

PROPOSED DEFENSE TO REPAYMENT REGULATIONS
PROTECT STUDENTS FROM MISLEADING AND DECEITFUL PRACTICES
Summary of NPRM – June 13, 2016

The Obama Administration is proposing new protections for borrowers and taxpayers against fraud, deception, and other misconduct by postsecondary institutions. The proposed regulations would create a clear, consistent, and transparent process for borrowers who have been harmed by their school's misconduct to seek debt relief, along with new warnings to help students steer clear of poorly performing proprietary schools. The proposed regulations would also protect taxpayers by requiring schools to provide greater financial protection to the Federal government based upon early indicators of school financial distress. In addition, the proposed regulations include measures that would end the use of both so-called "pre-dispute, mandatory arbitration agreements" and of class action bans that prevent students from having their day in court.

Corinthian Colleges Collapse Highlights the Need for New Rules of the Road

In May 2015, Corinthian Colleges, Inc. (Corinthian), a publicly traded company operating numerous postsecondary schools that in 2014 had enrolled over 70,000 students at more than 100 campuses nationwide, filed for bankruptcy. Corinthian collapsed under the weight of deteriorating finances and multiple federal and state investigations, one of which resulted in a finding by the Department that the college had misrepresented its job placement rates. After the closure of Corinthian, which included Everest Institute, Wyotech, and Heald College, the Department received thousands of claims for student loan debt relief from former Corinthian students. The Department is committed to ensuring that students harmed by Corinthian's fraudulent practices receive the relief to which they are entitled under existing closed school and borrower defense regulations, which is why the Department appointed a Special Master in June of 2015 to create and oversee a process to provide debt relief to Corinthian borrowers who apply for Federal student loan discharges based on claims against their schools. An updated report from the Special Master on progress under that process will be released later this month.

The current Direct Loan borrower defense regulation has existed since 1995 but had rarely been used prior to the collapse of Corinthian. As the Department applied the regulation to address the Corinthian claims, it became clear that significant changes were needed to better protect students and taxpayers. Accordingly, last September, the Department began a negotiated rulemaking process to clarify how Direct Loan borrowers who have claims against their institutions can seek relief and to strengthen provisions that will hold colleges accountable for their wrongdoing. Today, the Department is continuing that process by releasing proposed regulations to protect student loan borrowers from misleading, deceitful and predatory practices of, and failures to fulfill contractual promises by, institutions participating in the Federal student aid programs.

The Federal student aid programs are intended to provide all students with access to a high-quality postsecondary education that equips them 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 their programs, such as student career outcomes or financing needed to pay for those programs, or fail to fulfill their promises, student loan borrowers affected by those actions may be eligible for discharge of their Federal loans. Current provisions in Federal law and regulations, called "defenses to repayment" or "borrower defense," allow Federal student loan borrowers to receive a discharge of their Direct Loans if their colleges' acts or omissions give rise to a State law cause of action. The regulations proposed today would simplify and strengthen those provisions.

The proposed regulations would:

- Give borrowers access to clear, fair, and transparent processes to seek debt relief;
- Provide debt relief to borrowers without requiring individual applications in instances of widespread misrepresentations;
- Protect taxpayers by ensuring that financially risky institutions are prepared to take financial responsibility for government discharges of Federal student loans;
- Ensure that proprietary schools where students have poor repayment outcomes provide students with warnings, in plain language approved by the Department, so that students can make more informed enrollment and financing decisions;
- Ensure affected borrowers have information about and access to closed school discharge when schools close; and
- End the practice of schools forcing arbitration and preventing class actions.

Since taking office, the Obama Administration has worked to ensure that every qualified student in America has access to a quality, affordable college education that leads to a meaningful degree. Today's proposal is the latest in a series of steps the Administration has taken to hold institutions accountable and ensure students do not graduate with unmanageable debt. Among others, those efforts include issuing the landmark Gainful Employment regulations ending Federal student aid eligibility for career colleges that are not paying off for their students, establishing tougher regulations targeting misleading claims by colleges and incentives that drove sales people to enroll students through dubious promises, requiring States to step up their oversight through the state authorization regulation, creating a new Enforcement Unit to protect students and taxpayers from unscrupulous colleges, and pushing accreditors to take responsibility for ensuring quality student outcomes. In addition, the Administration has made historic investments to keep college within reach and to ensure that all student loan borrowers can cap their monthly payments at 10 percent of their income.

Summary of Major Provisions

Clear, Transparent Processes for Borrowers

These proposed regulations would put in place a borrower defense process that is clear, understandable, and easily accessible for borrowers; that facilitates collection and review of evidence for deciding claims; and that ensures claims are processed efficiently, transparently, and fairly. The regulations would replace a complicated, uneven, and burdensome standard based on the application of the laws and procedures of the various States with a new Federal standard that would make relief available when there is:

- A breach of contractual promises between a school and its students;
- A favorable non-default contested State or Federal court judgment against a school related to the loan or the educational services for which the loan was made;
- A substantial misrepresentation by the school about the nature of the educational program, the nature of financial charges, or the employability of graduates. The proposed regulations specify factors that, if present in conjunction with a misrepresentation on the part of the school, would likely elevate that misrepresentation to a substantial misrepresentation. Such factors would include:
 - Demanding that the borrower make enrollment or loan-related decisions immediately;
 - Placing an unreasonable emphasis on unfavorable consequences of delay;

- Discouraging the borrower from consulting an adviser, a family member, or other resource;
- Failing to respond to the borrower's requests for more information, including about the cost of the program and the nature of any financial aid; or
- Otherwise unreasonably pressuring the borrower or taking advantage of the borrower's distress or lack of knowledge or sophistication.

Opportunity for Group-wide Discharges

The proposed regulations would establish an important process for resolving claims based on conduct that harmed a group of borrowers. The Secretary could identify and provide relief to a group of borrowers from individually filed applications or from any other source of information, and could include borrowers who may not have filed an application for relief, in the event that common facts and claims exist that apply to the group of borrowers.

Student and Taxpayer Protections

Putting Financially Risky Colleges on the Hook for their Behavior

When colleges get into financial trouble or take actions that harm students they should be the ones held responsible for losses that arise on Federal student loans – not American taxpayers. The proposed regulations would hold institutions accountable so that taxpayers are protected against schools at risk of financial failure. These provisions would help to mitigate the effects of a large-scale closure akin to the demise of Corinthian. Specifically, the proposed regulations would establish a number of triggering and early-warning events, many of which would automatically require schools to put up funds, in the form of letters of credit (LOCs), that total at least 10 percent of the amount of Title IV funds received by the school over the previous year. These funds could be used to cover the costs of borrower defense and related claims in the event they arise. Those triggers would include instances in which:

- A state or federal government entity such as an attorney general, the CFPB, or the FTC brings a major suit against the school;
- The school has a substantial number of outstanding borrower defense claims;
- The school defaults on its own debt obligations;
- The school fails the 90/10 non-Federal revenue requirement;
- The school has more than half of its Gainful Employment students enrolled in programs that are not passing ED standards;
- The school's accreditor take an action that could result in the school losing its accreditation; or
- Other additional indicators of significant financial risk.

Early Warnings for Students

Institutions that set off the triggers described above would be required to warn their prospective and enrolled students that they've been required to provide this financial protection to the Department.

Additionally, proprietary institutions would be required to warn prospective and- enrolled students, individually and through promotional materials, if their students have very poor loan repayment outcomes. Proprietary institutions are far more likely to have poor repayment rates, along with lower post-college earnings and higher default rates, than public or non-profit institutions, and pose the greatest risk to students and taxpayers. Therefore, proprietary institutions where the typical borrower has not

paid down a single dollar of his or her loan balance within five years after leaving school, would have to warn students before they make significant decisions about college enrollment or borrowing.

Increased Access to Closed School Discharges

Many borrowers eligible for a closed school discharge do not apply. The Department is concerned that borrowers are unaware, as a result of insufficient outreach and information, that they may be eligible for student loan debt relief. In some instances, the closing school might inform borrowers of the option to complete their program through a teach-out, but fail to advise them of the option for a closed school discharge.

Currently, the Department sends those borrowers it identifies as potentially eligible for this relief an application and an explanation of the qualifications and procedures to obtain a closed school discharge. The proposed regulations would provide such information to borrowers earlier in the process, and would help to ensure that the borrowers receive accurate and complete information with regard to their eligibility for a closed school discharge, as well as provide for an automatic discharge for students who do not subsequently re-enroll at another school. With these changes:

- The Department would send closed school discharge applications and information to borrowers a second time, when their first loan payments are due;
- Schools with teach-out plans must also provide the application, as well as information on borrowers' right to opt-out of the teach-out and instead receive a discharge; and
- Borrowers who were enrolled at a closing school and who have not re-enrolled at another school within three years of that closure will automatically have their loans discharged.

Protections against Forced Arbitration

Recent history demonstrates the need to address bans by postsecondary institutions on both class actions and individual lawsuits by borrowers that prevent them from having their day in court. Some schools have limited students' ability to sue a school for wrongdoing by requiring students to agree to mandatory, pre-dispute arbitration as part of their enrollment agreements, or as a part of other agreements or documents. Corinthian included explicit class-action waiver provisions in enrollment agreements, and used those provisions, with mandatory pre-dispute arbitration clauses, to avoid class actions and individual lawsuits by students. If student class actions against Corinthian had been able to proceed, those actions could have compelled Corinthian to provide financial relief to the students and to change its practices while Corinthian was still a viable entity. Instead, affected borrowers with Direct Loans from attendance at any of the Corinthian schools are now only able to obtain relief by raising the schools' misconduct as a defense to their Federal loans through the Department's current borrower defense process.

The Department's proposed regulations include measures to protect students from signing away their ability to sue. The proposal would end some of the most common abuses by:

Forbidding Schools from Forcing Students to Go It Alone

Unfair practices by colleges don't just harm one student; they may well harm a large group. Class actions often offer the only feasible legal means for individuals to address wrongdoing given the cost of litigation and the small dollar amounts of individual students' claims, but many schools require students to agree not to bring class claims. Under the proposal, schools will no longer be able to forbid class actions.

Ending Day-in-Court Denials

The Obama Administration wants to empower students to seek relief directly from schools that break the law. Some schools tuck clauses into enrollment agreements that block students from ever taking the school to court and instead force them to arbitrate their claims. The proposed rules allow students to pursue their claims in arbitration, but only if they choose to – not if they're forced.

Prohibiting Gag Rules

College enrollment agreements can also be laden with other restrictions that silence students from voicing their concerns to authorities. The Department is concerned that some schools require students to first pursue an internal process before contacting accreditors and regulators about potential violations of the law. The proposal would bar this practice, while also providing more transparency on the outcomes of arbitration by requiring schools to notify the Secretary when arbitration and judicial claims are filed and the decisions and awards issued in arbitration and in court proceedings.

Other Provisions

Ensuring All Federal Student Loan Borrowers Have Access to Borrower Defense

The proposed regulations would recognize Federal Family Education Loan (FFEL) and Perkins loan borrowers' ability to receive borrower defense relief through Direct Consolidation Loans. The proposed regulations would also ensure that borrowers with FFEL Loans will have the same access to administrative forbearance as Direct Loan borrowers while their borrower defense claim is being evaluated. The proposed regulations would require lenders to grant a mandatory administrative forbearance for borrowers who have filed a borrower defense claim with the Secretary.

False Certification

To provide loan discharge relief in instances where schools falsely certify their students' high school diploma status, the proposed regulations would specify that a borrower qualifies for a false certification discharge if the borrower reported not having a high school diploma or its equivalent and did not satisfy applicable alternative to graduation from high school requirements. In these situations, the borrower would qualify for a false certification discharge if the school:

- Falsified the borrower's high school graduation status;
- Falsified the borrower's high school diploma; or
- Referred the borrower to a third party to obtain a falsified high school diploma.

In addition, the proposed regulations would amend the regulatory provisions granting a false certification discharge without an application to include cases in which the Department has information in its possession showing that the school has falsified the Satisfactory Academic Progress (SAP) of its students.

The proposed regulations would also:

- Expand the types of documentation that may be used for the granting of a discharge based on the death of the borrower ("death discharge") in the Perkins, FFEL, Direct Loan, and TEACH Grant programs;
- Codify the conditions under which the discharge of a Direct Subsidized Loan will lead to the elimination or recalculation of a Subsidized Usage Period under the 150 Percent Direct Subsidized Loan Limit or the restoration of interest subsidy;

- Make technical corrections to the regulation that describes the authority of the Department to compromise, or suspend or terminate collection of, debts;
- Make technical corrections to the regulations governing the Pay as You Earn (PAYE) and Revised Pay as You Earn (REPAYE) repayment plans;
- Allow for the consolidation of Nurse Faculty Loans;
- Allow borrowers to obtain a Direct Consolidation Loan if the borrower consolidates at least one eligible loan; and
- Clarify the conditions under which the capitalization of interest by FFEL Program loan holders is permitted.

Public Comment Period

The 45-day public comment period for these proposed regulations will begin once they are published in the Federal Register.