

Borrower Defense Final Regulations: Summary of Major Provisions

Clear, Transparent Processes for Borrowers

These final regulations put in place a borrower defense process that is easier to understand and more accessible for borrowers; that facilitates collection and review of evidence for resolving claims; and that ensures claims are processed more efficiently, transparently, and fairly. The regulations replace a complicated, uneven, and burdensome standard for assessing claims that is based on the application of various State laws with a new Federal standard that will make relief available when there is:

- A breach of contractual promises between a school and its students;
- State or Federal court judgments against a school related to the loan or the educational services for which the loan was made; or
- A substantial misrepresentation by the school about the nature of the educational program, the nature of financial charges, or the employability of graduates.

Changes from NPRM: The final regulations clarify how the Department will determine debt relief for borrowers. The Department has replaced the prescriptive formulas laid out in the proposed regulation with straightforward, conceptual examples that provide guidance to borrowers, schools, and the Department about how the Department might decide the level of loan relief to grant in different circumstances. These examples provide a much clearer picture of how relief will be determined. The final regulations also require, for borrowers who have filed a borrower defense claim with the Secretary, that servicers stop requiring payment on loans while borrowers' claims are being reviewed.

Statutes of Limitation

The final regulations state that there are no statutes of limitation for discharge of borrowers' loan balances still owed or relief based on State or Federal court judgments. The statutes of limitation for borrower claims to recover payments that have already been made on loans made on or after July 1, 2017 are six years for claims based on misrepresentation and breach of contract.

Opportunity for Group-Wide Discharges

The final regulations establish a process to make it easier for the Department to provide relief to groups of borrowers. Under the new regulations, the Secretary can identify groups of borrowers from individually filed applications or from any other source of information, and can 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. Where there were widespread misrepresentations, the Department may presume that borrowers relied on those misrepresentations without requiring an application.

Student and Taxpayer Protections

When colleges get into financial trouble or take actions that harm students, they should be the ones held responsible for losses that arise from discharged Federal student loans – not taxpayers. The final regulations will hold institutions accountable so that taxpayers are better protected when schools are at risk of closing, including when they may face closure because of liabilities from borrower defense claims. These regulations help to mitigate the effects of a large-scale closure akin to the demise of Corinthian.

Specifically, the final regulations establish a number of triggering and early-warning events that, if significant enough to cause a school to have a failing financial responsibility composite score, would automatically require the school to provide financial protection to the Department, such as a letter of

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credit (LOC), that totals at least 10 percent of the amount of Title IV funds received by the school over the previous year. The financial composite score is a measure of a school's financial viability, with failing scores indicating that schools are at risk of shutting down because they can't fulfill their financial obligations. Automatic triggering events include instances in which a State or Federal government entity such as an attorney general, the CFPB, or the FTC brings a suit against the school for borrower defense-related reasons, debts and liabilities stemming from borrower defense-related administrative actions, or any other lawsuit against the school that reaches summary judgment. Other triggers that are not tied to the school's composite score but that indicate risk of closure include:

- The institution fails the 90/10 non-Federal revenue requirement;
- The institution's cohort default rate exceeds 30 percent two years in a row after appeal.

In total, the amount of financial protection provided by institutions should be sufficient to fully cover any estimated losses to the government that may follow if the threats identified as triggering and early-warning events actually occur; however, the Department may reduce any required amount above 10 percent if an institution demonstrates that it is unnecessary to protect, or is contrary to, the Federal interest. These financial protection funds could be used to cover the costs of closed school discharges and/or borrower defenses in the event they arise.

Changes from NPRM: Upon review of the comments the Department received, we revised the financial responsibility provisions in the final regulations to better correspond with the Department's existing methods for assessing financial risk while factoring in certain events associated with a risk of closure. These revisions include:

- Integrating triggering events into the existing financial composite score framework;
- Establishing a minimum standard of protection, rather than requiring cumulative letters of credit;
- Ensuring opportunities for appeal for institutions to show that liabilities are insured or resolved; and
- Revising a number of the triggers to prevent automatically requiring financial protection in instances where actions or events do not necessarily reflect a risk of closure.

Early Warnings for Students

To ensure that students can make more informed decisions, the final regulations will provide students with more information about risky institutions. As part of that transparency goal, institutions that are required to provide financial protection to the Department due to triggering events discussed above will have to disclose this fact to students, if consumer testing shows that the warnings are useful to students.

Additionally, proprietary institutions will be required to include a warning in their advertising and marketing materials if their students have very poor loan repayment outcomes. Proprietary institutions are far more likely than public or non-profit institutions to have poor repayment outcomes, and pose the greatest risk to students and taxpayers. The Department already calculates repayment rates for nearly all borrowers at proprietary schools through the Gainful Employment regulations; thus, there will be little increase in burden. Proprietary institutions at which fewer than half of recent borrowers have paid down a single dollar of their loan balances three years after leaving school will have to include a

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warning in their promotional materials to inform student decisions about college enrollment or borrowing.

Changes from the NPRM: To ensure the financial protection disclosures are meaningful and relevant to students, the Department will determine through consumer testing which triggers require a disclosure – rather than requiring the disclosures for all events, even those that are less relevant to students. Additionally, the repayment rate warning provision was streamlined and clarified from the proposed regulations to rely on existing data reported through the Gainful Employment regulations for proprietary institutions, ensuring that information is efficiently and effectively communicated to students.

Increased Access to Closed School Discharges

Many borrowers eligible for a closed school discharge of their loans do not apply. The Department is concerned that some borrowers are unaware 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. Under the final regulations, borrowers will receive accurate and complete information with regard to their eligibility for a closed school discharge earlier in the process, and may receive automatic discharges if they do not subsequently re-enroll at another school. With these changes:

- The Department will 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 for closed school discharge, as well as information on borrowers' right to opt-out of the teach-out and instead receive a discharge; and
- Eligible borrowers who were enrolled at a school that closed on or after November 2013 and who have not re-enrolled at another school within three years of that closure will automatically have their loans discharged.

Changes from the NPRM: As described in the notice of final regulations, the Department plans to early implement the automatic closed school discharge provisions as soon as operationally possible. Early implementation allows, prior to July 2017, borrowers eligible for an automatic discharge without an application—meaning eligible borrowers who attended a school that closed on or after November 1, 2013, and who have not re-enrolled in another Title IV-eligible institution within three years of the school's closure—to be granted that discharge. Eligible borrowers who attended Corinthian at its closure will benefit from the intended early implementation of this provision.

Protections against Any Pre-dispute Arbitration Agreements

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 pre-dispute arbitration. 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

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change its practices while Corinthian was still a viable entity. Instead, affected Corinthian student borrowers with Direct Loans 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, with costs borne by the taxpayer. The final regulations will 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 final regulations, schools will no longer be able to forbid class actions for borrower defense-type claims.
- **Ending Day-in-Court Denials.** The Obama Administration wants to empower students to seek relief directly from schools that cause harm to the students. Some schools tuck clauses into enrollment agreements that block students from ever taking the school to court and instead commit them to arbitrate their claims before they arise. The final rule allows students to agree to arbitration of their claims, but only after disputes arise.
- **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 final regulations 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.

Changes from the NPRM: In the NPRM, the Department proposed to ban all pre-dispute mandatory arbitration agreements for borrower defense related disputes that were a condition of enrollment. Importantly, the final regulations ban *any* pre-dispute arbitration agreements, whether voluntary or mandatory, and whether or not they contain opt-out clauses. These changes will strengthen protections for students, and further the goals of this regulation, by ensuring that students who choose to enter into an agreement to arbitrate their borrower defense type claims do so freely and knowingly.

Other Provisions

Ensuring All Federal Student Loan Borrowers Have Access to Borrower Defense Relief

The final regulations recognize Federal Family Education Loan (FFEL) and Perkins loan borrowers' ability to receive borrower defense relief through Direct Consolidation Loans. The final regulations will 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, and this provision will be designated for early implementation on November 1, 2016.

False Certification

To provide loan discharge relief in instances where schools falsely certify their students' high school diploma status, the final regulations specify that a borrower qualifies for a false certification discharge if the borrower reported to the school that the borrower did not have a high school diploma or its equivalent and did not satisfy applicable alternative to graduation from high school requirements, but

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the school nevertheless arranged a loan. In these situations, the borrower will 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 final regulations 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 Final Regulations Also:

- Expand the types of documentation that may be used in granting 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.