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Upping the Ante for Student Aid

Princeton replaces loans with grants, and the rest of higher education struggles to keep up

By ANDREW BROWNSTEIN

For the lucky few who will make up Princeton University's next freshman class, the university's recent announcement that it was eliminating loans for undergraduates and replacing them with grants was a great relief.

For just about everyone else in higher education, the move seems to have sparked an epic case of anxiety.

That's because the decision, for all its apparent altruism, significantly tilts the balance in what is already an exhausting competition for the nation's elite students.

The student newspaper at Yale University may have put it best when it suggested that a top official, upon hearing the news, "dropped her morning bowl of Grape-Nuts."

At Harvard University, Derek Bok, the former president, posed the issue on the first day of an education class on problems faced by colleges. While most of the graduate students and future administrators in attendance agreed that the Princeton move would benefit some students in the short term, he said, they concluded it was "not a good idea for higher education."

"I think it represents a distressing tendency to focus on the quality of students on the day they arrive rather than on what happens after they get there," he said.

Admissions officials and educational consultants who followed the news spoke in gambling metaphors, predicting an increasingly heated "bidding war."

"It significantly ups the ante," said John Maguire, a one-time admissions director at Boston College and now chairman of Maguire Associates, an educational-consulting firm with more than 40 college clients. "It doesn't change the nature of the game, but it definitely takes things to another level."

Already, officials at the University of Pennsylvania are suggesting they will match Princeton's policies in certain cases.

Last month, Princeton announced that it would break with longstanding precedent and spend an additional \$16-million from its \$8.5-billion endowment in the next year to eliminate loans from undergraduate financial aid.

For most colleges, the move will be impossible to ignore, for reasons both obvious and intangible. "The no-brainer is that the most price-sensitive students are going to do a Jerry Maguire: 'Show me the money,'" said Dan Lundquist, vice president and dean of admissions at Union College, in Schenectady, N.Y.

In other words, why attend Union, or even Yale, if Princeton is offering a chance to attend with no loans attached?

Mr. Maguire -- the consultant -- said that a second, unintended consequence of Princeton's policy -- at every place except a few ultrawealthy institutions -- may be a decrease in the availability of money to help low-income students go to college. Most colleges don't have a fraction of Princeton's endowment, and competitive pressures may push them toward offering more aid to the most talented students, many of whom don't need the help.

"It's a move toward greater stratification, and greater stratification is the exact opposite of diversity, unless you believe in the perfect aristocracy of talent," he said.

The news is still fresh, and most university officials were reluctant to show their hands in the wake of the decision. But among several experts who follow higher-education finance, an early consensus was beginning to emerge about how Princeton's move alters the big picture: The not-so-subtle differences in the endowments and buying power of even Ivy League institutions will be writ large as a handful of top colleges emerge as "super elites"; more colleges, unable to match Princeton, will resort to "preferential packaging" or "merit-within-need" aid to attract top students; and finally, as colleges spend more and more money on luring students to their campuses, there will be increased debate about the resources left to educate them once they get there.

Once the wealthiest institutions -- Harvard, Yale, and Stanford Universities -- act, this theory goes, others will follow, in what Mr. Maguire calls a demonstration of the "domino theory."

Michael S. McPherson, president of Macalester College and one of two authors of *The Student Aid Game: Meeting Need and Rewarding Talent in Higher Education* (Princeton University Press, 1998), predicted a reaction from some of the super elites within the current admissions cycle. "The last time Princeton launched a pre-emptive strike, [Harvard] waited a year, and I think they felt like they were caught with their socks down," he said.

If any of that wealthy trio is planning a move, officials aren't saying so publicly. A Harvard spokeswoman said that if an announcement were made, it would come in late March, when the university sets its tuition.

Andrew K. Tiederman, communications director for the alumni affairs and development office at Harvard, explained that the university currently provides \$57-million in direct scholarship aid to undergraduates -- two-thirds from its endowment and one-third from its operating budget. To go further under the current budget formula, Mr. Tiederman said, deans would have to dip into the same pool from which they draw resources for items like computers and faculty salaries.

"We feel the self-help portion of the financial-aid package is very important," he said. ("Self help," in the euphemistic parlance of financial aid, means loans and work-study.)

A top Yale official suggested that Princeton's move represented a "philosophical shift" away from "the student [shouldering] some of the burden."

"There have been a set of Ivy League principles that have governed the way we have gone about financial-aid policy," Alison Richard, the provost, told the *Yale Daily News*. "Princeton has walked away. It can be considered an excellent thing, or an unfortunate thing." A Yale spokesman said the provost would not comment beyond what was in the student paper.

A Stanford official also declined to comment on whether the university would react to Princeton's plan.

Like few events in recent years, the Princeton move has underscored the vast differences in wealth even among Ivy League institutions. With \$1-million per student, Princeton had the second-highest endowment-to-student ratio in the country in 1999, according to the National Association of College and University Business Officers. (Rockefeller University had the highest, \$7-million per student, but has only 137 students, all at the graduate level.) Compare that with an elite institution down the list like Dartmouth College, which had \$327,000 per student in its endowment, and it is easy to understand why administrators are sweating.

Thus far, the Ivy League institutions, with the exception of Brown University, have retained a commitment to financing the education of all admitted students who demonstrate need, and have been loath to embrace merit aid.

For these reasons, the biggest squeeze, at least initially, is likely to be on the less-endowed Ivies like Cornell, Brown, and Penn, as well as their non-Ivy counterparts like Northwestern and Georgetown Universities, according to Mr. McPherson and Ronald G. Ehrenberg, a professor of labor economics at Cornell and author of *Tuition Rising: Why College Costs So Much* (Harvard University Press, 2000).

"Now these schools have two forms of pressure," Mr. Ehrenberg said. "They have pressure from above to eliminate loans. And they will have pressure from the schools below them that offer substantial merit scholarships and don't have to worry about need. It will be another nail in the coffin of need-based aid."

Observers will be watching these institutions closely because their reaction to Princeton's move may well set the tone for how institutions with lesser resources compete in the new environment.

Penn may have the most to lose. Of its applicants, more students also apply to Princeton than to any other institution. And Penn appears ready to spend more to keep those students.

In an e-mail message to *The Chronicle*, Lee Stetson, Penn's dean of admissions, said: "We will 'come into line' with any financial-aid package offered by both Penn and Princeton after a student appeals to us in April. In this manner, we can compete with the no-loan aspect of their new plan on a case-by-case basis." He would not elaborate.

Experts like Mr. Ehrenberg agree that institutions unable to match Princeton dime for dime will have to be selective about which of their neediest applicants to focus on. This "preferential packaging," which is nothing new to most colleges, could take the form of additional perks: Flying the family to campus, dinners with the president, a research stipend.

Some do this already, even while insisting that they provide aid based only on financial need. Cornell, for example, will replace up to \$3,500 in loans to undergraduates who show promise in the areas of research, community service, and leadership. Almost 1,100 students out of a student body of roughly 12,000 receive such grants through the Cornell Commitment program. Penn has a similar policy.

Or it could take the form of merit-within-need aid, in which loans would be eliminated for a select few.

Preferential packaging often entails a complex calculus in which committees can take months to decide which of their needy applicants they want most. Among the criteria are the usual suspects: Grade-point average, class rank, and, though few like to admit it, SAT scores. Race and gender are also factors. Some colleges award points to students more likely to accept and to those who they expect to fork over the most real money.

This approach raises some delicate questions. Most top students' first choices are not the lower-tier schools that are vying for them. The bidding war might have the affect of alienating others, whom Mr. Maguire calls a college's "bread and butter students."

"It's a huge balancing act, and there are always trade-offs," he said. "It's an ethical question about who you want to subsidize: those who want you the least, but you want the most; or those who want you the most, but you want least. That's a very difficult question, and one that will force colleges to do a lot of rethinking because of what Princeton has done."

It's not the first time Princeton has sent shock waves through academe by radically altering the rules of higher-education finance. In 1998, Princeton changed its formula for need by eliminating home value as a factor for applicants whose families make less than \$90,000 per year, and by replacing loans with grants for students whose families make less than \$40,000.

It took roughly two years for the aftershocks of that decision to reverberate through the system, and it is likely to be the same with the university's most recent move, said Mr. Lundquist, of Union.

The decision has sparked some soul-searching among "the Expendables" the self-deprecating name of a group of Northeastern colleges below the status of the Ivies, including Union, Colgate University, and Trinity College, in Connecticut.

Because of what Princeton did in 1998 and last month, those colleges will soon face a double squeeze on their operating budgets -- from the more-liberal needs analysis that reduces the amount paid by families, and from the necessity of using preferential packaging to compete with Princeton. With less money for supplies, computers, and faculty salaries, the result "could well be a Pyrrhic victory for higher education," Mr. Lundquist said.

"What's left to pay the bills and help colleges be great?" he asked. "Cutting faculty salaries? More aggressive, frequent fund drives? Admitting less-qualified full-pays?"

"Is a cheaper college education a good deal?" he continued. "The answer, at the wealthiest colleges, is probably yes. But for the vast majority of colleges and universities, we are running the risk of discounting toward disaster."

Such dire predictions from the experts beg the question: How did eliminating loans become such a bad thing?

It seems counterintuitive. For several decades, students graduating from elite private universities have complained bitterly about mounting loan burdens.

Certainly, the shift by Princeton spells greater freedom for students entering that university and those institutions that follow its lead. Vanessa Wills, a Princeton junior from Philadelphia, only has one more year to go and will have more than \$12,000 in loans to pay off when she graduates. Still, the change translates into an additional \$4,000-\$5,000 she doesn't have to pay. It also means she'll have a better answer for her fellow philosophy majors when they ask: "But how will I make a living?"

"For a lot of students, it will make a difference in the profession they choose," she says. "I know a lot of people who will go into consulting or i-banking for five years, and then go into what they really want to do."

And so the argument comes full circle. In the end, what is the point of higher education if students can't afford to pursue their dreams upon graduation?

With that in mind, Williams College, which has already garnered national attention for freezing tuition, recently approved a major reduction in the loan burden it asks students to carry. For students with an average family income of \$30,000 or less, the maximum loan for four years was reduced from \$10,000 to \$3,900. The largest loan burden, for families at the \$60,000-a-year-or-above income bracket, was reduced from \$18,000 to \$14,000 over four years.

"Colleges lament that more of their students don't go into nonprofits or K-12 teaching," said Morton O. Schapiro, president of Williams and the co-author of *The Student Aid Game*. "It always occurred to me as an economist that if you don't like the solution, you should look at what the incentives are. And when you saddle people with considerable loans upon graduation, it makes it harder for them to make the choice they might want to make."

Williams's board, which met two weeks before Princeton's decision, briefly discussed the idea of eliminating loans, but decided that now was not the time. Mr. Schapiro explained that Williams and Princeton do not compete for many of the same students and hence, the college will not face immediate pressure to react.

But if the dominoes fall closer to home, that view could change. "If Duke, Brown, or Swarthmore do it, it's a whole different story," he said.

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POINT OF VIEW

Is Princeton Acting Like a Church or a Car Dealer?

By GORDON C. WINSTON

Nothing illustrates the deep economic contradiction in U.S. higher education better than Princeton University's recent announcement that it would eliminate all loans in its financial-aid packages and instead offer outright grants. That's just for undergraduate students. The university also plans to be more generous to graduate students; first-year Ph.D. students in science and engineering will receive full tuition along with increased stipends for living expenses.

Princeton's actions are open to two very different interpretations:

The "Compassionate" Interpretation. The financial-aid changes reinforce and expand Princeton's long-term commitment to base its admissions decisions strictly on a student's qualifications, quite apart from his or her ability to pay, and then provide enough financial aid that he or she can attend. Although it is an expensive approach -- the increasing cost of "need-blind" admissions with full, need-based aid has induced many institutions to abandon the policy -- it is also a noble one. It has made Princeton, like the other top-priced private institutions that still follow the practice, accessible to all qualified students, regardless of their family incomes.

Until now, however, such programs have had a hitch: Some of the financial aid has come in the form of low-interest loans that students have to repay after graduation -- which can amount to \$15,000 or more at an expensive college. That burden may affect some students' choices of course work and careers -- they may take economics instead of classics, or seek out higher-paying but less rewarding jobs, simply so they can pay off their loans. Princeton's new policy allows students to graduate debt-free.

Even while still on campus, students who receive financial aid have different demands from those who pay full tuition and whose college experience doesn't involve loans or work-study jobs. Princeton's largess moves financial-aid students much closer to being just like everyone else in the student body.

The "Competitive" Interpretation. Princeton has just given its undergraduate students who receive financial aid what amounts to a significant price discount. Despite the complaints of parents and legislators about college costs, an institution like Princeton is already a bargain: Even students who pay the full sticker price are covering less than half the cost of their education -- the rest comes from the university's resources, such as private donations and endowment earnings. The latest price reduction, offered through the switch from loans to grants, really sweetens the deal. It will make Princeton the most attractive institution in the country to all those highly qualified kids who need financial aid. Several other colleges may quickly follow its lead, but if they don't Princeton can, for a time, get the pick of the applicant crop.

As for graduate students, Princeton's new policy isn't especially innovative -- it just turns up the heat a bit. Although the compassionate rationale for need-based aid has had little place in graduate-student recruitment, the competitive purpose has loomed large. For decades, Princeton and other elite institutions have been competing for the best and brightest graduate students by remitting tuition and offering handsome stipends. A quick scan last year of the Web sites of leading Ph.D. programs in economics revealed stipends -- in effect, negative tuition

-- that ranged from \$10,500 to more than \$15,000 per year. And lest such support be dismissed as wages for teaching and research assistance, the best students often had no obligations except to excel in their work.

So which is it? Is Princeton's undergraduate financial-aid policy high compassion or low competition? Is the university acting like a charity or a commercial entity, a church or a car dealer?

The churchly nature of colleges is embedded in their missions. Higher-education institutions not only educate leaders and create knowledge, but also encourage equality of opportunity and promote a civil, democratic society. It may seem sophisticated to brush those aims aside in favor of a more hardheaded emphasis on the business aspects of a college. But consider the most bottom-line question of all: Where does the money come from? The answer: Donors and taxpayers are responsible for 75 percent of the educational revenues that American colleges receive. Society's support of higher education -- the appropriations of public money, gifts, and the tax breaks on earnings -- is justified because colleges are, in significant part, organizations that do charitable things like helping low-income kids get high-cost educations.

It's also true, however, that the car-dealer aspect of colleges is more in evidence these days. Colleges clearly make a product (higher-education services) that they sell to customers (students) for a price (tuition). That the price covers, on average for all institutions in the United States, only a third of production costs goes largely unnoticed. And like a car dealer, an institution where people get better quality for their money generates more customers, signaling more success -- as measured as excellence, prestige, or a superior ranking by *U.S. News & World Report*.

In fact, it's the pursuit of such excellence that makes colleges behave like car dealers. Suggesting that you are against excellence is a bit like saying that you are against motherhood and apple pie. But that drive for excellence plays a powerful role in driving the competition, which isn't always pretty.

How does excellence come to have a dark side? First, students educate students -- in discussions that demand, challenge, and excite -- in classrooms, dorms, and coffee shops. Those colleges that want to improve try to recruit smarter students. Even if all else remains the same -- faculty, facilities, location -- when the SAT's of the entering class go up by 200 points on average, an institution will become, and be seen as, better than it was before.

But the universe of exceptionally smart students is limited. So if one college does attract freshman students with SAT scores that average 200 points higher, some other institutions will see their freshmen's SAT's fall. It's a zero-sum game.

Competition for excellence creates a positional arms race -- a college's access to those good students and the educational excellence they bring depends on its appeal relative to other institutions. The institution with the highest quality and the lowest price wins. For a long time, the most aggressive competition to recruit such students took the form of increasing quality -- by improving faculty-to-student ratios, building new facilities and better programs -- which meant higher costs for the institution. But lately, under the prodding of student-enrollment managers, price discounts have increasingly come into competitive play.

So is that what Princeton is up to? Is it jockeying to get more of the high-achieving low-income kids who would otherwise go to Yale or Stanford? It's certainly cutting prices for those very good students. Or is it moving closer to the charitable ideal of admitting all students purely on their merit and then supporting those who need it so that everyone can play on the same field? Is it using its increased wealth to better achieve its churchly mission?

The answer is, uncomfortably, both. It is being compassionate and competitive simultaneously, operating like a church and a car dealer at the same time.

On both grounds, we can expect 10 or so extremely wealthy and influential institutions to follow suit. Princeton's endowment increased by nearly \$2-billion last year, triggering its financial-aid policy change. But

Harvard's endowment leaped by \$5-billion, and Yale's endowment rose \$2.9-billion. Most likely, Amherst, Grinnell, Swarthmore, Wellesley, and Williams Colleges as well as the Massachusetts Institute of Technology and Stanford will be able to spread their wealth in the same way that Princeton has. So highly qualified, low-income students will probably be able to look at all of those institutions without the discouraging prospect of student loans.

Moreover, one has to ask if price competition will be confined to the packaging of undergraduate financial aid. Will the wealthiest institutions be tempted to reduce the sticker price for all undergraduate students? That would clearly improve their ability to compete for the very best students -- including those with considerable family wealth.

And if undergraduate sticker prices are forced down by competition at high-priced colleges, isn't that a good thing? Who wouldn't want lower prices all around -- for the neediest student on financial aid and for the one whose parents earn \$850,000 a year?

It's not clear that it is a good thing. It's not clear that higher education's charitable mission will be well served by transferring money to those who are already rich. My own research suggests that such transfers, in a highly competitive price environment, would be considerable. Indeed, like graduate students and a few isolated programs for freshmen, the institutions that can afford it might not only be forced to lower tuition, but also start to bid for the best and the brightest by paying them stipends to enroll. Aren't there better things -- more in line with their ideals and missions -- that those institutions can do with their good fortune than make elite higher education an even bigger bargain for wealthy families?

There are still other reasons to worry. All that compassion at those wealthy schools will have competitive, car-dealer effects that extend well beyond them. Most colleges haven't had the awesome good fortune of the wealthy elite institutions. Princeton's new policy has sharply raised the cost of doing the right thing by low-income students, and it remains to be seen what effect that cost increase will have on those students' access to high-quality education at the vast majority of other institutions with far less wealth.

Meanwhile, their dual nature -- church and car dealer -- will continue to create crucial and often defining choices for most colleges. A half-century ago, colleges largely dismissed the car-dealer aspect as unseemly and at odds with their higher purposes; now, the danger is that they will dismiss their charitable mission as oldfashioned and sentimental. The economic reality, however, is that neither church nor car dealer will win the soul of higher-education institutions. The tension between the two is built into colleges' basic economics, and institutions ignore either aspect at their own peril.

Gordon C. Winston is a professor of economics and a member of the Project on the Economics of Higher Education at Williams College. Papers on related topics are available at <http://www.williams.edu/wpehe> <http://chronicle.com>

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