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

In the Matter of **Docket No. 95-131-SA**

LEONARD'S HOLLYWOOD BEAUTY SCHOOL, Student Financial Assistance Proceeding

Respondent. ACN: 03-34044

Appearances: Edward Benoff, Esq., Philadelphia, PA, for Leonard's Hollywood Beauty School.

Stephen M. Kraut, Esq., Office of the General Counsel, United States Department of Education, Washington, D.C., for Student Financial Assistance Programs.

Before: Judge Richard F. O'Hair

DECISION

Leonard's Hollywood Beauty School (Leonard's) previously participated in the various student financial assistance programs authorized under Title IV of the Higher Education Act of 1965, as amended (HEA). 20 U.S.C. § 1070 *et seq.* and 42 U.S.C. § 2751 *et seq.* These programs are administered by the office of Student Financial Assistance Programs (SFAP), United States Department of Education (ED). On July 28, 1995 , SFAP issued a revised Final Audit Determination (FAD) in which it sought the return of $11,802 in federal funds. The FAD is based upon a May 23, 1991, program review report for the 1988-89, 1989-90, and 1990-91 award years. Leonard's filed a request for review on August 24, 1995 . Both parties filed submissions to this tribunal in response to the Order Governing Proceedings.

SFAP contends that Leonard's awarded Pell Grant funds to students who were selected for verification without verifying those students' application information. SFAP further alleges that Leonard's improperly awarded a $1,588 Pell Grant to a student who reported that she was in default on a loan made under the Title IV, HEA programs.

Leonard's responds that SFAP was barred from acting upon the July 28, 1995, FAD under the doctrines of *res judicata*, collateral estoppel, issue preclusion, and double jeopardy because of the terms of an agreement settling SFAP's previous termination and fine action against the

school. Leonard's also argues that it properly verified those students selected for verification and that it properly awarded the $1,588 Pell Grant at issue here.

Procedural issues

Leonard's argues that the present action is barred under the doctrines of *res judicata*, collateral estoppel, issue preclusion, and/or double jeopardy because the issues central to this action were resolved when a previous termination and fine action brought by ED against the school was settled on August 11, 1992. According to Leonard's, this settlement agreement resolved all outstanding matters, including the issues raised in the present action, with the exception of violations of criminal laws or civil fraud against the United States.

In Article II, Paragraph A, of the settlement agreement, ED specifically agreed to withdraw its November 8, 1991, termination and fine notice, in which it sought to terminate the school's eligibility and to impose a $16,000 fine. In exchange, Leonard's agreed in Article II, Paragraphs B and D, that its eligibility to participate in the Title IV programs would be terminated and that it would pay a $500 fine to ED.

Contrary to Leonard's claims, however, the settlement agreement did not resolve all outstanding matters. As SFAP correctly notes, Article III, Paragraph A, of the settlement agreement states as follows:

By this agreement, ED does not waive compliance by the School with any Federal or State law or regulation, past, present, or future, applicable to the School's administration of the Title IV, HEA Programs.

Ex. R-3, at 2.

This language very clearly preserves ED's right to seek redress for the school's prior noncompliance with all applicable Title IV, HEA statutes and regulations. This tribunal has stated previously that in order for *res judicata*, which is also known as claim preclusion,See footnote 1 *1* to apply there must be (1) a final judgment on the merits, (2) an identity of the cause of action between the two actions, and (3) an identity of the parties or their privies in the two actions. *In*

re Lincoln Technical Institute, Dkt. No. 91-38-SP, U.S. Dep't of Educ. (Interlocutory Decision) (October 30, 1992), at 14. Termination and fine proceedings under Subpart G are distinct from actions to recover misspent funds, such as this, brought under Subpart H. Therefore, the second requirement of an identity of the cause of action between the two actions is not satisfied here, and thus *res judicata* or claim preclusion does not apply. While the settlement agreement would bar SFAP from bringing another termination and fine proceeding based upon these alleged violations, it does not bar SFAP from attempting to recover the allegedly misspent funds.

Leonard's also cannot use the doctrine of collateral estoppel, also known as issue preclusion,See footnote 2 *2* to shield itself from the FAD in this case. In *In re Career Education, Inc.*, Dkt. No. 91-17-ST, U.S. Dep't of Educ. (August 28, 1992), this tribunal held the following:

Under the doctrine of issue preclusion, once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in a subsequent proceeding based on a different cause of action involving a party to the prior litigation.

Career at 25-26.See footnote 3 *3* Here, the previous termination and fine proceeding was settled by the parties. As a result, none of the issues in the present case were actually determined in the previous case. Therefore, collateral estoppel or issue preclusion cannot apply.

Also, the doctrine of double jeopardy is not applicable here. In *United States v. Halper,* 490 U.S. 435 (1989), the U.S. Supreme Court held that a defendant who already has been punished in a criminal prosecution may not be subjected to an additional civil sanction to the extent that the second sanction may not fairly be characterized as remedial, but only as deterrent or retribution, without violating the double jeopardy clause. In that case, the defendant had been previously convicted in a criminal action, and the government then brought a civil action. The district court had approximated the government's expenses as $16,000, but the government sought to recover $130,000 in the civil action. The Court, while allowing the government to demand civil compensation according to somewhat imprecise formulas, said that the civil compensation sought in that case bore no rational relation to the goal of compensating the government for its loss, but instead appeared to qualify as "punishment." The case was remanded to allow the government to demonstrate its damages.

In this proceeding, not only has there not been a criminal prosecution, but also SFAP is seeking only to recover its actual, estimated losses. It cannot be said that the compensation sought by SFAP bears no rational relation to the goal of compensating the government for its loss. As a result, the double jeopardy clause does not shield Leonard's from liability for these losses.

Thus, in accordance with Article III, Paragraph A, of the settlement agreement, SFAP's agreement to withdraw its termination and fine action under Subpart G did not preclude it from subsequently bringing this audit recovery action under Subpart H.

Finding 4--Failure to determine Pell Grant eligibility prior to certification of Stafford loans

In Finding 4 of the FAD, SFAP seeks the return of $647 which it estimated as its actual loss on a Stafford loan of $2,750 made to a student for whom SFAP alleges the school failed to determine the student's Pell Grant eligibility prior to certifying the Stafford loan. In its brief, however, SFAP states that it subsequently has determined that the student in question had applied, and was found eligible, for a Pell Grant. As a result, SFAP is withdrawing that finding. Accordingly, Leonard's has no liability under Finding 4.

Finding 5--Failure to verify Pell Grant applications

Under 34 C.F.R. § 668.54, an institution must verify the application information of a student if that student is selected by ED for verification, or if the institution has reason to believe that any information contained on the applicant's application is incorrect. Nonetheless, ED cannot require

an institution to verify more than 30 percent of its applicants in any award year. 20 U.S.C. § 1091(f).

SFAP points out that the close-out audit conducted by Leonard's independent auditor reported that the school did not verify the information on any of the student applications. ED Ex. 1-14. Finding 17 of the program review report issued on May 23, 1991, found that students 6, 12, 15, and 16 had been selected for verification, but that the school did not perform any verification checks on these students. In addition, it stated that there was no evidence that the school ever verified information provided by student applicants for the Pell Grant program. Ex. R-2-13. Finding 5 of the FAD alleges that Leonard's did not verify at least 30 percent of its applicants during the award years in question.

In its initial brief, Leonard's contends that it required applicants selected by ED for verification to submit documentation to verify the information used to determine the applicants' eligibility and that it reviewed all student submissions. To further support its position, the school also claims that, where applicable, students also completed and filed Verification Worksheets, and it included Ex. R-6 as an example of what its students submitted. Leonard's also objects to this proceeding because there has been no showing of an actual loss sustained by ED.

The Verification Worksheet submitted by Leonard's as Ex. R-6 is not for one of the four students questioned in the program review. As a result, it is insufficient to satisfy the school's burden under 34 C.F.R. § 668.116(d) of persuading this tribunal that it complied with the verification requirements. Moreover, as SFAP notes, this student checked on her Verification Worksheet that she had filed an income tax return, yet Leonard's did not include this income tax return with the other verification documents, as required under 34 C.F.R. § 668.54, 668.56(a),

and 668.57(a).

In its reply brief, Leonard's argues again that it verified all applicants selected by ED for verification, and it attached as Ex. R-9 the verification worksheets for several additional students. Only one of these students, however, was among the four students questioned by the program reviewers, and that verification worksheet was for a different year. The evidence submitted by Leonard's demonstrates that it verified student 12 for the 1990-91 award year, but the program reviewers found that this student was not verified for the 1989-90 award year, and the school has submitted no evidence to refute that assertion.

This tribunal has previously held that although ED is barred by statute from requiring an institution to verify more than 30 percent of its Title IV applicants in any given year, the institution must demonstrate that it verified at least 30 percent of its students selected for verification. *In re Fisk University,* Dkt. No. 94-216-SP, U.S. Dep't of Educ. (Oct. 5, 1995), at 3-4. Since Leonard's failed to do so, it is liable for 30 percent of the Pell Grant awards it disbursed because it has not shown these funds were properly expended. I agree with the school, however, that SFAP's liability figure of $9,567 is incorrect, and that the correct amount is $8,817.30. This amount is derived by multiplying $29,391, the amount of questioned costs in the FAD (ED Ex. 2-4) by 30 percent. Accordingly, Leonard's must repay $8,817.30 to ED under Finding 5.

Finding 7--Student in default status received Pell Grant funds

In Finding 7, SFAP alleges that a student who was in default on a Title IV, HEA loan improperly received Pell Grant funds of $1,588 during the 1987-1988 award year. In order to be eligible to receive a Pell Grant award, a student may not be in default on any Title IV, HEA program loan. 20 U.S.C. § 1091(a)(3). SFAP notes that Finding 7 of Leonard's close-out audit alerted Leonard's to this situation when it reported that this student's loan application indicated that the student was in default on a prior student loan. ED Ex. 1-14.

In response, Leonard's concedes that this student received a $1,588 Pell Grant during the 1987-1988 award year, but argues that this occurred before the July 1, 1988, effective date of 34 C.F.R. § 668.7, which contains the no prior default rule. Leonard's contends that it subsequently complied with that regulation. Nevertheless, 20 U.S.C. § 1091(a)(3) also required eligible students to not be in default on prior Title IV loans, and this statute was in effect during the 1987-88 award year.

Leonard's also submitted a Verification Worksheet dated August 3, 1987, which is contained at Ex. R-6, that bears no indication of this student's default status. Additionally, Leonard's submitted the student's application for a Stafford Loan, contained in Ex. R-7, which was signed on July 31, 1988, and indicates that the student was in default on a Title IV loan at that time. To satisfy its burden of persuasion under 34 C.F.R. § 668.116(d), however, the school needed to submit a student loan application for the 1987-1988 award year or some other document indicating that the student was not in default on a Title IV loan during that award year.

Since it did not do so, Leonard's is liable for the $1,588 Pell Grant awarded to this student.

FINDINGS

1. SFAP was not barred from acting upon the July 28, 1995 final audit determination under the doctrines of *res judicata*, collateral estoppel, issue preclusion, or double jeopardy because of an agreement settling SFAP's previous termination and fine action against the school which addressed identical findings.

2. Leonard's has no liability under Finding 4.

3. Leonard's awarded Pell Grant funds to students who were selected for verification without verifying those students' application information.

4. Leonard's improperly awarded a $1,588 Pell Grant to a student who reported that she was in default on a loan made under the Title IV, HEA programs.

ORDER

On the basis of the foregoing, it is hereby ORDERED that Leonard's Hollywood Beauty

School shall repay $10,405.30 to the United States Department of Education in the manner authorized by law.

_____
Judge Richard F. O'Hair

Dated: March 19, 1996

SERVICE

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

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Footnote: 1 *1 See Application of the New York State Department of Education, Dkt. No. 90-70-R, U.S. Dep't of Educ. (April 20, 1994), at 31 n.9, for a discussion of the terms res judicata, collateral estoppel, claim preclusion, and issue preclusion.*

Footnote: 2 *2 See supra note 1.*

Footnote: 3 *3 For a more complete discussion of issue preclusion, see Career at 24-25.*
