the date you are notified by the borrower to stop using the MPN.

If an error is discovered in a promissory note, the school should obtain legal advice about what action it should take. The appropriate school official and the student should sign by or initial all approved changes in the note.

Retention of records cite
34 CFR 674.19(e)(4)(iii)

When the borrower has fully repaid the Perkins Loan, the school must mark the note "paid in full," have it certified by an official of the school, and give the original note to the borrower. The school must keep a copy of the note for at least three years after the date the loan was paid in full.

Approved promissory notes

A school must use a promissory note that the Department has approved. In Dear Partner Letter CB-01-15, dated November 2001, the Department issued **open-end** and **closed-end** approved promissory notes for NDSLs and Perkins Loans. (Although schools no longer issue NDSLs to new borrowers, schools must issue NDSLs to borrowers who have outstanding balances on previous NDSLs or Defense Loans.) See Appendix A for copies of the approved promissory notes.

In Dear Colleague Letter CB-02-12, dated July 2002, the Department issued electronic versions of the Perkins Loan and NDSL promissory notes (Perkins eNotes). Schools that use the Perkins

ELECTRONIC SIGNATURE STANDARDS: HIGHLIGHTS FOR eNOTES

(For complete instructions, see the Standards for Electronic Signatures in Electronic Loan Transactions (Standards) in Dear Partner Letter GEN-01-06, dated May 2001.)

Why apply these standards?

If your school's system for processing Perkins eNotes adheres to the Standards and a court finds the loan legally unenforceable based solely on the processing of the electronic signature or related records, the Department will not consider your school liable for the loan and will not require your school to reimburse its Perkins Loan Fund.

If your school's system for processing Perkins eNotes does not adhere to the Standards and a court finds the loan legally unenforceable based solely on the processing of the electronic signature or related records, the Department has the option to require your school to reimburse its Perkins Loan Fund.

Verify the borrower's identity. Verify the borrower's electronic signature.

Collect at least the following identifying information: name, Social Security Number, driver's license number, date of birth. Verify the borrower's identity by authenticating this data with an independent source such as a national commercial credit bureau, a commercial data service, a state motor vehicle agency, or a government database.

The electronic signature may be a PIN, a password, another unique credential, a biometric value unique to the borrower, such as a fingerprint or retinal pattern, or a signature image. A typed name must be paired with one of the above to constitute an electronic signature.

Ensure that the electronic signature is secure.

Get the borrower's consent. Make sure the borrower understands.

Obtain consent from the borrower to use an electronic record. It must be clear that the borrower has consented to use a Perkins eNote in place of a paper promissory note. Require the borrower to confirm that she has the necessary hardware and software to view, print, download, or otherwise complete the electronic signature process. Keep a record showing that the borrower gave this consent prior to electronically signing the Perkins eNote.

Ensure that the borrower understands he is signing a promissory note. The borrower must click through all terms and conditions of the Perkins eNote and acknowledge that he has read the terms and conditions.

Notify the borrower when her electronic signature is about to be applied to the Perkins eNote. Give the borrower an opportunity to cancel the signature process.

After the borrower signs the Perkins eNote, provide the borrower with reasonable access to the full electronic record of the eNote.

eNotes must adhere to the Standards for Electronic Signatures in Electronic Loan Transactions published in Dear Colleague Letter GEN-01-06, dated May 2001. (See boxed text on previous page for more information.) The new promissory notes (including eNotes) are authorized for use through October 31, 2004.

The new promissory notes reflect changes required by the Higher Education Amendments of 1998. The major changes made to the promissory notes include:

- provisions for the implementation of the loan rehabilitation program and clarification that the 24% cap on collection costs that may be assessed on a rehabilitated loan does not apply if the borrower defaults again on the rehabilitated loan;
- retained grace periods for borrowers who are ordered to active duty for a period of more than 30 days;
- notification of the availability of the Department of Education's Student Loan Ombudsman;
- the expansion of borrower eligibility for volunteer service cancellations for NDSL loans;
- the addition of a new section on Discharges;
- the addition of the Privacy Act Notice, Financial Privacy Act Notice, and the Paperwork Reduction Notice;
- a correction to the cross-references to the Individuals with Disabilities Act (IDEA) to reflect statutory changes as a result of the reauthorization of IDEA in 1997;
- revisions to the Deferment section to reflect that deferment requests no longer need to be in writing and that it is no longer necessary for a borrower to request an in-school deferment; and
- revisions to the Deferment section relating to economic hardship deferments for borrowers who are in the Peace Corps or who have received an economic hardship deferment under the Federal Family Education Loan Program or the William D. Ford Federal Direct Loan Program.

In addition, minor editorial changes were made in various sections of the promissory notes.

Limits to promissory note changes cite
34 CFR 674.31(a)

Schools may not make changes to, deletions from, or additions to the prescribed language. However, you may delete bracketed text. Of course, you may print information (name, address, and telephone number) identifying your school in Section B, Item 6. You may also use appropriate coding (for example, bar coding to reflect the source, type, or other identification system for filing or processing) in this area. You may print bar coding or coding identifiers, such as student ID number or loan number, in the side or bottom margins to meet the requirements of your school's processing systems. You may not print these coding identifiers on the promissory notes in a way that would alter the general layout of the note. You may also print in the lower margin of the promissory note a reference to the type: for example, original, student copy, file copy.

You must print the promissory notes with black ink on white paper. You may not change the typeface, point size, and general presentation of the form from the documents approved by the Department. However, you may print your school's identifying information located in Section B, Item 6 in another color to make your school's name and address more pronounced.

Closed-end vs. open-end

"Closed-end" or "Limited" Note. This note is valid for not more than 12 months and usually covers one award year or one academic year. It may also be used for a single academic term. The loan amount must be entered in the note. Closed-end notes can be designed for a single disbursement (if the award is less than $501) or multiple disbursements.

"Open-end" Note. Schools can use an open-end promissory note to make loans for more than one award year. The borrower signs next to the specified amount of the approved loan each time the school awards a new loan. If a school uses an open-end note, it does not have to issue new notes for future loans it makes to the same borrower **unless** the requirements of the Federal Perkins Loan Program are changed by statute or regulation.

Boxes 9 and 10 on the "open-end" note are intended to show the loan amount and loan period for the first year that the borrower takes out a loan. The borrower would then sign and date the note on the bottom of the page. For each subsequent year, the loan amount, loan period, date, and signature would be filled out in the columns beneath Items 9 and 10. If the borrower does not take out any additional Perkins Loans in later years, the columns would be left blank.

Changes in loan amount

If a student's initial loan amount **decreases** and a disbursement has been made, the school can choose one of the following options:

- It may leave the loan amount unchanged. (The school's disbursement records will reflect the decreased loan amount. The school may also attach a statement to the promissory note to explain the decreased loan amount.)
- It may change the face of the promissory note to reflect the decreased loan amount. Both the student and the appropriate school official must initial the decrease. A school must not unilaterally change the amount of the loan.

If the student has signed the promissory note and the initial loan amount **increases after a disbursement has been made**, the action a school must take depends on the type of promissory note involved:

- If the student signed a closed-end promissory note, the school **must** issue a new closed-end note reflecting only the increase from the original loan amount.
- If the student signed an open-end promissory note, the school **must** reflect only the increase in the loan amount on the next line of the note.

Minimum monthly payment option

The optional provision regarding a minimum monthly payment amount is included as a single, optional sentence at the end of the repayment paragraph on page 1 of the promissory notes. A school would include this sentence in the promissory note if the school is exercising the minimum monthly payment amount provision. Page 2 of the promissory notes includes a summary of this provision.

If the optional provisions are included in the school's note, a minimum monthly payment of $40 is required for a loan made on or after October 1, 1992 to a borrower who had no outstanding balance on a Perkins Loan, NDSL, or Defense Loan on the date the loan was made. (For other borrowers, the monthly minimum amount remains $30.)

GENERAL DISBURSEMENT REQUIREMENTS

A school must disburse funds in accordance with the cash management requirements of the General Provisions. These requirements are discussed in *Volume 2 - Institutional Eligibility and Participation*. This section discusses disbursement requirements that apply specifically to the Federal Perkins Loan Program.

(See volume 4 for a discussion of how to handle overpayments.)

Power of attorney

Power of attorney cite
34 CFR 674.16(h)

A school official may not use a student's power of attorney to endorse any disbursement check or to sign for any loan advance unless the Department has granted prior approval. Approval may be granted only if:

- the borrower is not available to sign the promissory note and there is no one else (such as a relative, landlord, or member of the clergy) who could act on behalf of the student;
- the school shows that the funds cannot be directly deposited or electronically transferred;
- the power of attorney is not granted to a school official or any other official who has an interest in the loan; and

Uneven Costs/Unequal Disbursement Example

$1,000	Total Loan
- $ 300	Additional Costs at Start of School
$ 700	÷ 2 Payment Periods = $350 Regular Payment
$ 350	Regular Payment
+$ 300	Extra for Books & Supplies
$ 650	Total First Disbursement ($350 = Second Disbursement)

- the power of attorney meets all legal requirements under the law of the state in which the school is located and the school retains the original document granting power of attorney in its files.

Frequency of disbursements

A school that is awarding a Perkins Loan for a full academic year must advance a portion of the loan during each payment period, **even if it does not use standard academic terms**.

In general, to determine the amount of each disbursement, a school will divide the total loan amount by the number of payment periods the student will attend. For a school that measures progress in credit hours and has academic terms, a payment period is defined as a term (a semester, trimester, quarter, or nonstandard term). The definition of payment period for a school that does not have academic terms or a school that measures progress in clock hours is discussed in detail in volume 2.

A school may advance funds **within** a payment period in whatever installments it determines will best meet the student's needs. However, if the total Perkins Loan amount awarded a student is less than $501 for an academic year, only one payment is necessary.

Uneven costs/unequal disbursements

If a student incurs uneven costs or resources during an academic year and needs additional funds during a payment period, the school may advance the additional amount to the student in whatever manner best meets the student's needs. The school may exercise this option **regardless of whether or not the school uses standard academic terms**.

Returning funds disbursed prior to attendance

If a school advances funds to a student who withdraws or is expelled before the first day of classes, or never begins attendance, all funds disbursed are considered an overpayment. The school must return any advanced amounts to the Perkins Loan Fund.

Frequency of disbursements cite
34 CFR 674.16(b)

Uneven costs/unequal disbursements example cite
Dan will receive a $1,000 Perkins Loan and must spend $300 for books and supplies at the beginning of the school year. Ingram College could disburse that $300 along with the first payment. To determine the first payment, Ingram College subtracts the extra amount (in this case, $300) from the total loan ($1,000) and divides the remainder ($700) by the number of payment periods (in this case, 2). Ingram College then adds the regular amount for one payment period ($350) to the extra amount ($300) to determine the initial payment ($650). The remaining amount ($350) is then disbursed during the second payment period for a total loan of $1,000.

Uneven costs/unequal disbursements cite
34 CFR 674.16(c)

Paying before the student begins attendance cite
34 CFR 674.16(f)

Credit bureau reporting cite
34 CFR 674.16(i)

Credit bureau reporting

Schools must report the date and amount of each disbursement of Federal Perkins Loan to at least one national credit bureau. (Please see chapter 7 for more information about credit bureau reporting.)

2001 Promissory Notes

Questions and Answers

BOXES 9 AND 10 ON THE OPEN-END NOTE

Q. Why does the open-end note contain boxes 9 and 10 (loan amount and loan period), since the open-end notes are designed to accommodate multiple loans? What amount should campuses put in box 9, loan amount—the entire amount of disbursements or the first disbursement? If it is the entire amount, then the box could not be filled in until the student received his/her last disbursement.

A. Put the loan amount and loan period for the first year in Items 9 and 10. Have the borrower sign and date the note on the bottom of the page. For each subsequent year, put the loan amount, loan period, date, and signature in the columns beneath Items 9 and 10. If the borrower does not take out any additional Perkins Loans in later years, leave the columns blank.

On the old version of the open-end promissory note, there were two places for a first-year borrower to sign, once in the "Borrower's Signature" column, and again at the bottom of the page. The newly approved open-end promissory note only requires one signature for a first-year borrower.

CHANGES TO THE NOTES

Q. May schools make changes to the promissory note, such as adding text or data elements? May schools reduce the number of pages of the note by printing it on legal-size paper rather than letter-size? May schools make "non-substantive changes" to the note, such as changes in font, type size, etc?

A. The old Perkins promissory notes were not OMB-approved forms, and schools were permitted to include additional data elements or to make "nonsubstantive" changes to the notes. The new promissory notes---the text, data elements and format---have been approved by OMB. Schools may not add data elements, change or add language, or alter the general layout of the note. Schools may only make minimal modifications to these OMB-approved promissory notes, as described in Dear Partner Letter CB-01-13. These limitations on the modifications that schools may make to the Perkins promissory notes are consistent with the limitations on modifications that lenders and guaranty agencies are permitted to make to promissory notes in the Federal Stafford, PLUS, and Consolidation Loan programs.

THE HEIGHT OF THE BOXES

Q. The boxes in Sections A and B are not big enough to print the required information in. Can we increase the height of these boxes?

A. Schools may increase the height of the boxes to meet the requirements of individual processing systems, as long as the change doesn't alter the general layout of the form, result in reduced point size, move text from one page to another, or otherwise change the general presentation of the form.

Questions and Answers (cont'd)

NUMBER OF PAGES

Q. Do I print the promissory note on two double-sided pages or on four single-sided pages?

A. It's preferable for the school to print the promissory note on two sheets of paper, front and back. However, schools may print the note on four single-sided pages as well. Schools may also print the forms front and back on one 11" by 17" sheet of paper that, when folded over, forms a pamphlet of four 8 1/2" by 11" pages. This would retain the same general presentation of the form and the four-page format.

USE OF COLOR PAPER

Q. Can I print the borrower, file, and exit copy of the promissory note on colored paper, and the original on white paper?

A. The original and borrower copies of the notes must be printed in black ink on white paper (except the information in Section B.6 may be printed with different color ink if the institution wants to make that information stand out).

CODING IDENTIFIERS

Q. Can we add student ID number and note number [or other identifying information] in the margin of the note?

A. You may print coding in the margins to meet the requirements of individual processing systems, as long as they are not printed on the promissory note in a way that would alter the general layout of the note.