S&P Global
Ratings

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Summary:

Cook County Community College District No. 508 (City Colleges of Chicago), Illinois; General Obligation

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Summary:

Cook County Community College District No. 508 (City Colleges of Chicago), Illinois; General Obligation

Credit Profile		
US$80.0 mil unltd tax GO bnds (dedicated revs) ser 2017 due 12/01/2047		
Long Term Rating	BBB/Stable	New
Cook Cnty Comnty Coll Dist #508 (City Coll of Chicago) GO		
Long Term Rating	BBB/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'BBB' rating to Cook County Community College District (CCD) No. 508 (City Colleges of Chicago), Ill.'s series 2017 unlimited-tax general obligation (GO) (dedicated revenues) bonds. At the same time, we affirmed our 'BBB' rating on the district's outstanding GO bonds. The outlook is stable.

The series 2017 bonds and outstanding series 2013 bonds are secured by the district's unlimited ad valorem tax full faith and credit GO pledge. Series 2017 bond proceeds will be used for the design and construction of the Engineering and Advanced Manufacturing Center at Daley College, the expansion of the Olive-Harvey Campus to include a new 103,000 square-foot Transportation, Distribution, and Logistics building, capitalized interest through Dec. 1, 2018, and for the cost of issuance. Roughly $6 million of the $80 million par will go for reimbursement of past projects.

The bonds are alternate revenue source bonds payable from tuition and fees, state grants, and other pledged revenues. If pledged revenues are insufficient, the bonds are also secured by unlimited ad valorem property taxes. Under the bond resolution and trust indenture, City Colleges will abate the annual tax levy only to the extent that pledged revenues are on deposit in the pledged revenues account to pay debt service. The rating is based on the unlimited-tax GO pledge, which we view as the stronger security.

The 'BBB' rating reflects our opinion of the district's:

- Substantially weakened unrestricted net assets (UNA);
- Trend of operating deficits leading to a negative fund balance;
- Liquidity pressure caused in part by reduced and unreliable state funding;
- Decreasing enrollment;
- Moderately high-to-high overall debt burden that is increasing with very slow amortization; and
- Dampening effects of the combined pension liabilities and debt of the overlapping governmental entities on its tax base.

Partly offsetting those negative factors is our opinion of the district's participation in the deep and diverse economy of Chicago, which is the center of a major multicounty metropolitan statistical area (MSA), a massive tax base that

includes downtown Chicago, adequate-to-good incomes with extremely strong market value per capita, and inherent expenditure flexibility and some revenue-raising flexibility, albeit limited in the current environment.

Economy

City Colleges operates seven community colleges in the city, serving a population of 2.7 million in boundaries nearly coterminous with Chicago. Most of the district's tax base is in Cook County, with a very small portion in DuPage County. Equalized assessed valuation (EAV) for the district's tax base peaked in tax levy year 2009 at $84.6 billion before declining 26% between levy years 2009 and 2013 to $62.3 billion. EAV has since increased 4.1% in 2014, 9.3% in 2015, and 4.3% in 2016 to reach $74 billion. According to the Civic Federation, full market value for the city of Chicago (nearly coterminous with the district) is about $278 billion, which is extremely strong at $102,428 per capita. The district's operating levy is subject to the Property Tax Extension Limitation Law (PTELL), which limits levy growth to the lesser of 5% and the rate of inflation, with exception for new construction. Because of the past drops in EAV, the district now taxes at 71% of its education fund rate and 98% of its maximum operations and maintenance (O&M) rate in levy year 2016; the district reduced its education rate in 2015 after valuation growth. Median household and per capita effective buying incomes for Chicago are adequate at 88% and 97% of the nation's level, respectively.

Enrollment

Total semester credit hours generated peaked at 1.26 million in 2010 and have since declined by nearly 28% to 904,000 in 2017. The year-over-year decline was 8.1%. However, we note tuition and fee revenue increased 9.3% between 2010-2017. Management attributes the decline to a rebound in Chicago MSA employment (given community college enrollment is countercyclical) and the state's past lack of funding for the Monetary Award Program. The district's in-district hourly tuition and fees charges are among the lowest in the state at $89 per credit hour in 2015 and were flat for the past four years. Beginning in fiscal 2016, the colleges are switching to a flat-price tuition structure at $1,069 per semester for part time and $1,753 per semester for full time.

Finances

The district's finances weakened considerably as reported in the fiscal 2016 audit (June 30), due in large part to reliance on unpredictable state revenue, which dropped dramatically. Additionally, the district was overly optimistic in its budget assumptions for fiscal 2016 and again in fiscal 2017, although we note the recently enacted fiscal 2018 budget greatly improved its fiscal 2017 outlook. The reduced state revenue and optimistic budget assumptions in fiscal 2016, in part, led to a negative combined education and O&M funds ("general fund") that we expect to persist. The district was faced with liquidity pressures at the end of fiscal 2017 before the receipt of somewhat regular state funding after the implementation of the state fiscal 2018 budget. Management indicates liquidity is currently sufficient and we agree, given our analysis of cash flow projections. However, the projections include assumptions of timely payment of state aid and other receipt of revenues in a timely fashion. Moreover, we expect the negative fund balance to persist and note that it is indicative of the rating level.

The district's financial operations are reported on a full-accrual basis of accounting. State revenue accounted for 21% of in the general fund in fiscal 2015. In fiscal 2016, due to significantly reduced state funding, state revenue accounted for only 6% of general fund revenue. In fiscal 2017, additional state appropriation was not received within the accrual period and thus state revenue accounted for 10% of general fund revenue. If the roughly $34 million would have been booked to fiscal 2017, state revenue would have accounted for approximately 21% of general fund revenue—roughly

equal as a percentage to fiscal 2015. At fiscal year-end 2017 (June 30), the district reported a general fund balance of negative $82 million, or negative 29.3% of expenditures, after a $41 million deficit--much weaker than the roughly negative $42 million fund balance from fiscal 2016, which we expected. It was last positive in fiscal 2015. However, this does not reflect roughly $34 million in additional appropriated state revenue that was not received in the accrual period, which is included in the district's December cash flow projections.

The district reported a $0 balance in the bond and interest fund, an improvement from the negative $6.3 million fund balance in fiscal 2016, a negative $5.4 million fund balance in the auxiliary enterprises fund, and a negative $3.8 million in the restricted purposes fund at fiscal year-end 2017—a combined weaker position than fiscal 2016. Including all funds, City Colleges reported UNA of negative $37.7 million at fiscal year-end 2017, down from a positive $25 million at fiscal year-end 2016. That amount represents negative 8% of operating expenses, less depreciation. The working cash fund held $67 million in additional liquidity, which has been stable for at least three years. We note that community college working cash funds are more restricted than Illinois school district counterparts and serve as a cash flow tool rather than as additional reserves for operations. Liquidity has weakened and will likely remain pressured, in our view, with roughly $55 million in cash, cash equivalents, and short-term investments held in all funds at fiscal year-end 2017, down from $78 million in fiscal 2016, which constituted 11.5% of total operating expenses (less depreciation), down from 16.5% in fiscal 2016.

In fiscal 2016, the approved budget included roughly $58 million in state funding and received only $14.4 million—a shortfall of nearly $44 million. The budget included a $5.5 million surplus in the combined general fund before transfers. Estimates provided by management in July 2016 indicated a negative $36.4 million change in net position in the unrestricted funds (including education, O&M, auxiliary/enterprise, and working cash); it reported a negative $110 million change (partly due to a campus write-off and depreciation).

Since 2009, the district has maintained a policy to transfer its educational fund balances in excess of 3% of educational and unrestricted O&M fund combined expenses to the restricted O&M and plant funds—this policy was no longer active as of December 2016. It transferred $24.6 million from the educational fund to these funds in fiscal 2014, $19 million in fiscal 2013, and $42.3 million in fiscal 2012. However, we note it only transferred $607,000 in fiscal 2015 and made no transfer in fiscal years 2016 and 2017, indicating significantly weakening operational performance and a modification of its own policy, in our view. The district operates the restricted O&M fund as a capital projects fund; the restricted O&M fund reported a negative $15.7 million fund balance at the end of fiscal 2017, down from $14.8 million at the end of fiscal 2016, substantially down from $55.4 million in fiscal 2015 and $176 million at the end of fiscal 2012.

The fiscal 2017 budget included a $6.4 million combined general fund surplus and break-even across all funds—which we viewed as unlikely. The budget assumed receiving $48.5 million in state revenue, or over 85% of the amount received in fiscal 2015, which at the time was highly optimistic, in our opinion. The district had received $25.8 million before the supplemental appropriation of $31.4 million in the state's fiscal 2018 budget allocated for fiscal 2017. Had the district not received additional state funding after the close of the fiscal year, the budget gap would have been worse and would have substantially weakened the already negative fund balance. We expect the negative fund balance to improve after the receipt of the additional appropriation, which is now expected in late 2017. Management indicates it used the working cash fund for liquidity and has authorization for $60 million in tax anticipation warrants (TAWs),

which is not reflected in cash flow projections. We note liquidity is thin but is not likely an immediate concern given management's cash flow projections and plans to access external liquidity, in addition to its overall responsiveness.

In prior years, the district has made a wide variety of expenditure adjustments, including materials and supplies spending, contractual services, travel, capital spending, and a hiring freeze (although we note the freeze did not include faculty and essential positions). The district has announced its plans to sell its downtown headquarters and sold its TV station, with 118 layoffs at the district office and administrator positions at the colleges. It also intends to hold one-time sales of underutilized assets for fiscal 2018. In addition, it has some tuition and fee autonomy to better align the budget in the absence or reduction of state funding.

The state fiscal 2018 budget included revenue for CCDs at 90% of 2015 levels and the district budgeted for that amount—roughly $49 million (potentially higher at $50.2 million and not including adult education). With this appropriated state revenue, the fiscal 2018 budget is structured with a break-even result in the operating unrestricted funds that includes a $15 million repayment to the working cash fund and break-even across all funds, which we view as difficult to achieve. Continued revenue-raising measures and expenditure cuts will be necessary in fiscal 2018 and beyond to structurally align its budget.

Management

The district has a new chancellor as of early 2017.

We consider the district's financial management practices "standard" under S&P Global Ratings' Financial Management Assessment, indicating our view that the finance department maintains adequate policies in some, but not all, key areas. Past revenue and expenditures assumptions proved overly optimistic. Management uses zero-based budgeting at the department level and five-year financial projections to help plan the district's budgets, and provides quarterly budget-to-actual reports to the board. The district has formalized investment and debt management policies but lacks a robust fund balance policy. Although there is no formal minimum fund balance policy, management's target is to maintain the unrestricted educational fund balance at a maximum of 3% of operational expenditures for the prior year (a policy it modified in December 2016 given the current financial situation), and it targets at least $67 million of working cash.

Debt

The series 2017 (issued at $80 million) and outstanding 2013 bonds (issued at $250 million) constitute City Colleges' only direct GO debt. The overall debt burden (including substantial overlapping debt mostly from City of Chicago and Chicago Board of Education) is moderately high at $8,033 per capita and 7.8% of estimated full market value. Amortization is very slow, in our view, with only 18% of principal scheduled to mature within 10 years and only 49% within 20. The 2013 bonds have a 2044 final maturity and the 2017 bonds are expected to have a 2047 final maturity. Debt service carrying charges were what we consider low at roughly 4.4% of total operating expenses in 2016 and 2.6% in 2017. We understand City Colleges has secured $60 million of authorization for TAWs for liquidity if needed. It has no additional debt plans and it does not have any direct-purchase or private-placement obligations.

Pensions and OPEBs

The district participates in the State Universities Retirement System of Illinois (SURS), a cost-sharing multiemployer defined-benefit pension plan, but the state makes substantially all of the required contributions. In fiscal 2017, City

Colleges recognized on-behalf revenue and pension expense of $134 million, equal to the required contribution. The proportionate share of the state's net pension liability for the district is nearly $1.4 billion or 5.2204%. The SURS plan was poorly funded at less than 40% as of 2016. City Colleges pays about 85% of the cost of medical, dental, and vision insurance for retirees on a pay-as-you-go basis. It paid $6 million in 2017, less than 1% of total operating expenses. The unfunded actuarial accrued liability for OPEBs as of July 1, 2017, was $123.7 million and was 0% funded.

Outlook

The stable outlook reflects our view that the rating will not change within the one-year outlook period. Despite a persistent negative fund balance, the district's cash flow projections indicate liquidity is sufficient in the outlook period at the current rating level, especially given access to external liquidity if needed. However assumptions rely on receipt of timely state aid and other one-time revenue sources. We expect management to continue to address its structural imbalance through revenue enhancements and expenditure adjustments.

Downside scenario

We could lower the rating during the one-year outlook period should the district experience significant reductions or delays in state revenue (not expected in fiscal 2018) that meaningfully weaken operations and available reserves. We would also likely lower the rating if the district weakens its reserves with no immediate replenishment mechanism after a trend of negative financial operations. The potential effects on the district's tax base due to the combined pension liabilities and debt of the overlapping governmental entities could also pressure the rating.

Upside scenario

We could raise the rating after a sustained period of structural balance and an elimination of the district's negative fund balance and a significant improvement in liquidity, although we view this as unlikely in the outlook period. A higher rating is predicated on a rebuilding of the financial position and liquidity after the last several years of budgetary pressure.

Ratings Detail (As Of November 9, 2017)		
Cook Cnty Comnty Coll Dist #508 GO (BAM) (SECMKT)		
Unenhanced Rating	BBB(SPUR)/Stable	Affirmed
Cook Cnty Comnty Coll Dist #508 (City Coll of Chicago) GO (BAM)		
Unenhanced Rating	BBB(SPUR)/Stable	Affirmed
Cook Cnty Comnty Coll Dist #508 (City Coll of Chicago) GO (BAM) (SECMKT)		
Unenhanced Rating	BBB(SPUR)/Stable	Affirmed
Cook Cnty Comnty Coll Dist #508 (City Coll of Chicago) GO (BAM) (SEC MKT)		
Unenhanced Rating	BBB(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is

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