# The Bursting Bubble in Non-Profit Higher Education

## American Bankruptcy Institute Webinar
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American Bankruptcy Institute

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# John J. Monaghan

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**John J. Monaghan** is an attorney in Holland & Knight's Boston office and serves as the co-national practice group leader of the firm's Bankruptcy, Restructuring and Creditors' Rights Practice Group. Mr. Monaghan is particularly focused on representing major case participants in complex commercial insolvency and restructuring matters, with a particular focus on Chapter 11 cases. He represents both U.S.-based companies and non-U.S. companies in both in-court and out-of-court domestic and cross-border insolvency proceedings. Mr. Monaghan's creditor representations focus on matters involving senior lenders, both in syndicated and bilateral deals. He also has extensive experience representing creditors' committees, equity committees, purchasers of assets, landlords, licensors, trustees, parties to prepetition contracts and leases, litigants in adversary proceedings and unsecured creditors. His experience crosses a broad array of industries, including finance, manufacturing, construction, real estate, higher education, energy, technology, telecommunications, retail, healthcare, resort and hospitality, franchise, food service, leasing, maritime and aviation. He advises clients on the business aspects of bankruptcy and workouts, and represents clients in matters in bankruptcy court, as well as in other state and federal courts.

Mr. Monaghan has extensive experience advising for-profit and not-for-profit boards in connection with governance issues, as well as in litigating director and officer fiduciary duty issues for estate representatives and for directors and officers. Mr. Monaghan's litigation experience also includes defending and prosecuting fraudulent transfer and other avoidance actions.

Matters in which Mr. Monaghan has been lead counsel have resulted in the issuance of more than 30 published opinions on topics ranging from the impact of rights of first refusal on sales under a plan of reorganization to the constitutional authority of bankruptcy courts to enter final monetary judgments in fraud cases. He has been named as a top bankruptcy lawyer by numerous ranking publications, and in 2008, Mr. Monaghan was inducted as a fellow in the American College of Bankruptcy (ACB) – a professional, educational and honorary association whose membership is limited to those in the profession who exemplify the highest standards of professional and ethical standards. In 2010, he was named as a fellow of the American Bar Foundation (ABF). Mr. Monaghan was also named to the International Insolvency Institute (III) in 2016, an invitation-only institution consisting of the top cross-border financial industry professionals in the world.

A frequent lecturer on bankruptcy issues, Mr. Monaghan has presented seminars on the Bankruptcy Code safe harbors for financial industry transactions, the fiduciary duties of not-for-profit officers and directors in higher education, litigating contested plan confirmation proceedings, the purchaser's perspective in transactions with a Chapter 11 debtor, cross-border issues in energy industry insolvencies, and maritime insolvency issues for organizations, including the American Bankruptcy Institute (ABI), the National Conference of Bankruptcy Judges (NCBJ), the International Bar Association (IBA), Marine Money and the Association of Insolvency and Restructuring Advisors (AIRA).

# Mark D. Podgainy

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**Mark D. Podgainy, CTP**, is a managing director in the New York office with more than 20 years of experience working with healthy, underperforming and distressed middle market businesses, both as an advisor and as a member of the management team. He provides operations restructuring, business plan analysis, performance improvement, cash and vendor management, bankruptcy consulting and interim management services. He also works with law firms on forensic and litigation support assignments in bankruptcy cases. His clients have included business owners, boards of directors, private equity firms, lenders, creditors' committees and law firms, and he has worked in the consumer products, building products, food, hospitality, retail, apparel and textile, and real estate sectors. Mark also has experience with both the non-profit and education sectors, including ConnectEdu and The College of New Rochelle, both described herein.

Mark has extensive experience in successfully guiding middle market companies through workout and restructuring processes, both in court and out of court, throughout the country. He has served as CRO, interim CFO, treasurer or financial advisor in a variety of companies and situations. Outcomes have included successful reorganizations, enterprise and asset sales, wind downs and liquidations. In each situation, he has been able to address thorny financial, legal, organizational and governance issues to maximize recoveries for the parties-in-interest.

Mark has an MBA from Columbia University and a bachelor's degree from Cornell University's School of Hotel Administration. He is currently a board member of Neighborhood Housing Services of New York City, Inc., a non-profit that revitalizes underserved neighborhoods; the NYC Chapter of the Turnaround Management Association; and of 520 West 19th Street Condo Association. He is a Certified Turnaround Professional, a member of the American Bankruptcy Institute, the Turnaround Management Association, and the Cornell Hotel Society and has written frequently on mergers and acquisitions, real estate and related topics for numerous industry trade publications.

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**Matthew G. Roseman** heads the firm's Bankruptcy and Creditors' Rights department. He represents debtors, secured creditors, landlords and acquirers of assets in bankruptcy proceedings throughout the United States. Over his years of practice, Matthew has advised debtors and creditors in corporate reorganizations involving both public corporations and privately held businesses, and he has successfully argued a case of the first impression before the United States Court of Appeals for the 2nd Circuit involving an issue of the bankruptcy procedure. Matthew also has particular experience representing construction companies and contractors in bankruptcy proceedings and workouts, and he regularly provides True Sale, Safe Harbor and Non-Consolidation opinion letters in complex commercial transactions.

Bar Admissions
- New York
- U.S. Court of Appeals for the Second Circuit
- U.S. District Court for the Eastern District of New York
- U.S. District Court for the Southern District of New York

Education
- J.D., George Washington University Law School, 1988
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# Sean C. Southard

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**Sean Southard's** practice is focused on middle market businesses with extensive experience in areas of financial restructuring, acquisitions, financing arrangements, commercial transactions, as well as complex commercial litigation. During his years of practice, he has counseled both debtors and creditors in many industries and varying sectors of the economy in a wide range of matters, essentially from formation to liquidation.

Mr. Southard is also a registered mediator with the panels established by the Bankruptcy Courts for the Southern and Eastern Districts of New York. In this capacity, he has extensive experience settling and mediating commercial disputes and claims. Mr. Southard routinely appears in prominent local and national bankruptcy cases and out of court restructurings and frequently speaks publicly on timely commercial law and restructuring topics.

Mr. Southard is a graduate of St. John's University and received his law degree from St. John's University School of Law. While in law school Mr. Southard served as editor of the American Bankruptcy Institute Law Review. He also served as a legal intern with the Honorable Cornelius Blackshear, United States Bankruptcy Judge in the Bankruptcy Court for the Southern District of New York. Mr. Southard is admitted to practice in the State of New York and the United States District and Bankruptcy Courts for the Southern and Eastern Districts of New York. Mr. Southard routinely speaks publicly on timely commercial law and restructuring topics and is quoted in the popular press.

# How Did We Get Here?

# How Did We Get Here?

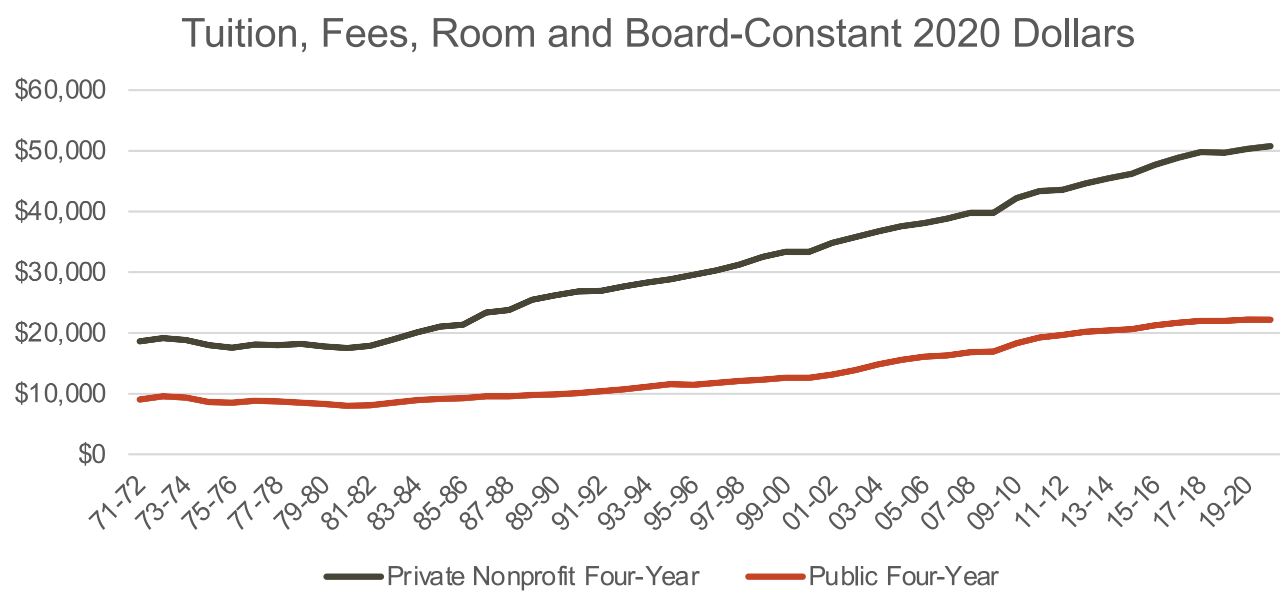
Overall enrollment has declined every year since 2014, with public 2-year colleges experiencing a greater than average decline. The COVID-19 pandemic had a significant impact on the enrollment trend in 2020.

| | Enrollment % Change from Prior Year | |
|---|---|---|
| Enrollment Year | All Institutions | Public 2-Year College |
| 2014 | -1.3% | -4.4% |
| 2015 | -1.7% | -2.4% |
| 2016 | -1.3% | -2.6% |
| 2017 | -1.0% | -1.7% |
| 2018 | -1.7% | -3.2% |
| 2019 | -0.8% | -1.4% |
| 2020 | -4.4% | -10.1% |

Source: National Student Clearinghouse Research Center

## How Did We Get Here?

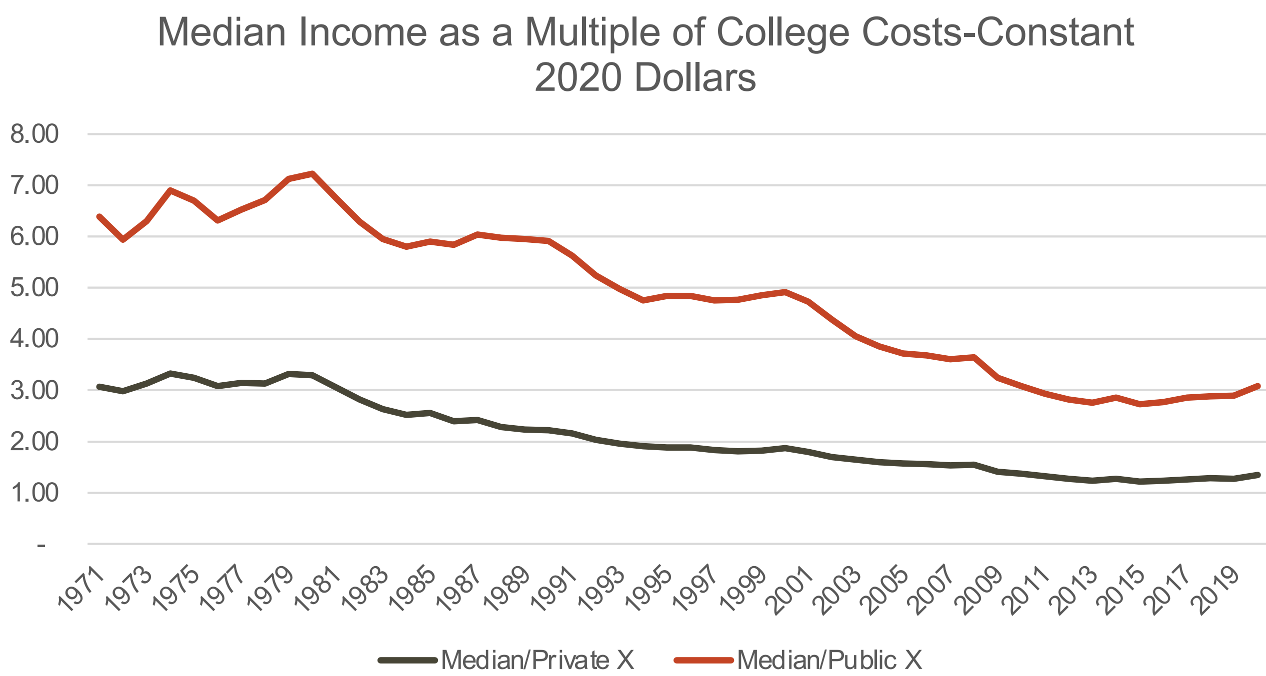
The cost of college has increased steadily over the last 40 years for both private and public institutions….




Source: The College Board

# How Did We Get Here?

….while median income as a multiple of college costs has steadily declined over the same period.

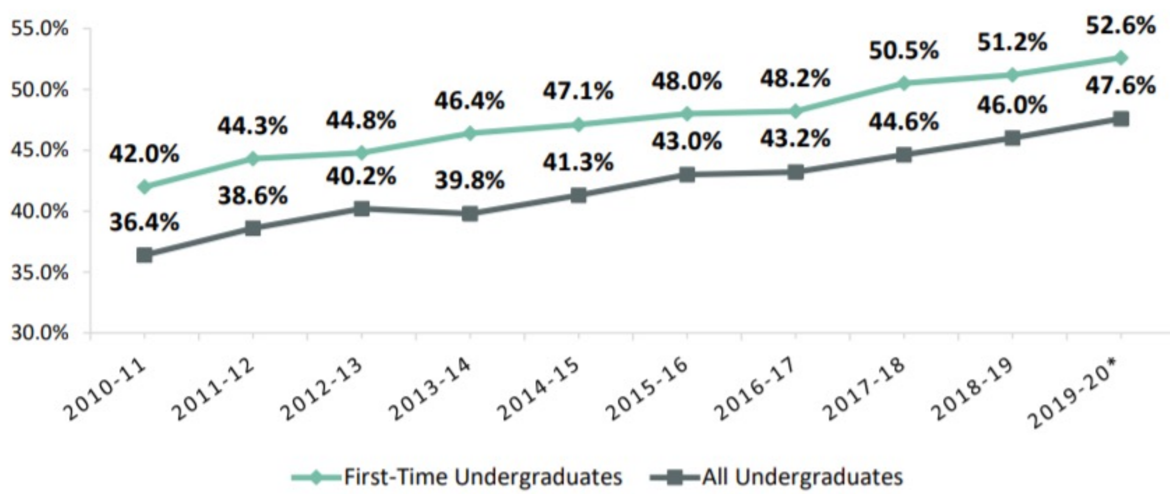



Source: DQYDJ

# How Did We Get Here?

In order to attract students in a high cost, declining enrollment environment, many institutions have increased their discounts.

FIGURE 1: AVERAGE INSTITUTIONAL TUITION DISCOUNT RATE, BY STUDENT CATEGORY




**Source**: NACUBO Tuition Discounting Study, 2010 to 2019; data are as of the fall of each academic year.
***Note:** Preliminary estimates.

## How Did We Get Here?

Over time, the government has increased the Stafford Loan borrowing limits, which has been an enabler in the run-up of college costs.

| Stafford Loans | | | |
|---|---|---|---|
| ***Annual Loan Limits--Dependent Students*** | | | *PLUS* |
| ***Effective Dates*** | *Subsidized* | *Unsubsidized* | *Loans* |
| **7/2/1967 to 5/31/1973** | $6,000 | $0 | |
| **6/1/1973 to 5/19/1977** | $7,500 | $0 | |
| **5/20/1977 to 10/16/1986** | $10,000 | $0 | |
| **10/17/1986 to 12/31/1986** | $10,000 | $0 | $20,000 |
| **1/1/1987 to 6/30/1993** | $13,250 | $0 | $20,000 |
| **7/1/1993 to 9/30/1993** | $17,125 | $0 | * |
| **10/1/1993 to 6/30/1994** | $17,125 | $0 | * |
| **7/1/1994 to 6/30/1996** | $17,125 | $0 | * |
| **7/1/1996 to 6/30/2007** | $17,125 | $0 | * |
| **7/1/2007 to 6/30/2008** | $19,000 | $0 | * |
| **7/1/2008 to the present** | $19,000 | $8,000 | * |
| ***Cost of Attendance minus Aid Received** | | | |

# How Did We Get Here?

Other issues include:

- **Changing demographics** – between 2000 to 2017, the U.S. population increased by 15 percent, from 282 million to 325 million. The traditional college age population, 18- 24-year olds, increased 13 percent between 2000 and 2010 (from 27.3 million to 30.8 million), but remained fairly constant between 2010 and 2017, ending at 30.5 million. *(Source: National Center for Education Statistics)*

- **Migration patterns** - people are moving from the Northeast and Midwest to sunbelt and southern states like Florida, Arizona, Texas, and Georgia. Geographic enrollment trends are following the same patterns. Smaller, private colleges have typically drawn from within their region, and migration towards central and southern states are projected to cause a decrease in high school graduates from the northeast.
  - U.S. census estimates from 2010 to 2018 show that the youth population dropped more than 10 percent in the New England states of Vermont, New Hampshire, and Connecticut. Meanwhile, New England, with over 250 colleges and universities, has disproportionately more four-year private non-profit colleges compared to the rest of the nation. Schools that draw from a wider geographic region, with high selectivity, strong matriculation and revenue diversity don't face the same vulnerabilities. *(Sources: Fitch Ratings, GlobeSt.com)*

- **Increase in supply** – the number of public and private non-profit four-year institutions increased from 1,830 in 2000 to 2,030 in 2019, an increase of 10.9%, while the number of private for-profit 4-year institutions increased from 210 to 300, an increase of 42.9%. *(Source: National Center for Education Statistics)*

# Institutions At Risk

# Institutions at Risk

Following are common characteristics of institutions most at risk:

- Small liberal arts schools
- Non-urban
- Tuition dependent
- Small endowments
- No differentiation – requiring steep discounts to attract enrollment

# Institutions at Risk

Below is an illustrative comparison of the balance sheets of three liberal arts institutions.

| | CNR | Dowling | Mt. Ida |
|---|---|---|---|
| **Assets** | **2018** | **2015** | **2015** |
| Cash and cash equivalents | $ 1,840,623 | $ 170,225 | $ 4,001,764 |
| Restricted cash | 1,000,001 | 3,514,940 | |
| Student accounts receivable, net of allowance for doubtful accounts | 6,701,212 | 960,635 | 488,317 |
| Contributions and other receivables, net | 1,919,996 | 2,088,137 | 51,148 |
| Other assets | 8,702,891 | 4,507,612 | 1,161,508 |
| Investments | 4,004,591 | 6,107,088 | 23,526,670 |
| Land, buildings, and equipment, net | 57,688,165 | 50,402,208 | 54,006,033 |
| **Total assets** | $ 81,857,479 | $ 67,750,845 | $ 83,235,440 |
| **Liabilities and Net Assets:** | | | |
| **Liabilities:** | | | |
| Accounts payable and accrued expenses | $ 10,322,893 | $ 8,364,048 | $ 780,466 |
| Payroll tax liabilities | 20,152,409 | | 2,006,845 |
| Notes payable | 5,344,508 | 6,757,500 | 12,518,376 |
| Student deposits and advance fees | 923,506 | | |
| Deferred revenue | 6,963,726 | 45,828 | 5,265,449 |
| Interest rate swap | 179,023 | | |
| Long-term debt | 46,689,492 | 46,675,039 | 39,353,139 |
| Accrued postretirement benefit obligation | 557,279 | | 5,006,629 |
| U.S. government grants refundable | 4,443,663 | | |
| Other Liabilities | - | 2,023,715.00 | 1,871,650 |
| **Total liabilities** | 95,576,499 | 63,866,130 | 66,802,554 |
| **Net assets (deficiency):** | | | |
| Unrestricted | (19,998,842) | (1,242,159) | 14,527,692 |
| Temporarily restricted | 2,528,107 | 3,217,303 | 628,349 |
| Permanently restricted | 3,751,715 | 1,909,571 | 1,276,845 |
| Total net assets (deficiency) | (13,719,020) | 3,884,715 | 16,432,886 |
| **Total liabilities and net assets** | $ 81,857,479 | $ 67,750,845 | $ 83,235,440 |
| Fixed Assets as % of all assets | 70% | 74% | 65% |
| Endowment (investments) as % of all assets | 5% | 9% | 28% |

# Institutions at Risk

Below is an illustrative comparison of the income statements of three liberal arts institutions.

| | CNR | Dowling | Mt. Ida |
|---|---|---|---|
| | 2018 | 2015 | 2016 |
| | Total | Total | Total |
| | - | – | - |
| **Revenues, investment return, and other support** | | | |
| Tuition and fees | 61,835,450 | 44,972,150 | 50,754,219 |
| Tuition Discounts | (16,132,486) | (18,417,312) | (18,645,121) |
| Auxiliary Enterprises | | 3,965,094 | |
| Contributions | 3,505,862 | 1,351,261 | |
| Grants and contracts | 3,003,978 | | 8,114,300 |
| Investment income | 410,255 | 41,664 | 7,543 |
| Sales and services of auxiliary enterprises | 4,255,185 | - | - |
| Other revenue | 532,477 | 694,886 | 1,536,414 |
| **Total revenues** | 57,410,721 | 32,607,743 | 41,767,355 |
| | | | |
| **Expenses** | | | |
| Salaries and wages | 24,896,538 | 13,436,015 | 16,126,892 |
| Employee benefits | 5,486,393 | 3,149,052 | 3,114,954 |
| Contracted services | 5,477,314 | 1,586,632 | 2,126,389 |
| Payroll tax penalties and interest | 2,673,382 | 958,045 | 1,345,914 |
| Professional fees | 3,218,933 | | |
| Supplies | 588,203 | | |
| Depreciation | 1,846,240 | 3,224,249 | 2,985,540 |
| Bad debt expense (recovery) | 1,357,183 | | |
| Interest | 3,241,791 | 3,233,750 | 1,546,618 |
| Rent and lease expense | 3,080,730 | 2,602,239 | 5,004,324 |
| Repairs and maintenance | 677,496 | | |
| Utilities | 1,362,861 | | |
| Insurance | 711,093 | 1,194,706 | 817,049 |
| Other expenses | 4,565,303 | 7,421,429 | 10,463,392 |
| **Total expenses** | 59,183,460 | 36,806,117 | 43,531,072 |

# Chapter 11 and Alternatives

# Issues With Chapter 11

## Chapter 11 does not offer higher education institutions an opportunity to rehabilitate.

§541. Property of the estate

(b) Property of the estate does not include—

(3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (20 U.S.C. 1001 et seq.; 42 U.S.C. 2751 et seq.),[1] or any accreditation status or State licensure of the debtor as an educational institution;

34 CFR § 600.7 - Conditions of institutional ineligibility.

(a) General rule. For purposes of title IV of the HEA, an educational institution that otherwise satisfies the requirements contained in §§ 600.4, 600.5, or 600.6 nevertheless does not qualify as an eligible institution under this part if –

(2) The institution, or an affiliate of the institution that has the power, by contract or ownership interest, to direct or cause the direction of the management of policies of the institution -

(A) Files for relief in bankruptcy, or

(B) Has entered against it an order for relief in bankruptcy;

# Issues With Chapter 11

20 U.S. Code § 1002 - Definition of institution of higher education for purposes of student assistance programs

(4) Limitations based on management
An institution shall not be considered to meet the definition of an institution of higher education in paragraph (1) if—

> (A)the institution, or an affiliate of the institution that has the power, by contract or ownership interest, to direct or cause the direction of the management or policies of the institution, has filed for bankruptcy, except that this paragraph shall not apply to a nonprofit institution, the primary function of which is to provide health care educational services (or an affiliate of such an institution that has the power, by contract or ownership interest, to direct or cause the direction of the institution’s management or policies) that files for bankruptcy under chapter 11 of title 11 between July 1, 1998, and December 1, 1998;

# Issues With Chapter 11

There are automatic stay exclusions under section 362(b), (14) through (16):

**(b)** The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay—

**(14)** under subsection (a) of this section, of any action by an accrediting agency regarding the accreditation status of the debtor as an educational institution;

**(15)** under subsection (a) of this section, of any action by a State licensing body regarding the licensure of the debtor as an educational institution;

**(16)** under subsection (a) of this section, of any action by a guaranty agency, as defined in section 435(j) of the Higher Education Act of 1965 or the Secretary of Education regarding the eligibility of the debtor to participate in programs authorized under such Act;

# Chapter 11 Alternatives

The choices available to institutions re: dependent on time and sufficient cash, and they include:

- "Performance improvement"
  - Offering new programs
  - Revamp marketing to drive enrollment
  - Cost reductions
  - Discontinue non-contributing programs
- Declare finance exigency
- Transaction
  - Sale
  - Merger
  - Joint venture
  - Cost sharing
- Teach-out
- Receivership
- Liquidation

# Chapter 11 Alternatives

Following are key considerations in choosing alternatives:

- Financial runway
- Gap between appraised and market values
- Dynamics of public vs. private debt
- Regulatory requirements
  - Accreditation
  - Attorney General
  - U.S. DOE
  - State DOE