**Department of Education**
**Notice of Proposed Rulemaking on**
**Program Integrity: Gainful Employment**
**(Docket # ED-2010-OPE-0012)**

***Submitted by:***
**The Coalition for Educational Success: Preparing the New American Workforce**

**Including: ATI Career Training Center; Concorde Career Colleges; YTI Career Institute; Beckfield College; Blue Cliff College; Dorsey Schools; Pacific College; Star Career Academy; Ogle School; Virginia College**

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## I. Introduction and Summary

A postsecondary education has become indispensible over the past several decades. With our changing economy, it is even more critical that the American workforce be well-trained and educated. Higher education, now more than ever, is a key component to a successful career. The Obama administration has acknowledged this fact with President Obama's goal of having the world's largest share of college graduates by the year 2020. To meet this goal, the country must graduate an additional eight million college students. See Sheryl Gay Stolberg, *Obama Calls for U.S. to Again Lead Graduate Rates*, New York Times, August 9, 2010. Unfortunately, this goal will be severely hindered, if not completely undermined, if the proposed regulation on gainful employment is finalized as written in the Notice of Proposed Rulemaking set forth by the Department of Education (the "Department") on July 26, 2010, at 75 Federal Register 43616 ("NPRM"). This regulation will drastically reduce the number of programs available to prospective students, decrease enrollment and graduation rates, and destroy any possibility of meeting President Obama's 2020 goal.

We respectfully request that the Department reconsider its proposed gainful employment regulation and develop further supporting data prior to publishing a final rule that is workable and applicable to all sectors. The current proposal for the debt-to-income and repayment ratios is unworkable and suffers from vagueness because it relies on data that neither the Department nor schools have on a programmatic basis. The rule does not address the Department's stated goal of encouraging institutions to improve their programs in order to better meet the needs of students and employers because the institutions do not have access to data that would allow them to learn ahead of time their programmatic debt-to-income or repayment ratios such that they know which programs require improved ratios.

The debt-to-income ratio in particular is unworkable as written because schools will not know that a program has failed the ratio until after the program has already failed. This ratio also fails to account for graduates who might have lower incomes due to temporary disabilities, or based on a decision to work part-time or to temporarily withdraw from the workforce in order to care for a parent or children. Using Bureau of Labor Statistics ("BLS") data would allow

institutions the opportunity to study and synthesize the debt and income data before facing any possible loss of programmatic Title IV eligibility. Even if the BLS data is used, however, it is more practical to allow a debt-to-income ratio of twelve percent of annual earnings, instead of the arbitrarily set eight percent figure.

The debt-to-income ratio will not accomplish the Department's goal of reducing program tuitions because the Department plans to determine student debt based on *all* debt the student incurs, well beyond the cost of tuition and fees. At the same time, the Department has established guidance that makes it very difficult for schools to stop students from borrowing more funds than they need to pay for their education. As a result, students may demand loan funding that well exceeds their tuition and fees based on federal formulas for loan eligibility, and increase a program's debt-to-income ratio regardless of moderate tuition and fee costs.

The repayment rate calculation likewise is unworkable because it fails to account for several categories of students who may be making payments on their loans but whose principal loan balance is not reduced in the single year that the Department will measure repayment. The repayment ratio would punish schools if their students temporarily dropped from the workforce or sought out government-sponsored and promoted protections such as deferment, forbearance, income contingent repayments, income based repayments, or interest only repayment programs. Further, schools have not had the opportunity to determine exactly how the Department is calculating the repayment rate or to obtain the underlying data.

Significantly, the proposed gainful employment rule fails to take into account the enormous effect it will have on women, minorities and students from low-income backgrounds. As illustrated throughout this comment, for-profit institutions provide the opportunity of higher education to a large percentage of students who would otherwise not attend a postsecondary institution. With a goal of graduating an additional eight million college students, a regulation that so severely restricts access to higher education is untenable. The Department's proposed metrics for gainful employment more accurately reflect the demographics of a school's educational programs than the quality of those programs. As such, the majority of programs terminated from the Title IV programs as a result of this rule would be programs that serve already underserved populations. In order to avoid this outcome, the Department should abandon the proposed rule. Alternatively, the Department's rule should consider as mitigating circumstances an institution's significant Pell eligible and minority populations.

The proposed repercussions of the gainful employment rule also are unworkable. First, the Department would have schools with a repayment rate below 45 percent and a debt-to-income ratio above eight percent of income (or 20 percent of discretionary income) provide a "prominent warning" in "all" materials. This disclosure requirement is overly burdensome and vague. Further, it is unprecedented. If the Department's goal is to ensure disclosure, a simple signed form would accomplish this goal. The gainful employment rule also would apply debt-to-income and repayment ratio data to programs within the same "job family" assuring that schools could not improve the curriculum or repayment rates of currently offered programs – which appears to be the opposite of the Department's stated goals. Moreover, the proposed rule would ignore data maintained by the Department of Labor and require schools to engage in an ad-hoc application process to seek approval for new programs, which process will be heavily impacted

by a few local employers and Department of Education personnel without any background in labor statistics or occupational forecasting.

For the reasons stated above, and for reasons further explained in these comments, the effective date of the proposed rule should be delayed to reflect the fact that institutions should not be held accountable for repayment rates and debt-to-income ratios for years prior to the publication of these proposed new standards. If the effective date of the regulation is set at July 1, 2014, schools will be on notice that these calculations will be made and will not face the possibility of being penalized for data set in prior years. Further, the underlying data should be published to schools and explained as needed well before the proposed rule becomes effective.

Students are in fact thriving at for-profit institutions as reflected in the graduation and placement rates at many for-profit institutions. If the Department proceeds with the onerous gainful employment regulation on the basis that the debt-to-income ratio and the repayment rate are legitimate and valuable measures of proper quality, then the rule should apply to all educational programs offered by all postsecondary institutions. Education provided by all sectors is foremost a means to employment, even if it provides many other benefits. Enforcing the proposed regulation against primarily for-profit institutions would constitute a thinly veiled attempt to reduce the number of for-profit institutions despite their innovation and progress with the most under-prepared students seeking postsecondary education.

The proposals set forth in this comment will maintain greater access to higher education while still protecting the Title IV programs.

## II. Comments to the Proposed Rule and Proposed Resolutions

We ask that the Department not finalize the proposed gainful employment definition as currently drafted and that the Department instead further study the data relevant to the repayment rate and debt-to-income calculation, provide the data to all institutions of higher education, and proceed with a phased implementation of the rule that allows institutions to review and react to the data provided. We ask this because the rule as currently drafted threatens to limit the availability of postsecondary education in America and because the data on which the relevant ratios are calculated is unknown to both the Department and its regulated entities. The Department must provide schools with more information, guidance and transparency regarding these calculations before they become effective.

### a. Comments to the Proposed Rule

*As requested by the Department, in order to ensure that these comments have maximum effect in developing the final regulations, we have clearly identified the specific section or sections of the proposed regulations to which each comment applies and we have arranged these comments in the same order as the proposed regulations. As a result, no priority should be assumed from the order of these comments. See NPRM at pg. 43616.*

i. Restricted Status and Debt Warning Disclosures

1. 34 CFR 668.7(a)(2)(ii), 34 CFR 668.7(d), 34 CFR 668.7(e) – Earnings Thresholds Should Be Adjusted From Eight Percent To Twelve Percent

We propose that the income threshold be adjusted from the current eight percent to at least twelve percent. The Department has offered no substantive justification for why eight percent is the appropriate threshold. The general rule of thumb is that 30 percent of annual income can be spent on housing costs. Mary Schwartz and Ellen Wilson, U.S. Census Bureau, *Who Can Afford to Live in a Home?: A look at data from the 2006 American Community Survey*, available at http://www.census.gov/hhes/www/housing/special-topics/files/who-can-afford.pdf. Housing and education are both major life investments which help pave the path to future security. Clearly, more than eight percent of income (as fixed during the first three years of employment) can be spent on paying for one's education. Increasing this threshold to twelve percent would be less than half of the expected upper level of spending on housing and would more accurately reflect the important role of education in our lives.

Alternatively, the Government Accountability Office ("GAO") has stated that "ten percent of first year income [i]s the generally agreed upon standard" for repayment of student loans. See Sandy Baum and Sal Schwartz, *How Much Debt is Too Much? Defining Benchmarks for Manageable Student Debt*, The College Board, 2006, pg. 2 citing GAO, 2003.

ii. Repayment Rate – 34 CFR 668.7(b) and (d)

1. 34 CFR 668.7(b)(1)(ii) – Only The Most Recent Data Should Be Used In Calculating Loan Repayment Rates

Pursuant to the proposed rule, the Department plans to analyze repayment rate data beginning in 2012 using data from the past four federal fiscal years. Therefore, institutions that for the past four years have complied with the statutes and regulations pertaining to Title IV eligibility could now be penalized because their past actions do not comply with newly proposed standards. It is clear that the Department is not legally permitted to retroactively apply its rules. The Supreme Court has established that the inquiry into whether a statute operates retroactively, "demands a commonsense, functional judgment about whether the new provision attaches new legal consequences to events completed before its enactment." *I.N.S. v. St. Cyr*, 533 U.S. 289, 291 (2001). The Department will thus have to satisfy the significant evidentiary burden typically faced by agencies seeking to conduct retroactive rulemaking, as the Supreme Court has asserted that there is a "presumption against retroactive legislation…deeply rooted in our jurisprudence." *Kaiser Aluminum v. Bonjorno*, 494 U.S. 827, 855 (1990).

Courts have consistently held that parties "should have an opportunity to know what the law is and to conform their conduct accordingly." See, e.g., *I.N.S. v. St. Cyr*, 533 U.S. at 316; Kaiser Aluminum, 494 U.S. at 855. The main reason that courts look unfavorably at laws with retroactive effects is that it is inherently unfair to punish a person or entity for past actions that when taken were entirely legal and in compliance with current laws. The proposed regulations

raise significant concerns with retroactivity and should be reconsidered; to avoid these concerns, the effective date of the gainful employment rule should be extended to July 1, 2014.

In addition, we request that the Department disclose, explain and confirm the accuracy of the National Student Loan Data System ("NSLDS") data on which it will base programmatic repayment rates. Many institutions' internal calculations do not appear to match Department calculations. Further, is not clear to many schools how repayments on consolidated loans are being treated, including where a student may have attended more than one school.

In summary, we agree that the Department should collect loan repayment related data over the next several years. However, in order to ensure that these new regulations are not applied retroactively, we propose that this data be published to institutions beginning in January 2011 and no adverse actions be taken against institutions until July 1, 2014 at the earliest. In 2014, the Department would be able to use 2009-2013 data without significant concern that its actions would be considered retroactive. Moreover, this delay would provide institutions and the Department time to test the underlying information and would provide additional time to institutions to determine what changes need to be made to their programs in order for them to meet the requirements of the gainful employment regulations. Without these revisions, institutions will be held accountable for events that occurred well before the repayment provision was proposed and for a ratio for which it lacks supporting data. We urge the Department to revise the repayment rule to clearly state that schools will not be penalized for data formed prior to the regulation's enactment, or July 1, 2014, whichever is earlier, and to allow for the publication to institutions of their repayment rate data, as well as a resource to obtain an explanation of that data, as needed.

2. 34 CFR 668.7(b)(3) – Repayment Calculations Should Include Payments On Loans That Are Subject To Interest-Only, Income Based and Income Contingent Repayment Plans

The numerator of the repayment calculation would include only those loans on which payments were made during the most recent federal fiscal year and reduced the outstanding principal balance on the loan (as well as any loans paid in full). The logic of including a loan in repayment only if it has had a reduction in principal during the most recent fiscal year is flawed. The government has made a policy decision to issue student loans that are not credit-based and to allow and even promote forbearances, deferments, loan consolidations, and income based and income contingent repayment plans. Many students, who are no different from the general population, will put off making payments today that they are *permitted* to make tomorrow. This is particularly true if the student left the workforce in order to attend school (or attended school as a result of being forced from the workforce) and needs some time to catch up on other priority payments such as housing, transportation or child care. But students also may choose to delay payments as a matter of sheer convenience. Schools should not be penalized because the government has determined as a matter of policy that it is appropriate to offer flexible payment plans and has left schools without the authority to control the payment plans chosen by their students.

Indeed, banks and other financial institutions rely on FICO scores, not income levels, to determine whether or not a particular individual will receive financing and how much it will cost

that individual to borrow money. A FICO score is comprised of the following factors: payment history (35 percent); total amount owed (30 percent); length of credit history (15 percent); new credit (10 percent) and type of credit in use (10 percent). See http://www.myfico.com/crediteducation/whatsinyourscore.aspx. Nowhere in this calculation does an individual's income come into play. This belies the Department's suggestion that it is commercially reasonably to associate a borrower's decision to choose income based repayment, income contingent repayment or interest-only repayment options with the quality of the institution's educational programs. More likely, a program's repayment rate as proposed by the Department is strongly related to the FICO scores of the enrolled students and, where applicable, their parents. Schools that understand this will begin redlining applicants according to their FICO scores in order to meet Department-imposed repayment ratios. This will disproportionately reduce educational access to minorities and low-income individuals.

Further, because the Department proposes to consider in repayment only those loans on which the principal has been reduced in the most recent federal fiscal year, the Department is ensuring that many loans that are currently being repaid but were in deferment at any time in the last two to four years will be excluded from the "repayment" category. See Mark Kantrowitz, *The Impact of "Persistence of Interest" on Loan Repayment Rates*, August 23, 2010, http://www.finaid.org/educators/studentaidpolicy.phtml.

The Department should consider a loan to be in repayment if a borrower has made at least four payments during the most recent fiscal year.

3. 34 CFR 668.7(b)(4) – Additional Types Of Deferments And Forbearances Must Be Excluded From The Repayment Calculation

The draft language in 34 CFR 668.7(b)(4) excludes from the repayment calculation "borrowers on an in-school deferment or a military-related deferment status." See NPRM at pg. 43638. This is a good first step. However, there are other borrowers who are not delinquent on their loans and do not meet these exceptions but have equally valid reasons for being on a forbearance or deferment.

The Department is exercising significant value judgments without explanation when it excludes from the calculation in-school deferments (which is likely to benefit two and four-year public and non-profit institutions and middle-class graduate students) but includes in the denominator (and not the numerator) deferments or forbearances obtained due to unemployment, maternity leave, disability, elder care or economic hardship. The Department requires schools and servicers to inform borrowers of their deferment and forbearance options. If a borrower chooses to leave the workforce for a period of time in order to care for children or a sick parent, or to have a medical procedure, that borrower's deferment or forbearance is just as legitimate as an in-school deferment. If a borrower's spouse loses his job, then that borrower may appropriately qualify for a forbearance, aside from the borrower's continuing employment. To exclude in-school deferments from the calculation and not other types of deferments is to say that generally middle-class borrowers who delay payment in order to obtain their graduate degrees are more responsible than borrowers who delay their payments in order to stay home

with children, provide elder care, resolve medical issues or pay other family bills during a difficult time.

The Department's proposed rule also does not anticipate any personal responsibility on the part of borrowers. Schools are required by the Department to allow students to borrow more than they need to pay for their education. The government offers forbearances, deferments and income based and income contingent payment plans that allow borrowers to put off for tomorrow the difficult task of repaying loans today and penalizes schools (and primarily for-profit schools) when they do. Students are no different than the general population and many students will choose the option of slower repayment because it is easier, just as many non-students choose to pay only the minimum balance on their credit cards. There is very little short-term impact on students if they opt for a slower repayment option. And yet, schools can have no impact on the repayment plans chosen by their students, particularly because students may change their plans well after graduation, including through loan consolidations.

The Department must either exclude from the repayment calculation all loans on which a deferment and forbearance is pending or it must enact strict standards for the issuance of deferments and forbearances.

iii. Debt-to-Income Ratio – 34 CFR 668.7(c)

1. 34 CFR 668.7(c) – Student Debt Should Include Only That Debt Obtained To Cover Tuition And Fees

The proposed rule currently includes in the calculation of median debt, *all* debt incurred by students who completed their program. This would include debt that is obtained for purposes other than the payment of institutional tuition and fees. And yet, the debt-to-income ratio contained in the NPRM will not cause schools to reduce tuition and fees unless the total amount of debt that is included in the ratio is capped at the cost of tuition and fees.

Students frequently over borrow and there is little that schools can do to prevent such practices. The Department has made it very clear that they are concerned with borrowing; however, the Department also makes it very difficult for institutions to deny students aid that is above the cost of tuition and fees. Institutions may reduce the amount that individual students may borrow only on a case-by-case basis and cannot refuse loans requested by students for living expenses. In fact, the 2009-2010 FSA Handbook states that a school "cannot engage in a practice of certifying Stafford loans only in the amount needed to cover the school charges, or to limit unsubsidized Stafford borrowing by independent students." 2009-2010 Federal Student Aid Handbook at p. 3-94. The Department has recently conducted several program reviews and criticized schools as part of those reviews for requiring students to explain why they need to incur debt beyond the level of tuition and fees. As a result, although the Department states that it is concerned about students taking out loans that they cannot afford, the Department has made it very difficult for institutions to reduce student borrowing.

The Department argues that the debt-to-income ratio will force schools to decrease tuition. See NPRM at pg. 43621. However, the Department should be well aware that due to the availability of stipends for "living expenses," decreases in tuition will not necessary reduce

student borrowing. For example, a student with maximum Title IV eligibility would be eligible to receive (and could demand) the same amount of student loan funds ($9,500) to help pay for a one-year academic program costing $15,000 as for a one-year academic program costing $10,000. This is true even if the student receives a $5,550 Pell Grant. The student enrolled in the program costing $10,000 could simply walk away with a $5,050 credit balance in this circumstance. As such, even if the institution that charged $15,000 for its educational program reduced the price of its program by 33 percent to $10,000, which is not a realistic expectation in many cases, this does not guarantee that student debt associated with the program will decrease.

The debt-to-income ratio as currently written will not cause schools to reduce tuition and fees because Department guidance and enforcement actions do not allow schools to limit student borrowing in any systemic manner. In order for the NPRM to have its desired effect, the total amount of debt that is included in the ratio must be capped at the cost of tuition and fees.

2. 34 CFR 668.7(c)(2) – Annual Loan Payments Should Differ Based On The Type of Program In Which A Student Is Enrolled

We urge the Department to revise its current assumptions under the debt-to-income ratio of a ten-year loan repayment amortization for all borrowers. The preamble to the NPRM states that "among bachelor's degree recipients in 1992-1993 who had student loan debt, about three-fourths fully repaid their loans in less than ten years." See NPRM at pg. 43644. As the Department acknowledges, however, this data is from "prior generations." See NPRM at pg. 43621. Much has changed in twenty years, particularly with the expansion of loan consolidations. Graduate students now borrow an average of $36,900 and those with loans at both the undergraduate and graduate levels borrow an average of $41,700. See National Center for Education Statistics ("NCES"), *Dealing With debt: 1992-93 Bachelor's Degree Recipients 10 Years Later*. The average amount of money borrowed from federal subsidized or unsubsidized Stafford loans or Supplemental Loans for Students by undergraduates at all types of institutions increased from $3,100 in 1992-93 to $5,000 in 2007-2008. See NCES, Table 1.1, *Trends in Undergraduate Stafford Loan Borrowing: 1989-90 to 2007-08*. Moreover, the percentage of undergraduates who borrowed any funds increased from 58.74 percent in 1992-93 to 79.5 percent in 2007-2008. See NCES, Table 343. *Percentage of Full-Time, Full-Year Undergraduates Receiving Aid, by Type and Source of Aid and Control and Type of Institution: Selected Years, 1992-92 through 2007-08*.

We strongly encourage the Department to determine the average repayment length for borrowers who went into repayment during the four most recently completed federal fiscal years in order to establish a more accurate assumed repayment amortization. We further propose that this amortization be subject to review every three years.

Alternatively, the amortization rate should vary depending on the program in which a student is enrolled. The amortization rates should be changed as follows: 15 years for certificate and associate's degree programs; 20 years for bachelor's degree programs, and 25 years for graduate degree programs. These changes are in line with the reality of the current cost of education and student repayment practices.

3. 34 CFR 668.7(c)(2) – Not Including Parental PLUS Loans As Debt In The Debt-to-Income Ratio Further Distorts The Ratio

The current NPRM excludes parental PLUS loans from the repayment rate. See NPRM at pg. 43639. As a result, loan debt levels associated with middle-class students attending public and non-profit universities is greatly understated. At the same time, the amount of debt students are claimed to undertake to attend for-profit schools is greatly overstated, since the majority of students attending for-profit schools are independent and low-income and therefore are more likely to receive additional support through unsubsidized Stafford loans instead of parent PLUS loans.

PLUS loans are federally guaranteed loans used predominantly by the middle class to support college students at non-profit and public institutions. They constitute educational debt and have a real cost to the federal government. The exclusion of these loans from the debt-to-income ratio reflects the Department's bias in depicting educational loan burdens and the costs of education attributable to various higher education sectors in general.

4. 34 CFR 668.7(c)(2) – Private And Institutional Loans Should Be Excluded From The Definition Of Loan Debt

The Department has stated that it is driven to propose the gainful employment rule based on the cost to the federal government of subsidized and unsubsidized federal student loans that are not repaid. See NPRM at pg. 43617-18. It is unclear then why the Department would consider private and institutional loans, which have no impact on the federal budget, in the debt-to-income ratio. Private loans should not be considered as "loan debt" under 34 CFR 668.7(c)(2).

iv. <u>34 CFR 668.7(c)(3) – Average Annual Earnings</u>

1. Average Annual Earnings Should Be Determined Using BLS Data So That Institutions Can Determine Regulation Requirements And Comply With Them

The Department cannot request institutions to adhere to regulations when they do not know what such regulations require. Currently, the Department proposes adding the following language to 34 CFR 668.7(c)(3), "The Secretary uses the most currently available actual, average annual earnings obtained from a Federal agency, of the students who completed the program during the 3YP . . ." when calculating the debt-to-income ratio. See NPRM at pg. 43639. The Department has already admitted that neither it nor institutions will have access to this information. Therefore, institutions will be entirely ignorant of the figures used to determine whether their programs are in violation of the gainful employment regulation and will have no ability to challenge the underlying data. Further, the schools will learn of noncompliance only after the data set is closed. The lack of access to the data compromises an institution's right to knowledge and notice. We strongly suggest that the Department return to the draft debt-to-income ratio presented in negotiated rulemaking and use the income statistics from BLS data to determine average annual earnings.

Institutions have access to and are already familiar with BLS data. They have developed an understanding of how actual wages relate to BLS data and how the statistical wages relate to program length and tuition and fees. By using BLS data, schools would be in a better position to assist students in determining and reducing their debt-to-income ratio. Using BLS data also would allow institutions to determine whether programs meet the Department's requirements and to make necessary changes prior to being subject to penalties for noncompliance. For example, if an institution determines that it does not have the ability to offer a particular program and also meet the proposed debt-to-income ratio for that program, then the institution can revise the program or it can teach out the students enrolled in the program and discontinue admissions to that program.

The Department states that the goal of the proposed regulation is to make institutions more accountable for the education they provide to their students. See NPRM at pg. 43618-43619. If this indeed is the goal, then schools must be informed *in advance* of the statistics that will be used by the Department to determine compliance. The use of BLS data is more equitable – it is available to institutions and provides them with the ability to at least estimate their performance with respect to loan repayment and gainful employment. Ultimately, the use of BLS data would enhance and encourage more transparency throughout the admissions and enrollment processes.

2. The Department Should Use The BLS Data When Determining Average Annual Earnings Because This Would Exclude The Possible Impact Of Graduates Employed In Cash Businesses.

Graduates who are in a mainly cash business, such as massage therapy or cosmetology, should not be included in the debt-to-income calculation because they will have a significant negative impact on a school's debt-to-income ratio. The National Center for Policy Analysis stated that in 1995, "it is estimated that Americans failed to report $630 billion in [adjusted gross income] on their tax returns." See Brief Analysis No, 273, Released on July 13, 1998. It was further reported in 2009 that that unreported income in the United States was as much as $2.25 trillion, "creating a ratio of unreported income to reported adjusted gross income that is approaching the peak levels of the World War II era" and that this unreported income is creating an unpaid tax liability of more than $600 billion for the federal government. See Kathleen Gallagher, *Underground Economy Thriving, UW Economist Says*, Milwaukee Wisconsin Journal Sentinel, April 13, 2009. While we do not condone the failure to accurately report income to the IRS, the Department must acknowledge that an underground economy exists and take that fact into account when proposing regulations that would calculate a debt-to-income ratio as a measure of program quality. Using the BLS data would reduce the impact of graduates who do not report their full income.

3. The Department Should Use The BLS Data When Determining Average Annual Earnings Because This Would Exclude The Possible Impact Of Graduates Employed Part-Time Or Temporarily Unemployed

The Department should use the BLS data to calculate debt-to-income ratios in order to avoid penalizing schools whose graduates choose to work part-time or choose to leave the workforce. Including part-time workers in the debt-to-income calculation would force institutions offering quality education to close down programs because their debt-to-income ratio will be drastically out of proportion. Such closures will have an enormous effect on female-dominated programs such as health sciences, for which, in 2003-2004, women constituted over 83 percent of the student population. See NCES, *Percentage Distribution of Credential-Seeking Undergraduates, by Sex, Race/Ethnicity, Age, Curriculum Area, Credential Goal, and Career Field of Study: 2003–04* at http://nces.ed.gov/surveys/ctes/tables/P51.asp.

For-profit institutions are attractive options to many low-income women because they provide necessary support services and programs that lead to professions with flexible schedules including cosmetology, nursing and other allied health professions, and massage therapy. The for-profit sector serves these students better than their traditional counterparts. In 2004, 58.3 percent of women completed certificates or associate's degrees within 150 percent of normal time at for-profit institutions. Publicly funded institutions saw only 24.2 percent of such female students graduate. Not-for-profit institutions graduated 45.7 percent of their female students enrolled in certificate or associate degree programs. See NCES, Digest of Education Statistics: 2009, Table 331. *Graduation Rates of First-Time Postsecondary Students who Started as Full-Time Degree Seeking Students, by Sex, Race/Ethnicity, Time between Starting and Graduating, and Level and Control of Institution where Student Started: Selected Cohort Entry Years, 1996 through 2004*.[1]

Fields like health sciences often provide employees, such as working mothers, the opportunity to work part-time. Some women attend school in order to obtain a higher paying job so that they can earn the same salary for skilled part-time work that they earned for unskilled full-time work. The Government Accountability Office ("GAO") has noted that "women are much more likely to work part-time or take leave from work to manage home and family responsibilities, such as caring for children." See GAO Report to Congressional Requesters, *Women's Earnings: Work Patterns Partially Explain Difference between Men's and Women's Earnings*, October 2003. In 2004, women working part-time made up 25 percent of all female wage and salary workers. See NCES, Table 3.14 *Percentage Distribution of Credential-Seeking*

[1] Similarly, the Program Policy Analysis & Government Accountability ("OPPAGA") Report from the Florida Legislature states that, compared to public institutions, "private [career education] programs generally had higher ratios of program graduates to students enrolled in 2007-2008" and "were more effective in producing program graduates." See OPPAGA Report at pg. 11. The report also found that graduates from public and private career education programs earned comparable wages. See Id. at pg. 12.

*Undergraduates with Each Major Field and Level of Credential Sought, by Dependency Status, Financial Aid Status, Previous Bachelor's Degree, and Postsecondary GPA: 1990, 2000, and 2004* at pg. 105 of the Statistical Analysis Report on Career and Technical Education in the United States, 1990-2005 and *Part-Time Workers: Who They Are and How Much They Earn*, U.S. Bureau of Labor Statistics, November 3, 2004.

The real life impact of the above statistics is that women are more likely to have lower incomes than their male counterparts. Therefore, females who must obtain loans in order to complete an educational program and who then must work fewer hours per year in order to care for children or attend to other familial responsibilities are likely to have a higher debt-to-income ratio and a lower repayment rate than males who complete the same program.

If the Department includes in the debt-to-income calculation graduates who work part-time or who temporarily leave the workforce then this will create a downward spiral. Programs that lead to occupations where part-time employment is readily available, such as the health sciences field, will lose Title IV eligibility because they fail to meet the gainful employment regulation. Women, who, as working mothers, find these occupations attractive, will have fewer higher education opportunities in that field. As a result, thousands of predominantly low-income women hoping to better their future will be without the means to an education. Given that for-profit institutions graduate certificate and associate degree seeking female students at a higher rate than any other sector (and a significantly higher rate than the public sector), it is inexplicable why the Department would penalize these programs simply because the women they graduate must balance work with caring for their families.[2]

To resolve this anomaly, the Department should use BLS data in order to calculate programmatic debt-to-income ratios. Alternatively, if the Department bases the debt-to-income ratio on actual income, including graduates who choose to work part-time or stop out from the work force, then it must also implement a procedure whereby programs that enroll female students do not suffer from this trend. This could be accomplished by adding a multiplier to the average annual earnings commensurate with the proportion of enrolled females in a particular educational program.

4. The Department Should Use The BLS Data When Determining Average Annual Earnings Because This Would Not Penalize Institutions Offering Programs That Generally Lead To Self-employment

Earnings amounts for self-employed individuals are not reported to the Social Security Administration ("SSA"). Schools that offer programs that may lead to self-employment would be harmed by the lack of data to calculate a debt-to-income ratio. Further, the proposed regulation does not consider the impact of sole proprietorships on the debt-to-income ratio wherein the company receives the income and pays the employee/owner a salary, which salary may be relatively modest if the company is also providing the employee/owner with health care,

[2] It is also inexplicable why the Department would not apply the same standards to the other sectors of higher education without limitation. See comments in section II, c, vii.

housing, transportation, and other benefits. Each of these factors would be mitigated through the use of BLS data.

5. Use Of 3YP Data

The proposed rule would calculate a program's debt-to-income ratio based on the income received during only the first three years of employment. This does not take into account the life-long benefit of higher education. A graduate will earn more money as he or she gains experience and responsibility. This is expected in any profession. Students clearly would have more difficulty repaying their student loans if they remained on the bottom rung of the earnings ladder throughout their career. However, that is not what happens. Instead, in early years, the loan repayments require a larger portion of the borrower's income and this is a bargained-for sacrifice. As the graduate becomes more established, however, the loan repayments become easier such that some graduates can pay off the remainder of their loans in a lump sum in either the 10th or 15th year of repayment. The Department should use the BLS data to determine the 50th percent level of income for students in a particular profession which will more likely track what a student would make within the first 10 years of his career. For those professions not requiring a graduate or first professional degree, the Department should assume a 75 percent earnings level for graduate borrowers.

6. Use Of P3YP Data

Under the proposed regulation, the Department will require institutions to prove that their graduates' salaries increase substantially in order to use prior 3YP salary information. However, institutions do not have this data. There also is no reason for requiring this proof. The Department can obtain income data for six prior years as easily as three prior years.

We suggest that the Department automatically calculate the debt-to-income ratio over the 3YP period as well as the 3PYP period and then provide schools with the benefit of the most favorable calculation. This will still provide the Department will the opportunity to review the debt-to-income ratio of program graduates but it will also provide some flexibility to institutions with respect to an otherwise very rigid and complicated calculation.

v. <u>34 CFR 668.7(d) – Debt Warning Disclosure</u>

The NPRM proposes that programs that do not maintain a 45 percent repayment rate or do not maintain a debt-to-income ratio that allows for payment of debt with "at least" (sic) 20 percent of discretionary income must provide a "prominent warning" in their promotional, enrollment, registration and all other materials in order to alert prospective and currently enrolled students that they may have difficulty repaying loans obtained for attending the program. See NPRM at pg. 43639. This same disclosure must include the program's most recent loan repayment rate and debt-to-income ratio. It is not feasible to provide a "prominent warning" in the average newspaper or TV advertisement, in every sign that advertises the program, or "all other materials" as the proposed overly broad rule states.

The Department maintains requirements for a variety of disclosures, from campus crime, to graduation rates, to descriptions of federal student aid programs. The specific manner of disclosure is not mandated. The Department's suggestion that schools must include a prominent warning regarding this single issue of debt-to-income ratios and repayment rates in "all other materials" is unprecedented. If the Department takes this approach, then it should also require the same prominent and ubiquitous warnings for every community college advertisement where that college has less than a 50 percent graduation rate, in the advertisements of every school with an athletic program that graduates less than 75 percent of its athletes, and in the advertisements of schools that graduate substantially less of their minority students than their non-minority counterparts.

The unprecedented nature of the disclosure requirements proposed in the gainful employment rule causes the rule to appear punitive instead of informative. If the Department wishes to require disclosure, it should require institutions to demonstrate that for those programs with a repayment rate of less than 45 percent and an annual loan payment that is greater than 20 percent of discretionary income or eight percent of average annual income, the institution provides written information to each applicant regarding its gainful employment rates. Schools could be required to obtain a signed notification from each student applying to an affected program in order to demonstrate that such notification is made prior to enrollment.

vi. 34 CFR 668.7(d) and (f) – Effective Date

The Department should not initiate any actions against a school based on the debt-to-income and repayment rate ratios prior to July 1, 2014.

The proposed regulation introduces two completely novel indicators that the Department believes measure the quality of education: loan repayment rates and debt-to-income ratios. As currently drafted, the NPRM fails to provide institutions a manner to determine whether or not they are in violation of these new standards. Without access to this data, it is incomprehensible how the Department can expect institutions to alter their behavior or comply with the regulation. Since it is not apparent that institutions will be privy to the information used by the Department to determine compliance, schools should have the opportunity to review the calculations and attempt to correct any problematic areas before any programs lose eligibility for Title IV funding. This process must include appeal rights.

If the Department adopts the proposed rule, we strongly suggest that language be added to provide a grace period to institutions, *without associated restrictions,* that initially fail to comply with the gainful employment regulation. Allowing institutions the chance to become compliant before adverse action is taken enables institutions to improve their programs in a timely manner while ensuring that potential students are not discouraged from pursuing postsecondary education.

This proposal to amend the effective date to July 1, 2014 is in line with the Department's stated goals of increasing repayment rates on student loans and reducing student debt load. Congress has set an appropriate example for such a phased in approach through the implementation of the three-year cohort default rates.

vii. 34 CFR 668.7(d) and (f) – Mitigating Circumstances – Percentage Of Pell Recipients

The Department of Education's rule should allow for lower repayment rates based on the percentage of Pell Grant recipients, or full eligibility Pell Grant recipients a school enrolls.

Higher education is now available to many types of students who otherwise would not have the opportunity to obtain a postsecondary education. Proprietary schools offer students open-enrollment and efficient course scheduling which greatly increases postsecondary opportunities to students who would have a limited chance of acceptance at schools with selective or even quasi-selective admissions processes, or who otherwise would attend community colleges. As community colleges begin to deny admission to those seeking an education and experience continued overcrowding, proprietary schools' open-enrollment policies are now and will become even more vital to the education of such students. See Caralee Adams, *Community Colleges Rethink 'Open Door' Admissions as Remedial Costs Rise*, Education Week, August 13, 2010 and Lisa W. Foderaro, *Two-Year Colleges, Swamped, No Longer Welcome All*, The New York Times, November 11, 2009.

While the NPRM correctly states that "[s]tudent loan debt is higher among graduates of for-profit institutions" it fails to acknowledge that loan debt is higher because a larger percentage of for-profit institution students are lower-income students - students for whom financial aid is the only way to pay for their education. See NPRM at pg. 43642. Richard D. Kahlenberg, senior fellow at Century Foundation Press and editor of Rewarding Strivers, stated that "Most colleges don't consider socioeconomic status in admissions. . . Being poor does not increase one's position at all at the selective institution." See Michelle J. Nealy, *Race, Class, and College Access Explored in 'Strivers' Research,* Diverse Education, June 18, 2010. For-profit institutions are able to offer a postsecondary education to students despite their socioeconomic status. Highlighting this fact, NCES has found that 50 percent of dependent students at for-profit institutions come from a family with a household income of less than $36,000. See NCES, *2008 Undergraduates Dependent Median Income Statistics*. In comparison, less than 14 percent of dependent students attending community colleges have a household income of less than $36,000, less than 18 percent of dependent students attending four-year public institutions come from a household income of less than $36,000, and less than 17 percent of dependent students attending four-year private institutions have a household income of less than $36,000. Id. at Table SA-9. Further, a study from 2003-2004 reflects that 76.1 percent of students at private for-profit institutions were independent (i.e., with no parental support) versus 34.3 percent of students at public four-year institutions, 61.2 percent at public two-year institutions and 37.7 percent at private non-profit, four-year institutions. See NCES, *National Postsecondary Student Aid Study 2003-2004*, Table A-2 at pg 35. NCES data reflects that 50 percent of independent students at for-profit institutions have a median income, including spousal income, of less than $20,000, as compared to almost $30,000 for students at community colleges. See NCES, *2008 Undergraduates Independent Median Income Statistics*. Clearly the for-profit institutions are serving a greater percentage of needier students than any other sector of higher education.

As impressive as it is that for-profit institutions can offer an education to students from such low-economic backgrounds where other institutions are unwilling or unable to do so, the

Department must realize that *with increased access comes increased need-based financial aid*, remedial training, and failure. If the government wishes to reduce the debt level of postsecondary institution graduates, it must review and improve the access that working class and low-income students have to grants. The gainful employment regulation ignores this fact. Given that minorities and lower-income students attend for-profit institutions at a greater rate than other private and public institutions, this regulation will have a disproportionate impact on the students who struggle and sacrifice the most in their quest to obtain an education.

Finally, although the Department's rationale for this rule is the cost of student debt (unpaid, delayed payment, or defaulted) on the federal government,[3] the charts on pages 43633 and 43699 of the NPRM show that most of the savings that the Department expects from this rule will result from Pell Grants that are not made to the poorest students, not from savings in the loan programs.

viii. 34 CFR 668.7(d) and (f) – Mitigating Circumstances – Demographics Of Student Body

The Department's rule should allow for lower repayment rates and debt-to- income ratios based on the demographics of the school's student body and its success rate in graduating minority students.

One unintended consequence of the proposed regulation is the devastating effect that the NPRM will have on minority and female students. A review of data provided by NCES reflects that African American and Hispanic students account for over 45 percent of the student population at for-profit institutions. In comparison, public institutions have an African American and Hispanic population of approximately 27 percent and these populations make up less than 25 percent of private non-profit institutions.

Despite these stark differences in student body statistics, the graduation rates of Hispanic and African American students from for-profit institutions are extremely close to the graduation rates at four year public and private institutions and significantly higher than the graduation rates at two-year public and private institutions. See NCES, *Enrollment in Postsecondary Institutions, Fall 2008; Graduation Rates, 2002 & 2005 Cohorts; and Financial Statistics, Fiscal Year 2008*, Page 14, Table 5, August 2010. In 2002, African Americans graduated at four-year for-profit institutions at a rate of 32.8 percent. This figure is just slightly lower than the national average graduation rate of African Americans at four-year institutions (38.9 percent). At four-year for-profit institutions, Hispanics graduated at a rate of 42.4 percent while public institutions have only a marginally higher graduation rate of 43.1 percent of their Hispanic population. In some

[3] See NPRM at pg. 43622 ("The second cost is taxpayer subsidies. When a borrower is unemployed or is forced because of low income to obtain a forbearance or deferment, the Government waives the interest on subsidized Stafford and Perkins loans. For example, the cost to the Government of three years of deferment is up to 20 percent of the value of the loan. Also, borrowers who have low incomes but high debt may reduce their payments through income based or income contingent repayment programs. These programs can either be at little or no cost to the Government or as much as the full amount of the loan with interest.")

cases, for-profit school graduation rates far outperform those from public and private institutions. For example, in 2005, two-year for-profit institutions graduated 49.1 percent of their African American students and 62.6 percent of their Hispanic students whereas two-year public institutions graduated African American and Hispanic students at the starkly low rates of 14.4 percent and 16.8 percent respectively, and two-year non-profit institutions graduate these students at rates of 40.6 percent and 45 percent, respectively. Id. It seems incongruous that the Department would support a regulation that so disproportionately affects for-profit schools and their students when graduation rates show that for-profit institutions are clearly succeeding in meeting the needs of African American and Hispanic students even where public and private institutions have failed.

It is no coincidence that for-profit institutions enroll a higher percentage of minority students and a higher percentage of low-income students. Indeed, these populations overlap substantially. For-profit institutions have flung their doors open to traditionally underserved populations and have served them better than traditional institutions of higher education. However, with these underserved populations come a lower repayment rate and even a lower debt-to-income ratio since these underserved populations still are more likely to be unemployed or to find lower paying jobs than their middle or upper income peers.

The fact that the repayment rate in particular is more an indication of a school's demographics than the quality of its programs is best demonstrated by the loan repayment data released by the Department on August 13, 2010. "For the 89 historically black colleges in the department's Excel spreadsheet, according to one estimate, the mean loan repayment rate was 20 percent, and a full 93 percent fell below the 35 percent threshold that would make for-profit colleges ineligible for aid under the department's scheme." See Doug Lederman, *Damaging Data on Loan Repayment*, Inside Higher Ed, August 16, 2010. Similarly, the average repayment rate of Hispanic Serving Institutions ("HSI") is approximately 42 percent with 121 institutions out of 225 HSI's (54 percent) under the 45 percent repayment rate threshold and 69 institutions (30 percent) under the 35 percent repayment rate threshold. A review of the repayment data thus shows that schools with higher percentages of PELL grant students and schools that serve a higher proportion of minorities generally have lower repayment rates than more selective institutions.

These issues have not gone unnoticed by minority advocacy groups. Harry Alford, president of the National Black Chamber of Commerce, expressed his concern with the proposed gainful employment regulation stating "Gainful employment will disproportionately harm low-income and minority populations by discriminating against students who must borrow the needed tuition to attend college. At present, Black students make up 18 percent of enrollees in for-profit colleges and universities – many of them would find it impossible to pursue higher education without this financial aid. Many of these private sector schools are the solution to our education challenges, not the problem." See Press Release, *Department of Ed Rule will Limit Access for Black Students*, July 23, 2010. Similarly, MANA, a national Latina organization, stated that "Implementation of the Gainful Employment Rule would deny Title IV financial assistance for [programs that serve minority populations]. . . This will adversely affect Hispanic students' ability to borrow money and will limit Hispanic students' access to higher education . . . any effort to lift the burden of student debt should not reduce educational opportunities for many

Hispanic and low-income students." See Press Release, *MANA Expresses Concern Over Impact of U.S. Department of Education's 'Gainful Employment' Rule on Minority Students*, July 23, 2010. The National Organization of Black Elected Legislative Women (NOBEL/Women) and the National Hispanic Caucus of State Legislators released similar press releases on July 26, 2010.

Although the Department states that the purpose of the loan repayment rate requirement is to reduce student debt, the primary effect will be to reduce access to higher education for those who need it most. See NPRM at pg. 43617-18. To obtain President Obama's goal of having the world's largest share of college graduates by the year 2020, access to postsecondary education for minorities and low-income students cannot be diminished.

ix. 34 CFR 668.7(g) – New Programs

1. 34 CFR 668.7(G) – The Department Should Rely On Published Department Of Labor Data In Determining Which New Programs May Be Approved

As currently drafted, the NPRM would require that all new programs receive approval from the Department "by providing documentation of the approval of the substantive change by its accrediting agency, providing projected five year enrollment estimates, as well as, obtaining documentation from employers not affiliated with the institution, that the program curriculum aligns with recognized occupations at those employers' businesses, the number and locations of the businesses, and that the projected number of job vacancies are commensurate with the anticipated size of the program." See NPRM at pg. 43636. Neither Department employees nor local employers should able to control the programs that a school may introduce. Rather, data published by the Department of Labor should be relied upon in order to confirm or deny new program eligibility, with appeal procedures allowed so that institutions can demonstrate the potential need for their programs.

We do not believe that it is within the Department's domain to regulate occupations or the substance of academic programs. See 20 U.S.C. §2306a (2010) ("Nothing in this chapter shall be construed to authorize an officer or employee of the Federal Government to mandate, direct, or control a State, local educational agency, or school's curriculum, program of instruction …"). However, if the Department insists on limiting the types of programs that may be offered to students who require financial aid in order to obtain a postsecondary education, we also do not believe that the Department maintains the expertise to determine which occupations will demonstrate future growth. Instead, the Department should rely on data already produced by the United States Department of Labor – which has a tremendous amount of expertise in historical and projected labor statistics – in determining which occupations are sufficiently promising to warrant the development and eligibility of additional educational programs. Specifically, the Department of Labor maintains an Employment Projections Program through which it "develops information about the labor market for the Nation as a whole for 10 years in the future." See http://www.bls.gov/emp/. The Department of Labor also maintains an *Occupational Outlook Handbook* that includes for each occupation the training and education

needed, earnings, expected job prospects, what workers do on the job, and working conditions. See http://www.bls.gov/oco/. This Handbook is updated every two years.[4]

One benefit of using BLS data is that institutions also will have access to this data and can confirm the need for new programs before substantial funding is expended to develop these programs. In addition, the Department would leave itself open to endless appeals if it were to determine the eligibility of new programs through ad-hoc employer recommendations and decisions made by Department of Education employees who lack expertise in the labor markets. The Executive Branch maintains a separate agency devoted to labor issues and it would be arbitrary and capricious to ignore that agency's data in favor of the ad-hoc decision making process that the Department proposes in the gainful employment rule.

The Department also proposes to apply existing debt-to-income ratio and repayment ratio data to new programs that are in the same "job family" as those programs already offered by an institution. This approach would prevent institutions from revising current programs in order to improve their content and possibly their debt-to-income and repayment ratios. Schools must be allowed to improve programs over time, which may result in "substantive changes" to those programs. Under the Department's proposed rule, those "substantive changes" would be viewed as new programs subject to old debt-to-income and repayment ratios. Any such approach to approving new related programs will inhibit institutions from improving their academic programs.

Finally, the Department should establish an appeal process whereby an institution may appeal any decision by a case team to deny the eligibility of a new educational program. The decision maker in such an appeal process should have substantial expertise in curriculum development and analyzing labor trends and occupational needs on a national and regional basis.

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[4] The potential to stifle innovation is clear. For example, Sunday's Miami Herald highlighted a Maryland Community College whose proximity to the National Security Agency led to a partnership for training cyber combatants, whose job it will be to defeat computer hackers and purveyors of malicious software. "We will map course curricula to those new job titles . . . we're talking about a whole new work force that doesn't exist today," said Kelly Koermer, the dean of the School of Business, Computing & Technical Studies, home of the Cyber Center. Kevin G. Hall, *Unemployment Creates New Role, and Pain, for Community Colleges*, Miami Herald, September 5, 2010. If schools were required to seek prior approval from local employers and the Department of Education for programs that would train a "new work force that doesn't exist today", they might never be approved under the Department's new standards. The Department's proposed rule would stifle innovation at community colleges and for-profit schools alike. Again, it is not the Department's domain to regulate upcoming occupations or the development of curriculum.

b. **The Rule Should Include the Following Additional Provisions**

i. The Department Should Consider Current Economic Conditions When Determining The Impact Of Repayment Rates And Debt-To-Income Ratios

Institutions should not be penalized for occurrences that are beyond their control. However, this is exactly the potential of the proposed rule. Since May 2009, the unemployment rate in the United States has been at least nine percent. The unemployment rate in New York City alone has hovered around nine or ten percent over the past year and "[reached] its highest level in nearly 17 years." See Patrick McGeehan, *City's Jobless Rate Rises to 10.6%*, New York Times, January 21, 2010. In March, the state of Florida reported that its unemployment rate hit a record 11.9 percent, which "ties a state record originally set way back in 1975." See Glen Osrin, *Miami Unemployment Rate Hits 11.7%; Worst Yet to Come?*, Examiner.com, March 11, 2010. The unemployment rate in Miami, in particular, was over 12 percent in March 2010. See David Volz, *Miami Dade's Unemployment Rate is 12%*, Examiner.com, April 17, 2010. The BLS reported June 2010 unemployment rate in Michigan at 13.2 percent, Ohio at 10.5 percent, Texas and New Mexico at 8.5 percent, and 8.3 percent in Louisiana. Although postsecondary institutions have been working to help their graduates find employment, some of these graduates, who are seeking employment in a very tough job market remain unemployed.

Penalizing institutions now for having a high percentage of graduates who are unemployed is counterintuitive. Studies have shown that unemployment rates are tied to lower levels of education. A 2009 BLS survey revealed that individuals with only a high school degree have a 9.7 percent rate of unemployment, compared to the 5.2 percent rate for individuals with a bachelor's degree. See 2009 Employment Projections, *Education Pays in Higher Earnings and Lower Unemployment Rates*, available at www.bls.gov/emp/ep_chart_001.htm.

The Department has realized the link between the economy and the repayment of student loans. See David L. Futrell, *Expected Jump in Cohort Default Rates May Surprise Some Schools*, posted on www.NASFAA.org, August 19, 2010. The NPRM should have a mechanism for considering current economic conditions when determining the validity of repayment rates and debt-to-income ratio results. We strongly suggest that the Department suspend or adjust the gainful employment calculation for periods when national unemployment is above seven percent. In the past twenty years, the yearly unemployment rate has exceeded seven percent only two times, once in 1992 with 7.5 percent and in 2009 with 9.3 percent. Since unemployment can vary widely across the United States, we also suggest that the rule be suspended for states or regions that have an unemployment rate above seven percent even when the national unemployment rate might be below this threshold. Providing institutions with this exception during times of high unemployment will provide appropriate mitigation related to gainful employment calculations.

ii. The Department Should Exempt Graduate Programs From Gainful Employment Regulations

As currently drafted, the regulation applies to all postsecondary education institutions, including graduates schools. However, given the maturity of graduate students and the large amount of money they are able to borrow, graduate students are a completely distinct class of students compared to students enrolled in associates' degree, bachelor's degree, or certificate programs and should be excluded from the regulation.

Graduate students are sufficiently sophisticated to determine whether they can afford the education that they seek. Moreover, graduate student borrowing limits are extremely high and schools are not able to freely deny access to student loans. In 1992-93, bachelor's degree recipients borrowed an average of $10,000 to help pay for their undergraduate education. Comparatively, graduate students with loans only at the graduate or first-professional level borrowed an average of $36,900 and those with loans at both the undergraduate and graduate levels had borrowed an average of $41,700. See NCES, *Dealing With Debt: 1992-93 Bachelor's Degree Recipients 10 Years Later*. These numbers are undoubtedly significantly higher today. On the other hand, in 2005 "[t]hose with master's degrees earned almost twice as much, and those with professional degrees earned over three times as much per year as high school graduates. In addition, those with professional degrees paid almost $19,000 more in total taxes in 2005 than high school graduates." See Sandy Baum and Jennifer Ma, *Education Pays. The Benefits of Higher Education for Individuals and Society*, The College Board, 2007, page 12. According to the same study, on page 10, the median *lifetime* earnings of those with Master's degrees can be expected to be almost twice as much as a high school graduate's, between two and two and one half times greater for those with a Doctoral degree as compared to high school graduates and even higher for those with a professional degree.

It is illogical to expect graduate students to repay their loans at the same rate as students who owe $26,000 to $32,000 less than they do. It is also illogical to assume that the substantial differential in pay for those with advanced degrees will be apparent in their first three years of post-graduation employment. Instead, the Department should exempt graduate programs from the gainful employment ratios or it should calculate the debt-to-income ratio assuming graduate students i) will repay their more substantial borrowing over a 25 year period and, ii) will earn at least the median salary shown for an occupation under BLS data (and 75 percent of the salary for those professions not requiring a graduate degree).

If graduate programs are subjected to this regulation as written it is doubtful that any graduate program at a for-profit institution will pass the debt-to-income ratio standard. These programs will be at great risk of being deemed ineligible and fewer students, and particularly fewer minorities, will be able to pursue graduate education. A regulation that results in reducing the number of highly educated individuals is clearly out of sync with the goals of the Obama Administration.

c. **General Comments in Response to the Preamble**

i. The NPRM Is Unconstitutionally Vague Thus Violating The Due Process Clause

The proposed rule contravenes the due process clause because it is unconstitutionally vague and would have an impermissible retroactive effect on proprietary institutions. In order to satisfy constitutional due process, regulations must be sufficiently specific to give regulated parties adequate notice of the conduct they require or prohibit. *Gen. Elec. Co. v. EPA,* 53 F. 3d 1324, 1328 (D.C. Cir. 1995) (citing *Gates & Fox Co. v. OSHRC*, 790 F. 2d 154, 156 (D.C. Cir. 1986)); *JIGC Nursing Home Co. Inc. v. Bowen*, 667 F. Supp. 949, 958 (E.D.N.Y. 1987) ("An agency cannot employ a standard so vague that it fails to give notice of how to present one's case."). As currently drafted, the proposed rule fails to provide constitutionally adequate notice to institutions to determine whether they would be in compliance with the gainful employment regulations.

The Department proposes the following language be added to 34 CFR 668.7(c)(3) concerning debt-to-income ratio, "[t]he Secretary uses the most currently available actual, average annual earnings obtained from a Federal agency of the students who completed the program during the 3YP…" NPRM at pg. 43639. The Department has confirmed that if it obtains the income data for the debt-to-income ratio from the SSA or the Internal Revenue Service, institutions will not have access to this data for privacy reasons. Thus, an institution will have no means of determining whether it is in compliance with the debt-to-income requirements until it is notified by the Department that it is non-complaint. And, the institution will never have a full opportunity to contest the accuracy of those findings. While the rule proposes that the loan repayment provisions will be applied on a program basis, the Department's data analysis has been conducted at the institutional level. In the NPRM, the Department acknowledges that it does not have data on repayment rates by program. See NPRM at pg. 43668 ("While repayment rates by program are not available, the Department has developed queries of the National Student Loan Data System to determine repayment rates by institution.") The Department lacks sufficient data upon which to base the minimum standards for loan repayment at the program level and as such, institutions would be unable to determine whether individual programs fall below the loan repayment threshold. Courts have held that such lack of notice runs afoul of due process protections. See *Gen. Elec. Co.*, 53 F.3d at 1328-29, ("[i]n the absence of notice – for example where a regulation is not sufficiently clear to warn a party about what is expected of it – an agency may not deprive a party of property by imposing civil or criminal liability"); *Satellite Broad Co. v. FCC*, 824 F.2d 1, 3 (D.C. Cir. 1987) ("[t]raditional concepts of due process incorporated into administrative law preclude an agency from penalizing a private party for violating a rule without first providing adequate notice of the substance of the rule"); *JIGC Nursing Home Co. Inc.*, 667 F. Supp. 949 (finding that the failure of the Department of Health and Human Services to specify an applicable standard to which a facility was held necessitated remand where information regarding peer group members was solely in the agency's possession and the plaintiff was unable to make any reasonable comparison with peer group costs).

Moreover, the NPRM as published contains many errors which make it difficult for an institution to determine the requirements and potential impact of the proposed rule. For example, (i) the charts on page 43621 state that a program with a debt-to-income ratio of eight percent or less and repayment rate below 35 percent will not be restricted and yet other sections of the NPRM at pages 43618 and 43638 state the opposite; (ii) the Department understates the number of students enrolled at proprietary institutions during the preceding four federal fiscal years as 376,000 at page 43634 thus drastically underestimating the proposed impact of the rule; (iii) the Department states at page 43635 that an institution must make debt warning disclosures "unless the program has a loan repayment rate of at least 45% ***or*** an annual loan payment that is at least 20% of discretionary income or 8% of average annual income", yet on page 44618 the proposed rule states that unless a program has a repayment rate of 45 percent **and** an annual loan payment that is not more than eight percent of average annual income or 20 percent of discretionary income, then the warning disclosure must be provided; and (iv) the Department states in several places on page 43635 and on page 43639 in the NPRM that annual loan payments must be "***at least*** 20% of discretionary income" or "***at least*** 8% of average annual income;" it is unclear what this latter statement means.

Such confusing and contradictory statements, and such lack of clarity in the underlying calculations, "[do] not inspire confidence in the clarity of the regulatory scheme." *GE Elec. Co.,* 53 F.3d at 368 (noting heightened concern about lack of clarity in regulations which the agency itself had difficulty determining were applicable to prohibited conduct).

ii. <u>The Missouri Study Cannot Be Used To Determine The Presumed Effects Of The Proposed Rule</u>

To assess debt and income levels by program, the Department worked with the Missouri Department of Higher Education to combine income information which the State has for programs at public and for-profit institutions with the Federal student loan information available from NSLDS. See NPRM at pg. 43668. The Department states that it did this because "Missouri is an appropriate and generally applicable lens to assess the potential effects nationally." Id. However, this is not the case and the Department must delay the publication of its final rule until the Department has better data from which to extrapolate the presumed effects of the rule.

In many important categories, the Missouri data is extremely different from the data from other states, which the Department terms "state average": (i) only 5.1 percent of the Missouri population speaks a language other than English at home whereas 17.9 percent of the national state average population speaks a language other than English at home; (ii) a mere 27.5 percent of students who attend postsecondary education in Missouri are non-White, compared to 41 percent of the national state average; (iii) 141,747 students in Missouri compared to 69,289 students in the national state average attend a private, nonprofit, four-year and above institution; (iv) 89,693 students in Missouri compared to 127,491 students in the national state average attend public two-year institutions. See *Gainful Employment Analysis Missouri Methodological Notes*, Prepared by the Office of Postsecondary Education ("OPE") with the assistance of the Missouri State Department of Higher Education ("MDHE"), available at http://www2.ed.gov/policy/highered/reg/hearulemaking/2009/ge-analysis-missouri.pdf. These large discrepancies do not allow the Department to determine the effects of the proposed rule across the nation.

Additionally, the Missouri study's institutional representativeness falls far short. Nationally, 28 percent of institutions are not-for-profit and 31 percent of Missouri institutions are not-for-profit. However, the institutions represented in the Missouri graduate (exiter) data file include only for-profit and public institutions. Id. As not-for-profit institutions do not participate in the MDHE data system, there is no data on students attending these institutions. Therefore, the Department's presumed effects of the rule fail to take into account 28 percent of its institutions. Moreover, cosmetology schools, which comprise approximately 38 percent of Missouri's for-profit institutions, are not represented in the Missouri data file. Id.

In its Gainful Employment Analysis Missouri Methodological Notes, the OPE admits that "Missouri data do not completely reflect either postsecondary institutions in that state, or more generally, institutions nation-wide." Id. It is therefore inexplicable how the Department can state that Missouri data can be used to extrapolate the presumed effects of the gainful employment rule. We urge the Department to delay the publication of its final rule until the Department has more accurate data from which to extrapolate the presumed nation-wide effects of the rule.

iii. <u>The NPRM Does Not Adequately Consider The Cost Of The Proposed Rule</u>

The NPRM makes several errors and omissions when considering the financial impact of the proposed gainful employment rule.

The Department notes in the NPRM that "[w]ith respect to the 2,086 proprietary institutions, the Department estimates that 376,000 student[s] … attended programs at those institutions during the preceding four FFY." See NPRM at pg. 43634. However, according to NCES data, enrollment at for-profit institutions in 2008 alone equaled over 3.2 million. See NCES, Table 10, *Postsecondary Institutions and Price of Attendance in the United States: Fall 2009, Degrees and Other Awards Conferred: 2008-09, and 12-Month Enrollment: 2008-09,* at page 18 *available at* http://nces.ed.gov/pubs2010/2010161.pdf. If this number is accurate, all of the Department's calculations respecting the burden of the proposed rule must be adjusted. We urge the Department to delay publishing a final rule while it reexamines these figures in order to provide further information regarding how these numbers were generated.

A further inconsistency arises regarding ineligible programs. The Department states that there are 2,649 programs that will be deemed ineligible due to the regulation. See NPRM at pg. 43632. However, when further discussing ineligible programs, the Department writes "[t]he Department estimates that there would be 3,000 programs in the ineligible category." Id. at pg. 43636. This discrepancy also needs to be addressed.

In addition, the Department's "Effect of Proposed Rule on Impacted Programs, Applying All Tests" section notes that the proposed regulations will apply to a total of 52,980 programs and 3,190,476 students. See NPRM at pg. 43632. This conclusion assumes that there is an average of 60 students enrolled per program (total number of students divided by total number of programs). However, the Department's other calculations which concern the number of students who will be fully eligible, ineligible, and restricted in Scenarios 1, 2, and 3, do not assume an

enrollment of 60 students per program. The chart attached hereto as Annex I shows the Department's calculations and the calculations that should have resulted using the Department's estimated 60 students per program figure.

As shown in Annex I, the Department's chart grossly overestimates the number of fully eligible students and grossly underestimates the number of students enrolled in restricted programs as a result of the proposed regulation. Since the number of restricted students who will be affected by this regulation is miscalculated, the Department's assessment of the increased burden to schools is grossly underestimated. We suggest that the Department review its calculations of students enrolled in restricted programs and burden hours to ensure that the hardship that this regulation will impose on schools and the Department is accurately represented.

The Department also omits any meaningful discussion regarding the costs of the rule when it considers that students who cannot enroll in for-profit institutions will be required to transfer to public institutions. As the Department briefly mentions when discussing the impact of the rule, public schools receive substantial public subsidies and their tuition and fee charges do not cover the cost of the education provided. See NPRM at pg. 43678. This fact needs to be considered in the entirety of the final rule, as published. For example, when comparing (i) the average tuition at for-profit institutions and the average indebtedness of students enrolled in for-profit schools with (ii) the average tuition at public institutions and the average indebtedness of students enrolled in public schools, and the resulting cost to taxpayers, the Department should address the fact that public schools receive significant subsidies that artificially reduce tuition and indebtedness rates but otherwise burden taxpayers to a greater extent than repayment rates or default rates would. The Department also should include the substantial subsidies provided to non-profit institutions when determining the comparative taxpayer burden of non-profit and for-profit institutions.[5] Finally, the Department should consider the taxes paid by for-profit institutions to help fund government programs when comparing the burden of the various sectors on taxpayers. Without these adjustments, the NPRM unfairly depicts the impact that for-profit, public, and private institutions have on taxpayers.[6]

Not only do for-profit institutions contribute to our nation's tax revenues, but they also aid in the nation's general economic recovery. For-profit institutions have both a positive direct and indirect effect on our economy. By providing an education to those who would not otherwise have access to higher education, for-profit institutions increase their graduates' earning capabilities and therefore, their spending activities. Moreover, in many communities for-profit institutions are the predominant providers of skilled workers in various fields. In fact, in some communities, they are the only sources of skilled workers. Therefore, on both a large and small scale for-profit institutions significantly contribute to both economic stimulus and recovery.

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[5] Note that public and private non-profit institutions also receive millions of dollars in non-title IV federal grants that for-profit institutions do not receive.

[6] See attached study, at Annex II, Charles River Associates, *An Analysis of Taxpayer Funding Provided for Post-Secondary Education: For-profit and Not-for-profit Institutions*, September 8, 2010.

Although the Department recognizes that as students are forced to transfer from for-profit institutions to public institutions more expenses than revenues will transfer to the public institutions, the Department does not adequately consider the differences in cost between providing additional funding to public institutions in order to expand their capacity against the cost of retaining the status quo – particularly where students will be transferred to institutions that have a history of graduating significantly fewer of their students. New funding that does not currently exist will have to be allocated to community colleges such that it is not clear that there would be any savings at all to taxpayers. Moreover, it is likely that as the costs increase to taxpayers the opportunities will decrease for students. Over the past fifty years, enrollment at community colleges has risen by close to 50 percent and recently, many community colleges have had to close admissions earlier than ever before. See Lisa W. Foderaro, *Two-Year Colleges, Swamped, No Longer Welcome All*, The New York Times, November 11, 2009. This demand coupled with states cutting their budgets will not allow community colleges to meet the need of a massive influx of students from other schools. Instead, the affected students will lose the opportunity for an education. The Department's analysis does not sufficiently consider these issues.

It is unclear why the Department would hinder access to for-profit institutions and prefer the education provided at community colleges when for-profit institutions often have much higher graduation rates. The costs associated with educating students who do not graduate from their programs have not been appropriately considered in the proposed rule.

iv. <u>The Proposed Rules Fail To Take Into Account The Societal Savings That Higher Education Provides</u>

Not only is an education an opportunity for growth and success but there also is data that reflects that it decreases the likelihood of incarceration and reliance on government assistance, such as welfare. Among non-institutional men aged 20-39, there is a notable correlation between education level and incarceration rates. Among white men from 1995-2001, 3.37 percent of incarcerated individuals had less than a high school diploma, while only .06 percent of individuals who had completed "some college" entered prison. These figures are even more startling for African Americans such that between 1995-2001, 16.3 percent of individuals with less than a high school degree entered prison, but only .54 percent of individuals with "some college" were incarcerated. See Bruce Western, et. al., *Did Falling Wages and Employment Increase U.S. Imprisonment*, Department of Sociology, Princeton University, January 2005, pg. 5. The Joint Economic Committee of the United States Congress noted in *Investment in Education: Private and Public Returns* that "data suggest that there is also a reduced reliance on welfare and public assistance programs among those with higher levels of education. In 1996, for example, 25-34 year-olds who ended their education after high school were ten times as likely as college graduates to have received income from Aid to Families with Dependent Children or public assistance income." See pg. 11 quoting the NCES, *The Condition of Education, 1998*, pg. 108. An estimate of welfare costs prepared by Henry Levin, et al. and published in *The Costs and Benefits of an Excellent Education for All of America's Children* illustrates that based on sources from 2006 and earlier, of the 1,216,800 recipients of Temporary Assistance for Needy Families, over 1.1 million had only a high school degree or less. The same is true for housing assistance of which 1,586,800 of the 1,640,900 had a high school degree or less and there were no recipients of food stamps with some college education or above. See

Table 10 at page 15. Clearly, the cost to taxpayers of educating students, even when default rates and repayment rates are included, is significantly less than incarcerating or providing public assistance to the same individuals. The Department's proposed rule and the associated rationale ignore the long-term benefits of obtaining postsecondary education for a large number of low-income individuals.

A study prepared by The College Board in 2007 reflects that in 2005, the median earnings of a high school graduate was less than $25,000. This number jumped to almost $30,000 for those with some college, $31,500 for individuals with an associate's degree and almost $40,000 for those with a bachelor's degree. These numbers reflect that "adults with associate degrees earned 29 percent more than high school graduates." See Baum and Ma, pg. 9. Similarly, a BLS survey reflecting 2009 annual averages for persons age 25 and over illustrates that as an individual's level of education increases, unemployment decreases and earnings increase. See Bureau of Labor Statistics, *Current Population Survey* available at http://www.bls.gov/emp/ep_chart_001.htm. With this increase in earnings, there was also an increase in the amount of taxes paid by these individuals. "The typical college graduate working full-time year-round paid 134 percent more in federal income taxes and almost 80 percent more in total federal, state, and local taxes than the typical high school graduate." Baum and Ma at pg. 9.

v. It Is Not Clear That The Proposed Rule Would Be Effective

As discussed in *How Much Debt is Too Much? Defining Benchmarks for Manageable Student Debt*, cited previously, "[a]cknowledging that debt obligations should not exceed certain percentages of income is insufficient protection for students. Sound advice for students is important but does not, on its own, provide viable alternatives for financial education. . . Well-designed loan forgiveness programs, income-contingent repayment plans consistent with manageable repayment levels, and provisions for discharging education loans in bankruptcy are all necessary components of an education financing system that protects students from excessive debt burdens." See pg. 12. The Department's current proposal to create an arbitrary threshold of debt-to-income in order to determine programmatic eligibility fails to protect the student from excessive debt – one of the supposed goals of the gainful employment regulation – and will limit student choice in academic programs.

Banks and other financial institutions rely on FICO scores, not income levels, to determine whether or not a particular individual will receive financing and how much it will cost that individual to borrow money. A FICO score is comprised of the following factors: payment history (35 percent); total amount owed (30 percent); length of credit history (15 percent); new credit (10 percent) and type of credit in use (10 percent). See http://www.myfico.com/crediteducation/whatsinyourscore.aspx. Nowhere in this calculation does an individual's income come into play. This belies the Department's suggestion that it is commercially reasonably to associate a program's debt-to-income ratio or repayment rate with the quality of its educational programs. More likely, a program's repayment rate as proposed by the Department is strongly related to the FICO scores of the enrolled students and, where applicable, their parents. Schools that understand this will begin redlining applicants according

to their FICO scores in order to meet Department-imposed repayment ratios. Once again, this will disproportionately reduce educational access to minorities and low-income individuals.

vi. The Proposed Rule Should Use Graduation Rates and Placement Rates As A More Accurate Measure Of Gainful Employment

We propose that the Department use graduation and placement rates rather than repayment rates and debt-to-income ratios to measure programmatic quality, including gainful employment, and that these measures of student success apply to all sectors of higher education.

The ultimate goal of education is to gain a better future and obtain a better job than one could without a postsecondary education – even if that program is not targeted to a specific profession. If an institution has a low graduation rate this indicates that a large number of its students have invested time and money without the benefit of completing an educational program. Placement rates in particular are a direct measure of whether an institution's programs lead to gainful employment. The debt-to-income ratios and the repayment rates, on the other hand, are convoluted metrics not directly related to gainful employment. As noted previously, the repayment rate is more directly related to a school's demographics, the income level of its students prior to obtaining an education, and even the repayment options offered by the federal government than it is to the quality of a school's programs. The debt-to-income ratio likewise is affected by many extraneous factors including regional differences in employment rates, student demographics, the willingness to report income, part-time employment and even temporary absences from the workforce. Although a school cannot control its placement rates entirely since these rates also are impacted by local economies and student choices, placement rates are at least directly related to the ability (and sometimes willingness) of a program's graduates to obtain employment in the field in which they trained. Further, low placement rates are the first indicator a school has that a particular program may need to be revised or terminated. Where national accrediting agencies already require schools to measure placement rates and the Department has encouraged regional accrediting agencies to likewise enforce more rigorous performance standards, it is unclear why the Department has developed metrics that will require inordinate efforts to maintain, that are obscured from the regulated entities and that are not directly related to "gainful employment", which merely means employment for pay.

All institutions, regardless of type, should be required to demonstrate that their programs perform as advertised – that is, that their students graduate and achieve desired employment that could not be obtained without the advertised education.

vii. The Proposed Rule, If Adopted, Should Apply To All Institutions That Participate In The Title IV Programs

Most public, private, or non-profit institution's educational programs, with the exception of recreational courses, are intended to prepare students for the work force, even if not for a specific profession. As a result, it is not clear why the Department has drafted a regulation that

so clearly focuses on, and negatively impacts, for-profit institutions.[7] The Department offers no convincing explanation as to why it does not more completely extend this rule, for example, to community colleges, which have an average loan repayment rate of 40 percent (four percent higher than the for-profit institution average) and are heavily subsidized by the public in order to maintain low tuitions that do not cover the cost of education. The Department's proposed rule would restrict or eliminate eligibility for a program at a for-profit institution but would allow a similar program with a similar repayment rate and likely a lower graduation rate to maintain its eligibility if it is offered at a community college and leads to a degree, or is a two-year transfer program.[8] Not only does this logic fail, but as community colleges abandon their open enrollment policies, it will leave many students uneducated, unskilled and a much greater burden on the taxpayers. See Caralee Adams, *Community Colleges Rethink "Open Door" Admissions as Remedial Costs Rise*, Education Week, August 13, 2010; Lisa W. Foderaro, *Two-Year Colleges, Swamped, No Longer Welcome All*, The New York Times, November 11, 2009.

Given the claimed benefits of this rule, such as reducing student loan defaults and costs to taxpayers for non-payment as well as determining the benefit of certain educational programs, there is no logical reason why only for-profit schools should be covered by this rule when it

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[7] The Department's bias in presenting this regulation is demonstrated by the illogic of threatening termination of programs that graduate more students than the programs that will not be governed by this rule, the recognition that repayment rates should be improved by all institutions while penalizing substantially one sector for low repayment rates, the mischaracterization of the cost of defaults and slow repayments by for-profit institution students versus the significant taxpayer subsidies provided to public and non-profit institutions, selective quotations from various studies which quotations seem to intentionally ignore the benefits of for-profit institutions and focus only on the negative aspects of for-profit institutions, the method of calculation of the repayment rates which benefits in-school deferments affecting mostly traditional institutions, the failure to note where other sectors similarly do not perform thereby imposing substantial costs on taxpayers, and even the Department's wholesale adoption of the mantra of the Institute for College Access and Success that "unlike publically controlled or non-profit institutions – for-profit institutions are legally obligated to make their profitability for shareholders their overriding objective" which even a small amount of research would refute as a mischaracterization of most states' corporate laws.

[8] We strongly object to the suggestion of the American Association of Community Colleges that the final regulations should not apply to one-year certificate programs at public institutions that, with the addition of certain general education courses, could lead to a degree. There is no regulatory logic to support this request and there is no qualitative distinction that warrants such an exemption. Rather, in light of the fact that community colleges have on average what the Department would describe as poor repayment rates and unsatisfactory graduation rates, the proposed rule should apply to *all* community college programs. At the very least, under current regulation, the rule should apply to all certificate programs, and all degree programs of less than two academic years in length. The Department must craft a responsible rule that is applicable to all programs that lead to gainful employment, which includes all programs of postsecondary vocational schools and all non-degree programs at institutions of higher education with the possible exception of two-year transfer programs which may be transferred to liberal arts degree programs.

could easily be applied to traditional institutions. The Department has already calculated the repayment rates of such institutions and the information needed to calculate debt-to-income ratios can and should be required from traditional institutions. See U.S. Department of Education, Estimated Repayment Rates by Institution - FY 2009, August 13, 2010.

## III. Closing

Higher education is vital to producing and supporting successful and well-rounded citizens and communities. President Obama has set a goal of leading the world in the percentage of college graduates by 2020. See NPRM at pg. 43617. See *Gainful Employment Analysis Missouri Methodological Notes*. To meet President Obama's goal of having the world's highest percentage of college graduates, more students, not less, must be provided the opportunity to seek higher education. We will fail to meet this objective if we deny education to minorities, women and students from low-income backgrounds as the proposed rule threatens to do.

Further, if the Department fails to require adherence to this rule (as appropriately amended based on the comments contained above) by all postsecondary institutions then it will become eminently clear that the true purpose of this rule is to penalize for-profit institutions and their students, not to protect the Title IV programs.

Thank you for the opportunity to comment on the proposed rule.

## Annex I

| | | Department's Calculations | Calculations using 60 students per program | Difference |
|---|---|---|---|---|
| **Scenario 1** | **Fully Eligible Students** | 2,618,476<br>(127 students per program) | 1,239,720 | **- 1,378,756** |
| | **Ineligible Students** | 307,000<br>(116 students per program) | 158,940 | - 148,060 |
| | **Restricted Students** | 265,000<br>(9 students per program) | 1,780,140 | **+ 1,515,140** |
| | **Total** | 3,190,476<br>**(60 students per program)** | 3,178,800 | - 11,676 |
| **Scenario 2** | **Fully Eligible Students** | 2,618,476<br>(127 students per program) | 1,239,720 | **- 1,378,756** |
| | **Ineligible Students** | 307,000<br>(116 students per program) | 158,940 | - 148,060 |
| | **Restricted Students** | 265,000<br>(9 students per program) | 1,780,140 | **+ 1,515,140** |
| | **Total** | 3,190,476<br>**(60 students per program)** | 3,178,800 | - 11,676 |

| | | | | |
|---|---|---|---|---|
| **Scenario 3** | **Fully Eligible Students** | 2,617,476<br><br>(127 students per program) | 1,239,720 | **- 1,377,756** |
| | **Ineligible Students** | 307,000<br><br>(116 students per program) | 158,940 | - 148,060 |
| | **Restricted Students** | 266,000<br><br>(9 students per program) | 1,780,140 | + **1,514,140** |
| | **Total** | 3,190,476<br><br>**(60 students per program)** | 3,178,800 | - 11,676 |

# Annex II

CRA Charles River Associates

**Prepared For:**

The Coalition for Educational Success: Preparing the New American Workforce

# An Analysis of Taxpayer Funding Provided for Post-Secondary Education: For-profit and Not-for-profit Institutions

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# Disclaimer

*This report was prepared at the request of The Coalition for Educational Success: Preparing the New American Workforce. It is based on data and information that were available at the time of the analyses. If additional data or information becomes available we may update or modify our report.*

The primary focus of this paper is to determine and compare the total costs borne by taxpayers for public and for-profit postsecondary colleges that are eligible to receive funding under Title IV of the Higher Education Act and other sources of government funding. For purposes of this paper, government funding includes *all* financial funding provided by the federal, state and local governments.

**Executive Summary**

In evaluating its proposed "Gainful Employment" rule as well as future government investments in higher education, the U.S. Department of Education ("DOE") should take into account the significant taxpayer savings provided by career and for-profit colleges. In the most conservative analysis, where only direct costs to taxpayers are considered, for-profit 2-year institutions produce graduates at a cost to taxpayers that is $25,546 lower on a per student basis than the public 2-year institutions. This amount takes into account the costs to taxpayers for providing federal direct loans to the students at the for-profit and public 2-year institutions. When indirect costs such as taxes paid by for-profit schools and lost revenues from tax-exempt public institutions are taken into account, the differential between for-profit and non-profit institutions is even greater.

Default rates on student loans have a small impact on the taxpayer cost differential between the two types of institutions. According to default data provided by the DOE, the cumulative lifetime default rates for the for-profit 2-year institutions and public 2-year institutions are 26.0% and 21.4%, respectively, for the federal loans that were originated in 2003 that entered repayment through September 30, 2009. Again, in the analysis presented above (which includes a conservative assumption that the recovery rate is 0% on defaulted loans), the total taxpayer cost for providing federal direct loans per graduated student for two-year programs is $709 for public 2-year institutions and $4,115 for the for-profit 2-year institutions. If one were to assume a recovery rate of 60%, the total costs to taxpayers for providing federal direct loans per graduated student would decrease to $284 for public 2-year institutions and $1,646 for the for-profit 2-year institutions.

In summary, the total taxpayer cost per graduated student is significantly higher at public 2-year institutions than at for-profit 2-year institutions. The table below highlights that the total

taxpayer cost per graduated student is more than $25,000 higher at public institutions than at for-profit institutions:

| | Public 2-Year Institutions [A] | For-profit 2-Year Institutions [B] | Difference [B] *minus* [A] |
|---|---|---|---|
| (Per Graduated Student) | | | |
| **Direct Government Funding Provided by Taxpayers** | $32,163 | $3,211 | ($28,953) |
| **Total Taxpayer Cost For Providing Federal Direct Loans** | $709 | $4,115 | $3,406 |
| **Total Taxpayer Cost Per Graduated Student** | $32,873 | $7,326 | ($25,546) |

For-profit 2-year institutions also deliver clear value to taxpayers in student outcomes. More than 75 percent of 2-year for-profit college graduates were placed into jobs within six months. We are unable to compute the placement rate for public 2-year institutions because the data is not available.

Student demand for higher education continues to grow as employers require higher skills while depending more heavily on schools for "on-the job" training. But the capacity of traditional not-for-profit schools has not kept pace, with the number of public 2-year institutions shrinking by 4.0 percent between 1996-97 and 2006-07. During this time, the number of the for-profit 2-year institutions increased by 13.4 percent, reflecting their focus on innovation and convenience to meet the needs of non-traditional students.

Importantly, both not-for-profit and for-profit college growth is crucial to meet future student demand. Continued government support to finance higher education is critical to assure student access to higher education. For example, in 2007-08, about half of all full-time undergraduate students relied on government loans to finance their higher education.[1] In stewarding these scarce public funds and in setting policy, government should clearly understand the dramatic costs savings and value provided by career colleges.

[1] Based on full-time, full-year undergraduates at all institutions. Source: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009*, Table 343

## Postsecondary Educational Institutions

Postsecondary educational institutions are schools, colleges and universities that are designed to meet the continuing education needs and interests of adults. These institutions provide academic, career and technical, and continuing professional education programs after high school. Degree-granting institutions include almost all 2- and 4-year colleges and universities that grant an associate or higher degrees (e.g., Bachelor and Masters degrees) and whose students are eligible to participate in the Title IV federal financial aid programs. Title IV programs, which are administered by the DOE, provide financial aid to postsecondary students. For purposes of this paper, degree-granting institutions exclude institutions offering only career and technical programs, which are shorter than 2 years.

There are three groups of postsecondary degree-granting institutions: (1) public institutions, (2) private not-for-profit institutions, and (3) private for-profit institutions. Public institutions are controlled and operated by publicly elected or appointed officials and derive their support primarily from public funds. In 2007, there were 1,685 public institutions in the United States with approximately 13.5 million full-time and part-time students, as shown in Exhibit 1. For example, the University of California, Los Angeles is a 4-year public institution and Pasadena Community College is a 2-year public community college. A 2-year public institution offers only associate degrees whereas a 4-year public institution grants mostly bachelor and higher degrees.

**Exhibit 1: Postsecondary Degree-granting Institutions in the United States**

| | Public Institutions | | | Private Not-for-profit Institutions | | | Private For-profit Institutions | | | All Institutions |
|---|---|---|---|---|---|---|---|---|---|---|
| | 4-year | 2-year | Total | 4-year | 2-year | Total | 4-year | 2-year | Total | |
| **Number of Degree-granting Insitutions, 2007-08** | 653 | 1,032 | 1,685 | 1,532 | 92 | 1,624 | 490 | 553 | 1,043 | 4,352 |
| (as % of all institutions) | | | 39% | | | 37% | | | 24% | 100% |
| **Enrollment, fall 2007** | 7,166,661 | 6,324,119 | 13,490,780 | 3,537,664 | 33,486 | 3,571,150 | 925,873 | 260,325 | 1,186,198 | 18,248,128 |
| (as % of all institutions) | | | 74% | | | 20% | | | 7% | 100% |
| **Associate's degrees, 2007-08** | 71,514 | 507,006 | 578,520 | 38,251 | 6,537 | 44,788 | 68,450 | 58,406 | 126,856 | 750,164 |
| (as % of all institutions) | | | 77% | | | 6% | | | 17% | 100% |
| **Bachelor's, Master's, First-professional and Doctor's degrees, 2007-08** | 1,371,951 | N/A | 1,371,951 | 837,193 | N/A | 837,193 | 133,969 | N/A | 133,969 | 2,343,113 |
| (as % of all institutions) | | | 59% | | | 36% | | | 6% | 100% |

Sources: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009*, Tables 5 and 187

A private not-for-profit institution is an educational institution in which the individual(s) or agency in control receives no compensation other than wages, rent, or other expenses for the assumption of risk in operating the institutions. It generates revenues primarily from sources other than public funds and is controlled by an individual or agency other than a state or the federal government. Private not-for-profit institutions may have been established by religious organizations or independent private entities. There were approximately 3.6 million students enrolled in 1,624 private not-for-profit institutions in the United States in 2007. (See Exhibit 1) Nearly 95% of these institutions are 4-year colleges and universities, such as Stanford University and Claremont McKenna College, which offer programs leading to bachelor and higher degrees.

Private for-profit institutions, also known as proprietary institutions, are education business organizations that prepare graduates for jobs and career advancement. These institutions receive little public funding and generally offer a focused range of programs in high-demand occupational or professional fields. Close to 1.2 million students were enrolled in private for-profit institutions in the United States in 2007. (See Exhibit 1) ITT Technical Institute, University of Phoenix and Strayer are some of the private for-profit institutions. Unlike the public and private not-for-profit institutions, about half of the degrees granted by private for-profit institutions are associate degrees.

Private for-profit institutions typically attract many non-traditional students. The "traditional" postsecondary students are characterized as those who have earned high school diploma, enroll full-time immediately after finishing high school, depend primarily on parents for financial support, and either do not work during the school year or work part-time. Traditional postsecondary students are generally able to spend most of their time on their studies and extracurricular activities at school. In contrast, non-traditional students have family and work responsibilities competing with school for their time, energy and financial resources. While there is no precise definition of "non-traditional" students, they are commonly defined in research a student who has one or more of the following characteristics: delays enrollment (does not enter postsecondary education in the same calendar year that he or she finished high school); attends part time for at least part of the academic year; works full time (35 hours or more per week); is considered financially independent; has dependents other than a spouse (usually children, but sometimes others); is a single parent (either not married or married but separated and has dependents); or does not have a high school diploma.[2]

According to a 2002 study conducted by National Center for Education Statistics ("NCES") at the DOE, only 11.3% of total students at private for-profit institutions in the United States were characterized as traditional students in 1999-2000, as shown in Exhibit 2. This is similar to the percentage of traditional students at public 2-year institutions. In contrast, the percentage of traditional students at public 4-year and private not-for-profit 4-year institutions ranged from 42.5% to 50.0%. (See Exhibit 2) Private for-profit and public 2-year institutions had high percentages of students who were financially independent, delayed enrollment, had dependents or worked full time, as shown in Exhibit 3.

[2] U.S. Department of Education, National Center For Education Statistics (NCES), *Nontraditional Undergraduate*, NCES-2002-012, August 2002, pp. 2-3.

**Exhibit 2: Traditional versus Nontraditional Students at Public and Private For-profit Institutions**

| Type of Institution | Traditional | Minimally Nontraditional | Moderately Nontraditional | Highly Nontraditional |
|---|---|---|---|---|
| **Public 2-year** | **11%** | 14% | 35% | 40% |
| **Public 4-year** | **43%** | 20% | 23% | 14% |
| **Private Not-for-profit 4-year** | **50%** | 15% | 16% | 19% |
| **Private For-profit** | **11%** | 15% | 39% | 35% |

Source: U.S. Department of Education, National Center For Education Statistics, *Nontraditional Undergraduates*, August 2002, Table 1.

**Exhibit 3: Percentage of Total Students With Non-Traditional Characteristics**

| Type of Institution | Financially Independent | Attended Part Time | Delayed Enrollment | Worked Full Time | Had Dependents | Single Parent | No High School Diploma |
|---|---|---|---|---|---|---|---|
| **Public 2-year** | 64% | 70% | 59% | 54% | 35% | 16% | 10% |
| **Public 4-year** | 38% | 33% | 32% | 26% | 18% | 9% | 2% |
| **Private Not-for-profit 4-year** | 37% | 28% | 34% | 29% | 19% | 9% | 3% |
| **Private For-profit** | 73% | 22% | 68% | 41% | 44% | 27% | 16% |

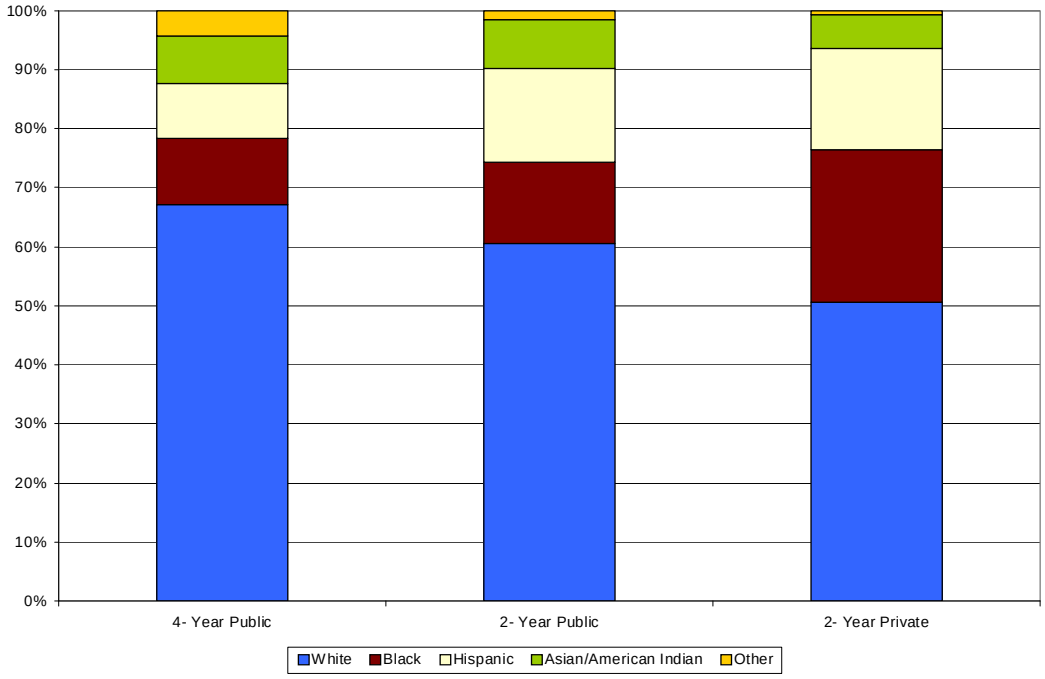
Source: U.S. Department of Education, National Center For Education Statistics, *Nontraditional Undergraduates,* August 2002, Table 2.

Private for-profit institutions in the United States also serve a disproportionate number of minority students, as many of these students are the first in their families to attend college. In 2007, about 48.8% of the students at the private for-profit 2-year institutions were Black, Hispanic, Asian and other minority races, as shown in Exhibit 4. The public 4-year and 2-year institutions had only 28.5% and 38.0%, respectively, in minority students as of 2007.

Many students at the career and community colleges received financial aid, such as Pell Grants and federal loans, from the federal government. The default experience of federal student loans is related to the mix and socio-economic demographics of these students, and may not depend

upon whether they are enrolled in a for-profit or public institution. Given that public 4-year institutions and private not-for-profit institutions have different student mixes and demographics than for-profit institutions, these institutions serve as poor benchmarks to the private for-profit institutions. The data presented here demonstrate that the appropriate comparables for the for-profit institutions are public 2-year institutions.

Exhibit 4: Total Student Enrollment In Fall by Race/Ethnicity
(U.S. Degree-granting Institutions, 2006-07)




Source: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009*, Table 227

**Who financed the costs of education in public and private for-profit postsecondary institutions?**

Based on detailed data published by NCES in the Digest of Education Statistics, we compiled the total costs of providing education to postsecondary students. The total costs include the education costs that are borne by students and by the local, state and federal governments, as shown in Exhibit 5. We also analyze the costs borne by other private parties.

For the academic year in 2006-07, annual prices for college tuition and required fees at public 2-year institutions amounted to $2,133 per full-time equivalent student. In 2006-07, the tuition

and required fees paid by students at for-profit 2-year institutions were $13,442 per full-time equivalent student.

**Exhibit 5: Costs of Providing Postsecondary Education, Per Full-time Equivalent Student**
(U.S. Degree-granting Institutions, 2006-07 in Constant 2007-08 Dollars)

| | | Public 2-Year Institutions | For-profit 2-Year Institutions |
|---|---|---|---|
| **Tuition and Required Fees Per Year** | [1] | $2,133 | $13,442 |
| (% of Total Costs Per Year) | [2]=[1]/[5] | 18.2% | 90.8% |
| **Government Grants and Contracts Per Year** | [3] | $9,599 | $1,361 |
| (% of Total Costs Per Year) | [4]=[3]/[5] | 81.8% | 9.2% |
| **Total Costs per Year** | [5]=[1]+[3] | $11,732 | $14,803 |
| Length of Program (in years) | [6] | 2.0 | 2.0 |
| **Total Costs For Completing the Program** | | **$23,464** | **$29,606** |

Sources: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009*, Tables 352 and 357

The tuition and required fees are only part of the total cost of providing education. The federal, state and local governments also provide substantial direct funding to post-secondary institutions. The costs borne by taxpayers include grants and contracts for operating revenues, appropriations and non-operating grants for non-operating revenues, and capital appropriations. In 2006-07, public 2-year institutions received on average $9,599 per full-time-equivalent student from government grants, contracts and appropriations, excluding federal direct student loans. That government funding accounted for 82% of the total costs for completing an associate degree in public 2-year institutions in 2006-07. Because public institutions receive substantial direct funding from the government entities, they charge lower tuitions and related fees than private institutions. The for-profit 2-year institutions received only $1,361 per full-time-equivalent student from direct government funding in 2006-07. This covers only 9% of the total program costs. It is not surprising, therefore, that the students at the for-profit 2-year institutions pay higher tuition and fees because they bear most of the costs of education.

In total, the annual costs of providing postsecondary education to public 2-year institutions were $11,732 per full-time equivalent student in 2006-07, as shown in Exhibit 5. With a program

length of 2 years, the total cost for completing an associate degree in public 2-year institutions is $23,464. The taxpayers bear most of the education costs at the public institutions. The total education costs for a student to complete an associate degree at the for-profit 2-year institutions were $29,606, as also shown in Exhibit 5. Unlike the public institutions, the students at the for-profit 2-year institutions fund over 90% of the total costs.

There are other education costs that are borne by the taxpayers and private third parties that are not included in our analysis. Some of these costs include tax benefits provided by the federal and state governments associated with private gift donations, property tax foregone by the local and state governments, and the state and federal income taxes paid by for-profit institutions which offset the costs borne by the taxpayers. A more detailed discussion of these costs is included in Appendix A.

**Total Taxpayer Cost per Graduated Student from Public 2-year and For-Profit 2-year Institutions**

In this section, we present the total direct cost, not including any of those indirect costs discussed in Appendix A, borne by taxpayers per graduated student at public 2-year and for-profit 2-year institutions. This is a very conservative way to compare the institutions. The analysis is based on data provided by the DOE. As discussed earlier in this paper, the total government funding provided to public 2-year and for-profit 2-year institutions were $9,599 and $1,361 per full-time equivalent student, respectively, in 2006-07. The taxpayers thus bear an additional cost of $8,238 ($9,599 minus $1,361) per full-time equivalent student at public 2-year institutions compared to the for-profit 2-year institutions.

Not all the students who received funding from the government graduated from the 2-year public institution they attended. Some students transferred to a 4-year institution before completing an associate degree while others dropped out of the public 2-year colleges. According to data provided by the DOE, 28.9% of students at public 2-year institutions transferred to a 4-year institution, with about one-third of those students completing an associate degree before the transfer. This means that 19.3% (2/3 of 28.9%) of the total students at community colleges transferred to a 4-year institution without graduating from the community

colleges. These students stayed at the community colleges for one to two years before their transfer.

The DOE data also shows that 20.3% of students (including one-third of the transferred students) at the community colleges graduated with an associate degree.[3] These students stayed at the community colleges for at least two years in order to complete the associate degree. The rest of the community college students either dropped out, exceeded the length deemed appropriate for graduation by the DOE, or transferred to a 4-year institution. Assuming these students only stayed at the community colleges for six months, we determine that a full-time equivalent student on average stays at the community colleges for approximately 1.0 year.

Not all community college students who transferred to a 4-year university without completing an associate degree graduate with a Bachelor degree. Data from the DOE shows that a 4-year public university has a graduation rate of 49.1% (for the 2001 starting cohort).[4] We believe this graduation rate is high for community college transfer students due to the fact that these students have a higher likelihood of being "non-traditional" students. Despite this fact, we use the 4-year public graduation rate of 49.1% in our analysis which we believe is a conservative assumption. Thus, 9.5% of total students at community colleges that transferred to a 4-year institution before completing an associate degree eventually graduated from the 4-year institution. Including these students in our calculation, the graduation rate of community colleges was 29.8% (20.3% graduated with an associate degree and 9.5% eventually graduated with a Bachelor degree from the 4-year institution). With a graduation rate of 29.8%, the total cost borne by taxpayers per graduated student is $32,163 ($9,572 total taxpayer cost per student divided by the graduation rate of 29.8%) for completing his associate degree at the community colleges. The calculations are shown in Exhibit 6.

It has been documented that public 2-year institutions have lower graduation rates than for-profit 2-year institutions. According to data provided by the DOE (for cohort year 2004),

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[3] Graduation percentage is based on the percent of students completing an associate degree within 150 percent of normal time (for 2004 starting cohort). Source: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009*, Table 331

[4] Based on percent completing Bachelor degrees within 5 years after start. Source: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009*, Table 331

the graduation rate of the for-profit 2-year institutions was 58.2%.[5] This is significantly higher than both, the graduation rate we calculated of 29.8% at the community colleges, and the DOE reported graduation rate of 20.3% at the community colleges. Note that the graduation rate for the for-profit 2-year institutions does not include any transferred students who did not complete an associate degree but eventually graduated with a Bachelor degree because such data is not readily available.

We follow the same procedure to calculate the total cost to taxpayers per graduated student for the for-profit 2-year institutions. By our calculations, the total cost to taxpayers for a graduated student at the for-profit 2-year institutions is only $3,211. The calculations are shown in Exhibit 6.

The direct government funding provided to post-secondary institutions are actual out-of-pocket costs to the taxpayers. This is because neither the post-secondary institutions nor the students have any obligation to repay those direct government funding. The direct government funding is thus notably different from federal direct student loans. In the case of federal direct loans, the borrowers are obligated and expected to repay the loans in full to the government with interest. There is no cost (putting aside the administrative fees) for the taxpayers to provide direct student loans unless the borrowers default on those loans and eventually do not fully repay the loan balance. This is discussed in greater detail in the next section.

Ignoring the effect of defaults on direct student loans for the public and private for-profit institutions, the for-profit sector costs the taxpayers significantly less than the public institutions. The taxpayers paid **$28,953** less in total cost to support a full-time equivalent graduated student attending a for-profit 2-year institution than at a public 2-year institution (total cost to taxpayers per graduated student of $32,163 to public 2-year institutions minus $3,211 to for-profit 2-year institutions) in 2006-07.

[5] *Id.*

## Exhibit 6: Total Taxpayer Cost Per Graduated Student Completing the Program In Public and Private For-profit Institutions

(U.S. Degree-granting Institutions, 2006-07 in constant 2007-08 dollars)

| | | Public 2-Year Institutions | For-profit 2-Year Institutions | Difference |
|---|---|---|---|---|
| | | [A] | [B] | [B] *minus* [A] |
| **Government Grants and Contracts** | [1] | $9,599 | $1,361 | |
| Average Years In School (Including Transfers and Dropouts) | [2] | 0.997 | 1.373 | |
| **Total Taxpayer Cost Per Student Completing the Program** | [3]=[1]*[2] | $9,572 | $1,869 | |
| Graduation Rate of Students (Including Non-graduates) | [4] | 29.8% | 58.2% | |
| **Total Taxpayer Cost Per Graduated Student** | [5]=[3]/[4] | **$32,163** | **$3,211** | **($28,953)** |

Sources: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009* , Tables 352 and 357;
Charles River Associates calculations.

*Notes:*

[2] Assumes graduated students stayed for 2 years; transferred students stayed for 1-2 years; and the rest of students stayed for 6 months only

[4] Based on graduation data provided by the U.S. Department of Education. Graduation rate for public 2-year institutions includes those students who transferred to a 4-year institutior and eventually graduated with a Bachelor's degree. No transferred students are included at the for-profit 2-year institutions to compute the graduation rate.

**Total Taxpayer Cost for Funding Federal Direct Loans**

Taxpayers also bear potential costs for funding the direct loans provided by the federal government to post-secondary students. A more detailed analysis of the federal direct loan program and the subsidy rate computed by the federal government on the direct loans is included in Appendix B. Because the interest rates charged by the federal government on the direct loans are higher than its borrowing rates, the federal government generates substantial income by making direct loans to students.

A loan is considered to be in default if the borrower fails to make a payment for 270 days (330 days if payments are due less frequently than each month). If a borrower defaults on a federal student loan, the obligation to repay cannot be discharged by filing bankruptcy under the current law. The government, through its various means, can collect the delinquent loans during the entire lifetime of the borrower. The government can utilize private collection agencies to collect the loans. It can also garnish wages and use the Treasury Offset Program to collect a portion of federal transfer payments that the delinquent borrowers receive (e.g. tax refunds or Social Security benefits).

Even when there is a loan default, the taxpayers may incur little cost if the federal government eventually recovers the loan principal and interest. According to the data published by the Office of Management and Budget ("OMB") for the budget in fiscal year 2011, the recovery rate of all obligations under the FDLP programs is estimated to be 110.60 for a loan principal of 100. This means that the federal government is expected to fully recover the loan principal and receive an interest of $0.11 for each dollar of direct loan made. OMB did not break down the recovery rate between not-for-profit and for-profit institutions.

In October 2000, the U.S. Government Accountability Office ("GAO") conducted a detailed study on the default rates for FDLP loans based on the 1998 cohort default data. The GAO study shows that the student loan default rates of 2-year institutions (both for-profit and not-for-profit) were twice as high as the public 4-year institutions. It concludes that "[T]he higher default rates for borrowers attending [public] 2-year and proprietary schools are indicative of

the higher risk of default that has historically been associated with these borrowers."[6] Past research conducted by GAO shows that default rate differences were related to characteristics such as the student's academic preparation for higher education or the family's socioeconomic status.[7] The GAO study also found that the federal direct loan default rate at the public 2-year institutions (at 12.5%) was comparable to that experienced by the proprietary schools (at 10.2%).

The DOE recently published updated default rates for the not-for-profit and for-profit institutions. The default rates are measured based on the cohort default rates on certain Federal Family Education Loan (FFEL) and FDLP loans for cohort years 2003 to 2007. The cohort default rate is the percentage of borrowers who enter repayment on certain federal loans during a particular federal fiscal year, October 1 to September 30, and default (or meet other specified conditions) prior to the end of the next fiscal year. The DOE also measured the cumulative lifetime default rate for loans originated by cohort year 2003 to 2007. A cumulative lifetime default rate is the percentage of loans that enter repayment in the FFEL and FDLP for a particular federal fiscal year and have defaulted through the end of the most recent federal fiscal year. Unlike the cohort default rate, which reflects a two-year indicator period, the cumulative lifetime default rate reflects the risk of default throughout the life of the loan. The DOE measured the default occurring from the time the loan entered repayment through September 30, 2009.

According to the DOE data, the cohort default rates for the for-profit 2-year and public 2-year institutions are comparable. For instance, for federal loans originated in cohort year 2003, the default rate is 8.0% for the for-profit 2-year institutions, as compared with the default rate of 7.6% for public 2-year institutions. The cohort default rates as measured by the DOE are shown in Exhibit 7A. The DOE only provided the cumulative default rates for the for-profit institutions (4-year and 2-year institutions) on an aggregate basis. For the federal loans originated in cohort year 2003, the cumulative lifetime default rate for the for-profit institutions

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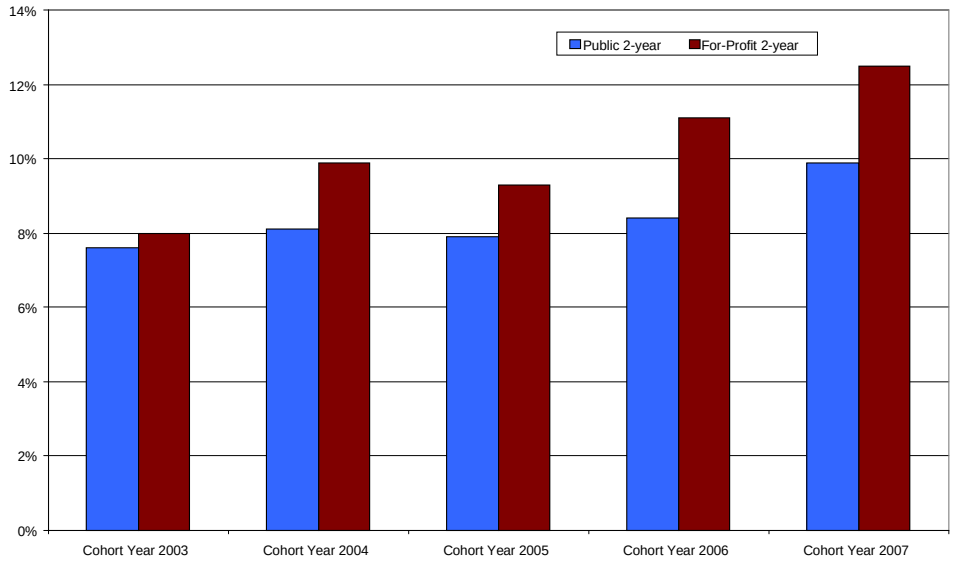
[6] GAO, Student Loans: Direct Loan Default Rates, 10/17/2000, p. 5

[7] *Id.*, p. 11. See also, GAO, Student Loans: Characteristics of Students and Default Rates at Historically Black Colleges and Universities, 4/9/1998.

is 26.0%. This is slightly higher than the cumulative lifetime default rate of 21.4% for public 2-year institutions. The cumulative default rates are shown in Exhibit 7B. Overall, the default rates between the for-profit and public 2-year institutions are comparable. This is consistent with the results of the GAO study discussed above.

Exhibit 7A: Cohort Default Rate of For-profit 2-Year and Public 2-Year Institutions*




*Based on proprietary 2-3 year and public 2-3 year institutions as published by the U.S. Department of Education

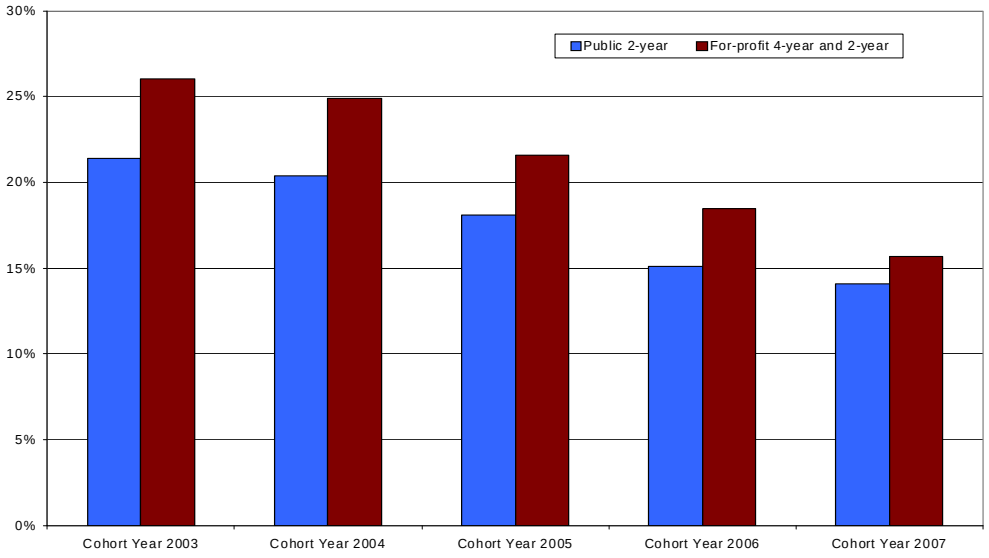
Source: The Department of Education, *Default Rates for Cohort Years 2003-2007*, December 14, 2009.

Note: A cohort default rate is the percentage of borrowers who enter repayment on certain Federal Family Education Loan (FFEL) Program or William D. Ford Federal Direct Loan (Direct Loan) Program loans during a particular federal fiscal year, October 1 to September 30, and default or meet other specified conditions prior to the end of the next fiscal year.

Based on data published by the DOE, we determine the average amount of direct loans provided by the federal government to students at the for-profit institutions (2-year and above) to be $6,709 per full-time equivalent student in 2007-08. If it is assumed that these loans experience a cumulative lifetime default rate of 26.0%, then the expected amount of defaulted loan will be $1,744 ($6,709 direct loans multiplied by the cumulative default rate of 26.0%) per full-time equivalent student per year. Assuming there is no recovery by the federal government on these defaulted loans, the expected defaulted loan amount of $1,744 represents a direct cost borne by the taxpayers to the student in one year. Based on an average stay of 1.37 years at school (as discussed in the last section), the total cost to taxpayers will be $2,395 ($1,744 total cost to taxpayers per year multiply by 1.37 years) per full-time equivalent student during his entire stay

at the for-profit institutions. Given a graduation rate of 58.2% for the for-profit 2-year institutions (as discussed in the last section), we calculate the total cost to taxpayers for federal direct loans to be $4,115 per graduated student ($2,395 per full-time equivalent student divided by the graduation rate of 58.2%). The calculations are shown in Exhibit 8.

Exhibit 7B: Cumulative Lifetime Default Rates of For-profit and Public 2-Year Institutions




Source: The Department of Education, *Default Rates for Cohort Years 2003-2007*, December 14, 2009.

Note: A cumulative lifetime default rate is a percentage of loans that enter repayment in the FFEL and Direct Loan Programs for a particular federal fiscal year and have defaulted through the end of the most recent federal fiscal year. Unlike the cohort default rate, which is utilized as an administrative tool for schools and currently reflects a two-year indicator period, the cumulative lifetime default rate is a performance tool focused on the risk of default throughout the life of the loan. This rate will be updated and published annually.

Note that the total cost to taxpayers of $4,115 per graduated student for the for-profit institutions is based on an assumed 0% recovery rate for the defaulted federal direct loans. This assumption is conservative and highly unlikely to be consistent with the actual loan recovery experience. By increasing the recovery rate to 60%, the total cost to taxpayers for providing federal direct loans is only $1,646 per graduated student for the for-profit institutions.

## Exhibit 8: Total Taxpayer Cost For Funding Federal Direct Loans at Public 2-Year and Private For-profit Institutions

(U.S. Degree-granting Institutions, 2007-08)

| | | Public 2-Year Institutions | For-profit Institutions (2-year and Above) | Difference |
|---|---|---|---|---|
| | | [A] | [B] | [B] *minus* [A] |
| Federal Loans to Students Per Year (for students receiving loans) | [1] | $4,600 | $7,230 | |
| % of Full-time Students Receiving Federal Loans | [2] | 21.5% | 92.8% | |
| **Federal Loans Per Full-time Equivalent Student Per Year** | [3]=[1]*[2] | **$989** | **$6,709** | |
| Cumulative Lifetime Default Rate (based on cohort year 2003) | [4] | 21.4% | 26.0% | |
| Expected Loan Defaults Per Full-time Equivalent Student Per Year | [5]=[3]*[4] | $212 | $1,744 | |
| Assumed Recovery Rate of Defaulted Loans | [6] | 0% | 0% | |
| **Total Taxpayer Cost For Funding Federal Direct Loans Per Student Per Year** | [7]=[5]*(1-[6]) | **$212** | **$1,744** | |
| Average Years In School (Including Transfers and Dropouts) | [8] | 0.997 | 1.373 | |
| **Total Taxpayer Cost For Funding Federal Direct Loans Per Student For Completing the Program** | [9]=[7]*[8] | $211 | $2,395 | |
| Graduation Rate of Students | [10] | 29.8% | 58.2% | |
| **Total Taxpayer Cost For Funding Federal Direct Loans Per Graduated Student** | [11]=[9]/[10] | **$709** | **$4,115** | **$3,406** |
| Total Taxpayer Cost For Funding Federal Direct Loans Per Graduated Student (Assuming a 60% recovery rate for defaulted loans) | | $284 | $1,646 | $1,362 |

[10] For public 2-year institutions, graduation rate includes those students who were transferred to a 4-year institution and graduated with a Bachelor's degree, even though they did not complete an Associate's degree at the public 2-year institutions.

Sources: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009* , Tables 331, 343 and 344; Cumulative lifetime default rates as provided by the Department of Education; Charles River Associates calculations.

Lastly, we follow the same procedure to compute the total taxpayer cost for providing federal direct loans to the public 2-year institutions. According to our calculations, the total taxpayer cost for providing federal direct loans to students at public 2-year institutions was $709 per graduated student in 2007-08. The calculations are also shown in Exhibit 8. Thus, the difference in the total taxpayer cost for providing federal direct loans between for-profit institutions and public 2-year institutions is **$3,406** ($4,115 minus $709) per graduated student. This is significantly less than the higher direct government funding of **$28,953** per graduated student that was provided by the local, state and federal governments to the public 2-year institutions than to the for-profit 2-year institutions as discussed in the last section. The taxpayers saved **$25,546** ($28,953 minus $3,406) per graduated student by providing post-secondary education through for-profit 2-year institutions than public 2-year institutions.

## Appendix A

There are other education costs that are borne by taxpayers and private third parties that we did not include in our analysis. One added cost is foregone property tax. While for-profit institutions are required to pay property taxes on their land, infrastructure, buildings and improvements, not-for-profit institutions do not pay such taxes. For example, the University of California, Los Angeles and Los Angeles Community College District reported a book value of $18.2 billion and $584 million, respectively, in land, infrastructure and buildings for 2007. Assuming a 1% property tax rate, they would have to pay about $850 and $60, respectively, in property taxes per each enrolled student, by our calculations. The foregone property tax represents an indirect cost borne by the taxpayers to fund not-for-profit institutions.

Many post-secondary institutions also receive private gifts and generate investment income from these gifts to fund their capital budgets. Capital outlay funding is typically separate from operating budgets because of the different revenue sources and the longer horizon for amortizing costs. Many discussions of higher education costs, in particular cost benchmarking between institutions, focus on operating budgets while excluding capital outlay appropriations.

The practice of excluding capital outlay funding understates the cost to taxpayers for the post-secondary institutions. For instance, in the case of private gift donations, the donors typically receive a tax benefit from the federal and state government. Thus, the taxpayers indirectly subsidize the post-secondary institutions by foregoing the taxes that the state and federal governments would have received from the donors. In 2006-07 (last year with available data), the public institutions and private not-for-profit institutions received $5.6 billion and $20.2 billion, respectively, in private gifts.[8] In contrast, the for-profit institutions received only a tiny amount of $3.7 million in private gifts.[9] Given that the not-for-profit institutions received most of the private gift donations, they received substantial indirect benefits from the taxpayers.

[8] Source: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009,* Tables 352 and 355

[9] Source: U.S. Department of Education, National Center For Education Statistics, *Digest of Education Statistics 2009,* Table 357

For the for-profit institutions, the taxpayers also receive substantial benefits associated with the state and federal income taxes generated by these institutions. Based on financial data published by the publicly-traded for-profit institutions, the average combined state and federal income tax paid by these institutions was $728 per student in 2008, as shown in Exhibit 9. Unlike the for-profit institutions, the not-for-profit institutions do not have to pay any state or federal income tax.

**Exhibit 9: Income Taxes Paid to Government Per Student By Private For-Profit Institutions**

$ in millions

| | | Taxes | | Enrollment | | Tax Per Student | |
|---|---|---|---|---|---|---|---|
| Company | Ticker | 12/31/2009 | 12/31/2008 | 12/31/2009 | 12/31/2008 | 12/31/2009 | 12/31/2008 |
| Strayer Education Inc. | STRA | $ 68.7 | $ 50.6 | 55,106 | 45,697 | $ 1,246 | $ 1,107 |
| Capella Education Co. | CPLA | 23.6 | 15.4 | 33,982 | 26,883 | 696 | 572 |
| Universal Technical Institute Inc. | UTI | 12.1 | 3.0 | 17,741 | 15,143 | 682 | 201 |
| DeVry, Inc. | DV | 101.9 | 55.8 | 80,251 | 67,235 | 1,270 | 831 |
| Education Management Corporation | EDMC | 62.7 | 45.5 | 113,964 | 97,128 | 551 | 468 |
| Career Education Corp. | CECO | 78.7 | 38.5 | 105,300 | 87,700 | 747 | 439 |
| Lincoln Educational Services Corporation | LINC | 34.9 | 13.3 | 29,340 | 21,667 | 1,188 | 616 |
| Apollo Group Inc. | APOL | 466.6 | 347.3 | 420,700 | 345,300 | 1,109 | 1,006 |
| ITT Educational Services Inc. | ESI | 191.1 | 125.9 | 80,766 | 61,983 | 2,366 | 2,030 |
| Corinthian Colleges Inc. | COCO | 80 | 20 | 76,165 | 67,270 | 1,048 | 293 |
| Grand Canyon Education, Inc. | LOPE | 18 | 4 | 37,709 | 24,636 | 477 | 156 |
| American Public Education, Inc. | APEI | 16 | 10 | 12,060 | 6,730 | 1,328 | 1,517 |
| Bridgepoint Education, Inc. | BPI | 35 | 7 | 53,688 | 31,558 | 654 | 224 |
| | | 1,189 | 736 | 1,116,772 | 898,930 | **1,028** | **728** |

Source: CapitalIQ database, Legg Mason equity research

**Appendix B**

A prominent student loan program provided by the federal government is the Federal Direct Loan Program ("FDLP"). Under FDLP, commonly known as the direct loan programs, students or their parents borrow money directly from the federal government through the school attended by the student. The first FDLP loans were made in the fourth quarter of fiscal year 1994. The FDLP program is administered by the DOE. The FDLP loans offer substantial financial benefits to borrowers because of their favorable terms, including lower interest rates than private student loans, flexibility of repayment options, and deferment of debt service under certain circumstances. For direct unsubsidized loans, the interest rate is fixed at 6.8%.[10]

Under the Federal Credit Reform Act ("FCRA") of 1990 and subsequent legislation, the cost of a federal loan is the net present value of all future cash flows associated with the loans made. FCRA requires the present values to be calculated by discounting the expected cash flows at the borrowing rates of the federal government (i.e., interest rates on Treasury securities). The cash flows for the loans do not include federal government's administrative costs for operating the loan programs.

In its research report published in November 2005, the Congressional Budget Office ("CBO") calculated the subsidy rates for the federal direct loans. CBO determined the subsidy rate of federal direct loans by discounting the cash flows to the year of the loan's disbursement to reflect the time value of money. For FDLP, there are two cash flows at the time of loan's disbursement: the disbursement of the loan to the individual borrower, and the loan origination fees of 1.5% that are charged by the government to the borrower. The cash flows over the life of the loan are based on the repayments of loan principal and interest by the borrower to the government. The repayment plan selected by a borrower has a large impact on the length and timing of the cash flows.

[10] Borrowers of direct unsubsidized loans are not required to demonstrate financial need. Direct subsidized loans are for students with financial need. The interest rate of direct subsidized loans for undergraduates is to be fixed at 4.5% if the first disbursement is between July 1, 2010 and June 30, 2010. The interest rate of direct subsidized loans for graduates and professional degree students are fixed at 6.8%.

In its study, CBO calculated a subsidy rate of -2.1% based on a hypothetical $3,000 direct loan that follows a standard 10-year plan. The negative subsidy rate indicates that the federal government records a budgetary savings of $0.02 for each dollar of direct loan made. The federal government is expected to make money on the direct loans because the interest rates charged by the federal government on the direct loan are higher than the Treasury rates. In the hypothetical example used by CBO, the loan rate was about 6.5% whereas the discount rate was only 5.3%. Given today's low Treasury rates, the subsidy rate will be higher. For instance, as of September 3, 2010, the interest rate on 10-year Treasury securities was only 2.72%. Based on the CBO hypothetical example and a loan rate of 6.8%, we calculate the subsidy rate to be -20.3% as shown in Exhibit 10A. This shows that the government generates substantial income by making direct loans to students, assuming there is no default on the loan.

**Exhibit 10A: Subsidy Rate for a Hypothetical $3,000 Loan Under the Direct Loan Program**

| | |
|---|---|
| Discount Rate | 2.72% |
| Loan Rate | 6.80% |
| **Subsidy Rate:** | **-20.3%** |

| | | Nominal Cash Flows | | | | | | | | | | | | Present Value of |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | **Total Cash** |
| | Disbursement | | | | | | | | | | | | | |
| [1] | Principal disbursement | 3,000 | | | | | | | | | | | | 3,000 |
| [2] | Borrower's origination fee | (45) | | | | | | | | | | | | (45) |
| | Repayment | | | | | | | | | | | | | |
| [3] | Principal | | | (219) | (234) | (250) | (267) | (285) | (305) | (325) | (347) | (371) | (396) | (2,491) |
| [4] | Interest | | | (204) | (189) | (173) | (156) | (138) | (119) | (98) | (76) | (52) | (27) | (1,074) |
| **[5]** | **Total Costs** | 2,955 | | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (610) |

Sources:
On-the-run 10-year Treasury rate from www.ustreas.gov
A CBO Paper, *Subsidy Estimates for Guaranteed and Direct Student Loans*, November 2005.

Note:
Discount rate is based on on-the-run 10-year Treausry rate as of 9/3/2010.

A loan is considered to be in default if the borrower fails to make a payment for 270 days (330 days if payments are due less frequently than each month). If a borrower defaults on a federal student loan, the obligation to repay cannot be discharged by filing bankruptcy under the current law. The government, through its various means, can collect the delinquent loans during the entire lifetime of the borrower. The government can utilize private collection agencies to collect the loans. It can also garnish wages and use the Treasury Offset Program to collect a

portion of federal transfer payments that the delinquent borrowers receive (e.g. tax refunds or Social Security benefits).

Even when there is a loan default, the net cost to the federal government is small if the government eventually recovers the loan principal and interest. This is because the federal government only loses the time of value of money on the repayment of loan principal and interest. To illustrate this point, we re-calculate the subsidy rate based on the hypothetical example discussed above but assume that the borrower delays the loan payments by two years. Under this scenario, the subsidy rate is calculated to be -14.1%, as shown in Exhibit 10B. The negative subsidy rate shows that the government still makes money on the loan on a net present value basis. Thus, as long as the federal government recovers its loan principal and interest, loan defaults are not costly to the federal government. According to the data published by the Office of Management and Budget ("OMB") for the budget in fiscal year 2011, the recovery rate of all obligations under the FDLP programs is estimated to be 110.60. This means that the government is expected to fully recover the loan principal and an interest of $0.11 for each dollar of direct loan made. OMB did not break down the recovery rate between not-for-profit and for-profit institutions.

**Exhibit 10B: Subsidy Rate for a Hypothetical $3,000 Loan Under the Direct Loan Program**
**(Assumes a delay of payment by 2 years)**

| | |
|---|---|
| Discount Rate | 2.72% |
| Loan Rate | 6.80% |
| **Subsidy Rate:** | **-14.1%** |

| | | Nominal Cash Flows | | | | | | | | | | | | | | Present Value of Total Cash Flows |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | |
| | Disbursement | | | | | | | | | | | | | | | |
| [1] | Principal disbursement | 3,000 | | | | | | | | | | | | | | **3,000** |
| [2] | Borrower's origination fee | (45) | | | | | | | | | | | | | | (45) |
| | Repayment | | | | | | | | | | | | | | | |
| [3] | Principal | | | | | (219) | (234) | (250) | (267) | (285) | (305) | (325) | (347) | (371) | (396) | (2,361) |
| [4] | Interest | | | | | (204) | (189) | (173) | (156) | (138) | (119) | (98) | (76) | (52) | (27) | (1,018) |
| **[5]** | **Total Costs** | 2,955 | | | | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (423) | (423) | **(424)** |

Sources:
On-the-run 10-year Treasury rate from www.ustreas.gov
A CBO Paper, *Subsidy Estimates for Guaranteed and Direct Student Loans*, November 2005.

Note:
Discount rate is based on on-the-run 10-year Treausry rate as of 9/3/2010.