

**CONSUMER: POST-SECONDARY EDUCATION -
DISTRESSED SCHOOLS AND STRESSED OUT PARENTS**

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RELIEF FROM STUDENT LOAN REPAYMENT

1. EXECUTIVE SUMMARY

Purpose of This Regulatory Action: The purpose of the borrower defense regulations is to protect student loan borrowers from misleading, deceitful, and predatory practices of, and failures to fulfill contractual promises by, institutions participating in the Department's student aid programs. Most postsecondary institutions provide a high-quality education that equips students with new knowledge and skills and prepares them for their careers. However, when postsecondary institutions make false and misleading statements to students or prospective students about school or career outcomes or financing needed to pay for those programs, or fail to fulfill specific contractual promises regarding program offerings or educational services, student loan borrowers may be eligible for discharge of their Federal loans.

The final regulations give students access to consistent, clear, fair, and transparent processes to seek debt relief; protect taxpayers by requiring that financially risky institutions are prepared to take responsibility for losses to the government for discharges of and repayments for Federal student loans; provide due process for students and institutions; and warn students in advertising and promotional materials, using plain language issued by the Department, about proprietary schools at which the typical student experiences poor loan repayment outcomes— defined in these final regulations as a proprietary school at which the median borrower has not repaid in full, or made loan payments sufficient to reduce by at least

one dollar the outstanding balance of, the borrower's loans received at the institution—so that students can make more informed enrollment and financing decisions.

Section 455(h) of the Higher Education Act of 1965, as amended (HEA), 20 U.S.C. 1087e(h), authorizes the Secretary to specify in regulation which acts or omissions of an institution of higher education a borrower may assert as a defense to repayment of a Direct Loan. Section 685.206(c), governing defenses to repayment, has been in place since 1995 but, until recently, has rarely been used. Those final regulations specify that a borrower may assert as a defense to repayment any “act or omission of the school attended by the student that would give rise to a cause of action against the school under applicable State law.”

In response to the collapse of Corinthian Colleges (Corinthian) and the flood of borrower defense claims submitted by Corinthian students stemming from the school's misconduct, the Secretary announced in June 2015 that the Department would develop new regulations to establish a more accessible and consistent borrower defense standard and clarify and streamline the borrower defense process to protect borrowers and improve the Department's ability to hold schools accountable for actions and omissions that result in loan discharges.

These final regulations specify the conditions and processes under which a borrower may assert a defense to repayment of a Direct Loan, also referred to as a “borrower defense.” The current standard allows borrowers to assert a borrower defense if a cause of action would have arisen under applicable State law. In contrast, these final regulations establish a new Federal standard that will allow a borrower to assert a borrower defense on the basis of a substantial misrepresentation, a breach of contract, or a favorable, nondefault contested judgment against the school, for its act or omission relating to the making of the

borrower's Direct Loan or the provision of educational services for which the loan was provided. The new standard will apply to loans made after the effective date of the proposed regulations. The final regulations establish a process for borrowers to assert a borrower defense that will be implemented both for claims that fall under the existing standard and for later claims that fall under the new, proposed standard. In addition, the final regulations establish the conditions or events upon which an institution is or may be required to provide to the Department financial protection, such as a letter of credit, to help protect students, the Federal government, and taxpayers against potential institutional liabilities.

These final regulations also prohibit a school participating in the Direct Loan Program from obtaining, through the use of contractual provisions or other agreements, a predispute agreement for arbitration to resolve claims brought by a borrower against the school that could also form the basis of a borrower defense under the Department's regulations. The final regulations also prohibit a school participating in the Direct Loan Program from obtaining an agreement, either in an arbitration agreement or in another form, that a borrower waive his or her right to initiate or participate in a class action lawsuit regarding such claims and from requiring students to engage in internal dispute processes before contacting accrediting or government agencies with authority over the school regarding such claims. In addition, the final regulations impose certain notification and disclosure requirements on a school regarding claims that are the subject of a lawsuit filed in court or that are voluntarily submitted to arbitration after a dispute has arisen.

2. BORROWER DEFENSE TO LOAN REPAYMENT (“BORROWER DEFENSE”)

- Rarely-used provision revised by the Department of Education (the “Department”) to protect students who have been victims of fraud as a response to the collapse of Corinthian Colleges
- Final Rule published November 1, 2016, effective July 1, 2017¹

Filing Claims for Borrower Defense

A. Eligibility

- Federal Direct Loan recipients
- Federal Family Education Loan (“FFEL”) and Perkins Loan recipients may obtain a Direct Consolidation Loan to receive the same administrative forbearance²

B. For loans disbursed on or after July 1, 2017:

Three grounds for Borrower Defense (preponderance of evidence standard)³

- (i) **Non-default, favorable contested judgment against a school**, in state/federal court/administrative tribunal, relating to the loan/educational services for which loan was made⁴
 - Not subject to SOL
- (ii) **Breach of contract** with the student (including enrollment agreements)⁵
 - SOL: within 6 years of breach to recover amounts previously collected (but later to collect amounts still owed)

¹ Student Assistance General Provisions, Federal Perkins Loan Program, William D. Ford Federal Direct Loan Program, and Teacher Education Assistance for College and Higher Education Grant Program, 81 Fed. Reg. 75926 (Nov. 1, 2016) (to be codified at 34 CFR parts 30, 668, 674, 682, 685, and 686).

² 34 CFR § 685.212(k)(2).

³ 34 CFR § 685.222(a)(2).

⁴ 34 CFR § 685.222(b).

⁵ 34 CFR § 685.222(c).

(iii) Borrower detrimentally relied upon **substantial misrepresentation** by the institution⁶

- “likelihood or tendency to mislead under the circumstances” or “omits information in such a way as to make the statement false, erroneous, or misleading”
- SOL: 6 years from discovery/reasonably should have discovered to recover amounts already paid (but later to collect amounts still owed)
- Intent not required- liable for negligent/unintentional misrepresentations
- **Prima facie evidence of reasonableness of borrower’s detrimental reliance on misrepresentation**
 - Demands borrower make enrollment/loan decisions immediately
 - Unreasonable emphasis on negative consequences of delay
 - Discouraging borrower from consultation with adviser/family
 - Failure to respond to borrower’s request for additional information regarding program cost
 - Other unreasonable pressure or exploitation of distress/lack of knowledge or sophistication

⁶ 34 CFR § 685.222(d).

C. For loans disbursed prior to July 1, 2017:⁷

- Claims must be grounded in state law- act/omission by the institution, relating to the loan/educational services for which loan was made (state SOL)

Processing Claims

A. Individual borrowers against open institutions⁸

- After claim submitted, Department weighs borrower's cost to attend the institution against the value of the education received, the value of the education that a reasonable borrower in similar circumstances would have received, and the value of the education that the borrower should have expected given the information provided by the institution
- Department may then bring a recoupment action against the school for all relief granted to the borrower

B. Individual borrowers against closed institutions

- Individuals may apply for discharge if:
 - (i) School closes while borrower enrolled and borrower fails to complete program because of the closure, or
 - (ii) School closes within 120 days after borrower withdraws
- Not eligible if complete comparable educational program at another institution (including through teach-out agreement or transferring credit to another institution) or if borrower completed all coursework for program

⁷ 34 CFR §§ 685.222(a)(1), 685.206(c).

⁸ 34 CFR § 685.222(e).

C. Group claims against open institutions⁹

- Borrowers may opt in/out of group claim
- If claim based on substantial misrepresentation that was widely disseminated, rebuttable presumption exists that each member of the group reasonably relied on misrepresentation¹⁰
- Institution then may be liable to the borrowers as well as to the Department for amounts discharged/reimbursed

D. Group claims against closed institutions¹¹

- Department will send closed-school discharge applications to borrowers when school closes and lender will provide borrower a closed school discharge application when first loan payments due¹²
- Institutions that submit teach-out plans must also provide borrowers a closed-school discharge application and notice that borrower may opt out of teach-out plan and instead receive a discharge
- If borrowers were enrolled at an institution that closed since November 1, 2013, and the borrowers haven't re-enrolled at another Title IV-eligible institution within three years of closure, the Department will automatically discharge these loans (borrowers from Corinthian Colleges included)

⁹ 34 CFR § 685.222(h).

¹⁰ 34 CFR § 685.222(f)(3).

¹¹ 34 CFR § 685.222(g).

¹² 34 CFR § 682.402(d)(7)(ii).

E. While claims are evaluated, loans will be placed in **administrative forbearance or stop collection (but interest will continue to accumulate)¹³**

- If application denied, borrower is responsible for repaying the loans, including interest that accrued during the forbearance period

F. Borrower Defense Claim Report¹⁴

- As of 10/28/2016, more than 15,000 claims have been approved, with a combined outstanding loan balance of \$247 million
- The Enforcement Unit will publish periodic reports detailing the Department's progress in processing these claims

Restore Semesters of Pell Eligibility for Students Affected by Closed Schools¹⁵

- Students have 12 semesters to receive Pell Grants to complete their education
- The Department may restore semesters of Pell grant eligibility for eligible students who were unable to complete their programs due to closure

Warning in Advertisements for Poor Loan Repayment¹⁶

- Proprietary institutions must provide a warning in advertisements and “promotional materials” if schools have poor loan repayment outcomes (if median borrower has not reduced the outstanding balance by at least one dollar by the end of the third year after entering repayment)
- Warning language: “U.S. Department of Education Warning: A majority of recent student loan borrowers at this school are not paying down their loans”

¹³ 34 CFR § 685.222(e)(2)(ii)(A).

¹⁴ *U.S. Department of Education Announces Final Regulations to Protect Students and Taxpayers from Predatory Institutions*, Department of Education (October 28, 2016).

¹⁵ John Kane, *Guidance on COD Processing of Pell Grant Restoration for Students who Attended Closed Schools*, Federal Student Aid (April 3, 2017),

<https://ifap.ed.gov/eannouncements/040317GuidanceCODProcPellGrantRestorationforClosedSchools.html>.

¹⁶ 34 CFR § 668.41(h).

- Promotional materials include website, catalogs, invitations, flyers, billboards, and advertising through radio, television, video, print media, social media, or the internet

Limits on Pre-dispute Arbitration Agreements/Class Action Waivers¹⁷

- Prospectively and retrospectively release Direct Loan borrowers from the school's pre-dispute arbitration agreements/class action waivers¹⁸

Institutional Accountability Provisions

- Schools showing signs of financial risk must provide an irrevocable letter of credit as insurance against the risks posed to taxpayers¹⁹

2. PUBLIC SERVICE LOAN FORGIVENESS (PSLF) PROGRAM²⁰

- Approved in 2007, this program forgives student loans of those who work in public service jobs for 10 years
- No debts have been eliminated, as the first wave of qualified workers will be eligible to submit applications for debt forgiveness in October 2017
- Only certain federal loans qualify (requires borrowers to restructure their debts)
- The Department recently suggested that approval letters sent by the administrator, FedLoan Servicing, may not be binding and may be rescinded at any time²¹
- Borrowers, along with the ABA, filed suit in early 2017 because they held jobs that they initially were told qualified for debt forgiveness, but then later had the decision reversed without a right to appeal

¹⁷ 34 CFR § 668.175(c).

¹⁸ 34 CFR § 685.300(e), (f).

¹⁹ 34 CFR § 668.15(d).

²⁰ 34 CFR § 685.219.

²¹ Stacy Cowley, *Student Loan Forgiveness Program Approval Letters May be Invalid, Education Dept. Says*, The New York Times (March 30, 2017).

3. LOAN FORGIVENESS UNDER THE TRUMP ADMINISTRATION

- The Trump Administration has not yet implemented changes to the loan forgiveness programs. But those in the Trump Administration, including Secretary of Education Betsy DeVos, have suggested that they may scale back regulations on for-profit educational institutions.²² For example, in April, DeVos withdrew, to negate ambiguity, guidance issued by the Obama Administration requiring the Federal Student Aid office to do more to help borrowers manage their debt.²³

²² Patricia Cohen, *For-Profit Schools, an Obama Target, See New Day Under Trump*, The New York Times (Feb. 20, 2017).

²³ Shahien Nasiripour, *DeVos Undoes Obama Student Loan Protections*, Bloomberg (April 11, 2017).