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A Risky Investment Strategy: Recent Trends in Federal Financial Aid Policy Do Not Meet the Needs of Low-Income Students

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A RISKY INVESTMENT STRATEGY

Recent Trends in Federal Financial Aid Policy Do Not Meet the Needs of Low-Income Students

Joint Economic Committee, Democratic Staff

Since the passage of the GI Bill in 1944, which allowed thousands of returning veterans to attend college, the federal government has made a significant investment in higher education – primarily through the provision of direct financial aid to students. In the 2000 – 2001 school year, the federal government dispensed \$50 billion in aid. As a nation, we have reaped the rewards of this investment: a highly skilled workforce; enhanced productivity and economic growth; and higher wages for college graduates.

Over the last fifty years, the number of students pursuing postsecondary education has grown seven-fold to almost 15 million.¹ The demand for highly educated and skilled workers will only continue to grow in the future. Most of the fast growing professions – such as health care and computer science – require at least a bachelor's degree. Jobs that require some type of postsecondary certification (a vocational award or higher) are expected to have faster-than-average employment growth in the coming decade and account for about 42 percent of total job growth from 2000 to 2010.²

Recent economic and financial aid policy trends, however, may keep many young people from being able to pursue higher education at a time when the nation most needs it. The problem is particularly acute for low-income students. Since the early 1970's, average tuition and fees at four-year public universities have more than doubled (in constant 2000 dollars).³ For households making \$25,000 a year, annual tuition and living expenses at a public university would consume almost half of their annual income. These prohibitive costs are part of the reason that low-income high school graduates enroll in college at a consistently lower rate than their higher-income peers.

Federal financial aid has not kept pace with rising costs. The Higher Education Act of 1965 outlined a federal commitment to give equal access to college for all students. It created the programs that have become the cornerstone of federal assistance – need-based aid, guaranteed student loans and work-study. Traditionally, this aid has been targeted toward the most risk-averse and cash constrained students. However, recent policy decisions have devoted a growing share of federal financial aid resources to middle- and upper-income students, primarily through the growth of the student loan program, tax credits and other tax incentives. At the same time, Pell

Grants for low-income students have declined in purchasing power over the last 25 years.

To meet the future demands of our increasingly technological and skill-based labor market, we need to continue to invest in higher education and increase the number of people with access to postsecondary education and training. Federal financial assistance for students who already have sufficient resources to afford college does little to increase the number of highly educated workers. The most efficient and effective use of federal dollars would be to concentrate them on those students who cannot otherwise afford postsecondary education.

I. Investing in Higher Education

Federal investment in higher education generates economic benefits in several ways:

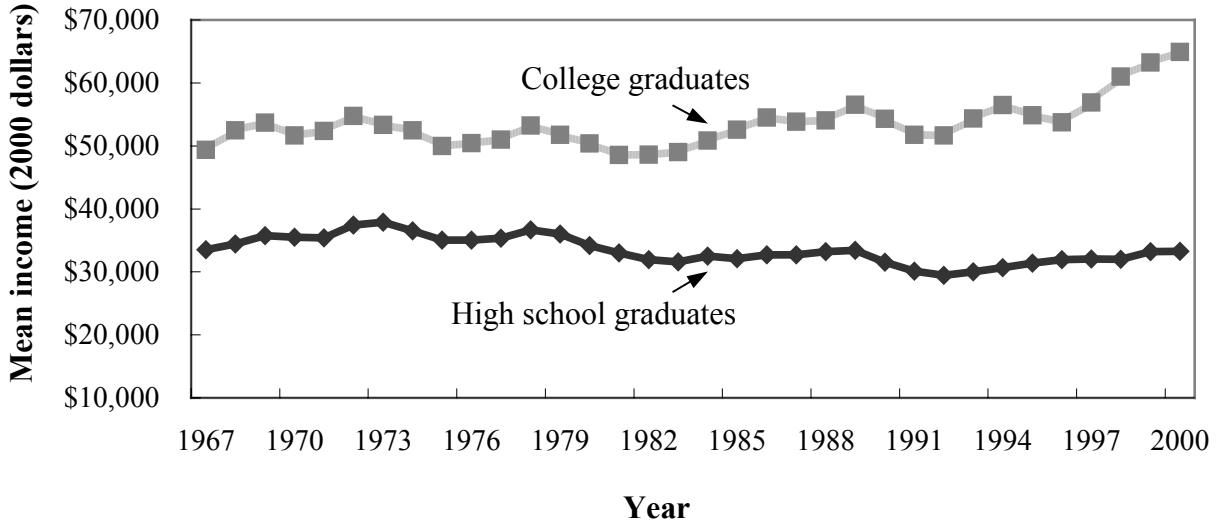
- **Meeting the Demand for a Highly Skilled Workforce.** More and more jobs in our economy require technological or specialized training. The need for workers with postsecondary training is expected to increase at a faster rate than the need for low-skill workers in the coming decade. According to estimates by the Bureau of Labor Statistics, almost a third of the growth in employment from 2000 to 2010 is expected to occur in occupations that require at least a bachelor's degree. Two of the fastest growing fields – computer science and health care – require at least a college education. Another 13 percent of job growth is expected to occur in fields that require an associate's degree or postsecondary vocational training, such as medical assistants and computer support specialists. These high-skill jobs also typically pay wages significantly above the average for all workers. Low-skill jobs are predicted to account for a larger share of employment growth. But most of these positions, such as food preparation, pay very low wages.⁴
- **Enhancing Productivity.** A key to long-term economic growth is an increasingly productive labor force. Workers become more productive both by having new and better equipment with which to work, and by acquiring new skills and knowledge. Improvements in labor force skills and “improvements in knowledge” account for a significant part of economic growth. Several researchers conclude that education alone accounts for about 15 to 20 percent of the growth in national income, with about a quarter of that stemming from higher education.⁵
- **Expanding the Labor Force.** Individuals with higher levels of education are more likely to be in the labor force. About 80 percent of adults with a bachelor's

degree or higher were labor force participants in 2000. However, less than half of adults without a high school diploma were working or actively seeking work.⁶ College educated workers are also less likely to be unemployed. In 2000, the unemployment rate for workers with a bachelor's degree was only 1.8 percent, according to the Bureau of Labor Statistics. High school graduates, however, had an unemployment rate that was almost twice as high. This holds true even during a recession. During the 1990 – 1991 recession, the March 1991 unemployment rate for high school graduates (6.7 percent) was more than twice as high as that of college graduates (2.9 percent).

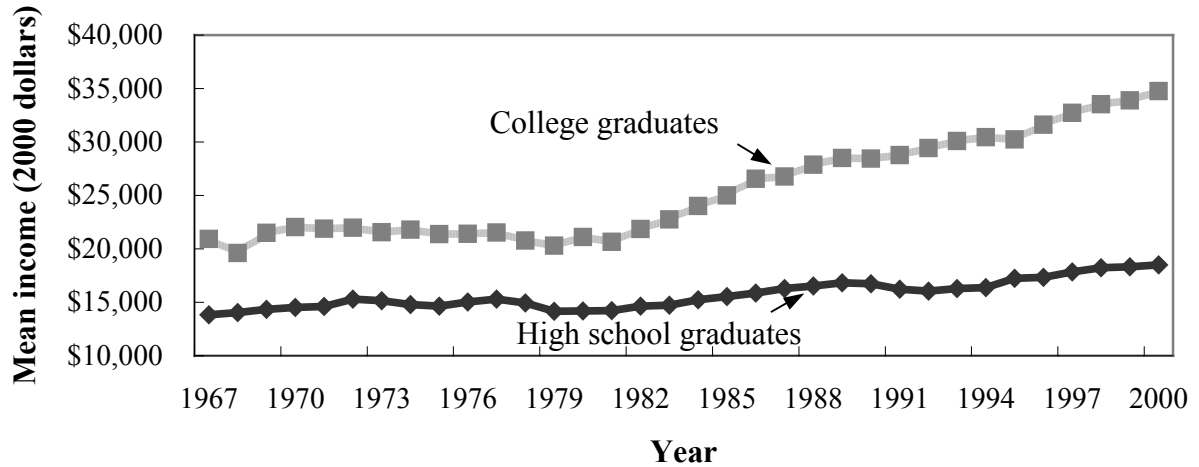
- **Increasing Wages.** College graduates have always earned more, on average, than those with less education. Since the 1980s, however, college graduates have experienced a much faster growth in average income than high school graduates. The gap widened during the economic boom of the 1990s. In 2000, the average income for a man with a college education was almost double that of a man with a high school diploma. Women with a college education had an average income that was almost 90 percent greater than women with a high school degree (see Graph 1). With higher wages, families have less need for social services and more disposable income to increase consumption.

Graph 1

Mean Income by Education Level for Men, 1967 - 2000 (2000 dollars)



Mean Income by Education Level for Women, 1967 - 2000 (2000 dollars)

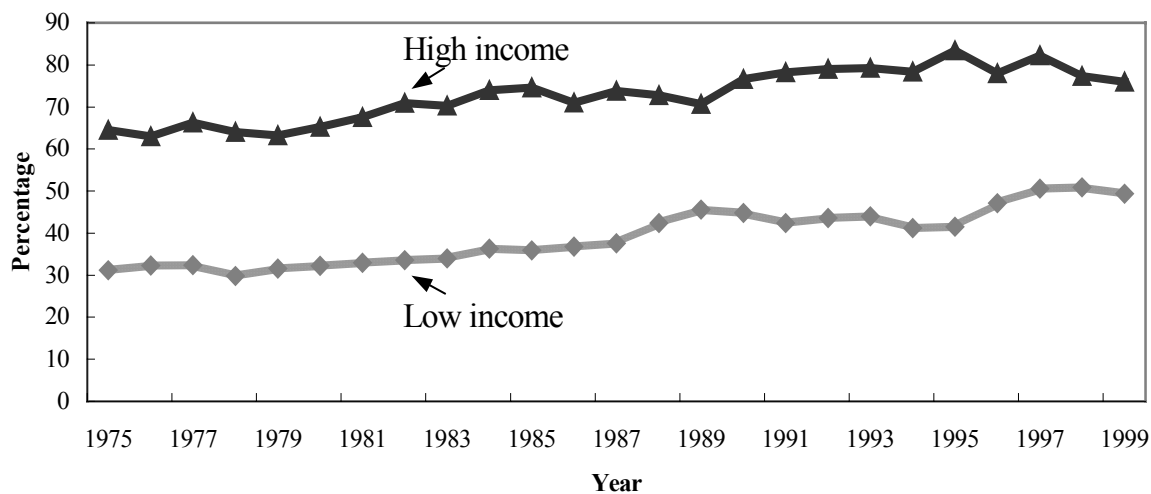


Source: Bureau of the Census, U.S. Department of Commerce

Inequities Persist

Despite the availability of federal student aid, there is still a persistent income gap in college attendance and completion. Low-income students are less likely to enroll and stay in college than high-income students. Every year for the last 25 years, less than half of high school graduates from families in the lowest income quintile proceed to college directly compared with more than three-quarters of students in the highest income quintile (See Graph 2).

Graph 2. Percentage of High School Graduates Enrolled in College by October after Completing High School 1975 - 1999



Source: U.S. Department of Education, *The Condition of Education*, 2001.

In the 1999 – 2000 academic year, only 13.3 percent of financially dependent undergraduates came from families with incomes less than \$20,000. Compared to higher income students, they were more likely to be members of a minority group and have parents with only a high school education or less.⁷

Lack of adequate academic preparation appears to account for only a portion of this difference in enrollment. Students from low-income families are more likely to attend lower-quality public schools and may not be as well prepared to enter college. But even when we look at those with adequate preparation, the gap persists. A study of academically qualified 1992 high school graduates found that only about half of

the students from families who made less than \$25,000 a year (1992 dollars) enrolled in a four-year college, compared with more than 80 percent of students from families that made \$75,000 or more (1992 dollars). If we narrow our focus to the most academically prepared students – who would likely have the greatest motivation to go to college – the income gap is just as large. Among students with the highest standardized test scores, only 58 percent of students from families in the lowest income quartile enrolled in college within two years compared with 86 percent of students from families in the highest income quartile.⁸

Despite the clear advantages to both the individual and society, some academically prepared students may not pursue higher education because of the high cost. Given the higher average wages for college graduates, students without enough cash on hand should be able to borrow against future earnings. But evidence suggests that students are much more sensitive to the high direct costs of going to college than the prospect of future income.⁹ A high degree of uncertainty surrounds the investment in higher education. There is no guarantee that students will complete their degrees. There is no guarantee of their future salary level. This uncertainty can make individuals less willing to take out loans. This is particularly true for low-income and minority students who may be more financially risk-averse than their wealthier peers.

Without a well-educated workforce, productivity and the economy could suffer. The federal government intervenes in the form of grants and guaranteed loans to help lower the cost of education and provide the means for people to pursue a college degree.

The Rising Cost of a College Education

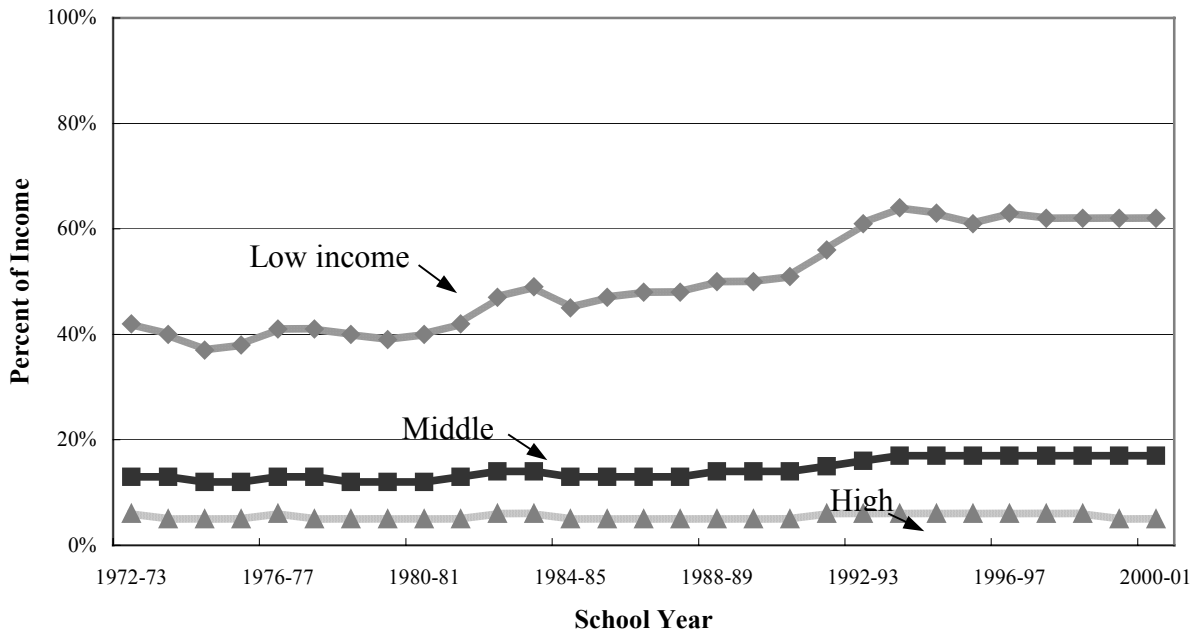
Low-income families have been hardest hit by the skyrocketing increases in college tuition over the last twenty years. Since the 1980s, average tuition has risen at twice the rate of inflation. For families in the top income quintile, the cost of college has remained steady at five to six percent of income because those families enjoyed rapid income growth over the same period.

But for families in the lowest income quintile, who earned an average of \$10,190 in 2000, the cost of college as a percentage of income has risen dramatically. In 2000–2001, the average public university cost would have consumed about 62 percent of income for these families. Adding books, transportation and other

expenses pushes the in-state cost of one year at a four-year public university even higher. The full cost is more than the mean income of families in the lowest income quintile and almost half the income of families in the next quintile. The cost of a private university was even more staggering — 166 percent of income.¹⁰

The situation is poised to become worse in the coming academic year. Historically, public university tuition increases are counter-cyclical — increasing when unemployment rates are rising.¹¹ With the recent economic downturn, several states have already announced double-digit increases in tuition. In Washington, the legislature is considering a 16 percent increase in in-state tuition to make up for a \$54 million cut in state university budgets. The University of Kansas may double the price of tuition over the next five years. To meet these costs, lower income students need substantial financial aid.

Cost of Attendance at a Public University as a Percentage of Income, 1972 - 2000



SOURCE: College Board, *Trends in College Pricing*, 2000.

II. Financial Aid Trends

The federal government is by far the largest provider of direct financial aid to students enrolled in postsecondary education and training. In the 2000 - 2001 school year, almost 70 percent of all direct student aid – about \$50 billion – came from federal sources. The amount of federal dollars devoted to student aid has grown by more than 80 percent over the last decade. In addition to direct aid, the government also provides funding to universities and colleges to help make college more affordable.¹²

Federal financial aid policy has gradually been moving away from its primary focus and commitment to helping the most financially needy students afford a college education. The share of federal need-based aid has dropped from 80 to 60 percent of all federal student aid over the last twenty years.¹³ Policy decisions about how much aid to offer and how to deliver the aid to students has meant that a much greater share of financial aid dollars is going to middle- and upper-income students.

Unsubsidized student loans, tax credits and other tax incentives have replaced grants as the primary vehicle for delivering federal financial aid. None is efficient at targeting low-income students. Loans are not an appealing option to low-income students who are likely to be financially risk-averse. Students cannot take advantage of non-refundable tax credits or deductions if they do not have any income tax liability. Tax-advantaged college savings accounts offer little help to families with limited disposable income.

Shift to Loans

Over the last twenty years, federal financial aid has shifted from a system based predominantly on grants to one based on loans. In 2000, roughly two-thirds of federal student aid was in the form of loans.¹⁴ Twenty years ago, however, loans made up only about 40 percent of federal aid to students. Over the last decade, the amount of loan aid has increased by more than 135 percent.¹⁵

Loan aid has increased primarily due to the creation of unsubsidized Stafford loans in 1992. Unlike subsidized loans aimed at lower-income students, these loans are open to all students regardless of income. At the same time, Congress increased the maximum loan amount. Today, almost half of all federal education loans — \$18 billion in 2001 — are unsubsidized loans to students or parents. The majority of these federal aid dollars are going to middle- and upper-income students. In 1999,

more than 80 percent of unsubsidized loans were to students with family incomes greater than \$40,000.

While the creation of unsubsidized loans has helped middle- and upper-income students with college costs, the availability of loans is less likely to induce students from low-income families to enroll in higher education. Most of these students cannot rely on their parents to help them financially either during or after college. A great many of them may be the first generation in their family to go to college. Low-income and minority students may have a greater level of uncertainty about their future earnings and they are more likely to be financially risk-averse. As a result, the availability of funds for school in the form of loans is not sufficient to make them think seriously about pursuing postsecondary education and training. Grants do not carry the same sort of financial risk for the student. Low-income and minority students are more likely to respond to grant aid rather than loans.¹⁶

Shift to Tax Credits and Deductions

With the introduction of the HOPE and Lifetime Learning credits in 1997, more financial aid is being delivered through the tax code. The Economic Growth and Tax Relief Reconciliation Act of 2001 expanded existing tax incentives, such as eliminating the federal income tax on withdrawals from state college tuition savings plans. It also created an above-the-line deduction for higher education expenses. [See box for descriptions of tax credits and incentives.] (The Act also included other higher education tax incentives – such as student loan deductions and loan forgiveness. This paper concentrates on tax provisions designed to help students pay tuition while they are in school.) Overall, the Joint Committee on Taxation estimates that these higher education tax credits and deductions will cost \$8 billion in FY 2002.¹⁷

Tax Credits and Tax Deductions

A tax credit is used to reduce an individual's income tax liability. The recipient generally must complete an income tax return to get the credit. If the credit is refundable, amounts in excess of a filer's tax liability are paid to the individual. The value of a tax credit is the same for all income levels.

A tax deduction reduces an individual's taxable income. Unlike a tax credit, a tax deduction increases in value for filers in higher tax brackets.

While tax credits, deductions and incentives help ease the financial burden of college for middle- and upper- income students, they have almost no impact on low-income students. For the most part, financial assistance delivered through the tax code is

inaccessible to low-income students, it does not meet their funding needs and it does not offer them the same amount of benefits as it does for higher-income students.

Financial aid delivered through the tax system is relatively inaccessible to low-income students for several reasons:

- **In order to claim one of the tax credits or the deduction, families must have income tax liability.** Students from families with incomes too low to incur taxes are not able to get any benefits. Families with low tax liability (less than the maximum amount of the credit) will have the value of the credit reduced so it does not exceed their tax liability. This means that the poorest students are ineligible for the HOPE and Lifetime Learning credits and the higher education deduction. Income tax data from 1999 show that less than 20 percent of filers who claimed a HOPE or Lifetime Learning credit had incomes below \$20,000 while almost 40 percent had incomes between \$50,000 – \$100,000.¹⁸

If existing higher education tax credits were made refundable, they would be more accessible to low-income students. With a refundable credit, students with no tax liability would be eligible for the credit and students with low tax liability would not have their credit reduced. However, students would still have to file a federal income tax return – even if they do not owe income taxes – in order to get the credit. This step adds another layer of complexity to the federal financial aid process.

- **Low-income families are less likely to have sufficient disposable income to take advantage of the new tax incentives for savings.** The new tax changes raise the contribution limit on Coverdell accounts from \$500 to \$2,000 annually. Families can also now make contributions to both a Coverdell account and a state tuition savings plan in the same year. These changes may increase the amount of saving in middle- and upper-income families. However, low-income families are much less likely to have the funds necessary to make these investments over time so they cannot reap any benefits from these tax incentives.

Tax incentives deliver the greatest benefits to those with the highest incomes:

- **The amount of the credit or deduction is reduced by other financial assistance.** The credits or deduction can only be applied toward money spent by the student on tuition and fees. Any scholarship or grant funds reduce the amount of award. To receive the maximum credit, students must have at least

\$2,000 in tuition and fees. As a result, low-income students who receive a Pell Grant or attend a lower cost college are probably not eligible for the maximum credit or deduction. In 1999, income tax data show that the average amount received by high-income filers who claimed a HOPE or Lifetime Learning Credit was almost twice as much as the average for the lowest-income filers who received a credit.¹⁹

- **The value of a tax deduction increases with income.** Families in higher tax brackets get a larger benefit from the higher education tax deduction than those in lower tax brackets. For example, a family in the 15 percent tax bracket would save \$15 by deducting \$100 in qualified higher education expenses. A family in the 27 percent bracket would save \$27. Families with no income tax liability would not be able to take the deduction at all.²⁰ This means that tax deductions disproportionately help the highest income students.

Tax credits do not help meet the cash flow constraints of low-income students:

- **Tax credits and deductions do little to help low-income students pay the tuition bill when it is due.** Families do not receive the benefits of a tax credit or deduction until they file their tax return – which is likely to be several months after they have paid the tuition bill. A tax credit or deduction does not help lower income families who must struggle to come up with the funds in September and January to pay tuition costs.
- **The value of the credit is not clear in advance.** The value of the education tax credits is calculated as a fraction of funds spent and taxable income. Students, therefore, do not know exactly how much they will receive until after their tuition dollars are spent. This uncertainty makes it difficult for students to rely on tax credits as a steady source of funding, so credits may have little impact on their assessment of the affordability of college.
- **Tax credits do not cover living expenses.** Even if low-income students can lower their tuition costs with grants or by attending a less expensive school, they are still faced with the reality of living expenses. Based on a survey of college students, the College Board estimates the living expenses of an in-state public university student to be more than \$8,000 annually.²¹ In many cases, these costs exceed the price of tuition. Neither the education tax credits nor the higher education deduction can be used for these costs.

Higher Education Tax Credits and Deductions

Below is a brief description of existing higher education tax credits and deductions, including changes and additions as a result of The Economic Growth and Tax Relief Reconciliation Act of 2001. The Act also included other higher education tax incentives — such as student loan deductions and loan forgiveness. This paper concentrates on tax provisions designed to help students pay tuition while in school.

Tax Credits and Deductions:²²

HOPE Scholarship and Lifetime Learning Tax Credits

The HOPE and Lifetime Learning tax credits were introduced as part of the Taxpayer Relief Act of 1997. The HOPE credit is for undergraduates in their first two years of postsecondary education. In 2001, the maximum credit was \$1,500: 100 percent of the first \$1,000 of qualified tuition and fees and half of the next \$1,000. As of 2002, the maximum credit will be indexed to inflation. Students enrolled in any year of postsecondary education can claim the Lifetime Learning credit. The maximum credit is \$2,000 — 20 percent of the first \$10,000 of qualified expenses. Only one credit can be claimed per student in any tax year.

Both credits are non-refundable so a student must have income tax liability to claim them and the amount of the credit cannot exceed the filer's tax liability. They are targeted to lower- and middle-income students. Both credits phase out between \$40,000 and \$50,000 for single filers and between \$80,000 and \$100,000 for joint filers. (These income thresholds will be indexed to inflation as of 2002.) The credit can be used for tuition and required fees. The amount of qualified expenses is reduced by scholarships, Pell Grants, veteran's educational benefits or employer-provided tuition reimbursements. The Joint Committee on Taxation estimates that these two credits will cost \$4.3 billion in FY 2002.

Higher Education Deduction

The Higher Education Deduction was enacted through the Economic Growth and Tax Relief Reconciliation Act of 2001. This is an above-the-line deduction that reduces the taxpayer's adjusted gross income. The deduction has higher income limits than the education tax credits. In 2002 and 2003, individuals with modified adjusted gross income of up to \$65,000 and joint filers up to \$130,000 can take a maximum deduction per return of \$3,000.

In 2004 and 2005, the maximum deduction rises to \$4,000 with the same income limits. In addition, individuals with modified gross income of more than \$65,000 but less than \$80,000 and joint filers with modified gross income of more than \$130,000 but less than \$160,000 will be eligible for a \$2,000 deduction. The deduction can be used for tuition and fees in any year of postsecondary education. It is set to expire on January 1, 2006. The Joint Committee on Taxation estimates the deduction will cost \$1.5 billion in FY 2002.

Tax-Advantaged Savings Accounts:

Coverdell Education Savings Accounts²³

Formerly known as education IRAs, Coverdell education savings accounts are tax-advantaged personal investment accounts for education expenses (including tuition, room and board and books). Contributions to an account are not deductible, but distributions are not taxed. The Economic Growth and Tax Relief Reconciliation Act of 2001 made several changes to current law that became effective on January 1, 2002. Coverdell accounts can now be used for any year of education – kindergarten through college. The annual contribution limit per beneficiary has been raised to \$2,000. This maximum contribution amount phases out for individuals with modified adjusted gross income between \$95,000 and \$110,000 and for joint filers between \$190,000 and \$220,000. Students can get a Coverdell distribution and claim a HOPE or Lifetime Learning credit in the same year but not for the same expenses. Contributions can be made to a Coverdell account and a qualified tuition savings plan in the same year. Taxpayers cannot take the higher education deduction for expenses paid for with funds from a Coverdell. Funds from a traditional or Roth IRA can be used for qualified higher education expenses without having to pay a penalty for early withdrawal. The funds are taxed as income however. The Joint Committee on Taxation estimates the exclusion of earnings for donations to Coverdell accounts will cost \$300 million in FY 2002.

Qualified Tuition Savings Plans²⁴

There are two types of qualified tuition savings plans (QTPs). In a *prepaid tuition plan* individuals purchase tuition credits at current prices at eligible postsecondary schools. *College savings plans* are state-sponsored investment accounts that can be used for any institution of higher education. QTPs are state-run so there is considerable variation from state to state. About 22 states have prepaid tuition plans and 46 states have college savings plans. The Economic Growth and Tax Relief

Reconciliation Act of 2001 allows private institutions to establish prepaid tuition plans.

In most states, there is no income limit for contributors. Earnings accumulate tax-free and, as of January 1, 2002, there is no federal income tax on withdrawals from state-sponsored QTPs. The funds can be used for qualified higher education expenses which include tuition, fees, books, supplies, and equipment required for enrollment or attendance, and reasonable costs for room and board for students attending at least half-time.

Contributors can establish accounts for the same student in several states. Contributions can be made to a Coverdell account and a QTP in the same year. A HOPE or Lifetime Learning credit can be claimed in the same year as a withdrawal from a QTP but they cannot be used for the same expenses. Taxpayers cannot take the higher education deduction for any expenses paid with funds from a QTP withdrawal.

Distributions from a prepaid tuition plan reduce the student's cost of attendance in the calculations for federal financial aid. However, assets in a college saving plan owned by someone other than the student's parent (e.g., grandparent) are not reported on the FAFSA.

Changes in federal tax treatment of QTPs that were the result of The Economic Growth and Tax Relief Reconciliation Act of 2001 are slated to sunset on December 31, 2010. The Joint Committee on Taxation estimates the exclusion of earnings on contributions to QTPs will cost \$50 million in FY 2003, but that the cost will reach over \$250 million by FY 2010.

III. Declining Grant Aid

Declining Purchasing Power of the Pell Grant

The Pell Grant program is designed to target the lowest-income students with grants that can be used toward tuition and living expenses. While this is an efficient mechanism for targeting appropriate aid to poor students, the size of the grant has not kept pace with rising costs.

Pell Grants were authorized by Congress in 1972 to provide financial assistance to the neediest undergraduates. Measured in constant dollars, the maximum and minimum awards have declined since mid-1970's.

In the 1975– 1976 school year, about 1.2 million students received a Pell Grant. The maximum award was \$4,484 and the average award was \$2,436 (both in 2000 dollars).²⁵ The maximum Pell Grant covered about 84 percent of the average tuition, room and board of a public four-year university.²⁶

For the 2001 - 2002 school year, about 9.4 million students applied for a Pell Grant, an increase of 9.8 percent over the previous year and significantly higher than the five-year average growth of 1.1 percent per year. 4.3 million students received a grant. The maximum award was \$3,750 and the average award was \$2,299.²⁷ The maximum Pell Grant covered about 42 percent of a student's educational expenses at a public, four-year university.²⁸

This represents a 50 percent decline in the purchasing power of a Pell Grant since 1975. Low-income students now must make up more of the difference in college costs with loans. Close to 90 percent of Pell Grant recipients who graduated from college in 1996 had borrowed a student loan, while less than 45 percent of all graduating students had loan debt.²⁹

State Grants

At the state level, the majority of student financial aid is need-based, but the share of merit aid is rising. The amount of money devoted to merit aid has grown by over 300 percent since the early 1980's. Need-based aid has grown by 88 percent over the same period.³⁰ In 2000 – 2001, 24 percent of state aid was not need-based, compared with 15 percent in 1995 – 1996.³¹

In 1972, Congress established a program that is now called the Leveraging Educational Assistance Partnership (LEAP) to encourage states to set up need-based grant and work-study aid programs. States are awarded funds through a formula and they must match federal funds dollar-for-dollar. In 1999 – 2000, more than \$900 million in need-based aid was awarded in addition to the \$25 million in federal funds appropriated for the program. Almost half of the dependent undergraduates who received LEAP funds came from families with incomes of \$20,000 or less.³²

When the program was first started, only half the states had a need-based grant program. Today, all fifty states and the District of Columbia offer need-based grants

and work-study aid. However, the President’s fiscal year 2003 budget did not request any funds for this program.

IV. Not Meeting the Need

These shifts in the amount and type of aid available mean that low-income students are coming up short in trying to pay their tuition bill and living expenses.

An analysis by the Department of Education of students in the 1995 – 1996 school year found that the unmet need of dependent students in the lowest income quartile far exceeded that of those students from high-income families. Unmet need is calculated as the cost of tuition and expenses minus financial aid and the expected family contribution. The unmet need of low-income dependent students at a public university is almost 10 times greater than that of students in high-income families.

| Financial Aid Falls Far Short of Need | |
|--|---|
| <u>Family Income Quartile</u> | <u>Unmet Need, 1995-96</u> <u>(1995\$)</u> |
| <u>Public 2-Year College</u> | |
| Lowest quartile | \$3,200 |
| Second quartile | \$2,700 |
| Highest quartile | \$ 100 |
| <u>Public 4-Year College</u> | |
| Lowest quartile | \$3,800 |
| Second quartile | \$3,000 |
| Highest quartile | \$ 400 |
| <u>Private 4-Year College</u> | |
| Lowest quartile | \$6,200 |
| Second quartile | \$4,900 |
| Highest quartile | \$3,000 |

SOURCE: U.S. Department of Education, *College Access and Affordability*, 1999

Two-year community colleges are often seen as a more affordable option for low-income students. But while the overall tuition cost may be lower, the out of pocket cost to the low-income student appears to nearly as high as that of a four-year college. It is unclear exactly how low-income students cover their unmet need — most likely through a combination of work and parental loans.³³

Looking Ahead

These challenges are likely to become more acute in the coming years. The demand for postsecondary training will increase – as will the demand for financial aid. By the end of this decade, the number of high school graduates will top three million. A large share of these students will want to continue their education. The Department of Education expects college enrollment to jump to 17.7 million students by 2011 — a 20 percent increase over current levels.³⁴ At the same time, members of the baby boom generation will be retiring and our labor force will need an influx of educated and skilled workers.

A large share of these students will likely be from low-income families. Analysts from the Educational Testing Service have estimated that 80 percent of the increase in new students between 1995 and 2015 will be minorities.³⁵ It is difficult to predict accurately how many of these new students will come from low-income families. But given the strong correlation between ethnicity and income, we can expect that more low-income students will be applying to college and they will need significant financial assistance.

Despite the increasing demand for highly educated workers, our federal financial aid policy is shifting away from need-based grants to loans, tax credits and other tax incentives. Students from low-income families are less able to access these forms of aid and they do not provide adequate or appropriate assistance. Federal policies that provide sufficient support for need-based grant aid are most likely to induce and enable more low-income students to enroll in college and acquire the skills they need for the future.

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Endnotes

¹ *Digest of Education Statistics 2001*. United States Department of Education. National Center for Education Statistics. 2002. NCES 2002 – 130. Table 172, page 206.

² “Occupational Employment Projections to 2010.” Daniel E. Hecker. *Monthly Labor Review*, November 2001.

³ All figures in this report are in 2000\$ unless otherwise noted.

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⁸ *College Access and Affordability: Findings from The Condition of Education 1998*. Susan P. Choy. January 1999. The United States Department of Education. NCES 1999-108.

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¹⁰ In 2000, the mean income of households in the lowest income quintile was \$10,190 and \$25,334 for the second lowest quartile. The average tuition for a public university was \$3,754. Data from the Annual Survey of Colleges found that the average annual expenses for a student living on campus was \$8,200. This brings the total cost of one year of public in-state college to \$11,954. This is 117% of the mean income for the lowest quartile and 47% of the mean income for the second lowest quartile.

¹¹ “College Entry by Blacks since 1970: The Role of College Costs, Family Background and the Returns to Education.” Thomas J. Kane. *The Journal of Political Economy*, Volume 102, Issue 5, October 1994.

¹² *Trends in Student Aid 2001*. The College Board. 2001.

¹³ *Trends in Student Aid 2001*. The College Board. 2001.

¹⁴ *The Role the Federal Student Loan Programs Play in Supporting Postsecondary Students*, March 12, 2001, by Adam Stoll. Congressional Research Service.

¹⁵ *Trends in Student Aid 2001*. The College Board. 2001.

¹⁶ Linsenmeier et al 2001 found that the enrollment rate of low-income minority applicants increased by about six percentage points when loans were replaced with grants in financial aid packages for low-income students. Jackson 1990 found that black college applicants responded more positively to scholarship aid than white college applicants – they were 11 percentage points more likely to enroll. Black applicants responded to scholarship aid more positively than loan aid. This study only looked at those who have decided to apply, it does not test the impact on high school students.

¹⁷ This total includes the HOPE and Lifetime Learning credits, the higher education expenses deduction, exclusion of earnings in Coverdell accounts, exclusion of earnings of qualified tuition programs, exclusion of scholarship and fellowship income and exclusion of employer-provided education assistance benefits. It does not include the cost of the deduction for student loans.

¹⁸ “Individual Income Tax Returns, 1999.” David Campbell and Michael Parisi. Fall 2001. *SOI Bulletin*.

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²⁰ *RS20289: Education Savings Accounts for Elementary and Secondary Education*, Updated August 23, 2001, by Bob Lyke and James B. Stedman. Congressional Research Service.

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²⁵ *2000 Status Report on the Pell Grant Program*. Jacqueline E. King. American Council on Education Center for Policy Analysis. 2001.

²⁶ *Access Denied: Restoring the Nation’s Commitment to Equal Educational Opportunity*. Advisory Committee on Student Financial Assistance. February 2001.

²⁷ United States Department of Education Budget Service.

²⁸ According to the *Trends in College Pricing 2001* by The College Board, the average tuition, room, and board for a four-year public university was \$9,008. Therefore, the maximum Pell Grant of \$3,750 is 42 percent of the cost of attendance.

²⁹ *2000 Status Report on the Pell Grant Program*. Jacqueline E. King. American Council on Education Center for Policy Analysis. 2001.

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³⁴ *Projections of Education Statistics to 2011*. United States Department of Education. National Center for Education Statistics. 2001a. NCES 2001- 083.

³⁵ *Crossing the Great Divide: Can We Achieve Equity When Generation Y Goes to College?* Anthony P. Carnevale and Richard A. Fry. 2000. The Educational Testing Service.