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Good and bad news about Washington's wrangling over debt ceiling

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As this musing is being written (July 30), there is no resolution to the debt ceiling negotiations that are going on in Washington. Is there anything to be learned from labor negotiations about this political process?

Union-management negotiations have been much studied, in part because information about them is more available than on other types of negotiations. There have been many empirical studies trying to understand the failures of union-management negotiations to reach "peaceful" resolutions, i.e., to understand why and when work stoppages occur. The negotiating process in collective bargaining itself has also been the subject of public policy; various policies have sought to encourage resolution of labor disputes. For example, the Federal Mediation and Conciliation Service was created to offer the services of professional mediators to union and management negotiators.

Clearly, there are many differences between the political negotiations process underway in Washington at this writing and a typical labor negotiation. But one similarity is the presence of a deadline. August 2 has been declared to be the date on which the debt ceiling will be hit and, therefore, the date at which – unable to borrow – the federal government will be short of cash to pay all its bills. This date is widely referred to in the news media as "default" although actual nonpayment of federal debt service – interest, etc., on Treasury securities - seems unlikely.

Interesting questions have been raised about whether August 2 is truly the date on which cash runs out and about whether there are ways for the Treasury to get around the ceiling limit, even if August 2 is the actual date. Nonetheless, so far the parties to the negotiation have been treating the August 2 date as a deadline. So what do we know about deadlines and negotiations?

It appears that deadlines must at least threaten unpleasant or potentially unpleasant consequences to facilitate agreements. When deadlines are totally arbitrary - one thinks about Israeli-Palestinian negotiations in which dates on which something is supposed to be agreed come and go without any real impact – they have no effect. But in the case of union-management negotiations, real things do happen at one critical date: the contract expiration. The contract expiration is more than an arbitrary date on the calendar.

Most union contracts have some version of a no-strike/no-lockout clause. So when the contract expires, so do those clauses. The parties are then free to impose economic harm on each other. Although we don't keep data on such things, it is often the case that settlements are reached just as the expiration date is reached, sometimes with midnight settlements.

I used to do a 2-hour simulation in a class dealing with labor negotiations — Yes, Virginia, there used to be classes on labor relations! — in which negotiating teams were given points for various contract gains (from their perspectives). After one hour, however, it was specified that the existing contract expired and a strike would immediately occur producing point losses. There was a one-shot point loss at that moment and then a loss for each minute of non-settlement. I won't go into more details — the game was elaborate with the union team, for example, split between skilled and unskilled workers with different point gains and losses — but suffice it to say that most settlements occurred just at the deadline. On the other hand, not all teams avoided strikes. In simulations as in real labor negotiations, an incentive to settle is not a guarantee of settlement.

At the time of the 1947 Taft-Hartley Act, there had been a wave of post-World War II strikes. Congress seemed to think that the strike problem reflected a need to make available more time for negotiations. If the parties just had more time, they would be more likely to settle peacefully rather than blunder into a work stoppage. Public policy should insist that they have enough time to work things out. So the Act includes a 60-day pre-notification period.

Under the Act, even though contracts have internal expiration dates, the contract could not end until one party notified the other at least 60 days in advance. The problem with this approach is that the parties obviously know when their contract expires — they negotiated it after all. So the phenomenon of the midnight settlement has nothing to do with notification and everything to do with having a deadline that has real consequences. With the deadline approaching, there is pressure on both sides to stop bluffing and to reveal their true negotiating positions. The imminent deadline thus facilitates a settlement, albeit often at the last minute. That's the Good News.

But there is Bad News, too. Obviously, there are cases in which settlements are not reached at or before the deadline and in which work stoppages occur. In some cases, these stoppages can turn out to be prolonged and destructive to both parties. So the fact that deadlines, even real deadlines, don't always bring about settlements is a part of the Bad News.

But there is another Bad-News feature of intense negotiations (which become more intense as the deadline/expiration date approaches). When a settlement is reached, the parties can suffer from an illusion about how the outcome should be evaluated. There is a distinction between reaching a deal — a narrow definition of success — and the quality of that deal.

It is easy for parties to negotiations who have had a really tough time reaching an accord to feel that they have been successful simply because they did reach a settlement and it was so difficult to get there. In the late 1970s, I examined the union sector in a Brookings book and noted that there seemed to be a bubble-like phenomenon occurring at that time in the union-nonunion pay differential. A continuous rise of that differential had to be ultimately unsustainable and yet, in each individual contract negotiation, the parties undoubtedly felt that they had reached the best deal possible. After all, the economic background of the 1970s was difficult. In the end, however, the process of the widening pay differential reversed with a wave of concession bargaining in the 1980s and substantial job loss and market-share loss in the union sector.

More recently, I have followed California budgetary policy and the negotiations in the state legislature and with the governor that produced eventual budget deals. The state constitution specifies that the legislature is supposed to enact a budget by June 15, i.e., two weeks before the start of the new fiscal year on July 1. Presumably, this advance date exists to give the governor time to decide whether to veto the budget, sign it as passed, or sign it with line-item vetoes. However, until recently, there was no consequence if a budget was not passed by June 15 since there were no penalties for the legislature if that deadline passed without a budget. State fiscal affairs between June 15 and June 30 continued normally under the terms of the yet-to-expire fiscal year; nothing was disrupted.

However, at one time the expiration of the California fiscal year on June 30 was similar to a contract expiration in the union sector. If there was no new budget enacted by July 1, state bills could not be legally paid until a deal was reached. So although under the state constitution the governor proposes a new budget in early January, the heavy negotiations in the legislature did not typically start until the June 30 deadline approached, almost six months later.

But sometimes — as in labor negotiations — a deal was not reached in time and there was no budget on July 1. When such episodes occurred, courts began stepping in, requiring that the state pay certain bills despite absence of a budget. The consequences of missing the June 30 deadline were thus progressively reduced since the government continued functioning in most respects. The June 30 deadline, in short, had less and less meaning as court interventions accumulated. Having a deadline on paper became less and less effective in incentivizing an on-time deal. Budgets were chronically enacted late.

Last November, however, California voters approved various budget-related ballot initiatives. Among them was a provision that members of the legislature would forfeit their pay for each day beyond the constitutional June 15 deadline that a deal with a "balanced" budget was not reached. It was not clear how this proviso would work in practice. But there was a clear rush in the legislature just before June 15 to pass something. The resulting budget was ruled to be unbalanced and legislators' pay began to be forfeited. A new deal was quickly reached. So the effect of the deadline was evident — the Good News. However, the quality of the deal (how the enacted 2011-12 California budget will work out as the current fiscal year unfolds) is not so evident — the Bad News. The budget was "balanced" in significant part on paper by making optimistic economic assumptions that might not be realized.

The difference between political negotiations — whether at the state or federal levels — and labor negotiations is that in the latter case, processes have evolved involving third parties — mediators, arbitrators — who can help the parties resolve their problem. In the case of political negotiations, such as those surrounding the federal debt ceiling, there seem to be no external facilitators available. Indeed, there are many centrifugal forces that have come into play.

So, as this musing is being written, what lessons do we draw? The August 2 deadline for the debt ceiling negotiations does seem to matter. The various parties seem to be taking it seriously and assuming that bad things could happen thereafter.

However, if the deadline turns out to matter enough to bring about a House-Senate-President accord, the contents of that deal need to be evaluated separately from the negotiations process. The fact that it was tough to get there does not mean that the outcome is inherently desirable. As in the case of labor negotiations in the 1970s, the consequences of tough bargaining were not immediately apparent to the negotiators. They undoubtedly felt that just reaching a deal was an accomplishment. But in the longer term the consequences were unfortunate.