

## Court allows Dept. of Education “borrower defense” final rule to take effect

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Thursday, October 18, 2018

The “borrower defense” final rule (Final Rule) issued by the Dept. of Education in November 2016 took effect at noon yesterday after Judge Randolph D. Moss of the D.C. federal district court [refused to grant the renewed motion for a preliminary injunction](#) filed by the California Association of Private Postsecondary Schools (CAPPS) seeking to preliminarily enjoin the arbitration ban and class action waiver provisions in the Final Rule. CAPPS had sought to block the provisions from taking effect pending the resolution of the lawsuit filed by CAPPS against the ED and Education Secretary Betsy DeVos to overturn the Final Rule. Judge Moss found that CAPPS had failed to show that any of its members was likely to suffer an irreparable injury in the absence of an injunction.

Shortly before the Final Rule’s initial July 1, 2017 effective date, CAPPS filed a motion for a preliminary injunction to which the ED responded by issuing a stay of the Final Rule under Section 705 of the Administrative Procedure Act (APA). The Section 705 stay was followed by the ED’s issuance of an interim final rule delaying the effective date until July 1, 2018 and the promulgation of a final rule further delaying the effective date until July 1, 2019 (Final Rule Delay).

On September 12, 2018, Judge Moss issued an opinion and order in *Bauer v. DeVos*, another case challenging the Final Rule in which he ruled that the ED’s rationale for issuing the Section 705 stay was arbitrary and capricious and that in issuing the Final Rule Delay, the ED had improperly invoked the good cause exception to the Higher Education Act’s negotiated rulemaking requirement. The case consolidated two separate lawsuits filed after the ED’s issuance of the Section 705 stay, with one filed by two individual plaintiffs and the other by a coalition of nineteen states and the District of Columbia. Both lawsuits were subsequently amended to challenge not only the Section 705 stay but also the other actions taken by the ED to delay the Final Rule’s effective date. While Judge Moss vacated the Section 705 stay, he stayed the vacatur until 5 p.m. on October 12, 2018.

After the ED filed a notice with the court in June 2017 regarding its initial delay of the Final Rule’s effective date until July 1, 2018, CAPPS withdrew its motion for preliminary injunction. Following the court’s decision in *Bauer*, CAPPS [filed its renewed motion for a preliminary injunction](#). In his decision denying CAPPS’ motion, Judge Moss stated that on October 12, the court extended the stay of the vacatur until noon on October 16.

The Final Rule broadly addresses the ability of a student to assert a school’s misconduct as a defense to repayment of a federal student loan. It does not apply to private loans. The Final Rule includes a ban on all pre-dispute arbitration agreements for borrower defense claims by schools receiving Title IV assistance under the Higher Education Act (HEA) and a new federal standard for evaluating borrower defenses to repayment of Direct Loans (i.e. federal student loans made by the ED). Both mandatory and voluntary pre-dispute arbitration agreements are prohibited by the rule, whether or not they contain opt-out clauses, and schools are prohibited from relying on any pre-dispute arbitration or other agreement to block a borrower from asserting a borrower defense claim in a class action lawsuit until the court has denied class certification and the time for any interlocutory review has elapsed or the review has been resolved. The prohibition applies retroactively to pre-dispute arbitration or other agreements addressing class actions entered into before July 1, 2017.

It would seem that because the Final Rule is now effective, the new federal standard it establishes for evaluating defenses to repayment would be applicable in actions seeking to collect on Direct Loans disbursed on or after

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July 1, 2017 or to recover amounts previously collected on such loans. However, because the arbitration ban and class action provisions of the Final Rule are requirements with which a school must comply as a condition of receiving Title IV assistance, the ED presumably could waive such requirements (as well as other provisions subject to ED enforcement such as the actions and events in the Final Rule that can trigger a requirement for a school to provide a letter of credit or other financial protection to the ED to insure against future borrower defense claims and other liabilities to the ED.)

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