Bond Case Briefs

Municipal Finance Law Since 1971

New Tax Law Means Fighting Over Unfunded State Pension Plans is About to Get Worse.

The recently enacted U.S. tax law restricts federal deductions for state and local taxes (SALT) to $10,000 — including local property and sales taxes as well as local income taxes. While this new restriction will have many implications, it will have a particularly draconian impact on states with large unfunded liabilities for pension benefits and retiree health care, in particular the residents of Illinois, Kentucky, Connecticut, and New Jersey.

Unless states can implement effective ways to circumvent the SALT restriction, they will face much higher political barriers to meeting their unfunded benefit obligations through increased tax revenues. Instead, states will be forced to severely cut spending on public services and/or adopt major reforms of their benefit plans.

A state has payment obligations from three main sources — interest on its outstanding bonds, unfunded liabilities for pension benefits, and unfunded liabilities for health care payments to state retirees (before Medicare at age 65). The interest on outstanding state bonds is relatively easy to estimate; the total outstanding amount of all state bonds was $500 billion in 2016. With the advent of improved accounting rules, it is now possible to compute the unfunded pension and retiree health care liabilities of each state.

Continue reading.

The Brookings Institute

Robert C. Pozen

Thursday, January 11, 2018