Chicago’s Pension Crisis

An Automatic Pension Stabilizer: Making Pension Funding as Binding as the Pension Promise

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Chicago is Drowning in Pension Debt

$53B

unfunded pension liabilities
across 5 systems (FYE 2024)

Funded Ratios (FY 2024)

24.5% Police & Fire
26% Municipal (MEABF)
42.6% Laborers
48% Teachers (CTPF)

All far below the ~80% benchmark often cited in public discussion - though that threshold is contested in the actuarial literature

The Scale of the Problem

Five major retirement systems - police, fire, municipal employees, laborers, and teachers - carry a combined $53 billion gap between assets and promises.

Pension contributions now consume **18% of the city's budget**, up from $1.4B in 2019 to $2.9B in 2025.

Every dollar in debt service is a dollar **not spent on schools, transit, or public safety.**

Amortizing $53B over 30 years at 6.5% takes **~$4.1B/yr - the amortization payment alone (Normal Cost is additional, not total required contribution)**. The city currently contributes $2.9B.

The System Was Designed to Underfund Pensions

01 The Pension Ramp

State law deliberately back-loaded contributions - keeping required payments artificially low for years while liabilities compounded.

The city paid below its actuarially required contribution for decades.

Result: Funded ratio fell from 85% in 2000 to under 30% today.

02 Benefit Expansions

COLAs and early retirement options were added without corresponding funding increases.

Illinois' Art. XIII, Sec. 5 makes earned benefits constitutionally irreversible.

Result: Liabilities locked in; only the funding side can move.

03 Optimistic Assumptions

Funds assumed roughly 6.75–7.25% returns; shortfalls against those targets added to the gap - but were a contributing factor, not the dominant cause.

The dominant institutional driver remained chronic underpayment of the required contribution, not investment underperformance.

Result: A contributor to the gap - but underfunding, not returns, is the core problem.

How the Debt Trap Works

Annual budget negotiation

- Pension contributions compete against schools, transit, police - every year.

Elected official calculus

- Cut a service voters notice today, or defer a pension payment they’ll notice in 20 years?

Funding rules permitted chronic underpayment

- Illinois’ statutory contribution formula allowed below-actuarial payments for years. Discretion enabled deferral.

The solution is not to change officials - it’s a better rule that works for all.

The Fix: Make the Right Choice Mandatory

The Proposal

A **certified Actuarially Determined Contribution (ADC)** - Normal Cost plus the scheduled closed-amortization payment - is the binding minimum, paid automatically every year in state statute.

When a fund's funded ratio deteriorates, supplemental recovery contributions are required on top of the ADC. **No trigger may ever reduce contributions below the certified ADC.**

The stabilizer does not **generate dollars**. It is a commitment device that recognizes actuarial costs on schedule and closes legacy debt on a fixed amortization, under independent oversight.

The political fight shifts:

From "whether to fund" (discretionary, always deferrable),
To "how to fund" (mandatory, tractable)

Four Design Safeguards

Certified ADC floor

The independently certified ADC is the minimum; recovery triggers only add to it, never subtract. Annual increases are capped at 1–2% of payroll during phase-in.

Closed amortization + lockbox

Legacy debt is retired on a fixed closed schedule; additional contributions are legally protected in a lockbox and cannot be reallocated.

Independent Review Board

An independent board certifies the ADC and funded status annually, separate from political budgeting; modification requires a supermajority.

Stress testing + public dashboard

Annual stochastic stress testing and a public dashboard disclose funded status and every trigger event to taxpayers, workers, and bond markets.

The Rule Is Simple - The Effect Is Structural

Funded Ratio - ADC is always paid in full		
Below 60%	Certified ADC + strongest supplemental recovery contribution (phased, capped)	⚠ **Critical**
60 – 70%	Certified ADC + smaller supplemental recovery contribution	⚠ **Stressed**
70 – 85%	Certified ADC only - no recovery surcharge unless stress tests indicate	✓ **Adequate**
Above 85%	Certified ADC continues; permit reserve buffer; reductions only if actuarially justified	★ **Healthy**

No tier may reduce contributions below the independently certified ADC - the ADC is a floor, triggers only add to it. All recovery contributions are 100% employer-funded by design; each fund's actuary certifies the ADC and funded ratio annually.

Employers Pay 100% - A Deliberate Design Choice

The Legal Reality

Illinois Constitution, Art. XIII, Sec. 5:

“Membership in any pension or retirement system of the State ... shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.”

Amending this requires a **three-fifths supermajority** in both chambers plus statewide voter approval.

The design implication: **accrued benefits cannot be cut. The APS places all recovery contributions on the employer side by design - avoiding any need to test employee-side changes against Illinois pension-protection law.**

Why This Is Also Good Politics

For unions: A guarantee that the city will actually fund the benefits it has promised. Underfunding is the real threat to retirement security.

For taxpayers: Deferred pension debt is just a future tax increase in disguise. Paying now is cheaper.

For bond markets: A credible, rule-based contribution path could, under favorable conditions, support Chicago’s credit standing and help contain borrowing costs.

The Stabilizer Doesn't Find the Money - It Forces Chicago To

What It Is NOT

✗ A revenue measure
✗ A bond issuance
✗ A pension benefit cut
✗ A promise that money will appear

The stabilizer does not resolve where the money comes from. That remains a political question requiring difficult tradeoffs.

What It IS

✓ A binding rule: if ratio falls, employer must pay more
✓ An institutional commitment device
✓ A reframe of the political question
✓ A structural fix for the governance failure

The debate shifts from WHETHER to pay to HOW to pay.

That is a more honest and more tractable political conversation.

The Math: $400M in Year 1, $2B by Year 5

Annual Additional Contributions

(Illustrative: assumes ~$10B payroll - materially larger than the four city-funded systems' actual payroll)

- **Year 1: +$400M**
- **Year 2: +$800M**
- **Year 3: +$1.2B**
- **Year 4: +$1.6B**
- **Year 5+: +$2.0B (sustained)**

Why It Helps - and Why It's Not Enough Alone

Amortizing $53B at 6.5% over 30 years takes **~$4.1B/year (amortization only; Normal Cost is additional).**

Current baseline: **~$2.9B/year.** Adding $2B stabilizer → **~$4.9B total**, above the amortization-only benchmark (full adequacy also depends on Normal Cost).

The honest caveat:

Adding $400M rising to $2B, on top of $2.9B already contributed, is a very large commitment. The proposal does not minimize that - it argues the alternative, continued deferral, is worse.

If liabilities grow 3%/year, $53B could reach ~$129B in 30 years - the stabilizer is **necessary but not sufficient.**

Does the APS Actually Work?

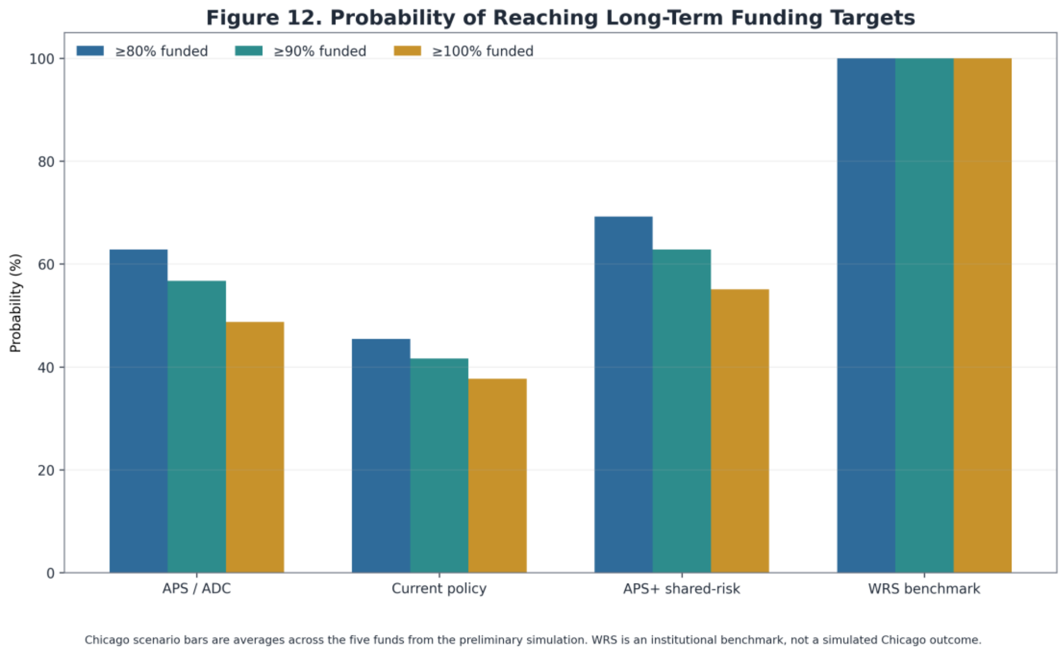

Figure 12. Probability of reaching ≥80% / ≥90% / ≥100% funding over 30 years, by scenario. WRS is an institutional benchmark, not a simulated Chicago outcome.

Status quo

Persistent long-run downside vulnerability.

Core APS / ADC-based rule

Materially improves the probability of reaching long-term funding targets.

Prospective shared-risk counterfactual

Shows additional improvement under a hypothetical prospective risk-sharing design; not part of the core APS.

WRS benchmark

Institutional reference point only; not a simulated Chicago outcome.

Author-generated 2,000-path Monte Carlo policy simulation calibrated to PPD and actuarial data; not an official actuarial forecast. Any prospective shared-risk figure is a counterfactual, distinct from WRS itself.

Wisconsin: A Dual-Response Pension Architecture

Wisconsin Retirement System (WRS)

~100%

funded for decades - while most peer systems deteriorated

A dual-response design absorbs shocks on two sides:

- Active-participant side: actuarially responsive contributions (predetermined, not negotiated)
- Retiree side: investment-sensitive annuity adjustments above a protected Core floor
- Shocks become predetermined adjustments, not ad hoc political negotiations

Chicago vs. Wisconsin

Funding ratio: Chicago 24–48% / WRS ~100%
Unfunded liability: $53B / Near zero
Governance: Discretionary / Rule-based
Benefits: Fixed by constitution / Variable

The adaptation for Chicago:

Illinois' constitution protects accrued benefits, so Chicago imports only WRS's legally transferable contribution- and governance-side discipline - not its retiree benefit-adjustment channel. That channel is, at most, a prospective option for future accruals.

The WRS Triggers Fired - And the System Held

Episode 1: The Great Recession (2008–2013)

5 years

of consecutive Core annuity decreases: the 2008 Core Fund loss set off five straight years of reductions for affected retirees.

Retirees saw their inflation adjustments cut - automatically, transparently, without legislative override.

Outcome: WRS recovered and stayed near full funding. Core annuities are protected by a floor - they can never fall below a retiree's original Core amount.

Source: Wisconsin ETF, "The Great Recession: 10 Years Later."

Episode 2: Market Shock (2022)

−21%

Variable annuity reduction after Core Fund returned −12.92% and Variable Fund −17.83%.

Real discomfort for retirees. Applied automatically. No legislative action. No override.

Outcome: Strong prior-year returns buffered Core. System remained solvent.

The lesson: institutional design held even when the adjustment was painful.

Source: Wisconsin ETF, 41st Annual Retired Lives Valuation (Dec. 31, 2022).

State Enabling Legislation: Permission to Tie Its Own Hands

Why State Action Is Required

- **Contributions are statutory:** Chicago's funds are governed by the Illinois Pension Code (40 ILCS 5/); the City's required contributions cannot be changed unilaterally by the Mayor and City Council.
- **No bailout sought:** The APS asks the General Assembly for authority to adopt an automatic funding rule - not for state dollars.
- **Authority, not appropriation:** Enabling legislation lets Chicago bind itself to actuarially adequate funding; the fiscal burden stays with the City.
- **A self-imposed constraint:** The point is a durable rule Chicago cannot later defer - a constraint it places on itself.

The Realistic Path

Phase 1 - State enabling legislation

Authorize automatic adjustments for the four city-funded systems. CTPF requires separate CPS/state coordination.

Phase 2 - City Council codification

Embed the mechanism in the municipal budget process with lockbox protections and a supermajority override threshold.

Phase 3 - Actuarial certification

Each fund's actuary certifies the funding ratio annually. Contribution adjustments apply the following fiscal year automatically.

Chicago should not ask Springfield for money. It should ask for permission to tie its own hands.

Where Does $2B Come From? An Honest, Uncertain Answer

Property & Sales Tax $470M–$660M

A 10–15% levy increase → ~$170–260M (applied to a sourced FY2024 base). A 1pp sales-tax increase → ~$300–400M is an illustrative planning estimate, not an official projection. Politically painful but the largest stable source.

Spending Reform Illustrative potential savings - not a committed funding source

Figures sometimes cited at 3–5% of a $16.6B budget are illustrative only: no Chicago-specific, program-level study validates them, and such savings are slow and politically difficult to realize.

Targeted Excise Taxes Tens of millions (liquor)

The only documented, in-motion excise is the off-premises liquor tax (see next slide), which yields tens of millions - a targeted complement with a public-health rationale, not a primary source.

Financial Tools Risk-bearing; not a structural substitute

Pension obligation bonds create a net benefit only if returns exceed borrowing costs (risky); asset monetization yields one-time proceeds without closing the recurring gap. Complements with material risk - never substitutes for structural reform.

The Liquor Tax: Small Revenue, Strong Logic

Already In Motion

Chicago restructured its Liquor Tax effective **March 1, 2026**. A 1.5% point-of-sale tax now applies to packaged goods establishments.

Two reasons it matters beyond revenue:

1. Public health rationale:

- Off-premises consumption linked to increased public safety costs. Revenue generation with a documented externality rationale.

2. Political tractability:

- Already enacted at 1.5%. Scaling is a credible next step. The mechanism exists - raising the rate is a simpler political ask than a new tax.

Projected Annual Revenue (COFA)

Baseline (no change):	**$28.6M**
1.5% (current, FY 2026):	**$31.9M**
3.0%:	**$35.2M**
4.5%:	**$38.5M**
6.0%:	**$41.8M**

Source: COFA, "Revenue Resource: Liquor Tax," Table 5 (2026).

Important caveat:
The incremental revenue (~$3M at the current 1.5% rate) is trivial against a ~$2B need - it illustrates a diversified strategy, not a solution. Chicago also already has among the highest combined municipal alcohol taxes in the nation, so cross-border purchasing risk is real.

The Risks Are Real - The Design Accounts for Them

Risk
Budget pressure: $400M–$2B/yr competes with services Phase-in cap (1–2%/yr). Relief only via a constrained fiscal-emergency mechanism: independent certification, disclosure, and every deferred dollar becomes dated closed-amortized debt - no resets.
Labor resistance: Unions may oppose budget constraints Frame as benefit security (100% employer); early bilateral engagement; underfunding is the real threat to pensions
Political override: Future legislatures may weaken the rule Codify in state statute (not ordinance); supermajority to modify; mandatory public reporting of trigger events
Liability growth: ~3%/yr growth could outpace contributions Treat stabilizer as floor; build 5–10% surplus buffer; pair with broader fiscal reforms
Workforce competitiveness: Higher employer costs may affect recruitment Phase gradually; targeted wage adjustments in high-demand fields; DB benefits still generous vs. private sector

Chicago Can Still Fix This - But the Rules Have to Change

01 The crisis is severe, but its cause is identifiable.

- Chicago's pension crisis is not simply the inevitable result of defined-benefit pensions. Decades of inadequate contributions allowed liabilities to compound.

02 The APS fixes the institutional failure at its source.

- The APS makes the certified ADC a binding minimum, closes the amortization schedule, and automatically requires additional recovery contributions when funded status deteriorates.

03 Chicago can put its pensions on a sustainable path.

- It will require real fiscal sacrifice. But Chicago does not need to break pension promises or wait for a bailout. It needs a durable rule that ensures today's obligations are actually funded today.

Make pension funding as binding as the pension promise.

Q & A

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Key Takeaway

Make pension funding as binding as the pension promise.

The APS replaces political discretion with automatic funding discipline - protecting workers, taxpayers, and Chicago’s fiscal future.