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ADMISSIONS, FINANCIAL AID, AND DEVELOPMENT POLICIES

by

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Would that academic institutions were simple organizations. If they were, the determination of what is considered ethical behavior in academic decision making probably would be clear cut. However, I will argue today, using admissions, financial aid, and development policies as examples, that what is ethical behavior may not be as clear cut as casual observers might think. And, whether behavior is judged ethical in one dimension of an institution's activities may well depend upon how decisions in this sphere interact with other uses of resources at the institution and what the institution's competitors are doing.

Admissions and Financial Aid Policies

For years the 'gold standard' in private academic institutions' admissions and financial aid policies has been to admit students without considering the financial need of applicants (need blind) and then to fully meet the financial need of all accepted applicants through a combination of grants, loan, and employment opportunities (need-based aid). Today only a handful of private institutions are both need blind in admissions and pursue need-based financial aid policies; these tend to be among our nation's most selective and wealthiest private institutions.

Why do they pursue such policies? In part it is because as nonprofits they are major beneficiaries of federal and state policies that reduce the federal and state income taxes that their donors pay and eliminate any taxation of their endowment earnings, provide exemptions for the institutions from paying local property taxes on their buildings that are used for educational purposes, and allow them to borrow funds to construct educational facilities at lower tax-exempt interest rates. Because of all of these tax benefits, the public at large is subsidizing these institutions to the tunes of literally billions of dollars of lost tax revenue a year. The public's willingness to do so is presumably based upon the belief that the selective private academic institutions are yielding benefits to society as a whole.

Because many of our nation's leaders are graduates of these institutions and a well-functioning democratic society requires that its leaders come from diverse socioeconomic backgrounds, these institutions have long understood that they have a special obligation to admit and enroll students from all socioeconomic backgrounds. More recently as attention has been placed on the role of a college education in providing earnings gains for graduates and some research by economists has shown that the

graduates of selective private institutions, especially those coming from families with relatively low family incomes, get an extra leg up in the labor market, this has provided an additional reason for the institutions to be concerned about the economic diversity of their student bodies.¹

In spite of their policies, at the turn of the 21st century, many of these institutions were enrolling relatively few students from families with modest financial backgrounds, as measured by the share of their students receiving Pell Grants. Substantial growth in their endowments during the 1990s allowed the richest institutions to reduce the loan components of their aid packages and the other selective privates followed to the best of their abilities. In 2007-08, pressure from the U.S Senate Finance Committee, which was concerned that the private institutions were not devoting enough of their resources to enrolling Pell Grant recipients, led the institutions to further improve their financial aid policies, with the wealthiest eliminating all loans from their aid packages. The other selective privates again followed to the best of their abilities eliminating loans for students whose families whose incomes, depending upon the institution, were either below \$60,000 or \$75,000 a year, as well as reducing loan burdens for other students. These policy changes led, on balance, to an increase in the share of students attending selective private institutions who were Pell Grant recipients.

But in 2008-09, the financial collapse and Great Recession that followed began to wreak havoc with the institutions' budgets. Declines in endowment and annual giving substantially reduced their revenues. Declines in family incomes and assets (including housing values) led to substantial increases in the financial need of their entering classes. Financial aid budgets exploded putting pressure on the institutions' funds available for educational purposes.

A number of institutions responded by modestly increasing annual loan limits for students whose family incomes were above some threshold. In doing so they sought to guarantee access to students with the greatest financial need. Wesleyan University, whose financial resources were more

¹ For example, Dominic J. Brewer, Eric R. Eide, and Ronald G. Ehrenberg, "Does it Pay to Attend an Elite Private College? Cross-Cohort Evidence on the Effects of College Type on Earnings", *Journal of Human Resources* 34 (Winter 1999) provide evidence that graduating from a selective private institution leads to higher earnings than graduating from other institutions. In contrast Stacy Berg Dale and Alan B. Krueger, "Estimating the Payoff to Attending a More Selective College: An Application of Selection on Observables and Unobservables", *Quarterly Journal of Economics* 117 (November 2002) find no such higher earnings gains on average, but they do find earnings gains for students from families with lower incomes.

limited than some of its competitors made a dramatic announcement in June 2010, that until it could raise enough new endowment to substantially increase its financial aid budget, it would admit the last share of its students (perhaps 10 percent in the following year) by only considering for admission applicants who did not need grant aid from the institution. That is, at least temporarily, it moved away from the full need blind admissions policy. Was this ethically the wrong thing to do?

I strongly believe that Wesleyan courageously faced a moral dilemma. Its increasing financial aid budget was seriously impacting on the resources it had available to provide a quality undergraduate education. Making decisions on the nature of financial aid policies cannot be made independent of their resource implications for the rest of the institution.

Given the constraint on its resources, continuing to make admissions decisions without considering at least some applicants' financial need would have required Wesleyan to increase loan limits in its financial aid packages to levels that might cause it to lose more accepted applicants to competitors. It would also likely restricts its financial aid recipients' choice of majors and post-college career options.²

Instead, it decided to bite the bullet in the short-run and admit only "full-paying" applicants once it exhausted the funds it had earmarked for grant aid. That meant in the short-run it reported share of Pell Grant recipients among its student body might well decline and that it would appear to the outside world to be backing away from its social obligation to enroll an economically diverse student body.

Of course it could have continued to make all of its admissions decisions need-blind and to admit the final group of students without providing any grant aid to them (admit-deny). It could have counseled these admitted students who had substantial financial need about the large loan burdens they would have to assume to attend the university and try to dissuade them from attending.

² Jesse Rothstein and Cecilia Rouse, "Constrained After College: Student Loan and Early-Career Occupational Choice", *Journal of Public Economics* 95 (February 2011) provide evidence that after a selective private university eliminated all loans from its financial aid packages it found that more of its graduates choose lower-paying "public interest" jobs, at least temporarily, after graduation.

However, this would have placed the institution in a position of rooting against itself; first admit the students, then try to convince them not to enroll, and if the institution's exhortations worked, then try to find more applicants to fill the unfilled seats in their class. And if the original admitted students with large loans did enroll, Wesleyan would have to worry that these students' accumulating debt burdens would reduce their chances of successfully completing their degrees and/or would limit their career options after graduation. Students talented enough to be admitted to Wesleyan surely will be attractive to other selective institutions and the small number of students with financial need who Wesleyan would have accepted under its previous policies should have enrollment options at other selective institutions.

Of course what is an ethically correct policy for an institution to pursue in a social sense depends upon what its competitors are doing. If all selective private colleges and universities adopted Wesleyan's strategy, enrollment of students from families with relatively modest financial means would most likely fall at these institutions as a group. To the extent that attendance at these institutions does confer additional lifetime economic and noneconomic benefits to such students, one should probably conclude that in such a circumstance, each institution's decision was not ethically correct.

A quick postscript: Now several years after the change in Wesleyan's policy, Wesleyan has received substantial endowment contributions for financial aid, including several gifts from its president. It has not gone back to a full need blind admissions policy and the share of its class admitted based on ability to pay has remained about 10 percent. However, it is spending more on financial aid than it did before the policy change and it has used its increased financial aid budget to provide better grant packages for its neediest applicants. Its goal in the future is to provide better packages for its middle-income applicants as well. Its enhanced grant aid packages for its neediest applicants, as well as its making submission of entrance exam test scores optional as of 2014-15, has allowed it to mitigate the negative effect of its new admissions policy on the share of Pell Grant recipients in its entering class. This share has fluctuated in recent years around 18 percent.³ *U.S. News & World Report's* web page listing of selective liberal arts

³ Private email correspondence from Wesleyan President Michael Roth (November 9, 2016). Kate Carlisle, "Wesleyan Makes Tests Optional in Admissions", *News@Wesleyan* (November 7, 2014). Lauren Rubenstein, "President Roth and Professor Weil Make Second Major Campaign Gift", *News@Wesleyan* (November 22, 2014)

colleges indicated Wesleyan was ranked 8th in the nation in terms of its share of Pell Grant recipients in 2014-15.

Development Policies

Many selective private academic institutions have both large endowments and large flows of annual contributions. While policy makers often complain that these institutions are not spending enough from their endowments on undergraduate financial aid, endowment funds are typically not a large pool of unrestricted assets. Rather the conditions under which they were granted to the university often restrict their use to very specific purposes. Only at the very wealthiest private institutions, places like Harvard, Yale and Princeton, do most dollars for undergraduate financial aid come from the endowment. At my own institution, whose endowment currently is in the six billion dollar range, around 80 percent of undergraduate grant aid dollars come from the unrestricted general operating budget, which is largely funded by undergraduate tuition dollars.

Senior leaders and development professionals at academic institutions work hard to raise substantial sums of new contributions each year. Some will create new endowment, some will be used for capital purposes, and some will go into the general operating budget of the university. Senior leaders and development professionals are concerned with the total level of giving they receive, how the giving is allocated across the three uses, and the purposes for which the funds are received. Potential donors often have strong preferences for the types of things they would like to see done with their funds and the institutions work hard to match donors' interests with the needs of the institutions.

Most large gifts come with the possibility of naming opportunities and depending upon the level of the gift these naming opportunities may be for buildings or parts of buildings, for named professorships, or for undergraduate financial aid. Many academic institutions have received donations to endow individual undergraduate scholarships. However, most have found that their really large donors, those with the financial capacity to make gifts at the eight figure or higher category, prefer to have their names on buildings or to support major new academic programs, rather than creating a named large endowment to support multiple undergraduate grant scholarships. Of course there have been a few exceptions.

But having said this, even if a gift is for a very different restrictive purpose, it may have the effect of freeing up institutional funds that can then be used for undergraduate financial aid. For example, a university may encourage donors to provide funding for named professorships that will largely go to existing faculty members to help ward off attempts by other institutions to hire star faculty. These professorships would presumably provide faculty members with higher salary levels and more research support than they otherwise would have received from the institutions.

To the extent that these professorships provide funds that cover all or most of the higher salaries of the faculty members and the institutions does not increase the size of its faculty, the funds that it otherwise would have spent on the newly named professors are freed up to be redirected to other uses, including increasing undergraduate grant aid from the unrestricted operating budget of the university. Critics who claim the university has not behaved in an ethical matter because it is not doing enough to raise endowments for undergraduate student grant aid miss a key point. Institutions must respond to donor preferences for giving, but try to shape the donation agreement in a way that allows the institution flexibility in the actual use of the donated funds.

I conclude with a personal story. To help celebrate our 50th wedding anniversary in June, my wife and I are providing a “substantial” gift to the public university from which we both received our bachelor’s degree. I hasten to add that what is considered a substantial gift at a relatively young and poorly-endowed public university is much smaller than what is considered a substantial gift at a well-endowed private institution. We had previously created an endowed scholarship at our alma mater to honor my parents; it was much cheaper for us to do so there than it would have been at a selective private institution because the public institution’s tuition is much lower.

In gratitude for our proposed new gift, the public institution is placing our names prominently in a room in an academic building that was paid for by state funds. We had planned to endow another scholarship at the institution but in return for making a somewhat larger gift, the university agreed to name this room after us. In theory, if the use of funds was not restricted in the agreement, because the building had already been paid for, the institution could have used our funds to endow more than one undergraduate scholarship.

However, a higher priority of the president of the institution is to build an endowment from multiple donors to create a flow of funds that can be used to help support the research of young recently tenured faculty members. He hopes that these funds will help these faculty members understand how much the institution values them and help the institution ward off raids from wealthier private universities on these faculty. Once our gift is received and the room named for us, the university can show the room to other alumni and explain to them how they can have rooms named after them if they also contribute to this fund.

Is the president behaving in an ethical manner by emphasizing the need for funds for faculty research support rather than for undergraduate financial aid, which the institution very much also needs? The quality of an undergraduate education depends upon the quality of the faculty and administrators need to decide whether more financial aid dollars or a higher quality faculty will benefit undergraduate students the most. Our agreeing to make the larger gift implies we believe his decision was correct.