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But the Pension Fund Was Just Sitting There...”

The Politics of Teacher Retirement Plans

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"But the Pension Fund Was Just Sitting There...": — The Politics of Teacher Retirement Plans

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ABSTRACT

The tension at the heart of pension politics is the incentive to address today's claimants and focus on the here-and-now at the expense of long-term concerns and more dispersed constituencies. In the private sector, rules and regulations seek to tame corner-cutting and short-sighted behavior. In the public sector, the primary safeguard is the self-discipline of public officials and the hope that they will not be unduly tempted by short-term electoral considerations or influential constituencies. Teacher pensions, in particular, pose two challenges for K-12 schooling. The first challenge is the political incentives that lead to irresponsible fiscal stewardship, as public officials make commitments to employees that outstrip the available funds. The second is that of electoral considerations which hinder modernization, as policymakers dance around existing structures built to serve an industrial-era workforce and ill-suited to attracting talent in the contemporary labor market. The alignment of the political stars has helped states and localities to address the first challenge, but there has been little evidence of a willingness to tackle the second. We examine the political control of public pensions, the influence of teacher associations, and the lack of institutional constraints on public officials to explain the severity of these challenges. Those dynamics are illustrated via discussion of fiscal crises in New Jersey, Oregon, and San Diego and the way in which those crises created opportunities for addressing enormous shortfalls in funding. We close by suggesting several measures that may encourage public officials to be more responsible fiscal stewards or to revisit anachronistic retirement systems in order to promote teacher quality.

In a memorable "Doonesbury" comic strip from the late 1970s, Gary Trudeau's Raoul Duke—serving at the time as general manager of the Washington Redskins—waved off the need to draft more linemen because he had managed to improbably sign star lineman "Lava Lava" Lenny from the Detroit Lions. When asked how he had pulled it off, Duke explained that he and Lenny's attorneys had gone to the mats and that he had not spent "a penny more than he's worth! I swear it! Besides, the pension fund was just *sitting* there!"

In this punch line, Trudeau captured the tension at the heart of pension politics—the incentive to address today's claimants and focus on the here-and-now at the expense of long-term concerns and more dispersed constituencies. Those temptations are omnipresent in the private and public sectors alike. In the private sector, rules and regulations seek to tame corner-cutting and short-sighted behavior—with varying degrees of success. In the public sector, including public education, the primary safeguard is the self-discipline of public officials and the hope that they will not be unduly tempted by short-term electoral considerations and influential constituencies.

Given the state of public pension funds, these safeguards hardly seem adequate. In 2008, the Pew Research Center projected that state pension plans, with a $2.7 trillion obligation in coming decades, are $731 billion short of the funds needed to meet those obligations.[1] The economic tumult of late 2008 and 2009 have substantially aggravated the situation since those estimates were issued. Meanwhile, Joseph O'Keefe of Fitch Ratings has noted that actuarial

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[1] Katherine Barrett and Richard Greene, "Promises with a Price: Public Sector Retirement Benefits," PEW Center on the States, 2008, p. 3, available from http://www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/State_policy/pension_report.pdf (accessed January 15, 2009).

studies suggest contribution rates for public employees are lagging benefit costs, meaning that the problem is due to get worse.[2]

Teacher pensions, in particular, pose two challenges for K-12 schooling. The first challenge is the political incentives that lead to *irresponsible fiscal stewardship,* as public officials make commitments to employees that outstrip the available funds. The second is that of electoral considerations which hinder *modernization*, as policymakers dance around existing structures built to serve an industrial-era workforce and ill-suited to attracting talent in the contemporary labor market. As we shall discuss, the alignment of the political stars has helped states and localities to address the first challenge, but there has been little evidence of a willingness to tackle the second.

Discussion of teacher pensions has focused on economic and technical questions such as whether pensions are adequately funded, how they impact state and district budgets, and how benefit formulas affect efforts to attract and retain talented teachers. What has garnered less attention is the degree to which unaffordable promises and anachronistic program designs are due to political incentives. Public pension systems inextricably intertwine political considerations with actuarial and technical ones, making it foolhardy to discuss reforms without contemplating how they may be affected by legislative preferences, constituent politics, and institutional arrangements. The Employee Benefit Research Institute has observed, "Because public employee benefit plans are legislative products, political forces impose a greater effect on their design than economic forces…The interest group activities can usually extend far beyond

[2] Richard H. Mattoon, "State And Local Government Public Pension Forum: A Conference Summary," The Chicago Fed, May 2006, p. 2, available from http://chicagofed.org/publications/fedletter/cflmay2006_226a.pdf (accessed January 15, 2009).

the public administrators and employees (and their unions and associations) that are directly affected."[3]

Treating public pension reform primarily as a technical, fiscal, or actuarial exercise is self-defeating because the key decision-makers are motivated by political, not economic, incentives. While officials in the private sector are driven, for better or worse, by investors who keep a fierce watch on profitability, public officials are judged by more ambiguous criteria. Public officials depend on public support; they must marshal votes and win elections, or at least be appointed and supported by elected officials, and cultivate influential, organized, and attentive constituencies. And few potent constituencies are focused on fiscal health or rationalizing benefit systems.

Unlike institutional shareholders, voters have little cause to focus upon balance sheets or on whether public agencies are maximizing productivity.[4] Instead, voters are most concerned with ensuring that taxes are not raised and that state programs that directly benefit them are maintained. Revising existing arrangements to promote amorphous ends like fiscal responsibility or teacher quality, however, imposes costs on a distinct and organized constituency of veteran teachers.

The costs of reform are concentrated upon today's career educators and union stalwarts. The benefits are spread widely among the state's citizens, prospective teachers, or teachers who are early in their careers or are uncertain of how long they will continue teaching. Long-time public employees have a great deal invested in existing pension systems. They have contributed to the plans over a period of years, understood their promised pension as a key element of their

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[3] EBRI, "The Fundamentals of Employee Benefit Programs," 2005, p. 4, available from www.ebri.org/publications/books/index.cfm?fa=fundamentals (accessed January 16, 2009).
[4] For a further discussion, see Frederick M. Hess, *Revolution at the Margins* (Washington, D.C.: Brookings Institution Press, 2002), p. 8-14.

compensation, and traded the opportunities they might have pursued in the privates sector for the security and assurances implied by public employment. The politics are predictable. Those who stand to lose are typically more energized, organized, and vocal than any of the potential beneficiaries, making it unpopular and politically perilous for public officials to address funding shortfalls or change retirement rules. This dynamic is not unique to pension politics; it is visible in policies from sugar subsidies to highway aid. Public officials will be loath to challenge the interest of an organized, attentive, and vocal constituency so long as they can acquiesce discreetly.

These political dynamics can flip when a fiscal crisis makes pension costs salient to the broader public by highlighting how its interests are being compromised or the public purse emptied in order to cater to public employees. Even amidst crises, however, reforms have often led to more sustainable benefit levels, but have done little to alter the seemingly intractable problem of rationalizing these systems. Addressing the pension challenge, then, is not merely a matter of technical patches; it requires understanding the complexity of the problem and the politics and incentives that shape pension reform.

What's the Problem?

Public pension systems are subject to three key political tensions. The first is that pensions are in the business of delayed gratification. They withhold money from employees today in order to provide benefits decades later. This is markedly out of sync with the interests of politicians, who run for reelection every few years and have every interest in delivering benefits today while pushing off the costs until later. Politicians are favorably disposed to generous pensions, as Olivia Mitchell and Kent Smetters of Wharton Business School note,

pensions "systematically transfer risk away from early generations and toward later generations…favor[ing] current taxpayers, plan participants, and politicians, at the expense of future taxpayers."[5] Lance Weiss, a senior manager at Deloitte Consulting in Chicago, has similarly explained, "Public pension policy often suffers from an 'It won't be my problem after I am out of office' mentality… Policy leaders reap political rewards for creating new benefits for public employees or underfunding retirement systems and using the money for other short-term goals."[6]

The costs and the full benefits of pension systems can be opaque to the larger public, so the incentives for legislators to make generous promises can be hard to resist. Marguerite Roza, of the University of Washington, has observed, "Teachers' retirement benefits, like their health benefits, are, on average, unusually generous when compared to the benefits received by employees in the private sector."[7] Renowned Harvard economist Edward Glaeser has opined, "Our local governments have pensions that are too high and salaries that are too low, because everyone screams at the prospect of a public servant getting paid a decent wage, but no one who isn't a CPA can figure out how much a benefits package is worth."[8] Glaeser has observed the "strong tendency to load compensation towards non-transparent forms of payment."[9]

The second, and perhaps most substantively relevant, challenge is that defined-benefit plans reflect an expectation that personnel will teach in the same state—or even the same district—for the length of their career. In 2007, an employee had to work approximately six

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[5] Olivia S. Mitchell and Kent Smetters, *The Pension Challenge: Risk Transfers and Retirement Income Security* (Oxford: Oxford University Press, 2002), p. 103.
[6] Deloitte Research, "Paying for Tomorrow: Practical Strategies for Tackling the Public Pension Crisis," 2006, p. 9, available from http://www.deloitte.com/dtt/cda/doc/content/VE_PS_Payingfortomorrow_dic06%281%29.pdf (accessed January 15, 2009).
[7] Marguerite Roza, "Frozen Assets: Rethinking Teacher Contracts Could Free Billions for School Reform, Education Sector, January 2007, available from http://www.educationsector.org/usr_doc/FrozenAssets.pdf (accessed January 15, 2009).
[8] Edward L. Glaeser, "Cleaning up the public pension system," *Boston.com*, April 30, 2007.
[9] Edward L. Glaeser, "Cleaning up the public pension system," *Boston.com*, April 30, 2007.

years to become fully vested in the typical public pension fund, with seven of the nation's largest teacher pension funds requiring ten years of service or more. Pension systems reflect a strict careerist tilt, in which educators are penalized for departing the profession before serving 25 years and in which they are penalized if they stay any longer—creating sharp cliffs that induce educators to stay when they are worn out or no longer effective and push teachers out even if they still have productive years ahead of them. Today's pension systems are not designed to enhance the management of the contemporary labor force but are a legacy adopted decades ago and designed to work in a very different labor market.

Economists Robert Costrell and Michael Podgursky have observed how pension rules influence teachers contemplating retirement and teacher quality, noting, "Teachers typically earn relatively little in the way of pension benefits until they reach their early fifties, when much larger benefits start to accrue. The system therefore pulls teachers to 'put in their time' until then, whether or not they are well-suited to the profession. Beyond that point, the pension system quickly begins to punish teachers for staying on the job too long, pushing them out the door at a relatively young age, often in their mid-fifties, even if they are still effective."[10]

Existing pension policies reduce worker flexibility and leave teachers hesitant to consider moving across state lines or across sectors—discouraging potential entrants who might not be inclined to commit to a decades-long career. A more flexible model would reduce the number of veteran teachers who feel compelled to put in their time in order to collect their full pension, ease exit from and reentry into the profession, give teachers more geographical flexibility, and enable the teaching profession to more effectively compete for college-educated talent. Such a model would incorporate defined-contribution plans, which are more amenable to employees in a

[10] Michael Podgursky and Robert M. Costrell, "Peaks, Cliffs, & Valleys: The Peculiar Incentives of Teacher Pensions," *Education Next*, Winter 2008, p. 22, available from http://www.hoover.org/publications/ednext/11130171.html (accessed January 15, 2009).

mobile workforce because they are portable, they make it clear how much any given employee is saving, and they allow employees to take the full value of their contributions with them if and when they change jobs.

Defined-benefit plans, on the other hand, almost always penalize employees for departing in their first decade of employment while offering substantial rewards to employees who remain in place for two decades or more. Defined-benefit plans also make the actual accumulated savings of a given employee much less straightforward, causing potential hires to underestimate the total compensation being offered.

Shifting from defined-benefit to defined-contribution retirement plans would reflect broader trends in the American economy. In 1979, 62 percent of private-sector workers were enrolled in defined-benefit plans, compared to 16 percent in defined-contribution plans. By 2005, those numbers had reversed, with 63 percent of private-sector workers participating in defined-contribution plans and just 10 percent participating in defined-benefit plans. In other words, most employers are responding to a more mobile world by making it easier for workers to enter or exit jobs without putting retirement benefits at risk.[11] That has not been the case in K-12 schooling. Matthew Lathrop, of the American Legislative Exchange Council, has noted, "The guaranteed benefit is only good for those who spend a substantial part of their career with one employer. That's an enormous drawback in today's economy."[12]

Finally, a third and related challenge is that many stakeholders—including legislators, board members, employee unions, fund management firms and actuaries—may have investment preferences that are not necessarily aligned to the long term interest of the fund. This can be due to a desire to hire management firms or to make investment decisions based on political, rather

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[11] Employee Benefits Research Institute, "Facts from EBRI," June 2007, p. 2, www.ebri.org/pdf/publications/facts/0607fact.pdf (accessed January 15, 2009).
[12] Julie Blair, "New Pension Plans Provide Educators with Options, Risks," *Education Week*, April 3, 2002, p. 1.

than fiduciary, considerations. Political officials and pension boards may also have incentives to take undue risks, since they stand to reap the benefits of successful but risky investments in the short term (e.g. by providing larger payouts or collecting smaller contributions) while pushing the consequences of shortfalls off until later. As pension expert David Hess has noted, "In addition to personal political motivations, outside political pressure, such as from the local mayor or governor, may be placed on politically-affiliated trustees." [13]

Illinois's infamous Governor Rod Blagojevich illustrates the allure that pension assets can hold for elected officials. In February 2003, Blagojevich "refinanced" Illinois' pension plan by issuing pension obligation bonds.[14] This entailed borrowing money at a six percent interest rate rather than raising the requisite $1.9 billion through taxes. Then, in March 2004, he cut the state's contribution to the pension fund in order to shore up the state budget.[15] Jon Bauman, executive director of the Illinois' Teachers Retirement System wryly observed, "It's a little bit like if you refinanced your house to save $60 a month and then went out and bought a Porsche."[16]

Such practices are familiar, popular short-term patches for public officials. Perhaps most notable in Illinois was the 2005 scandal involving Blagojevich and pension board member Stuart Levine. An ongoing investigation has unearthed an alleged kick-back scheme, rewarding pension board members for directing pension funds toward investment and consulting firms. The investigation revealed links to supporters of Blagojevich's gubernatorial campaign,

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[13] David Hess, "Protecting and Politicizing Public Pension Fund Assets: Empirical Evidence on the Effects of Governance Structures and Pracitces," University of California-Davis Law Review, 2005, p. 197, available from http://lawreview.law.ucdavis.edu/issues/Vol39/Issue1/DavisVol39No1_HESS.pdf (accessed January 15, 2009).
[14] John Chase and Ray Long, "State Floats Refinancing of Pensions to East Debt," *Chicago Tribune*, February 27, 2003, p. N1.
[15] Leslie Griffy, "Gov's Plan to Cut Pension Funding Could Cost $20 Billion, Critics Say," *Chicago Sun-Times*, March 15, 2004, p. 16.
[16] Leslie Griffy, "Gov's Plan to Cut Pension Funding Could Cost $20 Billion, Critics Say," *Chicago Sun-Times*, March 15, 2004, p. 16.

including convicted felon Antoin Rezko.[17] In less extreme cases, a pension board may choose to divest in companies whose politics or employment practices it finds unappealing or choose to keep business in-state by hiring a local fund management firm. Such decisions, while legal, frequently do not serve the broader public interest in the efficient delivery of benefits.

Public Pensions and State Government

Pension funds are hard-wired to the state political process by constitutional provisions, statutes, and collective bargaining agreements. The American Association of Retired People (AARP) reported in 2000 that 31 states have 93 constitutional provisions that establish governing structures and secure the rights of beneficiaries.[18] All other states either have protections for pensions written into statute or recognized under common law.[19] The Government Accountability Office's Director of Education, Workforce, and Income Security Barbara Bovbjerg, has explained, "These constitutional pension provisions prescribe some combination of how pension trusts are to be funded, protected, managed, or governed."[20]

State benefit formulas (including eligibility, contributions, and types of payments) are set by the legislature. Locally administered plans are typically governed by local laws. Boards of trustees establish the overall policies for the operation and management of the fund.

[17] Chris Fusco and Dave McKinney, "Feds Probe Gov Aide's Pension Role: Ex-Advisor's Firm Got $10 Million Investment Contract," *The Chicago Sun-Times*, August 11, 2005, p. 8.

[18] Government Accountability Office, Report to the Committee on Finance, U.S. Senate, "State and Local Government Retiree Benefits: Current Status of Benefit Structures, Protections, and Fiscal Outlook for Funding Future Costs," September 2007, p. 19. AARP has not conducted a similar analysis since 2000. The report's authors indicate that there have been few changes to constitutional pension protections since then and the GAO's review of the material in 2007 indicated that Oregon was the only state to add a constitutional provision during this time.

[19] Barbara D. Bovbjerf, Director of Education, Workforce, and Income Security and the Government Accountability Office, "State and Local Government Pension Plans: Current Structure and Funded States," Testimony before the Joint Economic Committee, July 10, 2008, p. 13, available from http://www.gao.gov/new.items/d08983t.pdf (accessed January 15, 2009).

[20] Barbara D. Bovbjerf, Director of Education, Workforce, and Income Security and the Government Accountability Office, "State and Local Government Pension Plans: Current Structure and Funded States," Testimony before the Joint Economic Committee, July 10, 2008, p. 13, available from http://www.gao.gov/new.items/d08983t.pdf (accessed January 15, 2009).

Boards of trustees typically have significant independence to manage and invest within the framework of state statutes governing actuarial assumptions, procedures for financial control and reporting, and investment policy. As creatures of the state, the behavior of pension boards is influenced by how rules are written, how personnel are appointed, and how their mission is defined. Boards are organized in a variety of ways. Some plans are overseen by elected officials and others by self-perpetuating boards; some have precise policies governing investments and the evaluation of performance while others have few formal policies; and some favor patient investment strategies while others trade much more actively.[21]

Pension boards vary substantially in size and composition. The National Association of State Retirement Administrators (NASRA) reports that boards range in size from 19 members (in the Tennessee Consolidated Retirement System) to five (in several states). Some boards are composed entirely of elected officials, others entirely of appointed members, and some entirely by ex officio members, but most include some combination of these.[22] The Public Pension Coordinating Council reports that the typical board is composed of 36 percent elected trustees, 15 percent ex officio trustees, and 44 percent appointed trustees.[23] Most governing boards do not handle investment decisions themselves but use outside firms to gauge requisite funds and manage investments.

While some intriguing research has sought to identify correlations between board characteristics and pension outcomes, that work has delivered a mixture of findings that are far

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[21] Michael Useem and Olivia S. Mitchell, "Holders of the Purse Strings: Governance and Performance of Public Retirement Systems," Pension Research Council, March 2000, available at http://knowledge.wharton.upenn.edu/paper.cfm?paperID=920 (accessed January 8, 2009).

[22] NASRA, Composition of Public Retirement System Boards. Note: This survey was not a complete survey of all pension boards, and only surveyed *state* level pension boards – so generalizing about the frequency of different board compositions is difficult.

[23] David Hess, "Protecting and Politicizing Public Pension Fund Assets: Empirical Evidence on the Effects of Governance Structures and Pracitces," University of California-Davis Law Review, 2005, p. 196, available from http://lawreview.law.ucdavis.edu/issues/Vol39/Issue1/DavisVol39No1_HESS.pdf (accessed January 15, 2009).

from dispositive.[24] Rather than focus upon the particulars of boards and plan arrangements, this analysis instead focuses on the broader political pressures at work.

Crucially, pension benefits are considered the property of beneficiaries. This makes them very different from, for example, Social Security benefits. State legislatures can change the terms of benefits for new hires but have little ability to adjust benefits already promised.[25] The National Conference of State Legislature's Ron Snell has explained, "It is very difficult or impossible to reduce pension benefit packages because of various constitutional and statutory guarantees and judicial decisions. Once granted, a pension is a contractual obligation of the employer, so that in most cases in most states it is impossible to cut the promise of a future benefit, or even to increase the employee contribution to the pension fund."[26] This means that if investments perform poorly, the employer (i.e. taxpayers) must usually make up any shortfall.

In some cases, pension benefits are not laid out in state or local statute but are negotiated between employers and unions, though the U.S. Department of Labor reports that the vast majority are determined by state legislatures rather than through collective bargaining

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[24] Olivia S. Mitchell and Ping Lung Hsin, "Public Sector Pension Governance and Performance," in *The Economics of Pensions: Principles, Policies and International Experience*, ed. Salvador Valdes Prieto (Cambridge: Cambridge University Press, 1997); Olivia S. Mitchell & Robert S. Smith, "Pension Funding in the Public Sector," *Review of Economics and Statistics* 76, no. 278 (1994); Marguerite Schneider and Fariborz Damanpour, "Public Choice Economics and PublicPension Plan Funding, an Empirical Test," *Administration and Sociology* 57, no. 34 (2002): 75-76; Barbara A. Chaney et al., "The Effect of Fiscal Stress and Balanced Budget Requirements on the Funding and Measurement of State Pension Obligations," *Journal of Accounting and Public Policy* 21, no. 287 (2002): 306-307; Roberta Romano, "Public Pension Fund Activism in Corporate Governance Reconsidered," *Colorado Law Review* 93 (1993): 795, 822; Kevin J. Murphy & Karen Van Nuys, "Governance, Behavior, and Performance of State and Corporate Pension Funds," University of Southern California, September 1994, p. 33-34, available from http://www-rcf.usc.edu/~kjmurphy/Pensions.pdf (accessed January 16, 2009).

[25] Barbara D. Bovbjerf, Director of Education, Workforce, and Income Security and the Government Accountability Office, "State and Local Government Pension Plans: Current Structure and Funded States," Testimony before the Joint Economic Committee, July 10, 2008, p. 14, available from http://www.gao.gov/new.items/d08983t.pdf (accessed January 15, 2009).

[26] Ron Snell, "Pension Tension: Very Few States Hold All the Assets They Should for Future Retirement and Health Care Benefits," *State Legislatures,* May 2008, p. 13-14, available from http://www.ncsl.org/magazine/articles/2008/08SLMay08_Pensions.htm (accessed January 15, 2009).

agreements.[27] Moreover, the Employee Benefit Research Institute has noted, "Even where collective bargaining over benefit issues is allowed, the legislatures generally retain some measure of control."[28]

Most teachers' pensions are included in plans that cover other public employees. In 33 states, teacher contributions go into a state fund; in the other 17 they contribute to a separate teacher retirement fund.[29] Many other school districts have their own, localized, pension plans for teachers. There are currently over 2,500 public pension plans across the country. Ninety percent of state and local workers are enrolled in state-administered plans, with the remainder participating in local plans.[30]

Legislators naturally prefer to see pension funds capture high returns—allowing them to minimize taxes or divert state contribution dollars to other budget items. If pension investments do not perform well enough to compensate for additional costs, the government must make up the difference. As David Hess has explained, "Since these additional contributions typically come from the government's general fund, they compete for funding with other government projects."[31] Given such alternatives, underfunding a pension plan can be an appealing option for policymakers—especially because the complexity of determining future liabilities and adequate funding levels provides public officials with substantial wiggle room.

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[27] Barbara D. Bovbjerf, Director of Education, Workforce, and Income Security and the Government Accountability Office, "State and Local Government Pension Plans: Current Structure and Funded States," Testimony before the Joint Economic Committee, July 10, 2008, p. 12, available from http://www.gao.gov/new.items/d08983t.pdf (accessed January 15, 2009).
[28] Employee Benefits Research Institute, "Facts from EBRI," June 2007, p. 3, www.ebri.org/pdf/publications/facts/0607fact.pdf (accessed January 15, 2009).
[29] Myron Lieberman, *The Teachers Unions* (San Francisco: Encounter Books, 2001), p. 169.
[30] Government Accountability Office, "State and Local Government Retiree Benefits: Current Status of Benefit Structures, Protections, and Fiscal Outlook for Funding Future Costs," Report to the Senate Committee on Finance, September 2007, p. 18, available from http://www.gao.gov/new.items/d071156.pdf (accessed January 15, 2009).
[31] David Hess, "Protecting and Politicizing Public Pension Fund Assets: Empirical Evidence on the Effects of Governance Structures and Pracitces," University of California-Davis *Law Review*, 2005, p. 193, available from http://lawreview.law.ucdavis.edu/issues/Vol39/Issue1/DavisVol39No1_HESS.pdf (accessed January 15, 2009).

Actuaries are charged with projecting the future costs of pension benefits and estimate the rate of return that the fund can expect. However, these estimates are widely recognized as malleable figures and board members have incentives to prefer actuaries and firms deemed to be team players. By manipulating actuarial assumptions, such as an expected rate of return, a fund can appear more funded than it would be if it used more conservative assumptions. Scholars Tim Eaton and John Nofsinger have also suggested that pension funds are systematically more likely to use assumptions requiring lower government contributions during fiscal downturns in order to mask shortfalls.[32] Indeed, many economists fear that actuaries are routinely underestimating the cost of public pensions by as much as a third.[33] Intended safeguards like independent pension boards and actuarial expertise too often provide a flimsy bulwark against chicanery or political irresponsibility.

Pensions and Public Employee Unions

Two dynamics of teacher union politics dominate public pensions. The first, and most obvious, is that those who are in line for pensions are intensely interested in the contributions they are asked to make, the age at which they become eligible for benefits, and the size of the benefit they will receive. Those who do not stand to benefit—meaning everyone in the state or community who is not a public employee—have little at stake in such questions. For disinterested parties, public employee benefits are one government outlay among many, one that exists outside of routine budget processes and one rarely scrutinized by the media. Even substantial changes to pension systems are unlikely to have more than a glancing impact on any individual taxpayer. Meanwhile, public employees are intensely interested, organized, and

[32] Tim V. Eaton & John R. Nofsinger, "The Effect of Financial Constraints and Political Pressure on the Management of Public Pension Plans," *Journal of Accounting and Public Policy* 23 (2004): 161, 169.
[33] Mary Williams Walsh, "Actuaries Scrutinized on Pensions," *The New York Times*, May 21, 2008.

aware that modest tweaks to formulas or retirement eligibility could be worth tens or hundreds of thousands of dollars to them personally. Consequently, public officials are presented with an active, organized, and influential constituency demanding generous benefits and minimal costs and opposition that is typically nonexistent or restricted to anti-tax activists or budget watchdogs that lack the votes, network, and resources of the public employee unions.

The second dynamic is the inevitable tension between younger public employees and their veteran peers. Veteran employees are deeply invested in promised benefits and regard any effort to alter those benefits as an attempt to renege on a promise. Newer employees have much less at stake. They are much further from collecting benefits, have contributed little into the system, and consequently face much smaller opportunity costs should they change employers. Moreover, newer teachers by and large younger and part of a generation that is much more familiar with a highly mobile job market than are teachers who entered the workforce two decades ago. Existing pension systems are a legacy of the industrial era, a time when employees routinely stayed with one employer for decades or their entire career—and where benefits premised on long service were the norm. Today, that is no longer the case for talented college graduates. The outdated system puts school systems at a disadvantage when it comes to recruiting and retaining that mass of potential hires who are not necessarily expecting to spend two decades or more teaching in a particular state.

The split between newer teachers and their veteran colleagues show up clearly, to take one example, in a 2008 Education Sector national survey of teachers. Twenty-six percent of recent hires think that the unions "lean more toward taking care of the needs of veteran teachers"

and just four percent think that they favor newer teachers.[34] New teachers are more likely to favor reforming traditional pay systems than veteran teachers. They are ten to twenty percentage points more likely than veteran teachers to favor giving financial incentives to teachers whose classes routinely outperform on standardized tests, who hold certification from the National Board for Professional Teaching Standards, or who receive outstanding evaluations from their principals.[35] Veteran teachers who entered the profession under the implicit understanding that they would not be monetarily rewarded for excellence but would be provided with job security, consistent pay raises, and a lucrative benefits package, are naturally less receptive to measures that would upend those arrangements than are teachers who have not made those same trade-offs and who have not spent decades in teacher lunchrooms and faculty meetings with like-minded colleagues.

Veteran interests typically predominate in negotiations and public debates. While it is theoretically possible for rapid staff turnover or aggressive organizing efforts spearheaded by a cohort of Teach For America entrants to give newer employees the upper hand in one or another locale, such an outcome is rare. The ranks of union leaders are dominated by long-time educators, as the process of establishing rank-and-file credibility typically takes years and requires extended service in a variety of lesser posts. Given the day-to-day demands on new teachers and the fact that approximately half of new teachers exit the profession within five years, it is no surprise that most teachers actively involved in union affairs are several years into

[34] Ann Duffett, Steve Farkas, Andrew J. Rotherham, and Elena Silva, "Waiting To Be Won Over: Teachers Speak on the Profession, Unions, and Reform," Education Sector, May 6, 2008, p. 14, available from http://www.educationsector.org/usr_doc/WaitingToBeWonOver.pdf (accessed January 15, 2009).
[35] Ann Duffett, Steve Farkas, Andrew J. Rotherham, and Elena Silva, "Waiting To Be Won Over: Teachers Speak on the Profession, Unions, and Reform," Education Sector, May 6, 2008, p. 14, available from http://www.educationsector.org/usr_doc/WaitingToBeWonOver.pdf (accessed January 15, 2009).

their tenure. As Ed McMahon of the Manhattan Institute has summarized, "The most senior employees…tend to wield the most clout within the unions."[36]

Union leaders in education, as in any sector, also place a premium on maintaining solidarity and unity—prompting them to prefer uniform, collective benefit systems and be disinclined to accept measures which differentiate employees or create individualized accounts. Given these dynamics, union demands are unsurprising. Union leaders want their members to receive comfortable benefits, want large taxpayer subsidies for those benefits, and want to be confident that the rules won't be changed on employees in the midst of their careers. Given their confidence that schools will not shutter due to international competition or pick up and relocate south of the border, teacher unions have little cause to fear that benefits would destroy jobs. Indeed, efforts to reduce class size have led to a 51 percent increase in the teacher workforce since 1980, creating more than a million new teaching jobs with no obvious negative impact on teacher benefits.[37]

The steadfast opposition of National Education Association (NEA) and American Federation of Teachers (AFT) affiliates and fellow employee unions to measures that would scale back benefits, increase employee contributions, or render the existing system more attractive to younger employees has typically been enough to stifle serious proposals to alter pension rules except in the most extraordinary crises. Indeed, while some observers have been trumpeting the need to overhaul teacher pensions since the 1970s, just eleven states and the

[36] E. J. McMahon, "Diffusing the Pension Bomb: How to Curb Public Retirement Costs in New York State," *Civic Report*, November 2003, p. 19, available from http://www.manhattan-institute.org/html/cr_40.htm (accessed January 15, 2009).
[37] National Center on Education Statistics, "Digest of Education Statistics," U.S. Department of Education, 2007, table 4, available from https://www.nces.ed.gov/programs/digest/d07/ (accessed January 15, 2009).

District of Columbia have adopted any kind of defined-contribution alternatives; and just four of these have defined-contribution plans as their primary plans.[38]

The source of teacher union influence on pensions also lies in their numbers, resources, and organization. While union membership in the U.S. has steadily declined in recent decades, from 24 percent of all public and private employees in 1973 to 12 percent in 2006,[39] public sector unions have gained in strength. Union membership among public sector employees grew from 23 percent in 1973 to 36 percent in 2006. While public and private sector employees were unionized at similar rates in 1973, by 2006 the public sector rate of 36 percent dwarfed the private sector rate of 7.5 percent.[40] This shift strengthened public employee unions and gave them an increasingly significant role in the ranks of organized labor. Public education's teacher unions, given the sector's 3.3 million full-time teachers, more than five million total employees, and millions of retirees, today rank among the nation's most influential unions. Indeed, with more than 80 percent of the nation's teachers in a union, teaching is the most highly unionized sector in America.[41] Nearly all belong to either the National Education Association or the American Federations of Teachers.

Including teachers and other employees in allied "education, training and library occupations," the NEA represents a total of 3.2 million[42] and the AFT a total of 1.4 million

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[38] Barbara D. Bovbjerf, Director of Education, Workforce, and Income Security and the Government Accountability Office, "State and Local Government Pension Plans: Current Structure and Funded States," Testimony before the Joint Economic Committee, July 10, 2008, p. 8, available from http://www.gao.gov/new.items/d08983t.pdf (accessed January 15, 2009).
[39] Census Bureau, "Historical Tables: Union Membership, Coverage, Density, and Employment, 1973 – 2007," available from http://www.unionstats.com (accessed January 15, 2009).
[40] Census Bureau, "Historical Tables: Union Membership, Coverage, Density, and Employment, 1973 – 2007," available from http://www.unionstats.com (accessed January 15, 2009).
[41] Deidre McFadyen, "Movement in Decline… And Why it Matters to UFT Members," *New York Teacher*, October 5, 2006, available from http://www.uft.org/news/teacher/labor/movement_decline (accessed January 15, 2009).
[42] National Education Association, "Influential Educators Elected to Represent 3.2 Million NEA Members," Press Release, 2008, available from http://www.nea.org/home/11082.htm (accessed January 16, 2009).

members (most, but not all, of them are teachers).[43] Surveying political contributions from 1989 to 2008, the nonpartisan Center for Responsive Politics named the NEA and AFT as two of the nation's twenty "most influential organizations in federal politics," with the NEA ranked 7th and the AFT 15th.[44] In the past eight years, the NEA and AFT have ranked among the top contributors to 24 of the 27 Democrats on the U.S. House of Representatives Education and Workforce Committee.[45] *Fortune Magazine* named teachers unions one of the 25 most influential interest groups in 2008.[46] In 2007, the NEA spent nearly $30 million on political activities and lobbying[47] and the smaller AFT over $18 million.[48]

It would be a mistake, however, to think the strength of the NEA or the AFT primarily lies in Washington. Most observers regard the unions as strongest at the state and local level where 90 percent of education spending takes place. Stanford political scientist Terry Moe has written that, in state legislatures, "The teacher unions are aggressive, omnipresent participants. This is often true even in right-to-work states. They monitor all relevant legislation, propose bills, carry out background research on issues, attend committee hearings, keep scorecards on legislators, and bring their formidable

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[43] American Federation of Teachers, "American Federation of Teachers Endorses Sen. Barack Obama," Press Release, July 13, 2008, available from http://www.aft.org/presscenter/releases/2008/071308.htm (accessed January 16, 2009).
[44] Open Secrets Center for Responsive Politics, 2008 database search for National Education Association, http://www.opensecrets.org/usearch/searchresults.php?searchTerm=National%20Education%20Assn&type=O
[45] Open Secrets Center for Responsive Politics, database analysis by the authors.
[46] Jay P. Greene and Jonathan Butcher, "Proximity and Power," *America.com*, May 8, 2008, available from http://www.american.com/archive/2008/may-05-08/proximity-and-power/?searchterm=jay%20greene (accessed January 15, 2009).
[47] U.S. Department of Labor, LM-2 Form for Labor Organization Annual, National Education Association, 2008, available from http://erds.dol-esa.gov/query/getOrgQry.do (accessed January 16, 2009).
[48] U.S. Department of Labor, LM-2 Form for Labor Organization Annual, American Federation of Teachers, 2008, available from http://erds.dol-esa.gov/query/getOrgQry.do (accessed January 16, 2009).

power to bear…On education, teacher unions are the 500-pound gorillas of legislative politics."[49]

Helping to explain union influence, economist Richard Freeman has reported that union members are about 12 percentage points more likely to vote than other citizens.[50] That finding echoes decades of research showing union members are more likely to vote than are nonmembers.[51] Stanford's Terry Moe has documented how teacher union influence is exercised, reporting that, in California's largest school districts, unions "support candidates for office in 92 percent of these districts. They make phone calls in 97 percent, they campaign door-to-door in 68 percent, and they provide mailings and publicity in 94 percent."[52]

Union clout was famously displayed in California in January 2005, when Governor Arnold Schwarzenegger proposed converting public pensions in California from defined-benefit plans to 401(k)-style defined-contribution plans. He explained that California had promised "state workers more than it should and more than it could," noting that pension obligations had grown from $160 million in 2000 to $2.6 billion in 2005.[53] Schwarzenegger proposed that pensions for new state workers reflect those for workers without government jobs.[54] He said that

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[49] Terry M. Moe, "A Union By Any Other Name," *Education Next*, Fall 2001, available from http://www.hoover.org/publications/ednext/3384186.html (accessed January 15, 2009).
[50] Richard Freeman, "What Do Unions Do ... to Voting?" presented at Cornell Labor Seminar *Welfare and Inequality in Advanced Industrial Societies* April 4, 2002.
(September, 2003). Revised as "What Do Unions Do to Voting Turnout?" February 2004.
[51] John Thomas Delaney, Marick F. Masters, and Susan Schwochau, "Unionism and Voter Turnout," *Journal of Labor Research*, September 1988.
[52] Terry M. Moe, "Teachers Unions and School Board Elections," in *Besieged: School Boards and the Future of Education Politics,* edited by William Howell (Washington, D.C.: Brookings Institution Press, 2005), p. 261.
[53] Arnold Schwarzenegger, "Governor Promotes Pension Reform Proposal in San Diego," speech delivered on February 10, 2005, available from http://gov.ca.gov/index.php?/speech/2280 (accessed January 15, 2009).
[54] Arnold Schwarzenegger, "Governor Promotes Pension Reform Proposal in San Diego," speech delivered on February 10, 2005, available from http://gov.ca.gov/index.php?/speech/2280 (accessed January 15, 2009).

if the Democratic-controlled state legislature did not support his proposal, he would put forward a referendum on the issue the following November.[55]

The proposed reforms drew immediate criticism from California's public employee unions.[56] The *San Francisco Chronicle* predicted, "Labor unions and education groups… will put up whatever it takes to challenge the governor."[57] Within weeks of Schwarzenegger's announcement, the California School Employees Association boasted that twenty unions representing 2.5 million members had already formed a "pension protection coalition."[58]

The union message was carried forth by sympathetic figures like teachers, nurses, firefighters, widows, and orphans who portrayed Schwarzenegger as cruel and out of touch. By spring, Mark Barabak and Robert Salladay observed in the *Los Angeles Times*, "In just a few months, Schwarzenegger has gone from seeming invincibility to a politically precarious state, his approval ratings sagging and his staff plagued by internal scuffles."[59]

In April, Schwarzenegger abandoned the proposal. Though he vowed to address the issue later, he ultimately settled for a commission to study the California pension system. Schwarzenegger's Post-Employment Benefits Commission submitted its report in July 2007 and issued 34 recommendations. Former Assemblyman Keith Richman dismissed the recommendations as failing to "address any of the substantive issues."[60] Ultimately, the bold effort led to a modest concession from California's State Teachers Retirement System

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[55] Evan Halper, "State of the State: Governor Targets Public Retirement Plans: Unions oppose proposal to make state pension packages more like private-sector 401(k)s," *Los Angeles Times*, January 6, 2005, A20.
[56] Evan Halper, "State of the State: Governor Targets Public Retirement Plans: Unions oppose proposal to make state pension packages more like private-sector 401(k)s," *Los Angeles Times*, January 6, 2005, A20.
[57] John Wildermuth, "Special Election Could Be Among Most Expensive," *San Francisco Chronicle*, January 7, 2005, A12.
[58] Gilbert Chan, "CalPERS leads fight on pension proposal," *Sacramento Bee,* January 21, 2005.
[59] Mark Barabak and Robert Salladay, "They've All Stepped on Schwarzenegger's Lines," *Los Angeles Times*, April 25, 2005, A1.
[60] Gilbert Chan, "Huge Tab for Retiree Health: Public Employee Costs Will Pass $118.1 billion in Next 30 Years, State Panel Finds," *Sacramento Bee*, January 8, 2008, p. A1.

(CalSTRS) that would allow the state to modestly reduce its contribution under certain circumstances.[61]

Few Safeguards on Public Pensions

There are few meaningful guardrails to prevent public officials from steering state pension systems into the ditch or to remind them of the need to stay on the straight and narrow. As Deloitte Research has pointed out, "There are generally no requirements forcing public retirement plans to fund their pension liabilities. As a result these plans are funded to varying degrees, including some that are completely unfunded and operate on a 'pay-as-you-go' basis."[62] Pension expert David Hess has explained, "Whereas federal law requires private pension plans to meet certain funding levels and insurance requirements, public pension plans do not face such requirements."[63] Private pensions, as Hess notes, are required to comply with the Employee Retirement Income Security Act of 1974 (ERISA), which established minimum funding standards for company sponsored plans. ERISA, which covers approximately 150 million Americans with more than 679,000 private retirement plans, is beset by its own shortcomings, of course, but that is a subject for another time. [64]

Public plans are governed by accounting standards set up by the Governmental Accounting Standards Board (GASB). These standards provide the framework for the annual audits that most governments contract to independent accounting firms, with those audit reports a

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[61] Deb Kollars, "CalSTRS Cuts State a Break: Teachers Pension Giant Agrees to Reduce Required Payments—Up to a Point," *Sacramento Bee*, March 7, 2008, A1.

[62] Deloitte Research, "Paying for Tomorrow: Practical Strategies for Tackling the Public Pension Crisis," 2006, p. 6, available from http://www.deloitte.com/dtt/cda/doc/content/VE_PS_Payingfortomorrow_dic06%281%29.pdf (accessed January 15, 2009).

[63] David Hess, "Protecting and Politicizing Public Pension Fund Assets: Empirical Evidence on the Effects of Governance Structures and Pracitces," *University of California-Davis Law Review*, 2005, p. 193-4, available from http://lawreview.law.ucdavis.edu/issues/Vol39/Issue1/DavisVol39No1_HESS.pdf (accessed January 15, 2009).

[64] Department of Labor, "About the Employee Benefits Security Administration," available from http://www.dol.gov/ebsa/aboutebsa/main.html (accessed January 15, 2009).

key factor in how credit risk agencies evaluate government credit quality. While GASB sets guidelines, however, it has little or no enforcement power and limited incentive to confront the states and localities that contribute to its budget. As a result, pension analysts fret that many states have adopted accounting methods determined more by politics than sound fiscal standards.[65]

Not infrequently, watchdog organizations and whistle-blowers have played crucial roles in creating enough visibility to prompt public officials to address pension issues. One such case unfolded in Massachusetts in early 2008, where the Massachusetts Taxpayers Association warned that a proposed boost in pension benefits "could cost the state more than $3 billion over the next 20 years."[66] The MTA president Michael Widmer said, "There is no money to pay for this enhanced benefit, regardless of the merits…It's another example of the administration and the Legislature passing a benefit and simply passing the buck to the future taxpayer."[67]

Governor Deval Patrick had supported the pension boosts, but requested an amendment limiting cost-of-living increases to those whose pensions were below $40,000. The legislature ignored the request, betting that Patrick would not use his veto. "We rolled the dice and we came up empty," said Ralph White, president of the Retired State, County, and Municipal Employees Association of Massachusetts.[68] Widmer, of the Massachusetts Taxpayer Association, said "The easy decision would have been to sign it and give an added benefit to 100,000 employees. But the state didn't have any money to pay for it."[69] The exposure and

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[65] David Cho, "Accounting Methods Threaten Public Pensions," *Washington Post*, June 27, 2008.
[66] Matt Viser, "Patrick Rejects Pension Increase, Benefit Could Have Cost State Billions," *The Boston Globe,* August 12, 2008, B1.
[67] Michael Levenson, "Pension Boost OK'd for State Workers, Patrick Signals Support, Critics Rail At Huge Cost," *The Boston Globe,* August 2, 2008, A1.
[68] Matt Viser, "Patrick Rejects Pension Increase, Benefit Could Have Cost State Billions," *The Boston Globe,* August 12, 2008, B1.
[69] Matt Viser, "Patrick Rejects Pension Increase, Benefit Could Have Cost State Billions," *The Boston Globe,* August 12, 2008, B1.

pressure from watchdog groups can awaken public concerns about unaffordable promises and change the politics of pension promises.

A Familiar Story: Crisis…and Then Reform

It is useful to see how these pressures play out in practice, encouraging gradually expanding promises and spurring public officials to hope that market gains or financial sleight-of-hand can spare them from making unpleasant choices. As the following brief tales from Oregon, New Jersey, and San Diego illustrate, it is only when the gloom of crisis finally descends that public officials muster the will to address the mismatch between promises and resources.

Oregon: "We've run out of excuses, folks"

In November 2002, the Oregon Public Employees Retirement System (PERS) triggered a crisis when it reported a $15 billion shortfall, after raising eyebrows the previous year when it noted an existing shortfall of nearly $10 billion. "We've had a sudden and sharp downturn in the markets that's been a big departure from our expectations," said PERS Executive Director Jim Voytko.[70] The immediate problem was the decline in the equity markets, but the deeper problem was a decade's worth of dubious decisions by the PERS board. During the 1990s, when the PERS fund consistently blew past the eight percent expected return mark—returning as much as 20 percent a year—the PERS board did not use the additional revenue to bolster its reserve funds. Instead, it boosted benefits at record rates and without regard to repeated warnings the system was being exposed to calamity.[71]

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[70] Brent Walth, "Shortfall in State Pension Fund Swells," *The Oregonian*, November 20, 2002, A1.
[71] Brent Walth, "Shortfall in State Pension Fund Swells," *The Oregonian*, November 20, 2002, A1.

Oregon's pension system had been regarded as lavish for more than two decades. A 1990 study by Portland's city auditor found that many workers retired with more take-home income than they earned while working, partly because they could roll in half of their unused sick leave. The official goal of PERS was to provide career public employees with the same net income in retirement, factoring in Social Security, as they had while working.[72] In 1994, *The Oregonian* reported that some financial advisors were telling clients not to bother saving for retirement at all. The paper noted advisors saying, "PERS benefits are so generous that it's not necessarily wise for public employees to sock away today's income for tomorrow's retirement. They just won't need the money." Ken Sutherland, an insurance company representative who worked with PERS members, said, "They don't realize how good they have it."[73]

In November 2002, *The Oregonian*'s Steve Duin railed, "We've run out of excuses, folks. At $15.7 billion, the unfunded liability for the Public Employees Retirement System works out to a $4,589 debt for every man, woman and hungry child in Oregon, including those who still have their heads in the sand. Not your problem, you say? Think again. YOUR Oregon Legislature greased the skids of this disaster, screwing up the compensation formulas, guaranteeing 8 percent annual returns, and stocking the PERS board with the government managers and union reps who pushed boom-time profits into retirement accounts instead of rainy-day funds."[74]

PERS officials issued preliminary estimates of the necessary increases in employer contributions the following month, forcing city managers, county officials and school leaders to confront the budgetary impact.[75] The *Oregonian* reported, "The growing pension costs will further drain the budgets of state and local governments—including those of school districts,

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[72] Jeff Mapes, "Oregon's PERS Under Intense Scrutiny," *The Oregonian,* April 11, 1993, C1.
[73] David Reinhard, "PERS: Scapegoats or Sacred Cows?" *The Oregonian*, February 20, 1994, D2.
[74] Steve Duin, "Believe It or Not, PERS is Your Problem," *The Oregonian,* November 24, 2002, B1.
[75] Richard Colby, "New PERS Costs Rock Public Sector," *The Oregonian,* December 11, 2002, C1.

cities and counties—that can't easily raise taxes and are already squeezed by a weak economy."[76] When it was reported that Oregon school districts would have to shell out an additional $123 million per year for pensions, an Oregon School Boards Association lobbyist declared, "That's outrageous," and announced the need for dramatic change—pointing to a new study showing Oregon schools are paying more for employee benefits than any state except Rhode Island.[77] In 2003, newly elected Democratic Governor Ted Kulongoski and the legislature did push to reform the system.

Republicans, who controlled the state House, pushed to recast the retirement system into a defined-contribution 401(k)-like pension, while Democrats, who controlled the state Senate, objected. A hybrid compromise emerged. Retirees would receive a pension benefit intended to approximate 45 percent of their working salary and would also be required to contribute six percent of their salary to a 401(k)-type investment account. Employers could agree to make this contribution in the employees' stead. The plan would cost employers about 8.6 percent of payroll for retirement benefits, compared to the 12.5 percent figure that prevailed.[78] The legislature also remade the PERS board, demanded up-to-date mortality tables, and eliminated the eight percent guaranteed annual growth in accounts.[79]

Because Oregon's plan actually reduced the pension benefits promised to current employees, it came under the inevitable legal challenge from public employee unions. Ultimately, the last hurdle was cleared when, in 2006, the 9th U.S. Circuit Court of Appeals ruled in favor of the state.[80] The result was a deficit that had reached $17 billion in 2003 had become a

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[76] Brent Walth, "Losses Will Drive Up PERS' Cost," *The Oregonian*, April 24, 2002, A1.
[77] *Statesman Journal*, "PERS Rates to Skyrocket in 2003," December 11, 2002, 1A.
[78] James Mayer, "PERS Deal Blends Elements of 401(k), Standard Pension," *The Oregonian,* June 27, 2003, A1.
[79] *The Oregonian*, "As Promised, PERS Reform; Now That Lawmakers Have Done All They Can on PERS, They Must Raise Money For Schools and Other Services," May 9, 2003, C10.
[80] Betsy Hammond, "Ruling Upholds PERS Change," *The Oregonian,* October 25, 2006, C3.

modest surplus by 2008. "It took a lot of political courage because you were really impacting—hurting is the right word—members and retirees," says Paul Cleary, executive director of the Oregon Public Employees Retirement System.[81]

New Jersey: "If the pension system is healthy…I say give it to them"

In the 1990s, New Jersey Governors Jim Florio and Christie Whitman took to balancing the state budget by redirecting dollars that would have otherwise funded the pension system.[82] In an attempt to improve the system's books, Whitman issued $3.4 billion in pension obligation bonds in 1997—essentially borrowing dollars to inject immediately into the pension fund by taking on new long-term obligations. By overfunding the pension fund through the bond initiative, Whitman was able to forego the state's annual contribution to the pension fund and instead use those dollars to avoid spending cuts or tax increases in an election year.[83] The nuts and bolts of Whitman's deal showed what a bad deal it was for New Jersey taxpayers—as the state promised an annual eight percent payment to bondholders, a calculation that made sense only because the state projected it would generate a 12 percent annual return on its investments.[84]

In 1990, a majority of the state's retirement plan assets were in safe, low-yielding, fixed-income accounts. By 2000, about 70 percent were invested in equities.[85] The booming 1990s stock market led to a surplus, prompting state and local government employees to push for a benefit boost in 2000—the last year of the dot-com boom. The acting governor, Republican Donald T. DiFrancesco, said, "The way I look at it, if the pension system is healthy, if we can give them some benefit resulting from the good economy, I say give it to them." In 2001, in the

[81] Dennis Cauchon, "States' Pension Increases Stir Debate" *USA Today*, June 12, 2008, 3A.
[82] Joe Donohue, "Shield for Pension Funds Gains Bipartisan Push," *Star-Ledger*, May 3, 1996, 23.
[83] Joe Donohue, "Pension Bonds Draw Caution on Wall Street," *Star-Ledger*, January 14, 1997, 1.
[84] Joe Donohue, "Teachers Back State Pension Bond Plan," *Star-Ledger,* March 7, 1997, 21.
[85] Kathy Kristof, "Employee Savvy Will Determine Future Benefits," *Star-Ledger*, January 30, 2000, 4.

midst of a heated election season, the legislature voted to enhance pension benefits by nine percent. In doing so, it committed $4 billion of the surplus accumulated during the boom years, despite an $8 billion dip the previous year.[86]

The Pension and Health Benefits Review Commission, made up of Treasury Department representatives and private citizens, voted 7-0 to recommend the Legislature adopt the pension boost."[87] The plan proceeded to sail through a legislative review panel, "generating less than 10 minutes of discussion."[88] Even though the state's pension funds lost $12.5 billion between June 2000 and March 2001—the entire surplus on which the legislature and pension board were counting—DiFrancesco signed the increased benefits into law in June 2001.[89]

In 2002, newly elected governor James McGreevy proposed an early retirement plan in order to reduce budget outlays. Similar efforts by Governor Florio in 1992 and 1994 led to short term budget savings but significantly increased long term pension costs.[90] The bill was nonetheless signed into law on May 31, with Treasury officials conceding the program would cost the state $220 million over the next five years.[91] Lawmakers also enacted dramatic changes at the Division of Investments, the Treasury Department branch that oversees the state's investment portfolio, replacing its director, changing the membership on the State Investment Council, and hiring an outside auditor.[92] By 2003, the state's once flush pension system was among the worst performing in the nation.[93]

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[86] Dunstan McNichol, "Panel Okays Increase in Pensions," *Star-Ledger*, June 9, 2001, 13.
[87] Joe Donohue, "Public Worker Pension Hike Begins Legislative Journey," *Star-Ledger*, May 22, 2001, 14.
[88] Dunstan McNichol, "Panel Okays Increase in Pensions," *Star-Ledger*, June 9, 2001, 13.
[89] Joe Donohue, "Public Worker Pension Hike Begins Legislative Journey," *Star-Ledger*, May 22, 2001, 14; Dunstan McNichol, "Panel Okays Increase in Pensions," *Star-Ledger*, June 9, 2001, 13
[90] Tom Hester, "Retire Early? Jersey Saves But Then Pays," *Star-Ledger*, May 14, 2002, 1.
[91] Tom Hester, "Governor Quickly Signs Bill on Early Retirement," *Star-Ledger*, May 31, 2002, 25.
[92] Dunstan McNichol, "State Considers Using Its Funds to Push for Corporate Reform," *Star Ledger,* December 20, 2002, 38.
[93] Dustan McNichol, "For 600,000 Pensioners, A Wealth of Concern," *Star-Ledger*, January 21, 2003, 9.

Under New Jersey state regulations, pension fund managers were allowed to assume an 8.75 percent return on investments and required to make up the difference when returns fell short. In 2004, local municipalities had to raise taxes to make their contributions to the state pension funds. The East Brunswick Finance Director said, "Everyone knew this holiday was coming to an end" and termed the suspension of state payments in 1997 "a classic example of sacrificing the future on the altar of the immediate."[94] Meanwhile, the McGreevey administration failed to inject the $400 million in 2003 that it was required by law to provide, with the state treasurer explaining the state couldn't "afford to make the contribution."[95]

Teachers unions blamed the state for failing to make required contributions. Lawmakers blamed the investment board for underperformance and called for investments in high-yield bonds and real estate (the investments that were doing well in the aftermath of the dot-com crash).[96] Meanwhile, Governor McGreevey did not direct any money into the pension fund in 2004, despite the actuary's recommendation that a $1 billion infusion was needed.

After McGreevey resigned amidst an unrelated 2004 scandal, acting governor Richard Codey announced that he would not seek election and pledged to veto any legislation that would enhance retirement benefits without paying for them.[97] Codey put aside $337 million in his budget for replenishing the pension system. It was no surprise when the pension crisis emerged as a key issue of the 2005 gubernatorial race.[98] Four union political action committees, including the New Jersey State Laborers PAC and the New Jersey Education Association (NJEA) PAC,

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[94] Tom Hester, "Pension Bill to Top $200M over Five Years," *Star Ledger,* March 16, 2004, 19.
[95] Dunstan McNichol, "Pension Fund For Teachers Asks State for Bailout," *Star-Ledger*, April 4, 2003, 21.
[96] Chris Sanders, "States Fed Up with Pension Managers," *Star-Ledger*, January 15, 2003, 21.
[97] Dunstan McNichol, "'Cadillac' of Plans Targeted," *Star-Ledger*, March 2, 2005, 18.
[98] Joe Donohue, "Pensions and Transit Are Key As Labor PACs Aid Candidates," *Star-Ledger*, October 25, 2005, 16.

were among the top ten givers in that year's campaign.[99] Democratic nominee Jon Corzine, a former Goldman Sachs executive and U.S. Senator, won the gubernatorial election.

After his January 2006 inauguration, Governor Corzine set to work on rehabilitating the state's pension funds. "Make no mistake—our unfunded pension obligation is a real bill," Corzine told lawmakers. Corzine's proposed $1.5 billion contribution would exceed the total payments governors made to the retirement funds over the preceding nine years, but amounted to just 70 percent of the amount actuaries deemed necessary.[100]

Corzine convened a special session to examine public worker benefits and cut property taxes, urging legislators to find ways to reduce pension costs. Proposals included raising the retirement age to 62, adding co-payments for health coverage, and rolling back pension benefits by about nine percent for new employees. Employee unions launched a fierce counterattack, saying that they supported proposals to curtail pension abuses but, in the words of the NJEA, regarded "any reduction in rank-and-file pensions…to be a non-starter."[101] This opposition was important because, noted Senator Gerald Cardinale, a Republican from Bergen County, "Some legislators are so afraid of the NJEA they quake."[102] Corzine responded by agreeing to negotiate with the unions at the collective bargaining table.

Those Democrats who had backed a reform bill in the face of union opposition felt undercut by Corzine's move to the collective bargaining table. "I think there is a fair amount of frustration on the part of members that they extended themselves, demonstrated courage, and it has not led to where it should, in the short term," Assembly Speaker Joseph Roberts said.[103] The

[99] Joe Donohue, "Pensions and Transit Are Key as Labor PACs Aid Candidates," *Star-Ledger*, October 25, 2005, 16.
[100] Dunstan McNichol, "State's Budget Headaches Took Shape Over A Decade," *Star Ledger*, June 19, 2006, 1.
[101] John Mooney, "Teachers Union Vows: Pension Cuts Will Flunk," *Star-Ledger*, November 10, 2006, 26.
[102] Tom Moran, "In Tax Fight, The Teachers Are a Study in Clout," *Star-Ledger*, August 11, 2006, 17.
[103] Deborah Howlett and Dunstan McNichol, "Democrats Say Corzine Turnabout Threatens Reform," *Star-Ledger*, December 9, 2006, 1.

bill that was subsequently passed by the legislature left most major changes to collective bargaining.

Corzine claimed some modest concessions from public workers' unions in the collective bargaining agreement, exchanging 3 to 3.5 percent raises over the following four years in exchange for a 1.5 percent contribution to health care costs, an increase in the retirement age for new workers from 55 to 60, and a cap on pension payments for some highly paid employees.[104] Corzine had made little direct headway on the pension shortfall, but was able to insist on four years of modest raises, returns worth close to $1 billion. The various unions approved the contract a few months later by safe margins. Scott Porter, an actuary for Milliman Consultants observed that the changes would not be visible in the short term. "Twenty years from now, then you'd start to see some of this," he said.[105] "This is a guy [Corzine] who stood up for organizing rights at Rutgers University; who spoke at our rally last summer; who made contributions to our pension for the first time in ten years," said Bob Master, lead negotiator for the Communication Workers of America (CWA). In light of the fact that lawmakers had boosted pensions 17 times since 1999, Master acknowledged that unions were fortunate to receive 13 percent in salary increases spread over four years and retain fringe benefits "essentially intact."[106]

In June 2008, still faced with a projected unfunded liability of $25 billion, the legislature sought to further trim the cost of the pension program by eliminating Lincoln's Birthday as a state holiday, raising the retirement age from 60 to 62, and barring public employees from using time worked in other states to reach the 25 years of employment needed to qualify for the

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[104] Deborah Howlett and Joe Donohue, "Corzine and Unions Shake Hands on Contract," *Star-Ledger*, February 22, 2007, p. 13.
[105] Dunstan McNichol, "Teachers' Pension fund Shows Greater Shortfall," *Star-Ledger*, March 2, 2007, 22.
[106] Dustan McNichol and Joe Donohue, "Union Pressure Fails, For Once, To Kill Pension Bill: Budget Panels' Votes Mark a Rare Rebuke," *Star-Ledger,* June 22, 2008, p. 21; Joe Donohue, "With Some Objections, the CWA OKs Contract," *Star-Ledger*, April 13, 2007, 17.

generous lifetime health benefits.[107] All these adjustments combined were still only expected to save $150 million by 2022.[108] The modest legislation dropped the more ambitious reforms that had been proposed, including measures that would base retirement benefits on the average of an employee's last five years' pay (rather than their last three years') and that would require part-time employees to work at least 30 hours per week to be eligible for a pension. The watered down legislation eventually passed, but Corzine postponed signing the legislation into law until late September to ensure that thousands of new teachers would be grandfathered under the old rules. If he had signed the legislation in June, it would have affected teachers hired after August 1.[109]

San Diego: "Enron-by-the-Sea"

It is useful to recognize that the issues faced by teachers are reflective of problems endemic to other public pension funds. San Diego is perhaps the poster child of a pension fund run amok, earning the moniker "Enron-by-the-Sea" for its disastrous experience earlier this decade. The system fell from a 100 percent to 67 percent funding ratio in just ten years, due to substantial benefits boosts for city employees, intentional underfunding, and conflicts of interest and corruption.[110] At the time, the San Diego pension fund was managed by the San Diego City Employees' Retirement System Trustees ("the Retirement Board"). composed of 13 members who which hired an outside actuary and investment firm.

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[107] Dustan McNichol and Josh Margolin, "Corzine's Delay is Teachers' Delight: New Instructors, Others Avoid Limit on Benefits," *Star-Ledger,* August 29, 2008, p. 17.
[108] Robert Corrales, "Governor Corzine Signs Pension and Benefits Reform Bill," *Press Release*, September 29, 2008, available from http://www.state.nj.us/governor/news/news/2008/approved/20080929a.html (accessed January 8, 2009).
[109] Dustan McNichol and Josh Margolin, "Corzine's Delay is Teachers' Delight: New Instructors, Others Avoid Limit on Benefits," *Star-Ledger,* August 29, 2008, p. 17.
[110] George Passantino and Adam B. Summers, "The Gathering Pension Storm: How Government Pension Plans are Breaking the Bank and Strategies for Reform," Reason Foundation, Policy Study 335, June 2005, p. 33, available from http://www.reason.org/ps335.pdf (accessed January 16, 2009).

While the market boom of the 1990s allowed San Diego in 1996 to increase employee benefits while reducing the city's contribution to the fund, the downturn in the early 2000s left benefits unfunded. In response to that downturn, however, the City Council refused to reduce benefits or offset the losses with increased payments to the pension fund in order to avoid having to trim city services. Instead, the city steadily increased pension obligations, often against the advice of financial advisors and actuaries. In 1997, a trial program was put in place (which became permanent in 2000) aimed to retain experienced employees. The Deferred Retirement Option Program (DROP) allowed senior city employees to continue to collect their regular salaries and to simultaneously draw retirement pay deposited into special accounts, if they agreed to work an additional five years. In 1997, San Diego added a program that allowed employees to boost their retirement pay by purchasing service credits, allowing them to purchase up to five more years than were actually worked. Objections from the pension system's actuary were ignored.[111]

In 2000, at the height of the dot-com boom, City Council members granted themselves a larger pension, lowering the age when members could collect pensions from 60 to 55 and boosting the formula used to determine their benefits.[112] In 2001, they reduced the retirement age and determined that benefits would henceforth be based on the highest salary earned during an employee's career instead of on the average of their three highest annual salaries.[113] In 2002, the pension fund lost millions, but Larry Grissom, the city's Retirement Administrator, said there

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[111] George Passantino and Adam B. Summers, "The Gathering Pension Storm: How Government Pension Plans are Breaking the Bank and Strategies for Reform," Reason Foundation, Policy Study 335, June 2005, p. 35, available from http://www.reason.org/ps335.pdf (accessed January 16, 2009).
[112] Caitlin Rother, "Council OKs Pension Improvements: Critics Call Action 'Grab' As Terms End," *San Diego Union-Tribune*, Sept. 13, 2000, p. B2.
[113] Luis Monteagudo Jr., "County Braces for Outflow of Employees, Pension Plan Upgrade Takes Effect Next Year," *San Diego Union-Tribune*, August 19, 2001, B1.

was no reason to worry and that, “If we never make another dime in income, we would be able to pay retirement benefits for the next 26 years.”[114]

Seven months later, the *San Diego Union-Tribune* reported the existence of a $721 million shortfall, up from $68 million two years before. Benefit increases approved by the council had driven up the city’s payroll costs by 18.5 percent over two years.[115] “Nobody wants to deal with it,” said Diann Shipione, a retirement board trustee and critic of the city retirement policy. “It’s financially and politically inconvenient.”[116] Shipione had warned the Mayor and the City Council in 2002 of the problem. In 2003, she again wrote to city officials and wrote an op-ed calling attention to the underfunding and the board’s refusal to acknowledge it.

The underfunding eventually led the U.S. Securities and Exchange Commission to rule that the city had defrauded investors in 2002 and 2003 by not disclosing the massive pension deficit. The SEC found that the city had filed “materially misleading” documents and committed securities fraud. An investigation was launched by City Attorney Michael Aguirre, a criminal case was pursued against six members of San Diego’s pension board, and Mayor Michael Richard Murphy resigned. At the end of 2008, these court cases were still pending, with the verdicts likely to affect whether the city can rescind promises made by those under investigation.[117]

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[114] Ray Huard, “Pension Fund Lost Millions Last Year: Unions Say City Retirees Are in No Financial Peril,” *San Diego Union-Tribune,* April 5, 2002, B1.
[115] Philip J. LaVelle, “Financial Realities Come Crashing Down on San Diego Pension Fund,” *San Diego Union-Tribune*, December 21, 2002, A1.
[116] Philip J. LaVelle, “City Pension System Seen Under Siege, Under-Funded, New Report Shows Threat to San Diego For Decades,” *San Diego Union-Tribune,* February 12, 2003, A1.
[117] Greg Moran, “Quicker Start to Pension Trial Urged; Prosecutors Point to Appeals Court Ruling,” *San Diego Union-Tribune,* December 25, 2008, B1.

In the meantime, the city adopted a series of short-term solutions. In 2004, it approved Proposition H, which added seven independent financial professionals to the board of trustees.[118] The city has implemented financial reporting requirements similar to those used in the private sector.[119] In 2006, San Diego adopted Proposition B, which required voters to approve employee pension-benefit increases for the next 15 years, and the new mayor and the city council agreed to redirect $100 million expected from a new stream of tobacco settlement money to bolster the pension fund.[120] Standard & Poor's suspended the city's credit-rating, barring San Diego from pursuing the popular option of issuing pension obligation bonds. The new mayor, Michael Sanders, also developed a payment schedule for the pension plan, which was adopted by the pension board in 2007 to pay off the liability over the next 15 years.[121] However, those promised contributions are now in jeopardy, as the pension deficit climbed to $2.55 billion during the market turmoil of late 2008 and early 2009.[122]

With legal battles still pending, Sanders is pursuing a hybrid pension system for future city employees that incorporates defined-contribution plans.[123] San Diego has pursued an array of reforms following its pension debacle yet, despite this crisis and the political aftermath, the various reform measures have not so far addressed the structural problems in the pension system.

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[118] Matthew T. Hall, "Mayor Taps Seven to Fill City Pension Board Seats: Panel to be Overhauled April 1 under Prop. H," *San Diego Union-Tribune,* February 26, 2005, B1.
[119] George Passantino and Adam B. Summers, "The Gathering Pension Storm: How Government Pension Plans are Breaking the Bank and Strategies for Reform," Reason Foundation, Policy Study 335, June 2005, p. 38-9, available from http://www.reason.org/ps335.pdf (accessed January 16, 2009).
[120] Matthew T. Hall, "Sanders-backed Propositions Passed," *San Diego Union-Tribune,* November 8, 2006, B1; Matthew T. Hall, "Council Backs Sanders' Pension Fix: Using Tobacco Cash for Deficit Purposes," *San Diego Union-Tribune*, February 7, 2006, B1.
[121] Jennifer Vigil, "Payment Span Set on Pension Debt," *San Diego Union-Tribune,* March 17, 2007, B1.
[122] Matthew T. Hall, "Sanders Has Mixed Success on City Goals: Mayor Set to Deliver State of City Address," *San Diego Union-Tribune,* January 12, 2009, B1.
[123] Jennifer Vigil, "Proposal to Be Part of Labor Contract Talks," *San Diego Union-Tribune*, March 4, 2008.

Conclusions

Reforming public pensions is as much a political exercise as a fiscal or technical one. Measures intended to rationalize existing practices must be designed accordingly. For one thing, existing safeguards, such as incorporating independent pension boards and actuarial expertise, too often prove a frail bulwark against irresponsibility. For another, even when public officials have been roused to confront pension problems and have enjoyed some success, as in Oregon, the victories have focused exclusively on budgetary shortfalls. They have not reworked retirement benefits in a manner that makes teaching more competitive with other professions in the contemporary labor market or helps school systems find ways to push out ineffective veterans and retain effective educators after they have qualified for their pensions. In fact, many cost-cutting measures exacerbate the faults in the existing structure by raising the retirement age and the number of years needed to become vested in the plan and increasing the contribution levels of new employees to compensate for the fixed contribution rates of veterans.

Active, organized, and vocal minorities routinely outweigh much larger but inattentive majorities in legislative processes. This is the case with issues ranging from tobacco to textiles. When it comes to public pensions, beneficiaries inevitably enjoy massive advantages in communications, awareness, and interest relative to taxpayers and would-be reformers. Consequently, addressing funding shortfalls or design issues requires far more than good ideas or thorough technical analysis—it requires proponents to change the political climate, foster awareness, forge support for change, alter political incentives, or design politically workable solutions.

As the preceding analysis suggests, public pension politics is inevitably characterized by four simple truths. First, underfunding is a persistent concern because elected officials will

always have cause to emphasize the short-term; this dictates a need to create institutions and rules that ameliorate that temptation or reward attention to the long term. Second, meaningful reform is only possible when the broad public is stirred and its electoral might is arrayed to neutralize the familiar advantages of the employee unions. Third, legislators and governors rarely accept responsibility for poor stewardship or extravagant promises, especially since they are able to blame pension managers and investments for funding shortfalls. The case of New Jersey illustrates the natural inclination for public officials to shift blame onto investment decisions or strategies as a way to setter attention away from their own fiscal decisions. Finally, modifying pension systems requires addressing concerns of veterans who will feel cheated out of what they are promised, organizing and selling advantages to younger educators and to recruiters, and designing systems that are clearly more responsive to public concerns and to the challenges of staffing schools—so as to provide plausible cover to advocates.

Given this landscape, there are at least four tacks that pension reformers might pursue to reshape the political context or alter the balance of power. The first is to embrace a "starve-the-beast" strategy. Since there are temptations for legislators to spend and unions to demand any available dollars, there is a perverse discipline implicit in funding shortfalls that dampens the urge to ratchet up benefits. In other words, the fiscally responsible course of maintaining healthy reserves can be regarded as an invitation to political irresponsibility. *Newark Star-Ledger* reporter Dunstan McNichol observed of New Jersey's staggering shortfall, "But something else may be at work here. It may be that the state has stumbled on the last, best defense against union demands for more. It's harder to tap into undernourished pension funds than healthy ones."[124]

Two provisos deserve notice here. For one thing, it is not clear how sustainable this strategy is over the long haul. For another, even when public officials finally bite the bullet on

[124] John McLaughlin, "Better At Doling Out Benefits Than Funding Them," *Star-Ledger*, June 10, 2004, 21.

the mismatch between promises and resources, as in San Diego or Oregon, there is little evidence that they have any real stomach to tackle pension rules that push out capable veterans at age 55 or keep worn-out teachers in the classroom for years past their "sell-by date." Why? Because while there may be bondholders and voters willing to punish for untenable shortfalls, there are no credit markets, editorial boards, or budget watchdogs similarly attentive to the state's response to labor market dynamics, leaving the preferences of union veterans largely unchallenged. So, the stories of "successful" pension reform are tales of fiscal responsibility that leave largely unaddressed the substantive barriers that pension systems pose to competing for twenty-first century talent.

Second, there is a persistent need to buy off or, in more decorous language, to "grandfather" current teachers and retirees when promoting change. This is due not only to legal limitations but because unions will fight bitterly to protect the benefits of current members while, whatever they say, less passionately protecting those of future members. Just as New Jersey's Governor Corzine was able to boost the retirement age from 55 to 60, but only for new hires, viable reforms must generally placate current teachers as the price for change. This limits the fiscal benefits of new rules and ensures that workforce transformation will be a decades-long process, but promises to change long-term expectations by altering the understood terms under which new entrants join the profession.

Third, reform requires that proponents change the context of the political debate by agitating, mobilizing, and publicly explaining the costs of current arrangements—and framing debates over policy and practice in terms of the actual costs imposed. This is extraordinarily difficult to do, and the reality is that it typically only happens when fiscal crisis throws existing policy choices into stark relief. When those moments emerge, reform-minded legislators and

advocates have the opportunity to harness public opinion. The script only flips for public officials when the vote is framed as irresponsible, craven, and kowtowing to “special interests.” Of course, the effort to manufacture such a moment can fall flat, as happened with Schwarzenegger’s effort in California—which is why it is so important that reformers use fiscal crises as opportunities for promoting measures that will modernize benefits and deliver responsible fiscal stewardship, and not simply settle for makeshift patches that soon allow states and localities to carry on business as usual.

Simple exhortation is unlikely to spur the necessary efforts or to render them effective. Today, the rewards for public officials who step up and take on pension reform are almost nonexistent; as actuary Scott Porter noted of Corzine’s efforts in New Jersey, “Twenty years from now, then you'd start to see some [of the fruits] of this.” Given that the rewards for pension reform are so out of step with political incentives, it is essential to devise institutions and arrangements that don’t depend on self-abnegating public officials to produce sensible reforms or responsible public stewardship. Relevant here is the manner in which H. Ross Perot’s 1992 bid for the U.S. Presidency led to extraordinary attention to the federal budget deficit, influencing policy choices by the Clinton administration and, most significantly, helping lead to the adoption of new budget rules in Congress that produced budget surpluses in the closing years of that decade.

Finally, and perhaps most significantly, there are tools and institutional innovations that can better enable public officials to make the kinds of difficult choices needed to rationalize existing pension plans or ensure responsible fiscal stewardship. Given the temptation for officials to cater to the demands of active, organized, and influential constituencies even when those may run counter to the public interest, the challenge is to find ways to modify those

incentives. One approach, particularly relevant to efforts to promote sound fiscal stewardship, is to craft rules that temper short-term political incentives. This might include increasing the autonomy and independence of auditors to provide greater insulation from pension boards and legislators. Another might be the creation of a federal or multi-state body with the authority to police public pensions and to establish guidelines regarding matters like fund balances and anticipated rates of return. Adopting such measures would be enormously difficult—since they run contrary to the normal incentives for elected officials—but the important thing is that they are measures that would need only to be adopted once. Afterwards, legislators would operate with more barriers against irresponsible behaviors (making it easier to explain "no" votes to interested constituencies) while forcing future officials who wish to make unaffordable promises to visibly and actively challenge these protections. If reformers were to use windows of opportunity to enact such measures, they are not merely solving the current problem but are altering the political calculus going forward.

A similar tack, but one perhaps better suited to pension modernization, is to devise reform packages that insulate the reform-minded from the wrath of veteran public employees while appealing to the sensibilities of civic leaders, journalists, and the broader public. The best-known version of this tack may be the U.S. Congress's Defense Base Realignment and Closure Commission (BRAC), which succeeded in closing more than 350 military installations through a process designed to counter the tendency for legislators to advocate realignment and modernization in theory, but to bitterly resist any effort to shutter a hometown base. The historic problem was that legislators might embrace the notion of new efficiencies and cost savings in theory, but face enormous pressures to protect hometown jobs—even when those might entail wasteful or duplicative spending. The key innovation of the BRAC process was that it

established criteria for base closures on the front end and then required legislators to vote the entire proposed package up or down. The process meant that officials could no longer lobby to protect particular bases, providing substantial insulation against irate constituents, even as it framed a vote to reject closures as a vote for inefficiency and waste.

Analogously, legislators find it enormously difficult to resist the pressure of public employee groups unwilling to contemplate even gradual changes in the familiar benefit structure and fearful that even changes which "grandfather" current employees may sow future splits within union ranks. Framing akin to the BRAC process, in which legislators are voting for a package of provisions to fundamentally modernize and rationalize teacher hiring (perhaps accompanied by heightened pay), could allow reformers to make a "no" vote look like a capitulation to narrow interests while offering a simple up or down vote that legislators could readily explain to the broader electorate as a vote in the public interest. None of this should be taken to suggest that such a path is easy or likely, only that approaches like this offer a more fruitful course than those tried thus far.

The temptation for politicians to see pension funds as just "sitting there" is profound, and Raoul Duke's jaunty solution—to "charge a little more for hot dogs this year"—will rarely suffice. Similarly, while schools are struggling to compete for talent in a new labor market, public officials find the pains of retooling industrial era benefits for a new era unappealing. Indeed, even the four courses noted above offer little support for states or districts seeking to shift from defined-benefit to defined-contribution plans or to revisit the industrial-era pension model. The evidence seems to suggest that the stars are more likely to align for the first kind of change than for the second. Only time will tell, however, whether looming fiscal crises, unaffordable promises, and heightened attention to the costs of public pensions will yield a new

era in which the electoral rewards for fiscal responsibility and workforce modernization rival those of impassioned claimants.

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