



**U.S. Department of Education
Office of Inspector General**

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December 23, 2002

MEMORANDUM

TO: Theresa S. Shaw
Chief Operating Officer
Federal Student Aid

FROM: Gloria Pilotti 
Regional Inspector General for Audit, Region IX

SUBJECT: FINAL AUDIT REPORT
United Education Institute's Administration of Student Financial Assistance Programs
Control No. ED-OIG/A09-B0025

Attached is our subject report presenting our findings and recommendations resulting from our audit of United Education Institute.

In accordance with the Department's Audit Resolution Directive, you have been designated as the action official responsible for the resolution of the findings and recommendations in this report.

If you have any questions, please contact me at (916) 930-2399.

Please refer to the above control number in all correspondence relating to this report.

Attachment



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December 23, 2002

ED-OIG/A09-B0025

Mr. William P. Murtagh, Jr.
President
International Education Corporation
2201 Dupont Drive, Suite 800
Irvine, California 92612

Dear Mr. Murtagh:

This is the Office of Inspector General's **Final Audit Report**, entitled *United Education Institute's Management of Student Financial Assistance Programs*. The purpose of the audit was to determine whether United Education Institute (UEI) met eligibility requirements and administered the Title IV programs in compliance with the Higher Education Act of 1965, as amended (HEA).

AUDIT RESULTS

UEI continued to return unearned Title IV funds late for students who withdrew from school. We concluded that UEI had generally complied with the HEA and Federal regulations in the areas of student eligibility, ability-to-benefit testing, award and disbursement of Title IV funds, and calculation of the return of Title IV amounts. We also concluded that UEI met program eligibility and institutional eligibility requirements.

In its comments to the report, UEI disagreed with the Office of Inspector General's (OIG) use of the date check cleared the institution's bank for evaluating the timeliness of UEI's return of Title IV funds and the recommended corrective action. UEI also provided comments on a draft finding related to compliance with the 90/10 Rule. After further evaluation, we removed the finding and reported our concerns regarding the 90/10 Rule in the OTHER MATTERS section of the report. UEI's comments and our response concerning the late return of Title IV funds are summarized in the report. The text of UEI's comments is included as an attachment to the report.

FINDING — UEI Continued to Return Unearned Title IV Funds Late For Students Who Withdrew From School

UEI's Independent Public Accountants (IPA) disclosed in its annual audit reports for fiscal years ended October 31, 1999 and 2000, that UEI had not returned unearned Title IV funds timely for

withdrawn students.¹ We found that UEI continued to return unearned Title IV funds late. Pursuant to 34 C.F.R. § 668.22(j)(1), an institution has 30 days from the date the institution determines that a student withdrew to return all unearned Title IV funds for which it is responsible.

In its corrective action plan for the audit report covering its fiscal year ended October 31, 2000, UEI explained actions taken to address findings on the late return of funds:

UEI has struggled with this very important issue. Corrective actions undertaken in the past have had disappointing results. Consequently, executive management has made a decision to review the entire refund process, including the “Return of Title IV funds” issue, from beginning to end. The objective of this action is to implement a process that will ensure that refunds are consistently made in a timely manner. This review process began March 2001 and computer-programming modifications have been identified. Upon completion of the final testing of the computer programming revisions, the new process will be implemented.

Officials of International Education Corporation (IEC), UEI’s parent corporation, informed us that, effective July 1, 2001, new procedures were implemented for processing the return of Title IV funds for students who had withdrawn. Under the new procedures, each UEI campus is responsible for calculating the amount of Title IV funds to be returned. The calculation is forwarded to IEC for verification. Then, IEC issues a check to return the Title IV funds to the program account or lender. Previously, Global Financial Aid Service, a third-party servicer, performed the return of funds calculations and sent the result to IEC for issuance of the refund checks.

To evaluate the effectiveness of UEI’s new procedures, we obtained a list of the 262 students who withdrew from school during the period July 1 to September 30, 2001, and were due a refund. We found that refunds for 94 of the 262 students were not paid within the 30-day time frame. The late refunds were paid an average of 12 days late and ranged from 1 to 100 days late.

Recommendations

We recommend that the Chief Operating Officer for Federal Student Aid—

- 1.1 Require UEI to take additional actions to improve its procedures for ensuring that unearned Title IV funds are returned timely.
- 1.2 Impose a fine, limit participation, or take other appropriate action as provided under 34 C.F.R. § 668, Subpart G.

¹ In the fiscal year 1999 audit, the IPA reported that Title IV funds were returned late for 2 of the 25 students in the refund sample. The IPA reviewed two samples in the fiscal year 2000 audit. The IPA reported that UEI returned Title IV funds late for 5 of the 50 students in the initial sample. In the second sample, Title IV funds were returned late for 13 of the 59 students sampled.

UEI's Comments

UEI disagreed with the finding and recommendations. In its response to the draft report, UEI took exception to the OIG's use of the date a check cleared the institution's bank to evaluate UEI's compliance with 34 C.F.R. § 668.22(j)(1). The regulation states—

An institution must **return** the amount of title IV funds for which it is responsible... as soon as possible but **no later than 30 days** after the date the institution's determination that the student withdrew.... [Bold emphasis added]

UEI stated that the HEA and regulations do not define the term "return" or specify how to determine when 30 days has elapsed. UEI stated that the only guidance issued by the U.S. Department of Education (Department) on the timeliness of returns is the cited regulation, which merely requires that funds be returned within 30 days. UEI acknowledged that the OIG provided a definition in its audit guide for *Audits of Federal Student Financial Assistance Programs at Participating Institutions and Institution Servicers*, dated January 2000, but maintained that the definition was never adopted by the Department and did not have the force of law.

UEI noted that the Department's regulation at 34 C.F.R. § 668.166(c)(2) defined "return," but UEI stated that the definition only applied to determining whether an institution has maintained excess cash. The regulation states—

For the purpose of this section, upon a finding that an institution has maintained excess cash, the Secretary—

(i) Considers the institution to have issued a check on the date that the check cleared the institution's bank account, unless the institution demonstrates to the satisfaction of the Secretary that it issued the check shortly after the institution wrote the check....

UEI concluded "...if the Secretary had intended to define the term 'return' for purposes of the R2T4 [return of Title IV funds] Rule to mean the date on which a check clears an institution's bank, the Secretary could have done so, as he effectively did in the Cash Management regulations. Instead, the Secretary did not proffer such a definition in Section 668.22(j) and the Secretary pointedly limited the definition in Section 668.166(c)(2) exclusively to that regulation. This action makes clear that under Section 668.22(j), the Secretary does *not* require an institution's repayment checks to have been cleared by its bank for such checks to be considered returned."

UEI also stated that applying the 30-day timeframe to the date check cleared the institution's bank presumes an institution can be held responsible for the time required by the bank to process and clear a check, as well as the time for the mail service to deliver the check. UEI cited the Department recently issued Notice of Proposed Rule Making (NPRM) (67 Fed. Reg. 51717, 51739, issued August 8, 2002), which considers the return of Title IV funds by check to be late if (1) the check is issued more than 30 days after the date the student withdrew or (2) the cancelled check shows that the check was received more than 45 days after the date the student withdrew. UEI acknowledged that the proposed regulations did not establish criteria for the period covered

by the finding, but stated that the proposed regulations confirm that the regulations do not currently use a check-cleared date to measure timeliness of payments.

UEI stated that the date the OIG used in its analysis was the date shown on UEI's bank statements rather than the bank cancellation stamp on the back of the checks. According to UEI, the date shown on the bank statement is normally several days after the date the bank stamped the check. UEI also stated that the OIG included in its review seven students who had earned 100 percent of the Title IV funds disbursed to them, and thus, the refunds were not subject to the 30-day requirement.

Using the date the check was prepared,² UEI determined that it returned Title IV funds on time for 250 of the 262 students (95.4 percent). UEI stated that an error rate of less than five percent did not warrant the additional oversight measures or adverse action recommended by the OIG.

OIG Response

While UEI is correct that current Federal regulations covering the return of Title IV funds applicable to our audit period did not define the term "return," we take exception to UEI's use of the date the check was prepared to assess its compliance with the 30-day requirement. The term "return" means more than placing a date on a check. The check date provides no assurance that the funds were, in fact, returned timely. The check clearance date shown on UEI's bank statements, which was used for the OIG's analysis, provides evidence that the funds were returned by that date. We confirmed with a bank representative that the date shown on the bank statements was the date the check was honored by the bank.

As noted in UEI's comments, the date used by the OIG is consistent with the guidance given to independent public accountants performing audits of institutions that participate in Title IV programs. The 2000 audit guide states "[r]efunds paid by check are considered paid on the date the check is honored by the institution's bank." Since its 1997 publication, the audit guide has consistently instructed auditors to use this definition. Also, as noted in UEI's comments, the audit guide definition is consistent with the definition of "return" used in the cash management regulations. Thus, the OIG appropriately used the date check cleared the institution's bank to evaluate UEI's compliance with 34 C.F.R. § 668.22(j)(1).

We revised the number of students cited in the report to exclude the seven students who had earned 100 percent of the Title IV funds. UEI's comments regarding the fairness of the 30-day timeframe may be relevant during the negotiated rulemaking process, but they are not relevant to an evaluation of the institution's compliance with the cited regulation.

As UEI appropriately concluded, the cited NPRM did not establish criteria for the period covered by our audit. Yet, we found that, even under the new regulations, UEI did not make refunds timely. The Department issued the final regulations related to the NPRM on November 1, 2002. The final regulations at 34 C. F. R. § 668.173 (b) state—

² In Attachment Q of UEI's response to the draft report, UEI shows the date used in its analysis as "Check Sent Date." We confirmed with UEI's Executive Vice President of Student Financial Services that the dates in this column actually represented the date on the check (i.e. the date the check was prepared).

- [A]n institution returns unearned title IV, HEA funds timely if—...
- (4) The institution issues a check no later than 30 days after the date it determines that the student withdrew. However, the Secretary considers that the institution did not satisfy this requirement if—
- (i) The institution's records show that the check was issued more than 30 days after the date the institution determined that the student withdrew; or
 - (ii) The date on the cancelled check shows that the bank used by the Secretary or FFEL [Federal Family Education Loan] lender endorsed that check more than 45 days after the date the institution determined that the student withdrew.

Based on available information,³ we concluded that refunds for 20 of the 262 students did not meet the above requirements. This 7.63 percent error rate exceeds the compliance threshold of 5 percent specified in 34 C. F. R. § 668.173 (c) (i). Given the results of our analyses and the fact that UEI has been cited for late refunds in prior audit reports, our recommendations that UEI take additional corrective action, and that Federal Student Aid take appropriate action as provided under 34 C. F. R. § 668, Subpart G, are warranted.

OTHER MATTERS

Recourse Loans Used in Revenue Percentage Calculation for 90/10 Rule. IEC calculated the revenue percentage for UEI and the corporation's other schools. The calculations included amounts from recourse loan transactions related to private loans that Sallie Mae, Inc. provided to UEI students under the condition that IEC guarantee the loans. Under its agreement with Sallie Mae, Inc., IEC was obligated to maintain a reserve fund equal to 30 percent of the principal balance of all outstanding recourse loans. The reserve fund was held and controlled by Sallie Mae, Inc.

IEC's experience with the recourse loans shows that most students will default and that IEC will be required to make full payment on the loans to Sallie Mae, Inc. The following are other indicators that IEC will be responsible for the recourse loans:

- IEC recognized a liability for losses in excess of the reserve amount held by Sallie Mae, Inc. As of October 31, 2001, IEC reported a liability of \$2,358,524 in its financial statements for future defaults on recourse loans provided to UEI students and students at other IEC schools.
- IEC recognized bad debt expense when recording recourse loan transactions in its accounting system. When UEI received a recourse loan disbursement, it recorded 30 percent of the loan principle as bad debt expense in the school's accounting records. When Sallie Mae, Inc. withdrew funds for defaulted loans from the reserve fund and conveyed the rights to collect on the loans, IEC recorded a bad debt expense in UEI's accounting records for the defaulted amount.

³ We did not have information in our audit working papers on the date lenders endorsed the refund checks. Therefore, for purposes of our analysis, we considered refunds to be timely if the checks were issued within 30 days of the withdrawal date and cleared by UEI's bank within 48 days of the withdrawal date. The 48-day period allowed 3 days for the endorsed check to be received and cleared by the institution's bank.

- IEC has not collected significant amounts from former students on defaulted loans. According to IEC officials, IEC routinely provided defaulted recourse loans to collection agencies and that, in fiscal year ended October 31, 2001 the collection agencies recovered only \$31,920 on defaulted recourse loans.

In our opinion, the above facts demonstrate that the recourse loan disbursements and other recourse loan transactions, in reality, represent financing transactions for which IEC bears the risk of loss similar to institutional loans with recourse. As such, only actual loan payments made by students to Sallie Mae, Inc. or IEC should be included as revenue for 90/10 Rule purposes. While IEC's inclusion of recourse loan receipts, net of amounts returned to Sallie Mae, Inc., in revenue percentage calculations does not appear to be prohibited by the regulations, we are concerned about the manipulation of the recourse loan transactions that occurred at UEI and the potential for future abuse.⁴

Delays in Title IV Receipts. IEC monitored its Title IV and non-Title IV revenues through the year to ensure that UEI and the corporation's other institutions meet the 90/10 Rule. When it appeared that UEI would exceed the 90 percent limit on Title IV receipts, IEC took steps to alter the timing of its cash receipts. We found that UEI stopped drawing funds from its Pell account and stopped receiving Federal Family Education Loan disbursements from lenders during the last months of its fiscal years ended October 31, 2000 and 2001. Also, during the last quarter of its fiscal year ended October 31, 2001, UEI encouraged students to refinance the balance due on their UEI retail installment contracts with loans provided under Sallie Mae Inc.'s Customized Career Training Loan Program.⁵ While these actions do not appear to violate applicable regulations or harm students, they could impact on UEI's ability to meet the 90/10 Rule in future fiscal years.

Financial Responsibility. An institution participating in the Title IV programs must demonstrate to the Department that it is financially responsible. IEC did not satisfy the Department's standards for financial responsibility as of October 31, 1999 and 2000. In response, IEC agreed to provisional certification of the Title IV participation agreements for UEI and its other institutions. IEC also provided the Department with letters of credit totaling \$3.5 million. As of May 2002, the Department continued to hold the letters of credit.

⁴ IEC arranged with Sallie Mae, Inc. to delay the required reserve fund payments to the reserve for August and September 2001 until after October 31, 2001, the end of the fiscal year. The agreement, which Sallie Mae, Inc. signed on September 5, 2001, contained the following statement: "We appreciate your agreement to help us satisfy the U.S. Department of Education regulation generally referred to as the 90/10 rule." As evidenced by this statement, the purpose of the delay was to shift reserve payments between fiscal years for purposes of IEC's 90/10 revenue calculations. Even though this arrangement had no impact on whether UEI met the 90/10 Rule for fiscal year October 31, 2001, we considered the arrangement to be an inappropriate manipulation of non-Title IV revenue.

⁵ Sallie Mae Inc.'s Customized Career Training Loan Programs offered student's payment terms and an interest rate that was lower than terms and interest rate contained in the institution's retail installment contract.

BACKGROUND

UEI is a proprietary institution with a main campus in Los Angeles, California, and six additional locations in San Bernardino, Huntington Park, San Diego, Ontario, Van Nuys and Chula Vista, California. Its corporate office, IEC, is located in Irvine, California. UEI received initial approval to participate in the Title IV, Student Financial Assistance programs on April 18, 1988. The Accrediting Council for Continuing Education and Training accredits the institution. UEI offers vocational training programs in the computer, medical, dental, and business fields.

UEI records show that the institution received over \$24 million of Title IV funds during the period November 1, 1999, to October 31, 2000. The 1999 Cohort Default Rate (most recent Department's published rate) for UEI was 5.5 percent.

On September 6, 2001 the OIG issued its Final Audit Report (ED-OIG/A06-B0014) on its audit of UEI's compliance with the Title IV, Student Financial Assistance, verification requirements. The auditors found that UEI reported incorrect verification results for 31 of 50 sampled Federal Pell Grant recipients. The OIG recommended that the Chief Operating Officer for Federal Student Aid confirm that UEI is reporting correct verification results to the Department.

AUDIT OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our audit was to determine if UEI met eligibility requirements and administered the Title IV program in compliance with the HEA. As described later in this section, our review covered varying periods depending on the area reviewed.

To accomplish our objectives, we obtained background information about the institution. We also reviewed applicable HEA provisions and Title IV regulations. We interviewed IEC and UEI administrators and staff and reviewed UEI's policies and procedures, accreditation document, licensure, and Title IV program participation agreement. We reviewed the *Compliance Attestation Examination of the Title IV Student Financial Assistance Programs* for its fiscal year ended October 31, 2000, prepared by UEI's independent public accountant. We also reviewed IEC's Consolidated Financial Statements as of October 31, 2000 and 1999.

Our review of the revenue percentage calculation for the 90/10 Rule covered UEI's fiscal years ended October 31, 2000 and 2001. As part of our review of the calculations, we reviewed files for 30 randomly selected students who received Sallie Mae loans to confirm that eligible students were provided the opportunity to obtain funds under the Title IV programs. The students were selected based on Sallie Mae loan dates and amounts.

To evaluate UEI's newly implemented procedures for the return of funds, we analyzed data for 262 students who had withdrawn from UEI during the period July 1 to September 30, 2001, and were due a refund. To evaluate UEI's other policies and procedures, we reviewed files for 50 randomly selected students from the universe of 3,903 students who started classes between July 1, 2000, and July 31, 2001 and received Title IV disbursements.

We relied on computer-processed data obtained from the institution's CLASS system for our review of the revenue percentage calculation for the 90/10 Rule, student eligibility, Title IV disbursements, and the return of Title IV funds. Our tests were limited to comparing the data to information in student files and tracing summary amounts by transaction codes to the worksheet used by IEC in its monthly tracking of the revenue percentage. We compared Title IV fund totals from the Department's National Student Loan Data System to information extracted by UEI from its CLASS System database. Based on these tests, we concluded that the data used were sufficiently reliable for meeting our objective.

We performed our fieldwork at IEC and UEI offices from August 2001 through January 2002. We held an exit conference with UEI officials on July 3, 2002. Our audit was performed in accordance with generally accepted government auditing standards appropriate to the scope of the review described above.

STATEMENT ON MANAGEMENT CONTROLS

As part of our review, we assessed UEI's management controls, policies, procedures, and practices applicable to the scope of the audit. We assessed the level of control risk for determining the nature, extent, and timing of our substantive tests. For the purposes of this report, we assessed and classified the significant controls related to the Title IV program as follows:

- Oversight of program eligibility
- Monitoring of institutional eligibility and financial responsibility requirements
- Student eligibility determinations
- Ability-to-benefit testing procedures
- Award and disbursement of Title IV funds
- Refunds/returns of Title IV funds

Because of inherent limitations, a study and evaluation made for the limited purposes described above would not necessarily disclose all material weaknesses in management controls. However, our assessment disclosed weaknesses related to the return of Title IV funds for students who withdrew. This weakness is discussed in the AUDIT RESULTS section of this report.

ADMINISTRATIVE MATTERS

Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report represent the opinions of the Office of Inspector General. Determination of corrective action to be taken will be made by the appropriate Department of Education officials.

If you have any additional comments or information that you believe may have a bearing on the resolution of this audit, you should send them directly to the following ED official, who will consider them before taking final action on the audit:

Ms. Theresa S. Shaw
Chief Operating Officer
Federal Student Aid
Union Center Plaza Building, Room 112G1
830 1st Street, NE
Washington, D.C. 20202-5402

Office of Management and Budget Circular A-50 directs Federal agencies to expedite the resolution of audits by initiating timely action on the findings and recommendations contained therein. Therefore, receipt of your comments within 30 days would be greatly appreciated.

In accordance with the Freedom of Information Act (5 U.S.C. § 552), reports issued by the Office of Inspector General are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions under the Act.

If you have any questions, please call me at (916) 930-2399. Please refer to the control number in all correspondence related to this report.

Sincerely,



Gloria Pilotti
Regional Inspector General
for Audit

cc: w/attachment

Mr. Ralph E. Acaba
IEC - Vice President of Student Financial Services

ATTACHMENT

UEI's Comments to the Report

The draft report provided to UEI for comment included a finding concerning compliance with the 90/10 Rule, which was revised and moved to the OTHER MATTERS section of the final report. Comments related to this finding and information subject to protection under the Privacy Act of 1974 have been omitted from this attachment. Also, we have not included the numerous attachments provided with the letter. The complete letter and its attachments are available upon request.

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September 5, 2002

Via FedEx

Ms. Gloria L. Pilotti
Regional Inspector General for Audit-Region IX
U.S. Department of Education
Office of Inspector General
501 I Street, Suite 9-200
Sacramento, CA 95814

Attn: Beverly A. Dalman

Re: United Education Institute
ACN: ED-OIG/A09-B0025

Dear Ms. Pilotti:

On behalf of United Education Institute ("UEI" or the "School"), we hereby respond to the Office of Inspector General's ("OIG") Draft Audit Report dated August 6, 2002, concerning UEI's compliance with the eligibility and administrative requirements applicable to the federal student financial assistance programs under Title IV of the Higher Education Act of 1965, as amended ("Title IV Programs") ("HEA"), Audit Control No. ED-OIG/A09-B0025 ("Draft Report"). This response is timely filed, within 30 days of such report.

We submit that there is no legal basis for Finding No. 1 of the Draft Report alleging UEI's failure to meet the requirements of the so-called "90/10 Rule" for fiscal year 2000. Furthermore, Finding No. 2 alleging late return of Title IV Program funds is not based on applicable regulations and does not accurately assess UEI's compliance with the return of funds requirements. Accordingly, both Findings should be withdrawn from the Final Report and the audit closed with no further action required on the part of the School.

OIG Note:

Comments contained on pages 1 through 17 addressing finding No. 1 of the draft report were omitted since, in the final report, we made no recommendation for corrective action by Federal Student Aid related to the 90/10 Rule.

FINDING NO. 2: UEI CONTINUED TO RETURN THE UNEARNED TITLE IV FUNDS LATE FOR STUDENTS WHO WITHDREW FROM SCHOOL

The Draft Report asserts that the School made late payments under the Return to Title IV Funds ("R2T4") Rule codified at 34 CFR 668.22 for 101 of 269 students who withdrew in the period from July 1, 2001 through September 30, 2001. We note that the Draft Report does not raise any questions about the accuracy of the School's R2T4 calculation and does not propose any repayment liability for this finding.

UEI strongly disagrees with this Finding because, for the transactions reviewed by the OIG, the School in fact issued more than 95% of its repayment checks within 30 days as required by the applicable regulation. Such issuance within 30 days is all that is required of UEI under federal law. The OIG, in contrast, is seeking to impose a standard that repayments must clear an institution's bank account within 30 days in order to be considered returned in a timely manner. This standard is in no way required by federal statute or regulation, nor has the Department issued any guidance to that effect. Consequently, the OIG is without authority to impose such a standard on UEI.

LEGAL STANDARDS

Section 484B of the HEA requires that when a student who receives Title IV program funds withdraws, the institution must return the appropriate amount of Title IV aid disbursed to that student, as calculated according to the legal formula. While the statute does not set out any specific standard for timeliness of repayments, it provides in pertinent part:

(a) RETURN OF TITLE IV FUNDS.—(1) IN GENERAL.—If a recipient of assistance under this title withdraws from an institution during a payment period or period of enrollment in which the recipient began attendance, the amount of grant or loan assistance (other than assistance received under part C) to be returned to the title IV programs is calculated according to paragraph (3) and returned in accordance with subsection (b).

(20 USC 1091b).

The applicable regulation, codified at 34 CFR 668.22(j)(1), sets forth the time frame for returning Title IV funds as follows:

An institution must return the amount of title IV funds for which it is responsible under paragraph (g) of this section as soon as possible but no later than 30 days after the date of the institution's determination that the student withdrew [...]

The regulation does not define the term "return," and no discussion of the meaning of that term appeared in either the preamble to the final regulations governing the R2T4 process (64 Fed. Reg. 59038, Nov. 1, 1999) or the Notice of Proposed Rulemaking ("NPRM") (64 Fed. Reg. 43024, 43036, Aug. 6, 1999). Moreover, the Department has not provided any clarification in the Student Financial Aid Handbook or other sources of guidance to institutions, such as the expansive Dear Colleague Letter issued by the Department in December 2000, to explain the workings of the R2T4 regulation (GEN-00-24). Therefore, the only "guidance" issued by the Department on the timeliness of returns is the aforementioned regulation, 34 CFR 668.22(j), which merely states without elaboration that funds must be returned within 30 days.

FACTUAL BACKGROUND

1. The OIG examined a list of 269 students who withdrew from UEI during the period of July 1 to September 30, 2001 for timeliness of return. Under the OIG's standard, the Draft Report asserts that returns "were not paid within the 30-day time frame" for 101 of those students. (See Draft Audit Report page 7).
2. Although the Draft Report does not explain the standard the OIG used to determine whether these returns were made in the required time frame, the OIG purportedly used the date on which the check cleared the institution's bank account.
3. While the Draft Report does not explain the OIG's methodology, it appears that the OIG did not actually use the check-cleared date as signified by the bank cancellation stamp on the back of the check, but rather used the date the check was posted according to the School's bank statement.
4. Based on the School's preliminary review to date, it appears the OIG included 7 students in the review who had earned 100% of the Title IV aid disbursed to them so there was no R2T4 payment to be made, and therefore the actual universe of students appropriate for review would be 262. (See R2T4 calculation sheets at Attachment P).
5. Based on the legal standard cited above, *i.e.*, 30 days for the institution to issue the return check, the School returned Title IV funds on time for 250 of the 262 students for a 95.4% compliance rate. (See spreadsheet at Attachment Q).

DISCUSSION

Based on the actual legal requirement that governs this process, UEI has determined that R2T4 payments were timely for 250 of the students reviewed, for a compliance rate of more than 95%. An error rate of less than 5% does not warrant a "late refund" letter of credit under 34 CFR 668.173(b), and it certainly does not warrant any additional oversight measures or adverse action as proposed in this Finding. We ask that this Finding be withdrawn in its entirety.⁵

I. Federal Regulations Do Not Require That R2T4 Checks Clear The Bank Within 30 Days, And An Institution Cannot Control The Timing Of The Bank's Clearance Process

Neither the statute nor the applicable regulation authorize the OIG to measure whether an institution paid R2T4 refunds within the 30-day time frame by referring to the date the checks clear the institution's bank. As noted above, the statute and regulation are silent on the issue of how to determine when 30 days has elapsed, and the Department has not clarified this issue in any sources of guidance to institutions. The Dear Colleague Letter (GEN-00-24) does not state or even suggest that funds are not considered to have been returned until they have cleared the institution's bank account.

Therefore, the only "guidance" issued by the Department on the timeliness of returns is the aforementioned regulation, 34 CFR 668.22(j), which merely requires that funds be returned within 30 days. This regulation does not dictate the point in the process at which funds are considered to have been returned, such as the date the check is issued, the date the check is mailed, the date the check is received by the institution's bank, or the date the check is cleared by such bank. While the OIG has set forth such a standard in its Audit Guide (page II-28 of the 2000 Audit Guide), that standard has never been adopted by the Department and does not have the force of law. The OIG has no authority to unilaterally define the term "return" such that return payments are considered to have been made only on the date the check clears the bank and appears on the institution's bank statement. Only the Secretary can establish such a requirement, and the Secretary has not done so.

⁵ We also note that the School has been significantly handicapped in responding to this Finding since the Draft Report does not provide a listing of R2T4 payments that the OIG deems to be late. The School has had to do its best to determine which students are on the OIG's list for that purpose. Furthermore, based on discussions with the auditors, it appears they did not even use the check-cleared date as shown by the bank's cancellation stamp on the back of the check, but rather used the cleared date as listed on the School's monthly bank statement. The date that a check is listed on the bank statement is normally several days or more after the date the bank stamped the check, so the OIG's standard is not only wrong, but its method to measure compliance with that improper standard is significantly inaccurate.

The OIG's interpretation of the standard presumes an institution can be held responsible for the time required by the bank to process and clear a check (as well as the time for the mail service to deliver the check). That position is untenable and fundamentally unfair since an institution cannot be held responsible for the activities of third parties, such as banks, that it cannot control. Indeed, we would note that different banks have different check clearance procedures, which may vary in time and which are not necessarily efficient.

An institution can control when it issues a check, but it has no control over when a bank honors that check, and the institution cannot be held accountable for the timing of the bank's actions (or inactions). Given the limited 30-day time period in which institutions must calculate, process and "return" R2T4 payments, the Department cannot and has not defined the "return" date based on action other than those actions within the institution's control, *i.e.*, the date on which the check is issued.

A. The Department Uses A Check-Cleared Standard For One Purpose Under The Cash Management Regulations But Not Under The R2T4 Regulations

It is telling that in a different regulation, 34 CFR 668.166(c)(2), the Secretary specified that a payment is considered to have been returned when an issued check clears the institution's bank account, and the Secretary made clear that this check-clearing standard applies *only* to that section of the Department's regulations. Specifically, the Cash Management regulation at Section 668.166(c)(2), which solely addresses consequences for maintaining excess cash balances, specifies:

For the purposes of this section, upon a finding that an institution has maintained excess cash, the Secretary—

- (i) Considers the institution to have issued a check on the date that the check cleared the institution's bank account, unless the institution demonstrates to the satisfaction of the Secretary that it issued the check shortly after the institution wrote the check;

(Emphasis added.) Clearly, if the Secretary intended to define the term "return" for purposes of the R2T4 Rule to mean the date on which a check clears an institution's bank, the Secretary could have done so, as he effectively did in the Cash Management regulations. Instead, the Secretary did not proffer such a definition in Section 668.22(j), and the Secretary pointedly limited the definition in Section 668.166(c)(2) exclusively to that regulation. This action makes clear that under Section 668.22(j), the Secretary does *not* require an institution's repayment checks to have been cleared by its bank for such checks to be considered returned. As the Secretary has not promulgated such a requirement for purposes of the R2T4 Rule, the OIG cannot unilaterally impose one in an audit report.

B. The Secretary Has Issued A Proposed Rule Adopting A Check-Cleared Standard For R2T4 Purposes For The Future, But No Such Regulation Currently Exists In Law

The Secretary recently issued an NPRM that would *for the first time and for the future* specify what the term “return” means regarding R2T4 checks, and this standard is not the harsh standard that the OIG is seeking to enforce here. Specifically, the proposed regulation, 34 CFR 668.173(b), which would take effect in the future, would clarify that R2T4 funds returned via check are considered returned in a timely manner if they are *issued by the institution within 30 days* of the date of the institution’s determination that the students withdrew and, as evidence of such “return,” clear the bank within 45 days. Proposed Section 668.173(b) specifically states:

(b) *Timely return of title IV, HEA program funds.* In accordance with procedures established by the Secretary or FFEL Program lender, an institution returns unearned title IV, HEA funds timely if—

(1) The institution deposits or transfers the funds into the bank account it maintains under § 668.163 no later than 30 days after the date it determines the student withdrew;

(2) The institution initiates an electronic funds transfer (EFT) no later than 30 days after the date it determines that the student withdrew;

(3) The institution initiates an electronic transaction, no later than 30 days after the date it determines that the student withdrew, that informs an FFEL lender to adjust the borrower’s loan account for the amount returned; or

(4) The institution issues a check no later than 30 days after the date it determines the student withdrew. However, the Secretary considers the institution did not satisfy this requirement if—

(i) The institution’s records show that the check was issued more than 30 days after the date the institution determined that the student withdrew; or

(ii) The date on the cancelled check show that the Secretary or FFEL Program lender received that check more than 45 days after the date the institution determined that the student withdrew.

67 Fed. Reg. 51717, 51739 (Aug. 8, 2002) (emphasis added). (See Attachment R).

In the negotiated rulemaking leading to this proposed rule, the negotiators expressed concern about the “ambiguity” in measuring timely return of Title IV funds by check since (as discussed above) the Audit Guide uses a check-cleared standard but the regulation does not. (See preamble to the NPRM, 67 Fed. Reg. at 51730). The Secretary recognized the validity of the negotiators’ position that “it was unfair to hold an institution responsible for a check

clearance process that is beyond its control.” Accordingly, the Secretary proposed a rule expressly confirming that Title IV funds are considered returned on time if the institution “*issues a check*” within 30 days and, as evidence of such issuance, the check clears the bank in 45 days. The NPRM, for the first time and for the future, is expected to incorporate a check-cleared date into the regulation, but it will provide a 45-day time frame for the check clearance process, not the 30-day deadline that the OIG is seeking to enforce here.

While the NPRM does not govern the finding in the Draft Report, it serves to confirm that the regulations do not currently use a check-cleared date to measure timeliness of payment for purposes of the R2T4 rule, not to mention a 30-days check-cleared date. Simply put, there would be no need for the Department to add a check-cleared standard to the regulation now if such a standard were already in force. As such, the Secretary’s action in proposing this new regulation makes plain that the Department currently does not require R2T4 checks to be cleared by the bank within 30 days to be considered returned in a timely manner, contrary to the OIG’s position.

II. The School Made Timely Returns In 95.4% Of All Cases Under Existing Law

The correct legal standard is highly relevant to this Finding because the School has determined that it issued checks within 30 days for 250 of the students cited in the Draft Report. (See spreadsheet at Attachment Q). As further discussed in Section III below, the School also has determined that at least seven students who withdrew and who were included in OIG’s calculation were not even eligible for any R2T4 payment. Consequently, no R2T4 returns were due for these students and, accordingly, no such returns can be considered late. Therefore, the School made timely payments to 250 of the 262 students who actually qualified for a R2T4 payment, for timely performance in 95.4% of all cases.⁶ Based on this performance, there is no rationale for any penalty, and this Finding should be withdrawn in its entirety.

III. The Draft Report Erroneously Labeled Seven Other Refunds As Return to Title IV Payments

The Draft Report erroneously included tuition-related refunds that the School made to the Department in connection with seven withdrawn students within the universe of R2T4 payments. Under 34 CFR 668.22(e), an institution is required to make a R2T4 payment only if a student withdrew up to the 60% point of the payment period or period of enrollment. After the 60% point, no R2T4 payment is required. However, an institution may still be required to make a non-R2T4, *tuition-related* refund to the Department in certain circumstances or under state law,

⁶ It is notable that the additional 15 days that the proposed Section 668.173(b) provides for a check to clear the bank correlates with the OIG’s own finding in the Draft Report (page 7) that the returned funds that the OIG deemed to be late under its check-cleared standard were late by an average of 12 days, well within the 15-day period that the proposed rule would allow for a check to clear the bank.

as was the case here. Specifically, upon a student's withdrawal, an institution recalculates what tuition the student owes or has overpaid according to its own tuition-refund policy. If the student overpays, California requires that the institution pay the overpaid tuition to the Department. However, such payments are not R2T4 refunds.

Indeed, in the preamble to the final R2T4 Rule, the Secretary clearly distinguished between R2T4 returns and other payments resulting from a school's refund policy:

The School's refund policy will govern what charges a student may owe after withdrawing, but that policy will not affect the amount of aid the student has earned under the return calculation. An institution's refund policy is also not taken into consideration for establishing the repayment obligations of the School and the student.

64 Fed. Reg. 59015, 59033 (Nov. 1, 1999).

UEI made payments to the Department based on state law requirements for seven of the students cited in the Draft Report, even though all seven completed more than 60% of the payment period and therefore earned 100% of the Title IV funds that were disbursed or could have been disbursed, as shown on the following chart, and supported by the R2T4 calculation sheets at Attachment P.⁷

	<u>STUDENT</u>	<u>SOC. SEC. #</u>	<u>PAYMENT PERIOD – % ATTENDED</u>	<u>PAYMENT PERIOD – % AID EARNED</u>
1	OIG Note: Student names and social security numbers contained in this table have been redacted to comply with the Privacy Act of 1974		91.1%	100.0%
2			81.5%	100.0%
3			100.0%	100.0%
4			74.3%	100.0%
5			77.0%	100.0%
6			82.3%	100.0%
7			77.0%	100.0%

As these transactions had nothing to do with R2T4, they cannot be considered late R2T4 returns in this Finding, and they should be eliminated from the Final Report. Accordingly, there

⁷ The School has only been able to conduct a preliminary review of this issue at this point in time. The School is still checking whether more than 7 of the students included in the OIG's calculation were not eligible for a R2T4 payment. However, due to time limitations and the difficulty of responding to a Draft Report that does not specify precisely which returns OIG determined were late, UEI has not had an opportunity to complete its analysis of this issue.

were 262 students in the universe under review and, using the actual legal standard, the School made timely payments for 250, for a 95.4% compliance rate.

CONCLUSION

Based upon the OIG's erroneous finding that UEI had returned nearly 38% of its R2T4 checks late, the Draft Audit Report concludes this finding with two recommendations: (1) That UEI take additional actions to improve its procedures for ensuring unearned Title IV funds are returned in a timely manner, and (2) that Federal Student Aid impose a fine, limit participation in the Title IV programs, or take other action against UEI under 34 CFR 668, Subpart G.

Both of these recommendations should be removed from the OIG's Final Report because the entire Finding is based on a standard for timeliness that the Department has never promulgated or endorsed. Even the NPRM, which adopts a check-cleared standard for the future, proposes a 45-day standard. As demonstrated above, UEI in fact returned more than 95% of the R2T4 checks at issue in a timely manner, *i.e.*, within 30 days. This high percentage satisfies the compliance threshold for determining whether an institution must post a letter of credit under 34 CFR 668.173, and therefore no fine, limitation or other adverse action is appropriate.

With regard to corrective measures, the School's compliance rate demonstrates that the measures UEI has implemented in the last two years to ensure it returns R2T4 checks in a timely manner have been successful and there is no reason for the Department to require additional measures. We briefly recount those measures here:

- Rather than have its third-party servicer manage the R2T4 calculations and payments, beginning in July 2001 UEI has handled those functions internally to assume total control over the process.
- Also in the spring of 2001, after reviewing the Departmental worksheets and software available on the market, UEI created its own worksheet format to accurately calculate the Title IV funds earned by students and the unearned portion to be returned. This worksheet has proven to be quite workable in enabling UEI to comply with the R2T4 requirements.
- Throughout this period, the School has hired additional staff for R2T4 purposes, conducted additional staff training, and developed additional procedures and tools to monitor and manage the R2T4 process.
- In May 2002, the School implemented a procedure to electronically inform an FFEL lender to adjust the borrower's loan account for the amount returned and transfer R2T4 funds to the FFEL lender by electronic funds transfer.

All of these actions have produced positive results, as evidenced by UEI's 95% compliance rate, as measured under the actual legal standard, for the period of the Draft Report. Moreover, the School's most recent Title IV Compliance Attestation Examination, for the stub

period November 1, 2001 to December 31, 2001 performed by its independent auditor, Almich & Associates, did not find *any* late R2T4 payments for that period, even though the auditor used the Audit Guide's standard of measuring returns by check clearance date. (See page 22 of Attachment S).

In July 2002, Almich also prepared an Independent Accountant's Report, at the request of the Accrediting Council for Continuing Education and Training ("ACCET"), the School's accrediting agency, with favorable results. (See Attachment T). The auditors examined records for 261 students who withdrew from four UEI campuses (Los Angeles, Huntington Park, Ontario and Van Nuys) in the first five months of 2002, and found that returns for all but 9 (3.5%) of the students were paid within 30 days of the date the School determined the student withdrew. That represents a compliance rate of 96.5%.

Clearly, based on the two most recent reviews conducted by an independent auditor, the steps that UEI has taken to improve its R2T4 procedures have resulted in a high level of compliance. While UEI continues to strive for 100% compliance, there is no basis for the OIG to recommend that the Department take any adverse action or demand further corrective action.

Thank you for the opportunity to respond to the Draft Report. If you need additional information, please let us know.

Sincerely,



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Enclosures
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