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THE FUTURE OF PENSIONS IN CHICAGO

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The city of Chicago faces budgetary pressure in the upcoming years because annual payments to its pension funds are projected to increase from year-to-year, with the most substantial increases projected to impact its 2020 and 2022 budgets. In addition, the pension funds are significantly underfunded and that has a negative impact on the city's overall fiscal health and credit rating.

The city of Chicago is responsible for four different public pension systems: the Firemen's Annuity and Benefit Fund, the Laborers' Annuity and Benefit Fund (LABF), the Municipal Employees' Annuity and Benefit Fund (MEABF), and the Policemen's Annuity and Benefit Fund. Both employees and the city pay money into the funds, and upon retirement employees receive a pension benefit. Notably, Chicago teachers are in a separate fund, for which Chicago Public Schools are responsible (and not the city government).

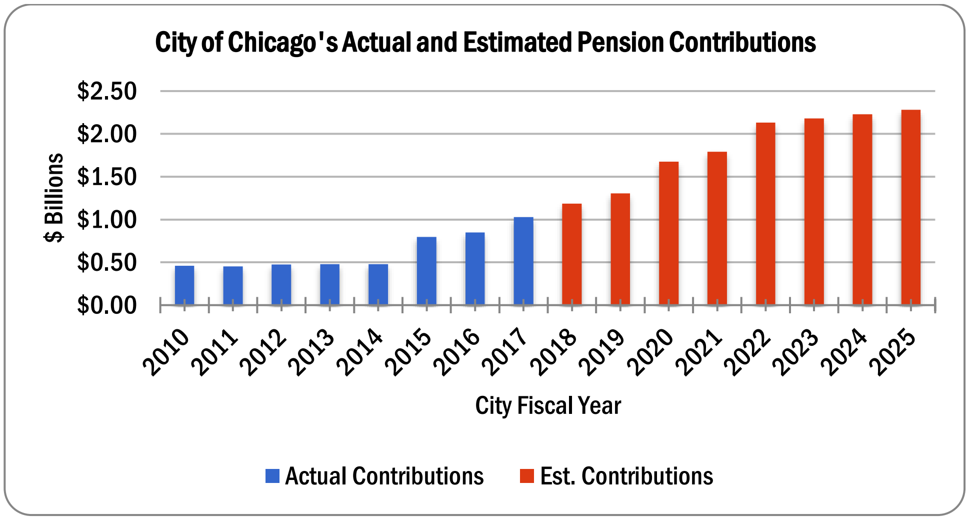
A government's contributions to its pension fund are typically tied to the cost of benefits and payments for any unfunded liabilities—this means that a government's payments increase as a pension fund's ***funded ratio*** decreases. The funded ratio is the ratio of pension liabilities to assets, where a funded ratio of 100% means that every $1 in pension liabilities is matched with $1 of assets. Chicago's four pension funds are significantly underfunded with a combined funded ratio of just 27%.

State law dictates how much money Chicago has to pay into the pension funds each year. Until recently the city's required contributions were not tied to the cost of benefits or unfunded liabilities, and this contributed to funds' poor financial condition today. The funding laws for all four funds were recently changed, with the police and fire funds changed in 2016 and the laws for LABF and MEABF changed in 2017. The table below summarizes the funding laws for the city's four funds.

Police and Fire Funds	**LABF and MEABF**
2015-2019 fixed dollar amounts; after 2019, city contributions must be sufficient so each fund has a funded ratio of 90% by the end of fiscal year 2055.	2017-2021 fixed dollar amounts; after 2021, city contributions must be sufficient so each fund has a funded ratio of 90% by the end of fiscal year 2058.

The city's contributions can be confusing to track because there is a difference between the city's budget year and when the actual payments to the funds are made (this is largely because of the property tax cycle). So the city's budget year 2020 contributions are actually paid in 2021. Because of this tracking discrepancy one document may have the contributions attributed to 2020 while another attributes them to 2021. When looking at Chicago's pension data, it is important to pay attention to whether the contributions being reported are categorized by the payment year or the city's budget year. State statute, for example, is mainly written per actual payment year. This brief, however, reports the city's pension payments per the city's budget year.

Recent estimates have Chicago's pension contributions increasing by nearly 30% (about $280 million) in 2020, and its payments are projected to increase each year thereafter (as shown in the chart below). The next mayor will need to propose the city's 2020 budget, as well as identify an overall plan for making the city's future required pension payments.



Candidates campaigning on changing Chicago's revenue structure will have to show how feasible their proposals are for crafting the 2020 budget. Below is a brief rundown of a few policies and their strengths and challenges.

City Income Tax would generate new revenue, but also requires action by state lawmakers and a change to the state constitution (which could not occur before November 2020). Several large cities, like New York and Philadelphia, have income or wage taxes.

Increasing Property Taxes is perhaps the most feasible action for a mayor, since the mayor can set the amount (called the "levy") to be collected, with the approval of the city council, with minimal interference from state officials. However, raising the city's property tax levy is likely to be especially unpopular, because it will compound the tax impact of increases in property values some property owners have recently experienced.

The Pension Obligation Bond (POB), an idea discussed by Chicago Chief Financial Officer Carole Brown at the city's 2018 investors' conference, would restructure Chicago's pension obligations by perhaps smoothing increases in pension payments. A POB may generate long-term savings; however, savings are not guaranteed, and will depend on market conditions. In addition, issuing a POB may reduce Chicago's capacity for other borrowing and may involve significant risks should the economy slow.

A Casino in Chicago could bring in significant new revenue**.** Current law (lobbied for by the Emanuel administration) specifies that if there is a Chicago casino, any revenue it generates will go to the police and fire pension funds.