
Legal and Practical Challenges Facing Illinois and Chicago Public Pensions

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I. **Introduction**

There is increasing attention to Illinois and Chicago pension plans as their chronic funding issues continue to worsen. As of 2023, there were 284,667 participants in Chicago-specific pension plans and 1,385,277 participants in Illinois pension plans.¹ Illinois's state-level pension debt is the largest in the nation at \$172 billion and the city of Chicago's pension systems carry over \$35 billion in debt, surpassing the pension debt of 44 states.² While several potential routes for reform have been proposed, there are substantial political and legal obstacles, particularly the Pension Protection Clause of the Illinois State Constitution.

a. Scope of Crisis

A common metric used to evaluate the health of pension plans is a funded ratio, which is the pension plan's assets as a percentage of liabilities.³ Illinois' pension plans have the lowest funded ratio in the nation, with a funded rate of only 50.6% in 2024.⁴ In comparison, the national average funded ratio is 81.4%.⁵ Illinois is one of only four states remaining below 60% funding.⁶ This issue extends to the individual pension plan level, with four of Illinois' pension plans in the ten worst-funded pension plans in the nation, the most of any other state.⁷ Further, when analyzing the size of unfunded liabilities relative to the size of a state's GDP, Illinois also has the lowest percentage in the nation at 18%.⁸

Chicago is facing its own pension funding crisis, as its debt has risen by 13% over the past five years.⁹ Chicago's police and firefighters plans are funded at 24.5%, its laborers fund is at 43% and its municipal workers fund is at 26%.¹⁰ There are multiple factors commentators point to when explaining the causes of the pension funding crisis, but it is generally thought to be a confluence of overgenerous pension benefits, insufficient and irregular funding by the state, and politically-manipulated investment assumptions and underfunding.¹¹ Specifically, Illinois pensions suffered significant investment losses due to recessions in 2000 and 2008.¹² The Chicago pension plans also lost \$16 billion during those recessions and have earned \$11 billion back.¹³ Further, Chicago was not required to fund their plans based on actuarial principles, which meant that the plans accumulated debt that accrues interest.¹⁴ State-funded pensions also

¹ <https://bit.ly/471BHL3>

² <https://bit.ly/48rigwa>; <https://bit.ly/4nYKFP2>

³ <https://bit.ly/4hc0SxH>

⁴ <https://bit.ly/4n4IQP9>

⁵ <https://bit.ly/48sf17G>

⁶ *Id.*

⁷ *Id.*

⁸ *Id.*

⁹ <https://bit.ly/3W9NpNh>

¹⁰ *Id.*

¹¹ <https://bit.ly/4n7e2NU>

¹² <https://bit.ly/495kFNq>

¹³ *Id.*

¹⁴ *Id.*

accrued significant debt as lawmakers have borrowed money to make the required contributions or skipped payments.¹⁵

b. Recent Legislative Activity

There are concerns that recent Illinois legislative activity will exacerbate the pension funding problem.¹⁶ In August 2025, Governor J.B. Pritzker signed House Bill 3657, which increases pension payouts for Chicago police officers and firefighters.¹⁷ An analysis of the bill has shown that it will increase pension debt by an estimated \$11.1 billion and result in a funded ratio for both pensions to be under 20%.¹⁸

An additional bill amending Illinois pension benefits was proposed in the spring legislative session, which as of September 2025 has not passed.¹⁹ The proposed bill, Senate Bill 1937 (“S.B. 1937”), makes changes to all state and local pension funds except for the Retirement Plan for Chicago Transit Authority Employees. It proposes increased benefits including lowering retirement ages, enhancing final average salary calculations, increasing pensionable salary caps, and increasing cost-of-living adjustments (“COLAs”).²⁰ The bill would cost the state \$273 million more than current law in the first year (FY 2027) and would require an additional \$63.5 billion in taxpayer contributions to pension funds through 2049.²¹

Labor union coalitions strongly supported S.B. 1937, arguing it was necessary to solve public employee shortages and to pass the “Safe Harbor Test.”²² Because Illinois public employees generally do not have to pay into Social Security, IRS standards create a “Safe Harbor Test” which requires pension plan benefits to be equivalent to Social Security benefits.²³ Advocates for S.B. 1937 argue that the bill is necessary to ensure Illinois pension plans pass the Safe Harbor Test.²⁴

However, part of the recently passed budget attempts to address the Safe Harbor problem, by appropriating \$75 million for budget reserves which can be accessed if their pension plans fail the Safe Harbor test.²⁵ In a press release, Governor Pritzker described the intention of the reserve fund as “cover[ing] the estimated first year costs of adjusting [Social Security Wage Base (“SSWB”)] for State Tier II members until legislation is enacted.”²⁶

¹⁵ <https://bit.ly/4hh8Cyl>

¹⁶ <https://bit.ly/3WabfZg>; <https://bit.ly/48xSal0>

¹⁷ <https://bit.ly/4nVzVky>

¹⁸ *Id.*

¹⁹ <https://bit.ly/3WIM3co>

²⁰ Fact Sheet on SB 1937, HA2: For State and Local Tier 2 Employees, CIVIC COMMITTEE COMMERCIAL CLUB OF CHICAGO.

²¹ *Id.*

²² <http://bit.ly/4hcCnR7>

²³ <https://bit.ly/3Jfude5>

²⁴ <https://bit.ly/4nQXIHX>

²⁵ *Id.*

²⁶ <http://bit.ly/3KJRvcF>

c. Overview of Illinois and Chicago Pensions

Illinois' public pension system is governed by the Illinois Pension Code, 40 ILCS 5/1-5/24 ("Pension Code"). Under the Pension Code, there are five main state-funded retirement systems:

Plan	Statute	Participants	Assets (millions)	Funded Ratio
State Employees' Retirement System of Illinois (SERS) ²⁷	40 ILCS 5/14-101	100,919	25,378.8	43.3%
Teachers' Retirement System of the State of Illinois (TRS) ²⁸	40 ILCS 5/15-101	171,445	73,585.5	45.8%
State Universities Retirement System (SURS) ²⁹	40 ILCS 5/15-101	228,105	28,770.9	46%
Judges Retirement System of Illinois (JRS) ³⁰	40 ILCS 5/18-101	957	18,226	44.3%
General Assembly Retirement System (GARS) ³¹	40 ILCS 5/2-101	128	6,265	24.2%

²⁷ <https://bit.ly/46QH8MG>

²⁸ <https://bit.ly/48xHhWu>

²⁹ <https://bit.ly/47dANtL>

³⁰ <https://bit.ly/4n59ebG>

³¹ <https://bit.ly/4nOG4if>

The city of Chicago contributes to four pension systems created by the Pension Code:

Plan	Statute	Participants	Assets (Millions)	Funded Ratio
Municipal Employees' Annuity & Benefit Fund of Chicago (MEABF) ³²	40 ILCS 5/8-202	36,968	1,271.8	24.25%
Laborers' & Retirement Board Employees Annuity & Benefit Fund (LABF) ³³	40 ILCS 5/11-101	7,645	1,253.4	42.7%
Policemen's Annuity & Benefit Fund ³⁴	40 ILCS 5/5-101	27,767	4,562.6	24.1%
Firemen's Annuity & Benefit Fund ³⁵	40 ILCS 5/6-101	4,775	1,774.2	23.7%

The Pension Code also establishes eight additional pension plans, many of which cover large local municipalities, all funded in part through participant contributions:

- Police Pension Fund – Municipalities 500,000 and under (40 ILCS 5/3-101) funded with municipal property taxes.
- Firefighters' Pension Fund – Municipalities 500,000 and under (40 ILCS 5/4-101) funded with municipal property taxes.
- County Employees' and Officers' Annuity and Benefit Fund – Counties over 500,000 inhabitants (40 ILCS 5/9-101) funded with county property taxes.
 - This provision establishes a plan for Cook County employees. The plan had \$14,658,155,957 in assets for 2024, a funding ratio of 65.93% and 58,856 members.³⁶
- Forest Preserve District Employees' Annuity and Benefit Fund (40 ILCS 5/10-101) funded with district property taxes.
- Park Employees' and Retirement Boards Employees' Annuity and Benefit Fund – Cities over \$500,000 (40 ILCS 5/12-101) funded with park district property taxes.

³² <https://bit.ly/4nhmFpm>

³³ <https://bit.ly/4h9K9Lo>

³⁴ <https://bit.ly/42FVqx4>

³⁵ <https://bit.ly/4olSfTJ>

³⁶ <https://bit.ly/4nU8zeB>

- This provision establishes a plan for Chicago Park employees. In 2024, the plan had \$450,974,225 in assets, with a funded ratio of 33.2% and 6,176 members.³⁷
- Metropolitan Water Reclamation District Retirement Fund (40 ILCS 5/13-101) funded with contributions by the Water Reclamation District.
- Public School Teachers’ Pension and Retirement Fund – Cities of over 500,000 Inhabitants (40 ILCS 5/17-101) funded through employer contributions (i.e., Chicago Public Schools) along with “contributions from any other sources.”
 - This provision establishes the Chicago Teachers Pension Fund. In 2024, the plan had \$12.7 billion in net assets, with a funded ratio of 48.1% and 96,000 members.³⁸ As of 2025, the plan was funded through a property tax levy, Chicago Public Schools contributions; and state contributions.³⁹
- Retirement Plan for Chicago Transit Authority Employees (40 ILCS 5/22-101) funded through contributions from the Chicago Transit Board.
 - This provision establishes a plan for Chicago Transit Authority employees. In 2024, the plan had an actuarial value of assets of \$2.12 billion, with a funded ratio of 54.39% and 7,734 members.⁴⁰

d. Funding

Illinois pension plans are funded through employer contributions, through state or local property, and employee payroll contributions.⁴¹ Under the Pension Code, state contributions were supposed to increase in stages until the pensions were 90% funded by 2045.⁴² However, Illinois lawmakers and governors have failed to set aside enough money for pensions over the years, and have skipped some pension payments altogether and borrowed money to make other payments.⁴³ Further, the amount Illinois lawmakers are required to contribute to the pension system is lower than the amount actuarially determined as necessary to pay down the pension debt.⁴⁴

Five pension funds rely on Illinois State revenue as their primary funding source, including the Illinois and Chicago Teachers’ pension plans, the State Employees and State Universities funds, and the General Assembly and Judges’ Retirement funds.⁴⁵ Chicago pension plans are primarily funded through local property taxes, as the Pension

³⁷ <https://bit.ly/4na36z0>

³⁸ <https://bit.ly/3KVMwp4>

³⁹ <https://bit.ly/4nctQyV>

⁴⁰ <https://bit.ly/43cDRF4>

⁴¹ <https://bit.ly/4q9wYyc>

⁴² 40 ILCS 5/14-131(e).

⁴³ <https://bit.ly/42G3Kgr>

⁴⁴ <https://bit.ly/4hfJpEE>

⁴⁵ <https://bit.ly/496Apj5>

Code provides that each municipal entity may levy taxes on property within its district to raise funds for its pension contribution although the City may also fund its obligations from other legally available sources including the proceeds of city borrowing.⁴⁶ The Chicago Transit Authority (“CTA”) pension plan receives specific state revenue funding from the Chicago Transit Authority, whose funding is generated through CTA system-generated revenue (e.g., ticket sales) and transfers from the State of Illinois.⁴⁷

In contrast to state-funded pensions, the Pension Code did not originally require Chicago-funded pensions to be funded based on actuarial principles under the Pension Code.⁴⁸ The Chicago and Cook County Pensions only paid a percentage of employee contributions from two years prior.⁴⁹ For example, the Municipal Employees’ Annuity and Benefit Fund required that the City of Chicago contribute a multiplier of 1.25 times the rate of employee contributes from two years earlier to determine its annual contribution, so for each dollar contributed by a City employee two years prior, the City would need to contribute \$1.25.⁵⁰ Accordingly, because the pension contributions were tied solely to payroll, the contributions were not affected by a change in benefits, or assets and investments, which allowed pension debt to accumulate.⁵¹ Additionally, the state passed legislation that allowed Chicago to make little to no pension contributions in 2006 and 2007, which further increased debt accumulation.⁵² However, this methodology changed in 2016 when state laws passed that changed the methodology to focus on funding the plans to a funding percent on a ramp-up schedule to get to 90% funded by 2058.⁵³

e. Benefits Accrual and Vesting

Each pension plan provides benefit accrual rules, but all feature two basic components: 1) the percentage of pension benefit that a worker accrues per unit of service and 2) the final average pay rules, which take into account a worker’s final years of compensation to calculate that worker’s pension benefit. All funds use the highest consecutive eight years of pay out of a worker’s final 10 years of employment. With the exception of the CTA pension fund, each plan limits a worker’s benefit accrual rate to a percentage of their final average salary, either 75 or 80%.

The Pension Code provides unique age and vesting requirements for each public pension plan. Further, different vesting rules apply depending on an employee’s first participation date. If an employee first participated in the pension plan prior to January 1, 2011, they have a Tier 1 plan. If an employee first participated in the pension plan after

⁴⁶ See e.g., 40 ILCS 5/8-173 (governing the Municipal Employees’ Annuity & Benefit Fund of Chicago; “Except as provided in subsection (f) of this Section, the city council of the city shall levy a tax annually upon all taxable property in the city at a rate that will produce a sum which, when added to the amounts deducted from the salaries of the employees or otherwise contributed by them and the amounts deposited under subsection (f), will be sufficient for the requirements of this Article. . .”).

⁴⁷ 40 ILCS 5/22-101.

⁴⁸ <https://bit.ly/3WCALXd>

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.*

⁵³ *Id.*

January 1, 2011, they have a Tier 2 plan. Generally, Tier 1 employees vest after five to eight years of service and Tier 2 employees vest after 10 years of service, with most plans imposing minimum age requirements for annuity eligibility. For all Tier 2 employees in Illinois pension plans, there is a ten-year vesting requirement. In the Cook County Pension Fund and the Chicago Municipal Employees' Fund, both Tier 1 and 2 plan participants are considered vested if they have ten or more years of service credit. For the Chicago policemen's and firefighters pension funds, there is a ten-year vesting requirement for Tier 2 employees and a 20-year vesting requirement for Tier 1 employees.⁵⁴

f. Governance

Under the Pension Code, each plan has a board of trustees tasked with managing the pension plan investments. Generally, each pension board is composed of employees, retirees, and senior public sector officials. The board is responsible for managing the assets of the fund, overseeing plan administration, and hiring local actuaries to verify the amount of the State's contribution to the pension plan. Every board member is required to attend eight hours of ethics training.

In addition to the boards of trustees for each plan, the Pension Code also established the Illinois State Board of Investment, which oversees the investments in three state plans: the State Employees' Retirement System, the Judges' Retirement System, and the General Assembly Retirement System. The Illinois Department of Insurance's Public Pension Division is responsible for managing local police and firefighter pensions for municipalities with a population under 500,000.

Any individual taking certain actions with respect to the investment of public pension funds has a fiduciary duty. These actions include exercising discretionary authority or control respecting management of the pension fund or management or disposition of its assets; rendering investment advice or advice on selection of fiduciaries for compensation; having discretionary authority or responsibility in the administration of the pension fund or retirement system. Fiduciary duties are also generally imposed on investment advisors, managers, and consultants to the pension funds.

II. Illinois Reform

Illinois has made many attempts at pension reform, with limited long-term success. Under the Tier 1 plan, members enjoyed generous benefits, including early retirement at age 60 and compounded annual pension increases at 3%.⁵⁵ These benefits have proved unsustainable as Illinois was unable to fund these liabilities. In the 1990s, Governor Jim Edgar introduced a funding plan to address the crisis, but underfunding has persisted. By 2009, the Tier 1 benefits were significantly underfunded, with an estimated \$62.4 billion in unfunded liabilities and a combined funded ratio of just 50.6%.⁵⁶

⁵⁴ <https://bit.ly/43mPpFM>; <https://bit.ly/47o8yJU>

⁵⁵ <https://bit.ly/4ohm7Ar>

⁵⁶ <https://bit.ly/48sEn5r>

The most significant reform occurred in 2010 with the creation of the Tier 2 pension system, which reduced benefits for new hires and was projected to generate an estimated \$71 billion in savings.⁵⁷ In 2013, the General Assembly passed Public Act 98-599 to curb the costs of the pension crisis further. However, in 2015, the Illinois Supreme Court struck it down for violating the Pension Protection Clause, as it reduced benefits for current pension plan members. More recently, in 2024, the Illinois Supreme Court upheld the state's reform efforts aimed at consolidating police and firefighter pension funds to improve investment returns. Today, the main challenge is ensuring Tier 2 pension systems comply with federal Safe Harbor laws, as stagnant salary caps risk forcing employees and employers into Social Security. Lawmakers face limited options: preserve Tier 2 savings, align the Tier 2 Salary Cap with the Social Security Wage Base, offer defined contribution plan options to future hires, implement new taxes, or seek a constitutional amendment. But any reform proposal will be constrained by legal concerns, severe fiscal impact, workplace impact, and political feasibility.

a. *In re Pension Reform Litigation*

The Illinois legislature has chronically underfunded Illinois pension systems. Due to concern over ongoing funding deficiencies, Illinois included a provision known as the “Pension Protection Clause” when it adopted a new constitution in 1970. This provision provides that “[m]embership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.” Ill. Const. article XII, section 5. The Illinois Supreme Court has held that the plain language of this clause “served to eliminate any uncertainty as to whether state and local governments were obligated to pay pension benefits to the employees.” *People ex rel. Sklodowski v. State*, 182 Ill. 2d 220, 228-29 (1998).

In fall 2013, as an attempt to address Illinois' large debt, the legislature passed a statute that, among other things, set forth mechanisms designed to reduce retirement annuity benefits for members of Tier 1 state pension plans. Five separate lawsuits challenging the law under the Pension Protection Clause were filed almost immediately and consolidated under *In re Pension Reform Litigation*, 32 N.E. 3d 1, 14 (2015). Four of the lawsuits also challenged the retirement annuity reduction provisions under article I, section 16, of the Illinois Constitution, which provides that no law impairing the obligation of contracts shall be passed. *Id.*

In 2015, the Illinois Supreme Court ruled on the consolidated cases. It held that the statute was unconstitutional because it violated the Pension Protection Clause, which expressly prohibited diminishment of benefits in public retirement systems. *Id.* at 28-29. The court also rejected the argument that it was nevertheless a valid exercise of the state's police power. *Id.* at 20. Additionally, the provisions reducing annuity benefits were not severable from the rest of the statute because the “overarching purpose of the law was to shore up State finances, improve its credit rating and free up resources for other purposes by reducing, i.e., diminishing, the amount of retirement annuity benefits paid to

⁵⁷ <https://bit.ly/3J86hJt>

Tier 1 members.” *Id.* Accordingly, the court permanently enjoined enforcement of the statute. *Id.* at 30.

This decision limits the options that Illinois has for reducing Illinois’s and Chicago’s substantial pension debt, as any pension reform cannot include a reduction in annuity benefits paid to members, absent a constitutional amendment.

***b.* Reform Proposals**

Illinois’ pension reform options include preserving Tier 2 savings, aligning the Tier 2 salary cap with the Social Security Wage Base, expanding defined contribution options for new state employees, and adjusting funding schedules. These measures aim to maintain federal compliance, reduce long-term liabilities, and provide more predictable costs without adding to the state’s unfunded obligations.

***i.* Preserve Tier 2 Savings**

One approach to addressing the Illinois pension crisis is to preserve the savings generated by Tier 2 pension systems, which are projected to save the state approximately \$71 billion by 2045.⁵⁸ By contrast, union proposals to expand Tier 2 benefits to mirror Tier 1 benefits would add nearly \$30 billion in costs.⁵⁹ Preserving the Tier 2 savings helps stabilize Illinois finances and prevents increased taxpayer burdens.

Specifically, Tier 2 plans differ from Tier 1 plans because they:

- (1) raised the retirement age from 60 to 67;
- (2) reduced the final average salary calculation from the average highest of four of the last ten years of service to the average highest of eight of the last ten years of service;
- (3) changed the annual pension benefits calculation from 3% compounded annually to 3% or one-half of the increase in the Consumer Price Index (“CPI”); and
- (4) imposed a limit on pensionable salary growth with a cap.⁶⁰

Advocacy groups such as the Illinois Policy Institute support maintaining these provisions,⁶¹ while public unions, such as We are One Illinois, argue that Tier 2 has weakened public employee recruitment and retention.⁶²

***ii.* Align Tier 2 Salary Cap with Social Security Wage Base**

⁵⁸ <https://bit.ly/46RaUkm>; <https://bit.ly/42CojKI>

⁵⁹ <https://bit.ly/4qd4nrK>; <https://bit.ly/3Jd8gwb>

⁶⁰ <https://bit.ly/4h9PCBU>

⁶¹ <https://bit.ly/478S8nA>

⁶² <https://bit.ly/4qaJ0aH>

To ensure compliance with the federal Safe Harbor laws, groups including the Civic Federation and Civic Committee of the Commercial Club of Chicago, and the Illinois Policy Institute have proposed raising the Tier 2 salary cap to match the Social Security Wage Base,⁶³ which is the maximum amount of a person's earnings subject to Social Security tax in a given year.⁶⁴

Safe Harbor laws require public pension plans to at least match the Social Security Wage Base.⁶⁵ This means that the public pension plan must provide minimum benefits that are comparable to Social Security benefits. To determine compliance, the IRS evaluates the key plan features, including:

- the compensation "multiplier" (the percentage of final pay per year of service);
- The number of years used to determine final average compensation under the plan; and
- The definition of compensation used by the plan.⁶⁶

Most public employees do not pay into Social Security because they opt into pension plans that provide coverage that is comparable to Social Security.⁶⁷ This allows Illinois to save money because the tax would be a total of 12.4% of federal taxes. This amounts to a tax of 6.2% of the employee's income and 6.2% from the employer.

The core issue is that pensionable salary under the Tier 2 pension systems is growing more slowly than the Social Security Wage Base. Because earnings above the Tier 2 Salary Cap are excluded from pension calculations, higher-earning public employees experience a smaller amount of their actual salary credited towards their pension than they would under Social Security. The disparity creates a risk of noncompliance with the Safe Harbor laws because Illinois pensions end up covering less income than Social Security would.

For example, in 2011, both caps were set at \$106,800. By 2024, the Social Security Wage Base rose to \$168,600, while the Tier 2 Salary Cap was \$125,744. This growing disparity occurs because Social Security adjusts for inflation. If the gap continues to widen, the pension plans may fail to meet the Safe Harbor requirements and could force employees and employers to begin paying into Social Security.

On June 1, 2025, Governor J.B. Pritzker announced that the Illinois General Assembly passed the state's \$55.1 billion fiscal year ("FY") 2026 budget, which includes a \$75 million reserve fund to cover the cost of adjusting certain Tier 2 members to the Social Security Wage Base until corrective legislation is enacted.⁶⁸ The Social Security

⁶³ <https://bit.ly/4ncyBsh>; <https://bit.ly/4nTM0qo>

⁶⁴ <https://bit.ly/4oqG349>

⁶⁵ <https://bit.ly/4olYp6j>

⁶⁶ *Id.*

⁶⁷ *Id.*

⁶⁸ <https://bit.ly/495r811>

Wage Base for 2025 is \$176,100, while the Tier 2 Salary Cap remains at \$125,744.⁶⁹ While the reserve fund offers temporary relief, it does not solve the underlying compliance issue. The Illinois Policy Institute has urged lawmakers to use the reserve fund only when a federal violation occurs. This would spare taxpayers from benefit hikes across the board and save Illinois billions of dollars in new debt. Without a comprehensive actuarial analysis, it is difficult to assess how many people might be at risk of violating the Safe Harbor laws and how much money the reserve fund needs to fill certain gaps.

Instead, permanently aligning the Tier 2 Salary Cap to the Social Security Wage Base would help pension plans in Illinois from falling out of compliance with federal law. The change would only affect those who earn above the Tier 2 Salary Cap, ensuring pension credit, while limiting the cost increase to about \$280 million annually for the next 20 years.⁷⁰ Although raising the Tier 2 Salary Cap would add costs to the state's ever-growing debt, the alternative is far more expensive. If the state fails to comply with the Safe Harbor laws, it could be required to pay the federal government more than \$856 million each year.⁷¹ Ultimately, this proposal is attractive because it provides higher earners with better retirement benefits.

iii. Offer Defined-Contribution Options for New State Employees

Another option is for Illinois to offer new state employees the defined-contribution ("DC") option that is currently available only to members of the State Universities Retirement Systems ("SURS"). Limiting this option to new hires avoids conflict with the Illinois' Constitution Pension Protection Clause, since contractual rights for current employees vest on the first day of employment.

Since 1998, SURS employees have been able to participate in the Retirement Savings Plan ("RSP"), formerly known as the Self-Managed Plan ("SMP"). Under the SMP, SURS members had to "use 100% of their assets to purchase an annuity at the time they retire to qualify for retiree healthcare or take a lump-sum distribution forfeiting retiree healthcare and requiring the participants to leave the plan at retirement."⁷²

Contrastingly, the newer plan, RSP, provides SURS members with an option that functions like a private sector 401(k) plan while maintaining the state-backed retirement protections.⁷³ A 401(k) plan is a qualified profit-sharing plan that allows employees to contribute a portion of their wages to individual accounts. Accordingly, the RSPs offer employees more flexibility regarding their retirement savings. Groups such as the Illinois Policy Institute proposed expanding the SURS pension plan to all state pension plans, as RSP is portable and offers more transparency. Additionally, these plans offer lower vesting requirements, allowing someone, for example, the ability to retire at age 62 with

⁶⁹ <https://bit.ly/4ofSwYc>

⁷⁰ <https://bit.ly/4nLgmew>

⁷¹ <http://bit.ly/4n6laZJ>

⁷² <https://bit.ly/3KPT6NY>

⁷³ <https://bit.ly/3W3f4iZ>

only five years of service and no age-based benefits reduction.⁷⁴ A full actuarial analysis is needed to estimate the potential state savings from adopting this proposal.

The options for a DC plan are mandatory in some states, optional in others, and offered as a hybrid DC/defined-benefit (“DB”) plan in other states. At least two states have seen great success after implementing similar plans.⁷⁵ Rhode Island and Tennessee have adopted similar plans and now have one of the best-funded pension plans in the country. In 2010, Rhode Island’s pension fund was severely underfunded, estimating \$7 billion in underfunded liabilities and a combined funded ratio of 48.4%.⁷⁶ In 2011, the General Assembly passed the Rhode Island Retirement Security Act (“RIRSA”) to address the pension woes. Among the various RIRSA reforms, Rhode Island implemented a hybrid retirement system plan comprised of a new defined-contribution plan and a limited distribution benefit plan. Within 11 years, the combined funded ratio increased to 60.4% and actuarial projections anticipate reaching an 80% fund ratio by 2031. As Pew Research notes, Rhode Island’s 2011 reforms have put the state on track to reach fiscal sustainability.⁷⁷

In 2023, Tennessee was ranked first in the country with the lowest unfunded pension liabilities.⁷⁸ The state’s public pensions have been well funded for decades. In 2014, Tennessee enacted legislation that required local governments to fully fund the actuarially determined contribution rate (“ADC”).⁷⁹ An actuarially determined contribution is the amount needed to fund benefits over time.⁸⁰ “The purpose of the law is to ensure financial stability and financial soundness of a political subdivision’s pension plan or plans to provide pension benefits for future generations of employees.”⁸¹ According to Pew Research, the 2014 hybrid plan, a combination of a defined benefit plan and a 401(k) deferred compensation plan, fixed employers’ contribution rates to a combined 9% (4% into the defined contribution component and 5% into 401(k) accounts).⁸² This plan saved Tennessee \$1.17 billion in employer contributions for state and higher education employees and public school teachers.⁸³

Adopting a similar defined-contribution option could help Illinois improve its funded ratio and become more fiscally sound over time. The defined contribution option provides

⁷⁴ *Id.*

⁷⁵ Other states have adopted the defined-contribution option, including Alaska, Colorado, District of Columbia, Florida, Indiana, Michigan, Montana, North Dakota, Ohio, Oklahoma, Pennsylvania, South Carolina, and Utah. See <https://bit.ly/4qhhZ5A>; <https://bit.ly/4hmt9lh>. The following states have adopted defined-benefit plans, including Alabama, Arizona, California, Delaware, Hawaii, Idaho, Iowa, Louisiana, Massachusetts, Maine, Maryland, New Hampshire, New Mexico, Nevada, New York, North Carolina, New Jersey, South Dakota, Texas, Vermont, West Virginia, Wisconsin, and Wyoming. *Id.* The remaining states have adopted a hybrid plan, including Connecticut, Georgia, Oregon, Virginia, and Washington. *Id.*

⁷⁶ <https://bit.ly/496lbtb>

⁷⁷ <https://bit.ly/4o3fF08>

⁷⁸ <https://bit.ly/43mfCUV>

⁷⁹ <https://bit.ly/47e1MFu>

⁸⁰ <https://bit.ly/4hc4la9>

⁸¹ *Id.*

⁸² <https://bit.ly/43cLpro>

⁸³ <https://bit.ly/4oInYUP> at 7.

employees flexibility with their retirement savings while simultaneously relieving the state of its pension burden.

iv. Extend the Pension Funding Deadline

Governor Pritzker proposed extending the pension funding deadline from 90% funding in 2045 to 100% funding in 2048.⁸⁴ In 1994, Governor Jim Edgar proposed to reform the Illinois pension crisis by reaching a 90% funding target by 2045, known as the Pension Ramp.⁸⁵ Lengthening the funding schedule by an additional three years to fund at 100% would relieve pressure from the state's budget in the early years, but the state will pay more for the benefits long-term.⁸⁶ According to Fitch Ratings, Governor Pritzker's plan could help ease risks associated with the Illinois pension obligations and improve credit quality.

However, the Center for Tax and Budget Accountability ("CTBA") proposes a different model that would save Illinois \$62.9 billion. Accordingly, CTBA proposes:

- (1) The current funded ratio for 2045 should be reduced from 90% to a target of 80% funded, which is the United States Government Accountability Office standard for a healthy public pension plan;
- (2) Issue a total of \$6.7 billion in pension obligation bonds over FY 2023 through FY 2030, using all bond proceeds to front-load payments to the pensions and retire existing unfunded liabilities;
- (3) Move the contributions to the pension plans from the last day of the fiscal year (June 30) to the first day of the fiscal year (July 1), generating an additional year of investment returns and positive compounding effect over time; and
- (4) Re-amortize the repayments of outstanding unfunded liabilities on a level-dollar basis, alleviating the fiscal strain the Pension Ramp will cause.⁸⁷

v. Increase Funding through Taxes

Illinois could increase its property taxes as a potential solution to the pension funding issue. The Federal Reserve Bank of Chicago has proposed a statewide residential property tax of approximately 1%, which could fully fund the pension debt over the next 30 years and would automatically expire once the debt is paid off.⁸⁸ For example,

⁸⁴ <https://bit.ly/3WF877S>

⁸⁵ <https://bit.ly/3LcRloD>

⁸⁶ <https://bit.ly/3KJG6tk> at 449.

⁸⁷ *Understanding – and Resolving – Illinois' Pension Funding Challenges*, CTAB (2023), see <https://bit.ly/4heCewh>.

⁸⁸ <https://bit.ly/4n4McSc>

under this plan, a homeowner with a home “worth \$250,000 would pay an additional \$2,500 per year in property taxes.”⁸⁹ The rationale is that property taxes provide a broad and stable revenue base, making them uniquely equipped to fund long-term obligations. The Federal Reserve Bank of Chicago finds this proposal to be fair, transparent, and equitable: most homeowners benefit from public services, payments are predictable, and wealthier households contribute more.⁹⁰

Critics, including the Illinois Policy Institute, argue that this proposal would disproportionately affect low-income and minority communities and impose substantial burdens on homeowners.⁹¹ The typical Illinois household could face an additional \$1,948 in property taxes annually.⁹² Communities such as Calumet City and Harvey, predominantly African American communities, would see their tax bills increase significantly. The Illinois Policy Institute further points out that the proposal does not address the root cause of the pension crisis, namely unsustainable benefits, and may exacerbate the housing market challenges by further depressing home values and impeding recovery.

Overall, while the property tax increase presents a measurable path to closing the pension funding gap, careful consideration of equity and market impacts would be necessary in its design and implementation.

III. *Legal and Practical Challenges*

The Pension Protection Clause of the Illinois Constitution prevents reductions to accrued benefits, a rule strictly enforced by the Illinois Supreme Court. While this forecloses most benefit cuts absent constitutional amendment, recent precedent allows structural reforms, such as pension fund consolidation, that improves efficiency without diminishing benefits.

a. Illinois Constitution Pension Protection Clause

The 1970 Constitution of Illinois, Article XIII, Section 5, known as the “Pension Protection Clause,” provides:

Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.

The Pension Protection Clause is an enforceable contractual relationship between public employees and the state or local government. The employee has constitutionally protected rights that “attach at the time an individual begins employment and becomes a member of the public pension system.” *Jones v. Mun. Employees’ Annuity & Ben. Fund*

⁸⁹ *Id.*

⁹⁰ *Id.*

⁹¹ <https://bit.ly/46SikQN>

⁹² *Id.*

of *Chicago*, 50 N.E.3d 596, 603 (2016) (applying *In re Pension Reform Litig.*, 32 N.E.3d 1 (2015)).

b. Calls to Amend the Illinois Constitution

Many have called for the Illinois Constitution to be amended through the General Assembly or a constitutional convention, as the Pension Protection Clause restricts further pension reform in the state. Whatever path to amendment is chosen, it must comply with both the state and federal constitutions, namely, the Contracts Clause, which prohibit the impairment of contracts.⁹³ An amendment or repeal of the Pension Protection Clause would depend on the extent of protection the clause grants before amendment.

Courts have interpreted the clause very stringently. In *In re Pension Reform Litig.*, 32 N.E.3d 1 (2015), the Supreme Court struck down Public Act 98-599 that aimed to curtail retirement annuity benefits in an effort to address the pension crisis. The Court held that even though there might be an economic crisis or when pensions are underfunded, the Illinois Constitution limits the General Assembly's ability to adjust parts of the system that contribute to these underfunded liabilities. Without amendment, as many argue, the proposals that various organizations offer may be legally blocked because of the Pension Protection Clause.

Amendment to the Illinois Constitution can occur in one of two ways: General Assembly or constitutional convention. The General Assembly would have to propose an amendment that requires three-fifths of the members in both chambers to pass. Once passed, the proposed amendment is placed on the ballot for voters to decide. Another way to amend the Illinois Constitution is through a constitutional convention. A question whether to hold a constitutional convention is placed on the ballot every 20 years, or the General Assembly can vote by a three-fifths majority to place the convention on the ballot. Voters must approve the measure for a convention to be called.

If amended, the Illinois Constitution could provide clearer legal authority, avoid constant litigation, and afford more tools to deal with unfunded liabilities. As noted above, several courts have rejected reform attempts that do not involve constitutional amendment. For example, in *Jones*, the Court applied the holding in *In re Pension Reform Litig.*, striking down reforms aimed at reducing pension benefits for city employees, finding that it violated the Pension Protection Clause. In *Matthews v. Chicago Transit Auth.*, 32 N.E.3d 1 (2016), the Court addressed the enforceability of retirees' health benefits under collective bargaining agreements. The Court found that the Pension Protection Clause guaranteed benefits that are provided to retirees under the collective bargaining agreement.⁹⁴ Accordingly, making changes to already-accrued vested benefits, retroactive cuts, or diminishing membership benefits would be found in violation of the constitution based on case law.⁹⁵

⁹³ Ill. Const. art. I, § 16; U.S. Const. art. I, §10.

⁹⁴ *Id.* ¶ 66.

⁹⁵ *In re Pension Reform Litig.*, 32 N.E.3d 1 (2015).

c. Whether Structural or Administrative Reforms Violate the Constitution

Structural or administrative reforms that do not reduce a member's accrued pension benefit might help overcome some of the legal challenges to reform. In 2024, Governor Pritzker scored a win on pension reform in the Illinois Supreme Court. In *Arlington Heights Police Pension Fund v. Pritzker*, 238 N.E.3d 1099, 1102–03 (2024), beneficiaries of local police and firefighter pension funds sued the Governor, challenging the constitutionality of Public Act 101-610 (the "Act").⁹⁶ The Act consolidated "local police and firefighter pension fund assets into two statewide pension investment funds, one for police and the other for firefighters."⁹⁷ The court held that the Act did not violate the Pension Protection Clause because the ability to vote in elections for local pension board members and have local pension board members control and invest pension funds is not a constitutionally protected benefit.⁹⁸ Further, the court stated that:

Plaintiffs do not explain how the payment of the startup costs impairs or diminishes payment of their pension benefits. The Act does not require the borrowing or the spending of any specific amount for the startup or administrative costs of the funds. Additionally, as previously noted, the two new statewide funds are intended to streamline investments and eliminate unnecessary and redundant costs, thereby ensuring that *more money* is available to fund local police and firefighter pension benefits.

Arlington Heights Police Pension Fund, 238 N.E. 3d at 1107.

Accordingly, this 2024 decision paves the way for legislatures to enact reform.

d. Political and Economic Barriers to Reform

Political and economic factors significantly constrain pension reform in Illinois. Public unions wield significant influence over pension reform, specifically opposing a reduction in benefits.⁹⁹ Unions argue that the current pension system makes it difficult to attract and retain employees for these state and local jobs.¹⁰⁰ Beyond direct opposition to benefit cuts, unions can mobilize political campaigns and media pressure, shaping public opinion and legislative outcomes.

Proposals to raise taxes or alter funding also carry the risk of voter backlash, particularly in a state already known for the highest property taxes in the nation.¹⁰¹ Legislators in districts with large numbers of public employees may resist reforms to avoid alienating their constituents. For example, in Chicago, pension reform was passed to align

⁹⁶ *Arlington Heights Police Pension Fund v. Pritzker*, 238 N.E.3d 1099, 1102–03 (2024).

⁹⁷ *Id.*

⁹⁸ *Id.*

⁹⁹ <https://bit.ly/4qbQOsx>

¹⁰⁰ <https://bit.ly/3KPdQpa>

¹⁰¹ <https://bit.ly/4q300PY>

Tier 2 benefits for Chicago’s first responders with the rest of the state. However, Chicago officials warned Governor Pritzker that the plan could cost the city billions of dollars. Despite these concerns, the General Assembly passed the bill, and Governor Pritzker signed it into law.¹⁰²

Economic barriers further complicate reform. Illinois faces a massive unfunded pension liability, limiting flexibility to redirect funds without raising new revenues. Funding reforms often require trade-offs with essential services. Continuing to underfund pensions could negatively impact the state’s credit rating by increasing borrowing costs and discouraging investment.¹⁰³ Additionally, proposals such as tax increases could lead to driving business and residents out of state.¹⁰⁴

Finally, administrative complexities across multiple state and local systems, combined with the potential for litigation even on permissible reforms, make comprehensive pension reform extremely difficult to implement without pushback. Therefore, any path toward meaningful pension reform in Illinois faces steep barriers, with political resistance and economic constraints working in tandem to stall lasting solutions.

¹⁰² <https://bit.ly/3WLhq69>

¹⁰³ <https://bit.ly/4qcVFtu>

¹⁰⁴ <https://bit.ly/48OVsqv>