Taxpayers Association of Central Iowa

ISSUE BRIEF

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Iowa's Public Pension Debt Eclipses Other Public Debt

A few weeks ago, *The Des Moines Register* reported that "Iowa racked up an additional $462 million in debt in the last fiscal year." (December 28, 2017, "Iowa's Government Debt Grows by Another $462 Million to Nearly $16 Billion.") The article was in reference to borrowing by all state and local government entities in Iowa.

IPERS' unfunded pension obligations now exceed the sum total of all general obligation (GO) debt in Iowa!

The truth is, this figure is dwarfed by a three times larger increase in debt that also occurred in 2017: $1.4 BILLION in new debt associated with the Iowa Public Employees Retirement System (IPERS). IPERS' unfunded pension obligations ($7 billion) now exceed the sum total of all general obligation (GO) debt in Iowa!

There is little to differentiate IPERS debt from other forms of public debt. In fact, pension debt is very much like GO debt, in that it is essentially backed by the full faith and credit of government. We don't hear a lot about it because it's difficult to explain, and perhaps because proponents of the status quo don't want it to be understood.

Understanding UAL and GO

What exactly is an "unfunded actuarial liability," and how is it similar to GO (General Obligation) debt?

Defined benefit pension plans like IPERS guarantee a specific retirement benefit based on each year of public service. These are like contractual obligations—they must be paid when due.

The plans work by setting aside enough money each year to eventually pay the benefit earned in connection with that year of service. Sixty percent is contributed by the employer (taxpayer) and 40 percent by the employee. The amount set aside must be invested and earn a return each year in order to eventually cover the cost of the benefit payouts. According to IPERS, investment earnings cover about 70% of benefit payments.

A plan that is 100 percent funded (no unfunded liability) is estimated to have enough dollars set aside to grow, under plan assumptions, into what will be needed to pay benefits that have already been earned, when they become due.

But what happens when investment earnings fall below assumptions, or even worse, when the amount already set aside suffers a loss in its value, as happened in 2009? Now, although the benefits have already been earned (and must eventually be paid), there is no longer enough principal set aside to earn the required interest. Catch-up or extra payments are required not only to replace that principal, but also to make up for the interest that is not being earned. Regular payments, much like any other debt payments, must be made over the next 25-30 years to gradually erase the unfunded liability, or "debt," and bring the plan back to 100 percent funding. These payments come from government budgets, and thus are essentially obligations backed by the "full faith and credit of government."

IPERS' total unfunded liability is now $7 billion, and the **annual "debt" or catch-up payments will grow to $424 million next year and to $800 million per year by 2038**. (This is in addition to the $827 million to be paid next year to cover the benefits earned that year, for a total of $1.25 billion just in 2018-2019!) The equivalent of a penny of sales tax each year is being diverted away from priorities like education in order to repay public pension debt.

The payments made each year to (eventually) cover benefits that are earned that year make sense. Taxpayers are paying for the service they received during the same time period. However, payments for public pension unfunded liability, which stretch 25-30 years into the future, obligate future generations of taxpayers to pay for services that were rendered before they were even born.

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While public pension debt is similar to GO debt in many ways, there's one big difference. It's one thing to obligate future taxpayers for something like a bridge, which will continue to serve future taxpayers who help pay for it. It's another thing to saddle future generations of Iowans with debt simply for operations, or services that were provided by public employees many years in the past. Since when are Iowans okay with that?

Sweeping this significant debt under the rug or minimizing it by saying we're "on track to full funding," won't make it go away. It is an obligation Iowans have, no matter what. However, it does illuminate the serious taxpayer risk associated with these types of plans, and it raises the question of whether we should be compounding the risk by continuing to add new employees to a system that is sustainable only by shifting responsibility to future generations, if at all.