Archived Information

# CONTENTS

## CHAPTER 6
## FEDERAL PERKINS LOAN PROGRAM

**INTRODUCTION ... 1**
Recent Changes to the Federal Perkins Loan Program ... 1
Participation Agreement and Federal Perkins Loan Fund ... 3
Allocation of Funds—Federal Capital Contribution ... 4

**SECTION 1: STUDENT ELIGIBILITY ... 7**
Eligibility Factors ... 8
Loan Availability ... 9
Eligibility of Student Who Drops Out ... 10

**SECTION 2: MAKING & DISBURSING LOANS ... 11**
Loan Maximums ... 11
Counseling Students ... 13
The Promissory Note ... 15
Comparison of July 1993 Notes with May 1996 Notes ... 16
Changes in Loan Amount—May 1996 Notes ... 17
School-Designed Note ... 17
Minimum Monthly Payment Option ... 18
Closed-end and Open-ended Promissory Notes ... 18
General Disbursement requirements ... 19
Frequency of Disbursements ... 21
Uneven Costs/Unequal Disbursements ... 21
Late Disbursements ... 22

**SECTION 3: REPAYMENT ... 23**
Grace Periods ... 23
Grace Period for Borrower attending Less Than Half Time ... 24
Prepayment ... 26
Repayment Plan ... 26
Exit Interview and Repayment Schedule ... 27
Developing a Repayment Schedule ... 27
Minimum Monthly Repayment Amounts ... 28
Establishing Repayment Dates ... 31
Interest Rates ... 32
Length of Repayment Period ... 32
Disposition of Promissory Note and Repayment Schedule ... 34

**SECTION 4: FORBEARANCE & DEFERMENT .......... 37**
Forbearance .......... 37
Deferment .......... 38
In-School Deferment—Common to All Program Loans .......... 39
Deferment of Loans Made on or After July 1, 1993 .......... 39
Deferment of Perkins Loans Made Before July 1, 1993 .......... 43
Deferment of NDSLs Made Between October 1, 1980 and July 1, 1993 .......... 46
Deferment vs. Postponement for Service That Will Qualify for Loan Cancellation .......... 48
The Concurrent Deferment Period .......... 49
Deferment and Default .......... 49
Deferment vs. In-School Enrollment Status .......... 50

**SECTION 5: CANCELLATION .......... 51**
U.S. Army Loan Repayment Program .......... 51
Common Cancellation Procedures .......... 51
Cancellation Provisions Common to All Loans Made After July 1, 1987 .......... 53
Law Enforcement Cancellation Provision—Specific to Loans Made on or After November 29, 1990 .......... 53
Cancellation Provisions Specific to Federal Perkins Loans and NDSLs Made on or After July 23, 1992 .......... 54
Military Service Cancellation—Applies to All Loans Made on or After July 1, 1972 .......... 55
Cancellation Provisions Specific to Perkins Loans .......... 55
Death, Total and Permanent Disability, and Bankruptcy Cancellation Provisions—Applicable to All Loans .......... 56
Criteria for Teacher Cancellation .......... 56
Criteria Borrower Must Meet for Military Cancellation .......... 61
Criteria for Head Start Cancellation .......... 61
Criteria for Employee of a Child or Family Services Agency .......... 61
Criteria for Law Enforcement or Corrections Officer Cancellation .......... 62
Criteria for Disability Cancellation .......... 62
Criteria for Receiving a Bankruptcy Cancellation .......... 63
Reimbursing Amounts Canceled .......... 63
Definitions .......... 64

**SECTION 6: DUE DILIGENCE—BILLING & ADDRESS SEARCHES .......... 67**
Exit Interview .......... 67
Contact During Grace Periods .......... 70
Billing Procedures .......... 71
Address Searches .......... 74

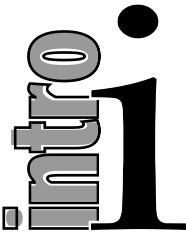
**SECTION 7: DUE DILIGENCE—LOAN COLLECTION .......... 77**
Collection Procedures .......... 77
Actions a School May Take to Avoid Litigation .......... 79
Litigation .......... 81
Deposit of Funds Collected .......... 82
Costs Chargeable to the Federal Perkins Loan Fund .......... 82
Using Billing and Collection Firms .......... 84

**SECTION 8: DEFAULT** ........ **87**
Compromise of Repayment of Defaulted Loan ........ 88
Penalty for Schools With High Cohort Default Rates ........ 89
Calculating a School's Cohort Default Rate ........ 89
Defaulted Loans Included in a School's Cohort Default Rate ........ 90
Rules for Calculating the Number of Days in Default ........ 92
Cohort Default Rate for a School With More Than One Location ........ 93
Default Reduction Plan ........ 94
Assignment ........ 97
Default Prevention Software ........ 99
Default and Student Eligibility ........ 99

**SECTION 9: BANKRUPTCY** ........ **101**
When Borrower Requests Discharge Based on Undue Hardship ........ 101
Procedures When Borrower Requests Adjustment in Repayment ........ 102

**SECTION 10: CREDIT BUREAU REPORTING** ........ **105**

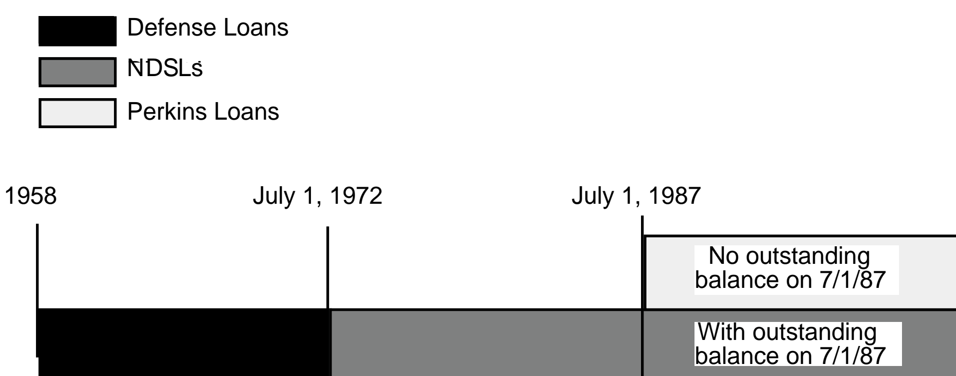
**SECTION 11: PROGRAM FUNDS** ........ **107**
Fiscal Procedures ........ 108
Recordkeeping Requirements ........ 110



# Introduction

Loans under the Federal Perkins Loan Program include Federal Perkins Loans, National Direct Student Loans (NDSLs), and National Defense Student Loans (Defense Loans). (No new Defense Loans were made after July 1, 1972, but a few are still in repayment.) Perkins Loans and NDSLs are low-interest, long-term loans made through institutional financial aid offices to help needy undergraduate and graduate students pay postsecondary educational costs. The school must give priority to students with exceptional financial need as defined by the school. (See Section 1 of this chapter.) The current interest rate is 5%.

Loans made before July 1, 1972 were Defense Loans. Loans made from July 1, 1972 through June 30, 1987 were NDSLs. A loan made on or after July 1, 1987 may be either an NDSL or a Perkins Loan. If the borrower has an outstanding balance on a Defense Loan or NDSL when the new loan is obtained, the new loan is an NDSL. If the borrower has no outstanding balance on a Defense Loan or NDSL when the new loan is obtained, the new loan is a Perkins Loan.




## RECENT CHANGES TO THE FEDERAL PERKINS LOAN PROGRAM

Part 673 has been added to the regulations as “Part 673—General Provisions for the Federal Perkins Loan Program, Federal Work-Study Program, and Federal Supplemental Educational Opportunity Grant Program,” published in the **Federal Register** (Part IV) on November27, 1996. Part 673 consolidates common provisions of the campus-based programs (formerly found in Parts 674, 675, and 676), and eliminates

duplicate provisions for each program. The regulations, which are effective July 1, 1997, are discussed in the Introduction to Chapter 5 of this Handbook.

***Recordkeeping requirements—34CFR 668.24 & 674.19***

New recordkeeping requirements for all Student Financial Assistance (SFA) programs were published in the **Federal Register** November 27, 1996 and become effective July 1, 1997. These regulations specify the length of time records must be kept and the formats in which they must be kept. These new requirements as they apply in general to all SFA programs are discussed in Chapter 3, Section 7. For information on how these requirements apply specifically to the campus-based programs, see Chapter 5, Section 3. For information on how these requirements apply specifically to the Perkins Loan Program, see Section 11 of this chapter.

Requirements for maintaining and accounting for SFA program funds are included in regulations published in the **Federal Register** November 29, 1996 and become effective July 1, 1997. The new cash management requirements that apply specifically to the campus-based programs are discussed in Chapter 5, Section 3. The new provisions that apply to all SFA programs are discussed in detail in Chapter 3, Section3.

***Cash management—34CFR 668.161 - 668.167***

The new cash management requirements that apply specifically to the Perkins Loan Program follow. (Section 11 of this chapter provides additional information on fiscal procedures and records.)

***Late disbursements***

◊ The late disbursement provision of the new cash management regulations applies specifically to the Federal Supplemental Educational Opportunity Grant (FSEOG) Program and the Perkins Loan Program. Regulations regarding late disbursements of an FSEOG were removed from 34 CFR 676.16(e), and revised regulations for late disbursements of FSEOGs and Federal Perkins Loans are now in 34CFR 668.164(g). A school may make a late disbursement of a Perkins Loan and/or an FSEOG to an ineligible student if the student became ineligible solely because the student is no longer enrolled at the school for the award year. Before the student dropped out, the school must have received a Student Aid Report (SAR) or Institutional Student Information Record (ISIR) for the student with an official Expected Family Contribution (EFC) and must have awarded the student the Perkins Loan or FSEOG. The school may make that late disbursement only if the funds are used to pay for educational costs that the school determines the student incurred for the period in which the student was enrolled and eligible, and the school must make the late disbursement no later than 90 days after the date the student became ineligible because he or she was no longer enrolled.

◊ Under the provisions of 34 CFR 668.163(c), schools must maintain the Perkins Loan Program Fund in an interest-bearing bank account or investment account (refer to Section 11 of this chapter).

◊ If a school credits a student's account at the school with Perkins Loan funds, the school must notify the student of the date and amount of the disbursement, the student's right to cancel all or a portion of that loan and his or her right to have the funds returned to the school's Perkins fund; a detailed discussion of these provisions is in Chapter 5, Section 3.

***Notification of a student's right to cancel loan—34CFR 668.165(a)***

## *PARTICIPATION AGREEMENT AND FEDERAL PERKINS LOAN FUND*

As discussed in Chapters 3 and 5, a school that wants to participate in any Student Financial Assistance (SFA) Program must sign a Program Participation Agreement with the Secretary. The agreement must be signed by the school official legally authorized to assume, on the school's behalf, the agreement's obligations.

For all of the SFA Programs, the agreement provides that the school must use the funds it receives solely for the purposes specified in the regulations for each program and requires the school to administer each program in accordance with the Higher Education Act of 1965 (HEA), as amended, and the Student Assistance General Provisions regulations. The agreement also requires the school to submit annually to the U.S. Department of Education a report containing information that will enable the Department to determine the school's cohort default rate (discussed in Section 8 of this chapter).

The agreement for the Perkins Loan Program also requires the school to establish and maintain a Perkins Loan fund (the fund) and to deposit into the fund—

◊ the Federal Capital Contribution (FCC) the school receives as its federal allocation for the program for each award year (see the next page);

◊ the school's matching share—the institution's capital contribution (ICC), discussed on the next page;

◊ payments the school receives for repayment of loan principal, interest, collection charges, and penalty or late charges on loans from the fund;

◊ payments the school receives from the federal government for cancellations (such as teacher cancellations) of Perkins Loans and NDSLs (see Section 5 of this chapter);

◊ any other earnings on fund assets, including net interest earnings on funds deposited in an interest-bearing account (total interest minus bank charges incurred on the account); and

◊ proceeds of any short-term no-interest loans the school makes to the fund in anticipation of receipt of its FCC or of loan collections.

## *ALLOCATION OF FUNDS—FEDERAL CAPITAL CONTRIBUTION*

As discussed in the introduction to Chapter 5, a school applies for program funds annually through the electronic *Fiscal Operations Report and Application to Participate* (FISAP). The Department allocates funds directly to schools. The allocation for the Perkins Loan Program, the FCC is the amount of funding the school is authorized to receive from the Department for an award year. This amount is based on the funds appropriated by Congress for the program, as well as the allocation formulas, which were established by law and which do not provide for appeals.

The following provisions of the HEA and the Perkins Loan Program regulations affect the school's allocation:

***Basis for initial allocation— HEA 462(a)***

***Basis for reallocation— 34CFR 673.4(a)***

***School's matching share— 34CFR 674.8***

◊ The Department bases the initial allocation of a school's FCC on the amount allocated to the school for the 1985-86 award year.

◊ The Department reallocates funds to schools by reallocating 80% of the total funds in accordance with the statutory formula in section 462(j) of the HEA and reallocating 20% in a manner that best carries out the purposes of the Perkins Loan Program.

◊ The school's matching share or ICC is one-third of the FCC (or 25% of the **combined** FCC and ICC); however, schools participating in the Expanded Lending Option (ELO) are required to provide a dollar-for-dollar match with the FCC.

◊ If a school returns more than 10% of its FCC, the Department will reduce the school's FCC for the second succeeding year by the dollar amount returned.

◊ A school may transfer up to a total of 25% of its FCC for an award year to either or both the FSEOG and FWS programs.

◊ A school may transfer up to 100% of its initial and supplemental allocations to the Work-Colleges Program.

◊ A school must match any funds transferred to another program at the matching rate of that program. The school does not have to provide matching funds until the transfer has occurred.

◊ A school must use the transferred funds according to the requirements of the program to which they are transferred.

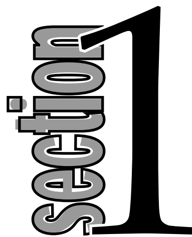
◊ A school must report any funds that are transferred to another program on the Fiscal Operations Report portion of the FISAP.

◊ A school that transfers funds to the FWS, FSEOG, and/or Work-Colleges programs must transfer any unexpended funds **back** to the Perkins Loan Program at the end of the award year.

◊ If a school's cohort default rate equals or exceeds 20%, the school's FCC will be reduced by a default penalty percentage calculated in relation to the school's cohort default rate. (See Section 8, "Default.")

***Transfer of funds to FWS and/or FSEOG—34CFR 674.18(c)***

***Reduction of FCC for high cohort default rate—34CFR 674.5***



# Student Eligibility

The eligibility criteria for Federal Perkins Loans are provided in 34CFR 674.9. Of course, a student must also meet the student eligibility criteria of the General Provisions (34CFR 668.32). Both undergraduate and graduate students may receive loans under the Perkins Loan Program. To be eligible for a Perkins Loan, a student must meet the general student eligibility requirements discussed in Chapter 2 of this handbook and must not have borrowed the maximum amounts listed in Section 2 of this chapter. A student who has earned a bachelor's or first professional degree may receive a Perkins Loan to pursue an **additional undergraduate** degree provided that he or she meets the eligibility requirements. A student engaged in a program of study abroad also may be eligible for a Perkins Loan.

***Study abroad***

An individual who is serving in a medical internship or residency program is not eligible for a Perkins Loan. This provision in Section 464(c)(2)(A)(i) of the Higher Education Act (HEA), as amended, became effective January1, 1990 and does not apply to dental internships. A student in a dental internship may receive a Perkins Loan.

***Medical interns and residents***

An incarcerated student is not eligible to receive a loan from any of the U.S. Department of Education's loan programs, including the Perkins Loan Program.

***Incarcerated students—34CFR 668.32(c)(2)(i)***

A school must give priority to those students with exceptional financial need as defined by the school using procedures it establishes for that purpose. The school's selection procedures must be in writing, uniformly applied, and kept on file at the school. Before an undergraduate student can receive a loan, the school must determine his or her eligibility or ineligibility for a Federal Pell Grant; a preliminary hand calculation is acceptable after a student has filed a *Free Application for Federal Student Aid* (FAFSA) with the Central Processing System (CPS). Note that even if the hand calculation shows the undergraduate student will be ineligible for a Pell Grant, the student must apply for one before a Perkins Loan can be awarded. Remember that a school may not disburse a Perkins Loan to a student unless he or she has an "official" Expected Family Contribution (EFC) that has been calculated by the CPS for the same award year in which the disbursement will be made.

***Exceptional financial need***

***Independent and less-than-full-time students***

A school must offer at least 5% of the dollar amount of loans made under the Perkins Loan Program to independent students and less-than-full-time students if the Federal Capital Contribution (FCC) for the program is partly based on the financial need of these students and the financial need of these students exceeds 5% of the total financial need of all students at the school (see Chapter 5, Section 1).

***Teacher certification programs***

A school may award a Perkins Loan and/or a Federal Work-Study (FWS) job to a student who is enrolled or accepted for enrollment at least half time in an eligible teacher certification or professional credential program. Eligibility criteria for such a program are discussed in Chapter 5, Section1.

## *ELIGIBILITY FACTORS*

***Willingness to repay***

In selecting among eligible applicants, a school must consider evidence of a student's willingness to repay the loan. Failure to meet payment obligations on a previous loan is evidence that the student is unwilling to repay other loans. (For more information, see "Default and Student Eligibility," in Section 8 of this chapter.)

***Loan that was written off***

If a borrower had a previous Perkins Loan, National Direct Student Loan (NDSL), or National Defense Student Loan (Defense Loan) that was written off because the school was unable to collect, the borrower may be eligible for a new loan only if he or she reaffirms the debt. Reaffirmation is not required if the amount written off was $25 or less. To reaffirm a debt that was written off, the borrower must acknowledge the loan in a legally binding manner, such as by signing a new promissory note, by signing a new repayment agreement, or by making a payment on the loan.

***Previous cancellation due to disability***

If a student has obtained a cancellation of a previous Perkins Loan or NDSL due to permanent and total disability and is applying for a subsequent Perkins Loan or NDSL, the borrower may be eligible to receive additional funds from the Perkins Loan Program if he or she meets certain conditions. These conditions follow:

- ◊ the borrower's physician certifies that the borrower's condition has improved and that he or she is able to engage in substantial gainful activity, and
- ◊ the borrower signs a statement acknowledging that any new Perkins Loan or NDSL cannot be canceled in the future on the basis of any present impairment, unless the condition substantially deteriorates to the extent that the definition of total and permanent disability is again met.

Note that if a loan was canceled based on the borrower's permanent and total disability, the borrower cannot subsequently be required to repay that loan, even if the borrower's medical condition improves to the point that he or she is no longer disabled, unless the school can prove that the claim of disability was fraudulent—refer to the discussion in Section 5 of this chapter.

***Previous discharge in bankruptcy***

As a result of the Bankruptcy Reform Act of 1994, a student may not be denied student financial assistance from the Department's programs, including the Perkins Loan Program, solely on the basis of a bankruptcy determination. If a student has filed for or received a discharge in bankruptcy, has had a student loan discharged in bankruptcy, or has not paid a student loan that has been determined by a court of law to be dischargeable in bankruptcy, the bankruptcy may be considered as evidence of an adverse credit history but cannot be the basis for denial of a future loan from the Perkins Loan Program or other student loan programs. A student is no longer required to establish eligibility for a new student loan by agreeing to repay the loan discharged in bankruptcy. However, schools may continue to consider the student's **post-**bankruptcy credit history in determining willingness to repay the loan.

## *LOAN AVAILABILITY*

Schools must make loans reasonably available to all eligible students, to the extent of available funds, with loans made first to students with exceptional need. A school may not exclude a particular category of students. As stated earlier, at least 5% of the Perkins Loan funds a school advances to students for an award year must be offered to independent students and less-than-full-time students if the school's FCC for that award year is partly based on the financial need of these students and the financial need of these students exceeds 5% of the total financial need of all students at the school.

***Schools may set priorities***

However, the school may set certain priorities when packaging aid. For example, a school could first distribute Perkins Loans to full-time third-year students whose financial need is at least $500 after their Expected Family Contributions (EFCs), Pell Grants, and any scholarships received have been subtracted from the cost of attendance. Perkins Loan funds may not be used exclusively for such a group, of course, but it is permissible to establish priorities.

***Schools may request certain disclosures***

In administering the Perkins Loan Program, a school must comply with the equal credit opportunity requirements of Regulation B (12 CFR Part 202). The Department considers the Perkins Loan Program to be a credit assistance program authorized by federal law for the benefit of an economically disadvantaged class of persons within the meaning of 12CFR202.8(a)(1). Therefore, a school may request that a loan applicant

disclose marital status, income from alimony, child support, and spouse's income and signature.

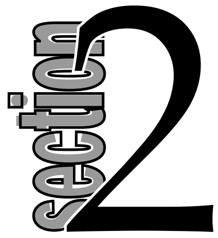
## ELIGIBILITY OF STUDENT WHO DROPS OUT

***Late disbursement— 34CFR 668.164(g)***

A student who drops out **before** receiving his or her Perkins Loan may be eligible to receive a payment, but only under the circumstances discussed below.

Regulations regarding late disbursement of a Perkins Loan were removed from 34CFR 674.16 (g), and revised regulations are now in 34CFR 668.164(g). A school may make a late disbursement of a Perkins Loan to an ineligible student if the student became ineligible solely because the student is no longer enrolled at the school for the award year. Before the student dropped out, the school must have received a SAR or ISIR for the student with an official EFC and have awarded the student the Perkins Loan or FSEOG. The school may make that late disbursement only if the funds are used to pay for educational costs that the school determines the student incurred for the period in which the student was enrolled and eligible, and the school must make the late disbursement no later than 90 days after the date the student became ineligible because he or she was no longer enrolled.

If a student drops out **after** receiving his or her Perkins Loan, but before the end of the payment period, the school determines the amount of any refund and repayment as discussed in Chapter 3, Section 4, "Refunds and Repayments."



# Making & Disbursing Loans

A Federal Perkins Loan or National Direct Student Loan (NDSL) is considered to be 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. Beginning July 1, 1996, the student is required to sign the promissory 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 continue to require a borrower to sign for each advance if it chooses to do so.

***34 CFR 674.16(c)(2)***

A financial aid administrator may not award or disburse a Perkins Loan or NDSL to a student if the combination of that loan and all of the student's other resources would exceed the student's need. The aid administrator must take into account those resources that he or she can reasonably anticipate at the time aid is awarded to the student, those the school makes available to its students, or those the aid administrator knows about. A list of resources and a discussion of overawards are in Chapter 5, Section 2.

***Financial need - Other resources***

***Maximum loan eligibility***

The regulations now provide uniform cash management rules, which became effective July1, 1995, for the Student Financial Assistance (SFA) Programs. These provisions cover disbursing funds to a student, crediting a student's account, calculating allowable charges, and holding student loans, and they are discussed in Chapter 3, Section 3. The major provisions affecting Perkins Loan disbursement are discussed on page 6-19.

***Disbursement of SFA funds—34CFR 668.164***

## LOAN MAXIMUMS

If a student is attending a school that does **not** participate in the Perkins Loan Program's Expanded Lending Option (ELO), which is discussed below, the maximum amount an eligible student may borrow is

- ◊ $3,000 per award year for a student who has not successfully completed a program of undergraduate education or
- ◊ $5,000 per award year for a graduate or professional student.

The maximum cumulative amount an eligible student may borrow at schools that do **not** participate in the ELO is

- ◊ $15,000 for a student who has not successfully completed a program of undergraduate education or
- ◊ $30,000 for a graduate or professional student, including loans borrowed as an undergraduate student.

***Expanded Lending Option (ELO)***

A school that maintains a cohort default rate of 15% or less may participate in the ELO if the school has signed an ELO participation agreement with the Department. (Cohort default rates are discussed in Section 8 of this chapter.)

Schools participating in the ELO are required to match the Federal Capital Contribution (FCC) on a dollar-for-dollar basis, and they may make loans to students at higher award-year and cumulative loan limits than nonparticipating schools.

***Loan limits at ELO schools***

If a student is attending a school that participates in the ELO, the maximum amount the 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 maximum cumulative amount an eligible student may borrow at a school that participates in the ELO is

- ◊ $20,000 for a student who has successfully completed two years of a program leading to a bachelor's degree but who has not completed the work necessary for the degree;
- ◊ $40,000 for a graduate or professional student, including loans borrowed as an undergraduate student; or
- ◊ $8,000 for all other students.

***Effect of repayment on loan limit***

All of the cumulative maximum amounts listed here include all Defense Loans, NDSLs, and Perkins Loans a borrower may have. Unlike repayment in the Federal Family Education Loan (FFEL) Program, repayment in the Perkins Loan Program does not establish a new cumulative loan limit. For example, 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 borrowed.

**Study abroad**

A student engaged in a program of study abroad may receive a Perkins Loan provided that he or she meets all eligibility requirements. A student studying abroad in a program approved for credit by the home school where the student is enrolled may exceed the annual and/or cumulative loan limits by 20% if reasonable costs of the program exceed the cost of attending the home school.

**Loans limits for teacher-certification students**

A student enrolled in a teacher certification program may be considered either an undergraduate or a graduate student. This determination is left to the student's school. The borrowing limit for a student enrolled in a teacher certification program depends on the school's determination of his or her status (undergraduate or graduate). A teacher-certification student who is considered to be a graduate student and who has already borrowed the cumulative maximum 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 cumulative maximum allowed for an undergraduate is not eligible to receive an additional Perkins Loan or NDSL.

## COUNSELING STUDENTS

**School must provide certain information**

**Before making the first Perkins Loan or NDSL disbursement,** the school must have the student sign the promissory note. (See Section 2 of this chapter.) The school must also furnish the student with certain information. It must inform the student about his or her rights and responsibilities under the Perkins Loan Program, and it must inform him or her that the loan may be used only for educational expenses and that he or she must repay the loan. The school should also make sure the student knows that the **school** holds the promissory note.

A school must also provide the student with the following information in writing before making the first loan disbursement:

1. the name of the school and the addresses where payments and communications should be sent;

2. a statement indicating that the school will report the outstanding balance of the loan to a national credit bureau at least annually;

3. the principal amount of the loan;

4. the stated interest rate;

5. the maximum yearly and cumulative amounts the student may borrow;

6. an explanation of when the student must start repayment and when he or she must begin paying the interest that accrues;

7. the maximum and minimum repayment terms the school may impose and the minimum monthly payment required;

8. 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;

9. options the borrower may have to consolidate or refinance;

10. the borrower's right to prepay all or part of the loan at any time without penalty;

11. a summary of circumstances in which repayment of the loan principal or interest may be deferred or canceled, including a brief notice about the Department of Defense program for repaying loans based on certain military service;

12. a definition of default and the consequences for the borrower, including a statement that the school may report the default to a national credit bureau;

13. the effect that accepting the loan will have on the borrower's eligibility for other types of student aid;

14. 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

15. an explanation of the costs that may be assessed the student in collecting the loan, such as late charges and collection and litigation costs.

The school must provide this 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.

***Obtain information from students***

The school is encouraged to use this initial counseling session to obtain the following information from a student:

◊ the student's name, current address, and Social Security Number;

◊ the student's parents' permanent address;

◊ the student's and his or her parents' telephone numbers;

◊ the student's expected date of graduation;

◊ the student's spouse's name and address;

◊ the student's spouse's employer;

◊ the names and addresses of two or three of the student's personal acquaintances; and

◊ the student's drivers license number, if any.

This information 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. Effective pre-loan counseling sessions will satisfy the school's requirement to tell each borrower about his or her rights and obligations and to provide information about the requirement to repay the loan. However, this counseling may not be used to satisfy the requirement for an exit interview. (See Section 6 of this chapter for more information.)

## *THE PROMISSORY NOTE*

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 be given 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; collection costs; attorney fees; and late charges.

***"Dear Colleague" Letters CB-93-9 and CB-96-8***

The Department has issued two sets of different promissory notes, either of which a school may use. "Dear Colleague" Letter CB-93-9, dated July 1993, included information and sample promissory notes. The Department issued redesigns of the July1993 promissory notes in "Dear Colleague" Letter CB-96-8, dated May1996. Both sets of notes (July1993 and May1996) include all changes required by the Higher Education Amendments of 1992. A school must use a promissory note that the Department has approved; the school may make only nonsubstantive changes to the note (such as changes to the type style or the addition of items such as the borrower's driver's license number).

A promissory note must state that the school is required to disclose to any one of the national credit bureaus with which the Department has an agreement the amount of the loan made to the borrower along with other relevant information. The note must also state that if the borrower

defaults on the loan, the school or the Department, if the loan is assigned to the Department for collection, is required to disclose the default and any other relevant information to the same national credit bureau to which the loan was originally reported.

***Minor who signs promissory note***

The Higher Education Amendments of 1992 eliminated the "defense of infancy," whereby the signing of a contract by a minor would not create a binding obligation. Under this provision of the law, a minor may sign a promissory note without an endorser or any security, and the minor who signs is responsible for repayment regardless of any state law to the contrary.

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. 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. 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.

## *COMPARISON OF JULY 1993 NOTES WITH MAY 1996 NOTES*

The Department redesigned the July1993 promissory notes to facilitate implementing the signature requirement change, which allows a school to obtain a borrower's signature on the note only once each award year, rather than each time a disbursement is made. The May 1996 promissory note is a single-page (front and back) document. Separate promissory notes based on the borrower's enrollment status (half time or greater or less than half time) have been eliminated, as were separate sections for obtaining information on prior Perkins Loans and for obtaining a borrower's signature for each loan advance.

There are no new provisions in the May1996 notes. A school still has the option of using a closed-end or open-ended note. The sample promissory notes issued in July1993 are open-ended notes. Those issued in May1996 are provided in both formats. As stated previously, a school is not required to use the May1996 notes. If a school chooses to use the July1993 promissory notes, it will be required to obtain the borrower's signature for each advance (disbursement) of the loan. **A school may not alter the July1993 promissory notes to reflect the changed signature requirement.** A borrower for whom the school uses a July1993 note is required to sign at the end of the last page of the note.

## CHANGES IN LOAN AMOUNT—MAY 1996 NOTES

**Decrease in loan amount**

If a student's initial loan amount **decreases**; the borrower has signed either an open-ended or a closed-end May 1996 promissory note; 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. This option requires that both the student and appropriate school official initial the decrease. A school must not unilaterally change the amount of the loan.

**Increase in loan amount**

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-ended promissory note, the school **must** reflect only the increase in the loan amount on the next line of the note.

## SCHOOL-DESIGNED NOTE

A school may develop its own notes, which may include some or all of the optional provisions in the Department-provided note. However, a school-designed note must include **all** of the required information and must be based on the sample notes the Department has provided. A school may not change the text or the order of the text in the Department-provided notes, and a school may not add provisions to the note. The school may add such information as the student's driver's license number to the note.

There is no minimum size of type or print specified for the notes. However, the notes must be legible so that a borrower would not be able to claim a defense against repayment of the loan because the print was too small to be read.

## MINIMUM MONTHLY PAYMENT OPTION

Optional provisions regarding a minimum monthly payment amount are included in the July1993 sample promissory notes (bracketed paragraphs III(5)(A) and III(5)(B)), and a school may choose to include these provisions. However, a school must either include both paragraphs or omit both paragraphs. If a school includes both paragraphs in the promissory note, the note must state the exact minimum monthly payment amount. If a school does not include the minimum monthly payment option in the note, the school may not require a minimum monthly payment amount from the borrower.

The optional provision regarding a minimum monthly payment amount is included as a single, optional sentence at the end of the repayment paragraph on page1 of the May1996 promissory notes. A school would include this sentence in the promissory note if the school is exercising the minimum monthly payment amount provision. Page2 of the May1996 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.)

## CLOSED-END AND OPEN-ENDED PROMISSORY NOTES

If a school is developing its own notes, it may use either "closed-end" ("limited") or "open-ended" notes. A note may be printed on more than one sheet of paper if the borrower signs each page or if each page contains the number of that page plus the total number of pages in the note (for example, page 1 of 3, page 2 of 3).

***Time limit for closed-end notes***

◊ **"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. If a school uses multiple disbursements and uses the July1993 promissory notes, the borrower must sign for each advance. If there will be only one disbursement, the borrower's signature at the end of the note is sufficient.

◊ **"Open-ended" Note.** If a school uses an open-ended note, it does not have to issue new notes for future loans it makes to the same borrower **unless** the requirements of the Perkins Loan

Program are changed by statute or regulation. An open-ended note may be used for several years.

The sample notes in "Dear Colleague" Letter CB-93-9 are open-ended notes. This open-ended note does not itself contain the specific amount of the approved loan. Instead, at the time of each disbursement, the school must enter the amount advanced and the date of receipt in the "Schedule of Advances," which is a part of the note. The borrower must sign this schedule **each time** he or she receives a disbursement. **It is not acceptable practice for the student to sign in advance.**

"Dear Colleague" Letter CB-96-8 also provides an open-ended note. Unlike the July1993 open-ended note, this open-ended note contains the specified amount of the approved loan for each award year.

***Requirements for loans that have been paid in full***

When a borrower has fully repaid a 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 repaid in full.

## *GENERAL DISBURSEMENT REQUIREMENTS*

A school must disburse Federal Supplemental Educational Opportunity Grant (FSEOG) funds to a student or the student's school account in accordance with the revised cash management regulations published in the **Federal Register** November 29, 1996 and effective July1, 1997. The new cash management requirements that apply specifically to the campus-based programs are discussed in Chapter 5, Section 3. The new provisions that apply to all SFA programs are discussed in detail in Chapter 3, Section3.

The new disbursement provisions that are specifically applicable to Perkins Loans follow:

***Notification of student's right to cancel loan—34CFR 668.165(a)***

◊ If a school credits a student's account at the school with Perkins Loan funds, the school must notify the student of the date and amount of the disbursement, the student's right to cancel all or a portion of that loan and his or her right to have the funds returned to the school's Perkins fund.

◊ The school must send the above notice, either in writing or electronically, within 30 days of the date the school credits the student's account at the school. If the school sends the notice electronically, the school must require the student to confirm receipt of the notice, and must keep a copy of the confirmation.

◊ The school must return the Perkins Loan proceeds, cancel the loan, or do both if

- it receives a loan cancellation request within 14 days after the school sends the notice to the student, or

- the school sends the notice more than 14 days before the first day of the payment period, and the school receives a loan cancellation request by the first day of the payment period.

◊ If the school does not receive the cancellation request within the time period described above, the school may return the loan proceeds, cancel the loan, or do both, but is not required to do so. The school must notify the student in writing or electronically of the school's decision.

A school may not disburse funds for a payment period until the student enrolls for that period.

The school must report the disbursement and amount of each Perkins Loan or NDSL to a national credit bureau with which the Department has an agreement. See Section 10 for further details on complying with this requirement.

***34CFR Section 674.16(f)***

Keep in mind that if a school makes payments before the student begins attendance, it must accept responsibility for any overpayment. If a student withdraws—or is expelled—before the first day of classes, for example, all funds disbursed are considered an overpayment and must be restored to the Perkins Loan fund. A student who never begins class is considered to have withdrawn.

***Power of attorney— 34CFR Section 674.16(i)***

A school official may not obtain a student's power of attorney to endorse any check used to disburse funds or to sign for any loan advance unless the Department has granted prior approval. The Department would not grant such a power of attorney unless the school could demonstrate that there is no one else (such as a relative, landlord, or member of the clergy) who could act on behalf of the student. There are no exceptions to gaining prior approval to obtain a student's power of attorney. For a student studying abroad, the school does not automatically obtain the student's power of attorney; the school will still be required to request the Department's approval and to demonstrate that there is no one else who can act on behalf of the student.

## FREQUENCY OF DISBURSEMENTS

Beginning July 1, 1997, 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**. Previously, a school was required to advance a portion of a Perkins Loan during each payment period only if the school used standard academic terms. A school that did not use standard academic terms was required to advance funds at least twice during the academic year—once at the beginning and once at the midpoint. Thus, for the purpose of the frequency of Perkins Loan disbursements, the standardization of disbursement rules across the SFA programs represents no change for schools using 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. The definition of payment period is in 34 CFR 668.4. 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 Chapter 3, Section 3.

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 amount awarded a student under the Perkins Loan Program is less than $501 for an academic year, only one payment is necessary.

***Student attending less than a full academic year***

For a student attending less than a full academic year, the amount advanced is determined by dividing the loan amount by the number of payment periods the student will attend in the academic year. Only one payment is necessary if the total Perkins Loan amount awarded to a student for an academic year is less than $501.

## 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 **regardless of whether the school uses standard academic terms**. Suppose that a student who will receive a $1,000 Perkins Loan must spend $300 for books and supplies at the beginning of the school year. That $300 could be disbursed along with the first payment. To determine the first payment, subtract the extra amount (in this case, $300) from the total loan and divide the remainder by the number of payment periods. The regular amount for one payment period is then added to the extra amount to determine the initial payment.

A school that has a two-semester system would determine the payments as follows:

| | |
|---|---|
| $1,000 | Total loan |
| - $ 300 | Additional costs at beginning of school |
| $ 700 ÷ | 2 payment periods = $350 regular payment |
| | |
| $ 350 | Regular payment |
| + $ 300 | Extra for books and supplies |
| $ 650 | Total first disbursement<br>($350 would be the second disbursement) |

Within a payment period, the school may advance funds in whatever installments it determines will best meet the student's needs.

## *LATE DISBURSEMENTS*

Regulations regarding late disbursement of a Perkins Loan were removed from 34CFR 674.16 (g), and revised regulations are now in 34CFR 668.164(g). A school may make a late disbursement of a Perkins Loan to an ineligible student if the student became ineligible solely because the student is no longer enrolled at the school for the award year. Before the student dropped out, the school must have received a Student Aid Report (SAR) or Institutional Student Information Record (ISIR) for the student with an official EFC and have awarded the student the Perkins Loan. The school may make that late disbursement only if the funds are used to pay for educational costs that the school determines the student incurred for the period in which the student was enrolled and eligible, and the school must make the late disbursement no later than 90 days after the date the student became ineligible because he or she was no longer enrolled.

# Repayment

## GRACE PERIODS

***Initial grace period***

A "grace period" is the period of time before the borrower must begin or resume repaying a loan. An "initial grace period" is one that immediately follows a period of enrollment and immediately precedes the date repayment is required to begin for the first time.

***Grace period depends on when loan was made***

For borrowers who have been attending at least half time, initial grace periods are either six or nine consecutive months after the borrower drops below half-time study at an eligible institution or at a comparable school outside the United States. The length of the initial grace period varies because of legislative changes to the Federal Perkins Loan Program. Repayment terms also vary, depending on when a borrower took out a loan. If a borrower has several loans, each is subject to the repayment terms in effect at the time the particular loan was made.

If a borrower requests a deferment to begin during the initial grace period, the borrower must waive (in writing) his or her rights to the initial grace period. The request for a deferment alone is not sufficient documentation for a school to waive the initial grace period; the borrower must also acknowledge in writing that he or she wants the waiver. (Deferments are discussed in Section 4, "Forbearance and Deferments.")

***Differences between Perkins Loan and NDSL grace periods***

Repayment of a Perkins Loan begins **nine months** after the date that the borrower drops below half-time enrollment. Repayment of a National Direct Student Loan (NDSL) made before October 1, 1980, begins **nine months** after the date that the borrower drops below half-time enrollment. Repayment of an NDSL made on or after October 1, 1980 begins **six months** after the date that the borrower drops below at least half-time enrollment.

For a student attending at least half time, the initial grace period does not end until he or she ceases to be enrolled at least half time for a **continuous** period of six or nine months, whichever is applicable. A borrower who returns to school on at least a half-time basis prior to completion of the initial grace period is entitled to a full initial grace period, calculated as six or nine consecutive months, from the date that he or she drops below half-

time enrollment again. Suppose, for example, that a borrower takes out a loan in the fall quarter, drops out of school for the winter quarter, and resumes at least half-time study for the spring quarter. The borrower would still be entitled to a full initial grace period once he or she again leaves school or drops below half-time status.

***Post-deferment grace period***

A "post-deferment grace period" is the period of six consecutive months that immediately follows the end of a period of deferment and precedes the date on which the borrower must resume repayment on the loan. A Perkins Loan or NDSL made on or after July 1, 1993 has a six-month post-deferment grace period after each of the authorized deferments, **including** the economic hardship deferment. A Perkins Loan or all NDSL made on or after October 1, 1980 but before July 1, 1993, has a six-month post-deferment grace period after each of the deferments that apply to those loans **except** the hardship deferment. Neither the deferment nor the grace period is counted as part of the 10-year repayment period.

It is important to note that grace periods are always day-specific; that is, an initial grace period begins on the day immediately following the day the borrower drops below half-time enrollment. Likewise, a post-deferment grace period begins on the day immediately following the day on which an authorized period of deferment ends.

**GRACE PERIODS**
(Borrowers Attending at Least Half Time)

| Type of Grace Period | Federal Perkins Loans | NDSLs made on or after 10/1/80 | NDSLs made before 10/1/80 |
|---|---|---|---|
| **Initial** | 9 months | 6 months | 9 months |
| **Post-Deferment** | 6 months | 6 months | None |

***Differing grace periods for a borrower***

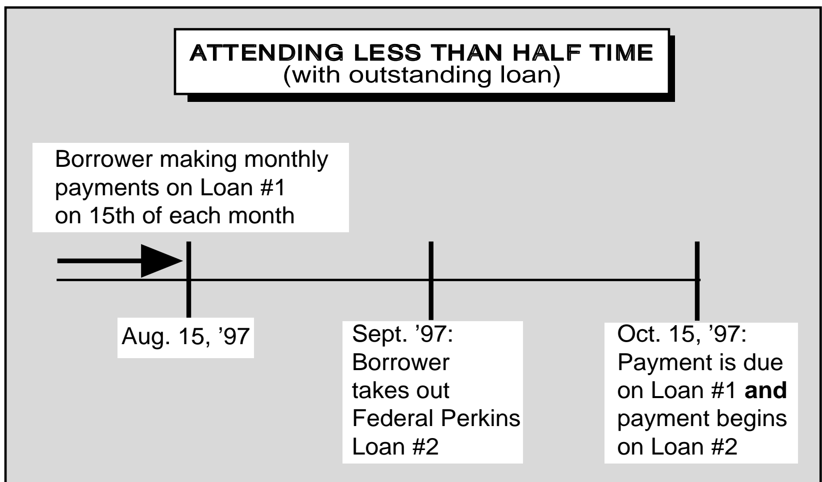
If a borrower has received loans with different grace periods (and different deferment provisions), the borrower must repay each loan according to the terms of its promissory note; the borrower must pay the minimum monthly payment amount that applies to each loan that is not in a grace or deferment period.

## *GRACE PERIOD FOR BORROWER ATTENDING LESS THAN HALF TIME*

***Borrower with outstanding loan(s)—34CFR 674.32***

A borrower who is attending **less than half time** and who has an outstanding Perkins Loan or NDSL must begin repayment on an **additional** loan when the **next scheduled installment** of the outstanding loan is due; there is no formal grace period or in-school deferment on the new loan.

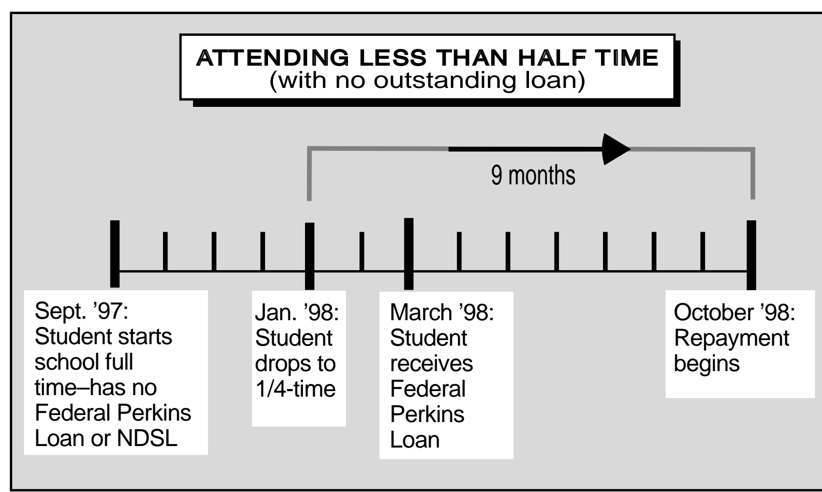
Suppose the borrower has been making monthly payments on Perkins Loan #1. He takes out Perkins Loan #2 in September 1997. His next payment on Loan #1 is due October 15. Therefore, he will begin repaying Loan #2 at the same time. **Remember that the repayment status of the outstanding loan determines the repayment status of the second loan**.




***Borrower with no outstanding loan(s)— 34CFR 674.32***

A borrower who is attending less than half time and who has no outstanding Perkins Loan or NDSL must begin repaying a new loan nine months from the date the loan is made **or** nine months from the date the borrower ceases to be enrolled as a regular student on at least a half-time basis,[1] **whichever is earlier**.

For example, a student starts school full time in September 1997. She does not have an outstanding Perkins Loan or NDSL. In January 1998, she drops to one-quarter time. In March, she receives a Perkins Loan. Nine months after the date the loan was made is December. Nine months after the time she dropped below half-time enrollment is October, and this nine-month period includes the date the loan was made. Because October is earlier than December, she must begin repayment in October.




[1] This nine-month period includes the date the loan was made.

## PREPAYMENT

***Payments received during the academic year the loan was made***

The borrower may prepay all or part of the loan at any time without penalty. Amounts repaid **during the academic year the loan was made** and **before the initial grace period has ended** are not considered prepayments, but **must be used to reduce the original loan amount.**

For example, suppose that a borrower receives a $1,000 Perkins Loan and that his grandmother gives him $400 during the academic year in which the loan is made. He receives the $400 before the initial grace period ends. The borrower applies the money to his Perkins Loan. The principal advanced to the borrower becomes $600. This is not considered a prepayment because the original loan amount has been reduced.

***Prepaying after the initial grace period***

If the borrower repays **more than the amount due** for any repayment period after the initial grace period has ended, the school must use the excess to prepay principal, unless the borrower designates the excess as an advance payment on the next regular installment. If the borrower designates the excess as an advance payment on the next installment and that advance payment exceeds the amount of the next regularly scheduled installment, the school must use the excess to prepay principal.

## REPAYMENT PLAN

Before the student ceases to be enrolled at least half time, the school must establish a repayment plan. The following provisions apply to the plan:

***34CFR 674.33***

◊ If the last scheduled payment is $25 or less, the school may combine it with the next-to-last payment.

◊ If the installment for all loans a school made to a borrower is not a multiple of $5, the school may round that payment to the next highest dollar amount that is a multiple of $5.

◊ Any payment a school receives must be applied in the following order:

1. collection costs,
2. late charges (or penalty charges),
3. accrued interest, and
4. principal.

If a student receives loans from more than one school, the repayment of each loan is made to (or default is attributed to) the school where the student received the loan.

***Loans at more than one school***

## *EXIT INTERVIEW AND REPAYMENT SCHEDULE*

At the time a borrower leaves school, the school must conduct an exit interview, during which a repayment schedule is provided to the borrower. (See Section 6 of this chapter for more information.) The U.S.Department of Education recommends a repayment schedule that shows the principal and interest due on each installment and the amount left to be paid. This type of schedule is not a requirement; however, a repayment schedule should contain at least

***34CFR 674.42***

***Repayment schedule provisions***

◊ the number of payments of principal or the number of equal payments,

◊ the rate of interest,

◊ the date the first payment is due, and

◊ the frequency of payments.

## *DEVELOPING A REPAYMENT SCHEDULE*

Interest on a loan must be computed at the rate of 5% per annum simple interest on the unpaid principal balance. Interest accrues on a Perkins Loan; it is not capitalized. Generally, interest is computed from the date a payment is received rather than from the due date. However, there are exceptions. For example, if a grace period expires in the middle of a month, interest may be computed to the beginning of the next month. Also, if a past-due payment is received before the next regularly scheduled payment, the interest may be computed according to the established payment schedule—no adjustments are necessary. Past-due payments should be applied in the same order as other payments, except that past-due payments must be applied to the “oldest” past-due dollars first.

To calculate the amount due in each payment over a period of 10 years, including principal and interest, a school may use the following table of constant multipliers. The table is based on the assumption that the school will not exercise a minimum monthly payment option. Using this table will ensure that each of the borrower’s payments sufficiently covers the interest accruing between payments and that the loan will be repaid within the specified amount of time.

***10-year repayment table***

| Annual Rate | Payment Frequency | Payments per Year | Total Payments | Constant Multiplier |
|---|---|---|---|---|
| 5% | Monthly | 12 | 120 | .0106065 |
| 5% | Bimonthly | 6 | 60 | .0212470 |
| 5% | Quarterly | 4 | 40 | .0319214 |

## *MINIMUM MONTHLY REPAYMENT AMOUNTS*

A school may require a borrower to pay a minimum monthly payment amount on an NDSL or on a Perkins Loan[2] if

◊ the promissory note includes a provision specifying a required amount for the minimum payment and the monthly repayment of principal and interest for a 10-year repayment period is less than the minimum monthly payment or

◊ the borrower has received loans with different interest rates at the same school and the total monthly payment would otherwise be less that the minimum monthly payment.

If the promissory note includes the optional minimum monthly payment provisions, the school may require the borrower to repay a monthly amount of at least $40—or $30 in the case of certain loans.

A school may require a borrower to pay at least $40 per month (or the equivalent in bimonthly or quarterly payments) if

◊ the monthly payment amount over a 10-year repayment period is less than $40[3] for a loan made on or after October 1, 1992 to a borrower who, at the time the loan was made, had no outstanding loan balance on a Perkins Loan, NDSL, or National Defense Student Loan (Defense Loan) **and**

◊ the promissory note includes an optional $40 minimum monthly payment provision.

A school may require a borrower to pay at least **$30** per month (or the equivalent in bimonthly or quarterly payments) if

◊ the monthly payment amount over a 10-year repayment period is less than **$30;**[3]

---

[2] The minimum monthly payment amount for a Defense Loan was $15.

[3] A student's monthly payment amount may need to be higher than $40 (or $30), of course, so that his or her debt is repaid by the end of 10years.

◊ the loan is

- a Perkins Loan or NDSL made before October 1, 1992 or
- a Perkins Loan or NDSL made on or after October1, 1992 to a borrower who, at the time the loan was made, had an outstanding loan balance on a Perkins Loan, NDSL, or Defense Loan; **and**

◊ the promissory note includes an optional $30 minimum monthly payment provision.

***Proportional repayment under minimum $40 (or $30) option***

The regulations require a school to divide the $40 (or $30) minimum monthly payment among the loans in the same proportion that the original loan principal of each loan bears to the total original principal of all loans. Thus, if the total monthly payment amount for more than one loan would otherwise be **less than the applicable minimum monthly payment amount** and if a school exercises the minimum monthly payment option, the 10-year table of constant multipliers cannot be used.

For example, suppose that a borrower with Perkins Loans of $1,500 and $1,000 (for a total debt of $2,500) has a promissory note that includes the minimum monthly payment provision. Using the constant multiplier table, the total monthly payment on the two loans would be less than $40:

$1,500 X .0106065 = $15.91 per month on loan #1

$1,000 X .0106065 = $10.61 per month on loan #2

$26.52 total payment per month

Because the monthly payment on the two loans is less than $40, the school may decide to exercise the minimum $40 payment option. If the school does so, the monthly payment for each loan is calculated by dividing the original principal of the loan by the total original principal of all loans:

$1,500 ÷ $2,500 = .600000 X $40 = $24 per month on loan #1

$1,000 ÷ $2,500 = .400000 X $40 = $16 per month on loan #2

$2,500 $40 total payment per month

If the borrower has received loans with different grace periods and deferments, the school must treat each note separately, and the borrower must pay the minimum monthly payment that is applicable to each loan that is not in a grace or deferment period.

***Minimum monthly payment amount and loans from more than one school***

A borrower may have received Perkins Loans or NDSLs from more than one school. If only **one** school exercises the $40 (or $30) option when the total monthly payment amount is less than $40 (or $30), that school receives the difference between $40 (or $30) and the repayment owed to the second school.

Suppose that School A, which does not exercise the minimum monthly payment option, receives $25 a month (the amount due under its established 10-year repayment plan). School B, which exercises the $40 option, would receive $15, the difference between $40 and the amount of principal and interest paid to School A.

If a borrower has obtained Perkins Loans or NDSLs from more than one school and **each** school exercises the minimum repayment option, the $40 or $30 minimum repayment is divided among the schools in proportion to the total amount of principal each has advanced.

If the total monthly repayment is **less than $40 (or $30)**, a school may exercise the minimum repayment options applicable to the respective loans. However, the maximum monthly repayment may not exceed $40 (or $30).

If the borrower owes funds to more than one school, he or she should contact any school that is exercising a minimum monthly payment option and should provide the following information:

- ◊ the names of all other schools to which the borrower owes funds under the Perkins Loan Program;
- ◊ the approximate amount of the indebtedness to each school; and
- ◊ any information that would help identify the loans—for example, the loan number and the dates of loan advances.

The school the borrower contacts should then contact the other schools and negotiate the amount each should receive from the borrower.

***Minimum monthly payment amount and different interest rates from the same school***

If a borrower has loans with different interest rates from the same school and if the borrower's total monthly repayment is **at least** $40 (or $30) for all loans, the school may not exercise the minimum monthly payment on any loan. If the total monthly repayment is **less than** $40 (or $30), the school may exercise the $40 (or $30) option, as long as the minimum monthly repayment provision was included in the promissory note. If the school exercises this option, the school must divide each monthly payment among all loans proportionate to the amount of principal advanced under each loan.

A school may reduce a borrower's scheduled payments for up to one year at a time if the borrower is paying the $40 (or $30) minimum monthly payment amount and if the school determines that the borrower is unable to make the scheduled payments due to hardship, such as prolonged illness or unemployment.

***Minimum repayment amount and hardship***

## *ESTABLISHING REPAYMENT DATES*

Depending on the repayment schedule (monthly, bimonthly, or quarterly), the borrower's first payment is due one, two, or three months from the date the grace period expires. Repayment schedules must be adjusted (preferably on the first installment) so that the loan will be repaid within the normal 10-year period or as prescribed in the terms of the promissory note.

For convenience, a school may establish standard repayment dates for borrowers who are on quarterly repayment schedules. The first repayment date may be the first day of the calendar quarter after the grace period has expired. Four standard repayment dates would be used: January 1, April 1, July 1, and October 1. (See the chart below.)

***Standard dates for quarterly repayment***

**EXAMPLE OF FEDERAL PERKINS LOAN QUARTERLY BILLING**
**With Four Standard Repayment Dates**

| Borrower's Termination Date | Initial 9-Month Grace Period Ends | Installment Due |
|---|---|---|
| January 1 | September 30 | January 1 |
| February 1 | October 31 | January 1 |
| March 1 | November 30 | January 1 |
| April 1 | December 31 | April 1 |
| May 1 | January 31 | April 1 |
| June 1 | February 28 | April 1 |
| July 1 | March 31 | July 1 |
| August 1 | April 30 | July 1 |
| September 1 | May 31 | July 1 |
| October 1 | June 30 | October 1 |
| November 1 | July 31 | October 1 |
| December 1 | August 31 | October 1 |

Another type of repayment schedule is a "rolling" quarterly repayment schedule in which each borrower's first repayment is due exactly three months after the date his or her grace period expires. For example, if a borrower's first grace period expires on May 17, the first installment payment is due August 18. Another borrower's grace period expires May18, so the first installment payment on that loan is due August19.

***"Rolling" quarterly repayment schedule***

**Effect of deferment on repayment dates**

For collection and bookkeeping purposes, a fixed repayment date is preferred. Otherwise, if the borrower is entitled to a deferment, the school may have problems computing payments due. (See Section 4 of this chapter.) Once the payment date is established, the borrower will owe principal and interest for any portion of a scheduled installment period not covered by a deferment. However, if the borrower is in deferment on a due date, any amounts owed are carried over and paid on the first due date on which the borrower is out of deferment.

## INTEREST RATES

The interest rate charged on the unpaid balance of a Defense Loan, NDSL, or Perkins Loan depends on when the loan was made. The interest rate is stated in the borrower's promissory note. The annual interest rate for loans made

◊ before July 1, 1981 was 3%;

◊ between July 1, 1981 and September 30, 1981 was 4%;

◊ on or after October 1, 1981 is 5%.

**Computing interest**

Interest on loans made on or after October 1, 1981 is computed at the rate of 5% per annum simple interest on the unpaid principal balance. Interest should be computed from the date when the payment is received rather than from the due date; however, interest charges may be computed to the nearest first-of-the-month, or they may be computed in accordance with the borrower's established schedule of payments of principal and interest if the borrower is making payments on a regular basis according to that schedule.

## LENGTH OF REPAYMENT PERIOD

**Maximum repayment period and repayment plans**

The term "repayment period" generally refers to the span of time the borrower is given to repay his or her loan—usually a maximum of 10years from the time repayment begins. (For the exception, see the discussions of hardship and low-income individual that follow.) A borrower must repay his or her loan, plus interest, in quarterly, bimonthly, or monthly installments over a 10-year period. The length of a repayment period may be less than 10 years because of minimum monthly payment requirements. Remember that a repayment period **never** includes authorized periods of deferment, forbearance, or cancellation.

If a borrower wants to repay the loan in graduated installments, he or she must request permission to do so from the school; if the school agrees to this type of repayment, a graduated repayment schedule is prepared and

submitted to the Department for approval. If the Department approves the school's request, the borrower may use the graduated method of repayment.

***Extension of repayment for hardship***

A school may **extend** a repayment period if the borrower is experiencing a period of prolonged illness or unemployment or if the borrower is a "low-income individual" (defined on the next page). Interest continues to accrue during an extension of a repayment period for any of these reasons.

***Extension of repayment for a low-income individual***

For NDSLs made on or after October 1, 1980 and for all Perkins Loans, a school may extend the borrower's repayment period up to 10 additional years if, during the repayment period, the school determines that the borrower qualifies as a low-income individual. The school must review the borrower's status annually to determine whether he or she still qualifies. Once a borrower no longer qualifies, his or her repayment schedule must be amended so that the number of months in it does not exceed the number of months remaining on the original repayment schedule (not counting the extension period).

***Other adjustments for low-income individuals***

There are two other ways that a school may adjust the repayment schedule for a borrower who qualifies as a low-income individual:

1. The school may require the borrower to pay a reduced amount for a limited time and then later increase the payment amount so that the borrower catches up on payments. For example, a school reduces the payment amount to $10 per month for six months and then increase it to $50 per month until the borrower catches up. The repayment period does not have to be extended.

2. The school may allow the borrower to pay $10 per month for a year and then resume normal payments. This type of adjustment extends the repayment period.

***Definition of "low-income individual"—34CFR 674.33(c)(2)***

The definition of low-income individual is based on the maximum income levels in the Income Protection Allowance (IPA) chart published annually in the *Federal Register*. The IPA chart for the 1997-98 award year was published May 31, 1996. See the maximum income levels for the 1997-98 award year in the chart that follows.

1. For an unmarried borrower without dependents, a low-income individual is one whose total income for the **preceding calendar year** did not exceed 45% of the IPA for the **current award year** for a family of four with one in college. For the 1997-98 award year, an unmarried borrower without dependents is a low-income individual if his or her 1996 income was $8,132 or less.

2. For a borrower with a spouse or legal dependents, a "low-income individual" is one whose total family income for the **preceding calendar year** did not exceed 125% of the IPA for the **current award year** for a family equal in size to that of the borrower's family with one family member in college.

| **Low-Income Individual**<br>**Maximum 1995 Income Levels for 1996-97 Award Year**<br>(derived from Income Protection Allowances published in the May 31, 1995 *Federal Register* and updated in the July 19, 1995 *Federal Register*) | | | | | | |
|---|---|---|---|---|---|---|
| Number of Family Members (including student) | 1 | 2 | 3 | 4 | 5 | 6 |
| Maximum 1994 Income Level | $7,943 | $14,350 | $17,863 | $22,063 | $26,038 | $30,450 |
| NOTE: For families of more than 6, add $3,438 for each additional family member. | | | | | | |

## *DISPOSITION OF PROMISSORY NOTE AND REPAYMENT SCHEDULE*

The school must keep the original signed promissory note and repayment schedule in a locked, fireproof container until the loan is repaid in full or until the original note and schedule are needed in order to enforce loan collection. Only authorized personnel may have access to these records.

Promissory notes for loans made prior to December 1, 1987 include a requirement to attach the repayment schedule to the promissory note. If a promissory note has this requirement in the "Repayment" section of the note, the lending school must be careful to attach the repayment schedule to that note. Promissory notes for loans made after December1, 1987 do not include such a requirement.

If the original promissory note is released for the purpose of enforcing repayment, the school must keep a certified true copy. To qualify as a certified true copy, a photocopy (front and back) of the original promissory note must bear the following certification statement signed by the appropriate school official:

> "CERTIFIED TRUE COPY: I declare under penalty of perjury that the foregoing is a true and correct copy of the original Promissory Note.
>
> Signature: ________________________________________
>
> Title: ____________________________________________
>
> Date: ____________________________________________"

At the exit interview, the school must provide a copy of the signed promissory note and the signed repayment schedule to the borrower. If the school is unable to obtain a **signed** repayment schedule, the school must provide the borrower with the schedule he or she will follow in repaying the loan.

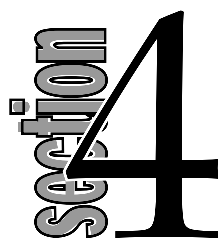
***Error in promissory note***

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.

***Loan that is paid in full***

When a loan has been repaid, the school should mark the note with the phrase "PAID IN FULL" and with the date the loan was paid in full, have the note certified by a school official, and give or mail 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 is paid in full.

Because a borrower must reaffirm a Perkins Loan that has been written off before he or she is eligible to apply for future federal student aid, the Department recommends that the school maintain a certified copy of the signed promissory note as well as a record of the full amount owed in its records beyond the three-year record retention requirement.



# Forbearance & Deferment

## FORBEARANCE

*Definition of forbearance*

If a borrower is willing but financially unable to make the required payments on a loan, he or she may request that the school grant forbearance. Forbearance is a temporary postponement of payments, an extension of time allowed for making payments, or the acceptance of smaller payments than were previously scheduled. Interest will continue to accrue during any period of forbearance. The borrower must request forbearance in writing, providing documentation that supports the borrower's claim that he or she is financially unable to make payments. Forbearance is available for all Perkins Loans and National Direct Student Loans (NDSLs), regardless of when they were made.

*Forbearance— 34CFR 674.33(d)*

When the school receives the borrower's written request and supporting documentation, the school must grant the borrower forbearance for a period of up to one year at a time. The forbearance may be renewed, but the periods of forbearance collectively may not exceed a total of three years. A school may apply an authorized period of forbearance to begin retroactively (that is, to begin on an earlier date than the date of the borrower's request) if the borrower requests that the school do so and if he or she provides adequate documentation to support the request.

Both loan principal and any interest that accrues must be included in the forbearance unless the borrower chooses to pay interest that accrues. The borrower and the school must agree in writing on the terms of forbearance. The forbearance must be in the form of a temporary cessation of payments unless the borrower chooses one of the alternative types of forbearance (as explained in the first paragraph above).

*Criteria for granting forbearance*

A school must grant forbearance if the total amount the borrower is obligated to pay monthly on all Student Financial Assistance (SFA) loans is equal to or greater than 20% of the borrower's total monthly gross income (defined on the next page). If the borrower's loan payments are due less frequently than monthly, a proportional share of the payments is

***Evidence the borrower must submit***

used to determine the equivalent in total monthly payments. For example, if a payment is due quarterly, divide the amount by three (because the payment covers three months) to determine the equivalent monthly payment amount. The school must require the borrower to submit at least the following documentation:

- ◊ evidence of the amount of the most recent total monthly gross income the borrower received and
- ◊ evidence of the amount of the monthly payments the borrower owes for the most recent month on his or her SFA loans.

***Definition of "total monthly gross income"***

Total monthly gross income is the gross amount of income received by the borrower from employment (either full time or part time) and from other sources.

***Other reasons for granting forbearance***

A school also must grant forbearance if it determines the borrower should qualify due to poor health or other acceptable reasons or if the U.S. Department of Education authorizes a period of forbearance due to a national military mobilization or other national emergency. The Department strongly encourages a school to grant forbearance to a borrower who is serving in Americorps.

## *DEFERMENT*

***Definition of deferment***

A borrower is entitled to have the repayment of a loan deferred under certain circumstances. A deferment is a period of time during which the borrower is not required to repay the loan principal. Interest will not accrue during any type of deferment except a hardship deferment. For loans made on or after July1, 1993, **interest does not accrue** during any type of deferment.

***Deferment and cancellation***

If a borrower is teaching or engaged in other services that qualify him or her for both deferment and cancellation, the loan deferment is considered to run concurrently with any period for which loan cancellation is granted.

***Applying for a deferment***

A borrower must apply for a deferment in writing by using a deferment form obtained from the business or student loan office of the school that made the loan (or from the school's billing service, if it uses one). The form must be submitted to the school along with whatever documentation the school requires. The school establishes a deadline for submitting the form and documentation. (The Department does **not** approve or supply deferment forms.) The borrower must file a form at least once a year for as long as the deferment can be claimed. The borrower must immediately report any change in deferment status to the lending institution.

## IN-SCHOOL DEFERMENT—COMMON TO ALL PROGRAM LOANS

***Required enrollment status***

A borrower may defer repayment of a Perkins Loan, NDSL, or National Defense Student Loan (Defense Loan) if he or she is enrolled at least half time in an eligible institution. Interest will not accrue during the deferment. To receive a deferment based on at least half-time enrollment, also called an in-school deferment, the student must be enrolled as a regular student in an eligible institution of higher education or a comparable institution outside the United States approved by the Department for deferment purposes. However, it is not a requirement that the school participate in the Federal Perkins Loan Program. If a borrower is attending a school that ceases to qualify as an institution of higher education, the borrower's deferment ends on the date the school ceases to qualify.

A regular student is one who is enrolled for the purpose of obtaining a degree or certificate. If the borrower is attending at least half time as a regular student for a full academic year and intends to do so in the next academic year, he or she is entitled to a deferment for 12 months.

## DEFERMENT OF LOANS MADE ON OR AFTER JULY 1, 1993

For Perkins Loans and NDSLs made on or after July 1, 1993, a borrower may defer loan repayment, and interest does not accrue while he or she

***In-school deferment***

◊ is enrolled at least half time as a regular student at an eligible institution and is attending classes at that school as described above;[1]

◊ is enrolled and in attendance as a regular student in a course of study that is part of a graduate fellowship program approved by the Department;[2]

◊ is engaged in graduate or post-graduate fellowship-supported study (such as a Fulbright grant) outside the United States;

***Rehabilitation training***

◊ is enrolled in a course of study that is part of an Department-approved rehabilitation training program for disabled individuals;

***Unemployment***

◊ is seeking and is unable to find full-time employment;[3]

---

[1] In-school deferments may no longer be granted to a borrower while serving in a medical internship or residency program, except for a program in dentistry.

[2] The borrower must provide certification that he or she has been accepted for or is engaged in full-time study in the school's graduate fellowship program.

[3] These deferments may not be granted in excess of three years.

***Economic hardship***

◊ is suffering an economic hardship[3] (discussed below); or

◊ is engaged in certain types of service that qualify the borrower for cancellation of the loan.[4]

***Post-deferment grace period***

A Perkins Loan or NDSL borrower is entitled to a 6-month grace period after each type of deferment (a "post-deferment" grace period). Neither the deferment nor the grace period is counted as part of the borrower's 10-year repayment period.

***Economic hardship deferment 34CFR Section 674.34(e)***

For Perkins Loans or NDSLs made **on or after** July 1, 1993, the hardship deferment has been replaced by the **economic hardship** deferment. A school may grant a deferment due to economic hardship for up to a total of three years. Unlike loans made before July1, 1993, loans made after that date do not qualify for **unlimited** deferments due to hardship. Also unlike the former hardship deferment, the new economic hardship deferment allows a borrower to defer interest as well as principal.

An eligible borrower is entitled to an economic hardship deferment for periods of up to one year at a time, not to exceed three years cumulatively if the borrower provides the school with satisfactory documentation showing that he or she

1. has been granted an economic hardship deferment under either the William D. Ford Federal Direct Student Loan (Direct Loan) Program or the Federal Family Education Loan (FFEL) Program for the same period of time for which the Perkins Loan or NDSL deferment has been requested;

2. is receiving federal or state public assistance, such as Aid to Families with Dependent Children, Supplemental Security Income, Food Stamps, or state general public assistance;

3. is working full time and is earning a total monthly gross income that does not exceed the greater of

    a) the monthly earnings of an individual earning the federal minimum wage or

    b) an amount equal to 100% of the poverty line for a family of two as determined in accordance with section 673(2) of the Community Service Block Grant Act;

---

[4] See Section 5, "Cancellation."

4. is not receiving total monthly gross income that is more than twice the amount in (a) or (b) above and that income minus an amount equal to the borrower's monthly payments on federal postsecondary education loans does not exceed the amount specified in (a) or (b) above; or

5. is working full time and has a federal educational debt burden that equals or exceeds 20% of the borrower's total monthly gross income and the borrower's total monthly gross income minus such burden is less than 220% of the greater of

   a) the monthly earnings of an individual earning the federal minimum wage or

   b) an amount equal to 100% of the poverty line for a family of two as determined in accordance with section 673(2) of the Community Service Block Grant Act.

For information on the minimum wage, contact the Wage and Hour Division of the U.S. Department of Labor. The telephone number is (202)219-7043.

The U.S.Department of Health and Human Services 1997 poverty line for a family of two is $13,270 for Alaska, $12,200 for Hawaii, and $10,610 for all other states.

***Documentation for economic hardship***

To support a borrower's eligibility for an initial economic hardship deferment based on the criteria in option 4 above, the school must collect at least the following documentation:

◊ evidence showing the amount of the borrower's most recent total monthly gross income from all sources—that is, the gross amount of income the borrower received from employment (either full-time or part-time) and from other sources and

◊ evidence showing the most recent monthly amount due on each of the borrower's federal postsecondary education loans, as determined by the method described below.

***Determining monthly amount due on education loans***

To determine the monthly amount due on federal postsecondary education loans, the school must count only the monthly amount that the borrower **would have owed** on each loan **if it had been scheduled to be repaid in 10 years** from the date the loan entered repayment; the school should disregard the actual repayment schedule or the actual monthly payment amount (if any) that the borrower would owe during the period for which the economic hardship deferment is requested.

To qualify for a **subsequent** period of deferment that begins less than one year after the end of the deferment described in option 3 or 4 above, the school must require the borrower to submit a copy of his or her federal income tax return if the borrower filed a tax return within the eight months preceding the date the deferment is requested.

For purposes of qualifying under option 3 or 5 of the economic hardship deferment, a borrower is considered to be working full time if he or she is expected to be employed for at least three consecutive months for at least 30 hours per week.

***Rehabilitation training program deferment***

To qualify for a deferment for study in a rehabilitation training program, all of the following criteria must be met:

1. The borrower must provide the school with a certification from the rehabilitation agency that the borrower is either receiving or scheduled to receive training services designed to rehabilitate disabled individuals.

2. The borrower must provide the school with a certification from the rehabilitation agency that one of the following entities licenses, approves, certifies, or otherwise recognizes the rehabilitation program as providing rehabilitation training to disabled individuals:

    - a state agency with responsibility for vocational rehabilitation programs;

    - a state agency with responsibility for drug abuse treatment programs;

    - a state agency with responsibility for mental health services programs;

    - a state agency with responsibility for alcohol abuse treatment programs; or

    - the U.S. Department of Veterans Affairs.

3. The rehabilitation agency must certify that the rehabilitation program provides or will provide the borrower with rehabilitation services under a written plan that

    - is individualized to meet the borrower's needs;

    - specifies the date on which the services to the borrower are expected to end; and

- is structured in a way that requires the borrower's substantial commitment to his or her rehabilitation. The Department considers a substantial commitment to be one of time and effort that would normally prevent an individual from engaging in full-time employment either because of the number of hours that must be devoted to rehabilitation or because of the nature of the rehabilitation.

## *DEFERMENT OF PERKINS LOANS MADE BEFORE JULY 1, 1993*

A borrower of a Perkins Loan made before July 1, 1993 may defer repayment if he or she is enrolled at least half time as a regular student in an eligible institution (as explained on page 6-39).

***Three-year deferments***

Such a borrower may also defer repayment for up to three years and interest will not accrue while he or she is

◊ a member of the U.S. Army, Navy, Air Force, Marines, or Coast Guard;

◊ a member of the National Guard or the Reserves serving a period of full-time active duty in the armed forces;

◊ an officer in the Commissioned Corps of the U.S. Public Health Service;

◊ on full-time active duty as a member of the National Oceanic and Atmospheric Administration Corps;

◊ a Peace Corps volunteer;

◊ a volunteer under Title I, Part A of the Domestic Volunteer Service Act of 1973 (ACTION programs);

◊ a full-time volunteer in service for a tax-exempt organization that the Department has determined is comparable to Peace Corps or ACTION service;[5] or

◊ temporarily totally disabled or unable to work because he or she must care for a **spouse or other dependent** who is so disabled.[5]

---

[5] See the criteria on the next page.

**Volunteer service comparable to Peace Corps**

A borrower is considered to be providing service comparable to Peace Corps or ACTION service if he or she meets all of the following five criteria:

1. The borrower serves in an organization that is exempt from taxation under the provisions of Section 501(c)(3) of the Internal Revenue Code of 1954.

2. The borrower provides service to low-income persons and their communities to assist them in eliminating poverty and poverty-related human, social, and environmental conditions.

3. The borrower does not receive compensation that exceeds the rate prescribed under Section 6 of the Fair Labor Standards Act of 1938 (the federal minimum wage), except that the tax-exempt organization may provide the volunteer with health, retirement, and other fringe benefits that are substantially equivalent to the benefits offered to other employees of the organization.

4. The borrower, as part of his or her duties, does not give religious instruction, conduct worship service, engage in religious proselytizing, or engage in fund raising to support religious activities.

5. The borrower has agreed to serve on a full-time basis for a term of at least one year.

**Temporary total disability**

Temporarily totally disabled, with regard to the borrower, means the inability due to an injury or illness to attend an eligible school or to be gainfully employed during a reasonable period of recovery.

Temporarily totally disabled, with regard to a disabled spouse or other dependent of a borrower, means requiring continuous nursing or other services from the borrower for a period of at least three months due to illness or injury.

An affidavit from a qualified physician[6] is required to prove disability. The definition of dependent for temporary total disability deferment purposes is the same as the definition used in the *Free Application for Federal Student Aid* (FAFSA) for a member of the independent applicant's household: A borrower's dependent is a child who receives more than half of his or her financial support from the borrower or another person who lives with the borrower and who receives more than half of his or her financial support from the borrower.

---

[6] A qualified physician is a doctor of medicine or osteopathy who is legally authorized to practice medicine.

**Internship deferment**

A borrower whose Perkins Loan was made before July 1, 1993 and who is serving in a medical internship or residency program is not considered to be in school for deferment purposes and may not receive an in-school deferment on that Perkins Loan for the internship or residency program; however, the borrower is eligible for an **internship deferment** for up to two years.

While the borrower is serving an eligible internship, he or she may defer repayment for up to two years. Interest will not accrue during the internship deferment. An eligible internship is one that requires the borrower to hold at least a bachelor's degree before beginning the program; in addition, the internship must meet the criteria of *either* a *or* b below to be eligible:

a. The successful completion of the internship must be required by a state licensing agency as a prerequisite for certification of the individual for professional practice or service. For this type of eligible internship, the borrower must provide the school with the following certifications:

   - a statement from an official of the appropriate state licensing agency indicating that the successful completion of the internship is required by the state licensing agency as a prerequisite for certification for professional practice or service;

   - a statement from the organization where the borrower will be an intern certifying that attaining a bachelor's degree is required to be admitted in the program;

   - a statement from the organization where the borrower will be an intern indicating that the borrower has been accepted into its internship program; and

   - certification of the dates when the borrower is expected to begin and complete the program.

b. The internship or residency program must lead to a degree or certificate awarded by an institution of higher education, a hospital, or a health care facility offering postgraduate training. For this type of eligible internship, the borrower must provide the school with a statement from an authorized official of the internship program certifying that

   - a individual must have a bachelor's degree to be admitted in the program;

- the borrower has been accepted into the program; and

- the internship or residency program leads to a degree or certificate awarded by an institution of higher education, a hospital, or a health care facility that offers postgraduate training.

A borrower of a Perkins Loan made before July 1, 1993 may also defer repayment (and interest will not accrue) during a period of

***One-year "working mother" deferment***

◊ up to one year if the borrower is a mother of a preschool-age child, provided the mother is going to work (or going back to work) at a salary that is no more than $1.00 above the minimum hourly wage or

***Six-month "parental leave" deferment***

◊ up to 6 months if the borrower is pregnant, or if he or she is taking care of a newborn or newly adopted child.[7]

***Hardship deferment***

A borrower may defer repayment for hardship, as determined by the school (for example, if the borrower is facing a prolonged period of illness or unemployment). Interest will continue to accrue during the deferment.

***Post-deferment grace period***

A borrower is entitled to a 6-month grace period after each of the deferments that apply to Perkins Loans (a post-deferment grace period) except after a hardship deferment. Neither the deferment nor the post-deferment grace period is counted as part of the 10-year repayment period.

## *DEFERMENT OF NDSLS MADE BETWEEN OCTOBER 1, 1980 AND JULY 1, 1993*

***At least half-time attendance***

A borrower of an NDSL made on or after October1, 1980 but before July1, 1993 may defer repayment if he or she is enrolled at least half time as a regular student in an eligible institution (as explained on page 6-39).

***Three-year deferments***

A borrower may defer repayment for up to three years (and interest will not accrue) while the borrower is

◊ a member of the U.S. Army, Navy, Air Force, Marines, or Coast Guard;

◊ a member of the National Guard or the Reserves serving a period of full-time active duty in the armed forces;

---

[7] This deferment is called a parental leave deferment. The borrower must be unemployed and not attending school and must apply for deferment within six months of leaving school or dropping below half-time status.

◊ an officer in the Commissioned Corps of the U.S. Public Health Service;

◊ a Peace Corps volunteer;

◊ a volunteer under TitleI, PartA of the Domestic Volunteer Service Act of 1973 (ACTION programs);

◊ a full-time volunteer in service for a tax-exempt organization the Department has determined to be comparable to Peace Corps or ACTION;[8] or

◊ temporarily totally disabled or unable to work because he or she must care for a **spouse** who is so disabled.[9]

***Two-year deferments***

A borrower of an NDSL made on or after October1, 1980 and before July1, 1993 may defer repayment for up to two years (and interest will not accrue) while the borrower is serving in an eligible internship. An eligible internship is one

◊ that requires the borrower to hold at least a bachelor's degree before beginning the internship program and

◊ that the state licensing agency requires the borrower to complete as a prerequisite for his or her certification for professional practice or service.

To qualify for an internship deferment, the borrower must provide the school with the following certifications:

◊ a statement from an official of the appropriate state licensing agency indicating that the successful completion of the internship is required by the state licensing agency as a prerequisite of certifying for professional practice or service;

◊ a statement from the organization where the borrower will be an intern certifying that attaining a bachelor's degree is required to be admitted in the program;

◊ a statement from the organization where the borrower will be an intern indicating that the borrower has been accepted into its internship program; and

◊ certification of the dates when the borrower is expected to begin and complete the program.

---

[8] See the volunteer service criteria on page 6-44.

[9] See the discussion of temporary total disability on page 6-44. A physician's statement is required.

A borrower may defer repayment for hardship, as determined by the school (for example, if the borrower is facing a prolonged period of illness or unemployment). Interest will continue to accrue during the deferment.

***Deferment provisions for loans made before 10/1/80***

For all NDSLs made on or after October 1, 1980 and before July 1, 1993, a borrower is also entitled to a 6-month post-deferment grace period after each of the deferments that apply to those loans except after a hardship deferment. Neither the deferment nor the post-deferment grace period is counted as part of the 10-year repayment period. For information on deferment provisions for loans made before October1, 1980, see the *1994-95 Federal Student Financial Aid Handbook* or 34CFR 674.37.

## *DEFERMENT VS. POSTPONEMENT FOR SERVICE THAT WILL QUALIFY FOR LOAN CANCELLATION*

For Perkins Loans and NDSLs made on or after July1, 1993, deferment of repayment is applicable during periods while the borrower is performing a service that will subsequently qualify him or her for cancellation of all or a portion of the loan. A school may grant a deferment of repayment for up to 12months at a time. Interest does not accrue during this period of deferment. A borrower is entitled to deferment and post-deferment grace periods; therefore, regardless of the length of time that the eligible service is performed, repayment is deferred during that period of service and does not resume until six months after the cessation of service.

Because a borrower of a loan made on or after July1, 1993 is entitled to a deferment while performing a service that will subsequently qualify him or her for cancellation of all or a portion of the loan, a school that is exercising the minimum monthly payment provision listed in the promissory note must cease doing so and grant a deferment to cover any period of qualifying service. The amount to be deferred and subsequently canceled must be calculated using the 10-year repayment period.

A borrower of a Perkins Loan, NDSL, or Defense Loan made before July1, 1993 may **not** receive a deferment during a period while he or she is performing a service that will subsequently qualify him or her for cancellation of all or a portion of the loan; rather, a school must grant **postponement** of loan repayment for a 12-month period if the borrower

- ◊ notifies the school in writing that he or she is performing a qualifying service and
- ◊ submits a statement specifying that he or she is so employed.[10]

---

[10] The statement must be signed by a responsible official in the military, agency, or school employing the borrower, and the statement must describe the borrower's job, list the period of employment, and state whether the job is full- or part-time.

Postponement differs from deferment in the following ways:

- ◊ the borrower is not entitled to a postponement;
- ◊ the borrower does not receive a grace period following postponement; and
- ◊ interest continues to accrue during postponement.

Because postponement is not an entitlement, a borrower who does not complete the period required to receive cancellation will be required to make any payments that had been postponed during the partial period of service. These payments become due and payable immediately upon the cessation of service.

A school that is exercising the minimum monthly payment provisions listed in a borrower's promissory note can still grant postponement to cover a period of qualifying service. If the school was originally exercising the minimum payment option, it must cease doing so if it grants postponement. The amount to be postponed and subsequently canceled must be calculated using the 10-year repayment period.

If a borrower has received more than one type of loan but is performing a service that qualifies only one loan for cancellation, the school may defer loan payments (or postpone loan payments for loans made prior to July 1, 1993) **only** on the loan that qualifies for the cancellation. The amount due on the loan that is not eligible for cancellation is the amount the borrower would normally pay.

## *THE CONCURRENT DEFERMENT PERIOD*

If a borrower is teaching or engaged in other services that qualify him or her for both deferment and cancellation, the loan deferment is considered to run concurrently with any period for which loan cancellation is granted.

## *DEFERMENT AND DEFAULT*

A borrower is not entitled to a deferment on a defaulted loan. If the borrower signs a new repayment agreement, however, a school may grant a deferment even if the school has accelerated[11] the loan. The school would have to de-accelerate the loan before granting the deferment. The policy to permit deferments on defaulted loans applies to all requests for deferment received after February 3, 1988, regardless of the date the loan was made.

---

[11] Acceleration is one of the penalties a school may impose on a defaulted loan. A loan that has been accelerated becomes due and payable immediately in one lump sum.

Before granting a deferment on a defaulted loan, the school may require the borrower to pay immediately late fees, collection costs, and some or all of the amount past due as of the date on which the school determined that the borrower had demonstrated eligibility for a deferment. The Department encourages schools to require the borrower to do so, thus "curing" the default.

The borrower must file for deferment on time and provide satisfactory documentation that he or she qualifies for the deferment. "On time" means by a deadline that the school establishes. **A school is not required to grant deferments on loans in default**; however, if a school does so, it is expected to calculate past-due accrued interest. If a school believes this is too burdensome, it may deny deferments on defaulted loans.

## DEFERMENT VS. IN-SCHOOL ENROLLMENT STATUS

A borrower may neglect to notify a school that he or she has enrolled at least half time at another school before the initial grace period expires. Because the school would not have this information, the school would assume that the student's repayment period had started and might demand payment from the borrower. In such a case, a borrower often requests a deferment rather than a continuation of his or her in-school status. Because the borrower reenrolled at least half time before the initial grace period expired, repayment had not yet started, and a deferment would not be appropriate.

The borrower may submit proof at any time—even after a loan has been accelerated—that he or she reenrolled at least half time before the initial grace period expired and that the repayment period should have begun later than the date originally calculated. **The school must recalculate that date if it receives this proof**. The school must also deduct from the loan balance any interest accrued and any late charges added before the date the repayment period actually should have begun.

Note that the borrower remains responsible for payments that would have been due under the recalculated repayment period and that the school is not obligated to grant a deferment for any payments past due under that period.

# Cancellation

A borrower may have all or part of his or her loan (including interest) canceled for engaging in public service such as teaching, service in the education component of a Head Start program, service in the Peace Corps or ACTION, or service in the military. Cancellation is also granted in case of the borrower's death, total and permanent disability, or—in some cases—bankruptcy. Definitions that apply to cancellation provisions are discussed on pages 6-63 through 6-65.

The promissory notes in "Dear Colleague" Letter CB-93-9, dated July 1993, incorporate changes in loan cancellation provisions required by The Higher Education Amendments of 1992 for Federal Perkins Loans and National Direct Student Loans (NDSLs) made on or after July 23, 1992. The U.S. Department of Education issued reformatted promissory notes in "Dear Colleague" Letter CB-96-8, dated May 1996.

***"Dear Colleague" Letters CB-93-9, July 1993 and CB-96-8, May 1996***

## U.S. ARMY LOAN REPAYMENT PROGRAM

It is useful to know that the U.S. Army offers a loan **repayment** program as an enlistment incentive. If the borrower of a Perkins Loan or NDSL (or Stafford Loan) serves as an enlisted person in the U.S. Army, in the Army Reserves, or in the Army National Guard, the U.S. Department of Defense will repay a portion of the loan. For more information, the student should contact his or her local military recruiting office. This is a recruitment program, not a cancellation, and does not pertain to an individual's prior service.

## COMMON CANCELLATION PROCEDURES

Although cancellation provisions vary, depending on whether the borrower has a Perkins Loan or NDSL, the following procedures apply to any loan:

◊ The borrower must apply for cancellation of his or her loan by obtaining the appropriate cancellation form from the business

or student loan office of the school that made the loan (or from the school's billing service if it uses one). The Department does not approve or supply cancellation forms. The form must be submitted to the school by the deadline the school establishes. The borrower must provide any documentation the school requests to show that he or she qualifies for cancellation. For information on documentation, see the appropriate cancellation category in this section.

◊ It is the school's responsibility to determine, based on the borrower's documentation, whether the borrower is entitled to have any portion of his or her loans canceled. This responsibility cannot be delegated.

◊ No portion of any loan may be canceled for services the borrower performed either before the date the loan was disbursed or during the enrollment period covered by the loan.

◊ Regardless of the repayment status of a loan, the school must cancel the loan upon receipt of proof of the borrower's death or upon the school's approval of a borrower's request for cancellation because of a permanent and total disability.

◊ Periods of loan deferment for public service that is also qualifying service for cancellation benefits are considered to run concurrently with any period for which a loan cancellation for such public service is granted.

◊ Defaulted loan amounts are not eligible for cancellation unless the only reason for the default was the borrower's failure to file a cancellation request on a timely basis. However, if the school has accelerated the account by the time the borrower files the necessary cancellation request forms, only eligible service performed **prior** to the date of acceleration can be considered for cancellation. A borrower is not entitled to cancellation for any eligible service performed **after** the date of acceleration.

◊ No repayment made by a borrower during a period for which the borrower qualified for a cancellation may be refunded unless the borrower made the payment because of the school's error. To reduce the chance of error, a school should keep the borrower informed of any new cancellation benefits.

◊ No borrower who has received an education benefit under Subtitle D of Title I of the National and Community Service Act of 1990 may receive a cancellation of a Perkins Loan or NDSL.

## *CANCELLATION PROVISIONS COMMON TO ALL LOANS MADE AFTER JULY 1, 1987*

The borrower of a Perkins Loan or NDSL made after July1, 1987 is eligible to have up to 100% of the loan canceled for qualifying service as

***Teaching in low-income schools***

◊ a full-time teacher in a public or nonprofit elementary or secondary school serving students from **low-income**[1] families or

***Teaching handicapped children***

◊ a full-time teacher of **handicapped students** in a public or nonprofit elementary or secondary school. The majority of the students the borrower teaches must be handicapped children.[2]

***Cancellation rates***

The cancellation rate per completed academic year of teaching is

◊ 15% of the original principal loan amount—plus the interest that accrued during the year—for each of the first and second years;

◊ 20% of the original principal loan amount—plus the interest that accrued during the year—for each of the third and fourth years; and

◊ 30% of the original principal loan amount—plus any interest that accrued during the year—for the fifth year.

***Service in Head Start***

A Perkins Loan or NDSL borrower who received the loan on or after July1, 1987 is entitled to cancellation of up to 100% of the loan for qualifying service as a full-time staff member in the educational part of a preschool program carried out under the Head Start Act. The cancellation rate is 15% of the original principal loan amount—plus the interest that accrued during the year—for each complete school year.

## *LAW ENFORCEMENT CANCELLATION PROVISION—SPECIFIC TO LOANS MADE ON OR AFTER NOVEMBER 29, 1990*

A borrower is entitled to cancellation of up to 100% of a Perkins Loan or NDSL made on or after November 29, 1990 for full-time service as a

[1] See the definition of this term at the end of this section. An official Directory of designated low-income schools is published annually by the Department.

[2] For loans made on or after July 23, 1992, this provision has been replaced by the “special education teacher” cancellation provision. A teacher of handicapped students/special education teacher is not required to teach in a low-income school to be eligible for cancellation.

qualifying law enforcement or corrections officer. The rates of cancellation for each completed year of service are the same as those for teachers:

- ◊ 15% of the original principal—plus any interest that may have accrued during the year—for each of the first and second years;
- ◊ 20% of the original principal—plus any interest that may have accrued during the year—for each of the third and fourth years; and
- ◊ 30% of the original principal—plus any interest that may have accrued during the year—for the fifth year.

### *CANCELLATION PROVISIONS SPECIFIC TO FEDERAL PERKINS LOANS AND NDSLS MADE ON OR AFTER JULY 23, 1992*

In addition to being eligible for the previously mentioned cancellation provisions, a borrower of a Perkins Loan or NDSL made on or after July23, 1992 is eligible to have up to 100% of the loan canceled for teaching or qualifying employment as

***Special education teacher***

- ◊ a full-time special-education teacher, including teachers of **infants, toddlers, children, or youth with disabilities**[3] in a public or other nonprofit elementary or secondary school system;

***Teaching math, science, languages***

- ◊ a full-time teacher in a public or other nonprofit elementary or secondary school in the fields of mathematics, science, foreign languages, or bilingual education or in any other **field of expertise**[3] that is determined by a state education agency to have a shortage of qualified teachers in that state;

***Health care***

- ◊ a full-time **nurse**[3] or **medical technician**[3] providing health care services;

***Early intervention***

- ◊ a full-time **qualified professional provider of early intervention services**[3] in a public or other nonprofit program under public supervision; or

***Employee of child or family service agency***

- ◊ a full-time employee of an eligible public or private nonprofit child or family service agency who is providing or supervising the provision of services to both **high-risk children**[3] who are from **low-income communities**[3] and the families of such children.

---

[3] See the definitions of these terms at the end of this section.

For these cancellation provisions, a borrower's loan is canceled at the rates shown below for each completed year of full-time employment or services or, in the case of teachers, for each full academic year of full-time teaching:

◊ 15% of the original principal loan amount—plus any interest that may have accrued during the year—for each of the first and second years;

◊ 20% of the original principal loan amount—plus any interest that may have accrued during the year—for each of the third and fourth years; and

◊ 30% of the original principal loan amount—plus any interest that accrued during the year—for the fifth year.

## *MILITARY SERVICE CANCELLATION—APPLIES TO ALL LOANS MADE ON OR AFTER JULY 1, 1972*

A borrower is also entitled to cancellation of up to **50%** of a Perkins Loan or NDSL for service in the U.S. Armed Forces in an **area of hostilities** or an **area of imminent danger** that qualifies for special pay under Section 310 of Title 37 of the U.S. Code. The cancellation rate for every complete year of qualifying service is 12 1/2% of the original principal loan amount plus any interest that accrued during the year.

## *CANCELLATION PROVISIONS SPECIFIC TO PERKINS LOANS*

***Service in Peace Corps or ACTION programs***

For **Perkins Loans only**, a borrower is entitled to cancel up to **70%** of the loan for service as a Peace Corps volunteer or volunteer under the Domestic Volunteer Service Act (ACTION program); an authorized official of the Peace Corps or ACTION program must sign the borrower's cancellation form to certify the borrower's service. The cancellation rate per year of service is

◊ 15% of the original principal loan amount—plus any interest that accrued during the year—for each of the first and second 12-month periods of service and

◊ 20% of the original principal loan amount—plus any interest that accrued during the year—for each of the third and fourth 12-month periods of service.

## DEATH, TOTAL AND PERMANENT DISABILITY, AND BANKRUPTCY CANCELLATION PROVISIONS—APPLICABLE TO ALL LOANS

Regardless of the repayment status of a loan, the school that was the lender must cancel the unpaid balance of the loan, including interest, upon receipt of proof of the borrower's death or upon the school's approval of the cancellation request of a borrower who became permanently and totally disabled after receiving the loan. A determination of permanent and total disability must be based on medical evidence certified by a physician (a medical doctor or doctor of osteopathy, but not a doctor of naturopathic medicine). If a loan is canceled based on the borrower's permanent and total disability, the borrower cannot subsequently be required to repay the loan, even if the borrower's medical condition improves to the point that he or she is no longer disabled, unless the school can prove that the claim of disability was fraudulent.

**Definition of teacher**

In some cases, a borrower's Perkins Loan or NDSL may be discharged in bankruptcy. For more information, see "Criteria for Receiving a Bankruptcy Cancellation" on page 6-62.

## CRITERIA FOR TEACHER CANCELLATION

Eligibility for teacher cancellation is based on the duties presented in an official position description, not on the position title. To receive a cancellation, the borrower must be teaching full time in a **public or other nonprofit elementary or secondary school system** and must be **directly employed** by the school system. There is no provision for canceling Perkins Loans or NDSLs for teaching in postsecondary schools.

A teacher is a person who provides to students

- ◊ direct classroom teaching;
- ◊ classroom-type teaching in a non-classroom setting; or
- ◊ educational services directly related to classroom teaching.

Two examples of qualifying individuals for the third category are school librarians and school guidance counselors.

A supervisor, administrator, researcher, or curriculum specialist is not a teacher unless he or she primarily provides direct and personal educational services to students.

A person who provides one of the following services does not qualify as a teacher unless 1) that person is licensed, certified, or registered by the appropriate state education agency for that area in which he or she is providing related special educational services and 2) the services provided by the individual are part of the educational curriculum for handicapped children:

- ◊ speech and language pathology and audiology;
- ◊ physical therapy;
- ◊ occupational therapy;
- ◊ psychological and counseling services; or
- ◊ recreational therapy.

For a borrower to be considered as teaching in a field of expertise, the majority of classes taught must be in the borrower's field of expertise. A borrower who is teaching in science, mathematics, foreign language, or bilingual education qualifies for cancellation even if the state has not designated the subject area in which he or she is teaching as a shortage area.

For a borrower to be considered as a full-time professional provider of early intervention services, the borrower must be employed in a public or nonprofit program under public supervision.

If the borrower teaches both children and adults, the majority of students must be children for the borrower to qualify for cancellation.

***Teacher who is not certified or licensed***

It is not necessary for a teacher to be certified or licensed to receive cancellation benefits. However, the employing institution must consider the borrower to be a full-time professional for the purposes of salary, tenure, retirement benefits, and so on. In other words, to qualify, the borrower should accrue the same benefits as teachers who are licensed and/or certified.

***Teacher's aide***

Under certain conditions, a teacher's aide may be considered eligible for teacher cancellation. The teacher's aide must meet the definition of a "full-time teacher." He or she must have a bachelor's degree and be a professional recognized by the state as a full-time employee rendering direct and personal services in carrying out the instructional program of an elementary or secondary school.

***Volunteer teachers***

Volunteer teachers are not considered to be professionally employed on a full-time basis and, therefore, are not eligible for teacher cancellation benefits.

***Private academy***

A borrower may receive teacher cancellation for services performed in a private academy if the private academy has established its nonprofit status with the Internal Revenue Service (IRS) and if the academy is providing elementary and/or secondary education according to state law.

***School accreditation***

A private elementary and/or secondary school does not necessarily need to be accredited for a borrower teaching there to qualify for teacher cancellation. However, the school must have established its nonprofit status with the IRS and must be licensed by the state (that is, must be providing elementary and/or secondary education according to state law).

A borrower may receive National Defense Student Loan (Defense Loan) cancellation for teaching in a proprietary institution if that institution has established its nonprofit status with the IRS.

***Preschool/ prekindergarten programs***

A borrower may receive teacher cancellation for teaching service performed in a preschool or prekindergarten program only if the state considers the program to be a part of its elementary education program. A low-income-school-directory designation that includes pre-kindergarten or kindergarten does not suffice for a state determination of program eligibility. The school must check with the state superintendant of public instruction to determine whether these programs are part of the **state** elementary education program.

***Teaching in Job Corps projects***

A borrower cannot receive teacher cancellation for teaching service performed in a Job Corps Project unless the teaching is considered to be conducted in an elementary or secondary school or school system.

The cancellation form the borrower files must be signed by an official in the school system or agency to certify the borrower's service.

The borrower must teach full time for a full academic year or its equivalent. There is no requirement that a teacher must teach a given number of hours a day in order to qualify as a full-time teacher; the employing school is responsible for determining whether or not the individual is considered to be a full-time teacher. An "academic year or its equivalent" for teacher cancellation purposes is defined as one complete school year or two half years that are

- ◊ from different school years, excluding summer sessions,
- ◊ complete,
- ◊ consecutive, and
- ◊ generally fall within a 12-month period.

**_Incomplete academic year_**

A borrower who cannot complete the academic year because of illness or pregnancy may still qualify for cancellation if he or she has completed the first half of the academic year and has begun teaching the second half, but the borrower's employer must consider the borrower to have fulfilled his or her contract for the academic year.

**_Cancellation for a combination of teaching_**

A borrower who is simultaneously teaching part time in two or more schools may request a cancellation based on teaching full time if he or she can obtain appropriate certification that he or she is teaching full time. The postsecondary school that made the loan may grant the cancellation if an official at one of the schools where the borrower taught certifies that the borrower taught full time for a full academic year. For example

◊ under a consortium agreement, a borrower may be employed by the consortium and teach at member schools;[4]

◊ two or more schools, by mutual agreement, could arrange to have one school employ the borrower on a full-time basis and then hire out his or her services to the other school(s) involved in the agreement;[5] or

◊ a borrower can be considered to have been a full-time teacher for an academic year if he or she can obtain appropriate certifications that he or she has taught in two half-time teaching positions for a complete academic year in two elementary or secondary schools or in two secondary schools.

A school may refuse cancellation for simultaneous teaching in two or more schools if it cannot easily be determined that the teaching was full time.

A cancellation based on teaching in a school serving students from **low-income** families may be granted only if the borrower taught in an eligible school that is listed in the *Directory of Designated Low-Income Schools for Teacher Cancellation Benefits*. The Department compiles and publishes this directory of low-income schools annually after consulting with each state's educational agency. The Department sends a copy of the directory to each school that participates in the Perkins Loan Program. The Department considers a school to be a low-income school only if 1) it is in a school district that qualifies for federal funding based on the large number of low-income families in the district and 2) more than 30% of the school's enrollment is made up of children from low-income families. The official 1996-97 Directory was issued to schools in October 1996.

---

[4] The consortium provides the certification of full-time teaching.

[5] The employing school certifies the borrower's full-time teaching status.

***Cancellation if school is removed from list***

If a borrower is teaching at a school that is on the list one year but not in subsequent years, the borrower may continue to teach in that school and remain eligible to receive a cancellation for service in that school. If a list is not available before May 1 of any year, the Department may use the previous year's list to make the service determination for that year. Information about specific schools listed in the directory may be obtained from

Ms. Sherraine Green
Campus-Based Programs Systems Division
Program Systems Service
Office of Postsecondary Education
U.S. Department of Education
600 Independence Avenue, SW, (ROB-3, Room 4051)
Washington, DC 20202-5447

Telephone: 202/708-5774

***Teaching at BIA schools***

All elementary and secondary schools operated by the Bureau of Indian Affairs (BIA) are considered to qualify as schools serving low-income families for the purpose of teacher cancellations of Perkins Loans and NDSLs. Elementary and secondary schools operated on reservations by Indian tribal groups under contract with the BIA are also considered to qualify for this purpose.

For Perkins Loans or NDSLs made **on or after** July 23, 1992, a borrower may receive a cancellation as a full-time special education teacher (including teachers of infants, toddlers, children, or youth with disabilities) in a public or other nonprofit elementary or secondary school system.

For Perkins Loans or NDSLs made **before** July 23, 1992, a borrower may receive a cancellation for full-time teaching of handicapped children for a full academic year or its equivalent. The borrower qualifies for this cancellation only if a majority of the students whom the borrower teaches are handicapped children. Handicapped children include those who are mentally retarded, hard of hearing, deaf, speech and language impaired, visually disabled, seriously emotionally disturbed, orthopedically impaired, autistic, have traumatic brain injury or specific learning disabilities, or are otherwise health-impaired children who require special education and related services because of their disabilities.

The **only** cancellation provisions for service in elementary or secondary schools are:

◊ teaching in schools serving low-income families;

◊ teaching mathematics, science, foreign languages, or bilingual education;

◊ teaching in a field of expertise that is determined by a state education agency to have a shortage of qualified teachers in that state;

◊ teaching as a special education teacher; and

◊ providing early intervention services.

### *CRITERIA BORROWER MUST MEET FOR MILITARY CANCELLATION*

To qualify for military cancellation, the borrower must be serving a period of full-time active duty in the armed forces (that is, the U.S. Army, Navy, Air Force, Marine Corps, or Coast Guard). A member of the National Guard or the Reserves serving a period of full-time active duty in the armed forces is also eligible to receive a military deferment. For a Perkins Loan or NDSL cancellation, the service in the armed forces must be in an **area of hostilities** or an **area of imminent danger** that qualifies for special pay under Section 310 of Title 37 of the U.S. Code. For Defense Loan cancellation, the service does not have to be in an area of hostilities or area of imminent danger. The borrower's Commanding Officer must certify the borrower's service dates. The cancellation rate of 12 1/2% of the original principal loan amount is for each **complete** year of service; service for less than a complete year or any fraction of a year beyond a complete year does not qualify.

### *CRITERIA FOR HEAD START CANCELLATION*

A full-time staff member is someone who is regularly employed in a full-time professional capacity to carry out the educational part of a Head Start program. The program must operate for a full academic year, or its equivalent, and the borrower's salary may not be more than that of a comparable employee working in the local educational agency. An authorized official of the Head Start Program must sign the borrower's cancellation form to certify the borrower's service.

### *CRITERIA FOR EMPLOYEE OF A CHILD OR FAMILY SERVICES AGENCY*

To receive loan cancellation for being employed at a child or family services agency, a borrower must be providing services **only** to high-risk children who are from low-income communities. The borrower may also be providing services to adults, but these adults must be members of the families of the children for whom services are provided. The services provided to adults must be secondary to the services provided to the high-risk children. The Department has determined that an elementary or secondary school system or a hospital is not an eligible employing agency.

## CRITERIA FOR LAW ENFORCEMENT OR CORRECTIONS OFFICER CANCELLATION

To establish the eligibility of a borrower for the law enforcement or corrections officer cancellation provision, the school must determine that 1) the borrower's employing agency is eligible and that 2) the borrower's position is essential to the agency's primary mission.

1. A local, state, or federal agency is an eligible employing agency if it is publicly funded and its activities pertain to crime prevention, control, or reduction or to the enforcement of the criminal law. Such activities include, but are not limited to, police efforts to prevent, control, or reduce crime or to apprehend criminals; activities of courts and related agencies having criminal jurisdiction; activities of corrections, probation, or parole authorities; and problems relating to the prevention, control, or reduction of juvenile delinquency or narcotic addiction.

   Agencies that are primarily responsible for enforcement of civil, regulatory, or administrative laws are ineligible.

2. For the borrower's position to be considered essential to the agency's primary mission, he or she must be a full-time employee of an eligible agency and a sworn officer or person whose principal responsibilities are unique to the criminal justice system and are essential in the performance of the agency's primary mission. The agency must be able to document the employee's functions.

Individuals whose official responsibilities are supportive, such as those that involve typing, filing, accounting, office procedures, purchasing, stock control, food service, transportation, or building, equipment or grounds maintenance are not eligible for the law enforcement or correction officer loan cancellation regardless of where these functions are performed. Also, a borrower employed as a public defender does not qualify for cancellation benefits under this provision.

## CRITERIA FOR DISABILITY CANCELLATION

Any Perkins Loan, NDSL, or Defense Loan will be canceled if the borrower dies or becomes permanently and totally disabled after receiving the loan. Permanent and total disability is the inability to work and earn money or to attend school because of an impairment that is expected to continue indefinitely or to result in death.

Even a 95% disability does not qualify the borrower for disability cancellation. Receiving Social Security disability benefits does not automatically qualify a borrower for permanent and total disability cancellation.

If a borrower becomes permanently and totally disabled, the school must decide whether to cancel the loan based on medical evidence (certified by a physician) that the borrower or his or her representative must furnish. This evidence must include statements from all physicians, hospitals, or agencies concerned with the case and should include certification that the criteria for permanent and total disability have been met. If a loan is canceled based on the borrower's permanent and total disability, the borrower cannot subsequently be required to repay the loan, even if the borrower's medical condition improves to the point that he or she is no longer disabled, unless the school can prove that the claim of disability was fraudulent. The Department does not approve or supply cancellation forms. In the case of a borrower's death, the school must receive a death certificate or other proof as required under state law.

## CRITERIA FOR RECEIVING A BANKRUPTCY CANCELLATION

A Perkins Loan, NDSL, or Defense Loan will be written off for bankruptcy if the school receives an official notice of discharge from a bankruptcy court unless the school is required to oppose the discharge. For more information, see "Bankruptcy" in Section 9 of this chapter. Note that a borrower is no longer required to reaffirm a loan discharged in bankruptcy before he or she is eligible to apply for additional student aid including loans. This is a provision of the Bankruptcy Amendments Act of 1994, effective October 22, 1994.

## REIMBURSING AMOUNTS CANCELED

For Perkins Loans and NDSLs, the Department will reimburse each school every award year for the principal and interest canceled from its Perkins Loan Fund for all of the cancellation provisions except for death, total and permanent disability, and bankruptcy. The school must deposit in its fund the amount reimbursed. Not that for loans made on or after July1, 1993, interest no longer accrues during the period that a borrower is performing service to qualify for cancellation benefits.

For Perkins Loans or NDSLs made **on or after** July 23, 1992, new cancellation provisions include several new terms that have not been defined previously in the regulations. Definitions of these terms are as follows:

**Children and youth with disabilities**. Children and youth from ages 3 through 21, inclusive, who require special education and related services because they have disabilities as defined in section 602(a)(1) of the Individuals with Disabilities Education Act;

Section 602(a)(1) defines "handicapped children" as children who are mentally retarded, hard of hearing, deaf, speech or language impaired, visually handicapped, seriously emotionally disturbed, orthopedically impaired, or other health impaired children or children with specific learning disabilities who by reason thereof require special education and related services.

**Early intervention services**. Those services defined in section 672(2) of the Individuals with Disabilities Education Act that are provided to infants and toddlers with disabilities;

**High-risk children**. Individuals under the age of 21 who are low-income or at risk of abuse or neglect, have been abused or neglected, have serious emotional, mental, or behavioral disturbances, reside in placements outside their homes, or are involved in the juvenile justice system;

**Infants and toddlers with disabilities**. Infants and toddlers from birth to age two, inclusive, who need early intervention services for specified reasons, as defined in section 672(1) of the Individuals with Disabilities Education Act;

Section 672(1) of the Act defines infants and toddlers with disabilities as those who

- ◊ have a diagnosed physical or mental condition which has a high probability of resulting in developmental delay or
- ◊ are experiencing developmental delays, as measured by appropriate diagnostic instruments and procedures in one or more of the following areas: cognitive development, physical development, language and speech development, psychosocial development, or self-help skills.

The term **infants and toddlers with disabilities** may also include, at a state's discretion, individuals from birth to age two, inclusive, who are at risk of having substantial developmental delays if early intervention services are not provided;

**Low-income communities**. Communities in which there is a high concentration of children eligible to be counted under Title I of the Elementary and Secondary Education Act of 1965, as amended;

**Medical Technician**. An allied health professional (working in fields such as therapy, dental hygiene, medical technology, or nutrition) who is certified, registered, or licensed by the appropriate state agency in the state in which he or she provides health care services; an allied health professional is someone who assists, facilitates, or complements the work of physicians and other specialists in the health care system;

**Nurse**. A licensed practical nurse, a registered nurse, or other individual who is licensed by the appropriate state agency to provide nursing services;

**Qualified professional provider of early intervention services**. A provider of services, as defined in section 672(2) of the Individuals with Disabilities Education Act;

Section 672(2) of that Act defines developmental services as those services that

◊ are provided under public supervision;

◊ are provided at no cost except where federal or state law provides for a system of payments by families, including a schedule of sliding fees;

◊ are designed to meet a handicapped infants's or toddler's developmental needs in any one or more of the following areas:

- physical development;
- cognitive development;
- language and speech development;
- psychosocial development; or
- self-help skills;

- ◊ meet the standards of the state, including the requirements of this part;
- ◊ include:
  - family training, counseling, and home visits;
  - special instruction;
  - speech pathology and audiology;
  - occupational therapy;
  - physical therapy;
  - psychological services;
  - case management services;
  - medical services only for diagnostic or evaluation purposes;
  - early identification, screening, and assessment services; and
  - health services necessary to enable the infant or toddler to benefit from the other early intervention services;
- ◊ are provided by qualified personnel, including
  - special educators;
  - speech and language pathologists and audiologists;
  - occupational therapists;
  - physical therapists;
  - psychologists;
  - social workers;
  - nurses; and
  - nutritionists; and
- ◊ are provided in conformity with an individualized family service plan adopted in accordance with Section 677 of the Individuals with Disabilities Education Act.

**Teaching in a field of expertise**. The majority of classes taught are in the borrower's field of expertise.

# Due Diligence—Billing & Address Searches

Due diligence is the steps schools must take to collect Federal Perkins Loans and National Direct Student Loans (NDSLs). These steps include, but are not limited to, billing the borrower, sending overdue notices when necessary, and conducting address searches if the borrower cannot be located. If billing procedures fail to get the borrower into repayment, schools must proceed to the second—and more intensive—stage of collection. This stage may include hiring a collection firm. In many cases, schools may have to litigate.

Due diligence comprises all these procedures, but it can also be as basic as keeping the borrower informed of all program changes that affect his or her rights and responsibilities and responding promptly to the borrower's inquiries.

***Keep borrower information current***

Keeping current information on a borrower makes it easier for the school to know when repayment must begin and where to send billing notices. The various offices at the school—the admissions, business, alumni, placement, financial aid, and registrar's offices, and others, as necessary—must provide the information they have available about the borrower to those offices responsible for billing and collecting loans to assist them in determining the following information about the borrower:

◊ enrollment status;

◊ expected graduation or termination date;

◊ the date the borrower officially withdraws, drops below half-time enrollment, or is expelled; and

◊ current name, address, telephone number, Social Security Number, and driver's license number (if any).

## *EXIT INTERVIEW*

Contact with the borrower becomes even more important just before he or she leaves school, when the school must hold an exit interview to explain the borrower's responsibility for repaying the loan and to state when the

first payment will be due and whether payments are to be made monthly, bimonthly, or quarterly. If individual interviews are not possible, group interviews are acceptable. The school must document its exit interviews.

***School must provide certain information***

During the interview, a borrower must be informed of the terms of the loan, the amount of the outstanding balance, and his or her obligation to repay according to the repayment schedule. The school must also make the borrower aware of the consequences of default, including the possibility that his or her account may be referred to a collection firm, that the default will be reported to a national credit bureau, and that legal action may be taken to collect the amount owed.

***Borrower rights and responsibilities***

A borrower must also be told his or her rights and responsibilities including

◊ his or her responsibility to inform the school immediately of any change in name, address, telephone number, Social Security Number, or driver's licence number;

◊ his or her rights to forbearance, deferment, cancellation, or postponement of repayment and the procedures for filing for those benefits;[1] and

◊ his or her responsibility to contact the school before the due date of any payment he or she cannot make.

***Additional information school must provide to borrower***

The school must provide the following additional information during the exit interview by including it either in the borrower's promissory note or in some other written statement the school gives the borrower. A school that is unaware that a borrower has left school must attempt to provide the required information to the borrower in writing upon learning that the borrower has left:

◊ the name and address of the school to which the debt is owed and the name and address of the official or servicing agent where communications should be sent;

◊ the name and address of the party where payments should be sent;

◊ the estimated amount the borrower owes on the date the repayment period is scheduled to begin and the amount of the total debt (principal and interest);

---

[1] See Sections 4 and 5 of this chapter for more information

- ◊ the interest rate and the projected total interest charges the borrower will pay;
- ◊ a discussion of the repayment schedule including the date the first installment is due, and the number, amount, and frequency of required payments;
- ◊ any special options for loan consolidation or other refinancing;
- ◊ a statement that the borrower may prepay all or part of the loan without penalty;
- ◊ a discussion of any fees that will be charged the borrower for not making payments on time;
- ◊ a description of any charges associated with default, such as liability for loan collection costs reasonably incurred by the school or the Department; and
- ◊ information about the borrower's rights to forbearance, deferment, cancellation or postponement of repayment and the procedures for filing for those benefits.

A school is no longer required to give borrowers information about the average indebtedness of students with Perkins Loans at that school.

***Collecting information during the exit interview***

The school must require the borrower to provide the following information during the exit interview, which the school must keep in its records:

- ◊ the borrower's expected permanent address after leaving school (regardless of the reason for leaving);
- ◊ the name and address of the borrower's expected employer after leaving school;
- ◊ the borrower's driver's license number;
- ◊ the address of the borrower's next of kin; and
- ◊ any corrections in the school's records relating to the borrower's name, address, Social Security Number, personal references, and driver's license number.

At the time of the exit interview, the borrower must sign the repayment schedule, and the school must give the borrower copies of the signed schedule and the signed promissory note. As previously noted, the school

must keep the original signed promissory note and repayment schedule in a locked, fireproof container until the loan is repaid or until the originals are needed to enforce collection of the loan. If the originals are released for enforcement purposes, the school must keep certified true copies of the documents released.

***Mailing exit interview materials***

If the school discovers that a borrower has left without having had an exit interview, the school must either contact the borrower and personally give him or her the information listed on the previous pages or mail this information. The school must also provide the borrower a copy of the signed promissory note and two copies of the repayment schedule, one of which the borrower must sign and return to the school.

## *CONTACT DURING GRACE PERIODS*

***Three contacts in nine-month grace period***

***Two contacts in six-month grace period***

The school must contact the borrower during both initial and post-deferment grace periods to remind him or her when repayment will begin or resume. For a loan with a nine-month initial grace period, the school must contact the borrower three times during the grace period. For a loan with a six-month initial grace period, the school must contact the borrower twice during that period. Most loans also have **post-deferment** grace periods of six months. For such a loan, the school must also contact the borrower twice during any post-deferment grace period. The chart below shows the length of initial and post-deferment grace periods for NDSLs and Perkins Loans.

**GRACE PERIODS**
(Borrowers Attending at Least Half Time)

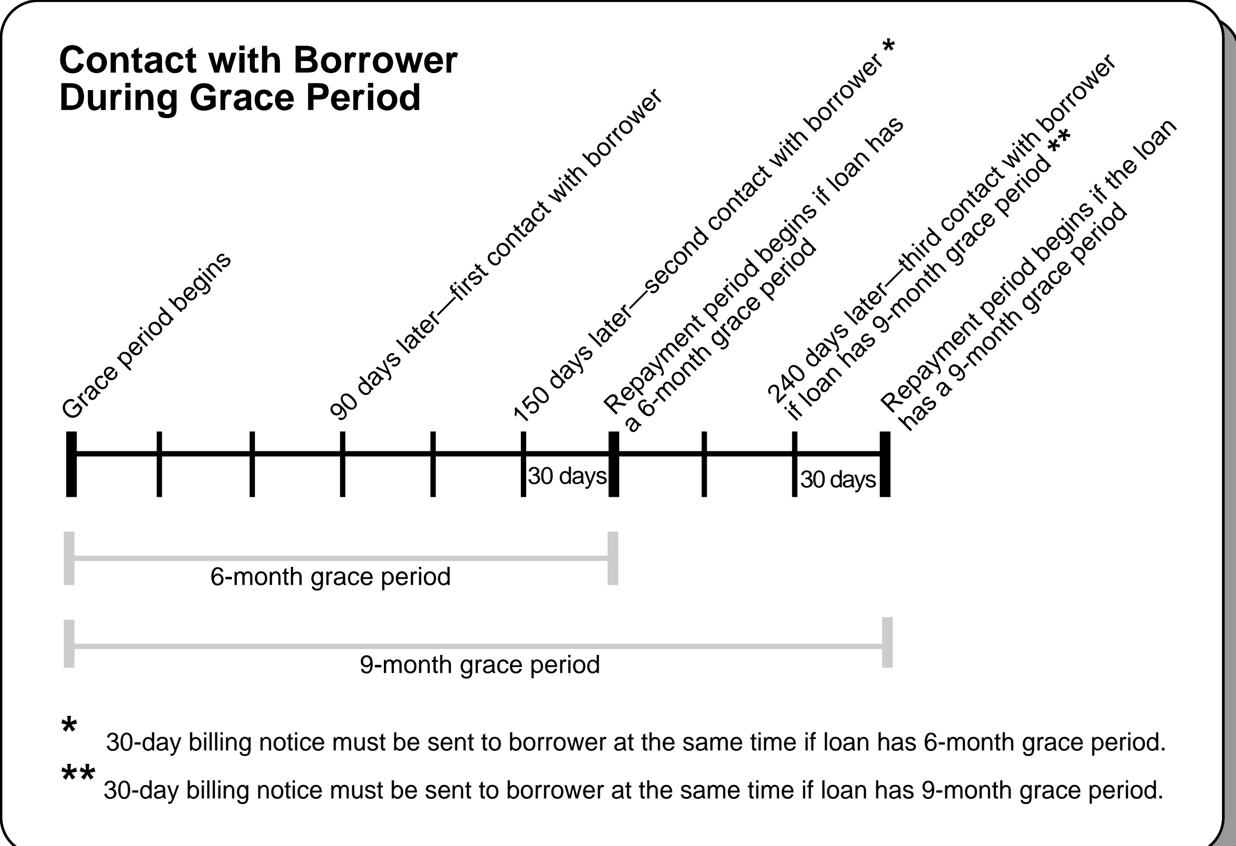
| Type of Grace Period | Federal Perkins Loans | NDSLs made on or after 10/1/80 | NDSLs made before 10/1/80 |
|---|---|---|---|
| **Initial** | 9 months | 6 months | 9 months |
| **Post-Deferment** | 6 months | 6 months | None |

The **first contact** must be **90 days** after any grace period (initial or post-deferment) begins. The school must remind the borrower of the responsibility to repay the loan and must send the borrower information about the total amount to be repaid (or remaining to be paid, if a payment has been made in the past). This information must include the amount of principal and interest over the remaining life of the loan and the due date and amount of the first payment (or next payment, if a payment has been made previously).

The **second contact** must be 150 **days** after any grace period begins, when the school must again remind the borrower of the due date and amount of the first (or next) payment. The second contact is timed to coincide with

the first billing notice for a loan with a six-month grace period (30 days before the first payment is due). These two notices may be combined.

For a borrower with a **nine-month** initial grace period, the school must make a **third contact 240 days** after the grace period begins to remind the borrower of the date and amount of the first payment. Like the second contact for a loan with a six-month grace period, this 240-day contact is timed to coincide with the first billing notice. Again, the school may combine the two notices. (Refer to the chart below.)




## *BILLING PROCEDURES*

Billing refers to that series of actions the school routinely performs to notify borrowers of payments due, remind them of overdue payments, and demand payment of overdue amounts.

The school may choose a coupon payment system as its method of billing. If so, the school must send the coupons to the borrower at least 30 days before the first payment is due. If the school does not use a coupon system, it must, at least **30 days** before the first payment is due, send the borrower a statement of account and a written notice giving the name and address of the party to which payments should be sent. The statement of

account includes information such as the total amount borrowed, the interest rate on the loan, and the amount of the monthly payment. For subsequent payments, the school must send the borrower a statement of account at least **15 days** before the due date of the payment.[2]

***First overdue notice***

If a payment is overdue and the school has not received a request for forbearance, deferment, postponement, or cancellation, the school must send the borrower an **overdue notice** within **15 days** after the due date.

***Late charge required***

For loans made for periods of enrollment beginning on or after January 1, 1986, schools are required to impose a late charge when the borrower's payment becomes overdue.[3] The charge is based either on the actual costs the school incurs in taking steps to obtain the overdue amount or on average costs incurred in similar attempts with other borrowers. The charge may not exceed 20% of the installment payment most recently due.

The school must also impose a late charge if the borrower's payment is overdue and the borrower has not filed a complete request for forbearance, deferment, cancellation, or postponement on time.[3] To be considered complete, the request must contain enough information for the school to determine whether the borrower is entitled to the relief requested.

Late charges on loans made for periods of enrollment that began on or after January 1, 1986 may be assessed only during the billing process; they may not be imposed once the school begins collection procedures. For a borrower who repays the full amount of past-due payments, the school may waive any late charges that were imposed.

***Optional penalty charge before 1/1/86***

Schools are authorized but not required to assess a penalty charge for an overdue payment on a loan made for a period of enrollment that began before January 1, 1986. The maximum penalty charge that may be assessed on a loan payable monthly is $1 for the first month and $2 for each additional month a payment is overdue; the maximum penalty for a loan payable bimonthly is $3; the maximum penalty for loans payable quarterly is $6. Penalty charges on these loans may be assessed only during the billing process.

The school may either add the penalty or late charge to the principal amount of the loan as of the first day the payment was due or may include the charge with the next payment that is scheduled after the date it notifies the borrower that the charge must be paid in full by the next payment due

---

[2] If the borrower elects to make payments by means of an electronic transfer of funds from the borrower's bank account, the school is not required to send the borrower a statement of account at least 15 days before the due date of each subsequent payment. However, the school must send the borrower an annual statement of account.

[3] The mandatory late charges do not apply retroactively to loans made before July 1, 1987, but would apply to any NDSL borrower who has a re-signed revised promissory note.

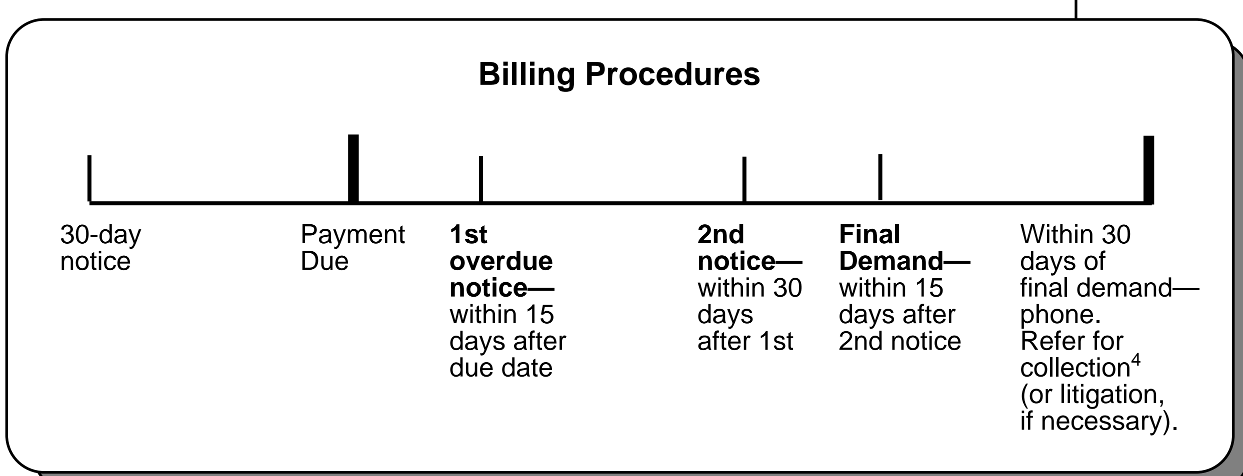
date. Schools may wish to use the first overdue notice to inform the borrower of the late charge.

***Second notice***

If the borrower does not satisfactorily respond to the first overdue notice, the school must continue to contact him or her. A **second overdue notice** must be sent within **30 days** after the first. If there is still no response, a **final demand letter** must be sent within **15 days** after the second notice. The letter may be (but does not have to be) sent by certified mail. The final demand letter must inform the borrower that unless the school receives a payment or a request for forbearance, deferment, postponement, or cancellation **within 30 days** of the date of the letter, the school will refer the account for collection[4] or litigation and will report the default to a credit bureau as required by law.

***Final demand***

The school may skip the first two letters and send just the final demand letter within **15 days** after the payment is overdue if the borrower's repayment history has been unsatisfactory or if the school can reasonably conclude the borrower does not intend to repay or to seek forbearance, deferment, postponement, or cancellation. A borrower is considered to have an unsatisfactory repayment history if he or she has previously failed to make payments when due, has previously failed to request deferment, forbearance, postponement, or cancellation on time, or has previously received a final demand letter.




***Telephone contact***

If the borrower does not respond to the final demand letter within 30days, the school must try to contact him or her by telephone before beginning collection procedures. As telephone contact is often very effective in getting the borrower to begin repayment, the school may be able to avoid the more costly procedures of collection.

---

[4] The school can use the services of the Department's Default Reduction Assistance Project (DRAP) before the loan goes to a collection firm; DRAP is discussed in Section 8, "Default."

If the school calls a number and there is no answer, the school should make at least one other attempt to reach the borrower on a different day and at a different time. If the borrower has an unlisted telephone number, the school must make reasonable attempts to obtain it by contacting sources such as the borrower's employer or parents. If the school is still unsuccessful, it should document that fact in its files.

If the borrower does not respond satisfactorily to the final demand letter, the school must try and recover the amount owed from the borrower. For loans made prior to July 23, 1992, the school must also try to collect the amount owed from any endorser of the loan. In an effort to recover the loan from one party or the other, a school often sends the endorser a copy of the final demand letter that was sent to the borrower and copies of all future communications about the borrower's debt, including dunning letters. For loans made on or after July 23, 1992, an endorser is no longer required.

***Acceleration***

The school may choose to accelerate a loan if the borrower misses a payment or does not file for deferment, forbearance, postponement, or cancellation on time. Acceleration means making payable immediately the entire outstanding balance including interest and any applicable late charges or collection fees. Because this marks a serious stage of default, the borrower should have one last chance to bring his or her account current. For that reason, if the school plans to accelerate the loan, it must send the borrower written acceleration notice at least 30 days in advance. The notice may be included in the final demand letter or in some other written notice sent to the borrower. If the loan is accelerated, the school must subsequently send the borrower a second notice to inform him or her of the date the loan was accelerated and the total amount due. Remember that acceleration is an option, not a requirement. However, if a school plans to assign the loan to the Department for collection, the school must first accelerate the loan. Once a loan has been accelerated, the borrower loses all rights to deferment and cancellation benefits for qualifying service performed after the date of acceleration.

## ADDRESS SEARCHES

The school must take the following steps to locate the borrower if communications are returned undelivered (other than unclaimed mail):

- ◊ review the records of all appropriate institutional offices and
- ◊ review telephone directories or check with information operators in the area of the borrower's last known address.

If these methods are unsuccessful, the school must either use its own personnel to try to locate the borrower (employing and documenting

efforts comparable to commercial skip-tracing services), or must use a commercial skip-trace firm. The school may elect to use the Internal Revenue Service skip-tracing service provided through the Department, discussed below.

If the school still cannot locate the borrower after taking these steps, it must continue to make reasonable attempts at least twice a year until

- ◊ the loan is recovered through litigation;
- ◊ the account is assigned to the Department; or
- ◊ the account is written off. (See Section7.)

***IRS/ED skip-tracing service***

To help locate a borrower whose collection notices are returned undelivered, a school may participate in the IRS/ED skip-tracing service. The Higher Education Amendments of 1992 eliminated the **requirement** that schools use the IRS/ED skip-tracing service in carrying out the provisions of due diligence. However, the Department strongly encourages schools to continue to use this service. The IRS/ED skip-tracing service is one of the most powerful tools available to schools for locating defaulted borrowers. The Department will continue to send schools that participate in the Perkins Loan Program periodic “Dear Colleague” letters that give instructions for completing the report. “Dear Colleague” Letter CB-96-15 (LD), dated July 1996, included instructions for completing the Report that was due by August 31, 1996.

***Filing a Safeguard Activity Report to use IRS/ED skip tracing***

In order to maintain eligibility to participate in the IRS/ED skip-tracing service, each participating school must submit an annual Safeguard Activity Report, in accordance with the IRS publication 1075. If a school fails to submit the Report, it will lose its eligibility to participate in the service. The reports help ensure that procedures are established and utilized to safeguard the names and addresses of defaulted borrowers under the Perkins Loan Program. General questions should be directed to the Department’s Program Systems Service, Campus-Based Programs Systems Division. The telephone number is (202) 708-6726.

# Due Diligence—Loan Collection

## COLLECTION PROCEDURES

Collection procedures are the more intensive efforts a school must make when borrowers have not responded satisfactorily to billing procedures and are considered seriously in default.

***Report default to credit bureau***

The **first** step a school must take in the collections process is to report a defaulted loan account to a national credit bureau organization with which the U.S. Department of Education has an agreement. (The debtor has the right to appeal the accuracy and validity of the information reported to the credit bureau.)

***Report changes in loan status to credit bureau***

The school must report any changes in the status of the borrower's loan account to the same national credit bureau to which the school originally reported the default. The school must use the reporting procedures required by that credit bureau. The school must also respond within one month to any inquiry received from that or any other credit bureau about the information reported on the loan amount.

***School or firm collects***

The **second** step the school must take in the collections process is to attempt collection by either using its own personnel or hiring a collection firm.

If the school's personnel or the collection firm cannot convert the account to regular repayment status by the end of 12 months (or if the borrower does not qualify for forbearance, deferment, postponement, or cancellation), the school has two options—either to litigate or to make a second effort to collect.

***Procedures for second effort to collect***

A second effort to collect requires one of the following procedures:

- ◊ If the school first attempted to collect by using its own personnel, it must refer the account to a collection firm unless state law prohibits doing so.

◊ If the school first used a collection firm, it must attempt to collect by using its own personnel or by using a different collection firm, or the school must submit the account to the Department for assignment.

If a collection firm (retained by a school as part of its second effort to collect) cannot place an account into regular repayment status by the end of 12 months (or if the borrower does not qualify for forbearance, deferment, postponement, or cancellation), the firm must return the account to the school.

***Procedures if school is unable to collect***

If the school is unsuccessful in its effort to place the loan in repayment after following the procedures above, the school must continue to make annual attempts to collect from the borrower until

◊ the loan is recovered through litigation;

◊ the account is assigned to the Department; or

◊ the loan is written off.

***Ceasing collection activity on defaulted loans***

A school may cease collection activity on a defaulted account with a balance of less than $25.00, including outstanding principal, accrued interest, collection costs and late charges if the borrower has been billed for this balance. The school will not have to exercise required due diligence even though interest will continue to accrue and may put the account over $25.00. The school must document that it ceased collection activity when the account was under $25.00. However, the school will not be able to assign the account to the Department, and the borrower will remain responsible for repaying the account, including accrued interest. The account will still be included in the school's cohort default rate, if applicable, and the borrower is still in default and ineligible for Student Financial Assistance (SFA) funds.

A school may cease collection activity on defaulted accounts with balances of less than $200, including outstanding principal, accrued interest, collection costs and late charges, if the school carried out the required due diligence and if the account has had no activity for four years. Such an account will be included in the school's cohort default rate, if applicable. The borrower is still in default and ineligible for additional SFA funds.

***Writing off accounts***

A school may write off an account with a balance of **less than $5.00**, including outstanding principal, accrued interest, collection costs and late charges. If the school writes off an account, the school may no longer include the amount of the account as an asset of the Federal Perkins Loan fund. If a school receives a payment from a borrower after the loan has been written off, it must deposit that payment into the fund.

The school must determine the amount of collection costs to be charged to the borrower for address searches, collection, litigation, use of contractors for collection of the loan, and/or bankruptcy proceedings. The collection costs must be based on either actual costs incurred in collecting the borrower's loan or average costs incurred for similar actions taken to collect loans in similar stages of delinquency. The school must assess all reasonable collection costs against the borrower without regard to any provisions of state law that would conflict with the above provisions.

***Assessing collection costs against borrower***

For loans made from 1981 through 1986, many promissory notes contain a limitation on the amount of costs that can be recovered from the borrower (25% of the outstanding principal and interest due on the loan). As this provision has not been applicable since the beginning of the 1987-88 award year, if these borrowers ask for new advances, the Department strongly encourages schools to issue new promissory notes without this provision and to require the provisions of the new note to apply to repayment of previous advances. The borrower will then be liable for **all** collection costs on all of his or her outstanding loans borrowed under this program. A school should note, however, that advances made prior to the signing of the new note do not qualify for new deferment and cancellation benefits.

***Limit on collection charges on older notes***

The school determines what collection costs are reasonable, as long as they are based either on actual costs the school incurs for the particular borrower or on average costs incurred in collecting loans in similar stages of default. The school should explain to the borrower how it calculates collection costs, based on the cost analysis used to support charges of these costs to the Perkins Loan Fund. The school must be able to document the basis for the costs assessed.

## *ACTIONS A SCHOOL MAY TAKE TO AVOID LITIGATION*

Before filing suit on a loan, a school may waive all collection costs on a loan if the borrower makes a lump-sum payment of the entire amount outstanding, including principal and interest; a written repayment agreement is not a precondition. The amount waived may be charged to the Perkins Loan Fund.

Another alternative is for the school to waive a **portion** of the collection costs on a loan if doing so will give the school greater flexibility in negotiating repayment. The school may waive a percentage of the collection costs, applicable to the amount then due on the loan, equal to the percentage of the past-due balance the borrower repays within 30 days of entering into a written repayment agreement with the school. For example, if the borrower repays one-half the outstanding balance on a loan within 30 days of the agreement, the school may waive one-half of

the collection costs incurred through the date of that payment. The amount waived may be charged to the Perkins Loan fund.

As stated earlier, a school may write off an account with a balance of **less than $5.00**, including outstanding principal, accrued interest, collection costs and late charges but may no longer include the amount of the account written off as an asset of the Perkins Loan fund.

***Compromise***

A school may compromise on the repayment of a defaulted loan if the school has fully complied with all due diligence requirements and the student borrower pays in a single lump-sum payment

- ◊ at least 90% of the outstanding principal balance on the loan;
- ◊ all interest due; and
- ◊ any collection fees due.

The federal share of the compromise repayment must bear the same relation to the school's share of the compromise repayment as the Federal Capital Contribution (FCC) to the school's loan fund under this part bears to the school's Institutional Capital Contribution (ICC) to the fund.

The Federal Family Education Loan (FFEL) Program regulations allow a borrower to receive a Federal Consolidation Loan that could include a defaulted Perkins Loan, National Direct Student Loan (NDSL), or Defense Loan on which the borrower has made satisfactory repayment arrangements if the defaulted loan will reenter repayment through consolidation. Consolidation Loans are discussed in Chapter 10.

Similarly, the William D. Ford Federal Direct Loan Program allows a borrower to receive a Direct Consolidation Loan that could include a defaulted Perkins Loan, NDSL, or Defense Loan. To consolidate a defaulted loan, the borrower must either agree to repay the Direct Consolidation Loan under that program's income-contingent repayment plan, or he or she must make satisfactory repayment arrangements on the defaulted loan before consolidating. Direct Consolidation Loans are discussed in Chapter 11.

The amount eligible for consolidation under either program is the sum of the unpaid principal, accrued unpaid interest, late charges, and outstanding collection costs. For the purpose of consolidating a loan made under the Perkins Loan Program, a borrower is considered to have made satisfactory repayment arrangements on a defaulted loan under either of the consolidation programs by making three consecutive monthly payments on time. A defaulted loan that is being repaid under a **court order** remains in default status until paid and is not eligible for consolidation.

## LITIGATION

If the collection procedures described in this section do not result in the repayment of a loan, the school must determine at least once a year whether all the conditions listed below are met. If so, the school must litigate. The conditions are

**HEA Section 484A(a)**

- ◊ the total amount owed, including outstanding principal, interest, collection costs, and late charges, on all the borrower's Perkins Loans and NDSLs at the school is more than $200;
- ◊ the borrower can be located and served with process;
- ◊ the borrower either has enough assets attachable under state law to cover a major portion of the debt or enough income that can be garnished under state law to satisfy a major portion of the debt over a reasonable period of time;[1]
- ◊ the borrower does not have a defense that will bar judgment for the school;[2] and
- ◊ the expected cost of litigation (including attorneys' fees) does not exceed the amount that can be recovered from the borrower.

Even if all the above conditions are **not** met, the school may sue if it chooses to do so. No federal or state statute of limitation can apply to enforcement actions to collect Perkins Loans or NDSLs.

The school must attempt to recover from the borrower all litigation costs, including attorneys' fees, court costs, and other related costs, to the extent permitted by applicable state law. The school is also required to try to recover all costs previously incurred in the collection of overdue payments if these collection costs have not been paid by the borrower; a percentage of these unrecovered costs may be charged to the fund as explained below.

**Assignment of amount of $25 or more**

If the school cannot collect a payment after following all collection procedures (including litigation, if required), it may, with the Secretary's approval, assign the account to the Department for collection. A school may assign a loan to the Department for collection if the amount outstanding is **$25 or more**, including principal, interest, collection costs, and late charges.

[1] Defining "a reasonable period of time" is left to the school.

[2] If the school determines that the borrower has a partial defense, it must weigh the costs of litigation against the costs of recovery based on the amount of the enforceable portion of the debt.

If the school has a cohort default rate of more than 20% as of June 30 two years before the school submits an assignment request, the school must provide documentation to the Department that it has complied with all of the due diligence requirements discussed in this chapter.

### *DEPOSIT OF FUNDS COLLECTED*

A school must deposit any funds collected into an interest-bearing bank account. A collection agency, collection attorney, or loan servicer is required to deposit funds collected into an interest-bearing account only if the agency, attorney or servicer holds such amounts for more than 45 days. The account must be insured by an agency of the federal government, secured by collateral of reasonably equivalent value, or invested in low-risk income-producing securities, such as obligations issued or guaranteed by the United States.

A school may deduct from the interest earned any bank charges incurred as a result of maintaining the fund assets in an interest-bearing account, such as service charges, and deposit only the net earnings into the fund.

### *COSTS CHARGEABLE TO THE FEDERAL PERKINS LOAN FUND*

The following costs of actions a school takes in an attempt to collect past-due payments on a loan must be charged to the borrower: billing costs associated with past-due payments (not routine billing costs) and costs of address searches, collection, litigation, the use of contractors, and bankruptcy litigation.

***Billing costs for past-due payments sometimes chargeable***

The only **billing costs** a school may charge the fund are the costs of telephone calls made to demand payment of overdue amounts not paid by the borrower. If the amount recovered from the borrower does not suffice to pay the amount of the past-due payments and the penalty or late charges, the school may charge the fund for only the unpaid portion of the actual cost of the calls.

Only the collection costs discussed below that are **waived or not paid by the borrower** may be charged to the Perkins Loan fund:

- ◊ **Collection costs waived**. As stated earlier, a school may waive all collection costs on a loan if the borrower, within 30days of entering into a new repayment agreement, makes a lump-sum payment of the entire amount outstanding or may waive a percentage of the collection costs equal to the percentage the borrower pays on the amount outstanding on the loan within 30days of entering a new repayment agreement. The amount waived may be charged to the fund.

◊ **Cost of a successful address search**. A reasonable amount for the cost of a successful address search, if not paid by the borrower, may be charged to the fund provided that the school either used a commercial skip-trace service or its own personnel, employing methods comparable to commercial skip-tracing practices. Defining a reasonable amount is left to the school.

◊ **Cost of reporting defaulted loans to credit bureaus**. The following costs not paid by the borrower may be charged to the fund: the cost of reporting a defaulted loan to a credit bureau, reporting any change in the status of a defaulted account to the bureau to which the school had previously reported the account, and responding to any inquiry from a credit bureau about the status of a loan.

◊ **Collection costs**. Collection costs not paid by the borrower may be charged to the fund if they do not exceed—for first collection efforts—30% of the total principal, interest, and late charges collected and—for second collection efforts—40% of the principal, interest, and late charges collected. The school must reimburse the fund for collection costs initially charged the fund but subsequently paid by the borrower.

◊ **Collection costs resulting from litigation, including attorney's fees**. Collection costs resulting from litigation, including attorney's fees, may be charged to the fund if not paid by the borrower, but must not exceed the sum of

- court costs specified in 28 U.S.C. 1920;
- other costs incurred in bankruptcy proceedings in taking actions required or authorized under 34CFR 674.49;
- costs of other actions in bankruptcy proceedings to the extent that those costs together with other costs incurred in bankruptcy proceedings do not exceed 40% of the total amount of judgment obtained on the loan; and
- 40% of the total amount recovered from the borrower in any other proceeding.

◊ **Costs of firm performing both collection and litigation services**. If a collection firm agrees to perform or obtain the performance of both collection and litigation services on a loan, the amount for both functions that may be charged to the fund may not exceed the sum of **40%** of the amount of principal, interest, and late charges collected on the loan, plus court costs specified in 28 U.S.C. 1920.

***Documentation of costs charged to the fund***

For audit purposes, a school must support costs charged to the fund with appropriate documentation including telephone bills and receipts from collection firms. Due diligence activities involving **fixed costs** (telephone contacts, credit bureau reporting, and bankruptcy procedures) may be charged to the fund whether or not the actions are successful. Other activities, such as address searches, collection, and litigation (other than bankruptcy), are typically performed on a **contingent-fee** basis; if these activities are successful, the school may charge the fund for the costs associated with them under the conditions stated previously. Because the school incurs no costs if these activities are not successful, it may not charge the fund for them unless they are successful.

As stated earlier, a school may write off a student's account if the total amount owed on the account is less than $5.00. "Total amount owed" means outstanding principal, accrued interest, collection costs, and late charges. If the school writes off an account, it no longer includes it as an asset of the fund. If the school receives a repayment from the borrower after the loan has been written off, the school must deposit it into the fund.

## *USING BILLING AND COLLECTION FIRMS*

The school may use a contractor for billing or collection, but the school is still responsible for complying with the Subpart C regulations regarding those activities. For example, the school, not the billing or collection firm, is responsible for deciding whether to sue a borrower in default. The school is also responsible for decisions about canceling, postponing, or deferring repayment, granting forbearance, extending the repayment period, and safeguarding the funds collected.

A school using a billing service may not use a collection firm that owns or controls the billing service or is owned or controlled by the billing service. In addition, a school may not use a collection firm if both the collection firm and billing service are owned or controlled by the same corporation, partnership, association, or individual.

***Quarterly activities statement***

A school using either a billing service or a collection firm must ensure that the service or firm issues, at least quarterly, a statement showing the activities for each borrower, such as amounts collected or changes in the borrower's name, address, telephone number, or Social Security Number, if known. The service or firm must also give the school, at least quarterly, a list of charges for skip-tracing activities and telephone calls.

The school must also ensure that the billing service or collection firm instructs the borrower either to mail payment checks to the school directly or to a bank where a lock-box is maintained for the school. Alternatively, the service or firm may deposit the funds into an interest-bearing institutional trust account.

If a billing service or a collection firm is depositing funds received directly from the borrower into an institutional trust account, this institutional trust account must be an interest-bearing account if those funds will be held for longer than 45 days. A billing service is not permitted to deduct its fees before depositing the amount it receives from borrowers. A collection firm may deduct its fees before depositing the funds it receives from borrowers if the school authorizes it to do so.

The firm may commingle in its accounts the funds collected as long as it can identify the interest earnings and the amount collected by the institution. If a **collection** firm chooses this last procedure, it may, **if the school authorizes it,** deduct its fees before depositing the amount collected. A **billing** service may **not** deduct its fees from the amount it receives from borrowers.

***Fidelity bond or comparable insurance***

Just as schools are required to keep adequate fidelity bond coverage to protect the government's interest in the Student Financial Assistance (SFA) funds they receive, it is appropriate to ensure the same sort of protection from third parties who handle Perkins Loan Program funds for the school. Accordingly, a school must ensure that its billing service and collection firm maintain a fidelity bond or comparable insurance to protect the accounts they service. Billing services (and **collection firms not authorized to deduct their fees** from borrowers' payments) must be bonded or insured in an amount not less than the amount of funds the school expects to be repaid in a two-month period on the accounts it refers.

***Larger bond for collection firm that deducts fees***

Collection firms authorized to deduct their fees from borrowers' payments must be bonded or insured:

1. If the amount the school expects to be repaid in a two-month period is **less than $100,000**, the collection firm must be bonded or insured in one of the following amounts, whichever is **less:**

    - 10 times the amount the school expects to be repaid on accounts it refers to the firm during a two-month period **or**

    - the amount the firm expects to collect in a two-month period on **all** accounts it has in its portfolio (not just the school's accounts).

2. If the amount the school expects to be repaid in a two-month period is **$100,000 or more**, the collection firm must be bonded or insured in an amount not less than the amount of funds the school can reasonably expect to be repaid during that two-month period. **The bond or insurance must name the school as beneficiary**. (This is not a requirement when the payments expected in a two-month period are less than $100,000.)

The school must review annually the amount of repayments it expects to receive from billing or collection firms to ensure adequate bond or insurance coverage.

***Law firm as collection firm***

A school using a law firm to collect must review the firm's bond or its insurance policy to determine whether the firm is protected against employee misappropriation. If the firm's malpractice insurance also covers misappropriation of funds, that policy is considered to provide coverage.

# Default

Default in the Federal Perkins Loan Program is defined as "the failure of a borrower to make an installment payment when due or to comply with other terms of the promissory note or written repayment agreement." Schools are required to comply with the due diligence regulations in regard to notifying the borrower about payments due or overdue, billing procedures, and collection procedures before resorting to litigation. Due diligence procedures are discussed in Sections 6 and 7 of this chapter.

***Definition of default***

A school must report a defaulted loan account to a national credit bureau organization with which the U.S. Department of Education has an agreement. A school must also report any change in account status to the same national credit bureau to which it originally reported the default, according to the reporting procedures of the credit bureau. If the school receives an inquiry from any credit bureau about the information reported on the loan, the school must respond to the inquiry within one month of its receipt.

***Report to credit bureau***

The debtor has the right to appeal the accuracy and validity of information reported to the credit bureau. For more information about reporting Perkins Loans or National Direct Student Loans (NDSLs) to a national credit bureau, see Section 10, "Credit Bureau Reporting."

A borrower who has made "satisfactory arrangements to repay" a defaulted loan reestablishes his or her eligibility to apply for federal student aid. However, the loan is still considered to be in default and will continue to be reported as defaulted to a national credit bureau organization with which the Department has an agreement. The term "satisfactory arrangements to repay" is defined as the "establishment of a new written repayment agreement and the making of one payment each month for six consecutive months." If a borrower has made satisfactory arrangements to repay a defaulted loan prior to the end of the cohort period and if the loan entered repayment during the cohort period, the loan is not included as a defaulted loan in calculating the school's cohort default rate.

***Default Reduction Assistance Project (DRAP)—"Dear Colleague" Letter CB-94-7***

To assist schools in bringing defaulted borrowers into repayment, the Department has established the Default Reduction Assistance Project (DRAP). Under DRAP, a school can request that the Department send a borrower any of three letters designed to warn the student of the seriousness of default. The Department provides these services at no cost to the school. Participation in DRAP is voluntary. General questions about DRAP should be directed to the Campus-Based Programs Systems Division. The telephone number is (202) 708-6726. As DRAP is intended to get the borrower back into repayment **before** the account goes to a collection firm, this service should **not** be requested once a collection agency is involved. DRAP service is usually provided during the 30-day period during which a school is awaiting response to the final demand letter.

***SkipTracing and the Safeguard Activity Report—CB-96-15 (LD), July 1996***

Although schools are no longer required to use the IRS/ED skip-tracing service for carrying out the due diligence provisions of the Perkins Loan Program, the Department strongly encourages schools to continue to use this service. The IRS/ED skip-tracing service is one of the most powerful tools available to schools for locating defaulted borrowers. In order to maintain eligibility to participate in the in the IRS/ED Skiptracing Service, each school that participates must submit an annual Safeguard Activity Report in accordance with IRS Publication 1075. If a school fails to submit the report, it will lose its eligibility to participate in the service. "Dear Colleague" letter CB-96-15 (LD), dated July 1996, included instructions for completing the report that was due by August 31, 1996. The reports help ensure that procedures are established and utilized to safeguard the names and addresses of defaulted borrowers under the Perkins Loan Program. General questions should be directed to the Department's Program Systems Service, Campus-Based Programs Systems Division. The telephone number is (202) 708-6726.

## *COMPROMISE OF REPAYMENT OF DEFAULTED LOAN*

To encourage repayment, a school may compromise on the repayment of a defaulted loan if the school has fully complied with all due diligence requirements discussed in Section 6 of this chapter and if the borrower pays in a single lump-sum payment

◊ 90% of the outstanding principal balance on the loan;

◊ the interest due on the loan; and

◊ any collection fees due on the loan.

The federal share of the compromise repayment must bear the same relation to the school's share of the compromise repayment as the Federal

Capital Contribution (FCC) bears to the Institutional Capital Contribution (ICC).

## *PENALTY FOR SCHOOLS WITH HIGH COHORT DEFAULT RATES*

If a school's cohort default rate meets the following levels, a default penalty is imposed on the school, as described below:

- ◊ If a school's cohort default rate equals or exceeds 15%, it must establish a default reduction plan;
- ◊ If the school's cohort default rate is greater than 15%, it may not participate in the Expanded Lending Option (ELO);
- ◊ If the school's cohort default rate equals or exceeds 20% but is less than 25%, the school's FCC will be reduced by 10%;
- ◊ If the school's cohort default rate equals or exceeds 25% but is less than 30%, the school's FCC will be reduced by 30%;
- ◊ If the school's cohort default rate equals or exceeds 30%, the school's FCC will be reduced to zero.

## *CALCULATING A SCHOOL'S COHORT DEFAULT RATE*

A school's cohort default rate is calculated for a particular year based on information the school provides on the annual Fiscal Operations Report.

***Definition of "cohort default rate"***

The term "cohort default rate" means (for any award year in which 30 or more current and former students at the school enter repayment on a loan received for attendance at that school) the percentage of those current and former students who enter repayment in that award year on the loans received for attendance at that school and who default before the end of the following award year.

For any award year in which **less** than 30 current and former students at the school enter repayment on a loan received at the school, "cohort default rate" means the percentage of those current and former students who entered repayment on loans received for attendance at that school in any of the **three** most recent award years and who defaulted on those loans before the end of the award year immediately following the year in which they entered repayment.

Each school's 1997-98 *Fiscal Operations Report and Application to Participate* (FISAP) lists the cohort default rate that affects the school for the 1997-98 award year. We will refer to that rate as the school's current cohort default

**Denominator of formula**

**Numerator of formula**

rate. This rate (for schools with at least 30 borrowers entering repayment each year) was calculated by computing the number of borrowers who entered repayment between July 1, 1994 and June 30, 1995. For purposes of the cohort default rate, a loan enters repayment only once in its life. This repayment begins the day after the end of the initial grace period or the day that the borrower waives his or her initial grace period.

The denominator in the calculation is the number of borrowers entering repayment during the specified award year (1994-95 for the 1997-98 FISAP). In calculating the default rate, each loan is attributed only to the school that made the loan.

The numerator in the calculation is the number of people in the denominator who were in default as of the end of the following award year. In calculating a school's current cohort default rate, the numerator is the number of people in the denominator who were in default at the end of the 1995-96 award year (June 30, 1996). For purposes of that calculation, as of June 30, 1996, a borrower must have been in default for at least 240 consecutive days for monthly payments or 270 consecutive days for other installments. Even if the school had paid off the loan, the borrower still had to be included in this calculation. However, borrowers who had made satisfactory arrangements to repay the loan could be excluded from the numerator.

## *DEFAULTED LOANS INCLUDED IN A SCHOOL'S COHORT DEFAULT RATE*

The criteria listed below determine which defaulted loans must be included in the formula to determine a school's cohort default rate:

◊ A borrower must be included in determining the school's cohort default rate if the borrower's default has persisted for at least 240 consecutive days for a loan repayable monthly or 270 consecutive days for a loan repayable quarterly.[1] This borrower must be included regardless of the loan's status on June30 of the second year of the cohort period.

- For example, if a borrower's loan is in default for at least 240/270 consecutive days and an authorized period of deferment begins after the 239th day past due, the loan would be counted as a default in the school's cohort default rate even if the loan is in a deferred status on June 30.

---

[1]Once the loan is 240/270 days delinquent, bringing the defaulted loan to less than 240/270 days delinquent or even bringing it current will not eliminate the loan from the cohort default rate.

Once the loan is 240/270 days past due, bringing it below 240/270 days past due or even bringing it current will not eliminate the loan from the cohort default rate. Because a borrower is not billed during an authorized period of deferment, the delinquency would not increase during the deferment.

***School makes payment***

◊ A loan is considered to still be in default if the school, its owner, agency, contractor, employee, or any other entity or individual affiliated with the school makes a payment to prevent the borrower from defaulting.

***Borrower pays loan in full***

◊ If a borrower pays a past-due loan in full, the loan will not be included in the school's cohort default rate.

***Satisfactory repayment arrangements***

◊ A loan that is in default but on which the borrower has made satisfactory repayment arrangements is **not** considered to be in default for the purpose of determining a school's cohort default rate.

***Borrower with loans from multiple schools***

◊ In the case of a student who has attended and borrowed at more than one school, the student and his or her subsequent repay– ment or default are attributed to the school where the student received the loan that entered repayment in the award year.

***Loan assigned to the Department***

◊ A defaulted loan that has been assigned to the Department is counted in determining a school's cohort default rate if the loan entered repayment during the appropriate time period. Assignments of loans to the Department no longer lower a school's default rate. In addition, the status of a loan that has been assigned to the Department is still considered in default until the loan is paid in full, even if the borrower has made satisfactory arrangements to repay the defaulted loan in order to qualify for additional aid from Student Financial Assistance (SFA) programs.

***Retroactive forbearance***

◊ A loan that is 24 days or more past due but on which the school has granted a retroactive forbearance (after providing the necessary documentation to the school) is considered to be in default only for the purpose of determining a school's cohort default rate. The loan is not considered to be in default for the purpose of determining the borrower's eligibility for additional SFA funds.

## RULES FOR CALCULATING THE NUMBER OF DAYS IN DEFAULT

The following rules are used in calculating the number of days a loan has been in default.

◊ The 240/270 consecutive days in default is determined by calculating the "age" of the account (that is, the number of consecutive days the oldest dollar is past due).

◊ A payment that a borrower makes on a past-due loan is applied to the oldest dollars first, effectively reducing the past-due status.

- For example, suppose a borrower's monthly payment amount is $50. The borrower has made no payments for 5 months, making the loan 150 days past due. The borrower then makes one $50 payment. The school applies the payment to cover the first month's payment that was overdue, reducing the loan's past-due status from 150 days to 120 days because the earliest past-due payment is now 4 months old. The calculation of the number of days overdue begins with the oldest dollar past due.

◊ A loan on which a borrower is past due and on which the borrower makes an occasional payment but never becomes current could be counted as a defaulted loan for the cohort default rate calculation despite the occasional payments. Because the delinquency is not being cured, the oldest past-due dollar could eventually become 240 days past due, making the loan count in the cohort default rate calculation. However, if the borrower makes enough occasional payments to prevent the oldest past-due dollar from becoming 240 days old, the loan would not be included in the cohort default rate calculation.

- For example, let's use the same scenario as the example above. The borrower's oldest dollar is 120 days past due. The borrower does not make any additional payments for 90 days, making the oldest dollar 210 days past due. The borrower then makes a $50 payment, reducing the past-due status to 180 days. Another 60 days elapse without the borrower making a payment, bringing the oldest dollar to 240 days past due. At that point, the loan would be counted in the school's cohort default rate even if subsequent payments reduce the past-due status to less than 240 days.

◊ An exception to the 240/270-day threshold will be granted in a case where a borrower

1. would have qualified for a deferment for a period beginning prior to the loan hitting the 240/270-day threshold and

2. failed to file a request for the deferment in a timely manner.

For such a borrower, the loan's past-due status would be adjusted to reflect the deferment period beginning date. However, note that the borrower would need to pay any past-due amounts that were due prior to the beginning of the authorized deferment periods, if the deferment period beginning date does not eliminate the loan's entire delinquency.

- Using the earlier example, the oldest dollar of the loan is 240 days past due. The borrower files a request for a deferment based on the fact that he or she is attending school and the enrollment period began on the date that the loan became 90 days past due. The past-due status of the loan is reduced to 90 days, and the loan is given a deferment status. This loan is treated as if the 240-day threshold had never been reached. Therefore, it would not be counted in the school's cohort default rate.

## *COHORT DEFAULT RATE FOR A SCHOOL WITH MORE THAN ONE LOCATION*

If a school has a branch or branches or has an additional location or locations, the school's cohort default rate applies to all branches and locations of the school as they exist on the first day of the award year for which the rate is calculated. The cohort default rate applies to all branches/locations of the school from the date the Department notifies the school of the rate until the Department notifies the school that the rate no longer applies.

***Change from branch to freestanding school***

If a school changes status from a branch of one school to a freestanding or independent school, the Department determines the cohort default rate based on the school's status as of July 1 of the award year for which the rate is being calculated.

***Cohort default rate of schools that merge***

If an independent school becomes a branch of another school or merges with another independent school, the Department determines the cohort default rate based on the combined number of students from both schools who enter repayment during the applicable award year and the combined number of students from both schools who default during the applicable award years. The new rate applies to the new consolidated school and all of its current locations.

**_Branch moves to another school_**

If a school changes status from a branch of one school to a branch of another school, the Department determines the cohort default rate based on the combined number of students from both schools who enter repayment during the applicable award year and the combined number of students from both schools who default during the applicable award years from both schools in their entirety.

**_Ownership changes_**

If a school has a change in ownership that results in a change in control, the Department determines the cohort default rate based on the combined number of students who enter repayment during the applicable award year and the combined number of students who default during the applicable award years at the school under both the old and new control.

## *DEFAULT REDUCTION PLAN*

Any school with a cohort default rate that equals or exceeds 15% must establish and implement a plan designed to reduce defaults by its students in the future. The school must submit to the Department by December 31 of the calendar year in which the cohort default rate was calculated

- ◊ a written description of the default reduction plan;
- ◊ a statement indicating that the school agrees to comply with the required measures listed in the following paragraph; or
- ◊ if the school already has a default reduction plan under the Federal Family Education Loan (FFEL) Program, a statement that the school agrees to apply that plan to the Perkins Loan Program.

A school's default reduction plan must include the measures listed below and a description of the measures the school will take to reduce defaults. The school must explain how it plans to

1. revise admission policies and screening practices, consistent with applicable state law, to ensure that students enrolled in the institution, especially those who are not high school graduates or those who are in need of substantial remedial work, have a reasonable expectation of succeeding in their programs of study;
2. improve the availability and effectiveness of academic counseling and other support services to decrease withdrawal rates, including
   - providing academic counseling and other support services to students on a regular basis, at a time and location that is convenient for the students involved;

- publicizing the availability of the academic counseling and other support services;
- establishing procedures to identify academically high-risk students and schedule those students for immediate counseling services; and
- maintaining records identifying those students who receive academic counseling;

3. attempt to reduce its withdrawal rate by conforming with its accrediting agency's standards of satisfactory progress and with those described in 34CFR 668.34 and improving its curricula, facilities, materials, equipment, qualifications and size of faculty, and other aspects of its educational program in consultation with its academic accrediting agency;
4. increase the frequency of reviews of in-school status of borrowers to ensure the institution's prompt recognition of instances in which borrowers withdraw without notice to the institution—reviews must be conducted each month;
5. expand its job placement program for its students by
   - increasing contacts with local employers, counseling students in job search skills;
   - exploring with local employers the feasibility of establishing internship and cooperative education programs;
   - attempting to improve its job placement rate and licensing examination pass rate by improving its curricula, facilities, materials, equipment, qualifications and size of faculty, and other aspects of its educational program in consultation with the cognizant accrediting body; and
   - establishing a liaison for job information and placement assistance with the local office of the United States Employment Service and the Private Industry Council supported by the U.S. Department of Labor.
6. remind the borrower of the importance of the repayment obligation and of the consequences of default, and update the institution's records regarding the borrower's employer and employer's address as part of the contacts with the borrower under 34CFR 674.42(b);

7. obtain from the borrower, at the time of a borrower's admission to the institution, information regarding references and family members beyond those provided on the loan application, in order to provide the institution or its agent with a variety of ways to locate a borrower who later relocates without notifying the institution;

8. explain to a prospective student that the student's dissatisfaction with, or nonreceipt of, the educational services being offered by the institution does not excuse the borrower from repayment of any Perkins Loan;

9. use a written test and intensive additional counseling for those borrowers who fail the test to ensure the borrower's comprehension of the terms and conditions of the loan including those described in 674.16 and 674.42(a) as part of the initial loan counseling and the exit interview;

10. during the exit interview provided to a borrower

    - explain the use by institutions of outside contractors to service and collect loans;

    - provide general information on budgeting of living expenses and other aspects of personal financial management; and

    - provide guidance on the preparation of correspondence to the borrower's institution or agent and completion of deferment and cancellation forms;

11. use available audio-visual materials such as videos and films to enhance the effectiveness of the initial and exit counseling;

12. conduct an annual comprehensive self-evaluation of its administration of the Title IV programs to identify institutional practices that should be modified to reduce defaults, and then implement those modifications;

13. delay loan disbursements to first-time borrowers for 30 days after enrollment; and

14. require first-time borrowers to endorse their loan checks at the institution and to pick up at the institution any loan proceeds remaining after deduction of institutional charges.

Procedures for submitting assignment of defaulted Perkins, NDSLs, or Defense Loans were discussed in Dear Colleague letter CB-95-13, dated June 1995 with a correction page provided in Dear Colleague letter CB-95-22, dated September 1995.

***Assignment conditions***

A school may assign a defaulted Perkins Loan or NDSL to the Department if

- ◊ the school has not been able to collect despite having followed due diligence procedures, including at least a first level of collection and litigation, if required by the regulations in effect on the date the loan entered default;
- ◊ the total amount of the borrower's account to be assigned, including outstanding principal, accrued interest, collection costs, and late charges, is $25 or more; and
- ◊ the loan has been accelerated.

A promissory note may be assigned only during the submission period established by the Department.

***Documents required for assignment***

A school must submit the following documents to the Department for any loan it proposes to assign:

1. an assignment form—ED Form 553, provided by the Department and completed by the school, which must include a certification by the school that it has complied with the due diligence procedures discussed in Sections 6 and7 of this chapter, including at least a first level collection effort;
2. the original promissory note or a certified copy of the original note;
3. a copy of the repayment schedule;
4. a certified copy of any judgment order entered on the loan;
5. one photocopy of completed ED Form 553;
6. a complete statement of the repayment history;
7. copies of all approved requests for deferment and cancellation;

8. a copy of the notice to the borrower of the effective date of acceleration and the total amount due on the loan;

9. documentation that the school has withdrawn the loan from any firm that it employed for address search, billing, collection or litigation services and has notified that firm to cease collection activity on the loans;

10. copies of all pleadings filed or received by the institution on behalf of a borrower who has filed a petition in bankruptcy and whose loan obligation is determined to be nondischargeable; and

11. documentation that the institution has complied with all of the due diligence requirements if the school has a cohort default rate that is equal to or greater than 20% as of June 30 of the second year preceding the submission period.

***Limitations on assignment***

The Department will not accept assignment of a loan if

◊ the school has not included the borrower's Social Security Number;

◊ the borrower has received a discharge in bankruptcy—unless the bankruptcy court has determined that the loan obligation is nondischargeable and has entered a judgment against the borrower or unless a court of competent jurisdiction has entered judgment against the borrower on the loan after the entry of the discharge order;

◊ the school has sued the borrower unless the judgment has been entered and assigned to the United States; or

◊ the loan has been canceled because the borrower has died or because the borrower has filed for, or been granted, cancellation due to permanent and total disability.

Assignments should be mailed to:

U.S. Department of Education
Perkins Loan Assignment
Processing Center
P.O. Box 4136
Greenville, TX 75403-4136

If the Department accepts the assignment of a loan, it will give the school written notice to that effect. **By accepting the assignment, the Department acquires all rights, title, and interest in the loan.** After the Department has

accepted the assignment of the loan, the school must endorse and forward to the Department any subsequent payment(s) the borrower may make.

If the Department later determines an assigned loan to be unenforceable because of an act or omission on the part of the school or its agent, the school will have to compensate the Perkins Loan Fund in the amount of the unenforceable portion of the outstanding balance. Once the fund is reimbursed, the Department transfers all rights to the loan back to the school.

A school must consider a borrower whose loan has been assigned to the United States for collection to be in default on the loan for the purpose of eligibility for assistance from SFA programs until the borrower provides the school with confirmation from the Department that he or she has made satisfactory arrangements to repay the loan.

## DEFAULT PREVENTION SOFTWARE

The Department's computer software, called Institutional Default Prevention System (IDPS), is available free of charge to schools participating in our federal student aid programs. IDPS is a valuable tool for default prevention and reduction. To use IDPS, a school needs an IBM-compatible personal computer with at least 640K memory, MS-DOS (version 2.1 or newer), a hard disk (10 Megabytes or larger), and a printer. Dear Colleague letter92-S-67, September 1992, included a description of the software and an order sheet. Questions about IDPS should be addressed to:

**IDPS computer software**

Attn: IDPS Software Distribution
U.S. Department of Education
7th and D Streets, S.W., ROB-3, Room 5012
Washington, D.C. 20202

Contact: Gail Gurley
Telephone Number: 202/708-8834

## DEFAULT AND STUDENT ELIGIBILITY

Regulations specify that, to be eligible to receive assistance under the SFA programs, a student must not be in default and must **certify** that he or she is not in default on any SFA loan. This certification is found on the 1996-97 *Free Application for Federal Student Aid* (FAFSA). Prior to the 1996-97 award year, the certification was on the *Student Aid Report* (SAR). However, the regulations also provide an exception to the above rule. A student who is in default on a loan made under the Perkins Loan Program (a Perkins Loan,

NDSL, or Defense loan) is eligible to receive assistance under an SFA program if the student is otherwise eligible and he or she:

◊ repays the loan in full or

◊ makes arrangements that are satisfactory to the holder of the loan to repay the loan balance and makes at least six consecutive monthly payments on time under these arrangements.

The term "satisfactory arrangements to repay" is defined as the establishment of a new written repayment agreement and the making of one payment each month for six consecutive months.

A student who is in default but has made satisfactory arrangements to repay the loan will receive a comment on his or her SAR that says

> "WARNING: Our records indicate that you are in DEFAULT on a federal student loan held by the U.S. Department of Education [or a state guaranty agency]. Since you have made satisfactory arrangements to repay this loan, you may be eligible to receive additional federal student aid at this time. However, if you fail to make scheduled payments, you will be denied future federal student aid."

***Willingness to repay***

When a school has filed suit to collect a defaulted Perkins Loan or NDSL and a judgment has been rendered on the loan, the borrower is obligated to repay only the amount of the judgment obtained on the loan. After a judgment is satisfied on the defaulted loan, the student is again eligible for future awards under these programs if all other eligibility criteria are met. However, if a judgment is satisfied **involuntarily** (such as by garnishing the borrower's wages), a school should consider this as evidence of unwillingness to repay and should deny further loan assistance to the borrower.

***Bankruptcy***

Note that an SFA loan that is discharged in bankruptcy is not considered to be in default for the purpose of obtaining further grant or work assistance under the SFA programs. It is no longer a requirement that a borrower reaffirm a loan discharged in bankruptcy in order to be eligible to obtain additional student loans; this change is a result of the Bankruptcy Amendments Act of 1994, effective October 22, 1994. (Refer to Section 9 of this chapter.)

***Loan consolidation***

As stated earlier, the FFEL and Direct Loan Program regulations allow a borrower to receive a Consolidation Loan that could include a defaulted Perkins Loan. See Section7 for more information. A defaulted loan that is being repaid under a **court order** would remain in default status until paid and is not eligible for consolidation.

# Bankruptcy

The basic actions a school must take when a borrower files for bankruptcy protection are covered her, in “Dear Colleague” Letter GEN-95-40, dated September 1995, and in 34CFR 674.49. For the best advice on how to proceed when a borrower files for bankruptcy protection, a school should consult its attorney.

***Stop collection outside bankruptcy proceedings***

If a school receives notice that a borrower has filed for bankruptcy protection, it must immediately stop collection efforts (outside the bankruptcy proceeding itself). If the borrower has filed under Chapter 12 or13 of the Bankruptcy Code, the school must also suspend collection efforts against any endorser for loans made prior to July 23, 1992. The school must file a proof of claim in the bankruptcy proceeding unless, in the case of a proceeding under Chapter7 of the Bankruptcy Code, the notice of meeting of creditors states the borrower has no assets.

Provisions of the Crime Control Act of 1990 extended from 5years to 7years the period of time a loan must be in repayment before it can be discharged under chapter 7, 11, 12, or 13 of the Bankruptcy Code and provided that a Student Financial Assistance (SFA) loan is dischargeable during that same 7-year period only if the borrower proves that repayment would constitute an undue hardship. The regulations also reflect the changes made to the Bankruptcy Code by section 3007 of the Omnibus Budget Reconciliation Act of 1990; the regulations provide that a discharge under 1328(a) of the Bankruptcy Code does not discharge an education loan unless the loan entered the repayment period more than 7years, excluding periods of deferment and forbearance, before the filing of the petition.

## *WHEN BORROWER REQUESTS DISCHARGE BASED ON UNDUE HARDSHIP*

If a borrower files for bankruptcy protection requesting discharge of a loan on the ground of undue hardship under Chapter 7, 11, 12, or 13 of the Bankruptcy Code, or under 11 U.S.C. 1328(b), the school must follow the procedures discussed on the next page.

If the loan has been **in repayment for 7 years or more** (excluding deferment and forbearance periods), the school may **not** oppose a discharge that has been requested on the ground of undue hardship.

If the loan has been **in repayment for less than 7 years**, the school must determine, on the basis of reasonably available information, whether repayment under the current repayment schedule or under any adjusted schedule would impose undue hardship on the borrower and his or her dependents. If this would not be the case, the school must then decide whether the expected costs of opposing the discharge would exceed one-third of the total amount owed on the loan (principal, interest, late charges, and collection costs). If the expected costs do not exceed one-third of the total amount owed on the loan, the school must oppose the discharge and, if the borrower is in default, seek a judgment for the amount owed. The school may compromise a portion of that amount, if necessary to obtain a judgment.

When a borrower has filed a request for discharge on the ground of undue hardship, if the school is required under the steps described above to oppose the borrower's request, the school may file a complaint with the court to obtain a determination that the loan is not dischargeable and to obtain a judgment on the loan.

## *PROCEDURES WHEN BORROWER REQUESTS ADJUSTMENT IN REPAYMENT*

Under Chapter 13, the borrower may request an adjustment in repayment terms. The borrower proposes a repayment plan, which is then ruled on by the bankruptcy court. If the borrower's repayment plan proposes full repayment of the loan, including all principal, interest, late charges and collection costs on the loan, no response from the school is required. The school is also not required to respond to a proposed repayment plan that does not include any provision in regard to the loan obligation or to general unsecured claims.

If the borrower proposes to repay less than the total amount owed, the school must determine, from its own records and court documents, the amount of the loan dischargeable under the plan. The school does this by subtracting the total proposed payments from the total amount owed. The school must also determine from its own records and court documents whether the borrower's proposed repayment plan meets the requirements of 11 U.S.C. 1325.[1] Two of those requirements are particularly relevant:

- ◊ First, the amount to be paid under the plan must at least equal the amount the school would receive if the debtor had filed under Chapter 7 rather than under Chapter 13.

[1] 11 U.S.C. 1307, 1325, and 1328(b) are laws applicable to bankruptcy cases in general, not just to Perkins Loan bankruptcy cases. 11 U.S.C. 1307 concerns the dismissal of a Chapter 13 case or the conversion of a case filed under Chapter 13 to a Chapter 7 proceeding. 11 U.S.C. 1325 concerns the confirmation by the court of a borrower's proposed repayment plan. 11 U.S.C. 1328(b) concerns the discharge of debts. A school should consult an attorney for the best advice in bankruptcy cases.

◊ Second, to pay creditors under the plan, the debtor must use all income not needed to support himself or herself and his or her dependents.

If the borrower's proposed repayment plan does not meet the requirements of 11 U.S.C. 1325, the school must object to the confirmation by the court of the proposed plan, unless the cost of this action will exceed one-third of the dischargeable loan debt; if the cost will exceed one-third of the dischargeable debt, the school is not required to take this action.

Also, when a borrower proposes to repay less than the total amount owed, the school must determine whether grounds exist under 11 U.S.C. 1307 (see footnote on previous page) for the school to move to have the Chapter 13 case either dismissed or converted to a Chapter 7 proceeding. Such grounds include a borrower's failure to (1) begin payments under the plan within the required time (usually 30 days from the date the plan is filed), (2) file a proposed plan in a timely manner, or (3) pay required court fees and charges. If the school determines that such grounds do exist, the school must move to dismiss or convert the Chapter 13 case to a Chapter 7 proceeding, unless the cost of this action will exceed one-third of the dischargeable loan debt.

After a borrower's proposed repayment plan is confirmed by the court, the school must monitor the borrower's compliance with the repayment plan. For a loan that entered repayment more than 7 years before the borrower filed for bankruptcy (excluding periods of deferment), if the school determines from its own records or court documents that the borrower either has not made the payments required under the plan or has filed for a hardship discharge under 11 U.S.C. 1328(b) (see footnote on previous page), the school must determine whether grounds exist under 11 U.S.C. 1307 to dismiss the case filed under Chapter 13 or to convert the Chapter 13 case to a Chapter 7 proceeding or whether the borrower is entitled to a hardship discharge. If grounds do exist under 11 U.S.C. 1307 to dismiss or convert a Chapter 13 case, the school must move to convert or dismiss the case. If a borrower has not demonstrated entitlement to a hardship discharge under 11 U.S.C. 1328(b), the school must oppose the hardship discharge request, unless the costs of these actions, when added to those already incurred, would exceed one-third of the dischargeable debt.

***Resuming billing and collection if loan is not discharged***

A school must resume billing and collection procedures after the borrower has received a discharge under 11 U.S.C. 1328(a) or U.S.C. 1328(b) unless (1) the court has found that repayment would impose an undue hardship or (2) the loan entered the repayment period more than 7 years before the filing of the petition and the borrower's plan made some provision regarding the borrower's loan obligation or general unsecured debts.

**_Agreement to repay loan discharged in bankruptcy no longer required_**

As stated earlier, a borrower is no longer required to establish eligibility for a new student loan by agreeing to repay a loan discharged in bankruptcy. As a result of the Bankruptcy Reform Act of 1994, effective October 22, 1994, a student may not be denied student financial assistance from SFA programs, including the Federal Perkins Loan Program, solely on the basis of a bankruptcy determination. If a student has filed for or received a discharge in bankruptcy, has had a student loan discharged in bankruptcy, or has not paid a student loan that has been determined by a court of law to be dischargeable in bankruptcy, the bankruptcy may be considered as evidence of an adverse credit history but cannot be the basis for denial of a future loan from the Perkins Loan Program or other student loan programs. However, schools may continue to consider the student's **post-**bankruptcy credit history in determining willingness to repay the loan.

# section 10 Credit Bureau Reporting

A promissory note for a Federal Perkins or National Direct Student Loan (NDSL) made by a school on or after July 23, 1992 must state that the school is required to disclose to any one national credit bureau the amount of the loan made to the borrower and that if the borrower defaults on the loan, the school must disclose that the borrower has defaulted, along with other relevant information, to the same national credit bureau to which it originally reported the loan.

***34CFR 674.31***

Before a school makes its first disbursement to a student, the school must provide the student with certain information, including a written statement indicating that the school must report any default on the loan to a national credit bureau. This statement may be on the written application material, on the promissory note, or on a separate written form.

***Provide default information to student***

At the time each disbursement is made, the school must report to any one national credit bureau with which the U.S. Department of Education has an agreement the amount of the disbursement, the date the disbursement was made, and the balance outstanding on the loan.

***Report disbursement to credit bureau***

The Department has entered into an agreement with each of the four national credit bureaus listed below. In order to comply with the credit-bureau reporting requirement, schools should enter into an agreement with any of the following national credit bureaus:

***Credit bureaus with which the Department has agreements***

| Bureau | Telephone |
| --- | --- |
| Trans Union: contact Jeff Bugajski | 312/466-7862 |
| Experience (formerly TRW): contact "Customer Service" | 800/831-5614 Ext. 3 |
| CBI Equifax: ask for the telephone number of the CBI Equifax "territory" servicing your school | 770/740-4376 |
| Consumer Credit Association, Inc.: contact the Manager of Data Management Services | 713/589/1190 Ext. 2101 |

Each credit bureau charges a fee for its services. These fees differ from national credit bureau to national credit bureau. These bureaus also have affiliated credit bureaus, which may have different fees from those of the national credit bureaus. The Department does not keep a list of these affiliated bureaus and their fees. A school must obtain the Department's approval before using an affiliated credit bureau.

The cost associated with reporting Perkins Loan disbursements to a national credit bureau may not be charged against the Perkins Loan Fund. However, the school may use its administrative cost allowance to pay for these charges. Collection costs, which include the costs associated with reporting a defaulted Perkins Loan borrower to a national credit bureau, must be charged to the borrower. The fund can be charged for these costs only in relation to the amount collected from the bureau, as described in Section7 of this chapter.

***Disclosure of borrower's account information***

The Privacy Act authorizes disclosure of a borrower's account information to creditors without the borrower's consent if such a disclosure would help enforce the terms and conditions of the loan. This authorization permits the release of information concerning loans in both default and nondefault status, and the authorization applies whether the reporting takes place at the time the loan is being disbursed or at the time the loan is in default status. Reporting good credit history (as well as reporting defaulted loans) is essential to ensure that current and future creditors have complete information regarding the credit obligations of the borrower.

The Fair Credit Reporting Act allows a borrower/debtor to appeal the accuracy and validity of the information reported to the credit bureau and reflected in the credit report. The school should be aware of this right and should be prepared to handle and potentially accept the borrower's correction of information in accordance with the provisions of the act.

Section 11

# Program Funds

As discussed in Chapters 3 and 5, a school that wants to participate in any Student Financial Assistance (SFA) Program must sign a Program Participation Agreement with the Secretary. The agreement must be signed by the school official legally authorized to assume, on the school's behalf, the agreement's obligations.

For all of the SFA Programs, the agreement provides that the school must use the funds it receives solely for the purposes specified in the regulations for each program and requires the school to administer each program in accordance with the Higher Education Act of 1965 (HEA), as amended, and the Student Assistance General Provisions regulations. The agreement also requires the school to submit annually to the U.S. Department of Education a report containing information that will enable the Department to determine the school's cohort default rate (discussed in Section 8 of this chapter).

As discussed in the introduction to this chapter, the agreement for the Federal Perkins Loan Program also requires the school to establish and maintain a Perkins Loan fund (the fund) and to deposit into the fund—

◊ the federal capital contribution (FCC) the school receives as its federal allocation for the program for each award year (see the next page);

◊ the school's matching share—the institution's capital contribution (ICC), discussed on the next page;

◊ payments the school receives for repayment of loan principal, interest, collection charges, and penalty or late charges on loans from the fund;

◊ payments the school receives from the federal government for cancellations (such as teacher cancellations) of Perkins Loans and National Direct Student Loans (NDSLs) (see Section 5 of this chapter);

◊ any other earnings on fund assets, including net interest earnings on funds deposited in an interest-bearing account (total interest minus bank charges incurred on the account); and

◊ proceeds of any short-term no-interest loans the school makes to the fund in anticipation of receipt of its FCC or of loan collections.

As discussed in the introduction to this chapter, a school applies for program funds annually through the electronic *Fiscal Operations Report and Application to Participate* (FISAP). The Department allocates funds directly to schools. The allocation (FCC) for the Perkins Loan Program is the amount of funding the school is authorized to receive from the Department for an award year. This amount is based on the funds appropriated by Congress for the program, as well as the allocation formulas, which were established by law and which do not provide for appeals.

The provisions of the HEA and the Perkins Loan Program regulations that affect the amount of a school's allocation are also discussed in the introduction to this chapter.

## FISCAL PROCEDURES

***Cash management—34CFR 668.163***

Requirements for maintaining and accounting for SFA program funds are included in 34 CFR 668.163 of the cash management regulations published in the **Federal Register** November 29, 1996, effective July 1, 1997. The cash management requirements that apply in general to SFA programs (those in the General Provisions) are discussed in Chapter 3, Section 3. The cash management requirements specific to the campus-based programs (those in the Federal Work-Study [FWS], Federal Supplemental Educational Opportunity Grant [FSEOG], and Perkins Loan regulations) are discussed in Chapter 5, Section3. The cash management provisions that apply specifically to the Perkins Loan Program are discussed here.

The new cash management requirements that apply specifically to the Perkins Loan Program follow. (Section 11 of this chapter provides additional information on fiscal procedures and records.)

***Late disbursement—34CFR 668.164(g)***

◊ Regulations regarding the late disbursement of a Perkins Loan were removed from 34CFR 674.16 (g), and revised regulations are now in 34CFR 668.164(g), discussed in Section2 of this chapter.

***Maintaining funds***

◊ Under the provisions of 34CFR 668.163(c), a school must maintain the Perkins Loan Program Fund in an interest-bearing bank account or investment account consisting predominately

of low-risk, income-producing securities, such as obligations issued or guaranteed by the United States; interest or income earned on fund proceeds are retained by the school as part of the Perkins Loan Fund.

◊ If a school credits a student's account at the school with Perkins Loan funds, the school must notify the student of the date and amount of the disbursement, the student's right to cancel all or a portion of that loan and his or her right to have the funds returned to the school's Perkins fund; a detailed discussion of these provisions is in Chapter 5, Section 3.

***Notification of disbursement***

Schools must continue to follow the previously established fiscal procedures:

***Cash management requirements specific to the Perkins Loan Program 34CFR 674.19***

◊ A school must establish and maintain an internal control system of checks and balances that ensures that no office can both authorize payments and disburse Perkins Loan funds to students.

◊ A separate bank account for federal funds is not required, unless the school fails to comply with the requirements in the cash management regulations and program participation standards discussed in Chapter 3, Section 3.

◊ A school must notify any bank that federal funds are deposited in an account by ensuring that the name of the account clearly shows that federal funds are deposited in the account or notify the bank in writing of the name of the account and keep a copy of this notice in its files.

◊ The school must maintain sufficient liquidity in the Perkins Loan Fund to make required disbursements to students.

◊ A school must deposit its ICC into its fund prior to or at the same time it deposits any FCC

◊ A school must establish and maintain program and fiscal records that are reconciled at least monthly.

◊ Each year a school must submit a Fiscal Operations Report plus other information required by the Department; the school must ensure that the information reported is accurate and must submit it on the form and at the time the Department specifies.

## RECORDKEEPING REQUIREMENTS

New recordkeeping requirements for all SFA programs were published in the **Federal Register** (Part IX) November 27, 1996 and become effective July 1, 1997. Revised was 34 CFR 668.24, and amended was 34 CFR 674.19, which now states that a school must follow the recordkeeping requirements in the General Provisions and those in the Perkins Loan regulations. The recordkeeping requirements that apply in general to SFA programs (those in the General Provisions) are discussed in Chapter 3, Section 7. The recordkeeping requirements specific to the campus-based programs (those in the FWS, FSEOG, and Perkins Loan regulations) are discussed in Chapter 5, Section 3. Information on FWS payroll records is provided in Section 3 of this chapter.

A list of records a school must maintain for all SFA programs is provided in 34CFR 668.24(c) and discussed in detail in Chapter 3, Section 7. Perkins Loan records a school must maintain include but are not limited to

- ◊ the Student Aid Report (SAR) or Institutional Student Information Record (ISIR) used to determine a student's eligibility for a Perkins Loan;
- ◊ the student's application data and data submitted to the Department or the school on behalf of the student;
- ◊ documentation of each student's eligibility for a Perkins Loan;
- ◊ documentation of the amount of a Perkins Loan, its payment period, and the calculations used to determine the amount of the loan;
- ◊ documentation of the date and amount of each disbursement of Perkins Loan funds;
- ◊ documentation of the school's calculation of any refunds or overpayments due to or on behalf of the student and the amount, date, and basis of the school's calculation;
- ◊ documentation of the payment of any refund or overpayment to the SFA program fund or the Department;
- ◊ information collected at initial and exit loan counseling required by Perkins Loan regulations; and
- ◊ reports and forms used by the school in its participation in a campus-based program, and any records needed to verify data that appear in those reports and forms.

In addition to following the recordkeeping requirements mentioned in Chapters 3 and 5, a school must continue to follow the procedures previously established in 34CFR 674.19 for documentation of a student's Perkins Loan repayment history. The school must maintain a repayment history for each borrower that shows

◊ the date and amount of each repayment during the life of the loan;

◊ the amount of each repayment credited to principal, interest, collection costs, and either penalty or late charges;

◊ the date, nature, and result of each contact with the borrower (or endorser for loans made prior to July 23, 1992) in the collection of an overdue loan; and

◊ copies of all correspondence to or from the borrower (and endorser for loans made prior to July 23, 1992), except for bills, routine overdue notices, and routine form letters (demand letters, notices of intent to accelerate, and the like are not considered to be routine form letters).

A school must make its records readily available for review by the Department or its authorized representative at an institutional location designated by the Department or its representative.

***Records readily available for review—34CFR 668.24(d)***

Generally, a school must keep records relating to the school's administration of a campus-based program or the Federal Pell Grant Program for three years after the end of an award year for which the aid was awarded and disbursed under those programs. There are some exceptions to this requirement:

◊ The school must keep the *Fiscal Operations Report and Application to Participate* (FISAP) in the Perkins Loan, FSEOG, and FWS Programs, and any records necessary to support the data contained in the FISAP, including "income grid information," for three years after the end of the award year in which the FISAP is submitted.

***34CFR 668.24(e)(1)(i)***

◊ The school must keep repayment records for Perkins Loans, including records relating to cancellation and deferment requests for at least three years from the date a loan is assigned to the Department, canceled, or repaid.

***34CFR 674.19(e)(1)(ii)***

◊ Records questioned in an audit or program review must be kept until the questions are resolved or until the end of the retention period applicable to the records, whichever is later.

***34CFR 668.24(e)(3)***

For information on the formats in which a school must keep its campus-based program records, see Chapter 5, Section 3.