

In Re: PUERTO RICO TECHNOLOGY AND BEAUTY COLLEGE,
LAMEC, INC. d/b/a/PUERTO RICO BARBER AND TECHNICAL COLLEGE,

Docket Numbers:

90-34-ST

90-38-ST

Student Financial Assistance

DECISION

Appearances: Baltasar Corrada for Puerto Rico Technology and Beauty College;

A.J. Amadeo Murga, Esq., for Lamec, Inc. d/b/a/Puerto Rico Barber and Technical College;

Stephen Kraut, Esq., for the Office of Student Financial Assistance, U.S. Department of Education

Before: Judge Daniel R. Shell

Background

The United States Department of Education, Office of Student Financial Assistance, Division of Audit and Program Review (Education) issued separate letters on July 17, 1990, to the Puerto Rico Technology and Beauty College (PR Tech) and to Lamec, Inc. d/lo/a Puerto Rico Barber and Technical College (Lamec) to terminate each school's eligibility to participate in Education's Title IV programs and to fine each school. The actions are based on the findings of an Education, Office of the Inspector General, audit of PR Tech's administration of the Title IV, Higher Education Act (MEA) funds for the award years 1984-85 through 1987-88. [See footnote 1 /](#) The auditors found that PR Tech failed to follow pertinent statutes and regulations by requesting and transferring \$403,875 in Education Pell Grant Program Funds to students of Lamec, an ineligible institution.

Finding number one of the Auditor's report, Change in Ownership of the Mavaquez School, states the Office of the Inspector General's June 27, 1990, audit position:

... both parties knew that Lamec was ineligible to participate in Federal SFA [Student Financial Assistance] programs since Lamec was neither licensed nor accredited, and had not entered into the required Program Participation Agreement with ED at the time of the sale....[See footnote 2 2](#)

Education asserts, in the auditor's findings, the schools have violated the following: 34 C.F.R. 668.4, 668.11, 668.18. A discussion of these sections will be found in a later portion of this decision. Based on the circumstances of the change of ownership of the Mayaguez facility, Education intends to fine both PR Tech and Lamec \$450,000 for 18 transfers of Title IV funds from PR Tech to Lamec during the period from July 1, 1987, through June 30, 1988.

Education agreed to drop Finding 2, Failure to Renew Operating Licenses, and Finding 3, Wages Earned, of the Audit report which had been incorporated by reference into the July 17, 1990, termination and fine notices issued to the schools. The withdrawal of Finding 2 is subject, however, to stipulations 83, 84, and 85. [See footnote 3 3](#) The stipulations preserve as a violation PR Tech's failure to renew operating licenses for the period of September 3, 1984, through April 1985 at its Flamboyant Garden facility. [See footnote 4 4](#) The audit found the failure to renew the license with the Puerto Rico Department of Education to be violations of 34 C.F.R. 668.3, 668.4, and 668.6. The discussion of these regulations will be covered later in this opinion. [See footnote 5 5](#)

It appears from the documents submitted that the parties have narrowed the issues in this dispute to the following: a) fines of \$450,000 each against PR Tech and Lamec for 18 transfers of federal funds through PR Tech to Lamec resulting from the Mayaguez sale, b) a fine of an uncertain amount against PR Tech for improperly using Title IV funds for students at its unlicensed Flamboyant Gardens facility, and c) termination of the two schools from participation in Title IV programs for the violation of the regulations listed in either the termination and fine notice or the audit letter dated June 27, 1990.

Due to the essentially identical facts and issues, the separate cases shown in the caption of this case were consolidated under joint case identification numbers 90-34-ST-for Puerto Rico Technology and Beauty College and 90-38-ST for Lamec, Inc. d/b/a/ Puerto Rico Barber and Technical College. [See footnote 6 6](#) This decision will address the hearing on the record requested by each institution.

The case is divided into two separate fact patterns: A) the circumstances surrounding the sale of the Mayaguez School in Bayamon and B) the circumstances of the license status of the Flamboyant Gardens facility. The relevant facts, arguments, law, discussion, and findings for the two fact patterns follow separately.

A.

Arguments Concerning the Change of Ownership of the Mayaguez School

Counsel for Education in his prehearing brief referred to the contract to sell the Mayaguez facility as a "scheme to falsely obtain Pell Grant funds from the United States Department of Education." [See footnote 7 7](#) Specifically, Education states:

Lamec received \$403,875 of Pell Grant Program funds from PR Tech, and disbursed those funds to its students, even though it was not eligible, to participate in [the] Pell Grant Program. [See footnote 8 8](#)

In its posthearing brief, Education refers to the schools actions in the following manner:

The acceptance of the \$403,875 from PR Tech under the above described circumstances is closely akin to the knowingly acceptance and expenditure of stolen money. [See footnote 9 9](#)

They argue that PR Tech improperly drew down Title IV funds for students at its formerly owned Mayaguez facility and passed the funds to Lamec, an ineligible institution, during the period July 1, 1987, through June 30, 1988. Lamec was ineligible because it was not accredited by a nationally recognized agency or association nor licensed by the Puerto Rico Department of Education.

II.

PR Tech argues that it entered into a service contract with Lamec wherein Lamec and its principals, Luis Matos and Efrain Cruz, were to advise PR Tech on various financial matters, student financial assistance, Puerto Rico Department of Education accreditation, and certification by the U.S. Department of Education. They assert that Lamec was given an option to purchase the Mayaguez branch of PR Tech and that Lamec's attorney, Eugenio Cabanillas, drafted the sales contract. Therefore, they reason that any difficulties created by clause 3-C of the sales contract should be assessed against Lamec. Clause 3-C requires PR Tech to make use of its permits and federal licenses to collect funds for the students enrolled at the Mayaguez campus during the period of the transfer of ownership. PR Tech claims to have relied on Lamec's lawyer's advice and the expertise of Lamec's principals (Mr. Luis A Matos and Mr. Efrain Cruz) while they operated under the service contract obligation. It was on this basis PR Tech assumed that the sales contract was a legal and valid contract.[See footnote 10 10](#) They maintain that PR Tech did not willfully or knowingly violate any regulation. Additionally, PR Tech argues that no evidence is offered to show any irregularities or misuse of the \$403,875 which PR Tech drew down from Education during 1987-88.[See footnote 11 11](#)

Even though the Mayaguez facility had been sold and since the Mayaguez campus was not recognized as a free standing school, counsel argues that PR Tech still retained control over the students and federal funds.[See footnote 12 12](#) PR Tech states in its posthearing brief:

PR Tech may have been mistaken as to the fact that students enrolled in the Mayaguez school were PR Tech students after July 1, 1987, but they [PR Tech] acted on that basis, to the point of reimbursing over \$14,000 to the U.S. Department of Education for students who withdrew from the Mayaguez school during that period.[See footnote 13 13](#)

III.

Lamec argues that Zenon Torres of PR Tech knew, on May 4, 1987, that the Mayaguez campus was not classified by the National Association of Trade and Technical Schools (NATTS) as a free standing school. Therefore, since the principal of PR Tech was aware of the impediment to the transfer, PR Tech could not effectuate a change of ownership to Lamec until and if NATTS granted free standing status.[See footnote 14 14](#) Since PR Tech accepted the final payment on the sales contract on June 30, 1987, and represented that the branch campus in Mayaguez was the property of the new owners, PR Tech should be held accountable for not being able to deliver a marketable school.[See footnote 15 15](#)

Finally, Lamec argues that the only attorney at the closing, Eugenio Cabanillas, represented the interests of the bank more than Lamec. [See footnote 16 16](#) In Lamec's opening statement, counsel stated that Lamec was not represented by legal counsel at the closing. [See footnote 17 17](#)

Facts Relevant to the Change of Ownership of the Mayaguez School

On the 23rd day of July 1986, PR Tech entered into a six months service contract with Lamec. [See footnote 18 18](#) Lamec contracted to provide various counseling services. [See footnote 19 19](#) Lamec was given by the terms of the service agreement an option to acquire the school in Mayaguez owned by PR Tech for \$180,000. The option to purchase states:

The parties to the contract agree that if after six (6) months this present contract is not renovated then Lamec, Inc., will have first (1st) option for the acquisition of the "School" in Mayaguez.... [See footnote 20 20](#)

The parties executed a sales contract for the purchase of the Mayaguez campus on April 29, 1987. [See footnote 21 21](#) By the terms of the service agreement, the contractual relationship of the parties was to terminate on January 23, 1987. However, the parties in stipulation number 8 agree that the purchase option agreement of the July 23, 1986, contract was extended two months on February 2, 1987. [See footnote 22 22](#) The agreement extension referenced in the stipulation states: ...Mister Zenon Torres, President of the said institution, prorates/extends said Sales Option Contract under the same terms and conditions for a term of sixty (60) days from this day. [See footnote 23 23](#)

When Torres was asked who owned the Mayaguez campus on July 1, 1987, he did admit, after considerable reluctance, that he did not own the school on July 1, 1987. [See footnote 24 24](#) On June 30, 1987, Lamec owned and was responsible for operating the Mayaguez campus. [See footnote 25 25](#) The contract price was paid June 30, 1987, and the parties notified the Puerto Rico Department of Education of the change of ownership. [See footnote 26 26](#) The sale was not conditioned upon Lamec first obtaining a certificate of eligibility from Education; nor did the contract contemplate any delays caused by the Puerto Rico Department of Education. [See footnote 27 27](#) The sales contract specifically states that PR Tech would continue to request and receive funds for the students enrolled at the Mayaguez campus until Lamec could obtain the necessary approvals to be eligible to participate in the Pell Grant Program in its own right. The parties agreed in Stipulations 48 through 76 that PR Tech drew down \$403,875 of Pell Grant Program funds for students enrolled in Lamec and paid to Lamec the funds drawn down. [See footnote 28 28](#) Lamec admits in stipulation number 77 that, before it used the funds to pay itself for its tuition and fees charged, it disbursed the \$403,675 to its students by crediting those students' institutional accounts. [See footnote 29 29](#)

Torres stated that even though the Mayaguez facility had been sold he considered the students still enrolled in PR Tech. [See footnote 30 30](#) He admitted that nothing in the agreement required PT Tech to continue its responsibility to the students. But he reasoned in light of the unresolved issues of free standing status of the Mayaguez campus, PR Tech maintained a continuing responsibility to the students. Torres testified:

I made the transactions - money transactions, I continued to lend the services - to provide the services for the Mayaguez facility, because we still had the responsibility... with the students, and with the agreement that we had with the Department of Public Instruction in Puerto Rico, the regulation demands that any owner of ta] school maintain responsibility over the students during the process of the sale.[See footnote 31 31](#)

His testimony relates to stipulation number 36 below:

chapter VI (1) of the PRDE [Puerto Rico Department of Education] Regulation also provides that "the new owners will have to sign the corresponding obligations jointly guaranteeing the commitments of the school pursuant to Chapter III (4), subsection (17) of this Regulation. As long as the new owners do not sign such guarantees, the previous owners will continue guaranteeing jointly the commitments made as if no transfer of ownership had taken place."[See footnote 32 32](#)

To insure PR Tech's compliance with the Puerto Rico Department of Education regulation cited above, Torres explained that his staff reviewed all of the papers that were submitted by Lamec for the Mayaguez campus before forwarding payments to Lamec.[See footnote 33 33](#) The payments were not made directly to the students, they were sent to Lamec.[See footnote 34 34](#) Eugenio Troche, PR Tech Financial Aid Officer, testified that he checked the records sent by the Mayaguez facility to verify the student progress and hours certified. Occasionally, he would go to the campus and check all the requirements. Upon completion of that task, he would disburse the money to Lamec.[See footnote 35 35](#) Torres admitted issuing eighteen checks to Lamec between July 1, 1987, and June 30, 1988.[See footnote 36 36](#) No one has ever indicated to him that the amounts paid were too much, too little, or otherwise improper.[See footnote 37 37](#) It was his belief that he was obligated to continue the draw down and disbursement process because Commonwealth law demands the accountability to the students and because the terms of the agreement of sale required it.

The parties provided considerable testimony on the advice received prior to the closing of the Mayaguez School. On cross examination by counsel for Lamec, Torres revealed that he did not consult with anyone on the requirements necessary to sell the Mayaguez facility to Lamec because:

The reason that I don't counsel anyone was because Mr. Matos was our consultant, and he know all about their programs because he working in that. That was the reason that I believe in him to do every document, sen[d] it to the Department of Education in Puerto Rico, because he was made all this translation.[See footnote 38 38](#)

Torres insisted that he relied on the advice of Matos and Cruz as he had previously done under the service contract. Torres further stated on cross examination that Mr. Lopez of the Banco Popular, the closing bank, suspended the meeting on April 29, 1987, due to objections the bank had with clauses in the sales contract. (emphasis added)[See footnote 39 39](#) Torres testified that he received a letter dated May 4, 1987, from NATTS which states:

Please be further advised that a change of ownership for the Mayaguez facility cannot be considered until the facility has been granted free standing status by the Accrediting Commission.[See footnote 40 40](#)

He claims that he nevertheless did not know that he could not sell the Mayaguez school as an independent facility.[See footnote 41 41](#) Even though Torres claims that he did not know that he could not immediately transfer the Mayaguez facility, a clause was inserted into the sales contract that would require PR Tech to draw down funds for the Mayaguez students during the transfer of the ownership. Paragraph 3-C of the sales contract states:

The appearing party of the first part [PR Tech] will permit the appearing party of the second part [Lamec] to use its federal permits and licenses to collect all the federal grants of the enrolled students or those enrolled in the future, during all the time that [will] be necessary, while the already started process to transfer the licenses and permits of collection grants under the name of Lamec, Inc. is concluded.[See footnote 42 42](#)

Counsel asked Torres "...Is there anything in this provision that you... are directed to draw down program funds and pay those funds to Lamec?" Torres responded by[See footnote 43 43](#) saying, "This-- when I signed this contract, I don't read." Later, he testified that he went to the closing on June 30, 1987, signed the document, and received his money - all while engaging in no conversation with anyone at the closing.[See footnote 44 44](#) He later stated that had he read the provision "...he would never sign it."[See footnote 45 45](#) He was asked if he ever read other contracts that he signed. He stated that prior to this contract he had not read contracts that he entered.

Judge Shell: You never read them?

Mr. Torres: No, I signed -- because I believe in lawyers. ... but not now.[See footnote 46 46](#)

Torres believed that the attorney who prepared the sales agreement was employed by Lamec.[See footnote 47 47](#) He asserted that Lamec paid for attorney Eugenio Cabanillas services. Both parties stated that Cabanillas was the lending bank's attorney. Mr. Cruz, testifying for Lamec, stated that the troublesome clause 3-C was put into the sales contract by the bank. It was the bank, according to Cruz that recommended attorney Cabanillas.[See footnote 48 48](#) Carlos Lopez, an officer of the bank, was present at the April 29th meeting and represented the bank's interest.[See footnote 49 49](#) According to Cruz, clause 3-C remained in the contract over Lamec's objection. "It was a guarantee for the bank to be able ... [to] collect the money."[See footnote 50 50](#) He further testified that the bank had already distributed 545,000 and the "rest that was ready to be lent to them would be lost" if the parties were unable to agree to the terms of the agreement with the inclusion of 3-C.[See footnote 51 51](#) Cruz later said, "It was not necessary, ... immediately we were going to do everything necessary to ... change of ownership, and it was not eliminated because the bank would not allow us."[See footnote 52 52](#)

In July or August 1987 according to Cruz, the Lamec Board requested its money back from PR Tech but was told that Mr. Torres did not have the money to give back.[See footnote 53 53](#) They made the August 1987 request for the return of the money because "we thought he had

offered us an institution that was accredited and that it was not." [See footnote 54 54](#) However, since they were not able to get the money back, Lamec continued with attempts to resolve the free standing status issue. [See footnote 55 55](#)

Cruz admitted that he signed the sales contract on June 30, 1987, and Lamec paid the full purchase price on that date. [See footnote 56 56](#) However, he further explained that he felt that the actual sale took place in January when the free standing status was given. He did admit that the contract contained no clauses which conditioned the sale on the school requiring a free standing status. [See footnote 57 57](#) The essence of Lamec's position is stated in Mr. Cruz's response to the following question by Education's counsel on cross examination:

Mr. Kraut: You signed the sales contract on June 30th, you paid the purchase price of \$180,000, you satisfied the purchase price on June 30th, you notified the Puerto Rico Department of Education that the sale took place as of June 30, 1987, and that Mr. Torres was no longer responsible for the operation of the school and Lamec was, what more needed to be done to finalize the sale of the school?

The witness: What happened was ... we had notification that the school was not free standing. [See footnote 58 58](#)

Mr. Cruz acknowledged the payment of salaries of the Mayaguez employees separate from PR Tech in the following exchange:

Mr. Kraut: After you earned those funds by crediting the students' account for tuition and fees, you used those funds to pay Lamec employees' salaries, including your own, is that correct?

Mr. Cruz: To cover the expenses of the institution, including the salaries. [See footnote 59 59](#)

Lamec was accredited in January 1988 by NATTS. [See footnote 60 60](#) On February 11, 1988, NATTS classified the PR Tech Mayaguez facility as a free standing school. [See footnote 61 61](#) Change of ownership was approved by NATTS on May 17, 1988. [See footnote 62 62](#) Upon Lamec's application to Education for certification to participate in Title IV, HEA Programs, Education found Lamec not to be financially responsible and required Lamec to post a \$125,000 performance bond. [See footnote 63 63](#) A bond was approved and Lamec entered a participation agreement with Education on October 26, 1988. [See footnote 64 64](#)

The Law Concerning the Change of Ownership of the Mayaguez School

Education refers to various statutes and regulations in either the notice of termination and fine issued by Molly Hockman or the Audit Review issued June 27, 1990. Reference is made to the following statutes and regulations: 20 U.S.C. § 1070a, 20 U.S.C. § 1094(c)(1)(D), 34 C.F.R. §§ 668.4, 668.7, 668.11, 668.18, 668.82, 668.84, 668.86 (1987).

Under 20 U.S.C. 1094 (c)(1)(D), Education is authorized to prescribe regulations to provide for the termination of the eligibility of an institution or impose a civil penalty. Education sets forth its reliance upon 34 C.F.R. 668.82(c) (1987) in its notice of termination and fine to both PR Tech

and Lamec as a basis for the action taken. [See footnote 65 65](#) Education's termination and fine notices to PR Tech and Lamec rely on 34 C.F.R. 668.82, 668.84, and 668.86 (1987) to impose an eligibility termination on the two institutions and to fine both schools \$450,000. Education relies upon 20 U.S.C. 1070a and 34 C.F.R. 668.7 (1987) for the Lamec violation of statutes and regulations; however, the reference to these sections is not significant. [See footnote 66 66](#)

In addition to the references in the termination and fine notice, one must look to Education's exhibit G-3, the Office of the Inspector General audit dated June 27, 1990, to be advised of the regulatory violations. That document is incorporated by reference into the notice of termination and fine issued by Molly Hockman. Concerning the sale of the Mayaguez facility, Education cites violations of 34 C.F.R. 668.4, 668.11, and 668.18 (1987). The following is a general discussion of the cited law.

The regulation at 34 C.F.R. 668.82 (1987) states: (a) A participating institution acts in the nature of a fiduciary in its administration of Title IV, HEA programs; (b) In the capacity of a fiduciary, the institution is subject to the highest standard of care and diligence in administering the programs and in accounting to the Secretary for the funds received under those programs. Recourse for the failure to maintain the required level of care is found in 34 C.F.R. 668.82(c) (1987): "An institution's failure to administer the Title VI, HEA programs, or to account for the funds it receives under those programs, in accordance with highest standard of care and diligence required of a fiduciary, constitutes grounds for a fine, or the suspension, limitation or termination of the eligibility of the institution to participate in those programs."

The remedial regulations are: 34 C.F.R. 668.84 (1987) The Secretary may impose a fine of up to \$25,000 per violation on an institution that - (1) Violates any provision of Title IV or any regulation or agreement implementing that title; or (2) substantially misrepresents the nature of its educational program, its financial charges or the employability of its graduates...; 34 C.F.R. 668.86 (1987) - The Secretary may terminate or limit the eligibility of an institution to participate in any or all of the Title IV, HEA programs if the institution violates any provision of Title IV of the HEA.

Although the termination and fine notices to the institutions do not refer to 20 U.S.C. 1094 (c)(2)(B), Education argues in its posthearing brief that that section of the Code gives the Secretary independent authority to fine the institution for those violations. [See footnote 67 67](#) Though not cited by Education in the termination and fine notices, Education in its prehearing brief argues that 34 C.F.R. 600.31(a), change of ownership, applies. Counsel does not state the year of the regulation revision but it appears that his reference is to the Code of Federal Regulations Revised Edition as of July 1, 1988. Counsel states that in the change of ownership of a school, the school must apply to Education to be certified as financially responsible and administratively capable under standards set forth in 34 C.F.R. 668.13 and 668.14. The period of time in question raised in the facts is June 30, 1987, through June 30, 1988. [See footnote 68 68](#) Section 668.18 revised July 1, 1987, is the relevant 34 C.F.R. section to review here. The regulations applicable are those in effect at the time of the disputed facts. [See footnote 69 69](#)

Section 668.4 (1987) states that the recipient of Title IV funds must be a proprietary institution of higher education legally authorized by the State in which it is physically located and

accredited by a nationally recognized agency or association. Section 668.11 (1987) requires that a proprietary institution of higher education set forth in 668.3 (1987) or a postsecondary vocational institution set forth in 668.4 (1987) must enter into a written agreement with the Secretary in order to participate in the Title IV student assistance program. [See footnote 70 70](#)

The regulation at 34 C.F.R. 668.18 (1987), entitled change in ownership or control, in part, states:

(a) An eligible institution, or a previously eligible institution that participated in any Title IV student assistance program, that changes ownership resulting in a change in control is not considered by the Secretary to be the same institution ... (c) For purposes of this subpart, "change in ownership that results in a change in control," means any action by which a person or corporation obtains authority to control the actions of an institution. These actions may include, but are not limited to--

- (1) The transfer of the controlling interest of stock of an institution to its parent corporation;
- (2) The merger of two or more institutions;
- (3) The division of one institution into two or more institutions;
- (4) The transfer of the assets of an institution to its parent corporation; or
- (5) The transfer of the liabilities of an institution to its parent corporation.

Findings on the Change of Ownership of the Mayaguez School

The major discussion of this case concerns the sale and transfer of ownership of the Mayaguez School. In its posthearing brief, Education states that Lamec received \$403,875 in Pell Grant funds from PR Tech from August 1987 through July 1988. Both schools knew that Lamec had neither been designated by Education as an eligible institution nor had it signed a program participation agreement with Education. [See footnote 71 71](#) Education counsel argues further in his posthearing brief:

Lamec's receipt of these funds [\$403,875] and its subsequent expenditure of those funds for its own benefit is essentially equivalent to its receipt and expenditure of stolen funds knowing all the time that such funds were stolen. [See footnote 72 72](#)

As authority for the termination and fine, Education cites, notice of violations from either the Hockman notice or the Audit Findings. The various sections of the regulations cited are: 34 C.F.R. 668.4, 668.11, 668.18, 668.82, 668.84 and 668.86 (1987).

Sections 668.84 and 668.86 (1987) are directed to the law authorizing the termination and fine action. These sections are not specific regulations governing the institutions administrative requirements. They are recovery regulations relative to the remedial function brought against the violator of a regulation and directed toward the enforcement of reasonable standards required for the administration of the programs. The regulations provide the authority to either terminate or fine the institutions. The citation of these sections does not provide a basis for an adverse ruling - only the authority to terminate or fine.

The regulation at 34 C.F.R. 668.4 (1987) requires that a school be a proprietary institution of higher education licensed in the state where it is located and accredited by a nationally recognized accrediting agency or association. The facts here clearly show that PR Tech was duly authorized by the Commonwealth of Puerto Rico to act as a proprietary school. In addition, it was recognized by NATTS, a nationally recognized association. It is also shown that Lamec was not licensed nor accredited during the period in question. If it is found that PR Tech was no longer the owner of the Mayaguez facility, it would be improper for it to disburse money to students attending an institution that is not licensed or accredited.

There is no dispute that Lamec did not have a participation agreement with Education. PR Tech had a participation agreement with Education as required by 34 C.F.R. 668.11. Without licensure from the Commonwealth of Puerto Rico and/or without a participation agreement, the disbursement of funds by Lamec would be a violation of 34 C.F.R. 668.4 and/or 668.11 (1987). As was stated above, if PR Tech no longer owned the Mayaguez school, it would be improper to give funds to students attending a school with no participation agreement with Education. Lamec was not an eligible institution to disburse federal funds because it had no authority from Puerto Rico and no participation agreement with Education.

Therefore, the question to decide is - what was the result of the contractual transaction that took place on June 30, 1987? Did PR Tech own the Mayaguez facility or did Lamec own the facility? The terms of the contract appear to be fulfilled in that the money passed from buyer to seller. The parties acknowledged to the Puerto Rico Department of Education a change of ownership. While it is true PR Tech continued to double check to see if all federal funds were being managed properly, the day to day operation seems to have been transferred to Lamec. The testimony is clear; the parties believed the employees of Mayaguez to be the employees of Lamec.

Education refers to 34 C.F.R. 668.18(c)(1987) for a definition of the change of ownership or control of the Mayaguez school. "Change of ownership that results in a change of control, "means any action by which a person or corporation obtains authority to control the actions of an institution". Education states in the Audit Finding 1 at page 6, "Based on the sales contract and on PR Tech's letter to the PRDE [Puerto Rico Department of Education], there was clearly a change of ownership and control over the Mayaguez school on June 30, 1987." Even though the appearances would lead one to believe that the ownership of the school transferred, the law of the Puerto Rico Department of Education does not permit a previous owner of a school to be released from the effects of their regulations. Chapter VI(1) is set out in the stipulations of the parties at number 36. It requires:

the new owners will have to sign the corresponding obligations guaranteeing the commitments of the school pursuant to Chapter III(4), subsection(17) of this regulation. As long as the new owners do not sign such guarantees, the previous owners will continue guaranteeing jointly the commitments made ,as if no transfer of ownership had taken place.

Here, the new owners were not permitted to sign the corresponding obligations as required by the above Commonwealth regulation because the school was not a free standing or an independent school. It was merely an extension of the other PR Tech schools. According to the

local Commonwealth law, the parties had to qualify the Mayaguez facility as a free standing | school before a change of ownership could take place. The terms I of the contract were completed as far as the parties were concerned but their will alone could not transfer the school ownership without first receiving the approval of the Commonwealth. The Commonwealth has determined that it is not in the public interest to permit the previous owner to be released from its obligations of ownership until the new owner meets all requirements of the Commonwealth. The law required the former owner, PR Tech, to indemnify the new owner until the parties met all of the Commonwealth requirements. The new and the previous owner hold "jointly the commitments made as if no transfer of ownership had taken place."

Since the Mayaguez School was not free standing, Lamec could not immediately meet the requirements of the local law. By implication of the Puerto Rico law, it is found that a total and complete change of ownership could not immediately transfer to Lamec. During the period of the transfer, PR Tech and Lamec jointly guaranteed the commitments of the school. They jointly held ownership of the Mayaguez School when the 18 transfers of funds were made. Therefore, it is found that PR Tech continued in the eyes of the Commonwealth of Puerto Rico law to remain the co-owner of record during the pendency of the ownership transfer. There is no violation of 34 C.F.R. 668.18 (1987) - the change of ownership regulation.

The last section Education cites as violated is 34 C.F.R. § 668.82 (1987). This section requires the highest level of care for the holder of federal Title IV funds. The passage of the fiduciary responsibility from the previous owner to the new owner must be done without loss of any federal funds to either Education or the student recipients. The intent of the regulation is manifest in the assurances of adherence to the former institution's approved refund policy, to honor enrollment contracts, to produce profit and loss statement, and audit information. The regulation does not specifically state that the transference of funds from a selling institution to the purchasing institution is improper. What is improper, according to 34 C.F.R. 668.82 (1987) is a breach of the high standard of care required of a fiduciary. It requires use of the federal funds for the intended purpose: Pell Grant participation. An institution may not intentionally or carelessly cause harm to the federal funds.

Was the highest standard of care used by the schools when they transferred federal funds on 18 occasions before the new owner had proper accreditation and licensure from the, Commonwealth of Puerto Rico? As a fiduciary, did PR Tech violate its fiduciary responsibility by transferring funds to Lamec? There is no evidence that the funds transferred on the 18 occasions in question were misappropriated, misused, or otherwise misapplied. No evidence is available to refute statements from both PR Tech and Lamec which show the funds being used for the intended purpose - the education of the students at the Mayaguez school. In fact, the evidence shows that the Puerto Rico Department of Education regulations require a selling institution to remain obligated to the commitments of its former students until all elements of the transfer have been completed. After the Mayaguez school closing on June 30, 1987, and before Puerto Rico would permit the release of the previous owner, PR Tech continued to verify all information that Lamec forwarded concerning the draw down and disbursement of funds. Furthermore, the evidence shows that PR Tech met its responsibility to its former students and to the federal government by continuing to refund money to Education. There has been no violation of -the fiduciary responsibility under 34 C.F.R. 668.82 (1987).[See footnote 73 73](#) It is therefore

found that neither PR Tech nor Lamec violated any statute or regulation in the sale and transfer of the Mayaguez school.

B.

Facts in the License Renewal for, Flamboyán Gardens

Education did agree to withdraw Findings 2 and 3 of the audit subject to the stipulated exceptions covered in the Stipulation of Fact numbers 83, 84, and 85.

Finding number 2 alleged that PR Tech failed to renew operating licenses with the Puerto Rico Department of Education for the award years 1984-85 through 1986-87 for the courses offered. [See footnote 74 74](#) The parties stipulated that during the period of September 3, 1984, through April 1985, PR Tech offered a course in Barbering and Styling and Cosmetology and Styling at Calle 18-S 3, Urb. Flamboyán Garden, in Bayamón. Pr Tech enrolled students in the courses; and PR Tech provide⁷⁵ Title IV HEA funds to its students enrolled in that facility. [See footnote 75 75](#)

Mr. Torres testified that he had licenses issued by the Puerto Rico Department of Education to offer Barbering and Cosmetology at the Flamboyán Gardens school in Bayamón. [See footnote 76 76](#) Later, he stated that the school was also permitted to operate a facility on Betences Street in Bayamón for the same courses. The license for the Betences Street facility expired on March 2, 1986, while the Flamboyán Gardens facility expired in September of 1984. [See footnote 77 77](#) He reorganized by uniting the two operations in April 1985 at a new location. On April 22, 1985, Torres notified the Department of Public Instruction of the change of location. [See footnote 78 78](#) The Department of Public Instruction granted the permission to change the location of the license on June 4, 1985. [See footnote 79 79](#)

Torres explained the circumstance that led up to the license merger by the Puerto Rico Department of Education. He testified that he told them he purchased the building for his new location in March of 1984 but had some rehabilitation to do before they could move into it. Torres stated:

....When I explained -- that I'm going to move to a new facility because I already bought the building, ... they tell me by phone that [is] no problem. I don't have to change ... [the] license at that time, because I have ... a license in Betences for all those courses... [See footnote 80 80](#)

In September 1984 after the Flamboyán Gardens license had expired about 10% of all the students in Bayamón were enrolled in the Flamboyán Gardens classes. Torres said that some of those students were taking classes at the licensed Bayamón facility. [See footnote 81 81](#)

A Discussion of the Law Concerning the License Renewal

The notice to terminate and fine PR Tech fails to provide a specific reference in its notice of the precise violation for the violation(s) alleged above. The notice merely states:

During award years 1984-85 through During the award years 1984-85 through 1986-87, PR Tech failed to renew operating licenses from the PRDE [Puerto Rico Department of Education] for many of the courses it offered. As a result, PR Tech was not legally authorized to provide those programs in Puerto Rico , and students enrolled in those courses were ineligible to receive Title IV , HEA assistance.[See footnote 82 82](#)

Finding 2 of the Audit report cites violations of 34 C.F.R. 668.3, 668.4, and 668.6 for the failure of PR Tech to renew the license of the Bayamon Flamboyen Gardens facility. Education also cites the pertinent part of the law of the Commonwealth of Puerto Rico.[See footnote 83 83](#) Education maintains that Puerto Rico law requires an institution offering a postsecondary education course in Puerto Rico to have a license issued by the Secretary of Education of Puerto Rico in order to be legally authorized to provide that course in Puerto Rico.[See footnote 84 84](#)

PR Tech had the responsibility to fulfill its contracts to the students enrolled at Flamboyen Gardens in Bayamon. The testimony indicates that the institution notified the Puerto Rico Department of Education of the relocation of its campus at Flamboyen Gardens. While some form of written verification from the Puerto Rico Department of Education would have been more creditable than the hearsay testimony given by the President of PR Tech, the telephonic decision given by the Puerto Rico Department of Education is unrefuted. Furthermore, 34 C.F.R. 668.18 (c)(2) (1987) states:

...change in ownership that results in a change in control, means any action by which a person or corporation obtains authority to control the actions of an institution. These actions may include, ... (2) the merger of two or more institutions

The action taken by PR Tech was a reorganization of the two facilities in Bayamon. They were merged into one new building. When the two campuses or institutions merged, the change of control from the Flamboyen Gardens facility merged into the Betences facility. The Betences facility had a valid license to operate during the period from September 3, 1984, through April 1985. It is found that Education has failed to show any facts to refute the merger of the two facilities. Nor has Education shown a violation of 34 C.F.R. 668.18 (1987).

Conclusion

Education has failed to show any violations in the sale of the Mayaguez school or any violations for PR Tech's failure to renew the license of the Flamboyen Gardens license. Finally, Education has failed to prove that either PR Tech or Lamec should be terminated from participation in the Title IV programs.

Issued: May 6, 1991
Washington, D. C. Daniel R. SHELL
Administrative Law Judge

[Footnote: 1](#) 1 Each notice recites Education's reliance on 34 C.F.R. 668.84 and 34 C.F.R. 668.86 for the schools termination from Title IV programs of the HEA of 1965, as amended, under 20 U.S.C. 1070 et seq. and to be fined.

[Footnote: 2](#) 2 Ed. Ex. G-3, at 7.

[Footnote: 3](#) 3 Stipulations of Fact, Received December 4, 1990, Pg. 16.

[Footnote: 4](#) 4 This is the only part of Finding 2 that remains as an issue.

[Footnote: 5](#) 5 The notice to PR Tech sets forth fines in addition to the termination of PR Tech. Education initially intended to fine PR Tech \$781,000 for various violations set out and an additional fine of \$450,000 for the 18 disbursements requested, received, and transferred for students at the Mayaguez Campus. In the notice to terminate, Education alleged that PR Tech was not authorized by the Puerto Rico Department of Education to use Title IV programs, yet requested and received \$528,940 in Pell Grant Program funds and falsely certified GSL Program loans which resulted in students receiving \$182,164 in GSL loans. For PR Tech's alleged false certification of 79 students on the GSL Program loan application, Education requests fines of \$1,000 for each false certification, a total of \$79,000. Education requests fines for PR Tech's improper disbursement of Pell Grant funds to 252 students at a rate of \$1,000 for each student, or \$252,000. Education also alleged that PR Tech failed to insure that the non-Federal share of CWS wages were paid by a non-profit organization employing PR Tech's students. The notice from Molly Hockman, Division of Audit and Program Review, is an ambiguous document which expresses confusion as to the penalties sought. It is of assistance in sorting out Education's position on the amount of fine requested to examine the conclusion found in section II at page 4 of the notice to terminate. It must be read in conjunction with Finding 2 and 3 of the Audit letter to PR Tech dated June 27, 1990. (Ed. Ex. G-3) However, Education's agreement to drop Findings 2 and 3 subject to the exceptions of stipulations numbered 83, 84, and 85 removes from the dispute some of the problem in ascertaining Education's demand. (See Stipulations of Fact, Pg. 16) Some findings of fact based on stipulations 83, 84, and 85 must still be resolved and will be decided in the body of this decision.

[Footnote: 6](#) 6 The latter case had been assigned to another Administrative Law Judge but that case was consolidated into one proceeding in the interest of effective adjudication of both cases.

[Footnote: 7](#) 7 Education's pre-hearing brief, submitted October 22, 1990, Pg. 1.

[Footnote: 8](#) 8 See the termination notice to Lamec, dated July 17, 1990, Pg. 2 § 1.

[Footnote: 9](#) 9 Education's posthearing brief, submitted February 15, 1991, Pg. 18.

[Footnote: 10](#) 10 PR Tech's posthearing brief Pg. 4-5.

[Footnote: 11](#) 11 PR Tech's posthearing brief Pg. 6; Tr. Pg 70.

[Footnote: 12](#) 12 Tr. Pg. 70.

[Footnote: 13](#) 13 See Pg. 8 of the posthearing brief submitted February 21, 1991.

[Footnote: 14](#) 14 Lamec Ex. 4 pg. 1 states "a branch or extension facility must exist for two years with all of the services normally expected of a free standing school and must operate in its approved status for one of the two years before being eligible to apply for free standing school status."

[Footnote: 15](#) 15 Ed. G-8, certification of the transfer of ownership.

[Footnote: 16](#) 16 Lamec's posthearing brief Pg. 3.

[Footnote: 17](#) 17 Tr. Pg. 36.

[Footnote: 18](#) 18 Lamec Ex. 2; Stipulation number 4.

[Footnote: 19](#) 19 The services include: recruiting students for the three schools located in Bayamon, Mayaguez and Arecibo, Puerto Rico; providing advice on programs of financial assistance, financial consulting, and accreditation by the Puerto Rico Department of Education and the Federal Department of Education; creating administrative and financial controls; providing advice on the structural and functional design of schools; executing market studies to determine courses of major demand; creating five curricula for courses of major demand in Puerto Rico; accrediting new courses; organizing teaching levels; preparing an institutional catalog in conformity with the accrediting agency on admission, registration, personal finances and contracting; preparing rules and regulations of the students and services for student counselling; placing and evaluation of students and for the process of self-evaluation; training institutional personnel to perform all services.

[Footnote: 20](#) 20 Lamec's Ex. 2. Pg. 5. The stipulations of the parties submitted incorrectly state that clauses nine and ten of that contract provide for a purchase option agreement in favor of Lamec for a period of six months. The terms state that Lamec will have a first option after six months of this present contract - meaning an unrenewed service contract. It would appear that Lamec was given a right of first refusal in the purchase of the Mayaguez school and not an option for six months. However, when the parties executed the sixty day agreement, PR Tech was obligated to an option to purchase for a sixty day option period.

[Footnote: 21](#) 21 Lamec's Ex. 3 and Ed. Ex. G-6 state April 29, 1987. However, Lamec's exhibit 7 states that the contract was executed on January 29, 1988. Much discussion and confusion has been generated by Lamec's Ex. 7 - the date of the sales contract being changed to the 29th of January 1988. But stipulation number 16 at 3 states that the purported sale took place on April 29, 1987. However, Lamec continues to argue that they did not get what they had contracted for until January 29, 1988, the date of their accreditation.

[Footnote: 22](#) 22 Stipulations submitted December 4, 1990, Pg. 3.

[Footnote: 23](#) 23 Lamec Ex. 25, Pg. 2 translations, Lamec Ex. 24, and PR Tech Ex. 7.

[Footnote: 24](#) 24 Education counsel asked a series of questions on this issue. See testimony on page 146 of the transcript. The admission appears on page 147. Later on Page 150, line 19, of the transcript, Torres admits that the employees of the Mayaguez campus were not employees of PR Tech. He also admitted that PR Tech no longer paid the rent on the Mayaguez facility. When asked, "Did you pay rents on any of the facilities used by the Mayaguez campus after... July 1st...?" He responded, "They pay." Tr. Pg. 150.

[Footnote: 25](#) 25 Stipulation number 32, submitted December 4, 1990, Pg. 7; also Ed. Ex. G-9.

[Footnote: 26](#) 26 The Puerto Rico Department of Education was notified of the change of ownership of the Mayaguez campus effective June 30, 1987. Stipulation number 31, submitted December 4,

1990.

[Footnote: 27](#) 27 Tr. Pg. 29; Sales Contract, Ed. Ex. G-6.

[Footnote: 28](#) 28 Stipulations number 48 through 76, submitted December 4, 1990, Pgs. 10-12 .

[Footnote: 29](#) 29 Ed. Ex. G-4 Pg. 2; Ed. Ex. G-5 Pg. 2; Tr. Pg. 32-33. Education did not certify Lamec until October 26, 1988, when Lamec posted a \$125,000 performance bond. Also see Stipulation number 77, submitted December 4, 1990, Pg. 12; the strained testimony of Torres on Tr. Pg. 91-93.

[Footnote: 30](#) 30 Tr. Pg. 150.

[Footnote: 31](#) 31 Tr. Pg. 90.

[Footnote: 32](#) 32 Stipulation number 36, submitted December 4, 1990, Pg. 8.

[Footnote: 33](#) 33 Tr. Pg. 174.

[Footnote: 34](#) 34 Tr. Pg. 17.

[Footnote: 35](#) 35 See Tr. Pg. 17 for the discussion on payments; Tr. Pg. 209.

[Footnote: 36](#) 36 Tr. Pg. 195.

[Footnote: 37](#) 37 Tr. Pg. 196.

[Footnote: 38](#) 38 Tr. Pg. 113-114.

[Footnote: 39](#) 39 Tr. Pg. 115.

[Footnote: 40](#) 40 Lamec Ex. 4 at 1, last paragraph.

[Footnote: 41](#) 41 Tr. Pg. 123.

[Footnote: 42](#) 42 Ed. Ex. G-6, Pg. 2-3.

[Footnote: 43](#) 43 Tr. Pg. 178; Tr. Pg. 197.

[Footnote: 44](#) 44 Tr. Pg. 133.

[Footnote: 45](#) 45 Tr. Pg. 181.

[Footnote: 46](#) 46 Tr. Pg. 198. *The inflection in his voice implied that since this experience he now reads all of his contracts.*

[Footnote: 47](#) 47 Tr. Pg. 86.

[Footnote: 48](#) 48 Stipulation number 38, submitted December 4, 1990, at Pg. 8.

[Footnote: 49](#) 49 Tr. Pg. 234.

[Footnote: 50](#) 50 Tr. Pg. 235.

[Footnote: 51](#) 51 Tr. Pg. 235.

[Footnote: 52](#) 52 Tr. Pg. 236.

[Footnote: 53](#) 53 Tr. Pg. 241.

[Footnote: 54](#) 54 Tr. Pg. 257. *The warranty argument may be appropriate in the Commonwealth forum but it is not relevant to this proceeding.*

[Footnote: 55](#) 55 PR Tech at Mayaguez, Puerto Rico was accredited by NATTS in November 1987. See Lamec's Ex. 6.

[Footnote: 56](#) 56 Tr. Pg. 254.

[Footnote: 57](#) 57 Tr. Pg. 256-257.

[Footnote: 58](#) 58 Tr. Pg. 284.

[Footnote: 59](#) 59 Tr. Pg. 298.

[Footnote: 60](#) 60 Stipulation number 37, submitted December 4, 1990, Pg. 8.

[Footnote: 61](#) 61 Lamec Ex. 8.

[Footnote: 62](#) 62 Stipulation number 40, submitted December 4, 1990, Pg. 9.

[Footnote: 63](#) 63 Stipulations numbers 43-44, submitted December 4, 1990, Pg. 9.

[Footnote: 64](#) 64 Stipulation number 46, submitted December 4, 1990, at Pg. 9-10.

[Footnote: 65](#) 65 Ed. Ex. G-4, Pg. 3; Ed. Ex. G-5, Pg. 3.

[Footnote: 66](#) 66 Ed. Ex. G-5, Pg. 2 refers to 34 C.F.R. 668.7 (1987) which defines an independent student. The relevance of this regulation is not obvious and will not be considered further. Education's reliance on 20 U.S.C. 1070a as a foundation is based on twenty five pages of the United States Code Annotated and does not provide specific reference of the law governing the institutional eligibility to adequately apprise Lamec or this tribunal of what statutory law has been violated. General reference to 20 U.S.C. 1070a is insufficient and will not be considered due to the vague nature of the alleged violation.

[Footnote: 67](#) 67 Posthearing brief, submitted February 15, 1991, Pg. 1516.

[Footnote: 68](#) 68 See Background of this discussion in an earlier portion of this decision at Page 1-2.

[Footnote: 69](#) 69 In Re Temple University, Dkt No. 89-26-S, U.S. Department of Education, (March 13, 1990), at 5-7.

[Footnote: 70](#) 70 Confusion is created in 34 C.F.R. 668.11(a)(2) and (3) due to an improper reference to sections of the regulations which define proprietary institutions of higher education and postsecondary vocational institutions. However, the institutions have not relied on this confusion as a defense to their actions or alleged error by Education. Furthermore, the essence of Education's position is that Lamec was not an eligible institution at the time of the transfer of the funds from PR Tech to Lamec, nor had Lamec a participation agreement signed by the Secretary of the Department of Education.

[Footnote: 71](#) 71 Education posthearing brief, submitted February 15, 1991, Pg. 12.

[Footnote: 72](#) 72 Post-hearing brief, submitted February 15, 1991, Pg. 14.

[Footnote: 73](#) 73 The testimony devotes much time to each institution's opinion of the status of the legal representation of attorney Eugenio Cabanillas. It is clear from the evidence that Counsellor Cabanillas represented the interests of the Banco Popular. The testimony of Mr. Torres concerning his reliance on attorney Cabanillas and the representations of the purchasers seems, at best, naïve. While one may conclude that it would have been prudent to employ legal counsel prior to the closing, that issue is not relevant to the decision in this case.

[Footnote: 74](#) 74 See termination notice to PR Tech dated July 17, 1990, Pg. 3.

[Footnote: 75](#) 75 Stipulation of Fact, Received December 4, 1990, numbered 83, 84, and 85, at Pg. 13.

[Footnote: 76](#) 76 PR Tech Ex. 13.

[Footnote: 77](#) 77 PR Tech Ex. 15.

[Footnote: 78](#) 78 PR Tech Ex. 16.

[Footnote: 79](#) 79 Tr Pg. 107.

[Footnote: 80](#) 80 Tr. Pg. 105.

[Footnote: 81](#) 81 Tr. Pg. 107.

[Footnote: 82](#) 82 E. Ex. G-4, at 3.

[Footnote: 83](#) 83 Ed. Ex. G-3. Pg 12

[Footnote: 84](#) 84 Education's prehearing brief submitted October 22, 1990, Pg. 13.
