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Reigning in State Pension Liabilities

by Romina Boccia
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From the Wall Street Journal:

> The new Republican House leadership, whose party benefited in November from public antipathy toward the bailout of banks, is moving to avoid a federal bailout of state and local pension funds.
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> Congress has little authority over, or responsibility for, state and local public-employee pensions. But with pension liabilities increasingly stressing state and municipal finances, the prospect that the problem will end up in Washington's lap has some academics and politicians urging that the federal government move preemptively.
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> The latest wrinkle: A bill introduced last week by three prominent House Republicans to deny states and localities the ability to sell tax-exempt bonds-the lifeblood for many governments-unless they report their pension-fund liabilities to the Treasury Department. The federal tax-free status of interest on municipal bonds helps generate demand for the bonds and lowers government borrowing costs.

This is a great bill which could help solve a long-due problem. State and local governments have been living beyond their means for too long, and the federal government should stop subsidizing irresponsible spending, especially since the Feds are also relied upon as lenders of last resort. Almost nothing is currently constraining state spending, placing a huge looming crisis at taxpayer's doorsteps.

States are getting, in essence, access to subsidized debt through tax-exempt bonds. As long as they budget responsibly, that's no big deal. However, states have been building up huge amounts of debt over the past 10 years to fund routine budget shortfalls for perks such as generous pension benefits. No one knows what the overall outstanding liabilities on state pension funds are. We do know that total state and local bond debt jumped 92 percent between 2000 and 2009-from $1.2 trillion to $2.3 trillion. However flawed current pension liability estimates may be, even conservative estimates suggest the liabilities are high enough to put the U.S. government in a serious dilemma when states begin defaulting on their generous pension promises. Federal government bail-outs will almost certainly be the outcome.

What needs to be done to solve this looming crisis are major budget reforms and cuts. Public sector unions present the largest barriers to such necessary restructuring. A study by the Cato Institute on employee compensation in state and local governments finds that public sector pay averaged $39.66 per hour in 2009, which was 45 percent higher than the private sector average, when accounting for wages and benefits. While private sector unions are constrained by the fact that higher business costs lead to lost sales and fewer jobs, public sector unions face no such constraint, and even well-intended government officials trying to reign in state and local pension liabilities have little bargaining material to go up against unions.

This bill would do much to constrain states and localities from spending irresponsibly and it would force public unions to cooperate with government officials to do what's necessary to reign in ever-growing pension liabilities. If this bill does not pass, I fear out-of-control state and local spending will burden current and future taxpayers by further adding to the federal deficit.