UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF POSTSECONDARY EDUCATION

THE ASSISTANT SECRETARY

April 26, 2012

GEN-12-08

Subject: Disbursing or Delivering Title IV Funds Through a Contractor

Summary: This letter provides general guidance to institutions that contract with third-party servicers to administer any aspect of their participation in the title IV, Higher Education Act (HEA) programs. The letter provides specific guidance to institutions that use contractors to deliver title IV credit balances to their students directly or through a contractor-supplied financial institution such as a bank or a credit union.

Dear Colleague:

This letter reminds institutions of their responsibilities under Department of Education (Department) regulations when they enter into contracts with servicers to administer any aspect of the institution's participation in the title IV, HEA programs. The Department's rules governing an institution's use of third-party servicers (servicers) are in 34 CFR 668.25. The following questions and answers (Qs & As) are intended to provide guidance to institutions that use, or intend to use, a third-party-servicer to carry out title IV programmatic requirements and activities, particularly activities related to delivering title IV credit balances to students directly or through a contractor-supplied financial institution such as a bank or a credit union. The information provided below is general in nature. Institutions and servicers must comply with the specific statutory and regulatory provisions applicable to third-party agreements.

GENERAL

Q1. What is the regulatory definition of a third-party servicer?

A1. With regard to institutions, the term "third-party servicer" is defined in 34 CFR 668.2 as "An individual [not including an employee of the institution] or a State, or a private, profit, or non-profit organization that enters into a contract with an eligible institution to administer, through either manual or automated processing, any aspect of the institution's participation in any title IV, HEA program."

Q2. What are examples of functions that can be performed by a third-party servicer on behalf of an institution?

A2. The regulatory definition lists some of the title IV functions that, if performed by a third-party on behalf of an institution, demonstrate that the third-party is a third-party servicer and trigger the requirements of 34 CFR 668.25. The listing, which is non-exhaustive, includes the following:

A. Processing student financial aid applications;

B. Performing need analysis;

C. Determining student eligibility and related activities;

D. Certifying loan applications (this would also include originating Direct Loans);

E. Processing output documents for payments to students;

F. Receiving, disbursing, or delivering title IV, HEA program funds, excluding lock-box processing of loan payments and normal bank electronic fund transfers;

G. Conducting activities required by title IV, HEA consumer information service regulations;

H. Preparing and certifying requests for advance or reimbursement funding;

I. Loan servicing and collection;

J. Preparing and submitting institutional eligibility and participation notices and applications; and

K. Preparing a Fiscal Operations Report and Application for Participation (FISAP).

Q3. Are there restrictions on the entities with whom an institution may enter into a third-party agreement?

A3. The regulations at 34 CFR 668.25(a) provide that an institution may enter into a third-party servicer agreement with an entity only to the extent that the servicer's eligibility to contract with the institution has not been limited, suspended, or terminated under Subpart G of the Department's Student Assistance General Provisions regulations.

Additionally, under the regulations at 34 CFR 668.25(d), a third-party servicer may not be one that –

- Has been limited, suspended, or terminated by the Secretary within the preceding five years;
- Has had, during the servicer's two most recent audits, an audit finding that resulted in the servicer being required to repay an amount greater than five percent of the funds that the servicer administered under the title IV, HEA programs for any award year;
- Has been cited during the preceding five years for failure to submit audit reports required under title IV of the HEA in a timely fashion.

In addition, a former third-party servicer, once subjected to a termination action by the Secretary, may not enter into a written contract to administer any aspect of an institution's participation in any title IV, HEA program if financial guarantees and acknowledgements of joint and several liability required under 34 CFR 668.25(d)(2) have not been provided.

Q4. What requirements apply to an institution that enters into a third-party agreement with an entity to perform a title IV, HEA function on the institution's behalf?

A4. The institution and the servicer are jointly and severally liable for any violation by the servicer of any title IV, HEA provision. 34 CFR 668.25(d)(2)(ii).

In addition, the institution must provide to the Secretary a copy of any contract it has entered into with the servicer.

The institution must notify the Secretary within 10 days of the date that –

- The institution enters into a new third-party servicer contract or significantly modifies an existing contract;
- The institution or the servicer terminates a contract; or
- The servicer stops performing the functions required under the contract, goes out of business, or files a bankruptcy petition.

The notice must include the name and address of the servicer.

Q5. Are there certain required conditions to which the servicer must agree in the contract with the institution?

A5. The agreement must be in the form of a written contract that may or may not require compensation to the third-party servicer. The contract between the institution and the third-party servicer must provide that the third-party servicer agrees to:

- Comply with all the title IV provisions (this includes those that refer solely to institutions as well as those that explicitly reference third-party servicers);
- Be jointly and severally liable with the institution for any violation by the third-party servicer of any title IV, HEA provision;
- Use any title IV funds (and any interest or earnings on them) solely for the purposes specified in and in accordance with the applicable program regulations;
- Refer any reasonable suspicion of fraudulent or criminal conduct in the title IV programs by the institution or by an applicant or student to the Department's Inspector General;
- Return to the institution all title IV, HEA program funds and records related to the servicer's administration in the title IV, HEA programs if the contract is terminated, if the servicer ceases to perform any functions prescribed under the contract, or if the servicer files for bankruptcy;
- Annually submit a compliance audit as provided at 34 CFR 668.23. For a servicer that contracts with several participating institutions, a single compliance audit can be performed that covers its administrative services for all those institutions. Additional information regarding these requirements can be found at the Department's Inspector General's Web site at:

http://www2.ed.gov/about/offices/list/oig/nonfed/sfa.html

TITLE IV DISBURSEMENTS AND CREDIT BALANCES

Q6. If my institution has contracted with an entity to deliver title IV credit balances to students, is the entity a third-party servicer?

A6. Yes, as discussed above in Q&A #1, a third-party servicer is an individual or organization that enters into a written contract with an institution to administer any aspect of the institution's participation in the title IV, HEA programs. This includes disbursing title IV funds, including paying or otherwise delivering title IV credit balances to students or parents.

Q7. If an institution has contracted with a third-party servicer to perform an institutional title IV, HEA program responsibility such as disbursing title IV credit balances, may the institution provide the third-party servicer with personally identifiable information (PII) from the education records of an eligible student without the consent of the eligible student—under Family Educational Rights and Privacy Act (FERPA) regulations, students who attend an institution of postsecondary education are eligible students who exercise their own rights under FERPA? Must the third-party servicer, like the institution, comply with the FERPA requirements?

A7. Yes, in certain circumstances a third-party servicer may be considered a school official for the purposes of FERPA and, in those circumstances, is permitted to receive and use PII from education records without the eligible student's consent to the same extent as an actual school official – provided that the servicer is not using the PII to set up a bank account for the student or to maintain a credit balance for the student, either of which requires the institution to obtain prior written consent of the student under title IV regulations at 34 CFR 668.164(c)(3)(i) and 668.165(b)(1)(ii).

FERPA regulations at 34 CFR 99.31(a)(1)(i)(B) describe the conditions that must be met for a contractor or other party to whom an institution has outsourced institutional services or functions to be considered a school official under FERPA. Specifically, the contractor or the other outside party must:

- Perform an institutional service or function for which the school would otherwise use employees;
- Be under the control of the school with respect to the use and maintenance of education records; and
- Comply with the FERPA requirements governing the use and redisclosure of PII from education records.

A school official may disclose PII from education records to a third-party servicer that meets the above criteria without the eligible student's consent, but only if the school official determines that the third-party servicer has "legitimate educational interests." 34 CFR 99.3(a)(1)(i)(A).

Each postsecondary institution is required to include the criteria for who is considered a "school official" and what is considered a "legitimate educational interest" in its annual notification of rights under FERPA, as required by 34 CFR 99.7(a)(3)(iii). A model notification is found here:

http://www2.ed.gov/policy/gen/guid/fpco/ferpa/ps-officials.html

For more information, please see the discussion on page 74813 in the preamble of the 2008 FERPA regulations at http://edocket.access.gpo.gov/2008/pdf/E8-28864.pdf.

Q8. Can a third-party servicer, without student consent, utilize the PII from education records provided to them by an institution for their proprietary use in a non-contracted enterprise such as additional financial products that they may offer?

A8. No. Under 34 CFR 99.33(a)(2), contractors to whom educational agencies and institutions disclose PII from students' education records may use that PII only for the purpose(s) for which they are disclosed. For a third-party servicer, that purpose is the title IV function the servicer has contracted to perform on behalf of the institution.

Q9. In some instances, institutions distribute a pre-loaded, yet-to-be activated debit card or similar product to their students, in anticipation that the students will opt to use it. Is the preloading of PII from students' education records for this purpose a FERPA violation, particularly if the student does not opt to authorize the account and activate the preloaded card?

A9. Yes. If the debit card is associated with a bank account which the institution wants the student to open, under 34 CFR 668.164(c)(3), an institution must have an eligible student's written consent before opening a bank account for a student. Disclosure of PII from education records to a contractor to provide students with bank accounts may only occur if the institution itself has been authorized to open such bank accounts for its students, thereby allowing the institution's contractor to perform an "institutional service or function for which the institution would otherwise use employees." Because, without student consent to open up a bank account, a contractor cannot qualify as a school official under 34 CFR 99.31(a)(1)(i)(A) and (B), discussed above, and because none of the other conditions set forth in 34 CFR 99.31(a) for disclosure by an institution of PII from an education record without consent are met, disclosure of the PII by the institution to the contractor in the circumstances described would constitute a FERPA violation.

Q10. May an institution, its third-party servicer, or the servicer's financial institution charge a fee for either opening an account or for receiving any type of debit card, stored value card, or another type of automated teller machine (ATM) card, or similar transaction device intended for delivering a title IV credit balance?

A10. No. Per 34 CFR 664.164(c)(3)(iv), regardless of how students receive their title IV credit balance funds, an institution, and any third-party servicer, is prohibited from charging a fee for delivering those title IV funds. Another example of an unallowable fee is the charging of a "lack of documentation" fee levied due to a student's failure to provide documentation required by law to open a new account in a time frame to suit the contractor or their financial institution.

Q11. What recourse does an institution have if a student neglects to comply with an institution's established policy that it will only make title IV credit balances available to a student either by electronic funds transfer to a student's bank or credit union account or otherwise restrict the issuance of the credit balance by transferring it to a debit card, stored value card, or other ATM card issued through a financial institution of the school's choosing?

A11. If a student does not comply with the institution's established policy, the school is still obligated to provide a check or cash for the amount of the credit balance to the student within the 14-day time frame provided for under 34 CFR 668.164(e).

Q12. If the institution offers a debit card, stored value card, or ATM card, or a similar transaction device through its servicer or its servicer's financial institution, when must the institution inform its students of the terms and conditions associated with the card?

A12. Under 34 CFR 164(c)(3)(ii), the institution must inform the student before the account associated with the card is opened of the terms and conditions of the card or other instrument, including any fees and other costs associated with the account. This information should include whether all or some of the fees incurred per month by the student will be refunded back to the student's account.

Institutions also should mention whether cards issued through its contracted financial institution's ATM are part of a surcharge-free network, indicate the name of the network, and indicate the approximate number of available ATM's in that network both nationally and locally. Institutions should also disclose how many surcharge-free ATM's are on their campus, their location, the hours that they are accessible to patrons, and, if available, a hyperlink to an ATM locator for their affiliated networks.

We also encourage institutions to publically disclose a breakdown of the average annual costs incurred by their students based on the debit cards activated via the third-party servicer agreement that is refreshed on an annual basis.

Q13. What are some proactive steps that an institution can take to control its costs in delivering a title IV credit balance to a student?

A13. It may be advisable for the institution to encourage its incoming students to open an account at a financial institution of their own choosing before classes start, or require students to provide information to the institution about their existing bank account where the institution can make credit balance payments cheaply and expeditiously via electronic funds transfers to those accounts.

Q14. Can a debit card provider participate with an institution by displaying each entity's logo on either the student's school identification card or single-use debit card?

A14. Currently there are no title IV prohibitions disallowing the debit card provider and the institution from displaying their respective logos on either the student's identification card or debit card.

Q15. Are there any current guidelines that institutions should follow in determining the number of their servicer's ATMs that are needed for a specific student population?

A15. No. Although 34 CFR 668.164 (c (3)(v) provides that an institution must ensure that students have convenient access to ATMs or a branch office of the bank in which the account was opened, the Department has not provided specific guidelines for determining the minimum number of a servicer's ATMs that should be available to its student population. At the request of the Department, the institution must show how it determined the number of surcharge-free

ATMs that are located on the institution's campus, in institutionally owned or operated facilities, or, consistent with the meaning of the term "Public Property" as defined in 34 CFR 668.46(a), immediately adjacent to and accessible from the campus.

We note that the intent of the regulations is to ensure that students can make unlimited withdrawals from their on-campus ATMs without incurring a fee.

If you have any questions about the information contained in this DCL, please contact Anthony Gargano by e-mail at anthony.gargano@ed.gov or by telephone at 202-502-7519.

Sincerely,

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