TOPIC: **FY 2021-22 STATE FUNDING ALLOCATIONS TO HIGHER EDUCATION INSTITUTIONS THROUGH FUNDING FORMULA**

PREPARED BY: **JASON SCHROCK, CHIEF FINANCIAL OFFICER, EMILY ORR, BUDGET DIRECTOR, EMMA FEDORCHUK, LEAD FINANCE ANALYST**

I. SUMMARY

Given current budget and revenue forecasts, it is likely that funding for higher education institutions will see a reduction in Fiscal Year 2021-22. The purpose of this agenda item is to give the Commission the opportunity to discuss different ways such a decrease may be approached using the new funding allocation formula, as well as provide background information to inform that discussion. This agenda item does not seek Commission action. This agenda item is intended to generate discussion which will inform future agenda items.

II. BACKGROUND

Fiscal Year 2020-21

State funding for public higher education institutions' operating budgets was reduced by $493 million, or 58 percent, in the state budget adopted by the legislature through the "Long Bill" (HB 20-1360). However, the Governor allocated $450 million in federal funds to the state's public higher education institutions from the federal CARES Act through an executive order. This money must be used by institutions for responding to public health needs resulting from COVID-19 and to provide economic support to the state through educating students. Per the Long Bill, 5 percent of the 58 percent cut to higher education institutions in FY 2020-21 is intended to be ongoing. The below table shows the state funding amounts incorporating the 5 percent ongoing cut by institution – this is the base from which the Department is working for FY 2021-22. State funding for public higher education institutions' operating budgets is currently expected to need to be reduced in FY 2021-22 from the levels shown in the table due to COVID-19's impacts on the state budget.

Table 1: FY 2020-21 Base Using 5% Ongoing Reduction

	FY 2020-21 Base (millions)
Adams	$16.4
Mesa	30.9
Metro	60.8
Western	14.5
CSU System	163.8
FLC	13.4
CU System	232.1
Mines	24.1
UNC	44.7
CCCS	180.9
Total	*$781.5*

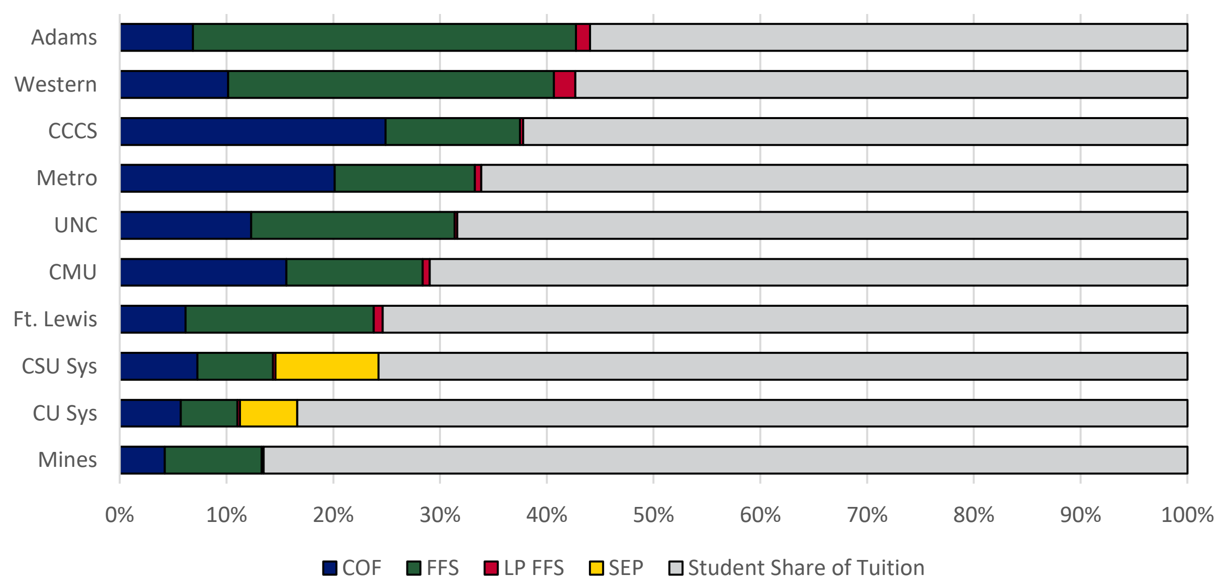
House Bill 20-1366

HB 20-1366 established a new funding allocation model for allocating state appropriations to public higher education institutions. FY 2021-22 is the first year in which this new model is required to be used by state statute. Attachment A (formula one-pager) contains further details on the model.

General Fund as a Proportion of E&G

Depending on their size and ability to generate tuition revenue, state appropriations constitute varying percentages of institutions' Education and General (E&G) budgets, a subset of higher education expenses that includes education and directly related expenses, plus state-funded research. Information on E&G budgets is collected annually via budget data books (BDB). The BDBs serve as a summary of unrestricted spending of funds, most of which are generated via General Fund support and tuition revenue. The chart below summarizes the state General Fund/tuition revenue split by governing board.

Chart 1: State General Fund (by Source) and Tuition Revenue Splits, 2018-19 Actuals



Base Cost Increases

Given current budget and revenue projections, a "flat" funding scenario (i.e. no increase or decrease in funding from the levels shown in the above table) is the most optimistic funding scenario at this time. However, even when all else is held constant, institutional costs generally increase each year from personnel-related costs, including Health/Life/Dental (HLD) benefits and the impact of inflation on certain operating costs. This increase is referred to as a governing board's core minimum, or base cost increase. In practice, this means that a "flat" funding scenario actually represents a functional cut to institutions. The below chart shows the estimated base cost increases for FY 2021-22 based on the following assumptions:

- No salary increase for FY 2021-22
- HLD employer contribution growth rate of 4.2 percent (based on the April 2020 Centers for Medicare and Medicaid Services National Health Expenditure Projections for State and Local Governments)
- Other cost growth of 1.9 percent (inflation rate based on Governor's Office of State Planning and Budgeting June 2020 CPI forecast)

Table 2: Estimated FY 2021-22 Core Minimum Cost Increases by Governing Board

	Total Base Cost Increase (millions)*
Adams	$0.5
Mesa	1.1
Metro	2.1
Western	0.4
CSU System	8.2
FLC	0.7
CU System	17.8
Mines	2.3
UNC	1.4
CCCS	5.7
Total	*$40.3*

*It is important to note that some governing boards indicates that these estimates understate their true base minimum cost increases.

Revenue Analysis/Hanover Research

The Department contracted with Hanover Research to conduct a study on institutional revenues and expenditures compared to their peers. The Department is analyzing the results of the research in conjunction with institutions. The final results of the study could offer valuable context for the Commission to consider in concert with the funding formula.

While all of Colorado's institutions receive less state funding than their peers, there are degrees of magnitude. Funding also varies in terms of total revenue based on institutions' widely varying abilities to charge tuition and generate enrollment increases. The Commission can expect additional details and results in the coming months as the final stages of the project conclude.

III. STAFF ANALYSIS

There are several approaches the Commission may consider in a reduction scenario. For example, the Commission could recommend that the allocations be based solely on the outcomes of the performance component of the formula through Step 2. Another simple, straightforward option is a proportional reduction in which each governing board's appropriation is reduced by the same percentage. While this approach treats each governing board equally, it is not necessarily equitable – there is a larger impact on institutions that rely more heavily on state funding (as shown in Chart 1). If this approach is desired, it may be better to not allocate the reduction through the formula and request that the formula be suspended for another year.

Should the Commission wish to take other factors into consideration, adjustments in funding can be made in either Steps 1 or 3 of the formula. In recommending these adjustments, for example, the Commission can consider an institution's reliance on state resources. This would benefit governing boards where state funding makes up a higher percentage of their budget. Other considerations could include preserving funding for governing boards who are furthest from their peers in terms of state appropriations or total revenue, as determined by the results of the Hanover study, or assessing funding needs of each governing board based on their unique circumstances.

IV. STAFF RECOMMENDATIONS

The Commission is not being asked to make a recommendation at this time. The Commission's discussion will inform a future agenda item, which staff will bring forward later in the budget process.

V. STATUTORY AUTHORITY

23-18-306. Duties and powers of the commission – budget provisions - periodic review of funding formula - report.

(1) (a) For the 2021-22 state fiscal year and each state fiscal year thereafter, the department and commission shall submit a budget request by November 1 of each year that includes:
(i) a detailed description of requests for additional ongoing and temporary funding pursuant to section 23-18-303.5 (2) and (3) and recommendations for additional funding, if any; and
(ii) recommendations for:
(a) changes in the amount of performance funding pursuant to section 23-18-303.5 (4), if any;
(b) the percentage allocation of performance funding among the performance funding metrics specified in section 23-18-303.5 (4)(b);
(c) additional funding for fee-for-service contracts pursuant to section 23-18-304, if any; and
(d) tuition spending authority for the state institutions of higher education.

ATTACHMENT(S):

Attachment A: Formula One-Pager