

The background of the cover is a photograph of the Illinois State Capitol building, showing the large dome and a statue on a pedestal in the foreground. The image is overlaid with a dark brown semi-transparent rectangle that contains the title text. A white jagged line, resembling a crack or lightning bolt, runs vertically down the right side of the dark rectangle.

4 WAYS TO **BREAK OUT** OF ILLINOIS' PENSION TRAP

January 2026

TABLE OF CONTENTS

Executive Summary.....	1
Introduction.....	3
A pension crisis 50 years in the making.....	5
1970: Madigan and the Illinois constitution.....	5
1989: The compounding COLA.....	6
1994: The Edgar Ramp.....	7
2010: The creation of Tier 2.....	9
2013: Blocked attempts at real reform.....	10
The current status of Illinois' pension systems.....	12
The state's pension crisis.....	12
Chicago's pension crisis.....	14
The suburban and downstate pension crisis.....	15
Enhancing benefits would worsen the trap for retirees and taxpayers.....	19
A comprehensive set of solutions.....	24
1) Maintain the "SSWB Reserve Fund" as a safety net for Tier 2.....	24
2) Give workers in every retirement system pension choice.....	26
3) Offer pension buyouts for downstate employees.....	29
4) Constitutional pension reform.....	29
Conclusion.....	32

EXECUTIVE SUMMARY

Illinois is trapped in the worst pension crisis in the nation. The state's five pension systems carry about \$144 billion in unfunded liabilities. The Reason Foundation reports it is the only state whose systems owe over \$100 billion more than they have on hand. Chicago's fire and police funds are flirting with insolvency. Illinois families pay the highest effective property taxes in the country, with most of those dollars being spent to keep up with overpromised pensions rather than to create better schools, safer streets or improved services.

Illinois can do better for its residents and its public servants.

This crisis did not happen overnight. During the past 50 years, a series of political choices locked Illinois into an unsustainable path. The 1970 Illinois Constitution enshrined a pension protection clause that courts have interpreted to shield not only earned benefits, but also all future benefit accruals from any reduction. The 3% compounding cost of living increase for retirees ensured liabilities grew far faster than taxpayers could keep up with. The 1994 "Edgar ramp" backloaded pension payments, encouraging governors and lawmakers to push costs into the future instead of fixing the underlying problem. Tier 1 benefit sweeteners kept costs rising. And when lawmakers finally attempted modest structural reforms in 2013 that would not have cut a single dollar of already-earned benefits, the Illinois Supreme Court struck them down.

Today, Illinois is left with a government employee retirement system that is both extremely generous for hundreds of thousands of retirees, inflexible for the needs of modern workers and dangerously unstable for everyone it serves. Every new "pension sweetener" piles more risk on top of an already fragile structure.

Advocates for richer Tier 2 benefits argue newer workers are treated unfairly and Illinois pensions may run afoul of federal rules mandating benefits at least match Social Security. But claims about this are currently unfounded because there has been no actuarial analysis at the individual plan level. In fact, evidence shows the real threat to retirement security is not benefit levels: it is the solvency of the systems themselves. Tier 2 already provides a secure retirement that is far more generous than Social Security for full-career workers, often guaranteeing at least two-thirds of final average salary with automatic annual increases. What drags down Illinois' retirement security ratings is an unwillingness to fix Tier 1 and a lack of flexibility for workers who need a different option.

Illinois needs comprehensive reforms that protects what workers have already earned, stabilizes pension finances and gives future employees more choice and flexibility. This report recommends four key steps:

1) Keep the “SSWB Reserve Fund” as a targeted safety net, not a benefit hike.

Rather than adding \$53 billion in new liabilities with benefit enhancements like raising the Tier 2 salary cap across the board, the state should use its new “SSWB Reserve Fund,” created to ensure compliance with federal pension rules, only if there’s a documented case where an individual Tier 2 benefit falls below the Social Security minimum. This “scalpel” approach preserves Tier 2’s savings while ensuring federal compliance.

2) Offer pension choice to all new public employees.

Illinois should extend the successful State Universities Retirement System defined contribution-style plan to employees in all pension systems. A portable, individually owned retirement account would better serve the many modern workers who will not spend 10 to 20 years in a single job, while also preventing new unfunded liabilities from piling up.

3) Expand pension buyouts to local systems downstate and in Chicago.

The state’s existing buyout programs have already reduced liabilities by billions of dollars while giving retirees more flexibility and control over their savings. Extending similar voluntary buyout options to local pension funds would let workers choose a lump sum they can invest or use for pressing needs, while lowering long-term costs for cities, counties and taxpayers.

4) Pass a constitutional amendment to allow future-focused pension reform.

Lasting change is impossible without fixing the pension protection clause of the Illinois Constitution. An amendment that clearly protects all benefits already earned while allowing reasonable adjustments to future benefit growth – such as replacing 3% compounding Tier 1 raises with inflation-indexed increases and lowering the cap on their pensionable salaries – would put Illinois on a realistic path to solvency without cutting any retiree’s current check.

If lawmakers pursue these reforms together, Illinois can finally start paying down its pension debt, protect retirement security for current and future workers, and relieve taxpayers from ever-rising taxes that crowd-out core services. If they do nothing or continue to increase benefits, Illinois will drift closer to pension insolvency, more credit downgrades and a further weakened economy.

INTRODUCTION

Most government workers in Illinois, such as teachers, police officers or sanitation workers, will receive a pension when they retire. State pensions are defined benefit plans, meaning the amount of money you get each month in retirement is based on a standard equation of how long you worked and how much you're paid at the end of your career. It is not linked to how much money you've personally saved or how much money the state has saved.

Private-sector workers usually have a 401(k) plan or some other plan in which the contributions are defined to yield a specific benefit. That allows workers to own their accounts, decide how much to put in and how to invest that money. With a pension, all the money for each worker in the system is combined into one big pool that's managed by the state or local government. Retirees don't have control over the money invested from their paycheck or the money matched by the state while they're working.

In Illinois, public sector pensions are a frequent topic of policy conversation because of the dangerously low funding ratios, high costs to taxpayers and lack of flexibility.

Pensions in Illinois

Illinois has 677 pension funds. Five of them are funded and run by the state government and make up two-thirds of the state's total pension debt. These state-run systems are:

- The General Assembly Retirement System
- State Employees' Retirement System
- State Universities Retirement System
- Teachers' Retirement System
- Judges' Retirement System

In Illinois' largest city, Chicago, there are several other notable pension systems. Four are funded and run by the city itself. These are:

- Municipal Employees' Annuity & Benefit Fund of Chicago
- Laborers' & Retirement Board Employees' Annuity & Benefit Fund
- Policemen's Annuity & Benefit Fund
- Firemen's Annuity & Benefit Fund

Other Chicago area pensions are managed a bit differently, but include:

- Chicago Teachers' Pension Fund
- Chicago Transit Authority Pension Fund
- Chicago Parks Pension Fund
- Metropolitan Water Reclamation District Retirement Fund

The remaining pension funds are for public workers in counties and municipal governments, as well as police and firefighters. Many of these are consolidated into the Illinois Municipal Retirement Fund or are part of the consolidated suburban and downstate police or consolidated suburban and downstate fire funds.

Across the state, Illinois pension funds carry \$493 billion in liabilities. The average funded ratio for these plans is 49%, leaving \$218 billion of those liabilities unfunded.

To put that into perspective, if Illinois paid an extra \$1 million dollars every day to pay down the debt, it would take nearly 600 years to fill the hole.

A PENSION CRISIS 50 YEARS IN THE MAKING

Illinois didn't stumble into this pension crisis. It has been taking slow, deliberate steps toward it for over 50 years. Lawmakers have repeatedly let stability suffer and chosen their own political gain by using short-term "fixes," benefit sweeteners and payment delays that pushed costs onto future taxpayers.

Five major events highlight the problem: the 1970 pension protection clause that locked in benefits and tied lawmakers' hands; the 1989 3% compounding cost-of-living adjustment that allowed benefits to grow faster than taxpayers could reasonably fund; the 1994 "Edgar ramp" that backloaded payments and hid the true cost; the 2010 creation of Tier 2, which slowed the bleeding but can only partially offset Tier 1 excesses; and the attempted 2013 reform that was struck down in court.

These decisions map Illinois' path toward the worst pension crisis in the nation.

1970: Madigan and the Illinois Constitution

There is plenty of blame to go around, but former Speaker of the Illinois House Michael Madigan, now serving time on federal corruption charges, was a major player in leading the state down this path.

Before he was elected to the Illinois House, voters chose Madigan as one of the delegates to the 1970 Illinois Constitutional Convention. That convention was where Illinois' pension crisis was born. Despite warnings against passing the amendment that would handcuff future lawmakers and stymie future reform, a majority of the convention, including Madigan, voted to include Article XIII, Section 5 in the new state constitution.

Known as the "pension protection clause," that section reads:

"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."

Because of this text, which may on its face seem unremarkable, Illinois has some of the most restrictive provisions for reforming pensions in the 50 states. It is one of only eight states that enshrine public pension benefits in its constitution. And Illinois is one of only 11 states that protect future accruals for all participants. This is largely because of how the Illinois Supreme Court has interpreted the law.

The state's courts have reliably struck down nearly all proposed reforms to Illinois' pension system, even modest reforms that would not touch current benefits.

Madigan's legacy on public pensions continued during his time in the Illinois House. He voted for every major bill that would increase Illinois' pension liabilities. In 1989, Madigan was a House sponsor for Senate Bill 95, which passed without an actuarial cost estimate. The bill was the start of 3% compounding benefit increases for retirees in Illinois' pension systems. Unlike a true cost-of-living adjustment, these guaranteed increases are not tied to the general price level or inflation, allowing benefits to quickly rise beyond taxpayers' ability to keep up with them.

1989: The compounding COLA

Some states adjust pensions each year as a way of keeping up with inflation over time. These increases are known as cost-of-living adjustments. Under Gov. Jim Thompson, the cost-of-living adjustment was changed from a simple 3% increase each year to a compounding 3% increase each year. Senate Bill 95 enacting the change was passed without an actuarial cost estimate.

Compared to neighboring states, it was an overly generous boost to benefits. Indiana's state managed hybrid plan does not grant automatic COLAs each year, which means several years can pass without any increase to annual benefits. Michigan employees hired before June 2012 who remained in the defined benefit plan receive an automatic, simple 3% post-retirement increase capped at \$300 annually. Because of the cap, only retirees with pensions of \$10,000 or less receive the full 3%. For example, a retiree making at least \$72,000 per year, which is common in Illinois, would be receiving a simple cost of living adjustment of 0.4%. In Wisconsin, adjustments are made only based on the system funding levels and market conditions, varying from year to year. This risk sharing is part of the reason why Wisconsin's pension system consistently ranks as one of the most well-funded in the country, reporting over 100% funding in 2024.

To make matters worse, inflation was nowhere near 3% in many of the years following the change. That means those 3% increases were more than just cost-of-living adjustments – they were large raises. Prior to the COVID-19 pandemic, these cost-of-living adjustments had outpaced inflation by almost 20%. Even during record-high inflation during COVID-19, these cost-of-living adjustments have still outpaced inflation by 11% since 1990.

In 2013, a presentation by the Commission on Government Forecasting and Accountability attributed a \$1.3 billion increase to the unfunded liability in 1990 because of the compounding 3% cost-of-living adjustment. In 2018, the IMRF estimated it was the cause of 25% of the unfunded liability faced by Illinois' state-funded pension. At the time, that amounted to \$33 billion dollars.

1994: The Edgar Ramp

In 1994, the state already owed about \$15 billion in pension debt. Gov. Jim Edgar and other lawmakers crafted a plan they said would fix Illinois' problems. In the two decades that have followed, it's had just the opposite effect – making problems much worse.

The plan proposed paying down the debt slowly, spread it out over 50 years until 2045. It made no adjustments to the mechanisms of pension plans that were creating the debt but freed up money that should have gone to pensions for other projects that politicians wanted to fund. The plan passed with no opposition.

This ramp enabled other governors to put off the problem even farther – borrowing money, raising taxes and even skipping pension payments altogether. Even though taxpayers have paid billions above what Edgar's plan originally estimated, the pension debt has exploded to \$143.5 billion – nearly 10 times what it was 30 years ago.

That's because a payment plan based on backloading debt was never designed to fix the problem. Forget a Band-aid solution – it was Scotch tape to keep public sector unions happy and make irresponsible spending possible. The wound continued to fester as government workers in their 50s retired with full benefits compounding 3% each year of their remaining lives.

In some cases, such as with the Teachers' Retirement System, the employee wouldn't have to pay any of their salary into the system – twice charging taxpayers to cover these overgenerous retirement benefits.

Taxpayers paid billions more than original ramp projections

Edgar ramp appropriations (1994) vs actual appropriations

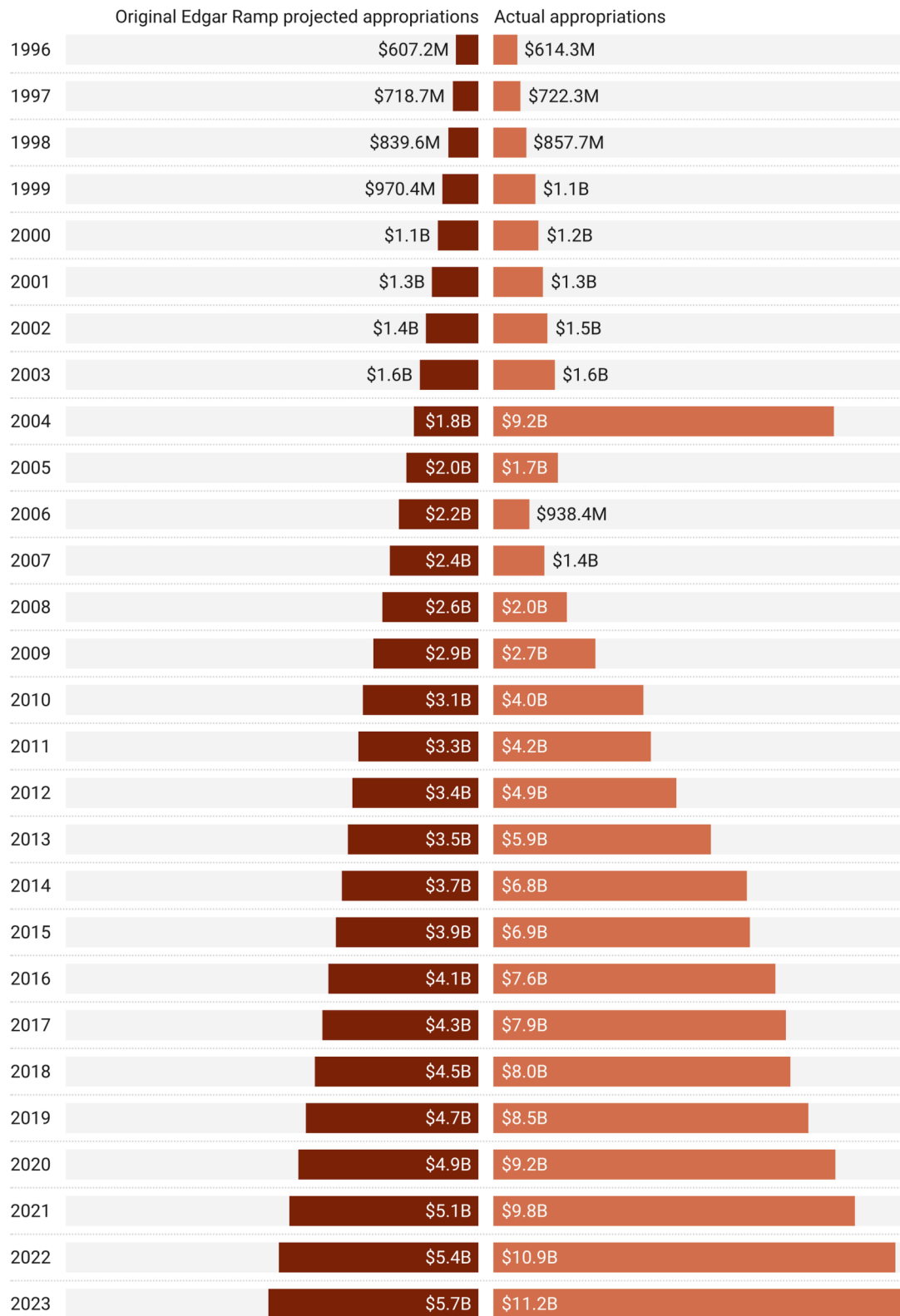


Chart: @illinoispolicy • Source: Commission on Government Forecasting and Accountability • Created with Datawrapper

2010: The creation of Tier 2

To address the growing pension crisis, the Illinois General Assembly created Tier 2 in 2010. This new set of pension benefits applies to state and local government employees hired starting Jan. 1, 2011. Here are the key changes implemented with Tier 2:

1. Increased retirement age: Full benefits are now available at age 67, up from 60 for most Tier 1 employees.
2. Reduced final average salary calculation: Changed from the highest four of the final 10 years to the highest eight of the final 10 years of service.
3. Imposed a limit on pensionable earnings: Initially set at \$106,800 in 2011.
4. Changed annual benefit increases: From 3% compounded for most Tier 1 employees to the lesser of 3% or one-half of the increase in the Consumer Price Index, non-compounded, for Tier 2.

The creation of Tier 2 was a positive reform, projected to save the state billions over time by significantly slowing the growth of pension liabilities. It doesn't put Illinois in the clear when it comes to pension debt. There are still far more employees in Tier 1 than most people realize, and the ability for Illinois' pension systems to survive ballooning Tier 1 benefits for that long is unlikely.

The Teachers' Retirement System, the largest of Illinois' five statewide pension systems, highlights the problem. Out of the 142,390 full-time and regular part-time active TRS employees, about 64% are in Tier 1. Many of them are nowhere near retirement: more than 35,000 are under age 45.

Tier 2 only applied to workers hired after Jan. 1, 2011. So, if a teacher was hired in 2010 at age 22, that person is a Tier 1 member. They could remain in TRS until 2045, working for 35 years, or could delay their retirement even later to accrue more benefits.

When they do retire, they will collect a Tier 1 pension with a 3% compounding annual cost-of-living adjustment until they die. Given Illinois' average life expectancy of 77, that could mean collecting benefits until 2065 – 20 years of Tier 1-level pension payments covered by Tier 2 workers and taxpayers. And the payments could extend far longer because many people will live decades past 77, and life expectancies have historically risen.

Tier 1 payments to rise faster than retiree benefits will drop

While benefit payments for those currently in retirement will drop about \$3 billion dollars from 2026 to 2046, benefit payments to those currently active in Tier 1 will increase by \$9 billion in the same period.

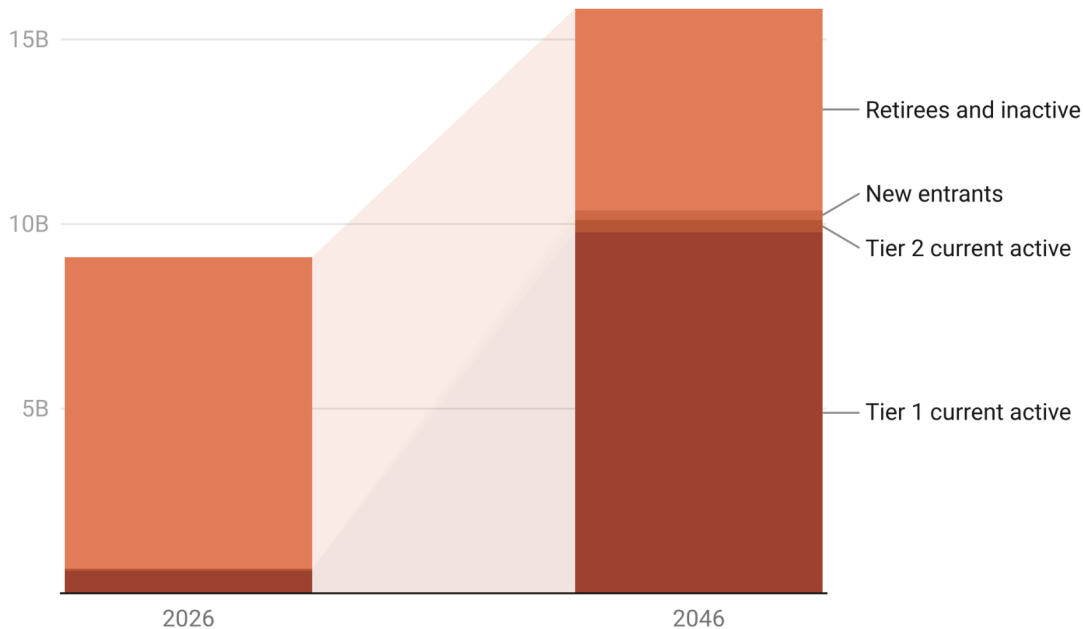


Chart: @illinoispolicy • Source: Teachers' Retirement System of the State of Illinois • Created with Datawrapper

Dozens of TRS retirees made over \$300,000 a year in 2024 retirement benefits and the average state retiree made \$93,558. The number of Tier 1 employees still actively accruing benefits means those numbers won't be going down anytime soon.

2013: Blocked attempts at real reform

In 2013, Illinois lawmakers tried to take action to reduce the real culprit: the future growth in Tier 1 benefits. Public Act 98-0599 would have made several modest changes to future benefit increases as well as increased funding guarantees without reducing any earned benefits for retirees or current workers.

First, the bill required the state to target 100% funding by 2044. Under current law, even if every assumption works perfectly, the state's pension system will never be fully funded, despite massive projected contributions. Current law only targets 90% funding by 2045, a violation of sound actuarial principles.

Perhaps the most important aspect of the 2013 reforms is they would have had a dramatic and positive impact on the state's finances. According to actuarial projections at the time, SURS would have reached full funding by 2037 while TRS, SERS and GARS would have all reached full funding by 2039. The state would have seen its unfunded liabilities decrease by \$23.7 billion in fiscal year 2015 and its fiscal year 2016 contribution reduced by \$1.2 billion. Through 2045, the state would have saved \$144.9 billion in contributions – enough to cover the state-managed pension debt.

All of this would have been achieved without reducing the pension payment to any current retiree or reducing the amount already earned and promised to any current worker. Future benefit changes focused on three key areas:

- Gradually increasing the retirement age for current state workers under the age of 45
- Capping the maximum pensionable salary, with future growth in the cap pegged to inflation
- Eliminating 3% guaranteed, compounding post-retirement increases in favor of a simple cost-of-living adjustment tied to inflation

It also included cost-of-living adjustment “holidays” to bring benefits back in line with inflation after decades of compounded 3% raises. This would not have decreased benefits, but would have resulted in multiple years during which, depending on age, a participant might not receive any cost-of-living adjustment to benefits.

Under PA 98-0599, pension costs as a percentage of general fund expenditures would have fallen below 2% of annual expenditures by 2040, with total pension costs falling below \$1 billion annually for the first time since 1998, according to actuarial projections at the time.

Unfortunately, the Illinois Supreme Court ruled in 2015 the pension protection clause of the state constitution protects not only earned benefits, but all potential future benefits as of the date an employee is hired by the state, striking down the 2013 reforms in their entirety. This restrictive interpretation has made even modest pension reforms difficult absent a constitutional amendment.

Lawmakers certainly could have foreseen the possibility of a court challenge and subsequent defeat of the reform. Had politicians included a constitutional amendment with their reform bill in the first place, they could have prevented a judicial setback. As it stands today, lawmakers have delayed action and allowed the pension problem to worsen significantly.

THE STATUS OF ILLINOIS' PENSION SYSTEMS

Today, Illinois has the worst pension crisis in the nation. No matter which way you slice it, Illinois' public-sector retirees are not set up for success in retirement and taxpayers are being overburdened by a debt that only continues to grow. The bulk of it is concentrated at the state level and within the city of Chicago, but other municipalities and counties are starting to feel the weight of how big the debts have grown.

The state's pension crisis

Illinois' five state-run pension systems are in serious financial trouble. Together, they owe about \$275 billion in promised retirement benefits but only have about \$131 billion on hand to pay for them. That means the state only has 47 cents on hand for every dollar of benefits that it owes to these employees when they retire. The national average is estimated to be 81 cents on hand for every dollar owed. Experts say when a fund has less than 60 cents on hand for every dollar owed, it's considered to be in real trouble. Less than 40 cents on hand indicates the fund may never recover.

Illinois' state pension debt nearing all-time high

Pension debt for five statewide public employee pension systems, 1999-2025.

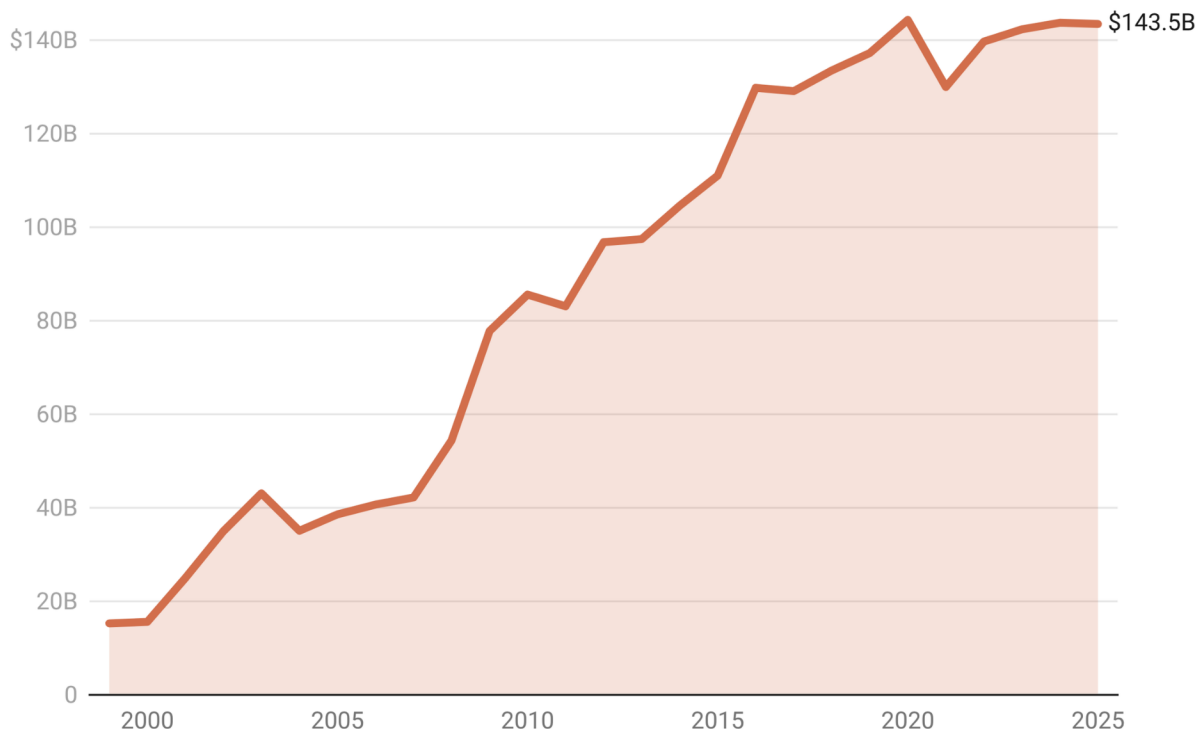


Chart: @illinoispolicy • Source: Illinois General Assembly Commission on Government Forecasting and Accountability special pension reports • Created with Datawrapper

That means Illinois has \$144 billion dollars in pension obligations it doesn't currently have the money to pay out. The Reason Foundation [reports](#) that, across the country, only Illinois has more than \$100 billion in state-managed pension debt, with California in second place at \$90 billion in unfunded pension debt for its state-managed plans. Illinois also has the highest pension debt per capita at \$11,355 per person from state-level liabilities.

If those numbers are too big to imagine, picture this: if you sold every NBA team, the state would still not have enough money to pay off its pension debt. Or if the state put another \$1 million a day towards the pension debt, it would take almost 600 years to satisfy it.

But money on hand for retirees isn't the only problem Illinois has to worry about. When looking at pension debt compared to the size of each state's economy, Illinois has the highest ratio in the nation. Its total pension debt equals nearly 20% of the state's economy. The next worst is Mississippi at 16%. Most other states are below 10%.

Illinois No. 1 for public pension debt as share of state GDP

State unfunded government pension liabilities as a percentage of gross domestic product versus funding ratios for end of fiscal year 2024

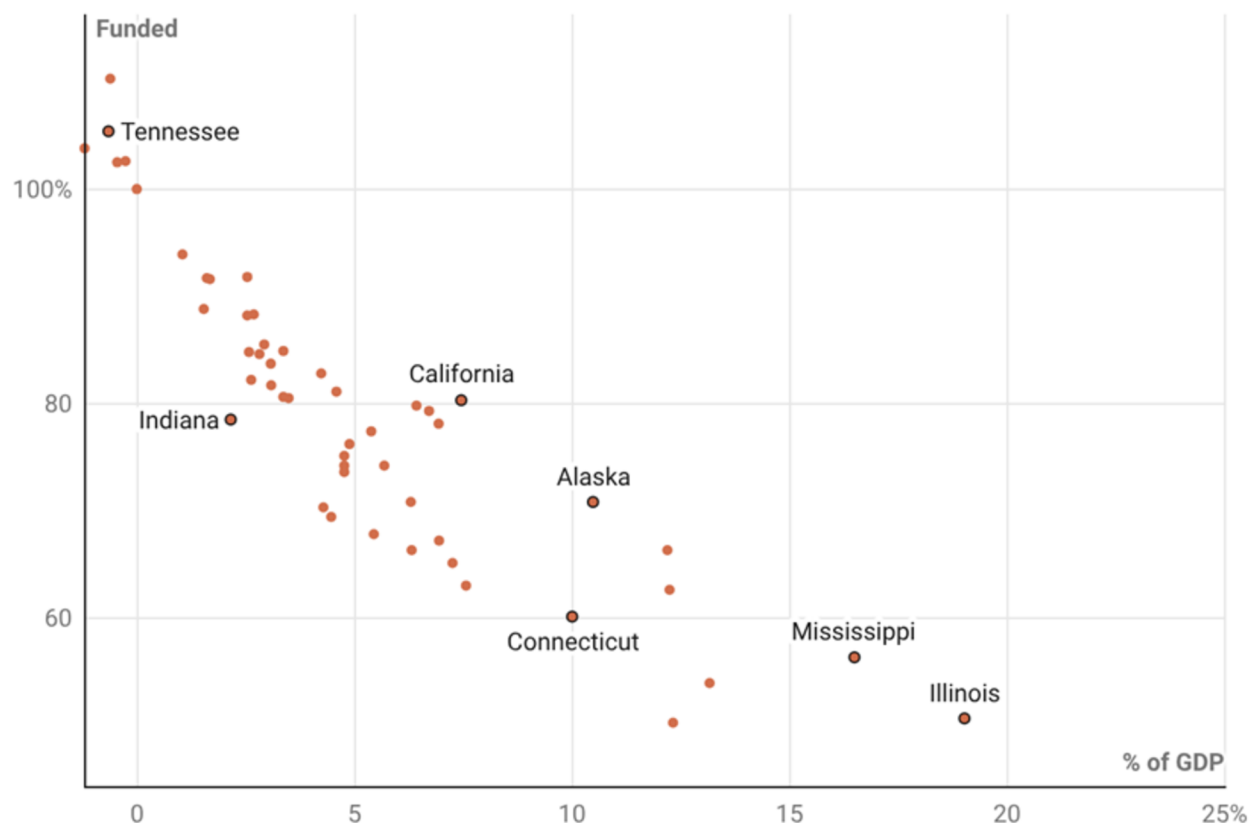


Chart: @illinoispolicy • Source: Equable Institute • Created with Datawrapper

To put it another way, think about a family earning \$50,000. They will have a much harder time paying off \$10,000 in credit card debt (20% of their income) than \$5,000 (10%). The same idea applies to Illinois. When a state takes on more debt as a share of the money they're making, it can quickly spiral out of control.

Three of Illinois' five state-run pension systems –TRS, JRS and SERS – are consistently ranked among the 10 worst-funded pension plans in the country, according to the Equable Institute. That report didn't include the General Assembly Retirement System because it's smaller than \$1 billion in assets. If it had, GARS would have joined the list as third worst in the U.S.

Chicago's pension crisis

Some of Chicago's pensions are doing even worse. Chicago's pension systems remain among the most poorly funded government retirement systems in the country. In 2023, the unfunded debt from just the city's municipal, laborers, police, fire and teachers' pension funds surpassed the pension debt of 43 states. In 2024, it climbed even higher to surpass the pension debt of 44 states.

Chicago's public pension debt bigger than 44 states

Unfunded state, local pension liabilities by state as of Dec. 31, 2024.

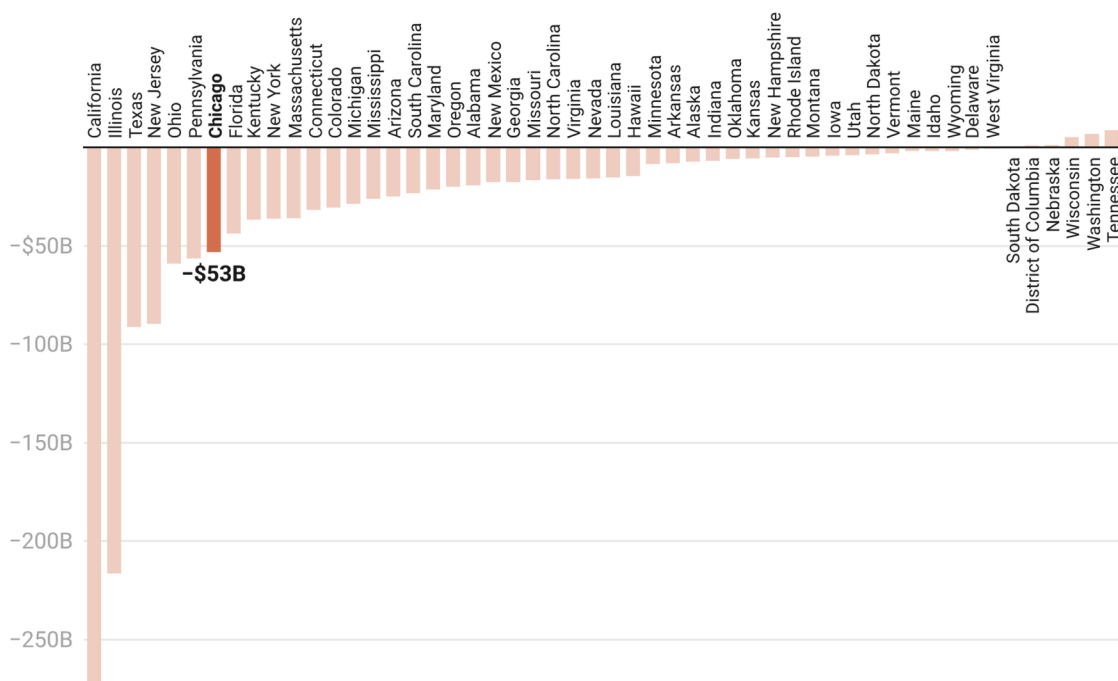


Chart: @illinoispolicy • Source: Equable Institute, 2025 State of Pensions • Created with Datawrapper

Data from the Equable Institute shows those five pension systems carry about \$53 billion in unfunded liabilities.

More than 80% of the city's property tax levy goes to pensions. Nearly all the increase in property taxes since 2014 has been consumed by the cost of keeping up with rising benefits.

Chicago businesses already pay the highest property taxes of any major city, two times the average of other U.S. cities. Residents contribute some of the highest residential rates nationwide.

Seven Chicago-area pension funds occupy spots among the 10 worst-funded local pension plans in the nation.

Yet lawmakers continue to dig Chicago's pension hole even deeper. In October 2025, the state passed a police and fire pension sweetener that adds \$11 billion in new liabilities, despite warnings from the mayor's office. Some estimates say these benefits have dropped the funding ratio for Chicago police and fire pensions to 18%.

In mid-September, Mayor Brandon Johnson had to dip into the city's cash reserves to cover \$28 million in payments for the fire pension so they wouldn't have to sell off assets.

All of that adds up to a city that must grapple with the realities of pension system insolvency.

The suburban and downstate pension crisis

In 2024, police and fire pensions outside of Chicago reported combined unfunded liabilities of \$34.7 billion.

That's not because taxpayers aren't paying their fair share. For example, municipal fire departments increased property taxes by \$371.6 million between 1996 and 2023, adjusted for inflation. While the total tripled, pensions have gone from taking less than half of the property taxes to taking nearly three-fourths: \$311.6 million more in 2023 than in 1996.

Actual fire protection operated on only \$60 million more than it did in 1996.

Local Illinois fire pensions take cash from protection

Municipal fire department property tax levies, 1996-2023, adjusted for inflation

■ Fire protection ■ Firefighter pensions

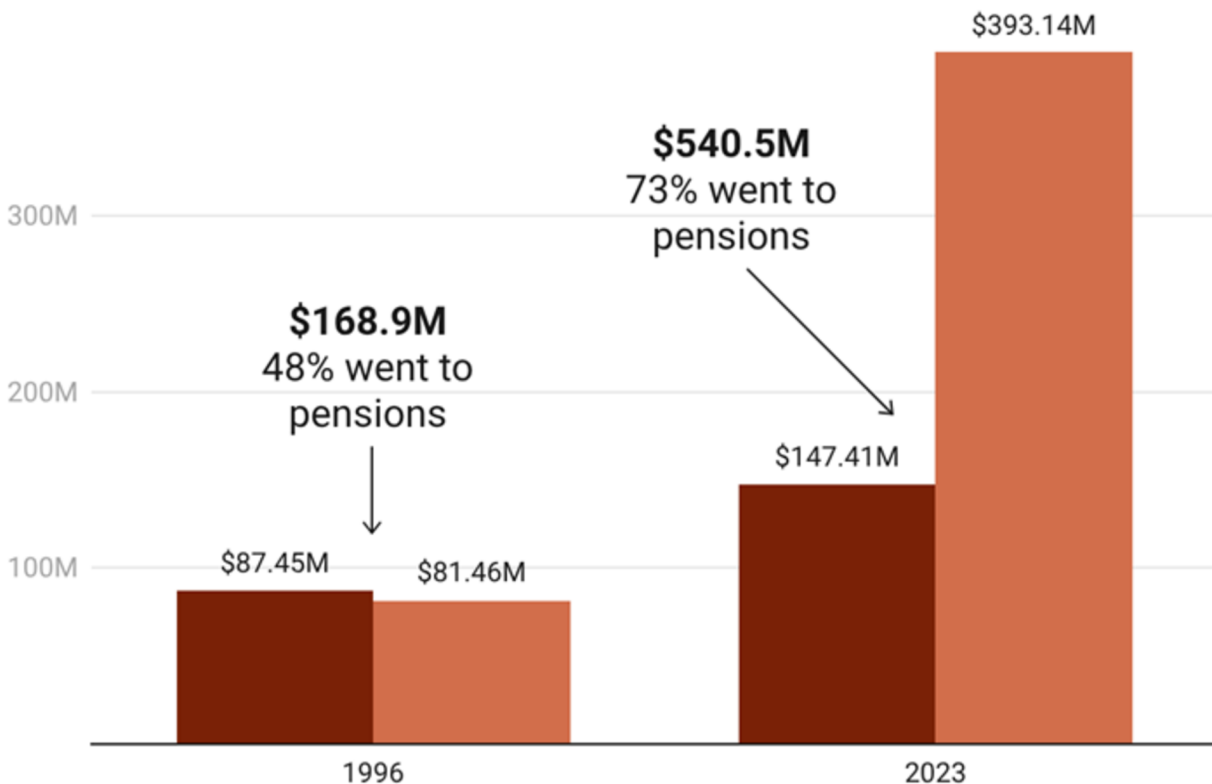


Chart: @illinoispolicy • Source: Illinois Department of Revenue • Created with Datawrapper

Illinoisans already pay the highest effective property taxes in the nation at 1.83%. But in some areas it's even worse. Lake County is a perfect example: The effective property tax rate is 2.68%. That's the highest in Illinois and ranks No. 9 nationwide.

Higher property taxes should lead to better-funded services, but that's not how things have played out. While the money going toward fire pensions in Lake County has grown by \$20.4 million, the amount going to services has dropped by \$3.3 million. The county sees 83% of property tax revenues collected for firefighters going toward their retirements rather than their work. Less than 30 years ago, it was only 38% of property tax revenues.

A similar issue persists with local police departments.

In St. Clair and DuPage counties, the effective property tax is 2.09% – among the highest rates in the state.

While the money going toward police pensions in St. Clair County has grown by \$8.9 million, the amount going toward services has only grown \$326,000. In DuPage County, \$53.8 million has gone to police pensions while only \$700,400 has gone to police services.

That's 99% of property tax revenues collected for police officers going toward retirements rather than the day-to-day work of protecting the community.

Illinois police pensions take cash from protection

Municipal police department property tax levies, 1996-2023, adjusted for inflation

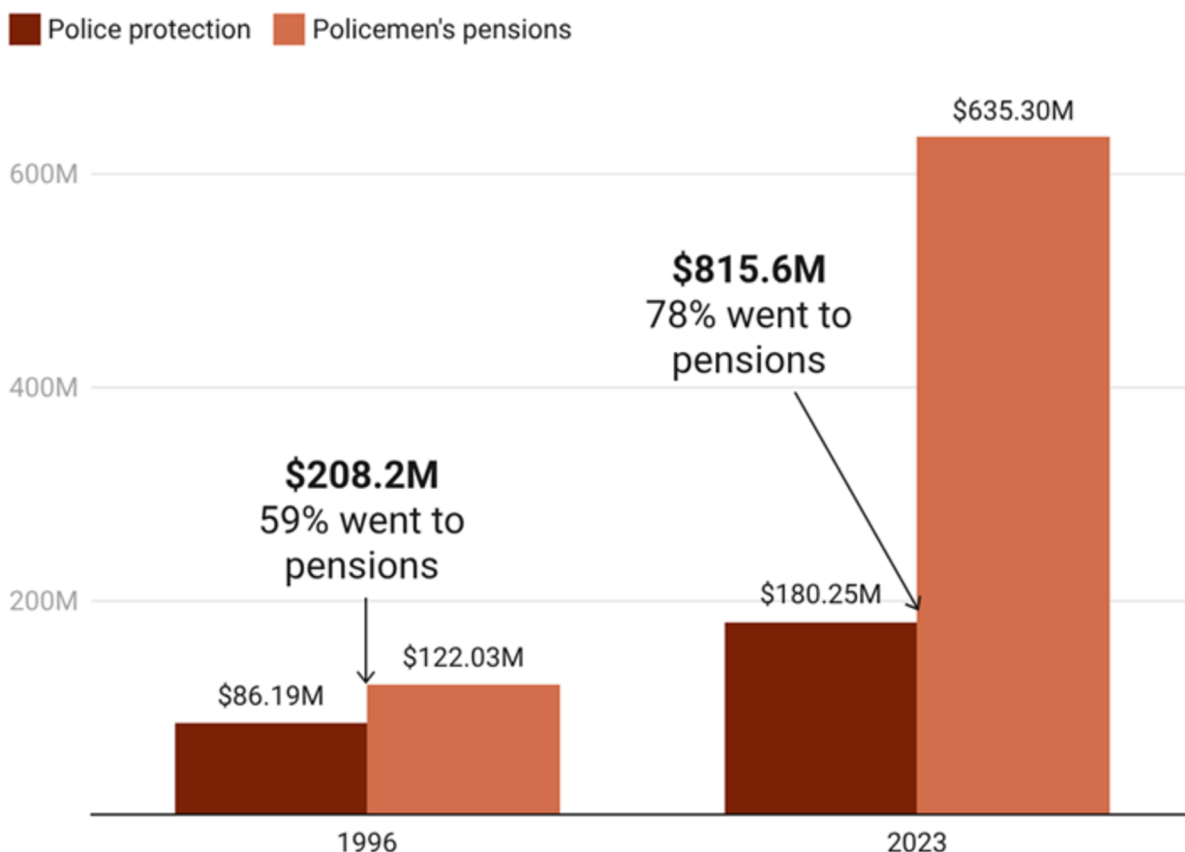


Chart: @illinoispolicy • Source: Illinois Department of Revenue • Created with Datawrapper

Illinois residents are paying more than ever while services receive less funding. That means less investment in the police officers and firefighters keeping the public safe and less training and equipment to keep them safe.

This setup makes bankruptcy nearly inevitable. The city of Harvey provides a cautionary tale.

Between 2016 and 2018, Harvey defaulted multiple times on debt service payments and remained in default until August 2023. As of April 2020, the city's police pension was a little over 53% funded, and as of April 2021, the firefighter pension fund was only 18% funded.

The city's annual budget for fiscal year 2021-2022, the most recent year available, appropriated almost one-fifth to police and fire pension payments and debt service. Those expenditures made up nearly half of their 2021 municipal property tax levy.

After years of financial mismanagement and missed contributions to both its police and fire pension funds, the Harvey Police Pension Fund won a \$7 million judgment against the city in 2017 through the state's pension intercept law.

Even after the city laid off 40 police and fire employees, Harvey had to negotiate with both pension funds as well as the Illinois Municipal Retirement Fund to access a portion of its tax revenues – just to meet payroll. They're over \$164 million dollars in debt.

In Illinois, municipalities can't file for bankruptcy, so Harvey did the only thing it could: in October 2025, the city unanimously approved the first step toward seeking state aid under Illinois' Financially Distressed City Law. They have had to partially shut down services and furlough over 40% of the city's workers.

Without reforms, this fate will eventually take more and more Illinois cities. It could happen to Chicago. It could happen to the whole state.

ENHANCING BENEFITS WOULD WORSEN THE TRAP FOR RETREES AND TAXPAYERS

Despite the crisis facing both individual cities and the entire state of Illinois, lawmakers have continued to propose increasing benefits. They argue the real problem with Illinois pensions is the lack of parity between Tier 1 and Tier 2 workers, and that solutions are needed to bring fairness to the system.

That's the wrong approach for two reasons:

1. **The biggest threat to retirement security** is the poor funding of these systems, not the benefits they provide
2. For long-term workers, **Tier 2 benefits are already generous**

The biggest threat to retirement security

A recent Bellwether Education Partners report gave an "F" ranking to Illinois pensions for long-term teachers and some government unions have latched on to it as proof retirements for those hired after 2010 need to be reformed.

But the biggest drag on retirement security – for both Tier 2 and Tier 1 workers – has nothing to do with benefits, but rather the fiscal instability of the whole system.

The only benefit factors included in Bellwether's analysis for long-term employees were the cost-of-living adjustment structure, how it measured up to inflation and the plan's adequacy at retirement. By having an automatic cost-of-living adjustment, Illinois received a full five points. Illinois received 4 out of 5 points for its annual cost of living adjustment. And Bellwether confirmed retirees could expect to replace 70.1% of their salaries at retirement, meeting the 70% metric commonly set to determine retirement benefit adequacy.

Why the "F" grade? Because the other four metrics they analyzed for the importance to long-term employees are in the hands of the state. The state's 10-year average investment returns of 8.3% earned it four out of five points. From there, the rankings tank. The state's funding schedule – the Edgar Ramp – only pays 74% of what's actuarially recommended, earning only two points. Unsurprisingly, the system's funding level earned it zero points and the amortization costs of 34.3% – which is also a measure of taxpayer strain – also earned zero points.

Other reports have pointed to similar concerns with Illinois' system. The Equable Institute, which separates out the value of benefits from the stability of the system, labeled the Teachers' Retirement System "possibly distressed," scoring it only 11 out of 27 points for solvency. The system received zero points for its ability to pay bills and manage tough times, and the plan is not estimated to be fully funded for at least 20 years in the best-case scenario.

The best way to improve these rankings and the outlook for full-career employees is to improve the plan's funding ratios and avoid returning to the disastrous Tier 1 model, where benefits outpaced the state's ability to pay. Inflating Tier 2 benefits risks collapsing the system.

Tier 1 retirement benefits are the biggest threat to Tier 2 retirement security.

The average career state pensioner in Illinois was paid \$93,558 in public retirement benefits during 2024, collecting \$24,538 more from Illinois' debt-riddled pension systems than the \$69,020 the average Illinoisan earned working. On average, these Tier 1 retired state employees will collect \$2.48 million in lifetime benefits.

That's four times as much as the \$609,230 the average American has saved by their retirement age, according to the most recent data. They only collected \$22,344 a year in Social Security retirement benefits.

Nearly 32,000 Illinois pensioners made over \$100,000 a year in their retirement in 2024 – 13% of all annuitants that year. If the average private-sector retiree tried to pay themselves that much, they'd be out of money in six years. Over 300 received over \$250,000 in retirement, putting them in the top 5% of income earners in the state.

Despite these huge benefits, Tier 1 workers contribute very little compared to what they receive. Looking at Illinois' five statewide retirement systems, most get \$19 in benefits for every \$1 they put in. The majority of Illinois school districts report covering some or all of their teachers' pension contributions, according to data with the Illinois State Board of Education. Of the 886 districts with data available, 491 (55%) cover 9 to 10.4% of their teacher's pension obligation, meaning these teachers make no contribution at all from their salary.

Tier 2 benefits are already generous

Public sector unions have been adamant that Tier 2 is unfair because it doesn't match the overpromised benefits of Tier 1. They have latched on to a “Safe Harbor” argument, claiming that Tier 2 benefits violate federal laws that say pensions have to be at least as generous as Social Security. Because the cap on pensionable earnings is below what the Social Security wage base is, they claim that to be the case.

However, this argument lacks crucial nuance about the difference between Social Security and Illinois pensions. Illinois pension benefits don't need to use the same cap as Social Security because they have more generous calculations.

For workers who have dedicated their lives to public service and earn below those caps, the structure of Tier 2 still provides a much stronger retirement package than Social Security.

For employees with 30 years of service, Tier 2 guarantees a minimum of 66% of their final average salary for life, with the annual pension payment growing annually. Based on the salary cap of \$127,283 for fiscal year 2026, this would amount to \$84,007.

That is nearly two times the maximum Social Security benefit of \$50,484 for an employee retiring at 67, and the maximum benefit would only apply to someone who had earned at or above the Social Security wage base for 35 years. In other words, very few people retiring on Social Security are in line to receive the maximum amount. In fact the average as of January 2025 is only \$23,712.

The Tier 2 system also directly links retirement benefits to an employee's average salary during the eight highest-earning years of the final 10 years of working. Typically that makes those benefits more generous than Social Security, which factors in 35 years' worth of a worker's earnings to calculate benefits. A state employee is virtually guaranteed to earn higher benefits under Tier 2 than under Social Security.

Almost all of Illinois' retirement plans got near perfect scores for long-term workers in the Equable Institute's Retirement Security Report, which analyzed 1,954 plans in 50 states on 11 metrics. Long-term workers were defined as those with at least 20 years before reaching retirement age.

Illinois' Tier 2 grants larger max payouts than Social Security

Illinois' Tier 2 pensions for state workers hired since 2010 have an annual benefits cap of \$84,007 compared to \$50,484 for Social Security.

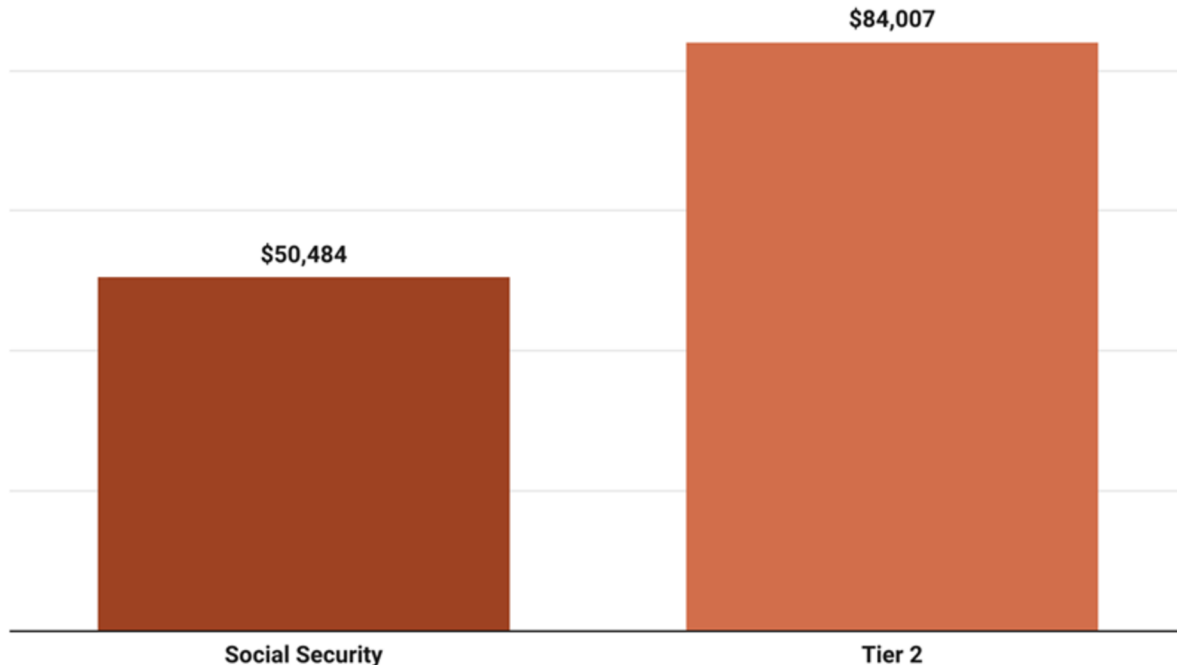


Chart: @illinoispolicy • Source: Illinois State University Retirement System • Created with Datawrapper

Equable's analysis, based on pension pay as a percentage of working wages and cost-of-living adjustments along with other factors, indicates Tier 2 provides these workers with an adequate retirement benefit. Tier 2 earns a perfect score on income replacement, with most full-career employees meeting or exceeding the 70% of working-years' salary commonly seen as adequate retirement income. The cost-of-living adjustment, which is automatic and linked to inflation, earns a solid score of 4 out of 5 points.

Pensioners should prioritize solvency; it's the only way they're guaranteed any benefits

The Illinois Constitution's freeze on benefit changes can leave public pensioners feeling temporarily secure in their retirement funds. However, insolvency would eradicate that safety, exposing retirees and taxpayers to ugly options.

In short, if the money runs out, pensioners are out of luck.

It is highly unlikely a court would be able to force a city or state to make pension benefit payouts if there is not enough money in the pension fund to cover them. That would leave pensioners with massive benefit reductions based on whatever money is left.

For that reason, keeping pensions solvent should be the top priority for those interested in protecting public service worker retirements.

A COMPREHENSIVE SET OF SOLUTIONS

Retirements for public sector workers in Illinois don't need to remain this way. The Illinois Policy Institute recommends lawmakers consider these four policies for holistic reform:

1. **Maintain the "SSWB Reserve Fund" as a safety net** for Tier 2 employees to prevent more debt being added because of pension sweeteners.
2. **Give workers in every retirement system pension choice**, so new employees can pick a retirement plan that will work best for their goals.
3. **Offer pension buyouts for downstate employees** who would like a lump sum payment – adding flexibility and saving more money for the state and municipalities.
4. **Pursue constitutional pension reform** to enable modest reforms to not-yet acquired benefits, as has been successfully done in other states.

1) Maintain the "SSWB Reserve Fund" as a safety net for Tier 2

In recent years, public-sector unions have been pushing for the state to add \$64.5 billion to its pension debt with bills that would boost Tier 2 pensions and let workers retire earlier. Their main argument has been that Tier 2 pensions violate federal laws because they are less generous than Tier 1 pensions. Not only is that suggestion unfounded without an actuarial analysis of individual plans, but the only benefit enhancement in this package that addresses a potential federal pension law violation is raising the pensionable salary cap. Additionally, raising the cap would only impact the highest paid workers, or those making over \$127,283 a year in fiscal year 2026. A higher cap would not help younger, lower-paid workers at all.

However, as an added precaution, state lawmakers at the end of the 104th General Assembly inserted the "SSWB Reserve Fund" into House Bill 1075, the massive "Budget Implementation Act." By avoiding pressure to undo the cost savings of Tier 2 benefits, state lawmakers succeeded in limiting the federal threat and the costs.

But the threat is not over.

Gov. J.B. Pritzker's press release describes the fund as setting aside \$75 million "to cover the estimated first-year costs of adjusting SSWB for State Tier 2 members until legislation is enacted."

The Social Security Wage Base is the maximum earnings on which you are taxed, \$184,500 as of 2026. It is also a limit on the benefits – someone making \$500,000 will get no more from Social Security than the person making \$184,500. The cap on earnings used to calculate Social Security and earnings used to calculate an Illinois Tier 2 pension were the same in 2011. But the pensionable salary cap today is \$127,283 – a high figure but much lower than the Social Security Wage Base, creating a gap.

This gap has become a growing concern because it creates the possibility a retiree's benefits could violate the federal laws that guarantee pensions will not fall below the Social Security benefits. One proposed solution to this problem has been to raise the salary cap to be the same as Social Security. The new state "SSWB Fund" seems to be intended to hold the money needed to make that adjustment.

The language also specifies how much of the fund should go to each of the state's pension systems if an adjustment is made. This would total more than \$13 billion in additional benefits by 2045.

But legislation that adjusts the final average salary has not been passed and does not need to be.

The language included in the budget stipulates if an individual's Tier 2 benefit is ever found to be below what they should have received if they were on Social Security, this reserve fund can cover the difference. Fixing a federal pension law violation doesn't mean raising the pensionable salary to match the Social Security wage base. It just means paying them the equivalent of what they should receive on Social Security when a violation is found.

This solution would prevent the state from paying Social Security payroll taxes or system-wide benefit spikes if a problem is found. It would also save taxpayer money from being prematurely spent or unnecessarily hoarded in the fund.

That means the best way forward is legislative restraint.

If lawmakers leave Tier 2 alone, Illinois pensions continue as designed and the reserve fund remains untapped until a real violation emerges. Should one arise, only the affected worker's annuity is corrected, sparing taxpayers from across-the-board benefit hikes.

By paying only when needed instead of boosting everyone's benefits because there might be a problem, the reserve fund preserves Tier 2's savings and avoids adding billions in new debt. It also means Illinois would not need to spend \$75 million this year and \$13 billion through 2045. An actuarial analysis that examines retirements on an individual basis should be conducted to determine how much is truly needed for the "SSWB Fund."

Preventing new costs is critical. The fund answers federal worries without inflating benefits unrelated to that issue.

2) Give workers in every retirement system pension choice

Despite claims that Tier 2 is a bad retirement plan, research shows it actually works well for long-term employees. However, medium-term workers with 10-20 years of service and short-term workers with less than 10 years are underserved. Increasing Tier 2's benefits won't solve that problem.

Neither the Tier 1 nor Tier 2 retirement systems serve short- and medium-term workers well. This is because traditional defined benefit pensions were designed for employees who stay in a job for decades. Retirement age, final average salary calculations and cost-of-living adjustments have less impact for short- and medium-term workers. Those who leave before 20 years of service also get little to no benefit because vesting requirements are eight to 10 years and you can't draw benefits before age 67 without a reduction in benefits. Additionally, pension contributions aren't held in individual retirement accounts, making them difficult to transfer to a new job.

Increasing benefits doesn't help people who never become eligible to collect them.

Instead, Illinois should offer defined contribution plans, similar to 401(k) systems in the private sector, as an option to all state employees. Defined contribution plans offer more mobility and flexibility for the modern workforce.

Wage and salary workers in the public sector today have a median tenure of 6.2 years. And that number is likely skewed because 3-in-4 government workers are aged 35 and older. Younger workers tend to stay in jobs for shorter periods. Across the public and private sectors, the median tenure of workers 55 to 64 is 9.6 years and 2.7 years for workers 25 to 34.

While public-sector workers do stay in their positions for longer than private-sector employees, turnover remains high, as is evidenced by the data on median tenure. Potential Illinois pension benefits may be generous, but only a fraction of newer public-sector workers will receive them because of steep eligibility requirements. Many will leave with nothing but a refund of their contributions.

Short- and medium-term workers need flexibility and mobility – both incompatible with a defined benefit pension. Illinois should offer defined contribution plans as an option for all government workers.

Illinois already has a proven alternative to traditional, defined-benefit pension plans operating successfully under the State Universities Retirement System for nearly 30 years. Since 1998, the Retirement Savings Plan, formerly called the Self-Managed Plan, has offered university employees within the SURS pension system greater control over their retirements, functioning similarly to private-sector 401(k) plans while maintaining the security of state-backed retirement benefits. It was created to give employees more choice when it comes to their retirement savings.

The mechanics of the plan are straightforward: employees contribute 8% of their paycheck, which the state matches with an additional 7.6%. These contributions are guaranteed – the state can't defer its obligations as it often does with pension payments, and employees must maintain consistent contributions.

This creates a reliable foundation for retirement planning that nearly 20% of newly hired university workers have chosen to embrace each year for the past five years. Participation is estimated to increase to nearly 30% in the future.

There's no reason to limit this option to only employees under the SURS pension system. Illinois should expand this plan to all five of its state pension systems as a new "flexible choice plan" that employees can pick for more control over their retirement finances. Similar plans have been enacted in Rhode Island and Tennessee, which has one of the best-funded pension systems in the country. A defined contribution plan offers more freedom and security for retirees, even in the face of shaky state finances.

State employees and taxpayers could benefit from the change.

Providing all these workers the freedom to join a similar defined contribution retirement plan would make pensions more secure for them and could help address some of the state's crippling fiscal problems.

What makes a retirement savings plan particularly attractive is its flexibility combined with built-in safeguards. While employees gain the freedom to manage their investments through established providers such as TIAA and Fidelity Investments, they also retain protections not typically found in private-sector plans. They can't borrow against their accounts or skip contributions, ensuring the funds remain dedicated to their intended purpose: a secure retirement.

Another key benefit is transparency. With a self-managed plan, employees can see exactly how much money they have saved, track their investment performance in real time and adjust their strategy as needed. This level of visibility stands in stark contrast to the traditional pension system, where benefits can seem abstract until retirement.

They also have lower vesting requirements. Someone wanting to retire at age 62 with a traditional Tier 2 plan would need to have 10 or more years of service. That same person on the Retirement Savings Plan would only need five years of service to retain their contributions, employer match and investment returns. If they were on a defined benefits plan, they'd only be eligible for a reimbursement of their contributions.

There are nearly 30,000 inactive Chicago teachers ineligible for a pension because they left after less than 10 years. Neighboring states have supported their teachers by implementing defined contribution plans with lower vesting requirements to attract more talent. For example, Michigan Public Schools implemented a defined contribution plan for employees hired on or after Feb. 1, 2018, with vesting at 50% after two years, 75% after three years and 100% after four years. Indiana offers a graded vesting schedule of 20% per year over five years.

Implementing something similar would help Illinois compete with them and attract the teachers it desperately needs.

For employees concerned about the state's ability to meet its pension obligations, a self-managed plan offers peace of mind. Unlike pension benefits that depend on future state funding, these retirement funds are secured in individual accounts that the state must fund with each paycheck. This guaranteed funding mechanism ensures promised benefits are delivered, providing a level of certainty that increasingly matters to public-sector workers.

Defined contribution plans can benefit both taxpayers and employees. The benefits are paid within the retiree's account during their career. Costs to the state are set and won't increase because of changes in actuarial variables such as longer life expectancies, changing retirement age or growing cost-of-living adjustments. They prevent the accumulation of unexpected liabilities driven by investment fluctuations and people living longer.

To implement this reform, the Illinois General Assembly should pass legislation to create a flexible choice plan all new state employees can pick rather than being added to Tier 2.

3) Offer pension buyouts for downstate employees

For those employees who are already members of Tier 1, the nature of a defined benefit plan leaves few options for flexibility. However, at the state level, a “pension buyout” was created in 2018 that introduces more flexibility and has reduced the state’s pension liability by \$1.5 billion dollars since its inception from the nearly 14,000 pension retirees who have chosen it.

A pension buyout allows government workers to take out a portion of the “net present value” of their pension – the amount needed today to fund a retiree’s lifetime benefit. After voluntarily “cashing out” all or a portion of their benefits at a 30-40% discounted rate, workers can roll the money into an IRA or 401(k) style plan and control their money forever. In return, the discount equals savings for taxpayers.

This flexibility allows retirees to withdraw a larger amount at one time – such as using the funds to pay for housing or medical expenses – a vital option for some based on their circumstances, but one which they don’t currently have. Plus, a self-directed account can be willed to family while a pension cannot.

Other retirees might desire to take the buyout because they are not confident in the stability of their pension funds. That’s understandable considering systems such as Chicago’s Police and Fire pensions have some of the lowest funding ratios in the country. In August 2025, Chicago’s mayor had to lend the firefighter pension fund money to make that month’s payouts so the city didn’t have to sell assets. If a system goes insolvent, there’s almost no legal protection to guarantee benefits. Those pensioners would simply be out of luck. Insolvency would be a nightmare for the people who dedicated their careers to the city.

Lawmakers should make a buyout option available to downstate pensioners. This approach gives pensioners flexibility, reduces government’s debt, protects taxpayers and creates the conditions for long-term economic recovery.

4) Constitutional pension reform

Solutions No. 1 through 3 are effective, but they only mitigate the real culprit of Illinois’ pension crisis: the state constitution.

Under the Illinois Supreme Court's 2015 precedent, a government worker's pension benefits cannot be changed in any way after their first day working for the state. This precedent protects not only the benefits a worker has accrued – or earned to date – but also the formula under which those benefits will increase going forward. This view of pension protections is more restrictive than both the federal contracts clause and other state protections. It denies Illinois lawmakers the flexibility they need to make financial decisions necessary for the fiscal health of the state.

Other state supreme courts have upheld pension reforms very similar to those Illinois attempted in 2013, even when recognizing that pensions are contractual benefits that cannot be diminished or impaired.

For example, the Colorado Supreme Court ruled reductions in future cost-of-living increases did not violate retirees' constitutional or contractual rights. The decision hinged on the differentiation between earned pension benefits, or vested base pension benefits, and future increases based on a COLA formula. According to the court, retirees in Colorado do not have an indefinite right to a particular COLA formula forever after their first date of hire.

Colorado's decision is consistent with an analysis of contract rights and pensions by a legal expert who focuses on employment benefits, Amy Monahan. Many states now view pension promises as contractual rights – though some states guarantee them through less protective standards, such as promissory estoppel or property rights – but that does not mean all such states offer retirees the same level of protection as Illinois.

For example, Hawaii's constitution specifically states only "accrued financial benefits" are protected, and courts there have interpreted this language as guaranteeing benefits already earned, but not the future growth in those benefits.

Other states that have seen success with reforming future benefits include Michigan, Arizona, Pennsylvania and Utah. Utah saw the need to reform pensions when annual pension expenditures reached 10% of the state's general funds budget, a level Illinois reached in 2009 and is nearly double that today.

If Illinois passes a constitutional amendment to modify the pension protection clause, clarifying that it protects only earned benefits, it can achieve similar success in protecting taxpayers, the state's fiscal health and public worker retirement security – all at the same time. Such an amendment to the state constitution should end the possibility of a successful legal challenge under state law.

The Illinois Policy Institute has advocated for a reform similar to the bipartisan reforms passed in 2013 that would set the state's pension systems on track to solvency through modest changes replacing Tier 1's 3% compounding post-retirement increases with a measure pegged to inflation, capping the maximum pensionable salary for workers hired before 2011, raising the retirement age and introducing potential cost-of-living adjustment holidays. This reform would only apply to future benefits, and no pensioner would receive a single reduction in their benefit check. That simple modification would save the state \$2 billion annually and would be much less drastic than reducing existing benefits or converting the defined benefit system to a defined contribution plan.

CONCLUSION

Illinois' pension systems are failing because the state allowed debt, delays and political bargaining to take precedence over fiscal responsibility. That path has left taxpayers overburdened, local governments strained and public workers increasingly uncertain about the future.

That path led us into a pension trap. A new path can get us out.

Illinois can protect the benefits workers have already earned while finally stepping toward stability. Maintaining a targeted safety net for Tier 2, expanding pension choice, offering voluntary buyouts and amending the constitution to allow future benefit reforms are not radical ideas. They are practical, proven tools used successfully in states that refused to let their retirement systems collapse under their own weight.

Every year of inaction pushes more Illinois families who can't keep up with the tax burden out of the state, drags more pension systems closer to insolvency and eliminates the ability of the state and cities to pay for essential services. Every year of delay increases the risk retirees will face insecurity instead of stability. The cost of standing still is far greater than the cost of structural, responsible reform.

Illinois cannot undo the past 50 years. But it doesn't have to stay trapped for the next 50. The state's workers, taxpayers and future generations deserve better.