Setting Institutional Student-Aid Policies: New Metrics for Governing Boards

BY DON HOSSLER AND DEREK PRICE

ONE OF THE MOST IMPORTANT FUNCTIONS OF THE governing board of a college or university is to ensure that it sustains financial health so it can effectively carry out its mission. Like all major expenses, institutional financial aid, when done well, reflects the mission, as well as the major priorities, of an institution. Yet it remains one of the most complex and least understood areas of institutional expenditures. Campus-based financial aid has become one of the single-largest expenditures for many independent and public colleges and universities, exceeded only by instructional expense and spending on auxiliaries. According to the College Board publication *Trends in Student Aid, 2013*, institutional grant aid almost doubled between 2002–03 and 2012–13 to more than $44 billion.

TAKEAWAYS

1. Campus-based financial aid has become one of the single largest expenditures for many colleges and universities.
2. Discussing how institutional aid is being used and the sources of that aid can be difficult because there are no commonly accepted metrics for reporting financial-aid expenditures.
3. AGB and NACUBO are working to provide a resource for senior campus policy makers to assist them in making smarter and more strategic decisions about institutional aid.

In practice, colleges and universities have numerous sources for institutional aid, including endowment funds, current tuition and fee revenue, and the general operating budget, but historically, the use of tuition revenue to achieve campus enrollment goals was rare. Beginning in the 1980s, however, independent colleges and universities that were neither well-endowed nor highly selective began using tuition revenue to provide scholarships. Since that time, tuition discounting (the practice of offsetting published tuition price or "sticker price" with institutional grant aid) has become commonplace and a major expenditure among independent colleges and universities.

Recent studies conducted by the National Association of College and University Business Officers (NACUBO) show that the average discount rate at private institutions in 2012 was 39.7 percent for all students and 45 percent for first-year students. More recently, tuition discounting has become increasingly common among public colleges and universities, with research showing that the average tuition discount rate (that is, the ratio of total institutional grant aid relative to gross tuition revenues) has been steadily rising since 2002, to 12.3 percent in 2008.

There is growing concern about rising discount rates at public institutions; in particular, some research concludes that sustained discount rates of 13 percent or higher risks those institutions' long-term financial health. Additionally, some policy makers have questioned the effectiveness of discounting. Headlines and commentary such as "Is Tuition Discounting Broken?" are becoming increasingly common. A 2013 issue of NACUBO's *Business Officer* reported that more than half of all independent colleges saw declines in the number of entering first-year students—despite an increase in institutional financial aid that resulted in higher discount rates over 2011. It is not surprising that both the private and public sectors are asking hard questions about the strategies associated with using tuition revenue to fund campus-based scholarships to induce students to enroll.

Governing boards have an important responsibility when it comes to decisions about the use of institutional financial aid to achieve strategic goals and determining how the use of tuition revenue or forgone revenue (i.e., tuition discounting) can advance the mission of the institution. Boards might discuss this issue within committee meetings, such as student affairs, academic affairs, finance, or enrollment. In 2010, an AGB examination of board committee structure reported that enrollment and enrollment management committees—the committees most often charged with discussing tuition discounting, enrollment goals, and student aid—were among the most common at independent institutions but not at publics. In any case, given the level of investment in institutional financial aid at many independent institutions and at an increasing number of publics, the issue of how institutional aid is funded and for what purposes has become an important subject for members of governing boards.

Deciding how institutional aid is funded and used to achieve strategic or mission-driven purposes is arguably one of the most multifaceted areas of postsecondary educational finance with which governing boards must deal. Campus-based financial-aid dollars can be used to increase socioeconomic and racial diversity, to bring in more revenue, or to enroll high-ability students in the pursuit of prestige. But those goals are in constant tension with one another, and it is seemingly impossible to simultaneously maximize institutional goals in all of those areas.

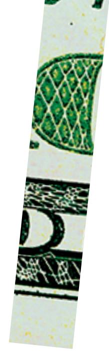
Examples of the tradeoffs abound: According to an *Inside Higher Ed* article (January 17), the University of Puget Sound reduced its discount rate from 43 percent to 38 percent. That reduction in institutional-aid expenditures reduced campus expenditures on need-based aid and resulted in a drop in enrollment among first-generation students from 17 percent to 8 percent. Vassar College, with a stronger endowment, increased its discount rate from 35 percent to 50 percent and increased its share of minority students from 20 percent to 35 percent. In Vassar's case, it appears the institution must have increased campus aid to low-income, nonmajority students, and this strategy was successful.

The Need for Uniform Data on Institutional Aid

Engaging board members, presidents, chief business officers, and enrollment managers in group discussions about how institutional aid is being used, and the sources of that aid, can be difficult. In large part, that is because there are no commonly accepted metrics for reporting financial-aid expenditures, let alone for comparing institutions, or for using standardized benchmarking tools to assess the use and efficacy of campus-based financial aid. This is a serious limitation that affects the ability of senior campus policy makers to carefully consider how they are spending their financial-aid dollars.

Additionally, many board members may not have a comprehensive understanding of how campus-based financial aid is spent and the implications of these expenditure decisions upon institutional health and vitality, unless there is a board committee that deals with enrollment concerns or the president or chief business officer makes it a point to educate board members on this topic. How might campus policy makers or boards of public institutions react, or what questions might they ask, if they learned that more than half of all campus aid was being awarded to students from families with incomes of $100,000 or more? Or that less than 20 percent of all campus aid was going to students from families with incomes below $35,000?

It is especially difficult for presidents to have candid conversations with peers about their use of campus-based financial aid because they could be accused of violating antitrust laws if they met together to discuss such strategies. At many institutions, presidents are not fully aware of where institutional aid is going and the effects of aid upon net institutional revenues or important enrollment-related goals. Moreover, some presidents would prefer that neither their cabinet of senior campus administrators, nor the board of trustees, become too involved in how the campus allocates its



financial-aid dollars. Finally, some presidents sense that a contingent of faculty and board members might not agree with campus financial-aid priorities, whether with respect to how aid is distributed among income groups to enroll a more diverse student body or the amount of aid going to meet demonstrated student financial need.

Fortunately, NACUBO and AGB received funding in 2012 from The Robert W. Woodruff Foundation to address this lack of information about institutional aid. The goal of the project, *Looking under the Hood*, is to provide a resource for campus leaders to assist them in making smarter and more-strategic decisions about institutional aid. It is designed to provide chief business officers, chief executives, and board members with a standard set of indicators or metrics that can be adopted as good practice. These indicators can be used annually to examine many aspects of institutional aid, including: 1) total financial-aid expenditures, 2) the tuition discount rate, and 3) how campus dollars are distributed to various student populations to achieve institutional goals, such as meeting student financial need, attracting more high-ability students, enrolling a more diverse student body, and enhancing institutional revenues. Given that colleges provided more than $44 billion in institutional aid in 2012–13, the development of such metrics is timely and perhaps even long overdue.

Key policy and practice questions that the metrics are intended to guide include:

1. *Are institutional-aid policies consistent with the mission and values of our institution?*
2. *Is institutional aid being delivered to the types of students we most want to see on our campus?*
3. *Is aid ultimately going to students who succeed (i.e., do students who receive our grants graduate)?*

Along the way to developing these institutional-aid metrics, an advisory board of trustees, presidents, and CBOs from public and independent colleges and universities indicated that the metrics to be developed should be simple and from easily accessible data sources; reflect an institutional perspective; be relevant to a diverse set of higher education institutions; and be intended for internal—not public—discussion. The advisory committee also expressed interest in the development of a dynamic Web-based tool to allow institutional leadership to compare their data with that of other institutions on these key metrics.

In addition, the tool could be used to upload data on institutional-aid expenditures and recipients that are not currently available from other sources—specifically, student demographic data, such as the percentage of aid awarded to students by income group, gender, or ethnicity. Only the institutions themselves can provide that type of data. The advisory committee urged its collection, but only if enough institutions are willing, so that the sample size is sufficiently large that individual participating institutions cannot be identified.

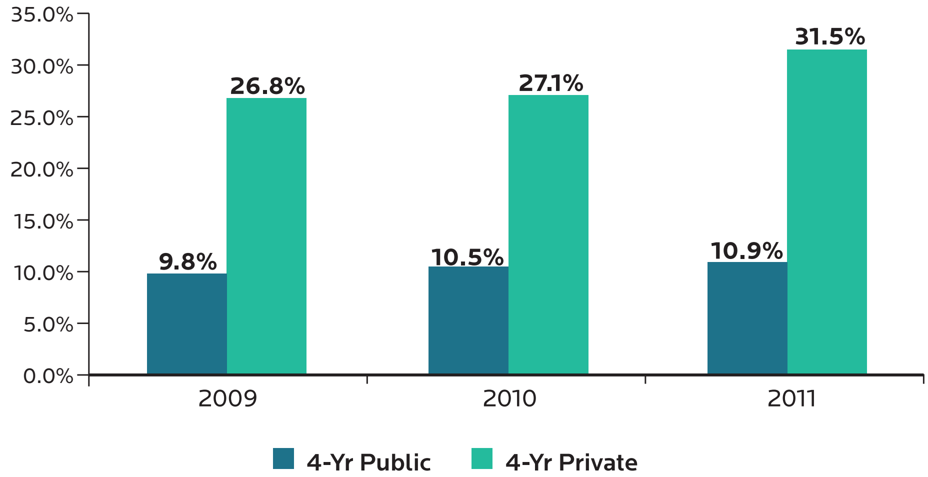
Examples from *Looking under the Hood*

During the first 18 months of the project, staff members and advisers developed and administered a survey of institutional-aid expenditures that the 10 colleges participating on the advisory committee completed. Two national data sources that provide information on colleges' finances and expenditures—IPEDS, the Integrated Postsecondary Education Data System collected by the National Center for Education Statistics, and the College Board's Annual Survey of Colleges (ASC)—were also merged to create an initial database of more than 1,400 institutions for the Web-based tool. In this next section, we provide examples of some of the metrics that have been developed for this project as well as how we envision they could inform a campus discussion on institutional-aid policy.

Figure 1 provides an example of one possible metric developed for this project: the percentage of tuition and fee "sticker price" that is covered by the average institutional grant per FTE undergraduate at public and independent four-year colleges and universities. These data indicate a small increase for public colleges and universities of about 10 percent between 2009 and 2011, and a larger increase for independent colleges and universities of more than 15 percent. To put this growth into perspective, the College Board reports that tuition and fees at public and private four-year colleges and universities increased between 2009 and 2011 by about 16 percent and 8 percent, respectively, in current dollars. That percentage growth in average institutional grant aid reflects an even more significant increase in dollars used for institutional grant aid—either from endowment income, the use of institutional resources, or from forgone revenue resulting from tuition discounting.

Are governing boards actively engaged in college decisions regarding the use of institutional grant aid, how it is funded, and for what purposes? Are trustees asking about the impact of those decisions, such as

Figure 1: Percentage of Tuition and Fee "Sticker Price" Covered by Average Institutional Grant per FTE Undergraduate



Data Sources: IPEDS and College Board. Calculations by NACUBO and AGB.

the results in terms of strategic or mission-driven goals the increases in institutional aid were expected to achieve? What is the pattern of change in how institutional-aid funds were spent over time? How does our spending on institutional aid compare with peer institutions on these metrics? Have other expenditures been deferred to fund financial-aid programs? We believe that metrics, such as this example and others in this article, can and should inform such strategic discussions among all college leaders, and especially board members.

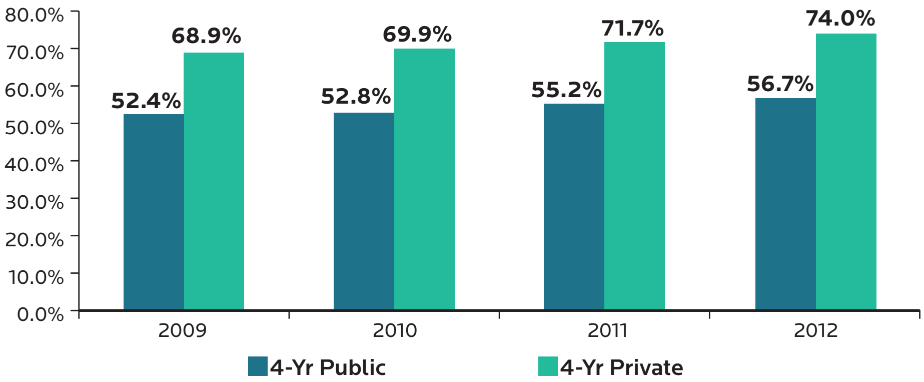
Figure 2 provides a different example of a proposed metric developed for this project: the percentage of institutional aid that is need-based. The data indicate a small trend toward increasing institutional need-based grant aid between 2009 and 2012. This trend is small—about a five-percentage point increase at private four-year institutions, and a four-percentage point increase at public four-year institutions. Although modest, it is not clear from these data why institutional need-based grant aid has increased over the past four years.

Several explanations are plausible. First, this trend could be a result of larger economic factors, such as the recession of 2008–09 and the resulting decline in employment and income among college-going students and their families, along with the slow and uneven economic recovery. Second, the trend could be an artifact of rising college prices and the corresponding increase in financial need among students that results from the federal and independent methodologies used to determine the amount students and their families have been expected to contribute toward their total higher education expenses. Third, this trend could be the outcome of intentional policy decisions by colleges and universities to direct more of their institutional grant aid toward need-based aid. In other words, are institutional leaders adjusting their spending on campus-based financial aid because of these external factors and to intentionally help students enroll in college by increasing need-based aid?

Should trustees be asking these types of strategic and intentional decisions about how, and for what reasons, institutional aid is distributed? More generally, do colleges have an explicit goal for awarding *need-based* institutional aid? How does the distribution of institutional aid between need and non-need comport with a college's mission and goals? Most important, an examination of this trend by senior campus administrators and governing boards can inform key institutional policies.

Figure 3 provides an example of one type of demographic-based metric we hope to create once more institutions provide data to us. The graph shows the distribution of institutional aid at one of the public four-year research universities that responded to the *Looking under the Hood* institutional-aid survey. These data indicate that about 25 percent of institutional-aid dollars is awarded to students with incomes less than $48,000, while 21 percent of institutional-aid dollars flows to students with income greater than $100,000, and almost 38 percent is awarded to students with unknown incomes. We hypothesize that many students with unknown income are higher-income students and/or are receiving awards based entirely on academic merit or other non-need criteria that do not

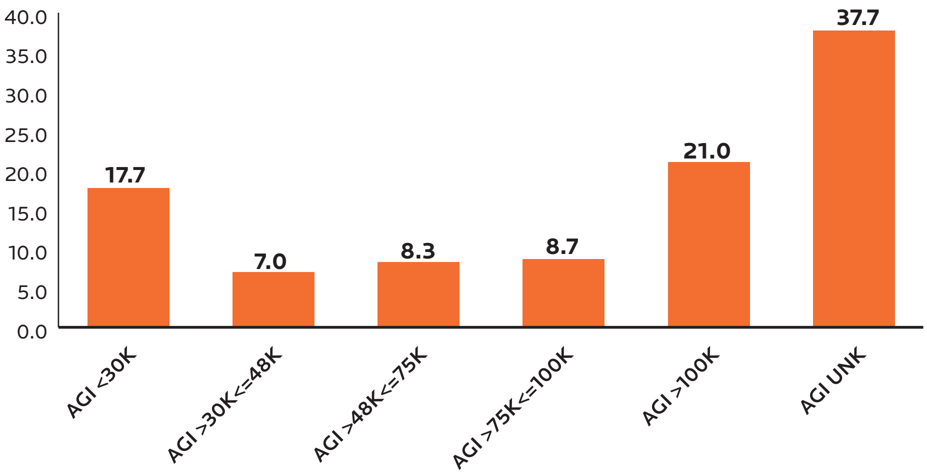
Figure 2: Percentage of Total Institutional Grant Aid that Is Need-based*



* Need-based is defined as any aid that meets students' financial need. Any merit or non-need scholarships that meet students' financial need is categorized as need-based. These data do not include tuition waivers.

Data Sources: IPEDS and College Board. Calculations by NACUBO and AGB.

Figure 3: Institutional-Aid Dollars Awarded by Adjusted Gross Income, Three-Year Average 2009–2011
Public Four-Year Research University



Data Source: *Looking under the Hood* institutional aid survey, 2013. Calculations by author.

take into account the financial need of the recipient.

Why might an institution award a majority of its institutional aid to students from higher-income families? Is this decision an intentional decision by college leaders? Are they seeking net-tuition revenue increases to replace a decline in state appropriations? Are they trying to address a "brain drain" by using institutional aid to recruit students with higher grades or stronger standardized test scores, which happen to be correlated with higher incomes?

Similarly, are they targeting institutional aid toward academic merit in order to maintain or enhance their institutional prestige or rankings? Are they shifting institutional-aid dollars to middle- and higher-income students, because they believe low-income students have other aid available to them, such as Pell Grants?

We hypothesize that if board members had access to this type of institutional aid metric, they could better understand where their institutional-aid dollars are going and discuss whether the distribution of aid dollars reflects strategic institutional goals and the overall mission of the college. In other words, is the distribution of institutional grant aid the result of intentional financial-aid policies determined by college leaders? We believe that they should be.

About *Looking under the Hood*

When AGB and the National Association of College and University Business Officers (NACUBO) partnered in 2012 to launch the *Looking under the Hood* project, with support from the Robert W. Woodruff Foundation, it was with the awareness that allocating tens of thousands of dollars to institutional financial aid each academic year requires major policy considerations among governing boards, chief executives, and chief business officers. As the article notes, over $44 billion in institutional aid is awarded annually for need-based and non-need-based aid, much of it financed through tuition and fee revenues.

The 34 metrics that have been developed for *Looking under the Hood* can help boards, chief executives, and business officers more fully understand their aid programs by placing those programs in a broad context. An online tool will display the metrics in graphic formats and allow institutional leaders to benchmark their aid programs, as well as to compare their metrics to national averages, institutional type, and self-selected peer groups (in aggregated form).

Each year, new financial data collected annually by IPEDS (the Integrated Postsecondary Education Data System) and the College Board will be added, enriching each metric and the online tool and allowing for the showing of long-term trends. The IPEDS and College Board data include information on more than 2,000 institutions and enable the development of such metrics as the percentage of total grant dollars awarded on the basis of need or academic merit.

In the near future, AGB and NACUBO hope to populate additional defined metrics on student demographics—institutional grant recipients by gender, race/ethnicity, and income level, and the retention and graduation rates of institutional-aid recipients, for example—data that are not currently collected from colleges and universities. Inclusion of several indicators on demographic data will further enrich the metrics and the benchmarking tool. The online tool will be accessible to AGB member boards this spring through a link on the AGB Web site. A parallel link will exist on the NACUBO Web site.

—Richard Novak, AGB Ingram Center Fellow

What Does It All Mean?

As we have already noted, the *Looking under the Hood* institutional-aid metrics are envisioned for institutional use and to inform a more strategic conversation among board members, presidents, chief business officers, enrollment managers, and other senior campus leaders about how institutional aid is used. Each of the indicators could be used with or without comparative data from a sample of peer institutions. Business officers and enrollment managers can use the data tables to track changes over time in the distribution of campus-based financial aid. This may prove to be the most useful function of the metrics, helping institutional committees and decision makers to determine how shifts in expenditure plans align with changes in the institution's mission and strategic plan. We hope that significant shifts in the allocation of scarce campus-aid resources reflect intentional decisions. When they do not, the metrics can serve as effective heuristic devices to stimulate discussion as to what happened and what steps can be taken to minimize the chances of surprises in the future.

The comparisons with a sample of peer institutions may also have the potential to answer the ever-important question of "How are we doing compared with similar institutions?" The ability to compare expenditures with peer institutions can help senior campus leaders raise broader questions: How similar are our aid-expenditure patterns to peer institutions? Is similar a desirable place to be? If our patterns are substantially different, is that because of distinct circumstances, such as a particular state financial-aid program that differs from most other states and affects how institutional-aid dollars are allocated? Or is it a result of changes in state appropriations? Or are they different for reasons that are not central to our mission or that are not desirable?

These tools will not answer all these important questions, but they can help stimulate vital discussions about one of the least well-understood but largest outlays on many campuses today. ■

AUTHORS: Don Hossler is the director for the Center of Postsecondary Research and professor of educational leadership and policy studies at Indiana University Bloomington. He is the chair of the *Looking under the Hood* advisory committee. Derek Price is the director of DVP-PRAXIS LTD and project advisor to *Looking under the Hood.*

T'SHIP LINKS: Kent John Chabotar, "Will Your Institution Pass the Financial-Responsibility Test?" July/August 2011. Lucie Lapovsky, "What Is the Net Price Calculator? Why Do Boards Need to Know about It?" May/June 2011. Sandy Baum, "Navigating the Complex World of Financial Aid." November/December 2010. Sandy Baum and Michael McPherson, "Student Aid and Access in the Economic Crisis." January/February 2009.

OTHER RESOURCES: *Trends in Student Aid, 2013* (The College Board, 2013).