



UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF HEARINGS AND APPEALS
400 MARYLAND AVENUE, S.W.
WASHINGTON, D.C. 20202
TELEPHONE (202) 245-8300

In the Matter of

Salon and Spa Institute,

Docket No. 18-16-SP

Federal Student Aid Proceeding

PRCN: 2016-3062-9350

OPE ID: 04169000

Respondent.

Appearances:

Anthony P. Troiani, Anthony P. Troiani, PC, for the Respondent, Salon and Spa Institute
Alexandra Sweeney, Office of the General Counsel, U.S. Department of Education for Federal Student Aid.

Before: Angela J. Miranda, Administrative Law Judge

DECISION

I. Jurisdiction and Procedural History

Salon & Spa Institute is a proprietary institution of higher education, offering non-degree 1-year programs and has been accredited by the National Accrediting Commission of Career Arts and Sciences (NACCAS) since at least September 2009. Institute for Esthetics and Cosmetology, L.L.C. (IEC, LLC) is a Texas limited liability company, whose members at formation were Aurora Lozano (Lozano), Julius “Rusty” Brechot (Brechot), and Mark A. Johnson (Johnson). IEC, LLC conducts business as Salon and Spa Institute (SSI or Respondent) operating in Brownsville, Texas. On about May 6, 2010, SSI submitted an application to participate in Federal Student Loan programs authorized under Title IV of the Higher Education Act of 1965, as amended (Title IV).¹ On July 15, 2010, SSI was granted provisional approval for participation, which extended through June 30, 2012, unless SSI reapplied for continuing participation. The Department asserts that SSI applied for recertification on January 12, 2012. On November 28, 2012, SSI was granted a program participation agreement (PPA), removing the provisional approval and extending SSI’s participation through September 30, 2016.

¹ 20 U.S.C. § 1070 *et seq.*

Although not related to this appeal, on or about February 20, 2012, SSI self-reported specific violations of statutory and regulatory requirements for the administration of Title IV funds to certain students without high school diplomas who demonstrated the ability to benefit from Title IV. Following that self-report, SSI was placed on heightened cash monitoring and a review by Federal Student Aid ensued.²

As related to this appeal, the parties agree that on January 14, 2014, the United States Department of Education (Department) became aware of a change in ownership that resulted in a change of control. Despite that agreement, the record is devoid of any documentary evidence establishing this as the date that SSI properly filed an application identifying a change in ownership. On February 4, 2015, following receipt of the January 30, 2015 letter from SSI's accrediting agency, Federal Student Aid (FSA) sent SSI a notice of loss of eligibility as of January 2, 2012. About a month after that notice was sent, on about March 4, 2015, SSI initiated an electronic application with the Department identifying a change of ownership that occurred on February 28, 2013. This was followed by a notice on April 6, 2015, that SSI's application for extension of its certification based on a change in ownership that resulted in a change of control was granted. On April 24, 2015, SSI was notified that a program review will be conducted to determine liabilities resulting from the institutions ineligibility from January 2, 2012 to April 5, 2015.³ A review was conducted on May 19 and 20, 2016, which was followed by issuance of a Program Review Report (PRR) on June 17, 2016.

Following receipts of SSI's initial and supplemental responses to the PRR, on January 25, 2018, the Department, FSA issued a Final Program Review Determination (FPRD) determining that SSI was ineligible to receive Title IV funds from January 2, 2012, when there was an unreported change of ownership, until April 5, 2015, the date prior to the Secretary's approval of SSI's electronic application. Consequently, FSA assessed a liability of \$1,228,774.32 for Title IV funds disbursed during that time period. In a letter dated March 13, 2018, SSI timely filed a request for a hearing to challenge that finding and liability assessment in the FPRD.

The Respondent filed an initial brief, FSA filed its responding brief, and the Respondent filed an optional reply brief. Following those submissions, this Tribunal required the Respondent to file a supplemental brief addressing a single issue of whether IEC, LLC, doing business as SSI, is a closely-held corporation, a publicly traded corporation, or other corporation as defined in 34 C.F.R. § 600.31(c) and FSA was provided an opportunity to file a reply to the supplemental brief.

² In response to this self-report, the Department conducted a program review of SSI from April 22 to 26, 2013. The Department issued a FPRD on March 22, 2016, assessing a liability, and SSI's timely appeal was filed on May 11, 2016. OHA assigned that appeal a docket number of 16-23-SP. An initial decision was issued on January 19, 2018, which is currently on appeal to the Secretary. The Respondent references this prior review herein and argues that SSI's disclosure to the Department and cooperation SSI provided to the Department's OIG in relation to that misdeed are evidence that SSI met its fiduciary duties herein, and therefore, absolve SSI of the liability imposed for its failure to timely report multiple changes in ownership that occurred following SSI's May 6, 2010 application for participation in Title IV, HEA programs.

³ In addition to these formal actions/contacts, the Respondent, through its representative initiated an informal (email) contact on November 15, 2014 directly with a compliance manager at FSA.

Upon reviewing the briefs and evidence filed in this appeal, I requested additional evidence. Specifically, I requested a copy of the April 6, 2015 PPA and the Eligibility and Certification Approval Report (ECAR). I received those documents along with the associated electronic application. I notified the representatives that I intended to add those documents to the record as a post-hearing exhibit. Each party was given an opportunity to object to the addition of these documents. Counsel for FSA had no objection. Counsel for the Respondent indicated he had no objection but conditioned his “no objection” upon the parties agreement and this Tribunal’s awareness that the change of control references the removal of the previous director and member of IEC, LLC, Lozano, which was carried out in March 2013 as “dictated by the Department.” I consider Respondent’s condition an objection to add this post-hearing exhibit to this record.

Having carefully considered Respondent’s objection, I find this exhibit is relevant and material to this appeal, overrule Respondent’s objection, and order that the exhibit be added to the administrative record. The PPA, ECAR, and Electronic Application are Department of Education records and materials consistent with 34 C.F.R. § 668.116. The information therein provide evidence that was previously absent from the record and facilitates understanding of the electronic application filed by SSI, as well as the review by the Department, which resulted in SSI’s eligibility to participate in Title IV HEA programs. Furthermore, the record is devoid of any evidence that the Department “dictated” the removal of Lozano as a director of SSI and member of IEC, LLC, except for the assertion in counsel’s objection.

Having been fully briefed, the administrative record is closed, and this matter is ready for decision.

II. Issues

1. Whether there was a change in ownership resulting in a change of control at SSI and, if so, when did such a change occur that made SSI ineligible to participate in Title IV, HEA programs?
2. If SSI had a change in ownership that made it ineligible to participate in Title IV programs, for what period was SSI ineligible?

III. Legal Framework/Applicable Laws and Regulations

A. Applicable Statute

Consistent with the Higher Education Act (HEA) of 1965, as amended,⁴ an institution of higher education qualifies for participation in Title IV, HEA programs upon the Secretary’s determination that the institution has the legal authority to operate within a State, has accreditation status, and has administrative capability and financial responsibility (20 U.S.C. § 1099c(a)). In determining an institution’s eligibility for participation, the Secretary makes a determination if the institution has the financial responsibility to meet all of its financial obligations, including refunds of institutional charges and repayments to the Secretary for liabilities and debts incurred in programs administered by the Secretary (20 U.S.C. §1099c(c)(1)(C)). The Secretary is authorized to establish an “administrative capacity standard”

⁴ 20 U.S.C. § 1070 *et seq.*

and may obtain financial guarantees from owners of the institution (20 U.S.C. § 1099c(d) and (e)). Financial guarantees may be required from one or more individuals who the Secretary determines exercise substantial control over the institution (20 U.S.C. § 1099c(e)(1)(A)).

The Secretary may determine that an individual exercises substantial control over the institution if an individual, directly or indirectly, controls a substantial ownership interest in the institution; if an individual, alone or together with other individuals, has a substantial ownership interest in the institution under a voting trust, power of attorney, proxy, or similar agreement; or if the individual is a member of the board of directors, the chief executive officer, or other executive officer of the institution (20 U.S.C. § 1099c(e)(2)(A)(i)-(iii)). The Secretary may determine that an entity exercises substantial control over the institution if an entity holds a substantial ownership interest in the institution (20 U.S.C. § 1099c(e)(2)(B)). Furthermore, an ownership interest is defined as a share of the legal or beneficial ownership or control of, or a right to share in the proceeds of an institution (20 U.S.C. § 1099c(e)(3)).

When an eligible institution of higher education has a change in ownership resulting in a change of control, then that institution's qualification to participate in Title IV programs terminates, unless that institution obtains continuing certification (20 U.S.C. § 1099c(i)(1)). The statute includes some examples of actions that may result in a change in control, but the list of examples is not exhaustive (20 U.S.C. § 1099c(i)(2)(A)-(F)).

All changes of ownership, however, do not result in a loss of eligibility. The statute identifies two examples of when a change in ownership does not result in a change in control (20 U.S.C. § 1099c(i)(3)). The first is when the sale or transfer occurs upon the death of an owner and the decedent's ownership interest is passed to a family member or a person holding an ownership interest in that institution (20 U.S.C. § 1099c(i)(3)(A)). The second is an action determined by the Secretary to be a routine business practice (20 U.S.C. § 1099c(i)(3)(B)).

B. Applicable Regulations

The Secretary's regulations provide specific requirements for an institution wishing to establish eligibility, maintain eligibility, and when an institution loses eligibility (34 C.F.R. § Part 600, Subparts B, C and D). When applying for initial eligibility an institution's application must establish it qualifies as an eligible institution (34 C.F.R. § 600.20(a)(1)). If it wishes to participate in Title IV, HEA programs, it must show it meets the requirements for participation in those programs as well as the requirements for financial responsibility under Part 668 (34 C.F.R. § 600.20(a)(2)). When initially applying, or reapplying to continue eligibility beyond the scheduled expiration of current eligibility, an institution is required to update application information (34 C.F.R. § 600.21). The institution is required to report certain changes, in a manner prescribed by the Secretary, within ten (10) days after those prescribed changes occur (34 C.F.R. § 600.21(a)). Furthermore, a designation of eligibility by the Secretary based on inaccurate information or documentation is void from the date the Secretary made the designation (34 C.F.R. § 600.40(c)(1)).

One prescribed change that requires reporting and that effects an institution's eligibility, is a change in a person's ability to affect substantially the actions of the institution if that person did

not previously have this ability (34 C.F.R. § 600.21(a)(6)). The Secretary considers a person to have the ability to substantially affect the action of the institution if the person, alone or with others, holds at least a 25 percent “ownership interest” as defined in § 600.31(b) or is a general partner, the chief executive officer, or the chief financial officer of the institution (34 C.F.R. § 600.21(6)(ii) and (iii)).

When there is a change in ownership that results in a change in control, an institution ceases to qualify as an eligible institution upon the change in ownership and control (34 C.F.R. § 600.31(a)(1)). A change in ownership that results in a change in control includes any change by which a person who has or acquires an ownership interest in the entity who owns the institution, acquires or loses the ability to control the institution (*Id.*). A private for profit institution that has undergone a change in ownership that results in a change in control may continue participation in Title IV HEA programs if a materially complete application is submitted no later than ten (10) business days after the change occurs (34 C.F.R. § 600.31(a)(2)(i)).

The regulations specify standards for identifying changes of ownership and control (34 C.F.R. § 600.31(c)). The standards are specific to seven types of business structures or institutions, including closely-held corporations, publicly-traded corporations, other corporations, partnerships or sole proprietorships, parent corporations, nonprofit institutions, and public institutions (34 C.F.R. § 600.31(c)(1)-(7)). The regulations, consistent with the authorizing statute, recognize that a change in ownership that results in a change of control is determined based on the type of ownership (i.e. business structure) or institution (nonprofit or public). As more fully discussed later in this decision, the business structure identified as “other corporations” applies to the business structure of IEC, LLC and ownership of SSI.

The category for other corporations applies to entities that are neither closely-held corporations nor corporations required to be registered with the Securities and Exchange Commission, i.e. publicly-traded (34 C.F.R. § 600.31(c)(3)). Subparagraphs (i) and (ii) apply to stock issuing corporations and subparagraph (iii) applies to “membership corporations.”⁵ In a membership corporation, a change in ownership that results in a change in control occurs when “a person who is or becomes a member acquires or loses control of 25 percent of the voting interests of the corporation and control of the corporation” (34 C.F.R. § 600.31(c)(3)(iii)).

The regulations include definitions used to assess when an institution undergoes a change in ownership that results in a change in control (34 C.F.R. §600.31(b)). Those applicable to this analysis are control, ownership or ownership interest, and person. Control means “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.” Ownership or ownership interest means a legal or beneficial interest in an institution, or a right to share in the profits derived from the operation of the institution. Person includes an individual as well as a legal person such as a corporation.

⁵ The Secretary offers definitions in §600.31(b) but does not define membership corporations. Generally, a limited liability company is a type of business structure that allows advantages from the corporate and partnership business structures and ownership is by membership (U.S. Small Business Administration, *Business Guide, Step 5: Choose a business structure*, <https://www.sba.gov/business-guide/launch-your-business/choose-business-structure#section-header-1>, (last visited March 27, 2020)).

An institution that underwent a change in a person’s ability to substantially affect the actions of the institution may apply for provisional extension of its certification (34 C.F.R. § 600.20(g)). The Secretary may continue the institution’s participation on a provisional basis, if the institution under the new ownership submits a “materially complete application” that is received by the Secretary no later than ten (10) business days after the day the change occurs (34 C.F.R. § 600.20(g)(1)). The regulation further directs what is required for a materially complete application (34 C.F.R. § 600.20(g)(2)(i)-(iv)). If the Secretary approves the institution’s materially complete application, the institution will be provided with a provisional PPA. That provisional PPA extends the terms and conditions of the program participation agreement that were in effect for the institution before its change of ownership (34 C.F.R. § 600.20(h)).

C. Applicable Policy

The Department provides policy guidance through annual Federal Student Aid Handbooks.⁶ The policy in relation to change in ownership that results in change of control is found in Volume 2, Chapter 5, Updating Application Information, Change in Ownership.⁷ Department policy informs participating schools that electronic submissions are required and must be made through the internet (Federal Student Aid Handbook, 2009-2010, Vol. 2, Ch. 5, p. 2-52, sidebar “Electronic submission required”). The Department policy tracks closely the applicable statute and regulations and specifically explains the standard of when a change in ownership results in a change of control based on the structure or governance of the eligible institution. The policy explains a change in ownership and control of a corporation that is neither closely held nor publicly traded occurs when a person who has or acquires both control of at least 25 percent of the total outstanding voting stock of the corporation and managing control of the corporation (*Id.* p. 2-54). Lastly, the policy explains the change in ownership interest and 25 percent threshold. The Handbook explains schools must report any change in ownership whenever an owner acquires a total interest of 25 percent or greater, an owner who held a 25 percent or greater interest reduces that interest to less than 25 percent, or when an owner of 25 percent or greater increases or reduces that interest but remains a holder of at least 25 percent (*Id.*).

Applying the law to the facts of this case, changes in ownership that changed SSI’s eligibility to participate in Title IV, HEA programs occurred on June 10, 2010 (while its initial application for participation was pending), January 2, 2012, and March 4, 2013. SSI failed to report these changes to the Department and failed to timely file an electronic application to obtain provisional eligibility after any of these changes. Therefore, SSI is liable for the return all Title IV moneys disbursed from July 15, 2010 until the Secretary approved a provisional PPA on April 6, 2015 (OES Documents 16 and 58).

⁶ Archived copies are available at: <https://ifap.ed.gov/ilibrary/document-types/federal-student-aid-handbook?archive=1> (last visited March 23, 2020) and current copies are available at <https://ifap.ed.gov/ilibrary/document-types/federal-student-aid-handbook> (last visited March 23, 2020).

⁷ All page cites in this decision are to the 2009-2010 edition of the Federal Student Aid Handbook. Notably the content in Volume 2, Chapter 5 was unchanged from the 2009-2010 edition to present (2019-2020 edition).

IV. Arguments and Analysis

A. Respondent's Initial Brief

The Respondent's primary argument is that the Department's termination of Title IV eligibility is contrary to the spirit and intent of the statute and regulations related to change in ownership resulting in a change in control. The Respondent argues the Department's FPRD imposing a liability is unwarranted and unconscionable. In support of this argument, the Respondent asserts that SSI met its fiduciary duty when, on February 20, 2013, two of the owners reported wrongful conduct of a third owner to the Department. Also in support of this argument, the Respondent, citing 20 U.S.C. § 1099c-1(b)(3), asserts the January 12, 2012 change in ownership was an excluded transaction and that SSI should have been permitted to correct or cure this administrative, accounting, or recordkeeping error if the error was not part of a pattern of error when there is no evidence of fraud or misconduct.

The Respondent presents a secondary argument suggesting the Department had other options such as imposing a fine, limitation, suspension, or termination from participation along with an emergency action pursuant to a Subpart G proceeding. In making this argument, the Respondent suggests if this Tribunal concludes there is a reporting violation, then the matter should be remanded to FSA for imposition of a fine, limitation, suspension, or termination and emergency action.

B. FSA's Responsive Brief

In the FPRD dated January 25, 2018, FSA identified and reviewed the June 10, 2010, January 2, 2012, and March 4, 2013 changes in ownership that were not reported to the Department consistent with the applicable regulations and SSI's fiduciary duty. FSA asserts it learned of these multiple changes in ownership only after SSI reported the changes to its accreditation agency and NACCAS issued its January 30, 2015 letter. In that letter, NACCAS approved SSI's changes in ownership as reported by SSI, and continued SSI's accreditation. FSA argued the failure to report the change in ownership that occurred on June 10, 2010, when Lozano's ownership share was reduced from 55 percent to 51 percent, was a serious omission. FSA, however, contends that because Lozano continued to retain a majority ownership interest of 51 percent after this change, it was not a change in ownership that resulted in a change in control. FSA concluded that the January 2, 2012 change in ownership resulted in a change in control. Since SSI failed to file a materially complete application to extend its eligibility within the regulatory prescribed time, FSA calculated liability for Title IV funds dispensed beginning January 2, 2012 through April 5, 2015. FSA primarily relies on sections 1099c(i)(1) and 1099c(i)(2)(B) of the applicable statute and Department regulations at 34 C.F.R. §§ 600.31(a)(1) and (b). FSA asserts that SSI is considered an "other corporation" under the regulations and cites 34 C.F.R. § 600.31(c)(3)(ii) as the applicable regulatory standard for determining a change in ownership as related to SSI.⁸ Lastly, FSA argues the Respondent's reliance on 20 U.S.C. § 1099c-1(b)(3) has no merit as the Respondent's failure to report a change in ownership resulting in a change in control is not an administrative, accounting, or recordkeeping error.

⁸ As detailed later in this decision, while I accept FSA's argument that IEC, LLC, SSI's level 1 owner is properly classified as other corporation. I reject FSA's application of subsection (ii) as the standard to be applied to SSI.

C. Respondent's Reply Brief

In its reply brief, the Respondent reiterates its argument that the error in its failure to report the change in ownership was a clerical error and FSA is not limited to the remedy it is seeking. The Respondent, for the first time, raises a defense of laches asserting that the Respondent “confronted the Department with the change of control issue during its NACCAS reaccreditation” and the Department acquiesced when it allowed SSI to continue its participation uninterrupted after January 14, 2014 (OES Documents 41, p. 7 and 49, p. 7). The Respondent argues the Department's delay was unreasonable and has harmed SSI.

D. Tribunal's Required Supplemental Brief

I required supplemental briefing by the Respondent on a specific issue, i.e. whether IEC, LLC, doing business as SSI, was a closely-held corporation, a publicly-traded corporation, or other corporation consistent with 34 C.F.R. § 600.31.⁹ The Respondent's supplemental brief asserts that IEC, LLC is not a closely-held corporation nor a publicly-traded corporation. The Respondent then contends that IEC, LLC's status as a limited liability company creates a different categorization from those set out in the regulation. In support of this contention, the Respondent analyzes the regulation and essentially concludes no portion of 34 C.F.R. § 600.31(c)(3)(i), (ii), or (iii) applies to a limited liability company. Having arrived at this conclusion, the Respondent argues since IEC, LLC's company agreement required a “supermajority when making fundamental business transactions” there was never a change in control under 34 C.F.R. § 600.31.

E. Analysis

Under the Higher Education Act of 1965, as amended, the Secretary makes the determinations on institutional eligibility for participation in Title IV programs (20 U.S.C. § 1099c(a)). In so doing, the Secretary is authorized to establish an “administrative capacity standard” and require financial guarantees from one or more individuals who the Secretary determines exercises substantial control over an institution of higher education (20 U.S.C. § 1099c(d) and (e)). Substantial control in this statute is measured by whether an individual, directly or indirectly, alone or together with other individuals, has or have a substantial ownership interest in the institution or an entity that holds a substantial ownership in the institution (20 U.S.C. § 1099c(e)(2)(A)(i)-(iii)). Consistent with this statute, the Secretary's regulations establish that an individual exercises substantial control over an institution if that individual, alone or with others, holds at least a 25 percent ownership interest in the institution (35 C.F.R. § 600.21(6)(ii)).

Applying this law and these regulations to the uncontested facts of this case, IEC, LLC, the limited liability company doing business as SSI, was co-owned by Lozano, Brechot, and Johnson since at least May 2006, a date prior to SSI's initial application to participate in Title IV

⁹ While FSA asserted IEC, LLC was an “other corporation” under the applicable regulation, the Respondent identified it as a limited liability company and a closely held entity. The Respondent was in the best position to provide clarification as to IEC, LLC's business structure.

programs (OES Document 57, pp. 177-211). Notably, in its initial application for participation SSI was identified as owned 100 percent by IEC, LLC (level 1), Lozano as 55 percent and Hair Do, LLP 45 percent (level 2), and Julius Brechot and Mark Johnson sharing equally the ownership represented by Hair Do, LLP (level 3) (*Id.* at pp. 2-8). Lozano's, Brechot's and Johnson's percentage of interest in IEC, LLC are consistent with the IES company agreement executed as of May 8, 2006 (*Id.* at pp. 177-211). Because Lozano held an ownership individually in IEC, LLC greater than 25 percent ownership interest, by operation of the Secretary's regulation, she exercised substantial control over SSI, the eligible institution. Hair Do, LLP (a partnership), owned 45 percent of SSI, and therefore, by operation of the Secretary's regulation, Hair Do, LLP, as an business entity, owning a share of SSI greater than 25 percent was an entity considered to exercise substantial control. Brechot and Johnson, who jointly owned Hair Do, LLP, were considered together to exercise substantial control over SSI, the eligible institution.

Considering the uncontroverted facts established in NACCAS's January 30, 2015 letter, SSI underwent multiple changes in ownership since May 2006 (OES Document 7). On dates unknown, SSI submitted one application for change of control (change of ownership) and two notifications of non-substantive change: change of ownership.¹⁰ On November 5, 2014, the Respondent's attorney emailed a compliance manger with FSA notifying her that NACCAS recently requested updated program participation agreements and ECARs for the July 15, 2010¹¹ [sic], January 2, 2012, and March 4, 2013 changes in ownership. SSI's attorney acknowledged that SSI cannot provide them because they do not exist, and further asserted SSI will not create them. Notably, the compliance manger responded that PPAs and ECARs were not generated for the July 15, 2010 [sic] and January 2, 2012 changes because those changes were not reported to the Department. The compliance manager reported the most recent change in ownership was under review (OES Document 15).

The information in the January 30, 2015 letter regarding SSI's original ownership structure (identified in the letter as Before the Change) mirrors the information provided by SSI to the Department at the time of its initial application for participation in Title IV programs (OES Document 57, pp. 2-8). According to SSI's filings with NACCAS, a change in ownership occurred on June 10, 2010 (identified in the letter as Change 1). Although IEC, LLC still owned 100 percent at level 1, there was a change in ownership at level 2. With this first change in ownership, Lozano's ownership, at level 2, dropped from 55 percent to 51 percent. Even with this drop in ownership, by operation of the Secretary's regulation, Lozano was still considered to exercise substantial control over SSI, the eligible institution. This change shows that Hairdo Beauty School, an entity not previously reported as an owner of SSI, owned 49 percent of SSI at level 2.¹² By operation of the Secretary's regulation, Hairdo Beauty School is a business entity

¹⁰ Respondent's briefs and arguments are devoid of any explanation or evidence as to how SSI determined whether an application or notification was required for each change that was reported. The Respondent failed to provide any copy of the application or notifications and instead relies on the information provided in the July 30, 2015 letter as evidence of changes in ownership that occurred. I take official notice that NACCAS maintains a website that allows both public and member access and NACCAS publishes a variety of Standards and Polices for public review and member benefit (National Accrediting Commission of Career Arts & Sciences, <https://www.naccas.org/>, last visited March 31, 2020).

¹¹ The date reported in the NACCAS January 30, 2015 letter was June 10, 2010.

¹² Based on name only in this letter, Hairdo Beauty School is a different business entity from Hair Do LLP. Notably, the Respondent has provided no evidence related to this business entity, but SSI is the source of this information in

that is considered to exercise substantial control over SSI, the eligible institution. After this change, Hair Do LLP's¹³ ownership was reduced from a prior owner of 45 percent at level 2 to a 2 percent owner at level 3. After this change, Brechot and Johnson continued as level 3 owners, equally owning the remaining level 3 ownership interest. By operation of the Secretary's regulation, Hair Do, LLP along with Brechot and Johnson, as owners of Hairdo Beauty School, were considered to exercise substantial control over SSI, the eligible institution. Based on the evidence included in the January 30, 2015 letter, SSI reported this change to NACCAS by filing a notification of non-substantive change: change in ownership, even though this change in ownership is a substantial change in the ownership and control of SSI, as defined in the Secretary's regulation. There is no evidence in the record that SSI reported this change in ownership to the Department while its initial application was pending or within 10 business days after the change occurred.

The information in the January 30, 2015 letter established there was another change in ownership of SSI that occurred on January 2, 2012. SSI reported this change by filing application for Change of Control (Change of Ownership) with NACCAS. This change, identified in the January 30, 2015 letter as Change 2, reported that as of January 2, 2012, SSI continued to be owned 100 percent by IEC, LLC at level 1 and was owned equally by Lozano, Brechot, and Johnson at level 2. By operation of the Secretary's regulation, Lozano, Brechot, and Johnson, as owners of 1/3 of IEC, LLC, each owned at least 25 percent of the institution, and therefore, they were considered to exercise substantial control over SSI, the eligible institution. The previous entities Hair Do, LLP and Hairdo Beauty School no longer had an ownership interest in SSI, the eligible institution. By operation of the Secretary's regulation, Hair Do, LLP and Hairdo Beauty School no longer were considered to exercise substantial control over SSI, the eligible institution. Based on this application as filed by SSI with NACCAS, this change in ownership was a substantive change in ownership and therefore a change in ownership that changed the control of SSI. There is no evidence in the record that SSI reported this change in ownership to the Department within 10 business days after the change occurred.

Lastly, the information in the January 30, 2015 letter regarding a change in ownership of SSI established that on March 4, 2013, SSI underwent a change in ownership and this change was reported by SSI by filing a notification of non-substantive change: change in ownership with NACCAS, identified as Change 3 in the January 30, 2015 letter. With this change, the recognized ownership structure of SSI is that IEC, LLC owns 100 percent at level 1 and Brechot and Johnson own equal shares at level 2. This change in ownership followed the February 4, 2013 termination of Lozano from SSI and the March 3, 2013 special meeting when Lozano was expelled from IEC, LLC (OES Documents 4 and 6). With Lozano's termination from SSI and her expulsion from IEC, LLC, she no longer had the ability to exercise substantial control over SSI, the eligible institution. By operation of the Secretary's regulation, Brechot and Johnson were still considered to exercise substantial control over SSI, the eligible institution, however, Lozano's loss of ownership, made this a change in ownership that resulted in a change in control. The designation of this change in ownership as a non-substantive change in ownership by SSI in its application to NACCAS is contrary to the Secretary's regulations. There is no evidence in the

its application and notices to NACCAS.

¹³ The January 25, 2015 letter indicates the 2 percent owner as Hairdo LLC, but presumably this should have been Hair Do LLP, consistent with the original ownership structure when Hair Do LLP was a level 2 owner at 45 percent.

record that SSI reported this change in ownership to the Department within 10 business days after the change occurred. Instead, both the Respondent and FSA report this change in ownership was reported to the Department on January 14, 2014, about ten months after the actual change.¹⁴ Despite this agreed upon report date, SSI's electronic application to the Department, was not filed until at least March 4, 2015. Thereafter, the Department issued the April 6, 2015 ECAR and Provisional PPA restoring SSI's participation in Title IV, HEA programs (OES Document 58).

The Secretary has the authority to determine if an individual or entity exercises substantial control over an institution (20 U.S.C. § 1099c(e)(2)(A)(i)-(iii) and (B)). Consistent with that statutory authority, the Secretary's regulations at 34 C.F.R. § 600.31(c), establish standards to determine when there is a change of ownership resulting in a change of control. This regulation establishes standards based on seven specified business entities or types of educational institutions and consistent with the regulations and evidence in this record, the applicable type of business entity for SSI is other corporations.

I accept Respondent's argument in the supplemental brief that IEC, LLC is not a closely-held corporation nor a publicly traded corporation. I accept FSA's argument that the standard to be applied to evaluate the change in ownership of SSI falls under the classification of other corporations in the Secretary's regulation. I reject Respondent's argument that IEC, LLC, as a limited liability company, creates a different categorization from those enumerated in the regulation. In rejecting this portion of Respondent's argument and accepting FSA's argument, I take official notice of common business structures as identified by the United States Small Business Administration (SBA).¹⁵ Based on the SBA's explanation that a limited liability company allows its member owners to take advantage of the some benefits of corporate business structures, it is appropriate to apply the standards the Secretary established for other corporations (34 C.F.R. § 600.31(c)(3)).

This section of the regulation includes three subsections. The first two use language relating to ownership interests as voting stock, signaling these two standards apply to stock issuing corporations (34 C.F.R. §600.31(c)(3)(i) and (ii)). The third subsection includes language related to a membership corporation (34 C.F.R. §600.31(c)(3)(iii)). Also, in support of application of this subsection, I note the evidence of IEC, LLC's company agreements included in this record, which identify IEC, LLC's ownership as one of membership (OES Documents 10 and 57, pp. 177-211). Since IEC, LLC, is neither a closely-held corporation nor required to be registered with the SEC, but is a membership company, then application of 34 C.F.R. § 600.31(c)(3)(iii) is appropriate.

With this finding, I reject FSA's argument and reliance on 34 C.F.R. § 600.31(c)(3)(ii), which led to FSA's conclusion that the change in ownership that occurred on June 10, 2010 (after SSI filed its application for participation but before SSI was awarded a Provisional PPA on July 15, 2010) was not a change in ownership that resulted in a change in control. To the

¹⁴ While both the Respondent and FSA assert SSI properly reported this change in ownership on January 14, 2014, the electronic application filed by SSI reporting this change in ownership is dated as March 4, 2015 (OES Document 58, p. 37). This evidence establishes that SSI did not report the change in ownership, electronically over the internet, as required by the Secretary, until at least March 4, 2015.

¹⁵ U.S. Small Business Administration, Review of Common Business Structures, <https://www.sba.gov/business-guide/launch-your-business/choose-business-structure#section-header-1> (last visited March 27, 2020).

contrary, SSI is the sole source of the information that the ownership of SSI changed on June 10, 2010 when SSI reported that change to NACCAS. SSI never provided an adequate explanation as to why it did not report this change to the Department while its May 6, 2010 application was pending as required by 34 C.F.R. § 600.21(a)(6). Without accurate information, the Secretary's designation of SSI as an eligible institution is void under 34 C.F.R. § 600.40(c)(1). Furthermore, the information that the entity Hairdo Beauty School was a new owner with a 49 percent ownership share of IEC, LLC originated with SSI when it filed a notification of non-substantive to substantive change form with NACCAS. SSI provided no explanation of why it chose to file a non-substantive to substantive change form to report this change to NACCAS.

The change in ownership that occurred on June 10, 2010, when Hairdo Beauty School (not a prior owner) acquired 49 percent ownership of SSI is a change in ownership that required reporting and this change in ownership resulted in a change in control of the educational institution. This is a change in control consistent with 34 C.F.R. § 600.21(a)(6)(ii), because Hairdo Beauty School, who previously had no ownership interest in SSI, gained an ownership interest that was more than 25 percent. While this first-time owner, Hairdo Beauty School, acquired an ownership interest in SSI, Hair Do LLP, an initial owner of 45 percent of SSI at level 2, dropped from a level 2 owner to only a 2 percent ownership interest at level 3. This loss of ownership also triggered SSI's reporting of this change in ownership that resulted in a change in control of SSI and SSI's failure to do so when its initial application for participation was pending, rendered the July 15, 2010 Program Participation Agreement void. For these reasons, I find FSA erred in its conclusion that the June 10, 2010 change in ownership was only a "serious omission" and I reject FSA's legal argument that this was not a change in ownership that resulted in a change in control.

The FPRD dated January 25, 2018, issued by FSA, determined the change in ownership that occurred on January 2, 2012 was a change in ownership that resulted in a change in control, necessitating the filing of a materially complete application complete application within ten business days of that change. In support of this conclusion, FSA's brief identified the multiple changes of ownership, but argues only the change in ownership on January 2, 2012 resulted in a change in control. While I agree in conclusion that the change in ownership on January 2, 2012 resulted in a change in control, I disagree with the analysis and argument presented by FSA. While FSA correctly identified other corporations as the applicable standard by which to determine if a change in ownership resulted in a change of control of SSI, FSA's application of 34 C.F.R. § 600.31(c)(3)(ii) is misplaced. As indicated earlier, that subsection applies to stock issuing corporations, which IEC, LLC is not. The change in ownership that results in a change in control on this date is not because Lozano's ownership interest dropped from 51 percent to 33.3 percent share at level 2. The change in ownership that results in a change in control is the elimination of the entity Hairdo Beauty School from an owner of 49 percent at level 2. With this change on January 2, 2012 and the application of 34 C.F.R. §§ 600.21(a)(6)(ii) and 600.31(c)(3)(iii), Lozano, Brechot, and Johnson continued to have the ability to exercise substantial control over SSI, because they each owned at least 25 percent ownership interest in SSI.

As discussed above, the change in ownership that occurred on March 4, 2013, where Lozano was expelled from the ownership of IEC, LLC, is also a change in ownership that resulted in a

change in control. The parties contend that SSI reported this change in ownership to the Department on January 14, 2014, approximately ten months after the change in ownership.¹⁶ FSA asserts it had no knowledge of the multiple changes in ownership prior to this date and it only became aware of the multiple changes when it received the January 30, 2015 letter from NACCAS. This assertion is supported by the evidence the Respondent submitted along with its supplemental brief on November 29, 2019 (OES Document 57). With that evidence, the Respondent filed copies of ECARs printed on April 27, 2011, January 24, 2012, May 20, 2013, and April 6, 2014. Each of the ECARs shows the ownership of SSI remained unchanged from its original report to the Department, i.e. SSI was owned 100 percent by IEC, LLC at level 1, 45 percent by Hair Do, LLP and 55 percent by Lozano at level 2, and equally by Brechot and Johnson at level 3. Notably, the information included in the ECAR was generated from an electronic application filed by SSI. The ECAR printed on April 6, 2015 shows the ownership of SSI as 100 percent by ECI, LLC since May 5, 2006 at level 1 and by Brechot and Johnson equally at level 2 since December 3, 2013 (OES Document 58, p 26). This information is derived from the electronic application dated March 4, 2015 (*Id.*, p. 37).

The Respondent's primary argument is that the Department's action of terminating SSI's Title IV eligibility is contrary to the spirit and intent of the change in ownership statutory and regulatory provisions and consequently, the Department's action and assessed liability is unwarranted and unconscionable. The Respondent presents two rationales in this argument and both are unsupportable in the context of this appeal.

In the first rationale, the Respondent asserts SSI met its fiduciary duty when Brechot and Johnson reported Lozano's wrongful conduct related to the administration of the ability to benefit provisions for individual student eligibility for Title IV HEA program funds. The Respondent asserts the Department continued to allow SSI's uninterrupted participation until February 5, 2015. Whether Brechot and Johnson, as owners of SSI with substantial control of the institution, met their fiduciary duty when they reported the misdeeds of Lozano, an original owner and Director of SSI, is not relevant to this appeal. In this matter, the owners of SSI had a duty to report all changes in ownership, whether occurring during the pending of its initial, or subsequent, application for participation and at any time after a program participation agreement was approved by the Secretary. If a report of a change in ownership was made within ten days of the change and accompanied by a materially complete application, the Secretary could have granted continued provisional participation. The evidence of this record shows SSI failed its duty to report the June 10, 2010, January 2, 2012, and March 4, 2013 changes in ownership and the only electronic application that was filed was not done until March 4, 2015.

The assertion that the Department continued to allow uninterrupted participation by SSI is unsupported as well. The Respondent asserts the report of Lozano's misdeeds occurred on February 20, 2013 and that SSI was placed on heightened cash monitoring about a month later,

¹⁶ FSA's brief identifies this date as a change in ownership. There was no change in ownership on this date, but rather this is the date that both FSA and the Respondent agree that a change in ownership was reported to the Department. FSA does not include any analysis of the March 4, 2013 change in ownership, because it contends this change in ownership does not provide the grounds for the FPRD at issue here. Review of the only online application for change in ownership that was filed with the Secretary, shows SSI was reporting the change in ownership that occurred on March 4, 2013. However, given that FSA determined liability attached at the earlier date occurring on January 2, 2012, it is understandable why FSA's brief concentrated on that earlier change.

on March 21, 2013. While the parties agree that the Department became aware of changes in ownership on January 14, 2014, the evidence in this appeal establishes the Department was unaware of the specifics of the all the changes in ownership, occurring since SSI's initial application, until after it received the information in the January 30, 2015 NACCAS letter. Upon receipt of that information, the Department acted quickly by issuing its February 4, 2015 Notice of Loss of Eligibility (OES Document 38). The evidence also establishes SSI did not file an electronic application reporting a change in ownership until at least March 4, 2015, when SSI reported that Lozano no longer had an ownership interest in IEC, LLC. SSI had a duty to report changes in ownership that result in changes of control and to file a materially complete application within 10 business days of the change, if the institution desired continued participation in Title IV HEA programs. The evidence of this record establishes SSI failed to meet that duty in relation to all changes in ownership occurring on and after June 10, 2010.

In the second rationale, the Respondent asserts the January 2, 2012 change in ownership was an excluded transaction. The Respondent relies on 20 U.S.C. § 1099c-1(b)(3) arguing SSI should be permitted to correct or cure an administrative, accounting, or recordkeeping error if the error is not part of a pattern of error and there was no evidence of fraud or misconduct. Reliance on this statute is misplaced. If SSI committed an administrative, accounting, or recordkeeping error that was revealed in the context of a program review, then this statute allows the institution an opportunity to cure if there was no evidence of fraud or misconduct. SSI's failure to properly report changes in ownership that result in a change in control of the institution is a requirement of continuing eligibility and certification procedures pursuant to 20 U.S.C. § 1099c. This statute allows the Secretary to determine administrative capability and financial responsibility of an institution of higher education. In so doing, the Secretary developed regulatory requirements to be followed by all eligible institutions of higher education. One such requirement is to timely report a change of ownership that results in a change in control. The failure to do so is a failure of the fiduciary duty of the eligible institution and not a mere administrative, accounting, or recordkeeping error. The consequence of such a failure is termination from participation unless that institution obtains continuing certification (20 U.S.C. § 1099c(i)(1), 34 C.F.R. §§ 600.20, 600.21, 600.31, 600.40). The Department's termination of SSI's eligibility to participate in Title IV HEA program funds is consistent with the applicable statute and Department regulations and is not unwarranted, unconscionable, nor contrary to the spirit and intent of the statutory and regulatory provisions.

The Respondent offers a secondary argument that the Department could have imposed a fine or limitation against SSI or commenced an emergency action against SSI rather than terminate SSI's eligibility to participate in Title IV HEA programs for failure to report a change in ownership that resulted in a change of control and failure to file a materially complete application to continue participation. In making this secondary argument, the Respondent contends if this Tribunal concludes there is a "reporting violation" that the Hearing Official may remand the case to FSA to determine if there is a Subpart G violation.¹⁷ The Respondent argues under a Subpart G violation, SSI would have an opportunity to defend against the allegations prior to terminating and due process is better served. This argument fails because Subpart G

¹⁷ Respondent's reliance on the Secretary's decision in *Ambassador Beauty College, Dkt. No. 97-22-ST, U.S. Dep't of Educ.* (Sec. Decision, February 17, 1999) is misplaced as that proceeding allowing a hearing official to exercise some discretion is within the context of a proceeding initiated under Subpart G, of which this proceeding is not.

proceedings do not apply when an institution fails to qualify as an eligible institution because the institution fails to satisfy the statutory and regulatory provisions that define an eligible institution (34 C.F.R. § 668.81(c)(1)).

In the Respondent's reply brief, SSI argues the Department's claims are time barred by the equitable defense of laches. For laches to apply in this case, there would have had to have been an unreasonable delay in the Department's actions and prejudice to SSI as a result of the Department's delay (*See In re Community College System of New Hampshire*, Dkt. No. 09-35-SA, U.S. Dep't of Educ. (June 21, 2010), *see also In re Platt Junior College*, Dkt. No. 90-2-SA, U.S. Dep't of Educ. (Jan. 19, 1990) (Dec. of Secretary)).

The Respondent asserts that SSI "confronted the Department with the change of control issue during its NACAAS [sic] reaccreditation" and the Department acquiesced. The Respondent contends the Department acquiesced when in response to an email on behalf of the Respondent, SSI was informed it is currently eligible to participate in Title IV programs. In making this argument, the Respondent fails to include that the response to the email inquiry advised SSI that the Department is still in the process of determining what action will be taken regarding the unreported changes in ownership. Also, the assessment of current eligibility was further qualified by "[a]s of today." Evaluating this response in the full context of what was occurring on November 6, 2014, when the responding email was sent, is required to determine if there was unreasonable delay and prejudice such that the equitable defense of laches applies.

In November 2014, the Department was aware in some manner that there was a change in ownership of SSI that was not previously reported to the Department. By letter dated January 30, 2015, from NACCAS, the Department received information about changes in ownership that occurred on June 10, 2010, January 2, 2012, and March 4, 2013. On February 4, 2015, the Department issued a notice of Loss of Eligibility (OES Document 38). On March 4, 2015, SSI dated its electronic application disclosing the ownership interest of Lozano, who previously owned a 55 percent ownership interest, and Hair Do, LLP, an entity that previously owned a 45 percent ownership interest of IEC, LLC, were ended on February 28, 2013 (OES Document 58, pp. 30-31). Thereafter, on April 24, 2015, the Department notified SSI it would conduct a program review for the period January 2, 2012 to April 5, 2015. Under these circumstances, the Respondent's contention that it was prejudiced because it relied on specific information provided by the compliance manager to its detriment is unpersuasive. Clearly the Respondent was on notice that the Department was aware of at least one change in ownership of SSI that was not reported to the Department and that the Department was determining what action will be taken. The characterization that this response was the Department acquiescing, is unsupportable and rejected.

Furthermore, any defense of laches that the Respondent asserts is undermined by SSI's failure to properly report the changes that occurred on June 10, 2010, January 2, 2012, and March 13, 2013 to the Department. This defense is further undermined by SSI's failure to submit a materially complete application within the regulatory time limit, within ten business days of those changes, if SSI wished to obtain continuing provisional approval for participation from the Secretary.

The Department reviewed all the changes in ownership as cited in NACCAS's January 30, 2015 letter. Although the Department, in the FPRD and in its brief, accepted the representation from NACCAS that the June 10, 2010 change in ownership was not a change in ownership that resulted in a change in control, as discussed previously in this decision, I find this determination is inconsistent with the applicable statute and regulations. I take official notice that NACCAS's determination was based on the forms and application filed by SSI. SSI provided no explanation as to why it selected the forms and application when it finally notified the accreditation agency of these multiple changes in ownership. Furthermore, SSI failed in its duty to report those changes to the Department and submit a materially complete application to secure continued provisional approval for participation. Although FSA accepted those classifications of changes as recognized by NACCAS, that was an error and inconsistent with the applicable statute, regulations, and its own policy.

In my review of this appeal, I am bound by the applicable statute and Department regulations and I may not waive them (34 C.F.R. § 668.117(d)(1)). I therefore find FSA's determination in the FPRD dated January 25, 2018 is only partially supportable (34 C.F.R. § 668.118(b)). In so doing, I reject the determination that the change in ownership that occurred on January 10, 2010 did not result in a change in control of SSI. The changes in ownership that occurred on January 2, 2012 and March 4, 2013 are also changes in ownership that resulted in changes in control. Because SSI reported only one of these changes in ownership and did not notify the Department that Hairdo Beauty School acquired an ownership interest of 49 percent after SSI filed its initial application for participation, but before the Secretary approved the application on July 15, 2010, the approval of SSI's eligibility was based on inaccurate and unreported ownership information as of that date. SSI's argument placing all the blame for failure to report the required changes on Lozano, one of the initial owners of SSI and the Director of SSI, does not absolve SSI and the other owners of their responsibilities. The evidence shows that Brechot and Johnson were involved in the initial application process. It also shows it was Brechot and Johnson who belatedly reported all the changes in ownership, including the June 10, 2010 change, to NACCAS. Based on the evidence, neither Brechot nor Johnson, as initial owners and the remaining owners of SSI after Lozano's expulsion from IEC, LLC, timely reported any of the changes of ownership to the Department.

The standard for identifying changes in ownership and control of an institution of higher education whose ownership is by membership, like IEC, LLC doing business as SSI, occurs when a person¹⁸ "who is or becomes a member acquires or loses control of 25 percent of the voting interests of the corporation and control of the corporation" (34 C.F.R. § 600.31(c)(3)(iii)). Applying this standard to the uncontroverted facts in this case, SSI was owned 100 percent by IEC, LLC on May 6, 2010 when SSI submitted its application to participate in Title IV HEA programs. At the second level of ownership, SSI was owned 55 percent by Lozano and 45 percent by Hair Do LLP, a business entity in the form of a limited liability partnership. At the third level of ownership, Brechot and Johnson owned equal shares of the 45 percent ownership held by Hair Do LLP. Applying the Secretary's definition of person, Lozano and the partnership Hair Do, LLP are deemed to have had control of SSI at the time of its application for participation and Brechot and Johnson, as joint owners of Hair Do, LLP, were deemed to have

¹⁸ The Secretary defines a person as a legal person (corporation or partnership) or an individual (34 C.F.R. § 600.31(b)).

had control of SSI at the time of application. On July 5, 2010, the Secretary granted provisional approval for SSI to participate in Title IV HEA programs and SSI's first PPA was signed and issued (OES Document 13).

Prior to the grant of provisional approval on July 5, 2010, the uncontroverted facts, as provided by SSI, establish there was a change in ownership of SSI on June 10, 2010. Based on the information that SSI provided to NACCAS, its accreditation agency, with that change in ownership, IEC, LLC continued to own 100 percent of SSI (level 1) but Lozano's ownership changed to 51 percent at level 2. Hairdo Beauty School, an entity who did not previously have any ownership interest in SSI, became a new owner of 49 percent at the level 2 ownership. With this change, the third level of ownership shared the 49 percent owned by Hair Do Beauty School. The division of ownership at level 3 consisted of 2 percent ownership by Hair Do LLP, and 49 percent ownership each by Brechot and Johnson. With this change in ownership, identified by SSI, and applying the standard in 34 C.F.R. §§ 600.21 and 600.40, the entity Hairdo Beauty School gained control of SSI. The Respondent provides no explanation as to why this was reported as a non-substantive change in ownership instead of a change in ownership that resulted in a change of control when SSI reported the change to NACCAS. There is no evidence in the record that SSI reported this change in ownership to the Department while its initial application was pending. Applying 34 C.F.R. § 600.40(c)(1), a designation of eligibility based on inaccurate information is void and therefore, the July 15, 2010 Program Participation Agreement, authorizing SSI's provisional participation is void.

The January 30, 2015 NACCAS letter identified one additional change in ownership of IEC, LLC which was doing business as SSI. This change occurred on or about March 4, 2013, when at Special Meeting of the members of IEC, LLC, members Brechot and Johnson voted to expulse Lozano as a member of IEC, LLC.¹⁹ With that expulsion, SSI reported a change in ownership to NACCAS by filing a notification of non-substantive change: change in ownership. The Respondent provides no explanation as to why this was reported as a non-substantive change in ownership instead of a change in ownership that resulted in a change of control. Applying the standards in 34 C.F.R. § 600.31(c)(3)(iii), Lozano lost control of SSI when her ownership interest was reduced from 33.3 percent to none. There is no evidence in the record that SSI reported this change in ownership to the Department within 10 business days after the change occurred.

Both the Respondent and the Department concur that on January 14, 2014, SSI reported, to the Department, a change in ownership that resulted in a change in control (OES Documents 30, p. 5, 36, p. 4, and 37, p. 9). The record is devoid of any written evidence of the change in ownership that was reported on January 14, 2014. SSI filed only one electronic application and that application was not filed until March 2015. The change in control that was reported in Respondent's electronic application showed a change in ownership at level 2. The application shows that level 2 prior owners of Lozano and Hair Do, LLP were no longer owners of SSI. Under the new ownership, effective December 3, 2013, prior level 3 owners, Brechot and Johnson, were now level 2 owners, each owning 50 percent.

¹⁹ As noted earlier, the Department's brief does not provide a full analysis of this change in ownership because the liability imposed by the determination that SSI lost its eligibility on January 2, 2012, also covers this change in ownership.

V. Findings of Fact and Conclusions of Law

1. Salon & Spa Institute (SSI) is a post-secondary, proprietary institution offering non-degree one-year programs and is accredited by the National Accrediting Commission of Career Arts and Sciences (NACCAS).
2. SSI operates under the ownership of Institute of Esthetics & Cosmetology, LLC (IEC, LLC), a limited liability company registered in the State of Texas.
3. On May 6, 2010, SSI filed an application with the Department to participate in Title IV, HEA programs. On that date, SSI reported that SSI was owned 100 percent by IEC, LLC (level 1 ownership). At level 2 ownership, Aurora Lozano (Lozano) owned 55 percent and Hair Do LLP owned 45 percent. At level 3 ownership of SSI, Julius Brechot (Brechot) and Mark Johnson (Johnson) shared equally in ownership of Hair Do LLP.
4. On a date undetermined in this record, SSI reported a change of ownership of SSI to NACCAS that occurred on June 10, 2010. When SSI reported this change in ownership to the accrediting agency, it was reported as a non-substantive change in ownership instead of a change in ownership that resulted in a change in control. The identification by SSI that this change was a change in ownership that did not result in a change in control of SSI is inconsistent with the Secretary's regulations. On June 10, 2010, the ownership of SSI at the second level changed to 51 percent owned by Lozano and 49 percent by Hairdo Beauty School, an entity that was not previously an owner of SSI. The ownership of SSI at the third level was Hair Do, LLC (presumably a typographical error and meant to be Hair Do, LLP) at 2 percent and the remaining ownership at level 3 was equally shared by Brechot and Johnson. This change of ownership occurred while SSI's application for participation was pending but not yet approved and the record is devoid of any evidence that SSI reported this change to the Department while its application was pending.
5. Without knowledge or notice of the June 10, 2010 change in ownership, SSI was provisionally approved for participation in Title IV, HEA programs by the Secretary with the issuance of a provisional Program Participation Agreement (PPA) on July 15, 2010.²⁰
6. On a date undetermined in this record, SSI reported a change of ownership of SSI to NACCAS that occurred on January 2, 2012. When SSI reported this change in ownership to the accrediting agency, it was reported as a change in ownership and change in control. The identification by SSI that this change in ownership resulted in a change in control of SSI is consistent with the Secretary's regulations. On January 2, 2012, ownership of SSI at the second level changed to equal shares by Lozano, Brechot, and Johnson. There was no longer a third level ownership and Hair Do, LLP and Hairdo Beauty School were

²⁰ On July 1, 2010, the PPA was signed by Aurora Lozano as the Chief Executive Officer for SSI and as a partner/owner and by Julius W. Brechot and Mark A. Johnson as partners/owners. The effective date of this PPA is the date signed on behalf of the Secretary, which was on July 15, 2010.

reported as no longer having any ownership interest in SSI. The record is devoid of any evidence that SSI timely reported this change in ownership to the Department.

7. Consistent with the requirements of the Provisional PPA, SSI reapplied for participation on November 16, 2012 under the signature of Lozano as the Institution's Chief Executive Officer, who also identified herself as the "School Director/Owner." The Secretary approved SSI's reapplication and issued a PPA on November 28, 2012. SSI's participation in Title IV programs was no longer provisional with this PPA. The record is devoid of any evidence that SSI reported the June 10, 2010 or January 2, 2012 change in ownership to the during the reapplication process.
8. On January 29, 2013, Lozano disclosed to Brechot and Johnson that she changed student grades from failing to passing to make those student's eligible for financial aid. On February 4, 2013, Lozano consented to her removal as School Director of SSI with an effective date of January 30, 2013.
9. On February 20, 2013, SSI reported to the U.S. Department of Education that SSI, by Lozano, as School Director, engaged violations of certain requirements under Title IV, relating to the ability to benefit from education or training offered by the institution.²¹
10. At a special meeting of IEC, LLC on March 4, 2013, Lozano was expelled as a member. On that same date, the ownership of SSI was changed. While IEC, LLC continued to own 100 percent of SSI at the first level of ownership, only Brechot and Johnson equally owned SSI at the second level of ownership.
11. SSI reported the March 4, 2013 change in ownership of SSI to NACCAS as a non-substantive change in ownership, representing there was no change in control in the ownership of SSI. This representation made to the accrediting agency is contrary to the Secretary's regulation. With the expulsion of Lozano as a member of IEC, LLC, she lost her ownership interest in SSI and therefore lost control of SSI.
12. Based on changes of ownership that were reported by SSI to NACCAS, the accrediting agency conducted a Show Cause Process on January 21, 2015. On January 30, 2015, NACCAS issued a letter approving SSI's reported changes in ownership and continued SSI's accreditation.
13. On February 4, 2015, the Director of the Dallas School Participation Division of Federal Student Aid notified SSI of its loss of eligibility dating back to January 2, 2012, due to a change in ownership on that resulted in a change in control on that date. SSI was advised this change in ownership was identified during the review of SSI's application for a change in ownership and SSI will be notified of institutional liability in another letter.
14. SSI submitted an online electronic application, dated March 4, 2015, to the Department. In that application, SSI reported that it is still owned 100 percent by IEC, LLC at level 1

²¹ As indicted previously in this decision, liability as a result of that violation, is a matter unrelated to this appeal. An initial decision, Docket No. 16-23-SP was issued on January 19, 2018, and is currently on appeal to the Secretary.

and has been so owned since May 5, 2006. SSI also reported that Lozano's and Hair Do, LLP, whose ownership started on May 5, 2016, ended on February 28, 2013. Lastly, SSI reported that prior owners Brechot and Johnson acquired 50 percent ownership at level 2 (a change from initial ownership at level 3) on December 3, 2013. While the evidence shows this application was initiated online and dated March 4, 2015, the parties' concur that the Department had knowledge of a change in ownership since at least January 14, 2014.²² Notably absent from this application is any information regarding the changes in ownership that occurred June 10, 2010 and January 2, 2012. The Department relies on information regarding these changes in ownership as identified in the January 30, 2015 letter from NACCAS. Since SSI is the sole source of information regarding the ownership of SSI that is reported to NACCAS, the Department, and this Tribunal, SSI alone, is responsible for the veracity of the information. With that responsibility, if SSI fails to provide evidence relevant to applications or forms it submitted to NACCAS, which were then memorialized by NACCAS and submitted as evidence by the Respondent, then this Tribunal and the parties to this matter are bound by the evidence in this record.²³

15. On April 6, 2015, the Secretary reinstated SSI's eligibility and provisionally approved SSI's participation in Title IV, HEA programs. This approval followed review of the only application SSI filed with the Department reporting a change in ownership that resulted in a change in control of SSI.
16. A review of SSI's administration of the programs authorized pursuant to Title IV of the Higher Education Act of 1965, as amended, was conducted by the Department from May 19 to 20, 2016.
17. A Program Review Report was issued on June 17, 2016 that addressed SSI's eligibility to participate in Title IV programs through April 5, 2015. Thereafter, SSI submitted two responses to the Program Review Report on August 31, 2016 and February 17, 2017
18. On January 25, 2018, the Department issued a FPRD which evaluated a full chronology of events beginning May 6, 2010, the date SSI submitted its initial application to participate in the Title IV HEA programs. This chronology of events identified the ownership structure of SSI prior to May 6, 2010 as well as the changes in ownership that occurred on June 10, 2010, January 2, 2012, and March 4, 2013.
19. The FPRD included one finding as it related to SSI's compliance with the statutes and regulations as they pertain to the institution's administration of the Title IV, HEA programs. The finding concluded that SSI lost eligibility to participate in Title IV programs on January 2, 2012 as a result of an unreported change in ownership resulting in a change in control and SSI did not regain eligibility until it was reinstated on April 5,

²² The Department refers to this application as a "Change in Ownership" and the Respondent references this application in its initial brief. A copy of this application was added to the record after the required briefing was done, post-hearing.

²³ For example, SSI fails to explain why it reported to NACCAS that the January 2, 2012 change in ownership was one that resulted in a change in control but, then argues the Department wrongfully determined that the January 2, 2012 change in ownership resulted in a change in control of SSI, the eligible institution.

2015. The Department assessed a liability of \$1,228,774.32 for the disbursements during the period of ineligibility.

20. The change in ownership that occurred on June 10, 2010, was a change in ownership that resulted in a change in control of SSI. Although SSI's initial application for approval as an eligible institution was pending on June 10, 2010, SSI failed to provide any notice of this change in ownership prior to the Secretary's provisional approval for participation in Title IV, HEA programs on July 15, 2010. Although SSI was accredited by NACCAS since at least September 2009, SSI did not report this change in ownership to NACCAS until about October 2014. Although the FPRD correctly concluded the "ownership structure approved by the Department was incorrect from the beginning as SSI did not update the ownership information in its initial eligibility application" FSA erred when it failed to recognize this unreported change in ownership voided the initial PPA.
21. The change in ownership that occurred on January 2, 2012 was a change in ownership that resulted in a change in control of SSI. SSI did not notify the Department nor file a materially complete application with the Department within ten business days of this change. SSI did not report this change in ownership to NACCAS until about October 2014. FSA was correct to find this change in ownership as a change that resulted in change of control of SSI. FSA's assessment of liability for disbursements of Title IV HEA program funds from this date is supported by the fact and law.
22. The change in ownership that occurred on March 4, 2013 was a change in ownership that resulted in a change in control of SSI. SSI did not notify the Department nor file a materially complete application with the Department within ten business days of this change. SSI did not report this change in ownership to NACCAS until about October 2014. FSA's failure to identify this as a change in ownership that resulted in a change in control of SSI is a harmless error, as the liability imposed covered disbursements after this date.
23. SSI's failure to report the June 10, 2010 change in ownership, that occurred while its application for participation in Title IV, HEA programs was pending, resulted in the Secretary's approval of SSI as an eligible institution without accurate ownership information. SSI's failure deprived the Secretary of the ability to properly determine administrative capability and financial responsibility of those individuals and business entities who exercise substantial control of SSI.
24. SSI's acknowledgment that the Department was unaware of any of the changes in ownership that occurred after May 6, 2010 is an admission that SSI secured its initial provisional approval as an eligible institution based on an application that misrepresented the ownership interests in SSI.
25. SSI's acknowledgment that the Department was unaware of any of the changes in ownership at the time the changes occurred or within ten business days of when the change was made, is an admission that SSI denied the Secretary the opportunity to notify SSI that the change in ownership effected SSI's eligibility and the effective date of that

change.

26. Having failed to timely notify the Department of the June 10, 2010, January 2, 2012, and March 4, 2013 changes in ownership, SSI is liable for any Title IV, HEA program funds distributed after there was a change in ownership that resulted in a change in control of SSI.
27. FSA erred in its determination that the change in ownership that occurred on June 10, 2010 did not result in a change in control. This determination is contrary to the applicable statute, applicable Department regulations, and the clearly stated policy of the Department.
28. SSI is liable for the return of any disbursements of Title IV, HEA program funds made by SSI after it was awarded provisional approval as an eligible institution on July 15, 2010 and before its eligibility was reinstated on April 6, 2016.

VI. Conclusion and Order

On the basis of the foregoing findings of fact and conclusions of law, it is **HEREBY ORDERED** that Salon & Spa Institute, pay to the U.S. Department of Education, in a manner as required by law, Title IV, HEA program funds disbursed between July 15, 2010 and April 5, 2015. This amount includes the liability of \$1,228,774.32, disbursed by SSI from January 2, 2012 until April 5, 2015, as established in the Final Program Review Determination, dated January 25, 2018 as well as an additional liability, to be determined by FSA and equal to the amount of Title IV, HEA programs funds disbursed by SSI from July 15, 2010 to January 1, 2012.

Dated: April 27, 2020

Angela J. Miranda
Administrative Law Judge

SERVICE

Service completed by Office of Hearings and Appeals Electronic Filing System (OES) automatic email notice** sent to the email of record for the following registered e-filers:

Anthony Troiani
1927 Norfolk St.
Houston, TX 77098
anthony@troianilaw.com

Alexandra Sweeney
Office of the General Counsel
U.S. Department of Education
400 Maryland Avenue, S.W.
Washington, DC 20202
Alexandra.Sweeney@ed.gov

**Service and receipt thereof will be the date indicated in the confirmation of receipt email for E-filing consistent with 34 C.F.R. § 668.122. Hard copies will NOT follow.

Courtesy copy to:

Lauren Pope
Administrative Actions and Appeals Service Group
Federal Student Aid
U.S. Department of Education
830 First St., N.E.
Washington, DC 20002-8019
By email to: Lauren.Pope@ed.gov