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

In the Matter of

SMITH BUSINESS SCHOOL, A/K/A INTERNATIONAL SCHOOL FOR CAREER EDUCATION,
Respondent.

Docket No. 95-108-SA
ACN: 03-31173
Student Financial Assistance Proceeding

Appearances: Barbara Herold, President, Smith Business School, Arnold, Maryland, for Respondent.

Alexandra Gil-Montero, Esq., Office of the General Counsel, United States Department of Education, Washington, D.C., for Student Financial Assistance Programs.

Before: Frank K. Krueger, Jr., Administrative Judge.

DECISION

INTRODUCTION

This case involves an appeal by the Smith Business School, also known as the International School for Career Education, of the final audit determination issued by the Student Financial Assistance Programs (SFAP), U.S. Department of Education (ED), on May 31, 1995, finding Respondent in violation of a number of regulatory requirements adopted in implementation of Title IV of the Higher Education Act of 1965, as amended. The audit determination is based on a close-out audit report submitted to ED on March 26, 1993, which covers award years 1989 through 1992. Respondent closed on July 8, 1992.

Four of the findings made in the final audit determination remain in contention and are the subject of this appeal. In Finding # 2, SFAP contends that Respondent improperly used $5,458 in Title IV funds to pay an institutional debt, and must repay ED this amount. In Finding # 6, SFAP contends that Respondent failed to make matching payments for Supplemental Educational Opportunity Grants (SEOG), for a liability of $2,000, which, as discussed below, has now been reduced by SFAP to $114. In Finding # 10, SFAP contends that Respondent failed

to make refunds in the amount of $15,147 on behalf of students receiving Federal Family Education Loans (FFEL) who withdrew from their courses of study prior to completion. SFAP also assessed interest payments and special allowances due to ED with respect to these unpaid refunds in the amount of $8,179. In Finding # 11, SFAP contends that Respondent owes ED $5,425 in unpaid Pell Grant and SEOG refunds to cover students who withdrew from their course of study prior to completion.

As discussed below, I find partially in favor of Respondent and partially in favor of SFAP.

DISCUSSION AND FINDINGS

Finding # 2

In October 1990, a creditor of the school attempted to execute a judgement against the school by having the Superior Court of the District of Columbia seize two of Respondent's bank accounts which contained Title IV funds to be used for Federal student financial assistance. The case was removed to the U.S. District Court for the District of Columbia and the funds at issue were eventually released to ED. Notwithstanding this full recovery, SFAP cited Respondent for violation of 34 C.F.R. § 668.16 (1990). This section provides that funds received under the various Federal student financial assistance programs are held in trust for the intended student beneficiaries and ED, and that the participating institution "may not use . . . these funds for any other purpose." SFAP seeks to recover $5,458 for this violation.

Respondent argues that it has no liability in this area since it joined forces with ED to successfully argue to the U.S. District Court for the District of Columbia that the money in the accounts belonged to ED. In August of 1992, ED received a check for $12,575 from Respondent's Title IV accounts which the court held in its registry until it was determined that ED owned the money.See footnote 1 *1* SFAP concedes that it eventually recovered all of the cash in Respondent's Title IV accounts and does not contest Respondent's contention that it fully cooperated with ED in recovering the Title IV funds temporarily held by the district court. As noted in the final audit determination, "[t]he auditor concluded that although the bank was notified that the account contained Federal funds, the bank ignored this when the judgement was executed." ED Exhibit 1-3. SFAP simply argues that Respondent was in violation of 34 C.F.R. § 668.16, because it failed to ensure that Federal funds held in trust for ED were not used for any purpose other than to pay for the education of its student beneficiaries.

I find that Respondent has not violated 34 C.F.R. § 668.16 (1990). Respondent did not use Title IV funds for any purpose other than the education of its students. Although the funds in question were initially held by the district court, they were simply held in a registry account until a proper determination could be made by the court concerning the proper ownership of the funds. As noted above, as a result of the adjudication in the district court, the funds were released to ED.

Finding # 6

Under 34 C.F.R. § 676.21 (1989, 1991), participating institutions are required to match SEOG funds from their own resources. The auditor determined that for the 1989-90 and 1991- 92 award years Respondent did not fully match the SEOG Federal shares, and an SEOG matching payment was made late for the 1989-90 school year. SFAP assessed liability at $2,000 for this violation.

Attached to its initial brief, Respondent submitted a letter dated June 9, 1993, addressed to Philip Brumbach, at SFAP's regional office in Philadelphia, wherein the auditor concluded that follow-up review indicated that Respondent fully matched the SEOGs for the 1991-92 award year. In its brief, SFAP "accepts" Respondent's evidence. Thus, the $2,000 liability is reduced to $114 for the 1989-90 award year. Respondent requests a waiver for the 1989-90 award year because it "discovered that additional institutional scholarships were awarded." Respondent's initial brief, p. 3.

I conclude that Respondent was in violation of 34 C.F.R. § 676.21 (1989) by failing to fully match the SEOGs for 1989-90, and owes ED $114 to cover its unmatched share of those grants. In its initial brief, Respondent submitted no evidence which supports its contention that it "discovered" additional institutional scholarships, or even states which year the alleged scholarships were provided. With its reply brief, Respondent attached certain student records which it contends demonstrate that it fully met its responsibilities to match the SEOGs in question. However, these exhibits are not trustworthy as they are unverified and without any foundation as to reliability. In addition, the exhibits were not submitted in a timely manner and with opportunity for review and comment by SFAP. The Order Governing Proceeding, issued on August 2, 1995, allows for the Respondent to submit a reply brief, but makes it clear that the brief is to deal with rebuttal matters only. The exhibits proffered as part of Respondent's reply brief clearly concern matters which were part of its case-in-chief and should have been brought forward when it submitted its initial brief, thus providing SFAP with an opportunity for review and objection.

Finding # 10

The auditor determined that refunds of Federal Family Education Loans (FFEL) were not made to the holders of these loans for students who terminated their courses of study prior to completion, in violation of 34 C.F.R. § 682.607. SFAP assessed lability for this violation at

$15,147. SFAP also assessed an additional $8,179 in interest and special allowances to cover these unsatisfied refunds.

In its defense, Respondent notes that when the school's Federal accounts were garnished and placed in the court's registry, one of the accounts was an operating account intended to cover loan refunds. In addition, SFAP placed the school on a reimbursement basis whereby the school was reimbursed for student assistance after the assistance was awarded, thus further preventing Respondent from having the necessary resources to provide student refunds. Respondent also argues that SFAP owes it $84,970 in unreimbursed Title IV money which it would have used for refunds. Respondent additionally requests that the special allowances and interest payments be waived in light of these circumstances.

SFAP argues that the issue of whether the Department owes Respondent any money for unpaid reimbursements is outside the scope of this proceeding. However, SFAP notes that Respondent's request has not been resolved because of outstanding liabilities of $56,384 associated with an earlier final program review determination issued in January 1992, and upheld on appeal in September of 1992.

I am sympathetic to Respondent's cash flow problems which appear to be caused in part by SFAP's delayed reimbursement. While the amount of the reimbursement owed to Respondent by SFAP may be involved in an earlier program review, by SFAP's own admission the amount involved is $56,384, thus leaving a balance of $28,586 owed to Respondent. This matter has been pending since 1992. However, while the Department cannot delay reimbursement indefinitely, an institution participating in the Federal student loan programs on a reimbursement basis must be prepared to have the cash resources necessary to provide timely refunds for students who withdraw from their education programs before completion and cannot rely on SFAP reimbursements to cover such refunds. The decision by SFAP to place Respondent on a cash reimbursement basis was within the discretion of SFAP in fulfilling its obligation to ensure that Federal funds are not jeopardized. Given the circumstances of this case, it does not appear that SFAP has abused its discretion. Thus, I find that Respondent was in violation of 34 C.F.R. § 682.607 (1989, 1991) by failing to make refunds on behalf of students receiving FFELs upon withdrawal from Respondent's program, and must reimburse the holders of these FFELs $15,157 to be credited to the accounts of these students. However, while I do not have the authority to waive this liability, *see* 34 C.F.R. § 668.117(d), SFAP should consider waiving or reducing the amount of money owed ED in light of its delay in processing Respondent's reimbursement request.

In its brief, SFAP agreed that the $12,575 it received in August of 1992 from Respondent's garnished Federal accounts should be used to reduce Respondent's liability to ED. In addition, SFAP must recalculate the amount of estimated interest and special allowances owed to ED to take into account this substantial payment it received which should have reduced the interest payments and special allowances made on behalf of Respondent and its students.

Finding # 11

The auditor found that refunds of Pell and SEOG funds were not made to ED on behalf of students who terminated their courses of study prior to completion, and Respondent owed ED refunds of $5,425. Such refunds are required under 34 C.F.R. § 668.22. Respondent defends by contending that it could not make refunds because part of the money ultimately returned to ED by the court from the garnished Federal accounts were intended to cover refunds. Once again, Respondent's cash flow problems do not legally excuse it from complying with the requirements that refunds be made to ED on behalf of students who withdraw from its education programs prior to completion. Thus, I conclude that Respondent is in violation of 34 C.F.R. § 668.22 for failure to make refunds for a liability owed to ED of $5,425.See footnote 2 *2*

ORDER

ORDERED, that Respondent pay ED a net amount determined as follows:

* $144 -- liability for unmatched SEOGs (SFAP Finding # 6) .
* $5,425 -- unpaid Pell and SEOG refunds (SFAP Finding # 11); subject to verification by SFAP (see footnote 2).
* Special allowances and interest payments made by SFAP which should not have been made had Respondent made FFEL refunds (SFAP Finding # 10); however, SFAP must recalculate the amount due in light of the $12,575 payment it received from Respondent's garnished Federal accounts.
* The total amount of the three items above must be reduced by the $12,575 payment received by SFAP in 1992.

FURTHER ORDERED, that Respondent pay to the holders of FFELs $15,147 to be credited to student accounts for unpaid refunds (SFAP Finding # 10).

November 30, 1995

Frank K. Krueger, Jr.
Administrative Judge

SERVICE

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

Ms. Barbara Herold, President
Smith Business College
a/k/a International School of Career Education
1321 Argyll Drive
Arnold, Maryland 21012

Alexandra Gil-Montero, Esq.
Office of the General Counsel
U.S. Department of Education
Room 5442
600 Independence Ave., S.W.
Washington, D.C. 20202

Footnote: 1 *1 It is not clear exactly how SFAP calculated liability for this finding. In the final audit determination SFAP contends that Respondent's Title IV funds were seized to satisfy a judgement and assessed liability at $5,458; and yet the court ultimately released $12,575 from Respondent's Title IV accounts to the Department.*

Footnote: 2 *2 On the basis of the present record, I cannot be sure that the $5,425 which SFAP alleges Respondent owes ED as reimbursement for unpaid Pell and SEOG refunds represents grant money in fact paid by Federal funds. Since Respondent was placed on a reimbursement basis sometime in 1989 (Respondent's initial brief, p. 6), and it has had an unsatisfied reimbursement claim with SFAP for $84,970 which appears to cover reimbursements for much of the period covered by the audit, it is possible that the Pell and SEOG reimbursements being sought in Finding # 11 are not valid since Respondent may have never received reimbursements for the Pell and SEOG grants at issue. However, since this issue was never raised by Respondent, and the record is devoid of evidence on the issue, I must conclude that Respondent has failed to meet its burden of proving that the expenditures questioned by SFAP in Finding # 11 were valid. See 34 C.F.R. § 668.116(d). Nevertheless, SFAP should ensure, either when seeking to enforce this decision or when entering into a final accounting and settlement with the Respondent, that there is no double payments made by Respondent to ED to cover these unpaid reimbursements.*
