



Why Performance-Based Funding Fails to Improve College Graduation Rates — And How States Can Do Better

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The number of students who enroll in college and take on debt without receiving a college degree is striking. Of all students enrolled in America's public four-year universities, less than 60 percent will graduate with a degree within six years. Even fewer enrollees graduate from two-year colleges, where only about 30 percent earn a credential within three years. To put this in perspective, over the past 20 years, more than 30 million students have enrolled in U.S. colleges only to drop out without receiving a degree or certificate.

What can be done? In response to what many call the "completion crisis," lawmakers in more than 30 states have implemented performance-based policies that fund universities based on how many students they *graduate* instead of, or in addition to, how many they *enroll*. The underlying logic is simple: if colleges have an incentive to graduate more of the students they enroll, they will invest more to help their students actually earn degrees.

The Weak Performance of Performance-Based Funding

Despite the intuitive appeal of performance-based funding, research evidence suggests these policies do not produce intended boosts in student graduation rates. In fact, after gathering all of the published, peer-reviewed research on the topic and combining it into one model, my colleagues and I have demonstrated that performance-based funding has, on average, zero impact on the number of students making it to graduation. Even more concerning, we find that the average performance-based funding policy reduces college access for underrepresented groups of potential students. This happens because college administrators raise admissions standards in hopes of narrowing admitted enrollees to only those most likely to make it to graduation.

Our results do not say that every kind of performance-based funding is bound to fail at improving college graduation rates, only that current policy designs in the vast majority of states are not accomplishing the intended policy goals. To make improvements in the future, we need to understand why such an intuitive and well-intentioned type of program so clearly fails to help more students graduate from college.

Oversights in Current Policies

My research pinpoints three areas where performance-funding policies fail to align with reality and thus prove ineffective.

- **Failure to recognize competing stakeholders.** For changes in state funding of colleges and universities to shift the priorities of university administrators, state legislatures would have to be the most important source of support. But this does not reflect current realities in higher education, because most institutions have multiple competing stakeholders ranging from donors and state regents to accreditation agencies and prominent politicians, all of whom can introduce competing pressures.
- **Colleges and universities have unequal capacities to improve graduation rates.** Research has shown that institutional capacities and student populations at community colleges are vastly different from those found at well-resourced research universities. Some colleges may be able to provide expanded student support, but others cannot. Indeed, many public two-year colleges are already underfunded and serve predominantly disadvantaged students. If the goal is to increase the quality of educational services, slashing appropriations to already struggling institutions could make the situation even worse for their students and teachers.

- **Financial incentives may have limited and unintended impacts.** Financial incentives may not be enough to impact complex outcomes and can lead to unintended consequences, such as reducing access to college for minorities and low-income people. In many fields of social policy, scholars have documented such patterns. For example, when hospitals have implemented performance-based funding models, health outcomes were not improved, instead surgeons and physicians misdiagnosed more patients and tried to avoid those with the greatest needs. Similarly, when policymakers tied funding for school teachers to standardized test results for their students, teachers narrowed instruction to tested areas rather than helping students learn to become critical thinkers.

How To Improve College Completion Rates

Taken together, real-world challenges make improving graduation rates much more complicated than many performance-based funding policies presume. So what should concerned policymakers do? There are two main ways forward.

- If a state is determined to use performance-based funding formulas for its public institutions, policymakers should design the formulas to encourage colleges and university leaders to target enhanced supports on the most vulnerable student populations. Recent research shows that performance-based funding can direct financial bonuses to institutions that provide access and extra supports to underserved student groups. Carefully designed policies can alleviate some of the negative side-effects of performance-based funding, by ensuring access to less privileged students as overall graduation rates are improved.
- More fundamentally, policymakers should address the root cause of the problem, not the symptoms. The **number one reason** so many students drop out is that college has become less affordable for many lower and middle-class families.

Indeed, instead of pursuing policies that manipulate incentives for institutions, state legislatures and others would be well advised to invest in need-based financial aid and other programs to help needy students stay in college until they graduate. Addressing the underlying issue of college affordability for low-income and middle-class families will not only improve completion rates, but also strengthen state and local economies. In turn, more students earning degrees will swell the ranks of skilled workers, boost economic growth and business profits, and generate more tax dollars to invest in education and other public necessities in the future.

Read more in Elizabeth Bell, Alisa Fryar, Nicholas Hillman, and David Tandberg, "When Intuition Misfires: A Meta-analysis of Performance-Based Funding" in *Research Handbook on Quality, Performance and Accountability in Higher Education*, edited by Ellen Hazelkorn, Alexander McCormick, and Hamish Coates (Edward Elgar Publishing, 2018).