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Misdeeds in the US Higher Education:

Illegality versus Corruption

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Corruption in higher education has long been neglected as an area of research in the US. The processes of decentralization, commoditization, and privatization in higher education rise questions of accountability, transparency, quality, and access. Every nation solves problems of access, quality, and equity differently. Thus, although prosecuting corruption in higher education is part of the legal process in every country, the ways in which legal actions are undertaken differ. This paper addresses the question: How is corruption in higher education understood and defined in legal cases, what particular cases receive more attention, and how these cases correlate with the major educational reforms, changes, and socio-economic context in the nation? Specifically, it analyses records of selected legal cases devoted to corruption in the US higher education. Decentralized financing of higher education anticipates cost sharing based in part on educational loans. The US higher education sector grows steadily, and so do opportunities for abuse, including in educational loans. The rapid expansion of education sector leaves some grey areas in legislation and raises issues of applicability of certain state and federal laws and provisions to different forms of misconduct, including consumer fraud, deception, bribery, embezzlement, etc. Higher Education Act, False Claims Act, and Consumer Protection Act cover corruption as related to the state and the public sector; corruption as related to client, business owner, and an agent; and corruption as related to consumer-business relations. However, the legal frame is simplistic, while the system of interrelations in the higher education industry is rather complex.

Key words: bribery, corruption, deception, fraud, higher education, law, loans, US

Introduction

Corruption in higher education has long been neglected as an area of research in the US. One reason for this might be that the relative scarcity of prosecuted cases has made it at first appearance not a large problem in the nation's higher education, not significant enough from the researchers' standpoint to be paid much attention. Another explanation for this is that the all of the scholars attended higher education institutions and most of them teach in colleges and universities. The sense of belonging and close affiliation may prevent from involving in research of academic corruption. Also, scholars as well as the media are overly cautious about the language of investigations and usage of such explicit legal terms as corruption, bribery, fraud, replacing them with such terms as misconduct and breach of integrity. Finally, definition of education corruption itself is still vague and undeveloped. This creates uncertainty in the subject matter of the prospective research, approaches to be applied, and methodologies to be employed. The limits of the object of the research, i.e. the locus, also remain unclear for those who would want to venture to study corruption in higher education.

Corruption in higher education is a newly emerging topic in the field of education research. Some aspects of corruption in education have been addressed in last two decades, including works by Anderson (1989), Anderson (1992, 1999), Eckstein (1993, 2001, 2003), Hallak and Poisson, (2002, 2007), Heyneman (2004, 2007), Noah and Eckstein (2001), Petrov and Temple (2004), Segal (2004), Sykes (1988), and Woshburn (2005), as well as in numerous news publications. There was an increase in the interest to the issue of corruption in higher education observed in recent years. Scholarly work on corruption in higher education is lacking while the problem itself is significant. Legal cases on corruption in higher education grow in number and receive more attention from the media, legislators, numerous constituents, and from

the general public. The presence of corruption in higher education throughout the world is a growing concern for the industry as it influences its effectiveness and efficiency. The negative impact of higher education corruption on economic development and social cohesion is also disturbing.

The three major issues in higher education are access, quality, and equity. These issues are universal and at stake in every nation. Corruption affects all three of these issues. It has a negative impact on the quality of higher education and other services; it increases inequality in access to higher education, and causes inequities. Every nation solves problems of access, quality, and equity differently. Thus, although prosecuting corruption in higher education is part of the legal process in every country, the ways in which legal actions are undertaken in order to prosecute and curb corruption in higher education differ. The major task of this paper is to address the question: How is corruption in higher education understood and defined in legal cases, what particular cases receive more attention, and how these cases correlate with the major educational reforms, changes, and socio-economic context in the nation? Specifically, it analyses records of selected legal cases devoted to corruption in higher education.

Defining corruption

The word *corruption* comes from the Latin word *corruptio*, which in Medieval Latin expressed a moral decay, wicked behavior, putridity, rottenness (Johnston 1996, p. 322). Milovanovic (2001) says that in this context one could talk of bribes, or other dishonest means for achieving particular disgraceful ends, as a symptom of an ailing society. Johnson's Dictionary defines bribe as "a reward to pervert the judgment or corrupt the conduct," while corruption is "a loss of purity and purpose, a social decomposition." (Osborne 1997, p. 10)

Transparency International uses a clear and focused operational definition of corruption as the misuse of entrusted power for private gain.¹

White and Allen point out that “Agreed upon definitions are rare, and definitions of corruption run the gamut of being too broad to be rendered relatively useless to being too narrow and thus be applicable to only limited, rare, well-defined cases.” (White and Allen, 2003, p. 282) The discussion of corruption is field specific. The literature in political science focuses on corruption in public policy. It includes rent-seeking behavior (Krueger, 1974; Klitgaard, 1986; White, 1996), the rise of state bureaucracies (Wilson, 1975; Weber, 1978), and cross-national characteristics (Treisman, 2000). The definition most cited in the political literature is given by Nye: “Corruption is behavior which deviates from the normal duties of a public role because of private-regarding (family, close private clique), pecuniary or status gains, or violates rules against the exercise of certain types of private-regarding influence. This includes such behavior as bribery (use of reward to pervert the judgment of a person in a position of trust); nepotism (bestowal of patronage by reasons of ascriptive relationship rather than merit); and misappropriation (illegal appropriation of public resources for private-regarding use).” (Nye 1967, p. 419)

It might be useful to start the endeavor of defining corruption in higher education with the legal definition of corruption as presented in the US federal laws. Similar to scholarly publications, in legislation most of the attention is paid to political corruption.²

¹ Transparency International, 2007. Retrieved June 22, 2007, from http://www.transparency.org/news_room/faq/corruption_faq

² See references to political corruption “Section 610 of the Federal Corrupt Practices Act makes it a crime for a corporation or a labor union to make a ‘...contribution or expenditure in connection with...’ federal elections.” Reference to *United States vs. International Union of Automobile Workers, CIO*, 352 US, 567, 575, (1957). Federal Corrupt Practices Act. Comments. Constitutionality of section 610 of the Federal Corrupt Practices Act. *California Law Review*,

In general, on the federal level, aside the political corruption, one may find more concerns with foreign corrupt practices than with domestic ones. These include The Foreign Corrupt Practices Act of 1977 (15 U.S.C. § 78dd-1, et seq.) The Foreign Corrupt Practices Act is a United States federal law known primarily for two of its main provisions, one that addresses accounting transparency requirements under the Securities Exchange Act of 1934, and another concerning bribery of foreign officials, and International anticorruption and good governance provisions.³ The Act was amended in 1998 by the International Anti-Bribery Act of 1998 which was designed to implement the anti-bribery conventions of the Organization for Economic Cooperation and Development (OECD). There are also Consumer and Borrower Protection regulations in the federal legislation, but they do not fill the gap between the legal regulations and a common sense understanding of corruption. This explains the presence of grey areas in the field of corruption that are left unattended. Different related laws may apply to different crimes or misdeeds, but precedents have to be made, corruptibility has to be established, and terminology has to be further developed.

The term most associated with corruption is bribery. Bribery signifies the phenomenon itself and the act of corruption, while bribe denotes the mean of exchange. USCS, when presents definition of corruption, primarily refers to Bribery and Graft section.⁴ Corruption is conventionally understood as indivisible from the public sector, requiring a public official to be a primary object of bribery.

4693), p. 439). The Federal Corrupt Practices Act §602, 18. In United States Code Service: lawyers edition. General Index A-C, USCS. Bribery and graft, p. 879

³ United States Code Service: Lawyers Edition. General Index A-C, USCS.

⁴ United States Code Service: Lawyers Edition. General Index A-C, USCS. Bribery and Graft section, p. 578.

According to §201 of the USCS, bribery of public officials and witnesses, the term “public official” means Member of Congress, delegate, or resident Commissioner, either before or after such official has qualified, or an officer or employee or person acting for or on behalf of the United States, or any department, agency or branch of Government thereof, including the District of Columbia, in any official function, under or by authority of any such department, agency, or branch of Government, or a juror. This also includes a “person who has been selected to be a public official.”⁵

A corrupt public official “directly or indirectly, corruptly demands, seeks, receives, accepts, or agrees to receive or accept anything of value personally or for any other person or entity in return for: (A) being influenced in his the performance of any official act; (B) being influenced to commit or aid in committing, or to collude in, or allow, any fraud, or make opportunity for the commission of any fraud, on the United States, or; (C) being induced to do or omit to do any act in violation of the official duty of such official or person.”⁶ A corrupt public official is a recipient in a corrupt transaction. Donor, or bribe-giver, is “whoever directly or indirectly, corruptly gives offers, or promises anything of value to any public official...”⁷

The legal structure that operates in the realm of bribery and corruption appears to be over-simplistic--there are bribe givers and bribe receivers. However, complexities come in when particular legal cases are considered and judged on, especially those involving large organizations and systemic abuse of public office. There are too many nuances, such as “had authority,” “did not have authority,” “accepted without an intent to change his opinion,” “gave gift without an intent to influence the discretion or change the decision,” etc.

⁵ United States Code Service: Lawyers Edition. Crimes and Criminal Procedures §§1-430. Title 18 USCS. Chapter 11. Bribery, Graft, and Conflicts of Interest, pp. 278-279.

⁶ Ibid., p. 279.

⁷ Ibid., p. 279.

Legality versus corruptibility

Not all illegal acts that take place in higher education constitute acts of corruption. At the same time, not all the acts that are commonly understood as corrupt are immediately or explicitly qualified as illegal. Broader conceptual understanding of corruption is needed. Legality and corruptibility may be dominating characteristics of a corrupt agreement. Corruptibility denotes possibilities for abuse and vulnerability of the system overall, while legality implies certain laws set by the public through the state or the ruling regime. The issue of legality versus corruptibility is appealing in the sense that it positions intents, possibilities, opportunities, mere expectations, and public trust against such specific terms as public office, size of a bribe, fact of bribery, etc.

Arora (1993) singles out four perspectives on corruption, including legal, historico-cultural, public interest, and market-centered approaches. Hodgkinson (1997) notes that “According to Arora, the main advantage of adopting a legal perspective on corruption is that it ‘...enables an agreement over the definition and ... scope of its study’ (1993:2). It therefore involves defining corruption in terms of behaviour which deviates from the legal norms of public office.” Hodgkinson presents a review of conceptual approaches to the issue of corruption, outlines primary and secondary corruption, and points to the weaknesses and possible pitfalls of marketisation in public services. He suggests that “The attempt to model public service organizations on private enterprise is meant to align the former with a changed socio-economic environment. The basic premise being that the success of the private sector model can be replicated in the public services. Marketisation has therefore involved a movement from ‘budgetary’ to ‘for-profit’ organizations.” (Hodgkinson, 1997, p. 15)

Legal perspective appears to be one of the accepted forms of approaching corruption. Arora points out that legal perspective "...enables an agreement over the definition and ...the scope of its study." (Arora, 1993, p. 2) In addition to legal perspective, there might be numerous other perspectives employed, including historic, cultural, public interest, and market-centered perspective. Another approach anticipates possible conceptual frames based on legal, economic, social, moral, and ethical responsibilities.

As applied to higher education, a legal lens uses the set-out laws and regulations that project on complex processes occurring in the education sector in order to sort out legal and illegal ones. The economic responsibility anticipates compliance with mutually accepted economic obligations under which violations of such obligations are considered a breach of contract. Reduced class time, increased class size, absence of office hours held by faculty members, and unfavorable lending terms and conditions on educational loans may be considered a breach of contract. While not necessarily specified in laws and legal provisions for higher education, such practices may be interpreted as a violation of economic responsibility.

The social responsibility frame is even more complex than legal and economic responsibility frames. The social responsibility frame anticipates that higher education institution adheres to all legal and economic obligations and, in addition, performs its societal duties. Educational, research, cultural, and other considerations are taken into account. The social responsibility frame views higher education institution as an organization that conducts responsible research for the betterment of the society, educates members of the society in accordance with the best standards available, and disseminates knowledge to those who are in need of it. Monetary transactions and the financial prosperity of an institution of higher learning

are secondary in such cases. This is also known as a service for public good that increases total social welfare of the society.

Finally, the moral or ethical responsibility is meant to move higher education institution to prioritize the issue of equity over the issue of quality, and quality over access. If under the economic responsibility frame, a university sets its admission criteria and regulates quality of educational services offered based on demand and supply on the education market, ethical responsibility anticipates equality in access to education and the provision of highest quality educational services under the conditions of maximizing the position of learners and the society overall rather than of profit maximization.

While ethical, social, and economic frames are more universalistic, the legal responsibility frame is clearly nation-specific. On the one hand, economic structures in the education sector vary country by country and can be assigned to a few basic models; on the other hand, legal perspective can allow for some future perspective rather than simple comparisons. Experiences of other nations and comparative perspective as applied to higher education corruption are of little help. The US higher education system is unique in the way it is organized and funded. The US higher education sector may be described as decentralized, market-oriented, and autonomous. Other developed nations, including the European Union, have centralized higher education sectors that may be characterized by weak links with businesses and slowly emerging market-like practices. Educational loans are not common in the developed nations. Hence, national legislations do not reflect such practices. The process of commoditization of higher education in the US continues, while in Europe it only emerges.

We consider corruption to be broader than it is defined in legal cases. At the same time we use the level of legal responsibility from the set of legal, economic, social, moral or ethical

responsibilities to qualify deeds as corrupt. But even this approach does not cover all the areas. There are so-called grey areas that may be judged as corrupt yet still not illegal. Norms of contractual behavior accepted by the society go ahead of legislation. The series of investigations launched by the Attorney General of New York, Mr. Cuomo, is a classical example of grey area application. It leads to new, more precise, more specific, contextual interpretation of existing laws, and results in new provisions, regulations, and codes of conduct.

Corruption in higher education

The definition of education corruption includes abuse of authority for material gain (Anechiarico and Jacobs, 1996). Heyneman adds to this definition by arguing the following: “But because education is an important public good, its professional standards include more than just material goods; hence the definition of education corruption includes the abuse of authority for personal as well as material gain.” (Heyneman, 2004, p. 638) Miller, Roberts, and Spence point to the relativity of the term corruption and apply it to academia:

The notion of a corrupt official or other role occupant exists only relative to some notion of what an uncorrupted occupant of that morally legitimate role consists of. The notion of an academic has at its core the moral ideal, or at least, the morally legitimate role, of an independent truth-seeker who works in accordance with accepted principles of reason and evidence, who publishes in his or her own name only work that he or she has actually done, and so on. So an academic motivated by a desire for academic status who intentionally falsifies his or her experimental results or plagiarizes the work of others is corrupt relative to the ideal or morally legitimate role of an uncorrupted academic. On the other hand, a person occupying an academic position who paid no heed whatsoever to the

truth or to principles of reasoning and evidence and who made no pretense of so doing would at some point cease to be an academic of any sort, corrupt or otherwise (Miller, Roberts, and Spence, 2005, p. 5).

The International Institute for Educational Planning (IIEP) offers defining corruption in education as a “misuse of public office for private gain that influences access, quality, and equity in education.”⁸ Sayed and Bruce (1998) and Waite and Allen (2003) present a broad social approach to define corruption. Petrov and Temple (2004) adhere to the legal approach to corruption and apply narrow definition of corruption that regards corruption as such only if it implies illegality.

National laws differ and legality and illegality are not universal. Accordingly, there might be not one universal definition of corruption in higher education that would apply equally well to different national systems in different historical periods. Granting access to publicly funded higher education on any premise other than academic merit is equated to corruption. Access to higher education in exchange for a bribe is deemed to be corrupt. In the decentralized market-based systems of higher education, gaining access to educational services in exchange for payments is a norm. Depending on the system and legal frameworks laid in the society, certain forms of funding, modes of operation, patterns of behavior, and standards of conduct in higher education may be considered corrupt or non-corrupt. Corruption in higher education is time and place specific and may be found in public and private higher education institutions.

Definition of corruption as it is used in economics underlines role of the state and assumes corruptibility of a government official. Corruption in higher education presents the need for a more inclusive definition. The challenge to the understanding of corruption as applied to

⁸ The International Institute for Educational Planning (IIEP), <http://www.unesco.org/iiep/eng/research/research.htm>

higher education arises when one is confronted with cases of bribery. These may take place in private higher education institutions as well as in the public ones. Anecdotal evidence from the Former Soviet Bloc indicates that bribery in higher education may be as common in private colleges as in state colleges and universities. Students pay bribes in exchange for good grades independently of the type of higher education institution. This urges for more inclusiveness in the definition of corruption.

This paper uses operational definition of corruption in higher education as a system of informal relations established to regulate unsanctioned access to material and nonmaterial assets through abuse of the office of public or corporate trust (Osipian, 2007). In this sense, corruption in the higher education sector anticipates abuse of public trust by certain participating groups or individuals-participants of educational process in a broad sense, and processes, closely related to educational process, such as research, selection of students, funding, faculty hiring and promotion, use of public property, etc. To summarize, this paper considers corruption as it implies illegality or a precedent and at the same time does not limit its area of investigation by the legal definition of corruption only.

Corruption as a grey area

A grey area is a term used to mark things that are unclearly defined, a border that is hard or even impossible to define, or a definition where the dividing line tends to shift. A grey area of definitions signifies a problem of sorting reality into clearly cut categories. A grey area in legal terms is an area where no clear legislation or precedent exists. It is also not clear whether the existing rules are applicable to specific cases and to what extent. A grey area of legislature as

applied to particular industries, sectors, market segments, or areas of social life signifies an ethical dilemma, where the border between corrupt and non-corrupt activities is vague.

Shleifer and Vishny (1993) use the term “grey area” in addressing economics of corruption. Economics has advanced significantly in modeling corruption, but is experiencing difficulties in testing the models due to the lack of large and reliable datasets (Rose-Ackerman 1978; Tirole 1992; Bardhan 1997). Whatever problem economists might have in explaining corruption is indicated by Rose-Ackerman’s (1978) definition of corruption as an “allocative mechanism” for scarce resources. The state monopolizes certain allocative functions, be it permissions and licenses, or access to public services. State officials’ profiteering is based on abuse of their discretionary powers and monopolistic positions.

Kaufmann and Vicente propose “a new explicitly micro-founded definition of corruption: it is viewed as a collusive agreement between a part of the agents of the economy who, as a consequence, are able to swap (over time; we present a repeated game) in terms of positions of power (i.e. are able to capture, together, the allocation process of the economy). This is the idea underlying high-level corruption or ‘influence’, and is broader than the notion of bribery, which corresponds to a particular sharing pattern of the joint payoff from the referred relationship.” (Kaufmann and Vicente, 2005, p.3)

The challenge to the domain of bribery in the issues of corruption, however, does not eliminate grey areas that exist in both legislation and scholarly work. Grey areas in legal scholarship and in economics project on legislation and the national economy, respectively, and overlap. Tax evasion and fraud as key characteristics of shadow or unofficial economy are good examples of such an overlap.

Petrov and Temple comment that “we find unconvincing the proposition that there exists a continuum from ‘honest’ to ‘corrupt’ behaviour. Such a continuum implies a ‘grey area’. The example given at a recent conference on corruption in education of such a ‘grey area’ was the practice of some US universities of giving the children of alumni preference in admission procedures (Hallak and Poisson, 2002). This example simply adds to our doubts about the ‘continuum’ notion: one may judge this to be an undesirable way of managing university admissions, but a stated institutional policy, presumably adopted with the intention of in some sense benefiting the institution as a whole, cannot, we suggest, sensibly be classified as corrupt.”⁹

Clearly, Petrov and Temple are against the notion of grey area. This paper agrees with the notion of legality and illegality as applied to the problem of corruption, yet considers necessary to accept the fact that not all types of corrupt activities or forms of corruption are embedded in the national legislations. Furthermore, the legal lens is perfectly applicable to corruption in education, but not sufficient to understand and reflect on the complexity of the issue. The broad scope of the problem explains the vagueness of its borders.

The legal frame, however, has its limitations. In Hodgkinson’s view, “A legal perspective would negate the possibility of investigating a change in the nature of corruption.” (Hodgkinson, 1997, p. 19) To substantiate this view, Hodgkinson refers to Arora, who points out that legal frame would not “...allow looking into actions or inactions which corruption laws do not cover, yet which need to be included. In fact, corruption laws and gaps in these may themselves be an object of corruption in some systems; yet legal perspective will not deal with such actions or

⁹ In their critique of the grey area notion, Petrov and Temple refer to Hallak, J., & Poisson, M. (2002). *Ethics and Corruption in Education. Results from the Expert Workshop held at the IIEP. Paris, November 2001.* Paris: IIEP-UNESCO.

inactions, for law permits their exclusion.” (Arora, 1993, p. 2) Change is not the only challenge to the legal approach. The use of terminology sets certain limits as well.

The term “white collar crime” was coined by Edwin Sutherland at the American Sociological Society meeting in 1939. Sutherland defined the term as “crime committed by a person of respectability and high social status in the course of his occupation.”¹⁰ White collar crime anticipates high skills of a criminal and sophistication of the criminal act. The Federal Bureau of Investigation (FBI) has adopted the narrow approach, defining white-collar crime: “...as those illegal acts which are characterized by deceit, concealment, or violation of trust and which are not dependent upon the application or threat of physical force or violence.”¹¹ According to the FBI white collar crime is estimated to cost the United States more than \$300 billion annually.¹²

White collar crime does not contradict the definition of corruption and can be linked to corruption through the legal concept of commercial bribery. People tend to use area-specific stamps, such as corporate fraud, political graft, abuse of public property, embezzlement from state funds, breach of academic integrity, etc. Accordingly, white collar crime is attached to the corporate world, embezzlement and fraud to the public sector, student cheating and plagiarism to the world of academia, and research fraud to think tanks. This type of heuristics prevents one from considering the many instances of corruption that take place in the education sector. Media reports and the results of investigations indicate that all of those forms of misconduct are common in higher education.

¹⁰ Sutherland, Edwin (1949). *White Collar Crime*. New York: Dryden Press.

¹¹ U.S. Department of Justice, Federal Bureau of Investigation (1989). *White Collar Crime: A Report to the Public*. Washington, D.C.: Government Printing Office. p. 3.

¹² Legal Information Institute. Cornell University Law School. Retrieved October 15, 2007, from http://www.law.cornell.edu/wex/index.php/White-collar_crime

Selection criteria for legal cases

The cases of corruption in higher education considered in US courts include fraud in educational loans, quality of educational programs, credentials, credentials evaluation and accreditation, attempts to monopolize discretion over the admissions decisions, collusion, embezzlement, research misconduct, and fraud.¹³

This paper uses the following selection criteria for choosing legal cases for consideration: degree of corruption, level of explicitness, scale and scope, significance, precedent, level of publicity, total funds at stake, and future prospects, including both domestic and international applications. Specifically, it focuses on cases that take place in higher education, positioned in so-called grey area or uncharted waters of legislation, yet may be highly explicit and deemed inappropriate or unethical, and significant and promising in terms of their scale and scope. They may become a precedent in legal practice as related to domestic laws applied to the US higher education sector.

At the same time, this study extends its reach in two critically important directions. First, it overcomes conventionally imposed limitation on cases of corruption as occurring in the public sector only. Second, it considers cases where higher education institutions interact with both the state and private for profit entities. The heavy involvement of state and federal funds along with state and federal regulations attached to funding, as well as the state interests in higher education in a broader sense form the bridge that connects the public and private sectors. This permits an

¹³ See court cases and decisions at West's Federal Practice Digest 4th, 18A and 18B, Colleges and Universities, St. Paul, MN: West Group, 1999; and West's Federal Practice Digest 4th, 18B, Colleges and Universities, Cumulative Annual Pocket Part. St. Paul, MN: West Group, 2007.

analysis of corruption independently from the form of property of a given higher education institution.

This paper considers corruption in higher education through the legal cases, following publications, legal records, and court cases in the United States (US). The major focus is on the few selected cases of corruption in US higher education. Some of these cases are broadly publicized in the media and discussed in scholarly literature.¹⁴ Others are only briefly mentioned in the specialized media sources that focus on problems of higher education, even though they may represent a legal precedent with a potentially large future impact on the industry.¹⁵ They are significant and affect large number of higher education institutions and constituents, including educators, students, parents, and general public. The legal cases to be analyzed are at the core of the development and the reform of higher education industry. They reflect processes of decentralization, commercialization, and marketization of higher education along with the processes of coordination, quality assurance, and state control in the industry.

This research carries certain limitations, which are expressed in the set selection criteria. The selection criteria restrict the study to significant cases of corruption in higher education, and hence preserve the high degree of relevance of the conducted research, while at the same time maintaining a reasonable level of abstraction in order to purify the legal cases and focus on their essence. For instance, if the United States Code Service (USCS)¹⁶ reports on a case of embezzlement of public funds, committed by an administrative staff member in a public higher

¹⁴ See, for instance, the price fixing investigation of the so-called Overlap group in 1991, reflected in some scholarly work, including Sykes, Carol. (1988). *ProfScam: Professors and The Demise of Higher Education*. Washington, D.C.: Regnery Gateway.

¹⁵ See, for instance, Van Der Werf, M. (2006, August 6). Lawsuit U. *The Chronicle of Higher Education*, 52(48), p. A23.

¹⁶ United States Code Service: Lawyers Edition. Crimes and Criminal Procedures §§1-430. Title 18 USCS.

education institution, this case will not be considered in this study. First of all, embezzlement is not limited to the higher education sector. This practice is not distinct but rather common for all the industries, including both public and private sectors. Second, the case of embezzlement is clear and is therefore not worthy of study. However, the way the court determined whether the case should be considered under the corruption law may be of interest, as it implies problem of definitions.

In a case where a university administrator and a custodian or subcontractor collide in order to unlawfully benefit from a certain operation, a court will only consider the case if the net benefit obtained in an illegal way sums up to five thousand dollars or higher. If, however, the net benefit will be lesser than five thousand dollars, the state statutes on corruption will not apply. Hence, if a public university overpaid a private contractor for the services rendered as a result of improper collusion between the administrator and subcontractor, the court will focus on the sum of the immediate damage.

This study tends to focus on the nature and the essence of a particular misdeed, rather than on the net benefit and the appropriate statutory limitations that may apply, depending on the state legislation. Simply put, for the court, the issue is both illegality and the size of illegally obtained benefit, while for this study the case of corruption exists no matter whether the total benefit was less than five thousand dollars or more than five thousand dollars. In addition, if an alleged collusion took place between relatives, then this study would classify such a case as an example of embezzlement, nepotism, and committed fraud.

Another limitation is concerned with clear cases of corruption. In such cases, no additional research is needed to establish the case of corruption, since it was already established by the court.

Legal cases: description and essence

Major cases under the False Claims Act include U.S. versus University of Phoenix, U.S. versus Oakland City University, and U.S. versus Chapman University. In the case of University of Phoenix, the complaint says that the institution certified that it was in compliance with all the US Department of Education regulations when it paid recruiters based on how many applicants they enrolled. This constitutes a direct violation of the law. The complaint was dismissed in U.S. District Court in Sacramento and is now on appeal at the U.S. Court of Appeals for the Ninth Circuit.

Similar to University of Phoenix, Oakland City University is accused of violating the False Claims Act. The case is considered a precedent because the Seventh Circuit of the U.S. Court of Appeals ruled that the university knew it was illegal to pay recruiters and deceived the US Department of Education in order to obtain a certification of eligibility to receive federal funds.

In the case of Chapman University, the complaint says that the institution, as part of the accreditation process, certified that it was giving the required amount of classroom instruction in its academic programs, when it was not. If it had revealed the truth, the complaint alleges, Chapman would not have been accredited and would be ineligible to receive federal grants and student loans. The case is active before U.S. District Court in Santa Ana, CA, because the judge denied a motion to dismiss it.

One of the most interesting legal cases that has developed over the last twelve months, starting in February of 2007, is a set of investigations launched by the Attorney General of the State of New York, Mr. Cuomo, that looks into educational lending practices and other related

issues. The investigation discovers possible misdeeds in the link between numerous colleges and universities and businesses. In addition, other abuses of students as consumers, such as false advertisements in study abroad programs, have also become objects for investigation.

New York has a rich history of corruption. This may be explained in part by the presence of a large diverse megapolis, New York City, and a large public sector, including public education. Large scale public projects and social programs, such as education, healthcare, public housing, transportation, utilities, and such, significant financial flows and monetary transactions, complexity of the system of public and private contractors and subcontractors, large bureaucratic apparatus, and complex relations between the state and the private sector create an ideal environment for corruption. As the result, there is a relatively well developed and detailed legislation on corruption, bribery, graft, and fraud in New York State as compared to other states. Numerous precedents and cases decided in state courts present an opportunity to research corruption in higher education in the legal context.

The Attorney General has been leading an ongoing investigation into the student loan industry. He requested information from more than sixty public and private colleges and universities nationwide regarding the standards they use to determine which lending companies are included on their “preferred lender” lists. Financial aid administrators often produce such lists to direct their students toward the lenders that are most preferred by the schools but may not offer the best deals for students and parents.

The Attorney General’s Office plans to file a law suit against Education Finance Partners (EFP), a student loan lender that operates in the growing industry educational loans. Investigations conducted by Mr. Cuomo revealed the existence of specific arrangements between the EFP and over sixty colleges and universities, including Fordham University, Long Island

University, St. John's University, Boston University, Clemson University, and Baylor University. A formal notice has been issued to the EFP that the Attorney General's office will be filing suit over deceptive practices in the company's student loan business. The suit is the first filed in a nationwide investigation into the college loan industry. Specifically, the EFP was accused of paying kickbacks to colleges and universities that consistently placed the company on the preferred loan providers list.

The initial investigation conducted by the Attorney General has revealed that "Education Finance Partners has repeatedly paid schools in exchange for steering loans to EFP and for putting EFP on 'preferred lender' lists. Approximately 90% of students choose their lenders from their school's preferred lender lists. Cuomo's investigation has uncovered that neither the schools nor EFP adequately disclose to students that EFP is paying the schools to be promoted as a 'preferred lender.' Cuomo's legal action alleges that the relationship and financial arrangements between EFP and the schools constitute a deceptive business practice. Cuomo also revealed today that EFP made its financial kickback arrangements with schools through what are called revenue sharing agreements, which often were based on a tiered system that would give a higher percentage to the schools based on the amount of loans referred."¹⁷

The arrangement of rewarding colleges by the lender that can amount to the practice of paying kickbacks resulted in potentially large amounts of money paid by the EFP to universities participating in the preferred lender program. For example, the EFP's agreement with Duquesne University gives the school 60 basis points, i.e. 0.6 percent of the net value of all referred loans. The agreements are structured to encourage the schools to refer as much business as possible to

¹⁷ Attorney General Andrew Cuomo announces first legal action in college loan industry investigation (March 22, 2007). Retrieved from http://www.oag.state.ny.us/press/2007/mar/mar22b_07.html

the EFP. For example, the EFP's agreement with Boston University provides that Boston University will receive 25 basis points or 0.25 percent of the net value of referred loans of at least \$1,000,000 up to \$5,000,000; 50 basis points or 0.5 percent of value of referred loans between \$5,000,000 and \$10,000,000; and 75 basis points or 0.75 percent of the net value of referred loans over \$10,000,000.¹⁸

Mr. Cuomo accuses that some schools, such as Drexel University in Philadelphia, received over \$100,000 in kickbacks from the EFP in a single year. Under Drexel's agreement with the EFP, dated April 1, 2006, Drexel has agreed to make the EFP its "sole preferred private loan provider." In return, the EFP has agreed that Drexel will receive 75 basis points (.75 percent) of the net value of referred loans between \$1 and \$24,999,999; and 100 basis point (1 percent) of all loan amounts of \$25,000,000 or greater. Furthermore, the Attorney general alleges that the EFP engaged in deceptive marketing practices by using schools' logos, mascots, and names in the EFP promotional materials to imply that the EFP had the school's official endorsement: "EFP's marketing practices were clearly intended to imply that the universities had endorsed EFP loan products for individual student borrowers. Deceptive marketing is just that and it limits the information available for students to get the best deal in their college loans."¹⁹

The named cases are clear candidates for legal precedents, insofar as these cases reflect on deeds that take place in higher education and positioned in grey areas. Such cases await legal interpretations that will likely be influenced by a socio-economic context rather than by previous precedents in similar circumstances alone.

Analysis and discussion: legal cases in the context

¹⁸ Ibid.

¹⁹ Ibid.

The analysis and the discussion of legal cases presented in this study seek to answer the following questions. First, what is in the essence of each case? What are the underlying interests of groups involved, including consumers of educational services, providers of educational services, regulatory authorities, legislators, and the state in general? Second, is the case new or there were earlier precedents or attempts to create a precedent on a similar case? Third, are there new ways to interpret old rules and laws that are used in the case? Fourth, how is the case positioned in the context of educational reforms and socio-economic processes in the society in general? This study addresses sequences of events or cases, existing established and possible ties, common fundamentals for different or similar cases, socio-economic context, trends in the education industry, and processes of modernization and reform in the society.

There is also an additional set of questions that may be addressed in the analysis and the discussion. This additional set includes the following major questions. First, what is the degree and direction of the governmental interference in each of the cases? Here, we attempt to consider the government in a broader sense than just a legislative branch that includes prosecutors and the court system. Second, what are the possible future implications of the processes, cases, and legal decisions made? Are there any spillovers or potential for spillovers on other national educational system? Broader spillovers on the European Union and the developing nations may be possible. Third, do the findings support our definition of corruption in higher education?

The case of the US versus University of Phoenix in 2006 points to the federal funds received by the University in form of student aid. The University might have been ineligible because of the non-compliance with the certain federal laws and regulations. The case is being developed on the ground of the False Claims Act and anticipates possible fraud in state-university relations. Chapman University received federal funds in form of student aid, but might

have been ineligible as well. The major challenge in the case considered in 2006 was the instruction time necessary to receive credit hours. As a result, students might have been defrauded because of the insufficient instruction time and the state was defrauded as well.

Possible corruption takes place in student-university relations and in state-university relations. The State of New York Attorney General launched an investigation in 2007 to discover some doubtful practices with lists of preferred providers of student loans, administered by colleges' financial aid officers. The case points to possible attempts to establish near-monopoly and to defraud students on the local markets of educational loans. The case involves state-university relations and student-university relations. The government conducted the investigation on the basis of students being defrauded and guided to more expensive loans by college administrators.

Cases built on the ground of anti-trust regulation have been considered before. One of the major cases that attempted to establish possible corruption in admissions involved MIT and a number of other Ivy League colleges in 1990. The colleges were making agreements prior to admitting graduate students in order to reduce the total cost of the offerings in form of scholarships and financial aid. This implies monopoly in admissions, collusion, and consumer fraud. The colleges admitted wrongdoing and stopped the practice, while MIT won on appeal, pointing to its non-profit status. Another broadly publicized case of 1985 involved Stanford University and later few other colleges. The major consideration here was overhead payments of up to 74 cents on every \$1 received in form of federal grants as well as the ways in which some of the federal research money were spent.²⁰ The case implied possible fraud in state-university

²⁰ Anderson, Martin. (1992). *Impostors in the Temple: American Intellectuals Are Destroying Our Universities and Cheating Our Students of Their Future*. New York: Simon and Schuster.

relations. It is within the Attorney General's purview to prosecute cases that imply monopolistic agreements.²¹

A number of cases involving diploma mills included state-university relations, consumer-university relations, and degree holder-employer relations. Cases of educational quality fraud involve consumers or students, providers or colleges, and accreditation agencies. Research fraud involves the state as the major source of funding, while the medical fraud committed in university hospitals involves patients and insurance companies.

The cases of corruption in higher education selected for this study include the most recent developments in college funding, including ties between colleges and the educational loans industry. The investigation was initiated by the Attorney General of the State of New York Mr. Cuomo and followed by another twenty seven states throughout the country. Two other cases based on the False Claims Act include a for-profit educational institution based in California that was accused by the state of defrauding its students, playing on the mismatch between students' financial aid and academic abilities and the case with the University of Phoenix. In the first case, there was a settlement achieved and the university ultimately agreed to a settlement of \$6.5 million in restitutions, penalties, fines, and compensatory payments, while the second case is still under review.

The recent scandals of university financial aid officers, preferred educational loan providers list, and possible kickbacks were highlighted in several issues of *The Chronicle of Higher Education* in April-August 2007, can be analyzed through the proposed classification

²¹ The attorney general had power to prosecute for offences committed as part of the means, plan, or scheme by which violations of §340, prohibiting monopolies were effected, and any criminal act done in furtherance of a violation of such section was subject to investigation and prosecution by the attorney general. *People v. Dorsey*, 1941, 176 Misc. 932, 29 N.Y.S.2d 637. *McKinney's Consolidated Laws of New York Annotated*. Book 19. General Business Law. Thomson West. 2004. p. 318.

frame. This will help to understand whether the cases represent corruption of higher education and what is in the essence of each case. In cases investigated by the State Attorney General Mr. Cuomo, financial aid officers suggested a particular private bank-lender to students. The bank may not have the best offerings for the students and would be ruled out otherwise. The non-competitive bank loan offers attract clients. This may constitute fraud. And fraud is a phenomenon of corruption. The next question is whether this is an intentional fraud or it is a result of negligence or incompetence.

Intentional fraud takes place if financial aid officers commit it in expectation of personal or material gain. Material gain can come through holding shares in the bank placed on the preferred loans provider list and through receiving kickbacks in the form of consultation fees, gifts, etc. Accordingly, the means of corruption are kickbacks. Banks might pay kickbacks deceptively worded as “referral affiliate benefit packages” to colleges’ financial aid officers in the form of gifts, meals, accommodations, consulting fees, travel expenses, registration fees, tuition waivers, and shares of the lending agencies. Being on the preference lender list increases the profitability of the bank, the profitability of the shares, and, hence, the revenue of the shareholders. Such practices raise several questions: Does this represent clear conflict of interest? Is this illegal? Is this against the university rules? Are such practices transparent? What rules are established and by whom?

The locus of corrupt activities in this case includes access to higher education and possible breach of contract. The area primarily affected is access to higher education since loans are intended to fund the studies. Educational loans provided on non-competitive ground or not the best possible terms and conditions reduce the degree of accessibility of higher education, increase student debt, and eventually lead to the withdrawal of more competitive providers from

the market. The practice of having a list of preferential loan providers may also constitute a breach of contract between the student and the university. This is only possible if universities are under the obligation to provide their current and prospective students with the best possible options in terms of educational loans, both private and public.

The possibly corrupt interactions in the presented case include: business-university relations with possible collusion between banks-providers of educational loans and universities or admissions officers; relations between students and college administration, where administrators commit possible fraud by presenting students with the preferred lenders list; and, finally, interactions between the state and higher education institutions, including the investigation conducted and out-of-court settlements achieved, as well as restitutions and voluntary acceptance of the code of conduct set by the state for the future.

Legal argumentation

Definitions of bribery are arguable. One of the issues that may be raised in connection with alleged kickbacks to particular college financial aid officers may be loans and tuition waivers that they received from for-profit providers of educational loans. People versus Hyde case of 1913 in the State of New York dismissed the charges of corruption on the ground that the fact of obtaining a loan itself does not constitute corruption unless the direct benefit to the loan receiver is proven.²²

²² “In order to constitute bribery within the meaning of former Penal Law 1909, §372 [now this section], it must be shown that the officer received some personal advantage, pecuniary or otherwise, that influenced his action or decision, and the fact that a city chamberlain received a loan in consideration for depositing moneys of the city in a certain bank does not constitute bribery in the absence of proof that the loan was in fact an advantage to him.” People v. Hyde (1 dept. 1913) 156 A.D. 618, 141 N.Y.S. 1089. McKinney’s Consolidated Laws of New York

The definitions of bribery are structured so to address donor and recipient issues or, as they are called in legal documents, bribe receivers and bribe givers. Bribe giving and bribe receiving can be of first, second, and third degree and constitute three different classes of felonies, accordingly. As related to bribe giver, §200.00 of the Consolidated Laws of New York states that “A person is guilty in the third degree when he confers, or offers or agrees to confer, any benefit upon a public servant upon an agreement or understanding that such public servant’s vote, opinion, judgment, action, decision or exercise of discretion as a public servant will thereby be influenced.”²³ As related to bribe receiver, §200.10 states that “A public servant is guilty of bribe receiving in the third degree when he solicits, accepts or agrees to accept any benefit from another person upon an agreement or understanding that his vote, opinion, judgment, action, decision or exercise of discretion as a public servant will thereby be influenced.”²⁴ There are also such terms as rewarding official misconduct and receiving reward for official misconduct and giving and receiving unlawful gratuities.

Bribes do not have to be in monetary form, but can be present in any form possible that conveys the benefit to bribe receiver. In *People versus Hochberg* case of 1978 it was established that “Benefit accruing to public official need not be tangible or monetary to constitute a ‘bribe’ .”²⁵ Sex can also be considered as a form of a bribe. *People versus Teitelbaum* court case of 1988 points to a clear case of corruption of government officials with sexual services being

Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999, p. 278.

²³ McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999. p. 259. Article 200. Bribery involving public servants and related offences, p. 267.

²⁴ Ibid, p. 275.

²⁵ *People v. Hochberg* (3 dept 1978) 62 A.D.2d 239, 404 N.Y.S.2d 161, McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999, p. 271.

used as a bribe: “Evidence that police officers had told narcotics offender that everything would be alright if she accompanied officers to apartment, and that offender had subsequently performed oral sex on officers, was sufficient to support officers’ conviction for bribe receiving in second [now third] degree.”²⁶

The scope of authority does not limit the responsibility for bribery.²⁷ Bribe giving anticipates a clear expectation that the public officer, i.e. bribe receiver or recipient retains the authority to help the donor to cross the red tape, i.e. overcome the restrictions set by the law or by the public officer himself/herself. It does not matter whether the public servant actually has a power or authority to meet the expectations of the donor and to match his/her demands in full. People versus Graham case of 1977 points out that the public official is “assumed to have power” by the bribe giver.²⁸

Agreement or mutual understanding is an essential characteristic of a corrupt transaction. The expectation of crossing the red tape should be present at least on the side of the bribe giver. People versus Tran case of 1992 found that “‘Agreement or understanding’ is the key element of the bribery statutes. The ‘agreement’ between the bribe giver and the bribe receiver must be mutual. Alternatively, the ‘understanding’ must be at least a unilateral ‘perception or belief’ in the mind of the bribe giver that the bribe ‘will’ influence the receiver’s conduct. If the bribe giver

²⁶ People v. Teitelbaum (2 Dept. 1988) 138 A.D.2d 647, 526 N.Y.S.2d 230. McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999, p. 279.

²⁷ “It is sufficient to justify conviction for bribery if officer to whom bribe was offered assumed under color of his office to perform function belonging to his office, even if right to perform function did not exist. People v. Chapman, 1963, 13 N.Y.2d 97, 242 N.Y.S.2d 200, 192 N.E.2d 160. McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999, p. 271.

²⁸ “‘Bribery’ is offering to public servant benefit to induce him to act or refrain from acting in matter over which he may be assumed to have power. People v. Graham (4 dept. 1977) 57A.D.2d 478, 394 N.Y.S.2d 982, affirmed 44 N.Y.2d 768, 406 N.Y.S.2d 36, 377 N.E.2d 480. p. 269.

offers or confers a benefit with only the intent that the bribe receiver's conduct be influenced thereby, or with only a 'mere hope' that the receiver's conduct would be influenced thereby, the crime of bribery is not committed."²⁹

Bribe giver or donor is not necessarily the initiator of a corrupt transaction. Extortion is another form of corruption that takes place when a public officer in charge demands a bribe from a potential donor in exchange for the officer's action or inaction in favor of the donor. Coercive power is usually used by the public servant in order to extort a bribe. The fact of extortion does not substitute for bribery, because extortion results in bribe. According to the Consolidated Laws of New York, "It is expressly made no defense to bribe receiving that the defendant was extorting or coercing a bribe and could therefore be guilty only of extortion or coercion, not bribe receiving [§200.15]."³⁰

In case of extortion, the donor is protected from the legal responsibilities that would normally apply to a bribe giver in a typical case of bribery. The special provision was introduced for such a protection, because in the case of extortion the donor is considered a victim of corruption rather than an accomplice. The Penal Law in New York State holds the donor harmless on the ground that he/she is a victim of coercion or extortion.³¹

²⁹ People v. Tran, 1992, 80 N.Y.2d 170. p. 260

³⁰ McKinney's Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999. Article 200, §200.05. Bribery involving public servants and related offences, p. 264.

³¹ "Upon the declaration that bribe receiving and extortion were not mutually exclusive crimes, the bribe giver who was the victim of extortion would no longer be able to defend on that basis. This, out of arguable 'equitable considerations' [compare Model Penal Code §240.1], a special defense to bribery was formulated which in essence held the giver harmless if the giver gave in response to extortion or coercion [§200.05]." Staff Comments of the Commission on revision of the Penal Law. Revised Penal Law. McKinney's Spec. Pamph, (1965), p. 291.

Corruption is not limited to bribery involving public servants and related offences. Legislation outlines yet another type of bribery, commercial bribery.³² Commercial bribery anticipates damage to employer. This makes commercial bribery a classical case of the principal-agent problem. Accordingly, numerous theoretical developments within the principal agent frame, made in economics and political science, may be applied to commercial bribery. The point we want to make in this paper is that the legal concept of bribery extends beyond the notion of public officer, i.e. that the employee who betrays his/her principal does not have to be a public employee. Accordingly, the state does not have to be involved. Involvement of the state through the state representatives is no longer a necessary precondition for the case to be considered within the realm of bribery and corruption.

The essence of bribery is in the intent to influence conduct of someone in charge of certain functions, duties, or responsibilities. In case of corrupt public official, the abuse is of the public, since the official represents interests of the public. But not all states or political regimes represent best interests of the public. Therefore, corruption is not limited to public officials or public sector. According to Consolidated Laws of New York, “The essence of bribery ... is in the ‘intent’ to influence improperly the conduct of another by bestowing a benefit, and the essence of bribe receiving is in the ‘agreement or understanding’ that the recipient’s conduct will be influenced by the benefit.”³³ This definition does not imply the participation of a public official or a public servant. Nor it implies any involvement of the state.

³² McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999. Commercial bribery, p. 122.

³³ McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999. Commercial bribery, p. 122.

Commercial bribery can be of two degrees. If the case of bribery was at the stage of intent or agreement, then it would qualify as a commercial bribery of second degree. If, however, the transaction itself would take place and there would be clear damage to the interest of the principal resulting out of such transaction, then commercial bribery would qualify as first degree. The Statutes of New York set a total benefit benchmark of \$1000 for the benefit to participating parties in a corrupt transaction and a damage of \$250 to the principal, betrayed by his/her agent.³⁴

Higher Education Act of 1965 regulates the sphere of educational loans in the US. However, some issues of consumer rights protection as well as state and federal jurisdictions are still not clear. Parents can borrow a PLUS Loan to cover education expenses for dependent undergraduate students enrolled at least half time in an eligible program at an eligible school. PLUS Loans are available through the Federal Family Education Loan (FFEL) Program and the William D. Ford Federal Direct Loan Program. Eligibility of a student anticipates high school diploma, eligibility of parents anticipates good credit, and eligibility of the program and the college anticipates accreditation. Conditionality is attached to all governmental educational loans and certain conditions apply to all the participants of this type of contract or transaction. At the same time colleges may be found under no responsibility to provide quality educational services to students and hence students can not return their payments made out of state loans, if no federal

³⁴ “If the value of the benefit exceeds \$1000, and as a consequence of the bribing or bribe receiving there is economic harm to the employer or principal in excess of \$250, the crimes are aggravated to commercial bribing in the first degree.” McKinney’s Consolidated Laws of New York Annotated with Practice Commentaries by William C. Donnito. Book 39. §170.00 to 219.end. West Group, 1999. Commercial bribery, p. 123.

loans are involved.³⁵ Student loans, made, issued, or guaranteed, under Higher Education Act are also exempt from federal trade Commission rule on preservation of consumer defenses.³⁶

The issue of educational loans and all the abuse associated with it extends beyond interactions between students and colleges, since colleges themselves do not hold student loans. The decision made in *Veal versus First American Savings Bank* states that “Rule that assignee who is not holder in due course takes instrument subject to defenses against assignor existing at time of assignment could not be used to charge lenders who granted guaranteed student loans with alleged fraudulent activities of insolvent business college, since college was never “holder” of student notes and lenders were never assignees of college.”³⁷ This provision points to the need to better educate consumers about educational and affiliated financial services. Consumers of educational services must be aware of quality, accreditation level, terms and conditions of educational loans, etc.

³⁵ C.A.7(Ind.) 1990. Students could not seek rescission of student loans guaranteed by state and private agencies on theory that, because of close connection between solvent business college and lenders and other defendants, defendants were subject to defense based upon college’s failure to provide student with education; since loans were guaranteed by private and state agencies, rather than federal government, they were not subject to protections of federal regulations, under which defense might be available in cases involving Federal Insured Student Loans and federal PLUS loans. Higher Education Act of 1965, §401 et seq., as amended, 20 U.S.C.A. §1070 et seq. *Veal vs. First American Savings Bank*, 914 F.2d 909, rehearing denied. Source: West’s Federal Practice Digest 4th, 18B, Colleges and Universities, St. Paul, MN: West Group, 1999, p. 9.25(2)

³⁶ Student loans, made, issued, or guaranteed, under Higher Education Act are exempt from federal trade Commission rule on preservation of consumer defenses, under which consumer credit contracts must advise holders of such contracts that they are subject to all claims and defenses that debtor has against seller of goods and services. Consumer Credit Protection Act, §104(6), as amended, U.S.C.A. §1603(6). *Veal vs. First American Savings Bank*, 914 F.2d 909, rehearing denied. Source: West’s Federal Practice Digest 4th, 18B, Colleges and Universities, St. Paul, MN: West Group, 1999, p. 9.25(2)

³⁷ Higher Education Act of 1965, §401 et seq., as amended, 20 U.S.C.A. §1070 et seq.; West’s A.I.C. §26-1-3-306. *Veal vs. First American Savings Bank*, 914 F.2d 909, rehearing denied. Source: West’s Federal Practice Digest 4th, 18B, Colleges and Universities, St. Paul, MN: West Group, 1999, p. 9.25(2)

Cuomo investigations of educational loans and study abroad programs are based on the provision that deceptive acts and practices are unlawful under the Consumer and Borrower Protection Act. As stated in the New York State legislation, “Deceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service in this state are hereby declared unlawful.”³⁸ In case of private educational loans, the consumer and borrower protection considers borrower as a consumer of financial services. This requires transparency and full disclosure of the terms and conditions under which the loan is furnished to the student and served by the student.

According to the Consumer Protection Act, “The essential elements of a violation of New York law prohibiting deceptive acts or practices in the conduct of any business, trade, or commerce or in the furnishing of any service in New York are: (1) proof that a “consumer-oriented” practice was deceptive or misleading in a material respect, and (2) proof that plaintiffs were injured thereby.”³⁹ But there is a safe harbor for lenders and college financial aid officers that may be found in the state legislation. Specifically, the court does not accept claims about deceptive practices when such practices were fully disclosed to the consumer.⁴⁰

The excursion into the legal definitions and peculiarities leaves many questions unanswered. For instance, both coercion and extortion are considered in legislation. However,

³⁸ Article 22-A. Consumer protection from deceptive acts and practices. §349. McKinney’s Consolidated Laws of New York Annotated. Book 19. General Business Law. Thomson West. 2004. p. 320.

³⁹ *Champion Home Builders Co. v. ADT Sec. Services, Inc.*, 2001, 179 F. Supp.2d 16, as amended. 10. Elements of action, generally. §349. Consumer protection, McKinney’s Consolidated Laws of New York Annotated. Book 19. General Business Law. Thomson West. 2004. p. 333.

⁴⁰ “There can be no claim for deceptive acts or practices when the allegedly deceptive practice was fully disclosed.” *Broder v. MBNA Corp.* (1 Dept. 2001) 281 A.D.2d 369, 722 N.Y.S.2d 524. 11. Deceptive acts, generally. §349. Consumer protection, McKinney’s Consolidated Laws of New York Annotated. Book 19. General Business Law. Thomson West. 2004. p. 335.

the bribe giver in such cases is considered a victim. But what about public employees and elected officials who are coerced by their supervisors to solicit bribes and accept bribes? This anticipates the corruption and coercion policy as a mechanism of administrative control. And what about complex systems? The entire legal frame appears to be quite simplistic.

Legal provisions that exist in the legislation, including Higher Education Act, False Claims Act, and Consumer Protection Act and are presented in this paper cover all the three areas: 1) corruption as related to the state (private individual bribes public official in order to obtain unduly benefits); 2) corruption as related to client and business (a client (subcontractor etc.) is abusing a business by bribing business' agent); and corruption as related to consumer and business (consumer fraud, when business deceives consumer). However, the legal frame is simplistic, while the system of interrelations in the higher education industry is rather complex.

Implications

Kaye, Bickel, and Birtwistle (2006) point out that “There is widespread concern that higher education is being compromised by being turned into a ‘commodity’ to be ‘consumed’.” The authors attempt to explore the trends in both the UK and US, and consider how the law has responded to them. They argue that “there is an important distinction to be drawn between ‘commodification’ and ‘consumerism’. Education has always been a commodity to be bought and sold; the true danger lies in the move to a ‘rights-based’ culture where students (and politicians) see education merely as something to be ‘consumed’ rather than as an activity in which to participate. Whilst the law seems thus far to have been something of a bulwark against this movement, it remains an open question as to whether this will continue to be the case if

HEIs do not themselves act more proactively in challenging this damaging view of higher education.” (Kaye, Bickel, and Birtwistle, 2006)

One can argue about the extent of consumerist approach in higher education across the nations, but the trend of presenting the higher education sector as a provider of educational services is obvious. The market mechanisms that are being introduced on an increased scale in higher education do not free the industry from corruption, including bribery and different other forms of misconduct. The equilibrium of supply and demand with consumers voting with their dollars for best possible choices do not necessarily lead to the elimination of public sector based corruption. Different forms of corruption exist in private sector as well. The legal definitions presented earlier explain why the range of investigations launched by the New York State Attorney General is under the auspices of consumer protection and fraud rather than corruption and bribery.

The case may necessitate development of certain measures, tools, and even institutions, such as the Consumer Education Fund established by the Attorney General of New York, as well as changes in legislation, designed to prevent doubtful practices in the future. Provision of private educational loans is a growing industry in the US. It rose sharply from \$1.7 billion in 1996 to \$17 billion in 2006 and is expected to grow continuously and rapidly in the future. Similar developments may take place in other nations in the future. The process of transferring education financing to private educational loans represents the major trend in the higher education funding and may soon be borrowed and adopted in other countries. Subsequently, legislative regulations and changes in the legislation are necessary as well as provisions in the university’s code of conduct not only in the US, but in many other nations.

The classification also points to some possible theoretical developments. The core of the

problem as related to corruption is in an intentional restriction of students' access to reliable information about the available educational loans. This implies imperfect information, imperfect competition between the educational lenders, and a certain degree of monopolization of the market of educational loans and eventually brings into fore the antitrust law.

The Cuomo cases in higher education are clearly not those of subprime loans and predatory lending, yet. However, this may well be the case in the future. The Consumer Education Fund, established by Mr. Cuomo, is primarily focused on educating constituents on predatory lending issues. There is a legacy to this issue as well. In 2000, then HUD Secretary Mr. Cuomo joined forces with Treasury Secretary Lawrence Summers, former President of Harvard University to form the national predatory Lending Task Force. Investigations in inappropriate lending patterns in higher education are not a surprise but rather a natural development. The investigations of misdeeds in educational loans touch upon broader financial aid issues and then naturally develop into investigations in possible abuses in study abroad programs. The investigations may eventually address all the areas where consumer fraud in higher education has a potential or already takes place.

Colleges use practices of hidden fees and bundling products and services. Even if predatory lending and consumer deception do not fall under the corruption and bribery provisions, kickbacks do. Kickbacks are bribes that are promised in advance and clearly anticipate expectations on the side of the bribe giver. At the same time they are paid *post factum* and present certain guarantees to the donor. As the educational loan industry grows, so are the

opportunities for abuse. This situation and what appears to be a long term trend in the education industry can no longer be ignored by the authorities.⁴¹

Higher education loans constitute an \$85 billion per year industry, as rightly mentioned by the Attorney General in multiple legal documents. The sum itself is not big, but the industry is growing rapidly.⁴² According to the New York State Department of Education, two-thirds of all four year college graduates nationwide now have loan debt, compared with less than one-third of graduates in 1993. In New York State, 59 percent of undergraduates took out loans to finance their college education. The average student graduating from a four-year college in New York owes \$17,594 on graduation day.⁴³

Lastly, the results of the investigations and intentions to sue point to the practice of what one would define as “admitting without admitting,” when colleges and private providers of educational loans *de facto* admit the wrongdoing or misconduct, but *de jure* regarded as not guilty. Both the higher education institutions and the providers of educational loans that are under investigation agree to stop their doubtful practices, sign the Code of Conduct offered by the Attorney General, and even contribute to the Consumer Education Fund, set by the Attorney General. This “voluntary” contribution, made by for-profit enterprises, along with the refusal to admit any wrongdoing prevents from establishing a true court based legal precedent. At the same

⁴¹ “EFP aggressively offered schools cash kickbacks in exchange for business,” Cuomo said. “This kickback scheme was widespread and took place from coast to coast, at colleges large and small, public and private. This lawsuit is just the beginning of an investigation that will show that lenders put market share above fair play. A preferred lender ought to mean that the lender is preferred by students for its low rates, not by schools for its kickbacks. With the cost of college rising every day, the last thing students want to hear is that their lender may be muscling aside a more competitive loan package.” Attorney General Andrew Cuomo announces first legal action in college loan industry investigation (March 22, 2007). Retrieved from http://www.oag.state.ny.us/press/2007/mar/mar22b_07.html

⁴² Retrieved January 31, 2008, from http://www.oag.state.ny.us/family/student_lending/student_lending.html

⁴³ Retrieved from http://www.oag.state.ny.us/press/2007/mar/mar22b_07.html

time, such half-victories achieved through bargaining and negotiations work as political dividends for Mr. Cuomo, who is an elected official.

The situation reminds a forceful offensive campaign of the state on the free enterprises with the demand for money. As follows from one of the settlements: “In recognition of the Attorney General’s leadership in improving the circumstances under which education financing is made available to college students and consistent with Sallie Mae’s commitment to educating the public about the financial aid process, Sallie Mae agrees to donate \$2 million to the New York Attorney General’s national fund for educating high school seniors and their parents regarding the financial aid process.”⁴⁴ The offensive campaign of the state is met with the traditional defensiveness of higher education institutions, in which the tradition of denial of any wrongdoing is certainly at least as strong as willingness to revise and change current institutional policies.

Conclusion

The importance of the study of court cases on corruption in US higher education is threefold. First, court cases present additional lenses to study definitions and aspects of corruption in higher education that do not exist in other systems. Second, the national system of higher education with its mixture of public and private, non-profit and for-profit higher education is undergoing process of evolutionary changes that vary from state to state. The forms of corruption develop and change accordingly. Third, the US higher education shows pathways for reforms in numerous other national educational systems. Many national systems of higher education, including those of the former Soviet Bloc, undergo major changes and reforms

⁴⁴ The report on the Settlement with Sallie Mae, April 11, 2007. Retrieved January 31, 2008, from http://www.oag.state.ny.us/family/student_lending/student_lending.html

moving toward the market-based systems that in many ways replicate higher education industry that exists in the US. Accordingly, forms of corruption that are currently present in the US education will eventually develop in the transition educational systems as well. Learning about the forms and mechanism through which corruption in US higher education perpetuates will help in predicting corruption in other national educational systems.

Those few works that address corruption in higher education focus entirely on the issue of access, including such aspects as admission, retention, and affordability. The issue of quality, not least fundamental, is still missing from the research on corruption in education. The legal frame offered in this paper and applied in investigations of allegedly corrupt activities on the side of educational institutions allows for addressing both issues: access and quality. The selection of cases and their analysis point to problems in both the access and the quality of higher education as well as the ways in which legislation and the judiciary may be used in such cases.

The processes of decentralization, marketization, commoditization, and privatization in higher education rise questions of accountability, transparency, quality, and access. Decentralized financing of higher education anticipates cost sharing based in part on educational loans. The decentralized US higher education that long been considered an exception among other developed nations now turns into a sector from which inferences are to be drawn. This anticipates spillovers of the problems, but not the solutions. Forms of corruption that long existed in the US education sector, including those in quality assurance through accreditation, compliance with state and federal laws, and provision of educational loans now have a perspective to develop in other educational systems as well.

The law and the legislative process in general is central not only to the way the US system is organized, but also to the way it operates and resolves current problems. This fully

applies to US higher education. If an individual or an institution wants to resolve a certain problem, the solution may be found primarily within the court system. The judge is to decide and the decision is to be made based on laws. National systems of higher education in other countries can be characterized as centralized systems with states often playing dominating role in most of the issues. Accordingly, the decisive power belongs to the executive branch, including the Ministry of education and other ministries that impose numerous regulations and restrictions, impose sanctions, and resolve current problems. If a higher education institution does not comply with certain rules and provisions and students' or state interest are compromised, the institution may well be placed on probation or closed, and the leaders of this institution may be reprimanded or replaced. The so-called administrative resource plays a key role in decision making and dispute resolution. Hence, while the problems faced by the US higher education industry and national education industries in other countries may be common, the solutions will have to be found in different areas. This statement explains why the essence of legal cases is important.

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Appendix A

Notice of Intention to Sue (Letter)

Dear Ms. Briones:

You are hereby notified that the Attorney General intends to commence litigation against Education Finance Partners (“EFP”) pursuant to Executive Law Section 63(12) and Article 22-A of the General Business Law (“GBL”), Sections 349 and 350, to enjoin unlawful and deceptive acts and practices in which EFP has engaged and continues to engage, and to obtain injunctive relief, restitution, damages, and such other relief as the Court may deem just and proper.

The unlawful and deceptive acts and practices complained of arise out of EFP’s student loan business. EFP has repeatedly and persistently offered to make payments, and has in fact made payments, to colleges, universities, and vocational schools (“Schools”) in exchange for those Schools (a) steering students to EFP loan products, and (b) placing EFP on the Schools’ “preferred lender” lists. Among the Schools with which EFP has had such revenue sharing agreements are: Baylor University, Boston University, Clemson University, Drexel University, Duquesne University, Fordham University, Long Island University, Pepperdine University - Graziado School of Business, St. John’s University, Texas Christian University, Washington University in St. Louis, and the University of Mississippi. In total, EFP has or has had such agreements with more than 60 schools across the nation.

The agreements entered into by EFP require the Schools to promote EFP to its students as a “preferred private loan provider via the school’s website, printed lender list, mailings, and other marketing opportunities to both first-time and serial borrowers who are candidates for a

private loan.” In return, the agreements require EFP to pay back to the school a percentage of the net value of the loans referred by each school. For example, EFP’s agreement with Duquesne University provides that the school will receive 60 basis points (.6%) of the net value of all referred loans. Some of the agreements are “tiered” so as to provide increasing financial incentives for the schools as more students take loans from EFP. EFP’s agreement with Boston University, for example, provides that the school will receive 25 basis points (.25%) of the net value of referred loans of at least \$1,000,000 up to \$5,000,000; 50 basis points (.5%) of the net value of referred loans between \$5,000,000 and \$10,000,000; and 75 basis points (.75%) of the net value of referred loans over \$10,000,000. In at least one instance (Drexel University), the agreement provides for EFP to be the exclusive preferred lender, resulting in the school’s pushing its students towards EFP and EFP alone. Thus, Drexel’s agreement with EFP, dated April 1, 2006, provides that Drexel has agreed to make EFP its “sole preferred private loan provider,” in consideration for which EFP has agreed that Drexel will receive 75 basis points (.75%) of the net value of referred loans between \$1 and \$24,999,999; and 100 basis point (1%) of all loan amounts of \$25,000,000 or greater.

Such steering and placement on the preferred lender lists occurred without disclosure to the student borrowers and their parents of the payments and offers to pay, and had the potential to mislead the student borrowers and their parents. The arrangement created unlawful conflicts of interest on the part of the Schools. To avoid these inherent conflicts of interest, EFP must sever its financial ties with the Schools to whose students it makes loans. It must compete for the students' loans by offering the best loan products to students, not the best kickbacks to the Schools.

EFP has also repeatedly and persistently engaged in misleading and deceptive business practices and false advertising by falsely representing, directly and by implication, that Schools endorse EFP's loan products and recommend those products for individual student borrowers. Specifically, EFP has (i) used Schools' names, logos, colors, and mascots in EFP's correspondence and on EFP's web-based promotional materials, creating the false impression that the Schools have endorsed EFP's products, and (ii) provided Schools with EFP promotional materials for insertion into the Schools' financial aid award packages and tuition cost of attendance bills, again creating the false impression that the Schools have endorsed EFP's products.

Retrieved May 21, 2007,
from <http://www.oag.state.ny.us/press/2007/mar/EFP%20Final%20Letter.pdf>