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# UPDATE: The State Authorization, Incentive Compensation & Misrepresentation Program Integrity Rules

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# State Authorization

- “State Authorization” is a core component of the definition of “proprietary institution of higher education” (34 C.F.R. § 600.5):

*(a) A proprietary institution of higher education is an educational institution that—*

*(4) Is legally authorized to provide an educational program beyond secondary education in the State in which the institution is physically located;*

- Historically, the Department of Education (“ED”) had viewed an institution as authorized for purposes of Title IV if the State in which the institution was physically located did not require licensure or authorization to operate in the State.

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# State Authorization

ED's Final Rule for Program Integrity Issues published October 29, 2010 (75 FR 66946) added the following to 600.5(a)(4):

*(a) A proprietary institution of higher education is an educational institution that—*

*(4) Is legally authorized to provide an educational program beyond secondary education in the State in which the institution is physically located in accordance with § 600.9*

# What is State Authorization under § 600.9?

There are 4 categories of state authorization:

- # 1: Institution is public, private nonprofit, or for-profit institution established by name by a State through a charter, statute, or other action issued by an appropriate State agency or State entity as an educational institution authorized to operate educational programs beyond secondary education, including programs leading to a degree or certificate.
  - Such an institution must comply with any applicable State approval or licensure process and be approved or licensed by name; may be exempted from such requirement based on its accreditation, or being in operation at least 20 years.
  - DCL GEN-11-05: A letter from the State acknowledging the institution is not sufficient “other action”.
  - DCL GEN-11-05: Institution must be authorized by all pertinent State agencies, which may extend beyond State educational agency.

# What is State Authorization under § 600.9?

- **#2: Institution is established by State on the basis of an authorization to conduct business in the State, or to operate as a nonprofit charitable organization, but not established by name as an educational institution.**
  - State must have an approval or licensure process, and the institution must comply with that approval or licensure process and be approved or licensed by name.
  - Such an institution may not be exempted from State approval or licensure based on accreditation, years in operation, or a comparable exemption.
  - DCL GEN-11-05: Articles of incorporation are not sufficient unless specific to the establishment of a postsecondary institution by name under state law (i.e., not necessarily the same form of articles as for other businesses or nonprofit entities in the State)

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# What is State Authorization under § 600.9?

- **#3: Authorized to operate by Federal or tribal governments:**
  - Includes Congressionally-chartered colleges and universities, military service academies.
  - Tribal colleges and universities, provided the tribal government has a process to review and act upon complaints.
  
- **#4: Exemption for religious institutions:**
  - Owned, controlled, operated, and maintained by a religious organization lawfully operating as a nonprofit religious corporation; and
  - Awarding only religious degrees or certificates.

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# What is State Authorization under § 600.9?

- All types of institutions authorized by a State must be subject to a process whereby the State reviews and addresses complaints directly or through referrals.
  - DCL GEN-11-05: Applicable State laws can include general consumer protection and fair-advertising laws. Delegation permitted, but final authority must remain with State.
  - DCL GEN-11-05: If multiple agencies are applicable to an institution, the institution must provide students and prospective students with contact information for filing complaints for all relevant agencies (e.g., nursing and cosmetology boards).

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# What is State Authorization under § 600.9?

- **Requirements took effect July 1, 2011**
  - For physical campus locations, two one-year extensions are possible if an institution obtains from its state an explanation of how extension(s) will permit the State to modify its procedures to permit compliance.
  - Second year of extension ends July 1, 2013, and after that date ALL institutions of higher education receiving Title IV funds are subject to the state authorization rule. See GEN-13-04 (January 23, 2013)

# Distance Education under § 600.9(c)

- If an institution is offering programs through distance or correspondence education to students in a State in which it is not physically located or in which it is otherwise subject to State jurisdiction *as determined by the State*, the institution must meet any State requirements for it to be legally offering postsecondary distance or correspondence education in that State.
  - An institution must be able to document to ED the State's approval upon request.
  - Regulation shifts focus, for distance education purposes, from where the institution is physically located to where students reside.
  - State requirements in this area can turn on how the state defines “doing business,” “offering educational programs” or “distance education.”

# Distance Education under § 600.9(c)

## ■ Dear Colleague Letters

### □ DCL GEN-11-05

- While the location of a student is initially determined at the time of enrollment, the student's eligibility under the state authorization requirement must be reevaluated before each new award to the student.
- There is no Federal minimum number of enrollments to trigger the Title IV requirements.

### □ DCL GEN-11-11

- ED will not initiate enforcement actions to establish liabilities for “distance education activities undertaken before July 1, 2014 if the institution is making *good faith efforts to identify and obtain necessary State authorizations before that date.*”
- ED will review carefully instances where institution is not acting in good faith, such as willfully refusing to comply with a State requirement for licensure.

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# Distance Education under § 600.9(c)

- Examples of “good faith efforts” from DCL GEN-11-11:
  - Documentation of a distance education management process for tracking students’ place of residence.
  - Documentation of correspondence with a State to discuss programs the institution is providing to students in that State.
  - An application to a State, even if it is not yet approved.
  - Documentation from a State that an application is pending.
  - ED has indicated that the above documentation need not be submitted to ED directly and can be kept in the school’s files in the event ED asks for it.

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# Distance Education under § 600.9(c)

- Department initially stated in DCL GEN-11-05 that it would not publish any list of State requirements for distance education.
- Department reversed position in DCL GEN-11-11 and stated it would develop a comprehensive directory of State requirements.

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# State Authorization

## Issues and Challenges

- How does an institution know which States will deem its distance education activities to require licensure?
  - Identify the institution's activities in each State, including but not limited to:
    - Student enrollments
    - Admissions activities and call centers
    - Advertising activities
    - Faculty presence
    - Computer servers
    - Participation at events
    - Externships

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# State Authorization

## What is a school to do? cont'd.

- **Distance education**
  - Take an inventory of which States you have students, admissions reps or call centers, advertising, faculty, etc.
  - Determine what States are meaningful, you may not want to operate in all 50 States due to the regulatory burden and cost.
  - Find an initial source/survey of state specific information until the Department releases a list to help understand individual State requirements (e.g. State Higher Education Executive Officers - [www.sheeo.org](http://www.sheeo.org)).
  - Reaching out to top states where you have students .
  - May need to terminate faculty, change programs by removing externship requirements in order to qualify for exemptions or may need to teach out students.
  
- **Develop a process to stay current**
  - State laws and requirements are changing, and will continue to do so.

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# State Authorization

## Issues and Challenges

- **When are Articles of Incorporation sufficient?**
  - An institution is legally authorized by a state if it is ”established by name as an educational institution through means such as a charter or state statute and is authorized by the applicable state agency to operate postsecondary education programs.” 34 CFR 600.9(a)(1)(i)(A).
  - DCL GEN-12-13 agreed that Articles of Incorporation may be sufficient if they establish an institution “by name” as an “educational institution.”
  - In some cases where an institution is Licensed By Means of Accreditation, amendments to the Articles may be necessary.
  
- **State Authorization Reciprocity Agreement (SARA)**
  - Lumina Foundation/Council of State Governments.
  - Draft model reciprocity agreement released April 2012: would give principal oversight responsibility to home state of school.
  - Full implementation will require individual state legislatures to act.

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# Incentive Compensation

- Compensation of any kind to recruiting, admissions, and financial aid employees and entities.
- Existing regulations substantially changed.
- New restrictions on incentives and compensation of any kind.
- Covered parties expanded (“to the top”).
- New rules on payments to third parties.

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# Incentive Compensation

Under New Regs, 12 “safe harbors” **eliminated** --

Institution agrees that it will not provide **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.

Applies to persons engaged in **any** student recruitment or admission activity or in making decisions about the award of financial aid, **any** employee who undertakes recruiting or admitting of students or who makes decisions about and awards title IV funds, and **any** higher level employee with responsibility for recruitment or admission of students, or making decisions about awarding title IV funds.

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# Incentive Compensation

- 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.
- Multiple pay adjustments of a covered employee is prima facie evidence of an improper payment.

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# Incentive Compensation

## The Preamble

### ED's two part test:

Is it a Commission, Bonus, or Incentive Payment – AND--

Is it paid based in any part, directly or indirectly, on success in securing enrollments or the award of financial aid

Salary increase based on merit, seniority, or length of employment allowed *subject to the new rule.*

Can apply **“to the top”** of the institution (i.e. Senior Management).

ED's reasoning: “senior management may drive the organizational and operational culture at an institution, creating pressures for top, and even middle, management to secure increasing numbers of enrollments from their recruiters.” 75 Fed. Reg. 34818.

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# Incentive Compensation

GEN-11-05:

Q: What “**standard evaluative factors**” other than seniority may an institution take into account in determining compensation of employees?

A: any qualitative factor not related to success in securing student enrollments or award of financial aid. e.g., job knowledge, professionalism, analytic ability, initiative in work improvement, clarity in communications, use & understanding of technology, accuracy, thoroughness, dependability, punctuality, adaptability, peer rankings, student evaluations, and interpersonal relations.

**BEWARE:** Despite ED’s guidance on evaluative factors, ED has indicated that it will take action when it perceives that non-enrollment criteria is being used to disguise enrollment-based criteria. (“Disguise”, “Pretext”, “Sham”).

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# Incentive Compensation

## ISSUES & CHALLENGES

- FY 2013 OIG Work Plan
  - Includes incentive compensation regulation compliance as a priority compliance initiative of OIG.

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# Misrepresentation Rule

- The HEA allows ED to suspend or terminate an institution from participation in Title IV Programs for “substantial misrepresentation” that may be made in three general areas:
  - **The nature of its educational program**
  - **Its financial charges; and**
  - **Employability of its graduates.**

A misrepresentation is **substantial** if the person to whom the statement was made “could reasonably be expected to rely, or has reasonably relied,” on the statement to that person’s detriment. No actual harm is required.

34 C.F.R. §§ 668.71-75.

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# Misrepresentation Defined

Any **false, erroneous or misleading** statement an eligible institution, one of its representatives, or any ineligible institution, organization, or person with whom the eligible institution has an agreement to provide educational programs, or to provide marketing, advertising, recruiting or admissions services makes **directly or indirectly** to a student, prospective student or any member of the public, or to an accrediting agency, to a State agency, or to the Secretary.

34 C.F.R. § 668.71(c).

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# Misrepresentation Defined

A misleading statement includes any statement that has the **likelihood or tendency to deceive or confuse**.

Note: *APSCU v. Duncan* stated that the rule does not prohibit “merely confusing statements.”

A **statement** is any communication made in writing, visually, orally, or through other means.

34 C.F.R. § 668.71(c).

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# Misrepresentation

**“Mislead”** – likelihood or tendency to deceive or confuse.

**How?** Statements made in writing, visually, orally, or through other means.

**By Whom?** Made by representatives, agents, vendors, as well as marketing, advertising, recruiting, and admissions services.

**To Whom?** Made *directly or indirectly* to students, prospective students, accrediting agency, State agency, Secretary, or any member of the public.

# Dear Colleague Letter

- ED has issued sub-regulatory guidance regarding the misrepresentation rule in a Dear Colleague Letter (DCL). The DCL does not fundamentally change the requirements but it clarifies that institutions will have statutory rights\* to notice and hearing before sanctions may be imposed, and that the rule applies only to those misrepresentations regarding the institution's educational programs, financial charges and graduate employability, and not just any misrepresentation regarding an eligible institution.

U.S. Department of Education, *Dear Colleague Letter re Implementation of Program Integrity Regulations*, GEN-11-05 (Mar. 17, 2011).

**\* NOTE:** The due process protections of 668 Subpart G are not required when ED pursues a revocation of a PPA or denies an application for recertification.

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# Nature of Education Program (§668.72)

- Type, Nature, and Status of Accreditation
- Transferability of credits
- Whether successful completion of course qualifies student for:
  - Acceptance to labor union
  - Government issued license or nongovernmental certification
  - Satisfaction of conditions generally needed to secure employment in the occupation
- Requirements for successfully completing the program including grounds for terminating enrollment.
- Whether courses are recommended or have been the subject of unsolicited testimonials or endorsements.
- Availability, frequency, and appropriateness of courses and programs to employment objectives

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# Nature of Education Program (§668.72)

## (Continued)

- Nature, age, and availability of training devices or equipment
- Availability of part-time employment or other forms of financial assistance
- Nature and availability of any tutorial or other supplementary assistance needed before, during or after course completion
- Nature or extent of any prerequisites for enrollment in any course
- Subject matter, content of course of study, or any other fact related to the credential awarded upon completion of course of study
- Whether academic, professional, or occupational degree conferred has been authorized by appropriate State agency
- Matters required to be disclosed under 34 C.F.R. 668.42 (Financial Aid) & 668.43 (School Information)

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# Nature of Financial Charges (§668.73)

- Offers of scholarships
- Whether a charge is customary charge
- Cost of program and refund policy
- Availability or nature of financial assistance
- Duty to repay loans regardless of whether student completes program or obtains employment
- Student's right to reject financial aid or other assistance or whether student must apply for particular type of aid

# Employability of Graduates (§668.74)

- School's relationship with any organization, employment agency, or other agency providing authorized training leading directly to employment
- School's plans to maintain placement services for graduates or otherwise assist in obtaining employment
- School's knowledge about current or likely future conditions, compensation, or employment opportunities in industry
- Whether employment is being offered by institution or that a talent hunt/contest is being conducted
- Government job statistics in relation to potential placement
- Other requirements generally needed to be employed:
  - commercial driving licenses
  - license to carry firearms
  - failing to disclose factors that would prevent applicant from qualifying for such requirements, such as existing prior criminal record or preexisting medical conditions

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# Misrepresentation

## PENALTIES

### Revocation of Program Participation Agreement

(the most extreme consequence: ends participation in Title IV without due process protections provided in 34 CFR 668 Subpart G) (Note: only applies to provisionally certified schools).

Denial of Participation Applications, e.g., denial of application for recertification.

Proceedings seeking fine, limitation, suspension, or termination.

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# Potential Statutory Actions

- False Claims Act – increased number of *qui tam* actions in sector.
- State Deceptive Trade Practices
- State Agency Rules and Regulations
- Criminal Fraud

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# Limitations in Scope

GEN-11-05:

Q: Do the misrepresentation regulations create a private right of action?

A: **No.**

Q: Do the misrepresentation regulations extend beyond substantial misrepresentations made re: educational programs, financial charges, or employability of graduates?

A: **No**, the rule did not expand the scope of misrepresentation beyond the three listed areas.

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# Enforcement

How might the Department Chose to Enforce?

“the Department has also always operated within a rule of reasonableness and has not pursued sanctions without evaluating the available evidence in extenuation and mitigation as well as in aggravation.”

75 FR 66914 (October 29, 2010)

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# Enforcement

- “As noted elsewhere in this preamble, the Department enforces its regulations, including those in subpart F of part 668 with a rule of reasonableness. ...For this reason, we agree to limit the reach of the ban on making substantial representations to statements made by any ineligible institution, organization, or person with whom the eligible institution has an agreement to provide educational programs or those that provide marketing, advertising, recruiting, or admissions services.”

Federal Register, April 13, 2011 (76 FR 20636)

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# Enforcement

- “...As a result, statements made by students through social media outlets will generally not be covered by these misrepresentation regulations.”
- Also statements made by entities that have agreements with the institution to provide services other than those relating to educational programs, marketing, advertising, recruiting, or admissions services will generally not be covered by these misrepresentation regulations (Example: Food Service).

Federal Register, April 13, 2011 (76 FR 20536)

# State Attorney General Activity related to misrepresentation

- **State Unfair and Deceptive Trade Practices Laws**
  - QuinStreet settlement with 20 states: sites used to recruit students “were deceptive and misleading in giving the appearance that the sites were operated, owned or endorsed by the U.S. government or military.”
  - Pending Kentucky AG Lawsuits: concern statements about placement rates (including alleged misrepresentations to accreditors), cost, employment prospects, and other misleading statements made in marketing.
  - State AG settlements: concern statements made about transfer of credit, job placement, cost, accreditation, and other issues.

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- Peter S. Leyton is the president of the Washington, D.C. area law firm of Ritzert & Leyton, P.C. (R&L) and head of the firm's education practice group. Since 1980, Peter has represented many institutions of higher education, publicly traded companies, private investment groups and others with respect to resolving regulatory/compliance matters as well as with respect to achieving desired transactional results through mergers, acquisitions and reorganizations. This work involves daily interaction with the U.S. Department of Education (DOE), national, regional and programmatic accrediting agencies as well as state licensing agencies and other third parties. Peter completed his second term on the Association of Private Sector Colleges and Universities board of directors in June 2012 and is actively involved in advising APSCU on legislative, regulatory and litigation matters. Peter received his law degree from Catholic University School of Law in 1980, a master's degree in public administration from American University in 1974, and a bachelor's degree in political science from Antioch College in 1971.
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