NATIONAL REVIEW

America's Predictable Pension Crisis

Politicians shun any 'meddling' with entitlements, but the math problem inherent in the system is unavoidable.

By George Will — February 22, 2017

Some American disasters come as bolts from the blue — the stock-market crash of October 1929, Pearl Harbor, the designated hitter, 9/11. Others are predictable because they arise from arithmetic that is neither hidden nor arcane. Now comes the tsunami of pension problems that will wash over many cities and states.

Dallas has the fastest-growing economy of America's 13 largest cities, but in spite of its glistening commercial towers, it represents the skull beneath the skin of American prosperity. According to its mayor, the city is "walking into the fan blades" of pension promises: The fund for retired police and firefighters is $5 billion underfunded. Prompted by projections that the fund will be exhausted within 20 years, retirees last year withdrew $230 million from it in a six-week span. In the entire year, the fund paid out $283 million and the city put in just $115 million. Last November, the *New York Times* reported that the police and fire fund sought a $1.1 billion infusion, a sum "roughly equal to Dallas' entire general-fund budget and not even close to what the pension fund needs to be fully funded."

Nowadays, America's most persistent public dishonesties are the wildly optimistic, but politically convenient, expectations for returns on pension-fund investments. Last year, when Illinois reduced its expected return on its teachers' retirement fund from 7.5 percent to 7, this meant a $400 million to $500 million addition to the taxes needed annually for the fund. And expecting 7 percent is probably imprudent. Add to the Illinois example the problems of the 49 other states that have pension debt of at least $19,000 per household and numerous municipalities, and you will understand why many jurisdictions will be considering buyouts, whereby government workers are offered a lump sum in exchange for smaller pension benefits. Last September, in the seventh year of the recovery from the Great Recession, the vice chair of the agency in charge of Oregon's government-workers' pension system wept when speaking about the state's unfunded pension promises passing $22 billion.

The Manhattan Institute's Josh B. McGee reports that teachers' pension plans, which cover more people than all other state and local plans combined, have at least a $500 billion problem. This is the gap between promised benefits and money set aside to fund them.

A clear and present consequence is, McGee says, "pension cost crowd-out." Because pensions are consuming a larger share of education spending, 29 states spent less per pupil on instructional supplies in 2013 than in 2000, and during that period, instructional salaries per pupil were essentially flat.

This is just another instance of public policies that transfer wealth from the young to the elderly who, after a lifetime of accumulation, are society's most affluent cohort.

Pensions, including those of private companies, are being buffeted by a perfect storm of adverse events: People are living longer. Economic growth is persistently sluggish. Bond yields have declined dramatically during seven years of near-zero interests rates, which produce higher valuations of equities, lowering the future returns that can be realistically expected. As of last August, the *Financial Times* reported that pensions run by companies in the S&P 1500 index were underfunded by $562 billion — up $160 billion in just seven months.

The generic problem in the public sector is the moral hazard at the weakly beating heart of what Walter Russell Mead calls the "blue model" of governance — the perverse incentives in the alliance of state and local elected Democrats with public employees' unions. The former purchase the latter's support with extravagant promises, the unrealism of which will become apparent years hence, when the promise-makers will have moved on. The latter expect that when the future arrives, the government that made the promises can be compelled by law or political pressure to extract the promised money from the public.

This game, a degradation of democracy, could be disrupted by laws requiring more realistic expectations about returns on pension-fund investments, or even by congressional hearings to highlight the problem. But too much of the political class has skin in the game.

The problems of state and local pensions are cumulatively huge. The problems of Social Security and Medicare are each huge, but in 2016 neither candidate addressed them, and today's White House chief of staff vows that the administration will not "meddle" with either program. Demography, however, is destiny for entitlements, so arithmetic will do the meddling.

— George Will is a Pulitzer Prize–winning syndicated columnist. © 2017 Washington Post Writers Group