

December 7, 2015

Compensation based on student completions now permissible, while compensation based on diversity recruitment still not allowed

At the end of November, the US Department of Education ("ED") issued important new guidance regarding its incentive compensation regulations, which ED says "clarifies and provides additional information" about part of the rules.¹ The new guidance makes two key points: (1) ED has reversed its prior position under its 2010 regulations and announced that compensating employees based on students who complete their educational programs is no longer a prohibited practice, and (2) ED confirmed its earlier guidance that compensating employees for success in enrolling minority students is still not permitted.

ED issued this new guidance in response to the continuing lawsuits filed by the Association of Private Sector Colleges and Universities ("APSCU") challenging various aspects of the "Program Integrity" regulations ED issued in October 2010, of which incentive compensation was one part. As a result of the lawsuit APSCU filed in 2011, the US Court of Appeals for the DC Circuit in 2012 issued a decision that criticized the portion of ED's new incentive compensation regulations that disallowed graduation-based and completion-based compensation, and remanded that issue back to ED, directing ED to justify its expansion of the statutory restrictions on enrollment-based compensation to student completions. The Court of Appeals also ordered ED to further explain the impact of the revised incentive compensation regulations on minority recruitment and enrollment.²

ED responded to the remand in March 2013 by updating the preamble to the regulations, offering some explanations but largely just repeating its previously stated justification. APSCU subsequently challenged ED's revised explanations as still being legally inadequate in light of the Court of Appeals' order.

In October 2014, the DC District Court once again remanded (but did not invalidate) those same portions of the regulations and ED's revised guidance, requiring ED to "provide record evidence in support of its graduation-based compensation ban," as well as to "address the potential effect on minority recruitment, i.e., whether minority enrollment could decline under the new regulations."³ More than a year after the Court remanded those two items for the second time, ED has now responded with the guidance discussed here.

Compensation based on student completion or graduation

Since 2010, when ED revised its incentive compensation regulations to eliminate all the pre-existing "safe harbors" and significantly constrict compensation options for institutions, ED has interpreted the incentive compensation law to include a ban on compensation based on students graduating from and/or completing their educational programs. ED's new November 2015 guidance removes this ban, stating that, in response to the District Court's decision, ED "has reconsidered its interpretation and does not interpret the regulations to proscribe compensation for recruiters that is based upon students' graduation from, or completion of, educational programs."⁴ This is a significant change in position by ED.

ED also says that it will not view the references in the regulations to recruiter enrollment activities that may occur "through completion" of a student's program⁵ as prohibiting graduation-based or completion-based compensation. ED goes on to explain that it has changed its interpretation because it lacks sufficient evidence to demonstrate that schools are using graduation-based or completion-based compensation as a proxy for enrollment-based compensation.

Despite this clear outcome from the court case, and ED's admission that it does not have evidence to support a ban on compensation based on student completion or graduation, ED's new guidance also includes language indicating that ED is suspicious of how schools may seek to compensate employees under this new guidance, and stating that it will scrutinize schools' compensation practices to see if they are using completion-based metrics as a guise for enrollment-based metrics. ED stated:

In assessing the legality of a compensation structure, the Department will focus on the substance of the structure rather than on the label given the structure by an institution. Thus, although compensation based on students' graduation from, or completion of, educational programs is not *per se* prohibited, the Department reserves the right to take enforcement action against institutions if compensation labeled by an institution as graduation-based or completion-based compensation is merely a guise for enrollment-based compensation, which is prohibited. Compensation that is based upon success in securing enrollments, even if one or more other permissible factors are also considered, remains prohibited.⁶

The court order from the APSCU case forced ED to issue this guidance admitting that it did not have evidence to support a ban on graduation-based compensation, but with the language quoted immediately above, ED is leaving the door open to scrutinize any plan that includes graduation- or completion-based compensation. Therefore, although the law does not prohibit an institution from implementing such a plan, we urge schools to use caution when developing and implementing any plan that includes incentive compensation based on the number or percentage of graduates or program completers, in an effort to reduce the likelihood of citation by ED.

ED's new guidance does not address schools' ability to pay incentive compensation for student retention that is less than completion. Recall that the prior safe harbor in the regulations permitted compensation based on students who completed at least one year of their educational program. We believe that the court orders and ED's new guidance do not re-instate the former safe harbor, and therefore that the only new compensation that ED is permitting is for students who complete their programs, not for students who persist to some point less than completion.

In addition, ED's new guidance does not address whether employees covered by the incentive compensation restrictions can be compensated based on graduates' job placement. ED's prior guidance was that incentive compensation based on retention, completion, graduation or placement was not permitted. In our view, the court orders and ED's admission that it does not have evidence to support a ban on completion-based compensation "breaks the chain" between the act of enrollment and the act of completion, such that compensation for any activity post-graduation, like job placement, would not be prohibited.

Impact on minority enrollment

The other issue addressed in ED's new guidance is compensation for the recruitment of minority students. In response to the District Court's requirement to address the effect that the incentive compensation ban could have on minority enrollment, ED reaffirms that the ban on compensation based on the enrollment of students covers all students, with no exception for minority students. ED discusses this issue at length in the new guidance, but its conclusion is clear: ED will apply the incentive compensation law as prohibiting incentive compensation based on the enrollment of any students, irrespective of the student's minority status and irrespective of whether the goal of the institution is to increase student diversity.

ED goes on to say that it "acknowledges that the amended regulations could negatively affect outreach and enrollment generally, as well as student outreach that is specifically targeted at promoting diversity, which could result in fewer minority students recruited and enrolled."⁷ ED also states that at this time it has no way to measure the impact that the incentive compensation ban may have on minority enrollment.

In sum, ED admits that minority enrollment may be affected, but states that the law still does not allow incentive compensation to promote or increase diversity at schools receiving Title IV funds.

If you have any questions about ED's new guidance or any aspect of the incentive compensation regulations, or if you would like to discuss revising any of your current compensation plans, please do not hesitate to contact us.

Notes

1. 80 FR 73991 (November 27, 2015).
2. *APSCU v. Duncan*, 681 F. 3d 427 (DC Cir. 2012).
3. *APSCU v. Duncan*, 70 F. Supp. 3d 446 (D.D.C. 2014).
4. 80 FR 73992 (November 27, 2015).
5. 34 C.F.R. § 668.14(b)(22)(iii)(B) and (iii)(B)(2)(ii).
6. 80 FR 73992 (November 27, 2015).
7. *Id.* at 73993.

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