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California's Higher Education Funding Landscape

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Key Takeaways

California's higher education systems are finally starting to see a return to pre-pandemic enrollment growth levels. But the number of college-age students is projected to plateau and then decline in the coming years. And the state is currently facing a multi-year, multi-billion-dollar budget deficit. Both dynamics taken together could make it a challenge to ensure stable funding growth in the near future. To inform future policies, this report examines higher education funding sources, analyzing revenue trends over the past decade, and comparing the state's funding model with other large states. We find:

- Appropriations for higher education are currently relatively stable, representing about 10 percent of the state's General Fund.
- California's higher education funding compares favorably to other states, with higher per-student state appropriations.
- Funding levels and revenue sources vary across the University of California (UC), California State University (CSU), and California Community Colleges (CCC), reflecting the different missions across the postsecondary segments.
- Tuition revenue for four-year institutions has become increasingly important, especially for UC. State support, however, makes up nearly all of the funding for CCC and a substantial portion for CSU.
- Both UC and CSU have recently entered multi-year tuition-increase agreements with the state in exchange for enrollment and student success milestones. Such increases are likely to make it harder for some families to afford college.
- Federal funding supplements core funding, primarily for student financial aid. The $10 billion dollars that California received in pandemic-era relief funding is now exhausted.

Introduction

In 2022, Governor Newsom outlined a plan to invest billions of dollars in the state's higher education system to "deliver a multi-year strategy to advance equity, access, affordability, and success" with the goal of increasing the share of Californians with either a degree or certificate to 70 percent by 2030. Also, in the 2023 state budget, the legislature presented a framework that would expand and simplify eligibility for Cal Grants, the state's financial aid program. To fully implement each of these ambitious goals will require significant and ongoing state investment, which needs a steady and predictable source of revenue.

California's higher education systems are entering an era of fiscal uncertainty as the population of young people is projected to stagnate or decline in the coming decade. As the state looks to turn the page after the pandemic and establish a more stable funding model, significant challenges lie ahead in the near term. The $10 billion in federal relief funding that provided a lifeline for colleges and universities during the pandemic has been exhausted. Tax revenues have declined due to a cooling stock market and tightening federal monetary policy, and the state has a projected multi-billion-dollar budget deficit.

This report begins with a general overview of how higher education funding works in California, and a brief discussion of past revenue trends. Next it discusses the rising trend in tuition reliance, especially for UC. It then outlines the variations in state funding policies and practices between the UC, CSU, and CCC systems, followed by a discussion of federal funding. Next, it adds historical context to explain funding growth trends over the past decade and the impact of differing funding levels on equitable access and success. It then places California's model in a broader context by comparing it to other large states. Finally, it concludes with a look forward and policy recommendations.

How California Funds its Colleges and Universities

Past recessions have shown higher education—the four-year public systems in particular—to be particularly vulnerable to cuts, as the University of California (UC) and California State University (CSU) systems are still considered discretionary in the state budget.[1] Notwithstanding, state funding has grown incrementally in the ten years since the steep cuts made after the Great Recession. Now California's economy has cooled, and the state is facing a multi-year, multi-billion-dollar budget deficit. To facilitate prioritizing higher education investments as the state navigates its budget deficits, policymakers will need to grasp how the systems are funded and what has changed during this recent period of steady growth.

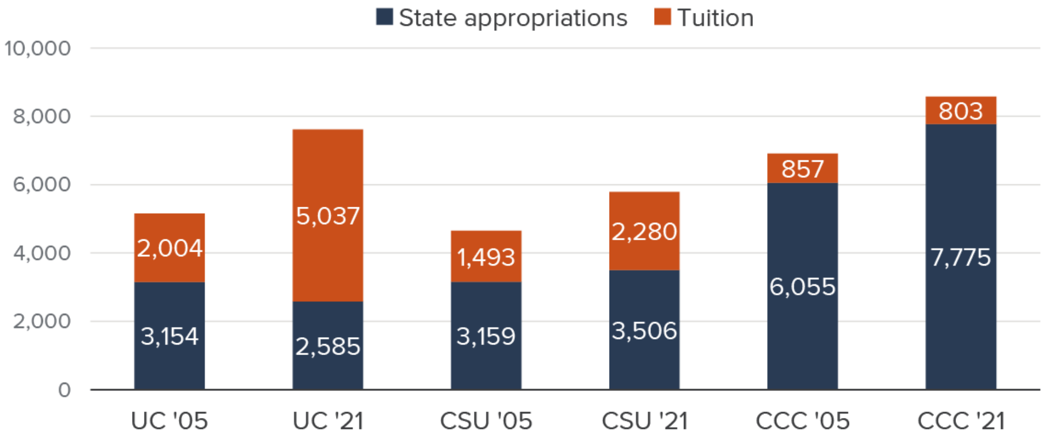
California's public higher education systems are funded primarily from two main sources—state appropriations and student tuition and fees.[2] For the four-year institutions, tuition has grown as a source of revenue over pre-Great Recession levels, particularly at UC. The breakdown varies from system to system. For example, in 2021–22, UC funding comprised two-thirds tuition and one-third state appropriations (Figure 1). At CSU, tuition accounts for half, and at the community college system (CCC) state appropriations make up about 90 percent. CSU and CCC still receive most of their funding from state appropriations, and CCC is less reliant on tuition than it was in 2005.

1. Certain General Fund programs are "protected" from cuts by state statutory requirements—such as Proposition 98 funding for K–12 schools and community colleges—or by federal matching requirements like TANF and other safety net programs. Other areas are also "protected" due to feasibility. For example, cutting funding to correctional institutions is very difficult due to legal requirements.
2. This report is investigating funding for undergraduate education. The full system budgets reflect the institutions' many missions and include other revenue streams to support these activities. This is especially true for UC—only about 11 percent of their total budget funds undergraduate education. UC hospital systems and research labs, for example, are large parts of the total budget but are for the most part self-supporting and do not receive much state funding.

Figure 1

Since 2005, tuition revenue has replaced more state funding for UC than for CSU and CCC

$ in millions



SOURCE: Integrated Postsecondary Education Data System (IPEDS).
NOTE: Nominal $ in millions.

Although the overall amount has increased as the General Fund has grown over time, the *share* of General Fund dollars allocated to higher education—UC, CSU, CCC, and the state's financial aid program (Cal Grants)—has not changed much since the Great Recession, hovering around 10 percent. It was higher in the 1980s and 1990s, at about 16 percent, but increases in funding elsewhere—particularly health care and K–12 schooling—have pulled the budget away from postsecondary education (Table 1).

Table 1

Higher education represents about 10 percent of California's General Fund for 2023–24

State agencies	Percent of General Fund (%)	General Fund allocation (thousands)
K-12 Education	35	$79,294,007
Health and Human Services	33	$73,961,734
Higher Education	10	$22,714,644
Corrections and Rehabilitation	7	$14,749,820
General Government	4	$8,688,981
Natural Resources	4	$7,838,077
Legislative, Judicial, Executive	3	$6,598,387

SOURCE: California Department of Finance.
NOTES: Table shows General Fund allocations for 2023–24, not total state budget. State agencies that make up less than 2 percent of General Fund spending are omitted here for brevity. These include Government Operations (1.8%), Transportation (1.5%), Business, Consumer Services, Housing (1.4%), Labor and Workforce Development (0.4%) and Environmental Protection (0.3%).

Growing Reliance on Tuition Revenue

California's progressive tax structure is closely tied to the stock market—it relies heavily on capital gains revenue. This translates to unpredictability and volatility in state revenues and thus funding for programs. From the institutions' perspective, tuition is a more predictable and thus attractive source of revenue. They can forecast expected revenue at different tuition levels more accurately, and plan for growth beyond the next fiscal year and the next state budget cycle.

This is especially the case for UC, with its intense student demand. Since UC campuses are highly selective and sought after by nonresident and international students, the system can raise tuition without fear of a decline in enrollment. Moreover, the state's Cal Grant financial aid program ensures that over half of UC students pay no tuition, so increases do not add more financial burden for students with lower family incomes.

In exchange for annual state funding increases, neither UC nor CSU have increased tuition since 2013. However, both have recently implemented new long-term plans for annual tuition growth, citing insufficient revenue and the need for the systems and students to have a more predictable tuition policy. In Fall of 2022, UC implemented its Tuition Stability Plan. This plan increased tuition by 2 percent for Fall of 2022, with annual increases by inflation as measured by the California Consumer Price Index. Tuition will be adjusted for each incoming undergraduate class but will subsequently remain flat until the student graduates, for up to six years. In September of 2023, the CSU Board of Trustees approved a tuition increase plan. The CSU plan would increase tuition annually by 6 percent. Unlike under the UC plan, all CSU students will see their tuition increase each year. Though these tuition plans will provide predictable funding to support campus operations, increased enrollment, and financial aid, they will also likely shift more of the cost of college to students and their families.

State Appropriations Policy Differs by System

Proposition 98 determines state funding for the California Community Colleges—by far their primary source (see text box below). In contrast, negotiations in the annual state budget process typically decide appropriations for the four-year university systems. During the 2022 budget process, both the University of California and California State University systems agreed to multi-year compacts that established predictable funding increases in exchange for commitments to make progress on shared goals for increasing student access and success. Both compacts extend to the 2026–27 fiscal year and are supported by annual 5 percent increases in base funding for both systems.

Proposition 98 formulas set state funding levels for k-12 schools and community colleges

Proposition 98—a ballot measure passed in 1988—establishes a minimum funding guarantee for California's community colleges and K–12 schools. School spending levels are meant to ensure that state support at least remains where it was in the late 1980s, but ideally it would grow with the economy and student enrollment. Though the policy appears to guarantee fixed funding shares at both community colleges and K–12 schools, support for the community colleges has fallen short of its 11 percent share[3] in almost every year, with increasing portions of Prop. 98 funds going to K–12 schools (Murphy 2004).

Funding levels are determined by a series of formulas, called tests. The first, Test 1, requires the state to spend the same share of the General Fund on K–12 schools and community colleges as it did in 1986–87. Test 2 funds schools at the prior-year amount with adjustments for changes in enrollment and per capita personal income (PCPI). Test 3 again sets the minimum to the prior-year amount and adjusts for enrollment, but now follows changes in the General Fund rather than PCPI. The state is required to provide the highest amount determined by the three tests, which has typically been Test 2 (Manwaring 2005).

During economic downturns, Test 3 has often been in effect. In particularly hard times, the minimum guarantee can be suspended altogether by a two-thirds vote of the legislature. In either case, deviations from the Test 2 amount—where annual growth is based on enrollment and PCPI—create an obligation for the state to increase school spending when the economy recovers. This "maintenance factor" requires an accelerated increase in the minimum guarantee over time to return funding to the level it would have been if there were no suspension of the guarantee or use of Test 3.

Among a variety of goals tied to improving outcomes like raising graduation rates and closing equity gaps, the compacts also call for 1 percent annual growth in enrollment in both systems. By 2026–27, this amounts to 8,000 more students at UC and 14,000 more at CSU. Additional commitments require that 15 percent of

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3. Additions of various funding priorities to the Prop.98 system have reduced the share of funds that the CCC may be entitled to, but actual appropriations remain below that share as well.

the enrollment growth in the UC occur at the Berkeley, Los Angeles, and San Diego campuses.[4] These campus-related increases in enrollment are paired with additional funding.

Both plans sunset by 2028, when they will be subject to reauthorization or adjustment by system leadership. It should be noted, however, that these compacts are non-binding and can be adjusted, delayed, or reversed if the state determines funding is lacking. Similarly, if the systems fail to reach their agreement goals, it is unlikely the promised funds would be adjusted accordingly. Nevertheless, determining state goals for higher education and aligning funding with those goals is an important step. Tuition plays a minor role at CCC compared to UC and CSU. However, an agreement with CCC lays out similar goals, though funding levels remain determined through the Prop. 98 formulas (see text box above).

State financial aid is largely delivered through the Cal Grant, but also includes other programs (such as the Middle Class Scholarship) that all combine to reduce costs for students in each of the higher education systems. Notably, the Cal Grant is an entitlement, with its value tied to the cost of attendance. Thus, when tuition rises at the UC and CSU, for many students the level of state support rises as well.

The Role of Federal Funding

Though tuition and state/local appropriations comprise most of the core funding for California colleges and universities, the federal government also contributes. This comes in the form of financial support for students, grants for research, and more recently, less structured funding due to the COVID-19 pandemic.

A majority of the loans students use to pay for tuition and/or other college costs come from the federal government. California colleges and universities see this federal financial aid in the form of tuition revenue, since the aid is given to students to cover tuition costs. About one in four students take out federal loans at CSU and UC, while less than 1 percent at CCC do so. Loan amounts vary, but the typical borrower at UC and CSU uses between $13,000 and $20,000 over the course of their undergraduate experience (Jackson and Starr 2023).

The federal government also provides grants that students do not have to pay back. The Pell Grant, which covers educational expenses for students with exceptional financial needs, is by far the largest federal grant program. In 2023, Californians received over 900,000 Pell Grants totaling over $4.7 billion. But the federal government also provides grants for research activities and other programs not necessarily included in core funding for educating students.

During the COVID-19 pandemic, the federal government provided aid directly to campuses across the country to make up for budgetary shortfalls associated with pandemic recovery. California public institutions received about $4.5 billion from March 2020 to March 2021, and all such aid was to be spent by 2023. Campuses spent those discretionary dollars on emergency aid for students, online instruction, replacement of auxiliary revenue (such as parking lots and dining halls), social distancing and health costs, and other pandemic-related costs (Jackson, Cook, and Starr 2022).

4. The compacts also require that the nonresident enrollment share not exceed 18 percent of UC campuses—this means medium-term decreases in that share at the Berkeley, Los Angeles, and San Diego campuses. Further new enrollments should maintain specified ratios of new undergraduates to transfer students—2:1 at UC and 1:1 at CSU.

Although these events are relatively uncommon, the COVID-19 pandemic was not the first time extra federal dollars went toward core funding. During the recovery from the Great Recession, the American Recovery and Reinvestment Act of 2009 provided discretionary money for campuses. In both cases, some of the federal funding was used in place of state appropriations and tuition revenue.

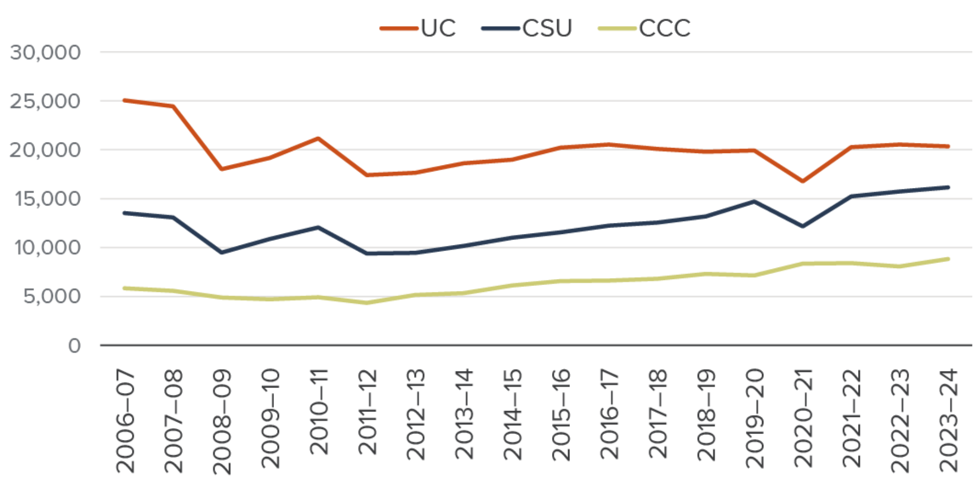
Recent Trends in Higher Education Funding

State funding for California's higher education systems grew steadily through most of the past decade (Figure 2). CSU and CCC are currently funded at record highs on a per student basis, surpassing the early 2000s when the state economy was growing rapidly. Though UC has not quite reached pre-Great Recession levels in per student funding, tuition increases and rising enrollments of nonresident students—who pay nearly three times as much tuition—has made up for some reductions.

Figure 2

Higher education General Fund allocations per student have grown faster at CSU and CCC than at UC

$ per FTE student



SOURCE: Authors' calculations using Department of Finance and FTE student enrollment data from the Legislative Analysts' Office.
NOTES: We use per Full-Time-Equivalent (FTE) synonymously with per student in this paper. An FTE is a count of the number of units taken by students divided by a full-time course load (for example, 15 at a semester institution). State General Fund dollars, inflation adjusted.

During the COVID-19 pandemic, all three systems saw significant growth in per student funding due to an unusual convergence of events: a decrease in enrollment that coincided with an overall increase in funding. Three federal stimulus bills (CARES, CRRSA, ARP) delivered $600 billion in total emergency funding to California, $10 billion of which went to its higher education institutions. In addition, state tax revenues were much higher than expected, creating a large budget surplus. Further, college enrollment growth trends were diverging across the systems at the same time.

UC and CSU saw slight enrollment increases, but growth was smaller than anticipated. Transfer students from the California Community Colleges make up about one third of UC enrollment and almost half at the

CSU. When the community college system saw a 20 percent decline in enrollment during the pandemic (Alesi Perez et al. 2022), the pool of transfer students shrank.

The higher education systems are now starting to see a return to pre-pandemic enrollment growth levels. But the number of college-age students is projected to plateau and then decline in the coming years. That could make ensuring stable funding growth a challenge in the near future.

Funding Equity

Funding levels at UC, CSU, and CCC are often substantially different from each other in part due to their distinct missions as set out by California's Master Plan for Higher Education. The CCCs offer a low-cost option to meet a wide variety of student goals, including earning associate's degrees or certificates, transferring to a four-year university, and lifelong learning. The CSU and UC systems offer bachelor's and master's degree programs, and the UC also offers doctorates.

Their funding differences reflect those missions—and the costs associated with them. UC tuition is higher, so it collects a bigger portion of its revenue that way ($14,395 per student in 2023) than the CSU ($7,972), which in turn is higher than the community colleges (about $1,300). State and local appropriations also reflect these differences (Figure 2). The UC system receives about $22,000 per pupil, CSU about $15,000, and CCC about $11,000.

Moreover, the systems don't educate the same students. Student populations at CSU and CCC mostly mirror the racial/ethnic composition of high school graduates in the state. At UC, Black and Latino students are underrepresented, and Asian-American students overrepresented. (Johnson, Bohn, Jackson, and Rodriguez 2019). Students at CSU are also more likely to be first-generation college students and receive Pell Grants than those at the UC.

California's efforts to fund postsecondary education are heavily invested in providing equitable access to higher education regardless of where students seek it. Financial aid grants are need-based and directed at students from the lowest-income families, covering tuition regardless of system. It is true that the state spends more money per student at UC, where Black and Latino students are underrepresented, and where students from wealthier families are likely to attend. However, the state subsidizes more of the total cost of education at CSU and especially at CCC.

California in Context

California's spending on public colleges and universities compares favorably to other states. The portion of funding from state appropriations is historically higher in California, which allows for lower tuition and a more affordable postsecondary education. However, as in California's four-year institutions, tuition is playing a more important role than ever across the nation.

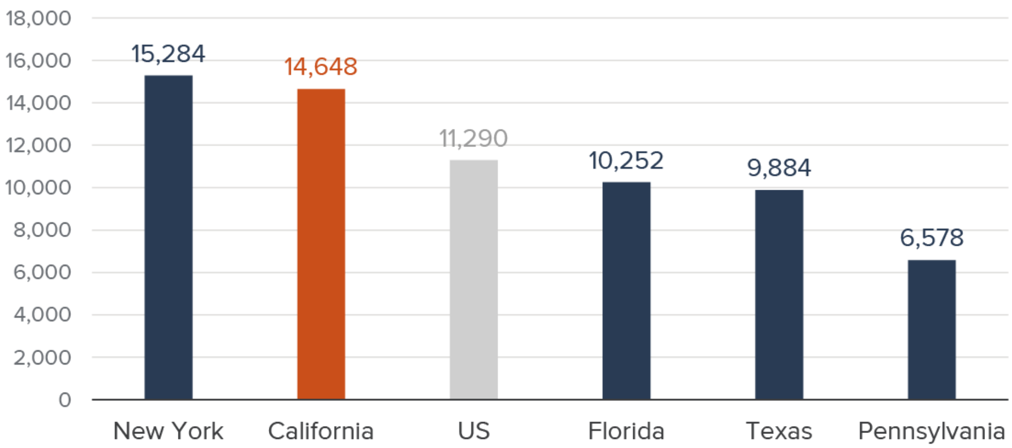
California Compares Favorably to Other States

California generally spends more than the rest of the country on higher education. Its per student state appropriations are well above the national average, and on the higher end compared to other large states like Texas, Florida, New York, and Pennsylvania (Figure 3). Also, the gap between California and the rest of the US is growing, with California spending about $14,000 per student in 2022, compared to a US national average of just over $11,000.

Figure 3

California spends more per student than most large states

Total state and local funding per FTE student ($)



SOURCE: State Higher Education Executive Officers (SHEEO) State Higher Education Finance Report 2023.
NOTE: Total state and local funding does not include federal stimulus dollars.

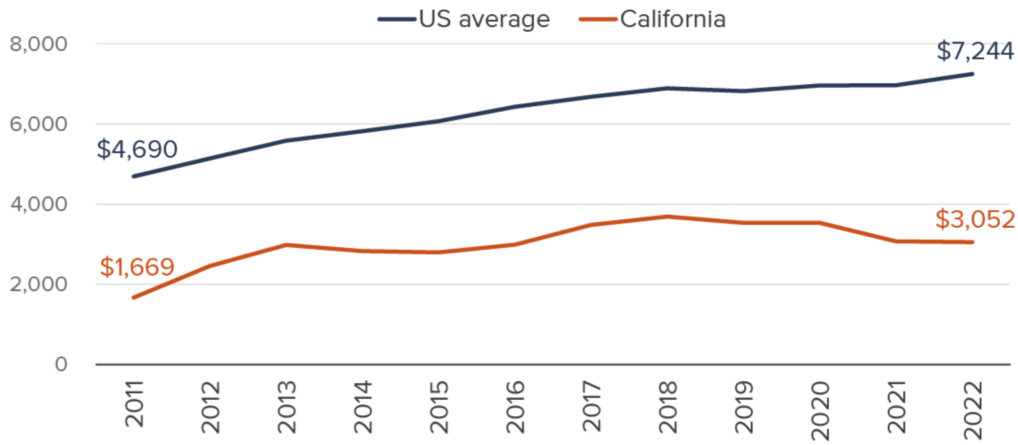
On the other side of the equation, California institutions generally collect less tuition per student than other states, with an average of about $6,000 compared to a national average over $10,000 (Figure 4).[5] This disparity comes from multiple factors: tuition at the UC and CSU are generally lower than four-year universities elsewhere, and many more students in the state begin at the community college level, where tuition is even lower.

5. We use “per student” interchangeably with per full-time-equivalent student (or FTE). A full-time-equivalent student is 15 units per term (for semester colleges).

Figure 4

Tuition revenue per student has risen in California, and even more so across the US

$ per FTE student



SOURCE: Integrated Postsecondary Education Data System (IPEDS).
NOTES: We use per Full-Time-Equivalent (FTE) synonymously with per student in this paper. An FTE is a count of the number of units taken by students divided by a full-time course load (for example, 15 at a semester institution).

California spends over $2.4 billion on financial aid for students. This aid is most often in the form of grants, which students use to pay for tuition, or in some cases room, board, books, and other costs. The institutions count this as tuition (and auxiliary) revenue, but it is state money passed through to the student. As tuition revenues are low and state appropriations high compared to the national average, California's per student financial aid expenditures are about average.

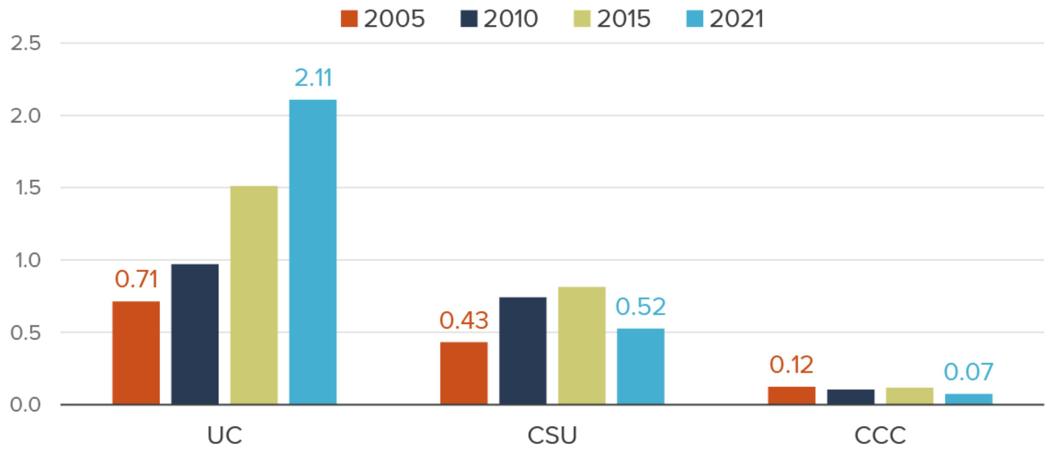
California's Institutions Differ from Those of Other States

While California may differ from other states, its three systems of public higher education also differ in amount and composition of revenue, as Figure 1 illustrates. Figure 5 shows that at four-year institutions like UC and CSU, the period after the Great Recession was associated with a rise in dependence on tuition revenue compared to state appropriations. The latter dropped throughout the nation as states struggled to balance their budgets.

Figure 5

Revenue sources have changed over time across California’s public higher education systems

Ratio of tuition to state appropriations



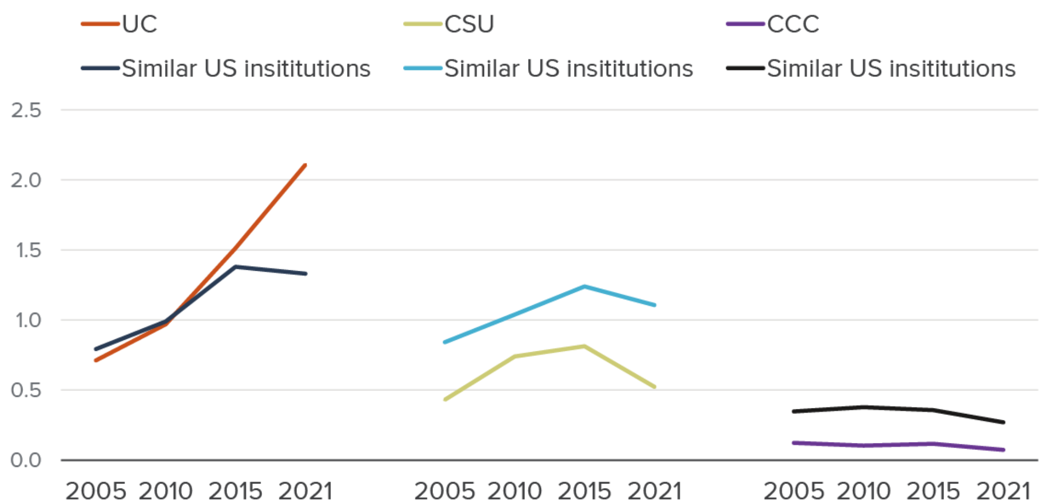
SOURCE: Integrated Postsecondary Education Data System (IPEDS).
NOTE: Data represent median institutions of UC, CSU, and CCC.

However, compared to the US institutions we chose for comparison (Figure 6), the UC system is now more reliant on tuition revenue. Compared to the CSU system, similar institutions across the US are more reliant on tuition than on state appropriations. Both CSU and UC have tuition plans that will likely increase those revenues for the next few years, which could change how much they rely on tuition should state appropriations not keep the same pace.

Figure 6

Higher education revenue source changes over time in relation to comparable institutions

Ratio of tuition to state appropriations



SOURCE: Integrated Postsecondary Education Data System (IPEDS).
NOTE: Data represent median UC and similar institutions, CSU and similar institutions, and CCC and similar institutions.

Just like community colleges across the nation, California community colleges receive more funding from state appropriations than from tuition. However, California has the lowest community college tuition in the nation and offers ample institutional financial aid, so CCCs rely almost exclusively on state appropriations. The Great Recession had little impact on that balance across the country and in the state.

Conclusion

California's higher education funding faces challenges as the state's fiscal outlook changes and upcoming demographic trends shift. However, how the state funds higher education will still impact affordability and equity, so it is critical to examine the factors that will impact higher education revenue over the next few years.

The state currently faces a multi-billion-dollar deficit over the next two years. The last time this happened—during the Great Recession—higher education experienced substantial General Fund cuts. This caused both the CSU and UC to double their tuition and incorporate other revenue-generating strategies such as raising fees and admitting more nonresident students.

Although it could change after the May budget revise, early indications from the governor's proposed 2024 budget shield higher education from cuts, but don't have the funding increases that UC and CSU have grown used to. At the same time, UC and CSU are both planning to raise tuition each year for the next five years. These extra funds will be important for the systems in the face of flat or perhaps declining state appropriations. On the other hand, this solution will make them increasingly reliant on tuition.

Shifts in higher education enrollment may also impact funding. COVID-related enrollment declines at community colleges and some CSU campuses are not yet fully restored. In addition, a decline of 120,000 high school graduates is projected over the next two decades. Tuition revenues and the budget process may change if big declines in enrollment occur at California's public universities.

California's Cal Grant financial aid system is primarily designed to provide tuition support to students. However, non-tuition costs like housing, food, health care, and transportation are increasing rapidly. This puts financial strain on students, some of whom must make a choice between reducing their course load in order to work—thereby taking longer to graduate—or taking out loans and graduating with a heavy debt load. Though the state has recently taken steps to help provide additional housing and basic needs supports for students, thinking creatively about how to maximize federal resources and considering additional non-tuition support through Cal Grants could help alleviate some of this strain.

For the future, more research should be focused on how institutions spend their dollars from each source. As California enters a prolonged period of moderate enrollment growth, opportunities arise to better target existing dollars to programs that improve student persistence and completion. Tracking dollars as they flow through the state's higher education systems is difficult, but as new data are made available, new research could help policymakers to prioritize successful programs and to better understand cost drivers.

The pandemic has shown that the state and its higher education institutions can be nimble and innovate to adjust to major disruptions. Moving forward, rethinking how to serve students and offering varying cost models could help California reach its goals of a more educated populace, a thriving economy, and improved economic mobility.

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