

# For-Profit Colleges: Growth, Outcomes, Regulation

## Why Do For-Profit Colleges Matter?

For-profit, or proprietary, colleges are the fastest growing postsecondary schools in the nation, enrolling a disproportionately high share of disadvantaged and minority students and those ill-prepared for college. Because these schools—many of them big national chains—derive most of their revenue from taxpayer-funded student financial aid, they are of interest to policymakers both for the role they play in higher education and for the value they provide to students and to society.

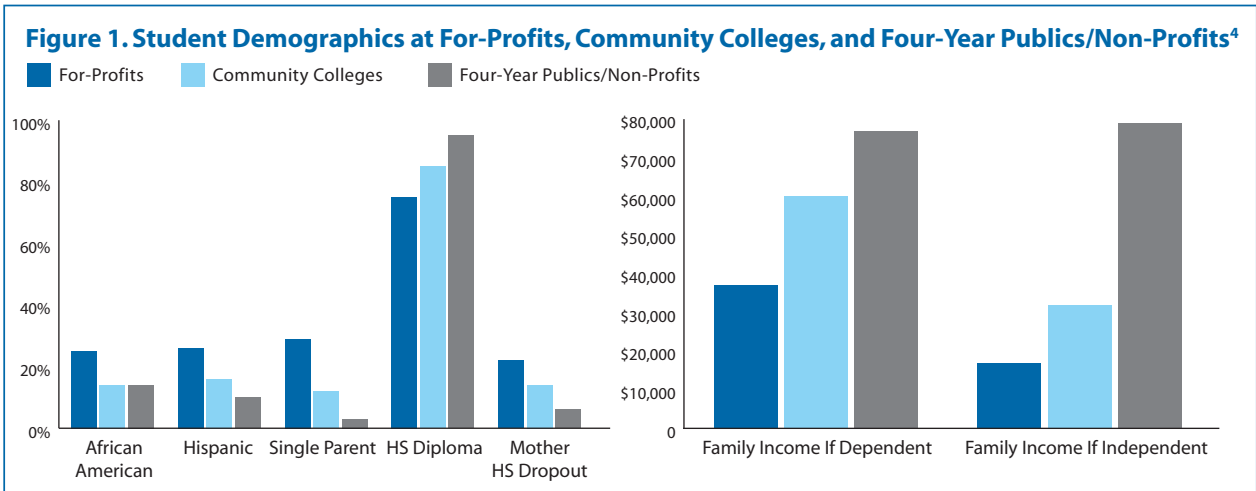
For-profit colleges primarily offer certificates and associate degrees in career-oriented programs, but they are also rapidly expanding their presence in the bachelor's degree market. While public colleges and universities have struggled to meet increasing enrollment demand in the face of state funding constraints, for-profit colleges have grown to meet student demand and have taken advantage of expanded federal student aid, which almost tripled to \$121 billion between 2000–01 and 2010–11.

In 2010–11, for-profit colleges enrolled 2.4 million students, or about 12 percent of all postsecondary students—more than three times as many as they enrolled in 2000–01. Large national chains of for-profit schools are responsible for nearly 90 percent of this growth.<sup>1</sup>

## Who Attends For-Profit Colleges?

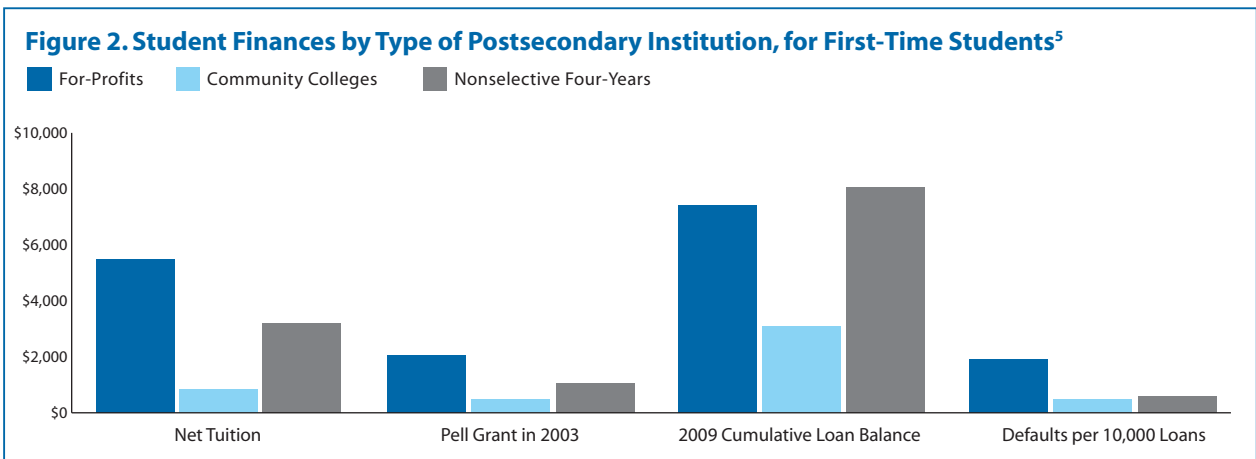
Students who attend for-profit colleges are more likely than those at other postsecondary institutions to be Black or Hispanic, to come from low-income households, to be single parents, and to have mothers who dropped out from high school (Fig. 1).<sup>2</sup> For-profit students are also more likely to be 25 or older (65 percent) and female (65 percent).<sup>3</sup>

The information provided in this brief is based primarily on the chapter “For Profit Colleges” by David Deming, Claudia Goldin, and Lawrence Katz in *The Future of Children* (Spring, 2013), Vol. 23, No. 1.



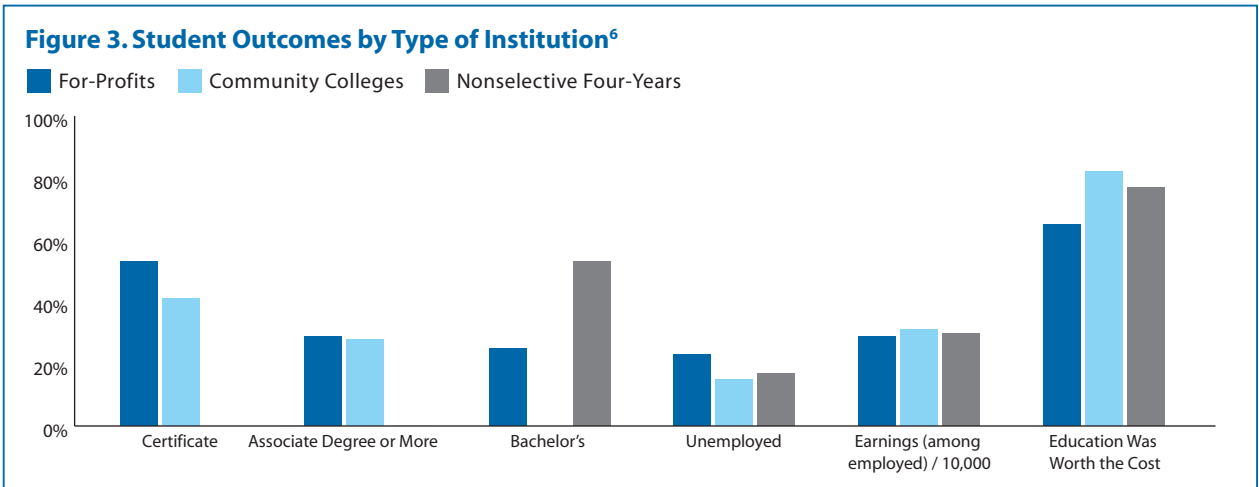
## Costs, Loans, and Default Rates at For-Profit Colleges

For-profit colleges are far more expensive than their counterparts in the public and non-profit sectors, and students who attend for-profit colleges take on a higher debt burden per year of postsecondary education. Those who attend for-profit colleges are also more likely to default on their student loans (Fig. 2).



## For-Profit Student Outcomes

Beginning students at for-profit colleges are more likely to complete certificate programs and associate degrees within six years than students at community colleges. However, because more community college students go on to complete bachelor's degrees, there is no overall difference in degree completion between associate degree seekers at the two types of institutions. On the other hand, for-profit students seeking a bachelor's degree are half as likely to complete one as students attending nonselective four-year public and non-profit institutions. Students who attend for-profit colleges are more likely to be unemployed and have lower earnings once they leave school, and are less likely to report feeling that their education was worth the cost (Fig. 3). Controlling for a wide range of student background characteristics and income narrows the gap in post-school employment and earnings by about 50 percent, but does not eliminate it.

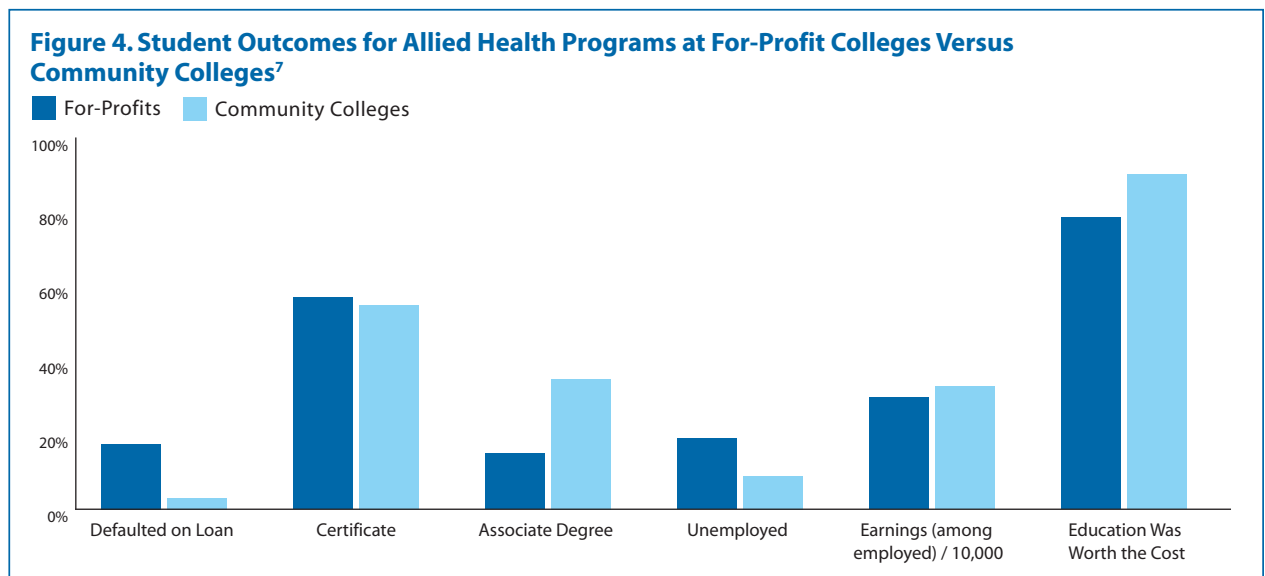


## Why Do Students Enroll in For-Profit Institutions?

For-profits have a higher cost of attendance than other types of colleges and offer equal or lower benefits. So why do students choose to attend for-profits?

### Career Orientation of For-Profit Colleges

The career and occupational training offered by for-profit colleges may be a central attraction for students. For-profits often advertise themselves as having close ties with industry, and they offer programs that are closely aligned with the needs of employers. Indeed many for-profit students enroll in short programs with specific job placement goals. However, a comparison of outcomes for students in allied health programs at for-profit and community colleges suggests that for-profit vocational programs do not provide a greater boost to students' careers than similar programs at community colleges (Fig. 4).



For-profit colleges' narrow focus on occupational training may in fact have disadvantages. Whereas flexibility is built into the design of community colleges, opportunities for exploration are limited at for-profits. Perhaps as a result,

for-profit students are less likely than community college students to pursue education beyond the credential they initially sought upon entry to college. After six years, 15 percent of associate degree seekers at community colleges went on to receive a bachelor's degree or were still enrolled at a four-year college, compared with only 5 percent of associate degree seekers at for-profit colleges.<sup>8</sup>

## Overcrowding at Community Colleges

Students may enroll in for-profit colleges when they are unable to get into courses or programs at their local community college. Community colleges have experienced stagnant or declining state funding over the past decade, and popular courses and programs have become increasingly overcrowded. In a nationally representative survey, 37 percent of U.S. community college students reported that they had been unable to enroll in at least one course during the fall 2011 semester because it was full.<sup>9</sup>

Evidence suggests that state budgetary difficulties have a significant impact on the growth of the for-profit sector. For example, a rigorous study in California found that for-profit colleges were more likely to open in areas where local community college bond referendums had recently failed to pass.<sup>10</sup>

## Marketing and Recruitment Practices of For-Profit Colleges

Students' enrollment decisions may also be influenced by the advertising and recruiting efforts of for-profit colleges. Publicly traded companies have a fiduciary duty to maximize value for their shareholders, and they devote a considerable proportion of net revenue to expanding enrollment through advertising, marketing, and recruitment.

When recruiters with strong compensation incentives conduct outreach to low-income, first-generation college students, there is the possibility that students will receive a less-than-straightforward explanation of the benefits and costs of enrolling in a for-profit college. Indeed, a 2010 investigation by the U.S. Government Accountability Office found that deceptive or otherwise questionable recruiting behaviors—sometimes bordering on fraudulent—were widespread among proprietary institutions.<sup>11</sup>

## Regulation of the For-Profit Sector

The federal government has enacted a number of regulations to govern for-profit colleges. These regulations address institutional eligibility for federal (mostly Title IV) student financial aid, student outcomes, and the use of incentives for employees involved in student recruitment.

### Higher Education Amendments of 1992

The Higher Education Amendments of 1992 banned for-profit colleges from using any form of compensation tied to enrollment or financial aid. Beginning in 2002, the ban was gradually weakened. For-profit colleges were permitted, for example, to adjust the wages of recruiters twice a year, so long as the adjustment was not “based solely on the number of students recruited, admitted, enrolled, or awarded financial aid.”<sup>12</sup>

### The 90/10 Rule

Implemented in 1998, the 90/10 rule requires that for-profit institutions be no more than 90 percent dependent on Title IV federal student aid as a share of total revenues. Federal grants and loans accounted for 73.7 percent of the revenues of Title IV-eligible for-profit colleges in 2008–09.<sup>13</sup> These figures understate the reliance of the for-profit sector on federal student aid, as they do not include military educational benefits.<sup>14</sup>

### Cohort Default Rate Regulation

The cohort default rate was originally implemented in the 1980s and was defined as the percentage of borrowers who default within two years of entering into loan repayment. Institutions with a two-year default rate that

exceeded 40 percent in a single year, or 25 percent in three consecutive years, would lose their eligibility for Title IV aid for one to three years.<sup>15</sup>

Because of concerns that the two-year window was not catching large numbers of defaults that occur in the third year after entering repayment, the Higher Education Opportunity Act of 2008 expanded the default rate window to three years starting with the 2012 cohort. Analyses of trial data suggest that lengthening the window from two to three years could more than double default rates for proprietary colleges.<sup>16</sup>

## Gainful Employment Regulation

The currently contested Gainful Employment Regulation was adopted in 2011 and is specifically targeted at for-profit colleges, although it also applies to certificate programs at public and non-profit colleges.<sup>17</sup> The regulation is a departure from the previous regulations because it targets individual programs within institutions and links the cost of higher education to earnings benefits.

Under the regulation, a program is considered to lead to gainful employment if at least 35 percent of the students in each cohort are in repayment of their federal loans; if the annual loan payment for a typical student is 12 percent or less of his or her annual earnings; or if the annual loan repayment for a typical student is 30 percent or less of his or her discretionary income. A program that fails all three measures for three out of four years loses Title IV eligibility.

An analysis of trial data from students enrolled in 2011 shows that approximately 8 percent of for-profit programs serving more than 30 students would fail the gainful employment standards (Table 1).

Category	Overall (%)	Public/Non-Profit (%)	For-Profit, Independent (%)	For-profit, Chain (%)
Failed all 3 standards	5.2	0.0	3.1	7.9
Failed annual earnings	10.0	0.5	9.4	12.4
Failed discretionary earnings	53.8	11.0	62.1	55.5
Failed repayment rate	40.5	15.9	36.2	48.9
Number of programs	3,696	364	1,495	1,837

Of the three measures that make up the gainful employment standard, the annual earnings measure is by far the easiest to meet: 95 percent of programs that failed the discretionary earnings standard also failed the annual earnings standard. A gainful employment standard based only on the annual earnings measure would raise the failure rate of large programs in for-profit chains to 12.4 percent from 7.9 percent, but would be far easier to administer.

The future of the gainful employment regulation is uncertain. A federal district court, hearing a lawsuit by the Association of Private Sector Colleges and Universities, held that the Department of Education had offered no reasoned basis for the 35 percent repayment rate threshold and, because the standards are designed to work together, vacated all three measures.<sup>19</sup> Litigation remains ongoing and in the spring of 2013 the Department of Education signaled its intention to revisit the regulation and seek other ways to define gainful employment.

## Conclusion

Although community colleges, compared with for-profits, may provide an equal or better education at a lower cost, demand for higher education is likely to outpace state funding in the near term. Thus, many students may not be choosing between for-profits and community colleges but between for-profits and no postsecondary education at all. A gainful employment regulation that attempts to estimate whether a program provides good value to students therefore seems appropriate.

The poor performance of students seeking bachelor's degrees at for-profits should concern taxpayers and policymakers because for-profit colleges, particularly the large chains, are rapidly expanding their bachelor's degree programs. Because tuition in bachelor's degree programs is higher and students enroll for more years, the federal government's per-student financial commitment for these programs is several times greater than for one-year certificate programs. In principle, greater taxpayer commitment should be accompanied by increased scrutiny of whether students complete their degrees and make sufficiently high earnings to justify the investment. However, because the set of skills gained in a bachelor's degree program are varied, as are students' potential occupations, regulation using a uniform standard of value presents a challenge.

One possible solution is to strengthen disclosure requirements,<sup>20</sup> allowing students to make more informed decisions about costs and benefits, so that the government would not have to impose a uniform standard of value on bachelor's degree programs. Additionally, requiring financial aid counseling by an independent third party could protect students from misleading information they may receive directly from recruiters.

Given that the for-profit sector will likely continue to play an important role in U.S. higher education in an era of fiscal constraints, a key challenge in regulating for-profit colleges will be to restrain overly aggressive and potentially misleading recruitment practices while not diminishing opportunities for disadvantaged students to gain postsecondary training and credentials.

## Endnotes

1. Deming, Goldin, & Katz (2012).
2. Deming et al. (2012, Table 1).
3. Student characteristics gleaned from the Beginning Postsecondary Students (BPS) longitudinal survey for 2004–09, which follows a nationally representative sample of first-time, full-year undergraduates who began their postsecondary schooling in the 2003–04 academic year. Part-time and returning students are not represented in the BPS data, and the comparisons in figures 1–4 do not apply to them.
4. Adapted from the 2004 to 2009 BPS longitudinal survey and the Integrated Postsecondary Education Data System (IPEDS). Unweighted sample sizes in the BPS are rounded to the nearest 10. The IPEDS tabulations cover the (undergraduate and graduate) enrollments of Title IV institutions in fall 2009. The BPS tabulations cover beginning postsecondary students entering a Title IV institution in the 2003–04 academic year (Deming et al., 2012).
5. Figures 2–4 are adapted from BPS:04/09 and are weighted to be nationally representative of first-time, full-year undergraduates in fall 2003. Net tuition is calculated as tuition minus total grants (including Pell Grants). The 2009 cumulative loan balance and default measures include only loans from federal Title IV sources. Net tuition, Pell Grants, and cumulative loan balance are in “current” dollars.
6. Certificate completion includes only students starting in certificate programs; associate or more completion includes those starting in associate programs; and bachelor's completion includes those starting in bachelor's programs. The unemployment and earnings measures exclude students who reported that they were still enrolled in school in spring 2009. See also footnote 5.
7. The sample consists of students who were enrolled in certificate or associate programs that were categorized as “Health Professions and Related Clinical Sciences” under the U.S. Department of Education's 2000 Classification of Instructional Programs (CIP) codes. The unemployment and earnings measures exclude students who reported that they were still enrolled in school in spring 2009. See also footnote 5.
8. BPS: 2004–09.
9. Pearson Foundation (2011). This survey may not reflect current conditions as community colleges have shown declines in enrollments since 2011 (National Student Clearinghouse Research Center, 2013).
10. Cellini (2009).

11. The GAO reissued its original August 2010 testimony on November 30, 2010 to clarify and add more precise wording but did not change its conclusions (U.S. Government Accountability Office, 2010).
12. Federal Student Aid Programs (2002).
13. Calculations based on data from the U.S. Department of Education, Federal Student Aid Data Center.
14. For-profits accounted for 36.5 percent of the Post-9/11 GI Bill benefits during the first year of the program and for 50 percent of the Department of Defense Tuition Assistance benefits in fiscal year 2011. See U.S. Senate Health, Education, Labor and Pensions Committee (2012).
15. Institutions and Lender Requirements Relating to Education Loans (2009).
16. In a trial analysis of the 2008 for-profit cohort, lengthening the window to three years more than doubled the default rate from 11.6 to 25.0 percent (Federal Student Aid, U.S. Department of Education, 2011b).
17. Program Integrity: Gainful Employment—Debt Measures (2011).
18. Data obtained from Federal Student Aid, U.S. Department of Education (2011a). These data report the performance of the institutions' 2011 graduates on the three gainful employment standards and are published for informational purposes only since the regulation does not apply to this cohort of students.
19. Association of Private Colleges and Universities v. Arne Duncan and United States Department of Education (2012).
20. Long (2010).

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