Franchising: An adequate Business Model for the “Proactive University”? A Public-Private Perspective on German HE

Britta Leusing

Currículo: estudia el doctorado en International Management en la University of Flensburg (Germany) y en la University of Southern Denmark. Consultora en temas educativos y de administración de la educación superior, con especialidad en impactos económicos en las regiones, acceso a la educación superior de los “estudiantes no tradicionales” y alianzas estratégicas entre instituciones públicas y privadas.

Resumen
Las instituciones de educación superior (IES) públicas están experimentando cambios en virtud de las crecientes presiones financieras, la autonomía y la diversidad de actores en un “mercado” que impone grandes retos. Estos cambios han conducido a que las IES adquieran formas empresariales, como la concesión de franquicias o licencias, que han alcanzado relevancia en el contexto de internacionalización y en la difusión de programas de estudio. Durante la década anterior, este fenómeno creció en Alemania, donde las universidades públicas empezaron a vender franquicias a instituciones de educación superior privadas y no reconocidas por el Estado. Esta situación es de especial interés porque el sistema de educación superior alemán es, tradicionalmente, estatal y concibe la universidad como una institución de prestigio y sólida.

Abstract
Public higher education institutions (HEIs) are experiencing circumstantial changes due to increasing financial pressure, higher autonomy and diversified actors on an increasingly challenging “market”. These changes have led to forms of “entrepreneurial behavior” in public HEIs, such as franchising arrangements, which have become prominent in the context of internationalization and the export of study programs. Over the last decade, a growing number of franchising arrangements on an intrastate level can be observed between public universities as franchisors and private, non-state recognized HEIs as franchisees in the German HE sector. The German situation is of special interest because the HE system is traditionally state-run and emphasizes the university as a prestige and sound institution. Students pay almost no tuition fees for a public university degree except those students enrolled in a franchise model, where the fees are about 9 times higher. Special organizational structures like intermediary stock companies and either the lack of or not commonly interpreted regulatory instruments lead to critical discussions of these models. The most crucial assumptions are that financial motives dominate decision making rather than pedagogical considerations and that public services are exploited to mask the interests of individuals. Although these presumptions cannot be rejected through the empirical results of case study analyses, the opportunities of such strategic alliances are not to be underestimated. With adequate external and internal quality assurance mechanisms, franchising models can be used to strengthen the market position of public universities through a higher number of students and an extended portfolio

1 The research topic of this paper is examined in a dissertation which is not finished yet.
of products and services. Additionally, HE programs can be offered more flexibly in regions with minimal HE infrastructure and/or with programs particularly designed for “non-traditional students”.


**INTRODUCTION**

Higher education institutions (HEIs) are experiencing circumstantial changes due to external pressures (financial challenges), institutional changes (higher autonomy) and diversified actors (non-profit, for-profit, not-for-profit). These changes create new strategic possibilities for the public university to succeed in the increasingly challenging higher education (HE) market. In this changing HE environment it is important to study the impact of external conditions on the behavior of HEIs in order to identify those conditions under which HEIs are best able to ensure quality, efficiency and accessibility (Enders & Jongbloed, 2007).

In this study, franchises of HE programs are to be investigated to examine opportunities that public universities have to react (better “proact”) strategically to market changes and thus become more proactive and entrepreneurial institutions. Additionally, the necessity of quality assurance mechanisms is to be discussed. Since franchising in HE has become more prominent in the context of internationalization and the export of study programs, the investigation concentrates on the “phenomenon” of HE franchises in Germany, especially between public universities as franchisors and private, non-state recognized HEIs as franchisees. The discussion of the risks and opportunities of these models will be empirically accompanied by case study analysis.

The public-private franchise model in German HE is legitimately declared as a “phenomenon”. Since the middle ages, Germany has run a HE system which is publicly organized and emphasizes the university as a prestige and sound institution. It is the state that has a traditional monopoly in HEIs. About 95% of students are enrolled in state HEIs and pay almost no tuition fees. Since World War II, however, especially in the last three decades, the number of private, state-recognized HEIs, as well as their share of enrolled students, has grown enormously. A market for private study programs with “consumers” willing to pay high tuition fees seems to have evolved. Besides state-recognized institutions, another form of private actors is competing on the HE market: non state-recognized providers offer tertiary education services without degree awarding power. The increasing demand of the students for state-recognized study degrees forces these institutions either to invest in getting a university status or to co-operate with public or state-recognized institutions e.g. via franchising - the less risky and less cost-intensive alternative. One of the delicate issues of this public-private arrangement is the fact that the students enrolled in these models pay tuition fees to a private institution for a public university degree. These fees can be about 9 times higher than for those students directly enrollment at public universities.
FRANCHISING AS A BUSINESS MODEL IN HE
Franchising in HE can be described as an arrangement between HEIs in which the franchisee acquires the right to subsume an academic program of the franchisor institution within a portfolio under its own name (Yorke, 1993, p. 167). In general, the courses are designed and developed in the franchisor HEI and delivered in the franchisee institution. The fundamental responsibility for quality assurance lies with the franchisor HEI. The franchisee employs the staff, makes resources available, and is responsible for the day-to-day administration of the courses (Robinson & Hammersley-Fletcher, 2006, p. 21).

Since the model is implemented in order to create additional financial sources, it is discussed very critically (Cavanaugh & Cavanaugh, 2006, p. B20; Woodrow, 1993, pp. 207-220). The most crucial issue in franchising models is that financial motives dominate rather than pedagogical considerations and that public services are exploited to mask the interests of individuals. Critics mistrust the equivalence and quality assurance in teaching and learning and sometimes disparage HE franchising as “McDonaldization” (Hayes & Wynyard, 2002). While talking about “McEducation” it is asked if it is “really higher education when it is delivered in that franchised way” (Milton cited from Strosnider, 1997).

HE franchising in the international context
The franchise model is generally applied in the context of exporting and importing higher education programs all over the world, especially in the USA, the UK and Australia. Internationalization of HE programs began in the 1980s when tuition fees from exchange students became an important financial resource.

Besides students studying in a foreign country (student import), there was a strong growth in the number of foreign students studying on off-shore campuses in their own country (export of study programs). Many of the off-shore campuses are set up by private enterprises on a franchise basis.

In these franchising arrangements a university sub-contracts a local provider in another country to offer selected parts or all of its degree programme (Healy, 2007, p. 334). They are often delivered in a “1 + 2”- or “2 + 1”-structure [the so-called “Twinning-system” (Schreiterer & Witte, 2001, p. 44)]. The franchisee delivers the first phase of the study program with the students completing their degrees as regular students at the franchisor HEI (Healey, 2007, p. 337). Additionally, the programs are often delivered via distance learning modules (Hahn, 2005, p. 23).

Data about the volume of franchise programs of the different countries is rare. For example, in 2004 the British Council estimated 180,000 international students studying for UK university degrees in franchised programs at off-shore campuses outside the UK. This is compared to 270,000 students studying on HE programs on-shore (Healy, 2007, p. 337).

Franchising to widen access to HE for “non-traditional students” in the UK
A long tradition of collaborations between Further Education Colleges (FECs) and HEIs in the UK is still supported through British educational policy agenda which aims at the expansion of HE in further education and a widening participation in HE from those sectors of society previously underrepresented. Especially in the 1980s and the early 1990s, the number of partnerships between the two types of institutions expanded and most of them were organized in a franchise model.
FECs deliver HE degrees on a part-time basis, including evening study programs (Robinson & Hammersley Fletcher, 2003, p. 20). In 2005/06 learners in FECs comprised approximately 11% of all HE learners, including 3% of whom were enrolled in franchised programs (Pye & Legard, 2008, p. 28).

Quality assurance in HE franchising

Quality assurance mechanisms for HE franchising arrangements were developed especially in the context of internationalization of study programs because governments feared the undermining of the reputation of the country’s HE brand. Quality assurance mechanisms are generally discussed on an external level (governmental interventions, guidelines) as well as on an internal level (quality assurance instruments between the franchising HEIs).

Governmental institutions such as funding councils and quality assurance agencies have developed guidelines and evaluation systems explicitly for HE franchise models. Accreditations, institutional reviews or codes of practice are either obligatory or optional. Particularly the latter are more often of a formal than of a content-based character (Schreiterer & Witte, 2001, p. 55).

Accreditation procedures are time-consuming and cost-intensive which leads to a higher degree of specificity of the franchised study program. They will raise the transaction costs associated with a switch to an alternative franchise partner. Argued in a resource dependence perspective accreditation can strengthen the ties between the two partners. In case that the university has the ability to accredit the franchise study program on its own responsibility its power on the franchisee grows (Emerson, 1962; Pfeffer & Salancik, 2003).

Although literature on HE franchise is rare, some studies on quality assurance instruments on the internal level can be found in the context of franchise arrangements between FECs and HEIs in the UK (see paragraph 2.2). Besides governmental approval Yorke (1993) identified some general principles for quality assurance, e. g. the soundness of the franchisee, real and adequate resources at the franchisee institution, and rigorous monitoring and review (Yorke, 1993, p. 178).

In addition, a guide (a guide for those FE Colleges and HE Institutions entering into Partnerships from HEFCE project “A Comparative Study of Leadership Governance and Management Issues of three HE/FE Partnerships”, http://lgm.hud.ac.uk/pdf/HEFCE-Guide3.pdf) for collaborations was developed based on a comparative study of Robinson and Hammersley-Fletcher (2006) about HE/FE partnerships, including franchising arrangements. Referring to quality assurance the authors emphasize to consider the development of handbooks and guidance documents, as well as approval and validation procedures.

HE FRANCHISING IN GERMANY

Environmental changes in German HE determining HE franchise

The German HE sector is traditionally dominated by public universities with a market share defined by the number of students: 95% (public institutions) compared to 4% at private HEIs (church-related universities [1% market share] are to be considered separately from private universities in German HE sector). Since 1980 the number of private universities increased from 10 to more than 90 and the relative as well as the absolute number of students enrolled in private institutions is growing disproportionately while it remains on a constant level in the public HE
sector (German Federal Statistical Office).

Besides the 90 private state-recognized HEIs, several for-profit actors are providing tertiary education services without university status and thus without degree-awarding power. They are offering their own institutional degree or a degree of a public German or foreign university e.g. via franchising. Since there is no official data about these institutions the number is guessed to be about 40 institutions.

The following environmental changes in the German HE sector determine franchising activities between public universities and private HE providers:

- Higher autonomy of public universities
- Increasing need for additional private funding sources
- Procedures of accreditation and state recognition
- Increasing demand and demographic developments
- Changes in demand
- Increasing supply

**Intrastate HE franchising in Germany**

In the German HE sector a few of private and public education providers with or without university-status are delivering study programs in a franchise model. Most of those franchise activities are not communicated transparently which makes a complete survey nearly impossible.

In an international perspective several private providers of tertiary education co-operate in a franchise model particularly with universities from the UK and the Netherlands. The ministries of education of the German federal states acknowledge the equivalency of the study program through a certificate.

Other private providers franchise the study programs of national public universities. One example contains a university of applied sciences which founded a stock corporation as franchisor. Actually eleven private providers are offering its study programs in the fields of health, media and business management for a monthly tuition fee of about 600€ compared to 70€ per semester for those students directly taught by public universities. The franchisees are regionally allocated, most of them in metropolitan, some in smaller, non-metropolitan areas. The students are taught the first 4 semesters at the franchisee institution and the last year they are enrolled at the public university.

Another example is an experienced provider in further education which cooperates with two public universities as franchisors. The provider runs several study centers in metropolitan and non-metropolitan areas, some of them in former East Germany, and offers the universities’ study courses mainly in the field of business management combined with technical disciplines as distance learning programs thus the main target group are employed students.

HE franchise activities and their legitimacy are discussed predominantly in the context of importing study programs from foreign universities (Hailbronner, 2007). In 2008 the Education Minister’s conference (KMK) passed guidelines for the approval of HE franchise. Some HE acts particularly refer to the accreditation of franchised study programs but findings from previous interviews lead to the assumption that either a fully knowledge or a common understanding about HE franchise is missing in governmental institutions and quality agencies.
OPPORTUNITIES OF HE FRANCHISE

Market growth and additional financial resources

The growing market-orientation in HE with a greater autonomy of public universities, the development of strategic goals and the strengthening of the universities’ profile enforce the strategic thinking and management of public universities. HE franchising with private providers might be a flexible opportunity for strategic alliances to increase market shares and to acquire additional financial resources. Based on the product-market growth matrix (Ansoff, 1957) the following chances in HE franchising can be identified:

i) Market development
For the franchisor HEI the alliance can enlarge the pool of potential students available through offering the study programs in new regions. Even in “risky” regions where the demand of students can not be forecasted with high certainty the financial risk for the HEI is limited due to the franchisee’s responsibility for the resources available. Depending on the educational funding system of the federal state the university gets more public funding through a higher number of students enrolled. Additionally the university gets on-going franchise royalties and / or franchising fees.

In the development of study programs economies of scale can be generated by the extended offer of an existing program and the synergetic use of course materials, particularly in the case of distance learning programs (e. g. e-learning platforms and correspondence units).

ii) Market penetration
Strategic alliances between a university and a private HE provider are one way to make organizations grow and to capture a market. Additionally the university can maintain and enhance their regional sphere of influence which strengthens its position face to face with competing HEIs, ministries and enterprises.

iii) Product development
Franchise agreements allow both, the university and the franchisee institution, to extend their portfolio of products and services. Study programs in non-mainstream subjects can be offered without financial risk for the public institution. The common development of a new product can create learning effects for both institutions. Providers of educational services can charge class rooms to capacity particularly via distance learning study programs which include periods of required attendance at the week-end when the building is usually not used.

iv) Diversification
Via franchising the provider of educational services can offer state-recognized study programs. For those who were not yet active on the HE market the study programs allow the acquisition of a new target-group. Additionally the collaboration with a public university can sanitize the image of the private provider.

Market persistence for private HE providers
The private HE provider escapes the cost and time intensive procedure of the state-recognition as university and thus of the institutional and program accreditation. At the same time, it presents the ability to offer state-recognized HE degrees
to react to the changing demand of the prospective students.

Since the Bologna process and the conversion of traditional academic awards to Bachelor’s and Master’s degrees, Germany is running a system of program accreditation which is applied to public and private HEIs. Before the latter receives the university status and thus the degree-awarding power, it has to be institutionally accredited by the German Science Council. Depending on the HE act of the federal state in question, both the accreditation of the programs and of the institution are prerequisites for the state recognition via the Ministry of Education. The costs for both procedures are about 100,000€ (including bureaucratic costs and agency fees) and take approximately 1.5 years. For each additional study program, an amount up to 40,000€ has to be added and the time and costs for the regular re-accreditation procedures (each 5–10 years) are to be calculated as well (Nickel, 2008; Wissenschaftsrat, 2010).

Besides accreditation, several further criteria are to be fulfilled in order to be able to run a state-recognized HEI. This can imply high financial investments: The institution has to offer not just one but multiple study programs, the qualification of the teaching staff must be equal to public universities (full-time professors) and it has to provide a debt guarantee (Darraz et al., 2009).

These aspects show that the costs and risks involved in running a state-recognized HEI are high. But for private providers state-recognized study programs are essential for their portfolio if they wish to remain competitive on the HE market. The tertiary education level gains importance for a professional career and the demand changes not only in a quantitative but also in a qualitative sense. Students are more informed about rankings and accreditations. They also exchange information and experiences / opinions in online forums or create their own websites on which HEIs and their teaching staff are systematically rated.

Especially in the private HE sector, the prospective students have become more sensitive regarding state recognition and accreditations. Private educational providers without degree-awarding power but with high tuitions fees are having difficulties with their image (Fricke, 2006).

**Widening and expanding access to HE**

Through franchising agreements, HE programs can be offered more flexibly in regions with minimal HE infrastructure and / or with programs particularly designed for “non-traditional students” [those usually excluded from HE due to geography, class or culture (e. g. without traditional HE qualification, employed students)]. Experiences in franchising between FECs and HECs in the UK (see paragraph 2.2) leads to the assumption that the access of these target-groups to HE is particularly facilitated as long as providers with a product portfolio including vocational and / or further education are involved as franchisee (Pye & Legard, 2008, p. 6). In Germany almost 80% of interested persons receive access to HEI via the traditional HE entry qualification, the “Abitur” (Nickel & Leusing, 2009, p. 49). Since discussions about a widened access for “non-traditional students” have been (re)started (Nickel & Leusing, 2009) due to the availability of international comparative studies (Schuetze & Slowey, 2000), these franchising arrangements can be considered as an adequate model to recruit adult students with or without traditional HE entry qualifications. They often require special formats of teaching and learning, especially distance learning modules, which allow them to combine study and work.
The co-operation with a vocational or further education institution guarantees a professional orientation, which can optimize the learning environment for these students. Instead of building up new HEIs or integrating special study programs in existing and traditionally run HEIs, the franchising arrangement is an opportunity to build up single study programs closer to “non-traditional students”, especially designed to meet their needs.

**Possible risks of HE franchise**

Mainly based on the principal-agent theory and the transaction cost approach, the possible risks of HE franchising are analyzed via two main determinants of transactions: information asymmetry and opportunism (Williamson, 1985; Richter & Furbotn, 2003). To analyze the behavior of the actors of HE franchise agreements two scenarios are created by way of example derived from the principal agent theory:

*First scenario: Public university as principal, private HEI as agent*

Regarding the university as the principal, which engages in franchise arrangements with private institutions ex ante and ex post agency costs may arise from the conflicting interests between the two partners. While the university is acting in the public interest to expand HE offerings and to generate additional financial resources which are used to improve the quality of teaching and research the franchisee aims at maximizing its individual interest which is profit making. These assumptions may result in adverse selection of the franchisee institution because it is hiding its main characteristics and intentions for the arrangement during and after the contract negotiation. To maximize the profit it acts opportunistically in a sense that it invests less in teaching and quality assurance mechanisms but taking high tuition fees of the student. These risks caused by hidden action and information are difficult and thus cost-intensive for the franchisor to monitor and to avoid. The public university has to fear damaging its reputation. Additional losses through externalities are induced by a bad, and highly paid teaching quality.

*Second scenario: Public university and private HEI as agent, student as principal*

In this case both, the franchisor as well as the franchisee, are counted as one agent, which offers the state-recognized study program and the degree as a common product to the student. Both actors are pursuing individual interest which is profit making. Special organization models (e.g. Stock Corporation) enable single members of the HE franchise (e.g. professors, managers) to generate financial benefits. To maximize the financial outcome the investment in teaching and quality assurance is low (hidden action and information) combined with high tuition fees. Franchisee and franchisor are exploiting the principal trust of students in public universities and their belief in high tuition fees as an indicator for high quality in education (hidden characteristics and intention) (Dotterweich, 2005).

**Discussion: Need for quality assurance and transparency**

In the context of internationalization of HE two main drivers for franchising arrangements can be identified: On the one hand, the fees of foreign students are important financial resources in times of budget cuts from the government. On the other hand, the franchising model has gained in importance to reach new markets abroad or to at least defend existing shares of foreign markets. Franchising univer-
tities are acting strategically and thus entrepreneurially - not surprising e. g. for Australian and American HE sectors in which “for-profit-behavior” is regarded as more usual. The German HE sector, however, has almost no experience in market-oriented behavior because of its long tradition of state run HEIs. The question is, is the German HE sector developing entrepreneurial thinking in that it co-operates with private education institutions? Can the “ethos of the German prestige university” be maintained even through public-private franchising arrangements?

The hitherto investigations show that HE franchising in Germany is a rare and not particularly transparent business model of several HEIs. Some of the franchising institutions refuse to use the term “franchising” because they fear an undermining of their reputation.

The model promises, however, opportunities for the whole HE sector:

- Strategic thinking and acting for public universities concerning market growth, strengthening of the university’s profile, additional financial resources
- Regional structural development through flexible offerings of HE study programs
- Progressive qualification opportunities for students and their employers.

Who exactly and in which extent the winners of HE franchises are, will be further investigated in empirical studies.

The very delicate issue in the HE franchise model between a private HE provider as franchisee and a public university as franchisor is the question of the allocation of losses and benefits between the private and the public sector. In German public HE students pay almost no tuition fees, but in the case of the franchise model with a private franchisee institution the students pay a high amount for the degree from a public university. Do the benefits of the public-private HE franchise legitimize the high tuition fees or are public services exploited to generate private profits?

The two selected scenarios (see paragraph 5) show possible risks of the public-private HE franchise. In both cases the student may suffer from bad quality for high costs and should be protected. These approaches open the discussion on governmental interventions and quality assurance mechanisms. To answer the question if and –if yes– what kind of internal and / or external quality assurance mechanisms are adequate all opportunities and risks of HE franchise have to be identified. The investigation has to consider the relevant environmental conditions of the HE sector in question and should start from the examination of each actor’s objectives. The particular aims of the partners determine their behavior which leads to the identification of the ex ante and ex post transaction costs for the public university, the private franchisee institution, and the student.

In case that HE franchise arrangements can be conducted efficiently universities are to inform in which mode and extend they can use the model to strengthen their strategic position on the HE market.

Additionally HE franchise models have to be transparently and conformly communicated to all involved actors from official HE institutions, universities and other education providers, from ministries and quality assurance agencies as well as to students and employers. The overall maxim shall be that “students should not become victims of entrepreneurial activities” (Koelman & de Vries, 1999, p. 175).
REFERENCES


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