Legislative Fiscal Bureau

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Educational Approval Board Student Protection Fund (Veterans Affairs -- General Agency Provisions)

[LFB 2003-05 Budget Summary: Page 460, #13]

CURRENT LAW

The Educational Approval Board (EAB) regulates more than 125 for-profit postsecondary schools, in-state nonprofit postsecondary institutions incorporated after January 1992, and out-of state nonprofit colleges and universities. The operation of the EAB is supported from a variety of fixed and variable fees.

The Board charges fixed fees for such actions as the approval of new schools and the approval of new or revised programs of study. The amount of the fee is based on the type of degree program being offered.

The general costs of EAB's operations are supported by annual renewal fees that are comprised of: (1) a fixed $500 payment; and (2) a proportionate fee sufficient to cover the Board's regulatory costs, less revenues from all other fees. Each institution's fee is based on its proportionate share of adjusted gross annual revenue to total adjusted gross annual revenues of all regulated schools times an annual assessment factor set to generate the required funding need. Currently, this assessment factor is $4.8711 per $1,000 of an institution's adjusted gross annual revenues.

The statutes also authorize the EAB to require regulated schools to post surety bonds. EAB requires most institutions to provide a surety bond equal to 125% of the amount of tuition collected. The purpose of the bond is to reimburse students, parents, or other sponsoring agents if the institution is unable to fulfill its contractual education obligations to the student.

Base level funding for the EAB is $433,900 PR annually. The Board is attached administratively to the Department of Veterans Affairs.

GOVERNOR

Provide $60,300 PR in 2004-05 under a new, PR continuing student protection appropriation under EAB. Specify that the new appropriation would be funded from fees received from proprietary schools to support a new student protection fund. Authorize the EAB to: (1) make payments to students, parents, or sponsors for full or partial tuition losses arising from the closure of a proprietary school; and (2) specify a fee, by administrative rule, that proprietary schools would have to pay into the fund.

DISCUSSION POINTS

1. Among other duties, the EAB is required to: (a) establish rules, standards and criteria to prevent fraud and misrepresentation in the sale and advertising of courses and courses of instruction; (b) promulgate rules on education loans, grants, and tuition payments; and (c) establish minimum standards for tuition refunds.

2. The Board requires regulated schools to estimate the number of students that will be attending their institution and to provide a surety bond equivalent to 125% of the estimated unearned tuition from these students. "Unearned tuition" constitutes the monies paid between the time the student pays tuition to an institution and the time at which the student completes the coursework for which the tuition is paid. The bond is intended to fund any obligations of the school to its students and others in the event the institution closes unexpectedly.

3. In most cases, enrollments from year-to-year are relatively stable and the amount of the required surety bond can easily be determined. In setting the amount of the surety bond, EAB staff typically rely on information that is contained in the school's annual financial report. Further, schools with a stable financial history, consistent satisfactory completion of instructional offerings, and accreditation by a recognized accrediting body may be granted a waiver by the Board and authorized a lowered surety bond level.

4. In 2002-03, some 85 institutions had posted surety bonds at or above the 125% of estimated unearned tuition level, while some 40 institutions had surety bonding below the threshold. (Of these 40 institutions, 32 had an EAB waiver.)

5. Currently, the amount of an institution's required surety bond ranges from $1,000 per year to $1,130,000 per year. The Board estimates that the cost of maintaining a surety bond for most institutions averages about $10 for every $1,000 of school revenues.

6. In the case of new institutions or institutions that offer a number of popular, new courses in emerging fields, actual course enrollments may be significantly higher than the projections used for purposes of establishing the amount of the surety bond. Where these types of institutions fail, the amount of the surety bond will typically not be sufficient to refund unearned tuition, fees or other obligations due the affected students.

7. Since 1995, there have been seven instances of what the Board terms "precipitous school closures." In all but one instance, the amount of the available surety bond was insufficient to cover the amounts due to students and others. The amounts due the displaced students ranged from $0 to more than $435,000 per school closing. In the absence of coverage by a surety bond, the Board had no recourse for providing relief to the affected individuals.

8. The Board believes that additional protection for such students could be achieved through the establishment of a student protection fund. All regulated schools in the state would be assessed proportionately for the purpose of establishing the fund. Once the fund is established and becomes operational, any future losses in excess of a failed institution's surety bond would be paid from the student protection fund.

9. The Board states that such a student protection fund would be built to an "appropriate level based on the fund's risk potential and a comprehensive review of such funds in other states. Initial discussions have focused on a $1,000,000 cap." Board staff have advised that a $1,000,000 reserve could be built up in four to five years, depending on withdrawals based on insufficient funds from school closings.

10. The Governor's recommendation would give the EAB the authority to establish a student protection fee amount by rule and to make payments from the student protection fund in the event of a school closure. Board staff have indicated that the student protection fee would likely be added to the variable portion of the renewal fee collected annually from regulated institutions. The Board's proposal anticipates that the amount of the annual fee would $1 per $1,000 of adjusted gross annual school revenues.

11. An argument in favor of establishing a student protection fund is that once the fund has achieved a suitable balance, it is likely that the Board could reduce current surety bonds requirements. While it is unknown at this time the amount of surety bonds that would be required once a sufficient balance was established in the student protection fund, the Board believes that the regulated institutions would realize savings. This is because the estimated annual costs of maintaining the student security fund [approximately $1 per $1,000 of annual revenues] would be less than the current funding requirements for a surety bond [approximately $10 per $1,000 of annual revenues]. While some level of surety bond would still likely be required, it can be argued that these costs would almost certainly be less than current requirements and net savings for the institution would be expected.

12. Further, in the absence of such a fund, it can be argued that there would be no other recourse available to students who incurred losses due to a school closure, where the amount of the required surety bond proved insufficient. Consequently, the Committee may view the establishment of a protection fund of last resort as desirable in this light.

13. Alternatively, it could be argued that the establishment of a statewide fund would force stable institutions to pay into a fund that would likely be used only to protect against high-risk, short-lived institutions. Further, given the relative infrequency of sudden school closures, the

Committee could conclude that the problems the fund is intended to address are so infrequent that the creation of the fund and the associated regulatory and assessment mechanisms would not be warranted.

14. However, if the Committee chooses to approve the Governor's recommendation and establish a student protection fund, the Committee may also wish to establish a limit on the amounts that may be assessed for the fund. The Board has indicated that a fund of approximately $1,000,000 appears reasonable. The Committee could include language limiting the Board from making further annual assessments for the fund any time the balance in the fund exceeds $1,000,000. With this type of limitation, any time the fund might be drawn down below the $1,000,000 threshold, the Board could resume assessments to replenish the fund.

ALTERNATIVES

1. Approve the Governor's recommendation providing $60,300 PR in 2004-05 under a new PR, continuing student protection fund appropriation under EAB, authorizing the Board to make payments from the fund to students and others for full or partial tuition losses arising from the closure of a proprietary school, and authorizing the establishment of a fee, by administrative rule, that proprietary schools must into the fund.

2. *In addition to Alternative 1,* include language limiting the Board from making annual assessments for the student protection fund any time the balance in the fund exceeds $1,000,000.

3. Delete provision.

Alternative 3	PR
2003-05 REVENUE (Change to Bill)	- $60,300
2003-05 FUNDING (Change to Bill)	- $60,300

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