Recession, Retrenchment, and Recovery:
State Higher Education Funding
& Student Financial Aid

Recession, Retrenchment, and Recovery: A Review the Literature

A Joint Project of SHEEO, NASSGAP and ISU
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The purpose of this document is to provide background from relevant policy research, economic analyses, and policymakers' perspectives regarding the impact of recessions on the financing of higher education. Many disciplines - education, economics and political science –investigate and attempt to explain the impacts of recession and the process and timing of recovery on the levels of higher education funding. The literature from these disciplines includes such diverse elements as the different state methods for funding higher education; state political structure and locus of control; state tax structures; governmental and societal philosophies about higher education; government intervention and belief in markets; and the hierarchy of influence on state policy and funding. This review provides a solid foundation for the *Recession, Retrenchment, and Recovery* project.

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Review of Selected Literature

The purpose of the *Recession, Retrenchment, and Recovery* project is to identify states that have successfully maintained financial access to postsecondary education for their students throughout economic cycles and to collect and disseminate policy strategies used by these states to help bridge these cycles. The project includes three phases: an analysis of historical state funding data for higher education and student financial aid, including a review of the literature; a survey of state higher education and student financial aid officials; and in-person interviews of selected state higher education policymakers.

Much has been written about the impact of recession on state higher education and student financial aid funding and the resulting effect on student financial access to higher education. Most particularly, forecasts prior to the turn of the century and studies generated in response to the economic downturn commencing in 2001 have produced dire predictions about higher education opportunity given the status of state funding demands, tax structures, and value given to postsecondary education.

Many disciplines - education, economics and political science among them – investigate and attempt to explain the impacts of recession and the process and timing of recovery on the levels of higher education funding These would include such diverse elements as the different state methods of funding higher education; state political structure and locus of control; governmental and societal philosophies about higher education; government intervention and belief in markets; and the hierarchy of policy and funding levers available.

The project team initially suggested that literature relating to higher education finance, student financial aid, economic recession, and student access to higher education be reviewed. References were provided from a symposium on higher education finance held at Illinois State University in April 2004, which served as the inspiration for this project.

In addition to an electronic search on the related topics and visits to websites of major policy centers, institutes, consultants and policy think-tanks, the *Chronicle of Higher Education*, *Journal of Student Financial Aid,* and the papers presented at the last five National Association of State Student Grant Aid Programs annual research conference were reviewed. This report provides a synopsis of selected studies that, for the most part, were published since 2000 and reflect the current economic environment as well as some earlier important seminal studies.

The literature surveyed for this review focuses on several broad areas. The first contains articles that attempt to broadly define the funding issues. Using historical, economic and forecasting approaches, the selected authors examine the decline in higher education funding and assess the outlook for recovery. A second broad category of literature reviewed attempts to define the parameters and detail the workings of the higher education funding process. This also includes literature identifying the core beliefs that govern these processes such as beliefs about states' responsibility for providing college access, and about the effective allocation of resources through markets.

The third category of articles reviewed describes the tension among the various parties in higher education that compete for the dollars allocated to the entire higher education system in each state. The tension caused by competition for state appropriations among the sectors of higher education is one obvious tension but others exist as well – such as the desire for state legislatures or Governors to control higher education dollars by attaching "strings" and implementing accountability measures. A fourth category of articles examines the current environment and new funding strategies which have been implemented or are under consideration.

Recession, Retrenchment, and Recovery

Funding for higher education, like many organizations supported by state tax revenues, varies with economic cycles. There have been five recessions in the past 30 years and most higher education systems have weathered these storms by making temporary spending adjustments and increasing tuition until state funding recovered. However, higher education observers suggest that the most recent recession and its aftermath indicate that public priorities and states' ability to support higher education may have changed significantly and that previous funding levels may not be restored.

Not Just another Recession

In "For Colleges, This Is Not Just Another Recession," David Breneman (2002) notes that "Every decade since 1970 has opened with a recession" but asserts that:

> …[A]s we work our way through yet another one, we should not complacently view it as just one more turn of the cycle. What distinguishes the recession of the early 2000s from previous downturns is that it is posing much more serious questions about the values of our society and the strength of our commitment to educational opportunity. Those questions involve fundamental issues about affordability and access for all qualified students.

Breneman pointed out that the recession of the early 1970s was due to economic stagflation – slow economic growth coupled with rising inflation. The era was characterized by low productivity gains, an energy crisis, and serious unemployment issues for college graduates. Faculty members saw declining real incomes; college enrollments continued to rise but at slower rates. It was also, however, the time of the Education Amendments of 1972 that made the federal government a significant provider of aid for low-income students. The Federal Pell Grant program was implemented (then called Basic Educational Opportunity Grants) and student loan programs were expanded. Breneman notes that "The nation pursued a commitment to ensure access to higher education for all qualified students."

IDENTIFYING THE FUNDING PROBLEM

Breneman (2002): Recent recession not like the past.

Time Period	**Economic Disturbance**	**H Ed Approp /State Rev**	**College Enrollment**
early '70's	stagflation	increased	low growth
early 80's	stagflation	increased	low growth
early 90's	recession	decreased	decline
early 00's	recession	decreased	high growth

Conclusion: Higher education cannot depend on state revenues increasing in the future, regardless of demand.

Hovey (1999)/Boyd (2002)

Forecast state structural deficits over decade (state tax revenues < state obligations)

Slow-growing tax revenues because

- no sales tax on services
- no sales tax on Internet purchases
- lack of state income taxes in 10 states
- small increase in capital gains, excise taxes

Rapidly-growing state obligations

- big appetite for services
- growth in entitlement programs

Impact on state finances

- 39 states (Hovey); 44 states (Boyd) will have structural deficits over the next decade

Impact on higher education funding

- % of revenue devoted to higher education will fall in most states
- Higher ed will have a "balance wheel" function in state budgets

The recession of the early 1980s resulted from foreign competition and schools received much of the blame for our lack of competitiveness – the Secretary of Education's report, *A Nation at Risk*, was published in 1983. Colleges raised tuition sharply to counter high inflation and falling enrollments and in the process of doing so, discovered that students' demand for education was relatively inelastic, they continued to buy even when prices rose. Following this realization, it was not surprising that college prices continued to rise and private schools implemented a new tuition policy – the beginning of the high tuition/high aid model. Higher education had entered the market economy.

Breneman identified the end of the cold war and reduced defense spending, along with more foreign competition, as helping to induce another recession in the early 1990s. Between 1991 and 1992, for the first time, state appropriations for higher education declined. Schools responded by increasing tuition and were actively encouraged to do so by many governors. While the "high-tuition/high-aid" policy was officially adopted in some states, during recessions the "high aid" part failed to materialize and enrollment declines were documented. Other pressing needs for state dollars began to grow – prisons, K-12 education, roads, Medicaid and pensions. As a result, the states' share of public higher education revenues continued to decline.

The shift was noticed by public university presidents who commented, "We used to be state-supported, then we became state-assisted, and now we are state-located." Others observed that they were leading a new type of institution: "privately financed public universities." Governors supported tuition freezes and rollbacks to address concerns about affordability for politically active middle class families. The rise of merit aid, tax credits and college savings accounts were devices to help middle- and upper-income families pay for college.

The dot-com bust of the early 2000s was the beginning of the latest recession, after nearly a decade of economic growth. The financial impact on colleges from this recession was the most severe. Tuition increases were at 15 to 30 percent to compensate for budget cuts resulting from large state revenue deficits – twice the level of the last recession. Raymond Scheppach, former director of the National Governors' Association, observed that the tax base that states rely on was designed for the manufacturing economy of the 1950s, not the service oriented economy of the 21st century. Washington has shifted social service obligations to the states. Private schools are in jeopardy as well – with those at highest risk being poorly endowed, tuition-dependent colleges with enrollments under 1,000.

Breneman noted that the number of high school graduates will increase, with the largest public high school graduating class ever in 2008 – 3.2 million students. The recessions of the '80s and '90s did not deal with increasing enrollment.

States have "clearly failed to learn and adapt to the underlying economic realities," Breneman, 2002. The political environment precludes taking a longer view, thereby subjecting government to the vagaries of the annual budget cycle. Further, institutions focused on new revenue streams rather than cost control. The "dysfunctional response of slashed higher-education budgets and sharp increases in tuition appears destined to continue."

Breneman noted that fundamental reform of state tax codes is needed. Most states need tax changes – basic tax fairness, which includes income taxes in states without them and taxes on services and the Internet. If coupled with changes in institutional efficiency and productivity, tax changes could minimize or erase the structural deficits now foreseen for higher education.

Retrenchment: Shifting Costs to Students

According to Pat Callan (2002) in *Coping with Recession: Public Policy, Economic Downturns and Higher Education*, formulas for setting tuition were early victims of a recession and the steepest tuition increases in the public sector occurred during recessions as states seek to shift their costs to users, including students and their families. Callan believes that higher education absorbs larger cuts when revenue shortfalls are allocated among state services and these costs are then shifted by the schools to the students. At the same time, no new financial aid will accompany the cost increases; in fact student aid may be reduced.

Although the early 2000s were not good years, they were cushioned somewhat by the robust good health of higher education during the late 1990s, Callan, 2002. However there are new considerations that will make future recessions harder: higher enrollments in general and of poorer students in particular; the different impact of higher education costs depending on one's generation – one generation attends school during "good times" with small tuition increases (or even tuition cuts) and generous financial aid; then the next generation attends during the bad times and encounters double digit tuition increases and cuts to financial aid. Also in the future the mismatch between the current public policies and students' needs will be exacerbated. Most of the recent increases in student aid have been for the middle class in the form of merit aid and tax credits. Most of the projected increase in numbers of students will come from families not able to take advantage of those programs.

Outlook for Recovery: Structural Deficits

Harold A. Hovey, in his prescient 1999 report, *State Spending for Higher Education in the Next Decade: The Battle to Sustain Current Support*, wrote that many states were headed toward structural deficits. The problem was clearly not as obvious in 1999 as it would become over the next 10 years. His fiscal forecast of state and local spending patterns indicated that, before the end of the first decade of the 21st century, only 10 states would have budget surpluses; one would have neither a surplus nor deficit; and 39 were projected to have structural deficits. Hovey added,

> Assuming that higher education were merely to share equally in the fiscal pain of helping states respond to their structural deficits (rather than being singled out for additional cuts, a 'balance wheel' function that higher education has served in the past) then, based on national averages higher education would not see expansion of spending patterns for any program except as financed by reductions in other programs within total higher education spending...

It was also noted that "at the same time that states will be facing structural deficits, [they will be] seeking to fund new initiatives in many state program areas outside of higher education, confronting the difficulty of cutting current services in these other program areas, and confronting the difficulty of raising taxes," Hovey 1999.

Hovey suggested the following outcomes of the predicted structural deficits:

1. Structural deficits will not be allowed to grow as large as forecasted because unbalanced budgets are generally not allowed, restricting cumulative deficits.

2. While spending reductions are assumed to be used to reduce deficits, tax increases are also possible. However, it is possible that taxes will be applied on items generally not responsive to economic growth, such as further taxes on goods rather than taxes on services or higher income taxes.
3. Spending will shift further from public spending to private spending. The increase in tuition and fees is one example of this shift.
4. States may require private spending for public purposes similar to the lifeline rates now offered by some utilities that are partially subsidized by other customers' rates.

Don Boyd (2002), in *State Spending for Higher Education in the Coming Decade* suggested that

> [E]ven if state and local governments close their current budget gaps with entirely recurring actions, rather than gimmicks that provide only temporary relief, most states will face continuing difficulty financing current services with existing revenue structures, and will not have resources for real increases in spending. Given that state and local governments have increased real per-capita spending significantly in each of the last five decades, this suggests citizens will have to either scale back their appetite for government services or support changes in revenue structures to finance new growth.

Within eight years from the time state and local governments close current budget shortfalls they are likely to face gaps that for the nation as a whole approximate 3.4 percent of revenue, Boyd, 2002. A total of 44 states face gaps under these assumptions, with 12 states facing gaps of 5.0 percent or more of revenue. While these gaps are smaller than the current crisis-induced gaps in many state budgets, the shortfalls have resulted from swift sharp shifts in the economy and financial markets. It was suggested that even after this crisis, states and local governments will face continuing stress.

Boyd cites two main problems for states' financial difficulties. First, spending in many states will be boosted by rapid growth in Medicaid, the health insurance program for the poor and medically needy. Second, tax revenues will not grow as fast as the economy due to projections of balanced economic growth. Unlike the late 1990s, the economy will not generate annual surges in capital gains income and there will be a significant slowing of sales tax revenue due to continued shifts in consumption from goods to lightly taxed services. He also expects tax revenue losses due to the difficulty of collecting taxes on Internet-related transactions and growth in excise tax revenues that will not keep up with overall economic growth.

Boyd summarizes his findings by stating,

> ...[F]or the nation as whole, state and local governments in aggregate are projected to face a gap of 3.4 percent of revenue at the end of eight years. Personal income, a broad measure of the

> economy, is projected to grow at an annual average rate of 5.1 percent. State and local spending needed to maintain current services is projected to grow a bit more slowly than the economy, at an average annual rate of 5.0 percent. Revenue, by contrast, is projected to grow considerably more slowly than the economy, at an annual average pace of only 4.5 percent.

He concluded that, “For the nation as a whole, higher education spending is projected to grow 40 percent over the 8-year period, considerably slower than the 47.4 percent growth projected for total spending – about 0.7 percent slower per year. Higher education is expected to grow faster than total spending in only 8 states and slower than the total in 42 states.”

Aligning Policies and Decisions: Appropriations, Tuition, and Student Financial Aid

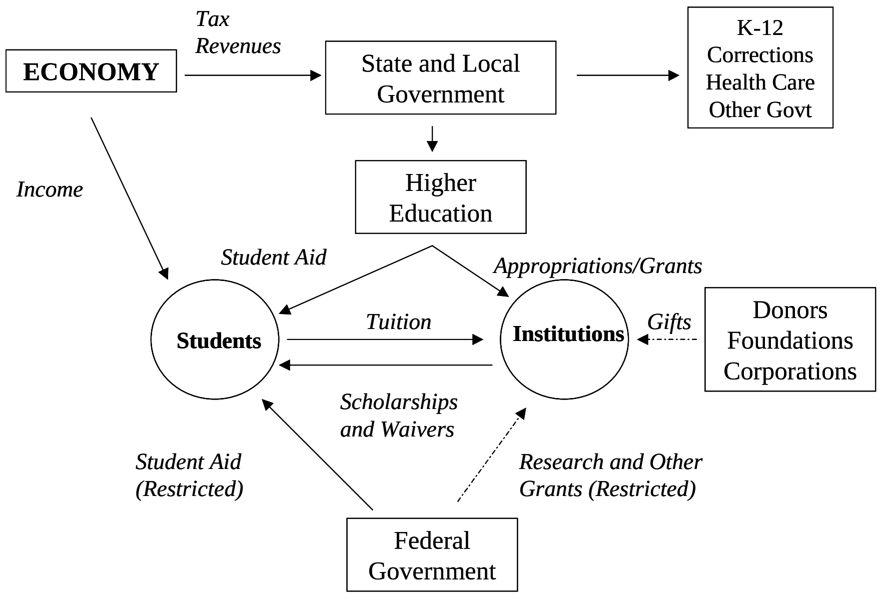
If predictions are accurate, the quality of higher education and the promise of inclusive access to opportunity may be at risk. In developing strategies for maintaining support for higher education, consideration should be given to how funding decisions are made and alignment of higher education’s needs with state policy goals and directions.

Funding as a Policy Tool

Dennis Jones’ (2003) purpose in “Financing in Sync: Aligning Fiscal Policy with State Objectives" was to “identify the distinct elements of financing policy, describe alternative forms of these elements, and illustrate the alignment of these policies in the context of alternative state priorities.” He concludes that “funding – with regard to both the levels and the methods by which resources are distributed – is the dominant policy tool used to affect higher education institutions and the outcomes they produce.” Financing is also a flexible tool because funding decisions are generally revisited each year by the legislature. Financing can act as both an incentive as well as a deterrent, containing elements of both the carrot and the stick; while rules tend to be viewed as completely negative.

The policy levers of higher education funding are identified in Figure 1. Jones (2003). Appropriations, defined as payments “made directly to institutions for support of general operations,” are subdivided into three categories: base institutional funding “for creation and maintenance of the educational capacity of the institution”; special purpose funding to “promote utilization of this capacity in ways designed to achieve state priorities (performance or incentive funds)”; and appropriations for capital additions or renewals. In addition to appropriations, other policy levers are tuition and fee policies (establishing “sticker prices” and policies on fees); state student financial aid policy (both need and merit based); and institutional financial aid of all types.

Figure 1
Overview of the Higher Education Funding Process



From "Aligning Fiscal Policy with State Objectives", page 7

Policy levers are almost never considered together but are usually managed in isolation and in no particular sequence. Jones (2003). Since these levers are manipulated by different entities they are also manipulated with different goals in mind. Generally, the goal of state legislatures is to control spending, while the institutions are attempting to maximize revenue and to provide resources to improve institution quality and status.

This piecemeal approach to higher education policy leads to an array of counterproductive outcomes, including reducing state support to schools during recessions causing tuition to rise; administering financial aid as fee waivers making recipients ineligible for tax credits; not integrating federal Pell grants into state needs analysis formulas; discounting tuition for students who would enroll and pay anyway; and holding tuition levels artificially below what most students would be able to pay, thereby eroding quality. Jones (2003).

To reduce the number of counterproductive outcomes, Jones recommended that financing policy reinforce state priorities; that states ensure institutional capacity to meet priorities; that tuition be affordable for most students; and that transparent funding mechanisms and fair treatment of all parties be encouraged.

Governance and Policy Goals

Kenneth P. Mortimer (2004) in "The Governance Context for State Policies on Appropriations, Tuition, and Financial Aid" outlines four key questions that can be asked to identify "the patterns and principles of governance in the states that are useful in describing the range of political behaviors that prevail" when decisions about appropriations, tuition and financial aid are made.

1. "What decisions are made about appropriations, tuition and financial aid?" Mortimer noted that "appropriations decisions cannot be separated from those made about the entire state budget." Decisions about taxes and the pressing demands of other functions of state government influence the appropriations, tuition and financial aid decisions as much or more than the split between the various types of appropriations to higher education.

2. "Who makes these decisions?" While all states have some process in place for approving appropriations, the authorities designated and the amount of control distributed varies from state to state. Most states "retain the authority to appropriate funds; the delegation comes variously on how to spend the monies appropriated." "Approximately 24 states have governing boards, 24 have coordinating boards, and two have planning agencies" to perform that function.

3. "What beliefs or assumptions are evident when these decisions are made?" and,

4. "What policy goals underlie these decisions?"

Mortimer identifies four separate policy roles that states may assume when determining appropriations for higher education. States may view themselves as providers and subsidize higher education "with little regard for the market." Or they may act as regulators by "controlling user charges and constraining institution discretion in the use of appropriations." Some states act as consumer advocates by redirecting at least some appropriations away from institutions into the hands of the student consumer. Or they may see their role as one of steering markets to "produce outcomes that are consistent with state priorities."

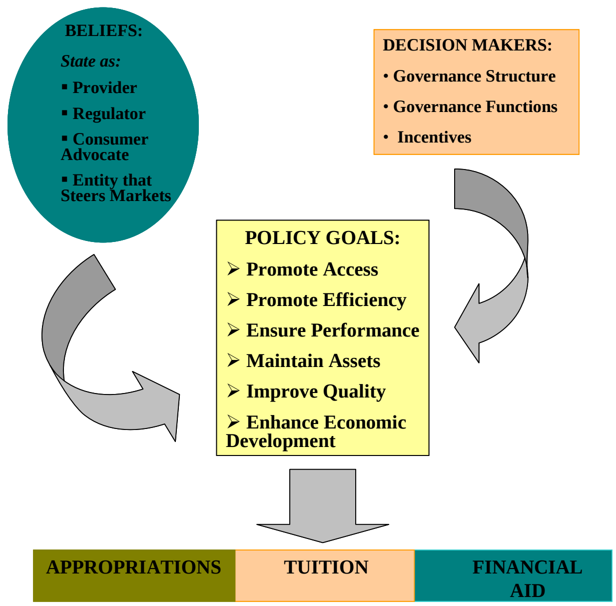
Mortimer suggested that direct appropriations may undervalue the total dollars going to postsecondary education. "In some states legal costs are included in the attorney general's budget." Other states put some fringe benefits (such as state cars) into other budgets. Debt service is often found in the general state budget.

According to Mortimer, appropriations, tuition and financial aid decisions are affected by:

- Governance structure: statewide policy boards, multi-campus boards or institutional governing boards. State policies set the hierarchy and decision making authority of each board.

- Governance functions: The Governor often has "more influence over the actual expenditure patterns after the appropriations are made than he may have over the appropriations process itself."
- Incentives: Who sets tuition and who keeps it? In Hawaii, the board set tuition and the state legislature felt the rate set was too low; it took over the process and tuition rose 50 percent. Many states have done the reverse – put the brakes on tuition increases proposed by the institutions.

Figure 2
Influences on the Higher Education Funding Process



Source: Kenneth P Mortimer, "The Governance Context for State Policies on Appropriations, Tuition, and Financial Aid for Higher Education, 2003

Mortimer identifies seven goals for the appropriation process: (1) promote access, (2) promote efficiency, (3) ensure performance, (4) maintain physical and human assets, (5) improve quality and prestige, (6) enhance state's economic development (support medical schools, engineering programs, high tech programs), and 7) promote a political/reform agenda such as literacy development or economic development. That these goals often conflict is obvious; the selection of goals and hierarchy of the selection can have profound impacts on the higher education funding process.

Three goals for tuition charges were identified: (1) affordability, (2) close revenue gaps, and (3) support differential missions and costs. In tandem with these goals are three for financial aid: (1) maintain affordability, (2) reward performance, and (3) stem the "brain drain." Again, these goals conflict and the selection and ranking of the goals determines the private/public split of higher education costs and the costs borne by students coming from different socioeconomic sectors.

Legislative Perspectives and Priorities

In *Linking Tuition and Financial Aid Policy: The State Legislative Perspective*, Julie Davis Bell (2003) wrote, “The rapidly changing demographic makeup of our population, projected growth in higher education enrollments, stagnant state economies, and increasing turnover among policymakers all point to the need to rethink how we finance higher education and how we ensure that the most economically challenged among us do not experience decreased access and choice options for postsecondary education.” Bell’s survey of legislators was commissioned as part of a larger project, *Changing Direction: Integrating Higher Education Financial Aid and Financing Policies*, at the Western Interstate Commission for Higher Education (WICHE) for the purpose of exploring the linkages between state funding and student financial aid policy. It received responses from 44 legislators from 29 states (including most of the “big” states except Texas, Indiana, New Jersey, and Minnesota).

Legislators saw a “distinction between the tuition policy process and the student financial aid policy process” and did not report a great deal of coordination “between the key state policymakers and educators on tuition and financial aid issues.” Overall, the legislators that responded were not critical of the process nor did they have frustrations with it. Although legislators “feel hampered by the economy in their policy decisions,” overall, most felt that their states’ tuition policy process and the student financial aid policy process were “fair, flexible and equitable.”

Only about half the respondents indicated that their state legislature had an overall philosophy regarding tuition and financial aid and of those, most indicated that this philosophy was always a consideration in policy making. However, policy concerns tended to be short-term and the legislatures most often dealt with “current issues rather than address issues in the long term.”

The legislators were asked to determine the relative significance of the roles of the legislature, the governor, and the higher education community in setting tuition policy and state student financial aid policy. Overall, respondents indicated that they had the most significant role of all policymakers regarding student financial aid policy while higher education governing boards were the most influential in setting tuition policy. Relative to the governor, legislators indicated their role was more significant on both tuition and financial aid policy.

The legislators who responded suggested their states ran the gamut in financial aid philosophies. While some suggested that no philosophy dominated, the majority listed one of the following: high tuition/high aid; low tuition/low aid; medium tuition/high aid; low tuition/high aid; low tuition/adequate aid; moderate tuition/moderate aid; “no qualified student should be excluded for financial reasons”; low tuition/high aid for students who need it.

Factors influencing state financial planning included the reality that "economic forces dictate fluctuations in tuition and student financial aid" expressed by nearly all respondents in some form, and the acknowledgement that funding is restricted by "state tax limitation structures" and "state political culture." Other practical factors included the number of applicants, job opportunities for graduates and the availability of federal funds. On a more philosophical level was the conflict between the competing ideas of need versus merit aid and the desire to target grant aid to certain populations.

Sobering answers were given to the question of what issues were likely to be before the legislature during the next two years. About 80 percent of the respondents indicated that decreasing the overall share of the state higher education budget would be discussed and 95 percent indicated that tuition increases would be on the agenda. Other topics of interest included limiting in-state tuition rates to four or five years; establishing different resident versus nonresident rates; linking tuition increases to family income or the CPI; having different tuition charges for different programs; increasing taxes to offset tuition increases; increasing need-based aid; increasing merit-based aid; achieving a better need/merit based mix of aid; shifting funds from institutional support to student financial aid programs; and performance funding.

> Some states are investigating new relationships with students and institutions that may offer new policy solutions. Colorado has been looking at how to fund students rather than institutions and how to provide more flexibility for public universities when setting tuition. Texas has been examining additional flexibility for institutions. South Carolina and other states are experimenting with greater use of performance funding.

Student Financial Aid: Access, Affordability, Need, and Merit

While demand for higher education tends to increase during recessions, there are growing concerns about students' ability to pay for college. States can influence or control both sides of the affordability equation – tuition and fee policies and student financial aid programs. Higher education observers have raised concerns about shifts from need-based to merit-based programs and the consequences for low-income students.

States' Contributions to Affordability

Mortimer (2004) observes that student financial aid provided by states is only a small fraction of the total financial aid budget. "In fiscal year 2001, state financial aid was only 7 percent of the total governmental financial aid available to students. Of the $74.3 billion available in financial aid, 68 percent ($50.7 billion) was federal, 19 percent ($14.5 billion) was institutional aid, and 5 percent ($4 billion) was private sector loans. Six states (CA, IL, NJ, NY, PA and MN) awarded $2.1 billion in need-based aid – 59 percent of the total."

Other forms of aid that are not normally reported in national data include $27.6 billion in non-grant forms, such as loan forgiveness, work-study and special scholarships. Another $525 million was given to students by state agencies other than the primary student aid agency, and state guarantee agencies guaranteed $25.9 billion in new federal loan volume.

Social Contract: Access and Affordability

According to the Commission on National Investment in Higher Education, "At a time when the level of education needed for productive employment is increasing, the opportunity to go to college will be denied to millions of Americans unless sweeping changes are made to control costs, halt sharp increases in tuition, and increase other sources of revenue." *Breaking the Social Contract: The Fiscal Crisis in Higher Education*, (1998). The Commission pointed out the following fundamental problems that threaten our society unless higher education is made more accessible:

- Some form of postsecondary education has replaced the high school diploma as entry into rewarding employment.
- Disparity between rich and poor will grow and threaten core democratic values unless we improve education levels.
- Higher education is facing a 'catastrophic' shortfall in funding. Deficits in operating expenses for the nation's colleges and universities will quadruple by 2015. If tuition increases no faster than inflation, the shortfall will be about $38 billion; if tuition increases at current rates, half of those who wish to pursue higher education will be shut out.

The Commission's asserted that increasing public investment and holding the line on costs is essential to accessible postsecondary education. Public funding of higher education has stagnated since 1976 and the Commission said it is time to make it a priority. Cost containment is also essential and can be achieved by changes in the higher education paradigm, specifically:

- Institutions need to make fundamental changes so that departments and programs become more flexible.
- Colleges and universities should differentiate missions.
- Colleges and universities should develop sharing arrangements to improve productivity.

Other observations by the Commission indicate that the failure to provide sufficient opportunity for postsecondary education would be to relegate large segments of society to minimal existences. Many of these families will be nonwhite. The immigrant population with little or no education is increasing; Hispanic students participate in higher education at about one half the rate of white students. In 1976, 90th percentile income families had incomes 9 times that of the 10th percentile families; projections indicate that by 2015 it will be 16 times greater.

Jillian Kinzie and others (2004) in *Fifty Years of College Choice: Social, Political and Institutional Influences on the Decision-Making Process* provides an historical account of the composition of college students and observes that decision-makers in higher education, families with college-age children, are sometimes overlooked. While the college-choice process has changed over time, there has also been "…a shift in focus regarding who benefits the most from higher education – the individual or society as a whole – directly affected public policy, institutional practices and students' college-choice decisions…."

Shifts in belief about who should attend college, social changes regarding gender and race, and the changing demographics of students attending college all affect how college is financed and what types of postsecondary education are favored. For example, the belief that minorities and women were denied access to higher education prompted greater government intervention and support during the 1970s; currently the perception that a college degree is disproportionately a private good may explain, at least in part, the reluctance to increase state funding for higher education.

Need-based and Merit Programs

Is college access for all still a priority for states? According to Edward St. John et al., in *Expanding College Access: the Impact of State Finance Strategies*, (2004) states still have the primary responsibility for financial access to college. After evaluating parameters of financial access - demographic contexts, financial controls, system capacity of the state system (percent enrollment) and higher education finance strategies (public sector tuition, need-based grants and non-need grants during the freshman year) - St. John concluded that "need-based grants had a stronger influence on enrollment rates of any variable tested…"

> States have the primary responsibility for ensuring financial access…. The early economic studies of college access documented that student financial aid had a direct influence on enrollment. However, the old consensus behind this research broke down after the net price concept used in these studies did not adequately explain the impact of new finance policies that influence access. St. John et.al. (2004)

Thomas R. Wolanin (2001) in *Rhetoric and Reality: Effects and Consequences of the HOPE Scholarship* describes a substantial shift in financial aid funding in favor of the middle class, even if it comes masked as student merit aid. He states,

> As college prices continue to rise above inflation rates and most measures of income, mechanisms to reduce the burden of paying for college gain greater support. …The passage of the Taxpayer Relief Act of 1997 represents a watershed event in the relationship between student support and tax policy. The Act's signature initiative, the HOPE Scholarship Program, provides annual benefits to

> students and their families rivaling the support provided through Pell Grants and other long-standing forms of federal student aid. Such a significant investment in taxpayer-funded support to aid students through the U.S. Tax Code is unprecedented.

The HOPE Scholarship and Lifetime Learning Credit account for 93 percent of all the benefits to individuals in higher education provided by the Act.

> In short, the HOPE Scholarship is simply a windfall to middle-income families. On the other hand, low-income families who face the greatest and most rapidly growing burden from college prices, receive no help from the HOPE Scholarship. …there is no evidence to date that the HOPE Scholarship increases enrollments in higher education for any income category of students or potential students.

HOPE Scholarships give aid to those who will attend college whether they receive other aid or not.

The National Policy Center for Higher Education's *Losing Ground: A National Status Report on the Affordability of American Higher Education* (2002), examines five national trends that are reducing access to college, particularly public colleges, for students from both lower and middle-income families:

- Increases in tuition have made colleges and universities "less affordable for most American families." Increases in tuition and fees have outstripped gains in family income for all but the wealthiest families.
- Federal and state financial aid to students has not kept pace with increases in tuition.
- More students and families at all income levels are "borrowing more than ever before to pay for college."
- The steepest increases in public college tuition have been imposed during times of greatest economic hardship, when families are least able to pay.
- State financial support of public higher education has increased, but tuition has increased more.

The tension between financial aid for lower-income students and the middle- and upper-middle class appears to be growing as the cost of college continues to increase faster than inflation and family incomes. The report concluded: *"regarding the affordability of a college or university education … Americans are losing ground."*

Trends and Consequences

As funding patterns change, there may be fundamental changes in some of the long-valued tenets of higher education. Concerns have focused on the lost of broad access for students to higher education. Declining state support may also lead to fundamental changes in how institutions are operated, particularly public universities.

More Demand, Less Opportunity

Jane Wellman (2002), in *Weathering the Double Whammy* described how governing boards of public and independent colleges are handling the cuts in higher education that have come from state revenue shortfalls at a time when the baby-boom echo and independent students unable to find employment during times of recession are driving up enrollments:

> State revenue shortfalls are resulting in cuts for higher education; the baby-boom echo is entering college; myriad immigrants and first-generation college students are now seeking higher education; and millions of current workers need to upgrade their skills…the challenge of doing more for many more with much less.

Schools have responded by "raising tuition; delaying capital outlay projects; freezing new hires; redirecting special revenues to general fund accounts; increasing employee contributions to their heath care plans; eliminating programs; sweetening incentives for early retirement; and laying-off employees. …nearly all [institutions'] have instituted one or more of those strategies."

Wellman advised that these are short run solutions when long-term resource management strategies are needed. A five step process was recommended:

1. Identifying the institution's challenges, both short and long term. Short-term problems respond to short-term solutions such as hiring freezes but long term, structural problems need to be addressed differently to ensure support for faculty and students.
2. Refocusing the institutional mission to take advantage of opportunities budget crises sometimes bring. In an era of deregulation and accountability (performance oriented budgeting) boards can gain control by "replacing rigid line-item budgets with block funds…and carryover budget authority….."
3. Assessing and integrating the institution's tuition, aid and outreach strategies.
4. Strengthening the commitment to cost management and cooperation.
5. Paying attention to enrollment planning and management. Wellman recommends that "boards pay particular attention to improving college-going rates among members of traditionally underrepresented constituencies."

Joseph Marks and J. Kent Caruthers (1999), in *A Primer on Funding of Public Higher Education*, provided an overview of sources of education dollars, the objectives of funding, use funding formulas to distribute funds, and finally, the distribution of those funds. Nationwide, about 40 percent of public four-year institutions' general operating budgets comes from state appropriations and an additional 24 percent from tuition and fees. The remainder comes from contracts and grants and other sources, including private gifts. The dollars are spent on instruction (37%), research (15%), support (23%), grant aid (8%), maintenance (7%) debt service (4%) and other miscellaneous (6%).

Funding priorities have changed during the past five decades. In the fifties' the priority was adequacy; the sixties' was growth; the seventies' was equity; the eighties' was stability and quality; and the nineties' was stability, performance, reform. The shifting objectives have given rise to different funding formulas. In this report, the current formulas in the 10 states in the Southern Regional Education Board were compared as to the roles of state agencies, the governor, and the legislature in their implementation. The differences in their implementation roles were significant and illustrate the wide range of funding options currently being used and considered.

Privatizing Higher Education

There may be serious societal implications for under-funding education. John Wiley (2004), in "Higher Education at the Crossroads: The Issues Demand a Serious Debate over How to Heal an Ailing System" calculates that we invest about $100,000 to produce a high school graduate. Those graduates will not earn enough to pay back in state and local taxes the cost of their education. Postsecondary education of some type is necessary for most high school graduates and may require new ways of funding to provide the access needed.

Currently public institutions comprise 25 percent of all four-year schools and enroll 65 percent of the students. Public institutions comprise 64 percent of all two-year schools and enroll 96 percent of all students at two-year colleges. Public schools comprise 41 percent of the total and enroll 77 percent of the students. Each taxpayer currently buys a stake in higher education at a rate of about $221 per capita.

Wiley noted that in Wisconsin the taxpayer-funded portion of the University of Wisconsin-Madison declined from 43 percent in 1973 to 21 percent in 2003. The decline was accelerated by a series of mandated expenditure reductions. State officials have been pushing public school education into the private model, specifically, the "high tuition/high aid" version of the private model. But private schools that operate successfully under this model usually have large endowments. The University of Wisconsin-Madison could privatize if it had an endowment of $8 billion and raised tuition to more than $20,000 per year. The current endowment, however, is only $2 billion and much of it is for restricted purposes. Furthermore, Madison is the only public school in Wisconsin with any significant endowment at all. On a national level, about $1.3 trillion in endowments would be required (currently it is $200 billion, including private schools.) Privatizing the public schools on a large scale is not an option as a future financial model.

Some states have tested versions of privatization, with pressure coming from both the state and the schools. Eric Kelderman (2004), in “States and Public Colleges Consider New Relationships,” described four proposals, in Colorado, South Carolina, Virginia and Wisconsin that have at least aspects of privatization. The changes in Colorado and South Carolina would privatize public universities and colleges, allowing them to set their own tuition and fees. In Virginia and Wisconsin, “giving public colleges more autonomy but perhaps less state funding” is gaining traction.

In “The Disappearing State in Public Higher Education”, Jeffrey Selingo (2003) suggested that “Slashing support for public colleges…is part of the ebb and flow of economic cycles. In bad times, state lawmakers use public higher education to balance their budgets, knowing that the institutions can raise tuition rates. Then, in good times, lawmakers funnel money back to the colleges to make up for the down years. It has worked that way for decades. But this time might be different.” The economic downturn of the early 2000s may bring on the “next wave in the privatization of public higher education.” He describes three types of privatization: (1) private foundations to raise money; (2) spinning off part of operations such as hospitals, law and business schools; and (3) encouraging private donations. Selingo’s Piecemeal Privatization table is shown below.

“Piecemeal Privatization” of Public Universities

- Market tuition rates for flagships coupled with less state support
- Education vouchers coupled with less direct institutional support
- Spinning off flagships as independent authorities
- Spinning off parts of the university such as law or medical schools
- Setting up private foundations and encouraging private donations
- University bankrolling of start-up companies
- Public-private partnerships
- Corporate funded research

Some states now want to get out of the business of higher education and some schools are ready to leave. Colorado, South Carolina, Wisconsin and Virginia are a few examples. “[Consumers] want high access, low tuition, top quality and no tax increases to pay for it.” Perhaps funding higher education has become a no-win situation for legislators, and turning it over to the market has increasing appeal.

Today, governors want two things from higher education: cost cutting and quick results. Policymakers were upset after pouring money into the system in the late 1990s; one year’s budget cuts made tuition jump more than it had in a decade. They asked the why colleges are unable to contain costs as other public services are expected to do.

Legislators are beginning to see higher education as a private good and consider $25,000, the price of a new car, a reasonable investment for students and families.. Fund–raising campaigns have convinced legislators that schools can raise their own funds. “At least 16 public universities…have…capital campaigns with goals of at least $1 billion, and many have well surpassed that amount.” The article quotes Paul E. Lingenfelter, executive director of SHEEO, “You never hear of a welfare program that has financial reserves or can raise money.”

Some states are thinking about major changes. In Colorado a voucher-like system would send money to students, not schools; this idea is backed by Colorado institutions that have seen their funding cut dramatically the past few years. South Carolina’s three major research universities want to break away from the state’s coordinating board so they could enter into private-public partnerships (private developers to build conference centers, research parks, etc.) In Wisconsin the suggestion is to turn over the University of Wisconsin system to an independent authority similar to the way the university hospital was spun off five years ago. Smaller privatization endeavors include breaking off the law or medical school. The University of Virginia’s business and law schools have been “weaning themselves from state support.”

Some higher education policymakers fear that talk of privatization may encourage state legislatures to further reduce funding because institutions will then have other options available for funding sources. Robert Zemsky, director of the University of Pennsylvania Institute for Research on Higher Education was quoted as saying that public colleges “are not places of public purpose anymore.”

Disconnecting Flagship Universities

Another view of the problem is chronicled by Ben Gose (2002) in “The Fall of the Flagships,” where protestations of poverty are found where one least expects it. About $7 billion in a permanent university fund makes the University of Texas at Austin and Texas A&M look rich but when the fund is spread over 17 campuses, it is not sufficient to meet their needs. Because Texas has no plan to see that costly (elite) education is maintained and because elite schools are not helping correct the issues that the Texas legislature currently cares about - changing enrollments to better reflect racial diversity and increasing enrollments - these two prestigious universities are in danger of being under-funded. At both institutions most of their students could afford higher tuition; the median family income of their students is $80,000. Other state flagships are experiencing similar problems. The University of Iowa has seen the proportion of its revenues coming from state funds drop from 75 percent in 1914 to 19 percent today.

Gose describes basic survival tactics for flagships: soliciting private gifts, bankrolling new companies derived from university research, gaining state approval to raise tuition to market rates, and trading off state support for autonomy. The University of Michigan, for example, benefited from loose state oversight that gave the university freedom to set tuition. It began endowment hunting early in the 1970s when it was afraid that Michigan would not support a first-tier school. Freedom to pursue other financing or a transparent state plan to distribute higher education financing seems necessary to preserve the quality of the flagship. According to Gose, having a flagship institution is a good thing for a state: “There is not a region of the country that is economically prosperous without a first-class institution.”

Creation of a large endowment could free schools from state politics. Some schools such as the University of California at Berkeley and the University of Virginia have each raised more than $1.3 billion in recent capital campaigns, and UCLA has passed the $2 billion mark. Gose states that, “It may be that we’re creating a super league of very-well-endowed private institutions, and then a second level of public universities that will work out some partnership with the states, using endowment and federal money to create a firmer compact.” There are problems with this approach, specifically that the schools may price out poor students, become beholden to corporations, exacerbate the pay differential by college discipline, and increase power of donors.

Returning to Texas as an example - tuition is tightly controlled by the state and its legislature takes any “excess” revenues. The University of Texas has little incentive to enroll out-of-state students since the state takes 85 percent of revenue it generates. Texas institutions also turn over 50 percent of the indirect costs of research received in federal grants – this rule alone cost the Austin campus $19 million one year. “Legislatures have a very good deal right now… they pay 20 percent and control 100 percent. Why would they give that up?”

A new financial officer at a Texas flagship institution thinks he can save $25 million through greater operating efficiency such as eliminating college cars, consolidating purchases, and eliminating paper. But it probably won’t be enough: “The democratization of higher education bodes well for participation rates but not for flagships.” Texas chooses to spend its money on less selective institutions that can expand to accommodate a larger and more diverse student body and offer a four-year degree at a more reasonable price.

Plans and Strategies

Few states and higher education systems have been able to develop methods for dealing with temporary or long-term changes in funding. Many expect that funding will be restored as soon as the economy cycles upwards and, therefore, make minor adjustments in spending or increases in tuition and fees to get them through.

Planning Ahead

In “Ensuring Access through Integrated Financing Policy,” David Longanecker (2002), argued that while state financial cut-backs pose hardships through reductions in aid and student services, these are usually coupled with increases in tuition and fees. Students and their parents lose out because states do not integrate policies on institutional subsidies, tuition and fees, and student financial aid. He estimates that nearly half of the states do not “fund a real financial aid program” and, of the ones that do, coordination with state tuition policy is missing: “The absence of such intentionally integrated policies in most states means that in tough times, when tuition logically increases, financial aid either declines or remains stagnant. States that truly value access for financially needy students can’t let that happen.”

However, there may be a silver lining to tight budgets because they shed light on possible “moribund and redundant academic and student services and [provide] a way to recast necessary but inefficient activities.” One of the changes Longanecker proposed was to “provide some capacity or incentive for institutions to plan ahead for variations in state funding.” He also observed that “…most of our public institutions have little ability to weather substantial funding fluctuations without reducing services in one fashion or another.” A variant on this approach would be to “allow institutions, within reason, to bridge funding reductions by borrowing and then repaying this indebtedness in better times.” Either policy could help ensure some funding stability and “lead to more rational budgeting.”

Longanecker does not agree that schools are overpriced for many students; “Many of our institutions charge far less in tuition today than most students can afford… [they] will go to college…there is virtually no price-elasticity of demand for these students.” But he advised that students from low-income families, whose college participation rates decline as tuition increases, need to be protected “by offsetting any increase in price with increased financial aid” requiring coordination between financial aid policy and tuition policy.

Short-term Strategies

Changes in the way higher education is funded are seen, not unexpectedly, in states with the greatest budget problems. *The Chronicle of Higher Education* tracks and reports on these changes, usually in its Government and Politics section. Several approaches have been identified.

Virtually every state in financial difficulty has allowed tuition and fees to rise at state schools to offset reductions in state appropriations. In FY2003, 25 state college or university systems increased tuition by 10 to 20 percent and some, in California, Arizona and New York, raised tuition 25 to 40 percent (Arnone, 2003). The net effect of these increases coupled with cuts in appropriations is lost revenue to the schools because they are generally unable (or not allowed) to raise tuition sufficiently to cover declining appropriations. Raising tuition has shifted the economic burden from the state to the student and some state schools are now closer to being “state assisted” rather than “state supported” (Fleming, 2004).

Schools are becoming more creative with tuition increases. A big initial tuition increase coupled with a four-year price stability guarantee is the method of choice in Illinois. Iowa, Kentucky, New York and Indiana are considering similar proposals (Klein, 2004; Arnone 2004). States are also removing tuition caps such as the ones in place in Ohio and Texas as other higher education funding dries up. One proposal in Ohio would raise tuition for in-state students at selective Miami University to the out-of-state rate and then provide a “resident scholarship” to rebate back part of the tuition increase (Breneman, 2003). However, drastically raising tuition can backfire on a university. Tightening the residency requirement at Utah State University, located close to the Idaho border, caused a freshman enrollment decrease of 300 students and resulted in a revenue decrease for the college (Hebel, 2002).

These increases in tuition are often accompanied by a hiring freeze. When a hiring freeze (or even faculty reductions) occurs during a period of record enrollment for higher education, increased student/faculty ratios occur. This may be a measure of increased productivity but, it is also argued, a measure of decreased quality (Selingo, 2002).

As revenues fall, competition for funding merit aid and need-based aid can also increase. Some states such as Texas, Minnesota and Pennsylvania are tightening up the eligibility requirements for need-based aid (ISAC, 2004) Illinois is also considering eliminating a small merit aid program to increase funding for its large need-based grant program. States with large merit-based programs, often funded by lotteries, such as Georgia, have also tightened up requirements and are still facing huge deficits (Selingo, 2002). Other “quick fixes” that are being implemented to improve affordability and hold college costs down are establishing increased state authority over colleges and tuition policies either by appointing strong boards as is being done in South Carolina and Alabama, putting limits on tuition increases (Florida, Michigan and Maryland), or by giving the state direct authority to set tuition rates (Louisiana, Kentucky).

Partnerships, Lotteries, and Vouchers

As described previously, maintaining public-private partnerships has become important in Wisconsin where universities are required to match certain public funds with private donations. In Tennessee, the partnership is between university grant seekers and state dollars. Some state dollars are earmarked solely for the purpose of acquiring research funds. Tennessee has been successful – generating four research dollars for every dollar of state funds, but in tough economic times even programs like these are in peril. Tennessee legislators also are making tough choices between access and quality. Feeling they can no longer provide both, they are limiting access and trying to better serve the students they now have. Other cost-saving measures include using more adjunct professors and cutting support for sports programs (Selingo, 2002).

Lotteries are being viewed with renewed interest. The large Georgia Hope program is funded by a lottery and, despite the projection of a $400 million deficit within five years, other states have copied part of the program. Florida’s “Bright Futures” program is also headed into the red with an $800 million deficit projected over the next 10 years (Schmidt, 2004). However Oklahoma, which had to make difficult cuts to higher education appropriations to maintain a merit/need state scholarship is considering a lottery to increase its revenues as are South Carolina and Tennessee (Arnone, 2003). Other new sources of revenue are being considered in Ohio (video slot machines at racetracks), Minnesota (casinos), and Kansas (technical colleges want the right to levy property taxes) (Schmidt, 2004).

Private schools are also looking for additional funds, often in the corporate world. In addition to the relationships already discussed, the biggest corporate donation recently occurred at the University of Arkansas, where the Walton family donated $300 million. The money comes with strings, with the Walton family being assured of being able to “monitor the success” of its donation (Stout, 2004).

Two ideas already discussed could potentially change the basic structure of public higher education. South Carolina has proposed “privatizing” some of its selective public colleges and letting them charge market rates. A proposal just adopted by Colorado puts in place a college voucher program that gives each student who applies a $2,400 state subsidy called the College Opportunity Fund while raising tuition at the colleges by a similar amount (Curtin, 2005).

Analytical Models and Data Resources

Evaluating States, Institutions, and Students

In "Information Sources for Answering Key Financing and Financial Aid Policy Questions: Current Practice and Future Possibilities" Paul Lingenfelter et.al. (2003) listed several key questions for consideration and suggested sources for the data needed to answer them. To answer the question: What is the capacity of the state to generate resources for higher education; they suggested an evaluation of state taxing capacity. States that depend on sales tax, that tax capital gains, use lotteries, have large numbers of the very young and the elderly or that have tax limitation laws that reduce state taxing authorities may have problems generating sufficient resources for higher education.

A second question - Is the capacity of higher education institutions in the state sufficient? - can be answered by an inventory of institutional resources by sector and matching them with students served; determining whether the state has a net inflow or outflow of students; performing an evaluation of institutional resources and determining whether these resources are restricted use; evaluating the utilization of core resources; reviewing institutional missions for cost-effectiveness and need; evaluating trends in dollars per FTE and faculty per FTE; and comparing estimates of future demand and future capacity. Lingenfelter advises that state policy makers seek answers to these questions and provides a valuable set of data sources in order for states to make comparisons and find needed data to perform self assessments.

Another policy question centers around the consumers of higher education - what is their capacity to pay for higher education? Data to be considered for this question include income profiles, college price trends, student price elasticity, net cost, state and federal assistance, proportions of need versus merit aid, students' annual and cumulative borrowing, student employment behavior and tuition tax credit usage.

A final policy question focused on results and the payoff to the state. Data that can be evaluated include total current postsecondary participation rates and participation by race; enrollment of both traditional and non-traditional students; and enrollment by program type. The authors also suggest studying the interactions of preparation, financial need and culture on influencing participation and success in higher education. The article suggests looking at where in the state's K-12 system are there important needs to improve preparation and opportunities to learn from successful practice. Lingenfelter concludes by advising an examination of the relationship of income race and attitude toward debt.

Measuring Support for Higher Education

The higher education funding process generates many data sets and statistics that can be used to track funding trends over time, and the changes that do take place can be identified and evaluated. But understanding exactly what each data set represents and making meaningful generalizations about a set of cold statistics can be challenging. In *Grapevine*, *An Annual Compilation of Data on State Tax Appropriations for Higher Education,* edited by James Palmer (2004); three variables measuring support for higher education are created from *Grapevine* survey data. The first is "capacity," defined as the percent change in general revenue funds; the second is "willingness" defined as the percent change in total state expenditures and the third is "effort" defined as the percent change in appropriations to higher education.

Palmer uses these three variables to characterize states by their financial viability (if their revenues have increased or not), by their willingness to spend money (willingness variable) and by their willingness to spend money on higher education (the effort variable). This allows some tentative conclusions to be drawn about why dollars are or are not flowing to higher education. A situation where total revenues have increased but total spending or spending on higher education has not is different from a situation where revenues have not increased and therefore higher education spending has not.

For example, between FY2003 and FY2004, in Illinois, capacity increased by 8.9 percent but willingness to spend overall only increased by 3.7 percent and those dollars weren't spent on higher education where effort flagged at –2.2 percent. During the same period, Arkansas saw a capacity increase of 8.5 percent, a willingness to spend increase of 8.5 percent, and an effort of 6.8 percent. Unfortunately, many states mimicked the pattern of Illinois, where states saw increases in capacity but showed declining effort in the funding of higher education.

In a review of *Grapevine* data for FY2005, Palmer indicated that, unlike FY2004, where overall appropriations to higher education fell for the first time in a decade by 2.1 percent, in FY2005, higher education appropriations rose by 3.8 percent to about $63 billion. However, there were wide state variations and no regional patterns could be discerned. Some states, such as Florida and Virginia, raised sales or other taxes, and used at least part of the funds to increase higher education appropriations at rates greater than inflation. Eight states cut higher education funding (West Virginia, Illinois, Minnesota, Wisconsin, Michigan, Oregon, Texas and Mississippi.) Seven states increased higher education funding but not by enough to compensate for previous cuts. Among college sectors, community colleges fared the best, helped in part by a big increase in community college budgets in California brought about, unfortunately, by decreased funding to its public four-year institutions.

Student financial aid data also were tracked to the extent possible. Not all states reported separate figures for student aid, but of the 34 that did, the average amount reported represented an increase of about 3 percent, totaling $4.4 billion.

Assessing Integration of State Policies

In *Informing the Integration of Tuition, Student Financial Aid, and State Appropriations Policies*, Paul T. Brinkman (2003) identified the importance of data collection in support of integrated state higher education policies. He identified four different kinds of data that could be collected to bolster the case for coordinated spending on higher education: (1) contextual and background data; (2) referential data, (3) indicator data; and (4) combined data for illustrative purposes.

Contextual and background data includes primarily national and state socioeconomic data such as the Consumer Price Index (CPI) and related indices; per capita disposable personal income (DPI) nationally and by state; state unemployment rates and tax revenues; and state and national demographic variables. He also includes data from research findings such as returns to a college education and the student price elasticity of demand for higher education.

Referential data include higher education variables compared on a national or regional basis such as access variables (percentage by age group enrolled in college) and low-income college participation rates; affordability indicators such as share of income necessary to pay for college or total student loan debt levels; private and public institution sticker prices; and state student aid expenditures.

The third data category, indicator data, consists mostly of time-series data such as variables described above as they change over time, plus other financial variables such as appropriations variables and state bond ratings. The fourth category combines the different data for illustrative purposes. Brinkman suggested that data collection and development needs to done with a purpose in mind and a focus around an organizing principle such as evaluating the changing economic burden of students over time or measuring the progress toward some defined end point such as movement toward a higher education access goal.

Identifying National Trends and Making Interstate Comparisons

The State Higher Education Finance (SHEF, 2004) report produced by the State Higher Education Executive Officers (SHEEO) is described as “a tool to help policy makers and educators address broad public policy questions.” It provides data to help answer questions about state college funding levels necessary to achieve certain higher education goals such as setting appropriate tuition levels, determining the correct levels of student financial assistance needed, and evaluating whether productivity improvements at institutions are possible without sacrificing quality. The report includes a discussion on the limitations and appropriate use of higher education financial data and reviews all state revenue sources supporting higher education (state and local taxes, lotteries, royalties and state-funded endowments.) It highlights national trends and provides interstate comparisons of state funding for higher education and net tuition revenues per FTE and evaluates state wealth and tax revenues per capita and the states’ overall allocation of revenues to higher education.

> [T]he data defy sweeping generalizations but a general pattern does emerge - Americans are increasingly interested in enrolling in higher education. The states have recognized and responded to this demand in varying ways and amounts. When state resources fail to keep pace with enrollment demand and inflation, tuition has grown and students have had to shoulder a greater portion of the financial burden.

The report describes the following trends:

- From 1970 to 2003 state funding kept pace with enrollment growth and the CPI. Constant dollar state support per student nearly kept pace with HECA index (CPI for higher education).
- Economic downturns depressed state funding per FTE. This has happened several times since 1979. A rebound occurs when enrollment growth moderates and funding increases.
- From 1991 to 2003, enrollment in public institutions increased by nearly 19 percent, with half coming since FY2001, the beginning of the current downturn. The percent increase in FTE since 1991 has already outstripped that of the previous two decades.
- Education appropriations per FTE in public institutions dipped during the early 1990s recession and recovered by 2000. However, recent decreases have resulted in a net decrease of 7.3 percent from $6,283 in 1991 to $5,823 in 2003. Budget shortfalls and increased enrollment both contributed to these results.
- Net tuition accounted for 26.2 percent of total higher education funding in 1991; in 2003 it was 33 percent.
- Total higher education funding per FTE in public institutions remained constant from 1991 to 2003; however it was tuition that increased (28.6%) while higher education appropriations decreased (7.3%).

The SHEF report documented substantial variations among states. Public institution enrollment growth ranged from 76.5 percent in Nevada to –3.5 percent in Rhode Island. Higher education appropriations per FTE grew 22.3 percent in Georgia and declined 42.6 percent in South Carolina. Net tuition revenues per FTE ranged from $9,154 in Vermont to $959 in California.

How states cut spending heading into recession and increase spending coming out of recession was described in the National Association of State Budget Officers (NASBO, 2004) annual *Fiscal Survey of the States*. In "fiscal 2002, 26 states reduced [the] budget gap by enacting across the board cuts and using rainy day funds, 15 states laid-off employees, five states used early retirement, 13 states reorganized programs, and 31 states used a variety of other methods…" Higher education appeared to be a declining priority in state appropriations; higher education spending as a percent of total state spending declined from 11.4 percent in fiscal 2002 to about 11 percent in fiscal 2003. The 2004 edition of the survey indicated that 2004 general fund spending was increased by about 3 percent and 2005 appropriations were estimated to increase by an additional 4.5 percent but will still be below the 27 year average. Only three states reported expecting negative growth budgets for FY2005.

Conclusion

When compared to other functional areas of higher education, studies concerning the process of funding higher education are relatively few; however, those studies that do exist make good use of the abundant data available. The reports that look at the overall funding of higher education arrive, by means of different processes, at a similar conclusion: that higher education funding is insufficient to meet the demand for higher education, as the delivery system of higher education is currently configured. This situation is unlikely to improve during the next decade because of state structural deficits – fundamental deficiencies in state revenues to meet state expenses - that may be temporarily masked but are not eliminated by upward swings in the business cycle. At the state level, funding for higher education is losing out two ways – it is falling as a percentage of state expenditures and, in some cases, is being cut from former levels. Since higher education costs are rising and must be paid, cost-burden shifting is occurring among states, the federal government, students and parents, and the institutions of higher education themselves.

Many of the articles reviewed in this survey detail these cost shifts, the beliefs and politics that support the changes, and the implications of the cost shifts on higher education in the future. Rising college enrollments, the perceived necessity of postsecondary education, the growing chasm between access to college for the well-off and for the poor, the importance of middle-income access, the commitment to merit aid and the increasing perception that education is more of a private good than a public one are all reasons cited that affect funding reallocation decisions apart from the shortage of state funds. Also discussed in this review are the impacts of these changes now being played out in some states where new reallocation ideas are being considered or implemented. The success or failure of these initiatives in higher education funding, which include formerly "unlikely to even be discussed" options such as public college vouchers and partially privatizing public flagship universities, will impact the higher education funding process for decades to come.

Application to the Recession Retrenchment and Recovery Project

The Center for the Study of Education Policy at Illinois State University (ISU), along with the National Association of State Student Grant and Aid Programs (NASSGAP) and the State Higher Education Executive Officers (SHEEO), has received grant support from the Lumina Foundation for Education to conduct a major study of higher education finance and student financial aid.

The study will examine the following key questions about states' student financial aid programs and strategies to maintain financial access:

- **<u>Recession</u>: What has been the affect of recessions on states' higher education funding and to what extent have states been able to recover after each recession?**
- **<u>Retrenchment</u>: What impact has the current recession had on states' higher education and student financial aid policies and priorities?**
- **<u>Recovery</u>: What strategies can state higher education systems pursue now to prepare for the next recession in order to maintain financial access for their students?**

The purpose of the *Recession, Retrenchment, and Recovery* project is to identify states that protected financial access to postsecondary education for their students throughout economic cycles. The project team will then identify and disseminate policy strategies used by these states to help other states bridge these difficult economic cycles. The project includes three phases: an analysis of historical state funding data for higher education and student financial aid, a survey of state higher education and student financial aid executives; and visits to selected states for in-person interviews of state higher education policymakers.

Undoubtedly this literature review is not totally encompassing but it provides a valuable resource for the project team in their work. It contains a summary of recent research and publications on the relationship of higher education funding, student financial aid funding and the impact of recessions. The literature helps to provide clarification of issues and concerns as they relate to recession, retrenchment and recovery in state higher education and student financial aid funding and the related effect on student financial access to higher education. The economic downturn commencing in 2001 has generated numerous data analyses and studies - as well as forecasts resulting in predictions about the outlook for higher education opportunity given the status of state funding demands, tax structures, and value given to postsecondary education. The research proposed in this project will make a valuable contribution to the literature with its findings, conclusions and recommendations.

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