

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

In the Matter of

**Docket Nos. 03-06-SA
and 03-07-SP**

STAGE ONE, THE HAIR SCHOOL,

Federal Student Aid
Proceedings

Respondent.

Appearances: Susan Koepp, of Cape Girardeau, Missouri, for Stage One, The Hair School.

Jennifer L. Woodward, Esq., of the Office of the General Counsel, United States Department of Education, Washington, D.C., for Federal Student Aid.

Before: Judge Ernest C. Canellos

DECISION

Stage One, The Hair School (Stage One), operated as a proprietary institution of higher education in Cape Girardeau, Missouri, offering programs in cosmetology. These programs were accredited by the National Accrediting Commission of Cosmetology Arts and Sciences and were eligible to participate in the Federal Pell Grant (Pell) and Federal Family Education Loan (FFEL) Programs under a provisional participation agreement that expired on September 30, 2002. The Pell and FFEL programs are governed by 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.* Within the U.S. Department of Education (ED), the office of Federal Student Aid (FSA) is the organization that administers these programs.

During the week of March 11, 2002, a team from FSA's Kansas City Case Management Team conducted a program review at Stage One to examine its administration of the Federal Student Aid programs. A number of violations were uncovered during this review. The violations alleged included: refunds either not made or refund calculations erroneously made, lack of administrative capability, failure to file the required annual audit, etc. These findings, as well as others, were included in a Final Program Review Report, issued on April 15, 2002. This report not only solicited Stage One's input on the findings, but also required it to accomplish a full file review for the 1998-99, 1999-00 and 2000-01 award years to determine the amount of refunds due to be returned to the Federal programs. In a separate proceeding, on April 18, 2002, FSA revoked Stage One's provisional certification of eligibility to participate in Federal student financial aid programs on the basis of the findings uncovered during the program review. One of the consequences of such revocation was the requirement that Stage One perform a closeout audit. Although it appealed the

revocation of its eligibility,^[1] Stage One took no action to comply with the requirements levied upon it by FSA (*i.e.* to perform a full file review, to submit the required periodic audit, and contract for and submit a closeout audit).

On November 15, 2002, FSA issued a Final Program Review Determination (FPRD) concerning the failure to comply with Title IV program requirements for award years 1998-99, 1999-2000, and 2000-01, as uncovered by FSA's review team and as enumerated in the Final Program Review Report. According to the findings in the FPRD, Stage One failed to properly calculate and pay refunds, as required by 34 C.F.R. § 668.82. Additional findings included: ability-to-benefit test not approved, Pell Grants disbursed prior to their entitlement, as well as assorted administrative failures. As a result, FSA determined that Stage One owed a total of \$158,271 to the Pell program and owed \$168,545 to the loan holders of the improper FFEL loans at issue. In response, on December 28, 2002, Stage One requested a hearing to challenge the findings of the FPRD and, once assigned the case, I issued an order to commence the hearing process.

Separately, because of its failure to submit a closeout audit, FSA, on November 7, 2002, issued a Final Audit Determination (FAD) demanding that Stage One return \$648,344, the total amount of Title IV funds it received during the period required to be covered by the audit report, *i.e.* January 1, 2000, to April 18, 2002. On December 17, 2002, Stage One appealed the findings of the FAD. This appeal was originally assigned to Judge Richard I. Slippen. Since the findings and the amounts demanded to be returned by the FPRD and FAD overlapped, on February 5, 2003, the appeal of the FAD was reassigned to me. Upon reassignment, I consolidated the two appeals into the current proceeding.

It is well established that in Subpart H -- audit and program review -- proceedings, the institution has the burden of proving by a preponderance of the evidence, that Title IV funds in issue were lawfully disbursed. 34 C.F.R. §668.116(d). If an institution fails to establish the correctness of its expenditure of federal education funds, it must return all such funds to ED. After a careful review of the entire record, including the documents submitted by Stage One, I find that Stage One has not substantiated its position that the findings contained in the FPRD and FAD are incorrect. It is abundantly clear that under the circumstances of this case, Stage One has not met its burden of proof.

As pertinent to the findings of the FAD, an institution that participates in Title IV programs has the responsibility to submit a closeout audit covering the period from the date of its last submitted periodic audit to the date it ceases to participate in the federal student financial aid programs. A closeout audit must be submitted to FSA within 45 days of that cessation. 34 C.F.R. § 668.26(b)(ii). In the absence of such a closeout audit, the institution must return all federal student aid funds that it received since its last submitted audit. *See, In re Excelsis Beauty College*, Docket No. 98-108-SA, U.S. Dep't of Educ. (October 4, 1999), and the cases cited therein.

I note that Stage One filed several documents along with its requests for administrative hearings. I find, however, that these documents are not probative of the allegations contained either in the FPRD or FAD. Stage One also iterated that its failure to submit a closeout audit was caused by the illness of the auditor and FSA's cutting off of funds. In addition, Stage One's owner complained that the recovery demanded by FSA is unfair because: the school has been operating since 1927, its students have a high pass rate, the school has a low default rate, and the school makes an important contribution to the community. Unfortunately, regardless of how noteworthy these factors might be, they do not constitute acceptable excuses for its failure to establish that the institution's expenditure of federal student aid funds was correct.

After the close of the briefing schedule, and in an apparent last ditch effort to justify its position relative to the FSA demand, Stage One filed an additional submission of approximately 200 pages of documentation with the tribunal in December 2003. To its credit, FSA's counsel reviewed the submission and, in a supplemental filing dated February 6, 2004, appropriately accepted some of the documentation as dispositive of some of the issues and reduced its demand accordingly. For the FPRD violations, FSA now demands the return of \$29,257 to the Pell Grant account and \$54,858 to the holders of the appropriate FFEL loans. As for the FAD liability, FSA now seeks \$297,406.87 for Stage One's failure to file a closeout audit or otherwise provide sufficient alternate proof of the appropriateness of expended Title IV funds.^[2] I note as significant that even after the extended period of time between the school's loss of eligibility and today, the required closeout audit still has not been submitted.^[3]

In summation, I am convinced that the findings contained in the FPRD and FAD sufficiently state allegations in a manner that demonstrate the existence of a *prima facie* showing that the institution failed to comply with Title IV program requirements. Consistent with the record before me, I find that Stage One has failed to meet its burden of establishing that its expenditures of Title IV funds, as enumerated in both the FPRD and FAD, were correct. Therefore, Stage One owes \$297,406.87 for the liability demanded in the FAD, as well as \$29,257 in Pell Grant liability and must pay \$54,858.13 to the current loan holders or otherwise repurchase the appropriate FFEL loans as provided in the FPRD.

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ORDER

On the basis of the foregoing findings of fact and conclusions of law, it is HEREBY ORDERED that Stage One, The Hair School, pay to the United States Department of Education the sum of **\$326,663.87**. In addition, it is HEREBY ORDERED that Stage One, the Hair School, pay **\$54,858.13** to the respective holders to repurchase the FFEL loans in question, consistent with the determinations contained in the FPRD and FAD and in the manner as required by law.

Ernest C. Canellos
Chief Judge

Dated: March 19, 2004

SERVICE

A copy of the attached document was sent to the following:

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[1] Stage One requested reconsideration of its revocation of eligibility. However, that decision was affirmed by FSA on June 21, 2002. The eligibility issue is not before me in this proceeding.

[2] Some of the reduction in FSA's demand results from a withdrawal of the amounts that were ordered returned in both the FPRD and FAD so as to avoid a double recovery. This is consistent with the concept that ED is entitled to be indemnified for the losses it suffers as a result of violations that are caused by participating institutions, but that the recovery should not result in ED's unjust enrichment.

[3] An institution that participates in Title IV programs has a fiduciary responsibility to account for federal funds. In the present case, the Respondent has failed to do so. Although it is possible, if not probable, that some of the funds in issue were correctly expended, there is insufficient basis for me to determine, with any degree of assurance, that this is so.