UNITED STATES DEPARTMENT OF EDUCATION
WASHINGTON, D.C. 20202

In the Matter of

WILLIAM TYNDALE COLLEGE,

Respondent.

Docket No. 03-58-SP

Student Financial
Assistance Proceeding

Appearances: David A. Sebastian, Esq., of Detroit, Michigan, for the Respondent

Jennifer L. Woodward, Esq., of Washington, D.C., Office of the General Counsel, United States Department of Education for the office of Federal Student Aid

BEFORE: Allan C. Lewis, Administrative Law Judge

DECISION

This is an action initiated by the office of Federal Student Aid of the United States Department of Education (FSA) to recover $65,731 of alleged ineligible disbursements of Title IV funds, including interest and special allowances related thereto, and to require William Tyndale College (WT) to purchase loans made under the Federal Family Education Loan program to students and parents in the amount of $278,879.56, plus accumulated interest charges. This action is based upon a final program review determination in which FSA concluded that the arrangement between WT and NorthStar Technical Institute (NS) failed to comply with 34 C.F.R. § 600.9 (2000), the regulation governing the out-sourcing of program courses by an eligible institution. Based upon the findings of fact and conclusions of law, *infra*, it is concluded that the United States Department of Education may recover approximately $62,562 and that WT does not have to purchase the loans made under the Federal Family Education Loan program.

I. Background

As of 2000, WT was a small private, nonprofit, college that offered two-year associate degree programs and four-year degree programs in various areas. By the end of 2000, it was experiencing a severe cash shortage and was making efforts to adopt new strategies to attract additional students. One strategy focused on students who were attending local computer technical training institutes. This approach envisioned these students pursuing, on a part-time basis, an associate degree at WT following the completion of their technical training.

In early 2001, an opportunity arose to attract these computer technical type students with the demise of Computer Learning Center (CLC), a national organization comprised of many local computer technical schools. The CLC school near WT had closed even though it was a financial success. Though WT lacked the capital and expertise to develop and operate such a technical school, a trio of its executives decided to pursue a private venture to essentially reopen this CLC school. The trio oversaw WT's day-to-day operation and was comprised of WT's president, Dr. McHann, WT's vice-president in charge of academic affairs, Dr. Burkeen, and WT's vice-president for enrollment, Dr. Cox.

The new venture was initially incorporated on March 8, 2001, as Tyndale Technical Institute and was later renamed NS. Between February and April 2001, the former assets, leases, equipment, and real estate of CLC were acquired and assigned to this corporation. Efforts were successful in retaining most of CLC's management and teaching staff. It was envisioned that the initial student population would consist of former CLC students who were now eligible to complete their studies at another institution under a teach-out program.

Because NS was not eligible to participate in a teach-out program, the trio had WT submit a teach-out program proposal to FSA and WT's accrediting agency. The program was approved.[1] As a result, WT received the financial aid due these students for the teach-out. These monies, less processing fees, were then paid to NS since it provided the teaching instruction.

As a new institution, however, NS faced problems attracting new students. There were few students who could afford to pay for their education. NS was not eligible to participate in the federal student aid programs and, hence, prospective students of NS could not obtain federal financial aid or student loans. NS skirted this prohibition by continuing the relationship established with WT under the teach-out program. In exchange for a $200 per student fee, WT registered the new attendees as students of WT, even though their course work was provided at

[1] The approval of FSA and WT's accrediting agency was specifically limited to the teach-out students. No new students could be enrolled under the teach-out agreement.

NS.[2] WT processed their financial aid requests as students of WT and, upon its receipt, forwarded their aid to NS.

Amid some controversy, Dr. McHann left his position as President of WT in mid-June 2001. Subsequently, the board of directors appointed an interim president. The interim president undertook a review of the relationship between WT and NS in late July 2001 and requested the assistance of a CPA firm. In early August 2001, the CPA firm reported its findings and expressed serious concerns regarding the arrangement between WT and NS. In late August 2001, WT's board of directors terminated the arrangement with NS.

On September 7, 2001, NS obtained an *ex-parte* temporary restraining order from a local county court that required WT to continue to register and process new WT students seeking their technical concentration at NS and to remit their financial aid and tuition receipts to NS. This matter was ultimately dismissed without prejudice on November 15, 2001.

Over the period June 8, 2001, through December 6, 2001, WT received approximately $517,000 in federal grants and loans for new students. Of this amount, WT returned or made restitution in the approximate amount of $200,000 to FSA or lenders.

On April 3, 2003, FSA issued a final program review determination. It concluded that the arrangement between WT and NS violated 34 C.F.R. § 600.9 (2000). This regulation governed the manner and extent to which an eligible institution, such as WT, may out-source a portion of its educational program to an ineligible institution, such as NS. As a result, FSA sought the recovery of $65,731 in grant disbursements, interest, and special allowances and the purchase by WT of 68 loans in the total amount of $278,879.56.

II. Opinion

WT is an institution that provides educational programs for which it awards an associate or baccalaureate degree and, as an eligible institution, it participates in the Title IV, HEA programs. Its eligibility extends only to those educational programs previously designated by the Secretary in its initial application or subsequently so designated.

[2] Dr. McHann envisioned a mutually beneficial partnership between WT and NS. As registered students of WT, these students would be more likely to continue their education on at least a part-time basis at WT after completing the course work at NS. Dr. McHann estimated that based on 400 students, the $200 per student registration fee would generate $80,000 of additional revenue for WT over the first two years and, if 200 students of NS continued their education at WT, an additional $1.5 million of revenue could be generated.

As an eligible institution, it may out-source a portion of its educational program with an ineligible institution subject to the limitations and requirements of 34 C.F.R. § 668.5(c) (2001)[3] --

> (c) . . . If an eligible institution enters into a written arrangement with . . . [an ineligible] institution under which the ineligible institution . . . provides part of the educational program of students enrolled in the eligible institution, the Secretary considers that educational program to be an eligible program if—
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> (1) The ineligible institution or organization has not had its eligibility to participate in the title IV, HEA programs terminated by the Secretary . . . .
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> (3) (i) The ineligible institution or organization provides not more than 25 percent of the educational program; or
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> (ii)(A) The ineligible institution or organization provides more than 25 percent but not more than 50 percent of the educational program;
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> (B) The eligible institution and the ineligible institution or organization are not owned or controlled by the same individual, partnership, or corporation; and
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> (C) The eligible institution's accrediting agency . . . has specifically determined that the institution's arrangement meets the agency's standards for the contracting out of educational services.

In the instant case, FSA's final program review determination found that WT's arrangement failed to comport with this out-sourcing regulation in several respects. First, WT failed to enter into a written agreement with NS. Second, WT out-sourced more than 50% of the educational program to NS. Third, if WT outsourced more than 25% but less than 50% of the educational program, WT failed to obtain from its accrediting agency a determination that its arrangement with NS met the accrediting agency's standards for the contracting out of educational services. Fourth, FSA determined that the trio controlled WT and NS and, therefore, WT was limited to out-sourcing no more than 25% of an educational program, a limitation that it had exceeded.

In its initial brief, WT produced no evidence to dispute these findings. Instead, it presented its case from the perspective that, assuming these violations of 34 C.F.R. § 668.5(c) were, in fact, true, they were merely "technical" in nature and did not warrant the extreme remedy of repaying all Federal monies disbursed and repurchasing all student loans. For its part, FSA submitted substantial evidence as part of its case.

[3] The final program review determination cited the out-sourcing regulation as 34 C.F.R. § 600.9 (2000). As of November 1, 2000, this regulation was renumbered and moved without substantive modification to Part 668 of 34 C.F.R. 65 Fed. Reg. 65,671 (2000). Hence, the above regulation is the appropriate regulation since the pertinent events occurred after November 1, 2000.

After a review of the record, it is determined that the findings of FSA are upheld with one exception noted in the footnote 4 below.

WT and NS did not execute a written agreement regarding WT's out-sourcing of a portion of an educational program as required by 34 C.F.R. § 668.5(c). It seems that Dr. Burkeen began work on a draft agreement in early April 2001 and, according to the CPA firm hired by WT to review and advise WT on its arrangement with NS, that draft was still not complete as of August. Subsequently, the arrangement between the entities was terminated before an agreement was signed.

Similarly, WT did not obtain a determination by its accrediting agency that its agreement with NS met NCA's standard for the contracting out of educational services. In August 2001, WT's CPA firm noted this failure and urged WT to take measures to rectify this problem. It was not rectified. Hence, the accrediting agency approval requirement to out-source between 25% and 50% of an educational program is not satisfied.[4] 34 C.F.R. § 668.5(c)(3)(ii).

Lastly, there is insufficient evidence to conclude whether WT out-sourced more or less than 50% of the educational program. Although one NS registration form indicates a total of 30 hours of courses taught by NS over the first two semesters, the record contains no evidence establishing the number of credit hours taught by WT as part of the program or the total credit hours of this program. Hence, the percentage of the program taught by WT is not determinable as a matter of fact. The record also contains a statement in a report by the CPA firm to the effect that less than 50% of the student's coursework would be conducted by NS. While this comment may serve as evidence, the report does not reveal the factual basis for such a conclusion. In the absence of other and more persuasive evidence, this is insufficient to satisfy WT's burden of proof. Therefore, the finding -- that WT outsourced more than 50% of the program -- is sustained. Accordingly, WT exceeded the maximum permissible percentage of the program that may be out-sourced under 34 C.F.R. § 668.5(c).

In summary, the arrangement between WT and NS failed to comply with the out-sourcing regulation in several aspects. There was no written agreement between WT and NS, a prerequisite regardless of the percentage of the educational program out-sourced. While a substantial portion of the educational program was out-sourced by WT, the actual percentage does not affect the outcome. If 25% to 50% of the educational program was out-sourced, then WT breached a second requirement: namely, it did not obtain its accrediting agency's

[4] The other requirement is that the two organizations are not owned or controlled by the same individual, partnership, or corporation. 34 C.F.R. § 668.5(c)(3)(ii)(C). While FSA found that control was present in this case, this conclusion is incorrect. Though the trio owned NS as shareholders, the trio did not control WT. WT is a non-profit, tax-exempt organization. As such, it has no shareholders. Its ultimate decision-making authority lies with its 18-member board of directors. Of the trio, only Dr. McCann was a member of the board. Therefore, the trio did not control WT.

determination that the out-sourcing arrangement met the agency's standards. If more than 50% of the program was out-sourced, then WT breached the provision limiting the out-sourcing to no more than 50% of the educational program.

Inasmuch as WT's arrangement with NS improperly out-sourced portions of its educational program, the remaining issue is the nature of the appropriate remedy. FSA seeks to recover $41,318 of Pell and FSEOG grant disbursements, the purchase of 86 loans in the amount of $278,879, and $31,776 of related interest and special allowances.

Initially, WT urges that there should be no penalty because the violations were "technical" in nature, unworthy of the imposition of the extreme remedy of treating the entire program as ineligible and requiring the repayment of all federal grants disbursed and the purchase of student loans. As support, it relies upon In re Mary Holmes College, Dkt. No. 94-32-SP, U.S. Dep't of Education (Mar. 30, 1995).

In Mary Holmes College, the college executed written agreements with two organizations under which these organizations provided the truck-driving component of the college's newly added Entrepreneurial/Truck Driving Program. The Department sought to recover approximately $700,000 of Title IV funds arguing, *inter alia*, that the program was ineligible and that the college failed to inform FSA of its out-sourcing arrangements.

While the tribunal concluded that the program was eligible and in compliance with the out-sourcing regulation, it determined that the college failed to inform FSA of this arrangement as required by 34 C.F.R. § 600.30(a)(5) (1991), the predecessor of the out-sourcing regulation at issue in this case. The tribunal characterized this error as "a technical violation, one not warranting, by itself, the imposition of the extreme remedy of treating the program as ineligible" and requiring the repayment of all Title IV monies disbursed to the students. Id. at 4.

The case at bar is much different. Here, there were substantive violations of the out-sourcing regulation: There was no written agreement. WT contracted out more than the maximum permissible percentage of the program. WT did not obtain approval of its out-sourcing arrangement with its accrediting agency. Hence, unlike the notification problem in Mary Holmes that may be characterized as procedural in nature, WT's improprieties are significant and substantive in nature. They violate the very heart and essence of the out-sourcing regulation, a regulation designed to ensure the integrity of the Title IV programs by setting forth specific requirements and limitations.

Next, WT argues that it is not liable for the $119,619.09 of loan and grant disbursements made between September 7 and October 5, 2001, because they were made in order to comply with a temporary restraining order issue by a local county court. On September 7, 2001, shortly after WT terminated its relationship with NS, NS obtained an *ex-parte* temporary restraining order. That order required WT to continue to register and process new WT students seeking their technical concentration at NS and to remit their financial aid and tuition receipts to NS. WT complied with this order until October 5, 2001, when it ceased its compliance.[5] WT's argument is that disbursements made to comply with a temporary restraining order of a court are lawful disbursements. As such, WT claims that it is not liable to the FSA for these payments.

This argument has no merit. As between WT and FSA, the arrangement is governed by the program participation agreement executed by the parties and that agreement incorporates the program regulations, including the out-sourcing regulation at issue. WT's liability stems from its violation of this regulation resulting in a breach of the program participation agreement. In contrast, it was the arrangement between WT and NS that provided the basis for the issuance of the temporary restraining order. Hence, there are two separate arrangements, each with its distinct rights and obligations. Therefore, FSA's rights under the program participation agreement are unaffected by a court order issued in regard to the arrangement between WT and NS.

There is, moreover, no equitable justification to reduce FSA's damages by virtue of WT's compliance with the court order. WT was a participant in the improper arrangement with NS and it should not benefit to the economic detriment of FSA as a result of its conduct. In Title IV programs, participating institutions are held to the highest standard of care and diligence as befits fiduciaries in administering these programs. In re Hi-Tech Institute of Hair Design, Dkt. No. 92-129-SA, U.S. Dep't of Education (July 14, 1994) (school not excused from obligation to repay monies fraudulently taken by financial aid officers); In re Warnborough College, Dkt. Nos. 95-164-ST and 96-60-SF, U.S. Dep't of Education (Aug. 9, 1996) (school responsible for, and fined as a result of, its agent's misrepresentation that it was part of a well-known university); In re Hamilton Professional Schools, Dkt. Nos. 01-13-EA and 01-14-ST, U.S. Dep't of Education (Sept. 7, 2001) (school terminated from participation in Title IV programs due to, *inter alia*, falsified attendance records resulting in accelerated earning of tuition, illegal disbursement of Pell Grant funds, and reduction of potential refunds due students due to early termination).

Lastly, WT rejects the loan-purchase remedy urged by FSA. It proposes that the damages for the 86 loans made in connection with the improper out-sourcing arrangement be determined under FSA's estimated actual loss formula. As the name implies, this approach yields an estimate of the amount of losses incurred by FSA. The estimate is the product of the total amount of ineligible loans and the institution's cohort default rate for a particular year. A cohort default rate represents the percentage of students who, after leaving an institution, default on their loans during the first year they are in repayment status. 34 C.F.R. § 668.183 (2001).

[5] Apparently, the temporary restraining order continued in effect until it was dissolved on November 15, 2001, when the matter was dismissed without prejudice. The record does not disclose whether there was a settlement in this matter.

Under this formula, FSA sustained $17,012 in damages in the instant case, *i.e.* the product of $278,879.56 of ineligible loans and WT's cohort default rate for 2001 of 6.1%.[6]

FSA urges that the FFEL liabilities must be measured by the Department's actual loss, rather than the estimated actual loss formula—

> [a]s recognized by this Tribunal in In the Matter of Christian Brothers Univ., Dkt. No. 96-4-SP (January 8, 1997) at 4, long-standing FSA policy requires that schools repay the actual amount of the Department's losses if known or quantifiable, and that using the estimated actual loss formula is only appropriate if the Department cannot ascertain with specificity what its actual losses are.[8]
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> WTC provided the Department with a spreadsheet identifying 139 students who attended the ineligible program and for whom WTC disbursed funds, 86 of whom received FFEL disbursements. [footnote and citation omitted.] Each of those 86 students will be due a closed school loan discharge because [NS] . . . closed before the students could complete their "program." Accordingly, FSA followed its long-standing policy when it calculated the FFEL liabilities in the FPRD. The FFEL liability amount of $278,879.56, plus interest accrued to date, is a loss to the Department that is ascertainable and exact and therefore should be upheld by this Tribunal.
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> ________
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> [8] The decision in Christian Brothers at 4, 5 quotes from the FSA's policy memorandum dated July 17, 1996 and acknowledges that the "estimated loss formula should not be used in cases where borrowers may qualify for a Closed School Loan Discharge under 34 C.F.R. § 682.402(c)."

FSA Surreply Br. at 8-9.

Initially, FSA's position is inconsistent with its own policy regarding the selection of the appropriate remedy. The test is not whether the purported losses are quantifiable. Rather, according to FSA's policy memorandum of July 17, 1996, at 3, and, as noted in Christian Brothers, at 4, the general rule is that "the estimated loss formula is to be used in lieu of requiring an institution to repurchase ineligible . . . loans." The loan-purchase approach is the exception to the general rule and is employed in four "specific instances," *i.e.* when all loans are in default, when students are eligible for loan relief, in refund situations, or when loans are certified knowing that the loans are ineligible. As for situations not discussed in the memorandum, the policy memorandum focused on the quantity of loans. The estimated loss

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[6] According to FSA's policy statement of July 17, 1996, at 2, the cohort rate for the period under review should be used "whenever possible." The tribunal takes judicial notice of WT's cohort rate for 2001, as obtained from the Department's public web site.

formula "should not be used in cases involving a small number of ineligible loans" such as 10 or fewer. Moreover, in cases involving a "larger number of loans, the . . . formula should be applied since the burden to the institution in identifying and purchasing all ineligible loans increases as does the burden on the Department to monitor and enforce the repurchase of the FFEL loans." Christian Brothers,
at 4; *see* FSA's policy memorandum at 5.

Inasmuch as the present case involves 86 loans, it is FSA's policy to employ the estimated loss formula absent the applicability of one or more of the designated exceptions. Here, FSA urges that the student loan relief exception governs this case. Under 34 C.F.R. § 682.402(d)(1), a student is entitled to the relief of a loan if the student's school closes--

> (i) The Secretary reimburses the holder of a loan . . . and discharges the borrower's obligation . . . if the [student] . . . could not complete the program of study for which the loan was intended because the school at which the . . . [student] was enrolled, closed.

This regulation and the other regulations promulgated under the Federal Family Educational Loan Program establish the rules governing the participants in this program. WT was a participant in the program. The student loans in question were issued to students enrolled in WT. The problem is that WT did not close, a prerequisite under the regulation to permit the discharge of a loan. Under these facts, the student loans in issue do not qualify for loan relief under the current regulation.[7]

It has been well over two years since NS was closed. There has been ample time in which to discharge the student loans that FSA maintains are dischargeable. Yet FSA proffers no evidence to establish whether these loans have, in fact, been discharged and presents no written argument that explains or justifies the discharge of these loans under the law. Given the policy enunciated by FSA itself, the plain language of the closed school regulation, and the facts in this case, the appropriate remedy for the improper disbursement of 86 loans is to determine the damages under the estimated actual loss formula. Accordingly, FSA is entitled to recover damages in the amount of $17,012, plus such other amount as may be determined by FSA.[8] In

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[7] Under 34 C.F.R. § 682.402(d)(1)(C), a school is defined so as to include a location or branch other than its main campus. NS is not, however, a separate location or branch of WT because the two schools do not share a common ownership or control. Therefore, the closing of NS does not bring the closed school regulation into play.

[8] FSA is entitled to recover a small portion of the $20,181 of interest and special allowances sought in connection with the student loans. The actual amount of recovery cannot be determined based on the record. Accordingly, FSA is directed to compute this amount in a manner consistent with this decision.

addition, FSA may recover the disbursements of grants under the Pell and FSEOG grant programs in the total amount of $41,318, plus interest relating to the grants in the amount of $4,232.

III. Order

On the basis of the foregoing, it is hereby ORDERED that William Tyndale College immediately and in the manner provided by law pay the United States Department of Education a sum of $62,562 and such other amount of interest and special allowances to be determined in accordance with this decision.

Allan C. Lewis
Chief Administrative Law Judge

Dated: April 7, 2004

<u>SERVICE</u>

A copy of the attached initial decision was sent on April 7, 2004, by certified mail, return receipt requested, to the following:

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