Why does college cost so much? In recent years college costs have risen faster than the rate of inflation. Using theory and evidence from course materials make an argument for why college costs are increasing so rapidly.

Several factors are contributing to the rate at which college costs are increasing. In the course materials, these theories are mostly presented independently. However, I believe two main forces are working together to drive college costs up.

The first factor that is driving the cost of college up is the shift in the way colleges are funded and the federal loan policy. Fifty years ago, colleges were primarily financed by the states. “Prior to the passage of the Higher Education Act of 1965, the federal government supplied only one form of aid generally available to all college students: National Defense Student Loans.” (Hearn, 2001, p. 144). Since that time, the federal government has steadily increased the amount of loans available to students. Hearn (2001) notes that since 1980-1981, “most of the absolute growth in aid totals has come from the growth of the dollar volume of federal loans (p. 146). The result of all of these new federal loans has been an explosion in the number of students who can afford to attend college. As with any market, an increase in demand without a corresponding increase in supply will lead to increased prices. Slaughter and Rhoades (2011) note that “federal loan programs enabled middle- and upper-middle-class students, especially those attending high-cost elite private institutions, to meet higher tuition costs (p. 436).

This trend is showing no signs of stopping. Recent changes in federal education financing policy, including new tax credits for education, may encourage “more young people…to enter college and those who already know they are going to attend may be willing to attend more expensive institutions” (Kane, 1999, p. 50). For this reason, the tax credits“provide
powerful incentives for states to consider raising community college tuition levels and for students to attend more expensive institutions (Kane, 1999, p. 50). Finally, at the same time that federal government policies were helping millions of Americans attend college, the states decreased their support of their institutions. “As postsecondary enrollments grew, state appropriations typically did not keep pace, leading to increases in public college tuition.” (Kane, 1999, p. 40). The 1990 report from the Pew Charitable Trust “The Lattice and the Ratchet,” sums up these forces very succinctly: “why even bother voluntarily capping revenues as long as there are ample students ready to pay for a first class education?” (Pew, 1990, p. 2).

The next factor that is contributing to the high cost of college is the nature of the business. Howard Bowen proposed the revenue theory of cost in the 1970’s. According to Breneman (2001), this theory states that “institutions of higher education raise all the money that they can and spend it on worthwhile activities” (p. 15). Breneman (2001) alludes to the positional nature of the higher education market, which was described in more detail by Winston (1999). “In higher education, managers appear motivated by what Clotfelter (1996) calls ‘the pursuit of excellence,’ a general goal which in practice means maintaining or improving the quality of the educational services they supply and the equity with which they are provided (Bowen and Breneman, 1993). This striving for academic excellence is often defined relative to other institutions” (Winston, 1999, p. 16). “Institutions index every financial variable to the outlays of a peer group, and judge themselves by where they fall in that relative ordering, always striving to increase their standing” (Breneman, 2001, p. 15).

In this competition, institutions have to spend money in order to stay competitive. This requires more revenue. Because that revenue is available in the market in the form of numerous subsidized students, institutions are able to continue raising prices. “The school with bigger
student subsidies has more and better maintained buildings, a more distinguished and influential faculty… a richer menu of student services…better food and fewer double and triple dorm rooms, smaller classes, more varied courses and programs, more outside speakers and debates, and extracurricular activities that are better funded” (Winston, 1999, p. 21). Because these things increase the institution’s standing in its peer group, institutions will keep spending money on them and they will keep increasing prices to pay for them.
References


