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

In the Matter of

DRAUGHON COLLEGE,

Respondent

Docket No. 93-4-ST

Student Financial Assistance Proceeding

DECISION

Appearances:
Yolanda R. Gallegos, Esq., and Duane Pugh, Esq., of Dow, Lohnes and Albertson, Washington, D.C., for Respondent.

Donald C. Phillips, Esq., of the Office of the General Counsel, U.S. Department of Education, for the Office of Student Financial Assistance Programs.

Before:
Judge Ernest C. Canellos

PROCEDURAL HISTORY

Draughon College (Draughon), of Oklahoma City, Oklahoma, is a post-secondary institution offering a variety of programs at two locations, Oklahoma City and Lawton. It participates in the Pell Grant Program, the Federal Family Education Loan Programs, formerly the Guaranteed Student Loan Programs, the Federal Supplemental Educational Opportunity Grant Program, the Federal Perkins Loan Program, and the Federal Work Study Program, all authorized under Title IV of the Higher Education Act of 1965, as amended (HEA). These programs are administered by the Office of Student Financial Assistance Programs (SFAP), United States Department of Education (ED).

Draughon is one of a number of postsecondary institutions which are wholly-owned by Fischer Educational System, Inc. (Fischer). Fischer has elected to maintain and file consolidated financial statements for itself and all its subsidiaries and has submitted such consolidated statements to ED in satisfaction of regulatory requirements of the Title IV Programs. Currently, Fischer acts as Debtors-in-Possession under a consolidated Chapter 11 Petition in Bankruptcy, filed in the United States Bankruptcy Court of the Middle District of Tennessee.

On December 15, 1992, SFAP issued a notice advising Draughon of an intent to terminate its eligibility to participate in federal student financial programs under Title IV of the HEA, and to impose a fine of $259,000. On January 7, 1993, Draughon timely requested a hearing and the

case was routinely assigned to Judge Ernest C. Canellos. Briefs and evidentiary submissions were made, and an evidentiary hearing was held in Washington D.C., on June 17, 1993. At the conclusion of the evidentiary hearing, the parties were authorized to file post-hearing briefs, which they did.

OSFA based its termination and fine action on the findings in a program review conducted at Draughon by ED's Regional Office in Dallas, Texas, from December 16-20, 1991. Based upon their review of student files and other pertinent information, program reviewers determined that Draughon had committed the following violations of program regulations: (1) untimely GSL refunds to lenders (34 C.F.R. § 682.607(c)(1); (2) failure to meet the ability-to-benefit requirements (34 C.F.R. § 668.7(b)(l); (3) failure to implement a default reduction plan (34 C.F.R. Part 668, Appendix D); (4) maintenance of excess cash on hand; (5) failure to meet consumer information requirements (34 C.F.R. § 668.43), and (6) failure to meet standards of financial responsibility (34 C.F.R. § 668.13).

DISCUSSION

- I -

Financial responsibility is a condition of participation in the Title IV programs. As a result, an institution is required to demonstrate that it is financially responsible to be admitted and continue to participate in those programs. 34 C.F.R. § 668.13. If an institution fails to make the requisite demonstration of financial responsibility, its eligibility to participate in Title IV programs must be terminated.

ED has met its burdens of proof and persuasion in this case by showing that Draughon is not financially responsible. It does so by showing that Draughon does not meet the required one-to-one ratio of current assets to current liabilities. 34 C.F.R. § 668.l3 (c) (2). Fischer has chosen to submit consolidated financial statements for itself and all its subsidiaries. A review of the consolidated balance sheets of Fischer and its subsidiaries revealed that on the Draughon balance sheet, listed as a current asset, was an inter-company receivable from Fischer for approximately $2 million. It that receivable is counted as a current asset, Draughon meets the current asset test. If not so counted, Draughon falls short of qualifying under that test and, therefore, is not financially responsible.

By definition, a current asset is one that, in the case of a receivable, will be repaid in one year. It is clear that this receivable from Fischer is not a current asset. It is not likely to be returned given the financial status of Fischer and, even if it were possible that it would be returned, it would certainly not be returned within one year.

Draughon asserts that ED can not look behind the listing of the receivable as a current asset, since their auditor listed it as such without comment. ED, on the other hand, argues that they must make an independent evaluation of the current asset status, and, having done so, has determined that it clearly is not such an asset. I agree with ED's position that they can independently assess the categorization of assets for purposes of determining compliance with

the standards of financial responsibility under Title IV and agree that this receivable is not a current asset.

- II -

Schools participating in the federal student financial assistance programs are required to make refunds to lenders within 60 days of the accrual of a refund entitlement. 34 C.F.R. § 682.607 (c) (l). Program reviewers determined that some refunds in their sample of student files were paid late. As a result, Draughon was requested to provide information on all refunds paid in the previous three award years. Based on inputs from Draughon, program reviewers determined that refunds were made late in 215 instances. At the hearing, Draughon argued that: the information they provided ED was incorrect because of unclear instructions from ED reviewers; if any late refunds were made, it was the fault of the corporate parent, Fischer, who actually paid refunds; and, in either case, such error should not be attributable to it.

Contrary to Draughon's claim, my review indicates the instructions they received were adequate, given the clear mandate of the regulations. Also, the inner workings of a corporate financial system can not act as a defense to a charge of making late refunds, since Draughon, as signatory to the Program Participation Agreement, is ultimately responsible for those refunds. It is also significant that making late refunds was a repeat finding.

- III -

A student who does not possess a high school diploma or its equivalent can only be admitted on the basis of an ability-to- benefit (ATB) from the education or training to be received. To be admitted on that basis, the ATB student must be administered a nationally recognized or industry-developed test. 34 C.F.R. § 668.7 (b) (l). Evidence reveals that 182 ATB students were admitted on the basis of an "Entrance evaluation which was neither nationally recognized nor industry-developed, but, rather, was an adaptation from another test. Of those students, 127 dropped out before completing the program.

Draughon's argument that the test was derived from a qualified test is insufficient to satisfy the specific requirements of the program regulations.

- IV -

As part of its responsibilities under its Participation Agreement, Draughon is required to maintain cash to pay Pell Grants at a level authorized in accordance with ED's Recipient Guide. That guide specifies that cash on hand should not exceed a three day requirement. Draughon does not dispute that it exceeded that limit, but argues that there is no specific statutory or regulatory authority requiring adherence to this limit on cash-on-hand and, as such, can not be the basis of an adverse finding. There is, however, clear authority for basing an action on a violation of the Program Participation Agreement. See In the Matter of Macomb Community College, U.S. Dept. of Ed., Docket No. 91-80-SP (June 28, 1993).

- V -

Evidence was presented on the issues of failure to fully implement a Default Reduction Plan and unmet consumer information requirements. In each instance, the evidence was insufficient to meet ED's burdens of proof and persuasion.

TERMINATION ISSUE

The procedures for initiating the termination of eligibility of an institution to participate in the Title IV, HEA programs are set forth at 34 C.F.R. § 668.86. Section 668.86(a) provides:

The Secretary may terminate or limit the eligibility of an institution to participate in any or all Title IV, HEA programs, if the institution violates any provision of Title IV of the HEA or any regulation or agreement implementing that Title.

ED seeks termination for Draughon's violations of program regulations, the most serious of which is the failure to satisfy the factors of financial responsibility as enumerated in 34 C.F.R. § 668.13. The record clearly supports such a characterization. In addition, the record supports the allegations of failure to timely pay refunds, violation of the ATB requirements, and maintenance of excess cash.

FINE CONSIDERATIONS

In addition to the proposed termination of eligibility, ED seeks a fine of $259,000 pursuant to § 487 (c) (3) (B) of the HEA, and 34 C.F.R. 668.84. ED describes Draughon as a large institution because its students received more than $4.5 million in student aid in the 1990-91 award year. I agree with that categorization. No attempt is made by ED to label the gravity of the violations other than to point out that they are repeat write-ups.

In reviewing the proposed fines, I note the Secretary's Decision in Puerto Rico Technology and Beauty College, and Lamec, Inc., U.S. Dept. of Ed., Docket Nos. 90-34-ST & 90-38-ST (June 11, 1993). There the Secretary iterates the statutory and regulatory requirement that in setting an appropriate fine, one must take into account the gravity of the violations and the size of the institution.

A total fine of $235,500.00 is requested by ED for the categories of violations sustained above. When assessing an appropriate "punishment" for the violation of program regulations, it is the total punishment that must be judged as appropriate. I believe a fine of $117,750.00 ($250 per refund violation and $500 for each ATB violation) is appropriate in this case. ED proposed no fine for the excess cash violation. The sum of this fine seems to be reasonable and just in light of the simultaneous imposition of the most severe sanction available, that of termination.

FINDINGS

On the basis of the evidence, I FIND the following:

Draughon failed to make timely refunds on 217 occasions.

Draughon violated ATB provisions on 182 occasions.

Draughon violated provisions regarding the maintenance of excess cash-on-hand.

Draughon does not meet standards of financial responsibility.

Draughon did not violate the provisions dealing with the implementation of a Default Reduction Plan or consumer information.

Draughon's participation in federal student financial assistance programs should be terminated.

A fine in the amount of $117,750.00 is warranted.

ORDER

On the basis of the foregoing it is hereby--

ORDERED, that the eligibility of Draughon College to participate in the student financial assistance programs under Title IV of the Higher Education Act of 1965, as amended, is terminated.

ORDERED, that Draughon College immediately and in the manner provided by law pay fines in the total amount of $117,750.00 to the United States Department of Education.

Judge Ernest C. Canellos

Issued: November 5, 1993
Washington, D.C.

SERVICE

On November 5, 1993, a copy of the attached document was sent by certified mail, return receipt, to the following:

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