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U.S. Department of Education provides guidance on implementation of 2016 "borrower defense to repayment" regulations

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On March 15, 2019, the U.S. Department of Education (ED) issued an Electronic Announcement to provide guidance to colleges and universities about selected provisions contained in final regulations often referred to as the borrower defense to repayment regulations, which were published on November 1, 2016 (the 2016 final regulations). For a summary of the 2016 final regulations, please see our previous alert. The selected provisions were originally scheduled to become effective July 1, 2017, but ED sought to delay their effective date. On March 19, 2019, ED acknowledged in the Federal Register that the selected provisions took effect as of October 16, 2018, in accordance with a court's decision in related litigation.

The 2016 final regulations borrower defense to repayment standard

In the March 15 Electronic Announcement, ED confirmed that it will apply the federal standard for borrower defense to repayment applications set forth in the 2016 final regulations for claims asserted as to Direct Loans first disbursed on or after July 1, 2017. Under the 2016 final regulations, a Direct Loan borrower may assert a claim based on several situations, including a judgment against the institution, breach of contract by the institution, or substantial misrepresentation by the institution.

Complying with other provisions of the 2016 final regulations

In the March 15 Electronic Announcement, ED also addressed institutions' responsibilities to comply with the following sections of the 2016 final regulations:

- *Financial responsibility triggering events:* The 2016 final regulations amend ED's regulations specifying the standards institutions must meet to be deemed financially responsible. Under the 2016 final regulations, an institution must notify ED within specific time frames of certain events, actions, or conditions that occur on or after July 1, 2017.[1] In the

[1] Those events, conditions, and actions include: certain debts, liabilities, and losses (34 CFR 668.171(c)); for proprietary institutions, noncompliance with the "90/10 rule" (34 CFR 668.171(d)); for publicly-traded institutions, certain actions by the U.S. Securities and Exchange Commission or relevant stock exchange (34 CFR 668.171(e)); and certain other factors and events related to the institution's state licensure, accreditation, or loan agreements (34 CFR 668.171(g)). See the 2016 final regulations at 81 Fed. Reg. 76,073 to 76,074.

Electronic Announcement, ED explained how institutions should handle reporting for events, actions, or conditions that occurred between July 1, 2017 and the date of the Electronic Announcement:

- With respect to debts, liabilities, and losses the impact of which was reflected in the institution's most recent financial statement submitted after July 1, 2017, the institution need give no further notice. However, separate notification is required for certain events that occurred after the end of the fiscal year covered by the most recent annual audited financial statements submitted to ED, including certain debts, liabilities, and losses and certain lawsuits that were filed after July 1, 2017 and remain pending as of the date of the Electronic Announcement.
- Proprietary institutions must notify ED of any violation of the 90/10 rule for any fiscal year beginning on or after July 1, 2017; publicly traded institutions must notify ED of certain actions by the U.S. Securities and Exchange Commission or stock exchange occurring after July 1, 2017.
- Institutions must notify ED of certain citations from state licensing or authorizing agencies, or show-cause orders or probation statuses from accrediting agencies, if such actions were unresolved as of March 15, 2019.
- Institutions must notify ED of violation of a provision in a loan agreement occurring after July 1, 2017 and constituting a default or delinquency that triggers remedial rights of the creditor.

In each case where notification is required, the institution must notify ED by sending an email to FSAFRN@ed.gov within 60 days of the Electronic Announcement – that is, by our calculation, May 13, 2019.

- *Class action bans and predispute arbitration agreement provisions*. The 2016 final regulations include certain prohibitions related to dispute resolution between institutions and students with respect to claims that are or could be asserted as a borrower defense claim under ED's administrative process.[2] The 2016 final regulations also require institutions to submit certain arbitral and judicial records to ED.[3] In the March 15 Electronic Announcement ED made clear that "[b]ecause the 2016 Final Regulations are now in effect, institutions are required to implement these changes." However, ED acknowledged that some institutions and students may have entered into now-prohibited agreements between July 1, 2017 and the date of the Electronic Announcement, and it may take some time to develop new, compliant agreements. Specifically, ED directed:
  - Any arbitration that was ongoing as of October 16, 2018 and initiated pursuant to a now-prohibited predispute arbitration agreement is deemed unenforceable. Institutions must notify borrowers within 10 days of the Electronic Announcement (by our calculation, March 24, 2019). A borrower may choose to continue with arbitration, but has no obligation to do so.
  - Within 90 days of the Electronic Announcement (by our calculation, June 12, 2019), institutions must submit copies of certain arbitral records for any dispute in arbitration based on a borrower defense claim that was pending as of or initiated after July 1, 2017. Within the same time frame, institutions must submit copies of

[2] The 2016 final regulations address internal dispute resolution (see 34 CFR 685.300(d)); class action bans (see 34 CFR 685.300(e)); and predispute arbitration agreements (see 34 CFR 685.300(f)).

[3] See 34.CFR 685.300(g) with respect to arbitral records and 34 CFR 685.300(h) with respect to judicial records.

certain judicial records for any lawsuit based on a borrower defense claim that was pending as of or initiated after July 1, 2017.

  - As contemplated by the 2016 final regulations, ED confirmed that institutions are not required to issue new enrollment agreements or contracts to students who may have accepted the now-prohibited provisions; however, those agreements cannot be enforced with respect to any borrower defense claim made by a Direct Loan borrower against the institution.

  - The institution may choose either (1) to amend its enrollment agreement to comply with the required prohibitions within 60 days of the March 15 Electronic Announcement or (2) to begin complying with the notice requirements of the 2016 final regulations within 60 days of the March 15 Electronic Announcement. If the institution chooses to comply with the notice requirement, it must provide the required notice no later than at the point of exit counseling or the date on which the institution files its initial response to a demand for arbitration or service of a complaint from a student who has not already received notice. The March 15 Electronic Announcement includes prescribed language for amendment of predispute arbitration agreements and class action waivers, as well as for notices to students concerning such agreements.

- *Financial protection disclosures*. The 2016 final regulations would require all institutions to disclose to prospective and enrolled students the occurrence of certain triggering events that are indicators of financial responsibility, based on ED's determination of the events for which such disclosure will be required and the form of such disclosure. Institutions are not required to make any such disclosures until ED completes consumer testing "in the near future."

- *Repayment rate disclosures*. The 2016 final regulations would also require proprietary institutions that do not meet a certain loan repayment rate to include a specific warning in promotional materials made available to prospective and enrolled students. Institutions are not required to make any such disclosures until ED completes consumer testing "in the near future to ensure the warning is meaningful and helpful to students."

Conclusion

Institutions that participate in the Title IV federal student financial aid programs should review the March 15 Electronic Announcement to identify compliance obligations that apply to them and to make preparations to comply in accordance with the deadlines set forth in the Electronic Announcement.

ED Secretary Betsy DeVos has expressed an intent to initiate revisions to the 2016 final regulations. ED conducted negotiated rule-making on the topic, but the negotiators did not reach consensus. ED published a notice of proposed rule-making in July 2018 but no final rule has yet been issued. Institutions should stay tuned for possible future developments in this area.

Contacts

Elizabeth B. Meers
Senior Counsel, Washington, D.C.
T +1 202 637 8676
elizabeth.meers@hoganlovells.com

Michelle Tellock
Senior Associate, Washington, D.C.
T +1 202 637 6561
michelle.tellock@hoganlovells.com