



Analysis of Recent Equable paper July 2020

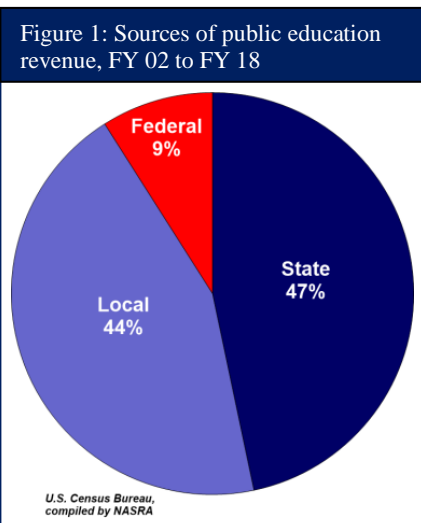
Researchers at Equable recently published a report titled “Hidden Education Funding Cuts: How Growing Teacher Pension Debt is Eating into K-12 Education Budgets.” The report consists of a brief narrative accompanied by a national report and 50 individual state reports, which together are intended to address the impact of teacher pension contributions on state education budgets.

The methodology and findings of the Equable report raise serious concerns. For example, the report:

- Overstates the percentage of education spending consumed by teacher pension contributions by drastically understating total public education expenditures;
- Makes tenuous claims that increasing teacher pension contributions are impairing states’ ability to deliver a quality public education by crowding out other education funding priorities;
- Excludes longer-term context of spending on pension costs;
- Omits necessary contextual information on factors driving differences in pension cost levels.

Overstated impact of teacher pension contributions on education budgets

The methodology deployed in the Equable report appears to significantly understate public education spending, with the understated figures serving as a reference point against which to measure teacher pension contributions. This methodology results in overstatement of the percentage of education spending consumed by teacher pension contributions.

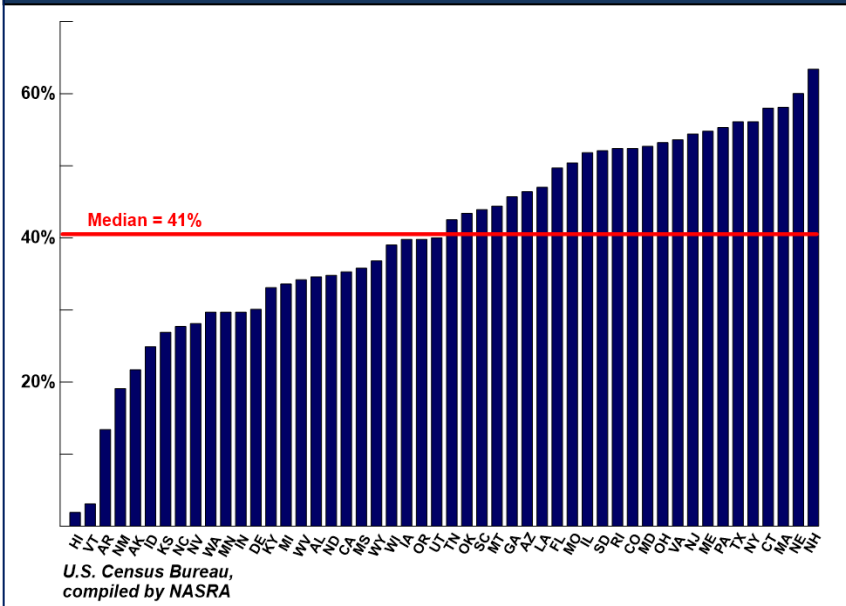


According to the U.S. Census Bureau, public elementary and secondary education expenditures totaled approximately \$721 billion in FY 2018, the latest year for which this data is available. The Census dataset further were derived from state, local, and federal sources. Figure 1 illustrates the sources of all public education revenue accumulated since FY 2002.

Despite the fact that state funds comprise less than one-half of public education revenue since 2002, state own-source revenue appears to be the only source for which the Equable report measures teacher pension contributions. Depending on the state, teacher pension contributions are made by state governments, school districts, or both, a fact that is acknowledged in the report:

The way that states typically pay for teacher pension costs, it is almost inevitable that education spending will be crowded out. Required contributions to teacher pension funds can be paid directly by the state out of legislatively managed funds, or they can be paid by the local employer such as a school district. Some states use both methods for different portions of pension costs. But in almost all cases, the dollars used are coming from funds intended to be spent on education – very few states use general fund dollars for teacher pension costs.

Figure 2: Percentage of state public education revenues sourced from local governments, FY 18



The exclusion of key sources of public education funding results in overstatement of the percentage of public education budgets that are consumed by teacher pension contributions nationally and in each state, with the level of overstatement varying based on individual state public education funding structures. As shown in Figure 2, state reliance on local funding sources varies, from less than 2.0 percent to just over 60.0 percent.

Regardless of the level of government from which they are sourced, public education revenues are used to fund a range of related expenses, and an accurate assessment of the impact of teacher pension contributions on public education

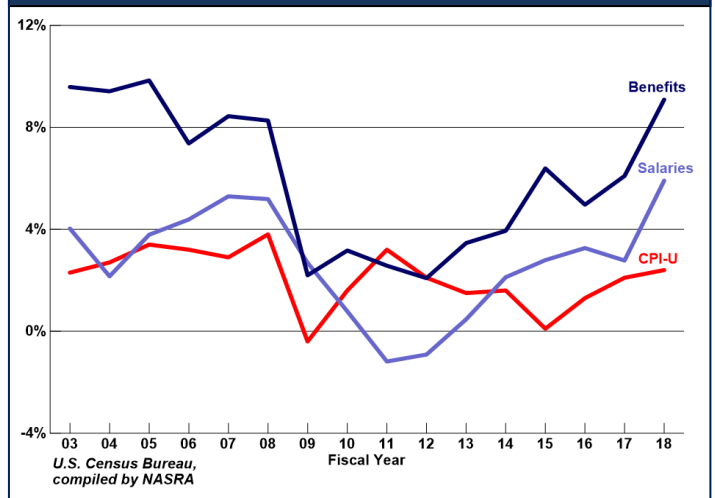
budgets should include revenues acquired from all sources – federal, state and local – rather than limiting the comparison to just state revenues.

Unproven claims of teacher pension contributions crowding out other public education priorities

The report cites rising teacher pension contributions as a percentage of public education spending as de facto evidence that those contributions are “crowding out,” or reducing, other forms of public education expenditures. As with the point discussed above, this claim is subject to scrutiny supported by the omission of locally-sourced public education revenues from the analysis, as well as other invalidating evidence.

If teacher pension contributions were truly crowding out public education spending, one might expect to see evidence in the growth of teacher wages and salaries, which, along with pensions and other benefits, comprise total teacher compensation. The Census data reveals that while growth in K-12 spending on employee benefits (a figure which includes pensions and, presumably, health care and other benefits) is higher in recent years, as shown in Figure 3, teacher wages and salaries also have grown, and this growth has been above inflation in most years and on average. Wage growth above inflation is an appropriate benchmark for the relationship between salaries and the purchasing power of wage earners, and since FY 03 teacher salaries grew by 2.7 percent on average, compared to 2.1 percent average annual inflation for the same period.

Figure 3: Annual change from prior year in teacher salaries, benefits, and inflation, FY 03 – FY 18

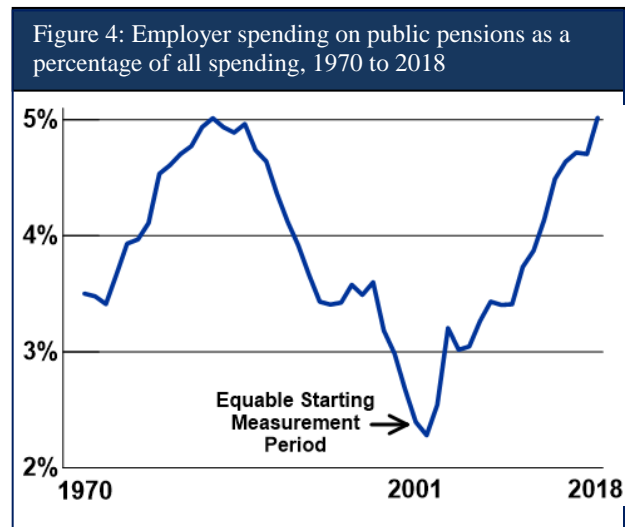


Furthermore, as the chart shows, years in which teacher salaries grew slower than inflation coincide with economic recessions, when growth in benefits also declined, thus reducing or eliminating the possibility that depressed salary growth was the result of teacher pension contributions.

Exclusion of longer-term context of spending on pension costs

The Equable report’s baseline year is 2001, a year that is near the low point of combined public pension employer contributions, measured as a percentage of all state and local government spending. Employer contributions reached this low point primarily as a result of strong investment performance in the preceding years, culminating in a combined public pension funding level of more than 100 percent, with many plans funded well above 100 percent. This strong funding level allowed employer contributions to decline to very low levels, including zero for some plans, and might be considered an actuarial dividend, as some states and cities used very low rates of required pension costs to increase spending in other areas, including K-12 education.

Employer contributions in Equable’s base year of 2001 were just 2.4 percent of all public sector spending, compared to an average amount spent on public pensions over the last 30 years of 3.6 percent. And that 2.4 percent, combined for all public pension plans, was more than 100 percent of the Annual Required Contribution recommended by actuaries for that year. Although Equable is relying on a dataset that begins with 2001, for purposes of comparing long-term public pension trends, a comparison that begins in 2001 inevitably will result in showing public pension plan costs rising disproportionately to other areas of spending. In fact, spending on public pension plans since 2002 have marked a return to more traditional rates of spending on public pensions.



Had the Equable study’s starting point been 1980 or 1990, for example, the report’s results likely would have been much different.

Omission of contextual information on factors driving differences in pension costs

Both the national report and individual state analyses omit consideration of important contextual information on factors driving differences in teacher pension cost levels among states. Two of these factors include differences in benefit levels (particularly as it pertains to differences in Social Security coverage), and employers’ commitment to making required pension contributions.

Nationally, approximately 40 percent of public school teachers participate in a public pension plan in lieu of Social Security. In several states, such as Connecticut, Illinois, Missouri, Ohio, Texas, and others, substantially all teachers are outside Social Security. Pension benefits – and costs – for those who do not participate in Social Security are typically higher than for those who do participate, in order to compensate for the absence of Social Security coverage. It is reasonable to assume that states whose teachers do not participate in Social Security will, all else equal, have lower public education expenditures as a result of not having to pay into Social Security. These states also have a higher baseline for teacher pension contributions, and, as a result of these two conditions, non-Social Security states could be expected to report higher percentages of public education budgets devoted to teacher pension contributions than states whose teachers are covered by Social Security.

While the report highlights states' historical records of teacher pension funding adequacy, its findings obscure important contextual information, pertaining in particular to states whose contributions exceed their actuarially determined contribution (ADC). A handful of states, including Ohio, Oklahoma, Nebraska, and West Virginia, and others, made contributions to their teacher pension plans in excess of their ADC in FY 2018. According to the methodology deployed in the Equable report, these states report higher "hidden cuts" to public education budgets as a result of these higher contributions than would otherwise be reported if these states were contributing at full actuarially determined levels. This negative framing obscures the fact that states that elect to contribute more than the ADC a) may source these extra contributions from surplus revenues that are not in competition with other public education funds and b) are exerting downward pressure on future pension cost by acting prudently to more rapidly eliminate their unfunded liabilities.

Conclusion

Contributions to teacher pension plans have grown in recent years, chiefly in response to growth in unfunded pension liabilities, use of more conservative actuarial assumptions and methods, and, in some cases, through employers' deliberate efforts to strengthen pension funding practices. While these trends are objective and observable, by omitting key public education revenues from their analysis and applying other distorting methods to present teacher pension contributions as a hindrance on other public education funding priorities, the Equable report presents a misleading characterization of their impact on K-12 education budgets.

Supporting data for this analysis is sourced from the U.S. Census Bureau Annual Survey of School System Finances: <https://www.census.gov/programs-surveys/school-finances/data/tables.html>.

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