Although most state and local government pension plans have sufficient resources to pay for their benefit obligations over the next several years, various studies indicate that the total unfunded liability for retiree health benefits of state and local governments may be as high as $1.6 trillion, according to a Government Accounting Office (GAO) report. Unfunded liabilities for health benefits are large because state and local governments typically have not set aside funds for future retiree health benefits, as they do for pensions. Instead, their practice has been to pay for these benefits due in a given year from revenues for that year. This approach can leave little flexibility for governments and may stress future budgets.

The GAO says 58 percent of 65 large public pension plans maintained a funding ratio of at least 80 percent in 2006, which is a level considered by many experts to be sound for state and local government. Even plans that have lower funded ratios are generally not at risk in the near term, since current assets and new contributions may be sufficient to pay benefits for several years, according to the report.

Senate Finance Committee Chair, Max Baucus (D-Montana) expresses concern that collapsed funds might seek a federal government bailout. “While the state and local pension plans seem to be in decent shape, the shortfalls in retiree health plans are troubling.” The Finance Committee would work to “curb the rising costs of health care” among other initiatives, according to Baucus. Ranking Member of the Finance Committee, Charles Grassley (R-Iowa) says, “It's good news that state and local government pensions plans appear to be healthy. It's important that they stay that way.” He suggests that Congress “keep tabs and take action if the situation changes.” He also says that states should pre-fund retiree health liabilities, while Congress looks at ways to hold down health care costs.
