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M E M O R A N D U M

TO: Barry D. Burgdorf
FROM: Karen Lundquist
SUBJECT: Comparison of Federal Regulations and the Texas Higher Education Fair Lending Practices Agreement

The Department of Education has adopted regulations governing certain aspects of the student loan industry relating to lender lists and to prohibited inducements. Although the regulations do not take effect until July 1, 2008, the Secretary of Education has urged institutions of higher education and lenders to voluntarily comply with certain key elements of the regulations before that date. (Dear Colleague Letter, August 9, 2007.)

UT System institutions are currently complying with the Texas Higher Education Fair Lending Practices Agreement, which also governs lender lists and prohibited inducements. In order to prepare for compliance with the new federal regulations, this memorandum provides a summary comparison of the regulations and the agreement.

The agreement specifically provides that it does not relieve an institution of higher education of its obligation to comply with all federal regulations, nor does it give an institution permission to engage in any act or practice prohibited by the regulations. If compliance with the agreement would cause the institution to breach a federal regulation, the institution is relieved of complying with the agreement only to the extent of avoiding such a breach. In such a case, the institution is required to promptly notify the Texas Attorney General of its inability to comply with the agreement, and the parties should make good faith efforts to negotiate appropriate revisions to the agreement in light of changes in the governing law.

In this memorandum, “regulations” means the federal regulations governing lender lists and prohibited inducements that take effect July 1, 2008, “agreement” means the Texas Higher Education Fair Lending Practices Agreement, and “schools” means institutions of higher education.

For a more detailed summary of the new regulations, please refer to the memorandum prepared by this office and dated February 19, 2008. In addition, a more detailed analysis may be necessary to respond to specific questions that may arise under the regulations.

Lender Lists

The regulations authorize schools to make available a list of recommended or suggested lenders. (34 CFR Sec. 682.212(h).) The regulations impose three major duties and restrictions that are not covered by the agreement. First, the regulations require a lender list to contain at least three lenders that are not affiliated with each other. Second, the regulations require schools to provide comparative information to prospective borrowers about interest rates and other benefits offered by lenders on the list. Third, for first-time borrowers, the regulations prohibit schools from assigning, through award packaging or other methods, a borrower’s loan to a particular lender.

The following is a summary comparison of the regulations and the agreement as they relate to lender lists.

Regulations: Lender list may not be used to deny or otherwise impede a borrower’s choice of lender. School must include a prominent statement on any information related to lender lists advising prospective borrowers that they are not required to use any lender on the list. School may not cause unnecessary certification delays for borrowers who use a lender not on the list.

Agreement: Lender list must state that a borrower has the right and ability to select lender of choice, is not required to use any lender on the list, and will not be penalized for selecting lender not on the list.

Regulations: Lender list must contain at least three lenders that are not affiliated with each other.

Agreement: No similar provision.

Regulations: Lender list may not include lenders that have offered financial or other benefits to the school in exchange for inclusion on the list or in exchange for any promise that a certain number of loan applications will be sent to the lender by the school or its students. (Note also that another new regulation, 34 CFR Sec. 682.200, provides that a lender is not an eligible lender if it offers payments or other benefits to a school, any school-affiliated organization, or any individual in exchange for placement on a school’s lender list.)

Agreement: Lenders cannot pay to be included on the lender list. Lender may not be placed on list or given favored placement on list for a particular type of loan in exchange

for benefits provided to the school or to its students in connection with a different type of loan.

Regulations: Lender list must disclose to prospective borrowers the method and criteria used by the school in selecting any lender that it recommends or suggests.

Agreement: Same, but list must also include relative importance of criteria.

Regulations: List and any accompanying information must be updated at least annually.

Agreement: List must be reviewed and updated at least annually.

Regulations: School must provide comparative information to prospective borrowers about interest rates and other benefits offered by lenders on list.

Agreement: No similar provision.

Regulations: For first-time borrowers, school may not assign, through award packaging or other methods, a borrower's loan to a particular lender.

Agreement: No similar provision.

The agreement contains additional requirements related to the compilation of lender lists, and schools must continue to comply with those requirements even though the requirements are not included in the regulations. For an explanation of those requirements, see Part IV.A, Sections 9Bi, 9C – F, and 9H, of the agreement.

Prohibited Inducements by Lenders

The regulations provide that a lender is not an eligible lender if the Secretary of Education determines that the lender has offered, directly or indirectly, points, premiums, payments, or other inducements to a school or other party to secure applications for FFEL loans or to secure FFEL loan volume. (34 CFR Sec. 682.200(b), definition of "Lender," Paragraph (5)(i)(A).) The regulations specifically list certain types of inducements covered by this provision, and the focus is on the lender's conduct. By contrast, the agreement focuses on the conduct of the school and its employees. Nonetheless, we believe that schools will find it useful to have a summary of the provisions in the regulations governing lender conduct and a corresponding summary of similar types of school and employee conduct covered by the agreement.

Note that the following terms are among those defined by the regulations:

"School-affiliated organization" means any organization that is directly or indirectly related to a school and includes alumni organizations, foundations, athletic organizations, and social, academic, and professional organizations.

"Other benefits" includes preferential rates for or access to the lender's other financial products, computer hardware or non-loan processing or non-financial aid-related computer software at below market rental or purchase cost, and printing and distribution of college catalogs and other materials at reduced or no cost. (The definition of "gift" in

the agreement includes any thing of value exceeding \$20, and specifically includes computer hardware for which the recipient pays a below-market price, and any printing costs or services.)

Regulations: Prohibits lender from offering payments or other benefits, including prizes or additional financial aid funds, to a prospective borrower in exchange for applying for or accepting a FFEL loan from the lender.

Agreement: No similar provision.

Regulations: Prohibits lender from offering **payments or other benefits** to a school, any school-affiliated organization, or any individual in exchange for FFEL loan applications, application referrals, or a specified volume or dollar amount of loans made, or placement on a school's lender list.

Agreement: Prohibits a school or a school employee from soliciting or accepting a gift exceeding \$20 in value from or on behalf of a lender.

Regulations: Prohibits lender from offering payments or other benefits provided to a student at a school who acts as the **lender's representative** to secure FFEL loan applications from individual prospective borrowers.

Agreement: School may not identify employee, representative or agent of a lender to borrowers as an employee, representative, or agent of the school. School may not authorize an employee, representative, or agent of a lender to represent, explicitly or implicitly, that he or she is an employee, representative, or agent of the school.

Regulations: Prohibits lender from offering payments or other benefits to a loan solicitor or sales representative of a lender who visits schools to solicit individual prospective borrowers to apply for FFEL loans from the lender.

Agreement: No similar provision.

Regulations: Prohibits lender from making payment to another lender or any other party of referral fees or processing fees, except those processing fees necessary to comply with federal or state law.

Agreement: No similar provision.

Regulations: Prohibits lender from soliciting an employee of a school or school-affiliated organization to serve on a lender's **advisory board** or committee, and prohibits payment of costs incurred on behalf of an employee of a school or school-affiliated organization to serve on a lender's advisory board or committee.

Agreement: Requires an institution employee to obtain prior written approval from the school's president before serving as a member or otherwise participating on an advisory board, board of directors, or any other board or management council of a lender. Prohibits school employee from accepting any remuneration or reimbursement of expenses for that service as a member or participant.

Regulations: Prohibits lender from offering to pay **conference or training registration, transportation, and lodging costs** for an employee of a school or school-affiliated

organization. Allows meals, refreshments, and receptions that are reasonable in cost and scheduled in conjunction with training, meeting, or conference events if those meals, refreshments, or receptions are open to all training, meeting, or conference attendees.

Agreement: Prohibits a school or school employee from accepting a gift exceeding \$20 in value from a lender, including a registration fee, meals, hospitality, lodging costs, and travel expenses. Allows training or informational material furnished to a school employee as an integral part of a training session.

Regulations: Prohibits lender from offering to pay **entertainment expenses**, including expenses for private hospitality suites, tickets to shows or sporting events, meals, alcoholic beverages, and any lodging, rental, transportation, and other gratuities related to lender-sponsored activities, for employees of a school or a school-affiliated organization.

Agreement: Prohibits a school or school employee from accepting a gift exceeding \$20 in value from a lender, including entertainment, meals, hospitality, lodging costs, and travel expenses.

Regulations: Prohibits lender from engaging in **philanthropic activities**, including providing scholarships, grants, restricted gifts, or financial contributions in exchange for FFEL loan applications or application referrals, or a specified volume or dollar amount of FFEL loans made, or placement on a school's lender list.

Agreement: Allows philanthropic gifts outside the office of student financial aid if not for the purpose of securing a benefit relating to student lending. Includes scholarships and similar awards that are passed directly on to students; buildings, rooms, facilities, or equipment for a department other than student financial aid; naming a facility or program; and programs or operations other than those related to the office of student financial services.

Regulations: Prohibits lender from providing **staffing services** to a school, except for services provided to participating foreign schools at the direction of the Secretary of Education, as a third-party servicer, or otherwise on more than a short-term, emergency basis, and which is non-recurring, to assist a school with financial aid-related functions.

Agreement: School may not identify employee, representative or agent of a lender to borrowers as an employee, representative, or agent of the school. School may not authorize an employee, representative, or agent of a lender to represent, explicitly or implicitly, that he or she is an employee, representative, or agent of the school.

Notwithstanding the above, the regulations authorize a lender, in carrying out its role in the FFEL program and in attempting to provide better service, to provide the following:

- Support of and participation in a school's or a guaranty agency's student aid and financial literacy-related outreach activities, excluding in-person school-required initial or exit counseling, as long as the name of the entity that developed and paid for any material is provided to the participants and the lender does not promote its student loan or other products. (Note: The agreement provides that a lender's own brochure or promotional literature is not considered to be a gift to the

institution or an institution employee. However, under the regulations, any materials provided by a lender as part of a school's outreach activities may not promote its student loans or other products.)

- Meals, refreshments, and receptions that are reasonable in cost and scheduled in conjunction with training, meeting, or conference events if those meals, refreshments, or receptions are open to all training, meeting, or conference attendees. (Note: See summary above concerning conference and training expenses.)
- Toll-free telephone numbers for use by schools or others to obtain information about FFEL loans and free data transmission service for use by schools to electronically submit applicant loan processing information or student status confirmation data. (Note: The agreement prohibits schools from directing a potential borrower to an electronic master promissory note or other loan agreement that does not allow the borrower to enter the lender code or name for any lender offering the relevant loan, but allows the school to direct a potential borrower to a particular lender's electronic loan agreement if the borrower represents that he or she wishes to engage that lender.)
- Items of nominal value to schools, school-affiliated organizations, and borrowers that are offered as a form of generalized marketing or advertising, or to create good will. (Note: The agreement generally defines a "gift" from a lender as any thing of value exceeding \$20 in value, other than a lender's own brochure or promotional literature.)
- Assistance to a school that is comparable to the kinds of assistance provided to a school by the Secretary of Education under the Direct Loan program, as identified by the Secretary in a public announcement, such as a notice in the Federal Register.
- A reduced origination fee in accordance with 34 CFR Sec. 682.202(c).
- A reduced interest rate as provided under the Higher Education Act of 1965, as amended.
- Payment of federal default fees in accordance with the Higher Education Act of 1965, as amended.
- Purchase of a loan made by another lender at a premium.
- Other benefits to a borrower under a repayment incentive program that requires, at a minimum, one or more scheduled payments to receive or retain the benefit or under a loan forgiveness program for public service or other targeted purposes approved by the Secretary of Education, provided those benefits are not marketed to secure loan applications or loan guarantees.

- Other services as identified and approved by the Secretary through a public announcement, such as a notice in the Federal Register.

The agreement contains prohibitions related to revenue sharing, high risk student loan agreements, and stock ownership, as well as certain requirements to disclose financing options, that are not covered by the regulations, and schools must continue to comply with those provisions. See Part IV.A, Sections 3, 6, 8, and 10, of the agreement.

Prohibited Inducements by Guaranty Agencies

The regulations provide that a guaranty agency may not, either directly or through an agent or contractor, offer directly or indirectly from any fund or assets available to the guaranty agency, any premium, payment, or other inducement to a prospective borrower of an FFEL loan, or to a school or school-affiliated organization or an employee of a school or school-affiliated organization, to secure applications for FFEL loans. (34 CFR Sec. 682.401(e).) The regulations specifically list certain types of inducements covered by this provision, and the focus is on the guaranty agency's conduct. By contrast, the agreement focuses on the conduct of the school and its employees. Nonetheless, as with the lender restrictions, we believe that schools will find it useful to have a summary of the provisions in the regulations governing guaranty agency conduct and a corresponding summary of similar types of school and employee conduct covered by the agreement.

Note that the regulations define a "guaranty agency" as a state or private nonprofit organization that has an agreement with the Secretary of Education under which it will administer a loan guarantee program under the Higher Education Act of 1965, as amended. Although the agreement excludes the Texas Guaranteed Student Loan Corporation (TG) from the definition of "student loan lender," TG is covered by provisions of the regulations relating to guaranty agencies.

Note also that the following terms are among those defined by the regulations:

"School-affiliated organization" means any organization that is directly or indirectly related to a school and includes alumni organizations, foundations, athletic organizations, and social, academic, and professional organizations.

"Other benefits" includes preferential rates for or access to the lender's other financial products, computer hardware or non-loan processing or non-financial aid-related computer software at below market rental or purchase cost, and printing and distribution of college catalogs and other materials at reduced or no cost. (The definition of "gift" in the agreement includes any thing of value exceeding \$20, and specifically includes computer hardware for which the recipient pays a below-market price, and any printing costs or services.)

"Premium," "incentive payment," and "other inducement" do not include services directly related to the enhancement of the administration of the FFEL Program that the

guaranty agency generally provides to lenders that participate in its program. However, those terms do apply to other activities specifically intended to secure a lender's participation in the agency's program.

Regulations: Prohibits guaranty agency from offering payments or other benefits, including prizes or additional financial aid funds, to a prospective borrower in exchange for processing a loan using the agency's loan guarantee.

Agreement: No similar provision.

Regulations: Prohibits guaranty agency from offering payments or other benefits, including prizes or additional financial aid funds under any Title IV or state or private program, to a school or school-affiliated organization based on the school's or organization's voluntary or coerced agreement to use the guaranty agency for processing loans, or to provide a specified volume of loans using the agency's loan guarantee.

Agreement: Prohibits a school or school employee from soliciting or accepting a gift exceeding \$20 in value from or on behalf of a guaranty agency, excluding TG.

Regulations: Prohibits guaranty agency from offering payments or other benefits to a school, any school-affiliated organization, or any individual in exchange for FFEL loan applications or application referrals, a specified volume or dollar amount of FFEL loans using the agency's loan guarantee, or the placement of a lender that uses the agency's loan guarantee on a school's lender list.

Agreement: Prohibits a school or school employee from soliciting or accepting a gift exceeding \$20 in value from or on behalf of a guaranty agency, excluding TG.

Regulations: Prohibits guaranty agency from offering to pay entertainment expenses, including expenses for private hospitality suites, tickets to shows or sporting events, meals, alcoholic beverages, and any lodging, rental, transportation, and other gratuities related to any activity sponsored by the guaranty agency or a lender participating in the agency's program, for employees of a school or employees of a school-affiliated organization.

Agreement: Prohibits a school or school employee from accepting a gift exceeding \$20 in value from a guaranty agency (other than TG), including entertainment, meals, hospitality, lodging costs, and travel expenses.

Regulations: Prohibits guaranty agency from engaging in philanthropic activities, including providing scholarships, grants, restricted gifts, or financial contributions in exchange for FFEL loan applications or application referrals, a specified volume or dollar amount of FFEL loans using the agency's loan guarantee, or the placement of a lender that uses the agency's loan guarantee on a school's lender list.

Agreement: Allows philanthropic gifts outside the office of student financial aid if not for the purpose of securing a benefit relating to student lending. Includes scholarships and similar awards that are passed directly on to students; buildings, rooms, facilities, or equipment for a department other than student financial aid; naming a facility or program; and programs or operations other than those related to the office of student financial services.

Regulations: Prohibits guaranty agency from providing staffing services to a school, except for services provided to participating foreign schools at the direction of the Secretary of Education, as a third-party servicer, or otherwise on more than a short-term emergency basis, and which is non-recurring, to assist a school with financial aid-related functions.

Agreement: School may not identify employee, representative, or agent of a guaranty agency to borrowers as an employee, representative, or agent of the school. School may not authorize an employee, representative, or agent of a guaranty agency to represent, explicitly or implicitly, that he or she is an employee, representative, or agent of the school.

The regulations also prohibit a guaranty agency from assessing additional costs or denying benefits otherwise provided to schools and lenders participating in the agency's program on the basis of the lender's or school's failure to agree to participate in the agency's program, or to provide a specified volume of loan applications or loan volume to the agency's program, or to place a lender that uses the agency's loan guarantee on a school's lender list.

Notwithstanding the above, a guaranty agency is not prohibited from providing the following:

- Student aid and financial literacy-related outreach activities, excluding in-person school-required initial or exit counseling, as long as the name of the entity that developed and paid for any material is provided to the participants and the guaranty agency does not promote its student loan or other products; but a guaranty agency may promote benefits provided under other federal or state programs administered by the guaranty agency. (Note: The agreement provides that a guaranty agency's own brochure or promotional literature is not considered to be a gift to the school or a school employee. However, under the regulations, any materials provided by a guaranty agency (other than TG) as part of a school's outreach activities may not promote its student loans or other products.)
- Meals and refreshments that are reasonable in cost and provided in connection with guaranty agency provided training of program participants and elementary, secondary, and postsecondary school personnel and with workshops and forums customarily used by the agency to fulfill its responsibilities under the Higher Education Act of 1965, as amended.
- Meals, refreshments, and receptions that are reasonable in cost and scheduled in conjunction with training, meeting, or conference events if those meals, refreshments, or receptions are open to all training, meeting, or conference attendees.
- Travel and lodging costs that are reasonable as to cost, location, and duration to facilitate the attendance of school staff in training or service facility tours that

they would otherwise not be able to undertake, or to participate in the activities of an agency's governing board, a standing official advisory committee, or in support of other official activities of the agency. (Note: The agreement prohibits a school employee from accepting remuneration or reimbursement of expenses from guaranty agencies, other than TG, for serving as a member of or otherwise participating on an advisory board, board of directors, or any other board or management council of a guaranty agency. It also prohibits a school or school employee from accepting any thing of value exceeding \$20 from a guaranty agency other than TG, but allows training or educational materials that contribute to the professional development of the employee.)

- Toll-free telephone numbers for use by schools or others to obtain information about FFEL loans and free data transmission service for use by schools to electronically submit applicant loan processing information or student status confirmation data. (Note: The agreement prohibits institutions from directing a potential borrower to an electronic master promissory note or other loan agreement that does not allow the borrower to enter the lender code or name for any lender offering the relevant loan, but allows the institution to direct a potential borrower to a particular lender's electronic loan agreement if the borrower represents that he or she wishes to engage that lender.)
- Items of nominal value to schools, school-affiliated organizations, and borrowers that are offered as a form of generalized marketing or advertising, or to create good will. (Note: The agreement generally defines a "gift" from a guaranty agency, other than TG, as any thing of value exceeding \$20, other than an agency's own brochure or promotional literature.)
- Assistance to a school that is comparable to that provided by the Secretary under the Direct Loan program, as identified by the Secretary in a public announcement, such as a notice in the Federal Register.
- Default aversion activities approved by the Secretary of Education under Section 422(h)(4)(B) of the Higher Education Act of 1965, as amended.
- Payment of federal default fees in accordance with the Higher Education Act of 1965, as amended.
- Loan forgiveness programs for public service and other targeted purposes approved by the Secretary of Education, provided the programs are not marketed to secure loan applications or loan guarantees.
- Other services as identified and approved by the Secretary through a public announcement, such as a notice in the Federal Register.

Rebuttable Presumption

The regulations provide that in certain actions against a lender or guaranty agency, if the Secretary of Education finds that a lender or guaranty agency provided or offered prohibited payments or activities under the regulations discussed above, the Secretary will apply a rebuttable presumption that the payments or activities were offered or provided to secure applications for FFEL loans or to secure FFEL loan volume. To reverse the presumption, the lender or guaranty agency must present evidence that the activities or payments were provided for a reason unrelated to securing applications for FFEL loans or securing loan volume. (34 CFR Secs. 682.413(h), 682.705(c).)