

STUDY OF HIGHER EDUCATION FUNDING AND ACCOUNTABILITY - BACKGROUND MEMORANDUM

STUDY RESPONSIBILITIES

Section 23 of Senate Bill No. 2003 directs a study of higher education funding and accountability, including a review of the progress made in implementing the Higher Education Roundtable recommendations relating to the University System meeting the state's expectations and needs, the funding methodology needed to meet these expectations and needs, and the appropriate accountability and reporting system for the University System. The study is to include an independent consultant's evaluation of the roundtable recommendations and goals and objectives of the University System, the long-term financing plan for the University System, the University System's prioritization of higher education funding, including the resource allocation mechanism addressing equity funding issues, and the accountability mechanisms.

In addition, the Legislative Council has assigned the committee responsibility to receive periodic reports from the State Board of Higher Education on the status of the board's review of the long-term financing plan, pursuant to Section 17 of Senate Bill No. 2003. A copy of Sections 17 and 23 of Senate Bill No. 2003 is attached as Appendix A.

BACKGROUND

The University System consists of 11 institutions under the control of the State Board of Higher Education. The system served approximately 52,129 students (headcount enrollment) during the 2003-04 academic year. Total appropriations by the 2005 Legislative Assembly for the 2005-07 biennium for higher education institutions and the University System office totaled \$565,710,001, of which \$387,157,893 was from the general fund. This includes:

- Block grant appropriations to each of the higher education institutions for operations and capital assets and \$178,552,108 from special funds, including \$175 million for capital improvement projects.
- Funding of \$2 million from the general fund for an equity pool. Section 9 of 2005 Senate Bill No. 2003 provides that the funding must be used to address equity at higher education institutions and other campus needs as determined by the State Board of Higher Education. The board may not select a formula for distributing the equity funding until January 1, 2006. (The consultant contracted with to evaluate the higher education funding and accountability will need to consider the allocation of this equity funding in their evaluation.)

The legislative appropriations for the 11 institutions, the University System office, and the Forest Service include funding for 2,194.42 full-time equivalent (FTE) general fund positions for the 2005-07 biennium. Tuition and fees are not specifically appropriated by the Legislative Assembly as statutory authority is provided for the continuing appropriation of these funds.

PREVIOUS LEGISLATIVE HIGHER EDUCATION STUDIES AND RELATED LEGISLATION 1999-2000 Study

The Higher Education Committee during the 1999-2000 interim studied higher education funding, including the expectations of the University System in meeting the state's needs in the 21st century, the funding methodology needed to meet these expectations and needs, and the appropriate accountability and reporting system for the University System. The committee, through the use of a Higher Education Roundtable consisting of the 21 members of the Higher Education Committee and 40 representatives from the State Board of Higher Education, business and industry, higher education institutions, including tribal and private colleges, and the executive branch, discussed shifts, trends, and realities that impact the state of North Dakota and the University System and developed expectations for the University System, recommendations concerning higher education in North Dakota, and accountability measures and success indicators that correspond with the expectations for the University System. A copy of the Higher Education Roundtable recommendations concerning higher education in North Dakota is attached as Appendix B.

The committee recommended six bills for consideration by the 2001 Legislative Assembly:

1. Senate Bill No. 2037 (2001), which was amended into Senate Bill No. 2003 (2001), provided a continuing appropriation for all higher education institutions' special revenue funds, including tuition income and local funds, and allowed institutions to carry over at the end of the biennium unspent general fund appropriations. The legislation was effective through June 30, 2003.
2. Senate Bill No. 2038 (2001), which was amended into Senate Bill No. 2003 (2001), required the budget request for the University System to include budget estimates for block grants for a base funding component and for an initiative funding component and a budget

estimate for an asset funding component and the requirement that the appropriation for the University System include block grants for a base funding appropriation and for an initiative funding appropriation and an appropriation for asset funding. The legislation was effective through June 30, 2003.

3. Senate Bill No. 2039 (2001), as passed, allowed the State Board of Higher Education to authorize campus improvements and building maintenance projects that are financed by donations, gifts, grants, and bequests if the cost of the improvement or maintenance is not more than \$385,000.
4. Senate Bill No. 2040 (2001), which failed to pass, would have allowed the University System to provide bonuses, cash incentive awards, and temporary salary adjustments without reporting the activity to the Office of Management and Budget as a fiscal irregularity.
5. Senate Bill No. 2041 (2001), as passed, included the committee's recommendation to recognize the institutions under the control of the State Board of Higher Education as the North Dakota University System and to require the University System to develop a strategic plan which defines University System goals and objectives and to provide an annual performance and accountability report regarding performance and progress toward the goals and objectives.
6. Senate Bill No. 2042 (2001), as passed, included the committee's recommendation to amend and repeal statutes relating to the powers of the State Board of Higher Education and the duties and responsibilities of institutions under the control of the State Board of Higher Education which were no longer appropriate.

The committee also recommended financial and nonfinancial accountability measurements to be reported annually at the University System level.

2001-02 Study

The Higher Education Committee during the 2001-02 interim studied the State Board of Higher Education's implementation of the performance and accountability measures report. The committee, through the use of a Higher Education Roundtable consisting of the 22 members of the Higher Education Committee and 44 representatives from the State Board of Higher Education, business and industry, higher education institutions, including tribal and private colleges, and the executive branch, reviewed plans for and accomplishments relating to the recommendations of the 1999-2000 Higher Education Roundtable, reviewed the state's New Economy Initiative and its linkage to the Higher Education Roundtable cornerstones and recommendations, and

developed high-priority action items concerning higher education in North Dakota. The committee also reviewed the University System long-term financing plan and resource allocation model approved by the State Board of Higher Education and the University System first annual performance and accountability report. A copy of the Higher Education Roundtable high-priority action items concerning higher education in North Dakota is attached as Appendix C.

The committee recommended four bills for consideration by the 2003 Legislative Assembly:

1. House Bill No. 1039 (2003), which was amended into House Bill No. 1003 (2003), provided for the extension of the continuing appropriation authority for higher education institutions' special revenue funding, including tuition. The legislation was extended through June 30, 2005.
2. House Bill No. 1040 (2003), which was amended into House Bill No. 1003 (2003), provided for the extension of the University System's authority to carry over at the end of the biennium unspent general fund appropriations. The legislation was extended through June 30, 2005.
3. House Bill No. 1041 (2003), which was amended into House Bill No. 1003 (2003), continued the requirement that the budget request for the University System include budget estimates for block grants for a base funding component and for an initiative funding component and a budget estimate for an asset funding component and the requirement that the appropriation for the University System include block grants for a base funding appropriation and for an initiative funding appropriation and an appropriation for asset funding. The legislation was extended through June 30, 2005.
4. House Bill No. 1042 (2003), which failed to pass, would have amended North Dakota Century Code (NDCC) Section 15-10-14.2 to require the University System performance and accountability report to include an executive summary and specific information regarding education excellence, economic development, student access, student affordability, and financial operations. The 2003 Legislative Assembly amended House Bill No. 1003 to provide legislative intent that the University System performance and accountability report include an executive summary and specific information regarding education excellence, economic development, student access, student affordability, and financial operations.

2003-04 Study

The Higher Education Committee during the 2003-04 interim studied higher education to further

refine the expectations of the University System in meeting the state's needs in the 21st century, the funding methodology needed to meet those expectations and needs, and the accountability system and reporting methodology for the University System. The committee, through the use of a Higher Education Roundtable consisting of the 16 members of the Higher Education Committee and 45 representatives from the State Board of Higher Education, business and industry, higher education institutions, including tribal and private colleges, and the executive branch, reviewed the status of higher education in North Dakota, developed meaningful recommendations for enhancing the economy and other appropriate issues concerning higher education in North Dakota, reviewed the progress made, current status, and further actions needed to enhance the economic and social vitality of the state and make the state more attractive for new business and business expansion; reviewed the impact of the Higher Education Roundtable on higher education in the state; and developed recommendations for action by the Legislative Assembly, University System, executive branch, and private sector. The committee also reviewed the University System long-term financing plan and resource allocation model approved by the State Board of Higher Education and the University System third annual performance and accountability report. A copy of the Higher Education Roundtable recommendations for enhancing the economy and other appropriate issues concerning higher education in North Dakota and recommendations for action by the Legislative Assembly, University System, executive branch, and private sector is attached as Appendix D.

The committee recommended four bills for consideration by the 2005 Legislative Assembly:

1. Senate Bill No. 2034 (2005), as passed, provides for the continuation of the continuing appropriation authority for higher education institutions' special revenue funds, including tuition, through June 30, 2007.
2. Senate Bill No. 2035 (2005), as passed, provides for the continuation of the requirement that the budget request for the University System include budget estimates for block grants for a base funding component and for an initiative funding component and a budget estimate for an asset funding component and the requirement that the appropriation for the University System include block grants for a base funding appropriation and for an initiative funding appropriation and an appropriation for asset funding through June 30, 2007.
3. Senate Bill No. 2036 (2005), as passed, provides for the continuation of the University System's authority to carry over at the end of the biennium unspent general fund appropriations through June 30, 2007.

4. Senate Concurrent Resolution No. 4002 (2005), which failed to pass, directed the Legislative Council to study during the 2005-06 interim, the State Board of Higher Education performance and accountability measures included in the report required by NDCC Section 15-10-14.2.

Information regarding the Higher Education Roundtables convened for each of the previous studies is available on the Internet at www.ndus.nodak.edu/reports/default.asp?ID=355.

LONG-TERM FINANCING PLAN AND RESOURCE ALLOCATION MODEL

The 1999-2000 Higher Education Roundtable recommended the State Board of Higher Education and the chancellor develop a long-term financing plan and a resource allocation model. As a result, the State Board of Higher Education contracted with the National Center for Higher Education Management Systems for assistance with the development of such a plan and model. The board reviewed the recommendations of the National Center for Higher Education Management Systems and adopted a long-term financing plan consisting of base operating funding, incentive funding, and capital asset funding components.

Base Operating Funding Component

The base operating funding component of the long-term financing plan provides funding to each higher education institution to support core campus functions, such as instruction, research, and public service. The funding for each institution is based on the institution's current state general fund appropriation with general fund appropriation increases to address parity and equity. Objectives of the base operating funding component are to:

1. Establish peer comparator institutions for each higher education institution based on agreed-upon selection criteria, including institution type, city size, Carnegie classification code, land-grant institution or medical school, total FTE students, total headcount enrollment, a percentage of part-time headcount, degrees awarded, degree program mix, and research expenditures. A copy of the peer comparator institutions for each higher education institution is attached as Appendix E.
2. Review national Integrated Postsecondary Education Data Systems (IPEDS) data on unrestricted state and local appropriations and net tuition revenues (total tuition revenue less scholarships, waivers, and discounts) on a per FTE student basis for each of the peer institutions.
3. Establish a base operating funding benchmark for each higher education institution based on the review of the state and local

appropriations and net tuition revenues per student information. The benchmarks are to be reestablished every six years and, in the intervening years, are to be inflated by a percentage amount equivalent to the consumer price index. The base operating

funding benchmarks as originally established by the State Board of Higher Education, the benchmarks as reported in the 2004 annual performance and accountability report, and fiscal year 2004 state appropriations and net tuition per FTE student are:

Institution	Original Base Operating Funding Benchmark	2004 Base Operating Funding Benchmark ¹	Fiscal Year 2004 State Appropriation and Net Tuition Per FTE Student	Fiscal Year 2004 State Appropriation and Net Tuition as a Percentage of the Current Base Operating Funding Benchmark
Bismarck State College	\$7,750	\$8,790	\$6,790	77%
Dickinson State University	\$7,500	\$8,500	\$6,530	77%
Lake Region State College	\$9,250	\$10,490	\$7,350	70%
Mayville State University ²	\$9,000	\$10,200	\$9,790	96%
Minot State University	\$8,500	\$9,640	\$8,230	85%
Minot State University - Bottineau	\$9,000	\$10,200	\$7,050	69%
North Dakota State University ³	\$10,500	\$11,900	\$9,030	76%
State College of Science	\$8,500	\$9,640	\$9,280	96%
University of North Dakota ⁴	\$13,250	\$15,020	\$11,300	75%
Valley City State University ²	\$9,000	\$10,200	\$10,660	105%
Williston State College	\$7,500	\$8,500	\$7,040	83%

NOTE: The State Board of Higher Education analyzes the status of the long-term financing plan by reviewing state appropriations, current base operating funding benchmarks, current FTE enrollment, and the established shared funding percentages. Therefore, the information presented above represents a portion of the items considered in analyzing the long-term financing plan.

¹The base operating funding benchmarks were originally established by the State Board of Higher Education for 1998-99 data comparisons and have been adjusted for inflation using the annual change in the consumer price index--3.7 percent for June 2000, 3.2 percent for June 2001, 1.1 percent for June 2002, 2.1 percent for June 2003, and 1.2 percent for June 2004.

²Revenue collected from technology fees has been subtracted from tuition collections.

³Funding appropriated for the Higher Education Computer Network (HECN), agriculture extension and experiment, and flood-related expenditures has been deducted from the institution's state appropriation.

⁴Funding appropriated for the HECN, Interactive Video Network, the On-line Dakota Information Network, and flood-related expenditures has been deducted from the institution's state appropriation.

4. Establish shared funding percentages to reflect that higher education funding is to be a shared responsibility between the state and

students. The following is a comparison of the shared funding percentages established by the board and fiscal year 2004 shares:

Institution	Target Funding Shares		Fiscal Year 2004 Funding Shares	
	State Funding Responsibility	Student Funding Responsibility	State Funding Responsibility	Student Funding Responsibility
Bismarck State College	75%	25%	44%	56%
Dickinson State University	70%	30%	51%	49%
Lake Region State College	75%	25%	44%	56%
Mayville State University ¹	70%	30%	66%	34%
Minot State University	65%	35%	54%	46%
Minot State University - Bottineau	75%	25%	63%	37%
North Dakota State University ²	60%	40%	43%	57%
State College of Science	75%	25%	61%	39%
University of North Dakota ³	60%	40%	40%	60%
Valley City State University ¹	70%	30%	69%	31%
Williston State College	75%	25%	52%	48%

¹Revenue collected from technology fees has been subtracted from tuition collections.

²Funding appropriated for the Higher Education Computer Network (HECN), agriculture extension and experiment, and flood-related expenditures has been deducted from the institution's state appropriation.

³Funding appropriated for the HECN, Interactive Video Network, the On-line Dakota Information Network, and flood-related expenditures has been deducted from the institution's state appropriation.

5. Determine the recommended base operating funding levels for each institution by taking into consideration the base operating funding benchmark, enrollment, and the recommended shared funding percentages.
6. Develop budget requests to move institutions currently funded at less than 85 percent of peer institution funding to 85 percent by the 2007-09 biennium and all institutions to 95 percent of peer institution funding by the 2013-15 biennium.
7. Allocate no more than 80 percent of all new state funding to parity and inflation and no less than 20 percent of the new funds to equity. The equity funding is to be distributed on a weighted average of each institution's gap differential to its peer comparator institutions.
8. State general fund appropriations should not be reduced for any institution from the previous biennium until such time that the institution exceeds 105 percent of its peer benchmark or enrollment declines are sufficient to cause a reevaluation of its benchmark.

Incentive Funding Component

The incentive funding component of the long-term financing plan includes funding for the State Board of Higher Education to support state and system priorities consistent with the goals of the Higher Education Roundtable. The State Board of Higher Education's goal for incentive funding is to have funding equivalent to 2 percent of the total University System's state general fund appropriation by the 2007-09 biennium.

Capital Asset Funding Component

The capital asset funding component of the long-term financing plan provides funding to each of the higher education institutions for maintenance and replacement of facilities and infrastructure. The State Board of Higher Education's goal for capital asset funding is for each of the institutions to phase in full funding of the Office of Management and Budget's buildings and infrastructure formula over a 10-year period (by the 2011-13 biennium) and to address the current deferred maintenance backlog over approximately a 14-year period (by the 2015-17 biennium). The funding provided to each of the institutions would be left to the discretion of the institution with appropriate approvals by the State Board of Higher Education for projects greater than \$100,000. Institutions would be given the authority to allocate dollars for repair and replacement priorities for both deferred maintenance and regular repair and replacement projects as determined by the institution. Institutions would be allocated to carry over unspent capital asset funding from one biennium to the next in order to complete projects started in one biennium but not completed until the next and to accumulate funds to

complete large projects that require multiyear funding. The capital asset funding component will be applied to new state buildings built on campuses; however, no new operating funds will be added to the base operating budget for operating costs if the operating base is already at the benchmark target.

PERFORMANCE AND ACCOUNTABILITY REPORT

North Dakota Century Code Section 15-10-14.2 requires the University System to provide an annual performance and accountability report regarding performance and progress toward the goals outlined in the University System strategic plan and related accountability measures. Section 20 of 2005 Senate Bill No. 2003 provides that the performance and accountability report as required by Section 15-10-14.2 is to include an executive summary and identify progress on specific performance and accountability measures in the areas of education excellence, economic development, student access, student affordability, and financial operations. The following is a summary of the performance and accountability measures identified in Section 20 of 2005 Senate Bill No. 2003:

1. Education excellence, including:
 - a. Student performance on nationally recognized exams in their major fields compared to the national averages.
 - b. First-time licensure pass rates compared to other states.
 - c. Alumni-reported and student-reported satisfaction with preparation in selected major, acquisition of specific skills, and technology knowledge and abilities.
 - d. Employer-reported satisfaction with preparation of recently hired graduates.
 - e. Biennial report on employee satisfaction relating to the University System and local institutions.
 - f. Student graduation and retention rates.
2. Economic development, including:
 - a. Enrollment in entrepreneurship courses and the number of graduates of entrepreneurship programs.
 - b. Percentage of University System graduates obtaining employment appropriate to their education in the state.
 - c. Number of businesses and employees in the region receiving training.
3. Student access, including number and proportion of enrollments in courses offered by nontraditional methods.
4. Student affordability, including:
 - a. Tuition and fees on a per student basis compared to the regional average.
 - b. Tuition and fees as a percentage of median North Dakota household income.

- c. Cost per student in terms of general fund appropriations and total University System funding.
 - d. Per capita general fund appropriations for higher education.
 - e. State general fund appropriation levels for University System institutions compared to peer institutions general fund appropriation levels.
5. Financial operations, including:
- a. Cost per student and percentage distribution by major function.
 - b. Ratio measuring the funding derived from operating and contributed income compared to total University System funding.
 - c. Ratio measuring the amount of expendable net assets as compared to the amount of long-term debt.
 - d. Research expenditures in proportion to the amount of revenue generated by research activity and funding received for research activity.
 - e. Ratio measuring the amount of expendable fund balances divided by total expenditures and mandatory transfers.
 - f. Ratio measuring net total revenues divided by total current revenues.

The State Board of Higher Education has adopted 9 performance and accountability measures, in addition to the 21 measures required by the 2005 Legislative Assembly, that are to provide guidance in establishing effective policy for the 11 system institutions. The following is a summary of the performance and accountability measures adopted by the State Board of Higher Education:

- 1. Workforce training information, including levels of satisfaction with training events as reflected in information systematically gathered from employers and employees receiving training.
- 2. Noncompleters satisfaction - Levels of satisfaction and reasons for noncompletion as reflected in a survey of individuals who have not completed their program or degree.
- 3. Student goals - Levels and trends in the number of students achieving goals and the institution meeting the defined needs and goals as expressed by students.
- 4. Levels of satisfaction with responsiveness, as reflected through responses to evaluations of companies receiving training.
- 5. Student participation - Levels and trends in rates of participation of:
 - a. Recent high school graduates and nontraditional students.
 - b. Individuals pursuing graduate degrees.
- 6. Student enrollment information, including:
 - a. Total number and trends in full-time, part-time, degree-seeking, and

non-degree-seeking students being served.

- b. The number and trends of individuals, organizations, and agencies served through noncredit activities.
- 7. Higher education funding - A status report on higher education financing as compared to the long-term financing plan.
- 8. Ratio of incentive funding to total University System state general fund appropriations.
- 9. Ratio of University System state general fund appropriation to total state general fund appropriations.

The first performance and accountability report was published in December 2001, and the report has been published each subsequent year. The most recent report may be viewed on the Internet at www.ndus.nodak.edu/reports/details.asp?id=465.

STUDY PLAN

The following is a proposed study outline for the committee's consideration in its study of higher education:

- 1. Provide input for development of a request for proposals and list of potential consultants relating to the funding and accountability study.
- 2. Receive consultants' proposals and provide input regarding the selection of a study consultant.
- 3. After an independent consultant has been selected by the Legislative Council, receive progress reports and a final report, including findings and recommendations from the consultant regarding the Higher Education Roundtable recommendations and goals and objectives of the University System, the long-term financing plan for the University System, the University System's prioritization of higher education funding, and the accountability mechanisms.
- 4. Receive information from the State Board of Higher Education, the institutions of higher education, higher education students, private and tribal higher education institutions, the executive branch, business, and industry regarding the consultant's findings and recommendations.
- 5. Receive periodic reports from the State Board of Higher Education on the status of the board's review of the long-term financing plan, pursuant to Section 17 of Senate Bill No. 2003.
- 6. Conduct a budget tour and site visit of the higher education institutions as assigned.
- 7. Receive testimony from other interested persons regarding the committee's study of higher education.

8. Develop recommendations and any bill drafts necessary to implement the recommendations.
9. Prepare a final report for submission to the Legislative Council.

ATTACH:5