

In Detroit's bankruptcy, why are contracts with workers a joke?

By DEAN BAKER

The decision by the City of Detroit to declare bankruptcy came as a shock to many. Detroit, which was once the nation's fifth-biggest city, is by far the largest government in the United States ever to declare bankruptcy. While Detroit has been seeing a falling population and worsening finances for five decades, bankruptcy is still a dramatic step.

One part of this story that is striking is the discussion in the media of how workers' pensions will fare in bankruptcy. Most articles seem to take it for granted that pensions will face large cuts, with some implying that retired workers may be in the same situation as unsecured creditors, getting just a few cents for each dollar owed.

This is striking because Michigan's state constitution seems to say as clearly as possible that pension payments are a contractual obligation of the state. Arti-

cle IX, Section 24 states:

"The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby."

That language would seem to put pensions ahead of bondholders in claims on the city's income and assets. That would mean that bondholders would only get any money if pension claims have been honored in full.

If that seems unfair to bondholders, remember that this provision in the constitution dates back to 1963. Anyone who lent Detroit money in the subsequent five decades presumably could have read the constitution and recognized that they would be behind retired workers in claims on the city's assets in the event of a bankruptcy.

If they lent the city money knowing

that pensions would have priority, then they have nothing to complain about. If bondholders didn't know that pensions would have priority, then they should do more homework before investing their money in the future.

It is striking that so many people in the media are acting as though this clause does not exist. Part of the story is undoubtedly a belief by many reporters that Detroit workers got overly generous pensions. The pensions of Detroit's workers are almost certainly better than private sector pensions, which have been rapidly disappearing. However, research shows that most public sector workers incur a wage penalty relative to private sector workers with the same education and experience. Better pensions and other benefits essentially even the score.

But even if Detroit's workers got a good deal with their pay and benefit package, so what? A contract is still a contract. Workers put in their time in exchange for a specific package of pay and benefits. How can the government arbitrarily change the terms of the deal after the fact?

There are businesses that end up getting very good deals from the government all the time. How often does a state or local government end up selling a parcel of land for a price that turns out to be hugely below its true value? Or they may give tax concessions to lure businesses that prove to be overly generous. It looks like the City of Chicago made a really bad deal in leasing its parking meters to Morgan Stanley for

three quarters of a century. Does Chicago get to just rewrite the terms of the contract?

In these cases involving businesses, somehow a contract is a contract, end of story. The relationship is sacred, and no one suggests changing the terms after the fact. However, in the case of the pensions for city workers, these are just office workers, custodians, or garbage collectors. The media would have us believe that contracts with these sorts of people aren't real contracts. If they prove inconvenient, then they can be changed.

While that may be the view that the media is trying to push, the rest of us should insist that the law and the constitution be respected. Detroit's city workers have as much right to have their contracts respected as the Wall Street bankers making millions and billions off contracts that are often far more questionable.

This is class war at its ugliest. The elites have to learn that they don't get to

change the rules as they go along, if they want their contracts to be respected they will have to respect contracts that protect working people as well.

(Editor's Note: Dean Baker is the co-director of the Center for Economic and Policy Research. He also has a blog, Beat the Press, where he discusses the media's coverage of economic issues.)

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