

2019

OVERVIEW AND ANALYSIS OF
COMPREHENSIVE ANNUAL FINANCIAL REPORT
CITY OF CHICAGO



The Comprehensive Annual Financial Report (CAFR) is a report used by cities and local governments to provide the public with their financial records each year while adhering to Government Accounting Standards Board (GASB) guidelines. The CAFR presents a comprehensive picture of the reporting entity's financial condition, how funds are spent and how funds are allocated throughout the year. The City of Chicago's CAFR is a narrative overview and analysis of the financial activities of the City for the fiscal year ending December 31, 2019.

OVERVIEW OF CAFR'S BASIC FINANCIAL STATEMENTS

This section is intended to serve as an introduction to the City's basic financial statements, which include the following components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the basic financial statements.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The *statement of net position* presents the financial position of the governmental entity and its component units. This statement is required to present all financial and capital resources using an economic resources measurement focus and the accrual basis of accounting. For a government body, a *statement of activities* is like a traditional income or change statement. It's fairly straightforward and lists the revenues and expenses of the government, and in some cases, the difference between them to show the balance. It's a quick reference to see financial condition of the government.

The financial statements shows the City's Liabilities and Deferred Inflows of the City exceeds assets and deferred outflows at the end of the fiscal year (FY) 2019 by a net deficit of \$29,459 million. The net deficit is made up of \$4,294.1 million in net investment in capital assets and \$4,314.5 million in net position restricted purposes, offset by an unrestricted deficit of \$38,067.6 million. An increase in transportation and public safety expenses had an adverse impact by increasing the net deficit to \$94.3 million in 2019. However, business-types activities help to offset the deficit thanks to the surplus from the O'Hare and Water Fund. The FY 2019, \$94.3 million deficit is a grave concern for Chicago taxpayers, stakeholders, and bond rating agencies. This draws great concerns due to the lingering pension issue, the Chicago Police Department contract, and projected deficits for FY2020. By using the surplus funds from business-type activities, it risks driving other funds into a deficit. In light of the present pandemic, multiple Enterprise Fund revenues are projected to be lower than the original projection. The reliance on other funds to balance the budget is not a fiscally responsible or sustainable practice?

Fund Financial Statements

These statements present information about major funds individually and non-major funds in aggregate for governmental and proprietary fund types.

To determine which category the fund falls into, one must ask the question, does it relate to the functions of a typical government? If yes, it falls under governmental funds, which are used to record and balance cash, data, and liabilities for all activities. Police, fire, other emergency services, and more all fall under this fund type. Governmental funds include the following:

General Fund

A general fund is the chief operating fund for the entire government. It in part/partly serves as a catch-all fund for resources that aren't required or designated for another fund. For example, the tax money generated by the United States Federal Government goes into the general fund.

Special Revenue Funds

These funds are used to track the revenue from specific sources restricted to certain purposes. It's the most commonly used fund and is typical for the funding of libraries, schools, and parks. Citizens can see the revenue generated for the building and/or maintenance of these specific sources.

Debt Service Fund

A debt service fund is used to pay back long-term debt issued to finance specific government projects. This includes both the principal and interest amounts paid out.

Capital Projects Fund

This accounts for financial resources related to the construction of major capital projects or facilities. Capital projects tend to include work on long-lived facilities like libraries or government buildings.

Government Funds

There are three major groups of government funds: governmental, proprietary, and fiduciary. In accounting, an account belonging in this fund is often due to the fact it doesn't fit in other designations. Under each of these three groups are different types of government funds.

Governmental Funds

A governmental fund is a grouping used in accounting for *tax-supported* activities completed by the federal government. Its opposite is a proprietary fund, which accounts for *business-like* activities conducted by the government. There are several government fund types, each of which maintains a balance sheet. Under the umbrella of a government fund, a branch demonstrates it spent the money it was allocated correctly through the maintenance of a balance sheet.

Proprietary Funds

This fund source operates as a business. They pertain to providing goods or services to the general public. It covers the services which are important but not essential to the way a government runs. An enterprise fund is a proprietary fund, as it is used for services the public received on a person-by-person basis. The City's has the following Enterprise Funds (Net Income for FY2019 indicated below):

- O'Hare Airport Fund \$202 million
- Water Fund \$172 million
- Sewer Fund \$92 million
- Midway Airport Fund (\$23) million (loss)

Fiduciary Funds

In January 2017, the Governmental Accounting Standards Board (GASB) issued Statement No. 84 Fiduciary Activities (GASB 84). GASB 84 defines four generic types of fiduciary funds:

Pension (and other employee benefits) Trust Funds are used to accumulate resources to fund pension and other post-employment benefits (OPEB) plans either as defined in GASB Statement No. 67 or 74, or a qualifying trust.

Investment Trust Funds are used to report the external portion of investment pools held in a qualifying trust. In this case, the “qualifying trust” definition does not include the irrevocable contribution criteria as it does for Pension and OPEB trusts.

Private-purpose Trust Funds are those funds held in a qualifying trust (same definition as Investment Trust Funds) that are not required to be reported in Pension (and other employee benefits) or Investment Trust Funds. These funds are used for specific purposes (such as endowments or scholarship funds) that were originally defined by the person or organization that gave the funds to the government.

Custodial Funds are used to report fiduciary activities that are not required to be reported as another fiduciary fund type. In practical terms, this equates to what was historically reported in Agency funds.

NOTES TO THE BASIC FINANCIAL STATEMENTS

Financial Analysis of the City as a Whole

Net Position - The difference between an entity's assets plus deferred outflows of resources and its liabilities plus deferred inflows of resources represents its *net position*. The net position has the following three components: 1) the difference between an entity's assets plus 2) deferred outflows of resources and its liabilities plus 3) deferred inflows of resources. The City's liabilities, and deferred inflows exceeded assets by \$29,459.0 million on December 31, 2019. In 2019 the City invested \$4,294.1 million in capital assets (land, buildings, roads, bridges, etc.) less any related debt used to acquire those assets that are still outstanding. The downside is that the assets are not available for future spending. The City's investment in its capital assets is reported net of the related debt. To repay the related debt the City will use other resources, subsequently, the capital assets cannot be used to liquidate these liabilities and deferred inflows. The City's net position, \$4,314.5 million, represents resources that are subject to external restrictions on how they may be used.

Governmental Activities

Revenues for all governmental activities in 2019 were \$8,125.3 million, an increase of \$680.2 million from 2018. Over half of the City's revenues were derived from taxes which increased by \$387.3 million (8.3%). In addition, other revenues increased by \$252.0 million (64.9%) primarily due to interest income, fair market value adjustment, and miscellaneous revenues.

Expenses for governmental activities in 2019 were \$8,676.2 million, an increase of \$374.4 million (4.5%) over 2018. The amount that taxpayers paid for these governmental activities through City taxes was \$5,061.1 million. Some of this cost was paid by those who directly benefited from the programs (\$899.5 million), or by other governments and organizations that subsidized certain programs with grants and contributions (\$640.6 million).

The net position of the City's governmental activities decreased \$548.4 million to a deficit of \$30,676.1 million primarily due to increases in transportation and public safety expenses, offset by tax revenues and grants and unrestricted contributions.

The City paid \$1,524.1 million for the “public benefit” portion with other revenues such as state aid, interest, and miscellaneous income. Although the total net position of business-types activities was \$1,217.1 million, these resources cannot be used to make up for the deficit in net position in governmental activities. The City generally can only use this net position to finance the continuing operations of the water, sewer, Skyway, and airport activities.

Business-type Activities

Total Revenues of the City’s business-type activities increased by \$222.3 million in 2019 mostly from an increase in charges for services, rental income, and other general revenues. The Water Fund's total operating revenues decreased by \$29.6 million (3.8%) from 2018 primarily due to an increase in doubtful accounts resulting from uncollected water charges from prior years’ accounts receivable and a decrease in water charges of \$16.9 million (2.2%). The increase in the doubtful account funds collected is due to a change in policy that eliminated the practice shutting off a property’s water service for nonpayment. The Sewer Fund's total operating revenues decreased in 2019 by \$18.6 million (5.0%) primarily due to a decrease in pumpage and an increase in bad debt expense compared to the prior year.

Financial Analysis of the City’s Funds

- The General Fund ended 2019 with a total Fund Balance of \$335.9 million
- The General Fund expenditures on a budgetary basis were \$33.8 million less than budgeted expenditures primarily due to positive variances for General Government expenditures
- *Changes in fund balance - The City’s governmental funds increased by \$408.6 million in 2019.*

General Fund Budgetary Highlights

- The City’s 2019 General Fund Budget of \$3,888.5 million was approved by City Council on November 21, 2018.
- General Fund revenues ended the year \$55.2 million over the 2019 Final General Fund Budget primarily as a result of not using \$82 million of budgeted prior year available fund balance and lower than anticipated revenues from other sources.
- Expenditures were \$33.8 million less than budgeted amounts as a result of favorable variances in general government expenditures.

Capital Asset and Debt Administration

Capital Assets - The City’s capital assets for its governmental and business-type activities as of December 31, 2019 amount to \$27,231.1 million (net of accumulated depreciation). These capital assets include land, buildings and system improvements, machinery and equipment, roads, highways and bridges, and property, plants and equipment.

Debt

At the end of the current fiscal year, the City had \$7,745.0 million in General Obligation Bonds and \$163.5 million in General Obligation Certificates and Other Obligations outstanding. Other outstanding long-term debts are as follows: \$2,641.9 million in Sales Tax Securitization Corporation Bonds (STSC Bonds); \$245.4 million in Motor Fuel Tax Revenue Bonds; \$16.2 million in Tax Increment Financing Bonds; and \$16,117.2 million in Enterprise Fund Bonds and long-term obligations

Enterprise Fund Revenue Bonds and Notes - The City's total assets increased by \$1,209.4 million. This increase primarily relates to a \$213.8 million net increase in property taxes and \$981.9 million increase in capital assets as a result of the City's capital improvement program, primarily at O’Hare due to the ongoing

O'Hare 21 program. On January 1, 2019, the Hilton O'Hare was transferred to the City as the 30-year lease term with HLT O'Hare, Inc. ended on December 31, 2018. The Hilton O'Hare building was recorded at a fair value of \$68.8 million in the financials as a capital contribution.

The City's General Obligation Bonds and Notes outstanding decreased by \$299.3 million during the current fiscal year due to payments on General Obligation Bonds and other debt and refunding of \$787.7 million, as well as a net decrease in Line of Credit balances of \$233.6 million, offset by \$722.0 million in General Obligation Bonds. In December 2019, Fitch Ratings, Moody's, and Standard and Poor's withdrew their ratings on the City's Water Revenue Bonds (First Lien) as all of the outstanding Water bonds were defeased. In November 2019, S&P Global Ratings assigned an AA- rating to the Sales Tax Securitization Corporation's second lien sales tax securitization bonds. During 2020, there were rating changes for the STSC Senior Lien Sales Tax Securitization bonds and the MFT bonds, and there were rating outlook changes for the City's General Obligation Bonds and STSC First and Second Lien Bonds.

Sales Tax Securitization Corporation Bonds: The City's deferred outflows and deferred inflows decreased by \$1,214.7 million and \$1,966.5 million respectively, primarily due to changes in assumptions for pension activities. The City's total liabilities increased by \$2,055.6 million primarily due to net pension liability and Sales Tax Securitization Corporation (STSC Sales Tax Securitization Bonds Series 2019A (\$605.4 million)).

Economic Factors and Financial Concerns

Regional, national, and global economies play a major role in the City's finances and economic outlook. The global COVID-19 pandemic will have a significant negative impact on economic conditions in 2020 and future years. The City stated in May 2020 that it anticipates a \$700 million revenue shortfall compared to the budget for the 2020 Fiscal Year. This shortfall may be addressed through a combination of expenditure reductions, revenue increasing policy and financial measures, delayed programs, and prioritizing pandemic response efforts that are reimbursable through Federal assistance.

The City must develop a sound financial strategy to better manage governmental activities to reduce the reliance on business-type activities. Because of the downturn in the economy coupled with the growing net pension liability; the City's future financial positions are in need of significant reassessment. This negative outlook will affect the City's ability to borrow and continue its unfavorable bond ratings. This will ultimately have a negative impact on taxpayers and city services.