STATE OF TENNESSEE
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Justin P. Wilson
Comptroller

March 28, 2011

The Honorable Mark Emkes
Commissioner, Department of Finance and Administration
State Capitol
Nashville, Tennessee 37243
And
The Honorable Patrick Smith
Acting Commissioner, Department of Education
Andrew Johnson Tower
Nashville, Tennessee 37243

Re: Basic Education Program Insurance Premiums

Gentlemen:

Our office recently received information that indicated that the state share of the insurance premium component of the Basic Education Program (BEP) is calculated in a manner that perhaps differs from external expectations.

The component of the BEP formula at issue relates to teachers' and other employees' health insurance premiums. Currently, the appropriations bill states that the State of Tennessee funds an amount not to exceed 45% of the total statewide cost of participation in the insurance plans for instruction and classroom positions funded through the BEP formula. The calculation is based on average monthly insurance premiums for all individuals participating in the state insurance plan.

During our interviews with various individuals in state government and the education community, we found the common understanding is that the state covers an average of 45% of annual health insurance premiums for these categories of employees. As such, the expectation is that the local education agencies (LEAs) must in turn be responsible for at least 45% of the insurance premiums for such employees who choose to have health insurance. Section 8-27-303(j)(1), *Tennessee Code Annotated,* states each LEA shall pay, as a minimum, the percentage specified in the appropriation act.

The BEP formula, however, only considers 10 of 12 months of insurance premiums. Therefore, the state's formula is, in effect, funding 45% of 10 of the 12 months of insurance premiums, resulting in an actual annual average percentage nearer 37.5%. The state does not fund 45% of the aggregate annual average insurance premium amount. LEAs, in contrast, are required to pay insurance premiums for each of the 12 months in a year, and to cover the 2 months not funded by the state. The extra 2 months are not part of the formula, even though the BEP formula is intended to estimate a sufficient amount of funds to provide a basic level of education for Tennessee students.

After extensive interviewing efforts, we were not able to get a definitive answer to the reasons why the calculation would only cover 10 months of insurance premiums that have to be paid for 12 months when the other components of teachers' compensation, such as salary, Social Security, and retirement, would be considered in the formula in total.

During our interviews, we determined that actual knowledge of the 10-month calculation was sparse and mostly concentrated in the Department of Finance and Administration (F&A). Some Department of Education employees became aware of the mechanics of the calculation in 2007. At that time, F&A staff had discussed phasing in funding for the remaining two months, but indicated the department was unable to initiate a phase-in plan due to lack of funding in the declining economy. From these discussions, the Education employees were under the impression that the 10-month calculation was an error but that there was not currently money available to fix the error.

According to F&A's Budget Office Director, the calculation of health insurance premiums on a 10-month basis began in 1993, was a policy decision in development of the BEP formula, was revisited and not changed in later years, and was continued in every subsequent appropriations bill, including the appropriations bill for fiscal year 2010-2011.

The Budget Office Director said that the logic of calculation premiums on a 10-month basis is that salaries are funded for 10 months of work and that other benefits (retirement contribution and FICA, or social security and Medicare contributions, which are a percentage of salary) also are based on 10 months.

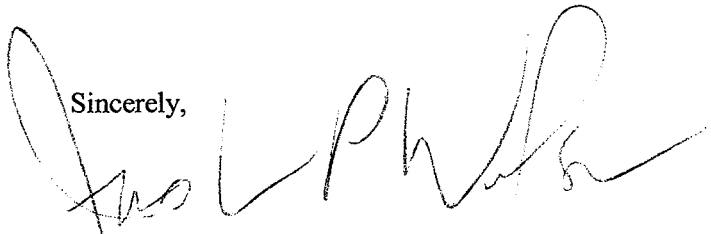
The views of the Budget Director are consistent with speculations by, and recollections of, some current and former F&A employees, that when the formula was initially developed in the 1990s, the state made a policy decision to include the funding for insurance premiums for only 10 months each year, since at the time most teachers only worked 10 months out of the year. Another rationale provided was that funding constraints were considered in making an adjustment to this BEP component.

The Budget Office Director also stated that even if funding of a state share of health insurance benefits on a 10-month basis were viewed as a mistake, rather than a policy decision, the provisions of law limiting the distribution of BEP funds to the appropriation made and providing a prorating method in such cases, would have resulted in no greater distribution of BEP funds to the local education agencies in each year. The Budget Office Director stated, however, that this was a policy decision, remains a policy decision, and that, in his opinion, the BEP formula has been and is at full funding.

F&A's Budget Office Director told us that the appropriations bill being drafted for 2011-2012 reflects the calculation of the state share of the health insurance premiums on a 10-month basis, continuing the policy decision of the last 19 years. The Budget Office Director estimates that an additional annual outlay of $58 million would be required to fund the extra 2 months for fiscal year 2011-2012.

The mechanics of the BEP formula are a policy matter. Because the intricacies of the BEP funding formula are not necessarily transparent to the education community or members of the General Assembly, and because the state share of the insurance premium component is a significant aspect of BEP funding, we believe that it is important, and timely, to draw attention to this matter.

Sincerely,



Justin P. Wilson
Comptroller of the Treasury

cc: The Honorable Randy McNally, Chair, Senate Finance, Ways and Means
The Honorable Charles Sargent, Chair, House Finance, Ways and Means
The Honorable Dolores Gresham, Chair, Senate Education
The Honorable Richard Montgomery, Chair, House Education