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What options do state and local leaders have to cut spending and balance budgets without resorting to layoffs?

NEW TOOLKIT FOR CUTTING EMPLOYEE COSTS WITHOUT LAYOFFS

New York City: As of September 2010, state and local governments had 19.4 million employees earning an average of \$40.10 per hour in compensation—\$26.25 as wages and \$13.85 as benefits. Together, wages and benefits combine to make up 43 percent of state and local spending. Since employee compensation accounts for nearly half of state and local spending, compensation reform is a necessity as governments struggle under financial strain.

“**Tools for Better Budgets: Options for State and Local Governments to Manage Employee Costs,**” a new Manhattan Institute Issue Brief by Josh Barro released today, March 1st, provides a menu of options for compensation reform **in three key areas: retirement benefits, health benefits, and employer-employee relations** as state legislators across the country are looking to rein in spiraling costs. Since layoffs are usually the most disruptive way to reduce costs, this brief provides public sector managers with alternatives in the following areas:

Retirement benefits: The first step to the reform of public-employee pensions is to fix the accounting of pension funds so that it is possible to answer simple questions such as: How large is our unfunded liability, and how much does it cost to award pension benefits? Answers to these questions will help build support for pension reform following the private-sector model of plan termination: new hires are moved to a new, defined-contribution system; existing employees keep what they have earned to date but earn new benefits in the defined-contribution system; and retirees see no change to benefits. To save real money quickly, state and local governments will have to reduce the benefits being earned by employees on the payroll today. Active employees should be allowed to keep benefits that they have already accrued to date but should face cuts to the benefits that they will earn for future years of service to the extent that reducing future benefit accruals is possible while retaining quality talent.

Health benefits: This is the largest non-cash component of employee compensation. The average government worker earns \$4.65 per hour in health benefits, compared to \$2.10 in the private sector. State and local governments should aim to be competitive with the private sector by capping the value of benefits for public workers at a fixed ratio of the average benefit value for private sector workers in the state.

Employer-employee relations. Too often the playing field in bargaining is slanted in favor of public employee unions. The boldest move would be to prohibit collective bargaining entirely in the public sector, already in effect in Virginia and North Carolina. Intermediate options include: Implementing home rule for collective bargaining, limiting the scope of collective bargaining, ending or reforming binding arbitration, repealing laws that give automatic raises to out-of-contract workers, prohibiting public employee strikes, and eliminating the “dues check-off.” Civil service rules should also be reformed, including by eliminating “Last In, First Out” rules that force school districts to terminate good teachers.

As benefit costs continue to rise rapidly—benefits costs per employee rose by 21 percent from 2005 to 2010 while salaries and wages increased by 14 percent—mayors, governors, and state legislators have no choice but to make cuts while maintaining vital services. This report is a timely resource providing a wide array of cost-cutting measures as an alternative to layoffs.

The study can be accessed online at http://www.manhattan-institute.org/html/ib_09.htm. If you would like to schedule an interview with the author, please contact Kasia Zabawa at (646) 839-3342 or by email at kzabawa@manhattan-institute.org.

About the author:

Josh Barro is the Walter B. Wriston Fellow at the Manhattan Institute, focusing on state and local fiscal issues. He is the co-author of the Empire Center for New York State Policy's "[Blueprint for a Better Budget](#)" and author of "[Underfunded Teacher Pension Plans: It's Worse Than You Think](#)." His recent work has included studies on public employee pensions and on property-tax reform. Barro is a frequent television, radio, and print commentator on fiscal and economic issues. He writes on fiscal issues for *RealClearMarkets.com*, is a regular contributor on *National Review Online* and has also written for publications including the *New York Post*, the *New York Daily News*, *National Affairs*, *National Review*, and *City Journal*.

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