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Part VII

Department of Education

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34 CFR Part 668

Student Assistance General Provisions; Final Rule

DEPARTMENT OF EDUCATION

34 CFR Part 668

RIN 1840--AC09

Student Assistance General Provisions

AGENCY: Department of Education.
ACTION: Final regulations.

SUMMARY: The Secretary amends the Student Assistance General Provisions regulations to further implement changes made to section 435 of the Higher Education Act of 1965, (HEA) as amended by the Higher Education Technical Amendments of 1993 (Technical Amendments). These regulations modify the procedures that the Secretary uses to decide appeals of and challenges to the determination of institutional cohort default rates in the Federal Family Education Loan (FFEL) Program.

EFFECTIVE DATE: These regulations take effect July 1, 1995. However, affected parties do not have to comply with the information collection requirements in Sec. 668.17(f) and (h) until the Department of Education publishes in the **Federal Register** the control number assigned by the Office of Management and Budget (OMB) to these information collection requirements. Publication of the control number notifies the public that OMB has approved these information collection requirements under the Paperwork Reduction Act of 1980.

FOR FURTHER INFORMATION CONTACT: Geneva Coombs, Default Management Section, U.S. Department of Education, 600 Independence Avenue, SW., (room 3916, ROB- 3), Washington, DC 20202-5449 for information regarding deadlines and procedures related to the appeal of cohort default rate determinations by institutions. Telephone (202) 708-9396. For information on other policy issues related to this regulation, contact Pat Newcombe, Federal Family Education Loan Program Section. Telephone (202) 708-8242. Individuals who use a telecommunications device for the deaf (TDD) may call the Federal Information Relay Service (FIRS) at 1-800-877-8339 between 8 a.m. and 8 p.m., Eastern time, Monday through Friday.

SUPPLEMENTARY INFORMATION: Section 2(c)(55) of the Technical Amendments amended section 435 of the HEA to modify the process governing institutions' appeals of their cohort default rates based on allegations of improper loan servicing and collection.

On March 22, 1994, the Secretary published a proposed rule and notice in the Federal Register, 59 FR 13606, requesting comments on the procedures that should be established to implement the statutory amendments. The Secretary indicated that he would issue final regulations establishing procedures for institutions to appeal their default rates based on allegations of improper loan servicing or collection. The Secretary also solicited public help in developing those procedures.

After reviewing the comments received in response to the proposed rule, the Secretary issued interim final regulations on April 29, 1994. 59 FR 22278. These regulations were in final form with a stated effective date, but invited additional public comments that could result in future revisions to the regulations. Any revisions would have a later effective date. The Secretary received 80 comments in response to the regulations published on April 29. The Secretary has considered all of these comments in preparing these revisions to the final regulations. Some of the changes suggested by the commenters are reflected in these revisions. The Secretary's response to the suggestions made by the commenters is provided after the following discussion of the changes made to the final regulations. To ensure that the public understands how the revisions affect the final rule, the Secretary is publishing complete revised versions of Sec. 668.17(f), (g) and (h).

Revisions to the Final Rules published on April 29, 1994

The Secretary has revised the standard for determining whether an institution has shown that, for purposes of an appeal of a cohort default rate, improper servicing or collection is considered to have caused a default. In particular, the Secretary has determined that, for purposes of appeals of cohort default rate calculations only, a lender's failure to perform certain collection actions will be considered to have caused a default. The Secretary has revised the regulations to provide that improper servicing or collection will be considered to have caused a default if the borrower has not made a payment on the loan and the institution can prove that the lender failed to perform one or more of the following activities (if such activities were required on the particular loan): (1) Send at least one letter (other than the final demand letter) urging the borrower or endorser to make payments on the loan; (2) make at least one attempt to reach the borrower by phone; (3) request preclaims assistance from the guaranty agency (if required), or (4) send the final demand letter. Therefore, the loan will be excluded from the default rate calculation if the borrower did not make a payment on the loan and the institution can show that the lender missed one of these four activities. If the borrower did not make a payment on the loan and the lender did not make contact with the borrower because the borrower could not be located, the default will be considered to have been caused by improper servicing or collection if the loan file does not include a certification or any evidence that skip tracing activities were performed before the claim was submitted.

The Secretary has determined that it is appropriate to focus the evaluation of cohort default rate appeals on these particular activities because these activities are important elements of the loan servicing and collection process. Each of the activities considered in the cohort default rate appeal process (letters, phone calls, preclaims assistance, final demand and skip tracing) represent a different method of collecting on a loan. The Secretary believes that if each collection technique is used, a default on the loan should not, for cohort default rate appeal purposes, be considered to have been caused by improper servicing or collection.

The Secretary receives hundreds of cohort default rate appeals annually and resolution of these appeals requires significant staff time and resources. In light of these factors and the tight statutory time frames for filing and deciding appeals, the Secretary believes it is necessary to have an appeal process that will result in the rapid and fair adjudication of appeals. The servicing and collection activities identified above are reflected in the loan servicing and collection records that are available to institutions and the Secretary as part of the appeal process. The Secretary will be able to review these records and determine, in a relatively straightforward fashion, whether the relevant servicing and collection activities have been performed. Accordingly, the Secretary believes that the adoption of this modified appeal standard will contribute to ensuring a fair and workable appeal process.

The Secretary has determined that if a borrower made a payment on the loan, the default on the loan cannot be considered to have been caused by improper servicing or collection. The payment by the borrower demonstrates that the borrower is aware of his or her repayment obligation and reflects an affirmation of the debt. This restriction is also consistent with 34 CFR 668.17(e)(1)(ii)(B) which counts as a default any loan on which an institution or related individual or entity makes a payment in order to avoid a default on the loan.

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The Secretary's decision to revise the appeal standard for cohort default rate appeals is based, in large part, on the need to respond to Congress' intention that appeals of loss of FFEL Program eligibility should be filed and resolved within a relatively short period of time. The Department considers the standard included in the April 29 final regulations to be faithful to the letter and purpose of section 435 of the HEA. However, the Secretary has found that determinations under this standard are quite time-consuming for institutions, guaranty agencies and the Department. Hence, while the Department continues to consider the original appeal standard an appropriate implementation of Congressional intent, the Department's experience demonstrates that it does not sufficiently contribute to satisfaction of the statutory goal of ensuring quick and fair decisions.

In preparing these final regulations, the Secretary focused on the two clear goals of section 435 of the HEA: first, to hold institutions with unacceptably high default rates responsible for those rates and the costs to the taxpayers of those defaults; and second, to allow institutions to appeal the determinations of their rates and provide decisions on those appeals in relatively rapid fashion. The standard for deciding appeals included in these final regulations will achieve these goals. The promulgation of these rules allows institutions to avoid responsibility for certain loans where arguably the regulatory violations amounted to improper servicing or collection that are presumed to have "caused" the default for purposes of the cohort default rate appeals. In addition, the regulations will allow the Secretary to make timely appeal decisions based on a quick review of certain records. An appeals process that is based on elaborate rules or that requires time- consuming review would not serve either purpose.

The Secretary believes that this revised standard for evaluating cohort default rate appeals based on allegations of improper loan servicing or collection may make it easier for institutions to prove that loans should be removed from the calculation. The Secretary further believes that institutions with pending appeals before the Department should receive the benefit of this revised standard. Therefore, the Secretary intends to apply the revised standard to pending appeals as a matter of administrative adjudication except where the standard included in the April 29 regulations would be more favorable to the institution.

The final regulations require the institution to notify the Secretary as well as the appropriate guaranty agencies that it is appealing its cohort default rate. This requirement will ensure that the Secretary is notified that an institution has timely appealed so the Secretary does not take action to end the participation of the institution.

The final regulations eliminate the requirement that guaranty agencies provide a list of certain dates for each loan included in the sample of loan servicing and collection records provided to the institution. The Secretary has determined that it is not necessary to have these dates listed separately as part of the appeal.

The final regulations include a definition of "loan servicing and collection records" for purposes of the cohort default rate appeal process. The regulations define the term to mean the default claim package submitted by the lender to the guaranty agency on which the decision to pay a default claim was based. The Secretary believes these records will provide institutions with sufficient information on which to appeal under the revised appeal standards in these regulations. The Secretary notes that the regulations allow the guaranty agency to provide copies of loan servicing and collection records in an electronic or other format if the institution agrees.

The regulations have also been modified to provide some flexibility to guaranty agencies in providing loan servicing and collection records to institutions. Under existing regulations, guaranty agencies are required to provide loan servicing and collection records to a requesting institution within 15 working days of receiving the request. This deadline is consistent with the statutory time frames that govern an appeal by an institution that is subject to loss of FFEL eligibility based on default rates in excess of certain thresholds for each of the three most recent fiscal years. However, the statutory time limit does not apply to institutions which are challenging the calculation of their cohort default rate but are not subject to the loss of FFEL Program eligibility. While these institutions may wish to challenge a cohort default rate calculation, they are not subject to the statutory time frames. Therefore, the Secretary has decided that the requirement that a guaranty agency respond to a request for a sample of loan servicing and collection records within 15 working days will apply only to institutions which are subject to loss of FFEL eligibility. A guaranty agency will have 30 calendar days to respond to a request for servicing and collection records from an institution which is not subject to loss of FFEL Program eligibility.

The regulations have also been modified to clarify that, if the guaranty agency chooses to charge for copying and providing the servicing and collection records, the institution must pay the amount owed to the agency before the agency is required to copy and provide the records. The regulations provide that the agency must inform the institution of the amount owed within 15 working days of the date the agency receives the institution's request for records and the institution must pay the amount owed within 15 working days of receiving the notice of charges from the agency. If payment is not received within this time frame, the institution will be considered to have waived its appeal and the guaranty agency will notify the institution and the Secretary that the institution has apparently waived its appeal in regard to loans guaranteed by that guaranty agency. The Secretary will decide that the institution has not met its burden of proof in regard to the servicing or collection of loans guaranteed by a guaranty agency which the institution did not pay unless the institution proves that the agency's conclusion that the institution waived its appeal was incorrect.

Analysis of Comments

Comments: Many commenters suggested that the Secretary should remove from the calculation of the cohort default rate any loan that was not serviced or collected in strict compliance with the Department's due diligence requirements in 34 CFR 682.411. The commenters suggested that the standard included in the final rules would be inconsistent with statutory intent unless the standard required the exclusion of all loans as to which lender servicing did not strictly comply with 34 CFR 682.411. The commenters claimed that the statutory provisions did not refer to a "causation" requirement and that the Secretary's approach was thus inconsistent with the statute. The commenters complained that the Department's rules reflect a bias against certain types of institutions and were part of an attempt to force certain institutions to close. Finally, the commenters suggested that, without a reference to strict compliance with 34 CFR 682.411, lenders would not have any incentive to comply with the Department's rules.

Discussion: The Secretary does not agree with the suggestion that Congress intended to require the exclusion of all loans on which the lender may not have strictly complied with the requirements of 34 CFR 682.411. The statutory term "improper servicing or collection" is not defined or used elsewhere in the HEA and the Secretary sees no basis for the commenters' claim that it must be defined by strictly incorporating other distinct statutory terms (such as "due diligence") or other specific regulations. The Secretary also does not agree with the suggestion that even a minor or technical non- compliance with the requirements of 34 CFR 682.411 should be considered to have caused a default for cohort default rate purposes. Moreover, the commenters did not cite to any legislative history supporting their claimed interpretation of the statute. The assertions by some commenters that any "servicing error" (a term that does not appear in the HEA or the regulations and has no clear meaning) requires the removal of loans from the cohort default rate calculation similarly has no basis in the HEA.

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Many commenters misunderstand the purpose of 34 CFR 682.411. The requirements in 34 CFR 682.411 are designed to ensure that lenders and guaranty agencies receiving FFEL Program benefits (such as reinsurance and interest and special allowance payments) take certain collection actions in regard to the loans. These requirements have never been intended to set forth standards which, if not followed in their entirety, would excuse borrowers who refuse to repay their loans. Similarly, they are not intended to provide protection for institutions that fail to meet the statutory requirements for continued participation in the FFEL Program. In enacting various statutory provisions, Congress has stated its determination that institutions bear a significant responsibility for defaults in the FFEL Program. See, for example, sections 428A(a)(2), 435(a)(2), 494C(b), 496(a)(5)(J) of the HEA. The Secretary does not believe that a lender's failure to strictly satisfy the requirements for Federal benefits should excuse the institution from the statutory consequences of its high default rate. Moreover, the commenters' suggestion that 34 CFR 682.411 is intended to provide a comprehensive definition of "due diligence" is inaccurate. The Secretary's decisions regarding payments of reinsurance are governed by compliance with other requirements relating to loan servicing and collection in addition to 34 CFR 682.411. See 34 CFR 682.208 and Part 682, Appendix D.

The claim by some commenters that the statute does not support a causation requirement is also incorrect. As noted in the decision of the U.S. Court of Appeals for the District of Columbia Circuit in *Atlanta College of Medical and Dental Technology v. Cavazos*, 987 F.2d 821, 830 (D.C. Cir. 1993), Congress required that a loan would be taken out of the default rate calculation only if the institution's cohort default rate would be inaccurate or improper due to the improper servicing or collection. Congress did not explain how improper servicing or collection could cause a default rate to be inaccurate or incomplete but left the implementation of this requirement to the Secretary. There is no evidence that Congress intended to require the Secretary to look behind the guaranty agency's claims payments. In fact, a review of every guaranty agency claim payment would be a very time consuming and resource intensive process and is inconsistent with the tight time frames in section 435(a)(2) of the HEA.

The statutory requirement that an inaccurate or incomplete cohort default rate be "due to" improper servicing or collection is the source of the causation requirement found in the Secretary's regulations at 34 CFR 668.17(f). The Secretary believes that the requirement of a causal link comports with the statutory language and intent. *See Atlanta College*, 987 F.2d at 830.

Despite the Secretary's conclusion that the standard in the interim final regulations for determining whether a default was caused by improper servicing or collection--i.e., did the borrower receive notice that the time for repayment had begun--is consistent with the intent of section 435 of the HEA, the Secretary has determined that the revised standard included in these regulations is a preferable policy course. The statute does not specify the specific causal link that should be required to remove a loan from the cohort default rate calculation. Thus, implementation of this requirement is within the Secretary's discretion. *See Atlanta College*, 987 F.2d at 830. In exercising that discretion, the Secretary has also considered the statutory provision which directs the Secretary to resolve appeals within a relatively short period of time--45 days. The selection of this time period strongly suggests that Congress did not intend the Secretary to have a complicated or burdensome appeal process. To satisfy this apparent Congressional intent, the Secretary has adopted the revised and simplified appeal standard reflected in these final regulations.

The Secretary strongly rejects the suggestion that the regulations themselves are intended to force certain institutions to close, but this may be a result of section 435. Section 435(m)(4) of the HEA requires the Secretary to publish default rates for institutions participating in the FFEL Program. Obviously, Congress has determined that it is important for the public to have this information. The Secretary has also found that some lenders also use their own measures of default rate to measure their risk of loss in relation to loans made to students attending a particular institution. The Secretary believes that Congress viewed the cohort default rates as a means of allowing lenders to compare different institutions with a common measure. Thus, the impact of these regulations on any particular type of institution results from the statutory provision itself and not from the specific regulatory provisions.

The commenters argue that a lender has no incentive to comply with the requirements of 34 CFR 682.411 unless loans on which the servicing and collection activities are not in strict compliance with the requirements of that section are removed from the calculation of the cohort default rate. This argument reflects a misunderstanding of the FFEL Program. To receive reinsurance payments on a defaulted loan, the guaranty agency must determine that the lender complied with the Secretary's due diligence requirements, 34 CFR 682.406. Thus, the lender's due diligence activities on the loans are subject to review by the guaranty agency and the Secretary. These reviews may result in administrative actions against lenders and guaranty agencies, and provide a more appropriate method of oversight than the time-sensitive cohort default rate appeal process. The Secretary believes that these reviews provide reasonable assurance that a lender is satisfying due diligence requirements.

In reviewing individual cohort default rate appeals, the Secretary has found that institutions claim violations of due diligence requirements in situations where the lender has properly complied with the regulations. The various self-proclaimed loan servicing experts utilized by institutions appealing cohort default rates appear to have used their own standards for due diligence rather than utilizing the Secretary's rules and have mistakenly claimed that their own interpretation of due diligence somehow defines the statutory term "improper servicing or collection". Thus, the claims by these institutions have simply slowed the process of adjudicating cohort default rate appeals rather than contributing to the identification of improper servicing or collection activities by lenders. Moreover, many institutions have previously submitted appeals based on generalized claims of improper servicing or collection activity. Section 435(m)(1)(B) of the HEA, however, requires appeals to be supported by "evidence submitted in support of the institution's timely appeal." The Secretary does not believe that generalized claims of "servicing errors" satisfy this requirement.

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Changes: The Secretary has retained the requirement that, for a loan to be excluded from the calculation of the cohort default rate, the improper servicing or collection must have caused the default. However, as discussed above, the Secretary has modified the regulations to identify specific loan servicing or collection problems that will be assumed to have the required causal connection for purposes of section 435(m)(1)(B) of the HEA.

Comments: One commenter suggested that the Secretary should consider the servicing of a loan to have "caused" a default if the servicing of the loan made a default more likely.

Discussion: Section 435 of the HEA does not provide that a default was caused by allegedly improper servicing or collection activity simply because the activity may arguably have incrementally increased the likelihood of default. In fact, the foremost objective of section 435 is to remove from the FFEL Program institutions whose students default at an excessive rate. While the law provides for the removal of loans from the default rate calculation where a default was "due to" improper servicing or collection, there is no support for the commenter's claim that any increase in the probability of a default should be sufficient.

Defaults occur for a variety of reasons. Congress, however, did not provide that an institution could avoid responsibility for its default rate by simply pointing to contributing factors arguably beyond its control. The lack of provision for such a general causation defense suggests that Congress intended to hold institutions responsible for their unacceptably high rates of loan defaults, based on the reasonable conclusion that such institutions bear a fair share of responsibility for many of those defaults. See S. Rept. 102-58, 102d Cong., 1st. Sess. 10 (1991).

The commenter's reading of the requirements in section 435 of the HEA does not comport with the statute's goal of establishing institutional responsibility for high cohort default rates. In light of the statute's goal of institutional responsibility the Secretary does not believe that it is appropriate to remove a loan from the cohort default rate calculation absent a significant showing of improper servicing or collection that seriously affects the collectability of the loan.

Changes: None.

Comments: One commenter suggested that the institution should not have the burden of proving that the improper loan servicing or collection occurred, but that the lender should be obligated to prove that proper servicing occurred at the time the default claim is submitted.

Discussion: In general, the Secretary agrees with the commenter that the lender is responsible, when it submits an insurance claim, for showing that a loan was serviced in accordance with the Department's requirements. Accordingly, the Secretary refuses to pay (or requires repayment of) reinsurance on loans which are not properly serviced. The lender's obligation, however, relates to the lender's qualification for FFEL Program benefits. In the particular circumstance of an institution's appeal of its cohort default rate, the institution bears the burden of proving that the default rate, which is calculated based on the official records of the FFEL Program, is inaccurate or incorrect. Section 435(a)(3) of the HEA appropriately places the burden of showing this fact on the institution. The alternative of requiring lenders to defend their compliance with the Secretary's servicing and collection rules as part of the cohort default rate appeal process would significantly complicate the process and seriously delay decisions while interfering with the Department's other oversight efforts.

Changes: None.

Comments: Some commenters proposed that the Secretary remove from the calculation of the cohort default rate loans on which the lender did not request preclaims assistance from the guaranty agency or the guaranty agency did not provide notice of the lender's request for preclaims assistance to the institution.

Discussion: As noted earlier, under the revised regulations, a lender's failure to request preclaims assistance from the guaranty agency may be considered improper servicing or collection and result in the exclusion of the affected loan from the calculation of the institution's cohort default rate. The Secretary does not agree with the commenter's suggestion, however, that the loan be excluded if the guaranty agency did not notify the institution of the request. Since a default occurs before the guaranty agency begins servicing and collection activity on the loan, the issue for appeals based on allegations of improper loan servicing is on the actions of the lender, not the guaranty agency. Moreover, consideration of whether the agency notifies the institution of the request for preclaims assistance could result in unequal treatment of different institutions. A guaranty agency is only required to notify an institution of the request for preclaims assistance if the institution has requested such notification and pays a fee. See section 428(c)(2)(H) of the HEA. An institution which had not requested such notice or which did not pay the fee would not have a basis for challenging the rate. As a result, questions of whether an institution properly requested notification and paid any required fee could raise issues of fact that would require a time consuming resolution process. In contrast, the guaranty agency records which the institution will receive on the sample of loans provided by the agency will reflect whether the lender requested preclaims assistance.

The Secretary also determined that consideration of the notice to the institution would significantly increase the burden on guaranty agencies and the Secretary. Since the guaranty agency's notice to those institutions which request notice is not part of the lender claim file and is not part of lender due diligence, documentation of that notice would have to be located elsewhere in the records of the guaranty agency. This additional search would likely delay the appeal process. Moreover, it has been the Secretary's experience that even when guaranty agency records indicate that the institution was notified of the preclaims assistance request, the institution frequently claims that it did not receive notice. Resolution of conflicting claims would further burden the appeal process. In this situation, the Secretary is not satisfied that the effort to produce these additional records is justified by the result.

Changes: The Secretary has modified the regulations to provide that a lender's failure to request preclaims assistance, if such a request was required, will be considered as improper servicing or collection of the loan that caused the default for purposes of a cohort default rate appeal.

Comments: A number of commenters recommended that a loan be eliminated from the calculation of the cohort default rate if the borrower is not located and the lender did not perform skip tracing.

Discussion: The Secretary believes that adequate skip tracing efforts are necessary to protect the Federal taxpayers' investment in the FFEL Program. However, the Secretary notes that skip tracing only occurs when the borrower has failed to fulfill his or her obligation to notify the lender if the borrower moves. The Department's regulations urge institutions to stress the borrowers' responsibility for informing the lender of any new address as part of the institution's default reduction efforts. 34 CFR Part 668, Appendix D. Moreover, the regulations also require institutions to provide information on new addresses of borrowers to lenders. 34 CFR 682.610(f). Thus, a lender is only required to begin skip tracing efforts when the borrower (and in some cases, the institution) has failed to fulfill his or her obligations. Therefore, the Secretary does not believe that a lender's failure to perform specific skip tracing steps should be considered to have caused a default for cohort default rate appeal purposes.

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The Secretary believes, however, that a lender's failure to perform skip tracing at all could, in appropriate cases, be considered to cause a default for cohort default rate purposes. The Secretary notes that while lenders maintain records of their skip tracing efforts, those records are not generally submitted to the guaranty agency as part of the claim file. Instead, the lender certifies that skip tracing was performed. The accuracy of the certification is subject to review by the guaranty agency and the Department and a false certification could subject the lender to a claim under the False Claims Act. In this situation, the Secretary believes that the lender has a strong incentive to provide an accurate certification. Moreover, efforts to determine in detail what skip tracing efforts were performed by a lender would require a search of the lender's records and would be very complicated and time-consuming. (The same is true, in general, of the suggestion that the Secretary assess the quality of the lender's letters and phone calls as part of the appeal process.) Hence, the Secretary will limit the inquiry regarding skip tracing to a simple, mechanical question. As long as the claim file submitted by a lender includes a certification (or, if required by the guaranty agency, other evidence) that skip tracing was performed, the Secretary will conclude that the loan was not improperly serviced or collected with regard to skip tracing. However, absent such evidence, a loan on which no payment or contact has been made will be excluded from the cohort default rate on appeal.

Changes: The Secretary has changed the regulations to provide that if the borrower does not make a payment and no contact was made with the borrower, a lender's failure to provide a certification (or other evidence) that skip tracing, if required, was performed will result in exclusion of the loan from the calculation of the cohort default rate on appeal.

Comments: A number of commenters urged the Secretary to provide institutions more time to complete and submit appeals to the guaranty agencies and the Secretary. Some commenters also proposed that the guaranty agency be permitted to extend the time for the institution to submit its appeal based on a showing by the institution of good cause, such as the number of records involved, other activities such as a visit by an accreditation team or staff illnesses.

Discussion: The Secretary believes that the regulations provide sufficient time for an institution to complete and submit appeals and are consistent with the strict time periods for appeals included in section 435(a)(2) of the HEA.

Changes: None.

Comments: Some commenters recommended that the Secretary grant an institution's appeal if the guaranty agency does not provide the complete loan servicing and collection records within the time set forth in the regulations. A couple of commenters also recommended that the regulations require the Secretary to issue a decision on the institution's appeal within a specified time period.

Discussion: The Secretary does not believe it is appropriate to automatically grant an institution's appeal if the guaranty agency misses a deadline to provide records to the institution. An institution that brings a timely appeal continues to participate in the FFEL programs while it completes the appeal and is not harmed by a delay. The Secretary believes that the guaranty agencies will take appropriate steps to provide records within the regulatory time frames. However, in appropriate cases, the Secretary may consider taking action to levy a financial penalty or to limit, suspend or terminate a guaranty agency's participation in the FFEL Program based on violations of the regulatory time frames.

The Secretary agrees with the commenters that it is important to decide appeals within a reasonable period of time. However, it is impossible for the Secretary to anticipate how many appeals will be filed in a particular year, how complex those appeals will be and what resources can be applied to deciding those appeals. The Secretary fully intends to take appropriate steps to satisfy the statutory requirement that appeals be decided within 45 days. However, this statutory requirement clearly does not mean that the institution's appeal must be granted if the Secretary cannot complete consideration of the appeal within 45 days. *Pro Schools, Inc. v. Alexander*, 824 F.Supp. 1413 (E.D. Wisc., 1993).

The Secretary appreciates the institutions' interest in a timely decision on a cohort default rate appeal. Indeed, a primary reason for the adoption of the revised appeal standard reflected in these final regulations is to reduce the complexity of the appeal process for all parties. The Secretary believes that the revised appeal standard will permit guaranty agencies to provide records to institutions more quickly, allow institutions to complete their appeals and permit the Secretary to resolve those appeals more rapidly. A more complicated appeal standard would not fulfill Congress' direction (and the commenters' request) that appeals be decided expeditiously.

Changes: None.

Comments: Some commenters recommended that a loan be removed from the calculation of the institution's cohort default rate if the loan was sold or transferred and the borrower was not properly notified of the sale or transfer of the loan.

Discussion: The Secretary acknowledges that, in the past, the sale or transfer of a loan may have been a confusing situation for some borrowers; however, the commenters did not provide any evidence that a sale or transfer of a loan contributes to a default. Moreover, since 1991 the Secretary has required both the buyer and the seller of a loan to notify the borrower if the transaction results in a change in the identity or address of the party to whom payments should be sent. The Secretary believes that these notices have generally addressed any confusion on the part of the borrowers. Finally, the Secretary notes that the revised standard for deciding servicing-based appeals addresses the situation in which it is claimed that the borrower did not receive notice of a loan transfer, since it will ensure that the borrower has been notified of the obligation to repay the loan.

Changes: None.

Comments: Some commenters complained that the failure of a lender or servicer to timely apply a refund payment to a student's account should be considered to have "caused" a default and result in the elimination of the affected loan from the calculation of the cohort default rate.

Discussion: The Secretary shares the commenters' concern regarding the effect that a lender's failure to receive or apply a refund to a borrower's account may have on the borrower's repayment record. The Secretary, however, believes that an evaluation of whether the fact that the borrower's account does not reflect a required refund "caused" the default would be largely speculative since the only issue would be the amount of the default. Moreover, documentation of payment of a refund is not generally included in the claim file submitted by the lender to the guaranty agency and is not generally considered a part of the lender's due diligence efforts. Thus, consideration of this issue would require an extensive, time-consuming review of the lender's own records. In the Department's experience, it is more typical that the institution failed to pay the refund to the lender on a timely basis or failed to pay the appropriate refund. The Secretary does not believe it would be appropriate for a high default institution to reduce its default rate because of its failure to fulfill its obligation to make timely refunds.

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The Secretary notes that if the institution shows that a loan should have been canceled because the student did not attend and the institution returned the funds to the lender, the default is removed from the default rate calculation as an issue of erroneous data, not as a loan servicing or collection issue.

Changes: None.

Comments: A number of commenters proposed that the Secretary simply remove loans made or held by certain lenders or guaranty agencies from the calculation of the cohort default rates. For example, some commenters suggested that any loan made by a lender who was later subject to action by the Resolution Trust Corporation should be removed from the calculation. Other commenters suggested that if the institution could show that a particular lender or guaranty agency had a high default rate or did not service loans effectively, all the loans made by that lender or insured by that agency would be eliminated from the calculation of the default rate for that institution.

Discussion: The Secretary does not agree that all the loans made by a certain lender or guaranteed by a certain agency should be removed from the calculation of the cohort default rates. First, the Secretary notes that, under the law, the issue is whether the institution's inaccurate or incomplete cohort default rate is caused by lenders' improper servicing or collection. Generalized assertions that a given lender has "high levels" of "servicing errors" have little probative value when the issue is whether a given loan should be excluded from the default rate calculation because the loan defaulted "due to" improper servicing or collection. A mere allegation that a lender does not properly service loans in general does not show that the alleged improper servicing or collection affected a particular institution's rate. Generalized condemnations of the actions of a guaranty agency--which insures loans from many lenders made to borrowers for attendance at many different institutions--are even less valuable. More importantly, Congress was aware of the broad general complaints by institutions about loan servicing and expressly required that the Department base loan servicing appeal decisions on a review of a representative sample of individual loan servicing records rather than broad allegations.

The Secretary also notes that, in the limited situations in the past in which large scale loan servicing and collection problems have occurred, individual loans which were identified as having been affected were determined to be ineligible for reinsurance. As a result, those loans were not included in the calculation of the default rates.

Changes: None.

Comments: Two commenters suggested that the regulation specify the information that the Secretary will provide to institutions with their default rate notification letters.

Discussion: The Secretary acknowledges that the institution should be provided basic information necessary to evaluate the data on which the default rate calculation is based and will continue to provide that information. However, the Secretary does not believe it is necessary or appropriate to specify, in regulations, the specific data elements that will be included in the information provided to institutions with the default rate notification letters. Specification of the data elements in the regulations would needlessly restrict the Secretary's flexibility in implementing a relatively new procedure.

Changes: None.

Comments: An organization of guaranty agencies noted that the institution has 10 working days from the date it receives the default rate notice from the Secretary to begin the appeal process by submitting its request for records to the guaranty agency. However, the agency may not know the date on which the institution received the notice and will not know whether the institution's appeal is timely. The commenter suggested that the guaranty agency be permitted to use the date of the notice plus 3 days in the absence of other official documentation of receipt.

Discussion: The Secretary does not believe that it is necessary to establish regulatory guidelines for determining when the institution receives the default rate notice. The Secretary generally sends default rate notices to institutions by overnight mail and can generally determine when the institution actually received the notice. The Secretary does not anticipate that there will be many cases in which a guaranty agency has questions about the timeliness of an institution's appeal. However, in those cases, the guaranty agency should contact the Department to determine the date the institution was notified of its rate and calculate the appeal deadline based on the information provided by the Department.

Changes: None.

Comments: A number of commenters complained that a guaranty agency did not have enough time to provide records to the institution. Some commenters suggested that the guaranty agency should have up to 60 days to provide records. Other commenters suggested that the time in which the agency would have to provide records should not run from the date the agency receives the institution's request, but should begin with the date the institution pays any applicable fee for the records. Other commenters objected to the regulations allowing the guaranty agencies to charge reasonable fees for providing records and requested that the Secretary strictly enforce the time deadlines on the guaranty agencies.

Discussion: The Secretary understands that the 15-day deadline for providing records to institutions places a burden on guaranty agencies because most institutions submit their requests for documents at about the same time. However, section 435(a)(2)(A) of the HEA establishes a limited time in which an institution can submit an appeal of its loss of FFEL Program eligibility based on its default rate. Accordingly, the Secretary believes that it is necessary for the guaranty agency to provide the records within 15 working days in cases in which the institution may lose FFEL Program eligibility. There is no statutory deadline for an institution with a default rate over 20 percent but which is not subject to the loss of eligibility to file its appeal. Accordingly, the Secretary believes that guaranty agencies should have a limited amount of additional time to provide records to this latter group of institutions. The Secretary believes that this revision will allow guaranty agencies to better manage their obligations under the regulations, while a longer time period would unduly delay the appeal process.

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In addition, the Secretary notes that some guaranty agencies have taken the position that institutions must pay the fee for the records before the agency provides the records. The Secretary sees no reason to require guaranty agencies to supply records free of charge and previously authorized guaranty agencies to charge a reasonable fee not to exceed $10 per file. The Secretary has now amended the regulations to specifically authorize guaranty agencies to require payment of the fee before providing the documents. The guaranty agency must notify the institution of the amount of the fee within 15 working days of the receipt of the institution's request for records. If the institution pays the fee on time, the guaranty agency must provide the records to the institution within 15 working days and the institution has 30 calendar days from the date it receives the records to file its appeal. The regulations have also been amended to provide that if the guaranty agency does not receive payment of the fee from the institution within 15 working days of the date the institution received the notice of the amount of fee from the agency, the institution will be deemed to have waived its right to appeal. The Secretary reminds guaranty agencies that they should notify the institution of the amount of the fee through a method (such as a return receipt) that identifies the date the institution received the fee notice. The institution may also wish to use a similar delivery method that ensures that the guaranty agency receives the institution's payment on time.

Changes: The regulations have been amended to allow the guaranty agencies up to 30 calendar days to provide loan servicing and collection records to an institution which is not subject to loss of FFEL eligibility based on default rates. The regulations have also been changed to require a guaranty agency which charges a fee to notify the institution of the amount due within 15 working days of the date the agency receives the institution's request and allow the guaranty agency to withhold records until the appropriate fee has been paid. The regulations also provide that if the guaranty agency does not receive payment from the institution within 15 working days of the date the institution received the guaranty agency's fee notice, the institution will be considered to have waived its appeal. The guaranty agency must notify the institution and the Secretary in writing of the apparent waiver. The Secretary will determine that an institution which does not pay a required fee has not met its burden of proof in regard to the loans insured by that guaranty agency unless the institution can first show that the agency's conclusion that the institution waived its appeal was incorrect. An institution could meet this requirement by presenting evidence, such as a return receipt, proving that the institution delivered timely payment to the guaranty agency.

Comments: A number of commenters suggested changes in the method used to pick the sample of loans for which the institution will receive loan servicing and collection records. Some commenters suggested methods other than the method established in the regulations or recommended that the institution or an independent auditor be required to pick the sample.

Discussion: The Secretary has not seen any problems with the standard for picking the sample included in the interim final regulations and is satisfied that the standard is appropriate. The Secretary issued a letter to all guaranty agencies in June 1994 providing suggestions as to how the sample could be selected. An agency which follows that guidance will have complied with the regulatory requirements. However, the Secretary understands that there are other methods an agency may use to pick the sample that also satisfy the regulatory requirements, and the Secretary does not wish to bar the use of these other methods. Accordingly, the Secretary does not believe it is necessary to change the regulations at this time. As the Department develops more experience with the appeal process, however, the Secretary may consider issuing further guidance in this area.

Changes: None.

Comments: One commenter objected to the requirement that the guaranty agency provide a list of certain dates as well as provide the servicing and collection records. The commenter pointed out that this requirement forced the agency to review all of the records rather than just providing copies to the institution.

Discussion: In light of the revised standard for reviewing appeals based on allegations of improper loan servicing and collection, the Secretary has determined that it is no longer necessary to require the guaranty agency to provide a list of certain dates for the loans in the sample.

Changes: The requirement in § 668.17(f)(3)(E)(2) that the agency provide a list of certain dates for the loans in the sample has been deleted.

Comments: One commenter stated that institutions should not have to provide the Department with a list of the number of loans insured by each guaranty agency that were included in the calculation of the default rate since that information will be available from the National Student Loan Data System (NSLDS).

Discussion: The Secretary needs the list of loans to fully evaluate an appeal. However, NSLDS is not fully operational at this time and the necessary information is not yet available from that system. Once NSLDS is fully operational, the Secretary may reconsider whether it is necessary for institutions to submit this information. In the meantime, however, the information is easily available to institutions and the Secretary believes that placing this minor burden on the many institutions which appeal will contribute to timely resolution of appeals.

Changes: None.

Comments: One commenter recommended that after the institution files its appeal with the Department, the guaranty agency should have an opportunity to respond to any allegations of improper loan servicing and collection before the Secretary makes a decision.

Discussion: The Secretary does not believe that it is useful to provide the guaranty agency an opportunity to respond to allegations of improper loan servicing and collection as part of the cohort default rate appeal process. The guaranty agency is not a party to the proceeding but merely provides evidence necessary for the Secretary to make the decision. Participation by guaranty agencies in the cohort default rate appeal process would add needless complexity and delay. If the Department determines, based on evidence resulting from cohort default rate appeals, that a guaranty agency improperly received reinsurance, the agency will have an opportunity to respond to this determination prior to the imposition of any liabilities.

Changes: None.

Comments: One commenter objected to the requirement that an institution must submit "substantial evidence" to rebut the guaranty agency's records. Another commenter asked the Secretary to define "substantial evidence".

Discussion: The guaranty agency's records are the official records of the FFEL Program and are generally presumed to be accurate. To overcome this presumption, the Secretary believes it is appropriate to require the institution to present more than a mere minimum of evidence. "Substantial evidence" is a well defined term in administrative law. In general, "substantial evidence" is "more than a mere scintilla. It means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Consolidated Edison Co. v. NLRB*, 305 U.S. 197, 229 (1938). The Secretary does not believe it is necessary to include this definition in the regulations.

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The alternative to this rule would require the Secretary to conduct a painstaking document-by-document review to validate guaranty agency records. The Secretary does not believe that such an effort would be productive or consistent with the objective of deciding appeals expeditiously.

Changes: None.

Comments: One commenter asked the Secretary to clarify that an institution cannot challenge its default rate in any other proceeding before the Department or a guaranty agency if it does not file a timely appeal. Another commenter objected to the provision limiting an institution to one appeal of a default rate. The commenter noted that the default rates are generally released during the busiest time of the year for institutions, and that institutions which are not faced with the loss of eligibility should have additional time to submit a notice of appeal to the guaranty agency.

Discussion: The regulations clearly specify that an institution which does not timely appeal its cohort default rate cannot challenge that rate in any other proceeding before the Department. The Secretary does not believe it is appropriate to include a restriction on challenges in proceedings governed by guaranty agency rules. However, the Secretary encourages guaranty agencies to include such a restriction in their own rules. The Secretary further notes that the Department, not guaranty agencies, determine cohort default rates. Accordingly, a guaranty agency's claimed determination of an institution's default rate does not constitute a decision by the Secretary.

The Secretary also believes that it is appropriate and necessary to limit institutions to one timely appeal opportunity for each default rate calculation. Multiple appeals by an institution place a significant additional burden on the Department and the guaranty agencies. The Secretary also does not deem it appropriate to allow institutions to delay certain appeals. Cohort default rates are released annually and expeditious consideration and resolution of appeals will maximize the period during which the institution has a definitive default rate. To provide institutions with multiple appeals would result in a substantial waste of resources and might encourage institutions to engage in strategies to delay final decisions regarding their rates.

Changes: None.

Comments: A number of commenters suggested changes to § 668.17(h) which provides for pre-publication review of default rate data by institutions. One organization of guaranty agency representatives requested that the agency be given additional time to respond to requests for correction of information. This organization also suggested that the opportunity to correct data should only be provided to institutions with a most recent cohort default rate above 20%.

Discussion: The Secretary believes that the regulations provide sufficient time for a guaranty agency to respond to allegations of erroneous data by institutions. The pre-publication review process must be completed in sufficient time for the Secretary to incorporate corrections into the default rate calculations and issue rates at approximately the same time each year. The Secretary will, of course, monitor the progress of this system.

At this time the Secretary has decided that it is not appropriate to restrict the right to pre-publication review to certain institutions. The Secretary will monitor the impact and benefit to institutions of pre- publication review to determine if changes are appropriate in the future.

Changes: None.

Comments: A few institutional commenters objected to the provision preventing an institution from alleging errors in the data unless the allegations had been asserted in the pre-publication review process. The institutions argued that new challenges should be permitted because new information might be developed. Another institution asked the Secretary to delete the statement that the time for filing a request for correction with the guaranty agency begins at the time the institution receives or should have received the information from the Secretary.

Discussion: The Secretary strongly believes that it is vital to have a cohort default rate appeal process that results in timely, final appeal decisions by the Department. This goal has been frustrated in the past by institutions which constantly raise new objections to their default rate data after receiving unfavorable decisions on earlier complaints. In the vast majority of cases, these complaints do not justify significant further changes in the institution's default rate and appear designed simply to delay the final resolution of the institution's cohort default rate. Thus, the Secretary believes it is reasonable and appropriate to limit the institution to one opportunity to raise allegations of inaccurate data.

The Secretary also believes that it is appropriate to start the process for challenging data with the date the institution received or should have received default rate information from the Secretary. In the past, some institutions have tried to delay their appeal deadlines by refusing to accept delivery of the default rate notification letter or have claimed after the fact that they did not receive it although the Secretary has a signed return receipt showing receipt. These regulations seek to eliminate the use of this tactic.

Changes: None.

Comments: An organization of guaranty agencies suggested that § 668.17(h)(2) be modified to change the requirement that an institution provide the guaranty agency with "any evidence" it believes supports its contention that the default rate data are incorrect. The organization recommended the deletion of the word "any" to clarify that the institution must submit evidence to support its claim, rather than simply making the allegation. The organization also asked the Secretary to address the treatment of situations where an institution submits questionable documentation to the guaranty agency.

Discussion: The Secretary agrees with the commenter's suggestion that the regulation be modified to require an institution to submit evidence to support a claim that the default rate data are inaccurate.

The Secretary also agrees that the issue of questionable documentation needs to be addressed. The guaranty agencies and the Secretary share the responsibility to identify questionable information. To ensure that issues of questionable documentation are addressed, the Secretary has modified § 668.17(h)(5) to clarify that the changes to default rate data will only be made when the error is confirmed by the guaranty agency and approved by the Department. This change clarifies the Secretary's authority to question a change accepted by the guaranty agency that may have been based on questionable documentation. In any cases in which the Secretary or guaranty agency identifies questionable documentation, the Secretary or the agency will notify appropriate investigative offices and request appropriate action.

Changes: The word "any" has been deleted from § 668.17(h)(2). In addition, § 668.17(h)(5) has been changed to provide that the information used to calculate default rates will be changed to reflect allegations of error made by institutions which are confirmed by the guaranty agency and accepted by the Secretary.

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Comments: One commenter requested that the Department not publish the default rates for lenders, holders and guaranty agencies until those organizations have an opportunity for pre-publication review of the data.

Discussion: The Secretary does not believe that lenders, holders and guaranty agencies need pre-publication review of the default rate data. Congress provided for pre-publication error correction for institutions only, but made no such provision for lenders, holders and guaranty agencies. Moreover, most of the information regarding default rates comes directly from those sources and should be correct. In addition, although the HEA requires the publication of these rates for purposes of public information, there is no loss of eligibility related to those rates. Congress has provided the opportunity for institutions to review the data because of certain consequences resulting from those calculations. Lenders, loan holders and guaranty agencies do not have a similar need for protection.

Changes: None.

Executive Order 12866

These final regulations have been reviewed in accordance with Executive Order 12866. Under the terms of the order, the Secretary has assessed the potential costs and benefits of this regulatory action.

The potential costs associated with the contents of the final regulations are those resulting from statutory requirements and those determined by the Secretary to be necessary for administering the FFEL Program effectively and efficiently. Burdens specifically associated with information requirements, if any, are identified and explained elsewhere in this preamble under the heading *Paperwork Reduction Act of 1980.*

In assessing the potential costs and benefits--both quantitative and qualitative--of these final regulations, the Secretary has determined that the benefits of the final regulations justify the costs.

The Secretary has also determined that this regulatory action does not unduly interfere with State, local and tribal governments in the exercise of their governmental functions.

Paperwork Reduction Act of 1980

Sections 668.17(f) and (h) contain information collection requirements. As required by the Paperwork Reduction Act of 1980, the Department of Education will submit a copy of these sections to the Office of Management and Budget (OMB) for its review. (44 U.S.C. 3504(h)).

These regulations affect institutions of higher education and guaranty agencies that participate in the Federal Family Education Loan Program. The Secretary needs the information to properly administer certain aspects of that program. The collection and reporting burden for the 300 institutions which challenge the calculation of their cohort default rates under these provisions is expected to increase by 15,600 hours. The collection and reporting burden for the 46 guaranty agencies which must respond to the institutions' requests under these regulations is expected to increase by 2,576 hours.

Organizations and individuals desiring to submit comments on the information collection requirements should direct them to the Office of Information and Regulatory Affairs, OMB, Room 3002, New Executive Office Building, Washington, DC 20503; Attention: Daniel J. Chenok. Comments on the burden estimate must be received on or before December 29, 1994.

List of Subjects in 34 CFR Part 668

Administrative practice and procedure, Colleges and universities, Consumer protection, Education, Grant programs-education, Loan programs-education, Reporting and recordkeeping requirements, Student aid.

(Catalog of Federal Domestic Assistance Number 84.032, Federal Family Education Loan Program.)

Dated: November 18, 1994.

Richard W. Riley,
Secretary of Education.