FINANCIAL AID and ENROLLMENT

Questions for Boards to Consider

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AGB ASSOCIATION OF GOVERNING BOARDS OF UNIVERSITIES AND COLLEGES

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Since 1921, the Association of Governing Boards of Universities and Colleges (AGB) has had one mission: to strengthen and protect this country's unique form of institutional governance through its research, services, and advocacy. Serving more than 1,300 member boards, 1,900 institutions, and 36,000 individuals, AGB is the only national organization providing university and college presidents, board chairs, trustees, and board professionals of both public and private institutions and institutionally related foundations with resources that enhance their effectiveness.

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About The Looking Under the Hood: Institutional Aid Benchmarking Tool

The *Looking Under the Hood: Institutional Aid Benchmarking Tool* was developed in collaboration with the Association of Governing Boards of Universities and Colleges (AGB) and the National Association of College and University Business Officers (NACUBO) and is supported by the Robert W. Woodruff Foundation. This new tool is for governing boards, chief executives, and chief business officers looking to review their institutional aid policies. It enables them to view and benchmark their institutional aid policies against a customized set of peers. The initial set of metrics included in the tool is based on financial data collected by IPEDS and the College Board's Annual Survey of Colleges.

This paper was written as part of this project to spur further conversations among board members about institutional student aid. Many of the questions posed for board members throughout this report can be addressed by using the *Looking Under the Hood: Institutional Aid Benchmarking Tool*. For more information about this project and the tool, please visit: http://agb.org/determining-institutional-student-aid-policy.

Financial Aid and Enrollment: Questions for Boards to Consider

As we emerge from the extreme financial pressures of the Great Recession, it is time for board members to take a step back and think about long-term strategies for ensuring that financial aid policies are consistent with institutional mission at the same time that they serve fiscal and enrollment goals.

All boards are aware that enrollment numbers are critical to the institution's long-term stability. It is common to ask whether small increases or decreases in the number of students might improve future prospects. Perhaps a lower enrollment goal would increase academic quality and selectivity and put less pressure on the financial aid budget. Perhaps a higher enrollment goal would bring in needed additional revenues. But there is no doubt that the number of students—and particularly the number of tuition-paying students—is a vital variable to monitor.

Financial aid policies may be more obscure to many board members. By now it should be understood that because of the discounts offered to students, net tuition revenues are lower than gross tuition revenues—and it is only the net revenues that can fund the activities of the institution. But the nuances of financial aid policy and its relationship to mission and enrollment goals are less transparent. The discussion that follows highlights some key concepts, trade-offs, and questions with which college and university administrators are grappling. While board members can determine these policies only at the broadest level, it is important that they understand the issues, provide constructive guidance, and clarify institutional priorities.

About two-thirds of full-time undergraduates attending private, nonprofit, four-year institutions and over one-quarter of those enrolled in public four-year institutions receive institutional grant aid.[1] Whether viewed as an expenditure category or as a discount from tuition, the impact on institutional budgets is significant and growing.

What is the relationship between tuition and financial aid?

When institutions raise their tuition prices, they are likely to spend more on need-based financial aid because of the larger gap created between ability to pay and sticker price. They may also spend more on non-need-based aid, designed to encourage students with particular characteristics to enroll.

Institutional grant aid creates a gap between the sticker price and the net price students actually pay to institutions, as well as a gap between gross tuition revenue (tuition times number of students) and the net tuition revenue the institution actually receives. Increases in institutional grant aid may reduce net revenues by simply lowering the prices students pay, or it may increase net revenues by bringing in more students.

Of critical importance, increases in financial aid accompanying tuition increases are sometimes so large that the institution does not generate any new net tuition revenue. It is net tuition revenue—not the amount of financial aid or the percentage of gross tuition dedicated to financial aid—that determines financial strength.

Questions Board Members Should Ask

How do trends in tuition prices and net tuition revenues compare over time at your institution?

How has the percentage of students receiving institutional grant aid and the average aid they receive changed in recent years?

Is there evidence that financial aid is bringing in desirable students who would not otherwise enroll?

Why do institutions charge different students different prices?

The awarding of institutional grant aid leads to different students paying different prices. Some students pay less because their financial circumstances make it difficult for them to pay. Others pay less—although they could pay the full price—because the institution is providing a discount in an effort to influence their decision about where to enroll.

This is a pricing pattern that economists call "price discrimination." Movie theaters price discriminate when they charge lower prices for children or senior citizens. Airlines do this when they charge different prices depending on when and where you buy your ticket and how long you plan to stay. Car dealers price discriminate when they bargain differently depending on their sense of how much you are willing to pay.

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[1] NCES (National Center for Education Statistics), National Postsecondary Student Aid Study, Power Stats calculations. http://nces.ed.gov/datalab/

Price discrimination is not a bad thing. Some students can easily afford the sticker price, and would be able and willing to pay even more. In most cases, they are paying less than the cost of their education because even the full sticker prices incorporates subsidies from the endowment, annual giving, state appropriations, or other sources. They are not being cheated, and lower prices would not necessarily change their opportunities or their choices. Other students are not able or willing to pay the current sticker price. Charging them a lower price makes it possible and desirable for them to enroll.

Financial aid is an expenditure made to shape the student body.

Some institutions have long waiting lists of students willing to pay their sticker prices. Most of these are highly selective, nationally known, private institutions or flagship public universities. These institutions discount their prices to attract different students than those who would enroll without financial aid. They want the best students they can get, and many of those students simply cannot pay on their own. They may also want students with particular capabilities who will be drawn in by financial aid. For those institutions, financial aid is an expenditure made to shape the student body.

Many other institutions would have empty seats if they did not discount so generously. If they lowered the sticker price enough to fill the class, their total revenues would be too low to operate. But if they can draw in some full-pay students, while charging others a lower price—something close to the maximum each student is willing and able to pay—they can fill their classes while taking in adequate net revenues. The full-pay students are no worse off because of the presence of other students who are there only because of the lower net prices they were offered. In fact, those students who are paying lower net prices probably increase the quality of the education that all students at the institution receive.

Questions Board Members Should Ask

How are the prices different students are asked to pay determined at your institution?

How do net tuition prices differ across students with different characteristics?

Is the institution transparent about how it determines the aid students in different circumstances and with different characteristics will receive?

Would it be better to simplify the pricing structure by lowering the sticker price and reducing the number and value of the discounts offered?

Many board members (and many other interested parties) are frustrated by the complexity of the pricing structure at colleges and universities and would like to know if there is a better model available. Some of the alternatives to consider might be:

- Lower the sticker price for all students and reduce financial aid;
- Raise the sticker price and increase financial aid;
- Promise students that the sticker price will stay the same for four years;
- Promise students that the sticker price will rise by the increase in the Consumer Price Index (CPI) or by CPI + 1 percent or + 2 percent every year;
- Promise need-based aid recipients the net price they pay will stay the same for four years (or increase by the CPI).

Some colleges and universities have implemented one or more of these strategies, but there are no magic bullets. Each institution must carefully examine its circumstances to find the optimal path. Institutions that discount for almost all students are more likely than others to seriously consider lowering the sticker price. Institutions facing uncertain non-tuition funding streams face greater risk if they make promises about future tuition levels.

Questions Board Members Should Ask

How do tuition and fees at your institution compare to the national average for your sector? For your type of institution within the sector?

Have you looked at alternative pricing models to be sure yours is most appropriate for your circumstances?

Would lowering your sticker price end up subsidizing affluent students more and placing added strains on your need-based aid budget?

Can increasing efficiency and lowering costs solve the tuition problem?

Offering a quality college experience requires considerable resources. Every institution could find efficiencies that lower its costs, and it is vital that we find ways to make higher education more affordable, but the solutions are not likely to be simple. Despite impressions to the contrary, institutional expenditures have not, in most cases, been rising rapidly. The explanation for the rate of increase in tuition lies more with declines in non-tuition revenue sources (particularly at public colleges and universities) and a growing gap between sticker prices and the net prices students actually pay after discounts from institutional grant aid (particularly at private institutions).

There is reason to be optimistic that technology will facilitate declines in instructional costs, but to date, most high-quality online learning has not been cost saving. All institutions should be exploring this area, in addition to examining administrative structures, purchasing patterns, and potential collaboration with other institutions for potential efficiencies.

Some of the expenditure patterns to which colleges and universities have grown accustomed, such as the practice of adding new programs while rarely eliminating old ones, should change. Board members must ask hard questions about innovation and efficiency, but should remember that too much focus on cost cutting can erode the quality of education offered.

QUESTIONS BOARD MEMBERS SHOULD ASK

Has the administration carefully reviewed the budget with openness to making changes that would increase efficiency while maintaining quality?

How has the size and cost of the administrative structure changed over the past decade?

What is the attitude on campus toward using technology to lower instructional costs and toward cooperation with other institutions that might reduce duplicative efforts?

How does financial aid affect students' enrollment decisions?

Price affects the enrollment decisions of some students more than others. Not surprisingly, there is considerable evidence indicating that lower-income students are more sensitive to price differences than more affluent students are. It's easy to imagine a family with little discretionary income struggling to piece together the funds for college and seeing no choice other than allowing a $5,000 price differential to be the deciding factor. In contrast, a family with an income of $300,000 might well encourage their child to enroll in the best school she can get into—the one that feels most appropriate, regardless of price. And a $150,000-a-year family will fall somewhere in between. Price will matter, but it will take bigger price differences to sway a decision away from a first-choice institution.

Some students and parents may react differently to a scholarship that provides a discount from a high price than they would to the same price without that appealing incentive. This may be because the high sticker price conveys a sense of quality, or it may be because the scholarship makes them feel that the institution particularly values their student.

It's not always easy to know how much of a discount particular students require to be convinced to enroll. Inquiries about better aid packages may not provide clear evidence, since low-income and first generation families are less likely to be assertive. Moreover, the factors distinguishing families with the ability to pay who are really likely to opt for the "best deal" from those who, while wanting to be sure to not to leave money on the table, don't have price at the top of their lists of deciding factors, are not obvious.

Many institutions rely on enrollment management consultants to guide decisions about allocating financial aid. These consultants can bring valuable expertise and experience, but they should not be making the decisions on their own. Their craft is not a science, and their priorities may not be identical to those of the institution. The widespread influence of this industry has almost certainly increased competitive expenditures on "merit" awards.

Questions Board Members Should Ask

Has the institution experimented with alternative-aid strategies and evaluated the effectiveness of both need-based and non-need-based aid?

Is the institution carefully monitoring the models and advice provided by external consultants?

Which students are most likely to be sensitive to changes in financial aid awards and which students would be more likely to respond to other efforts to attract them to the institution?

What is the difference between need-based aid and non-need-based or "merit-based" aid? Do these types of aid have different impacts on enrollment?

The term "merit aid" is frequently used to apply to any institutional aid that is not based on financial need. Sometimes it really is merit aid and is limited to the students with the strongest academic credentials. But sometimes it is just "non-need-based" aid, going to all or most accepted candidates.

The line between need-based aid and non-need-based aid is not so clear. Some institutions, particularly the most selective ones, allocate all of their institutional grants on the basis of financial need. Students with the most limited incomes and assets get the most generous aid packages, and those deemed able to pay the full price on their own are expected to do so. With relatively small percentages of applicants accepted, the reward for merit is the acceptance itself. These schools do compete with each other, but large percentages of accepted candidates choose to enroll, budgets are sound, and the purpose of financial aid is to ensure that the most-qualified class possible can be enrolled.

At other institutions, while supporting students who cannot afford to pay on their own is the primary purpose of financial aid, institutional grants are also used to increase the probability that students who can pay will choose to enroll. There may be merit awards for those with the highest test scores, for those with particular leadership skills, or for musicians.

Another model, which is increasingly common, is to give institutional grants—or discounts—to the vast majority, or even to all of those who are accepted. These "merit" awards are not really based on merit. They are just bargaining chips designed to increase enrollment.

Institutions that give the most generous grants to students with the highest test scores or the best high school GPAs may be heavily subsidizing relatively wealthy students, while leaving lower-income students to fend for themselves. But many non-need-based awards go to students who actually do have financial need. So if we ask what percentage of the aid budget is allocated based on criteria other than need, the answer is a larger number than if we ask what percentage of the aid dollars go to students who could afford to pay without assistance.

This is an important distinction. Some “merit aid” helps to meet financial need. Other “merit aid” takes dollars away from meeting need and from other parts of the budget in an attempt to increase the enrollment of students who can pay. Sometimes this merit aid diminishes the ability of the institution to address other priorities. But in some cases, if it is really effective, it can attract extra students and extra dollars and increase the net revenues available to meet those other priorities, such as adding courses, increasing faculty salaries, or providing more aid to low- and moderate-income students.

Questions Board Members Should Ask

How much of the financial aid at your institution is allocated on the basis of financial need and how much is allocated on the basis of academic, athletic, or other characteristics?

How much of the financial aid at your institution that is not need-based goes to students who have financial need?

Has there been careful thought given on your campus to the pros and cons of subsidizing students who can afford to pay the full sticker price?

How do we prioritize certain enrollment targets over others?

Financial aid serves multiple purposes, and it is important that boards discuss priorities, principles, and strategies with college and university administrators and other members of the community. There is frequently tension over the balance between need-based aid and “merit” aid, athletic aid, or other forms of aid designed to attract particular students.

Financial aid is sometimes required to fill seats. But on every campus, it is an important tool for shaping the class. Few institutions are satisfied with a student body that is homogeneous in terms of race/ethnicity or socioeconomic status. Without need-based institutional grant aid, enrolling low- and moderate-income students, black and Hispanic students, and others with particularly limited resources is not realistic. On the other hand, many institutions are dependent on net tuition revenues to fund their programs and do not think they can afford to focus on supporting access and diversity at the expense of attracting students with resources. It seems contradictory to speak of offering discounts in order to enroll full-pay students, since they are obviously not paying the full price under these circumstances. Rather, the issue is that a $10,000 discount from a $50,000 price yields much more net revenue than a $30,000 award to a lower-income student.

On every campus, there should be conversations about institutional values and priorities. It is important to recognize that the financial aid budget can support multiple goals. That said, the tradeoffs are real, and institutions that emphasize increasing the test scores of their incoming students and use their financial aid budgets for this purpose are likely to be sacrificing access and socioeconomic diversity.

Questions Board Members Should Ask

Is the institution satisfied with the size and characteristics of the student body?

If the goal is to raise the level of the academic credentials students bring, what is the motivation for this goal?

What are the trade-offs involved in enrolling a class with more students who cannot afford to pay the full sticker price?

Should "need-blind admissions" and "meeting need" be goals for most institutions?

Over half of the four-year colleges and universities in the U.S. accept at least 75 percent of their applicants, so the question of whether or not financial circumstances should affect a student's probability of admission is relevant for a limited number of institutions. However, for those colleges and universities in a position to use the admissions process to shape their classes, it is a very important question.

Many institutions find that they have more qualified applicants with financial need than their budgets will support.

The issue sounds straightforward. It's hard to argue that it is fair or desirable that colleges and universities whose goal it is to provide educational opportunity to students who can make the most of the experience should turn away applicants because they can't afford the tuition. Rather, financial aid should support these students. In fact, knowing the challenges of growing up in disadvantaged families, neighborhoods, and elementary/secondary schools, it would seem reasonable to be more favorable towards low-income students than to those from more privileged backgrounds with the same grades and test scores.

But many institutions find that they have more qualified applicants with financial need than their budgets will support. Accepting candidates without meeting their financial need means either that they won't be able to enroll, so the acceptance is not meaningful, or that they will enroll and face serious financial problems. It seems more responsible to turn them down. Most "need-aware" institutions accept most of their class without regard to financial need, but when they get to the marginal admits, they look for those who can pay. In other words, rather than using different admissions criteria overall for students who can pay the full price and those who cannot, they accept the most qualified students. However, because they have limited budgets for financial aid, at some point in the admissions process, they do pass over some students with financial need in favor of less qualified students who do not require financial aid. They may also grant admission to some applicants whose parents are alums and/or have made sizeable donations, even if those applicants are less qualified than some others who are not accepted.

Each institution facing the choice of committing to a need-blind admissions policy must carefully consider the pros and cons and ask the following questions:

- How many students are affected by the current policy?
- How are the students who gain admission because of the policy different from those who are rejected because of it?
- What impact would this commitment have on the budget?
- What would happen if another recession hit and many more applicants had more financial need?
- What priorities would lose out if the financial aid budget grew to support a need-blind admissions policy?

Institutions that do not have the necessary resources or are not willing to make the trade-offs involved in accepting all qualified low-income students in the pool and providing them with ample financial aid should acknowledge the constraints they face and be clear about their policies.

Questions Board Members Should Ask

Does ability to pay enter into admissions decisions at your institution and, if so, how many applicants are affected?

What would be the likely impact on the budget of ignoring financial circumstances in admissions decisions?

Is the institution meeting the financial need of the students who are accepted by packaging ample grant aid? Or are there significant gaps between the resources students need and those the institution can provide—gaps that would grow if more high-need students were admitted?

How are institutional enrollment and aid policies related to the growing concerns about student debt?

Press coverage of student debt is quite misleading. It is not uncommon to read about a student who borrowed $80,000 or $100,000 on the way to a bachelor's degree. Buried in the article might be a reference to the reality that among the 70 percent of bachelor's degree recipients who graduate with debt, the average amount borrowed is about $30,000. Among 2011–12 bachelor's degree recipients, about 5 percent had accumulated as much as $60,000 in debt. Less than one half of one percent borrowed $100,000. [2]

A key problem with many of the discussions of the impact of student debt is that they compare people with student debt to people with similar levels of education and similar incomes who don't have debt. Of course those whose parents were able to pay are better off. But the real question is: When students borrow money to enroll in your institution, do they end up better off than they would have been making another choice?

[2] NCES (National Center for Education Statistics), National Postsecondary Student Aid Study, Power Stats calculations. http://nces.ed.gov/datalab/

Too many students leave college without a degree.

If many students borrow and don't graduate, or if many students graduate with more than $40,000 or $50,000 in debt, the institution has some real soul searching to do. Why are students borrowing so much? Are they getting an education and a credential that makes it worth it? What could the institution do to mitigate this problem? It's not just that the Department of Education and Congress have started to look more closely at institutions with many students who have high debt levels. It's also that some institutions may be leaving their students worse off than they found them. Higher education's mission certainly goes beyond increasing students' lifetime incomes, but it is irresponsible and unethical to put students in a situation where they pay so much for college that they never see financial benefits.

Questions Board Members Should Ask

How many of your students borrow to help finance their education, and what is the average debt level at graduation? How many students borrow much more than the average?

How have borrowing patterns at your institution changed over time?

Are there changes in your financial-aid policies that might reduce the extent to which your students have to rely on loans?

How should institutions think about the shift in the national conversation from college access to college success?

As recently as 10 years ago, people concerned with unequal access to higher education across demographic groups and the population's overall level of educational attainment devoted all of their attention to college access. The concern was that the price of a college education excluded too many people from disadvantaged backgrounds. Public and institutional policies, therefore, should do as much as possible to correct this problem by subsidizing these students and bringing prices within reach.

While the access question remains very real and quite challenging, attention has broadened to focus more on college success and degree completion. We have done a much better job of getting students from all backgrounds into college than we have of supporting them in achieving their goals. Too many students leave college without a degree, and the gaps in completion rates across income groups are larger than the gaps in enrollment rates.

Board members should pay attention to their institutions' retention and graduation rates and consider the causes and implications. It's not just that the federal government is focusing on this issue and making the information public. It's also that institutions are not accomplishing their mission if students are not leaving with credentials of value.

There is not only one standard for an acceptable completion rate. Institutions that enroll better-prepared students have higher graduation rates than those that accept students facing greater challenges. However, increasing selectivity is not the best approach to solving the completion problem. Rather, finding ways to better support students and help them overcome challenges should be the goal. Financial aid may well play a part, since money problems contribute to many students' inability to achieve their academic goals.

Questions Board Members Should Ask

What percentage of students who enroll at your institution complete associate degrees within two to three years, to bachelor's degrees within four to six years? Are the rates very different for students from different socioeconomic and racial/ethnic backgrounds?

How does your graduation rate compare to those at other institutions enrolling similar student bodies?

What kinds of academic, social, and personal support systems are in place to help students complete their degrees?

Do institutions have to choose between a commitment to equity and access or a focus on efficiency and fiscal stability?

If an institution succeeds in winning desirable applicants from peer institutions by offering non-need-based aid, the peer institutions are not likely to sit by idly. They will offer competitive packages. It is easy to see how competition for these students can lead to a price war, depleting institutional funds without bringing any more-qualified and well-heeled students into the applicant pool. Everyone will lose in the long run—except those lucky students who could have paid full price, but who now enjoy lower net prices than even students from the lowest-income families.

The issue of destructive competition that can lead to losses for all is frequently difficult for institutions to grasp. They look at short-term successes and can't see how it could be in their interest to sacrifice those successes for the greater good. But the reality is that if all institutions behave this way, those students without the ability to pay will simply drop out of the pool, and collectively the institutions will not be able to improve the quality of the students they enroll.

Increasing selectivity is not the best approach to solving the completion problem.

In fact, equity and efficiency frequently reinforce each other, both from society's perspective and for the individual college or university. Equity dictates that each institution provide the best possible education to the students who are qualified to enroll—regardless of ability to pay. That means making need-based aid a priority—possibly at the expense of institutional prestige, some campus amenities, programs, or other worthy expenditures.

Efficiency means making decisions that allow the institution to provide as much quality education at the lowest cost possible and ensuring that the institution has a strong bottom line in both the short term and the long term. Rising in the rankings might be a good way to attract more applicants. Providing discounts to students who could afford to enroll elsewhere to draw them to campus might increase net revenues. Ensuring financial strength is a pre-requisite to providing equitable opportunities. In other words, a focus on equity does not mean ignoring efficiency. And a focus on efficiency cannot exclude equity.

Recognizing that making ethical choices is not always straightforward does not diminish—and in some ways underscores—the importance of keeping ethics at the forefront of the decision-making process. There is no question that, in recent years, the pendulum in admissions and financial aid has swung too far from a focus on equity and access and toward a focus on improving the prestige or the bottom line of the institution. Campus decision makers should reject the notion that ethical priorities are a luxury they cannot afford.

Questions Board Members Should Ask

How do your institution's merit-aid awards compare to those of your competitors?

Is there a good balance between long-term and short-term goals for aid?

Do people tend to debate need-based versus merit-based aid or are they open to the idea that these policies may complement each other?

Conclusion

Institutional financial aid serves multiple purposes. Without this assistance, students from disadvantaged backgrounds, and even many from middle-class households, would be unable to enroll. If these students do enroll, but receive inadequate financial support, their chances of succeeding in college are reduced, and if they do graduate, they risk accruing excessive debt.

But financial aid is not just about supporting students who cannot afford to pay. Grants—or discounts—to students also influence the enrollment decisions of students with financial means and multiple options. Board members should be part of the conversation on campus that defines enrollment goals, priorities for financial aid, and the principles on which decisions about unavoidable tradeoffs should rest.

About The Author

Sandy Baum is a senior fellow at the Urban Institute and a research professor at the George Washington University Graduate School of Education and Human Development. Professor emerita of economics at Skidmore College, Dr. Baum earned her BA in sociology at Bryn Mawr College, where she is currently a member of the board of trustees, and her PhD in economics at Columbia University. She has written and spoken extensively on issues relating to college access, college pricing, student aid policy, student debt, affordability, and other aspects of higher education finance.

Dr. Baum has co-authored the College Board's annual publications *Trends in Student Aid* and *Trends in College Pricing* since 2002. She also co-authors *Education Pays: The Benefits of Higher Education for Individuals and Society.* She wrote the 2011 AGB publication, *Tuition and Financial Aid: Nine Points for Boards to Consider in Keeping College Affordable.* She chaired the College Board's Rethinking Student Aid study group, which issued comprehensive proposals for reform of the federal student aid system in 2008, and the Rethinking Pell Grants study group, which issued recommendations in April 2013. She chaired a Brookings Institution study group that issued its report, *Beyond Need and Merit: Strengthening State Grant Programs,* in May 2012. Recent work includes studies of how behavioral economics can inform student aid policy, a meaningful definition of college affordability, and tuition and financial aid strategies for broad access to public institutions. She is a member of the board of the National Student Clearinghouse.

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