Interview with Henry Scheff

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Interviewer: Philip Pogue

Pogue: This is Phil Pogue. We're in Chicago, Illinois at the American Federation of State, County and Municipal Employees (AFSCME) Building. It's October 14, 2015. The work were doing for the Abraham Lincoln Presidential Library is on the history of the five Illinois's state pension systems. We're talking today to Hank Scheff, who will be sharing his involvement with pension history in Illinois. Thank you for being a participant in this project. To begin with, Hank, could talk about your own family background, educational experiences and work experiences?

Scheff: Sure, Phil. I was born on the South Side of Chicago in 1950. I'm a baby-boomer, intact nuclear family. My father was a dentist; my mother was a social worker. She's still alive. [I have] three brothers, grew up on the southeast side, first Marionette Manor, then South Shore. [I] went to South Shore High School, graduated in 1967, went on to Grinnell College. I think it's safe to say I was a campus activist, anti-war activist and supporter of progressive causes. Learned about community organization through a urban studies program I participated in the fall of 1970 in Chicago and

Henry Scheff
AFSCME Research and Employee Benefits Director

interned with some community organizations. Met people from the Industrial Areas Foundation.

When I graduated in 1971, I sort of thought I'd go to law school but not now (laughs). Through contacts at the urban studies program, I became an intern with something called the Citizen Action Program. In Chicago, it was an Alinsky-sponsored Industrial Areas Foundation-sponsored, citywide coalition, community organization, that originally worked on pollution.[1] It worked on a number of different issues: mortgage redlining, transportation, education.[2] I worked there for about four years, doing a lot of tactical research and leadership development kinds of things, working with the media. We did, you know, a lot of research and exposés, working with reporters, similar to what the Better Government Association was doing at that time.[3] We also did that.

[I] elected not to go to law school. When that organization [Citizens Action Program] started to unravel, I had, just from my political persuasions and my understanding of unions and talking to my grandfathers who were in unions, said, "Boy, it'd be nice to land a job with the labor movement, if I could." And I did. So, I went to work for the Amalgamated Clothing Workers of America in 1976, as a researcher, leadership trainer with the education department and eventually worked as a straight union organizer for them for a couple of years in 1979 and 1980.

[I] discovered, at the end of the Reagan administration, that you really could not organize in the private sector. Union busting was alive and well. It wasn't invented after Jimmy Carter was well ensconced. Before Carter and during the Carter administration, which is when I was doing this organizing, I had friends at AFSCME who I had met from community organizing days. I'd said, "If you have a place for me (laughs), I'm ready to move into the public sector." So, they hired me.

AFSCME hired me in 1981 as communications director. I edited the union newspaper, which basically meant producing it, writing it, photographing it. I had a contract to lay it out and design it with somebody else. But short of that, I did all of it and then interfaced with the news media. I was the union's spokesperson with the news media. In '86 or '87—I forget exactly when they posted a job for employee benefits and budget analysis kind of work, fiscal policy and health insurance, pensions and so on—I applied for it and was given that job.

[1] Saul David Alinsky was an American community activist and political theorist. His work through the Chicago-based Industrial Areas Foundation, helping poor communities organize to press demands upon landlords, politicians and business leaders won him national recognition and notoriety. (https://en.wikipedia.org/wiki/Saul_Alinsky)
[2] Redlining is the systematic denial of various services to residents of specific, often racially associated, neighborhoods or communities, either explicitly or through the selective raising of prices. (https://en.wikipedia.org/wiki/Redlining)
[3] The Better Government Association (BGA) is a Chicago-based investigative journalism non-profit organization. (https://en.wikipedia.org/wiki/Better_Government_Association)

Then I retrained; I had to go train myself in that. So I did. I was in that position until I retired in 2012. Director of Research and Employee Benefits eventually became the title of that position.

After retiring in October of 2012, I retained a relationship with AFSCME as a consultant. What I do for them now is I run a health plan for them, the staff health plan for the employees of the Illinois division of AFSCME, which is Council 31. Not for the members, for the professional staff of the union, I run their health plan.

Pogue: Following up on some of the things you mentioned, why did you pick Grinnell College?

Scheff: It was the best four-year liberal arts college that I got into. I wanted a small school. I wanted small classes. I wanted to know my professors. I wanted to not have a huge number of students around. I wanted to get to know my fellow students. I thought it would easier in a class of 275 than in a class of 6,000. University of Wisconsin was my big school choice; I had gotten into there.

Pogue: You talked about urban studies; could you explain a little bit about what that was?

Scheff: Well, the Grinnell College and eleven other colleges, small colleges in the Midwest, have had something called the Associated Colleges of the Midwest. They had a consortium. One of the main reasons to have a consortium is they could offer programming jointly that they couldn't offer individually, study abroad, urban teaching, internships, all kinds of stuff. So they had created an urban studies program for people that were interested in urban planning, political science, politics, social work, the whole urban environment. It was a brand-new program; it started actually in the fall on '69. I was in the second group. But I did that.

I was interested in those kinds of things and interested in living on my own in the city with a bunch of other young people and learning about that stuff. Internships was a big part their program that was attractive, a lot of small seminars, a lot of learning done by interacting with organizations in the city and political leaders and so on. It was attractive for me, and it was a lot less painful than sitting in political science classes.

It was the equivalent of three classes; it was twelve credit hours in whatever your major was. I dodged three very boring political classes by doing that. It allowed me to actually have a major, without subjecting myself to the crap that was the political science academic profession of the time, and I would suggest, probably still is.

Pogue: You use the terms progressive and union organizer. What do those terms mean?

Scheff: The conventional terms of what they mean, progressive being on the left, socialist, if you will, social democratic political leanings. Union organizer, meaning identify a group of workers working for an employer that have complaints and grievances, and talk to them, and find out if they're interested in having a union so they can have an impact at their workplace and working with them to form a union and all that entails.

Pogue: The job that you had at Amalgamated Clothiers…?

Scheff: (interrupts) Amalgamated Clothing Workers of America.

Pogue: What kind of responsibilities did that include?

Scheff: Well, I had a couple of different jobs there. I didn't do just one thing. But I did a lot of leadership training, training of shop stewards, training of local union officers, training locals how to get involved in the political process, register their members to vote, turn out in elections, learn about national issues that were important to that union to help them engage. They were very interested in trade, for example. I had to learn a lot about trade—The apparel industry was already undergoing a lot a pressure from foreign competition back then—and then a variety of those responsibilities.

I also did a lot of research around the employers that they were bargaining with or hoping to organize, so that they knew what they were up against, going to public sources, learning about the companies—a lot of them were small companies—looking at the news stories—if they were in the news—for a number of years, and writing briefing papers for the organizing staff before I became one. Here's what you need to know about this company. Here's what the workers may be telling you about things that have happened here and so on.

Pogue: In 1987, you got into employee benefits?

Scheff: Right.

Pogue: Had you had much experience dealing with that, prior to that?

Scheff: Well, I was reporting on them because I wrote the union newspapers. So I was a recipient of them. I was in pension plans. I had health benefits. I have a facility for numbers, so I found those interesting.

I appreciated that things like health benefits and pensions are a critical part of compensation for workers and under-appreciated as their importance to workers. And [I] thought this was something that, if I mastered it, I could have a significant impact in helping the union further the benefit packages, which is a way to enhance people's compensation that some might be more obtainable than wages. Many unions actually pursued that strategy of putting the resources they were able to extract from employers into benefits because of their value to the workers and the fact that they're tax free.

Pogue: Then you worked many years for AFSCME? What is AFSCME?

Scheff: The American Federation of State, County and Municipal Employees, AFLCIO (American Federation of Labor and Congress of Industrial Organizations).

Pogue: When did it actually get formed?

Scheff: About 1935, plus or minus…in Wisconsin.

Pogue: And what are the major objectives of AFSCME?

Scheff: Bargain contracts, collective bargaining agreements is the main business for any union. Bargain and enforce contracts, governing the wages, hours and conditions of employment for the union members.

Pogue: How many members currently belong to AFSCME?

Scheff: I believe around 70,000 in Illinois and nationally, probably about 1.3 or 1.4 million.

Pogue: How do the members contribute to AFSCME? Is it dues?

Scheff: Union members pay dues, and they contribute by their participation. We say over here, union membership is not a spectator sport. If you want to have a strong union, you don't just collect the money from your members and tell them you're an insurance company, and you'll take care of them. You involve them in the activities in the union and activities of bargaining to make sure the bargaining committee has strong support in politics and public engagement, because that's how you have strength.

Pogue: So AFSCME is the national organization. You said it started in Wisconsin. When did it get started in Illinois?

Scheff: Oh, it's got origins going back probably in the '40s and '50s. I'm not really sure. I wasn't alive or engaged at the time. But they had some collective bargaining agreements in place, going back certainly in the '60s and '70s. The first contracts in state government were under [Illinois Governor Dan] Walker, who issued an executive order after he became governor in early '73 that permitted collective bargaining for state employees.

AFSCME organized most of the state employees while Walker was governor and had collective bargaining agreements in place. That was a big growth time period for AFSCME in Illinois. And then there were other contracts too, but they didn't have any legal standing. There was no bargaining law in

Illinois. It was just the executive order; it only applied to workers under the governor.

Then in 1983, the public employee unions were able to get a public employee bargaining law, two actually. Two bargaining laws passed in Springfield. They were signed by Governor [Jim] Thompson in late '83. They went into effect, I think, July 1 of '84? Then there was a huge growth spurt after those bargaining laws, a lot of organizing done.

Pogue: The title of the entity includes county and municipal, so that means that county workers and municipal city, town, village…

Scheff: (interrupts) Right. Park district, housing authority, sanitary district, anything. Any unit of local government is subsumed under the definition of municipality, the way we look at it.

Pogue: Illinois is a pretty diverse state, so you've got many different types of occupations and groups and geographic locations that are part of the…

Scheff: It's a statewide organization, and state government is everywhere. People think of state government as Springfield. But the State historically has a correctional system and a system of institutions for disabled people, the developmentally disabled. It used to have a big system for that and the mentally ill. Many of the agencies have regional operations, the Department of Children and Family Services, that has child abuse investigators and other people to help families who are dysfunctional, having problems. So, there are field offices all over the place.

The unemployment offices are all over. The Department of Public Aid, in the old days that would be the welfare office. There is no such thing as welfare anymore, but they had administered the TANF; Temporary Assistance for Needy Families is what they call welfare now. So, state government is everywhere, not just in Springfield and Chicago.

And, of course, every county has got a government. Every city has got some kind of a government, even the small ones. School districts have employees who are not teachers, as you would know, Phil. So support staff… Historically the teachers' unions were not all that interested in the support staff, so we had many support staff. Now many support staff are in the teacher's union, depends on where they are.

Pogue: Is the makeup of your membership in Illinois half state, half county/municipal, or is county municipal the…

Scheff: (interrupts) I would say it's about two-thirds state, maybe a little less than that, 60 percent state, maybe 8 or 9 percent university support, and then the rest municipal, county/municipal.

Pogue: Has the university been a new area for AFSCME?

Scheff: No, they've had support staff at universities, going back before the bargaining act, mostly blue collar. But now we have a lot white-collar units at universities.

Pogue: How does bargaining impact pensions?

Scheff: That's a complicated question. Maybe we get into it through your other questions. But briefly, just so you have a framework to think about it, Phil, pensions are creatures of state law and existed for decades prior to collective bargaining. And suffice it to say the collective bargaining laws talk about wages, hours and other conditions of employment. The unions would argue that pensions would be in there. The only people that we've ever talked pensions to, as employers of the State of Illinois and the City of Chicago, that I can recall… And they [the State of Illinois and the City of Chicago] took the position that they [pension benefits] were not mandatory subjects of bargaining under the act, so that they didn't have to bargain them. That subject, as far as I know, has never been litigated. So, nobody actually knows.

However, as a practical matter the union **did** negotiate pension benefits with the [Governor James] Edgar administration. Changes were agreed upon, and we never arrived at an answer to the question of whether it was a mandatory subject of bargaining. We said it was, and they said it wasn't. Nonetheless, we bargained on it. We never got to the question of whether putting it in the contract was enough to effectuate it. We agreed that, to be on the safe side, we should enact it and put it into the statute. So, we agreed that we would jointly get the changes that were negotiated enacted in the General Assembly, so they would be part of the law, not just in the contract.

Pogue: You said this was during the Edgar administration. Was that about the time of the '95…?

Scheff: (interrupts) It was after that.

Pogue: After that.

Scheff: After the funding law was put into place. It was in '97.

Pogue: Do you sense that the workforce use pensions as a benefit?

Scheff: Yes.

Pogue: When do you sense that employees view a pension as a more important benefit?

Scheff: Well, the older they get, the more important it is. If you talk to twenty-something citizens, it's what you'd expect, Phil. Twenty-somethings don't care, and some of them say, "How come that money's coming out of my check? I'm never going to see it, blah blah blah. I'm not going to stay here that long."

Then you've got people that are in their forties and fifties. They're still there, and they realize they are going to stay there that long. Certainly the bargaining that took place with the Edgar administration… There was a lot more going on than just bargaining. It was a whole campaign to improve the level of pension benefits for state workers. The impetus of it was a growing perception that…

We helped form it, but you can't make stuff up and have it resonate with people. The state employees really began to see that their pension benefits were not adequate for a secure retirement. They were activated in huge numbers around that campaign to improve their pension, which included mass meetings and all kinds of stuff with the General Assembly because we knew that we had to pass it. We couldn't just bargain it with the governor; we had to pass it.

So, we didn't want it litigated. We didn't know how it would turn out. If we put it in the contract and didn't pass it, we had no idea whether the courts would bless it. We didn't want to take that chance. So, we were running, simultaneously, a lobbying, grassroots advocacy campaign with the members and the leaders of the General Assembly and also running a bargaining campaign with the governor, so that we could get the governor's agreement on the provisions and get a bill that he agreed with and go to the General Assembly with an agreed bill. Under the way things worked back then, agreed bills had a very good chance of passing, particularly if they were paid for.

Pogue: So '95,'97, there was a lot of movement on pension issues in Illinois. Was this somewhat bipartisan?

Scheff: Certainly there were members of the General Assembly who were Republicans and Democrats, both who were sympathetic to the notion that the pension benefit was inadequate, and these bills passed by overwhelming huge majorities. So, yes, there was bipartisan support. That had been true under

Thompson too. There were some changes that were made, not negotiated but lobbied for, that Thompson signed. Some significant benefit improvements were agreed upon with Thompson and enacted.

Pogue: At AFSCME, you've been pretty much involved with employee benefits since '87. Have those responsibilities or their focus changed over that time, or have they been pretty consistent?

Scheff: It was pretty consistent. The big change was in 2001, when I told the business manager, "You're not really paying a whole lot of attention to our benefits (laughs) as full-time professional staff, and I would be happy to relieve you of that responsibility if you're willing to give it to me." He said he was, and then I took it over. So, I became the one who was working with… At that time we worked with an insurance broker, obtaining group insurance.

It was a little laboratory for me to learn from management's side [of] what does it take to actually have a first-class benefit plan, you know, health, dental, vision plan, to obtain it, purchase it, administer it, bargain it with the staff union. Could I learn things doing that, that would be useful in bargaining with the employers? That was a big change and really a great opportunity for me to learn and to do something really important for my coworkers, which was to help them arrive at and maintain a first-class benefit plan in something that would do more than just insure them against catastrophic expenses but actually work with them on their health issues and make the plan cost effective because it was actually a health plan, as opposed to a sickness plan. That's a longer side-track, and we're not going there because we have two hours. So, we're done with that. This is about pensions.

Pogue: There was some major pension legislation for AFSCME members that took place during the '80s, '90s and in the current time. Did AFSCME take a view on these? The first one was pension holidays.

Scheff: We opposed pension holidays, always did, consistently opposed them.

Pogue: Were there any significant changes in IMRF (Illinois Municipal Retirement Fund) rules?

Scheff: Yeah, we tried to—this isn't about the IMRF—we had obtained in the General Assembly, and Thompson signed a provision to compound the 3 percent annual cost of living adjustment. Compounding, meaning the 3 percent would be based on your current pension, not your pension the day you retired. And we sought that for the IMRF. We were never able to obtain it, but we did obtain something called the 13th Check.[4] In lieu of compounding, there was a supplemental benefit that was basically arrived at in many, many discussions with the Illinois Municipal League and other employer groups. They agreed that they would be willing to spend some additional amount of payroll, a defined percentage of payroll, that would go towards this 13th check or supplemental benefit, so we did that.

Pogue: Bond sales to support pensions?

Scheff: Opposed.

Pogue: Why was there opposition?

Scheff: Well, let me put it in context. We believed that—this was consistent throughout my entire tenure at AFSCME—that the problem of fiscal stress in Illinois government was a revenue problem, period; i.e. not a spending problem. It was a revenue problem. So when there was budget pressures, which is, of course, is what led to things like pension holidays and pension obligation bonds, we

[4] Each July, IMRF retirees receive a supplemental benefit payment, commonly known as the "13th check," a benefit provided by the Illinois Pension Code since 1993. The 13th Check exists to reduce the negative impact of inflation on the value of an IMRF pension.(https://www.imrf.org/en/news/2021/06-june/2021-13th-payment)

advocated for more revenue, and that was consistent, from day one always, more revenue, progressive if possible, progressive taxation. We were always for progressive taxation. But a dollar of revenue was a dollar of revenue, and we would welcome it, regardless of how it came to government. Our position was always, raise the money; don't take pension holidays; raise the money; don't do risky pension obligation bonds.

Pogue: COLA [Cost of Living Adjustment] compounded would be one of the bigger benefit enhancements. Was that one of the first big ones?

Scheff: Yeah, that was sometime in the late '80s. I don't remember the exact year, '87,'89, something like that, yeah.

Pogue: And then there was this formulary change that helped.

Scheff: Formula.

Pogue: Formula change.

Scheff: A formulary is a list of prescription drugs maintained by a pharmacy benefit manager. That's what a formulary is. That's one of many definitions of formulary. That's the main one that's used now. Yes.

Pogue: What was that all about?

Scheff: Well, Illinois pension benefits for state employees, particularly, but also for teachers were well below the levels in other states. I had actually done the work on that. Illinois pension benefits for state workers ranked forty-ninth out of the fifty states. There's only one state that had more meager benefits than Illinois. Retirement policy makers generally, over the years, have said a reasonable replacement ratio for somebody to be able to afford retirement was like 80 percent of their pre-retirement income.

The state benefit formula did not throw off anywhere remotely that. Even if you factored in the Social Security—state employees do get Social Security—you weren't there; you weren't even close. So, this was a big issue for state employees, that their pension benefits were bottom of the barrel. That was by any measure too. There were still private sector pensions back then. The trend was to eliminate them. But by any measure, these were very meager benefits.

Pogue: So the formula changed. How significant was it?

Scheff: It moved us from forty-ninth into the mid-twenties. We went from below, way below, median benefit to about a median benefit. That meant that, combined with Social Security, you could get to that 80 percent replacement ratio.

Pogue: Did the Rule of 85 come later, or is that part of this?[5]

Scheff: I'm trying to remember. I think that was part of this. I think it was part of the package, yeah.

Pogue: I always heard state employees say eighty-five; that was a combination of their age and service. And if they got to…

Scheff: (interrupts) So if you were fifty-five, right, and you had thirty years of service, you could retire with the multiplier times thirty years of service, and you wouldn't get a reduction for retiring under age sixty, which was the normal retirement age. That was a benefit that was prevalent in other states and other systems and something that the members wanted badly and was put into the package, as I recall.

Pogue: Then in the early '90s, there was a thing called the Five Plus Five, which added five years of credit for someone who was fifty or five years of experience, whatever.[6] Did AFSCME have a position on that?

Scheff: Well, that was done a couple of times. We took no position on it either time, publicly; we had no public position on either one of those. Privately we thought it was a bad idea, and privately we really tried to stop the second one, after we saw what the first one did. We tried to stop the 2002 one as best we could, without a public campaign, but pleaded with the members of the General Assembly and the leaders not to do it. George Ryan wanted to do it. They saw that they were going to get a Democratic governor. [They] may have passed it after [Governor] Rod [Blagojevich] was already elected.

Pogue: Why did AFSCME think this was a bad idea?

Scheff: Because it would hike the unfunded liabilities of the pension fund. It would decimate the workforce and cause a lot of stress on the members who would be still working in state government. It would reduce the numbers of union members, and there was no way that the numbers that left would be replaced. It would hurt the membership of the union; you'd have fewer members. And it was inherently unfair.

It was granting a windfall benefit to a group of basically undeserving people who were only eligible because they happened to have been around long enough and attained enough of an age to be on the right side of the line, an

[5] The Rule of 85 changed the eligibility for retirement by allowing state employees whose years of service and age equal 85 to retire without a reduction. (https://www2.illinois.gov/sites/SRS/SERS/Publications/Newsletters/00dec.pdf)

[6] Signed into law in January 1993, Five Plus Five lets teachers and administrators age 49 and older retire early by buying up to five years of credit for age and experience toward their pensions. The goal of many teachers who sign up is to qualify for a full pension. (https://www.chicagotribune.com/news/ct-xpm-1994-04-17-9404170336-story.html)

eligibility line that said, if you have X age and X service, you can do this, and if you don't, you can't. Somebody could miss by a week, and they were SOL as they say. Why were they SOL [Sadly Out of Luck], and somebody who made it by two weeks on the other side got to spend five cents for a dollar of enhanced benefits? So inherently unfair.

Pogue: Were other pension enhancements made that we haven't talked about, that you thought would be significant?

Scheff: (long pause) Not that I can think of.

Pogue: Not necessarily related to pensions, but impacting locals paying for pensions is tax caps. Did AFSCME take any position…?

Scheff: (interrupts) We were always against tax caps. We're against and have been [against] anything that restricted the ability of the government to raise money. I'll tell you a little colloquial story. The first week I came here, I was public relations director and, in fact, communications director. It was explained to me this way. I said, "So, what about tax policy?" Basically my supervisor said this, "AFSCME never met a revenue we didn't like."

Pogue: Do pension costs impact salaries and other benefits…?

Scheff: (interrupts) Of course.

Pogue: And how do they do that?

Scheff: Well, they take away resources into benefits that might otherwise be available for salaries. It's well-known that there's been a tradeoff in the country at large, in the public sector, when you look at position to position comparisons, real legitimate comparisons of people doing the same work or the same kind of work or work requiring the same level of educational attainment. Private sector people make more in salary and have less in benefits. And public sector workers have more in benefits and less in salary. So, it's a tradeoff.

Pogue: How did the pension funding progress under the various governors, from Jim Thompson to Pat Quinn?

Scheff: You really want to go back before that. Under Walker, pension funding was improving, under the standard that they were using. They never paid much attention to what actuaries said. But effectively, the pension funding levels were improving under Walker.

The first pension holiday was taken by Thompson, who changed the funding policy from 100 percent of payout to something like 60 percent of payout. In other words, under Walker the state put 100 percent of what the benefit payout was to the retirees, so that's even. But then the workers put in their contributions, so that meant there was a growing fund, right?

Thompson's budget director felt like they could afford to put in less and that the stock market was going to grow at 9 or 10 percent a year, ad infinitum. So when they had their first budget crunch, in that early Reagan recession, they decided they were going to cut the pension funding. AFSCME was very upset about that.

I can remember there were meetings with the administration about that. We said, "We can't support this." They wanted us to…but we can't support it. They said, "Well, we want to do this. And if we don't do it, we'll be laying off our members," We said, "We don't our members laid off. You should raise the money." They didn't want to lay off the members. We didn't want to lay off the members. So, they took this pension holiday, partial pension holiday.

They said it was going to last for one year and that they would go back to 100 percent of payout, starting in whatever it was, fiscal '84, whatever it was. And they continued the underfunding for the balance of the Thompson administration. So, for every year he was governor, subsequent, he never went back to 100 percent of funding. It fluctuated.

It was 44 percent some years, 50, 60. Then that perpetuated into the Edgar administration, until they realized what the funding status going down under that thing, that something had to be done. That's where the pension ramp came, in the Edgar administration, where he had a giant agreed bill between the Democrats and the Republicans. Speaker Madigan was involved in that. I can't remember who the Senate head was. It might have been Emil Jones. I don't remember.

They had a big, agreed bill to start funding the pensions. But they didn't raise taxes, so they couldn't really do it all at once. That's where the fifteen-year ramp came in. Starting in Fiscal '96 through 2011 (more or less), they were on this ramp. The ramp didn't stick, but that's another story. That was the intent of the law was they would ramp up to an actuarial funding standard that would get the pensions 90 percent funded by 2044. So it was a fifty-year funding plan, 2045, I guess.

Pogue: Did the ramp hold until the recession or…?

Scheff: (interrupts) Pretty much, yeah.

Pogue: When did you feel that the public became more alarmed about where pensions were going? Was it a concern? You said a lot of the enhancements were in the '80s and '90s, and now we're in 2015, and we have more of the austerity on pension enhancements. When do you feel the change took place, that more people became aware of pensions as an issue in state politics?

Scheff: Well, I'm not sure I accept the premise of your question, Phil. Who are these people that you're talking about? Are you talking about the average voter? Are you talking about elected officials? I mean, [are you] talking about the Civic

Committee of the Commercial Club of Chicago and the Civic Federation. I don't know who you're talking about.

Pogue: Well, the rank and file retirees are more jumpy about pension changes.

Scheff: Well, retirees are always concerned about whether their pensions are going to be there. The reality is that Illinois pensions have been historically underfunded almost from the get-go. The reason the 1970 Constitution contains a very strong pension protection clause on the benefit side is they were concerned because the state historically had always behaved badly with respect to putting in the actuarially required contribution.

It's nothing new. What changed probably was one too many recessions and one too many pension holidays that didn't go well and people in the General Assembly starting to get concerned, stoked by the business community, that we have to start paying for these things. The public generally, I think, was probably indifferent on it and actually, in the short run, has been the beneficiary of the pension underfunding. To put it crudely, the public has been getting, all these years, in round numbers, a dollar's worth of service for eighty cents.

The state services, City of Chicago, Cook County, all the underfunded pensions. It's not true for the IMRF, but for all the other pensions that were underfunded, the workers accrued a benefit, and the wages were paid, the health insurance was paid for, and the pensions were not, even though they were earned, right? You earn a pension every day you work. You earn that share of your pension, Phil.

So the public was getting a dollar's worth of benefits for eighty cents, so they were benefiting. That obviously can't go on in perpetuity. Now the public is faced with the pension funds are low enough and the politicians have realized they can't keep doing that. In a sense, they've painted themselves into a corner, politically. You can't do pension holidays anymore. It's frowned upon by the power elite and the media and everybody. They won't let you do that. They used to wink and nod and be okay with it. The [*Chicago*] *Tribune* was upset about the pension holidays before the pension bonds. They didn't scream that loud, compared to how they do now. Now you can't do that anymore.

So what is the government's cost now? Well, you could say, "Okay, we got to pay 100 cents on the dollar." Well, no. No because the pension funds are underfunded, right? A dollar payment for a dollar's worth of benefits just keeps it from getting **worse** maybe. It doesn't dig us out of the hole. So, what the state is facing now in the City of Chicago—and there's a big property tax increase in the mayor's budget here to fund the pensions—now they got to pay a buck and a quarter for a dollar's worth of services, to make up for the deal they were getting before.

Now that's a very crude way of looking at it. But from the point of view of pure economics, that is exactly the result of pension holidays and pension bonds. Pension bonds are a complete scam, whether we talk about that or not. I don't know if it's on your question [list]. But that is a complete scam, in some ways worse than a pension holiday.

Pogue: Could you explain that a bit?

Scheff: Okay, so you float bonds, $10 billion in the state's program, and then you give the $10 billion to the pension funds, and you skip fifteen months of pension payments. You just give them the cash. You take no money from general revenue for fifteen months. You don't give that to the pension funds. That's like $2.7 billion worth of contributions that they don't get. And you say, "Well, over the life of the $10 billion, when you invest it over thirty years, they'll more than make up for that $2.7 billion that we don't put in, right?

But the state has $10 billion of bonded debt over here. Well, what is that? What is it? It's pension debt. It's just got a different name, right? So, the idea that they reduced the pension debt by $10 billion by giving the pension funds $10 billion is a complete fiction. It's "truthy" as Stephen Colbert would say; it's "truthy" the pension funds got the $10 billion.[7] It has the air of "truthiness." But the state owes $10 billion to some people who lent them $10 billion, the bond holders.

What did the state get for that? Nothing. They got to give the pension fund $10 billion. You still add it up, it's the same pension debt, except the state skipped $2.7 billion in payments. Now, when that's over, they have to figure where we're going to get three 3 billion or whatever it is to make next year's pension payment, where we have been spending that money on services because we haven't been putting it in the pension funds, a complete and utter disaster.

When the noted pension expert, Alicia Munnell… She's nationally known. She's at Boston… BU or Boston College, I forget.[8] She's a noted economist. When she was in Illinois giving a seminar to…I think it was the IGPA, (Institute of Government and Public Affairs), the University of Illinois operation, [she] was asked, "When do you do pension obligation bonds?" Her answer was, "Never, never." That's the right time to do pension obligation bonds, never. It's a complete scam.

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[7] Stephen Colbert is an American comedian, writer, producer, political commentator, actor, and television host. He is best known for hosting the satirical Comedy Central program "The Colbert Report" from 2005 to 2014 and the CBS talk program "The Late Show with Stephen Colbert" beginning in September 2015. (https://en.wikipedia.org/wiki/Stephen_Colbert)

[8] Alicia Haydock Munnell is an American economist who is the Peter F. Drucker Professor of Management Sciences at Boston College's Carroll School of Management. (https://en.wikipedia.org/wiki/Alicia_Munnell)

Pogue: Then the causes of the pension crisis, from what I've heard you say, are about revenue, and then the….

Scheff: It's an antiquated, inadequate revenue system. Pension underfunding is not the disease; it's the symptom.

Pogue: And then the recessions impacted investment, which was one of the key…

Scheff: (interrupts) But actuaries have that baked into their assumptions. So, if you look at the IMRF, which is one of your questions here: "What's the difference between the IMRF and these other pension funds?" The IMRF is not a state fund. That's the Illinois Municipal Retirement Fund. Today they're like 95 or 97 percent funded. Why is that? Because the governmental units were required to make their actuarially determined contributions, always, never pension holidays, never bonds, never scams.

Was their portfolio affected by recessions? Of course, just like everybody else's. These pension funds, the reason they're cost-effective, compared to individual accounts, is they're in it for the long haul. When you retire, if you have an account like a 401K at the time of your retirement that you might have no control over, it's a huge factor in the security of your retirement. If you retire during a down market, and you buy an annuity, you're going to have a much smaller annuity than if you retire during an up market. Then you've got a bigger nest egg.

Well, public pension basically insures all that. It doesn't matter when you retire. It's in there for the long haul. If they have a bad year, okay. If they're there forever, and you look at the longest span of the returns on the stock market or real estate or whatever you want to do, they're pretty solid. So, it doesn't really matter. If you put the money in, some years you're going to make out and other years you're not. Over the long run, you're going to be fine. And the IMRF is fine.

And public pension plans in many areas of the country are just fine because they understand that this is something that is your first priority or maybe your second, after your bond payments. But pension funds come off the top. There not funded by what's left over. In Illinois, we always funded them based by what was left. If we could afford them, great. If we couldn't, we short funded.

Pogue: Does that mean then—in your opinion now, not talking about AFSCME, but just your opinion—the 1970 Constitution had flaws because it had a requirement, a pretty strong requirement, for pensions but a very weak requirement on the mandatory funding of them.

Scheff: Well, certainly in hindsight, you'd have to make that conclusion. Now, whether that was the fault of the constitution or whether that was the fault of the supreme court that interpreted it to be only a benefit requirement, I guess you could say the language should have been stronger. A strong legal case was made in the IFT

[Illinois Federation of Teachers] case from the early ‘90s, that the intent in the language meant that they needed to put the money in. But the supreme court didn’t see it that way. So, I guess you would say in hindsight it should have been stronger language. Certainly, the supreme court has strongly backed up what it means on the benefits side.

Pogue: What is “Tier 2?”[9]

Scheff: Tier 2 affects people hired on or after January 1 of 2011, I believe, 2011 or 2012, whatever. I don’t know; you’d have to ask SERS (State Employees Retirement System) what the day is. I don’t remember, one of those, January first. It affects new hires because the constitutional down diminishment clause, everybody agrees, does not affect people who are not here yet; i.e., not on the payroll yet. So, everybody agreed you could diminish benefits for people who hadn’t been hired yet. That what’s Tier 2 is. Now there’s four years of those people on the payroll or almost four years, whatever.

Pogue: How significant has Tier 2 been in helping with the pension issue?

Scheff: It hasn’t; it hasn’t helped hardly at all. Everybody knew it wouldn’t because the big problem in funding for state pensions was never the cost of the benefits that were accrued this week, this month, this year. It was the debt. It’s what you already owed. So, what you already owed, you already owed. That’s people on Tier 1. So, Tier 2 provides a miniscule amount of budget relief in that the new hires cost less. But there aren’t that many of them. There hasn’t been that much hiring in state government, and the people who were there on Tier 1 continue to accrue their old benefit at the same level.

Of the state’s pension payment, $4 out of $5 are for the debt. Or as James Carville might say, “It’s the pension debt, comma, stupid.”[10] So no, it didn’t provide any significant relief, and nobody who was a knowledgeable observer at the time thought it would.

Pogue: Did the temporary income tax help with the pension problem?

Scheff: Absolutely. It should have been permanent because, as I said earlier, the problem in Illinois is a revenue problem. The temporary income tax increase was a temporary solution to the revenue problem. Given the limits of the Illinois Constitution, it was not a bad solution.

[9] Tier 2 is a “defined benefit” plan that provides pension benefits based upon final pay and years of service. This plan provides service, disability, and survivor pension benefits as well as retiree health insurance subsidies to eligible sworn members and certain qualified survivors. (https://www.lafpp.com/post/tier-2-pension-plan-information)

[10] Chester James Carville Jr. is an American political consultant and author who has strategized for Democrat candidates for public office in the United States, and in 23 nations abroad. (https://en.wikipedia.org/wiki/James_Carville)

Pogue: Did that lead to improved funding of the pensions? Did it deal with a backlog of bills?

Scheff: It allowed for the first time in a long time the state to make its actuarial pension payment under the ramp, yes. The state was so far behind that it didn't affect the back bills as rapidly as some would have hoped. But yes, the state was whittling down its backlog of bills during the time that the temporary income tax increase was in effect. Yes, it was doing both. It wasn't big enough to quickly eliminate the backlog. But over time, it was working to eliminate the back bills.

Pogue: You talked about the actuaries? Who are these actuaries, and where do they come from?

Scheff: Well, actuaries work in the retirement and insurance industry to figure out, over many, many years, what a promise benefit's going to cost, whether it's a life insurance benefit or a pension benefit or health benefit or whatever, where you're promising things for people in the long run. They look at underlying cost trends. They look at how long people are going to live. They look at how sick people are going to be. They look at how much the investment portfolio is likely to earn.

They have these huge data sets that really track each individual who's covered and project out what the costs are going to be over a huge time span, forty, fifty, sixty years, and tell the employer how much money does it cost to finance that. How much benefits do people earn in a given budget year that has to be put aside now, that under our earnings assumptions will throw off enough money that it can be funded, a net number, net of the [money] employees put in too, net of the employee contributions? What needs to be put in to finance the benefit, fully?

Pogue: Do the state employees then do they have a RFP [Request for Proposal] to hire a set of actuaries for a certain period of time?

Scheff: Yes. They hire a consulting firm, an actuarial firm, to do it. Sometimes they hire consulting firms to help them dope out investment projections and stuff. It might be a different firm. And they [the firm] come up with assumptions that they enact as part of their policy: How long are people going to live? What mortality table are they going to use? What's the earning's assumption for the portfolio? How do they want to allocate their assets? They use the best talent they can get to project that out. Then they try and invest the money with the lowest fees that they can.

Pogue: And IMRF is made up of many different employers,

Scheff: Over 3,000 employers.

Pogue: How do actuarial studies work for each of those?

Scheff: Well, there's elected trustees, and the funds are co-mingled. It's one fund. It's not 3,000 funds. So, the IMRF has one co-mingled fund. And the employers have accounts, nominal accounts, that show what their balance is. But it's not really a fund; it's more of a nominal account.

Pogue: The City of Moline, compared to the City of Aurora, could have different…

Scheff: No, uh-uh, not really. Well, they probably could, but they're not materially…not hugely different. They could be somewhat different if somebody's spiking salaries at the end of their career. If they did an early retirement. IMRF early retirements have to be paid back very quickly. So, there could be some variation, but it's not going to be much. Yeah, the nominal accounts could have some variation. But compared to the police and fire fund, they're going to be very well funded.

Pogue: The police and fire funds, how do they differ?

Scheff: They're not in the IMRF, and there's no actuarial funding requirement. The only public pensions in Illinois where the employer's got to put in the money, come hell or high water, is the IMRF.

Pogue: When Governor Quinn called for pension reform, what was the view of AFSCME?

Scheff: We knew that there needed to be reform of the funding. We knew that the statute was inadequate, given the fact that the supreme court didn't rule correctly back in the '90s and that we were interested in doing something to get the pensions funded and that we were willing to engage in discussions around that and possibly even explore some modification of benefits, if we could get a real funding requirement.

Pogue: How many different groups were parties in this?

Scheff: All of them, all of them, all of the public employee unions that have members in state funds: the two teacher unions, the service employees, the fire fighters, the FOP (Fraternal Order of Police), the teamsters, the laborers, the building trades. The AFL-CIO was there, making sure that public employees broadly were represented.

Pogue: How often did the group meet?

Scheff: A lot in 2012, '11, whenever. Subsequent to Tier 2, 2011, 2012, yeah.

Pogue: Who was spearheading efforts to get all these groups together?

Scheff: The governor, the speaker, the Senate president, the AFL-CIO. The Union Coalition was called, We are One Illinois, we are one, o-n-e, Illinois.

Pogue: Did this group come up with some recommendations?

Scheff: Well, we recommended some very strong funding language that would have given the pension funds the contractual right to get their actual contributions and give them, the pension funds, the legal standing to sue to get them and give the participants of the pension fund the legal standing to sue the pension funds if the pension funds weren't actively engaged in getting their money.

Pogue: Did the group have any concessions that they were willing to make?

Scheff: Yeah, there were. There were some limits on cost-of-living that would have applied to higher income retirees.

Pogue: More like Social Security limits?

Scheff: They were below that. They were below the Social Security earning limits but still pretty generous, maybe $60,000. Above $60,000 for coordinated with Social Security and above $80,000 for non-coordinated or something… It was not a huge concession, but something.

Also having people work longer on a phased-in basis, changing the normal retirement age to higher amounts over time, phased in, kind of like the way Social Security phased in higher normal retirement ages. So, some… We're talking hundreds of millions or billions of dollars of concessions over the long run, in exchange for a hard funding requirement.

Pogue: And did this lead to legislation?

Scheff: No.

Pogue: Why not?

Scheff: Because the unions didn't give enough to suit the elected leaders.

Pogue: There were various pension bills being floated about during that time period. Senator [John J.] Cullerton had one.

Scheff: Senator Cullerton embodied what we'd ultimately agreed to. That never passed. It was never given a vote in the House.

Pogue: It did pass the Senate?

Scheff: It did pass the Senate, yeah.

Pogue: But not called in the House?

Scheff: Not called in the House. That bill died, and then subsequently Madigan and Cullerton came up with their own version that had deeper cuts, that the unions opposed. That's the one that the supreme court threw out.

Pogue: And this was Senate Bill 1?

Scheff: Right.

Pogue: Obviously then, ASFCME was negative toward that…

Scheff: All the unions were negative that I can recall. We Are One Illinois opposed it and told the leaders at the time that it would be litigated if they passed it. Cullerton and his counsel were skeptical that it would pass muster anyway. But he, since he thought his would…He thought the one that we agreed to, the unions agreed to with him, would pass muster. I'm not sure whether it would have. Certainly, the politics would have been better, right? If the supreme court was looking at a bill that was blessed by the public unions and agreed to, notwithstanding the pension protection clause, they might have looked at it differently than one where the unions were all against it, right? It was more draconian in the cut, more obvious to diminish benefits in which the unions got nothing.

Under the one we agreed to with Cullerton, arguably, the unions could have said, "We got something." This is just that whole theory of contract, like you could only change it if the workers got something in the deal, since it included a radically improved funding regime with some teeth in it. The union legal team would have said to the supreme court, "Well, we did get something. Our members didn't get an actual benefit here, but they got a more secure pension. Their funds are going to get paid. This pension fund is their money, and now the state is actually going to put in what they've owed." That's worth something in the tradeoff, right? So that was the theory, but it was never tested because it was not enough for Quinn or Madigan, apparently.

Pogue: You've indicated that AFSCME was supporting, along with all the other groups and We Are One Illinois. Did AFSCME provide testimony at the district and supreme court levels when this case came up, or were they friends of the court or…?

Scheff: (interrupts) We had members who had standing who were plaintiffs, and we paid for their lawyers.

Pogue: What did that mean, to have standing?

Scheff: Well, you're impacted by the law.

Pogue: So you had…

Scheff: (interrupts) You had union members and retirees who are impacted by the law. That's who does the suing. I don't know whether the union had friends, briefs or not. I have no idea. It didn't really matter. It was the union lawyers. The firm was selected and hired by We Are One Illinois and was financed by the unions on a proportional basis to their membership in state government. [They] did a kickass job, unanimous decision—much to the consternation of the *Chicago Tribune*—written by Lloyd Karmeier, who is generally acknowledged to be the corporation's guy on the supreme court, the one the trial lawyers try to defeat. He's the corporations' guy.

Bob Thomas voted for it, the former place kicker for the [Chicago] Bears, a big Republican. The Republicans all lined up, much to the consternation of the Civic Committee, the Commercial Club, and the Civic Federation of Chicago. Why did the Republican members of the supreme court line up in favor of protecting the pensions? Why did the corporations guy write it? Because the law was so f…ing crystal clear, that's all they could do. There was never a case on the other side.

Pogue: Prior to that, which probably spelled a conclusion of the supreme court, was the health care case in which the state employees had reductions for the retirees. That seemed to surprise many folks.

Scheff: Right. That was six to one, with all the Republicans voting that the state couldn't start charging retirees a premium for their retiree health, when historically they didn't.

Pogue: Was that a surprise to you, that the supreme court…

Scheff: (interrupts) It was a surprise to me. It was a surprise to a lot of people, except AFSCME's lawyer. He was the only one that wasn't surprised. He felt like he could do it.

Actually, the dissent is interesting too because that was the warning shot.

Pogue: You're talking about Justice [Anne] Burk's…

(interrupts) Justice Burk's dissent basically said, "I don't think this pension protection clause applies in this case, but it surely applies to the pensions; they can't reduce those." Anybody reading that would have thought that there was a good shot of a unanimous rejection of Senate Bill 1, which is what happened.

Pogue: Before we leave the pension legislation that came out in the last three or four years, was there any other particular legislation that you thought had promise, besides the one Senator Cullerton…?

Scheff: (interrupts) No.

Pogue: Where do we move forward to solve the pension issue?

Scheff: Well, I said earlier; I'll reiterate it. The pension issue is a symptom. The disease is an antiquated, inadequate, regressive, inelastic revenue system. As I said earlier, it's an issue of keen interest to public employee unions generally and ASFCME in particular. We'll be in trouble until we address it. We have a revenue system that dates from the '30s. It's an eighty-five-years antique. We need a revenue system for the twenty-first century.

Pogue: To do that would take a constitutional amendment?

Scheff: Yes, to do it right. There are those that argue that there are ways to get close to it, under the constitutional restrictions for a flat rate income tax, for a number of years. The public employee union supported the League of Women Voters, and other people became part of Dawn Clark Netsch's plan, when she ran for governor, which was to graduate the exemptions. You can have a flat income rate tax and then reverse graduate the exemptions.

You have a large personal exemption. And then phase it out as income grows, so that it's $5,000 or $6,000 or $7,000 a person. Then, once family income hits $50,000, you start slowly reducing it. When family income is at a $120,000, then there is no exemption, or it's only $1,000 or something token. So you get an effective graduated income tax, with a nominal flat rate.

She was for that. She got hammered in the General Assembly for that. And actually, the unions dreamed that up; it wasn't her idea. It was a good idea. It should have been tried. The supreme court might have blessed it.

The other big thing, of course, is to tax the modern economy, not the 1930's economy. That means you have to extend the sales tax base to services, particularly high-end services, where a lot of money is spent accounting: healthcare, legal, consulting.

Pogue: As we close, there are some outstanding issues that are still on the table, tied to pensions. One is the idea of a pension cost shift for downstate teacher pensions. Although AFSCME is not always involved with that, there are probably some…

Scheff: (interrupts) We have very few members in the Teachers' Retirement System, very few—There's some state educators that are in it—very few.

Pogue: So AFSCME has not taken any position on this one.

Scheff: Not to my knowledge. But we appreciate the position of our friends in the teacher's unions on it. How's it going to get paid for? There's nothing intrinsically wrong with the idea, except where are school districts going to come up with the money to do it when they're tax capped and don't have much legal authority to raise their own money?

But if you totally revised the revenue system and gave school district's reasonable tools to do it, I would suspect the unions would be okay with it, as part of a master plan that made economic sense. Certainly, there's something structurally unusual and maybe dysfunctional about having the school districts… some word from their pension costs of their compensation decisions—There's a problem with that—and the pension spiking, which is really invented for the superintendents.

But once the unions found out about it, they figured, "Hey, why not for our members too?" If the benefits determine, in some significant measure by your average salary in your last three or four years, why not load up some of the money in the settlement on people that say, "I'm retiring in four years. Give me a bigger raise." And everybody else agrees to take a lower raise because, hopefully, that provision will be there for them when they retire. You can see how it happens. It's not a good thing. It's a structural flaw in the system that people took advantage of. That's kind of human nature.

But to think you could fix it with a wave of a magic wand. No. If you all of a sudden told the school districts that they had to pay for all this, how do you do it without gutting public education?

Pogue: Re-amortization has also been talked about. Is that something that's viable?

Scheff: Well, of course, you can do it. People do it on their homes all the time. The question is, does it make any sense? It depends on what your priority is. It's like the same way they sell cars. It's like, which costs less? What costs less, to re-amortize the debt or to not re-amortize the debt? Well, what do you mean by costing less?

If your object is to keep your monthly payment and your annual payment as low as possible, if that's your definition of the lowest cost, then you re-amortize the pension debt, and you take much longer to pay it. You pay more over the life span of paying it off because you've extended… It's like, if you finance your house over thirty years, you're going to pay more than if you finance it over fifteen. If you pay for a car over six years, it's going to cost you more than if you pay for it over three years, right?

So, it's like what cost are you concerned about, Phil? If you're concerned about your kids and your grandkids, which people claim they are, right…? Whether they are or not is an open question, but if you really care about your kids and your grandkids and their costs, then the lowest cost is not to re-amortize the pension debt.

You're asking a question about re-amortizing and making it take longer. Your question was not re-amortize it, like pay it off quicker, right?

Pogue: Right.

Scheff: But that's actually the lowest cost ways to pay it off quicker. So, smart families will pay off their house quicker, right, because that finances a better retirement for them, if they're not making a mortgage payment. In fact, it can help them pay for college. It's a smarter way to save for college than putting money away in your kid's name. It's much smarter to have your house paid for when your kids get to college, and then the college-aid formula assumes that a quarter of your income is going to housing. But they don't ask. You don't have to prove anything. That's an assumption. They don't penalize you for paying your house off. All you're paying is property taxes and maintenance and stuff, and you've got disposable income that can help you pay for college.

That's all I have to say about re-amortization. [It] depends on what you're talking about. It's a complicated question, but basically, it's no different than any other debt. What's important to you is low cost now or lost cost over the whole thing?

Pogue: Does AFSCME have a view of what the level of unfunded liability should be? We hear the goal is 100 percent, and then maybe the target is 80 percent, or the target is where we are now; we're at 40 percent. Does AFSCME care, or do they…?

Scheff: We would like, and always have, a revenue system that was modern enough, progressive enough, adequate enough, elastic enough to throw off enough money to get over a reasonable time period to 100 percent.

Then there's the practical politics. So, when the ramp said, "We're going to target 90 [percent]." Do you know how they got to ninety? Edgar's plan was 100, and Madigan's was eighty. That's how they got to ninety. They merged the two bills. If that's the best they can do, we're going to stay off that bill. No, it was better than nothing.

We were supportive of that bill, even though we thought the ramp was a mistake, and it would be better to raise enough money to hit the target now. We testified; we want a plan that's level for the fifty years now because it will be less stressful down… We were skeptical that the state could stick to the ramp. But at the end of the day, that's the bill that's there that's being voted on. It was better than nothing, a lot better than nothing, so we supported it.

Pogue: As we get close to the end, you've talked about having more revenue come in. Do you feel it needs to be designated for pensions and solely for pensions? Or is it…

Scheff: (interrupts) No.

Pogue: So, it could be competing with other programs and program enhancements?

Scheff: It isn't a question of competing. It's a question of… The idea that pensions are this separate thing. Pensions are part of what people earn. It needs to be paid for as people earn it. The unfunded liability is a debt, and it has to be paid. It just a debt. It's no different than any other debt. It's not a special category. Any public entity needs enough revenue to exist and to meet its obligations. And earmarking, you know, is generally a bad idea and unnecessary, if you're running the railroad correctly, and hamstrings you unnecessarily.

Pogue: Are there any other points you'd like to make about pensions that we haven't…?

Scheff: (interrupts) Well, let me see what was on this list; you've been keeping track of it. (long pause) Well, thirteen. As I said, the municipal pensions, except for the IMRF, are in as bad shape is the state or worse, if you look at Chicago Fire and Chicago Police. Bankruptcy is a real possibility for those.

Pogue: Now, on some of those, the unions that actually made concessions and...

Scheff: (interrupts) Well, it's mostly for the Tier 2; they got the funding. The Police and Fire funds got a funding regime in exchange for agreeing to Tier 2. They were more concerned about making them happy than the other public employee unions. The other unions got nothing for Tier 2.

But, no, they didn't affect their Tier 1 benefits at all; they gave up nothing. I think I said enough about early retirement, didn't I? (reads from the list) Closing corporate tax breaks, good idea. The *Tribune*, actually, ironically, just did a great story on the edge credits. Did you read that?

Pogue: Yes.

Scheff: There's a technical term for that.

Pogue: Technical?

Scheff: Pissing money away! It looks like you covered the waterfront pretty well.

Pogue: Well, Hank, I want to thank you for giving us an overview of your involvement with Illinois pension history, going back…

Scheff: (interrupts) Actually, there is more I should talk about because we really glossed over the bargaining and the legislative campaign for the benefit enhancement.

Pogue: Okay, would you like…

Scheff: (interrupts) We talked about the fact that we were able to attain average benefits or medium level benefits. We went from forth-ninth to the middle of the pack. But we didn't talk about what the state got from that deal, okay? There was big sacrifices that the Edgar administration asked state employees to make, through their union, that we ultimately agreed to. So, the benefit enhancement was paid for in the following three ways, and they all add up to a significant amount of actual dollar savings to the state.

Number one: the Edgar administration had budgeted and was prepared to give us a 3 percent raise that year. We did not take it. That raise was to be allocated in perpetuity to the pension fund. So, we forwent a 3 percent raise, which is worth more than 3 percent, by the way, because there's rollup costs. You don't get a raise; there are no pension costs, no social security costs, no life insurance costs, other benefits that are tied to wages. So, it was actually worth close to 4 percent.

We changed the retiree health insurance entitlement prior to the benefit, pension benefit enhancement, that went into effect January 1, 1998. If you retired from state government or from public universities, with eight or more years of state credit or university credit, you got free retiree health insurance for yourself and subsidized for your dependents.

The pension enhancement applied to people who retired on or after January 1, 1998. [It] didn't raise the pension benefits for people already retired. Those people had their pensions, right? So, for those people who were eligible to retire under the higher formula, they had to work **twenty** years in order to get the full subsidy. Basically, it was done on a phase-in basis; people earned 5 percent of the value of the single retiree health insurance program for the employee only for each year of service. They still needed eight to qualify, or they get nothing. But at eight years, it would be eight times five; they would get 40 percent of the value, and they would pay sixty. Then each additional year they worked beyond eight, their payment would go down by 5 percent of the cost of the insurance. So, a ten-year person would pay half, fifteen-year person would pay 25 percent of the premium; an eighteen-year person would pay 10 percent of the premium; a nineteen-year person would pay 5 percent of the premium, twenty-year or more person would get it free. So that was a lot of people paying premiums that didn't pay any more.

And the union gave back a benefit that was negotiated originally with Thompson, as an incentive for people to not abuse sick leave. So, state employees, starting in 1984, for sick leave they accrued that they didn't use upon retirement, they got fifty cents on the dollar, in cash. It didn't apply to any accrued sick leave they had before 1984. Edgar wanted an end to that, so we agreed to an end to that. So sick leave that accrued on or after January 1, 1998 had no cash value.

We gave up the cashable sick leave, the pay raise, and free health insurance after eight years of service, as part of the package to get the higher pension formula in the Rule of 85. And Edgar fully supported that, testified that our concessions paid for the pension benefit, substantially—like 90 percent of it was covered—substantially paid for the benefit.

It was lovey-dovey and agreed to, and that is why the thing passed, virtually unanimously, because members of the General Assembly **believed** that they were voting on a responsible, compromised, negotiated settlement. And they were, a story that is not told in the *Chicago Tribune*, but a true story. That's how it happened.

The members of the General Assembly wanted to vote for something because, during that campaign, there were massive accountability sessions all up and down the state, with hundreds of state employees, in a lot of times, high school auditoriums, with their members of the General Assembly up on a panel, listening to the testimony of how meager the retirement was and something had to be done about it. And "If we come to an agreement with the governor, will you support it?" Of course, they would say, "Well, it depends on what it is, but we'd like to help you if we could." It has to be responsible and blah, blah, blah. So, that's what we came up with, a responsible benefit increase.

They contrast that with an irresponsible benefit increase, like the early retirement, which is an example of the dysfunction of the pension system and the fiscal structure. The early retirement in 2002, the one sponsored by George Ryan, when they passed it, they promised in the legislation that it would be paid for **fully** in ten years, and they were going to pay for it with the payroll savings because thousands of people would leave, and they would only replace some fraction of them, generating lots of payroll savings, right? So, it was going to be paid for in ten years.

Now, they didn't know how many people were going to take it. So they didn't know what it was going to cost. So they didn't have a number for the first year. So they had to put something in there. So they put in $70 million. That was the actual number, Phil. And they said, "Okay, we'll put in $70 million of payroll savings in year one, and then the actuaries will tell us how much the thing cost. Then we'll put in level dollars for the other nine years, whatever it is, the level amount of money in dollars, no interest rate assumption. We'll just pay for the whole thing, and there will be plenty payroll savings to do it.

Of course, we opposed the whole thing. So, we opposed and said, "We don't care what you do. This is a bad idea; don't do it." But they wanted to act fiscally responsible. "This is the responsible thing to do," they wanted to say. So that's what they did. They put in the $70 million.

And then the actuaries come back. The thing cost like, I don't know, like $2.9 billion or 3.something. I can't even remember how many billions it cost. It cost a lot a money. The actuaries said, "It's going to cost like $290 million in fiscal '04—I think that was the second year of it, yeah. It was going to cost, like almost $300 million in fiscal '04. Well, they didn't have…notwithstanding that 11,000 people left, like a quarter of the state workforce left, just about or a fifth, whatever. They didn't have the $300 million in year two.

So, what do they do, Phil? They said, "We'll in seventy again, and then we'll re-amortize it for the eight years." Okay? Then they get to '05, and the bill is $330 million, or whatever it is, to amortize it. Of course, it was accruing interest, right? The payments, the $10 billion, is static, whatever the interest rate assumption is. It was like $350 million or something for the other eight years. Guess what? They still hadn't hired… They still hadn't filled the jobs, right? Still no money; they didn't have enough money to do it and finance government, your school district, wherever you were working, Phil. They didn't have enough money to do all that.

So, you know what they did? They put it on the ramp. They just said, "This unfunded liability, we'll just co-mingle it with everything else, and it will be paid off by 2045." That's what they did. Again, the unions were opposed to it, weren't involved in it. There was demonstrably over $1 billion. By the time they did this, there was $1 billion of annual payroll savings. That's what those 11,000 people would have been earning, with their benefits and everything, had they still been on the payroll in 2005. The program generated more than enough savings to fund the added costs.

So why wasn't it funded? Why didn't they put the money in? Inadequate revenue system, they didn't have the money. That's kind of your object lesson of where the actual problem was. Even though they planned to do it. They said they were going to do it. They swore on in on the oath that this was their law. And they generated the savings to do it. They couldn't do it. They just couldn't do it.

Pogue: Is this part of the problem then of pension legislation, that's there not clear actuarial information before people vote…?

Scheff: (interrupts) **No**. They had the information; they knew. I just told you the story. They had the information. They knew what it cost. They had decided they were going to pay it in ten years. And the actuary said [speaking rapidly], "Here's what it cost. We've identified these 11,000 people. We know how long they're going to live, based on our assumptions. We know what their benefits are going to cost. They've all been calculated. We know how much the COLA costs. We know everything. We might be off marginally. But based on all of our assumptions, this is what they're going to cost." And they had the payroll savings.

Pogue: You mentioned…

Scheff: (interrupts) So, it's not a question of not having the information. It's a question of not having the political will to raise the money.

Pogue: I guess what I was talking about is that they didn't know how many were going to take it, so they didn't know how many…

Scheff: (interrupts) **No**, because the more that took it, the more payroll savings. It's a proportional thing. You can't say, because more people took it, you couldn't afford it. More people took it; there was more savings. In fact, they had pledged that they were going back-fill 50 percent of the jobs. It's now twenty, almost

2016, those 11,000 people are still gone. They haven't replaced any of them. In fact, they've continued to shrink government.

Pogue: Hank, I want to thank you for sharing all of this information with us, and I appreciate you being a part of our project.

Scheff: Thank you, Phil.

(end of transcript)