



UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

Audit Services
New York / Boston Audit Region

August 4, 2010

Control Number
ED-OIG/A02J0001

Steve Bonkowski
President
Everest Institute
1505 Commonwealth Avenue
Brighton, MA 02135

Dear Mr. Bonkowski:

This **final audit report**, entitled *Everest Institute's Lender Agreements*, presents the results of our audit. The purpose of the audit was to determine whether the agreements between the institution and all lenders complied with the anti-inducement provisions of the Higher Education Act of 1965, as amended (HEA). Our review covered the period July 1, 2007, through September 30, 2008.

BACKGROUND

Everest Institute (Everest), located in Brighton, Massachusetts, was known as Bryman when it was acquired by Corinthian Colleges, Inc. (Corinthian) in December 1995. The school's name was changed to Bryman Institute in June 1996 and was changed again in April 2007 to its current name, Everest Institute. Everest offers programs in Dental Assisting, Medical Assisting, and Medical Administrative Assistant. For the 2007-2008 award year, Everest received a total of \$5,455,237 in Federal Family Education Loan Program (FFELP) funds.

Corinthian is a publicly traded corporation based in Santa Ana, California, that operates 89 for-profit colleges in the United States. Corinthian had private loan agreements with three lenders: Student Loan Xpress, Inc. (SLX), Sallie Mae, Inc. (SLM), and College Loan Corporation. These agreements provided private loans to Everest students who still needed financial assistance after exhausting Federal financial aid.

According to Section 435(d)(5)(A) and (C) of the HEA,¹ eligible lenders are prohibited from offering or paying certain inducements in connection with FFELP loans:

¹ All citations to the HEA are to the requirements in effect during our audit period, from July 1, 2007 through September 30, 2008.

The term “eligible lender” does not include any lender that . . .

(A) offered, directly or indirectly, points, premiums, payments, or other inducements, to any educational institution or individual in order to secure applicants for loans under this part; [or]

.

(C) offered, directly or indirectly, loans under this part as an inducement to a prospective borrower to purchase a policy of insurance or other product. . . .

A violation of this prohibition may result in the lender’s disqualification from further program participation and other sanctions.

AUDIT RESULTS

We found that the agreements between Corinthian and two lenders were not in accordance with the HEA. We determined that Corinthian had two agreements with SLX and one agreement with SLM that included inducements prohibited by the HEA.² The two agreements between Corinthian and SLX included prohibited inducements in the form of Web site services by SLX and provisions limiting Everest’s students’ access to private loans based in part on Everest’s FFELP volume and Federal cohort default rate. The SLM agreement offered inducements to parents of Corinthian students to borrow PLUS loans with SLM.

Section 435(d)(5) of the HEA prohibits offering or paying inducements to institutions to secure loan applicants or offering FFELP loans as an inducement for a borrower to purchase another product from a lender. We found that the lenders entering into the agreements did not comply with the HEA’s requirements. We did not identify any noncompliance by Everest with Section 435(d)(5)(A) and (C) of the HEA; however, the lenders offered inducements to the school in the agreements. Since our audit was of the school and the noncompliance we identified was attributable to the lenders, we present the details of the agreements between Corinthian and the two lenders in the Other Matters section of this report.

Scope Limitation

In our Audit Notification Letter, sent to the president of Everest on October 10, 2008, we requested the most recent and prior year’s internal audit reports for Everest since *Government Auditing Standards*, paragraph 7.11(e), states, “[a]uditors should assess audit risk and significance within the context of the audit objectives by gaining an understanding of . . . the results of previous audits and attestation engagements that directly relate to the current audit objectives.” Corinthian responded that the internal audit reports were not applicable to our audit. While interviewing the president of Everest, he informed us that Corinthian’s Internal Audit Department conducts an audit of the campus every year and if we wanted a copy we were to go

² The agreements between Corinthian and the lenders applied to all of Corinthian’s schools, which included Everest.

through the Corinthian/Everest audit liaison. A second request for Everest's internal audit reports was made to Corinthian's audit liaison.

On December 11, 2008, Corinthian's audit liaison informed us, in an email, that:

The candid self-appraisals contained in our internal audits can only be conducted because we understand they aren't going to be disclosed to third parties. If these audits were freely available to third parties, we . . . would be hesitant to conduct robust internal audits for fear that the information contained in those reports could be used to our detriment. And in fact, no government agency has, to our knowledge, ever sought our internal audit reports. For that reason, we prefer to maintain our practice of keeping our internal audit reports confidential within the company.

More to the point, however, our internal audits are not designed to identify "lender inducements," so the Brighton reports would not be helpful in that regard anyway. I have personally reviewed the internal audits for the Brighton campus for the past three years and can confirm to you they contain no findings regarding lender inducements (or even inquiries into that subject matter). If the OIG's [Office of Inspector General] audit is moving beyond lender inducements, we would appreciate the opportunity to discuss the revised scope.

On March 23, 2009, Corinthian and OIG agreed that Everest would produce the "index" of its internal audits in an attempt to demonstrate to OIG's satisfaction that the issue of prohibited inducements was not covered by its internal audits. Corinthian's legal counsel provided, via email, three documents in Portable Document Format (PDF), entitled "Internal Compliance Audit Audit Program – US Schools," which consisted of a table of contents for each section of Everest's internal audit reports for fiscal years 2006, 2007, and 2008. Upon review of the table of contents provided, we requested additional details on selected sections of these reports for review. Our request for selected sections of Everest's internal audit reports was denied.

We determined that the table of contents was insufficient to satisfy our requirement of obtaining an understanding of internal controls within the context of our audit objective. Although the stated subject areas did not indicate that the internal audits specifically examined the issue of prohibited inducements, we could not determine whether the internal audits contained findings relevant to our audit without examining the internal audits reports. *Government Auditing Standards*, paragraph 8.11, states, "[a]uditors should also report any significant constraints imposed on the audit approach by information limitations or scope impairments, including denials of access to certain records or individuals."

Corinthian Comments

Corinthian concurred with OIG's Audit Results section that Everest was not in violation of Section 435(d)(5)(A) and (C) of the HEA. However, Corinthian expressed no view on OIG's Other Matters section and reserved the right to concur or disagree with the information at a later time. Additionally, Corinthian disagreed with the scope limitation and requested that the scope limitation be removed from the report. Corinthian stated that while it recognized the importance of auditors assessing audit risk through gaining an understanding of the results of previous audits, such assessment should be

performed within the context of the audit objectives and the results of previous audits that relate to the current audit objectives as indicated in *Government Auditing Standards*, paragraph 7.11(e). Corinthian further stated that its audit liaison made representation that the internal audit reports did not address the issue of prohibited inducements and its outside counsel reviewed the internal audit reports and informed OIG that such reports did not address the issue of prohibited inducements. Corinthian argued that OIG's request for the internal audit reports raised the issue of whether the internal audit reports were protected under the "self-critical analysis privilege," citing *Bredice v. Doctors Hosp.*, 50 F.R.D 249 (D.D.C. 1970). Corinthian stated that the "self-critical analysis privilege" protects evaluative materials from disclosure in order to permit a business to engage in candid self-assessment without fear that such materials will be used against it. Corinthian's response is included in its entirety as an Attachment to this report.

OIG Response

Corinthian's comments did not cause us to change our scope limitation. Corinthian's assertion of a self-analysis privilege to withhold internal audit reports does not change our obligation to report a scope limitation under *Government Auditing Standards*; that obligation applies regardless of whether information is validly or improperly withheld. We routinely request and receive without objection internal audits prepared by parties that we audit. We note that in *Bredice*, the case cited by Corinthian, the district court applied the self-analysis privilege in the context of private litigation. The Court of Appeals for the District of Columbia subsequently concluded that "[c]ourts with apparent uniformity have refused its application where, as here, the documents in question have been sought by a governmental agency." *FTC v. TRW, Inc.*, 628 F.2d 207, 210 (D.C. Cir. 1980).

OTHER MATTERS

The agreements between Corinthian and SLX and SLM did not comply with the prohibitions on inducements in Section 435(d)(5)(A) and (C) of the HEA, and they contained inducements that were attributable to SLX and SLM. We found that two agreements between Corinthian and SLX and one agreement between Corinthian and SLM included prohibited inducements. In general—

- SLX agreed to provide prohibited services to Corinthian, assisting it with the development of a Web site and administrative reports;
- SLX limited Everest students' access to private loans based on Everest's FFELP loan volume and Federal cohort default rate; and
- SLM agreed to offer students' parents a \$500 credit towards closing costs of a new SLM Home Loan, if the parents borrowed PLUS loans with SLM.

A March 30, 2007, agreement between Corinthian and SLX specifically stated that "SLX shall assist Corinthian with the development of a [Web] site providing student loan information and assist Corinthian in establishing a link to SLX's [Web] site (including a splash page) for the

purpose of PLUS pre-approval, loan management, and Stafford loan applications.”³ SLX also agreed to provide administrative reports for each campus Corinthian owned, upon Corinthian’s request.

Another agreement between Corinthian and SLX offered Credit Risk Subsidy Program (CRSP) loans to Everest’s high risk student borrowers but required Corinthian to pay a 10 to 40 percent premium on those loans. The agreement limited Everest’s students’ access to CRSP loans based on Everest’s FFELP loan volume and Federal cohort default rate.⁴ Under this agreement, SLX could temporarily terminate the agreement if the CRSP loans exceeded 15 percent of all educational loans made to Corinthian’s students, including loans made under the FFELP. In addition, the agreement stated that it may be terminated immediately by SLX upon delivery of written notice to the school if the school’s Federal cohort default rate exceeded 15 percent.

A program review report of “Fifth Third Bank as Eligible Lender Trustee (ELT)” issued by the U. S. Department of Education’s (ED) Federal Student Aid (FSA) on February 23, 2009, also reported the two concerns we identified with respect to SLX. The program review report indicated that Fifth Third Bank, as ELT for SLX, provided Web site redesign services to a particular educational institution with the sole purpose of securing FFELP volume. As set forth in the report, such services are prohibited by Section 435(d)(5)(A) of the HEA.

The program review report also found that a termination clause present in many SLX agreements tied private loans to overall education loan volume. The report stated that the application of the clause to the overall education loan volume which included FFELP loans could appear to be increasing the amount of private loan volume that a school may have available to its students. The report recommended that SLX modify its agreements to clearly explain that the relationship between a school’s access to private loans and SLX’s FFELP volume is to limit its financial risk.

Resolution of the above mentioned program review report was included in a Determination and Voluntary Disposition (Settlement Agreement), dated March 23, 2009, between ED, Fifth Third Bank, SLX and SLX’s parent company, CIT Group Inc. Fifth Third Bank and CIT Group Inc. agreed to respectively pay ED the sum of \$300,000 and \$4,837,500. ED agreed to take no further action against Fifth Third Bank or CIT Group Inc. on the issues raised in the program review report.

On November 17, 2009, SLX was made aware of the results of our audit and given an opportunity to respond. SLX’s response was provided to us on December 4, 2009, indicating that SLX did not concur with our results. According to its response, SLX did not believe any improper inducements occurred in its agreements with Corinthian since it had developed its loan programs in consultation with experienced industry counsel and within the context of the guidance that was available from ED at the time. In addition, SLX believes that the issues raised by our audit are moot because SLX has ceased originating both government guaranteed and

³ A “splash page” is the page of a Web site that the user sees first before being given the option to continue to the main content of the site. Splash pages are used to promote a company, service, or product or are used to inform the user of what kind of software or browser is necessary in order to view the rest of the site’s pages.

⁴ In general, Federal cohort default rates, calculated under 34 C.F.R. Part 668, Subpart M (for Federal fiscal year 2008 and earlier) were the percentage of a school’s borrowers who entered repayment on FFELP or William D. Ford Federal Direct Loan Program loans during a Federal fiscal year and defaulted before the end of the following Federal fiscal year.

private student loans, and any actual or potential issues on inducements had been resolved by the Settlement Agreement with ED.

SLX's comments did not cause us to alter our conclusion that improper inducements were offered. On July 9, 2010, we separately referred the SLX issues to FSA in an alert memorandum, *Lender Agreements between Sallie Mae and Student Loan Xpress and Corinthian Colleges, Inc., Contained Inducements* (Control Number ED-OIG/L02K0001), in which we recommend FSA determine whether the issues were resolved by the Settlement Agreement, and to take appropriate actions if the issues were not resolved.

Sallie Mae Offered Parents an Inducement to Borrow PLUS Loans

SLM's agreement with Corinthian states that SLM would provide a \$500 credit towards closing costs on a new SLM Home Loan to parents who obtained a PLUS loan from SLM. A March 21, 2007, "Letter of Understanding" between Corinthian and SLM summarized the products and services that SLM would provide to Corinthian, its students, and their parents. According to the letter, SLM would be Corinthian's primary loan provider and would grant Corinthian students access to both Federal and private education loans. Included in this agreement was a provision for parents to obtain a one-time \$500 credit towards their closing costs of a new home loan from SLM if the parent obtained a PLUS loan from SLM. Through this provision, parents of Corinthian students were offered an inducement to borrow PLUS loans in order to qualify for a one-time \$500 credit towards closing costs on a new SLM Home Loan. According to Section 435(d)(5)(C) of the HEA, lenders cannot offer, directly or indirectly, loans as an inducement to a prospective borrower to purchase other products.

On November 16, 2009, SLM was made aware of the results of our audit and given an opportunity to respond. SLM provided a response on December 4, 2009, indicating that it did not concur with our results. According to its response, SLM did not believe that the \$500 closing cost credit was an inducement by SLM for Corinthian parents to apply or obtain PLUS loans from SLM. SLM stated in its response that it did not violate Section 435 (d)(5)(A) and (C) of the HEA in view of the facts that: 1) the \$500 closing cost credit was not, in fact, marketed to any prospective parent borrower, and 2) Corinthian parents were allowed to obtain PLUS loans regardless of whether they agreed to apply for or obtain an SLM home loan. SLM stated that no PLUS borrower at Everest obtained a mortgage from SLM during the timeframe.

As part of this audit, we did not examine how SLM marketed its mortgage loans or marketed the FFELP loans to Everest students and parents and cannot corroborate the statements made by SLM. However, whether or not the closing credit was in fact marketed to students or parents, the fact remains that SLM offered the inducement through the agreement itself in violation of Section 435 (d)(5)(A) and (C) of the HEA. While parents may have been allowed to obtain PLUS loans regardless of whether they agreed to apply for or obtain an SLM home loan, the \$500 credit was an inducement to obtain PLUS loans, thus violating Section 435(d)(5)(C) of the HEA. Therefore, we have not modified the Other Matters section based on SLM's comments and separately referred this matter to FSA in the memorandum we issued on July 9, 2010.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our audit was to determine whether the agreements between the institution and all lenders for the period July 1, 2007, through September 30, 2008, complied with the anti-inducement provisions of the HEA. We reviewed all agreements between lenders and the school, including the corporation that owned the school.

To accomplish our objective, we:

- Obtained an understanding of Everest's and Corinthian's internal controls over prohibited lender inducements by conducting interviews with school and corporate officials.
- Reviewed requirements prohibiting lender inducements in the HEA and regulations.
- Reviewed Everest's documents related to all lenders, including (but not limited to):
 - The list of lenders Everest and Corinthian had interacted with in the past 5 years;
 - Everest's chart of accounts;
 - Individual student files for those who participated in the FFELP.
- Obtained and reviewed written policies and procedures regarding incentives that may be provided to Corinthian employees.
- Obtained and reviewed a list of charitable contributions made by Corinthian.
- Obtained and reviewed any agreements between the corporate entity, the school, and lenders to identify those with arrangements that warrant further review or indicated potential improper inducement activities.
- Obtained and examined Everest's general ledger detailed accounts report.
- Obtained and reviewed Corinthian's and Everest's latest audited Financial Statements and Compliance Attestation Examination of the Title IV Student Financial Assistance Programs and the related audit documentation.
- Conducted interviews with the Independent Public Accountants (IPA) that performed the consolidated financial statements audit and Everest's Compliance Attestation Examination of the Title IV Student Financial Assistance Programs.

We conducted audit fieldwork at Everest's campus in Brighton, Massachusetts, from October 27, 2008, through October 31, 2008. We conducted fieldwork at Corinthian's corporate headquarters, located in Santa Ana, California, from May 11, 2009, through May 15, 2009. In addition, we went onsite at the IPA's office in San Diego, California, to review the work of the IPA that performed Everest's compliance audit. We held our exit conference with Everest on August 31, 2009.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Scope Limitation

A request for Everest's internal audit reports was made on two separate occasions. In response to our first request, Corinthian responded that the internal audit reports were not applicable to our audit. Upon our second request, we were informed that Everest's internal audit reports did not contain any findings related to lender inducements. On March 23, 2009, Corinthian and OIG agreed that Everest would produce the table of contents of its internal audits in an attempt to demonstrate to OIG's satisfaction that the issue of prohibited inducements was not covered by its internal audits. Upon review of the table of contents provided, we requested additional details on selected sections of these reports for review. Our request for selected sections of Everest's internal audit reports was denied. Corinthian's refusal to provide Everest's internal audit reports prevents us from obtaining a complete understanding of internal controls within the context of our audit objective and causes us to qualify any conclusions we have drawn on the basis of the data made available.

ADMINISTRATIVE MATTERS

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 Education Department official, who will consider them before taking final Departmental action on this audit:

William J. Taggart
Chief Operating Officer
Federal Student Aid
U.S. Department of Education
Union Center Plaza, Room 112E1
830 First Street, N.E.
Washington, DC 20202

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

We appreciate the cooperation and assistance extended by your staff during the audit. If you have any questions, please contact me at (646) 428-3888.

Sincerely,

/s/

Daniel P. Schultz
Regional Inspector General
for Audit

Acronyms /Abbreviations Used in this Report

C.F.R.	Code of Federal Regulations
Corinthian	Corinthian Colleges, Inc.
CRSP	Credit Risk Subsidy Program
ED	U.S. Department of Education
ELT	Eligible Lender Trustee
Everest	Everest Institute – Brighton
FFELP	Federal Family Education Loan Program
FSA	Federal Student Aid
HEA	Higher Education Act of 1965, as amended
IPA	Independent Public Accountant
OIG	Office of Inspector General
PDF	Portable Document Format
Settlement Agreement	Determination and Voluntary Disposition
SLM	Sallie Mae, Inc.
SLX	Student Loan Xpress, Inc.

Attachment



LEGAL DEPARTMENT

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May 25, 2010

Via e-mail and Overnight Mail

Daniel P. Schultz
Regional Inspector General for Audit
U. S. Department of Education
Office of Inspector General
32 Old Slip, 26th Floor
Financial Square
New York, NY 10005

Re: Draft Reports: *Everest Institute's Lender Agreements* (Control Number ED-OIG/A02J0001) and *National Aviation Academy - New England's Lender Agreements* (Control Number ED-OIG/A02J0005)

Dear Mr. Schultz:

We are in receipt of your draft audit reports entitled *Everest Institute's Lender Agreements* (Control Number ED-OIG/A02J0001) and *National Aviation Academy – New England's Lender Agreements* (Control Number ED-OIG/A02J0005), both dated April 26, 2010, and appreciate the opportunity to respond. As you are aware, Corinthian Colleges, Inc. ("Corinthian") is the parent company of Everest Institute in Brighton, Massachusetts ("Everest"). Additionally, prior to May 1, 2008 Corinthian was the parent company of WyoTech Bedford ("WyoTech"), now known as National Aviation Academy - New England ("NAA-NE").

Audit Results

Corinthian concurs that during the relevant periods Everest and WyoTech were not in violation of Section 435(d)(5)(A) and (C) of the Higher Education Act of 1965, as amended (the "HEA"). We express no view as to the compliance of lenders that are described in the draft audit reports.

Other Matters

Corinthian has no comment regarding the findings with respect to NAA-NE after the

change of ownership on May 1, 2008. Additionally, Corinthian has no comment on the information contained in the "Other Matters" sections of the draft reports because they do not allege that Everest or WyoTech were in non-compliance with Section 435(d)(5)(A) and (C) of the HEA. Rather, they address alleged non-compliance by lenders. Corinthian reserves the right to concur or disagree with the information in the future, if necessary.

Scope Limitation

Corinthian disagrees with the scope limitation described on pages 2-3 and 7 of the draft audit report for Everest, and pages 3-4 and 9-10 of the draft audit report for WyoTech. We recognize the importance of auditors assessing audit risk by gaining an understanding of the results of previous audits, but, as the draft audit reports note, such assessments are to be performed "within the context of the audit objectives," and the auditors are to review previous audits that "relate to the current audit objectives." Everest Draft Audit Report, at 2 (quoting Government Auditing Standards, at ¶ 7.11(e)).

Internal Audits were Unrelated to the Audit Objectives

Corinthian's audit liaison made representations to the auditors that the internal audits in question did not address the issue of prohibited inducements and, therefore, did not "relate to the current audit objectives," i.e., the inducement prohibition. Further, Corinthian's outside counsel, Jonathan Vogel, reviewed the internal audit reports and explained to the OIG's chief counsel that the internal audits did not address lender inducements. Moreover, Mr. Vogel explained that Corinthian was reluctant to disclose evaluative materials, and that, considering that the internal audits did not at all address the issue of prohibited lender inducements, the auditors' examination of those evaluative materials would not be "within the context of the audit objectives."

In order to enable the auditors to verify that the internal audits did not address prohibited lender inducements, Corinthian provided the auditors with relatively detailed indices of the compliance areas addressed in the internal audits for fiscal years 2006, 2007, and 2008 that were requested. The indices showed that prohibited lender inducements were not addressed in the internal audits.

The Self-Critical Analysis Privilege Protects against Disclosure

In discussions with OIG's chief counsel, Mr. Vogel explained that the auditors' request for Everest's voluntary, internal audits raised the issue of whether those audits were protected under the self-critical analysis privilege, or the important public policy considerations that underlie it. The self-critical analysis privilege protects evaluative materials from disclosure in order to permit a business to engage in candid self-assessments without fear that such materials will be used against it. See, e.g., Bredice v. Doctors Hospital, Inc., 50 F.R.D. 249 (D.C. 1970).

The self-critical analysis privilege protects an organization from the dilemma of either (i) investigating possible regulatory violations, ascertaining whether they exist, and correcting any violations, but thereby creating a self-incriminating record that may be evidence of liability, or (ii) deliberately foregoing an internal evaluative review and making a record on the subject (and possibly leaving a regulatory violation uncorrected) in order to lessen the exposure of regulatory claims. The self-critical analysis privilege is similar to, and based on the same public policy considerations as, Rule 407, Federal Rules of Evidence, which excludes evidence of subsequent remedial measures. Without this privilege, organizations such as Corinthian would be chilled from such self-analysis. Indeed, in our experience, regulatory bodies have seemed to understand this concern, as this is the first time we have encountered a request from a regulatory body for our internal audits.

Summary

In summary, as demonstrated by the draft audit reports' "Other Matters" sections, the auditors obtained from Everest and WyoTech all of the schools' primary sources of information on the issue of prohibited lender inducements. As a result, the auditors did not experience "any significant constraints imposed on the audit approach." Everest Draft Audit Report, at 3 (quoting Government Auditing Standards, at ¶ 8.11). Despite the assertion in the draft audit reports to the contrary, the auditors did, in fact, obtain a "complete understanding" of the schools' information related to prohibited lender inducements. Everest Draft Audit Report, at 7. There is, therefore, no reason for the draft audit reports to qualify their conclusions on the basis of the information made available.

Corinthian respectfully requests that the scope limitation be removed from both draft audit reports.

Sincerely,



Stan A. Mortensen
Executive Vice President
and General Counsel

cc: Jonathan Vogel, Esq.
Linda Buchanan