

**BEFORE THE
DEPARTMENT OF CONSUMER AFFAIRS
FOR THE BUREAU FOR PRIVATE POSTSECONDARY EDUCATION
STATE OF CALIFORNIA**

In the Matter of the Statement of Issues Against:

EL PORTAL COLLEGE,
Rose Padilla, 51% owner,
John Hague, 49% owner

Institution Code No. 24179339

Respondent.

Case No. 998688

OAH No. 2013060468

DECISION AND ORDER

The attached Proposed Decision of the Administrative Law Judge is hereby adopted by the Director of the Department of Consumer Affairs as its Decision in the above-entitled matter, except that pursuant to Government Code Section 11517(c)(2)(C), the Decision is hereby modified for technical reasons as follows:

1. Paragraph 1 of the FACTUAL FINDINGS on page 2, shall read as follows:
“Joanne Wenzel (Complainant) filed the First Amended Statement of Issues, Case number 998688, in her official capacity as the Deputy Chief of the Bureau for Private Postsecondary Education, Department of Consumer Affairs.”
2. Paragraph 12 of the FACTUAL FINDINGS on page 3 shall refer to “California Code of Regulations, title 5, section 71745, subdivision (a)(6).”
3. Paragraph 1 of the ORDER on page 8 is deleted, and the ORDER shall read as follows:

“Given the foregoing, the Application for Approval to Operate El Portal College, a non-accredited institution, filed by Rose Padilla, 51% owner, and John Hague, 49% owner, is GRANTED, and the Approval to Operate shall be issued.”

The proposed decision of the Administrative Law Judge is not otherwise amended, modified, or altered.

This Decision shall become effective OCT 17 2014.

IT IS SO ORDERED: SEP 17 2014



DOREATHEA JOHNSON
DEPUTY DIRECTOR OF LEGAL AFFAIRS
DEPARTMENT OF CONSUMER AFFAIRS
STATE OF CALIFORNIA

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Statement of Issues Against:

EL PORTAL COLLEGE,
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JOHN HAUGE, 49% OWNER

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Respondent.

Case No. 998688

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PROPOSED DECISION

Administrative Law Judge Vallera J. Johnson, State of California, Office of Administrative Hearings, heard this matter in San Diego, California, on June 17, 2014.

Marichelle S. Tahimic, Deputy Attorney General, represented Complainant Joanne Wenzel, Deputy Bureau Chief of the Bureau for Postsecondary Education, Department of Consumer Affairs.

John Hauge represented Respondent El Portal College, Rose Padilla, 51% owner, and John Hauge, 49% owner.

The matter was submitted on June 27, 2014.¹

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¹ The hearing concluded on June 17, 2014. The record remained open for receipt of additional documentary evidence from Respondent. On June 18, 2014, Respondent submitted financial statements that included a statement that the entity is able to pay operating expenses that are due within 30 days, marked Exhibit B. On June 23, 2014, Respondent filed revised financial statements, marked Exhibit C. Without objection by Complainant, Exhibits B and C were admitted. On June 27, 2014, the record was closed, and the matter was submitted.

FACTUAL FINDINGS

1. Joanna Wenzel (Complainant) filed the First Amended Statement of Issues, Case number 998688, in her official capacity as the Deputy Bureau Chief of the Bureau for Private Postsecondary Education, Department of Consumer Services.

In the First Amended Statement of Issues, Complainant seeks to deny the Application for Approval to Operate a Non-Accredited Institution of El Portal College, Rose Padilla, 51% owner, and John Hauge, 49% owner (Respondent), on grounds that Respondent did not file financial statements that complied with Education Code section 94887 and California Code of Regulations, title 5, sections 71240, 71745, and 74115, subdivision (b)(1).

Respondent filed a timely Notice of Defense, requesting a hearing in this matter.

2. On November 30, 2011, the Bureau received Respondent's Application for Approval to Operate a Non-Accredited Institution (Application #24171). Respondent's packet included the Bureau's application, corporate documents, educational documents and financial statements.²

On January 26, 2012, Bureau staff notified Respondent of deficiencies in Application #24171. The financial statements did not comply with California Code of Regulations, title 5, section 71745, in that there was no statement by Respondent's certified public accountant (CPA) that the financial statements had been audited or reviewed in accordance with generally accepted accounting principles (GAAP); further, the letter from Jack T. Ferguson, Respondent's CPA, stated "These statements were prepared from information provided by the client, and as such, no reliance should be placed upon them."

3. By letter, dated March 20, 2012, the Bureau notified Respondent that a Provisional Approval to Operate was granted, effective March 20, 2012, through September 20, 2012, on the condition that Respondent submit financial statements in compliance with California Code of Regulations, title 5, section 71745, before September 20, 2012. Upon compliance, the Bureau would issue a full approval to operate. However, if Respondent did not comply in a timely manner, the Provisional Approval to Operate would be revoked.

4. By email, dated September 12, 2012, Respondent's office manager forwarded a "Profit & Loss" statement for the institution to the Bureau. By email, dated September 13, 2012, the Bureau notified Respondent's office manager that the "Profit & Loss" statement did not comply with the Bureau's regulations regarding financial statements and provided Respondent with a copy of the appropriate regulation.

5. On September 28, 2012, Respondent requested a two-month extension to submit financial statements.

² Financial statements include a balance sheet, income statement, statement of cash flow, and accompanying footnotes.

On October 8, 2012, the Bureau granted the requested extension until November 20, 2012.

6. By email, dated November 23, 2012, Derek Thomas, Respondent's CPA, provided reviewed financial statements for the year ending 2011 to the Bureau "in accordance with the income tax basis of accounting."

7. On December 19, 2012, the Bureau denied Application #24171 because the reviewed financial statements used "an income tax basis of accounting;" as such, the financial statements were not in compliance with the requirement for audited or reviewed financial statements prepared in accordance with GAAP.

8. On February 5, 2013, Respondent submitted another set of financial statements, reviewed by Thomas, to the Bureau. The financial statements continued to be deficient in that there was insufficient information in the financial statements to ascertain whether Respondent had the ability to pay all operating expenses within 30 days.

For the year ending 2011, there was \$8,541 cash available to pay expenses. However Respondent's annual expenses exceeded \$160,000. There was no information about when teaching services were provided or when funds would be available from the federal, state, and county governments to pay Respondent's expenses.

9. Each party called an expert witness, a CPA licensed to practice in the State of California for more than 30 years. Barry A. Franzen (Franzen) evaluated the financial statements submitted by Respondent and testified on behalf of Complainant. Thomas prepared Respondent's last two sets of financial statements based on documentation provided by Respondent and testified as Respondent's expert witness. Each expert demonstrated that he was knowledgeable about GAAP and the distinction between preparing financial statements in accordance with GAAP and the income tax basis of accounting. There was no dispute that each was qualified and competent to testify as an expert witness.

10. Complainant's expert witness explained that there was insufficient information in Respondent's financial statements to ascertain whether Respondent could pay its expenses within 30 days; he needed to understand the institution's cash flow; from the documentation provided, he did not understand when revenues came in or expenses were due and payable.

11. Thomas prepared the financial statements for the year ending 2011 in accordance with GAAP.³

12. Thomas established that, for year ending December 31, 2011, Respondent's current assets to current liabilities ratio exceeded 1.25, the ratio required by California Code of Regulations, title 5, section 7145, subdivision (a)(6). He explained that in order to determine a ratio, current assets are divided by current liabilities. Generally speaking, the

³ Exhibit 11

higher the ratio, the more liquid the company is, and therefore its ability to pay its debt. For the year ending December 31, 2011, according to its balance sheet, Respondent had current assets of \$8,541 and current liabilities of \$824. As such, its ratio was 10.

Respondent provided a document prepared by its office manager that demonstrated that Respondent had sufficient cash flow to pay its bills within 30 days during 2011 and 2012.⁴

Based on financial information provided by Respondent, Thomas demonstrated that the ratio of assets to liabilities is 10 and that, based on the information contained in Exhibit A, for the year ending 2011, Respondent was able to pay its operating expenses within 30 days.

13. Respondent's office manager prepared a document, marked and admitted as Exhibit A. This document established that during 2011 and 2012, Respondent paid its expenses within 30 days.

14. In Thomas' opinion, it was inappropriate for an independent CPA to prepare financial statements in accordance with GAAP that demonstrated that the institution could pay its expenses within 30 days. He testified "that, as an independent accountant, it would be inappropriate for him to state that the institution could pay its expenses within 30 days; it would be another engagement." In other words, Thomas would be retained as a CPA to gather and verify information, as Respondent's office manager did.

15. Thomas was not familiar with Bureau regulations that govern preparation of financial statements.

16. In response, Complainant's expert witness explained that financial statements belong to Respondent, not the CPA. As such, Respondent could include a footnote in the financial statements that states that Respondent paid its expenses within 30 days. The CPA could review the financial statements and all other appropriate documents to sign off on the financial statements.

17. There was no evidence that Respondent intentionally failed to file financial statements in compliance with the Bureau's regulations. Respondent did not file financial statements in compliance with Bureau's requirements because neither Respondent nor its CPA understood how to bring the financial statements into compliance. John Hague represented that Respondent was willing to include the footnote described by Franzen; Thomas stated that, based on an appropriate review, he would sign off on these financial statements. Without objection by Complainant, the administrative law judge allowed Respondent to file said financial statements subsequent to the hearing, with leave for Complainant to make any objection.

⁴

Exhibit A

18. On June 18, 2014, Respondent filed financial statements for the year ending 2011 and an attached letter from Thomas, the CPA.⁵ Contained within the financial statements is Footnote C, which states: "Pursuant to the requirement of California Code of Regulations Section 71745, the organization paid all operating expenses within 30 days."

19. On June 23, 2014, Respondent filed revised financial statements for the year ending 2011 and an attached letter from its CPA. There is no difference between the initial and revised financial statements.⁶

20. Complainant had an opportunity to review the financial statements submitted subsequent to the hearing and made no objection.

LEGAL CONCLUSIONS

1. Education Code section 94886 states:

Except as exempted in Article 4 (commencing with section 94874) or in compliance with the transition provisions in Article 2 (commencing with Section 94802), a person shall not open, conduct, or do business as a private postsecondary educational institution in this state without obtaining an approval to operate under this chapter.

2. Education Code section 94887 states:

An approval to operate shall be granted only after an applicant has presented sufficient evidence to the bureau, and the bureau has independently verified the information provided by the applicant through site visits or other methods deemed appropriate by the bureau, that the applicant has the capacity to satisfy the minimum operating standards. The bureau shall deny an application for an approval to operate if the application does not satisfy those standards.

3. California Code of Regulations, title 5, section 71100 states:

(a) An applicant seeking approval to operate pursuant to Section 94886 of the Code, other than Approval to operate by Accreditation pursuant to Section 94890(a)(1) of the Code, shall complete the "Application for Approval to Operate for an Institution Not Accredited," Form Application 94886 (rev.

⁵ Exhibit B

⁶ Exhibits A and B

2/10). An applicant seeking approval to operate by accreditation pursuant to Section 94890(a)(1) of the Code shall comply with section 71390.

(b) An applicant shall submit the completed form, the information or documentation required by this Article, the appropriate application fee as provided in Section 94930.5(a)(1) of the Code, and any appropriate annual fee as required by Article 1 of Chapter 5 of this Division, to the Bureau.

(c) An application that fails to contain all of the information required by this article shall render it incomplete.

4. California Code of Regulations, title 5, section 71745 states:

(a) The institution shall document that it has at all times sufficient assets and financial resources to do all of the following:

(1) Provide all of the educational programs that the institution represented it would provide.

(2) Ensure that all students admitted to its educational programs have a reasonable opportunity to complete the programs and obtain their degrees or diplomas.

(3) Maintain the minimum standards required by the Act and this chapter.

(4) Pay timely refunds as required by Article 13 of the Act.

(5) Pay all operating expenses due within 30 days.

(6) Maintain a ratio of current assets to current liabilities of 1.25 to 1.00 or greater at the end of the most recent fiscal year when using generally accepted accounting principles, or for an institution participating in Title IV of the federal Higher Education Act of 1965, meet the composite score requirements of the U.S. Department of Education. For the purposes of this section, current assets does not include:

intangible assets, including goodwill, going concern value, organization expense, startup costs, long-term prepayment of deferred charges, and non-returnable deposits, or state or federal grant or loan funds that are not the property of the institution but are held for future disbursement for the benefit of students. Unearned tuition shall be accounted for in accordance with general accepted accounting principles.

[¶] . . . [¶]

(c) An institution shall provide to the Bureau its most current financial statements upon request.

5. California Code of Regulations, title 5, section 71240 states:

(a) The Form Application 94886 shall contain a statement that the institution has and can maintain the financial resources required pursuant to section 71745.

(b) The institution shall submit current, reviewed financial statements at the time it applies for approval to operate. Each set of financial statements shall comply with Section 74115 of this chapter.

6. California Code of Regulations, title 5, section 74115 states:

(a) This section applies to every set of financial statements required to be prepared or filed by this Act or by this chapter.

(b) A set of financial statements shall contain, at a minimum, a balance sheet, an income statement, and a cash flow statement, and the preparation of financial statements, shall comply with all of the following:

(1) Audited and reviewed financial statements shall be conducted and prepared in accordance with the generally accepted accounting principles established by the American Institute of Certified Public Accountants by an independent certified public accountant who is not an employee, officer, or corporate director or member of the governing board of the institution.

[¶] . . . [¶]

(3) The financial statements shall establish that the institution meets the requirements for financial resources required by Section 71745.

[¶] . . . [¶]

(5) Any audits shall demonstrate that the accountant obtained an understanding of the institution's internal financial control structure, assessed any risks, and has reported any material deficiencies in the internal controls.

[¶] . . . [¶]

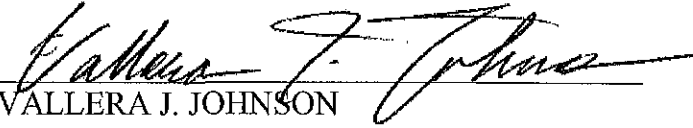
7. The Bureau denied Application #24171 because the financial statements were not filed in accordance with Bureau requirements. Respondent's financial statements were deficient because Respondent's CPA was not aware of the Bureau's regulations governing financial requirements or what needed to be done in order to comply. During the hearing, he gained an understanding of the Bureau's regulations and expectations regarding the financial statements. On June 18, 2014, Respondent filed revised financial statements that complied with California Code of Regulations, title 5, section 71745. As such, it is appropriate to grant Application # 24171 at this time.

ORDER

1. The request of Joanne Wenzel, Deputy Bureau Chief of the Bureau for Private Postsecondary Education (that the Director of the Department of Consumer Affairs deny the application of Rose Padilla, 51% owner, and John Hauge, 49% owner, El Portal College) is denied.

2. The Application for Approval to Operate El Portal College, a non-accredited institution, from Rose Padilla, 51% owner, and John Hauge, 49% owner, is granted.

DATED: July 29, 2014


VALLERA J. JOHNSON
Administrative Law Judge
Office of Administrative Hearings