The Closure of Institutions of Higher Education: Student Options, Borrower Relief, and Other Implications

Updated February 5, 2019
Summary

When an institution of higher education (IHE) closes, a student’s postsecondary education may be disrupted. Students enrolled at closing IHEs may face numerous issues and may be required to make difficult decisions in the wake of a closure. Two key issues students may face when their IHEs close relate to their academic plans and their personal finances.

The academic issues faced by students when their schools close include whether they will continue to pursue their postsecondary education, and if so, where and how they might do so. Students deciding to continue their postsecondary education have several options. They may participate in a teach-out offered by the closing institution or by another institution. A teach-out is a plan that provides students with the opportunity to complete their program of study after a school’s closure. Students may also be able to transfer the credits they previously earned at the closed IHE to another IHE. If a student is able to transfer some or all of the previously earned credits, he or she would not be required to repeat the classes those credits represent at the new institution; if a student is unable to transfer previously earned credits, the student may be required to repeat the classes those credits represent at the new IHE. Decisions regarding the acceptance of credit transfers are within the discretion of the accepting IHE.

The financial issues faced by students when their schools close include whether they are responsible for repaying any loans borrowed to attend a closed school and how they might finance any additional postsecondary education they pursue. In general, a closed school loan discharge is available to a borrower of federal student loans made under Title IV of the Higher Education Act (P.L. 89-329, as amended), if the student was enrolled at the IHE when it closed or if the student withdrew from the IHE within 120 days prior to its closure. Additionally, the student must have been unable to complete his or her program of study at the closed school or a comparable program at another IHE, either through a teach-out agreement or by transferring any credits to another IHE. Borrowers ineligible for a closed school discharge may be able to have eligible Title IV federal student loans discharged by successfully asserting as a borrower defense to repayment (BDR) certain acts or omissions of an IHE, if the cause of action directly relates to the loan or educational services for which the loan was provided. Whether a borrower may have discharged all or part of any private education loans borrowed to attend the closed IHE may depend on the loan’s terms and conditions.

Some students may also face issues regarding how they might finance future postsecondary educational pursuits. If a borrower receives a closed school discharge or has a successful BDR claim, the discharged loan will not count against the borrower’s Subsidized Loan usage period, which typically limits certain borrowers’ receipt of Direct Subsidized Loans for a period equal to 150% of the published length of his or her academic program, and a borrower’s statutory annual and aggregate borrowing limits on Direct Subsidized and Direct Unsubsidized Loans are unlikely to be affected. Students who receive a Pell Grant for enrollment at a school that closed may have an equivalent amount of Pell eligibility restored. Likewise, if the student used GI Bill educational benefits from the Department of Veterans Affairs for attendance at a closed school, those benefits can be restored.

Students may be reimbursed for payments on charges levied by closed IHEs that are not covered by other sources from a State Tuition Recovery Fund (STRF). The availability of and student eligibility for such funds vary by state, and not all states operate STRFs. Finally, the receipt of any of the above-mentioned benefits may have federal and state income tax implications, including the potential creation of a federal income tax liability for borrowers who have certain loans discharged.
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Introduction

In academic year (AY) 2017-2018, 6,700 institutions of higher education (IHEs), enrolling over 27 million postsecondary education students in AY2016-2017, participated in the federal student aid programs authorized under Title IV of the Higher Education Act of 1965 (HEA; P.L. 89-329, as amended). These IHEs ranged in sector, size, and educational programs offered. They comprised all sectors (i.e., public, private nonprofit, and proprietary), with some IHEs enrolling as few as three students and others enrolling over 190,000 in a single year. Offered educational programs varied from certificate programs in career and technical fields to doctoral and professional degree programs.

Most of these IHEs operate from year to year with few severe financial or operational concerns; however, each year, a few do face such concerns, which may cause them to close or significantly curtail operations. The recent closure of multiple large, proprietary (or private, for-profit) IHEs has brought into focus the extent to which a postsecondary student’s education may be disrupted by a school closure. However, even in instances of a small IHE’s closure, student concerns remain the same. Concerns include the following, among others: Can they continue their postsecondary education at another school? How will they finance future postsecondary educational pursuits? Are they liable for repaying loans they may have borrowed to pursue a postsecondary credential that they were unable to obtain because of an IHE’s closure?

This report provides an explanation of the options a postsecondary student may pursue in the event the IHE he or she attends closes, any financial relief that may be available to such students, and other practical implications for students following a school’s closure. First, this report describes the academic options available to such students, such as participating in a teach-out or transferring to a new IHE. Next, it discusses issues related to financing a postsecondary education, including the extent to which borrowers may have any loans borrowed to finance educational expenses discharged due to a school closure and whether future financial assistance, including federal student loans, Pell Grants, and GI educational benefits, may be available to students should they decide to continue their postsecondary education at another IHE. This report then describes additional relief that may be available to students who attended IHEs that closed, such as the potential to have tuition paid reimbursed through a state tuition recovery fund. Finally, this report describes some potential income tax implications for students when their IHE has closed, including the extent to which they may incur a federal income tax liability for loans discharged and whether higher education tax credits remain available to them in future years.

The Appendix provides a list of abbreviations used in this report.

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4 For additional information on some of these closures, see CRS Report R44068, Effect of Corinthian Colleges’ Close on Student Financial Aid: Frequently Asked Questions, archived, available to congressional clients upon request, and CRS Insight IN10577, The Closure of ITT Technical Institute, archived, available to congressional clients upon request.
Academic Options and Consequences

In the event of a school closure, currently enrolled students must consider their academic options, including whether they will continue pursuing their postsecondary education, and if so, where. Two options that may be available to students include teach-outs and credit transfer.

Teach-Out Plans and Agreements

To participate in the Title IV federal student aid programs, an IHE must, among other requirements, agree to submit a teach-out plan to its accrediting agency if it intends to close a location that provides 100% of at least one educational program offered by the IHE or if it intends to otherwise cease operations. As part of a teach-out plan, an IHE may enter into a teach-out agreement with another IHE to provide the closing IHE’s students with an educational program of similar content.

Teach-Out Plans

A teach-out plan is an institution’s “written plan that provides for the equitable treatment of students if [the IHE] ceases to operate before all students have completed their program of study.” Accrediting agencies establish the criteria IHEs must meet when submitting a teach-out plan; thus, there are no standard components of a teach-out plan. Typically, however, in a teach-out plan, an IHE may be required to include provisions for students to complete their programs of study within a reasonable amount of time, a communication plan to affected parties (e.g., faculty and students) informing them of the impending closure, and information on how students may access their institutional records.

Teach-Out Agreements

As part of a teach-out plan, an IHE may enter into a teach-out agreement with another IHE. A teach-out agreement is an agreement between the closing IHE and another IHE that provides the closing IHE’s students with a reasonable opportunity to complete their programs of study at the new IHE. Teach-out agreements are used when an IHE ceases operations before all of its enrolled students are able to complete their programs of study. Under a teach-out agreement, the new IHE must

- provide students with an educational program that is of an acceptable quality and reasonably similar in content, structure, and scheduling to that provided by the closing IHE;

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5 34 C.F.R. §668.14(b)(31). In addition, IHEs are required to submit teach-out plans to their accreditors when ED initiates an emergency action against or limitation, suspension, or termination of an IHE’s participation in an HEA Title IV program; when an IHE’s accrediting agency acts to withdraw, terminate, or suspend an IHE’s accreditation or preaccreditation; or when the IHE’s legal authorization to operate within a state is revoked.

6 HEA §487(f)(2).


8 34 C.F.R. §602.3.
• be accredited or preaccredited by a Department of Education (ED) recognized accrediting agency, remain stable, carry out its mission, and meet all obligations to its current students; and
• demonstrate that it can provide students with access to its services without requiring students to move or travel a substantial distance.\textsuperscript{9}

In addition, teach-out agreements may establish the cost of attendance for students being taught out.\textsuperscript{10}

When implemented, teach-out agreements may take a variety of forms. For instance, a teach-out agreement may provide that the teach-out institution will provide the faculty and student supports necessary to deliver the closing IHE’s educational programs at the closing IHE’s facilities for the remainder of the academic year in which the closing IHE ceases operations.\textsuperscript{11} In other instances, a teach-out agreement may provide educational programs to the closing IHE’s students at the teach-out IHE’s facilities.

In the event an IHE closes without a teach-out plan or agreement in place, the IHE’s accrediting agency must work with ED and appropriate state agencies to assist students in finding opportunities to complete their postsecondary education.\textsuperscript{12}

Credit Transfer

In lieu of a teach-out, students of closed IHEs may be able to continue their postsecondary education by transferring some or all of the credits earned at the closed IHE to another IHE. In general, credit transfer is the process of one institution (the accepting institution) measuring a student’s prior learning (typically via coursework) at another institution (the sending institution) and comparing that prior learning against educational offerings at the accepting institution. The accepting institution determines whether a student’s prior learning meets its standards and whether the prior learning is applicable to its educational programs. If it determines the prior learning meets its standards, the accepting institutions gives credit toward its educational programs for the prior learning, such that a student transferring credits need not repeat all or part of a program’s curriculum. Transfer-of-credit policies are determined by individual IHEs.

To smooth the credit transfer process, some IHEs have entered into articulation agreements. Articulation agreements are agreements between two or more IHEs demonstrating that a student’s prior learning from a sending IHE meets the accepting IHE’s standards. Typically, they guarantee acceptance of at least some credits earned at the sending institution by the accepting institution.

The HEA does not require Title IV participating IHEs to maintain transfer-of-credit policies nor does it specify requirements for transfer-of-credit policies for IHEs that do have them. The HEA does, however, require that Title IV participating IHEs make publicly available any transfer-of-credit policies they may have in place.\textsuperscript{13} In disclosing transfer-of-credit policies, accepting IHEs

\textsuperscript{9} 34 C.F.R. §602.24(c).
\textsuperscript{11} See, for example, Southern New Hampshire University, “Southern New Hampshire University to Lead ‘Teach-Out’ of all Daniel Webster College Programs,” press release, September 13, 2016.
\textsuperscript{12} 34 C.F.R. §602.24(d).
\textsuperscript{13} HEA §485(h).
must include information on the criteria the institution uses in evaluating credit transfers, and all institutions that are parties to articulation agreements must disclose a list of IHEs with which it has articulation agreements.

Students who attended a closed IHE may decide to continue their postsecondary education at another IHE and may wish to transfer credits earned at the closed IHE to the new IHE. Typically, students must initiate the credit-transfer process by expressing interest in transferring credit to another IHE. The IHE would then inform the student of next steps the student must take to enroll. Because IHEs set their own credit transfer criteria, credit transfer may not be guaranteed. Thus, some students may have all or a large proportion of their previously earned credits transferred to an accepting IHE and may experience little to no disruption or delay in their postsecondary educational pursuits, while others may have few or no credits transferred to an accepting IHE and may experience significant disruptions and delays in their postsecondary education. In addition, a student may incur greater financial obligations (e.g., student loans) if he or she must repeat coursework because credit from the closed school did not transfer.

Finally, students who successfully transfer some or all of their previously earned credits would be required to meet the accepting IHE’s satisfactory academic progress (SAP) policies to maintain eligibility to receive Title IV funds at the accepting IHE. IHEs may establish their own SAP policies, but these policies must meet minimum federal standards, which must establish a minimum grade point average (or equivalent) and a maximum time frame in which students must complete their education program (pace of completion). Only transfer credits that count toward a student’s educational program at the accepting IHE are included in the accepting IHE’s calculation of SAP. Thus, if a student is unable to transfer any credits from a closed IHE to another IHE, the student’s previously earned credits will not count toward the accepting IHE’s SAP calculation and would not have the potential to affect the student’s aid eligibility with respect to SAP at the new IHE. However, should some or all of a student’s previously earned credits from a closed IHE transfer to another IHE, depending on the accepting IHE’s specific SAP policy, a student’s Title IV eligibility may be affected such that he or she may not be meeting the IHE’s SAP policies and thus may be ineligible for Title IV aid at the accepting IHE.

In cases, a teach-out agreement may specify that the credits a student earned at the closed institution will transfer to the new IHE. See, for example, Higher Learning Commission, “Teach-Out Requirements: Provisional Plan and Teach-Out Agreements,” March 2017, https://downloadna11.springcm.com/content/DownloadDocuments.aspx?Selection=Document%2C2C73d8aaaf-d1fb-df11-bf75-001cc448df6a%3B&aid=5968, accessed February 5, 2019.

For information on how often credits transfer, see Sean Anthony Simone, Transferability of Postsecondary Credit Following Student Transfer or Coenrollment: Statistical Analysis Report, National Center for Education Statistics, NCES 2014-163, August 2014.

34 C.F.R. §686.34. A student’s pace of completion is calculated by dividing the total number of credits a student has successfully completed by the number of credits the student has attempted. A student becomes ineligible for Title IV aid when it is mathematically impossible for him or her to complete their course of study within 150% of the length of the program (e.g., six years for a full-time, full-year four-year program) for undergraduate students and within the maximum time frame established by the IHE for graduate students.


In general, it appears that a student’s pace of completion is unlikely to be affected by a credit transfer, as typically, only successfully completed courses at the original IHEs may be transferred to an accepting institution. However, successful course completion is defined by individual IHEs. Thus, an accepting IHE defines successful completion as any grade higher than an F (or its equivalent), then a student might be able to transfer credits from a class in which he or she earned, for instance, a D. This D would be included in the accepting IHE’s calculation of the student’s grade point average for purposes of determining SAP. Such grades may have the effect of bringing the student’s GPA below the federally required C minimum, such that he or she may become ineligible for Title IV student aid at the accepting institution.
Financial Options and Consequences

Along with considering academic options in the event of a school closure, students may also need to consider the financial options available to them, as they may have received financial assistance to help finance their education at the closed school and may need to seek financial assistance should they decide to continue pursuing a postsecondary education. Considerations for students who borrowed funds (or parents who borrowed funds on behalf of a student) to finance their education at a closed school include whether they are responsible for repaying any loans borrowed to attend the school. Considerations for students who wish to continue their education at another IHE include the extent to which their eligibility for various forms of financial aid (e.g., Direct Loans, Pell Grants, GI Bill Educational Benefits) may be affected by their previous use of those benefits at the closed school.

Loan Discharge

In some instances, individuals who borrowed funds to finance postsecondary education expenses may be provided some relief from being required to repay their loans, depending on the type of loan they seek to have discharged and specific borrower circumstances.

Federal Student Loans

Students who attended a school that closed (or the parents of students who attend a school that closed) may have borrowed federal student loans to help finance their postsecondary education at the closed school. For HEA Title IV federal student loans (i.e., loans made under the Direct Loan [DL], Federal Family Education Loan [FFEL], and Perkins Loan programs), borrowers may be provided some relief from being required to repay their federal student loans through a closed school loan discharge. In addition, borrowers who are ineligible for a closed school loan discharge may, in certain circumstances, seek debt relief on their Title IV student loans by asserting a borrower defense to repayment (BDR) for certain acts or omissions of an IHE, if the cause of action directly relates to the loan or educational services for which the loan was provided. The availability of a BDR claim may be closely related to a school’s closure, as oftentimes, a BDR claim is predicated on misleading representations of an IHE relating to the educational services provided, and in recent years allegations of misrepresentation have played a part in the ultimate closure of some IHEs.20

Previously, regulatory provisions addressed closed school discharge standards and procedures. They also addressed BDR standards and procedures, but in a somewhat limited manner. On November 1, 2016, ED promulgated new regulations (hereinafter, “the 2016 regulations”) intended to create a more robust set of standards and streamlined procedures for assessing BDR claims and to make some changes to the closed school discharge procedures.21 These regulations were scheduled to take effect on July 1, 2017, but prior to the effective date, ED issued a Final

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20 For instance, in 2014 ED placed restrictions to Title IV aid on IHEs owned by Corinthian Colleges, Inc. (CCI) to address concerns relating to a variety of practices, including inconsistencies in job placement rates that had been presented to students. In response to its limited access to federal student aid funds, CCI closed and sold many of its IHEs. CRS Report R44068, Effect of Corinthian Colleges’ Closure on Student Financial Aid: Frequently Asked Questions, archived, available to congressional clients upon request.

Rule establishing July 1, 2019, as the new effective date for the regulations. Following a series of lawsuits, however, a court vacated the delay of the 2016 regulations. The 2016 regulations went into effect October 16, 2018, and ED is currently working to fully implement the 2016 regulations. On July 31, 2018, ED issued a new Notice of Proposed Rulemaking to revise the BDR standards. A Final Rule has not yet been issued, and it appears that the potential new BDR regulations would not go into effect until at least July 2020.

The following section of the report describes the closed school discharge and BDR regulations, as in effect on October 16, 2018.

**Closed School Loan Discharge**

Students who attended a school that closed (or their parents) may be eligible to have the full balance of the outstanding HEA Title IV loans they borrowed to attend the IHE discharged. In general, borrowers of Title IV loans may be eligible to have the full balance of their outstanding HEA Title IV loans discharged (including any accrued interest and collection costs) if they, or the student on whose behalf a parent borrowed in the case of Parent PLUS Loans, are unable to complete the program in which they enrolled due to the closure of the school. Borrowers who have their loans discharged due to a school closure are also eligible to be reimbursed for any amounts previously paid or collected on those loans, and if any adverse credit history was associated with the loan (e.g., default), the loan discharge will be reported to credit bureaus so that they may delete the adverse credit history associated with the loan.

**Closed School Loan Discharge Eligibility**

Typically, to be eligible for loan discharge due to school closure, a student must have been enrolled in an IHE when it closed or must have withdrawn from the IHE within 120 days prior to its closure. In addition, the student must have been unable to complete his or her program of

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27 81 Federal Register 75926, November 1, 2016.

28 HEA §437(c)(1); HEA §455(a)(1); HEA §464(g). In some instances, borrowers who are ineligible to have their federal student loans discharged due to school closure may be able to seek debt relief for their DL and FFEL program loans for a variety of other reasons. For additional information, see CRS Report R40122, Federal Student Loans Made Under the Federal Family Education Loan Program and the William D. Ford Federal Direct Loan Program: Terms and Conditions for Borrowers.

29 34 C.F.R. §§674.33(g)(2); 682.402(d)(2); 685.214(b).

30 The Secretary may extend the 120-day period in exceptional circumstances.
study at the closed school or in a comparable program at another IHE, either through a teach-out agreement or by transferring any credits to another IHE.

If the closing school offers the option for students to complete their education through a teach-out agreement with another IHE, a student may refuse the option, and the borrower may still qualify for loan discharge. However, in general, a borrower may not qualify for a closed school discharge in the following scenario: a student refuses the teach-out, later enrolls at another IHE in a program comparable to the one in which he or she had been enrolled, receives transfer credit for work completed at the closed school, and completes the program at the new IHE.

Alternatively, if a student transfers credits to a new school but completes an entirely different program of study at the new school, then the borrower is eligible for loan discharge, regardless of the fact that some credits from the closed IHE may have transferred to the new IHE. This is because the program at the new school is entirely different than the one for which the loans were intended at the previous school.

Finally, to obtain discharge a borrower must cooperate with ED in any judicial or administrative proceeding brought by ED to recover amounts discharged from the school. If a borrower fails to cooperate with ED, the loan discharge may be revoked.

Closed School Loan Discharge Procedures

Borrowers may have their loans discharged in one of two ways: (1) by applying for a closed school loan discharge or (2) by having their loans automatically discharged by the Secretary of Education (the Secretary).

Borrowers applying for a closed school discharge must fill out the closed school loan discharge application and return it to their loan servicer. Generally, while a borrower’s loan discharge application is being considered, the borrower’s loan is placed in forbearance until a discharge decision is made. Under forbearance, a borrower is able to temporarily stop making payments or reduce the monthly payments on his or her federal student loans. During this time, interest

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31 There is no formal definition of comparable program. However, information made available by ED to former Corinthian Colleges students provided an illustrative example of when a program might be considered comparable: “for instance, if you were taking a criminal justice program and you transferred to another criminal justice program, that would be a transfer to a similar program.” Borrowers self-certify whether their new program of study is similar to their program of study at the closed school. See U.S. Department of Education, Office of Federal Student Aid, “Information About Debt Relief for Corinthian Colleges Students,” https://studentaid.ed.gov/sa/about/announcements/corinthian, accessed October 25, 2018.


33 Ibid.


35 For instance, the borrower may be required to provide testimony supporting a request for discharge.

36 34 C.F.R. §§674.33(g), 682.402(d), 685.214(c) & (d).


38 34 C.F.R. §§674.33, 682.211, 685.205. Unlike the FFEL and DL programs, the Perkins Loan program regulations do not specify that an IHE must place a borrower’s loan in forbearance while his or her closed school loan discharge application is being processed; however, the regulations do state that an IHE may place a borrower’s loan in forbearance due to several specified reasons “or for other acceptable reasons.” In addition, in certain stages of the closed school discharge application process, an IHE (or ED, in the case of Perkins Loans held by ED) may be required to suspend efforts to collect on a borrower’s Perkins Loans.
continues to accrue on both subsidized and unsubsidized loans. In addition, collections on an eligible defaulted loan cease, although a borrower may continue to make payments on the loan.

Borrowers may initiate the closed school loan discharge process on their own; however, the Secretary is required to identify all borrowers who may be eligible for a closed school discharge upon a school’s closure and mail to each borrower a discharge application and an explanation of qualifications and procedures for obtaining a discharge, if the borrower’s address is known. After the Secretary sends notice to a borrower, the Secretary suspends any effort to collect a borrower’s defaulted loans. The borrower then has 60 days in which to submit a closed school discharge application. If the borrower fails to submit such an application within the 60-day time frame, the Secretary resumes collections and again provides the borrower with another discharge application and an explanation of qualifications and procedures for obtaining a discharge. Should a borrower not submit a closed school discharge application within the 60-day time frame, he or she may still submit a closed school discharge application at any time for consideration.

Alternatively, a borrower’s loans will be automatically discharged by the Secretary, if with respect to schools that closed on or after November 1, 2013, the Secretary determines that the borrower did not subsequently reenroll in any Title IV eligible institution within three years after the school closed. A borrower’s loans also may be automatically discharged if the Secretary determines the borrower qualifies for the discharge based on information within ED’s possession.

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39 In certain circumstances, including when an IHE submits a teach-out plan to its accrediting agency because it intends to close a location at which 100% of at least one program is offered or otherwise cease operations, the IHE is required to provide to enrolled students a closed school discharge application and a written disclosure describing the benefits and consequences of a closed school discharge. 34 C.F.R. §668.14(b)(32).

40 This paragraph generally describes the procedures associated with closed school loan discharges as specified in regulations. The descriptions herein are drawn from the regulations specific to the Direct Loan program (34 C.F.R. §685.214), but are generally applicable to the Perkins Loan and FFEL programs as well. However, because parties other than ED may be responsible for administrative functions associated with closed school discharges in the Perkins Loan and FFEL programs, the tasks described in this report may vary somewhat from what Perkins Loan and FFEL program loan holders other than ED may be required to undertake. Closed school discharge procedures specific to the Perkins Loan program and the FFEL program can be found at 34 C.F.R. §674.33 and 34 C.F.R. §682.402, respectively.

41 If the borrower’s address is unknown, ED attempts to locate the borrower by consulting with a variety of parties, including the closed school, the school’s accrediting agency, and the school’s licensing agency. 34 C.F.R. §685.214(f)(3).

42 Upon resuming collection on a borrower’s loans, ED grants forbearance of principal and interest for the period during which the collection activity was suspended and may capitalize any interest accrued but not paid during that time. 34 C.F.R. §685.214(f)(4).

43 34 C.F.R. §685.214(f)(1).

44 In the instance of a FFEL program loan, ED may automatically discharge a borrower’s FFEL program loan if he or she qualifies for and received a closed school discharge of his or her Direct Loan program or Perkins Loan program loans. Similarly, ED may automatically discharge a borrower’s Perkins Loan program loan if he or she qualified for and received a closed school loan discharge of his or her Direct Loan program or FFEL program loan and “was unable to receive a discharge on his or her … Perkins Loan because the Secretary of Education lacked statutory authority to discharge the loan.” See 34 C.F.R. §§682.402(d)(8), 674.33(g)(3). The Perkins Loan provisions appear to apply largely Perkins Loan program loans made prior to 1998, when ED did not have legal authority to discharge such loans due to a school’s closure. The rationale behind the FFEL program loan provisions is not explicitly identified in materials located and reviewed for this report. See 64 Federal Register 41236, July 29, 1999.
Relief Provided

If a borrower receives a closed school discharge, the full balance of the outstanding Title IV loan borrowed to attend the IHE is discharged and the borrower is qualified to be reimbursed for any amounts previously paid or collected on those loans. In addition, for loans that were considered in default, ED is to consider such loans not in default following discharge, and the borrower is to regain eligibility to receive additional Title IV assistance.\(^{45}\) Finally, ED is to update consumer reporting agencies so that they may delete any adverse credit history associated with the loan.\(^{46}\)

Borrower Defense to Repayment

Even if borrowers who attended a closed school are ineligible for a closed school loan discharge, they may, in certain circumstances, seek debt relief on their Title IV student loans by asserting a borrower defense to repayment (BDR) certain acts or omissions of an IHE, if the cause of action directly relates to the loan or educational services for which the loan was provided. The availability of a BDR claim may be closely related to a school’s closure, as oftentimes, a BDR claim is predicated on misleading representations of an IHE relating to the educational services provided, and in recent years, allegations of misrepresentation have played a part in the ultimate closure of some IHEs.\(^{47}\) Whether a borrower may seek this type of relief depends on the type of Title IV loan borrowed. The standard under which a BDR may be reviewed also depends on the type of Title IV loan borrowed and when the loan was disbursed. Newly promulgated BDR procedures apply to many, but not all, BDR claims and vary depending on the type of Title IV loan.

If a borrower’s BDR is successful, ED is to determine the amount of debt relief to which the borrower is entitled, which can include relief from repaying all or part of the outstanding loan balance and reimbursement for previous amounts paid toward or collected on the loan. Additionally, if an adverse credit history was associated with the loan (e.g., default), the loan discharge is to be reported to credit bureaus so that they may delete the adverse credit history associated with the loan.\(^{48}\)

Applicable Borrower Defense to Repayment Standards

The HEA specifies that Direct Loan borrowers may assert as a defense to repayment certain “acts or omissions of an institution of higher education.”\(^{49}\) Although this statutory language is specific to Direct Loans, implementing regulations have expanded the instances in which a borrower of a non-Direct Loan may assert a BDR claim. Thus, loans that are potentially eligible for discharge under a BDR claim include Direct Loan program loans and Federal Family Education Loan

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\(^{45}\) Individuals become ineligible for additional Title IV student aid if they default on a Title IV loan. HEA §484(a)(3).

\(^{46}\) 34 C.F.R. §674.33(g)(2), 682.402(d)(2), 685.214(b).

\(^{47}\) For instance, in 2014, ED placed restrictions to Title IV aid on IHEs owned by Corinthian Colleges, Inc. (CCI) to address concerns relating to a variety of practices, including inconsistencies in job placement rates that had been presented to students. In response to its limited access to federal student aid funds, CCI closed and sold many of its IHEs. CRS Report R44068, Effect of Corinthian Colleges’ Closure on Student Financial Aid: Frequently Asked Questions, archived, available to congressional clients upon request.

\(^{48}\) 34 C.F.R. §685.222(i).

\(^{49}\) HEA §455(h).
program loans and Perkins Loans program loans, if they are first consolidated into a Direct Consolidation Loan.\footnote{Other non-DL program loans that are potentially eligible for discharge under a BDR claim if they are first consolidated into a Direct Consolidation Loan include Health Professions Student Loans, Loans for Disadvantaged students made under Title VII-A-II of the Public Health Service Act, Health Education Assistance Loans, and Nursing Loans made under part E of the Public Health Service Act. 34 C.F.R. §685.212(k)(2).}

In addition, even if a FFEL program loan is not consolidated into a Direct Consolidation Loan, FFEL program regulations specify instances in which a FFEL program loan may not be legally enforceable, such that a borrower need not repay it. ED has stated that the claims a borrower could bring as a defense against repayment under the FFEL program are the same as the pre-July 1, 2017, standards (discussed later in this report) that could be brought under the DL program.\footnote{34 C.F.R. §685.222(b)-(d).} Perkins Loan program loans that are not consolidated into Direct Consolidation Loans may not assert a BDR claim.

In general, two separate BDR standards may be applied to eligible student loans under the Direct Loan program regulations. For eligible loans made prior to July 1, 2017, a borrower may assert as a defense to repayment an IHE’s acts or omissions that “would give rise to a cause of action against the school under applicable State law,” and the IHE’s acts or omissions must relate to the making of the loan for enrollment at the IHE or the provision of educational services for which the loan was provided\footnote{A substantial misrepresentation is “[a]ny false, erroneous, or misleading statement an [IHE] or one of its representatives…makes directly or indirectly to a student, prospective student or any member of the public, or to an accrediting agency, to a State agency, or to the Secretary” on which “the person to whom it was made could reasonably be expected to rely, or has reasonably relied, to that person’s detriment.” An IHE is deemed to have made a substantial misrepresentation when it (or its representatives) makes a “substantial misrepresentation about the nature of its educational programs, its financial charges, or the employability of its graduates.” 34 C.F.R. §688.71(b) and (c).} (hereinafter, “pre-July 1, 2017, standard”). For eligible loans made on or after July 1, 2017, a borrower may assert as a defense to repayment one of the following, as it relates to the making of a borrower’s loan for enrollment at the IHE or the provision of the educational services for which the loan was made (hereinafter, “post-July 1, 2017, standard”):\footnote{To assert a successful BDR claim, FFEL borrowers must satisfy the general pre-July 1, 2017, BDR standards and must also prove additional components, such as showing that the FFEL lender offered payment or other benefits to the IHE for referring borrowers to the specific FFEL lender. These standards apply to FFEL program loans held by private sector and state-based entities and those owned by ED. 34 C.F.R. §682.209(g) and U.S. Department of Education, “Notice of Interpretation,” 60 Federal Register 37768-37770, July 21, 1995.}

- A substantial misrepresentation by an IHE that the borrower “reasonably relied on to the borrower’s detriment when the borrower decided to attend, or to continue attending, the school” or decided to take out certain loans;\footnote{A contract between an IHE and a borrower could include, for instance, an enrollment agreement, a school catalog, or a student handbook. Department of Education, “Student Assistance General Provisions,” Federal Perkins Loan Program, Federal Family Education Loan Program, William D. Ford Federal Direct Loan Program, and Teacher Education Assistance for College and Higher Education Grant Program,” 81 Federal Register 39341, June 16, 2016.}
- A nondefault, contested state or federal court judgment against an IHE; or
- A breach of contract by an IHE,\footnote{55 A contract between an IHE and a borrower could include, for instance, an enrollment agreement, a school catalog, or a student handbook. Department of Education, “Student Assistance General Provisions,” Federal Perkins Loan Program, Federal Family Education Loan Program, William D. Ford Federal Direct Loan Program, and Teacher Education Assistance for College and Higher Education Grant Program,” 81 Federal Register 39341, June 16, 2016.} where an IHE failed to perform obligations under the terms of a contract with a student, such as the provision of specific programs or services.

As indicated above, the BDR standard applied in a borrower’s case may depend to a large extent on the date on which a borrower’s loans were disbursed. However, other considerations that relate
to the type of federal student loan made also play a role in determining which BDR standard may apply in a borrower’s case. In general, for DL program loans not paid off through a Direct Consolidation Loan, the BDR standard used would depend on the date on which a borrower’s loans were disbursed. For FFEL program loans not paid off through a Direct Consolidation Loan, the pre-July 1, 2017, standard would apply. For DL program loans paid off through a Direct Consolidation Loan, the BDR standard used would depend on the date on which the underlying Direct Loan was disbursed. For eligible non-DL program loans paid off through a Direct Consolidation Loan, the BDR standard used would depend on the date on which the Direct Consolidation Loan was made.\(^{56}\) Direct Consolidation Loans comprising underlying loans disbursed both before and after July 1, 2017, would necessarily have been disbursed after July 1, 2017. Thus, in this scenario, the post-July 1, 2017, standard would apply to any eligible non-DL program loans paid off through the Direct Consolidation Loan and either the pre- or post-July 1, 2017, standard would apply to any Direct Loans paid off through the Direct Consolidation Loan, depending on the date the underlying Direct Loan was disbursed. Table 1 depicts the BDR standard that would be applied in a BDR proceeding based on type of federal student loan at issue and the date on which the loan was disbursed.

Table 1. Borrower Defense to Repayment Standard Used in a BDR Proceeding

By loan type and disbursement date

<table>
<thead>
<tr>
<th>Loan Type &amp; Disbursement Date</th>
<th>BDR Standard Applied</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Pre-July 1, 2017</td>
</tr>
<tr>
<td>DL Program Subsidized and Unsubsidized Loans</td>
<td>✓</td>
</tr>
<tr>
<td>Disbursed pre-July 1, 2017</td>
<td>✓</td>
</tr>
<tr>
<td>Disbursed on or post-July 1, 2017</td>
<td>✓</td>
</tr>
<tr>
<td>FFEL Program Subsidized, Unsubsidized, and Consolidation Loans(^a)</td>
<td>✓</td>
</tr>
<tr>
<td>Disbursement date inapplicable(^b)</td>
<td>✓</td>
</tr>
<tr>
<td>DL Program Consolidation Loans</td>
<td>✓</td>
</tr>
<tr>
<td>Underlying DL Program Subsidized &amp; Unsubsidized Loans</td>
<td>✓</td>
</tr>
<tr>
<td>Underlying loan disbursed pre-July 1, 2017</td>
<td>✓</td>
</tr>
<tr>
<td>Underlying loan disbursed on or post-July 1, 2017</td>
<td>✓</td>
</tr>
<tr>
<td>Underlying Eligible Non-DL Program Loans(^c)</td>
<td>✓</td>
</tr>
<tr>
<td>Direct Consolidation Loan disbursed pre-July 1, 2017</td>
<td>✓</td>
</tr>
<tr>
<td>Direct Consolidation Loan disbursed on or post-July 1, 2017</td>
<td>✓</td>
</tr>
</tbody>
</table>


\(^a\) FFEL program borrowers must satisfy the general pre-July 1, 2017, BDR standards and must prove additional components, such as showing that the FFEL lender offered payment or other benefits to the IHE for referring borrowers to the specific FFEL lender. 34 C.F.R. §682.209(g).

\(^b\) 34 C.F.R. §685.222.

\(^c\) 34 C.F.R. §685.222.
b. The SAFRA Act (P.L. 111-152, Title II, Part A) terminated the authority to make new FFEL program loans after June 30, 2010.

c. Eligible non-DL program loans include FFEL program loans, Perkins Loan program loans, Health Professions Student Loans, Loans for Disadvantaged students made under Title VII-A-II of the Public Health Service Act, Health Education Assistance Loans, and Nursing Loans made under part E of the Public Health Service Act.

**BDR Procedures**

Regulations establish two separate processes through which a BDR claim may be asserted on a borrower’s DL program loans: an individual claim process and a group claim process. This section of the report describes the 2016 regulations’ BDR procedures for DL program loans (including Direct Consolidation Loans that repaid eligible non-DL program loans for which a borrower asserts a BDR claim) under which BDR claims may be more likely to be asserted, as DL program borrowers account for approximately 80% of all borrowers with outstanding Title IV loans. The procedures described herein would not apply to ED-owned FFEL program loans or to FFEL programs loans held by private and state-based entities that are not consolidated into Direct Consolidation Loans. For such ED-owned FFEL program loans, ED would review and adjudicate any BDR claims. For such FFEL program loans not owned by ED, BDR claims procedures may vary by loan holder.

To assert a BDR claim as an individual, a borrower must submit a BDR application, which among other items requires the borrower to provide evidence that supports his or her BDR claim. Upon receipt of the application and while the BDR claim is evaluated, ED places any nondefaulted Direct Loans into forbearance and ceases collections on defaulted loans. If a borrower with a FFEL program loan files a BDR claim with ED, ED notifies the lender or loan

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57 Prior to the current regulations going into effect on October 16, 2018, regulations did not specify formal BDR procedures. Therefore, ED had established informal procedures through which borrowers were able to seek BDR relief. Because the current regulations’ implementation date was delayed from July 1, 2017, to October 16, 2018, ED has not yet fully implemented the procedures specified in the 2016 regulations.


59 Under the FFEL program, loans were originated and serviced by private sector and state-based lenders and were funded with nonfederal capital. ED guaranteed lenders against loss (e.g., through borrower default or discharge due to death or permanent disability). Although FFEL program loans were last disbursed in 2010, many remain outstanding. In some instances, private or state-based lenders continue to service FFEL program loans. In other instances, ED has purchased FFEL program loans from the lenders and is now the owner of the loans. In these cases, the loans are serviced by ED-contracted student loan servicers.

60 Upon submitting a BDR claim on an ED-owned FFEL program loan that is not consolidated into a Direct Consolidation Loan, the borrower is to be offered the opportunity to place the loan in forbearance while the claim is being reviewed. CRS email communication with U.S. Department of Education personnel on December 10, 2018.

61 Borrowers of such loans must contact the holder of their FFEL program loans for information on the BDR process. Upon submitting a BDR claim on an FFEL program loan not owned by ED, the borrower is offered to opportunity to request that his or her loan be placed in forbearance while the claim is being reviewed. U.S. Department of Education, Application for Borrower Defense to Loan Repayment, OMB No. 1845-0146, Exp. Date December 31, 2019.

62 34 C.F.R. §685.222(e). In January 2017, ED promulgated regulations that updated its general hearing procedures for actions to establish liability against an IHE and establishing procedural rules governing recovery proceedings under the 2016 BDR regulations. These procedural requirements are beyond the scope of this report. See Department of Education, “Student Assistance General Provisions,” 82 Federal Register 6253, January 19, 2017.

63 See U.S. Department of Education, “Application for Borrower Defense to Loan Repayment,” OMB No. 1845-0146, Exp. December 31, 2019. This form was approved prior to implementation of the current regulations.

64 During forbearance, interest continues to accrue on both subsidized and unsubsidized loans. A borrower may opt out of forbearance and continue making payments on his or her loan.

65 A borrower may continue making payments under a rehabilitation agreement or other repayment agreement on the defaulted loan.
holder, as appropriate.66 The lender places the loan in forbearance in yearly increments,67 and the loan holder ceases collection on any defaulted loans while a borrower’s BDR claim is being evaluated.68 If ED determines that the borrower would be eligible for relief if he or she consolidated the FFEL program loan into a Direct Consolidation Loan, the borrower would then be able to consolidate the loan into a Direct Consolidation Loan69 and receive BDR relief.70 If ED determines that the borrower would not qualify for BDR, then the loan is removed from forbearance or collections resume, as appropriate.71

To determine whether an individual qualifies for BDR relief, the Secretary designates an ED official to review the borrower’s application and resolves the claim through a fact-finding process. As part of that process, ED notifies the IHE against which the BDR claim is asserted and reviews any evidence submitted by the borrower and other relevant information, such as ED records and any submissions from the IHE. After the fact-finding process, the ED official issues a written decision on the claim. If the claim is approved in full or in part, ED notifies the borrower of the reason for the denial, along with other relevant information.72 The decision made by the ED official is “final as to the merits of the claim and any relief that may be granted on the claim.”73 However, if the borrower’s claim is denied in full or in part, the borrower may request that ED reconsider his or her claim upon the identification of new evidence. In addition, ED may reopen a BDR application at any time to consider evidence that was not considered in the previous decision.

Regulations also establish a group process for BDR claims.74 Under these procedures, upon consideration of factors such as a common set of facts and claims or fiscal impact, the Secretary may initiate a process to determine whether a group of borrowers has a BDR claim. ED may identify members for a group BDR claim by either consolidating applications filed by individuals in the above-described process that have common facts and claims or by determining that there are common facts and claims that apply to borrowers who have not filed individual applications. Loans of borrowers who have filed individual claims that are consolidated into a group BDR claim remain in forbearance or suspended collections as described above, and loans of identified group members who have not filed individual claims are placed in forbearance or suspended collections as described above. ED notifies identified group members of the group proceeding

66 The regulations are silent regarding whether lenders of Perkins Loans are required to place Perkins Loans into forbearance or to cease collections on Perkins Loans should a Perkins Loan borrower file a BDR claim with ED. ED has indicated it is not its current practice to request or require Perkins Loan holders or servicers to place borrowers into forbearance or to cease collections on a Perkins Loan for purposes of BDR. CRS email communication with U.S. Department of Education personnel on November 6, 2018.

67 A borrower may opt out of forbearance and continue making payments on his or her loan. 34 C.F.R. §682.211(i)(7).

68 Regulations specify that upon receipt of a BDR application, ED will notify the borrower of the option to continue making payments under a rehabilitation agreement or other repayment agreement on a defaulted loan. It appears this might apply in the instance in which a borrower of a FFEL program loan first submits a BDR application to ED, prior to loan consolidation. 34 C.F.R. §685.222(e)(2)(ii)(C).

69 If borrowers choose to not consolidate their FFEL program loans into a Direct Consolidation Loan, they may still pursue a BDR claim under the FFEL program BDR standards and procedures.

70 The loan would remain in forbearance until the loan is consolidated. 34 C.F.R. §682.211(i)(7).

71 34 C.F.R. §§682.211(i)(7), 682.410(b)(6)(iii).

72 34 C.F.R. §685.222(e).

73 34 C.F.R. §685.222(e)(5).

74 34 C.F.R. §685.222(f).
and informs them that they may opt out of the group proceeding.\textsuperscript{75} ED also notifies the school against which the group BDR claim is asserted.

For the fact-finding portion of a group BDR claim, one set of procedures applies to a BDR claim relating to loans made to attend a school that has closed\textsuperscript{76} and from which there is no financial protection or other entity that ED may recover losses from associated with the BDR claims.\textsuperscript{77} Another set of fact-finding procedures applies to BDR claims relating to loans made to attend a school that has closed and for which there are financial protections or other entities from which ED may recover losses associated with BDR claims, or that is open. If the claim relates to loans made to attend a school that has closed and for which there is no financial protections or entities against ED may recover, a hearing official considers any evidence and arguments presented by ED on behalf of the group,\textsuperscript{78} along with any additional information such as ED records or responses from the school that the ED official considers necessary. After the fact-finding process, the ED official issues a written decision on the claim. As with the individual claims process, if the group claim is approved in full or in part, ED notifies the borrowers of the relief provided. If the claim is denied in full or in part, ED notifies the borrowers of the reason for the denial, along with other relevant information. The decision made by the ED official is “final as to the merits of the group borrower defense and any relief that may be granted on the group claim.”\textsuperscript{79} However, if relief for the group has been denied in full or in part, an individual borrower may file a claim for individual relief as previously described. In addition, ED may reopen a BDR application at any time to consider evidence that was not considered in the previous decision.\textsuperscript{80}

Group BDR procedures for a claim that relates to loans made to attend a closed school for which there are financial protections or entities from which ED may recover losses or to loans made to attend an open school are substantially similar to those procedures for group BDR claims for closed schools without financial protections described above.\textsuperscript{81} However, in addition to the above-described procedures, the IHE against which the claim is brought is given the opportunity to present evidence and arguments during the fact-finding process. In addition, the school or the ED official who presented the group’s BDR claims may appeal the decision of the hearing official within 30 days after the decision is issued and received by the school and the ED official. Should an appeal be made, the hearing official’s decision does not take effect pending the appeal. The Secretary issues a final decision on the appealed claim. If relief for the group has been denied in full or in part, and after a final decision has been made (either following an appeal by the school or the ED official or after 30 days from the hearing official’s decision have passed), an individual borrower may file a claim for individual relief as previously described. Additionally, ED may reopen a BDR application at any time to consider evidence that was not considered in the previous decision.

\textsuperscript{75} It is unclear how a borrower who has successfully asserted an individual BDR claim may be affected by any subsequent group proceeding.

\textsuperscript{76} This standard would apply regardless of whether the borrower(s) were enrolled at the IHE at the time it closed.

\textsuperscript{77} Financial protections from which ED may recover losses associated with BDR claims include, for example, letters of credit. Other entities from which ED may recover such losses include, for examples, affiliates of a closed IHE.

\textsuperscript{78} The ED official may also present evidence and arguments, as necessary, on behalf of individual group members. 34 C.F.R. §685.222(g)(1).

\textsuperscript{79} 34 C.F.R. §685.222(g)(2).

\textsuperscript{80} 34 C.F.R. §685.222(g)(4).

\textsuperscript{81} 34 C.F.R. §685.222(f).
Finally, to obtain relief a borrower must cooperate with ED in the relevant individual or group BDR proceeding. If a borrower fails to cooperate with ED, the relief may be revoked.\textsuperscript{82}

\textit{Relief Provided}

Regulations specify the relief that may be afforded to a borrower who, as an individual or as part of a group, successfully asserts a BDR.\textsuperscript{83} This section of the report focuses on BDR relief available to borrowers with DL program loans, including Direct Consolidation Loans that repaid eligible non-DL program loans. However, it should be noted that borrowers of FFEL program loans that have not been consolidated into Direct Consolidation Loans are eligible to have all or part of their loan discharged, and may be eligible to be reimbursed for payments previously paid toward or collected on the loans if certain conditions are met.\textsuperscript{84} Borrowers of Perkins Loans are ineligible for BDR relief unless they first consolidate their loans into a Direct Consolidation Loan.

For Direct Loans, if a borrower defense is approved, ED (either the ED official in an individual BDR claim or the hearing official in the group BDR claim) determines the appropriate amount of relief to award the borrower. Relief provided can include a discharge of all or part of the loan amounts owed to ED on the loan at issue. A borrower may also be eligible to have all or part of amounts previously paid toward or collected on his or her loan reimbursed by ED. Payments made or collections on Direct Loans, including Direct Consolidation Loans that repaid eligible non-DL program loans, are reimbursable by ED if the borrower asserted the BDR claim within the applicable statute of limitations\textsuperscript{85} and the payments were made directly to ED.\textsuperscript{86} Reimbursements are to equal the amount by which the payments or collections on the loans (or portion of the loan in the case of Direct Consolidation Loans to which a BDR claim applied to some, but not all, of the underlying loans) exceed the amount of the loan that was not discharged.\textsuperscript{87}

To calculate the amount of relief to be provided, ED takes into account a variety of factors, depending on the basis on which the BDR claim was brought.

- **Substantial misrepresentation**: ED is to factor the borrower’s cost of attendance to attend the IHE, the value of the education the borrower received, the value of the education that a reasonable borrower in the borrower’s circumstances would have received, the value of the education the borrower

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\textsuperscript{82} 34 C.F.R. §685.222(j).
\textsuperscript{83} 34 C.F.R. §685.222(i).
\textsuperscript{84} In general, FFEL program loans (both those owned and not owned by ED) may be discharged if a borrower satisfies the general pre-July 1, 2017, BDR standards and proves additional components, such as showing that the FFEL lender offered payment or other benefits to the IHE for referring borrowers to the specific FFEL lender. 34 C.F.R. §682.209(g). Payments made on FFEL program loans may also be reimbursable. To assert a BDR claim, a FFEL program loan borrower who decided not to consolidate his or her loan into a Direct Consolidation Loan can assert a BDR claim against any lender holding the loan, including ED in the instance of ED-owned loans, and may directly pursue reimbursement from the holder. 34 CFR §382.209(g).
\textsuperscript{85} There is no statute of limitation under which a borrower must assert a BDR claim for purposes of having the outstanding balance of his or her loan discharged. However, in certain circumstances, a borrower must assert a BDR claim within specified statutes of limitation for purposes of receiving reimbursement for previous payments made or collected on a loan. The applicable statute of limitation that applies for reimbursement purposes depends on the particular defense (i.e., substantial misrepresentation, breach of contract, or court judgment against an IHE) the borrower asserts. 34 C.F.R. §§685.212(k)(1)(ii), 685.212(k)(2)(iii).
\textsuperscript{86} Thus, payments made on non-DL program loans prior to consolidation are not reimbursable by ED.
\textsuperscript{87} 34 C.F.R. §§685.212(k)(1)(ii), 685.212(k)(2)(iii).
should have expected given the information provided to the borrower by the school, and/or any other relevant factors.

- **Court judgment against the IHE:** If the judgment provides specific financial relief, ED will provide the unsatisfied amount of relief. If the judgment does not provide specific financial relief, ED “will rely on the holding of the case and applicable law to monetize the judgment.”

- **Breach of contract by the IHE:** ED is to determine relief “based on the common law of contracts” and other reasonable considerations.

In addition to monetary relief, other relief, as appropriate, may be provided to a borrower. Such relief may include, but is not limited to, determining that the borrower is not in default on his or her loan and is eligible to receive additional Title IV assistance and updating reports to consumer reporting agencies so that they may delete any adverse credit history associated with the loan.

**Teacher Education Assistance for College and Higher Education Grants (TEACH Grants)**

TEACH Grant recipients whose TEACH Grants have converted into a Direct Loan for failure to complete TEACH Grant service requirements may seek relief under either a closed school discharge or a successful BDR. Program regulations specify that for individuals who do not complete the program’s teaching service requirements, the TEACH Grant converts into a DL and the individual “is eligible for all of the benefits of the Direct Loan Program.” Thus, so long as an individual meets all applicable closed school discharge or BDR criteria, they may be provided relief from repaying a TEACH Grant that has converted into a DL.

**Private Education Loans**

In some instances, students who attended a closed school may have borrowed private education loans to help finance their postsecondary education at the closed school. Private education loans are nonfederal loans made to a student to help finance the cost of their postsecondary education. Unlike federal student loans, which have statutorily prescribed terms and conditions that are typically uniform in nature, private education loan terms and conditions are primarily governed by market conditions that may vary greatly, depending on a variety of factors such as the lender, the borrower’s creditworthiness, and the market. Thus, the extent to which a private education

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88 34 C.F.R. §685.222(i)(2)(ii).
89 34 C.F.R. §685.222(i)(2)(iii).
90 ED may consider information derived from a sample of borrowers when determining relief for a group of borrowers. For all borrowers asserting a BDR claim, ED may also rely on conceptual examples of relief provided in the regulations. 34 C.F.R. §685.222(i)(4). See 34 C.F.R. Part 685, Subpart B, Appendix A.
91 34 C.F.R. §685.222(i)(7).
92 34 C.F.R. §686.43(b)(2).
93 TEACH Grant regulations do not provide for a discharge of an individual’s duty to meet TEACH Grant service requirements due to a school closure or BDR. However, an individual may request that his or her TEACH Grant be converted into a DL because he or she has decided not to fulfill the service requirements or “for any other reason.” 34 C.F.R. §686.43(a). Thus, it appears an individual could request his or her TEACH Grant be converted into a DL and then seek relief from DL repayment under a closed school discharge or a BDR, while also not being required to meet TEACH Grant service requirements.
loan borrower may be provided relief from the requirement to repay their loans may largely depend on the individual private education loan’s terms and conditions.\textsuperscript{95}

**Relief for Pell Grant Recipients\textsuperscript{96}**

Pell Grant recipients who attended an IHE that closed may have some portion of their Pell eligibility restored. All Pell Grant recipients are subject to a cumulative lifetime eligibility cap on Pell Grant aid equal to 12 full-time semesters (or the equivalent). The HEA exempts from a student’s lifetime eligibility cap the period of attendance at an IHE at which a student was unable to complete a course of study because the IHE closed.\textsuperscript{97} ED uses its information technology systems to adjust Pell eligibility for those students who attended a closed school and were not reported as having “graduated” from that school.\textsuperscript{98} Following an adjustment, ED notifies students of the adjustment.

**GI Bill Educational Assistance Benefits\textsuperscript{99}**

GI Bill entitlement may be restored following a school closure. However, a school closure may result in some GI Bill participants receiving an overpayment of benefits that they would become responsible for repaying.

**Restoration of Entitlements**

Prior to 2015, GI Bill entitlement was not restored for benefits received at an educational institution that later closed.

The Harry W. Colmery Veterans Educational Assistance Act of 2017 (P.L. 115-48) authorizes the restoration of GI Bill entitlement for individuals affected by school closures. Generally, GI Bill recipients are entitled to benefits equal to 36 months of full-time enrollment (or the equivalent for part-time educational assistance) under one GI Bill. In the case of the Survivors’ and Dependents’ Educational Assistance Program (DEA; 38 U.S.C., Chapter 35), recipients who first enrolled in a program of education before August 1, 2018, have 45 months (or the equivalent for part-time educational assistance) of entitlement. Entitlement is restored for an incomplete course or program for which the individual is unable to receive credit or lost training time as a result of an

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\textsuperscript{95} In some instances, a private education loan lender or a third-party may agree to provide some debt relief to private education loan borrowers. For instance, a third-party agreed to provide approximately $480 million in debt relief to former Corinthian Colleges students who borrowed private education loans to attend Corinthian Colleges. Consumer Financial Protection Bureau, “Special Bulletin for Current and Former Students Enrolled at Corinthian-Owned Schools,” February 3, 2015, http://files.consumerfinance.gov/f/201502_cfpb_bulletin_current-and-former-students-enrolled-at-corinthian-owned-schools.pdf.

\textsuperscript{96} This section of the report was authored by Cassandria Dortch, CRS Specialist in Education Policy. For additional background information, see CRS Report R45205, *Harry W. Colmery Veterans Educational Assistance Act of 2017 (P.L. 115-48)*.

\textsuperscript{97} HEA §437(c)(3).


\textsuperscript{99} This section of the report was authored by Cassandria Dortch, CRS Specialist in Education Policy.
The Closure of Institutions of Higher Education

P.L. 115-48 applies to school closures occurring after January 1, 2015. In addition to restoring such entitlement, P.L. 115-48 permits the VA to continue paying a Post-9/11 GI Bill housing allowance through the end of the academic term following such closure but no longer than 120 days. Entitlement is not charged for the interim housing allowance. The extension of benefits following such closure is only applicable to the Post-9/11 GI Bill.

Finally, P.L. 115-48 requires that the Department of Veterans Affairs (VA) notify affected individuals of imminent and actual school closures and notify them how such closure will affect their GI Bill entitlement. GI Bill participants must apply for benefit restoration and the housing allowance extension.

### Overpayment of Benefits

Under general GI Bill regulations, if there are mitigating circumstances, a GI Bill participant who withdraws from all courses may remain eligible for benefits for the portion of the course completed. However, if there are no mitigating circumstances, the individual may be required to repay all benefits received for pursuit of the course. Mitigating circumstances are circumstances beyond the individual’s control that prevent the individual from continuously pursuing a program of education. A school closing is considered to be a mitigating circumstance.

Some GI Bill benefits, such as advance payments and the Post-9/11 GI Bill tuition and fees payment, Yellow Ribbon payment, and books and supplies stipend, may be paid as a lump sum before or at the beginning of an academic term. An overpayment may occur for a prorated portion of those upfront payments if an individual is unable to complete the academic term without mitigating circumstances.

Under Post-9/11 GI Bill regulations, the VA may determine the ending date of educational assistance based on the facts found if an eligible individual’s educational assistance must be discontinued for any reason not described in regulations. A school that permanently closes may qualify as a reason not described in regulations.

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100 The amount of entitlement restored for closures occurring from January 1, 2015, through August 16, 2017, is based on the entire period of the individual’s enrollment in the closed school. The restoration of entitlement went into effect November 14, 2017.

101 Eligibility for interim housing allowance payments began August 16, 2017. The interim housing allowance payments were payable effective August 1, 2018. The later effective date gave the VA the opportunity to adapt its administrative processes and systems to make payments.

102 The Department of Veterans Affairs (VA) automatically grants mitigating circumstances for up to six credits the first time a student reduces or terminates and mitigating circumstances must be considered. This automatic grant is called the 6-Credit Hour Exclusion.

103 The VA has indicated that students may be subject to debt for the closure of ITT Tech if the students received benefits (books and supplies) for a term they are unable to complete. U.S. Department of Veterans Affairs, “More Information Concerning ITT Tech’s Closure,” September 13, 2016, available at http://www.benefits.va.gov/gibill/, as of October 14, 2016.

104 38 C.F.R. §21.9635(bb).

105 The VA has indicated that “no debts will be created against students because of the [Corinthian College] closure” unless the student dropped classes prior to the closure. U.S. Department of Veterans Affairs, “Corinthian College Students—What You Should Know,” April 30, 2015, available at http://www.benefits.va.gov/gibill/ as of December 14, 2015.
Additional Student Aid Eligibility

For students who wish to continue their education at another IHE, another financial consideration related to an IHE’s closure is the extent to which the students’ eligibility for various financial aid sources may be affected by their previous use of those benefits at the closed institution. In addition to the duration of eligibility limits generally placed on Pell Grants and GI educational benefits discussed in the previous section, other federal student aid eligibility criteria that could affect future receipt of additional Title IV student loans include borrowing limits and eligibility limitations for receipt of Direct Subsidized Loans.

Loan Limits

Generally, annual and aggregate borrowing limits apply to Title IV student loans. Annual loan limits prescribe the maximum principal amount that may be borrowed in an academic year, and aggregate limits apply to the total amount of outstanding Title IV loans that borrowers may accrue.106 Borrowing limits for DL program loans107 vary by borrower academic standing (e.g., grade or credential level), loan type (e.g., Subsidized or Unsubsidized Direct Loan), and dependency status.108 For borrowers who receive a closed school discharge or whose loans have been discharged under a successful BDR claim, any discharged loans do not count against their annual and aggregate loan limits.109

Eligibility for Direct Subsidized Loans

In general, for borrowers of Direct Subsidized Loans, the federal government pays the interest that accrues on the loan while the borrower is enrolled in school on at least a half-time basis, during a six-month grace period thereafter, and during periods of authorized deferment. Individuals who are new borrowers on or after July 1, 2013, may only receive Direct Subsidized Loans for a period of time equal to 150% of the published length of the borrower’s academic program (e.g., a borrower enrolled in a four-year degree program may receive six years’ worth of Direct Subsidized Loans).110 However, for borrowers who receive a closed school loan discharge or who successfully assert a BDR claim, the discharged loan will not count against the borrower’s Subsidized Loan usage period.111

State Tuition Recovery Funds (STRF)

In addition to available debt relief, some states operate state tuition recovery funds (STRFs), which may reimburse students for charges paid to closed IHEs that are not covered by other sources. For example, a student may have his or her Direct Loan discharged due to school

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106 No aggregate limits are placed on PLUS Loans.
107 Borrowing limits also applied to FFEL and Perkins Loans; however, the authority to award new FFEL program loans was terminated in FY2010 and the authority to award new Perkins Loans expired on September 30, 2017.
108 For additional information on loan limits, see CRS Report R40122, Federal Student Loans Made Under the Federal Family Education Loan Program and the William D. Ford Federal Direct Loan Program: Terms and Conditions for Borrowers.
110 HEA §455(q).
111 HEA §437(c)(3) and 34 C.F.R. §685.200(f)(3) and (4).
The Closure of Institutions of Higher Education

closure, and an STRF may provide relief to cover expenses such as cash payments made directly to a closed IHE for tuition payments or to provide relief on private student loans borrowed to attend an IHE. The availability of and eligibility for such funds vary by state; not all states operate STRFs.\footnote{For additional information, see National Consumer Law Center, Student Loan Borrower Assistance Project, “State Programs,” http://www.studentloanborrowerassistance.org/loan-cancellation/state-programs/, accessed October 29, 2018.}

**Income Tax Consequences**\footnote{This section was written by Margot Crandall-Hollick, CRS Specialist in Public Finance, and Brian T. Yeh, CRS Legislative Attorney.}

Borrowers whose student loans are discharged due to school closure will be subject to federal and state income taxes on the discharged loans unless they qualify for an exception. Students who received funds from an STRF might similarly be subject to tax on any funds received, although the tax treatment of such funds is unclear. Additionally, there could be tax consequences for individuals who had previously claimed certain federal education tax benefits. This section examines the potential federal and state tax consequences that may arise for these borrowers and students.

**Federal Tax Treatment of Cancelled Debt**

Under the Internal Revenue Code (IRC), borrowers whose debt is forgiven must generally include the amount of the canceled debt in income when determining their federal income tax liability.\footnote{26 U.S.C. §61(a)(12); Treas. Reg. §1.61-12. See also United States v. Kirby Lumber Co., 284 U.S. 1, 3 (1931) (treating discharged indebtedness as income at a time when the IRC did not yet address its tax treatment).} In other words, they are subject to tax on the amount of the discharged loan. There are, however, various exceptions to this rule under which a borrower may exclude from income all or part of the forgiven debt.\footnote{See, for example, 26 U.S.C. §108 (allowing taxpayers to exclude canceled debt under certain conditions).}

The HEA contains several exceptions providing for certain student loan discharges. These exceptions apply to borrowers of FFELs, Direct Loans, and Perkins Loans who borrowed such loans to attend any IHE and whose loans are discharged due to school closure.\footnote{HEA §§437(c)(4), 464(g)(4), and 455(a)(1).} Under the HEA exceptions, these borrowers will not be subject to federal income taxes on the discharged amounts so long as the student borrowers (or students on whose behalf a parent borrowed) meet the general criteria regarding the discharge of debt tied to closed schools described earlier in this report.\footnote{HEA §§437(c)(4), 464(g)(4), and 455(a)(1). See also Rev. Proc. 2015-57, 2015-51 I.R.B. 863 (providing that former students of Corinthian Colleges, Inc. whose federal student loans are discharged under the closed school discharge procedure will not be taxed on the amounts, citing to these statutes).}

The HEA does not address the tax treatment of (1) federal student loans discharged due to a successful borrower defense to repayment or (2) private education loans that are discharged under most circumstances.\footnote{Private education loans discharged after December 31, 2017, and before January 1, 2026, due to the death or total and permanent disability of the student may be excluded from gross income for purposes of federal income taxation. See 26 U.S.C. §108(f)(5).} As such, in these cases, the borrowers will be taxed on the amount of the discharged loan unless they qualify for an exception found outside of the HEA. Federal tax law...
provides several exceptions that may be relevant to borrowers whose loans are discharged. For example, IRC Section 108 excludes forgiven debt if the taxpayer is insolvent. Thus, borrowers whose liabilities exceed the fair market value of their assets immediately prior to discharge will not be taxed on the discharged student loan. Another example of an exception that might be relevant is the disputed debt doctrine. Under this doctrine, a discharged loan is not considered income for federal tax purposes if the loan was based on fraud or misrepresentation by the lender.

Guidance issued by the Internal Revenue Service (IRS) in 2015 and 2017 illustrates how the doctrine might be applied in the student loan context. The 2015 guidance provides that former students of Corinthian Colleges, Inc. (CCI) whose federal student loans are discharged under a defense against repayment claim will not be taxed on the discharged amounts because many would likely qualify under the disputed debt doctrine due to the school’s fraudulent behavior. In 2017, the IRS extended this same relief to former students of schools owned by American Career Institutes, Inc. (ACI). In addition, in 2018 the IRS issued guidance explaining that it would provide similar tax treatment regarding the discharge of private student loans taken out by borrowers who attended schools owned by CCI or ACI, where the loans are discharged due to legal settlements of cases brought by federal and state governmental agencies alleging that CCI, ACI, and certain private lenders engaged in unlawful business practices.

In order to exclude a discharged loan from income, borrowers must determine that they qualify for an exception based on their individual circumstances and be able to show that the determination is correct if the IRS contests it. If the IRS disagrees and assesses tax based on the amount of the discharged loan, the taxpayer may challenge the assessment in federal court.

Federal Tax Treatment of State Tuition Recovery Funds

Students who receive funds from STRFs might also face federal tax consequences, although the tax treatment is less clear. As a general rule, any amount received by a taxpayer is includible in gross income, and potentially subject to taxation, unless specifically excluded by law. It is not clear how this principle applies in the context of STRF payments, as there do not appear to be court decisions or IRS guidance addressing the issue. There are several theories under which students could arguably exclude the payments from income, depending on their circumstances and the specifics of the state’s plan. For example, the payment might be treated as a nontaxable reimbursement of tuition, scholarship, or state benefit. If the payment is excluded from the

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120 Ibid. §108(a)(3).
121 See, for example, Preslar v. Comm’r, 167 F.3d 1323, 1329 (10th Cir. 1999); Zarin v. Comm’r, 916 F.2d 110, 115 (3rd Cir. 1990).
125 The borrower may file suit in the U.S. Tax Court prior to paying the disputed amount or in the U.S. Tax Court or appropriate federal district court after paying such amount. See 26 U.S.C. §§6213(a), 7421; 28 U.S.C. §1340. See also 26 U.S.C. §6201(d) (providing that if an information return filed by a third party serves as the basis for the IRS’s determination that a taxpayer owes tax, the IRS then has the burden of producing reasonable and probative information concerning the alleged deficiency). This provision may be relevant for student borrowers because their discharged loans should be reported by the lender to the IRS on an information return. Ibid §6050P.
126 Ibid. §61(a).
127 See, for example, Comm’r v. Glenshaw Glass Co. 348 U.S. 426, 431 (1955) (interpreting “gross income” to mean “accessions to wealth, clearly realized, and over which the taxpayers have complete dominion”) (emphasis added); 26 U.S.C. §117 (excluding qualifying scholarships from income); Rev. Rul. 2003-12, 2003-1 C.B. 283 (discussing the
student’s income, the student may be required to account for previously claimed federal education tax benefits, as discussed below.

Federal Higher Education Tax Benefits

Along with the potential taxation of discharged student loans and amounts received from STRFs, a school’s closure or the discharge of a borrower’s student loan may have consequences related to higher education tax benefits. While there are a variety of federal tax benefits that help offset some of the costs of a higher education, four are relevant for purposes of this report for reasons discussed below.128 These four benefits include the following:

- **The student loan interest deduction**, under which qualifying taxpayers may annually deduct up to $2,500 of student loan interest for the entire duration of repayment.129

- **The tuition and fees deduction**, which allows taxpayers to reduce their income subject to tax for tuition and fees paid annually, up to $4,000, depending on their income level.130 As of the date of this report, the tuition and fees deduction cannot be claimed on 2018 or subsequent tax returns.

- **The Lifetime Learning Credit (LLC)**, under which qualifying taxpayers may annually reduce their tax liability for tuition and fees paid, up to $2,000.131 The LLC is a nonrefundable credit, meaning any amount of the credit in excess of income tax liability is effectively forfeited by the taxpayer.

- **The American Opportunity Tax Credit (AOTC)**, under which qualifying taxpayers can reduce tax liability by $2,500 per student annually (depending on eligible expenses and the taxpayer income level).132 The AOTC can be claimed for tuition and fees and books, supplies, and equipment, but not room and board.133 Additionally, the AOTC is a refundable credit, which means taxpayers with little to no tax liability can receive up to $1,000 of the AOTC as a refund check.134

Tuition and fees paid with the proceeds of a loan can count toward claiming these tax benefits, but any aid that is tax-free, such as a Pell Grant, must generally reduce the amount of expenses against which the benefits may be claimed.135 As a general rule, either the parent or the student who pays the qualifying education expenses will claim the tax benefit, depending on whether the general welfare exclusion, which has been developed by the IRS through a series of administrative rulings and excludes qualifying governmental benefits from income).

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128 For a summary of all higher education tax benefits that a student may be eligible for, including benefits for student debt and for saving for higher education, see CRS Report R41967, *Higher Education Tax Benefits: Brief Overview and Budgetary Effects*.


130 Ibid §222. The ultimate tax savings from the tuition and fees deduction depends on the taxpayer’s marginal tax rate. For example, if the taxpayer’s top tax rate is 10%, deducting $4,000 will reduce tax liability by $400; however, if the taxpayer’s top tax rate is 25%, the same deduction will reduce tax liability by $1,000.

131 Ibid §25A(c).


134 Ibid. §25A(i)(5).

135 Ibid. §§25A(g)(2), 221(d)(2), 222(c)(2)(B).
student is the parent’s dependent for tax purposes. Taxpayers can generally only claim one tax benefit per student annually.

Availability of Benefits for Students Whose School Has Closed

Students who continue to pursue higher education after a school closure are eligible for these education tax benefits, pursuant to the requirements applicable to all taxpayers. However, in some instances, a taxpayer who claims the AOTC may be ineligible for the credit in future years due to statutory restrictions on the period of education for which students may claim the credit. Specifically, the AOTC can only be claimed for expenses incurred during the first four years of a postsecondary education, irrespective of whether those first four years lead to a postsecondary credential. Therefore, for example, it appears that if a student attended a school for three years and that school closed, the maximum remaining time the student could claim the AOTC is one additional year. There is seemingly no IRS guidance or case law addressing how this requirement is applied in the context of students whose schools have closed, including students who may have to pay back previously claimed credits (discussed below).

The other three benefits contain no limits on the period of education in which students may claim them.

Federal Tax Treatment of Previously Claimed Education Tax Benefits

Taxpayers may be required to account for previously claimed education tax benefits if they subsequently qualify to exclude discharged student loans or STRF payments. The borrowers who might be affected are those who

- claimed the LLC or AOTC for expenses that were paid with the proceeds from a student loan that was subsequently discharged,
- deducted expenses for tuition and fees that were paid with the proceeds from a student loan that was subsequently discharged,
- deducted interest on a student loan that was subsequently discharged, or
- claimed a tax credit (i.e., the LLC or AOTC) or a deduction (for tuition and fees or student loan interest) for expenses that were reimbursed by an STRF payment.

In order to prevent these borrowers from getting the double benefit of both (1) a credit or deduction and (2) the exclusion of the discharged loan or STRF payment, such borrowers may be required to pay back the value of the credit or deduction. However, there may be circumstances

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136 Ibid. §§25A(g)(3) & (5), 221(c), 222(c)(3); Treas. Reg. §1.25A-5(a). See also Treas. Reg. §1.25A-5(b) (treating expenses paid by a third party, such as grandparents or noncustodial parents, as paid by the student under certain circumstances).

137 See, for example, 26 U.S.C. §§25A(c), 221(e)(1), 222(c)(1) & (2).

138 Ibid. §25A(b)(2)(A) & (C), (i)(2).

139 Note that these tax consequences might also apply to any taxpayers who claimed the Hope Scholarship Credit, which was replaced by the AOTC beginning in 2009. See American Recovery and Reinvestment Act of 2009, P.L. 111-5, §1004, 123 Stat. 115, 313 (2009). The Hope credit is codified at 26 U.S.C. §25A(b).

140 See Hillsboro Nat’l Bank v. Comm’r, 460 U.S. 370, 377-80 (1983) (discussing the origin of the judicially developed tax benefit rule, which prevents taxpayers from receiving double tax benefits on the same income or transaction); 26 U.S.C. §111 (partially codifying the tax benefit rule); Treas. Reg. §1.25A-5(f)(3), (4) (requiring the education tax credits be recaptured if the taxpayer receives a refund of the expenses).
in which the IRS will not require a taxpayer to account for previously claimed tax benefits. For example, in its 2015, 2017, and 2018 guidance addressing former students of CCI and ACI, the IRS announced that it would not require these borrowers to account for previously claimed education tax benefits. The IRS did not explain its reasoning in reaching this determination, and it is not clear the extent to which the agency may provide similar benefits to other borrowers.

State Income Tax Consequences

A school closure or the discharge of a student loan may also result in state income tax consequences. Most states use the IRC’s definition of income as the starting point for computing state income tax liability. As such, to the extent that the borrower must pay federal income tax on the discharged debt or account for previously claimed federal education tax benefits, he or she may be taxed at the state level as well. Similarly, to the extent that the borrower qualifies to exclude the amounts from federal income taxation, such treatment may also apply at the state level. However, while most state tax codes follow the IRC, states are not required to adopt the federal definition of income and, thus, some states may provide for different tax treatment. Furthermore, states with their own education tax benefits or tuition recovery funds may have laws or policies specifically addressing the state tax treatment of the benefits and funds.

142 Ibid.
143 See Personal Income Tax Quick Answer Charts: Starting Point for Personal Income Tax, State Tax Guide (CCH) ¶700-003 (Nov. 30, 2016) (showing that most states use the federal definition of gross income, adjusted gross income, or taxable income as the basis for computing state individual income tax liability).
Appendix. List of Abbreviations

The following are abbreviations used throughout this report.

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>ACI</td>
<td>American Career Institutes</td>
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<td>AOTC</td>
<td>American Opportunity Tax Credit</td>
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<td>BDR</td>
<td>Borrower defense to repayment</td>
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<td>CCI</td>
<td>Corinthian Colleges, Inc.</td>
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<td>DL</td>
<td>Direct Loan</td>
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<td>ED</td>
<td>U.S. Department of Education</td>
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<td>FFEL</td>
<td>Federal Family Education Loan</td>
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<td>HEA</td>
<td>Higher Education Act</td>
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<td>IHE</td>
<td>Institution of higher education</td>
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<td>IRC</td>
<td>Internal Revenue Code</td>
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<td>IRS</td>
<td>Internal Revenue Service</td>
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<td>LLC</td>
<td>Lifetime Learning Credit</td>
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<td>SAP</td>
<td>Satisfactory Academic Progress</td>
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<td>STRF</td>
<td>State Tuition Recovery Fund</td>
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<tr>
<td>TEACH Grant</td>
<td>Teacher Education Assistance for College and Higher Education Grant</td>
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<tr>
<td>VA</td>
<td>Department of Veterans Affairs</td>
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Author Information

Alexandra Hegji
Analyst in Social Policy

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