NASFAA Analysis of U.S. Department of Education Notice of Proposed Rulemaking (NPRM) on Gainful Employment

August 16, 2010

Institutions are encouraged to copy NASFAA on all comments submitted to the U.S. Department of Education on the NPRM at policy@nasfaa.org.

Opening Doors of Educational Opportunity

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General Summary

On July 26, the Federal Register published a Notice of Proposed Rulemaking (NPRM) that would define "gainful employment" for non-degree programs at public and nonprofit postsecondary institutions, and virtually all programs at for-profit institutions. This definition will affect the eligibility of the program for Title IV assistance.

Please bear in mind that this article describes *proposed* rules. An NPRM by definition is not yet final. Final rules are issued only after a period of public comment, which may result in alteration of the proposed rules. Generally, NPRMs raise questions; answers to questions posed during the public comment period are published with the final rule. The information and examples in this article are based on NASFAA's best understanding, but some aspects of the proposed rule need clarification.

This NPRM is one of the most rigorously explained and complex proposals to come from the Department of Education. Careful analysis and comments by institutions will be critical for a final rule that is both meaningful and achievable. ***Responses to the NPRM are due no later than September 9, 2010.*** Final rules must be issued by November 1 to become effective by July 1, 2011.

Programs Subject to Gainful Employment Criteria

The Higher Education Act defines three types of eligible institution for purposes of participating in the Title IV federal student aid programs:

- Institutions of higher education
- Postsecondary vocational institutions
- Proprietary institutions

General principles

An institution's type is defined in part by the entity that controls it (i.e., public, private non-profit, for-profit) and in part by the length of the educational programs it offers. An institution under public or private nonprofit control can be either an "institution of higher education" or a "postsecondary vocational institution." A school under public or private nonprofit control can qualify as both an "institution of higher education" and a "postsecondary vocational institution" simultaneously, each type encompassing its corresponding eligible programs.

An institution controls which of its programs will participate in Title IV, and can exclude otherwise eligible programs from Title IV participation. However, the law specifies that certain educational programs are Title-IV eligible only if they prepare students for gainful employment in a recognized occupation. Current regulations define "recognized occupation" but not "gainful employment."

Program eligibility, current regulation with revisions proposed by 6/18/10 (NPRM changes shown by redlining)

Under regulations that define "eligible program," 668.8(c) specifies that an eligible program provided by an institution of higher education must—

(1) Lead to an associate, bachelor's, professional, or graduate degree;

(2) Be at least a two-academic-year program that is acceptable for full credit toward a bachelor's degree; or

(3) Be at least a one-academic-year training program that leads to a certificate, ~~degree,~~ or other nondegree recognized ~~educational~~ credential and that prepares a student for gainful employment in a recognized occupation.

Under 668.8(d), an eligible program provided by a postsecondary vocational institution—

(1)(i) Must require a minimum of 15 weeks of instruction, beginning on the first day of classes and ending on the last day of classes or examinations;

(ii) Must be at least 600 clock hours, 16 semester or trimester hours, or 24 quarter hours;

(iii) Must provide undergraduate training that prepares a student for gainful employment in a recognized occupation; and

(iv) May admit as regular students persons who have not completed the equivalent of an associate degree;

(2) Must—

(i) Require a minimum of 10 weeks of instruction, beginning on the first day of classes and ending on the last day of classes or examinations;

(ii) Be at least 300 clock hours, 8 semester or trimester hours, or 12 quarter hours;

(iii) Provide training that prepares a student for gainful employment in a recognized occupation; and

(iv) (A) Be a graduate or professional program; or

(B) Admit as regular students only persons who have completed the equivalent of an associate degree; or

(3) For purposes of the FFEL and Direct Loan programs only, must—

(i) Require a minimum of 10 weeks of instruction, beginning on the first day of classes and ending on the last day of classes or examinations;

(ii) Be at least 300 clock hours but less than 600 clock hours;

(iii) Provide undergraduate training that prepares a student for gainful employment in a recognized occupation;

(iv) Admit as regular students some persons who have not completed the equivalent of an associate degree; and

(v) Satisfy the requirements of paragraph (e) of this section

[*Note: Paragraph (e) defines minimum completion rate and placement rate criteria.*]

At an "institution of higher education," no degree program would be subject to gainful employment. All other eligible programs for this type of institution fall under the "at least one academic year" certificate category and are subject to the gainful employment requirement. This includes non-degree graduate programs.

A "postsecondary vocational institution" encompasses the eligible programs defined under 668.8(d), but these would not be degree programs, nor would they be certificate programs that are least one year in length, because those programs belong to the "institution of higher education" side of the house. A "postsecondary vocational institution" would encompass only programs that are less than a year in length and meet the requirements of 668.8(d).

A "proprietary institution" is under private for-profit control; 668.8(d) also applies to proprietary institutions. These schools can offer programs that meet the *minimum* length criteria under 668.8(d), but can also be one year or longer and can result in a degree. However, all of those programs—except the liberal arts baccalaureate added to 668.8(d) specific to proprietary schools—must meet gainful employment criteria.

Notice of Proposed Rulemaking (NPRM), 7/26/10

Under the NPRM, a program would be considered to provide training that leads to gainful employment in a recognized occupation if—

> (i) The program's annual loan repayment rate is at least 35 percent;
>
> (ii) Using the three-year period (3YP), the program's annual loan payment is 30 percent or less of discretionary income or 12 percent or less of average annual earnings; or
>
> (iii) Using the prior three-year period (P3YP), the program's annual loan payment is less than 20 percent of discretionary income or less than 8 percent of average annual earnings.

[Note: The "three-year period" (3YP) means the three most recent award years prior to the year used to derive earnings. The prior three-year period (P3YP) goes further back to the 4th, 5th, and 6th most recent award years. More detail further below: read on!]

However, meeting one of the foregoing standards might not result in *full* eligibility. ED places a program on a restricted status under the following conditions—

> (i) The program has an annual loan repayment rate of less than 45 percent; and
>
> (ii) The program has an annual loan payment that is more than 20 percent of discretionary income and more than 8 percent of average annual income using 3YP, and if applicable P3YP.

The NPRM thus proposes two tests that would determine whether an educational program meets the gainful employment requirement. Following is a summary, then we will look at each test in detail:

(1) The ***annual loan repayment rate test*** is an expression of the percentage of borrowers who are successfully reducing the principal of their FFEL and Direct loans. The rate encompasses all students who attended the program, whether they left before or after completing it, whose loans entered repayment during a specified period. There is a question as to whether the calculation includes all of a student's FFEL and Direct loans, regardless of the program or school for which they were made, or just the loans made for the program under assessment. The proposed rule language describing the second test (debt-to-income, described below) specifically excludes loans made at other schools; the proposed language for the repayment rate does not have that language.

(2) The ***debt-to-income test*** considers whether the percent of a borrower's income that must be used to satisfy loan repayment is reasonable. The debt-to-income test uses loans of all types, including private loans, but specifically excludes loans made for attendance at any other institution, unless it is under common ownership or control (applicable to for-profit schools). This test looks only at borrowers who actually completed the program. Two alternative measures are available to meet this test, and two sets of timeframes are allowed for each measure. One measure uses discretionary income, and the other uses annual earnings. One timeframe uses borrowers who completed the program during the three most recent award years preceding the year for which earnings data is used; the other consists of the three award years prior to that, i.e., the 4th, 5th, and 6th most recent award years.

Each test has two thresholds: a "gold standard" and a minimum standard. If the gold standard is met for both tests, the program remains eligible with no caveats. If the program fails the minimum standard for both tests, eligibility is lost. In between the two thresholds eligibility is maintained but additional mandates are imposed. The NPRM includes charts that summarize these statuses and also a timeline for implementation.

This structure is something like a traffic light: green for good to go, yellow for proceed with caution, and red for stop:

- A program that meets the stricter "gold standard" of both tests—that is, the annual loan repayment rate and one of the two debt-to-income measures for one of the timeframes—has a green light.
- A program that meets the stricter standard on one test but only the minimum standard on the other, or fails the other, has a light that just turned yellow and the school must provide warnings and additional disclosures to students.
- A program that meets just the minimum standard on both tests has a traffic light that's been yellow for a while, and there is a traffic cop on the corner watching; this program can continue to participate in Title IV but has restrictions placed on its eligibility that allows the Department of Education to provide closer oversight.
- A program that passes the minimum standard on one test but fails the other is racing towards an intersection where the yellow light is dangerously close to turning red; the traffic cop is revving his engine preparing to stop the program. Such a program also has restrictions placed on it and is dangerously close to losing eligibility for Title IV aid.
- A program that fails both tests gets stopped by the red light: it loses eligibility immediately for newly admitted students; students who were already in attendance become ineligible after the following full award year.

Details on the Two Tests

Test #1: The annual loan repayment rate for the program, based on loans that entered repayment in the prior four Federal fiscal years, is at least 35% as a minimum, or 45% as the "gold standard."

$$\frac{\text{OOPB of LPF } \textit{plus} \text{ OOPB of RPL}}{\text{OOPB of all loans for students attending the program}}$$

Which translates to:

$$\frac{\text{(Original outstanding principal balance of loans paid in full)} + \text{(Original outstanding principal balance of reduced principal loan)}}{\text{Original outstanding principal balance of all loans for students attending the program}}$$

Which means:

ELEMENT 1
(For loans that have been repaid in full at time of calculation—except those included as underlying loans in a Consolidation Loan that has not yet been paid in full—the outstanding balance on FFEL or Direct loans owed by students who attended the program, including capitalized interest, on the date those loans entered repayment)

+

ELEMENT 2
(For loans on which payments made during the most recently completed Federal fiscal year have either reduced the principal balance or qualify for the Public Service Loan Forgiveness program, the outstanding balance on FFEL or Direct loans owed by students who attended the program, including capitalized interest, on the date those loans entered repayment)

divided by

(The original outstanding principal balance of all loans for students attending the program)
ELEMENT 3

Excluded from both numerator and denominator:

- Borrowers on an in-school deferment or a military-related deferment status
- Borrowers entering repayment after March 31 of the most recent Federal fiscal year

While this test considers only debt incurred under the FFEL and Direct Loan programs, it appears from the proposed rule language that all of a student's FFEL and Direct Loan debt is counted, regardless of the program or school in which some or all of that debt was incurred. It is NASFAA's understanding that ED intended to count only loans made for the program under assessment.

[Note: Use of only loans made for attendance in the program would overcome one of the most vigorous objections raised during the negotiated rulemaking sessions leading to this NPRM, in which the Department proposed using all of a student's loan debt, not just that incurred for the program under assessment.]

All attendees are considered, not just those who completed the program.

Example: Annual loan repayment rate for 2012 for one-year certificate program

Assuming the four most recent Federal fiscal years for the 2012 annual repayment rate are 2008 through 2011, the 2012 rate would use loans that entered repayment October 1, 2007, through March 31, 2011. This would include loans *made* before October 1, 2007, since students who borrowed at the beginning of their one-year program would have attended at least through that academic year and then had a 6-month grace period before entering repayment. This four-year period could actually be a year earlier (fiscal years 2007 through 2010) depending on when it is calculated and the period to which it applies (fiscal year 2012, which begins October 1, or award year 2012-13, which begins July 1). This is a question that needs additional clarity in the final rule.

Suppose 150 FFELP or Direct Loan borrowers who attended the certificate program entered repayment during the period Oct. 1, 2007 through Mar. 31, 2011.

- Of those, 10 withdrew from the program before completing it; five of the 10 immediately repaid the portions of their loans not returned by the school to the lender before the loan would have gone into repayment; they do not count anywhere in the formula for the 2012 repayment rate. The other five entered repayment on or after October 1, 2007, and they all complete repayment before the 2012 rate is to be calculated. The total amount outstanding on their loans at the time they entered repayment was $10,000. This amount goes into the numerator under element 1 and into the denominator (element 3).

- Of the remaining 140 borrowers, 25 are in an in-school deferment or military-related deferment; they do not count in any element for the 2012 rate.

- Of the remaining 115, 15 are in default and have made no payments during the most recently completed fiscal year. Their combined original outstanding principal balance totals $130,000. This amount counts in the denominator only.

- Of the remaining 100, 20 are in an income-based repayment plan with monthly payment amounts that are not high enough to reduce the principal of their loans. Their combined original outstanding principal balance totals $300,000. This amount counts in the denominator only.

- Of the remaining 80, 10 are in forbearance or hardship deferment. Their combined original outstanding principal balance is $70,000. This amount is added only to the denominator, as they are not considered to be paying down their loan debt.

- The remaining 70 are all in repayment and have made payments that reduce their principal balance during the most recently completed fiscal year. Their total combined original outstanding principal balance is $490,000. This figure becomes element 2 in the numerator and is also added to element 3 (the denominator).

The figures in the ratio are:

$$\frac{\$10{,}000 + 490{,}000}{\$10{,}000 + 130{,}000 + 300{,}000 + 70{,}000 + 490{,}000} = \frac{500{,}000}{1{,}000{,}000} = 0.50$$

The 2012 annual loan repayment rate for this certificate program would be 50%. The threshold for eligibility is 35%, so Test 1 is passed, and the program is eligible regardless of the debt-to-income test. Further, the threshold for full as opposed to restricted eligibility is 45%, so this program remains eligible with no caveats ***if*** the second test is also passed at its higher standard. Both tests must be calculated to determine whether the program's eligibility is subject to additional oversight.

One question that arises here concerns excluded loans. Do you exclude loans that are in an in-school or military deferment at the time of calculation of the rate, or that have been in such a status throughout the most recent fiscal year?

Another question concerns students who return to school after completing the program and borrow again, either at your school or at another. For example, a student attends your program in 2007-08; that loan enters repayment during FY 2008. That's used to calculate the 2012 rate. The student returns to school in 2009-10, the previous loan goes into deferment and is not used in the 2013 rate. The student enters or re-enters repayment on both loans in FY 2010. Are both loans used to calculate the 2014 rate for the first program?

Aug. 1, 2007	Mar 1, 2008	Sep. 1, 2008	Mar. 15, 2009	Oct. 15, 2010
Student borrows subsidized Stafford	Enrollment ends	Repayment begins, in FY 2008	Student borrows unsubsidized Stafford; in-school deferment for subsidized loan	Enrollment ends; repayment resumes on sub loan and begins on unsubsidized loan in FY 2011

Test #2: The program's annual loan payment is: 30% or less (20% or less for "gold") of discretionary income or 12% or less (8% or less for "gold") of average annual earnings for the three most recent award years; or less than 20% of discretionary income or less than 8% of average annual earnings for the prior three award years (4th, 5th, and 6th award years.

Discretionary income measure:
Annual loan payment < Discretionary threshold * (Average Annual Earnings − (1.5 * Poverty Guideline))

Annual earnings measure:
Annual loan payment < Earnings threshold * Average Annual Earnings

This test looks at *all* loan debt—federal, state, private, institutional, including institutional financing plans—but only loans incurred for attendance at the institution offering the program being assessed, and only for students who actually completed the program. The proposed rule specifically excludes any debt obligations arising from student attendance at prior or subsequent institutions unless, for proprietary schools, the other and current institutions are under common ownership or control, or are otherwise related entities. The proposed rule language is not clear as to whether loans made at the same school for other programs count.

The thresholds are taken from the test parameters given in the regulation (for example, the minimum standard for the discretionary threshold would be 30% when using the most recent three award years; the "gold standard" would be 20%).

Discretionary income is defined as the difference between average annual earnings and 150% of the most current Poverty Guideline for a single person in the continental U.S. The Poverty Guidelines are published annually by the U.S. Department of Health and Human Services (HHS) and are available at *http://aspe.hhs.gov/poverty*.

The annual loan payment would be calculated based on a standard 10-year repayment plan for the median loan debt of students who completed the program during the most recent three award years before the earnings year (the most recent calendar year for which earnings data are available).

> *[Note: The median of a finite list of numbers can be found by arranging all the observations from lowest value to highest value and picking the middle one. Using median loan debt means that the highest and lowest debts cancel each other out. As a result, if fewer than half of the students who completed a program borrowed any loan, the median debt would be 0.]*

The average annual earnings are the most currently available actual, average annual earnings, obtained from Social Security Administration (SSA) or another Federal agency, of the students who completed the program during the most recent three award years.

> *[Note: Using the actual earnings of the program's graduates addresses a major concern raised during negotiated rulemaking about use of BLS data for national average earnings linked to specific CIP codes, which was ED's original approach.]*

The annual loan payment and the annual earnings could also be calculated for students who completed the program during the prior three award years if those data are available (i.e., the fourth, fifth, and sixth award years prior to the earnings year). The institution would have to show that students completing the program typically experience a significant increase in earnings after an initial employment period, explain the basis for that earnings pattern, and supply certain data ED would need to perform the calculation. The institution would have to provide information such as survey results of employers or former students, or through other empirical evidence, documenting the increased earnings.

> *[Note: This approach addresses an argument made during negotiated rulemaking that in some fields, earnings start low but quickly increase. It might also serve to smooth out bumps in the economy somewhat.]*

Example: discretionary income measure

Suppose for this example the actual, average earnings for program completers is $20,000, and the program's annual loan payment is $1,000. For 2010, the poverty guideline for a single individual in the continental U.S. is $10,830.

The measure is: Annual loan payment < Discretionary threshold * (Average Annual Earnings – (1.5 * Poverty Guideline)). For the minimum standard using the most recent three year period, the threshold is 30%:

.30 x ($20,000 – (1.5 x $10,830)) = $1,126.50

So, is $1,000 less than the minimum standard under the discretionary income measure? Yes. The minimum standard is passed.

For the "gold standard," the threshold is 20%: .20 x ($20,000 – (1.5 x $10,830)) = $751

Is $1,000 less than the gold standard discretionary income measure? No.

Example: annual earnings measure

Again, the actual, average annual earnings figure for this example is $20,000 and the annual loan payment is $1,000.

The measure is: Annual loan payment < Earnings threshold * Average Annual Earnings. For the minimum standard using the three year period, the threshold is 12%; for the gold standard it is 8%:

.12 x $20,000 = $2,400
.08 x $20,000 = $1,600

For this measure, the program meets the stricter gold standard.

If the program met neither higher standard for the debt measures, the institution could demonstrate that graduates typically experience a significant increase in earnings after an initial employment period. The debt measures would then be calculated based on the prior three-year period. There is only one set of thresholds for the prior three-year period.

<u>Consequences of test results</u>

If a program passes the higher "gold standard" of both tests (loan repayment rate and one of the debt-to-income ratio measures), no additional requirements or restrictions would be placed on the program.

If a program passes the gold standard of only one of the tests (and either the minimum standard of the other test or fails the other test), the program would remain eligible but must warn current and prospective students about the difficulty of repaying loans and must disclose the gainful employment tests. The warning must be prominent in the school's promotional, enrollment, registration, and all other materials, including those on its Web site, and in all admissions meetings with prospective

students. Then warning must be designed and intended to alert prospective and currently enrolled students that they may have difficulty repaying loans obtained for attending that program.

If a program passes only the minimum standard on both tests, or passes the minimum on one test but fails the other, the program would remain eligible but on a restricted basis. The institution would have to:

- Provide annual affirmations from employers that are not affiliated with the institution that the curriculum of the additional program aligns with recognized occupations at those employers' businesses, and that there are projected job vacancies or expected demand for those occupations at those businesses;
- Make the debt warning disclosures described above; and
- Limit the enrollment of Title IV aid recipients in that program to the average number enrolled during the prior three award years.

The NPRM also proposes to require specific approval from ED for new programs that are subject to the gainful employment requirements, with appropriate documentation regarding the gainful employment definition.

Please copy NASFAA on your responses to ED regarding this NPRM, at policy@nasfaa.org.