

Who Wants to Be a Millionaire?
Benefiting From and Paying for Higher Education

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You probably *are* a millionaire . . . in a manner of speaking. If you add up the earnings you have made or will make over your working life (and convert it to 2008 dollars), it mostly likely will come to over a million dollars. This is especially true if you have a college degree. There's no doubt that typical college grads do very well for themselves relative to what they would've done with only a high school degree. I expect that this will continue to hold for the foreseeable future.

But who pays for students' college education? Most states have a well-developed system of public universities in which tax revenue pays a substantial share of the cost of obtaining a college degree. But an immediate question arises: if college is such a great investment, why do we have to be enticed by subsidized tuition to take it? My answer is that we really don't have to be nor, for the most part, should expect to be.

This issue of paying for college is squarely in front of us given the current state budgetary outlook and Governor Beshear's proposed a 12% cut in funding for higher education. So it is particularly fitting to look more closely at paying for college.

Let's begin by reviewing some basics of UK's budget last fiscal year (see <http://www.uky.edu/OPIE/FactBooklet0607.pdf>). Excluding the hospital, UK's expenditures for the 2006-2007 fiscal year were about \$1.2 billion. Not all of these funds were for instructional purposes, though, given UK's large service function and other obligations, making comparisons to purely teaching institutions difficult. Nevertheless, it is worthwhile to examine revenue sources. Funds from state government were \$318 million; around 26% of the total. While this does not represent a majority of the funding, state support is still quite important. In fact, it is more important than tuition revenue. In 2006-2007, UK's total tuition revenue – based on roughly \$6,500 per year for undergraduates – was about \$221 million; only 18% of the total budget. The remaining funding comes from a variety of sources, including grants and contracts and donations, but it's clear that students and their families directly pay a just a small share of the cost of their college education.

But college is typically a great personal investment for students. Let's look at some data to illustrate. To get an estimate of the usual financial payoff of a college degree, I examined data from the 2006 Current Population Survey (CPS). The CPS reports earnings by age in 2006 for individuals of differing levels of education that enables one to construct an estimate of what today's graduates' lifetime earnings will be (see http://pubdb3.census.gov/macro/032007/perinc/new04_001.htm). If you just add up the average annual earnings from age 18 to 64 for high school grads, you get \$1.7 million. For college grads it's \$2.8 million. College is looking pretty good. A better

way to assess this difference, though, it to compute the present discounted value of the high school and college earnings streams and then take the difference. Depending on the interest rate I choose for discounting, I get between a quarter and a half million dollars! Still a heck of a deal.

Remember, though, that this is the financial payoff that typically occurs, but it's not the expected payoff for everyone. In fact, in a heterogeneous society like our own, there will be many people who would not achieve this payoff for college and are better off not going. These could be folks that, for example, can go into the family business right out of high school, or who are especially good at the skilled trades, or are suited to jobs that community and technical schools train people for.

But for the typical person, college is a great deal even at private college tuition rates of \$20,000 per year. Over four years, paying \$80,000 in tuition to get between $\frac{1}{4}$ and $\frac{1}{2}$ million later still sounds pretty darn good. Of course, we don't need to be told that this is a good deal and for the most part, people would go ahead and make the investment in college without subsidized tuition by the state. Most families of college students are pretty well off and have the means to arrange their finances to pay substantially steeper tuition than UK and many other state universities charge. For those who aren't as well off, there are other options. Perhaps the most obvious is student loans. This is not a bad option at all . . . leaving college with tens of thousands of dollars of debt is not a bad deal by any stretch if it enables you to earn $\frac{1}{2}$ million dollars more. And, of course, another option for the really low-income families is direct financial aid.

State-subsidized tuition is essentially financial aid for everyone. Many claim it's important to keep tuition low to insure that college is affordable for all. But by doing so, we are giving financial aid to everyone who goes to college, the majority of whom are well off. Many of the state's poorer citizens will not ever make it to college, yet pay their payroll, income, and sales taxes and buy their lottery tickets to subsidize high-income families' tuition expenses. That just doesn't sit well by my moral compass. Charging higher tuition to most students and focusing financial aid on the truly needy targets the subsidy on the group many people are most concerned about.

Expecting beneficiaries of a good or service to pay for it is not a crazy idea. In fact, we do this all the time. It's the basis of a market economy; you buy the goods and services that you use. This is true of even really expensive items like houses and cars. Borrowing tens of thousands or hundreds of thousands of dollars to buy a house is not a bad thing if you have the future income to pay the money back. Likewise for borrowing to obtain a college degree.

Setting tuition to better reflect the cost of higher education has various other salubrious effects. There's an old saying that "he who pays the piper calls the tune." Thus, with state government funding so important in UK's budget, we are dragged toward whatever political fad du jour that comes out of Frankfort regarding higher education. Charging higher tuition and moving our revenue base away from state support gives UK all the more reason to pay less attention to Frankfort and more to our students

and their families. Additionally, this would release a lot of administrative time, energy, and resources spent schmoozing in Frankfort that can be devoted toward improvements for students, faculty, and staff. Further, UK and other universities could unfasten themselves from what has proven to be variable and unreliable support from state government.

One often hears the argument that college provides social benefits beyond the benefits to those who get their degree, implying state support is appropriate. This may be true, but these societal gains are likely swamped by the individual benefits and simply don't rationalize the preponderance of tax support for colleges. Thus, while one may justify some level of state support for colleges on this basis, it's appropriate that the main source of funding are the main beneficiaries . . . the college graduates themselves.