THE CENTURY FOUNDATION | 1919 2019

COMMENTARY EDUCATION

New Data Supports Rejection of DeVos Arbitration Regulations

NOVEMBER 09, 2018

In 2016, the Department of Education banned colleges' use of forced arbitration for students taking out federal loans. Under the ban, colleges that wanted to receive federal aid could not deny their students the option of taking them to court for allegations such as fraud and deception. (The inclusion of forced arbitration clauses in student enrollment agreements is a common practice at for-profit colleges.) Secretary of Education Betsy DeVos is trying to reverse that ban. But new arbitration records, published by a large chain of for-profit colleges, the Education Corporation of America (ECA), reveals why DeVos's action is wrongheaded.

The Education Corporation of America faces a long list of problems. Under the Department of Education's 2014 gainful employment rules, a number of ECA schools had to improve student outcomes, or risk losing access to federal aid, including Pell grant and Direct Loan dollars. Then, in 2016, the Department of Education derecognized ECA's long-time accreditor, ACICS, which meant that ECA's federal funding would be jeopardized if it failed to gain approval by another accreditor.[1] Luckily for ECA, it seems to have a savior in Betsy Devos regarding both these troubles: she is seeking to scrap the gainful employment rules, and revived ACICS earlier this year.

But ECA's troubles remain. After seeing the company's 2016 financial statements, the Department of Education threw down a yellow flag and required the company to meet more stringent financial requirements, including making student aid disbursements under heightened cash monitoring (requiring the school to pay students upfront and then get reimbursed), in order to retain eligibility to receive federal financial aid dollars. ACICS recently raised questions about ECA's financial troubles. ECA announced in September that it would close twenty-six campuses by 2020. And the chain says it cannot afford to repay all the claims that it may owe to creditors, landlords, and students.

Lawsuit Related to Financial Troubles Reveals New Data

Last month, in what seems to be a Hail Mary attempt to save itself, the school filed for receivership, a legal cousin of a bankruptcy proceeding (which the Higher Education Act makes clear would end access to federal student aid dollars). ECA's lawsuit failed, with a federal judge dismissing the case this week. But in the course of making its case to halt creditors and others from pursuing claims, and to demonstrate the precariousness of its financial position, the company attached Exhibit 5: a detailed list of court actions and arbitration proceedings against ECA between 2010 and 2018. From at least 2010, ECA schools such as Virginia College have used enrollment agreements to force students to waive their legal rights in favor of forced arbitration.[2] Exhibit 5 gives the public a rare glimpse into the nature of student allegations, including arbitration actions, against ECA.[3] An analysis of these records tells us:

- Of the 107 legal actions, 49 actions were from current or former students (some actions included several students).

- A whopping 36 of the 49 actions[4] from students involved allegations of breach of contract, fraud, deceit, misrepresentation, false advertising, unjust enrichment, breach of duty—the kinds of allegations that lead to students invoking a "borrower defense" in arguing that they should not have to repay their student loans. (In the course of litigation, these student complaints could unearth whether there existed a pattern of deceptive practices that should trigger action by regulators.)

- Of those 36 student actions that map onto borrower defense relief, half were initiated as court cases, and subsequently forced into arbitration settings by ECA's lawyers. In other words, while Devos has tried to frame arbitration as "pro-student" (providing the "opportunity" for students to seek redress directly from institutions), the reality is that half of the aggrieved students chose another path. Either these student plaintiffs did not know they were required to go straight into arbitration, or they deliberately tried to avoid the process by filing a civil action first instead. And the number of students trying to avoid arbitration is likely higher, given that some of the cases listed as arbitration proceedings have a history in the courts not included in Exhibit 5.

Exhibit 5 provides us with a window into attempts by students to push back on deceptive practices. We don't know how they fared in arbitration, although evidence shows that these proceedings often unfairly favor schools. But we do know that, had at least some of those cases been publicly litigated, the Department of Education and state agencies would have had more information at their disposal that may have triggered intervention to end any bad practices years ago—protecting students and also saving taxpayers' money.

Protecting Students, but also Taxpayers

When a school goes broke, the Department of Education, and the taxpayers who support it, are left to cover the costs of student loan discharges resulting from deceptive practices or school closings. The Department of Education must and should discharge student loans for any students who were defrauded by ECA and for any students attending ECA campuses right now if they close; as of March 2018, there were at least 98 borrower defense claims pending at the Department. But while ECA should bear the costs of those loan cancellations, their court filings imply a financial situation that may leave limited cash to pay back the Department for discharges.

Had at least some of those cases been publically litigated, the Department of Education and state agencies would have had more information at their disposal that may have triggered intervention to end any bad practices years ago.

Taxpayer protection was precisely the rationale behind the Obama administration's 2016 arbitration ban: specifically, the Department of Education was interested in "preventing the institutions empowered to arrange Direct Loans for their students from insulating themselves from direct and effective accountability for their misconduct, from deterring publicity that would prompt government oversight agencies to react, and from shifting the risk of loss for that misconduct to the taxpayer." A well-publicized lawsuit, the Department of Education stated, "is more likely to attract the attention and risk of compensatory or

prophylactic enforcement action by this Department and other government agencies." Such enforcement action would help end bad behavior and the waste of taxpayer dollars, such as the thousands of fraud-based borrower defense claims incurred following the 2015 collapse of Corinthian Colleges.

The good news is that, under a court ruling that took effect October 16, 2018, students won the right to sue around student loan issues at any school that accepts federal student aid dollars, including Virginia College and other ECA subsidiaries. The court found that the Devos Department of Education illegally delayed the Obama administration's 2016 borrower defense regulations banning the use of forced arbitration, and thus the arbitration ban is now in effect: students who say they were defrauded by schools like Virginia College can now have their day in court. But the Department is still writing a new regulation to block students from court in the future. Exhibit 5 shows why the Devos deregulation machine, now delayed in its efforts until at least 2020, should reverse its proposal when it releases its final rule and retain the ban permanently.

EDUCATION SECRETARY BETSY DEVOS TESTIFIES DURING A SENATE APPROPRIATIONS SUBCOMMITTEE HEARING ON CAPITOL HILL, JUNE 5, 2018 IN WASHINGTON, DC.(PHOTO BY MARK WILSON/GETTY IMAGES)

Notes

1. An accreditation body, ACCET, found that ECA systematically failed to meet completion and job placement benchments and "failed to demonstrate positive student outcomes to validate the vast majority of its training programs at the vast majority of campuses." At some Virginia College campuses, job placement rates are as low as 16 and 30 percent.
2. A 2016 update to ECA's enrollment agreement further restricted students' legal rights—preventing them from joining together in class action proceedings.
3. The complaint states they will provide a list of open cases, but Exhibit 5 provides both open and closed cases. ECA later amended its filing to just include the nineteen open cases.
4. Additional cases may have involved those allegations but ECA leaves the allegations column blank.

Yan Cao, Fellow

Yan Cao is a fellow at The Century Foundation where she works on higher education policy with a focus on expanding opportunity, reducing inequality, and ensuring fair outcomes for students.

Jen Mishory, Senior Fellow

Jen Mishory is a senior fellow at The Century Foundation, working on issues related to workforce, higher education, and health care, and a senior policy advisor. Prior to joining TCF, Jen co-founded and served as the Executive Director of Young Invincibles, which has grown to become the largest advocacy organization in the country representing young Americans.