Dear Secretary Cardona:

I write regarding the U.S. Department of Education (Department) process for reviewing, approving, and monitoring for-profit college conversions to non-profit institutions. The U.S. Government Accountability Office (GAO) recently investigated the conversion process and found serious shortcomings in the Department’s monitoring of converted institutions, which gives rise to risks of insiders taking advantage of non-profit institutions at student and taxpayer expense.¹ These issues combined with concerns raised at a Committee hearing this April² demonstrate that the Department and the Internal Revenue Service (IRS) must take steps to reform their processes and halt the approval of all conversions until they finalize those reforms.

GAO’s findings indicate that lapses in Department oversight have allowed billions to flow annually to institutions it treats as non-profits, but which may operate as for-profits.

GAO found that the Department allowed numerous concerning conversion transactions to proceed under its current process. These transactions often consisted of a for-profit college selling its institution, or component parts such as the institution’s brand, to a newly created non-profit. While only a small number of conversions involved insiders (owners or executives controlling both the non-profit purchaser and for-profit seller simultaneously), insider

conversions received more than 75 percent of all federal aid received by converted institutions.\(^3\) GAO found that these institutions perform worse financially than converted institutions that do not involve insiders, putting students and taxpayers at risk, and that existing regulations fail to prevent these institutions from improperly channeling benefits to insiders.\(^4\)

In case studies of insider conversions, GAO identified characteristics of insider conversion deals that differed from non-insider conversion deals, which created these risks of abuse. For instance, in insider conversions, the non-profit always took out loans with the insiders to finance purchases of the for-profit college.\(^5\) In nearly all cases, these loans primarily paid for intangible assets like goodwill, brand names, accreditation, or established student relationships as opposed to tangible assets like buildings, equipment, or other physical capital.\(^6\) By comparison, GAO found that among randomly selected conversions that did not involve insiders, the non-profits primarily purchased tangible assets and assumed no debt whatsoever to finance the transaction.\(^7\)

Moreover, in several conversions, the for-profit college retained some essential assets after the sale, effectively forcing the non-profit college to enter a long-term contract with the legacy for-profit entity.\(^8\) In these cases, the legacy for-profit could essentially exert control over the operations of the non-profit in perpetuity while extracting most of the revenue at the non-profit. Put differently, the non-profit was a shell company passing through profits to the legacy for-profit. GAO found that these issues arose, in part, because the Department had failed to effectively oversee insider transactions and monitor the non-profit entity following the transaction.\(^9\)

**Insider conversions trick students and regulators leading to significant costs.**

On April 20, 2021, the Committee held a hearing entitled, “For-Profit College Conversions: Examining Ways to Improve Accountability and Prevent Fraud” that examined the risks presented in GAO’s report. At this hearing, witness testimony demonstrated that these risks materialize into concrete harms to students and taxpayers. For instance, as part of her testimony, Ms. Yan Cao of The Century Foundation described her analysis of borrower defense claims demonstrating the disproportionate harm these conversions cause students.\(^10\) These borrower defense claims allow students to have their loans forgiven if they can demonstrate that their college engaged in certain forms of misconduct, most commonly fraudulent representation or

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\(^3\) During the 2018-19 award year, all converted institutions received $2.3 billion in federal student aid with $1.8 billion going to insider conversions. GAO-21-89, *Higher Education: IRS and Education Could Better Address Risks Associated with Some For-Profit College Conversions*, 17-18 (Dec. 31, 2020).

\(^4\) *Id.* at 26-31.

\(^5\) *Id.* at 22.

\(^6\) *Id.* at 29.

\(^7\) *Id.* at 29.

\(^8\) *Id.* at 34-35.

\(^9\) *Id.* at 46-49.

misleading advertising. Ms. Cao’s analysis shows that more than 70,000 of the 300,000 Borrower Defense claims submitted to the Department were submitted by students at converted institutions masquerading as non-profit while funneling profits to private owners.11

The cost of these claims are eventually borne by taxpayers. For instance, Dream Center Education Holdings collapsed after initiating a conversion transaction and defrauding students.12 The Department estimates that this single failed conversion led to students taking out $600 million in loans in the years leading up to its collapse. Many of those loans due to the institution’s closure will be forgiven by the Treasury allowing Dream Center investors to potentially walk away without liability and leave taxpayers holding the bag.13

At the April hearing, Republican members of the Committee repeatedly noted that converted schools make up less than 0.1 percent of all for-profit institutions,14 translating to approximately 0.01% of all U.S. institutions of higher education participating in federal student aid.15 But as Ms. Cao’s analysis demonstrates these colleges account for about 25 percent of all student claims of institutional misconduct.16 Simply put, rather than demonstrating that this sector doesn’t merit attention due to its small size, the disproportionate impact this small number of schools is having on students underscores concentrated malfeasance that needs further examination.

The Department has made some progress, but it should halt approvals of all conversions until it implements GAO’s recommendations and coordinates more effectively with IRS.

Recognizing the need to scrutinize these transactions, the Department has taken steps to strengthen its application and oversight process. Specifically, the Department agreed with GAO’s recommendation that it “develop and implement monitoring procedures for staff to review the audited financial statements of all newly converted nonprofit colleges for the risk of improper benefit.”17 And the Department plans to develop these procedures alongside new post-

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13 Id. at 3.
15 According to GAO as of the publication of the Dec. 2020 report, there were 44 converted institutions of higher education and the most recent Title IV volume reports indicate that there are approximately 4274 institutions eligible to receive Direct Loans. U.S. Gov’t Accountability Off., GAO-21-89, Higher Education: IRS and Education Could Better Address Risks Associated with Some For-Profit College Conversions, 17 (Dec. 31, 2020).
16 See Aarthi Swaminathan, Exclusive: Education Department data details struggle for students who feel defrauded, Yahoo! Finance (Apr. 20, 2021).
17 Id. at 49-50.
transaction reporting requirements for newly converted colleges. The Department’s enhanced oversight has led it to deny two conversion transactions in recent years – Grand Canyon University (GCU) and the Center for Excellence in Higher Education (CEHE) – in both cases citing that private individuals or corporations would have been the primary beneficiaries of the alleged non-profit.

Nonetheless additional reforms are necessary. For instance, the IRS recently informed the Committee that it takes no affirmative steps to coordinate with the Department on conversion review. Though the IRS cannot affirmatively provide tax information to the Department, the Department may provide information back to IRS after it approves or denies conversion transactions. This coordination would be a particularly good use of resources, given that the IRS approves non-profit status largely based on representations made by converting entities, whereas the Department reviews actual executed contracts which may substantially differ from those representations. Consequently, ED has not notified IRS that the two entities described above may not be eligible for tax-exempt status, a benefit they enjoy as of the date of this letter. Accordingly, the Committee will be referring these organizations to the IRS for review of their tax-exempt status.

Given GAO’s findings and recommendations, it is clear the Department has substantial work ahead of it to ensure the integrity of the conversion process. For that reason, I recommend the Department take immediate action to protect students and taxpayers by:

1) Halting all decisions on conversion applications while the Department considers GAO’s findings and recommendations.

2) Establishing formal interagency channels to share every conversion decision with the IRS and brief the IRS on its findings whenever the Department denies a conversion of an institution the IRS has approved for tax-exempt status.

Additionally, members of the Committee raised several issues during the April hearing, to which only the Department can provide responses. To ensure the Committee best understands the risks inherent in for-profit conversions, please respond to the requests below. These documents should be provided in accordance with the enclosed document production instructions. If the Department has any questions about how to comply with a document request or the production instructions, please contact Benjamin Sinoff at Benjamin.Sinoff@mail.house.gov.

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18 Id.
20 IRS briefing of Committee staff (Apr. 14, 2021).
21 Id.
22 Id.
1) Federal law requires for-profit colleges to derive no more than 90% of their revenues from Title IV federal student aid (90/10 rule). Does the Department track whether recently converted institutions’ meet this standard?

   a. If so, please provide documents sufficient to show which converted institutions the Department tracks for compliance with the 90/10 rule, the extent and duration of such tracking, and consequences, if any, for violations.

   b. If the Department tracks some but not all converted institutions’ adherence to the 90/10 rule, please explain how the Department determines which institutions it tracks.

   c. To the extent data is available, please provide a list of any converted institutions that derived more than 90% of their revenue from Title IV federal student aid, including the year(s) these institutions did not comply and any consequences the Department imposed on those institutions.

2) On May 24, 2018 Dr. Arthur Keiser presided as chair over a meeting of the National Advisory Committee on Institutional Quality and Integrity (NACIQI) that considered the use of accreditor reviews of approving for-profit to non-profit conversions. At that meeting Dr. Keiser stated, “I have consulted with the NACIQI counsel and determined that my recusal [from this meeting] is unnecessary.”23 Please provide all communications between Dr. Arthur Keiser and NACIQI or Department staff regarding his recusal from the May 24, 2018 meeting, including any decisions or opinions issued by ethics counsel.

3) The Department has received over 70,000 applications for borrower defense relief from students who attended schools like Alterius, Bryant & Stratton, Dream Center schools, Keiser University, Liberty University, Purdue University Global, Stevens-Henager, United Medical Academy, and Wright Career College, all of which present concerns recently described in the GAO report: "Higher Education: IRS and Education Could Better Address Risks Associated with Some For-Profit College Conversions."24 Please identify the number of borrower defense claims associated with each of those schools during the periods before and after ED approved any changes in ownership or changes to nonprofit status;

   a. To the extent that ED has prepared any analysis describing the nature or merit of those claims, please provide copies of those materials; and

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b. Please also provide the same information for any schools not listed above
(including for schools with fewer than 100 claims), that converted from for-profit
to nonprofit status within the past ten years.

4) Please provide unredacted copies of every Department decision on Change of
Ownership (CIO) for Center for Excellence in Higher Education (CEHE) institutions25
as well as documents sufficient to show any updates or changes that the Department has
since issued to schools owned or operated by CEHE. Please also provide all CIO
decisions for institutions listed in the Department's May 27, 2021 report on proprietary
institution conversions.

Please send all official correspondence and information relating to the requests outlines from 1-4
to the Committee's Clerk at Mariah.Mowbray@mail.house.gov.

Sincerely,

ROBERT C. “BOBBY” SCOTT
Chairman

Enclosure: Committee on Education and Labor Production Instructions

Cc: The Honorable Virginia Foxx, Ranking Member

The Honorable Charles P. Rettig, Commissioner, Internal Revenue Service

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25 U.S. Dep’t of Educ. Office of Federal Student Aid, Re: Decision on Change of Ownership for: Stevens Henager
College, OPE 003674, CollegeAmerica Denver, OPE 025943, CollegeAmerica Arizona, OPE 031203, California
decision.pdf.