Difficult Reforms and The Art of the Possible: Pension Reform by Stealth?

R. Kent Weaver
Georgetown University and the Brookings Institution
Potential strategies to address sustainability issues in retirement income systems:

• *Retrenchment, eg.*
  – increase age of eligibility
  – reduce benefits

• *refinancing* programs by finding additional revenue sources

• *restructuring* programmatic commitments by
  – eliminating or replacing old programs
  – creating new pension tiers
  – changing the philosophy of existing programs
Difficult pension reforms confront a fundamental trade-off/dilemma:

- **Clarity**— if workers are to adapt successfully to new pension policies, they must be given clear signals early about changing their savings and retirement behavior

- **Obfuscation/Stealth**— sending clear signals about future cutbacks or contribution increases
  
  - Causes politicians to fear electoral or social retribution
  
  - Makes it less likely that a reform will be adopted if opponents mobilize against it
And politicians think in the short term: to the next election

So politicians seek ways to distance themselves from unpopular changes through “stealth”
What are stealthy pension reforms:

A. Stealthy Reform Processes limit inputs into reform process
   - Changes by decree
   - Changes by legislation that are rushed through with no time for public debate
What are stealthy pension reforms:

B. Stealthy Changes in Policy

– Changes in benefits
  • indexation mechanisms (e.g., to shift in lower of wages or prices)
  • Increase in years of contributions required to earn “full” benefits

– Changes in taxes that take effect with a delay

– NDC or quasi-NDC Automatic stabilizing mechanisms (visible when they hit, but unclear effects when they are enacted)
Stealth mechanisms attempt to take advantage of:

- Public’s inattention to policymaking
- Complexity of pension policy
- Voter’s myopia and forgetfulness
Stealth policymaking is

• More feasible when:
  – Pension system is very complex and opaque
  – Key political and social actors collude or at least acquiesce in reform

• Less feasible when:
  – Civil society actors fill in citizens’ gaps in knowledge
  – There are multiple stages and veto points in the policymaking process
Stealth versus inclusion in pension reform processes: Advantages and disadvantages

+ Stealth may avoid policy stalemate
- Stealth may lead to mistrust in:
  • government
  • pension system
- Stealth privileges actors with greater information and access
- Stealth may lead to policy reversal when effects become visible or control of government shifts
- Stealth may reduce desired behavioral response if individuals do not realize that pension system terms have changed
How can the clarity/obfuscation trade-off be resolved?

• Bad way #1: Conceal the effects of the reform or mislead about its effects.
• Bad Way # 2: Delay the effects of the reform so only the youngest voters are affected
• Better but Difficult Way # 1: Be clear about the affects of the reform and sell it to the public as the right thing to do
• Better but Difficult Way # 2: Be clear about the affects of the reform after forming a broad political coalition to develop and sell the reform, so that:
  – Voters do not blame a single party
  – Politicians do not fear that their party will be singled out for blame for imposing losses on voters
  – Reform is likely to survive a change in the governing party(ies)
Possible mechanisms for achieving “Better but Difficult Way # 2”:

• Blame diffusing “policy cartels”
  – Pension working group in Sweden
  – Multi-party pension consensus (Germany)
  – New Zealand Multiparty pensions Accord
  – Canadian finance ministers’ working group on Canada Pension Plan reform

• Pacts between social partners (employers and unions)
The bottom line:

• Each country must develop pension reform mechanisms tailored to their own political system—there is no single template
• Blame-diffusing mechanisms usually break down over time as politicians face strong electoral pressures to criticize “difficult” reforms
• Consensus on difficult pension reforms is unlikely, but acquiescence is more feasible