A Legislator's Toolkit for the New World of Higher Education

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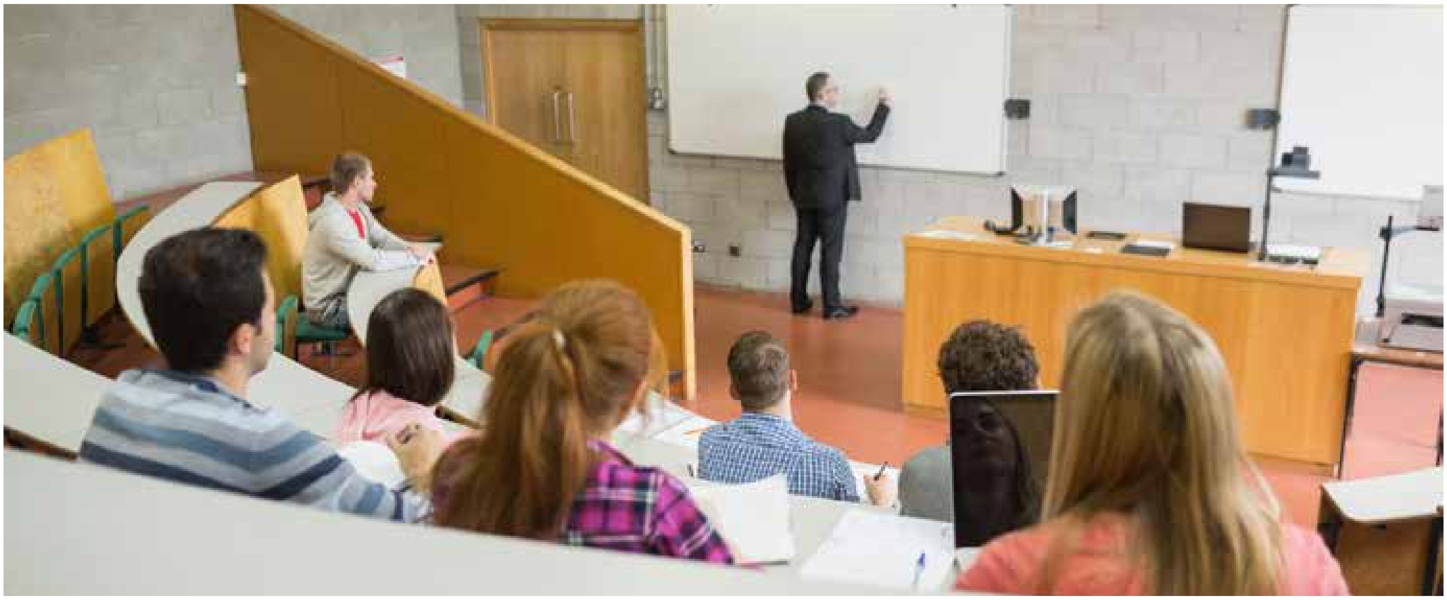


Paper No. 4

Outcomes-based Funding as an Evolving State Appropriation Model

BY BENNETT G. BOGGS

A rapidly changing global economy coupled with a public perception of universities as unresponsive to a changing marketplace have created a genuine challenge for American postsecondary education. One popular response over the past few years has been to develop outcomes-based (or performance-based) funding models by which state legislatures determine and measure the ability of their postsecondary institutions to meet defined state needs. As part of "A Legislator's Toolkit to the New World of Higher Education" series, this brief provides an overview of this funding model and how it continues to evolve. Considerations of benefits and challenges, as well as examples of successful implementations, are provided. Finally, recent legislation and state developments are offered to show how states are shaping this model to meet their specific needs.

About this series

With the support of the Laura and John Arnold Foundation, this is the fourth of eight briefs published by NCSL as "A Legislator's Toolkit to the New World of Higher Education." The series seeks to inform legislators about the current challenges to public postsecondary education so that they can form cohesive, strategic approaches to building effective and efficient postsecondary systems responsive to future statewide economic and community needs. In addition, a database housed on the NCSL website will identify other states' approaches to governance, funding and affordability, allowing policymakers to share information, exchange ideas and adopt the best practices that meet their state's particular needs.

What is the origin and purpose of outcomes-based funding?

Outcomes-based funding allocates a part of a state's overall appropriation to its postsecondary institutions based on student outcomes rather than on enrollment or historically standard allocations. In the 1960s and 1970s, enrollment-based models were the primary method by which states calculated the appropriations to their public colleges and universities—and reflected the era of baby boomers flooding American campuses. Beginning with Tennessee in 1978, a few states began developing institutional performance indicators to be included in the funding formulas. In these early efforts, participation was voluntary, and indicators were focused on broad topics such as increasing the number of programs with academic accreditation, testing students in their majors with standardized exams to show overall ability, and engaging constituents to ascertain satisfaction. Meeting such indicators provided a small "bonus" allocation to the college or university in addition to its general funding. The purpose was to provide simple financial incentives for colleges and universities to consider broad state priorities beyond traditional campus calculations. In these early efforts, states learned that some indicators could be poorly designed and difficult to measure. Also, inconsistent funding led many states to abandon their efforts.

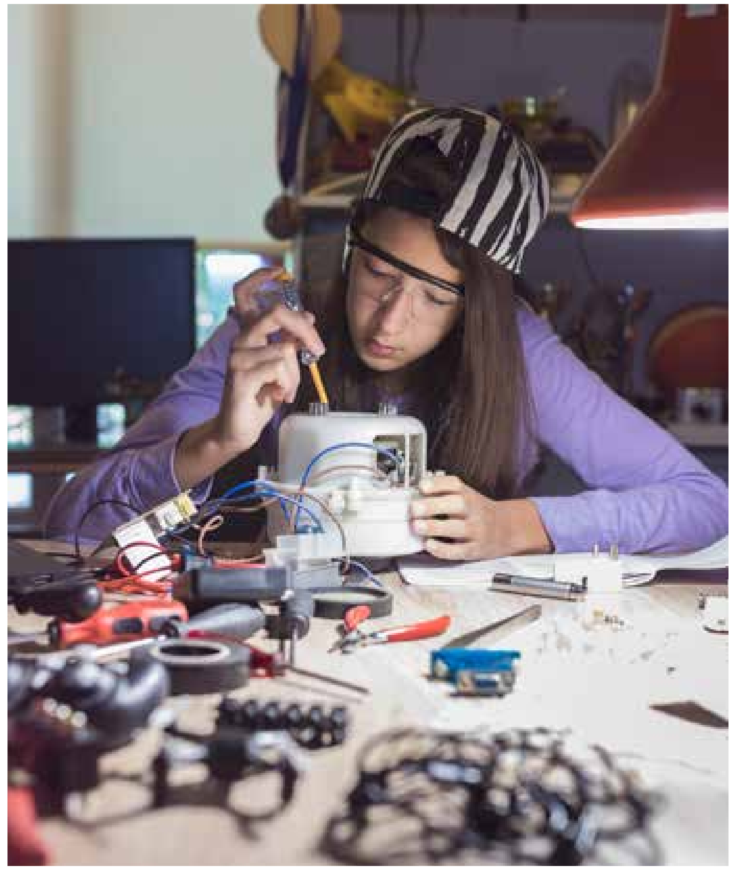
Following the Great Recession, states began to reconsider their traditional postsecondary funding methods that were disconnected from pressing state needs. Drawing from the earlier performance indicator models, states sought to have postsecondary funding aligned with state goals and to hold institutions accountable for student outcomes and success. This approach has been attractive. As of January 2018, 41 states are involved in outcomes-based funding for their postsecondary institutions in some capacity: Thirty states employ outcomes-based policies, six states have created but not yet implemented their policies, and five states are designing their outcomes-based policies.

What are the benefits and challenges?

As states have implemented outcomes-based funding policies, natural differences in approaches have occurred. However, HCM Strategists education consultants Martha Snyder and Scott Boelscher have noted that the most successful ones share guiding principles that offer the following benefits. These policies:

- Mirror the state's attainment needs and priorities, with explicit focus on increasing postsecondary success among specific student populations.
- Provide a reliable and formula-driven funding structure that fosters and rewards continuous improvement by all postsecondary institutions.
- Allocate resources continually over time as part of the overall funding of postsecondary institutions.
- Involve state and institutional stakeholders in developing the performance measures and to ensure broad understanding, clarity and commitment in implementing the policy.
- Phase in implementation so that institutions have time to adjust their internal planning and practices.
- Use performance measures that reflect the different institutional sectors and missions (i.e., research universities, regional/comprehensive universities, community colleges) and reward student outcomes as defined within the context of that sector.
- Execute consistently for three to five years, and then take time to evaluate and update as needed given new state needs and/or an awareness of unintended consequences.
- Research has shown that there are common challenges with designing outcomes-based funding models. Weaker designs fail to heed these cautions:

Allocations tied to outcomes-based funding need to be significant enough and sustained long enough to drive institutional planning and behavior. This can be difficult to do in states facing difficult revenue issues. Postsecondary education scholars Amy Li, Alec Kennedy and Margaret Sebastian have found that outcomes-based funding of over 5 percent was tied to community colleges producing increases in short-term certificate completions but declines in associate degree completions. In short, these institutions appear to have discovered that the outcomes formula provided community colleges greater financial rewards in the short term. This prompted them to guide students to short-term programs rather than consider longer-term alternatives leading to lasting workforce gains.



Minority-serving institutions can lose significant funding per student when compared to similar institutions in non-outcomes-based funding states. University of Wisconsin researchers Nicholas Hillman and Daniel Corral found that by their missions, these institutions are designed to attract and support underserved students who may require greater time and assistance to complete academic programs. When competing "head-to-head" with other public institutions, they may not show the same outcomes in the same time frames.

Choosing the right data to track, and tracking it appropriately, is easier said than done. Postsecondary education scholars David Tandberg and Nicholas Hillman found that adjusting which students are counted and when they are counted could significantly change the manner in which an institution scored. While one might suppose certain data could be manipulated, many of these kinds of questions are genuinely difficult to untangle in terms of defining who exactly is counted and when.

Are there different types that states use?

While most all outcomes-based models share similar benefits and challenges, the plans among the states can vary significantly. The differences can include such aspects as the specific performance indicators used and the percentage of funding allocated to each one, and whether the indicators are applied systemwide or adjusted per each sector within the system. In her research, Martha Snyder has developed four types of outcomes-based models that researchers now use to differentiate in their investigations of effective policies. The four types are:

TYPE 1—VERY BASIC MODEL:

- New money as a one-time bonus allocation only—no state-base funding involved
- Less than 5 percent of appropriation
- Institution mission not reflected
- Degree completion not included
- Underrepresented student success not included
- May not have been sustained for two or more consecutive years

TYPE 2—LIKE TYPE 1 EXCEPT:

- Allocates some recurring dollars (not a one-time bonus)
- Degree completion included

TYPE 3—LIKE TYPE 2 EXCEPT:

- Allocates 5 percent to 24.9 percent of overall appropriation
- Institutional missions reflected
- Underrepresented student success included
- Involves two-year and four-year institutions in all sectors

TYPE 4—CURRENTLY MOST ROBUST MODEL. LIKE TYPE 3 EXCEPT:

- Completion/attainment goals in place
- More than 25 percent of recurring allocation involved
- Sustained for two or more consecutive years

Understanding the experiences of states in expanding and adjusting their outcomes-based policies helps to explain the development of these four types of outcomes-based models as well as the process by which states identified and adapted them for their own goals. Two states—Indiana and Tennessee—offer excellent examples of lessons learned as they developed their own outcomes-based policies.

Lessons learned: Indiana and Tennessee

During the 1990s, **Indiana** created the 21st Century Scholars Program to expand access to postsecondary education. To this day, this program offers early-commitment financial aid to low-income students. In 2005, the state developed the Core 40 high school diploma focused on college preparation with a rigorous curriculum that became the standard at all high schools. The state also converted the state technical colleges into a statewide comprehensive community college system which immediately added 30,000 new college students. Yet these accomplishments in increasing access did not lead to increased completions and degree attainments. State leaders realized that as the workforce needed better-educated workers, postsecondary focus needed to shift from access to success.

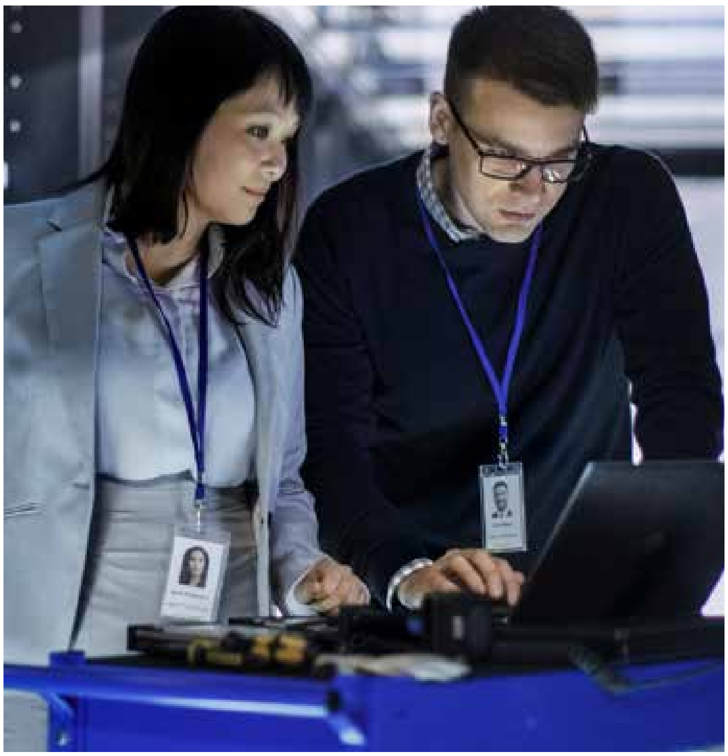
In response, the Indiana Commission for Higher Education created a set of three strategic plans. Each plan intentionally built on the outcomes of the previous one to meet state educational attainment goals. In 2007, the first plan emphasized improving overall access, expanding affordability, strengthening student college preparedness and developing programs addressing workforce needs. In 2012, the second plan focused on increasing on-time college graduation, doubling the number of certificates and degrees awarded by 2025, and increasing postsecondary attainment to 60 percent of the state's adult population by 2025. In 2016, the third report clarified direct channels and timelines for college completion and enhanced quality of competency-based credentials and intentional career preparation.

Parallel to producing these reports, efforts were underway to involve stakeholders in developing an effective outcomes-based funding model. In 2003, one indicator was designed to match federal research dollars at the state's research universities. In 2007, following four years of careful discussions and preparation, a proposal was approved by the state legislature for the first outcomes-based indicators for postsecondary institutions to be included in the state budget. Each biennium state budget since that time has incorporated an outcomes-based funding model recommended by the Indiana Commission for Higher Education.

The result has been a dynamic outcomes-based funding model that adjusts to meet the needs of both the state and the institutions. In 2007, the metrics focused on transfer, on-time graduation and increasing the number of awarded degrees. In 2009, metrics addressing completion by at-risk students and workforce training provided by two specific institutions were included. In 2011, the transfer and workforce-training measures were removed and the legislature directed that the entire formula be reviewed to consider institutional missions and other possible improvements. In 2013, the formula included metrics for specific institutional missions and at-risk students that were connected to student success and economically in-demand—or "high-impact"—degrees. In 2015, the formula was again refined to be more inclusive of other specific institutional missions with specific institutional goals. During this time, the percentage of state appropriation tied to outcomes-based metrics has increased from 1 percent to 6.5 percent. The key has been that the model has become more sophisticated as those involved gained a level of understanding and confidence in the way it was defined and administered.

A review of student outcomes in Indiana between 2005 and 2014 reveals that outcomes-based funding has had a positive impact on bachelor's degree completion, and students majoring in economically desired majors. In addition, institutions have improved student advising and support programs with better course scheduling and availability.

A key aspect to note is that Indiana also adjusted its state financial aid policies to better align with the outcomes-based funding metrics associated with attainment and completion goals. In 2013, the legislature passed HEA 1348, setting academic credit levels and time frames for students to complete in order to renew their aid. In related research, postsecondary education consultant Dennis Jones has shown that addressing issues of financial aid and tuition is important if outcomes-based funding models are to be effective. Otherwise, institutions have other revenue streams to turn to instead of focusing on performance metrics. This is a matter of state policies working together and not at cross-purposes.



As noted previously, **Tennessee** was the first state to undertake an outcomes-based funding strategy, which it has maintained in some form for its public institutions since that time. In 2010, the state legislature passed the Complete College Tennessee Act, which established that all postsecondary funding would be based upon the outcomes-based model. This significant decision has supported many state postsecondary initiatives, including the "Drive to 55" campaign, which set a goal of 55 percent of all Tennesseans holding a postsecondary degree or credential by 2025.

In preparing the groundwork for the 2010 College Completion Act, the Tennessee Higher Education Commission developed the performance indicators for the outcomes-based funding model by carefully engaging a wide array of stakeholders. In particular, the commission engaged the Statutory Formula Review Committee, which included representatives from the state's public universities, governing boards and community colleges along with state government officials. The metrics developed in consultation with this committee were used for the initial 2010-2015 funding period. The committee still reviews revised metrics to ensure alignment with overall state postsecondary goals. As with Indiana, the metrics have evolved over time to reflect specific institutional missions, different postsecondary sectors, workforce needs, and at-risk and adult learners.

In 1979, Tennessee allocated only 5 percent of the total state postsecondary appropriation to outcomes-based funding policy. As noted above, in 2010 all state funding was based on performance metrics. As of 2016, more than 85 percent of state allocations were devoted to outcomes-based funding with the remaining 5 percent reserved for quality assurance funding and 10 percent for operations and maintenance expenditures.

Since 2010, Tennessee has increased bachelor's degree completions 3.4 percent each year while associate degree completion has increased 6.5 percent each year. Enrollment has remained steady, which indicates institutions have learned to focus on completions and student success. State leaders claim the outcomes-based focus has transformed the overall postsecondary conversation to focus on comprehensive degree and credential completion.

Common lessons learned between Indiana and Tennessee include: Engage stakeholders early and often; begin with clear goals and policies; take time to set the right performance indicators; reflect institutions' missions and different sectors' purposes; align other related financial aid policies; phase in and maintain the investment across budget cycles; make the amount of money meaningful; and evaluate and revise.

How legislatures can help

Currently, 41 states have some form of outcomes-based funding activity underway. There are abundant examples of possible legislation. In 2017 alone, 34 bills were introduced in 14 states with five enacted. In 2018, 24 bills were introduced in seven states with five enacted. However, five states provide interesting review.

In **California**, as part of the 2018 state budget, the Legislature passed an outcomes-based funding formula for the state's 114 community colleges, which enroll 2.1 million students. Of $7.4 billion in general funding, 40 percent (nearly $2.5 billion) over the next three years will be tied to measures of student success and enrollment numbers of low-income students. Specifics include increasing degree and certificate production, boosting transfer to the public universities and reducing achievement gaps among underrepresented students.

In **Colorado**, the legislature passed House Bill 18-1226, which requires the Department of Higher Education to prepare a return on investment report of undergraduate degree and certificate programs offered by the public colleges and universities. The report must include information related to the number of students enrolled and degrees awarded annually; average time to completion per program; average number of credits earned by students; average cost to complete the degree for in-state students; average student loan debt; average annual earnings of graduates two, five and 10 years after graduation; and employment rate of degree programs during those time periods. While not precisely outcomes-based funding in terms of allocations, the required return-on-investment report specifies what are common performance metrics.

In **Florida**, legislators passed Senate Bill 4, which modified their outcomes-based funding metrics by increasing the authority of the Board of Governors in deciding the metrics. It also limits comparison of institutions to one another (specifying their missions) and adds $20 million to the formula for allocation. The modifications allow the universities that improve their performances on a series of measures—including graduation rates, salaries of recent graduates, retention of students and student costs—to receive their full share of state performance funds regardless of greater improvement measured at another university.

In addition to these three states passing legislation, two states are actively reviewing their outcomes-based funding formula in preparation for upcoming 2019 sessions. The **Idaho** Legislature's Joint Finance-Appropriations Committee is working with the State Board of Education to change the 29-year-old enrollment formula to an outcomes-based one. The state board has facilitated a three-year process to design the new formula, which it intends to present formally to the Legislature in January. The three-year plan is expected to request $16 million in "phased-in" state funding for the new formula, which will focus on increasing degrees and certificates, high-impact fields, at-risk students and students graduating on time. The proposal will be for all sectors of Idaho postsecondary education.

Following a time of no state budgets, **Illinois** has been convening a higher education workgroup of stakeholders, including legislators, to discuss outcomes-based funding. The purpose is to help public colleges and universities recover from their financially starved years and focus on improving enrollment and graduation rates. Early discussions involve differentiating among the institutions' missions and the manner the institutions address regional state economic and community needs.

Conclusion

Outcomes-based funding policies connect postsecondary institutions and planning to statewide economic, workforce and community needs. Over the past 40 years, these models have been refined as lessons have been learned and data collection enhanced. State legislatures have much to draw upon in their considerations of how their postsecondary institutions can better serve statewide economic and community needs.

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- Promote policy innovation and communication among state legislatures
- Ensure state legislatures a strong, cohesive voice in the federal system

The conference operates from offices in Denver, Colorado and Washington, D.C.

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