

## DEPARTMENT OF EDUCATION

## 34 CFR Part 685

RIN 1840-AC68

## William D. Ford Federal Direct Loan Program

AGENCY: Department of Education.

ACTION: Notice of proposed rulemaking.

**SUMMARY:** The Secretary proposes to amend the regulations governing the William D. Ford Federal Direct Loan (Direct Loan) Program. These amendments are a result of recently enacted changes to the Higher Education Act of 1965 (HEA) made by the Higher Education Amendments of 1998 (1998 Amendments). The proposed regulations would amend the current regulations to: remove references to the phase-in of the Direct Loan Program, update the loan interest rate formulas, and reflect the Secretary's authority to charge reduced loan fees on Direct Subsidized and Direct Unsubsidized Loans and to charge reduced interest rates to encourage on-time loan repayment.

**DATES:** We must receive your comments on or before July 30, 1999.

**ADDRESSES:** Address all comments about these proposed regulations to Ms. Nicki Meoli, U.S. Department of Education, P.O. Box 23272, Washington, DC 20026-3272. If you prefer to send your comments through the Internet, use the following address: [dlndprm@ed.gov](mailto:dlndprm@ed.gov)

**FOR FURTHER INFORMATION CONTACT:** Ms. Nicki Meoli, U.S. Department of Education, 400 Maryland Avenue, SW., ROB-3, Room 3045, Washington, DC 20202-5346. Telephone: (202) 708-8242. If you use a telecommunications device for the deaf (TDD), you may call the Federal Information Relay Service (FIRS) at 1-800-877-8339.

Individuals with disabilities may obtain this document in an alternate format (e.g., Braille, large print, audiotope, or computer diskette) on request to the contact person listed in the preceding paragraph.

**SUPPLEMENTARY INFORMATION:****Invitation To Comment**

We invite you to submit comments regarding these proposed regulations. To ensure that your comments have maximum effect in developing the final regulations, we urge you to identify clearly the specific section or sections of the proposed regulations that each of your comments addresses and to arrange your comments in the same order as the proposed regulations.

We invite you to assist us in complying with the specific

requirements of Executive Order 12866 and its overall requirement of reducing regulatory burden that might result from these proposed regulations. Please let us know of any further opportunities we should take to reduce potential costs or increase potential benefits while preserving the effective and efficient administration of the program.

During and after the comment period, you may inspect all public comments about these proposed regulations in Room 3045, Regional Office Building 3, 7th and D Streets, SW., Washington, DC, between the hours of 8:30 a.m. and 4:00 p.m., Eastern time, Monday through Friday of each week except Federal holidays.

**Assistance to Individuals With Disabilities in Reviewing the Rulemaking Record**

On request, we will supply an appropriate aid, such as a reader or print magnifier, to an individual with a disability who needs assistance to review the comments or other documents in the public rulemaking docket for these proposed regulations. If you want to schedule an appointment for this type of aid, you may call (202) 205-8113 or (202) 260-9895. If you use a TDD, you may call the FIRS at 1-800-877-8339.

**General****Background**

On October 7, 1998, President Clinton signed into law the 1998 Amendments (Pub. L. 105-244) that amended the HEA. Among the many important provisions of the new law was the reauthorization of the Title IV Student Financial Assistance Programs. The 1998 Amendments also contained a number of changes to the Title IV programs. This notice of proposed rulemaking (NPRM) addresses changes that affect the Direct Loan Program.

**Negotiated Rulemaking**

Section 492 of the HEA requires that, before publishing any proposed regulations to implement programs under Title IV of the HEA, the Secretary obtain public involvement in the development of the proposed regulations. After obtaining advice and recommendations, the Secretary must conduct a negotiated rulemaking process to develop the proposed regulations. All published proposed regulations must conform to agreements resulting from the negotiated rulemaking process unless the Secretary reopens the negotiated rulemaking process or provides a written explanation to the participants in that

process why the Secretary has decided to depart from the agreements.

To obtain public involvement in the development of the proposed regulations, we published a notice in the **Federal Register** (63 FR 59922, November 6, 1998) requesting advice and recommendations from interested parties concerning what regulations were necessary to implement Title IV of the HEA. We also invited advice and recommendations concerning which regulated issues should be subjected to a negotiated rulemaking process. We further requested advice and recommendations concerning ways to prioritize the numerous issues in Title IV, in order to meet statutory deadlines. Additionally, we requested advice and recommendations concerning how to conduct the negotiated rulemaking process, given the time available and the number of regulations that needed to be developed.

In addition to soliciting written comments, we held three public hearings and several informal meetings to give interested parties an opportunity to share advice and recommendations with the Department. The hearings were held in Washington, DC, Chicago, and Los Angeles, and we posted transcripts of those hearings to the Department's Information for Financial Aid Professionals' website (<http://www.ifap.ed.gov>).

We then published a second notice in the **Federal Register** (63 FR 71206, December 23, 1998) to announce the Department's intention to establish four negotiated rulemaking committees to draft proposed regulations implementing Title IV of the HEA. The notice announced the organizations or groups believed to represent the interests that should participate in the negotiated rulemaking process and announced that the Department would select participants for the process from nominees of those organizations or groups. We requested nominations for additional participants from anyone who believed that the organizations or groups listed did not adequately represent the list of interests outlined in section 492 of the HEA. Once the four committees were established, each negotiating committee met to develop proposed regulations, for several days each month, from January through May.

The proposed regulations contained in this NPRM reflect the final consensus of the negotiating committee, which was made up of the following members:

American Association of Community Colleges.  
American Association of Cosmetology Schools.

American Association of State Colleges and Universities.  
 American Council on Education.  
 Career College Association.  
 Coalition of Associations of Schools of the Health Professions.  
 Coalition of Higher Education Assistance Organizations.  
 Consumer Bankers Association.  
 Education Finance Council.  
 Education Loan Management Resources.  
 Legal Services Counsel (a coalition).  
 National Association of College and University Business Officers.  
 National Association of Equal Opportunity in Higher Education.  
 National Association of Graduate/Professional Students.  
 National Association of Independent Colleges and Universities.  
 National Association of State Student Grant and Aid Programs.

National Association of State Universities and Land-Grant Colleges.  
 National Association of Student Financial Aid Administrators.  
 National Association of Student Loan Administrators.  
 National Council of Higher Education Loan Programs.  
 National Direct Student Loan Coalition.  
 Sallie Mae, Inc.  
 Student Loan Servicing Alliance.  
 The College Board.  
 The College Fund/United Negro College Fund.  
 United States Department of Education.  
 United States Student Association.  
 U.S. Public Interest Research Group.  
 Under committee protocols, consensus meant that there was no dissent by any member of the committee. Thus, the proposed regulations in this document have been

agreed to by each of the organizations and groups listed as members of the committee.

### Proposed Regulatory Changes

#### Section 685.202

#### Interest Rates and Loan Fees

#### Interest Rates

The proposed regulations would implement changes to section 455(b) of the HEA that affect the interest rates charged on Direct Loan Program loans.

The interest rate formulas that apply to Direct Subsidized, Direct Unsubsidized, and Direct PLUS Loans that are first disbursed on or after October 1, 1998 and before July 1, 2003 are as follows:

For	During	The interest rate is	But will not exceed (percent)
Direct Subsidized, Direct Unsubsidized ...	Repayment .....	91-day Treasury bill rate + 2.3 .....	8.25
	In-School Grace Deferment .....	91-day Treasury bill rate + 1.7 .....	8.25
Direct PLUS .....	All Periods .....	91-day Treasury bill rate + 3.1 .....	9

The interest rate formulas that apply to Direct Consolidation Loans that are first disbursed on or after July 1, 1998 are as follows:

For a direct consolidation loan	During	The interest rate on the student loan portions is	The interest rate on the PLUS loan portion is
Application received before 10/1/98 and first disbursement on or after 7/1/98.	Repayment .....	91-day Treasury bill rate + 2.3 (Will not exceed 8.25%).	91-day Treasury bill rate + 3.1 (Will not exceed 9%).
	In-School Grace Deferment .....	91-day Treasury bill rate + 1.7 (Will not exceed 8.25%).	91-day Treasury bill rate + 3.1 (Will not exceed 9%).
Application received between 10/1/98 and 1/31/99.	All Periods .....	91-day Treasury bill rate + 2.3 (Will not exceed 8.25%).	91-day Treasury bill rate + 2.3 (Will not exceed 8.25%).
Application received on or after 2/1/99 and before 7/1/2003.	All Periods .....	Weighted average of interest rates on loans being consolidated, rounded to nearest higher one-eighth of one percent (Will not exceed 8.25%).	Weighted average of interest rates on loans being consolidated, rounded to nearest higher one-eighth of one percent (Will not exceed 8.25%).

### Loan Fees

The Secretary proposes to amend § 685.202(c) to clarify that the Secretary charges a loan fee on a Direct Subsidized or Direct Unsubsidized Loan not to exceed four percent of the principal amount of the loan. The Secretary interprets the 1998 Amendments as authorizing him to charge a reduced loan fee to all Direct Subsidized and Direct Unsubsidized Loan borrowers and to provide a reduction for borrowers demonstrating greater financial need. This authority is consistent with the authority provided to lenders in the FFEL Program under section 438(c)(2) of the HEA. The Secretary notes that the authority to charge a reduced fee in both the FFEL Program and the Direct Loan Program

does not apply to PLUS loans in either program.

While the negotiators reached consensus on all of the proposed regulations included in this NPRM, some negotiators expressed a belief that the HEA requires the Secretary to charge a loan fee equal to four percent of the principal amount of the loan on a Direct Subsidized or Direct Unsubsidized Loan. As discussed below, however, the Secretary and some other negotiators believe that the Secretary does have the authority to charge reduced loan fees.

FFEL Program lenders are required to pay the Secretary a loan origination fee equal to three percent on all Stafford loans. Prior to enactment of the 1998 Amendments, on Unsubsidized Stafford Loans lenders were required to pass on the fee to the borrower, but lenders were not required to pass on the fee to

Subsidized Stafford Loan borrowers. In addition, prior to enactment of the 1998 Amendments, there were no statutory or regulatory provisions controlling a lender's decision to offer a reduced loan origination fee. The 1998 Amendments now establish conditions under which a lender may charge reduced loan origination fees to some or all Stafford loan borrowers, thus making the lower fee a term or condition of the loan. In addition to the lender origination fee, guaranty agencies are authorized to charge a one-percent guarantee fee to borrowers. Similarly, prior to enactment of the 1998 Amendments, the Direct Loan Program charged a loan fee equivalent to the amount of the loan origination fee and the guarantee fee charged to FFEL Stafford Loan

borrowers. Generally, these practices resulted in consistent treatment of borrowers. However, depending on which loans they received and whether their particular lender or guaranty agency chose to offer them a reduced fee on their loan, some FFEL Stafford Loan borrowers paid lower fees.

To promote consistent benefits to borrowers, the 1998 Amendments, for the first time, established certain standards that must be met in order for lenders to reduce loan origination fees in the FFEL Program. The HEA now requires lenders to provide reduced loan origination fees to all borrowers or to borrowers who demonstrate a greater financial need. Proposed regulations implementing these standards were agreed to during the negotiations and will be published shortly. With these standards, all similarly situated borrowers with loans from a specific lender will be treated equally.

Nothing in the 1998 Amendments or its legislative history indicate that Congress intended to deny the benefits of reduced loan fees to borrowers in the Direct Loan Program. In fact, Congress retained the provision that borrowers in the Direct Loan Program should receive the same terms, conditions, and benefits on their loans as borrowers of similar loans in the FFEL Program unless specifically provided for otherwise. The Secretary believes that the 1998 Amendments created a new statutory basis for borrowers to insist on equal treatment from their lender on loan fees, including a lower fee if the lender chooses to offer a lower loan fee to at least some borrowers. The Secretary does not believe that Congress affirmatively intended to deny this benefit to Direct Loan borrowers. Accordingly, the Secretary believes that the HEA permits him to charge reduced loan fees to borrowers in the Direct Loan Program.

In accordance with 5 U.S.C. 553(b)(A), this preamble announces the Secretary's interpretative rule that he can charge reduced loan fees in the Direct Loan Program consistent with the lenders' authority to do so in the FFEL Program. The provision contained in this NPRM is consistent with the Secretary's interpretative rule. The Secretary will consider the public comments received on this proposed provision and determine whether any changes should be reflected in the final rule.

#### *Section 685.211*

##### *Repayment Incentives*

The proposed regulations would implement a change to section 455(b) of the HEA, which authorizes the Secretary

to charge borrowers reduced interest rates to encourage on-time loan repayment. The repayment incentives that the Secretary offers to Direct Loan borrowers must be cost-neutral and in the best financial interests of the federal government.

The proposed regulations provide the Secretary with the flexibility needed to offer additional or different repayment incentives in response to changes in economic conditions or to the Direct Loan Program statute. As written, the language mirrors the authority of lenders and guaranty agencies in the FFEL Program to offer benefits to borrowers.

Shortly, the Secretary will charge a reduced interest rate to those borrowers repaying by means of automated account debiting. Borrowers repaying via automated debiting of their personal checking, savings, or other type of account at a financial institution will receive a reduction in the interest being charged on their Direct Loans. The Secretary has determined that the reduced interest charge will be cost-neutral and has so advised the Office of Management and Budget, which is now conducting its own review consistent with section 455(b) of the HEA.

#### *Sections 685.400 and 685.401*

##### *School Participation Requirements*

The proposed regulations would implement changes to section 453(b) of the HEA by deleting all references to the phase-in of the Direct Loan Program and the transition from the FFEL Program to the Direct Loan Program. The proposed regulations move the school selection provisions to § 685.400 and remove § 685.401 from the Direct Loan Program regulations.

#### **Executive Order 12866**

##### *1. Potential Costs and Benefits*

Under Executive Order 12866, we have assessed the potential costs and benefits of this regulatory action.

The potential costs associated with the proposed regulations are those resulting from statutory requirements and those we have determined as necessary for administering this program effectively and efficiently.

In assessing the potential costs and benefits—both quantitative and qualitative—of this regulatory action, we have determined that the benefits would justify the costs.

We have also determined that this regulatory action would not unduly interfere with State, local, and tribal governments in the exercise of their governmental functions.

#### *Summary of Potential Costs and Benefits*

Proposals implementing the statutory change in borrower interest rates have been estimated to increase costs to the Federal Government by \$147 million over five years. Costs increase under this change because interest rates charged to Direct Loan borrowers—and corresponding repayments to the Federal Government—are reduced. The change represents a significant economic benefit to Direct Loan borrowers.

There are no Federal costs associated with the proposed regulations allowing the Secretary to offer reduced borrower interest rates as incentives to encourage on-time repayment. The HEA requires that any such incentives be cost-neutral. The Secretary intends to use this authority to charge a reduced interest rate to borrowers repaying by means of automated account debiting; this reduction will be structured to ensure its cost-neutrality.

#### *2. Clarity of the Regulations*

Executive Order 12866 and the President's Memorandum of June 1, 1998 on "Plain Language in Government Writing" require each agency to write regulations that are easy to understand.

The Secretary invites comments on how to make these proposed regulations easier to understand, including answers to questions such as the following:

- Are the requirements in the proposed regulations clearly stated?
- Do the proposed regulations contain technical terms or other wording that interferes with their clarity?
- Does the format of the proposed regulations (grouping and order of sections, use of headings, paragraphing, etc.) aid or reduce their clarity?
- Would the proposed regulations be easier to understand if we divided them into more (but shorter) sections? (A "section" is preceded by the symbol "\$" and a numbered heading; for example, *§ 685.211 Miscellaneous repayment provisions*.)
- Could the description of the proposed regulations in the **SUPPLEMENTARY INFORMATION** section of this preamble be more helpful in making the proposed regulations easier to understand? If so, how?
- What else could we do to make the proposed regulations easier to understand?

Send any comments that concern how the Department could make these proposed regulations easier to understand to the person listed in the **ADDRESSES** section of the preamble.

**Regulatory Flexibility Act Certification**

The Secretary certifies that these proposed regulations would not have a significant economic impact on a substantial number of small entities. None of the parties affected by these proposed regulations—individual Direct Loan borrowers—would be considered small entities for the purposes of the Regulatory Flexibility Act.

**Paperwork Reduction Act of 1995**

These proposed regulations do not contain any information collection requirements.

**Assessment of Educational Impact**

The Secretary particularly requests comments on whether these proposed regulations would require transmission of information that any other agency or authority of the United States gathers or makes available.

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(Catalog of Federal Domestic Assistance Number 84.268 William D. Ford Federal Direct Loan Program)

**List of Subjects in 34 CFR Part 685**

Administrative practice and procedure, Colleges and universities, Education, Loan programs—education, Student aid, Vocational education.

Dated: June 10, 1999.

**Richard W. Riley,**  
Secretary of Education.

For the reasons stated in the preamble, the Secretary proposes to amend title 34 of the Code of Federal Regulations by revising Part 685 to read as follows:

**PART 685—WILLIAM D. FORD  
FEDERAL DIRECT LOAN PROGRAM**

1. The authority citation for part 685 continues to read as follows:

**Authority:** 20 U.S.C. 1087 *et seq.*, unless otherwise noted.

2. Section 685.202 is amended by revising paragraphs (a) and (c)(1) to read as follows:

**§ 685.202 Charges for which Direct Loan Program borrowers are responsible.**

(a) *Interest—(1) Interest rate for Direct Subsidized Loans and Direct Unsubsidized Loans.* (i) *Loans first disbursed before July 1, 1995.* During all periods, the interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 3.1 percentage points, but does not exceed 8.25 percent.

(ii) *Loans first disbursed on or after July 1, 1995 and before July 1, 1998.*

(A) *During the in-school, grace, and deferment periods.* The interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 2.5 percentage points, but does not exceed 8.25 percent.

(B) *During all other periods.* The interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 3.1 percentage points, but does not exceed 8.25 percent.

(iii) *Loans first disbursed on or after July 1, 1998.*

(A) *During the in-school, grace, and deferment periods.* The interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 1.7 percentage points, but does not exceed 8.25 percent.

(B) *During all other periods.* The interest rate during any twelve-month period beginning on July 1 and ending

on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 2.3 percentage points, but does not exceed 8.25 percent.

(2) *Interest rate for Direct PLUS Loans.* (i) *Loans first disbursed before July 1, 1998.* During all periods, the interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 preceding that period. The interest rate is equal to the bond equivalent rate of 52-week Treasury bills auctioned at the final auction held prior to that June 1 plus 3.1 percentage points, but does not exceed 9 percent.

(ii) *Loans first disbursed on or after July 1, 1998.* During all periods, the interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 3.1 percentage points, but does not exceed 9 percent.

(3) *Interest rate for Direct Consolidation Loans.*

(i) *Interest rate for Direct Subsidized Consolidation Loans and Direct Unsubsidized Consolidation Loans.*

(A) *Loans first disbursed before July 1, 1995.* The interest rate is the rate established for Direct Subsidized Loans and Direct Unsubsidized Loans in paragraph (a)(1)(i) of this section.

(B) *Loans first disbursed on or after July 1, 1995 and before July 1, 1998.* The interest rate is the rate established for Direct Subsidized Loans and Direct Unsubsidized Loans in paragraph (a)(1)(ii) of this section.

(C) *Loans for which the consolidation application is received by the Secretary before October 1, 1998 and for which the first disbursement is made on or after July 1, 1998.* The interest rate is the rate established for Direct Subsidized Loans and Direct Unsubsidized Loans in paragraph (a)(1)(iii) of this section.

(D) *Loans for which the consolidation application is received by the Secretary on or after October 1, 1998 and before February 1, 1999.* During all periods, the interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 2.3 percentage points, but does not exceed 8.25 percent.

(E) *Loans for which the consolidation application is received by the Secretary on or after February 1, 1999.* During all periods, the interest rate is based on the weighted average of the interest rates on the loans being consolidated, rounded to the nearest higher one-eighth of one percent, but does not exceed 8.25 percent.

(ii) *Interest rate for Direct PLUS Consolidation Loans.*

(A) *Loans first disbursed before July 1, 1998.* The interest rate is the rate established for Direct PLUS Loans in paragraph (a)(2)(i) of this section.

(B) *Loans for which the consolidation application is received by the Secretary before October 1, 1998 and for which the first disbursement is made on or after July 1, 1998.* The interest rate is the rate established for Direct PLUS Loans in paragraph (a)(2)(ii) of this section.

(C) *Loans for which the consolidation application is received by the Secretary on or after October 1, 1998 and before February 1, 1999.* During all periods, the interest rate during any twelve-month period beginning on July 1 and ending on June 30 is determined on the June 1 immediately preceding that period. The interest rate is equal to the bond equivalent rate of 91-day Treasury bills auctioned at the final auction held prior to that June 1 plus 2.3 percentage points, but does not exceed 8.25 percent.

(D) *Loans for which the consolidation application is received by the Secretary*

*on or after February 1, 1999.* During all periods, the interest rate is based on the weighted average of the interest rates on the loans being consolidated, rounded to the nearest higher one-eighth of one percent, but does not exceed 8.25 percent.

(4) *Interest rate reductions.* The Secretary may reduce the interest rate on a Direct Loan as provided in § 685.211(b).

\* \* \* \* \*

(c) \* \* \*

(1)(i) Charges a borrower a loan fee not to exceed four percent of the principal amount of the loan on a Direct Subsidized or Direct Unsubsidized Loan; or

(ii) Charges a borrower a loan fee of four percent of the principal amount of the loan on a Direct PLUS Loan.

\* \* \* \* \*

3. Section 685.211 is amended by redesignating paragraphs (b), (c), (d), and (e) as paragraphs (c), (d), (e), and (f), respectively; by adding a new paragraph (b); by revising the first sentence of newly redesignated paragraph (e)(2); and by revising newly redesignated paragraph (e)(3) to read as follows:

**§ 685.211 Miscellaneous repayment provisions.**

\* \* \* \* \*

(b) *Repayment incentives.* To encourage on-time repayment, the Secretary may reduce the interest rate for a borrower who repays a loan under

a system or on a schedule that meets requirements specified by the Secretary.

\* \* \* \* \*

(e) \* \* \*

(2) If the Secretary makes the determination described in paragraph (e)(1) of this section, the Secretary sends an ineligible borrower a demand letter that requires the borrower to repay some or all of a loan, as appropriate. \* \* \*

(3) If a borrower fails to comply with the demand letter described in paragraph (e)(2) of this section, the borrower is in default on the entire loan.

\* \* \* \* \*

4. Section 685.400 is amended by adding a new paragraph (d) to read as follows:

**§ 685.400 School participation requirements.**

\* \* \* \* \*

(d) The Secretary selects schools to participate in the Direct Loan Program from among those that apply to participate and meet the requirements in paragraphs (a)(1), (b), and (c) of this section.

**§ 685.401 [Removed and Reserved]**

5. Section 685.401 is removed and reserved.

[FR Doc. 99-15278 Filed 6-15-99; 8:45 am]

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