OPINION: Arne Duncan and Carl Allegretti on how progress in reducing gun violence hinges on more than policy. **PAGE 14**

STOGIES: He's managing a boutique cigar empire—from Warrenville. **PAGE 4**

CRAIN'S
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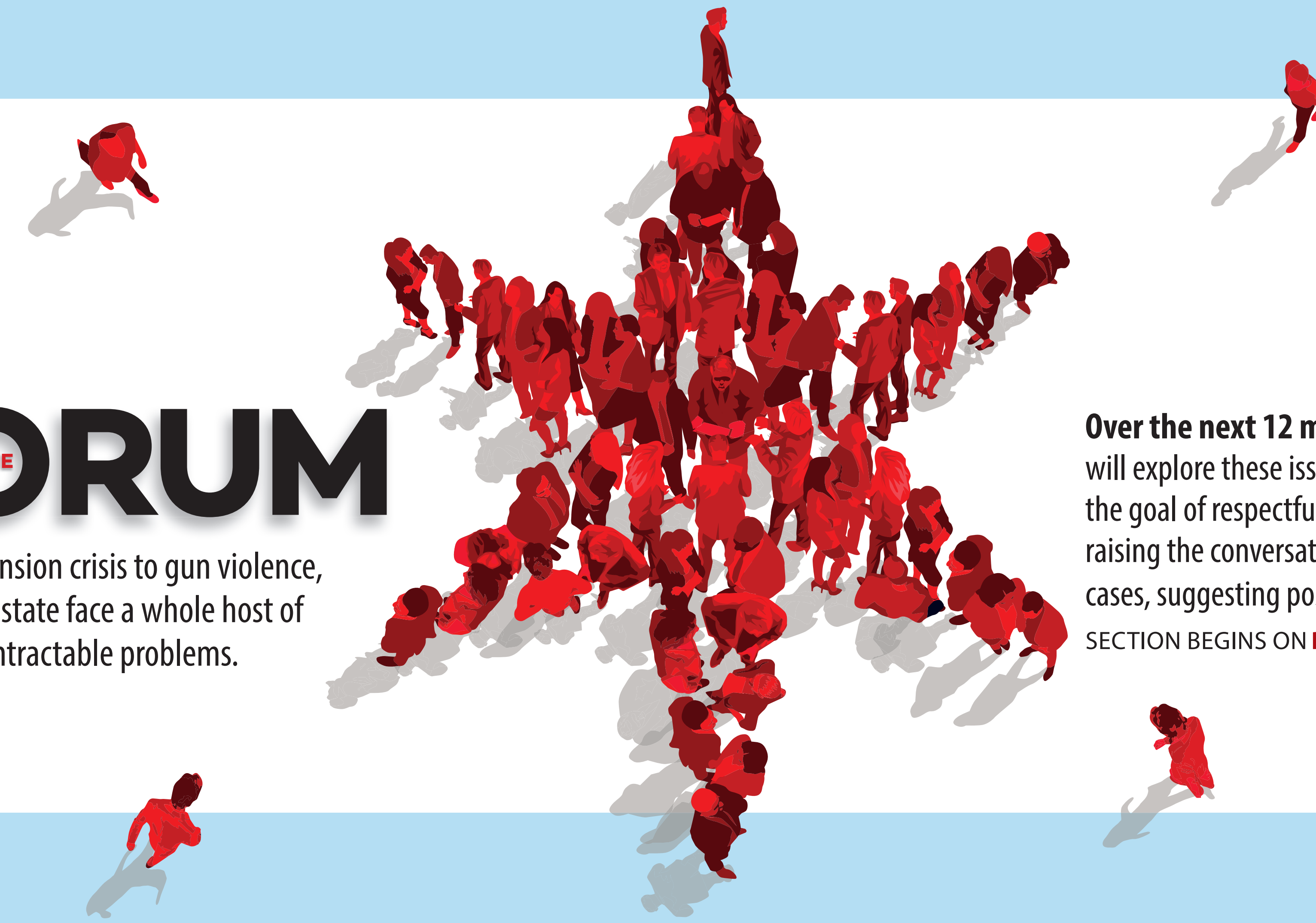


THE FORUM

From the pension crisis to gun violence, the city and state face a whole host of seemingly intractable problems.

Over the next 12 months, Crain's will explore these issues in depth with the goal of respectfully and objectively raising the conversation, and in some cases, suggesting possible solutions.

SECTION BEGINS ON **PAGE 17**

DANIEL HERTZBERG

Kraft Heinz's Boca bummer

Food giant bought fake-meat maker 20 years ago. How come Beyond Meat and Impossible get all the attention?

BY DALTON BARKER

When Kraft Foods acquired Boca Burger nearly 20 years ago, the Chicago-based startup seemed perfectly positioned to bring meat substitutes to the masses.

Boca was a guerrilla marketing sensation, with a devoted following and an endorsement from Oprah Winfrey. Kraft thought it was getting a pacesetter in a market poised for explosive growth.

"Boca Burger gives Kraft an excellent position in the high-growth soy-based meat alternatives category," the president of Kraft's Oscar Mayer division said at the time.

Today, Boca is struggling to regain its mojo in a market suddenly ablaze thanks to new rivals offering products that apparently taste a lot more like meat. While Beyond Meat and Impossible Foods grab headlines and customers, Boca's share of meatless product sales in the U.S. dropped to 3.8 percent last year from 7.3 percent in 2013.

With Boca lagging, its corporate parent—now called Kraft Heinz—must play catch-up in a fast-growing business it could have dominated.

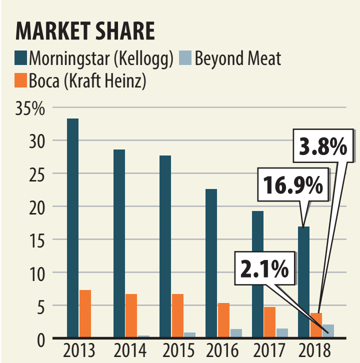
What happened to Boca's buzz? It's a familiar story of a promising upstart languishing after acquisition by a corporate giant. The lessons are particularly relevant now, as multinational packaged-food companies desperate for growth scoop up small players in hot market niches.

Boca was just such a company back in 2000. Operating from a 20-person headquarters in the Civic Opera building in Chicago, the team used catchy marketing

See BOCA BURGER on Page 36

CRUMBLING MARKET SHARE

Boca Burger was losing ground even before upstarts Beyond Meat and Impossible Foods shook up the meat substitute market.



Source: Euromonitor

Mental health and the C-suite: Who's at risk?

Many high-powered CEOs don't seek treatment for overwhelming life struggles or depression. When they don't, the consequences can be grave.

BY LISA BERTAGNOLI

Gail Golden had an uneasy feeling when a client she was coaching, a high-powered executive, told her he was planning a weekend at his family's summer cottage. The executive, who was in his 50s, was being reorganized out of his job. His marriage was in trouble, and he had a difficult personality.

"He was a very bright guy—big personality, domineering. He knew he was smart, and he wielded his intelligence in ways that bullied other people," recalls Golden, a management psychologist and principal at Gail Golden Consulting, a Chicago-based executive coaching firm. The

AP IMAGES

Chicago School Board President Michael Scott is among execs who have committed suicide.

cottage was where his father had committed suicide. "It was like, 'Holy crap,' " Golden recalls. "This was not good."

She asked the executive to check in with her over the

See CEOs on Page 36

Exploring public policy issues that matter to Chicago business

CRAIN'S FORUM

PENSIONS

Can a new governor and Chicago mayor end half a century's failure to fix Illinois' pension crisis?

DEFUSING THE BOMB

BY GREG HINZ

HENRY GREEN REACHED FOR THE MICROPHONE to deliver a message that may sound familiar.

Illinois' system for paying public employee pensions is a disaster, the Urbana lawyer declared, pointing to a sevenfold increase in unfunded liabilities in barely 20 years. "Despite repeated warnings, the General Assembly has failed to meet its commitment" to set aside adequate funds, leaving hundreds of thousands of workers in fear for their retirement livelihood and creating "a staggering liability for future taxpayers."

Only the message wasn't delivered last week, or even last year. Green spoke as a delegate to the state constitutional convention—in 1970. Almost half a century of political failure since, only one thing really has changed: the size of the hole, with unfunded liability in state pension accounts rising from a troublesome $2.5 billion then to an almost unbelievable $133.5 billion-plus now.

Unfortunately, it's very believable—as real as it gets. If you live or work in Illinois, you're on the hook to somehow reduce or pay off that debt, with the slow-moving crisis crippling the state's ability to invest in schools, infrastructure and other wealth-producing enterprises without further raising taxes.

Finding a remedy in many ways is the biggest challenge facing our two new government CEOs: Gov. J.B. Pritzker and Mayor Lori Lightfoot. They take control at an opportune time. But with their options limited by legal, political and economic obstacles, it's far from clear that either has the political will and vision to surpass their predecessors and actually solve the problem.

If they don't, one thing is certain: The damage will

See CRISIS on Page 20

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Business, union and academic leaders weigh in. PAGES 18, 19, 22 & 23

How Arizona, Rhode Island dealt with their crises. PAGE 24

At ChicagoBusiness.com/CrainsForum: 7 ideas to stop kicking the pension can, expanded Forum coverage.

CRAIN'S FORUM

IDEAS

LETTER FROM THE PUBLISHER

Welcome to the Forum

A new mayor. A new governor.

And a host of problems.

At this moment, unlike others in recent history, we await action—potentially on a significant scale—that would alter the course of local history on many fronts. Yet we are also clear-eyed in knowing that to get there, we need sober, but elevated, discussion that's aimed toward solutions.

And so we present Crain's Forum—an ambitious 12-month print and digital deep dive into the seemingly intractable problems facing our great city and state. The goal is to respectfully and objectively raise the conversation about these issues. And in some cases to suggest possible solutions wherever, and however, they might exist.

Most important, we want to make readers aware of the power that information can bring to creating meaningful change in regard to the challenges ahead for our city and state.

At times, those issues seem vast and incongruent. They include the confusing elements involved in meeting our pension obligations, fairly and within our means. And they also encompass the gun violence that plagues many of our neighborhoods across the state. But the discussion also is focused on sustainable school funding, taxation, affordable housing, jobs, clean water, cannabis legalization and a number of other issues that touch all of us.

Each month, we will spend significant reporting resources on a specific issue in our print editions. We will offer up our pages to a wide array of outside voices to deepen the conversation. We will open up our website at ChicagoBusiness.com/CrainsForum at no cost to readers to make sure everyone has a chance to see the ideas we're putting forward and use our social media channels to give people a voice in the discussion.

We will make sure every legislator in the state and every sitting Chicago City Council member will receive a copy of the Forum every month so that those in positions of power are better informed.

We are proud to bring you this journalism, and we are grateful to the three underwriters of this program—the Joyce Foundation, CIBC and GCM Grosvenor. Their support allows us to expand our journalism to cover these subjects in depth and to make sure everyone in the city and state has access to this content now and going forward.

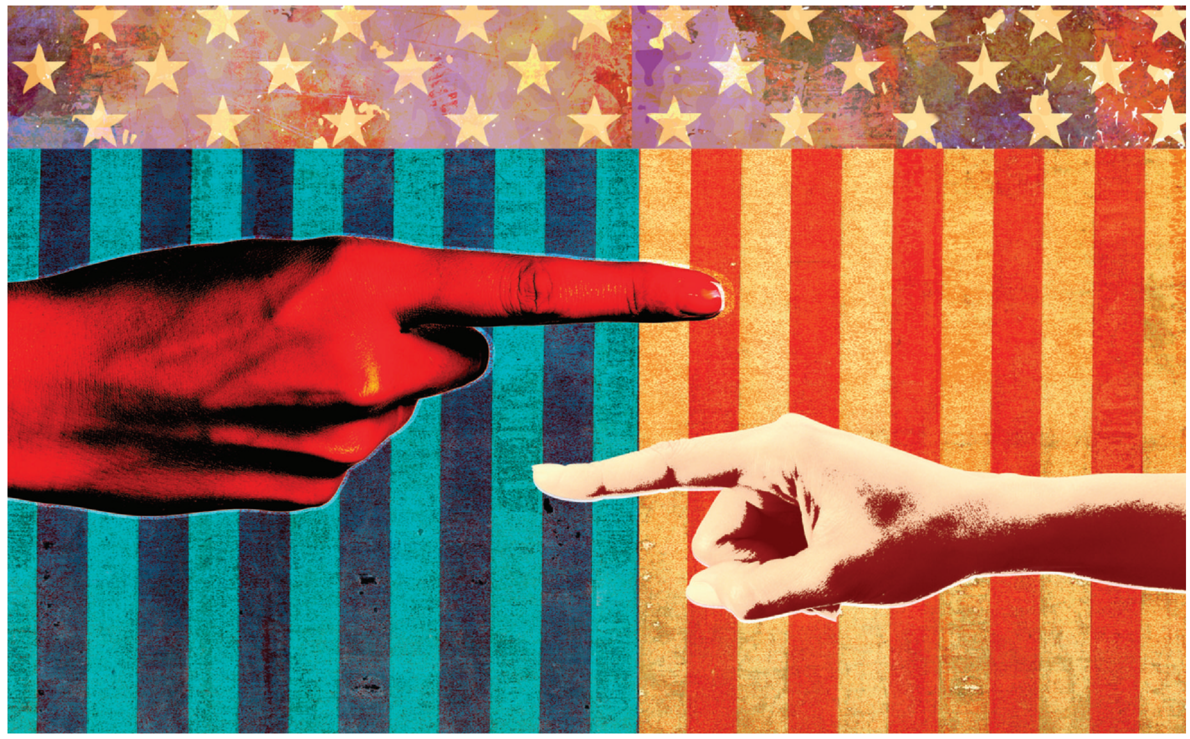
And we'd like to hear from you.

Please be part of the conversation on our Facebook page and drop us a note at CCBForum@crain.com if you'd like to see us cover a particular issue. And you can receive Forum-related opinion pieces, articles and data directly to your mailbox by signing up for our weekly newsletter at ChicagoBusiness.com.

Most of all, thank you for reading.

Jim Kirk

Publisher and executive editor
Crain's Chicago Business



GETTY IMAGES

STATE ASSET TRANSFERS, PPPs COULD OFFSET LIABILITIES

Time to stop finger-pointing, using taxpayers like ATM

Jack Lavin *is president and CEO of the Chicagoland Chamber of Commerce, which represents 1,000 member companies and their 400,000 employees.*

Our state's unfunded pension system is a looming, ticking time bomb, and the longer we wait to address it, the more likely it will cause the next great financial crisis.

Business likes stability. But, with five state of Illinois pension funds having over $134 billion in unfunded obligations, and billions more in unfunded obligations spread across the more than 650 other pension funds throughout the state, we have too much uncertainty leading to a fiscally unstable environment in Illinois. This isn't good for business and isn't good for Illinoisans.

The Illinois Supreme Court has spoken loud and clear that we must pay our pension obligations. Teachers and university workers do not receive Social Security. Their pension is their Social Security. Would we deny ourselves the Social Security that we have earned?

While many solutions have been proposed throughout the years, it has become clear we can't just cut our way out of this fiscal mess. We've tried that.

It is time to stop arguing about the past and pointing fingers and look to the future. It's time to be honest with ourselves and our children.

There is no one magic answer to solve a problem that has been decades in the making. We need to broaden our thinking and start being bold and innovative in our solutions. Taxpayers cannot continue to be an ATM for this issue.

One of the answers to solving this crisis lies in the transferring of government-owned, revenue-producing assets to pension funds, which will reduce the pension debt obligation. This works by transferring assets that have a consistent revenue stream, like water and sewer systems, parking garages, real estate, and sustainable regulatory and licensing fees.

These assets would be marked to market versus book value on a municipal or state government balance sheet and offset the pension liability. They are still publicly owned assets, but now, we have monetized them and matched the true value of the public assets to liabilities.

Another type of asset transfer is public-private partnerships for new infrastructure. New assets, like the proposed transit-oriented One Central development in the South Loop, have the potential to fund pensions for years to come. Once the transportation hub is built with private funding, the state would make equity payments using the new sales tax revenue generated at the development to acquire it over 20 years and transfer the value to the state to mitigate pension liabilities, bringing a long-term, income-producing asset into the fold to pay for pensions.

This development, and others like it, has

> **We must pay our bills, keep our promises and be accountable. Pension obligations will no doubt require some tough choices.**

the potential to be a win-win investment as it brings new jobs to the region and lowers the state's pension obligation. These types of public-private partnerships with pension funds are done as a normal course of business in Canada, Europe and Australia.

Gov. J.B. Pritzker has created the Pension Asset Value & Transfer Task Force to examine state assets and recommend how they can be used to stabilize state finances. The city of Chicago should consider creating a similar task force.

We must pay our bills, keep our promises and be accountable. Pension obligations will no doubt require some tough choices. We need to think more broadly and differently if we are to solve this problem and ensure employees who earned their pensions receive their pensions.

JIM KIRK PUBLISHER • **ANN DWYER** EDITOR • **HUGH DELLIOS** CONTRIBUTING EDITOR • **THOMAS J. LINDEN** CREATIVE DIRECTOR • **JASON McGREGOR** DIGITAL DESIGN DIRECTOR • **DANIELLE NARCISSÉ** COPY CHIEF

PENSION PROMISE CAN'T BE BROKEN

A funding problem needs a funding solution

Roberta Lynch *is executive director of the American Federation of State, County & Municipal Employees Council 31. The union represents 100,000 active and retired public-service workers in Illinois.*

They teach our kids, respond to emergencies, care for people with disabilities and prevent child abuse. They staff our libraries, drive trains and buses and pick up our trash. City, county, state, school district and university employees provide these and countless other public services across Chicago and throughout Illinois every day.

We count on them to shape the lives of our young people, to rush in when disaster strikes, to aid families and communities in crisis. They count on us to keep the commitment made for security and dignity in their retirement years.

Illinois public pensions are modest: just $34,084 for the average state employee retiring on the standard formula, according to the retirement system's latest annual report, and $34,413 for retirees in the Chicago municipal fund who aren't eligible for Social Security. Reality in most cases is far from the six-figure outliers whose benefits make headlines and fuel political attacks on the pension funds.

Public employees contribute significantly toward their own retirement—in most cases, 8 to 12 percent of every paycheck they earn. And because most public workers can't earn credits toward Social Security, that modest pension is their primary if not sole source of income in retirement.

Still, there's no avoiding the pension-debt elephant in the room. It stems from decades of decisions—by politicians of both parties and at all levels of government—to short or altogether skip obligatory contributions, effectively borrowing employees' retirement income to finance a public body's operations, benefiting all of us who received the services we depended on.

Using the retirement systems like a credit card was a convenient alternative to raising revenues or reducing expenditures. Yet over the past decade, instead of facing up to the situation and beginning to repay the money that was borrowed, too many politicians tried to cut benefits instead.

First a lesser "Tier 2" pension plan was instituted for public employees hired since 2011. Its provisions are so meager that experts believe it may violate federal regulations.

Then both the state and the city of Chicago backed legislation cutting retirement benefits. When unions sued—invoking the Illinois Constitution's pension clause, which states that membership in a public retirement system is a contractual relationship, the benefits of which can't be diminished—courts threw the changes out.

Now some of the same interests want to wipe out the constitutional pension guarantee. That's immoral, threatening the retirement security of those who've served their communities and paid their share and who depend on a modest pension. And it's illegal, ignoring the U.S. Constitution's prohibition on impairment of contracts.

The most rational approach is to pay the entire cost of benefits earned each year, plus a slice of the accrued underfunded liability.

A funding problem requires a funding solution. And pension debt runs up interest, so the sooner it's paid off, the lower the cost. The most rational approach is to pay the entire cost of benefits earned each year, plus a slice of the accrued unfunded liability enough to retire it over time.

The key is having sufficient revenue. City, county and state governments must be able to maintain and improve the public services that people need while also paying the debts owed.

We're encouraged that Gov. J.B. Pritzker and Mayor Lori Lightfoot have said they recognize that pensions are a promise to public-service workers that can't be broken. When the state realized an unexpected spike in tax returns this spring, the governor dedicated it to making the state's full pension payment. And he's leading the way toward fair tax reform that will raise future revenue in a more equitable and sustainable way. Public employees of every kind are counting on other employers to follow suit.

CRISIS

Continued from Page 17

only worsen from a continued failure to lance a boil that's been building since Richard Nixon was president.

Consider:

- As a share of spending in the state's operating account, or general funds, pension outlays have risen from 2.9 percent in 1996, when a long-term, 50-year funding plan pushed by former Gov. Jim Edgar went into effect, to a projected 24.4 percent this year. Yes, 1 dollar in every 4.
- The soaring cost of servicing pension debt is devouring all else in state government. In 1996, the state spent almost six times as much on aid to elementary and high schools as it did on pensions. Last year, those lines crossed. Paying retirees has become a bigger priority than educating our kids, according to data from the Illinois Commission on Government Forecasting & Accountability, the Legislature's fiscal research unit.
- Even with that spending growth under the "Edgar ramp," taxpayers today are paying far more to the state's employee pension systems than originally expected: for instance, $9 billion in fiscal 2018 compared to the original $4.54 billion projection.
- Despite that huge increase in taxpayer spending, the financial condition of the funds is stagnant, with unfunded liability rising $98.43 billion between fiscal 2004 and 2018 and the funds still having only about 40 percent of the assets they'll need to pay promised benefits—almost exactly where they were a decade ago.
- Why are we no better off? A main reason is that, even now, with the state spending $9 billion a year on pensions, we're putting in roughly $3.5 billion less than detailed financial projections by actuaries require. That's the "tread water gap," as Moody's Investors Service puts it, and when you're not even treading water, you're falling further behind.
- Trends may reverse and slowly improve in about a decade when state workers hired since 2011 become a significant part of the total state employment pie. But the emergence of "Tier 2" workers is no certain panacea. Their pension benefits likely are too low for federal law. That would mean more spending to fix that problem.

"Everybody's looking for a silver bullet. I don't think there is one," says Edgar, referring to calls for the state or its pension funds to seek bankruptcy, or end pensions altogether, to fix things.

"It's politics," former Mayor Rahm Emanuel told me on one of his final days in office, reflecting on how he'd done more than his predecessors to cure the city's pension problems, but still left a $1 billion hole for successor Lightfoot to fill in the next two years.

Rulings by the Illinois Supreme Court "really (have) us in a death grip," says former state Rep. Elaine Nekritz, one of the chief authors of a 2013 rescue plan that would have forced workers and not just taxpayers to bear some of the cost of a fix. "It's basically what they told us: Go find a way to pay for it."

If you can.

HOW DID WE GET HERE?

So how do we get out of a fix that has us competing to claim the worst-funded pension system in the nation? The place to start is looking at how Illinois got here, and not repeating it.

According to COGFA, the biggest reason for the state's pension woes is that lawmakers, be they Democrat or Republican, for many decades consistently failed to set aside what actuarially is required. Instead, the money has been diverted to more immediately pressing and arguably more popular needs.

"It's human nature," says Charlie Wheeler, a longtime watcher of state government from his perch as head of the public affairs reporting program at the University of Illinois at Springfield. " 'Long term' is the next election, in two years. Schools have to open right now, but a lot of people don't care very much about pensions that will be paid in 20 years."

In budget season, "reducing the pension payment causes the least pain," says Tim Blair, executive director of the $17.5 billion State Employees' Retirement System, which covers nonteaching workers.

NEWSCOM

Chicago Mayor Lori Lightfoot

AP IMAGES

Gov. J.B. Pritzker signs the state budget and legislation related to a graduated income tax in Illinois June 5 at the Thompson Center in Chicago.

With unions also focused on the short-term bottom line—pay hikes for their members—lawmakers repeatedly found cause for a pension payment holiday, in which the state makes less than its normally required payment. But, like putting the mortgage payment on your credit card, the bill eventually comes due with interest.

The most notorious example—and there have been several through the years—came under Gov. Rod Blagojevich in fiscal 2006 and 2007, after officials decided to refinance part of the state's pension debt by issuing a giant $10 billion pension obligation bond.

As a pure arbitrage play, the strategy has worked, says then-state Chief Financial Officer John Filan, who asserts that the state made more money from investing POB proceeds than it had to pay to borrow. The problem is that Blagojevich skimmed more than $2 billion off the top to pay for other state programs. That left the pension funds little better off than they were, because the state suspended making its full regular annual payments.

Lawmakers in 2013 did try to strike a compromise that would help taxpayers.

At the behest of Democratic leaders, Nekritz and then-state Sen. Daniel Biss tried to split the baby, passing a plan to sharply up the state's annual payments in exchange for workers contributing more and getting less. But the plan was rejected by the Illinois Supreme Court on grounds that the state constitution's pension clause, which delegate Green helped draft, created "an enforceable contractual relationship, the benefits of which shall not be diminished or impaired."

The state likely hurt its own case by cutting income tax rates shortly before the court ruling and then arguing it was too strapped to pay up. The court didn't buy it.

"They essentially held (pension promises) are an individual right, not a bargained right," Nekritz says of the landmark 2015 ruling. Meanwhile, co-sponsor Biss walked away from his own creation, pretty much apologizing for having dared suggest that workers get less, when he ran for governor in 2016.

The state's experience ultimately crippled an effort by Emanuel to pass a similar compromise for city funds—though not until his second term, after he'd been re-elected. When the court tossed that, too, Emanuel moved toward fully paying what the city owed. But the record tax hikes he pushed through—bringing in hundreds of millions of dollars—produced only about half of what's needed annually to hit full funding.

In the midst of that, Republican Gov. Bruce Rauner took office and, with all the subtlety of a bull in a china shop, tried to dictate solutions to a heavily Democratic Legislature, from bankruptcy to hobbling unions and outsourcing jobs. Nothing happened.

Now politics isn't the only reason for the pension shortfall. Another is that, over time, the amount taxpayers are paying has become unreasonable.

Most of the savings in the Nekritz/Biss bill would have come by junking the 3 percent annual compound cost-of-living adjustment that most pensioners now get in favor of a lesser COLA. The original clause was enacted in 1989 when Republican Jim Thompson was governor and inflation was running well above 3 percent.

"The (Democratic) Legislature wanted it," Thompson shrugged in a recent interview. "The fiscal note did not project anywhere near the amount that we're paying now."

Despite his intentions, the 3 percent COLA in an era of 1 or 2 percent inflation means that, over time, state pension costs are rising dramatically in real terms—doubling every 25 years, according to the Civic Federation. But labor leaders who spend tens of millions of dollars on political candidates every election season aren't budging. Why should they? The Illinois Supreme Court says the money is due and owing.

Other major reasons for the $113.5 billion hole: declining assumed rates of return on pension investments; a state workforce that's roughly 20 percent smaller than it was, and therefore contributing fewer dollars; and demographic factors—primarily the fact that people now live longer and draw their pensions for years longer.

"No plan is permanent. Things have to change," Edgar says now.

But the investment and demographic factors are the cause of about 40 percent of the state's pension shortfall, COGFA says. Combined with intentional underfunding by politicians, the stage was set for today's morass.

A FEW GOOD SIGNS

As Illinois waits to see how seriously Pritzker and Lightfoot address the larger problem, there are a few bright signs—but their impact is limited.

The biggest is the growth of Tier 2 workers, who were told when they were hired that they'd get lesser pension benefits and thus are not covered by the 2015 court mandate. To put it bluntly, the people who get the biggest Tier 1 checks eventually will die off, replaced by cheaper newbies. But at least some of the savings will disappear if Tier 2 benefits have to be raised. Confides a top Springfield insider, "Tier 2 is paying more in contributions than they'll get in benefits. They're subsidizing the state. There will be a reckoning."

Another good sign is that a voluntary buyout plan, in which workers can choose to get money upfront in exchange for a smaller COLA, has had a solid response rate, with nearly a third in a pilot group taking the deal. But the savings so far are small, in the range of $50 million a year at SERS, that agency says.

All of the above leaves limited options for the new leaders who have their chance: Pritzker and Lightfoot. They essentially have two exit paths: sharply cut costs or suck it up and pay. Either involves political risk.

On the cutting side, the core of Rauner's plan—allow bankruptcy so contracts governing pensions can be tossed out—was a political nonstarter when he was in office and is not seriously being pursued by anyone at the moment.

Arguably more feasible is a call from groups such as the Civic Federation to push for a constitutional amendment to trim pension benefits. If Pritzker wants to let people vote next year on a graduated income tax, they ought to be able to decide on pensions, too, the argument goes.

Advocates point to Arizona, which had similar language to Illinois' and changed it. But there are legal reasons to think that state's experience could not be replicated here. Arizona is considerably more conservative than Illinois. More significantly, the Arizona decision has not been legally challenged as it almost certainly would be here on grounds that it violates the Illinois Constitution and the contracts clause of the U.S. Constitution.

Lightfoot has hinted at a third cost-cutting option: ending pensions for newly hired workers. But she has given no details and would have to cross her progressive political base to pursue it.

The other exit path—pay off the debt with more revenue—appears to be where Pritzker is headed.

It could come from the graduated income tax—Pritzker promises $200 million a year if it passes, and he told Crain's in early June that he might go higher—or more city property taxes, taxing retirement income, expanding gambling or some of the numerous other ideas that have been kicked around, all of which impose at least some pain on residents and some risk to the state's economic competitiveness.

Pritzker does hope for some savings from consolidating the numerous small pension systems in suburban and downstate areas and is looking at transferring certain assets to the pension funds, but not the biggest potential items: the Illinois Tollway or Lottery.

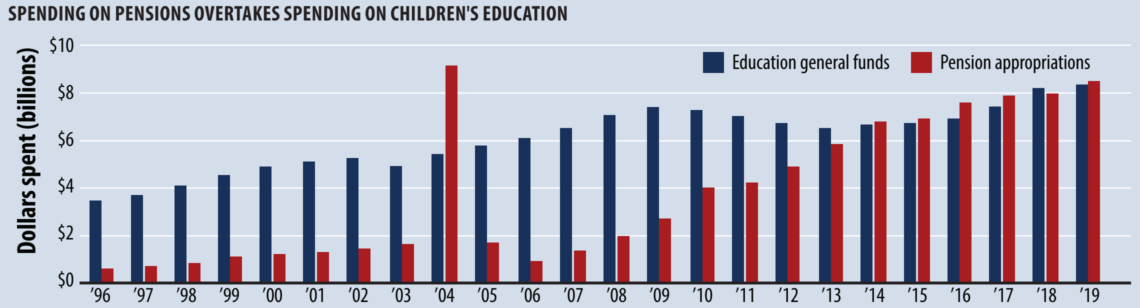
Overall, though, he's given no sign of willingness to cross his union allies. Asked recently when the state finally will turn the pension corner, he replied, "The (Edgar) ramp is what it is."

At least the governor no longer is proposing his own pension holiday, as he did earlier this year before getting an income tax windfall. That means the problem won't get even worse. But will it ever get better?

Only if our leaders spend the political capital to actually solve the problem without writing a blank check. New executives lead the state and city, and both have big ambitions. It's up to you, Mr. Governor and Madam Mayor. Let's see your plan.

SPENDING ON PENSIONS OVERTAKES SPENDING ON CHILDREN'S EDUCATION

The cost of servicing Illinois' pension debt continues to soar, devouring state government resources. This year, the state spent more on pensions than on educating children, according to data from the Illinois Commission on Government Forecasting & Accountability, the Legislature's fiscal research unit. By contrast, in 1996, the state spent almost six times as much on aid to elementary and high schools as it did on pensions.

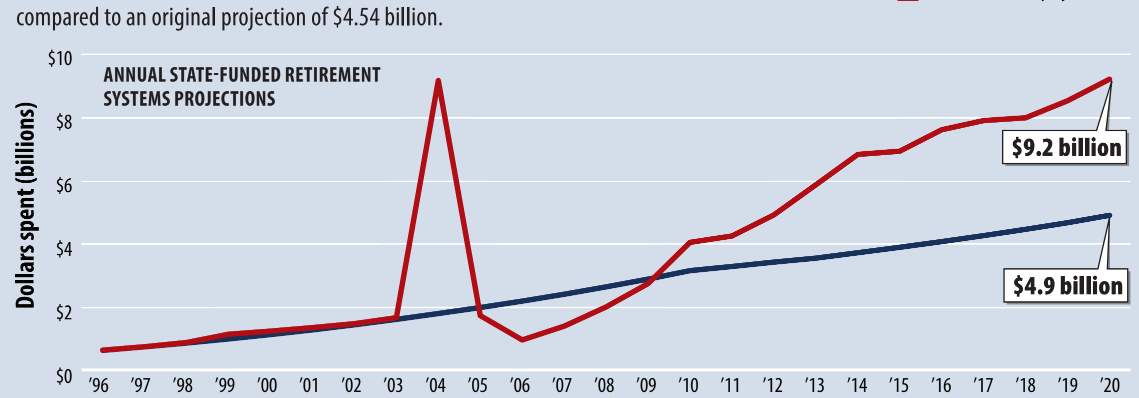


Sources: Illinois State Board of Education, COGFA

Notes: Fiscal year 2004 retirement appropriations authorized include $7.3 billion in proceeds from the sale of pension obligation bonds. 2017 includes $533 million for FY2016 and FY2017 provided from PA 99-0524.

PENSION PAYMENTS OUTPACE PREDICTIONS

Taxpayers are paying far more to the state's employee pension systems today than originally calculated for the "Edgar ramp" in 1994. For instance, they paid $9 billion in fiscal year 2018 compared to an original projection of $4.54 billion.

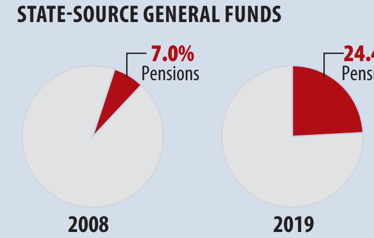


Source: COGFA

Notes: 2019 data include actual figures from 1996 to 2018. Data for 2019 and 2020 are projections.

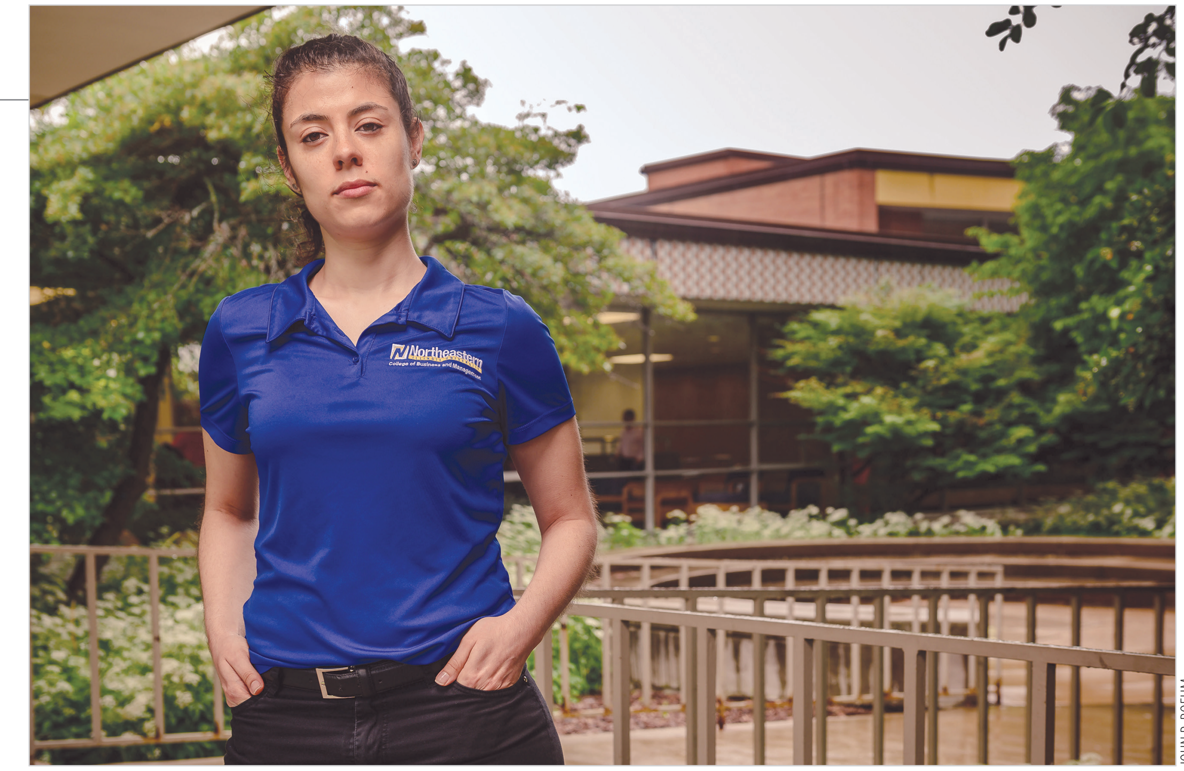
SOARING PENSION PAYMENTS DEVOUR STATE BUDGET

Pension outlays now eat up 1 of every 4 dollars of state spending in the state's operating account, or general funds, they have risen from 2.9 percent in 1996 to a projected 24.4 percent this year.



Notes: FY2019 is an estimate

Source: Civic Federation



JOHN R. BOEHM

State employee Stacy Alikakos, 33, believes millennials like her and other younger workers will foot the bill for an older generation's fiscal mistakes.

State workers steadfast despite uncertainty, reform demands

Mulling early buyouts, angered by Tier 2 deal

BY DAVID MENDELL

Twenty-year veterans worried about losing their cost-of-living increases. Retirement-age workers torn over accepting an early pension buyout. Millennials upset about receiving lesser benefits than their more seasoned colleagues.

The roughly 61,000 people who work for the state of Illinois are by no means a monolithic force. But as new political leadership takes over in both Springfield and Chicago, together state employees remain steadfast that they alone shouldn't sacrifice to shore up the state's cash-starved pension system.

Interviews with public-sector workers revealed a common thread about the state's chronic pension distress: Foremost, they are frustrated that elected leaders have steered their pension funds into a mountain of debt. They devoutly believe they deserve the benefits promised to them. And they resent a public image that they will live the high life with inflated payments awaiting them in retirement.

"I don't feel that state employees should be asked to give up something else," says Stephen Mittons, a child protection investigator for the Department of Children & Family Services. "You hear things like, 'Maybe if they gave up their COLA, we could straighten this out.' Well, that was a promise made to employees and something earned by the employees."

The workers don't deny that the system is too heavily in debt and action is needed. Privately, a few say they might be open to proposals to tax their pension payments—but only at a modest rate, and only if the revenue is channeled back to ensure benefits continue for workers retiring behind them.

"But judging from history, I don't trust them to put it where it belongs," says a secretary of state employee who declines to give his name when interviewed outside a motor vehicle/drivers' services office. "They always take the money for something else and just kick the can down the road."

To ease the state's overall pension obligations, legislation enacted in 2018 gives many public employees the option of early pension buyouts and accelerated payments at a reduced value of their overall vested pension. It started as a pilot project, but Gov. J.B. Pritzker has proposed making the program permanent.

Nearly a third of those offered the accelerated payment plan—469 of 1,504—have accepted, a pension system spokesman says.

GETTING LESS

Workers were emboldened by the Supreme Court's 2015 ruling that legislation trimming their benefits was unconstitutional. Yet some workers are getting less. Those hired since 2010—nearly a third of the workforce—have been dropped into a second pension tier in which they contribute just as much but are vested later and will receive smaller retirement COLAs.

Without giving specifics, Daniel Montgomery, president and chief operating officer of the Illinois Federation of Teachers, calls the split pension structure "illegal" and hints that unions again might seek a remedy in the courts.

"As far as I can tell, it is one of the worst pensions of any state in terms of value," he says. "The rank and file are saying, 'Why are we the ones paying? Where is the business community? What are they willing to give up?' "

Stacy Alikakos, 33, is one of the Tier 2 employees, and she's not happy about it.

An adviser to graduate students at Northeastern Illinois University, she says she sees former colleagues who've retired under the Tier 1 system struggle to make ends meet and wonders how she'll be able to manage with even less.

She believes millennials like her and other younger workers will foot the bill for an older generation's fiscal mistakes.

"I find it very irresponsible and I am very angry," Alikakos says. "I don't understand why protecting people's livelihoods hasn't been a priority."

The secretary of state worker, who's worked for the state for three decades, is in his 60s and nearing full retirement. He worries that cost-of-living adjustments and other benefits will be siphoned from his retirement income to shore up the pension systems.

Among proposed solutions is curtailing or taxing workers' 3 percent annual COLAs, which puts at least some state workers on track to earn six figures over the course of retirement.

"When I started in government service, people laughed at my salary because I made so little and could barely live on it," says the employee, who now earns about $56,000 a year. "If they change the formula, I'm screwed."

Mittons is a U.S. Marine veteran who's worked for DCFS for 24 years and is an elected trustee on the State Employees Retirement System board. The average annual state pension for a 26-year worker who retired in fiscal year 2018 is $40,085.

"Nobody is going to live lavishly off that," Mittons says. "My colleagues, as beleaguered as they are, are still here every day. No one comes into state service to get rich. They come into state service because they see the need to serve."

FORUM IDEAS

REFORMS MUST ACCOMPANY REVENUE HIKES

Consolidate funds, tax retirement income

Laurence Msall *is president of the Civic Federation, an independent, nonpartisan, 120-year-old tax policy and government research organization whose membership includes business and professional leaders.*

Earlier this month, the Illinois General Assembly adjourned its spring session, once again without addressing the state's most pressing financial issue: pensions.

The state's unfunded liability for its five pension systems stands at nearly $134 billion. Statewide, local governments' unfunded liabilities add an additional $60 billion to that figure. Under newly signed legislation, the state's biggest fund, the Teachers' Retirement System, stands to see its obligations increase annually by tens of millions of dollars going forward.

The only good budget news for pensioners is that in fiscal year 2020, the state will make its full statutory general funds pension payment of $8.1 billion. This is not the amount that actuaries have determined as necessary to improve the condition of the funds. However, even this payment, when combined with the cost of paying existing pension debt service, will consume 24.3 percent of state-source general funds revenue, or nearly a quarter of the operating budget.

Without substantive reform—and despite the extraordinary amount of money being shoveled at the problem—the state and its local governments will continue to struggle with pension funding challenges and the crowding out of essential government services. In order to meaningfully tackle Illinois' pension crisis, revenue increases *must* be accompanied by reforms as part of a comprehensive, statewide solution.

The Civic Federation's Kearney Center for Public Pensions has developed a bipartisan, equitable framework to address this crisis and move Illinois forward.

> **Illinois is one of only three states with an income tax that exempts all retirement income from taxation.**

An essential first step would be for state and local leaders to work together on consolidating Illinois' 650-plus state and local public employee pension funds. In addition to increasing transparency and accountability by centralizing functions, this step could save hundreds of millions of dollars on an annual basis in management efficiencies and increased investment returns. We encourage the governor and his task force to give serious consideration to this area of reform.

An even better first move would be statewide consolidation of the pension funds with the additional step of the state absorbing the unfunded liabilities of local funds, including Chicago's. Only the state of Illinois has the adequate tax capacity to shoulder this crushing burden. Illinois must end the practice of myriad local governments taxing citizens with little regard for the cumulative effect of separate taxes on taxpayers.

Local funds would keep responsibility for their normal (annual) costs, which are much more reasonable for local governments to manage. This would enable billions of dollars in local property tax relief throughout the state and free up room in local budgets for investment in public safety and other important services.

Under such a plan, Illinois will have shifted billions of dollars to its balance sheet, which cannot be tackled under the state's current tax structure or even with the graduated income tax proposal approved by the General Assembly and governor. To finally and decisively fix the problem, Illinois has no choice but to also eliminate unaffordable loopholes, such as its overly generous tax exemption on retirement income.

Illinois is one of only three states with an income tax that exempts all retirement income from taxation. Low-income seniors in Illinois who cannot afford to stop working still pay state taxes on their income. Taxing retirement income in alignment with the federal tax code would increase equity and generate $2 billion to $3 billion annually for the state while protecting the most vulnerable seniors by exempting income under a certain threshold.

Solving Illinois' pension crisis will require a comprehensive solution and shared sacrifice. Although the General Assembly has very recently adjourned, Illinois cannot afford to wait much longer to resolve our state and local pension crisis and stabilize our governments.

RETHINK THE CRISIS APPROACH

Hasty, shortsighted reforms make for more pain later

Amanda Kass *is associate director of the Government Finance Research Center at the University of Illinois at Chicago's College of Urban Planning & Public Affairs.*

Gov. J.B. Pritzker and Mayor Lori Lightfoot are under pressure to do something—anything—about Illinois' and Chicago's "pension crises." But I caution them, and their constituents, against hasty, shortsighted reforms that would trade smaller payments now for more pain later.

Any proposal to address a pension crisis should be scrutinized to identify whether the underlying goal is improving the pension systems' finances or closing a government's budget gap. No simple solution exists to address both simultaneously.

While often invoked, a definition of "pension crisis" is rarely offered. The phrase conjures images of retirees' monthly benefits suddenly being halted. While not the present situation, the pension systems' low level of funding has many worried it could happen. My colleagues Robert Bruno and David Merriman and I share this concern, but we argue that the "pension crisis" framework obscures the real, underlying problems and creates the unattainable expectation that the "crisis" must, and can, be solved immediately.

Such thinking is misguided, in part, because pension systems' finances are in constant flux, and unfunded liabilities represent a long-term form of debt. As such their financial condition is not something to be "solved."

The phrase "pension crisis" is often invoked in relation to two issues. The first is governments' structural deficits. High pension contributions are often pinned as the root of these deficits; however, these payments are just one source of budgetary stress—others at the state level include backlogged bills from the multiyear budget impasse and increased education spending. The second issue is the pension systems' poor finances. These issues are in tension, and addressing one necessarily exacerbates the other.

The pension crisis framework has historically led to reactive policies that focus on short-term "solutions" that cost more long term. Lawmakers have tried cutting pension benefits multiple times only to have the Illinois Supreme Court strike down their efforts. Although reduced benefits for new hires is legal, it can also be problematic. For example, the reduced benefit tier for anyone hired after 2010 is so low that it likely runs afoul of federal laws concerning public pensions. Correcting this deficit could end up costing more than expected savings.

> **The pension crisis framework has historically led to reactive policies that focus on short-term "solutions" that cost more long term.**

ISTOCK

Contributions today are large because for decades both Illinois and Chicago underfunded their pension systems. Even when lawmakers have created plans to pay down unfunded liabilities, they have done so by putting in ramp periods that keep contributions artificially low, thereby extending the practice of underfunding (albeit less so than before). The nature of the ramps and the backloaded repayment schedules re-creates the "crisis" as time goes on. These ramps ultimately cost more than if governments immediately started properly funding their pension systems.

One reason for caution is that lawmakers just legalized recreational marijuana and expanded gambling (including authorizing a Chicago casino), and both will generate revenue for Illinois and Chicago. Another revenue-generating item—amending the state constitution to allow a graduated income tax rate structure—will be on the 2020 ballot. While some might suggest pension holidays until new revenue is realized, this would be a costly mistake.

Political and public sentiment for the new administrations to do something immediately will create fertile ground for pension "fixes" to flourish. The best course of action for the near term is for both Illinois and Chicago to make the payments required under current law. Only after the downward trend in the pension systems' finances has been reversed should lawmakers even consider extending the repayment schedules and/or lowering the funding targets.

GETTY IMAGES

AMEND THE CONSTITUTION

Cuts would protect taxpayers *and* workers

Adam Schuster *is director of budget and tax research at the Illinois Policy Institute.*

Pension math is highly dependent on assumptions about the future. With the economy slowing and the risk of a recession growing, its worth asking what a downturn could do to Illinois' pension systems if Springfield doesn't take meaningful action to address its $134 billion debt problem. The short answer? Illinois' 667 public pension funds will enter a virtually irreversible financial death spiral.

An actuarial analysis commissioned by the Illinois Policy Institute shows if state-run pension funds lose 20 percent of their asset value as a result of a recession—the same loss experienced in 2009—and the average return on investment matches the 4.6 percent the funds experienced in the 10 years after the last recession, the state's major retirement systems will run out of money in less than 30 years.

Under this scenario, the State Universities Retirement System would be the first to reach insolvency, and the fund would be unable to pay full benefits by 2039. The other systems would see their funding ratios (the amount of money on hand to pay promised benefits) decline precipitously each year despite constantly increasing employer contributions. Retirement systems for teachers, state employees and elected officials would run out of money between 2046 and 2048.

Legal scholar and pensions expert Amy Monahan has argued even ironclad legal provisions preventing benefit cuts cannot be used to force states to pay full benefits from insolvent funds. Simply put, if there's no money, benefits can't be paid without impairing the state's ability to exercise the basic functions of government.

> **Illinois must act now, while thoughtful and balanced reforms can still save pensioners and taxpayers from a painful fate.**

Illinois must act now, while thoughtful and balanced reforms can still save pensioners and taxpayers from a painful fate. A constitutional amendment that protects earned benefits but allows for adjustments in unaccrued benefits would allow the General Assembly to cut costs while responsibly eliminating the debt. This would secure the retirement benefit workers have been promised and also stabilize the pension funds.

A look at smaller-scale pension crises across the country shows what happens when lawmakers ignore reality.

In Central Falls, R.I., pension debt led to the city's bankruptcy, and pension plan participants saw current benefits cut by up to 55 percent, even for retired workers. And in the largest municipal bankruptcy in U.S. history, Detroit public employees saw pension benefits slashed, and a federal court rejected retirees' legal challenge to reinstate their full pensions.

Even without a recession, the status quo is already harming the state's economy, taxpayers and Illinois' neediest residents. Illinois spends more than 25 percent of annual general revenues on pensions and related costs. That 25 percent includes debt service on pension obligation bonds and the state's new responsibility for contributing to the employer cost of the Chicago Teachers' Pension Fund, which gives a fuller picture of what pensions truly cost the state than direct contributions alone.

If we stay this course, not only will Illinois fail to protect taxpayers and the public services they rely on, but lawmakers will also take away public workers' retirement security.

CHANGE THE ILLINOIS NARRATIVE

A 'holistic' fiscal plan should accompany any tax plan

Kelly Welsh *is president of the Civic Committee of the Commercial Club of Chicago, a group of 90 senior executives of the Chicago region's leading employers.*

For more than a decade, the Civic Committee of the Commercial Club of Chicago has sounded the alarm about Illinois' growing pension debt and has strongly advocated for pension reform and ensuring the financial health of the state's pension system.

In 2006, when we issued our first report on state finance, "Facing Facts," the unfunded liability of the state pension funds was $40.7 billion. In 2009, when we issued "Facing Facts Revisited," the pension debt was $77.8 billion. Since then, the state's pension debt has grown to $133.5 billion, despite ever-growing contributions, the adoption of a Tier 2 pension system for new employees and an employee buyout program, as well as one of the longest economic expansions in history.

And under the state's current statutory pension contribution schedule, the unfunded pension liability will keep growing until 2028. As a result, Illinois' pension debt is among the worst in the nation and the state has the worst credit rating in the country.

Illinois has many strengths, including its position as a key transportation hub, its diversified economic base, its outstanding universities and research centers, and its highly educated workforce, but the state's financial issues are a flashing warning light to businesses and people deciding to invest or live here.

As business leaders, we have seen the impact of the state's financial issues on the decisions businesses make every day about whether to invest and grow in Illinois or somewhere else. Because of its many strengths, the state's economy continues to grow, but Illinois is punching below its weight, lagging its peers and the U.S. on key economic growth metrics.

Earlier this year, we released "Restore Illinois: A Foundation for Growth," which provided a holistic plan for addressing the state's fiscal challenges. The report outlined a financial framework that included implementing long-term financial planning and increased financial transparency, eliminating the state's structural budget deficit and its unpaid bill backlog—now approximately $7 billion—establishing a reserve fund to enable the state to weather an economic downturn, and implementing a new funding plan to pay down the over $130 billion in unfunded pension liabilities.

> **We must change the reality of the state's fiscal condition to change the narrative about our state.**

Our proposal also provided recommendations for spending reductions and revenue increases that would help the state get back to fiscal stability, while minimizing as much as possible the negative impact of taxes on people and businesses deciding whether to live, invest and create jobs here.

A lot was accomplished in the last legislative session, including passage of a balanced budget and a much-needed infrastructure program. Yet despite the passage of legislation designed to provide the state with additional revenue, including from the proposed graduated income tax, there is no plan to deal with the state's credit rating or its massive pension debt. To put it plainly, Illinois has a tax plan without a fiscal plan.

The veto session later this year will provide another chance to address unfinished business. The administration and Legislature should use this opportunity to pursue a broad fiscal plan that will show Illinois is serious about tackling its fundamental financial challenges and reduce the uncertainty and apprehension about the state's direction.

We must change the reality of the state's fiscal condition to change the narrative about our state. We look forward to continuing to work with the state's leadership to develop constructive solutions for the state's fiscal condition so that Illinois can reach its full potential as a world-class place to live, work and do business.

CRAIN'S FORUM PENSIONS

How Arizona, Rhode Island broke the mold

BY JUDITH CROWN

While few states face an underfunded-pensions problem as dire as Illinois', those lauded for enacting reforms have defied the odds in instructive ways, even if the details are not directly applicable elsewhere.

In Arizona, a traditionally conservative state where labor isn't as powerful as in the East and Midwest, unions stepped outside their traditional stance and pushed for a solution, endorsing an amendment to constitutional restrictions that stood in the way. They teamed up with a libertarian think tank.

"YOU HAVE TO TAKE THE EMOTION OUT."

Leonard Gilroy, Reason Foundation

In Rhode Island—as Democratic as Illinois, though considerably smaller—reform was spearheaded with single-minded determination by then-state Treasurer and now Gov. Gina Raimondo with an assist from a state Superior Court judge who ordered the two sides to work out their differences.

Those involved say it's an undertaking that requires uniquely motivated leaders adept at relentlessly communicating the risks and rewards to their constituents and persistent and flexible enough to navigate contentious negotiations.

"You have to get people in a room," says Leonard Gilroy, vice president of government reform at the Reason Foundation, the Los Angeles-based libertarian group that consulted on Arizona's negotiations and helped defend workers' benefits. "You have to take the emotion out and turn it into a technical discussion rooted in people's shared interests."

Arizona voters last fall adopted the second of two amendments to a state constitution clause that prevents state worker benefits from being "diminished or impaired." A comparable clause in the Illinois Constitution resulted in the state Supreme Court striking down a 2013 reform attempt by the General Assembly.

The Arizona referendum enabled the state to change an arcane formula that determined cost-of-living increases for elected officials and corrections officers based on their fund's investment returns. That formula had siphoned off gains made during robust stock markets so that less money was left for lean times, occasionally leaving workers with no cost-of-living increases. The amendment substituted a formula tied to the cost of living in Arizona, capped at 2 percent.

An earlier amendment approved the change for police and firefighters. The Arizona Legislature also approved a new statewide system for firefighters and police officers hired after 2012 in which employee contribution costs are shared evenly with employers.

OVERCOMING OBSTACLES

In several ways, the Arizona initiative was easier than an amendment some are demanding in Illinois: The referendum was intended to shore up the funds' solvency without directly reducing worker or retiree benefits, which might have triggered a legal appeal based on federal law that protects contracts. It's also easier to pass a constitutional amendment in Arizona, with simple majorities required, whereas Illinois requires three-fifths votes. But reform proponents still cite Arizona for demonstrating the joint will to overcome its obstacles.

The initial impetus for reform came from the firefighter and police unions. The original investment mechanism had taken out half the gains over 9 percent, "and there's no way the retirement system could recover," says Jim Mann, chair of the state Fraternal Order of Police's legislative committee.

The unions' thinking, according to Scott McCarty, chair of the League of Arizona Cities & Towns public-safety pension reform task force, was, "Let's solve this ourselves rather than have somebody else solve it for us."

The fire and police unions worked with a bipartisan legislative task force that included town and city employers. McCarty, finance director in the Phoenix suburb of Queen Creek, says the employers allowed the unions to take the lead and develop their own criteria for evaluating proposals, "so it wasn't their plan versus our plan," he says.

The unions had been pressured to make concessions, but their cause was bolstered by the libertarians at the Reason Foundation. "They said, 'You can't change benefits for people already here,' " the FOP's Mann says. "The legislators trusted them. That was different from labor saying, 'You can't do that.' "

All participants then agreed to the referendums for the narrow purpose of adjusting the retiree benefit calculator, under which retirees are better off, Mann says. That clearly defined goal made reform easier as compared to the more sweeping changes some are pursuing in Illinois.

In Rhode Island, then-Treasurer Raimondo and Gov. Lincoln Chaffee in 2011 created a 12-member pension advisory group, whose recommendations led to the Legislature's passage of a reform bill not dissimilar to elements in Illinois' 2013 law that was later struck down.

"Raimondo was courageous politically," says Sarah Anzia, a political science professor at the University of California, Berkeley, who has studied government pensions. Raimondo, a venture capitalist, was rewarded by being elected governor in 2015, although union opponents "continued to make things difficult," Anzia says.

Rhode Island did not face the same constitutional restrictions. When unions filed lawsuits, the judge in the case ordered talks under the supervision of a federal mediator. A settlement covering about 100 municipal plans was ratified in 2015 and upheld by the state Supreme Court last year.

The settlement preserved 95 percent of the reforms, says Evan England, a spokesman for current state Treasurer Seth Magaziner. The final package froze cost-of-living increases for retirees, and senior workers were required to contribute more to their defined-benefit plans.

Reforms didn't reverse the woes of the pension systems overnight. Both Arizona's and Rhode Island's plans still are funded only in the 50 percent range, though on a quicker path to full funding.