

$$\begin{aligned}\text{Primary Reserve ratio} &= \frac{\text{Adjusted Equity}}{\text{Total Expenses}} \\ \text{Equity ratio} &= \frac{\text{Modified Equity}}{\text{Modified Assets}} \\ \text{Net Income ratio} &= \frac{\text{Income Before Taxes}}{\text{Total Revenues}}\end{aligned}$$

(2) The ratios for private non-profit institutions are:

$$\begin{aligned}\text{Primary Reserve ratio} &= \frac{\text{Expendable Net Assets}}{\text{Total Expenses}} \\ \text{Equity Ratio} &= \frac{\text{Modified Net Assets}}{\text{Modified Assets}} \\ \text{Net Income ratio} &= \frac{\text{Change in Unrestricted Net Assets}}{\text{Total Unrestricted Revenues}}\end{aligned}$$

(c) *Excluded items.* In calculating an institution's ratios, the Secretary—

(1) Generally excludes extraordinary gains or losses, income or losses from discontinued operations, prior period adjustments, the cumulative effect of changes in accounting principles, and the effect of changes in accounting estimates;

(2) May include or exclude the effects of questionable accounting treatments, such as excessive capitalization of marketing costs;

(3) Excludes all unsecured or uncollateralized related-party receivables;

(4) Excludes all intangible assets defined as intangible in accordance with generally accepted accounting principles; and

(5) Excludes from the ratio calculations Federal funds provided to an institution by the Secretary under program authorized by the HEA only if—

(i) In the notes to the institution's audited financial statement, or as a separate attestation, the auditor discloses by name and CFDA number, the amount of HEA program funds reported as expenses in the Statement of Activities for the fiscal year covered by that audit or attestation; and

(ii) The institution's composite score, as determined by the Secretary, is less than 1.5 before the reported expenses arising from those HEA funds are excluded from the Primary Reserve ratio.

(Authority: 20 U.S.C. 1094 and 1099c and section 4 of Pub. L. 95-452, 92 Stat. 1101-1109)

§ 668.173 Refund reserve standards.

(a) *General.* The Secretary considers that an institution has sufficient cash reserves (as required under § 668.171(b)(2)) to make any refunds required under § 668.22 if the institution—

(1) Satisfies the requirements of a public institution under § 668.171(c)(1);

(2) Is located in a State that has a tuition recovery fund approved by the Secretary and the institution contributes to that fund; or

(3) Demonstrates that it makes its refunds timely, as provided under paragraph (b) of this section.

(b) *Timely refunds.* An institution demonstrates that it makes required refunds within the time permitted under § 668.22 if the auditor(s) who conducted the institution's compliance audits for the institution's two most recently completed fiscal years, or the Secretary or a State or guaranty agency that conducted a review of the institution covering those fiscal years—

(1) Did not find in the sample of student records audited or reviewed for either of those fiscal years that—

(i) The institution made late refunds to 5 percent or more of the students in that sample. For purposes of determining the percentage of late refunds under this paragraph, the auditor or reviewer must include in the sample only those title IV, HEA program recipients who received or should have received a refund under § 668.22; or

(ii) The institution made only one late refund to a student in that sample; and

(2) Did not note for either of those fiscal years a material weakness or a reportable condition in the institution's report on internal controls that is related to refunds.

(c) *Refund findings.* Upon a finding that an institution no longer satisfies a refund standard under paragraph (a)(1) or (2) of this section, or that the institution is not making its refunds timely under paragraph (b) of this section, the institution must submit an irrevocable letter of credit, acceptable and payable to the Secretary, equal to 25 percent of the total amount of title IV, HEA program refunds the institution made or should have made during its most recently completed fiscal year. The institution must submit this letter of credit to the Secretary no later than—

(1) Thirty days after the date the institution is required to submit its compliance audit to the Secretary under § 668.23, if the finding is made by the auditor who conducted that compliance audit; or

(2) Thirty days after the date that the Secretary, or the State or guaranty agency that conducted a review of the institution notifies the institution of the finding. The institution must also notify the Secretary of that finding and of the State or guaranty agency that conducted that review of the institution.

(d) *State tuition recovery funds.* In determining whether to approve a State's tuition recovery fund, the Secretary considers the extent to which that fund—

(1) Provides refunds to both in-State and out-of-State students;

(2) Allocates all refunds in accordance with the order required under § 668.22; and

(3) Provides a reliable mechanism for the State to replenish the fund should any claims arise that deplete the fund's assets.