

UNDERSTANDING HIGHER EDUCATION FINANCE

INTERVIEW WITH SHERMAN DORN
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As part of a project on higher education finance supported by the Bill and Melinda Gates Foundation, Nate Johnson interviewed a number of experts and leaders to gather different perspectives on how major budget choices are made. The interviews have been condensed for publication so that the key insights are available to anyone who is interested.

This interview with Arizona-based Sherman Dorn, author of Accountability Frankenstein (2007), addresses the cyclical nature of higher education demand, declining state funding, the tendency to cut budgets and raise tuition during bad economic times, and mobilizing alumni networks for state funding support.

Given that states cannot deficit spend, what are the ways that states can try to work with the countercyclical nature of higher education demand where enrollment—student demand—goes up just when the state has less money to support expansion in higher education?

I think it depends on whether or not the construct of an individual state budget divides capital from operational expenditures. I do not know state budget structures nearly well enough to know where in a state capital expenditures work in that way. In some states, as in Florida, it's done on a cash basis when there's state funding. Universities have to accumulate all the cash on the project often over multiple years in order to start construction. That often dominates capital expenditure politics in higher ed. in Florida.

In other cases, it can be done off of credit, and then the question is in terms of the total—especially in good years if you start doing debt-financed projects—what's the state credit like Kansas or Illinois at the moment? In what states is there a cap on state debt or public debt? That's a background structure that probably is dependent. What is the ratio of capital budgets to operational budgets in public higher ed. in general? I'm not sure that would really save you that much.

The institutions that have figured out how to survive the last 10 years have often started with a diversified funding base. Michigan is probably the most prominent one, where I think they started the last recession with under 10% of their operational budget coming from the state. Arizona's public funding of universities, and we're not even talking about the community colleges here, dropped fairly precipitously. Part of the background is how much universities have tried to move away already from a dependency on state budgeting. The political dilemma here is severe. University presidents and other higher ed. leaders get almost nowhere by complaining about declining state funding.

It's the tuition increases that get public attention, and people don't often connect those directly to the declines in state funding that are usually the primary cause.

Right, and there's some debates about that. Certainly, for regional state university campuses and community colleges, there's a direct relationship. For public universities, there's a little bit more of a debate on that. If your budget is cut, are you a good shepherd and do your best by graduating students and continuing research and serving the public of your state? Inevitably, the answer pretty much has to be yes. If you are successful as an institution with lower-based funding from the state then state politicians will go, oh, I guess you didn't need our money anyway, so this is a catch-22.

Institution leaders who transition across a state budget crisis and continue later on, especially, they have to figure out how to make the case for additional state investment when the institution appears to be doing fairly well. You're certainly not going to claim that you're doing an awful job as an institutional leader with fewer state dollars. You have to explain, and you have to figure out a strategy. If you were doing so well as an institution with fewer state dollars, why should the state need to give you more?

That is, going forward, the fundamental dilemma. The tuition is part of it, but I think that's a slightly different landmine.

The risk in higher education is that whether you're at Yale or at a community college, your students aren't average or typical because students are so distributed across different types of institutions that the system as a whole doesn't look like any one given institution.

This may be my particular experience, but for 20 years I've been at public colleges of education and public research universities where the majority of our undergraduates are transfers generally from community colleges. That is a fundamental reality, especially when I was teaching undergraduates in Florida where I desperately needed the transfer students who were over 25 in order to make my class operate the best that I could. I needed undergraduates with some life experience. That plus the fact that my faculty union in Florida included chapters from research universities and community colleges that made it almost impossible if you were paying attention to care only about the public research university side.

How can community colleges work with the cyclical nature of demand and the tendency to cut budgets and have pressure to raise tuition during bad economic times?

That's probably an essential piece of this. There are probably a couple of different ways to think about this, and it really depends on the politics of an individual state. Rainy day funds is a fairly serious problem because as you see in states, no matter what the political orientation is, the temptation when you have a statewide surplus is to use it for tax cuts or for other giveaways that both not only erode the assets that are saved in a rainy day fund but, in the case of tax cuts or tax credits, permanently erode the tax space. When a recession hits, it's a whammy in terms of the asset base as well as the taxable base as well as the actual economic woes.

if I were in the state legislature, I would propose the equivalent of a rainy-day fund but for dedicated purposes, especially for community colleges because of the countercyclical enrollment pattern in them. The key question is: How do you pitch it? How do you sell a trust fund that cannot be tapped into except by community colleges and except when enrollment is rising as the result of a recession? Because if you start sinking funds into it, it suddenly becomes a target. The only way that I can think of to do this is to tie such a trust fund to a bond issue, so that it becomes bonded revenue, and then it becomes much harder to do that. This would be something like a reverse sinking fund—or just call it enrollment increase sinking fund—and tie a bond to it.

I don't know how you would do it, or what the bond would be for, but in essence create a revenue stream from the state in good times that could be drawn on not only for a bond, so you'd have to be very careful; only a portion of the revenue could be tied to bonded revenue. The majority of the fund could be tapped by community colleges with a certain amount of increasing enrollment and maybe tied to some state economic indicator, like the state's unemployment rate or the state's trends in unemployment claims.

There are two tricks about it. One is, how do you pitch it politically in good times and argue that this should be a first call for dollars above state research universities or on par with state research universities? Then, how do you prevent it from being eroded or seen as an asset that can be raided by a state legislature when the fund looks pretty large? I don't know how to do that. That's the key thing. Assets have to be squirreled away in a way that is both politically viable and that doesn't become a target of a raid between when it's set up and when it's needed.

I don't know of any community college with a budget surplus right now. If there were, and certainly for the rare public university that can do this, to sink some funds into assets that are not held by the publicly controlled entity but, rather, by the affiliated entity would in essence be a self-funded sinking fund.

If you are talking about the institution budget, the president will call up legislators, mobilize alumni networks to increase or protect the institutional budget. There's just not the same kind of political clout around students in the same way.

Part of this is just the reality of the political pull, in most states, of public research universities, especially flagships. It's the path dependency. Probably at least a significant plurality of states has large numbers of state legislators who are alumni of and therefore beholden to the states' public universities. It would be interesting to see if there are any states where a large minority came through community colleges in the state. Actually, I suspect that might be an interesting political strategy if anybody could create a caucus of community college alumni in a state legislature.

Those sort of built-in constituencies as a de facto political strategy can maintain programs for a very long time, so it's not enough to boost budgets for entire institutions or sectors usually. It really can create interesting consequences years down the line.

What have you learned since moving to Arizona?

The zeroing out of budgets for Maricopa and Pima County community colleges was the major surprise. Coming from a state where the community colleges actually had a somewhat larger political pull than in some other states, to move to Arizona where obviously they did not have enough pull to protect a statewide budgeting. Now in Arizona, community colleges are also supported by property taxes unlike in Florida, but that was one of the surprises since coming here.

The second surprise is direct management of higher education by the legislature. I don't know to what extent that's because more than 60% of the population is in Maricopa County, and there are only three public research universities, or to what extent the longest serving university president, Michael Crow, and the Arizona Board of Regents have persuaded the legislature that they don't need to do direct management of universities. I have been quite pleased that, at least thus far, some of the things that I saw in Florida I haven't seen here in Arizona in terms of those attempts.

Sherman Dorn previously taught at the University of South Florida, Vanderbilt University, and the University of Delaware.