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Junk-Rated Chicago Schools Plan New Kind of Bond Issue.

CHICAGO — Chicago’s public school (CPS) system plans to sell a new type of bond issue in an attempt to separate the debt from the district’s severe financial woes and protect it in a potential bankruptcy filing, according to a document released by the district on Tuesday.

The preliminary prospectus for the debt indicates the Chicago Board of Education will issue \$500 million of bonds secured solely by a capital improvement property tax and not by the district’s general obligation pledge.

That pledge currently covers about \$6.8 billion of existing bonds that are rated junk by Moody’s Investors Service, S&P, and Fitch Ratings.

CPS, the nation’s third-largest public school system, is struggling with pension payments that will jump to about \$720 million this fiscal year from \$676 million in fiscal 2016, as well as drained reserves and debt dependency - factors that have pushed its GO credit ratings deep into the junk category and led investors to demand fat yields for its debt.

Illinois Governor Bruce Rauner last week vetoed a bill to give CPS a one-time \$215 million state payment to help cover pension costs.

Ratings for the new bonds, backed by a \$45 million a year property tax levy approved by the Chicago City Council in 2015, were not available. Because that tax revenue can only be used to fund capital projects and not operations, CPS is hoping bondholders will consider the debt a safer bet than the district’s GO bonds.

A CPS spokeswoman could not immediately be reached for comment.

CPS cannot currently file for municipal bankruptcy in Illinois, although there have been attempts to change state law to allow such a move. The prospectus includes legal opinions on a “hypothetical bankruptcy” by CPS that conclude payments on the new bonds would not be automatically stopped by a federal bankruptcy court and that bondholders would retain a lien on the tax revenue.

The prospectus was released a day before the schools’ governing board, appointed by Chicago Mayor Rahm Emanuel, votes on an amended fiscal 2017 budget to account for a new contract with teachers. The bond issue is tied to a bigger capital plan CPS announced last week.

The bonds, to be priced through Barclays and J.P. Morgan, carry term maturities in 2036 and 2046.

By REUTERS

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(Reporting by Karen Pierog; Editing by Matthew Lewis)

