

The Evolving Economic Structure of Higher Education

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INTRODUCTION

As an industry, higher education shows some striking anomalies. It is the only important industry in the United States that has been increasingly socialized in recent decades: the market share of public institutions grew, roughly, from 50 percent to 80 percent over the last half of the twentieth century.¹ Now the industry is suddenly heading down a very different path, with the market share of proprietary institutions—which was negligible thirty-five years ago—presently in excess of 10 percent.² Such contradictory developments bring into question the future economic organization of higher education and the forms of financing and regulation that might be appropriate to it. I'll offer here some speculation in that direction, focusing just on several of the main structural features of the industry and, of necessity, addressing them at a very general level. And I'll compare the evolution of higher education with the evolution of health care, seeking the reasons for both similarities and differences. The general conclusion I offer, perhaps unsurprising in the current political and economic climate, is that market forces are likely to play a much larger role in higher education in the future than they have in the past, and a larger role than they play in health care as well.

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¹ Compare US Census Bureau, *Statistical Abstract of the United States: 2004–2005* 169, online at <http://www.census.gov/prod/2004pubs/04statab/educ.pdf> (visited Oct 25, 2011), with US Census Bureau, *Statistical Abstract of the United States: 1953* 125, online at <http://www2.census.gov/prod2/statcomp/documents/1953-02.pdf> (visited Oct 25, 2011).

² See Kelly Field, *For-Profit Colleges Win Major Concessions in Final 'Gainful Employment' Rule*, *Chron Higher Ed* (June 2, 2011), online at <http://chronicle.com/article/For-Profit-Colleges-Win-Major/127744/> (visited Oct 25, 2011).

I. WHAT KIND OF A GOOD IS HIGHER EDUCATION?

It is often said—particularly in support of public subsidies—that higher education is a public good that benefits society as a whole.³ This seems a difficult conclusion to support, however. The overwhelming bulk of the returns to an education surely accrue to the individual who receives it, whether we look at its consumption-good aspects (such as learning for its own pleasures, socializing, or playing sports) or its production-good aspects (such as acquiring skills and contacts that will increase one’s expected earning power). While there are surely some external benefits when an individual gets a good education, the ratio of social to private benefits is arguably not much different than when an individual builds a house or buys a truck.

There is another respect, however, in which education—and higher education in particular—is rather different from most ordinary goods and services. It is—particularly at the higher end of the market—an “associative good,” in the sense that the value that a customer derives from patronizing a given producer is highly dependent upon the personal qualities of the producer’s other customers.⁴ The attraction of attending Harvard College, for example, derives not just—or perhaps even principally—from the quality of the teaching that Harvard offers but also in important measure from the intelligence, motivation, prior education, athletic ability, family, and social connections of Harvard’s other students. In substantial part, Harvard is selling its students to each other.

Markets for associative goods behave differently from other markets. For one thing, they tend to be selective with regard to their customers and to stratify, with the highest-quality tranche of customers patronizing one producer, the second-highest-quality tranche patronizing a second producer, and so on down the scale of quality.⁵ For another, producers of associative goods have an incentive to be smaller in scale than they would be absent the associative character of their goods, and to respond to increased demand by increasing the minimum quality they require of their customers rather than increasing the quantity they produce.⁶

³ See, for example, Jonathan D. Glater, *The Other Big Test: Why Congress Should Allow College Students to Borrow More through Federal Aid Programs*, 14 NYU J Leg & Pub Pol 11, 13 (2011).

⁴ See Henry Hansmann, *The Ownership of Enterprise* 185–94 (Belknap 1996).

⁵ See Henry Hansmann, *A Theory of Status Organizations*, 2 J L, Econ, & Org 119, 120, 122–23, 129 (1986).

⁶ See Hansmann, *The Ownership of Enterprise* at 185–90 (cited in note 4). See also Hansmann, 2 J L, Econ, & Org at 120, 123–25, 129 (cited in note 5).

II. FINANCING AND OWNERSHIP

Whether pursued as an aid to consumption or to production, higher education requires a substantial investment at the beginning of one's adult life, in the form of both direct expense and forgone earnings, while the returns from that investment are likely to be spread out over many subsequent decades. Students who don't come from wealthy families therefore need third-party financing to cover the initial cost. But it is difficult for students to bond themselves credibly to repay educational loans, since human capital provides poor security. Higher education is also an investment with much higher personal risk than social risk, since its return to any particular individual is hard to predict. For both these reasons, unsubsidized loans obtained on the private market are commonly insufficient to finance an efficient level of higher education. Much of the evolution in the institutions providing American higher education since the colonial days can be seen as an effort to arrange other sources of financing.⁷

A. Supply-Side Private Donations

Many private colleges and universities were, of course, founded or sustained in their early years by gifts from otherwise unrelated benefactors, such as the eponymous Harvard and Yale. Philanthropic contributions from third parties such as these have continued, but today are substantially overshadowed by donations from the institutions' own graduates, which are frequently an important source of revenue.⁸

Why do graduates give to their alma mater—rather than, for example, giving to other colleges and universities that might have greater need for the funds? From an economic point of view, the arrangement has much of the character of an implicit loan program. Colleges charge many or all of their students less than the full cost of their education, with the understanding that the tuition discount represents, in effect, a loan from the college that the student is expected to repay by making donations proportionate to their subsequent financial fortune in life. This arrangement has important efficiencies, not only in supplying credit where it would otherwise be unavailable but also in providing an important element of risk sharing.

⁷ See generally Daniel A. Wren, *American Business Philanthropy and Higher Education in the Nineteenth Century*, 57 *Bus Hist Rev* 321 (1983).

⁸ See James Monks, *Patterns of Giving to One's Alma Mater among Young Graduates from Selective Institutions*, 22 *Econ Educ Rev* 121, 121 (2003).

A norms-based implicit loan program of this sort works quite effectively for many well-established elite institutions such as Harvard, Yale, and Princeton. But this form of financing is clearly inadequate for newer or less prestigious institutions, which frequently lack a large cadre of grateful graduates. Efforts to make such contingent loan programs explicitly contractual rather than merely implicit, which were tried out with high expectations several decades ago, have collapsed owing to adverse selection.⁹

Whether private donations come from third-party benefactors or from an institution's own graduates, any private college or university that relies upon them must, as a practical matter, be organized as a nonprofit entity. The nondistribution constraint that characterizes a nonprofit provides an important degree of assurance to donors that the benefit of their contributions will be passed through to the institution's students, rather than simply being appropriated by those who control the organization. This surely goes far in explaining the large role historically played by nonprofit institutions in higher education in the United States.¹⁰

B. Supply-Side Governmental Subsidies

As the demand for higher education has expanded, private philanthropy has become increasingly inadequate as a solution to the problem of financing a college education, and it has been even less successful in financing graduate education in the arts and sciences. The result has been an increasing resort to government as a source of financing.¹¹

Historically, much of that financing has been on the supply side, as state and local governments have built large systems of government-owned-and-operated institutions of higher education, ranging from local community colleges to major research universities, and have then charged local citizens low or no tuition to enroll. From the first Morrill Act of 1862,¹² a significant component

⁹ See Alan B. Kruger and William G. Bowen, *Income-Contingent College Loans*, 7 J Econ Persp 193, 195–96 (1993); Marc Nerlove, *Some Problems in the Use of Income-Contingent Loans for the Finance of Higher Education*, 83 J Polit Econ 157, 165, 180 (1975). Yale's Tuition Postponement Option, in effect from 1972 to 1978, was the most prominent effort. See *Still Paying after All These Years*, 62 Yale Alumni Mag (Feb 1999), online at http://www.yalealumnimagazine.com/issues/99_02/l_v.html (visited Oct 25, 2011) (discussing the drawbacks of Yale's Tuition Postponement Option plan, which required students to make tuition payments based on their income after graduation).

¹⁰ See Henry B. Hansmann, *The Role of Nonprofit Enterprise*, 89 Yale L J 835, 859–62 (1980).

¹¹ See US Census Bureau, *Statistical Abstract of the United States: 2012* 186, online at <http://www.census.gov/compendia/statab/2012edition.html> (visited Oct 25, 2011).

¹² Pub L No 37-108, 12 Stat 503 (1862), codified at 7 USC § 301 et seq.

of the funds for these institutions has come from the federal government, but the bulk of the governmental funds has been provided by the states.¹³ While the land-grant colleges of the late nineteenth century substantially expanded the role of public education, an even larger expansion came a century later, following the Second World War. As Table 1 shows, in 1949 roughly half of all postsecondary students were enrolled in private nonprofit institutions, and the other half in public institutions—a ratio that had remained essentially constant at least since 1920.¹⁴ Twenty-five years later, in 1974, that ratio had changed dramatically, with public institutions holding nearly four times the market share of nonprofit institutions¹⁵—a ratio between the two ownership forms that has since remained roughly constant.¹⁶

This great expansion of public colleges and universities in the third quarter of the twentieth century was a response to rapidly growing demand. As Table 1 shows, total enrollment in institutions of higher education was more than four times larger in 1974 than it was in 1949, spurred by large numbers of returning soldiers, the postwar baby boom, greater prosperity, demand for a more highly skilled workforce, and substantial increases in government funding. Rather than seeking to induce the nonprofit sector to expand sufficiently to accommodate most or all of the expanded enrollment, state and local governments simply built and operated the necessary facilities themselves, expanding old campuses and establishing new ones.¹⁷

This was probably the only feasible route. Nonprofit institutions were unlikely to meet the rapidly swelling demand regardless of the kind or quantity of subsidies offered them. Nonprofit institutions in general exhibit sluggish supply response, expanding only slowly when demand increases.¹⁸ One reason is that nonprofits generally

¹³ See Wren, 57 *Bus Hist Rev* at 321–23 (cited in note 7).

¹⁴ See Henry Hansmann, *The Changing Roles of Public, Private, and Nonprofit Enterprise in Education, Health Care, and Other Human Services*, in Victor R. Fuchs, ed., *Individual and Social Responsibility: Child Care, Education, Medical Care, and Long-Term Care in America* 245, 267 table 9.2 (Chicago 1996).

¹⁵ National Center for Education Statistics, *Total Fall Enrollment in Degree-Granting Institutions, by Attendance Status, Sex of Student, and Control of Institution: Selected Years, 1947 through 2008* (2009), online at http://nces.ed.gov/programs/digest/d09/tables/dt09_189.asp (visited Oct 20, 2011).

¹⁶ *Id.*

¹⁷ Alice M. Rivlin and June O'Neill, *Growth and Change in Higher Education*, 30 *Proc Acad Pol Sci* 66, 69 (1970).

¹⁸ See Henry Hansmann, *The Effect of Tax Exemption and Other Factors on the Market Share of Nonprofit versus For-Profit Firms*, 40 *Natl Tax J* 71, 77–78 (1987); Bruce Steinwald and Duncan Neuhauser, *The Role of the Proprietary Hospital*, 35 *L & Contemp Probs* 817, 829–30 (1970). See also Henry Hansmann, Daniel Kessler, and Mark McClellan, *Ownership*

have poor access to capital, being barred from equity financing and limited in their ability to borrow—particularly in the start-up phase.¹⁹ Moreover, established nonprofits commonly react to increased demand by increasing the quality rather than the quantity of the services they offer—a phenomenon that’s easy to observe among elite colleges. One reason for this, presumably, is that personal pride and satisfaction from providing high-quality services are important incentives for nonprofit managers.²⁰ Another likely reason—at least among the more selective colleges—is that the associative aspect of higher education pushes in the same direction.²¹

A third alternative for meeting the large postwar increase in demand for higher education was to induce entry by proprietary institutions. Only tentative efforts in this direction were made in the first twenty-five years after the Second World War.²² More recently, however, subsidizing expansion of for-profit higher education has become a major component of federal aid programs.²³ The evolution of demand-side subsidies, particularly from the federal government, is at the center of these developments.

C. Demand-Side Governmental Subsidies

The GI Bill of 1944²⁴ gave veterans extensive demand-side subsidies for higher education and made those subsidies tenable at proprietary as well as nonprofit and governmental schools.²⁵ The succeeding five years saw the creation of more than five thousand proprietary schools, many of which were thought to be vastly overcharging for the education they offered.²⁶ Congress responded

Form and Trapped Capital in the Hospital Industry, in Edward L. Glaeser, ed, *The Governance of Not-for-Profit Organizations* 45, 57–68 (Chicago 2003) (providing empirical evidence of the relative slowness of nonprofits in exiting an industry with falling demand). See also generally Darius Lakdawalla and Tomas Philipson, *Nonprofit Production and Competition* (NBER Working Paper No 6377, Jan 1998), online at <http://www.nber.org/papers/w6377.pdf> (visited Oct 26, 2011) (listing other factors limiting expansion of nonprofit firms).

¹⁹ See Hansmann, 89 *Yale L J* at 877 (cited in note 10).

²⁰ See *id.* See also Edward L. Glaeser and Andrei Shleifer, *Not-for-Profit Entrepreneurs*, 81 *J Pub Econ* 99, 107–08 (2001) (asserting that reputational concerns help to increase quality of nonprofit services).

²¹ See Hansmann, 2 *J L, Econ, & Org* at 119–20 (cited in note 5).

²² See Nicholas R. Johnson, *Phoenix Rising: Default Rates at Proprietary Institutions of Higher Education and What Can Be Done to Reduce Them*, 40 *J L & Educ* 225, 228–29 (2011).

²³ See *id.* at 231–38.

²⁴ Servicemen’s Readjustment Act of 1944 (GI Bill), Pub L No 78-346, 58 Stat 284.

²⁵ GI Bill § 400, 58 Stat at 290.

²⁶ Daniel Golden, *Veterans Failing Shows Hazards of For-Profit Schools in GI Bill*, Bloomberg (Sept 23, 2010), online at <http://www.bloomberg.com/news/2010-09-23/veterans-failing-to-learn-show-hazards-of-for-profit-schools-under-gi-bill.html> (visited Oct 26, 2011).

with a provision in the Veterans' Readjustment Assistance Act of 1952²⁷ requiring that proprietary schools receiving that federally subsidized tuition have a student body in which at least 15 percent of the students were paying tuition without the aid of the GI Bill, hence exposing the schools to a limited market test.²⁸ Congress went even further when it passed the Higher Education Act of 1965,²⁹ Title IV of which became and has remained the principal source of federal student aid for higher education.³⁰ That Act expressly confined financial assistance to students who attended public or nonprofit institutions,³¹ cutting out proprietary institutions completely.

Perhaps owing to changes in national politics, demand-side subsidies were again made widely available to proprietary schools with the enactment of the 1972 amendments³² to the Higher Education Act of 1965, which eliminated the restriction of Title IV aid to students at governmental and nonprofit schools.³³ Subsequent amendments to the Act in 1979³⁴ and 1986³⁵ further broadened access to for-profit schools while also increasing the amount of loan funds available.

The result was a repetition of the experience with the first GI Bill. The grants and the subsidized and guaranteed loan funds provided under this legislation fueled a rapid rise in the market share of proprietary schools that began in the 1970s.³⁶ As Table 1 shows, that market share doubled between 1974 and 1979, and by 2009 was thirty times larger than it had been in 1974. Indeed, by 2009, private institutions were serving one-third of all students enrolled in private (nongovernmental) institutions of higher education. Many of these institutions are large. As of 2010, fourteen of the companies

²⁷ Pub L No 82-550, 66 Stat 663, codified at 38 USC § 991 et seq, repealed by the Veterans' Readjustment Benefits Act of 1966, Pub L No 89-358, 80 Stat 12.

²⁸ Veterans' Readjustment Assistance Act of 1952 § 226, 66 Stat at 667. See also generally Golden, *Veterans Failing Shows Hazards of For-Profit Schools in GI Bill* (cited in note 26); Robert Shireman, *For Guidance on For-Profit Colleges, Look to the GI Bill* (Campus Progress May 11, 2011), online at http://www.campusprogress.org/articles/for_guidance_on_for-profit_colleges_look_to_the_gi_bill/ (visited Oct 26, 2011).

²⁹ Pub L No 89-329, 79 Stat 1219, codified as amended in various sections of Title 20.

³⁰ William S. Howard, *The Student Loan Crisis and the Race to Princeton Law School*, 7 *J L, Econ, & Policy* 485, 495 (2011).

³¹ Higher Education Act of 1965 § 435(a)(4), 79 Stat at 1247-48, 20 USC § 1001(a)(4).

³² Education Amendments of 1972, Pub L No 92-318, 86 Stat 235, codified as amended in various sections of Title 20.

³³ Education Amendments of 1972 § 131, 20 USC § 1002(a)(1)(A).

³⁴ Higher Education Technical Amendments of 1979, Pub L No 96-49, 93 Stat 351, amending various sections of Title 20.

³⁵ Higher Education Amendments of 1986, Pub L No 99-498, 100 Stat 1268, codified at 20 USC § 1001 et seq.

³⁶ See William Beaver, *For-Profit Higher Education: A Social and Historical Analysis*, 25 *Sociological Viewpoints* 53, 56-57 (Fall 2009).

providing postsecondary education were publicly traded, and the largest of them, the University of Phoenix, enrolled 470,000 students.³⁷

These proprietary institutions are extraordinarily dependent upon federal subsidies. As of 2010, for example, the University of Phoenix obtained 88 percent of its revenue from Title IV funds,³⁸ and this figure seems typical for the proprietary higher education sector in general.³⁹ In turn, proprietary institutions account for a disproportionate share of Title IV funds: 19 percent as of 2009, as compared with 48 percent for public schools and 33 percent for private nonprofits.⁴⁰

The rapid growth in proprietary schools over recent decades has seemingly been accompanied by an equally rapid growth in exploitation of both consumers and the federal government, echoing the experience under the first GI Bill. The typical form of abuse is to induce individuals to enroll, against their interest, in courses of instruction that are unsuited for them, that they are unlikely to complete, that teach skills for which there is no market, or that are simply overpriced. Schools induce these individuals to pay for this unproductive education not just with federal grants but also with loans that are provided or guaranteed by the federal government, but for which the students will remain personally liable. (Indeed, current law generally prevents these loans from being discharged even in bankruptcy.⁴¹) Congress and the Department of Education have sought to control this abusive behavior in recent years through a sequence of regulatory measures, with only modest results to date.⁴² We will return below to the prospects for ultimate success in this regard.

³⁷ Compare Apollo Group, Inc, *2010 Annual Report* 14 (2010), online at <http://www.apollogrp.edu/Annual-Reports/Apollo2010AR.pdf> (visited Oct 26, 2011), with University of California, *Statistical Summary of Students and Staff* 1–27 (2009), online at <http://www.ucop.edu/ucophome/uwnews/stat/statsum/fall2009/statsumm2009.pdf> (visited Oct 26, 2011).

³⁸ Apollo Group, Inc, *Form 10-K for the Fiscal Year Ended August 31, 2010* 35, online at <http://www.sec.gov/Archives/edgar/data/929887/000095012310094652/p18193e10vk.htm#124> (visited Oct 26, 2011).

³⁹ For example, the proportion was 82 percent in 2010 for Kaplan Higher Education, a subsidiary of the Washington Post Company with ninety-seven thousand students enrolled. See Washington Post Company, *Form 10-K for the Fiscal Year Ended January 2, 2011* 1–2, online at <http://sec.gov/Archives/edgar/data/104889/000119312511053497/d10k.htm> (visited Oct 26, 2011).

⁴⁰ See Government Accountability Office, *Proprietary Schools: Stronger Department of Education Oversight Needed to Help Ensure Only Eligible Students Receive Federal Student Aid* 5 (Aug 2009), online at <http://www.gao.gov/new.items/d09600.pdf> (visited Oct 26, 2011).

⁴¹ See 11 USC § 523(a)(8).

⁴² Government Accountability Office, *Proprietary Schools* at 9, 22–28 (cited in note 40).

D. A Comparison to Health Care

The evolution of the American health care industry, and particularly the hospital sector, provides an instructive comparison to the development of higher education. The growing demand for hospital care after the Second World War was first met by supply-side subsidies, such as the federal Hill-Burton grants to public and nonprofit hospitals.⁴³ The implementation of Medicare and Medicaid in the mid-1960s altered that approach, providing extensive demand-side subsidies for hospital services that could be used at proprietary hospitals as well as at nonprofit and public hospitals. The result was the entry and rapid growth of proprietary hospitals, including publicly traded hospital chains. The market share of proprietary hospitals, which had remained constant at 6 percent from 1960 to 1971, doubled over the next 20 years to 12 percent in 1992.⁴⁴ This growth came entirely at the expense of the share held by government-owned hospitals, which declined from 31 percent in 1971 to 24 percent in 1992.⁴⁵ The proprietary hospitals that proliferated after 1965 did not, in general, present serious problems concerning quality of care or exploitation of patients. Although there were some scandals, they typically involved financial fraud directed at the governmental Medicare and Medicaid programs rather than provision of substandard care to patients, or systematic provision of expensive care for which there was no medical need.⁴⁶

What accounts for the relative success in expanding the hospital sector by encouraging the expansion of proprietary institutions through demand-side subsidies, while the same approach was accompanied by serious problems in higher education and, instead, public institutions have been relied upon for increasing the supply of higher education?

Medical doctors as of 1965 practiced almost universally as sole practitioners or in partnerships, and hence were essentially in business for themselves.⁴⁷ They were generally not employees of the

⁴³ See Department of Health and Human Services, *Hill-Burton Free and Reduced-Cost Health Care*, online at <http://www.hrsa.gov/getthehealthcare/affordable/hillburton/hillburton.pdf> (visited Oct 26, 2011).

⁴⁴ Hansmann, *Changing Roles* at 254 (cited in note 14).

⁴⁵ *Id.* at 256.

⁴⁶ While there is substantial evidence of excessive care in the sector in general, it seems to have been induced in large part by the threat of malpractice litigation and to have affected nonprofit as well as for-profit hospitals. See Office of Technology Assessment, US Congress, *Defensive Medicine and Medicine Malpractice*, OTA-H-602, 39–74 (GPO 1994). See also Daniel Kessler and Mark McClellan, *Do Doctors Practice Defensive Medicine?*, 111 Q J Econ 353, 356–58, 372–88 (1996) (explaining how tort reforms affect the practice of defensive medicine).

⁴⁷ Hansmann, *Changing Roles* at 257 (cited in note 14).

hospitals in which they had admitting privileges but rather billed their patients separately while at the same time exercising considerable control over the hospitals' management.⁴⁸ As a consequence, proprietary institutions were perfectly familiar to them, while at the same time the profession was overtly hostile to the socialization of medicine.⁴⁹ College and university professors of that era, in contrast, were nearly all employees of nonprofit or governmental institutions, with little experience—and much suspicion—of proprietary enterprise.

A related reason for the success of proprietary hospitals may be that, since medical doctors were not employees of the hospitals where they treated patients, they had an interest in maintaining the quality of those hospitals and were in a position to police effectively the services that the hospitals offered. The nonprofit or governmental form was not needed to blunt the institutions' incentives to behave opportunistically for their patients.

Yet another reason may be that hospital care is a more homogeneous service than is higher education, and hence is easier to monitor and regulate either publicly or privately. An appendectomy is performed more or less in the same way in all US hospitals, without major variation among institutions that treat the prosperous and the poor, the educated and the ignorant, the ambitious and the lazy. An introductory course in English literature, on the other hand, may take a very different shape for different types of students.

III. QUALITY ASSURANCE

The account of the evolution of higher education offered above raises two questions. First, is for-profit higher education just a hothouse flower, opportunistically taking advantage of poorly regulated public subsidies—and something that will largely disappear if and when meaningful consumer-protection regulation can be implemented? Second, even if there is a permanent place for a substantial for-profit sector in higher education, will that place always be at the bottom of the educational hierarchy, largely providing basic preparation for trades of limited sophistication? To answer either question, it's necessary to address the problem of quality assurance.

⁴⁸ See Mark Pauly and Michael Redisch, *The Not-for-Profit Hospital as a Physicians' Cooperative*, 63 *Am Econ Rev* 87, 87–88 (1973).

⁴⁹ See Kim Geiger and Tom Hamburger, *AMA Does 180 on Health Care*, *Chi Trib* 42 (Sept 13, 2009).

American higher education flourished for two hundred years without a meaningful system of governmental quality regulation. To be sure, beginning at the end of the nineteenth century, a private-sector form of quality assurance grew up in the form of the six regional accrediting associations for colleges and universities.⁵⁰ But these associations, which are controlled by the institutions that they accredit,⁵¹ have never succeeded in establishing—or even tried to establish—clear and objective ratings or even minimum standards for accreditation. Rather, they have traditionally seen their role as simply working with each individual institution to help it define and meet its own internal goals. It may be, however, that there is relatively little more that can be done. Widely applicable and objective standards for measuring the quality of education that any institution provides are difficult to devise without making them arbitrary and stifling.

Despite the lack of external policing, the overall quality of American higher education has been high by world standards, and until recently there have been remarkably few scandals involving the quality of education offered even by individual institutions. There seem to be two possible explanations for this: (1) institutional form and (2) competition.

A. Institutional Form

One reason why quality assurance has not been a major problem may be that, until recently, nearly all nongovernmental institutions of higher education were nonprofit. The nonprofit form dulls the incentives of managers to exploit their consumers, giving them instead an incentive to provide a level of quality higher than that which would maximize net revenue.⁵² If the quality of service offered by proprietary schools is too difficult for students or their parents to assess *ex ante* with much accuracy, then the sector may be poorly suited to profit-seeking firms, at least until some effective form of quality regulation can be established. If, moreover, effective forms of regulation can be established only for simple trade schools, and not for the elaborate forms of education now offered by the more

⁵⁰ See Mary Glenn Wiley and Mayer N. Zald, *The Growth and Transformation of Educational Accrediting Agencies: An Exploratory Study in Social Control of Institutions*, 41 *Sociology Educ* 36, 36–37 (1968); California Postsecondary Education Commission, *Accrediting Agencies*, online at <http://www.cpec.ca.gov/CollegeGuide/AccreditingAgencies.asp?Type=Regional> (visited Oct 26, 2011).

⁵¹ See Howard, 7 *J L, Econ, & Policy* at 505 (cited in note 30); William E. Troutt, *Regional Accreditation Evaluative Criteria and Quality Assurance*, 50 *J Higher Ed* 199, 199–203, 206–09 (1979).

⁵² See Glaeser and Shleifer, 81 *J Pub Econ* at 100–02 (cited in note 20).

selective institutions, then the latter institutions evidently must continue to be organized as either nonprofit or governmental entities.

B. Competition

With the exception of the military academies, the US government has never itself owned and operated institutions of higher education.⁵³ Rather, the governmental presence in administering education, while large, has been at the state and local level. While the politics behind this development are the same that produced a highly fragmented and apparently inefficient banking system for the better part of two centuries,⁵⁴ the consequences for higher education have evidently been salutary. Public as well as private colleges and universities have had to compete in a national market for both students and faculty. And, although those colleges and universities have, until recently, been almost exclusively either governmental or nonprofit, they have evidently responded well to the pressures of that competition. It is difficult to find any other reason to explain why American higher education is so strong by world standards while American primary and secondary education—commonly a local public monopoly—is so weak.

The constitutional powers of the individual states play an important role here. The courts have never found higher tuition for out-of-state students at state universities to be an impermissible burden on interstate commerce.⁵⁵ Consequently, state universities routinely discriminate in this fashion, and therefore have a strong incentive to attract students from other states. The European Union—regrettably, and perhaps tragically—seems not to have taken a lesson from this experience. The creation of a European common market for higher education held out the promise that interstate competition would overcome the deleterious effects of the centralized state control of higher education that has become characteristic of European nations, and that arguably accounts for the decline of European universities in the twentieth century after nearly a millennium of world dominance. But the promise of such

⁵³ See Department of State, *A Diverse Educational System*, online at <http://usinfo.org/enus/education/overview/ch6.html> (visited Oct 21, 2011).

⁵⁴ See Geoffrey P. Miller, *Interstate Banking in the Court*, 1985 Sup Ct Rev 179, 181–83, 208–25. See generally Eugene Nelson White, *The Political Economy of Banking Regulation 1864–1933*, 42 J Econ Hist 33 (1982).

⁵⁵ The Supreme Court has never explicitly ruled that charging higher tuition to out-of-state students at public educational institutions is consistent with the dormant Commerce Clause. Nonetheless, “[t]here are . . . strong indications that the Court would find no commerce clause problem if the question were squarely presented.” Dan T. Coenen, *State User Fees and the Dormant Commerce Clause*, 50 Vand L Rev 795, 807 n 60, 840–41 (1997).

competition has seemingly been scotched by EU regulations prohibiting public universities from admitting students from other EU member states on different terms than those offered in-state students.⁵⁶ The consequence is that the challenge to the United States for world superiority in higher education may well come from Asia rather than from Europe.

It remains to ask whether national (or international) competition will be sufficient to discipline for-profit institutions of higher education if and as they expand their share of the market. This is a question that perhaps needs to be addressed separately for the top end of the market (high-quality undergraduate and graduate education in the arts and sciences) and for the bottom end of the market (instruction in basic skills for specific trades).

It seems plausible that competition would be more than adequate to discipline for-profit institutions at the top end of the market, if there were any. Institutions at that level quickly develop national reputations, and there are many publications available to help develop and spread these reputations among potential consumers. If for-profit institutions were to seek to enter the top end of the education market, therefore, there is every reason to believe that market forces would quickly sort the wheat from the chaff. The question for elite higher education, instead, is whether proprietary institutions are for some reason incapable of creating the right incentives for producing quality equal to the level reached by prominent public and nonprofit colleges and universities. This is a question we will return to below.⁵⁷

It is less obvious that competition alone, absent regulation, can provide adequate discipline for proprietary schools at the lower end of the market for higher education, where they are now concentrated. Experience to date suggests that completion alone will not suffice.⁵⁸ But there is reason to be hopeful. For one thing, the problem has been largely driven by excessively easy credit subsidized by the federal government—offering a strong parallel, as many have noted, to the credit-driven housing bubble of the recent past and the

⁵⁶ See *Gravier v City of Liège*, Case 293/83, 1985 ECR 593, ¶ 26 (Court of First Instance); *Commission of the European Communities v Austria*, Case C-147/03, 2005 ECR I-5969, ¶ 75 (Second Chamber). But see *The Queen v London Borough of Ealing*, Case C-209/03, 2005 ECR I-2119, ¶¶ 56–57 (Grand Chamber).

⁵⁷ See Part IV.

⁵⁸ See, for example, Golden, *Veterans Failing Shows Hazards of For-Profit Schools in GI Bill* (cited in note 26); Beaver, 25 *Sociological Viewpoints* at 55–56 (cited in note 36).

opportunistic transactions it fostered.⁵⁹ One solution is to make proprietary institutions ineligible for participation in federal educational aid programs. But that would throw out the baby with the bathwater.

Direct regulation of the minimum acceptable quality of education that can be offered by an institution participating in federal student aid programs also does not seem a promising approach. To be sure, it is an approach that looks more feasible for the types of trade-focused education offered by most proprietary schools than for education at the top of the market. But directly measuring the quality of instruction is nonetheless an elusive task. The private-sector accrediting agencies, as we have noted, have not been very successful at it.⁶⁰ And the special agencies that have grown up to accredit for-profit schools are understandably no better.⁶¹

But direct regulation of quality may not be essential. The core problem presented by opportunistic proprietary schools seems not so much that they offer an education that is in itself of insufficiently high quality to be useful to anyone, but rather that it is sold to the wrong people, and at an excessively high price. In essence, the abusive schools are not offering their students too little education but rather too much education, or the wrong kind of education. And these are easier problems to solve through regulation. Current and proposed regulatory reforms in fact take this approach, restricting access to federal student aid for schools that attract little tuition beyond federal aid funds, or that have disproportionately large numbers of students who fail to complete their degrees, or fail to find employment following graduation, or fail to repay their loans.⁶²

There is a parallel here in the experience with proprietary hospital care. Though there have been a number of financial scandals involving for-profit hospitals, particularly with respect to abuse of

⁵⁹ See, for example, *Higher Education: The Latest Bubble?*, Economist Schumpeter Blog (Economist Apr 13, 2011), online at http://www.economist.com/blogs/schumpeter/2011/04/higher_education (visited Oct 21, 2011).

⁶⁰ See notes 50–51 and accompanying text.

⁶¹ See, for example, Kevin Kinser, ASHE Higher Education Report, *From Main Street to Wall Street: The Transformation of For-Profit Higher Education* 98–99, 106–08 (Jossey-Bass 2006).

⁶² See Department of Education, Program Integrity: Gainful Employment-Debt Measures, 76 Fed Reg 34386, 34413–18 (2011) (amending 34 CFR § 668); Department of Education, *Obama Administration Announces New Steps to Protect Students from Ineffective Career College Programs* (June 2, 2011), online at <http://www.ed.gov/news/press-releases/gainful-employment-regulations> (visited Oct 27, 2011); Johnson, 40 J L & Educ at 238–51 (cited in note 22).

public subsidies under Medicare and Medicaid,⁶³ scandals involving the quality of hospital care seem to be rare. The large proprietary hospital chains perhaps understand that a scandal involving poor-quality care in any part of their system could severely damage the reputation of the enterprise as a whole, cutting revenues badly, whereas defrauding a public insurance program does not pose a threat to anybody's life, including the lives of the individuals covered by the program. The regulatory response has been more careful audits of proprietary hospitals. More generally, empirical studies have had to look hard to find systematic differences in the quality of care offered by nonprofit and for-profit hospitals.⁶⁴ And the quality of instruction offered by an institution of higher education, it would seem, is no harder for consumers to evaluate than is the quality of the medical care offered by a hospital.

Ongoing changes in the lower end of the education market may also permit competition to discipline proprietary institutions more effectively in the future, with decreasing reliance on public regulation. The tendency toward consolidation of proprietary schools into a smaller number of large firms makes reputation more effective as a constraint on firm behavior. New information technologies, such as online learning, may further foster consolidation, both nationally and internationally.

However difficult it may be to assure reasonable quality and pricing in proprietary postsecondary education, there may be little choice but to undertake the task. The evidence suggests that public schools, such as community colleges, are insufficiently flexible to provide the variety and quantity of vocational and trade school programs, or the adjustment of those programs to the practical needs of students, that proprietary institutions can offer.⁶⁵ And nonprofit institutions, as we have noted,⁶⁶ tend to have a high-quality bias that causes them to refrain from serving the low end of the market in service industries. Thus, whether the service is nursing care, day care,

⁶³ See Dan Ackman, *Disaster of the Day: HCA*, *Forbes* (Dec 15, 2000), online at <http://www.forbes.com/2000/12/15/1215disaster.html> (visited Oct 21, 2011).

⁶⁴ See, for example, Catherine Plate, *The Differentiation between For-Profit and Nonprofit Hospitals: Another Look*, 12 *Rsrch Healthcare Fin Mgmt* 7 (2008). But see Pauline Vaillancourt Rosenau and Stephen H. Linder, *Two Decades of Research Comparing For-Profit and Nonprofit Health Provider Performance in the United States*, 84 *Soc Sci Q* 219, 220–29 (2003); Pervaiz Alam, Essam Elshafie, and David Jarjoura, *The Effect of Ownership Structure on Performance of Hospitals*, 12 *Acad of Acct* 37, 47 (2008).

⁶⁵ See Regina Deil-Amen, James E. Rosenbaum, and Ann E. Person, *Illusions of Opportunity? From College Access to Job Access at Two-Year Colleges*, in Gary Orfield, Patricia Marin, and Catherine L. Horn, eds, *Higher Education and the Color Line: College Access, Racial Equity, and Social Change* 107, 116–25 (Harvard 2005).

⁶⁶ See note 20 and accompanying text.

or primary and secondary education, nonprofit institutions are common in the top end of the market but generally do not provide the low quality but essential services that are all that the poor and disadvantaged can pay for.⁶⁷

In sum, there seems good reason to believe that proprietary institutions will continue to expand their role in the lower end of the market for postsecondary education, at least if appropriate regulation is adopted to enhance the effectiveness of competition (although the initial effect of such regulation may be to shrink the proprietary sector—perhaps radically—by squeezing out the more opportunistic of the current schools).

But can proprietary institutions also ultimately succeed at the higher end of the education market? We turn to that issue next.

IV. CHARACTERISTICS OF NONPROFIT AND PUBLIC INSTITUTIONS

We noted above that competition may well be an effective source of discipline for high-end proprietary schools.⁶⁸ But are there important characteristics of the best nonprofit and governmental colleges and universities that cannot be replicated by proprietary firms? In approaching the latter question, we'll focus on three central and related issues: research, academic tenure, and faculty self-governance.

A. Research

Faculties at major nonprofit and public universities are generally expected to engage in academic research as well as teaching. Might it be difficult for proprietary institutions to produce research of similar quantity and quality, given that research, unlike education, is commonly a public good?

Even if the answer to this question is no, this need not be a bar to an important role for proprietary institutions in higher-quality higher education. Many of the nation's best undergraduate colleges—such as Amherst, Smith, and Williams—provide no substantial amount of graduate education and have faculties that are principally focused on undergraduate teaching rather than research. It is with institutions such as these that proprietary schools might first be expected to compete.

⁶⁷ See, for example, Niccic L. McKay, *The Effect of Chain Ownership on Nursing Home Costs*, 26 *Health Servs Rsrch* 109, 109–10 (1991) (noting that nonprofit nursing homes serve disproportionately the high-quality high-cost end of the market).

⁶⁸ See Part III.B.

Moreover, proprietary institutions may well be able to undertake research as well as teaching. A large fraction of research in the sciences is funded by governmental or private grants⁶⁹ that presumably could be administered by proprietary as well as nonproprietary institutions. Many specialized proprietary research firms already get the bulk of their income from governmental research grants and contracts.⁷⁰ And some of the nation's largest university-affiliated hospitals, which undertake substantial research and teaching, are administered by for-profit hospital chains under contracts that at most leave the hospitals nonprofit in name (and tax status) only.⁷¹

B. Tenure

Lifetime tenure for faculty is one of the most striking features that distinguishes the internal organization of public and nonprofit institutions of higher education from typical investor-owned firms, whether in higher education or in industry in general.

Although the tenure system has roots at least as far back as Harvard's adoption in the 1820s of an "up or out" system for electing tutors to endowed professorships, it is largely a twentieth century phenomenon. The principal moving force behind its adoption was the American Association of University Professors (AAUP), formed as a guild of sorts in 1913,⁷² and the principal characteristics of the tenure system were established in agreements negotiated between the AAUP and the America Association of Colleges (a grouping of university presidents).⁷³ The second and stronger of these agreements, adopted in 1940, essentially followed the Harvard "up or out" model. The model embodied in this agreement spread rapidly; by 1970 it had been adopted by virtually every substantial institution of higher education in the country.⁷⁴

In recent decades, however, the tide has turned. From 1975 to 2009, the proportion of faculty on the tenure track in US colleges fell

⁶⁹ See Becky Oskin, *The Road Less Traveled*, *New Scientist* 54, 54 (August 27, 2011).

⁷⁰ See Congressional Budget Office, *Federal Support for Research and Development* (June 2007), online at <http://www.cbo.gov/ftpdocs/82xx/doc8221/06-18-Research.pdf> (visited Oct 31, 2011).

⁷¹ See John A. Kastor, *Selling Teaching Hospitals and Practice Plans: George Washington and Georgetown Universities* 1, 183–91 (Johns Hopkins 2008).

⁷² See Walter P. Metzger, *Academic Tenure in America: A Historical Essay*, in William R. Keast and John W. Macy Jr, eds, *Faculty Tenure: A Report and Recommendations by the Commission on Academic Tenure in Higher Education* 93, 135–36 (Jossey-Bass 1973).

⁷³ See *id.* at 148–56.

⁷⁴ See *id.* at 152–55.

by nearly half, from 57 to 30 percent.⁷⁵ The common alternative to a tenure track appointment is a contract for a term of one year or longer, either full-time or, increasingly, part-time.⁷⁶ Colleges and universities are making the shift from tenured to nontenured faculty in several ways. Some are keeping the tenure system for selected faculty but are hiring an increasing percentage of faculty off the tenure track; some are abolishing tenure for all future hires, while grandfathering faculty who already have tenure; and some new institutions are being founded without tenure from the beginning.⁷⁷ Proprietary schools generally do not grant tenure, while institutions at the top of the market—the elite schools and colleges—have been the slowest to move away from tenure.⁷⁸

What accounts for this dramatic rise and ebb in the tenure system during the latter half of the twentieth century, and what is likely to happen to tenure in the future? Changes in demand and supply of professorial talent may explain much of the recent past. The enormous postwar demand for faculty gave the profession substantial bargaining power, and it must have been tempting for university administrators to bid for faculty by offering employment benefits, such as tenure, many of whose costs would be incurred by the university only far in the future, while the benefits would be immediate. Since the early 1970s, however, the supply of new PhDs has substantially exceeded the demand for academic faculty,⁷⁹ and bargaining power has shifted. Yet these market shifts do not tell us clearly whether social welfare might be best served by retaining tenure in at least the upper ranges of the higher education market.

⁷⁵ Laura G. Knapp, Janice E. Kelley-Reid, and Scott A. Ginder, *Employees in Postsecondary Institutions, Fall 2009, and Salaries of Full-Time Instructional Staff, 2009–10* 3 (National Center for Education Statistics 2010), online at <http://nces.ed.gov/pubs2011/2011150.pdf> (visited Oct 31, 2011) (“Of the approximately 1.4 million full-time professionals reported to be employed at degree-granting institutions and administrative offices (excluding medical schools) . . . 21 percent [have] tenure, 9 percent [are] on tenure track.”); Robin Wilson, *Tenure, RIP: What the Vanishing Status Means for the Future of Education*, *Chron Higher Ed* (July 4, 2010), online at <http://chronicle.com/article/Tenure-RIP/66114/> (visited Oct 31, 2011).

⁷⁶ See Jack Stripling, *Most Presidents Prefer No Tenure for Majority of Faculty*, *Chron Higher Ed* A12 (May 15, 2011); Robin Wilson, *Contracts Replace the Tenure Track for a Growing Number of Professors*, *Chron Higher Ed* A12 (June 12, 1998).

⁷⁷ See Wilson, *Contracts Replace the Tenure Track*, *Chron Higher Ed* at A12 (cited in note 76); *Observations on Creating a New Paradigm for Undergraduate Education in Engineering, Hearings before the Secretary of Education’s Commission on the Future of Higher Education* *5–7 (Mar 20, 2006) (testimony of Richard K. Miller, founding president, Franklin W. Olin College of Engineering), online at <http://www2.ed.gov/about/bdscomm/list/hiedfuture/2nd-hearing/miller2.pdf> (visited Oct 31, 2011).

⁷⁸ See Stripling, *Most Presidents*, *Chron Higher Ed* at A12 (cited in note 76); Wilson, *Tenure, RIP*, *Chron Higher Ed* at A12 (cited in note 75).

⁷⁹ See *Supply-Side Academics*, 10 *Nature Neuroscience* 1337, 1337 (2007).

To approach that question, it makes sense to start with costs and benefits.

The conventional argument for tenure in higher education is that it provides the protection needed for faculty members to address controversial topics in both teaching and research.⁸⁰ As others have pointed out, however, this is not a particularly persuasive justification. Lifetime tenure is neither necessary nor sufficient to protect intellectual freedom in colleges and universities, including in particular the freedom to express socially or politically unpopular views.⁸¹ The strongest justification that has been offered for tenure, rather, is that it facilitates hiring competent faculty.⁸² Knowledge in academic disciplines has become so specialized and esoteric, it is argued, that the choice of whom to hire in a given field must be delegated to the school's current faculty who specialize in that field. If those faculty lack tenure, however, they may not choose the most qualified candidates for fear of hiring their own replacements.⁸³ Against this benefit must be set off the familiar disadvantages of extreme job security, including institutional rigidity, poor incentives for productivity, discouragement of institutional risk taking, and the paradoxical pressure on young untenured faculty not to offend their elder colleagues.

We can get some helpful perspective on the evolving trade-offs among these considerations by looking at large corporate law firms in the United States, which for the first three quarters of the twentieth century almost uniformly adhered to a rigid up-or-out system of employment, combined with an expectation that promotion to partner meant lifetime employment with the firm—precisely like academic tenure.⁸⁴ Since the legal market was reasonably competitive and the lawyers involved owned their own firms, there is every reason to believe that the long survival of this

⁸⁰ See Richard T. De George, *Academic Freedom and Tenure: Ethical Issues* 13–14 (Rowman & Littlefield 1997).

⁸¹ See Stephen J. Ceci, Wendy M. Williams, and Katrin Mueller-Johnson, *Is Tenure Justified? An Experimental Study of Faculty Beliefs about Tenure, Promotion, and Academic Freedom*, 29 *Behav & Brain Sci* 553, 567–68 (2006); Richard Posner, *Tenured Employment*, Becker-Posner Blog (Jan 15, 2006), online at <http://www.becker-posner-blog.com/2006/01/tenured-employment--posner.html> (visited Oct 31, 2011) (“If a university wishes to offer its faculty protection against political retaliation for unpopular views, it can do that by writing into the employment contract that politics is an impermissible ground for termination.”).

⁸² See H. Lorne Carmichael, *Incentives in Academics: Why Is There Tenure?*, 96 *J Pol Econ* 453, 454–63, 471 (1988).

⁸³ See *id.* at 454–63, 471. For other arguments, see Michael S. McPherson and Gordon C. Winston, *The Economics of Academic Tenure: A Relational Perspective*, in Matthew W. Finkin, ed., *The Case for Tenure* 99, 106–21 (Cornell 1996).

⁸⁴ See Mark Galanter and Thomas Palay, *Tournament of Lawyers: The Transformation of the Big Law Firm* 26–32 (Chicago 1991).

pattern of employment was a strong indication of its efficiency. And the principal purpose it served, arguably, was the same as in higher education: it provided the senior members of the firm with an incentive to hire the best young talent they could find, without worrying that they were thereby putting their own employment at risk.

But the tenure system in law firms began breaking down in the last quarter of the twentieth century. The principal reason seems to be that the market for corporate legal services shifted from being a market for law firms to a market for individual lawyers. As legal services became an increasing expense to corporations, those corporations created larger and more sophisticated in-house legal staffs.⁸⁵ At first those in-house lawyers used their expertise to hire different law firms for different types of legal problems rather than getting all their services from a single firm, as had previously been common.⁸⁶ Then they moved on to shopping for the services of individual lawyers who appeared specially qualified.⁸⁷ Those lawyers then came to have personal reputations apart from that of the firm with which they were affiliated. The result was that highly productive lawyers could and did insist on higher remuneration than their colleagues received, breaking up the lockstep pay schemes of the past and producing substantial lateral mobility across firms, as well as more frequent divisions and mergers of firms.⁸⁸ Retaining low-productivity partners became expensive, cutting into the revenues available to hire or retain more productive colleagues, and generating frictions among partners in allocating earnings. Partnership has, as a consequence, become something much less than a guarantee of lifetime employment, as partners still in midcareer are expelled from their firms.⁸⁹ At the same time, law firms are increasingly hiring new lawyers on a non-partner-track basis, with no guarantee of ongoing employment.

Arguably much the same thing is now happening in American colleges and universities. The quality of individual faculty members

⁸⁵ See Sung Hui Kim, *The Banality of Fraud: Re-situating the Inside Counsel as Gatekeeper*, 74 *Fordham L Rev* 983, 999 (2005).

⁸⁶ See Abram Chayes and Antonia H. Chayes, *Corporate Counsel and the Elite Law Firm*, 37 *Stan L Rev* 277, 289–99 (1985).

⁸⁷ See Ted Schneyer, *Reputational Bonding, Ethics Rules, and Law Firm Structure: The Economist as Storyteller*, 84 *Va L Rev* 1777, 1786–87 (1998).

⁸⁸ See Robert William Hillman, *Hillman on Lawyer Mobility: The Law and Ethics of Partner Withdrawals and Law Firm Breakups* 6–9 (Aspen 2d ed 1998).

⁸⁹ See Elizabeth Goldberg, *The Departed*, *Am Law* 144, 145 (May 2007) (discussing the restructuring of a variety of law firms, and noting that many top law firms are “unabashedly pursuing growth strategies that entail orchestrated exits of partners who are deemed to be underperformers”).

is becoming increasingly apparent to persons outside the individual's own faculty. An individual's scholarship can be evaluated not just by reading the publications and working papers that are now so easily available electronically, but also by the increasing capacity for objective comparative criteria such as citation counts. And the near ubiquity of student teaching evaluations now makes the quality of teaching much easier to assess from outside the teacher's own institution as well.

One consequence of these increasingly public reputations for individual teachers and scholars not just at the top, but throughout the academic hierarchy, is that it is less obvious that an institution must rely heavily on its own faculty to hire their new colleagues. This means that it is less important to grant them tenure. Moreover, the thicker market for academic reputation seems to be leading to much greater dispersion in faculty salaries, with superstars bringing in far more than their less conspicuous colleagues.⁹⁰ This means that, if a faculty decides to hire someone of great prominence or even great promise, they may be deciding to reduce the amount of funds available for their own salaries. Perhaps more seriously, it increases heterogeneity among members of a faculty with respect to their terms of employment. And, as I have argued at length elsewhere, strong homogeneity in this respect seems essential to effective self-governance.⁹¹ The more informationally efficient that the national—or, increasingly, international—market for individual faculty becomes, therefore, the less discretion we can expect to be delegated to university faculties to choose their own colleagues, and consequently the less need there will be for academic tenure.

C. Governance

For similar reasons, we can reasonably expect that faculty self-governance in all respects—not just with respect to hiring but also with respect to setting the curriculum and allocating teaching responsibilities and research opportunities among the faculty—will decline. When a faculty—or any group—must decide collectively to allocate benefits and burdens among themselves, it is difficult to settle on any rule other than equality. Hence, all members of a given university department are generally expected to do roughly the same amount of teaching and committee work regardless of their relative skills as scholars and as teachers. In general, then, the future is likely

⁹⁰ Linda A. Bell, *More Good News, So Why the Blues? The Annual Report on the Economic Status of the Profession, 1999–2000*, 86 *Academe* 11, 15–17 (March–April 2000).

⁹¹ This is a central theme of Hansmann, *The Ownership of Enterprise* (cited in note 4).

to bring greater centralization of authority within American universities, which means an administrative model much closer to that found in conventional proprietary firms.

V. A TOTALLY PROPRIETARY SECTOR?

Should we therefore expect that American higher education will eventually be populated entirely with for-profit firms? That seems unlikely. A more plausible scenario is that proprietary institutions will continue to increase their market share, but that public and private nonprofit institutions will continue to have a substantial presence. Proprietary firms may displace or acquire many of the less well-established nonprofit colleges, but the elite institutions will continue to thrive. Indeed, there is evidence that nonprofit firms, once established, can compete with proprietary firms in a variety of industrial settings. Nonprofit institutions, moreover, are slow to exit markets whether they are thriving or not.⁹² (Perhaps the huge endowments that some universities have accumulated, seemingly without a persuasive rationale,⁹³ will ultimately be spent to keep these institutions in business, for better or for worse, much beyond the time when they would otherwise become unsustainable.) State colleges and universities, meanwhile, will continue raising the tuition they charge until they are effectively offering the same terms as nonprofit and proprietary institutions, and will come increasingly to resemble private nonprofits—more like the University of Pennsylvania than the University of California.

CONCLUSION

In the early 1970s, it was reasonable to expect that the future would bring increasing socialization of both health care and higher education in the United States. In health care, it seemed likely that insurance covering both physician and hospital care would be largely nationalized. Although hospitals might remain largely private nonprofit or local governmental institutions, their performance, and that of individual physicians, would effectively be governed by the incentives created by the national insurance scheme. In higher education, state and local universities and colleges would continue to expand their domination not just in terms of market share, but also

⁹² See Deloitte, *Trends in Hospital Ownership Type and Capacity: A Decomposition Analysis* 14 (2009), online at http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/us_ps_FinancingHumanServicesReport_080709.pdf (visited Oct 21, 2011).

⁹³ See Henry Hansmann, *Why Do Universities Have Endowments?*, 19 *J Legal Stud* 3, 4, 13, 39–40 (1990).

in terms of quality. After all, the University of California at Berkeley had become the finest university in the world. Private nonprofit colleges and universities would continue to serve a generally prosperous elite seeking an education accompanied with substantial amenities, but would become increasingly marginal for higher education as a whole.

Of course, it hasn't worked out that way. Health care took a strong turn toward capitalism, with large investor-owned corporations rapidly expanding their presence in hospital care, health insurance, and physician practices (via for-profit health maintenance organizations). Higher education has moved more slowly in this respect, but the pace seems to be increasing. The public presence in the industry is retreating, the proprietary presence is expanding, and both public and nonprofit institutions are coming increasingly to resemble proprietary firms as public institutions charge ever higher tuition and the nonprofit institutions centralize authority and treat faculty more and more like ordinary employees.

In the long run, in fact, it seems reasonable to expect that the market will play a much larger role in higher education than it will in health care. Individuals need insurance against bad health, but it is not obvious that there is any effective way to provide efficient health insurance in a competitive market. An effective health insurance policy should presumably be lifelong, but the rate of change in health care is so great that it is difficult to write an efficient contract for even a year or two. Government may for now be able to force the construction of subnational pools for which private insurers can bid, but with high residential and employment mobility it seems quite possible that this approach will ultimately fail and full nationalization of health insurance will be required, leaving it to the national government rather than the market to make basic decisions about the type of health care to be provided, and its distribution across the society.

Higher education, meanwhile, seems to be going in the reverse direction. The unit of consumption will probably continue to shrink, as students increasingly shop across institutions for individual courses rather than looking for a single vendor of a four-year experience. And online learning should expand radically the range of institutions and courses available. The national government will play an increasing role in financing, which will come largely on the demand side through relatively unrestricted grants and loans to students that are tenable at well-regulated proprietary schools as well as at nonprofit and public institutions. Subject to this broad subsidy, market forces will continue to determine the quantity and

character of education provided. Proprietary institutions will come to dominate the lower end of the education market and will make inroads in the top end as well, while public colleges and universities retreat relatively rapidly and nonprofit institutions retreat rather more slowly.

Capitalist higher education may be a bit unnerving for some of us. I've spent most of my life teaching at an institution whose neo-Gothic architecture makes it look very much like a monastery. It even has a cloister in the courtyard. For the present, that appearance isn't entirely misleading as to the atmosphere within. But after a few more decades the architecture may be the only remnant of medieval higher education that survives.

TABLE 1. ENROLLMENT IN DEGREE-GRANTING INSTITUTIONS BY OWNERSHIP FORM, 1949–2009

Year	Total Enrollment	Public		Control of Institution					
		Enrollment	%	Total	Private		For-profit		
					Not-for-Profit	Not-for-profit %	For-profit	For-profit %	
1949*	2,444,900	1,207,151	49.4	1,237,749	---	---	---	---	
1954*	2,446,693	1,353,531	55.3	1,093,162	---	---	---	---	
1959	3,639,847	2,180,982	59.9	1,458,865	---	---	---	---	
1964	5,280,020	3,467,708	65.7	1,812,312	---	---	---	---	
1969	8,004,660	5,896,868	73.7	2,107,792	2,087,653	26.1	20,139	0.3	
1974	10,223,729	7,988,500	78.1	2,235,229	2,200,963	21.5	34,266	0.3	
1979	11,569,899	9,036,822	78.1	2,533,077	2,461,773	21.3	71,304	0.6	
1984	12,241,940	9,477,370	77.4	2,764,570	2,574,419	21.0	190,151	1.6	
1989	13,538,560	10,577,963	78.1	2,960,597	2,731,174	20.2	229,423	1.7	
1994	14,278,790	11,133,680	78.0	3,145,110	2,910,107	20.4	235,003	1.6	
1999	14,791,224	11,309,399	76.5	3,481,825	3,051,626	20.6	430,199	2.9	
2004	17,272,044	12,980,112	75.2	4,291,932	3,411,685	19.8	880,247	5.1	
2009	20,427,711	14,810,642	72.5	5,617,069	3,765,083	18.4	1,851,986	9.1	

* Degree-credit enrollment only.

Source: National Center for Education Statistics, *Digest of Education Statistics: Total Fall Enrollment in Degree-Granting Institutions, by Attendance Status, Sex of Student, and Control of Institution: Selected Years, 1947 through 2009* (2010), online at http://nces.ed.gov/programs/digest/d10/tables/dt10_197.asp (visited Jan 15, 2012).