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Submitted via Federal eRulemaking Portal

The Honorable Miguel Cardona
United States Department of Education
400 Maryland Avenue, SW
Washington, D.C. 20202

Brian Schelling
United States Department of Education
400 Maryland Avenue, SW
Washington, DC 20202

Re: Docket ID ED-2021-OPE-0062

Dear Secretary Cardona and Mr. Schelling,

We, the undersigned Attorneys General of Massachusetts, Minnesota, Alabama, California, Colorado, Connecticut, Delaware, District of Columbia, Hawaii, Idaho, Illinois, Maryland, Michigan, New Jersey, New York, North Carolina, Oregon, Pennsylvania, Rhode Island, Washington, and Wisconsin along with the Executive Director of the Hawaii Office of Consumer Protection, write to share our views on the U.S. Department of Education's ("ED") proposed rulemaking regarding the 90/10 Rule and changes in institutional ownership.

We wish to express our strong support for ED's regulatory goals. ED's proposed 90/10 regulations represent critical improvements to the Rule's application and protect borrowers from dangerous loopholes. With respect to ED's proposals regarding changes in institutional ownership (CIO), we are pleased that ED has recognized the risks posed to borrowers by institutional conversions, particularly those from for-profit to nonprofit status. ED's proposals will help prevent sham conversions that imperil borrowers and squander the taxpayers' investment. However, we urge the Department to strengthen its CIO proposals to eliminate opportunities for dangerous financial entanglements that remain unaddressed by the proposed regulations.

I. 90/10 Rule

The undersigned attorneys general support the proposed updates to the 90/10 Rule, which effectuate Congress's recent action to close the loophole related to financial aid administered by the VA and otherwise improve the Rule's application.

The 90/10 Rule was originally directed by Congress in 1992 as a response to findings of fraud, waste, and abuse in the for-profit higher education sector. While investigations identified concerns across all types of institutions, reports by ED's Office of Inspector General and the GAO found that for-profit schools were the primary contributor to the industry's growing problems. Such issues included tuition increases tied to maximum financial aid (rather than market factors), disbursements of financial aid without concern for whether students could repay their debt, and other problems with program integrity. Congress created the 90/10 Rule as a bright-line quality-control measure: schools would have to maintain and invest in programs that offered sufficient quality to attract a minimum level of nongovernmental financial support and prevent the worst examples of abuse within the sector.[1]

Bad actors, however, soon found ways to exploit gaps in the 90/10 framework—specifically, the exclusion of benefits disbursed from the VA from the calculation of federal aid revenues. As a bipartisan group of 22 state attorneys general observed in a 2012 letter to Congressional leadership, federal and state investigations in the late 2000s and early 2010s revealed "that some for-profit schools engage in high-pressure sales tactics, targeting vulnerable populations including disabled veterans" and "other illegal conduct including alleged violations of [] recruiter compensation laws, false representations concerning post-graduation employment rates and improper handling of student financial aid."[2]

The state attorneys general also noted that, since the 90/10 Rule went into effect, a new and troubling dynamic emerged in the industry, whereby "a large population of veterans and service men and women with access to new and generous educational benefit packages [] have become a rich target for aggressive college recruiters." Because the Post 9/11 GI Bill made billions of dollars in new educational revenue available for veterans and their families, a new market of potential paying students emerged for schools looking to exploit and maximize financial aid. While these new benefits administered by the VA were funded by taxpayers, none of these dollars counted towards schools' 90% cap on federal funding. The exit of private student lending from the for-profit education market further made these VA benefits attractive to schools struggling to meet 90/10 thresholds. In sum, the "90/10 loophole" not only undermined the purpose of the Rule, it also created perverse incentives for abusive and low-quality programs to target recruitment at servicemembers and veterans. The state attorneys general thus strongly urged Congress to "close

[1] The 90/10 Rule Under HEA Title IV: Background & Issues, Congressional Research Service, April 26, 2021.

[2] Ltr. from Kentucky Attorney General Jack Conway to Sen. Patty Murray, Rep. Jeff Miller, Sen. Richard Burr, Rep. Bob Filner, Sen. Tom Harkin, & Sen. Michael Enzi, May 29, 2012.

this loophole, protect our tax dollars, and protect our service members from these predatory practices."[3]

For these reasons, we were heartened to see the American Rescue Plan Act of 2021 fix the 90/10 loophole by amending the HEA to provide that schools may not derive more than 90% of their revenues from *all* federal education assistance funds. Such funds must include GI Bill and Tuition Assistance benefits administered by the VA, as well as other federal funds used to pay a student's tuition and fees. ED's current 90/10 proposals, which reflect consensus from negotiated-rulemaking sessions earlier this year, closes the loophole and effectuates Congressional intent.

We similarly support ED's other updates to the 90/10 Rule based on the consensus of the negotiated rulemaking. ED's proposal includes welcome changes that will clarify the 90/10 Rule's formula and process, prevent abuse, and enhance consumer protection, including by:

- Preventing schools from delaying disbursements to game the Rule,

- Ensuring that federal funds received directly by students and paid towards tuition and fees are counted towards revenue calculations,

- Requiring cash-basis accounting methods to calculate revenue percentages,

- Preventing schools from collecting non-Federal revenue from test-preparation courses and other programming where the school is not providing helpful training or education in the student's field of study,

- Requiring disclosures to students about a school's failure to meet 90/10 guidelines and its important implications for loss of financial aid eligibility,

- Clarifying that scholarships are designated funds from outside sources that are unrelated to the institution, its owners, or affiliates, and

- Clarifying the types of revenues falling under different portions of the 90/10 equation.

Additionally, we commend ED's goal of preventing schools from attempting to use high-cost institutional financing to meet 90/10 revenue requirements. As our states' chief civil law enforcers, we have substantial experience in addressing complaints concerning high-cost institutional loans made by for-profit schools to finance tuition and fees.[4] It is important that ED's proposal prevents schools from including interest from institutional lending as revenue under the

[3] *Id*.

[4] *See, e.g., Minnesota v. Minn. Sch. of Bus.*, 899 N.W.2d 467 (Minn. 2017) (holding that high-interest institutional loans made by for-profit colleges violated state usury and lender-licensing laws); *Illinois v. Alta Colleges, Inc.*, No. 14-C-3786, 2014 WL 4377579, at *1 (N.D. Ill. Sept. 4, 2014) (rejecting challenge to claims that institutional loans violated consumer-lending laws); *CFPB v. ITT Educ. Servs., Inc.*, 219 F. Supp. 3d 878, 913 (S.D. Ind. 2015) (same); *CFPB v. Corinthian Colleges, Inc.*, No. 1:14-CV-07194, 2015 WL 10854380, *4 (N.D. Ill. Oct. 27, 2015) (ordering default judgment for claims for illegal institutional lending).

Rule. This follows Congressional intent to only include revenue that pays for tuition and fees and ensures that schools are not incentivized to charge exorbitant interest on their institutional financing.

We are also concerned about the growing use of "income share agreements" (ISAs) as a source of institutional financing for schools. Indeed, civil regulators have brought enforcement actions to prevent the use of ISAs that violate state laws.[5] ED's proposed Rule instills guardrails relating to the use of ISAs, including by ensuring identification of tuition charges covered by ISAs and an imputed interest rate. The proposal also caps the imputed interest rate to that allowed for unsubsidized federal loans and prevents sales of ISAs from being included as non-Federal revenue. We believe that these proposed standards are beneficial and will help prevent the 90/10 Rule from creating incentives for reckless and predatory institutional financing to our states' residents.

II. Changes in Institutional Ownership

Years of investigations and enforcement actions by our offices have resulted in considerable public scrutiny of for-profit schools. Facing this backlash, for-profit schools have increasingly sought to convert themselves into nonprofit entities to benefit from the reputational and regulatory benefits of this status. However, these conversions have not eliminated institutional misconduct and the risk of harm to students. Under existing regulations, such conversions have been able to proceed despite continuing financial entanglements with prior owners and institutional incentives that risk harm to borrowers and taxpayers. In fact, while fraud complaints at nonprofit institutions are relatively rare, one study from 2021 found that for the proceeding five years, the largest number of fraud complaints came from three nonprofit institutions, all of which had previously been proprietary and where control never fully shifted away from former owners with ongoing financial interests.[6]

In 2020, the GAO published a report that highlighted some of the risks associated with for-profit to nonprofit conversions.[7] Seventy five percent of institutions converting from for-profit to nonprofit status between January 2011 and August 2020 were sold to entities that have never before operated education institutions.[8] Such conversions pose serious risks to students. One third of these transactions involved some level of "insider involvement", raising the risk of continued financial entanglements with previous owners.[9]

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[5] *See, e.g., Washington v. Prehired* LLC, No. 22-2-08651-3 SEA, Compl. (Wash. Super. Ct. June 8, 2022); *In re Better Future Forward*, Consent Order, 2021-CFPB-0005 (CFPB Sep. 7, 2021); *In re Meratas, Inc.*, Consent Order, NMLS ID No. 2120180 (Cal. Dep't Fin. Protection & Innovation Aug. 5, 2021).

[6] The Century Foundation, "These Colleges Say They're Nonprofit – But Are They?" January 2021, https://tcf.org/content/commentary/colleges-say-theyre-nonprofit/?agreed=1

[7] U.S. Government Accountability Office, "IRS and Education Could Better Address Risks Associated with Some For-Profit College Conversions," December 2020.

[8] *Id.* at 29.

[9] *Id.*

The risk of harm posed by such conversions and their increasing prevalence necessitate a concerted regulatory response by ED. We agree with ED that "it is necessary to reevaluate the relevant policies to accommodate the increased complexity of changes in ownership arrangements and to mitigate the greater risk to students and taxpayers when institutions fail to meet Federal requirements."[10] We are glad that ED recognizes the risks posed by these conversions and is seeking to address these concerns in the current proposed regulations. In particular, we are heartened to see ED proposing a definition of "nonprofit institution" that goes a long way towards ensuring that schools converting from for-profit to nonprofit status do not maintain financial entanglements with private actors that could result in detrimental financial incentives for the institution. We also support ED's effort to clarify: (1) its authority to determine that a school undergoing a change of ownership may not be entitled to continued access to Title IV funds if it no longer meets the requirements of Title IV eligibility, and (2) ED's authority to impose conditions on an institution's temporary provisional program participation agreement (TPPPA) while ED is reviewing the institution's proposed change of ownership.

Although we commend ED for proposing considerable and substantive improvements to its existing regulations, we urge ED to adopt additional measures to ensure that it is not inadvertently creating loopholes that are subject to abuse by institutions with problematic financial incentives. Unfortunately, owners of for-profit schools have already demonstrated the ability to structure complex financial transactions in an effort to benefit from nonprofit status while maintaining financial entanglements that pose the same risks to students that ED, and the states, have been combatting for years. We urge ED to adopt regulations that further minimize opportunities for regulatory evasion.

A. Further Constrain Definition of Nonprofit Institution

We applaud ED for its proposals to clarify the definition of ''nonprofit institution'' in § 600.2 to make clear that a nonprofit's net earnings may not benefit a natural person or private entity, and that a nonprofit institution "is not an obligor on a debt to a former owner or affiliated person or entity" and cannot "enter into a revenue-sharing or other kind of agreement involving payment to a former owner or affiliated person or entity."[11]

While the proposed language would provide important protections from improper revenue-sharing between converted nonprofit institutions and former owners or affiliated entities, we are concerned that the proposal does not go far enough. Rather than barring converted nonprofit institutions from engaging in *any* revenue-sharing arrangements or service agreements with entities affiliated with former owners, the Department proposes taking on the considerable burden of assessing whether continued revenue-sharing arrangements or service agreements "are reasonable based on the market price for the services or agreements."[12] As the state attorney general representatives noted during the negotiated rulemaking sessions, engaging in assessments

[10] 87 Fed. Reg. 45,437.

[11] *Id.* at 45,440.

[12] *Id.* at 45,461.

of fair market value can be onerous, particularly in the context of educational services, where fair market value may be difficult to determine. Our offices have considerable experience undertaking such analyses and have firsthand knowledge of how complicated and resource-intensive these analyses can be. In light of the risks posed by continued revenue-sharing arrangements and contractual obligations, we propose that ED eliminate this exception to the prohibition on revenue-sharing and other agreements with entities affiliated with former owners. Doing so would protect students, eliminate opportunities for mischief, and preserve Departmental resources.

B. Retain 25% Threshold for Determining that Change of Control Occurred

Under present regulations, ED determines that a change in institutional control has occurred, necessitating automatic review, "either when a person acquires both control of at least 25 percent of the outstanding voting stock of the corporation and control of the corporation or when a person ceases to own or control that proportion of the stock of the corporation or to control the corporation." [13] ED proposes to expand the list of criteria that constitute a change of ownership, but to replace the 25% threshold with a 50% threshold. While we support ED's expansion of the circumstances indicating a change of ownership, we urge ED to retain the 25% threshold, where applicable.[14]

It is indisputable that entities with less than 50% of voting interests can exercise considerable control over an institution through voting blocs and other structural arrangements. Indeed, ED has acknowledged as much in lowering the reporting requirements for changes in ownership from 25% to 5% changes in ownership interests. In doing so, ED justified the proposed change by explaining that ED needed to monitor smaller changes in ownership interests more closely because "institutions might seek to evade Department oversight."[15] We agree with this observation and have serious concerns that raising the threshold from 25% to 50% will facilitate efforts to "evade Department oversight." While the overwhelming majority of regulatory changes proposed by ED in this NPRM will have the effect of improving oversight and protecting students, this proposal will have the opposite effect. We do not share ED's confidence that reducing the reporting threshold will mitigate the detrimental effects of raising the threshold for what automatically constitutes a change of ownership requiring Departmental review. Rather, we fear that this change will create an incentive for former owners and their affiliates to evade regulations by establishing creative arrangements that appear to fall below the 50% change of control threshold. As such, we encourage ED to reconsider this change.

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We strongly support ED's proposed regulations, which will protect student loan borrowers from institutional misconduct and safeguard the taxpayer investment. We appreciate ED's thoughtfulness and diligence and look forward to continuing our mutual work to support and protect borrowers.

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[13] *Id.* at 45,466.

[14] *Id.* at 45,467.

[15] *Id.* at 45,465.

Sincerely,

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