

# THE EVOLVING RELATIONSHIP: Public Institutions and Their States

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Public higher education institutions and states have found themselves in a quandary in recent years. State budgets are stressed in accommodating the demands of financing elementary and secondary education and the rising costs of Medicaid while demand for public higher education continues to increase with no signs of slowing down.<sup>1</sup> Over the past five years, state investment in public institutions has failed to keep pace with rising inflation and skyrocketing enrollments at public colleges and universities. Between fiscal years 2001 and 2006, enrollment at public institutions increased by 14.8 percent while state and local support per student fell 14.2 percent over the same time period. Over the course of those five years, public higher education appropriations per full-time equivalent (FTE) student declined in 43 out of 50 states.<sup>2</sup> In response, many public institutions have been seeking to grow their existing funding sources or find new revenue streams, and are beginning to look more like their independent counterparts.

In recent years, policymakers, the higher education community, and the media have placed considerable attention on understanding the changing relationship between public universities and their states, the causes and consequences of this transformation, and its effects on students and families. In just the past year, a significant number of books and articles have been published by higher education researchers on the “de facto privatization” of public universities.<sup>3</sup> In addition, the American Council on Education’s Futures Project convened roundtables on the subject, and both national and trade media have devoted columns and entire issues to raising awareness. In some states, such as Colorado and Virginia, awareness has translated into action on legislation to grant public institutions more autonomy.<sup>4</sup>

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1 Nationally, demand for higher education is projected to increase. From 2004 to 2015, the U.S. Department of Education projects total enrollment in degree-granting institutions to increase 13 percent, reaching 19.5 million students. However, the level of growth is projected to vary among states. According to the Western Interstate Commission for Higher Education’s 2003 report, “*Knocking at the College Door: 1998 to 2018*,” states in the southwest and southeast are expected to experience considerable growth while some states are forecasted to experience enrollment losses.

2 State Higher Education Executive Officers (SHEEO). 2007. *State Higher Education Finance FY 2006*. Every state experienced enrollment growth over the five-year time period.

3 See Priest, Douglas M. and Edward P. St. John, eds. 2006. *Privatization and Public Universities*. Bloomington and Indianapolis: Indiana University Press. Lyall, Katherine C. and Kathleen R. Sell. 2006. *The True Genius of America at Risk: Are We Losing Our Public Universities to De Facto Privatization?* American Council on Education/Praeger Series on Higher Education.

4 American Council on Education. 2005. *Peering Around the Bend: The Leadership Challenges of Privatization, Accountability, and Market-based State Policy*. The Futures Project.



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In an effort to gain a more in-depth understanding of the varied relationships between public universities and states, NACUBO—with assistance from its research universities council—surveyed the 102 public flagship universities in May 2006. The online survey specifically sought to gauge the level of autonomy these research universities have with respect to academic, fiscal, and administrative issues compared to a decade ago, as well as how many institutions recently had legislation approved aimed at increasing their institution's fiscal or managerial autonomy.

Surveys were submitted by 59 institutions, representing 40 states for a response rate of 58 percent. Two thirds of respondents represented large institutions with FTE student enrollments of 20,000 or more in fall 2005 (see *Table 1*). Seventy-one percent of institutions indicated that less than 30 percent of their FY2006 current fund revenue was from state tax dollars, with four institutions indicating that less than 10 percent of their current fund revenue came from state tax dollars.

**TABLE 1: Profile of Responding Institutions**

| <b>Distribution of Fall 2005 Full-Time Equivalent (FTE) Student Enrollment of Participating Institutions</b> |                |          |
|--|----------------|----------|
|  | <b>Percent</b> | <b>N</b> |
| 5,000–less than 10,000   | 5%             | 3        |
| 10,000–less than 20,000  | 29%            | 17       |
| 20,000 or greater  | 66%            | 39       |

| <b>Distribution of Fiscal Year 2006 Current Fund Revenue of Participating Institutions</b> |                |          |
|--|----------------|----------|
|  | <b>Percent</b> | <b>N</b> |
| Less than \$500 million  | 31%            | 18       |
| \$500 million–less than \$1 billion  | 39%            | 23       |
| \$1 billion–less than \$1.5 billion  | 12%            | 7        |
| \$1.5 billion or greater   | 19%            | 11       |

| <b>Distribution of the Percentage of Fiscal Year 2006 Current Fund Revenue from State Tax Dollars of Participating Institutions</b> |                |          |
|---|----------------|----------|
|   | <b>Percent</b> | <b>N</b> |
| Zero  | 0%             | 0        |
| Greater than 0, but less than 10%   | 7%             | 4        |
| 10%–less than 15%   | 17%            | 10       |
| 15%–less than 20%   | 9%             | 5        |
| 20%–less than 25%   | 10%            | 6        |
| 25%–less than 30%   | 29%            | 17       |
| 30%–less than 40%   | 25%            | 15       |
| 40%–less than 50%   | 3%             | 2        |
| 50%–100%  | 0%             | 0        |

\* Percentages may not equal to 100 due to rounding



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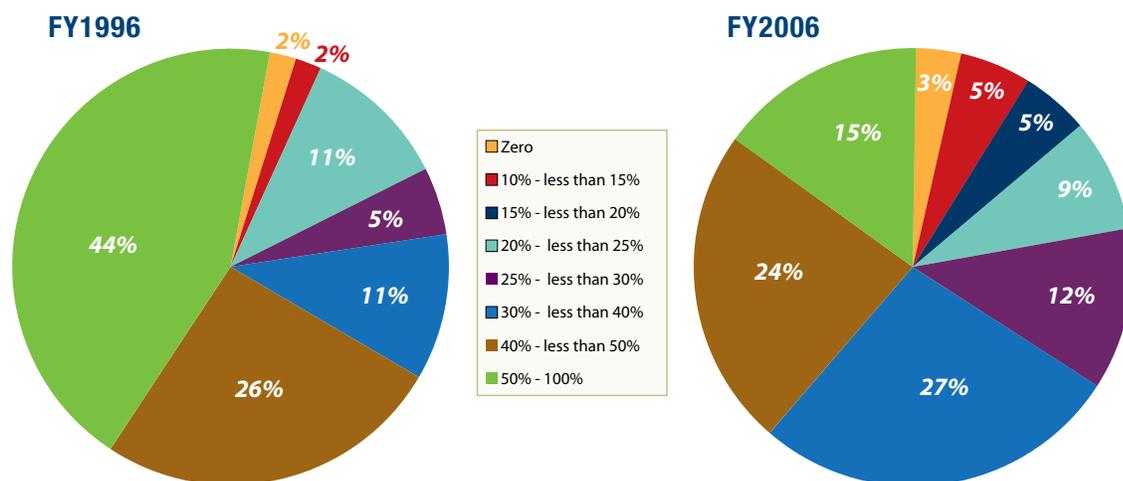
## Budgets: Today vs. Yesterday

The percentage of unrestricted operating budgets funded from state tax dollars has declined over the past 10 years (FY1996 to FY2006) on average, according to survey respondents (see *Table 2*). In FY1996, 44 percent of institutions reported that state tax dollars accounted for between 50 to 100 percent of their unrestricted operating budget. A decade later, this number drops to 15 percent. Not one institution reported an increase in the percentage of their operating budget supported by the state over the 10-year period.<sup>5</sup> Seventy-one percent of institutions reported a decline in state tax dollars as a percentage of their unrestricted operating budget over the decade while a quarter reported no change in support. It is important to note that the NACUBO survey did not explore the direct cause of the decline and therefore cannot answer whether it is due to a decline in dollars appropriated to these institutions or whether operating budgets are

increasing at a faster rate due to needs for increased institutional spending, or a combination of these two factors.

Regardless of the reasons for the decline, as the proportion of unrestricted operating budgets derived from state tax dollars decreased over the past 10 years, the percentage of operating budgets funded from tuition and fees, annual gifts, and endowment income increased for many institutions (see *Table 3*). Ninety percent of respondents indicated that the percentage of their unrestricted operating budget supported by tuition and fees increased over the past 10 years, and 86 percent indicated that it had increased over the course of just two years (FY2004 to FY2006). Over the past decade, 60 percent and 51 percent of respondents reported increases in the percentage of their budgets resulting from annual gifts and endowment income, respectively.

**TABLE 2: Distribution of the Percentage of Unrestricted Operating Budgets Supported by State Tax Dollars: FY1996 and FY2006**



*Note: No respondents indicated that greater than zero, but less than 10 percent of their unrestricted operating budget was supported by state tax dollars in either FY1996 or FY2006. No respondents indicated that 10 percent to less than 15 percent of their unrestricted operating budget was supported by state tax dollars in FY1996.*

<sup>5</sup> Two institutions (3 percent) did not provide the percentage of their institution's operating budget supported by the state in FY1996; therefore, NACUBO was unable to determine whether their institution experienced a decline, no change, or increase in the percentage of support over the decade.



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**TABLE 3: Changes in the Percentage of Unrestricted Operating Budgets and Spending Provided by States at Responding Institutions**

|  | 10 Years         |                           |           | 2 Years          |                           |           |
|--|------------------|---------------------------|-----------|------------------|---------------------------|-----------|
|  | FY1996 to FY2006 |                           |           | FY2004 to FY2006 |                           |           |
|  | Declined         | Remained approx. the same | Increased | Declined         | Remained approx. the same | Increased |
| The percentage of your unrestricted operating budget (excluding auxiliary, restricted, or plant funds) coming from tuition and fees has: | 7%               | 3%                        | 90%       | 3%               | 10%                       | 86%       |
| The percentage of your unrestricted operating budget (excluding auxiliary, restricted, or plant funds) coming from annual gifts has:     | 11%              | 30%                       | 60%       | 10%              | 45%                       | 45%       |
| The percentage of your unrestricted operating budget (excluding auxiliary, restricted, or plant funds) coming from endowment income has: | 4%               | 46%                       | 51%       | 4%               | 57%                       | 39%       |
| The percentage of your spending on capital projects that is provided by the state has:   | 42%              | 25%                       | 33%       | 28%              | 38%                       | 35%       |
| The percentage of your spending on deferred maintenance that is provided by the state has:   | 49%              | 32%                       | 19%       | 36%              | 41%                       | 22%       |
| The percentage of your spending on debt service that is provided by the state has:   | 25%              | 58%                       | 18%       | 24%              | 71%                       | 5%        |



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## *Who's In Control?*

As states and public institutions continue to redefine their relationship, NACUBO was particularly interested in the level of autonomy afforded to institutions from the state in the following areas—academic, fiscal, and administrative—and if that level of autonomy has changed from a decade ago.

Responding institutions indicated a high level of institutional control for the majority of surveyed academic, fiscal, and administrative areas, with exception in the administrative areas of risk management/insurance programs, capital construction project approval, and employee benefits packages where more variation was found (see *Table 4*). Two thirds or more of responding institutions reported that their institutional level of control had not changed over the past decade in every area, with the exception of procurement.

In **academic** areas, the majority of institutions reported having “full” or “significant” control in both the elimination and creation of academic programs and determination of student enrollment size. Respondents also indicated a high level of institutional control over **fiscal** issues. For example, institutions reported a high level of control over budget flexibility and tuition and other revenue collections, with 86 percent and 85 percent indicating “full” or “significant” institutional control, respectively. More than three quarters

(77 percent) reported that they currently have “full” or “significant” control over procurement. However, the trend in procurement over the last 10 years is unclear as 21 percent of responding institutions reported greater control over the area of procurement a decade ago, half reported that the control had not changed, and 22 percent indicated that their institution had less control 10 years ago.

In **administrative** areas, such as control of risk management/insurance programs or employee benefits packages, institutional control varies, but the level of control has remained relatively the same compared to 10 years ago. For example, a third of respondents indicated “minimal” or “no” institutional control in the area of risk management/insurance programs while a third indicated that they had full control. Only 10 percent of institutions reported that they had less control in this area a decade ago while more than three quarters indicated that their control is the same as it was 10 years ago. Similarly, 38 percent of respondents reported “minimal” or “no” institutional control over employee benefits packages while over half indicated that they had “significant” or “full” control in this area. Almost 40 percent of institutions reported equal control with the state on capital construction project approval while only 12 percent indicated full control in that area.



**TABLE 4: Level of Institutional Control: Today vs. 10 Years Ago**

| <b>ACADEMIC</b>   |                                      |                          |               |   |   |   |        |
|---|--------------------------------------|--------------------------|---------------|---|---|---|--------|
|   | <b>CURRENT INSTITUTIONAL CONTROL</b> |                          |               | <b>INSTITUTIONAL CONTROL 10 YEARS AGO COMPARED TO TODAY</b> |   |   |        |
|   | Full or Significant                  | Equal Control with State | Minimal or No | Greater Institutional Control 10 Years Ago                  | Same Institutional Control 10 Years Ago | Less Institutional Control 10 Years Ago | Unsure |
| Creation of New Academic Programs                             | 81%                                  | 14%                      | 5%            | 3%  | 86%                                     | 5%                                      | 5%     |
| Elimination of Academic Programs                              | 90%                                  | 9%                       | 2%            | 3%  | 88%                                     | 3%                                      | 5%     |
| Determination of Student Enrollment Size                      | 90%                                  | 10%                      | 0%            | 3%  | 86%                                     | 5%                                      | 5%     |
| <b>ADMINISTRATIVE</b>   |                                      |                          |               |   |   |   |        |
|   | <b>CURRENT INSTITUTIONAL CONTROL</b> |                          |               | <b>INSTITUTIONAL CONTROL 10 YEARS AGO COMPARED TO TODAY</b> |   |   |        |
|   | Full or Significant                  | Equal Control with State | Minimal or No | Greater Institutional Control 10 Years Ago                  | Same Institutional Control 10 Years Ago | Less Institutional Control 10 Years Ago | Unsure |
| Risk Management/Insurance Programs                            | 55%                                  | 12%                      | 33%           | 7%  | 78%                                     | 10%                                     | 5%     |
| Travel  | 73%                                  | 10%                      | 17%           | 9%  | 74%                                     | 12%                                     | 5%     |
| Motor Pool  | 79%                                  | 7%                       | 14%           | 7%  | 81%                                     | 7%                                      | 5%     |
| Capital Construction Project Approval                         | 42%                                  | 39%                      | 19%           | 10%   | 72%                                     | 12%                                     | 5%     |
| Faculty and Staff Full-Time Equivalent (FTE) Position Control | 88%                                  | 5%                       | 7%            | 7%  | 81%                                     | 7%                                      | 5%     |
| Employee Benefits Packages                                    | 52%                                  | 10%                      | 38%           | 3%  | 85%                                     | 7%                                      | 5%     |
| Information Technology Systems                                | 93%                                  | 5%                       | 2%            | 3%  | 83%                                     | 9%                                      | 5%     |
| <b>FISCAL</b>   |                                      |                          |               |   |   |   |        |
|   | <b>CURRENT INSTITUTIONAL CONTROL</b> |                          |               | <b>INSTITUTIONAL CONTROL 10 YEARS AGO COMPARED TO TODAY</b> |   |   |        |
|   | Full or Significant                  | Equal Control with State | Minimal or No | Greater Institutional Control 10 Years Ago                  | Same Institutional Control 10 Years Ago | Less Institutional Control 10 Years Ago | Unsure |
| Procurement   | 77%                                  | 18%                      | 5%            | 21%   | 53%                                     | 22%                                     | 3%     |
| Budget Flexibility  | 86%                                  | 7%                       | 7%            | 16%   | 66%                                     | 16%                                     | 3%     |
| Treasury Services   | 72%                                  | 10%                      | 17%           | 10%   | 79%                                     | 7%                                      | 3%     |
| Debt Issuance   | 67%                                  | 18%                      | 16%           | 3%  | 81%                                     | 10%                                     | 5%     |
| Resident Tuition Rate Setting                                 | 71%                                  | 10%                      | 19%           | 12%   | 74%                                     | 12%                                     | 2%     |
| Tuition and Other Revenue Collections                         | 85%                                  | 12%                      | 3%            | 5%  | 79%                                     | 10%                                     | 5%     |

Note: Survey respondents were asked to rate their current level of institutional control by the following levels: Full Institutional Control, Significant Institutional Control, Equal Control with State, Minimal Institutional Control, and No Institutional Control. Percentages for Full Institutional Control and Significant Institutional Control have been combined in this graphic as well as the percentages for Minimal Institutional Control and No Institutional Control.

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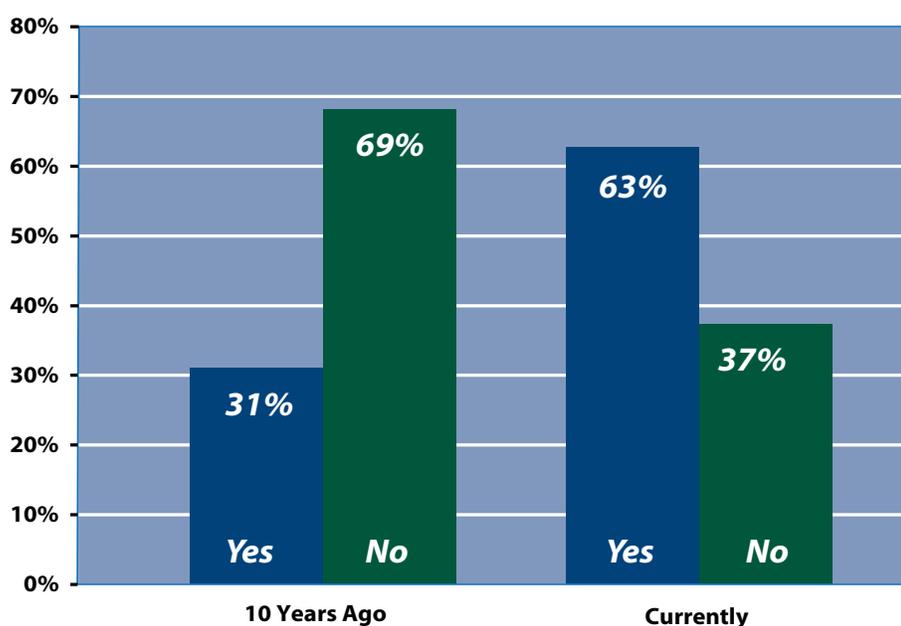
While state support as a percentage of operating budgets has declined, accountability requirements from the state and other stakeholders is rising (see Table 5). Ten years ago, approximately one third of responding institutions were required to formally report to the state on performance metrics. In contrast, currently, more than 60 percent are required to do so. Twenty of the institutions surveyed must now report to their states but were not required to do so 10 years ago. Only five institutions reported incurring financial penalties for failure to perform on state metrics.

Some participants are partnering with private entities to handle functions previously supported by the state. In order to respond to changes in revenue streams, approximately a third of institutions have partnered with private entities or created 501(c)(3)s. Of those, more than half indicated “housing” as the function handled by these partnerships in order to meet rising enrollment demands in the most timely manner. Other reasons for partnerships or new 501(c)(3)s include food services, debt issuance, and fundraising or investment management purposes.

## Future Directions

State appropriations for public higher education increased in almost all 50 states in fiscal year 2007, according to the annual “Grapevine” study conducted by the Center for the Study of Education Policy at Illinois State University. Total general-fund appropriations for the 2006-07 fiscal year rose by 7 percent from the previous year to \$72.2 billion. However, the rise of state appropriations over two consecutive years needs to be considered within the context of states recovering from appropriation declines between 2002 and 2005. On average, from FY2002 to FY2007, state appropriations increased 2.9 percent across the states, with six states experiencing a percentage decrease in appropriations over this five-year period. Only two states experienced a double-digit percent increase over this same time period. Though the FY2007 data showed an increase in support from FY2006, when projected enrollments and continued inflation are considered, it follows that many survey respondents indicate they are preparing for a different future.

**TABLE 5: Responding Institutions Required to Report to State on Accountability/Performance Metrics**



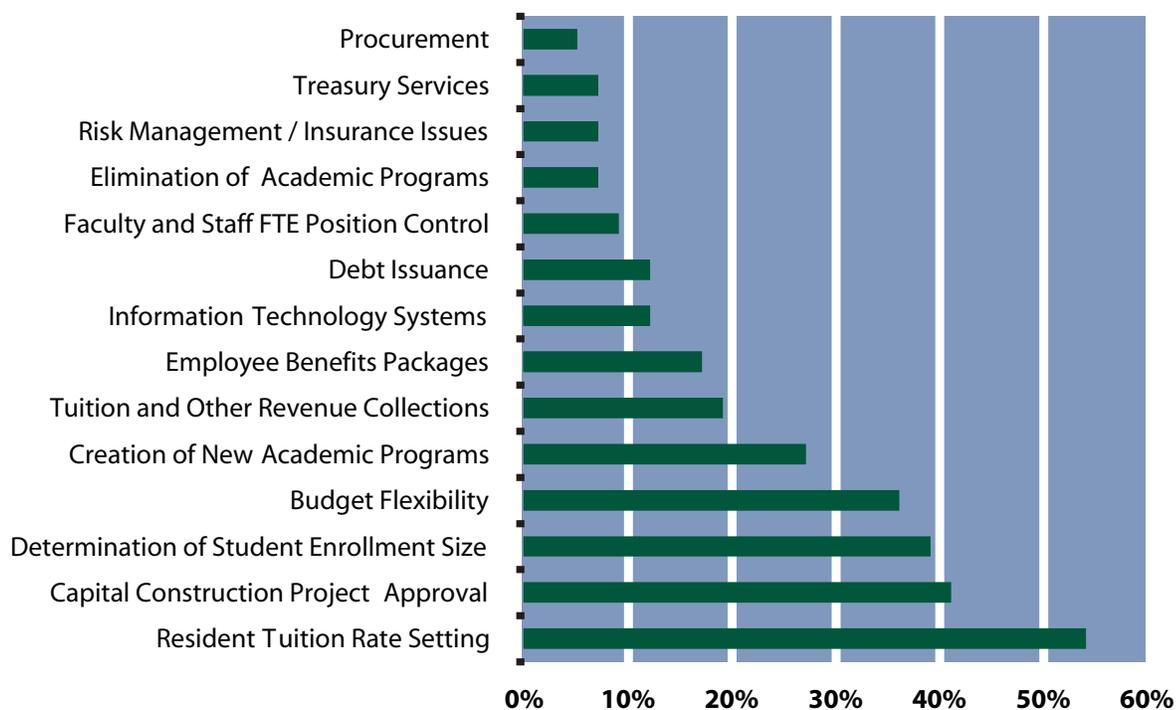
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For example, when asked to identify the three issues most critical to their institution's future success, responding institutions reported having control over setting tuition for in-state students as most critical; 18 institutions ranked "resident tuition rate setting" as the most critical with 32 institutions ranking this in their top three control areas (see Table 6). Possibly anticipating accommodating an even larger, more diverse, future student body, control over "capital construction project approval" and "determination of student enrollment size" received the second and third highest overall number of votes.

An overwhelming number of respondents believe their institution is headed for greater fiscal and managerial autonomy from their

respective states. Approximately 90 percent of responding public flagship research institutions indicated that their future financial strategy would aim for greater fiscal and/or managerial autonomy from the state in the next five years. In just the past five years, 16 institutions reported that legislation was approved in their state aimed at increasing their institution's fiscal or managerial autonomy; nine institutions reported that legislation was approved in their state to increase both their institutions' fiscal and managerial autonomy. As many business officers anticipate a more autonomous future, two questions remain: Will their institution's relationship with the state continue to evolve? How can the business office best prepare?

**TABLE 6: Ranking of Institutional Control Areas Critical to Future Success of Responding Institutions**



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