Pension Politics

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(based on research collaboration with Terry M. Moe)
Some common explanations...

- The problem is faulty actuarial assumptions.
- The problem was caused by the Great Recession.
- In some places, “fiscal discipline simply appear[s] not to be part of the state’s culture.”
The public pension problem is a political problem that calls for a political explanation.

Funded ratios are important indicators, but they reflect the outcomes of many different kinds of decisions over the years.

We should consider the incentives decision-makers face when deciding on benefit levels, contribution levels, and investment strategy.

Standard accounts downplay the importance of politics.
DECISIONS ABOUT BENEFITS
Prior to 2009, it was incredibly tempting for politicians to increase pension benefits.

- Most voters weren’t paying attention to pensions.
- The interest group system was one-sided.
- Elected officials could increase benefits without spending any more money (in the short run).
Voters became attentive and (more) informed.

**The politics of pension benefits changed with the onset of the Great Recession.**
Number of news articles about state and local public pensions, by year

The politics of pension benefits changed with the onset of the Great Recession.

- Voters became attentive and (more) informed.
- The interest group system was no longer one-sided.
- But...elected officials still have incentives to push costs into the future (if possible).
Public employee pension benefit changes

Increases Decreases

“An Illinois Pension Bailout?”
*Wall Street Journal, Review & Outlook, September 20, 2012*

“[T]he Democrats who are running Illinois into the ground can’t bring themselves to oppose union demands...It’s no surprise that many of the states deepest in the red are public union strongholds. For decades, Democrats have bought union support in elections by using surplus revenue during good times to pad pension and retiree health-care benefits.”
Democrats, 1999-2008: 97%
Republicans, 1999-2008: 92%
Democrats, 2009-2011: 98%
Republicans, 2009-2011: 66%

Percent voting “yes” on benefit decreases, 2009-2011

<table>
<thead>
<tr>
<th>Party</th>
<th>Democratic Unified Governments</th>
<th>Non-Democratic Unified Governments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Democrats</td>
<td>87%</td>
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DECISIONS ABOUT CONTRIBUTIONS

- Decisions about the assumptions
- Decisions about employee contributions
- Decisions about making the actuarially required contribution (ARC)
Elected officials have incentives to keep rosy assumptions as they are.

Shouldn’t government employees—and their unions—work to ensure that contributions are sufficient?

- These are *their* pensions. They should want to make sure that funds are sufficient to pay benefits.

But:
- Benefits are backed by legal guarantees.
- An increase in required contributions might lead to an increase in employee contributions.
- An increase in employer contributions might decrease funding for other things that public sector unions want.
- Are union leaders thinking long-term?
- Changes that make pensions look more expensive might get voters’ attention—and make them negative toward pensions.
Size of pension boards of trustees

Source: Authors’ data collected from state statutes.
Who are the trustees?

Source: Authors’ data collected from state statutes.
Who chooses the “employer” and “employee” trustees?

Source: Authors’ data collected from state statutes.
Average of % employee trustees

- < 7.5%
- [7.5%, 7.75%)
- [7.75%, 8.0%)
- >= 8.0%

Percent employee trustees and discount rate, 2013

Source: Authors’ data on board composition; discount rates from the Public Plans Database, Center for Retirement Research, 2015.
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Source: Authors’ data on board composition; discount rates from the Public Plans Database, Center for Retirement Research, 2015.
Proportion of ARC paid, 2013

Source: Authors’ data on board composition; Proportion of ARC Paid from the Public Plans Database, Center for Retirement Research, 2015.
Funded ratio, 2013

Source: Authors’ data on board composition; Funded Ratio from the Public Plans Database, Center for Retirement Research, 2015.
Historically, it has been incredibly tempting for politicians to increase benefits.

To some extent, the politics of benefits is different now. But will it stay that way? Maybe, maybe not.

Political incentives have been—and remain—stacked against responsible contributing.