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## **Chicago's Unmentionable Pension Solution Haunts Mayoral Election.**

(Bloomberg) — Chicago could avert financial doom with a new casino or an expanded sales tax. Or it could relieve the pressure from \$20 billion in pension debt by slapping a levy on commuters.

As the city's credit rating slides toward junk status, the most direct remedy to dodge the threat of insolvency — raising property taxes — is barely mentioned by the two men vying to run Chicago in the next four years.

In the race for mayor, to be decided in an April 7 run-off, Mayor Rahm Emanuel and his challenger, Jesus "Chuy" Garcia, are treating the option as political poison even though it may be inevitable.

"My plan specifically avoids increasing property taxes," Emanuel, 55, said in a March 16 debate, promoting a broader sales tax and the casino.

Garcia, too, supports expanding the sales levy, and suggested in a debate Thursday night that the city consider a luxury tax on some purchases by higher wage earners. He also says Chicago first needs performance audits to assess its financial situation.

"Difficult decisions, hard decisions are going to have to be made," Garcia said in the latest debate.

Both candidates have stopped short of issuing irrevocable declarations against boosting property taxes. Yet their political discomfort is a tribute to the enduring public furor over such levies, about four decades after California sparked a nationwide revolt against the largest source of local-government income.

### **Recession Whammy**

The sensitivity resonates in cities like Chicago, where the double-whammy of the recession and foreclosures cut home values by an average 24 percent from their peak in 2003, according to a study by DePaul University.

While proposing a property-tax boost may be abhorrent before the election, after the vote is a different matter. Even as Emanuel, mayor since 2011, and Garcia, a 58-year-old Cook County commissioner, try to distance themselves from it, an increase has taken on a sense of inevitability.

"I believe we can truly say that it will happen, but it is all in how much," Chicago Alderman Carrie Austin, an Emanuel supporter and chairman of the City Council's budget committee, said this month.

"That's a bullet that we will have to bite because we have to right our ship," Austin said.

### **Credit Deterioration**

Investors who have watched the city's credit standing deteriorate say there's no choice if Chicago is to corral the cost of pension liabilities — the annual payment will swell to \$1.1 billion, from \$480

million this year. Moody's Investors Service cut its \$8.3 billion of general obligations to Baa2 last month, two steps above junk, citing the retirement expenses. Chicago can't reduce workers' retirement benefits without state legislative approval.

"Limitations on benefit reforms will likely leave large tax increases as the only viable solution, a challenge given the city's historical reluctance to tap its property tax base," Matt Fabian, a partner at Concord, Massachusetts-based research firm Municipal Market Analytics, said in a March 16 report.

Chicago isn't master of its financial destiny. State legislators would have to approve a tax on the 600,000 commuters who work in the city, or any effort to impose an income tax.

Emanuel, former chief of staff for President Barack Obama, floated a \$250 million property-tax boost last year to pay for pension obligations. He dropped the plan in the face of City Council opposition, and is taking a different route this time. He's proposing to build a casino, dedicating the revenue to retirement debt, and extend the sales tax to services. Again, he can't do either without state approval, and even with that consent, the casino wouldn't be built in time to contribute to next year's pension payment.

### **Direct Control**

A property-tax increase, though, is within the city's direct control. The levy generated \$824 million last year, equivalent to about 9 percent of this year's spending plan, according to Chicago's annual financial analysis.

The population of the nation's third-most-populous city fell 7 percent in the last decade to 2.7 million, according to the Census Bureau. The drop increases pressure on the tax base to pay for retirement commitments, some made decades ago.

"The problem is you're paying the bills of the city of 30 years ago with today's population," said Norton Francis of the Tax Policy Center in Washington. "That's a huge challenge for cities."

### **Tax Burden**

In Chicago, property taxes have risen even as housing values dropped. The effective tax rate jumped 32 percent from tax year 2003 to 2012, according to the Civic Federation, a nonprofit research group specializing in government finance.

Although the national recession ended in 2009, housing values in parts of the South Side have yet to recover, according to the Institute for Housing Studies at DePaul University. The area is home to many mostly black precincts, where Emanuel's support has dropped relative to the 2011 election.

Opposition to property taxes is part of the campaign dialogue. Emanuel criticized Garcia for a vote he cast in favor of a higher levy — in 1986.

Credit analysts and rating companies want Chicago to enact sustainable solutions, not patchwork fixes, to its financial woes, said Paul Mansour, head of municipal research at Conning, which oversees about \$11 billion in municipal debt, including Chicago holdings.

"As much as property-tax increases are abhorred by residents, we in the municipal community prefer them because they're easier to predict," said Mansour, who's based in Hartford, Connecticut.

"It's hard to imagine a situation where increases in the property taxes are not some part of the

equation,” he said.

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