

BLUE MODEL BLUES

Another Way Pension Liabilities Are Mismeasured

Regular readers of this blog know that a pension meteor is headed for state and local governments, and that deceptive accounting practices obscure the likely scope of the destruction. The biggest source of confusion has to do with rates of return: Most pension funds assume that their assets will grow at rates of seven to eight percent per year indefinitely, a virtual impossibility in this age of low interest rates and sluggish growth.

A recent *Governing* magazine report highlights another way liabilities can be mismeasured. Many taxpayers live in jurisdictions that are on the hook for pensions from many different government agencies, including city governments, county governments, and school districts. So while the per capita pension debt for the City of Denver is just \$709 per capita, for example, the “overlapping” obligations on its taxpayers are actually nearly eight times that high:

At the end of fiscal year 2015, Dallas had an unfunded pension obligation of \$1,371 per capita. Denver’s was barely half that at \$709 per capita. From that number alone we might conclude that Denver is in much better financial shape.

But now let’s add a few crucial layers of complexity. First count up each city’s “overlapping” pension obligations. Overlapping means two or more jurisdictions share some portion of their respective property tax bases. We can think of a region’s property tax base like money in a shared savings account: When one jurisdiction takes money out, there’s less for everyone else.

Dallas shares parts of its property tax base with 20 other governments, including counties, schools, hospitals and community colleges. These other entities’ unfunded pension obligations add up to \$1,362 per capita. Denver shares its tax base with just one other entity — the Denver School District — but that district’s pension obligation is a comparatively high \$4,876 per capita. So Dallas’ total direct and overlapping pension obligation is \$2,733 per capita; Denver’s is \$5,585.

Estimating the true cost of unfunded pension obligations is a messy business. Numbers publicly touted by politicians, unions and the actuaries they employ tend to downplay the \$3.4 trillion problem and the existential threat it poses to blue model governance nationwide.

A sustainable fix to America's public pensions will likely require intensive reforms to state and local governance, including the replacement of defined-benefit plans with 401(k)s and robust checks on the lobbying and political power of public sector unions. But the first step toward implementing these changes is for public administrators to come clean with taxpayers about the extent of the mess they are in. Until public sector pension funds are governed by the same rigorous accounting rules that apply in the private sector, it's likely that instead of gradual reforms, states and localities will continue to govern by crisis, propping up the current system with every last cent and then declaring bankruptcy or asking for bailouts when it all comes tumbling down.

Posted: Today at 11:05 AM