Financing of Higher Education in the Professional

Schools of the University of Chicago

Memorandum written at the suggestion of Walter J. Blum after consultations with Harry Kalven, Jr. and Aaron Director (all of them of the Law School of the University of Chicago).

Today, most of the schools operated by our private universities are run at a deficit; that is, the fees charged the students do not cover the actual cost of providing them with education. Since education for the professions, such as given in the law school, the medical school, the school of engineering, and in physics or chemistry, considerably increase the earning power of a man, it should be possible to provide in a market economy funds for the financing of such education, and if such funds were provided to the student it would no longer be necessary to sell such education below cost. The following is a set of provisions which serve to illustrate in what manner this could be accomplished at the University of Chicago.

(1) There shall be set up a corporation to be called hereafter the Fellowship Investment Corporation. This corporation will accept funds from private individuals, foundations, etc. who are desirous of investing under the conditions set forth below, and the corporation will provide funds for students certified to her by the University of Chicago. The funds granted shall be sufficient to carry a student through medical school, law school, etc. by providing for about $3,000 a year for each year of study. For one or two years after the student has left school he is not required to make any payment, but after a certain period he shall amortize his obligation to the Fund at a rate of about 10% of his income. No interest shall be charged and the amount paid by the student to the Corporation is not fixed in dollars but rather controlled by the current average national"spendable income." The "average spendable income" is defined by taking the average per capita income and deducting from it what the average individual has to pay in taxes.

Between the years 1900 and 1950 the average real income rose at an average rate of $2\frac{1}{2}\%$ per annum. Therefore, if there had been no change in the purchasing power of the dollar during the past 50 years, the provision here proposed would be corresponding to an annual interest rate of $2\frac{1}{2}\%$ on the average. In fact, there had been, of course, a considerable fall in the purchasing power of the dollar and the provision here proposed would have safeguarded the investor against loss resulting from this fall.

(2) The investor who turns over a certain fund to the Corporation shall obtain certificates for a corresponding "nominal value" which have maturities distributed over a period of perhaps 15 years. These certificates shall be purchased back by the Corporation in the year of maturity at a price which is determined by the per capita spendable income index in the year of maturity. The purchase price could be,lower in principle, lower or higher than the nominal value, and therefore, if properly set up, the investor will have to pay a capital gain tax rather than income tax whenever the purchase price of the certificates exceeds the nominal value.

(3) The University of Chicago shall offer to able students who are desirable members of its professional schools "Investment" fellowships of this type. Over a period of the next few years during which this program gathers momentum, the University shall increase the number of students in these schools and at the same time the University shall gradually raise the fees (either to holders of Investment fellowships along or preferably to all students) with a view to bringing these fees as soon as possible up to the actual per capita cost (not the marginal cost!).

(4) The University shall guarantee the investors against any possible default by the Corporation, and shall have the right to sue individual students who might default.

(5) It is assumed that wealthy individuals and perhaps foundations, might be induced to make long term investments in Investment fellowships. This type of

investment will be probably one of the safest investments, and even though its revenue is small, the fact that the revenue would be classed as "capital gain" rather than "income" would offer some attraction to those who are in the high income brackets. The absence of an interest rate charge gives the investment a generous character and since the investor is called upon to invest "in the future of America" and since he would, in fact, fulfill a useful social function, these fellowships might have a certain appeal to an important class of investors.

(6) The risk that the University takes by guaranteeing the investor against default should be more than compensated for by the opportunity offered to increase the number of students and to increase fees to the level where they fully meet the costs.