INTRODUCTION:

On October 29, 2010, the U.S. Department of Education ("ED") published final regulations on 14 topics relating to the integrity of federal student financial aid programs under Title IV of the Higher Education Act of 1965, as amended. [1] The new rules address program integrity in five areas: institutional eligibility to participate in Title IV programs, recruiting and admissions, eligibility of particular educational programs for Title IV assistance, eligibility of students to receive Title IV assistance, and Title IV aid disbursements and refunds. ED has since issued several “Dear Colleague” Letters to provide guidance concerning these new rules, which go into effect on July 1, 2011.

On June 13, 2011, ED published further final regulations on the program eligibility topic of “gainful employment.” [2] Those regulations, which establish metrics for determining whether certain educational programs lead to “gainful employment in a recognized occupation,” go into effect on July 1, 2012.

Although largely directed toward for-profit postsecondary education institutions, [3] these new rules have significant implications for nonprofit and public higher education institutions as well. This NACUA NOTE is the first in a three-part series of Notes that will summarize selected aspects of these complex, and sometimes confusing, new rules. Part I addresses the issues of state authorization, incentive payments, and misrepresentation. Part II will address the new federal definition of credit hours, as well as ED’s new disclosure and reporting requirements. [4] A final Note will cover gainful employment program requirements in more detail. As the July 1, 2011 implementation deadline approaches, these Notes are intended to provide an easily accessible review of key compliance obligations and answers to frequently asked questions related to the new rules. For more detailed discussion, readers are encouraged to visit NACUA’s online resources on the program integrity rules. [5]

DISCUSSION:

State Authorization

In order to be eligible to participate in the Title IV programs, an institution must be legally authorized to provide an educational program beyond secondary education in the state in which the institution is physically located. [6] Current regulations do not define what constitutes sufficient state authorization for purposes of compliance with that requirement. The new program integrity regulations address this by establishing rules about the type of state action that is required in order for an institution to be
authorized properly for Title IV purposes.

**What constitutes sufficient state authorization under the new rule?**

Under the final rule, in order to meet the “legally authorized” requirement, state authorization must satisfy new requirements. First, the state in which the institution is located must have a process to review and take appropriate action on complaints concerning postsecondary educational institutions, including enforcing applicable state laws. [7] Second, the institution must fall within one of the following categories with respect to any state in which it is located:

- The institution is established as an educational institution by charter, statute, constitutional provision or other action issued by an appropriate state agency or state entity that identifies the institution by name and affirms or conveys to the institution the authority to operate educational programs beyond secondary education, including programs leading to a degree or certificate. The institution must comply with any applicable state approval or licensure requirements, but the state may exempt such institution from any approval and licensure requirements based on the institution's accreditation by an ED-recognized accreditor or based on the institution being in operation for at least 20 years. [8]
- The institution is authorized to conduct business or operate as a nonprofit charitable organization, is approved or licensed by name by the state to offer programs beyond secondary education, including programs leading to a degree or certificate, and is not exempt from state approval or licensure requirements based on accreditation, years in operation, or other comparable exemption. [9]
- The institution is authorized by name by the federal government to offer postsecondary education (e.g., service academies). [10]
- The institution is authorized by name by an Indian tribe to offer postsecondary education, provided the institution is located on tribal lands and the tribal government has a process to review and act appropriately on complaints concerning an institution and enforces applicable tribal requirements and laws. [11]
- The institution is exempt from state authorization requirements as a religious institution under state constitution or law, provided the institution is owned, controlled, operated and maintained by a religious organization lawfully operating as a nonprofit religious corporation and awards only religious degrees or certificates. [12]

**If an institution is exempt from state approval or licensure requirements and exemption is permissible for purposes of the new state authorization requirement, must the institution be exempted by name?**

As indicated above, certain institutions may be exempted from state approval or licensure requirements and nevertheless be legally authorized for Title IV purposes. However, ED has indicated that the requirement that the institution be named in any state action related to its authorization also applies to any exemption. [13]

**Does the new state authorization rule require that a particular agency be responsible for complaints regarding institutions?**

A state must have a process to handle complaints regarding all institutions in the state, except federally run institutions and tribal institutions. ED has clarified that the regulation does not require that a single agency be responsible for all complaints, nor does it require that agencies with particular expertise be responsible for complaints. ED also has advised that a state may rely on a governing board or central office of a state-wide public institution system to handle complaints regarding system institutions if the state has determined that the board or central office is sufficiently independent. [14]
Does the new state authorization requirement apply to distance or correspondence education?

If an institution offers postsecondary distance or correspondence education to students in a state in which the institution is not physically located or in which the institution is otherwise subject to state jurisdiction, the institution must meet any requirements for the institution to be legally offering postsecondary distance or correspondence education in that state. [15] The institution must be able to document state approval for distance education if requested by ED. [16] ED has indicated that if no approval or licensure is required, the institution is not required to have a document from the state that indicates that no approval is required, but the institution must be able to demonstrate upon request that no approval is required. [17]

Does ED plan to publish state-by-state information on state authorization requirements?

ED has indicated its commitment to work with appropriate parties to develop a comprehensive directory of state requirements, and it plans to make any final directory available on its website. [18] The State Higher Education Executive Officers (“SHEEO”), the national association of state higher education executive officers, is in the process of developing a directory of agencies and individuals responsible for implementing state quality assurance laws as well as a compendium of state laws and regulations. [19]

By when must an institution comply with the state authorization requirements?

The new state authorization requirements are effective July 1, 2011. [20] Institutions that are unable to comply with the state authorization requirements, other than those applicable to distance and correspondence education, may request a one-year extension of the effective date to July 1, 2012, and if necessary, an additional one-year extension to July 1, 2013. [21] To receive an extension, an institution must obtain an explanation from the state of how a one-year extension will permit the state to modify its procedures to comply with the new requirements. [22] ED has provided no mechanism for extension of the effective date of the state authorization requirements applicable to distance and correspondence education. However, ED has indicated that it will not initiate any action to establish repayment liabilities or limit student eligibility for distance education activities undertaken before July 1, 2014, provided the institution is making good faith efforts to identify and obtain necessary state authorization before that date. [23] According to ED’s April 20 “Dear Colleague” Letter (amended May 6), a good faith effort could include any one or more of the following: documentation that an institution is developing a distance education management process; documentation that an institution has contacted a state directly to discuss matters pertinent to determining whether authorization is required; an application to a state; and documentation from a state that an application is pending. [24] Although the language in the “Dear Colleague” Letter seems to indicate that only one of these steps might be sufficient to demonstrate good faith, pursuing multiple steps would provide greater evidence of good faith efforts. By contrast, evidence of bad faith would include documents that show the institution knew of a state requirement and willfully refused to comply with it. [25]

What steps should an institution be taking to comply with the new state authorization requirements by July 1?

An institution should evaluate its formation documents and its status under state postsecondary education approval and licensure laws to determine whether it has sufficient state authorization for Title IV purposes. If not, the institution should determine what action is required to bring the institution into compliance and, if necessary, take steps to obtain appropriate documentation from the state to enable the institution to seek an extension of the effective date. In addition, an institution should identify its distance education programs, if any, and the states in which students in those programs reside. It should establish a distance education management process to track initiation of
distance education programs and residence of distance education students. The institution should determine whether it is required to obtain approval from states where its distance education students reside and, if so, it should pursue promptly obtaining any required approvals.

**Incentive Payment**

The Higher Education Act ("HEA") generally prohibits institutions from providing any commission, bonus, or other incentive payment based directly or indirectly on success in securing enrollments or financial aid to any person or entity engaged in any student recruiting or admission activities or in making decisions regarding the award of student financial assistance. [26] The HEA exempts from the incentive payment ban “the recruitment of foreign students residing in foreign countries who are not eligible to receive Federal student assistance.” [27] The new incentive payment rule reflects that exception. [28]

In 2002, ED adopted 12 “safe harbors” to define circumstances in which an institution would not violate the incentive payment rule. [29] The new incentive payment rule abolishes those safe harbors and adopts a broad interpretation of the incentive payment ban.

**Which employees are covered by the incentive payment ban?**

The new incentive payment rule applies to “any person . . . who is engaged in any student recruitment or admission activity, or in making decisions regarding the award of title IV, HEA program funds.” [30] Such employees include “any employee who undertakes recruiting or admitting of students or who makes decisions about and awards title IV, HEA program funds, and any higher level employee with responsibility for recruitment or admission of students, or making decisions about awarding title IV, HEA program funds.” [31] ED has provided some guidance concerning the types of activities that are and are not within the scope of the regulation. [32] In particular, ED has clarified that “[s]enior managers and executive level employees who are only involved in the development of policy and do not engage in individual student contact or the other covered activities . . . will not generally be subject to the incentive compensation ban.” [33]

**What types of compensation for employees does the incentive payment ban cover?**

The new incentive payment rule prohibits “any commission, bonus, or other incentive payment based in any part, directly or indirectly, upon success in securing enrollments or the award of financial aid” to any covered employee. [34] ED defines “[c]ommission, bonus, or other incentive payment” broadly to include “a sum of money or something of value, other than a fixed salary or wages, paid to or given to a person or an entity for services rendered.” [35] The rule generally prohibits multiple adjustments to compensation in a calendar year for covered employees, [36] but permits (1) ”[m]erit-based adjustments” not based in any part, directly or indirectly, upon success in securing enrollments or the award of financial aid and (2) “[p]rofit-sharing payments” as long as the institution does not provide such payments to covered employees. [37] ED has clarified that the general prohibition on profit-sharing payments to covered employees does not prohibit them from participating in 401(k) or other employee benefit plans that are “neutral with respect to the role the recipient plays in student recruitment or the securing of financial aid.” [38] ED has also advised that cost-of-living adjustments are permissible. [39]

**What type of payments to employees are based on “success in securing enrollments or the award of financial aid”?**

The new incentive payment rule defines ”[s]ecuring enrollments or the award of financial aid” expansively to cover “activities that a person or entity engages in at any point in time through completion of an educational program for the purpose of the admission or matriculation of students
for any period of time or the award of financial aid to students.” [40] Such activities include “contact in any form with a prospective student, such as, but not limited to – contact through preadmission or advising activities, scheduling an appointment to visit the enrollment office or any other office of the institution, attendance at such an appointment, or involvement in a prospective student’s signing of an enrollment agreement or financial aid application.” [41]

**What criteria may an institution use to make compensation decisions with respect to covered employees?**

ED has advised that institutions may use as a basis for compensating covered employees (1) seniority or length of service [42] and (2) qualitative considerations such as job knowledge and professionalism, skills such as analytic ability, initiative in work improvement, clarity in communications, and use and understanding of technology, and traits such as accuracy, thoroughness, dependability, punctuality, adaptability, peer rankings, student evaluations, and interpersonal relations – provided that such considerations “are not related to the employee’s success in securing enrollments or the award of financial aid.” [43] Institutions may also have “salary scales that reflect an added amount of responsibility” in certain circumstances. [44]

**Does the new incentive payment rule affect compensation of athletic coaches?**

Although coaches may be covered employees, ED has stated that it does not consider “‘bonus’ payments made to coaching staff or other athletic department personnel to be prohibited if they are rewarding performance other than securing enrollment or awarding financial aid, such as a successful athletic season, team academic performance, or other measures of a successful team.” [45]

**What service providers are covered by the incentive payment ban?**

The new incentive payment rule covers any entity that “is engaged in any student recruiting or admission activity, or in making decisions regarding the award of title IV, HEA program funds.” [46] ED’s guidance concerning the types of activities that are and are not within the scope of the regulation apply to service providers as well as employees. [47]

**What types of compensation arrangements for covered service providers are permissible under the incentive payment rule?**

The new incentive payment rule permits payments to covered third parties “for the provision of student contact information for prospective students” in certain circumstances. [48] An institution may not base such payments on “[a]ny additional conduct or action by the third party or the prospective students, such as participation in preadmission or advising activities, scheduling an appointment to visit the enrollment office or any other office of the institution or attendance at such an appointment, or the signing, or being involved in the signing, of a prospective student’s enrollment agreement or financial aid application.” [49] In addition, an institution may not base such payments on “[t]he number of students (calculated at any point in time of an educational program) who apply for enrollment, are awarded financial aid, or are enrolled for any period of time, including through completion of an educational program.” [50]

**Does the new incentive payment rule prohibit tuition-sharing arrangements with service providers?**

ED has advised that it “generally views the payment based on the amount of tuition generated as an indirect payment of compensation based on success in recruitment and therefore a prohibited basis upon which to measure the value of the services provided.” [51] ED will permit such payments,
however, if:

- “the institution determines the number of enrollments,“
- the service provider is unaffiliated with the customer institution and any other “institution that provides educational services,”
- provides “bundled services that include recruitment,” and
- “does not make prohibited compensation payments to its employees”; and
- “the institution does not pay the entity separately for student recruitment services.” [52]

**What steps should an institution be taking to comply with the new incentive payment rule by July 1?**

Institutions should identify their covered employees, evaluate whether their compensation arrangements comport with the new incentive payment rule, and to the extent that they do not, make necessary modifications to comply. Similarly, institutions should identify their covered service providers, evaluate whether the contract pricing structure is consistent with the new incentive payment rule, and if not, determine whether the institution has rights under the contract to renegotiate the price, terminate the agreement, or invoke a dispute resolution procedure.

**Misrepresentation**

The HEA permits ED to suspend or terminate from participation in Title IV programs an institution that engages in “substantial misrepresentation of the nature of its educational program, its financial charges, or the employability of its graduates.” [53] ED’s new regulation on misrepresentation defines more broadly the nature of such misrepresentations and expands the sanctions that ED may impose for substantial misrepresentations. [54]

**What types of statements does the misrepresentation rule prohibit?**

The new misrepresentation rule makes the institution responsible for substantial misrepresentations by the institution itself, a representative of the institution, or any person or entity with whom the institution has an agreement to provide educational programs, marketing, advertising, recruiting or admissions services. [55] The rule prohibits substantial misrepresentations “in all forms, including those made in any advertising, promotional materials, or in the marketing or sale of courses or programs of instruction offered by the institution.” [56] The rule contains lengthy examples of misrepresentations relating to the nature of an educational program, [57] the nature of an institution’s financial charges, [58] and the employability of graduates. [59] The new misrepresentation rule does not apply to statements by students through social media outlets or by vendors that are not providing covered services. [60]

**What does ED mean by “substantial misrepresentation”?**

ED defines “misrepresentation” broadly to include “[a]ny false, erroneous or misleading statement” that the institution, a representative of the institution, or a covered service provider makes “directly or indirectly” to a student, prospective student, a member of the public, an accrediting agency, a state agency, or ED. [61] “A misleading statement includes any statement that has the likelihood or tendency to deceive or confuse.” [62] If a person to whom the misrepresentation was made “could reasonably be expected to rely, or has reasonably relied,” on the misrepresentation, the misrepresentation would be “substantial.” [63]

**What sanctions can ED impose on an institution that violates the new misrepresentation...**
In the event of a substantial misrepresentation, the new misrepresentation rule authorizes ED to deny applications by the institution, for example, to add locations or programs; initiate proceedings to fine an institution or limit, suspend, or terminate its participation in Title IV programs; or revoke a provisionally certified institution’s participation in Title IV programs. [64]

What steps can an institution take to ensure that its employees and contractors are accurately describing the institution to prospective students and others?

Institutions should regularly review their websites and other informational materials for accuracy and completeness. Institutions should train their employees and the employees of any vendors providing covered services concerning the institution’s educational programs, financial charges, and employment of graduates. Institutions should monitor from time to time employees’ and vendors’ communications with prospective students and members of the public and take corrective action where needed.

CONCLUSION:

ED’s final rules on program integrity have extensive implications for institutional operations. Securing all required state authorizations and ensuring that an institution does not run afoul of ED’s broadened bans on incentive compensation and misrepresentation are first steps in complying with the new rules. But as Parts II and III of this series will address, those obligations are not the end of the story. Among other things, ED’s new rules will require institutions to comply with a new federal definition of the credit hour and to satisfy a number of new disclosure and reporting requirements. Moreover, “gainful employment” regulations will require institutions to meet certain minimum standards with respect to programs that are required to lead to gainful employment in a recognized occupation in order for students in the program to receive federal student financial aid. While the new regulations are complex and broad in scope, this NACUANOTE series should serve as a starting point for institutions to identify and review their new compliance obligations.

FOOTNOTES

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RESOURCES:

- NACUA State Authorization Rule Resource Page
- State Higher Education Executive Officers, State Authorization Resources and Directory
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