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

In the Matter of **Docket No. 96-132-SP**

LIBERTY ACADEMY OF BUSINESS, Student Financial Assistance Proceeding

Respondent. PRCN: 199530311685

Appearances:

Charlotte Matthews, President and CEO, Philadelphia, PA, for Liberty Academy of Business.

Kelly J. Andrews, Esq., Office of the General Counsel, United States Department of Education, Washington, D.C., for Student Financial Assistance Programs.

Before:

Chief Judge Ernest C. Canellos

INTERIM DECISION and ORDER

Liberty Academy of Business (Liberty) was a proprietary institution of higher education located in Philadelphia, Pennsylvania, which offered programs of study in business. Effective on January 22, 1993, Liberty became eligible to participate in the Federal Pell Grant and the Federal Family Education Loan Programs authorized under Title IV of the Higher Education Act of 1965, as amended (Title IV), 20 U.S.C. § 1070 et seq. and 42 U.S.C. § 2751 et seq. Liberty was accredited by the Accrediting Council of Independent Colleges and Schools (ACICS). On February 8, 1996, however, ACICS accreditation was withdrawn. Apparently, as a consequence of such loss of accreditation, on February 21, 1996, Liberty closed. At the time of its closure and for some unspecified period of time prior to that date, Liberty was on the reimbursement system of payment for Pell Grant purposes.

On August 23, 1996, the Acting Chief, Institutional Review Branch Region III, Office of Student Financial Assistance Programs (SFAP) of the U.S. Department of Education (ED) issued a final program review determination (FPRD) finding that Liberty had violated a number of regulations promulgated pursuant to Title IV. The FPRD had its genesis in an on-site program review of Liberty's Title IV compliance for the award years 1994-1995 and 1995-1996, which occurred on November 27 - December 1, 1995, and December 7 - 14, 1995, just prior to the school's closure. The FPRD contained eleven findings. First, Liberty lacked the administrative capability to administer Title IV programs because there were no checks and balances in place, as required. Specifically, it was alleged that the functions of authorizing Title IV payments and making those payments were impermissibly carried out by the same person, the owner. For that alleged violation, the FPRD demanded the return of all the federal student financial assistance funds which Liberty disbursed during the 1994 award year ($523,214 broken down as follows: Pell grants - $250,123, Stafford

loans - $269,791, and SLS loans - $3,300) and the 1995 award year ($554,539 broken down as follows: Pell grants - $225,668, and Stafford loans $328,871), for a total demand of $1,077,753.See footnote 1[1] Second, Liberty could not demonstrate that its Paralegal, Executive Secretary, and Business Administration programs were approved by ACICS, therefore, it could not establish that they were eligible programs. Some of the other findings included: misrepresentation of programs, inadequate internal controls, accounting records not reconciled, and failure to properly calculate refunds. Since SFAP determined that the funds which it could have demanded for the second and subsequent findings were subsumed in the funds that it had already demanded for the first finding, no separate monetary finding was calculated nor was a separate demand made for them in the FPRD.See footnote 2[2]

On September 28, 1996, Liberty appealed the FPRD. It argued in its appeal and in its brief, in essence, that it had no compliance problems and that no violations had been established by SFAP. Liberty claimed that its most recent periodic audit was filed on August 24, 1995, and that audit covered the award year July 1, 1994, to June 30, 1995. Further, it claimed that it failed to file the close-out audit covering the period from July 1, 1995, to the date of closing, February 21, 1996, only because it did not have the requisite funds to pay for such an audit. Liberty also pointed out, without any further explanation as to the effect of such a situation, that since the school had closed, all of its records were removed and retained by the Pennsylvania Department of Education.

In its Response brief, SFAP argued that its evidence supported the findings in the FPRD and that Liberty had submitted no evidence to refute those findings. Apparently in recognition of the tenuous basis for FPRD's demand relative to the lack of administrative capability, however, counsel's brief deviated from the findings of the FPRD and inexplicably changed the demand to the return of: (1) $554,539 for the federal student financial aid awarded during the 1995 award year on the sole basis of Liberty's failure to file a close-out audit as required by 34 C.F.R. § 668.26(b)See footnote 3[3] and, (2) $434,256 for the Title IV aid allegedly improperly awarded to students in Liberty's three ineligible programs.See footnote 4[4] The total demanded by the brief is $1,062,745.

The facts indicate that when it was certified as eligible to participate in Title IV Programs, Liberty offered a Paralegal diploma program. This diploma program was accredited by ACICS and approved by the State. Contemporaneously, Liberty also enrolled students in two other diploma programs, i.e. the Business Administration and the Executive Secretary programs. These programs were timely approved by the state and accredited by ACICS. Beginning in May 1993, Liberty enrolled students in a Paralegal Associate in Specialized Business (ASB) degree program; this program was approved by the state on May 24, 1994, and ACICS on June 6, 1994. Separately, beginning on January 10, 1994, Liberty enrolled students in a Business Administration ASB program and an Executive Secretary ASB program. On November 9, 1994, these two programs were approved by the State, however, they were never approved by ACICS. SFAP counsel's claim results from a demand for the return of all of the federal aid given to students in these three programs for the respective periods of time when the programs were either not accredited or approved by the state.

In its brief dated December 6, 1996, Liberty denies that it approved the expenditure of Title IV funds for ineligible programs, as alleged by SFAP. Rather, it claims that each of the three programs was approved by ACICS as a diploma program and each had been approved by the state. As a result, they were clearly eligible programs for Title IV purposes. Liberty's position is cogently stated in its brief, as follows:

> The point that the institution has tried to make clear to the U.S. Department of Education is that the procedure it followed in raising the award level from diploma to ASB degree is the same route that any postsecondary institution would pursue. The programs continue to run while the institution seeks approval for any change in its programs. At no time did this institution disburse financial aid to students for programs not approved. The programs were approved by both the State and ACICS and the institution was authorized to award the diploma by both the State and ACICS. . . . *In the case where a program remains the same (courses credits, length of time), and the only change is in the level of the award, the program continues to be eligible for participation in Federal Title IV aid* (emphasis added).

Liberty provided no legal authority for such an assertion. SFAP did not address this claim directly but did point out that ACICS had determined in a Special Evaluation Report that the degree and diploma programs were different in length

and in course content, and that information was provided to Liberty on November 7, 1995. What remains for my consideration is Liberty's argument that the programs in issue were approved and, therefore, eligible and that Liberty's machinations to convert those programs to degree status were routine and, at most, constituted a minor and non-actionable event.See footnote 5[5]

DISCUSSION

In an appeal of a finding in an FPRD, the institution has the burden of proving that the Title IV funds in question were lawfully disbursed. 34 C.F.R. § 668.116(d). However, before I reach that issue, I must decide a threshold question, i.e. can ED effectively alter its demand in its brief from that which it made in the FPRD, so as to change not only the amount it demands to be returned but also the legal basis for that demand. This determination, obviously, implicates the constitutional question of what constitutes adequate notice in an administrative process so as to satisfy the requirements of due process as commanded in the Fifth Amendment of the U. S. Constitution. Within that context, a cardinal principle of administrative law is that timely and adequate notice is a basic element of due process. G*oldberg v. Kelley*, 397 U.S. 2545 (1970). This is especially true in cases, like the subject one, which are originated under Subpart H, where the FPRD effectively imposes the burden of proof and persuasion on the Respondent.

Here, Liberty was notified by the FPRD that it was required to return all the Title IV funds disbursed during the 1994 and 1995 award years because it lacked administrative capability -- it failed to provide adequate checks and balances in its system of internal controls. Liberty defended itself somewhat on the merits on the basis of its small size and its limited resources, and argued that since the school was closed, it was too late to take corrective action. It is important to note that this was the only actionable finding in the FPRD and that the claims which SFAP now pursues did not become claims until it filed its brief, which, coincidentally, happened to be the final pleading in the record.See footnote 6[6] Liberty's prior submissions readily agreed with SFAP's claim that it had not provided the required close-out audit, but defended itself on that issue by arguing that it did not have the funds with which to engage an auditor. There was no doubt that the close-out audit requirement was clear and understood -- the Respondent cannot claim “surprise”sufficient enough to interfere with its ability to defend itself or meet its burden of proof, however, this was not posited as a “finding.” Although Liberty's brief admits that the violation occurred, one is left to ponder what would have happened had Liberty been put on notice in the FPRD that it was risking the return all Title IV aid by not filing its audit, as opposed to defending against an allegation that it believed was unsupportable. From the record, I cannot conclude that given the option -- pay back all Title IV funds or file the close-out audit, Liberty would not have filed the audit. Consequently, I find that there was a failure of notice.

If I were able to proceed to the merits of this case, a number of other issues are readily apparent. First, should Liberty be required to return all Title IV funds it disbursed during the period of time between the date of the last audit and the date of closing? In addition, were Liberty's Paralegal, Executive Secretary, and Business Administration programs eligible for Title IV funding? Finally, in either of the above situations, can Liberty be forced to return the face value of FFEL loans rather than the estimated actual loss? *See In Re Christian Brothers University*, Docket No. 96-4-SP, U.S. Dep't of Educ. (February 13, 1997).

As to the first issue, SFAP points out that the jurisprudence of this tribunal is that if an eligible institution fails to submit a close-out audit or otherwise fails to prove that expenditures were proper, then it owes back all the Title IV student aid that it has disbursed because it has not met its burden of establishing that the said Title IV aid was proper. *In re Cosmetology College*, Docket No. 94-96-SP (November 27, 1995); *In re Long Beach College of Business*, Docket No. 94-78-SP (October 5, 1995); and *In re Calvinade Beauty Academy*, Docket No. 93-151-SA (September 18, 1995). The basic reasoning behind those decisions is that without such an audit, SFAP cannot be assured that the federal funds were not misspent. As a corollary, however, we have recognized that other evidence may satisfy the Respondent's evidentiary burden that such aid was proper. *In re Selan's System of Beauty* Culture, Docket No. 93-82-SP, U.S. Dep't of Educ. (December 19, 1994). There, SFAP required the institution to perform a complete file review covering five award years. The institution submitted evidence that was probative of its expenditure of Title IV funds, but did not amount to a full file review. SFAP argued that since the evidence submitted was not in compliance with its directive, the evidence

carried no weight. In that decision, I upheld SFAP's calculation of liability for reasons unrelated to the issue here, but recognized that in instances where SFAP has some degree of reliable and relevant evidence on how the institution expended Title IV funds, the institution should not owe a liability calculated on the basis that none of the Title IV funds were accounted for. *Id*. Here, unlike most instances where a school closes without any audit trail subsequent to a prior audit report, we have *some* evidence which is available to SFAP for its consideration of whether there was compliance with Title IV. Approximately two months prior to Liberty's closure, SFAP program reviewers were on-site for approximately thirteen days reviewing Liberty's compliance with Title IV program rules. Also, Liberty was on the Pell reimbursement system of payment which required Liberty to justify, to SFAP's satisfaction, each Pell Grant payment prior to its disbursement. Based upon my review of the manner in which SFAP's demand has been formalized, it seems clear that neither of these factors was considered by SFAP in its decision-making process.

FINDINGS and ORDER

Given the discrepancies noted above, I find that the record, as currently constituted, is insufficient for purposes of proceeding to decision. Therefore, based on the limited facts of this case and in the furtherance of judicial economy, I REMAND the FPRD to SFAP for action consistent with the discussion above. Such action should include, at a minimum, a modification of the FPRD so that it reflects the true bases for SFAP's demand, and, at the same time, formally puts the respondent on notice of those bases. The respondent is then free to make decisions under a correct premise. In addition, the parties should discuss the other issues raised in whatever pleading they generate in returning this dispute to me for my decision.

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Ernest C. Canellos, Chief Judge

Dated: December 8, 1997

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]*It is not clear on what legal basis SFAP demanded the return of all the funds disbursed during the two award years in question. Failure to evidence administrative capability is a factor in determining whether the institution should continue to participate in the Title IV programs, or be terminated. 34 C.F.R. § 668.16. See also, In re Universidad Eugenio Maria de Hostos, Docket No. 95-128-ST, U.S. Dep't of Educ. (January 21, 1997). However, to my knowledge, such an allegation, even if clearly established, has never been determined to support a demand for the return of all Title IV funds. Further, SFAP cites no statute, regulation or case decision which authorizes such a remedy. Notably, cases that have discussed the general issue concerning the fair and accurate assessment of liability in a*

Subpart H proceeding have adopted the principle that SFAP is only entitled to recover losses directly attributed to the institutions's improper expenditure of Title IV funds. See In re Muscular Therapy Institute, Docket No. 94-79-SP, U.S. Dep't of Educ. (July 14, 1995).

Footnote: 2 *[2]It would appear prudent to make a monetary determination as to each finding so as to account for the possibility that the main finding would not be approved upon review.*

Footnote: 3 *[3]Whenever a Title IV eligible institution closes or ceases to provide educational services, 34 C.F.R. § 668.26(b)(2)(ii) requires that the institution provide to the Secretary a letter of engagement from a Certified Public Accountant, indicating that a close-out audit will be done, and the audit report must be submitted within 45 days of the date of that letter of engagement. Although a comment referring to a failure to file such audit is contained in the FPRD, the findings are not based on that violation. However, counsel for SFAP, in her brief, recasts SFAP's demand against Liberty as follows: "Liberty breached its fiduciary duty to account for federal funds by failing to submit a close out audit and must return the Title IV funds it received during the unaudited period."*

Footnote: 4 *[4]SFAP's counsel asserts in her brief that this figure is reflected in an attachment to the FPRD; however, based upon my examination of the FPRD, I am unable to determine how the figure was arrived at. In addition, the demand for the return of funds for the ineligible programs seems to overlap with the demand for the return of all the funds for the 1995 award year, and both seem to seek the return of the face value of FFEL loans rather that the estimated actual loss which SFAP has, heretofore, adopted as the amount which it could recover.*

Footnote: 5 *[5]The record is silent on whether the programs would be eligible for a higher Title IV payment as a degree program rather than as a diploma program or, if it were eligible for a higher amount, whether any such additional sum was disbursed.*

Footnote: 6 *[6]Although Liberty could have moved for permission to file a Reply Brief, it did not do so. It should be noted that Liberty is represented by its owner, a non-lawyer, and that this might explain why no such request was forthcoming.*
