

CALIFORNIA DEPARTMENT OF JUSTICE

TITLE 11. LAW

DIVISION 1. ATTORNEY GENERAL

**CHAPTER 10. BUREAU FOR PRIVATE AND POSTSECONDARY EDUCATION
EXEMPTION VERIFICATION**

INITIAL STATEMENT OF REASONS

PROBLEM STATEMENT

Effective January 1, 2022, the Bureau for Private Postsecondary Education (the “Bureau”) within the Department of Consumer Affairs is prohibited from verifying the exemption of, or contracting to handle complaints for, a nonprofit institution that operated as a for-profit institution during any period on or after January 1, 2010, unless the Attorney General has first verified specified information regarding the nonprofit institution. (Ed. Code, § 94874.1, subd. (a).)¹ The Attorney General must provide written notification to the nonprofit institution and the Bureau of the Attorney General’s verification within 90 days of receipt of all information the Attorney General determines is necessary for the verification. (*Id.*, subd. (d).)

The proposed regulation creates a procedure for the Attorney General to verify the information specified in section 94874.1. On a prescribed form, the institution will be required to provide the effective date the for-profit institution became a nonprofit, a full description of the transaction converting the institution from for-profit to nonprofit status, including all agreements entered into between the nonprofit institution and the for-profit institution, all related financial information, and a statement from the nonprofit institution’s board of directors as to why they believe the transaction is or was necessary or desirable. Further, the institution will be required to answer:

- Whether the nonprofit institution acquired the for-profit institution’s assets for no more than the fair value of the assets.
- Whether the nonprofit institution executed agreements for goods or services for no more than the fair value of the goods or services.
- Whether all core functions of the nonprofit institution are conducted by, or under the direction of, the nonprofit institution.
- Whether the nonprofit institution entered into any contracts, loans, or leases with a term longer than three years with the former for-profit institution’s owners and managers.

BENEFITS ANTICIPATED FROM REGULATORY ACTION

The California Private Postsecondary Education Act of 2009 (the “Act”) (§ 94800 et seq.) provides for the regulation of private postsecondary educational institutions by the Bureau. The

¹ All references are to the Education Code unless otherwise indicated.

Act applies to private entities with a physical presence in the state that offer postsecondary education, but certain institutions are exempt from the Act. (§ 94874.)

Under section 94874.1, subdivision (a), which became effective January 1, 2022, the Bureau is prohibited from verifying the exemption of, or contracting to handle complaints for, a nonprofit institution that operated as a for-profit institution during any period on or after January 1, 2010, unless the Attorney General first verifies specified information listed in the statute. The proposed regulation creates the procedure for the Attorney General to verify the information required by section 94874.1.

Private postsecondary schools complement the public education system by helping develop a trained workforce to meet the demands of California businesses and the economy. However, concerns about the value of degrees and diplomas issued by private postsecondary schools, and the lack of protections for students and consumers of the services provided by the private postsecondary schools, highlight the need for strong state-level oversight of private postsecondary schools. (§ 94801, subd. (b).) The proposed regulation promotes this need for state-level oversight by the Department of Justice, Office of the Attorney General, of those nonprofit institutions that previously operated as a for-profit institution.

SPECIFIC PURPOSE AND NECESSITY OF EACH SECTION

Subdivision (a) requires the nonprofit institution to request verification by submitting the “Application for Verification,” Form CT-SCHOOL-1. Requiring submission on the prescribed form ensures that the institution provides all required information to the Attorney General.

Subdivision (b) requires the nonprofit institution’s president, chief executive officer, treasurer, or chief financial officer to sign the Application for Verification, Form CT-SCHOOL-1, under penalty of perjury. The necessity for a signature under penalty of perjury by a high-level officer of the institution is to impress upon applicants the seriousness and importance of signing the form, to attest to the accuracy and completeness of the information submitted, and to deter misrepresentations and submission of false information.

Subdivisions (b)(1) through (b)(5) require the applicant to provide information identifying the institution and contact person for the application. This information is necessary so that the Attorney General can verify the information required to be evaluated under section 94874.1, subdivision (a), and contact the institution if additional information is required.

Subdivision (b)(6)(A) requires the institution to provide the effective date and a full description of the transaction converting the institution from for-profit to nonprofit status, including all agreements entered into between the nonprofit institution and the for-profit institution, all related financial information, and a statement from the nonprofit institution’s board of directors as to why they believe the transaction is or was necessary or desirable. This information is necessary to evaluate the overall legitimacy of the transaction that converted a for-profit institution into a nonprofit institution.

Subdivision (b)(6)(B) requires the institution to answer whether it acquired the for-profit institution's assets for no more than the fair value of the assets. This information is necessary to verify that the transaction was an arms-length and a fair transaction for the nonprofit institution. Section 94874.1, subdivision (a)(1), requires the Attorney General to verify this information, and requires "fair value" to be demonstrated through one of the following: (1) a third-party appraisal based on comparable assets acquired by, or goods or services procured by, nonprofit corporations in similar market conditions; (2) independent financing of the acquisition or procurement based upon the asset acquired or goods or services procured; or (3) full and open competition in the acquisition of the assets or procurement of the goods or services. (§ 94874.1, subd. (c).)

If the applicant answers the question in subdivision (b)(6)(B) in the affirmative, subdivision (b)(6)(C) requires the institution to answer whether it executed agreements for goods or services for no more than the fair value of the goods or services. This information is necessary to verify whether the institution entered into agreements for goods or services with the for-profit institution and whether the transactions were arms-length and fair to the nonprofit institution. Section 94874.1, subdivision (a)(2), requires the Attorney General to verify this information.

If the applicant answers the questions in subdivisions (b)(6)(B) and (C) in the affirmative, subdivision (b)(6)(D) requires the institution to answer whether all of its core functions are conducted by, or under the direction of, the nonprofit institution. Section 94874.1, subdivision (a)(3), requires the Attorney General to verify this information to ensure that the nonprofit institution, and not the for-profit institution, is carrying on the core functions of the institution. Section 94874.1, however, does not define "core functions." The regulation defines "core functions" to mean control of student instruction; academic research and public service; curriculum development and management and development of instructional personnel; institutional support including management and planning; student recruitment and marketing; and faculty recruitment and retention. In determining the core functions of a postsecondary educational institution, the Department accepted input from stakeholders and considered and reviewed the major functions of institutions of higher education described by the National Center for Educational Statistics.

If the applicant answers the questions in subdivisions (b)(6)(B), (C) and (D) in the affirmative, subdivision (b)(6)(E) requires the institution to answer whether it entered into any contracts, loans, or leases with a term longer than three years with the former for-profit institution's owners and managers. This information is necessary to verify the legitimacy and fairness of contracts, loans, or leases to the nonprofit institution. Section 94874.1, subdivision (a)(4), requires the Attorney General to verify this information unless the nonprofit is owned by or controlled by a public institution of higher learning.

Subdivision (c) requires the nonprofit institution to submit additional information if necessary for the Attorney General to complete an evaluation of the Application for Verification. Some for-profit colleges used complicated financial schemes and shell corporations to wrongfully claim nonprofit status without adopting the restrictions that actually protect students. After reviewing the submitted documents, the Attorney General may need to review additional information to

complete the evaluation and ensure that the institution has not deceptively claimed nonprofit status to attract students and escape regulatory oversight by the Bureau.

Subdivision (d) explains that the Application for Verification will not be deemed received under section 94874.1, subdivision (d), until the Attorney General has received all the information the Attorney General determines is necessary for the required verification, including, all information required by the Application for Verification, and all additional information requested by the Attorney General. This requirement is necessary to ensure that the Attorney General has sufficient time and information to thoroughly evaluate the Application for Verification.

Subdivision (e) requires the institution to designate any information submitted as confidential and provide a detailed explanation supporting the request for confidentiality. Public access to information promotes transparency and accountability to the public. Placing the burden on the institution motivates the institution to carefully consider and explain whether the information is confidential or a trade secret, which saves time and resources during the Attorney General's review of information deemed confidential.

Subdivision (e) also requires the institution to provide a redacted copy of the information believed to be confidential. This is necessary so the public can access the redacted copy if the Attorney General determines the information is truly confidential and not subject to public disclosure.

Subdivision (f) requires the institution to submit the completed Application for Verification by uploading it on the Department's website and mailing one hard copy or one electronic copy to the Attorney General's Office. This is necessary to ensure that the Application is properly received. It is not uncommon for computer upload and download failures to occur. Providing a copy of the Application for Verification by mail will ensure that the application is received.

ECONOMIC IMPACT ASSESSMENT/ANALYSIS

The Department concludes:

(1) It is unlikely that the proposal will create or eliminate jobs within the state because the proposed regulation prescribes the procedure for the Attorney General to verify an institution's nonprofit status. Although an applicant may need the services of a third-party appraiser to establish "fair value," the Department anticipates that, annually, not more than one applicant will request verification of its nonprofit status from the Attorney General. This infrequent verification process will not likely create new appraiser jobs within the state.

(2) It is unlikely that the proposal will create new businesses or eliminate existing businesses within the state because the proposed regulation prescribes the procedure for the Attorney General to verify an institution's nonprofit status. If the Attorney General denies the verification, the institution will continue operating but it will operate under the oversight of the Bureau.

(3) It is unlikely that the proposal will result in the expansion of businesses currently doing business within the state because the proposed regulation prescribes the procedure for the Attorney General to verify an institution's nonprofit status. Although an applicant may need the services of a third-party appraiser to establish "fair value," the Department anticipates that, annually, not more than one applicant will request verification of its nonprofit status from the Attorney General. This infrequent verification process will then only marginally expand a particular appraiser's business, if at all. Also, the third-party appraisal could be performed by a business outside the state.

The Department also concludes that:

(1) The proposal would benefit the health and welfare of California residents by verifying the nonprofit status of institutions of higher learning and ensuring that students and taxpayers are not misled by untruthful claims.

(2) The proposal would not benefit worker safety because it does not regulate worker safety standards.

(3) The proposal would not benefit the state's environment because it does not change any applicable environmental standards.

TECHNICAL, THEORETICAL, AND/OR EMPIRICAL STUDIES, REPORTS OR SIMILAR DOCUMENTS RELIED UPON

The Department relied on the following technical, theoretical, or empirical studies, reports or similar documents in proposing these regulations:

National Center for Educational Statistics, Integrated Postsecondary Education Data System (IPEDS) Survey Components. (<https://nces.ed.gov/ipeds/use-the-data/survey-components-glossary/2>.)

EVIDENCE SUPPORTING DETERMINATION OF NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The Department has made an initial determination that the proposed action would not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The proposed regulation prescribes the procedure for the Attorney General to verify an institution's nonprofit status. The proposed regulation requires the institution to provide necessary information on a form prescribed by the Department. The Department has determined that any cost impact to businesses from the proposed regulations would be minimal. The Department estimates that it will take no more than an hour to complete and submit the required form or any additional information requested by the Attorney General.

REASONABLE ALTERNATIVES TO THE PROPOSED REGULATORY ACTION THAT WOULD LESSEN ANY ADVERSE IMPACT ON SMALL BUSINESS

The Department determines that these proposed regulations do not affect small businesses because nonprofits are exempt from the definition of “small business.” (Gov. Code, § 11342.610, subd. (b)(6).)

REASONABLE ALTERNATIVES TO THE PROPOSED ACTION AND THE AGENCY’S REASON FOR REJECTING THOSE ALTERNATIVES

The Department finds that no alternatives were presented to, or considered by, the Department that would be more effective in carrying out the purpose of these proposed regulations or would be as effective and less burdensome to affected private persons than these proposed regulations.

Performance Standard as Alternative:

The proposed regulation requires the institution to provide necessary information on a form prescribed by the Department. Requiring the institution to provide information via the prescribed form is the easiest way to make sure that the institution provides all required information. By creating a procedure for the Attorney General to verify the nonprofit status of a higher education institution, the proposed regulation protects students and ensures that appropriate oversight remains.