Strengthening the Federal Role in the Federal-State Partnership for Funding Higher Education

Sandy Baum and Michael McPherson

December 2020

The national interest in narrowing the gaps in educational opportunity across socioeconomic, racial, and ethnic groups and in increasing educational attainment cannot be addressed without a strong federal effort. The current system has failed to achieve these goals. State funding has not kept up with increased enrollments, and during economic downturns, the prices students pay rise and the resources their institutions have to support their success decline. Moreover, there is dramatic variation in the opportunities available to students depending on their state of residence. Ameliorating these problems will require policies that will help students with limited means pay for college and will also support states and institutions in providing high-quality, affordable education to students from all backgrounds.

The pandemic has severely strained state budgets, and they will not recover quickly. History provides lessons about what happens to public college tuition under these circumstances. When funding per student declines, tuition rises rapidly. Absent federal action, the small tuition increases of the past few years will be replaced by steep increases alongside declines in funds available to institutions to support their programs.

Circumstances differ considerably by state. The range of appropriations levels, tuition prices, financial aid programs, and college enrollment and completion rates across the nation show the different priorities of state governments. This variation generates stark differences in educational opportunities among people in similar circumstances who happen to live in different places. This inequality increases the importance of federal action at the same time that it complicates the development of a more equitable and efficient federal-state partnership.

Currently, the federal government’s best tool to lessen the impact of rising tuition prices is Pell grants for low-income students. Policymakers could choose only to increase federal investment in Pell, but it may be time for a more involved partnership that would provide states incentives to adequately fund higher education and ensure more equity across states. In this brief, we explore mechanisms the federal government might use—and the inherent trade-offs of each—to ensure students across the country have access to affordable, high-quality college options.

The Current Federal-State Partnership

Many calls for increasing college affordability focus on building a federal-state partnership that would involve the federal government providing funding to states or public colleges and universities in exchange for agreements about keeping prices down. Some proposals involve greater oversight responsibilities for the federal government.[1] Some proposals would exclude states or institutions that do not agree to make tuition free or allow all students to avoid accumulating debt.[2] Conversations surrounding these ideas rarely articulate them as developing out of the current federal-state partnership for funding higher education. But the reality is that the federal government has borne an increasing share of higher education costs over time.

States provided almost $13 billion in financial aid to students in 2018–19, but most of the funds they appropriate for higher education go to institutions—almost entirely public institutions—to fund their operations. In contrast, the federal government provides funding for research and other grants and contracts to institutions, but most of its higher education funding is in the form of financial aid to students.

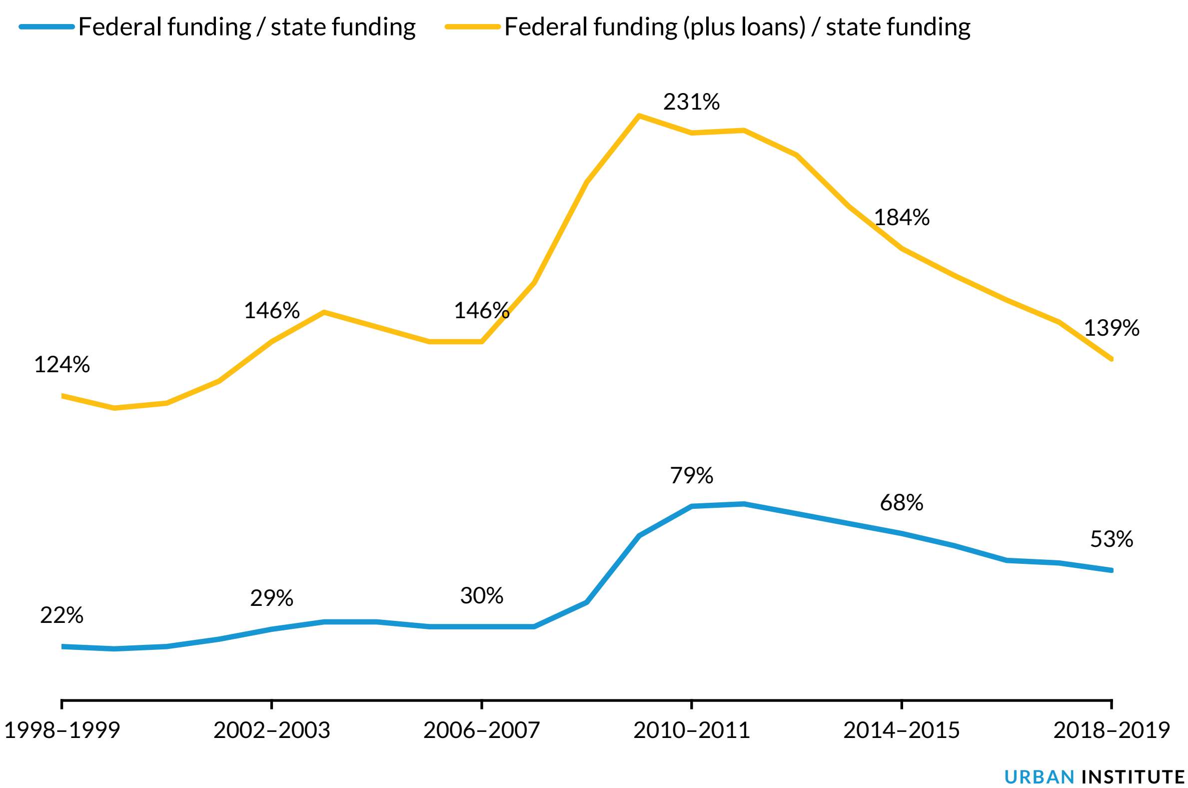
In 1998–99, the $20.1 billion (in 2019 dollars) in federal grant aid and tax credits and deductions to students equaled 22 percent of the $58.3 billion that state and local governments provided to higher education. By 2008–09, that ratio had risen to 40 percent. After rising to a peak of 80 percent because of changes during the Great Recession, these federal subsidies to students were 53 percent of state and local funding in 2018–19 ($55.3 billion versus $105.2 billion). Including education loans yields a federal total ($143.9 billion) that is 39 percent higher than the state and local funding amount.

The trend over the coming years will depend on how states handle post-COVID-19 challenges and how the federal government chooses to support educational opportunity.

FIGURE 1

Federal Aid Relative to State and Local Support for Higher Education, 1998–99 to 2018–19

The federal role in financing higher education has grown over time



Source: Authors' calculations based on State Higher Education Finance data from the State Higher Education Executive Officers Association and Jennifer Ma, Matea Pender, and CJ Libassi, *Trends in College Pricing and Student Aid 2020* (New York: College Board, 2020).

Variation across States

States have a wide range of levels of appropriations per student and tuition prices. In 2020–21, average tuition and fees at public four-year institutions range from $5,790 in Wyoming and $6,370 in Florida to $16,960 in New Hampshire and $17,510 in Vermont. At public two-year colleges, prices range from $1,430 in California and $1,940 in New Mexico to $7,100 in New Hampshire and $8,600 in Vermont.

In 2018–19, appropriations per full-time equivalent student ranged from $3,180 in New Hampshire and $3,300 in Vermont to $18,990 in Hawaii and $19,010 in Alaska. Ten states provided $5,700 or less per student, and 10 states provided more than $9,400.

Some states choose a high-tuition model with high need-based aid so their limited resources can most effectively target low-income students. In New Jersey, where tuition and fees for full-time, in-state students at four-year institutions average $14,380, state grant expenditures account for a relatively large share of total appropriations, and need-based state grant aid per student is the highest in the nation. A federal policy that focuses either on published tuition prices or on average prices net of grant aid without respect to which students pay higher net prices and which pay lower net prices will discourage this approach, spreading subsidies more equally across all students regardless of their financial capacity.

What Is the Best Way for the Federal Government to Increase Its Role in Funding Higher Education?

The federal government can increase its role through several strategies. It does not have to choose one approach at the exclusion of others but must find an appropriate balance for the distribution of federal funds.

Strengthen the Pell Grant Program

Pell grants are awarded to students whose financial circumstances limit their ability to pay for college. The largest grants go to the students with the fewest resources. Grant levels decline gradually as students' and families' ability to pay increases. Students can use their funds at any eligible public or private school to pay tuition or for the nontuition expenses that account for a large share of most students' budgets.

Many advocates and policymakers, including president-elect Joe Biden, have proposed doubling the Pell grant maximum, currently set at $6,345, an increase from $6,195 in 2019–20 and $5,775 in 2015–16.[3] A bill introduced in the House of Representatives in 2019 proposed increasing the maximum grant in 2020–21 to $10,230. Other bills would fund Pell grants entirely through mandatory spending, link the maximum grant to inflation, or otherwise increase the program's coverage and generosity. In deciding whether and how to adjust Pell, federal policymakers should consider the following:

- The $6,345 maximum Pell grant for 2020–21 does not cover student living expenses, even for the rare students whose tuition and fees are covered by aid other than Pell. Students who work at the minimum wage for 15 hours a week for 30 weeks during the academic year—the most that could reasonably be expected of someone also enrolled full time—would need about $8,000 of additional aid to generate an income equal to 150 percent of the federal poverty level for a single person, even before considering paying for books and supplies.
- In 2017–18, 20 percent of dependent Pell grant recipients were from families with incomes below $20,000, and 95 percent were from families with incomes below $60,000. Under the current system for allocating Pell grants, every increase in the maximum award automatically increases the income levels at which students are eligible. Modifying the formula, as in the FAFSA Simplification Act of 2019,[4] could allow the maximum income level and the maximum grant to be determined separately.
- Researchers, advocates for students, and many members of Congress have long pushed for simplifying both the application process and the formula for allocating Pell grants to reduce barriers for low-income students. For most current Pell recipients, a simple formula would have

little impact on award levels. As higher-income students are brought into the program, however, more recipients will be from families with more complicated finances. Notably, the wealth differences between Black families and white families with similar incomes are more relevant for determining differences in financial capacity among middle-income families than among low-income families.

- Estimates of the cost of doubling the maximum Pell grant without changing the formula indicate that the program's cost ($28 billion in 2019–20) would more than double.[5]
- Increasing the Pell grant is vital but will not address the inequality of opportunities for residents of different states.

Provide Federal Funding to Supplement State Funding for Higher Education

Another set of proposals focuses on directing federal dollars to states or institutions. In 2016, both Bernie Sanders and Hillary Clinton proposed federal programs to supplement state funding to lower or eliminate the tuition students pay at public institutions. The Obama administration proposed using federal dollars to ensure that no community college students would have to pay tuition for two years of study. The Biden plan includes a similar provision, proposing a federal-state partnership with the federal government covering 75 percent of the cost and states contributing the remainder. The Debt-Free College Act of 2019, introduced by Senator Schatz (D-HI), would require the US Department of Education to award grants for federal-state partnerships to provide debt-free college for students at in-state public institutions and at historically Black colleges and universities and minority-serving institutions.[6]

FREE AND DEBT-FREE COLLEGE

Proposals for "free" or "debt-free" college are politically popular, but who would benefit and how much it would cost depends on program design. As policymakers navigate college affordability program designs, they should consider the following:

- "Free" and "debt-free" mean different things. "Free college" almost always refers to tuition or possibly tuition and fees. "Debt-free tuition" means students can pay their tuition without borrowing—that their expected family contribution plus grant aid will cover tuition and fees. Students from affluent families would still pay tuition. Unlike free college programs, debt-free tuition programs direct their funds to students with the most limited resources.
- "Last dollar" versus "first dollar" is an important distinction. Last-dollar programs fill in the gap between existing grant aid and new sources of aid, providing most of the new funds to students whose incomes are too high to qualify for federal and state need-based aid. These programs do not leave students with funds to help cover nontuition expenses. First-dollar programs, like the one Biden proposes and the College for All Act of 2017,[7] provide aid to all students to cover their tuition and fees. Students with aid from other sources can use that money to meet nontuition expenses.

- Even with free tuition or debt-free tuition, many students will have to borrow to cover their living expenses. (Students who now receive enough grant aid to cover their tuition and fees accumulate almost as much debt as other students.[8]) Debt-free college is more ambitious. Students would not have to borrow at all (although they could still borrow if they wish). Senator Schatz's debt-free college proposal would create a one-to-one federal match for state spending on higher education and use those funds to fill unmet need for students pursuing college degrees.[9] Any college expenses above a student's expected family contribution would be covered, with priority going to Pell grant recipients. Students who can pay the full cost of attendance would not receive funding. All dollars would go to those who cannot afford to pay on their own.

- President-elect Biden's proposals for higher education include federal subsidies to make community college tuition-free for all students and public four-year institutions tuition-free for students with household incomes below $125,000. Basing eligibility on financial circumstances makes sense, but it would be inequitable for students with household incomes of $125,001 to pay much more because of an extra dollar of income. Moreover, single adult students with incomes of $100,000 can afford college more easily than students whose parents are responsible for paying out of their $100,000 incomes. A single income threshold may sound simple, but policymakers should consider having the subsidy phase out above an income threshold and consider accounting for family size by basing eligibility on income relative to the federal poverty level.

FINANCING FREE OR DEBT-FREE COLLEGE: REQUIRED STATE MATCH

In addition to deciding which kind of free college plan to pursue, the details of the partnership between the federal government and state governments can differ. Policymakers should consider the following:

- Proposals to cover existing tuition, as suggested in the College for All Act, will direct more funds to states that have higher tuition prices than to states that have been providing enough funding to keep tuition moderate. An alternative would be to fix the subsidy at the national average tuition and fee level or at some estimate related to the average cost of educating students. Such a system would require greater funding increases from states that now have lower appropriations levels.

- To finance the match, states would need to devote more of their own resources to higher education or reduce institutional operating budgets to free up funds. This system raises questions about opportunities for students in states that do not participate and about the adequacy of institutional resources in participating states.

- If some states refuse to participate in a federal matching program—as some states have refused federal subsidies under the Affordable Care Act—will their students just be out of luck? It is unlikely that the federal government will promise to fully cover out-of-state tuition wherever students choose to enroll. A more generous Pell grant program would mitigate this problem, but it would be best to design a program that matches state funding, even if that funding is too low to accomplish all national goals, rather than exacerbating differences in students' opportunities from state to state.

- A last-dollar program under which Pell funds cover part of tuition and fees would likely cost $65 to $70 billion a year, the total net undergraduate tuition revenues public institutions receive beyond federal student aid. This cost would be split by federal and state governments. A first-dollar program, which would allow students to use their Pell dollars for living expenses, would cost more than $80 billion a year.[10]
- As made clear by the COVID-19 crisis, state revenue constraints are likely to make it impossible for states to maintain the promised low (or zero) price for all students in economic downturns. Maintenance-of-effort requirements are critical to ensure federal funds supplement state funds, rather than replace them. But good intentions can be stymied by economic realities, and a partnership program should provide for an increased federal contribution in cases where a recession sharply decreases state revenues. The Bipartisan Policy Center proposal that states be required to allocate funds annually to a rainy-day fund could also help address this issue (Hoagland et al. 2020).

AN ALTERNATIVE APPROACH TO FUNDING A FEDERAL-STATE PARTNERSHIP

- Another approach is to give federal funds to states to provide a match for state contributions to higher education. Rather than focusing narrowly on tuition charges, this type of program would reward state investments, making it possible for states to adopt lower tuition and more generous need-based grant aid, as well as better funding of institutions, particularly those that enroll large numbers of low-income students.
- A matching system for appropriations would provide more federal funding to states that provide more support for higher education or that more successfully increase their level of support. It would not have to involve all-or-nothing participation for states. This approach would focus on lowering prices for students and providing more resources for institutions but would not require states to reach zero (or debt-free) tuition levels.
- Some partnership funds could encourage state need-based aid. The now-defunct LEAP (Leveraging Educational Assistance Partnership) Program provides a precedent for this approach.

INSTITUTION-LEVEL CONSIDERATIONS

As these considerations make clear, matching state funding is likely to be more effective in strengthening education than just covering tuition. But the distribution of that funding among institutions is also critical.

Currently, funding per student is far lower at community colleges and broad-access public four-year institutions than at flagship universities with more selective admissions criteria. The federal government could provide incentives for states to allocate funds across institutions and across students in ways that reduce disparities between students from disadvantaged backgrounds and students with more resources. This is likely to involve more generous funding of the broad-access institutions that educate most students from the lower half of the income distribution. One option might be to use different matching rates depending on the financial circumstances of students benefiting from state subsidies. Or the federal government might provide subsidies to colleges and universities based on the Pell grant eligibility of students who succeed. This approach shares the goals of the Biden proposal for a Title I–type program for higher education.

A program through which the federal government provides funds to states or institutions to supplement state and local appropriations in funding public higher education would be a more radical change than expanding Pell grants. Designing such a program is not simple, and it would be prudent to launch experimental programs with rigorous evaluation before implementing a large-scale national program. Inevitably, some provisions will be less effective than anticipated, and some will cause unintended and undesirable consequences. But this type of partnership could increase opportunities and reduce inequities beyond the reach of the Pell grant program or other types of student aid.

Focusing on Quality and Student Success

Proposals for a larger federal role in the federal-state partnership for funding higher education generally focus on price rather than on student outcomes or educational quality. Lower prices are important, but they do not solve all problems related to educational attainment or affordability. Any such program must also focus on educational quality, resources that support students, and student outcomes. It is not enough to encourage students to enroll in college. For most students, making the investment pay off well requires successful completion of a high-quality credential. Without provisions to prioritize spending on student supports at broad-access institutions, states and institutions will likely be forced to devote all their available resources to keeping prices down, rather than to improving or even maintaining quality.

An alternative—or a supplement—to a broad federal program to subsidize state spending on higher education could involve a competitive grant program along the lines of the Race to the Top program included in the American Recovery and Reinvestment Act of 2009 for K–12 education.[11] A growing body of evidence indicates that added spending at less selective postsecondary institutions increases completion rates and is even more effective than giving students equivalent extra money or lowering tuition prices. Running an award program for institutions that financed specific initiatives such as intensive student advising or use of predictive analytics—and carefully evaluating effectiveness—could lay the groundwork for a national program.

Increased federal funding will generate an appetite for increased federal regulation of the ways colleges and universities are run. But the federal government is ill equipped to run these institutions or to set requirements that likely will fail to recognize the wide variation in institutions, programs, student demographics, and state needs. Instead, the federal government should develop appropriate accountability metrics to ensure that keeping prices down does not push quality improvement off the agenda. The focus should be on student outcomes.

TABLE 1

Options for Expanding Federal Investment in Higher Education

	Policy Options for the Federal Government			
	Fund free public tuition with a required state match	**Fund debt-free public tuition with a required state match**	**Match state spending on public higher education**	**Fund large increase in Pell**
Impact on federal budget	High (depends on match and state participation)	High, but lower than free tuition	Limited (depends on match and state funding levels)	Limited (depends on maximum Pell and other formula provisions)
Impact on state budgets	High for participating states (depends on required match)	High for participating states, but lower than free tuition (depends on required match)	At state discretion; dollars go further because of federal match	None
Impact on institution budgets	Could lead to declines in operating funds because top priority is holding prices down; size of effect depends on details of maintenance of effort	Some downward pressure on operating funds possible, but less than under a free tuition plan	More funds available; divided between lowering prices and increasing quality	None; institutions might choose to reduce grant aid budget
Federal regulatory burden	High	High	Moderate	Low
Distribution of benefits to students and families	Toward high-income students because of college enrollment patterns, particularly if last dollar	Toward low-income students, because high-income students would contribute according to ability to pay	Depends on state decisions about pricing, allocations to institutions, and operating budget decisions; higher spending (and matching) for broad-access institutions shifts subsidies to less affluent students	Focused on low- and moderate-income students; could bring more middle-income students into the program

Conclusion

The federal government has a responsibility to provide opportunities for all citizens. It should not stand by while states that do not prioritize education deny opportunity to their residents.

The federal government has, in fact, taken an increasing role in financing higher education. It does this primarily through financial aid to individual students. The Pell grant program, which awards grants to low- and moderate-income students, is a critical piece of making college possible for students who cannot afford to pay on their own. But the grants are not now adequate to support expenses students must cover beyond tuition and fees to succeed in college. It is time to increase funding for this program.

It is also time to consider the nature of the federal-state partnership, the logic underlying it, and the strengths and weaknesses of approaches to modifying it. Only with this perspective can Congress make informed decisions about proposals for reforming the federal role and about the trade-offs involved in delivering funds to states or institutions to provide incentives for them to change their behavior, as opposed to putting all new federal dollars into the Pell grant program or other aid that goes directly to students.

Funding students is not enough. State and local appropriations for public higher education have proven unstable and have not kept up with the nation's growing need for college education. Moreover, the variation across states in the availability of affordable, high-quality higher education is not in the national interest. The federal government should provide incentives for states to increase their funding and distribute it equitably and should supplement that funding to increase educational opportunities.

A balanced policy should reflect a combination of increasing federal need-based grant aid to students and strategically supporting state investments in higher education. Federal student aid mainly helps students and families with the most limited incomes. Tuition reduction is of most interest to families that now must pay full tuition or close to it and would like to minimize both the amount they pay and the need to borrow. Federal subsidies for appropriations can increase institutional resources, supporting increased student success and program completion, a widely shared national goal, in addition to lowering tuition prices.

A well-designed partnership will focus on both quality and price. Tuition-free college may not be a bargain if the price of making college free is a fiscal squeeze that causes fewer people to graduate or causes graduates to have weaker career performance. A partnership that best supports low-income students would direct support particularly to institutions that educate large numbers of students from low-income backgrounds. It should allow students to use their need-based grant aid for nontuition expenses and should not draw sharp lines between students who receive generous benefits and those with slightly higher incomes who receive no benefits. Matching state funding to encourage states to make higher education a priority but accommodating economic cycles is likely to be a more workable plan than just covering the tuition that states and institutions charge.

The costs of such a program—to the federal government and to the states—will depend on the details. The choice of strategies for lowering the federal cost could have serious implications for program effectiveness. For example, a first-dollar program that allows students to use their need-based aid for nontuition expenses will require more money than a last-dollar program, which only fills gaps to cover tuition. But abandoning the first-dollar approach would help high-income students at the expense of low-income students. An alternative would be to lower the income cap on eligibility. A program covering tuition for all students from households with incomes below $125,000 would include about 85 percent of undergraduate students (75 percent of dependent students and 95 percent of independent students). Lowering the income limit to $100,000 would include nearly 80 percent of undergraduate students (65 percent of dependent students and just over 90 percent of independent students).[12]

The federal government should demand reasonable accountability for the use of its funds in achieving desired outcomes. But states and localities are frequently better equipped to determine the best way to reach those goals. The federal government should limit its role to financial support guided by outcome-oriented accountability rules defined around such matters as improved completion rates and better placement of students in jobs with living wages and further education. Federal authorities should avoid interfering with the design and running of higher education institutions.

The economic hardship generated by the pandemic makes it urgent that the federal government develop policies for a more active role in ensuring access to high-quality, affordable higher education for students across the country. The current Pell grant aid for low- and moderate-income students is vital but inadequate. The federal government should strengthen that program but also develop a program for long-term support of public colleges and universities that will provide incentives and support for states to increase their funding for higher education. Designing an equitable and efficient program requires acknowledging differences in resources and priorities across states and targeting limited funds to support students facing the largest financial barriers.

Notes

1 For example, under the College for All Act, "To qualify for federal funding, states…will need to maintain spending on their higher education systems, on academic instruction, and on need-based financial aid. In addition, colleges and universities must reduce their reliance on low-paid adjunct faculty. No funding under this legislation may be used to fund administrator salaries, merit-based financial aid, or the construction of non-academic buildings like stadiums and student centers" (Sanders, n.d.). In contrast, the Debt-Free College Act of 2019 imposes only such requirements as strengthening transfer mechanisms and establishing, implementing, or expanding college completion programs, including activities such as hiring counselors and increasing academic support programs.

2 The Debt-Free College Act of 2019 would require that states cap tuition and fees at public institutions of higher education as of the date of enactment of the act, with a yearly increase allowed based on the Consumer Price Index. See Debt-Free College Act of 2019, S.672, 116th Cong. (2019). Most plans promise federal support on the condition that states meet a portion of the costs of eliminating tuition and fees.

3 "Doubling Down on Doubling the Pell Grant," DoubleThePell.com, accessed December 7, 2020, https://doublethepell.com/; and "The Biden Plan for Education beyond High School," JoeBiden.com, accessed December 7, 2020, https://joebiden.com/beyondhs/.

4 FAFSA Simplification Act of 2019, S.2667, 116th Cong. (2019).

5 Matthew Chingos, "Evaluating Proposed Changes to Pell Grants," *Urban Wire* (blog), Urban Institute, December 3, 2019, https://www.urban.org/urban-wire/evaluating-proposed-changes-pell-grants.

6 Debt-Free College Act of 2019, S.672, 116th Cong. (2019).

7 College for All Act of 2017, S.806, 115th Cong. (2017).

8 Sandy Baum and Michael McPherson, "'Free College' Does Not Eliminate Student Debt," *Urban Wire* (blog), Urban Institute, August 22, 2019, https://www.urban.org/urban-wire/free-college-does-not-eliminate-student-debt.

9 US Senator Brian Schatz, "Shatz, Pocan Reintroduce Legislation to End Student Loan Debt Crisis," press release, March 6, 2019, https://www.schatz.senate.gov/press-releases/schatz-pocan-reintroduce-legislation-to-end-student-loan-debt-crisis.

[10] Estimates are based on authors' calculations from Integrated Postsecondary Education Data System data for 2017–18.

[11] American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 (2009).

[12] Based on estimates from the 2016 National Postsecondary Student Aid Study, adjusted for inflation.

References

Hoadland, G. William, Shai Akabas, Kenneth Megan, Jinann Bitar, Kody Carmody, Elizabeth Middleton, and Mariette Aborn. 2020. *A New Course for Higher Education: Strengthening Access, Affordability, and Accountability*. Washington, DC: Bipartisan Policy Center.

Sanders (Office of US Senator Bernie Sanders). n.d. "The College for All Act." Washington, DC: Sanders.

About the Authors

Sandy Baum is a nonresident fellow in the Center on Education Data and Policy at the Urban Institute and professor emerita of economics at Skidmore College. An expert on higher education finance, she speaks and writes extensively about issues relating to college access, college pricing, student aid policy, student debt, and affordability. Baum earned her BA in sociology from Bryn Mawr College, where she serves on the board of trustees, and earned her PhD in economics from Columbia University.

Michael McPherson was the fifth president of the Spencer Foundation and is a nonresident fellow in the Center on Education Data and Policy. He is a nationally known economist whose expertise focuses on the interplay between education and economics. McPherson holds a BA in mathematics, an MA in economics, and a PhD in economics from the University of Chicago.

Acknowledgments

This brief was funded by the Bill & Melinda Gates Foundation. We are grateful to them and to all our funders, who make it possible for Urban to advance its mission.

The views expressed are those of the authors and should not be attributed to the Urban Institute, its trustees, or its funders. Funders do not determine research findings or the insights and recommendations of Urban experts. Further information on the Urban Institute's funding principles is available at urban.org/fundingprinciples.

500 L'Enfant Plaza SW
Washington, DC 20024

www.urban.org

ABOUT THE URBAN INSTITUTE

The nonprofit Urban Institute is a leading research organization dedicated to developing evidence-based insights that improve people's lives and strengthen communities. For 50 years, Urban has been the trusted source for rigorous analysis of complex social and economic issues; strategic advice to policymakers, philanthropists, and practitioners; and new, promising ideas that expand opportunities for all. Our work inspires effective decisions that advance fairness and enhance the well-being of people and places.