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August 11, 2021

The Honorable Charles P. Rettig
Commissioner
U.S. Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20224

Dear Commissioner Rettig:

I write to submit the following supporting documentation for the Committee's referral to the Internal Revenue Service (IRS) regarding the activities of University of Arizona Global Campus (UAGC), currently a 501(c)(3) tax-exempt organization.

The U.S. Government Accountability Office (GAO) recently investigated the process through which for-profit educational institutions convert to non-profit status and found serious shortcomings, such as the possibility of insiders taking advantage of non-profit institutions at student and taxpayer expense.¹ These issues, combined with concerns raised at a hearing before the Committee,² suggest that the IRS should revisit and review previous approvals of UAGC's 501(c)(3) exemption.

The requisite Form 13909 is enclosed with this letter.

Summary

UAGC received 501(c)(3) exemption status in April 2021. This referral describes UAGC activity that appears to violate the requirements of tax-exemption, namely engaging in commercial, for-profit business activity for the benefit of Zovio, Inc., a for-profit corporation.

¹ See U.S. Gov't Accountability Off., GAO-21-89, *Higher Education: IRS and Education Could Better Address Risks Associated with Some For-Profit College Conversions*, 39 (Dec. 31, 2020).

² See *For-Profit College Conversions: Examining Ways to Improve Accountability and Prevent Fraud*, Hearing Before the H. Comm. On Educ. and Labor, 117th Cong. (2021), available at <https://edlabor.house.gov/hearings/for-profit-college-conversions-examining-ways-to-improve-accountability-and-prevent-fraud>.

This referral requests that the IRS revisit and review its previous approval of 501(c)(3) exemption to UAGC.

UAGC is engaged in commercial, for-profit business activities.

Zovio, Inc., a publicly traded for-profit corporation, incorporated in Delaware, sold Ashford University to the University of Arizona in November 2020. Ashford University then applied to become a non-profit entity known as University of Arizona Global Campus (UAGC). UAGC received section 501(c)(3) exemption in April 2021.

Under section 501(c)(3) of the Internal Revenue Code, in order to be tax-exempt an organization must be organization and operated exclusively for an exempt purpose.³

As the United States Tax Court stated in *Intl. Postgraduate Foundation*, “[w]hen a for-profit organization benefits substantially from the manner in which the activities of a related organization are carried on, the latter organization is not operated exclusively for exempt purposes within the meaning of section 501(c)(3), even if it furthers other exempt purposes.”⁴

Your agency’s own guidance outlines several key factors to consider when determining whether an institution is overly reliant on a for-profit, such as whether the entity:

- 1) Purchases everything it needs to operate from a for-profit management company;
- 2) Is severely impaired in its ability to remove itself from the management agreement, due to the consequences of removal and its reliance on the for-profit;
- 3) Is totally dependent on one for-profit company for its operation; or
- 4) Has ceded too much control of its operations to the for-profit, such that the educational institution only operates at the for-profit’s sufferance.⁵

UAGC’s conduct appears to violate the requirements of a 501(c)(3) exempt organization because, as outlined below, it is not organized and operated exclusively for an exempt purpose, and it fails several of the factors outlined in the IRS’ analysis of private benefit under section 501(c)(3).

UAGC and Zovio are inextricably linked financially for the benefit of Zovio.

Since the sale of UAGC from Zovio to the University of Arizona, the finances of these entities have been intertwined. As part of the sale, UAGC and Zovio entered into the Asset Sale and Purchase Agreement and the Services Agreement (“Agreements”). Under these Agreements, Zovio provides a considerable number of services to UAGC: recruiting, financial aid advising and processing, collections, counseling, data management, business analytics, comprehensive

³ See “Exception Requirements for 501(c)(3) Organizations,” Internal Revenue Service, available at <https://www.irs.gov/charities-non-profits/charitable-organizations/exemption-requirements-501c3-organizations>.

⁴ See *Intl. Postgraduate Med. Foundation v. Commissioner*, 56 T.C.M. (CCH) 1140 (Tax 1989) citing *Better Business Bureau v. United States*, 326 U.S. 279, 283 (1945) and *Nat. Ass’n. of American Churches v. Commission*, 82 T.C. 18, 28-29 (1984) which conclude that “the existence of a ‘single noneducational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes’”.

⁵ See generally Megosh, Scollick, Salins, Chasin, “H. Private Benefit Under IRC 501(c)(3),” available at <https://www.irs.gov/pub/irs-tege/eotopich01.pdf>.

information technology services, academic support services, learning management system, course platforms, writing and tutoring services, 24/7 help desk, library administration among others. In addition to being paid for the services provided, Zovio is also entitled to a percentage of UAGC's revenue, up to approximately 19.5%, on top of charges for the services rendered.⁶

UAGC is a captive client of Zovio.

The Agreements essentially render UAGC unable to operate independently. Zovio is guaranteed exclusivity for any programs offered to US-based students online for the 15-year term of the Agreement.⁷ UAGC is not allowed to test the marketplace for other service providers for the services it purchases from Zovio and cannot terminate the Agreements until the end of an initial 7-year term, and even after that only at substantial cost.⁸ Additionally, UAGC cannot take any action which could cause more than 5% loss of students;⁹ and if UAGC attempts to form, operate, or acquire another education institution, Zovio retains substantial rights to gain the business of the *new* entity as well.¹⁰ Essentially, UAGC is a captive client of Zovio and cannot remove itself from Zovio without considerable cost.

Zovio's profitability as a publicly traded company relies on UAGC.

Arguably, Zovio would not be viable as a profitable, publicly traded company without UAGC. Zovio's filings with the Securities and Exchange Commission (SEC) show how reliant Zovio is on UAGC for revenue as well as for its existence. Zovio's main client is UAGC, and Zovio anticipates that "[i]nitially, substantially all of [Zovio's] revenue is derived pursuant to the Services Agreement" with UAGC and UAGC will "account for a large percentage of [Zovio's] revenue for the foreseeable future."¹¹

In 2020, UAGC accounted for \$356.1 million of revenue for Zovio's University Partner segment out of a total segment revenue of \$376.2 million – nearly 95% of Zovio's University Partner revenue comes from UAGC.¹² If we look at Zovio's total revenue for 2020, which also includes some of Zovio's new ventures, UAGC still accounts for more than 89% of Zovio's total revenue.¹³

The 2020 10-K filing discusses several risk factors, all related to UAGC: enrollment rates and revenue at the school, UAGC's status with the Department of Education as a non-profit entity, and UAGC's eligibility to participate in Federal Student Aid programs.¹⁴ As outlined by Zovio

⁶ See Ashford Asset Purchase and Sale Agreement, Exhibit A and Exhibit B-1, Section 5.2, available at <https://assets.documentcloud.org/documents/7202039/Ashford-Asset-Purchase-Agreement-With-Exhibits.pdf>

⁷ See *id.* at Exhibit B-1, Section 2.2.1.

⁸ See *id.*

⁹ See *id.* at Exhibit B-1, Section 6.5.

¹⁰ See *id.* at Exhibit B-1, Section 2.2.

¹¹ See Zovio, Inc. (ZVO) 2020 10-K Filing, pg. 16, 20, available at <https://www.sec.gov/ix?doc=/Archives/edgar/data/1305323/000130532321000013/zvo-20201231.htm> (hereinafter Zovio 2020 10-K Filing).

¹² See *id.* at pg. 81.

¹³ See *id.*

¹⁴ See *id.* at pg. 15, Item 1A, Risk Factors.

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itself to its potential investors, any changes to UAGC, its programs, enrollment, and revenue would severely impact Zovio's existence.¹⁵

Conclusion

Based on the factors outlined by the IRS, UAGC's actions appear to violate requirements of its tax-exemption under section 501(c)(3) by engaging in commercial, for-profit business activities for the benefit of Zovio.

UAGC purchases a substantial number of services from Zovio in order to operate and, as such, is dependent on Zovio for its operation. Additionally, UAGC is severely impaired in its ability to remove itself from Zovio.

Based on the substantial benefit UAGC provides to Zovio, UAGC is not operated exclusively for a 501(c)(3) purpose and is arguably a *de facto* a for-profit entity.

In summary, based on the information provided above, we request the IRS to review its previous approval of 501(c)(3) exemption to UAGC.

Sincerely,



ROBERT C. "BOBBY" SCOTT
Chairman

Enclosure:
IRS Form 13909

Cc: The Honorable Virginia Foxx, Ranking Member
Cc: Sunita Lough, IRS Deputy Commissioner of the Tax Exempt and Government Entities
Division (TE/GE)

¹⁵ See *id.* at pg. 20.