**Issue Paper 1**

**Session 2: January 8-11, 2018**

**Issue:** Whether to establish a Federal standard for the purpose of determining if a borrower can establish a defense to the repayment of a Direct Loan or recover for amounts already paid on a Direct Loan based on an act or omission of an institution.

**Statutory cite:** §455(h) of the Higher Education Act of 1965, as amended

**Regulatory cite:** 34 CFR685.206(c), 685.222, 685.300, 685.308

**Summary of changes:** Creates a regulatory section that establishes, for loans first disbursed on or after July 1, 2019, a new Federal standard applicable to borrower defense claims made by borrowers and for Department recovery actions against institutions. Under the proposed regulations, borrowers with an eligible Direct Loan would be entitled to a discharge (or recover amounts already paid) of all or a portion of the loan if the borrower establishes either: (1) an institutional misrepresentation, (2) a court judgment against an institution, or (3) a final judgment from an arbitrator against an institution. The proposed regulations would also describe in detail how a borrower establishes the basis for a claim.

**Changes:** See regulatory text below.

*[Note to negotiators: §685.222 is a new section. For ease of readability and editing during negotiated rulemaking, the section is formatted as plain text, rather than redline.]*

**§685.222 Borrower defense and Department recovery actions against institutions**

(a) *Introduction*.

(1) For the purposes of this section and § 685.206(c), a “borrower defense” refers to an act or omission of an institution at which the borrower enrolled that relates to the making of a Direct Loan for enrollment at the institution or the provision of educational services for which the loan was made, and includes one or both of the following:

(i) A defense to the repayment of amounts owed to the Secretary on a Direct Loan, in whole or in part; and

(ii) A right to recover amounts previously collected by the Secretary on the Direct Loan, in whole or in part.

(2) A borrower may assert a borrower defense of a Direct Consolidation Loan that repaid a Direct Loan, FFEL Program Loan, Federal Perkins Loan, Health Professions Student Loan, or Loan for Disadvantaged Students under subpart II of part A of title VII of the Public Health Service Act; or a Health Education Assistance Loan, or Nursing Loan made under part E of the Public Health Service Act on which the borrower had a basis for a borrower defense claim prior to the consolidation.

(3) For loans first disbursed prior to July 1, 2019, the borrower may assert a borrower defense of a Direct Loan consistent with section 685.206(c).

(4) For loans first disbursed on or after July 1, 2019, the borrower may assert a borrower defense of a Direct Loan consistent with this section.

(5) The Department may initiate a recovery action against an institution consistent with paragraph (c) of this section.

(6) The Department administers this section consistent with the procedures described in section 685.206(c) and 34 CFR Part 668, Subpart G.

(b) *Borrower defense*.

(1) For loans first disbursed on or after July 1, 2019, the Secretary will discharge the borrower’s obligation to repay a Direct Loan and will refund amounts paid on the loan, in whole or in part, less any amounts already refunded to the borrower from any source pursuant to section 685.206(d)(8), if the borrower establishes a defense by clear and convincing evidence that--

(i) The institution at which the borrower enrolled acted with an intent to deceive, knowledge of the falsity of a misrepresentation, or a reckless disregard for the truth in making a misrepresentation of material fact, opinion, intention, or law upon which the borrower reasonably relied in deciding to obtain a Direct Loan to enroll or continue enrollment in a program at the institution, and which resulted in financial harm to the borrower;

(ii) The borrower has obtained, from a court of competent jurisdiction, a nondefault contested State or Federal judgment and was awarded monetary damages against the institution relating to the loan or the provision of educational services for which the loan was obtained; or

(iii) The borrower has obtained, from an arbitrator or a hearing official in a State or Federal administrative tribunal agreed to by the borrower and the institution, a nondefault contested judgment, or equivalent final determination, and was awarded monetary damages against the institution relating to the loan or the provision of educational services for which the loan was obtained.

(2) For the purposes of this section—

(i) A misrepresentation is a statement, act, or omission by an institution that would mislead a reasonable person regarding the nature of the educational program, the nature of financial charges, the employability of graduates of an educational program, the eligibility of the educational program for licensure or certification, the State agency authorization or approval of the educational program, or an accreditor approval of an institution or educational program. Evidence that a misrepresentation described in paragraph (b)(1)(i) of this section has occurred includes, but is not limited to:

(A) Actual licensure passage rates materially different from those included in the institution’s marketing materials, website, or other communication made to the student;

(B) Actual job placement rates materially different from those included in the institution’s marketing materials, website, or other communication made to the student;

(C) The inclusion in the institution’s marketing materials, website, or other communication made to the student of specialized, programmatic, or institutional certifications or approvals not actually obtained or the failure to remove within a reasonable period of time such certifications or approvals from marketing materials, website, or other communication when invalidated or withdrawn;

(D) The inclusion in the institution’s marketing materials, website, or other communication made to the student of representations regarding the widespread or general transferability of credits that are only transferrable to limited types of programs or institutions or the transferability of credits to a specific program or institution when no reciprocal agreement exists with another institution or such agreement is materially different than what was represented;

(E) A representation regarding the employability or specific earnings of graduates without an agreement between the institution and another entity for such employment or sufficient evidence of past employment or earnings to justify such a representation;

(F) A representation regarding the availability, amount, or nature of any financial assistance available to students from the institution or any other entity to pay the costs of attendance at the institution that is not fulfilled following the enrollment of the borrower;

(G) A representation regarding the amount of tuition and fees that the student would be charged for the program that is materially different in amount, method, or timing of payment from the actual tuition and fees charged to the student;

(H) A representation that the institution, its courses, or programs are endorsed by vocational counselors, high schools, colleges, educational organizations, employment agencies, members of a particular industry, students, former students, or governmental officials when no such endorsements exist as stated;

(I) A representation regarding the institution’s size, location, facilities, training equipment or the number, availability, or qualifications of its personnel that are materially different from the institution’s actual circumstances at the time the representation is made;

(J) The nature or extent of prerequisites for enrollment in a course or program; or

(K) Any other circumstances as determined by the Secretary.

(ii) A violation by the institution of a requirement of the Higher Education Act or the Department’s regulations is not a basis for a borrower defense claim unless the violation would otherwise give rise to a successful borrower defense claim under this section or section 685.206(c), as applicable. The Secretary will not approve a borrower defense claim under this section or section 685.206(c) of this Part when the borrower submits a claim based on—

(A) Personal injury;

(B) Sexual harassment;

(C) A violation of civil rights;

(D) Slander or defamation;

(E) Property damage claims;

(F) Educational malpractice, which is a tortious claim about the general quality of the student’s education or the reasonableness of an educator’s conduct in providing educational services; or

(G) Academic disputes and disciplinary matters.

(iii) Financial harm to the borrower has occurred when the borrower suffers monetary loss as a consequence of a misrepresentation described in paragraph (b)(1)(i) of this section or as found by a court, arbitrator, or hearing official pursuant to a judgment as described in paragraphs (b)(1)(ii) and (b)(1)(iii). Financial harm does not include damages for nonmonetary loss such as inconvenience, aggravation, emotional distress, pain and suffering, punitive damages, or opportunity costs. Financial harm is such monetary loss that is not predominantly due to intervening local, regional, or national economic or labor market conditions. Evidence of financial harm includes, but is not limited to the following circumstances:

(A) A significant difference between the borrower’s earnings after completing the program and the earnings listed for the borrower’s program of study in the institution’s marketing materials, website, or other communication made to the student;

(B) A significant difference between the borrower’s earnings after completing the program and the earnings for similar borrowers employed in the program’s intended occupational field, determined by, for example, earnings below the lowest income quintile for the program of study’s intended occupational field according to the Standard Occupational Classification (SOC) code as published by the U.S. Bureau of Labor Statistics;

(C) Lower or lost wages, extended periods of involuntary unemployment, or the cost of obtaining nontransferable credits;

(D) A significant difference in the amount or nature of the tuition and fees charged by the institution for which the Direct Loan was disbursed and the amount or nature of the tuition and fees the borrower reasonably believed the institution would charge or was charging;

(E) The borrower’s inability to secure employment in the field of study for which the institution expressly guaranteed employment; or

(F) The borrower’s inability to complete the program because the institution no longer offers a requirement necessary for completion of the program in which the borrower enrolled.

(3) The Secretary may determine at any time that a borrower defense claim should not be approved based on evidence that rebuts the borrower’s claim, including any evidence provided by the institution at which the borrower enrolled. Such evidence may include, but is not limited to--

(i) For a claim based on licensure exam passage rates, the institution or program has a licensure exam passage rate associated with the program in which the borrower enrolls that, at a minimum, reasonably approximates the passage rates included in the institution’s marketing materials, website, or other communication made when recruiting the student;

(ii) For a claim based on the inability of the borrower to obtain the necessary certification or licensure for employment in the program’s intended field of employment, the borrower has obtained a certification or licensure related to the program in which the borrower enrolled without needing to complete additional coursework after completing the program;

(iii) The institution provided information to the borrower to correct the misrepresentation prior to the borrower enrolling in the program; or

(iv) The institution demonstrated that its representative or agent made a misrepresentation that was inconsistent with or prohibited by the institution’s policies, procedures and training at the time it was made.

(4) For purposes of this section, the term “institution” includes an eligible institution, its representatives and agents, or any 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.

(c) *Department recovery actions against institutions*. The Secretary may initiate a recovery action against an institution when the Secretary determines that the borrower has asserted a successful borrower defense against the institution as described in this section or section 685.206(c) of this Part.

(d) *Limitations period*. A borrower must file a claim under paragraph (b)(1) of this section within three years of the date the borrower discovered, or reasonably should have discovered, the misrepresentation.

**§685.300 Agreements between an eligible school and the Secretary for participation in the Direct Loan Program.**

(a) *General*. Participation of a school in the Direct Loan Program means that eligible students at the school may receive Direct Loans. To participate in the Direct Loan Program, a school must—

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(8) Accept responsibility and financial liability stemming from its failure to perform its functions pursuant to the agreement;

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(11) Accept responsibility and financial liability stemming from losses incurred by the Secretary for repayment of amounts discharged by the Secretary pursuant to sections 685.206, 685.214, 685.216, and 685.222;

**§685.308 Remedial actions.**

(a) *General*. The Secretary may require the repayment of funds and the purchase of loans by the school if the Secretary determines that the school is liable as a result of-- --

(1) The school's violation of a Federal statute or regulation;

(2) The school's negligent or willful false certification under section 685.215; or

(3) The school’s actions that gave rise to a successful claim for which the Secretary discharged a loan, in whole or in part, pursuant to sections 685.206, 685.214, 685.216, and 685.222.