



City of Chicago
Richard M. Daley, Mayor

Gene R. Saffold
Chief Financial Officer

Suite 600
33 North LaSalle Street
Chicago, Illinois 60602
(312) 744-1034
(312) 744-0014 (FAX)
<http://www.cityofchicago.org>

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Contact: Peter Scales
Office of the CFO
(312) 744-1821

COMMISSION TO STRENGTHEN CHICAGO'S PENSION FUNDS RELEASES REPORT ON FISCAL HEALTH OF PENSION SYSTEM

The Commission to Strengthen Chicago's Pension Funds released a report today that warns that the pension funds for City of Chicago employees are so severely underfunded that they lack the financial assets to guarantee pensions for their members.

The Commission report also cautioned that without drastic funding changes, the pension systems will start to run out of funds in a decade or sooner.

"Chicago is not alone – this is a challenge faced by pension plans in cities and states across the country," said City of Chicago Chief Financial Officer Gene Saffold.

"As Mayor Daley has said, as we look toward solutions, we must look at every option that helps take the burden off taxpayers, because people are concerned today about keeping their own jobs and pensions and want their tax dollars spent on improving our economy and their quality of life," he said.

"They're angry at a system that they believe helps preserve pensions for bureaucrats, and we have to appreciate that those who contribute to their pensions are going to have to sacrifice in order to keep their pensions sound," added Saffold.

The commission of key Chicagoans was assembled by Mayor Richard M. Daley two years ago to examine the financial strength of the City's four pension funds - Fire, Police, Laborers, and Municipal Workers.

It includes representatives from the pension fund executive directors, trustees and employee representatives, as well as representatives from the labor, business, consulting and banking communities. The Commission was chaired by Dana Levenson, former City CFO and presently a Managing Director of The Royal Bank of Scotland and the City's Chief Financial Officer Paul A. Volpe, who was later replaced by Gene R. Saffold.



The report states that fixing the funding issues will cost approximately \$710 million per year, growing with inflation for the next 50 years, in addition to the annual pension contributions required under current law. However, the report points out that recent changes to state pension laws calling for a two-tiered system with reduced benefits for future employees other than public safety will reduce that cost to approximately \$660 million.

The commission found that at the end of 2009, the four pension funds covering employees of the City of Chicago, and non-teaching employees of the Chicago Public Schools, had a combined actuarial liability of more than \$25.4 billion and assets with a market value of \$10.9 billion, resulting in an unfunded actuarial liability of \$14.6 billion and a funded ratio of 43 percent.

As recently as 2000, the aggregate funded ratio was 83 percent, within the range deemed satisfactory for public defined benefit pension funds. The market decline from mid-2007 to early 2009 drove the funded ratio as low as 36 percent; it has since recovered to 43 percent at the end of 2009.

“The financial health of each of the City’s four pension funds has deteriorated due to increasing liabilities, inadequate contributions, which are based on a fixed percentage of payroll, as opposed to actuarial need, and adverse market conditions leading to fluctuating returns on investment which could not keep pace with the growth in liabilities,” according to the report.

Under current actuarial assumptions, and accounting for changes in state pension laws, raising the funded ratio to 90 percent by 2062 would require contributions to increase by approximately \$660 million in 2012, and increase proportionate to payroll every year until the goal is met. Employees, who now contribute between 8.5% and 9.125% of their gross pay, would have to contribute more. Under current law, contributions in 2012 will be approximately \$793 million, \$480 million by the City and \$313 million by employees.

“The City and its taxpayers will have to increase the amount they contribute. Employees will have to contribute a larger portion of their pay, and benefits may have to be reduced for employees hired in the future,” according to the report.

The commission made several recommendations to Mayor Daley, aimed at reaching and sustaining higher funded ratios for all of Chicago’s pension funds, including that:

- The Plans should have an actuarially-based funding policy, rather than the current policy of employee contributions being based on a percentage of salary.
- Plan changes for new employees will be necessary, and pursuant to the new state law, some of those changes have already gone into effect for new Municipal and Laborer Fund employees. Those changes include amending the

way Final Average Pay is calculated, changing the way Cost of Living is annually adjusted, and later retirement ages with larger reductions for early retirement.

- Contributions will have to be increased, and new sources of revenues identified. Employee contributions should also not exceed the value of benefits on a career basis.
- The pension funds must review any provisions in current law for refunds or for alternative benefit calculations, to ensure that the anticipated financial results of a reform program are actually obtained.
- A variety of other reforms should be considered, including reforming potential abuses, establishing sound reciprocity with other Illinois public pensions, new structures to manage investments, and improved administration of disability claims and benefits.

All of the aforementioned steps and others are included in the report and are intended to reduce further – and substantively – the \$660 million per annum that it will take to return these pensions to fiscal health

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