

Now that MRC has laid out the landscape affecting the American research university enterprise, I would like to home in on some of the concerns facing public research universities such as yours.

Let me begin by noting just how incompatible the marching orders you are receiving from your states are:

- You are first challenged to dramatically broaden participation in higher education to help build a competitive workforce, by expanding the production of baccalaureate graduates.
- At the same time you are expected to provide both the world-class research and the professional graduates (scientists, engineers, doctors, teachers) necessary to sustain an innovation-driven and globally competitive national economy
- And you are expected to do it all while reducing the relative burden on tax payers who face other public spending priorities such as health care, retirement, and national security.
- Needless to say, these challenging and quite incompatible objectives are stimulating additional demands for greater productivity, cost-effectiveness, and accountability for learning outcomes.

These demanding and at times contradictory challenges could put public research universities at some risk over the next several decades.

Let me explain...

Despite their immense importance as national assets, public research universities in the United States remain tightly bound

both in public purpose, tax support, and governance to their states.

- Even as states demand more from their public universities—increasing the production of college degrees, expanding access to underserved communities, and achieving world-class performance in research and graduate studies—appropriations have been declining.
- While some of this erosion of state support is due to the cyclic fluctuations in the economy, it is also becoming clear that in most states aging populations will increasingly shift priorities for state tax dollars to the address the needs and concerns of the elderly (e.g., retirement security, health care, safety from crime and terrorism, and tax relief) rather than investing them in the future through education and innovation.
- We have already seen the share of operating funds provided through state support drop below 20% for many of our institutions (at Michigan is it now less than 6%), and with the current economic collapse it is almost certain that this erosion will continue in most states for the foreseeable future.
- While university leaders continue to make strong appeals for adequate state support, many have concluded that the most prudent course is to manage their institutions under the conservative assumption that they are likely to experience declining state support for several decades, until the baby boomers pass on into the sunset.

Public universities are further disadvantaged by political constraints (e.g., constraints on tuition, affirmative action, technology transfer, internationalization) that not only limit their flexibility and agility to adapt to a rapidly changing world but also

their capacity to serve the public interest, for example, in broadening educational opportunities for an increasingly diverse population.

- Furthermore, the intensely political nature of the governing boards of public universities is also a formidable challenge since it tends to react defensively protect the status quo rather than allow strategic actions designed address future challenges and opportunities.
- In fact, the public agenda demanded by state government and the public at large increasingly tends to focus myopically on near term agendas such as degree production, cost reduction, and accountability
- Rather than on the broader missions of the university such as creating and applying new knowledge to serve society, defending and propagating our cultural and intellectual heritage, challenging our norms and beliefs, enhancing social mobility, and producing the leaders of our governments, commerce, and professions.

Finally, the competitive landscape between public and private higher education has been shifting dramatically.

- The highly competitive nature of higher education in America, where universities compete for the best faculty members, the best students, resources from public and private sources, athletic supremacy, and reputation, has created an environment that demands achievement.
- However, while competition within the higher education marketplace can drive quality, if not always efficiency, it has an important downside.

- When serious imbalances arise in available funding, policy restrictions, and political constraints, such competition can deteriorate into a damaging relationship that threatens not only institutional quality and capacity but more seriously the national interest.
- Today an intensely Darwinian, 'winner-take-all' ecosystem is evolving in which the strongest and wealthiest private research universities have become aggressive predators, raiding the best faculty and students from less generously supported and politically or policy constrained public research universities while manipulating federal policies (e.g., research funding, student financial aid, tax benefits) to sustain a system in which the rich get richer and the poor get devoured.

The plight of the public research university is not only a serious challenge to the states but as well as to the nation.

- Today the public research university in reality is the backbone of advanced education and research in the United States.
- These remarkable institutions, because of their size, intellectual breadth, and quality produce most of the scientists, engineers, doctors, lawyers, teachers, and other knowledge professionals for the nation.
- They conduct most of America's basic research.
- And they perform most of the public service sought by the states—ranging from health care to agricultural and industrial extension to economic development to social mobility.

Our public research universities represent one of this nation's most valuable assets. It would be a national disaster if the public research university in the United States were to deteriorate to the point at which it could no longer conduct advanced education and research at world-class levels!

## So What Is Going On?

Clearly we live in a time of great change, an increasingly global society, driven by the exponential growth of new knowledge and knitted together by rapidly evolving information and communication technologies.

- It has become apparent that the strength, prosperity, and welfare of a nation in today's global knowledge economy will demand a highly educated citizenry enabled by development of a strong system of tertiary education.
- It will also require institutions with the ability to discover new knowledge, develop innovative applications of these discoveries, and transfer them into the marketplace through entrepreneurial activities.
- Hence nations are increasingly challenging their universities to broaden educational opportunity, achieve world-class standards, in quality and reputation, and become more efficient and productive.
- Yet it is clear that achieving such objectives, both complex and frequently incompatible, will require significant change, at the public policy level of both the federal government and the states, the institutional level of colleges and universities, and the attitudes of students, parents, and the public at large.

While public surveys still suggest strong support of American higher education, numerous studies sponsored by government, business, foundations, the National Academies, and the higher education community have suggested that

- The past attainments of American higher education may have led our nation to unwarranted complacency about its future.
- Here there are three issues of particular importance: accountability, economics, and markets.

## Accountability

Of particular importance here was the National Commission on the Future of Higher Education—the so-called Spellings Commission—launched by the Secretary of Education in 2005 to examine issues such as the access, affordability, accountability, and quality of our colleges and universities.

This unusually broad commission, comprised of members from business, government, foundations, and higher education, concluded that

- “American higher education has become what in the business world would be called a mature enterprise, increasingly risk-averse, at times self-satisfied, and unduly expensive.
- It is an enterprise that has yet to address the fundamental issues of how academic programs and institutions must be transformed to serve the changing educational needs of a knowledge economy.
- It has yet to successfully confront the impact of globalization, rapidly evolving technologies, an increasingly diverse and aging population, and an evolving marketplace characterized by new needs and new paradigms.”

More specifically, the Commission raised two areas of particular concern about American higher education:

- “Too few Americans prepare for, participate in, and complete higher education. Notwithstanding the nation’s egalitarian principles, there is ample evidence that qualified young people from families of modest means are far less likely to go to college than their affluent peers with similar qualifications. America’s higher-education financing system is increasingly dysfunctional. Government subsidies are declining; tuition is rising; and cost per student is increasing faster than inflation or family income.”
- Furthermore, at a time when the United States needs to be increasing the quality of learning outcomes and the economic value of a college education, there are disturbing signs that suggest higher education is moving in the opposite direction. Numerous recent studies suggest that today’s American college students are not really learning what they need to learn.

The Commission issued a series of sweeping recommendations to better align higher education with the needs of the nation, including

- 1) reaffirming America’s commitment to provide all students with the opportunity to pursue postsecondary education;
- 2) restructuring student financial aid programs to focus upon the needs of lower income and minority students;;
- 3) adopting a culture of continuous innovation and quality improvement in higher education;



- 4) greatly increasing investment in key strategic areas such as science, engineering, medicine, and other knowledge-intensive professions essential to global competitiveness;
- 5) ensuring that all citizens have access to high quality educational, learning, and training opportunities throughout their lives through a national strategy to provide lifelong learning opportunities at the postsecondary level, and
- 6) demanding transparency, accountability, and commitment to public purpose in the operation of our universities.

Actions have been launched by government and the higher education community at the federal and state levels to implement several of these recommendations over the next several years.

- Yet, because of the cacophony of criticism and speculation following the release of the Commission's report, it is also important to note here what were NOT included as recommendations: no standardized testing, no tuition price fixing, no national (federal) accreditation process, and no federalization of American higher education, which constitutionally remains the responsibility of the states and the private sector.
- But it is also not surprising that similar conclusions have been reached by groups at the state level such as the National Conference of State Legislators (NCSL, 2006), the State Higher Education Executive Officer's National Commission on Accountability in Higher Education (SHEEO, 2005), and the National Center for Policy and Higher Education's Measuring Up report cards (NCPHE, 2008).

- For example, the NCSL report begins with the premise: “There is a crisis in American higher education. It has crept up on us quickly. It has become clear that the states and the federal government have neglected their responsibilities to ensure a high-quality college education for all citizens. Too many students are falling through the cracks. As a result, U.S. citizens are not achieving their full potential, state economies are suffering, and the United States is less competitive in the global economy.”

## Economics

As we have noted earlier, aging populations are not likely to give higher education a priority for state tax dollars for perhaps a generation or longer.

- Hence even as states are depending more on their public universities—expanding access to underserved communities, achieving world-class performance in research and graduate studies key to regional economic competitiveness—state appropriations are declining while demands for higher efficiency and accountability are intensifying.
- “The inflation adjusted per FTE student expenditures by U.S. public higher education have been nearly flat for the last 20 years. Accordingly, tuition has substantially increased as a percentage of the total cost per student (revenue from tuition plus state appropriations).” (McPherson and Schulenberger, NASULGC)
- “In short, public higher education has lived with about constant revenues while being forced to deal with increased costs of technology, employee health care, student services, etc. This is why most universities

constantly feel the pressure to cut the cost of some activities despite tuition increases.”

But NASULGC also goes on to warn:

- “If the current decade-long trajectory of tuition and family incomes continue, lack of affordability could greatly limit both student choice and weaken institutions.
- The body politic in the years ahead will likely intervene before the affordability challenge places the possibility of earning a college degree beyond a significant proportion of the public.
- That political intervention could take the form of price controls, faculty workload mandates, uniform limitation of the maximum credit hours needed to earn a degree, forced reduction of the attention given to research, or some yet unimagined but perhaps even more potentially harmful intervention.
- The widely reported status of U.S. higher education as “best in the world” could be jeopardized by actions that threaten our universities’ independence and the diversity of their highly successful approaches to delivering higher education.

## Market Forces

Such geopolitical, demographic, and economic factors are stimulating powerful market forces that are likely to drive a massive restructuring of the higher education enterprise, similar to those experienced by other economic sectors such as banking, transportation, communications, and energy.

- We have been moving toward a revenue-driven, market-responsive higher education system because there is no way that our current tax system can support the degree of universal access to postsecondary education required by knowledge-driven economies in the face of other compelling social priorities (particularly the needs of the aging).
- This is amplified by an accelerating influence of the market on higher education and a growing willingness on the part of political leaders to use market forces as a means of restructuring higher education in order to increase the impact of the competition.
- Put another way, market forces are rapidly overwhelming public policy and public investment in determining the future course of higher education.

Yet the increasing dominance of market forces over public policy raises two important challenges.

- Whether a deliberate or involuntary response to the tightening fiscal constraints and changing priorities for public funds, the long standing recognition that higher education is a public good, benefiting all of our society, is eroding.
- Both the American public and its elected leaders increasingly view higher education as a private benefit that should be paid for by those who benefit most directly, namely the students.
- Without the constraints of public policy, earned and empowered by public investments, market forces could so dominate and reshape the higher education enterprise that many of the most important values and traditions of

the university could fall by the wayside, including its public purpose.

Higher education in America is intensely competitive in a marketplace for the best faculty members, the best students, resources from public and private sources, athletic supremacy, and reputation.

- This frequently ruthless competition poses a particularly serious threat to the nation's public research universities, particularly when the playing field becomes uneven due to public policies at the state and federal level that favor some institutions over others.

More specifically, today most public research universities find themselves caught between the rock of declining state support and the hard-place of the predatory practices of rich private universities.

- Aging populations are not likely to give higher education a priority for state tax dollars for perhaps a generation or longer.
- Hence, even as states are depending more on their public universities—expanding access to underserved communities, achieving world-class performance in research and graduate studies key to regional economic competitiveness—state appropriations are declining while demands for higher efficiency and accountability are intensifying.

In sharp contrast, due both to booming financial markets and favorable federal financial aid and tax policies, many private universities have managed to build endowments so large (at least on a per student basis) that they have become essentially

independent of the traditional revenue streams supporting higher education, e.g., student tuition, R&D grants, even private giving.

- For example over the past several months we have seen a few of the rich and famous universities propose to use their massive endowments for broader purposes such as reducing costs to the middle class (here it is hard to understand how a \$180 K family income is 'middle-class, although perhaps it is to some elite institutions), creating more faculty lines, building more buildings, and so on.
- But there is something important happening here, besides Senator Grassley waving his sword threatening to tax endowment earnings or at least require higher payouts for educational purposes. Roughly a dozen private universities have now managed to build endowments so large, at least on a student basis, that they have become independent of the education marketplace (e.g., student tuition, R&D grants, even private support).
- When an institution makes several times as much from investments as from any other revenue stream, it begins to behave more like a bank than an educational institution.
- While several of the public universities are also building significant endowments, their size on a per-student basis pales in comparison with those amassed by the elite private universities. This has created a serious competitive imbalance for the best faculty, the top students, and resources such as gifts, grants, and federal largesse. The wealth gap between the rich privates and flagship publics is getting larger and larger.

As an article in Business Week last spring put it:

- “The fabulous prosperity of America’s top tier of private universities is defined by the great magnitude of their wealth relative to their modest size and to the rest of the higher education universe. The gilding of the Ivies offers a striking manifestation of the contemporary American tendency of the rich to get much richer and casts into sharp relief the travails of America’s public institutions of higher learning, which educate 75% of the country’s college students.
- While the Ivies, which account for less than 1% of the total, lift their spending into the stratosphere, many public colleges and universities are struggling to cope with rising enrollments when most states are devoting a dwindling share of their budgets to higher education. It is unlikely that more money has ever been lavished on the education of so few.”
- “The Ivy’s cannot fairly be blamed for public education’s financial predicament, but they certainly are exploiting it. Even the most prestigious of public universities are increasingly hard-pressed to repulse richly financed, Ivy Plus raiding sorties seeking to steal distinguished faculty members and their research grants.
- Ivy administrators argue that gathering the best researchers in resource-rich havens has a synergistic and broadly beneficial effect. It has even been suggested that as lesser (i.e., public) universities lose market share, they would be wise to really emphasize social science or humanities and have science endeavors that are not as ambitious as the elite private institutions.

“For better or worse, the infusion of riches at the Ivy Plus schools has dramatically extended their lead over everyone else,

especially the public colleges and universities that collectively serve the vast majority of American students.

- This dominance—and the inequities that it fosters—are likely only to grow.
- Hence, the public policy issue: *Is this concentration of financial, faculty, and student resources in a small number of wealthy private institutions, in part at the expense of the flagship public universities, in the national interest.*"

This creates a serious competitive imbalance in the marketplace for talented faculty, outstanding students, and public and private resources, since the wealth gap between the rich privates and flagship publics is growing ever larger. This is aggravated by the political constraints on public universities that not only limit their flexibility and agility, but also hinder their capacity to compete (e.g., constraints on tuition, affirmative action, technology transfer, and globalization).

There is growing concern about the degree to which current federal policies (e.g., tax policy, financial aid policies, tuition constraints, sponsored research policies) preferentially favor private higher education.



So...What to do?

Premises

- One of the great strengths of American higher education is the presence of a system of world-class public and private research universities, sustained by public policies that ensure sufficient balance in financial assets, flexibility, and quality to serve the diverse needs of the nation.
- Both public and private universities have an obligation to serve the public purpose and meet the needs of the nation, since all benefit from public support, and while characterized by different legal status and governance, are in fact public bodies.
- State funding of public higher education is likely to decline over the next several decades as aging populations give highest priority for public tax dollars to health care, retirement security, and tax relief rather than investments in education.
- It is essential that federal and state policies in areas such as tax benefits, student financial aid, research funding, and regulation sustain quality, diversity, and balance in America's higher education system rather than threaten competitive balance and drive predatory behavior.

Policy Issues

- How best can the United States achieve and preserve the competitive balance between public and private research universities necessary to address the diverse needs of the nation? How do federal policies in areas such as taxation,

student financial aid, research support, and regulation affect this competitive balance?

- The flagship public research universities represent an asset of immense importance to the nation. How can the federal government best protect these assets, a key element of its intellectual infrastructure, during an era in which the states responsible for and dependent upon these institutions no longer have the capacity or the will to adequately support them?

## What Might Be Done?

### At the Federal Level

- A 21<sup>st</sup> century analog to Land Grant Acts designed to sustain the quality of flagship public universities during a period when state resources are dominated by the priorities of an aging population rather than investment in education. (For example, using revenue from the auctions of the digital spectrum, much like the sale of federal lands in the 19<sup>th</sup> century.)
- Incentives to states to explore restructuring public higher education to better enable institutions to serve both state and national needs during a period of limited state resources.
- A modification of those federal policies that preferentially advantage a particular element of the research university system (public or private) and enable predatory practices.
- Although controversial, it may be time to raise the issues about the equity and public value of federal tax policies that while benefiting higher education also can drive serious inequities, including the treatment of charitable

giving, endowment earnings, and unrelated business income (e.g., intercollegiate athletics).

To be more specific, tax policy at the state and federal level provide substantial subsidies of higher education through the foregone tax revenues arising from the treatment of university gifts, certain unrelated business income (think football seat taxes and skybox leases), and endowment earnings as charitable gifts and nontaxable income, respectively.

- To be more specific, when a university receives gifts that are deducted as charitable contributions, other taxpayers subsidize in effect these foregone tax revenues.
- Similarly, the nonprofit nature of endowment earnings also makes them exempt from the taxes that would apply to for-profit company revenues.
- It is estimated that foregone tax revenues or “tax expenditures” from charitable gifts and endowment earnings amount to roughly \$16 B per year (assuming an average 30% tax rate on the \$25 B of gifts and \$27 B of endowment earnings), which amounts to a federal government subsidy of as much as \$50,000 per student at well-endowed private colleges and universities, leading to the ironic situation that when all support, public and private, is accounted for, several of these institutions are among the most “publicly supported” universities in the nation.
- Of course, one can make a strong case for the appropriateness of some degree of public support of private higher education. Yet these “tax expenditures”, while very real and perhaps appropriate burdens on state and federal tax revenues, are rarely included in the total picture of cost, price, and value of a college education,

although they would significantly modify the true costs and public subsidy picture of American higher education.

- Furthermore, their existence raises the serious policy issue as to which is more in the public interest: Subsidizing the education of rich kids at rich institutions at \$50,000 each, or using these funds to provide Pell Grants to ten poor kids to enable their education at public colleges and universities!”

(NOTE: This issue was placed on the table at one of the meetings of the Spellings Commission, to be quickly swept aside by representatives from private universities...)

#### At the State Level

- To launch major public awareness campaigns aimed at persuading voters about the importance of investing in higher education and stimulating efforts to restore funding adequate to sustain world-class public research universities while meeting the growing needs for post-secondary education as a key to economic prosperity and social well being.
- To encourage experimentation in creating a more differentiated higher education structure that better aligns the balance between autonomy and accountability with the unique missions of research universities (a la Virginia).
- To dramatically improve the quality of governance of public universities, streamlining state regulation and constraints and improving the quality of those appointed to university governing boards.

#### At the Institution Level

- Encourage and enable public research universities to develop and implement strategies to survive what could be a generation-long period of inadequate state support with their capacity, quality, and reputation intact.
- Seek a cultural change in the predatory behavior of wealthy universities, throttling back the incentives for raids for faculty, students, and resources (e.g., discouraging deans from raiding faculty from less fortunate institutions with exorbitant offers and instead focus them on internal faculty development).
- (And if necessary to get private university leaders to the table...) Use the political clout of the public universities to seek a modification in federal tax policy that removes the current advantages benefiting wealthy private institutions (e.g., tax endowment earnings, require a litmus test of charitable contributions, more rigorously evaluate unrelated business income) (e.g., threaten nuclear retaliation if wealthy institutions continue their predatory practices...)

# A Final Observation

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At one of our discussions of these issues among university leaders, one of our well-known colleagues from a well-known private university put it this way:

- If Harvard were to disappear tomorrow, there would be several private universities that could move rapidly to fill this hole.
- But if a couple of decades from now we were to find universities such as universities such as California, Michigan, Wisconsin, North Carolina, and Texas were no longer world-class, the nation would be in very big trouble indeed.

Hence our challenge today: To find ways to ensure that the nation's public research universities remain world-class during the next several decades!!!

So...how can we help?

- At the National Academy level?
- At One Dupont Circle?
- Through groups like the American Academy of Arts & Sciences
- Through our own institutions

What would be most helpful to you?