



INSTITUTE FOR HIGHER EDUCATION
LEADERSHIP & POLICY

INVEST IN SUCCESS:

*How Finance Policy Can Increase Student Success
at California's Community Colleges*

by

Nancy Shulock and Colleen Moore

Institute for Higher Education Leadership & Policy

California State University, Sacramento

October 2007



CALIFORNIA STATE UNIVERSITY
SACRAMENTO
Institute for Higher Education Leadership & Policy

6000 J Street, Tahoe Hall 3063 | Sacramento, CA 95819-6081
T (916) 278-3888 | F (916) 278-3907 | www.csus.edu/ihe



INSTITUTE FOR HIGHER EDUCATION
LEADERSHIP & POLICY

INVEST IN SUCCESS:

*How Finance Policy Can Increase Student Success
at California's Community Colleges*

by

Nancy Shulock and Colleen Moore

Institute for Higher Education Leadership & Policy

California State University, Sacramento

October 2007



Acknowledgments

The authors are grateful to the William and Flora Hewlett Foundation for providing funding for this research. The report benefited from the thorough review, at various stages, by Jim Austin, Kathy Blackwood, Dona Boatright, Steve Boilard, Pamela Burdman, Bernadine Chuck Fong, Mary Gill, Bruce Hamlett, Dennis Jones, Mark Wade Lieu, David Longanecker, Patrick Murphy, Tom Nussbaum, Brad Phillips, Bob Shireman, Michael Shires, Erik Skinner,

Abdi Soltani, John Spevak, Paul Steenhausen, Robert Turnage, David Wolf, and Bill Zumeta. We received helpful research assistance from Jackie Chin, Angela Owens, and Eric Mao. We are grateful to the many individuals in the California Community College system who provided information, documents, and opinions related to finance policies. The analysis and conclusions are, of course, those of the authors.

Table of Contents

Executive Summary	iv
I. Introduction	1
Declining Fortunes	1
An Expanding Focus: Ensuring Access to Success	2
Aligning Policy with State Priorities	3
Identifying State Priorities	4
Finance Policy and Student Success	6
Outline of Report and Research Methods	7
II. Policy Audit	8
Overview of California Community College Funding	10
Proposition 98	10
Apportionments	12
Enrollment Growth	15
Categoricals	18
Restrictions on the Use of Appropriated Funds	25
Student Fees	31
Financial Aid	36
III. Summary and Conclusions	43
Policies Undermine State Priorities	43
Policies Do Not Provide Colleges the Means to Fulfill their Missions	45
Affordability Policy is Needed	47
IV. Directions for Future Reform	49
National Reform Efforts	50
Investing in Success	52

Executive Summary

Declining Fortunes

There is growing concern about the declining economic competitiveness of the United States relative to both established and developing nations. A telling indicator of declining fortunes is that this country is doing less well in educating new generations than are many other nations. Countries that are doing better at educating their young people will see rising educational attainment compared to the United States, where educational attainment is declining. As other countries are doing a better job educating young people than is the U.S., other states are doing a better job than is California. California's rank among states in the educational attainment of the working-age population is slipping.

A second telling indicator is the contrast between access to higher education and completion of college programs. The U.S. is near the top in international comparisons in college participation rates but close to the bottom in completion rates. California is near the bottom of the pack, nationally, in a country that is struggling to keep pace globally, placing 46th among states in the number of bachelor's degrees awarded per 100 undergraduates enrolled. A slate of recent studies has concluded that California will need to increase degree attainment among its own population if it is to meet the need for college educated citizens and workers.

In a 2007 study entitled *Strategies for Improving Student Success in Postsecondary Education*, Arthur Hauptman suggests that the nation's lack of college success and inability to close the equity gaps stem from policy priorities and funding systems that favor access over readiness and success. Our study examines whether state policies in California stand in the way of greater student success. We examine finance policy for the California Community Colleges (CCC) in an effort to understand whether policies are well targeted to help the state reverse its declining fortunes or if policy changes are needed. We focus

on community colleges because they serve by far the most students and can have the biggest impact on the trends cited above – not because policies for the other segments of education are presumed to be satisfactory.

An Expanding Focus: Ensuring Access to Success

The good news is that after decades of state and federal policy attention to increasing access to higher education in this country, there is now considerable focus across the country on improving student success in college. The CCC system has signaled its commitment to student success with a new strategic plan with a goal of “student success and readiness,” an annual conference on student success, a new initiative to increase student success in basic skills, and countless local efforts to increase student success.

The catch is that public policies don't often support the rhetoric around student success. A commitment to increase student success, no matter how genuine, is not enough if public policies work at cross purposes. If we know that today's students require intensive support services but we don't give colleges the resources and the authority to provide those services, we should not expect students to succeed. If we know that heavy work schedules prevent students from giving enough attention to their studies but our policies leave students with insufficient financial aid, we should not expect students to succeed. We should change the policies that impede student success.

Policy barriers can frustrate the best efforts to improve practices at the colleges. Resource constraints are certainly at the root of these frustrations and must be addressed, but whatever the level of funding, policies must be designed deliberately to accomplish their intended purposes. What is needed are resources *and* policies that ensure that resources are used effectively to promote student success and California's prospects.

Aligning Policy with State Priorities

Effective state finance policy must reinforce state priorities and provide colleges with the necessary means to meet those priorities. Finance policy is a powerful tool because it sends strong signals about what's important and provides incentives for certain behaviors. But finance policy sends signals whether or not the policies have been explicitly chosen to align with real priorities. The signals embedded in the policies create *de facto* priorities, which may not be the priorities that policy makers would explicitly embrace. Like many other states, California has no *explicit* priorities for its higher education system other than the broad tenets of the 1960 Master Plan for Higher Education. That makes it more likely that outcomes are driven by *de facto* priorities rather than priorities that reflect conscious choices of lawmakers and vital needs of the state.

A 2004 report, *Ensuring Access with Quality to California's Community Colleges*, concluded that current community college finance mechanisms provide barriers to success rather than promoting it. It recommended a comprehensive review of finance policies to understand whether policies, collectively, are accomplishing their intended purposes. This report presents the results of such a review. We looked at finance policy, broadly defined to include appropriations, categorical programs, restrictions on the use of funds, and policies on fees and financial aid. We examined the incentives embedded in these policies that influence the actions of institutions and students, who respond rationally to such incentives. Our purpose is to understand whether the policies promote, or undermine, state priorities.

Claiming that colleges and students respond to incentives is only to credit them with being rational, and in no way suggests any lack of commitment to success. To the contrary, faculty and staff have demonstrated a strong commitment to student success through the strategic plan and several ongoing system initiatives. But money *matters*, especially to the resource-poor community colleges whose faculty and staff must always be concerned with next year's budget simply to survive. In an effort to provide the best education possible, college faculty and staff are sometimes driven to maximize revenues and respond to fiscal incentives – even when those actions may not be best for students. As the

bestselling book *Freakonomics* points out, incentives explain how things *are*, not how we would like them to be.

Identifying State Priorities

In the absence of official policy objectives for higher education, the analysis draws upon the priorities outlined in pending legislation. SB 325 (Scott) – called “Postsecondary Education: Educational and Economic Goals for California Higher Education” – contains a set of six questions that, together with specific performance indicators and targets, comprise a useful set of state priorities for purposes of this analysis. We adapt these six priorities to a community college focus, and analyze current finance policies to see if they promote or impede achievement of these priorities.

1. ***Increase the college readiness of incoming students***

Some of the most powerful reforms occurring across the country are those that enlist colleges and universities as partners with K-12 to help improve the readiness levels of incoming students. CCC policies can influence college readiness among recent high school graduates as well as adults.

2. ***Provide broad access to higher education for Californians who seek or need a college credential***

Declines in education levels of the population call for increasing the number of educated Californians. Access by those individuals *who seek a college credential in order to enter or advance in the state workforce* addresses this problem. The CCC is authorized to offer instruction that does not lead to credentials and there is strong community support for that role. But from the perspective of meeting public priorities for social and economic vitality, the mission to award educational credentials (including the provision of prerequisite basic skills) takes precedence.

3. ***Ensure that community college education is affordable***

Affordability must address all costs of attending college, including textbooks, transportation, housing, health care, childcare, and other living expenses. Community college fees account for only five percent of college costs. If college is not affordable, when

considering all of these costs and financial aid, students are forced to work too much for their own good, academically. Making college affordable and reducing excessive work hours will improve student success.

4. Increase completion rates for associate degrees, certificates, and baccalaureate degrees via community college transfer

Success in community college includes accomplishments other than program completion, but the economic prospects for the state are so dim without huge gains in educational attainment among growing populations that a focus on program completion is justified. Across the nation, community college success is defined in terms of degree completion, as evidenced by major national projects to improve student success and the goals set by many states.

5. Meet the needs of the state and regional workforce

Often described as the engine of California's economy, the community colleges are critical to preparing the workforce. The CCC can sustain that engine in several ways: quality programs that give students the knowledge and skills to succeed in the 21st century workplace; programs that collectively meet the needs of the state, with a particular focus on addressing the shortfalls reported in fields such as nursing, teaching, and science and math professions; and responsiveness to the distinct workforce and training needs of each college's local region.

6. Ensure the efficient use of public funds invested in higher education

It is important that community college finance policies promote the efficient use of public funds because funding is scarce in relation to the extensive and critical set of missions. Resources are invested efficiently if they are directed to areas of greatest need and achieve the best results possible for a given level of investment.

Finance Policy and Student Success

This is an opportune time for a systematic look at finance policy, with mounting pressures on the CCC to account for increased success, the system's own commitment to student success, and lawmakers' growing awareness that community colleges are vitally linked to future economic and social health. The finance reforms enacted in 2006 pursuant to SB 361 have earned broad support for increasing the equity of allocations across districts. This accomplishment could provide a basis on which to build the next stage of reforms that would extend the focus beyond base appropriations to other dimensions of finance policy and from *district equity* to *student success*.

As we documented in a policy brief, *Rules of the Game*, too few CCC students are completing degrees and certificates. Colleges need the capacity – both resources and supportive public policies – to ensure that more students can meet their educational goals. *Rules of the Game* identified two domains of state policy that impede college efforts to help students succeed. One is enrollment and course-taking patterns that students follow, including the counseling and support they receive in making those decisions. We subsequently issued a detailed report, *Beyond the Open Door*, that analyzed those policies and offered recommendations for increasing student success. This report addresses the second policy domain highlighted in *Rules of the Game* – state finance policies that affect how much money the colleges have, how they may use those funds, and how student enrollment is supported through fees and financial aid.

State appropriations per full-time student at the CCC are less than 60 percent of that for students at the California State University (CSU) and less than one-third that of students at the University of California (UC). When fee revenues are accounted for, the revenue differential is vastly magnified because the CCC collect very little student fee revenue compared to the four-year institutions. Strict comparisons are hard to interpret in view of the different missions assigned to each segment and the inability to compare expenditures for undergraduate students. But the large remedial mission performed by community colleges is more expensive than has typically been recognized in community college funding levels across the nation. Community

college students generally require considerable institutional resources if they are to succeed.

In view of the state's continuing structural budget deficit, there are unlikely to be more than incremental gains in per-student funding in the near future. This will continue to put a premium on the effective use of limited resources. This report, through a systematic review of finance policies, seeks to determine whether the people of California are, as the title of this report suggests it is possible, investing in success.

Policy Audit Findings

The report includes extensive descriptions and analyses of the complex realm of community college finance policy. For descriptions of the policies and a full analysis, the reader will have to consult the full report.

Proposition 98 creates a disincentive for cooperation between K-12 and CCC on college readiness reform and fails to direct funding toward the greatest need with respect to enrollment growth trends within each sector.

Base funding policies create pressures to maximize early term enrollments but give no financial incentive to improve outcomes such as persistence, course completion, degree completion, or student learning. They provide no incentive to enroll students (e.g., degree seeking, low-income, underserved) who would increase overall educational attainment levels in the state. Some of the means to increase enrollment, such as allowing late registration and minimizing course prerequisites, work against student completion. There are disincentives to invest in high cost programs.

Enrollment growth policies create incentives for districts to expand enrollment, but only up to a specified cap. High-growth districts have little means to respond to excess enrollment, which could impede access. Low-growth districts are encouraged to recruit students. The method for allocating district caps can create a disconnect between actual need and authorized enrollments.

Categorical funding, as implemented, is a flawed mechanism for addressing priorities. In a system of local and state-level governance, categorical funding could potentially steer districts toward meeting high priority

state goals. However, there is no apparent logic as to which programs receive categorical funding, as it is used to support core functions such as student advising and compensation for part-time faculty. The stated goals of the categorical programs are not always promoted by the funding mechanisms. Categorical programs impose unnecessarily high administrative costs on colleges. By segmenting a college budget into various protected pieces, categorical funding prevents colleges from developing college-wide priorities for the allocation of resources.

Restrictions on the use of funds deprive college leaders of flexibility and authority they need to manage their institutions. Community colleges are locally governed in order to meet the diverse needs of the state's communities. Having one-size-fits-all requirements for how colleges can spend their funds, who they can hire, and for how long discounts the local variations and the ability of college leaders to know how best to manage their funds.

Fee policies are principally about keeping fees low to promote access. Low fees promote high rates of college participation among broad populations, many of whom never complete an academic credential or seek to complete one. Although low fees are largely responsible for per-student funding being well below the national average, there is virtually no stakeholder support for increasing fees. College funding derives largely from FTES so any action that could reduce enrollment is opposed. In addition, fee revenue is deducted from state funding entitlements so it is not treated or viewed as a potential source of additional revenue that could increase access and success.

Financial aid in the form of waived fees and Cal Grants reduce financial barriers to access, and the Cal Grant program contains some incentives for students to prepare and perform academically. The fee waiver program has no incentives for students to prepare for college or make academic progress once enrolled. The Cal Grant award has declined severely in purchasing power to the point where students face serious affordability problems, even with an award. With the emphasis on keeping fees low as the primary means to make college affordable, policy has given insufficient attention to the larger costs of college.

Table ES-1
Summary of Policy Alignment with Priorities

	Readiness	Access	Affordability	Completion	Workforce	Efficiency
Proposition 98	-	-		-	-	-
Apportionments	-	+/-		-	+/-	-
Growth	-	+/-		-	-	-
Categoricals:						
Matriculation	-	+/-	-	-	-	-
EOPS		+	+	+	+	-
DSPS		+		-		-
Part-time Faculty		+/-		-		-
Financial Aid Administration		+	+	-		+/-
Expenditure restrictions:						
50% instruction	-	+/-		-	-	-
75% / 25%		-		+/-	-	-
60% part time		-		-	-	-
2 semester temporary		-		-	-	-
Student employment			-	-		-
Fees:						
Lack of policy		-	-	-		
Low fees		+/-	+/-	-	-	-
Waivers		+	+/-	-	-	-
Revenue offset		-		-	-	-
No fee non-credit	+	+/-	+	+/-	+	-
Prohibit campus fees	-	-		-		-
Financial Aid:						
BOG waivers	-	+/-	+/-	-	+/-	-
Cal Grant	+/-	+/-	+/-	+	+/-	+/-
Focus on fees		-	-	-		-

Key: + indicates that the policy promotes the priority

- indicates that the policy fails to promote, or works at cross purposes to, the priority

As a result, community college students do not get all the financial aid for which they are eligible. Lack of aid causes students to work more than necessary, which is a serious factor in their lack of success.

Policies Undermine State Priorities

Table ES-1 summarizes the analysis of the policies with respect to the six priorities. A “+” indicates that the policy promotes the priority; a “-” indicates that the policy fails to promote, or works at cross purposes to, the priority. This summary does not reflect the different magnitudes of the effect of each policy, but it does reveal a substantial misalignment between policies and priorities. The greatest alignment is with the access priority, but even those policies do little to encourage access by the growing numbers of under-served Californians – precisely those individuals whose education is most likely to stem the decline in educational attainment and workforce quality.

The analysis of policy impact is predicated on the proposition that people, both individually and as institutional representatives, respond to incentives. An assertion that faculty, staff, and students respond to fiscal incentives entails no judgments about their values. When enrollment-driven funding leads colleges to allow late registration beyond what they know is good for student success, it is not because colleges care little about student success. They are playing by the rules of the game that have been established for them as they strive for financial survival. If a student continues for several terms without seeing a counselor and makes no forward progress toward her goals, it is not because she doesn’t care about her future but likely because the wait to see a counselor is too long and there is no need to make forward academic progress in order to renew her fee waiver.

Policies Do Not Provide Colleges the Means to Fulfill their Missions

The CCC is expected to fulfill a broad and costly set of missions at a fraction of the cost of universities. Experts have warned against ignoring capacity issues when developing policies to promote college access. Access is of little value to students if colleges cannot accommodate them and serve them effectively. Ensuring that colleges have the means to

fulfill their missions goes beyond funding levels and includes the freedom to use resources – whatever their level – most effectively. This requires a set of policies that do not work at cross purposes to system and student effectiveness. It requires that colleges have the decision-making authority to direct resources to where they are most needed.

Our analysis has revealed a very strong emphasis on policies that stimulate enrollment without an equivalent policy focus on getting the CCC system the resources and decision-making authority it needs to serve these large numbers of students effectively. The funding available to the system is determined more by K-12 enrollments than by community college enrollment demand and total funding is artificially capped by formula. There is very little fee revenue available to the system and that which is collected does not augment college budgets. The distribution of core and targeted funds to districts places other factors before the needs of students and communities. Regulatory restrictions seriously impede local discretion to make the best use of resources.

Affordability Policy is Needed

The long-standing assumption that keeping fees low (and waiving them for needy students) will ensure affordable community colleges has proven misguided. There is a serious affordability problem in the CCC that has little to do with fees. A comprehensive affordability policy must be developed to (1) address the full costs of college attendance, (2) take full advantage of federal grant and loan programs, (3) increase the purchasing power of Cal Grants, (4) establish an institutional aid program in the CCC similar to the State University Grant Program and the University of California Grant Program, and (5) consider whether higher fees for *non-needy* students could *increase* access and success by augmenting state appropriations with much-needed revenues.

Those who oppose fee increases express genuine concerns that any fee increase will reduce access among the at-risk and poor students who depend on the community colleges for a secure future. But no one who cares about the economic and civic health of the state wants to deprive needy Californians of an education. *The question is whether access for those individuals can be protected in such a way that does not deprive the institution of needed resources.*

Proponents of no- or low-fee community colleges would like to see the state budget reflect different policy choices. But the same demographic changes that have shaped today's community college are increasing the competition for state funds – for an array of health and social services required by the growing numbers of immigrants and disadvantaged populations. In view of these competing priorities and the tax-limited environment in which we live, it may be that current fee policies can be maintained only at the expense of inadequate funding for the community colleges to serve students.

Not all community college students are low-income. By design, a full two-thirds of California high school graduates are ineligible for direct enrollment in UC or CSU and are directed to community colleges if they attend in-state public institutions and many others choose to attend a community college for reasons of convenience and access to quality teachers and programs. The median household income of dependent CCC students is similar to that of all California households. This suggests that many CCC students would not be financially disadvantaged by a modest increase in fees. It is time to take a fresh look at the relationship among fees, financial aid, state support and access to see if there are options other than waiting for taxpayers' and lawmakers' priorities to change.

Directions for Reform

Various groups have identified problems with CCC funding mechanisms in recent years, including the Assembly Committee on Higher Education, whose working group identified in 2004 some of the same problems that our research has confirmed, such as under-funding with respect to mission, extensive bureaucratic restrictions, and limited district flexibility to raise additional revenue. Independently, the CCC system convened a working group of finance experts that recommended changes that led to the enactment of important reforms, but the reforms did not address some of the broader issues raised by others and confirmed here.

Inspired by national policy experts and organizations, there is a great deal of activity across the country in exploring or implementing new approaches to finance policy to help accomplish state priorities. In many cases these new

directions recognize that finance policies often mistakenly steer people in ineffective directions. We have categorized these approaches by (1) whether they aim to influence the behavior of colleges or students and (2) which of the six proposed priorities they address, and we list them in the full report. It is our intention to encourage conversations in California about how the state might adapt some of these ideas to our circumstances and design fair and sensible budgeting systems that can help college faculty and staff increase student success.

Investing in Success

The new directions in policy reform show that investing in success applies to all aspects of finance policy – not only to the way that annual budgets are allocated to colleges. It applies to eligibility requirements for financial aid, fee policy, flexibility in the use of resources, differential funding for higher cost programs and services, faculty salaries, and collaborative efforts between colleges and high schools. A variety of strategies along these lines might be used to improve student success. They are not typically thought of in the context of finance policy reform, but they should be.

Policies that affect basic college allocations create the most powerful incentives because they affect the distribution of core funding. If Californians are to invest wisely in the success of community college students, it is vital that funding mechanisms be structured to include incentives for achieving positive outcomes. The question, which continues to perplex American higher education, is *how best to incorporate measures of success into funding decisions*.

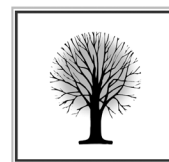
Performance funding has largely failed across American higher education and has a deservedly bad reputation among educators. The conventional wisdom behind performance funding is fundamentally flawed because it assumes that a very small pot of funds set aside to reward performance after the fact is going to change the nature of the enterprise. When those changes don't result, the performance fund is typically deemed expendable – usually after a short trial period, such as occurred with the Partnership for Excellence program (PFE) in the community colleges.

There is a better approach, which we call *investing in success*. The fundamental difference is that investing in success acknowledges that improving performance is not an add-on responsibility. It is an ongoing and costly undertaking and should be *institutionalized* into the basic funding formula so as to provide a stable and significant funding source. *Investing in success* changes the incentives built into core funding while performance funding leaves the current incentives in place and sets up a small categorical program to fund performance. Funds earned under an *investing in success* model are, by definition, part of a college's base funding, while funds earned under traditional performance budgeting approaches are bonuses that may or may not last.

Investing in success works by *re-conceptualizing the workload* that state funding covers through the basic allocation. Workload is currently defined as 3rd week enrollment and colleges are funded to serve it. Additional workload factors could be added, such as teaching students for a full term, serving financially disadvantaged students, guiding students through basic skills, enrolling students in specified programs, or producing certificates and degrees. These are just a few of the many possibilities for redefining workload to align funding with priorities. The full report includes a hypothetical illustration of how this model works and how the inclusion of different performance-related workload factors can alter a college's funding level without the setting of arbitrary targets and the imposition of rewards or penalties.

Under this approach, the state's investment in success increases each year as workload growth funds are provided to the system. This ensures that college progress is not funded at the expense of other colleges. Investing in success has the additional advantages over traditional performance funding of sending the message that performance is something to be institutionalized – not pursued at the margins and at some times but not others.

Change in finance policies will not come easily. There are powerful political interests behind the current policies. But there is too much at stake for the future to acquiesce to policies that place the needs of stakeholder groups ahead of the needs of students and California's economic future. It is essential to find finance mechanisms that will ensure that California invests enough in its community college system and invests in success.



INVEST IN SUCCESS

I. Introduction

"Whereas for most of the 20th century the United States could take pride in having the best-educated workforce in the world, that is no longer true."

Tough Choices, Tough Times, Report of the New Commission on the Skills of the American Workforce

"Americans know that the U.S. risks falling behind and understand the relationship between education and competitiveness."

Innovation and U.S. Competitiveness: Addressing the Talent Gap, Business Roundtable

"There is a crisis in American higher education...Too many students are falling through the cracks. As a result, U.S. citizens are not achieving their full potential, state economies are suffering, and the United States is less competitive in the global economy."

Transforming Higher Education, National Conference of State Legislatures

Declining Fortunes

There is a growing concern among the nation's leaders about the declining economic competitiveness of the United States relative to both established and developing nations. As one example, the U.S. Secretary of Education's Commission on the Future of Higher Education was established in 2005 to develop a national strategy to ensure the U.S. can compete effectively in the global economy. The following year, the National Conference of State Legislatures laid out its case for *Transforming Higher Education* calling it a "national imperative."¹ The National Governors' Association joined in with its annual conference in 2007, called *Innovation America*, focused on "...helping colleges and universities better prepare the workers of tomorrow..."²

A telling indicator of declining fortunes is that this country is doing less well in educating new generations than are many other nations. While the U.S. is second only to Canada among the twenty-nine Organization for Economic Cooperation and Development (OECD) nations in

the percent of its population ages 35 to 64 with an associate's degree or higher, its ranking falls to eighth when the 25 to 34 age group is considered, with several countries poised to overtake the U.S. in the next several years.³ Countries that are doing better at educating their young people will see rising overall educational attainment compared to the United States, where educational attainment is projected to decline.

As other countries are doing a better job educating young people than is the U.S., other states within the U.S. are doing a better job educating young people than is California. California ranks second among the 50 states in the share of the population age 65 or older with an associate's degree or higher, but its rank declines with each successively younger age group. Among younger workers ages 25 to 34, California ranks 30th among the states.⁴ The failure to keep up with other states in educating younger generations is contributing to California's relative decline in overall educational attainment. While California remains slightly above the national

average for the percent of the population with an associate or higher level degree, over a fifteen year period the gap between California and the national average has narrowed.⁵ This means that educational attainment in California is growing more slowly than the nation as a whole. If this trend continues for even a few more years, California will fall below the national average in the educational attainment of its population.

A second telling indicator is the contrast between access to higher education and completion of college programs in both the United States and California. OECD data from 2004 show that the U.S. is near the top among OECD nations in college participation rates but close to the bottom in completion rates.⁶ And California is near the bottom, nationally, in a country that is struggling to keep pace globally, placing 46th among states in bachelor's degrees awarded per 100 undergraduates enrolled. A slate of recent studies has concluded that California will need to increase degree attainment among its own population if it is to meet the need for college educated citizens and workers.⁷

In a 2007 study entitled *Strategies for Improving Student Success in Postsecondary Education*, Arthur Hauptman asks why the U.S. has done so much better at achieving high levels of access than in promoting student success.⁸ His answers have everything to do with public policy and the influence that policy has on educational outcomes. He offers three policy-related explanations for the lack of college success and, in particular, for our nation's inability to close the equity gaps throughout the educational pipeline:

- Funding and policy priorities favor access over readiness and success.
- Federal and state policies are not well targeted toward low-income students.
- There is a disconnect between policy design, implementation, and effect.

This study asks whether we might similarly conclude that state policies in California are standing in the way of greater student success. In particular, the study examines finance policy for the California Community Colleges (CCC) in an effort to understand whether policies are well targeted to help the state reverse its declining fortunes or if policy changes are needed.

An Expanding Focus: Ensuring Access to Success

The good news is that after decades of state and federal policy attention to increasing access to higher education, there is considerable focus across the country on improving student success in college. Much of this effort involves community colleges, where the common goal is to increase the numbers of certificates and degrees awarded to community college students and the transfers to four-year institutions.⁹ States are giving particular emphasis to improving student readiness for college, because academic preparation in high school has a powerful influence on college success.¹⁰

The California Community College system has signaled its commitment to student success with a new strategic plan that identifies a key goal of "student success and readiness,"¹¹ an annual conference on student success,¹² a new system-wide initiative to increase student success in basic skills,¹³ and countless local efforts aimed at increasing student success.

But there is a catch: a commitment to increase student success, no matter how strong and how genuine, is not enough if public policies work at cross purposes. If, as a nation, we realize that open-access institutions hold the key to future prosperity because they serve the vast majority of students, but we continue to fund them far less generously than selective institutions, we should not be surprised if educational attainment levels don't rise. If we lament the low levels of enrollment by low-income students in selective colleges but continue to award institutional financial aid on the basis of merit, irrespective of financial need, we cannot expect much change in enrollment patterns.

Moving closer to home, if we know that a rigorous high school curriculum is the best predictor of college success and that most incoming community college students need remediation, but our policies do not clearly communicate college readiness expectations, even the best efforts to improve outcomes in basic skills courses are disadvantaged from the start. If we understand the importance of student support services to today's students but our policies limit the hiring of counselors and other student services staff, we should not be surprised when colleges can't steer students toward success. If we grasp the severity of the nursing

shortage in California, but our policies make it difficult for community colleges to expand nursing enrollment and hire nursing faculty, we shouldn't hope to alleviate the shortage. Finally, if we know that heavy work schedules prevent students from giving enough attention to their studies but our policies leave students with insufficient financial aid, we should change those policies.

Changing public policy is not easy. Nor is it typically seen as part of the job of college faculty and staff. So in the pursuit of increased student success they engage in professional development, write grants in the hope of piloting new programs, review data, and advocate for more funding. They do all they can, in the absence of systematic efforts to address structural barriers, but are so often frustrated by the lack of scalability of small efforts that show promise for improving outcomes. Certainly resource constraints are at the root of these frustrations and must be addressed. But public policies matter independent of resource levels. If not well designed to accomplish their intended purposes, policies can provide roadblocks to student success. What is needed is a combination of additional resources and policies that put resources to the best use.

Aligning Policy with State Priorities

Dennis Jones, a leading expert on higher education policy, advises states across the U.S. that in order to be effective, state finance policy must satisfy the following criteria:¹⁴

- Policies should reinforce state priorities.
- The institutional capacity necessary to meet the stated priorities must be created and sustained.
- The contributions required of students and taxpayers should be affordable.

He notes that state finance policy is a powerful tool because it sends strong signals about intent and can provide incentives for certain behaviors. The problem is that it sends signals whether or not the policies have been explicitly chosen to align with real priorities. The signals embedded in the policies create *de facto* priorities, even if those are not the priorities that policy makers would explicitly embrace. Like many other states, California has no *explicit* priorities for its higher education system other

than the broad tenets of the 1960 Master Plan for Higher Education.¹⁵ That makes it more likely that outcomes are driven by *de facto* priorities rather than priorities that reflect conscious choices of lawmakers.

Another aspect of alignment involves integration across various aspects of policy. Jones urges states to ensure that finance policies and decisions are made as a coherent package, not as independent actions, and to recognize that the methods by which funds are allocated are key elements of policy, as different allocation methods elicit different institutional behaviors.¹⁶

Hauptman, in the 2007 report cited above, concludes that “while there is growing rhetorical commitment to student success, the reality is that policies often do not mirror the rhetoric. Whether intentional or not, policies in many states are at best benign and often antithetical to improving student success.” He calls for new forms of finance policy that will “create incentives for students to be better prepared and for institutions to enroll and graduate more at-risk students.”¹⁷

In 2004, the National Center for Public Policy and Higher Education published *Ensuring Access with Quality to California's Community Colleges*.¹⁸ That report called attention to the considerable challenges facing the community colleges. A central critique included in the report's findings is that current community college finance mechanisms “serve to provide barriers to progress rather than promoting it.”¹⁹ The “essential first step” in aligning resource allocation mechanisms to programmatic priorities is to perform a *policy audit* of the system's finance infrastructure, the report concluded.

A policy audit is a means to understand whether policies, collectively, reinforce a state's priorities. It requires taking a comprehensive look at policies – in this case, at finance policies – in marked contrast to the incremental, fragmented way that policy is typically developed. A policy audit reveals to lawmakers whether the *overall* system of laws and regulations that they have designed is likely to get them the results they want.

Key to understanding the likely impact of policy is to examine the incentives embedded in those policies

that influence the behaviors and actions of institutions and students, who naturally respond rationally to such incentives.²⁰ Through the incentives they create, policies define the rules of the game under which institutions and students operate.²¹ If a state seeks certain outcomes, its leaders must understand whether the incentives inherent in the policies are aligned with those outcomes, i.e., whether it is reasonable to expect that institutions and students will behave in ways consistent with the desired outcomes.

Claiming that colleges and students respond to incentives is only to credit them with being rational, and in no way implies that neither is committed to successful outcomes. To the contrary, CCC faculty and staff have demonstrated clearly their strong commitment to student success through the strategic plan and several ongoing system initiatives. But money *matters*, especially to the resource-poor community colleges whose faculty and staff must always be concerned with next year's budgetary allocation simply to survive. Our discussions and interviews with officials across the CCC system confirm that in an effort to provide the best education possible, college faculty and staff are sometimes driven to maximize revenues and respond to fiscal incentives – even when they might question the efficacy of those actions in terms of what is best for students. After all, as the bestselling book *Freakonomics* points out, incentives explain how things *are*, and not how we would like them to be.²²

By identifying these incentives, this report aims to show what California is, in effect, buying with its investment in its community colleges. Further, it seeks to make a case for changing policies so that California will invest in success.

Identifying State Priorities

The *Ensuring Access* report criticized current finance practices for not being aligned with identified needs and objectives. But California has not set forth clear and specific policy objectives for higher education. The tenets of the Master Plan are not nearly specific enough to guide the state's investment of resources.

Important steps toward establishing state priorities have emerged from the Legislature. In 2004, the Legislature passed a bill which set forth four broad goals for higher education as the basis for a first-ever statewide

accountability system for California higher education. The bill was vetoed by the Governor in 2004,²³ but it did signal a willingness on the part of the Legislature to identify statewide objectives to guide policy development.²⁴ This effort has been revived and reshaped in the current legislative session as SB 325 (Scott) – called “Postsecondary Education: Educational and Economic Goals for California Higher Education.” The bill contains a set of six questions that restructure, but are consistent with, the goals adopted by the Legislature in the 2004 version. It addresses the Governor's concerns by specifying performance indicators to track progress in each area along with targets. It was developed with reference to data on the performance of California higher education and thus reflects documented areas of priority need. In its Senate committee hearing the bill received support from the three segments of public higher education. It seems reasonable to consider these a useful set of state priorities for purposes of this analysis.

Adapting these six priorities to a specific focus on the California Community Colleges, we define a set of six state priorities against which we analyze current finance policies. We analyze the policies for the extent to which they promote or impede achievement of the priorities by means of the incentives they contain for colleges and students.

1. **Increase the college readiness of incoming students**

Some of the most powerful reforms occurring across the country are those that enlist colleges and universities as partners with K-12 to help improve the readiness levels of incoming students. The community colleges face tremendous challenges in serving so many students who are under-prepared for college-level work. To the extent that more incoming students are prepared for college – with an adequate academic background and the necessary information about what it takes to become ready for college success – the colleges' task becomes less daunting.²⁵ CCC policies can influence college readiness. Since the community colleges serve large numbers of students who are not entering directly from high school, the colleges play an important role in influencing the readiness of college bound adults as well as of recent high school graduates.

2. *Provide broad access to higher education for Californians who seek or need a college credential*

We address this question from the perspective of the projected decline in education levels of the California workforce and projected shortages of educated workers. Heeding these forecasts calls for improving educational attainment in California, defined in the measurable terms being used across the nation – college credentials that have been shown to correlate with increased personal economic security and state civic, social, and economic health. *Access by those individuals who seek a college credential in order to enter or advance in the state workforce* will yield the greatest benefit to Californians. The CCC is authorized to offer instruction that does not lead to credentials and there is strong community support for those offerings. But from the perspective of meeting public priorities for social and economic vitality, the mission to award educational credentials (including the provision of prerequisite basic skills) should take precedence.

3. *Ensure that community college education is affordable*

Affordability must take into account all of the costs of attending college. College costs include not only fees, but textbooks, transportation, housing, health care, childcare, and other living expenses. In fact, community college fees account for only 5 percent of the costs of college attendance.²⁶ If college is not affordable, when considering all of these costs, students are forced to work too much for their own good, academically, if they are even able to attend at all.²⁷ In our analyses of a cohort of CCC students, we found that students who attended full-time for at least the majority of terms in which they enrolled, had completion rates *four times higher than* students who attended on a more part-time basis.²⁸ To the extent that college costs, even with financial aid, lead students to attend part-time to accommodate more work hours, affordability is a major factor in college success as well as in college access. Put simply, community college students work too much to be as successful as we need them to be. It is in the state's best interest to make college more affordable and discourage excessive work hours.

4. *Increase completion rates for associate degrees, certificates, and baccalaureate degrees via community college transfer*

While success in community college can involve accomplishments other than program completion, the economic prospects for the state are so dim without huge advances in educational attainment among growing populations that a focus on completion of degrees and certificates is justified. Across the nation community college success is being defined in terms of degree completion, as evidenced by major national projects to improve student success. Notable examples include the *Achieving the Dream* project led by the Lumina Foundation and the *Opening Doors* project run by MDRC – both of which state their goals in terms of helping low-income students earn college credentials. Reflecting this focus, the CCC Strategic Plan has a strategy under its student success goal for increasing degrees and certificates awarded.

5. *Meet the needs of the state and regional workforce*

Often described as the engine of California's competitive economy, the community colleges are critical to preparing students for the workforce. This goal is aimed at sustaining that engine through several dimensions: quality programs that give students the knowledge and skills to succeed in the 21st century workplace; programs that collectively meet the needs of the state, with a particular focus on addressing the shortfalls reported in fields such as nursing, teaching, and science and math professions; and responsiveness to the distinct workforce and training needs of each college's local region.

6. *Ensure the efficient use of public funds invested in higher education*

Such benefits will be maximized to the extent that our investment in community colleges provides a good return. It is especially important that community college finance policies promote the efficient use of public funds because funding is so scarce in relation to the extensive mission. Resources are invested efficiently if they are directed to areas of greatest need and achieve the maximum return with respect to meeting the identified goals of readiness, access,

affordability, completion, and workforce needs, as defined immediately above.

Finance Policy and Student Success

Major changes to CCC finance policy were enacted into law in 2006 pursuant to SB 361. These changes were the result of years of hard work by various stakeholders and demonstrate that reform, although hard, is possible. Most observers agree that SB 361 has introduced greater equity into district allocations. This is a true accomplishment in the complex political environment of the CCC, but more work is needed in two respects. First, general appropriations policy is but one part of finance policy; also included are policies on categorical funding, fees, financial aid, and regulations on expenditures. Second, SB 361 was focused on equity to the 72 districts and not directly on outcomes for students. While leveling the playing field among districts to serve students is a worthy objective, and was a legislative priority, it doesn't necessarily address the degree to which all districts can leverage their resources to improve student success. The question is whether lawmakers want to make student success a priority as well.

As we documented in *Rules of the Game*,²⁹ opening the college doors to Californians is not enough today. Too few CCC students are completing degrees and certificates after they pass through the open college door. Colleges need the capacity – both in terms of resources and supportive public policies – to ensure that more students can be successful in meeting their educational goals.

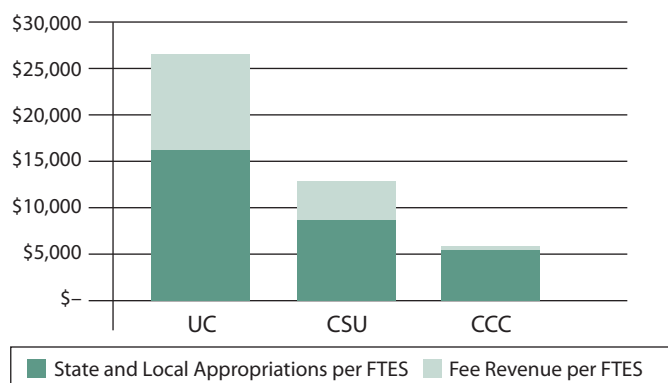
Rules of the Game identified two areas where state policies could be reformed to become more supportive of college efforts to help students succeed. One area relates to the enrollment and course-taking patterns that students follow in college and the kinds of counseling and support they receive in making those decisions. We subsequently issued a detailed report, *Beyond the Open Door*,³⁰ that analyzed those policies and offered recommendations for increasing student success via policy reforms. The second area is finance policy – state policies that affect how much money the colleges have, how they use those funds, and how student enrollment is supported through fees and financial aid. This report is an analysis of how finance policy reform might improve rates of student success in the California Community Colleges.

This is an opportune time for a systematic look at finance policy for the CCC:

- The system has committed itself to increasing student success through the implementation of its new strategic plan.
- There are mounting pressures on the CCC to account for increased levels of student success, including, in particular, increased degree and certificate production to help address the projected shortfall of educated workers.
- There is growing awareness nationally, and especially in California, that community colleges are vitally linked to future economic and social health, as they are the principal route to economic security for so many adults – young and not so young.
- Amid widespread concern that the mission of the CCC may outstrip available resources, it is critical to examine whether policies help or hinder the system in its attempts to leverage scarce resources to accomplish state priorities.
- The SB 361 reforms addressed longstanding concerns about the equity of allocations to districts and thereby created an opportunity to rectify other shortcomings of the current finance policies.

An examination of CCC finance policy must begin with a look at its overall level of resources. Figure 1 shows that government appropriations per full-time student at the CCC are less than 60 percent of that for students at the California State University (CSU) and less than one-third that of students at the University of California (UC). When fee revenues are accounted for, the differential in revenues is vastly magnified because the CCC collect very little student fee revenue compared to the four-year institutions. Strict comparisons are hard to interpret in view of the different missions assigned to each segment. State budgeting practices do not allow comparisons across segments of funding levels *for undergraduate students only*. Nevertheless, the comparatively low level of funding in the CCC puts a premium on the effective use of those limited resources.

Figure 1: Funding for Higher Education, 2006-07



Source: Legislative Analyst's Office, *Analysis of the 2007-08 Budget Bill*

Community colleges are under-funded for the expansive mission assigned to them. The remedial mission served by community colleges is not something that can be done on the cheap. More generally, the students increasingly served by community colleges are those who require more, not fewer, institutional resources, because they bring with them such limited understanding of the dimensions of college success.³¹ Not only do they need quality classroom instruction, but they need a full array of support services to sustain their academic careers.³² But California is not alone in allocating the least amount of resources per student to this sector. In view of the state's continuing structural budget deficit, it may be unrealistic to expect more than incremental gains in funding.

Because they survive with such limited funding, we often hear that the community colleges are "efficient." The community colleges are indeed inexpensive – both for students and taxpayers. But efficiency involves the relationship between inputs and outputs. It is one thing to keep the price low for students and taxpayers; it is quite another to ensure that colleges have the resources they need to serve students effectively.

Outline of Report and Research Methods

Section II of this report applies the policy audit technique in a systematic analysis to determine whether community college finance policies are aligned with state priorities. Because it begins with descriptions of each policy, it provides a comprehensive review of finance policy. It can be used as reference for those who are interested in specific policies

and need not be read in totality in order to understand the conclusions of the research. Section III summarizes the findings of the policy audit with respect to Jones' three criteria for effective finance policy: (1) does policy reinforce state priorities? (2) does it provide the colleges with the capacity to fulfill their missions? and (3) does it require affordable contributions from taxpayers and students?

Section IV describes efforts nationwide to reform finance policy, using the framework of the six state priorities to suggest why California lawmakers may want to consider various alternative approaches. Some of the alternatives are aimed at incorporating performance factors into funding mechanisms. Because there is great controversy over what is commonly termed "performance funding" and because there are better and worse ways to incorporate performance into funding, the report ends with an analysis of how we believe that California can *invest in success* in such a way that avoids the pitfalls of traditional performance funding.

We began the project by convening a group of external advisors, including a leading national expert on the use of policy audits, to identify the most important policies to include in the audit. We defined "finance" broadly to include appropriations, fee, and financial aid policies, as well as the regulations imposed on colleges to guide their use of funds. We pursued four parallel tracks for data collection. The first involved an extensive review of legal and other policy documents to provide background on the policies in question. A second involved interviews with community college personnel to understand how these policies influence actions across the system. These included meetings with the CEO board and the executive boards of the three organizations that represent the vice presidents for finance, instruction, and student affairs. We followed the board meetings with individual interviews. We met twice with the Chancellor's cabinet to share our ideas and seek input into our research. Third, we participated in national workshops on community college finance and associated meetings with national experts to help identify policies in other states that illustrate the use of incentives to accomplish state educational priorities. Fourth, we performed a comprehensive literature search of finance policy reforms being recommended by experts, or being implemented or considered by other states. The draft report was reviewed by over twenty individuals – many of whom are experienced members of the CCC community.

II. Policy Audit

“Policy has become the accretion of many special purpose acts and actions, layered each upon the other.”

Ensuring Access with Quality to California’s Community Colleges, National Center for Public Policy and Higher Education

“Rather than making long-term strategic policy decisions, higher education policy is based on reaction to the latest budget crisis or policy fads. This is exacerbated by the fact that higher education legislative policy is diffused among different legislative committees so that policy and budget decisions often are not coordinated.”

Transforming Higher Education, National Conference of State Legislatures

“We all learn to respond to incentives, negative and positive, from the outset of life.”

Freakonomics, Steven Levitt and Stephen Dubner

This section provides a systematic analysis of finance policies in the California Community Colleges. After an overview of system funding, we analyze the principal finance policies that affect the flow of resources within the California Community Colleges, including:

- policies that govern the way state funds are appropriated to the system and distributed across the 72 districts – base funds and special purpose funds
- the laws and regulations that constrain how those funds can be used
- aspects of fee policy and financial aid policy

Each policy is described and then the incentives it creates for institutions and/or students are noted. For each policy we include a summary table to indicate alignment with six priorities

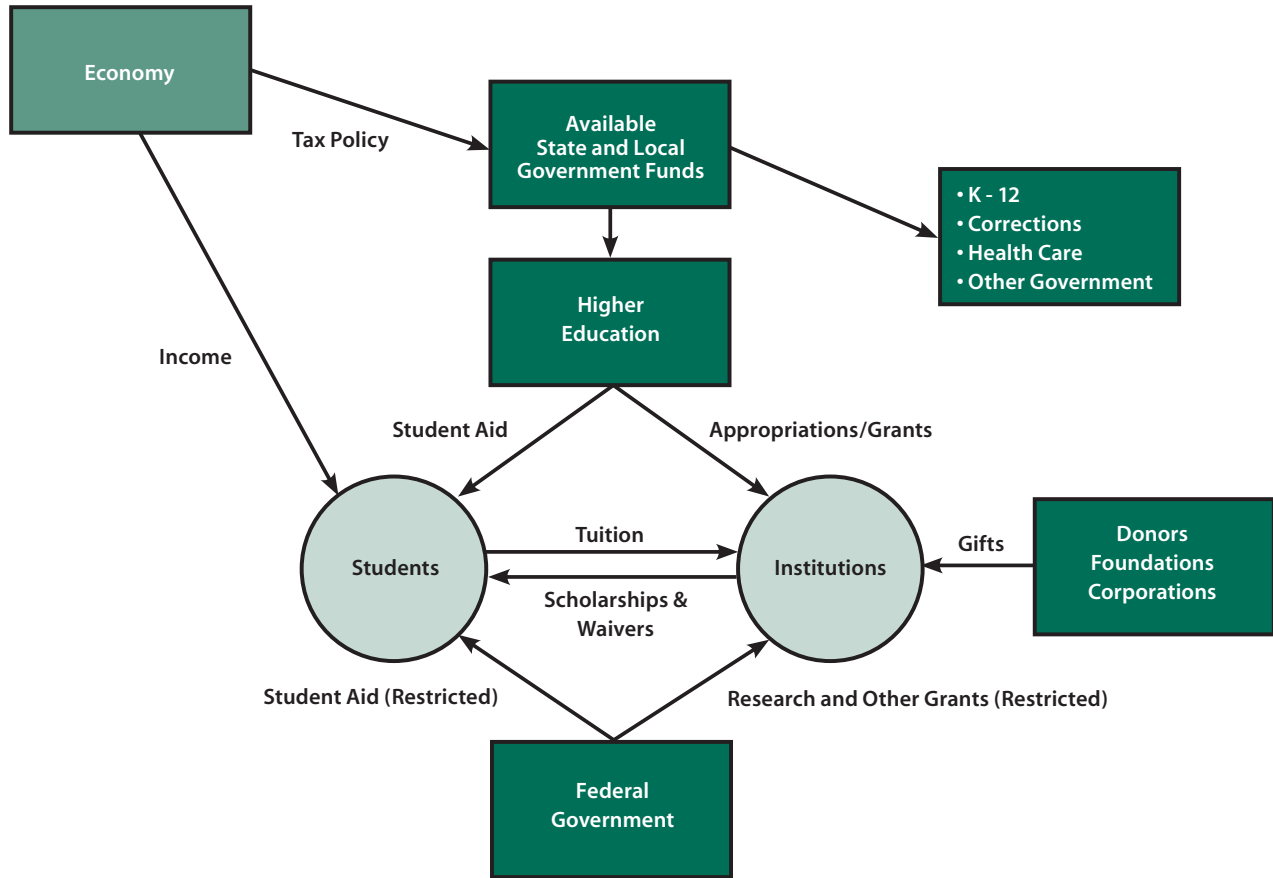
(including only those priorities that are relevant to the particular policy):

1. readiness
2. access
3. affordability
4. completion
5. workforce
6. efficiency

If a policy helps achieve the priority we so indicate with a “+”; if a policy does not support, or impedes, the priority, we so indicate with a “-”. If we find a mixed impact, we assign both scores.

A caveat is in order: the incentives that we identify will be operative in the direction indicated *only* if institutional actors or students are aware of the policy features that contain the incentives. It could be that the state, in a sense, gets away with some poorly designed policies because people are unaware of them.

Figure 2: The Flow of Funds in State Finance Policy



Source: National Center for Higher Education Management Systems (NCHEMS)

Conversely, it could be that well-designed policies fail to have a beneficial effect for the same reason. Our purpose is to examine whether there is an effective framework for accomplishing state priorities.

Our analysis of finance policy is guided by the conceptual framework developed by the National Center for Higher Education Management Systems and the Western Interstate Commission on Higher Education. Figure 2 displays the flow of funds that are influenced by state finance policies. It shows that finance policy encompasses the state's appropriations to institutions, the state's support to students in the form of student financial aid, the flow of funds between students and colleges in the form of tuition and fees collected and waived and scholarships awarded. Good finance policy is achieved when appropriations, tuition/fee,

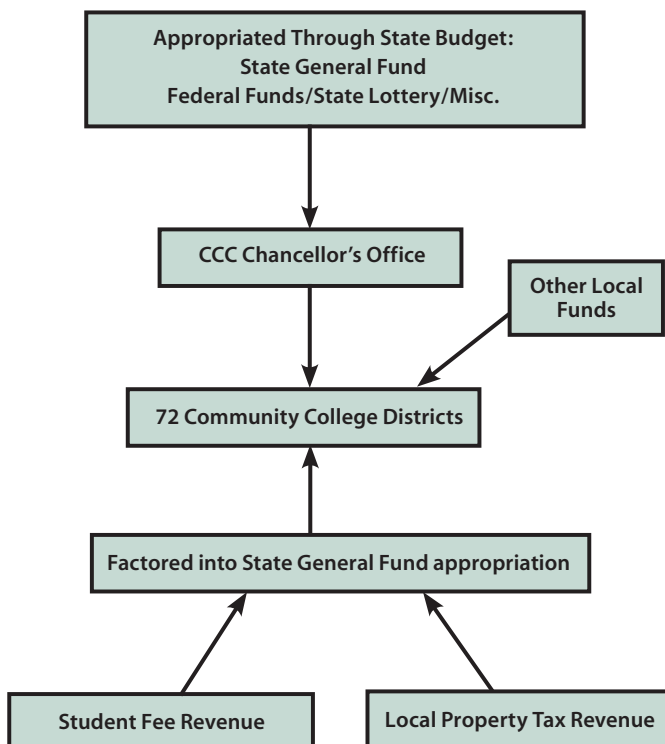
and financial aid policies work intentionally together to reinforce state priorities.

Our goal in this analysis is to encourage new thinking about finance policy and start to build some momentum for reforming parts of the financing structure. It could be helpful, for example, to think not only about how much (or little) money is flowing to the system and its colleges but how that money might be used to encourage student success; to ask whether fee waivers and financial aid programs could change student behaviors as they ease their financial burdens; to question how much regulation of college expenditures is needed and when categorical requirements should supersede local decisions; and to consider how to put more resources under the control of the colleges so they can be appropriately responsive to local needs.

Overview of California Community College Funding

Community colleges receive funding from a variety of sources to support their operations. As shown in Figure 3, these sources include the state General Fund, local property tax revenue, student fees, federal funds, state lottery funds, and miscellaneous other state-controlled funds. Not all this funding is appropriated in the state budget act. Local property taxes and student fee revenue are received directly by districts from local governments and students, respectively. However, in developing the state budget, the Legislature counts that revenue toward each district's budgeted funding, and provides the remainder in state funds. In effect, fees and property tax revenue are interchangeable with state funding. Thus, the combination of funds from the state budget, local property taxes, and student fees is referred to as "state-controlled funding." Revenues from student fees account for about 5 percent of the state-controlled revenues.

Figure 3: California Community College Funding



For 2007-08, community colleges will receive about \$6.8 billion in state-controlled funding for operational costs. The state appropriates funding from state bond issues to fund the construction of community college facilities. Districts raise and control some revenue locally that is not subject to the state budget process. These include funds raised by local bond elections to renovate, upgrade, and build facilities, and operating revenues for specific purposes such as maintaining parking facilities and campus health centers and performing educational services under contract with local businesses.

The state budget provides CCC funding initially to the state Chancellor's Office (CO), which is responsible for allocating virtually all of it to the 72 community college districts. The Chancellor's Office uses a variety of formulas prescribed in statute and regulation for these allocations. In the simplest terms, funding is provided in two ways: (1) as general-purpose funding known as "general apportionments," and (2) as "categorical" funding which is restricted to specified purposes. Multi-campus districts in turn allocate this funding among their campuses – again consistent with myriad statutes and regulations.

Use of apportionment funding at the local level is heavily influenced by local collective bargaining, under which each of the 72 districts bargains its own contract with union representatives. The contract provisions on faculty salaries are important determinants of the flexibility, or lack thereof, that districts have in the allocation of resources. District-level collective bargaining places districts in competition with one another and gives unions the opportunity to compare salaries across districts as a lever in bargaining.

Proposition 98

Most state support for community college districts falls within the parameters of Proposition 98. Passed by the voters in 1988, Proposition 98 amended the state constitution to establish a minimum funding guarantee for K-14 education. Each year, a complicated formula is used to determine the minimum level of support (made up of state General Fund and local property tax revenues) that must be provided for K-14 education. In simple terms, the formula generally increases the prior year's funding level to reflect state economic expansion and K-12 enrollment growth. The

Proposition 98 funding guarantee is not affected by CCC enrollment growth.

Because Proposition 98 applies to all of K-14 education, it pits community colleges against K-12 schools for relative shares of total Proposition 98 funding. Although statute specifies a 10.9 percent share of Proposition 98 funding for community colleges, the Legislature routinely suspends that provision and provides community colleges with somewhat less than their statutory share. (The 2007-08 budget provides the CCC with 10.7 percent of total Proposition 98 funding.) Therefore, community college funding is influenced less by their workload needs and more by (1) what the Proposition 98 formula requires be spent on K-14 education and (2) the relative priorities determined through the political process for K-12 and community colleges.

Although Proposition 98 sets a minimum K-14 funding level, the guarantee is viewed as a target that is seldom exceeded, because doing so would ratchet up the minimum guarantee in future years. Therefore, the state is unlikely to provide CCC with more funding than the difference between the minimum guarantee and what is provided for K-12. To provide more than this to CCC would over-appropriate Proposition 98. And because K-12 education is compulsory, CCC tends to be in a less advantageous position in the competition for Proposition 98 resources.

The statutory split between K-12 and community colleges is fixed – there is no statutory recognition that relative enrollments and growth rate patterns for K-12 and community colleges will vary over time. There is little analytical justification for meeting this particular target, given that CCC's enrollment levels and other cost drivers have changed in different ways from those in the K-12 sector. Still, in the absence of programmatic bases for determining CCC appropriations, 10.9 percent of Proposition 98 funding has become a surrogate for "need" and community college advocates regularly characterize their falling short of this target as under-funding.

Another important dynamic created by Proposition 98 is the distinction between "local assistance" funding that goes to the individual college districts and "state operations" funds that support the Chancellor's Office. State funds appropriated to community college districts

are counted under Proposition 98, while state funds in support of the CO, as a state agency, are not. As a result, the state (and particularly the Department of Finance) views augmentations to the CO as discretionary increases to overall state spending, while spending on local districts is subsumed under Proposition 98 and "would have to be spent anyway." With no funding guarantee, the Chancellor's Office competes with all state agency functions for funding. Over the last ten years its funding has declined as a share of total system funding – from 0.5 percent in 1996-97 to 0.2 percent in 2006-07. During the same time span it has lost 19 percent of its positions as the system has grown significantly in size and complexity.

Incentives

Proposition 98 causes policy makers to perceive a tradeoff between CCC and K-12, rather than considering community college funding priorities within the broader context of all state functions, or even within the context of the state's higher education enterprise. In effect, Proposition 98 funding becomes an enormous categorical program whose funding cannot be moved outside of K-14 education. There is little incentive for policy makers or CCC advocates to consider the actual needs or costs of providing quality community college education because the funding level is virtually pre-determined. In addition, there is no incentive for community college advocates to support costly K-12 reform efforts – even those that would clearly benefit the colleges by producing better prepared students – because the two systems are in direct competition for resources.

With the level of guaranteed funding under Proposition 98 unaffected by community college enrollment, there is a disconnect between CCC funding growth and CCC costs as they are influenced by enrollment growth. This disconnect can work against efforts to increase participation rates in the CCC. In addition to a growing number of high school graduates, California has over 1.6 million working-age adults, ages 18-34, who lack a high school diploma.³³ Addressing the educational capital needs of the state requires an effective mechanism for reaching this group but the current mechanisms are not working. California ranked 49th among states in 2000 in the number of General Educational Development certificates (GEDs) awarded to 18-24 year olds as a percentage of those in that age group with less than a

high school education.³⁴ Even though community colleges share responsibility with K-12 for adult education, the Proposition 98 formulas provide a disincentive for the CCC to increase college enrollment rates within this population. Unless the CCC share of Proposition 98 funding were to be significantly increased – an unlikely prospect based on history – serving large numbers of this under-educated adult population would reduce the funds available to serve students holding high school diplomas.

Even without accounting for the adult population, the statutory Proposition 98 split does not encourage lawmakers to adjust funding to match enrollment demand. K-12 and CCC enrollment typically grow at different rates — indeed, for the next several years they are expected to change in different directions, with K-12 enrollment actually *declining* while CCC enrollment *grows*. Other things equal, this would justify CCC receiving a larger share of total Proposition 98 resources, at least until the enrollment trend were to reverse. But since the formula does not account for the relative enrollment or growth rates in each sector, whether or not the CCC share increases will be the result of political forces.

The distinction between CCC local assistance funding (which is subject to Proposition 98) and state operations funding (which is not) creates its own incentives. Because the Constitution requires the state to spend at the minimum Proposition 98 guaranteed level, there is usually much more scrutiny of proposed augmentations for the Chancellor’s Office administrative functions than there is for proposed increases in local assistance. One impact of this is a system office that is generally recognized as under-funded with respect to its mission to provide leadership over the enormous system. In recent years the loss of CO staff has forced a shift toward regulation and compliance and away from substantive leadership. Even so, in many areas its ability to provide regulatory oversight falls well short of what is called for in law and regulations.

A second impact of the funding distinction between state administration and local assistance is the incentive it creates to use local funding and local staff to perform statewide coordinating functions. In recent years the state has used local assistance monies to fund a number of programs that are statewide rather than local — such as an outreach

campaign about community college affordability and a statewide accountability system. Funding for these programs was provided directly to particular community college districts, which in turn were contracted to provide the statewide services. Logically, these programs might well have been run through the CO, but they were run through a district to count the funding under Proposition 98.

Do Proposition 98 policies reinforce state priorities?

Readiness	-	Competition for funds between K-12 and CCC creates a disincentive for the CCC to support costly K-12 reform
Access	-	Funding split does not reflect relative growth rates
Completion	-	Disincentive for readiness is a disincentive for completion because poor preparation is a major risk factor in completion
Workforce	-	Disincentive to address problem of adults without high school degrees because it would reduce funding for other enrollments
Efficiency	-	Funds are not directed toward the greatest need in terms of enrollment growth trends within each sector

Apportionments

With districts lacking the control over local property tax revenue or fee revenue that community colleges in many other states have, state apportionments are the main source of district funding and the only true source of general purpose funding. About four-fifths of the annual state appropriation for community colleges is for general apportionments. This is funding the CO allocates to each district in support of basic operating costs. Apportionment funds are general purpose funds that can be used at the discretion of districts (subject to the many rules and regulations that govern the system). While total funding for the community colleges is not determined by system enrollment, individual allocations to districts are heavily

enrollment-driven. This is reflected in the apportionment formulas, described in this section, and in the allocation formulas for funding enrollment growth, described in the next section.

The CO has little meaningful discretion in deciding how much funding will go to each district – apportionment allocations are derived according to a complex series of formulas that are contained in statute. Because it constitutes such a large share of each district’s budget, and because it is general purpose funding, the allocation of apportionment funding is a major concern for all community college districts. In 2006, the Legislature enacted SB 361, which revised the general apportionment formula that had been in place since the late 1980s. This section describes the new general apportionment mechanism as well as three other key features of apportionment policy and then summarizes the incentives they contain with respect to the six priorities.

(1) General Apportionments

Under the new law, each district receives general apportionment funding in two ways. First, each district receives a basic allocation of several million dollars based on the number of colleges and off-campus centers of at least 1,000 FTES in the district. This basic allocation is intended to recognize the fixed cost associated with maintaining and operating colleges and centers. Second, each district receives funding for each full-time equivalent student (FTES) served up to the maximum it is authorized to serve. For 2006-07, most districts received a standard amount of \$4,367 for each credit FTES student, an amount to be adjusted each year for inflation. (About 10 percent of districts received somewhat more than this amount per student, for reasons described in the next section.) Amounts for non-credit are less, and depend on the type of non-credit instruction, as described in (3) below. The FTES-based portion of a district’s allocation is by far the largest source of district funds.

(2) Equalization

Under the prior apportionment system, known as Program Based Funding, not all districts received the same allocation per FTES. This was due to a variety of factors, some intentional (such as accommodating economies of scale) and some unintentional (such as historical differences in local property tax rates that were retained in state formulas

after Proposition 13 shifted control of financing the colleges to the state). A perennial issue under Program Based Funding was how funding levels could be made more equitable.

Over the past decade the Legislature invested hundreds of millions of dollars to raise the per-student funding rate of lower-funded districts. With a final \$160 million investment in the 2006-07 budget, the state has declared that its equalization goal has been achieved, and SB 361 will prevent erosion of that achievement by funding growth in all districts at the same rate. This may not be the end of the equalization issue, however. The methodology for equalizing districts that was contained in SB 361 is just one of a number of approaches that have been proposed, and it would not be surprising, based on history, if districts were to advocate alternative approaches to equalization.

(3) Non-Credit Funding

Non-credit education, as described on the CO website, provides individuals with “skills that are critical to their ability to become or remain independent and to contribute to the economy of California.”³⁵ Authorized categories for state-supported non-credit education are set forth in the California Education Code as Parenting, Elementary and Secondary Basic Skills, English as a Second Language (ESL), Citizenship, Adults with Disabilities, Short-term Vocational, Older Adults, Home Economics, Health and Safety. These same services are provided in some areas of the state through K-12 adult education and in other areas through community colleges. Some community college districts have large non-credit programs and some have none at all.

Until 2006-07, there was one funding rate for each non-credit FTES and all districts received that same amount. The rate was set in statute at \$1,100 in 1983 and has been increased each year to account for inflation. The rate for 2006-07 was \$2,626 – about 60 percent of the average credit rate. The reduced rate reflects an assumption that non-credit instruction is less costly. Beginning in 2006-07, SB 361 authorized a higher per-FTES funding level for certain types of non-credit courses (defined as “career development and college preparation” courses) of \$3,092, to be increased for cost-of-living. Proponents of the change argue that this portion of non-credit instruction serves students who aim

to transition into credit programs but must begin at very basic skill levels. They maintain that these programs should eventually receive the same priority (and funding) as credit instruction, much of which similarly provides basic skills to under-prepared students.

Although non-credit enrollment is funded separately from credit, both forms of FTES count equally toward a district's cap, which, as we discuss below, is the maximum amount of FTES for which it may receive funding in a given year.

(4) Cost-of-Living Adjustment (COLA)

Statute requires that CCC's annual budget request include a COLA on general apportionments (and selected categoricals) that is based on a national inflation index. The COLA is intended to cover all cost increases experienced by a community college district – not just salaries, but utilities, instructional equipment and supplies, building maintenance, and other costs.

Under state law, faculty and staff at each community college district bargain collectively. Many campus budget officers report that they face huge pressures from unions to increase faculty and staff salaries by at least the percentage amount of the district's COLA, whereas there are no strong constituencies pushing for increases for operating budgets. When COLA funds are used primarily or exclusively for salaries, there are not enough COLA funds left to cover the cost of inflation on non-salary expenses. Districts need to rely on *growth* funds to make up for the cost of inflation. That is, they need to *grow* just to *maintain* current non-salary operations. This forces cutbacks elsewhere since the growth money has been partly committed to inflation, not growth.

Incentives

The prevailing incentive embedded in the apportionment formulas is to maximize FTES in order to maximize dollars. With credit FTES funded at a higher rate than non-credit, districts have an incentive to favor credit over non-credit enrollment. But non-credit instruction can provide a low-cost way to increase enrollment with classes in, for example, parenting and citizenship, since credit and non-credit enrollments both count toward a district's enrollment. Within credit FTES, there is a disincentive to offer high-cost programs because all programs, regardless of cost, are funded at the same rate.³⁶ Within non-credit, the enhanced

rate of funding now provided for career development and college preparation instruction creates an incentive to focus non-credit instruction on these sequenced offerings aimed at career development. Districts also have an incentive to operate more campuses and centers.

The pressure to increase enrollment comes not only from the FTES-based funding but from the COLA provision. As noted above, enrollment growth funds are often the only source of money to increase operating budgets for non-salary items.

The features of apportionment funding fail to provide financial incentives to improve outcomes such as course completion, degree completion, or student learning. Nor do they provide any incentive to enroll the kind of student (e.g., degree seeking, low-income, underserved) that would increase overall educational attainment levels in the state. FTES generated by first-generation college students is of equal value, financially, as FTES generated by degree-holding adults taking courses for personal enrichment.

At a more micro level in the college classroom, FTES-based funding that derives from 3rd week course enrollment (when the official count is taken) sets up a variety of incentives for faculty and students, none of which promotes success. For example, most districts allow students to register late for classes (up to the census date to maximize funding), even though joining a class already in progress reduces a student's chances of success.³⁷ Instructors have an incentive to allow students to register late because it helps them ensure the class will not be canceled and because healthy course enrollments may help the department in negotiations for more money or more faculty. For these same reasons, instructors have no *financial* incentive to drop "no shows" before census date to make room for additional students who may be on waiting lists. Once FTES counts are official, instructors have no financial incentive to try to retain students in their classes who may be struggling and could benefit from referrals to student or academic support services.

For their part, students have little incentive to seek assistance before dropping a course. State regulations authorize districts to permit no-penalty withdrawal from courses up to three-fourths of the way into a term.³⁸ And, as discussed later in the section on fees, no fees are charged for dropping a course. Faculty have until that same late date into the term to

process the course drops. Collectively, then, policies provide no financial incentive to students or faculty for students to complete the courses in which they enroll.

The FTES-funding model helps sustain the limited use and enforcement of course prerequisites that, in general, characterizes the CCC system.³⁹ In interviews, many college officials mentioned the positive impact that course prerequisites could have on student persistence and success but acknowledged that FTES considerations play a big role in their limited use. Officials fear that if students were required to achieve certain proficiency levels before enrolling in more advanced courses, FTES in those advanced courses would suffer to the detriment of the department or even the college itself. As one vice president said, when asked why his college does not enforce the very course prerequisites that he said would greatly increase student success: “we would go broke.” The following comment by a community college dean makes all too clear the kinds of trade-offs that are made in the service of the enrollment-driven funding policies:

“The need to improve basic skills is an important issue, one that I support. But I think that we find ourselves in a dilemma. While we want to improve reading, English and math, we know that if we toughen up in those areas, similar to what the four-year colleges and universities have done, it will impact enrollment and funding. The solution lies with changing the funding formula.”⁴⁰

Again and again, as we discuss this project with campus officials, this message is repeated in one form or another: as long as colleges continue to have to operate with enrollment-driven funding policies (and, some say, “chase after growth”), they will not be able to do their best to promote student success.

Do apportionment policies reinforce state priorities?

Readiness	-	Disincentive to alert prospective students to the importance of being college ready because it could reduce FTES
Access	+/-	Incentive to increase enrollment; no incentive to favor enrollment of credential-seeking students over personal enrichment; all credit enrollment valued equally

Completion	-	No incentive for course completion; incentive to allow late registration and to minimize prerequisites impedes completion; focus on fairness to districts rather than outcomes for students
Workforce	+/-	Incentive to offer more workforce oriented non-credit under enhanced funding rate; disincentive to invest in costly programs and to add new programs to meet workforce needs if initial FTES will be low
Efficiency	-	Focus on inputs does not direct funds where they would have the most impact on outcomes

Enrollment Growth

The annual Budget Act includes an appropriation (essentially, a categorical item) specifically for enrollment growth. This appropriation is associated with a particular number of additional FTES. The 2007-08 Budget Act included \$107 million for an additional 23,000 FTES. State law requires the Board of Governors’ annual budget request to include FTES growth to reflect, at a minimum, an equally weighted average of the rate of change in the state population of persons ages 19 to 24 and persons ages 25 to 65, as determined by the Department of Finance for the preceding fiscal year. To the extent the state unemployment rate exceeds five percent for the prior fiscal year, the requested FTES growth is to be increased according to a specified methodology. However, there is no statutory requirement that any amount of enrollment growth be *funded* in the annual budget. And as noted above, the appropriations to the CCC are determined by Proposition 98, irrespective of these projections of FTES increases.

Once the budget is enacted, the CO allocates the enrollment growth funding to the districts to establish the new enrollment “cap” – or maximum authorized level of *funded* enrollment – for each district. The cap is essentially a tentative assurance to fund enrollment up to a certain

Class Size Incentives Can Affect Student Success – A Hypothetical Example

Colleges are funded on the basis of enrollment in the 3rd week of class. What happens to students after that point (whether or not they succeed) does not affect funding. Here is a hypothetical example of how the incentives can work against student success:

- A college sets the appropriate size limit for lecture classes at 40 and maintains waiting lists to replace students who drop the course.
- As long as an instructor has a class roster of 40, he or she does not have to admit students from the waiting list.
- Attrition occurs but students neglect their responsibility to drop the course, having little financial incentive to do so, due to low, or waived fees.
- Faculty leave the students on the official list (not always knowing if they truly intend to drop); this keeps the official enrollment count up and ensures that the class will not be canceled, but precludes students entering from the waiting list.
- *Result:* the college gets funding for students who drop, students drop courses that they might have completed, with appropriate support services, and students on waiting lists are denied access to classes they may need.

If colleges received funding for students who *completed* the course, the incentives would be entirely different. Colleges would be inclined to enforce student drop responsibilities and faculty would be inclined to admit students from the waiting list, and would likely encourage wait-listed students to attend class from the beginning so as not to fall behind. Faculty would want to become more closely involved with students and academic support units to help students get all available help before deciding to drop a course.

limit. A district needs to earn this funding by actually enrolling the additional students. Unlike K-12 enrollment, community college enrollment is not an entitlement and the state is under no obligation to fund it. Yet as open-access institutions, community colleges may collectively experience enrollment demand that exceeds the amount of enrollment funded in the budget.

Growth in the cap is based on district population growth, but there is a bias for growth in the computation of district caps. District growth caps are augmented if the district's college participation rate is lower than the statewide average. Moreover, each of the 72 districts is *authorized* to grow by at least 100 FTES even if the district's population growth trend has been negative. If districts in low-growth areas are able to recruit or attract enough students to *achieve* their authorized caps, the sum of all district caps will exceed the systemwide allotment for growth, which is based on *actual* statewide growth trends. When this happens, district funding is reduced proportionately and high-growth districts must share the funding deficiency with low-growth districts.

Enrollment above the cap is not funded in the initial allocation. However, if some statewide growth money remains after all districts have been funded for all enrollment growth up to their caps, then this leftover funding is allocated to districts that have enrollment above their caps. In addition, in some years, the state has provided extra growth funding specifically to fund enrollment that is above cap.

While districts receive no *growth* funding for students they do not enroll, they do not lose base enrollment funding for the first year they experience an enrollment decline. This policy, known as stability funding, allows a district to retain enrollment funding for one year even for slots that are no longer filled with students. The intent is to smooth out funding changes created by temporary (one-year) disruptions in enrollment due to factors like buildings being taken out of commission for repairs or local roadway disruptions. A district loses funding for a slot in the second year it is vacant.

Incentives

The principal incentive a district faces from this policy is to grow – but not beyond its enrollment cap. Districts with different growth patterns have very different incentives. Community colleges are required by law to admit any

California resident with a high school diploma or equivalent, and may admit anyone over 18 years of age who “is capable of profiting from the instruction offered.”⁴¹ Districts facing major growth pressures must be careful not to grow too much, because they may receive no funding for growth over the cap. (The lack of resources for districts to accommodate enrollment over cap is a consequence of system fee policy as well, which we discuss later.) Districts in this situation must, in effect, make choices about who gets access, not through admissions decisions but by deciding which and how many courses will be offered. These decisions are influenced by factors such as faculty employment status (e.g., full-time, part-time, tenure) and projected class size and may, out of necessity, not always be in the best interests of students and their needs for courses.

At the other end of the scale, districts experiencing slow growth or decline have every incentive to increase enrollment any way they can, irrespective of local need. In extreme cases, this can push districts to take unethical or ethically questionable actions such as occurred with the dual enrollment of high school athletic teams in college physical education classes for after school practice (see box) or when a college offered non-credit exercise classes in a local nursing home. In other instances, districts can be tempted to recruit students to attend for recreational or personal enrichment reasons. This practice is legal, but must be questioned in the context of more pressing enrollment needs. Fiscal pressures to grow can also encourage laudable outreach efforts into underserved populations that could benefit from increased educational attainment.

In seeking to make growth caps, districts have a fiscal incentive to minimize the offering of expensive courses. It costs a district much more to offer a nursing class than a history class, for example, yet all credit FTES is funded at the same rate. This can lead to a mismatch of course offerings with student demand and local need.

Districts may face financial pressure to focus on new enrollment over retention of current students as a means to make growth caps. Some college officials believe that it can cost more to retain a student than to admit a new student because college funding levels don't readily permit the level of intensive services that many students require in order to persist and succeed. Therefore, while a retained student taking

Case Study: FTES-Driven Funding Did Encourage Questionable Actions

- In 2002, the *Orange County Register* revealed that some local colleges were inappropriately inflating their FTES enrollment to increase state funding.
- Under the guise of concurrent enrollment bridge programs, some colleges were enrolling high school students in college credit PE classes that were not open to the public.
- In many cases, these “classes” were regular after-school practices or off-season workouts of high school sports teams, held at the high school facility.
- The colleges received FTES funding from the state for these students, while the students received college credits and the high school coaches received extra pay for their high school coaching duties.
- To resolve the issue, 38 of the 72 community college districts returned \$25 million in state funding, although Department of Finance estimate of the total funding received by colleges through such practices was substantially higher.
- Legislation was enacted (Chapter 786, Statutes of 2003) to tighten the conditions under which community colleges may enroll high school students. But many districts reduced *legitimate* concurrent enrollment of high school students, an unfortunate outcome given the benefit to students and the state of having students get a head start on earning college credits – a practice which is on the rise in other states as part of college readiness reforms.

12 units generates the same amount of funds as does a newly enrolled student taking 12 units, colleges may see incoming students as the best way, financially, to meet their enrollment

caps. Efforts are underway within the system to demonstrate to colleges that retention may be a more cost-effective strategy than commonly believed, through the contribution of retained students to FTES-based funding.⁴² Whether it does cost more to retain a student than to enroll a new student is unclear and likely varies considerably across colleges.

An indirect consequence of the enrollment growth funding policy is that districts have an interest in opposing fee increases. With district funding so heavily dependent on enrollment levels, *any* threat to a district's FTES is a threat to its fiscal position. From this perspective, it is immaterial to districts *which* students might forgo enrolling if fees increase. For example, students who are taking advantage of low fees to use college recreational, music, or art facilities for personal enrichment purposes may decide against enrolling if fees increase. The loss of these students would have no negative impact on the education levels of Californians or on colleges' ability to meet local workforce needs, yet colleges fear the drop because their life blood of FTES-driven state appropriations is affected.

Do enrollment growth policies reinforce state priorities?

Readiness	-	Disincentive to stress college readiness standards due to feared negative impact on enrollment
Access	+/-	Incentive for districts to grow and to provide access to new students except where growth exceeds cap; No incentive to favor enrollment of credential-seeking students over personal enrichment; all enrollments valued equally
Completion	-	Districts rewarded for census enrollment regardless of student outcomes; no incentive to provide costly support services to increase retention if growth cap can be met in less expensive ways
Workforce	-	Disincentive to expand expensive workforce programs
Efficiency	-	Disconnect between growth funding and actual demand

Categoricals

The annual budget for the CCC contains 22 separate line items, called categoricals, which are appropriated for specific purposes. Districts receive these funds in addition to their base allocation. Categorical funding is a prominent feature of community college finance policy, accounting for over one-fifth of the budget – nearly \$800 million. The majority of funding for student services is provided as categorical funding.

Categorical funding enjoys strong support from various stakeholder groups eager to build in line-item protections for their priorities. Campus officials acknowledge that categoricals help insulate funds from union pressure to direct funds to faculty salary increases. Categorical funding also gives the Governor and the Legislature greater control over college spending than is provided through the base appropriation. Instead of leaving fiscal decisions to district boards and presidents, categorical funding directs that certain funds be spent in accordance with specified conditions. This funding strategy is intended to ensure that districts address specific state priorities under the assumption that prevailing local priorities would cause districts to under-invest in these areas.

The approach raises interesting issues for a system of 72 local districts and 109 colleges that is steadfast in its message that local differences call for locally-driven priorities and practices. In such an environment, what is the appropriate balance to strike between state and local priorities? When is there a compelling interest such that state or system priorities must override local priorities? And in those cases, what is the best mechanism for ensuring that state priorities are addressed by local districts? Further, should categoricals be needed for programs and services that are among the core functions of every college, e.g., for academic advising or for compensating part-time faculty for holding office hours?

In this section we describe five of the larger categorical programs and analyze whether the incentives contained in the funding formulas accomplish the intended purposes and how they align with the state's priorities. We end with conclusions about categorical funding as a tool of finance policy in the CCC.

(1) **Matriculation**

According to the CO website, the goal of matriculation is “to ensure that all students complete their college courses, persist to the next academic term, and achieve their educational objectives through the assistance of the student-direct components of the matriculation process. ...”⁴³

Matriculation funds are allocated to provide students with the following services: admissions, orientation, assessment and testing, counseling, and student follow-up. Funds are allocated to colleges on a per-student basis for three different categories of credit student enrollment:

- new students
- continuing students
- pre-collegiate (basic skills) enrollment.

For each of these categories, the formula provides a different per student amount:

- New students are funded at *2.4 times* the funding provided for continuing students.
- Pre-collegiate enrollments are funded at *.7 times* the amount provided for continuing students.

Colleges receive a minimum allocation of \$50,000 regardless of size and are guaranteed at least 95 percent of their previous year’s matriculation allocation regardless of changes in enrollment. Matriculation regulations state that each dollar provided for matriculation must be matched at a 3:1 ratio by each college. There is a separate formula to generate funding for non-credit students. These funds can only be used to provide matriculation services to students enrolled in non-credit courses or programs. A 1:1 match between district and state categorical funds is required for non-credit matriculation funds.

A small matriculation unit within the CO provides technical assistance to colleges and oversees a highly complex and regulated system of test validation for assessment, under which the CO approves tests for use at each college.⁴⁴ There are currently over 150 different instruments on the approved list. The CO has had to suspend the matriculation site visits that were a major component of its oversight role, due to lack of staffing.

Incentives

The funding incentives are misaligned with the program’s stated goal. Whereas the goal of matriculation is course completion and student persistence, the funding formula rewards new enrollment over continuing enrollment by providing 2.4 times more funding for a new student than for a continuing student. There is nothing in the matriculation funding formula that takes student progression, completion, or success into account. Additionally, funding is unaffected by students *served* or services *provided*. So there is no fiscal incentive in the formula to provide matriculation services at all.

Services are supposed to be mandatory for most matriculated students, but in fact, there are wide variations across campuses in the degree to which matriculation services are provided. Some colleges report that there are few, if any, consequences to students for not participating in matriculation services. Since service levels do not affect funding, colleges do not carefully enforce the mandatory provisions. More importantly, colleges are reluctant to institute any requirements that could cause students to drop out of school, since lost enrollments result in reduced college funding. Students, therefore, often have little incentive to avail themselves of these supposedly mandatory services, such as orientation and advising.

The wide variety of local assessment instruments and placement policies send multiple and complex signals to prospective students about what it takes to become ready for college-level work. It can lead students to shop around for those colleges with the most lenient policies.

Do matriculation policies reinforce state priorities?

Readiness	-	Discourages readiness by sending complex, multiple signals about college readiness through decentralized assessment process
Access	+/-	Promotes broad access but not necessarily by credential-seeking students
Affordability	-	Lack of incentives to make forward progress can increase student costs by increasing time-to-degree

Completion	-	Impedes completion by funding new students at higher rate than continuing students and basic skills students; no incentive to actually provide services or to help students persist and succeed
Workforce	-	Lacks incentives for students to obtain, or colleges to provide, advising about careers and related academic pathways
Efficiency	-	Complex approval and validation process; 95 percent prior year funding guarantee

(2) *Extended Opportunity Programs and Services (EOPS)*

According to the Chancellor's Office website, the "EOPS program's primary goal is to encourage the enrollment, retention and transfer of students handicapped by language, social, economic and educational disadvantages, and to facilitate the successful completion of their goals and objectives in college."⁴⁵ EOPS provides funding to colleges for the provision of support services, including financial assistance to students. The budget for 2007-08 includes \$120 million for this program, which is about one-sixth of the categorical budget. Colleges are funded pursuant to the following formula:

- a base allocation of \$50,000 per college
- 90 percent of funds above the base allocated based on number of eligible students served
- 10 percent of funds above the base allocated based on "college effort" (defined as college funds allocated to EOPS above the required minimum 15 percent match)
- guarantee of at least 95 percent of prior year funding unless more than 5 percent of funds are unspent.

The funding provided above the \$50,000 base depends on total funds available. Not all eligible students can be served. Instead, colleges have a cap on the number of eligible students they are funded to serve.

To be eligible for EOPS services, a student must:

- be a California resident
- be enrolled full-time at the time of acceptance into the program
- have completed fewer than 70 units of college-level coursework
- meet the requirements for a Board of Governors' fee waiver
- be "educationally disadvantaged" as indicated by lack of high school diploma or GED, high school grade point average (GPA) below 2.5, or basic skills eligible
- maintain "satisfactory academic progress" to remain in the program, with definition determined by the college and included in the student's academic plan.

Title 5 regulations require that each college receiving EOPS funds employ a full-time director unless it receives a waiver from the Chancellor. Regulations cite specific criteria for the Chancellor to use in approving any waiver request.

Incentives

The formula encourages colleges to enroll disadvantaged students in the program – up to their funded cap – and provide them services. The count of students served is based on students who have on file (1) an EOPS application, (2) an educational plan, and (3) a mutual responsibility contract, and who attend at least one class. The formula takes no account, however, of the level of services provided, student progression, completion, or success. Since there are more eligible students than can be accommodated, colleges have little to lose if students fail to make satisfactory academic progress because other students can be enrolled in their places. To the extent that the matching requirement is monitored, colleges have an incentive to allocate base college funds to the program as it generates additional categorical funding. However, the guarantee of at least 95 percent of prior year funding reduces the financial risk to colleges of not maintaining enrollment in the EOPS program. With the subsequent year allocation reduced if more than 5 percent of funds are returned, the

incentive is for spending money irrespective of outcome.

Students have an incentive to enroll full time for initial enrollment in the program, and to make satisfactory progress, although there is no requirement that students continue to be enrolled on a full-time basis.

Do EOPS policies reinforce state priorities?

Access	+	Promotes broad access since program serves disadvantaged students only and colleges receive more funding, up to a cap, for additional students enrolled
Affordability	+	Provides financial aid to increase the affordability of college
Completion	+	Encourages full-time enrollment, gives students an educational plan and some financial assistance, and requires that students maintain satisfactory progress
Workforce	+	Provides academic plan and counseling on local career prospects
Efficiency	-	95 percent prior year funding guarantee; use it or lose it rule; limited flexibility due to requirement for full-time director; reporting requirements

(3) Disabled Students Programs and Services (DSPS)

DSPS is intended to allow eligible students to “participate as fully and benefit as equitably from the college experience as their non-disabled peers.”⁴⁶ The 2007-08 Budget includes \$115 million for the program. DSPS provides funding for a variety of support services, specialized instruction, and educational accommodations for students with disabilities. After some funds are taken off the top to be used for specific purposes, as identified in the annual budget, colleges are funded pursuant to the following formula:

- a base allocation per college
- 90 percent of funds above the base allocated based on weighted student count for the previous year,

reflecting the average cost of providing services to students with a particular disability and the number of students with that disability who received services

- 10 percent of funds above the base allocated based on college effort (i.e., college general funds allocated to DSPS).

Incentives

The funding formula gives colleges an incentive to enroll eligible students and provide appropriate services as well as to dedicate some general campus funds above the base categorical funding. Colleges are not discouraged from serving high-cost disabled students because they receive different amounts based on the type of disability. There is nothing in the formula that takes student success into account so colleges have little incentive to ensure successful completion of student goals.

Do DSPS policies reinforce state priorities?

Access	+	Promotes access by encouraging enrollment of students with disabilities
Completion	-	No features to encourage persistence or completion
Efficiency	-	Reporting requirements pose high administrative costs

(4) Part-time faculty

Three separate categorical items provide for part-time faculty compensation, benefits, and office hours. Together they are intended to provide better compensation to part-time faculty than might occur as a result of local collective bargaining. The compensation item is intended “to assist districts in making part-time faculty salaries more comparable to full-time salaries for similar work...”⁴⁷

- Chapter 943, Statutes of 1996 established the Part-Time Faculty Health Insurance program with intent of providing part-time faculty and eligible dependents with access to health insurance.

- Chapter 933, Statutes of 1997 created the CCC Part-Time Faculty Office Hours Program to compensate part-time faculty who hold office hours related to their teaching load.
- Part-time faculty compensation funds were first provided in 2001-02 after two state offices concluded, in reports for the Legislature,⁴⁸ that part-time faculty earned lower wages and benefits for teaching activities than full-time faculty with comparable experience and backgrounds.

For the first two programs, districts are expected to allocate campus matching funds and are compensated on the basis of submitted claims. State reimbursements are limited to 50 percent of the claim. When district claims exceed the appropriated amounts, claims are prorated. Only a small portion of districts apply for these funds – about 30 submitted claims under each program during 2005-06. Even with a limited number of claims, requests far exceed available funds. Districts submitting claims in recent years received 14 cents and 59 cents for each eligible dollar claimed in the benefits and office hours programs, respectively.⁴⁹

Part-time faculty compensation funds are allocated to districts based on FTES, with the number of part-time faculty having no bearing on the allocation. In districts with equal FTES, the one with the lower percentage of part-time faculty can afford to give a larger salary increase to its part-time faculty. Budget language directs that the funds be used to supplement district funds to compensate part-time faculty in order to achieve “parity” with full-time faculty compensation but may not be used to exceed parity. Districts that achieve parity may use the funds for any other educational purpose. According to the State Auditor, absence of parity prevails because districts have been able to attract part-time faculty willing to work under terms of locally-bargained contracts.⁵⁰ The Auditor found no constraints on local districts in the collective bargaining process that prevent parity in compensation, office hours, or benefits.

Incentives

The low reimbursement rates provided for college expenditures on health benefits and office hours give only a small incentive for colleges to allocate more for this purpose than they would in the absence of the program. As evidence, only about 30 of the 72 districts submitted claims. The large districts always submit claims, according to Chancellor’s Office staff, which implies that the impact of the program on equitable part-time faculty compensation may be as much a function of district staffing and sophistication as of the needs across various districts.

The compensation program contains a minor incentive to increase enrollment, as funds are allocated based on FTES regardless of the actual proportion of part-time faculty employed by the district or the cost to achieve parity. There is no incentive for districts to attain parity in compensation because they receive the funds regardless of their parity status. The degree to which the allocation moves a district toward parity is dependent upon the percentage of part-time faculty in a district: the higher the percent of part-time faculty, the less likely the allocation is to move the district to parity.

Do part-time faculty policies reinforce state priorities?

Access	+/-	Incentive to enroll students but irrespective of educational goals and with no relation to the goals of categorical program
Completion	-	Potential to make part-time faculty a more stable component of college culture is nullified by limited impact of only 40 percent of districts applying for office hour and health insurance funds
Efficiency	-	Inefficient to override local collective bargaining; high administrative costs to submit claims and satisfy reporting requirements; disconnect between FTES-based allocation and purpose of the program

(5) Financial aid administration

The Student Financial Aid categorical was established to increase access to college and participation in financial aid programs by low-income and disadvantaged students. Funding for the program was more than quadrupled when the Legislature increased community college fees in 2003-04. This additional funding was intended to increase student awareness of, and participation in, financial aid programs, with particular focus on the Board of Governors' (BOG) fee waiver and the federal Pell grant program.

A portion of the funds is allocated to districts to defray their administrative costs of implementing the Board of Governors' fee waiver program. Another portion is for a statewide media campaign to promote the messages around affordability and financial aid availability. The majority of the funds are allocated to campuses as follows:

- a fixed amount of \$50,000 per campus
- the remainder based on a formula reflecting two equally weighted factors: a college's percent of system-wide FTES and its share of system-wide BOG waiver recipients.

Funds are intended to be used by colleges to provide additional staff and related expenses to support direct contact with potential and current financial aid applicants and are to supplement, not supplant, funds allocated for the administration of student financial aid during a base year (2001-02). The program provides roughly one half of the total funds used by colleges for the administration of student financial aid, with the other half coming from general fund budgets through local budget decisions. Colleges are required to submit spending plans and reports to the system office, detailing the locally planned expenditures with respect to the specific strategies pursued.

Incentives

The formula provides a weak incentive for enrollment growth and for growth in the number of students receiving BOG fee waivers. Because the formula awards funds on the basis of a district's *share* of system totals, it is unlikely that year-to-year growth in either FTES or BOG recipients will make much difference in a district's allocation. The

provision of a base amount of \$50,000 per college ensures that funding from year to year will be fairly stable, irrespective of campus implementation or program impact.

The Chancellor's Office monitors the maintenance of effort requirement and the expenditures and accomplishments by each college. But it is not clear that there are any consequences for local performance. In its initial report to the Legislature after 2003-04 program implementation, the Chancellor's Office identified a small number of colleges that failed to satisfy the maintenance of effort requirement and provided reasons why that happened, but there were no adjustments made to future allocations.⁵¹

Do financial aid administration policies reinforce state priorities?

Access	+	Funds allocated in part on enrollment of needy students in the BOG fee waiver program
Affordability	+	Helps more students apply for financial aid by requiring that funds be spent on financial aid administration
Completion	-	No financial incentive for colleges to help needy students persist or complete their academic programs
Efficiency	+/-	Allocation based in part on enrollment and number of fee waivers directs funds in proportion to need; Extensive program and reporting requirements ⁵² prevent districts from achieving goals in the most efficient manner

Categorical Funding is a Problematic Funding Mechanism

As implemented in the California Community Colleges, categorical funding is only partially effective in meeting state priorities and has several shortcomings:

(1) There is no clear logic for when categoricals are appropriate

In a system of local and state-level governance, the categorical funding mechanism has the potential to guide local districts toward the accomplishment of high priority state goals. However, there is no apparent logic as to which programs receive categorical funding in terms of their relationship to state priorities. Why is special, protected state funding needed for colleges to assess incoming students and advise them into appropriate courses? Is this not a core college function which colleges should need no extra incentive to fulfill? How is this different from other basic college functions like providing reference librarians or computer lab staff to help students in their academic pursuits, services for which there is no categorical funding? Moreover, what is the state interest in supporting 72 local collective bargaining processes while providing special funding to override the outcomes of those processes with respect to part-time faculty compensation?

An example of appropriate state intervention in local priorities might be a special categorical program to encourage districts to develop common course numbering to simplify the transfer of credits among colleges. This would clearly be a case where the state would be using this funding mechanism to compel attention to a state priority that would not be attended to otherwise.

(2) Program goals are not always advanced

Even if one accepts the purposes for which categoricals *have* been established, the analysis above leads to the conclusion that those purposes are not likely to be accomplished through the current funding design.

First, district funding, under the five programs reviewed above, is not driven by the outcomes achieved – or even by the services provided. Funding is based on inputs, such as enrollment and past year expenditures. There is no assurance that the intended goals of each program will be accomplished. If the state wants results that require overriding local priorities, it is reasonable that it pay for those results. But the current approach gives funds to districts irrespective of those intended outcomes. In some cases districts are not even required to spend the funds on the program's purpose.

Second, the funding formulas themselves are not designed to align with stated program goals. Many of the categoricals provide districts an arbitrary base allocation that is not tied to need and at least one program has a formula that is inconsistent with the program's goals. Several formulas include a guarantee of 95 percent of prior year funding regardless of accomplishments, which provides little incentive to meet program objectives. Penalizing districts for not spending the money promotes a use it or lose it mentality to spend, regardless of need or outcome.

Third, the existence of categorical funding may, in fact, reduce a college's local support for these programs. Most categoricals are designed to augment funding for activities already funded in part from district base budgets. Paradoxically, this approach may allow districts to reduce their investment in areas that the state wants expanded. Maintenance of effort and local match requirements attempt to guard against the supplanting of district funds but the Chancellor's Office limited staffing typically precludes comprehensive enforcement of these provisions. Indeed, many campus officials acknowledge that meeting these requirements is often left to the honor system.

(3) Categoricals have high administrative costs

In an attempt to ensure that programs accomplish their goals, the Legislature imposes heavy reporting requirements on the CO, and the CO, in turn, imposes heavy reporting requirements on districts. Separate reporting requirements exist even for programs with similar goals. For example, districts must prepare and submit separate plans for each of three programs discussed above (Matriculation, EOPS, and DSPS) even though the programs have similar goals and serve many of the same students. Each program calls for students to indicate educational objectives and enter into contracts or educational plans; all three provide counseling and advising, orientation, and job placement assistance. These reporting requirements create considerable, and sometimes duplicative, workload at the campus and district levels to prepare the reports, and at the system level to monitor district reports. When issues of non-compliance arise, as they invariably do, the standard response by the state and the system is to enact more rules and regulations, which require more enforcement. This exacerbates the tendency to focus on regulations and enforcement instead of on results.

(4) Categoricals preclude shared understandings of priorities

It was stated in interviews many times over that a principal reason for categorical – which predominate in the student services arena – is that advocates for the programs and services supported through categorical funding do not trust local boards or local officials to do the right thing. Or, more charitably, they don't believe that local boards or local officials wield sufficient power to do the right thing. Categoricals are also defended as necessary to insulate certain non-FTEs generating activities from financial pressures to increase enrollment. It may be naïve to believe that a college could develop a resource allocation process that would attempt to match allocations with the priorities of the institution as a whole, without the constraints and protections attendant to the many categorical funding streams. However, it is discouraging to accept as inevitable a process that is built around fear and distrust – a process that will never compel all parties to collectively define institutional priorities.

Restrictions on the Use of Appropriated Funds

"If states are going to hold the postsecondary system accountable for the major outputs in the compact, they need to be willing to reduce rules and regulations over the system so that it has the flexibility to meet the goals."

A Compact for Postsecondary Education, National Governors' Association

In the report *Ensuring Access with Quality to California Community Colleges*, the CCC are described as "one of the most highly regulated systems of higher education in the nation" with "myriad prescriptive statutes and regulations" that impede colleges' efforts to use their limited resources most effectively.⁵³ These regulations are imposed by the Legislature, primarily motivated by political concerns, as well as by the system itself as a means to implement legislative mandates. However well-intentioned they may be upon initial adoption, they bind the hands of leaders to use resources most effectively, cost

considerable sums in administrative compliance, and divert attention from matters of quality and student success.

The *Ensuring Access* report called for an external commission to conduct an in-depth review of the regulatory impediments to efficiency, access, and quality. This report does not provide an in-depth review of the multitude of constraints and regulations contained in the Education Code and Title 5 regulations since the focus is on finance policy. But the examples included here illustrate the larger concern raised in the report that the California Community Colleges are "plagued" by a legacy of "detailed state regulations that erroneously assume 'cookie cutter' uniformity of the colleges."⁵⁴

This section describes and analyzes five regulations that prescribe the use of funds by colleges. In an environment of local collective bargaining, where teaching is central to the mission of the colleges, it is no surprise that instructor salaries are the focus of four of these regulations. Each of the first four policies has strong support among certain faculty groups because the policies protect quality education, as they understand it.

(1) 50 percent of expenditures on classroom instruction

Districts must expend at least 50 percent of their operating budgets on instructors' salaries and benefits each fiscal year.⁵⁵ The current version of the law was enacted in 1961 in response to concerns that colleges were increasing class size and allocating more money to administrative and counseling services. It was, and is, seen as a means to protect educational quality by preventing excessive expenditures on administration and ensuring that adequate funds are devoted to the core of the enterprise. Yet the specific 50 percent standard is arbitrary. And expenses beyond instructor salaries are not necessarily administrative but cover many core services that directly support instruction.

Counselors and librarians are *not* included in the instructional portion of the budget. Additionally, those portions of a faculty member's workload that are not actually "devoted by the instructor to the teaching of students of the district," such as curriculum development, department or college governance, and hiring committees, must be pro-rated out of the computation of "salaries of classroom instructors."⁵⁶

If a district fails to meet the 50 percent requirement, it must submit forms to the Chancellor's Office, notify its faculty, hold a public hearing declaring why it did not make it, and develop a plan to remedy the problem. The deficit is reported to the Board of Governors. If a district persists in missing the standard, ultimately it has the choice of forfeiting funds to the state or paying faculty the additional amount that would be required to reach the 50 percent standard.

Incentives

Incentives are relevant in two ways: those attendant to the law itself and those that prevent any reconsideration of the law.

The law creates an incentive to increase spending on faculty salaries if necessary to reach 50 percent, regardless of the needs of students, the college, or the local community. Circumstances have changed dramatically since this provision was enacted. If there is truth to the claim that funds spent on administrative support detract from educational quality and student success, the same cannot be said for funds spent on student support services such as financial aid counseling, academic counseling, and retention programs. These services are increasingly vital to today's community college students.⁵⁷ Districts are faced with an incentive to assign lower priority to some of the functions that they know are critical to student success. They also have an incentive to minimize the portion of faculty time devoted to activities outside of the classroom (e.g., curriculum development, academic advising, advising student clubs and organizations), activities which are important contributions of full-time faculty.

There is a disincentive to replace retiring faculty with less costly junior faculty – generally a very cost-effective action as it frees up salary dollars for other campus priorities. If a district is right at 50 percent and replaces retiring senior faculty with the exact same number of junior faculty, it could fall below the 50 percent target. In that situation, a college might, in order to stay in compliance, hire more faculty than would be justified on the basis of need and other priorities.

While the 50 percent law was intended as a floor for expenditures on instruction, it has become as much a ceiling as a floor in some districts. In these cases, local officials have an incentive to limit the expenditure of funds on classroom instruction because they would face criticism for spending

more than is required in the face of competing priorities. Either way, there are incentives to attend to pressures – financial and political – other than those reflecting the needs of students and the local community.

The incentives that keep the law in place are also important to understand. FTES-driven funding provides an incentive for enrollment *but not necessarily for quality*. Without the 50 percent law, a college could divert funding from classroom instruction, without losing enrollment or revenue, by increasing class size. At a certain point, this would lower quality. If colleges had fiscal incentives for *quality*, not just enrollment, there would be a built-in guard against diverting excessive funds from the classroom.

Does "50 percent" policy reinforce state priorities?

Readiness	-	Discourages time spent by faculty and staff working with K-12 to align curriculum or otherwise help improve readiness
Access	+/-	Promotes access through spending guarantee on classroom instruction; impedes access through limits on functions supportive of access (e.g., outreach to K-12, financial aid administration)
Completion	-	Discourages investment in support services that are increasingly critical to persistence and success
Workforce	-	Disincentive for faculty to participate in curriculum development needed to align academic programs to needs of the workforce
Efficiency	-	Imposes artificial constraints on use of resources

(2) 75/25 ratio of full-time to part-time faculty

AB 1725, enacted in 1988, requires that 75 percent of the hours of credit instruction at each community college district be taught by full-time faculty. The balance between full-time and part-time faculty in community colleges has been a national concern since the inception of two-year institutions. The publicly-reported motive behind California's adoption of this provision was to ensure that hiring decisions be made on the basis of quality, not fiscal, considerations. The actual genesis of the requirement was a negotiated settlement between administrators and faculty that reconciled union concerns about full-time employment with management's concerns about the length of service required for granting tenure.⁵⁸ The requirement has been refined over the years, including the addition of counselors and librarians to the full-time category.

Because full-time faculty participate more fully in curriculum development, student advising, departmental administration, and other activities, a core of full-time faculty is vital to educational quality. At the same time, "the employment of part-time temporary faculty is both appropriate and necessary, especially in vocational programs where part-time faculty members may be practicing professionals in the field."⁵⁹ The 75/25 ratio is an arbitrary standard that was not based on research on educational quality but was a political compromise over other issues, as noted above. Some research has since found that a higher percentage of part-time faculty in an institution reduces the likelihood of completion, while other research has found no effect.⁶⁰ In any case, there is no particular analytical justification for the 75 percent figure across all colleges.

The Title 5 implementing regulations are constructed around a "faculty obligation number" for the employment of full-time faculty by each district. The number has been adjusted each year since 1988 based on changes in district enrollment. If a district falls short of its obligation, it loses the funds equivalent to its shortfall. The implementing regulations do not ensure that the ratio of full-time to part-time faculty improves for those districts whose ratio in 1988 was below 75 percent because it is based on replacing departing full-timers with new full-timers, not with increasing the portion of full-timers. As a result, most districts are in compliance with the obligation number but many are out of compliance with the 75 percent

ratio. A Chancellor's Office Workgroup found an average ratio of 62 percent in Fall 2004.⁶¹ The Fall 2005 Faculty Obligation Report shows that only three districts are at, or above, 75 percent full-time faculty whereas all but three have met their faculty obligation targets.

There have been battles internal to the system over how the ratio itself is computed. For example, faculty overload units are, at the insistence of faculty, not included in the computation of full-time credit instruction. This seems to signal that the purpose of the rule is not as much about the quality of instruction delivered to students as it is about the employment of full-time faculty. Most importantly, these battles illustrate a key feature of the CCC regulatory environment, in which the focus of debates is often on factors other than what will foster increased student success.

A main area of dispute on the 75/25 policy concerns the application of the ratio to career/technical faculty. The issue is whether there may be a greater need for part-time faculty in career/technical fields where practitioners from business and industry are valuable in the classroom and where reliance on tenured faculty may limit the flexibility of colleges to respond to rapid changes in industry. Governor Schwarzenegger's California Performance Review (CPR) recommended modifying the requirement for career and technical instruction, suggesting that colleges redirect the savings toward expanding instruction.⁶² Later, the Administration sponsored legislation to exempt career technical faculty from the 75/25 law out of concern that the law inhibits colleges from appropriate expansion and alteration of vocational offerings.⁶³ The Academic Senate of the CCC has formally opposed the exclusion of career/technical faculty.⁶⁴

The Workgroup report on the 75/25 policy identified some internal resistance to the policy on the grounds that "the regulations do not take into account how the unique characteristics of an individual college can affect its ability to make progress toward this statewide goal."⁶⁵ The report cited challenges faced by small colleges, including small class size, difficulty in creating a full-time load in some disciplines, and other built-in inefficiencies that make the 75/25 requirement unrealistic for them. It noted that large

urban districts face difficulty attracting full-time faculty because of the high costs of living. The report stated that many districts have higher priorities than meeting the 75/25 ratio, including hiring additional classified staff in support of technology, student services, and learning resources, contractual obligations to existing faculty and staff, and flexibility in course offerings to respond to changing community needs. The Workgroup recommended revisions to the regulations to accommodate variability in circumstance and concluded that a new “dedicated funding stream” is essential to making progress toward increasing the percentage of full-time faculty employed by the system.

Incentives

The policy contains a strong incentive for districts to meet their faculty obligation number because they lose funding if they fail to meet it. The incentive to meet the target places districts in the position of putting financial considerations above educational quality considerations, in precise opposition to the stated purpose of the policy. For example, districts may have to hire full-time faculty when the highest priority is to expand instruction in areas for which part-time faculty are more readily available or more qualified. Most important, decisions like these have to be made for reasons that may have little to do with student success.

As discussed with respect to the 50 percent law, there is a clear relationship between the strong support for the 75/25 rule and the incentives built into FTES-driven funding. A college most certainly could achieve the same FTES at less cost or it could increase its FTES at no additional cost if it were to rely more heavily on part-time faculty. At some point, quality would suffer. But as long as colleges have no *fiscal* incentive to deliver quality, there will be strong support for regulatory limits on the use of part-time faculty.

Does “75/25” policy reinforce state priorities?

Access	-	Encourages hiring of full-time faculty irrespective of student demand; could reduce access to courses and programs in fields where part-time faculty are more prevalent
---------------	---	---

Completion	+/-	Encourages hiring of full-time faculty, who are more available to help students through their programs; but can impede offering classes that students need
Workforce	-	Limits flexibility of colleges to respond to local workforce needs
Efficiency	-	Imposes artificial constraints on the use of resources; enforces single standard despite huge variation in mix of curriculum, cost of living, faculty hiring pools, faculty contract obligations

(3) 60 percent limitation on part-time faculty workload

The Education Code classifies any employee who teaches no more than sixty percent time at a college as temporary, and therefore not eligible to move into the tenure system.⁶⁶ Known as the sixty percent law, this provision was enacted in 1967 pursuant to SB 316. It serves as a cap on the workload of a part-time faculty member beyond which the college is required to hire that individual on a tenure track. As such, it protects districts from lawsuits by part-time faculty who seek permanent jobs. The law was amended in 2003 to ensure that the non-teaching aspects of part-time faculty workload do not count toward their 60 percent limit.

The sixty percent law created a class of employees known as freeway flyers - adjunct faculty who cobble together full-time employment by teaching classes in multiple districts. Opponents of this law claim that it hurts student instruction because these faculty have limited time for direct student contact. They charge, as well, that it constitutes an “end-run around tenure” to obtain “a cheaper and more malleable workforce, the permanent ‘temporary’ employee.”⁶⁷ Faculty associations and unions at community colleges have debated changes to this law, and legislation has been proposed to increase the percentage to 80 percent, which would do nothing to provide long-term job security to part-timers, but would reduce their need for freeway flying in order to piece together a full workload. Some worry

that any changes to the law allowing adjunct employees to teach closer to full time in a district would constitute an even greater end run around tenure, and worsen labor conditions in community colleges.

Incentives

The 60 percent law causes districts to distribute their part-time faculty workload across more individuals than it would in the absence of the limit in order to prevent having to offer tenure and long-term contracts to more faculty. This creates more administrative workload for hiring and managing a greater number of faculty. The 2003 change in the law made it more practical for districts to give non-classroom assignments to part-timers.

Does “60 percent” policy reinforce state priorities?

Access	-	Inhibits spending instructional dollars on the faculty and course sections judged to best meet the needs of students
Completion	-	Inhibits persistence and completion by limiting availability of part-time faculty to students
Workforce	-	Prevents districts from employing certain faculty more than 60 percent time when that person’s expertise may be needed to best align the curriculum with the needs of local workforce
Efficiency	-	Constrains districts from determining most efficient allocation of instructional budget; imposes high costs on districts to monitor compliance with 60 percent limit

(4) Two-semester limitation on temporary faculty hiring

Education Code Sections 87480-87482 define “temporary” faculty as those hired to respond to short-term needs created by sudden enrollment increases or replacement in the classroom of faculty who are ill or on leave. The law limits the period over which temporary faculty may be employed to two semesters over the period of three years. The limitation is intended to allow districts to use temporary, full-time faculty

to respond to short-term needs but to prevent them from relying too heavily on temporary faculty at the expense of supporting a core of full-time and part-time, benefited faculty.

Incentives

The two-semester limit can prevent districts from investing appropriately in programs for which permanent faculty cannot easily be recruited. A case in point is the current nursing situation (see box on p. 30). Districts have not been able to compete successfully in the marketplace for full-time nursing faculty. There are opportunities to hire practicing clinical nurses to teach part-time on a temporary basis, but the two-semester limitation makes it difficult for districts to use temporary faculty over an extended period as they develop more permanent staffing solutions.

Does two-semester limit policy reinforce state priorities?

Access	-	Limits access into certain programs if district is unable to hire sufficient faculty to expand program offerings
Completion	-	Limits course offerings that students may need
Workforce	-	Discourages districts from employing part-time faculty as needed to offer high-demand programs
Efficiency	-	Constrains districts from determining the most efficient allocation of their instructional budgets

(5) Limitations on student employment on campus

Education Code provisions make it difficult for colleges to hire students to work on campus by requiring that all district employees either be academic or classified employees, the working conditions of the latter subject to collective bargaining. The law exempts full-time students employed part time and students enrolled in college work-study programs, although it requires that the employment of these students “shall not result in the displacement of classified personnel.”⁶⁸ Unless a part-time student is hired and compensated as a classified employee, he or she cannot work on campus unless enrolled in a work-study program

funded by federal or state funds. Additionally, Education Code section 81676 provides that persons employed in college-run bookstores must be part of the classified service. Around the country, including California's public universities, large numbers of students are employed on campuses as a way of meeting students' financial needs while maximizing their connection to campus and meeting colleges' needs for jobs to be performed as appropriate to college student abilities.

Incentives

These prohibitions can cause colleges to hire classified staff at higher salaries than would be necessary and cause students to seek employment off campus, which reduces the time they are able to spend on campus.

Do student employment policies reinforce state priorities?

Affordability	-	Students are denied access to employment that could help them defray college expenses
Completion	-	Limits student involvement in campus life which, research shows, reduces persistence and success ⁶⁹
Efficiency	-	May cause districts to pay more for the same work

Case Study: Attempts to Address the Nursing Shortage

Chapter 837, Statutes of 2006 (SB 1309, Scott) is a noble effort to address a problem of extreme importance to the state – a severe shortage of nurses – amid myriad regulatory constraints. One of the constraints the state faces in producing an adequate number of nurses is a shortage of nursing faculty. Clinical nurses typically earn much higher salaries than do nursing faculty. The shortage of faculty prevents districts from expanding their nursing enrollments as much as they otherwise could, within available resources. Colleges have found that clinical nurses are often interested in teaching part-time and/or on a temporary basis. But the regulations governing the hiring of part-time and temporary faculty restrict this option.

In addition to other provisions to help districts recruit nursing faculty, the new law attempts to navigate its way through hiring restrictions, as follows:

- It exempts clinical nursing faculty from the two-semester limitation on the hiring of temporary faculty – increasing the limit to four semesters within any period of three academic years, through 2014.
- It requires districts that use this nursing exemption to report data to the Chancellor's Office on the number of faculty hired under the exemption and the impact of that hiring on the district's ratio of full-time to part-time faculty (by reporting the ratio for three years prior to the new hiring and each year thereafter).

- It requires the Chancellor's Office to report, in writing, to the Legislature on how many districts employed faculty under the exemption provisions of the new law and what the impact of the hiring has been on the ratio of full-time to part-time faculty for three years prior to the new provision and each year thereafter.
- It forbids a district to employ a clinical nurse pursuant to this new law if such hiring results in an increase in the ratio of part-time to full-time nursing faculty.

The layering of regulation upon regulation is consistent with the way that the community colleges have been governed and reflects their K-12 heritage and complex political environment. The needs of internal stakeholder groups appear to have taken precedence over the needs of the state and the students on this issue. In the face of an extreme nursing shortage, and the opportunity for the community colleges to play a major role in addressing it, what we have instead are more constraints, more administrative workload, and impediments to using clinical nurses to help the colleges accommodate more nursing students. The interests of the state have been sacrificed in favor of arbitrary limitations that, however well-intentioned, have not been justified on educational grounds, and were enacted before anyone could have envisioned their impact on the health of Californians.

Student Fees

The aspects of fee policy that are most relevant to a discussion of incentives facing students and institutions are:

- the absence of a policy for determining the level of student fees
- the historically low level of fees
- fee waivers for needy students
- the offset of fee revenue in apportionment calculations
- no fee charged for non-credit instruction
- prohibitions on campus-level fees.

We analyze each of these in turn and conclude with a summary of the collective impact of student fee policies on the behaviors of students and colleges, and ultimately on the state goals that need attention.

(1) Absence of policy establishing fee level

In this instance the state “policy” is the absence of policy for setting an appropriate level of student fees, or the share of costs that the state should expect non-needy students to pay. The annual per-unit fee is set by the Legislature. Since the inception of the enrollment fee in 1984, changes in the fee level have been in response to state budget conditions. Budget downturns have led to five increases in the fee and three times an improved state economy has occasioned a fee reduction.⁷⁰ Precipitated by external conditions rather than purposeful policy, changes have been immoderate and unpredictable – quite the contrary to stated state policy for adjusting fees.

Incentives

Sudden increases in fees have been accompanied by enrollment drops that have concerned lawmakers and college officials alike, since college funding is so dependent upon growing enrollments. Even though reductions in course sections, caused by budget cuts, have been shown to be in part responsible for enrollment declines,⁷¹ colleges fear fee increases for their impact on FTES-driven funding. College and system officials become partners with students in the lobbying efforts against fee increases. The absence

of a fee policy leaves the level of the enrollment fee open as a political issue each year and diverts attention from larger issues of affordability. With fees accounting for five percent of college costs, failure to focus on the major cost components is likely one reason why CCC students apply for and receive financial aid at lower rates than community college students in other states.⁷² Finally, the absence of a fee policy may reinforce the tendency of Californians to view community college fees only as barriers to enrollment and not as a source of revenue to colleges. A fee policy would likely be based on the idea that students and taxpayers have a shared responsibility to fund the community college system – calling attention to fees as a source of revenue that can help pay for student access to college and to classes.

Does the absence of a fee policy reinforce state priorities?

Access	-	Depresses access by unpredictable, immoderate increases
Affordability	-	Reduces attention to primary determinants of affordability
Completion	-	Heightens resistance to fees, depriving colleges of revenue that could increase course offerings and support services

(2) Historically low fee levels

California has a long-standing commitment to access as set forth in the 1960 Master Plan and as funded through 50 years of low-cost public institutions and state funding for financial aid programs. Affordability is recognized in state law. In Section 66002(e)(3) of the California Education Code, the Legislature finds and declares,

“California must support an educational system which prepares all Californians for responsible citizenship and meaningful careers in a multicultural society; this requires a commitment from all to make quality education available and affordable for every Californian.”

Since the state relies on the CCC to provide the majority of the access to affordable education, it has followed a policy of very low fees in that segment. California's community college fees are the lowest in the nation. At \$20 per unit, a full-time academic year load of 30 units will cost \$600. The national average for two-year public colleges is \$2,272.⁷³ Most community college students attend less than full time and incur annual fees of less than \$500, unless they are financially needy, in which case they pay no fees (the fee waiver policy is discussed later).

Fees, being low, are not the main driver of college affordability.⁷⁴ Table 1 shows college cost information to which the California Student Aid Commission website directs students. The table shows that fees account for five percent or less of the total cost.

Table 1
Fees are a Small Portion of College Costs

	Living With Parents	Living Independently
Fees	\$480*	\$480*
Books and supplies	\$1,422	\$1,422
Room and board	\$3,978	\$9,936
Miscellaneous	\$3,330	\$3,348
TOTAL	\$9,210	\$15,186
Fee as a % of Total	5.2%	3.2%
* Estimate is for 12 units/semester. Source: <i>How Much Does College Cost?</i> accessed at http://www.californiacolleges.edu/finance/how-much-does-college-cost.asp		

Incentives

Low fees provide a strong incentive for students to enroll in college. The impact of low fees on access is well known and highly celebrated in California. Less often discussed are some of the less sanguine incentives embedded in a low fee policy. It stands to reason, unless basic economic and psychological tenets are wrong, that students value more highly that for which they must pay more. At the cost of \$60 per class, a non-needy student (the only students who

need to pay fees) is unlikely to take as much care in selecting appropriate courses and staying enrolled until the end as he or she would if a more substantial personal investment were required. A needy student faces no fee-related financial costs of dropping a course, taking the wrong course, or performing poorly and having to repeat the course. As the Little Hoover Commission noted in its 2000 study:

*"There is little financial incentive for students to make good progress or invest the time and effort necessary to make good course selection decisions. Low tuition encourages students to pick and choose courses knowing they can be dropped with little financial impact."*⁷⁵

Our analysis of the six-year enrollment patterns of the 1999-2000 entering cohort of CCC students confirms that there is a high rate of course dropping in the CCC.⁷⁶ Certainly there are reasons other than low fees why students drop courses. But the high course drop rate suggests that students are not deterred by financial consequences from dropping courses. Another report suggested that placing a higher price tag on community college courses would send a signal to some students to take the experience more seriously.⁷⁷

While low fees encourage college enrollment, they do not necessarily help the state increase education levels. From one perspective, high college participation is validation that the state provides broad access to college and values lifelong learning. But from another perspective it raises a question about the return on investment of those scarce dollars that taxpayers make available for educating Californians. In addition to promoting access by those seeking basic skills, degrees, or career advancement, low fees encourage enrollment for other purposes. Over 85,000 students, accounting for 16 percent of the cohort of first-time CCC students in 1999-2000, enrolled for personal enrichment, outside of any degree or certificate program.⁷⁸ Many of these enrollments were in art, music, foreign languages, humanities, and physical education classes. One could reasonably ask whether the state funds that support these students at low or no fees might better address state priorities if used to improve levels of support for degree-seeking students or to enroll more degree-seeking students. If fees were higher, the incentive structure would change such that some students attending for personal enrichment

would value the courses sufficiently to pay more for them and others would choose not to enroll. Either way there would be more resources available that the state could use to support credential-seeking students.

Also worth noting are the incentives *forgone* by a policy of low fees. Low and waived fees deprive the system of a powerful tool for influencing student outcomes. Across the country, as states grapple with ways to increase student completion rates, fee policy is being recognized as having many more dimensions than just up or down, high or low. Fees can be raised, lowered, refunded, and waived *conditionally* if students engage in desired behaviors. For example, students who attain proficiency in English and math within a prescribed timeframe could pay reduced fees for the remainder of their terms. Fees could be refunded once a student has completed some portion of her program of study. Or, students who enroll in high-need programs could have their fees waived. Options like these will be discussed in more detail in Part IV. By having such a low fee, the system loses huge opportunities to influence student success and shape desired state outcomes. A major lever for changing outcomes is forfeited.

Does low fee policy reinforce state priorities?

Access	+/-	Encourages access but not necessarily by those seeking educational credentials; limits access by limiting revenues
Affordability	+/-	Helps keep college inexpensive, yet does little to address the overall affordability issue
Completion	-	Discourages careful enrollment decisions by students; deprives state of powerful tool to influence student success; reduces student awareness of financial aid options which could promote success

Workforce	-	Prevents colleges from using fee policy to encourage students to enroll in high-need programs
Efficiency	-	Fails to target public dollars to needy students; subsidizes students who would willingly pay a higher fee

(3) Fee waivers for needy students

Students with demonstrated need have their enrollment fee waived. There are two quick eligibility determinations (public assistance recipients, family income below 150 percent federal poverty level) and one that involves computing federal estimated family contribution and subtracting that from cost of attendance. Any student who demonstrates at least one dollar of need gets a full fee waiver. Many middle class families can qualify for the waiver based on this third eligibility method.⁷⁹ The Legislative Analyst’s Office reports that a dependent student in a family of four with an income as high as \$80,000 could receive a fee waiver.⁸⁰ There are no other eligibility requirements for receiving or renewing a waiver, such as grade point average, unit load, or progress toward an academic goal. The fees waived in 2007-08 are estimated to amount to \$224 million in revenue that will not be collected by the system.⁸¹

This section analyzes the impact of this policy from the perspective of fee policy. In a subsequent section on student financial aid, we again discuss the BOG fee waiver program in relation to student financial aid policies.

Incentives

The previous section described how the policy of low fees limits the state in implementing policy options being considered in other states to encourage certain student behaviors. The fee waiver policy exacerbates this limitation by charging no fees to a significant portion of the student body. Twenty-nine percent of all students receive a fee waiver. Students who apply for and receive a fee waiver take a much higher course load, on average, than those who do not, such that the quarter of the student body receiving waivers account for 42 percent of FTES.⁸² This suggests that many eligible students taking one or two courses do not bother to get a waiver but could, for example, if fees rose or if differential fee rates were set to encourage full-time

attendance (making fees higher for part-time students). The eligibility for a fee waiver by such a large portion of the student body means that the system has very little opportunity to influence student behavior through fee policy.

Does fee waiver policy reinforce state priorities?

Access	+	Promotes access among those populations whose increased educational attainment is vital to the state's well-being
Affordability	+/-	Eliminates fees as a component of costs for needy students yet does little to address the overall affordability issue
Completion	-	Nullifies ability to use fee policy to encourage completion for the large number of students eligible for fee waivers
Workforce	-	Limits use of fee policy as a mechanism to encourage students to enroll in programs of high need in the region
Efficiency	-	State pays some of the cost that the federal government is willing to pay through tuition tax credits

(4) Offset of fee revenue in apportionment calculations

All but two percent of the revenues collected from the student enrollment fee is deducted from the computed state apportionment to districts. The two percent is intended to be used by districts to cover administrative costs of fee collection. In effect, fee revenue is just a revenue source that contributes to the computed district funding entitlement. The entitlement is computed, local property taxes and fee revenues are credited toward that amount, and state General Funds are allocated to make up the balance. Under this system, fees are not seen by students or colleges as a potential source of *added* revenue. Fees are viewed only as a barrier to access instead of as a source of revenue that can *increase* access by financing

more class sections or more services. In theory, fees could be used to augment available revenues, but the practice in the state, for UC and CSU as well as for the CCC, is to consider fee revenue as an offset to state appropriations.

Incentives

The offset policy removes any incentive for colleges to support fee increases as a means of revenue enhancement because they know that a fee increase will not increase revenues to the system. Students, likewise, have no incentive to support a fee increase because they have no reason to think that it will enhance course availability or support services. Until a fee policy is adopted that makes it clear that a rise in fees is a net revenue gain to colleges (e.g., a fee policy under which students pay a fixed percent of per-student costs), colleges and students will continue to overlook the possibility that fee increases can *increase* access by providing more revenue to support course sections.

The removal of fee revenue from local control leaves college leaders with no tools for responding to short-term enrollment changes and other local conditions. In many states, control of tuition revenue is an important tool by which college presidents can manage their resources to meet local demand. In the CCC, college presidents must focus their energies on managing the myriad state formulas and rules.

Does policy of offsetting fee revenue reinforce state priorities?

Access	-	Discourages support for fee revenue that could increase access
Completion	-	Discourages support for fee revenue that could enhance support services that promote persistence and success
Workforce	-	Limits college ability to respond to short-term enrollment needs of the workforce
Efficiency	-	Limits local control over resources to meet local needs

(5) No fee charged for non-credit instruction

Unlike credit courses, for which non-needy students pay a per-unit enrollment fee, non-credit courses are free to all students, regardless of financial circumstances. As the name implies, non-credit courses provide no college credit for students who take them. However, non-credit courses in basic skills areas of English and math may serve as prerequisites for eventually moving to credit courses. Non-credit courses are offered in nine categories: parenting; elementary and secondary basic skills; English as a second language; citizenship; disabled adults; older adults; health and safety; short-term vocational; and home economics. In fall, 2006 there were more than 35,000 non-credit FTES students enrolled in the community colleges.⁸³

Incentives

Because non-credit courses are offered for free, students may have an incentive to enroll in them even if they perceive only a small value in the course. With little financial investment, students have little to lose if they drop out of a non-credit class, and have little reason to object if the course does not meet their expectations. As a result, students may be less committed to their coursework and may demand less from their instructors than if they were paying for non-credit courses.

Does policy of no fees for non-credit reinforce state priorities?

Readiness	+	Encourages adults to begin to prepare for college-level work
Access	+/-	Encourages enrollment of students who must begin at very low levels of basic skills instruction before attempting credit work; includes courses which are not prerequisites for credit
Affordability	+	Makes non-credit instruction affordable to all Californians
Efficiency	-	Subsidizes some students who would willingly pay a fee

Completion	+/-	Encourages movement of students from non-credit to credit due to higher credit funding rate; no financial incentive to keep student enrolled beyond census
Workforce	+	Provides language skills to non-English speaking and low-skill workers, increasing workforce competency

(6) Prohibitions on most campus-level fees

Districts can charge students a mandatory fee only if it is expressly authorized by law.⁸⁴ Under current law, community colleges are prohibited from imposing fees for such things as dropping courses after the census date, repeating courses, or registering late for classes.

Incentives

Districts are deprived of a tool by which they could encourage successful student enrollment behaviors and improve the efficiency of campus operations. Research has shown that late registration in courses and rampant course dropping reduce the chance of successful course completion.⁸⁵ If students had to pay a fee for such behavior they might better plan their educational programs. In addition, if students paid a penalty for taking the same course more than two times, for example, they might be inspired to work harder at succeeding. To the extent that prospective students are aware that community colleges have lenient policies for course repeats and course drops, these policies also act as disincentives for students to prepare better for college. If students knew that there were penalties for failing or dropping courses, they might do more to prepare before enrolling.

Districts would also benefit from a reduction in these kinds of unsuccessful behaviors because they could use their resources more efficiently, filling a greater percentage of available classroom seats and serving more students with the same amount of total resources.

Does policy prohibiting campus fees reinforce state priorities?

Readiness	-	Students not encouraged to increase college readiness
Access	-	Reduces access through inefficient use of available space in classes
Completion	-	Deprives colleges of a tool for influencing student behavior in ways that could increase their success
Efficiency	-	Colleges could serve more students at the same cost if fees could be used to encourage successful course-taking patterns

Conclusions regarding fee policy impact on state goals

Each of the various aspects of fee policy has its own set of impacts, as discussed above. The overriding characteristic of fee policy for the California Community Colleges is that it sustains very low fees in the effort to maximize access and enrollment. The consequences of this can be summarized as follows:

- California has very high participation rates among broad populations, many of whom never complete an academic credential or seek to complete one.
- CCC revenues per student are well below national averages with the difference largely attributable to the low level of fee revenue.
- Despite the impact of low fees on system revenues, there is virtually no stakeholder support for increasing fees, as fees are viewed only as barriers to access – not as a source of revenue that could increase access and success.
- Taxpayers cover most of the educational costs for middle- and upper-income students who would be able to pay more for their education.
- The deduction of fee revenue from appropriations computations leaves colleges without control over revenues that could be used to respond to short-term needs.

The low fee policy must be understood within the context of the funding formulas that reward enrollment growth. We have observed that lawmakers are not particularly interested in an analysis of *which* students did or did not gain access to the community colleges when fees were raised or lowered, and are not convinced by the argument that low fees do not help needy students because needy students do not pay fees. This is likely because they are representing the interests of the colleges in their districts who “live or die” on the basis of enrollments – irrespective of who the enrollees are. What is most important, within this policy framework, is that higher fees mean lower FTES and fewer dollars and lower fees mean higher FTES and more dollars. Within this framework, it matters not whether the FTES will translate into educated Californians, more social and economic equality, and improved economic health. Only when colleges are funded for educating students and not for simply enrolling them can we expect more attention to the nuances of fee policy raised in this section.

Financial Aid

Students attending California Community Colleges have access to various forms of student financial aid:

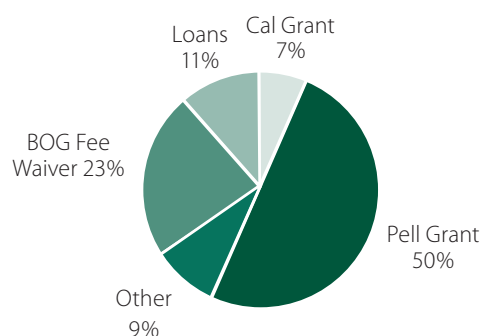
- The program serving the largest *number* of students is the Board of Governors’ fee waiver program, which serves 29 percent of the students enrolled for credit.
- The program providing the greatest *amount* of funding is the federal Pell Grant program, which provides grants to about 10 percent of credit students and provided \$590 million in direct aid to CCC students in 2005-06.
- The Cal Grant program, which gets most of the policy attention in Sacramento, serves *by far the fewest students* and distributes the least amount of funds – providing \$76 million to about 2.5 percent of credit enrollment in 2005-06 and accounting for only 7 percent of aid funds.

- Students also receive federal loans, work-study funds, and various other grants and scholarships, which collectively account for 20 percent of total financial aid.

Figure 4 shows the distribution of student aid in 2005-06.

Below we describe and analyze state financial aid policy in three parts: the BOG fee waiver, Cal Grant, and the overall approach to providing student financial aid to community college students.

Figure 4:
Financial Aid By Type in 2005-06 -
Cal Grant Accounts for Small Amount of Aid



Source: California Community Colleges Chancellor's Office Data Mart:
<http://www.cccco.edu/divisions/tris/mis/reports.htm>

(1) Board of Governors' Fee Waiver

The BOG fee waiver is effectively an entitlement program with estimated foregone revenue included in the state budget each year. Twenty-nine percent of all credit students receive the waiver, accounting for 42 percent of credit FTES.⁸⁶ The larger percentage of FTES waived is a result of the enrollment patterns of the waiver recipients who tend to enroll in more units than non-recipients. The waivers granted in 2005-06 cost the state about \$274 million. The program was included in the same legislation that established the first community college enrollment fee in 1984 so that fees would not hinder students from obtaining a higher education.

There are three categories of eligibility for the waiver – the first two provide quick eligibility for the most needy (through a short form that can be processed on demand) while the third category extends eligibility to these students as well as

to anyone who demonstrates any financial need through the filing of the federal Free Application for Federal Student Aid (FAFSA) form, which requires more time:

- Part A: recipient of Temporary Assistance for Needy Families (TANF), Supplemental Security Income (SSI) or General Assistance public benefits
- Part B: students with family incomes that fall under a set of annually indexed cut-offs (set at 150 percent of the federal Department of Health and Human Services [HHS] poverty standard)
- Part C: any student who demonstrates "financial need" according to federal methodology

Gaining eligibility under Parts A and B does not require the student to fill out the FAFSA. Income verification under Part B is required under Title 5 regulations but is interpreted by some campuses to mean simply a signed statement, as opposed to independent determination or a tax return. The FAFSA is used in determining eligibility under Part C. Any student demonstrating at least one dollar of unmet need under part C gets a full fee waiver. All California resident students who receive a Pell Grant or a Cal Grant get a BOG waiver because, by definition, they demonstrate financial need.

The BOG fee waiver is notably devoid of traditional eligibility criteria. Table 2 compares the eligibility criteria for the BOG waiver, Cal Grants, and Pell Grants. While the two grant programs place a variety of conditions on students receiving and/or retaining the grant, the BOG fee waiver has very limited academic-related conditions. Students get a full waiver regardless of the number of units they take, the length of time over which they enroll, their grades, and their academic progress or lack thereof, unless they are dismissed from the college.

Incentives

The absence of non-income criteria for the fee waiver gives students little incentive to engage in behaviors that improve their chances of success, e.g., selecting a program of study, enrolling in 6 or more units, maintaining good grades. A student who drops all her courses or earns all failing grades does not have to pay back the waiver and can continue to receive a full subsidy for the costs of her education as long as she is eligible for continued enrollment. Such a student

Table 2
BOG Fee Waiver Compared to Cal Grant and Pell Grant

	BOG Fee Waiver	Cal Grant	Pell Grant
Eligibility based on:			
<i>GPA prior to receipt</i>	No	Yes - 2.0 for Cal grant B, 3.0 for Cal Grant A, 2.4 for CCC Transfer Entitlement Grant. For Competitive Cal Grant and Cal Grant C the GPA is one component of the student's "score."	No
<i>Age</i>	No	Age is indirectly a feature because students are only eligible to apply for the Entitlement straight out of high school (or in their first year of college), with some exceptions.	No
<i>Program goal</i>	No	Cal Grant A: Program is at least 2 academic years in length. Cal Grant B: Program is at least one academic year in length. Cal Grant C: Program is at least 4 months in length.	Must be enrolled in a degree program leading to a recognized degree or certificate
<i>Satisfactory academic progress (SAP) required for renewal</i>	Yes - but only the institutional progress requirement for all students, not the more typically stringent financial aid progress requirements.	Yes - State statute requires Cal Grant to be governed by federal SAP rules (see Pell Grant).	Yes - requires both qualitative progress (2.0 GPA) and quantitative progress (complete a minimum percent of courses attempted)
<i>Minimum # Course Units</i>	No	Yes - need to be enrolled in at least 6 units	No
<i>Ineligible if hold bachelor's degree?</i>	No	Yes - cannot hold one (with one exception for 5th-year teaching credential students)	Yes - cannot hold one (with one exception for 5 th -year teaching credential students)
Eligibility time limit	None	Until completion of BA or equivalent of four years of full-time study	No time limit as long as student remains in a degree program as an undergraduate
Deadline to apply	At any time until the close of Spring term	March 2 before the academic year begins (Entitlement); Sept 2 of the academic year (Competitive)	June 30 th of the academic year

could continue with that pattern with no limit placed on the number of terms she could get her fees waived, as long as she is eligible for continued enrollment at the college.

Because students can qualify for a waiver without filling out the FAFSA, they may not become aware of the state and federal aid that may also be available to them. As a result, they may get their fees waived but not receive the financial aid they need to help meet the more substantial costs of college attendance. In fact, California students apply for and receive federal Pell grants at substantially lower rates than community college students in other states.⁸⁷ Recent efforts to emphasize the FAFSA have resulted in significant increases in Pell Grant participation.⁸⁸

The assumption that affordability is addressed by waiving fees for needy students has led financial aid offices to underemphasize other sources of aid and has removed political pressures for enhanced institutional aid in the CCC. In addition to low rates of application for and award of Pell grants, a much lower percent of California's community colleges students receive state aid (Cal Grants in this case).

From the institution's perspective, there is no incentive to control the number of students who obtain fee waivers under the existing criteria or to advocate for tightening the eligibility criteria, because waivers don't cost them anything: the colleges are reimbursed by the state for the lost revenue regardless of how many waivers are awarded. In fact, awarding waivers is a way to increase enrollment and FTES-generated revenues. As a result, community college fee waivers may be granted to students who are not likely to benefit from them, in terms of enhanced participation, persistence, and success.

Do BOG fee waiver policies reinforce state priorities?

Readiness	-	No incentive for students to have minimum high school GPA or to take a rigorous high school curriculum to increase readiness
Access	+/-	Promotes access but also hinders access by under-emphasizing importance of other financial aid

Affordability	+/-	Increases affordability but also hinders it by under-emphasizing other financial aid; lack of incentives to make forward progress can increase student costs by increasing time-to-degree
Completion	-	No incentive for students to progress toward their goals and for institutions to ensure that waivers are actually helping students succeed; encourages students to work more than they would if fee waiver award was coordinated with other sources of available aid
Workforce	+/-	Lack of requirement for enrollment in degree program extends benefits to students who are coming just for skill upgrades, but lack of incentives for persistence and completion may impede the completion of workforce programs
Efficiency	-	Student aid administered as fee waivers deprives some recipients of federal tax credits, leaving federal aid unspent ⁸⁹

(2) Cal Grant

The statewide financial aid program is administered by the California Student Aid Commission. It is a complex structure of grant programs but the primary grant available to and used by CCC students is the Cal Grant B (both Entitlement and Competitive Programs). Cal Grant A awards cover tuition and fees, which are covered by the BOG waiver for all CCC Cal Grant recipients. Consequently, Cal Grant A awards have no monetary value for CCC students unless or until they transfer to a four-year institution. In order to receive a Cal Grant, applicants must meet multiple criteria including minimum GPA, family income and asset ceilings, timely submission of the FAFSA form, and timely reporting of their GPA. The application

process requires that students complete the federal FAFSA form. Table 2 displays the academic-related criteria.

For community college students, Cal Grant B covers “access costs” related to housing, food, books, supplies, transportation, and other additional expenses up to \$1,551 per year for students taking a minimum of 12 units per term. There are two components to the Cal Grant B program – Entitlement grants and Competitive grants:

- Entitlement Grants are aimed at recent high school graduates, and are guaranteed to every student who is eligible. Students must apply within one year of graduating from high school or achieving the equivalency.
- Competitive Grants are available to older students but are limited to 22,500 awards per academic year. Half of these grants are set aside for students who apply by the March 2nd deadline, with the remaining half set aside for students who are attending a community college and who apply by the September 2nd deadline. Because of its limited availability, many students who apply for the Competitive grants are not awarded one. In 2005-06, only 18 percent of eligible applicants received one.⁹⁰ Selection is based on a composite score that takes into consideration family income, parents’ educational level, GPA, time out of high school and other factors.

Other Cal Grants are available, as follows:

- Cal Grant C awards help pay for costs at occupational or career colleges. This \$576 award is for books, tools and equipment. To qualify, a student must enroll in a vocational program that is at least four months long at a California Community College (or other institutions). Funding is available for up to two years, depending on the length of the program.
- A Community College Transfer Entitlement Cal Grant is available to students who did not receive a Cal Grant directly after high school, but who maintained at least a 2.4 GPA in community college, became

eligible to transfer to a four-year university before the age of 28, and meets the Cal Grant eligibility and financial requirements.

The real value of the access cost portion of the Cal Grant B has declined steeply over the years, rising only 15 percent in the last twenty years. Had it kept up with the California Consumer Price Index (CCPI) since the program’s inception in 1969 the value of the access cost grant would be \$5,190 – nearly three times the current award.⁹¹ Similarly, the value of the Cal Grant C has declined over time and would be four times its current amount had it kept up with the CCPI.

Incentives

The Cal Grant program is a mixture of need and merit. It provides an incentive for high school students to maintain a 2.0 GPA, provided students are aware of the program’s rules. However, there is no requirement regarding the rigor of the high school courses taken by students (i.e., whether or not the student has pursued a college preparatory curriculum) as long as the student has met the requirements for graduation from high school. In fact, the Cal Grant Programs specifically deny use of honors grade points (where a B in an Advanced Placement class or honors class may get 4.0 points in most high schools, it must be changed back to 3.0 points for Cal Grant). Ironically, concern about Cal Grant eligibility may discourage some students from taking a more rigorous curriculum because it is harder to earn high grades in advanced courses.

Students must maintain a 2.0 GPA to *remain* eligible for the Cal Grant but conditions relating to a student’s progress toward his or her educational goals can vary across colleges and are not uniformly strict.

Imposing a March 2nd application deadline for a Cal Grant rewards those students who have the information and the wherewithal to plan ahead for their college education. However, before students can receive a Cal Grant, they have to fill out a FAFSA application. This can be a hurdle for students and families who lack sufficient English- or Spanish-language skills (the FAFSA is available in Spanish).

Limiting the entitlement to recent high school graduates was a decision made on both fiscal and programmatic grounds when the Cal Grant program was redesigned in

2000. Fiscal staff were concerned that a financial aid program open to anyone regardless of age would be too costly and would make annual cost projections difficult. However, a strong consensus did exist that priority should be given to high school students because the entitlement aspect of the program would encourage more students to excel in school. Legislative staff and other observers say the limit on competitive awards was not intended to exclude older students. Rather, it was the result of political compromises and the inability to accurately estimate their population size. Regardless of intent, the impact of the policy is to provide an incentive for students to enroll in college soon after graduating from high school, if they are aware of these rules.

Do Cal Grant policies reinforce state priorities?

Readiness	+/-	Incentive for students to maintain 2.0 GPA but may discourage taking advanced courses
Access	+/-	Increases access for younger students but impact is mixed or negative for the older population; impact on access is likely dependent upon adequate staffing for financial aid outreach and administration and high school counselors
Affordability	+/-	Affordability is impeded by diminished purchasing power of the Cal Grant awards and limited availability of competitive grants
Completion	+	Completion encouraged by merit and satisfactory progress components of eligibility, and requirement that students must enroll for at least 6 units in a degree program
Workforce	+/-	Cal Grant C program aims to provide incentives for career/technical programs, but Cal Grant C has been under-utilized and is not targeted to particular workforce needs

Efficiency	+/-	Cal Grant B targets aid to needy students through means test Cal Grant C has inefficient, complex application system to award very small sums in very targeted program areas to students who must then reapply if their program goals change
-------------------	------------	---

(3) Financial aid focus on fees instead of affordability

Despite the availability of over \$1 billion of grants and loans for CCC students, the state lacks a *coordinated* policy for increasing affordability for current and prospective CCC students. This shortcoming results from several features of current policy:

- The BOG fee waiver creates undue policy focus on the smallest component of college costs, with the probable result, however inadvertent, that many students never apply for other sources of aid for which they would be eligible and that policy makers fail to comprehend larger issues of affordability. *The perception that, but for the enrollment fee, community colleges would be “free” obscures the real cost of community college attendance.*
- The fee waiver application, for many students, does not require completion of a FAFSA. Believing they have taken care of financial aid opportunities, students may elect to just fill out the BOG fee waiver form because it is so much easier and has no deadline. This can cause students to under-apply for grants and loans.
- There is no equivalent at the CCC to the institutional aid programs at the UC and the CSU (the UC Grant and the State University Grant). As a result, there is no vehicle for CCC students to receive campus aid awards to fill the unmet need after other sources of aid have been exhausted. The State University Grant at the CSU, for example, can be used to assist those who do not qualify for a Cal Grant due to the GPA requirement, family

income criteria, and/or age limitation. Except for small programs targeted to specific groups (like the EOPS categorical program), community college students receive no institutional assistance in covering these additional expenses because their institutional aid is limited to the fee waiver.

- There appears to be a bias in the financial aid process against advising CCC students to apply for federal loans. Although 50 percent of student aid *statewide* is in the form of federal loans, such loans accounted for only 11 percent of the total aid awarded to CCC students in 2005-06. Whereas more than one-fourth of all students receive fee waivers, fewer than six percent of students receive federal loans.⁹²
- Fee and aid policies are not designed to take advantage of available federal aid. Tax credits, Pell Grants, and loans that would be available to CCC students and families are left unused.

Incentives

As noted above, current policies contain disincentives for students to apply for all of the financial aid for which they may qualify. This causes students to work more than necessary and take fewer classes, lowering their chances of completion.⁹³ As one indication that CCC students do not maximize their aid opportunities, one study found that California had the second lowest percentage of its public community college students receiving Pell Grants – a percentage that was just over half the national average.⁹⁴

Institutions have a disincentive to encourage students to take out loans since institutional penalties for excessive default rates are serious. Since a student who completes a FAFSA becomes eligible for federal loans, institutions have a disincentive as well to encourage students to complete the FAFSA. Failure to complete a FAFSA severely limits student access to available aid. The risk of default could be lessened if the CCC had a more comprehensive policy addressing college affordability and if finance policies were more supportive of completion so that default rates would be lower.

Does policy focus on fees reinforce state priorities?

Access	-	Impedes access because students do not maximize available financial aid
Affordability	-	State aid has not kept up with costs and policies do not facilitate students taking full advantage of available aid
Completion	-	Students encouraged, by lack of integrated aid, to work more and/or stop out of college, lowering chances of completion
Efficiency	-	Efficiency hampered by lack of policy integration; state funds are used for costs that the federal government would cover

III. Summary and Conclusions

"We must move out of the policy boxes that have guided our activities in the past and move forward with new approaches....We can continue to watch the economic divide grow within our country....or we can change our education policies...."

David Longanecker, *Thinking Outside the Box*, WICHE, 2007

"States and their colleges and universities must together align the mission of postsecondary education systems with the economic needs of the regions and states where they are located."

A Compact for Postsecondary Education, National Governors' Association

"It will require prioritizing higher education on the legislative agenda, approaching fiscal and policy decisions in a different way and exerting strong leadership."

Transforming Higher Education, National Conference of State Legislatures

Having analyzed the policies that govern the flow of resources to and within the community college system, we return to the criteria for effective higher education finance policy:⁹⁵

- Policies should reinforce state priorities.
- The institutional capacity necessary to meet the stated priorities must be created and sustained.
- The contributions required of students and taxpayers should be affordable.

Our analysis indicates that, according to these three criteria, California's finance policies for its community colleges are not as effective as they need to be.

Policies Undermine State Priorities

In the absence of an official set of priorities for higher education, our analysis used the priorities that are included in pending legislation, SB 325

(Scott). These priorities capture the growing sentiment across the state and within the CCC system that educational attainment in the state, fueled by community college student success, must be increased. It is important not to wait for the legislation to be enacted to begin considering how policies can better align with these priorities, about which there appears to be little disagreement. Calling attention to the benefits of aligning policies with state priorities may have the additional advantage of drawing attention of lawmakers to the need to enact formal goals. As Jones cautions, "in states where the objectives are not clear, institutions have the luxury of establishing their own priorities, the sum of which are not necessarily in line with state needs."⁹⁶

Table 3 summarizes the analysis of incentives contained in the policies with respect to the six priorities. It is an aggregate summary of many policies, the nuances of which are discussed in Section II. The summary table cannot convey the relative magnitude of the incentives. Simply adding up the plusses and minuses does not give

Table 3
Summary of Policy Alignment with State Goals

	Readiness	Access	Affordability	Completion	Workforce	Efficiency
Proposition 98	-	-		-	-	-
Apportionments	-	+/-		-	+/-	-
Growth	-	+/-		-	-	-
Categoricals:						
Matriculation	-	+/-	-	-	-	-
EOPS		+	+	+	+	-
DSPS		+		-		-
Part-time Faculty		+/-		-		-
Financial Aid Administration		+	+	-		+/-
Expenditure restrictions:						
50% instruction	-	+/-		-	-	-
75% / 25%		-		+/-	-	-
60% part time		-		-	-	-
2 semester temporary		-		-	-	-
Student employment			-	-		-
Fees:						
Lack of policy		-	-	-		
Low fees		+/-	+/-	-	-	-
Waivers		+	+/-	-	-	-
Revenue offset		-		-	-	-
No fee non-credit	+	+/-	+	+/-	+	-
Prohibit campus fees	-	-		-		-
Financial Aid:						
BOG waivers	-	+/-	+/-	-	+/-	-
Cal Grant	+/-	+/-	+/-	+	+/-	+/-
Focus on fees		-	-	-		-

Key: + indicates that the policy promotes the priority
 - indicates that the policy fails to promote, or works at cross purposes to, the priority

an accurate sense of the effect of the policies, since some affect a much greater portion of a college's budget or a student's experience. But the table does reveal a substantial misalignment between policies and state priorities. The greatest alignment is with the priority of access but even there, policies do little to encourage access by the growing numbers of under-served Californians – precisely those individuals whose education is most likely to stem the decline in educational attainment and workforce quality.

The analysis of policy alignment, summarized in Table 3, is predicated on the proposition that people, both individually and as institutional representatives, respond to incentives.⁹⁷ It is important to reiterate that an assertion that faculty, staff, and students respond to fiscal incentives entails no judgments about individuals' values. When enrollment-driven funding leads colleges to allow late registration beyond the point they know is good for student success, it is not because colleges care little about student success. They are playing by the rules of the game that have been established for them as they strive for financial survival. When academic leaders fail to expand nursing programs, it is not because they wish poor health care on Californians – it's because they face pressures to make their dollars stretch as far as possible. When students sign up for more classes than they know they can complete and drop most of them after the census date, it is not because they want to prevent other students from finding a seat in those classes – it's because it seemed like a reasonable thing to do since there are no financial consequences for dropping courses. And if a student continues for several terms without seeing a counselor and makes no forward progress toward her goals, it is not because she doesn't care about her future but likely because the wait to see a counselor is too long, and there is no need to make forward academic progress in order to renew her fee waiver.

One possible reason for the misalignment between policies and priorities is the uncoordinated process by which finance policy is made. In the community colleges, not only is there the typical fragmentation of policymaking attention to the major elements of finance (appropriations, fees, financial aid) but there is the fragmentation brought about by the many categorical programs. With separate funding decisions for each categorical program, there is

little opportunity for lawmakers to see the big picture. Nor is there reason for colleges to take a comprehensive look at available resources with respect to college priorities – since important pieces of their funding come not as general purpose funding but with conditions and constraints.

The focus of policy development is often on the equity of the allocations across the 72 districts. It is a focus on inputs – not on outcomes, on fairness to institutions – not on equitable distribution of educational opportunities among Californians. Certainly the effort to distribute resources fairly across districts is ultimately about fair distribution of educational opportunity, but the institutional interests become paramount. Great care is given to devising apportionment formulas, equalization methodology, categorical formulas, and other regulatory provisions such that no district feels unduly disadvantaged by being urban or rural, large or small, wealthy or poor, multi-campus or single-campus, or by other characteristics.

Perhaps because there are no official state priorities to provide a framework for policy discussions, policy negotiations tend to be about winners and losers among districts. This approach is a rational way for districts to protect their shares of a scarce resource but it does little to focus on the needs of students and the state. The institution-centered approach does not lend itself to addressing, through resource allocation, discrepancies across the state in educational attainment or widely varying regional growth patterns. The focus on inputs has also led to heavy reliance on surrogates for quality, such as the 50 percent law and the 75/25 ratio, that drive use of resources independent of the needs of specific student populations, the state, or the local communities.

Policies Do Not Provide Colleges the Means to Fulfill their Missions

The California Community Colleges have been assigned tremendous responsibility under the Master Plan, in terms of the proportion of students served and the multiple missions they are to fulfill. There is a serious misconception, not only in California, that because community colleges are teaching institutions without the research and professional school missions of universities, they can provide quality

education at a fraction of the cost of universities. This misconception is particularly evident in the remedial function that is increasingly falling to community colleges to fulfill. Disadvantaged and under-prepared students require many more services, and more intensive and even intrusive services, if they are to have much chance of success. These are costly services to deliver. Yet across the country community colleges receive substantially less funding per student than do four-year institutions.

Experts have warned of the dangers of ignoring resource issues when developing policies to promote college access. As Jones states, “policies that make it economically possible for students to attend college are of little use if the institutions do not have the capacity to accommodate them.”⁹⁸ Our review of finance policies has revealed a very strong emphasis on policies that stimulate enrollment – e.g., low fees, readily available fee waivers, enrollment-based apportionments, college allocations biased toward growth, and categorical funds based on enrollment instead of services provided. But there has not been equivalent policy focus on getting the CCC system the resources it needs to serve these large numbers of students effectively. The bulk of the funding is determined more by K-12 enrollments than by community college enrollment demand and total funding is artificially capped by formula. State funds that could enhance college programs and services instead are used to pay student aid costs that the federal government would pay if fee and aid policies were designed to coordinate better with federal policy. And there has been no serious policy attention devoted to understanding what a fair share contribution to college resources *by non-needy students* might be. Fees continue to be seen only as barriers to access – not as a source of much-needed revenue for the system.

Ensuring that the colleges have the needed capacity to fulfill their mission goes beyond funding levels. It includes the flexibility to use resources – whatever their level – most effectively. It requires policies that do not work at cross purposes to system and state priorities, contrary to what is revealed in Table 3.

Additionally, *capacity* requires that colleges have the *decision-making authority* to direct resources to where they are most needed. The California Community Colleges are heavily

regulated, with regulations imposed by the Legislature, the system’s Board of Governors, and local boards. The policies discussed above constitute only a sample of the provisions in law and regulation that govern the use of resources across the system. Hundreds of pages of Education Code, Title 5 regulations, and system office implementing guidelines make it nearly impossible for even the most diligent college official to understand fully how funds are to be used. The 2007-08 Budget Act contains a schedule of twenty-three specified appropriations for discrete purposes along with twenty-seven items of complex budget instructions that further control the uses of funds.

The tendency to regulate comes from within the system as well as from outside. Community college representatives speak often of the uniqueness of each college as the rationale for local governance and locally-driven policies and practices. Yet internal stakeholders advocate for the many categorical programs that include countless *standardized* mandates on colleges, regardless of local circumstances. The unwillingness to give colleges more authority to use their resources reflects ambivalence about local control. The distinctiveness of districts prevails, for example, when it comes to decisions about what courses to offer, but not when it comes to the faculty who offer the courses.

The upshot of the ambivalence is a profusion of regulations that impose mandates while acknowledging vast complexities in the environment in which the mandates are implemented. Acknowledging the complexities typically calls for measures like maintenance of effort or matching requirements, waivers, and claims submission, and almost always for compliance monitoring by the Chancellor’s Office. Demands for compliance monitoring often exceed what Chancellor’s Office staffing levels can accommodate, resulting in a plethora of un-enforced laws and diminished system influence over local practice. For their part, districts are often unable to meet the strict requirements of the law, due to local circumstances, and they confront large administrative costs to comply with reporting and other requirements.

The situation warrants review, as it seems to provide neither the local authority to use college resources to best meet local needs nor the Board of Governors’ authority to steer the system toward meeting the needs of the state. Where

local discretion in the use of funds is appropriate, college officials should have more authority to make resource allocation decisions. Where state priorities take precedence, an alternative policy framework should be developed that is based on outcomes and incentives – rather than inputs, regulation, compliance, and auditing.

Affordability Policy is Needed

The lack of an affordability policy may be the best example of how policy making across the realms of appropriations, tuition, and financial aid is not well-coordinated. The lack of coordination has important consequences with respect to a critical state need: ensuring affordable access to quality education for growing numbers of Californians. In the CCC, the long-standing assumption has been that as long as fees are kept low and the BOG fee waiver is available, community college will be an affordable option for most Californians. Lawmakers need to address affordability in a comprehensive manner that includes (1) addressing the full costs of college attendance, (2) taking full advantage of federal aid grant and loan programs, (3) maintaining the purchasing power of Cal Grant access grants, (4) establishing an institutional aid program in the CCC similar to the State University Grant Program and the University of California Grant Program, and (5) considering whether increasing fees for non-needy students could *increase* student access and success by augmenting state appropriations with much needed revenues.

A recent report has documented that affordability is a serious problem in the CCC. More importantly, it concludes that the affordability problem has little to do with fees.⁹⁹ The most telling evidence of the affordability problem offered in the report is that community college students in California have more unmet need *after* financial aid is accounted for than do community college students in other states. The report shows that a smaller proportion of CCC students receive federal and state aid than do students in other states and that a larger portion of them work close to full time. The report recommends a number of enhancements to the Cal Grant program and moderate fee increases matched by increased state funding to augment the resources available to help students succeed.

Jones' affordability criterion calls for contributions that are

affordable to *students and to taxpayers*. What taxpayers can afford is not something that we can know – as it involves values about the role and size of government. What we can say is that California taxpayers have been making it clear for many years that they do not support tax increases. In such a tax-limited environment, it seems important to question whether some portion of the community college student body could afford to pay higher fees. *Needy students do not pay fees*, so by definition, fee increases would be borne by non-needy students.

In a 2004 report laying out its strong support for having no fees at the CCC, the Academic Senate of the California Community Colleges decries the “shift in political priorities” that has led to the imposition of fees at the CCC and the raising of fees at UC and CSU. The Senate opposes these policy choices and argues, with respect to full taxpayer support for community college education: “It’s not that the state can’t afford it; it’s that voters or policy makers have apparently made other choices, either explicitly or implicitly, by overt action or by passive complicity.”¹⁰⁰ These choices, however, reflect other implications of the same demographic changes that have shaped today’s community college. The growing numbers of immigrants, and of low-income, disadvantaged populations, require increased taxpayer support not only for education but for a whole array of health and social services. In view of these competing priorities for state funding, it may be that what the Senate calls a “principled” stance in favor of no fees can be maintained only at the expense of continued inadequate funding for the community colleges to serve students.

It is important to remember that not all community college students are low-income. By design, a full two-thirds of California high school graduates are ineligible for direct enrollment in UC or CSU and are directed to community colleges if they attend in-state public institutions. Many students in the top one-third of their high school class choose to attend a community college for reasons of convenience and access to quality teachers and programs. As shown in Table 4, the median household income of dependent CCC students is virtually equal to that of all California households. There are certainly many CCC students who would not be financially disadvantaged by a modest increase in fees.

Table 4
Median Household Income, 2002

All California residents¹	\$49,738
CCC Dependent students²	\$49,805
CCC Independent students²	\$29,013

¹ American Community Survey, 2002

² National Postsecondary Student Aid Survey (NPSAS:04) as reported by Zumeta & Frankle (2007). NPSAS:04 income data represents income for 2002. Students under 24 years of age are generally considered dependent unless both parents are deceased, they are married, have dependents of their own, or have veteran status.

Additionally, many students attend community college for personal enrichment. These students tend to be white, older, and to already hold college degrees¹⁰¹ – most likely able to pay more than \$20 per unit. By asking taxpayers to foot most of the bill for students who are not seeking a credential and for many students who are willing and able to pay more for the courses they value, the state loses the opportunity to invest more in students whose educational attainment is vital to the state's future. Providing free or near-free lifelong learning is an admirable goal of any society, but likely an untenable one in a society that values low taxes as much as ours does. In such a world, it is incumbent upon policy makers to use limited public dollars to maximize public value – which requires that individuals who lack the educational credentials they need for economic security are able to attend colleges that have enough resources to help students succeed.

Enrollment-driven finance policy is the principal reason why California is not able to engage in conversations about affordability, fees, and the implications for college revenues. History has shown that enrollment tends to vary inversely with fee levels. Colleges resist fee increases because they fear losing FTES. But an analysis by the Chancellor's Office showed that the enrollment drop that followed the recent fee increase was more concentrated among older, part-time students with stated goals other than earning a college credential, and that there was no disproportionate impact on

the overall racial or income distribution of the student body.¹⁰² It would be useful to discuss whether the loss of some older, part-time students who are enrolled for reasons other than seeking credentials might be a price the state is willing to pay for having more fee revenue to support students who are pursuing their first postsecondary credentials. However, these conversations are precluded by colleges' overriding interest in keeping any and all students in order to meet enrollment caps and preserve funding.

This is a time when the state needs college-going to increase – not decrease. The Academic Senate and the many others who oppose fee increases express genuine concerns that any fee increase will reduce access among the at-risk and poor students who depend on the community colleges for a secure future. The dire need for improved access *and success* by this population makes it incumbent upon those who have engaged for years in the same conversation about fees and access to *change the conversation*. No one who cares about the economic and civic health of the state wants to deprive needy Californians of an education. *The question is whether access for those individuals can be protected in such a way that does not deprive the institution of needed resources.*

It might be that keeping fees low for everyone – non-needy included – is not the most effective way to provide *meaningful* access – that is, access to a college with resources to help students succeed. But with FTES driving budgets, these conversations never occur because any drop in enrollment, regardless of who is affected, depresses revenues. It is time to take a fresh look at the relationship among fees, financial aid, state support and access to see if there are options other than waiting for taxpayers' and lawmakers' priorities to change.

IV. Directions for Future Reform

“Rather than add on a new layer of requirements sometimes you need to start by scraping the barnacles off the bottom of the boat.”

Dennis Jones, NCHEMS President

“An incentive is simply a means of urging people to do more of a good thing and less of a bad thing.”

Freakonomics, Steven Levitt and Stephen Dubner

Across the nation, policies are not conforming to the growing rhetoric about the need to improve student success in order to produce a competitive workforce for today’s global economy.¹⁰³ This research shows that California is no different. The CCC has committed itself in rhetoric and in action to increasing student success, but the state and system policies that govern the flow of funds throughout the system are not well aligned with that commitment. With policies working at cross purposes, the system’s best efforts will be hard-pressed to produce the hoped-for results. The system may have the will but lacks the resources, the enabling policy environment, and the control over its own resource decisions to most effectively meet the needs of students and Californians.

The ineffectiveness of funding mechanisms for the CCC has been a recurring issue for the Legislature and the state. Various groups have examined the funding structure within the past few years to determine potential revisions and methods for improvement.

In 2003, the chair of the Assembly Committee on Higher Education convened a working group to review the community college funding mechanism. The group agreed on the need for simplification of the funding mechanism and for state funding incentives that contribute to

a focused CCC mission and that link funding to the attainment of state priorities, consistent with that mission. It identified a number of weaknesses in the funding mechanism, including:¹⁰⁴

- Funds are not allocated to CCC districts with sufficient sensitivity to the real costs of providing instructional services.
- Extensive bureaucratic restrictions are placed on the expenditures of funds.
- Unjustifiable differences exist in revenues among the CCC districts.
- Local districts have limited flexibility to raise additional revenue.
- The student fee revenue serves as an offset to General Fund apportionment funding rather than as an enhancement.
- The state-level statutory mission of the CCC is so broad that the institutions, by necessity, are under-funded.

The committee specified that a comprehensive reform effort should address all of these issues by clarifying state priorities, eliminating “inefficient and excessive” statutory provisions, developing a fee policy and a means of funding colleges that is more reflective of actual costs.¹⁰⁵

The Community College League of California subsequently recommended a new funding approach based on the results of a year-long effort by a systemwide workgroup of business officers. (The League's work was focused on cost and equity issues and did not address the full list of issues considered by the Assembly Committee.) The Board of Governors adopted the recommendations in March 2005, many of which were enacted through SB 361 in 2006. The reform was celebrated by many within the system as the culmination of a three-year, hard-fought battle that ultimately yielded consensus around a simplified, more equitable funding structure. Reaching consensus across such a diverse system of local districts, each with multiple stakeholders, was indeed a major accomplishment. Yet equity of funding across districts – the focus of SB 361 – is just one of several concerns about community college finance policies. This change may have opened the door for further reforms that can address a broader set of issues within the context of state priorities.

National Reform Efforts

Inspired by concerns about declining economic prospects, many states are exploring or implementing new approaches to finance policy to help them accomplish their priorities. In many cases these new directions recognize the power of financial incentives to change behaviors and involve the targeted use of funds to encourage the desired outcomes. There are also instructive examples from other countries, some of which have moved even further in introducing incentives into funding approaches. Additional reform ideas are being advanced in the policy research literature.

Nearly ten years ago in a research paper prepared for the World Bank, D. Bruce Johnstone suggested that real finance reforms in higher education would involve accepting that:¹⁰⁶

- individuals at all levels of the higher education enterprise are “rational actors” who respond to incentives
- the rules of the game for the receipt of public revenues constitute a powerful system of incentives with different impacts upon different players
- the difficult academic and resource allocation decisions at the institutional level are facilitated by government

budget rules that are “sensible, fair, transparent, and stable.”

The flurry of activity around the country indicates that true reforms are underway. The following summary of some of these reforms is intended to encourage conversations in California about how we can harness the power of incentives within the design of fair and sensible budgeting systems that can help college faculty and staff make the difficult resource decisions that face them.

We have categorized these ideas by (1) whether they aim to influence the behavior of colleges or students and (2) which of the six priorities they address. Some of the reform ideas address multiple priorities (e.g., completion and workforce) but we list each idea only once. A fuller explanation of the reforms and where they are being considered or adopted is outside the scope of this study but will be the subject of future research by our Institute.

Incentives for Colleges

Readiness

- Colleges and high schools both receive enrollment funding for high school students who enroll in community college classes (called “dual enrollment”) in order to encourage K-14 cooperation and eliminate any disincentives for either institution to support these programs.
- States provide financial incentives for K-14 cooperative efforts to improve alignment of curriculum and assessments.

Access

- Colleges receive a richer per-student funding rate for those students who come from disadvantaged backgrounds (however defined).

Affordability

- Colleges receive higher funding per student for Pell Grant recipients.
- Colleges receive funding for every student who completes a FAFSA.

Completion

- In addition to receiving funds for FTES, colleges receive a portion of their base funding for the number of students who have reached certain benchmarks. Care is taken not to disadvantage colleges that serve under-prepared students.
- Colleges receive a portion of their funds based on the share of eligible students who apply for and receive various forms of financial aid.
- Colleges receive financial incentives for partnering with four-year institutions to make upper-division coursework available on community college campuses.
- Funding formulas provide higher per-student funding for remedial classes to recognize high costs and ensure adequate supply of seats.

Workforce

- Colleges receive special funding to provide hiring bonuses for faculty in high-need but hard-to-fill positions, like nursing.
- Colleges receive more funds per FTES for *high-cost* programs.
- College receive higher per-student funding for enrollment in *high-need* programs. This has the added advantage of encouraging colleges to help students declare a program goal.
- Colleges receive a portion of their funding based on the number of students who complete a workforce program and transition into high wage employment.

Efficiency

- Colleges receive some funding based on the portion of first-time students who are enrolled in a specific degree/certificate program and have an approved academic plan laid out for meeting that goal.
- Colleges are granted increased flexibility to use their resources in exchange for budgets that are allocated in part based on performance.

- Tuition rates are set in recognition of federal aid and tax policy to maximize the use of federal dollars.

Incentives for Students

Readiness

- Students receive scholarships or other forms of financial reward for completing a rigorous high school curriculum with specified grade point average.
- Minimum financial aid eligibility requirements are established that incorporate college readiness factors, like high school curriculum and GPA.
- Students in high school take community college classes without paying tuition.
- Students pay a surcharge for exceeding an established level of remedial units.

Access

- Financial aid awards are inclusive of the major costs facing part-time students, such as child care and transportation.
- Tuition and financial aid policies are designed and targeted to have the maximum impact on access by those students who would not otherwise attend college.

Affordability

- Financial aid policies are coordinated with federal aid availability so that students have an incentive to increase their course units. Increased federal aid compensates for loss of income from fewer hours worked.
- Students who complete a transfer program and earn an associates degree in the process can continue to pay community college tuition rate (or reduced university tuition) upon transfer to a four-year institution.
- Students attend tuition free and pay back based on future earnings.

- States implement a “share of cost” fee policy under which student tuition revenue accounts for a fixed percentage of the cost of instruction. This creates an incentive for students to keep colleges accountable for controlling costs.
- More work-study and other on-campus jobs are provided. This has benefits for completion as well as affordability.
- Financial aid awards increase if students perform well academically.

Completion

- The per-unit tuition is reduced as a student’s unit load increases, encouraging students to attend on a more full-time basis.
- Financial aid programs provide incentives for students to enroll full-time and continuously – as both are strong correlates of completion.
- Conditions for renewing financial aid include making forward academic progress with some established timelines.
- Aid amounts are tiered, with higher awards for higher academic performance – among needy students.
- Students pay a penalty for dropping courses.
- Students must meet requirements of satisfactory academic progress to have financial aid (including waivers) renewed.
- Students receive a bonus payment for completing an academic program.
- High-risk students receive a bonus payment for completing particular courses or groups of courses.
- Students are required to pay back financial aid if they do not complete their program in a specified time period or do not attend continuously.

Workforce

- Students who enroll in and complete high need programs receive scholarships, tuition rebates or loan

forgiveness above their regular financial aid eligibility.

Efficiency

- Students who complete certificates or degrees or become transfer ready within a specified period receive tuition rebates, loan forgiveness, or other forms of financial reward.
- Students who take more than a certain number of units in total are assessed a tuition surcharge to encourage better planning and make existing resources and facilities available to serve more incoming students.

Investing in Success

The above listing gives a flavor of the many directions that reform is taking. The examples are all ways in which incentives might be used as purposeful policy instruments to achieve specific positive outcomes. This concept of investing in success applies to all aspects of finance policy – not only to the basis on which funds are allocated to colleges. The list shows, for example, that the concept applies to eligibility requirements for financial aid, fee policy, flexibility in the use of resources, differential funding for higher cost programs and services, faculty salaries, and state incentives for collaborative efforts between colleges and high schools. A variety of strategies along these lines might be used to influence student outcomes. They are not typically thought of in the context of finance policy reform, but they should be.

Turning to policies that affect basic college allocations, it is these policies where the incentives are most powerful because they affect the distribution of core funding. If Californians are to invest wisely in the success of community college students, it is vital that funding mechanisms be structured to include incentives for achieving positive outcomes. The question, which continues to perplex American higher education, is *how best to incorporate measures of success into funding decisions*.

Success is Not an “Add-on” Responsibility

In addressing this question, it is critical to distinguish *investing in success* from performance funding, which has largely been a failure across American higher education and has a deservedly bad reputation among educators. The

fundamental difference between the two is that investing in success acknowledges that improving performance is an ongoing and costly undertaking and should be *institutionalized* into the basic funding formula so as to provide a stable and significant funding source, while performance funding places the burden of improving performance on a very small pool of funds that is not guaranteed to last (and usually doesn't).

In short, investing in success changes the incentives built into core funding while performance funding leaves the current incentives in place and sets up a small categorical program to fund performance. Funds earned under an investing in success model automatically are part of a college's base funding, while funds earned under traditional performance budgeting approaches are bonuses that may or may not last.

Performance funding has been implemented amid great controversy and with little success in a number of states.¹⁰⁷ The antipathy is not surprising *because the conventional wisdom behind the adoption of these plans is misguided.*

The current paradigm for performance funding is as follows: (1) set aside a small pot of money (2-5 percent) – ideally new funds; (2) select the dimensions of performance to be rewarded and corresponding performance indicators, (3) set targets on each indicator for each institution based on comparisons with peer institutions or other standards; (4) allocate base funds to institutions as usual; (5) determine, at the end of the year, which colleges met/did not meet their targets; (6) award the performance funds (or assess the penalties) from the 2-5 percent performance pot.

In theory the model may be appealing, at least to lawmakers, because it seems to reward performance. In practice it is fatally flawed for several reasons:

- A performance pot of 2-5 percent is too small to make a significant difference yet it raises expectations among lawmakers, who believe they have funded performance and engage in undue monitoring of the funds.
- Performance becomes marginalized, as 95-98 percent of the budget continues to be allocated irrespective of performance.

- The performance pot becomes vulnerable to budget cuts because it is a categorical item. With the unreasonable expectation that 2-5 percent of funds can improve performance, the pot becomes an easy target for budget cutting.
- Targets are arbitrary and therefore controversial. If a college fails to meet its target, its defenders argue that the target was unreasonable; a college that makes its target may be said by others to have had an easy target.
- If performance funds are cut, as is often the case, lawmakers send the message that performance matters only when there is extra money. Colleges sour on the idea of performance funding because they believe that lawmakers haven't kept their end of the bargain.

These problems were part of the CCC experience with the Partnership for Excellence (PFE) between 1998 and 2004. The program was plagued from the start with controversy over the appropriateness of the targets, the baseline data for evaluating outcomes with respect to targets, and the mechanisms for linking rewards and sanctions to college performance. The Legislative Analyst's Office (LAO) reviewed the program in 2002 and recommended that the Legislature consider terminating the experiment, based in part on its conclusions that the performance targets were of questionable validity and that it was unclear how much of the progress toward these targets was due to the performance funds and how much to enrollment growth.¹⁰⁸ Districts faced challenges in trying to allocate PFE funds to non-recurring expenses when many felt that improving performance required increases to core allocations. The Board of Governors never identified an acceptable basis to allocate funds that took account of performance. When the program's funding was reduced and then the program eliminated, districts felt that the state had rescinded its commitment to support performance improvements.

Investing in success avoids these pitfalls by building performance-related workload factors into the core funding formula. There are no arbitrary targets, no decisions about rewards and penalties, no fruitless attempts to determine whether outcomes are the result of a performance pot, and no

danger of losing performance funds because performance is institutionalized into the annual base appropriation. Colleges get a clear message that performance is not an add-on but is an expected outcome of taxpayers' investments.

Redefining "Workload"

Performance funding models provide base funds to continue business as usual and add small performance pots as bonuses. Investing in success *re-conceptualizes the "workload"* that state funding covers through the basic allocation. Workload is currently defined as 3rd week enrollment and colleges are funded to serve it. Alternatively, workload could be defined as teaching students for a full term, serving financially disadvantaged students, guiding students through basic skills, or producing certificates and degrees. These are just a few of the possibilities for redefining workload to align funding with state priorities. If it is indeed in the state's interest that community colleges not only enroll students but educate a broad section of the California population, then the workload that the state funds should reflect these public purposes.

With workload redefined to incorporate elements of success, the state would be obligated to increase funding as success increased. Workload increases are currently funded through an annual enrollment growth adjustment. That is consistent with workload being defined as enrollment. When enrollment increases, funding must increase to keep up with the workload. If workload were redefined to include *performance-related factors*, the investment in success would increase each year that success increased. The more progress colleges made in accomplishing the new workload factors, the more growth money would be provided to ensure that college progress was not funded at the expense of other colleges. There would be an increasing pie each year from which to invest in success. This is dramatically different from the vulnerable pot of performance funds that the CCC had under PFE. The Legislative Analyst's Office has projected significant new revenues available under Proposition 98 over the next five years. But it also projects a decline in CCC enrollment.¹⁰⁹ This seems an opportune time to shift the basis for *growth* funding away from just growth in enrollment and toward *growth in success*.

A Hypothetical Example

We have constructed a hypothetical example using a ten-college system to illustrate how this model works. The

example compares allocations to these ten colleges under three different allocation methods:

- 3rd week FTES only
- 3rd week FTES plus term-end FTES
- 3rd week FTES plus term-end FTES plus FTES generated by Pell Grant recipients

These are just some of the possible factors that could be used. As discussed below, choosing which workload factors to fund would need to be the focus of thoughtful discussion across the system.

Tables 5-7 show the college allocations under each of these methods, including the workload factors from which the allocations derive. Each table shows the percentage that each college accounts for in the workload factor – labeled "College %." Funds are distributed to each college based

Table 5
1-Factor Allocation

	Census FTE	Base Allocation @ \$5000 per FTE	College %
College:			
1	5,000	\$25,000,000	5.0%
2	10,000	\$50,000,000	10.0%
3	12,000	\$60,000,000	12.0%
4	5,000	\$25,000,000	5.0%
5	9,000	\$45,000,000	9.0%
6	25,000	\$125,000,000	25.0%
7	17,000	\$85,000,000	17.0%
8	2,000	\$10,000,000	2.0%
9	5,000	\$25,000,000	5.0%
10	10,000	\$50,000,000	10.0%
Total	100,000	\$500,000,000	100.0%

Table 6
2-Factor Allocation – Adding Course Completion

	Census FTE	College %	Course Completion Rate	Term end FTE	College %	75% FTE Allocation	25% Course Completion Allocation	Total Allocation	College %
College:									
1	5,000	5.0%	93%	4,650	5.6%	\$18,750,000	\$7,016,538	\$25,766,538	5.2%
2	10,000	10.0%	89%	8,900	10.7%	\$37,500,000	\$13,429,503	\$50,929,503	10.2%
3	12,000	12.0%	85%	10,200	12.3%	\$45,000,000	\$15,391,115	\$60,391,115	12.1%
4	5,000	5.0%	84%	4,200	5.1%	\$18,750,000	\$6,337,518	\$25,087,518	5.0%
5	9,000	9.0%	83%	7,470	9.0%	\$33,750,000	\$11,271,729	\$45,021,729	9.0%
6	25,000	25.0%	82%	20,500	24.7%	\$93,750,000	\$30,933,124	\$124,683,124	24.9%
7	17,000	17.0%	81%	13,770	16.6%	\$63,750,000	\$20,778,006	\$84,528,006	16.9%
8	2,000	2.0%	80%	1,600	1.9%	\$7,500,000	\$2,414,293	\$9,914,293	2.0%
9	5,000	5.0%	79%	3,950	4.8%	\$18,750,000	\$5,960,285	\$24,710,285	4.9%
10	10,000	10.0%	76%	7,600	9.2%	\$37,500,000	\$11,467,890	\$48,967,890	9.8%
Total	100,000	100.0%	83%	82,840	100.0%	\$375,000,000	\$125,000,000	\$500,000,000	100.0%

Table 7
3-Factor Allocation – Adding Pell Grant Recipients

	Census FTE	College %	Course Completion Rate	Term end FTE	College %	Pell Grant FTE	College %	65% FTE Allocation	25% Course Completion Allocation	10% Pell Grant FTE Allocation	Total Allocation	College %
College:												
1	5,000	5.0%	93%	4,650	5.6%	750	2.4%	\$16,250,000	\$7,016,538	\$1,184,834	\$24,451,372	4.9%
2	10,000	10.0%	89%	8,900	10.7%	2,000	6.3%	\$32,500,000	\$13,429,503	\$3,159,558	\$49,089,060	9.8%
3	12,000	12.0%	85%	10,200	12.3%	4,800	15.2%	\$39,000,000	\$15,391,115	\$7,582,938	\$61,974,054	12.4%
4	5,000	5.0%	84%	4,200	5.1%	1,500	4.7%	\$16,250,000	\$6,337,518	\$2,369,668	\$24,957,186	5.0%
5	9,000	9.0%	83%	7,470	9.0%	2,970	9.4%	\$29,250,000	\$11,271,729	\$4,691,943	\$45,213,672	9.0%
6	25,000	25.0%	82%	20,500	24.7%	4,500	14.2%	\$81,250,000	\$30,933,124	\$7,109,005	\$119,292,129	23.9%
7	17,000	17.0%	81%	13,770	16.6%	11,220	35.5%	\$55,250,000	\$20,778,006	\$17,725,118	\$93,753,124	18.8%
8	2,000	2.0%	80%	1,600	1.9%	760	2.4%	\$6,500,000	\$2,414,293	\$1,200,632	\$10,114,925	2.0%
9	5,000	5.0%	79%	3,950	4.8%	1,750	5.5%	\$16,250,000	\$5,960,285	\$2,764,613	\$24,974,898	5.0%
10	10,000	10.0%	76%	7,600	9.2%	1,400	4.4%	\$32,500,000	\$11,467,890	\$2,211,690	\$46,179,580	9.2%
Total	100,000	100.0%	83%	82,840	100.0%	31,650	100.0%	\$325,000,000	\$125,000,000	\$50,000,000	\$500,000,000	100.0%

Figure 5
Comparison of Three Allocation Methods

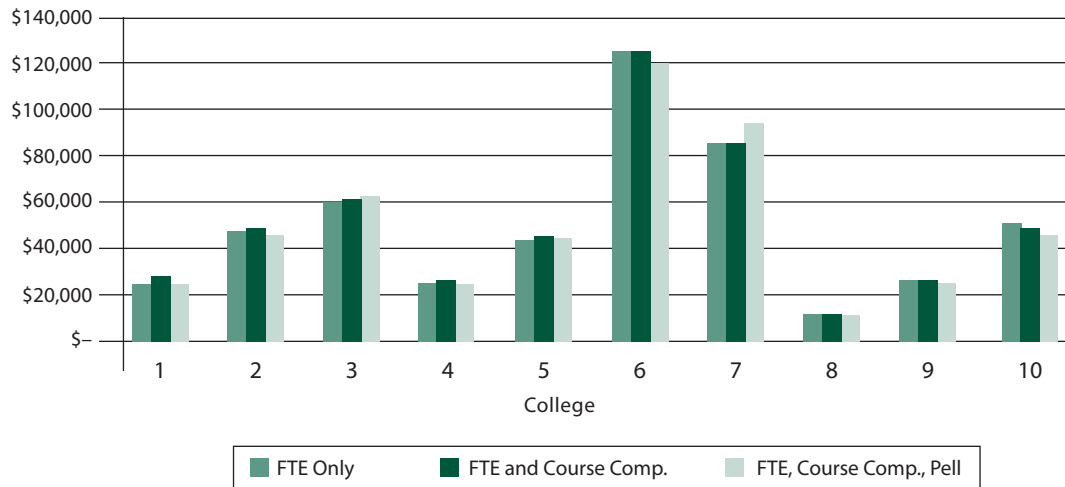


Table 8
Comparison of Three Allocation Methods

	FTE Only	FTE and Course Comp.	FTE; Course Comp; Pell FTE
College:			
1	\$25,000,000	\$25,766,538	\$24,451,372
2	\$50,000,000	\$50,929,503	\$49,089,060
3	\$60,000,000	\$60,391,115	\$61,974,054
4	\$25,000,000	\$25,087,518	\$24,957,186
5	\$45,000,000	\$45,021,729	\$45,213,672
6	\$125,000,000	\$124,683,124	\$119,292,129
7	\$85,000,000	\$84,528,006	\$93,753,124
8	\$10,000,000	\$9,914,293	\$10,114,925
9	\$25,000,000	\$24,710,285	\$24,974,898
10	\$50,000,000	\$48,967,890	\$46,179,580
Total	\$500,000,000	\$500,000,000	\$500,000,000

on those percentages. For example, in Table 5 the entire system allocation is driven by one factor – census FTES. Since College 1 has five percent of the system FTES it receives five percent of the allocation.

In Table 6 there is an additional factor. Of total system funding, 75 percent is allocated based on FTES. College 1 received its five percent share of those funds. But 25 percent of system funding is allocated based on term-end FTES. College 1 accounts for 5.6 percent of term-end FTES and therefore receives that share of the \$125 million allocated systemwide for that factor. Table 7 follows the same logic, with the addition of a third workload factor. The total system budget is now divided into three parts, with 65 percent allocated based on census FTES, 25 percent based on term-end FTES, and 10 percent based on FTES generated by Pell Grant recipients. College 1 accounts for a somewhat smaller percentage of Pell Grant FTES (4.9) so gets a slightly smaller portion of the funding that is allocated based on that factor.

Table 8 and Figure 5 summarize the dollar allocations under the three methods. Some colleges fare better than others when the additional performance-related workload factors are added. In each table the magnitude of the change in allocation for a college is strictly a result of the assumptions we made about the percentage of the total budget for the ten-college system that is allocated based on each of the workload factors. We have constructed this hypothetical example to show that changes can be significant yet need not be radical.

Tradeoffs and Challenges: Finding a Workable Approach

Designing an allocation model to invest in success is complicated and this very simplistic hypothetical illustration presents only a snapshot of one year's allocation using three factors out of any number that might be selected. There are a number of choices to make when designing such a model, including:

- Which workload factors should be included?
- What portion of the allocation should be driven by workload factors other than enrollment?

- Over what period of time should these performance-related workload factors be phased in to allow colleges time to adapt to new expectations?

In selecting the factors to include, one must be attentive to the new incentives that would be created, so as not to encourage new forms of behavior that are counterproductive to the intended results. If colleges were funded on the basis of courses completed or degrees awarded, they could be hesitant to enroll high-risk students or they could be encouraged to reduce standards. These are serious concerns but they can be addressed. For example, there could be a separate workload factor for enrolling and graduating high-risk students. Performance could be defined in terms of improvement for each college with respect to itself – not as compared to different colleges with different circumstances. Or, the formula could be designed to fund forward progress or academic momentum, regardless of where a student begins.

It should be possible, if not easy, to select factors that anticipate and minimize perverse incentives. More importantly, it is necessary to alter the current incentives in order to accomplish outcomes in the best interest of students and the state. Current policies, with incentives dominated by enrollment and the FTES chase, will not get California where it needs to be. It is important that those who are quick to point out the undesirable incentives that could arise from new funding models, if not designed carefully, also acknowledge the incentives that accompany a straight FTES model. Incentives are a fact of life – that is the main point of this report. The challenge is to get them right.

The second choice – what portion of this investment should be allocated on the basis of the carefully chosen performance-related workload factors – is also difficult. There is a strongly held assumption that any investment in success must be made only *after* core funding is provided as necessary to operate the institution. *This is the assumption that is challenged by the invest-in-success approach.* It is the assumption of the conventional approach by which only add-on funds are used to buy the desired performance. The desire for core funding is valid – institutions need a certain guarantee of stability in their funding. But it is unrealistic to pin hopes of performance gains on such a small portion

of institutional funds, as borne out by the largely failed history of performance budgeting in U.S. higher education. Furthermore, how can one distinguish between what is necessary to operate the institution and what is meant to deliver successful outcomes? Does this mean that operating without success is acceptable?

Stability is indeed important but it can be addressed within the invest-in-success paradigm. The fear of destabilizing allocations is warranted within the traditional paradigm under which funds are withheld and awarded if performance targets have been met. Clearly a state cannot withhold large portions of college funding and dole it out as rewards. However, under the invest-in-success paradigm that incorporates new factors into the base allocation, it becomes possible to expand the amount of funding oriented to performance without causing major disruptions. Figure 5 shows that even with 35 percent of the base allocation dependent upon performance-related workload factors, funding can be quite stable.

Stability would also be promoted if state lawmakers were to identify a set of long-term priorities for California higher education and orient funding toward those priorities. College officials could be assured that their efforts to respond to new priorities would be sustainable. The priorities set forth in pending legislation (SB 325) and used to guide this analysis could fulfill this need. They could become the basis for a funding approach that builds upon the gains realized in the reforms recently enacted through SB 361 but *extends* those reforms to align funding with measures of success.

The third question – how should performance factors be phased into a funding model – also addresses the need for stability. New workload factors can be phased in over whatever time period is deemed sufficient to allow colleges to adapt to new workload expectations.

Investing in success does not have to be a threat to the integrity of the community college or to the rest of the higher education enterprise, where its benefits should also be explored. Approached thoughtfully, it can be a means to support the increased performance that everyone seeks and the state badly needs. SB 361 reforms were adopted after a group of stakeholders worked through a set of difficult

issues. Similarly, a working group might be organized around the following set of principles to extend those reforms to incorporate performance into community college finance mechanisms:

1. Community colleges should receive sufficient funding from the state to provide them the resources and authority to fulfill their assigned missions
2. There must be clear priorities that define lawmakers' expectations for success
3. Funding mechanisms covering appropriations, categoricals, regulations, fees, and financial aid, should align incentives with these priorities
4. Allocation mechanisms must provide for stable and predictable funding levels based on agreed-upon workload factors that reflect desired outcomes
5. Funding mechanisms must be easy to understand so that their purposes are clear
6. Funding mechanisms must be perceived as fair, with fairness across districts achieved when districts with the same workload receive the same funding

This report aims to convince readers to look at finance policies in a new light. It is not only the amount of funding that matters but whether policies allow the system to realize the greatest benefit from available resources. An understanding of the effect of current policies and the possibilities presented by new policies could help unite community college advocates, lawmakers, and others who are dedicated to seeing that California invests in success.

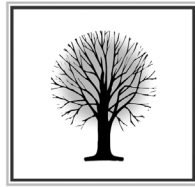
Notes

- ¹ National Conference of State Legislatures (2006). *Transforming higher education: National imperative – state responsibility*. Recommendations of the Blue Ribbon Commission on Higher Education. Washington, DC: NCSL.
- ² National Governors' Association (2007, July 10). *Innovation, education top meeting agenda for governors*. Retrieved July 23, 2007 from <http://www.nga.org/portal/site/nga>.
- ³ National Governors' Association (2007). *Innovation America: A compact for postsecondary education*. Washington, DC: NGA, p. 2.
- ⁴ NCHEMS Information Center for Higher Education Policymaking and Analysis (www.higheredinfo.org) based on data from the US Census Bureau, 2005 American Community Survey.
- ⁵ California Postsecondary Education Commission (2007). *Public higher education performance accountability framework report: Goal – contributions to economic, civic and social development: Educational attainment of population*. Sacramento, CA: CPEC.
- ⁶ Organisation for Economic Co-operation and Development (2006) as cited in Hauptman, A. M. (2007). *Strategies for improving student success in postsecondary education*. Boulder, CO: Western Interstate Commission for Higher Education, p. 3.
- ⁷ Johnson, H. P. & Reed, D. (2007, May). Can California import enough college graduates to meet workforce needs? *California Counts: Demographic Trends and Profiles*, 8(4). San Francisco: Public Policy Institute of California; Fountain, R. & Cosgrove, M. (2006). *Keeping California's edge: The growing demand for highly educated workers*. Sacramento, CA: Applied Research Center, California State University, Sacramento; Baldassare, M. & Hanak, E. (2005). *California 2025: It's your choice*. San Francisco: Public Policy Institute of California.
- ⁸ Hauptman, A. M. (2007). *Strategies for improving student success in postsecondary education*. Boulder, CO: Western Interstate Commission for Higher Education.
- ⁹ Specific references are too numerous to list, as many states have set forth goals to increase the education levels of their population in an attempt to improve their economic fortunes. The multi-state project, *Achieving the Dream*, typifies the approach, explaining that because "access alone is not enough," "*Achieving the Dream* is working to help more students earn certificates or degrees that open the door to better jobs, further education, and greater opportunity." (<http://www.achievingthedream.org/default.tp>). Similarly, the Community College Research Center at Teachers College found that "success within the community college remains an issue because many community college entrants leave higher education without a degree" (Dougherty, K. J. & Reid, M. (2007). *Fifty states of Achieving the Dream: State policies to enhance access to and success in community colleges across the United States*. New York: CCRC, p. 1).
- ¹⁰ Adelman, C. (2006). *The toolbox revisited: Paths to degree completion from high school through college*. Washington, DC: National Center for Education Statistics. (ERIC Document Reproduction No. ED490195)
- ¹¹ California Community Colleges System Strategic Plan Steering Committee (2006). *Education and the economy: Shaping California's future today*. Sacramento, CA: California Community College Chancellor's Office.
- ¹² Information on the annual conferences sponsored by the Research and Planning Group for California Community Colleges is available at www.rpggroup.org/SuccessConf-Main.htm.
- ¹³ For background information and a description of activities, see a conference presentation on the Basic Skills Initiative at http://www.ccccio.org/documents/BSICIOCSSO_000.ppt.
- ¹⁴ Jones, D. (2003a, April). Financing in sync: Aligning fiscal policy with state objectives. In *Policies in sync: Appropriations, tuition, and financial aid for higher education* (pp. 9-10). Boulder, CO: Western Interstate Commission for Higher Education. He includes two additional criteria: that all parties feel they are being treated fairly and that the funding mechanisms be transparent so that the decisions made by different parties can be mutually reinforcing. We believe these issues are addressed adequately in the three criteria that we cite above and discuss later in this report.
- ¹⁵ California State Department of Education (1960). *A master plan for higher education in California: 1960-1975*. Sacramento, CA: California State Department of Education.
- ¹⁶ Jones, D. (2003b, October). Financing in sync – policy brief. *Policy Insights*. Boulder, CO: Western Interstate Commission on Higher Education.
- ¹⁷ Hauptman, 2007, p. 20
- ¹⁸ Hayward, G. C., Jones, D. P., McGuinness, A. C., & Timar, A. (2004). *Ensuring access with quality to California's community colleges*. San Jose, CA: National Center for Public Policy and Higher Education. The study was funded by the William and Flora Hewlett Foundation.
- ¹⁹ *Ibid.*, p. 7
- ²⁰ Hauptman, 2007, p. 20. For a theoretical discussion of the role of incentives in shaping the behaviors of rational actors in higher education organizations, see Levin, H. (1991). Raising productivity in higher education. *The Journal of Higher Education*, 62(3), 241-262.
- ²¹ We recently published a policy brief that discussed the impact of some finance policies on completion rates in the CCC [see Shulock, N. & Moore, C. (2007). *Rules of the game: How state policy creates barriers to degree completion and impedes student success in the California community colleges*. Sacramento, CA: Institute for Higher Education Leadership & Policy]. This report is a more comprehensive examination of the issues of incentives embedded in finance policies and how those incentives affect outcomes in the California Community Colleges.
- ²² Levitt, S. D. & Dubner, S. J. (2005). *Freakonomics: A rogue economist explores the hidden side of everything*. New York: William Morrow.
- ²³ The Governor's veto message indicated that he vetoed it because (1) there were no specific outcomes specified for the four broad goals and (2) the entity charged with collecting and analyzing the data was proposed to be restructured in the California Performance Review. There was no indication that the Governor did not support the goals themselves.
- ²⁴ SB 1331 (Alpert) in the 2003-04 legislative session. The goals contained in the bill reflect the recommendations of an accountability workgroup formed by Senator Alpert and address educational opportunity, college participation, student success, and the social and economic benefits that accrue to the state from its investments in higher education. The veto message referred to the bill being premature in the context of other reforms to be proposed by the then-new Governor.
- ²⁵ Conley, D. T. (2005). *College knowledge: What it really takes for students to succeed and what we can do to get them ready*. San Francisco: Jossey-Bass; Kirst, M. W. and Venezia, A. (2004). *From high school to college: improving opportunities for success in postsecondary education*. San Francisco: Jossey-Bass.
- ²⁶ Zumeta, W. & Frankle, D. (2007). *California community colleges: Making them stronger and more affordable*. San Jose, CA: National Center for Public Policy and Higher Education; *How Much Does College Cost?*, accessed at <http://www.californiacolleges.edu/finance/how-much-does-college-cost.asp>

- ²⁷ *Ibid.*
- ²⁸ Moore, C. & Shulock, N. (2007). *Beyond the open door: Increasing student success in the California Community Colleges*. Sacramento, CA: Institute for Higher Education Leadership & Policy.
- ²⁹ Shulock & Moore, 2007
- ³⁰ Moore & Shulock, 2007
- ³¹ Person, A., Rosenbaum, J., & Deil-Amen, R. (2006). Student planning and information problems in different college structures. *Teachers College Record*, 108(3), 374-396; Goldrick-Rab, S. (2007). *Promoting academic momentum at community colleges: Challenges and opportunities*. New York: Columbia University, Teachers College, Community College Research Center.
- ³² Purnell, R. & Blank, S. (2004). *Support success: Services that may help low-income students succeed in community college*. New York: MDRC.
- ³³ US Census Bureau (2005). *American Community Survey*. Retrieved July 27, 2007 from http://factfinder.census.gov/servlet/DTTable?_bm=y&-context=dt&-ds_name=ACS_2005_EST_G00_&-mt_name=ACS_2005_EST_G2000_B15001&-mt_name=ACS_2005_EST_G2000_C15001&-CONTEXT=dt&-tree_id=305&-geo_id=04000US06&-search_results=01000US&-format=&-_lang=en.
- ³⁴ Hayward, et al., 2004, p. 13
- ³⁵ See http://www.cccco.edu/divisions/esed/aa_ir/noncredit.htm
- ³⁶ In recent years special grant funding has been provided for expanding high cost programs such as nursing, but these are typically competitive grants and have not affected the basic incentive of the funding formula, which discourages offerings of high cost programs.
- ³⁷ Smith, A. B., Street, M. A., & Olivarez, A. (2002). Early, regular and late registration and community college student success: A case study. *Community College Journal of Research and Practice*, 26, 261-273; Angelo, D. T. (1990). The relationship between late registration and student persistence and achievement. *College and University*, 65(4), 316-327.
- ³⁸ California Code of Regulations, Title 5, Section 55758.
- ³⁹ We discuss this in more detail in Moore & Shulock, 2007, pp. 27-30.
- ⁴⁰ Association of California Community College Administrators (2006, May). *ACCCA Reports*.
- ⁴¹ Education Code Section 76000.
- ⁴² Center for Student Success (2007). *Basic skills as a foundation for student success in California Community Colleges: Part 3 - A tool to estimate costs and downstream revenue*.
- ⁴³ See <http://www.cccco.edu/divisions/ss/matriculation/matriculation.htm>
- ⁴⁴ For a description of the process of test validation and approval, see Moore & Shulock, 2007, pp. 28-29.
- ⁴⁵ See <http://www.cccco.edu/divisions/ss/eops/eops.htm>
- ⁴⁶ See <http://www.cccco.edu/divisions/ss/disabled/dsps.htm>
- ⁴⁷ Included as "budget language" each year in the Budget Act. See Chapter 47, Statutes of 2006 (AB 1801), Item 6870-101-0001.
- ⁴⁸ California State Auditor (2000). *California community colleges: Part-time faculty are compensated less than full-time faculty for teaching activities* (Report 2000-107). Sacramento, CA: California State Auditor; California Postsecondary Education Commission (2001). *Report on part-time faculty compensation in California Community Colleges*. Sacramento, CA: CPEC.
- ⁴⁹ Memo from Frederick E. Harris, Assistant Vice Chancellor College Finance and Facilities Planning, April 5, 2007
- ⁵⁰ California State Auditor, 2000
- ⁵¹ California Community College Chancellor's Office (2003). *Preliminary report to the Legislature in response to 2003-04 Budget Act language: Information on the effect of fee increases on enrollment and a report on efforts to mitigate loss of access through improved financial aid outreach and administrative capacity*. Sacramento, CA: California Community College Chancellor's Office.
- ⁵² *Ibid.* Report describes many implementation difficulties that districts faced.
- ⁵³ Hayward et al., 2004, p. xii.
- ⁵⁴ *Ibid.*
- ⁵⁵ California Education Code section 84362(d).
- ⁵⁶ Board of Governors (2001, July 9-10). *Part-time faculty issues* (agenda item 6.3), p. 5.
- ⁵⁷ Purnell & Blank, 2004; Jenkins, D. (2006). *What community college management practices are effective in promoting student success? A study of high- and low-impact institutions*. New York: Community College Research Center, Teachers College, Columbia University; Adelman, C. (2005). *Moving into town and moving on – the community college in the lives of traditional-age students*. Washington, DC: National Center for Education Statistics. (ERIC Document Reproduction No. ED496111)
- ⁵⁸ Personal communication with Bernadine Fong, retired president of Foothill College, September 7, 2006.
- ⁵⁹ California Community College Chancellor's Office (2005a). *Workgroup on 75/25 Issues: Report and recommendations*. Sacramento, CA: California Community College Chancellor's Office, p. 7.
- ⁶⁰ Bailey, T. R., Calcagno, J. C., Jenkins, D., Kienzl, G., & Leinbach, T. (2005). *Community college student success: What institutional characteristics make a difference?* New York: Community College Research Center, Teachers College, Columbia University; Jacoby, D. (2006). Effects of part-time faculty employment on community college graduation rates. *Journal of Higher Education*, 77(6), 1081-1103; Ehrenberg, R. & Zhang, L. (2004). *Do tenured and tenure-track faculty matter?* Working Paper 10695. Cambridge, MA: National Bureau of Economic Research.
- ⁶¹ California Community College Chancellor's Office, 2005a
- ⁶² California Performance Review Commission (2004). *The public perspective: Report of the California Performance Review Commission* (recommendation ETV 27). Sacramento, CA: California Performance Review Commission.
- ⁶³ AB 1425 (Daucher), in the 2005-06 legislation session.
- ⁶⁴ Academic Senate Resolution 13.01, Fall, 2004; 75:25 Task Force Recommendations from Final Report, 6/1/05, accessed at <http://www.asccc.org/Events/Faculty/Presentations2005/FinalReccs.doc>.
- ⁶⁵ California Community College Chancellor's Office, 2005a, p. 14.
- ⁶⁶ California Education Code section 87482.5(a).
- ⁶⁷ Goldstein, M. M. (2005). *Legislative history of the "Sixty Percent Law."* Retrieved July 30, 2007 from, <http://www.cdfa.org/60history.html>.
- ⁶⁸ Education Code section 88076.
- ⁶⁹ Kuh, G. D., Kinzie, J., Schuh, J. H., Whitt, E. J. (2005). *Student success in college: Creating conditions that matter*. San Francisco: Jossey-Bass.

- ⁷⁰ California Community College Chancellor's Office (2005b). *Impacts of student fee increase and budget changes on enrollment in the California Community Colleges*. Sacramento, CA: California Community College Chancellor's Office.
- ⁷¹ *Ibid.*
- ⁷² Zumeta & Frankle, 2007
- ⁷³ The College Board (2006). *Trends in college pricing*. Washington, DC: The College Board.
- ⁷⁴ Zumeta & Frankle, 2007
- ⁷⁵ Little Hoover Commission (2000). *Open doors and open minds: Improving access and quality in California's community colleges*. Sacramento, CA: Author, p. 59.
- ⁷⁶ Analyses in Moore and Shulock (2007) show that 42 percent of those students classified as likely seeking a credential dropped more than one in five of their courses over the six-year period, after the census enrollment date.
- ⁷⁷ Murphy, P. J. (2004). *Financing California's community colleges*. San Francisco, CA: Public Policy Institute of California, p. 70.
- ⁷⁸ Shulock & Moore, 2007. Personal enrichment students were defined as non-degree seeking students for whom the majority of course enrollments were neither occupational nor remedial in nature, including classes in art, music, foreign languages, humanities, and physical education.
- ⁷⁹ California Community College Chancellor's Office (2003). *The Board of Governors' fee waiver program: Program summary*. Sacramento, CA: California Community College Chancellor's Office.
- ⁸⁰ Legislative Analyst's Office (2006). *Analysis of the 2006-07 Governor's Budget*. Sacramento, CA: Legislative Analyst's Office, p. E-222.
- ⁸¹ This assumption is reflected by the Department of Finance in the computation of state funding.
- ⁸² Legislative Analyst's Office (2006). *Analysis of the 2006-07 Governor's Budget*. Sacramento, CA: Legislative Analyst's Office, p. E-222.
- ⁸³ Based on figures from the Chancellor's Office datamart at www.cccco.edu/divisions/tris/mis/reports.htm
- ⁸⁴ California Code of Regulations, Title 5, Section 51012.
- ⁸⁵ Smith et al., 2002; Adelman, 2005; Moore & Shulock, 2007
- ⁸⁶ Zumeta & Frankle, 2007, p. 3
- ⁸⁷ *Ibid.*, p. 46
- ⁸⁸ Zumeta & Frankle, 2007
- ⁸⁹ Jones, 2003a, p. 9
- ⁹⁰ Zumeta & Frankle, 2007, p. 43
- ⁹¹ *Ibid.*
- ⁹² *Ibid.*, p. 21
- ⁹³ Adelman, 2005; Hoachlander, G., Sikora, A., Horn, L., & Carroll, C. D. (2003). *Community college students: Goals, academic preparation, and outcomes*. Washington, DC: National Center for Education Statistics.
- ⁹⁴ Romano, R. & Millard, T. (2005). *If community college students are so poor, why do only 16.9% of them receive Pell Grants?* Paper presented at the annual meeting of the Council for the Study of Community Colleges, Boston, MA.
- ⁹⁵ Jones, 2003a, pp. 9-10
- ⁹⁶ *Ibid.*, p. 9
- ⁹⁷ This is a basic tenet of social science, psychology, and economics, but for a specific application to higher education, see Levin (1991).
- ⁹⁸ Jones, 2003a, p. 10
- ⁹⁹ Zumeta & Frankle, 2007, p. vii.
- ¹⁰⁰ The Academic Senate for California Community Colleges (2004). *What's wrong with student fees? Renewing the commitment to no-fee, open access community colleges in California*, p. 35.
- ¹⁰¹ Moore & Shulock, 2007, p. 6
- ¹⁰² California Community College Chancellor's Office, 2005b. The report explained that the enrollment declines were largest in those sections taught by part-time faculty, where colleges had the most flexibility to make staffing reductions.
- ¹⁰³ Hauptman, 2007, p. 20.
- ¹⁰⁴ Assembly Committee on Higher Education (2003, December 9). *Summary of Informational Hearing: Community college funding: what revisions should be made in community college finance*. Retrieved on August 8, 2007 from http://www.assembly.ca.gov/acs/committee/c11/hearing_docs/finance_hearings/Summary%20of%20December%20%20hearing.doc.
- ¹⁰⁵ *Ibid.*, pp. 3-4.
- ¹⁰⁶ Johnstone, D. (1998). *The financing and management of higher education: A status report on worldwide reforms*. Washington, DC: The World Bank, pp. 23-24.
- ¹⁰⁷ Burke, J. C. & Minassians, H. (2003). *Performance reporting: "Real" accountability or accountability "lite."* Seventh annual survey. Albany, NY: The Nelson A. Rockefeller Institute of Government.
- ¹⁰⁸ Legislative Analyst's Office, (2002). *Analysis of the governor's budget, 2002-2003*. Sacramento, CA: Legislative Analyst's Office, pp. E241-E249.
- ¹⁰⁹ Legislative Analyst's Office (2007). *Analysis of the governor's budget, 2007-08*, Sacramento, CA: Legislative Analyst's Office, p. E49.





THE INSTITUTE FOR HIGHER EDUCATION LEADERSHIP & POLICY
thanks the following sponsor for its support of this research and report.

THE WILLIAM AND FLORA
HEWLETT
FOUNDATION

The Institute for Higher Education Leadership & Policy seeks to enhance the contribution of California higher education to the state's well-being by producing information relevant to policy makers, practitioners, and educators.



Institute for Higher Education Leadership & Policy

6000 J Street, Tahoe Hall 3063 | Sacramento, CA 95819-6081
T (916) 278-3888 | F (916) 278-3907 | www.csus.edu/ihe