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Moody's Explains Itself.

Last week, a court ruling struck down Illinois' pension changes, and days later, Moody's Investors Service downgraded the Chicago's (but not Illinois') debt to junk status. Moody's phones must have been ringing off the hook. So this week, in an unusual move, it released an FAQ regarding the downgrade of the city and not the state.

Moody's said in the May 18 document that it didn't downgrade the state because Illinois has more flexibility and isn't in as tight a financial predicament as Chicago. Illinois had not yet enacted its pension law so it wasn't incorporated into its credit rating. Chicago's pension law, which cuts retiree benefits, is also tied up in a legal battle and has yet to be enacted, but Moody's said the recent state-level ruling will lead to a reversal of that law. That, Moody's said, leaves the Windy City left only with the option of increasing its payments into the pension plan to keep it solvent — a feat that will require considerable cash for a city that's already heavily leveraged. Illinois, on the other hand, has potentially other options, Moody's said. The agency added that the Supreme Court could have ruled more narrowly and said that benefit modifications are permissible under certain circumstances, which would have been more favorable for Chicago's own hopes at reducing its pension liabilities.

"Instead, our interpretation of the court's opinion is that benefit modifications are impermissible under any circumstances," Moody's said. "Given the stridency of the court's opinion, we believe that the opportunities for benefit reform are now significantly more limited."

Moody's also said that while Chicago has a strong economy, immense tax base (\$187 billion) and population (2.7 million), its "overall debt and unfunded pension liabilities are very high compared to other major U.S. cities." Any future ratings changes for Chicago — for better or worse — will "largely reflect city officials' actions on pension contributions and, ultimately, the growth of debt and pension leverage on the city's balance sheet." The agency also clarified it doesn't think Chicago is at risk of defaulting on debt or declaring bankruptcy.

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