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Michael M. Alba and Anthony Raymond A. Goquinco

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Table of Contents

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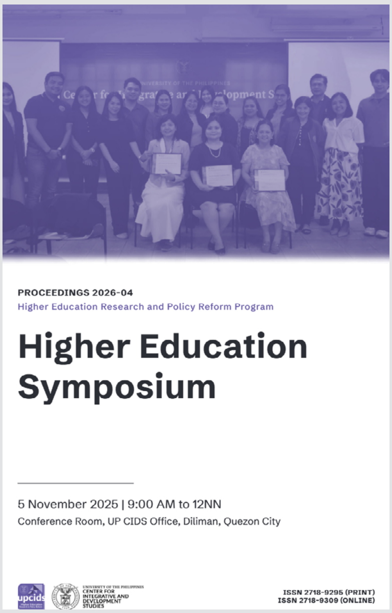

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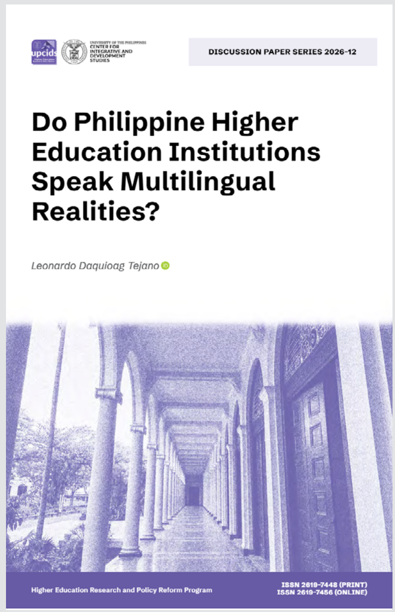
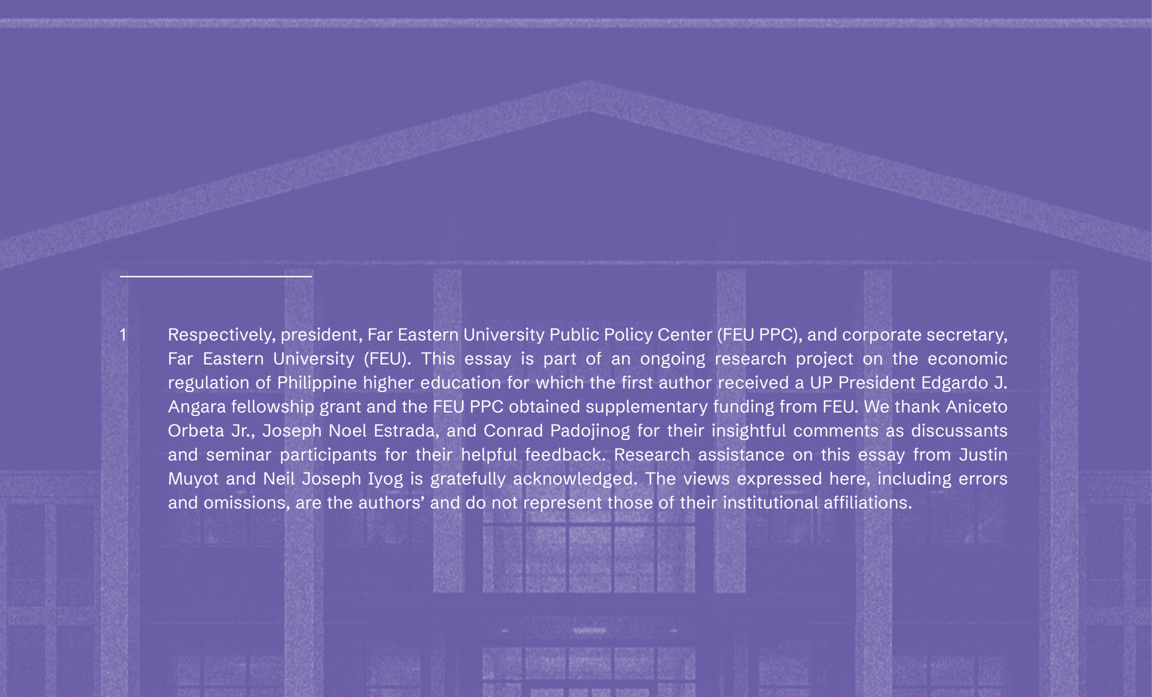


DISCUSSION PAPER

Do Philippine Higher Education Institutions Speak Multilingual Realities?

The Commission on Higher Education's De Facto Price Cap Regulation of Private Higher Education Institutions

Michael M. Alba and Anthony Raymond A. Goquinco[1]



1 Respectively, president, Far Eastern University Public Policy Center (FEU PPC), and corporate secretary, Far Eastern University (FEU). This essay is part of an ongoing research project on the economic regulation of Philippine higher education for which the first author received a UP President Edgardo J. Angara fellowship grant and the FEU PPC obtained supplementary funding from FEU. We thank Aniceto Orbeta Jr., Joseph Noel Estrada, and Conrad Padojinog for their insightful comments as discussants and seminar participants for their helpful feedback. Research assistance on this essay from Justin Muyot and Neil Joseph Iyog is gratefully acknowledged. The views expressed here, including errors and omissions, are the authors' and do not represent those of their institutional affiliations.

Key Highlights

- **Main argument:** Although the Commission on Higher Education (CHED) formally regulates tuition and other school fees (TOSFs) of private higher education institutions (HEIs) through a price-approval process, its implementation under CHED Memorandum Order (CMO) 03 series of 2012 functions in practice as an $I - X$ price cap scheme in which I is the previous year's regional inflation rate, X is fixed at zero, and the regulatory period is one school year. While this high-powered incentive mechanism encourages operational efficiency, it may also discourage quality improvements. More fundamentally, the paper argues that TOSF-related information asymmetries in higher education can be addressed more efficiently through transparency requirements rather than through price regulation.

- **Policy landscape:** The paper traces the evolution of CHED's regulation of TOSFs from 1995 to the present and examines the legal and institutional framework established under CMO 03 series of 2012. It also situates tuition regulation within the broader governance of Philippine higher education, contrasting the regulatory regime for private HEIs with the publicly funded procurement model applied to state universities and colleges (SUCs) and CHED-accredited local government universities and colleges (LUCs) under Republic Act (RA) 10931.

- **Methods:** Using the economics of regulation as its analytical framework, the paper interprets CHED's regulatory practice through the lens of incentive regulation and price-cap regulation. It analyzes the design and implementation of CHED's tuition-regulation framework, evaluates its welfare implications, and compares alternative institutional arrangements for addressing information asymmetries and promoting efficiency, quality, and social welfare.

- **Findings:** The analysis finds that CHED's de facto price-cap regulation is administratively simple but imposes all cost risks on private HEIs, creating strong incentives for efficiency while potentially weakening incentives to improve quality. It also identifies several shortcomings in CHED's current regulatory framework, such as the absence of a formal appeals process, insufficient transparency in application processing, the lack of restrictions on fees unrelated to student learning, and the absence of accountability mechanisms for CHED's implementation of price regulation. More broadly, the paper finds that the asymmetric governance of private HEIs, on the one hand, and SUCs and CHED-accredited LUCs on the other, is difficult to reconcile with the constitutional principle of public-private complementary, competitive neutrality, and the efficient use of public funds.

- **Policy recommendations:** The paper recommends replacing price regulation with a one-stop online disclosure platform requiring HEIs to publish, for every incoming student cohort, the complete term-by-term schedule of fees covering the entire degree program (including for field trips and other activities). If price-cap regulation is retained, it should use expected rather than past inflation, incorporate a past-period correction factor, and allow negative values of X to reward quality improvements. The paper also recommends strengthening CHED's regulatory framework by establishing a formal appeals mechanism, enhancing transparency and accountability, prohibiting extraneous fees, institutionalizing competitive neutrality, aligning HEI's societal roles with appropriate funding sources, and articulating a coherent governance framework grounded in the constitutional principle of public-private complementarity.

- **Conclusion:** The paper concludes that coherent governance of Philippine higher education requires regulatory arrangements that consistently promote efficiency, quality, equity, and social welfare. This entails replacing or substantially reforming CHED's current tuition-regulation regime and aligning the governance of both private and public HEIs with the principles of public-private complementarity, competitive neutrality, and the judicious use of public funds.

Introduction

In the exercise of its regulatory authority, the Commission on Higher Education (CHED) has primarily focused on curriculum matters, as indicated by the number of memorandum orders it has issued, classified by their subject headings.[2] Among the Commission's various mandates, however, the power to regulate the tuition and other school fees (TOSFs) of private higher education institutions (HEIs) is perhaps what is top of mind for the majority of Filipinos, given the issue's politically contentious nature – with the slightest suggestion of increased charges drawing media attention and sparking student protests. Yet, CHED's practice of this power has never been formally examined for its efficiency and social welfare implications.

Addressing this research gap, this paper follows a usual textbook approach whereby the model that best reflects CHED's price regulation practice – i.e., the price-cap incentive scheme – is first described and its features and implications are explained. The Commission's issuances on the subject are then briefly reviewed in chronological sequence, ending in CHED Memorandum Order (CMO) 03 series of 2012, which promulgated the rules and procedures that are currently in place.

To set the stage for the analysis, the study describes the elements of this last CMO in detail. These include: the legal bases of CHED's authority to regulate school fees; the Commission's aspirations for the memorandum order; the factors that are to be considered in evaluating an HEI's application; the application procedure rules and grievance provisions; and the roles of national and regional multi-sectoral committees, the CHED Regional Offices (CHEDROs), and the Office of the CHED Executive Director.

CHED's de facto regulatory practice is then assessed from various aspects: its design framework, its choice of values for the price-cap equation, and the appropriateness of price regulation as the solution to information-asymmetry market failures in higher education, such as predatory pricing, locked-in costs and the "holdup" problem, and stranded costs.

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2 From the Commission's establishment in 1994 up to April 2024, policies, standards, and guidelines for undergraduate programs and for graduate programs accounted for 29.9 percent and 4.0 percent, respectively, of all commission memorandum orders; those for tuition and other school fees comprised only 1.0 percent.

The paper also brings attention to the uneven governance of private HEIs and state universities and colleges (SUCs) private HEIs, on the one hand, and state universities and colleges (SUCs) and CHED-accredited local government universities and colleges (LUCs)[3], on the other, brought about by the disparate mechanisms for paying the schools' degree-granting activities: for private HEIs, these are funded by TOSF revenues; for the aforementioned government schools, they are fully subsidized by the government under Republic Act (RA) 10931 or the "Universal Access to Quality Tertiary Education Act." This disparity raises questions about the consonance of higher education governance with the constitutional provision on public-private complementarity in education, the regulatory principle of competitive neutrality, and the efficient use of public funds; and for each tenet, the paper notes the adverse effects on efficiency and social welfare when it is not upheld.

The paper concludes by urging for the formulation of a governance framework for higher education that is grounded on the three basic precepts. It also suggests two alternative ways for improving on CHED's de facto price-cap regulation of private HEI TOSFs.

The Price-Cap Regulation Model

Price-cap regulation is an incentive regulation model that focuses on controlling the price of the commodity or set of services under regulation. In this model, the regulator sets, over a pre-specified effectivity period, a ceiling on the amount by which a firm may increase its price over the previous period. A generic form that captures the essential characteristics of this scheme is known as the $RPI - X$ (Retail Price Index minus X) or the $I - X$, where RPI or I is a measure of inflation and X is an adjustment for efficiency or productivity improvements (that can be shared with the consumers in the form of lower prices).

As its name suggests, the $I - X$ model limits the firm's price increases to no more than the percentage-point difference between a designated inflation-rate measure, I, and an efficiency- or productivity-offset factor, X. Formally,

$$P_t \leq P_{t-1} \cdot (1 + I - X),$$

3 Henceforth, we use "SUCs" to refer collectively to SUCs and CHED-accredited LUCs.

where P_t and P_{t-1} are, respectively, the prices charged for the regulated good in periods t and $t-1$. To be noted is that, within the rule's period of effectivity, the firm need not seek regulatory approval for price adjustments; these just have to be below or equal to the price cap.

As for the time frame of the period of effectivity, this is generally weighed by the regulator against the degree of uncertainty it perceives about changes in costs and demand – the duration tending to be shorter the greater the uncertainty, to enable the regulator to quickly update the values of the price-cap equation. This is because the regulator usually comes under public or political pressure when either (a) the net revenues of regulated for-profit firms are deemed excessive or the expenditure levels of regulated non-profit firms are considered wasteful – implying that the price cap is too generous – or (b) the net revenues of for-profit firms are judged to be insufficient, if not negative, or the expenditure levels of non-profit firms are unable to adequately support firm operations – implying that the price cap is too low for regulated firms to be sustainable or to maintain quality standards.

Price-cap regulation has the following regulatory-system features: First, compared to cost-of-service, average-cost-pricing, or rate-of-return regulation,[4] it is easier for the regulator to administer, being informationally less demanding. With pricing decoupled from explicit considerations of the firm's costs and sustainability, the regulator need not be mindful of cost and demand data (on which the firm has an information-asymmetry[5] advantage); more precisely, it need not be concerned about the adverse-selection problem

4 Cost-of-service, average-cost-pricing, and rate-of-return regulation are labels for essentially the same regulation model meant to address the natural monopoly problem. Here it suffices to say that the scheme is information intensive because it requires the regulator to know market demand and the cost structure of the regulated firm(s).

5 Information asymmetry is a situation in which one party in a transaction possesses more or better information, which may take the form of adverse selection or moral hazard. In adverse selection, the hidden or unobservable information is a pre-transaction, immutable attribute or trait; in moral hazard, it is an unobservable, post-transaction behavioral response to the ensuing incentives. In the economics of regulation, the adverse selection problem is usually cast as a firm's cost (or efficiency) DNA, i.e., whether it is inherently a high-cost (or inefficient) or low-cost (or efficient) operation (an attribute that the firm would know, but which the regulator cannot readily observe), while the moral hazard problem is generically referred to as the firm management's "effort" to reduce costs and improve efficiency – behavior which again is not readily observable by the regulator.

regarding the firm's type and how to cap the firm's economic rent to address the moral hazard problem of inducing the appropriate intensity of the firm's effort in case it is a low-cost operation.[6]

Second, predatory pricing is not an issue since the firm does not have much discretion in setting prices, with P_{t-1} a given, I exogenously determined by economy-wide factors and estimated by an independent government agency, and X prescribed by the regulator.

Third, price-cap regulation is a very high-powered incentive regulation model:[7] the regulated firm (rather than consumers or taxpayers) bears the burden of all costs and their associated risks. On the flip side, its behavioral implication is, because the firm is the residual claimant of any cost savings, it has a strong incentive to be operationally efficient, possibly even to the detriment of quality, especially if there are no safeguards or monitoring processes and no adverse consequences for producing substandard output.

Fourth, in a multi-period context at least three issues emerge:

a. The regulator must be careful not to set off a "ratchet effect," whereby the cost-reducing effort (or moral hazard variable) of the firm in the current period is penalized with a higher offset factor value in future periods, as this would serve to disincentivize the firm from innovating and undertaking efficiency or productivity improvements.

b. To maintain its credibility, the regulator must be wary of (perceptions of) regulatory capture in assigning the value of X. Setting it too low may be perceived by stakeholders to be a bias for the regulated firm; setting it too high may be seen to be endangering the firm's viability and trigger a ratchet

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6 In the canonical model of regulation developed by Laffont and Tirole (1993), the regulator sets the incentives such that a high-cost firm earns no economic rent but exerts less-than-efficient effort (in order to satisfy the firm's participation constraint), while a low-cost firm is ceded an economic rent to incentivize it to exert the efficient level of effort (because, otherwise, the low-cost firm would simply mimic the behavior of the high-cost firm).

7 Defined as the percentage of realized costs borne by the regulated firm, the power of an incentive scheme is an important concept in policy debates about the relative merits of regulation (and procurement) models. This is because the higher the power of a scheme, (a) the greater is the firm's incentive to save on costs of operation – which the regulator hopes will induce the firm to be more operationally efficient rather than reduce quality, (b) the greater is the risk to the firm of cost shocks, but (c) the greater are the opportunities for the firm to extract an economic rent.

effect, disincentivizing the firm from innovating or, worse, to skimp on quality. It is therefore important that the regulator maintain arm's-length relationships with all stakeholders and adopt an evidence-based approach in determining the value of *X* during regulatory rate reviews.

c. Price-cap regulation institutionalizes "regulatory lag" in that, during the term of effectivity of the price cap, the regulator cannot reset the pricing rule, giving the regulated firm some flexibility to adjust prices (as long as they're below the cap). The firm is thus incentivized to "beat the odds," i.e., develop and adopt cost-reducing technologies that result in efficiency improvements greater than *X*, thereby improving its financial standing.

A Review of CHED's Price Regulation Authority

Price regulation (rather than price-cap regulation) has been a significant part of CHED's regulatory practice since the Commission's establishment with the enactment of RA 7722, otherwise known as the Higher Education Act of 1994. Its first issuance on the subject, CHED Order (CO) 12 series of 1995, specified the procedural and document requirements for private HEIs that sought to increase TOSFs for School Year (SY) 1995–1996 and mandated the allocation rule that 70 percent of the proceeds from the fee increases be utilized for the compensation and other benefits of teaching and non-teaching personnel (except those that are also principal stockholders of the school) and 20 percent be earmarked for infrastructure and facilities improvements as well as operational costs.

The CO was quickly supplanted by CMO 03 series of 1997, which among other changes declared the new guidelines to take effect from (rather than for) SY 1997–1998, and which in turn was amended by CMO 16 series of 1997 to set a 31 March 1997 deadline for the consultation period with stakeholders.[8]

To comply with then President Fidel Ramos's directive, CMO 13 series of 1998 created the National Multi-Sectoral Committee on Tuition Fee[s] and the Regional Multi-Sectoral Committees on Tuition Fee[s], with the latter

8 Ironically, CMO 16 series of 1997 did not foresee the need to set similar deadlines for later school years, just as CO 12 series of 1995 limited its instructions to SY 1995-1996, which CMO 03 series 1997 had to correct.

charged with (a) oversight functions over their corresponding CHEDROs in the monitoring of the private HEIs' implementation of school-fee policies and (b) resolving disputes elevated by the CHEDRO. It was also the first CHED issuance that (*i*) directed SUCs and CHED-Supervised Institutions to adopt socialized tuition fee schemes and (*ii*) mentioned sanctions for violations of tuition fee guidelines and policies.

CMO 14 series of 2005 amended by CMO 05 series of 2006, CMO 42 series of 2006, and CMO 07 series of 2007 were the first set of CHED issuances to explicitly adopt price-cap regulation, setting the prevailing national headline inflation rate as the ceiling for percentage increases in school fees.

Remarkably, not taking cognizance of the price-cap issuances,[9] CMO 16 series of 2008, as amended by CMO 39 series of 2008, reverted the guidelines and policies to CMO 13 series of 1998 and additionally required the CHEDROs to monitor that HEIs (a) provide scholarship grants to at least five percent of their incoming freshman population in compliance with Section 8b of RA 8545, otherwise known as the "Expanded Government Assistance to Students and Teachers in Private Education Act," and (b) allocate the proceeds from the fee increases in accordance with the 70-20-10 rule (that 70 percent be allocated to personnel benefits, 20 percent to institutional development, and 10 percent to return on investment).

The latest issuance thus far on policies and guidelines on TOSF increases is CMO 03 series of 2012, which consolidated the provisions of all previous Commission memorandum orders on the subject, except CMO 16 series of 2008 and its amendments, with the scholarship grants for freshmen not being mentioned at all.

As the memorandum order currently in force as well as being illustrative of CHED's regulatory practice on fee setting, CMO 03 series of 2012 is described in greater detail below.

9 This oversight signaled to the research team the need for a searchable CMO database with a digital platform that supports queries by keyword and subject heading. With the help of Abad, Abad, and Associates Law Offices, the FEU PPC developed the resource, which may be accessed at https://publicpolicy.feu.org.ph/cmo-database/. The statistics reported in footnote 2 were generated using the database.

In consonance with previous issuances, CMO 03 series of 2012 cites the following as the bases for and the legal framework of CHED's authority to regulate tuition and other school fees:

- The Philippine Constitution of 1987, Article XIV, Section 4(i), which provides that: "The State recognizes the complementary roles of public and private institutions in the educational system and shall exercise reasonable supervision and regulation[10] of all educational institutions."

- Batas Pambansa 232 (The Education Act of 1982, henceforth BP 232), which, prior to the ratification of 1987 Constitution, served as the basic law empowering the government to supervise, manage, and regulate education in the Philippines.

    - Section 3 declares that it is "the policy of the State to establish and maintain a complete, adequate, and integrated system of education relevant to the goals of national development."

    - Section 42 provides that: "Each private school shall determine its rate of tuition and other school fees or charges. The rates and charges adopted by schools pursuant to this provision shall be collectible, and their application or use authorized, subject to rules and regulations promulgated by the Ministry of Education, Culture, and Sports."[11]

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10 Here it is worth distinguishing between the meaning of regulation in legal and constitutional discourse and in economics. In law, regulation refers to the authority of the State to prescribe, supervise, restrict, or direct private conduct through rule-making, adjudication, and enforcement. In economics, regulation refers to an institutional arrangement in which a public authority establishes and enforces rules that shape the incentives and behavior of market participants in an industry in pursuit of specified public objectives, ostensibly to improveI social welfare.

11 The comma after the phrase "shall be collectible" is grammatically consequential and gives rise to two competing interpretations for Section 42: that (a) both the collection and utilization TOSFs are subject to the rules and regulations issued by the then Ministry of Education, Culture, and Sports, and (b) only the utilization of TOSFs, not their collection, is subject to the same. The first interpretation treats the comma as an innocuous pause; the second, as a significant break, otherwise it would not be there.

- RA 7722, which, as mentioned above, established CHED and thereby transferred the power to regulate higher education from the Department of Education, Culture, and Sports (DECS), considering that the Act repealed neither BP 232 nor Presidential Decree (PD) 451 (see the next bullet point on the Supreme Court decision in Lina v. Cariño).

  - Section 2 declares that: "The State shall protect, foster, and promote the right of all citizens to affordable quality education at all levels and shall take appropriate steps to ensure that education shall be accessible to all."

  - Section 8n gives the Commission the power to "promulgate such rules and regulations and exercise such other powers and functions as may be necessary to carry out effectively the purpose and objectives" of the Higher Education Act.

  - Section 8o charges the Commission to "perform such other functions as may be necessary for its effective operations and for the continued enhancement, growth, or development of higher education."

- The Supreme Court decision in Lina, Jr., v. Cariño (General Register (GR) 100127), which established that DECS through its Secretary had the power to issue rules and regulations governing the collection of tuition, particularly the imposition of a maximum rate to be collected, as this had earlier been provided for in a series of legislative acts, such as: Act 2706 (the "Private School Law of 1917"), as amended by Act 3075 (of 1923) and Commonwealth Act 180; RA 6139; and PD 451.

- The Supreme Court decision in St. Joseph's College v. St. Joseph's College Workers Association (SAMAHAN) (GR 155609), which clarified that, regardless of the effect of school fee increases on gross education revenues, 70 percent of the proceeds from the increased fees must be allocated to personnel benefits.

- Commission En Banc (CEB) Resolution 322-2011 as reflected in the minutes of the 384th regular meeting of CHED Commissioners, which approved the "Enhanced Policies, Guidelines, and Procedures Governing (a) Increases in Tuition and Other School Fees, (b) [the] Introduction of New Fees, and (c) for Other Purposes," the title of the document that eventually became CMO 03 series of 2012.

The CMO also takes care to declare that, in implementing this price-regulation function, CHED aspires to ensure "the reasonableness and propriety of tuition and other school fee charges" by balancing considerations of access to education and "the sustainability and viability of school operations" – for which reason, for transparency, it requires increases in school fees and the introduction of new fees to undergo an application and consultation procedure with the following factors to be taken into account: the regional inflation rate, the financial standing of the HEI, the financial capacity of the student population, the impact of calamities, and the school's quality as well as its missions and vision.

For private HEIs,[12] the application and consultation procedure is as follows:

- The HEI president or head must submit to the appropriate CHEDRO the following notarized documents by April 1 of the calendar year that the school fee increases or new fees are to take effect:[13]
    - a letter of advice (LOA) of the HEI's intent;
    - a certificate of compliance (COC) that the proceeds from school-fee increases of the current school year are being allocated according to the 70-20(-10) rule;
    - a certificate of intended compliance that the proceeds from school-fee increases being applied for will be allocated according to the same rule;

12 Under RA 10931, the Philippines adopted what essentially is a procurement model for SUCs: through budgetary appropriations, the national government buys seats in SUCs for them to fill – in effect, rendering moot the SUC provisions in CMO 03 series of 2012. Nonetheless, it remains to be pointed out that CHED never had approval authority over SUC school fee charges. Prior to the enactment of RA 10931, RA 8292 (the Higher Education Modernization Act of 1997), Section 4d, had assigned the power to set school fees to the SUC governing boards. In the CMOs, CHED's regulatory authority over SUCs on fee setting was limited to ensuring that consultation with stakeholders took place and that the proceedings of those deliberations as well as the fees decided on by the SUC board were reported to the appropriate CHEDRO. (LUCs stand on an altogether different legal footing: established under the governance of their respective local government units, they generally do not fall under the regulatory jurisdiction of CHED, although CHED-accredited LUCs qualify for the benefits and subsidies provided under RA 10931.)

13 In other words, the submission deadline is about two to four months before the next school year starts, which is mandated by RA 11480 to be between the first Monday of June and the last day of August.

- a comparative schedule of school fees juxtaposing the current and proposed prices, and expressing the line-by-line difference in peso and percentage terms;
- a certification on the consultation process, which includes reports on the proceedings and outcomes of meetings; and
- a the list of officers of the student government or of school-recognized student organizations.

The consultation process itself must satisfy the following requirements:

- It must be initiated by the HEI president or head, or his/her duly designated representatives.
- The appropriate CHEDRO must be informed at least 15 days before the consultations are held.
- The consultation meetings must involve the student government (or, in its absence, school-recognized student organizations) as well as faculty, non-teaching personnel, and alumni associations.
- Notices of meetings must be sent to all parties and conspicuously posted on school bulletin boards at least 15 days before the meeting dates (to give sufficient time for stakeholders to conduct consultations with their constituents).
- In the consultation meetings, the HEI must justify its proposed changes in school fees; and the meetings themselves must hold discussions on the advantages and disadvantages of the fee changes.
- The HEI's latest audited financial statements must be made available to authorized parties upon request. Otherwise, the HEI forfeits its right to change the school fees and additionally may be levied other penalties and other sanctions by the CHEDRO.
- The consultation period must have been completed by February 28 of the calendar year that the school fee changes are to take effect.

The guidelines on the approval process of school fee changes are straightforward: The CHEDRO must act within 30 days of the HEI's submission of the required documents or before April 15 (presumably whichever is earlier). If no action is taken within the time frame, the application is deemed approved.

During the 30-day review period, should the CHEDRO note deficiencies in the application documents, it may ask the HEI to correct and resubmit the papers within 15 days.

The CMO also includes grievance provisions:

- Complaints about school fee charges that did not undergo or were not included in the consultation process are to be endorsed by the HEI's student government to the CHEDRO within 30 days of the last consultation meeting.

- School fee charges that are found in violation of the CMO's provisions are disallowed, and funds collected from these charges would be returned to the students.

- HEIs that are found to have violated the CMO's provisions may, on the recommendation of the Regional Multi-Sectoral Committee on Tuition and Other School Fees, be barred from applying for school fee increases. In addition, CHED may impose "penalties such as the revocation of permits, downgrading of [accreditation] status, [and phasing out of academic programs]."

Finally, the CMO resurrects the national and regional multi-sectoral committees of CMO 13 series of 1998, and specifies responsibilities for the CHEDROs and the Office of the Executive Director in connection with price regulation. The national committee is charged with reviewing, recommending, and evaluating the policies and guidelines on school fee adjustments and exercising oversight functions over the regional committees. The regional committees, in turn, are directed to ensure that (a) the CHEDROs monitor HEI compliance, (b) meetings with stakeholders are held, and (c) when requested, it constitutes itself as the regional monitoring team to check compliance complaints.

Outside of their approval authority on the applications, the CHEDROs are mandated to (a) resolve disputes and complaints or elevate them to the regional committee and then endorse the committee's recommendations to the

CHED Executive Director; (b) monitor HEI compliance (including using an evaluation instrument prepared by a CHED ad hoc committee); (c) report on school fee changes and related developments; (d) act as the chair and secretariat of the regional committee; and (e) assist the regional committee when it is requested by stakeholders to check the compliance of specific HEIs.

In the case of the Office of the Executive Director, the scope of responsibilities is limited to consolidating the CHEDRO reports and deciding on disputes referred by the regional committee.

Analysis

As written in CMO 03 series of 2012, CHED's official policy is technically one of price regulation. But perhaps as a vestige of CMO 14 series 2005 and its amendments – which explicitly adopted price-cap regulation – and because CMO 03 series of 2012 merely enumerates the factors that may be considered but does not elaborate how these should be used to evaluate an HEI's application, in practice the CHEDROs implement price-cap regulation (with different regions (or regional directors) interpreting the memorandum-order provisions differently).[14]

In any case, CHED's de facto regulatory practice may be characterized as an $I - X$ price-cap model where I is the regional inflation rate, the offset factor X is fixed at zero, and the period of applicability is limited to one school year. This is a very high-powered incentive-regulation model where the HEI is the residual claimant of cost savings and the effectivity period of the price-cap equation (and the values of its variables) is kept to the minimum possible duration, most

14 In focus group discussions of member associations of the Coordinating Council of Philippine Educational Associations (COCOPEA) conducted by the FEU PPC research team (Santos 2025), participants volunteered that: (a) CHED does use a price-cap model; (b) it is extremely difficult to get approval for fee increases higher than the regional inflation rate – even if an HEI's stakeholders had acceded to them during the consultation process – because the application is referred to the CHED national office, which can add six to ten months to the processing time; (c) in some regions, the price cap is applied to each fee and, if not followed, the HEI is advised to redo its applications by spreading the excess in the price hike across other fees to maintain the overall price increase [a rather silly rule which unduly delays the processing of an HEI's application and is an instance of regulatory overreach]; (d) other than the regional inflation rate, the factors listed in CMO 03 series of 2012 are not given weight, which limits an HEI's capacity to undertake quality improvements, effectively freezing the quality distribution of private HEIs; and (e) CHED's price-cap formula is not responsive to rapid changes in costs that HEIs incur during the school year.

likely because CHED considers the demand and cost conditions in Philippine higher education to be volatile and politically fraught.

In the design of the CMO's regulatory framework, at least four features are missing. First, a formal appeals process is not provided for. If the CHEDRO returns its application papers and asks it to correct for "deficiencies," whether justified or not, outside of informally lobbying the CHED Regional Director, an HEI has no recourse except the courts. This gives CHEDROs extensive latitude in exercising policy; there are no checks to curb regulatory overreach, except expensive and time-consuming legal action.

Second, the CMO fails to require both the CHED national office and the CHEDROs to make public the reports on how HEI applications are processed. This is ironic: CHED invokes transparency to justify the public consultation requirement in the application procedure for adjusting school fees, but exempts itself from adhering to the principle.

Third, absent from the guidelines are rules on what fees can be charged – the only consideration being that stakeholders agree to them during the consultation process. But a moral question is involved: should school fees not be limited to activities that are directly related to student services? Unfortunately for students, this has not been so. A case in point: schools have been known to charge faculty research fees on the argument that research activities enhance teaching quality. Still, the question remains: why should students pay for activities not *directly* connected to their learning and schooling experience? Should not these other activities be funded out of cost savings or non-tuition revenue inflows?

But schools resort to this practice only because the roles society designates for HEIs are not aligned with funding sources. As pointed out in Alba (2026), HEIs are called on to: (a) confer academic degrees; (b) push the boundaries of knowledge through research; and (c) develop research-based solutions to the most challenging social problems in its geographic area of influence. Yet private HEIs in the Philippines have but one significant revenue stream: enrollment, in connection with its first role.

As the regulator of Philippine higher education, CHED must address this misalignment and advocate for policies that capacitate HEIs to perform their research and public brain-trust roles. After all, the outputs of these activities are pure public goods (i.e., their benefits are non-rival and non-excludable) –

so that it is incumbent upon the government to provide financial and other support for them (such as establishing research coordination and collaboration networks and a backbone infrastructure for research).

Fourth, the CMO does not make CHED accountable for implementation lapses. For instance, it is not clear that the national and regional multi-sectoral committees have been regularly convened and what impacts they have had. No reports have been disseminated on the national committee's work on the policies and guidelines on school fee adjustments or its oversight functions over the regional committees. Nor have there been reports on the regional committees' activities regarding their specific mandates.

As for CHED's de facto price-cap equation itself, there are at least two problems with CHED's choice of variable values: First, CHED assumes that the inflation rate of the past 12 months (from January to December, since consultations start in February of the next year) would continue to prevail in the following year. Hence, its formula simply substitutes the inflation rate of the preceding year π_{t-1} for I_t (with the offset factor X fixed at zero): formally, $P_t \leq P_{t-1} \cdot (1 + \pi_{t-1})$. Effectively, this means that HEI pricing is always one year behind inflation trends, so that school fees are generally not aligned with cost movements. A better formula would be to use the expected regional inflation rate π_t^e with a past year correction factor, $I_t = \pi_t^e - (I_{t-1} - \pi_{t-1})$, which can be operationalized by mandating the Department of Economy, Planning, and Development or the Philippine Statistics Authority to provide estimates of expected regional inflation rates based on the national inflation rate forecast of the *Bangko Sentral ng Pilipinas* .

Second, the CHED formula does not include the offset factor, and misses the opportunity to incentivize innovations and quality enhancements. As an example, CHED could specify negative values for X, graded by the HEIs' status along CHED's vertical typology (so that autonomous HEIs would be rewarded with the most negative offsets). CHED could also extend similar favors to HEIs in calamity-hit areas (to enable them to recover faster), in progressive cities or provinces (to empower them to keep up with their locale's economic growth challenges as well as incentivize them to take up their public brain-trust function), or that have quality aspirations (to allow them to leapfrog to a higher standard, which can lead to dynamic changes to the quality distribution of HEIs). The formula can still be rule-based – a publicly transparent, negotiated outcome between CHED and HEIs – and subject to third-party, publicly disclosed performance reviews, with only those institutions that implement their plans successfully being allowed to continue to enjoy offsets.

The fundamental question, though, is: why does CHED have to practice price-cap regulation? The reasons are probably that:

- Owing to the country's *ilustrado* legacy, Filipinos place a high premium on higher-education credentials – college graduates are lauded as "*may pinag-aralan*" – which implies that the market demand curve is relatively price inelastic.
- Since HEIs have a monopolistic cost structure (Alba 2026), there is public concern that HEIs could engage in predatory pricing.

What is missed is the following characterization: The economic good (or outcome) that the college student desires to purchase is the academic degree. But it can only be obtained at some future time and paid for in installments (i.e., per academic term), with the student exerting considerable effort (a moral hazard variable) to satisfy, term by term, her school's curricular requirements. Since schools set fees on a year-to-year basis, how much the student has to pay per academic term is highly variable and subject to uncertainty. In other words, at entry as a college freshman, the student does not have a clear sense of how much her college education would ultimately cost – even though the curriculum is already fixed. Moreover, there are locked-in costs, which may cause a "holdup" problem and leave her with stranded costs: a student in the middle of her schooling journey will find it neither easy nor convenient to transfer schools if levied an unexpected, large price increase (i.e., because she has locked-in costs, her school tells her to "stick 'em up" – a holdup situation); furthermore, transferring to another school may leave her with stranded costs if her new institution credits only a few of the units she has earned.

Instead of price(-cap) regulation, however, CHED can address the information-asymmetry problem by (a) establishing and maintaining a one-stop online platform where each HEI is obligated to have a website and (b) requiring HEIs to publish, for each of their academic program offerings and for the entering freshman class of each school year, the term-by-term schedule of subjects (including activities like field trips) that the students will be registering for and the associated fees that will charged – over the entire period it will take the students to complete their degrees. Doing so provides entering students with full information about costs and also avoid locked-in costs and hold-up problems and stranded costs.[15] If she doesn't like any feature of the schedule of costs in any school year, she is free to walk away from that HEI before enrolling as a freshman student.

Arguably, another benefit of the online platform is that it will be easier for CHED to administer than price regulation. Instead of having to process and evaluate HEI applications annually, CHEDROs will only need to ensure that each HEI under their jurisdictions have updated its website by a given date. Price regulation is rendered moot.

Note as well that the incentive scheme is still high-powered: HEIs remain the residual claimants of cost savings. Admittedly, an added downside is that HEIs are made to bear the risks of incorrect inflation forecasts over the four or five years of a course of study (which may be a bit long). But this problem can be mitigated by providing an escape clause allowing HEIs to revise cost estimates of the remaining school years of a given student cohort should the actual regional inflation rate exceed a pre-determined ceiling set by CHED (or should an HEI be hit by a calamity), subject to the documented approval of stakeholders in a CHED-specified consultation procedure and with the CHEDROs monitoring compliance.

Finally, what remains to be considered are the big-picture implications of the uneven governance policies that are being applied to private HEIs and SUCs. CHED implements a price-cap mechanism for private HEIs, while RA 10931 effectively stipulates a procurement model for SUCs, which may be characterized as the government "buying seats" in the academic offerings of

15 HEIs can also be required to maintain on the platform comprehensive information about their institutions, ranging from their vision and mission statements to program-level indicators such as licensure exam passing rates, cohort survival rates, graduation rates, institutional and program accreditations, and other performance measures. The platform can also be designed to support sophisticated queries. For example, a user could ask: Which three HEIs in Region VII have the highest passing rates in the licensure exam for accountancy? or Which HEIs demonstrate a strong institutional commitment to environmental sustainability? By substantially reducing information asymmetries at the outset, the platform would lower the search and information costs faced by prospective students in choosing a college or university and an academic program best suited to their interests and aspirations.

The website would also provide CHED with valuable usage analytics. By analyzing users' search behavior and geographic origin, CHED could infer the catchment area of each HEI – that is, whether it attracts students primarily from its locality, its region, or the country as a whole – which, in turn, could inform policies on the entry and exit of HEIs in a given area. Analysis of users' search queries could likewise reveal the most significant concerns of prospective students, thereby informing future disclosure and regulatory policy.

public institutions. Because the price-cap model is extremely high-powered, private HEIs are incentivized to be operationally efficient, possibly at the expense of quality (owing to quality's implied higher cost), since standards are not systematically monitored[16] and, outside of reputational loss to the HEI, there are no penalties for transgressions. By contrast, the procurement model of RA 10931 is an extremely low-powered scheme: as designed by the law, SUCs do not bear any of their degree-granting costs; in principle, the government fully pays for them. But any cost savings at the end of the fiscal year are returned to the national treasury. SUCs are thus incentivized to simply fully utilize their funding allocations, regardless of efficiency or quality considerations, only taking care that their expenditures do not run afoul of Commission on Audit rules.[17]

SUCs that take a long-term perspective, however, may be incentivized to pursue growth in student numbers as a hedging strategy – i.e., to use size as a form of "too big to fail" insurance – in case public funding proves unsustainable and the number of state schools would need rationalizing.

Unfortunately, this prospect aligns with how the demand side of the higher education market may be shaping up. As a consequence of the disparate payment mechanisms – price regulation for private HEIs and government funding for SUCs – demand may be bifurcating: students with a credentialist view of education may be flocking to SUCs, while the minority who view education as conferring world-of-work productivity as well as life skills may

16 Program and institutional quality assurance, whether by CHED's Institutional Sustainability Assessment, any member association of the Federation of Accrediting Agencies of the Philippines, or the ASEAN University Network – Quality Assurance, are all voluntary initiatives for HEIs.

17 SUCs do have serious challenges due to RA 10931. In lieu of the more spread-out risk of student nonpayment of school fees under the old socialized tuition program, they now face the risk of nonpayment by a single payer – the government as monopsonist. In other words, they are now more exposed to government failure. Reportedly, from SY 2017-2018 to SY 2021-2022 the government froze SUC fees to their 2016 levels. Then in 2022 the government was unable to fully disburse the budgetary allocations that were owed to SUCs. How SUCs were able to maintain quality given these assaults on their financial resources is thus a question worth exploring if RA 10931 were to be evaluated.

be gravitating to the perceived quality (or value-for-money) institutions.[18] The end result is likely to be overcrowding in SUCs (that are pursuing a growth-in-numbers strategy) and declining enrollments in private HEIs not known for their quality, potentially leading to their closure.

Ultimately, this difference in the enrollment-revenue sources of public and private HEIs raises questions about the policy's consonance with three fundamental concerns: public-private complementary in education, competitive neutrality, and the appropriate scope of government spending.

First, what does the constitutional provision on public-private complementarity in education and "reasonable supervision and regulation of all educational institutions" actually mean in terms of the State's governance policy and practice? Is the nation's preference that SUCs are to have institutional primacy in the delivery of higher education services – and that private HEIs are to serve only niche segments of the higher education market? If so, the country should brace for government failure in the higher education sector – in the forms of, among others, delayed adjustments to cost-inflation pressures, delayed or only partial reimbursements of outlays, and intertemporal changes in the government's budgetary preferences – and, in turn, the persistence of the long-running national learning crisis.[19]

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18 In the economics of education, there are three competing hypotheses on the relationship between education, productivity, and earnings. Human capital theory maintains that there is a direct causal effect running from schooling to wages (through productivity): education enhances worker productivity, which in turn is rewarded by higher wages. The screening model argues that the statistical correlation between education and earnings is spurious; it is innate ability (an adverse selection variable) that is the primary determinant of productivity (and wages). But high-ability individuals (who find learning easier so that they have lower schooling costs) use education to differentiate themselves from low-ability, low-productivity peers (who, with their higher schooling costs, are unable to do the same). Hence, educational attainment may be used to screen high-ability (productive) individuals from low-ability peers. Credentialism claims that the education does not confer productivity, but only performs a certifying or licensing role. In other words, education simply certifies workers for certain jobs or gives them license to practice certain professions that earn higher wages. But educated workers are not necessarily more productive.

19 On the other hand, public-private complementary can mean that the State provides higher education only in underserved areas and where there are market failures that regulation cannot address. Considering this option entails involved analysis (and another paper). Suffice it to say here that Cornell University is an example worth emulating: the university has both a private and public character, where colleges that provide practical education and public service, especially in fields important to the economy of New York State, are publicly subsidized and, as in other land-grant institutions, New York residents are charged lower fees.

Second, is it the policy of the State to forgo competitive neutrality – the regulatory principle that government-owned and private firms should compete on an equal footing, without either enjoying advantages based solely on ownership status? If so, the country's higher education sector will never operate efficiently and sectoral incentives to innovate would be dampened, since HEIs would not be competing on merit alone, but would be incentivized to engage in rent-seeking. Such a policy would distort the higher education market, misallocate resources, and produce suboptimal outcomes.

Third, given the high marginal cost of public funds for the Philippines,[20] is it not more judicious for the State to circumscribe a reduced role for the government as provider of higher education services? At least two arguments support this policy stance: (a) as small-government conservatives claim, (because of the specter of government failure) philosophically it is better for the State to focus on its primary functions of providing for national defense, public order and safety, diplomatic and international relations, and other public goods; and (b) market-based solutions allow the government to conserve its limited resources and allocate them to their most important or highest-return uses.

Concluding Remarks

This paper examines CHED's regulation of private HEI school fees. It traces the evolution of CHED's issuances on the subject, but particularly focuses on CMO 03 series of 2012, which promulgated the rules and procedures currently in force. It finds that while CHED's formal policy is price regulation, this is de facto implemented as an $I - X$ price-cap model, where I is the past-year regional inflation rate, the offset factor X is fixed at zero, and the effectivity period is one school year. This administratively simple, but high-powered incentive model places the full burden of cost risks on HEIs, incentivizing operational efficiency, potentially at the cost of quality.

On the design of the price-regulation framework as specified in the CMO, the paper observes notable deficiencies: it lacks a formal appeals process, fails to require public disclosure of application-processing reports, does not prohibit fees extraneous to student learning activities, and has no provisions for holding CHED accountable for implementation lapses.

20 As discussed in Alba (2026), the marginal cost of public funds (in the "excess burden" sense) is estimated by Jones et al. (1990) to be 2.5 for the Philippines, which means that every peso that the government collects in taxes translates to a cost of ₱3.50 (1.0 + 2.5) in lost economic output.

The study suggests that CHED's price-cap equation can be improved by operationalizing I to be the expected regional inflation rate π_t^e less a past-year correction factor, i.e., $I_t = \pi_t^e - (I_{t-1} - \pi_{t-1})$, where π_{t-1} is the regional inflation rate in the previous period, and X to take on negative values to incentivize quality improvements. But it argues that a more effective, welfare-enhancing alternative is a one-stop online platform where HEIs will be required to publish, for each of their program offerings and for the freshman class of every school year, the term-by-term schedule of courses and fees covering the entire period of study. Not only does this arrangement remove the students' cost uncertainty, it also addresses the information-asymmetry problems the student may be subjected to (such as predatory pricing and locked-in- and stranded-cost and the holdup) without heavy-handed regulatory intervention.

Beyond the regulatory model, the paper highlights the broader governance issue of the uneven treatment of private HEIs and SUCs – the former regulated by a high-powered price-cap regime, the latter governed by a low-powered mechanism under RA 10931 that fully subsidizes students without efficiency or quality incentives. This disparity raises fundamental questions about how higher education governance policies align with the constitutional provision on public-private complementarity, competitive neutrality, and the judicious use of public funds in higher education – with non-alignment resulting in inefficiencies, welfare losses, and socially sub-optimal outcomes in the sector.

Ultimately, if the higher education sector is to move toward a coherent, efficient, and equitable governance framework, the following reforms – in decreasing order of importance – must thus be undertaken:

1. The constitutional mandate on public-private complementarity in education must be explicitly and fully articulated in clear policy and operational terms. Only then can there be a coherent governance framework.

2. Competitive neutrality must be institutionalized as a fundamental principle of governance. Unless private HEIs and SUCs operate in an even field, the higher education sector will never be efficient and will only yield sub-optimal outcomes – as HEIs would be incentivized to engage in rent-seeking activities.

3. Public spending must be targeted with high precision. Given the Philippines' high marginal cost of public funds, government budgetary allocations must be focused on interventions with the highest social returns and must keep benefit leakages and misallocations to a minimum.

4. The societal roles of HEI must be aligned with sustainable funding sources. Degree-granting activities should be primarily financed by TOSF revenues, while research and public brain-trust initiatives, the outputs of which are public goods, must be funded by the government, possibly through a strengthened Higher Education Development Fund.

5. The one-stop online platform should be adopted in lieu of price-cap regulation.

6. If price-cap regulation is retained, *I* should be operationalized as the expected regional inflation rate less a past-period correction factor and *X* should allow negative values. CMO 03 series of 2012 must also be amended to cure the deficiencies noted in this paper.

Implementing these reforms would establish a governance framework for higher education that is internally consistent and conducive to efficiency, equity, and quality initiatives. Better still, it would enable the country to make significant, tangible progress on the high aspirations and hopes the Filipino people have for higher education.

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