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**DCL ID: FP-07-01**

**Subject:** FFELP Loans Eligible for 9.5 Percent Minimum Special Allowance Rate

**Summary:** This letter restates the applicable requirements of the HEA and regulations that control whether FFELP loans acquired with funds derived from tax-exempt financing sources acquire eligibility for special allowance payments at the 9.5 percent minimum return rate

Posted on 01-24-2007

Dear Colleague:

Recent examination of activities involving tax-exempt financing of Federal Family Education Loan Program (FFELP) loans indicates that it is appropriate to restate the requirements of the Higher Education Act of 1965, as amended (HEA) and the Department's regulations that control whether FFELP loans made or acquired with funds derived from tax-exempt financing sources acquired eligibility for SAP at the 9.5 percent minimum return rate.

The HEA identifies the specific sources of funds derived from a tax-exempt obligation that can be used to acquire loans that qualify for SAP at the 9.5 percent minimum return rate. 20 U.S.C. § 1087-1(b)(2)(B)(i)(2006). These sources are: (1) funds obtained from the issuance of a tax-exempt obligation originally issued prior to October 1, 1993 or from investment earnings on the proceeds of such an obligation; and (2) funds obtained as collections on, interest benefits or special allowance payments on, or income on, loans made or purchased from the proceeds of that tax-exempt obligation. Id. The regulations describe these sources of funds in precise terms, as follows:

(c)(3)(i) . . . the special allowance rate is one-half of the rate calculated under paragraph (c)(1)(iii)(F) of this section for a loan made or guaranteed on or after October 1, 1980 that was made or purchased with funds obtained by the holder from--

(A) The proceeds of tax-exempt obligations originally issued prior to October 1, 1993;

(B) Collections or payments by a guarantor on a loan . . . purchased with funds obtained . . . from obligations described in paragraph (c)(3)(i)(A) of this section;

(C) Interest benefits or special allowance payments on a loan . . . purchased with funds obtained . . . from obligations described in paragraph (c)(3)(i)(A) of this section; <sup>1</sup>

(D) The sale of a loan . . . purchased with funds obtained . . . from obligations described in paragraph (c)(3)(i)(A) of this section; or

(E) The investment of the proceeds of obligations described in paragraph (c)(3)(i)(A) of this section.

34 C.F.R. § 682.302(c)(3)(i) (2006). These requirements have been in effect since 1993. Only the loans described in these statutory and regulatory provisions are eligible for SAP at the 9.5 percent minimum return rate. Each of the five categories (paragraphs (c)(3)(i)(A) through (c)(3)(i)(E)) includes funds separate and distinct from the funds in any other category. Each category of funds includes only those funds obtained directly from the specific source named in that paragraph.

Loans acquired from these five sources can be divided into two categories. The first category is "first-generation loans" - and includes only those loans acquired using proceeds of the tax-exempt obligation (i.e., funds obtained directly from the issuance of the tax-exempt obligation). See 34 C.F.R. § 682.302(c)(3)(i)(A) (2006). The second category is "second-generation loans" - and includes only those loans acquired using funds obtained directly from first-generation loans.<sup>2</sup> See 34 C.F.R. § 682.302(c)(3)(i)(B)-(D) (2006). Funds obtained as collections on second-generation loans, interest and special allowance payments on second-generation loans, or sales of second-generation loans, or those same kinds of funds obtained from later generation loans, are not eligible sources of funds under the statute or regulation. Therefore, loans acquired with funds from second-generation loans or later generations of loans are not eligible for SAP at the 9.5 percent minimum return rate.

Further, the Department pays SAP if it receives an accurate and complete request for payment from a lender. 20 U.S.C. § 1087-1(b)(3) (2006). A request for payment is accurate and complete if it contains all the information required by the Department, and does not include any loans that the Department has directed the lender to exclude from its request. 34 C.F.R. § 682.305(b)(5) (2006).

Finally, for your information, I have attached a more detailed letter that was sent to all lenders currently claiming SAP at the 9.5 percent minimum return rate.

James Manning  
Delegated the Authority of the Assistant Secretary  
Office of Postsecondary Education

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<sup>1</sup> The term "sale" as used in paragraph (c)(3)(i)(D) includes both a sale to a third party and an intra-portfolio transfer of loans.

<sup>2</sup> Loans from investments of proceeds, described in paragraph (c)(3)(i)(E), are like second-generation loans - the loans themselves qualify for the minimum rate, but loans acquired with funds obtained as collections, interest and SAP, or the sale of those loans described in paragraph (c)(3)(i)(E) do not. To ensure clarity regarding the eligibility of loans made from various funding sources, therefore, any references here to second-generation loans are to be understood to include loans made from investment earnings.

Attachments/Enclosures:

[FP-07-01:FFELP Loans Eligible for 9.5 Percent Minimum Special Allowance Rate in PDF Format, 121KB, 6 pages](#)