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Pension Theft: Class War Goes to the Next Stage

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In the past two days we've seen a federal judge rule that Detroit can go bankrupt, putting its workers' pensions in jeopardy, and we have seen Illinois' legislature vote for substantial cuts in its retirees' pensions. Undoubtedly these two actions are just the tip of the iceberg. We have opened up a new sport for America's elite: pension theft.

The specifics of the situations are very different, but the outcome is the same. Public employees who spent decades working for the government are not going to get the pensions that were part of their pay package. In both cases we have governments claiming poverty, and therefore the workers are just out of luck.

Before getting to the specifics of these cases, it is worth dealing with a couple of points. First, there has been a huge media campaign to trumpet the generosity of public-sector pensions. The Washington Post once ran a major front-page article on public pensions in which its poster child was a former official in a small California city who was getting a pension of more than $500,000 a year.

Of course this sounds horrible, and it is. The official had been the city manager and had assigned himself several other top jobs, all of which came with generous pensions. He also was under indictment.

This is not close to the typical pension in California or anywhere else. In the case of Detroit, the typical pension is a bit more than $18,000 a year. In Illinois it's around $33,000 a year. It's important to note that most Illinois workers do not get Social Security, so this is their whole retirement income.

The other item generally missing from the coverage is that these pensions are part of workers' pay. Controlling for education and experience, public-sector pay is somewhat lower than the pay of private-sector workers. The more generous pension and health care benefits that most public-sector workers enjoy are offsetting lower wages.

The pensions are not gifts bestowed by the government on workers; they are part of workers' pay. When the city of Detroit or state of Illinois cut workers' pensions, they are in effect saying that they are not going to pay workers for the work they did.

Turning to the specifics, there is no doubt that Detroit is in bad financial shape. Part of this can be attributed to mismanagement and corruption. However, by far the biggest factor is the decline in the auto industry, which was the driving force of the city's economy.

This decline has far more to do with national economic policy than any decisions made by the city government. It also didn't help matters that the state of Michigan made it very easy to escape the problems of the city by stepping over the city line into the suburbs, which many of its middle-class residents did.

Detroit workers might be forgiven if they thought they could count on getting the pensions for which they worked. After all, the Michigan Constitution prohibits the state from cutting pensions. And the city of Detroit is a creation of the state of Michigan, which might have led them to believe that the Michigan Constitution also applied to Detroit. However, a federal judge just ruled otherwise. Now Detroit's workers face the prospect of a bankruptcy judge taking large chunks out of their pensions.

The story of Illinois pensions should be at least as infuriating. Unlike Detroit, the economy in Illinois is reasonably healthy. News reports often tout its unfunded liability of $100 billion without pointing out that this is an obligation that needs to be met over the next 30 years. During this period, Illinois' economy will exceed $18 trillion in output, putting the liability at roughly 0.6 percent of the state's future income. That is hardly trivial, but neither is it an unbearable burden.

The disturbing aspect about the Illinois situation is that the underfunding of the pension was a deliberate choice. For years the governor and Legislature approved budgets that did not make the required contribution to the pensions. (The city of Chicago, under Mayor Richard M. Daley, did the same thing.) This was a deliberate shafting of workers in which most of the state's leading political figures acquiesced.

Among those who deserve special vilification in this story are the bond-rating agencies (yes, the folks who rated all those subprime mortgage-backed securities as Aaa). During the years of the stock bubble in the 1990s, they analyzed pension funds using the assumption that the bubble would persist indefinitely. This meant that state and local governments had to make little or no contribution to their pensions.

Unfortunately, it was a habit that stuck. Even after the bubble burst, they continued to contribute little or nothing to their pensions.

So now Illinois, Chicago and several other state and local governments have badly under-funded pensions. It would seem that they would have an obligation to raise the revenue needed to pay workers, after all this money they are owed.

But in 21st-century America, contracts and the rule of law apparently don't mean anything, at least not if the people at the other end are ordinary workers. So, rather than inconvenience all those rich folks at the Chicago Board of Trade or other highly successful businesses with a larger tax bill, the plan is to stiff the firefighters, the schoolteachers, and the people who collected garbage for 30 years.

It may turn out to be the case that the rich and powerful can just rewrite the rules as they go along. But at least the people should know that theft is now in style when it's their property at stake.