Research

Showing Up is Not Enough: Performance-Based Funding in Federal Education Policy

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INTRODUCTION

Nearly all public education funding is driven by how many and what type of students show up on so-called 'count days.' In other words, funding is determined by student attendance rather than outcomes and results. This unquestioned practice of funding schools based almost exclusively on attendance misaligns incentives, rewards sub-par performance, and diminishes the imperative for significant and sustained educational outcomes. The value of opportunities provided to students must consider equity of student outcomes – not just tax dollars allocated to education systems. Disruption is needed, for simply providing funding to schools does not produce results; however, providing funding to schools that produce results is game-changing.

Government budgets pay for inputs rather than producing outcomes. It has been almost impossible to redirect scarce public resources based on the comparative performance of different schools, or to stop spending money on programs that don't produce results. As Eric Hanushek and Alfred Lindseth wrote, "Questions as to whether or how to change existing ways of doing things to make education dollars more effective are rarely addressed." [1]

Our education system is not sustainable at its present level of productivity. The more than $600 billion U.S. taxpayers spend every year on public elementary and secondary education equates to at least 5.4 percent of the nation's GDP.[2] Globally, according to George Mason University's Mercatus Center, U.S. spending per pupil is second highest among the 34 member countries of the Organization for Economic Cooperation and Development (OECD). Yet, U.S. student performance on the OECD's Program for International Student Assessment (PISA) was 17thin reading, 20th in science and 27th in mathematics.[3]

Fortunately, however, there has recently been a greater focus among the states on measurable academic results to drive school funding. As Michigan Governor Rick Snyder wrote, "school funding should be based upon academic growth and not just whether a student enrolls and sits at a desk."[4] Michigan and other states are implementing Performance-Based Funding (PBF), which seeks to better align funding for schools based on improved performance of schools individually and systemically.

PBF provides an opportunity to make strategic investments in schools by focusing school funding on desired results. This paper examines the potential of performance-based funding at the federal level.

LABORATORIES OF INNOVATION: PBF IN THE STATES

There is an emerging bipartisan consensus that it is no longer acceptable to throw good money after bad on ineffective government programs, because special interests manipulate government budgets to protect their interests regardless of actual results.

PBF models are being implemented by some states in the context of higher education, as well as career and technical education. Additionally, some states are utilizing PBF as a funding mechanism in elementary and secondary education. Arizona began a statewide PBF program in 2013, called "Student Success Funding," which expanded in 2014.[5] Arizona Governor Doug Ducey is leveraging these past efforts with a new approach using an achievement school district model.[6] Michigan has been implementing a PBF model since 2012.[7] Pennsylvania took a slightly different approach, providing funding flexibility in exchange for performance based outcomes.[8] Florida, Wisconsin, and Oregon have all recently began exploring PBF. In each case, the amounts of funding are modest, but the potential impact promises to be significant.

Colorado is the latest state to join the PBF movement. Colorado Governor John Hickenlooper signed into law a bill based on the Social Impact Bond approach, which is a variation on the notion of paying for success (i.e., PBF). The Colorado law enables the state to partner with service providers and private sector investors or philanthropists to fund and provide interventions in order to increase economic opportunity, support healthy futures, and promote child and youth development. [9] While the Colorado approach is different than other state approaches, it focuses on fundamentally altering the delivery of funding to one based on results.

These state initiatives ensure education funding is focused on key outcomes, experimentation with different interventions to produce results, and systemization of continuous improvement.

PBF DESIGN PRINCIPLES

While states are leading the way in adopting PBF strategies, it should be considered for federal education funding as well. When doing so, lawmakers need to consider key design principles that would apply to any PBF approach at the federal level.

Measuring Academic Achievement

To ensure there is no disincentive for schools to serve the students who need them most, a PBF model measuring student progress must account for student performance growth, which acts as a counter-weight to a sole focus on absolute performance, thereby equally including students who are significantly behind. By looking at growth longitudinally, there is further protection against penalizing schools who serve high(er) numbers of struggling students.

The vast majority of weight in a PBF model should be given to measurable, academic metrics and less weight to non-academic factors. In addition, consideration and potential weight could be part of mission-specific goals for schools that are focused on a particular student population or academic area.[10]

Funding Subject to PBF

Another key principle to consider is the amount of funding subject to performance consideration. Significant improvements to incentives and academic performance can be made with even small changes to the funding structure. Any PBF model that encompasses all – or significantly more than 10 percent – of a district or school's funding would put that institution in serious jeopardy of not being able to operate, either because there is not sufficient cash flow to cover ongoing costs or because budget planning would be so contingent as to render resource allocations impossible. An effective PBF model still relies on fixed operating costs being borne by existing funding streams, but variable costs become subject to meeting performance targets on defined metrics. [11]

For example, both Michi-gan and Arizona have included a relatively small amount of funding in their PBF models. In Michigan, every school is potentially eligible for up to $100 per pupil in PBF. [12] In Arizona, under the previous Student Success Formula, the maximum per-pupil achievement payment would be $500. In addition to achievement pay-ments, the maximum per-pupil improvement payment would also be $500, for a total of $1,000 per student.[13]

PBF IN THE ELEMENTARY AND SECONDARY EDUCATION ACT

While the non-financial policy of the Elementary and Secondary Education Act (ESEA) has been radically overhauled since the law's inception, there has not been a similar focus on the equally important financial policy in the ESEA. Title I of the ESEA is the single largest K-12 investment that the federal government makes. At the heart of the Title I is a bargain: a significant investment of federal dollars for students in poverty coupled with a demand for significantly improved outcomes for those students.

There are a number of ways to incorporate PBF into the ESEA – especially Title I – and the following examples are a few of the different options Congress could take toward a truly revolutionary reauthorization.

Title I Funding Formulas

While there have been changes on the margins of Title I formulas, there has not been a comprehensive rethinking of how federal funding is provided to states, districts, and schools. This is a significant missed opportunity given that Title I provides supplemental education funding to nearly 24 million students in more than half of all public schools, including 68 percent of elementary schools.[14] With serious efforts to reauthorize the ESEA underway, now is the time to systemically reform how Title I dollars are allocated.

Currently, Title I funds go to states and districts based on four separate formulas: the Basic, Concentration, Targeted, and Education Finance Incentive Grant formulas. Once these funds reach districts, they are combined into one funding allocation to be used for the same Title I program purposes. All four formulas focus on the number and/or percentage of students in poverty. The four Title I formulas are overly complicated and fundamentally flawed. They are the result of political compromise and outdated thinking, and do not take into account any consideration of actual performance.

Providing additional resources does not necessarily result in student success; moving from inputs to outputs by focusing on measureable achievement has characterized the modern era of education reform. And while the No Child Left Behind Act moved in this direction with its non-fiscal policy changes, it left the job unfinished by failing to factor achievement results into the Title I formulas.

While some have suggested various tweaks to the Title I formulas, they all miss the basic point that funding should contain a performance component. As policymakers consider reauthorization of the ESEA, incorporating PBF into Title I could deliver long-term, positive results. The most fundamental way to achieve performance-based funding in Title I of the ESEA would be to consolidate the four Title I formulas into two funding streams: one that provides the vast majority of funding based on students in poverty and one that rewards performance.

Impact of Title I Formula Changes

Simplifying the Title I formulas would create greater transparency and offer better accountability for federal funding. Title I could be far simpler by giving states the ability to distribute Title I funds to districts through per-pupil allocations based on the actual number of poor students they serve. This approach is simple, easy to understand, and consistent with the movement to personalize education. Personalizing the Title I formulas by ensuring that every student in poverty is counted and receives an equitable share of Title I funding will create a "student-centered" funding formula that isn't subject to progressive's notions about what constitutes an appropriate concentration of funding to drive Title I funding.

The second formula would then incorporate PBF, and could potentially offset some of the funding changes under the core, student-centered funding approach by allowing those districts to recoup funding by outperforming other districts in the state.

The recommendation is that not less than 90 percent of Title I funding be distributed through the student-centered formula already present in the current structure. To provide an initial view of the impact of such a change, we used data analyses by the Education Trust[xv] and Center for American Progress.[16] [17] This student-centered formula can be illustrated with the following table, which shows the total gain or loss to districts in a particular state, by district child poverty rate:

TABLE 1. ESTIMATED CHANGE IN TITLE I ALLOCATIONS DUE TO STUDENT-CENTERED TITLE I FORMULA

Gain or Loss to Districts by District Poverty Rate			
	<15%	15 – 30%	>30%
Colorado	$8,413,174	($7,611,341)	($801,833)
Louisiana	($80,304)	$6,809,941	($6,729,635)

Source: Center for American Progress

Then, up to 10 percent of the remaining Title I funds could be distributed using a performance component. The impact of building in this second performance-based formula can be illustrated by adjusting the examples from above for the change in distribution of funds. Specifically, incorporating PBF in this way would result in smaller funding increases for districts gaining under the student-centered funding approach and bigger deficits for districts decreasing under the student-centered formula (i.e., in Colorado, the districts with greater than 30 percent poverty would have 10 percent less available, or approximately $80 thousand fewer Title I funds).

TABLE 2. ESTIMATED CHANGE IN TITLE I ALLOCATIONS DUE TO STUDENT-CENTERED AND PBF TITLE I FORMULAS

Gain or Loss to Districts by District Poverty Rate				
	<15%	15 – 30%	>30%	PBF $ Available (10% of Title I)
Colorado	$7,571,856	($8,372,475)	($882,016)	$15,245,104
Louisiana	($88,334)	$6,128,947	($7,402,599)	$29,204,762

*Original Table Edited by Authors

As can be seen from this table, the amount of funding available through a PBF Title I formula could potentially offset the reduction in funding to districts from the current formulas to the student-centered model provided the districts show academic improvement.

Regarding what criteria should be used to gauge academic performance, the academic design principle described above is a starting point. Policymakers could allow states to best define the academic performance criteria, only ensuring the criteria are simple, transparent, and focused on academic growth.

Finally, in order to maintain the accountability of this new funding structure, there should be no hold-harmless provisions to soften the impact of this fundamental transformation. If students aren't held harmless when they receive an inferior education, why should districts or schools be held harmless when they provide inferior results? Since the purpose of the funding change is to produce better results by creating the right incentives, those changes have to be allowed to take place.

PBF Title I Reservation/Set-Aside

Another approach to including PBF in the ESEA is by creating a reservation, or set-aside, of Title I funds to allow states like Arizona, which are focusing on expanding or replicating very high performing low-income schools, to have access to some Title I funds to drive performance. Too often, Title I funds go to low performing schools year after year, giving them little pressure to improve. Providing a set-aside is a good option if the goal is to promote a transition to high-performing low-income schools.

As an example, Arizona Governor Ducey's Arizona Public Schools Achievement District initiative expands the impact of excellent schools through their expansion, replication, or a focus on teaching other schools to do what they do, with half of the projects in the district for low-income schools, which is where Title I funding would play a role.[18]

In fact, some Senators are trying to introduce this approach to the ESEA by allowing states to reserve a percentage of Title I funding to be directed toward statewide efforts to expand high performing, low income public district and charter schools. This would allow states like Arizona to give funding to the district and charter school leaders who are producing results.

Alternatively, policymakers could consider amending the current law's Section 1117 of Title I, dealing with school support and recognition. This section contains the seeds of PBF that, with modification, could become a possible solution.

The current Section 1117 allows a state to set-aside a portion of its Title I funding to reward successful schools. This language could be tweaked to become a performance-based approach by requiring funds to be used to reward schools. Second, the statute should be further modified to require a 10 percent set-aside of Title I funds regardless of funding increases (or decreases) year-over-year. Finally, the reward criteria should be aligned with state accountability systems, but should focus on growth in achievement over time, consistent with the design principle articulated above.

While this approach does not address the fundamentally flawed Title I formulas, it could achieve the same purposes.

Impact of PBF Title I Reservation/Set-Aside

Using the 2014 Title I allocation tables from the U.S. Department of Education[19], initial modeling of the potential impact of setting aside 10 percent of state Title I funds under Section 1117 could be significant. For example, by utilizing a state set-aside of 10 percent in Arizona, over $32 million would be available, while in Indiana, almost $26 million would be available to incentivize districts and schools to raise achievement and compete for these performance-based funds.

TABLE 3. ESTIMATED IMPACT OF 10 PERCENT TITLE I PBF SET-ASIDE ON SELECTED STATES

State	FY 2014 Actual Allocation for Districts	10% set-aside for PBF	Revised FY 2014 Title I Allocation for Districts
Arizona	$325,175,411	$32,517,541	$292,657,870
Indiana	$259,897,172	$25,989,717	$233,907,455

To dive deeper, a state could require districts to set-aside 10 percent of their Title I funds for PBF. To illustrate the analysis, district Title I allocations in Arizona and Indiana were modified to model the impact of such a set-aside. At the district level, in Arizona, this set-aside could yield almost $2.6 million in total in Phoenix, while in Indiana, it could provide $1.4 million in Gary and $3.2 million in Indianapolis, if those districts showed significant improvement. These amounts, while modest in the scheme of overall Title I budgets, if made available in a performance-based context, could yield better, faster improvement.

TABLE 4. ESTIMATED IMPACT OF 10 PERCENT TITLE I PBF SET-ASIDE ON SELECTED DISTRICTS

District	FY 2014 Title I Allocation	10% set-aside for PBF	Revised FY 2014 Title I Allocation
Phoenix School District	$25,916,398	$2,591,640	$23,324,758
Gary Community Schools	$14,049,304	$1,404,930	$12,644,374
Indianapolis Public Schools	$32,427,259	$3,242,726	$29,184,533

The bottom line is that a 10 percent Title I set-aside would serve as a major incentivizing force for states, districts and schools to improve performance.

Social Impact Bonds

Another approach to include PBF in the ESEA would be to create a pilot program utilizing Social Impact Bonds (SIBs), similar to Colorado's approach. SIBs are set up to direct public funding to those institutions and programs that are clearly demonstrat-ing their impact through rigorous results, thereby mitigating financial risk to the taxpayer, and providing an effective means for state and local governments to scale up successful innovations.[20] Senators Hatch and Bennett recently introduced legislation to provide for social impact partnerships through the Treasury Department that could serve as a model for the ESEA.[21]

In a typical SIB, the government con-tracts with an entity to provide services. The government only pays the service provider based on the achievement of performance targets. If the service provider fails to achieve the performance target(s), the government does not pay. Payments can increase for performance that exceeds the min-imum, up to a pre-determined maximum. The service provider gets operating funds by raising capital from private commercial or philanthropic investors. These investors have the opportunity to earn both social and financial returns while putting their capital to work in service of society. In short, this approach is a performance-based contract.[22]

The federal government could become a strategic partner with state and local governments in establishing SIB projects. There are a number of different ways the SIB model could be incorporated into the ESEA; for example, the federal government could match state and local funds in a combined funding pool that would only be paid out if a school (or district) met performance targets; the school or district would raise funds from investors to operate. If the school or district met or exceeded its performance targets, the combined government funding pool would then be paid out to the investors.

As the understanding of SIBs develops, it is clear that any Federal effort most allow for flexibility in the structure and funding of SIBs, with state and/or local governments having a key role in determining how the funds are used in projects. For example, tiered performance payments based on degreed of success may be needed for a project to be considered. In other cases, some credit enhancement may allow projects to attract investors that may not be willing to risk so much capital initially.[23]

FIGURE 1. EXAMPLE OF A SOCIAL IMPACT BOND MODEL

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Or, in a more limited fashion, the federal government's contribution to a SIB could be to fund the return on investment payment to the investors, including any performance bonuses for outstanding results.

Incorporating a SIB into the ESEA would truly create a "Race to the Top," unlike the Obama Administration's competitive grant program of the same name, which poured more money into the usual policy approaches and promises of improvement, rather than based on actual evidence of improvement and without significantly changing the underlying fiscal policy.

CONCLUSION

The problem of misaligned incentives is a well-researched topic in numerous fields. It has not been a topic of deep research and reflection in education, where the misalignment between funding and performance is at best a drag on the system and student performance, and at worst a fundamental flaw that ensures our schools will never improve sufficiently for our nation to live up to its founding ideals of equality and opportunity.

PBF is a promising new approach that has the potential to improve results, overcome barriers to social innovation, and encourage investments in cost-effective approaches. It does this by ensuring that public funding goes to those schools that are clearly demonstrat-ing their impact through rigorous outcome-based performance measures and providing an effective launching pad for scaling schools and innovations that produce results.

PBF can provide a new approach to improving academic outcomes outside the traditional reform approaches, while addressing systemic inefficiency.   Nowhere is this more needed than in the antiquated and convoluted Title I funding formulas in the ESEA.

[1] Eric Hanushek and Alfred Lindseth, Hoover Institution, Stanford University, excerpt from Schoolhouses, Courthouses, and Statehouses: Solving the Funding-Achievement Puzzle in America's Public Schools (Princeton University Press, 2009); http://hanushek.stanford.edu/sites/default/files/publications/Hanushek%2BLindseth%202009%20DefiningIdeas.pdf (accessed 2015).