"Outcome Funding"

Tennessee experiments with a performance-based approach to college appropriations

By Robert A. Jones

NASHVILLE

WHEN THE NASHVILLE songwriter Kris Kristofferson famously penned the words "freedom's just another word for nothing left to lose," he was not likely contemplating Tennessee's higher education system. But the lines are more apt than he might have imagined.

Tennessee, long at the bottom of the higher education heap, is throwing out the rule books that have governed its state colleges and universities. With little to lose, the state leadership is gambling that a sweeping reform, anchored by a new approach to funding, will pull the state system out of its long trough and lift it, at least, to the national average.

Beginning this year, Tennessee is promising to boost the production of college graduates by 3.5 percent annually, yielding a cumulative 210,000 more bachelor's and associate's degrees by 2025. At the same time, Tennessee officials say they will reduce college dropouts dramatically, and achieve those results at a lower per-student cost than today.

The reform has attracted national attention because of its scope, which includes every level of public institution from community colleges to the University of Tennessee, and because it incorporates many of the strategies currently favored by education foundations and think tanks. As such, Tennessee is seen as the laboratory where those strategies will be tested.

"We are doing these things aggressively. It seems a little strange to say it, but Tennessee has become the leading edge of change in higher education," said John Morgan, chancellor of the Tennessee Board of Regents. "Other states are now looking at us to see what's going to happen."

Reform, and promises of reform, constitutes a way of life in higher education, of course. Many such attempts fail to produce long-lasting change and, collectively, the makeovers have not stemmed the decline that has seen the United States fall from first place to tenth among nations in the percentage of young people earning a college degree.

Education experts are hoping the Tennessee plan will turn out differently, and they see a couple of reasons for optimism. First, according to Dewayne Matthews of the Lumina Foundation for Education, the Tennessee approach is comprehensive rather than piecemeal, and derives its authority not from agency directives but from legislation passed with overwhelming support from both Democrats and Republicans.

That legislation, the Complete College Tennessee Act, was passed in 2010 and spells out specific goals such as increases in graduation rates and the retention of students in the first years of college. It then ties future funding for each institution to the achievement of those goals.

Stan Jones, president of Complete College America (a national nonprofit organization that advised the state at various times in the process), sees a second hopeful sign. "The most elegant reform plan will do no good if it's not supported by high officials in the state," he said. "In Tennessee the leadership has consistently provided support, and they have built a consensus that continues to the present."

Wade Payne, Black Star, for CrossTalk

Jamie Woodson, a Republican state senator, says that "rewarding higher education with larger budgets is not part of the conversation. The conversation is about outcomes."

Jones noted, for example, that the Tennessee legislation was sponsored by former Governor Philip Bredeson, a Democrat, and now has been endorsed by the new Republican governor, Bill Haslam.

Ironically, Tennessee is also seen as fertile ground for an education experiment because of its lamentable past. Today, 31 percent of Tennessee adults ages 25–34 have a college degree, a figure that ranks the state just below Mississippi. An analysis by Complete College America shows that only 12 percent of Tennessee's ninth graders will eventually earn a four-year or two-year degree.

The state's flagship institution, the University of Tennessee, is widely seen as a ho-hum research university subject to rapid turnover of presidents. At the state's community colleges, two-thirds of the students fail to transfer to four-year institutions or to graduate. And the state's parsimony in funding has pushed tuition so high that the National Center for Public Policy and Higher Education (which publishes *National CrossTalk*) gave Tennessee an F in college affordability in 2008. The situation has only worsened since then.

"Large states like California and New York, especially if they see themselves having a proud history, can be very difficult places to get consensus on reform," said Jones. "A place like Tennessee is an easier environment to work in because it's smaller, and no one is kidding themselves about the need to get the job done."

Tennessee, long at the bottom of the higher education heap, is throwing out the rule books that have governed its state colleges and universities.

The high concept behind the Tennessee plan is disarmingly simple: The state will reward each campus according to its "outcomes"—the production of degrees, retention of students, and other measurable factors—rather than its enrollment. Each institution will be given its own set of goals and will be measured according to its success in

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"We will see some institutions with improved performance who receive fewer dollars because others improved even more," says Joseph DiPietro, president of the University of Tennessee. "That's when the in-fighting will start."

meeting those goals.

This strategy, known as performance funding, has been used for decades in other guises. Typically it was employed as a reward, or cherry, on top of an enrollment-based funding formula. If college administrators achieved certain goals they would be favored with a few extra percentage points of funding.

The Tennessee plan tosses out the enrollment formula altogether and puts performance funding on steroids. Henceforth, in Tennessee, 100 percent of funding will be based on outcomes and none on enrollment.

It comes as no surprise that this idea did not come bubbling up from the campuses. The architects, rather, were a handful of officials at the Tennessee Higher Education Commission (THEC), working with the legislature and the office of then-Governor Bredeson.

"A lot of things came together at once," said Richard Rhoda, executive director of the commission. "We had a governor who would ask questions like, 'Why aren't students graduating from our colleges?' At the same time the state was reforming its K–12 system, and the issue became, how are we going to provide for the larger number of kids successfully graduating from high school?"

Bredeson was a Democrat, and a plan to alter the higher education system typically would set the stage for a political battle in the legislature. But that did not happen, largely because the proposals emanating from THEC and its consultants emphasized accountability, cost savings, and the production of educated workers—themes beloved to Republicans.

The Complete College Tennessee Act of 2010 spells out specific goals for each institution, then ties future funding to the achievement of those goals.

Gordon Fee, a retired Lockheed Martin executive at the Oak Ridge National Laboratory, said state businessmen were ready to support a change in direction because they were increasingly frustrated by the lack of skilled and educated workers in the state.

"I would hear stories that managers were going further and further outside the state to attract people who could fill the jobs they had," said Fee. "You got the sense that the state was producing graduates with the wrong skills or in the wrong field, and that we needed to make a change."

By early 2010, the Complete College Tennessee Act was passed with hardly a dissent in the legislature. The first provision of the act directed THEC to link higher education to "the state's economic and workforce development."

College leaders initially were a harder sell. Dennis Jones, president of the National Center for Higher Education Management Systems and a Tennessee consultant, said many campus presidents saw danger signals in the legislation but were eventually persuaded that a major change was necessary to pull the state out of its trough.

"Tennessee is so far below the national average that small tweaks weren't going to work," said Jones. "And a big selling point was the economic impact of success. If higher education met the new graduation goals, Tennessee's per capita income could rise 20 percent. That's huge."

The THEC plan that grew out of the legislation developed several strategies to ease students' path toward a degree, such as uniform core courses and uniform course numbering in community colleges and universities.

In addition, all remedial or developmental education was handed over to community colleges, whether students are enrolled in a community college or a university. Cleveland State Community College in southeastern Tennessee has become a national leader in designing computer-assisted developmental courses, and it is hoped that the Cleveland successes will be adopted on a larger scale.

But, in general, Tennessee laid out few such programs. According to David Wright, director of policy at THEC, the planners in Nashville decided they would determine "the what and not the how" of the reform.

"We did not want to pretend that we had all the answers here in Nashville," Wright said. "It seemed a better idea to let each institution handle the issue of how to achieve the goals. And if a particular institution comes up with a great approach, it's our hope that we can seize on those good ideas and scale them up across the system."

And so Tennessee's fate in higher education rests almost exclusively on the success of its incentive funding. And in that area, the state planners have broken new ground.

To begin, each campus was assigned a mission statement, an otherwise innocuous-looking document that has the effect of defining—and limiting—that institution's academic pursuits. The University of Tennessee at Knoxville's mission statement, for example, heavily emphasizes research, professional education such as nuclear engineering, and, curiously, printmaking.

In effect, the mission statement gives UT Knoxville a license to pursue and expand those programs. And because other institutions' mission statements will not include some of UT's programs, UT Knoxville will be protected from incursions into its turf. For the time being, printmaking appears to be safe at the home of the Vols.

But what the mission statement gives, it also takes away. Nowhere does UT Knoxville's mission statement mention a medical school. The campus does not have a medical school—the main UT medical school is located in Memphis—and the mission statement makes it more certain that the situation will remain so.

Those limitations were intentional. "Under the old funding formula using enrollment, the way (for a campus) to get more money was to start new programs, and sometimes we saw a duplication of programs," said Rhoda. "Under the new plan, which rewards the production of graduates, a lot more thought will be given to where programs are likely to be high producers."

Not surprisingly, the development of the mission statements set off a lively round of lobbying by campus presidents to make sure their institutions were defined in the most satisfactory and rewarding fashion.

At the University of Memphis, President Shirley Raines said she tried, and ultimately failed, to have her campus described as a research institution more or less equivalent to UT Knoxville. The difference between what she wanted and what she got might appear subtle to a casual observer, but Raines said the distinction looms large because a broader research role would ultimately bring more dollars into her university.

"We produce something like 150 doctorals a year," she said. "I think we compare very favorably to UT Knoxville on that score, and we haven't given up on this issue. There's going to be an opportunity to tweak these things over the next year, and I expect we will take advantage of that."

The mission statements have another, more nervous-making purpose. By defining each campus, they serve as the basis for that campus' funding formula, the metric that will be used to judge its performance.

The metric, in fact, is the beating heart of the Tennessee system. It employs ten criteria, ranging from freshman retention to research dollars gained. Each year an institution will receive a score for each criterion. The higher the total score, the more funding that campus will receive.

But the criteria are weighted differently for each institution according to its mission statement. Thus the University of Memphis, whose research component is not described as loftily as UT Knoxville's, will be rewarded less vigorously for an increase in research activity than will the UT campus.

According to Raines, that difference could amount to millions of dollars per year. Raines says she very much supports the concept of an outcome-based approach to university funding but is wary of what she sees as the devils in the details. "I firmly believe that the people (at THEC) are working in good conscience, and these issues will get resolved," she said.

The new funding system begins this year but will incorporate what one education official termed a "soft roll-out." In effect, that means the impact of campus performance on funding will grow slowly over the next three years until it reaches the 100 percent level.

Because of the soft roll-out, no campus will experience a sharp uptick or downtick in funding. And even after three years, when the new system is fully operational, the formulas will limit the annual loss or gain for an individual campus to approximately two percent a year, according to Russ Deaton, director of fiscal affairs at THEC. "It is designed to produce incremental impacts," he said. "Of course, over time those impacts could compound for an institution with consistent low scores."

The reality that campuses will be competing with each other for available dollars has not been lost on college presidents in the state. All presidents and other campus officials interviewed for this article expressed at least guarded support for the new system, but the uncertainties have lent a breathless quality to the experience.

A two percent swing at the University of Memphis, for example, could amount to more than $5 million a year. With a metric containing ten criteria, and a different weight assigned to each criterion, predicting the result in advance at any campus becomes virtually impossible.

"I applaud Tennessee for being bold with this plan," said Carl Hite, president of Cleveland State Community College in southeastern Tennessee. "No other state has come close to going from 100 percent seat-count funding to 100 percent outcome funding. At this point, though, I don't think anyone knows how the system will play out for their campus."

An analysis by Complete College America shows that only 12 percent of Tennessee's ninth graders will eventually earn a four-year or two-year degree.

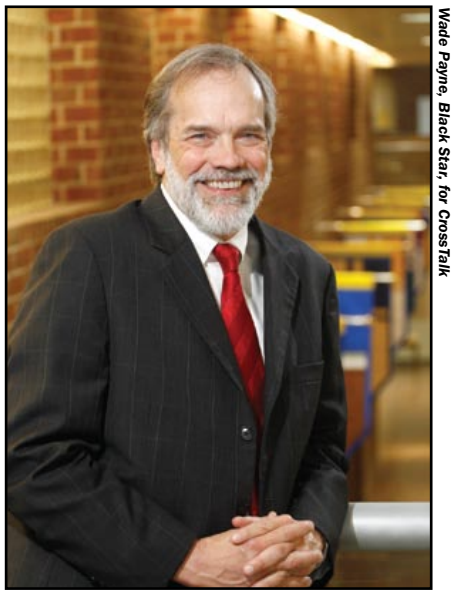
To add some clarity—and perhaps to get the juices flowing—THEC has posted a "dynamic model" of the new funding mechanism on its website that allows administrators to play with different outcomes. A college president, for example, can plug in an improvement in freshmen retention and see the extra dollars flowing to the campus. Since the dynamic model assumes a zero-sum environment, he can also see equivalent dollars being subtracted from other campuses.

Hite said he suspects every campus president has spent some time with the dynamic model, spinning out scenarios, and he laughs about his own experiences. "If I have a target of 100 in a certain area and I type in a result of 110, I can see how much we get, and then I can see who's going to be mad at me because I took their money. When someone wins, someone else loses."

The complexity of the system also raises the question of whether it could be gamed by clever campus officials. For example, if retention and graduation rates reign supreme in the new system, could some institutions raise their scores by judiciously reducing the number of risky freshmen they admit? Could graduation awards, or other criteria results, be shifted from one year to the next?

Rhoda, the executive director of THEC, concedes that any funding system is vulnerable to manipulation, but he believes the new model will prove to be more honest than its predecessor. "In the past, with enrollment funding, the game was to bulk up in the fall when students were counted," he said. "The new approach has been pored over by campus presidents and chief academic officers, and we've tried to keep it as straightforward as possible. If soft spots show up with the new system, we can fix them."

John Morgan, the Board of Regents chancellor, says another wrinkle lies in the system's subtle but perverse incentive for administrators to withhold strategies that prove successful. "If you are a campus president and you find the secret of success, you might want to keep it to yourself because your discovery



Wade Payne, Black Star, for CrossTalk

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gives you a competitive advantage," he said.

The answer might be a device that rewards collaboration, allowing the originator of a new strategy to share in the success of others who adopt it.

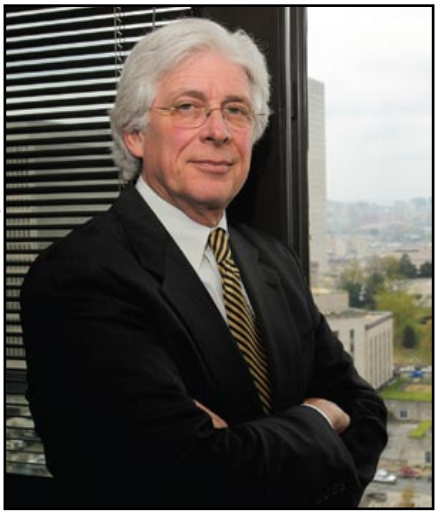
The largest uncertainty surrounding the new funding system, however, is not the response on the campuses where, as one administrator said, "we've all drunk the Kool-Aid." Rather, it's the response in Nashville where a new Republican governor and a legislature with 20 newly elected conservative Republicans will hold sway over the higher education system and its budget.

Haslam, the new governor, took office in January and thus far has voiced support for the outcome-based program. Haslam comes from a wealthy family in Knoxville that has a long history of involvement with the University of Tennessee, and he made higher education reform a central part of his gubernatorial campaign.

The legislature is more of a wild card. It turned decidedly more conservative after last November's election, and many of the new members campaigned on a small-government platform.

Higher education officials say they have little fear that the legislature would attempt to dismantle or seriously tinker with the program. After all, the system reflects many Republican ideas in regard to government.

The anxiety, the officials say, stems from the fear that the legislature and Haslam may not accept what the higher education community sees as the implicit political deal of the new system. In a nutshell, that perceived deal says that if higher education succeeds in its gamble and operates at higher efficiencies, then the state will reward it financially. It amounts to pay-for-performance, another Republican ideal.



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Richard Rhoda, executive director of the Tennessee Higher Education Commission, believes the new funding system will prove to be more honest than its predecessor. "We've tried to keep it as straightforward as possible," he says.

Education officials argue that this deal is not merely a matter of fairness. Rather, it is crucial for the new system to survive and thrive.

Joseph DiPietro, president of the University of Tennessee, described the problem this way: "If everyone performs well and the funding stays flat, we will see some institutions with improved performance who receive fewer dollars because others improved even more. That's when the in-fighting will start."

Right now, said DiPietro, "We are all locked arm in arm, and we are convinced this is going to be a major step forward. With flat funding, that attitude could erode."

Morgan reiterated that rewarding better performance is "the key to the program's success. Without it, you're going to get cynicism and resentment. College administrators are not going to bust themselves trying to increase productivity if they believe they will be punished for it. Nobody wants that."

Hite, the president of Cleveland Community College, noted that the old route of increasing budgets by increasing enrollments has been taken away, and college presidents now need the assurance of another route toward expansion other than snatching funds from their brother institutions.

Dennis Brack, Black Star, for CrossTalk

"The most elegant reform plan will do no good if it's not supported by high officials in the state," says Stan Jones, president of Complete College America. "In Tennessee the leadership has consistently provided support."

"The legislature told us that the new standard would be the outcomes at our institutions. OK, that's fine, but if we measure up to the new standard, don't come back and say we have to cut you more," Hite said.

The crucial year, the educators say, will be 2012, when the financial results of the outcome funding are first felt on the campuses. If the state provides enough money so that every campus with improved performance sees an uptick in funding, the new system may be over the hump.

But the idea of an implicit deal is greeted with some skepticism in the state capital. Mark Cate, a senior advisor to Governor Haslam, said the question of whether improved performance would be rewarded with more funding is "impossible to answer today. Appropriations are always a matter of what's possible and what's not. Everyone is also curious how the new (Republican) players in the legislature will affect things going forward."

Jamie Woodson, a Republican state senator and a co-author of the Complete College Tennessee legislation, agrees that reform in a zero-sum game is "a real challenge for the leadership in higher education."

"At the end of the day, though, that's their job. It's not about getting more money," Woodson said. "What I'd want every institutional leader to do in the morning when they get in the shower is think what they can do to align their institution with the needs of the state, which means making Tennessee a more competitive place for growth and jobs."

Right now, Woodson added, "rewarding higher education with larger budgets is not part of the conversation. The conversation is about outcomes."

Ultimately, the fate of the funding issue will depend on economic recovery in Tennessee over the next year, which is unpredictable. As of yet, a resurgence in the economy and tax revenues has not occurred in any dramatic fashion. Several weeks after Woodson made her comments, Haslam unveiled his budget for the upcoming year. It proposed a two percent cut in higher education. ◆

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