
New Math Deals Minnesota's Pensions the Biggest Hit in the U.S.

- **State's public pensions go to 7th-worst funded from 30th**
- **"It's a crisis," says director of pension commission**

Minnesota's debt to its workers' retirement system has soared by $33.4 billion, or $6,000 for every resident, courtesy of accounting rules.

The jump caused the finances of Minnesota's pensions to erode more than any other state's last year as accounting standards seek to prevent governments from using overly optimistic assumptions to minimize what they owe public employees decades from now. Because of changes in actuarial math, Minnesota in 2016 reported having just 53 percent of what it needed to cover promised benefits, down from 80 percent a year earlier, transforming it from one of the best funded state systems to the seventh worst, according to data compiled by Bloomberg.

"It's a crisis," said Susan Lenczewski, executive director of the state's Legislative Commission on Pensions and Retirement.

The latest reckoning won't force Minnesota to pump more taxpayer money into its pensions, nor does it put retirees' pension checks in any jeopardy. But it underscores the long-term financial pressure facing governments such as Minnesota, New Jersey and Illinois that have been left with massive shortfalls after years of failing to make adequate contributions to their retirement systems.

The Governmental Accounting Standards Board's rules, ushered in after the last recession, were intended to address concern that state and city pensions were understating the scale of their obligations by counting on steady investment gains even after they run out of cash — and no longer have money to invest. Pensions use the expected rate of return on their investments to calculate in today's dollars, or discount, the value of pension checks that won't be paid out for decades.

The guidelines require governments to calculate when their pensions will be depleted and use the yield on a 20-year municipal bond index to determine costs after they run out of money.

The Minnesota's teachers' pension fund, which had $19.4 billion in assets as of June 30, 2016, is expected to go broke in 2052. As a result of the latest rules the pension has started using a rate of 4.7 percent to discount its liabilities, down from the 8 percent used previously. Its liabilities increased by $16.7 billion.

The worsening outlook for Minnesota is in line with what happened nationally. Pension-funding ratios declined in 43 states in the 2016 fiscal year, according to data compiled by Bloomberg. New Jersey had the worst-funded system, with about 31 percent of the assets it needs, followed by Kentucky with 31.4 percent. The median state pension had a 71 percent funding ratio, down from 74.5 percent in 2015.

For a look at Bloomberg's pension ranking, click here.

While record-setting stock prices boosted the median public pension return to 12.4 percent in 2017, the most in three years, that won't be enough to dig them out of the hole.

Only eight state pension plans, in Minnesota, New Jersey, Kentucky and Texas, used a discount rate "significantly lower" than their traditional discount rate to value liabilities, according to July report by the Center for Retirement Research at Boston College.

"Because of that huge drop in the discount rate under GASB reporting, their liabilities skyrocket," said Todd Tauzer, an S&P Global Ratings analyst. "That's why you see that huge change compared to other states."

Public finance scholars at George Mason University's Mercatus Center have found "considerable variance" in how states were applying the new standards. In Illinois, for example, despite the state's poor history of funding its plans, actuaries project they won't run of money until 2072.

In Minnesota lackluster returns and years of shortchanging have taken a toll. The state's pensions lost 0.1 percent in fiscal 2016.

But other factors also helped boost Minnesota's liabilities: Eight of Minnesota's nine pensions reduced their assumed rate of return on their investments to 7.5 percent from 7.9 percent, while three began factoring in longer life expectancy.

Minnesota funds its pensions based on a statutory rate that's lower than what's need to improve their funding status. School districts and teachers contribute about 85 percent of what's required to the teacher's pension, according to S&P Global Ratings.

"It's woefully insufficient for the liabilities," said Lenczewski, the director of Minnesota's legislative commission on pensions. "You just watch this giant thing decline in funding status."

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