Hidden Education Funding Cuts

Arizona

Pension costs are consuming nearly six times as much state education funding today as they were two decades ago

Teacher retirement systems across the country have seen costs rise over the past two decades, driven largely by growth in pension debt (known as unfunded liabilities). The costs of paying down these shortfalls in teacher pension funds have been steadily cutting into the spending on key education priorities. The effects are felt particularly hard in high-need districts which have fewer local resources to draw on to fill in the gaps when education costs rise, creating less funding for teacher salaries and programs aimed at improving academic and other outcomes.

However, this squeeze has not been felt uniformly across all states, as revenue and education spending experiences have varied. As a result, there are notable differences in the degrees of crowd out that pension debt costs have had on education spending when looking from state-to-state.

This profile provides detailed analysis for your state, supplementing the analysis highlighted in our primary research on Hidden Education Funding Cuts in America. The profile examines three key elements:

- **State Education Spending:** tthe state's "own-source" K–12 spending for 2001–2018, both in the aggregate and on a per student basis. This excludes federal funding (which is typically not used to pay pension costs and local revenues (which also vary as a funding source from state-to-state);
- **Pension Funding Status:** the pension system's unfunded actuarial accrued liabilities (UAAL) and actuarially determined employer contributions (ADEC) for 2001–2018; &
- **Education Crowd Out:** the shares of a state's own-source K–12 spending consumed for the pension contributions paid for 2001–2018.

For each element identified above analyses are from a state budgeting perspective, excluding both federal and local funding. We offer illustrations of trends over time, and a brief analysis of those trends. The last page includes a quick glossary of terms and link to the methodology for all of the data provided.

It is important to note that all charts provide figures adjusted for inflation except for displays of state own-source K–12 spending. This allows for a reference of how much of the increase in nominal education spending is just driven by inflation as opposed to the expansion of education budgets.

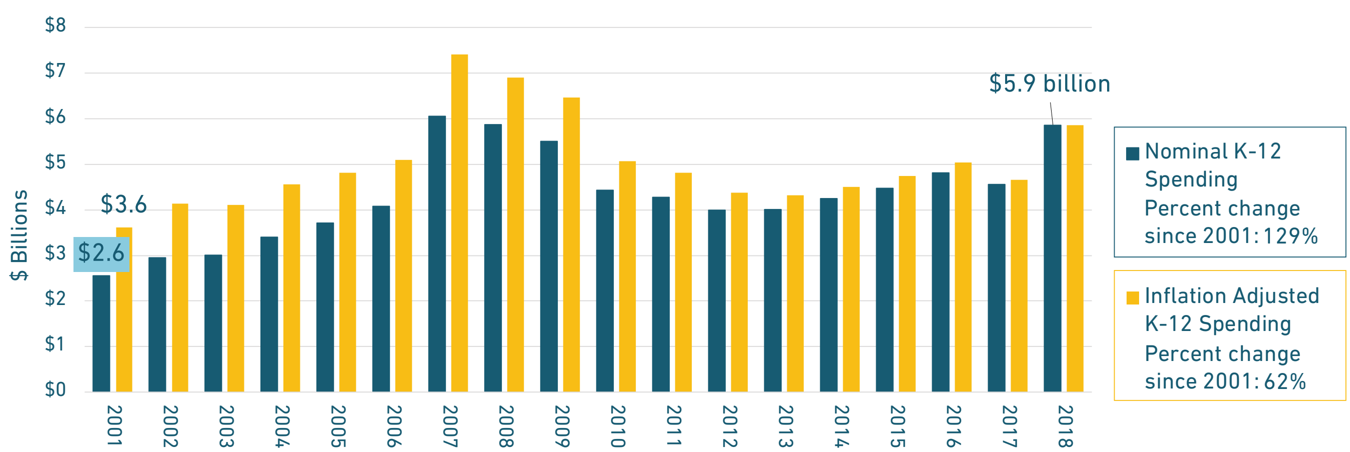
The Grand Canyon State is home to more than 7 million citizens, and 1.1 million primary and secondary school students. In 2018, the total state budget exceeded $37.5 billion — funds for schools, transportation, public safety, and other public services. Out of that spending, the state's own-source expenditures — defined as all state funding that does not draw on federal or local revenue — totaled $21.5 billion.

Arizona teachers are enrolled in a guaranteed income plan, known as a defined benefit pension, administered by the Arizona State Retirement System (ASRS). ASRS manages retirement benefits for nearly 600,000 active and retired teachers, municipal employees, and state workers. Although ASRS provides retirement for more than just teachers, the teachers comprise the largest share (43%) of any group of members.

EDUCATION SPENDING

In 2018, Arizona's state distributed K–12 expenditures totaled $5.9 billion. Out of that total, $4.8 billion came from state own-source funding while the remaining $1.1 billion was from federal grants and other education programs (local sources provided additional funding).

Figure AZ1: Arizona increased state education funding by more than $2 billion after accounting for inflation.



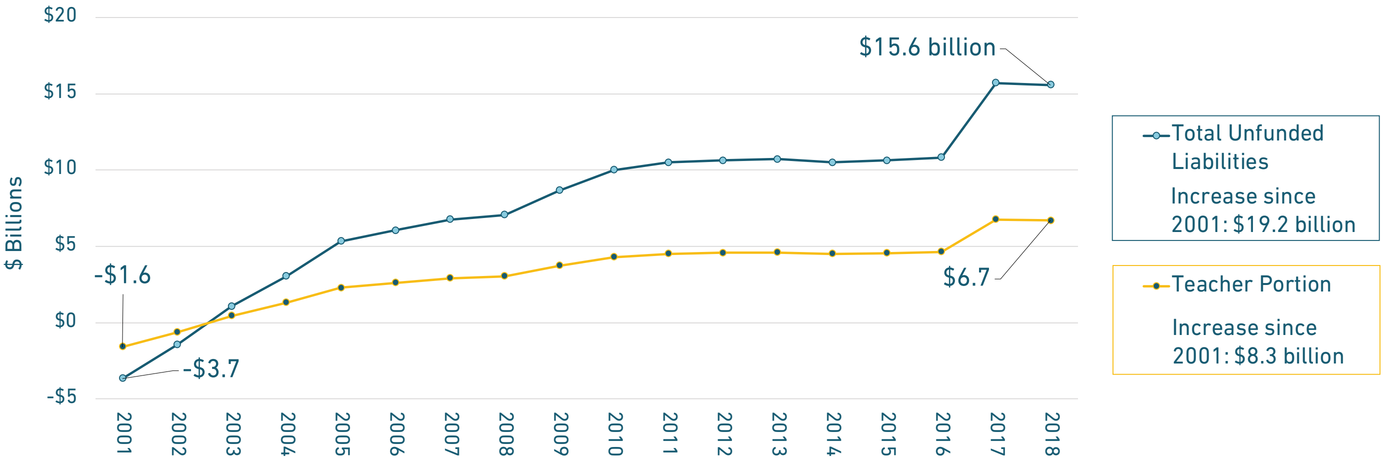
State Own-Source K–12 Spending, 2001–2018

As figure AZ1 illustrates, state spending on primary and secondary education in Arizona has increased significantly since 2001 — growing by $3.3 billion in nominal dollars; however, it only increased moderately after adjusting for inflation, going up by only $2.3 billion. On a dollars per student basis, spending increased 41% since 2001 — growing from $3,980 to $5,184 (inflation adjusted).

PENSION FUNDING STATUS

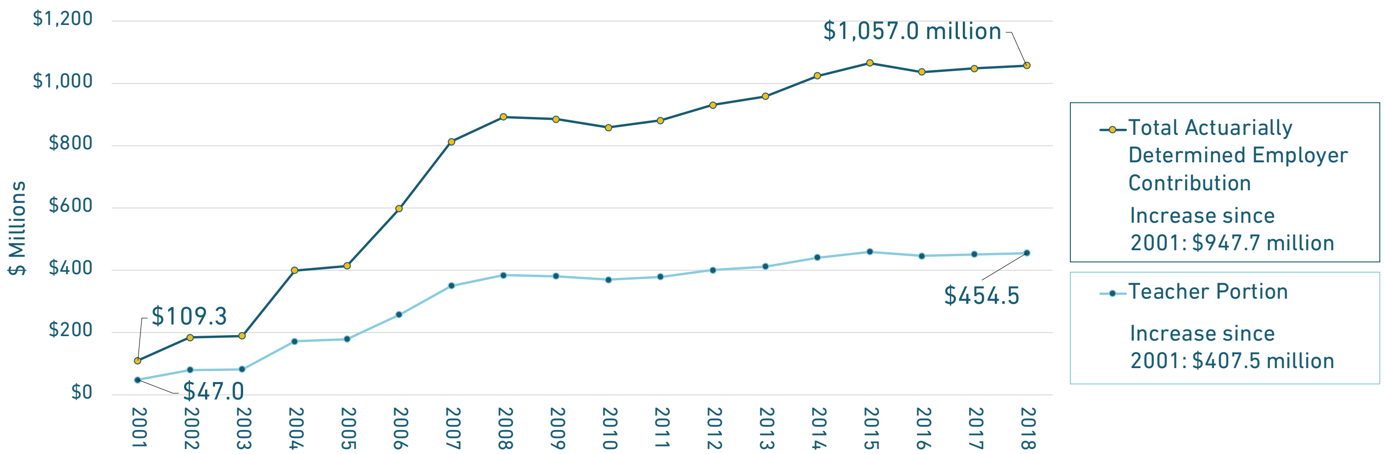
As recently as 2002, ASRS was running a surplus. However, over the past 16 years a combination of underperforming investments coupled with changing demographics have resulted in a growing unfunded liability for ASRS — reaching nearly $15.6 billion in 2018. Figure AZ2 shows the change in the unfunded liabilities and Figure AZ3 illustrates the change in what state actuaries have recommended as contributions from government employers.

Figure AZ2: ASRS had a surplus in 2002. Since then the plan has developed more than $15 billion in pension debt.



ASRS Unfunded Liabilities (Actuarial Value), 2001–2018

Figure AZ3: While the debt has grown, required contributions to ASRS have exploded to nearly ten-times as much as in 2001.

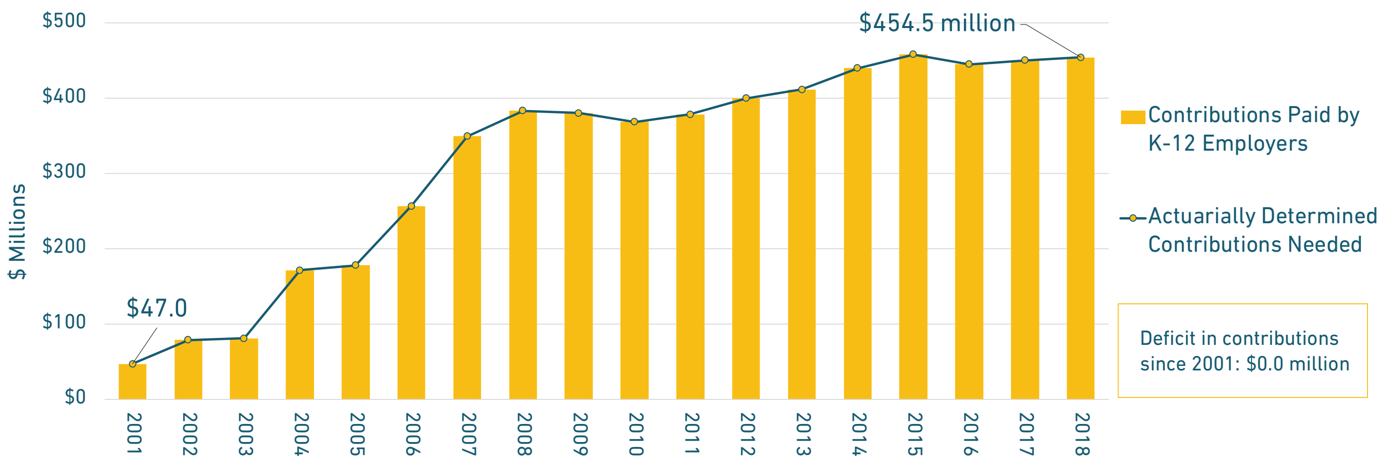


ASRS Actuarially Determined Employer Contributions, 2001–2018

There are a number of states across the country that do not always ensure that the ADEC is paid in full into the pension fund each year. Arizona is one of the states that has demonstrated a strong commitment to paying the full required contribution, as shown in Figure AZ4.

As a result, the increase in contributions actually paid by the state and school districts for teachers mirrors the growing trend displayed in Figure AZ3, with K–12 employer related contributions increasing nearly ten-fold from $47 million in 2001 to more than $450 million in 2018.

Figure AZ4: Arizona paid its full actuarial bill to ASRS each year. The increase in unfunded liabilities meant actual pension contributions paid have grown nearly ten-fold since 2001.



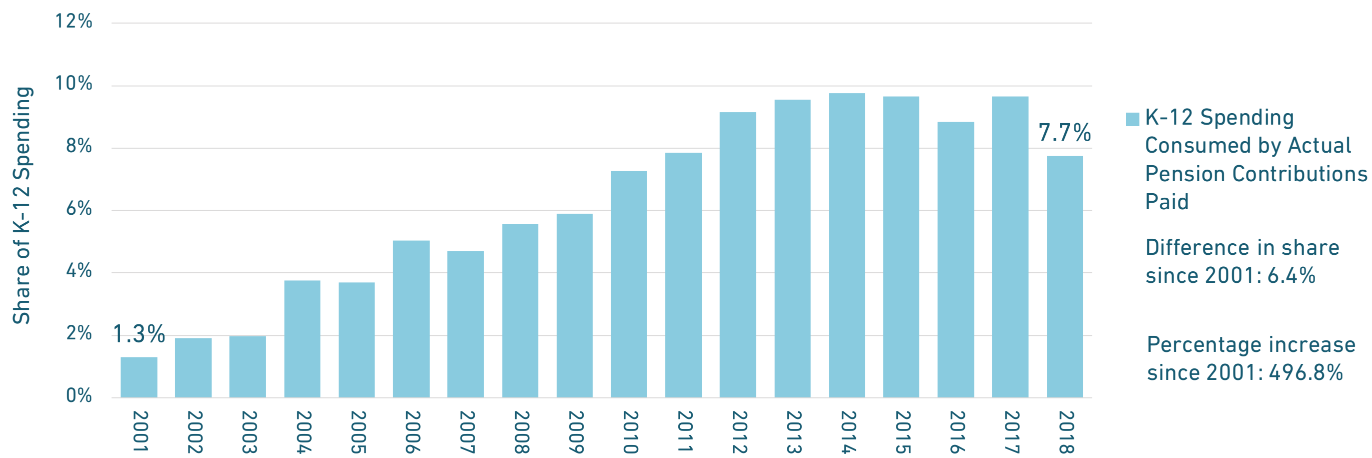
Actuarially Determined Employer Contribution Compared to Actual Contributions Paid to ASRS, 2001–2018

Paying the full required pension bill each year is the bare minimum for ensuring a pension system is fully funded. However, from the perspective of education funding, any increase in pension costs is going to be viewed negatively if it is shrinking the dollars available for teacher salaries and serving kids. In an ideal world, Arizona would have ensured that funding for education expanded at least as fast as the growth in the ADEC shown above. But as we show in the final chart on the next page, that hasn't happened.

PENSION COSTS CROWDING OUT K–12 SPENDING

The growing costs of funding ASRS have soaked up an increasing share of Arizona education spending. This is especially important for teachers, as the growth in ASRS's costs outpaced the growth in state own-source K–12 spending. In fact, ASRS's contributions reported as a share of K–12 spending increased from 1.3% in 2001 to 7.7% in 2018, shown in Figure AZ5.

Figure AZ5: The hidden cut to Arizona's state education funding is serious. ASRS contributions are consuming nearly five times as much state K-12 funding in 2018 as 2001.



Pension Costs as a Share of State Own-Source K–12 Spending
Contributions Paid and Actuarially Determined Employer Contribution, 2001–2018

The hidden education funding cuts in Arizona have been driven by both fast-growing pension contributions and slow-growing education budgets. Until the 2018 increase in overall education spending in Arizona, the hidden crowd out was even worse, as seen in five-year data for 2013-2017 where pension contributions consumed nearly 10% of K–12 education spending.

Arizona has met its commitments to funding ASRS by paying the full ADEC each year, but the costs of paying down the system's debt have grown significantly faster than the state's own-source education spending. Unless there is a change that reduces ASRS costs and/or adjusts the state's education funding to fully account for pension contributions, Arizona's education funding will continue to suffer this hidden cut in dollars intended for serving the state's children.

An even more concrete way to understand how changes in pension debt and pension costs have influenced education resources is to think about them relative to total student enrollment. Table AZ1 shows the teacher portions of the UAAL and actual pension contributions on a per student basis compared against state education spending. Breaking the numbers down this way shows that growth in unfunded pension liabilities and related pension contributions have outpaced per student spending by the state. In fact, without a 2018 bump the education budget, Arizona would be spending less per student today than 2001, after accounting for inflation and pension costs.

Table AZ1:State education spending has grown to nearly $5,000 per student, but debt and contributions have grown much faster.

Year	Total State K–12 Spending Per Student	Per Student Share of Pension Debt	Pension Debt as % of Per Student Spending	Employer Pension Cost Per Student	Per Student Spending Minus Pension Cost
2001	$3,980	-$1,731	Fully Funded	$52	$3,928
2002	$4,394	-$662	Fully Funded	$84	$4,310
2003	$4,222	$474	11.2%	$83	$4,138
2004	$4,536	$1,303	28.7%	$171	$4,365
2005	$4,650	$2,214	47.6%	$172	$4,478
2006	$4,769	$2,438	51.1%	$240	$4,529
2007	$6,823	$2,672	39.2%	$321	$6,502
2008	$6,347	$2,794	44.0%	$353	$5,995
2009	$5,998	$3,457	57.6%	$353	$5,645
2010	$4,730	$4,008	84.7%	$344	$4,386
2011	$4,463	$4,177	93.6%	$350	$4,113
2012	$4,012	$4,197	104.6%	$367	$3,645
2013	$3,914	$4,182	106.8%	$373	$3,541
2014	$4,055	$4,059	100.1%	$396	$3,659
2015	$4,277	$4,118	96.3%	$413	$3,863
2016	$4,488	$4,143	92.3%	$397	$4,091
2017	$4,134	$5,988	144.9%	$399	$3,734
2018	$5,184	$5,921	114.2%	$402	$4,783

Notes: Values are inflation adjusted dollars spent per student to allow for comparison of spending over time. Figures reflect the K–12 employer portion of liabilities and employer contributions.

Per Student Share of ASRS Unfunded Liabilities and Actual K–12 Employer Contributions, 2001–2018

ABOUT THIS PROJECT

The growing cost of unfunded pension promises is having direct and immediate influence on the ability of local school districts to serve children. To show how hidden education funding cuts work, we built a dataset of state-level K–12 education spending and combined it with contribution rate data for state pension plans where teachers are participants. Merging these two data types shows how the rate of change in teacher pension costs is growing much faster than education budgets nationally.

To review data at the national level, visit Equable.org/hiddenfundingcuts and check out: "Hidden Education Funding Cuts: How Growing Teacher Pension Debt Payments Are Eating into K–12 Education Budgets." To learn more about our data and how we calculate a state's hidden education funding cut, check out the methodology.

However, the hidden funding cuts to education have not been felt uniformly across all states, as revenue and education spending experiences have varied. For some states, slow growth in K–12 spending has combined with the explosion in pension debt to create a significant threat, potentially crowding other items out of the education budget. In California, for example, a report by Pivot Learning found that rising pension contributions, driven by efforts to repay pension debt, have led to deferred maintenance of schools, larger class sizes, reduction or elimination of after-school programs, and a reduction in educational equity.

But, for other states, K–12 spending itself has grown significantly, even after accounting for inflation, and this has offset part of, or most of, the state's increase in pension costs (though in these cases, it is likely that policymakers were not increasing K–12 spending simply to offset the growth in pension costs). And a few states have even managed to buck the trend entirely. While this profile details the experience of an individual state, we encourage you to explore the profiles of other states to see how their trends compare. A collection of profiles for all 50 states and Washington, DC can be found here.

ABOUT THE AUTHORS

Jonathan Moody is vice president of Equable Institute, where Anthony Randazzo is executive director. Moody has worked on state fiscal policy since 2014 including time as research officer at the Pew Charitable Trusts. Randazzo has worked with over a dozen states on retirement system improvements, and formerly was managing director of the Pension Integrity Project.

QUICK GLOSSARY

Actuarially Determined Employer Contributions (ADEC): This is the money that actuaries calculate should be paid each year by the state and local employers to cover pension benefits earned plus to pay down any pension debt (after accounting for any employee contributions).

Unfunded Liability (UAAL): This is the shortfall in money that a pension fund should have on hand to pay all future promised benefits. Think of this as pension debt owed to retirement systems to pay promised pension benefits. In technical terms, this refers to the Unfunded Actuarially Accrued Liability.

Own-Source K–12 Spending: This is the money spent on primary education using state resources only, excluding any federal funding, local resources, or expenditures on higher education.