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Saving Illinois: Getting More Bang for the State's Bucks.

Illinois is teetering on bankruptcy and other states are not far behind, largely due to unfunded pension liabilities; but there are solutions. The Federal Reserve could do a round of "QE for Munis." Or the state could turn its sizable pension fund into a self-sustaining public bank.

Illinois is insolvent, unable to pay its bills. According to Moody's, the state has $15 billion in unpaid bills and $251 billion in unfunded liabilities. Of these, $119 billion are tied to shortfalls in the state's pension program. On July 6, 2017, for the first time in two years, the state finally passed a budget, after lawmakers overrode the governor's veto on raising taxes. But they used massive tax hikes to do it – a 32% increase in state income taxes and 33% increase in state corporate taxes – and still Illinois' new budget generates only $5 billion, not nearly enough to cover its $15 billion deficit.

Adding to its budget woes, the state is being considered by Moody's for a credit downgrade, which means its borrowing costs could shoot up. Several other states are in nearly as bad shape, with Kentucky, New Jersey, Arizona and Connecticut topping the list. U.S. public pensions are underfunded by at least $1.8 trillion and probably more, according to expert estimates. They are paying out more than they are taking in, and they are falling short on their projected returns. Most funds aim for about a 7.5% return, but they barely made 1.5% last year.

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Published on Monday, July 24, 2017 by Common Dreams

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