



Decoding the Final Borrower Defense Rule

A Webinar Series from the Thompson Coburn Higher Education Team



Borrower Defense Webinar Series

- Webinar series schedule:
 - **The New Borrower Defense Framework (November 29, 2016)**
 - The Revised Financial Responsibility Standards (December 1, 2016)
 - Changes to Closed School and False Certification Discharge (December 6, 2016)
 - The Elimination of Pre-Dispute Arbitration Clauses and the New Repayment Rates for Proprietary Schools (December 8, 2016)

WELCOME & INTRODUCTION

- **Aaron D. Lacey**
 - Partner, Higher Education Practice, Thompson Coburn LLP.
- **Higher Education Practice**
 - Provide regulatory counsel on federal, state, and accrediting agency laws and standards (e.g., Title IV, Title IX, Clery, consumer information).
 - Assist with postsecondary transactions, contract drafting and negotiation, policy creation, and compliance systems design.
 - Represent institutions in student and employee litigation, government investigations, administrative proceedings, audits, and reviews.

Welcome & Introduction

- **Prior Experience**
 - Senior Vice President of Regulatory Affairs & Strategic Development for postsecondary institution. Oversaw regulatory, compliance, and government affairs matters for 24 campus locations in Midwest and Southeast United States, as well as for online division.
 - Attorney in DC Higher Education Practice. Provided regulatory and policy guidance, managed agency proceedings, drafted and negotiated wide variety of agreements.

Presentation Outline

- Politics & Prognostications
- The New Rule from 40,000 Feet
- The Borrower Defense Origin Story
- The New BD Framework
 - Claims on Loans Made Before July 1, 2017
 - Claims on Loans Made After July 1, 2017
 - BD Claims and Risk Management
 - The Individual Claim Process
 - The Group Claim Process
 - Calculating Relief
- TC Resources

Politics & Prognostications



Look Into My Crystal Ball...

Will this rule ever go into effect?

- **The Congressional Review Act**
 - Permits Congress to enact a “resolution of disapproval,” which if passed by both houses of Congress and signed by the President overturns any rule promulgated by a federal administrative agency.
 - Congress must act within 60 legislative days of a rule’s introduction.

Look Into My Crystal Ball...

- Sets an expedited legislative path, requires only a simple majority rather than the usual 60 votes needed to block a filibuster.
- Removal through rulemaking
 - ED can modify or remove the rule through the rulemaking process
- Suspension of enforcement
 - ED can simply determine not to enforce the rule

Look Into My Crystal Ball...

- Congress will not act, nor will the White House, if the borrower defense rule is not a **priority**.
- The borrower defense statute and existing rule are already on the books, and will remain even if the new rule is struck down.
- Thousands of claims are being submitted, and will have to be dealt with through some process.

The New Rule from 40,000 Feet



Elements of the New Rule

Borrower Defense Framework

Financial
Responsibility Triggers

Arbitration
Agreements

Closed School
Discharge

False
Certification
Discharge

Misrep-
resentation

Repayment
Rates for
Prop. Schools

Implementation Timeline

DATE	2016 RULEMAKING EVENTS
Jan. – Mar.	<ul style="list-style-type: none">• Negotiated rulemaking committee meets
June 16	<ul style="list-style-type: none">• Proposed rules published
August 1	<ul style="list-style-type: none">• Comment period closes
Nov. 1	<ul style="list-style-type: none">• Publication of final rule in Federal Register*
July 1, 2017	<ul style="list-style-type: none">• Effective date of new rule^

*Pursuant to Section 482(c) of the HEA, ED must publish final regulations before November 1 of a given year in order for them to take effect on July of the following year.

^Also pursuant to Section 482(c) of the HEA, ED has designated certain regulations for voluntary, early implementation by the regulated community, and elected to implement early certain requirements that are entirely the responsibility of ED.

The Borrower Defense Origin Story

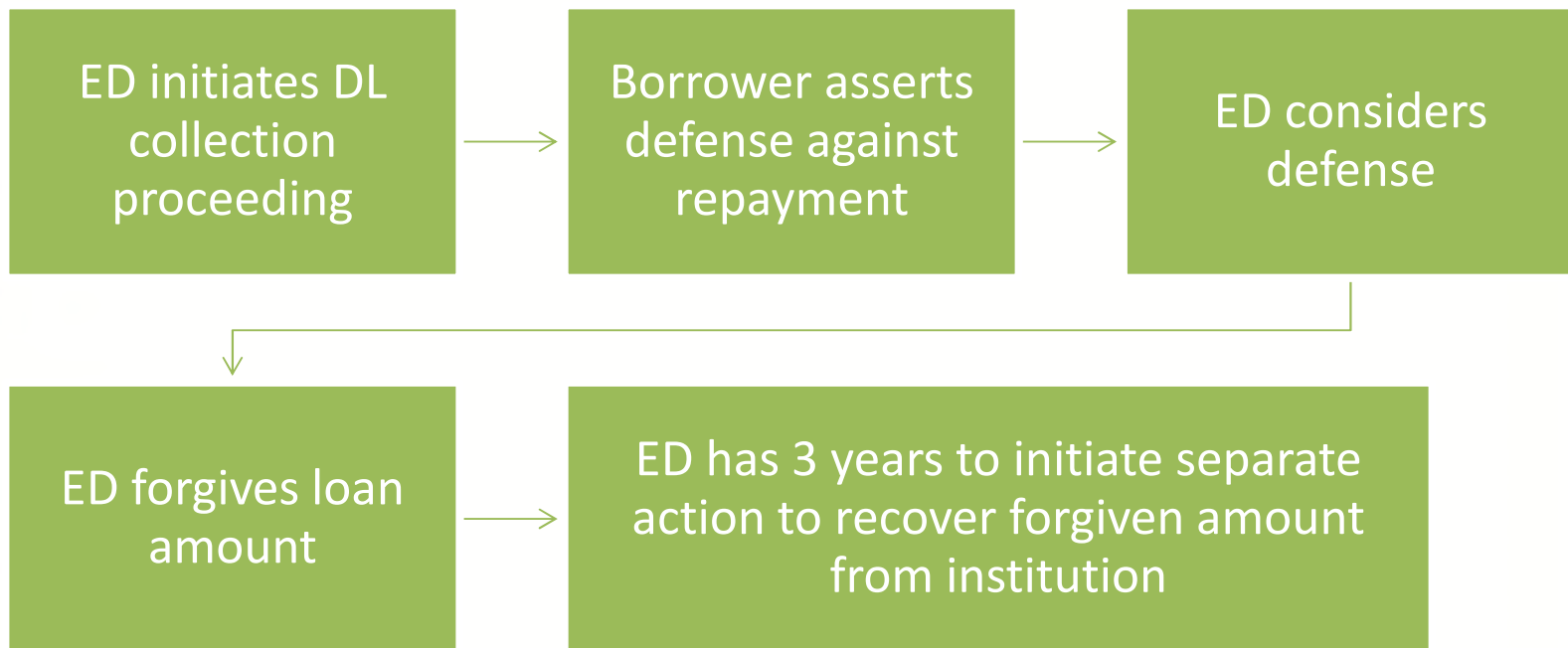
In 1993, Congress created the Direct Loan program. As part of that legislation, Congress directed:

[T]he Secretary shall specify in regulations which acts or omissions of an institution of higher education a borrower may assert as a defense to repayment of a loan made under this part[.]

HEA 455(h); 20 USC 1087e(h).

The Borrower Defense Origin Story

The following year, ED introduced at 34 CFR § 685.206(c) the basic framework that still exists today:



The Borrower Defense Origin Story

Under current law, a **defense** includes:

[A]ny 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.

34 CFR § 685.206(c)

The Borrower Defense Origin Story

In 1995 Notice of Interpretation, ED added that cause of action must directly relate to the **loan** or to the school's **provision of educational services** for which the loan was provided.

- Personal injury tort claims or actions based on allegations of sexual or racial harassment, for example, would be excluded.

60 Fed. Reg. 37768 (Jul. 21, 1995).

The Borrower Defense Origin Story

With regard to timing:

- A borrower can assert a defense at any time, without regard to when the underlying act or omission occurred.
- ED only has three years from borrower's last award year to "initiate proceeding" to **recover** lost funds from school.

34 CFR § 685.206(c)(3).

The Borrower Defense Origin Story

- No discussion in current law of the “process” ED would follow in a **recovery** action - no reference to Subpart G (FLST) or Subpart H (Audit/PR).
- However, in 1995, ED acknowledged schools “entitled to due process in these proceedings.”

60 Fed. Reg. 37768 (Jul. 21, 1995).

The New BD Framework for Loans Made Before July 1, 2017



For Loans Made **Before** July 1, 2017

Nixes Collection Action

- No longer requires collection action to precede defense claim

Similar definition of borrower defense claim

- Must be cause of action under State law
- Codifies “loan or educational service”

Same time limit on borrower asserting claim

- Borrower may assert defense at any time

New time limits on ED recovery actions

- Time limits tied to statute of limitations and notice of claim

New individual claim process

- No collection proceeding required
- ED staff reviews claim

New group claim process

- ED initiates process (no claims required)
- Hearing official reviews group claim

New methods for calculating relief

- New methods include valuation of institution’s education

Time Limit on Recovery Actions

ED may initiate a recovery action against a school within the later of:

- Three years from the end of the last award year in which the student attended the school; or
- The State statute of limitations applicable to the cause of action on which the borrower defense claim is based.

ED may initiate a recovery action **at any time** if the school had **notice** of the claim before the later of the two periods expires.

New 34 CFR § 685.206(c)(3)-(4).

Time Limit on Recovery Actions

A school has notice if it has received:

- Actual notice from the borrower, a borrower rep, or from ED;
- A class action complaint that **may** include the borrower; or
- Written notice, including a civil investigative demand or other written demand for information, from a Federal or State agency that has power to initiate an investigation into conduct of the school relating to specific programs, periods, or practices that **may** have affected the borrower.

New 34 CFR § 685.206(c)(3)-(4).

The New BD Framework for Loans Made After July 1, 2017



For Loans Made **After** July 1, 2017

No collection action required

- Does not require collection action to precede defense claim

New definition of borrower defense claim

- Judgement, breach of contract, and substantial misrepresentation

New time limitations on asserting claim

- Few limitations, which vary by nature of claim

New time limitations on recovery actions

- Time limits tied to statute of limitations and notice of claim

New individual claim process

- No collection proceeding required
- ED staff reviews claim

New group claim process

- ED initiates process (no claims required)
- Hearing official reviews group claim

New methods for calculating relief

- New methods include valuation of institution's education

BD Claim Defined

A borrower defense exists where an act or omission of the school relates to (1) the making of the loan or (2) the educational services for which the loan was provided, and:

- Was the basis for a **judgement** against the school;
- Was the basis for a **breach of contract**;
or
- Was a **substantial misrepresentation**.

New 34 CFR § 685.222(a)-(d).

BD Claim Defined

A violation by the school of an HEA eligibility or compliance requirement is not a basis for a borrower defense unless the violation would **otherwise** constitute a basis for a borrower defense.

New 34 CFR § 685.222(a)(3).

Judgement

Would include any non-default, favorable contested judgment secured by a borrower **or governmental agency** based on State or Federal law in a court or administrative tribunal of competent jurisdiction.

No limitation on when a claim could be brought.

New 34 CFR § 685.222(b).

Breach of Contract

Would include any failure to perform under terms of contract with student, without regard to materiality. Contract could include “an enrollment agreement and any school catalogs, bulletins, circulars, student handbooks, or school regulations.”

No limitation on claims to discharge future amounts owed and **six-year limitation** (from the date of the breach) on claims to discharge amounts already paid.

New 34 CFR § 685.222(c); 81 Fed. Reg. 39341 (June 16, 2016).

Substantial Misrepresentation

Would include any substantial misrepresentation made by the school or any contractual partner. No materiality standard, but borrower must show actual, **reasonably reliance** to his or her detriment.

No limitation on claims to discharge future amounts owed and **six-year limitation** (from the date of discovery) on claims to discharge amounts already paid.

New 34 CFR § 685.222(d).

Misrepresentation Defined

Misrepresentation: Any false, erroneous or misleading statement an eligible institution, one of its representatives, or any ineligible institution, organization, or person with whom the eligible institution has an agreement to provide educational programs, or to provide marketing, advertising, recruiting or admissions services makes directly or indirectly to a student, prospective student or any member of the public, or to an accrediting agency, to a State agency, or to the Secretary. A misleading statement includes any statement that has the likelihood or tendency to **mislead under the circumstances**. A statement is any communication made in writing, visually, orally, or through other means. Misrepresentation includes the dissemination of a student endorsement or testimonial that a student gives either under duress or because the institution required the student to make such an endorsement or testimonial to participate in a program. **Misrepresentation includes any statement that omits information in such a way as to make the statement false, erroneous, or misleading.**

New 34 CFR § 668.71(c).

Subst. Misrepresentation Defined

Substantial misrepresentation: Any misrepresentation on which the person to whom it was made could reasonably be expected to rely, or has reasonably relied, to that person's detriment.

- ED has made abundantly clear that institutions are accountable, even where mistakes are made.

New 34 CFR § 668.71(c).

Subst. Misrepresentation Defined

“We believe that an institution is responsible for the harm to borrowers caused by its misrepresentations, even if such misrepresentations cannot be attributed to institutional intent or knowledge and are the result of inadvertent or innocent mistakes. Similarly, we believe this is the case even for statements that are true, but misleading.”

81 Fed. Reg. 75948 (Nov. 1, 2016).

Reasonable Reliance

Finding of reasonable reliance more likely if evidence shows school was:

- 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.

New 34 CFR § 685.222(d)(2).

Risk Assessment

Claims will be easier to bring:

- The rule permits defense claims to be brought outside the context of a collection action and without regard to whether a borrower is able to make loan payments.
- The rule does not include a materiality standard for breaches of contract.

Risk Assessment

- The rule does not include a *bona fide* materiality standard for substantial misrepresentations.
 - A borrower could establish a claim by providing evidence that the institution made a misrepresentation – even if by mistake – and that she reasonably relied upon it to her detriment. Neither the mistake, nor the detriment, need be material.
 - Moreover, in group claims, there would be a rebuttable presumption of actual reliance.

Risk Assessment

ED has increased ability to recover from institutions:

- ED can initiate recovery actions years after the alleged act or omission.
- ED can re-open claims to review new evidence.
- ED can even certify and bring group claims on behalf of borrowers.

Risk Assessment

It is extraordinarily difficult to control all representations made by a large institution:

- We all have knuckleheads
- Vendors are difficult to monitor

We don't know whether the next administration will keep the promises made by the drafters of the rule.

Risk Management

- Keep policies, marketing materials, and all other external communications lean and flexible.
- Review and enhance controls in vendor contracts, include explicit indemnification for borrower defense liabilities.
- Ensure behaviors highlighted by ED are prohibited in policy and practice (e.g., codes of conduct, internal protocols).

Examples of BD Claims

BD Claim 1: A school represents to prospective students, in widely disseminated materials, that its educational program will lead to employment in an occupation that requires State licensure. The program does not in fact meet minimum education requirements to enable its graduates to sit for the exam necessary for them to obtain licensure.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Relief 1: Borrowers who enrolled in this program during the time that the misrepresentation was made should receive full relief. As a result of the schools' misrepresentation, the borrowers cannot work in the occupation in which they reasonably expected to work when they enrolled. Accordingly, borrowers received limited or no value from this educational program because they did not receive the value that they reasonably expected.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Risk Management Lesson: Carefully review and map licensure requirements for graduates in all applicable jurisdictions.

- Ensure that plain disclosures are made and acknowledged prior to enrollment.
- Update disclosures quarterly.

Examples of BD Claims

BD Claim 2: A school states to a prospective student that its medical assisting program has a faculty composed of skilled nurses and physicians and offers internships at a local hospital. The borrower enrolls in the school in reliance on that statement. In fact, none of the teachers at the school other than the Director is a nurse or physician. The school has no internship program. The teachers at the school are not qualified to teach medical assisting and the student is not qualified for medical assistant jobs based on the education received at the school.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Relief 2: This borrower should receive full relief. None of the teachers at the school are qualified to teach medical assisting, and there was no internship. In contrast to reasonable students' expectations, based on information provided by the school, the typical borrower received no value from the program.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Risk Management Lesson: Keep marketing and admissions materials current, **and** keep admissions personnel apprised of any current or **planned** changes to program or program personnel.

Examples of BD Claims

BD Claim 3: An individual interested in becoming a registered nurse meets with a school's admissions counselor who explains that the school does not have a nursing program but that completion of a medical assisting program is a prerequisite for any nursing program. Based on this information, the borrower enrolls in the school's medical assisting program rather than searching for another nursing program, believing that completing a medical assisting program is a necessary step towards becoming a nurse. After one year in the program, the borrower realizes that it is not necessary to become a medical assistant before entering a nursing program. The borrower's credits are not transferrable to a nursing program.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Relief 3: This borrower should receive full relief. Because it is not necessary to become a medical assistant prior to entering a nursing program, she has made no progress towards the career she sought, and in fact has received an education that cannot be used for its intended purpose.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Risk Management Lesson: Document student interests and career objectives in an application for admission.

Examples of BD Claims

BD Claim 4: A school tells a prospective student, who is actively seeking an education, that the cost of the program will be \$20,000. Relying on that statement, the borrower enrolls. The student later learns the cost for that year was \$25,000. There is no evidence of any other misrepresentations in the enrollment process or of any deficiency in value in the school's education.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Relief 4: This borrower should receive partial relief of \$5,000. The borrower received precisely the value that she expected. The school provides the education that the student was seeking but misrepresented the price.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Risk Management Lesson: Ensure that tuition and fee information is clearly documented.

- If program or credit hour costs are subject to change, such qualifications should be plain, and acknowledged in writing by the student.
- If program or credit hour costs are increased, ensure increases are plainly communicated to students in advance.

Examples of BD Claims

BD Claim 5: A school represents in its marketing materials that three of its undergraduate faculty members in a particular program have received the highest award in their field. A borrower choosing among two comparable, **selective** programs enrolls in that program in reliance on the representation about its faculty. However, although the program otherwise remains the same, the school had failed to update the marketing materials to reflect the fact that the award-winning faculty had left the school.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Relief 5: Although the borrower reasonably relied on a misrepresentation about the faculty in deciding to enroll at this school, she still received the value that she expected. Therefore, no relief is appropriate.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Risk Management Lesson: Be a selective institution with award-winning faculty.

- Focus monitoring and control efforts on representations that are material to the quality of the program.

Examples of BD Claims

BD Claim 6: An individual wishes to enroll in a selective, regionally accredited liberal arts school. The school gives inflated data to a well-regarded school ranking organization regarding the median grade point average of recent entrants and also includes that inflated data in its own marketing materials. This inflated data raises the place of the school in the organization's rankings in independent publications. The individual enrolls in the school and graduates. Soon after graduating, the individual learns from the news that the school falsified admissions data. Notwithstanding this issue, degrees from the school continue to serve as effective, well-regarded liberal arts credentials.

New Appendix A to subpart B of part 685.

Examples of BD Claims

Relief 6: The borrower relied on the misrepresentation about the admissions data to his detriment, because the misrepresentation factored into the borrower's decision to choose the school over others. However, the borrower received a selective liberal arts education which represents the value that he could reasonably expect, and gets no relief.

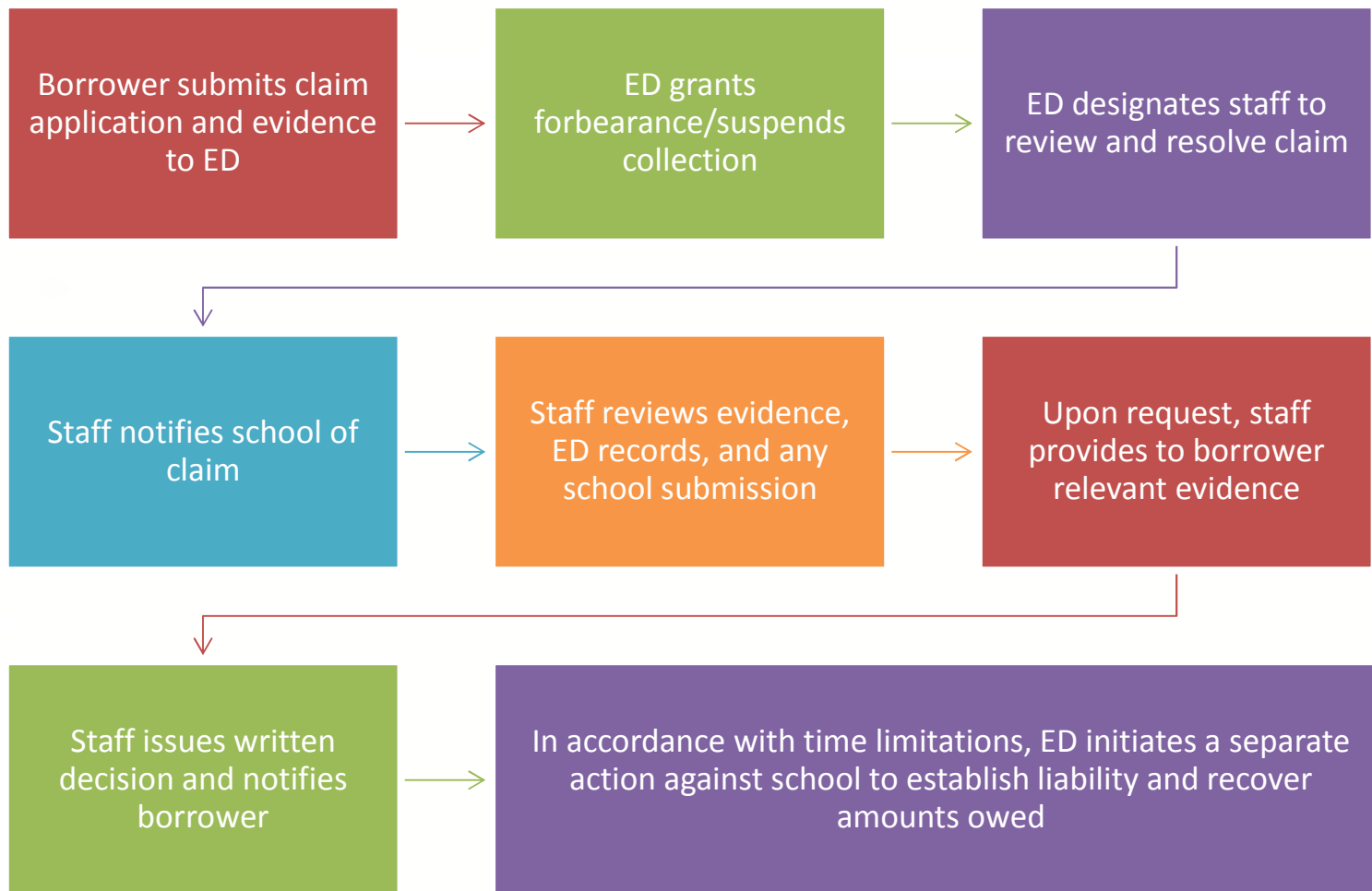
New Appendix A to subpart B of part 685.

Examples of BD Claims

Risk Management Lesson: Monitor closely representations made to third parties by any person or department affiliated with the institution.

ED could determine, separately, that the school violated the title IV requirement that it not make substantial misrepresentations pursuant to 34 CFR 668.71, which constitutes an enforceable violation separate and apart from any borrower defense relief.

Individual Claim Process



New 34 CFR § 685.222(e).

Individual Claim Process

- A borrower may request reconsideration at any time based on **new evidence**, which is relevant evidence (1) not previously provided and (2) not identified in the final decision as evidence relied upon.
- ED may reopen a claim at **any time** to consider new evidence.

New 34 CFR § 685.222(e)(5).

Individual Claim Process

ED may initiate a recover action against a school:

- At any time for claims based on judgments against a school.
- For six years where claims are based on breach of contract or substantial misrepresentation.
- **At any time** if the school had **notice** of the claim before the noted periods expire.

New 34 CFR § 685.222(e)(7).

Procedural Concerns

Independent hearing official not required

ED not required to supply evidence to school

School not guaranteed right to respond

No guaranteed timeframe for response

ED not required to provide school with written determination

School has no right to request new review based on new evidence

Does not discuss process for ED recovery action

Affords no appeal opportunity to schools

ED's Procedural Punt

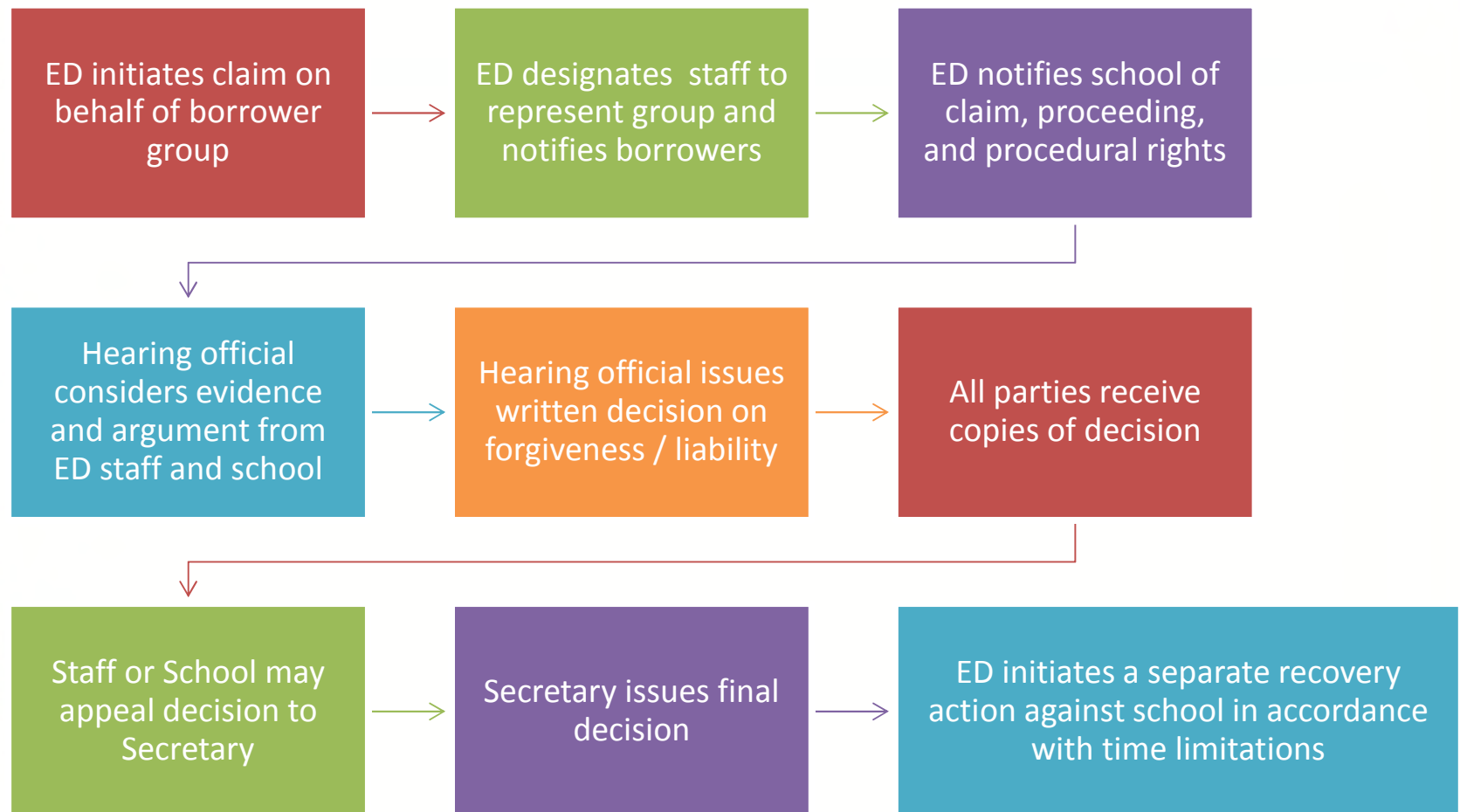
ED has indicated that it will “outline more specific details about the process for schools and borrowers in forthcoming procedural rules.” With regard to recovery actions:

- It “will ensure an opportunity for the school to present its defenses and be heard.”
- It will be comparable to subpart G (FLST) and subpart H proceedings (audits, program reviews).
- Conducted by an independent ED official.
- An appeal option may not be provided.

The Group Claim Process



Group Claim Process (Open School)



New 34 CFR § 685.222(f) and (h).

Group Claim Process (Open School)

- If relief for the group has been denied in full or in part, a borrower may still file an **individual claim** based on the same underlying act or omission.
- ED may reopen a claim at **any time** to consider new evidence.

New 34 CFR § 685.222(h).

Group Claim Process (Open School)

- If relief for the group has been denied in full or in part, a borrower may still file an **individual claim** based on the same underlying act or omission.
- ED may reopen a claim at **any time** to consider new evidence.

New 34 CFR § 685.222(h).

Group Claim Process (Open School)

ED may initiate a recover action against a school:

- At any time for claims based on judgments against a school.
- For six years where claims are based on breach of contract or substantial misrepresentation.
- **At any time** if the school had **notice** of the claim before the noted periods expire.

New 34 CFR § 685.222(h)(5).

Procedural Concerns

ED not required to provide school with evidence filed in support of claims

ED not required to identify to school evidence ED considers relevant

School not guaranteed a right to respond to ED

No timeframes specified for communications with ED

Appeal right guaranteed, but no procedures discussed

New rule suggests separate recovery proceeding, but no procedures discussed

Another Procedural Punt

The Department understands commenters' concerns regarding the broad guidelines for the group fact-finding process... The Department is developing procedural rules to govern the fact-finding processes... which will establish these details more firmly and be informed by the procedures and protections established by the Department in its other administrative proceedings, such as 34 CFR part 668, subparts G and H.

81 Fed. Reg. 75970 (Nov. 1, 2016).

Calculating Relief



Calculating Relief

- The **amount** of relief granted is determined by ED, and can range from nothing to all amounts previously paid and still owed on the loan plus “any associated costs and fees.”
 - Excludes non-pecuniary damages such as inconvenience, aggravation, emotional distress, or punitive damages.

New 34 CFR § 685.222(i).

Calculating Relief

- Relief is offset by any financial benefit already received by borrower and related to borrower defense (e.g., through refund, settlement, debt forgiveness).
- Under the new rule, the **methodology** used to calculate relief varies based on the nature of the underlying claim.

New 34 CFR § 685.222(i).

Calculating Relief

Judgment Against the School

- Where the judgment awards specific financial relief, relief will be the amount of the judgment that remains unsatisfied, up to the amount of the loan
- Where the judgment does not award specific financial relief, ED will “rely on the holding of the case and applicable law to monetize the judgment.”

New 34 CFR § 685.222(i).

Calculating Relief

Breach of Contract

- Relief will be determined according to the common law of contracts, subject to the loan cap limitation and “any other reasonable considerations.”

New 34 CFR § 685.222(i).

Calculating Relief

Substantial Misrepresentation

- ED will balance various factors:
 - Cost of attendance
 - The value of the education received
 - The value of the education that a reasonable borrower in the borrower's circumstances would have received
 - The value of the education the borrower should have expected given the information provided by the institution
- Schools have the burden of proof regarding the value of their education

New 34 CFR § 685.222(i).

TC Resources



TC Resources

Our higher education law blog, [REGucation](#).



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Title IX and due process: ED tells Wesley that accused student not treated fairly

[Paul Stoehr](#) [Aaron Lacey](#) [November 2, 2016](#)



In a rare move, the Department of Education announced on October 12, 2016, its determination that Wesley College in Delaware had violated Title IX by failing to provide appropriate procedural protections to a student accused of sexual misconduct. [READ MORE](#)



Contact Information

Aaron D. Lacey, Esq.

Partner, Higher Education Practice

Thompson Coburn LLP

alacey@thompsoncoburn.com

314-552-6405

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