



Closing “Covert For-Profit” Loophole that Allows Colleges and Universities to Escape Accountability

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America’s colleges and universities are a source of national pride. While there are ongoing national discussions about college affordability and the heavy burden of student loan debt, there is little doubt about the quality and value of most American college degrees. The pay gap between college graduates and everyone else, for example, has never been higher.¹

But, this tradition of quality and value does not quite hold up in the for-profit college sector, where owners and investors can enrich themselves at the expense of their students. Due to a long history of scandal going back decades,² for-profit colleges have a deservedly bad reputation. Owners of for-profit schools, fueled by taxpayer-backed student loans, frequently grow their schools rapidly,³ while overcharging for the education and using the proceeds for aggressive recruiting and profit.⁴ In many cases, the schools mislead prospects about the value of their schools’ programs⁵ and the promise of a high-paying job.⁶ They commonly use manipulative sales tactics,⁷ hire unqualified faculty,⁸ enroll unprepared students,⁹ and hide their misdeeds through forced arbitration clauses,¹⁰ all while leaving students with crushing student loan debts¹¹ and school executives and investors with bulging bank accounts.¹²

Practices in the sector have eviscerated the value of a for-profit college degree—many programs have a negative value, meaning that graduates’ wages fall below those of a high-school degree holder, and sometimes below poverty level.¹³ A study of outcomes of the schools that are the most driven by profit—

those owned by private equity investing firms—found that private equity control of schools leads to “higher enrollment and profits, but also to lower education inputs, lower graduation rates, higher tuition, higher per-student debt, lower student loan repayment rates, and lower earnings among graduates.”¹⁴

Highly visible scandals at for-profit colleges such as ITT Tech and the University of Phoenix educated consumers and policymakers about the hazards of investor control of schools, and this increased scrutiny has contributed to a decline in enrollment at for-profit schools.¹⁵

But some for-profit executives have found a way to claim nonprofit status without adopting the nonprofit financial accountability that has largely prevented predatory practices at public and nonprofit schools. Companies that take this deceptive approach are getting away with it in growing numbers, racking up more fraud complaints than nonprofit schools not compromised by financial entanglements with former owners.¹⁶

Congress can address this problem of “covert for-profit” colleges by taking three steps:

- + Restoring the budget and vigor of the IRS’s oversight of charities. For many decades, the IRS has been the lead agency policing the validity of claims of nonprofit control, with experienced staff who did detailed examinations of corporate governance and financial ties. Budget cuts

by Congress, however, have practically eliminated the agency's enforcement capability, allowing covert for-profits to claim IRS approval.¹⁷

+ Tightening the requirements for a college to be considered a nonprofit by ensuring that the school's board has no financial interest in the school and is fully in control, not ceding power to an executive, contractor or landlord, as proposed here.¹⁸

+ Requiring that, when a college converts from for-profit to nonprofit, it goes through a rigorous review of the terms of the conversion, as proposed here.¹⁹

Valid public and nonprofit control of colleges has proven to be the most effective way to prevent them from taking unfair advantage of students and taxpayers, and to hold the colleges and their leaders accountable when they do. Preserving the integrity of nonprofit and public status is among the most important steps Congress could take to protect America's college students.

Notes

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