[Don't Mess Around With Government Pensions.](#)

No one likes making pension fund payments. You have to take money that you could be enjoying right now, and hand it over to some stranger, in the hopes that decades hence, when you're ready to retire, said stranger will hand it back to you and enable to live out your golden years in reasonable comfort. The connection between sacrifice and reward is, let us say, a little too distant for proper enjoyment.

You know who likes pension funds payments the least of all? Taxpayers. Because they're not even sacrificing for their own retirements, but so that someone else can enjoy a comfortable old age.

Naturally, this leads to a lot of wrangling. And the nature of this wrangling is that most of it will be, to the average taxpayer, insanely boring: knock-down drag-out fights over financial arcana such as "discount rates" and "funding ratios." This tends to sound, to your average person of normal interests and intelligence, like the adults talking in a Charlie Brown cartoon.

Unfortunately, no matter how boring and technical this stuff sounds, it matters. Getting these boring, technical details right is how we ensure that pensioners do not, suddenly and for no apparent reason, find themselves without their long-awaited pension check. And that taxpayers do not find that their taxes have, suddenly and for no apparent reason, risen to levels they cannot afford.

Nonetheless, there will always be a constituency arguing for a more optimistic assessment of how to sacrifice less now and still meet future obligations. Sometimes that even includes the folks getting the pensions.

The political left often prefers a looser (and therefore riskier) standard, because the more conservative the method you use to value the liabilities, the more the government has to put into the fund right now. This makes generous pension benefits seem more expensive to current taxpayers, lessening support for them. The stricter standards also limit the government's ability to spend money right now on stuff the left wants to do. Thus, those of us who think that a conservative standard is the correct one, periodically end up contending with a new report that brightly suggests that everything would be much better if we fiddled with the accounting standards to lower the amount we require governments to contribute.

One recent installment in this perennial debate comes out of Berkeley's Haas Institute for a Fair and Inclusive Society. The author, Tom Sgouros, has a background in public finance, and his arguments are careful and mathematically literate. Nonetheless, I find them unconvincing.

I favor a conservative approach, and I mean "conservative" in the accounting, rather than the political sense. To err on the side of caution. And why should we be cautious? So we can make darned sure that workers get what they're owed.

Sgouros agrees, in fact, that such conservative standards are the correct approach for valuing private-sector pension contributions, in case the business goes bust and the pension needs to stand on its own. But he says that governments are different, because they can’t go out of business. In other words, government pensions are less risky, so they don’t need such strict standards.

This is … sort of true. A government pension plan can, in theory, operate underfunded forever — as long as the tax base and the workforce are growing faster than their current pension liability.

It’s not quite true that governments are permanent. But if the U.S. government has gone down and Illinois is just a name in the history books, the status of the state teachers’ pension fund is probably going to be the least of everyone’s worries.

In less extreme scenarios, government finances are ultimately constrained by the much-maligned Laffer Curve. There is some point, however high the percentage, beyond which raising the tax rate not only doesn’t bring in more revenue, but actually lowers government income. And the smaller the level of government, the lower the tax rate at which Laffer effects kick in. If your block had the ability to levy a 25 percent tax on your income, and actually did so, you’d sell your house pretty quick. It’s much harder to pick up and move to another country. We also have to factor in the fact that, in a democracy, voters can go to the polls and say “no more,” which is a sort of secondary Laffer point that people planning in decades have to reckon with.

Cities tend to declare bankruptcy precisely because they’re near one of those points, through some combination of financial mismanagement and local economic decline. When they have exhausted their ability to borrow, or wheedle bailouts out of some larger government entity, they end up with an unpalatable choice between cutting municipal services or failing their creditors — of which the future beneficiaries of an underfunded pension plan are one.

But even if you argue that the ability of governments to tax is greater and more flexible than I credit, that doesn’t suggest we can do away with conservative accounting standards for government pensions. We need them more than ever.

If you argue that government pensions don’t need huge assets on hand, because they have more protection in the form of an unlimited claim on taxpayer wallets, then you need to add a stakeholder to the pension calculation: the taxpayer.

Those taxpayers have a right to decide how much they’re willing to spend on the people employed by their municipality or state. Hiding the true cost of that compensation by lowering the pension funding requirements — while simultaneously relying on an unpriced, undisclosed call option on their future earnings to make the math work — is both unfair and undemocratic.

There’s one more reason that we should use a conservative standard: It increases the amount of money we have to put in right now, but it lowers the amount that has to be put in over time. Compound investment returns are a powerful force, one that, over decades, can dramatically reduce the percentage of salaries and taxes that have to be devoted to the pension system. Forgoing those gains because they require political pain now is a mistake.

Most state and local pension plans are not at a point where they’d have to cut benefits tomorrow, and few of them will be in that situation in the near future. But the whole point of a pension is to allow people to know that they’ll be secure decades from now, when things may be very different.

Which means that the people in charge of the pension should be planning for that, not saying “Well, the taxpayer of tomorrow will figure out some way to make the numbers work.” Current contributions should be invested to cover the future benefits for current workers; future contributions should be devoted to the workers who make them. And no one should be relying on future taxpayers to bail them out of a jam, not least because there's no way to know if they'll be able to.

This isn't a liberal or a conservative idea. It's the basic common-sense reasoning of people who want to make sure they can pay their bills.

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