

Negotiations on New Defense to Repayment Rules Fail: It's All Up to ED Now

March 28, 2016

Following a highly charged, often contentious three days of debate, the third session of the Negotiated Rulemaking on Borrower Defense to Repayment (DTR) ended as it started, without consensus. The Department of Education (ED) is now free to promulgate the regulations it wants, entirely independent of the DTR negotiations.

Eleven "issue papers" were discussed, covering a wide range of topics, many of them completely unrelated to the original purpose of drafting regulations for the implementation of a provision of the Higher Education Act intended to establish a process for determining whether borrowers could avoid repayment on a Federal Direct student loan based on an act or omission by their school. Instead, ED, along with negotiators representing state attorneys general and consumer and student groups, used the rulemaking process to seek to create rules far beyond DTR, affecting completely unrelated provisions of statute and regulation, as well as creating new and extremely broad rules tied in the most tenuous manner to the statutory DTR provisions.

Two major themes have emerged:

- As was the case with Gainful Employment, a brief statutory provision that for decades had very limited applicability (five DTR claims prior to 2015) is being used as a platform for what is likely to emerge as a substantial revision of the relationship of institutions to their students, with the creation of costly administrative requirements and the potential for significant institutional liability.
- As was *not* the case with Gainful Employment, the new DTR Rules will apply to *every single school, college and university* – public and non-profit as well as for-profit – that participates in the Title IV student aid programs.

Notwithstanding the universal application of DTR, the entirety of the Negotiated Rulemaking has been characterized as a response to the precipitous collapse of Corinthian College and as a way to protect students from the depredations of for-profit institutions. The first day of this latest round of negotiations included appearances by both Senator Elizabeth Warren and Representative Maxine Waters whose fiery rhetoric set the tone for the remainder of the discussions: They expressed great concern about "predatory for-profit schools," entreating the negotiators to provide broad borrower relief without complicated requirements. Moreover, they strongly supported additional prescriptive regulations unrelated to the DTR statute, such as banning arbitration agreements that they asserted schools use "to hide their unethical and illegal behavior." Consumer advocates and student groups, largely supported by representatives of attorneys general, battled the relatively few representatives of institutions and postsecondary organizations over virtually every aspect of the proposed rules from the validity of high school diplomas to the usefulness of student disclosures.

Issue Papers prepared by ED staff have raised a host of issues that should be of very serious concern to every institution that takes part in the Title IV programs. These papers include draft regulatory language for:

- federal standards for borrower relief with few, if any, time limitations, using a broadened definition of misrepresentation, contract breach, and state or federal court judgments against the institution;
- the establishment of relief processes for both individual borrowers and groups of borrowers that greatly expand the role of outside government agencies and advocacy groups and rely almost entirely on ED discretion;
- the establishment of an ill-defined process, which inherently amplifies ED's discretion, for the determination of the school's responsibility to repay relieved loans to ED;
- broad new financial capability rules including Letters of Credit using automatic "early warning" triggers that could be extremely burdensome for for-profit and non-profit institutions; and
- the addition of new rules on the use of arbitration provisions in student agreements.

During the course of the three day rulemaking, negotiators complained about the lack of time to review new proposed materials and the feeling that the review and discussion were rushed and insufficient for effective negotiation. At one point there was even a demand by some negotiators that a fourth session be added, to which ED responded in a burst of candor that it was not feasible if the rule was to be published "before the end of the current administration."

Because the panel did not reach consensus, ED is now free to write its own version of the proposed rules. ED's most recent drafts in the final Issue Papers likely provide a preview of where ED is going. In order to meet ED's stated goal of having the DTR rule in place by July 1, 2017, the final rule must be published by November 1, 2016. We anticipate that schedule will necessitate ED publishing a proposed rule for public comment during the summer.

Note that ED asked the Office of Management and Budget (OMB) – which must sign off on any new regulations – for an "expedited review" of the proposed rules. That was denied on the basis of their uncertain budgetary implications, and OMB will be unlikely to sign off on the new rules until the budgetary implications are reasonably well known. This is a very important issue – and one that ED studiously avoided confronting during the negotiations: every loan that cannot be collected due to a successful "defense to repayment" is a liability for the federal government (the DTR rules are being written to apply only to the Direct Loan Program). How much that liability might be if thousands, or tens or even hundreds of thousands, of former students apply for relief is unknown, and ED has declined to attempt to quantify it. That there will be some mechanism to recover funds from the affected schools also leaves open a huge question of how that might be accomplished. Given ED's reluctance to hazard any estimate, when and if OMB will give its approval remains an open issue.

The proposed rules and the discussion were complex and contentious and the potential impact of these new rules could be devastating to some institutions and costly to many. We encourage you to carefully review the draft proposals and those that will be published in the coming months, and to use the public comment period to make well-reasoned and factually-supported arguments to ED. We encourage you to closely review Cooley's follow-up alerts on each of the DTR high impact areas which we will be issuing over the course of the next few weeks. Remember: no category of institution will be immune from the impact of these rules.

Cooley has been tracking the development and evolution of the Borrower Defense to Repayment provision since it first arose in the context of the Corinthian collapse, and our experts have attended each day of the rulemaking. We are well versed in the nuances of the current draft proposals and their potential impact on all types of institutions. We welcome the opportunity to discuss our views and to assist in the drafting of comments during the upcoming response period.

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Key Contacts

Kate Lee Carey San Diego	kleecarey@cooley.com +1 858 550 6089
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Vince Sampson Washington, DC	vsampson@cooley.com +1 202 728 7140
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