



Docket ID ED–2015–OPE–0103

Comments on Proposed Rules on Borrower Defenses and Financial Responsibility

August 1, 2016

The National Association of Student Financial Aid Administrators (NASFAA) submits these comments in response to the Notice of Proposed Rulemaking (NPRM) published June 16, 2016, concerning borrower defenses to loan repayment and financial responsibility standards for institutions. NASFAA represents nearly 20,000 financial aid professionals who serve 16 million students each year at approximately 3,000 colleges and universities of all sectors throughout the country. NASFAA member institutions serve nine out of every ten undergraduates in the U.S.

NASFAA supports the Department of Education’s (ED) intent to standardize the discharge process for loans made under fraudulent or false pretenses, deceptive practices, or other recognizably duplicitous circumstances, and to establish a federal definition of permissible defenses to borrower repayment. Further, schools that encourage or have a pattern of such behavior should be held fully accountable for losses to the federal government.

In regard to institutional eligibility to participate vis à vis financial responsibility, a school’s financial strength must be measured under reasonable standards of financial responsibility. We are not convinced that the rules proposed in this NPRM effectively measure an institution’s financial strength, were negotiated with adequate expert representation, or fall within the parameters anticipated or intended by Congress under section 498 of the Higher Education Act.

While we encourage ED to continue to work towards the goals associated with borrower relief, we have some general concerns that apply to any framework for regulations related to borrower defenses, protection of public funds, and institutional eligibility:

- *Due process must not be undermined.*

Due process includes, but is not limited to, an opportunity for schools to resolve lawsuits before penalties are imposed; pre-emptive punishment hardly aligns with the presumption of innocence. Assuming an event constitutes a mortal threat while limiting a school’s right to explain why its ability to meet its financial obligations or provide necessary administrative resources is not significantly affected, do not reflect that

principle. Further, true due process involves hearing officials who are independent of all parties to a dispute, and allows all parties equal opportunity to present new relevant information that might lead to re-opening a case, or subjects them to equal limitations on that opportunity. It is unclear in the proposed rule under 668.222, or indeed in existing rules under subpart G, who would appoint a hearing official, what their expertise would be, whether it would be a politically appointed person or whether it would be someone with expertise in the law, higher education, or student financial aid. Given the authority being given to the hearing official, it is vital that this position truly be an independent arbiter, not just independent of the designated Department official. free of political influence, with sufficient higher education jurisprudence.

- *Steps taken by ED to protect the public interest should not contribute to an institution's inability to function financially.*

Pre-emptive steps taken by ED based on "trigger" events under proposed 668.171(c) should not further weaken an institution's financial strength while it is still unclear that the institution will fail. Steps taken to secure financial protections for the federal government should not undercut the institution's ability to overcome the triggering event. The public is not served if regulations are more concerned with securing a school's assets rather than ensuring that schools -- that have already been deemed eligible by statute and are in compliance with implementing requirements -- are supported during a temporary, unusual, or uncertain financial threat.

- *Risk assessment should be rigorous and exhaustive to ensure that ED takes action only on circumstances that herald a real and imminent probability of school closure and loss of federal funds.*

Risk assessment of events that might trigger ED action under proposed 668.171(c) should be exhaustively investigated so that steps to secure assets are taken only for those events, and the circumstances in which they occur, that indicate school closure is unavoidable and would otherwise result in ED's inability to collect adequate liabilities. All risk can never be mitigated; in our efforts to offer disadvantaged students educational opportunity, some risk should be shared in the case of events that are not a result of illegal, noncompliant, fraudulent, or intentionally misleading behavior.

We also support the response to this NPRM of the National Association of College and University Business Officers (NACUBO), and the comments made by the American Council on Education (ACE).

## **Financial Responsibility**

The preamble states that ED seeks to take action at the time an event that may affect an institution's viability takes place rather than waiting on annual audited financial statements. However, section 498 of the Higher Education Act places emphasis on the objective evidence of audits: "The determination as to whether an institution has met the standards of financial responsibility provided for in paragraphs (2) and (3)(C) shall be based on an audited and certified financial statement of the institution." The law requires an institution to establish "with the support of a financial statement audited by an independent certified public accountant in accordance with generally accepted auditing standards that the institution has sufficient resources to ensure against the precipitous closure of the institution, including the ability to meet all of its financial obligations...." The law further allows ED to require additional audits. Such an expansion of the definition of financial responsibility as is proposed in the NPRM, with potentially damaging financial penalties, should be supported overtly in the law, and section 498 of the Higher Education Act does not seem to us to do so.

We do not object to notification requirements for certain events between audit submissions, especially in the context of monitoring situations that have already identified a school as at risk, but those events, and ED's actions in response to them, need to be re-negotiated with the appropriate representatives at the table, and the assumptions made about the potential impact of those events need to be tempered by better information about the school's overall financial standing as well as regard for due process. The negotiating committee that led to this NRPM did not meet the spirit of negotiated rulemaking given the absence of the expertise that would have been provided by business and chief financial officers.

We question whether triggers should include measures that are already being used to determine or limit institutional or program eligibility under different rules and purposes – such as cohort default rates and gainful employment measures – and whether they are legitimate indicators of financial strength. Creating triggers above and beyond the existing requirements is tantamount to creating additional institutional eligibility requirements outside of those already identified by federal statute. Broad institutional eligibility requirements are the purview of Congress. We do not believe triggers that are already being used to determine other areas of institutional eligibility are appropriate reasons to obtain financial protection against imminent school closure. We also do not believe that ongoing unresolved lawsuits are a sufficient basis for the federal government to essentially seize control over a portion of an institution's assets. Due process demands that lawsuits be carried to resolution before penalties are imposed.

Proposed changes to 668.175 would specify the required amount of letters of credit based on the triggering event. The regulation is unclear as whether an institution would have to provide multiple letters of credit if more than one event is triggered or if the institution had already submitted a letter of credit for some other reason previously. ED needs to ensure that through its investigation and the imposition of cumulative financial assurances it does not contribute to an institution's financial failure. Perhaps a weighting of factors or a cumulative limit would be more reasonable than demanding multiple and cumulative letters of credit.

### **Warnings**

Warnings based on proposed requirements in the NPRM that have not been rigorously proven to demonstrate serious financial danger is destruction of reputation by insinuation, not fact. ED should allow stronger due process for financial protection penalties before requiring disclosures, to give an institution the opportunity to demonstrate that it is not in danger of closure.

### **Provisional Certification**

There appears to be a change in the applicability of the provisional certification alternative at 668.175 which is not mentioned in the preamble. It is unclear whether this is intentional or a typographical error.

The current regulation at 668.175 allows the provisional certification alternative for institutions that do not meet the general standards in 668.171(b), which encompasses several measures of financial responsibility, or due to an audit opinion or past performance; the preamble states this as well. The NPRM rule language allows the provisional certification alternative if—

- (i) The institution is not financially responsible because it does not satisfy the general standards under §668.171(b)(1), is subject to an action or triggering event under § 668.171(c), or because of an audit opinion described in §668.171(f); or
- (ii) The institution is not financially responsible because of a condition of past performance, as provided under §668.174(a), and the institution demonstrates to the Secretary that it has satisfied or resolved that condition.

Sec. 668.171(b)(1), as cross-referenced in clause (i) above, in the proposed rule just encompasses one measure, the composite score. That seems to leave out the other two conditions in (b)(2) and (b)(3) from any alternatives, as the zone alternative continues to apply only to composite score deficiencies. It is unclear whether the exclusion of the measures in

(b)(2) and (b)(3) from either alternative (zone or provisional certification) was intentional or if (b)(1) should just be (b). Section 668.175(c) would be unchanged and still cross-references 668.171(b) in its entirety, so is the intent to allow only the letter of credit alternative under 668.175(c), which has no other requirements such as restrictions on disbursement methods, for deficiencies in cash reserves and meeting financial obligations or providing administrative resources?

It also appears that the proposed substitution of cash for a letter of credit or the set-aside in paragraph (h) would not be permissible substitutes for the letter of credit alternatives in 668.175(b) or (c); is that correct? Only the provisional certification alternative in proposed paragraph (f) refers to these substitutes, as there is no letter of credit requirement in the zone alternative. However, both the preamble and paragraph (h), by cross-reference to paragraph (d), refer to the cash/set-aside substitutes as applicable to the zone alternative.

### **Repayment Rate**

ED states in the NPRM preamble that it “will look for ways to harmonize the multiple repayment rate methodologies, contingent on consumer testing and user needs.” We agree that should be done. We disagree that yet another repayment rate definition should be imposed before a single preferred and demonstrably effective methodology is determined.

### **Borrower Defenses and Misrepresentation**

We find the three areas of defenses against repayment identified in 685.222 to be generally reasonable grounds for borrower relief. We agree that ED should have the ability to invoke efficiencies such as a group claim process. We also appreciate the efforts ED made to consider and incorporate a number of tentatively agreed upon points raised during negotiated rulemaking relating to borrower defenses.

NASFAA supports a strong and enforceable regulation prohibiting misrepresentation. NASFAA and our members believe strongly that unscrupulous institutions that purposefully prey on students harm all of higher education as well as the students that are ultimately harmed by unkept promises.

However, we are deeply troubled by ED’s discussion of intent. We believe that the regulation should distinguish between deliberate deception or intentional misleading and inadvertent mistakes. While the preamble gives a reasonable explanation of how misrepresentation, including omissions, should be viewed, refusing to consider intent as a factor does not seem

reasonable when applying the regulation to LS&T procedures. We believe a distinction can be made between requiring responsibility for error by making a harmed consumer whole -- even if a false or misleading statement was unintentional or not made with the school's prior knowledge -- and imposing additional penalties on a school that shows a pattern or intent to deceive or defraud. The misrepresentation regulations would be used for multiple purposes, one that would subject the school to substantial penalties including loss of eligibility, and one that would support borrower defenses against repayment. For purposes of institutional eligibility and other substantial penalties, intent or knowledge on the part of the school should be a factor. Lack of intent to misrepresent or mislead should not, however, affect a legitimate borrower defense.

We recognize that the regulation does incorporate another test under "substantial misrepresentation," which is the reasonableness of having relied on a statement that was not accurate or complete. This caveat is especially important as more emphasis is put on misrepresentation regardless of intent. For example, a student tour guide might offer information or respond to a question with inaccurate information; that should never rise to the level of substantial misrepresentation: even with training, a student tour guide should not be considered a source of information upon which a prospective student should rely to make a decision on attendance. We would also contend that an error or oversight in a statement in one publication that is correctly and completely presented in all other publications should not be considered a preponderance of evidence. We would like ED to elaborate on reliance and reliability, and how preponderance of evidence is viewed in cases of misrepresentation.

A borrower who files a defense to repayment will experience immediate relief due to forbearance or suspension of collection. However, any interest that is not paid during forbearance is capitalized. A borrower should not be discouraged from, or unduly penalized for, mounting a defense to repayment that could involve extended investigation by having accrued interest capitalized if the defense is rejected. ED should set a limit on the interest that can be capitalized or the length of time for which accrued interest can be capitalized.

Finally, we believe that borrowers should have sufficient time to come to a decision on filing a defense to repayment under 685.222. However, we do believe that some limitation is necessary to ensure due process for schools. Schools are generally not required to keep records for more than three years, making it difficult to establish actual events (both acts and omissions) as time passes. ED's reasons for proposing a 6-year limit under certain circumstances, based on the most common state laws, seems reasonable, and the fact that ED can re-open cases under the proposed rule gives additional protection to the borrower.

Where the proposed rule does not currently have a period of limitation, we urge ED to establish one. If a borrower obtains a judgment against the school under 685.222(b), for example, a time period triggered by the date of the judgment could reasonably be established. Likewise, a breach of contract should become apparent by some definable point, after which the borrower should have a specified period to apply defense rules. It appears that the longest state rule for statutes of limitations on written contracts is 10 years, which coincidentally corresponds to the length of a standard repayment plan.

### **False Certification Discharges**

Proposed 685.215 would allow a false certification discharge of a loan if the borrower, because of a physical or mental condition, age, criminal record, or other reason accepted by the Secretary, would not meet State requirements for employment (in the student's State of residence when the loan was originated) in the occupation for which the training program supported by the loan was intended. Why is there no caveat that the institution knew or could be expected to have known about the disqualifying condition? Should a student who intentionally concealed a disqualifying condition obtain the discharge? What about a borrower whose disqualifying impairment occurs after the fact, but does not qualify for a disability discharge? In such situations, it should be clearly stated that the school should not be subject to any penalty under 685.308.

### **Conclusion**

We support ED's efforts to improve borrower defenses to repayment, and we understand that misrepresentation is a key element to that initiative. The proposed rules would benefit from some adjusting in their final development based on comments from the higher education community.

We believe any changes to financial responsibility standards require further consideration and input from experts, and should not be finalized at this time.

Sincerely,



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President & CEO, NASFAA