

The Great Pension Crisis: From Grey Capitalism to Responsible Accumulation

Robin Blackburn

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Pension finance has in the past posed a strategic choice for countries whatever their level of development. If handled well, it has allowed states to construct a regime of accumulation which both promotes development and embodies social guarantees for the population. Postwar Japan, Singapore, France and Germany are all examples of states that used pension funding to mobilize popular savings and boost national wealth. In each of these cases savings were husbanded by non-commercial social or para-state institutions, which helped to define distinctive welfare regimes.

It will be the argument of this paper that in the 21st century the need to boost pension provision, prompted by the new demographics of the aging society, could open the path to a far-reaching socialization of the accumulation process. This would require a full-scale assault on the prevailing - but failing - structures of Anglo-Saxon capitalism. In my view the large fund-managers and banks have helped to create the crisis of corporate governance and bear much responsibility for both the bubble and the slashing of pension prospects in its aftermath. The transformation of the current Anglo-Saxon pension fund regime requires a new model of de-commodified governance, a new source of public finance and a readiness to draw on the experience of 'socially responsible investment' (SRI), and kindred movements. The alternative I will explore would also require significant modification to the European or Far Eastern models of state-sponsored pension provision, aiming largely to retain their fairly generous level of provision but to find new sources of finance and to establish more democratic forms of accountability in the management of social funds.

Let us first briefly review existing alternatives and establish whether they are working well or badly. The neo-liberal consensus has, since at least the publication of the World Bank's report *Averting the Old Age Crisis* (1994), insisted on the scale of the pension crisis and on the need for far-reaching measures to tackle it. The report faults comprehensive state provision financed by payroll taxes for increasing economic rigidity, slowing growth, raising labor costs and boosting unemployment. Private pension delivery is faulted for its unevenness – even in the US and Britain, wealthy countries with a mature financial services industry and many fiscal incentives to pension savings, only a half of the citizens reaching retirement had any secondary provision. The report argued that every employee should be obliged to enroll in a pension plan run by the financial services industry. The state was to offer a safety-net but was to vacate the field of secondary and pre-funded pension provision. In this vision citizens were to be legally obliged to pay their pension contributions to a private financial institution which would then invest them in the stock market. Recent years have brought home the double jeopardy of such a proceeding and have made many appreciate the strengths of the traditional public provision, which itself emerged in consequence of market failure during the interwar years.

The traditional postwar pattern was for the state to guarantee a basic state pension to all citizens, financing this by means of a special tax or social insurance contribution. This is true

even in the United States, with its strong financial sector and famous individualism. During the Great Depression private savings were wiped out and many commercial pension schemes collapsed. This created a situation which allowed President Roosevelt to introduce a public retirement system with his Social Security Act of 1935, though it only became truly universal in the early postwar period. US Social Security has withstood several attempts at privatization and acquired the reputation of being ‘the third rail of American politics’. And while US social and political arrangements are generally hostile to redistribution, Social Security does redistribute from richer regions and citizens to poorer ones.¹

However the generous hopes of the founders of Social Security have been under attack for many years now. In the United States the basic state pension only offers a bare subsistence and is paid for by a social insurance contribution which works like a payroll tax. Citizens have been encouraged to join private pension schemes by generous tax concessions and such schemes supply a secondary source of retirement income for about half of the working population. Britain has a similar mixed system in which private provision is subsidized by public tax relief to the great benefit of the private financial services industry. Successive British governments from Thatcher to Blair have followed the path of ‘implicit privatization’, namely holding down the value of the basic state pension as a way of encouraging people to take out private provision. In the US there is a vociferous lobby pressing for commercially-supplied ‘individual accounts’ to be carved from the existing Social Security regime, a proceeding which would weaken its finances and, in all likelihood, lead to eventual wholesale privatization.²

In the large countries of continental Europe the state undertakes some pension provision itself but also mandates independent, non-commercial entities, in France representing employers and trade unions, to manage pension provision. In Germany and Italy public provision is supplemented by a requirement that corporations build up reserves which are held to finance pensions for their employees. These reserves have played a crucial role in buttressing corporate finance. In postwar Japan the state used citizens’ pension contributions to finance extensive public infrastructure projects; roads, harbours, bridges and so forth. In Singapore the Central Provident Fund has played a similar role. One way or another pension provision is intimately related to the regime of accumulation, such that savings for retirement have often furnished a crucial source of investment making possible general economic advance.³

¹ The redistributive effects of Social Security are established by James K. Galbraith et al, ‘The US Model’, *New Left Review*, 237, 1999. The reasons for the hardness of the program during the Presidencies of Reagan, Clinton and, so far, George W. Bush is the topic of chapter 6 of my book, *Banking on Death or Investing in Life*, London and New York 2002.

² For examples of the US controversy see Eric R. Kingson and James H. Shulz, eds., *Social Security in the 21st Century*, New York, 1997. For a critique of the program see Sylvester Scheiber and John Shoven, *The Real Deal: the History and Future of Social Security*, New Haven CT, 1999, and for a defense see Dean Baker and Mark Weisbrot, *Social Security*, Washington 2000.

³ A useful comparative study is Francois Charpentier, *Retraites and Fonds de Pension*, Paris 1998. For Japan and Singapore see, respectively, Bernard Ecclestone, *State and Society in Postwar Japan*, Oxford 1989, p, 97 and Michael Hill and Lian Kwen, *The Politics of Nation-Building in Singapore*, London 1995.

Costs of the Third Age

Today there are few countries where future pension provision does not furnish a challenge. In every advanced country, even those with mean state retirement provision, pensions take a huge bite out of the public finances. This is because we are here dealing with the livelihood of a tenth or more of the population - just keeping them alive, let alone fit and comfortable, is a major undertaking. With a decline in the birth rate and steady increases in longevity, the aging society further intensifies the pension finance problem. Those who have tried to make proper provision, but have been short-changed by providers or sponsors, react with anger as well as disappointment. Then there is the question of rising medical expense with those over 60 generating medical costs, each year, three or four times the bill for those under 60. Some of this cost inflation in the US is caused by expensive and wasteful forms of commercial health care. But the experience of many countries demonstrates that if the health of the over-60s is to go on improving then medical expenditure will also have to rise.

Many will want to work past what was previously thought to be the normal retirement age. Those over 55 or 65 may retire from their previous occupation but they feel they have much to get out of life and to contribute to society. As Peter Laslett puts it, retirement is being replaced by the Third Age. Instead of retiring the over-60s go back to college or learn a new occupation, or begin to play a more active role in the community. The social contribution of the Third Age is encouraged by pension provision, rather than rendering it unnecessary. It allows the second or third occupation to be undertaken for its own sake. Once the older person has some security of income then they can take up retirement work, or contribute to family or civil society.⁴ If they are thrown into abject poverty this contribution becomes much less likely. In the aging society retirement provision may well come to absorb 15 per cent or more of GNP, and if medical expenses are included the cost would be greater. In developing societies families may absorb some of the costs of the aging society but their ability to do so is increasingly limited by geographical mobility, rising medical costs and the difficulties which working families have in meeting essential outgoings. There is good reason to believe that the provision of a basic pension state becomes unavoidable in a complex modern society, partly because of popular pressure, partly because it facilitates labor mobility, and partly because some of the stronger capitalists preferred to see all employers bearing the same welfare burdens.⁵ In his classic study Gosta Esping-Andersen argued that public-mandated pension provision should be seen as a way of, in effect, 'de-commodifying' labour power, since the state was taking from private citizens much of the burden of providing for themselves in old age.⁶

⁴ For a visionary outline of the 'Third Age' as a life stage with huge potential see Peter Laslett, *The New Map of Life*, 2nd ed., Basingstoke, UK, 1996.

⁵ John Myles, *Old Age in the Welfare State: the Political Economy of Public Pensions*, Lawrence (KA) 1989; Peter Swenson, *Capitalists Against Markets*, Cambridge 2002..

⁶ Gosta Esping-Andersen, *The Three Worlds of Welfare Capitalism*, Oxford 1990.

The pay-as-you-go (PAYGO) method of funding pensions through payroll taxes has proved to be administratively efficient and cost-effective. There is no better way of supplying a basic pension. This method, with its ability to count on future contributions to meet the entitlement built up by current contributions, can only be entrusted to the state.⁷ But in a society where age cohorts are of greatly varying size, and where longevity is increasing steadily, it is problematic to expect PAYGO to supply secondary as well as basic pensions to all. The revenue in current PAYGO systems stems from payroll taxes whose yield will reflect the numbers in employment and their level of income. The size and productivity of the workforce thus constrain income to the scheme. The numbers in employment will be reduced by any contraction in cohort sizes, or growth in the time necessary to educate and train the workforce. And in an aging society even a gently growing labor force can be outpaced by a more rapidly growing elderly population. What counts in a retirement system is the ratio between the number of active employees and the numbers qualifying for a pension. Global demographic projections show an increasing proportion of the adult population living past retirement age. The aging of the population is a feature of both developed and developing countries. The UN mid-range projection tells us that the over-60s, who comprised 30.7 persons per 100 adults in 1998 in the developed countries, will comprise 62.3 persons per 100 adults in those countries in 2050. In Latin America the proportion rises from 13 over-60s per 100 adults in 1998 to 39 over-60s per 100 adults in 2050. In Asia, including China and India, the anticipated proportion of those over 60 rises from 14.1 per 100 adults in 1998 to 40.8 in 2050.⁸ In each society rising numbers and rising expectations will give critical mass to the Third Age.

The overall dependency ratio is likely to be improved by a declining proportion of children but the need for longer periods of education and training will offset this to a considerable extent. The fall in the number of workers to dependents can be alleviated by rising productivity and by immigration but there are inherent limits here since workers will hope to garner some benefit from rising output and migrant populations also experience increasing longevity, with younger immigrants wishing either to send money home or bring over their elderly relatives.⁹

The Need to Supplement PAYGO

If retirement income derives only from payroll taxes and social insurance contributions from today's workers then the aging society will either lead to a steeply rising tax rate or to a sharp fall in the living standards of older people, or to some combination of the two.¹⁰ In

⁷ The classic account is Paul Samuelson, 'An Exact Consumption-Loan Model of Interest With or Without the Social Contrivance of Money', *Journal of Political Economy*, December 1958.

⁸ *World Population Prospects: the 1998 Revision*, Volume III, *Analytic Report*, United Nations 2000, p. 168.

⁹ Neil Gilbert claims that so far as Europe is concerned: 'To keep a constant relationship between the number of people aged 15 to 64 and people of 65 years of age and over requires an influx of over 1.3 billion people over the next 50 years.' Neil Gilbert, *The Transformation of the Welfare State: The Silent Surrender of Public Responsibility*, Oxford 2002, p. 34. This book furnishes a good summary of the recent erosion of public provision, though the author's own standpoint is far too accommodating, or sympathetic, to this process.

¹⁰ The classic exploration of these alternatives is Richard A. Musgrave, 'A re-appraisal of Financing Social Security', in *Public Finance in a Democratic Society*, Volume II, *Fiscal Doctrine, Growth and*

practice older people do have other sources of income - notably from earnings or from the ownership of assets. An increase in the earnings ability of older people requires two things (1) efficient and comprehensive public health services (2) employers who are willing to employ older persons. The asset income accruing to older persons can be raised if they own property or some small enterprise (farm or small business), and this can be enhanced if they sell or mortgage their stake. However the latter procedures will also be a source of risk and debt. Alternatively asset income can derive from a pension fund which owns income-yielding assets, notably company shares or government bonds. In practice the asset income derived from pension funds is likely to have a crucial role to play in most parts of the world if the aging society is not to drive up payroll taxes to counter-productive levels, and/or to cut the living standards of the retired.

As European finance ministries have long ago discovered, high payroll taxes can create unemployment and the end-result is that the tax yield does not rise as fast as anticipated. In Germany, France and Italy payroll taxes – that is taxes levied on each employed worker – amount to 40 per cent of wages, with the proportion going to pensions amounting to 19 per cent of wages. Social taxes are here falling on working people and count as a tax on jobs. Official unemployment rates have run at ten per cent or more over the last decade while the proportion of those aged 15-59 who are in employment reaches only around 60 per cent, with unemployment heavily concentrated among older and younger workers, and women. Employment is about 15 points higher in the US.¹¹ It is not the level of benefits that is at fault but the insistence on financing those benefits wholly on a PAYGO basis, and from payroll taxes alone. Surely there is a better way to finance pensions than this?

One alternative, favored by a number of writers, would be to move away from payroll taxes, which are regressive, and instead allow general taxation to take the strain of rising pension provision.¹² This would certainly be more progressive but would risk overloading the public exchequer or putting pensions in competition with other desirable social programs. General tax revenues will anyway have to underwrite many of the extra expenses of an aging society. Given the multitude of legitimate and necessary calls on the public purse - for more spending on health and education - it would be good if it does not have to furnish all retirement income as well. Much recent writing on the welfare state stresses the importance of child-friendly policies as a way of counter-balancing the aging trend. For example, better provision of child care or measures to alleviate child poverty, might persuade women to have more children.¹³ If it is at all possible to finance secondary pensions in ways leave more resources for other social budgets then this would be desirable.

Institutions, Brighton 1986, pp. 103-122.

¹¹ Directorate General of Economic and Financial Affairs, European Commission, Economic Paper 170, May 2002.

¹² Some of the best recent surveys of pension finance plump for this approach. See, in particular, John Myles, 'A New Social Contract for the Elderly?', in Gosta Esping-Andersen et al, *Why We Need a New Welfare State*, Oxford 2002, pp. p. 130-72; and Nicholas Barr, *The Welfare State as Piggy Bank*, Oxford 2001.

¹³ See, e.g., Esping Andersen's contributions to *Why We Need a New Welfare State*, or Theda Skocpol, *The Missing Middle*, New York 2000.

Some object that future incomes will have to be met from future production so that the precise financing method adopted does not matter. While there is truth in the initial observation the conclusion does not follow. A prior claim over the production of the future is set up by the prevailing pattern of property relations, above all by the ownership of stocks and bonds. The latter instruments ensure that future income will be divided, in the first place, between that accruing to owners of capital and that going to those who sell their labor power. The fiscal policy of the state may modify the distribution of income, but in practice those who own productive assets will still command significant streams of income. While pension provision will always need to make demands on the fiscal capacity of the state it might well be advantageous for it also to derive supplementary income from capital assets. At present labor incomes attract quite heavy taxation and levies on wealth are becoming steadily lighter. It would therefore be good to pre-fund pension provision, with the accent on capital levies.

The advocates of privatisation are wont to scare the public by totting up the anticipated deficit of public retirement programs and occupational schemes. Thus Niall Ferguson and Laurence Kotlikoff warn of a supposed deficit of \$44 trillion that will be precipitated as 77 million baby-boomers embark on retirement, beginning in 2008 and stretching down to mid-century.¹⁴ While it makes sense to anticipate some future costs these alarmist exercises are very one-sided, taking no account of the diversity of ways of covering future retirement needs and neglecting to examine the severe problems of their own preferred alternative, commercial pre-funding. Moreover these authors are focusing only on the expense of current US public programs - Social Security and Medicaid - rather than the full retirement costs of the cohorts concerned. Since these programs are not that generous, and the US is a very rich country, their alarm is absurdly over-pitched.

While alarm over public commitments can be overdone, because the state will retain a capacity to tax, the commercial provision of retirement income has itself been plagued by uncertainties, agency problems, information asymmetry and, last but not least, fund deficits. In 2002-3 pension fund deficits weighed heavily on the Anglo-American-style economies as we will see. In an uncertain economic climate it would not make sense to meet them from current tax income - but it could be desirable to match them to assets which can deliver future income. Willingness to earmark assets for pension funds does not mean that pre-funding has to be handed over to the commercial financial services industry. It does mean that it would be good to find a way of obliging corporations and big wealth-holders to play their part.

The neo-liberal and neo-conservative approaches to the challenge of the aging society argues for the downgrading or scrapping of public provision in favor of commercially-supplied pensions, with the large finance houses such as Fidelity, Morgan Stanley, Merrill Lynch and Barclays playing the key role. It is often argued that we will only be able to afford pensions for future generations if all citizens are legally obliged to make large and regular cash contributions to the banks and money managers. The World Bank Report *Averting*

¹⁴ Niall Ferguson and Laurence Kotlikoff, 'The Fiscal Overstretch That Will Undermine an Empire', Financial Times, 15 July 2003. These authors, respectively an economic historian at NYU and an economist at Boston University, have repeated this theme in a stream of articles, and in their books.

the Old Age Crisis remains the locus classicus of this approach and the financial services industry which stands to gain new business itself constitutes a powerful lobby pressing the case for this type of compulsory pre-funding.¹⁵

Paradoxically, however, the discourse of ‘pension reform’, as it is often called, raises issues which are antithetical to the individualism and faith in the market which are integral to the neo-liberal view of society. The proposed pension regime will only come into being thanks to the state compulsion required to oblige citizens to contribute to a commercially-supplied pension fund. The state is also likely to have a key role in selecting which finance houses qualify for receipt of this new business. So these particular arrangements have little to do with a free market and are more reminiscent of the ‘tax farming’ of Europe’s Anciens régimes, an arrangement whereby monarchs like Louis XVI of France sold the right to collect taxes to private financiers for a lump sum. In this case the state is selling the right to collect a payroll tax in return for transferring its future obligation to pay pensions to a private finance house. A risk not confronted is that the commercial organization, after collecting these taxes for a few decades, invests them poorly and goes bankrupt. Even if this is avoided the saver could encounter heavy charges. Whatever happens private management of pension money hands great power to the fund managers.

In fact the pre-funding of pension entitlements could follow a logic very different from that so insistently recommended to us, namely a logic of ‘responsible accumulation’. As noted above postwar Japan and Singapore have shown that publicly organized pension funds can play a crucial role in fostering investment and growth. Furthermore social movements and trade unions can acquire enhanced bargaining power if they have a say in the disposition of pension funds - but only if the state empowers them by ensuring sources of finance, and principles of accountability, social responsibility and universality. And it would be best for tax subsidies to be reserved to not-for-profit organizations and denied to commercial money managers..

In my view the right to adequate pensions will remain very precarious for all those sectors of the population who have no claim, or only a very modest claim, on asset income. So long as pension commitments are funded only on a PAYGO basis, that is to say funded out of current taxation, they will, I believe, be inadequate and vulnerable. Social movements and trade union action will be able episodically to defend decent levels of provision but if these movements fail to find the path to more durable institutional guarantees then there will always be the risk of weariness and distraction, or of a failure constantly to resist the erosion of popular conquests by the persistent, sapping pressure of capitalist structures and interests. In a capitalist society there are a relatively small number of owners of productive assets who will receive the future streams of income which those assets will generate. Those who do not command such productive assets will find that they have to sell their labor power to feed themselves and their families. For the elderly this is a dismal prospect since their labor power has diminished or disappeared, and they do not wish to add to the burdens already carried by their children.

¹⁵ Peter Peterson, president of the Blackstone group and a former Reagan Cabinet officer, contributes one of the liveliest polemics in favor of privatization, *Grey Dawn*, New York 1997.

Anglo-Saxon Economics and the Problems of Grey Capital

The onset of globalization has tended to coincide with attacks on public pension provision. In the immediate postwar world the economic capacity of the state seemed considerable and had a tendency to grow. It furnished one of the guarantees of prevailing welfare arrangements, including pension entitlements. Yet since the late seventies or early eighties there has been an apparent erosion of the economic power of the state, often actively abetted by the policies of neo-liberal governments. Austerity programs were introduced, entitlements whittled down, and finally large scale privatization programs successfully introduced in one country after another throughout the whole world.¹⁶ Commercial pension funds often purchased equity in the privatized concerns. In the early or mid 1990s some hoped that North Western Europe or parts of South East Asia might offer a model different from that of 'Anglo-Saxon' economics, or stock-market capitalism, and successfully resist the advance of privatization, social cut-backs and market de-regulation. But they could not. Japan became stuck in a stubborn post-bubble depression while the major European economies could not overcome 'Euroscelerosis' - high levels of unemployment and low levels of growth. Both Japan and Europe have adopted elements of the stock market formula and are encouraging private provision of pensions, but without overcoming the obstacles to renewed growth. The Japanese government found that one of the most crucial ingredients of its postwar growth model - the mobilization of retirement savings for public infrastructure projects - has brought steadily decreasing returns.¹⁷

The travail of the European and Japanese economies in the 1990s combined with the soaring advance of the US led to claims that the United States had found a miraculous formula for sustained growth. But from the perspective of 2003 things look very different and it is now clear that the institutions of Anglo-Saxon capitalism confront deep problems. The dot-com bubble has burst, the large telecom companies are mired in debt, the energy traders have been found guilty of faking revenues on a vast scale, and there is widespread distrust of the accountants, bankers, lawyers and regulators who helped to devise the off-balance sheet partnerships and credit derivatives that allowed this to happen. Arthur Andersen, one of the 'big 5' accounting firms and an enthusiast for privatization, has broken up. In the last five years a thousand US companies have been forced to restate their accounts because of irregularities. Across the whole US economy chief executives and their tame boards of directors have taken shareholders for a hugely expensive ride while awarding themselves ever more extravagant 'compensation'. The boards of the large companies issued stock options to senior executive and other favored employees. They then borrowed money from the banks which they used to buy back the company's shares, thus driving up their price and making their own share options more valuable. Robert Brenner explains that the major US non-financial corporations borrowed \$1.22 trillion in the years

¹⁶ For important caveats to this 'globalizing' argument see P. Hirst and Thompson, *Globalization in Question*, London 1998.

¹⁷ Gavan McCormack, 'Japan's Iron Triangle', *New Left Review*, new series No 13, January-February 2002. For European problems see Andrea Boltho, 'What's Wrong with Europe?', *New Left Review*, 2/22, July-August 2003.

1994-99 but used 57 per cent of this money to buy-back company shares while only 15 per cent was used for capital expenditure.¹⁸ Such business heroes as Kenneth Lay of Enron, Bernie Ebbers of Worldcom, and Dennis Kozlowski of Tyco, have been forced to resign but so far they hold onto most of their extraordinary booty. In contrast employees who held corporate stock have seen their savings decimated. Indeed, more generally, the banks which made loans to these companies and then succeeded in selling on – as a ‘credit derivative’ – their consequent credit exposure to companies they knew were overstretched (if not worse). The purchasers of the credit derivatives were very often pension funds. In this way banks passed the parcel while pension funds took a double hit. Partly in consequence US banks have survived the period 2000-3 in far better shape than they did the recession of 1989-92.¹⁹

But while the banks’ balance sheets are quite strong their public reputation is weak. The publication of thousands of cynical e-mails written by analysts to colleagues rubbishing stocks they were recommending to clients has undermined public confidence. There is also a widely-acknowledged distrust of the effectiveness of public regulation, notwithstanding new laws (Sarbanes/Oxley in 2002) and an elaborately brokered deal between Wall Street and the regulators in which the former agreed to pay \$1.4 billion in compensation. At one point a majority of the members of the board of the NYSE were either themselves under indictment or were members of companies under investigation. Among the technical challenges facing regulators are the need to ensure that derivatives are not being used to evade key rules (such as that against insider trading), and also the SPEs and other such devices are not being used to evade corporate taxation. Few doubt that these practices are currently commonplace.

The recent problems of Anglo-Saxon capitalism stem, to a significant degree, from the failure of the pension fund managers, and other institutional investors, successfully to control the new breed of chief executive or to properly represent the interests of the ultimate beneficiaries. The problem is that the fund managers of the corporate pension schemes are themselves chosen by the sponsoring corporations. Moreover the finance houses which manage pension funds also look on the corporations for much other valuable business. Unless a business is in evident crisis the fund managers can be relied on to support the chief executive. The public sector pension funds are a little different, and have lately shown bursts of ‘shareholder activism’ – for example protesting at the exorbitant extent of executive compensation. On a few occasions they have even initiated action that removed an under-performing CEO. But the norm is for the fund managers to play a passive and supine role.²⁰

A pronounced feature of 1990s-style Anglo-Saxon economics was accelerating inequality, and a declining propensity to save amongst the great bulk of richer consumers. The rich saw no necessity to save, because the value of their holdings rose with the stock exchange boom,

¹⁸ Robert Brenner, ‘The Boom and the Bubble’, *New Left Review*, new series No 6, November-December 2000, pp. 5-44, p. 24. See also the expanded account in Robert Brenner, *The Boom and the Bubble*, London 2002.

¹⁹ For more on the role of credit derivatives see my ‘The Enron Debacle’, *New Left Review* 14, March-April 2002. (Also available at newleftreview.org).

²⁰ Robin Blackburn, *Banking on Death or Investing in Life: the History and Future of Pensions*, London 2002, especially pp. 99-225. See also Teresa Ghilarducci, *Labor’s Capital: the Politics and Economics of Pension Funds*, Cambridge, MA, 1992.

but the generality of employees locked into pension plans continued to contribute the funds which, together with the buy-backs, drove up stock prices. The buoyancy of the consumer market also persuaded overseas investors to make acquisitions in the US, masking the decline in domestic savings.

A major force in the erratic global capital flows and share bubble of the late 1990s was the pension funds managed by the major banks, money managers and insurance houses. These funds are hugely important in the United States and Britain but are also significant in Japan, Australia, Canada, the Netherlands, Switzerland, Brazil, Chile and Sweden. The fund managers have become notorious for 'short-termism' and the 'herd instinct' as well as for indulging corporate self-aggrandizement and malfeasance. The phenomenon of the pension funds thus represents a massive alienation of social property. Indeed policy holders often find their own savings being used in ways which damage their own communities for the sake of speculative investment in distant and strange locales. It should also always be remembered that the private pension funds have benefited from large-scale tax relief. Each year the US Federal authorities forego over \$100 billion of tax income because of the fiscal privileges enjoyed by pension plans and 401(k)s, with the subsidy often accruing to the provider or sponsor not the contributor. This buoyant world of the subsidized private pension funds has tended to undermine and eclipse the world of public pension provision.

The Failures of Private Provision

The private pension providers have themselves been fairly profitable and many of the fund managers have been extravagantly paid. But the economics of the post-bubble period have ravaged and deflated the savings made by so many working people in the Anglo-Saxon countries. Following three years of a swooning stock market the position of personal pension funds in the UK and US is dire, with fund values down by between a third and a half. In June 2003 Cazalet Consulting reported that the funds of UK life companies, many of whom supply personal pensions, had dropped by £50 billion in one year to reach £225 billion. The collapse of Equitable Life, founded in 1762, shows that even the oldest and most respectable suppliers can fail. But these types of market risk are not the only problem. The cost of customizing pensions on an individual basis is always high, and commercial providers spend lavishly on promotion and salaries. Personal pension plans receive apparently generous tax breaks and some of those who retired in the 1990s should have done quite well. But much, if not all, of the tax break is absorbed by charges. Indeed even those who faithfully contribute to one scheme for forty years find that charges subtract about 20 per cent of the pot; those who switch or have interruptions can lose 40 to 50 per cent. In the UK most of the eventual pot has to be used to buy an annuity; over the last decade the retirement income that can be bought with each £100,000 in the pot has dropped from £8,000 to £5,000.

In the US those clicking on Microsoft's financial adviser are advised that a couple would need \$1 million if they are to guarantee themselves a retirement income of \$40,000 a year. In other words to get a middle class pension you have to be a millionaire! The average holding in a 401(k), the most popular US savings vehicle, is only \$20,000 and usually fails

to reach six figures let alone seven. These days even the better off mournfully quip that their 401(k) has shrunk to a 201(k).

The pension elite used to be those with membership in an occupational 'defined benefit' (DB) scheme. In these occupational schemes the employer contributes quite generously to the scheme and guarantees a pension related to salary. These schemes are still quite common in the public sector where they enjoy an ultimate government guarantee, something which, at least in the developed countries, makes them much more secure than company-sponsored schemes. The only drawback is that sectoral or municipal budgets are commonly expected to pick up the tab for rising pension costs, so meeting their pension obligation may lead to cutting jobs, salaries and services. The advance of privatisation can also lead to erosion of pension rights so even the historically well-placed public sector is feeling the pension squeeze.

In recent years the corporate sector has increasingly replaced DB arrangements by offering new employees so-called 'defined contribution' (DC) schemes in which the employee's retirement income will be set by whatever the fund can afford. Not only does the employee bear the market risk but the employer contributes much less, say 3-6 per cent of salary rather than 12-15 per cent as in a good DB scheme. While DC schemes are more portable studies show that they are rarely set at a level that will furnish a pension that will replace half of previous income and are often far below this.

Though their membership may be frozen, the traditional DB schemes remain hugely important. They still control large assets - probably around \$3 trillion of assets in the US and perhaps £300 billion of assets in the UK - and have many millions of members. While employers can try to freeze or withdraw from these schemes many are now quite mature. Freely entered into by corporations in more expansive times they impose legal obligations which cannot easily be shrugged off. Indeed so considerable are these obligations that they now pose a real threat to the financial good health of some of the world's largest and most famous corporations.

It has been estimated that the DB pension funds run by the S&P 500 were underfunded to the tune of \$300 billion at the close of 2002; in the UK the DB pension funds of the FTSE 100 have a combined deficit of £85 billion. In the UK actuaries and auditors allowed employers to skip contributions worth £27 billion over the last decade and a half, a sum which if invested at the time would have covered a half or more of the current funding gap. In the US GE went for thirteen years without making a payment to its pension fund. The pension funds are run by the sponsoring company and used as part of its financial planning. The value of the pension funds was rising with the stock market and the company-nominated trustees projected that since they would continue to rise at ten per cent a year or more so the employer could take a contribution holiday. In the early years of the downturn auditors continued to condone under-funding by allowing fund trustees to project unrealistic future returns. But with three years of falling markets this is becoming increasingly difficult to do.

Mature pension funds are often worth as much as, or more than, the parent company. This is true of Rolls Royce and Boeing, Ford and Unilever. Indeed there are many large companies

where today the pension fund deficit alone is now greater than half the market valuation of the company: GM, US Steel, Colgate - Palmolive, Campbell Soup, Lucent, Goodyear, Marconi, ICI and BT. Pension deficits themselves eat away the value of a company's stock. The deficit does not, of course, have to be fixed all at once but the needed measures to reduce the under-funding absorb resources that could otherwise be available for investment. The result is job-shedding and slashed investment programs at companies like IBM, Verizon, Corus and a string of financial service providers. At a time when the 'Anglo-Saxon' economies are threatened by recession this sort of pressure is, to put it mildly, very unwelcome.²¹

It might be asked why corporate sponsors allowed their pension funds to sink in this way. Why didn't they put by reserves in the boom years of the 1990s instead of taking all those 'contribution holidays'?. During the 1990s boom many companies skipped contributions on the grounds that the rise in the value of the fund made it unnecessary to pay them.. While short-termism is partly to blame the complicated rules of DB funds penalize over-funding as well as under-funding. Regulations against over-funding seem to have been designed to prevent companies using their pension funds as a tax shelter in which to stow away surplus profits, with the aim of drawing them down later. As it is DB pension schemes have a strongly 'pro-cyclical' character, promoting over-heating during booms and aggravating cut-backs during recessions.

Many members of DB schemes find themselves with a strong claim against financially weak employers. If the experience of US steel workers is anything to go by those employees will find that they will be asked to dilute their pension rights in order to save their jobs. Such is the flawed structure of the prevailing DB regime that employees can find it makes sense to agree to such proposals. The flaw in the DB structure is that the pension is guaranteed only by one company, the employer. The risk involved for members is spread over several decades – quite long enough for a company to go from being a favored blue chip to an abandoned hulk.

Pensions can be looked at as a deferred wage but they pose a far more difficult problem to the employee and trade union negotiator. If the pay check bounces you learn about it right away. But pension promises concern a fairly remote future. The management that offers the pension package will be ancient history by the time the pension has to be paid. So locking in that promise becomes demanding and difficult.

The UK government announced in June 2003 that it would introduce an insurance scheme. In the US such an arrangement, the Pension Benefit Guaranty Corporation (PBGC), was established in 1974 to which all employers are compelled to subscribe but it has not worked very well. Employers who are in difficulties allow their pension funds to go deeper in deficit counting on the PBGC to bail out their employees. When times are bad the PBGC's reserves are quickly used up, in fact currently it is \$5 billion in the red itself and simply does not have the resources to cover the chronic deficits which it has identified at 270 large corporations. And even in better times the PBGC only guaranteed a proportion of pension

²¹ I have more on all this in 'The Great Pension Crisis', *The Nation*, 16 February 2003.

rights. Likewise the new UK scheme will guarantee 90 per cent of the promised pension and the inflation indexing of the latter will be significantly weakened.

Even supposing it desirable, an insurance approach is expensive to apply to companies which are in the grip of strong cyclical tendencies, such that they rise and fall together. When deficits already loom, and companies are strapped for cash, finding the extra contributions is difficult without cutting back on investment and employment. It might be thought that companies could borrow money – but this is very difficult for those lumbered with pension deficits. Governments are understandably loathe to step in with public money. After all the member of an occupational scheme whose pension has been shrunk by 40 per cent is still better placed than many of their fellow citizens – a half of whom have no secondary coverage at all. And the members of a DB scheme are still better off than the members of a DC scheme, because their employer will have contributed to the fund and because they will now have a guarantee of a pay-out related in some way to salary. But whether an employer offers a DB scheme remains purely voluntary and there is little doubt that the extra expense of insurance will lead to further closures. All of these considerations led Brendan Barber, the TUC general secretary, to comment on the insurance proposal: ‘Britain needs a bigger pensions pot and tweaking at the edges of a voluntary system is not going to achieve this.’

So far public pension entitlements, though somewhat diluted, still remain in something like their old form in many advanced countries. The state’s command of assets and ability to levy taxation has been reduced and this compounds the problem of relying only on taxation for pension provision. A public or social power which commanded more surplus-generating economic assets, and larger fiscal capacities, would be better-placed to deliver on welfare promises. It would still require a vigilant public opinion to make sure that there was no slippage but at least the potential resources would be there.

Strengths of Public Sector Fund Management

I am here assuming, contrary to neo-liberal dogma, that public agencies can effectively discharge the tasks of pension fund management. The case for opposing the privatizing message of the World Bank’s 1994 report, *Averting the Old Age Crisis*, was advanced in an important theoretical paper submitted to a World Bank conference on the future of old age security in Washington in September 1999 by Peter Orszag and Joseph Stiglitz (at this time Stiglitz was himself Chief Economist at the World Bank). The paper, which comprehensively demolished the arguments of *Averting the Old Age Crisis* may still be consulted on the World Bank web site or in a volume which it was subsequently to publish.

22

The Orszag/Stiglitz paper argued that a well-run public pension system could deliver results that were as good as - or better than - those produced by a well-run private system. The advocates of privatization claimed that commercial competition would ensure that private

²² Robert Holzmann and Joseph Stiglitz, eds., *New Approaches to the Old Age Crisis*, Washington DC, 2001. The arguemtn of this essay influenced Barr in *The Welfare State as Piggy Bank*, a book that is sceptical of privatisation but has little to say for pre-funding. Barr has recently worked for both the World Bank and IMF, a sign of some fissure in the privatisation consensus.

pensions would be delivered at low cost but the evidence showed that suppliers chasing pension contracts that were to last a lifetime had a motive to engage in exorbitant marketing expenditure. Furthermore advocates of privatization generally accepted the need for public regulation. Yet if the public agency could be trusted with the regulatory function might it not also be capable of organizing a trust fund?

Orszag and Stiglitz's paper favors the public organization of pensions because of its built-in cost-advantage over private provision and because well-staffed public bodies have the capacity to remedy the information asymmetries which afflict the individual when confronted with long term uncertainty and the wiles of the financial services industry. Indeed there is a bias towards collective provision in pensions because of the expense of marketing and administering millions of individualized schemes and because of the logic of risk-pooling and information-sharing. Within the commercial pension sector occupational schemes applying to a large number of workers generally achieve scale economies, and consequently yield a better return, than personal schemes tailored to an individual. And many occupational schemes are not run by commercial concerns and thus save a further element of commercial profit by undertaking their own fund management. The record of the large pension funds run by public sector workers in the US bear out this argument. Thus the returns achieved by CALPERS and by TIAA-CREF, the university teachers' pension fund, have been well above those available from the purely commercial sector of private pension provision. In occupational schemes employers absorb much of the administrative costs and the more people in the scheme the lower the charges.

State-run schemes share the cost advantages of occupational schemes. Those based on a fund should have much lower costs than private schemes: thus administration and marketing soaks up 2 per cent of the asset value each year of Chile's famous private pensions funds, the AFPs, while it only accounts for 0.2 per cent of the assets of the publicly-run Singapore Central Provident Fund.

How to Pay for Second Pensions? The Advantages of a Share Levy

My case for universal, pre-funded secondary pensions, and non-commercial fund management, complementing a PAYGO-financed basic pension, still begs the question of how the resources for this are going to be raised. I have already argued that conventional tax revenue should be drawn on sparingly or not at all. What scope is there for fiscal innovation? There are a range of possibilities here, each of which could help to build a pension reserve, some of them particularly well-tailored to the long-run nature of the problem.

1. *Employee contributions.* Of course, employees themselves could and should make contributions to a secondary scheme, according to their ability to do so. The existence of the contribution is important for generating a widespread sense of ownership of the program, as well as a source of finance. In contrast to payroll taxes the contribution rate should be progressive. The large numbers of US and UK employees who earn little more than the minimum wage should be given contribution credits. Care-givers and the unemployed should also receive second pension credits. While employee contributions up to about 5 per cent of income will raise serious sums, they will not, by themselves, normally cover the

needs of the scheme. If the contribution rates for those on average incomes are pushed too high then labor costs are raised and job-shedding encouraged, just as with over-reliance on payroll taxes.

2. *Proceeds of public assets or sale of licenses.* Governments with plans to license use of the airwaves, would do well to vest them in pension funds benefiting all citizens.

Nationalization and state ownership often remains the best way of guaranteeing public services - deregulation and privatization has brought a trail of disasters in its wake - and can sometimes yield a revenue surplus. But subsidies are often required for such services.

Moreover, some variants of the public ownership model have created nesting grounds for special interests, rather than serving the welfare of all. The ownership of some public assets by democratically accountable and non-commercial pension funds in each region could yield revenue for a useful purpose, and furnish another model of public enterprise, but, other than in oils states, will only be a supplement.

3. *Betterment Levies* Governments could also place a tax on any increase in commercial site values – including the land on which shopping malls and luxury apartments are built. The rise in the value of commercial land is invariably the consequence of public infrastructure investments in roads and other amenities. It is therefore especially appropriate for it to be a source of public revenue.

4 *Wealth Tax.* There is also a case for considering a ‘wealth tax’, though the experience of several European countries suggests that this type of levy is prone to run into serious loophole problems. The reason for this is that the threshold for the tax has to be set quite high if it is not unfairly to penalize small businesses, farms, and owners of homes that have become expensive urban real estate. Like estates duties (death taxes) reasonable exemptions from the wealth tax can be exploited by the truly wealthy. At all events the tax take from wealth taxes is nowhere very significant.

5. *A Share Levy.* I have left till last what I believe to be the most promising source of finance for pension systems, namely share levies calculated as a proportion of corporate profit. A crucial problem of pension finance is to restore the employers’ contribution, following the switch from DB to DC occupational schemes by many employers. If all citizens are to be able to receive a decent pension then ways must be found to oblige employers to start contributing again. Simply imposing compulsory cash contributions on the employer is not, however, advisable since this raises their labor costs and inclines them, in recessions, to shed labor. There is also reason to believe that corporation taxes are often passed on to the consumer in higher prices.²³

Under the share levy the government requires all corporations to issue new shares to a public pension trust fund each year equivalent to 10 per cent of their profits. Private corporations and large partnerships might be allowed to issue profits-related bonds instead while concerns employing fewer than ten people would be exempt. The trust fund would use

²³ Joseph A. Pechman, *Federal Tax Policy*, New York 1983, pp. 135-40.

the resources obtained by the corporate levy to establish secondary pension arrangements for all citizens. In the US this might include both shoring up the finances of the PBGC and establishing a state-level network of regional social funds which would receive proceeds from the share levy calculated according to the age characteristics of their populations. The various beneficiaries of the share levy would not be able to sell the shares for a lengthy period. Unlike corporation tax the share levy would not subtract from companies' cash flow. Unlike compulsory financial contributions to each worker's pension pot it would not swell labor costs nor act as a tax on jobs. Unlike corporation tax the share levy could not be passed on to consumers in higher prices. With multi-national enterprises the assessment would be similar to that prevailing for corporation tax and the shares could be either in the local subsidiary or in the parent. Employees would be due to benefit from the fund or funds which received their employers' shares but these would be pooled on a regional and/or industrial basis so that no fund was over-reliant on any one enterprise. In principle all citizens' would benefit from the future pension income generated by these share-holdings. The contributions to the secondary system given on behalf of care-givers and the unemployed would come from this source.

It may seem counter-intuitive in the post-bubble climate to suggest that shares should play an important part in the pre-funding of pensions. However the trust funds would often hold the shares for lengthy periods to derive dividend income from them. Dividends are much less volatile than share price, making this a perfectly rational strategy. Since shares are long-term assets they are a good match for pension fund deficits. Moreover remedying those deficits by requiring companies or individuals to make a cash contribution would make no sense in recessionary conditions, such as obtain in the post-bubble environment.

Over time the share levy would transfer control of economic assets from individual capitalists to the pension and social security funds. Care would be taken that all genuine pension funds received more than they lost from the workings of the share levy. This method of financing would also furnish a powerful lever to the funds, enabling them to promote good corporate governance and socially-responsible investment. The social funds would use their shareholding power to act against business-leaders who claim excessive compensation, or deny good working conditions and labor rights to their employees, or invest in ecologically-dangerous processes for short-term reasons. The national power responsible for the levy could ensure an equitable regional distribution of the resulting assets and could thus help to promote national integration and social solidarity.

The proposed share levy will furnish assets which can immediately offset pension fund deficits, and pooled funds could also serve as an insurance reserve. But the question should be addressed of whether such funding really releases more resources for future pension needs. Since the pensions of the future are paid out of future output pre-funding only helps if it transfers real claims on future income streams to the pension fund.²⁴ The proposed device

²⁴ This point is stressed in Nicholas Barr, *The Welfare State as Piggy Bank*, pp. 146-7 where this author points out that pre-funding only helps if either it reduces future spending (e.g. servicing the national debt), or sets aside resources to meet future needs, or if it helps to raise future output. The proposed scheme fits the bill because it (1) would build up socially-owned assets which count against the national debt, (2) it would transfer claims on future dividend income and (3) it would certainly aim to contribute

meets this test since, in effect, it dilutes current shareholdings by a small amount each year transferring the benefit to the pension reserve fund. Whatever dividends the company decides to pay, a portion will now go to pay pensions.

The share levy I advocate is very similar to that proposed by Rudolf Meidner, chief economist of the LO (the Swedish trade union federation), in the 1970s and which was partially implemented in Sweden in the 1980s. The Swedish ‘bourgeois parties’ were strongly opposed to the scheme and so were the twenty or so family-controlled conglomerates which control so much of the Swedish economy. The scheme had a number of design features which aroused fear or opposition. It appeared to favor private sector workers over public sector workers and no specific purpose was proposed for these ‘wage earner funds’, as they were called. The scheme gave a big role, some claimed an overweening role, to the trade unions. The Social Democratic government diluted many of the provisions of the scheme, reducing its incidence and insisting that the shares should be acquired by the funds in a more conventional way. Nevertheless the corporations were obliged to raise large sums. Within less than ten years the funds established by the scheme controlled 7 per cent of the shares quoted on the Stockholm stock exchange. The scheme was suppressed by a conservative Swedish government in 1992 and its resources devoted to a series of research institutes. In countries where most enterprises are owned by a large number of fragmented share-owners resistance might be less effective than in Sweden.²⁵

It would clearly be easier for large states or regions – the US, the EU, Japan - to introduce the share levy than for smaller states which have less leverage over large corporations. However it should be noted that many states are now able to levy corporation tax at rates of 20 per cent or more, and to raise serious sums in this way. In principle the share levy should be no more difficult to calculate or levy than corporation tax. And, as noted above, issuing new shares is easier than finding cash. Of course it remains the case that companies do make routine use of tax havens, SPEs and so forth to evade tax. The US and the EU are certainly in a position to curb these practices if they wish. Partly because of their need for revenue, and partly because of heightened security anxieties, both US and European authorities are currently seeking to penalize and suppress these types of money laundering and tax evasion. Multi-national corporations have long used transfer pricing to accrue profit in locales where taxation is lowest. But a determined public authority can insist on proper disclosure as the price of access to its production facilities or market.

I have stressed the dangerously ‘pro-cyclical’ features of current DB pension fund arrangements, encouraging asset booms and aggravating downturns. Since pension expenditures, and the revenues needed to pay for them loom so large in national accounts their precise incidence can be varied in ways that tame the business cycle and counter-balance inflationary or deflationary dangers. When inflation threatens to get out of hand then employers and staff can be encouraged or obliged to increase their cash contributions; when

to raised output by encouraging effective and responsible shareholding.

²⁵ Rudolf Meidner, *Employee Investment Funds: An Approach to Collective Capital Formation*, London 1978 and the contribution by Jonas Pontusson on Sweden to Perry Anderson and Patrick Camiller, eds., *Mapping the Left in Western Europe*, London 1994. See also Jonas Pontusson, *The Limits of Social Democracy*, Ithaca 1992.

deflation looms then the emphasis can fall on asset levies, so demand will not be diminished. John Maynard Keynes – probably influenced by his Cambridge colleague the ‘liberal socialist’ James Meade - advocated the raising of contributions for a national social security trust fund in 1940 when the outbreak of war threatened to bring about excessive inflation. In a pamphlet entitled *How to Pay for the War* he advocated a system of ‘deferred pay’ as a substitute for increasing income tax. In his scheme five per cent of pay would be paid into special accounts controlled by independent social institutions; money from these accounts could be drawn down at a later period to cover health or retirement needs. In Keynes’s scheme a postwar capital levy would ensure that there were enough resources to meet all needs when the draw-downs began.²⁶ (The arrangements proposed by Meidner were also designed to counter-balance the business cycle; he also devised a scheme whereby Swedish companies could stow away tax-free profits in an ‘investment fund’ during boom periods, and draw them down when times were more difficult)..

The Shape of the New Pension Regime

In most countries today there is still a basic state pension. In the reformed pension regime the basic state pension would be raised until it was equivalent to about 40 per cent of average earnings (in the UK it is currently only 15 per cent and in the US approximately 25 per cent). To achieve this priority goal it might be necessary for the public reserve fund elaborated above to make some top-up payments. The basic pension should be paid in full to all citizens (at present many are not entitled to it because of limited contribution records). Each person’s membership in three secondary pension funds would aim to supply about 30 per cent of average earnings, or of their own previous earnings, up to three times average earnings, whichever was the higher. There would be some variation in retirement income, reflecting different contribution records and investment returns. As in today’s occupational schemes contributions would be calculated as a proportion of income for those in employment. Those who were unemployed, or caring for dependents, would benefit from contributions paid on their behalf from the pension reserve.

Extra matching funds, drawn from the pension reserve, could be used to encourage contributions from members. This would offer incentives to save, based on higher entitlement, to those who have larger contributions. However a ceiling would prevent the rich from building up extravagant levels of entitlement. The principles used here would resemble those already used to calculate a sliding scale of retirement income according to contributions in the US Social Security system and in the UK SERPS (State Earnings-Related Pension Scheme). At present tax incentives offer greater breaks to the well-off than to the poor because the tax system is still at least mildly progressive. Matching contributions would enable the pension fund system to give larger incentives and rewards to the poor than to the rich.

The national trust fund would channel a flow of new shares to registered pension funds based on their membership. It would require of all funds that they achieve a publicly-audited social investment grade before receiving allocations of shares from the levy. Among the

²⁶ John Maynard Keynes, ‘How to Pay for the War’, *Collected Writings*, Vol. IX, London 1972.

features of a fund which would earn it a social investment grade rating would be that (1) it is egalitarian in its internal structuring, (2) gives democratic representation to its members (3) accepts a code of practice based on social priorities and (4) commits to holding most of its assets for, say, five years. (5) accepts fair rules of distribution of benefits. The most generous tax concessions would be available only to socially or mutually-owned funds which give some direct representation to benefit holders, qualify as socially-responsible funds, and allow for a modicum of re-distribution from those with higher lifetime earnings to those with lower lifetime earnings.

Individuals might have rights in three different funds – based on region, occupation, leisure pursuit, and school or college - in order to spread risk. All members of a fund – whether beneficiaries or contributors – would have an equal voice and vote on its policy. However the audit process would ensure that funds kept to actuarially-fair pay-out rates, so that the goal of paying future pensions was not jeopardized by excessive payments in the present. The expertise of universities could be drawn upon to strengthen fund management. The audit process would seek to ensure that pension money was invested in deserving projects and not exposed to undue risk.²⁷

Basing pension funds on alumni associations, resident groups, occupational groups, sporting clubs and other affinity groups, would help to promote participation and reduce costs. In the US the state level Federal Reserve Banks could play a key role as managers of the state-level pension reserve trust fund. They could maintain a register of approved funds, offer actuarial advice and conduct their own independent research. The latter would be welcome to all shareholders, since, even post Sarbanes-Oxley, it is unrealistic to expect banks to disclose rigorous information about their favored corporate clients.

I have pointed out that most of the large funds established for public sector employees in the US are not now commercially run and have a quite good record. In limited ways they display an improvement over the commercial model. Their costs are low and the return they furnish is a good one. Because they are run on a not-for-profit basis, and their benefits are usually guaranteed by the state, they offer greater security than financial houses that can suffer commercial failure. But they remain vulnerable to market shocks.

Pension funds are, of course, a form of capitalist property, albeit a rather strange one, and would remain so even when reformed and ‘socially regulated’. It might seem to some of the defenders of the welfare state that all such funds should simply be abolished and replaced by tax-based state provision. In a previous section I attempted to show why this is a misguided view. Even those who remain unconvinced should ponder the practical difficulty of winding up schemes into which many millions of workers have contributed over much of their working life. In the past labor movements won pension coverage for their members, today they are left to cope with the crisis of pension provision. In some cases trade unions have themselves secured representation on trustee boards and have discovered the new information and leverage that this can give them even in today’s pension regime.²⁸

²⁷ I give more details of such matters in *Banking on Death*, pp. 465-539.

²⁸ For a collection which throws much light on this experience see Archon Fong, Tessa Hebb and Joel Rogers, eds., *Working Capital: the Power of Labor’s Pensions*, Ithaca 2001.

Integrating the new secondary pension regime with existing schemes will require careful negotiations. All past contributions could be recognized for those schemes which merge with the new system. Employers who already supply a scheme that is as generous as, or more generous than, the new national scheme, could be entitled to a substantial rebate on their share levy. However the closure or freezing of many of the best DB schemes in the last few years means that the number that would still qualify is likely to be limited. Moreover, in long run, the new scheme, backed by more than the resources of a single company, would be able to offer greater security. Institutions like the Pension Benefit Guaranty Corporation (PBGC), which insure secondary funded schemes, would be entitled to call on the pension reserve. But companies which persistently called on its aid would be obliged to sign up as full members of the national scheme. Indeed the PBGC, with its experienced staff, might be expanded to administer the national pension reserve.

The package of measures I advocate would aim to establish a quite new pension fund regime, one utterly distinct from that associated with pension funds as we know them today, whether in the UK, the US, Chile or the Netherlands. In these countries, and a widening circle of imitators, pension funds pursue the narrowest commercial objectives and ignore both policy-holders and any wider notion of the public interest.

I have argued that pre-funded pension provision could be transformed into a means to buttress future entitlement and to restore economic leverage to public authorities and social movements. Secondary pension provision will receive the added clout of command of economic assets. Furthermore, all tax-subsidized retirement programs and pension funds would earn their tax breaks by demonstrating a sense of social responsibility. Likewise concerns which are in receipt of investment from tax-subsidized pension funds should undergo a regular social audit. The perspective I am advocating sees fully- or partially-democratized and socialized pension funds as (1) a way of asserting a claim to future streams of income from the productive assets concerned and (2) pushing today's accumulation process in socially-desirable directions. At the limit these twin processes could, if sufficiently well-grounded politically and socially, begin to press towards a non-capitalist mode of accumulation.

The essential features of the proposed system are the diversity of sources of finance, including the share levy, and the steps taken to foster non-commercial custodianship, social responsibility and democratic accountability. These principles could be worked out in a number of different ways reflecting different institutional legacies and popular understandings. I have suggested that each individual should be a member of three different schemes but this is not an essential aspect of the new pension regime I am proposing. It would be perfectly possible to graft the share levy, and the principles of socially-responsible investment, onto existing public pension provision - say a more generous version of Social Security in the US and an amalgamation of the UK's existing State Second Pension and SERPS (State Earnings Related Pension Scheme). In this case most of the resources raised by the levy would be distributed, on the basis of population, to trust funds in every state or region. Some resources from the levy scheme, to being with perhaps a third, would be used to guarantee, or boost, the secondary pension promised by existing DB or DC schemes, according to criteria of fairness established by a National Pensions Board and making use of

the apparatus of the PBGC. Such a pattern could address concerns felt both by those who now have little confidence in the public programs 'being there' for them when they come to retire. It might also reassure small shareholders that their small loss as a result of the share levy would be amply made up by their enhanced pension prospects. Thus in the US the value of Social Security entitlements to a thirty year-old employee on average earnings have been calculated as over \$300,000; this is the sum that such a worker would have to pay to an insurance company to acquire such protection. Measures that would restore confidence in the system and increase its generosity could well prove widely acceptable. Furthermore, using the existing systems of public administration would have cost benefits. Since entitlements in existing schemes are already individualized several features of the regime I have suggested would be easily incorporated. When an individual moved from one state, or region, to another then they would carry their entitlement with them. And the various trust funds could be made democratically accountable, with actuarial safeguards for generational equity. This regionally-distributed model would still mean that there would not be one big public trust fund, with the over-accumulation of power this might imply.

The New Pension Regime and Responsible Accumulation

I have stressed some technical advantages of social and public provision as against private and individual provision. While these are important they by no means ensure that public or social funds will be run in a socially responsible way. Many of the British and American occupational funds have shared the vices of the private funds and have sometimes exhibited the same 'short-termism' and herd instinct as the commercial money managers. The responsibility for this state of affairs lies partly with the legal status of pension fund trustees and the obligations it lays on them. Under the antique provisions of trustee law in the UK and US policy-holders are treated exactly as women or minors were in the eighteenth century. The policies followed by the pension scheme are not determined by the scheme's existing and future beneficiaries. Instead they must respect a curious financial orthodoxy, stating that the funds must be invested according to the criteria of 'prudent experts' in the financial services industry. If trustees chose to invest in, for example, the development of their own region, then they could find themselves the target of legal action. In consequence the trustees find themselves obliged to ignore the needs of the communities in which their members live. Obviously a new statute for pension funds should allow members to elect the trustees and to have a role in formulating general investment policy. The excesses of the bubble economy have discredited the 'prudent man' rule and already permit a looser interpretation of its provisions.

In recent years the public sector funds have also supported campaigns to improve corporate governance and to promote social responsibility. Responding to pressure from social movements and trade unions, Calpers, the Californian Public Employee Retirement System, announced in early 2002 that it would review all its investments with the aim of promoting fair employment practices. Calpers controls \$130 billion of investments. It announced that it might withdraw from investments in companies which are implicated in dangerous working conditions and the denial of trade union rights. However it is worth pointing out that funds which practice Socially Responsible Investment (SRI) now more typically use a strategy of engagement than one of boycott and withdrawal.

‘Engagement’ involves direct approaches to management, backed up by the use of ‘activism’ at AGMs to publicize and penalize bad practice. Funds which benefited from the share levy would naturally own shares in a great variety of concerns and would sometimes be barred from selling those shares. For them this type of engagement - ‘voice’ rather than ‘exit’ - makes the best sense, as it begins to do even for today’s index-tracking funds. Michael Calabrese has pointed out that the strategy of engagement allows social funds to avoid the predicament of ‘having no ownership rights at the companies they most want to change’.²⁹

The pension trust funds would, thus, be expected to play an active part as shareholders in promoting good corporate governance and the avoidance of socially or ecologically harmful practices. It might be objected that beneficiaries of the pension funds, having a pecuniary stake in profitable abuses, would often turn a blind eye to them. According to this argument, allowing members more of a say would actually diminish the pressure for good governance and social responsibility. But it should be remembered that the investment portfolios will be very diversified. The policy-holders’ stake in any one corporation will be very small and their financial return will not mature for quite a long time. I believe that in these circumstances it will be possible to persuade majorities that social injustice and ecological irresponsibility are not the best way to build healthy enterprises nor to contribute to long term fund value. After all, the generality of citizens may well have to pay for the cost of this irresponsibility and injustice long before they can claim any tiny and notional super-profit it might generate. The social funds could thus seek both to promote responsible accumulation and to offer the generality of citizens a chance to participate in shaping the future of their communities. The boards of the Anglo-Saxon corporation would, in consequence, also need to be made far more accountable to shareholders.

The pension funds will be receiving a stream of cash as well as shares, because of members contributions as well as investment income. So they will have money to invest. Regional funds could be allowed, indeed encouraged, to channel a limited portion of their surplus revenue - say no more than 20 per cent - to meeting local investment needs. This might be done by encouraging regional authorities to float development bonds to improve social infrastructure (water, sewage, roads, schools, hospitals etc). These bonds could then be sold to the regional social security funds. Such bonds would carry the guarantee of the issuing authority and would help to diversify fund holdings. Pension funds might also be allowed to invest in low cost social housing. While there should be limits, so that risks do not become overly concentrated, Gordon Clark points out that the experience of such investments, as undertaken by trade union-run funds, has been very positive.³⁰ Similarly Peter Self has proposed that ‘super-annuation funds’ should be made available for ‘longer-term investments which would yield environmental benefits (such as more durable products or energy savings), or which would make a socially-informed use of the many new and

²⁹ Michael Calabrese, ‘Building on Success: Labor-Friendly Investment Vehicles and the Power of Private Equity’, in Fong, *Working Capital*, pp. 93-127, p. 120.

³⁰ See Gordon Clark, *Pension Fund Capitalism*, Oxford 2000, pp. 210-34.

disturbing inventions (such as genetic engineering) which would otherwise be left to commercial exploitation'.³¹

Each year all companies would be required to submit to a social audit, to establish their adherence to acceptable and sustainable working methods, and their commitment to appropriate levels of investment in research and development. Funds which invested in such companies would be rewarded with tax exemption on the consequent earnings. Funds themselves, as noted above, would also have to establish their bona fides - not only as retirement organizations but also as responsible and alert custodians of the all the shares they held. Different social investment grade ratings might be linked to different tax concessions, with the possibility that some might be denied registration altogether. In the US and Britain there are a small number of pension consultants, such as William Mercer and Watson Wyatt, who have accumulated much experience in evaluating pension fund managers. A way would have to be found to draw on, or replicate, their expertise and information.

Measures encouraging corporate social responsibility should be seen as a complement rather than an alternative to legislation, the more so since it would itself require legal backing. There will be bad practices which should simply be outlawed, and other usages which it may be more appropriate to limit. The internal reinforcement of good practice at which the registered pension trust funds should aim would have the further advantage that it could help to discourage bad practices in all areas where the enterprise was active as an investor or purchaser, including those outside its home jurisdiction.

My proposal that pension funds should be obliged to follow socially-responsible policies if they were to receive tax breaks, was singled out for criticism in some reviews of *Banking on Death* - notably those by the *Economist*, by John Chown, a tax specialist in the *TLS*, and by Howard Davies, the then-Director of the UK's Financial Services Authority, in *The Guardian*.³² It was urged that pension contributors would only accept traditional profit-maximizing approaches to investment. But this objection underestimates how discredited such strategies are in the wake of the bubble. And it fails to register the new respectability of SRI.³³ Both the NYSE and the FTSE now both organize SRI indices. These are early days and the procedures and criteria used in drawing up such lists are still primitive. In the future they will be refined and elaborated not abandoned. Indeed some observers believe that the day of the 'universal investor', whose investments are so diversified that they do not properly have 'externalities', has already dawned.³⁴ The true interests of beneficiaries do not automatically entail benign and progressive policies, but they do offer scope for constructing arguments and campaigns which will methodically target the irresponsible practices that shift cost and risk to the wider community. Such is the complexity of the market system that gains in one area may well lead to off-setting losses in another. But, over time, the incremental

³¹ Peter Self, *Rolling Back the Market: Economic Dogma and Political Choice*, Basingstoke 2000.

³² 'Matters of Life And Death', *Economist*, 30 August 2002; John Chown, 'Live Long, Work Long', *TLS*, 23 August 2003; Howard Davies, 'Cracking the Nest Egg', *The Guardian*, 24 August 2003.

³³ For a guide to SRI by an established practitioner see Amy Domini, *Socially-Responsible Investment*, Chicago 2001.

³⁴ See, James Hawley and Andrew Williams, 'The Emergence of Universal Owners', *Challenge*, vol. 43, No. 4, July-August 2000, pp. 43-61. Also the writings of the 'share activist', Robert Monks, *The New Global Investors*, Oxford 2001.

logic would be to stimulate social invigilation and to furnish those campaigning against corporate abuses with powerful allies within the corporate structure itself.

The approach I am sketching has some similarities to that advocated by Michel Aglietta. He argues that employees can gain considerable leverage over the corporate elite by asserting their latent control over the retirement funds lodged in their name.³⁵

Any reform of pension funds aimed at making them engines of social self-management should take heed of the experiences of each country and in particular of the different historic form of social conquests. It would be absurd to introduce Anglo-Saxon-style individualized pension plans to a country where they were unknown only to reform towards a more collective model. Paradoxically the global spread of stock markets makes share levies possible and necessary in a widening circle of countries. It also increases the need for robust regulatory institutions, capable of evaluating annual accounts, and, in the case of public utilities, prices and programs of investment. It is usually not difficult to see the ways in which the share levy and the funded approach can be used to strengthen existing systems of pension provision.

The proposed pension fund regime would gradually bring about a restructuring of economic relations in the direction of a sort of 'stakeholder capitalism' and eventually, perhaps, beyond it.. There would be much greater equality between citizens, and every citizen would have a significant stake in the property regime. Membership in a fund would carry with it the right to regular information and consultation on the fund's policies. The share levy would, over time, transfer the ownership and control of decisive assets into the hands of working people and the citizens generally. The device would continually check market-related tendencies towards inequality within its jurisdiction. It would give citizens and workers real leverage over the economic process as a whole, not simply the workings of a given enterprise, as in some schemes of worker self-management. Employees and citizens would themselves have to address the tensions and trade-offs between current and future interests. They would do so within a framework that did not, as in today's 'financialisation' and 'generational economics', reduce future needs to present values, or assume that every arrangement and relationship should be abandoned once a financially superior alternative is sighted. The fact that decisive assets are held by non-commercial funds will allow them to weigh non-commercial considerations and will, at least partially, 'de-commodify' the social entity exercising ownership. Social movements and workforces would have greater scope to influence investment decisions.

The new pension fund regime would not suppress market relations and would still make use of market signals. It would thereby hope to simplify price formation and avoid the difficulties and complexities of non-market price formation and coordination, as in many variants of planned economy or participatory economics. The combination of markets and of a species of share-ownership would still yield decisions, and determine comparative prices, more economically than procedures that require everyone to inform themselves about, and participate in, in every decision. The latter is not only cumbersome but also can find it

³⁵ See the postface to Michel Aglietta, *The Theory of Capitalist Regulation*, London 1999, and Michel Aglietta, *Le capitalisme de demain*, Fondation Saint Simon 1998.

difficult to allocate voting power (since, for example, the workers at larger enterprise should not always outvote the workers at smaller one).³⁶

The proposed pension fund regime is, in some ways, close to the schemes of ‘market socialism’ and ‘socialization of the market’ theorized respectively by John Roemer and Diane Elson, and their ideas might be drawn upon to give it greater coherence.³⁷ Unlike such models, the proposed regime of ‘responsible accumulation’ aims to address the specific failures and vulnerabilities of ‘grey capitalism’. While it addresses some sources of inequality, unemployment, exploitation and alienation it will not remove them all. For example, though it might offer some openings to ‘fair trade’, it might make little dent on international inequality. It might also prove to be unstable, or transitional to some other, hopefully more equitable and advanced regime. My own guess would be that such a regime will not simply suppress the institutions of capitalism but will also find progressive and democratic uses for them in a progressively non-capitalist context.

While my proposals may seem fairly limited from a radical anti-capitalist perspective, they are likely to be far-reaching enough to provoke stiff resistance. But at least the proposed measures give the majority tangible gains and build on already-functioning institutions. Since it would not be difficult to ensure that every genuine pension fund received more than it lost from the Meidner levy one line of attack would be pre-empted. Existing shareholding wealth would be diluted by only about 1 per cent a year, on average. Moreover, some shareholders might appreciate the new institutional pressure for good governance. Chief executives might not welcome the new investors but the share levy would pose less problems than do corporation taxes, since the levy makes no cash demands on the company - it simply directs the dividends to a different group of shareholders.

The proposed measures robustly address the yawning and widely acknowledged crisis of pension provision. There are few alternative proposals which can claim the same. Moreover the interlinked proposals are all based on tendencies or practices already present in today’s ‘grey capitalism’ and their suggested re-arrangement into a more coherent, democratic and accountable schema is, I believe, consequently deserving of the name ‘real utopia’.

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Robin Blackburn is Visiting Distinguished Professor at the Graduate Faculty, the New School University, New York, and Professor of Sociology at the University of Essex. He is an editor of New Left Review and his most recent book is Banking on Death, or Investing in Life, the History and Future of Pensions, Verso London 2002.

³⁶ I explore some of these problems in ‘Fin de Siécle’, *New Left Review*, 1/ No 185, January-February 1991; also published in Robin Blackburn, ed., *After the Fall: the Failure of Communism and the Future of Socialism*, London 1992.

³⁷ See John Roemer, *The Future of Socialism*, New York 1994 and Diane Elson, ‘Socializing the Market’, *New Left Review*, 1/No. 172, Nov-Dec., 1988.