



Joint Subcommittee On Postsecondary Education Policy and Budget

60TH Montana Legislature

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FUNDING FORMULA REVIEW WORK PLAN ITEM

BACKGROUND INFORMATION

September 25, 2007

During the 2005-2006 interim, the Legislative Finance Committee (LFC) conducted a funding study to address concerns about the formula used to determine the state appropriation for Montana's community colleges. Concerns about that formula focused on the need for a formula that is transparent, able to be understood by policy makers, and that the formula factors are both meaningful and accurate.

During the course of that study and the resulting legislation, the LFC oversight subcommittee suggested that the recommended changes to the community college funding formula should be considered for application to the university educational units as an option for calculating the base funding levels for the university system campuses.

Therefore, the PEPB has been asked to review and consider funding formula options, including the new community college funding formula, that may be used to determine the base funding level for the university units in order to achieve similar public policy goals that the formula be transparent, simple enough to be easily understood, and that the formula factors be both meaningful and accurate.

In starting this PEPB interim discussion, below is a review of the new community college funding formula that was approved in SB 12 in the 2007 regular session of the legislature.

It is not the intent of this report to suggest that the new community college funding formula is ideal and should be used to determine the state appropriation for the university units, but rather this report is intended to review the formula as an option for PEPB consideration, a starting point for this interim project to consider funding formula ideas for the university educational units of the Montana University System.

Since 1981 the general fund appropriation for the community colleges has been based upon a three-factor funding formula as follows:

- The cost of education per FTE student
- Annual FTE student enrollment projections
- The state percent share of funding

The funding statute, 20-15-301 MCA, requires that these three factors be multiplied to determine the state general fund appropriation. The statute, however, did not identify a specific method to determine what the cost of education per student was during each year of the budget. As a result, over the years the cost of education figure became so distorted that the LFC study concluded that the formula “appears that legislators are funding a state percentage of an irrelevant number” (that cost of education being irrelevant).

Therefore, the LFC recommended the following revisions to the funding formula:

- The community college funding formula should rebase the cost of education (COE) factor of the formula so that it accurately reflects the actual cost of education. The COE should be based upon actual figures averaged across the community colleges for FY 2006, which would then serve as the base year for the 2009 biennium budget
- The rebased COE should start with cost of education data from the Commissioner of Higher Education (CHE) form 201, which each college is statutorily required to complete 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
- The calculation to rebase the COE should be made each biennium using the CHE 201, thus eliminating the need to make a special adjustment calculation of the base COE factor, which was done in the past and has led to problems in the formula
- The new CHE 201 model should 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
- That this fixed/variable costs calculation should be reviewed and updated every third biennium (every 6 years)

As a result of these recommendations the legislature approved SB 12 amending the community college funding statute so that the three-factor funding formula looks like the following:

$$[(\text{Annual FTE Student Enrollment Projections} \times \text{Variable Cost of Education per Student}) + \text{Fixed Cost of Education}] \times \text{State Percent Share} = \underline{\underline{\text{State General Fund Budget}}}$$

- Student Enrollment Projections = the aggregated FTE count that the three colleges project for each year of the proposed biennial budget
- Variable Cost of Education per Student = the total variable costs for the base year divided by the actual FTE student enrollment for the base year (both derived from base-year CHE 201 form)
- Fixed Cost of Education = the total fixed costs for the base year (derived from base-year CHE 201 form)
- State Percent Share = the percent of the CHE 201 derived fixed + variable costs calculation that the legislature decides, as a matter of public policy, to support with a state appropriation. The state percent share factor is the mechanism through which the legislature would exercise public policy in this formula, as the percent level established is purely a matter of the public policy decision the legislature makes based upon available state revenue and the amount of funding the legislature determines that state government should support Montana resident students attending community colleges

The LFC oversight subcommittee members concluded that the new formula more accurately reflects the cost of education, is transparent and easier to understand, and it allows the legislature to apply public policy by setting the state percent share against that accurate cost data in order to determine the state appropriation level. It is through this factor that public policy is most directly applied to the community college assistance program, as this indicates the level of support that

the legislature determines that state government should support the cost of education for Montana resident students, based upon available state revenue.

Another important addition to the formula is the fixed/variable cost calculation, as the state funding level better contemplates the types of costs that the colleges confront in educating students. This was included in order to provide a better, more reliable management tool to the colleges as they build their annual budget.

PEPB Option: Appoint a working group to discuss the viability of adopting this type of funding formula to determine the base funding level of state funding for the eight educational units of the MUS, and/or to consider other options as well. Request that this group report back to PEPB at the **March 13, 2008** meeting with a recommendation on whether or not to proceed. Working group members may include representatives from LFD, OBPP, OCHE, and MUS university units, together with a legislator and Regent member.

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