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THE PROFIT IN PROPRIETARY EDUCATION: AN EXPLORATORY EXAMINATION OF STUDENT LOAN RATES

Tiffanie Turner
Ph.D. Student, Hampton University
tiffanienturner@gmail.com

Abstract
The needs of adult learners and the rising tuition at traditional colleges and universities has stimulated the emergence of for-profit higher education in the United States as a viable sector of postsecondary education (Morey, 2004). Previous literature have examined choice selection and compared traditional and nontraditional higher education curricula. This author's research has found limited scholarly examination of the relationships between student loan defaults and revenue. This article will empirically analyze these factors to determine that there is a significant correlation of student default rates and revenues at proprietary institutions.
Key words: for-profit higher education; proprietary institutions; student loan default; postsecondary education; private-equity funds

INTRODUCTION

Globalization and economic changes have increased the need for higher education. Adult learners are seeking quality, low-cost, non-traditional instruction to further their careers. Despite the online and distance learning option provided by nonprofit universities, for-profit higher education organizations are challenging teacher-driven, research-based institutions. For the purposes of this article, the term for-profit universities & colleges and proprietary institutions will be interchangeable and refers to higher education systems publicly traded in U.S. markets. Once seen as vocational and certification-based schools, Fortune 500's 2014 top for-profit companies – Graham Holdings Inc. (#614); Apollo Education Group Inc. (#638); Education Management Corporation (#837); and DeVry Education Inc. (#978) now attract approximately 621,300 students and generate a combined revenue of $9.24 billion in 2013. These organizations quickly adapt programs to meet challenging industry needs. For-profit universities' degree programs now rival nonprofit universities by offering associate, bachelor, master and doctoral degrees in the arts, sciences, as well as technical career fields.

Previous literature on this topic as primarily examined the differences in nonprofit and for-profit instructional philosophies, for-profit private equity benefits, the behavioral traits that influence students to select for-profit institutions. The preliminary review of literature finds a breach in the analysis of additional factors that affect the bottom line at for-profit universities. This includes studies considering the number of degree programs offered by Graham Holdings, Apollo Education Group, Education Management Corp., and DeVry, Inc. Next, the financial status of each university will be examined under the evidence in the national rise in student loan defaults. Student loan default is defined by the U.S. Department of education as failure to make payments on student loans as scheduled according to the terms of the promissory note signed at the time of the loan. The U.S. Federal Higher Education Act of 1965 designated student financial aid under Title IV funds. To maintain eligibility to participate in these programs, institutions must comply with regulatory requirements including financial aid management, educational programs and recruiting practices under the Higher Education Opportunity Act of 2008 (HEOA). Additionally, federal regulations enacted the 90/10 rule that institutions receiving at least 90% of its revenue in two fiscal years from Title IV programs could lose its eligibility to participate. These factors create a delicate balancing act for proprietary institutions that heavily rely on tuition to support its operations.

The purpose of this paper will be to empirically review scholarly and industry studies concerning the viability and longevity for for-profit universities. This research will add to the limited body of scholarly studies regarding the relationship of for-profit educational programs and financial status. This article will be structured as follows: a review of previous literature regarding the increase

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in higher education student enrollment; the rise of for-profit universities; criticisms and the future of these companies. Next, the paper will utilize data gathered from the United States Department of Education, U.S. Census and for-profit universities' financial statements from 2011-2013 to determine relationships and correlations between and within the four for-profit organizations to determine the outcomes of the following hypothesis:
H1: A proprietary institution's student loan default rate is correlated to its annual earnings.

LITERATURE REVIEW

According to the National Center for Education Statistics (NCES), the total average income of full-time workers, age 25-34 in 2012 was $38,000 per year. Those workers with a bachelor's degree or higher averaged $50,000 per year. In the same year NCES reported 1,017,538 associates; 1,791,046 bachelors; 754,229 masters; and 170,062 doctor's degrees were confirmed in the United States (NCES, 2014). The United States Census projects that there will be 21,082,000 students enrolled in college in 2015. In that same year it is projected that 3,603,000 degrees will be conferred (U.S. Census, 2011). According to the National Center for Education Statistics NCES), postsecondary education is a $559 billion industry. There is a need for higher education to access leadership positions and to greater civic involvement (Floyd, 2007). Studies by Apling (1993), Kinser (2006) and Phipps, Harrison, and Merisotis (1999) have examined the student demographics at for-profit universities and found that in certificate programs the student is likely a white female, less than 24 years old from a low-income background. In four-year profit universities the profile is starkly different with the propensity of students being white males over the age of 29 years (Sheldon, 2009). The characteristics of the higher education student are changing as more adults are returning to the classroom to improve technical skills and receive degrees to become competitive in the changing, global economy. Balancing career and family, these mature students seek convenience and accelerated degree programs. Traditional public and profit nonprofit colleges attempt to accommodate this student segment with satellite campuses and distance learning programs but rising tuition costs and traditional curriculum lack attractiveness. For-profit universities, sometime referred to as proprietary schools, provide flexible scheduling with year-round enrollment, online options, small class sizes, convenient locations and credit for life experiences. The types of program for-profit institutions offer can also influence student decisions about enrollment (Morey, 2004). These higher education institutions have found economies of scale through the elimination of expensive facilities, tenured, research-centered faculty and athletics. These characteristics of for-profit universities are attracting a large and growing population of students entering the education market – particularly working adults, part-time students, and students with children (NCSL, 2014).

For-profit institutions have been in existence since the colonial era (Ruch, 2001). In the 19th century commercial schools were developed for the purpose of business training. After World War II, for-profits schools were receipts of the newly created G.I. Bill, providing educational opportunities for returning soldiers. It would not be until mid-1970 that for-profit universities would receive federal aid, utilized by a large portion of students. Since the early 1990's the undergraduate enrollment at for-profit universities has grown at a faster rate than public and private nonprofit universities in the United States. The past 20 years has seen the enrollment at for-profit universities increase by 225% according to the National Conference of State Legislatures (NCSL). In the ten year span of 2000 to 2010 enrollment at these schools grew to 1.7 million students (NCES, 2014). According to the National Center for Education Statistics, in 2012 for-profit universities conferred 207, 108 associate's; 132,654 bachelor's; 79,491 master's; and 5,852 doctor's degrees. Despite this growth in degree programs, certification programs still top the list at 430,457 awarded in 2012.

As previously discussed, the changing needs of higher education students and changes in the economy makes the cost of education a critical factor. Four-year for-profit institutions' average tuition and fees were $13,900 in 2012 compared to $28,100 at private nonprofits. Likewise, two-year for-profits averaged $14,200 for full-time tuition while private nonprofits averaged $14,300 (NCES,

2014). Morey (2004) posits that cost reduction strategies places for-profit universities above public postsecondary institutions but below private nonprofits, exactly in the desired target region.

A second financial benefit for a proprietary institution is its publicly traded status. Categorized as private-equity funds, these institutions are similar to venture capital. Private-equity funds typically by ownership or minority stake in established companies with a history of profits (Blumenstyk, 2003). These institutions are traded on both the NAS-DAQ and New York Stock Exchange. Due to recent stock mark volatility, private-equity funds have been the optimal choice to raise capital in the for-profit university segment. The streamlined and structured operations and curricula is attractive to investors as an indicator of potential high return on investment. The rapid growth of for-profit universities has made them viable investments, even for prominent college endowments such as Brown University and John Hopkins University. This article will conduct several statistical tests using data gathered from Fortune 500's top for-profit higher education groups. The following section will provide a brief overview of each company.

Graham Holdings, Inc. is a multi-division incorporating for-profit institutions, cable and television broadcastings. The former holding of The Washington Post newspaper, this company operates Kaplan Schools, founded in 1937, it is a mixture of test prep, higher education and professional learning centers. The companies postsecondary division, Kaplan Higher Education is composed of both domestic, professional learning centers with 16 campuses serving approximately 45,076 students. Kaplan University, a subunit within this division, offers online masters, bachelor's and associate's degree programs in education, business, criminal justice, healthcare and other fields. Kaplan University's 11 campuses and online courses enrolled approximately 42,900 in 2013. In the same year, the institution awarded 15,295 degrees. Kaplan University receives "higher scores than the national average in effective teaching practices, quality of interactions, learning strategies and higher-order learning" (www.ghco.com, p. 6). It is also ranked by U.S. News as the best online bachelor's degree program.

CEO, Donald Graham stated in the company's 2013 financial report that the future of their "U.S. higher education business is in question" (www.ghco.com, p. 4). This is due in part to governmental arguments to control tuition costs, increase the enrollment and graduation of minority students and to monitor the value of education against graduates' salaries. Mr. Graham states that the government is not focused on assisting for-profit universities in meeting these goals. Kaplan's response to government recommendations to have minority students repay a larger portion of their student loan is to reduce their program offerings that have served this student segment. To combat this issue as well as ensure that the minority student population was not overlooked, the company created the Kaplan Commitment. It is a multiple week trial period in which students can enroll in courses to determine if Kaplan Higher Education is a right fit. During this period the student incurs no cost but the program has generated a giant cost to the company, approximately $100 million since its 2010 inception. A result, Kaplan Higher Education's enrollment has been steadily decreasing from 80,000 in 2011 to 65,000 in 2013.

62% of Graham Holdings revenue is generated from its educational division (www.ghco.com). Operating revenues from 2011 to 2013 averaged $3,490,000 with average common stockholders' equity at 9.0% in 2013 (www.ghco.com). U.S. Federal student financial aid made up approximately 76% (approximately $819 million) of Kaplan Higher Education's revenue in 2013. Kaplan University reports in its 2013 financial statements that for their two-year student cohort default rates, the program averages at 15%, lower that the federal exceeding rate of 40%. Adjusting to market and demand changes, the company will continue its 2012 initiative to consolidate its market presence at some fixed-facility campuses. To address the growing governmental concerns, Graham Holding's CEO has vowed to continue to find ways to lower tuition costs, increase the enrollment and graduation of low-incomes students and provide measurable methods of the value and employability of a Kaplan University education.

Apollo Education Group was founded in 1973 and is the world's largest private education provider (www.apollogrp.edu) with subsidiaries such as Apollo Global and Western International University. Apollo's flagship subsidiary, the University of Phoenix, host 226 campuses serving 489,558 students in both online and classroom environments. The University of Phoenix offers a number of associate's; bachelor's; master's and doctoral degree programs in fields such as human services, psychology, business and technology. For the purposes of this study, the University of Phoenix will be examined, excluding the company's international education programs and professional development programs.

Overall the company's revenues and operating profits declined in 2013. The 2013 fiscal year brought the Apollo Education Group $3.7 billion in revenues, generating $2.19 per share, down from $3.22 per share in 2012. Of this total, $3,304,464 (90%) is attributed to the University of Phoenix. Student loan amounts can reach $12,500 for part-time students and $20,500 for graduate students (www.apollogrp.edu, p. 17). 83% of the university's revenue in 2013 was generated from tuition and fees with 77% of student loans making up the university's Title IV funds. The issue of student default rates is not a critical issue for the University of Phoenix's latest two- and three-year cohorts at 14.3% and 26% respectively in 2011.

CEO Greg Cappelli stated in the company's 2013 financial report that the "mission is to combine our education and career enhancement tools with our students' talents to move forward in life" (www.apollogrp.edu, p. 3). This effort includes providing educational experiences that directly correlate to a student's career choice. Apollo Education Group set several initiatives in 2013 including additional certificate programs, creating adaptive learning systems, implementing a new learning platform and developing new retention initiatives. Despite these efforts, the Apollo Education Group is also consolidating its locations by closing 115 campuses in 36 states. Additionally the company plans to streamline administrative and student services.

Education Management Corporation is a 40-year old company comprised of four student-centered subsidiaries – The Art Institutes, Argosy University, Brown Mackie College and South University. Operating in 107 locations in 32 states and Canada, Education Management Corporation serves approximately 132,000 students in campus, online and hybrid degree programs. Programs include media arts; information technology; culinary; fashion; and legal fields.

In 2013, Education Management Corporation generated $2.5 billion in net revenues with 73.4% of their gross receipts ($1,976,800,000) generated by Title IV financial assistance, this was down from 84.2% in 2012. This decrease also resulted in an earnings per share of -$2.15. In 2013, the company's net annual retention rate was 60%. For the past three years, none of Education Management Corporation's subsidiaries have not been greater than 25% for their two-year cohort student default rate.

The company has established the goal of achieving 1,000,000 graduates by 2020 (www.edmc.com, p. 4). This will be accomplished through increasing student retention and completion rates; improving tuition costs; fostered an engaged learning environment and protect the company's market share and reputation at the local, regional and national levels.

Founded in 1931, DeVry, Inc.'s mission is supports nine subsidiary, postsecondary institutions in the United States and abroad. This includes US-based DeVry University, DeVry Brazil, Chamberlain College of Nursing, and Ross University of medicine and veterinary medicine. Operating in 90+ locations, DeVry, Inc. serves approximately 160,000 students. Its associate's bachelor's; master's and doctoral programs cover a diverse career field including accounting; computer technology; healthcare administration; justice administration; and web graphic design.. 90% of its 2012 graduates are placed in the job market within six-months and with averages salaries of $43,500 annually.

In 2013 DeVry, Inc.'s revenue reached $1.96 billion, a decrease of 5% from the previous year. The company's shareholders' equity reached $1,397,156 compared to $1,356,393 in the previous year. Having a 13.3% four-year cohort student loan default rate, DeVry University's comparatively low

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cohort default rate is a direct correlation to its commitment to graduate employment success (http://www.devryfacts.com). DeVry has a two-fold plan for future enhancements including providing a more robust disclosure of student outcomes including tracking the number of graduates, those that continue to graduate school or employment and their ability to repay student loans. Secondly, CEO Daniel Hamburger proposes a change in the company's name to DeVry Education Group to reflect the educational environment while maintain is 80+ year reputation.

CRITICISMS AND BENEFITS

It is the entrance of the for-profit institutions into the core college curriculum that raises concern and presents challenges (Winston, 1999a). Some critics note that most students who enroll at for-profit universities do so because they were "advised" on a particular program from a sales team masked at "admission counselors". The uniform curriculum at many for-profit institutions does not allow the instructor the flexibility of teaching to the specific needs of the class. This adherence to a centralized curriculum can also be attributed to the lean faculty with many instructors fully employed within their field and are hired according to the scheduled needs of the institution. Another concern with for-profit curriculum is the student-centered evaluation of programs. 33-50% of traditional university faculty workload is centered on research. Without this function, faculty at proprietary institutions have more time for teaching (Morey, 2004). Unlike the grant and appropriations received from public and private, nonprofit universities, for-profit institutions view students as customers and evaluate programs and staff by the rating of its "customers." Authors such as Ruch (2001) posit that the mature student population at for-profits will demand rigor and relevance from their educational experience due to the need to attain professional certification. Morey's (2004) research found that the University of Phoenix prepare course syllabi every three years and offer no electives. Experts argue that curriculum rigidity and "customer satisfaction" does not ensure that students are receiving the education for citizenship and access to opportunities that accompanies a traditional public or nonprofit education (Morey, 2004).

A benefit of for-profit universities is that they are market driven but this is also weakness of these institutions as revealed by increasing student loans, competitive job markets and growing student loan defaults. Nearly 95% of for-profit university revenue is generated from tuition and fees (Ruch, 2001). According to NCES, two-year public colleges, derive 17% of revenue from tuition and fees with 71% from government grants and appropriations. Private nonprofits receive 74% from tuition and private for-profit 89%. The same 89% tuition and fee base serves as the main source of revenue at 4-year for-profit colleges where as 39% and 21% apply to private nonprofit and public colleges respectively. In 2011 student loan defaults at 4-year private for-profit universities over shadowed both public and private nonprofit at 13.4% compared to 6.8% and 5.1% respectively (NCES, 2014). Critics argue that programs leave students with large amounts of debt, few employable skills, and at a greater risk of not completing a degree at all (NCSL, 2014).

Increasing student loan defaults and pressures to further regulate for-profit universities' eligibility for student loans has attracted the attention of federal and state governments. The U.S. Department of Education issued the following release in 2013 regarding the issue financial aid eligibility for higher education institutions:

Certain schools are subject to sanctions for having two-year default rates of 25 percent or more for three consecutive years, or over 40 percent for one year. As a result, these schools will face the loss of eligibility in federal student aid programs unless they bring successful appeals. (U.S. Department of Education, 2013).

States such as Connecticut, Maryland and California have taken steps to, at some level, regulate for-profit universities to ensure proper allocation of student financial aid including monitoring student loan defaults (NCSL, 2014). Michigan, for example, has classified for-profit schools under the state department of energy and labor when enables schools to sell student product or services with proceeds supporting the school. This move from the jurisdiction of the state department of education

means these schools no longer have authority to confer degrees upon students. David Breneman, one of the editors of *"Earning for Learning: The Rise of For-Profit Universities,"* posits the regulatory environment will not present an obstacle to the growth of for-profit universities. The books cites that technological developments, unbundled services and economies of scale will continue to make this higher education segment a viable competitor in the years to come. Although most nonprofit universities initially did not view for-profits as a source of competition, public perceptions of the merit of this higher education segment has changed and traditional universities are beginning to take note (Newman and Couturier, 2001).

Due to the limited scholarly literature and empirical studies on for-profit universities and concerns regarding the viability of the education and increasing student loan defaults, this article pursues the examination of the relationships between program offerings, student loan default rates and earnings at proprietary institutions.

METHODOLOGY

This exploratory study will be empirical in design using secondary data from the financial statements of four for-profit institutions named in Fortune 500 2014 list as well as governmental reports. Using multiple regression with a confidence level of 95%, the study will provide an outcome for the following hypothesis:

Ho1: There is a significant relationship between student loan default rates and annual earnings.

H1a: There is no relationship between student loan default rates and annual earnings.

RESULTS

Regression tests was computed to assess the relationship between 2013 revenues for the identified for-profit universities and the 2010 two-year student default rates. Using a p-value of .05, the R value of .723 indicates a high degree of correlation. The test's r^2 indicates that 52.2% of the default rate explains the institutions' 2013 revenue. The hypothesis will be rejected and the alter hypothesis, that there is a significant relationship between revenue and student fault rates will be accepted.

A .544 KMO measure indicates that the small sample (N=10) size is adequate. Despite small correlations and student loans being the largest outlier at 23.2, the conformity of the Bartlett's test confirms that 63% of the relationships are explained by other variables. An analysis of the scree plot using Eigen values, shows there are three significant variables (see Appendix A). The type of institution has an initial communality of .671, lower than the remaining variables indicating a lower regression relationship.

Table 2.
Communalities[a]

	Initial	Extraction
Type of Insititution	0.671	0.619
any aid	0.99	0.999
Federal grant	0.986	0.977
Student loan	0.956	0.953
Work study	0.958	0.999
Vetrans' benefits	0.778	0.999
Parent PLUS loan	0.938	0.883

Extraction Method: Maximum Likelihood.

a. One or more communality estimates greater than 1 were encountered during iterations. The resulting solution should be interpreted with caution.

Finally, 91% of the total variance has been explained by the three significant variables with a goodness of fit of .432, indicating that there are no further shared variances in extracting additional factors (see Appendix B). The second hypothesis is rejected, accepting the alternative that there are dormant variables in the relationships of types of institutions and financial aid sources for undergraduate students in the US.

CONCLUSION

The need for education for career mobility have resulted in education becoming a lifelong necessity (Morey, 2004). Academia continues to monitor the impact for-profit universities. Most fundamentally, for-profit higher education and nonprofit education institutions are different at their core (Morey, 2004). The former's bottom line is to provide convenient and expedited education while maximizing profit. The latter's goal is to develop democratically well-rounded students that have experienced various echelons within academia. The curriculum structure of for-profit institutions centers on learning outcomes and practical application. This manifest in the flexibility and variety of degree programs. For-profit universities have demonstrated cost-efficient, consumer-oriented and profit maximizing ways of developing and delivering training programs (Morey, 2004). But this has also come at a cost at the majority of for-profit institution's revenues are derived from tuition and fees. The rising cost of education, cut backs in student loans and rising student loans defaults are beginning to impact this industry. This article's analysis were focused on the impacts of student default rates and financial aid on revenue. The results of the regression analysis determined that an institution's revenues are over 50% explained by the percentage results of student default rates. This also coincides with the literature's summary that the profiled for-profit universities are responding to federal government concerns in the rising student loan default rates, especially at proprietary institutions. The researcher acknowledges that there are limitations to the study including but not limited to the sample size used in conducting statistical tests; the selected examination period; and unknown errors with the secondary data used in the analysis; and time and data constraints in completing the research.

IMPLICATIONS AND FUTURE RESEARCH

Intended for financial stakeholders, the research will provide additional predictors in future financial aid, loan default and profits for these private-equity institutions. There are several avenues for future research in regard to this topic. The study may be expanded to include a larger sample for proprietary institutions in a comparison of earnings prior to and proceeding HEOA. An exploration of ethnicity, specifically in the U.S. Hispanic population, student loan default rates and revenues may be analyzed for a more detailed predictor of future financial trends in for-profit universities. Further research can conduct a longitudinal study regarding the financial growth or decline of for-profit universities based on campus location. Finally, longitudinal research may be conducted to observe a cohort's relationship between job placement rate, salary track and student default rates.

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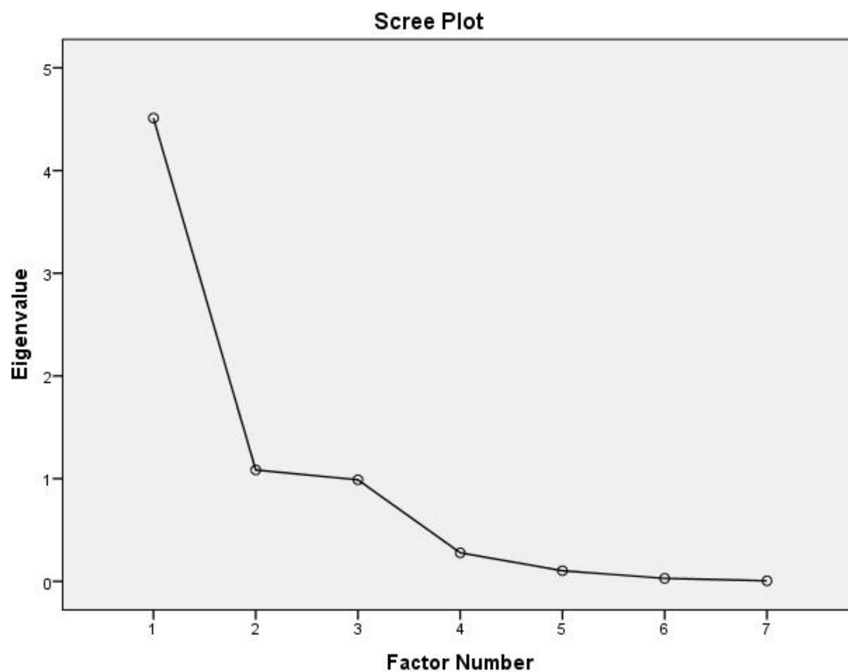
APPENDIX I - Eigen Values



APPENDIX II - Total Variance Explained

Factor	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings[a]
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total
1	4.511	64.44	64.44	3.768	53.835	53.835	4.208
2	1.085	15.494	79.934	1.384	19.773	73.608	1.211
3	0.989	14.126	94.06	1.276	18.226	91.834	2.073
4	0.278	3.973	98.033				
5	0.103	1.478	99.511				
6	0.029	0.415	99.926				
7	0.005	0.074	100				