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## The Evolution of State Higher Education Public Funding Policy

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## **Abstract**

In the past several decades, public colleges and universities have increasingly struggled to fund all of the programs demanded of them as states slowly drain funding from their coffers. This discussion will examine different policies and frameworks that have been used by states to determine funding for their public institutions. Different factors that will be considered include political relationships, governance structures, and accountability models. The political trend of “free college” will also be considered. Then, the discussion will narrow to South Carolina funding policy, how it has changed over the years, and what the current challenges are. A policy proposal for South Carolina will conclude the argument.

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## **The Evolution of State Higher Education Public Funding Policy**

In roughly the past fifty years, higher education has gone from being an optional luxury to a mandatory stepping stone. Supply and demand for higher education institutions has exploded. The number of students enrolled in a college or university increased by roughly 240% between 1965 and 2016 (Statista, 2018). The rate of increase is still significant. Just between 2000 and 2016, enrollment increased by 28% (National Center for Education Statistics (NCES), 2018). Funding colleges and universities went from a B-list policy issue to one of massive importance. However, despite the rapidly growing demand, investment in higher education has gone down consistently since 1980 (Mortenson, 2012). State funding has decreased on average by 40.2% between 1980 and 2011. While two states (Wyoming and North Dakota) have increased or maintained their portion of funding, the remaining forty-eight states have cut their funding by 14.8 to 69.4%. South Carolina specifically has decreased its investment by 66.8% during that time period. If we project a continuation of this trend, higher education nationwide will be privatized (i.e. have no public funding) by 2059. South Carolina will hit zero public funding in 2031 (Mortenson, 2012).

As a college degree becomes more and more expected for young professionals, demand has become more inelastic. Students (and their families) are more willing to pay whatever it takes to get a college education. The combination of increased inelastic demand, evaporating state support, and demand for more services, among other factors, has led schools to increase tuition. Since 1980, tuition has increased by 247% at flagship universities, 230% at state universities, and 164% at community colleges (Moretenson, 2012). Private schools too have seen a stark increase. Since 1988, tuition has increased 129% at the average private nonprofit institution (Martin, 2017).

Additionally, schools have an incentive to enroll fewer low-income students and focus their efforts on recruiting students who can afford higher tuition. State schools desire non-resident students because out-of-state tuition is usually two to three times more than what state residents pay (Mortenson, 2012). The cost burden has effectively been transferred from the state to the individual. In 1975, local and state funding covered 60.3% of all the money spent on higher education. By 2010, that proportion decreased to 34.1%. The leftover portions have to be covered by students in the form of tuition and the federal government in the form of grants (Mortenson, 2012).

In the past several political cycles, divergent policy positions have been thrown around. Should all public institutions be free or heavily subsidized? Should states offer scholarships to students or give money directly to universities? Should the current funding trend continue until all schools are privatized? The arguments in response to these questions change dramatically depending on party, state, and structure.

This discussion will provide an understanding of where higher education funding policy has been, where it is now, and where it may be going. It will examine different funding models and types of state appropriations. It will begin with a broader focus of the nation and then narrow down to look specifically at South Carolina. The discussion will conclude with a policy proposal for South Carolina and suggestions of how the state can sustainably continue to provide public higher education in an affordable, equitable way.

### **Part 1: A Historical View of Higher Education Funding**

As discussed, the cost of higher education has increased exponentially. In fact, the expense of higher education has consistently grown faster than both income levels and the national cost of living. From 1875 to 1930, the cost increase was because of investment; as higher education became more accessible to the masses, supply had to grow to keep up. New

schools were founded, and existing schools expanded to try to meet the demand (Kimball & Luke, 2018). However, after 1930 the cost continued to grow even though demand had started to level out. There are two predominant theories for why this was.

The first model is the Revenue Theory of Cost. Basically, this argument is that operation costs were set by how much money the school was able to raise rather than by actual need. This begins a vicious cycle. Costs increase because more money can be feasibly raised, but in the future more money must be raised because costs have increased. Once this cycle begins it's almost impossible to reverse (Kimball & Luke, 2018).

The second model is the Cost Disease Theory. In the past 200 years, the goods-producing industries have seen massive increases in productivity. The introduction of new technologies and manufacturing practices have meant that more goods can be produced with fewer man hours, thus decreasing production costs. Personal services like education, however, have not seen the same productivity increase. For the most part, teaching an introductory math class requires the same number of teacher hours now as it did a century ago. While technology is just starting to change the education landscape, the industry just has not seen the same efficiency improvements that goods producing industries did. However, even with productivity stagnant, compensation still has to stay on pace across industries, so production cost in personal industries continues to increase (Kimball & Luke, 2018).

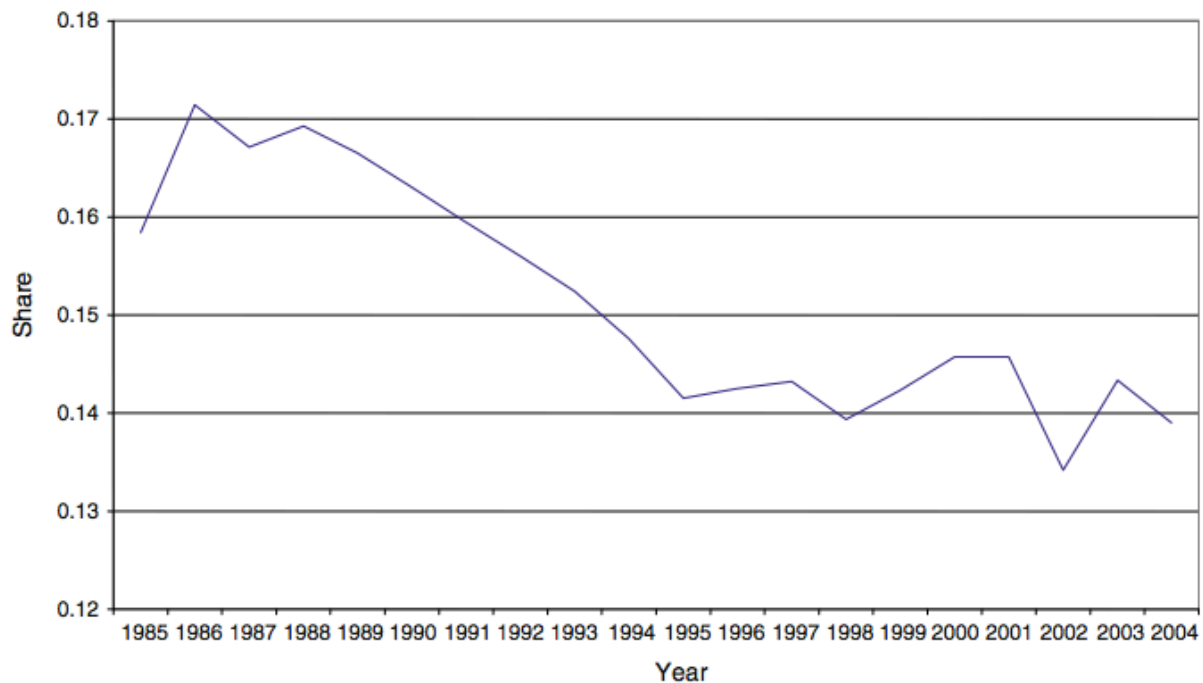
So now we have some idea of why costs may have increased so rapidly, but what made states divest during that time? In the past several decades we have seen the most aggressive changes in how states fund higher education. The average funding per student has dropped more than 30% in the past 30 years. This decrease must be made up for in increases in tuition and decreases in spending. Research says that the pass-through rate is roughly 25.7%. This means that for every \$1,000 reduction in appropriations, the average student will pay \$257 more per

year. The rate has fluctuated between 18.3 to 26.6% but has increased over time (Webber, 2017). Tuition increases have barely offset the long-run decline in appropriations per full time equivalent student (FTE). State funding per FTE peaked in fiscal year (FY) 1987 at \$7,993 but has fallen to an average of \$6,454 in 2010. The sum of net tuition revenue and appropriations per FTE was roughly the same in that same time period, meaning tuition went up the same amount as appropriations went down (Ehrenberg, 2012). Of course, this increase in tuition means that many students will require more aid. In 2010, states spent \$242.50 per resident for higher education operating expenses, \$29.60 per resident for grants, and \$28.10 per resident for need-based aid (Lowry, 2016).

Unsurprisingly, state funding took the biggest hit during the 2008 recession. As states needed to spend more on safety net programs, education budgets took a hit (Tandberg, 2010). However, states did not fully reinvest in higher education once the economy rebalanced. Public divestment led to massing increases in tuition and cuts in services (Webber, 2017). State dollars per FTE fell 23% between 2007-2012 and net tuition increased 19% around the same time (Kimball, 2014). The cost burden once again shifted more from the state to the student.

In fact, higher education is often the first state budget to be slashed during economic hardships or periods of shifting priorities because institutions are usually able to make up the difference with tuition increases, endowment, more out-of-state students, and deferred maintenance (Tandberg, 2010; Kimball, 2014). Indeed, higher education can serve to balance the state budget in times of need. According to the National Association of State Budget Officers, "...in fiscal 1995, higher education comprised 12.9 percent of general fund spending, while in fiscal 2018, higher education made up an estimated 9.7 percent of general fund expenditures. Over that same period, Medicaid went from representing 14.4 percent of general fund spending to 20.2 percent," (NASBO, 2018). The state can pump more money into

education during economic upswings (and enjoy the political benefit) and make deep cuts when the money is required elsewhere. In fact, economic conditions are the best predictor of budget cuts regardless of other factors like political environment and governance structure (Kimball, 2014).



(Figure 1. Graph depicting the decrease in higher education funding as a share of total state spending. Adapted from “Politics, Interest Groups and State Funding of Public Higher Education” by D.A. Tandberg, 2010, *Research in Higher Education*, 51(5), p. 416. Copyright 2010 by Springer Science + Business Media, LLC.)

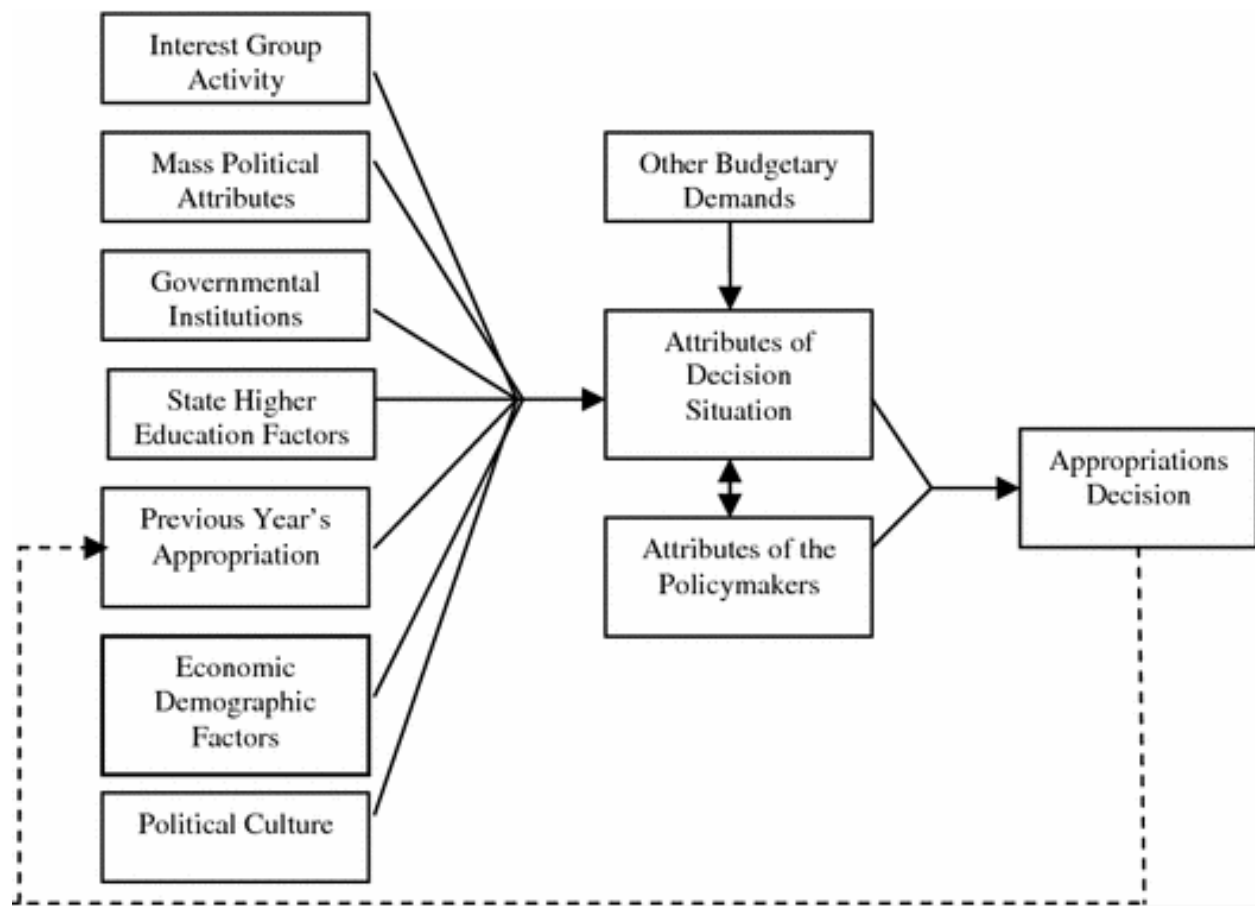
## Part 2: Approaches and Models of Higher Education Funding

### Section A: The Tandberg Fiscal Policy Framework

In this section, we will examine a variety of different models that have been researched and tried in different contexts. The first is the Tandberg Fiscal Policy Framework. This model argues that political actors are motivated by self-interest but impacted by their environment. Attributes that affect the environment include interest groups, political factors, government



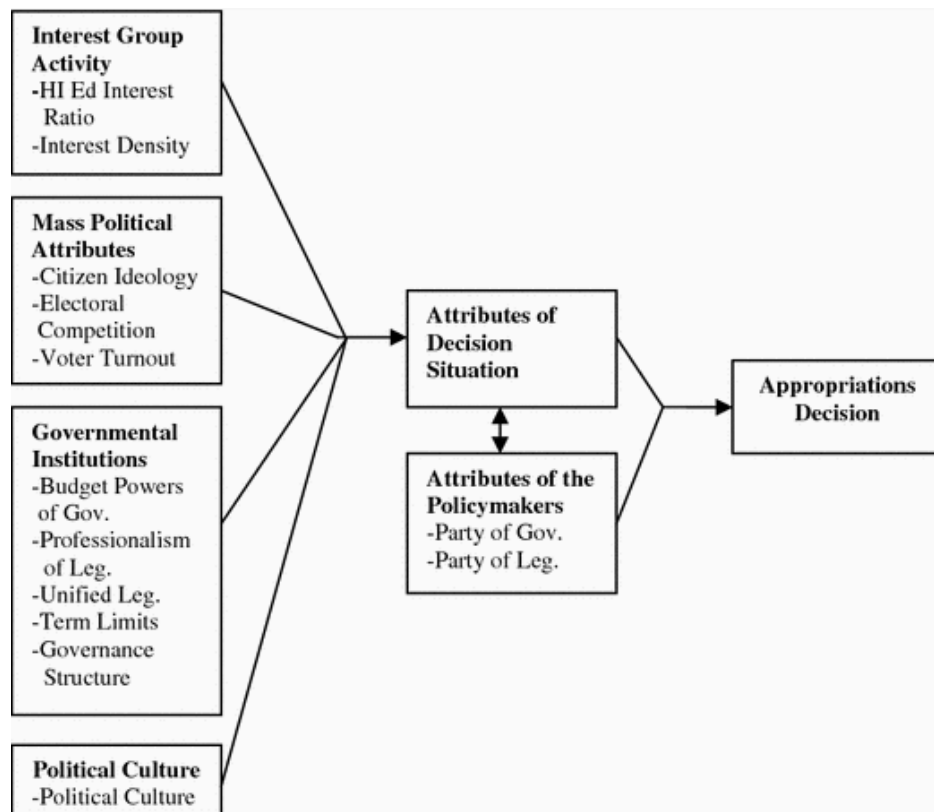
institutions, state higher education priorities, economic demographics, political culture, and budgetary demands (Tandberg, 2010). Let us examine several of these individual factors.



(Figure 2. Tandberg's Fiscal Policy Framework. Adapted from "Politics, Interest Groups and State Funding of Public Higher Education" by D.A. Tandberg, 2010, *Research in Higher Education*, 51(5), p. 416. Copyright 2009 by SAGE Publications.)

Interest groups can have a very powerful impact on state policy outcomes and spending priorities. These groups are most successful when there are only a handful in the area but are concentrated around a particular policy area and have significant economic power. It's important to note that higher education institutions themselves act as interest groups. Most (if not all) have teams that engage in lobbying to compete for limited dollars (Tandberg, 2010).

Economic and demographic makeup are also big motivating factors. States with younger populations tend to fund higher education more fully. Additionally, Democrats tend to look much more favorably upon higher education than Republicans—56% of liberals are confident in U.S. colleges while only 33% of Republicans are (Pew Research Center, 2017). Also, when a large portion of the population is below the Pell grant level of income, states fund higher education less because it doesn't have the tax base to support it and education largely goes to benefit the rich anyway (Tandberg, 2010). As expected (and demonstrated in the Great Recession), support is also decreased in times of economic stress and higher unemployment (Tandberg, 2010).



(Figure 3. Fiscal policy framework variables. Adapted from “Politics, Interest Groups and State Funding of Public Higher Education” by D.A. Tandberg, 2010, *Research in Higher Education*, 51(5), p. 416. Copyright 2009 by SAGE Publications.)

Interestingly, the makeup of the legislature (beyond political party) also plays a part. Legislative professionalism (i.e. to what extent the state legislature is like Congress in terms of staffing, compensation, time in session, etc.) is correlated with policy innovation and greater general spending. Unsurprisingly, when legislatures are campaigning in more competitive races, they tend to support positions that will help the widest range of constituents, which is in line with the Median Voter Theorem (Toutkoushian & Hollis, 2006). Also, districts that have a greater voter turnout elect more responsive representatives and they tend to support higher education funding (Tandberg, 2010).

#### *Section B: Political Relationships*

The focus of other funding models is how political relationships drive spending outcomes. The relationship between the State Higher Education Executive Officer (SHEEO) and the governor directly influences the amount of state support to the higher education system in general. (For SC, the SHEEO is currently Michael LeFever, the interim President and Executive Director of the Commission for Higher Education.) In most states, the SHEEO plays the role of policy advisor. He or she recommends resource allocation, oversees regulations, awards grants, and is accountable for the performance of public institutions. In comparison, the governor has tremendous influence regarding the budget (Tandberg, Fowles & McLendon, 2017). The SHEEO (along with every other department head, institution, and person impacted by the budget) attempts to influence the governor to look upon his or her agency generously. The notable issue, however, is that the SHEEO (and many other important executives) is appointed by the governor and is subject to termination by the governor as well. This incentivizes the SHEEO to find personal favor with the governor to protect his or her job and policy concentrations. This leaves room for conflicts of interest and other relationship concerns that

likely will not lead to the most equitable or accountable distribution of funds (Tandberg, Fowles & McLendon, 2017).

### *Section C: Governance Structure*

Another theory says the type of education governance structure can make a big difference in the way states manage their public institutions. Each state has some sort of higher education board involved in organizing public institutions and setting policy within those schools. Board members can be appointed, elected, or some mix of both. South Carolina board members are appointed by the legislature (Mann, 2017). Typically, there are three different structures that can yield different results (Knott & Payne, 2003). The first is a centralized board that usually favors strong regulation, low tuition, and broad access. In 2003, 75% of students enrolled in public education were a part of a multi-campus or consolidated governance system under a single board. Governors tend to favor this structure because it makes it easier to coordinate across functions to satisfy a broad constituency. In contrast, legislators tend to prefer a decentralized board with individual university managers focused on research, publication, and external grants. This fragmented management structure separates control so that legislators can try to cater to narrower constituencies and special interest groups. Experts and education professionals tend to prefer decentralization as well, as it gives them the most control. Additionally, there tend to be more resources and a higher level of productivity associated with this type of system. The final structure is a hybrid of the two. This allows more focus on low tuition and larger undergraduate population than decentralized systems and more emphasis on research and grants than centralized structures (Knott & Payne, 2003).

### *Section D: Accountability Models*

By far the most prevalent funding model used by states is the accountability or performance funding model. Driven by wasteful spending and corruption, current politics

demand that politicians and agencies be accountable for every dollar of taxpayer money that they spend. Additionally, performance-based funding makes it much easier for political leaders and the public to evaluate agencies. In theory, this makes budgeting less political and more merit based (Kimball, 2014). However, decisions are not made in political vacuums and performance metrics are rarely used in a neutral way. Agencies are able to manipulate their data in the short term to protect their interests. There is incentive to game the system. Even if metrics were completely reliable, it's unclear if poor performance should lead to more or less funding (Kimball, 2014).

There are three main types of accountability policies. The first is performance reporting; the government will collect data, but they will not be used to influence the budget. Performance budgeting takes it a step further. Data are considered when developing the budget, but there is no formal benchmark or requirement. Finally, performance funding is the most extreme. In this case, some percentage of funding is linked directly to performance (Kimball, 2014).

There are several issues associated with performance funding. The first is the most crucial: it's not effective. Different states use different metrics—graduation rate, retention rate, degree production, undergraduate population, student diversity—but research has shown that none of those metrics improve when you base the budget on them. Furthermore, legislators still privilege institutions to which they have close personal ties, so the idea that performance funding removes political bias is debunked. Overall, institutions become more concerned with overcoming political bias than improving their metrics (Kimball, 2014).

One major unintended consequence of performance funding models is equity for minority serving institutions (MSIs). MSIs enroll about 25% of all college students but about 75% of minority students and students who attend are generally less affluent. They produce similar results to non-MSIs in terms of degree completion. Between 2005 and 2015, twenty-one states

adopted or redesigned some version of performance-based funding. They rewarded the number of degrees awarded, the number of transfer students, retention rates, course completion, job placement, and research funding. In other words, they paid for outputs rather than inputs. These requirements were standardized across institution types but MSIs were disproportionately affected. The average MSI lost \$750 per FTE when compared to other schools. They responded by decreasing student to faculty ratios and other support and raising tuition (Hillman & Corral, 2017). While these outcomes were certainly not intended, they give just one example of how biased and ineffective these models can be.

Looking across all kinds of schools in all states, however, the overall differences in spending based on funding are smaller because the majority of states have divested in higher education and schools have had to rely more on private funding (Kimball, 2014). Indeed, there has been a major trend towards privatization or diversification of funding. If nationwide trends seen since 1980 continue, higher education will be completely privatized by 2059 (Mortenson, 2012). This trend has been seen in two ways: through a direct increase in private funds and a decreased reliance on public revenue and appropriations. Some schools have tried to decrease reliance on public funds because of the amount of regulation and hoop jumping that comes with the money (Kwiek, 2017). Some schools have supplemented their income with the pursuit of economic activity in the form of contract research and more additional fees for activities (Stachowiak-Kudla & Kudla, 2017). Regardless of how they do it, without education funding reform, universities will be forced to find other ways to fund themselves in the very near future.

### **Part 3: “Free College”**

A recent buzzword in education politics is “free college”. While this idea was relevant in some states prior to 2016, a potential Democratic presidential nominee, Bernie Sanders, made free college one of his major policy points during his campaign. Most politicians have

disregarded the idea as too expensive and unobtainable, but some states have tried out programs to assist students with the cost of higher education.

States have three ways they can attempt to make college education more attainable: they can find ways to make school more affordable; they can make it possible to transition across institutions without loss of credits; or they can make higher-quality education available for more residents (Perna, Leigh & Carroll, 2017). Indeed, over a dozen states now offer grants to pay for all or some of college in some way (Turner, 2018). Legislators have to choose between boosting appropriations, grants, or financial aid. More professional legislatures have more grants and financial aid. The number of grants offered decreases as the number of governing boards increases (as discussed in the previous model) but financial aid does not (Lowry, 2016). Overall, most assistance comes in the form of grants. In FY 2014-15, 20% of all higher education funding was in the form of direct grants to students on the basis of merit, need, or both (Perna, Leigh & Carroll, 2017). To see what different states have tried, let's take a look at some of the different programs that have been implemented.

The first is the Tennessee Promise. This program covers tuition and fees for community or technical colleges for Tennessee residents who graduated from in-state high schools. In general, Tennessee is notably favorable towards state sponsored aid programs and they have sixteen other scholarships, grants, and aid options (Perna, Leigh & Carroll, 2017.).

A similar option is the Oregon Promise, which offers tuition for up to ninety credits (about three years full time) of community college for Oregon high school graduates. A prior version of the program had a higher level of emphasis on need-based aid (Perna, Leigh & Carroll, 2017). However, in the first year of the new program, less than half of the participants were needy enough to qualify for a Pell Grant (Turner, 2018).

One of the handful of programs that includes four-year schools is the New York Excelsior Scholarship. Recipients are eligible for up to \$5,500 per year for full time tuition at two- or four-year public colleges or universities. While it is not purely need-based, that factor is taken into consideration. New York, like Tennessee, is very generous with its aid programs and it has twenty other programs, most of them need-based (Perna, Leigh & Carroll, 2017).

The oldest program by far is the 21<sup>st</sup> Century Scholars Program in Indiana, which is nearly thirty years old. The program covers tuition for a two- or four-year degree at a public *or private* school. Students may be eligible for additional funding to cover cost of living. Middle school students who qualify for free or reduced lunch can apply for this program as early as seventh grade. If they meet a series of requirements over the course of high school, including keeping a B grade average, then they will qualify for the program when they graduate (Turner, 2018).

As expected, it is impossible to fund these programs indefinitely (Perna, Leigh & Carroll, 2017). In fact, Indiana's 21<sup>st</sup> Century Scholars Program costs a remarkable \$160 million per year (Turner, 2018). Less generous programs obviously cost less, but it is challenging for legislators to justify extremely expensive projects that won't impact broad swaths of their constituency and won't see results for several years.

The Education Trust recently reviewed fifteen statewide programs to determine if they met certain criteria focused on increasing educational equity. The criteria are whether the program funds four years of tuition for a bachelor's degree; assistance in cost of living; inclusion of adult, non-traditional, and part-time students; no GPA requirement above a 2.0; and that funds do not convert to a loan if criteria are not met. This study on "free college" programs found "that states vary wildly in how they define both 'free' and 'college'," and none met all of the criteria they were seeking (Turner, 2018).

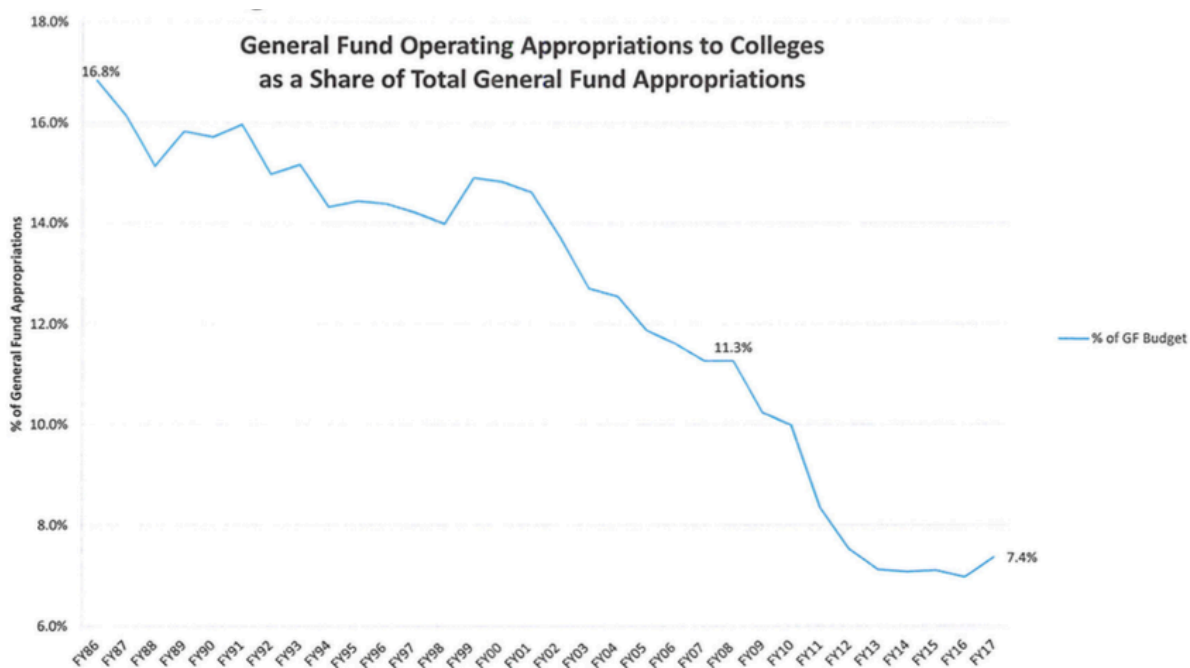


State	Living costs for low-income students	Fees for all recipients	At least 4 years of college	Tuition at 4-year colleges	Adult and returning students	Students with a 2.0 GPA	Students enrolling half time	Stays a grant forever
<b>California</b> (California College Promise Grant*)	Yes	No	No	No	No	Yes	No	Yes
<b>Delaware</b> (SEED Scholarship)	No	No	No	No	No	No	No	Yes
<b>Hawaii</b> (Hawaii Promise Scholarship)	No	Yes	Yes	No	Yes	Yes	Yes	Yes
<b>Indiana</b> (21st Century Scholars)	Yes	Yes	Yes	Yes	No	Yes	No	Yes
<b>Louisiana</b> (TOPS Opportunity Award)	Yes	No	Yes	Yes	No	No	No	Yes
<b>Maryland</b> (Guaranteed Access Grant)	Yes	Yes	Yes	Yes	No	Yes	No	Yes
<b>Missouri</b> (A+ Scholarship)	No	Yes	No	No	No	No	No	Yes
<b>Montana</b> (Montana Promise*)	No	No	No	No	Yes	No	Yes	Yes
<b>Nevada</b> (Nevada Promise Scholarship)	No	Yes	No	No	No	Yes	No	Yes
<b>New York</b> (Excelsior Scholarship)	No	No	Yes	Yes	No	Yes	No	No
<b>Oklahoma</b> (Oklahoma's Promise)	Yes	No	Yes	Yes	No	Yes	Yes	Yes
<b>Oregon</b> (Oregon Promise Grant)	No	No	No	No	No	Yes	Yes	Yes
<b>Rhode Island</b> (Rhode Island Promise Scholarship)	No	Yes	No	No	No	No	No	Yes
<b>Tennessee</b> (Tennessee Promise Scholarship, Tennessee Reconnect Grant)	No	Yes	No	No	Yes	Yes	No	Yes
<b>Washington</b> (College Bound Scholarship)	Yes	Yes	Yes	Yes	No	Yes	Yes	Yes

(Figure 4. The Education Trust's variables and evaluation of various college assistance programs. Adapted from "If 'Free College' Sounds Too Good To Be True, That's Because It Often Is" in *National Public Radio*, by C. Turner, 2018, Retrieved November 12, 2018 from [https://www.npr.org/sections/ed/2018/09/12/643673271/if-free-college-sounds-too-good-to-be-true-that-s-because-it-often-is?utm\\_source=npr\\_newsletter&utm\\_medium=email&utm\\_content=20180916&utm\\_campaign=ed&utm\\_term=nprnews](https://www.npr.org/sections/ed/2018/09/12/643673271/if-free-college-sounds-too-good-to-be-true-that-s-because-it-often-is?utm_source=npr_newsletter&utm_medium=email&utm_content=20180916&utm_campaign=ed&utm_term=nprnews). Copyright 2018 by National Public Radio.)

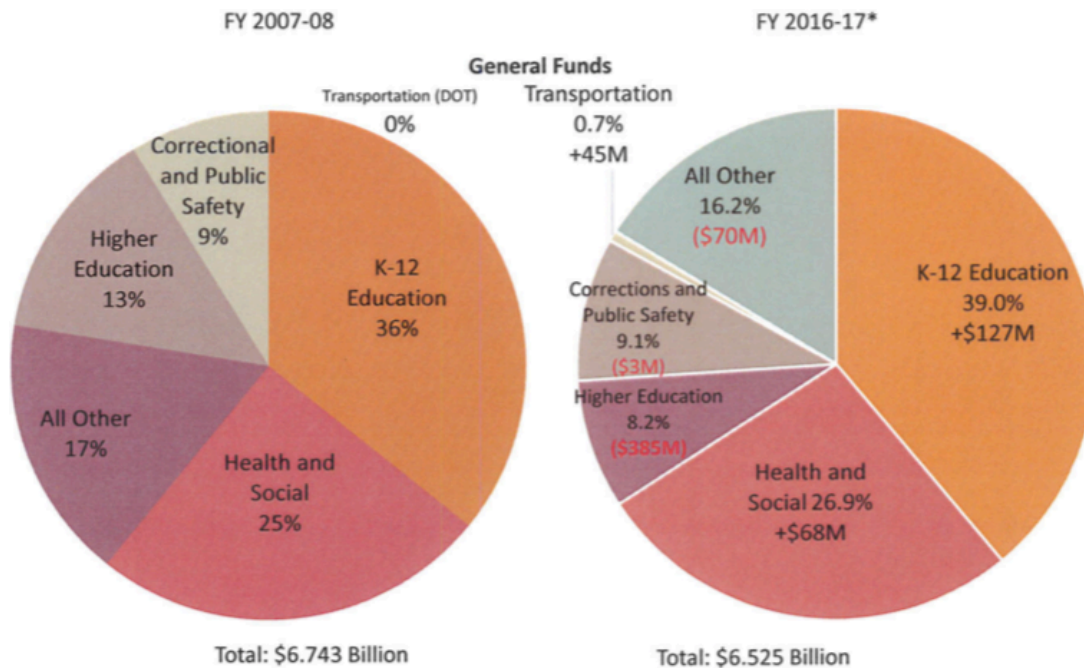
#### Part 4: South Carolina, A Case Study

Similar to most southern states, South Carolina faces problems related to the financing and prioritization of higher education. There are multiple issues that contribute to these challenges. The first is the steep decrease in state appropriations. According to the state Commission for Higher Education (CHE), state funding for higher education in fiscal year 2015-2016 was 35% lower than before the recession in 2007-2008, which is approximately the same level of funding as in the 1980s, not considering inflation or enrollment growth (Glenn & Armour, 2016). That's a decrease of \$267 million. The number of dollars spent per pupil has also been cut by over half, from \$5,581 in 1981-1982 to \$2,507 in 2016-2017 *after* inflation adjustments (Parks, 2017).



(Figure 5. General fund appropriations decreasing over time. Adapted from SC Finance Committee by C. Parks. March 2017.)

Clearly, a significant amount of money has been reallocated, but to where? Just looking at how the percentages have changed over the past ten years, most pieces have fluctuated within about a percent, while K-12 education has increased 3%, or \$127 million (Parks, 2017).



(Figure 6. General fund appropriations sector breakdown. Adapted from SC Finance Committee by C. Parks. March 2017.)

A couple years ago, I interviewed Craig Parks, formerly a Senior Research Analyst for the Senate Finance Committee specializing in higher education funding and currently the Director of Governmental Affairs for the University of South Carolina. When asked why more money was being allocated to K-12 funding, he said, “It’s largely because of tax policy. South Carolina prides itself in being a low tax state, and we won’t raise taxes just to help a small segment of the population trying to go to college. The way some see it, higher education is a privilege, while K-12 education is seen as a constitutional right. Scarce dollars need to go towards constitutional rights first,” (Parks, 2017).

What does this decrease in funding do to tuition rates? While tuition has been rising for decades, state tuitions rates have increased particularly sharply in the past ten years. In-state and out-of-state tuition for four-year South Carolina universities has gone up roughly 50% since 2007-2008, from \$7,887 to \$11,525 and from \$16,957 to \$25,425 respectively (Glenn & Armour, 2016). Comparing South Carolina to the rest of the nation is equally disheartening. While the average tuition for in-state universities in 2013-2014 was \$7,500 for the nation, South Carolina's average was almost at the very top of the list at \$10,100, a remarkable 35% more (Park, 2017). Future projections of average nationwide college-costs are even more disheartening. Kal Chany, the author of *How to Pay for College Without Going Broke*, did some calculations based on the current national trends and inflation rates, and he found that the average cost of an in-state education would likely cost over \$40,000 *per year* in 2030 (Landsman, 2012).

#### Projected Tuition Costs Fall 2029- Spring 2030\*

School type↕	5 % increases↕	6 % increases↕	7 % increases↕
4-year public (out of state)	\$71,373	\$84,651	\$100,239
4-year private (non-profit)	\$92,869	\$110,146	\$130,428
4-year public in-state	\$41,228	\$48,898	\$57,609

Source: Campus Consultants Inc \* Includes room and board

(Figure 7. Projected tuition increases for different institution types. Adapted from

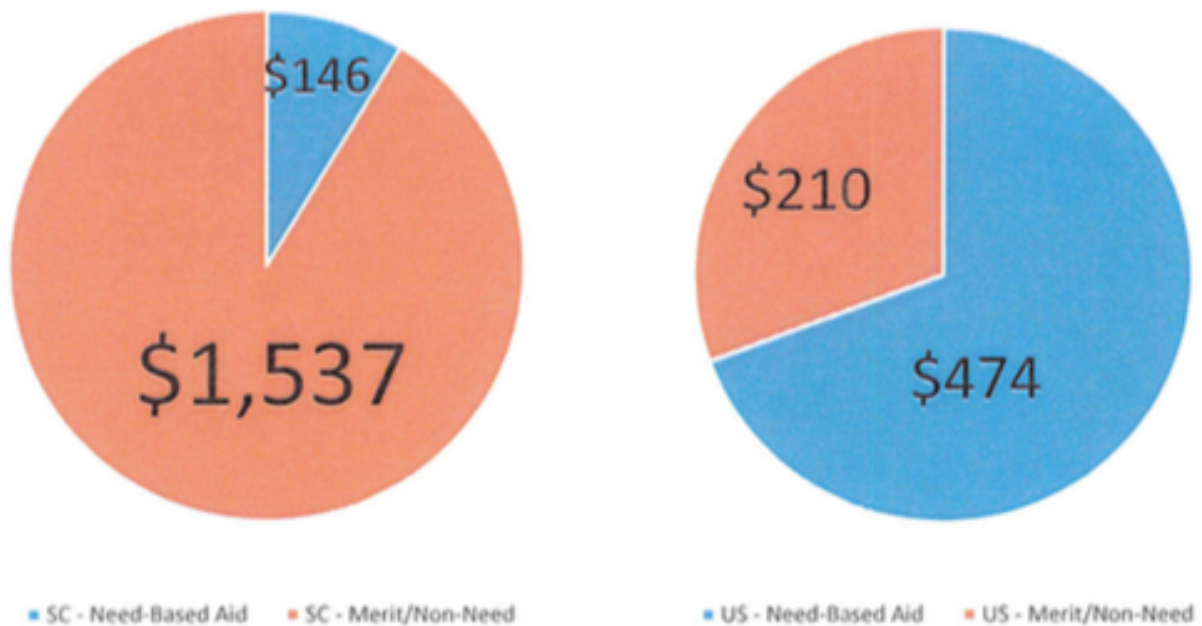
CNBC, by S. Landsman. Retrieved 19 November, 2018 from

<https://www.cnbc.com/id/47565202>. Copyright 2018 by CNBC LLC.)

It doesn't make sense that at 35% decrease in state allocations should lead to a 50% increase in tuition. So where did the extra dollars go? The disparity comes from a change in *how* the state dollars are being spent. In the past thirty years, the funding trend has moved away

from direct support of institutions towards scholarship funding. Whereas the state used to give each school a certain amount of money to fund operations, maintenance, salaries, scholarships and more, South Carolina now puts more dollars into funding merit scholarships, like the Palmetto Fellows, LIFE, and HOPE scholarships. Mr. Parks describes this as the free market approach. Students earn scholarships based on their GPA and standardized test scores and they can take that money to whichever school they choose, public or private. However, this means that state schools get fewer dollars than they were getting before (since some of those scholarship winners are going to private schools), and thus must raise tuition to be able to pay their professors and maintain their buildings (Parks, 2017).

From FY 2000 to 2016, there was a more than 23% drop in funding for operational costs and a 453% increase in scholarship and grant funding, about three quarters of which went towards Palmetto Fellows, LIFE, and HOPE (Parks, 2017). Since 2000, funding for merit awards has increased 12% a year, while need-based funding has increased only 4% per year (Parks, 2017). Additionally, the average merit award covers a bit over a third of in-state tuition while need-based awards cover just over a tenth (Parks, 2017). Finally, the three merit awards benefit majority white students; anywhere from 51% to 85% of recipients are white as of 2015 (Parks, 2017). The need-based funding is closer to 50% white, 50% non-white students (“Summary Report”, 2006). The figure below clearly shows the increase in scholarship funding disproportionately supports high-achieving students in a proportion much higher than the rest of the state and nation (Parks, 2017).

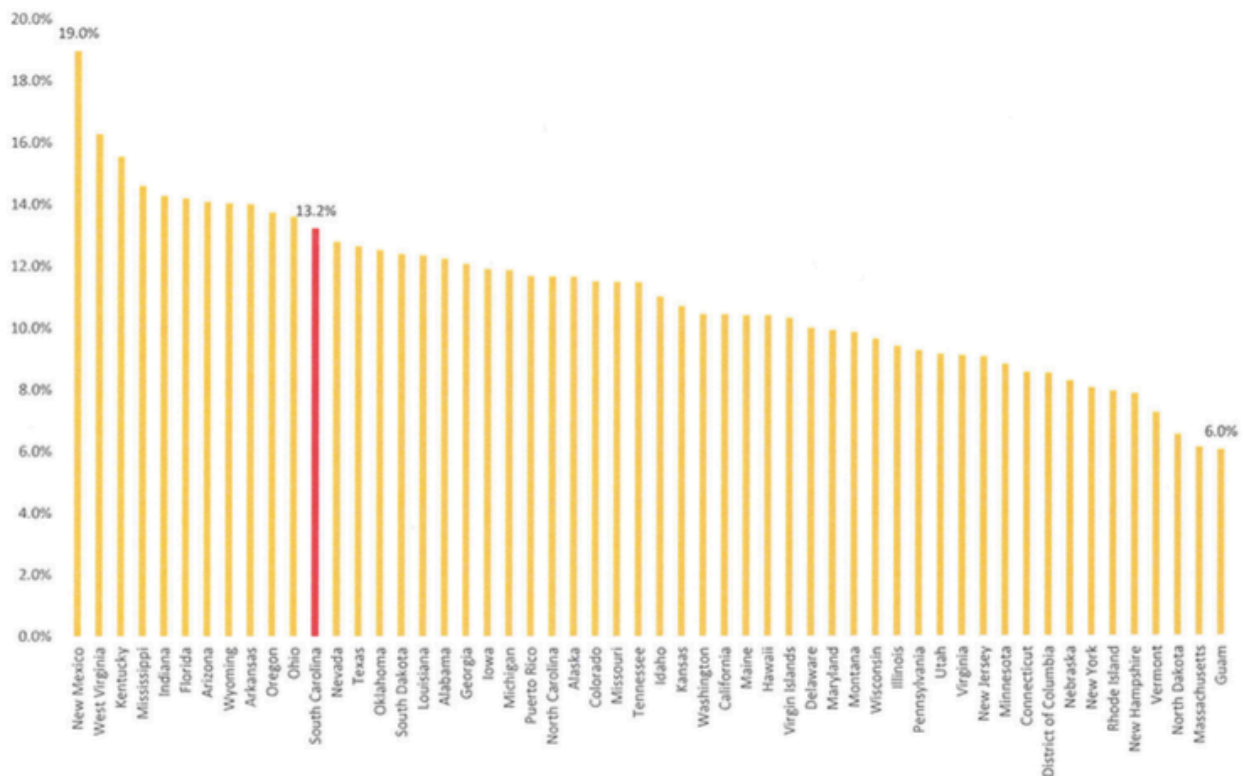


(Figure 8. Need and merit based aid in SC compared to US. Adapted from SC Finance Committee by C. Parks. March 2017.)

In order to try to benefit more students, the Department of Education changed the K-12 grading scale from a seven-point scale to a ten-point scale for all public schools so that more students would qualify for the state merit scholarships. Roughly 12,000 more students, out of 160,000 in the state, became eligible, costing about \$88 million over four years. While it is positive that more students are getting aid to go to school, it is questionable whether that \$88 million dollars should go to benefit only 7.5% of the student population (Parks, 2017). Additionally, this is only a patch solution. Grade schools cannot keep changing the grading scale to benefit more students financially; ultimately, there will always be a majority who are disadvantaged by this shift in the system.

Since scholarship money is scarce, and tuition rates have increased, and students are forced to take out more debt in order to get an education. This is a particularly pertinent problem in South Carolina. As higher education has become more of a necessity in the working world, an increasing number of students who perhaps would not normally have gone to a four-year

institution feel obligated to get a bachelor's degree. These students are the ones most impacted by the debt brought on by high tuition rates, as many of them do not qualify for merit funding. Even for the students who do qualify for merit aid, the HOPE scholarship has a value of \$2800 total, the LIFE is \$5,000 per year, and the Palmetto Fellowship is \$6,700-7,500 per year. Need-based aid is maxed out at \$2,500 per year. These funds are helpful but cover a third to a half (at most) of in-state tuition, which means that students still need to take out debt (Glenn & Armour, 2016). In 2013, the average American student took out \$20,980 in debt if they attended a research university, and \$10,906 if they attended a four-year non-research university. In South Carolina, that same student would take out \$25,559 or \$13,629, respectively. This is 22-25% higher than the national averages. Additionally, South Carolina's loan default rate was in the highest third of the nation (Parks, 2017).



(Figure 9. Risk of loan default by state. Adapted from SC Finance Committee by C.

Parks. March 2017.)

This leaves countless students paying for their degree for decades to come, which was not a common problem only a generation ago.

When the education lottery was started in 2002, it was designed to be a supplement to funding already in place supporting K-12 and higher education. There was a specific promise made that money generated by the lottery would not replace current funding. This means that lawmakers would not reallocate current education funding with the expectation that the lottery would just fill the gap. However, the Legislative Audit Counsel recently released a report showing that over the course of the lottery's lifetime, \$2.1 billion has been replaced (Daprice, 2018). According to Wes Hickman, South Carolina spokesman, "The only way to help us freeze tuition or slow tuition growth is through increased funding to the higher institutions that pay for operational expenditures. In fact, the [audit] makes that exact point. The authorizing legislation for the lottery says that funds must supplement, not supplant, the funding levels for higher education that existed at the time. However, as we've been saying for years and the [audit] concludes, that's exactly what has happened" (Daprice, 2018).

The Attorney General says that the legislature is allowed to contradict a state statute when allocating taxpayer money, however. The money that has been marked for education must be spent on education, but what exactly is included in that is flexible. Lottery money has thus been divided between funding merit-based scholarships like the LIFE, HOPE, and Palmetto awards and basic needs like technology and textbooks that are supposed to be paid for through appropriations (Daprice, 2018).

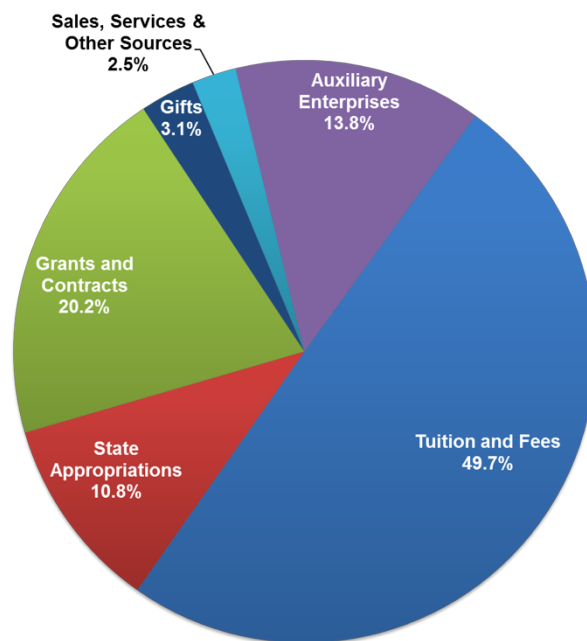
## **Part 5: Running the University of South Carolina's Budget: Interviews with Administrators**

On September 18, 2018, Leslie Brunelli, USC's Vice President for Finance and Chief Financial Officer, and aforementioned Craig Parks, formerly a SC Senate Senior Budget Analyst



and current Director of Government Relations for USC, sat down with me to discuss the practical challenges that they face in running the university on a daily basis. We discussed how funding policy has changed over their careers, the current attitudes towards higher education, and how they see the future being funded.

The University of South Carolina was never really a completely public university. At the recent height of state funding, the government provided 35-40% of the annual operating budget, whereas now that number is closer to 10-20% (10% of the total budget, 20% of the operating budget). The biggest hit, unsurprisingly, came from the recession, but the funding was never quite replaced.



(Figure 10. USC System Total Budget Breakdown. Adapted from USC Columbia Finance & Facilities Overview, September 2018.)

Actually, the total number of dollars being spent on higher education hasn't changed so dramatically, but they have shifted away from funding operations to funding scholarships. Brunelli thinks that scholarships are positive; they encourage faster graduation, they incite hard work, and they make education more attainable. The problem is that students can (and do) lose

scholarships. There is only a 72% retention rate for LIFE Scholarships from freshman to sophomore year. Scholarship retention requires a high GPA and other challenging requirements, and students can have a challenging time meeting those expectations, particularly in their first year out of high school. This means that students face stress regarding if they will be able to make their necessary tuition payments.

The previously outlined state funded scholarships (need and merit based) are available to students who go to private colleges as well. In fact, \$58 million goes to private institutions every year in the form of state funded scholarships. The fact of the matter is that private schools are expensive, and students qualify for much more need-based funding if they attend a private school even if their overall costs would be lower if they attended a public school.

According to Parks, the attitudes surrounding higher education in South Carolina (and the South in general) are unique. Higher education is seen as a transactional good (benefiting the individual), not a public good (benefiting the public at large). Thus, some think it should be paid for by the individual and not the state.

Furthermore, technical colleges are viewed more favorably because ideally graduates can go straight into a job ready and able to work. The problem with this idea, however, is that these graduates need to be retrained over time. Brunelli challenges the idea that four-year college graduates are not ready for the work force. She advocates for the idea that higher education teaches students how to learn, and they can then keep up with a changing job market that requires diverse skill sets.

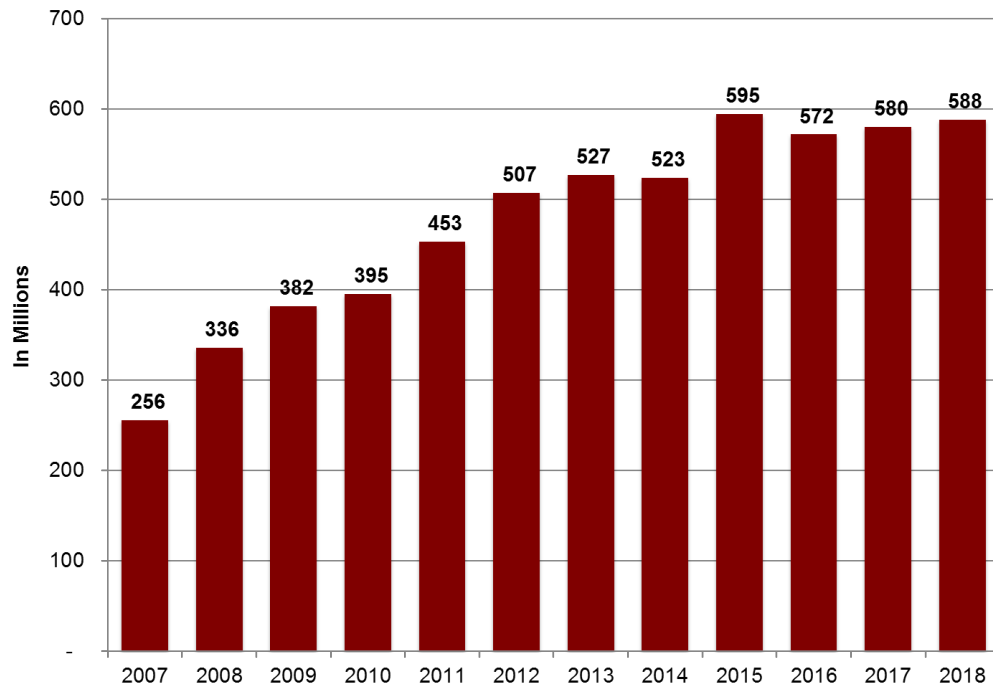
Having a well-trained, well-educated work force is a benefit for the whole community, not just the individual, but that's not the common perception of legislators. While the state is committed to maintain funding, it currently has no intentions to expand any programs and money

has actually been leaking from programs over time (see the discussion on the education lottery above).

Brunelli and her finance team struggle to do a lot with a little. Most programs are not deeply funded, and long-term issues are falling through the cracks. Some classes are large, professors are teaching more classes, there are fewer administrative staff, and buildings may not be properly maintained. South Carolina has not had a capital bond bill since the 1999-2000 fiscal year. Bond bills are loans that the state takes out on behalf of state or private entities. For example, South Carolina sometimes takes out bond bills to encourage large corporations like Boeing and BMW to build plants. These bills are relatively common for higher education nationwide, but not in South Carolina. In the past 50 years, South Carolina has taken out \$2.5 billion in bond bills over all sectors. North Carolina took out \$3 billion in one year for higher education alone.

Even though there is limited financial support for capital projects, there are still major rules and regulations the university must meet. This combination makes capital projects a major challenge. Any building project that costs more than \$1 million takes eighteen to twenty-four months to be approved by the state *after it has already gone through USC's rigorous approval process*. According to Brunelli, discussions surrounding the new law school started in 1999 and its doors just opened in 2017. Smaller projects, like the renovation of the old law school, are in the works four to five years before they open. This might be understandable if the state were undertaking the full cost, but the state is only contributing \$10 million of the project's \$80 million price tag. This means that the university must take on its own debt to fund projects. The total outstanding debt as of June 30, 2018 was \$587,695,000. A portion of this cost is directly reflected in tuition. Each resident student pays \$319 per year and each non-resident student pays \$815 per year to pay for this debt. This is not even the total amount of state institution bond

debt, only the amount serviced by tuition. The total number was \$144.4 million as of June 30, 2018.



(Figure 11. USC Ten Year Debt Total. Adapted from USC Columbia Finance & Facilities Overview, September 2018.)

The future of education funding is unclear. Because of the US Supreme Court decision *South Dakota v. Wayfair, Inc.*, ecommerce businesses are now required to collect online sales taxes. This creates \$100-200 million in unclaimed state revenue for South Carolina that higher education may be able to pull from. While this is certainly helpful, it doesn't make up everything that has been lost. Unfortunately, there doesn't seem to be another easy way to get additional revenue without raising taxes or taking revenue from another sector.

Brunelli predicts that the number of public schools in South Carolina will decrease. The state currently has thirty-three public college and universities, which is relatively high (the twenty-second most in the nation). While no one wants to decrease access to education, the

growing popularity of online education may help maintain access while condensing the density of schools in the state.

## **Part 6: Proposed Solutions for South Carolina**

Now that the problem has been fully articulated, what can be done? CHE estimates that spending must increase by over 30% in order to make up the difference between what colleges and universities need and what they are being offered currently (Glenn & Armour, 2016). Of the \$600 million extra that the General Assembly got to spend on the budget in FY 2017-2018, not a penny went towards higher education. In FY 2018-19, South Carolina decreased its funding by 3.7%, the most in the nation (Toppo, 2019). Therefore, it is unlikely to expect that significant and consistent increase in appropriations that is needed. What other options are there? There are four main routes that have been discussed.

The first solution that has been proposed creates a new bond bill. A bond bill allows the state to borrow money in order to pay for necessary maintenance for universities. This highly benefits the colleges, because they are not responsible for taking on that debt, but they still get the benefit of new or repaired buildings. Lawmakers like them because it still gives the state some control over how the money is used. These types of bills are common in most higher education systems, though, as previously discussed, South Carolina has not used them often. Nevertheless, there has been some discussion among lawmakers to create a new bond bill. This new bill would borrow \$1 billion dollars to pay back over fifteen years. This bond bill would likely slow the increase in tuition costs, since schools would have help in funding the cost of repairs. This solution would assist a great portion of students, but it is unviable in this form. It would force the state to take on a significant amount of debt, and once the money runs out, schools would be stuck in the same situation as before.

The second possibility is that the General Assembly could allocate nearly all of the current higher education budget towards making two-year technical schools free for those who qualify. Totally funding the existing twenty two-year technical schools in South Carolina would likely be cheaper in the short run than partially funding all thirty-three public universities as the state does currently (Glenn & Armour, 2016). However, as the program continued, it would undoubtedly grow exponentially. More students would opt for two-year degrees than the current campuses could support, and then the state would eventually end up in a situation similar to what is has now. While this would tremendously help a handful of students in the short run, students still seeking a four-year degree would be immensely disadvantaged, as tuition rates for universities would skyrocket even further to make up for the evaporation of state funding. In the end, the state would end up in a similar mess to what it faces now.

The third option is to do some major cost cutting. Some schools, such as the University of Wisconsin at Stevens Point, have chosen to remove some major programs and fire tenured professors to save money (Smith, 2019). The University of South Carolina could choose to do something similar or start to close smaller satellite campuses in an effort to centralize and focus on the most profitable degree programs. Unsurprisingly, this decision was wildly unpopular to University of Wisconsin students, and likely would be equally unpopular in South Carolina. One of the biggest risks would be that prospective out-of-state students would be driven away to universities with more major options and lower student to faculty ratios, which would hurt the bottom line even more.

The fourth and final solution is almost definite to occur at some point, particularly if no other significant action is taken immediately. In the long term, higher education will most likely become privatized. If current trends continue, South Carolina will offer no state funds to higher education by 2031, and schools will be forced to come up with 100% of their own costs

(Mortenson, 2012). Tuition will increase to private college levels or higher, and some combination of the following three things will have to happen: each student will have to take out a significant amount of debt; only the very wealthy will qualify for education; or universities will be forced to come up with tremendous cost-cutting measures. Many institutions will be unable to come up with enough students and donors to cover costs, and smaller schools will be forced to close. It is nearly impossible to know how the higher education system would function if it were privatized, but there is no doubt that it would look and operate very differently than it does now, and likely not for the better.

In my opinion, there is, however, a compromise that can help manage the problems that higher education is facing. My solution has two parts which work in tandem. The first part is in the form of a bond bill every three years. These bond bills would be in smaller amounts than the one currently suggested, but it would occur more frequently. The benefit of this would be to keep maintenance regular so that buildings would stay in good shape and require fewer big fixes. Making these bills a regular occurrence would also give universities confidence that they will have money to maintain their campuses, and thus can devote money to other programs that will benefit students or reign in the increases in tuition. Politically, it would be easier to pass bond bills for smaller amounts, and it would not necessarily be seen as a funding increase to higher education.

The second part would include a gradual shift back from scholarship funding to direct university support. State schools will get more direct allocations, which was the norm thirty years ago, which they can use for whatever programs they choose. Overall scholarship funding is unlikely to decrease, as some universities may choose to spend some of that extra money on merit and need-based scholarships. Schools and the state as a whole still have an incentive to recruit the most talented students, and so there will always be a place for scholarships and grants

based on merit. One potential political problem with this aspect is that universities may choose to award more scholarships to out-of-state students than to in-state, which would be unpopular to lawmakers and to the public. However, many out-of-state students are recruited partially because of the tuition money they bring with them. That factor may no longer play into scholarship decisions if universities have a more reliable funding source through direct appropriations. Even if the ratio of in-state to out-of-state students does become skewed, it is not unreasonable for the General Assembly to require a certain percentage of scholarship recipients be from South Carolina.

This two-pronged plan will increase the total higher education budget very minimally, if at all, so K-12 schools and the rest of the state programs will still be fully funded. Private schools will receive little to none of the benefits that they were previously getting from students bringing in HOPE/LIFE/Palmetto Fellows scholarships, and so they may be negatively impacted, but state schools will be getting their funding directly from the state once again and the middle man of the “free market” will be cut out. Tuition increases will slow, and all universities and colleges and students will benefit.

This funding problem was not developed overnight, and it will not be fixed overnight either. However, by leveling how and how many dollars are distributed to schools, all students will see a positive improvement, and each school will be able to better support itself. With consistent commitment to this new plan, higher education in South Carolina could possibly become a model for states nationwide to follow.



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