[Fitch Rates $500MM Chicago Board of Ed (IL) Bonds 'A' on Special Revenue Analysis; Outlook Stable.](#)

Fitch Ratings-New York-08 December 2016: Fitch Ratings has assigned an ‘A’ rating to the following Chicago Board of Education, IL bonds:

–$500 million dedicated capital improvement tax bonds, series 2016.

The bonds are expected to price the week of Dec. 12. Proceeds will finance specific capital projects listed in the authorizing resolution.

The Rating Outlook is Stable.

The Board of Education’s Issuer Default Rating (IDR) is ‘B+’ with a Negative Rating Outlook. The distinction between the ‘A’ rating on the series 2016 bonds and the ‘B+’ IDR reflects Fitch’s assessment that the pledged revenues meet the definition of “special revenues” under the U.S. Bankruptcy Code and therefore, bondholders are legally insulated from any operating risk of the board.

SECURITY
The bonds are secured by a first priority lien on revenues from the capital improvement tax (CIT), a district-wide property tax.

KEY RATING DRIVERS

SPECIAL REVENUE ANALYSIS: The ‘A’ rating on the dedicated CIT bonds is based on a dedicated tax analysis without regard to the board’s financial operations. Fitch has been provided with legal opinions by board counsel that provide a reasonable basis for concluding that the tax revenues levied to repay the bonds would be considered ‘pledged special revenues’ under Section 902(2)(e) of the U.S. Bankruptcy Code in the event of a board bankruptcy.

PREDICTABLE REVENUES: Growth in the levy (currently $47.9 million) is set by state statute at the rate of inflation; however, the levy jumps up in 2033 by $142.5 million, then resumes inflation-based growth. Debt service schedules are sized to the minimum levy, without assuming inflationary increases.

STRONG RESILIENCE OF PLEDGED TAX SECURITY: A multi-year levy with pre-determined minimum amounts combined with limited volatility in historical property tax collection rates support strong financial resilience for debt service coverage throughout economic declines.

RATING SENSITIVITIES

PROPERTY TAX COLLECTION RATES: The rating is sensitive to declines in property tax collection rates of a scale that would materially erode the protection inherent in the expected coverage ratios, given the fixed-dollar levy, 1.1x additional bonds test and moderate historical delinquency experience.

CREDIT PROFILE

The Chicago Board of Education provides preK-12 education to over 390,000 students within the city of Chicago. Its taxing jurisdiction is coterminous with the city of Chicago. The Chicago Public Schools (CPS) manages the school system, which is composed of 673 school facilities.

CIT VIEWED AS SPECIAL REVENUES

The specific features of the bonds meet Fitch's criteria for rating special revenue obligation debt without consideration of the board's general credit quality. Fitch believes bondholders are effectively insulated from the operating risk of the board as expressed in its IDR.

Fitch sets a high bar for considering local government tax-supported debt to be secured by special revenues, which provide security that survives the filing of a municipal bankruptcy (in preservation of the lien) and benefit from relief from the automatic stay provision of the bankruptcy code. We give credit to special revenue status only if, in our view, the overall legal framework renders remote a successful challenge to the status of the debt as secured by special revenues under Section 902 (2) (e) of the U.S. Bankruptcy Code.

Fitch has identified a number of elements we consider sufficient to reduce the incentive to challenge the special revenue status given the definitions outlined in the bankruptcy code. These include clear restrictions on the use of pledged revenues for identified projects and clear separation from the entity's operations. Fitch has undertaken an extensive review of the statutory provisions that govern the use of the CIT. Those provisions, along with the legal documents governing the bond issuance, provide sufficient strength for Fitch to rate the CIT bonds higher than the IDR.

The bonds are secured by a first priority lien on CIT revenues. The board is authorized under the Illinois School Code to levy the CIT on all taxable property within the district, which is coterminous with the city of Chicago. State statute limits the permitted uses of CIT revenues to include construction, acquisition and equipping of school and administrative buildings, and site improvements. The board has identified specific capital projects in the bond resolution that may be funded either by bond proceeds or by residual CIT revenues. Any amendments to the project list must be passed by board resolution. The revenues legally cannot be used for general operations of the board.

STRONG RESILIENCE OF PLEDGED CIT SECURITY

The multi-year levy supporting debt service on the bonds required and received approval by the Chicago city council; however, no further approvals are necessary for the levy to be extended and collected for the life of the bonds. The multi-year levy is set by resolution at the time of bond issuance and no policy action is required to offset potential declines in assessed value. Importantly, the minimum amount of the levy is knowable in advance and the debt service schedule is sized to that, allowing for a minimum of 1.1x coverage. This leaves only the risk of diminishing collection rates, which historically have been well within the norm for U.S. municipalities.

To evaluate the sensitivity of the dedicated revenue stream to cyclical decline, Fitch considers both revenue sensitivity results (using a 1% decline in national GDP scenario) and the largest decline in revenues over the period covered by the revenue sensitivity analysis. Since the CIT revenue history is insufficient to conduct this analysis, Fitch uses a proxy of overall property tax collection rates, which it believes approximates future risk to CIT revenue sufficiency.
Based on historical property tax collection rates, Fitch's Analytical Sensitivity Tool (FAST) generates a fairly modest 1.7% scenario decline in pledged revenues. The largest cumulative decline was a 2.7% decline during the recession between 2008 and 2009.

Given the 1.1x coverage, pledged revenues could withstand a 9% decline before they were insufficient to fully cover debt service. This is 3.3x the largest actual cumulative decline, or 5.3x the recessionary impact estimated in Fitch's FAST scenario. Recent tax increases by Chicago-area governments could contribute to delinquencies beyond historical experience in a recession, but even so, Fitch believes collection rates would continue to support financial resilience consistent with an 'A' rating.

Chicago acts as the economic engine for the Midwestern region of the United States. The city's residents are afforded abundant employment opportunities within this deep and diverse regional economy. The city also benefits from an extensive infrastructure network, including a vast rail system, which supports continued growth. The employment base is represented by all major sectors with concentrations in the wholesale trade, professional and business services and financial sectors. The city's economic indicators are mixed with elevated individual poverty rates and average per capita income levels, but strong educational attainment levels. Recovery from the recession has been slow but steady. The unemployment rate is almost half of its recessionary peak but remains elevated relative to the state and nation. Population losses appear to have reversed.

ADEQUATE STRUCTURAL PROVISIONS
The additional bonds test dictates that projected CIT revenues must provide at least 1.1x coverage of annual debt service in each bond year. Projections may not include assumptions for inflationary increases prospectively. Fitch's analysis assumes the pledged revenues would be leveraged to the full extent allowable under the additional bonds test.

Under the flow of funds, the CIT revenues are collected by the county collectors of Cook and DuPage Counties. The board has directed the collectors to transmit the CIT revenues directly to an escrow agent. The escrow agent transfers revenues needed for payment of debt service to the bond trustee daily. Revenues in excess of those required to meet annual debt service may be available to reimburse CPS for authorized capital expenditures.

The board covenants not to revoke the direction to the county collectors as long as the bonds are outstanding. Based upon review of bond counsel opinions Fitch believes that any future attempt to revoke the direction to the county collectors would be contrary to state statute.

The debt service reserve requirement of 14% of maximum annual debt service (MADS) will be funded with bond proceeds.

The board's 'B+' IDR with a Negative Outlook reflects CPS's chronic structural imbalance, slim reserves and weak liquidity position which are exacerbated by rising long-term liability costs, an historically acrimonious labor relationship and the lack of an independent ability to raise revenues. For more information on the board's IDR, please see 'Fitch Rates $426MM Chicago Board of Education (IL) ULTGOs 'B+'; Outlook Negative' dated Nov. 7, 2016.

Contact:

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

Secondary Analyst
Amy Laskey
Managing Director
+1-212-908-0568

Committee Chairperson
Laura Porter
Managing Director
+1-212-908-0575

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at ‘www.fitchratings.com’.

Copyright © 2025 Bond Case Briefs | bondcasebriefs.com