Insight

The Department of Education’s Final Rules on Targeted Federal Student Loan Forgiveness Programs: Expanded Eligibility and Continued Focus on For-profits

TOM LEE | NOVEMBER 21, 2022

Executive Summary

- On October 31, 2022, the Department of Education released final regulations on five targeted federal student loan forgiveness programs that are slated to go into effect July 1, 2023.
- The final regulations mainly loosen the programs’ eligibility requirements, allowing the Biden Administration to forgive the loans of more borrowers.
- The loan forgiveness provided by these expanded programs will be targeted toward current and former students at for-profit colleges.

Introduction

On October 31, 2022, the Department of Education (ED) released final regulations on five federal targeted student loan forgiveness programs. These regulations, slated to go into effect July 1, 2023, originate from the regulatory changes to the loan forgiveness programs the Biden Administration proposed in July 2022. The five programs codify certain standards under which the federal government can cancel borrowers’ outstanding federal student loan balances. The final rules mainly ease the programs’ eligibility requirements, allowing the Biden Administration to forgive the loans of more borrowers, namely those who currently attend or have attended for-profit colleges.

The five programs are:

1. Borrower Defense to Repayment (BDR):
2. Public Service Loan Forgiveness (PSLF);
3. Total and Permanent Disability Discharge (TPD);
4. Closed School Discharge (CSD); and
5. False Certification.

ED also released a final rule on interest capitalization on federal student loans. Those changes will eliminate instances of interest capitalization when it is not required by law. Interest capitalization occurs when unpaid interest is added to the principal of a loan on federal student loans. Below is a review of the final regulations for the five targeted forgiveness programs and interest capitalization on federal student loans.

Borrower Defense to Repayment

BDR allows borrowers of federal direct loans to make a claim for federal student loan forgiveness if they believe they were misled or defrauded by the higher education institution they attended, or if they believe their higher education institution engaged in misconduct in violation of certain state laws. Since BDR's creation in 1994, the program has been changed twice under 2016 and 2019 regulations, with each set of regulations applying different standards. Therefore, BDR standards are applied differently for loans based on disbursement date.

The 2022 final regulations establish a single set of standards that would apply to all BDR applications for loans disbursed after July 1, 2023, or for pending applications prior to that date that have yet to receive a disposition. There are now five types of grounds on which BDR claims can be filed under the final rule:

1. Substantial Misrepresentation;
2. Substantial Omission of Fact;
3. Breach of Contract;
4. Aggressive and Deceptive Recruitment; or
5. "A federal or state judgement or departmental adverse action against an institution that could give rise to a borrower defense claim."

ED expanded the definition of misrepresentation to include "false, erroneous or misleading statements concerning institutional or programmatic admissions selectivity if the institution or program employs an open enrollment policy." The July proposed regulations did not include the language regarding whether an institution or program employs an open enrollment policy. Without that language, it was possible the expanded definition could have been broadly interpreted to forgive student loans at non-profit universities that may have made false or erroneous statements about their selectivity. By including the language on open enrollment policy, it is most likely this expanded form of misrepresentation would apply to for-profit colleges, as they more typically use open-enrollment policies.

Preponderance of Evidence and Detriment

When looking into claims, ED will now use a "preponderance of the evidence standard to determine whether the institution committed an actionable act or omission and, as a result, the borrower suffered detriment." This means ED will not necessarily have to determine as a matter of fact that a college committed one of the five types of violations, but rather whether it was more likely than not the violation occurred.

Group Claims

These final regulations also expand the ability of borrowers to file group claims. The proposed regulations in July would have allowed state requestors, such as a state attorney general, to file BDR claims for groups of borrowers. The final regulations now also allow for other "third-party requestors," such as a legal assistance organization, to file group claims on behalf of borrowers.

Full-discharge Only

Under prior regulations ED could, depending on various factors, elect to grant partial forgiveness for an approved BDR claim. Under the final rule, if ED approves a claim, it will grant full discharge on federal student loans associated with the BDR claim.

Recoupment

Last, the final rule outlines how ED will recoup costs from institutions. Under current regulations, if a BDR claim is approved, the amount of loans forgiven will simply be written off by ED. Under the final regulations, if a BDR claim is approved and associated loan balances forgiven, ED will seek to recoup those costs from the institution with which the claim is associated.

Public Student Loan Forgiveness

PSLF allows the federal government to forgive outstanding federal student loan debt if a borrower:

1. Has been employed by a federal, state, or local government, tribal agency, or nonprofit organization;
2. Works full-time for that agency or organization;
3. Has direct federal loans, or their loans have been consolidated into a direct loan;
4. Is currently enrolled in an income-driven repayment plan; and
5. Makes 120 qualifying monthly payments.

If a borrower believes they meet these standards, they can apply through PSLF to receive forgiveness on their remaining federal student loan debt. Under current regulations, a borrower "must make each of the 120 monthly payments within 15 days of the scheduled due date for the full scheduled installment amount for that payment to qualify toward PSLF." The final rule instead allows borrowers to receive credit toward forgiveness for late payments made in installments or as a lump sum. The final rule will also allow ED to "include certain periods of deferment or forbearance to count toward PSLF and to count payments made on underlying loans prior to consolidation will reduce the time period for some existing PSLF recipients to achieve forgiveness." What's more, the rule will give borrowers a "weighted average of existing qualifying payments toward PSLF when they consolidate their Direct loans."

The final rule defines full-time employment at 30 hours per week across one or more jobs to qualify for forgiveness under PSLF. The rule also expands the definition of qualifying employer to "include an individual who works as a contracted employee for a qualifying employer in a position or providing services which, under applicable state law, cannot be filled or provided by a direct employee of the qualifying employer." Taken together, these changes will push more borrowers over the threshold required to receive forgiveness under PSLF.

Total and Permanent Disability

TPD allows for the cancellation of federal student loans if a borrower is totally and permanently disabled. The final rules ease many of the requirements and standards to receive forgiveness through TPD. Under current regulations, a borrower must provide documentation to ED from the Department of Veterans Affairs, the Social

Security Administration, or a physician showing they are totally and permanently disabled. After receiving forgiveness under TPD, a borrower must not have annual employment earnings that exceed 100 percent of the federal poverty guideline for a family of two, among other things.

The final rule amends TPD so that nurse practitioners, physicians' assistants, and licensed psychologists are now eligible to provide sufficient documentation demonstrating total and permanent disability for applicants. Most important, current regulations require a three-year income monitoring period for borrowers who have received a TPD discharge. The final rules eliminate this post-discharge income monitoring requirement.

Closed School Discharge

Closed School Discharge allows ED to forgive federal student loan balances for borrowers whose schools closed while they were enrolled or shortly after their withdrawal. The final rule on CSD focuses on granting automatic discharges. More specifically, ED removed the current requirement that a borrower may only qualify for a CSD without an application if the borrower does not re-enroll in an eligible Title IV school within three years of the school's closure date. Instead, ED would automatically discharge loans for a borrower within one year of the school's closure date unless the borrower accepts and completes an approved teach-out agreement. For borrowers "who accept a teach-out or a continuation of the program at another branch or location of the school but do not complete the program, their discharge would be done one year after their final date of enrollment in the teach-out or at the other branch or location of the school." These changes would give borrowers more time to request CSDs, and give ED more power to automatically forgive loans through the program without borrower-submitted applications.

False Certification

Through False Certification Discharge, ED can forgive the outstanding federal student loan balances of borrowers whose school falsely determined they were eligible to receive federal student loans.

ED will now use the borrower's status of having a high school diploma or equivalent at the time of origination of the federal loan, instead of, as under current regulations, the borrower's status at the time of disbursement of the loan. Because origination of loans occurs before disbursement, this proposed change effectively increases the time period during which a borrower could have been falsely certified, therefore making it easier for prospective federal student loan holders to receive forgiveness. The final rules also create a group-claim mechanism like that of BDR and CSD. Through the group-claim mechanism, ED would have more flexibility to forgive debt through FCD without necessarily judging the individual merits of each borrower in that group.

Interest Capitalization

The final rule also eliminates all instances where interest capitalization is not required by law, such as the Higher Education Act (HEA). This means "interest will no longer be added to a borrower's principal balance when a borrower first enters repayment, after periods of forbearance, and upon leaving all IDR plans except for IBR." This includes the Pay As You Earn (PAYE) and Revised Pay As You Earn (REPAYE) plans.

Overall, unlike the changes to the targeted forgiveness programs, the changes to interest capitalization do not increase eligibility for borrowers to receive forgiveness. Instead, these changes to interest capitalization will reduce the rate at which outstanding balances can grow due to borrowers not paying interest for various reasons, such as when entering forbearance due to economic hardship.