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Article

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PENSION REFORM: HANS-WERNER'S RESEARCH AND POLICY IMPACT

JAMES POTERBA*

Two of the hallmarks of Hans-Werner's long and distinguished research career are his uncanny ability to identify the most important unresolved issues in economic policy design and his remarkable capacity to offer novel and insightful analysis on these issues. Even on questions that have been studied by many others, Hans-Werner has found ways to provide new perspective and to suggest creative solutions, enriching both academic discourse and the public policy debate. These talents are well-illustrated by his analysis of public pension reform, a subject that attracted his attention in the late 1990s.

Hans-Werner began to study pensions at a time when there was a growing recognition that Germany's public pension system was on an unsustainable trajectory. The tax rates that were projected to apply to future workers seemed infeasible. What should be done? With characteristic clarity and insight, Hans-Werner observed that the key challenge was the result of demographic change. A decline in Germany's rate of population growth, which translated into forecasts of growing numbers of older and retired individuals relative to the number of active workers, was the basic source of long-term pressure on the pension system. Hans-Werner communicated this insight to policy-makers, and at the same time, he found an innovative way to formulate the analysis of public pension systems for the research community. His widely-cited *International Tax and Public Finance* paper on 'Why a Funded Pension System Is Useful and Why It Is Not Useful', published in 2000, developed the concepts of explicit and implicit tax burdens for a public pension program. It showed that a transition from a pay-as-

you-go to a funded pension system, without any change in the benefits promised to existing participants, would not alter the sum of these burdens – a key point that needed to be recognized in analyzing policy reforms.

Hans-Werner did not limit himself to conceptual discussion of pension systems. Working with other researchers at CES, he developed a model of Germany's pension system that made it possible to analyze how various reforms, including complete or partial transition to a fully-funded system, would affect the system's sustainability and the tax burdens on various generations. Hans-Werner also drew attention to potential reforms that were not directly focused on public pensions, but that would have important consequences for the pension system. He suggested, for example, that tax and benefit policies be tilted to encourage higher fertility, perhaps by varying the rate of contribution to the pension system as a function of an individual's number of children. He also pointed to the potentially important role of immigration policy in addressing long-term pension funding challenges. By framing the challenge of pension reform in a broader economic context, Hans-Werner was able to bring novel policy options to the public policy dialogue.

The research that Hans-Werner carried out in the late 1990s played a key role in stimulating further analysis of public pension reform in Germany and many other nations. Its impact was not limited, however, to the research community. It also was an important input to the significant reforms of the German public pension system that were adopted in 2001, the so-called 'Riester reforms'. These changes, which shifted away from the pay-as-you-go model and introduced a fully-funded pension account as a component of old-age support, were in the spirit of the reform proposals that Hans-Werner had analyzed. These reforms were pioneering. Taken together, the German public pension reforms of 2001 and 2004 substantially strengthening the pension system's long-term sustainability.

Hans-Werner is one of the most versatile economists of his generation. He has repeatedly displayed com-

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fort and ease in mastering new concepts and tools for the analysis of particularly pressing policy questions. When the problem of funding public pensions became a first-order topic of policy debate, he directed his research attention to understanding source of the problem, even though this had not been a topic of his prior research. He also proposed potential solutions. Once pension reforms had been enacted, Hans-Werner's research shifted to other, more immediate, issues. Few economists have offered insights and constructive policy advice on so many different topics, spanning taxation, climate and energy policy, pensions, immigration, monetary and credit policy, and labor market reform. Fewer still have been able to carry out path-breaking research while also performing policy analysis that has constructively advanced the policy process. Hans-Werner is a member of this extraordinary group.