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

In the Matter of	**Docket No. 03-100-SP**
AMERICAN BUSINESS COLLEGE,	Federal Student Aid Proceeding
Respondent.	PRCN: 200240220394

Appearances: Peter S. Leyton, Esq., and Dana M. Fallon, Esq., of Ritzert & Leyton, P.C., Fairfax, Virginia, for American Business College.

Denise Morelli, 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

PROCEDURAL HISTORY

American Business College (American) provided educational programs of study in Basic and Advanced Cosmetology at three locations, Bayamon, Isabela and Carolina, Puerto Rico. It was accredited by the National Accrediting Commission of Cosmetology and Sciences and was eligible to participate in the Pell Grant Federal Student Aid Program authorized 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 has cognizance over and administers this program.

From August 19–23, 2002, Institutional Review Specialists from FSA's New York Case Management Team conducted an on-site program review of American's administration of the Pell Grant program for award years 1999–2000, 2000–2001, and 2001–2002. During the course of the review and subsequent investigation, which included interviews of current and former students, evidence was uncovered indicating that the student files contained pervasive erroneous information. As a consequence, on November 7, 2002, FSA issued a Notification of Emergency Action and Termination of Eligibility to participate in Title IV programs, and a fine. These actions were initiated under authority of Subpart G, 34 C.F.R. § 668.81 *et seq.* Shortly

thereafter, American closed, rendering the termination and emergency actions moot. Later, the fine action was resolved through settlement.

Separately, FSA reviewed the information it had garnered during the review and investigation to determine the extent that federal funds had been misspent and, therefore, should be returned. As a result, and under authority of Subpart H, 34 C.F.R. § 668.111 *et seq.*, on July 29, 2003, FSA issued an Expedited Final Program Review Determination (EFPRD) demanding that American return $2,245,488 to ED. This demand was based on two actionable findings. First, FSA determined that Pell Grant funds had been improperly disbursed to ineligible students, in violation of 20 U.S.C. § 1091(d), and 34 C.F.R. § 668.32(e)(2). This finding had its genesis in the Title IV requirement that students who do not posses a high school diploma or its equivalent must pass an independently administered and approved ability to benefit test (ATB) in order to be eligible to receive Title IV funds. According to American, it complied with this requirement by engaging Mr. Pablo Burgos, an independent test examiner, to administer the Spanish Assessment of Basic Education (SABE), an authorized ability to benefit test, to each prospective student who did not possess a high school diploma or its equivalent. However, during its investigation and as part of its inquiry into American's practices, FSA claims that its reviewers interviewed 71 students who reported that either Mr. Burgos did not administer the test or, they took no test at all -- in some instances, students claimed that their school records maintained by American were falsified. Further, FSA claimed that although Mr. Burgos may have administered the ATB tests at American after January 2002, he was not a certified test examiner at that time, which is required. Faced with that information, FSA decided that American's records were so unreliable as to be insufficient to establish the eligibility of any ATB students. Consistent therewith, FSA determined that any student ever admitted to American on the basis of ATB was ineligible and, as a result, American must return $1,677,005 to ED for the Title IV student aid erroneously provided to these students.

The second finding involved an allegation that some students were disbursed more in Pell Grant aid than they were entitled. This finding implicated two separate types of errors. One was the improper granting of a second disbursement of Pell grant funds to students before they had satisfied the prerequisites to such disbursement. The other was that refunds to the Pell Grant fund for students who had withdrawn prior to the completion of their program were understated either because the students' hours of attendance were intentionally overstated or because in its refund calculations, American factored in more for equipment that it provided than was authorized. This finding resulted in an FSA demand for return of $568,483.

PARTIES' POSITION

American appealed the above two findings of the EFPRD. In its initial brief, it succinctly argued that American's written policy required that all ATB students take the SABE test and such test was to be administered by Mr. Burgos. Although it claimed general compliance with policy, American concedes that in its own inquiry initiated after FSA's visit, it discovered that three former employees at the Bayamon and Carolina campuses had violated this directive and had, as a convenience to the students, administered some of the SABE exams themselves. Although not necessarily presented as a justification or excuse, American pointed out that those

particular students completed the SABE on their own and that the exams were provided to Mr. Burgos for scoring. Additionally, American asserted that, at the Isabela campus, Mr. Burgos administered all 31 of the ATB exams and that the resulting $82,897.59 in Pell grants was clearly proper. To rebut FSA's second basis for ATB liability, American also provided a certificate from the SABE publisher stating that Mr. Burgos was an authorized test examiner in January 2002 and beyond. In summary, American argues that it did not falsify records, Mr. Burgos administered almost all the ATB exams, Mr. Burgos was an authorized ATB test examiner, and demanding the return of any Title IV aid to ATB students with the exception of those who were administered the SABE by American's employees, is unfair and improper. American also urged that I consider the fact that it has provided a quality vocational education and that its students have maintained a high percentage of completion, placement and licensure at the three campuses.

American agrees to repay the Pell Grants disbursed to students who were administered the ATB test by school employees. Although it states that it cannot ascertain the exact number of such students, it proposes that to arrive at the liability, I should refer to the figures that FSA included in its brief that it filed in the fine action referenced above. From that, I should take the 34 students who, when interviewed, claimed that they were administered the ATB test by school employees and order that their $67,974 in Pell Grants be returned as damages for the ATB violation. If I determine that such result is inadequate, then in the alternative, they propose that I should take that figure and apply it against the total grants provided to all of the students who were interviewed resulting in an 11.1% error rate.[1] When that error rate is applied to the universe of all ATB students, a $190,125 liability would result.

As to the second finding, American claims that in its refund calculations, it excluded the cost of unreturnable equipment that had been issued to its students as authorized in 34 C.F.R. § 668.22(c)(5)(ii) and § 668.22(d)(3)(ii). It claims that it marked up the equipment slightly and not in an excessive manner, and that such action has been previously authorized. Also, American claims that it utilized the FSA-provided software to calculate refunds, but, it does acknowledge that an independent auditor it hired determined that, although FSA's calculation of liability is too high, it does have liability for improper refunds in the amount of $359,833.

In its responsive pleading, FSA accepted the certificate from the SABE publisher as being dispositive of Mr. Burgos' authority to be a test examiner after January 2002 and, as a consequence, it withdrew $218,898 from its demand relative to the ATB violation.[2] Further, although FSA conceded that some of the ATB processing was proper, it asserted that because of

[1] I cannot verify those figures, including the proposed error rate, since ED's brief in that fine action is not included in the record. ED does not, however, directly challenge the proffer in this proceeding except where it makes a separate assertion that 71 students made such declarations.

[2] FSA now considers that Mr. Burgos' activities relative to ATB testing were proper subsequent to January 2002, yet improper prior to that date. Without some clear indication of why it reached such a different conclusion, it would seem that FSA's position on this issue is clearly inconsistent especially when it, otherwise, demands the return of all Pell Grants given to ATB students.

the questionable validity of American's records, it was not possible to determine the extent of the violations. FSA argued that American's claim that it substantially complied with ATB test requirements is belied by the results of FSA's interviews with the 71 students, who claim otherwise. Finally, FSA admits that it did not interview any students from the Isabela campus but urges that, since the ATB violations were so endemic at the other two campuses, the same activities obviously also did occur at the Isabela campus.

In a reply brief, American argued for the first time that the process FSA adopted in issuing the EFPRD had violated its rights. Specifically, American complains that FSA chose to finalize its demand without first issuing a draft program review report. The issuance of such a report, which is common practice, would have given American an opportunity to contest the findings before they were finalized.[3] Also, it produced statements from four students and a number of school employees indicating that Mr. Burgos administered all ATB tests. That being the case, American argues that an error rate calculation should be utilized rather than declaring all ATB testing as flawed. Finally, by applying an error rate calculation to the ATB violations, $190,125, and by accepting its auditor's calculation of the refund liability, $359,883, American concedes that it really owes, at most, $550,008, and urges that sum should be offset against Pell Grant funds that American has earned and that FSA currently holds.[4]

STANDARD OF REVIEW

A review of both parties' submissions reveals that clearly there were violations of the ATB rules and erroneous calculations of refunds. Other than an assertion by FSA and some suspicions, however, there does not appear to be evidence of systemic fraud by the school's administration. What is also abundantly clear, is that the parties are in essential disagreement as to the standards I should apply in determining how much American owes the Federal government to compensate it for its losses.

I begin my consideration of these issues by noting that this proceeding is governed by regulations promulgated under Subpart H of the general provisions. It is well established that in a Subpart H -- audit and program review proceeding, the institution carries the burden of proving by a preponderance of the evidence that the Title IV funds in issue were lawfully disbursed. In accordance with 34 C.F.R. § 668.116(d), to sustain its burden, an institution must establish, that (1) the questioned expenditures were proper and (2) the institution complied with program requirements. It is clear that American cannot satisfy this burden because it is unquestionable that violations did occur. After making that finding, what is left for me to determine is the amount of recovery that is due to FSA. In that vein, it has been consistently held that the remedy

[3] There is no requirement that FSA issue a preliminary report of the type mentioned by American. Since American had notice of the allegations contained in the EFPRD and an adequate opportunity to defend itself, I find this complaint to be without merit.

[4] Although set-off is clearly a recognized legal concept, I have no jurisdiction to adjudicate the merits of any set-off claim in this proceeding.

available to FSA under Subpart H is contractual in nature and allows only for the recovery of provable losses.[5]

ABILITY TO BENEFIT

As is evident throughout the law, a party claiming damages in any litigation has the obligation to establish the extent of such damages.[6] Here, in determining what are the provable damages, I am presented with a situation where it is quite apparent that some of the Pell Grant funds in issue were properly expended while other such funds were improper. My task is to determine, if possible, the extent of each category. FSA suggests that, because of the difficulty in sorting out which ATB disbursements fit into which respective category, I should opt to consider all ATB aid prior to January 2002, as improper.[7] The problem with such a determination is that it obviously overstates the recovery and, in effect, gives FSA a windfall. The evidence of record is clear -- some ATB disbursements at the Bayamon and Carolina campuses were erroneous. Just as clear, there is no evidence that there were such erroneous payments at the Isabela campus -- the mere suspicion of such irregularity is, clearly, insufficient.

Further, FSA's basis for its demand for the return of all Title IV funds disbursed to ATB students appears questionable as too great a leap in logic.[8] FSA claims that it interviewed a number of students and that 71 said that either Mr. Burgos did not administer their ATB exam or they took no such exam at all. It is unclear from the record exactly how many students FSA interviewed. Were only 71 students interviewed and all made such statements, or were more students interviewed? If so, how many other students were interviewed, and what did they say regarding ATB testing? As is evident, the result reached under each such scenario would be markedly different. Significantly, however, FSA's brief cites seven students as examples of the statements made by the 71 ATB students. I have reviewed each statement and observe the

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[5] *See, e.g. In the Matter of Avalon Beauty College,* Dkt. No. 04-24-SP, U.S. Dep't of Education (December 29, 2004) (On Appeal to the Secretary); *In the Matter of Macomb Community College,* Dkt. No. 91-80-SP, U.S. Dep't of Education (Final Decision June 28, 1993) (Macomb)

[6] A party is entitled to recover damages that are the proximate result of the harm. Damages that are remote, contingent and speculative in character cannot be recovered. *See, e.g., Apperson v. Security State Bank,* 215 Kan. 724, 528 P.2d 1211 (1974). Moreover, applying the well-settled *Hadley v. Baxendale Rule,* damages may be awarded for harm that is foreseeable or within the contemplation of the parties and which is caused by or connected to the basis of liability. *Hadley v. Baxendale,* 9 Exch. 341, 156 Eng. Rep. 145 (1845). Uncertainty as to the fact of whether damages were sustained at all is fatal to recovery, but uncertainty as to amount is not, if evidence in the record furnishes a reasonably certain factual basis for computation of loss. 22 Am.Jur. 2d Damages § 332 (May 2004).

[7] As indicated earlier, FSA originally demanded the return of all Pell Grant aid disbursed to ATB students; however, it now accepts such aid after January 2002, as proper.

[8] One is left to ponder here whether, in FSA's view, once it made its determination relative to the efficacy of the student records, any evidence that American could submit would suffice to satisfy the Respondent's prescribed burden of proof in this Subpart H proceeding.

following relative to credibility and establishment of the premise propounded: all were translations of statements apparently made by students, they were apparently unsworn, and they apparently did not entail any critical questioning by FSA investigators. As to the content, three students said they never took an exam, three said a man at the school gave the exam and the seventh said someone at the school gave the exam. Since I could not find any reference in the file indicating which other students were included in the 71, I randomly reviewed 26 student files out of the universe of American's 356 ATB students included in the record, and could find no other statement that would fit that category. Given the paucity of credible evidence from either party as to how ATB testing was administered, it is impossible for me to determine the extent of what actually occurred relative to that question.[9]

More importantly, however, I am not unmindful of an aspect of this issue that I believe is critical. There is the possibility that if all Title IV aid is returned, the respective ATB students could be liable to pay for the tuition and fees that American had, otherwise, earned by educating them. In a nutshell, American provided educational services to the students under an enrollment agreement that provided in pertinent part that "the student whose financial aid does not cover the total cost of the course is responsible for paying the school the difference not covered by the grant." If students received appropriate education, would American have the legal right to initiate an action in contract to recover from the students?[10] If the answer is yes, then have we not frustrated the purpose of the Pell Grant Program and, in an attempt to save federal funds, passed on the cost to needy students, who are supposed to be the direct beneficiaries of the Pell Grant Program? As we have observed in the past, this is an unexpected result of FSA's use of the Subpart H procedures to, in effect, punish the institution for its failures, rather than the use of the more appropriate Subpart G.[11]

After having considered all the above-discussed factors and the ramifications of each, I find that I am unable to determine in any precise way how much American must return to ED for the ATB violation. I reach this conclusion by rejecting, as factually unsupportable, FSA's allegation that all the ATB aid should be returned as compensation for its loss to the Pell Grant fund. Rather, I find that the most appropriate method of arriving at the damages for this violation is by applying an error rate calculation, as discussed above, to the entire ATB universe

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[9] Significantly, there is no statement from Mr. Burgos describing his involvement with ATB testing at American included in the record. American claims that he was on military duty in Iraq from February 2003, but doesn't provide any current status or reason why he isn't available now.

[10] The parties do not address this matter, and the tribunal knows of only one statutory provision that under limited circumstances not relevant here, vests authority in the Secretary to discharge obligations. *See* 20 U.S.C. § 1087(c)(1)(2000), 34 C.F.R. § 682.402(e) (2000) (for example, the Secretary may discharge a borrower's obligation with respect to a loan where the borrower's eligibility to receive the loan was falsely certified by an eligible school).

[11] It is interesting to note that in this case FSA did avail itself of the remedies in Subpart G, including a fine action. Although Subpart G and H remedies are not mutually exclusive and are designed to accomplish separate purposes, one could ponder whether FSA has been adequately compensated and any further recovery would, ultimately, be at the expense of the innocent needy students.

of $1,677,005. A further complicating factor is, however, that the exact error rate is not clearly ascertainable from the record. One possibility is applying the error rate proposed by American, 11.1% based on 34 students.[12] Another possibility is calculating a rate based on the 71 students, as reported by FSA. Complicating my resolution of this quandary is FSA's decision to seek the return of all Title IV funds provided to ATB students in this proceeding rather than attempting to perfect any claim for a recovery based on a sampling error. This tactical decision now leaves the record insufficient for me to calculate an error rate on FSA's terms. Consequently, I find only so much of a recovery of Title IV funds for the ATB violation as is arrived at by applying the American proposed error rate of 11.1% to the ATB universe of $1,677,005 or $186,148, supportable in the record.

REFUNDS

The refund issue is more narrowly focused here. Both FSA and American agree that the proper method of calculating the loss occasioned by erroneous refunds is to project the sample error rate to the universe of refunds. *See generally, In the Matter of Instituto de Estetica y Belleza Marugie,* Docket No. 03-21-SP, U.S. Dep't of Educ. (March 1, 2004). As with any application of a sample error, the result is, at best, a "guesstimate." Here, each side applies this concept to reach a somewhat different result. FSA calculates that $568,483 must be returned for this finding, while American agrees that it owes $359,833.

Although each side obliquely contests the other party's formulation for determining liability, they really only disagree as to whether or not ATB students should be included in the universe of students. FSA is of the opinion that all ATB students should be removed from consideration to avoid duplication because they anticipate that full recovery will be ordered for their aid. American posits that to arrive at the most appropriate figure, ATB students must be included. In seeking to arrive at the most appropriate figure, it seems clear that if ATB students are included then the errors uncovered in the sample would be diluted by the larger universe of student files examined, the net result being that the recovery would be lower than if they were not included. Also, by including ATB students, the sampling process results in a clearer picture of liability -- it recognizes the reality that some ATB students had their refunds calculated in error while some had them calculated correctly and, therefore, the result is more accurate. Most important, there is absolutely no indication in the record that refunds for ATB students were treated any differently than for non-ATB students.

Consistent with the above, I find that the most appropriate method of calculating liability for the second finding is to consider the universe to be all students who withdrew, to include the appropriate ATB students. Applying that determination to the facts, I find that American owes $359,883 for this finding.

[12] As noted earlier, American made its proposal regarding the ATB liability by extrapolating a sample in its appeal as well as in its Initial Brief and exhibits. In its two separate responsive pleadings, FSA chose, for some unspecified reason, not to address American's input or submit any evidence that contradicted the same.

ORDER

On the basis of the foregoing findings of fact and conclusions of law, it is ORDERED that American Business College pay to the U. S. Department of Education $186,148 for the ATB violation and $359,833 for the refund violation for a total of $545,981.

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Ernest C. Canellos
Chief Judge

Dated: March 24, 2005

SERVICE

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

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