# FOLLOW THE MONEY:
## Strategies for Using Finance to Leverage Change in Higher Education

### OVERVIEW

The U.S. is a world leader in per-student higher education spending, but lags when it comes to realizing a return on that investment. The nation ranks low when it comes to higher education attainment rates, a position that has real consequences for individuals who enroll and do not finish and for the nation's economic vitality. In 2009, state and local governments spent $88.8 billion to fund public higher education. At the same time, less than 60 percent of students can expect to get a certificate or degree within six years, according to one federal estimate.

The U.S. spends twice as much as the average industrialized country on higher education, but continues to slide relative to other nations in the percentage of young adults with an associate degree or higher. Currently, the U.S. ties for eighth place among developed nations in postsecondary attainment among younger adults, who are now completing less higher education than their parents.

Despite recent reductions in state aid to higher education, state taxpayers continue to be the largest single source of unrestricted funds that colleges need to hire faculty and provide core student services. This means that governors and other state policymakers continue to have significant leverage over the priorities and direction of their public higher education systems.

Through strategic financing policies and with existing budget development and appropriations processes, governors can create a virtuous cycle of investment, savings, and reinvestment to help states reach the ambitious attainment goals that states and the nation need.

### IN THE STATES

Governors are in a key position to use finance as a lever to promote higher education productivity through their budgeting authority, their annual budget addresses, and other finance-related powers. There are three primary strategies governors can employ to restructure college costs and graduate many more students from high quality programs within existing resources:

1. **Performance funding**. Traditionally, states have funded higher education chiefly on the basis of inputs such as enrollments and prior years' spending. But, governors increasingly are tying state support to an institution's performance—specifically, how well it graduates students. At a minimum, performance funding should be substantial enough to get colleges' attention and change the way they allocate resources to promote student completion. Research indicates this means at least 5 percent of base state funding (and growing over time)—not new money alone—be allocated on the basis of a few course and degree completion measures, with a premium for the success of underrepresented students and on year-over-year increases.

   **Indiana** has gradually increased its focus on performance in higher education budgeting and funding under the leadership of Governor Mitch Daniels. In 2009, the governor and legislators approved a plan to increase the share of state higher education funding allocated on the basis of performance measures (e.g., total degree completion and degree completion by low-income students) to 15 percent over the next several years. Additionally, the enrollment component of the state's funding formula is now based on completed credits rather than attempted credits.

The state also has used performance measures in allocating budget reductions. In 2009, the governor asked the commissioner of higher education to apportion a $150 million mid-year budget reduction using institutional efficiency and degree production data (with high performing institutions receiving greater relief from cuts) rather than simply implementing an across-the-board reduction.

2. **Tuition and financial aid.** Governors set the tone for how to balance college affordability against requests from colleges and universities for more tuition revenue. As state budget revenues continue to decline, they should not be too quick to give away tuition authority—or be reluctant to take it back in the face of large tuition increases.

   Some governors have used their tuition authority as leverage to make needed change in higher education. In **Virginia**, colleges and universities were required to accept a statewide transfer agreement and accountability metrics in exchange for increased autonomy to set their own tuitions. Governor Chris Gregoire of **Washington** indicated this year that she expects similar changes from public colleges before she will grant more tuition authority.

   Some governors are calling for higher education to tie tuition increases to a common standard, such as an inflation index. Others—including **Maryland** Governor Martin O'Malley—have used tuition freezes to compel institutions to seek out and reinvest cost savings as a funding source for meeting attainment goals.

   State student aid programs provide governors another opportunity to encourage students to finish the certificate and degree programs that they start—and to do it as quickly as possible.

   In **Indiana**, Governor Daniels opened up state need-based financial aid to students in the state's newly created Western Governors University Indiana, an online institution that organizes its programs around students' mastery of content rather than seat time. This promotes shorter time to degree, which reduces costs to students.

   Facing a deep budget crisis, **Florida's** Bright Futures scholarship program stopped funding:

   - Fees for courses from which students withdraw. Requiring students to repay scholarship money for dropped courses resulted in tens of thousands of fewer withdrawn credit hours;
   - Full-time students who don't finish at least 24 credit hours a year. Previously, the scholarship program only required students to *attempt* 24 credits;
   - Students who take more than five years to finish their bachelor's degrees; and
   - Course credits taken beyond degree program requirements.

   Additionally, **Texas** requires public colleges and universities to charge in-state undergraduates the out-of-state tuition rate when they have accumulated 140 credits but do not yet have a bachelor's degree (the average bachelor's degree requires 120 credits).

3. **Better business practices.** During budget and appropriations decision making, governors and legislators should consider asking chancellors and presidents to demonstrate how they are adopting the following types of good business practices:

   - Systematic reviews and prioritization of programs (campus operations, academics, and athletics) and use of these critical analyses to eliminate, outsource, restructure, or consolidate the lowest-priority programs and services;
   - Joint/bulk purchasing of products and services such as health care, pharmaceuticals, and energy;
   - Employee contributions to health care and retirement plans that reflect reasonable employer-to-employee contribution levels;
   - Consolidated back-office operations (e.g. financial aid processing, construction management) across institutions and sectors using common technology; and
   - Evidence that institutions are reallocating savings toward increasing their capacity to graduate more students.

   In **Ohio**, Governor Ted Strickland developed statewide college-attainment goals, along with a strategic plan for how to reach those goals with available funding. He asked campuses for explicit plans to save 3 percent per biennium. At the same time, the state expects to save at least $100 million from efforts to implement a common technology platform, combine “back-office” functions, widen membership in joint purchasing pools, and implement e-procurement.

   While the governor sought additional higher education funding in the annual appropriations bills, campus budget officers said they recognized that his financing policies—including the biennial savings targets and tuition freeze—have created an environment where they have much stronger incentives to collaborate, share degree programs, and accept each other’s credits—in other words, to make higher education more collaborative and productive.

## IDEAS FOR ACTION

- Include performance measures (e.g., degrees awarded, degrees awarded to low-income and minority students) as part of the regular budgeting process for higher education. State funding for public colleges and universities should be based on measures of student progress and success not on just enrollment or what other colleges spend.
- Review tuition, appropriations and state student aid policies relative to college completion and attainment goals. These policies should work together to promote early and on-time graduation among colleges and their students. Policies that run counter to this objective (e.g., allowing students to take the same course multiple times) should be revamped.
- Establish a policy that requires all public colleges and universities, as part of the budget development process, to identify a specified level of cost savings (e.g., 3 percent of base funding) and a plan for reinvesting those savings in efforts to boost attainment rates.

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