UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF HEARINGS AND APPEALS

IN THE MATTER OF
ILLINOIS MEDICAL TRAINING CENTER,
Chicago, IL,

Respondent

Docket No. 93-87-SA

Student Financial
Assistance Proceeding

DECISION

ALBERT C. EBERT, Chairman, for Respondent.
STEVEN Z. FINLEY, Esq., for Student
Financial Assistance Programs of the
United States Department of Education.

Before
Paul J. Clerman, Administrative Law Judge:

Respondent, Illinois Medical Training Center (IMTC), is a for-profit proprietary school at Chicago, IL, that entered into an institutional participation agreement with the United States Department of Education (ED) pursuant to 34 CFR 668.12 that permits IMTC's students to receive federal student financial aid under the provisions of Title IV of the Higher Education Act of 1965, as amended (HEA) . To commence or to continue participation in Title IV HEA programs, an institution such as IMTC must demonstrate that it is administratively capable of meeting the requirements for participation in such programs as set out in standards of administrative capability at 34 CFR 668.14. Such institutions, while participating in Title IV HEA programs., must act in the nature of a fiduciary in the administration of those programs, and in that capacity the institutions are subject to the highest standard of care and diligence in administering those programs and in accounting to ED's Secretary for the funds received under those programs, as required under 34 CFR 668.82(a) and (b).

Included in the Title IV HEA programs in which IMTC has participated are the Pell Grant (PELL), Supplemental Educational Opportunity Grants (SEOG), College Work Study (CWS), Perkins Loans (PERKINS), Family Education Loan (FEL) which was formerly the Guaranteed Student Loan (GSL), Stafford Loan (STAFFORD), Supplemental Loans for Students (SLS), and Federal PLUS (PLUS).

In a letter/notice sent July 1, 1993, by the Audit Resolution Branch of ED's Office of Postsecondary Education Institutional Monitoring Division, IMTC was issued a Final Audit Determination (FAD) in accordance with 34 CFR 668.112. The FAD contained a series of determinations based on an audit report issued February 14, 1992, by the Inspector General for Audit of ED's Region V (the RIGA audit), and on an audit report issued April 20, 1990, on behalf of IMTC by a certified public accountant (the CPA audit) . Among other things, IMTC was directed in the FAD to reimburse ED in the total amount of $5,887,979 as a result of findings in the RIGA and CPA audits. IMTC was advised that its failure to conform with Title IV HEA requirements in the future may lead to an adverse administrative action, including, ultimately, termination of its eligibility to participate. IMTC was notified of its right to appeal the FAD, and in due course, by letter dated August 13, 1993, IMTC submitted its appeal, requesting a hearing in the matter. On August 26, 1993, the undersigned Administrative Law Judge was designated to be the hearing official. I issued a procedural order on November 23, 1993, setting the matter for hearing, such hearing to consist of the filing of briefs and related documents by the parties.

A brief and related documents were timely filed by ED's Office of Student Financial Assistance Programs (SFAP) . IMTC had notified me by letter dated September 7, 1993, that it "no longer has full time staff on a daily basis," and had furnished the addresses of its President, CPA and owner for the receipt of correspondence. My procedural order was served on IMTC's owner/Chairman. IMTC has failed to file a brief in this proceeding.

The CPA audit examined IMTC's systems of internal controls for the two-year period ended June 30, 1989, and in connection with that examination selected records and transactions in the PELL, GSL, PLUS, SEOG, and CWS programs were tested. The testing disclosed instances of noncompliance with governing laws and regulations. The CPA audit found that during that two-year period IMTC did not in all material respects administer those programs in compliance with laws and regulations, including those pertaining to financial reports. The CPA audit found that, as of June 30, 1989, IMTC's percentage of defaulted loans was 35.76 percent, a default rate that was excess of ED's guidelines. The excessive default rate is attributed to the making of loans to students who are not capable of assuming the obligations of indebtedness. There was also found an excessive student drop rate, 43 percent as of June 30, 1988, and 38 percent as of June 30, 1989. These rates were found to be excessive when compared with the total number of enrolled students, based on criteria established by ED. The excessive drop rates are attributed to the enrollment of students without adequate prior testing and students who lack the ability and aptitude for completing their courses of instruction.

It was found in the RIGA audit that during the period July 1, 1987, through June 30, 1990, IMTC disbursed $3,162,292 in student aid funds, and that during approximately the same time period IMTC was certified as eligible for about $4.6 million in GSL funds. The RIGA audit reviewed IMTC's institutional eligibility based on ability-to-benefit criteria for the two-year period ended June 30, 1989 and for an additional eleven-month period ended May 24, 1991. Based on cash management criteria IMTC was examined for a one-year period ended June 30, 1989, and for a nine-month period ended March 31, 1991. In the course of the review auditors examined selected administrative and accounting records, IMTC policies, licensing and accreditation documents, bank and attendance records, audit reports and working papers. Various IMTC officials, teachers, and students were interviewed, as were others, and field work was performed at IMTC's facility and at the facility of its accountant. The PELL files of randomly-selected students were reviewed as were student files from class start rosters. All reviews are stated to have been conducted in accordance with generally-accepted standards.

Significant IMTC internal administrative controls were assessed and classified in the RIGA audit into certain categories, and material weaknesses were identified which affect adversely IMTC's ability to administer student financial aid programs. The results reached in the RIGA audit were that IMTC (a) admitted as regular students persons who were beyond the age c: compulsory school attendance and did not possess a high school diploma or its equivalent without first properly determining their ability to benefit; (b) overstated the length of its programs; (c) demonstrated weaknesses in administering student financial aid programs; and (d) demonstrated weaknesses in its management of funds from Title IV HEA programs. It was concluded in the RIGA audit that IMTC did not meet statutory and regulatory standards pertaining to institutions of higher education, and, thus was ineligible to participate in Title IV HEA programs.

The RIGA audit recommended that IMTC be directed to establish and implement procedures to correct the deficiencies found, and additionally to: (1) refund to ED certain questioned costs aggregating $3.2 million; (2) purchase from GSL lenders costs of $4.6 million and refund to ED related interest and allowances; and (3) remit to ED $4,782 in interest-related excess cash and lost income on PERKINS accounts. Regarding overstated program lengths, it was recommended that IMTC be instructed to correctly calculate the lengths of its programs, to quantify past overlengths, and to make future awards based on correct lengths. With regard to program administrative weaknesses, it was recommended that IMTC be instructed to establish and implement policies and procedures to properly administer Title IV HEA programs. It was recommended in connection with cash management that IMTC be instructed to develop and implement adequate cash management procedures that meet federal requirements. The RIGA audit also recommended that the Office of Postsecondary Education consider taking appropriate administrative action to protect the interests of student program participants and of the taxpayers.

The FAD concurred with findings in the CPA and RIGA audits. The FAD noted the default rate found in the CPA audit, 35.76 percent, and pointed out that the PERKINS program requires that in order for an institution to receive any federal capital contribution (FCC) its default rate may not exceed 15 percent, and that in order to receive the full amount of FCC the default rate must not be more than 7.5 percent. The FAD also noted that IMTC has discontinued the use of PERKINS funds, and the FAD concurred with the recommendation in the CPA audit that IMTC must assign all such loans to ED and return all FCCs that were received during the award years. With regard to the excessive dropout rates found in the CPA audit, the FAD pointed out that under 34 CFR 668.15 a high withdrawal rate is considered to be an indication of impaired administrative capability on the part of an institution when: (a) more than 33 percent of the enrolled regular students withdraw during the academic year in an institution that has a common academic year for the majority of its students, or (b) in an institution that does not have a common academic year, more than 33 percent of the enrolled regular students withdraw during. any eight-month period. The FAD noted that ED's Institutional Participation Division had been advised of IMTC's high withdrawal rate, which fact is to be considered in subsequent evaluations of IMTC's administrative capability .

The FAD notes that 34 CFR 668.14 provides that to participate in Title IV HEA programs an institution must be able to adequately administer those programs, and that 34 CFR 668.23 provides that a participating institution must perform financial and compliance audits of its programs. Further, as noted, the student assistance general provisions in Part 668 of 34 CFR in section 674.19 (PERKINS), 675.19 (CwS), 676.19 (SEOG), and 690.81 (PELL), require that an institution: (a) must establish and maintain on a current basis financial records that reflect all program transactions, general ledger control accounts, and related subsidiary accounts that identify each program transaction and separate those from all other institutional activity; (b) keep intact and accessible all records of receipt and expenditure of federal funds; and (c) reconcile at least on a monthly basis fiscal records in PERKINS, CWS and SEOG programs. The FAD states that sound business management procedures dictate that PELL records be reconciled monthly as well.

The FAD indicates that IMTC was required throughout the entire period of its participation in Title IV HEA programs to have procedures in place to ensure that it was in compliance with regulatory requirements, but that IMTC failed to retain accounting records for its PELL, SEOG, PERKINS, CWS, and STAFFORD programs and failed to have those programs audited The FAD concluded that all funds received by IMTC for those programs for the 1988 and 1989 award years must be disallowed. In connection with the CPA audit, the FAD calculates IMTC's repayment liability for PELL, SEOG, CWS, and PERKINS funds to aggregate $2,001,221. Based on IMTC's latest (1990) cohort default rate of 47.7 percent, the FAD estimates ED's actual losses on account of defaults and excessive subsidies paid to lenders for ineligible students' STAFFORD loans aggregate $1,551,680. Thus, on the basis of the CPA audit, the FAD concludes that ED must be reimbursed by IMTC in the amount of $3,552,901.

After review of the RIGA audit, the FAD concluded that IMTC did not properly determine the ability to benefit for students who did not have a high school diploma or its equivalent, as required under 34 CFR 600.11. It was found that students admitted during the 3-year period ended June 30, 1990, and ineligible, were disbursed some $3.2 million in PELL, SEOG, OWS and PERKINS funds, and that between July 1, 1987, and November 30, 1991, IMTC certified $7.1 million in GSL funds. In STAFFORD funds, the FAD found, IMTC disbursed more than $1.6 million to ineligible students, an based on IMTC's cohort default rate the FAD estimated that ED incurred an actual loss of $1,051,058. Combined with an actual loss to ED of $739,200 in PELL, SEOG, CWS and PERKINS funds disbursed to ineligible students, the FAD calculates that IMTC must reimburse ED in the aggregate amount of $1,790,258 in connection with finding No. 1 of the RIGA audit. With regard to the $739,200 amount, however, the FAD notes that IMTC can reduce its liability by omitting funds included in the $3,552,901 amount to be reimbursed under the CPA audit.

Based on the auditor's sample results which showed that 262 students out of 570 received an average of $2,060 each in PELL funds for which they were not entitled, the auditor extrapolated this sample to conclude the IMTC students received an aggregate amount of $539,720 which IMTC must repay on account of improper expenditures identified in the audit. The FAD also found that IMTC must remit to ED a total of $5,100 for cash management deficiencies, as follows: (a) $4,217 in interest imputed on excess cash balances during the 1-year period ended June 30, 1990, for the reason that funds drawn down too far in advance of IMTC's needs or otherwise idled in its accounts deprives ED of interest benefits it would receive from use of those funds: (b) $565 in interest, because IMTC did not keep PERKINS funds in an interest-bearing account as required under 34 CFR 674.19(b) (4) (i) during the period July 1, 1988, through March 31, 1991; and (c) $318 in bank service charges incurred on IMTC's PERKINS account during a 2-year period and on its CWS account during a 1-year period. IMTC must refund this amount to ED or demonstrate that unspent funds were available to pay these charge from IMTC's administrative cost allowances.

The FAD recapitulates the funds that are due to ED from IMTC based on the two audits, as follows:

The CPA audit:	
Finding No. 3 - - -	$2,001,221
	1,551,680
	$3,552,901 total
The RIGA audit:	
Finding No. 1 - - -	$1,051,058
	739.200
	$1,790,258 total
Finding No. 3 - - -	$539,720
Finding No. 4 - - -	$5,100

The FAD noted that in the RIGA audit the auditors identified a number of administrative weaknesses which, to them, indicate an impaired ability on the part of IMTC to properly administer Title IV HEA programs. Included among the approximately ten categories identified were: failure to adequately track student attendance; charging higher tuition amounts than were listed on signed enrollment agreements; charging student ledger accounts for transportation costs and offsetting these charges with Title IV HEA funds, contrary to governing regulations; failure to make refunds to students promptly; failure to calculate student refunds on a pro rata basis; and awarding diplomas to some students who dropped out before completing the programs in which they were enrolled.

On brief, SFAP stresses that in order to continue to participate in Title IV HEA programs IMTC must demonstrate that it is capable of meeting the obligations for such participation as laid down in 34 CFR 668.14 et sea., including the requirement that IMTC administer those programs with adequate checks and ability-to-benefit testing, on its face according to SFAP was actually prepared for a completely different school. Another such document which describes itself as an analysis of reasons for withdrawal and dropped students and related factors, appears to attempt to justify IMTC's practice of enrolling students that lack a high school diploma or its equivalent on the ground that "preventing continuing education on grounds of lack of formal educational background is virtual assurance of perpetuated economic and educational depravity [sic] - a lockup from which persons without GEDS are not likely to escape even though the evidence supports their Ability to Benefit." In these and other documents, according to SFAP, IMTC attempted to lay a foundation for its decision to boost student enrollment by accepting students who lack high school diplomas or its equivalent. Viewed in context with low admissions standards adopted for such students, SFAP sees support for the conclusions in the audits that IMTC failed to administer properly its ability-to benefit testing.

SFAP alleges on brief that throughout the review process, although given. the opportunity to do so, IMTC failed to show that it has properly expended the Title IV HEA funds involved in this proceeding. SFAP alleges that ED, on the other hand, has met its obligation to establish the reasons for which IMTC must repay to ED the Title IV HEA funds that IMTC has improperly taken and expended. SFAP contends that at no time during the course of the CPA and RIGA audits, or later, has IMTC come forward with probative evidence, nor has it submitted with its request for review any such evidence, to establish that the expenditures questioned in those audits were made properly in accordance with law and regulation. It is the position taken by SFAP that IMTC failed to establish that its acts, or failures to act, were proper within either the letter or the intent of the governing law and regulations. SFAP requests on brief that the findings in the FAD be adopted in their entirety.

After due consideration of all the evidence of record, I conclude and I find that the CPA and RIGA audits are adequately documented and supported, and I adopt the findings in those audits. Specifically, in the CPA audit (ACN 05-24075), I find that IMTC's default rate as of June 30, 1989, was 35.76 percent, and was in excess of the standard set by ED for the audited period. As a consequence, and as recommended in Finding No. 1 of the CPA audit, IMTC will be, and is hereby, directed to assign to ED all qualifying PERKINS loans and to return to ED all federal capital contributions that were received by IMTC during the involved award years. I find, also, that IMTC's dropout rates as of midyear 1988 and 1989, respectively, were 43 percent and 38 percent; that these are deemed to be high withdrawal rates under 34 CFR 668.15 and, as such, to indicate an impaired administrative capability on the part of IMTC to administer student aid programs under Title IV HEA; and that the high withdrawal rate of IMTC should be used in subsequent evaluations of its administrative capability.

I also find that due to missing and/or incomplete accounting records and supporting documentation for the 2-year period ended June 30, 1989, a statement of changes in student financial aid balances for that period could not be compiled, and that therefor IMTC was not in compliance with ED's audit requirement. Student aid programs require that institutions must establish and maintain on a current basis all records, accounts, and controls that identify separately each program transaction, and must keep intact and accessible all records of receipt and expenditures of federal aid funds. These programs, and sound business management, dictate that program and fiscal records be reconciled monthly as well. I find that IMTC failed to retain such records and failed to have those programs audited, and that as a result all funds received by IMTC in these programs for the 1988 and 1989 award years must be disallowed. The repayment liability of IMTC in the PELL, SEOG, CWS and PERKINS programs is as shown in the recapitulation previously noted.

I find, as set out in the RIGA audit (ACN-05-10007) in Finding No. 1, that IMTC did not have an established procedure, nor a means to document that such a procedure was being followed, to determine its students' ability to benefit, and I conclude that IMTC failed to properly determine for students who lacked a high school diploma or its equivalent their ability to benefit as required under 34 CFR 600.11. I find that, as estimated in Finding No. 1, and as a consequence of Title IV funds disbursed to ineligible students who failed to complete the training for which they enrolled, as based on IMTC's 1990 cohort default rate . of 47.7 percent, IMTC must reimburse ED in the amount of $1,051,058, which is ED's actual loss as estimated. In the alternative, IMTC may repurchase from the appropriate lenders the improper loans made to ineligible students in the amount of $1,646,047, in STAFFORD loans. In addition, IMTC must reimburse ED in the amount of $739,200 for funds disbursed to ineligible students who failed to complete their training under the PELL, PERKINS, CWS, and SEOG programs, but may reduce this amount in the amount of such funds that may be included in IMTC's liability under Finding No. 3 or the CPA audit.

I further find that IMTC must repay to ED the amount of $539,720 in Title IV funds improperly expended in PELL programs as described in Finding No. 3 of the RIGA audit, and that IMTC must remit to ED on account of cash management deficiencies the amount of $5,100 as described in Finding No. 4 of the RIGA audit.

Respondent is directed to correct the impairments to its ability to properly administer Title IV HEA programs in the several specific administrative weaknesses set out in pages 7 and 8 of the FAD, and to comply with the detailed reimbursement instructions set out in pages 12 and 13 of the FAD. In lieu of the 45-day period for repayment compliance in the FAD, however, IMTC is directed to comply with the requirements of this decision no later than sixty (60) days after the date of service hereof.

<u>IT IS SO ORDERED</u>.

By Paul J. Clerman, Administrative Law Judge.

2 May 1994,
at Washington, D.C.