PERFORMANCE-BASED FUNDING IN HIGHER EDUCATION

What is performance-based funding?

Performance, or outcome-based funding, seeks to better align institutional incentives within the higher education system with the needs of the state, particularly in filling the talent pipeline for high-demand, high-paying occupations. **The basic concept is simple: post-secondary institutions are financially rewarded through higher appropriations for hitting desired outcomes**. Some performance funding systems also penalize institutions for failing to achieve outcome measures by decreasing underperformers' budgets.

Thirty-two states have some form of performance-based funding system in higher education. Each state has varying metrics and overall percentages attached to the incentive funding. Some states use performance-based funding in a bonus-like system, with institutions receiving increased funding when they achieve important metrics, but not having funds "at-risk" if failing to meet them, while others use outcomes-oriented formulas to determine most of an institution's funding each year. The adoption of more rigorous performance-based funding models has grown in popularity, with states seeing the method as a way to improve alignment between higher education goals and economic needs.

Ultimately, the success of a performance-based funding scheme is dependent on the selection of appropriate goals and metrics. Not all performance-based funding systems are created equal.

State Success Stories

Indiana
Indiana's Performance Funding per-unit payment. Indiana sets metrics once every two years and places a dollar amount for each attainment of that metric. Each metric is measured by a change in average output. For example, a research institution's STEM bachelor's degree completion addition to the average is worth $25,000 in FY 2022-2023. If the institution increased their three-year average in 2017 to 2019 by 200 students, then the institution would receive $5 million for that metric. Note, however, that the amount per metric may be proportionally adjusted based on funding availability.

Indiana's model began with 1% of funding being put through outcome metrics to now **6% of operational funding comes from performance funding**. Indiana's program has been highly successful; studies found that between 2010 and 2015, there was a **22% increase in degree completion for "high impact degrees"**.

Florida
Florida's higher education system is funded according to a set of guiding principles developed for the state's PBF model: 1) use metrics that align with strategic plan goals, 2) reward excellence or improvement, 3) have a few clear, simple metrics and 4) acknowledge the unique mission of different institutions.[1] The Board of Governors that administers the system evaluated 40 different metrics before choosing 10 metrics that are, for the most part, applied to all 12 institutions, no matter the type.

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[1]Board of Governors for the State University System of Florida, Performance-Based Funding Overview Document, March 2021.

<u>Florida's Performance Based Funding Metrics</u>

1. Precent of Bachelor's Graduates Employee (Earning $25,000+) or Continuing Education
2. Bachelor's Degrees Awards in Areas of Strategic Emphasis
3. Median Wages of Bachelor's Graduates Employed Full-Time
4. University Access Rate (Percent of Students with Pell Grant)
5. Average Cost to The Student (Net Tuition Per 120 Credit Hours)
6. Academic Progress Rate (2nd Year Retention with GPA Above 2.0)
7. Four Year Graduation Rate, Full Time or Full Time Equivalent
8. a. Graduate Degrees Awarded in Areas of Strategic Emphasis
   b. Freshman in Top 10% of Graduating High School Class
9. a. Two-Year Graduation Rate for Transfers
   b. Six-Year Graduation Rate for Student Who Are Awarded a Pell Rant in First Year
10. Institution Choice

The total performance-based funding allocation for the 2021-2022 school year was $560 million, including both investments by the state and institutions. Florida has seen this investment pay off. For example, there was a **14.5% 4-year graduation rate increase from 2009-2013 to 2016-2020** (metric 4) and **20.7% increase is median wages of bachelor's graduates employed full time from 2012-2013 to 2018-2019** (metric 2).

Tennessee
Tennessee uses two different formulas to determine the funding amount for institutions. The first is an outcome-based funding formula, used for the bulk of Tennessee's institutional funding, and the second is Quality Assurance Funding (QAF), bonuses for specific quality metrics.

The outcomes based formula is where institutions receive the bulk of their funding. Each institution begins with a starting point amount based on the previous year's allocation. Any new funds are determined based on the formula. The formula uses a three-year average for each outcome and differentiates the outcome goals for universities and community colleges. There is also a greater weight for focus populations, again based on institution type (focus populations include low-income students, adult learners, etc.).

Tennessee's Quality Assurance Funding (QAF), previously performance based funding, seeks to assure continual improvement on quality in universities and community colleges. The QAF formula is reviewed every five years, to ensure relevance and effectiveness. Each institution begins with the outcomes-based funding total. The QAF formula allows institutions to receive an additional incentive for meeting other quality control metrics. The goals for QAF are to: increase points associated with accreditation, focus on student equity, further institutions' emphasis on quality, and workforce alignment.

A differentiation between Indiana, Florida, and Tennessee is the competitive aspect that Tennessee adds. Institutions are *competing* for a share of the available funding each year. This competition allows for constant striving for improvement relative to each institution's peers.

Texas

In 2013, Texas adopted a performance-based funding formula for its technical and community colleges, comprised of 10% and 88% of funding, respectively. Their formula uses a per student achievement point system. The system rewards institutions based on students meeting criteria such as completion of a college level math course, completing 15 semester credit hours, earning a certificate or degree, and transferring with a threshold of credit hours. Each point earning category has different points awarded to it, so the institution gets a different dollar amount for each student in each category. In 2018, the dollar per point was approximately $172, while for 2020-2021, the amount was increased to just over $200.

Although the Texas program has had success, it is not without issues. A 2015 study showed that the metrics used disproportionately did not fund community colleges with high percentages of disadvantaged students. The metrics are underinclusive when considering at-risk students and could even encourage the recruitment of only students who are already likely to succeed. A remedy was attempted in 2019, but did not pass in the legislature.

Oklahoma's Performance Funding Can Be Improved

Though Oklahoma's higher education system advertises that it uses performance metrics in establishing institutional budgets—and even has adopted administrative rules to that effect—it is unclear to what extent performance-based funding is actually realized in practice.
Due to a unique constitutional provision, Oklahoma's legislature is required to fund the entire higher education system in a single lump sum, rather than institution by institution. The Oklahoma State Regents of Higher Education , a nine-member board appointed to staggered nine-year terms, then distributes the funds to particular institutions "according to its needs and functions."

In 2012, the Council of Presidents adopted a performance-based funding formula to assist in the distribution of the allocated funds, however it is unclear the extent to which this formula dictates funding decisions.

The Oklahoma State Regents, however, have signaled an intention to more rigorously and uniformly apply performance metrics to their budgeting process going forward. A new strategic plan recently developed by the Oklahoma State Regents, Blueprint 2030: Innovating and Elevating Oklahoma Higher Education for Tomorrow's Workforce, includes development of a new performance-funding formula.

Rewarding Higher Education Institutions for In-Demand Degrees

Alignment of higher education and workforce needs is imperative for business success economic growth in Oklahoma. In particular, ensuring high-paying, high-demand fields have a steady supply of up and coming talent is critical to Oklahoma's economic success. There is perhaps no better or more direct way to achieve this important goal than by aligning monetary incentivizes for higher education institutions to produce desired outcomes.

Recommendations

Oklahoma should implement performance-based funding both within its existing budgetary framework and through legislation that seeks new ways to further incentivize particularly acute state workforce needs. The State Regents should develop a rigorous performance-funding framework based on best practices from other states, and transparently and faithfully apply that framework to budgeting decisions for institutions. As a state-funded and operated system, these metrics should be geared to Oklahoma's economic needs and state goals, and weights and funding amounts should align accordingly. The legislature can enhance the effectiveness of a new performance-based funding approach by enacting legislation that provides additional, "bonus" funding on top of the state's lump-sum higher education appropriation for particularly acute state workforce priorities.

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