

The Role of Receiverships, Bankruptcies, and other Restructuring Options in Higher Education




NASASPS | Annual Conference
Jacksonville, Florida | April 15, 2019

About the Presenters

- Aaron D. Lacey
 - Partner and Practice Leader, Higher Education Practice, Thompson Coburn LLP
- Higher Education Practice
 - Provide **regulatory counsel** on federal, state, and accrediting agency laws and standards (e.g., Title IV, GE, BDR, Title IX, Clery Act, ADA).
 - Represent institutions in student and employee **litigation**, **government investigations**, administrative proceedings, audits, and reviews.
 - Assist with postsecondary **transactions**, contract drafting and negotiation, policy creation, and compliance systems design.



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About the Presenters

- Craig S. Dean
 - Managing Principal, AEG Partners
- Turnaround Practice
 - With more than 25 years of experience as a financial advisor, corporate executive and **turnaround manager**, Craig has extensive knowledge of the inner workings of business and how to successfully navigate and resolve complex issues.
 - Has worked on a broad spectrum of corporate challenges—from underperforming companies seeking to improve profitability to stressed and **severely distressed** situations.
 - Experience includes working in the distressed **education** arena involving operational, regulatory and accrediting matters. Most recently he served as financial advisor for Vatterott College in St. Louis, guiding the organization through the receivership process. He also has served on corporate boards and in fiduciary trustee positions.



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Presentation Overview

- The Rise of the Distressed Institution
- Restructuring and Bankruptcy
- The Middle Ground: Receivership and ABC
- A Focus on Receiverships in Higher Education

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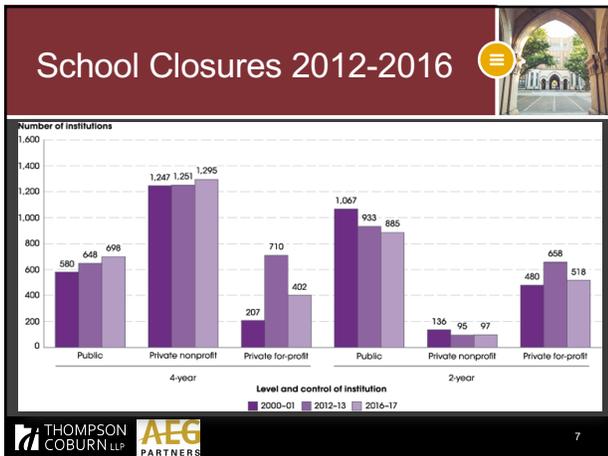
The Rise of the Distressed Institution

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School Closures 2012-2016

- Per **NCES**, between 2000–01 and 2012–13, the number of private for-profit **4-year institutions** more than tripled, from 207 to 710, then declined by more than 40 percent to 402 in 2016–17.
- Between 2000–01 and 2012–13, the number of private for-profit **2-year institutions** increased 37% from 480 to 658, and then declined 21% to 518 in 2016–17.

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School Closures Since 2016

- Education Dive [reports](#) that since 2016:
 - **108** institutions have closed.
 - Of the 108, 66 for-profit, and 41 private, non-profit.
 - **69** institutions have merged, consolidated, or been acquired.
 - Of the 69, 8 for-profit, 24 private, non-profit, and 36 public.
 - Some institutions on this list had many locations and tens of thousands of students (e.g., ITT, ECA).
- **Another 34** institutions are expected to close, merge, consolidate, or be acquired by 2023.

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Looking for Answers

- In recent years, institutions have been faced with a combination of challenges, including:
 - Declining Enrollments
 - Regulatory Actions
 - Regulatory Inconsistency
 - Poor Management
 - Culture Shift
 - Changing Student Demographics
 - International Student decline

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Declining Enrollments



- The biggest factor is economics. The country has pulled out of the Great Recession, and employment is booming.
- Overall enrollment is still well above what it was in 2000, and ED **estimates** that it will increase moderately over the next decade. But the trend is **down**, particularly among career-focused institutions.

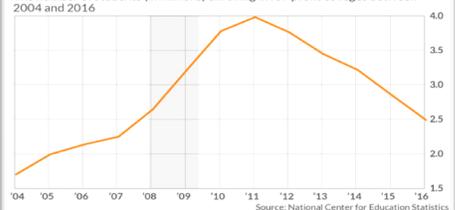


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Declining Enrollments



For-profit college enrollment spiked during the recession
 The number of students (in millions) enrolling in for-profit colleges between 2004 and 2016



Source: National Center for Education Statistics



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Declining Enrollments



- After peaking in 2010, enrollment at **for-profit institutions** decreased by 47% (from 1.7 million to 915,000 students) between 2010 and 2016.
- According to the **National Student Clearinghouse**, enrollment has continued to decline across almost all sectors since 2016, with four-year, for-profit institutions experiencing the most dramatic decline (about **21%**).



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Declining Enrollments

Term Enrollment ESTIMATES FALL 2018

Table 1: Estimated National Enrollment by Sector (Title IV Degree-Granting Institutions)

Sector	FALL 2017		FALL 2017		FALL 2018	
	Enrollment	% Change from Prior Year	Enrollment	% Change from Prior Year	Enrollment	% Change from Prior Year
Total Enrollment, All Sectors	18,482,391	-1.7%	18,811,280	-1.0%	18,010,459	-1.4%
Four-Year Public	8,087,410	0.0%	8,082,105	-0.2%	8,100,118	0.2%
Four-Year Private Nonprofit	3,984,957	2.4%	3,775,147	-0.4%	3,788,980	-0.6%
Four-Year For-Profit	765,696	-15.1%	801,331	-7.1%	970,267	-14.5%
Two-Year Public	5,445,562	-3.2%	5,624,282	-1.7%	5,721,678	-2.6%
Unduplicated Student Headcount (All Sectors)	18,196,846	-1.4%	18,463,677	-1.1%	18,063,617	-1.4%

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Declining Enrollments

- Most institutions are tuition revenue driven. A decline in enrollments must be met with **timely contraction** of expenses.
- This is a significant challenge for higher education, particularly on the traditional side.
 - Moody's 2019 **outlook** for higher education is negative, noting that "increasing expenses outpace constrained revenue for most universities and colleges."
- The failure to timely contract can leave schools with unmanageable debt and mounting expenses.

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Regulatory Actions

- Beginning in 2010, the prior administration led a highly publicized "crackdown" on for-profit schools, utilizing ED, SEC, FTC, DOJ, and CFPB. Aided by Sen. Harkin (D-IA), Sen. Durbin (D-IL), and others in Congress, as well as State Attorney Generals.
 - 2010 undercover GAO investigation; Harkin report; increased and targeted program reviews; revised audit guide; gainful employment rule; borrower defense to repayment rule; hostile cash management actions.
- These efforts damaged industry reputation, depressed enrollments, restricted federal aid flow, and increased costs associated with litigation, agency investigations, and regulatory compliance.

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Regulatory Inconsistency



- Both the prior and current administration have repealed, revised, and created rules and processes (GE, BDR, Title IX), and taken actions that dramatically impact the sector (ACICS).
- Efforts to comply with or accommodate these activities have been, and continue to be, extremely costly to institutions.

Poor Management



- From 2000 to 2010, enrollment at private for-profit institutions increased by **329%** (from 403,000 to 1.7 million students).
 - In comparison, enrollment increased by 30% at public institutions and by 20% at private nonprofit institutions during the same period.
- During any period of explosive growth, **poor managers** will be hired into the space. During a period of stress or decline, poor managers often are unable to lead their departments or institutions successfully.

Culture Shift



- We may be experiencing a culture shift, insofar as postsecondary education is not the imperative it used to be. Alternatives may be more attractive, ranging from apprenticeships, or even “dirty jobs.”
- While this poses a challenge to traditional, degree-granting institutions, it may prove an advantage to more nimble, certificate-focused entities (e.g., coding boot camps).

Changing Demographics



- The number of individuals seeking postsecondary education differs dramatically in various parts of the country.
 - For example, the number of traditional college-age students is falling in New England, which has many colleges, with the result that supply is outpacing demand.
- Such shifts could also be favorable. For example, population growth in both Texas and North Carolina has been relatively strong in recent years.

International Student Decline



- International students are on the decrease. According to the Institute of International Education, enrollments of international students fell by 6.6 percent at American universities in academic year 2017-18 compared to the year before, marking the second straight year in declines in new enrollments.
- This has a greater impact than other students, as foreign student tuition revenue is used to subsidize the cost of domestic students.

Restructuring and Bankruptcy



The Restructuring Alternative

- **Out-of-court** restructuring can assist schools that are underperforming, in a crisis, or are healthy, but with underperforming elements.
 - Can take many forms, from the most basic review of costs and expenses to a full blown balance sheet and operational overhaul.
 - Can help to stabilize financial and operational performance by developing and implementing comprehensive profitability and working capital plans.



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The Restructuring Alternative

- Examples of out-of-court restructuring efforts can include:
 - Long-term business plan development and implementation
 - Business reviews
 - Operational restructuring
 - Contingency planning
 - Debt reorganization and financial restructuring
 - Capital raising
 - Liquidity and business stabilization
 - Management of sales of non-core assets
 - Restructuring planning and implementation



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The Restructuring Alternative

- Unfortunately, as a whole, the education sector has been **slow to embrace** restructuring as a response to institutional stress. Possible explanations include:
 - Stigma of failure that does not exist in other sectors;
 - Public service nature of industry creates conflict between "mission" and creditor protections; and
 - Widespread view that all institutions will suffer equally in a highly regulated industry inhibits active financial management.



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Bankruptcy and the Title IV Dilemma

- Congress amended the Higher Education Act in 1992 to, among other things, permanently strip any institution of its Title IV eligibility if it filed for bankruptcy protection.
 - Amendment was intended to eliminate the use of the bankruptcy laws, namely the automatic stay, in order to escape action by the Dept. of Education against an unscrupulous institution.
- Prohibition is echoed in the regulations, which specify that an educational institution loses Title IV Program eligibility if either the institution or the company that controls the institution files for relief in bankruptcy or is ordered into bankruptcy.

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Bankruptcy and the Title IV Dilemma

- Courts have upheld USED's ability to strip an institution of Title IV funding upon the filing of a bankruptcy.
 - In re Betty Owen Schools, Inc. (Bankr. S.D.N.Y.) – Bankruptcy Court upheld Dept. of Ed.'s ruling refusing to allow new owner that purchased substantially all of the debtor's assets in bankruptcy to immediately reapply for Title IV funding.
 - In re Lon Morris College (Bankr. E.D. Tex.) - Bankruptcy Court upheld Dept. of Ed.'s ruling stripping Lon Morris College's Title IV status upon commencement of its chapter 11 case.

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Bankruptcy and the Title IV Dilemma

- When statute was passed, Congress likely didn't anticipate the ever increasing need for a restructuring alternative for a significant percentage of highly reputable and publicly significant institutions.
- The threat of a bankruptcy filing is often the only governor in creditor negotiations to a creditor strategy to dismantle the institutions.
- The time is ripe for Congress to reconsider the outright ban, or for USED to consider creative alternatives.

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Benefits of Chapter 11



- The Debtor's ability to reject leases and cap lessor damages to statutory cap.
- The Debtor's ability to capitalize an under-market leases by assigning leases to better use notwithstanding lease prohibits.
- The ability to re-characterize sale leasebacks into secure financings in order to stretch out payments.
- The **automatic stay** of all litigation, pre-petition obligations, and creation of a beneficial forum to resolve or estimate all litigation in an expedited timeframe.

What do these have in common?



- Marvel Entertainment
- Schwinn Bicycle Company
- General Motors
- Chrysler
- Delta
- American Airlines
- Converse
- The New England Patriots
- Eddie Bauer
- Six Flags

The Middle Ground: Receivership and the ABC



Receivership



- State or federal
- Purpose to facilitate restructuring, sale or teach-out (or some combination)
 - A process that will avoid Title IV de-funding and the loss of accreditation
- Company placed under court's protection while settles financial affairs
- Court appoints Receiver, whose role is to
 - Take possession of the property and other assets
 - Oversee management an operation of the company
 - Facilitate resolution of disputes.



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Receivership Issues



- Appointment of Receiver
 - Typically sought by creditor with liens against the school's assets.
 - > Neutral, third party to manage assets and maximize recoveries.
 - > Replace the management team.
 - In recent education cases, however, appointment of the receiver has been requested by the school itself
 - > Discretion of the court.
 - > Management remains in place.
- Advance preparation with key constituents essential
 - **DOE** – to allow access to Title IV funds, assurance that school is **not attempting to avoid teach out liabilities**.
 - **Accreditor** – assurance that school is going to **maintain operations consistent with accrediting standards**.
 - **State Regulators**



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Receivership Pros / Cons



- Pro
 - Automatic stay – trade creditors / litigation
 - Ability to reject leases.
 - Less stringent procedural requirements and fewer constituencies than other in-court options (Chapter 11), so more cost effective.
 - Less transparent / publicity verses a bankruptcy filing.
- Con
 - Not a solution for a negative cash flow school
 - Inconsistent state laws
 - Risk that creditors can force a Chapter 11 or 7



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State vs. Federal Receivership




- State
 - Works well if most operator's schools concentrated in one state (lease / contract rejections)
 - Could do multiple state filings, but costly.
 - Receivership provisions vary greatly by state, so not always an option
- Federal
 - Most applicable if school operates in multiple states
 - Likely higher standard for court to approve.



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Assignment for the Benefit of Creditors ("ABC")




- ABCs function under state law
 - Similar to Receiverships, state provisions vary widely including the amount of court oversight.
- Process -- assets legally transferred to an "Assignee"
 - Appointed by company
 - Charged with marshalling and selling assets and / or business.
- Issues
 - Does not discharge debts (vs bankruptcy)
 - No automatic stay against collection actions or lawsuits
 - Time issues in education regulatory environment
- Works best for smaller school located within a single state



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A Focus on Receiverships in Higher Education







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The Case Studies

- Myers University (2007)
 - State receivership
- Vatterott Educational Centers, Inc. (2017)
 - State receivership
- Education Corporation of America (2018)
 - Federal receivership
- Dream Center Education Holdings (2019)
 - Federal receivership

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One Size Does Not Fit All

- Not all receiverships are the same.
 - Myers University successfully achieved a sale and when it ultimately closed five years later, did so in an orderly fashion.
 - Vatterott remained open and stable for 18 months, taught-out multiple campuses, and graduated thousands of students while operating inside a state receivership.
 - Virginia College and Argosy University both closed within two months of being placed in receiverships.
- We suggest that receiverships should be examined and managed closely on a case-by-case basis. Avoid one-size-fits-all policies.

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Objectives Vary

- Receiverships can facilitate restructuring, sale or merger, or simply afford a vehicle for a more orderly closure.
- Receiverships also may have different value in different jurisdictions.
 - For MA, ECA receivership may successfully serve as path to survival for NECB
- We suggest that regulators require that institutions provide very clear objectives and timetables for the institutions under their jurisdiction.

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Circumstances Can Change Rapidly



- We strongly suggests that regulators be aware of, and prepare for, the possibility of rapid, material change.
 - Landlords and other creditors may not cooperate (e.g., involuntary bankruptcy).
 - Receivership judge may not be cooperative (e.g., discontinue a litigation stay)
 - States outside of jurisdiction may not honor receivership protections
 - Negative regulatory action (e.g., USED places institution on HCM-2).

Changed Circumstances Can Lead to Rapid Closure



- Receiverships are delicate and such changes can have immediate and severe consequences.
 - Teach-out plans submitted in good faith can be rendered useless.
 - Changed economics can dictate a precipitous closure.
- Consider requesting contingency plans that account for different scenarios.

Agency Interests May Not Align



- We encourage members of the triad to coordinate closely, and where interests do not align, to voice concerns.
- If there is a lack of coordination and communication among the triad, a single regulator can take action that may undermine the interests of another.

TC Resources





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Higher Ed Webinar Series




2018/2019 Series Calendar	
August 2018	Student Litigation
September 2018	Mergers and Acquisitions in Higher Education
October 2018	Higher Ed and the November Elections
November 2018	USED's Proposed Title IX Rules: A Detailed Examination
January 2019	Fair Debt Collection Practices Act & Student Loan Servicing
February 2019	The Road from the Final Four
March 2019	Intellectual Property Primer for Institutions
April 2019	First Amendment Trends in Higher Ed
May 2019	Charitable Planning Update

 If you would like to register for our webinars, email irosey@thompsoncoburn.com and we will send you a link as we open each webinar for registration.



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Aaron Lacey is the host of our higher education webinar series, as well as a frequent presenter. Aaron's practice is dedicated entirely to helping institutions of higher education navigate complex legal and regulatory matters. With time spent both in practice and in-house counsel, Aaron has significant experience in the areas of law, ethics, and accreditation agency rules and standards that govern postsecondary institutions. He is frequent writer and speaker on topics relating to higher education policy and its funding, financial aid programs, and is also the editorial director of *REGULATION*, the firm's higher education law and policy blog.



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Webinars on Demand




TCLE(90)		
<p>USED's Proposed Title IX Rules: A Detailed Examination</p> <p>November 29, 2018 Register</p>	<p>Don't Get Spooked! What the Midterms Mean for Higher Education</p> <p>October 31, 2018</p>	<p>Planning Using the Proposed Regulations under IRC §§ 199A and 643(f)</p> <p>October 30, 2018 View Recording</p>
<p>Mergers and Acquisitions in Higher Education: Key Points of the Letter of Intent</p> <p>September 12, 2018 View Recording</p>	<p>Minimizing Litigation Risk As To Student-Related Disputes</p> <p>August 28, 2018 View Recording</p>	<p>Notice of Proposed Rulemaking on Borrower Defense</p> <p>August 14, 2018 View Recording</p>
<p>The Dodd Frank Rollback: Easing the Rules for Commercial Real Estate (HVCRE) Lending</p> <p>August 2, 2018 View Recording</p>	<p>Cahill 2036, 2038, 2703: Mazzei Disregards Corporate Arrangements, Investment Partnership Traps</p> <p>July 31, 2018 View Recording</p>	<p>Midcourse Conflicts</p> <p>June 27, 2018 View Recording</p>
<p>Client Identification</p>	<p>Properly Extending Credit for Private Education Students</p>	<p>Partnership Audit Rules: Effects on Tax-Professors, Litig...</p>



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Trouble afoot: Duke's 'Shoe-gate' highlights current controversies in college basketball
 ■ [Ira Wadew, A.](#) ■ [March 8, 2019](#)



In the recent UNC v. Duke basketball game, Zion Williamson's injury set off a firestorm of discussion around a "one-and-done" system that put his lucrative pro career in jeopardy so he could take the court for a university that may never hand him a diploma. [READ MORE](#)

USED's proposed Title IX rules: Complimentary webinar now available on-demand
 ■ [Aaron Lacey](#) ■ [December 12, 2018](#)



On November 29, Aaron Lacey presented a webinar examining the U.S. Department of Education's proposed Title IX rules in significant detail. These proposed rules, if implemented, will constitute the first significant revision of the Department's Title IX regulations in over 40 years. [READ MORE](#)

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