Pew Study Finds States Face $2.73 Trillion Bill for Retiree Benefits

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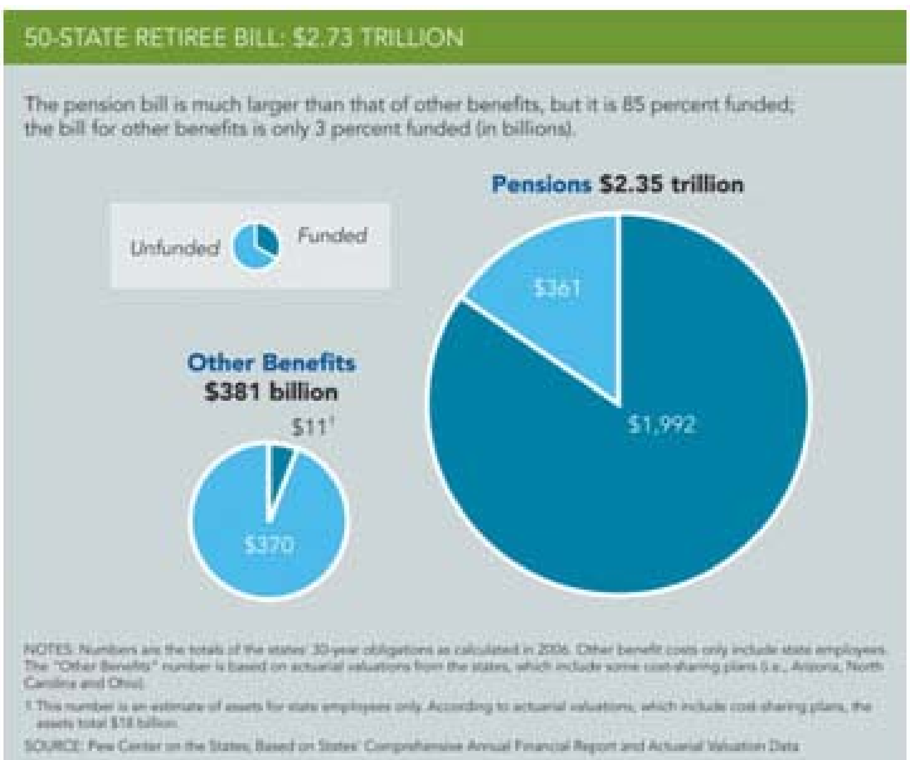
States have promised at least $2.73 trillion in pension, health care and other retirement benefits for public employees over the next three decades, according to a report released today by The Pew Charitable Trusts' Center on the States. *Promises with a Price*, the first 50-state analysis of its kind, finds that states have saved enough to cover about 85 percent of their long-term pension costs, but only 3 percent of the funds needed for promised retiree health care and other non-pension benefits. All told, states already have set aside about $2 trillion to meet their long-term obligations. But they still need to come up with about $731 billion—a conservative figure that does not include all costs for teachers and local government employees.



“Now we know the magnitude of this bill—and paying it will require an enormous investment of taxpayer dollars,” said Susan Urahn, managing director of the Pew Center on the States. “For states that have dug themselves into a deep hole, there are no quick and easy solutions—but there are fiscally responsible steps all states can take. These will require time, attention and, above all, political will.”

Pensions

Nationally, state pension plans are in reasonably good shape. At the end of fiscal year (FY) 2006, states had set aside over $1.99 trillion of the $2.35 trillion they had made in pension promises—leaving about $361 billion unfunded.

But the good news nationally masks important variations across the states:

- Over the past decade, only a third of the states have consistently set aside the amount their own actuaries said was necessary to cover the cost of promised benefits over the long term.
- Twenty states had funding levels of less than 80 percent at the end of FY 2006—below what most experts consider healthy.
- Several states have seen particularly troubling drops in their pension funding levels. Some of the biggest drops have occurred in Hawaii, Kentucky, New Jersey, Pennsylvania and Washington.

Retiree Health Care and Other Benefits

For years states have been required to publicly report their long-term pension liabilities. Until now, they have not had to disclose the price tag of non-pension benefits, such as health care, dental and life insurance. Because of a new rule by the Governmental Accounting Standards Board, states will identify these costs in their FY 2008 financial reports, which are expected to come out between December 2008 and March 2009. The Pew Center on the States has developed a first-of-its-kind preview of these numbers.

Pew found that states’ long-term price tag for retiree health care and other non-pension benefits is about $381 billion for state employees alone (excluding obligations for teachers and other local government workers). About 97 percentof that 30-year obligation was unfunded at the end of FY 2006.

Other key findings include:

- Only six states—Arizona, North Dakota, Ohio, Oregon, Utah and Wisconsin—were on track at the end of FY 2006 to have fully funded their non-pension promises for the next 30 years.
- Half of the states account for almost 94 percent of the non-pension liabilities.
- None of the five largest states—California, Texas, New York, Florida and Illinois—had put aside money for non-pension benefits as of FY 2006.
- Per capita costs for retiree health care and other benefits range from less than $200 in North Dakota, South Dakota and Wyoming to more than $5,000 in Delaware, Hawaii and Connecticut. (Note that per-capita statistics do not tell the whole story because they do not take into account state differences in wealth or ability to pay the bill.)
- Eleven states face long-term liabilities in excess of $10 billion. These include New York at $50 billion, California at $48 billion, and Connecticut and New Jersey at nearly $22 billion each.

Promising Approaches

Promises with a Price finds that while there are no quick and easy solutions, states can take steps to reduce their liabilities. For example, West Virginia reduced its long-term bill coming due for its non-pension benefits by more than half, from an estimated $7.8 billion to $3.4 billion, after setting up a trust fund for payments and adopting several other reforms.

“States have the means to control their destinies. They just have to have the political will to do so,” said Katherine Barrett, co-author of the report. “For a state to succeed, it must use reliable data and good planning, carefully analyze whether proposed new benefits are affordable, and, above all, do its best to make full payments each and every year to reduce the long-term cost.”

A range of promising approaches are in play across the country. An increasing number of states are both setting aside money and restructuring benefits to reduce costs:

- At least five states—including Ohio, Washington and Oregon—offer hybrid pension plans that combine elements of both defined benefit and defined contribution plans.
- Some states are raising the retirement age and closing loopholes within pension systems that allow employees to inflate the amount they collect after retirement.

- For non-pension benefits, states are increasing premiums and co-pays and raising the number of years of employment required for lifetime or fully subsidized benefits, among other reforms.
- At least 13 states have set up irrevocable trusts to pay for retiree health care in years to come.

About the Methodology

Promises with a Price, written by Katherine Barrett and Richard Greene, involved extensive data collection, a thorough analysis of actuarial studies and evaluations, and interviews with experts and individuals knowledgeable about particular states. For the pension systems, the Pew Center on the States examined state annual reports with information over 10 years. Data for this section were obtained from State Comprehensive Annual Financial Reports (CAFR), as well as CAFRs from state pension systems. For non-pension benefits, Pew reviewed CAFRs and the preliminary actuarial assessments completed for most states of their non-pension liabilities over the next 30 years. Several states have not completed their actuarial evaluations. The research was augmented with interviews with actuaries, economists, state controllers, auditors, legislative analysts and other experts in the field.

About Pew

The Pew Charitable Trusts applies the power of knowledge to solve today’s most challenging problems. The Pew Center on the States identifies and advances effective policy approaches to critical issues facing states.