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Chicago Says Banks Won't Demand Penalties After Cut to Junk.

Chicago said Bank of America Corp., Goldman Sachs Group Inc. and other banks won't force it to pay penalties triggered when its credit rating was cut to junk by Moody's Investors Service, giving the city time to refinance debt.

In bond documents released Thursday, Chicago said it reached an agreement with banks that backstop its general-obligation bonds and sold it interest-rate swaps. The city said they won't demand penalties before Sept. 30, unless it can't refinance the floating-rate debt by June 8 or Moody's lowers the rating again.

The agreements provide time for Mayor Rahm Emanuel to bolster the city's finances after downgrades from the three biggest credit-rating companies. Chicago plans to sell about $806 million of bonds next week. It had planned to issue $383 million on May 19, but delayed the sale as investors demanded increasingly higher yields.

The loss of an investment-grade rating threatened to put added pressure on Chicago by giving banks the right to require it to repay debt early or pay fees to break swap contracts. Moody's said Chicago faced as much as $2.2 billion in such penalties.

Kristen Kaus, a spokeswoman for Bank of America in New York, declined to comment on the agreement. Michael DuVally, a spokesman for Goldman Sachs, which has a swap agreement with Chicago, also declined to comment.

Eliminating Risk

Emanuel's administration had already been planning to avoid the penalties with the refinancing that's now set for next week.

So far, it has used short-term borrowing and other city funds to pay about $139.5 million to break swaps, including one with Bank of New York Mellon Corp. on May 19, according to the bond documents released Thursday.

The city has also been able to secure more credit from some banks. JPMorgan Chase & Co. and Morgan Stanley will each provide an additional $200 million to Chicago, according to the documents. A unit of Bank of America, the lead underwriter on $423 million of planned Chicago deals, has an existing revolving line of credit with the city.

Chicago was cut to junk by Moody's after the Illinois Supreme Court ruled that retirement benefits are safeguarded under the state constitution. That cast doubt on Chicago's ability to plug a $20 billion pension shortfall that threatens the city's solvency.

Bloomberg

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May 21, 2015