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Lurking Behind the Headline: Significant Regulatory Changes Beyond Gainful Employment in ED's Latest NPRM

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More than a year after the Department of Education (ED) completed its negotiated rulemaking covering an array of regulations related to institutional and programmatic eligibility for federal financial aid, ED published a substantial notice of proposed rulemaking (NPRM) on May 19, 2023. The NPRM is ambitious in its scope and includes another long-awaited iteration of ED's Gainful Employment (GE) rules.

This NPRM comes on the heels of a litany of new rules, including, among others, rules that broaden borrower defense to repayment (BDR) regulations, tighten the 90/10 calculation, and update change in control regulations, all set to take effect July 1, 2023. Also in the background are substantial recent policy and regulatory announcements, including guidance broadening the scope and interpretation of the third-party servicer rules, a push to require individual board members and executives to assume liability for institutional funds, and another large negotiated rulemaking set to roll out in 2023. Individually, each of these new initiatives requires close review and attention but collectively, this recent flurry of activity is unwieldy at best, and the breadth of the NPRM requires an all-hands approach to understand and prepare for the potential impact.

It's important to note that, while the spotlight is on the new GE rule, several of the other proposals in this NPRM will have a significant impact on institutional operations and eligibility for public, nonprofit and proprietary institutions.

ED is accepting public comments on these proposals via its submission portal through **June 20, 2023**. We're aware that various stakeholders have asked ED to extend the comment period but, at this point, there is no extension.

We've briefly described the key proposals below.

1. Gainful Employment (GE)

The Higher Education Act (HEA) specifies that certain programs are eligible for Title IV program funds if they prepare students for "gainful employment in a recognized occupation." But the HEA does not define or further explain that concept, so ED's latest NPRM aims to do so through a pair of debt and earnings metrics. ED has implemented versions of this rule at various points over the last decade and the latest proposal borrows largely from the 2014 version of ED's GE rule, which was rescinded by the prior Administration in 2019.

The proposal will use metrics calculated annually to assess whether certain programs lead to "gainful employment," as well as to evaluate whether **all** programs are "high debt" or "low earnings":

1. Debt-to-earnings (DTE) metrics, which compare the debt burden of program graduates to their annual and discretionary income.
2. An earnings premium (EP) metric, which analyzes the earnings of programs graduates relative to the earnings of individuals who have only a high school diploma.

The DTE metrics, with some tweaks, were part of the 2014 GE rule, while the EP metric is new in this NPRM.

These metrics will have different consequences for different programs and institutions. All Title IV-eligible programs, whether degree or nondegree, and whether offered at nonprofit, public, or proprietary institutions, will disclose their EP and DTE rates. Programs with rates that do not meet the thresholds established by ED will be categorized as either "high debt burden" or "low earnings," and institutions will need to need to obtain student acknowledgement of those labels before they can disburse Title IV funds to students.

Only certain programs – specifically, all programs offered by proprietary schools and nondegree programs offered by public and nonprofit schools (collectively known as "GE Programs")— will face Title IV-eligibility consequences, depending on the outcome of the metrics. GE Programs that do not meet certain thresholds established by ED in two of three consecutive years will lose Title IV eligibility.

The implementation of this will require significant annual data reporting from institutions related to their Title IV-eligible programs, including data around each individual student, program cost, and institutional and private loans. In addition, there are also several unknowns about how this framework will operate in practice. ED contemplates that the disclosure and student acknowledgement side of the framework will use an ED-operated website, which hasn't been developed yet. In addition, to calculate its metrics, ED will need to obtain anonymized earnings data from another federal agency – such as the IRS or the SSA) – through an interagency agreement, which is not yet in place, nor has a specific agency been identified as the source (although ED says it prefers to work with the IRS).

Also with the publication of the NPRM, ED released program-level data purporting to estimate institutional performance under this rule, drawing on several sources of data currently available to ED. Notably, it's not likely that any of the data used here will be the actual data used to calculate metrics when the rule takes effect, because ED has not yet decided from where it will obtain earnings data, institutions have not yet provided any of the needed student-level data, and the years from which ED is drawing may not align with the cohort years at the time any rates are officially calculated.

Finally, other topics in this NPRM pick up on the GE rule as well. The administrative capability proposal would consider an institution not administratively capable if at least half its total Title IV funds come from failing GE programs, or if at least half its full-time Title IV students are enrolled in failing GE programs. The certification proposal would limit the number of hours in a GE program to the greater of the required minimum number of clock or credit hours, as established by the state in which the institution is located, or any federal agency or the institution's accrediting agency.

2. Financial responsibility

The NPRM proposes a number of changes to ED's financial responsibility regulations, including reverting to a more expansive version of events – similar to the version that was in effect in 2016 – that must be reported to ED and may result in a reassessment of the institution's financial condition. The NPRM also adjusts requirements with respect to the timing and form of institutional financial statements, and modifies the financial review requirements for institutions that undergo a change in control.

Financial audits timing and form

In an effort to receive information about financial situations as soon as possible, ED proposes that proprietary institutions must submit annual financials either six months after the last day of the fiscal year or 30 days after the auditor issues its report, whichever is earlier. The NPRM would also make mandatory a more detailed related party disclosure and require foreign-owned institutions to provide organizational documents for controlling owners. In addition, ED is proposing that financial statements include a footnote to disclose spending on recruiting, advertising, and pre-enrollment expenditures in the previous fiscal year, which ED believes are possible indicators of financial instability. Finally, as under current rules, the auditor's opinion cannot be adverse, qualified, or disclaimed, or otherwise disclose a going concern. The proposed regulations will add that the auditor's opinion cannot include a disclosure about the institution or an ownership entity's diminished liquidity or ability to continue operations.

Financial responsibility after a change in control

ED is proposing to relocate and amend the financial tests it applies to institutions undergoing a change in control. These changes would retain the existing same-day balance sheet tests, and also specify that a new owner's historic financials must satisfy certain metrics, including the composite score. In examples where there may be no new owner with control, or where a new owner does not have historic financials, an automatic letter of credit may be required. Finally, the NPRM allows ED to determine that an institution is not financially responsible following a change in control because the repayment of acquisition debt is inconsistent with an institution's available cash.

New financial responsibility obligations

ED has added "obligations" that all institutions must meet in order to be considered financially responsible. In addition to making timely refunds and meeting the required financial ratios, which have long existed, ED is also proposing that institutions must pay credit balances on time and according to the regulations, make payments on financial obligations in less than 90 days, make payroll on schedule, and not borrow from retirement funds or other restricted sources without authorization.

Updates to triggering events

ED has updated the mandatory and discretionary "triggering" events that must be reported to ED, typically within 10 days of occurrence. Depending on the circumstances, some mandatory triggers are "automatic," meaning the occurrence of

the event indicates a financial responsibility failure, without recalculating the composite score.

This set of automatic triggers includes:

- If provisionally certified due to a change in control, the school is sued by a federal or state entity, or through a qui tam/False Claims Act suit.
- Receiving more than 50% of its Title IV funds for programs failing the GE metrics.
- Any oversight body requires the school to submit a teach-out plan.
- A state authorizing agency notice of a violation that would result in a revocation if the violation is not fixed.
- If publicly traded (now defined as directly or indirectly owned at least 50% by a public entity), either the school (or the owner's publicly traded ownership entity) is subject to a suspension or revocation of exchange registration, or Securities and Exchange Commission actions filed in court, an exchange notifies the entity that it is not in compliance with the listing requirements, failure to file a required SEC report, or an equivalent action in a foreign exchange.
- One year of failing the 90/10 ratio.
- Two years of cohort default rates over 30%.
- A loss of eligibility in another federal educational assistance program.
- An ED action results in a default or adverse condition in a credit agreement.
- The school declares a state of financial exigency to any governmental agency or accreditor.
- The school, an owner or controlling/managing entity files for receivership.

ED has also created another set of mandatory triggers that, when reported, will result in a recalculation of the school's most recently files composite score. These triggers include:

- If the school's composite score is less than 1.5, and a debt or liability from a "settlement, arbitration proceeding, or a final judgment in a judicial proceeding" reduces the score to below 1.0.
- ED has initiated an action to recover loan discharges, and the adjudicated claims would bring the composite score below 1.0.
- If a for-profit school has a composite score below 1.5 or, in the first year following a change in control, withdraws owner's equity by any means, unless it is a transfer within the same school group or a required payment, and that withdrawal results in a composite score below 1.0.
- A contribution in the last quarter of the fiscal year, followed by a distribution in the first two quarters of the following fiscal year that reduces the composite score below 1.0.

In addition, ED has proposed new discretionary triggering events. In these circumstances, the issue must be reported to ED, and ED which will determine whether the reported incident is likely to have a materially adverse effect on the school's financial health (at ED's discretion). These discretionary triggers include:

- Accrediting or governmental agency action placing the school on probation or show cause, or a comparable status.
- The school or its owners violate a credit agreement that results in change in terms, or the creditor takes action to withdraw or suspend the agreement.
- "Fluctuations" in Title IV volume.
- "High" annual dropout rates.
- For schools on reporting following a change in control, or due to a financial responsibility issue, the reports indicate a failure of ratios, negative cash flows or other indicators of a material change to finances.
- Pending group BDR claims that, if approved, could be subject to recoupment.
- Discontinued programs that impact more than 25% of enrolled students.
- Closure of more than 50% of the school's locations, or a location where more than 25% of students are enrolled.
- Citation by a state agency for failing to meet requirements.
- Loss of eligibility in other federal assistance programs.
- Investigations by a stock exchange.

Finally, regardless of the type of trigger, if ED believes it meets the thresholds as defined, it will require an at least 10% letter of credit based on the prior year's Title IV receipts, and each trigger requires its own letter of credit, so any institution that experiences multiple triggers will be required to post at least 10% per triggering event.

3. Administrative capability

The NPRM proposes additions to ED's "administrative capability" rules, which implement the HEA's requirement that institutions must demonstrate they are administratively capable to administer Title IV program funds. These additions

include new components to the financial aid counseling requirements around cost of attendance and sources of financial aid and specifying that certain negative actions by other regulatory agencies will result in an institution being not administratively capable. The NPRM also incorporates other existing rules into the administrative capability requirements, including certain aspects of the past performance rules and the misrepresentation rules, as well as prohibiting delayed disbursements of Title IV funds.

Other key proposals on this topic are listed below.

High school credential verification

The NPRM adds parameters to how institutions must evaluate the high school credentials of prospective students, which has long been an area of ambiguity. Under the current rules, institutions must develop and follow procedures to evaluate the validity of a student's high school diploma, if the institution or ED has reason to believe the diploma or school is not valid. But there was no further guidance to institutions on when or how to conduct that evaluation. The NPRM proposes that adequate procedures may include obtaining certain documentation from the high school or a state regulatory agency attesting to the rigor of the high school or confirming that the high school does not appear on any invalid list published by ED (although ED has, notably, declined to publish such a list for many years). Certain high school credentials also would be presumptively invalid: those that do not meet applicable requirements in the state where the school is located; those that are determined invalid by ED, a state or a court; those that require little to no secondary coursework to obtain the diploma; and those issued by an unaccredited entity that maintains a business relationship or is otherwise affiliated with the institution at which the student is enrolled.

Adequate career services

ED is proposing that institutions must provide adequate career services to eligible students who receive Title IV aid. In making this determination, ED will consider (1) the share of students enrolled in GE programs; (2) the number and distribution of career services staff; (3) the services institutions promise to students; and (4) the presence of institutional partnerships with recruiters and employers who regularly hire graduates.

Accessible clinical and externship opportunities

ED proposes that all institutions must provide students with "geographically accessible" clinical or externship opportunities related to and required for completion of a credential or licensure. These opportunities must be provided within **45 days** of successful completion of other coursework.

4. Certification

ED proposes a number of changes to its procedures for certifying institutions to participate in the Title IV programs. ED has always had broad discretion to approve or not approve, or otherwise condition, an institution's participation, and this NPRM signals a continuation of that approach. ED's proposal specifies a number of circumstances in which ED may place or continue an institution on provisional status, including if ED decides the institution is "at risk of closure." The proposal gives ED the flexibility to impose agreement terms from one to three years, depending on how soon it wants to review the institution again, which is largely consistent with current ED practice.

Several other changes in this section will have a significant impact, as listed below.

Supplementary performance measures

The proposal will establish certain metrics for ED to consider in deciding whether to certify an institution's participation in the Title IV programs. These include a withdrawal rate, an institution's GE metrics, the amount the institution spends on instruction and related activities, academic support, support services and recruiting, as well as the licensure pass rates in licensure programs. The NPRM does not set forth specific benchmarks or penalties – it only states that ED will consider these factors in assessing the institution's certification.

Liability and Program Participation Agreement (PPA) co-signatures for controlling owners

In March 2022, ED published an electronic announcement that updated PPA signature requirements for entities exercising substantial control over nonprofit and proprietary institutions, authorizing ED to require those entities to sign the PPA in certain situations, thereby assuming joint and several liability for an institution's federal student aid obligations. The NPRM proposes to significantly expand that policy by requiring, as a default, authorized representatives

of entities that directly or indirectly control an institution to sign the PPA, even if there is no reason to believe the institution poses a risk to taxpayer dollars. The NPRM includes broad examples of circumstances that signal an entity can control the institution and indicates ED will aggregate the ownership interests and other rights of affiliated or related entities, as well as require authorized representatives of all such entities to sign the PPA.

Notably, the NPRM does not address whether and when individual board members and executives may be asked to assume personal liability for institutional obligations by signing the PPA. Currently, those expectations are set forth in a more recent ED electronic announcement from March 2023 and have not yet been incorporated into a rulemaking.

New PPA certifications

Under current rules, institutions must certify that they comply with the authorization requirements of each state in which students are located. Many institutions satisfy this requirement through participation in the State Authorization Reciprocity Agreement (SARA), which also requires member institutions to agree to uniform consumer protection policies. The NPRM would require institutions to certify compliance with consumer protection laws related to closure, recruitment, and misrepresentation for the state in which the institution is located, as well as each state in which enrolled students are located. This would apply even if the institution were authorized to provide education to students in the state through its SARA membership and increases the obligations of all institutions to ensure compliance with laws that vary greatly by state.

In addition, the NPRM heightens compliance obligations related to professional licensure programs, adding to disclosure requirements put in place through a 2019 negotiated rulemaking. Under the current rules, institutions must identify and make available lists of states (1) in which each licensure program meets the requirements for licensure, (2) in which each licensure program does not meet the requirements for licensure, and (3) for which the institution has not made a determination. Under the NPRM, simply disclosing this information would be insufficient. Rather, institutions would also be required to certify to ED in its PPA that each licensure program satisfies all educational prerequisites for each state in which students enrolled in the program are located. This includes certifying that each licensure program is programmatically accredited, if required for licensure in a state.

Conditions on approval

Although ED already wields considerable discretion to impose any conditions on an institution's participation in the federal student aid programs, the NPRM would codify some specific conditions ED may impose for provisionally certified institutions. Conditions may include limits on the acquisition of another institution or entering into written arrangements with other institutions, as well as hiring a monitor to review marketing and recruiting materials. The NPRM also codifies other conditions that are already commonly imposed on provisionally certified institutions (especially after a change in control), including limits on growth and cash and student complaint reporting, as well as conditions specific to institutions converting to nonprofit status.

5. Ability to benefit (ATB)

ED reached consensus on changes to the ATB rules during negotiated rulemaking. Under existing law and regulation, students without a high school diploma or GED may access federal student aid by passing an exam approved by ED, meeting a state process to establish eligibility, or successful completion of six credits, or the equivalent, toward a degree or certificate at the institution. Regardless of which of the ATB alternatives applies, a student must be enrolled in an eligible career pathways program in order to be eligible under the ATB option.

The academic credit and passing test score options are essentially unchanged in the proposed rule, which instead focuses primarily on the state process alternative. ED is attempting to codify the process by which states can establish their program and maintain eligibility, based on the success rate of the students who attend college under this ATB alternative.

The bottom line

The NPRM is complex and covers a significant number of regulations and subjects that require careful review and analysis. Please contact us to discuss any aspect of ED's proposal.

Nancy Anderson focuses on regulatory issues affecting higher education institutions, including compliance with federal, state and accrediting agency requirements.

Kate Lee Carey focuses on the legal, accreditation, administrative and regulatory aspects of regionally and nationally accredited higher education institutions and companies that provide services to the education industry.

Caitlyn Shelby advises postsecondary institutions, K-12 schools and education companies on matters involving accreditation, state authorization and the provision of online education, and monitors legislative and regulatory developments in these areas.

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