INVESTING IN THE FUTURE: SHARING RESPONSIBILITY FOR HIGHER EDUCATION ATTAINMENT

EXECUTIVE SUMMARY

Prepared by the
NATIONAL COMMISSION ON FINANCING 21ST CENTURY HIGHER EDUCATION
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LETTER FROM THE COMMISSIONERS

The University of Virginia Miller Center created the National Commission on Financing 21st Century Higher Education in 2014. The purpose was to recommend funding changes to the U.S. public higher education system so the nation can attain a goal of having 60 percent of its labor force with a postsecondary degree or certificate by 2025. This means that 16.4 million more Americans must graduate with a postsecondary degree or credential above current projections between 2017 and 2025. To meet the goal, the nation must maintain high school graduation and college entrance rates at or above 75 percent and 70 percent, respectively—reachable goals which are close to historical norms. It must also increase college graduation rates from 40 percent to 60 percent.

Increasing the college graduation rate will be inherently challenging particularly given the coming surge of low income students and students of color that historically have been less prepared to attend postsecondary schools. In outlining our recommendation, we emphasized strategies that help underrepresented students attend college and attain a degree or certification. If we fail to dramatically raise the college completion rates of these students, we will not achieve the 60 percent goal nationally.

Policymakers must recognize that urgent action is needed. Already, at least 10 other nations have surpassed the U.S in terms of the percent of population (aged 25-34) having a postsecondary degree or certificate. The cost to our nation in terms of economic growth, job creation, standard of living, and all other benefits that accompany higher levels of education for our citizens is too high to fail.

To learn more about the challenges and road map to attaining the goal, the commission engaged highly qualified experts to write 10 white papers on different dimensions of the current and future public higher education system. The commission asked all the authors to ignore the limits of current policies and engage in “blue sky” thinking on individual topics. Each paper represents the views of the individual authors, not the commission. Nevertheless, the papers have provided a foundation for the recommendations in this final report. In addition, the commission hopes the papers stimulate further discussion and debate about higher education funding.

The 10 papers and the final report focus on answering three primary questions related to reaching the 60 percent goal. First, how do we realign incentives and retarget existing public funding to make the entire system more affordable while increasing graduation rates for students generally but students of color and low-income individuals in particular? Second, what are the new, innovative models to deliver postsecondary education that can both lower the cost and increase the productivity of the entire system? Third, what options do federal and state governments and the private sector have for increasing funding for higher education?

This final report makes nine broad recommendations and a significant number of specific actions that states and federal policy makers can adopt to reach the goal. Essentially, it will take a stronger federal, state, business, higher education partnership to make the goal fully operational. While the U.S higher education system is still the envy of the world the nation is clearly at a major crossroads given the increased income inequality and the fact that many workers feel left behind economically. It is our hope that national and state policy leaders are able to gain valuable insights and policy direction from the combination of the 10 white papers and this final report. The time for transforming and adequately financing the public higher education system is now.
National Commission on Financing 21st Century Higher Education

- Mike Castle, former governor of Delaware and former U.S. congressman (co-chair)
- Bob Graham, former governor of Florida and former U.S. senator (co-chair)
- Andrea J. Ayers, president and chief executive officer (CEO), Convergys
- Jorge Benitez, (retired) CEO United States and senior managing director, Accenture North America
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- David W. Nelms, chairman and CEO, Discover Financial
- Edward B. Rust Jr., chairman (retired) and CEO, State Farm Insurance Company
- Lou Anna K. Simon, president, Michigan State University
The members of the commission wish to acknowledge the many people and organizations involved in completing this project.

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Executive Summary

The mission of the National Commission on Financing 21st Century Higher Education is to identify finance options that enhance innovation, productivity, and capacity within public postsecondary education so that 60 percent of Americans 25 to 64 years of age can achieve a high-quality postsecondary degree or certificate by 2025. The commission embraces this goal because we believe that it is necessary to safeguard the future economic prosperity and mobility of Americans.

The United States faces a shortage of skills and talent, and many in our nation are unable to fulfill the educational ambitions within their reach and capabilities. As a result, the United States has fallen behind other countries in building a highly educated workforce. Although 44 percent of the U.S. population aged 25 to 34 has a college degree now, 10 other countries have higher percentages for the same age group.

Signs of stagnating growth and economic problems were on the horizon before 2008 when the great recession began, and the economy has since struggled to regain its footing. Economic growth has averaged only 2.1 percent per year and productivity has averaged only about 1 percent each year. Both are substantially below their long run averages of the last century. Total unemployed, people who want to work but are discouraged from looking, and people who are working part time because they cannot find a full-time job peaked in 2010 but remains at 9.8 percent. Moreover, U.S. income inequality, on the rise for decades, is now the highest since 1928. A deficit of skills in a large part of our working-age population—either due to a lack of proper education and training or because an individual’s skills are outdated—will only make these problems grow.
A Call to Action

In 1945, the United States faced a similar crisis: After more than four years of war, millions of men and women returned to their homes to rejoin the economy and society, but their years of service had left major gaps in their education and training, threatening to hinder their economic potential. The federal government responded by passing the GI Bill to cover the costs for veterans who wanted to complete their education and enhance their skills. About 2.2 million returning service members used the benefits to attend college, and 5.6 million used them to attend vocational schools. This infusion of educational support enriched the United States by producing 450,000 engineers; 240,000 accountants; 238,000 teachers; 91,000 scientists; 67,000 physicians; 22,000 dentists; and many other highly capable individuals. Similar bills were enacted after the Korean and Vietnam Wars. The United States became the world leader in educational attainment, and several decades followed of unprecedented income growth, higher living standards, and rising productivity.

The commission believes that the country faces a similar call to action today. Many of our citizens are unable to realize their educational goals and possibilities, often for reasons beyond their control. Rising tuition costs and plummeting support for public colleges have priced some low-income students out of higher education and left low- and middle-income students with fewer choices. In addition, countless students have difficulty completing college, often leaving without a degree but still accruing significant student debt. This is particularly true for students of color and low-income students, who often graduate from low-performing kindergarten through grade 12 (K–12) systems and may not be adequately prepared for the rigors of postsecondary education. To change this trajectory, the federal government, states, the private sector, and individual colleges and universities must pursue radical change. The nation must help more students succeed in college, increase graduation rates, make college more affordable, and invest the necessary dollars to raise college access and attainment levels. Only then can we regain our footing and build a society that enjoys educational fulfillment and the benefits that flow from it.

Commission Recommendations

In developing our recommendations, the commission focused on four key challenges:

• The changing demographics of the college-going population: Today’s K–12 student population (potential college-goers) is vastly different from their counterparts of just 20 years ago. The percentage of white students has fallen from 65 percent in 1996 to just under 50 percent in 2015, the Hispanic student population has grown from 14 percent to almost 26 percent over the same period, while the black population has remained at about 16 percent. In addition, the percentage of school-aged children eligible for free or reduced-priced lunch grew from 38 percent in 2001 to 52 percent in 2014. These students often face barriers in accessing postsecondary education and attaining a degree for a variety of reasons, including inadequate preparation at the K–12 level because of low-performing schools, poor career guidance, difficulty paying for college, and lack of support systems while attending college. Yet these are the same demographic cohorts that must succeed in college if the nation is to achieve the 60 percent goal.

• The price and affordability of college: For many students, particularly those from median or lower income families, the price of college is prohibitive. The total cost of attending a public college or
university, including tuition and fees, room, and board, has risen steadily for decades. In 1985, the total annual cost of attending a four-year public university was $3,682, while a two-year college cost $2,807. By 2013, these costs had jumped to $17,474 for a four-year public university and $8,928 for a two-year public college. Today, 56 percent of all students must take out loans to attend college, and many leave college—with or without a degree—burdened with unsustainable debt. The high number of low-income and underrepresented students who must complete college to meet the 2025 goal cannot bear these costs or high levels of debt. Instead, they will need more grant support and lower cost education options.

- **Insufficient financial support to institutions and students:** State and federal support to public higher education is both insufficient and inefficient to help the nation meet the 2025 goal. For many decades, state and local appropriations to public institutions covered more than half of college costs, helping temper tuition increases. Recently, however, levels of state aid have fallen, pushing tuition higher. At the same time, student grant aid per person (primarily from the federal government) has fallen, increasing the tuition burden on individuals who can least afford it.

- **Persistently low college completion rates:** The nation’s ability to achieve the 2025 attainment goal depends on dramatically raising college completion rates, which have been low for years. For four-year institutions, only 33.5 percent of entering freshmen graduate within four years, and only 57.2 percent graduate within six years. For two-year public institutions, only 19.5 percent of students graduate within three years. These completion rates vary considerably by race and ethnicity. To raise completion rates, colleges will need to invest in strategic interventions to help individual students, and that will cost money.

To achieve a working-age population that has a college attainment rate of 60 percent by 2025, we must graduate an additional 16.4 million people with two- or four-year degrees or industry certificates between 2017 and 2025. This means that public institutions will need to award 1.22 million more degrees each year, while private institutions will need to award an additional 601,333 credentials annually. Based on current spending figures and degrees conferred each year, the commission estimates that public colleges and universities will require approximately $30.1 billion more annually over current projections between now and 2025 (in 2014 dollars). Likewise, student aid will need to increase by approximately $14.4 billion (47 percent) annually to cover the additional graduates attending either public or private colleges.

To reach the 2025 goal, the commission presents the following recommendations.

**Recommendation 1. Increase federal and state institutional support**

The federal government will need to play a prominent role to help meet the 60 percent goal. Since 2008, state budgets have had difficulty returning to prerecession levels, and the growing costs of Medicaid have added to that strain. States should maintain their commitments to public colleges in real terms at least, but the commission believes that the federal government must establish a sustained level of institutional support. Therefore, the commission recommends that the federal government provide an annual block grant to states totaling $15 billion, which each state would then match to maintain its current higher education funding level in real terms plus additional dollars to achieve a national total of $5 billion per year in additional state funds. Such funds would be used to support the annual costs of public institutions and help keep tuition costs in check. Because the
projections on resource needs are based on extrapolating current expenditure data, the commission also recommends that the federal government conduct an analysis to establish more precise estimates and adjust the recommendations of this report accordingly.

**Recommendation 2. Enhance state revenue to support higher education**

To guarantee that ample revenues are available to fund higher education, states should update their revenue systems to reflect the 21st-century economy. Current revenue systems were built for a 1950s manufacturing-based economy, not for the high technology, service-oriented economy of the 21st century. Sales and use taxes, which generally apply to goods and not services, are not keeping up with state economic growth. Moreover, many purchasers, such as governments, nonprofit charities, and religious and educational institutions, are exempt from paying taxes. Finally, income taxes in many states are not sufficiently progressive—indeed, most are often regressive in nature—thus failing to capture more revenue from high-income earners.

To ensure continued support for higher education, states should consider the following actions:

- Expand state sales and use taxes to key services to expand the tax base, and reduce some of the exemptions so that revenues grow more in line with total economic activity.
- Ensure that Congress enacts the federal Marketplace Fairness Act, which would allow states to require out-of-state sellers over the Internet to collect the sales and use taxes.
- Increase the progressiveness of state individual income taxes.
- Establish state education rainy-day funds to support investments in times of economic stress and high unemployment.
- In positive budget years, focus on nonrecurring public college investments that will reduce future government costs, such as clearing deferred maintenance backlogs, building technology infrastructure, or investing in energy-efficient systems in buildings.

**Recommendation 3. Stimulate the development and implementation of low-cost education delivery models**

States should take the lead, using additional funds above current commitments, to spur development, implementation, and scale-up of lower cost education delivery models. These funds should be used to offset some of the start-up and scale-up costs associated with the lower cost approaches that schools employ.

- To encourage development of lower cost models, states should consider the following policies:
  - Provide competitive grants to universities and colleges to offset a portion of the start-up costs for developing and piloting lower cost delivery models. Such grants can also encourage partnerships among schools with the private sector in such demonstrations.
  - Provide bonuses in the form of temporary higher institutional aid for schools that bring low-cost delivery systems to scale.
**Recommendation 4. Encourage productivity in the postsecondary system**

“Higher education productivity” refers to the number of degrees conferred per dollar of spending. The commission believes that most public institutions can improve their productivity and graduate more students while lowering or holding steady the overall cost per degree. We think that a reasonable goal for most colleges and universities is to increase productivity by at least 1.5 percent per year over the next decade to yield an average annual savings of $5 billion from all public institutions between 2017 and 2025.

States can adopt several policy options to encourage increased productivity:

- States should employ outcomes-based funding (OBF) formulas when distributing institutional aid so that colleges and universities that increase productivity receive more resources. As Chapter 3 describes, states can use OBF formulas to allocate annual appropriations to higher education institutions or assign bonus payments (above annual appropriations) based on performance. These funding models must include weighted variables that ensure sufficient aid to promote continued access and increased success for low-income students, students of color, and even adult and academically underprepared students. Weightings should also reward institutions that control costs. States must continue to update and revise the productivity incentive system over time as data and experience accrue. In the early years of implementation, states should be prepared to increase appropriations to schools that serve student populations that typically underperform in college. These students will need additional support systems and interventions to complete their education.

- State higher education agencies should negotiate tailored productivity agreements with individual colleges and universities. Some schools may be able to commit to goals equal to or higher than those the commission recommends, while others may need a few years to ramp up services before meeting the 1.5 percent annual goal.

- States can provide competitive grants to institutions or groups of institutions to help them build data systems that track student readiness and performance. Data from these systems can help institutions develop and employ tailored intervention strategies.

**Recommendation 5. Create incentives for students to graduate on time**

Students must be encouraged to graduate on time and institutions must be encouraged to help them. Options include:

- Reforming Pell Grant program rules to enable low-income students to take 15 credit-hours per term instead of the current (and inadequate) full-time definition of 12 credit-hours, with state aid rules reflecting these changes;

- Reforming financial aid policies (federal and state) to enable students to take courses in the summer (in addition to fall and spring terms) as incentives for completing programs on time or early;

- Linking renewal of financial aid eligibility (federal and state) to milestones on the path to degree completion (for example, 25 percent, 50 percent, and 75 percent program completion); and

- Reducing federal loan repayments for early or on-time completion.
**Recommendation 6. Help students and their families make better decisions**

Better information must be available to all students and parents when choosing degree programs and schools. Information should include the cost of attaining a credential or degree from various institutions available in the region and the potential wage value of different credentials. (A major reason some students default on college debt is because they choose careers that do not adequately compensate them for the cost of attending college.) In addition, reliable information must be available about alternative financing options from local scholarships, state and federal grants, and loans. Well-trained counselors must be available to meet with students and their families so that they thoroughly understand all the options available and potential financial outcomes.

States can take several actions to better inform students and their families:

- Provide information to likely eligible ninth-graders (based on family income) about the financial resources and options available to them to attend college. Provide an early guarantee to them of the financial aid available if they meet certain conditions on graduation.
- Provide information to all ninth graders on the opportunities, costs, and benefits of programs, classes, and/or tests that can be used to earn college credits while in high school. These include the International Baccalaureate Program, Advanced Placement (AP) classes and tests, and dual-enrollment programs that allow high school students to receive both high school and college credit for taking a college-level course.
- Ensure that financial and curriculum counselors are accessible to high school students and adults interested in attending college.
- Develop and disseminate information that can answer common questions that students and families have before selecting a state college or university, including graduation rates for different cohorts of students, what students can expect to learn and earn after they have completed a given program, and what the total price and time commitment will be to complete a degree.

**Recommendation 7. Increase and reform financial aid to target low-income students**

We must enable more low-income students than ever before to attend and complete college. To succeed, these students must be able to pursue their education—for at least the first two years—at little or no cost, which means that more federal and state aid must be allotted to low-income students in the form of grants, while loans must be minimized or made unnecessary.

States and the federal government will need to take several policy actions to achieve this goal:

- All states should develop financial aid formulas that allocate federal, state, and institutional aid to students on a sliding scale. The formulas should award the highest dollar grants to low-income students and provide a mix of grants and loans to other students based on a sliding scale of income. Students at or below 200 percent of the federal poverty level (FPL)—approximately $24,000 per year for an individual—should receive sufficient financial aid to cover 90 percent of all college costs for at least the first two years.
- States should ensure that all state financial aid considers student income and is not based on merit alone.
- The federal government should expand Pell Grant program funding by $15 billion per year and cap grant awards to students at 400 percent of the FPL.

- Simplify federal needs analysis, and align state needs analysis to require only the income and asset information that students and families already provide through annual income taxes. Automatically qualify students who receive other federal means-tested benefits.

- Streamline the federal grant and loan programs. The 14 federal loan programs can be simplified into one income-contingent loan repayment, with the same borrowing caps for all undergraduate students.

- Consolidate federal tax expenditures that subsidize higher education into a single refundable, income-capped lifetime learning tax benefit.

- Provide consolidated information on all forms of financial aid given to students in a simplified award letter that includes information about all grants and loans and that shows the total monthly loan payments for all borrowing.

**Recommendation 8. Develop additional private funding**

Although it is doubtful that private financing of higher education will ever become a large source of funds, significant changes are taking place in that market now that could allow individuals and the private sector to make a significantly larger contribution in the future. States should encourage and experiment with many of the new possibilities while maintaining consumer protections:

- *Experiment with new approaches to increase college savings:* Participation in college savings plans is low and skewed toward upper income families. Many state 529 plans already feature one-time raffles in which families that meet certain criteria can win several deposits to their 529 plan. Prize-linked savings—where participants who save a certain amount of their income are eligible to win a prize every month—have been shown to positively affect saving behavior among lower income individuals. States may need to reform banking regulations to allow for more prize-linked college savings. Fifteen states have already done this to date.

- *Create space for new private lending models:* A handful of private firms are experimenting with underwriting models that look beyond traditional measures of creditworthiness to lend based on student behavior, projected earnings, and institutional and program quality. By providing more information about potential college costs and earning related to specific degree programs, states could help encourage expansion of these models to other populations and inject greater market discipline into the system.

- *Empower institutions to be entrepreneurial:* A handful of states, such as Iowa, Kansas, and Michigan, have empowered two-year colleges to sell bonds to finance customized job training for employers and employees. The models differ across states but generally works as follows: Employers and a community college enter into a training agreement that specifies the training program and the planned number of new hires. The college then sells bonds to fund the training, and the bonds are repaid by new employees through a payroll deduction. These public–private models can expand access to job training that is clearly aligned to local employer needs.

- *Experiment with social impact bonds (SIBs):* “Social impact bonds” are essentially pay-for-performance contracts in which public-sector entities commit to fund demonstrable improvements
in social outcomes. The public entity mitigates its financial exposure and exacts savings by structuring arrangements that allow third-party backers to frontload the necessary resources and contract with partners that administer the programs. Investors are paid by revenue from the state to the bond administrators if they meet the performance goals of the program. Like bonds, SIBs have a fixed term; unlike bonds, they do not have a fixed rate of return because the ultimate return depends on performance. As financing vehicles go, the SIB is a new idea, with the first known use in 2010 in the United Kingdom.

- **Experiment with shared income agreements**: Shared income agreements involve tuition loans from vendors that receive a fraction of the student's earnings over a period after graduation. This agreement effectively aligns the interest of the funder and the student to identify effective, low-cost programs that deliver value. Purdue University has launched a pilot program for this concept.

**Recommendation 9. Take advantage of private-sector programs**

The private sector currently spends about $28 billion on tuition reimbursements and another $58 billion on training and development programs that are contracted out to postsecondary education providers or private firms. This spending represents an opportunity for states to take advantage of these programs and retarget them to increase the number of degrees, certificates, and credentials, especially for low-income individuals. States can take advantage of private-sector programs in several ways:

- **Enhance business tuition-reimbursement programs**: More than half of U.S. firms that employ 20 or more workers offer their employees reimbursement for courses taken at colleges and universities. To help expand these programs and target them at low-income employees, states could provide small matching grants to low-income individuals who take courses that lead to credentials and provide tax credits to firms that expand reimbursement programs.

- **Retarget corporate training and development programs**: Employers spend approximately $58 billion in corporate training and development contracted to other businesses, educational institutions, or private individuals. About 59 percent of this money is spent on individuals who already have a bachelor's degree, 25 percent on those with some college, and 17 percent on workers with a high school diploma or less. Unfortunately, much of the spending on employees without degrees does not result in a formal certificate or credential or even credit toward one. Here, too, states could provide small grants to businesses to enhance their training programs so that they result in a formal degree or certificate.

- **Expand state employer-based work and learn programs**: States should examine their existing employer work and learn programs like apprenticeships to determine whether they could be expanded by offering tuition reimbursements to participants and/or tax credits to employers.

- **The federal government should update section 127 of the tax code, which allows businesses to exclude from gross income up to $5,250 of educational assistance furnished to an individual during a calendar year**: The amount in section 127 has not increased since 1986, but the federal government could increase it to $11,244 to offset inflation, and then index it to the Consumer Price Index. Alternatively, the federal government could convert the amount to a tax credit for low-income individuals.
Businesses should be encouraged to help employees repay college loans. A number of employers have begun helping employees pay off their student loans, often in occupations that are difficult to fill. The federal government could encourage such action by adding student loan repayment by firms to section 127 of the tax code, which allows such benefits to be paid with pretax dollars. In addition, state governments could use the communications channels they have, including the governor’s bully pulpit, to encourage more businesses to offer such benefits. States also could match part of the employer’s loan repayment share (for the first year only, for example) to help fill certain hard to fill critical occupations.

Conclusion

As discussed, to reach the 60 percent goal it will be necessary to increase the number of individuals with a postsecondary degree or certificate by an additional 16.4 million over and above the base line between now and 2025. The commission estimates that public colleges and universities will need approximately $30.1 billion more over current projections yearly between now and 2025 (2014 dollars) to reach the goal. The commission believes the federal government, states, public colleges and universities, and the private sector should work together to pay for these additional costs.

The commission recommends that the federal government provide $15 billion in matching grants to states, while requiring states to contribute an additional $5 billion. The commission also recommends that colleges and universities improve their efficiency and productivity so that they can save approximately $5 billion each year, thus lowering the total amount needed. Finally, through supportive policies, it is hoped that the private sector can be encouraged to provide the remaining $5 billion in annual investment needed.

Achieving the 2025 goal will require urgent action and a stronger higher education partnership among federal and state governments, the private sector, and postsecondary institutions. The nation will need to commit new resources to this goal, and institutions must commit to achieving greater productivity. The commission believes that these are reasonable prices to pay to retain—and, in some cases, regain—our standing in the world as measured by educational attainment and economic growth.