

Issue Paper 6

Program Integrity and Improvement Issues

Issue: Definition of Adverse Credit for Direct PLUS Loan Eligibility

Statutory cite: §428B(a)(1)(A) of the HEA

Regulatory cite: 34 C.F.R. §685.200(c)(1)(vii)

Summary of Issue: The Department makes Direct PLUS Loans to parents of dependent undergraduate students and to graduate and professional students. For any academic year of study, a PLUS loan borrower may borrow up to the difference between the student's cost of attendance and other estimated financial aid for the student. Section 428H(d)(4)(A) of the HEA also provides that a dependent student whose parent is unable to borrow a PLUS loan may receive Direct Unsubsidized loans up to the annual loan limit applicable to an independent undergraduate student.

Under §428B(a)(1)(A) of the HEA (which applies to the Direct Loan Program under §455(a)(1) of the HEA), to be eligible to receive a Direct PLUS Loan, the applicant must not have an adverse credit history as determined pursuant to regulations promulgated by the Secretary.

Under the Direct Loan program regulations at 34 CFR §685.200(c)(1)(vii), a PLUS loan applicant is considered to have an adverse credit history if, as of the date of the credit report on the applicant, the applicant:

1. Is 90 days or more delinquent on any debt; or
2. Has been the subject of a default determination, bankruptcy discharge, foreclosure, repossession, tax lien, wage garnishment, or write-off of a Title IV debt in the five years preceding the date of the credit report.

The regulations provide that the absence of a credit history is not considered to be an adverse credit history and is not a basis for denying a Direct PLUS loan. An applicant with an adverse credit history can receive a PLUS loan if he or she obtains an endorser who does not have an adverse credit history, or if he or she can document to the satisfaction of the Secretary that extenuating circumstances exist.

The definition of adverse credit for Direct PLUS loan eligibility was included as part of the final standards, criteria, and procedures for the first year of the Direct Loan Program's operation which were published on January 4, 1994. Direct Loan program regulations developed through negotiated rulemaking and published on December 1, 1994 incorporated the same adverse credit criteria and added the current provisions which address the status of applicants with no credit history and provide for PLUS loan eligibility based on the borrower's documented extenuating circumstances. As part of final regulations published on November 1, 2013, the Department added a provision to the regulations that provides that the Secretary may determine that extenuating circumstances exist based on documentation that includes, but is not limited to, an

updated credit report, a statement from the creditor that the borrower has made satisfactory arrangements to repay the debt, or a satisfactory statement from the borrower explaining any delinquencies with outstanding balances of less than \$500. This provision was added to reflect the Department's procedures and a similar rule in the Federal Family Education Loan Program (FFELP).

Direct PLUS Loan applicants are evaluated at least once each academic year to determine if they have an adverse credit history. A significant number of applicants initiate the process online by completing the Federal Direct PLUS Request for Supplemental Information. The Department receives a credit report on the applicant from the credit reporting organizations. The Department then determines the applicant's PLUS loan eligibility based on the regulatory definition of adverse credit. Applicants who are denied based on adverse credit are informed of their option to secure a PLUS loan using an endorser who does not have an adverse credit history or to request reconsideration of the adverse credit determination based on extenuating circumstances, and for parent applicants, of the dependent student's ability to borrow an increased amount of Direct Unsubsidized Loan.

In 2010, when Congress changed the HEA to provide that all new student and parent loans would be made under the Federal Direct Loan Program, the Department discovered that the definition of adverse credit history was being applied in a manner that was inconsistent with the Direct Loan regulations and with the regulations and practices followed in the FFELP. Specifically, for the Direct Loan program, the Department was not counting debts in collection or debts that had been charged off as constituting adverse credit history, as required by the regulations. The Department took steps to address this inconsistency and to ensure that the Direct Loan Program was in compliance with the Department's own regulations. By November 2011, the Department's practices were consistent with the regulations.