Report: Hawaii Ranks Near Bottom in National Economic Outlook, Debt Analysis, by State Budget Solutions

Photo courtesy of HTA

***BY MALIA ZIMMERMAN* -** When it comes to state debt, Hawaii was ranked poorly in a report released today by State Budget Solutions, a non partisan government accountability group that tracks state debt and spending.

Bob Williams, president of State Budget Solutions, says Hawaii's economic performance is 12th best in the country, but the economic outlook is 46th best.

That compares with the 2008 and 2009 reports that had Hawaii during both years at 41 for its economic outlook, and the 2010 report that had the state at 39.

Why the drop in the ranking?

Williams pointed to the top marginal personal income tax, which is at 48th highest; the General Excise Tax burden on the sales of goods and services, which is at 49th highest; and Hawaii's estate and inheritance tax, which has risen to 50 percent.

In addition, Hawaii ranks near the highest taxed state overall, Williams said.

"The governor and legislature apparently don't understand how free markets work - high taxes kill jobs," Williams said.

Hawaii's financial condition was the topic of a recent House-Senate informational briefing hosted by the House minority caucus earlier this month.

Sheila Weinberg, founder of the Chicago-based Institute for Truth in Accounting, told lawmakers that Hawaii state government’s financial situation is dire, mainly because of unfunded obligations that total in the billions of dollars.

The institute earlier reported that Hawaii is the 5th worst “sinkhole” state, with $19.5 billion worth of assets, but only $3.9 billion are available to pay $15.4 billion of bills as they come due.

The Institute also estimated that each person here - a state with just under 1.3 million residents - carries over $25,000 in debt from past government spending.

For Hawaii, there are two major unfunded obligations that Weinberg, two credit rating agencies, and Hawaii’s State Budget and Finance Director Kalbert Young, have singled out as problematic – the state Employee Retirement System (ERS) and the Hawaii Employee-Union Health Benefits Trust Fund (EUTF).

While various studies show Hawaii's unfunded obligations at different amounts, Weinberg's group used the state's own numbers that show that $3.9 billion is state's share of $5.1 in unfunded liabilities; the counties owe the rest.

And because the EUTF is a pay as you go system, the state has no funding or assets to cover the $7.2 billion needed to cover state and county retirees' healthcare as promised to them – and the costs keep rising. The state pays out about $1.2 billon a year.

The Hawaii State Teachers Association needs another $1.6 billion for teachers healthcare, but this is also a pay as you go system with no assets or funding set aside to cover the total.

Weinberg said just to pay off the EUTF obligation, Hawaii would have to stop paying all of its state workers for 4 years just to catch up.

Because the state is not paying off these debts in full – or even budgeting for them – Weinberg said taxpayers in the future are being burdened with this debt.

Budget & Finance Director Kalbert Young, who manages the state budget, shares the concerns outlined by Weinberg and the two state credit agencies, Moodys and Standard & Poors, which recently downgraded Hawaii. He told lawmakers during that October briefing that some changes are being made to improve the state's financial conditions, but more needs to be done.

Young confirmed what national studies show: Hawaii is one of, if not the most, generous states for government employee retirement benefits.

Young also provided more information to *Hawaii Reporter* on the state's debt and unfunded obligations.

The actuary report for July 1, 2009 (issued in May 2011), lists the Present Value of Benefits for the ERS at $18.1 billion, but the actuarial liability is $14.1 billion, he said. (The latter is the number indicative of the unfunded liability).

The $14.1 billion quantifies the value of the obligation that was made to government employees and retirees when they enter retirement - and all taxpayers are going to be impacted by this, Young said.

"The State and taxpayers have not been paying into the EUTF to fund up its future liabilities. Instead, the State and taxpayers have been content to pay only the yearly premium costs and expenses. Well, the cost of this coverage continues to increase at a rate faster than revenue is projected to increase. Since the liability is not being met, the liability is recorded on the State's financial statements, which reduce our asset position. In the end, the State and taxpayers will either have reduced services to fund growing health insurance premiums, or to begin funding the liability, or taxes and revenues will have to be increased to pay for either," Young said.

How can the state cover its debt? There really is only one way to make up the liability... and, that is to fund it, Young said, but he warned that taxpayers should recognize and realize they are paying for costs where they are not receiving any benefit.

"That is why the current system of paying only annual expenses is not wise or sustainable. It is unlikely that this benefit can be changed for current retirees or current employees for when they retire. But, it is unlikely that we can continue offering this benefit to all future employees. I believe that's where we need to start changing the system," Young said.

The Administration has already begun trying to address what many analyst say is a dire situation, Young said, including introducing a bill that would have stopped the practice of reimbursing retirees for Medicare Part B, which amounts to approximately $40 million a year in FY11 and is projected to grow to $47+ million in FY12.

"The public and the legislature argued against reducing this benefit for government retirees. If benefits can not be reduced for current retirees or current employees when they retire, then we are only left with changing this benefit for future not-yet-hired employees. This will reduce the unfunded liability in time - decades decades from now. It's a start.

The Administration intends to continue pressing for reform that will slow the growth in the liability and eventually address it. I don't know what the legislature collectively would offer towards this problem," Young said.

The state's financial woes have had an impact on its bond rating - the State was recently downgraded by both Moody's and Fitch, with both citing the large unfunded liability in the EUTF as one of the four top reasons for the downgrade and they also cited that the liability is growing.

"I believe given the statistics on Hawaii's liability relative to other states, Hawaii could be faced with future credit action if we do not pro-actively begin to address this matter," Young said. "Credit downgrades impact taxpayers because they translate to higher interest rates and borrowing costs. As a result, taxpayers will have to pay more for government or they will have to accept a larger portion of their taxes going towards debt."

Hawaii isn't the only state struggling under the weight of its debt and spending issues. The State Budget Solutions report reveals aggregate state debt presently exceeds $4 trillion.

California, New York, Texas, New Jersey, and Illinois are the states with the largest total deficits, while states ranking well include Vermont, North Dakota, South Dakota, Nebraska and Wyoming.

In terms of future economic performance, New York, Vermont, Maine, California, and Hawaii scored the lowest, while the states with the best outlook include Utah, South Dakota, Virginia, Wyoming, and Idaho. State Budget Solutions said the outlook predictions were determined after its researchers analyzed economic data over for 10 years.

The report notes that while liabilities are not actually debt, they are a stream of future spending obligations that states have committed themselves to spending.

Like in Hawaii, Pensions and Other Post Employment Benefits (OPEB) are straining budgets in other states.

"Just How Big are Public Pension Liabilities?" - another report by State Budget Solutions - says minimum unfunded liabilities total more than $3.4 trillion.