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Fitch: Cook County, IL Budget Includes Novel Pension Funding Approach.

Fitch Ratings-New York-19 November 2015: The Cook County, IL ('A+' /Negative Outlook) fiscal 2016 budget, which was approved by the county commission yesterday, includes an alternative pension funding mechanism that Fitch Ratings believes has the potential to advance the discussion on appropriate funding of public pensions in Illinois.

The county's pension strategy is notable, as it includes actuarially determined funding of the pension liability, but appears to ignore the restrictions imposed by the current pension statute, leaving the county vulnerable to potential litigation from taxpayers challenging the increased payments.

Fitch will monitor these developments closely to assess the impact on long-term credit quality. The Negative Outlook incorporates Fitch's concerns including those surrounding the county's ability to implement an affordable plan to shore up pension funding. This plan, if it survives legal testing, could address those concerns; but if legal challenges invalidate it, the county will again become reliant upon state legislative action to improve pension funding.

County administrators drafted a pension reform proposal, which included changes to the benefit structure and actuarial funding of pensions, but were unable to gain state legislative support for passage. Structural changes to pension plans, including changes to funding, require state legislation in Illinois. The fiscal 2016 budget includes a modified version of the pension reform plan, excluding the benefit structure changes, but retaining the actuarial funding aspect. Fitch occasionally sees local governments seeking to pay more than their legally required amount, but rarely significantly more, as Cook County is doing.

Under an intergovernmental agreement between the county and the pension fund, the county contracts to make payments on an actuarial basis, using a 30 year layered amortization structure, with future payments subject to annual appropriation by the county board of commissioners. The statutory pension payment required under existing law of \$195 million for fiscal 2016 is payable from a separate property tax levy dedicated to pensions. The county is planning to make an additional payment of \$270.5 million in fiscal 2016 and \$340 million in fiscal 2017. After that, it anticipates the amount of the additional payment will rise by a manageable 2% annually through 2046.

The additional contributions will be funded by a 1% increase in the county sales tax. With this change, the county's portion of the 10.25% sales tax will be 1.75%. The increase will be effective Jan. 1, 2016 and is budgeted to provide \$308 million in fiscal 2016 (representing eight months of collections) and \$473.8 million in fiscal 2017 (full year of collections). In addition to the supplemental pension payments, the sales tax increase is budgeted to provide funding for several other priorities, including highway funding to address deferred maintenance, increased debt service costs, and pay-go technology implementation. Total general fund expenditures, net of the supplemental pension payment, are budgeted to increase by a modest 2.2%.

Contact:

Primary Analyst
Arlene Bohner
Senior Director
+1-212-908-0554
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Eric Friedman
Director
+1-212-908-9181

Tertiary Analyst
Shannon McCue
Director
+1-212-908-0593

Media Relations: Sandro Scenga, New York, Tel: +1 212-908-0278, Email:
sandro.scenga@fitchratings.com.

Additional information is available at 'www.fitchratings.com'.

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