Research may help states address unfunded retiree liabilities

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Research shows that, nationally, states are facing more than $550 billion in unfunded liabilities associated with health care and other non-pension benefits for retired state employees, a situation many states are now struggling to fix. New research from North Carolina State University has identified a number of trends that are consistent among those states with the biggest funding problems - information that may help states find a solution to the funding shortfall.

"We've identified some state government characteristics that seem to contribute to these unfunded liabilities, and have found some states that have done a good job of limiting their liability," says Dr. Jerrell Coggburn, associate professor and head of the Department of Public Administration at NC State. "Tracking these characteristics, and those states that have done well, could help guide those states that are currently weighing how to move forward to address their own unfunded liability concerns." Coggburn co-authored the research with Dr. Rick Kearney, director of NC State's School of Public and International Affairs.

In 2007, state governments for the first time made public their unfunded liability for state employee retiree benefits (other than pensions), such as health care. States began reporting on unfunded liability for pensions in the 1990s. Unfunded liability is the amount of money a state will need to set aside in order to meet expected costs - in this case, costs associated with state retiree benefits.

According to the 2007 data, states have a collective unfunded liability of

approximately $558 billion for retiree health care. However, the burden of the unfunded liability is not distributed evenly. For example, New Jersey has a total unfunded liability of $68.8 billion, or $7,950 per citizen, whereas Virginia has an unfunded liability of $1.6 billion, or $214 per citizen. Coggburn and Kearney evaluated the 2007 data to determine what state-level factors may contribute to the disparity in unfunded liabilities among states.

"What we found makes sense," Coggburn says. "For one thing, we found that states which have larger workforces per capita have larger liabilities. In other words, the more employees a state has per taxpayer, the higher a state's unfunded liability tends to be."

Kearney and Coggburn also found that states doing a poor job of setting aside funds to support state employee pensions have also done a poor job of addressing unfunded liabilities related to retiree health care and other benefits. "This shows that financial management trends tend to be consistent from state to state," Coggburn says, "at least in regard to pensions and retiree benefits." The authors also show that pension underfunding negatively affects state bond ratings, which drives up state borrowing costs, and warn that similar underfunding for retiree health care can make the situation even worse.

"We also found that more liberal states, which can be construed to be more employee-friendly, have more generous retiree benefit plans - and also have higher unfunded liabilities," Coggburn says. "However, there are some significant exceptions. For example, Louisiana and Alaska are considered to be relatively conservative, yet both states carry over $4,000 in unfunded liability for retiree benefits per citizen. Meanwhile, some fairly moderate states, like Wisconsin and Virginia, carry less than $300 in unfunded liability per citizen.

"This research gives us a good idea of what is going on in state

governments that is contributing to the unfunded liability problem, but balancing the need for good financial management with the need to attract, retain and motivate a strong public workforce means that there are no easy answers," Coggburn says.

The research, "Trouble Keeping Promises? An Analysis of Underfunding in State Retiree Benefits," is published in the January/February 2010 issue of the journal *Public Administration Review*.

Provided by North Carolina State University

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