

Performance Funding: Impacts, Obstacles, and Unintended Outcomes

Many states are implementing performance funding systems as a means to improve the performance and efficiency of their public higher education institutions. As legislators develop and refine performance funding policies, it is important to consider what the research tells us about the impacts of performance funding on student outcomes and institutional behavior, as well as the obstacles and unintended effects that performance-based funding programs may encounter.

Over the years, thirty-two states have implemented some form of performance funding at one or another time; Tennessee was the first to do so in 1979. This brief summarizes findings from extensive reviews of the research literature on performance funding nationwide.^{1,2}

Performance Funding 1.0 Versus 2.0

- **The early (and still present) form of performance funding is known as PF 1.0.** PF 1.0 takes the form of a bonus over and above regular state funding for higher education and is allocated on the basis of intermediate- and long-term indicators.³ Examples of such PF 1.0 programs are those established in Tennessee in 1979, Florida in 1996, and Ohio in 1995.
- **In PF 2.0 programs, performance funding is part and parcel of the regular state base funding allocation.** The new performance funding programs established in Indiana (2009), Ohio (2009), Pennsylvania (2002), and Tennessee (2010) are notable examples of PF 2.0. Typically, the new funding formulas retain enrollments as one funding driver. Tennessee, however, has completely dispensed with tying operating funding to enrollment.

Research Evidence on the Impacts of PF 1.0

These findings are derived from studies of performance funding 1.0. [Analysis of PF 2.0](#) is still in its early days.

- **Performance funding has had immediate impacts on colleges** in the form of changes in institutional finances, institutional knowledge of state priorities for higher education, and institutions' awareness of their own performance on state metrics. However, there is little evidence that performance funding brings increased state resources to improve institutions' capacity to respond to performance funding demands.⁴
- **Performance funding has led to intermediate institutional changes** in the form of changes in academic and student services policies, programs, and practices intended to improve student outcomes.
- **There is little evidence that PF 1.0 programs significantly increase rates of student retention and graduation.** Most careful quantitative analyses of the impacts of PF 1.0 on retention and graduation rates have not found statistically significant impacts.⁵ Thus far, we lack analyses of comparable methodological rigor of the impacts of large-scale PF 2.0 programs.

Research Evidence on Obstacles and Unintended Impacts of PF 1.0

- **Performance funding programs have encountered a range of obstacles**, including the use of inappropriate performance measures; lack of sufficient state funding for new institutional efforts to improve student outcomes; the brief duration of many performance funding programs; uneven knowledge about performance funding within institutions; inadequate institutional capacity for orga-

nizational learning and change; and institutional resistance to and gaming of the performance funding system.

- **Performance funding can have troublesome unintended impacts**, including grade inflation and a lowering of academic standards; restrictions on admission of less prepared and less advantaged students; unexpected costs of compliance; a narrowing of institutional missions; and a diminished faculty voice in academic governance.

Addressing Possible Obstacles

- **Improve indicators and measures so as not to disadvantage community colleges.** For instance, successful completion should be defined as including transfer to four-year colleges, and outcomes should be tracked over longer timeframes than just three years after college entrance.
- **Insulate performance funding from the state revenue cycle.** Performance funding is more stable when embedded into the base state funding formulas. Additionally, performance funding should represent a more substantial portion of base funding.
- **Help colleges improve their capacity for organizational learning.** Colleges will need funds to acquire new data management systems, hire more institutional researchers, and train faculty and research staff to analyze performance data, and they will need technical assistance to better devise solutions to performance problems.
- **Include colleges in the design of performance funding programs.** Bringing college leaders, faculty, and staff into the process of designing performance funding programs will reduce unanticipated obstacles and negative impacts and will foster more support for the programs.

Protecting Against Possible Unintended Outcomes

- **Remove disincentives to enrolling disadvantaged students** by allowing performance targets to vary based on student characteristics, by comparing colleges to peer colleges, and comparing colleges' current performance to their own past performance.⁶ States should offer direct incentives for admitting less advantaged students.^{7,8}
- **Protect academic standards** by monitoring degree requirements and course grade distribution, by taking anonymous surveys of faculty to detect whether they are under pressure to weaken requirements, and by conducting student learning assessments.

- **Combat the narrowing of education missions** by specifying indicators such as success in developmental education, general education, and continuing education.
- **Lower compliance costs** by minimizing data demands placed on colleges and relying instead on data they are already collecting.

1. Dougherty, K., & Reddy, V. (2011). *The impacts of state performance funding systems on higher education institutions: Research literature review and policy recommendations* (CCRC Working Paper No. 37). New York, NY: CCRC.
2. Dougherty, K., & Reddy, V. (Eds.). (2013). *Performance funding for higher education: What are the mechanisms? What are the impacts?* *ASHE Higher Education Report*, 39(2).
3. Burke, J. C. (Ed.). (2002). *Funding public colleges and universities for performance: Popularity, problems, and prospects*. Albany, NY: Rockefeller Institute Press.
4. Dougherty, K. J., Jones, S. M., Lahr, H., Natow, R. S., Pheatt, L., & Reddy, V. (2013). *Envisioning performance funding impacts: The espoused theories of action for state higher education performance funding in three states* (CCRC Working Paper No. 63). New York, NY: CCRC.
5. Dougherty & Reddy (2013).
6. As done in Washington State—see Shulock, N., & Jenkins, D. (2011). *Performance incentives to improve community college completion: Learning from Washington State's Student Achievement Initiative*. New York, NY: CCRC.
7. As done in Ohio and Tennessee—see Ohio Board of Regents. (2013). *State share of instruction handbook: Providing the methodology for allocating state share of instruction funds for fiscal year 2014 for use by: University regional and main campuses*. Columbus, OH: Author.
8. See also Tennessee Higher Education Commission. (2012). *2012–13 outcomes formula model*. Nashville, TN: Author.

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