Hidden Education Funding Cuts

Kentucky

Pension costs are consuming more than twice 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 state profile examines three key elements:

- **State Education Spending:** the 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 actuarially 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.

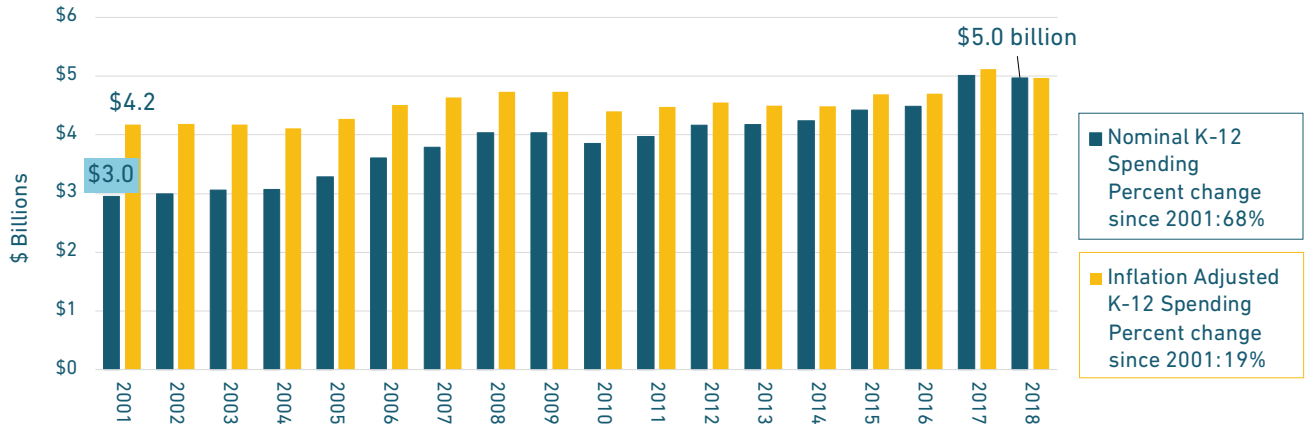
The Bluegrass State is home to more than 4 million citizens, and 680,000 primary and secondary school students. In 2018, the state's total expenditures exceeded $34 billion — funds for schools, transportation, public safety, and other public services. Out of that spending, the state's own-source expenditures — defined as all state funding that does not draw on federal or local revenue — totaled $21.6 billion.

Kentucky teachers are enrolled in a guaranteed income plan, known as a defined benefit pension, administered by the Teachers' Retirement System of the state of Kentucky (TRS). TRS manages retirement benefits for roughly 125,000 active and retired teachers (including some faculty at smaller public universities).

EDUCATION SPENDING

In 2018, Kentucky's state distributed K–12 expenditures totaled $5.8 billion. Out of that total, $5 billion came from state own-source funding while the remaining $854 million was from federal grants and other education programs. (Local sources provided additional funding.)

Figure KY1: Kentucky's state spending on education only increased by $800 million after accounting for inflation



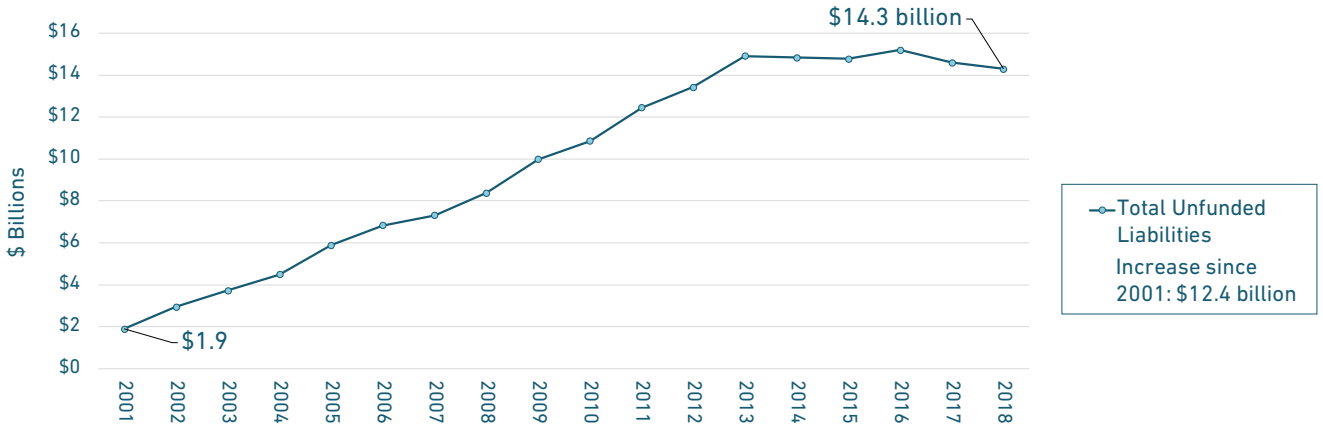
State Own-Source K–12 Spending, 2001–2018

As figure KY1 illustrates, state spending on primary and secondary education in Kentucky has increased moderately since 2001 — growing by $2 billion in nominal dollars; however, the increase was much less after adjusting for inflation, growing by only $800 million. On a dollars per student basis, spending increased 17% since 2001 — growing from $6,249 to $7,312 (inflation adjusted).

PENSION FUNDING STATUS

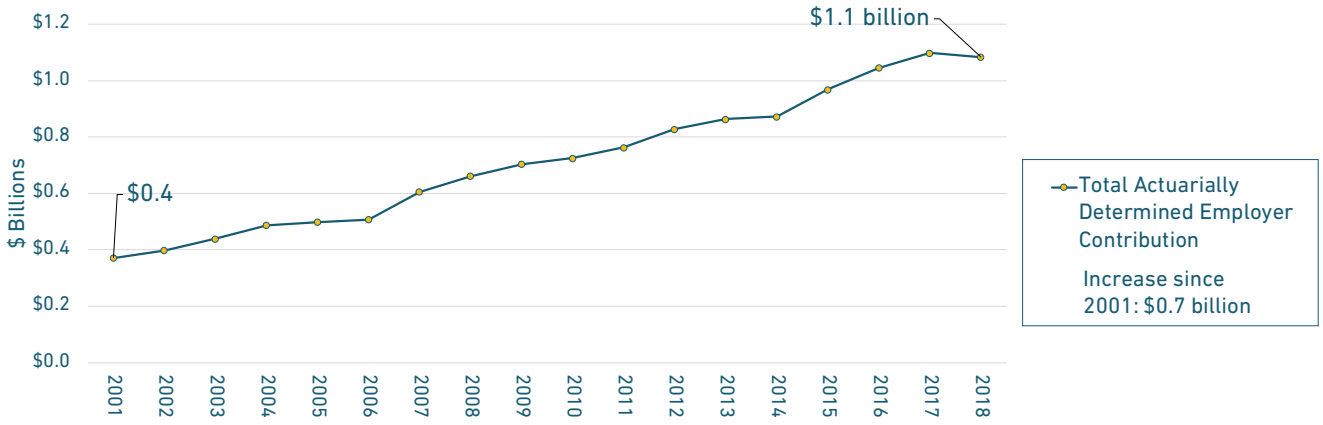
In 2001, TRS was facing less than $2 billion in pension debt. However, over the past 17 years a combination of underperforming investments coupled with changing demographics have caused the unfunded liability for TRS to explode — reaching $14.3 billion in 2018. Figure KY2 shows the change in the unfunded liabilities and Figure KY3 illustrates the change in what state actuaries have recommended as contributions from government employers.

Figure KY2: TRS's pension debt has grown more than seven-fold since 2001.



TRS Unfunded Liabilities (Actuarial Value), 2001–2018

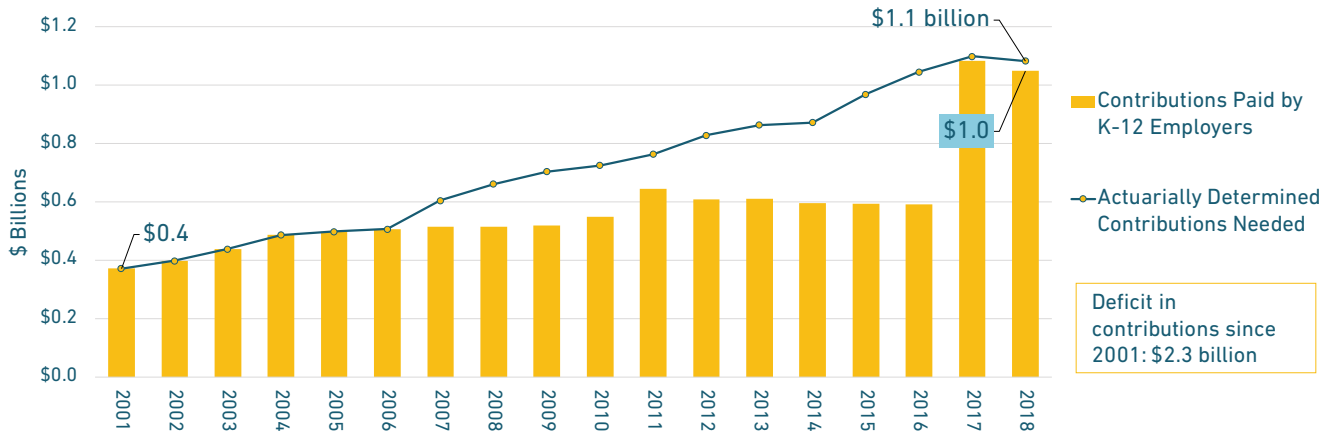
Figure KY3: To address growing pension debt the amount actuaries recommend the state contribute to TRS has nearly tripled.



TRS 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 to the pension fund each year. Unfortunately, Kentucky is one of those states, failing to pay the full pension bill each year from 2007 through 2016, shown in Figure KY4. As a result, the actual contributions paid into TRS using education funds have been less than if the ADEC trend displayed in Figure KY3 was paid in full, but the actual contributions paid to TRS have still more than doubled from $372 million in 2001 to $1 billion in 2018. However, much of the increase in contributions paid happened in 2017 when the state made an active decision to pay almost the full ADEC, going from $592 million in 2016 to $1.1 billion in 2017. The resulting spike in contributions paid illustrated in Figure KY4 just underscores how much the state was shorting its pension bill in the years leading up to 2016.

Figure KY4: Kentucky has only paid its full actuarial bill to TRS once since 2006, shorting the plan by $2.3 billion.



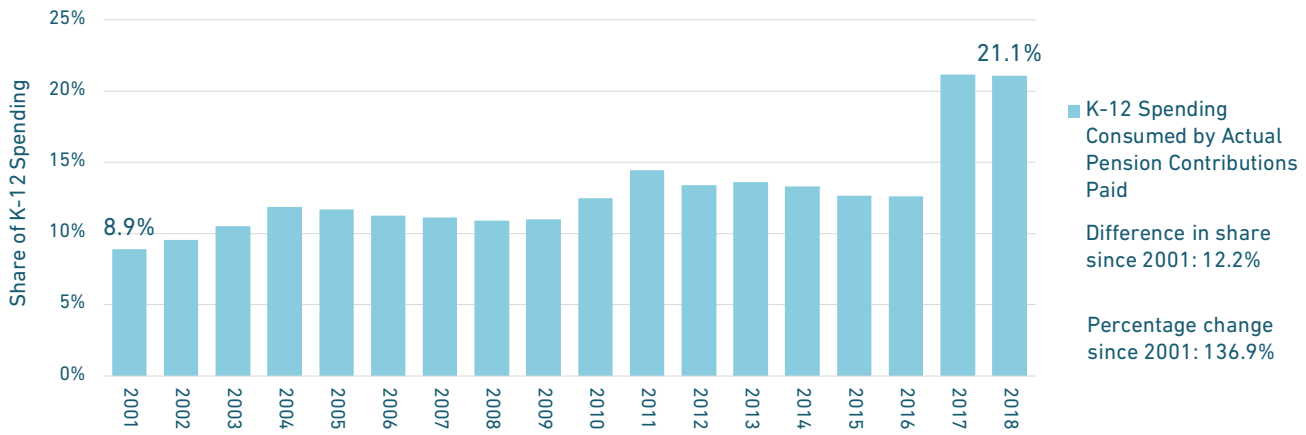
Actuarially Determined Employer Contribution Compared to Actual Contributions Paid to TRS, 2001–2018

Paying the full required pension bill each year is the bare minimum for ensuring a pension system is fully funded. Best practice would be for Kentucky to adopt a policy of ensuring the ADEC is paid every year. However, from the perspective of education funding, any increase in pension costs will be viewed negatively if it is shrinking the dollars available for teacher salaries and serving kids. If the ADEC had been paid every year without some adjustment to expand Kentucky's education funding, then the state could have suffered an even larger hidden cut than we show in the final chart on the next page.

PENSION COSTS CROWDING OUT K–12 SPENDING

The growing costs of funding TRS have soaked up an increasing share of Kentucky's state education spending. This is especially important for teachers, as the growth in TRS's costs outpaced the growth in state own-source K–12 spending. In fact, TRS's contributions reported as a share of K–12 spending increased from 8.9% in 2001 to 21.1% in 2018.

Figure KY5: The hidden cut to Kentucky's state education funding is serious. TRS contributions are consuming more than twice as much state K–12 funding in 2018 as 2001.



Actual Pension Costs as a Share of State Own-Source K–12 Spending, 2001–2018

As Figure KY4 indicates, before the state's increased commitment to paying the pension bill in 2017, contributions to TRS had still grown from $372 million in 2001 to $592 million in 2016, a 59% increase. Even while shorting the full pension bill, state education funding was not keeping pace with pension costs — in 2016 the share of state K–12 spending going toward TRS had climbed to 12.6%. Once we include the increase in contributions starting in 2017, the share is even higher.

Kentucky has failed to meet its commitments to funding TRS by not paying the full ADEC each year. But even the actual amounts paid have grown significantly faster than the state's own-source education spending. Unless there is a change that reduces TRS costs and/or adjusts the state's education funding to fully account for pension contributions, Kentucky'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 KY1 shows 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, after accounting for inflation and pension costs, Kentucky only spent $108 more per student in 2018 than 2001.

Table KY1: State education spending per student increased by $1,100 from 2001 to 2018, but pension debt and contributions have consumed nearly all of that growth.

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	$6,249	$2,843	45.5%	$556	$5,692
2002	$6,231	$4,390	70.5%	$593	$5,637
2003	$6,193	$5,523	89.2%	$651	$5,542
2004	$6,062	$6,644	109.6%	$720	$5,342
2005	$6,280	$8,667	138.0%	$733	$5,547
2006	$6,603	$10,003	151.5%	$743	$5,860
2007	$6,962	$10,973	157.6%	$773	$6,190
2008	$7,068	$12,512	177.0%	$771	$6,297
2009	$6,960	$14,697	211.2%	$764	$6,196
2010	$6,544	$16,132	246.5%	$815	$5,729
2011	$6,555	$18,254	278.5%	$945	$5,610
2012	$6,641	$19,603	295.2%	$890	$5,752
2013	$6,634	$22,015	331.8%	$903	$5,731
2014	$6,520	$21,558	330.7%	$867	$5,653
2015	$6,835	$21,518	314.8%	$864	$5,971
2016	$6,866	$22,226	323.7%	$865	$6,001
2017	$7,497	$21,397	285.4%	$1,587	$5,910
2018	$7,312	$21,029	287.6%	$1,542	$5,770

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 TRS 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.