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GAO
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Highlights

Highlights of GAO-08-223, a report to the Committee on Finance, U.S. Senate

STATE AND LOCAL GOVERNMENT RETIREE BENEFITS

Current Funded Status of Pension and Health Benefits

Why GAO Did This Study

Pension and other retiree benefits for state and local government employees represent liabilities for state and local governments and ultimately a burden for state and local taxpayers. Since 1986, accounting standards have required state and local governments to report their unfunded pension liabilities. Recently, however, standards changed and now call for governments also to report retiree health liabilities. The extent of these liabilities nationwide is not yet known, but some predict they will be very large, possibly exceeding a trillion dollars in present value terms.

The federal government has an interest in assuring that all Americans have a secure retirement, as reflected in the federal tax deferral for contributions to both public and private pension plans. Consequently, the GAO was asked to examine: 1) the key measures of the funded status of retiree benefits and 2) the current funded status of retiree benefits. GAO analyzed data on public pensions, reviewed current literature, and interviewed a range of experts on public retiree benefits, actuarial science, and accounting.

What GAO Recommends

GAO is not making recommendations in this report. Experts on public benefits funding provided technical clarifications, which were incorporated as appropriate.

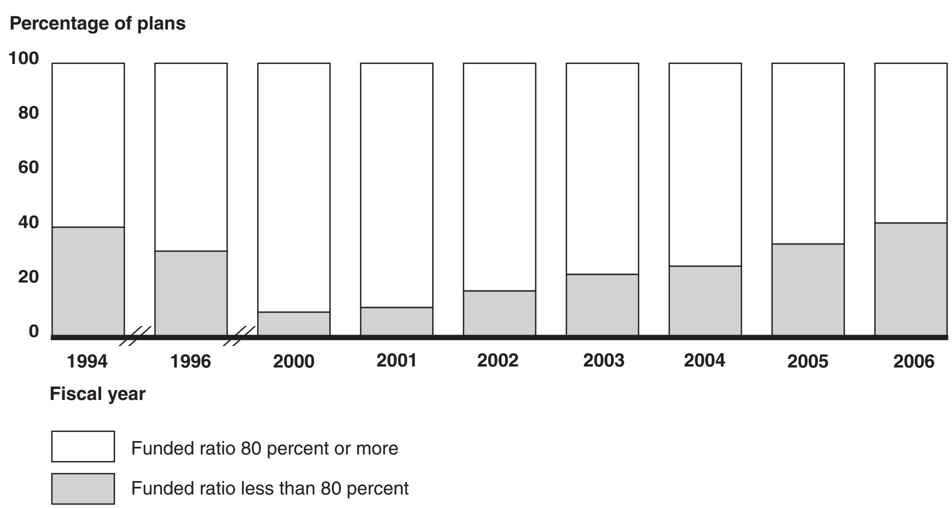
To view the full product, including the scope and methodology, click on GAO-08-223. For more information, contact Barbara Bovbjerg at (202) 512-7215 or bovbjergb@gao.gov.

What GAO Found

Three key measures help to understand different aspects of the funded status of state and local government pension and other retiree benefits. First, governments' annual contributions indicate the extent to which governments are keeping up with the benefits as they are accumulating. Second, the funded ratio indicates the percentage of actuarially accrued benefit liabilities covered by the actuarial value of assets. Third, unfunded actuarial accrued liabilities indicate the excess, if any, of liabilities over assets in dollars. Governments have been reporting these three measures for pensions for years, but new accounting standards will also require governments to report the same for retiree health benefits. Because a variety of methods and actuarial assumptions are used to calculate the funded status, different plans cannot be easily compared.

Currently, most state and local government pension plans have enough invested resources set aside to keep up with the benefits they are scheduled to pay over the next several decades, but governments offering retiree health benefits generally have large unfunded liabilities. Many experts consider a funded ratio of about 80 percent or better to be sound for government pensions. We found that 58 percent of 65 large pension plans were funded to that level in 2006, a decrease since 2000. Low funded ratios would eventually require the government employer to improve funding, for example, by reducing benefits or by increasing contributions. However, pension benefits are generally not at risk in the near term because current assets and new contributions may be sufficient to pay benefits for several years. Still, many governments have often contributed less than the amount needed to improve or maintain funded ratios. Low contributions raise concerns about the future funded status. For retiree health benefits, studies estimate that the total unfunded actuarial accrued liability for state and local governments lies between $600 billion and $1.6 trillion in present value terms. The unfunded liabilities are large because governments typically have not set aside any funds for the future payment of retiree health benefits as they have for pensions.

Percentage of State and Local Pension Plans with Funded Ratios above or below 80 Percent



Source: GAO analysis of PFS, PENDAT data.