The Heritage Foundation

ISSUE BRIEF

No. 4216 | MAY 09, 2014

Citizen Approval of Government Pay: Require Public Ratification of Union Contracts

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Many state and local governments face severe financial problems, driven in part by rising compensation costs of state and local government workers. Union political influence enables them to co-opt the collective bargaining process. When they negotiate with politicians elected with their help, unions can control both sides of the bargaining table to the detriment of the taxpayers who foot the bill. States can mitigate this problem by giving voters the same right to vote on labor contracts that they currently have on capital bonds.

Union Contracts Undermining State and Local Governments

Excessive labor costs threaten many state and local government budgets. The City of Detroit filed for bankruptcy in July 2013, largely because of its underfunded government employee pensions.[1] Government worker compensation costs also bankrupted Vallejo, California,[2] which spent three-quarters of its budget on police and firefighters. These bankruptcies represent the tip of the iceberg. Moody's estimates that U.S. states and cities have over $2 trillion in liabilities for underfunded pensions.[3] Such liabilities are forcing governments to cut services significantly and to raise taxes.

This paper, in its entirety, can be found at **http://report.heritage.org/ib4216**

Produced by the Center for Data Analysis

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Excessive government compensation rates—not payroll headcount—drive this problem. The average government employee makes considerably more than a comparable private-sector worker. In many states, government employees pay little to nothing for their health coverage while accruing large pension benefits. For example, the average government employee in California makes 30 percent more than they would in the private sector—with expensive benefits driving that premium.[4] In Ohio, the typical government employee makes 42 percent more compensation than a comparable private-sector worker.[5]

Inflated Compensation Costs

Government unions are a major reason for this disparity. Collective bargaining laws give government unions a monopoly over the government's labor force.[6] If a union does not agree to management's proposed terms, it can disrupt public services, as San Francisco Bay Area transit riders learned recently during the transit strike that paralyzed the region.[7]

Government unions can also help to elect the politicians with whom they negotiate. In 2012, the national headquarters of the American Federation of State, County, and Municipal Employees spent one-third of its budget on politics and lobbying.[8] When unions can elect sympathetic politicians, they effectively control both sides of the bargaining table. The politicians want to please their campaign supporters by giving them a generous contract, while the unions want more money for their members, but no one speaks for the citizens receiving public services or the taxpayers paying for the contract.

This dynamic enables government unions to win very expensive compensation packages. For example, in California, government unions spent millions campaigning for Gray Davis in the 1998 gubernatorial election. After his election Governor Davis signed legislation significantly sweetening government pensions. The changes allowed government employees to retire at age 55 with a pension worth three-fifths of their final salary.[9]

The only way to solve this problem completely is to eliminate collective bargaining in government. Without such reforms, policymakers should pursue alternative policies to limit the cost of union contracts, such as requiring that the contracts negotiated by unions and politicians be approved by the citizens.

Bond Elections

Most state constitutions require local governments to obtain voter approval before issuing bonds.[10] If the city council wants to issue new debt—creating long-term financial obligations for city residents—those citizens must first approve it at an election. Advocates must persuade the public, not just elected officials, that their proposal justifies the costs to residents.

These constitutional provisions arose after many states borrowed heavily in the 1830s to fund capital improvements, such as canals and railroads. Many of these projects went bankrupt, leaving taxpayers covering large losses. Afterward, many states passed constitutional provisions restricting state debt issuance.[11] Subsequently, municipalities began issuing bonds to fund capital projects. Many of them also borrowed irresponsibly, and the Panic of 1873 rendered many local governments insolvent. This produced a wave of state constitutional amendments requiring voter approval for municipal debt.[12]

These constitutional provisions were driven by the impression that special interests often gained control of local politicians, leading municipalities to borrow for projects that did not serve the common

1. Todd Spangler, "Detroit Not Alone Under Mountain of Long-Term Debt," *Detroit Free Press*, July 22, 2013, http://www.freep.com/article/20130721/NEWS06/307210073/detroit-bankruptcy-pension-benefits-unfunded-liability (accessed May 6, 2014).
2. Tim Reid, "Two Years After Bankruptcy, California City Again Mired in Pension Debt," Reuters, October 1, 2013, http://www.reuters.com/article/2013/10/01/usa-municipality-vallejo-idUSL2N0HM05C20131001 (accessed May 6, 2014).
3. Joan Gralla, "U.S. Munis Face $2 Trillion in Unfunded Pension Costs," Reuters, July 2, 2012, http://www.reuters.com/article/2012/07/02/us-usa-municipals-moodys-idUSBRE86119220120702 (accessed May 6, 2014).
4. Jason Richwine and Andrew G. Biggs, "Are California Public Employees Overpaid?" Heritage Foundation *Center for Data Analysis Report* No. 11-01, March 17, 2011, http://www.heritage.org/research/reports/2011/03/are-california-public-employees-overpaid.
5. Andrew G. Biggs and Jason Richwine, "Public vs. Private Sector Compensation in Ohio," American Enterprise Institute, September 14, 2011, http://www.aei.org/papers/economics/fiscal-policy/labor/public-vs-private-sector-compensation-in-ohio/ (accessed May 6, 2014).
6. This is known as "exclusive representation," in which the union negotiates on behalf of all current employees and potential new hires.
7. Contract disputes are resolved in two primary ways in government collective bargaining negotiations: strikes and arbitration. Some states, such as California and Illinois, allow government employees to go on strike. Other states take disputes to an unelected third-party arbitrator, who hands down a contract that is binding on both sides.
8. U.S. Department of Labor, "Form LM-2 Labor Union Annual Report: American Federation of State, County and Municipal Employees," 2012, File No. 000-289, http://kcerds.dol-esa.gov/query/getOrgQryResult.do (accessed May 6, 2014). In 2012, AFSCME spent $70 million on politics and lobbying out of an overall budget of $211 million.
9. Steven Malanga, "The Pension Fund That Ate California," *The City Journal*, Winter 2013, http://www.city-journal.org/2013/23_1_calpers.html (accessed May 6, 2014).
10. Twenty-seven states have such requirements. See the Alabama constitution, art. XII, 222; Alaska constitution, art. IX, 9; Arizona constitution, arts. VII, 13 and IX, 8; Arkansas constitution, amend. 62, 1; California constitution, art. XVI, 18; Colorado constitution, art. XI, 6; Florida constitution, art. VII, 12; Georgia constitution, art. IX, 5; Idaho constitution, art. VIII, 3; Louisiana constitution, art. VI, 7, 14, 33, and 35; Maryland constitution, art. 11-E, 5; Michigan constitution, art. IX, 25; Missouri constitution, art. VI, 26; Nebraska constitution, art. XIII, 2; New Mexico constitution, art. IX, 12; North Carolina constitution, art. V, 4; North Dakota constitution, art. X, 15; Oklahoma constitution, art. X, 26 and 27B (1990); Oregon constitution, art. XI, 11; Pennsylvania constitution, art. IX, 10; South Carolina constitution, art. XVII, 7B; South Dakota constitution, art. XIII, 4; Texas constitution, art. III, 52; Utah constitution, art. XIV, 7; Virginia constitution, art. VII, 10; Washington constitution, art. VIII, 6; and West Virginia constitution, art. X, 8.
11. Clayton P. Gillette, "Direct Democracy and Debt," *Journal of Contemporary Legal Issues*, Vol. 13, No. 2 (2004).
12. Ibid.

good.[13] Requiring voter approval would enable citizens to reject imprudent capital obligations.

States should extend this voter oversight to local governments' labor obligations, which can create even longer-term obligations. Union contracts set wage and salary levels that are difficult to reduce subsequently. Moreover, they often include retirement benefits that taxpayers must pay for decades. For example, if a 25-year-old newly hired government employee whose contract includes pension and health benefits lives to age 85, taxpayers will still pay for that labor contract six decades later. Voters should have a say in accepting such obligations.

Union Contract Ratification Votes

Most unions submit the contracts they negotiate to a ratification vote by their members.[14] The contract takes effect only if a majority of union members agree to it. The union members, not their representatives, have the final say. Even if union negotiators agree to concessions, union members can reject them. For example, the Lake County Education Association in Florida agreed to a contract without across-the-board raises for education personnel. The union's members rejected the proposed contract by a 2 to 1 margin, and the union went back to the bargaining table with the school district.[15]

This system pressures elected officials to accept union demands. Union negotiators frequently argue they need more concessions to persuade their membership to ratify the contract. Often they get them. The final contract in Lake County included general raises.[16]

Voters and taxpayers have no equivalent say over the government labor contracts negotiated on their behalf. They must accept and pay for the contracts that their politicians negotiate—politicians who often focus on winning reelection instead of on spending tax dollars prudently.

Extend Ratification Power to All Citizens

States should correct this imbalance by equalizing the treatment of capital and labor obligations and extending the ratification power to all citizens. Before a government union contract takes effect, local governments should hold a special election for public approval of the contract.[17] Before the election, the government would mail out brochures summarizing the agreement and its costs. The contract would take effect only if a majority of voters approve it.

Citizen ratification would prevent unions from co-opting the bargaining process. Even if a politician elected with union support agreed to an expensive contract, the voters could reject it. Thus, winning over local politicians would no longer enable unions to control the bargaining process. This would make imprudent contracts much rarer.

This reform would also give elected officials more leverage in negotiations. They could argue that, while they might accept the union's demands, the voters would not, so the union needs to come closer to their position. Citizen approval would reduce the costs that collective bargaining imposes on taxpayers. Detroit and Vallejo may well have avoided bankruptcy if their union contracts had required public approval.

Contract Summaries

While conceptually straightforward, implementing citizen ratification and voter arbitration would require working out many practical details. Foremost among these is how to summarize the contracts for voters so that they can cast an informed ballot. States should not allow politicians or unions to write the summaries. Instead, states should establish templates for contract summaries to highlight key facts for voters, including:

13. Stewart E. Sterk and Elizabeth S. Goldman, "Controlling Legislative Shortsightedness: The Effectiveness of Constitutional Debt Limitations," *Wisconsin Law Review* (1991), pp. 1301–1313.

14. Neither federal nor state law requires unions to hold a ratification vote, but most unions do so as a matter of internal policy.

15. Erica Rodriguez, "Lake Teachers Vote Down Contract with No Raise," *Orlando Sentinel*, June 5, 2013, http://articles.orlandosentinel.com/2013-06-05/news/os-school-teacher-lake-contract-vote-20130605_1_lake-teachers-grassel-lake-county-education-association (accessed May 6, 2014).

16. "Lake County Teachers Ratify Contract," *The Daily Commercial*, November 10, 2013, http://www.dailycommercial.com/news/article_877f5a07-574a-576c-9534-2c9ff8c6c9da.html (accessed May 6, 2014).

17. This would apply both to contracts negotiated between a local government and a union and to contracts selected by an arbitrator (in those states that resolve impasses through binding arbitration). Arbitrators should not have the power to impose financial obligations on the public without the voters' consent. To minimize costs, this election would take place after union members vote for ratification.

- The total estimated change in labor costs under the contract.
- The average, minimum, and maximum hourly or annual labor costs under the contract.
- The amount employees would pay toward their health and retirement benefits.
- Retirement ages and benefits, if negotiated.
- Average paid leave granted.
- The total and average per resident increases in property taxes needed to fund the contract. This would be similar to the tax rate statements prepared for many bond elections.
- The long-term (e.g., 20 years) changes to property taxes needed to fund future commitments in the contract, such as retirement benefits.

Importantly, governments should report pension (and thus total compensation) values using the fair market valuation method. Many state and local government pension plans assume unrealistically high rates of return on their assets, which understate the cost of employee compensation.[18] California initially estimated that Governor Davis's pension changes would cost taxpayers little. Those optimistic projections cost California taxpayers heavily when the stock market did not grow as much as the state's actuaries assumed. Voters cannot cast an informed ballot if they do not understand the true cost of the contract.

Impasse Resolution

Voters and unions may disagree over the size of union contracts. States currently resolve disputes between unions and elected officials either with the union going on strike or an arbitrator imposing a contract. Neither method appropriately resolves disputes between unions and the public writ large. The government should not empower unions to strike against the electorate, holding essential services hostage until voters agree to union terms. Nor should unelected and unaccountable arbitrators impose financial obligations on taxpayers without their consent.

Instead, employment terms should continue at those of the previously ratified contract until voters approve a new one. Importantly, the contract would remain in place at its previous level of compensation, meaning that annual raises would not automatically continue.[19] This would enable the government to function on terms that the voters have accepted, while requiring unions to compromise to win any increases in nominal pay. This would resolve disputes without either shutting down services or allowing an unelected official to impose terms on taxpayers.

One concern with defaulting to the previous contract is that it would give unions little incentive to make concessions. They are guaranteed at least what they had before, less the rate of inflation. However, this does nothing to reduce existing incentives to make concessions. In states that allow strikes, the discomfort of striking pressures unions to agree to more taxpayer-friendly terms. In states with binding arbitration, where the arbitrator could still impose concessions, the arbitrator's contract would not take effect until the voters ratified it.

Implementation

States would also need to work out the logistics of conducting the elections. Contract negotiations would seldom overlap with regularly scheduled primary or general elections. If voters reject an initial contract, they would subsequently need to vote on the renegotiated contracts. Holding special in-person elections at polling places would prove costly in most states. States should instead mail absentee ballots to every registered voter in the jurisdiction, along with the summary of the contract. Voters would have a period of time (i.e., 30 days) to return the ballots, after which the government would tabulate the results. Mail-in ballots would increase voter

18. Andrew G. Biggs and Kent A. Smetters, "Understanding the Argument for Market Valuation of Public Pension Liabilities," American Enterprise Institute, May 2013, http://www.aei.org/files/2013/05/29/-understanding-the-argument-for-market-valuation-of-public-pension-liabilities_10491782445.pdf (accessed May 6, 2014).
19. For example, many government union contracts include provisions such as a 4 percent annual pay increase. If the voters rejected new contracts, those previously awarded would remain in place, but future increases would not occur until the voters ratified a new contract.

participation and turnout. They would also make holding re-votes on new contracts straightforward. To reduce taxpayer expenses, states could require unions to split the cost of holding the election. This would also encourage unions to propose contracts likely to win acceptance.

States should also consolidate contracts and elections across bargaining units. Some cities negotiate one master contract covering every unionized city employee. Others negotiate multiple separate contracts, each covering a different group of workers (e.g., clerical, maintenance, trash and collectors). In the latter case, holding separate votes on each contract would leave taxpayers voting every few months, each time on a different contract representing a different group of workers.

States can solve this problem by consolidating contracts so that one master contract covers every employee represented by the same union in a government workplace. Citizens would only need to vote once on the master contract, not separately for each bargaining unit. Alternatively, states could limit citizen ratification to only contracts that increase labor costs by more than the rate of inflation or that create long-term obligations. This would limit the number of votes while giving voters control over long-term spending levels.

States should also stagger the contracts negotiated at different levels of government so they expire at different times. For example, county contracts could expire in the first year, municipal contracts in the second year, and school board contracts in the third year, with each contract lasting for three years. Every year, voters would weigh in on one contract for one level of government.

Conclusion

In many states, government employees earn considerably more than comparable private-sector workers. These union contracts now threaten many state and local governments with bankruptcy. Many local politicians have cared more about gaining union support for their reelection bids than spending tax dollars responsibly.

Similar problems with municipal debt led states to require voter approval of municipal debt. States that choose to collectively bargain with government unions should put government labor contracts on an equal footing with capital obligations by requiring voter approval before government union contracts can take effect. Such a reform would allow voters to exercise responsible oversight over local government finances.

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