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IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH, CENTRAL DIVISION

CENTER FOR EXCELLENCE IN HIGHER EDUCATION, an Indiana Corporation, *Plaintiff*, v. JOHN B. KING, JR., in his official capacity as Secretary of the United States Department of Education; UNITED STATES DEPARTMENT OF EDUCATION; and UNITED STATES OF AMERICA, *Defendants*.	**COMPLAINT AND JURY DEMAND** Case No. 2:16-cv-00911-PMW Magistrate Judge Paul M. Warner

COMPLAINT AND PRAYER FOR RELIEF

Plaintiff, Center for Excellence in Higher Education, Inc. ("Plaintiff" or "CEHE"), alleges the following, by and through its attorneys, for its complaint against Defendants John B. King, Jr., in his official capacity as Secretary of the United States Department of Education ("King" or the "Secretary"), the United States Department of Education (the "Department"), and the United States of America (the "United States"):

PARTIES

1. CEHE is a tax-exempt, nonprofit corporation under section 501(c)(3) of the Internal Revenue Code ("IRC"), incorporated under the laws of the State of Indiana, with its principal place of business at 4021 S 700 E, Suite 400, Salt Lake City, Utah 84107.

2. John B. King, Jr. is the Secretary of the Department. His official address is 400 Maryland Avenue, S.W., Washington, D.C. 20202. He is being sued in his official capacity. In that capacity, King has overall responsibility for the operation and management of the Department. King, in his official capacity, is therefore responsible for the Department's acts and omissions alleged herein.

3. The United States Department of Education is, and was at all times relevant hereto, an executive agency of the United States Government. The Department, in its current form, was created by the Department of Education Organization Act of 1979, 20 U.S.C. § 3401 *et seq.*, Pub. L. No. 96-88, 93 Stat. 668. The Department is headquartered at 400 Maryland Avenue, S.W., Washington, D.C. 20202.

4. The United States of America is the federal government formed under the Constitution of the United States, with its capital in Washington, D.C.

JURISDICTION AND VENUE

5. This action arises under the Higher Education Act of 1965, 20 U.S.C. § 1001, *et seq*. ("HEA"). This Court has subject-matter jurisdiction over this action under 28 U.S.C. § 1331. The Court is authorized to issue the nonmonetary relief sought herein pursuant to 28 U.S.C. §§ 2201, 2202.

6. Venue is proper in this Court under 28 U.S.C. § 1391(e)(l) because this is an action against the United States, an officer of the United States, and an agency of the United States. A substantial part of the events or omissions giving rise to this action occurred in this judicial district. Plaintiff resides in this judicial district. No real property is involved in the action.

FACTUAL ALLEGATIONS

A. CEHE Acquires Ownership of Formerly Proprietary Colleges

7. CEHE is a nonprofit public benefit corporation incorporated under the Indiana Nonprofit Corporation Act of 1991 ("the Act") on December 22, 2006.

8. Founded by philanthropists who had donated millions of dollars to colleges and universities in the United States and who were concerned about higher education's continuing decline, CEHE was organized for the purpose of promoting excellence in higher education by working with philanthropists, institutions of higher education, and charitable organizations to develop and implement research and educational programs designed to ensure that American colleges and universities were training students for the challenges of a global marketplace. CEHE's founders believed that through effective philanthropy, due diligence, proper

governance, and management accountability, America's colleges and universities could be transformed into high-performing institutions that prepare today's students to be tomorrow's leaders.

9. CEHE is authorized under its articles of incorporation to pursue these purposes—as well as to assist and engage in all activities which serve chartable, educational, literary and scientific purposes, which are permitted to be carried on by nonprofit corporations under the Act and under the provisions of section 501(c)(3) of the IRC.

10. CEHE's founding Board of Directors consisted of Michael Leven, representing the Marcus Foundation, James Arthur Pope, representing the John William Pope Foundation, and Charles Harper, from the Templeton Foundation.

11. On September 4, 2007, the Internal Revenue Service ("IRS") classified CEHE as a public charity under 509(a)(1) and 170(b)(1)(a)(vi) of the IRC and exempt under section 501(c)(3) of the IRC from federal income taxation. See **Exhibit 1** (September 4, 2007 IRS 501(c)(3) Determination Letter).

12. On that date, the IRS issued CEHE a determination letter classifying CEHE as a tax-exempt nonprofit corporation under section 501(c)(3) of the IRC. The determination letter also confirmed that contributions to CEHE were tax deductible under section 170 of the IRC.

13. In 2012, after years of evaluating and commenting on higher education, CEHE began exploring the opportunity of tackling head-on the challenges facing higher education by becoming a direct provider of higher education.

14. Those investigations culminated in negotiations for CEHE to merge its operations with those of Stevens-Henager College, Inc., a Utah corporation; CollegeAmerica Denver, Inc., a

Colorado corporation; CollegeAmerica Arizona, Inc., a Colorado corporation; California College San Diego, Inc., a Utah corporation; and CollegeAmerica Services, Inc., a Nevada corporation (collectively, "the Acquired Corporations").

15. Prior to the merger, the Acquired Corporations were owned and operated by the Carl Barney Living Trust ("CBLT") whose trustee was Carl Barney ("Barney").

16. Several of the Acquired Corporations owned and operated colleges ("the Colleges") that participated in federal student financial aid programs ("Title IV programs") as eligible proprietary institutions of higher education.

17. At the time of the negotiations, CEHE's Board of Directors consisted of G.M. Curtis, a retired professor of history at Hanover College and Fellow at the Liberty Fund; Todd Zywicki, George Mason University Foundation Professor of Law, Senior Scholar of the Mercatus Center at George Mason University, and Senior Fellow at the F.A. Hayek Program; and William Dennis, former professor at Denison University and Senior Fellow of the Atlas Economic Research Foundation.

18. The individuals comprising CEHE's Board of Directors ("the independent board") had no ownership interest in or other affiliation with the Acquired Corporations, the Colleges, the CBLT, or Barney.

19. Prior to approving the merger, the independent board retained legal counsel, consulted valuation experts, and conducted significant due diligence on the Acquired Corporations, including an evaluation of the fair market value of the Colleges. See **Exhibit 2** (Declaration of John S. Mercer).

20. On December 31, 2012, the Acquired Corporations merged with and into CEHE. As a result of the merger, CEHE, as the surviving corporation, acquired ownership and operation of the Colleges as nonprofit colleges within the meaning of section 501(c)(3) of the IRC.

21. Following the merger, CEHE amended its articles of incorporation and bylaws, which included naming Barney as a member of CEHE and the Chairman of the Board of Directors. The independent board approved the amendments to CEHE's governance documents before the merger occurred.

22. CEHE's amended governance documents also added, among others, Todd Zywicki, William Dennis, and G.M. Curtis, former directors of the independent board, to CEHE's Board of Directors.

23. The Indiana Nonprofit Act of 1991, under which CEHE is incorporated, obligates CEHE's directors, including Barney, to discharge their duties (1) in good faith, (2) with the care an ordinary person in a like position would exercise under similar circumstances, and (3) in a manner the directors reasonably believe to be in the best interests of the corporation. Indiana Code Ann. § 23-17-13-1. CEHE's Board of Directors have always made a good faith effort to discharge their duties in compliance with these requirements and, in particular, so acted in their capacity as the independent directors with respect to the merger.

24. Barney and/or CBLT do not own CEHE's assets under the laws of the State of Indiana, which is where the nonprofit was organized and created. Similarly, neither have any ownership rights to the assets of CEHE.

B. The IRS Approved CEHE as an Educational Organization

25. Soon after the merger, CEHE submitted a letter to the IRS requesting confirmation of its public charity status and reclassification from that of a publicly supported organization under sections 509(a)(1) and 170(b)(1)(A)(vi) of the IRC to that of an educational organization under sections 509(a)(1) and 170(b)(1)(A)(ii) ("the determination letter request"). See **Exhibit 3** (February 27, 2013 Post-Merger Request Letter to IRS).

26. Enclosed with the determination letter request, CEHE included an executed Form 8940, "Request for Miscellaneous Determination," and a completed Schedule B of the IRS Form 1023 with respect to that section of the form applicable to educational institutions.

27. The determination letter request also provided significant details about the terms of the merger and related transactions, including all of the information the IRS needed to determine whether the merger agreement and related financial transactions complied with the IRS' limitations on private inurement, prohibitions against private benefit, and rules concerning excess benefit transactions in section 4958 of the IRC.

28. The determination letter request explained that:

a. CEHE issued promissory notes for the acquisition of the Colleges in an amount that reflected their fair market value;

b. CEHE's independent Board of Directors reviewed the form and amount of consideration to be paid to the former owner of the Acquired Corporations, and concluded (i) that the merger provided CEHE with fair market value; (ii) that CEHE would provide a modest consulting fee, substantially lower than fair market value, to the former owner for his continued

advisory services; and (iii) that leases of land and buildings from the former owner were at fair market rates; and

c. CEHE's independent Board of Directors approved all changes to CEHE's corporate governance before consummation of the transaction.

29. On July 25, 2014, the IRS issued CEHE a determination letter confirming CEHE's tax-exempt classification under section 501(c)(3) of the IRC. See **Exhibit 4** (July 25, 2014 IRS Letter Updating Charity Status). The determination letter further explained that, upon review of CEHE's determination letter request and supporting documentation, the IRS concluded CEHE met the requirements for classification as an educational organization as described in sections 509(a)(1) and 170(b)(1)(A)(ii) of the IRC.

C. New Ownership and Control of the Colleges by the Nonprofit Organization Triggers a Change of Ownership and Control Under the Department's Regulations

30. Prior to the merger, the Acquired Corporations owned the Colleges and they were proprietary institutions pursuant to the Department's regulatory definition. At that time, each of the Colleges participated in Title IV programs, operating multiple campuses in several states. All of the Colleges were in good standing with their respective state regulatory agencies, accrediting bodies, and the Department.

31. Upon the merger, the Acquired Corporations merged with and into CEHE, transferring exclusive ownership and operational control of the Colleges into CEHE, a nonprofit corporation.

32. Following the merger, the Colleges met the definition for a nonprofit institution under the HEA, as ones "owned and operated by one or more nonprofit corporations or

associations, no part of the net earnings of which inures, or may lawfully inure, to the benefit of any private shareholder or individual." 20 U.S.C. § 1003.

33. Likewise, the Colleges met the Department's regulatory definition for a nonprofit institution contained in 34 C.F.R. § 600.2. To wit:

a. The Colleges were owned and operated by CEHE, a nonprofit corporation, with no shareholder or individual benefiting from the net earnings of the corporation;

b. The Colleges were legally authorized to operate as nonprofit organizations in each state in which they are physically located; and

c. The IRS determined that CEHE was a tax-exempt organization to which tax contributions are deductible under 501(c)(3) of the IRC.

34. Under the Department's regulations, this change in ownership and control terminated the Colleges' eligibility to participate in federal student financial aid programs under the HEA. 34 C.F.R. § 600.31.

35. Under the HEA, when an institution of higher education undergoes a change in ownership or control, the institution's program participation agreement expires and the institution's eligibility to participate in HEA programs ceases. 34 C.F.R. § 600.31.

36. While the loss of eligibility to participate in HEA programs occurs when a new owner acquires an institution, the Department also recognizes other kinds of "covered transactions" that result in a change in ownership or control, including when a for-profit institution becomes a nonprofit institution. 34 C.F.R. § 600.31(d)(7); 59 Fed. Reg. 22324 (Apr. 20, 1994); Federal Student Aid Handbook, Volume 2, Chapter 5, p. 2-92 (August 2015).

37. Indeed, the Department has clarified that a change in an institution's tax status "from a taxable to a tax-exempt entity that qualifies under 501(c)(3) of the Internal Revenue Service. . . constitutes a change of ownership and control." 59 Fed. Reg. 22324 (Apr. 20, 1994).

38. To reestablish the Colleges' eligibility to participate in HEA programs, the Department's regulations required CEHE to submit applications to the Secretary to approve the Colleges' new owner's participation in Title IV federal financial aid programs. The Department's regulations permit the Secretary to continue an institution's participation in Title IV programs on a provisional basis while the institution awaits reinstatement of eligibility for the institution's new owner. 34 C.F.R. § 600.20(g).

D. CEHE Submits A Change of Ownership Application Through the Department's Pre-Acquisition Review Process

39. Given the significant effect a change in ownership has on an institution's participation in Title IV programs, the Department allows institutions anticipating a change in ownership to submit a pre-acquisition review application for its review. The pre-acquisition review application is submitted via an electronic application ("E-App") system established and maintained by the Department. The purpose of the pre-acquisition review is to allow the Department to review the proposed change of ownership and identify any concerns, clarifications, or issues it may have before the transaction is consummated.

40. Although the Department neither approves nor denies a pre-acquisition review application, the Department notifies the institution whether or not the pre-acquisition review application is approvable, if the institution properly completed the E-App, and whether the Department identified any items that need to be addressed before a final application would be approvable. 64 Fed. Reg. 58608 (Oct. 29, 1999).

41. The purpose of this pre-acquisition review process is to permit the Department to determine whether the institution has completely and accurately answered all the questions in the application. 64 Fed. Reg. 58608; Department of Education, Federal Student Aid Handbook, Vol. 2, Ch. 5, p. 2-94 (August 2015).

42. The pre-acquisition review process also allows the institution to ascertain what, if any, additional requirements the Department may impose on the institution to re-establish eligibility. This is the fundamental purpose of the Department's pre-acquisition review process.

43. CEHE took advantage of the Department's pre-acquisition review process. Before acquiring the Colleges, CEHE apprised the Department of the planned changes to the corporate ownership of the Colleges.

44. In a letter dated October 2, 2012, counsel for the Colleges informed the Department of the planned merger of the Acquired Corporations into CEHE. See **Exhibit 5** (October 2, 2012 Pre-Acquisition Review Request Letter). The letter also informed the Department that CEHE was recognized by the IRS as a nonprofit corporation exempt from federal income taxation since 2007.

45. Counsel further explained that, upon completion of the merger, CEHE would be the sole owner and operator of the Colleges. The letter informed the Department about the anticipated funding for the transaction and the effect of the planned transaction on the Colleges' existing leases, facilities, and operational resources.

46. Finally, in view of the significant stake the Colleges—and their students—had in ensuring a smooth change of ownership, the letter inquired as to whether or not the merger of the

Colleges into CEHE would prompt the Department to impose any special terms or conditions upon CEHE in new program participation agreements.

47. On November 2, 2012, the Department responded to the Colleges' pre-acquisition review request by requesting additional documentation it wanted to examine including the following:

a. A copy of CEHE's 501(c)(3) determination letter from the IRS;

b. The names of the individuals or entities comprising CEHE's Board of Directors;

c. A copy of CEHE's bylaws and articles of incorporation;

d. A detailed description or copy of any draft contracts or agreements that CEHE may enter into as a result of the change of ownership; and

e. A copy or detailed description of the planned payment arrangements associated with the loans necessary to consummate the transaction of the change in ownership.

48. Counsel for the Colleges responded to the Department's November 2, 2012 letter shortly thereafter, submitting the required pre-acquisition review E-App and providing the Department with the requested information and documentation. See **Exhibit 6** (November 2, 2012 Response to Pre-Acquisition Review Request Letter).

49. CEHE's November 2, 2012 letter included as attachments, CEHE's 501(c)(3) determination letter (dated September 4, 2007), the names of the individuals and entities comprising CEHE's Board of Directors, and CEHE's articles of incorporation and bylaws.

50. The response letter also included a detailed memorandum describing the anticipated transaction. The memorandum included draft contracts and agreements and a detailed description of the planned payment arrangements to consummate the merger.

51. The detailed description of the planned payment arrangements that the Colleges provided to the Department disclosed the existence of seller loans and identified how the payment amounts would be determined and the manner in which payments would be made to the seller.

52. By letter dated December 20, 2012, the Department informed the Colleges of the results of its pre-acquisition review and its assessment of CEHE's response and the related documentation the Department had received from the Colleges. See **Exhibit 7** (December 20, 2012 Pre-Acquisition Review Letter from Department). The Department reminded CEHE that the Secretary could continue an institution's participation in Title IV programs on a provisional basis *only* if the institution submitted a materially complete application within ten (10) business days after the change in ownership occurred.

53. In its pre-acquisition review response, the Department added that, to the extent CEHE completed the E-App and submitted the required documentation following the merger, the Department foresaw no impediment to the issuance of a temporary program participation agreement upon CEHE becoming the owner and operator of the Colleges.

54. In the Department's pre-acquisition review response, it identified only one unique requirement with which the Colleges would have to comply following the change in ownership from proprietary to nonprofit. Notably, the Department stated that, because the change in ownership included an institutional change in structure from proprietary to nonprofit, CEHE would have to report the Colleges' percentage of annual revenue received from Title IV programs (the "90/10 rule") for the Colleges' upcoming fiscal year ending December 31, 2013. CEHE relied on the Department's representation in this regard. In its letter informing the

Colleges of the results of its review, the Department provided no indication that it would classify the Colleges as proprietary institutions for Title IV regulatory purposes following the change in ownership while the Colleges' E-Apps were pending.

55. The Department had previously announced that "the change from for-profit to nonprofit status warrants adopting as those conditions of the required provisional certification *those restrictions that would have applied to the institution had it remained a for-profit entity*." 59 Fed. Reg. 22324 (Apr. 20, 1994). Importantly, however, those conditions of the provisional certification that would apply, had the institution remained a for-profit entity, must be specified in the institution's provisional program participation agreement. 34 C.F.R. § 668.14(a)(1); see also Mission Group Kansas v. Riley, 146 F.3d 775 (10th Cir. 1998) (addressing the Secretary's assertion that he was authorized to "[specifically] condition[] [an institution's] receipt of Title IV funds on their complying with the [90/10] rule for a provisional period – despite [the institution's] non-profit status").

56. This requirement for specificity in the provisional program participation agreement applies equally to the temporary provisional program participation agreement issued to CEHE immediately following its ownership of the Colleges. Consistent with its regulations, the Department specified only one for-profit requirement (the 90/10 Rule) with which the Colleges were required to comply following the change in ownership. The 90/10 Rule requirement was specifically limited to the Colleges' first fiscal year following the change in ownership. See Department of Education, Federal Student Aid Handbook, Vol. 2, Ch. 5, p. 2-65 (August 2015) ("A school that converts from a for-profit to a nonprofit status must report its

compliance with the 90/10 revenue test for the first year after its conversion."); See also **Exhibit 7**.

57. CEHE informed the Department of the Colleges' change in ownership within ten business days of the transaction closing and provided supplementary documentation to its previously filed E-Apps, as required by 34 C.F.R. § 600.20(g).

58. Upon receipt and verification of CEHE's materially complete application, the Department, on January 31, 2013, issued CEHE temporary provisional program participation agreements ("TPPAs") for the Colleges. The TPPAs continued the Colleges' participation in Title IV programs on a provisional basis while the Department completed its review of CEHE's applications for new program participation agreements following the Colleges' change of ownership.

E. The Department Delays Action On CEHE's Approvable Application For Over Forty-Four Months

59. On January 31, 2013, the Department issued TPPAs to CEHE for the Colleges. The TPPAs continued the Colleges' participation in Title IV programs on a provisional basis while the Department continued its review of CEHE's applications for new program participation agreements following the Colleges' change in ownership. 34 C.F.R. § 600.20(h).

60. Because CEHE was a nonprofit corporation at the time it acquired the Colleges, CEHE was subject to the regulations applicable to nonprofit organizations after the merger. CEHE was also required to submit new applications for the Colleges' participation following the merger.

61. Although CEHE was required to comply with the Department's 90/10 Rule for the 2013 fiscal year, the Secretary did not impose that requirement in the TPPAs it issued to

CEHE. Regardless, each of the Colleges complied with the 90/10 Rule during the 2013 fiscal year.

62. Following the Secretary's execution of the TPPAs on January 31, 2013, the Colleges were allowed to continue to participate in Title IV programs on a month-to-month basis.

63. Since issuance of the TPPAs, several of the Department's public disclosures confirmed the Colleges' nonprofit status. For example, data collected and reported in the Department's College Scorecard, College Navigator, and Integrated Postsecondary Education Data System websites list the Colleges as nonprofit institutions. Additionally, all of CEHE's actions, communications, and correspondence with the Department since the merger have correctly identified the Colleges as nonprofit institutions.

64. Each year, the Department requires institutions participating in Title IV programs to submit audited financial statements in order to demonstrate that they meet the Department's financial responsibility standards. 34 C.F.R. § 668.171(a). The Secretary determines whether an institution is financially responsible, in part, based on the institution's equity, primary reserve, and net income ratios. 34 C.F.R. § 668.171(b)(1). Under the Department's regulations, the formula for these ratios for nonprofit institutions is different from the formula for proprietary institutions. 34 C.F.R. § 668.172(b)(1-2). An independent auditor must prepare an institution's annual audited financial statement report and, in order to do so, must know whether to apply the nonprofit or for-profit institution formula for the ratios.

65. Moreover, pursuant to the regulations of the Office of Management and Budget applicable to nonprofit audits and generally accepted accounting principles ("GAAP"), the

accounting standards applicable to nonprofit institutions of higher education differ substantively from those applicable to proprietary institutions.

66. Between November 2012 and April 2016, CEHE submitted to the Department four annual audited financial statements. Each of these audited financial statements clearly identified CEHE's 501(c)(3) status and the Colleges' nonprofit status.

67. The Department accepted CEHE's audited financial statements that were prepared in accordance with the accounting standards applicable to nonprofit corporations and/or institutions. It also relied upon CEHE's audited financial statements to make determinations as to the Colleges' compliance with the Department's financial responsibility requirements. Indeed, following its review of CEHE's 2013 and 2014 audited financial statements, the Department concluded that CEHE's financial responsibility composite score fell short of the Department's regulatory minimum. As a result, the Department demanded a substantial letter of credit ("LOC"). The Department's initial LOC demand to CEHE was for $71,600,000, which represented 50% of the Title IV distributed by the Colleges in the previous financial aid award year. Historically, LOC's required by the Department based on concerns about an institution's financial responsibility have been much smaller than the amount the Department demanded of CEHE.

68. The Department informed CEHE of its demand for an LOC in a letter dated January 26, 2015. See **Exhibit 8** (January 26, 2015 Department Letter Demanding 50% Letter of Credit). The letter explained that the Department required an LOC because CEHE's composite score was below the Department's minimum requirement. The Department knew at the time it required CEHE to post the LOC that CEHE was a nonprofit corporation operating the Colleges

as nonprofit institutions because CEHE's audited financial statements for 2013 and 2014 had been prepared in accordance with the standards for nonprofit institutions.

69. From April through June 2015, CEHE made numerous urgent requests to meet with Department officials to discuss the LOC. The Department repeatedly refused to meet. It was only after CEHE's numerous electronic mails and letters explaining why the Department's demand for an LOC of over seventy million dollars was unwarranted that the Department ultimately agreed to lower its LOC demand to $42.9 million dollars on May 1, 2016.

70. However, even with the lower LOC demand, CEHE advised the Department that it could not secure such a large LOC given the Colleges' financial position and the current banking environment in the United States. CEHE further informed the Department that the only reason CEHE failed to meet the composite score minimum was because of the debt and goodwill on CEHE's balance sheet. CEHE demonstrated to the Department that CEHE met all of the other financial responsibility requirements. Finally, notwithstanding CEHE's otherwise overall financial stability, CEHE informed the Department that its demand for an immediate $42.9 million dollar LOC would cause the Colleges to be unable to pay on-going expenses and payroll and therefore force the Colleges to close.

71. On May 11, 2015 CEHE sent a letter to the head of the Department's Federal Student Aid ("FSA") division requesting an immediate meeting to avoid the closure of the Colleges and the negative impact closure would have on students and employees. The Department again refused to meet. It was only after a Utah Congressional delegation intervened on behalf of CEHE that the Department agreed to meet.

72. On May 16, 2015, the Department advised Eric Juhlin, CEHE's Chief Executive Officer, that it would meet with him on May 20, 2015 to discuss its $42.9 million dollar LOC demand. However, before the Department would meet with CEHE on May 20, 2015, it demanded an initial $14.3 million dollar LOC by May 18, 2015. CEHE asked the Department to suspend any LOC demand until after the parties had the chance to meet on May 20, 2015. The Department agreed to do so, but only on the condition that CEHE immediately suspend the Colleges' participation in Title IV programs. CEHE had no choice but to suspend the Colleges' participation in Title IV programs because of its need to meet with the Department.

73. Mr. Juhlin, CEHE's legal counsel, and CEHE's Chairman met with Robin Minor, head of the FSA division, and other Department officials on May 20, 2015. During the meeting, Department officials refused to answer any questions from CEHE. Initially, the Department officials said that their meeting participation would be limited to listening to what CEHE had to say and that they would not respond to any questions from CEHE. Despite months of prior communications between the parties, the Department revealed for the first time during the meeting that its LOC demand was also predicated upon a pending federal False Claims Act *qui tam* action and a lawsuit by the Colorado Attorney General against CEHE. As of the date of the meeting, each case was still in the pleading and discovery stage.

74. During the meetings, CEHE presented a plan to restructure its debt and other balance sheet accounts designed to cause CEHE to meet the required composite score. CEHE also sought assurances from the Department that, if it implemented the plan, the LOC demand would be withdrawn following CEHE's submission of audited financial statements demonstrating a compliant composite score. The Department refused to provide any such

assurance. Instead, the Department stated it would take several months review any new audited financial statements and renewed its demand that CEHE immediately post an LOC for $42.9 million dollars.

75. Ultimately, the Department agreed to an alternative to its LOC demand. The Department said CEHE could make three escrow deposits of $14.3 million dollars each, totaling $42.9 million dollars, by December 31, 2015, in lieu of a letter of credit.

76. CEHE then implemented a restructuring plan, which included, in late 2015, a renegotiation and reduction of existing debt. The reduction totaled $300,000,000. Accordingly, CEHE's audited financial statements for fiscal year 2015 were submitted to the Department in March 2016. The audited financial statements demonstrated that CEHE met the Department's required composite score of at least 1.5. Despite CEHE's satisfaction of the 1.5 composite score along with all of the other requirements of financial responsibility and its request that the escrow funds be released, to date, the Department has refused to release them.

77. CEHE's 2013, 2014, and 2015 annual audited financial statement reported the Colleges' composite score *using the calculation applicable to nonprofit institutions* and each audited financial statement submitted to the Department conspicuously identified CEHE's and the Colleges' nonprofit status. In fact, the Colleges' composite score would have been higher if it had been prepared under the Department's standards applicable to proprietary institutions.

78. As noted above, the Department used the 2013 and 2014 audited financial statements as the basis for its demand for an LOC. In making its LOC demand, the Department treated the seller notes as debt. Had the Department treated the seller notes as equity equivalents,

CEHE's composite score would not have been below the Department's required threshold because there would have been far less debt and a significant increase in equity equivalents.

79. In its August 11, 2016 Decision on Change of Ownership ("Decision") demanding that the Colleges be considered proprietary institutions for Title IV purposes, the Department has chosen to treat the seller notes as equity equivalents as opposed to debt. The Department now claims that the payments on the seller notes are distributions of net profits such as a dividend. **Exhibit 9**.

80. The Department has offered no statutory or regulatory basis for characterizing the seller notes as debt in its demand for an LOC in early 2015 and then treating the seller notes as equity equivalents in its August 2016 Decision.

81. By September 2013, the Department had received all of the merger documents (including the seller notes) and related information necessary to make a determination of whether the seller notes were equity equivalents or debt. The Department has never explained why it took almost three years for it to issue its Decision. It also appears that the Department conveniently changed its characterization of the seller notes to meet its political purposes with respect to the demand for an LOC and its Decision denying nonprofit status under Title IV. Such action is arbitrary and capricious.

82. The Department knew at the time it required CEHE to post the escrow deposit that CEHE's Colleges were owned and operated by a nonprofit corporation and that CEHE was operating the institutions as a nonprofit. As noted above, CEHE had prepared and submitted annual audited financial statements to the Department under nonprofit institution auditing standards and the Department had accepted them.

83. Despite knowing and previously accepting that the Colleges had been operating as nonprofit institutions, the Department *first* notified CEHE that the Department wanted to consider the Colleges as proprietary institutions in a letter dated March 15, 2016. See **Exhibit 10** (March 15, 2016 Department Initial Notice Letter). The Department has never explained why it took thirty-nine (39) months after CEHE acquired the Colleges and one year after it imposed the LOC requirement on CEHE's institutions to reach this conclusion.

84. The Department's March 15, 2016 letter included no reference to any statutory or regulatory support for an assertion that the Colleges must be proprietary institutions for Title IV purposes even though the change of ownership and control transferred to a nonprofit corporation and even though the changes necessitated the applications. See 34 C.F.R. § 600.20(b)(2)(iii) (requiring an institution to reapply "to the Secretary for a determination that institution" meets the applicable requirements to "[r]eestablish eligibility . . . *after the institution changes its status* as proprietary, nonprofit, or public institution") (emphasis added).

85. Upon information and belief, the Department has arbitrarily targeted institutions submitting change in ownership applications in instances in which the new owner is a nonprofit corporation by treating those institutions as if they were proprietary institutions during the pendency of their applications. This practice is improper and unjust because it is occurring without forewarning and is contrary to the Department's historic practice. It is being done solely to subject the institutions to more burdensome compliance requirements.

86. For example, on August 29, 2015, the Department notified CEHE via email that the Colleges had failed to report information required by the gainful employment regulations

applicable to proprietary institutions. See **Exhibit 11** (August 29, 2015 Department Electronic Mail re: Gainful Employment).

87. The Department's gainful employment regulations became effective on July 1, 2015, some two-and-one-half years after CEHE acquired the Colleges. Regardless, these regulations are not applicable to CEHE because CEHE's Colleges are nonprofit colleges exclusively offering degree-granting programs.

88. In an email dated August 30, 2015, CEHE promptly notified the Department that CEHE had no programs to which gainful employment requirements applied because CEHE's nonprofit colleges were exclusively offering degree-granting programs.

89. The Department's March 15, 2016 letter indicates that the Department had always considered the Colleges for-profit institutions. **Exhibit 10**. This letter reversed the Department's previous notification that the Colleges were required to comply with only one regulation applicable to proprietary institutions (i.e., the 90/10 Rule) for the year immediately following the change in ownership. **Exhibit 7.** As such, the Department retroactively applied proprietary school regulations to CEHE.

90. CEHE responded to the Department's March 15, 2016 letter by letter dated April 20, 2016. See **Exhibit 12** (April 20, 2016 CEHE Letter to Department). The letter expressed CEHE's concern about the Department's contention that it considered the Colleges to be for-profit institutions despite the fact the institutions had been operating as nonprofit institutions for over three years. Since it was such a shocking and important matter to CEHE, it asked for an immediate meeting or a telephone conference with the Department to resolve the issues.

91. Upon information and belief, the Department is subjecting converted nonprofit institutions to for-profit requirements, without prior notice, while the institution's change in ownership applications are pending before the Department. Such actions indicate an intentional effort to close those formerly for-profit institutions. As noted above, the Department's recent efforts to impose its gainful employment rules on nonprofit institutions are particularly revealing in this regard. For example, during the negotiated rulemaking sessions for gainful employment, the President's Special Assistant for Education publically observed that the Administration "believe[s] [it] needs to cut [for-profits] out. . . of federal aid." Roberto J. Rodriguez, Conference on Student Loans-Opening Plenary Session (Oct. 24, 2013). The assistant affirmed that this was "the whole premise behind [the] [gainful] employment regulation[s]." Id.

92. Upon information and belief, the Department intentionally delayed action on CEHE's change of ownership applications pending resolution of litigation challenging the implementation of the gainful employment regulations. See Assoc. of Private Sector Colleges & Universities v. Duncan, No. 15-5190, 2016 U.S. App. LEXIS 4381 (D.C. Cir. Mar. 8, 2016).

F. The Department Acted Arbitrarily and Capriciously in Denying CEHE's Application and its Request for Reconsideration

93. On August 11, 2016, approximately forty-four months after CEHE submitted its change of ownership applications, the Department issued a press release along with a redacted version of the Decision denying CEHE's Colleges nonprofit status for Title IV regulatory purposes. See **Exhibit 13 (**August 11, 2016 Press Release Denying Request to Convert to Non-Profit Status ("Press Release")).

94. The second sentence of the Press Release clarified how this affected CEHE going forward: "The denial means that the colleges' programs must continue to meet requirements under the federal Gainful Employment regulations."

95. CEHE first learned of the Department's Decision through the Department's Press Release. **Exhibit 9**.

96. The Decision claims that the Colleges failed to meet the definition of a nonprofit institution set forth in 34 C.F.R. § 600.2.

97. The Department defines a "nonprofit institution" as an institution that is (i) "owned by one or more nonprofit corporations or associations, no part of the net earnings of which benefits any private shareholder or individual"; (ii) "legally authorized to operate as a nonprofit organization by each State in which it is physically located"; and (iii) "determined by the U.S. Internal Revenue Service to be an organization to which tax contributions are tax-deductible in accordance with section 503(c)(3) of the Internal Revenue Code." 34 C.F.R. § 600.2.

98. Alternatively, in a different subsection, the Department defines a nonprofit institution simply as any entity that "[i]s determined by the U.S. Internal Revenue Service to be an organization to which contributions are tax-deductible in accordance with section 501(c)(3) of the Internal Revenue Code." 34 C.F.R. § 600.2.

99. Under the HEA, a proprietary institution is by definition not "a public or other nonprofit institution." 20 U.S.C. § 1002 (b)(1)(C); 34 C.F.R. § 600.5(a)(1).

100. The Decision asserts, "[a] state authorization and IRS determination do not themselves confer nonprofit status for Title IV purposes." The Department stated further that it

"must make an independent determination that the institution is 'owned and operated by one or more nonprofit corporations or associations, no part of the net earnings of which benefits any private shareholders or individual.'"

101. The Department denied CEHE's application to participate in Title IV programs under its nonprofit status stating that it reached this conclusion based on this independent determination. The Decision argues that the Colleges failed to meet the definition of nonprofit institutions because the merger transaction "was structured" to benefit the former owner and because the former owner "retained control" over the Colleges as a member of CEHE and as "Board Chairman of CEHE's board."

102. The Department identified three particular findings supporting its Decision:

a. The financing for the merger transaction "results in financial benefit which inures to [the former owner]" of the Colleges;

b. The Colleges leased property owned by the former owner and "lease payments" "provide[d] additional economic benefit" to the former owner; and

c. The former owner "retained control" of the Colleges in his role as member of CEHE and as "Board Chairman of CEHE's Board."

See **Exhibit 9.**

103. The Decision also informed CEHE that the Colleges would have to be operated as proprietary institutions for Title IV regulatory purposes if the Colleges wanted to continue participating in Title IV programs. In other words, CEHE would have to "meet the. . . HEA reporting and program eligibility requirements applicable to for-profit institutions, including the 90/10 eligibility requirements. . . and the gainful employment program requirements. . . ."

104. The Department's Decision instructed CEHE to submit gainful employment certifications within three weeks notwithstanding the fact the Department was aware that the Colleges had already been operating as nonprofit institutions for almost four years.

105. As noted in its Press Release, the Department intended its Decision to send a "clear message" to other schools thinking of "converting to non-profit status" – "Don't waste your time."

106. The Department on August 11, 2016 issued the Decision. It established a ten-day deadline for CEHE to submit any request for reconsideration CEHE intended to make.

107. On August 12, 2016, CEHE asked the Department for an extension of the ten-day deadline to submit a request for reconsideration. CEHE made the request due to the significance of the issues, the uncertainty caused by the Decision, and concern about the impact on the Colleges' students and employees. While it took the Department almost four years to evaluate and respond to CEHE's applications for changes in ownership, CEHE only asked for a thirty-day extension. See **Exhibit 15** (August 12, 2016 Letter to Department Requesting Extension).

108. The Department denied CEHE's request for an extension on August 16, 2016, asserting that the 10-day period was sufficient to provide any additional factual information. See **Exhibit 16** (August 16, 2016 Denial of Request for Extension Re: Request for Reconsideration).

109. CEHE met the deadline by filing a Request for Reconsideration on August 21, 2016 with the Department ("Request for Reconsideration"). See **Exhibit 14**.

110. Since the Decision imposed an ultimatum that CEHE had to either sign Provisional Program Participation Agreements by August 31, 2016 to avoid losing the right to participate in Title IV programs, CEHE asked the Department to extend the deadline for

executing the Provisional Participation Agreements to September 30, 2016. See **Exhibit 17** (August 16, 2016 Letter to Department Requesting New Deadline to Sign PPAs). The request was also made to provide the Department with adequate time to carefully review and consider CEHE's request for reconsideration.

111. The Department denied CEHE's request on August 17, 2016. See **Exhibit 18** (August 17, 2016 Denial of Request for Extension of Time to Respond). The denial also reiterated the Department's contention that the Colleges' gainful employment certifications were past due. This assertion is further indicates the Department's improper motives and/or bad faith. CEHE had previously told the Department that, solely to preserve the Colleges' participation in Title IV programs, CEHE would submit the gainful employment certifications despite not being lawfully subject to them. CEHE then asked the Department to make its E-Apps accessible so CEHE could update its information including submitting the gainful employment certifications. Because the database is not accessible to CEHE without the Department's assistance, CEHE's E-Apps are technically still under review. The Department never responded to CEHE's requests seeking access to open the E-Apps. In any event, CEHE could not update the E-App to provide the gainful employment certifications because the Department refused to act.

112. Contrary to subsequent actions described below, the denial also promised that if a request for reconsideration was submitted, "the Department will review and consider that request." **Exhibit 18**.

113. In what may be an unprecedented action by the Department, on August 22, 2016, less than 24 hours after CEHE submitted a 17-page Request for Reconsideration that included over 90 pages of exhibits, the Department denied CEHE's Request for Reconsideration through a

press statement by its spokeswoman, Kelly Leon. She stated that the Department was "standing firmly behind its decision to deny" CEHE's applications seeking to the Colleges recognized as nonprofit institutions for purposes of Title IV programs. The Department's denial was also reported by media groups, such as *Politico*. The press statement was made even though CEHE has not received any communication in response to its Request for Reconsideration from the office that issued the Decision.

114. CEHE feels compelled by duress and the lack of a reasonable alternative to sign the PPAs proffered by the Department because of the catastrophic impact the Department's denial of access to Title IV programs would have on the students and employees at the Colleges, the economic damage CEHE would suffer, and in order to mitigate any such damages. CEHE intends to do so, under protest, by the deadline unilaterally imposed by the Department. Notwithstanding, CEHE is reserving all of its available legal rights and remedies. By signing the PPAs because of the Department's coercion, CEHE is not waiving any of its rights and expressly reserves all rights to pursue any remedies available to it so that the Colleges are properly recognized and granted status as nonprofit institutions having all rights to participate in Title IV programs, among any other remedies and damages.

G. The Department's Application Of Its Nonprofit Requirements Is Arbitrary And Capricious and Inconsistent with the Treatment of Similarly Situated Nonprofit Schools

115. The Department's three-part definition of a nonprofit institution in its regulations implements the definition of a nonprofit institution found in the HEA. The HEA defines a nonprofit institution as "a school. . . or institution owned and operated by one or more nonprofit

corporations or associations, no part of the net earnings of which inures, or may lawfully inure, to the benefit of any private shareholder or individual." 20 U.S.C. § 1003.

116. The private inurement prohibition contained in the HEA's definition of a nonprofit is essentially the same language included in the definition of a nonprofit under section 501(c)(3) of the IRC, which includes, in relevant part, that "no part of the net earnings of [the nonprofit corporation] inures to the benefit of any private shareholder or individual."

117. Indeed, before the HEA was adopted in 1965, the IRS had developed an interpretation of private inurement under section 501(c)(3) of the IRC. Congress intended this established meaning of the private inurement prohibition to control in the HEA.

118. At the time of the enactment of the HEA, federal courts had interpreted the private inurement prohibition of 501(c)(3) to permit tax-exempt nonprofit corporations to borrow money from an insider to purchase assets at fair market value and to repay the debt with revenue from the tax-exempt operations ("Transactional Exemption").

119. Federal courts have clarified that the Transactional Exemption applies to any transaction negotiated at arm's length with a person having no prior relationship with the exempt entity, regardless of the relative bargaining strength of the parties or the resultant control that the contract gives a party over the exempt entity.

120. The IRS formally adopted this position in Treasury Regulation 53.4958-4.

121. This regulation provides that the private inurement prohibition does not apply to fixed payments made pursuant to an initial contract, even if such payment would otherwise constitute an excess benefit transaction. See Treasury Regulation 53.4958-4(a)(3)(i) and (vii).

122. An initial contract is a binding written contract between an organization and an individual who was not an insider immediately prior to entering into the contract. See Treasury Regulation 53.4958-4(a)(3)(iii).

123. A fixed payment means an amount of cash or other property specified in an initial contract or determined by a fixed formula specified in the contract that is paid or transferred in exchange for the provision of specified services or property. See Treasury Regulation 53.4958-4(a)(3)(ii)(A).

124. A fixed formula may incorporate an amount that depends on future specified events or contingencies (e.g., revenues generated by activities of the organization) provided that no person exercise discretion when calculating the payment amount or in determining whether payment is made. These regulations permit the use of a cash-flow-based formula to determine the amount and timing of payments.

125. Prior to its Decision requiring that CEHE's Colleges be considered proprietary institutions, the Department had consistently interpreted 34 C.F.R. § 600.2 in accordance with the IRS' interpretation of private inurement when ruling on change of ownership applications following an institution's change to nonprofit status.

126. Upon information and belief, the Department has approved numerous change of ownership applications from formerly proprietary institutions seeking to participate in Title IV programs as nonprofit institutions following transactions in which the nonprofit buyer made cash-flow-based payments to the for-profit seller.

127. Indeed, on November 23, 2011, the Department approved the change in ownership application of Remington Colleges, Inc., a nonprofit corporation classified as a public

charity under section 170(b)(1)(A)(ii) of the IRC ("Remington"), to participate in Title IV programs as a nonprofit institution following its acquisition of schools previously owned by Education America, Inc., a for-profit corporation.

128. The Remington transaction was substantially similar to the CEHE transaction. Like the CEHE transaction, the Remington transaction was structured as an asset purchase in which the seller received payment in the form of promissory notes. The terms of the Remington note provided for payments based on Remington's future cash flow formula similar to the formula used to finance the CEHE transaction. Remington leased numerous buildings directly from the former owner or entities the former owner controlled. Remington's Board of Directors included the primary shareholder of the former owner of the educational institutions.

129. Moreover, like the CEHE transaction, the terms of the Remington transaction were submitted to the IRS as a part of Remington's application for designation as a tax exempt public charity under section 501(c)(3) of the IRC. The IRS issued a determination letter granting Remington tax-exempt status and classified Remington as a public charity. The IRS would not have issued the determination letter if the Remington's conversion transaction financing and lease contracts constituted a private benefit to the former owner.

130. The Department was aware of the terms of the Remington transaction when it approved Remington's change in ownership application.

131. In January 2012, the Department similarly approved the application of schools previously owned by Keiser School, Inc., a for-profit corporation, and acquired by Everglades Colleges, Inc., a nonprofit corporation classified as a public charity under section 170(b)(1)(A)(ii) of the IRC ("Everglades").

132. The Everglades transaction was structured as an asset purchase and donation with the seller receiving promissory notes as the form of payment.

133. Similar to the CEHE transaction, the terms of the Everglades note provide for payments based on Everglades' surplus earnings. The primary shareholder of the former owner in that transaction was the president of the nonprofit schools and a member of the board of trustees when the nonprofit submitted its change-in-control application. Moreover, like the CEHE transaction, Everglades' nonprofit schools leased property from entities owned in part by the former owner's primary shareholder.

134. More recently, in 2015, the Department approved the change-in-control application of previously for-profit schools acquired by UMA Education, Inc., a nonprofit corporation classified as a public charity under Section 170(b)(1)(A)(ii) of the IRC ("UMA"). UMA consummated the conversion transaction in March of 2015.

135. Like the CEHE transaction, the UMA transaction was structured so that the seller received promissory notes as the form of payment. The terms of the notes provide for payments of a fixed amount but delays payment until UMA's net current assets exceed certain specified thresholds based upon its cash flow. Like the cash flow notes CEHE issued, UMA is obligated to make note payments to the seller depending upon its cash flow. Furthermore, the executive officers of the seller in the UMA transaction became executive officers of UMA following the transaction.

136. Both before and after the CEHE transaction, the Department has applied the IRS private inurement principles and approved change of ownership applications and participation for nonprofit institutions using cash-flow formula based notes.

137. Congress has been fully aware of the Department's approval of these transactions and has taken no action to amend the HEA to require an interpretation of the private inurement principle inconsistent with the well-established IRS interpretation.

138. The Senate Committee on Health, Education, Labor and Pensions' report ("HELP report") on for-profit education has a section devoted to nonprofit conversion transaction. It specifically mentions the Everglades and Remington transactions. The HELP report notes that the transactions were accomplished using contingent note payments and that the sellers remained involved after the transactions and nonprofit conversions. Notwithstanding this report, Congress took no action to amend the HEA to reverse these longstanding interpretations of 20 U.S.C. § 1003 in order to preclude transactions involving promissory note payments based upon a nonprofit's cash flow.

139. Although the HEA has been amended on numerous occasions, the definition of a nonprofit institution (20 U.S.C. § 1003) has remained unchanged since the initial Higher Education Act of 1965.

140. Moreover, the Department continued after the issuance of the HELP report to apply its private benefit prohibition consistent with the longstanding IRS interpretation when approving applications following for-profit to nonprofit conversion transactions.

141. In requiring CEHE's Colleges to be proprietary for Title IV purposes, the Department reversed its long-standing position and abandoned its prior practice of applying 34 C.F.R. § 600.2 consistent with the IRS private inurement principles. Moreover, this determination came years after CEHE submitted the applications.

142. The Department's profit distribution theory reflected in the Decision ignores how the seller promissory notes are treated under GAAP. The debt is classified as long-term debt. Long-term debt is a liability on a nonprofit's statement of financial position (a nonprofit's balance sheet equivalent). The payments due on the debt are classified as expenses on a nonprofit's statement of activities (a nonprofit's income statement equivalent). Under GAAP's nonprofit accounting standards, nonprofits do not have net earnings but have a net change in assets. The net change in assets is determined after accounting for the seller note payments in the same manner as all other indebtedness of a nonprofit. The audited financial statement submitted to the Department reflects the "above the net change in assets line" treatment of the payment of interest and principal and related accruals relating to the seller note.

143. The determination of the payment amount owed on the seller promissory notes in the CEHE transaction being tied to cash flow does not convert the obligation to one to be paid from net earnings under any definition of net earnings or net change in assets under GAAP standards or otherwise. The Department's conclusion that the payment amount determination formula contained in the promissory notes in the CEHE transaction is the same as a distribution of net change in assets or profits is incorrect and ignores applicable accounting principles.

144. The term "net earnings" is not ambiguous. It has had the well-established and commonly understood meaning contained in GAAP for decades. Congress intended for net earnings to have that meaning when it adopted the HEA. The Department's interpretation of net earnings as reflected in its Decision directly contravenes precedent and Congressional intent.

COUNT I
(Declaratory Judgment Action)

145. Plaintiff incorporates the preceding paragraphs as if they were fully set forth herein.

146. The Colleges are nonprofit institutions as defined in the Department's regulations.

147. Both the HEA and the Department's regulations define nonprofit institutions and proprietary institutions in a mutually exclusive manner.

148. As a matter of law, the Colleges became nonprofit institutions of higher education on the date of the merger.

149. Because the Colleges meet the Department's definition of a nonprofit institution of higher education, the Department acted arbitrarily and capriciously in concluding that the Colleges are proprietary institutions of higher education, which is a decision contrary to the HEA and the Department's regulations.

150. An actual and justiciable controversy has arisen between the parties regarding the Department's regulations concerning the definition of a nonprofit institution and the Department erred in concluding that the Colleges are proprietary institutions of higher education.

151. There is no adequate remedy by which these controversies may be resolved other than the relief requested herein.

152. Plaintiff is therefore entitled, pursuant to Rule 57 of the Federal Rules of Civil Procedure, to a declaratory judgment order from this Court declaring that the Colleges are nonprofit institutions for purposes of Title IV programs and entitled to be regulated as nonprofit institutions commencing on the date of the change in ownership.

COUNT II
(Administrative Procedure Act)

153. Plaintiff incorporates the preceding paragraphs as if they were fully set forth herein.

154. The Department's Decision denying CEHE's change in ownership applications to participate in Title IV programs as a nonprofit institution is arbitrary and capricious, and Plaintiff is therefore entitled to have the decision vacated and set aside pursuant to 5 U.S.C. § 706.

155. The Department's Decision disregards clear Congressional intent expressed in the HEA to the extent it interprets 34 C.F.R. § 600.2's "private benefit" principle to disqualify a section 501(c)(3) nonprofit corporation from being a nonprofit institution of higher education under the HEA because it has purchase money indebtedness with payment amounts based upon a cash-flow formula.

156. Moreover, the Department's decision is arbitrary and capricious because the Decision reverses the Department's prior interpretation of 34 C.F.R. § 600.2 without providing a reasoned explanation for this change.

157. The Department failed to engage in reasoned decision-making and arbitrarily and capriciously treated CEHE differently than similarly situated institutions whose applications the Department approved.

158. The facts alleged above and the numerous political activities by the Department described in **Exhibit 14** highlight the Department's extremely improper series of actions during the extraordinarily long time it was considering CEHE's change of ownership applications. The actions by the Department evidence a politicization of the change in ownership process intended to achieve a political agenda and in contravention of its duty to act impartially, fairly, and within

the confines of recognized law and precedent. The Department's Decision refusing to recognize CEHE as a nonprofit educational institution denies CEHE the associated rights and protections to which it is entitled as a matter of law and it is arbitrary, capricious, and violates the APA.

159. The actions by the Department are part of its concerted effort to deny CEHE and its Colleges regulatory status permitted by the HEA and likewise deny them the ability to survive and operate as nonprofit educational institutions for the public good.

160. Plaintiff is, therefore, entitled to an order and judgment from this Court declaring that the Department's August 11, 2016 letter Decision is not in accordance with law and is arbitrary and capricious within the meaning of 5 U.S.C. § 706, and ordering the Department to hold that the Colleges are nonprofit educational institutions for all purposes.

COUNT III
(Equitable Estoppel)

161. Plaintiff incorporates the preceding paragraphs as if they were fully set forth herein.

162. Upon the completion of the merger, the Department affirmatively informed CEHE that it would be required to comply with the 90/10 requirement imposed on for-profit institutions only during the 2013 fiscal year.

163. The Department did not require CEHE or the Colleges to comply with any other HEA regulations generally applicable only to proprietary institutions at any time prior to March 15, 2016.

164. Moreover, following the merger, the Department-run College Scorecard, College Navigator, and Integrated Postsecondary Education Data System websites conspicuously identified CEHE as a nonprofit institution for Title IV purposes.

165. CEHE reasonably relied upon the Department's pre-acquisition review response not identifying any special conditions other than its imposition of a single proprietary requirement (i.e., compliance with 90/10 during the 2013 fiscal year) when proceeding to close the transaction.

166. CEHE complied with the 90/10 rule for the 2013 fiscal year. Since the merger, CEHE operated the Colleges in compliance with the Department's nonprofit regulations.

167. This includes, among other compliance requirements, CEHE's preparation of financial statements and audits in fiscal years 2013, 2014, and 2015, which were prepared in accordance with the Department's standards for nonprofit institutions.

168. The Department accepted each of CEHE's annual financial audits. Each financial audit conspicuously identified CEHE's nonprofit status and the Colleges as nonprofit institutions.

169. CEHE's 2013 annual financial audit reported its composite score *using the nonprofit ratios*.

170. CEHE's composite score would have been higher if prepared under the Department's standards for proprietary institutions. Similarly, the score would have been higher if the seller notes had been classified in a manner consistent with the Department's position in its Decision that the seller note payments are distributions of net earnings and not indebtedness.

171. The Department specifically reviewed CEHE's 2013 annual financial audit and imposed significant additional financial requirements on CEHE based on its composite score as determined under the applicable nonprofit ratios.

172. On January 26, 2015, the Department cited CEHE's composite score in demanding that CEHE post an LOC for $71,600,000 if it wanted to continue participating in Title IV programs.

173. The Department knew at the time it made the demand that CEHE considered itself a nonprofit institution and that it operated in accordance with the related nonprofit requirements. By that date, the Department had already received CEHE's 2013 fiscal year financial audit, which was prepared under the Department's nonprofit standards.

174. The Department's position that the seller notes are a form of equity providing for distributions of net earnings or profits as opposed to classifying them as indebtedness is contrary to its interpretations of CEHE's audited financial statements. For example, the Department relied on those audited financial statements to impose a $42,996,000 escrow deposit requirement.

175. The Department first notified CEHE on March 15, 2016 that it still considered CEHE a proprietary institution for Title IV program purposes. It was not until August 11, 2016, that the Department denied CEHE's application to participate in Title IV programs as a nonprofit institution of higher education.

176. The Department's affirmative acts at all times prior to March 15, 2016 were consistent with its recognition that the Colleges had nonprofit status and that they would be regulated as nonprofit institutions under the HEA.

177. CEHE relied upon the Department's regulations in operating the Colleges as nonprofits while the Department considered its applications for almost four years. By operating the Colleges consistent with the Department's regulations applicable to nonprofits, CEHE reasonably relied on the Department's communications and actions to conclude that it was not

considered for-profit institutions and subject to such related regulations. As a result of the arbitrary and capricious Decision, the Colleges' continued eligibility to participate in the Title IV programs is in immediate jeopardy. The Colleges will suffer irreparable and significant damage if the Colleges are required to comply with the Department's for-profit regulations.

178. Plaintiff is, therefore, entitled to an order and judgment from this Court estopping the Department from denying CEHE's nonprofit status and classifying CEHE as a proprietary institution for purposes of the HEA and Title IV programs.

COUNT IV
(Judicial Estoppel)

179. Plaintiff incorporates the preceding paragraphs as if they were fully set forth herein.

180. On May 2, 2014, the United States intervened in a False Claims Act *qui tam* action against Stevens-Henager College and CEHE (as the owner of or the successor in interest to Stevens-Henager College), alleging that Stevens-Henager College knowingly made false certifications regarding its compliance with the requirements of Title IV of the HEA in its 2007 and 2010 PPAs.

181. In its complaint in intervention, the Government alleged that CEHE is an Indiana nonprofit corporation and that CEHE became the owner of the Colleges on December 31, 2012.

182. In doing so, the Government correctly acknowledged that CEHE owns and operates the Colleges as nonprofit institutions.

183. On March 30, 2016, prior to the filing of an answer, the District Court for the District of Utah entered an order ruling on a motion to dismiss the complaint in intervention in which the Court adopted the Government's allegation that the Colleges merged into an Indiana

nonprofit corporation, CEHE, on December 31, 2012, and that CEHE *operates* the schools as a result of the merger. See ECF Doc. 245, United States District Court of Utah, Central Division.

184. Plaintiff is, therefore, entitled to an order from this Court estopping the Department from asserting that the Colleges' former owner "retains control" over the Colleges, an assertion that is contrary to the position taken by the United States in earlier litigation instigated against CEHE.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff demands judgment as follows:

1. Under the First Cause of Action, an order and judgment declaring that the Colleges are nonprofit institutions for purpose of Title IV programs and therefore entitled to be regulated as nonprofit institutions commencing with the date of the change in ownership;

2. Under the Second Cause of Action, an order and judgment declaring that the Department's August 11, 2016 letter Decision is not in accordance with law and is arbitrary and capricious within the meaning of 5 U.S.C. § 706, and ordering the Department to hold that the Colleges are nonprofit educational institutions for all purposes;

3. Under the Third Cause of Action, an order and judgment estopping the Department from denying CEHE's nonprofit status and classifying CEHE as a proprietary institution for purposes of the HEA and Title IV programs;

4. Under the Fourth Cause of Action, an order and judgment from this Court estopping the Department from asserting that the Colleges' former owner "retains control" over the Colleges, an assertion that is contrary to the position taken by the United States in earlier litigation instigated against CEHE;

5. Attorneys' fees and costs; and

6. Any other relief that the Court deems just and equitable.

JURY DEMAND

Pursuant to Rule 38, Federal Rules of Civil Procedure, Plaintiff hereby demands a trial by jury of all issues so triable.

Dated this August 30, 2016:

Respectfully submitted,

SNELL & WILMER L.L.P.

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EXHIBIT LIST TO CEHE COMPLAINT

1. September 4, 2007 IRS 501(c)(3) Determination Letter;
2. Affidavit of John S. Mercer;
3. February 27, 2013 Post-Merger Request Letter to IRS (without referenced exhibits);
4. July 25, 2014 IRS Letter Updating Charity Status;
5. October 2, 2012 Pre-Acquisition Review Request Letter;
6. November 2, 2012 Response to Pre-Acquisition Review Request Letter;
7. December 20, 2012 Pre-Acquisition Review Letter from Department;
8. January 26, 2015 Department Letter Demanding 50% Letter of Credit;
9. August 11, 2016 Department Decision on Change of Ownership (Redacted);
10. March 15, 2016 Department Initial Notice Letter;
11. August 29, 2015 Department Electronic Mail re: Gainful Employment;
12. April 20, 2016 Letter to Department;
13. August 11, 2016 Press Release Denying Request to Convert to Non-Profit Status;
14. August 21, 2016 Request for Reconsideration;
15. August 12, 2016 Letter to Department Requesting Extension;
16. August 16, 2016 Denial of Request for Extension Re: Request for Reconsideration;
17. August 16, 2016 Letter to Department Requesting New Deadline to Sign PPAs; and
18. August 17, 2016 Denial of Request for Extension of Time to Respond.