For-Profit College Regulation: Overdue, Highlights Need for Expanded Public Postsecondary Education Alternatives

I. Introduction

“Until recently I thought that there would never again be an opportunity to be involved with an industry as socially destructive and morally bankrupt as the subprime mortgage industry,” said Steve Eisman, of FrontPoint Partners, a unit of Morgan Stanley. “I was wrong. The for-profit education industry has proven equal to the task.”

The subprime mortgage crisis was fueled in part by financial institutions targeting individuals, particularly low-income minorities, and luring them into mortgages they could not repay. In the wake of the Great Recession spawned by the subprime lending crisis, for-profit colleges are capitalizing on the financial insecurity of individuals in an unstable job market, seducing them with the promise of higher-paying employment that can only come with additional education. With strikingly low completion rates, and few job prospects for graduates, the only certainty for students at for-profit colleges appears to be significant debt.

The Department of Education has responded by issuing new regulations of for-profit colleges designed to increase transparency, eliminate deceptive marketing and recruiting practices, and shut down colleges with significant percentages of graduates unable to make their loan payments. For-profit colleges characterize the regulations as misguided and wrong-headed, which will have the effect of foreclosing educational opportunities to those who need them most, particularly underrepresented minorities and low-income students.

The Department of Education hopes to curb the abuses of an industry whose explosive profits are primarily fueled by federal government loans and Pell grants. For-profit colleges have

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less than 10 percent of the nation’s college students, but receive about 25 percent of all federal student-aid disbursements.\(^2\) Borrowers who attend for-profit schools represent 43 percent of all federal student loan defaults, even though they make up only 12 percent of enrollments and 24 percent of federal loan dollars.\(^3\)

While regulation of for-profit colleges is absolutely crucial, the for-profit educational sector’s growth underscores the demand for increased educational opportunities and access. In addition to increasing transparency among for-profits and eliminating schools that do not meaningfully equip their graduates for gainful employment, the government should also work to expand and promote access to our nation’s community colleges and public universities.

II. Background

There is a significant demand for educational opportunities that for-profits seek to meet. For-profit career colleges primarily grant associate’s degrees and undergraduate certificates but are swiftly expanding into the bachelor’s degree market. Among the more well-known institutions are the University of Phoenix, Strayer University, Kaplan Higher Education and DeVry University. In 2009, the University of Phoenix Online was the largest individual for-profit grantor of bachelor’s degrees (more than 14,500) and associate’s degrees (more than 12,000).\(^4\)

At for-profit colleges, half of the undergraduate credentials awarded annually—1.6 million of a total of 3.2 million—are for associate’s degrees or certificates. Associate’s degrees are generally completed in two years of full-time course work, although many students take

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longer to graduate. A large portion of associate’s degree recipients transfer the credits earned toward a bachelor’s degree program after graduation.\(^5\)

Certificates are generally career-focused and range from trade certifications for truck drivers, home health workers, bar-tenders or massage therapists to credentials in computer network administration or construction management. Requirements for certificates vary from a few courses to as many as three or four years of full-time study.\(^6\)

According to a recent Pew Research study on the for-profit sector, the industry is rapidly expanding, and more college students are attending private for-profit schools, where levels and rates of borrowing are highest. Over the past decade, the private for-profit sector has expanded more rapidly than either the public or private not-for-profit sectors. In 2008, for-profit institutions granted 18% of all undergraduate awards, up from 14% in 2003. Students who attend for-profit colleges are more likely than other students to borrow, and they typically borrow larger amounts.\(^7\)

From 1998 to 2008, overall post-secondary enrollment increased 31 percent, while the for-profits’ enrollment grew by 225 percent. For-profits account for less than 10 percent of students yet receive almost a quarter of the federal student aid. In 2008-2009, for-profits received $4.3 billion in Pell grants and $19.6 billion in Stafford loans.

The 14 publicly traded education companies have combined enrollment of 1.4 million students. The largest, the University of Phoenix, has 458,000 students, more than the undergraduate enrollment of the entire Big Ten conference schools. Of the publicly traded for-profit colleges, at least seven have most of their students enrolled exclusively in online programs.

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\(^6\) *Id.*
\(^7\) *Id.*
Unsurprisingly, for-profit colleges they have some of the highest operating profit margins among companies on the stock exchange.\(^8\)

**III. Borrowing Trends**

For profit-colleges are extremely profitable for the institutions, but are less than profitable for students. One-quarter (24\%) of 2008 bachelor’s degree graduates at for-profit schools borrowed more than $40,000, compared with 5\% of graduates at public institutions and 14\% at not-for-profit schools. Roughly one-in-four recipients of an associate’s degree or certificate borrowed more than $20,000 at both private for-profit and private not-for-profit schools, compared with 5\% of graduates of public schools.\(^9\)

Although private for-profit schools specialize in different fields of study than do public and private not-for-profit schools, the differences in borrowing patterns persist within fields of study. For almost every field of study at every level, students at private for-profit schools are more likely to borrow and tend to borrow larger amounts than students at public and private not-for-profit schools.\(^10\)

Graduates of private for-profit schools are demographically different from graduates in other sectors. Generally, private for-profit school graduates have lower incomes, and are older, more likely to be from minority groups, more likely to be female, more likely to be independent of their parents and more likely to have their own dependents.\(^11\)

Low-income and minority students make up 50 and 37 percent of students at for-profits, respectively. More than a quarter of black, Hispanic, and low-income students began their

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\(^10\) Id.

\(^11\) Id.
college careers at for-profit institutions in 2003-04, compared with only 10 percent of whites and seven percent of non-low-income students. And while for-profits enroll only 12 percent of all college students, they are responsible for 20 percent of black students and a full 24 percent of Pell Grant recipients.\(^\text{12}\)

A study of the for-profit sector issued by the Education Trust characterized the receipt of federal funds by for-profit institutions as a “reliable, sustainable, and expanding revenue stream for the sector.” In the 2008-2009 school year, for-profit colleges received 4.3 billion in Pell grants, and nearly $20 billion in federal student loans. Consequently, the average for-profit school “derives 66 percent of its revenues from federal student aid, and 15 percent of institutions receive 85 to 90 percent of their revenue from Title IV.” The University of Phoenix alone received over $1 billion in Pell Grant funding in the 2009-2010, and risks exceeding federal limits\(^\text{13}\) by deriving over 90 percent of its revenues from federal financial aid in 2010.\(^\text{14}\)

### IV. Student Outcomes

Among first-time, fulltime, bachelor’s degree-seeking students who enroll at for profit institutions, only 22 percent earn degrees from those institutions within six years. By contrast, students at public and private nonprofit colleges and universities graduate at rates two to three times higher—55 and 65 percent, respectively. Representatives from the for-profits

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\(^{12}\) Education Trust, supra note 3.

\(^{13}\) For-profit institutions are eligible for Title IV funds if they meet certain requirements. Along with more general requirements that all educational institutions must meet, for-profit colleges must enter a “program participation agreement” with the Department of Education that requires the school to derive not less than 10 percent of revenues from sources other than Title IV funds and certain other federal programs (known as the “90/10 Rule”). Found at http://www.gao.gov/new.items/d10948t.pdf.

\(^{14}\) Education Trust, supra note 3.
Contend these numbers do not include all of their students, especially those who attend part-time or transfer in to the institution. As the Education Trust noted, this is also true of the federally reported graduation rates for other colleges.\textsuperscript{15}

Two year and less than two year for-profit colleges had better graduation rates. At two-year for-profits, 60 percent of students earn an associate’s degree or certificate within three years. At less than two-year for-profits, 66 percent earn a credential within three years. These completion rates are much higher than the 22-percent rate at public community colleges. However, given the significant debt students incur and their inability to repay, it is doubtful the credentials students earn at these schools, with the intention of preparing themselves for lucrative jobs and careers, are worth the cost. Even those who manage to graduate are not entering the jobs, and bringing home the income they had planned for when they entered the institution.\textsuperscript{16}

The cost of attendance at for-profit institutions is high. According to the Education Trust, at all levels—four-year, two-year, and less than two-year—tuition and fees in 2009-2010 at for-profit colleges were far higher than those at public institutions. Once grant aid is taken into account, the unmet need for low-income students at for-profit schools is even higher than at private nonprofit colleges and universities, which use institutional grants to help defray college costs. At four-year for-profits, low-income students must find a way to finance almost $25,000 each year, with only a 22-percent chance of graduating.\textsuperscript{17}

V. Deceptive Practices

An investigation of for-profit colleges by the United States Government Accountability Office (GAO) revealed what many students and former career college employees could readily

\textsuperscript{15} Education Trust, supra note 3.

\textsuperscript{16} Id.

\textsuperscript{17} Id.
confirm, that many for-profit institutions encourage fraud and engage in deceptive and questionable marketing practices to recruit new students (and capture more federal aid dollars).\textsuperscript{18}

The GAO conducted undercover tests at 15 for-profit colleges\textsuperscript{19} and found that 4 colleges encouraged fraudulent practices and that all 15 made deceptive or otherwise questionable statements to GAO’s undercover applicants. For-profit college personnel encouraged four applicants to falsify data on their financial aid forms to qualify for federal aid—for example, one admissions representative told an applicant to fraudulently remove $250,000 in savings. Other deceptive behavior included exaggerated representations of undercover applicants’ potential salary after graduation, failure to provide clear information about the college’s program duration, costs, or graduation rate despite federal regulations requiring them to do so.

Specifically, staff commonly told GAO’s applicants they would attend classes for 12 months a year, but represented the annual cost of attendance for 9 months of classes, misleading applicants about the total cost of tuition. Admissions staff pressured applicants to sign a contract for enrollment before allowing them to speak to a financial advisor about program costs and financing options. However, in some instances, undercover applicants were provided accurate and helpful information by college personnel, such as not to borrow more money than necessary.\textsuperscript{20}

Career colleges have also preyed on veterans, many of whom are eligible for tuition reimbursement under the GI Bill, which Congress increased in 2008 to help military personnel


\textsuperscript{19} A group representing commercial colleges sued the G.A.O., accusing it of negligence and malpractice over what the suit called an “erroneous and completely biased” report criticizing commercial colleges.

\textsuperscript{20} For-profit Colleges, supra note 18.
returning from wars in Iraq and Afghanistan.\textsuperscript{21} A year after payments on the most recent G.I. Bill started, more than 36 percent of the tuition payments made in the first year of the program — $640 million in tuition and fees — went to for-profit colleges.\textsuperscript{22} Current and former for-profit college recruiters disclosed to the \textit{New York Times} that there was an “intense drive” to enroll new veterans, to the point that many military personnel were signed up for classes when recruiters knew they were likely to drop out or fail.\textsuperscript{23}

\section*{VI. Reform}

The calls for regulation of for-profit colleges resulted in the issuance of new rules by the Department of Education. The finalized rules go into effect July 2011, and will provide important protections to students. For-profit schools will be barred from paying recruiters based on how many students they enroll. For-profit colleges and nonprofit vocational programs will be required to inform prospective students of graduation and job placement rates and do a better job of validating an applicant’s high school credentials and ensuring that he or she has the ability to benefit from the program.\textsuperscript{24}

The most controversial of the proposed regulations, the “gainful employment” rule, was put on hold, and will be reissued at some point in 2011 to ensure that it does not harm well-run for-profits that offer a genuine service to students who are not eligible for traditional colleges.\textsuperscript{25} Under the original gainful employment rule, the Department would define whether a program

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\textsuperscript{22} Lipton, \textit{supra} note 21.

\textsuperscript{23} Id.


\textsuperscript{25} Rules, \textit{supra} note 24.
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successfully prepared students for gainful employment using a two-part test: measuring the relationship between the debt students incur and their incomes after program completion; and measuring the rate at which all enrollees, regardless of completion, repaid their loans on time. If a program graduated a large share of students with excessive debt-to-earnings ratios, it would be required to clearly disclose debt burdens to current and prospective students. The program could also become ineligible to participate in federal student aid programs.26

As expected, for-profit colleges have objected, and the Career College Association has sued the Department of Education over the new regulations, arguing that the Department has exceeded its authority, and the regulations are unconstitutionally vague.27

The other objections to reform propagated by for-profit colleges are the supposedly detrimental effects increased regulations will have on low-income and minority students. Arguments in favor of for-profit colleges typically underscore the access these institutions provide underserved populations that otherwise lack traditional postsecondary educational opportunities.28 The abysmal rates of graduation are explained by reference to the demographics of students who attend, the implication being that low-income minority students would fail to graduate at the same rate whether at a for-profit college or a traditional four year public university.29

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29 Lewin, supra note 27.
Other objections to reform stem from a distaste of general government interference in free-market activities, and see regulation of for-profit colleges as another instance of the federal government overstepping its bounds to disrupt gainful private activity.  

VII. The Future

Regulation of for-profit colleges is absolutely necessary to prevent the further exploitation of both taxpayers and vulnerable students. However, a former teacher at a for-profit college was correct when he wrote in the New York Times, “We need to quit subsidizing for-profit colleges, and instead devote our resources to expanding and improving the system of state and community colleges that work more effectively for a small fraction of the cost.” This same individual wrote, “The real problem that’s being ignored in this debate is that more Americans than ever are now trying to pull themselves out of the recession through education, and there aren’t enough affordable degree programs to serve them.”

In addition to combatting the rampant greed that engenders exploitation of the vulnerable, there are also chronically low expectations of non-traditional, low-income, and minority students that must be resisted. Many believe that if these students are going to fail anyway, there is no harm in simply taking their money without offering any meaningful service or instruction. However, the proliferation of for-profit colleges demonstrates a demand for higher education, which has long been used as the means of upward mobility. The government would do well to expand the availability and scope of public educational institutions, instead of funding waste and injuring the future of those it purports to help.

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32 Dehn, supra note 31.