

# For-Profit Model in Higher Education

**Vasudha Ramakrishna**

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## 1. ABSTRACT

It is important to distinguish the for-profit form from other private providers in education as an increasing number of countries identify it (although vaguely) and address the potential legal and ideological challenges of its entry. By understanding the dimensions of this form in countries where it is well established it would be easier to check for its de-facto existence in ambivalent countries like India. This paper examines how for-profit educational institutions function under different regulatory frameworks. It further explores the possibility of the entry of “for-profit” players in the Indian higher education sector and the optimum regulatory framework for the same. The paper seeks to cumulate international responses to a for-profit entry, the legitimacy issues, and definitional problems in order to recommend anticipatory policies for India. It intends to understand the challenges currently in setting up of higher education institutions regulatory, financial and otherwise and whether the profit motive alone will incentivize more players to invest. It also focuses on securing the rationale behind legislators’ resistance to this form and attempts to understand if the academia and market reflect the same reservations. Finally it attempts to study and import the successful private training and coaching classes’ model in India.

## 2. INTRODUCTION

Higher education had been a privilege in many countries<sup>1</sup>. The state did not guarantee it, or work as extensively towards providing it to everyone like in the case of primary education. Institutions of higher education (both public and private) were more selective and exclusive, with or without constitutional guarantees resulting from -geographic, income based and infrastructural constraints. As education levels increased across the spectrum, and there was growth in enrolment in the secondary level more students demanded and became eligible for pursuit of higher education. The job market also saw an increased demand for higher education. Governments then recognized that higher education satisfies the needs of the industry, by providing skilled labour, professionals and entrepreneurs. Shortages in state funding, its inability to meet demand and emergence of private interest in higher education has eventually seen the rise in the for-profit form.<sup>2</sup>

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1 Right to higher education is not constitutionally guaranteed in most countries. Countries like, Russia, Ukraine, France, Sweden, Italy, Libya, UAE, Cuba, Venezuela, Ecuador, Bolivia guarantee it while India, China, Australia, USA, Canada, Argentina and most African countries don't guarantee it. Article: Higher education- Creative destruction economist, 28th June.

2 Together with the economic value of education increasing and yet the funding for public higher education decreasing, for-profit colleges and universities emerged in 1970s (Tierney and Henshke)

There has been a rapid expansion of the for-profit form of higher education internationally in countries where it has legal status and also broader social legitimacy. As they develop in other countries, the question of for-profit players entering the otherwise strong, public dominated education set up has to be addressed. The reluctance of these countries to view education as a commercial rather than a charitable undertaking and the inconsistent international performance of for-profit educational institutions has rendered the transition or conversion tentative.

This paper examines the for-profit form of higher education, and the reasons behind its growth and increasing demand- by identifying its characteristics, the circumstances, and the regulatory framework surrounding its emergence. The model has been analysed with respect to the best practices of different countries, and the policy frameworks established. It is essential to study their significance in providing opportunities for different (marginalized) demographics and the regulations that enable catering to them freely, while maintaining certain standards. This paper attempts to add to the current literature on for-profit higher education by considering this in the Indian context. In order to visit the possibility of importing this model to India the paper sets the background of higher education in India, and its many challenges. India also has for-profit forms in the unregulated sector of coaching and training classes, the paper appraises its functioning to act as an efficiency test.

The paper thus seeks to answer the following questions:

1. Is it acceptable for the private sector to focus on commercially profitable programs with strong market demands in education?
2. How can the risks and benefits of the for-profit model in higher education be balanced by regulation?
3. Should the same quality assurance and regulatory frameworks apply to public and private providers?

The paper hypothesizes that the for-profit model could be a beneficial option under an optimal regulatory framework in India.

Due to the fairly recent emergence of the for-profit form as a licit provider of education in many countries the existing literature has focused on scaling it internationally and defining its main types. US patterns have largely been an illustration of the global behaviour of such forms, and have been studied extensively. This paper notes that the relative efficacy of for-profit institutions can only be optimized under particular regulatory frameworks and hence attempts to document the circumstances under which it has emerged in different countries and the successes and failures of the model under the different policy frameworks. While over regulation is stifling, a lack of effective audits could result in exploitative functioning. This paper does not argue for or against the case of for-profits, as a consensus on the relative merits and de-merits of for-profit higher education is difficult to arrive at given how empirical findings can be interpreted either ways (Maggio, Z). However it recognizes the inevitability of its entry due to the supply demand gap in Indian higher education and hence focuses on policy requirements in case of an entry.

### 3. METHODOLOGY

This paper largely employs secondary sources of data including articles, papers and books for studying the for-profit model in higher education. The paper uses the case study method to analyse models in different countries. There is some qualitative analysis of existing data on enrolment, dropout rates, expenditures, and teacher recruitment in for-profit institutions, however largely restricted to the US. For the Indian perspective opinions of investors in education, experts, academics and the policy makers have been considered. The successes and failures of private coaching classes which function as for-profits and are largely unregulated, have been included in the study, as these are largely aligned with international trends with respect to the functioning of for-profit models in education and could be indicative of the potential challenges in case of a for-profit entry in higher education.

### 4. FOR-PROFITS

#### 4.1 Defining Private forms:

While in most industries the “not-for –profit” system has separate legal, and functional provisions because private usually equals working with a profit motive, in the education sector in many countries this has not been the case. Education by default, and legal definition, has been a charitable endeavour. Hence all early private institutions traditionally were largely philanthropic, associated with a trust or religious institution (The Philippine private education providers are divided into sectarian and non-sectarian, as the first private forms were church affiliated), followed by individual family or business owned not-for-profit forms. Thus there is a lack of recognition, and acceptance of this model, which has contributed to its legitimacy issues, both legal and social. Most legal frameworks ignore this form, or have ambiguous laws, neither treating them as legal or illegal. Universally too there is no overarching definition to for-profits, and its legal status faces challenges in many countries.

While defining for-profit forms in higher education Tierney, Henschke, and Lechuka, identified definitional discrepancies on three considerations:

1. The distinction between for-profit and non-profit: Not for profit institutions also make profits, from two sources, (a) economic rents and (b) subsidies while the former does not increase college outputs the latter is used for funding other missions<sup>3</sup> of the college which may not directly accrue to the student profile but does increase the colleges’ output. Strictly speaking these revenues act as disguised profits as they are either not beneficial or not directly beneficial to the candidates education (Fried.H, 2011). Hence the essence of the distinction lies in the application of the profit earned and not the act of earning of profits. Many countries in

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<sup>3</sup> The author mentions over-compensation and featherbedding as forms of economic rents and other parts of the tuition, which are used to subsidize either research or other courses and programs.

central and Eastern Europe assume non-profit status of private higher education institutions despite their for-profit financing and operations model (Slantcheva, Levy, 2007).

2. The classification and identification of higher education: The UNESCO classifies six levels of education with higher education subsuming level 4-6.<sup>4</sup> Many countries consider degree granting institutions and universities to be higher educational institutions, which corresponds to level 5 and 6 of the OECD, this reduces the size of the for-profit sector. (Tierney, Henschke, and Lechuka,) in their book suggest that the plethora of for-profit forms exist in the tertiary sectors and hence a broader view of higher education would be an accurate indicator of their multiplicity and growth. Objective definitions of higher education are not easy to come by but it is broadly accepted that higher education fulfils four major functions (Cemmel, J):

“1- The development of new knowledge (the research function), 2- The training of highly qualified personnel (the teaching function), 3- The provision of services to society, 4- The ethical function, which implies social criticism”. So any institution fulfilling these categories should be considered in the purview of higher education.

3. The treatment-legal and otherwise of for- profit status: Due to the unregulated taxation policy, and the higher education institutions not being classified as non-profit organizations they have to pay taxes in Georgia (similar is the case with Russia)(Sharvashidze.G, 2005), (Tierney, Henschke, and Lechuka,).

In the absence of an internationally recognized definition an overarching definition of for-profits could be: ‘A private institution in which the individual(s) or agency in control receives compensation other than wages, rent, or other expenses for the assumption of risk’ is considered a for-profit institution (NCES, 2008,P.673). **Largely the definition of for-profit institutions is not dependent on whether they make profits, but on what they are able to do with the profit earned. For-profits can do whatever they want with the money they generate, they can sell shares in the company, pay dividends, invest in businesses, liquidate all assets or pursue completely unrelated activities (Kinser and Levy, 2005; Tierney, Hentschke, Lechuga, Pg 147).**

#### 4.2 Education a public good<sup>5</sup> (Grace, 1989):

Education has largely been state provided. The universality principle behind education automatically made it the state’s responsibility. The egalitarian principle that education should

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4 Level4-Post secondary, non-tertiary education

Level5-First stage of tertiary education (not leading directly to an advanced research qualification)

Level6-Second stage of tertiary education (leading to an advanced research qualification)

5 The concept of public goods is important in analysing the role of the government in allocating resources and providing them. Public goods are defined by two characteristics: 1) Non-excludability: It is not possible to exclude non-payers from consuming the good.2) Non-rivalry in consumption: Additional people consuming the good do not diminish the benefit to others.

be available to all supports the claim that for this purpose education cannot be for-profit. The free education in certain countries encourages the feeling of entitlement amongst students to free education (for instance the Brazilian Constitution prohibits the collection of tuition fees at public institutions, slowly countries providing higher education for free has reduced)<sup>6</sup>. However the state does not have unlimited funds, at some point it has to limit the subsidised (often free) provision of education. Herein the driving principle of state funded and operated education-universal access; cannot be achieved. When there is a financial and resource crunch, scalability is largely affected. The education system then is forced to exclude certain parts of society (invariably the marginalised sections), and compromise on quality. Students will then be stuck in a trap in the absence of alternatives due to the state monopoly. The rationale behind state run education and what it finally achieves become antithetical. This merits the participation of multiple providers even in the education sector, akin to any other service sector. This blanket trajectory has been largely the case for private sector entry in different countries at different stages. Nevertheless the states role cannot be completely eliminated; it still proves to be important as a sponsor and regulator.

Education meets the criteria of being non-excludable and non-rivalrous, requisite characteristics of a public good (Cemmel. J). When it comes to higher education being a “public good”, the consensus around it is a little weak. Although it makes important contributions to the larger capacity building exercise of the society, the private benefits<sup>7</sup> of college education are marked. The argument then moves to whether higher education is a right or a privilege.

### 4.3 Expansion:

As the higher education sector expands, resulting from greater demand states have recognized the need to design strategies to accommodate newer forms of providers to supplement state education. John Fieldon (2008) in his paper identifies several reasons for countries deciding to undertake strategic planning in higher education, which coincides with the reasons for the entry of for-profit forms in higher education in those countries.

1. Countries in pursuit of a new vision resulting from a transformation from a socialist to a market economy: The Mongolian government embarked on liberalization and privatization in the higher education sector in 1990 when it transitioned from a socialist to a democratic model.

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<sup>6</sup> The list of such countries providing higher education for free has reduced to only a few countries (Brazil, Sri Lanka, Tanzania, and some European countries).

<sup>7</sup> OECD. Education at a glance, 2006-page 121, “Attaining higher levels of education can be viewed as an economic investment in which there are costs paid by the individual (including reductions in earnings while receiving education) that typically result in higher earnings over the individual’s lifetime. In this context, the investment to obtain a university level degree, when undertaken as part of initial education, can produce private annual returns as high as 22.6%, with all countries showing a rate of return above 8%.”

2. Countries undergoing a transformation process after the abolition of a divisive system: South Africa in an attempt to repudiate the alienation caused by higher education due to apartheid enlisted the introduction of international providers of higher education by encouraging cross-border efforts. This intent is clear from the clearly laid out objective: “to redress past inequalities and to transform the higher education system to serve a new social order, to meet pressing national needs and to respond to new realities and opportunities” (South Africa Department of Education 1997).
3. The pursuit of mass higher education and the recognition of state constraints, financial and infrastructural propel countries to consider non-state providers as important stakeholders.
4. Development visions of different countries for their growth give importance to the role of higher education.

The final two reasons form the causes of the development of the for-profit sector in most countries; with countries like Malaysia and Singapore having goals of becoming regional hubs the government facilitates capacity building exercises with private entry.

#### **4.4 Behaviour of for profits:**

1. For profits tend to specialize in the area of vocational forms of training, and offer courses with lower academic reputation targeting non-traditional students (Cowen. T, Papenfuss. S, 2009).
2. Structural changes in for-profit institutions are easier to bring about, because of the flexibility brought about by the profit incentive for mergers, exits and opening up of franchises as these decisions will be based on financial viability. This could potentially harm students if the changes are sudden as mobility between institutions in higher education may not be as flexible.
3. For-profit firms in an attempt to reduce costs may deliver inferior services, when they cannot be evaluated effectively like in the case of education (Hausmann, 1987). Sceptics have countered that for-profit schools have incentives to reduce costs and to innovate, leading to both higher quality and greater efficiency in education (Tironi, 2006; Hoxby, 2003).
4. Profits incentivize efficient decision-making, and cost effectiveness. These motivations are missing amongst not-for profits that would rather by creative accounting over-compensate themselves. (Glaeser and Schleifer, 2001).
5. Sometimes the motivations of for-profits and non-profits are reversed. Non-profits may also engage in profit making activities while, for-profit firms may wish to reinvest the proceeds back into the institution. Despite profit being allowed in the US there are many institutions that prefer to remain not for profit due to subsidies and tax exemptions, while others prefer to convert. (Weisbrod, 1998). Subsidies and tax



regulations majorly determine for-profit or not-for profit status, favourable tax laws and subsidies motivate for-profit status for example in the Philippines their prominence is attributed to relatively equal tax treatment for all educational institutions students (Cowen. T, Papenfuss. S, 2009).

James Tooley (1999) argues that the profit motive is highly beneficial for education as markets will self regulate to ensure high quality and cost-effectiveness. He has listed seven, virtues of the profit incentive. This paper discusses them to understand the role and influence of the profit incentive. :

- a) The desire for expansion: Successful educational institutions will have the desire to expand only with a strong motivation, like the profit incentive. Without the profit incentive investors are unlikely to expand in disadvantaged areas. This expansion has also lead to the employment of online education techniques by many universities, so as to increase access. In practice the expansionary tendencies have been largely representative of oligopolistic frameworks as a few successful institutions expand, and provide for a majority. For instance NIIT has no major competitors in the Indian market, and in the US about 62% of the revenue in for-profit education is accounted for by eight major companies (Mckowan). This works contradictory to the idea of the profit motive -more players and hence greater choice. The market then largely functions as a monopoly, as the existing giants create barriers to entry for new players. Higher education also departs from Tooley' s idea wherein there is a certain motivation for colleges to resist expansion to establish exclusivity (Mckowan). The value of the institution diminishes if it expands and becomes accessible to everyone.
- b) The Necessity for Quality Control: The market eliminates the requirement for any form of state control, for ensuring quality. As the institutions revenue largely depends on enrolment, it has to constantly deliver good quality to bring in more students, and retain existing ones. However there have been instances of dubious quality despite high demand due to a lack of alternatives resulting from financial or other barriers. Additionally many students lack the resources to corroborate claims of quality, hence institutions can afford to compromise.
- c) Brand names solve the information problem: The market is seen to exploit consumers when there is a lack of information. According to Tooley, proper branding can prevent this. The brand will be indicative of the quality, and thus students can make informed choices. This component does hold merit to a large extent as the brand value has characteristics of extreme polarity, negative reviews and experiences could easily reverse the case. Brand dependency however has many limitations. Brands have two

dimensions, perceived and real quality ascription. The brand name may not be completely indicative of quality as intensive marketing techniques are employed to win consumers. Hence it is in the best interest of institutions to maintain good quality to retain brand name. There will always be a gap between the actual and perceived quality, due to creative branding.

Tooley highlights the necessity of research and development among for-profits as a function of competition. He asserts that the models best practices are research based, and this gets replicated when the research is disseminated across the different units of the institution, and /or the market. Being embedded in a larger organization facilitates the flow of information (such as research on best practices) between the schools in a franchise (McMeekin, 2003).

- d) Proper rewards for and utilisation of teachers: For-Profits have performance and output related pay for teachers to optimise teacher performance. Their performance could be checked on the basis of test scores, absenteeism etc. This characteristic however may not have a high degree of influence on student learning because for-profits have highly standardised curriculums and teaching material, with set course designs leaving little room for teacher inputs and hence lower initiative for innovation directed toward improving student performance. Secondly this market largely employs part-time faculty, and teacher mobility is high. While this has its advantages, it reduces the influence of performance-based pay on teacher efficiency.
- e) Attracting investment and cost effectiveness: The inelastic nature of demand for higher education and its not for profit functioning leaves little incentive for institutions to be cost-effective and check rising tuition costs. For profit institutions on the contrary need to keep a check on this to increase revenues and finally profits. It is important to note however that the lower tuition they offer is a function of the lack of additional facilities they have to offer as compared to traditional institutions and the other cost reduction practices they employ. For-profits efficiently use fixed capital by increasing the size of batches or having multiple batches for the same course in the same facility in shifts as seen in the unregulated tuition classes in India, which may have adverse effects on quality.
- f) Concern for student destinations: Tooley argues that the profit incentive will ensure that institutions provide students with employment or at least skills necessary for subsequent employment. This is the reason for for-profits largely providing vocation oriented courses, based on the needs of the industry. In India too for-profits have proliferated in the fields of vocational and technical education, and placements are an

important driver of enrolment in these institutions. However critics argue that student destinations can not be limited to employment and for profits due to their narrow curricular focus do not offer much else.

## 5.CASE STUDY-AREAS

### 5.1 Scale

For-profits represent the fastest-growing sector worldwide (Altbach, P. Levy, D. 2005). Many countries do not legally permit for-profit higher education institutions (e.g., Poland, Portugal, Russia, Tanzania, Uruguay) or at least are ambiguous as to whether for-profit institutions can be legally recognized. Other countries permit for-profits only in non-university sectors like Chile (Kinser and Levy, 2005) and India. The United States has the most well established forms of for-profits, and sets the precedents for global trends as also is the chief campaigner and initiator of cross border initiatives. Africa despite not traditionally having private higher education has seen for-profit models in practice; even in the absence of legal status post the 1990's. South Africa explicitly recognizes this form and is aligned largely with international trends. The for-profit sector has been an important component of the rapidly expanding private sector in Asia. In Latin America, Brazil and Peru recognize for-profit higher education and Chile allows it only in non-university institutions.

### 5.2 Matrix

#### 1.USA:

**The United States has had a long history of private sector involvement. The 19<sup>th</sup> century saw the for- profit form emerging as an important provider in the higher education sphere with the expansion of for-profit business schools across America (Kinser, K. 2006).**

#### **Growth and Scale:**

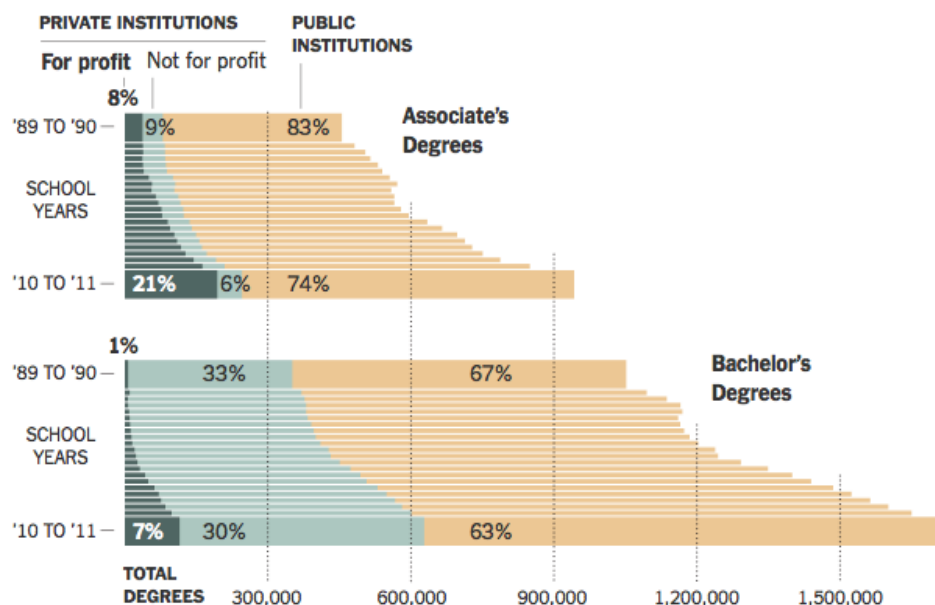
**From 2000 to 2012, total enrolment at for-profit institutions increased by 235 % (Douglass, 2012) and for-profit institutions now enrol 12% of all college students in the country (Lynch, Engle, and Cruz, 2010).**

#### **Courses Offered:**

**Well- defined courses of a short duration, which are highly job oriented. (David Deming, Claudia Goldin, and Lawrence Katz)**

**For-profit schools offer doctorates but also non-degree courses, and they run programs on healthcare, business, and computers to cosmetology, massage, and dog grooming. The for-profit sector offers almost no general education and liberal arts programs**

**COLLEGE DEGREES AWARDED, BY INSTITUTION TYPE**



Source: National Center for Education Statistics  
 Percentages may not add to 100, because of rounding.

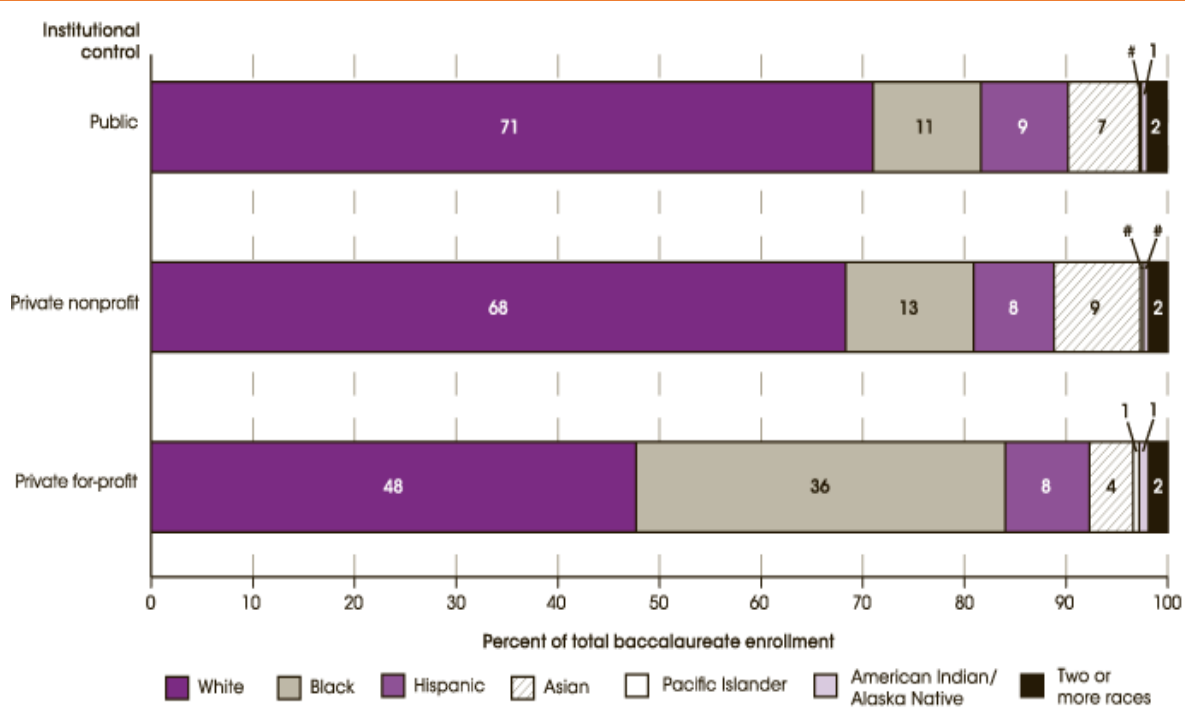
The chart shows that for-profits have seen higher growth in associate degrees, which are the equivalent of the first two years in a four-year undergraduate program.

**FIGURE 1 - ENROLLMENT RATES IN THE USA**

**Enrolment rates, dropout and default rates:**

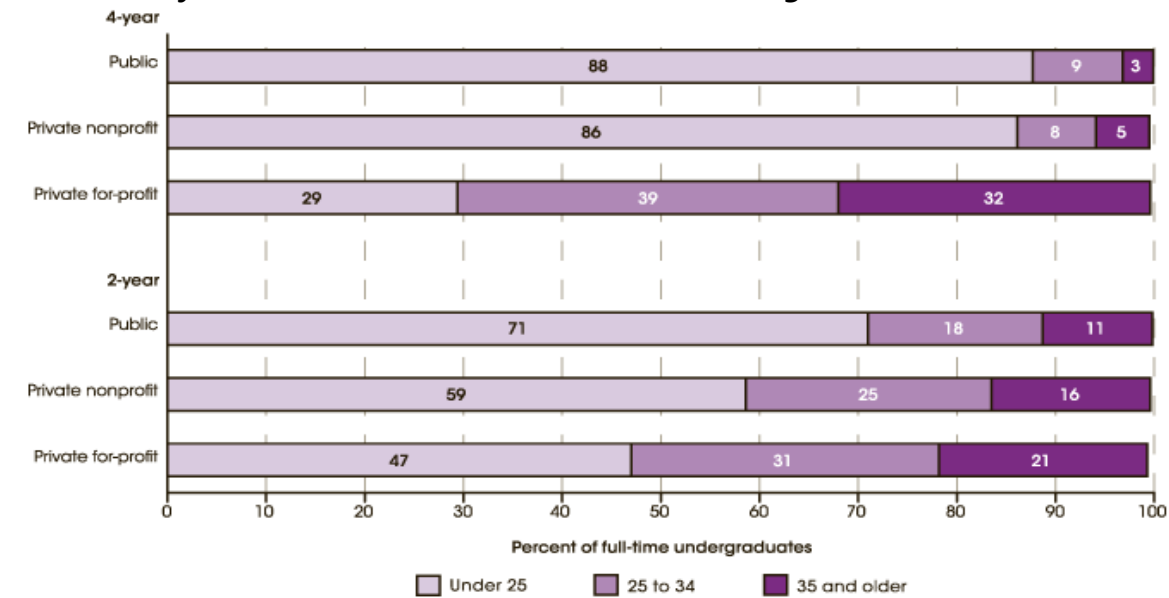
For-profit students are disproportionately dependent on federal financial aid. They have a higher likelihood of defaulting due to the high dropout rates. "They account for 47% of the defaults." (Deming, David J., Claudia Goldin, and Lawrence F. Katz. 2012).

**Student demographics:** For-Profits enrol a larger number of non-traditional students and high-risk candidates. They are almost always non-selective, but sometimes require secondary school completion, as financial aid is contingent upon a high school degree (Wildavsky B, Kelly A, Carey K .PG 186,).



**FIGURE 2 - ENROLLMENT DISTRIBUTION BASED ON RACE IN USA, SOURCE: NCES**

- 1. Minority Communities: For-profits “disproportionately serve older students, women, African- Americans, Hispanics, and those with low incomes.”(Deming, David J., Claudia Goldin, and Lawrence F. Katz. 2012.).**
- 2. Do not meet minimum college requirements: many are not high school graduates.**
- 3. Many candidates work full time while enrolled and attend part time courses.**
- 4. Many candidates are older than the traditional age criteria of 18-24.**



**FIGURE 2 - ENROLLMENT DISTRIBUTION BASED ON AGE IN USA**

- 5. Largely funded by federal student aid. Dependent students in the lowest income quartile.**
- 6. No parental support, who are married, or are single parents**

Good Practices: (Wildavsky B, Kelly A, Carey K).

1. The courses at for-profits are highly structured, and fixed. This ensures better quality control and standardisation. Although there is lower flexibility after enrolment, the pre-enrolment conditions are quick, and easy.
2. The courses are highly career oriented, and 'overall education' is secondary. In order to expedite entry into the job market, 80% of for-profit courses are full-time.
3. Client centred: For-profits offer many student centric services including identification of literacy and mathematic deficiencies for quick remedial for entering students. For instance the University of Phoenix has a tracking mechanisms where teachers diagnose problems of students both academic and otherwise and alert the concerned redressal bodies. This is in sharp contrast to traditional colleges where students are expected to self-diagnose.
4. Innovative techniques: Make customized tutorials, work samples, guides and study aids. For instance Phoenix makes two writing support services available, write point and tutor review, which review grammar and give detailed feedback on academic writing respectively. Many for-profits also employ online teaching for distance learning students.

Potential Problems:

1. Mergers, acquisitions and capacity building is faster in the for-profit market, although this is a good trait it has scope of dissolving institutions, this uncertainty and transience poses a major risk of displacing students.
2. This sector is far more prone to exploiting vulnerable students, as they are largely dependent on federal aid. Many firms employ intensive marketing techniques, as a product building exercise, students lacking resources to corroborate the facts may become subjects of dubious quality.
3. The regulation of debt default rates, and gainful employment for eligibility of title4 aid-which also require schools to meet accreditation and licensing standards and publicly disclose information about cost, debt, and program effectiveness. The institutions must stick to the caps and keep loan default rates under 30% in order to continue receiving federal financial aid. A lot of programs would become ineligible, and the demographic dependent on these colleges may be denied access to education.

**Brazil:**

The proliferation of business oriented for-profit institutes emerged in the 1970's, an addition to the pre-existing church run and other non-profit institutions (Eunice R. Durham). The major private sector expansion took place between 1995 and 2005, where in 2004 the market was worth 4 billion USD, with an expected growth rate of 10 billion USD. (Institute for higher education policy, 2009).

#### Growth and Scale:

An increase in demand for higher education accompanied by the government's goal to increase enrolment propelled reforms in the Education act, which eased restrictions and simplified accreditation and certification processes. 89% of the higher education sector was private with 19% of them being church run or philanthropic, and the remaining being largely commercial or profit oriented in 2007. (IHEP, 2009)

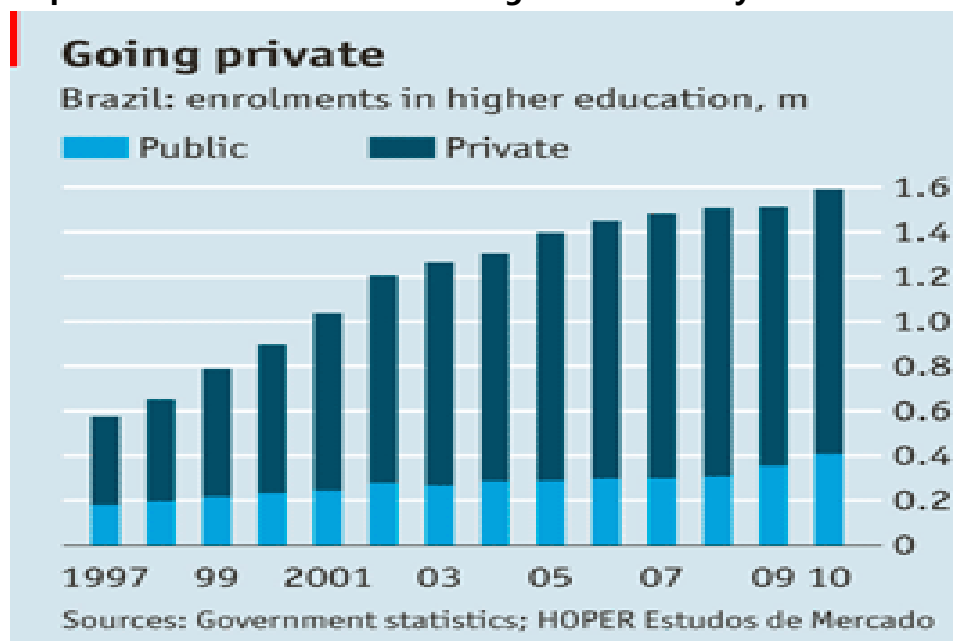
	PUBLIC SECTOR	PRIVATE SECTOR
INSTITUTIONS	11.3%	89.0%
UNDERGRADUATE ENROLLMENT	25.9%	74.1%
GRADUATE ENROLLMENT	82.0%	18.0%
FULL-TIME FACULTY	70.4%	29.6%
FACULTY WITH DOCTORATE	63.0%	37.0%

SOURCE: MINISTRY OF EDUCATION, NATIONAL INSTITUTE OF EDUCATIONAL STUDIES AND RESEARCH (INEP), CENSO DO ENSINO SUPERIOR (BRASÍLIA: MINISTÉRIO DA EDUCAÇÃO, 2007).

The above table shows the teacher recruitment strategies of for-profits who employ fewer doctorates and have a higher percentage of part-time faculty.

### Enrolment:

Brazil's for-profits enrolled over two million students in 2010 – 43% of the private sector and 32% of the overall higher education system (Salto D, 2014). By 2000, just a year after full legal approval to allow for-profit higher education, the sub-sector already enrolled 18% of the private sectors and 12% of the higher education system's students.



Consistent with major tendencies in private higher education globally, the for-profit sub-sector accumulates its largest share of enrolments in the fields of social science, business and law (51%), education (17%) and health and social welfare (15%).

FIGURE 4-ENROLLMENT DISTRIBUTION IN BRAZIL, SOURCE: ECONOMIST

### Good practices:

#### 1.The paradox of private players functioning like public institutions:

Similar to the American aid default situation, Brazilian private institutions faced large financial challenges with students not paying debts, and federal regulation dictating course completion guarantees to these students by the institutions. However the final degree granting took place only after the final settlement of the loans (Institute for higher education policy, 2009).

2.Checks on quality are maintained on the private sector by stipulations for periodic accreditation. The state expects private colleges to seek authorization from the Ministry of Education to create and organize courses and to set enrolment numbers. All private institutions must be re-accredited every three years after an evaluation process.



Potential Problems:

**1. Around 95 % of the for-profits are non-university institutions, the policy environment has ensured that these institutions are more non selective while the state universities are more selective to ensure greater access. The state universities have entrance exams, which limit the access of low-income students to these institutions, and hence most of them enrol in tuition funded private institutions and do not avail the free, superior quality public education. The low quality of private institutions has forced the government to increase regulation over them (IHEP,2009).**

**2. "Although the Education Act recognizes the existence of teaching-oriented institutions, it applies the same faculty standards to all institutions, without differentiating between the goals and organization of different institution types." (Institute for higher education policy, 2009).**

**3. The state has introduced minimum educational qualifications of teachers: 30 % of the faculty must hold doctoral degrees, and 20 % must work under full-time academic contracts. The for-profit sector largely appoints part time teachers and faculty; these stipulations would increase costs and in turn tuition. This high tuition directly affects access of marginalized communities who frequent these institutions.**

**4. Private donations are rare in Brazil and thus limit the funding sources of private institutions (including for-profits).**

#### **Mongolia:**

**The government started a systematic privatization program to counter budget constraints and to ease transition into a market economy. The Government privatization program of the social sector aimed to reduce the states role in higher education. Treading cautiously the government embarked on a process of contractual management of the privatization process of select universities. This contracting out of management of institutions to private players has increased the accountability of institutions.**

**Potential Problems (IHEP, 2009)**

**1. Private institutions bear the burden of high taxes imposed by the government, including**

income taxes.

2. The government does not have the ability to properly evaluate and monitor the performance of privatized institutions. Monitoring and evaluation guidelines for the privatization process are generally lacking. Institutional accreditation is a voluntary process, due to which few private institutions accredited.

3. The government has left the regulation of the sector to the market completely with minimal intervention.

**Malaysia:**

“At the time of Independence in 1957, opportunities for higher education in Malaysia were limited, as there were no public universities in the country”. Private higher education institutes, were present as tutorial centres for transnational programs that were geared toward selected skills and professional qualifications (Tham, 2010). These institutes continued to grow post independence particularly, due to the shift from a government-led to a private sector-led form of development in the country. In the mid-1980s the domestic liberalization in manufacturing and service sectors, including education further fostered the growth of this sector. The government gave permission for twinning arrangements between local private educational establishments and international universities (Sivalingam undated).

1. In Malaysia, the term “higher education” refers to all post-secondary education that leads to the award of certificates, diplomas, and degrees. Hence these institutes are a major part of the higher education industry.
2. The growth of this sector has been largely in encouragement of cross border and international programs. The government reduced certain regulation for these institutes like removing the necessity to instruct in Malay.

## 6. INDIAN HIGHER EDUCATION

### 6.1 Structure

India has the largest higher education system in the world by the number of institutions (Joshi. K.M, Ahir K. V). With around 700 universities, which can be categorised into state, private, central, deemed and universities of national importance; and about 35000 colleges (UGC, 2013). It ranks third in terms of enrolments with about 17 million students (UGC, 2012). The break-up of number of HEIs in the country shows that the share of state universities is the highest (44%) followed by private universities (22%), deemed universities (18%), institutes of national

importance (10%) and central universities (6%), (UGC, 2013). 73% Colleges are privately managed; 58% Private unaided and 15% Private aided (Deloitte, 2013).

The private sector can be divided into the regulated and the unregulated segments based on whether they come under the purview of an educational regulatory body and if they can run as for-profit entities.

1.Regulated Sector: The regulated sector consists of (i) those universities that are affiliated with the University Grants Commission, which ensures certain standards, and requirements as well as funding for affiliated institutions and prescribes requirements for prospective affiliates. (ii) AICTE (All India Council for Technical Education) which maintains standards for technical institutions, and other professional bodies like the Bar Council of India, which ensure the same for professional institutions. These institutions can exist as a trust, society or a section 25 company and run as not for profit entities.

2. Unregulated Sector: This sector includes all those institutes, carrying out activities not included in the formal education system that either provide services like content providing, vocational training institutes and constitute the coaching and training institutes for entrance tests, languages etc. which are registered public or private companies, who can make profits and distribute them (PWC report).

### **6.3 Finance:**

Higher education occupies a low priority in public expenditures. Its share of GNP was nearly 1 % during the 1970s, just 0.35% in the mid-1990s before increasing modestly to 0.6 by the end of the decade as reported in an article by Mathew, P M 2013 Spend More on Higher Education. Public spending on education is largely diverted to primary and secondary education, which has caused a crowding out of the higher education sector. In the tenth five year plan it was stated that, "Since budget resources are limited, and such resources as are available, need to be allocated to expanding primary education, it is important to recognize that the universities must make greater efforts to supplement resources from the government." Higher education sees a higher percentage of private spending predominantly in training and providing a variety of services to students and educational institutions, due to no restrictions on profit making and distribution (PWC Report). The government of India like many other countries is reducing responsibility of higher education by limiting subsidies (Srivastava, Amarnath, 2002), augmenting tuition fees and encouraging private sector participation. According to a web article by Misha Sharma " How is Higher Education Financed In India?" The reduction in public expenditure has led to tuition fee hikes, with rising self-financing institutions, which charge tuition fees on full cost- recovery basis. This arises from a lack of alternative sources of funding. For instance, alumni contributions are an important source of financing for not for profits in the United States and Canada where there is a culture of regular giving by alumni, and it has been estimated that the total of U.S. private college endowments amounts to \$222 billion (Filedon J, 2008), this has been either very low (seen amongst the IIT'S) or non-existent in the Indian

scenario. Private individuals did heavily fund public education in India however this has seen a decline, from private philanthropy being as high as seventeen % in 1950 to less than two % (Kapur B, Mehta P, 2004). Additionally the not for profit clause in education discourages many investors from entering the sector.

## 6.4 Legitimacy

### Legal

In India the setting up of and/or running of an educational institution has not been included under article 19(1)(g) of the constitution, hence it cannot be regarded as “trade” or “commerce”. The judiciary has not been successful in defining the role of private institutions, and has been unable to balance the commercial and charitable nature of private institutions. While it ruled that education is not a business, and cannot generate wealth there was a review of this in the TMA Pai case in 1992 when the court ruled, “reasonable surplus to meet the expansion and augmentation of facilities does not amount to profiteering.”

**Table 2: Legal Precedents.** (Loomba G; Kapur B, Mehta P, 2004).

1. St Stephens vs University of Delhi, 1992	Court supported state regulation in admissions and tuition to ensure no profiteering
2. Unni Krishnan v. State of Andhra Pradesh (AIR 1993 SC 2178)	Upheld the autonomy of self-financing institutions in decisions of fees and admission within a state determined cap. However maintained that education was not a trade or commerce.
3. Aditanar Educational Institution v. Addl. CIT (224 ITR 310)	If after meeting the expenditure, a surplus resulted incidentally from an activity lawfully carried on by an education centre; such an institution would not cease to be one that existed solely for educational purposes since the underlying object was not to make profit.
4. TMA Pai Foundation v. State of Karnataka, (2002) 8	Reversal of private sector

SCC 481	autonomy with upholding of charitable nature of higher education.
5. Islamic Academy of Education v. State of Karnataka,(2003)6S.C.C697,773	A 'reasonable surplus' resulting from higher fees than Governmental institutions was not profiteering as it was made for developmental purposes.
6. P.A. Inamdar v State of Maharashtra.	Granted autonomy to make legitimate surpluses with the condition of regulation of fees and surpluses to prevent unreasonable profits.

Kapur and Mehta in their 2004 paper describe an essential reluctance of the courts to accept private forms in higher education. They are suspicious of their entry but are grudgingly accepting their inevitability. The authors report that the court has been unable to define education as a service, (which include commercial transactions) hindering grievance redressal for students and have had merely a 'procedural' effect on checking quality. The growing private sector faces many legal challenges due to the lack of clarity in the law.

## State

The political class in India maintain that education should remain charitable, the following response to a Lok Sabha question summarises political (majority) view on this.

1. Question by Shri Laxman Tudu, answered on 8/5/2013 by Shashi Tharoor

"The Government has consistently held the view that education in India cannot be regarded as a commercial activity and all educational institutions have to be set up in the "not for profit" mode. The National Policy on Education, 1986 (as modified in 1992), encourages non-governmental and voluntary efforts in Education, while preventing the establishment of institutions, which intend to commercialize Education. The Policy envisages that in the interest of maintaining standards and for several other valid reasons, the commercialization of technical and professional education will be curbed."<sup>8</sup>

<sup>8</sup> His complete response: An alternative system will be devised to involve private and voluntary efforts in Education, in conformity with accepted norms and goals. The Government has taken several initiatives to curb the commercialization of education. The Section 13 of the Right of Children to Free and Compulsory Education (RTE) Act, 2009 clearly prohibits the collection of any capitation fee. As regards the higher educational institutions, a legislative proposal namely "The Prohibition of Unfair Practices in Technical Educational Institutions, Medical Educational Institutions and Universities Bill, 2010" has already been introduced in Parliament.

The final draft of the 12th five-year Plan however suggested a revisiting of the not for profit status of education. This ran into opposition from the human resource development ministry. The paper suggested this in light of the target of achieving a 30% gross enrolment ratio by 2022, the supply demand gap and lack of alternative financial resources for private players to raise money. This recommendation was not carried forward, but sparked a political debate on this possibility.

### *Regulation*

“The education system remains suspended between over-regulation by the state on the one hand, and a discretionary privatization that is unable to mobilize private capital in productive ways. The result is a sub-optimal structuring of higher education. Instead of being part of a comprehensive program of education reform, private initiatives remain hostage to the discretionary actions of the state (Kapur and Mehta, 2004).” Private enterprise has attempted to find ways around the highly restrictive regulations such as the government stipulating high standards of input mainly infrastructure and controlling teacher salaries. This has only given rise to nepotism and crony capitalism further marginalising the genuine players in education.

### *Taxation and not for profit status:*

As part of the not-for profit condition on non-public educational institutions, these can be set up by trusts, societies, and section 25 Companies<sup>9</sup>. Each of these are governed by different regulatory bodies, tax laws and acts.

**Tax Exemptions:** The Income Tax Act, 1961, governs tax exemption of not-for-profit entities. Religious or charitable Organizations may qualify for tax-exempt status if certain conditions are met. The government permits corporate houses to set up higher educational institutions by floating a separate not-for-profit entity under Section 25 of the Companies Act 1956. They therefore run on a two-tiered system, where the building and land are in the name of the private company, while the service is offered by the trust. However, in both the structures non-profit or society and trust, profits cannot be taken out of the institution and have to be reinvested. Institutions registered under the Act have to use their profits, if any, in promoting the institutions. The Act also prohibits the payment of any dividend to its members. The association may enjoy all the privileges of charitable trusts, but are scrutinised by the Income-Tax Department and not Charity Commissioner, unlike limited companies.

## Market

Education is a difficult business to build scale in; because (i) the absence of clear profit making structures makes it difficult to raise capital and (ii) the local costs outweigh the common costs in the case of multiple institutes. There is hardly any venture capital investment that has gone to setting up schools in India. According to a research report published in January 2009 by IDFC SSKI, only \$180 million of private equity investment has taken place in the formal education sector. Despite the high regulation it makes for an attractive sector because of: greater demand than supply, high barriers to entry, tuition hikes, high visibility of revenue, and it working with a negative working capital. The simplest way to raise money is through equity, but no private investor wants to invest money in a not-for-profit trust. This is why the entrepreneurs getting into the business have created two legal structures. A trust that runs the school and books all the expenses, and a company that owns the land, building, management and technology and leases it to the trust for a fee.

### *Private Coaching Classes in India:*

Coaching and tuition centres form a part of the unregulated sector in India. Since they are not part of the formal education system “these companies are subject to all other relevant laws of the land like income tax, shops/establishment polices, labour laws, company laws etc.” (PWC Report). Private coaching institutes, which offer additional training for entrance exams and don’t offer a degree, do not come under the purview of the UGC or the Union HRD ministry. They make high profits, which can be distributed. These institutions are seen as poachers who employ intensive advertisement tactics, and mislead poor students who do not crosscheck their credentials. These students often borrow money to enrol, and might end up securing unsuccessful results. “The coaching centres do not follow any uniform management system. Many institutes are registered as profit-making private companies and several are unregistered and they run as unregulated business.” Basant Kumar Mohanrt, Govt wants to keep hands off coaching cells, The Telegraph, March 18,2014).

As many as 83 per cent of India’s high school are enrolled for tuitions at these coaching centres, according to a 2012 report by the Asian Development Bank (ADB). The coaching sector was estimated to be worth over \$6.4 billion in 2008, according to the report.

Table 3: Trends aligned with for-profit models (newspaper articles, check references)	
1.Intensive advertisement strategies	Advertising performance by means of ranks, and marks obtained to attract students are employed. Some issue false and misleading advertisements, using the names and

	photographs of successful students without their permission.
2.Reason for emergence	The inability of the Indian schooling system to keep up with the numbers and meet the specific needs of different demographics.
3. Narrow curricular focus	Competitive entrances for professional courses, specific skill training and language courses.
4. Student Demographic	Every student attends these coaching classes because of the universality of entrances but many of the training institutes cater to weaker students who are not well adjusted in the mainstream education sector.
5. Short duration of courses	Entrance exam orientation accounts for the short duration.
6.Financing	Tuition dependent, many large ones like NIIT raise equity as public limited companies.
7.Innovative teaching methods	Employ online teaching, publish notes, guides etc.
8.Mergers and acquisitions	Examples: Educomp Solutions Ltd acquired Vidyamandir Classes in 2010; Triumphant Institute of Management Education Pvt. Ltd (TIME) took a majority stake in Veta, an English language training chain in south India. CL Educate in 2011 took over G.K. Publications, a Noida-based publisher of competitive exam books. Before that it had acquired Arun Roy Classes, an IIT test-prep chain in Maharashtra, and Law School Tutorial in north India.



## 7. ANTICIPATORY POLICY RECOMMENDATIONS

Higher education in India faces challenges of: 1) Low Quality, and a weak signalling effect to the job market<sup>10</sup>, 2) Low Research output, 3) Low access to higher education. There is no consistent evidence to suggest a link between profit and improved outcomes and better quality. As seen in the international experiences it actually raises issues of dubious quality, and/or lower quality than public institutions. Studies also prove that for-profits undertake lower research because they have fewer incentives to invest in it. However the profit incentive does help in ensuring greater access, given that the entry of more players solves the supply demand gap that the state is unable to fill, as well as the fact that these institutions internationally have been seen to cater to marginalised and non traditional sections. The similarities between the circumstances under which other countries have transitioned into for profit forms, and India's current situation are indicative of an inevitable profit entry, to meet the demand for higher education. This makes it necessary to understand the failures and successes of this form, resulting from different degrees of regulation in order to suggest measures in the event of the entry of this form in higher education.

Given the international precedents exclusive reliance on either market or state initiatives will not result in efficiency; a system incorporating both aspects would be ideal. Additionally

1. Regulation: Stringent, standardised regulations could be constraining for the smooth functioning of for-profit forms. Certain circumstances may have better outcomes under market mechanisms and natural agreements between the players. For-profit forms are very responsive and adapt to the changes in demand, regulation should not come in the way of this flexibility. This does not disqualify the need for effective regulation to ensure better quality as for-profit firms in an attempt to reduce costs may deliver inferior services, if they cannot be evaluated effectively like in the case of education.

a) **Accreditation and Evaluation:** Accreditation should be made mandatory for all institutions to keep checks on quality and protect the students. Information directories with the list of accredited institutes should be made public, and counselling centres could be charged with transmitting this information. Institutions would be incentivised to seek accreditation if students are more aware. There are multiple models for accreditation based on:

**Agency:** The Netherlands demonstrates the efficacy of autonomous and independent agencies in the monitoring and evaluation process. In Brazil, a collaborative effort by a professional association, the government, and higher education institutions successfully reformed the curriculum to better align with the job market. Hence a **non-state**

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<sup>10</sup> The primary function of a university degree is to provide a minimum signalling effect to the job market. In India the uncertain quality of higher education institutions fails to satisfy this function (Kapur. D, Mehta. P.2004).

specialised agency with representatives from all the stakeholders could be a viable option. The other option could be a model of state control based on an agreed contract between the state and each institution. "Such contracts will take the particular history and plans of the institution into account and will set out an expectation of the outcomes that the university will achieve. These contracts are becoming more focused on performance and results rather than inputs to the system such as student numbers. In Austria, for example, 20 % of the state funding is related to indicators of results agreed in performance contracts (Fieldon, J. 2008)."

**Standards:** Accreditation standards should differentiate between the goals of the institution; the infrastructural norms and other inputs should be aligned with the goals of the institution and the demographic. Since these institutions provide disproportionately to the marginalised sections issues of quality emerge. To retain student enrolment they may dilute the syllabus, rendering all the students mediocre. On the other hand conventional mainstream quality standards may become counter-productive and further exclude these students. Thus standards need to be ensured after due consideration to student background. In the Netherlands model of having different requirements for institutions with different purposes, universities can develop different measures of quality (IHEP, 2009). This differs from the uniform standardization to the effect that it is more inclusive and offers greater choice. This can also be seen in the private coaching industry where a plethora of centres provide training with different approaches and the performance requirements for the recognised marginalised are different (separate cut offs, less stringent pre eligibility criteria.) in competitive examinations.

b) **Protection of students:** The common issue of dubious quality and exploitation of marginalised students by means of misleading advertisements because of their lack of resources to corroborate facts could be solved by the government investing in **informing choice**. Information channels could be more formalised like web portals and independent counselling centres which educational institutions cannot manipulate. Additionally norms requiring **advertisements** to be supported with **auditable** evidence should be introduced, with external auditing agencies checking credibility. Courses should be required to have **pre-eligibility criteria**, to prevent students from enrolling to courses they cannot successfully complete or benefit from. Due to mergers, acquisitions and other structural changes being common amongst for-profits audits should be made to ensure that there are provisions for the students to complete their courses in case of such scenarios.

2. Funding: Since for-profits are highly tuition dependent, there is a possibility of inflating tuition in the absence of alternative resources. The government could make **alternative resources** available by diversifying funding, tax rebates, and exemptions for donors. For-profit forms would be eligible to raise capital in the financial markets through bonds; there could be credit agencies, which scrutinise the financial stability, which would incentivise institutes to earn favourable credit ratings and better terms in financial markets. Students at for-profits face more scrutiny for government financial aid, which is conditional on quality parameters in many countries to justify taxpayers' money in "commercial institutions". This hinders access and limits their options. Access to fiscal support can be need based initially and slowly be made conditional on performance to ensure accountability, and lower misuse. Merit based scholarships would incentivise both students and institutions to deliver.
3. Ownership: While transitioning India could begin by leasing out to for-profits, services and other ancillary functions in existing state universities to solve the prestige problem (college decisions are made based on the prestige of the institution, which may be lower for newer for profits). The management model in Mongolia where state universities are leased out for a time period is a good example of joint ownership.
4. The roles of the different stakeholders need to be well defined:
  - (a) There is a lack of a well-defined governance structure allowing for a proper distribution of responsibilities to all 'players' private and public. In the event of a for-profit entry a clear legislative framework specifying the roles of both sectors, their relationships and the areas of cooperation needs to be put in place to prevent confusions arising from ambiguity. If the higher education goals are distributed in a definite form the transition would be more focused and targeted. Definitions of the roles of the public sector at the various levels central, state and institutional as well as the roles of private 'for profits' and other stakeholders need to be designed.
  - (b) Due to the historic bias against profits as well as the novelty of such institutions, during its entry there would be a lack of trust. Hence trust building mechanisms need to be established. Channels between all the stakeholders that support dialogue and debate need to be invested in to ensure replication of best practices of all the existing models. Due to the vocation focus of for-profits, alliances could be forged between the industry and academia to support the employment needs of the students.

## 6. CONCLUSION

The introduction of the profit incentive could be a possible solution for the supply demand gap in higher education. With careful regulation it is possible to align commercial interests with the provision of education. Although this paper identifies a few regulatory methods and models for importing such a model there are multiple other factors, which need to be studied further to answer the India question effectively. The regulatory barriers to set up a college or a university need to be studied to understand whether profit alone, if at all will incentivise the entry of more players because “the non-profit status in India allows for tax exemption and makes it easier to launder money; it also gives access to free land without inviting public interest litigation (PIL)” (Kapur. D, Mehta. P.2004). Private will also needs to be gauged - how ready is the private sector in India to step in when public education is failing? It has been estimated that over Rs 10,000 crore of capital can be readily deployed towards new capacity creation provided more partners are welcomed in the national mission for education. There is evidence that for-profit education will inevitably play a huge role in countries with ambitious enrolment targets because of the speed of growth needed. However the ease of transition largely depends on the policy frameworks established and hence merits more attention in India.

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