Rethinking Public Sector Compensation

What Ever Happened to the Public Interest?

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The Carter Presidential Library and Museum
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A Broken System

The current way we **reward** and **manage** employees is skewed too heavily towards pensions and retiree health care.
Public Employment

Current system places too much emphasis on:
- Job Security
- Time Served

Rather than:
- Performance
- Innovation
- Entrepreneurial Thinking
An Unsustainable System

Creates significant challenges for:

✓ service delivery
✓ efficiency
✓ responsiveness
Employee Compensation

Deferral of employee compensation

Shifts costs to

Future Generations

With interest!

Expensive and ethically troublesome personnel system

Results in
Pensions Gone Wild!

Estimates place the **unfunded liability** for pensions and retiree health care between $1 trillion and $3 trillion!
To put this in perspective if you stack a trillion $1 bills on top of each other, you can reach the moon and back, **four times!**

*According to astrophysicist Neil deGrasse Tyson*
The typical **public pension plan** assumes its investments will earn average annual returns of 8% over the long term\(^1\)

Actual experience since 2000 has been much less – 5.7% over the last 10 years\(^2\)

\(^1\)Center for Retirement Research at Boston College  
\(^2\)National Association of State Retirement Administrators
State and Local Gov’t Accounting Rules

- Governments do not use their investment assumptions to project future asset growth.
- Governments measure what they will owe future retirees, in today’s dollars.
- Private companies have been prohibited from this doing since 1993.
Recent Chapter 9 pension-related bankruptcies

- Vallejo, California – inability to pay pension obligations (2008)
- Prichard, Alabama – inability to pay pensions, especially state mandated increases (2009)
- Central Falls, Rhode Island – inability to pay obligations, especially pensions (2011)
Cities in California Exploring Bankruptcy

- Stockton – pop. 290,000
- Hercules – pop. 26,000
- Lincoln – pop. 43,248
- Milpitas – pop. 66,790
States where pensions are running out of money

<table>
<thead>
<tr>
<th>State</th>
<th>Pension Liability</th>
<th>Percent of Pension Funded</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kentucky</td>
<td>$36 billion</td>
<td>58%</td>
</tr>
<tr>
<td>Illinois</td>
<td>$126 billion</td>
<td>51%</td>
</tr>
<tr>
<td>New Hampshire</td>
<td>$8 billion</td>
<td>58%</td>
</tr>
<tr>
<td>New Jersey</td>
<td>$135 billion</td>
<td>66%</td>
</tr>
<tr>
<td>Oklahoma</td>
<td>$35 billion</td>
<td>57%</td>
</tr>
<tr>
<td>Kansas</td>
<td>$21 billion</td>
<td>64%</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>$61 billion</td>
<td>68%</td>
</tr>
<tr>
<td>Colorado</td>
<td>$55 billion</td>
<td>69%</td>
</tr>
<tr>
<td>Maryland</td>
<td>$53 billion</td>
<td>65%</td>
</tr>
</tbody>
</table>
Who’s to Blame?
The Iron Triangle

Elected Politicians

Gov’t Bureaucracies  Interest Groups
Public Sector Compensation

Elected Politicians (Mayor, City Council/County Commission)

Iron Triangle

Funding/Oversight

Approve Contracts

Legislates/Donates or Invests

Government Bureaucracies (City/County Management)

Interest Groups (Labor Representatives/Employee Groups)
Seniority Rules!

Understanding the civil service system...
Public vs. Private

Who really makes more?
Public vs. Private cont’d

- Public sector workers at all levels (federal, state, and local) earn **higher wages** and **benefits** than their private sector counterparts.
However, when comparisons of similar workers are made between the two with regards to education, age, and occupation, most studies show public workers are either modestly over or underpaid.
The Education Divide

- Most significant factor...
  - *Without* college degrees, employees do do better working for governments
  - Public employees *with* college degrees do worse
Main Controversy

How much to value deferred benefits such as:

- Pensions
- Retiree health care
- Job security
Benefits Costs as a % of Total Compensation
Public vs. Private Sector

Source: Bureau of Labor Statistics
Lifetime Earning

Blue-collar

White-collar
(Public) Workers of the World Unite!
Standard

- Public employees should be compensated in a manner comparable to their private sector counterparts.
- This is consistent with economic and efficiency principles and concepts of fairness and equality.
Prescription for Reform

- Increased transparency
- Avoiding conflicts and self-dealing in awarding compensation
- Pensions and other post-employment benefits (OPEB)
  - Raising retirement age
  - Eliminating current abuses
  - Increased employee contributions
  - Moving employees to 401k-style or hybrid plans (portability)
  - Moratorium on new benefits until plans are fully funded
  - Fully fund pension and OPEB obligations
  - Independent analysis of benefit costs that outline how the plans will be funded now and in the future
  - Voter approvals of OPEB increases
- Retiree health care reform
Prescription for Reform cont’d

- Civil service reform
- At will employment
- Broadbanding
- Move away from time served compensation to rewarding employees for high performance, innovation and entrepreneurial thinking (bonus structure)
Prescription for Reform cont’d

• Collective bargaining compensation
  • Subject collective bargaining to open meeting laws
  • Right to work (prohibit compulsory union membership/dues)
  • Prohibit strikes by public workers
  • Do not subject certain deferred compensation benefits (i.e., pensions and retiree health care) to collective bargaining
  • Community members/citizens appointed to collective bargaining teams
  • In lieu of arbitration and when an impasse occurs, allow elected officials or the community to decide...
Thank you for your time today!

- For more information, visit www.rethinkingpublicpay.com

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