Drowning in Debt: Financial Outcomes of Students at For-Profit Colleges

Testimony to the Senate Health, Education, Labor and Pensions Committee

Dr. Sandy Baum
Senior Fellow, George Washington University School of Education and Human Development
Senior Associate, Institute for Higher Education Policy
Independent Policy Analyst for the College Board
Associated Consultant, HCM Strategists

June 7, 2011

The title of this hearing suggests two major areas of concern. One is the impact of education debt on students. The other is the role of for-profit colleges in serving a growing portion of the postsecondary population. Student loans are an important and justified component of our higher education financing system. For-profit colleges provide a valuable alternative for some students and some institutions in this sector engage in some practices that public and private nonprofit colleges would be wise to emulate. But there is overwhelming evidence that large numbers of students, particularly students from low-income backgrounds, are suffering great hardship as a result of the excessive borrowing required to finance their enrollment in for-profit institutions. It is easy to find individual success stories in this sector, just as it is easy to find individual stories of over-borrowing and failure in the nonprofit sectors. But these anecdotes can't change the compelling story told by the data. Borrowing large sums of money to enroll in the for-profit sector is a ticket to personal crisis for a large proportion of students. Institutions that leave students worse off than they were when they arrived are the exception in the public and private nonprofit sectors. Unfortunately, they appear to be the norm in the for-profit sector.

In this testimony, I will begin by summarizing some of the data on student debt across postsecondary sectors and will then analyze why we face this very serious problem and suggest constructive ways of approaching it.

Student Borrowing Patterns

Table 1: Student Loan Debt of 2007-08 Degree and Certificate Recipients

2007-08	Median loan debt (2007-08)	Degree Recipients with Federal Loans	Degree Recipients with Non-Federal Loans	Degree Recipients with Any Education Loan	Average Federal Loan Debt	Average Non-Federal Loan Debt	Average Total Loan Debt
Bachelor's degree	$20,000	62%	33%	66%	$17,800	$12,600	$23,100
Public 4-Year	$17,700	58%	28%	62%	$16,900	$9,800	$20,200
Private 4-Year	$22,400	69%	42%	72%	$18,700	$16,900	$27,600
Private For-Profit	$32,700	94%	64%	96%	$25,900	$11,500	$33,100
Associate's degree	$10,000	43%	22%	48%	$11,100	$7,000	$13,300
Public 2-Year	$7,100	33%	15%	38%	$9,000	$5,700	$10,100
Private For-Profit	$18,800	97%	60%	98%	$14,700	$8,400	$19,700
Certificate	$9,000	58%	34%	63%	$8,900	$5,900	$11,300
Public 2-Year	$6,500	24%	12%	30%	$8,900	$4,500	$8,800
Private For-Profit	$9,700	85%	51%	90%	$8,600	$5,900	$11,500
Source: National Postsecondary Student Aid Study 2008							

As Table 1 indicates, 62% of 2007-08 bachelor's degree recipients graduated with student debt. The median debt among borrowers was about $20,000. Among those who received their degrees from for-profit institutions, 96% had debt and the median amount they borrowed was $32,700. Most of these students took federal loans, but two-thirds of the four-year college graduates from this sector also relied on nonfederal loans, which carry higher interest rates and lack the repayment protection provisions of federal student loans.

Averages hide important differences among students. While the typical college graduate has a manageable amount of student debt and a credential that will pay off well in the labor market, there are too many exceptions to this pattern. These exceptions are highly concentrated in the for-profit sector.

Table 2: Distribution of Total Undergraduate Debt by Sector and Type of Degree of Certificate, 2007-08

	No Debt	Less than $10,000	$10,000 to $19,999	$20,000 to $29,999	$30,000 to $39,999	$40,000 or more
Bachelor's Degree						
Public Four-Year	38%	16%	19%	14%	6%	6%
Private Nonprofit Four-Year	28%	10%	19%	17%	10%	15%
For-Profit	4%	4%	12%	23%	33%	24%
Associate Degree						
Public Two-Year	62%	23%	9%	3%	1%	1%
For-Profit	2%	22%	34%	23%	13%	6%
Certificate						
Public Two-Year	70%	21%	7%	1%	1%	0%
For-Profit	10%	46%	34%	8%	2%	1%

Note: Data include federal loans, private loans, and loans from states and institutions. Parent PLUS Loans, credit card debt, and loans from friends and family are not included. Percentages may not sum to 100 due to rounding. Data include students who attended less than half-time (13% of students), and who do not qualify for Stafford loans but do qualify for some nonfederal loans.
Source: *NPSAS*, 2008.

While many students in other sectors graduate without debt, this is not the case in the for-profit sector. Moreover, as reported in Table 2, 57% of 2007-08 bachelor's degree recipients from this sector graduated owing $30,000 or more. In contrast, 25% of those who earned their degrees in the private nonprofit sector and 12% from the public sector borrowed this much. Over 60% of the students who earned associate degrees from public two-year college graduated debt-free. Only 2% of those earning associate degrees and 10% of those earning certificates from for-profit institutions were in this situation. While only 5% of public sector AA degree recipients owed as much as $20,000, 42% of those from the for-profit sector had this much debt.[1]

[1] Sandy Baum and Patricia Steele, "Who Borrows Most?" The College Board, 2010.

Table 3: Median Debt of 2007-08 Bachelor's Degree Recipients, by Dependency Status and Income

	Dependent Student Family Income					
	Less than $30,000	**$30,000 to $59,999**	**$60,000 to $89,999**	**$90,000 to $119,999**	**$120,000 or Higher**	**Independent Students**
Public Four-Year	$16,500	$17,400	$17,000	$16,300	$14,500	$20,000
Private Nonprofit Four-Year	$21,000	$23,100	$21,100	$22,000	$18,000	$24,600
For-Profit	$30,500	$24,600	$34,600	$28,000	$34,300	$32,700
Percentage with Debt						
Public Four-Year	68%	69%	61%	52%	40%	68%
Private Nonprofit Four-Year	84%	83%	75%	68%	74%	74%
For-Profit	99%	99%	99%	99%*	99%*	95%
Source: NPSAS 2008						

Students from affluent families are less dependent than others on borrowing to finance their education. The same is true for independent students. In 2007-08, 80% of the undergraduate students enrolled in the for-profit sector were independent, relying only on their own resources and financial aid, primarily from the federal government. Fewer than 60% of public two-year college students were in this category. About half of the dependent students enrolled in for-profit institutions came from families with incomes below $40,000. This compared to 35% in two-year public colleges and about 25% in four-year public institutions[2].

However, as shown in Table 3, controlling for dependency status and income leaves wide differences in the borrowing patterns across sectors. Because very small numbers of dependent students from affluent families enroll in for-profit institutions comparisons of low-income students are more meaningful. The 68% of dependents students from families with incomes below $30,000 who borrowed for the bachelor's degrees they earned from public colleges in 2007-08 had median debt of $16,500. The 99% of students from this income category who borrowed for the bachelor's degrees they earned from for-profit colleges had median debt of $30,500. Independent students graduated with median debt of $20,000 from public colleges, $24,600 from private nonprofit colleges and $32,700 from for-profit colleges.

Among low-income Hispanic students, 43% of 2007-08 for-profit bachelor's degree recipients had debt exceeding $30,500. This was true of 22% percent of those earning degrees in the private nonprofit sector and only 1% of those who graduated from public colleges and universities.[3]

[2] Sandy Baum, Jennifer Ma, Kathleen Payea, *Education Pays 2010*, The College Board.

[3] Patricia Steele and Sandy Baum, "Who Borrows Most?" The College Board, 2010

The large numbers of students who enroll in postsecondary institutions but never earn a degree or certificate are not included in these data on the debt levels of graduates. Bachelor's degree completion rates are much lower in the for-profit sector than in other sectors. Of first-time full-time students who began studying for a bachelor's degree at a four-year institution in 2002, 57% earned a B.A. at the institution at which they began within six years. Completion rates averaged 65% at private nonprofit, 55% at public four-year, and 22% at private for-profit institutions.

Among students at for-profit four-year institutions, 16% of blacks and 28% of Hispanics who enrolled in 2002 had earned a bachelor's degree six years later. Among those who enrolled at public four-year colleges and universities, 39% of blacks and 46% of Hispanics had earned degrees. The gaps between completion rates for black first-time full-time students and those for white and Asian students are larger in the for profit sector than in the public and private nonprofit sectors.[4]

The story for shorter-term institutions, which enroll just over one-third of students in the for-profit sector, is much more encouraging for that sector. Reported completion rates for two-year institutions include both two-year degrees and certificates earned over shorter periods of time. These completion rates for students who began their studies in 2004 were highest in the for-profit sector, where 60% of full-time students completed their credentials within three years, compared to 50% of those in private nonprofit and 22% of those attending public two-year colleges.

Table 4: Percentage Borrowing and Average Amounts Borrowed Among All Students and Among Full-Time Students by Dependency and Sector, 2007-08

	Percent with Any Loan	Percent with Federal Loans	Average Federal Loan per Borrower	Average Federal Loan per Student	Percent with Private Loans	Average Private Loan per Borrower	Average Private Loan per Student	Private Loans as a Percentage of Total Borrowed
Full-Time Students								
All Students	54%	50%	$5,400	$2,700	19%	$7,800	$1,500	36%
Dependency								
Dependent	50%	46%	$4,800	$2,200	18%	$8,400	$1,500	41%
Independent	65%	62%	$7,000	$4,300	23%	$6,300	$1,500	25%
Sector								
Public 4-Year	54%	50%	$5,200	$2,600	15%	$7,000	$1,100	29%
Private Nonprofit 4-Year	66%	62%	$5,600	$3,500	28%	$10,200	$2,900	45%
Public 2-Year	23%	20%	$4,100	$800	7%	$4,400	$300	26%
For-Profit	92%	88%	$6,400	$5,700	43%	$7,100	$3,100	35%

Source: Patricia Steele and Sandy Baum, "How Much are College Students Borrowing," The College Board, 2009; NPSAS 2008.

[4] NCES, Beginning Postsecondary Students 2009, http://nces.ed.gov/datalab/index.aspx

The annual borrowing data reported in Table 4 include both those students who will go on to earn degrees and those who will not. In 2007-08, when 54% of all full-time students relied on loans to finance their studies and 19% borrowed from private sources, 92% of those enrolled in for-profit institutions borrowed and 43% took private loans. Full-time for-profit students borrowed an average of $5,700 in federal loans and $3,100 in private loans per student. Those enrolled in private nonprofit colleges and universities borrowed an average of $3,500 in federal loans and $2,900 in private loans per student. The parallel figures for public four-year colleges were $2,600 and $1,100 and public two-year college students borrowed only an average of $800 in federal loans and $300 in private loans.

Default Rates

In FY 2009, the official default rate for for-profit four-year institutions was 16%. For four-year colleges in the public and private nonprofit sectors it was 5%. The default rate for for-profit two-year schools was 15%. For public two-year colleges it was 12%.[5] But as noted above, a relatively small percentage of students in this sector rely on student loans. While the default rate for for-profit institutions is a close approximation of the percentage of students from that sector who have defaulted on loans, the default rate for community colleges has to be divided by 3 or 4 to arrive at an estimate of the percentage of students from that sector who default.

Students at some private nonprofit colleges accumulate high debt levels because of high sticker prices and inadequate institutional aid. However, these schools are few and far between. Out of 1,635 private nonprofit schools, 30 have a default rate over 30%. Students enrolled in these 30 schools constitute 1.1% percent of all private nonprofit enrollment and account for 0.8% of all private nonprofit students in repayment and 4.3% of all private nonprofit defaults. Ninety-three colleges in this sector – 6% of the total - have a default rate over 20%. Students enrolled in these 93 schools constitute 8.6% of all private nonprofit enrollment, and account for 5.2% of all private nonprofit students in repayment and 20.2% of all private nonprofit defaults.

In contrast, out of 1,806 for-profit schools, 273 have a default rate over 30%. Students enrolled in these schools constitute 13.8% of all for-profit enrollment and account for 15.1% of all for-profit students in repayment and 24.6% of all for-profit defaults. A startling 792 for-profit schools – 44% of the total – have a default rate over 20%. Students enrolled in these schools constitute 68.6% of all for-profit school's enrollment and account for 66.8% of all for-profit students in repayment and 79.2% of all for-profit defaults.[6]

Student loan default is a very real problem for the federal government. The problem is not just loss in taxpayer dollars. Our education financing system is far from perfect, but we

[5] http://www.ifap.ed.gov/eannouncements/attachments/052011AttachFY2009FY2009_DraftNationalCDRWithPrior2yrscomparison.pdf

[6] Data provided by staff of the U.S. Senate Committee on Health, Education, Labor, and Pensions in May 2011.

have made choices about relying on general subsidies from state and local governments to public institutions and on targeted federal subsidies to individual students, combining loans with grants. Loans that are not repaid end up as subsidies to students allocated partially on the basis of financial difficulty, but also on the basis of some combination of failure to succeed in the educational system and failure to manage responsibilities. But student loan default is an even bigger problem for individuals. A student who ends up not benefiting from his education who either did not borrow or borrowed a small amount has lost time, a financial investment, and an opportunity. But a similar student who ends up defaulting on her loans will be plagued by much larger financial problems for years to come.

How is the For-Profit Sector Different from Other Postsecondary Sectors?

The prevalence of high debt levels and high default rates in the for-profit sector justifies a focus on this sector. Individual institutions and categories of students in other sectors who are in similar circumstances also merit particular attention. But it is worth thinking analytically about why so many problems are concentrated in for-profit institutions. Too much of the debate on this issue is tinged with ideology. Are critics of the sector opposed to market forces or to the idea of profits? Are owners, managers and supporters of the sector evil people who cannot see beyond their own pocketbooks?

The reality is that the fundamental purpose and structure of for-profit entities differs from that of public and nonprofit entities. If the outcomes of these structures could not be differentiated, proponents of the free market would not be such strong opponents of a larger role for government in the production of goods and services. The market works very well for our economy and our society in many cases. But it is not difficult to see that all market outcomes are not optimal. We have seen all too well in recent years the dangers of inadequate consumer protection, inadequate information, and inadequate regulation of financial markets. By definition, for-profit enterprises are run with the goal of maximizing profits. Managers have a fiduciary responsibility to make the interests of owners their primary focus.

When the for-profit sector was smaller, it consisted largely of small privately owned institutions. Some owners of for-profit colleges founded their institutions to provide specific opportunities to specific types of students and are deeply committed to the well-being of their students. But the sector is increasingly dominated by large, publicly held companies. Where it exists, good will and social consciousness on the part of the officers of these companies can only go a limited distance in determining how the firms operate. Comparison of compensation levels in the three major sectors of postsecondary education is instructive. Average compensation for the five highest-paid public university chief executives in 2009-10 was $860,000. The five highest-paid Ivy League presidents received an average of $1.3 million in 2008-09. The top five leaders of publicly traded for-profit postsecondary institutions received and average of $10.5 million in 2009.[7]

---

[7] http://chronicle.com/premium/stats/990/private/private.php?year=2009&Order=pay; http://chronicle.com/article/Sortable-Table-Compensation/126965/;

In our market economy, firms have to continue to grow in order to be appealing to investors. Between fall 2000 and fall 2009, full-time enrollment in degree-granting institutions in the for-profit sector increased from 366,000 to 1.5 million. In just nine years, the sector went from enrolling 4% of full-time students (and 3% of all students) to enrolling 11% of full-time students (and 9% of all students). Among students in this sector, 61% are enrolled in institutions that offer four-year degrees, 24% are in two-year institutions, and 15% attend less-than-two-year institutions.[8]

Among students who earned bachelor's degrees, 76,000 (5% of the total) came from the for-profit sector in 2007-08. The for-profit sector awarded 127,000 associate degrees — 17% of the total. In 2008-09, students in the for-profit sector received 25% of all subsidized and 28% of all unsubsidized Stafford Loans.[9]

Economic theory suggests that market forces lead to efficient outcomes if certain stringent conditions are met. These conditions include the absence of significant externalities – the costs and benefits of the product or activity must accrue to the direct participants without significant impact on others - and notably, perfect information. Consumers must have the information necessary to make sound judgments about which products and services will meet their demand. They must understand the characteristics of what they buy, how the products and services produced by different firms compare, and the prices they will pay. The rapid growth in enrollments in the for-profit sector is not just a reflection of increased demand. It's not that so many students are suddenly making informed decisions about the best way to realize their educational dreams. A combination of aggressive recruiting and the growing funding and space constraints in the public sector have changed the way students perceive their options.

The market for higher education meets few of the requirements for perfect competition. Students can't buy one, try it, and buy a different brand next time if they are unhappy with the outcome. There is little market incentive for producers to provide thorough and accurate information because they do not rely on repeat customers and once students make a choice, it is likely to take them a long time – and a lot of payments – before they learn the true properties of what they have purchased.

Well-designed consumer protection makes market forces work more effectively. It doesn't make sense to have students give up large amounts of time, energy, and money to test for themselves whether institutions offer reasonable education and training. Postsecondary education is an investment that typically provides a high rate of return to both the students who participate and to society as a whole. But it can be a risky investment. If we subsidized

---

http://chronicle.com/article/Graphic-CEO-Compensation-at/66017/

[8] Sandy Baum, Kathleen Little and Kathleen Payea, "Trends in For-Profit Postsecondary Education", The College Board, forthcoming.
[9] The College Board, *Trends in Student aid 2010*.

only students who have a very high probability of succeeding and seeing their investment pay off handsomely, we would fail to provide opportunities to many individuals who cannot afford them on their own. We know some students will fail, either because they aren't up to the task or because circumstances interfere with their success.

But we shouldn't subsidize students to play the lottery. Students who enroll in institutions or programs that graduate fewer than 20% (or 15% or 30%) of their students or that succeed in placing only a small percentage of their students in remunerative positions in the fields for which they have been trained are playing the lottery. They are making a significant investment in an undertaking that has a stunningly low probability of success. Our political philosophies might lead us to debate whether or not we should prevent them from playing this lottery. But it is difficult to come up with sound principles of public policy that would support our subsidizing them to play this lottery. And unfortunately, even the best available information is unlikely to discourage the most vulnerable students from playing the lottery with a combination of taxpayer funds and funds they will only have to pay off in a vague and distant future.

Public Subsidies

There is nothing inherently wrong with people making profits from providing education. And no doubt there are some efficiencies in the for-profit sector that could, if applied in other sectors, both improve the learning experiences of students and reduce the cost of providing those experiences. But holding up this sector as an example of market forces at work is simply inaccurate. Many institutions in this sector receive close to 90% of their revenues from federal student aid. That number is actually higher if the federal funds that are excluded under the 90/10 regulations are considered. Very few students are actually paying with their own money to enroll in these institutions. Why is it that only independent students and dependent students from low-income families choose the for-profit sector? Don't these particularly vulnerable students, who are most likely to be making their educational choices without the advice of college-educated parents or well-trained counselors deserve added consumer protection, rather than maximum opportunity to make decisions with a high probability of damaging their futures?

Surely there should be better regulation of an industry that is so heavily financed by taxpayers and that has such a dramatic influence on the lives of so many Americans – particularly vulnerable Americans. Advocates of the sector frequently contend that restrictions on their institutions will deprive low-income students of educational opportunities. But if these opportunities lead to heavy debt burdens and questionable credentials, they are not opportunities in any meaningful sense of the word. Is it wrong to regulate payday lenders because it might deprive vulnerable individuals of the right to borrow money at extraordinary interest rates and generate debts they will never be able to repay? Is it wrong to regulate car dealers because we might deprive consumers of purchasing cars that have every likelihood of self-destructing on the road? Institutions in the for-profit sector that are serving their students well should be first in line arguing for protection against their colleagues whose drive for profits is exploiting students and undermining our ability to use market forces to the fullest to further our educational goals.

Conclusion

Encouraging students to pursue postsecondary education is vital to the future of our nation and to the futures of individual students, particularly those who come from environments where they have limited resources and limited educational experiences. The only way we can succeed in providing the educational opportunities our diverse population requires is to assure the health and stability of a variety of postsecondary institutions serving a variety of needs.

Many people concerned with improving educational opportunities speak of student debt as though it were a blight on the higher education landscape and a clear sign of the moral weakness of our society. In fact, the existence of a robust federal student loan program is a tribute our nation's commitment to postsecondary educational opportunity. Higher education is the best investment most young people can make. No one would suggest that people refrain from starting well-conceived and well-researched small businesses if they don't have the cash up-front. The idea is that the investment will pay off over time – enough to repay the necessary loans and then some. Comparisons of the success rate for investments in college and investments in small businesses overwhelmingly favor college.

But college does not turn out to be a good investment for everyone who tries it. We certainly don't want to discourage students who are not virtually assured of success from taking the risk of enrolling. But that doesn't mean we should encourage every student to pursue whatever educational path might tempt them. And we should certainly think carefully about the incentives we provide students and about the extent to which we protect them against risk.

For-profit institutions are capable of improving student outcomes. In fact, in anticipation of greater government regulations, some institutions have taken steps to restrict the enrollment of students with little chance of succeeding, to counsel students more effectively about borrowing, and to find other ways of reducing their attrition and default rates. But they won't take these steps on their own. And the students who unwittingly become the victims of the drive for profits cannot wait for solutions far in the future.

Debating how best to resolve the problem of student debt among students who enroll in for-profit postsecondary institutions should not be a debate about free markets versus government intervention. The market for higher education does and should rely heavily on market forces. But it is not and never will be a textbook example of competitive markets. The for-profit sector, which has the potential to make important contributions to educational opportunity in the United States, relies on the federal government for most of its revenues. Virtually all students borrow – and borrow heavily – to study in this sector. Almost half of the institutions in this sector have official student loan default rates over 20%. Some institutions in this sector successfully meet the needs of their students but they are a dwindling portion of the sector. Unfortunately, the rapid enrollment growth in this sector does not reflect informed consumer response to a high quality product. With more transparency and more consumer protection, the for-profit sector will be able to make greater contributions to our educational system without damaging the futures of so many vulnerable students.