Proposed Borrower Defense Rules May Significantly Impact Higher Education Institutions

Insights
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The US Department of Education (ED) recently released a significant Notice of Proposed Rulemaking which could impact most institutions of higher education. In a nutshell, the proposed regulations are designed to provide student borrowers with new ways to assert defenses to repaying student loans and, perhaps more significantly, to allow ED to seek reimbursement from schools for such claims brought by students.

The proposed rules, which can be found here, are designed to govern the Borrower Defense to Repayment (BDTR) provision of the Higher Education Act. It is important to note that these proposed rules almost universally apply to all institutions participating in the Direct Loan program, including public and nonprofit institutions, and would generally apply to all Direct Loans originated after July 1, 2017.

Revised Law Would Create New Kinds Of Claims
The Higher Education Act currently provides that:

Notwithstanding any other provision of State or Federal law, the 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, except that in no event may a borrower recover from the Secretary, in any action arising from or relating to a loan made under this part, an amount in excess of the amount such borrower has repaid on such loan.

The proposed rules identify three broad "acts or omissions" upon which students could base a BDTR claim, all of which are subject to a mere preponderance of the evidence standard:

- a favorable decision for the student in a state or federal court case involving the loan, or the educational services for which the loan was made;
- breach of contract (generally the enrollment agreement, either in its express terms or implied) by the school; or
- a "substantial misrepresentation" by the school about the nature of the educational program, the nature of the financial charges, or the employability of graduates.

Regarding the latter in particular, ED's definition of "substantial misrepresentation" is exceptionally broad. For instance, it does not require an intentional institutional deception, but merely requires a borrower to establish that the representation was "misleading under the circumstances." The proposed rule also adds that "substantial misrepresentation" includes any statement made by a representative of an institution that omits information in such a way as to make the statement false, erroneous, or misleading.

Significant Impact Expected

Perhaps most significantly, the proposed rules provide a structure for ED to recoup its losses directly from the student's former institution. More specifically, ED would have the authority to "initiate a proceeding" to seek repayment from the school for any loan amounts forgiven. No details have yet been provided for how that "proceeding" will unfold.

In the event ED provides relief to a group of former students, there is no separate proceeding. Instead, ED initiates a "fact-finding process" after the formation of the group claim. If ED determines a group discharge is warranted, it will automatically assign liability to the institution.

This is a significant piece of rulemaking with which all higher education institutions should familiarize themselves. The deadline to file comments on these proposed rules is August 1, 2016, after which they are expected to be finalized by late 2016 or early 2017.

If you have any questions about these proposed regulations or how they may affect your institution, please feel free to contact any member of the Fisher Phillips Higher Education Practice Group.

This Legal Alert provides an overview of specific proposed regulations. It is not intended to be, and should not be construed as, legal advice for any particular fact situation.

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