

Cost of Higher Education: The Miller Center National Debates

Background: Understanding Higher Education's Business Model

As the recession has taken its toll on several businesses, people have begun to examine their business models to determine where the failure occurred. Higher education seems to be included in this examination as its increased costs threaten to outstretch the capacity of the public to pay for it.

With for-profit industries, the business model is based on producing a quality product, at a reasonable price that will entice the public to buy. When firms fail, new companies, often with lower production costs or new technologies, enter the market place to displace older industries and provide consumers with newer, often better, products. The company's main responsibility is to provide a quality product at an optimum price. Those who can do it best receive the largest market share and thus their business model succeeds. If they don't or if its product doesn't satisfy the needs of the customer, the customer has the option of going somewhere else.

In looking at whether higher education's business model is succeeding, it's important to first state society's expectation of higher education and its responsibilities. The public relies on higher education to provide educational opportunities for all citizens able to benefit. In addition to preparing students for the job market with a quality education in a designated field, higher education is also responsible for instilling civic and community leadership—essential skills in a democratic society. Higher education is also expected to develop new knowledge and share that knowledge through education, public service, and support economic development. In considering whether higher education's business model is successful, one must consider not just whether institutions can stay financially solvent, but also meet these vital social responsibilities.

Another factor to consider when examining higher education's business model is the failure rate. A shocking percentage—one in two—students will fail to complete a bachelor's degree. Worldwide, the United States has slipped to 15th on college degree completions and 7th in the percentage of young adults enrolled in college.

History of Funding Higher Education

Before the 1980s, most of the expense for a college education was picked up by the states. In some areas this meant college tuition was virtually free for the student. After 1980, state support declined. As an example, state support for public education institutions dropped from \$7269 per student in 1985 to \$6445 per student in 2005, an 11.3 percent decrease. What this means is that the cost of higher education has shifted from the general taxpayer to the individual student and family. As states continue to experience budget challenges, it's unlikely this trend will change soon.

Public education institutions responded to the dwindling state support by seeking funds from other sources—philanthropy, research support, and the primary source, increased tuition. As a result, the cost for a four-year-in-state tuition was \$7020 in 2009 and total expense, including room and board and incidentals averaged \$19,338. Tuition for a four-year private college or university in 2009 was \$39,028. This translates to a four-year college education cost of nearly \$80,000 for public institutions and \$160,000 for private.

These increased costs have had a tremendous impact on students and families in affording a college education. Figure 1 shows the growth of medium family income with a variety of other spending categories. While medium family income from 1982 to 2006 rose by 147 percent, college tuition and fees rose 439 percent. This increase has affected lower income families the most as the cost for a two-year and four-year education takes up a larger percentage of their income. The result will be that rising costs will discourage many lower and middle income students from going to college.

Managing its Business Model—Reasons for the Increased Costs

A major concern related higher education's business model is that colleges and universities cannot or will not control their cost increases. In for-profit industries when productivity goes up, salaries usually go up. This is different in public education. Though the number of students seen by college and university faculty and the number of graduates remains relatively the same year to year, the cost of faculty salaries goes up every year. This is due to the fact that if they didn't, college and university professors would go into other lines work where salaries for similar education and experience do increase.

Another reason production costs are hard to control in higher education is that to attract students and provide a broad range of opportunities, colleges and universities provide an endless array of worthy activities and so institutional leaders raise money to spend on these worthwhile activities. As a result, the increased costs in higher education do not follow traditional business model of higher the productivity drives and justifies higher revenue.

Others argue the reason higher education costs have increased is the accessibility of large government grants and loans such as Pell Grants and Guaranteed Student loans create an impression that students have ways to afford the costs and thus higher education institutions don't have much incentive to cut costs. In a similar way it is said that due to the high desirability and prestige of a college education, ambitious students will pay any price to attend a quality school.

The Unknown Effects of Future Events

One factor that has already been introduced into many higher education institutions but whose impact is not yet fully known is the implementation of online courses. Will this new technology have the potential to make traditional face-to-face instruction go the way of traditional newspapers? Could entire courses be developed online and used as substitutes for faculty taught classes? Wholesale replacement of faculty doesn't seem likely. Pure online courses seem to work best with older, part-time students who can work from home one course at a time. Increased costs of residential higher education might accelerate this process, but right now it seems unlikely there will be a complete shift.

Another factor that might pose a threat to higher education's business model is the regionally accredited, degree granting, for-profit institutions such as the University of Phoenix. During the latest recession, this industry grew and performed well while traditional institutions lost revenue. They seem to be most successful attracting the older, adult students and rely on this market, but there is little evidence that this group will become a viable competitor for most of the undergraduate students.