

U.S. Department of Education Reinterprets Incentive Compensation Ban

This past month, the U.S. Department of Education softened one aspect of its hardline stance against incentive compensation. The incentive compensation ban, which applies to institutions of higher education that receive federal student aid, prevents admissions and financial aid employees from being compensated based on their successes in securing either enrollments or student aid awards. In its latest statement on the ban, the Department has clarified, among other things, that completion-based and graduation-based incentives are now permissible. Nevertheless, the Department has also signaled that it will continue to view such incentives with skepticism. We expect that the Department will continue to carefully consider all relevant facts and circumstances to evaluate whether graduation based incentives are, in fact, prohibited enrollment based compensation.

Shifting Rules on Graduation-Based Incentive Compensation

1994	Prohibited
2002	Permitted
2010	Prohibited
2015	Permitted

The Incentive Compensation Ban

In higher education, unlike most other fields, a recruiter may not be paid based on how successfully he or she recruits. Since 1992, federal law has prohibited schools receiving federal financial aid from providing “any commission, bonus, or other incentive payment based directly or indirectly on success in securing enrollments or financial aid” to personnel working in admissions and financial aid. This ban was enacted in response to reports of abusive recruiting practices, in which schools enrolled unqualified students receiving federal student aid. The ban goes so far as to preclude institutions from promoting admissions staff based, in any way, on how many students the staff member successfully recruited. The Department views the ban as a tool for ensuring that admissions officers act as counselors and professionals, rather than members of a sales team.

Violating this ban may trigger severe sanctions. The Department has stated that, in response to violations, it may terminate, suspend, or limit an institution’s participation in federal financial aid programs, impose fines on the institution, or require the institution to take corrective actions, including the repayment of student aid funds received in violation of the ban. In addition, institutions have been subject to False Claims Act cases for violating the ban, some of which resulted in multi-million dollar settlements. This is an area where compliance is critical.

Prior Prohibitions on Retention-Based Compensation

The Department has flip-flopped on whether schools may reward admissions staff based on how long recruited students remain enrolled in the institution, *i.e.*, so-called retention-based compensation.

An early Department regulation construed the ban as prohibiting retention-based incentives. The U.S. Department of Education noted poor experiences with such practices, finding that schools had “lowered satisfactory progress standards and, in extreme cases, falsified attendance and leave of absence records, all in an effort to keep students enrolled,” and then, after the students reached a set retention point, “the students were dropped.” The Department thus initially prohibited any incentive compensation based on retention.

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That position was then relaxed in 2002 when the Department created a retention-based safe harbor. The safe harbor permitted compensation “based upon students successfully completing their educational programs or one academic year of their educational programs, whichever is shorter.” The safe harbor, however, did not last long.

The Department rescinded the safe harbor in 2010. The Department reasoned that, because “an institution’s resolute and ongoing goal should be for its students to complete their educational programs,” an institution could not reward employees “beyond their standard salary or wages for their contributions to this fundamental duty.” The Department announced that “paying bonuses” or other incentives “to recruiters, based upon retention, completion, graduation, or placement remain in violation of [the] prohibition on the payment of incentive compensation.”

The Clarified Rule on Retention-Based Compensation

The Department has once again shifted its position on retention-based compensation. Its new position comes in response to a court ruling in the latest lawsuit filed by the Association of Private Sector Colleges and Universities against the Department challenging the incentive compensation rules. The U.S. District Court for the District of Columbia found, in October 2014, that the Department had not sufficiently justified its 2010 ban on retention-based incentives and ordered the Department to reconsider its position.

At the end of November 2015, the Department announced that it would no longer “interpret the regulations to proscribe compensation for recruiters that is based upon students’ graduation from, or completion of, educational programs.” The Department stated that it lacked sufficient evidence to substantiate its earlier hypothesis that schools were using graduation-based or completion-based compensation as a proxy for enrollment-based compensation. In essence, the Department conceded that it lacked a basis for the broader prohibition.

On its face, the Department’s new interpretation largely reflects the old safe harbor. A significant difference, however, is that the 2002 safe harbor permitted incentive-based compensation upon the completion of a single year of an academic program. By contrast, the Department’s latest interpretation permits compensation linked only to the full completion of a program, such as graduation from an institution.

Moreover, the Department has signaled that it may view completion-based or graduation-based incentives with heavy skepticism. The Department warned that, “although compensation based on 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 is merely a guise for enrollment-based compensation, which is prohibited.” This statement suggests lingering doubt within the Department about completion-based and graduation-based incentives.

Conclusion

Once again, the rules for incentive-based compensation have changed, and, once again, colleges and universities may consider rewarding admissions staff based on whether admitted students complete, or graduate from, academic programs. However, in light of the Department’s continued skepticism of such incentives, colleges and universities should seek legal guidance to ensure any such incentives fully comply with applicable laws and rules.

If you would like our assistance, or if you have any questions about this LEGALcurrents®, please contact any member of our Higher Education or Government and Internal Investigations practice groups at (585) 232-6500. ■



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