OPINION | CHARLES CHIEPPO

In balancing the budget, Baker and legislators need to think long-term

**By Charles Chieppo**   JUNE 28, 2016



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Human nature is such that elected officials aren’t always great about doing what’s in their constituents’ long-term interests. “Long-term,” after all, often translates to taking a political hit now only to have one of your successors get credit down the line.

But as the state budget debate continues, a recent report from J.P. Morgan demonstrates why Governor Baker and legislators should be careful not to lose sight of the Commonwealth’s long-term fiscal sustainability. It finds that only five states need to dedicate a larger percentage of state revenues to amortize pension, other post-employment benefits (mostly health insurance), and bonded debt liabilities over 30 years than Massachusetts does.

Michael Cembalest, author of the Morgan report,“The ARC and the Covenants, 2.0” (ARC refers to the acronym for “annual required contribution”), finds that it will take about 22 percent of the Commonwealth’s revenues to retire these liabilities; right now we’re contributing around 14 percent. His projections assume a realistic 6 percent return on assets like state pension funds.

Once a state gets to 25 percent, Cembalest says “the math becomes very difficult.” If you’re wondering how difficult, consider this: To solve the problem exclusively with additional revenue, spending cuts, or increased employee pension and retiree health insurance contributions, New Jersey, which would have to dedicate more than 35 percent of state revenues to amortize its massive liabilities over 30 years, would either need to increase revenues by about one quarter or cut spending by a similar amount. Connecticut, which would need to dedicate just about 35 percent of revenue, would have to raise employee contributions by a stunning 699 percent.

As it currently stands, retiring liabilities in 30 years would require Massachusetts to do one of the following: increase taxes by 7 percent, cut spending 6 percent, or more than double employee contributions.

The news isn’t all bad for Massachusetts. The J.P. Morgan report’s finding that the 22 percent of revenues the Commonwealth would have to devote to amortize liabilities represents an improvement over the original 2014 study, which calculated that a quarter of state revenues would be required — the point at which Cembalest says the math stops adding up.

In addition, the study confirms that our “Taxachusetts” days are a thing of the past. Of the six states that require the largest percentage of revenues to retire their liabilities, only New Jersey has a lower effective tax rate on middle-income earners.

But it also suggests that the problem can’t be solved by taxes alone. Of the four states that are in the worst shape, three — Illinois, Connecticut, and Kentucky — already have effective tax rates that are among the nation’s highest. The best solution is likely a balanced approach that includes a combination of revenue, cuts, and increased employee contributions.

“The ARC and the Covenants, 2.0” offers a cautionary tale about the dangers of short-term thinking. In an era in which leaders struggle to balance the books from year to year, let’s hope the budget Governor Baker ultimately signs will exhibit one of the rarest characteristics of leadership: the ability to postpone gratification for the sake of a sustainable future.

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