

STATEMENT OF NEED AND REASONABLENESS

Proposed Amendment to Rules Governing Supplemental Student Loan SELF Program, *Minnesota Rules, 4850.0010 to 4850.0018*

INTRODUCTION

The Minnesota Office of Higher Education proposes amendments to rules governing its supplemental student loan SELF Program.

About the SELF Program. The Minnesota Student Educational Loan Fund (SELF) Program helps students who need assistance in paying for education beyond high school. The SELF Program is a long-term, low-interest educational loan available from the Office of Higher Education. The program is distinctive to Minnesota, and the Office of Higher Education is the only lender in the program.

The SELF program does not receive state appropriations. Funding for SELF Loans is obtained through the issuance of revenue bonds. The revenue bonds are repaid from interest earnings.

Before applying for a SELF Loan, students are required to seek other sources of federal, state, institutional, and private aid for which they may be eligible.

Undergraduate students may borrow up to \$6,000 per year for the first two years, and \$7,500 per year thereafter (a maximum SELF total of \$34,500). Effective for loans disbursed or certified after July 1, 2007, the limits for all undergraduate grade levels will be \$7,500 per year. The minimum loan size is \$500.

Graduate students may borrow up to \$9,000 per year and can't exceed \$52,500 in SELF Loans, including his or her undergraduate SELF debt.

Summary of rules amendments. The Office of Higher Education is considering rule amendments that would:

- Allow for nonaccrual of interest or payment for up to three years for someone with a temporary total disability.
- Allow for a one-time rehabilitation of a loan within two years of a default date.
- Allow for a loan interest rate reduction for active duty military personnel.
- Increase the cosigner minimum age from 18 to 24 unless the cosigner is a sibling of the loan originator.
- Increase the acceptable limit of negative credit items from \$50 to \$300 to be an eligible cosigner.
- Eliminate the personal financial statement as an alternative to a credit report for cosigner credit approval.

- Expedite the loan and further eliminate paper loans by adding language allowing electronic signatures when the process has been adopted by the agency.
- Add language to clarify when a loan is cancelled due to total and permanent disability.

The request for comments period ended May 23, 2007 and no comments were received. These proposed rules changes were previously reviewed by legislators concerned about some of the proposed changes and student members of the Higher Education Student Advisory Council, which provides the office with student perspectives on statewide higher education issues and policies including financial aid. Their concerns were met in the proposed rules draft language.

ALTERNATIVE FORMAT

Upon request, this Statement of Need and Reasonableness can be made available in an alternative format, such as large print, Braille, or cassette tape. To make a request, contact Mary Lou Dresbach at 651-642-0567. TTY users may call 800-627-3529.

STATUTORY AUTHORITY

The Office's statutory authority to adopt the rules is set forth in *Minnesota Statutes* section 136A.16, which states:

The office shall adopt policies and prescribe appropriate rules to carry out the purposes of sections [136A.15](#) to [136A.1702](#). The policies and rules except as they relate to loans under section [136A.1701](#) must be compatible with the provisions of the National Vocational Student Loan Insurance Act of 1965 and the provisions of title IV of the Higher Education Act of 1965, and any amendments thereof.

Under this statute, the Office has the necessary statutory authority to adopt the proposed rules.

REGULATORY ANALYSIS

1. Affected parties.

Most of the proposed changes would help students who borrowed loans and their cosigners. The following would be supporters:

- People with temporary total disabilities who would now be exempt from loan interest and loan payments for up to three years.
- Military personnel who may be eligible for reduced interest while on active duty.
- People who defaulted on their loan would now have the one time opportunity to rehabilitate their defaulted loan, and clear their credit history if permitted by the credit bureau.
- Parent's of dependent students who do not want their children to cosign loans for other students.
- Cosigners with credit disputes up to \$300 who would now qualify.

- Providers of bond funding for the loans would support any changes that might decrease defaulted loans.

Opponents may include the following:

- People who oppose the guidelines/criteria used to include new groups of exemptions for repayment—military personnel and people with temporary total disabilities.
- People between the ages of 18 to 24 who currently qualify as cosigners and would now not be eligible to cosign a student loan.
- People who do not have a credit report and could no longer qualify to cosign a loan.

2. Probable costs to the agency and to any other agency of the implementation and enforcement of the proposed rule and any anticipated effect on state revenues

- Some of the proposed changes will allow for a small number of new loans to be approved.
- Loan quality will be improved by decreasing the number of defaulted loans.
- Loan collection will be improved by providing incentives for people with defaulted loans to make payments.
- Loan earnings will be reduced by allowing for reduced interest for active duty military personnel and no interest for people with temporary total disabilities.

3. Determination of whether there are less costly methods or less intrusive methods for achieving the purpose of the proposed rule

These proposed rules were determined to help the affected parties. See rule analysis below.

4. A description of any alternative methods for achieving the purpose of the proposed rule that were seriously considered by the agency and the reasons why they were rejected in favor of the proposed rule

There are no alternatives since these rules are part of a student loan program.

5. The probable costs of complying with the proposed rule.

See rule analysis below.

6. The probable costs or consequences of not adopting the proposed rule.

See rule analysis below.

7. There are no differences between the proposed rule and existing federal regulations.

ADDITIONAL NOTICE

Our Notice Plan also includes giving notice required by statute. We will mail the rules and Notice of Intent to Adopt to everyone who has registered to be on the agency's rulemaking mailing list under Minnesota Statutes, section 14.14, subdivision 1a. We will also give notice to the Legislature per *Minnesota Statutes*, section 14.116. Besides posting the proposed amendments in the State Register, we also posted the notice on the front page of our agency Web site, and mailed the notice to the financial aid offices of the 300 post-secondary institutions that participate in the SELF program.

COST OF COMPLYING FOR SMALL BUSINESS OR CITY

This section does not apply.

RULE-BY-RULE ANALYSIS TO PROPOSED SELF RULES

Changes/edits to existing rules.

4850.0011 DEFINITIONS.

Subp. 9. Creditworthy cosigner.

- Increase the acceptable limit of negative credit items from \$50 to \$300. This will enable people with small credit disputes to still qualify as a cosigner. For example, someone with a late or non-return of a movie rental, cell phone charges or contract termination disputes, medical equipment rental and insurance coverage disputes. The agency would be able to approve a small number of additional loans that were previously denied.

Subp. 10. Cosigners.

- Increase the cosigner minimum age from 18 to 24 unless the cosigner is a sibling of the loan originator.
 - a) Loan quality would improve by decreasing the number of defaults since defaulted loans are significantly higher when the cosigner is under 24 years old. Cosigner's under age 24 generally do not provide any additional financial support for the loan if the borrower can't make the payments.
 - b) Cosigners younger than 24 would have their personal financial future protected. In the agency's experience, co-signers under the age of 24 have often been students cosigning loans for other students who are roommates, boyfriends, girlfriends or friends. If the borrower cannot make loan payments, the cosigner is legally required to pay the loan. Increasing the age of the cosigner will decrease the likelihood that a cosigner in a temporary relationship with the borrower will be held liable for another student's loan in future years. Siblings are excluded from the 24 year old requirement because siblings have an inherent permanent personal relationship with the borrower.

Parents of dependent students have requested that their sons or daughters not be eligible to cosign loans for someone else. If the borrower defaults, the cosigner—who may still be a student—will jeopardize their financial aid. State grant funding is withheld for both the borrower and cosigner if the loan defaults. In this situation the cosigner's parents have to fund more of the cosigner's education due to loss of financial aid. Also, the cosigner would not be eligible for student loans and may be required to pay higher interest rates on credit cards, car and house loans or reduce their eligibility to receive such loans.

- Eliminate the personal financial statement as an alternative to a credit report for cosigner credit approval.

The situation where the cosigner has no credit history and is ultimately approved for the loan is rare. For calendar year 2006, less than 40 out of 30,000 applications were approved based on a personal financial statement. The requirement for a personal financial statement can result from the person incorrectly entering his/her social security number during the online pre-approval process. With the elimination of the personal financial statement, the potential cosigner will be unable to proceed unless a correct social security number has been provided. This will eliminate unnecessary completion and review of the personal financial statement. In addition, information submitted on personal financial statements is very subjective and cannot be substantiated by the agency.

Subp. 24a. Loan forgiveness.

- Clarify that this subsection applies to people with total and permanent disabilities. Include language taken from federal law that defines who determines the disability and what time during the loan process the disability must occur.

Subp. 27. Repayment period.

- Repeal this section as this language is now included in *M.S. 136A.1701 Subp.4*.

Subp. 28b. SELF III loans.

- Add the new SELF IV loans to this section.

Subp. 29. Transition period.

- Add language allowing borrowers to extend the transition period if permitted by the terms of the promissory note as now stated in *M.S. 136A.1701 Subp. 4*.

4850.0012 SCHOOL AGREEMENTS AND STUDENT APPLICATIONS.

Subp. 3. Application and promissory note.

- Expedite the loan and further eliminate paper loans by adding language allowing electronic signatures when the process has been adopted by the agency.

4850.0014 AMOUNT AND TERMS.

Subpart. 1. Loan Amounts.

- Repeal language about the maximum loans amounts as these are now stated in *M.S. 136A.1701* Subp. 4.

Subp. 3. Interest rate.

- Add the new SELF IV loans to this section.

4850.0018 CLAIMS.

Subp. 2. When paid.

- Add language to clarify when a loan is cancelled due to total and permanent disability.

The following three sections are new.

4850.0011 DEFINITIONS.

Subp. 24b. Nonaccrual of interest during period of temporary total disability.

Allow for nonaccrual of interest or loan payment for up to three years for someone with a temporary total disability.

- This will allow borrowers who have been in an accident or who have medical conditions, such as cancer, where the long term outcome is not clear, not lapse into default due to their temporary inability to make loan payments. Offering up to three years of nonaccrual of interest or loan payment will give the borrowers and cosigner's financial respite if needed. If the borrower's temporary total disability becomes a permanent disability the loan would be forgiven before lapsing into default.

Subp. 31. Defaulted Loan Rehabilitation.

Allow for a one-time rehabilitation of a loan within two years of a default date.

- This would improve loan collections by providing incentives for people with defaulted loans to initiate repayments. Borrowers encounter a variety of situations—financial or otherwise—where loans default. They may not know the loan is in default, or will go into default because they did not notify the loan servicer of their address change in a timely manner. Personal relationship situations arise between the original borrower and cosigner where one party is withholding information from the other party, due to divorce, for example. A defaulted loan

stays on the credit report of the borrower and cosigner for seven years resulting in credit denials or higher interest rates; rehabilitation may prevent this.

Subp. 32. Active military duty interest reduction benefit.

Interest rate reduction for active duty military personnel.

- This benefit is part of an overall state goal of providing additional benefits to military personnel due to the increased number of military personnel called to active duty.

CONCLUSION

Based on the foregoing, the proposed rules are both needed and reasonable.

August 20, 2007
Date

Susan Heegaard
Director

Minnesota Office of Higher Education

STATEMENT OF NEED AND REASONABLENESS SUPPLEMENTAL MATERIALS

Proposed Amendment to Rules Governing Supplemental Student Loan SELF Program, *Minnesota Rules, 4850.0010 to 4850.0018*

The Minnesota Office of Higher Education submits the following items to correct the defects in its August 20, 2007 Statement of Need and Reasonableness that were identified by the Administrative Law Judge in the March 4, 2008 Order on Review of Rules.

A. Cost of Complying For Small Business or City

As required by *Minnesota Statutes*, section 14.127, subd. 1, the Office of Higher Education has considered whether the cost of complying with the proposed rules in the first year after the rules take effect will exceed \$25,000 for any small business or small city. It does not. The proposed rule affects individuals who borrow a loan to finance their postsecondary education and the borrower's designated individual co-signer, not any small businesses or city. Consequently, there is no cost to small business or small cities.

B. Probable Costs of Complying with the Rule

As required by *Minnesota Statutes*, section 14.131 (5), the Office of Higher Education has determined the proposed rules has no direct affect on governmental units or businesses. These rules govern loans to individuals to help finance their postsecondary education.

There are no direct costs for individual borrowers or co-signers to comply with the proposed rules. Potentially, a small number of borrowers may need to find another co-signer if their first choice for a co-signer is someone between the ages of 18 and 24 who is not a sibling or a co-signer who does not have any active financial credit. Borrowers who are unable to find a co-signer meeting the proposed new rules may need to seek another lender and the lender may charge a higher interest rate. Any additional cost to an individual borrower who uses a different loan program other than SELF cannot be determined as it would depend on the amount borrowed and the interest rate used by another lender.

Funding for the SELF program is from interest and principal repayments from the borrowers and the sale of bonds. There are no state appropriations for the SELF program. All program costs must be covered by the borrowers. Default rates are higher for SELF loans where the co-signer is younger than 24 years old and for loans without a financial credit history. Increasing the co-signer age and requiring a proven financial credit history is expected to reduce the default rate. By eliminating high risk borrowers, the SELF program will be able to offer more benefits to borrowers by providing a temporary disability option and a military interest reduction benefit.

C. Performance-Based Review

Minnesota Statutes, sections 14.002 and 14.131, require that the Statement of Need and Reasonableness describe how the agency, in developing the rules, considered and implemented performance-based standards that emphasize superior achievement in meeting the agency's regulatory objectives and maximum flexibility for the regulated party and the agency in meeting those goals.

These proposed rule amendments provide more flexibility and options for borrowers and co-signers to either rehabilitate a defaulted loan, eliminate interest payments on a loan, or defer their loan repayment. Individuals serving in the military may be offered the option for a reduction in the interest rate while on active duty. Borrowers while in an approved temporary-disability status would be offered the option to eliminate interest and defer loan payments. Current rules may force people with temporary disabilities into possible default. All borrowers and co-signers who default on their loan would now be offered an opportunity to rehabilitate their defaulted loan.

In addition, our agency refined the rule language to make them clear and unambiguous so borrowers and co-signers could understand the new options.

D. Consultation with the Commissioner of Finance

As required by *Minnesota Statutes*, section 14.131, the Office of Higher Education has consulted with the Commissioner of Finance. We did this by sending the Executive Budget Officer copies of the documents sent to the Governor's Office for review and approval by the Governor's Office prior to the Office of Higher Education re-publishing the Notice of Intent to Adopt Rules Without a Public Hearing. Copies were sent on March 10, 2008. The documents included: the Governor's Office Proposed Rule and SONAR Form; final draft rules; and Statement of Need and Reasonableness dated August 20, 2007.

E. Additional Notice

A Request for Comments was published in the *State Register* on March 2, 2007. The proposed rules and a Notice of Intent to Adopt Rules Without a Hearing was re-published in the *State Register* no later than April 7, 2008 as required by the Office of Administrative Hearing. At that time, the Office of Higher Education made the proposed rules available and sent the Notice of Intent to Adopt Rules Without a Hearing to the following parties:

- Individuals and organizations on the Office's registered rulemaking list;
- Chairs of legislative committees with oversight of the Office;
- Financial Aid Directors at higher education institutions eligible to participate in the SELF program;
- 13 Higher Education Veterans Program's Regional Coordinators from the mymilitary.org website;
- Minnesota National Guard Public Affairs;
- Minnesota Department of Veterans Affairs;
- Advocacy organizations and disability-specific organizations

Minnesota Commission Serving Deaf and Hard of Hearing People
Department of Employment and Economic Development, Rehabilitation
Services Branch
Minnesota State Council on Disability
ADA Minnesota
Minnesota State Services for the Blind; and
Posting on the Office's web site.

SONAR Supplement Dated: March 14, 2008