The Challenges of Health and Welfare Benefit Costs for California Districts

Paul Bruno

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Paul Bruno
University of Southern California's Rossier School of Education

Executive Summary

Researchers in the Getting Down to Facts II project showed that while the financial picture has improved in recent years for California's school districts, several important challenges remain. This policy brief explores one of these challenges in greater detail: the costs of health and welfare benefits for district employees.

In reality, employee health benefit costs pose two distinct challenges for districts. First, the cost of providing benefits to each employee has increased substantially over time. Because districts require employees to pay only a relatively small portion of these annual costs, most of the growing costs are directly paid for by districts.

Second, most districts continue to provide health benefits to their employees after they retire. As more workers retire, the costs of these retiree benefits consume a larger share of districts' budgets. Moreover, districts have often not set aside funds to pay for these benefits while employees earn them. In some districts, this has resulted in unfunded liabilities totaling many thousands of dollars per student.

These health benefit costs and liabilities put strain on district budgets. This makes it more difficult for districts to address their other priorities, such as increasing teacher salaries or supplementing services for disadvantaged students. This is particularly true as districts also navigate other financial pressures, such as growing costs for special education programs and teacher pensions.

Districts can and should do more to navigate these health benefit costs and to make sure that they are sustainable. State policymakers may have a role to play as well. Taking these steps will not be easy, and different solutions will be appropriate for different districts. However, postponing these hard choices will only make them more painful.

The Challenges of Health and Welfare Benefit Costs for California Districts

Like many employers, almost all school districts in California offer health and welfare benefits (or health benefits, for brevity) to their active, full-time employees. Most commonly, these health benefit packages include coverage for workers' medical, dental, and vision services, as well as life insurance. Additionally, most districts offer health benefits to some of their former employees. Because these benefits are in addition to any pensions employees receive, they are known as "other [than pensions] post-employment benefits," or OPEBs. Typically, the largest components of these OPEBs are health benefits for retirees. OPEBs can be attractive for teachers in California, who can often retire and begin receiving pension benefits well before they are eligible to enroll in Medicare.

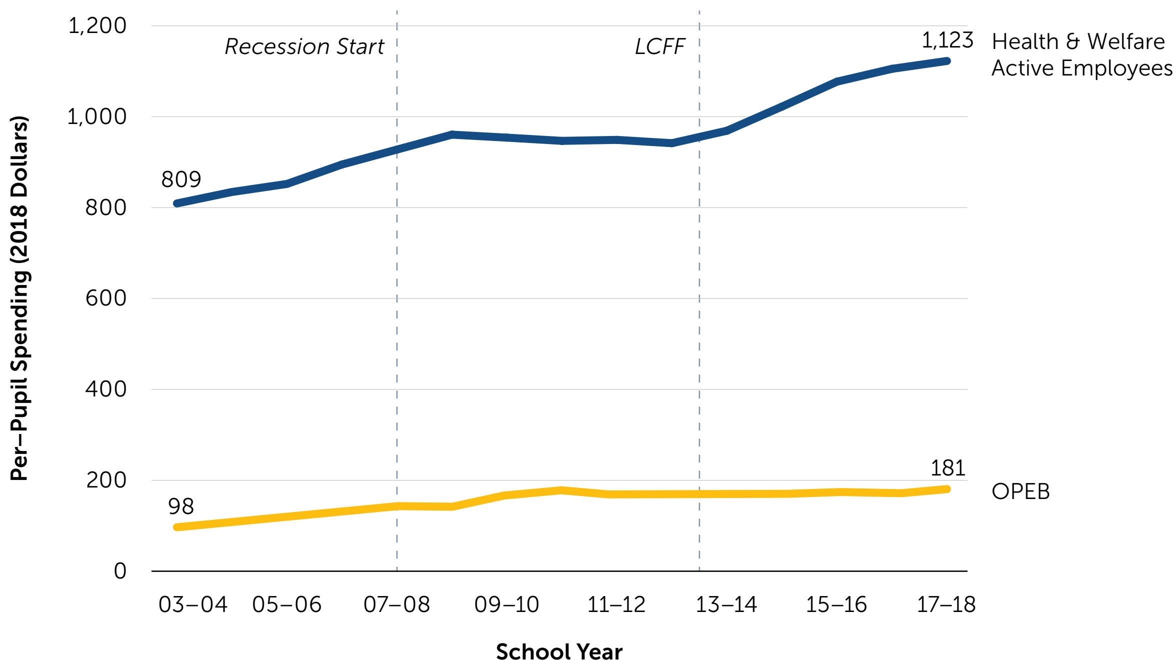
In this brief, I use data from districts' annual financial reports and data on salaries and benefits for district employees to show how the costs of these health benefits have changed since the 2003–2004 school year.[1] I first show that costs for health benefits have grown faster than district spending as a whole and that this is due primarily to higher benefit costs for each staff member. I then highlight ways in which this cost growth and large unfunded OPEB liabilities may put pressure on district budgets. I conclude by discussing steps that policymakers at the state and local levels can take to help districts manage the growth of health benefit costs more effectively.

Health Benefit Costs Have Grown Faster Than Total Spending

Most spending in school districts goes towards staff compensation.[2] In 2017–2018, the most recent year for which data are available, 50 percent of all district spending ($7,455 per pupil) went towards staff salaries.[3] Seven percent of spending ($1,123 per pupil) went towards health benefits for active employees. Roughly 1 percent of spending ($181 per pupil) was for OPEBs. This includes benefits being claimed by former employees and amounts set aside for OPEBs being earned by active employees.

The costs of health and welfare benefits have grown faster than overall district budgets in recent years. Between 2003–2004 and 2017–2018, total district spending per student increased 18 percent ($2,354 per pupil) after adjusting for inflation. As shown in Figure 1, per-pupil spending on health benefits for active employees increased 39 percent (from $809 to $1,123). Per-pupil spending on OPEBs increased by 85 percent (from $98 to $181). All health benefits, including OPEBs, now represent 8.5 percent of all district spending, up from 7.1 percent in 2003–2004.

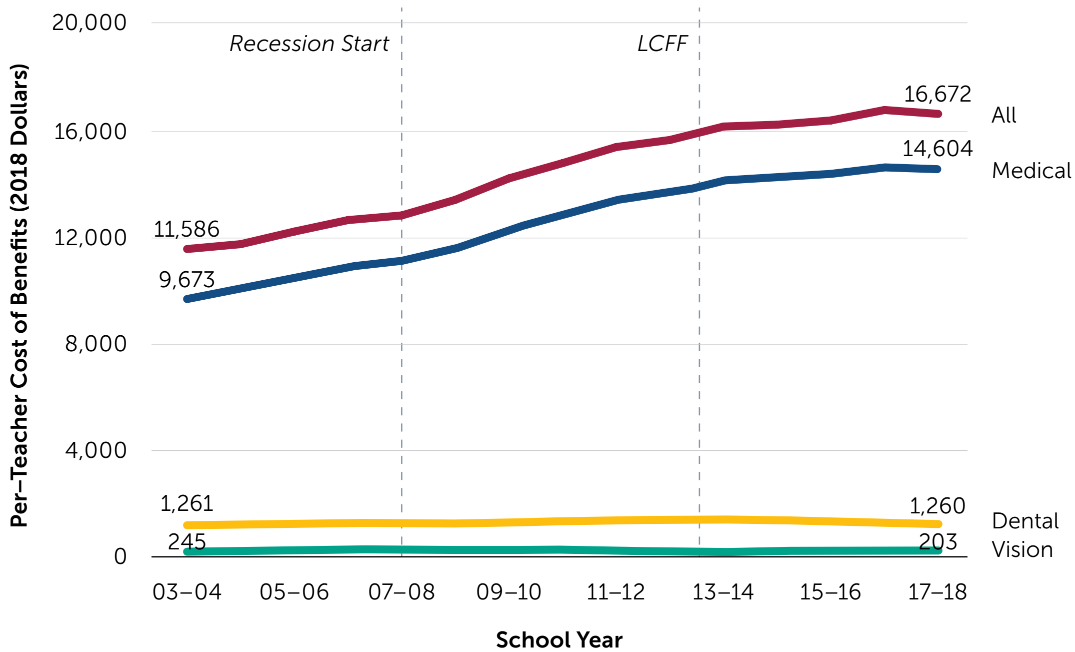
Figure 1. Per-pupil Spending on Health and Welfare Benefits



This growth in health benefit costs is due to two factors. First, districts in California employ slightly more staff for each student than in the past. In 2015–2016, California schools employed one staff member for every 10.9 students, compared to one staff member for every 11.2 students in 2003–2004.[4] Employing more staff per student tends to increase the per-pupil cost of employee benefits, and staffing ratios have likely increased further in the last few years. However, these changes only explain a small portion of the increases in benefit costs.

Second, and more importantly, the cost of health benefits for each staff member is much higher today than in the past. For example, the average annual cost of health benefits per teacher has increased by 44 percent since 2003–2004 (Figure 2). This has been driven primarily by growing per-teacher costs for medical benefits, as opposed to dental, vision, or other benefits. In 2003–2004, the average cost of medical coverage for a teacher was $9,673. By 2017–2018, that had increased by 51 percent, to $14,604. J-90 files do not include detailed benefit data for non-teaching staff, precluding similar analyses for other district employees. However, benefits for teachers are among the largest benefit expenses for districts and benefit packages for different kinds of staff are likely similar within a district.[5]

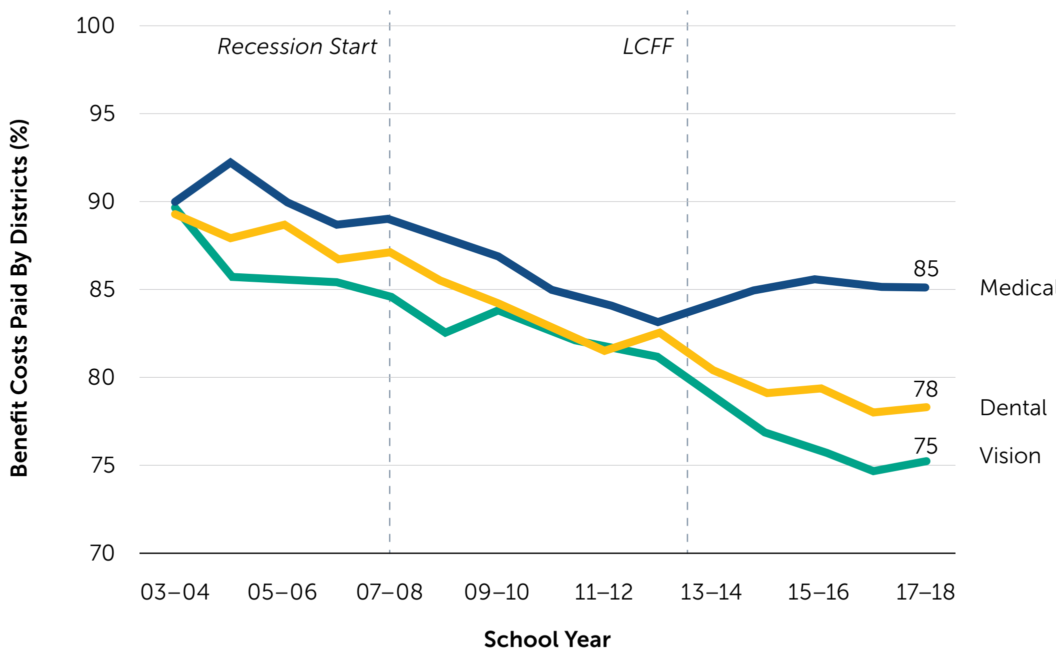
Figure 2. Annual Per-Teacher Cost of Health and Welfare Benefits



This pattern of rapidly increasing per-staff health benefit costs is not unique to school districts or to California. Indeed, these increases are roughly similar to, though perhaps slightly larger than, premium increases observed during this period for employer-provided health insurance nationwide.[6]

However, the challenge of benefit cost inflation is particularly difficult for California districts because they pay a larger share of employee benefit costs than many other employers. Figure 3 shows the share of costs paid by districts for different types of health benefit. For example, in 2017–2018 districts on average paid approximately 85 percent of the cost of their teachers' medical benefits, while teachers paid the remainder. These district contribution rates have fallen over time but remain high; for comparison, other employers often pay between 62 percent and 82 percent of medical plan premium costs on average, depending on the type of plan and the size of the employer.[7] Because districts are responsible for large shares of teachers' benefit costs, when the costs of health benefits increase, districts are responsible for the large majority of the additional expense. Districts are responsible for smaller shares of costs for other health benefit plans—such as those for dental or vision coverage—but as shown in Figure 2 above these other plans represent only a small portion of overall health benefit costs.

Figure 3. Share of Teachers' Annual Benefit Costs Paid by Districts



Districts With Large Health Benefit Expenditures

One way to see the importance of the share of benefit costs paid by districts is to look at districts with the highest health benefit spending. Table 1 lists the 10 districts with the highest per-pupil spending on health benefits for active employees (i.e., excluding OPEBs) and the 10 districts dedicating the largest shares of their total spending to health benefits. Because per-pupil costs are often very high and can fluctuate substantially in smaller districts, Table 1 includes only districts with at least 2,500 students.

Table 1. Districts With the Highest Health and Welfare Benefit Spending, 2017–2018

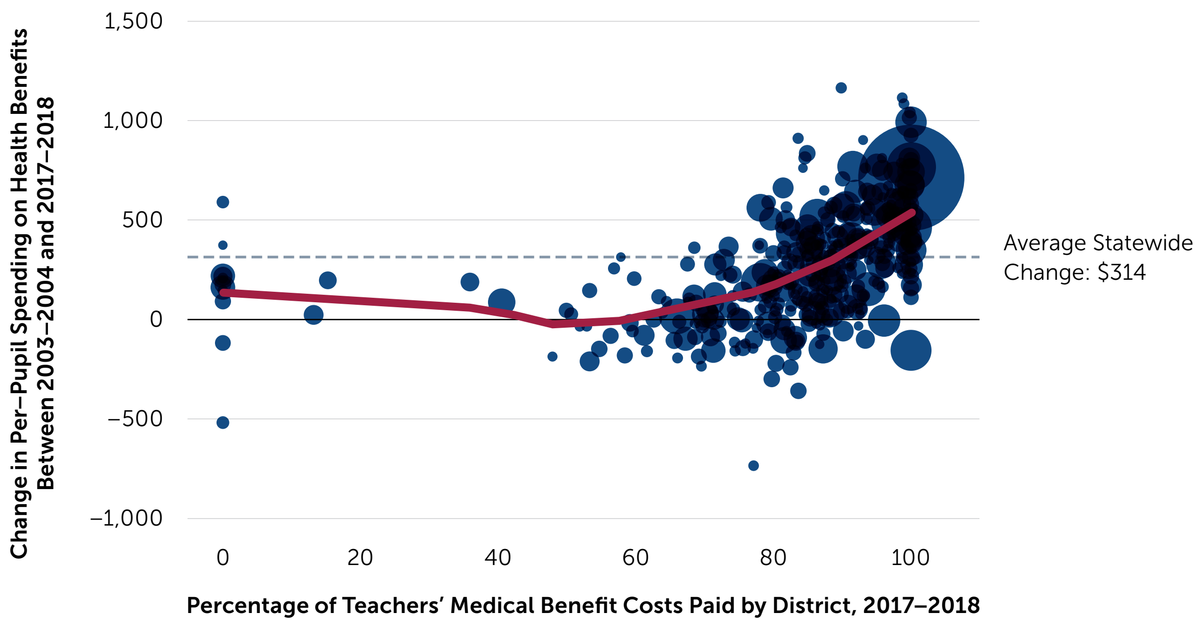
	Health Benefit Spending		% of Teachers' Benefit Costs Paid by District			
District	**Per Pupil**	**% of All Spending**	**Medical**	**Dental**	**Vision**	**Enrollment**
Highest per-pupil spending on health and welfare benefits						
Pajaro Valley Unified	2844	16.9	97.7	98.8	100	18220
Mountain View-Los Altos Union High	2213	9.8	99.8	100	100	4285
Sacramento City Unified	2045	12.6	100	100	100	40508
Solana Beach Elementary	1923	5.6	93	91	100	2916
Albany City Unified	1914	11.3	98.9	100	100	3656
Sequoia Union High	1872	6.2	100	100	100	8837
Coachella Valley Unified	1854	11.0	99.7	100	100	18146
Southern Kern Unified	1838	10.7	98.8	100	100	3560
San Diego Unified	1825	9.1	100	100	100	104454
Washington Unified	1817	11.6	96.1	0	0	2602
Largest percentage of spending on health and welfare benefits						
Pajaro Valley Unified	2844	16.9	97.7	98.8	100	18220
Pacifica	1585	14.1	95.8	100	0	3111
Salinas City Elementary	1681	13.6	88.6	94.7	100	8844
King City Union	1560	13.2	99.1	100	100	2661
Sacramento City Unified	2045	12.6	100	100	100	40508
Anaheim Union High	1627	12.1	100	100	100	30704
Richland Union Elementary	1678	12.1	100	100	100	3031
Bakersfield City	1763	12.1	100	100	100	30699
Victor Elementary	1472	12.1	100	100	100	12479
Los Banos Unified	1454	12.0	87.1	100	100	10863

Note: Excludes districts with fewer than 2,500 students. District contributions to benefit costs come from J-90 files. For Pajaro Valley Unified and Los Banos Unified, district benefit cost shares are taken from 2016–2017 as these districts did not report these figures in 2017–2018.

Whether districts' health benefit spending is ranked per-pupil or as a share of total spending, the highest spending districts pay nearly all of their teachers' benefit costs. Districts in Table 1 commonly pay 100 percent of the costs of dental and vision plans, compared to statewide averages of 78 percent and 75 percent, respectively. They also pay at least 87 percent of annual medical plan costs, typically the largest component of health benefit costs. This places many of these districts well above the statewide average of 85 percent. This is likely a major contributing factor to these districts' high health benefit spending levels. Every district in this table spends at least 29 percent more per pupil on health benefits than the statewide average, and all but two dedicated an above-average share of spending towards health benefits.[8]

Similarly, districts making larger contributions to teachers' health benefit plans have seen faster growth in their health benefit spending. Figure 4 shows inflation-adjusted changes in per-pupil spending on health benefits between 2003–2004 and 2017–2018 for districts paying different percentages of teachers' medical benefit costs.

Figure 4. Changes in Health Benefit Spending by District Contribution Share



Note. Excludes districts with fewer than 2,500 students in 2017–2018. Marker size proportional to enrollment. Health benefit spending includes spending on all health and welfare benefits for active employees excluding OPEBs. Curve is lowess.

Recall that spending on health benefits for active employees increased $314 per pupil for districts statewide since 2003–2004. As shown in Figure 4, this was driven primarily by districts paying 80 percent or more of their teachers' medical benefit costs in 2017–2018. These districts increased their health benefit spending by $400 per pupil during this time. For districts paying 90 percent or more, the increase was even larger: $488 per pupil.

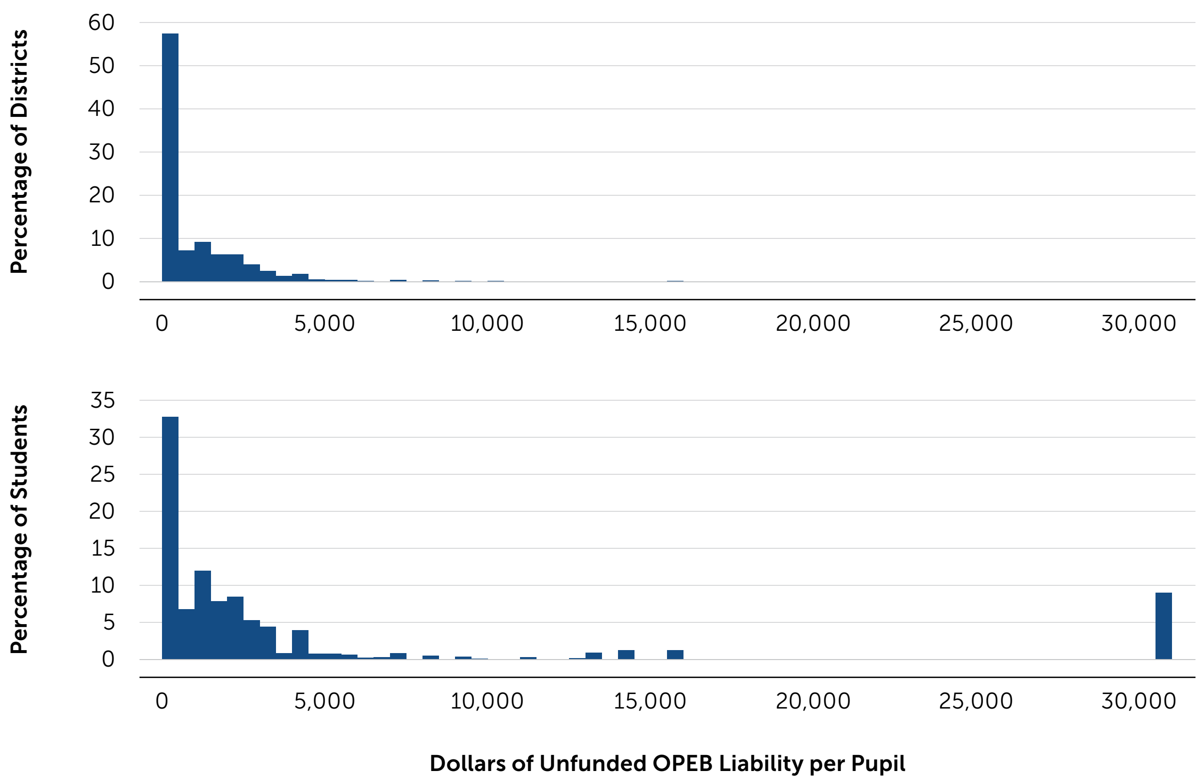
At the same time, districts paying smaller percentages of medical benefit costs saw smaller, if any, increases, perhaps because they had reduced their contribution shares over time or because they were responsible for smaller portions of plan cost increases to begin with. Among districts bearing less than 80 percent of the cost of teachers' medical plans, spending on health benefits increased only $87 per pupil during this period. It is difficult to know what district health benefit costs would have been under different benefit packages, but these patterns suggest that higher per-pupil costs for districts are at least partially the result of districts shouldering high percentages of employee benefit costs.

Districts Also Have Large Unfunded OPEB Obligations

OPEBs represent an additional challenge for many districts. In addition to the fact that health benefit costs are increasing in general, districts have in some cases accumulated large unfunded OPEB liabilities (i.e., OPEBs promised to their employees but for which they have not set aside funds). Statewide, these unfunded OPEB liabilities total approximately $26 billion, or about $4,700 per pupil.

However, as shown in Figure 5 some districts have much larger unfunded OPEB liabilities than others. In fact, half of districts reported less than $5 per pupil in such liabilities. At the same time, approximately one third of districts reported unfunded liabilities of $1,000 or more per pupil and as high as $67,000 per pupil.

Figure 5. Districts' Per-Pupil Unfunded OPEB Liabilities



Note: One district with liabilities greater than $35,000 per pupil excluded.

Districts With Large OPEB Liabilities

Comparing the top and bottom panels of Figure 5 also shows that the largest per-pupil liabilities tend to be in districts with larger enrollments. For example, while 57 percent of districts report unfunded OPEB liabilities of less than $500 per pupil, those districts enroll only one third of students. Meanwhile, the 100 districts with the largest per-pupil liabilities—at least $2,795—represent roughly 10 percent of districts but 28 percent of enrollment. This is in part because larger districts tend to offer more generous OPEBs than smaller districts and are more likely to offer OPEBs at all.

Even within these 100 districts, liabilities are disproportionately concentrated among a small number of districts. Table 2 lists districts with the largest total unfunded liabilities. These 10 districts alone represent roughly three quarters of the unfunded OPEB liabilities held by districts statewide. The Los Angeles Unified School District alone holds more than half of statewide liabilities.

Table 2. Districts With the Largest Total and Per-Pupil Unfunded OPEB Liabilities

Largest Total Unfunded Liabilities			
District	**Total (Millions)**	**Pupils**	**Per Pupil**
Los Angeles Unified	15456	506531	30514
Fresno Unified	996	70648	14098
San Francisco Unified	681	52273	13026
Sacramento City Unified	632	40508	15595
West Contra Costa Unified	443	28318	15635
Long Beach Unified	333	74157	4491
Clovis Unified	300	42720	7014
Chaffey Joint Union High	198	23871	8294
Alhambra Unified	192	16794	11421
Garden Grove Unified	183	43131	4248

Largest Unfunded Liabilities Per Pupil			
	Total (Millions)	**Pupils**	**Per Pupil**
Midway Elementary	6	85	67013
Los Angeles Unified	15456	506531	30514
Eureka City Schools	108	3678	29442
Healdsburg Unified	24	1517	16066
West Contra Costa Unified	443	28318	15635
Sacramento City Unified	632	40508	15595
Fresno Unified	996	70648	14098
San Francisco Unified	681	52273	13026
San Lorenzo Unified	134	10467	12790
Alhambra Unified	192	16794	11421

Note: Liabilities reflect disclosures on J-90 surveys.

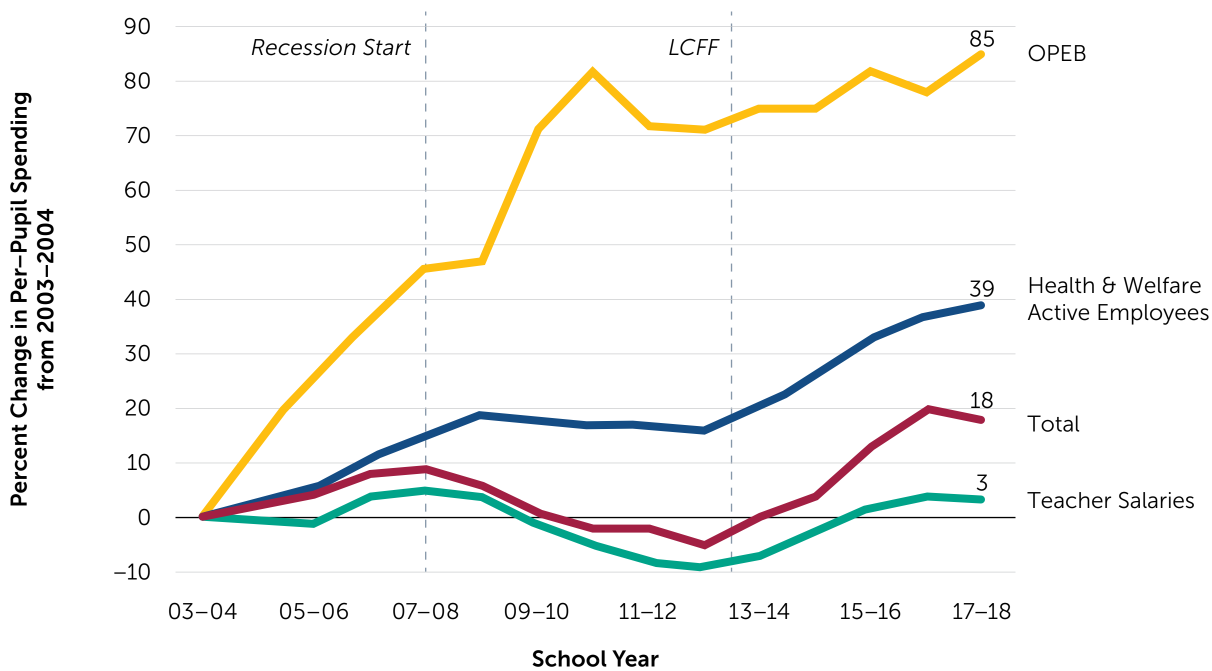
Large liabilities may be easily dealt with by districts with large enrollments. However, Table 2 also shows that in practice these large aggregate liabilities typically translate into large per-pupil amounts that may be difficult to manage. For example, in 2017–2018 the 10 districts with the largest total unfunded OPEB liabilities also had per-pupil liabilities of at least $4,248. They also spent $627 per pupil on OPEBs for active and former employees, or 3.5 percent of their total spending (not shown). Table 2 also lists the 10 districts with the largest per-pupil liabilities, and some of these districts have per-pupil liabilities that are larger still. These districts spent $734 per pupil on OPEBs, or 4 percent of their total spending, four times the statewide average.

Changes to governmental accounting standards have increasingly required districts to document OPEB liabilities and the extent to which they have been funded.[9] Accordingly, districts increasingly report setting aside funding for these OPEB benefits as employees earn them. However, large, previously unfunded liabilities often remain, and in many cases districts do not make the full annual contributions to their OPEB programs that would be required to fully cover their liabilities for both current and former employees.[10]

Health Benefit Costs Put Pressure on District Budgets

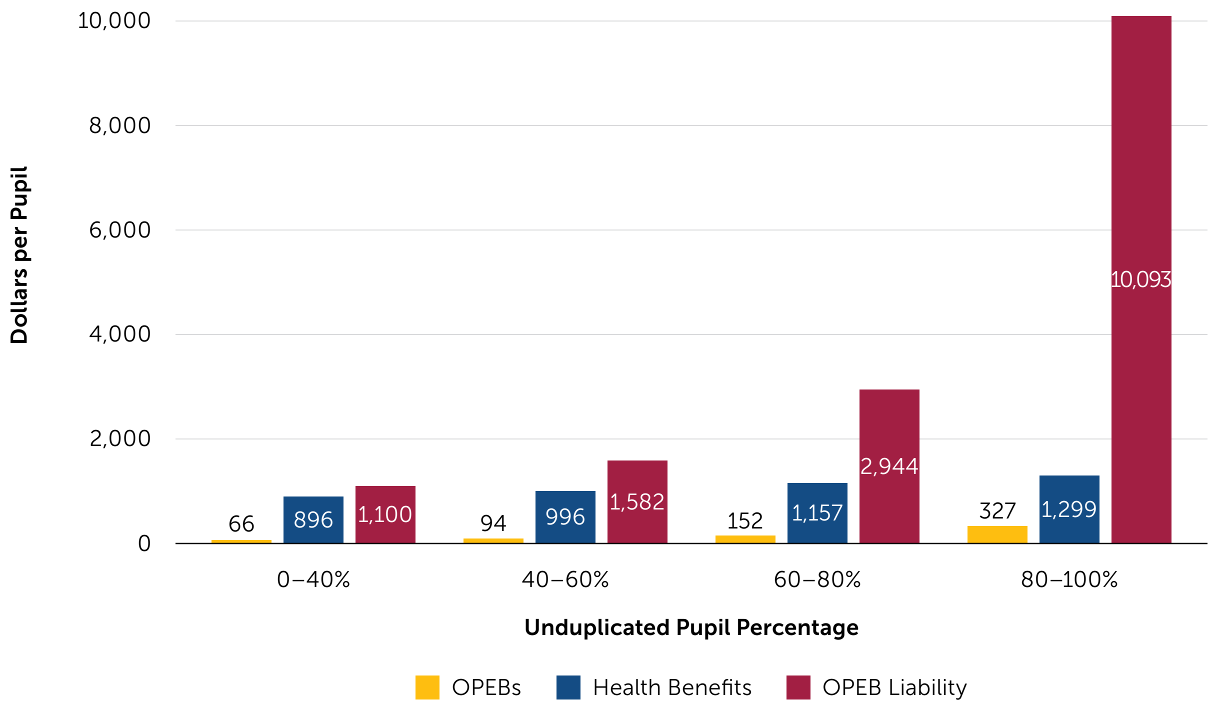
Growing health benefit costs are concerning for two reasons. First, growing benefit costs likely limit districts' abilities to pursue other priorities, such as teacher salary increases. As shown in Figure 6, spending on teacher salaries per pupil has increased only 3 percent since 2003–2004 after adjusting for inflation, even as total spending has increased by 18 percent. Accordingly, during this period average teacher salaries increased only 5 percent—from roughly $78,000 to $82,000—even as teachers became slightly more experienced (and thus earned higher salaries) on average (not shown). Whether districts would have made larger increases in teacher salary spending if faced with lower health benefit costs is uncertain. However, money spent on health benefits must come from somewhere in the budget and, at a minimum, higher health benefit costs make salary increases more difficult.

Figure 6. Changes in Per-Pupil Spending Since 2003–2004



Higher spending on health benefits may also make it more difficult for districts to provide targeted educational services for students prioritized under the Local Control Funding Formula: students who are low income, English learners, or in the foster system, so-called "unduplicated pupils." This is particularly concerning given that, as shown in Figure 7, OPEB and health benefit spending and unfunded OPEB liabilities all tend to be higher on a per-pupil basis in districts in which these unduplicated pupils represent a larger percentage of enrollment.

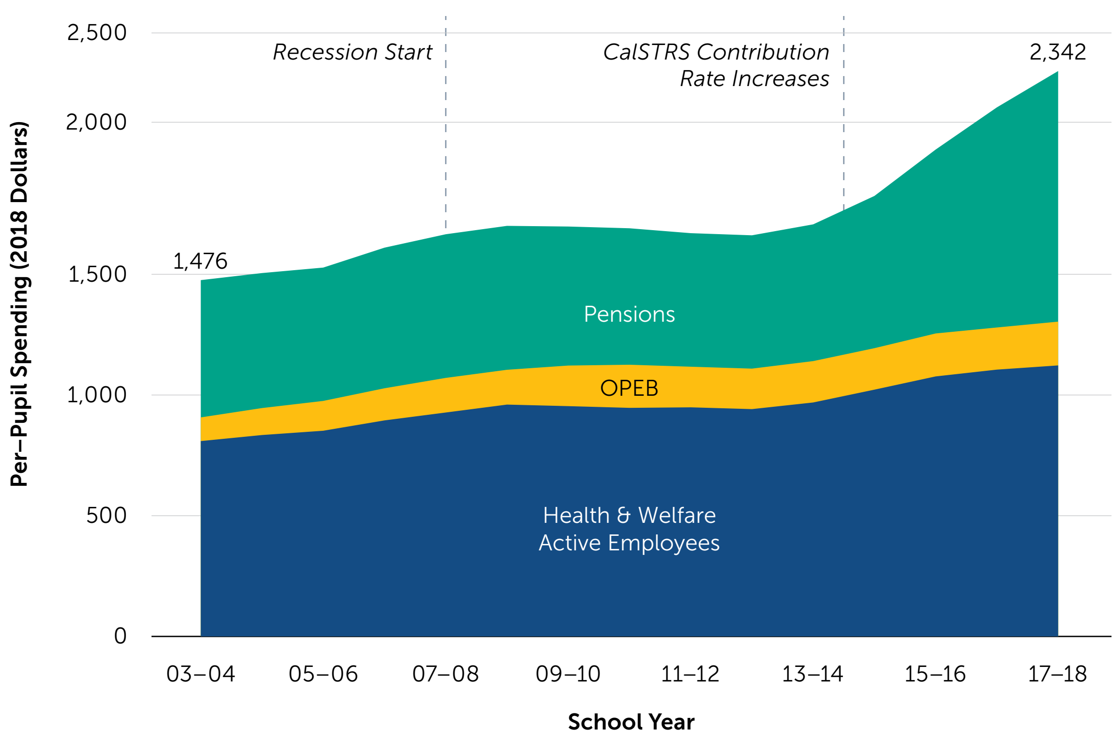
Figure 7. OPEB and Health Benefit Spending and Unfunded OPEB Liabilities by District Unduplicated Pupil Shares



Second, OPEB liabilities will remain and benefit costs are likely to continue rising even if district revenues stagnate or decline. As shown above in Figure 6, spending on neither OPEBs nor health benefits for active employees fell substantially after the start of the Great Recession, even as total spending fell dramatically. And growing revenues in the LCFF era may have obscured liabilities and cost increases in recent years, but there is no guarantee that this revenue growth will continue.

Even if the state economy remains strong and district revenues hold steady, districts may struggle to navigate these cost pressures due to other looming financial challenges. For example, to address funding shortfalls in the state's teacher pension plan (the California State Teachers' Retirement System, or CalSTRS), California legislators increased the contributions that districts must make to CalSTRS from 8.3 percent of teachers' salaries in 2013–2014 to 14.4 percent in 2017–2018. As shown in Figure 8, this has contributed to substantial increases in districts' total pension spending. Districts in 2017–2018 spent $1,038 per pupil on pension contributions for their employees, an increase of 83 percent ($472 per pupil) from 2013–2014. Districts now spend almost as much on pensions as they do on health benefits for their active employees ($1,123 per pupil). Moreover, the statutory contribution rate to CalSTRS will continue to increase for districts over the next several years, to 19.1 percent of teachers' salaries by 2020–2021.[11] In the coming years, districts will need to manage their health benefit costs while simultaneously making these larger payments to staff pension plans.

Figure 8. Spending on Health Benefits and Pensions



Policymakers Can Take Additional Steps to Manage Health Benefit Costs

School districts in California are required by law to negotiate their health benefit packages locally. This may complicate potential state involvement in these issues and makes it difficult to generalize about districts' challenges. However, local control and diversity among school systems also mean that districts can learn from each other about how to handle these growing cost pressures.

For example, there is evidence that some districts in California are trying to limit their health benefit costs by requiring employees to pay a larger share of health plan costs. As shown above, in Figure 3, teachers in California now pay 15 percent of the annual cost of their medical coverage, up from 10 percent in 2003–2004. Some evidence indicates that when teachers pay a larger portion of their benefit costs, districts save money both because teachers are paying more of the cost of each plan and because teachers enroll in cheaper plans.[12]

However, the total effects of such changes will depend on what districts do with the savings and how much teachers value different types of health benefit. One concern with reducing the share of benefit costs paid by districts is that this may effectively reduce teachers' (or other employees') total compensation. However, if districts use the resulting savings to increase salaries, teachers have the option of using that salary to buy additional health benefits. The average teacher, therefore, may be no worse off—and may be better off—under such a system. Additionally, districts may be able to help their employees bear a larger share of their health benefit costs by offering so-called "cafeteria" plans, such as flexible spending accounts. These plans allow workers to have a portion of their salary redirected to an account that can be used pay for certain kinds of health services. Because these salary deductions can be made on a pre-tax basis, they effectively make health benefits cheaper for employees to buy.

Some districts also appear to be taking steps to reduce or better manage OPEB costs. For example, OPEB packages appear to be becoming slightly less generous. Compared to 2011–2012, fewer districts in 2017–2018 offered health benefits to retirees for life, to retirees over age 65, or to retirees at all. And among districts that do offer health benefits for retirees, these benefits expire at a slightly lower age on average, or after a smaller number of years.[13] Some districts are also requiring that teachers serve longer in the district to earn OPEBs. Districts are also increasingly funding their retiree benefits as teachers earn them, which both prevents the accumulation of large unfunded liabilities and saves money over the long term because investment returns can be used to pay for a portion of the benefits.

Other policy levers may exist at the state level. Some states require at least some prefunding of OPEBs. For example, states can require that active employees contribute a portion of their compensation towards the cost of their own future retirement benefits. However, states requiring such OPEB prefunding also typically administer the OPEB program themselves. Such rules and regulations may be more complicated in California, where OPEB packages are negotiated and administered locally.

More general approaches may be possible for state policymakers even if direct involvement in the management of district benefit packages is not. For example, some states adjust district funding for differences in the cost of workers in different areas.[14] Districts with the largest benefit expenditures and OPEB liabilities are often in locations where college graduates earn high salaries. These higher-cost districts would tend to benefit most from such adjustments, making their health benefit costs more manageable and may in any case need to offer more generous benefits to attract staff.

Conclusion

It seems clear that health benefit costs represent an important challenge for California's school districts. On the one hand, districts need to offer attractive compensation packages, including health benefits, to effectively recruit and retain teachers and other staff. On the other hand, costs of health benefits have grown rapidly, are consuming growing shares of districts' budgets, and may be preventing districts from investing in other priorities. This is particularly true for those districts that offer the most generous health benefit packages to their employees and for those that have accumulated large unfunded OPEB liabilities. However, all districts must navigate the pressures associated with health care cost inflation and may find this particularly difficult if revenue growth slows or reverses.

Different districts will likely require different strategies to address these challenges. Any strategy will likely require hard choices between competing district priorities, such as balancing health benefits against higher salaries, or higher per-staff compensation against higher staffing levels. However, it is essential that districts confront these challenges directly, and as early as possible. Postponing these choices will only make them more difficult and painful.

Endnotes

[1] Expenditure data come from district reports using the state's standardized account code structure (SACS). Staff compensation data come from "Salary and Benefits Schedule for the Certificated Bargaining Unit" (J-90) surveys.

[2] Bruno, P. (2018). District Dollars 2: California School District Finances, 2004–5 through 2016–17. *Getting Down to Facts 2*: Stanford, CA.

[3] All figures are in 2018 dollars. Per-pupil figures are enrollment weighted and include charter schools that report their expenditures to the state in SACS as part of the district's general fund. I use total spending rather than limiting my analysis to day-to-day operational spending because common definitions of operational spending, such as California's official "current expense of education," typically exclude retiree benefits (i.e., OPEBs). Total expenditures include spending on facilities and debt service, which can make figures more volatile from year to year. Results are qualitatively similar if operational spending is used, if all charter schools are excluded, or if average daily attendance (ADA) is used. However, health benefits represent a larger share of operational spending than of total spending, and per-pupil OPEB liabilities are larger if all charter school enrollments are excluded.

[4] U.S. Department of Education, National Center for Education Statistics, Common Core of Data (CCD), "State Nonfiscal Survey of Public Elementary/Secondary Education," 2000–01 through 2015–16.

[5] Benefit data from J-90 files include staff other than teachers (e.g., nurses) if they are paid on the teacher salary schedule.

[6] Claxton, G., Rae, M., Long, M., Damico, A., & Whitmore, H. (2018). Employer Health Benefits: 2018 Annual Survey. San Francisco, CA: Henry J. Kaiser Family Foundation.

[7] Ibid.

[8] The Solana Beach Elementary and Sequoia Union High districts have above-average per-pupil spending levels in most years and had particularly high spending in 2017–2018 (up to approximately $34,000 per pupil) due to unusual facilities spending. This reduces the share of all spending they dedicate to health benefits.

[9] Governmental Accounting Standards Board Statements 45 (2004) & 75 (2015).

[10] Bruno, P. (2018). District Dollars 2: California School District Finances, 2004–5 through 2016–17. *Getting Down to Facts 2*: Stanford, CA.

[11] Koedel, C., & Gassmann, G. E. (2018). Pensions and California Public Schools. *Getting Down to Facts 2*: Stanford, CA.

[12] Costrell, R. M. (2015). *District Costs for Teacher Health Insurance: An Examination of the Data from the BLS and Wisconsin*. In *Productivity for Results: Vol. 8*.

[13] Author's calculations from J-90 files. School districts in California are required by law to allow retired teachers, and certain other types of retirees, to purchase medical coverage through the district at their own expense. This option is not considered an OPEB because retirees bear the full annual cost.

[14] Imazeki, J. (2018). Adequacy and State Funding Formulas: What Can California Learn from the Research and National Context? *Getting Down to Facts 2*: Stanford, CA.

Author Biography

Paul Bruno is a Ph.D. candidate at the University of Southern California's Rossier School of Education and a former middle school science teacher. He studies teacher quality, teacher labor markets, school choice, and school finance.

About

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PACE
Policy Analysis for California Education

Stanford Graduate School of Education
520 Galvez Mall, CERAS 401
Stanford, CA 94305-3001
Phone: (650) 724-2832
Fax: (650) 723-9931

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