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

In the Matter of **Docket No. 96-9-SA**

UNITED EDUCATION INSTITUTE, Respondent.

Student Financial Assistance Proceeding

ACN: 09-30002

Appearances:

Leslie H. Wiesenfelder, Esq., and Sherry Mastrostefano, Esq., Dow, Lohnes & Albertson, Washington, D.C., for Respondent.

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

Before:

Frank K. Krueger, Jr., Administrative Judge

DECISION

Introduction

Respondent, United Education Institute (UEI), is a private vocational school licensed by the State of California and accredited by the Accrediting Council for Continuing Education and Training. At the time of the audit report at issue in this proceeding, UEI operated a main campus in Los Angeles and five satellite campuses elsewhere in southern California. UEI offered a variety of vocational programs, including electronics and microcomputer repair, medical assistance, computer training, and English as a Second Language (ESL). Ninety percent of UEI's students were enrolled in its ESL program. Approximately 84 percent of UEI's students received some type of assistance under Title IV of the Higher Education Act of 1965, as amended, mostly Pell Grants.

In 1993, the Office of the Inspector General (OIG), U.S. Department of Education (ED), conducted an audit of UEI's administration of the Title IV programs for the period of July 1, 1992, through June 30, 1993. On August 10, 1994, OIG issued its audit report, in which it found that UEI was in violation of Title IV by understating refunds due to students who dropped out of its ESL program. On October 19, 1995, ED's Student Financial Assistance Programs (SFAP) issued a final audit determination which adopted the findings of the OIG audit report and directed that UEI refund $302,000 to ED for the understated refunds. By letter dated December 21, 1995, UEI appealed the SFAP determination. The parties submitted briefs and exhibits in support of their positions, and oral argument was held on June 6, 1996.

For the reasons provided below, I agree with SFAP that UEI understated the amount of refunds due under its ESL program. However, since my basis for this conclusion is different from that of SFAP, the amount due to ED for the understated refunds must be recalculated.

Discussion

I. Background:

UEI's ESL program was forty-eight semester hours in length, consisting of two enrollment periods of twenty-four semester hours each. In October 1992, UEI increased the tuition for the entire ESL program from $4,800 to $7,600. This raised the tuition for each enrollment period from $2,400 to $3,800. In April 1993, UEI offered students the option of completing the program in three enrollment periods consisting of sixteen semester hours. The tuition for the entire program taken over three enrollment periods was $9,600, with the tuition rate for each period of $3,200. Due to their economic circumstances, most of UEI's ESL students qualified for Pell Grants. UEI's tuition changes had no effect on the amounts or number of Pell Grant awards.

When UEI raised its tuition in October 1992, it also implemented an “incentive loan program” wherein interest-free loans were given to students to cover the difference between their Pell Grants and the tuition. For example, for a tuition charge of $3,200, and where the student qualified for a Pell Grant of $2,400, UEI would give a student an incentive loan of $800 to cover the difference between the Pell Grant and the tuition charge. Students participating in the incentive loan program would sign a contract in which the loans were repayable within six months after graduation or after the student dropped out of the program. If the student graduated from the ESL program with fewer than twelve absences, the school would forgive repayment of the loan.

The OIG auditors concluded that the incentive loans were not valid for the following reasons: UEI forgave loan balances for graduates with fewer than twelve absences; UEI did not make a serious attempt to collect loan balances owed by students; UEI did not record the loan balances in its accounting system; and the loans were used to cover tuition increases that had no link to instructional changes. Specifically, the audit report noted that, on the face of the loan agreement, students who graduated from the program with less that twelve absences had their loans forgiven. For those students who graduated with twelve or more absences, or who dropped out of the program before completion, the auditors found that the school sent one letter informing a student of his or her obligation to repay the loan balances. If the student did not respond to the letter, no follow-up effort was made. The auditors examined a random sample of 284 student files from the 1,323 students who withdrew from the ESL program, and found that UEI received no payments from any of these students for the incentive loans. Further, the auditors found that UEI kept no master record acknowledging the loans as accounts receivable, or any ledgers keeping track of the loans. Based on these factual findings, the auditors concluded that UEI never intended to collect the loans, and were used for the sole purpose of inflating the cost of attendance in order to be able to retain more Pell funds if a student dropped out of the program. By increasing the tuition charge, UEI was able to increase the amount of tuition allegedly earned on behalf of a student who withdrew, thereby decreasing the amount of Pell refunds.See footnote 1[1]

Based on the original tuition rate, OIG recalculated the refunds due on behalf of the students included in the sample that they reviewed, and projected the recalculation for all students who withdrew from the ESL program during the audit period. OIG estimated the amount due for all students to be $252,000. In addition, UEI identified an additional $50,000 in refunds that the school failed to pay from July 1993, to April 1994, as a result of the alleged artificial tuition charge. Consequently, SFAP directed UEI to pay $302,000 in unpaid Pell Grant refunds.

Under pressure from OIG, UEI discontinued the incentive loan program in April 1994.

II. Incentive Loans As *Bona-Fide* Institutional Financial Aid:

In response to the OIG findings, UEI submitted the sworn statement of Abdi Lajevardi, President of UEI since 1987. According to Mr. Lajevardi, UEI increased its tuition in October of 1992 in part due to its need to cover increased fees assessed by the State of California, to pay for continuing educational courses to ensure that its ESL teachers met state requirements, and to pay for independent monitors for its ability-to-benefit tests. UEI also anticipated a decrease in revenue as a result of a new state policy which required a full refund or additional instruction to students who graduated from its programs, but failed post-graduate tests. In addition, UEI was indeed anticipating less revenue as a result of the new Federal *pro-rata* refund requirements. Declaration of Abdi Lajevardi, Exhibit R-4 at 4-5. Mr. Lajevardi noted that UEI had only very modest increases in its tuition for the ESL program over the previous three years ($200), and that other schools in its geographic area charged approximately $3,200 for ESL programs. Thus, UEI concluded that its ESL tuition was too low in relation to its anticipated and actual costs. *Id.* at 5.

According to Mr. Lajevardi's declaration, around the same time UEI decided to increase its ESL tuition it also decided to implement the incentive loan program to encourage students to complete the ESL program. UEI determined that, although students usually enroll in vocational education programs in order to earn a credential to obtain employment in a particular field, students take ESL in order to learn English well enough to communicate with others. Because facility in English is easily demonstrated through conversation, a certificate from an ESL program does not have the same intrinsic value as other academic credentials. As a result, as soon as students were able to communicate effectively enough in English to secure employment, they often dropped out of the ESL program. UEI, of course, believed that students should remain in the program until completion in order to achieve the maximum level of competence. Moreover, UEI's state authorizing agency requires institutions to maintain at least a 60 percent completion rate for each of its educational programs or risk losing its license to provide the programs. Thus, UEI designed the incentive loan program questioned by SFAP. *Id.* at 5-6.

In response to SFAP's charge that the incentive loans are not binding agreements, Mr. Lajevardi noted that students sign promissory notes for the loans. *Id.* at 7. When UEI instituted the incentive loan program it had hoped that the program would be financially viable in that it would collect enough money from students not able to have their loans waived and maintain enough corporate-sponsored students to be able to pay for the waived loans through its increased tuition. *Id.* at 13. Most students, of course, took advantage of the program, although a few students had the difference between their Pell Grants and the full tuition paid for by a corporate sponsor or rehabilitation agency. *Id.* at 7 and Exhibit R-16. However, very few of the students who dropped out of the program, or completed it with more than twelve absences, paid off their loans. Although UEI sent a collection letter to each of its former students, 20 percent were returned as undeliverable. UEI did not send repetitive collection letters or make any further attempt to collect the loans because, according to Mr. Lejevardi, the school knew, due largely to the economic and transient nature of its ESL students, that the loans were largely uncollectible. Exhibit R-4 at 9-10.

In response to the charge that UEI never kept track of the incentive loans in its accounting system, Mr. Lajevardi notes that, during the time period at issue, UEI was on a cash accrual system of accounting and thus did not report the incentive loans on its financial statements until cash was actually received. *Id.* at 11. UEI submitted an opinion from its CPA that this method of accounting was in accordance with generally accepted accounting principles. Exhibit R-20.

The only "rebuttal" evidence submitted by SFAP was a declaration by James Okura, the OIG supervisory auditor in this case. Exhibit E-7. Although Mr. Okura expressed his opinion that the incentive loans were not valid loans, his declaration is nothing more than a reiteration of the conclusions made in the OIG audit report and adds nothing of value to the record.See footnote 2[2] Mr. Okura makes no attempt to further elaborate on the OIG conclusions or to address any of the testimony given by Mr. Lajevardi.

Under 20 U.S.C. § 1070a-6(5) (1990),See footnote 3[3] the cost of attendance can only include those tuition and fees normally "charged" to a student. According to SFAP, quoting from *Black's law Dictionary* and *Webster's Ninth New Collegiate Dictionary*, to "charge" means to "impose a burden, duty, obligation, or lien, to create a claim against property; to assess, to demand ..."; to "fix or ask a fee or payment...." Under the plain meaning of the term "charge," to qualify as tuition under Title IV, the student must have a legal obligation, duty, or burden to pay the alleged charge. SFAP brief at 8. I accept the SFAP definition. Under the terms of the promissory notes signed by the students, a clear, unequivocal, legal obligation was created requiring the students to repay the loans if they dropped out of the program or completed the program with twelve of more absences. The fact that the loan agreements provided for possible forgiveness of the loans has no impact on the legality of the obligation created.

The fact that UEI never attempted to seek enforcement does not undermine the legal significance of the debt created by the notes. Mr. Lajevardi's declaration, which was available to SFAP before Mr. Okura's declaration was executed,See footnote 4[4] states why UEI never sought enforcement. Mr. Lajevardi's declaration also states why the incentive loans were not included in UEI's financial statements and notes that other records concerning the loans were maintained by the school. Neither Mr. Okura, nor anyone else in SFAP or OIG, made any attempt to rebut Mr. Lajevardi's declaration on any of these points. Finally, the fact that the tuition increases were not linked to any instructional change in the ESL program is not conclusively probative of whether the loans at issue were valid. Institutions may decide to increase tuition on the basis of criteria other than instructional content. Indeed, Mr. Lajevardi's declaration provided a number of economic reasons as to why the tuition was increased. Mr. Lajevardi's declaration is credible and, since it was unrebutted, must stand.

There is no statute, regulation, or ED policy that directly deals with institutional loans as a cost of attendance.See footnote 5[5] What case law that exists supports UEI's position.See footnote 6[6] In *In re Mount Wachusett Community College*, Docket No. 94-102-SP, U.S. Dept. of Educ. (Sept. 1, 1995), *certified by Secretary* (Nov. 22,1995), the judge held that tuition could be included for incarcerated students in the cost of attendance calculation because the students were potentially liable for any unpaid balances that existed at the end of the year even though the institution routinely waived any charges which remained after Title IV assistance was credited to the student accounts. In *In re Hallmark Institute of Technology*, Docket No. 94-127-SP, U.S. Dept. of Educ. (Aug. 23, 1995), and *In re Arkansas Valley Technical Institute*, Docket No. 95-52-SP, U.S. Dept. of Educ. (Jan. 31, 1996) the judge held that tuition and fees could be included in the calculation of the cost of attendance where the tuition and fees were reimbursed to the institution from another source since the students were billed and remained liable for the tuition and fees if the reimbursement was not received.

Thus, under the language of 20 U.S.C. § 1070a-6(5) and the prevailing case law of this tribunal, I must conclude that the incentive loan program represented a valid means of providing institutional financial assistance and represented a *bona-fide* charge to UEI students which could be included as a valid cost of attendance for purposes of determining refunds.

III. Improper Calculation of Refunds by UEI:

Although UEI contends that the tuition increases were *bona-fide* and that the incentive loans were valid, it ignored this position when it calculated the refunds due on behalf of the students who dropped out of the ESL program. Under 34 C.F.R. § 668.22(a) (1992), "an institutional refund means the amount paid for institutional charges for a payment period by financial aid and/or cash payments minus the amount retained by the institution for the portion of the payment period that the student was actually enrolled at the institution." The record demonstrates that when UEI performed this mathematical calculation, it did not treat the amount of the tuition represented by the incentive loan program as financial aid or payment received. This failure had the effect of having the Pell Grant program pay for most of the tuition and fees earned by the institution, rather than distributing those cost among all sources of payment, including the institutional loan program. Put another way, the Pell Grant program in effect funded most of the incentive loans for students who dropped out of the ESL program.

This effect may be seen by examination of UEI's own evidence. For example, V.R. was a student in UEI's ESL program who dropped out during the first payment period. According to her enrollment agreement, V.R.'s tuition was to be paid as follows:

Total tuition and fees: $3,200.00
Pell: $1,533
Incentive loan: $1,667

Exhibit R-12-1.

At the time of V.R.'s withdrawal, the school had distributed one-half of the Pell Grant, or $766. Exhibit R-12-4.See footnote 7[7] Thus, V.R. was also disbursed one-half of her incentive loan, or $833.50. However, there is no recognition of the incentive loan in the refund calculation. UEI calculated the refund by subtracting the amount earned from the Pell funds received rather than by subtracting the amount earned from the total financial aid package as required by the regulation. UEI determined the refund as follows:

Pell funds paid: $766.00

Tuition and fees earned: 773.44

Refund : . . . . ($7.44)See footnote 8[8]

Exhibit R-12-4.

V.R.'s refund should have been calculated as follows:

Tuition and fees paid: $1,600.00
Pell funds: $766.50
Incentive loan:. 833.50
Tuition and fees earned:. 773.44

Refund. $826.56

Under the regulations in effect during the period at issue in this case, UEI could retain a portion of the refund based on the amount of the incentive loan it provided to the student at the time the student dropped the program, or, in the case of V.R., approximately 52 percent of the refund. *See* 34 C.F.R. § 668.22 (a)(3)(ii) (1992).

Other examples of UEI's miscalculations appear in Exhibits R-12-10 to R-12-13. In Exhibit R-12-10, UEI's record shows no refund due to the Pell program. However, a refund of approximately $393.00 was due for this student which should have been distributed between the Pell Grant fund and the incentive loan program. Similarly, Exhibit R-12-13 shows no refund due to the Pell program, when a refund of approximately $711 should have been distributed between the Pell Grant program and the incentive loan program. In both of these cases UEI paid itself the tuition it earned completely from the Pell Grant program, and then went to the student for the balance, which was a minimal amount which the students simply paid off. If one examines the OIG audit work papers (Exhibit E-6), one can see that UEI miscalculated the refunds for all of its student who dropped out of the ESL program.

In addition to violating 34 C.F.R. § 668.22(a) in its calculation of refunds, UEI also violated its fiduciary duty to ED. Under the Title IV program, wherein participating institutions are distributing Federal money, the institutions act as a fiduciary. 34 C.F.R. § 668.82 (1992). “Fiduciary” is defined as “[a] person having duty, created by his undertaking, to act primarily for another's benefit in matters connected with such undertaking.” *Black's Law Dictionary* 563 (5th ed. 1979). As to matters within the scope of a fiduciary duty, the person having the fiduciary duty must not benefit at the expense of the beneficiary to the duty. *Cf. Restatement 3d Trusts*, S.170. By charging, in most cases, the entire tuition earned to the Pell program, rather than allocating the cost more equitably between the Pell program and the incentive loan program, UEI acted to its own benefit and to the detriment ED in violation of its fiduciary duty.

Findings and Conclusions

1. The increased tuition to UEI's ESL program implemented in October 1992 and April 1993 represented *bona-fide* tuition charges to students and could be used in the calculation of the cost of attendance for purposes of determining refunds due on behalf of students who withdrew from the ESL program prior to completion.

2. The incentive loans made by UEI to students to cover the cost of tuition not covered by the Pell Grant program were valid institutional loans, even though UEI failed to collect those loans from most of the students in the program.

3. As valid institutional financial assistance to cover *bona-fide* educational charges, the institutional loans should have been used in UEI's calculation of refunds, and UEI's failure to include the institutional loans in the calculation was a violation of 34 C.F.R. § 668.22(a)(2) (1992).

4. UEI's failure to use the incentive loans in calculating the refunds due to the Pell Grant program clearly benefitted UEI to the detriment of the Pell Grant program, in violation of UEI's fiduciary duty under 34 C.F.R. § 668.82 (1992).

ORDER

ORDERED, that UEI recalculate all refunds for students who withdrew from its ESL program between October 1992 and April 1994 in accordance with section III of this decision, and promptly pay that amount to ED.

August 16, 1996

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:

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Footnote: 1 [1] *Beginning on July 23, 1992, institutions participating in the Title IV programs were required to make refunds which were the larger of refunds provided under applicable state law, under the policy of the accrediting agency, or under the pro-rata refund formula provided under Title IV. 20 U.S.C. § 1091b.*

Footnote: 2 [2] *UEI objected to the admission into the record of Mr. Okura's declaration because, although he is a CPA, he is employed by OIG and his professional opinion as a CPA should be accorded little weight. This objection is overruled and the declaration is accepted. OIG CPA's are entitled to professional opinions, although, as noted above, Mr. Okura'a opinion is of little value in that it fails to specifically address UEI's evidence.*

Footnote: 3 [3] *Under the Higher Education Amendments of 1992, Congress replaced normally "charged" with normally "assessed"; the new definition became effective on July 1, 1993. See 20 U.S.C § 1087ll (Supp. 1996). Both parties agree that this change was inconsequential and has no effect on the analysis or result in this case. SFAP brief at 7, n. 4; UEI reply brief at 3, n. 2.*

Footnote: 4 [4] *Under the briefing schedule established for this case, UEI filed its brief and exhibits over thirty days prior to the filing by SFAP. In addition, Mr. Lajewardi's declaration, and most of the UEI exhibits, were also submitted as attachments to UEI's request for appeal and were, presumably, reviewed by SFAP in the thirty days it retained the appeal request prior to forwarding it to the Office of Hearings and Appeals for the administrative review.*

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[Footnote: 5] *The only policy statement remotely material to the issue at hand is a statement in the preamble to the Department's final regulations concerning the requirement that for-profit institutions must demonstrate that at least 15 percent of their educational revenues are acquired from sources other than the Title IV programs. There it is stated, at 59 Fed. Reg. 22328 (April 29, 1994), that ED would not consider an institutional loan to be valid for purposes of calculating the non-Title IV revenue unless the loans were routinely repaid by the student borrowers. What value such a statement may have on the outcome of this proceeding is negated by the fact that the preamble was published during the month in which UEI discontinued the incentive loan program.*

[Footnote: 6] *[6] The cases cited by SFAP are inapposite. SFAP cites In re Educational Management Systems, Inc., Docket No. 94-31-SA, U.S. Dept. of Educ. (June 22, 1990), certified by Secretary (May 18, 1995); In re Microcomputer Technology, Docket No. 94-88-SA, U.S. Dept. of Educ. (May 5, 1995), certified by Secretary (Aug. 15, 1995); and In re Massachusetts School of Barbering and Men's Hairstyling, Docket No. 94-128-SP, U.S. Dept. of Educ. (May 12, 1995), certified by Secretary (Sept. 18, 1995). These cases dealt with the inclusion of tuition in the cost of attendance for incarcerated students who received their educational instruction for free. The students were not charged or otherwise billed for anything in relation to the programs.*

[Footnote: 7] *[7] One half of the total Pell Grant for V.R. would have been $766.50, but UEI appears to have dropped the fifty cents in doing its refund calculation.*

[Footnote: 8] *[8] In this case, as can be seen, V.R. ended up owing money, rather than getting an actual refund. In this case, as well as all the others, where the student owed money over and above the tuition paid for by the Pell program, UEI billed the student under the incentive loan program. In several cases, some students, unlike most, actually paid off their incentive loans. See Exhibit R- 12. However, in these few cases the students were billed much less than they actually owed, because UEI was using the Pell program to pay off most of the loan balances. In cases where the amount owed was very small, such as in V.R.'s case, the student simply paid off the loan. See Exhibits R-12-5 and R-12-6.*