SKETCHING A NEW CONSERVATIVE EDUCATION AGENDA

# Outcomes-Based Higher Education Funding: A Case Study from Texas

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## Key Points

- Despite higher education's emphasis on diversity, the structure and function of postsecondary institutions feature remarkably little meaningful diversity.
- One exception to this rule is Texas State Technical College (TSTC), which focuses exclusively on economic advancement and is funded based on the economic benefits it provides to its graduates.
- Policymakers in other states who are looking to build more responsive and effective postsecondary institutions ought to take a close look at the financial structure that has enabled TSTC's unique success.

In *A Time to Build: From Family and Community to Congress and the Campus, How Recommitting to Our Institutions Can Revive the American Dream*, the American Enterprise Institute's Yuval Levin distinguishes three competing missions of the American university: social, economic, and truth-seeking. The creative tension among these missions is one reason American universities are the envy of the world. But as he—like us—sees it, the social mission is increasingly dominating the other two.

And yet for all the higher education sector's emphasis on "diversity," it boasts remarkably little institutional diversity. A happy exception to this is Texas State Technical College (TSTC), a college that focuses exclusively on economic returns, which could provide a model for legislatures in other states to emulate.

TSTC is remarkable for two reasons. First, its single mission is graduating students who can go on to attain higher-paying jobs. Second, Texas's state funding formula was specifically designed to hold it accountable to accomplish this mission. Texas statute stipulates that TSTC will offer "courses of study in technical-vocational education for which there is demand" and "contribute to the educational and economic development of the State of Texas by offering occupationally oriented programs." In developing these programs, "primary consideration shall be placed on industrial and technological manpower needs of the state."[1] In Levin's taxonomy, TSTC's mission is *only* focused on the economic mission.

While TSTC is a two-year institution that offers associate degrees and certificates, it is also a structural outlier in the higher education sector. It is not a part of the community college system. It is a separate state agency serving students on 10 campuses. A large proportion of TSTC's student body is comprised of nontraditional students, and its TSTCYou programs operate on a "Performance-Based Education"[2] model in response to employer feedback and student needs.

TSTC's singular focus has enabled it to buck national trends affecting community colleges. For example, a recent National Bureau of Economic Research working paper noted that Assembly, Repair, and Manufacturing (ARM) programs were particularly hard-hit by the COVID-19 pandemic due to challenges with in-person instruction in highly hands-on formats. Male enrollment declined 15 percent—more than female enrollment, which declined 6.8 percent—a change that the authors attribute largely to the concentration of men in ARM fields.[3]

The Texas community college sector saw a fall semester head-count decline[4] of 13.5 percent from 2019 to 2021, with male enrollment down 15.2 percent and female enrollment down 12.3 percent. In contrast, TSTC—whose program offerings skew heavily toward ARM fields—has seen head-count *growth* from 2019 to 2022. Certified head counts[5] via the Texas Higher Education Coordinating Board point to *more* male than female enrollment at TSTC since 2019.

What is the engine of TSTC's success? According to a recent presentation by Chancellor Michael Reeser to the Texas Commission on Community College Finance, TSTC's incentives line up with its mission.[6] The mechanism is the returned-value funding model, whose exact methodology is spelled out (for the curious) in the Texas Higher Education Coordinating Board's rules.[7]

Here's the simple version. TSTC's appropriation is the aggregate of TSTC's "value add," as calculated by its direct and indirect contributions to the state's economy for each cohort member. A cohort is comprised of graduates, transfers, and leavers in a designated year. A cohort member's direct and indirect contributions are determined by their incremental wage—that is, their wages after finishing the program minus the minimum wage. (Incremental wages are calculated for the first five years after finishing the program.) The additional tax revenue from this higher wage is determined (including a small, assumed spillover effect), and the state and TSTC split the higher tax revenue, with TSTC getting a commission rate of 36 percent.

To better illustrate how this works, we'll provide an example of a hypothetical graduate. Let's call him Jose, the heating, ventilation, and air conditioning repairman. His return value payment for TSTC would be calculated as follows:

1. Jose's incremental wages (actual wage minus the minimum wage) for the first five years after graduating are calculated. Suppose Jose earns $54,000 per year, and the minimum wage is $15,080. His incremental wage each year would be $38,920, which is $194,600 over five years.

2. The state's economic benefit is calculated as the direct and indirect increase in tax revenue from these incremental wages.

   a) Jose's incremental wages are multiplied by 7 percent (an estimate of how much he will pay in taxes), yielding $13,622. This is the direct increase in the state's tax revenue.

   b) To account for assumed spillover effects (indirect increase in tax revenue), the direct value is multiplied by 1.5, yielding $20,433.

   c) The total increase in tax revenue is the sum of the direct and indirect taxes ($34,055).

   d) TSTC receives 36 percent of the additional tax revenue ($12,260), and the state keeps the remaining 64 percent ($21,795).

Texas has the somewhat unique ability to verify graduate wages through a cooperative arrangement between the Texas Higher Education Coordinating Board and the Texas Workforce Commission (TWC). The Texas Higher Education Coordinating Board obtains unemployment insurance (UI) wage records from the TWC, collates the data using student social security numbers, and runs the formula calculation. TSTC can then access that data from the Texas Higher Education Coordinating Board. Texas Public Policy Foundation research indicates that improvements to UI wage records in Texas could lead to more public institutions implementing successful funding models that include postgraduation wages as a component of their formula.[8] States with a less robust wage information infrastructure can emulate Texas's example.

Students who are attracted to TSTC's mission know exactly what they're going to get. Billboards up and down I-35 through central Texas make a simple pitch: Complete one of nine eligible programs, and you either "Get a Job or Get a Refund."[9] (Students can partake in the money-back guarantee if they can't obtain a job within six months after graduation.) The eligible programs include diesel equipment, robotics, welding, and industrial systems and directly reflect the labor market demand in information technology, advanced manufacturing, transportation, and the energy and construction trades. TSTC sunsets all its programs annually to ensure they are meeting the needs of high-wage, high-demand industries. After all, its existence depends on it.

Compared with TSTC's focused mission, public two-year junior colleges in Texas operate at a disadvantage. Their enabling statute gives them multiple missions:

> Texas public junior colleges shall be two-year institutions primarily serving their local taxing districts and service areas in Texas and offering *vocational, technical, and academic courses* for certification or associate degrees. *Continuing education, remedial and compensatory education* consistent with open-admission policies, and programs of counseling and guidance shall be provided. Each institution *shall insist on excellence in all academic areas—instruction, research, and public service. Faculty research*, using the facilities provided for and consistent with the primary function of each institution, *is encouraged.*[10] (Emphasis added.)

These community colleges would be better off, and maybe could recover their enrollment, if their mission were more tightly articulated and their financial incentives directly lined up with their institutional mission. Unfortunately, TSTC is the only example of this in Texas. In other states, community colleges face a similarly mixed set of missions and incentives that largely maximize contact hours rather than provide economic benefits for their students.

Policymakers in Texas or other states who are looking for ways to make the postsecondary system as a whole more responsive to the local economy's needs could restructure community colleges into two separate divisions: one that encompasses career-focused programs, with funding based on labor market outcomes, and another that focuses on academic preparation, with funding based on transfers to four-year institutions that result in credentials of value or low student loan debt relative to earnings. This approach may not work for all community colleges, and as an alternative, Texas could eliminate the service district areas that form roadblocks to competition among the two-year sector, allowing TSTC or other public two-year colleges to operate in new regions.

Too much of the conversation about higher education revolves around elite or flagship state four-year universities. Governors and state legislators should broaden their focus and home in on exactly what they want in return for their investment of taxpayer money. The example of TSTC demonstrates that tightly aligning funding to economic outcomes can provide the basis for a highly efficient and successful postsecondary entity. Policymakers ought to either consider legislation enabling the creation of analogous institutions or shift the funding system of existing postsecondary institutions to one that has a clear and direct feedback mechanism for economic results.

## About the Authors

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## Notes

1. Tex. Educ. Code § 135 (1971) (revised 1991).
2. Texas State Technical College, "TSTCYou," https://www.tstc.edu/you.
3. Diane Whitmore Schanzenbach and Sarah Turner, "Limited Supply and Lagging Enrollment: Production Technologies and Enrollment Changes at Community Colleges During the Pandemic" (working paper, National Bureau of Economic Research, Cambridge, MA, January 2022), https://www.nber.org/papers/w29639.
4. Texas Higher Education Accountability System, Public Two-Year Colleges: Community Colleges, 2022, http://www.txhigheredaccountability.org/acctpublic/?goal=#goal27&sector=#twoYearCC&instId=390.
5. Texas Higher Education Accountability System, Texas State Technical College, 2022, http://www.txhigheredaccountability.org/acctpublic/?goal=#goal27&sector=twoYearTSTCL&instId=553.
6. Mike Reeser, *The Return-Value Funding Method,* Texas State Technical College, January 2022, https://reportcenter.highered.texas.gov/meeting/advisory-committee-supporting-documents/txcccf-presentation-michael-reeser-jan-18-2022.
7. Texas Higher Education Coordinating Board, *Texas State Technical College System Returned Value Funding Model Methodology*, July 2013, https://reportcenter.highered.texas.gov/reports/data/texas-state-technical-college-system-value-add-formula-methodology.
8. Erin Davis Valdez and Anthony Jones, "Filling in the Gaps: Ensuring Workforce Data Transparency to Improve Training Pathways," Texas Public Policy Foundation, November 5, 2021, https://www.texaspolicy.com/filling-in-the-gaps-ensuring-workforce-data-transparency-to-improve-training-pathways.
9. Texas State Technical College, "Payment Information 2021–2022," https://www.tstc.edu/admissions/tuition/#MBG.
10. Tex. Educ. Code § 130 (1987).