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Chicago Public Worker Pension Reform Plan Found Illegal.

A plan to ease Chicago's \$20 billion public-worker pension deficit is illegal, an Illinois judge ruled, leaving the city vulnerable to another credit downgrade.

Immediately after the ruling, Standard & Poor's said it would probably lower the city's rating again if a solution isn't found. S&P already cut Chicago's rating earlier this month to BBB+, or three levels above junk.

The Illinois Constitution bars the diminishing of public pensions, state court judge Rita Novak ruled Friday. The Illinois Supreme Court in May killed similar changes to the state's pension funds for the same reason.

Rejection of the state plan led within a week to a downgrade of Chicago credit to junk status. Chicago's pensions will be broke in about 10 years without the plan, city lawyers argued before the ruling.

The city's pension plan and the one covering state workers both envisioned cuts in future cost-of-living increases. Chicago argued that its plan was different from the state's because it increased city funding of pension funds and the Illinois measure only reduced benefits.

Novak rejected the city's arguments.

General Assembly

The state constitution "affords the participant protection against" cuts in benefits even if the general assembly changes the pension code, the judge wrote in her 35-page ruling.

The city will appeal to the state supreme court, Chicago's lawyer said after the ruling.

"We continue to strongly believe that the city's pension reform legislation, unlike the state legislation held unconstitutional this past spring, does not diminish or impair pension benefits, but rather preserves and protects them," Stephen Patton, a lawyer for the city, said in an e-mailed statement.

The American Federation of State, County and Municipal Employees Council 31, one of the plaintiffs in the suit, urged the city in an e-mailed statement "not to take up further time and expend additional taxpayer dollars on an appeal of today's decision."

Job Cuts

The court fight over pension reform comes as the city and state face increasing financial pressure. Chicago's public school system is eliminating 1,400 jobs. Illinois' retirement fund has a \$111 billion shortfall. And the state is operating without a budget because of stalemate between Republican Governor Bruce Rauner and the Legislature's Democratic leadership.

The pension system in Chicago is \$20 billion short and is only 36 percent funded, compared with 61 percent in 2005.

Chicago's measure, signed into law last year, restructured the pensions of laborers and municipal workers, requiring employees and the city to pay more into the plan while benefits are reduced. The pension plans for fire and police retirees weren't affected.

The city reform was developed in negotiations with 28 of 31 affected unions, Mayor Rahm Emanuel said in May. The employees had a "full funding guarantee," the city said. Union-backed beneficiaries sued on behalf of retirees and employees to block the reform.

Truck Driver

The plan didn't have the support of pensioners, Charles Lomanto, a retired truck driver for the city of Chicago, told reporters outside Novak's courtroom Friday.

Under the plan, which took effect Jan. 1, pensioners lost all but .85 percent of an expected 3 percent increase in benefits, Lomanto said. Meanwhile, Lomanto said, his health insurance premium costs rose to \$1,300 a month from \$740.

"Rahm never came to retirees and said, 'Hey, can we talk?'" Lomanto said. "Unions can't negotiate on behalf of retirees."

The rejection leaves Chicago with no viable plan to solve the pension deficit, said Sarah Wetmore, vice president and research director at the Civic Federation, a Chicago nonprofit that tracks municipal finance.

"Without these reforms, the city reverts back to an inadequate funding formula that has resulted in such severe underfunding that actuaries expect the Municipal and Laborers Funds will run out of money within the next decade -- an unthinkable prospect," she said.

'Credit Neutral'

Moody's Investors Service called the ruling "credit neutral" for Chicago because of the expected appeal to the state supreme court.

"The ruling is one step forward in the process of resolving outstanding questions on the constitutionality of the 2014 legislation," Matt Butler, assistant vice president and Moody's lead analyst for Chicago, said in an e-mailed statement.

Chicago's financial woes and credit downgrades have burdened the city with higher borrowing costs as investors demand larger yields, relative to top-rated bonds, to buy its securities.

Yields on some Chicago bonds are close to the highs reached when Moody's Investors Service cut the city's rating to below investment grade in May after the Illinois Supreme Court struck down the state's pension overhaul.

The price of a taxable Chicago bond maturing in 2042, the most actively traded city security Friday, was little changed at 99.2 cents on the dollar. The securities yield 7.8 percent, almost 5 percentage points above benchmark Treasuries, according data compiled by Bloomberg.

Supreme Court

“Barring a reversal at the supreme court, this puts us back to square one on pension reform in Chicago,” said Richard Ciccarone, Chicago-based chief executive of Merritt Research Services LLC, which analyzes municipal finances. “Now the pressure on the city to come up with a solution here that won’t unduly burden taxpayers, and at the same time achieve some level of reform is going to be challenging.”

The case is Jones v. Municipal Employees Annuity and Benefit Fund of Chicago, 2014CH20027, Circuit Court, Cook County, Illinois, Chancery Division (Chicago).

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by Margaret Cronin Fisk

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