

Department of Legislative Services
2012 Session

FISCAL AND POLICY NOTE

House Bill 1297
Appropriations

(Delegate Howard, *et al.*)

Higher Education - Private Career Schools - Financial Guarantee Requirements

This bill limits the amount of a financial guarantee that a private career school may be required to provide in order to operate in the State. The amount is capped at the lesser of the maximum student tuition liability or \$300,000. The bill also specifies the form of financial guarantee required by a private career school.

Fiscal Summary

State Effect: The Maryland Higher Education Commission (MHEC) can handle any additional reassessments required due to the reduced financial guarantee with existing resources.

Local Effect: None.

Small Business Effect: Meaningful. Private career schools that are required by the Secretary of Higher Education to have a financial guarantee greater than the amount required under the bill will benefit from modest reductions in fees associated with paying for a letter of credit or purchasing insurance in the form of a bond; however, if a private career school with inadequate financial guarantees closes, all remaining private career schools may be assessed additional fees to restore the Guaranty Student Tuition Fund.

Analysis

Bill Summary: Private career schools that are seeking an initial certificate of approval may be required to maintain a financial guarantee for five years. The financial guarantee must be in the form of a performance bond or a letter of credit. The amount of the financial guarantee needs to be sufficient to protect 100% of the tuition liability of the maximum student enrollment of the school, up to a maximum of \$300,000. However, the

Secretary may determine that a lesser percentage is sufficient based on the financial condition of the school as reflected in an audited financial statement.

With certain exceptions, private career schools that have had a certificate of approval for more than five years may not be required to have a financial guarantee. The Secretary of Higher Education may require a private career school to maintain a financial guarantee if the Secretary determines that the school does not meet either of these criteria: (1) the U.S. Department of Education financial criteria required to participate in federal financial aid programs; or (2) a one-to-one ratio of liabilities to assets based on reviewed financial statements. If the Secretary determines that a financial guarantee is required, the guarantee must be (1) in the form of a performance bond or a letter of credit; and (2) in an amount that is sufficient to protect 30% of the tuition liability of enrolled students, up to a maximum of \$300,000. Private career schools that offer distance education programs must maintain a financial guarantee for each distance education program (1) in the form of a performance bond or a letter of credit; and (2) in an amount that is sufficient to protect 100% of the tuition liability of enrolled students, up to a maximum of \$300,000.

Current Law: Most postsecondary education institutions must obtain a certificate of approval from MHEC before they are allowed to operate in the State. However, certain institutions are exempt from obtaining a certificate of approval from MHEC. These institutions are either under charter from the General Assembly or religious institutions meeting certain qualifications. MHEC grants a certificate of approval exemption after an institution demonstrates it meets the requirements to qualify for an exemption.

MHEC may require *any* institution of postsecondary education that is required to obtain a certificate of approval to furnish a performance bond or other form of financial guarantee to the State. The institution is guaranteeing it will perform faithfully all agreements or contracts it makes with its students. The bond or guarantee has to be in the form and amount required by the Secretary of Higher Education.

The total liability of an entity insuring an institution may not exceed the amount of the bond or guarantee. If the total amount of claims filed exceeds the amount of the bond or guarantee, the insurer must pay the amount of the bond to the Secretary for distribution to the claimants.

MHEC may create and operate a guaranty fund for private career schools. The fund is to be used to reimburse any student at a private career school who is entitled to a refund of tuition and fees because the institution has failed to perform faithfully any agreement or contract with the student or failed to comply with certain rules. The fund can also be used for any other function related to the original purpose deemed appropriate by the Secretary of Higher Education.

Chapter 277 of 2011 requires each private career school and for-profit institutions that is required to obtain a certificate of approval to pay an annual fee into the fund. Except for-profit institutions in fiscal 2012 and 2013, MHEC determines the amount of the fee based on the probable amount of money needed for the fund for each fiscal year as specified in the Code of Maryland Regulations (COMAR). If the monies in the fund are insufficient to satisfy claims, the participating institutions may be reassessed. The institutions must pay the additional amount required. MHEC may not issue a certificate of approval to, and must revoke any certificate of approval previously issued to, an institution that fails to pay any annual fee or reassessment. MHEC must also deposit into the fund any penalty assessed against a private career school for failure to meet conditions or standards. MHEC may enforce the claim of any student to the extent of any actual or authorized reimbursement from the fund. Chapter 277 capped the annual fee charged to for-profit institutions at the lesser of 0.0025 of gross tuition or \$30,000. The provision terminates June 30, 2013.

The State Comptroller is responsible for maintaining the fund and may deposit the assets of the fund in any manner that is consistent with the purposes of the fund. All interest or other return on fund investment must be credited to the fund. MHEC, through the Attorney General, may enforce any claim.

Background: Private career schools offer the training needed in dozens of fields, ranging from electronic repair and computer operation to cosmetology and allied health. During the 2008-2009 academic year, approximately 29,100 students were enrolled in 174 private career schools throughout the State. At that time, the allied health schools had the largest percentage of students; approximately 10,200 students were enrolled at 37 schools. The average program completion rate for all private school career schools was 70%.

The Guaranty Student Tuition Fund is capped at \$1.0 million in COMAR. MHEC reports that the Guaranty Student Tuition Fund currently contains approximately \$500,000, which MHEC reports took years to amass. This is the fund of last resort if a school closes owing tuition refunds to students. The first source of a refund is the school itself. The next is the school's financial guarantee, if the school had one. MHEC advises that about 77% of the private career schools (134 schools) are required to have a financial guarantee. Of the 134 private career schools required to maintain a financial guarantee: 88 are required to maintain a 100% financial guarantee; 21 are required to maintain a 50% financial guarantee; and 25 are required to maintain a 30% financial guarantee. Of the 88 private career schools required by the Secretary to maintain a 100% financial guarantee, 45 schools have been in operation for six or more years.

MHEC advises that the Secretary currently requires 18 private career schools to have a financial guarantee above \$300,000. These 18 schools have financial guarantees ranging from \$407,000 to \$6.2 million; however, many of these schools are not required to have a financial guarantee that covers 100% of liability. There are also additional schools with a tuition liability over \$300,000 that MHEC does not require to post a guarantee. If the financial guarantee were capped at \$300,000 and the Guaranty Student Tuition Fund stayed at \$500,000, then if any of these schools closed, the maximum student refund from these sources would be \$800,000. In that case, the Guaranty Student Tuition Fund would be completely depleted, and if another school closed, the maximum student refund would be \$300,000. MHEC reports that, for the last precipitously closed school, approximately \$1.2 million in refunds were made to students.

Students that received federal student financial aid from programs authorized under Title IV of the federal Higher Education Act of 1965 (as amended), which includes federal Unsubsidized Stafford loans, federal Subsidized Stafford loans, federal PLUS Loans, federal Perkins Loans, federal Pell Grants, and the federal Supplemental Educational Opportunity Grants, may have additional protections for their Title IV aid. However, these protections are not guaranteed, as the federal government only is required to consider refunding tuition and may choose to disqualify a program from loan discharge. This can occur for many reasons, one of which is if the school altered the program from its originally approved form or content.

State Fiscal Effect: If a private career school with inadequate financial guarantees closes and the additional student refunds required exceed funds in the Guaranty Student Tuition Fund, MHEC may be required to assess the remaining private career schools an additional fee to cover student tuition. As long as the reassessments are infrequent, MHEC can handle the extra workload with existing resources.

Small Business Effect: Private career schools that are required by the Secretary of Higher Education to have a financial guarantee greater than the amount required under the bill will benefit from some modest reductions in fees associated with paying for a letter of credit or purchasing insurance in the form of a performance bond.

However, if a private career school with inadequate financial guarantees closes, all remaining private career schools may be assessed additional fees to restore the Guaranty Student Tuition Fund. Of the 18 schools that are required to have financial guarantees greater than \$300,000, 15 are required to have a financial guarantees of \$500,000 or more, which is greater than the funds available in the Guaranty Student Tuition Fund, and 11 are required to have a financial guarantees of \$1.0 million or more, which is greater than the Guaranty Student Tuition Fund \$1.0 million cap.

MHEC advises that, in addition, the negative publicity from even one public career school closing with inadequate protection for student's tuition has the potential to negatively impact enrollments and goodwill for the entire industry.

Additional Information

Prior Introductions: HB 872 of 2010 was withdrawn before a hearing in the House Appropriations Committee. HB 1174 of 2009 received a hearing in the House Appropriations Committee, but no further action was taken.

Cross File: None.

Information Source(s): Maryland Higher Education Commission, Department of Legislative Services

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