

“Governments should not promise pension benefits to employees and then kick the costs of those pensions to future taxpayers.”

Michigan lawmakers tackle a difficult problem

After years of ignoring the problem, state takes action to solve escalating pension debt

By James M. Hohman | December 2025

Michigan lawmakers deserve applause for paying down employee pension system debt. The state has taken important steps to deal with accumulating retirement debt and stop making promises that defer costs to future taxpayers.

Governments should not promise pension benefits to employees and then kick the costs of those pensions to future taxpayers. They should save money on their pension funds, invest wisely, and use the returns to pay for the costs of monthly benefit checks.

Michigan governments, as well as state and local governments around the country, have tried to do that. And they've failed spectacularly. By underfunding the state's pension system over many years, without ever asking employees or taxpayers for permission, Michigan leaders made their own workers the state's largest creditors.

This is a hard problem. There are few political benefits for keeping a pension system fully funded. No one invites lawmakers to a ribbon-cutting ceremony when they've saved enough to pay for all pension benefits. There always seems to be a better way to spend a dollar in the state pension system than paying down pension debts.

Elected officials also can use a variety of tricks to avoid debt payments. They can play with investment return assumptions or extend debt payment schedules. They can change smoothing assumptions during good times and use other gimmicks to limit debt payments. Few spending interests criticize officials when they defer pension debt payments.

There are steep consequences for that lack of interest in catching up and for the political acceptance of deferring payments to pension funds. Michigan's

largest government pension system, which covers all public school employees in the state, has been underfunded in 51 out of the past 52 years. (The one-year exception was due to a funding gimmick.)

Despite the bad incentives, Michigan lawmakers have made a lot of progress over the past fifteen years. They've changed their assumed rates of return from 8% to 6%, making it easier to meet expectations but also making the underfunding problem look worse. They've chosen debt payment schedules that pay down debt rather than inflate it over the short term.

They've also prefunded retiree health care benefits. Pensioners receive medical insurance benefits from the system, and lawmakers hadn't even tried to set money aside to cover those costs until 2011. Now they've saved enough money to pay for all the benefits that have been offered to pensioners and current workers.

And they've worked to prevent themselves from developing further debt. Using better assumptions helps prevent future underfunding, and employees themselves will share the costs of underfunded pension debts, should they arise. That is if they choose the pension option rather than a 401(k) plan, where employees remain in control of their retirement funds and taxpayers are not at risk from underfunding.

While the politics of pensions encourage lawmakers to kick the costs of today's government service onto tomorrow's taxpayers, Michigan lawmakers have avoided that tendency. They have put more cash into the pension system. They are paying down debts. They've prefunded retiree health care benefits. This will protect pensioners and taxpayers alike.

The benefits for these changes are still years off. The system requires billions more in payments before benefits are fully prefunded. When they are, taxpayers can finally save some money.

It could have been easy for Michigan legislators to avoid and ignore pension problems. That's the path of least resistance for many lawmakers around the country. Instead, they made some wise decisions and set the state on a path to ensure that the costs of pensions are paid as they are earned.

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James M. Hohman is director of fiscal policy for the Mackinac Center for Public Policy.