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

In the Matter of	**Docket No. 04-25-SP**
INSTITUTO FONTECHA,	Federal Student Aid Proceeding
Respondent.	PRCN: 200330221784

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

Denise Morelli, Esq., Office of the General Counsel, United States Department of Education, Washington, D.C., for Office of Federal Student Aid.

Before: Richard F. O'Hair, Administrative Judge

DECISION

Instituto Fontecha (Fontecha), located in Santurce, Puerto Rico, and with satellite locations in Caguas, Bayamon, and Rio Piedras, is a participant in Federal Student Aid programs 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.* The Office of Federal Student Aid (FSA), U.S. Department of Education (ED), administers these programs. From June 9 – 13, 2003, reviewers from FSA's New York Case Management Team conducted a program review of Title IV programs administered at Fontecha. The findings of this review are found in the March 1, 2004, Final Program Review Determination (FPRD). Fontecha exercised its right to appeal the findings of this FPRD and requested a hearing.

The first of three findings of the FPRD alleges that Fontecha lacked financial responsibility because two individuals, Mr. Carlos Alfonso Ramirez, also known as Mr. Alfonso, and Ms. Grace Fontecha, improperly played a significant role in the daily operation of Fontecha – their role was improper because of their past performance at a previous institution of higher education. FSA charges that the resulting lack of financial responsibility caused Fontecha to be ineligible to receive federal student aid for award years 1997-1998 through 2002-2003, leading

to institutional liabilities of $10,026,404. The second finding alleges that Fontecha disbursed federal student aid to 273 students at ineligible locations. The last finding in this proceeding alleges that Fontecha failed to make timely, appropriate refunds to ED for students who withdrew prior to the completion of their program.[1] Fontecha has the burden of persuasion in this Subpart H proceeding. 34 C.F.R. § 668.116(d).

Finding 1

To participate in the Title IV programs an institution must meet the standards of financial responsibility. 34 C.F.R. § 668.171. One of the criteria that ED examines to ensure an institution is financially responsible is the past performance of the persons affiliated with an institution. An institution is not financially responsible if a person who exercises substantial control over the institution in question, or any member of that person's family, exercised substantial control over another institution that owes a liability for a violation of a Title IV program requirement.[2] 34 C.F.R. § 668.174(b)(1)(i). The regulations define control as the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise. 34 C.F.R. § 600.31(b).

FSA alleges that Fontecha was not financially responsible because, during the years covered by the program review, Mr. Alfonso and Ms. Grace Fontecha exercised substantial control over Fontecha. FSA further alleges that Mr. Alfonso previously owned and operated York College, Inc. and Ms. Fontecha was on York College Inc.'s board of directors. FSA states that York College owes ED over three million dollars in Title IV liabilities assessed in three final program review determinations issued between May 1993 and May 1995. Additionally, FSA asserts that Fontecha was not financially responsible because Mr. Santiago Parlade, the school's majority stockholder, failed to disclose on Fontecha's applications for recertification in 1997 and 1999 that his mother, Ms. Fontecha, was on the York College board of directors.[3] Therefore, FSA maintains that both of these situations constitute a violation of the past performance provisions of the regulations.

According to FSA, the evidence in the record contradicts Fontecha's claim that Mr. Alfonso, a prior stockholder of Fontecha, was no longer an owner or administrator at Fontecha. First, FSA points to student statements in which the students claimed Mr. Alfonso handled all the administrative problems which arose at the school. Next FSA proffers evidence that students claimed that Mr. Alfonso introduced himself as the director of Fontecha at new student orientations and that Ms Fontecha introduced herself as one of the school's owners. Finally,

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[1] Liability for the second and third findings was subsumed in the FPRD's liability for the first finding.

[2] *See generally*, *In the Matter of Teddy Ulmo Institute*, Dkt. No. 03-42-SF, U.S. Dep't of Educ. (April 5, 2005).

[3] Mr. Alfonso and Ms. Fontecha were married at the time Ms. Fontecha served on York College Inc.'s board of directors but were divorced shortly thereafter. Ms. Fontecha is also the mother of Mr. Alejandro Farinacci, the Director of Fontecha's Bayamon campus.

FSA asserts that Fontecha's own employees described Mr. Alfonso as one of the Directors/Managers of the school, an opinion they developed because he seemed to make all of the major decisions and he would go to the various locations to ensure the employees were working and enrolling students.

Fontecha argues that Mr. Alfonso had no authority to make ultimate decisions regarding operations and management and, therefore, did not exercise substantial control over the institution. Although Mr. Alfonso previously served as its director, Fontecha asserts that he was fired in 1997 because FSA had determined his past performance with York College rendered him ineligible to remain as the school's director. Fontecha maintains Mr. Alfonso had no formal association with the school until he was hired in 2001 as a consultant for accreditation and marketing; he was not hired to perform any director or management functions. Fontecha states that Mr. Alfonso sold his stock in the school to Mr. Colon in 1993, leaving Mr. Colon and Mr. Parlade as the sole stockholders in the corporation doing business as Fontecha. To support its position, Fontecha submitted copies of the stock certificates and a statement from a CPA who has examined the school records and concludes that Mr. Parlade and Mr. Colon are the sole owners. Fontecha also submitted sworn statements from Mr. Alfonso and Ms. Fontecha in which they deny their ownership of Fontecha.

Fontecha further contends that because its president, Mr. Parlade, resided in Miami, some of the responsibilities for handling Fontecha's day-to-day operations were assigned to both his mother, Ms. Fontecha, and Mr. Alfonso, but that neither were given authority to exercise substantial control. Fontecha asserts that the student statements supporting FSA's claim of a past performance violation contain insufficient detail to be credible and were made without the students having a complete understanding of the corporate and management structure of the school. The school also suggests that many of the students thought the school was owned by Ms. Fontecha because they both have the same name, and because of her frequent presence on the campus where she had an office for her modeling school, Fontecha Modeling Academy. Fontecha further states that Mr. Alfonso and Ms. Fontecha were not regular attendees of the orientation programs for new students, and when they did attend, they did not tell the students they owned the school.

Based on my review of the evidence, I have concluded Fontecha was not financially responsible during the award years in question because persons who exercised substantial control over Fontecha had previously exercised substantial control over another institution that owes a liability for a violation of a Title IV program requirement. Respondent concedes that during Mr. Parlade's absence from Puerto Rico, Mr. Alfonso and Ms. Fontecha had, or were given, authority to supervise the day-to-day operations of the school. Moreover, it is also apparent to me that the level of their daily activities and public statements indicate they also exercised the authority to direct the management and policies of the school. The record also reveals that Mr. Alfonso and Ms. Fontecha owned, or exercised substantial control over, York College, an institution that currently owes ED over three million dollars in Title IV liabilities. Arming Mr. Alfonso and Ms. Fontecha with the authority to operate the school was an irresponsible action and one which should have been familiar to the school, in light of Mr. Alfonso's removal from the position of director in 1997 for the very same reason. With these

facts before me, I find that Fontecha was not financially responsible during the award years in question because of this past performance violation.[4]

Finding 2

FSA next asserts that Fontecha made illegal disbursements of Title IV funds to 273 students enrolled in ineligible programs at ineligible locations. When an institution receives a certificate of eligibility under Title IV, that certificate applies to all locations identified in its application and approved by ED. 34 C.F.R. § 600.10(b). Generally, if, at a later time, the institution wishes to provide instruction at an additional location, it must notify ED of its intentions before it disburses Title IV funds. 34 C.F.R. § 600.21(a). If the institution acquires the assets of another institution that provided educational programs at that location during the preceding year and participated in the Title IV programs during that year, then the acquiring institution must apply to ED and wait for approval before disbursing funds to the students at that additional location. 34 C.F.R. § 600.20(c)(1)(iii); 34 C.F.R. § 600.20(f)(3). However, if the applicant wants to provide instruction at the site of a closed institution that owes a liability for violations of Title IV, and the applicant acquired the assets of that closed location, then the applicant must wait two years before applying for certification for that location. 34 C.F.R. § 600.32(b). This two-year period can be waived if the acquiring institution agrees to repay all liabilities owed by the closed institution. 34 C.F.R. § 600.32(c).

According to FSA, Fontecha provided a teach-out for students who were enrolled in two institutions that had been terminated from participation in the Title IV programs and owed liabilities for violations of Title IV; and Fontecha acquired the assets of the two institutions. Fontecha conducted the teach-out at the three locations of the terminated institutions: Caguas, Bayamon, and Rio Piedras, Puerto Rico. FSA states that the teach-out began in March 2002 and Fontecha made the last Title IV disbursements for these students by November 2002. In September and October of that year, Fontecha submitted an application to add new programs at these three locations and ED requested the school to submit licensing and accreditation information for them. ED determined that Fontecha had acquired the assets of the terminated schools and that the locations could not be Title IV eligible locations for a period of two years. FSA asserts that ED telephonically notified the school of this determination on January 9, 2003, in person on January 31, 2003, and in writing on February 11, 2003. Fontecha paid the Title IV liabilities incurred for the Caguas location in order to obviate the two-year waiting period and ED approved Caguas' eligibility on March 6, 2003. The Bayamon and Rio Piedras locations remained ineligible for Title IV purposes.

FSA states that it obtained documents and statements that confirm Fontecha's instruction at the ineligible Bayamon and Rio Piedras locations and the school's disbursement of Title IV funds after its teach-out at those locations ended. Consequently, FSA asserts that Title IV disbursements made to students after the teach-out ended in November 2002 were improper. FSA identified disbursements to 273 students that totaled $880,979, some of which FSA asserts

[4] There is insufficient evidence to find that Mr. Parlade failed to properly complete his 1997 and 1999 applications for recertification.

were made after Fontecha was notified on two occasions in January and once in February 2003 that these disbursements were impermissible.

Fontecha concedes that it authorized Title IV funds for its students at these two locations in anticipation of the students either attending classes at an eligible location or the locations becoming eligible, but it asserts it did not disburse these funds until the students moved to eligible locations. Fontecha states it moved the Rio Piedras students to its eligible Santurce campus on February 3, 2003, and the Bayamon students were transferred to Santurce on March 3, 2003.[5] It maintains that, once the students were relocated to eligible locations, it was then entitled to Title IV funds for the second and third payment periods.

FSA challenges Fontecha's assertion that it moved its students to Santurce prior to the end of the second academic period. FSA argues that its interviews with Fontecha's students and faculty show that the bulk of the students did not transfer to Santurce until well after they received Title IV disbursements while still attending classes at the ineligible Bayamon and Rio Piedras locations. FSA also asserts that its reviewers discovered classes were still being conducted at the Bayamon and Rio Piedras locations at the time of their June 2003 program review. Finally, FSA reports that a number of students stated that they attended classes in Santurce during March and April 2003, but then resumed classes at the ineligible locations. FSA states that students claimed they were once again relocated to the Santurce location at the time of the program review.

The tribunal finds that Fontecha disregarded the eligibility limitations imposed on it by the regulations and improperly drew down and disbursed Title IV funds to students who it scheduled for attendance at ineligible locations. The school continued these Title IV disbursements even after repeated notifications from ED personnel that Bayamon and Rio Piedras were ineligible locations. Fontecha has failed to convince me their activities complied with the requirement that it disburse Title IV funds only to students enrolled in classes conducted at eligible locations, with the exception of six students[6] out of 273 who they have shown did make the move to the Santurce location. Final liability for this section is subsumed in that of the first finding.

Finding 3

FSA alleges that Fontecha failed to properly and timely calculate refunds for students who withdrew from the institution.[7] According to FSA, Fontecha labeled students who stopped attending classes during an academic quarter as withdrawals; it labeled students who completed the previous academic quarter but failed to return for a subsequent quarter as inactive. For four

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[5] Fontecha admits that it erred by crediting the accounts of seven Bayamon students on February 3, 2003, prior to their move to Santurce, and returned the funds for these students to ED.

[6] Student Nos. 100, 155, 263, 277, 305, and 306.

[7] Initially, there were 21 instances of violations in this finding that involved 20 students, with Student No. 119 being included in two categories. FSA withdrew its allegation regarding one student (Student No. 9), thus leaving 20 instances of violations involving 19 students.

of the 20 instances at issue, FSA asserts that the school failed to classify these students as withdrawals warranting the computation of refunds.[8] For nine of these 20 instances, FSA asserts that Fontecha failed to calculate refunds.[9] For the remaining seven instances, FSA asserts that Fontecha failed to make timely refunds.[10] In summary, after withdrawing student No. 9 from consideration, FSA charges that refunds were not made in 13 instances and there were seven late refunds.

For all students who withdraw from classes before completing a school term, the institution must determine if the amount of Title IV assistance disbursed to the student exceeds the amount of Title IV funds earned as of the date of the withdrawal. 34 C.F.R. § 668.22(j)(1). All unearned Title IV funds must be returned to ED within 30 days of the institution's determination that the student withdrew. *Id*.

Fontecha admits that it owed refunds in 19 of the 20 instances at issue and that those 19 refunds have been paid. Fontecha next argues that a refund is not due for one student (Student No. 10) because the student attended the Santurce location, an eligible location. Fontecha also concedes that 11 of the 19 refunds it agreed it owes were not timely; however, it asserts that all refunds have been paid. Therefore, it maintains that its only liability is $237.59 for imputed interest for these late refunds. The school also denies there was any intent to defraud ED of these refunds; rather, it argues that its failure to timely calculate and pay the refunds was an oversight due to the school's difficulty in determining when a student has withdrawn.

FSA counters Fontecha's assertion that Student No.10 was not due a refund by pointing to evidence that the student dropped out of school about the second or third week of the fall 2002 semester. Additionally, FSA disagrees with Fontecha's assertion that the school made refund payments to ED for those students that it admitted were due. After examining the school's student ledger cards, FSA contends that Fontecha is not claiming that it actually sent a check to ED for the amount in question, but rather that the school deducted the amount of the refunds from the amounts Fontecha claimed in its reimbursement requests to ED. According to FSA, for whatever reason, these reimbursement requests have not been processed; therefore, ED has received no payment or credit for these refunds.

The record reveals, and the parties do not dispute, that refunds were due for 19 of 20 instances and that late refunds were made on behalf of seven students. The evidence also reveals that Student No. 10 was due a refund because this student withdrew from school early in the fall 2002 semester. Fontecha did not submit any evidence supporting its assertion that it already made 19 of the 20 refund payments at issue. Further, if FSA's characterization of Fontecha's claimed payment of refunds is correct, it is beyond the authority of this tribunal to offset liabilities assessed in a Subpart H proceeding with amounts that may be due under claims filed by a school

[8] Student Nos. 5, 10, 48, and 122.
[9] Student Nos. 23, 46, 49, 65, 75, 84, 101, 119, and 126.
[10] Student Nos. 2, 12, 14, 24, 81, 119, and 192.

under ED's reimbursement system.[11] Consequently, I find that Fontecha has not demonstrated that it has paid the owed 19 refunds. Therefore, Fontecha remains liable for its failure to properly and timely pay refunds for the cited instances.[12]

ORDER

On the basis of the foregoing, it is hereby **ORDERED** that Instituto Fontecha pay $10,026,404 to the United States Department of Education.

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Judge Richard F. O'Hair

Dated: May 22, 2006

[11] *See In re Modern Trend Beauty School*, Dkt. No. 98-109-SP, U.S. Dep't of Educ. (March 14, 2001).

[12] FSA did not separately compute a liability for Finding No. 3 because it was subsumed within Finding No. 1.

SERVICE

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

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