CAPITAL RESEARCH CENTER

Organization Trends

What's Behind the Attack on For-Profit Colleges?

How Concern Over Student Loan Defaults Obscures the Real Issue

By RiShawn Biddle

***Summary**: America's for-profit colleges and universities have been leading innovators in higher education. They provide millions of college students, many of them older and working full-time, with flexible and affordable ways to acquire a worthwhile education. But a soon-to-be announced Department of Education regulation is set to penalize for-profit colleges for their high rates of student loan default. The federal crackdown on privately-operated for-profit colleges is prompted by radical philanthropist George Soros, a phalanx of stock manipulators, and left-wing activists and politicians. Their efforts to damage this vital sector of higher education ignore the real issues: the runaway spending and declining quality of higher education.*

Profit **is a swear word in the Obama White House which is trying to kill the for-profit college sector. Here President Obama meets with Sen. Tom Harkin (center) and Education Secretary Arne Duncan (left) in February of this year.**

Few institutions in the otherwise stodgy world of America's higher education system have spurred more innovation – or attracted so much scrutiny – as the nation's for-profit colleges, universities and technical schools. Once burdened by reputations for shoddy training and fly-by-night operations, they have become formidable challengers to traditional public and private universities, and they compete for smart students—and their tuition dollars. Some 438,100 students are enrolled at the University of Phoenix, a subsidiary of Apollo Group, the education services giant. It is the nation's third-largest university system after the State University of New York (SUNY) and California State University systems. For-profits account for 77 percent of the 483 new colleges and universities created in the U.S. between 2005 and 2010, according to the Carnegie Foundation for the Advancement of Teaching.

Most for-profit colleges focus on professional training rather than the humanities and liberal arts. By offering flexible, nontraditional class schedules, they appeal to those who want more economic opportunities, to blacks, Latinos and the poor, to busy mid-career workers and former high school dropouts-turned-GED recipients. For-profits also pioneer in using

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the Internet and other new technologies to instruct large numbers of students who can't attend a traditional campus classroom. Without for-profit institutions, it will be hard for President Obama to achieve his goal of increasing the number of adults age 25 to 34 with college degrees. The administration wants to raise the percentage from 42 to 60 percent over the next nine years.

It's therefore disturbing that the Obama administration and leading Democrats such as Tom Harkin (D-Iowa), chairman of the powerful Senate Health, Education, Labor and Pensions Committee, want to stifle the growth of the for-profit college sector. They are trying to restrict the flow of federal student aid dollars to for-profit schools and the students who attend them, and they have the support of a bizarre coalition of hedge fund players and left-wing groups that want to hobble for-profits for their own diverse reasons.

For-profit colleges have spent the past year battling the U.S. Department of Education over a new rule ostensibly aimed at reducing the number of college students who default on their federal student loans. The so-called Gainful Employment rule, set to go into effect next month, would cut the amount of student loan money and Pell grants available to for-profit colleges (and community colleges with vocational education programs) if students carry debt-to-income ratios considered too high and have loan repayment rates considered too low. The rule says a for-profit college graduate's annual loan payment should not exceed more than 8 percent of the expected annual earnings of the occupation for which the student is preparing. (The rule doesn't apply to students at public or nonprofit colleges.) For-profit colleges would be held responsible for their students' loan defaults. If the Gainful Employment rule is not revised, it could force many for-profit colleges to reject aspiring students deemed to be unacceptable financial risks.

The for-profit higher education sector is also taking hits from the Government Accountability Office (GAO), the watchdog arm of Congress. After investigating 15 for-profit colleges, the GAO reported in August 2010 that all "made deceptive or otherwise questionable statements" and four "encouraged fraudulent practices" such as falsifying data on federal student aid applications. Three months later, the GAO admitted some errors but still stands by its report.

Supporters of a Crackdown

The crackdown has taken a toll on the reputations and bottom lines of the for-profits, with shareholders of the major providers bearing $3 billion in paper losses—10 percent of their market value—since July 2010, when federal officials first announced the proposed rules. The market value of Strayer Education, whose schools serve 50,416 students, declined by 45 percent, with investors taking a $1.2 billion hit. In March Apollo Group announced $97 million in losses during its fiscal second quarter thanks to a 22 percent decline in enrollment. (It earned $90 million and enrollment increased 18 percent during the same period a year earlier.) In May, media giant Washington Post Co. reported a seven-percent decline in revenue at its Kaplan University division and a 22 percent decline in enrollment during its first fiscal quarter.

By contrast, the crackdown has been lucrative for money managers. Steve Eisman, a tough-talking money manager who runs the FrontPoint Partners division of the financial services giant Morgan Stanley, is betting that for-profit colleges will lose their federal funding. Eisman has declared that for-profit colleges are "as socially destructive and morally bankrupt as the subprime mortgage industry." In 2007 he hedged his bets and made a fortune by short selling subprime mortgage securities. To ensure that his next "big short" pays off, Eisman has met with the Department of Education officials who are writing the Gainful Employment rule, and he has testified against for-profit higher education before a Senate committee.

Radical philanthropist George Soros, who made billions of dollars speculating in the currency markets, is also a major funder of the campaign against for-profit education.

Soros's grantmaking foundation, the Open Society Institute (OSI), has generously supported policy groups and advocacy organizations that are strong proponents of increased regulation of for-profit higher education. The National Consumer Law Center ($700,000 in total OSI support since 2001), the New America Foundation ($3.2 million since 2001) and the Center for American Progress ($4.1 million since 2005) favor increased government regulation of for-profit use of federal student loan funds. Like Eisman, they have been in contact with Department of Education officials on the Gainful Employment rule. Ironically, the Center for American Progress, which

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is directed by former Clinton White House chief of staff John Podesta, supports charter schools. Like for-profit colleges, charter schools are privately-operated entities that receive taxpayer subsidy.

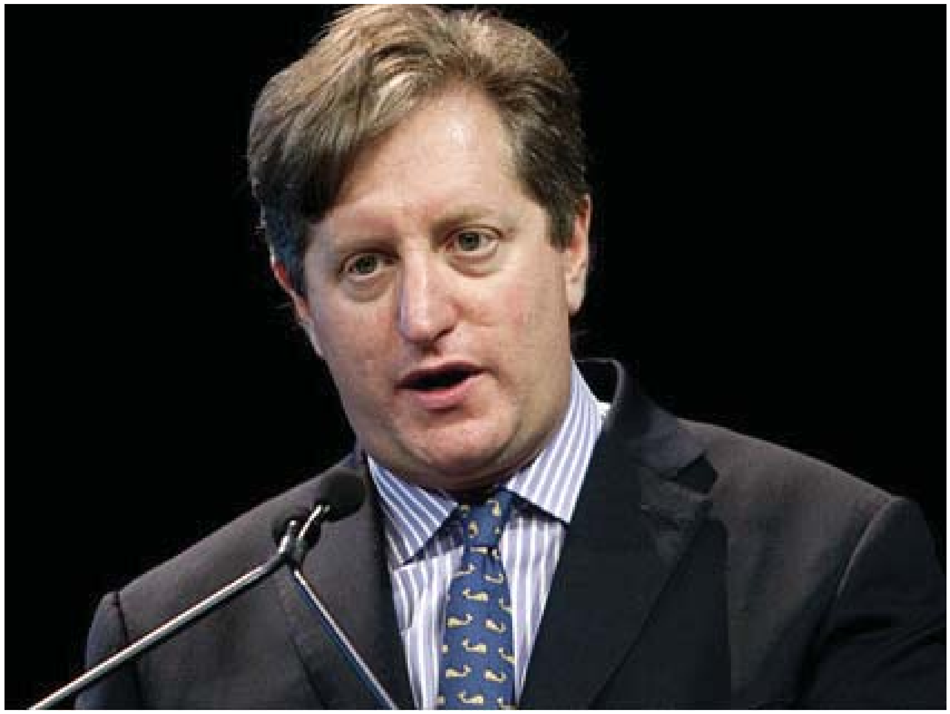
Defenders of the For-Profits

Eisman and the other foes of for-profit higher education have come under return fire from the for-profit colleges, which have an army of paid lobbyists eager to defend the sector's right to federal loan subsidies. But it's noteworthy that left-leaning groups are also critical of the Obama administration's Gainful Employment rule. They are suspicious of contacts between higher education officials and hedge fund short-sellers like Steve Eisman.

Jesse Jackson, civil rights organizations such as the National Urban League and some members of the Congressional Black Caucus decry the crackdown. They say the proposed restrictions will keep poor blacks and Latinos from getting the college degrees they need to compete in the job market.

In October 2010, Keiser University, a Florida-based for-profit college filed a lawsuit (since dropped) against Florida State Community College in Jacksonville. The suit charged that Florida State's president maligned Keiser's reputation in an email he sent Eisman.

On March 17, 2011 the government transparency group Citizens for Responsibility and Ethics in Washington (CREW) filed a Freedom of Information Act request to learn more about how the Education Department had formulated the Gainful Employment rule. CREW uncovered emails detailing the all-too-cozy dealings between supporters of the crackdown like Eisman and the Soros-backed think-tanks and the Obama education department.



Wall Street hedge fund manager Steve Eisman

Evading the Real Issue of Higher College Costs

The federal crackdown on for-profit colleges does not address the real problems of financing American higher education. Steve Eisman and his liberal allies in public and nonprofit higher education say for-profit colleges recruit poorly-educated students who are unlikely to graduate and offer them shoddy courses in low-paying career fields in which jobs are scarce.

That's funny. The same charges also apply to nonprofit and public universities. It's true that 12 percent of for-profit students who attended college in 2008 defaulted on their student loans within two years of leaving school. But it's also true of seven percent of collegians overall. Students who attend historically black colleges and universities default at a rate of 20 percent.

College costs have increased at twice the rate of inflation for the past three decades. Americans borrow $126 billion a year to finance their college costs – and only 31 percent of first-time collegians graduate on time. Only 22 percent of first time full-time community college students graduate in three years.

Nonprofit and public universities charge ever-higher tuitions without having to prove the real value of what they offer taxpayers or students. They also benefit from direct and indirect subsidy: through state appropriations and student aid scholarships and loans. It's likely that the low rate of college graduation results less from financial hardship than from the low quality of instruction and curricula provided by the nation's K-12 schools. One-third of college freshmen and sophomores took remedial math and reading courses in 2006 because they are poorly prepared in high school for college work.

For-profit colleges are no innocents. Much of the profit in for-profit higher education depends on the sector's successful lobbying for federal and state student aid. For-profits can't whitewash the fact that they account for 44 percent of all federal student loan defaults – despite serving just seven percent of the nation's college students. But for-profit colleges also have pioneered innovations that open the doors of college to poor and minority households and provide training for high-skilled blue- and white-collar jobs. When hedge fund speculators conspire with public education officials to push for-profits out of business they are demonstrating that depending on government money carries with it the danger of government regulation.

Increasing Public Dependency

The first for-profit colleges appeared only in the 19th century. Unlike public and nonprofit private colleges, they served a humble purpose: teaching basic business skills to an emerging class of accountants, white collar workers and entrepreneurs. John D. Rockefeller graduated from a for-profit, Chancellor University. Henry Ford and R. J. Reynolds are alumni of Bryant & Stratton Business College. After World War II there were secretarial schools, schools of cosmetology, barber colleges and schools of auto repair. For-profit colleges remained an education backwater in 1980 with just 100,000 students enrolled in their programs. Mistakenly associated with diploma mills, they got no respect. Only one in 10 schools offered degrees—and these were often not accredited by regional higher education associations charged with monitoring quality.

Changes occurred in the 1990s. In 1992, Congress amended the Higher Education Act. It restricted the flow of Pell grants to for-profit schools to ensure that federal funding didn't account for more than 85 percent of a for-profit's revenues. Responding to market forces, for-profits moved away from such fields as cosmetology and toward computer technology, healthcare and business administration. The stock market helped. In 1991, DeVry Inc. became the first publicly-traded for-profit university system. With access to capital markets, other higher education companies were formed. Although they do not benefit nearly as much as private nonprofit and public schools, for-profit colleges also learned to count on state appropriations to reduce their upfront tuition costs. For-profit schools gain $1.41 per student in direct and indirect government aid compared to $6.92 acquired by nonprofit colleges and a whopping $27.12 per student that goes to public universities, according to a 2010 study by consultants Robert Shapiro and Nam D. Pham.

The new push for quality and access to capital allowed for-profits to maximize their greatest innovation—creating flexible and convenient class schedules. A for-profit school such as the Arts Institute of Pittsburgh lets students arrange their course schedule into three four-hour blocks, which lets them balance classwork with job and childcare schedules. And online courses are available at any time of day, in any location. For-profits also figured out how to serve new "customers"—African-Americans and Latinos ignored by traditional higher education.

However, for-profits became increasingly reliant on government benefits when the federal government decided in 2003 to consider online courses as comparable to traditional classroom courses. For-profit colleges got another assist from the feds in 2008 when Congress amended the law authorizing the G.I. Bill to pay full college costs (and a partial subsidy for housing and book costs) for Iraq War veterans and those serving in the armed forces after 9/11. Today a quarter of the nation's for-profit schools generate at least 80 percent of their revenue from federal student aid, according to the U.S. Department of Education.

Playing Favorites

By 2010, for-profit colleges accounted for seven percent of all college students; Apollo Group's University of Phoenix had surpassed California State University as the nation's second-largest university system by enrollment. Between 1980 and 2010, for-profits increased enrollment at a 9 percent clip, six times greater than their traditional peers. President Obama proposed spending an additional $12 billion in federal funding for community colleges in hopes of adding 5 million more new graduates by 2020.

However, the Obama administration was also encouraging the enemies of for-profit higher education. They complained about low-quality course offerings and low graduation rates. They particularly focused on the amount of debt for-profit students take on to finish school. The average for-profit student graduates with a debt load of $32,909, far more than the $20,040 debt incurred by graduates of public colleges and $27,535 in debt borne by graduates of nonprofit private colleges.

Particularly vexed about the growth of for-profits are three nonprofits funded by George Soros's Open Society Institute. The National Consumer Law Center began the attack on the for-profit sector with a 2005 report, "Making the Numbers Count: Why Proprietary School Performance Data Doesn't Add Up and What Can Be Done About It." Another go-to source for for-profit opponents is the New America Foundation's *Higher Ed Watch* blog edited by Stephen Burd, a former *Chronicle of Higher Education* reporter. And the influential Center for American Progress goes after for profits with its "Campus Progress" website and its Progress Action Network advocacy arm. (CAP was most recently profiled by Sean Higgins in the February 2011 *Organization Trends*.)

What's Behind the Education Department Rule?

The first recent salvo against for-profits came in early 2009, when the Obama administration named for-profit foe Bob Shireman, founder of the Institute for

College Access & Success (TICAS), as deputy undersecretary of education. He was put in charge of the federal student financial aid system. Eight months later, the agency appointed a 28-person panel to advise federal officials on new student aid rules. A year after that Sen. Tom Harkin (D-Iowa), the education committee chairman, declared that for-profits were more concerned about "their bottom line" than about student success.

Meanwhile, for-profits were under fire from hedge fund investors. Leading the charge was Eisman, a stock analyst-turned-money manager who helped Morgan Stanley and its clients make billions during the financial meltdown by successfully betting that subprime mortgages would go bust. Using a Wall Street technique called short selling (in which a speculator bets that the shares of a company will decline and then reaps a profit when they do), Eisman wagered that shares in firms such as Apollo Group and Washington Post Co. would decline by as much as 50 percent when the federal government crafted new regulations.

An Obama campaign donor, Eisman in April 2010 met with Shireman and David Bergeron, the education department official who was drafting the for-profit regulations. The agency wouldn't disclose the meeting until it was pressed by *Fortune* magazine, eventually claiming the meeting "was fully appropriate."

By July 2010, Department of Education officials were circulating advanced copies of the proposed rules (including the Gainful Employment provision) to CAP, New America Foundation and other for-profit foes, according to agency e-mails obtained by CREW in response to a Freedom of Information Act request. Tipped off about the proposal, these groups had a head start in promoting them. CREW has no evidence that Eisman received advance notice, but it did find an e-mail from Eisman warning Bergeron that "education stocks are running because people are hearing DOE is backing down on gainful employment." When the Department finally released the Gainful Employment rule, for-profit share prices took a hit. Apollo Group's shares lost 1.9 percent of their value by the end of the following business day, with investors losing $135 million.

George Soros

A month later, on August 3, the GAO released its error-riddled report on for-profit colleges declaring that its investigation revealed falsified student financial data and other "questionable sales and marketing tactics." For example**,** GAO inaccurately reported that a Pennsylvania-based for-profit college told an undercover agent not to report a $250,000 inheritance on his financial aid forms. It later was revealed that excluding the inheritance was the undercover investigator's idea. A red-faced GAO was forced to reissue a revised version of its report, but by then the damage was done. By December, share prices of some for-profit colleges had declined by half.

(At press time an article by the Daily Caller's Jonathan Strong asserted that a leaked GAO email showed that GAO was placed under "extreme short time frames" by Sen. Harkin to churn out the report. The news item also indicated that the email said "congressional staffers" had demanded that several details be included in the document as it was being finalized.)

For-profit colleges fought back. Their alphabet soup of trade associations – APSCU (Association of Private Sector Colleges and Universities), CES (Coalition for Educational Success), and CCA (Career Colleges Association) hired high-profile Democrats, including former Clinton administration official Lanny Davis, to win support for their cause. In January, they sued the Department of Education to block enforcement of Gainful Employment. They also won support from congressional Republicans who now control the House. In February, the Republican majority, along with 58 Democrats, voted to bar federal education officials from implementing Gainful Employment. The Senate failed to take up the measure, putting the Obama administration in the uncomfortable position of not only battling Republicans but also Democrats, including members of the Congressional Black Caucus and other left-leaning lawmakers, over the for-profit regulations.

The Department of Education admitted that it used shoddy information to develop Gainful Employment and another proposed rule to deny aid to students attending for-profit, nonprofit and public colleges with three-year default rates of greater than 30 percent. In April, the department announced that it would further revise its estimates of loan default rates.

The Real Issues Facing Higher Education

Despite scoring some propaganda points against for-profit schools federal officials have failed to address the most critical issues confronting higher education: its increasing cost and declining quality.

Since the end of World War II, federal and state governments have made it their mission to expand the number of students attending college. Yet runaway spending is making higher education unaffordable. Today, after K-12 and Medicaid, higher education is the third-biggest line item in state budgets. Even with federally-guaranteed loans and federal and state subsidies, the average family in 2008 would need to devote an estimated 27 percent of its income to pay for an education at a four-year public university, seven percentage points higher than in 2000, according to the National Center for Higher Education Management Systems – and this is even with federally-guaranteed loans and state subsidies (the percentage of income to pay for a private university is 80 percent, a 22 percent jump). With graduation rates as low as 12 percent for community colleges, and almost as low for many public universities, taxpayers, families and politicians are beginning to ask tough questions about higher ed spending.

The single-minded focus on finding more money for higher education has obscured the increasingly slipshod quality of undergraduate education. Failing public and nonprofit universities are almost never shut down or lose accreditation. Last year in the *Washington Monthly* for-profit critic Kevin Carey noted that it took 29 years for Washington D.C.'s Southeastern University to finally lose its higher ed certification and be shut down despite its long history of fiscal mismanagement and low graduation rates.

The biggest problem for higher education is one that colleges can't address: the low level of American educational achievement at the K-12 level. About one-third of U.S. high school students drop out and few high school graduates are prepared to handle college coursework. American 15-year-olds rank 25th in student achievement internationally, according to a 2009 survey conducted by the Organisation for Economic Co-operation and Development. Only two U.S. states teach math to the high standards set by Singapore.

Oddly enough, the for-profit colleges that liberal think tank experts shun may hold some of the tools to address these problems. Higher education reformers are learning to embrace the online learning tools first developed by for-profit colleges. Public universities, faced with a parental backlash over tuition increases and a taxpayer backlash over public sector retiree benefits, may be forced to expand their own online offerings.

For-profit learning offers many possibilities for improving higher education. But the sector won't flourish as long as it remains on the government dole and subject to politically-driven regulation.

RiShawn Biddle, editor of education reform website Dropout Nation (www.dropoutnation.net), is a co-author of *A Byte At the Apple: Rethinking Education Data for the Post-NCLB Era.*

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BrieflyNoted

The former national chief organizer of **ACORN** has launched a new left-wing group aimed at carrying on her radical un-American agenda. **Bertha Lewis**, who last year called the Tea Party movement a “bowel movement,” launched the New York-based **Black Institute** earlier this year. The group’s agenda is almost identical to that of ACORN, which filed Chapter 7 bankruptcy in November, but with a focus on African-Americans. ACORN lawyer **Arthur Schwartz** is on the group’s board of directors, and **Mary Sobecki**, a program officer with the **Needmor Fund**, a far-left ACORN funder, is on its board of advisors.

Lewis popped up in May at a Brooklyn rally against the world’s largest retailer. On a YouTube video the bard of ACORN accuses the company of unfair hiring practices and is shown singing “**Walmart** sucks! Walmart sucks! Walmart sucks!” The potty-mouthed Lewis is a former squatter who first got involved with ACORN after illegally occupying an abandoned property.

Where did **Steve Kest** go? Last year the former executive director of **ACORN** joined **Van Jones** as a senior fellow at **John Podesta**’s **Center for American Progress Action Fund**. But recently all references to Kest’s appointment have disappeared from the Center’s websites. Spokespersons for CAP ignored **Capital Research Center**’s repeated requests for information about Kest’s whereabouts. Kest participated in the cover-up of a million-dollar embezzlement at ACORN perpetrated by **Dale Rathke**, brother of disgraced ACORN founder **Wade Rathke**.

MoveOn is promoting a YouTube video in which two left-leaning billionaire philanthropists, **Warren Buffett** and **Bill Gates**, urge that taxes be raised on Americans. “The taxation system is much too flat in this country and frankly I think that Bill and I should have a higher rate on the income we get,” said Buffett during a panel discussion. “I go along with that wholeheartedly,” added Gates. “I think we probably need a more progressive system as we look to balance the budget.”

Comedian **Stephen Colbert**, a liberal who plays a conservative commentator on TV, filed papers in Washington, D.C. to create a “super PAC” that can raise and spend unlimited funds on campaigns, the Daily Caller website reports. “I want to open the Colbert super PAC for all those PAC-less Americans,” he quipped as a crowd gathered outside the Federal Election Commission chanted his PAC’s motto: “Making a better ‘tomorrow’ tomorrow.”

The latest obsession of **George Soros** is “political polarization”—something to which he has greatly contributed. Soros says polarization is “endangering our open society,” writes reporter Kenneth Vogel in *Politico*. He told an audience at the **Cato Institute** that “the two sides in the current disputes have each got hold of one half of the truth which they proclaim to be the whole truth.” Tedious.

What part of “spreading the wealth” doesn’t **Arianna Huffington** understand? Fresh off her lucrative sale of the Huffington Post website to **AOL**, Huffington now wants even more people to blog for her for free. In charge of AOL’s blogging operations, the conservative-turned-liberal is encouraging bloggers to provide their services to Patch.com. She describes the new website as “AOL’s national network of hyperlocal sites currently covering community life in over 800 towns across America.”

Americans for Prosperity vice president for policy **Phil Kerpen** is writing a book on the regulatory excesses of the **Obama** administration. The book, *Democracy Denied: How Obama is Ignoring You and Bypassing Congress to Radically Transform America - and How to Stop Him*, is scheduled to be published in October by BenBella Books. Kerpen wrote the October 2009 *Foundation Watch* that profiled the **Apollo Alliance** and was a major player in the 2009 ouster of green jobs czar Van Jones from the Obama White House.