Date: October 10, 2013

Subject: Updated UW Analysis: "Pay It Forward"

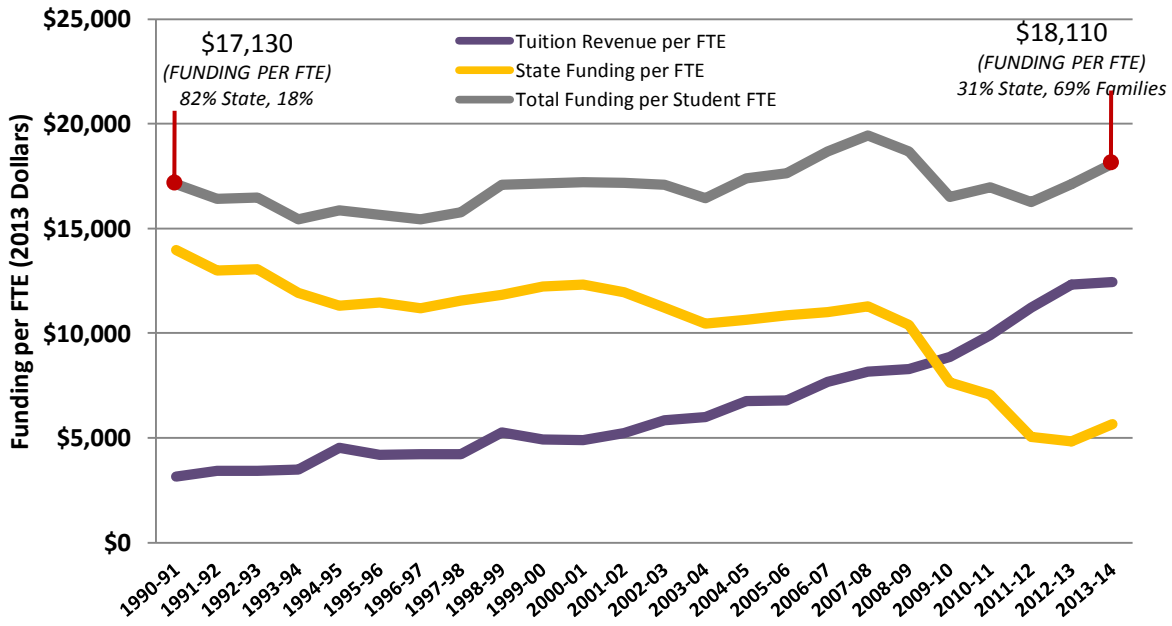
Pay It Forward (PIF) offers an alluring, simple tuition repayment arrangement during a time when student debt concerns are at a fever pitch. However, good timing and easily understood propositions do not make sound, or even achievable policy. PIF, at its core, is a framework by which students in small programs, single universities, or even entire states or countries would pay no tuition and fees upfront (though they would pay all other educational expenses upfront), and ultimately pay back a certain percent of their adjusted gross income for 25 years into a fund to pay tuition expenses for current students (or, really, university operations).

Additions to ongoing tuition and financial aid policy debates are welcome; but those that do not begin with an accurate base of assumptions, or fail to integrate critical elements, must be examined carefully. PIF is not a new concept, but this iteration provides several noteworthy implementation examples, one of which involves the University of Washington (UW). Because of this, it is critical to clarify or, in some cases, correct problematic assumptions underpinning the proposal. Namely, PIF fails to integrate federal, state, and institutional financial aid information, it would prove harmful to the viability and quality of institutions, and it may prove to be more expensive for the students it claims to protect.

PIF assumes current state and tuition revenue per student FTE is all the University needs to operate indefinitely

Figure 1 displays state funding and tuition revenue per student FTE over time.

Figure 1: Funding Per Student FTE (All "State Funded" FTE Included)



Although the graph above shows interesting trends of two major types of funding as well as the combined amount of funding per student FTE, it does not provide a comprehensive basis for the PIF proposal for the following reasons:

1. The chart leaves out other revenue sources that we increasingly rely on to provide critical support for core educational operations;
2. The chart includes all student categories in all academic disciplines; and,
3. The chart is limited to prior years and does not contemplate future investments or critical expenses, which ensure the continued quality of our state's flagship university.

Figure 1 has been used in the past to illustrate both the revenue and cost of core educational operations at the University. However, the conversation about cost per student has evolved over the years given better information from the latest Office of Financial Management (OFM) higher education expenditure study. **Tuition and state support are not the only sources of funds for undergraduate instruction; it is also funded through endowment returns, philanthropic gifts, and more.** Thus, it would be a mistake to base PIF principles on the assumption that resources expended on undergraduate education have been flat for twenty years.

OFM's study provides an indication about expenditures per undergraduate FTE in a more comprehensive manner, including revenue sources not previously contemplated by previous Higher Education Coordinating Board cost studies. The OFM study estimated that the annual expenditure level per UW undergraduate FTE was $13,586; per UW undergraduate engineering FTE, the annual expenditure was $23,150; and per UW undergraduate nursing student FTE, the annual expenditure was $30,723. The assumptions and applications of indirect and direct expenditures by program and student level are imperfect, but these results indicate that **expenditures vary by discipline and as is clear in the report, expenditures per undergraduate FTE vary by institution**.

The study also shows the variation of expenditures by student level and almost one-third of UW students are above the undergraduate level. the amount of combined state and tuition funding available on a total per student FTE basis is not equivalent to the amount of expenditures used to educate each undergraduate student at the UW for several reasons. First, almost 30 percent of UW students are graduate and professional students, and expenditures vary by student level. Thus, combined state and tuition funding per student, calculated over all students, does not tell us about expenditures for undergraduates. PIF claims that its fund (financed by UW graduates) will grow sufficiently to allow for even more students to attend the UW without paying upfront tuition costs. However, it would seem that this component assumes a fixed level of state and ever growing "PIF" funding to support enrollment growth. As we have relied less on state funding, the revenue sources marshaled for the support of our students have only increased in number and volume. **That the UW would operate for any number of years with flat funding is to assume no faculty salary increases, no additional faculty hires, stagnant teaching and research assistant FTE and salaries, and no critical infrastructure fixes.** We fear the loss of top faculty and teaching assistants to other schools – as faculty in many disciplines are compensated well below peer averages – and that our students would study in derelict, over-capacity facilities. Additionally, though PIF would add incremental student FTE using additional revenue from the PIF fund, we would challenge its advocates to question where these students will study, given that most colleges are at or over capacity. The primary drivers of state and tuition-funded expenditures are salaries, benefits, and capital infrastructure maintenance. Replacing these revenue sources with one stagnant (or possibly declining) funding source, which assumes revenue growth will be devoted to student FTE growth, will harm quality in countless ways.

Interestingly, in the last legislative session, UW students publicly committed to increase tuition rates to generate revenue for faculty salaries. UW students understand that their tuition revenue pays faculty salaries, which is correlated with faculty retention and recruitment, academic and research quality, and the market value of their degrees.

As many have pointed out, the **PIF proposal does not fully unpack the complications and unknowns of graduates' incomes over time**. The proposal assumes an increasing number of students paying a percentage of their adjusted gross incomes (AGI) (which are also assumed to increase) into the fund over time. However, the proposal would seem to incent individuals to avoid entering the workforce. What of graduates who attend graduate school, underemployed individuals, fathers and mothers who chose not to work, and those who enter into lower paying fields? Are these individuals then eligible for a financial windfall in a way that an individual who earns more money over time or remains in the workforce is not?

Any student who expects to earn a high income after graduation would also expect to pay more for his or her education than the actual cost of tuition; thus, that student would have a strong incentive to not enroll in an institution that installed PIF or to view the program as fundamentally unfair. If enough of these students enroll elsewhere, or if they were convinced to attend a university with the option to pay tuition instead of entering a PIF arrangement, the program would likely not be financially sustainable. It might also have the unintended consequence of changing or lowering the "quality" of our student body, which would have an effect on the workforce in our state.

Another significant implementation issue only briefly acknowledged is the means by which PIF participants would be held accountable for payments. While PIF advocates acknowledge that the IRS would need to be involved in the execution of PIF, it is not clear whether this would be an actionable or lawful approach. Could earnings be garnished if students did not pay their PIF obligation? This problem comes into sharp relief when considering partial PIF implementation, whether by a state, an institution, or one program in an institution. How might small actors serve as collection agencies? How might institutions such as the UW handle tracking students when there is no infrastructure to do that work? What of transfer students or students who have earned several credits, but not degrees? What are small actors to do when graduates leave the US and do not file tax returns or maintain a US address?

The unknowns inherent in the revenue side of PIF are monumental and yet largely unanswered by its advocates.

Instead of focusing energy on obvious barriers to implementation, PIF assumes they will be dealt with eventually

Exploring alternative higher education funding ideas is important. Providing small acknowledgements of significant barriers to implementation without contemplating actionable steps to overcoming those barriers is unhelpful. For each implementation idea, significant challenges arise for institutions and students alike.

1. **PIF assumes graduates' starting salaries will be low and remain thus**

PIF is based on the belief that students will perceive that paying a certain amount of their AGI for the next 25 years is less of a risk than taking on student loans; it is not clear whether this assumption is correct. Moreover, this approach may cost many students more than it currently costs them to use student loans to cover tuition. The proposal assumes a relatively low starting salary to demonstrate how students may benefit from PIF. The table below shows the cost of PIF for students with various starting salaries. For the sake of comparison, note that if a student today took a loan of $48,000 to cover tuition for four years and if that loan was a ten-year loan with a 5 percent interest rate, then the total cost to the student would be $61,000.

Table 1. Student expenses under PIF

Starting Salary	Cost to Student under PIF*
30,000	36,000
35,000	44,000
25,000	51,000
40,000	58,000
45,000	66,000
50,000	73,000
55,000	80,000
60,000	88,000
65,000	95,000
70,000	102,000
75,000	109,000
80,000	117,000
85,000	124,000
90,000	131,000
95,000	139,000
100,000	146,000
*** Assumes 3% salary increase per year**	

It is difficult to determine starting salaries of recent graduates and any estimates of average starting salaries must be viewed as suggestive at best. That said, it may be worth noting that a recent PayScale ranking of starting salaries by college reported an average starting salary for UW baccalaureate recipients of $49,000. **In fact, a student must have a starting salary below $42,000 to pay less under PIF than they would to using the student loan described above**.

2. **PIF does not contemplate the use of federal and state financial aid grant programs accurately**

The proposal states that, under PIF, "students retain access to federal financial aid to cover their cost of living, books, etc." It must be noted, however, that by removing the cost of tuition and fees from a student's budget, that student's level of calculated need will fall, as will their eligibility for various federal and state need programs. Unless PIF is implemented on a nationwide basis with appropriate adjustments in federal aid policy as part of the Higher Education Act, students will be less able to cover other costs of education with existing aid packages.

3. **PIF overpromises the state contribution in the state-wide implementation scenario**

Under the state-wide implementation scenario, students in all Washington public universities would simultaneously be included in PIF. The estimate of first-year expenses is $600 million with costs escalating up to $1.4 billion in the fourth year. At that point, hopefully, some graduates begin paying into the fund (though it is not clear how many students would be graduated and at what rate they'd be replenishing the fund). Setting aside the state's rather low four-year graduation rate and unknown first-year starting salaries for new graduates, the estimates for ongoing PIF related expenses are wildly low and, as described above, call into question our ability to remain competitive and provide quality to our students.

It is flawed to assume, as the proposal does, a guaranteed amount of state funding (noted as offsetting the eventual "contribution" back to the University); the University cannot expect that the state will be able to afford a steady flow of enrollment-based funding. We have seen state funding per FTE swing dramatically with each recession. In FY08, the state provided $11,540 of funds per UW FTE and now provides less than $5,550 per UW FTE (including, again, all student FTE and not simply undergraduates). The latest state revenue forecast predicts flat or slightly higher collections for the ongoing biennium, with probable downside risks. Our state is just now recovering from the Great Recession and is facing significant financial commitments to K12 as part of the McLeary Decision. **To assume that the state will increase its funding enough to sustain a growing population of undergraduates at a consistent, inflation adjusted per student rate is to ignore forty years of per student state funding trends. Until the fund would become self-sufficient at year 25, the state would need to front $22 billion in university funding.**

If some portion of state support were to be supplemented with private endowed or one-time funds, cash flow issues would become problematic. Imagining a scenario in which either a new cohort or an entire university would not pay tuition upfront, but rather a bond, new tax revenue, or endowed/gift funds would be used to "float" the University, is extremely unlikely. Temporary funds from one-time cash gifts cannot be used for faculty salaries or permanent, ongoing expenses. Endowed gifts take several years to generate sufficient capital for disbursement, they cannot be used in the short-term, and they are susceptible to market fluctuations.

4. **PIF could harm the students it claims to protect by robbing them of needed grant funding**

The PIF proposal contains an implementation scenario where "Husky Promise" students commit to paying 1 percent of their AGI into the PIF fund as a first stage of implementation. Under this scenario, UW undergraduates who qualify for Pell or State Need Grants (SNGs) and, thus, currently benefit from the Husky Promise program—which is the UW's commitment to charging them no tuition and fees—would continue to pay no tuition upfront. However, instead of having their tuition covered without any future obligation, these students would have to pay back tuition and fee expenses as a percentage of their income for 25 years. In other words, though students with significant need currently receive federal, state, and institutional grants for tuition and fees, they would pay back these fees under a PIF scenario.

Currently, a significant amount of tuition revenue from undergraduate students is returned to resident undergraduate students with need—whether these students are called "Husky Promise" or not—and up to 60 percent of total need (which takes into account costs like room, board, textbooks, etc.) is met for the neediest students. Aid is distributed to students from families making more than 50 percent of median family income on a sliding scale after neediest students are packaged. In other words, and as will be discussed in greater detail in the next section, aid is reaching middle income students already at the UW, though on a sliding scale.

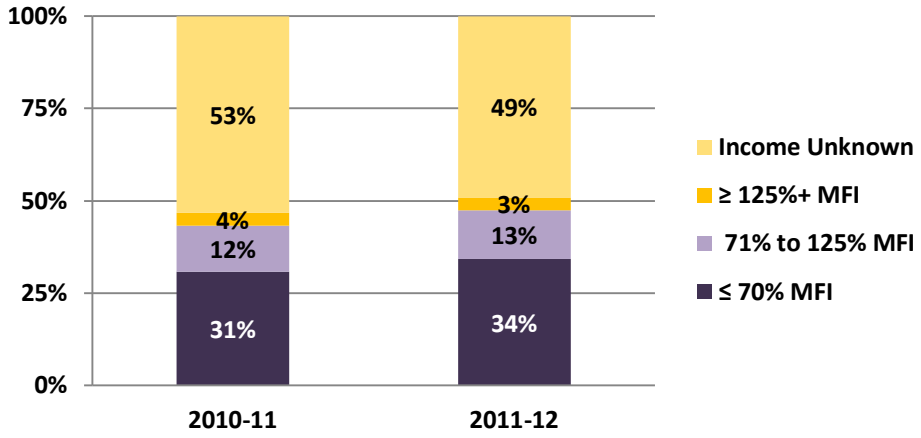
Under PIF, the Husky Promise students who already face loan debt from other, non-tuition educational expenses would be required to pay back not just those loans, but their tuition and fees as well. This would not be an improvement over the status quo. Apart from an obvious student equity issue, it is unclear how institutions are to track the repayment of students who may qualify for SNG, Pell or other loans—which would put them in PIF territory—during some years but not others. Tracking these students (not to mention tracking graduates' payments into the PIF fund over time) will require significant new staffing at our university, meaning more operating revenue would be needed from the PIF fund, the state, and/or students.

PIF assumes that tuition costs are currently out of reach for lower- and middle-income students

While PIF's advocates correctly link declining state appropriations to rising tuition rates, the proposal does not describe the effect of grants and loans on our students. Further, it makes the inaccurate assumption that pursuing higher education is out of reach of many students.

While it is clear that rising tuition rates are an effect of declining state appropriations and that many students and families shoulder the burden of funding core university operations, it isn't true that the socioeconomic composition of our undergraduates has significantly changed, even after Regents approved a 20 percent tuition increase in 2011-12.

Figure 2: UW
Undergraduate Residents by Income Relative to MFI



Rising tuition rates might have meant a loss in the economic diversity of some student populations, but this has not been the case at the UW. Last year, close to one-third of UW undergraduates received Pell Grant funding, 29 percent of all UW freshmen were the first in their families to attend college, and 33 percent (about 9,200) of UW undergraduate residents were eligible for the Husky Promise program.

Grants and Waivers

Changes in UW grants and waivers awarded to undergraduate residents demonstrating need are shown in Table 2. As shown, institutional grant aid awarded to undergraduate residents demonstrating need doubled from 2010-11 to 2011-12, increasing from $16.2 to $32.6 million. Waivers increased by almost 30 percent, from $10.5 to $13.5 million. The increases were dramatic on a per-student basis as well, in **spite of the fact that more students demonstrated need**.

Table 3 shows the distribution of scholarship, grant, and waiver aid by source to undergraduate residents demonstrating need; it also shows the use of loans and work study by those students. As presented, institutional aid increased the most, and state aid also showed an increase.

Table 2: UW Grants and Waivers to Undergraduate Residents Demonstrating Need

Year	Total		Average*	
	Grants	Waivers	Grants	Waivers
2010-11	$16,200,000	$10,500,000	$1,091	$704

2011-12	$32,600,000	$13,500,000	$2,041	$842
Increase	101%	29%	87%	20%

*Average is calculated over all students demonstrating need, regardless of aid received.

Table 3: Aid to UW Undergraduate Residents Demonstrating Need, by Source and Type

	Scholarships, Grants, and Waivers					Loans and Work Study	
	Federal	State	UW	Endowment	Other	Loans	Work Study
	Total						
2010-11	$47.8 M	$41.6 M	$29.4 M	$4.6 M	$7.3 M	$84.8 M	$1.1 M
2011-12	$47.6 M	$56.1 M	$49.1 M	$5.8 M	$8.3 M	$89.6 M	$2.2 M
	Average (Per-Student Aid to Students Demonstrating Need)						
2010-11	$3,217	$2,798	$1,980	$307	$493	$5,705	$73
2011-12	$2,975	$3,506	$3,068	$364	$520	$5,602	$138

Loans

Describing UW students' use of federal loans as a "problem" or a "crisis" is purely subjective. Though the average student loan debt upon graduation has increased and will likely increase in the future, half of our students graduate with no debt and those who leave with average $20,316 in debt, compared to the national average of over $26,000. Our graduates pay back their loans consistently. Additionally, although the national cohort default rate includes all students and not just undergraduates, our three-year rate remains seven percentage points below the national average, at 3.2 percent.

Assuming that undergraduate loan use remains moderate and below national averages, it is important to challenge PIF advocates to show exactly how much students would pay back over time under PIF, compared to the income-based loan repayment structure. As demonstrated above, we believe that our lower and middle income students, as well as students who do not quality for aid, will all pay more eventually under a PIF scenario.

Conclusion

PIF advocates claim that their approach to financing higher education is novel. However, there is nothing innovative about applying an income-based approach to pricing goods and services to benefit individuals, and the public, at large. Students have enjoyed predictable, differential tuition pricing by income, family size, and net assets for decades. So, we would ask PIF advocates what their model achieves that the current model does not? The unknowns are far too many, the analysis far from rigorous, and the implementation barriers too great. Further, and perhaps most importantly, students from all backgrounds may end up paying more under the PIF model than they would otherwise. States such as Washington cannot afford the upfront expense and small actors such as departments or individual universities are not in the business of serving as collection agencies.

Rallying support for increased public funding of higher education is a worthwhile and critical endeavor. We believe that PIF distracts the higher education community from that work.

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