Supplemental Testimony of Robyn Smith,
Legal Aid Foundation of Los Angeles and National Consumer Law Center,
Before the U.S. House of Representatives Subcommittee on
Higher Education and Workforce Investment
regarding
"Protecting Students and Taxpayers: Improving the Closed School Discharge Process"
October 21, 2021

Introduction

Chairman Scott, Chairwoman Wilson, Ranking Member Murphy and Members of the Committee, thank you for inviting me to answer two additional questions regarding closed school discharges. I offer my supplemental testimony on behalf of the low-income clients of the Legal Aid Foundation of Los Angeles (LAFLA) and the National Consumer Law Center (NCLC). For more information about LAFLA, NCLC, and my background, please refer to the testimony I submitted on September 30, 2021.

Question 1: Recently, the Department extended the look-back period for students that attended ITT Technical Institute, which officially closed in September 2016. While the look-back period for that closure was originally May 2016, the Secretary under his discretion extended the closed school discharge window to March 31, 2008 based on a review of external evidence form the bankruptcy court proceedings for ITT. This evidence demonstrated that March 2008 was when the company's executives publicly disclosed the start of a financial scheme that kicked off a series of misrepresentations to hide the true nature of the school's finances. Similar stories exist about other for-profit institutions that have abruptly shuttered. Given this, do you think there should be changes in how the Secretary uses that discretionary authority to extend the look-back period?

Legal services organizations have long witnessed the long decline in the quality of education provided by schools prior to sudden closures. We see many students who withdraw more than 6 months before a closure because it has cut essential instructional services to stay afloat financially. In these cases, institutions often stop investing in necessary instructional equipment, materials and facilities, stop paying instructor wages, refuse to replace instructors who have departed, and discontinue programs before students have completed them.

These schools also engage in misconduct designed to keep them in business and reduce liability for closed school discharges to the Department of Education (the Department).[1] They often conceal their financial precarity by refusing to pay living "stipends" from Title IV funds to students, while reporting that those funds have been paid;[2] reporting that students have completed their educations, when in fact they have not; concealing that students have withdrawn in order to keep Title IV funds that should be refunded; pressuring recruiters to deceptively increase student enrollments and revenues; and failing to report students who are on leaves of absence when the school closes. As the GAO has plainly stated: "research has indicated that a school's financial struggles can have negative effects on its operations."[3]

The Department promulgated the "exceptional circumstances" regulation to ensure that closed school discharge relief is available to students who, due to such practices, withdraw more than 120 or 180 days prior to the school closure.[4] The regulations do not define extenuating circumstances, but provide examples of the type of conduct or events that cause or indicate significant deterioration in educational services prior to closure, such as loss of accreditation or the discontinuance of a majority of a school's programs.[5] These examples are explicitly non-exhaustive.[6]

Unfortunately, the Department has rarely used this discretion. The Department's failure to extend the look-back period means that many students who withdraw due to school misconduct remain on the

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[1] The HEA requires the Department to "pursue any claim available to any [borrower who has been granted a closed school discharge] against the institution and its affiliates and principals . . . .).). 20 U.S.C. § 1087(c).
[2] For example, before it closed, Argosy University kept over $13 million in Title IV living stipends intended for students, and spent it on payroll and other overhead expenses while altering financial records so that it would appear that the stipends had been paid to students. Michael Vasquez & Dan Bauman, *How America's College Closure Crisis Leaves Families Devastated*, CHRON. OF HIGHER EDUC. (April 4, 2019).
[3] U.S. Gov't Accountability Off., GAO-17-555, Higher Education: Education Should Address Oversight and Communication Gaps in its Monitoring of the Financial Conditions at Schools 28 (2017) ("For example, two studies that we reviewed found that financial shortfalls can cause schools to reduce course offerings and increase class sizes. Two other studies have also found that declines in schools' resources per student can result in reduced student supports and lower rates of graduation.") (citations omitted).
[4] *See* 34 C.F.R. §§ 682.402(d)(1)(i) (FFEL Loans); 685.214(c)(1)(i)(B), (c)(2)(i)(B) (Direct Loans); 674.33(g)(4)(i)(B) (Perkins Loans).
[5] 34 C.F.R. § 685.214(c)(1)(i)(B) (Direct Loans for schools that closed prior to July 1, 2020).
[6] 34 C.F.R. §§ 682.402(d)(1)(i) (FFEL Program Loans); 685.214(c)(1)(i)(B), (c)(2)(i)(B) (Direct Loans); 674.33(g)(4)(i)(B) (Perkins Loans).

hook for repayment of their federal loans. Students, for example, may withdraw because they cannot afford expenses necessary to stay in school after the school has withheld the portion of their federal financial aid available for living expenses (often referred to as "living stipends"). They may also withdraw because classes get cancelled, instructors fail to show up for class, computers and instructional equipment break down, or small classes are merged into large and unmanageable classes involving students at multiple levels of their programs.

Recently, we were encouraged to see the Department extended the ITT Tech closed school look-back period to March 31, 2008, providing much needed relief to borrowers who withdrew during this period because:

> the institution engaged in widespread misrepresentations about the true state of its financial health and misled students into taking out unaffordable private loans that were allegedly portrayed as grant aid. ITT's malfeasance drove its financial resources away from educating students in order to keep the school in business for years longer than it likely would otherwise have, resulting in debts that are being discharged starting today.[7]

In order to ensure that the Department provides relief to these harmed students more often, it should incorporate a presumption into the exceptional-circumstances regulation. This presumption should expand the look-back eligibility period to the date of the types of events specified in the regulation, unless the Department publishes a written finding, based on clear and convincing evidence, that the school did not reduce instructional expenses or student services, misrepresent its financial health to students, shareholders, or any government agency, or engage in substantial misrepresentations[8] from that date.

The Department should apply this presumption in the future and retroactively. It should review all schools that have closed without an orderly and pre-planned process, to determine whether this presumption should apply to them as well. The following are examples of criteria that should trigger the presumption for an extension of the eligibility look-back period to the date indicated:

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[7] U.S. Dep't of Educ., Press Release, *Extended Closed School Discharge Will Provide 115K Borrowers from ITT Technical Institute More Than $1.1B in Loan Forgiveness* (Aug. 26, 2021), *available at* https://www.ed.gov/news/press-releases/extended-closed-school-discharge-will-provide-115k-borrowers-itt-technical-institute-more-11b-loan-forgiveness.

[8] 34 C.F.R. Part 668, Subpart F.

- If a school discontinued 50% or more of its programs during a 12-month period, the date on which the number of discontinued programs reached 50%.
- The date that the Department put a school on heightened cash-monitoring (HCM) status, if the school was not subsequently restored to full eligibility without monitoring prior to closure. The Department has done this before, including by extending the closed school pre-withdrawal eligibility period for Corinthian Colleges students back to June 20, 2014, the date upon which it placed Corinthian's schools on HCM status.[9] The Department should do the same for the schools owned by Education Corporation of America (ECA), which was placed on HCM status in March 2015 and closed in December 2018.[10]
- The date that an institutional accrediting agency revoked accreditation, put the school on probation, issued an order to show cause, or took other adverse public action which was not lifted prior to the school's closure. This includes Charlotte Law School, whose accreditor, the American Bar Association, placed it on probation on February 3, 2016, and which subsequently closed on August 10, 2017.[11]
- In the event a state or federal government agency has issued an order or obtained an adverse court judgment against the school for federal or state law violations that requires the payment of penalties, fines, restitution, or other moneys, and the payments have adversely impacted the school's finances, the date on which the first federal or state violations upon which the order or judgment is based occurred. This includes the Art Institutes, Argosy University, South University, and Brown-Mackie Colleges, which were owned by Education Management Corporation (EDMC). On November 16, 2015, a federal court entered a Consent Judgment ordering EDMC to pay $95.5 million to ED and several states for its

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[9] *See* U.S. Dep't of Educ., Press Release, *U.S. Department of Education Heightens Oversight of Corinthian Colleges* (June 19, 2014), Kelly Field, *Plan to Forgive Corinthian Students' Loans Gives Hope to Other Borrowers*, CHRON. OF HIGHER EDUC. (July , 2015).
[10] Alex Elson, *Justice at Last*, Nat'l Student Loan Defense Network, 4-6 (Oct. 2020) (citations omitted), *available at* https://www.defendstudents.org/news/body/docket/100-Day-Docket-Expanding-Debt-Relief.pdf/.
[11] *Id*. at 3 (citations omitted).

illegal scheme to pay incentive compensation to recruiters based on the number of students they enrolled.[12] This judgment was the beginning of the end for these schools. It led to the closure of 22 Brown-Mackie campuses in June 2106, and the sale of most other campuses to the Dream Center Foundation. Most of these campuses closed in December 2018 and March 2019.[13]

- When the Department denies a school's application seeking to renew Title IV eligibility (re-certification) or revokes a school's Title IV eligibility, the earliest date of the school's violations underlying these decisions. This includes Medtech College, which closed immediately after the Department denied its application for recertification on July 26, 2016. The Department's denial was based on substantial misconduct that occurred 2014 (and possibly earlier).[14]

Each of the described circumstances clearly implicates a degradation in educational value long preceding the closure date. Government agency findings of legal violations necessarily relate to conduct that predated the findings themselves by months or even years. A school's decision to discontinue the majority of its programs obviously calls into question the quality of those that remain. These and the remaining above-described circumstances should trigger a presumption extending the look-back period for closed school discharge eligibility.

Question 2: As we heard from the GAO testimony, closed school discharges have cost taxpayers more than $1 billion. What recommendations do you have for the Department and Federal Student Aid to better recoup funds to make student borrowers and taxpayers whole?

Congress entrusted the Department and Federal Student Aid (FSA) with the authority[15] needed to serve as a responsible steward of the Title IV program. Yet, the Department has failed to build an internal

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[12] *Id*. at 4 (citations omitted).
[13] *Id*. (citations omitted).
[14] *Id*. at 6-7 (the evidence underlying the Department's denial of Medtech College's application are not publicly available, and may pre-date 2014) (citations omitted).
[15] While the Department has policy making authority, FSA is tasked with implementing the regulations. 20 U.S.C.A. § 1018(b)(2)(A)(vi). Thus, for the response to Question 2, the "Department" refers to FSA and the Department collectively.

enforcement or investigatory capacity commensurate with the responsibility Congress provided. As a result, irresponsible and poor performing schools continue to receive federal aid while obscuring their financial instability and hiding the use of predatory practices that increase litigation and enforcement liability.

Even when the Department knows a school is in trouble and at risk of closing, it has routinely failed to use the mitigation tools it has within its arsenal to protect students and taxpayers. In the past, when the Department has become aware that a school is becoming an increasingly risky investment – due to financial instability, a change in ownership, or the discovery of predatory conduct, among many other reasons – it has typically allowed the school to continue enrolling new students and receive federal aid with little limitation.[16] As a result, schools can spend unlimited time in Heightened Cash Monitoring status – a strong tool the Department has to closely monitor schools that are considered financially unstable – with little or no impact on their ability to recruit students, often using predatory means to do so.[17] The failure to aggressively intervene when a school shows signs of trouble increases the volume of wasted tax dollars as well as the number of borrowers who are harmed.

To protect taxpayer dollars and student borrowers from the consequences of sudden school closures, the Department must make better use of the enforcement authority it already has. It should take swift action to minimize harm, improve how it assesses financial responsibility and risk, require sufficient

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[16] For example, despite violating financial responsibility regulations from 2006 on, Education Management Corporation's schools (Art Institutes, Argosy, South University and others) were allowed to continue receiving federal funding. U.S. Dep't of Educ., Office of Inspector General, *Inspection of the Department's Activities Surrounding the Sale of Postsecondary Schools to Dream Center Education Holdings,* No. I05T0010 at 3 (June 29, 2021), *available at* https://www2.ed.gov/about/offices/list/oig/auditreports/fy2021/i05t0010.pdf. The schools were still permitted to receive federal funds even after entering into a settlement with the Dept. of Justice and 40 state attorneys general that resolved allegations that the schools were utilizing predatory and deceptive recruitment practices. *See* U.S. Dep't of Just., Press Release, *For-Profit College Company to Pay $95.5 Million to Settle Claims of Illegal Recruiting, Consumer Fraud and Other Violations* (Nov. 16, 2015), *available at* https://www.justice.gov/opa/pr/profit-college-company-pay-955-million-settle-claims-illegal-recruiting-consumer-fraud-and.

[17] For example, Walden University has remained on Heightened Cash Monitoring since 2015 due to repeated financial responsibility failures of its parent company, Laureate. *See* U.S. Dep't of Educ., Heightened Cash Monitoring, https://studentaid.gov/data-center/school/hcm. Daymar College has continued to receive federal funding even after it settled a case with the Kentucky attorney general which resolved allegations that the school engaged in predatory recruitment practices. *See* Complaint, Case No. 11-CI-01016 (Jul 27, 2011) https://ag.ky.gov/pdf_news/daymar-complaint.pdf.

financial guarantees from at-risk institutions, and act to recover funds from school investors and executives via bankruptcy, civil litigation, and criminal litigation quickly after a school closes. To save taxpayer dollars and protect borrowers, the system needs wholesale improvement.

A. The Department should strengthen its oversight and take swift action to ensure that schools are following statutory and regulatory safeguards that are designed to protect against school closures.

Mitigating the damage a closing school causes is best accomplished by ensuring that only high quality, financially stable schools are allowed to receive federal aid in the first place. Congress entrusted the Department with the power to determine when a school fails to be a sound investment for taxpayer dollars and borrowers. Accordingly, it has the responsibility to determine which institutions "qualify" for participation in Title IV programs[18] and may certify that institutions are eligible to receive Direct Loan funding only when, among other things, the institution demonstrates sufficient "financial responsibility,"[19] has not had "severe performance deficiencies,"[20] has no outstanding debts owed to the Department,[21] and demonstrates sufficient "administrative capacities."[22] Each of the these criteria may be used to assess whether or not a school is at risk of closing. In addition, because Congress expected the Department to be a responsible steward of federal funds, Congress gave it the discretion to establish other criteria needed "to protect the financial interest of the United States" and promote the purpose of the Higher Education Act (HEA).[23] Thus, the Department has the discretion to use other methods to identify institutions that may adapt their business practices to avoid detection by the aforementioned criteria.

The Department should implement a number of changes to better identify schools at risk of sudden closures and mitigate the harm to taxpayers and students. First, the Department should increase staff and resources available to focus on the investigation of schools that are failing any of these criteria. Currently, the Department typically performs largely paper-based program reviews of all Title IV schools, which

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[18] 20 U.S.C. §§ 1002(a)(5), 1099c(a);
[19] *Id*. at § 1099c(c).
[20] *Id*. at § 1087c(c)(2)(D).
[21] *Id*. at § 1087c(c)(2)(E).
[22] *Id*. at § 1099c(d).
[23] *Id*. at § 1087c(c)(2)(F).

involves a review of a school's financial aid documentation. While this is an important review for all Title IV schools, the Department should increase the number of specialized staff charged with affirmatively investigating, beyond a review of student federal financial aid files, institutions that have failed one or more of the above-described standards. The staff should also be charged with independently identifying schools that are engaging in illegal conduct that can cause financial instability or taxpayer and student losses (instead of waiting for state enforcement actions or borrowers to raise the alarm). Indeed, the Department has allowed schools to continue receiving aid for years even after they have failed to meet these mandatory standards, resulting in the loss of billions taxpayer dollars.[24] FSA recently announced the formation of an Enforcement Office,[25] but to be successful, it must have the resources to hire adequate numbers of well-trained staff. In addition, it must have the resources needed to allow it to monitor, identify, and prepare the Department to take appropriate action against at-risk schools, using a variety of monitoring and investigative tools such as undercover shoppers, interviews of former students, undercover reviews of admissions training processes, and audits of marketing claims that financially unstable or predatory schools often falsify, such graduate placement rates.

Second, the Department can better utilize provisional program participation agreements (PPPAs) to prevent taxpayer losses and student harm. The Higher Education Act allows the Department to implement a corrective action plan in the form of a PPPA for schools that fail many of the above criteria. The Department can use PPPAs to restrict access to federal funding and require schools to implement necessary improvements, providing that if the school fails to improve, the Department will quickly cut off federal aid. Despite the availability of this critical accountability tool, the Department has not yet revoked a single PPPA, even in cases where there has been evidence that many schools subject to those agreements have broken the law or continued to fall far short of the Department's mandatory financial

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[24] *See* Dan Zibel, Aaron Ament, & Kirin Jessel, *The Missing Billion*, Nat'l Student Loan Defense Network (June 2021), *available at* https://www.defendstudents.org/news/body/NSLDN_paper_Missing_Billion.pdf.

[25] U.S. Dep't of Educ., Press Release, *U.S. Department of Education to Establish an Enforcement Office Within Federal Student Aid* (Oct. 8, 2021), *available at* https://www.ed.gov/news/press-releases/us-department-education-establish-enforcement-office-within-federal-student-aid.

stability requirements.[26]

Finally, in addition to bolstering investigational focus and capacity and strengthening its use of PPPAs as an accountability tool, the Department can reduce taxpayer losses by ensuring that schools and their owners pay the fines and fees associated with statutory and regulatory violations before being allowed to renew their eligibility in the Title IV program. Failure to pay such fees is a strong sign that either the school lacks the financial capability of doing so or does not care to comply with federal law, both of which indicate a school could suddenly close due to financial mismanagement or an eventual government action based on illegal practices. In the past, after the Department has found that a school has violated statutory authority and imposed a fine, it has often failed to aggressively pursue collections against that school. In its recent report *The Missing Billion*, the National Student Loan Defense Network illustrated how the Department has allowed schools to continue receiving Title IV aid despite failing to pay fines, fees, and judgments and displaying clear performance deficiencies as a result of school fraud and other illegal conduct that harmed students.[27] The report found that institutions' debts currently total nearly $1.5 billion.[28]

The Department has even allowed individuals to own or operate schools that receive Title IV funding when the prior schools they owned and operated closed and then failed to reimburse the Department for the resulting taxpayer losses. For example, TA Associates, which owned the now-defunct Vatterott Colleges, owes the Department over $244,350,339.[29] Yet, the Department has continued to allow TA Associates to hold a substantial ownership interest in Full Sail, a school chain that continues to receive Title IV funds, without holding either Full Sail or TA Associates liable for the debt.[30]

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[26] Yan Cao, *Predatory Colleges Think They Are Too Flawed To Fail. Biden's Department of Education Should Prove Them Wrong,* The Century Found. (Sept. 9, 2021), *available at* https://tcf.org/content/commentary/predatory-colleges-think-flawed-fail-bidens-department-education-prove-wrong/?session=1.

[27] Dan Zibel, Aaron Ament, & Kirin Jessel, *The Missing Billion*, Nat'l Student Defense Network (June 2021), *available at* https://www.defendstudents.org/news/body/NSLDN_paper_Missing_Billion.pdf.

[28] *Id*.

[29] *Id*.

[30] *Id*.

B. The Department should improve how it measures financial responsibility.

Currently, the Department's financial responsibility measure does not adequately identify financially unstable schools. The Department requires that schools receiving federal aid pass a series of tests which essentially measure three ratios: primary reserves, equity, and net income.[31] The "composite score" reflects all three ratios and is intended to reflect the overall health of the institution. A composite score can range from negative 1.0 to positive 3.0. If an institution has a score equal or greater to 1.5, it is considered financially stable. Schools with a score between 1.0 and 1.5 are subject to cash monitoring, whereas schools with a score below 1.0 may continue to receive federal funding if they are provisionally certified. As a condition of provisional certification, the school is required to post a letter of credit equal to ten percent or more of the Title IV aid the school received in the institution's most recent fiscal year.

These standards require too little of schools when they are in clear financial trouble and fail to adequately sound the alarm on many risky schools. Experts have concluded that the financial responsibility standards have often failed to provide adequate warning that a school closure is coming and have failed to provide adequate compensation when closures have occurred.[32] The failure of the financial responsibility score to warn of impending closures may be due to its failure to include potential legal liability in its calculation. Schools often appear financially sound despite carrying significant risk due to the predatory practices they use to enroll students or engaging in securities fraud. When such schools ultimately close, if they were provisionally certified and had a financial accountability score, many were only required to post a letter of credit equal to ten percent of the Title IV funds received in the most recent fiscal year. This amount barely scratches the surface of a closed school's liabilities for closed school discharges.

The Department should strengthen the financial responsibility score so that it better identifies at-

[31] This is a summary of the financial responsibility provisions from the Department's website, *available at* https://studentaid.gov/data-center/school/composite-scores.

[32] *See, e.g.*, Robert Shireman, The Policies That Work--And Don't Work-- To Stop Predatory For Profit Colleges, The Century Found. (May 20, 2019), *available at* https://tcf.org/content/report/policies-work-dont-work-stop-predatory-profit-colleges/#policy7.

risk schools and substantially increase the amount of funding schools must provide through a letter of credit when they fail the financial responsibility standards.

C. The Department should conduct an in-depth investigation after a school closes and must use all tools available after a school closes to recoup losses.

Currently, when a school closes, as far as we know the Department does not complete a post-mortem to analyze why the school closed and whether any misconduct was associated with the closure. In fact, the Department does little to preserve necessary evidence to establish school liability and ensure that students are able to obtain debt relief. This evidence includes student records, advertisements, email servers, admissions officers' scripts, lead generator arrangements, and other information which will disappear if the Department does not ensure that it is maintained. (Many of the state governments and accreditors also fail to ensure that these records are maintained). As a result, the Department limits its ability to recoup losses caused by the closure because it does not seek out the evidence necessary to prosecute the school and the deeper pockets who may have profited from the school. While the Department may file a claim as a creditor in the school's eventual bankruptcy, it generally files low-priority claims as an unsecured creditor and, as a result, recoups only pennies on the dollars owed.

The Higher Education Act allows the Department to hold school officials, investors, and others personally liable for specific types of institutional debt.[33] By failing to engage in a post-mortem investigation and ensure the maintenance of evidence after a school closes, however, the Department is forgoing the opportunity to hold school executives, officials, or investors who engaged in illegal misconduct liable for the closure of the school and any other resulting losses. It effectively turns a blind eye to criminal conduct, and ignores potential civil actions that could yield substantial dividends. If the Department were to engage in a robust investigation, it would deter unscrupulous school owners from capriciously closing schools and might give rise to RICO, False Claims Act, and other federal claims that would allow it to recover lost funds. The Department should investigate school closures and all avenues

[33] Dan Zibel & Alice Yao, *Protection and the Unseen*, Nat'l Student Loan Defense Network (Oct. 2020), *available at* https://www.defendstudents.org/news/body/docket/100-Day-Docket-Personal-Liability-Report.pdf.

to the recoupment of losses sustained by taxpayers and students.

Thank you again for the close attention you are paying to how to protect the most vulnerable student loan borrowers, as well as taxpayers, and for the opportunity to provide this testimony. Please feel free to contact me if you have any additional questions.