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Chicago Tax Increase Spurs Bond Rally as Pension Debts Lingers.

Chicago Mayor Rahm Emanuel pushed through the biggest property-tax increase in the city's history to help pay its annual pension-fund bills. Eliminating the \$20 billion debt to retirees that's pushed its bond rating to junk will still have to wait.

The city's aldermen Wednesday voted 35 to 15 to boost real-estate levies by \$543 million over the next four years. Emanuel, a Democrat who won re-election this year, said it will steady the city's finances and avoid the need for police and firefighter layoffs.

The push has driven a rebound in the price of Chicago's bonds, which tumbled after Moody's Investors Service in May pulled the city's investment-grade rating because of escalating retirement costs. It marks one of the strongest efforts yet to deal with financial pressure that built over the past decade as Chicago shortchanged employees' pensions by billions, even though it may do little to cut the obligation that was left behind.

"No one should think that as a result of passing this property-tax increase and this budget that the city has accomplished stabilization of the pension funds or its overall finances," said Laurence Msall, president of the Civic Federation in Chicago, who supports the tax increase, calling it a positive, needed step. "That is going to have to be worked on and evaluated every year going forward."

Chicago has contributed \$7 billion less than actuaries recommended over the last decade, which by last year left the public-safety, municipal and laborers funds with about 35.5 percent of what they need for retirement checks that will be due in the coming decades, city documents show. As the annual payments rise, the squeeze that has been put on the budget triggered a series of downgrades this year that have left Chicago with a lower rating than any big city except Detroit.

The tax will be increased by \$318 million in 2015, followed by additional jumps of \$109 million in 2016, \$53 million in 2017 and \$63 million in 2018. The funds will go to the police and firefighter pensions.

Emanuel praised the "decisive and determined" action by the council to address years of deferred payments and rising costs.

"I do believe the city of Chicago's public finances are more secure, more stable, and stronger today than they were before," Emanuel told reporters at City Hall after the passage of the real-estate levies and his \$7.8 billion spending plan for 2016.

The uncertainty surrounding Chicago's finances has been heightened by a political impasse in Illinois's state capital, where Republican Governor Bruce Rauner and the Democrat-led legislature have been unable to pass a budget for the year that started four months ago. Emanuel has been counting on a law that would cut the city's 2015 contribution to the public-safety pensions to \$619 million from current law's \$840 million.

While lawmakers passed the bill in May, they haven't sent it to the governor for his signature.

Kicking Can

Rauner in June called the plan "a kick the can down the road pension bill" without saying what he would do. Catherine Kelly, his spokeswoman, referred to those comments when asked whether he would sign it.

The nascent effort by Chicago to cope with the retirement strains has been welcomed by investors and credit-rating companies. Fitch Ratings called Emanuel's budget a "positive credit development." A portion of Chicago's general-obligation bonds due in 2035 traded for an average of 98 cents on the dollar Tuesday to yield 5.2 percent. That price is up from 84 cents on May 18, soon after Moody's cut the city to junk.

"Undoubtedly it's the responsible thing to do," said Ty Schoback, a senior analyst in Minneapolis at Columbia Threadneedle Investments, whose company manages about \$30 billion in municipal bonds, including some Chicago debt. "At the end of the day, businesses and individuals just want to see that government is making steps toward stabilizing their financial situation."

Emanuel has sought to shelter lower-income residents from the impact of the tax increase. His administration has asked Illinois lawmakers to allow Chicago to double the homestead exemption to \$14,000. A bill that would do so was approved by a House committee last week.

Business groups argued that the higher taxes will punish employers already affected by a higher minimum wage that Emanuel championed. In January, Chicago will also have the highest sales tax in the nation because of an increase taking effect in Cook County, which needs to stem its own pension crisis.

"It's another expensive burden," said Michael Reeve, vice president of government relations at the Chicagoland Chamber of Commerce. "It's not good for the overall economic climate of the city, county and state to shift more of that responsibility and costs of these mandates onto businesses."

Still Short

While the property tax increase shows that Chicago is willing to deal with its obligations, its annual payment is still "significantly short" of what actuaries would likely recommend, said Richard Ciccarone, chief executive officer of Merritt Research Services.

Chicago has budgeted \$978 million in 2016 for its four pensions, up from \$885.7 million in 2015, according to city documents. That still falls behind the 2014 actuarially-required contribution of \$1.7 billion, according to bond documents.

"Taxpayers are going to be paying for past service for years to come after they've been retired," said Ciccarone, who is based in Chicago. It's "falling short while they leave a burden for the future."

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