Tackling Chicago's looming deficit and beyond: Illinois Policy Institute recommendations

Pensions and personnel costs are the No. 1 cost-drivers behind Chicago's billion-dollar budget deficit. The following analysis illustrates the magnitude of these problems and offers solutions to address them.

Pensions fast facts

Total debt in Chicago-controlled funds: $29.2 billion

Chicago pension contributions set to spike twice over next decade
Statutory contributions to the four city pension funds, fiscal years 2018-2028

Fiscal Year	Contribution	Increase over prior year	% increase
2018	$1,024,512,000	$-	
2019	$1,184,000,000	$159,488,000	15.6%
2020	$1,305,000,000	$121,000,000	10.2%
2021	**$1,674,669,000**	**$369,669,000**	**28.3%**
2022	$1,791,164,000	$116,495,000	7.0%
2023	**$2,130,579,000**	**$339,415,000**	**18.9%**
2024	$2,181,157,000	$50,578,000	2.4%
2025	$2,230,954,000	$49,797,000	2.3%
2026	$2,280,318,000	$49,364,000	2.2%
2027	$2,329,760,000	$49,442,000	2.2%
2028	$2,379,844,000	$50,084,000	2.1%

Source: City of Chicago Fiscal Year 2018 Financial Analysis

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Chicago's 2018 Comprehensive Annual Financial Report, or CAFR, and 2018 actuarial reports for police, fire, municipal and laborers retirement funds show significant increases in the city's deficit and pension liabilities:

- Chicago's bond debt totaled $10.2 billion as of Dec. 31, 2018 – $8.2 billion of general obligation bonds and $2 billion of bonds secured by Chicago's share of state sales tax revenue.
- Chicago's actual end of year deficit for 2018 was $438 million. The city's long-term net deficit (liabilities minus assets) saw an increase of nearly $1 billion to $29.4 billion, which reflected a $559 million increase in OPEB liabilities resulting from more accurate GASB reporting requirements.
- Pension debt for the four city funds increased to $29.2 billion from $27.6 billion, while the funding ratio decreased to 25% from 26%.
- The spikes in pension contributions in 2021 and 2023 will be larger than previous reports based on the pension systems' newly released reports: Pension contributions could be $5 million higher in 2021 and $118 million higher in 2023.
- Starting in 2021, the statutory payment to the firefighters' pension fund will equal 79% of payroll and remain constant at that level. Chicago will be paying for almost two full workforces.
- The laborers' retirement fund contribution will be 58% of payroll in 2022 and only gradually decrease to 52% in 2044.
- The police retirement fund contribution will increase to 57% in 2021 and remain constant at that level.
- The municipal employees' retirement fund contribution will increase from 23% of payroll in 2020 to 50% in 2027 and remain at that level until 2059.

Pension solutions

- The only way to save workers' retirements is to adjust the Illinois Constitution's pension clause. We recommend the mayor endorse an amendment to the state constitution to protect earned benefits while slowing the growth in new pension obligations.
- Examples of benefit changes could include: moving retirees from guaranteed compounding post retirement raises to true cost-of-living adjustments tied to inflation; raising retirement ages for younger workers; capping maximum pensionable salaries; and implementing COLA holidays for retirees who have benefited from annual adjustments that far exceeded inflation.
- Pension reform has the potential to net savings in the hundreds of millions of dollars while actually increasing funding targets to 100% from 90%, in line with actuarial best practices. These reforms could help raise the city's credit rating, potentially lowering the cost of debt service for the city on top of reducing contributions.
- Consolidating Chicago's pension funds with downstate funds could also generate significant savings. Fund consolidation could take advantage of economies of scale, eliminate duplicative administrative costs and create greater investment opportunities, according to the Civic Federation.

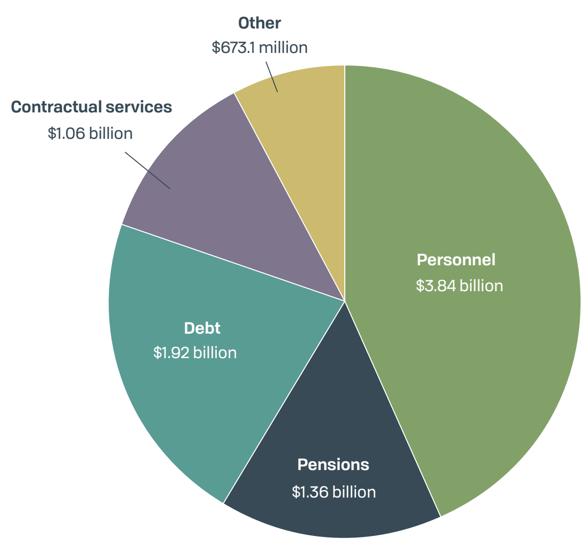
Labor costs fast facts

Personnel expenses cost Chicago nearly $3.9 billion per year

- Personnel-related expenses consume the largest portion of the city's budget. Police and firefighters represent 38.5 percent and 14.6 percent, respectively, of the city's workforce and a majority of its personnel expenses.
    - The Office of Inspector General, or OIG, recommended in its 2017 report that the city and employee unions **consider pay increases tied to CPI** rather than a stated percentage increase. By contrast, the 2012 contract gave police and fire personnel an 11.52% cumulative pay increase over the five-year contract period. In fiscal 2017, Chicago paid $1.964 billion for police and fire personnel. Based on the 11.52% increase, the amount is $203 million higher than at the start. If the CPI increase of 3.75% had been in effect, the net increase would have been $137 million less.

How Chicago is spending local funds in 2019

The city has $8.85 billion available in 2019 from all local sources



Source: City of Chicago 2019 Budget Overview

- Some labor contract provisions negatively affect the city's capacity to innovate and modernize its operations to deliver services more efficiently. Addressing just two of these, duty availability pay and compensatory time buybacks, could save as much as $60 million in just one year of the contract. That could total hundreds of millions of dollars over a five-year contract. Some of the provisions the mayor should address include:
  - **Side letters:** These are amendments outside of the contracts that create ambiguity and undermine transparency. Some of these remain in effect after a contract has expired and can prevent efficient contract enforcement and administration. According to the OIG, there are 42 police and 51 firefighter side letters in their contracts.
  - **A lack of adequate "reopener provisions"** that would allow the city to reopen contract negotiations in the event of a deterioration of the city's finances during an economic downturn.
  - **"Duty availability pay"** for which no specific purpose is stated in contracts but is understood to compensate police and fire personnel because they may be called to duty on their days off. Chicago paid over $56 million in duty availability pay in fiscal year 2016.
  - **"Compensatory time buybacks"** that permit police personnel to accumulate up to 200 hours of compensatory time annually in lieu of overtime during their careers and cash it in upon retirement. Chicago paid out over $23 million in compensatory time buybacks between 2013 and 2017 – $4.6 million per year.
  - **"Holiday on furlough days,"** also known as "Daley days," that consider fire personnel to have worked on a holiday if the holiday occurs during a vacation.
  - **Employees should bear more of their health care costs.** Currently, health insurance premiums paid by city employees are capped at $2,228 annually regardless of salary. By contrast, the national average for employees at private sector firms with more than 200 employees is $4,917.
    - Adopting a cap that aligns with the national average and that would apply to employees with a $90,000 salary and family coverage could save $2,689 for every employee in this category.