Pennsylvania School Boards Association

Education Research & Policy Center

Issue Brief on

COMBINING SOCIAL SECURITY WITH BASIC EDUCATION FUNDING:

Flexibility or cost shifting?

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Acknowledgements

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EXECUTIVE SUMMARY

The economic climate over the past several years reduced the state's tax revenue. The state made the determination to spend stimulus funding (ARRA) on education including supplanting state dollars. The loss of ARRA funding was then passed back to districts as part of the 2011-12 state budget. The governor's proposed 2012-13 budget suggested consolidating transportation funding and Social Security funding with the basic education funding. This consolidation of funding was presented as the Student Achievement Education Block Grant (SAEBG). The concept was said, "To redesign school and district funding to provide flexibility that allows decision-making to rest with the local school district administrators and local school boards."[1] This PSBA-ERPC issue brief looks at the impact of consolidating the Social Security subsidy into the SAEBG.

The proposed SAEBG approach to funding does not provide flexibility. Given the history of funding, this approach would likely force a shift in spending away from students to cover the state's share of Social Security payments.

Combining Social Security with Basic Education Funding (BEF) changes the funding from a predictable subsidy to amounts established as part of the budget process. Under the rationale provided in the governor's proposed budget, a district would be able to allocate any unneeded Social Security subsidy for alternative uses. This rationale assumes that the districts will be able to reduce current salary costs in the future and the current subsidy will provide more money than will be required for the employer share of Social Security.

Under the governor's proposed 2012-13 budget, the state would have distributed $504,774,468 to districts as part of the new SAEBG. The Social Security allocated to the SAEBG represents an across the board 9.5% increase to every district for this subsidy. What does this increase really provide for school districts? Is it flexibility, or is it cost shifting?

This issue brief reviews the basic educational funding subsidy and projections from three different views. First, the issue brief analyzes the current funding structure without a block grant and assumes that it remains unchanged (no SAEBG). In the second and third views, the governor's budget proposal assuming the SAEBG is the basis for analysis. The difference between the second and third views of the analysis is a difference in the assumption about the projected growth of payroll and block grant subsidy.

Comparing the second and third views shows that if the payroll grows at a rate greater than the percent increase in the SAEBG, then the cost shifts to the district. If the reverse occurs and the subsidy grows faster than the payroll, the cost shifts to the state. Given the historical pattern of school district payroll increases and subsidy increases, the more likely of the two views with the SAEBG is the second view where the payroll grows faster than subsidy and the cost shifts to the district.

Consolidating Social Security funding with the basic education funding does not provide flexibility. If the concept is, "To redesign school and district funding to provide flexibility that allows decision-making to rest with the local school district administrators

and local school boards,"[2] then the consolidation of Social Security funding with the BEF does not achieve the intended outcome.

To the contrary, given the history of funding, this approach will likely force a shift of spending away from students to support Social Security payments. Unless the legislature is willing to remove the mandates associated with school district staffing, the ability of school districts to realize the stated goal of flexibility by consolidating Social Security subsidy in the SAEBG will not occur.

PSBA-ERPC Issue Brief

COMBINING SOCIAL SECURITY WITH BASIC EDUCATION FUNDING: Flexibility or cost shifting?

The governor's proposed 2012-13 budget suggests consolidating transportation funding and Social Security funding with the basic education funding. This consolidation of funding was presented as the Student Achievement Education Block Grant (SAEBG). The concept is said, "To redesign school and district funding to provide flexibility that allows decision-making to rest with the local school district administrators and local school boards."[3] This paper looks at the impact of consolidating the Social Security subsidy into the block grant.

The proposed SAEBG approach to funding does not provide flexibility. To the contrary, given the funding history (last year plus with an average of about 2%), there will likely be a spending shift away from students to support Social Security payments. District flexibility is limited when it comes to addressing staffing and related necessary actions.

Social Security

Social Security was originally adopted by the Federal Government in 1935 as the Old-Age, Survivors, and Disability Insurance Act. Social Security is funded by a dedicated payroll tax. This tax is formally known as the Federal Insurance Contribution Act tax (FICA). More recently, the tax has been split between FICA and Medicare to reflect contributions to both programs. The current employer tax rate is a combined 7.65% of payroll with 1.45% for Medicare and 6.2% for Social Security to a maximum compensation of $110,100.[4] The employer tax is in addition to the employee tax for Social Security. This means that the ultimate cost driver for increased Social Security/Medicare is the payment of salaries and wages paid to district employees.

History of the Social Security subsidy

The state participation in funding part of the districts' employer Social Security is provided in the Public School Code of 1949. Act 491 of 1952 authorized the coverage of certain officers and employees of the commonwealth and political subdivisions including school districts to participate in the Social Security program including payment of the employer share of the tax.[5] Sharing of the employer contribution was originally added by Act 660 of 1956[6]. Act 660 of 1956 specifically added section 9.1, which reads in part,

> "The Commonwealth shall be reimbursed to the extent of the total amounts contributable by the employes and to one-half of the amounts contributable by the school district, joint schools and departments."

The Public School Code of 1949 continues to provide for a sharing arrangement with local districts for the employer share of the Social Security payment.[7] The method of making the payment was changed from districts reimbursing the commonwealth, as established by Act 660 of 1956, to the commonwealth reimbursing the districts, as provided for by Act 29 of 1994. The state budget beginning in at least 1972-73 clearly presents the state share of Social Security cost as a line item.[8] The sharing arrangement was re-affirmed as part of Act 29 of 1994 and Act 120 of 2011.

Current subsidy payments

Under the current process, districts are responsible for making the full payment of the employer share of Social Security and are then reimbursed by the state for half of that payment. The Social Security subsidy is currently paid through a predictable formula and commitment by the state. Payment is based on school district actual payroll expenditures. Districts submit monthly payroll information to PDE, which in turn distributes the Social Security subsidy payments based on estimates and uses the data submitted by the districts to make adjustments twice during the year.

Combining Social Security with Basic Education Funding

Combining Social Security with Basic Education Funding (BEF) shifts the subsidy from a formula to amounts established as part of the budget process. Under the rationale provided in the governor's proposed budget, a district would be able to allocate any unneeded Social Security subsidy for alternative uses. The ability relies on an assumption that the districts will be able to reduce salary costs below the current fiscal year and the current subsidy will provide more money than will be required for employer share of Social Security. The key component of the change that is being proposed is the elimination of a predictable Social Security subsidy.

Under the governor's proposed 2012-13 budget, the state would have distributed $504,774,468 to districts as part of the new SAEBG.[9] The Social Security allocated to the SAEBG appears to represent an across-the-board 9.5% increase to every district for this subsidy. However, this 9.5% represents the inclusion of the intermediate units' subsidy for Social Security. The following analysis makes the assumption that the amount of Social Security subsidy included in the SAEBG will grow as part of future budget proposals and legislative adjustments to the proposed budgets. While the SAEBG would have contained additional consolidation of funds as part of the budget proposal, this analysis is limited to the Social Security portion.

Data analysis

The analysis looks at the subsidy and projections from three different views. First, the reviews the current funding structure without a block grant and assumes that it remains unchanged in future years (no SAEBG). In the second and third views, the governor's budget proposal assumes the SAEBG is the basis for analysis. The difference between the second and third views of the analysis is a difference in the assumption about the projected growth of payroll and block grant subsidy. In the first and second views of the analysis, the assumption is that payroll will increase at the historical rate of increase as modified by wage freezes, which is estimated to be 3%. The subsidy increase assumption in the first view is growth equal to growth consistent with the current subsidy calculation. In the second view of the analysis, the assumption is that the SAEBG growth of revenue will be at the historical rate of the BEF subsidy excluding the effect of ARRA funding or a growth assumption of 2%. In the third view of the analysis, the assumption about SAEBG growth and Social Security expenditure growth is reversed with subsidy at 3% and Social Security expenditure at 2%.

Payroll calculations used in this analysis are based on a PSERS-calculated 2010-11 payroll of $11.662 billion dollars. The analysis is limited to school districts and does not included PSERS eligible payrolls for career and technical centers, intermediate units and charter schools. There is a small difference between PSERS-covered payroll and the districts' liability for Social Security payroll. Differences include those positions which do not meet the minimum hours worked requirement for participation in PSERS or salaries which exceed the Social Security income maximum.[10]

View 1 Analysis – Current funding (no SAEBG)

Using the base payroll for 2010-11 and multiplying this by the combined Social Security and Medicare

Table 1 **Projected payroll and Social Security subsidy – No block grant**

	2010-11	2011-12	2012-13	2013-14	2014-15
Projected Payroll*	11,662,780,135	12,012,663,59	12,373,043,45	12,744,234,79	13,126,561,791
Social Security/ Med *	892,202,680	918,968,761	946,537,824	974,933,958	1,004,181,977
Current Sharing **	446,101,340	459,484,380	473,268,912	487,466,979	502,090,989
Added to BEF ***		460,958,270	460,981,250		

*Payroll projected at 3% based on historical rate plus known settlements. Social Security/Medicare based on 7.65% of projected payroll. **Current sharing based on one half of the projected Social Security/Medicare projection. ***Amount of Social Security subsidy added to the SAEBG under the governor's proposed budget along with adjustment for prior year for comparison purposes.

Table 2

Projected payroll and Social Security subsidy – Block grant
Payroll grows at 3%, subsidy grows at 2%

	2010-11	2011-12	2012-13	2013-14	2014-15
Projected Payroll *	11,662,780,135	12,012,663,539	12,373,043,445	12,744,234,749	13,126,561,791
Social Security/Med *	892,202,680	918,968,761	946,537,824	974,933,958	1,004,181,977
State Share **	446,101,340	459,484,380	460,958,270	470,177,435	479,580,984
District Share ***	446,101,340	459,484,380	485,579,554	504,756,522	524,600,993

*Payroll projected at 3% based on historical rate plus known settlements. Social Security/Medicare based on 7.65% of projected payroll. **Current sharing based on one half of the projected Social Security/Medicare projection. ***Amount of Social Security subsidy that is the responsibility of the local districts based on a 2% increase in basic funding.

rate of 7.65% produces an employer contribution of $892.2 million. When shared equally between the state and the districts, this produces $446.1 million share for each in 2010-11. The PDE estimated state share of Social Security for the 2011-12 year is $460,958,270. By increasing the payroll by 3%, the state share increases from $446.1 million in 2010-11, to the PDE estimated for 2011-12 year. This calculation does not include an estimate of non-PSERS payroll. Thus the difference between PSERS covered payroll and Social Security payroll is $1.47 million. Table 1 shows the increases in payroll based on an assumption of 3%. The combined Social Security and Medicare rate of 7.65% is applied to the projected payroll.

The governor's proposed 2012-13 budget added a 9.5% ($43.8 million) across-the-board increase for Social Security. This increase was the redistribution of the state's share of Social Security for intermediate unit employees. Under the governor's proposal, the districts would need to increase their payments to the intermediate units by the amount of the state's share of Social Security.

View 2 Analysis – Block grant (SAEBG enacted)

This analysis looks at the impact of the proposed block grant funding assuming that payroll increases by 3% and the block grant increases by 2%, including the state's share of the Social Security subsidy. Table 2 presents the impact of a 3% salary increase with related Social Security/Medicare based on 7.65%.

As shown in Table 2, assuming projected salary increases of 3% and projected subsidy increases of 2% the result is a shift in the costs of the employer share of Social Security away from the shared funding (no block grant) to the districts (with a block grant). As presented in Table 2, if the negotiated settlements or the need for additional staff increase the covered payroll by more than the increase in the block grant, the cost will shift to the local district.

Table 2 shows what is believed to be the most likely event at the state level. It is even more likely that at the district level, districts impacted negatively will be at disparate rates across the state. Growing or low-wealth districts will have little to no ability to pass this cost on to the local tax base. Districts with no growth or declining market values also will have little to no ability to pass any cost increases on to the local tax base.

View 3 Analysis – Block grant (SAEBG enacted)

The analysis shown in Table 3 presents the impact of the proposed block grant funding assuming that payroll increases by 2% and the block grant subsidy increases by 3%. It is also assumed that the state share of Social Security subsidy is part of the block grant. This view of the analysis of the data shows that the cost would be shifted to the state. Given that the increases presented in this view are not consistent with the historical increase in either salaries or subsidy, then this result is not very likely to occur. It is also noted that the overall subsidy received by districts from the state for 2011-12 and proposed for 2012-13 have actually declined which makes subsidy increases greater than salary increases very unlikely.

Table 3

Projected payroll and Social Security subsidy – Block grant
Payroll grows at 2%, subsidy grows at 3%

	2010-11	2011-12	2012-13	2013-14	2014-15
Projected Payroll *	11,662,780,135	11,896,035,738	12,133,956,452	12,376,635,581	12,624,168,293
Social Security/ Med *	892,202,680	910,046,734	928,247,669	946,812,622	965,748,874
State Share **	446,101,340	455,023,367	460,958,270	474,787,018	489,030,629
District Share ***	446,101,340	455,023,367	467,289,398	472,025,604	476,718,246

*Payroll projected at 2 % based on historical rate plus known settlements. Social Security/Medicare based on 7.65% of projected payroll. **Current sharing based on one half of the projected Social Security/Medicare projection. ***Amount of Social Security subsidy that is the responsibility of the local districts based on a 3% increase in basic funding.

Table 4

Projected District share of Social Security/Medicare cost from Tables 1, 2 and 3

District Share from:	2010-11	2011-12	2012-13	2013-14	2014-15
Table 1 Results: No SAEBG*	446,101,340	459,484,380	473,268,912	487,466,979	502,090,989
Table 2 Results: SAEBG* (Districts pay more)	446,101,340	459,484,380	485,579,553	504,756,572	524,600,993
Table 3 Results: SAEBG** (State pays more)	446,101,340	455,023,367	467,289,398	472,025,604	476,718,246
Proposed Budget***			460,981,250	470,200,875	479,604,893
Table 2 minus Table 1	0	0	12,310.641	17,289,593	22,510,004
Table 3 minus Table 1	0	(4,461,013)	(5,979,594)	(15,441,375)	(25,372,743)

*Based on payroll increase of 3% and subsidy increase of 2%. **Based on payroll increase of 2% and subsidy increase of 3%. ***Projected growth at 2%.

Impact on districts – Comparison of different views

Examining the difference in the estimated Social Security subsidy for 2014-15 for the data presented in Table 1 and Table 2 shows that the shift in the increase favors the state at the expense of the districts. The projected Social Security/Medicare cost in 2014-15 is $502.09 million with equal sharing (no SAEBG). However, the shift shows the states share in Table 2 increases to $479.58 million while the district increases to $524.60 million (with the SAEBG).

Comparing the views with the SAEBG, Table 2 and Table 3, shows that if the payroll grows at a rate greater that the increase in the SAEBG, then the cost shifts to the district. If the reverse occurs and the subsidy grows faster than the payroll, the cost shifts to the state. Given the historical pattern of payroll increases and subsidy increases, the more likely of the two views with the SAEBG is presented in Table 2 where the payroll grows faster than subsidy and the cost shifts to the district.

As shown in Table 4, the current Social Security subsidy with no SAEBG (Table 1) will continue to provide equal sharing of the employer cost. This is the starting point for comparison purposes. Table 2 results, with SAEBG, included the payroll increasing by 3% and the subsidy by 2%, shifting the cost to the district. Table 3 results, with SAEBG, where the subsidy increases faster than the cost, will shift the cost to the state.

Chart 1

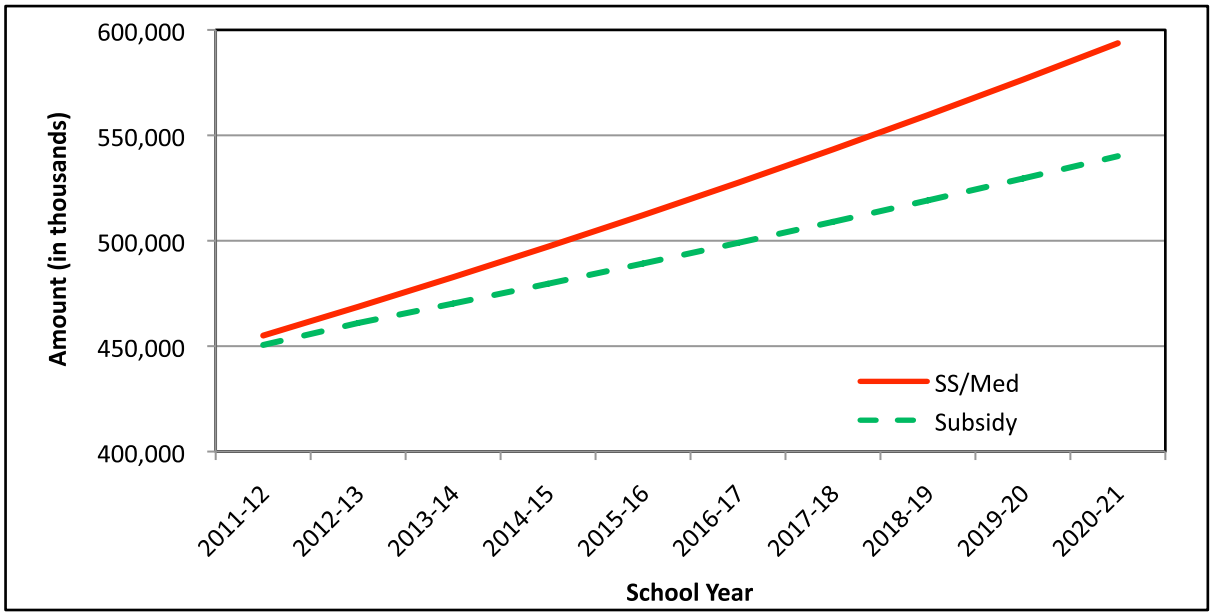

Chart 1 shows the comparison of the district share of Social Security/Medicare under the current subsidy (no SAEBG) and the projected state subsidy with the SAEBG. The assumptions for the projections in Chart 1 are Social Security expenditures will grow by 3% per year and subsidy will grow by 2% per year. The subsidy projection is also adjusted to incorporate the proposed 9.5% increase in the Social Security subsidy included in the budget as part of the SAEBG. Under this projection, the districts will see adverse impact not later than 2019-20.

Districts have limited ability to control cost

A district, in the short-term, has limited ability to control the projected increase in salary and wages paid. Pursuant to the provisions of Act 195 of 1970 and Act 88 of 1992, the professional staffs in all school districts are covered by collective bargaining agreements. Further, a substantial portion of the support employees are also covered by collective bargaining agreements.

While the districts are required to negotiate for salaries and wages, additional provisions of the School Code limit the districts' ability to react to financial issues. Districts are not permitted to lay off teachers for financial reasons.[11] Furloughs are limited to:

(1) Substantial decrease in pupil enrollment
(2) Curtailment or alteration of the educational program with approval by PDE
(3) Consolidation of schools, within a single district, or through a merger of districts

Additionally, school districts are required when they meet the provisions of the School Code to layoff on the basis of reverse seniority in the district. Another limitation on school districts in the School Code states, "A school entity shall realign its professional staff so as to insure that more senior employes are provided with the opportunity to fill positions for which they are certificated and which are being filled by less senior employes."[12]

Another provision of the School Code prevents districts from reducing salaries. This section of the School Code provides, "The salary of any district superintendent, assistant district superintendent or other professional employe in any school district may be increased at any time…, but there shall be no demotion of any professional employe either in salary or in type of position, except as otherwise provided in this act, without the consent of the employe, or, if such consent is not received, then such demotion shall be subject to the right to a hearing before the board of school directors and an appeal in the same manner as hereinbefore provided in the case of the dismissal of a professional employe."[13]

No real flexibility with SAEBG

It is expected that the most likely impact of the SAEBG will be as shown in Table 2 where the cost increases at a rate greater than the subsidy. This means

the district will have no real flexibility as a result of the SAEBG. In fact, districts would probably have less flexibility where higher costs in relation to lower subsidy increases will require shifting from student needs to supplement Social Security expenditures.

Consolidating Social Security funding with the basic education funding does not provide flexibility. If the concept is, "To redesign school and district funding to provide flexibility that allows decision-making to rest with the local school district administrators and local school boards."[14] Then the consolidation of Social Security funding does not achieve the intended outcome.

To the contrary, the history of subsidy increases when applied to the SAEBG will likely force a shift of spending away from students to support Social Security payments. It is even more likely that at the district level, those districts impacted negatively will be at disparate rates across the state. Growing or low-wealth districts will have little to no ability to pass this cost on to the local tax base. Districts with no growth or declining market values also will have little to no ability to pass any cost increases on to the local tax base. Unless the legislature is willing to remove the mandates associated with school district staffing, the ability of school districts to realize the stated goal of flexibility by consolidating Social Security subsidy in the SAEBG will not occur.

The state is set up to come out neutral, while the elimination of a predictable and formulaic system will create winners and losers, and will most likely impact those with the least ability to cover the cost.

Footnotes

[1] Governor's Executive Budget 2012-13, Department of Education, page E15.11.

[2] Governor's Executive Budget 2012-13, Department of Education, page E15.11.

[3] Governor's Executive Budget 2012-13, Department of Education, page E15.11.

[4] Social Security tax rate is found at http://www.irs.gov/pub/irs-pdf/p15.pdf, IRS Publication 15, Circular E Employers Tax Guide, 2012. Income limits found at http://ssa- custhelp.ssa.gov/app/answers/detail/a_id/240/session/L3RpbWUvMTMzNDI0NTQwMy9zaWQvYzZPN1ZzVms%3D, both retrieved April 12, 2012.

[5] Act 491 of 1952 was signed by the governor on Jan. 5, 1952. Provisions of the Act made employee contributions retroactive to January 1951. Further Act 491 created a state agency to administer the provisions of the Commonwealth participation in Social Security.

[6] Act 660 of 1956 amended 24 PS § 2119. This section of the School Code was originally adopted as part of the School Code in 1917 and pertained to employee retirement benefits.

[7] 24 Pa. C.S.A. § 8329, Payments on account of Social Security deductions from appropriations.

[8] "Governor's Budget for 1972-73 Shows $451 Million Increase," Information Legislative Service, PSBA, Harrisburg, PA., Vol. X, No. 17, Apr. 28, 1972, Page 11.

[9] The proposed amount of Social Security funding included in the SAEBG for school districts is found in the supplemental budget detail, 2012-2013 Proposed SAEBG (Excel) , retrieved 4-5-12 from: http://www.education.state.pa.us/portal/server.pt/community/education_budget/8699/student_achievement_education_block_grant/539259.

[10] PSERS eligibility is based on a minimum of 500 hours per year. This may exclude some support positions such as cafeteria employees, substitute aides and janitors. Substitute teachers may also be excluded.

[11] School Code, 24 PS § 11-1124, Causes for suspension.

[12] School Code, 24 PS § 11-1125.1, Persons to be suspended.

[13] School Code, 24 PS § 11-1151, Salary increases; demotions.

[14] Governor's Executive Budget 2012-13, Department of Education, page E15.11.

The PSBA Education Research & Policy Center is an affiliate of the Pennsylvania School Boards Association. The PSBA Education Research & Policy Center is dedicated to the purpose of in-depth research and analysis of issues affecting public education in Pennsylvania.

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