**EDUCATION ALERT: SDNY Upholds Validity of Gainful Employment Rule**

**Executive Summary**

On May 27, 2015, in *Association of Proprietary Colleges v. Duncan*,[[1]](#footnote-1) New York’s Southern District Court issued an important ruling associated with the U.S. Department of Education’s (“Department”) “Gainful Employment” regulations (“GE Rules”).[[2]](#footnote-2) The Court upheld the validity of the GE Rules in their entirety. The Court also held that:

1. Proprietary colleges do not have a constitutionally protected property or liberty interests in their continued eligibility to participate in federal funding programs under the Higher Education Act (“HEA”), and the GE Rules afford affected schools all the due process that is constitutionally due.
2. The GE rules do not have a retroactive effect.
3. The GE Rules are a reasonable interpretation under the HEA of an ambiguous statutory command.
4. The GE Rules – and the debt-to-earnings ratios (“D/E rates”) contained therein – are the product of reasoned decision making and are not arbitrary or capricious.

**Case Holding & Analysis**

Following the publication of the GE Rules, the Association of Proprietary Colleges (the “APC”), a collection of 23 degree-granting for-profit institutions with 34 campuses in New York State, brought suit against the Department challenging the GE Rules on violations of due process, statutory authority, and arbitrary and capriciousness under the Constitution and Administrative Procedure Act (“APA”).

After a brief overview of the facts and circumstances that gave rise to the GE Rules, the Court soon a discussion of the GE Rules within the context of the HEA, a summary of the 2011 proposed GE Rules, and a summary of the current GE Rules, the Court considered the APC’s arguments in turn.

1. Due Process
2. Procedural Due Process

The Court noted that a “court will only look to whether the government’s procedures comport with due process if there is property or liberty interest[s].”

* 1. Property Interest

The Court noted that while the United States Supreme Court has found constitutionally protected property interests in the “continued receipt of benefits flowing from social welfare programs” where eligibility is defined by a statutory and/or administrative framework; there is a split amongst the Circuit Courts as to whether schools have constitutionally protected property interests. The Court agreed with the D.C. Circuit (and disagreed with the Seventh Circuit, which previously held schools had a property interest in Title IV eligibility) and held that “proprietary colleges do not have a ‘vested right’ to continued eligibility to participate in Title IV federal funding programs under the HEA” The Court reasoned that:

proprietary colleges are not … direct beneficiaries of the funding programs administered under the HEA. Rather, they are … third party beneficiaries [because] they receive the federal dollars … only if, and when, their students do…. The statutory scheme does not ‘require a certain outcome’ and thus ‘does not create ‘entitlements’ that receive constitutional protection.’[[3]](#footnote-3)… Rather, it gives [the Department] latitude to decide whether to confer Title IV funding eligibility on a particular program.’[[4]](#footnote-4)

* 1. Liberty Interest

The Court found APC’s arguments of “financial detriment” and “reputational interest” unpersuasive and insufficient. Following Second Circuit precedent[[5]](#footnote-5), the Court framed APC’s argument as “a stigma-plus claim based on the reputational and financial harm … its members will suffer if the GE Rules go into effect as written.” The Court noted that APC had not shown that proprietary colleges have a constitutionally protected liberty interest in their continued eligibility to participate in federal funding programs under the HEA.

* 1. Process Provided

The Court dismissed APC’s claims that the GE Rules deprive APC of due process and held that “[e]ven if its members had a constitutionally protected property and/or liberty interest in continued eligibility to participate in federal funding programs under Title IV of the HEA, APC’s due process claim would fail because the GE Rules afford affected schools all the process that is constitutionally due.” The Court provided an overview of the eligibility determination process to illustrate that the GE Rules afford due process.

After [the Department] compiles a list of students who completed the relevant program during the appropriate time – a list it compiles using information provided by the institution – it gives the school an opportunity to correct that list.[[6]](#footnote-6)… [the Department] provides the institution with ‘the mean and median annual earnings’ data as well as ‘the individual student loan information used to calculate the rates, including the loan debt that was used in the calculation for each student.’[[7]](#footnote-7) [the Department] allows the institution then to ‘challenge the accuracy of the loan debt information’ (but not the annual earnings data provided by the Social Security Administration) before calculating, and informing the institution of, the final D/E rates.[[8]](#footnote-8) Upon publication of the final D/E rates, ‘an institution may file an alternate earnings appeal to request recalculation of the program’s most recent final D/E rates.’[[9]](#footnote-9)

APC contended that “the GE Rules – and, in particular, the regulations governing calculation of the D/E rates – deprive its member institutions of due process” because: (1) APC “accuses [the Department] of denying school access to the individual student earnings data that underlie the D/E rates calculation.” APC further provides that this denial “renders for-profit colleges … unable meaningfully to challenge an ineligibility determination.” (2) “GE Rules are flawed because the Social Security Administration earnings data on which they rely [upon] are ‘systemically inaccurate’ due to ‘improper[]’ calculations.” (3) “GE Rules are ‘impermissibly retroactive’ because they depend, at least to some extent, upon data that precede the rules’ enactment date.”

In addressing APC’s first argument, the Court compared the private interests of other traditionally afforded protections to APC’s interest of eligibility to participate in Title IV and found that APC’s interests did not “hold a candle” to the traditionally afforded protections.

[P]roprietary institutions’ purported interest in remaining eligible to participate in federal student aid programs under Title IV does not hold a candle to the private interests traditionally afforded strong protections, … such as the continued receipt of welfare and unemployment benefits, the retention of one’s job, or even freedom from imprisonment.… [[10]](#footnote-10) Most proprietary colleges offer multiple programs, and an ineligibility determination for one has no bearing on the eligibility of others. Further, a program deemed ineligible … remains free to enroll students able to finance their education in other ways. By contrast, [the Department] has a strong interest in ensuring that students – who are, after all, the direct (and Congress’s intended) beneficiaries of Title IV federal aid programs – attend schools that prepare them adequately for careers sufficient for them to repay their taxpayer-financed student loans.

As to APC’s second argument, the Court held that there was no showing that “providing … individualized earnings data would decrease any risk of an erroneous eligibility determination.” The Court reasoned that “[t]here is no greater risk of an erroneous eligibility determination under the GE Rules than there would be if there were ‘additional or substitute procedural safeguards….’” The court noted that the “additional” or “substitute” safeguards in this case would be:

giving proprietary colleges access to the Social Security Administration earnings data that underlie the DE rates. It is, of course, worth noting that the GE Rules give institutions a number of opportunities to participate in the process, thus guarding against the risk of an unsound ineligibility determination.

The Court dismissed APC’s “glut” of pre-eligibility-determination process arguments, noting that “the Constitution does not always demand [pre-deprivation process].[[11]](#footnote-11) Even if pre-deprivation were a demand in this case, “[t]he GE Rules give affected institutions at least three opportunities to make submissions to [the Department], and two of those are pre-eligibility determination.”

1. Retroactivity

In regards to the retroactivity of the GE Rule, the Court concluded that “[t]he GE rules have only [a] future effect.” The Court reasoned that the GE Rules “neither affect programs’ past eligibility for Title IV funding, nor require schools to refund federal student aid money received before the regulation’s effective date.” The GE Rules, “merely ‘look to the recent performance of a program’s former students in order to determine whether that program will be eligible, in the *future*, to receive Title IV funds.’”[[12]](#footnote-12)

1. Statutory Authority

The Court also rejected APC’s statutory authority argument, relying on Judge Contreras’s analysis of the statutory authority for the original GE Rule in *APSCU v. Duncan.*[[13]](#footnote-13) Further, the Court rejected APC’s argument “that the GE Rules ‘conflict[] with the … statutory framework’ of the HEA by ‘usurp[ing] the traditional role of accrediting bodies,’ like the New York Board of Regents, in evaluating student achievement and in determining the acceptable educational standards for proprietary institutions.” The Court noted that while “[f]ederal law does prevent [the Department] from dictating state schools’ curricula or otherwise micro-managing their day-to-day operations,”[[14]](#footnote-14) “it says nothing about prohibiting the Department from conditioning schools’ eligibility for federal student aid on performance-based metrics measuring graduates’ success.”

The Court dismissed APC’s argument that “the GE Rules, and what they are designed to measure, are not a reasonable construction of the statutory requirement that programs ‘prepare students for gainful employment in a recognized occupation.’” The Court determined that “the adequacy of a program’s preparation is difficult to measure, but “[i]f ‘a program of training to prepare students for gainful employment’ does not in fact lead to jobs for any of its students, it is reasonable to conclude that those students were not truly prepared.’”

1. Arbitrary and Capricious

APC’s arguments that the data and methodology also failed to persuade the Court. The Court again relied on Judge Contreras’ 2012 opinion for support. The Court further reasoned that “APC’s argument on this point appears utterly to disregard the extensive statistical analyses underlying the GE Rules, [including] … a series of multivariate regression analyses [the Department] conducted before promulgating the final regulations.”

Once again, following the precedent of *APSCU*, [[15]](#footnote-15) the Court rejected, “APC’s argument that the [Department] ‘arbitrarily picked the time period [as soon as 18 months] for measuring earnings.’” The Court noted that the Department’s finding:

[m]easuring income shortly after graduation … provides a clearer picture of the ‘current or recent performance of the program’ and is a far better indicator than lifetime earnings of whether a recent graduate is capable of paying off student debt when that debt becomes due. Put another way, income earned in the first few years after graduation is more obviously tied to one’s training than income earned decades after one leaves school.

APC’s argument that the Department acted arbitrarily and irrationally in setting the annual earnings and discretionary income thresholds “mischaracterizes the GE Rules and the findings on which they are based.” The Court noted that the Department provided “citations to at least four studies that have accepted this standard in the context of student debt” and further provided that the National Association of Student Financial Aid Administrators “established their own student loan debt guidelines based on the eight percent threshold.”[[16]](#footnote-16) The Court held that “[t]he annual earnings and discretionary income thresholds …‘were based upon expert studies and industry practice – objective criteria upon which the Department could reasonably rely.’”[[17]](#footnote-17)

The Court stated that the lowering of the “thresholds for passing those metrics from 12 and 30 percent, respectively, in the 2011 Rules, to eight and 20 percent, respectively, in the current GE Rules … misses the mark.” Its rationale is based upon the facts that: (1) “it is not inherently problematic for an agency to change its position;” (2) the change that APC termed as “dramatic” was “really a change in name only” because “[t]he 2011 Rules never went into effect … and institutions did not actually rely on them by committing to a ‘settled course of behavior’ governed by those rules;” and (3) the “[Department] did provide a ‘reasoned explanation’ for changing the passing thresholds from 12 and 30 percent in the 2011 Rules to eight and 20 percent in the current GE Rules” because the “[Department] determined that programs whose graduates were averaging payments between 8-12 percent of annual earnings and 20-30 percent of discretionary income ‘are much more similar to their failing counterparts than their passing counterparts.’”

Based on this additional data, it was neither arbitrary nor capricious for [the Department] to conclude that ‘the stricter thresholds would more effectively identify poorly performing programs.’ Nor was it unreasonable for [the Department] to justify eliminating the statistical ‘buffer’ included in the 2011 Rules based on its conclusion that the ‘three-tier pass, zone, fail construction’ in the GE Rules provides sufficient protection against the possibility that ‘atypical factors,’ such as an unrepresentative cohort of students or a struggling economy, could doom an otherwise high-performing program.

The court briefly glossed over the remaining APC arguments and stated that the remaining APA arguments “fall flat.” Notably, rejecting APC’s “absurd results” argument under the rationale that “a hypothetical case in which the rule might lead to an arbitrary result does not render the rule arbitrary or capricious.”[[18]](#footnote-18)

**Conclusion**

There are a number of practical takeaways from this decision.

* While this Court agreed with the D.C. Circuit that schools have no vested right to future eligibility to participate in federal student loan programs, the question of whether a school has a recognizable property interest in continued eligibility to participate in programs that provide federal aid money to students still needs to be addressed by the Second Circuit.
* The rule affirms the use of a single metric (D/E rates) to calculate Title IV eligibility, and the Court further expanded that D/E rates consists of multiple metrics – debt to annual earnings and debt to discretionary income. The Court further elaborated that the Department analyzed a number of options and it was within their discretion to reject other, untested metrics, notwithstanding the Department’s prior insistence that two metrics were necessary to evaluate schools.

As of this writing, the parties are evaluating the decision. There has been no indication of whether either party will seek appeal of this ruling to the United States Second Circuit Court of Appeals. Also, argument in a nearly identical case in the DC District Court (*APSCU v. Duncan*) was had on May 21. To be sure, the issue is not yet over.

1. *Association of Proprietary Colleges v. Duncan, et al.*, 1:14-CV-08838. [↑](#footnote-ref-1)
2. Program Integrity: Gainful Employment, 79 Fed. Reg. 64, 890 (Oct. 31, 2014). [↑](#footnote-ref-2)
3. *Sealed v. Sealed*, 332 F. 3d 51, 56 (2d Cir. 2003). [↑](#footnote-ref-3)
4. *Plaza Health*, 878 F.2d at 582; *see also* *San Juan City Coll. V. United States*, 391 F. 3d 1357, 1364 (Fed. Cir. 2004). [↑](#footnote-ref-4)
5. *See, e.g., Velez v. Levy*, 401 F.3d 75, 87 (2d Cir. 2005); *Patterson v. City of Utica*, 370 F.3d 322, 330 (2d Cir. 2004); *DiBlasio v. Novello*, 344 F.3d 292, 302 (2d Cir. 2003). [↑](#footnote-ref-5)
6. *See* 34 C.F.R. §§ 668.404(e), .405(b)-(c), .411. [↑](#footnote-ref-6)
7. *See Id.* § 668.405(e)(3)(i). [↑](#footnote-ref-7)
8. *See Id.* § 668.405(f)-(g). [↑](#footnote-ref-8)
9. *See Id.* § 668.406. [↑](#footnote-ref-9)
10. *See, e.g., Turner v. Rogers*, 131 S. Ct. 2507, 2510-11(2011) (freedom from imprisonment); *Gilbert v. Homar*, 520 U.S. 924 (1997) (job retention); *Fusari v. Steinberg*, 419 U.S. 379 (1975) (unemployment benefits); *Goldberg v. Kelly*, 397 U.S. 254 (welfare benefits). [↑](#footnote-ref-10)
11. *See, e.g.,* *Matthews v. Eldridge*, 424 U.S. 319 (1976) (The Court noted that,”[t]he private interest at stake here – for-profit colleges’ continued eligibility to participate in federal student loan programs under the HEA – unquestionably is weaker than the private interest at stake in *Matthews*, the continued receipt of disability benefits.”) [↑](#footnote-ref-11)
12. *APSCU*, 870 F. Supp. 2d at 151 (emphasis in original). Judge Contreras concluded that terminating “‘schools’ future participation in the Title IV … programs based on their past track record” does not “amount to retroactive application.” *Id*. (ellipsis in original). [↑](#footnote-ref-12)
13. *See* *APSCU*, 870 F. Supp. 2d at 146, 149. [↑](#footnote-ref-13)
14. *See* 20 U.S.C. § 1232a (prohibiting the federal government from, among other things, exercising “any direction, supervision, or control over the curriculum, program of instruction, administration, or personnel of any educational institution, school, or school system”). [↑](#footnote-ref-14)
15. *See APSCU*, 870 F. Supp. 2d at 152 (“[T]he Department rationally concluded that considering a significantly longer earnings window in calculating the debt-to-income tests could weaken or sever the connection between earnings and education.” (internal quotation omitted)). [↑](#footnote-ref-15)
16. 79 Fed. Reg. at 64,919 & nn. 100-03. [↑](#footnote-ref-16)
17. *APSCU*, 870 F. Supp. 2d at 153. [↑](#footnote-ref-17)
18. *Am. Hosp. Ass’n v. NLRB*, 499 U.S. 606, 619 (1991) (internal citations omitted). [↑](#footnote-ref-18)