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CONNECTING STATE AND INSTITUTIONAL FINANCE POLICIES FOR IMPROVED HIGHER EDUCATION OUTCOMES

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Abstract

This paper provides a conceptual framework that examines the interrelationship between state and institutional finance policies, including state appropriations, tuition and financial aid. It explores how state higher education goals can be advanced through outcomes-based funding policies that provide incentives for institutional behavior, and how policies can be designed to maximize student success.

Overview

States pursue their higher education objectives in a number of ways. As a result of the traditions of academic freedom and institutional autonomy, as well as labor laws and a general deference to academia or curricular issues, state policymakers tend to be less directive with state colleges and universities than they are with other state-funded agencies. Still, higher education exerts such influence on a state's economy and residents that policymakers maintain a strong interest in the activities and outcomes of higher education institutions.

One of the more powerful levers states use for influencing these institutions is finance policy. Even with recent reductions in state budgets, state colleges and universities have continued to rely heavily on state appropriations. Because of this, a state's finance policies can have a strong influence on institutional behavior, which in turn can directly affect student educational outcomes.

This paper examines how state finance policies interact with institutional finance policies, and how the interaction can promote the achievement of state higher education goals. First, the various state and institutional finance strands are identified and explored. The paper then looks at how outcomes-based financing policies can direct institutional policies toward the achievement of state higher education goals, with a separate focus on several key aspects of outcomes-based funding.

Goals and Policies

The higher education goals sought by states typically emphasize the educational attainment of state residents. While specific and detailed goals tend to be uncommon, states generally expect that public higher education institutions produce graduates with credentials that meet the state's workforce needs and fulfill the personal aspirations of the student population. Unfortunately, traditional state financing policies are often ineffective for achieving those goals and expectations. **Figure 1** illustrates the competing interests between state and institutional finance policies among three critical facets: state appropriations, tuition and financial aid. Each of these is described in detail below.

Figure 1. Traditional Finance Policies of States and Institutions Often Not Aligned

Finance Strand	State Policies	Institutional Policies
State Appropriations	"Base plus" (augment prior year's allocation); pay for enrollment	Full-time-equivalent-based allocation; collective bargaining agreements; promotion of research and prestige programs
Tuition	Limit tuition to promote affordability	Raise tuition to generate more revenue
Financial Aid	Allow students to choose from wide institutional options; promote broad, affordable access	Restricted to use at the institution itself; promote enrollment

State Appropriations

State Policies. Direct appropriations in the state budget constitute a major finance lever available to state policymakers. Even with the recent recession, which led to state budget cuts for higher education, state appropriations remain a major source of core institutional funding.

State appropriations for higher education traditionally have been determined using a "base plus" approach, where the prior year's funding level is augmented for various cost increases, including inflation and enrollment growth. State policymakers typically have not scrutinized higher education spending for direct conformance with detailed budget assumptions. Instead, states have traditionally taken a "black box" approach to higher education funding, where specific programmatic expenditures are seen as less important than the number of students moving through the institution. State policymakers generally focused on providing access by funding an adequate number of enrollment slots at various colleges and universities. They generally assumed that, once admitted, these students would

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successfully complete their courses of study and graduate with credentials in reasonable amount of time. This approach is an artifact of earlier years, when student populations were perceived to be homogeneous.

Institutional Policies. State appropriations sometimes are provided to individual campuses or departments and sometimes to university or college systems as a whole. In the latter cases, system governing boards may be assigned the task of allocating funding within the system. Policies for allocation are quite varied among the different systems.

In some cases, funding is distributed according to the number of full-time-equivalent students enrolled. (This makes policies regarding enrollment targets and caps all the more high-stakes.) In other cases, different funding rates are provided for different types of students, depending on class level, major or other criteria. Another critical policy element is the allocation of funding between classroom and non-classroom costs. These and other allocation choices can have a substantial effect on higher education outcomes and the extent to which state goals are achieved.

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Tuition—The Students' Contribution

Another major source of core institutional funding is the amount of tuition and fees paid by students. At publicly supported institutions, students typically do not pay the full cost of their education. Instead, public funds are used to subsidize the education costs of all resident students. As a result, public institutions are usually less expensive to attend than comparable private institutions.

State Policies. While some state legislatures or coordinating boards set tuition levels for public institutions, in many states, the institutions themselves possess this authority. Yet even in these cases, the state can exert considerable influence over tuition levels. For example, states may adopt tuition guidelines to inform the institutions' tuition deliberations. To give added weight to these guidelines, the state budget appropriation may assume a particular level of tuition revenue.

For state policymakers, a key consideration with regard to tuition has been affordability. They often see tuition as a potential impediment to access by lower-income families. However, low-tuition policies are a blunt instrument that subsidizes all students alike, regardless of their need. Moreover, such policies ignore the role of financial aid, which can defray tuition costs.

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Institutional Policies. Many systems and institutions possess the formal authority to set tuition (though often in consultation with state policymakers). While state policymakers generally desire to hold tuition down in order to preserve affordability, institutional policymakers frequently seek to increase tuition as a way of increasing system revenue. Some institutions leverage tuition policies to increase student success. For example, block tuition[1] pricing can encourage full-time enrollment, and partial tuition rebates for on-time graduation promotes timely completion. Still, even institutions that are particularly focused on underserved populations can feel a pull to increase tuition as a way of bolstering program quality and services. Indeed, some institutions view tuition as a mechanism whereby wealthier students help to subsidize needier students, who may have their tuition waived or otherwise covered through aid programs. At the same time, of course, students and state policymakers often provide counter pressure on institutions to hold down tuition.

Actual decisions by institutional policymakers are heavily influenced by the relationship between state appropriations and tuition revenue. If these elements are treated as independent policy choices, institutions have a strong incentive to increase tuition as a way of increasing total revenue. This approach views state funding for higher education not so much as a general price subsidy to students, but rather as a public contribution to the institutions themselves.

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Alternatively, state policy may connect tuition and state appropriations as fungible sources of base support for higher education. In this case, a tuition increase would simply offset what otherwise would have been appropriated by the state. This would dampen an institution's financial incentive to raise tuition.

[1] *Block tuition plans aim to shorten students' time-to-degree and lessen expenses by allowing students to enroll in courses within a designated range of credits (for instance 12-18 hours per semester) at a flat price.*

Financial Aid: Preserving Affordability

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State Policies. Generally, state financial aid programs function to promote affordability. In these cases, eligibility is based on family income and assets, frequently relying on information or calculations associated with the federal Free Application for Federal Student Aid (commonly known as FAFSA).

Some financial aid programs have additional or secondary goals, such as rewarding merit or encouraging enrollment in state institutions. Some states have tailored their financial aid programs specifically to advance student completion and attainment. For example, disbursing financial aid in installments over the course of the academic year can help students to manage their budgets—and thus their ability to stay in school. Similarly, programs that provide specific non-cash benefits such as tuition waivers can help students to stay on track.

While state financial aid programs generally allow students to attend any of a broad range of higher education institutions, recent years have seen increased concern about public financial aid being used at for-profit institutions — especially those with low graduation rates or high rates of student-loan defaults. A variety of policies have been adopted to address these concerns, including requirements that eligible institutions maintain graduation and default rates within specified parameters.

Institutional Policies. Institutional financial aid programs are typically distinct from state-run programs. Institutional aid programs can have different eligibility criteria, cover different costs, and have different sources of funding. Institutional policies may emphasize a different balance of merit and need criteria and may focus on tuition waivers or stipends. Many institutional aid programs are nominally funded through redirected tuition revenue.

By design, institutional financial-aid programs are only available to students attending that institution. This contrasts with a statewide program that can allow students greater choice in where they use their aid. On the other hand, institutional programs can be better-oriented to the needs of the students served by the particular institution. It is also sometimes easier for campuses to tailor institutional aid to a financial-aid "package" that takes into account the federal, state, private and other aid the student may have received.

Other Sources of Funding

Higher education institutions can receive funding from a number of sources beyond state appropriations. Especially during the recent recession, many institutions turned to fundraising, seeking donations, sponsorships and other gifts. The federal government has also sought an increasing role in financing (and thus influencing) higher education institutions. For example, in 2009, the federal American Recovery and Reinvestment Act provided states with $48.6 billion via the State Fiscal Stabilization Fund to maintain support for K-12 and higher education, approximately $8 billion of which states devoted to higher education.[i] Also, funding for Pell Grants and other financial-aid programs was significantly increased, with much of this funding ultimately provided to higher education institutions through student tuition payments.

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Finance Strands and Incentives

Enrollment-Driven Funding. As noted above, traditional higher education finance policies have generally funded programs in proportion to their enrollment. These policies assumed that costs were fairly consistent among students, and that students would be successful once they were admitted to adequately funded programs.

However, a changing economic landscape and a much more diverse student body have challenged those assumptions. In today's higher education environment, students have widely varying levels of preparation and needs, leading to very different degrees of success. Traditional finance policies thus are poorly suited to the achievement of educational outcomes, as they do not differentiate among students, and they focus on enrollment rather than completion and learning. They direct focus away from the demographic differences between successful and unsuccessful students, and thus are not attentive to equity gaps. Moreover, a policy that provides funding strictly based on full-time-equivalent student enrollment will encourage admissions, but does nothing to encourage graduation. When it is simply enrollment that is funded, institutions have little incentive to find innovative ways to boost student success. When there is no difference between funding for successful and unsuccessful students, institutional inertia is more likely to take hold and preserve old educational-delivery models, whether they work or not.

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An especially egregious example of the shortcomings of enrollment-based funding involves an early census date used by a particular higher education system. Institutional funding was largely dependent on the number of full-time-equivalent students enrolled as of the third week of instruction. Faculty were encouraged not to drop absent students, and not to schedule exams, until after the census date had passed and the college had secured its funding for the students. After the census date, however, there was considerably less institutionalized concern for student success in the term.

Enrollment-focused funding policies extend to financial aid as well. For example, a financial-aid program might provide a tuition waiver to a student who remains enrolled in some minimum number of units per term—regardless of the whether the student is making progress toward a degree or successfully completing courses. These kinds of programs reflect a wasted opportunity to provide incentives to aid recipients to make meaningful progress toward their degrees. (In 2008, the federal Higher Education Act was amended to require "satisfactory academic progress" among aid recipients, but institutions are allowed some discretion in how they fulfill this requirement.)

It has become clear that institutional policies need to be more nuanced and responsive to the diverse needs of their students. And it has become equally clear that finance policies create incentives that can either encourage or impede responsiveness to students' needs. Enrollment-focused finance policies are poorly suited to the need and desire of states to promote completion, increase overall attainment, close equity gaps and otherwise improve education outcomes. Such policies tend to discourage risks associated with innovation and instead have a bias toward the status quo. As the shortcomings of traditional, enrollment-driven funding policies have become increasingly evident, there has been a growing call for new policies that provide incentives for a focus on desired outcomes. Many of the new policy options center around the notion of outcomes-based funding.

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Outcomes-Based Funding. Several states are moving away from a strict enrollment-funding approach and instead developing or implementing outcomes-based funding policies of varied scope and levels of sophistication. In its simplest form, outcomes-based funding connects state budget allocations to the attainment of designated, measurable educational outcomes, with a direct link to a state's higher education goals. Such systems often place primary emphasis on metrics such as student graduations, course completions and year-to-year persistence. **Figure 2** summarizes how an outcomes-based funding orientation could be reflected in state and institutional policies across the three finance strands.

Figure 1. Traditional Finance Policies of States and Institutions Often Not Aligned

Finance Strand	State Policies	Institutional Policies
State Appropriations	Funding allocation based on student outcomes (such as completion, graduation and learning)	Allocated among and within institutions to promote student success (per best practices and evidence-based policies)
Tuition	Integral part of higher education funding; the student's share	Encourages success-oriented student behavior (such as full-time attendance and focused course-taking)
Financial Aid	Promotes affordability (even with higher tuition); encourages success-oriented student behavior (such as timely completion and satisfactory grade-point average)	Packages aid to maximize benefit of financial-aid dollars; Encourages success-oriented student behavior (such as timely completion and satisfactory grade-point average)

Outcomes-based funding policies hinge on the principle that institutions and students respond to financial incentives. Of course, all financing policies create incentives of some kind. As noted above, enrollment-based funding creates an incentive for institutions to enroll students. Outcomes-based funding, by contrast, seeks to provide incentives for a fuller and more robust range of outcomes valued by policymakers. It is critical, therefore, for outcomes-based funding to be grounded in clear and well-articulated goals.

Outcomes-based funding works on several levels. First, it clarifies what is most important to state policymakers. Should the state focus on producing career and technical education certificates? Is transfer a priority? Does the state need to address an achievement gap with minority students? Should the annual production of science, technology, engineering and mathematics degrees be increased? Is remediation a concern? An effective outcomes-based funding policy makes the specific goals clear, so that higher education institutions know what is expected of them.

Second, outcomes-based funding measures the extent to which goals are being achieved. When funding is linked to performance, data on student outcomes are required to allocate funds. Therefore, a reliable data-collection system is an important component of outcomes-based funding. But higher education data are not just useful for the funding formula. They also serve as policy assessments of what works and what is ineffective, and they help both policymakers and institutions identify best practices and facilitate improvement. Higher education data also facilitate transparency in public financing by highlighting what taxpayers and students receive for their investments in higher education.

Third, outcomes-based funding promotes state goals by creating a direct relationship between attainment of outcomes and receipt of funding. More and better outcomes result in more funding for the institution, which provides incentives for innovative efforts to improve performance. All major finance strands can be pressed into the service of improving outcomes: state allocations can be directed at services and programs with the highest potential for fostering student success; tuition policies can be set up to encourage full course loads and expeditious movement through degree programs; and financial aid can be structured not just to promote affordability, but also to provide incentives for academic effort.

In all these and other areas, outcomes-based funding can provide an effective bridge between state and institutional finance policies. It allows for considerable autonomy to institutions in pursuing whatever strategies they feel are appropriate to produce the expected outcomes. At the same time, it ensures that the state's needs and priorities are addressed by their public education institutions.

Modifications Respond to Criticism. Initial forays into performance-based funding[2] were somewhat clunky and limited, with states providing a small financial "reward" to institutions for meeting certain output metrics.[ii] As described in greater detail below, many higher education institutions criticized elements of these early efforts, objecting with some justification that these policies inadvertently encouraged colleges and universities to relax academic standards and/or to avoid admitting at-risk students, among other unintended consequences.[iii] It should be noted, however, that these criticisms are not an indictment of performance- or outcomes-based funding per se, for they acknowledge the power of finance policies to influence behavior. Instead, the critiques called attention to poorly developed funding metrics and other design flaws.

Today, the most promising practices in outcomes-based funding policies have been developed to respond directly to these and other criticisms. Overall, these more nuanced policies are recognized for having notable design improvements relative to early performance-based funding plans. Robust outcomes-based funding policies employ metrics that are well aligned with state goals, acknowledge differential costs, protect education quality, leverage the expertise and commitment of faculty and staff, and honor the unique missions of different institutions.

[2] *"Performance funding" funding" refers to a broad set of policies linking allocation of resources to accomplishment of certain desired objectives. Historically, postsecondary performance funding models were often add-ons or bonuses to base institutional allocations that institutions earned for meeting various goals or benchmarks. Additionally, many of these earlier models included measures focused more on inputs or processes than student progression and outcomes and were not intended to drive increased student completion. Today's outcomes-based funding models similarly seek to motivate and reward progress toward a set of stated goals, but have a direct link to the state's higher-education attainment needs and place primary emphasis on student completion and on narrowing attainment gaps across racial, ethnic, and socioeconomic groups, though they often include measures beyond student progression and completion. Advanced outcomes-based funding models also determine how a significant portion of the state's general budget allocation to institutions is determined.*

Robust outcomes-based funding policies employ metrics that are well aligned with state goals, acknowledge differential costs, protect education quality, leverage the expertise and commitment of faculty and staff, and honor the unique missions of different institutions.

For example, under a current outcomes-based funding policy, higher education institutions may receive more funding for the success of an at-risk student than for that of a better-prepared student. This both acknowledges that at-risk students often require more and higher-cost services, and provides institutions with a dividend for admitting a student with a potentially lower likelihood of success. In addition, outcomes measures under current outcomes-based funding policies have been refined as a result of study and conversations with experts and stakeholders, which can increase acceptance by institutions. Even more importantly, successful outcomes-based funding policies leverage the expertise and commitment of faculty and other institutional staff. These groups are familiar with student needs and capabilities, and they have a professional interest in the mission of their institutions.

As noted above, policies leveraging financial incentives can extend beyond state appropriations. For example, tuition policies can encourage students to focus on degree-applicable coursework by imposing a surcharge on "excess" course units (for instance, those in excess of 120 percent of the units required to complete the major). Similarly, financial-aid policies can be structured to encourage continuous enrollment or other practices that are associated with student educational success.

Current outcomes-based funding policies are intentionally protective of education quality. In addition to existing mechanisms such as accreditation and faculty governance, best practices in outcomes-based funding incorporate quality audits, employer satisfaction surveys, licensure pass rates and other direct and indirect measures of education quality.

Work in Progress. Notwithstanding recent improvements in outcomes-based funding best practices, some groups on campuses and elsewhere continue to voice concerns about and resist adoption of outcomes-based funding. Among the more fundamental concerns are beliefs that valuable education outcomes cannot be reduced to a small number of quantitative metrics; that outcomes-based funding implicitly questions faculty's inherent commitment to education quality; and that outcomes-oriented funding formulas infringe on academic autonomy with political motivations. For critics on some campuses, the burden of proof is on proponents of outcomes-based funding to demonstrate whether these critiques are valid.

Interrelationship Among Finance Strands. Policies and practices related to the various finance strands collectively work toward the achievement of higher education goals. For example, state appropriations provide base funding for higher education institutions; tuition policies both provide additional base funding and ensure that students make a meaningful contribution toward their own education; and financial aid policies help to ensure that higher education is affordable to state residents.

Ideally, the separate finance strands should be mutually reinforcing. In some cases, however, they can conflict with one another and impede the achievement of higher education goals. For example, some states hold tuition low in an effort to promote affordability, but in so doing reduce core revenue flowing to higher education institutions, which can lead to reduced enrollment slots and/or program quality. As an alternative, a robust, need-based financial aid program could protect affordability while permitting higher tuition levels. This higher tuition, in turn, can enable institutions to expand access and quality by funding additional enrollment slots, increased counseling and other student support services.

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Putting Outcomes-Based Funding Into Practice

While outcomes-based funding makes logical sense in theory, there are many considerations and concerns when putting it into practice. Four key considerations are (1) the identification of goals; (2) the selection of metrics and collection of data; (3) alignment of accountability; and (4) determination of what portion of funding to base on outcomes. Each is discussed below.

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Identifying unambiguous, measurable goals. A common misperception about performance funding is that it is a radical departure from traditional, enrollment-based funding. In the literal sense, enrollment-based funding is a form of performance funding, in that certain performance (i.e., the enrollment of students) is funded. The goal implied by traditional enrollment-based funding policies is primarily college attendance by state residents.

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The problem, of course, is that enrollment is a highly elastic concept in terms of cost and outcomes. Providing instruction to one full-time-equivalent student guarantees little more than approximately 30 hours of seat time. The type of instructor, the student-faculty ratio, the condition of the facilities (including classrooms, laboratories and libraries), the rigor of the instruction, ancillary services such as counseling and advising, and other aspects of the educational experience are not defined in the traditional enrollment-based funding model. As a result, there is a strong incentive to reduce costs in these areas. This in itself is not a concern, except that there is no counterbalancing force to ensure program quality. If a full-time-equivalent student taught by an experienced professor is funded at the same level as a full-time-equivalent student taught by a graduate student, the institution experiences a strong financial incentive to use the less-costly instructor, without regard to the actual quality of teaching either provides.

Outcomes-based funding offers a more sophisticated incentive structure that steers institutional policies toward specific goals. For example, if a state is concerned that a significant percentage of enrolled students fail to complete their courses, it could provide a funding allocation on the basis of course completion. Or, a state seeking to increase degree attainment among financially needy residents could provide a higher funding rate for academic progress by these students. Such a policy explicitly highlights the goal of increasing educational attainment within this group and implicitly recognizes that educating these students often requires additional resources (such as institutional aid or more intensive counseling). At the same time, this approach does not fund specific new programs or costs; rather, it allows institutions to use these resources however they think best. Institutional policies are directed toward the achievement of state goals not because the state requires this, but because the funding model provides incentives for the achievement of those goals.

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Selecting specific goals is not a simple task. In developing goals, state policymakers should be cognizant of the incentives (intentional and unintentional) that institutions will encounter. For example, it is not just how much education is achieved, but who is educated: an institution could significantly increase educational attainment by focusing on certain groups, while neglecting other, perhaps harder-to-educate groups. To avoid such unintended outcomes, outcomes funding can be adjusted for certain student factors, such as the students' degree of preparation, family income or other risk factors. Effective outcomes-based funding models recognize that some students are harder to educate than others, and combat the incentive to "cherry pick" only the easier (less-costly) students by funding at-risk or underserved students at a higher rate. In this way, the risks associated with enrolling such students are captured in the funding rate.

Selecting metrics and collecting data. As noted above, outcomes-based funding models rely on thoughtful measures of outcome attainment, as well as robust data systems to connect these measures to funding allocations. Clearly, the legitimacy of a state's funding model depends on the validity of the metrics used. For example, a state funding model could reasonably be criticized for defining recent graduates' income as a measure of education quality, since so many other factors affect income. Similarly, grade-point average is not an ideal measure of education quality; at best, it measures a student's performance level (irrespective of the extent to which this performance is due to the relative level of difficulty of the associated coursework). Moreover, grade-point average is not benchmarked with a fixed standard, which leaves it susceptible to grade inflation. Ideal metrics related to learning would be "value-added" measures that utilize pre- and post-tests to measure actual gains (such as the Collegiate Learning Assessment).

Institutions are often wary of public reporting of performance data, expressing concern about misinterpretation of data by potential students and policymakers alike. For example, an institution that serves predominantly at-risk students will likely have lower completion and graduation rates than a more selective institution, and some could conclude that the institution is not as effective or efficient compared with the more-selective institution. Such a conclusion could be erroneous. The solution, however, is not concealing data—rather, it is a transparent data system that is clear about what the metrics do and do not mean, and that takes into consideration the specific types of students and educational mission of the institution.

Overall, the efficacy of outcomes-based funding depends on the perceived legitimacy of the data collection system. This can be achieved not only by addressing the issues listed above, but also by ensuring the fair and responsible management of data. Ideally, this task would be assigned to an independent body, such as a higher education coordinating board or an independent commission.

Overall, the efficacy of outcomes-based funding depends on the perceived legitimacy of the data collection system.

Aligning accountability. For an outcomes-based funding system to be effective, there must be alignment between the funding outcomes and the parties responsible for those outcomes. For example, a statewide goal such as increased educational attainment by the state's population is beyond the direct control of any given institution. A single institution could actually increase its number of graduates, but if other institutions performed worse, statewide attainment could go down. In this case, a metric that measures individual institutions' degrees awarded year over year would be better than one that measures statewide attainment rates. Similarly, a state funding policy could be criticized on accountability grounds if it provides financial rewards to a four-year institution accepting transfer students from community colleges without considering the production of transfer-ready students from the two-year institutions.

An effective outcomes-based funding policy, therefore, holds institutions responsible for that which is within their control. This promotes both acceptance of the policy and a more efficacious incentive structure.

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Determining what portion of funding to base on outcomes. Early efforts to phase in performance funding typically linked only a fraction of an institution's funding to specified outcomes. Unsurprisingly, this can significantly weaken the ability of such performance funding to influence behavior. When the majority of an institution's base revenue is awarded for maintaining the status quo, it is difficult for a small additional appropriation to boost incentives for significant change and risk-taking.

To meaningfully guide institutional funding and programmatic decisions, an outcomes-based funding system should create a significant financial stake in higher education performance. In recent years, it is not unusual for 10 to 25 percent (or more) of an institution's budget to be dependent on performance indicators. Most of the rest is provided on basis of enrollment or a general institutional operating amount.

Some assert that virtually all of a higher education institution's funding should be tied to performance. They argue that all spending should in theory contribute (directly or indirectly) to the educational success of students, so why should any substantial amount of an institution's budget be shielded from accountability? Tying most funding to performance sends a powerful message about the purpose of funding, and strengthens incentives to make every dollar count. Critics object that an entirely performance-funded budget leaves no room for error. Funding only course completions, for example, does not provide any funding for the student who takes six weeks of classes and then drops out. However, this objection can be addressed by weighting the amount of funding per outcome to allow for some acceptable level of failures. For example, funding tied to course completions could build in some expected and acceptable level of non-completions. Additionally, the institution would receive some level of tuition for students that enroll and drop out partway through. Policymakers need to consider the best use of state dollars and how they are reinforced or interact with other income sources for institutions.

Finally, the very language used to define and describe a performance or outcomes-based funding mechanism can affect its success. Some states, for instance, have historically treated performance funding as a bonus that states can earn for exceeding threshold targets. This suggests that higher productivity is an exceptional accomplishment rather than an expected goal. Also, the more that performance funding is treated as a separate reward for achieving targets, the more that it can be perceived as less permanent and susceptible to cuts at a time of budget constraints.

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Conclusion

State finance policies can have a major influence on how institutions allocate funding, set tuition, administer financial aid and approach other fiscal and programmatic decisions. Outcomes-based funding in particular provides a way to direct institutional performance toward the achievement of defined goals, while preserving the autonomy that has historically been accorded to academia. Done well, it brings the separate finance strands at the state and institutional levels into harmony, supporting institutional investment in student success that can lead to increased success and educational outcomes.

Outcomes-based funding in particular provides a way to direct institutional performance toward the achievement of defined goals, while preserving the autonomy that has historically been accorded to academia. Done well, it brings the separate finance strands at the state and institutional levels into harmony, supporting institutional investment in student success that can lead to increased success and educational outcomes.

Key points for consideration by policymakers include:

- While common in past years, enrollment-driven funding policies are poorly suited to the diverse student populations and attainment needs of today and offer limited accountability for use of public funds.
- Many of the early efforts at performance-based funding were fairly criticized for a lack of sophistication that gave rise to unintended consequences, such as weakened academic standards or heightened selectivity in admissions. Current outcomes-based funding policies have been much more attentive to those potential pitfalls.
- A well-designed outcomes-based funding policy utilizes unambiguous, measurable goals, developed with the assistance of key stakeholders. Using a trusted, independent organization to collect, analyze and promulgate data that track progress toward those goals helps ensure the validity of the overall policy.
- To be effective, an outcomes-based funding policy should align accountability for funding outcomes with the parties responsible for those outcomes and make provision for factors that are beyond an institution's control. This aligns incentives with controllable choices and promotes acceptance of the policy.
- Across the country, there has been considerable variation in the percentage of institutional funding that is subject to outcomes-based funding mechanisms. In general, larger percentages provide stronger incentives and are less likely to be dismissed as boutique or temporary add-ons to the main funding system.
- Policymakers should evaluate all finance strands—state support, tuition policy, and student aid—and how they interact with each other. Ideally, the policies are mutually reinforcing and aligned with the state priorities of access, affordability and student success and completion.

Author Bio

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Steve Boilard is the Executive Director of the Center for California Studies at Sacramento State, where he is also on the faculty of the Public Policy and Administration department. Previously, Steve spent 14 years at the California Legislative Analyst's Office, heading the office's Higher Education unit. He holds a doctorate in political science from the University of California at Santa Barbara.

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