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Ted Boettner: Crisis may be overstated

CHARLESTON, W.Va. -- Phil Kabler recently told readers the state's $8 billion unfunded retiree health care liability, or Other Post Employment Benefits (OPEB), represented "the biggest financial crisis facing the state."

Lawmakers are now poised to set aside $600 million to help fund the liability. While it's hard to deny that this is a problem, we should respond judiciously and not overreact. A failure to do so could damage the state's ability to make the important investments in its people and infrastructure that form the foundation of our economy.

Many years ago, state employees and teachers were told that in exchange for pay increases that they "may" receive health insurance upon retirement. The state budgeted for this subsidy on a pay-as-you-go or cash basis until recently when the General Accounting Standards Board issued Rule 45.

The rule required that states account for the cost of non-pension benefits like health care on an accrual basis. This means the state has to estimate the "net present value" of retiree health care costs until the employee's death, recognize it as a liability, and start setting aside additional funds that reflect medical inflation.

While transparency is a good thing, there are several problems with this rule.

First, the state has no statutory legal obligation to fund retiree health care. Therefore, the rule rests on the false assumption that the benefit is a "liability." Before lawmakers spend hundreds of millions of dollars, it should be established whether the employer subsidy for PEIA retiree health care is a real obligation.

Second, the $8 billion figure is flawed. Unlike defined pension annuities that can be reasonably predicted over time, determining the cost of health care over the life of a workforce is not. This is why groups such as the American Association of Actuaries are critical of this method being used in the private sector. Also, the state's actuaries are assuming that the nation's health care costs will continue to grow at unsustainable levels indefinitely.

The cause for alarm is also hard to reconcile given that West Virginia has funded its future retiree health care costs better than 37 states, according to a recent report by the Pew Center on States. Pew also noted that 22 states have put zero funds toward respective OPEB obligations.

The central reason why lawmakers, especially the governor, are concerned is the potential to lower the state's bond rating (credit score) or the state's ability to finance capital projects.

A lower bond rating means higher loan interest rates, which translate into higher costs for the state to build schools and other projects. So far, OPEB hasn't affected the state's bond rating. In fact, our bond rating was upgraded last year. The truth is bond-rating agencies were already incorporating the state's OPEB liability into their bond rating before the new accounting rule, and they don't rank it as a critical factor in determining a state's bond rating.

The alarm might also stem from the fact that lawmakers don't want the state's OPEB obligations to resemble the state's employee pension woes, which are comparatively underfunded. As long as the state can afford to pay its share of OPEB, then it should do so and not let unelected accountants dictate policy. If we can't afford the payment in the future, then changes will have to be made beyond what has already been done.

The real question is: Do we invest $600 million in the stock market (trust fund) or do we invest that money in our future workforce that could yield even higher returns?

As John Maynard Keynes said, "Once we allow ourselves to be disobedient to the test of an accountant's profit, we have begun to change our civilization."

Boettner is executive director of the WV Center on Budget and Policy.