STATEMENT MADE AT THE PUBLIC HEARING ON THE PROPOSED FY1999 CITY OF CHICAGO BUDGET, NOVEMBER 4, 1998, BY THE CIVIC FEDERATION

The Civic Federation would like to thank the Mayor and the members of the City Council for this opportunity to comment on the proposed FY99 budget. As a government and finance watchdog group, The Civic Federation has closely monitored and commented on the fiscal health of local area governments for over 100 years.

OVERVIEW

The following is an overview of The Civic Federation's testimony of the proposed FY99 City of Chicago Budget. An analysis of these issues follows this overview.

Section I: **Budgetary Highlights**

A. Total Net Appropriations:

- The City's proposed FY99 net appropriation is 4.6% higher than for FY98, increasing from $4.34 billion to nearly $4.5 billion.
- The City's Corporate Fund is increasing by 5.5% from $2.173 billion in 1998 to $2.293 billion in 1999.
- Personal services are increasing by 3% from 1.783 billion in 1998 to $1.84 billion in 1999.
- Contractual services are increasing by 18.4% from $227 million in 1998 to $269 million in 1999.

B. Corporate Fund Revenues:

- Total corporate fund revenues are projected to rise by 2.3%, from $2.116 billion to $2.164 billion. Non-tax (i.e fees and charges) Corporate Fund revenues also will rise slightly, up from $512 million to $518 million.

C. Property Tax Levy:

- The FY99 City budget proposes a 3% decrease in the property tax levy, from approximately $678 million to $659 million. A 10% increase in property tax support for debt services and a 7% rise in funding for libraries has been proposed for FY99. Concurrently, decreases have been proposed for property tax transfers to the Corporate Fund and for City Relief.

The Civic Federation **supports** the Mayor for proposing a decrease in the property tax levy and for maintaining an overall moderate rate of net appropriation growth. However, we caution that while the revenue stream is strong currently, there will inevitably be an economic downturn. Unfortunately, we see no evidence that City is taking the necessary steps to prepare for this inevitable downturn.

The Civic Federation is **disappointed** that the City did not take advantage of its strong financial position to finally eliminate the $25 million Employer's Expense or "head" tax. The head tax is an anti-business tax that helps inhibit the creation of new jobs and promotes economic development in the suburbs, not the City. The City's abolition of the head tax for firms with 50 or fewer employers and concurrent reduction from $5 to $4 for remaining firms in the FY95 budget was welcomed by The Civic Federation and the entire business community. We believe that completing the job and abolishing the tax should be a major focus of the City's fiscal policy.

Section II: City Council Pay Increase

The Civic Federation **opposes** the method by which members of the Chicago City Council approved a pay increase because of: 1) the lack of an independent review of appropriate compensation levels; and 2) the lack of more opportunity for public participation and discussion on the issue. The Federation urges the creation of an independent Compensation Review Board (CRB) to establish compensation schedules for elected officials in the future.

Section III: Pensions

The Civic Federation **supports** recent legislation advanced by the City of Chicago to reduce two of its four statutory multiples that determine the contribution to its pension funds from the tax levy. However, The Civic Federation cautions the City of Chicago against providing future annuitant benefit increases without identifying sources of funding for those increases.

Section IV: Financial Condition

According to The Civic Federation's independent longitudinal review of the City's financial practices between FY93 and FY97, Chicago is in **good** financial health, a tribute to the City's superior financial management and the effects of a high-performing economy. Specifically:

- The City's general obligation bond rating was upgraded by Moody's Investors Service to A1 from A2 in FY98. Thus, the City's bonds are of high investment quality, offering solid investment potential.
- The City has adequate resources on hand to met its financial obligations over time;
- There have been no dramatic increases in the City's Short-term debt load; and
- The City does not rely heavily on risky forms of revenues to cover expenditures

The City's long-term per capita debt load has increased by 21% between FY93 and FY97, from $1,191 to $1,440. While currently not out of line with long term debt per capita figures for other large industrial cities such as Philadelphia and Detroit, future increases in this indicator bear watching.

Section V: Comparative Analysis: Chicago vs. Eight Major Industrial Cities
A comparative analysis of the financial condition of the City of Chicago and eight other major U.S. cities with populations over 1 million for FY97 shows that for most indicators used by the Federation, the Southwestern and Western "sunbelt" cities of Los Angeles, Houston, San Diego, Phoenix, and Dallas were in a stronger financial position than the "frostbelt" Midwestern and Eastern cities of New York, Chicago, Philadelphia, and Detroit. Thus, the "frostbelt" cities had lower cash solvency ratios, less liquidity and higher amounts of long-term debt per capita.

Compared to the four frostbelt cities reviewed, Chicago tends to have a greater availability of both liquid and illiquid assets to cover its financial obligations. It also has lower long-term debt per capita than New York and Philadelphia and shares with New York and Philadelphia a relatively low reliance on risky forms of revenue.

Section I. BUDGETARY ISSUES

A. Total Appropriations

The City's proposes FY99 net appropriation is 4.6% higher than for FY98, increasing from $3.911 billion to nearly $4.093 billion.

Figure 1-1

Total Appropriations, City of Chicago: FY98 and FY99

	FY98	FY99 Proposed	% Change
Corporate Fund	2,173.4	2,292.0	5.5%
Special Revenue Funds	356.6	355.7	-0.3%
Pension Funds	345.8	322.0	-6.9%
Debt Service Funds	430.4	455.1	5.7%
Enterprise Funds	1,035.7	1,071.7	3.5%
Total Appropriation	**4,341.9**	**4,497.4**	**3.6%**
Less Proceeds of Debt	(212.8)	(197.0)	-7.4%
Less Internal Transfers	(217.2)	(206.9)	-4.7%
Net Appropriation	**3,911.9**	**4,093.5**	**4.6%**

Small increases are proposed for Corporate Fund, Debt Service and Enterprise Fund appropriations. Within the Enterprise Funds, a 5% increase in fee revenues is projected for the City's two airports, rising from $553 million to $581 million. Decreased appropriations are projected for the Pension Funds as a result of recent legislation passed in Springfield as well as for the Special Revenue Fund.

B. Corporate Fund Revenues

The table below compares tax and non-tax revenues by category for the Corporate Fund in FY98 and as proposed in FY99. As the table below shows, total corporate fund

revenues are proposed to rise by 2.3%, from $2.116 billion to $2.164 billion. All tax revenues will rise only slightly, by 0.2%. Several tax revenue sources will actually fall, including a 5.5% decrease in recreation taxes collected. Non-tax revenues also will rise slightly, up from $512 million to $518 million.

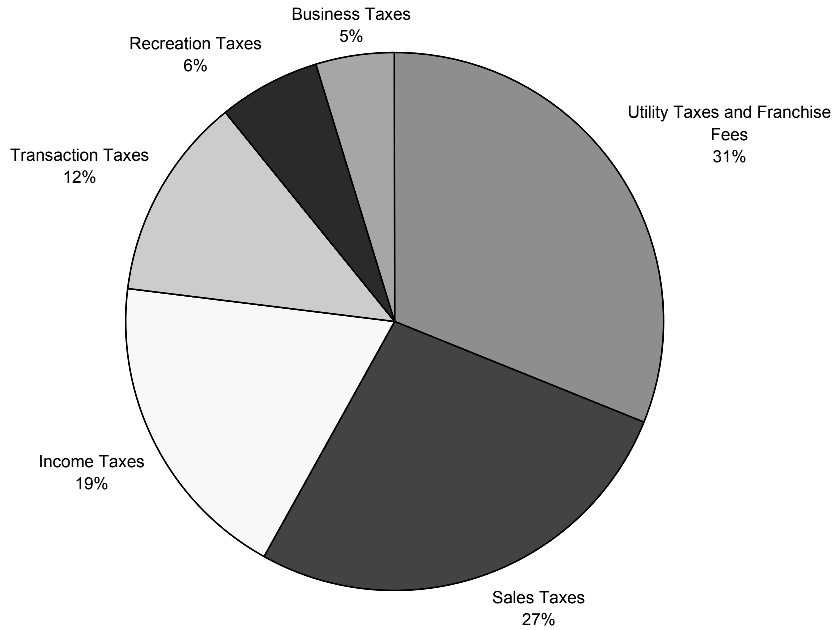
Figure 1-2

Corporate Fund Revenues, City of Chicago: FY98 & FY99
(In $000s)

	FY98 Year End Estimate	FY99 Proposed Budget	% Increase
Tax Revenue			
Utility Taxes and Franchise Fees	403.8	411.2	1.8%
Sales Taxes	364.0	358.7	-1.5%
Income Taxes	244.0	250.0	2.5%
Transaction Taxes	166.0	163.0	-1.8%
Recreation Taxes	**86.7**	**81.9**	**-5.5%**
Business Taxes	**61.5**	**62.5**	**1.6%**
Total Tax Revenue	**1,459.3**	**1,462.7**	**0.2%**
Non-Tax Revenue			
Internal Service Earnings	243.6	235.1	-3.5%
Fines & Forfeitures	101.0	105.0	4.0%
Licenses & Permits	59.5	59.8	0.5%
Current Service Charges	55.8	58.3	4.5%
Municipal Utilities	19.0	19.6	3.2%
Leases, Rentals & Sales	7.8	17.1	119.2%
Reimbursement, Interest & Other	25.5	23.7	-7.1%
Total Non-Tax Revenue	512.2	518.6	1.2%
Total Corporate Fund Revenue	**2,116.5**	**2,164.4**	**2.3%**

The pie chart below presents FY99 Corporate Fund tax revenues by source. As the chart demonstrates, utility taxes and franchise fees comprise the largest tax source of corporate fund revenues, at 31% of the total. Utility taxes are assessed on electricity, telecommunications and natural gas usage, while franchise fees are imposed on each utility's right to operate in the City. The next largest tax revenue sources are sales taxes, which bring in 27% of all tax revenues and income taxes at 19% of the total.

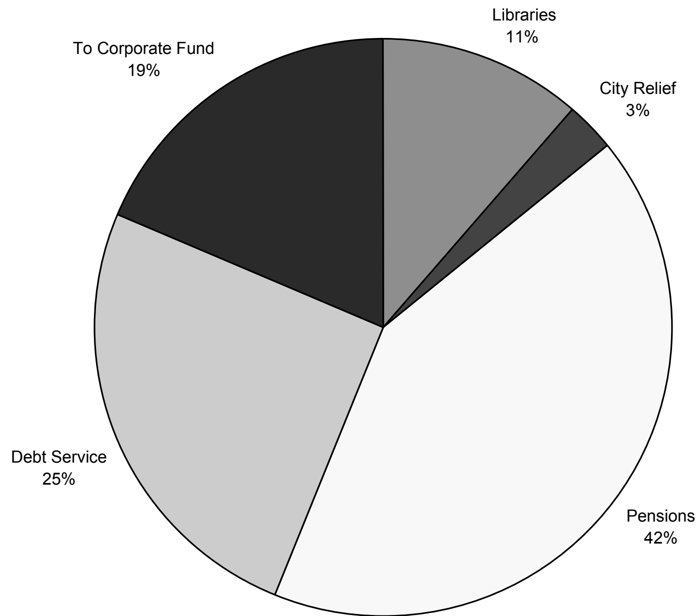
Figure 1-3



C. The Property Tax Levy

The pie chart below represents the proposed distribution of property tax revenues in the FY99 budget. The largest portion (42%) is used to fund the City's pension contributions for municipal employees. The next portion of the levy, or 25% of the total, is used to retire long-term debt. Of the remaining portion, 19% is transferred to the Corporate Fund, 11% is used to fund City libraries, and 3% is used for City Relief purposes.

Figure 1-4



The FY99 City budget proposes a 3% decrease in the property tax levy, from approximately $678 million to $659 million. A 10% increase in property tax support for debt services and a 7% rise in funding for libraries has been proposed for FY99. Concurrently, cuts have been proposed for property tax transfers to the Corporate Fund and for City relief.

The Business Cycle: An Economic Downturn is Inevitable

Length of Business Cycles

BUSINESS CYCLE REFERENCE DATES		DURATION IN MONTHS			
Trough	Peak	(Trough From Previous Peak)	Contraction (Trough to Peak)	Expansion Trough from Previous Trough	Cycle Peak from Previous Peak
April 1958	April 1960	8	24	47	32
February 1961	December 1969	10	106	34	116
November 1970	November 1973	11	36	117	47
March 1975	January 1980	16	58	52	74
July 1980	July 1981	6	12	64	18
November 1982	July 1990	16	92	28	108
March 1991		8	--	100	--

Source: National Bureau of Economic Research, Inc.

The United States in general, and the City of Chicago in particular, is currently in the eighth year of an economic boom. Unemployment is low, revenue collections are up and consumer confidence is high. However, all good things come to an end, including economic upturns. Unfortunately, the City is not now taking the necessary steps to prepare for the inevitable downturn.

The table above presents historic data on business cycle expansions and contractions. The average length of a business cycle between 1958 and 1990 was approximately 55 months. The current business cycle, which began in 1991, has continued to date for 92 months. Thus, the possibility of a contraction occurring in the near future is likely.

Section II. City Council Pay Increase

The Civic Federation opposes the method by which a compensation increase was approved for members of the Chicago City Council. Rather, The Civic Federation believes that compensation increase proposals should be reviewed by an independent Compensation Review Board (CRB). Modeled after the State of Illinois' CRB, a Chicago CRB would be charged with the responsibility of reviewing Chicago's elected officials compensation programs and making recommendations for approval by the City Council.

The purpose of the CRB will be to conduct independent reviews to determine the future compensation of elected officials and prevent the obvious conflict of interest that arises when elected officials set their own salaries. In order to increase the CRB's accountability to the public, the Federation recommends that the CRB be required to conduct public hearings for each recommendation, and that each meeting be subject to the Open Meetings Act.

The CRB will be charged with making recommendations to the City Council for changes to elected officials' compensation. Upon receiving the recommendations, the City Council will have the authority to approve or reject any recommendation that is made, but will not have amendatory powers. In addition, the City Council can only approve compensation recommendations at a meeting prior to the election of the officers whose compensation is to be fixed.

In 1995, The Civic Federation supported an ordinance before the City Council that would have created a CRB for elected city officers, sponsored by Alderman Margaret Laurino (39th). In addition to supporting the ordinance, the Federation asked that the measure be strengthened by prohibiting CRB members from having any financial interest in or dealings with the City of Chicago governmental offices for two years prior to their appointment and during their tenure on the Board.

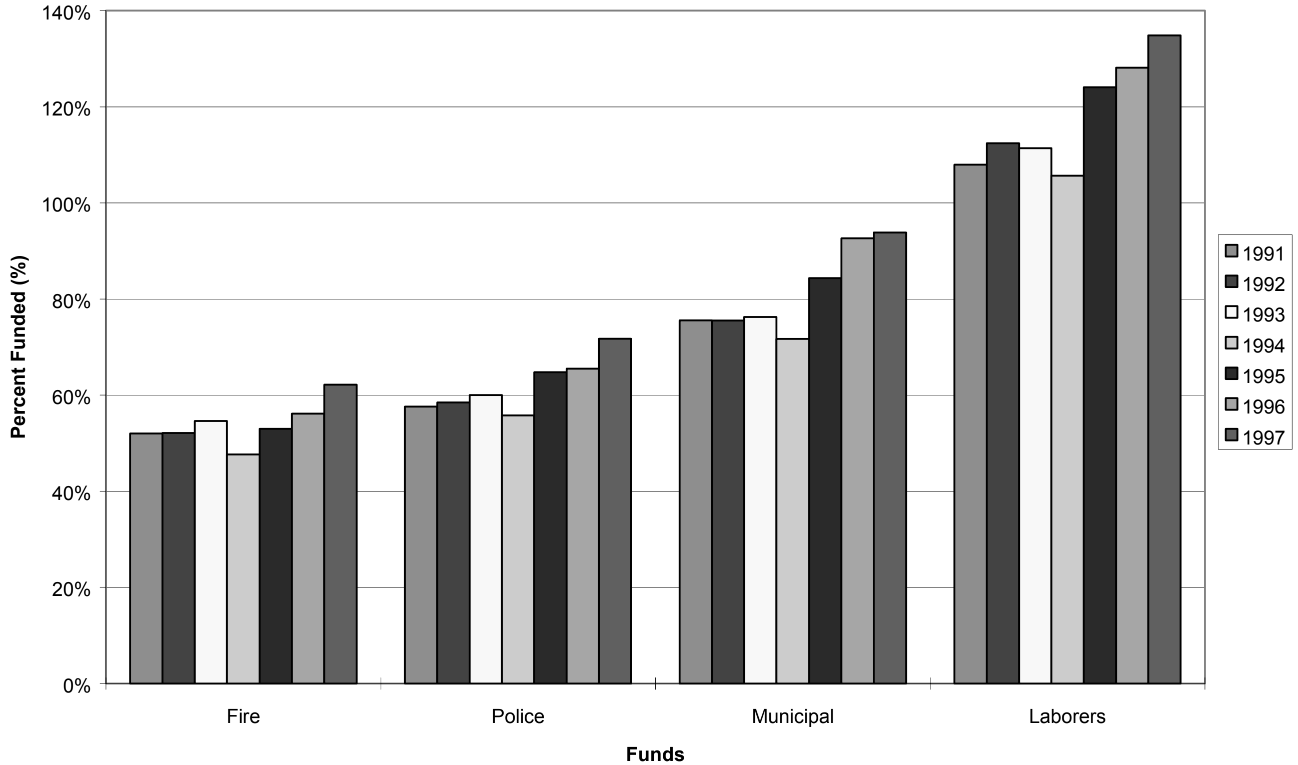
Section III. PENSIONS

As part of its annual review of the financial condition of the City of Chicago, The Civic Federation closely monitors and reports on the funding status of the City of Chicago's four pension funds.[1] In past statements, The Civic Federation has cautioned against any dramatic changes to the funding strategies governing the City of Chicago's pension funds. However, given the magnitude of the recent growth in the economy, specifically in the financial markets, the Federation agrees with the changes to the statutory multiples[2] that determine the local property tax levy that supports these funds. The Federation endorses the recent action taken by the Illinois General Assembly to decrease the statutory multiples that determine the City of Chicago's property tax levy for the Laborers' and the Municipal Employees' funds.

Based on our analysis, The Civic Federation supports the action taken by the Illinois General Assembly to change the City of Chicago property tax levy for 1999 by approximately $45 million. Based on this decrease in the property tax levy, the City of Chicago is proposing a $20 million tax abatement. Under the proposed $20 million tax abatement, the owner of a home with an estimated market value of $150,000 will save $28 per year. The owner of a $10,000,000 commercial business property would save $4,877 per year. In addition, part of the savings will be converted into the annual debt service payments for a $260 million bond issue and provide $12.6 million in new contributions to the historically underfunded Firemen's and Policemen's funds.

The Civic Federation recommendation is based on the recent significant improvement to the funded ratios of the City of Chicago's four pension funds. As the chart below indicates, all four funds have had significant increases in funded ratios during the past six years. As indicated in the chart below, the Laborers' Fund is now overfunded at 134.9%. The Municipal Fund is now over 90% funded at approximately 94%, and Two of the less well-funded funds have been the Policemens' and Firemens' funds. In 1997, the Policemens' fund reached 70% funded for the first time in many years. The Firemen's is at 62.2%

Figure 3-1



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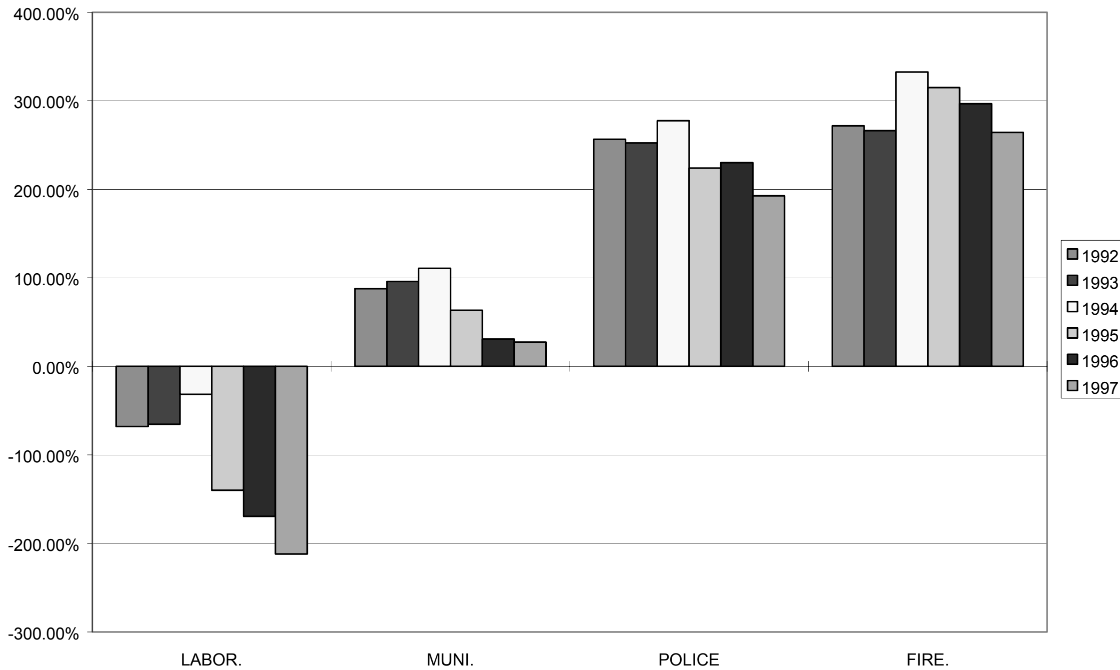
[1] The City of Chicago's four pension funds are the Firemen's Annuity and Benefit Fund of Chicago, the Laborers' & Retirement Board Employees' Annuity and Benefit Fund of Chicago, the Municipal Employees' Annuity and Benefit Fund of Chicago, and the Policemens' Annuity and Benefit Fund of Chicago.
[2] The statutory multiple is used to determine the employer contribution, i.e., the property tax levy. The employer contribution equals the statutory multiple times the total amount of contributions made by employees in the calendar year 2 years prior to the year of the levy.

In addition to reporting on a fund's funded ratio, another indicator of a pension fund's progress is the reporting of a fund's unfunded liability as a percentage of covered payroll. One of the functions of this indicator is an illustration of a funds ability to manage or make progress on reducing its debt or unfunded liability. Much like funded ratios, healthy funds are ones that continue to reduce debt over time without dramatic reductions at the expense of employees or taxpayers. An indication of a reasonable funding strategy would be a gradual decrease in unfunded liability as a percent of covered payroll over time. If the opposite is true, unfunded liability continues to increase as a percentage of covered payroll, then a new funding strategy and/or benefits granted by the fund needs to be reevaluated.

Figure 3-2



As the above chart illustrates, the four local pension funds have quite different unfunded liabilities as percentage of covered payroll. In generating this indicator, smoothed market value would have been preferred as a means for determining a fund's unfunded liability. However, given that some funds are only calculating this number from 1996, the market value (recognizing investments at current value) is used to determine unfunded liability.

In terms of the funding progress, the Laborers' Funds is negative in terms of this indicator. A negative indicator shows that a fund's current and projected assets are in surplus of its current and projected liability. Simply, its current and projected revenue stream exceed its current and projected debt.

Past Civic Federation statements regarding pension funding have stated that caution be used when efforts are being made to change the revenue structures of these funds. However, given the recent strong financial markets, The Civic Federation believes that it is now appropriate to increase the contributions to these funds. We do caution that any increase in the contributions to the Policemen's and Firemen's funds, derived from the property tax levy, not be viewed as an opportunity in the near term to increase benefits to the participants of these funds. In addition, we recommend that the proposed changes not be viewed as permanent. Financial markets that increase one day can reverse the next. The Civic Federation recommends that the financial health of these funds be closely monitored to prevent further underfunding of these funds.

Section IV. FINANCIAL CONDITION

The following indicators provide a snapshot of the City of Chicago's overall financial condition over the past five fiscal years, from FY93 to FY97. FY97 is the last year for which complete financial information is available.

The Civic Federation has developed the Financial Indicators as a first-of-its-kind tool to analyze governmental financial condition. While other studies have fashioned analytical tools to assist government financial managers, this is the first effort aimed at assisting taxpayers to better understand the financial condition of local governments.

Based on analysis of selected financial indicators, the City of Chicago is in good financial health:

- The City's general obligation bond rating was upgraded by Moody's Investors Service to A1 from A2 in FY98. Thus, the City's bonds are of high investment quality, offering solid investment potential.
- The City has adequate resources on hand to met its financial obligations over time;
- There have been no dramatic increases in the City's Short-term debt load; and
- The City does not rely heavily on risky forms of revenues to cover expenditures

The City's long-term per capita debt load has increased by 21% between FY93 and FY97, from $1,191 to $1,440. While currently not out of line with long term debt per capita figures for other large industrial cities such as Philadelphia and Detroit, future increases in this indicator bear watching.

A. QUALITY OF REPORTING

In order to evaluate the quality of governmental financial reporting, The Civic Federation has established a five-point grading scale, drawing upon standards established by the Governmental Accounting Standards Board (GASB). In order to merit a grade of 5/5 the following criteria must be met:

1) The Comprehensive Annual Financial Report (CAFR) format is used;
2) Generally Accepted Accounting Principles (GAAP) are used for financial statements;
3) There is an Unqualified Audit Opinion;
4) Financial Reports are released within 6 months of the close of the fiscal year; and
5) GAAP was used for presenting budgetary data in its General and Special Revenue funds.

The City of Chicago received a rating of 4/5 for all five of the years examined. Chicago consistently lost one point in the quality of their financial reporting due to the fact that the City did not use Generally Accepted Accounting Principles (GAAP) for the adoption of its budget. The City's Annual Appropriated Budgets were adopted on a budgetary basis, a method that is not consistent with GAAP.

Figure 4-1

THE CITY OF CHICAGO CHECKLIST
FOR FINANCIAL REPORTING: FY93 - FY97

CRITERIA	FY93	FY94	FY96	FY96	FY97
CAFR FORMAT	YES	YES	YES	YES	YES
GAAP USED FOR FINANCIAL STATEMENTS	YES	YES	YES	YES	YES
UNQUALIFIED AUDIT OPINION	YES	YES	YES	YES	YES
FINANCIAL REPORT RELEASED IN 6 MONTHS	YES	YES	YES	YES	YES
GAAP USED FOR BUDGET	NO	NO	NO	NO	NO
RATING	**4/5**	**4/5**	**4/5**	**4/5**	**4/5**

The City of Chicago operates under a mayor-council form of government. The financial statements present the City government and its four component units as one entity. The component units include: The Municipal Employees' Annuity and Benefit Fund; The Laborers' and Retirement Board Employees' Annuity and Benefit Fund; The Policeman's Annuity and Benefit Fund of Chicago; and The Firemen's Annuity and Benefit Fund.

B. FINANCIAL INDICATORS

The following section presents indicators that provide benchmarks of the financial health of the City of Chicago. They include: 1) liquidity, 2) cash solvency, 3) budgetary solvency, 4) financial stability and 5) risk factors.

1. Liquidity

Liquidity is the ready availability of cash, including the ability to convert assets into cash on short notice without loss of value. The following funds are reasonable options for internal borrowing and are, therefore, grouped together for this analysis: General Fund (GF), Special Revenue Fund (SRF) and Proprietary Funds. Capital funds are not included in this analysis because comparisons would be distorted by the mere timing differences in capital spending and debt financing activity, resulting in the large temporary fund balances. Also, borrowing from Capital Project Funds and Debt Service Funds may be restricted by bond covenants. Even without legal restrictions, the asset level of these funds can be quite volatile, making them an unreliable source of internal financing.

The liquidity ratio is calculated according to the formula below:

LIQUIDITY = CASH & SHORT-TERM INVESTMENTS / ACCOUNTS PAYABLE.

If the ratio is at least one the government should have enough resources to pay its bills as they come due.

As Figure 4-2 shows the City of Chicago had an **adequate** liquidity ratio for each of the years the study examined. The ratio ranged from a high of 3.4 in FY97 to a low of 2.0 in FY96. For the five years analyzed the liquidity ratio averaged 2.6. Thus, The City of

Chicago consistently maintained adequate funds to pay its bills as they came due during the time period analyzed.

Figure 4-2

LIQUIDITY RATIO FOR THE CITY OF CHICAGO
GENERAL, SPECIAL REVENUE & PROPRIETARY FUNDS:
FY93 - FY97

FISCAL YEAR	CASH + SHORT-TERM INVESTMENT	ACCOUNTS PAYABLE	RATIO
1993	$ 550,003,000	$ 230,723,000	2.3
1994	$ 540,882,000	$ 204,523,000	2.6
1995	$ 503,657,000	$ 204,413,000	2.5
1996	$ 562,579,000	$ 269,144,000	2.0
1997	$ 608,858,000	$ 178,513,000	3.4
AVERAGE	**$ 553,195,800**	**$ 217,463,200**	**2.6**

2. Cash Solvency: Current Fund Balance Ratio

Cash Solvency indicators measure the government's ability to meet its financial obligations over an indefinite period, long enough to convert illiquid assets to cash. The Civic Federation used a current fund balance ratio to measure cash solvency for the General and Special Revenue Funds.

CURRENT FUND BALANCE RATIO = (UNRESERVED GF AND SRF FUND BALANCE + THAT PORTION OF THE RESERVED FUND BALANCE EARMARKED FOR ENCUMBRANCES)
/ COMBINED GF AND SRF OPERATING EXPENDITURE.

In order to assess the size of the fund balance ratios, the Civic Federation has devised a rating system, which is listed below:

- If the Current Fund Balance Ratio is less than 10%, the government unit under review can be said to have Low Cash Solvency.
- If the Current Fund Balance Ratio is at least 10% but less than 25% of spending, it can be said to have Adequate Cash Solvency.
- If the Current Fund Balance Ratio is at least 25% but less than 50% of spending, it can be said to have Substantial Cash Solvency.
- If the Current Fund Balance Ratio is 50% or greater, it can be said to have High Cash Solvency.

The ratings are offered as a guide to taxpayers to use in raising questions with government officials regarding unreserved fund balances. Whenever Cash Solvency is too high, the government might consider shifting toward longer term holdings, retiring debt, or adjusting the income streams feeding the funds in order to bring income in line with current spending requirements.

According to Figure 4-3, the current fund balance of both the General and Special Revenue Funds has averaged 9.7%. Therefore, according to the current fund balance ratio calculations, the City of Chicago's General and Special Revenue Funds can be placed in the "Low" cash solvency category for the average of the five years the study examined. However, the City's current fund balance ratio grew 35%, increasing from 7.9 to 10.7 between FY93 and FY97. In FY95, FY96, and FY97 the City of Chicago General and Special Revenue Funds maintained a current fund balance ratio of over 10% and can be placed in the "Adequate" Cash Solvency Category for each of these years.

Figure 4-3

CURRENT FUND BALANCE RATIO FOR GENERAL AND SPECIAL REVENUE FUNDS OF CITY OF CHICAGO: FY93-FY97

FISCAL YEAR	Unreserved GF & SRF Fund Balance	GF & SRF Expenditures	Ratio	Rating
1993	$ 222,347,000	$ 2,828,673,000	7.9	Low
1994	$ 255,764,000	$ 3,001,951,000	8.5	Low
1995	$ 332,250,000	$ 3,139,760,000	10.6	Adequate
1996	$ 361,358,000	$ 3,307,082,000	10.9	Adequate
1997	$ 362,451,000	$ 3,378,156,000	10.7	Adequate
AVERAGE	**$ 306,834,000**	**$ 3,131,124,400**	**9.7**	**Low**

3. BUDGETARY SOLVENCY

Budgetary solvency measures a government's ability to generate enough revenue over the course a normal budgetary period to meet its expenditures and prevent deficits. We have measured budgetary solvency through the use of two measures:

- The surplus or deficit trend in fund balances for the General, Special Revenue, Debt Service, and Capital Projects funds; and
- Short-term debt trends over time.

A. Surpluses or Deficits

Figure 4-4 examines fund balances in each of the City of Chicago's Governmental Funds for FY93 to FY97. All of the Governmental funds showed a surplus, indicating healthy budget solvency for the years examined. While the Governmental Funds experienced substantial growth, the other Funds grew at a moderate rate:

- The General Fund grew 112%, increasing from $102 million to $216 million;
- The Special Revenue Fund grew 21%, increasing from $160 million to $194 million;
- The Debt Service Fund grew 25%%, increasing from $137 million to $171 million; and
- The Capital Project Fund grew 11%, increasing from $310 million to $345 million.

Figure 4-4

GOVERNMENTAL FUNDS GROUP
FUND BALANCES: FY93 - FY97

FISCAL YEAR	General Fund	Special Revenue Fund	Debt Service Fund	Capital Project Fund
1993	$102,011,000	$ 159,642,000	$ 137,851,000	$ 309,637,000
1994	$131,889,000	$ 130,872,000	$ 198,672,000	$ 574,249,000
1995	$150,629,000	$ 145,004,000	$ 223,662,000	$ 354,052,000
1996	$189,578,000	$ 189,493,000	$ 203,374,000	$ 355,834,000
1997	$216,330,000	$ 194,435,000	$ 170,957,000	$ 345,141,000
Average	**$158,087,400**	**$ 163,889,200**	**$ 186,903,200**	**$ 387,782,600**

B. Short-Term Debt Trends

Short-term debt is a financial obligation that must be satisfied within one year. An increasing trend in short-term debt may be a warning sign of coming financial difficulties.

Figure 4-5 shows that Chicago's short-term debt has increased only slightly during the time period of the study. Between FY93 and FY97 Chicago's short term debt increasing 13.1%, rising from $1 billion to $1.1 billion.

Figure 4-5

SHORT-TERM DEBT TRENDS
FOR THE CITY OF CHICAGO:
FY93 - FY97

FISCAL YEAR	Total Short-Term Debt	Percent Change
1993	$ 1,014,925,000	-
1994	$ 1,009,273,000	0.6%
1995	$ 1,041,778,000	-3.2%
1996	$ 1,151,497,000	-10.5%
1997	$ 1,147,439,000	0.4%
Average	**$ 1,072,982,400**	**-**

4. FINANCIAL STABILITY

Financial stability is the ability of a government to maintain its current financial policies. The following section sets forth some general indicators of financial stability for the City of Chicago. They include general obligation debt credit ratings, long-term debt per capital, and pension funding ratios.

A. Credit Rating

The City's general obligation bond rating was upgraded by Moody's Investors Service to A1 from A2 in FY98. Thus, the City's bonds are of high investment quality, offering solid investment potential.

B. Long-Term Debt Per Capita

Figure 4-6 presents long-term debt per capita trends for the City of Chicago for FY93 to FY97. The long-term debt analysis includes claims payable, employee vacation leave, capital leases, notes payable, and general obligation bonds payable. Any increases in this category bear watching as a potential sign of increasing financial risk.

As Figure 4-6 shows, long-term debt per capita assumed by Chicago has grown significantly over the five year period this study examines. Between FY93 and FY97 long-term debt per capita grew 21%, increasing from $1,191 to $1,440. The average long-term debt per capita for the five years the study examined was $1,338 of long-term debt per capita.

Figure 4-6

LONG-TERM DEBT PER CAPITA IN THE CITY OF CHICAGO FY93 - FY97

Fiscal Year	Total Long-Term Debt	Population	Total Long-Term Debt per Capita
1993	$ 3,314,419,000	2,783,726	$ 1,191
1994	$ 3,488,310,000	2,783,726	$ 1,253
1995	$ 3,709,701,000	2,783,726	$ 1,333
1996	$ 4,098,850,000	2,783,726	$ 1,472
1997	$ 4,007,512,000	2,783,726	$ 1,440
AVERAGE	**$ 3,723,758,400**	**2,783,726**	**$ 1,338**

5. RISK FACTORS

This portion of the analysis presents calculations for two different types of financial risk faced by local governments: 1) exposure to risk from relying too heavily on potentially unstable sources of revenue, and 2) the possibility of property tax increases due to rising expenditures.

A. Risk Exposure Factor Ratio

Risk Exposure Factor ratios measure the percentage by which a government will have to increase property taxes to cover a 1% shortfall in risky revenue sources, if services are to be maintained at current levels and other revenue sources are not available. Some of these sources of revenue and sources of risk are listed below:

- Investment Income is subject to *market* risk.
- Intergovernmental Revenue is subject to *political* risk. Welfare reform provides a good example of this type of risk.
- Transfer In is subject to two kinds of *management* risk, (1) the budget of the fund will not be balanced in the future, given that it is currently out of balance, and (2) the surplus in the originating fund will be eliminated.

The risk exposure factor ratio is calculated according to the following formula:

RISK EXPOSURE FACTORS = (INVESTMENT REVENUE + INTERGOVERNMENTAL REVENUE + TRANSFERS IN) /PROPERTY TAX REVENUE.

Figure 4-7 shows that the City of Chicago's risk exposure factor ratio averaged 3.4 for the five years that the study examined. This means that the City would been required to raise taxes or cut spending by 3.4% on average to cover a 1% shortfall in intergovernmental revenue, had it occurred. In short, over the period of this study, the City did not rely to heavily on risky forms of revenues to cover expenditures.

Figure 4-7

RISK EXPOSURE FACTOR RATIOS FOR
THE CITY OF CHICAGO FY93 - FY97

FISCAL YEAR	G & SR Intergovernmental, Interest & Transfers In & Out	G & SR Fund Property Tax Revenue	Ratio
1993	$786,540,000	$235,405,000	3.34
1994	$846,331,000	$246,655,000	3.43
1995	$938,103,000	$264,154,000	3.55
1996	$934,486,000	$281,654,000	3.32
1997	$938,273,000	$278,564,000	3.37
AVERAGE	**$888,746,600**	**$261,286,400**	**3.40**

B. Tax Leverage Factor Ratio

The Tax Leverage Factor Ratio is the rate by which government must increase its property taxes to maintain all services at existing levels in response to a one-percent increase in the budget for those funds supported by property tax revenue, assuming no offsetting increases in other revenue. This ratio gives planners a baseline to evaluate their long-term budget balancing efforts.

The Tax Leverage Factor Ratio is measured according to the formula presented below:

TAX LEVERAGE FACTOR = TOTAL GF & SRF OPERATING EXPENDITURES / PROPERTY TAX REVENUE.

Figure 4-8 shows that the tax leverage factor ratio for the City of Chicago for FY93 to FY97. The City's tax leverage ratio factor averaged 12%, this means that a 1% increase in the City budget would require a 12% increase in property taxes if other sources of revenue were not available.

Figure 4-8

TAX LEVERAGE FACTOR RATIOS FOR THE CITY OF CHICAGO FY93 - FY97

Fiscal Year	GF & SRF Funds Total Operating Expenditures	GF & SRF Funds Property Tax Revenue	Ratio
1993	$ 2,828,673,000	$235,405,000	12.0
1994	$ 3,001,951,000	$246,655,000	12.2
1995	$ 3,139,760,000	$264,154,000	11.9
1996	$ 3,307,082,000	$281,654,000	11.7
1997	$ 3,378,156,000	$278,564,000	12.1
AVERAGE	**$ 3,131,124,400**	**$261,286,400**	**12.0**

V. COMPARATIVE ANALYSIS: CHICAGO'S FINANCIAL CONDITION COMPARED TO OTHER MAJOR U.S. CITIES

The following figures compare the financial performance of the City of Chicago to eight other major U.S. cities with populations over 1 million. The analysis is based upon data from comprehensive annual financial reports for FY97. The indicators summarized include:

- Quality of Reporting;
- Liquidity;
- Cash Solvency: Current Fund Balance Ratio; and
- Risk Factors
    - Risk Exposure Factors and
    - Tax Leverage Factors

This comparative analysis shows that for three of the financial indicators presented, the Southwestern and Western "sunbelt" cities of Los Angeles, Houston, San Diego, Phoenix, and Dallas were in a stronger financial position than the "frostbelt" Midwestern and Eastern cities of New York, Chicago, Philadelphia, and Detroit. These findings are consistent with other research that shows a pattern of financial stress or decline in the older "frostbelt" cities of the Mid-West and East Coast and consistent financial strength in the younger "sun-belt" cities in the southern and western part of the United States. Thus:

- The two cities with a current fund balance ratio above the average of 24 - Los Angels and Dallas - are located in the sunbelt, while their sunbelt counterpart of San Diego was close behind with a ratio of 21. In contrast, all four of the frostbelt cities analyzed ranked far below the average.

- The frostbelt cities if New York, Philadelphia and Chicago had the top three long-term debt per capita while the three cities at the bottom of the list were all in the sunbelt; and

- All five sunbelt cities had liquidity ratios above the average of 5.1 while all four frostbelt cities had liquidity ratios of 3.7 or less.

In addition, three of the six cities located in the frostbelt for which data were available - Detroit, Chicago and New York - relied much more heavily on potentially risky sources of revenues than Los Angeles, San Diego and Dallas.

Compared to the four frostbelt cities reviewed, Chicago tends to have a greater availability of both liquid and illiquid assets to cover its financial obligations. It also has lower long-term debt per capita than New York and Philadelphia and shares with New York and Philadelphia a relatively low reliance on risky forms of revenue.

Quality of Financial Reporting

Figure 5-1 presents ratings of the quality of financial reporting for FY97 for the nine cities the study analyzed. New York was the only city to fulfill all the criteria and receive a rating of 5/5. The eight other city's in the study -- Los Angeles, Chicago, Houston, Philadelphia, San Diego, Phoenix, Dallas, and Detroit -- all received rating of 4/5 due to the fact that they did not use generally accepted accounting principles for the adoption (GAAP) of their annual budget.

Figure 5-1

QUALITY OF FINANCIAL REPORTING

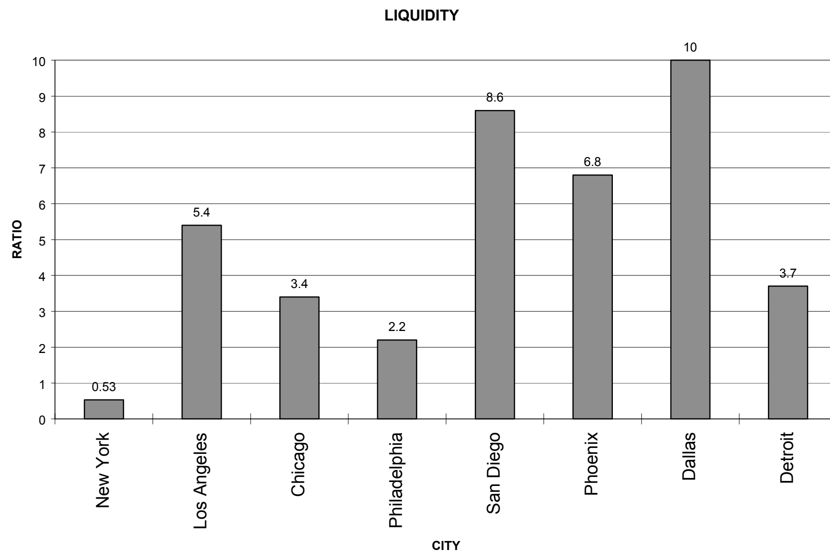
Municipality	CAFR Format	GAAP Used For Financial Statements	Unqualified Audit Opinion	Financial Reports Within 6 Mos.	GAAP For Budget	Rating
Chicago	**Yes**	**Yes**	**Yes**	**Yes**	**No**	**4/5**
Dallas	Yes	Yes	Yes	Yes	No	4/5
Detroit	Yes	Yes	Yes	Yes	No	4/5
Houston	Yes	Yes	Yes	Yes	No	4/5
Los Angeles	Yes	Yes	Yes	Yes	No	4/5
New York	Yes	Yes	Yes	Yes	Yes	5/5
Philadelphia	Yes	Yes	Yes	Yes	No	4/5
Phoenix	Yes	Yes	Yes	Yes	No	4/5
San Diego	Yes	Yes	Yes	Yes	No	4/5

Liquidity Ratio

Figure 5-2 shows that there was a wide variation of liquidity ratios between nine cities the study examined. The ratios ranged from a high of 10 in Dallas to a low of 0.53 in New York. The average liquidity ratio for the eight cities the study analyzed was 5.1. Chicago ratio of 3.4 was below the average and ranked as the third lowest among the nine cities the study analyzed.

Figure 5-2

LIQUIDITY RATIOS



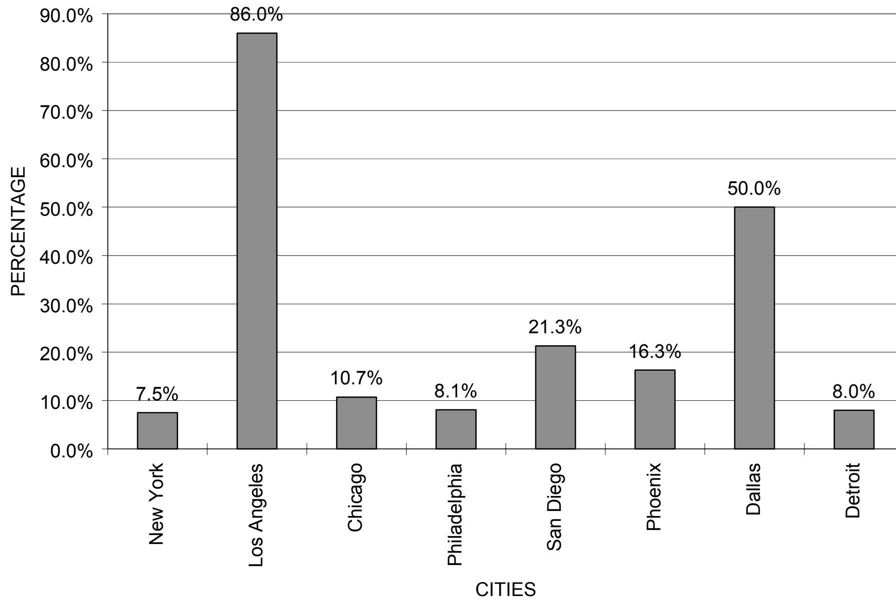
Solvency Indicators: Current Fund Balance Ratio

A. Current Fund Balance Ratio: General and Special Revenue Funds.

The average current fund balance ratio of the nine governments examined was 24%, warranting a rating of substantial cash solvency. Figure 5-3 shows Los Angeles can be placed in the high cash solvency category and Dallas can be placed in the substantial category. With a 10.7% current fund balance ratio, Chicago qualified for a rating of adequate cash solvency, along with the sunbelt metropolises of San Diego and Phoenix. Houston, Detroit, Philadelphia, and New York were all placed in the low category.

Figure 5-3

CURRENT FUND BALANCE RATIO

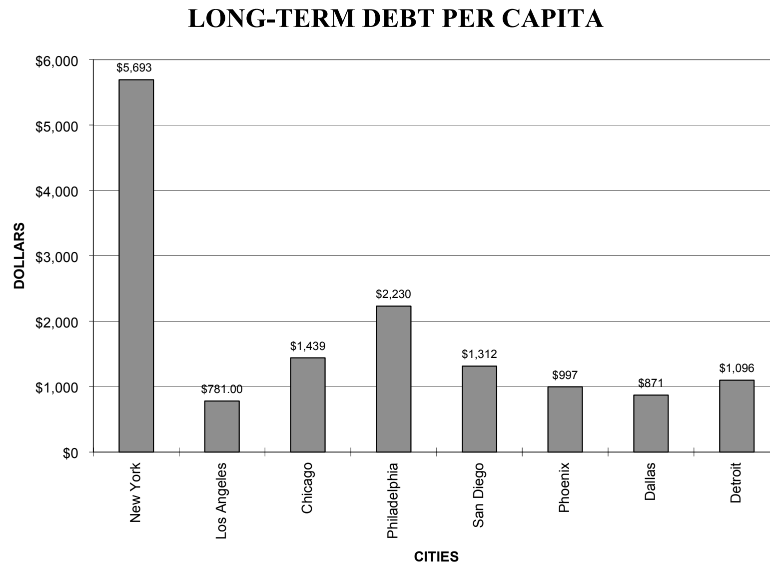


Long-Term Debt Per Capita

The average long-term debt per capita of the nine cities the study examined was $1,736. However, this figure is very inflated because of New York's extraordinarily high long-term debt per capita amount of $5,693 per person, due to approximately $31 billion in General Obligation Bonds outstanding. When New York is dropped from the sample, the average long-term debt capita figure falls to $1242. Chicago's long-term debt per capita sum of $1,439 ranks higher than this figure, falling between San Diego at $1312 and Philadelphia at $2230.

Figure 5-4

LONG-TERM DEBT PER CAPITA



Risk Factors

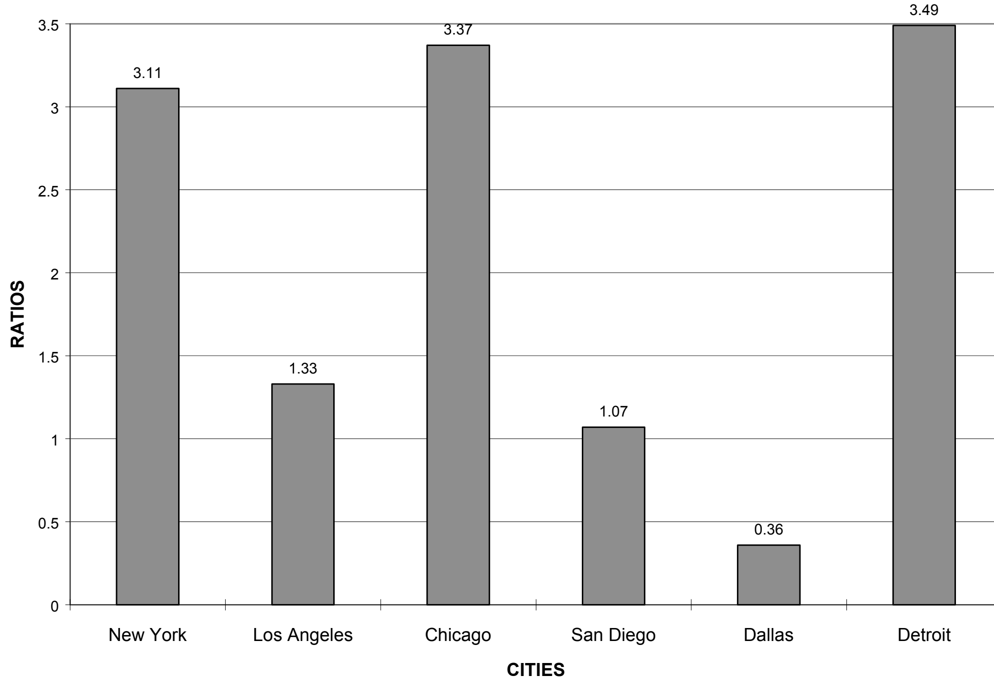
A. Risk Exposure Factor Ratios

Figure 5-5 shows the Risk Exposure Factor Ratios for the six cities for which data was available. Risk Factor Ratios could not be calculated for Houston, Philadelphia or Phoenix due to the fact that their financial statements did not separate property taxes from other tax revenues.

For the six cities the study examined the average risk exposure factor ratio was 1.6. The sunbelt cites of Dallas, San Diego, and Los Angeles relied far less on risky revenue sources than their frostbelt counterparts of Detroit, Chicago, and New York. Dallas had the lowest ratio at 0.36 and Detroit had the highest ratio, at 3.49.

Figure 5-5

RISK EXPOSURE FACTOR RATIOS



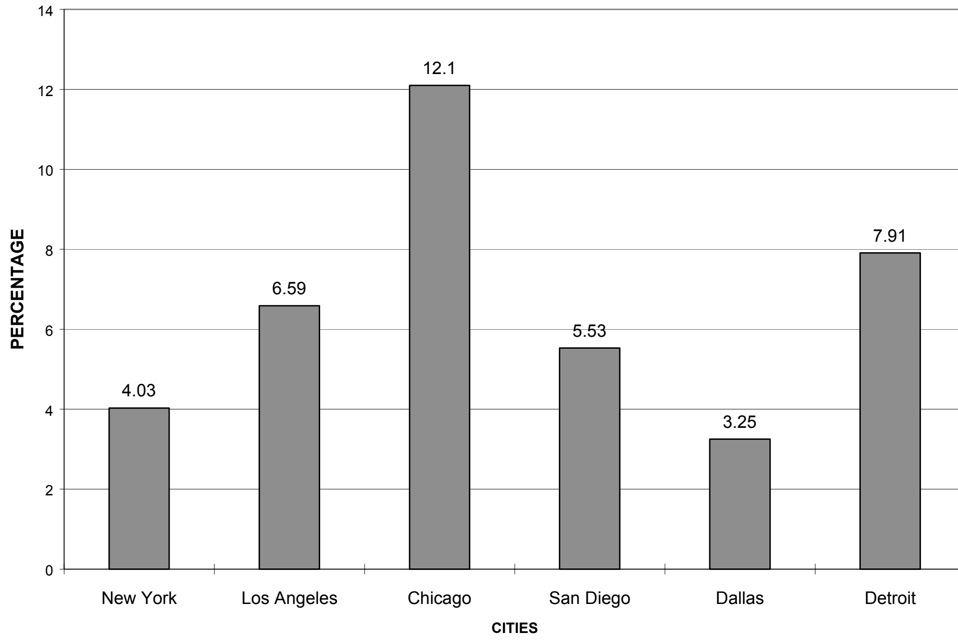
Tax Leverage Factor

The average Tax Leverage Ratio for the six cities the study analyzed was 5.3. Figure 5-6 shows that Chicago, with a tax leverage ratio of 12.1%, was at the highest risk for having to increase property taxes if a budgetary increase had been forthcoming.

Tax Leverage factors could not be calculated for Houston, Philadelphia or Phoenix due to the fact that their financial statements did not separate property taxes for other forms of tax revenue.

Figure 5-6

TAX LEVERAGE RATIOS



Respectfully Submitted,

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