

UNDERSTANDING HIGHER EDUCATION FINANCE

INTERVIEW WITH PHIL OLIFF RESEARCH MANAGER, THE PEW CHARITABLE TRUSTS

As part of a project on higher education finance supported by the Bill and Melinda Gates Foundation, Nate Johnson interviewed a number of experts and leaders to gather different perspectives on how major budget choices are made. The interviews have been condensed for publication so that the key insights are available to anyone who is interested.

This interview with Phil Oliff, whose career has been focused at the intersection of education policy and finance and tax and budget policy, addresses cyclical patterns of state and federal support, budget volatility, and the variation in federal and state funding across the U.S.

Are there areas other than higher education where there is a similar relationship between state and federal budgets, or is higher education really where the cyclical pattern of decreasing state support and increasing federal support is stronger than in other areas of government?

I haven't looked specifically at that area, comparing it across different areas of government. One thing I will say is a big difference between federal and state governments is states' need to balance their budgets. When a recession hits, and they have a budget gap, they've got very limited choices. They need to either cut spending, raise revenues, draw down reserves or some combination of the three to fill that hole. The federal government is different in that the federal government can run a deficit.

Higher education, researchers have found, is the most cyclical area of state spending. When you take a look, and you compare other areas, that cyclical trend hits hardest in higher education.

Do you think it's likely to get more or less volatile over time?

It's an open question. Higher education at the state level has traditionally been very sensitive to economic cycles. It tends to go down during periods of economic weakness, and now you see it coming back up as the economy strengthens. I think it's a really open question as to what's going to happen if another recession hits. It's very possible that it will go back down again.

Given all the constraints on other financial variables in state government, higher education becomes the last discretionary piece where all of the budget volatility ends up. Do you think that's right?

We at Pew specifically haven't gone back and tested it. Certainly, if you look back at the data, the higher education funding is highly cyclical. You can see that pattern where it goes down during recessionary periods and comes back up during economic recoveries. The federal-state lens is something that we want to dig deeper into in the future. Higher education is very different, in terms of the federal-state relationship, from other major areas where there are significant federal and state investments.

For example, in K-12 education, in Medicaid, in transportation, you see that the federal dollars generally flow through state and local governments. Then there are generally strings attached to that funding in some way, whether it's maintenance of effort requirements or matching requirements in the case of Medicaid. In K-12, you have a requirement that federal funding should supplement and not supplant state funding.

Higher education is different from many of the other major policy areas where there's significant federal and state investments. The difference in higher education is that, for the most part, those dollars don't flow directly through state and local governments, and there generally aren't the same kinds of strings attached to that federal funding—specifically for states.

You see the biggest cuts to state higher education funding and the biggest spikes in tuition at public schools immediately following economic downturns. So these funding cuts and tuition increases are happening just when enrollments are surging and you have the biggest drops in family income. When the economy is recovering, and there's a little more money in the state's budget, state funding starts to come back up and tuition starts to stabilize. Over time, those things tend to happen at the times of least need rather than most need. I think that's really a key financial challenge for public higher education.

In terms of thinking through what the policy implications of all of this are, what we tried to do is take a step back and look at the big picture, to provide a kind of factual frame for policy discussions going forward. Trying to, in a very clear and simple way, look at the big picture of federal and state higher education funding.

I think when we started out on this work, we had seen a fair bit analyzing what was going on with federal higher educational funding and state funding separately, but less analysis looking at federal and state funding on the same plane and looking at how they fit together.

One of our key findings from this analysis was this major shift in federal and state funding. With the decline in state funding and growth in federal funding, it was really more of a shift between federal and state funding than even I had anticipated—a shift not only in who's paying for higher education, and the levels of funding, but also because the federal and state governments pay for a higher education or support higher education in these very different ways.

The biggest chunk of federal money going to support for students is to be used at a range of different institutions, versus states providing the biggest chunk of funding in the form of general support—specifically for public institutions, it was a shift not just in these relative levels of funding, but in the way that public funding supports the higher education system.

Understanding that, and thinking through that shift, is really important for thinking through policy going forward. Our report tried to provide building blocks for understanding that shift, and our hope is that it can spur informed thinking about policy approaches going forward.

Do you have any general thoughts about what some of the constraints on states might be or on what the federal government is well-suited to do or not well-suited to do?

One of the key lessons that came out of our analysis is just how dramatic the differences in the relative levels of federal and state funding are across states. Not just in terms of the size of the federal and state funding, and the size relative to each other, but also in other categories of funding. We looked specifically at public colleges and universities across states, and then charted out what those differences looked like. The finding was really, in many ways, we're dealing with 50-plus different state systems of higher education.

At the federal level, two of the biggest chunks of funding and what drives this variation across states, is both financial need with the Pell Grants, and also the types of research that's going on.

At the state level, a lot of it depends on policy choices. There are probably very different answers for different states, but one possible explanation is the kind of philosophies the states have about how higher education should be funded. A couple of examples we specifically looked at were North Carolina and Wyoming. Both have written into their constitution that public higher education should be as close to free as possible. When we crunched the numbers, we really saw that philosophy borne out in the data. We saw both of those states had higher-than-average state support for public higher education institutions and collected lower-than-average net tuition revenue.

Even when you're thinking about federal policy and where the federal funding fits in, there's going to be a different story in different states. It's important to keep that variation in mind when you think about policy.

Phil Oliff is a research manager for the fiscal federalism initiative at Pew Charitable Trusts. He previously worked as a policy analyst with the Center on Budget and Policy Priorities and served as a Hugh L. Carey Fellow in Governmental Finance with New York State's Division of Budget.