Issue Paper 5
Session 3: March 16-18, 2016

Issue:	Whether to revise the financial responsibility regulations, and whether to add disclosure requirements, to help protect students, the federal government, and taxpayers against potential school liabilities and risks.
Statutory cite:	§§487(a) and (c), 498 of the Higher Education Act of 1965, as amended, 20 U.S.C. 1094(c), 1099c; 454(a)(6)
Regulatory cite:	34 CFR Part 668 Subpart L, 34 CFR 668.41, 668.90, and § 685.300

Summary of Changes:

Under the HEA and the regulations in Subpart L, a school is financially responsible, in part, if it provides the administrative resources necessary to comply with the title IV program regulations and meets all of its financial obligations. In general, a school that is not financially responsible may (1) participate as a financially responsible school if it submits an irrevocable letter of credit (LOC) for an amount determined by the Secretary that is not less than 50% of the title IV funds it received during its most recently completed fiscal year, or (2) participate under a provisional certification and submit an LOC for an amount determined by the Secretary that is not less than 10% of the title IV funds it received during its most recently completed fiscal year.

We propose to amend the general financial responsibility standards in Subpart L to include actions and events that indicate or signal that (1) a school is likely to have to pay borrower defense claims, and (2) a school's ability to pay claims or continue its participation in the title IV programs is compromised. These actions and events would trigger a requirement that the school submit an LOC based on prior repayments or for an amount that is not less than 10%, for each action/event, of the amount of title IV, HEA program funds received by the school during the most recently completed award year. The Secretary may accept cash or agree to a set aside (reserve fund) in lieu of an LOC but for an equivalent amount. We are making conforming changes to Subpart G to update references in current regulations to refer as appropriate to Subpart L and to address the scope of appeals of financial responsibility determinations made under these revised regulations. We present two options to amend the Direct Loan Program Participation Agreement requirements to better protect borrowers and taxpayers from losses resulting from acts or omissions of schools that would lead to borrower defenses.

In addition, we are adding to the reporting and disclosure provisions in 34 CFR 668.41 a requirement that a school would have to warn enrolled and prospective students a) of any requirement to post a letter of credit to the Department or b) if it has poor repayment outcomes. Repayment rates could be calculated by evaluating the share of each borrower's debt that has been paid down over a period of five years and calculating the median rate of those borrowers. Assuming typical interest rates and a 20-year repayment period, a borrower would be expected to have repaid 15 percent of his original principal balance at the five-year mark. The target for the repayment rate is set at 0 percent (below which the typical borrower is not repaying any of his principal balance within five years, i.e. is in negative amortization)..

Changes: See attached regulatory language.

Subpart L Financial Responsibility

§668.171 General.

(a) ***

(1) Provide the services described in its official publications and statements;

(2) Meet all of its financial obligations; and

(3) Provide the administrative resources necessary to comply with title IV, HEA program requirements.

(b) General standards of financial responsibility. Except as provided under paragraphs (c) and (d) of this section, the Secretary considers an institution to be financially responsible if the Secretary determines that—

(1) The institution's Equity, Primary Reserve, and Net Income ratios yield a composite score of at least 1.5, as provided under §668.172 and appendices A and B to this subpart;

(2) The institution has sufficient cash reserves to make required returns of unearned title IV HEA program funds, as provided under §668.173;

(3) The institution is able to meet all of its financial obligations and otherwise provide the administrative resources necessary to comply with title IV, HEA program requirements; and

(4) The institution or persons affiliated with the institution are not subject to a condition of past performance under §668.174(a) or (b).

(c) *Actions and triggering events*. An institution is not able to meet its financial or administrative obligations under paragraph (b)(3) of this section if it is subject to one or more of the following actions or triggering events.

(1) *Repayments to the Secretary*. At the present time or at any time during the three most recently completed award years, the institution is or was required to repay the Secretary for losses from borrower defense claims in an amount that, for one or more of those years, exceeds the lesser of $100,000 or 10 percent of its current assets, as reported in the most recent audited financial statements submitted by the institution to the Secretary.

(2) *State or Federal agency actions*. At the present time or at any time during the three most recently completed award years, the institution is or was—

(i) Required to repay a debt or liability arising from an audit, investigation, or similar action initiated by a State, Federal, or other oversight entity or settles or resolves a suit brought against it by that entity that is based on claims related to the making of a Federal loan or the provision of educational services, for an amount that, for one or more of those years, exceeds the lesser of $100,000 or 10 percent of its current assets, as reported in the most recent audited financial statements submitted by the institution to the Secretary; or

(ii) Being sued or was sued by one or more State, Federal, or other oversight entities based on claims of any kind unless those claims are included in paragraph (c)(2)(i) of this section, and the potential monetary sanctions or damages from that suit or suits are in an amount that exceeds 10 percent of its current assets, as reported in the most recent audited financial statements submitted by the institution to the Secretary.

(3) *Accrediting agency actions*. At the present time or any time during the three most recently completed award years, the institution is or was—

(i) Required by its accrediting agency to submit a teach out plan, for a reason described under 34 CFR 602.24(c)(1), that covers the institution or any of its branches or additional locations; or

(ii) Placed on probation or issued a show cause order, or placed on an accreditation status that poses an equivalent or greater risk to its accreditation, by its accrediting agency for failing to meet one or more of the agency's standards, and the accrediting agency does not notify the Secretary within six months of taking that action that—

(A) The institution has come into compliance with the agency's standards; or

(B) The institution's failure to comply with the standards within this timeframe has not had and is not expected to have a material adverse financial impact on the institution, and the accrediting agency anticipates that the institution will come into compliance within a longer time frame set by the accrediting agency pursuant to 34 CFR 602.20.

(4) *Loan agreements and obligations.* As disclosed in a note to its audited financial statements or audit opinion, or reported by the institution under paragraph (d) of this section, the institution—

(i) Violated a provision or requirement in a loan agreement with its largest secured creditor; or

(ii) Failed to make a payment in accordance with its debt obligations to its largest secured creditor for more than 120 days.

(5) *Non-title IV revenue*. For its most recently completed fiscal year, the institution did not derive at least 10 percent of its revenue from sources other than title IV, HEA program funds, as provided under §668.28(c);

(6) *Cohort default rates*. The institution's two most recent official cohort default rates are 30 percent or greater, as determined under subpart N of this part, unless the institution files a challenge, request for adjustment, or appeal under that subpart with respect to its rates for one or both of those fiscal years that remains pending, results in reducing below 30 percent the official cohort default rate for either or both years, or precludes the rates from either or both years from resulting in a loss of eligibility or provisional certification.

(7) *Publicly traded institutions*. As reported by the institution under paragraph (d) of this section, or identified by the Secretary—

(i) The Securities and Exchange Commission (SEC) warns the institution that it may suspend trading on the institution's stock, or the institution's stock is delisted involuntarily from the exchange on which the stock was traded;

(ii) The institution disclosed or was required to disclose in a report filed with the SEC a judicial or administrative proceeding stemming from a complaint filed by a person or entity that is not part of a State or Federal action under paragraph (c)(1) of this section; or

(iii) The institution failed to file timely a required annual or quarterly report with the SEC.

(8) *Gainful employment*. As determined annually by the Secretary, the number of students enrolled in gainful employment programs that are failing or in the zone under the D/E rates measure in §668.403(c) is more than 50 percent of the total number of students enrolled in all the gainful employment programs at the institution. The Secretary does not calculate this percentage if less than 50 percent of all the students enrolled at the institution who receive title IV, HEA program funds are enrolled in gainful employment programs.

(9) *Withdrawal of owner's equity*. For an institution whose composite score is less than 1.5, any withdrawal of owner's equity from the institution by any means, including by declaring a dividend.

(10) *Other events or conditions*. The Secretary determines that there is an event or condition that is reasonably likely to have a material adverse effect on the financial condition, business, or results of operations of the institution, including but not limited to whether—

(i) There is a significant fluctuation between consecutive award years in the amount of Direct Loan or Pell Grant funds, or a combination of those funds, received by the institution that cannot be accounted for by changes in those programs;

(ii) The institution is cited by a State licensing or authorizing agency for failing State or agency requirements;

(iii) The institution fails a financial stress test developed or adopted by the Secretary to evaluate whether the institution has sufficient capital to absorb losses that may be incurred as a result of adverse conditions and continue to meet its financial obligations to the Secretary and students;

(iv) The institution or corporate parent has a non-investment grade bond or credit rating;

(v) As calculated by the Secretary, the institution has high annual dropout rates; or(vi) Any event reported to the SEC.

(d) *Reporting requirements*. In accordance with procedures established by the Secretary, an institution must notify the Secretary of any action or event identified in paragraph (c) of this section no later than 10 days after that action or event occurs. The Secretary may take an administrative action under paragraph (g) of this section against the institution for failing to provide timely notice under this paragraph.

(e) Public institutions. (1) The Secretary considers a domestic public institution to be financially responsible if the institution—

(i)(A) Notifies the Secretary that it is designated as a public institution by the State, local, or municipal government entity, tribal authority, or other government entity that has the legal authority to make that designation; and

(B) Provides a letter from an official of that State or other government entity confirming that the institution is a public institution; and

(ii) Is not subject to a condition of past performance under §668.174.

(2) The Secretary considers a foreign public institution to be financially responsible if the institution—

(i)(A) Notifies the Secretary that it is designated as a public institution by the country or other government entity that has the legal authority to make that designation; and

(B) Provides documentation from an official of that country or other government entity confirming that the institution is a public institution and is backed by the full faith and credit of the country or other government entity; and

(ii) Is not subject to a condition of past performance under §668.174.

(f) Audit opinions. Even if an institution satisfies all of the general standards of financial responsibility under paragraph (b) of this section, the Secretary does not consider the institution to be financially responsible if, in the institution's audited financial statements, the opinion expressed by the auditor was an adverse, qualified, or disclaimed opinion, or the auditor expressed doubt about the continued existence of the institution as a going concern, unless the Secretary determines that a qualified or disclaimed opinion does not have a significant bearing on the institution's financial condition.
(g) Administrative actions. If the Secretary determines that an institution is not financially responsible under the standards and provisions of this section or under an alternative standard in §668.175, or the institution does not submit its financial and compliance audits by the date and in the manner required under §668.23, the Secretary may initiate an action under subpart G of this part to fine the institution, or limit, suspend, or terminate the institution's participation in the title IV, HEA programs.

§668.175 Alternative standards and requirements.

(a) *General.* An institution that is not financially responsible under the general standards and provisions in §668.171, may begin or continue to participate in the title IV, HEA programs by qualifying under an alternate standard set forth in this section.

(b) *Letter of credit alternative for new institutions.* A new institution that is not financially responsible solely because the Secretary determines that its composite score is less than 1.5, qualifies as a financially responsible institution by submitting an irrevocable letter of credit, that is acceptable and payable to the Secretary, for an amount equal to at least one-half of the amount of title IV, HEA program funds that the Secretary determines the institution will receive during its initial year of participation. A new institution is an institution that seeks to participate for the first time in the title IV, HEA programs.

(c) *Letter of credit alternative for participating institutions.* A participating institution that is not financially responsible either because it does not satisfy one or more of the standards of financial responsibility under §668.171(b), or because of an audit opinion described under §668.171(d), qualifies as a financially responsible institution by submitting an irrevocable letter of credit, that is acceptable and payable to the Secretary, for an amount determined by the Secretary that is not less than one-half of the title IV, HEA program funds received by the institution during its most recently completed fiscal year.

(d) *Zone alternative.* (1) A participating institution that is not financially responsible solely because the Secretary determines that its composite score is less than 1.5 may participate in the title IV, HEA programs as a financially responsible institution for no more than three consecutive years, beginning with the year in which the Secretary determines that the institution qualifies under this alternative.

(i)(A) An institution qualifies initially under this alternative if, based on the institution's audited financial statement for its most recently completed fiscal year, the Secretary determines that its composite score is in the range from 1.0 to 1.4; and

(B) An institution continues to qualify under this alternative if, based on the institution's audited financial statement for each of its subsequent two fiscal years, the Secretary determines that the institution's composite score is in the range from 1.0 to 1.4.

(ii) An institution that qualified under this alternative for three consecutive years, or for one of those years, may not seek to qualify again under this alternative until the year after the institution achieves a composite score of at least 1.5, as determined by the Secretary.

(2) Under this zone alternative, the Secretary—

(i) Requires the institution to make disbursements to eligible students and parents, and to otherwise comply with the provisions, under either the cash monitoring or reimbursement payment method described in §668.162;

(ii) Requires the institution to provide timely information regarding any of the following oversight and financial events—

(A) Any event that causes the institution, or related entity as defined in the Statement of Financial Accounting Standards (SFAS) 57, to realize any liability that was noted as a contingent liability in the institution's or related entity's most recent audited financial statement; or

(B)Any extraordinary losses, as defined in accordance with Accounting Principles Board (APB) Opinion No. 30;

(iii) May require the institution to submit its financial statement and compliance audits earlier than the time specified under §668.23(a)(4); and

(iv) May require the institution to provide information about its current operations and future plans.

(3) Under the zone alternative, the institution must—

(i) For any oversight or financial event described under paragraph (d)(2)(ii) of this section for which the institution is required to provide information, provide that information to the Secretary by certified mail or electronic or facsimile transmission no later than 10 days after that event occurs. An institution that provides this information electronically or by facsimile transmission is responsible for confirming that the Secretary received a complete and legible copy of that transmission; and

(ii) As part of its compliance audit, require its auditor to express an opinion on the institution's compliance with the requirements under the zone alternative, including the institution's administration of the payment method under which the institution received and disbursed title IV, HEA program funds.

(4) If an institution fails to comply with the requirements under paragraphs (d) (2) or (3) of this section, the Secretary may determine that the institution no longer qualifies under this alternative.

(e) (reserved)

(f) *Provisional certification alternative.* (1) The Secretary may permit an institution that is not financially responsible to participate in the title IV, HEA programs under a provisional certification for no more than three consecutive years if—

(i) The institution is not financially responsible because it does not satisfy the general standards under §668.171(b)(1) or (3), or because of an audit opinion described under §668.171(f); or

(ii) The institution is not financially responsible because of a condition of past performance, as provided under §668.174(a), and the institution demonstrates to the Secretary that it has satisfied or resolved that condition.

(2) Under this alternative, the institution must—

(i) Submit to the Secretary an irrevocable letter of credit that is acceptable and payable to the Secretary, submit cash, or agree to a set-aside under paragraph (h) of this section, for an amount determined by the Secretary under paragraph (f)(4) of this section~~,~~, except that this requirement does not apply to a public institution; and

(ii)Comply with the provisions under the zone alternative, as provided under paragraph (d)(2) and (3) of this section.

(3) If at the end of the period for which the Secretary provisionally certified the institution, the institution is still not financially responsible, the Secretary may again permit the institution to participate under a provisional certification, but the Secretary—

(i) May require the institution, or one or more persons or entities that exercise substantial control over the institution, as determined under §668.174(b)(1) and (c), or both, to submit to the Secretary financial guarantees for an amount determined by the Secretary to be sufficient to satisfy any potential liabilities that may arise from the institution's participation in the title IV, HEA programs; and

(ii) May require one or more of the persons or entities that exercise substantial control over the institution, as determined under §668.174(b)(1) and (c), to be jointly or severally liable for any liabilities that may arise from the institution's participation in the title IV, HEA programs.

(4) The institution must submit to the Secretary an irrevocable letter of credit for an amount that is—

(i) For repayments to the Secretary for losses from borrower defense claims under §668.171(c)(1), the greatest annual loss incurred by the Secretary during the three most recently completed award years to resolve those claims or the amount of losses incurred by the Secretary during the most recently completed award year, whichever is greater, plus a portion of the amount of any outstanding or pending claims based on the ratio of the total value of claims adjudicated in favor of borrowers during the three most recently completed award years to the total value of claims adjudicated during the three most completed award years;

(ii) For a State or Federal action under §668.171(c)(2)(i) or (ii), 10 percent or more, as determined by the Secretary, of the amount of Direct Loan program funds received by the institution during its most recently completed fiscal year; and

(iii) For any other action or triggering event described in §668.171(c), or if the institution's composite score is less than 1.0, or the institution no longer qualifies under the zone alternative, 10 percent or more, as determined by the Secretary, of the total amount of title IV, HEA program funds received by the institution during its most recently completed fiscal year.

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(h) Set-aside. If an institution does not provide cash or the letter of credit for the amount required under paragraph (d) or (f) of this section within 30 days of the Secretary's request, the Secretary offsets the amount of title IV, HEA program funds that an institution has earned in a manner that ensures that, by the end of a nine-month period, the total amount offset equals the amount of cash or the letter of credit the institution would otherwise provide. The Secretary maintains the amount of funds offset in a temporary escrow account, uses the funds to satisfy the debt and liabilities owed to the Secretary not otherwise paid directly by the institution, and returns to the institution any funds not used for this purpose during the period for which the cash or letter of credit was required.

§668.41 Reporting and Disclosure of Information.

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(h) *Loan repayment rate.* For any fiscal year in which an institution's loan repayment rate is less than zero, the institution must disclose information about that rate to enrolled and prospective students in the manner described in paragraph (j), (k), (l) and (m) of this section.

(1) *Methodology.* For each fiscal year, the Secretary calculates the institution's loan repayment rate for the cohort of borrowers whose Direct Loans entered repayment at any time during the fifth fiscal year prior to the most recently completed fiscal year by—

(i) Determining the original principal balance of the loans for each of those borrowers;

(ii) Determining the current principal balance of the loans for each of those borrowers;

(iii) Calculating the difference between the original and the current principal balance of the loans for each of those borrowers and expressing that difference as a percentage reduction of, or an increase in, the original principal balance; and

(iv) On a scale where percentage reductions in principal are positive values and percentage increases in principal are negative values, determining the median value. The median value is the repayment rate for that fiscal year.

(2) *Definition of terms and exclusions.* For purpose of calculating the loan repayment rate under this section—

(i) The term—

(A) "Original principal balance" (OPB) means the amount of the outstanding balance, including capitalized interest, on the Direct Loans owed by a student for attendance at the institution on the date the loans first entered repayment. The OPB does not include PLUS loans made to parent borrowers or TEACH Grant-related loans. For consolidation loans, the OPB includes only those loans attributable to the borrower's attendance at the institution; and

(B) "Current principal balance" (CPB) means the amount of the outstanding balance, including capitalized interest, on the Direct Loans owed by the student at the end of the most recently completed fiscal year. For a defaulted loan, the CFB is equal to the OPB.

(C) "Measurement period" refers to the period of time between the date that a borrower's loan enters repayment and the end of the fiscal year for which the CPB of that loan is determined.

(ii) The Secretary excludes a borrower from the calculation if—

(A) One or more of the borrower’s loans were in a military-related deferment status at time during the measurement period;

(B) One or more of the borrower's loans are either under consideration by the Secretary, or have been approved, for a discharge on the basis of the borrower's total and permanent disability, under 34 CFR 682.402 or 685.212;

(C) The borrower was enrolled in another institution during the measurement period; or

(D) The borrower died.

(*3*) *Secretary’s calculation of repayment rate*. The Secretary determines the repayment rate as follows:

(i) *Creating the list of students.* (A) The Secretary selects the students to be included on the list by Identifying the borrowers who entered repayment on FFEL or Direct Loans received for enrollment at the institution during the five award years prior to the most recently completed award year, and the borrowers who are in default, the original principal balance of each borrower at the time the borrower entered repayment, the amount of the principal balance at the end of the most recently completed award year, and the borrowers that would be removed from the list under paragraph (2)(ii) of this section.

(B) The Secretary provides the list to the school.

(C) *Institutional corrections to the list.* (*1*) The Secretary presumes that the list of borrowers and the identity and loan information for those borrowers are correct unless the school provides evidence to the contrary that is satisfactory to the Secretary, in a format and process determined by the Secretary. The schools bears the burden of proof that the list is incorrect.

(*2*) No later than 45 days after the date the Secretary provides the list to the school, the school may— (*i*) Provide evidence showing that a borrower should be included on or removed from the list pursuant to paragraph (h)(3)(i)(A) of this section or otherwise; or

(*ii*) Correct or update a borrower’s identity or loan information;

(*3*) After the 45-day period expires, the school may no longer seek to correct the list of borrowers or revise the identity or loan information of those borrowers included on the list.

(*4*) The Secretary considers the evidence provided by the school and either accepts the correction or notifies the school of the reasons for not accepting the correction. If the Secretary accepts the correction, the Secretary uses the corrected information to create the final list.

(ii) *Notice* of *draft repayment rate*. The Secretary notifies the school of the draft repayment rate, the borrowers who are included on the final list and the loan data used to calculate the repayment rate.

(A) *Institutional challenges to the rate.* No later than 45 days after the Secretary notifies an institution of its draft loan repayment rate, the institution may challenge the accuracy of the information that the Secretary used to calculate the draft rate by submitting, in a form prescribed by the Secretary, evidence satisfactory to the Secretary demonstrating that the information was incorrect.

(B) The Secretary considers any evidence provided by the institution challenging the accuracy of the information the Secretary used to calculate the draft rate and notifies the institution whether the challenge is accepted or the reasons the challenge is not accepted. If the Secretary accepts the challenge, the Secretary uses the corrected data to calculate the final loan repayment rate.

(C) An institution may challenge the Secretary's calculation of the loan repayment rate only once for an award year. An institution that does not timely challenge the rates waives any objection to the rates as stated in the notice.

(iii) *Final calculations.* (A) After expiration of the 45-day period, and subject to resolution of any challenge under paragraph (3)(i)(C) of this section, an institution’s draft repayment rate constitutes the final rate for the institution.

(B) The Secretary informs the institution of its final repayment rate by issuing a notice of determination.

(4) *Privacy considerations.* An institution is not required to disclose a repayment rate if the repayment rate is based on fewer than 10 borrowers who have entered repayment in the award year.

(i) *Letter of Credit disclosure*. For any fiscal year that an institution is required to submit an irrevocable letter of credit under 668.175(d) and (f), the institution must disclose information about that requirement to enrolled and prospective students in the manner described in paragraph (j), (k), and (l) of this section.

(j) *Form of notice to students*. (1) The disclosures that institutions must provide to current and prospective students must include warning language that the Secretary will publish in the Federal Register.

(2) The Secretary will conduct consumer testing to make the disclosure language as meaningful as possible.

(k) *Delivery to enrolled students*. (1) An institution must provide the disclosures required by paragraphs (h) and (i) of this section by means of a notice in writing to each enrolled student no later than 30 days after being informed by the Secretary of its student loan repayment and/or a requirement to post an irrevocable letter of credit by—

(i) Hand-delivering the disclosure notification as a separate document to the student individually or as part of a group presentation; or

(ii) Sending the disclosure notification to the primary email address or other electronic communication method used by the institution for communicating with the student about the program.

(2) The institution must—

(i) Ensure that the disclosure notification is the only substantive content in the message;

(ii) Receive electronic or other written acknowledgement from the student that the student has received the message, except that written acknowledgment of hand-delivered disclosures is required only in connection with the disclosures described in paragraph (h) above;

(iii) Send the disclosure(s) using a different address or method of delivery if the institution receives a response that the message could not be delivered; and

(iv) Maintain records of its efforts to provide the required disclosure notification.

(l) *Delivery to prospective students*. (1) An institution must provide the disclosure required by paragraphs (h) and (i) of this section to each prospective student at the first contact between the institution and the student by—

(i) Hand-delivering the disclosure notification as a separate document to the prospective student individually, or as part of a group presentation; or

(ii) Sending the disclosure notification to the primary email address or other electronic communication method used by the institution for communicating with the prospective student.

(2) The institution must—

(i) Ensure the disclosure notification is the only substantive content in the message;

(ii) Receive electronic or other written acknowledgement from the prospective student that the student has received the message, except that written acknowledgment of hand-delivered disclosures is required only in connection with the disclosures described in paragraph (h) above;

(iii) Send the disclosure notification using a different address or method of delivery if the institution receives a response that the email could not be delivered; and

(iv) Maintain records of its efforts to provide the required disclosure notification.

(m) *Promotional materials.* (1) All promotional materials made available by or on behalf of an institution to prospective students that identify the institution by name must include—

(i) The disclosure of the repayment rate required in paragraph (h) in a prominent manner; or

(ii) Where space or airtime constraints would preclude the inclusion of the disclosure, the Web address (URL) of, or the direct link to, the disclosure, provided that the URL or link is prominent, readily accessible, clear, conspicuous, and direct.

(2) Promotional materials include, but are not limited to, an institution's catalogs, invitations, flyers, billboards, and advertising on or through radio, television, print media, the Internet, and social media.

(3) The institution must ensure that all promotional materials, including printed materials, about an institution are accurate and current at the time they are published, approved by a State agency, or broadcast.

§668.93 Limitation.

A limitation may include, as appropriate to the Title IV, HEA program in question—

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(h) A change in the participation status of the institution from fully certified to participate to provisionally certified to participate under §668.13(c).

(i) Other conditions as may be determined by the Secretary to be reasonable and appropriate.

§668.90 Initial and final decisions.

(a)(1) * * *

(2) The hearing official's initial decision states whether the imposition of the fine, limitation, suspension, or termination sought by the designated department official is warranted, in whole or in part. If the designated department official brought a termination action against the institution or servicer, the hearing official may, if appropriate, issue an initial decision to fine the institution or servicer, as applicable, or, rather than terminating the institution's participation or servicer's eligibility, as applicable, impose one or more limitations on the institution's participation or servicer's eligibility.

(3) Notwithstanding the provisions of paragraph (a)(2) of this section—

(i) If, in a termination action against an institution, the hearing official finds that the institution has violated the provisions of §668.14(b)(18), the hearing official also finds that termination of the institution's participation is warranted;

(ii) If, in a termination action against a third-party servicer, the hearing official finds that the servicer has violated the provisions of §668.82(d)(1), the hearing official also finds that termination of the institution's participation or servicer's eligibility, as applicable, is warranted;

(iii) In an action brought against an institution or third-party servicer that involves its failure to provide a letter of credit or other financial protection in the amount specified by the Secretary under §668.15 or subpart L of part 668, the hearing official finds that the amount of the letter of credit or other financial protection established by the Secretary is appropriate, unless the institution can demonstrate that the amount was not warranted because—

(A) The events or conditions identified by the Secretary as the grounds on which the protection is required no longer exist or have been resolved in a manner that eliminates the risk they posed to the institution’s ability to meet its financial obligations; or

(B) The institution has proffered alternative financial protection that provides students and the Department adequate protection against losses resulting from the risks identified by the Secretary.

Adequate protection consists of one or more of the following–

(1) A deposit with the Secretary of cash or a cash equivalent in the amount of financial protection demanded by the Secretary to be held by the Secretary in escrow; and

(2) An agreement with the Secretary that a portion of the funds earned by the institution under a reimbursement funding arrangement will be temporarily withheld in such amounts as will meet, by the end of a nine-month period, the amount of the required financial protection demanded;

(iv) In a termination action taken against an institution or third-party servicer based on the grounds that the institution or servicer failed to comply with the requirements of §668.23(c)(3), if the hearing official finds that the institution or servicer failed to meet those requirements, the hearing official finds that the termination is warranted;

(v)(A) In a termination action against an institution based on the grounds that the institution is not financially responsible under §668.15(c)(1), the hearing official finds that the termination is warranted unless the institution demonstrates that all applicable conditions described in §668.15(d)(4) have been met; and

(B) In a termination or limitation action against an institution based on the grounds that the institution is not financially responsible–

(1) Upon proof of the conditions in §668.174(a), the hearing official finds that the limitation or termination is warranted unless the institution demonstrates that all the conditions in §668.175(f) have been met; and

(2) Upon proof of the conditions in §668.174(b)(1), the hearing official finds that the limitation or termination is warranted unless the institution demonstrates that all applicable conditions described in § 668.174(b)(2) or 668.175(g) have been met.

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

Option A:

§ 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--

(1) * * *

(10) Provide that the school will not charge any fees of any kind, however described, to student or parent borrowers for origination activities or the provision of any information necessary for a student or parent to receive a loan under part D of the Act or any benefits associated with such a loan;

(11) Provide that:

(i) The school will notify the Secretary upon the submission of the initial filing of any claim, whether in arbitration or in a court, asserted by a student, whether as an individual or as a member of a class, or by a governmental agency, based on any act or omission of the school attended by the student that relates to the making of a Federal loan or the provision of educational services financed by that loan;

(ii) The school will not compel, through the use of pre-dispute mandatory arbitration agreements or any other means, arbitration of any such claims asserted by students in cases filed in a court on behalf of a class unless and until class certification is denied or the class claims are dismissed;

(iii) The school will allow any borrower to resolve any claim described in paragraph (a)(11)(i), if in arbitration, in person or by electronic means;

(iv) The school will not compel any borrower to resolve any claim described in paragraph (a)(11)(i), in a court whose district does not include the school;

(v) If the school enters into arbitration or requires arbitration with any borrower on a claim described in paragraph (a)(11)(i), it will ensure that--

(A) The Secretary receives a copy of each filing by any party and each order, ruling, decision or other written document produced by the arbitrator, within 10 days of the filing, in the case of a filing by the school, or the school's receipt of the filing, order, ruling, decision, or other written document, in any other case;

(B) The proceedings in such arbitration are open to the public and recorded and transcribed with such recordings and transcriptions available to the Secretary upon request;

(C) No party is prohibited from speaking, writing, or otherwise communicating about the claims at issue or any other matter related to the arbitration, except that the parties to the arbitration may agree not to reveal the terms of any settlement;

(D) Multiple borrowers may bring common claims in one arbitration proceeding, provided they would meet the requirements for bringing such common claims that would apply in the United States district court for the district in which the school is located; and

(E) If the school has the right to bring any type of claim outside of arbitration, the borrower has an equivalent right to bring such claims outside of arbitration; and

(12) Comply with other provisions that the Secretary determines are necessary to protect the interests of the United States and to promote the purposes of part D of the Act.

Option B:

§ 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--

(1) * * *

(10) Provide that the school will not charge any fees of any kind, however described, to student or parent borrowers for origination activities or the provision of any information necessary for a student or parent to receive a loan under part D of the Act or any benefits associated with such a loan;

(11) Provide that for any claim related to the making of a student loan or the provision of educational services:

(i) The claim may only be arbitrated with the student's consent after the claim arises;

(ii) The school will not prohibit students from asserting any such claim in cases filed in a court on behalf of a class; and

(iii) The school will notify the Secretary upon the submission of and submit copies of any initial filings and decisions for such claim whether filed in court or in arbitration; and

(12) Comply with other provisions that the Secretary determines are necessary to protect the interests of the United States and to promote the purposes of part D of the Act.