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Fitch: Illinois Securitization Structures Not Subject to State Revenue Diversion.

Fitch Ratings-New York-03 May 2018: Tax revenues sold to corporations such as Chicago's Sales Tax Securitization Corp. (STSC) are not at risk of diversion under the Illinois Pension Code, according to Fitch Ratings. Under a 2017 revision to the Illinois Municipal Code, home rule municipalities can sell revenues or taxes received from the state to not-for-profit corporations that serve as financing vehicles.

These entities, which include STSC (sales tax bonds rated AAA/Stable) and The Bridgeview Finance Corp. (sales tax securitized bonds rated BBB+/Stable) have no pension obligations and therefore there is no legal basis by which their revenues would be diverted by the state comptroller. In fact, under the municipal code the state pledges not to limit or alter the rights and powers vested in the state comptroller, treasurer or department of revenue that would impair any contract made by the transferring unit with the issuing entity, including contracts executed in connection with the issuance of debt. The state also pledges not to alter the basis on which the transferring unit's share or percentage of receipts transferred to the issuing entity is derived.

Recent changes to the Illinois Pension Code, made prior to the revision of the municipal code, require payments to municipal pension plans to be based on actuarial formulas. Previously, the annual required contributions were based on a percentage of payroll, unrelated to pension funding status. Provisions of the revised pension code require the state comptroller to deduct any portion of the required contribution not paid by the municipality from its allocation of state funds. The proportion that could be deducted ramped up from one-third of the amount received from the state in fiscal 2016 to 100% beginning in fiscal 2018, up to the amount of the delinquent payment. This legislation has recently become a topic of discussion, as the state comptroller diverted $7 million in funding for the city of Harvey to the police pension fund, resulting in significant layoffs. The diversion is being litigated. Harvey has dedicated tax bonds outstanding but the city continues to own the pledged revenues.

Revenues sold through securitizations are not subject to diversion in the event the transferring unit underfunds public safety pension contributions. However, transferring units are still at risk of having other funds diverted in this case. For example, if the city of Chicago (Issuer Default Rating of BBB-/Stable) were to fail to fully fund required contributions to its police and fire pensions, the sales taxes that were sold to the STSC would not be available but the comptroller could divert funds for pension contributions from certain sources otherwise due to the city as designated in the pension code. Fitch expects the city will adhere to its plan to fully fund the pension contributions required by state law.

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