

COMMUNITY COLLEGE FUNDING STUDY

A Report Prepared for the
Legislative Finance Committee
Community College “Bulldog” Committee



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At the March meeting of the Legislative Finance Committee (LFC), the decision was made to defer action on the community college funding study until the June meeting, where staff would present a report to address specific issues and data requests made by LFC members. This report is intended to address all of those issues and to provide the additional information necessary for the LFC to make a decision on the options presented.

SUMMARY

While none of the models recommended in the legislative options would lead inevitably to an increase in the level of state funding for the community colleges, an analysis of the data tables in this report indicates that the model that uses the CHE201 form to rebase the cost of education factor (COE) results in the least dramatic change to the state percent share level in order to maintain the current state funding levels stated in HB 2. The NACUBO model, on the other hand, would create a larger change to that state percent share level.

The specific issues raised by LFC members are addressed below as follows:

- o Provide an illustration for each college that identifies the actual percentage being funded by the state appropriation under the existing formula (the two most recent fiscal years)

Figure 1
Community College Funding Formula - Actual State Percent Share 2005 and 2006
Comparative of HB 2 Funding Level and Actual College Costs per FTE *

	FY 2005 Actual			FY 2006 Operating Budget		
	HB 2 Funding Per FTE	Actual Cost Per FTE	State Percent Share	HB 2 Funding Per FTE	Budgeted Cost Per FTE	State Percent Share
Dawson	\$2,627	\$6,373	41.2%	\$2,758	\$6,115	45.1%
Flathead	2,636	6,267	42.1%	2,758	6,190	44.6%
Miles	2,624	7,131	36.8%	2,758	7,554	36.5%
Average	\$2,629	\$6,590	39.9%	\$2,758	\$6,620	41.7%

Sources: CHE201 Operating Budget Forms (9/21/05) & LFD Fiscal Reports (includes scholarship/waiver expenditures)
Note: The CHE201 Form reflects the Current Unrestricted Operating Funds for the Community Colleges
* HB 2 lists the State Percent Share as 46% in FY05 and 53% in FY06

- o Provide a historical illustration for each college that demonstrates the COE comparative between what is listed in HB 2 and the CHE 201 operating budget form for that fiscal year

Figure 2
Community College Funding Formula - Cost of Education Factor (COE)
Comparative Between Actual Operating Budgets and HB 2 Statement of the COE

College	COE FY 2006		COE FY 2005		COE FY 2004		COE FY 2003		COE FY 2002		COE FY 2001	
	HB 2	Budgeted CHE201	HB 2	Actual CHE201								
Dawson	\$5,203	\$6,115	\$5,706	\$6,373	\$5,706	\$6,411	\$5,267	\$6,890	\$5,267	\$6,466	\$5,000	\$6,646
Flathead	5,203	6,190	5,706	6,267	5,706	5,280	5,267	5,186	5,267	5,371	5,000	5,501
Miles	5,203	7,554	5,706	7,131	5,706	7,460	5,267	6,580	5,267	6,083	5,000	5,533
Average	\$5,203	\$6,620	\$5,706	\$6,590	\$5,706	\$6,384	\$5,267	\$6,219	\$5,267	\$5,973	\$5,000	\$5,893

Sources: CHE201 Operating Budget Forms & LFD Fiscal Reports (includes scholarships/waiver expenditures)
Note: Flathead experienced a dramatic, but temporary enrollment increase in FY2003 and FY2004 related to local/regional economic dislocation and subsequent worker retraining programs.

- Provide a historical illustration for each college that demonstrates the COE comparative between what is listed in HB 2 and the NACUBO formula
 - Includes all funds

Figure 3
Community College Funding Formula - Cost of Education Factor (COE)
Comparative Between NACUBO Formula Results and HB 2 Statement of the COE

College	COE FY 2008		COE FY 2006		COE FY 2004		COE FY 2002	
	HB 2	Projected NACUBO (All Funds)	HB 2	NACUBO (All Funds)	HB 2	NACUBO (All Funds)	HB 2	NACUBO (All Funds)
Dawson	N/A	\$10,524	\$5,203	\$9,562	\$5,706	\$9,540	\$5,267	\$8,533
Flathead	N/A	11,771	5,203	10,025	5,706	6,484	5,267	7,371
Miles	N/A	10,251	5,203	10,184	5,706	9,708	5,267	8,927
Average	N/A	\$10,849	\$5,203	\$9,924	\$5,706	\$8,577	\$5,267	\$8,277

Sources: NACUBO Formula Calculations Submitted by Each College & LFD Fiscal Reports (includes scholarships/waiver expenditures)
Note: Flathead experienced a dramatic but temporary FTE enrollment increase in FY2004 related to a local/regional economic dislocation and subsequent worker retraining programs.

- Excludes federal funds (federal funds average 10.4 percent of total FY 2006 college budgets)

Figure 4
Community College Funding Formula - Cost of Education Factor (COE)
Comparative Between NACUBO Formula and HB 2 Statement of the COE

College	COE FY 2008		COE FY 2006	
	HB 2	Projected NACUBO (Exclude Federal Funds)	HB 2	NACUBO (Exclude Federal Funds)
Dawson	N/A	\$9,321	\$5,203	\$8,469
Flathead	N/A	10,647	5,203	8,997
Miles	N/A	\$9,303	5,203	9,215
Average	N/A	\$9,757	\$5,203	\$8,894

Sources: NACUBO Formula Calculations Submitted by Each College & LFD Fiscal Reports (includes scholarships/waiver expenditures)

- Excludes capital funds (capital funds average 2.6 percent of total FY 2006 college budgets)

Figure 5
Community College Funding Formula - Cost of Education Factor (COE)
Comparative Between NACUBO Formula Results and HB 2 Statement of the COE

College	COE FY 2008		COE FY 2006	
	HB 2	Projected NACUBO (Exclude Capital Funds)	HB 2	NACUBO (Exclude Capital Funds)
Dawson	N/A	\$10,524.0	\$5,203.0	\$9,562.0
Flathead	N/A	11,008	5,203	9,332
Miles	N/A	10,175	5,203	10,103
Average	N/A	\$10,569	\$5,203	\$9,666

Sources: NACUBO Formula Calculations Submitted by Each College & LFD Fiscal Reports (includes scholarships/waiver expenditures)

- Excludes both federal and capital funds (federal and capital funds average 12.9 percent of total FY 2006 college budgets)

Figure 6
Community College Funding Formula - Cost of Education Factor (COE)
Comparative Between NACUBO Formula Results and HB 2 Statement
of the COE

		COE FY 2008		COE FY 2006	
College	HB 2	Projected NACUBO (Exclude Capital & Federal Funds)	HB 2	Projected NACUBO (Exclude Capital & Federal Funds)	
Dawson	N/A	\$9,321	\$5,203	\$8,469	
Flathead	N/A	9,883	5,203	8,305	
Miles	N/A	<u>9,227.00</u>	<u>5,203.00</u>	<u>9,134.00</u>	
Average	<u>N/A</u>	<u>\$9,477</u>	<u>\$5,203</u>	<u>\$8,636</u>	

Sources: NACUBO Formula Calculations Submitted by Each College & LFD Fiscal Reports (includes scholarships/waiver expenditures)

- For the above models (CHE201 and NACUBO) provide an illustration that demonstrates what the state percent share would need to be under each formula in order to fund the community colleges using the three-factor funding formula at a level that would be revenue neutral

- ***See Appendix Table 7 for CHE 201:***

It should be noted that the calculations for these illustrations simulated what would have actually happened in building these budgets in prior years had the formula been using the CHE201 form. Specifically, that the actual base year expenditures for each model were used, taken from the CHE201 form for the base year that was used at that time to calculate the subsequent biennial budget. The ultimate objective of this illustration is to determine how the use of the CHE201 form would affect the state percent share in order to reach the same appropriation level that was actually made in HB2 for each of the fiscal years illustrated.

It should also be noted that there are two fixed/variable cost ratios illustrated here, one at 60/40 and one at 80/20. You will note below that the preliminary formula offered by the community colleges projects a 78/22 fixed/variable costs ratio, but since this formula is intended to be only preliminary, I thought it important to display the potential range within which the college preliminary formula falls.

- ***See Appendix Table 8 for NACUBO***

It should be noted that the calculations for these illustrations simulated what would have actually happened in building these budgets in prior years had the formula been using the NACUBO calculations. Specifically, that the actual base year expenditures for each model were used, taken from the NACUBO calculation for the base year that was used at that time to calculate the subsequent biennial budget. The ultimate objective of this illustration is to determine how the use of the NACUBO formula would affect the state percent share in order to reach the same appropriation level that was actually made in HB2 for each of the fiscal years illustrated.

It should also be noted that the fixed/variable cost ratio used for the NACUBO model formula used the colleges 78/22 preliminary calculation in order to illustrate the anticipated impact of this projected formula.

- A proposed formula to determine the fixed vs. variable costs at each college (one that is transparent and verifiable) that could be used under the models being considered. The legislature may want to recommend that any formula that is adopted should be reviewed on a regular basis (e.g. every other biennium)

The colleges have worked collaboratively to devise a preliminary formula to determine the proportion of their annual costs that are fixed vs. variable. That formula starts by determining the costs of their “core” or required courses, many of which are those that comprise the transfer student curriculum (those students intending to utilize their two-year community college degree to transfer to a four-year campus and work toward a bachelor’s degree). From that point the formula considers the costs of hiring adjunct faculty, who are hired on a short-term contractual basis that permits change to be made in the event of student enrollment fluctuations.

Based upon these preliminary calculations, 50 percent of the instructional costs at each college are variable, those that are influenced each budget year by the level of student FTE enrollment.

The overall budget impact of this 50 percent of instructional costs calculation, establishes an average total proportion in FY2006 for the three colleges of 78 percent fixed costs and 22 percent variable costs, and in the projected budget for FY2008 that proportion is 79 percent fixed costs and 21 percent variable costs.

At this point, this proposed formula should be considered preliminary and, should the legislature adopt this formula alternative, it is recommended that the original funding study work group would work together with the colleges to develop a more specific fixed/variable costs formula in much more detail, with a priority that this formula would be transparent and verifiable. The primary objective of this preliminary formula at this point was to demonstrate that such a formula could be established in a collaborative and reasonable manner.

- A list of potential bill draft/statute changes that would be required under either of the models being considered

Should the legislature decide to recommend a model that includes a fixed vs. variable costs calculation, there would need to be a bill draft to amend the following statutes as noted in ***bold-italicized font*** and should the legislature recommend the NACUBO model to include federal funding in the COE calculation, there would need to be a bill draft to amend the following statutes as noted in **bold underline**:

20-15-310. Appropriation. It is the intent of the legislature that all community college spending, other than from **non-federal** restricted funds or funds generated by an optional, voted levy, be governed by the provisions of this part and the state general appropriations act. The state general fund appropriation must be based on a budget amount per full-time equivalent student ***for variable costs and on a budget amount for fixed costs***, as determined by the legislature. The student count may not include those enrolled in community service courses as defined by the board of regents.

History: En. Sec. 2, Ch. 495, L. 1981; amd. Sec. 1, Ch. 494, L. 1989.

20-15-312. Calculation and approval of operating budget. (1) Annually by September 1, the board of trustees of a community college shall submit an operating budget to the board of regents for their review. The operating budget of the community college must be financed in the following manner:

- (a) The general fund appropriation must represent a specific percentage of the budget amount per full-time equivalent student ***for variable costs and on a budget amount for fixed costs***, as determined by the legislature. This percentage must be specified in the appropriations act appropriating funds to the community colleges for each biennium. This percentage does not apply to any portion of the unrestricted budget in excess of the budget amount per full-time equivalent student ***for variable costs and the budget for fixed costs***, as determined by the legislature.
- (b) The mandatory levy amount must represent a specific percentage of the budget amount per full-time equivalent student, as determined by the legislature. This percentage must be

specified for each community college by the board of trustees of the district and approved by the board of regents.

- (c) The funding obtained in subsections (1)(a) and (1)(b) plus the revenue derived from tuition and fee schedules approved by the board of regents and unrestricted income from any other source **together with federal funding as part of the general fund appropriation calculation only** is the amount of the unrestricted budget. A detailed expenditure schedule for the unrestricted budget must be submitted to the board of regents for their review and approval.
- (d) The amount estimated to be raised by the voted levy must be detailed separately in an expenditure schedule.
- (e) The spending of each restricted funding source must be detailed separately in an expenditure schedule.
- (f) The expenditure schedules provided in subsections (1)(c) through (1)(e) represent the total operating budget of the community college.
- (g) The board of regents shall review the proposed total operating budget and all its components and make any changes it determines necessary. The board of trustees of a community college district shall operate within the limits of the operating budget approved by the board of regents.

History: En. Sec. 4, Ch. 495, L. 1981; amd. Sec. 2, Ch. 494, L. 1989; amd. Sec. 4, Ch. 243, L. 1997.

DECISION OPTIONS FOR LFC

(see decision tree attached for decision options illustration)

OPTION ONE

~~Do nothing. The legislature may wish to maintain the current COE factor and the variable historical methods that have been used to adjust this factor in each biennial budget. While the COE factor has some problems, the actual results reflected in HB 2 appropriations have maintained a 4.58 percent average annual growth rate (though this is driven primarily by student enrollment increases of 2.62 percent) during the 25 year history of the formula (see Table 1 above), which appears to be a reasonable comparative to other inflationary indices. In addition, the formula and COE factor have allowed maximum budget policy discretion and flexibility in putting together 25 years of state budgets.~~

The LFC eliminated further consideration of Option One at the March 9, 2006 meeting.

OPTION TWO

Rebase the COE factor in order to establish a new base figure, and consider recommending a specific method for adjusting this new base COE factor in each subsequent budget.

If the legislature wishes to rebase the COE factor in order to see that it more accurately reflects the actual cost of education, the COE could be recalculated based upon actual figures averaged across the community colleges for FY 2006, which will serve as the base year for the 2009 biennium budget. There are two rebasing models that could be considered by the legislature:

- Adopt the cost of education figures from the Commissioner of Higher Education (CHE) form 201, which each college is required to complete, as per statute, in establishing annual operating budgets. CHE 201 includes a separate accounting schedule for the current unrestricted operating funds, segregating these funds from others, including restricted, auxiliary, and capital funds.
- Adopt the “Methodology for Identifying the Cost of Delivering Undergraduate Education” as devised by the National Association of College and University Business Officers (NACUBO). The NACUBO formula was specifically developed for this purpose, to provide public policy makers with a transparent

mechanism to determine the cost of education at any type of higher education institution. In a test run of the formula performed as part of each community college site visit, the formula was transparent and adaptable to each college operations. The formula essentially has each college allocate costs to various educational functions (e.g. instruction, student services, library, etc.), these are totaled and allocated by the number of FTE students. There would need to be a set of universal definitions devised, however, to assure equalized application. According to the test run of the NACUBO formula, the projected COE factor for FY 2006 is \$8,486 if an average cost is used, and it is \$8,442 if a weighted average cost is used.

- It should be noted that the NACUBO formula includes federal revenue that CHE 201 does not count, as these are considered “restricted funds” under current fiscal policy of the community colleges. The advantage to including federal costs would be that it provides a more complete calculation of the total costs of education at each community college. The exclusion of federal funds, as part of restricted revenue, is related to the policy goal of maximizing local control through the opportunity for local trustees to implement a voted tax levy on the local community. Including federal revenues in this component of the state budget calculation does not appear to impinge upon that local control policy goal. It should be noted, that if the legislature considers the NACUBO formula these additional federal funds would need to be considered in order to explain a higher COE factor in making historical comparisons. Most important, however, including federal funds (restricted revenues) in the COE factor calculation may require an amendment to the community college funding statute (20-15-301 MCA, et. seq.).

In considering these two options for rebasing the COE factor, it is apparent that adopting the CHE 201 form would eliminate the possibility of changing statute and eliminate the need for adjusting the formula, as the NACUBO option presents. It should also be noted that the CHE 201 option has the advantage of having an extended historical function within the Montana University System and the community colleges. It is already well understood by all parties.

Separate from the calculation to rebase the COE factor is consideration of recommending a method to adjust the base going forward in subsequent biennial budgets. There are a number of adjustment models that the legislature may want to consider, including the following:

- Do nothing and make no specific recommendation on an adjustment method, thus allowing the past practice of executive budget recommendation and legislative review, consideration of amendment, and approval each biennium.
- Recalculate the base each biennium, using one of the above models, thus eliminating the need to make an adjustment calculation of the base COE factor. Under this model the budget process essentially becomes a “zero-based” model rather than a base plus incremental adjustments model.
- Recommend an adjustment to the COE base factor from among the universal inflationary indices:
 - Consumer Price Index U.S. cities average (CPI).
 - Montana Personal Income Growth rate (PI).
 - Montana Personal Income Per Capital Growth rate (PerCap PI).
 - Montana Wage & Salary Growth rate (Wage&Salary).

OPTION THREE

Rebase the COE factor, using one of the above models, in order to establish a new base figure, but also include a calculation that establishes both a fixed cost of education component and a variable cost of education component, which, together, would comprise the new COE factor. Then consider recommending a specific method for adjusting this new base COE factor in each subsequent budget, selecting from the above adjustment options.

Should the legislature select this option, a fixed vs. variable cost model for the COE factor, it is recommended that the working group be charged to work with the community colleges to establish a transparent and logical formula to define which expenditures in their budgets are fixed and which are variable. In a preliminary discussion with the fiscal staff of the colleges, there was speculation that fixed costs comprise approximately 60 percent of the total expenditure budget. All colleges agreed that a transparent formula could be achieved.

This option would best address the additional concerns that have been raised about the COE factor not being an accurate reflection of community colleges costs in that it assumes that all expenditure levels are driven by the enrollment FTE count. The colleges consider this to be the preferred option.

APPENDIX TABLE 7

Not Contemplate Fixed vs. Variable Costs Formula							
Community College Funding History Three Factor Formula and HB 2 Appropriations Adjusted State Percent Share for CHE201 to Be Revenue Neutral					Check Column	Check Column	
Fiscal Year	Student Enrollment Projections	CHE201 Cost of Education Factor (COE)*	State Percent Share to Maintain HB 2 Funding Level	Adjusted HB 2 Appropriation (with CHE201)	HB 2 Actual Appropriation	State Percentage Support (in HB 2)	
2001	2,180	\$4,910	51.93%	\$5,559,043	\$5,559,000	51%	
2002	2,030	5,507	50.56%	5,651,964	5,651,748	53%	
2003	2,040	5,507	50.56%	5,679,807	5,679,546	53%	
2004	2,322	5,728	46.66%	6,205,331	6,205,139	47%	
2005	2,369	5,728	45.94%	6,233,911	6,233,759	46%	
2006	2,631	5,934	46.47%	7,255,221	7,255,219	53%	

Incorporates Fixed vs. Variable Costs Formula @ 60/40 Ratio							
Community College Funding History Three Factor Formula and HB 2 Appropriations Adjusted State Percent Share for CHE201 to Be Revenue Neutral					Check Column	Check Column	
Fiscal Year	Student Enrollment Projections	CHE201 Cost of Education Factor (COE)*	State Percent Share to Maintain HB 2 Funding Level	Adjusted HB 2 Appropriation (with CHE201)	HB 2 Actual Appropriation	State Percentage Support (in HB 2)	
2001	2,180	\$10,659,274	52.15%	\$5,559,024	\$5,559,000	51%	
2002	2,030	11,323,280	49.91%	5,651,675	5,651,748	53%	
2003	2,040	11,345,307	50.06%	5,679,461	5,679,546	53%	
2004	2,322	12,761,399	48.63%	6,205,868	6,205,139	47%	
2005	2,369	12,869,086	48.44%	6,233,785	6,233,759	46%	
2006	2,631	\$15,224,607	47.66%	\$7,255,287	\$7,255,219	53%	

Incorporates Fixed vs. Variable Costs Formula @ 80/20 Ratio							
Community College Funding History Three Factor Formula and HB 2 Appropriations Adjusted State Percent Share for CHE201 to Be Revenue Neutral					Check Column	Check Column	
Fiscal Year	Student Enrollment Projections	CHE201 Cost of Education Factor (COE)*	State Percent Share to Maintain HB 2 Funding Level	Adjusted HB 2 Appropriation (with CHE201)	HB 2 Actual Appropriation	State Percentage Support (in HB 2)	
2001	2,180	\$10,644,347	52.23%	\$5,559,010	\$5,559,000	51%	
2002	2,030	11,371,464	49.70%	5,651,618	5,651,748	53%	
2003	2,040	11,382,477	49.90%	5,679,856	5,679,546	53%	
2004	2,322	12,581,711	49.32%	6,205,300	6,205,139	47%	
2005	2,369	12,635,554	49.33%	6,233,498	6,233,759	46%	
2006	2,631	\$15,095,243	48.07%	\$7,255,529	\$7,255,219	53%	

* Source: CHE201 Actual Operating Budgets (COE averages)
HB2 Figures above exclude one-time-only funding

APPENDIX TABLE 8

Not Contemplate Fixed vs. Variable Costs Formula						
Community College Funding History Three Factor Formula and HB 2 Appropriations Adjusted State Percent Share for NACUBO to Be Revenue Neutral					Check Column	Check Column
Fiscal Year	Student Enrollment Projections	NACUBO Cost of Education Factor (COE)*	State Percent Share to Maintain HB2 Funding Level	Adjusted HB 2 Appropriation (with CHE201)	HB 2 Actual Appropriation	State Percentage Support (in HB 2)
2002	2,030	\$8,277	33.64%	\$5,651,457	\$5,651,748	53%
2004	2,322	8,577	31.16%	6,205,164	6,205,139	47%
2006	2,631	\$9,924	27.79%	\$7,255,198	\$7,255,219	53%
* Source: NABUBO Formula Calculations (includes all funds)						
HB2 Figures above exclude one-time-only funding						

Not Contemplate Fixed vs. Variable Costs Formula						
Community College Funding History Three Factor Formula and HB 2 Appropriations Adjusted State Percent Share for NACUBO to Be Revenue Neutral					Check Column	Check Column
Fiscal Year	Student Enrollment Projections	NACUBO Cost of Education Factor (COE)	State Percent Share to Maintain HB2 Funding Level	Adjusted HB 2 Appropriation (with CHE201)	HB 2 Actual Appropriation	State Percentage Support (in HB 2)
2006*	2,631	\$8,894	31.01%	\$7,255,205	\$7,255,219	53%
2006**	2,631	9,666	28.53%	7,255,280	7,255,219	53%
2006***	2,631	\$8,636	31.93%	\$ 7,255,371	\$7,255,219	53%
* Source: NABUBO Formula Calculations (w/o federal funds)						
** Source: NABUBO Formula Calculations (w/o capital funds)						
*** Source: NABUBO Formula Calculations (w/o federal funds and capital funds)						
HB2 Figures above exclude one-time-only funding						

Incorporates Colleges Fixed vs. Variable Costs Formula						
Community College Funding History Three Factor Formula and HB 2 Appropriations Adjusted State Percent Share for NACUBO to Be Revenue Neutral					Check Column	Check Column
Fiscal Year	Student Enrollment Projections	NACUBO Cost of Education Factor (COE)*	State Percent Share to Maintain HB2 Funding Level	Adjusted HB 2 Appropriation (with CHE201)	HB 2 Actual Appropriation	State Percentage Support (in HB 2)
2004	2,322	\$18,120,751	34.25%	\$6,205,451	\$6,205,139	47%
2006	2,631	\$19,827,995	36.59%	\$7,255,262	\$7,255,219	53%
* Source: NABUBO Formula Calculations (includes all funds)						
HB2 Figures above exclude one-time-only funding						

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