Facts About Higher Education Financing

Paying for college is a partnership. The federal government, states, institutions, foundations, and individual students and their families all have a role in paying for college.

- **Government.** The federal government is key to ensuring equal educational opportunity and access, primarily through student aid programs. States also assure access by partially subsidizing public colleges to keep tuitions within reach of their citizens and by supplementing federal student aid with their own grant programs.
- **Institutions.** Institutions also play an important role in ensuring access through the investment of significant resources in financial assistance for students. Institutions seek to maximize quality and minimize tuition increases. None of the nonprofit public and private, two- and four-year institutions charge tuition equivalent to the full costs of a college education.
- **Nonprofits.** Private foundations and other nonprofit organizations provide funding to institutions to support academic and student aid programs. In addition, many nonprofit and civic organizations provide scholarships directly to students.
- **Students and families.** The final component of the funding partnership is "self help." Students and their families provide this component by using savings, earnings and/or loans to pay tuition and fees. The amount students and their families are expected to pay depends on their financial resources. Students from very low-income families are not usually expected to pay tuition. Instead, federal, state and institutional funds cover their tuition.

Tuition does not cover the full cost of the education provided. Institutions supply a great deal of 'indirect' aid to students by raising and supplying funds that allow students to pay far less than the actual cost of their education. Experts estimate that, after this indirect and direct student aid is taken into account, students pay, on average, about one-third of their actual educational costs.

At a number of institutions, endowments help restrain tuition increases and maintain access for many students. At many colleges and universities, endowment spending contributes significant resources toward operating budgets; in some cases, it is the largest source of revenue for the college or university. In this way, endowment spending serves to hold tuition below the level necessary if tuition alone paid the true cost of educating a student. In addition, endowment spending at many colleges and universities supports a substantial amount of institutional aid to students from low- and middle-income families. Private colleges in particular have substantially increased the amount of institutional aid they provide. The average grant at the schools with the largest endowments covers approximately 80 percent of the cost of tuition. Moreover, relying on endowment spending and other private resources, a number of colleges and universities are replacing loans with grants as part of their student financial aid packages.

Tuition is driven by many factors and colleges and universities must weigh them when setting tuition. Tuitions are a direct function of a combination of realities including: decreased state support for public institutions; increased federal, state, and regulatory requirements; increased health care and other employee benefits costs; increased energy costs; the demand and need for up-to-date information technology; and, student and family demands for increased services and amenities. In setting tuitions, public and private institutions must balance these costs with anticipated support from tuition dollars, endowment income, charitable support, and state and federal funding. Generally, at public institutions, state policymakers play a large role in such decisions as they are largely driven by funding received from the state. When states cut their appropriations for colleges and universities, public institutions are forced to raise tuition to make up at least part of the resulting budget shortfall. Furthermore, in many states, state governments themselves set the tuition levels. Private institutions set their own tuition, but they operate in a very competitive environment. They have to construct tuition and aid policies that allow them to fill their classes and offer the programs and facilities that will keep them competitive.

Colleges and universities face myriad factors that increase costs. Decreasing state appropriations, increased investment in institutional student assistance, rising labor costs, keeping pace with scientific knowledge, updating and maintaining technology, and complying with federal, state and local regulations all drive up college costs. There is a direct and inverse relationship between the level of state appropriations and the level of tuition increases. Each dollar cut from state allocations can require more than twice that amount in tuition increases, since tuition makes up only about a quarter of institutional income. Despite these issues colleges are searching for new and innovative ways to cut costs and minimize tuition increases. On campus after campus, major program reductions and hundreds of layoffs have occurred as public higher education has sought to educate growing student populations with flat or declining revenues. In addition, colleges and universities are increasingly outsourcing campus services, realigning their hiring practices to lower labor costs, and merging or closing campus offices and programs.

Cuts in state budgets for higher education hurt both public and private institutions. **Public institutions** depend on state governments for the bulk of their operating support. However, in the last 20 years, states have systematically reduced spending on higher education and increased tuition to offset the reduced revenue. While the exact percentage differs from state to state, in 1980, states provided 46 percent of the operating support for public colleges and universities. By 2005, that amount had fallen to 27 percent. During the same period, tuition as a source of revenue increased from 13 percent to 18 percent. The bottom line for public colleges and universities is that tuition increases are merely offsetting reductions in state revenues.

Private colleges and universities face a different set of circumstances. Few independent institutions receive significant amounts of state support for their operating budgets. However, many states provide financial aid that helps students attend these institutions. When state financial aid is reduced as a result of budget cuts, colleges must use even more of their own funds to fill the gap.

This information was compiled with the assistance of the American Council on Education (ACE), the Association of American Universities (AAU), the National Association of Independent Colleges and Universities (NAICU), the National Association of State Universities and Land-Grant Colleges (NASULGC), Council for Advancement and Support of Education (CASE), and others. For additional information, please contact Erin A. Hennessy, ACE Office of Public Affairs, at (202) 939-9367 or erin_hennessy@ace.nche.edu.