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## FORUM

### Focus State Subsidies on Low-Income Students

When one considers the recent increases in public tuition, no matter what one's ideological stance, it is clear that our system of financing higher education is broken. Even a die-hard, high-tuition advocate would be unlikely to recommend annual increases of 25 percent or 30 percent, catching enrolled students in the middle of their programs and confronting new students and their families with unexpectedly large burdens. What has caused such sharp increases, what is the prospect, and what might be done to minimize the worst effects?

One underlying cause is outmoded and inequitable state revenue systems that simply are not able to raise enough tax money to meet legislated requirements for public expenditure. An orgy of tax cutting between 1994 and 2001 cost the states 8 percent of their revenue, or roughly \$40-billion. A second cause is the rapid growth of Medicaid, which is placing (and will place) ever-growing demands on state revenue. Combined, those factors mean that we are not simply experiencing another business cycle, soon to be solved by economic growth alone. Most states have created structural -- not just cyclical -- deficits, and higher education happens to be the easiest place to make large cuts in the increasingly small part of a state budget that is discretionary. Unless legislators, governors, and the public reverse course on their "no new taxes" fixation, the cuts to higher education, and the sharp tuition increases they have produced, will be an enduring part of our environment.

It is pointless, therefore, to attempt to dream up ideal solutions to the tuition problem. The states (with help from the federal government) have put themselves in a box, with few palatable alternatives. Indeed, the best one can do is to set priorities among the burdens the situation imposes, and try to ameliorate the worst cases. In my judgment, the most serious problem over the next several years is the likelihood that many high-school graduates from low-income families will be denied an opportunity to enroll in college and earn a degree. Consequently, my suggestions focus exclusively on that issue.

The first step is to ensure that as much state subsidy as possible is directed to low-income students on the basis of financial need. When times were flush, the states could reasonably create expensive merit-based scholarships such as Georgia's HOPE, providing free tuition to students with specific academic credentials without reference to family income. In today's world (and the world likely to be with us for some time), such programs are a luxury no longer affordable. Families that have the income to pay college costs must be asked to pay, so that qualified low-income students are not denied educational opportunity.

Asking students who are uncertain of their academic abilities to borrow heavily to finance their first years in college would guarantee that many would not enroll. Consequently, I would front-load federal Pell Grants into the first two years to give low-income students larger grants, expecting those who succeed and remain in college to do their borrowing for the third and subsequent years. That proposal is controversial within higher education, as four-year institutions fear that two-year colleges and others that offer less than a baccalaureate will capture a greater share of the grants. Others worry that students will



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### Match Revenue Scenarios With Long-Term, Strategic Goals

Sharp tuition increases in public colleges and universities have prompted a spate of creative marketing mechanisms that seek to distinguish an institution or state system from others in the competitive market for students. The decision in Illinois earlier this year to allow public institutions to guarantee a fixed rate of tuition over four years of college is one example of this drive to stand apart. While such efforts may temporarily create a modest market advantage for individual universities or systems, however, they will do little to slow the troubling long-term trend of unpredictable and seemingly uncontrollable hikes in public tuitions.

For example, City University of New York raised undergraduate tuition for state residents at its senior colleges by 25 percent this year, the first increase of any kind in eight years. While the actual price tag of \$4,000 for CUNY tuition may seem relatively modest, such a large single-year jump shocked students and their families.

The factors that have contributed to the price increases are well known. The single most important is that states have reduced their support for institutional operating costs. As my colleagues and I at the Institute for Higher Education Policy pointed out in a 2001 study of college costs and prices for the U.S. Department of Education, that trend actually emerged as a critical issue earlier in the 1990s -- well before the recent double hit of an economic bust and cuts in federal support that has had such a draconian impact on state budgets.

Another important contributor to escalating tuitions is that the market permits it. Even though public-sector tuitions have increased faster than the rate of inflation for more than 20 years, enrollments have continued to ratchet upward. Simply put, the students keep paying, thus allowing tuitions to keep rising.

The authority for setting tuition frequently rests outside of a public university -- with a state governing or coordinating board, the legislature, or some other entity -- so the institution often actually has little to do with setting rates. But the planning and budgeting processes at many colleges haven't helped manage tuition effectively either. Most public institutions still build their budgets by using the baseline of the prior year and simply adding to it, all in the name of increasing academic quality, improving student access, and enhancing overall institutional prestige. Few develop academic plans with any serious consideration of the likely sources and amounts of revenue -- including tuition revenues -- needed to support those plans.

In thinking about how to construct a public-sector tuition policy, states and public universities should tackle such root causes head on. It would make more sense to set parameters for tuition increases and develop different revenue scenarios *first*, and then match those with the different strategic goals of each institution.

Another way to make tuition increases more predictable, and keep them within an appropriate range, is



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### More Need-Based Aid Would Level the Playing Field

Announcements by some states that public-college tuition rates have risen by double-digit percentages for the 2003-4 academic year have generated near panic reactions. In their haste to "do something," unfortunately, policy makers have proposed solutions that are, for the most part, either ineffectual or destructive. While access to higher education for low-income students has never been satisfactory, and state budget cuts present new threats, the fact that students in the top half of the income distribution have to pay a higher proportion of the cost of their education is not a crisis. Quality education is expensive to produce, and someone has to pay for it.

Tuition is increasing because of a combination of the rising cost of educating students and the declining priority placed on higher education in severely strained state budgets. While increased efficiencies in institutional operations are imperative, even they will not eliminate the necessity for more tuition revenue to support quality higher education. Passing laws that punish institutions or deprive students of financial aid at places where there have been large tuition increases will not change the fundamental forces at work. The same is true of proposals that promise to maintain constant tuition levels over specified periods of time.

The danger of rising tuition is *not* that middle- and upper-income students will lose educational opportunities. Regardless of their academic-ability levels, most affluent young people enroll in college, and they will continue to do so even with significantly higher tuition levels. The danger is that low-income students will be increasingly cut off from the opportunities available to others.

The solution is not to hold tuition for *all* students at levels so low that institutions do not have adequate revenues. The solution is to provide sufficient need-based aid to prevent qualified students from being excluded from higher education for financial reasons. A few states have resisted the recent trend toward non-need-based grants and have incorporated increased financing for low-income students into their austerity budgets. All states should design targeted programs that guarantee grants to low-income students. Moreover, students should see those programs in place well before they reach college age, so that student aid is as transparent as tuition bills.

In other words, instead of focusing just on sticker prices, policy makers, educational institutions, and others involved in the college-financing process must clearly publicize available grant aid and call attention to the net prices that students actually pay for college. Although need-based grant funds remain woefully inadequate, growth in both grants and subsidized loans has caused the actual price that students pay for college to rise much more slowly than posted tuition levels. One of the hazards of policies designed to minimize increases in tuition is that the resulting scarcity of funds will lead to reduced money for need-based grants and, therefore, to higher prices for those students who are least able to afford them.

Focusing on net price and need-based aid is the appropriate strategy for mitigating the problem of



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### **Reducing Uncertainty About Costs Would Increase Enrollments**

Public higher-education institutions historically charged zero or low tuition to ensure access. The reasons they have raised tuition are twofold: to be able to compete for faculty members and students with private institutions, where on average tuition has gone up 2 percent to 3 percent a year more than inflation for at least the last 40 years; and to offset reductions in state support. Because revenues per student have not increased as rapidly at public institutions as at private ones, faculty salaries at public colleges have fallen behind, forcing those institutions to increasingly rely on adjunct and non-tenure-track faculty positions, which has surely reduced the quality of public higher education.

Governors, state legislatures, campus leaders, and the public need to have an informed dialogue about whether this situation is satisfactory and, if not, what role state appropriations, tuition policies, and other forms of revenue should play in remedying it. Absent such discussions, I will take our goals to be maintaining -- or, if possible, expanding -- access to public higher education, preventing quality from declining further at those institutions, and reducing uncertainty among students about the tuition costs they will face during their college years.

As we consider how to achieve those goals, we should keep in mind that the well-publicized large percentage increases in tuition at public institutions this year are, in most states, actually smaller in dollar terms than the tuition increases occurring at private institutions. Moreover, for many students from lower- and lower-middle-income families, they are being offset by increased support from federal and state financial-aid programs.

A number of economists have argued that front-loading the federal Pell Grant program (providing larger awards to students in their early college years than in their later years) would increase enrollment rates of students from low-income families, who may be reluctant to borrow before they have successfully completed their first year in college. However, many in the higher-education community, including myself, oppose such proposals because of the fear that front-loading would increase the share of federal aid dollars going to proprietary schools, most of which offer nondegree programs of less than two years.

To accomplish the same objective as front-loading and reduce uncertainty about college costs, public institutions could charge tuition levels that start off low and then increase at a specified rate (known at the time of initial enrollment) during a student's years in college. Low first-year tuition would encourage initial enrollment of students from lower-income families. Higher subsequent tuition would come at a time when those students and their families should be more willing to borrow, while providing the revenue that institutions need to maintain quality. Each year's tuition could be higher than the previous year's by a percentage increase that exceeded expectations of inflation by several percentage points a year. First-year tuition could increase for each new class every year by a similar percentage. Such predictable annual increases in freshman tuition would be far preferable to the practice in many states of freezing tuition for a number of years, which necessitates a much larger increment when an increase is finally permitted.



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### Close the Public-Private Quality Gap

Public colleges and universities around the country have announced double-digit tuition increases. The pattern is familiar during economic downturns, when higher education is more vulnerable to cutbacks than almost all other state-supported sectors. But public institutions should not hold too much hope that the problems facing them will simply disappear once state revenues recover.

The long-term challenges for public higher education have little to do with traditional issues such as faculty salaries and student admissions. The first challenge is the rise in state Medicaid obligations. Our analysis of Medicaid and higher-education budgets in every state from 1980 through 1998 suggests that each new dollar spent on Medicaid crowds out higher-education appropriations by 6 to 7 cents. According to such estimates, the \$120 increase in Medicaid spending per capita from 1988 to 1998 appears to explain most of the \$10 decline in real state higher-education appropriations per capita over the same period. And as the baby boomers retire and health care becomes ever more expensive, state Medicaid costs are likely to climb much higher -- more than doubling as a share of gross domestic product by 2030.

A second challenge comes from demographic trends. Over the past two decades, as the job prospects of those with no postsecondary training have dimmed, the percentage of 18- to 24-year-olds enrolled in college has risen more than a third, from 26 percent to 36 percent. Fortuitously for state budgets, the number of college-age youth declined by about 15 percent from 1980 through 1996. However, over the next decade, as the children of baby boomers increasingly reach college age, the number of college-age youth will be rising in many states. If the proportion of college-age youth enrolled in college remains high (or continues rising!), many states will find themselves hard-pressed to offer the same options to future generations.

In their stewardship of public higher education, state governments have tried to simultaneously keep tuition low for state residents regardless of their ability to pay, maintain access for low-income students, and offer a high-quality public education to all students (who attend community colleges through flagship institutions). With tight budgets and enrollments rising, state leaders are increasingly being forced to choose which of those three commitments they can keep.

Tuition increases produce negative headlines, creating an incentive for state leaders to minimize them. But the stopgap efforts to avoid further tuition hikes have created other problems. Gaps in college enrollments by race and income seem to be widening, in part because many states have not fully offset the cost of rising tuition with increased grant aid for low-income youth.

Also, despite their size, the tuition increases over the past two decades have only partially offset the decline in state appropriations. The result is a largely unnoticed, but quite troubling, deterioration in the quality of public higher education relative to that of the private sector. Public-private gaps in various indirect measures of educational quality -- expenditures per student, faculty salaries, faculty teaching



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### **Public Colleges Should Save for a Rainy Day**

State budget shortfalls have led to often devastating cuts in appropriations to public colleges and universities. To determine whether this is a sign of things to come -- and, if so, whether anything can be done about it -- we need to distinguish between two kinds of reductions: those resulting from the end of our nation's unprecedented economic expansion, which lasted from March 1991 to March 2001, and a less obvious long-term shift in the priorities for public expenditures away from higher education.

Since we have not succeeded in relegating the business cycle to a chapter in economic-history textbooks, considerable volatility in state budgets is likely to stay with us. What is worse, the shift in state priorities that took place in the 1990s -- toward prisons, health care, elementary and secondary education -- means that public colleges and universities will be forced to live with a slice of the appropriations pie that will be too small to continue their basic educational operations. Consider that, in 1980, state and local spending on public colleges and universities amounted to 62 percent of their educational and general revenues; by 2000 that figure had fallen to 51 percent, with the federal government providing an additional 13 percent, mainly in the form of research support. Although presidents of public institutions are eager to follow their private counterparts in building endowments to cushion budgets during recessions, private sources -- gifts and endowment earnings -- accounted for just 3 percent of their revenues in 1980, rising to only 7 percent in 2000. In the same period, tuition revenues rose from 15 percent to 24 percent. It seems inevitable that public institutions will attempt to solve their financial woes by charging increasingly higher tuitions in the future.

Does that mean that we will eventually see public institutions relying on tuition revenues in the same way that privates do? We doubt it. Private institutions still get more than twice as large a share of educational and general revenues from tuition as do publics -- 55 percent vs. 24 percent in 1995-96, the most recent year for which fully comparable data are available -- and, given basic differences in mission and governance between the two sectors, the gap will probably never completely close, even if it will narrow. But when private colleges and universities raise tuition, they often provide more financial aid as well: Assuming the will and the resources, they do not necessarily raise the net price to students from less-affluent families. It is much more difficult to pull that off at public institutions, where much of the government financial-aid budget may be managed by an agency that is financially supported separately from the legislators or the college officials who set tuition.

Particularly worrisome is that state legislatures, obsessed with demonstrating "quality" (which usually means improving the quality of those who enroll rather than of the educational process), have focused on attracting students with high SAT scores. The price of "keeping the valedictorians home" has been an extraordinary rise in merit aid at public institutions over the past decade. The percentage of state financial aid not allocated based on need held steady at 10 percent between 1981 and 1993, but then rose steeply to almost 25 percent in 2000. With striking increases in sticker prices in state after state, coupled with the greater need for financial assistance that inevitably takes place during an economic downturn, less-affluent students face increasingly dire prospects.

