STATEMENT MADE AT THE PUBLIC HEARING ON THE PROPOSED FY2002 METROPOLITAN WATER RECLAMATION DISTRICT OF GREATER CHICAGO, DECEMBER 12, 2001

The Civic Federation would like to thank the President and the Board of Commissioners for this opportunity to comment on the proposed FY2002 budget of the Metropolitan Water Reclamation District (MWRD). We would also like to commend the MWRD's Budget and Finance staffs for their hard work and effort in preparing this budget in these difficult times as we face a looming recession and heightened security concerns.

I. OVERVIEW OF TESTIMONY

The Civic Federation **opposes** the property tax increase proposed in the MWRD's proposed FY2002 budget. Simply put, we do not feel that increasing taxes in this time of recession is a prudent action. Thus, we are opposing all local government tax hikes this year, even if they are modest.

The Civic Federation believes governments must do everything possible to focus on cutting costs or enhancing non-tax resources. To this point, we question why a property tax hike is necessary when the MWRD has historically maintained large fund balances.

While The Civic Federation opposes the property tax increase, we do commend the MWRD for maintaining good financial condition. Long-term debt has declined, the District's bond ratings are excellent, and pension fund assets are more than sufficient to cover liabilities.

The Civic Federation also commends the MWRD on producing an excellent budget document. The budget is cutting edge in format and style, informative and very user friendly. We also applaud the District for utilizing best practice financial management techniques, such as financial policies and long-term financial planning

Based on our analysis of the budget, audited financial reports and Civic Federation research The Civic Federation offers the following policy recommendation and notes several issues of concern.

Recommendations: Consider Reducing Large Fund Balances, Implement Joint Health Insurance Purchasing

Given that the U.S. is now in a recession, the MWRD may well endure more bad fiscal news during FY2002. Thus, it is imperative that the District undertake measures that can generate additional budgetary savings and help both policymakers and staff plan strategically for future contingencies. The Civic Federation recommends that MWRD pursue the measures outlined below to reduce the tax burden and generate additional budgetary savings.

MWRD Should Consider Reducing Historically High Fund Balances

From FY1996 to FY2000, the MWRD's General and Special Revenue fund balances averaged $148 million while expenditures averaged $258 million. This is a fund balance/expenditure ratio of 57%, high by most standards. This high rating suggests that the MWRD should consider shifting toward longer-term holdings, retiring debt or adjusting the income streams feeding the funds to bring income into line with current spending requirements.

Join with Chicago Area Governments to Pursue Joint Purchasing of Health Insurance

The cost of health care is rising rapidly once again. In the first quarter of 2001, the cost of medical care services rose by 4.9% alone.[1] Indeed, the MWRD's tentative FY2002 budget forecasts a 10% to 12% increase in health care costs for the District in the near term.[2]

To contain skyrocketing health care costs, The Civic Federation urges the MWRD to aggressively pursue the joint purchasing of health care insurance with other governments in the Chicago area. A recent study conducted for The Civic Federation on the feasibility of consolidated health insurance purchasing found that forming a joint insurance pool consisting of the employees of the City of Chicago, Cook County (excluding the Forest Preserve District), Chicago Park District, Chicago Transit Authority, the City Colleges of Chicago, the Chicago Public Schools and the Chicago Housing Authority could yield projected savings of $40.1 million in the first year or $222 million over a 5-year period.[3]

Concerns: Property Tax Refunds, Short-Term Debt Increase

The Civic Federation has comments on several financial issues. They are presented below.

Property Tax Appeal Board Decisions Could Lead to Substantial MWRD Revenue Loss

The Civic Federation is very concerned that recent decisions by the Illinois Property Tax Appeal Board (PTAB) could result in potentially huge losses in Chicago area local government revenue. If the decisions stand and are applied to all eligible property within the District's boundaries, the MWRD could face a loss of $30 million per year.

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[1] Health Care Financing Administration. Recent Changes in Medical Prices: 1997-2001. See www.hfca.gov/stats/indicatr/tables/t9.htm.
[2] See Metropolitan Water Reclamation District Tentative FY2002 Budget, p. 3.
[3] The Civic Federation. *Feasibility Study of Consolidated Purchasing: Chicago Public Employers*. A Study Conducted by the Segal Company. February 23, 2001.

Rapid Growth in Short-Term Debt

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 future financial difficulties. The MWRD's short-term debt obligations grew 41% between FY1996 and FY2000. This increasing trends bears watching, particularly as short-term debt rose slowly between FY1993 and FY1998.[4]

II. FY2002 BUDGET SUMMARY

The MWRD's proposed FY2002 total appropriation is $793.3 million. This is a decrease of $182 million from FY2001.

The District is requesting a $4.3 million, or 1.1% increase in its total property tax levy, from $381 to $385 million. The District argues that the increase is needed because of: a) reductions in revenues from the personal property replacement tax (PPRT), investments, and net assets appropriable; and b) increased expenditures for health care, early retirement contributions, and salary increases. The District will eliminate 17 positions to cut costs.

III. FINANCIAL ISSUES AND TRENDS

This section provides summaries of key expenditure and revenue issues and trends likely to impact the MWRD's financial situation in the forthcoming fiscal year.

Recent Property Tax Appeal Board Decisions: MWRD Faces Potential Annual Loss of $30 million

Recent decisions by the Illinois Property Tax Appeal Board (PTAB) could result in potentially huge losses in local government revenue. If the decisions stand and are applied to all property in the county, The Civic Federation's projections indicate that the MWRD could face a loss of $30 million per year. The maximum potential loss to all governmental units in Cook County could well exceed $500 million per year. These losses could come at a time when property assessment levels are soaring and revenue growth is anemic due to the economic downturn.

The Illinois State Constitution requires that the highest assessment level be no more than 2.5 times the lowest assessment level. The Cook County ordinance that classifies property for taxation sets the lowest assessment level at 16% for residential property and the highest assessment level at 38% for commercial property. However, the Illinois Department of Revenue conducts studies every year claiming that residential property is actually assessed at closer to 10% of its value. Based on these studies, the PTAB has created a new level of assessment for non-residential (business and apartment) property. This new level of assessment is the result of multiplying the Department of Revenue's

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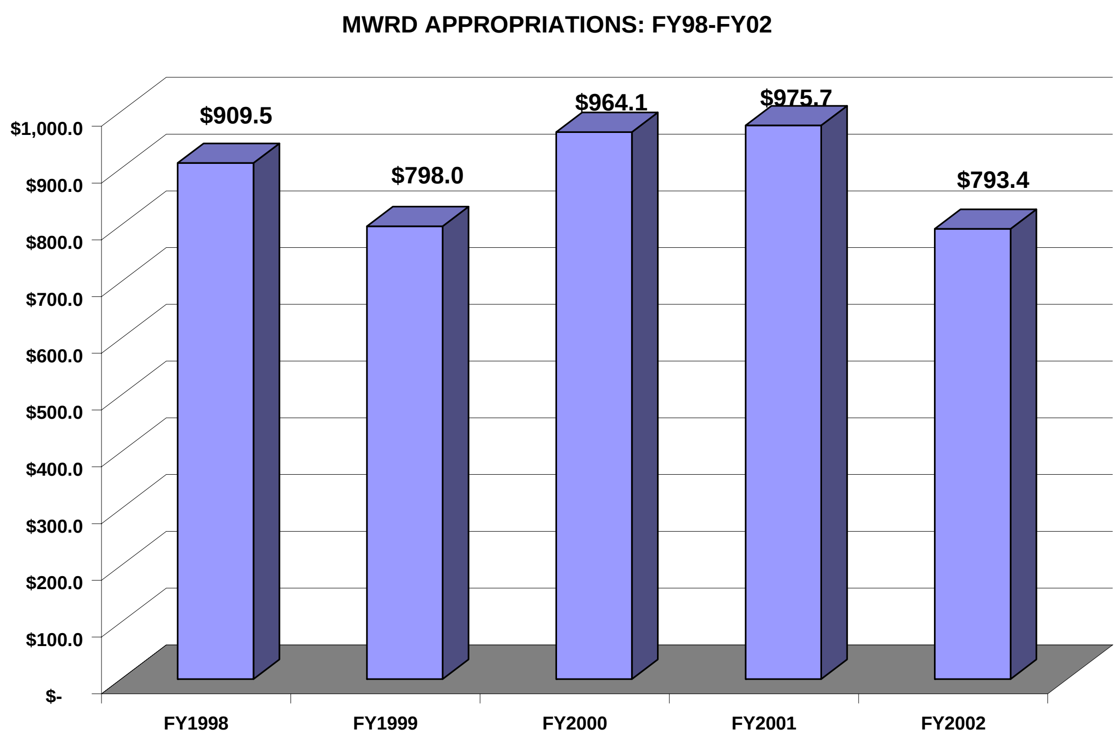
[4] See Short-term debt analysis in The Civic Federation. *Waterways for Our Future: Governance and Finance*. May 2000.

median residential assessment level of approximately 10% by 2.5. The result is a maximum assessment level of 25%. Therefore, a commercial property appealing its assessment to the PTAB would be assessed at 25% of its value, rather than 38% as the county ordinance directs. This lower assessment level, if applied to all properties currently assessed at more than 25% of full value, would result in large refunds for commercial and industrial properties.

Unless it is addressed soon, PTAB's decision has the potential to cause a serious fiscal crisis in Cook County. The Civic Federation believes that it is imperative that the MWRD join with other local governments and the State of Illinois to address local governments' overreliance on property taxes.

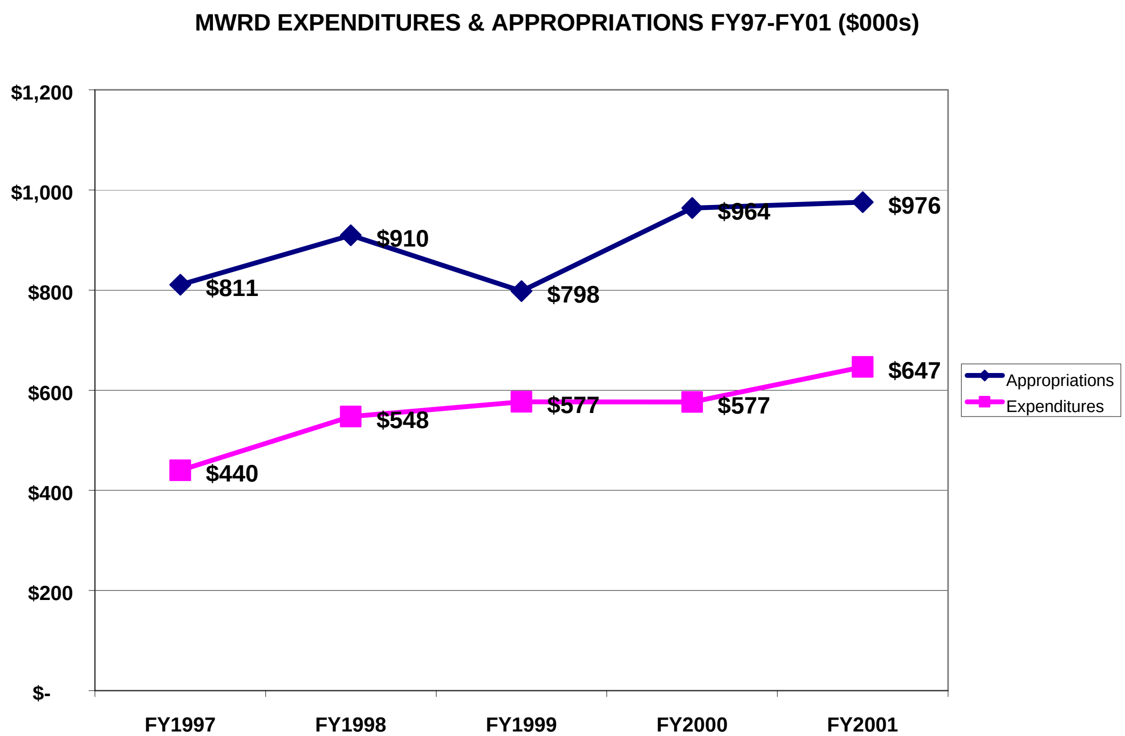
Appropriations: Down 19% in FY2002

The exhibit below shows MWRD appropriation trends between FY1998 and FY2002. The District proposes to appropriate $793.4 million in FY2002, roughly the same level as in FY1999. The sharp drop ($182 million) in appropriations from last year is primarily due to a decrease in appropriations for capital projects as major infrastructure projects are completed. Over the 5-year period of this analysis, appropriations will decline by $116 million, a 13% decrease.



Trend Toward Wide Variance Between Expenditures and Appropriations

The MWRD has for many years appropriated far more in resources than it spends, as the exhibit below shows. The variance between expenditures and appropriations averaged $334 million between FY1997 and FY2002. Thus, during those years, the MWRD spent an average of only 63% of what it appropriated. This raises questions regarding whether the District is over appropriating far in excess of maintaining prudent reserves.



MWRD Maintained High Fund Balances FY1996-FY2000

The MWRD has maintained high fund balances, according to a review of its audited financial statements. In order to assess the size of the fund balances, the Civic Federation has devised a current fund balance ratio which divides the dollar amount of General and Special Revenue Fund balances by combined General and Special Revenue Fund expenditures.

The exhibit below, which presents ratios from FY1996-FY00, shows that MWRD General and Special Revenue fund balances averaged $148 million. During that same period, the District's current fund balance ratio averaged 57%, giving it a "High" cash solvency rating. This suggests that the MWRD should consider shifting toward longer-term holdings, retiring debt or adjusting the income streams feeding the funds to bring income into line with current spending requirements.

MWRD CURRENT FUND BALANCE RATIO			
FY	GF & SRF Fund Balance	GF & SRF Operating Exp.	Ratio
1996	$ 129,957,000	$ 242,791,000	54%
1997	$ 133,268,000	$ 242,791,000	55%
1998	$ 152,015,000	$ 252,318,000	60%
1999	$ 157,451,000	$ 273,000,000	58%
2000	$ 167,109,000	$ 281,824,000	59%
Average	$ 147,960,000	$ 258,544,800	57%

Property Tax Levy: 1.1% Increase to $385 Million

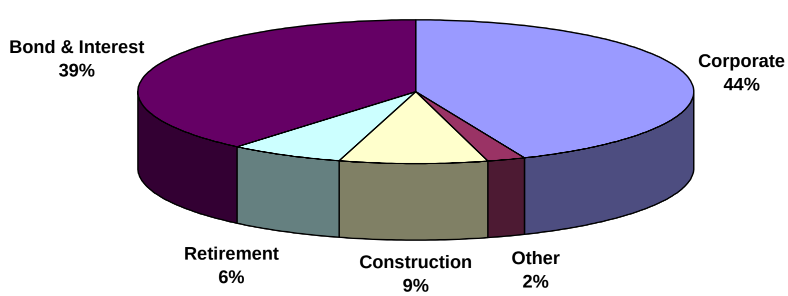
The MWRD proposes to increase its property tax levy by 1.1% in FY2002, from $381 million to $385 million. This includes increases of $8.8 million for the Corporate Funds, $4.7 million for the Bond and Interest Fund, $100,000 in the Retirement Fund, and $600,000 in the Corporate Working Cash and Reserve Claim Funds. The Construction Fund was decreased by $500,000. The total levy has increased by 13% since FY1998.

The exhibit below shows the distribution of the MWRD property tax levy proposed for the FY2002 budget. The Corporate Fund and the Bond and Interest Funds consume 83% of the total levy while four smaller funds split the remaining 17%. The “other” category includes the corporate working cash and reserve claim funds.

Personnel: 17 Fewer Positions in FY2002

The MWRD workforce has remained fairly constant over the past five years, averaging 2,253 positions. 2,257 positions are budgeted for FY2002, a decrease of 17 positions. Since FY1998, there has been an overall increase of 18 positions from FY1998. The Corporate Fund funds approximately 90% of the positions. The remaining 10% are

MWRD PROPERTY TAX LEVY DISTRIBUTION BY FUND FY2002



funded by the Capital Improvements Bond Fund.

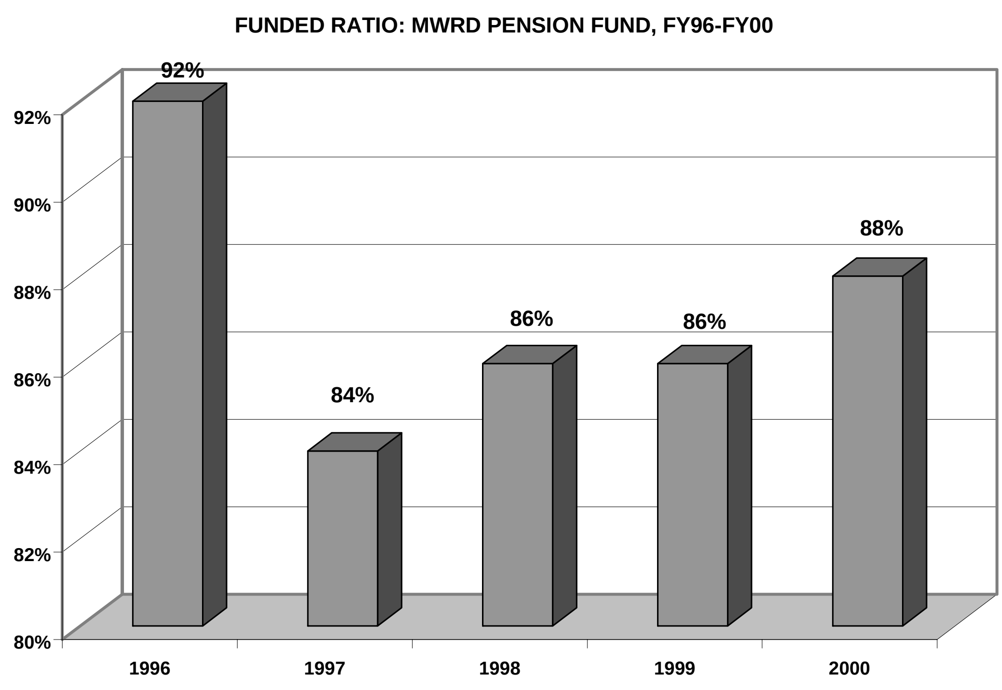
Pension Trends

The Civic Federation used three measures to present a multi-year evaluation of the fiscal health of the MWRD's pension fund: funded ratios, the investment rate of return and the value of unfunded liabilities.[5]

Funded Ratios – Actuarial Value of Assets

The following exhibit shows the funded ratio for the MWRD's pension fund. This ratio shows the percentage of pension liabilities covered by assets. The lower the percentage the more difficulty a government may have in meeting future obligations.

The funded ratio for the MWRD's pension fund averaged 87% from FY1996 to FY2000. Thus, during this period, the MWRD had more than sufficient assets to cover pension liabilities in the long term.

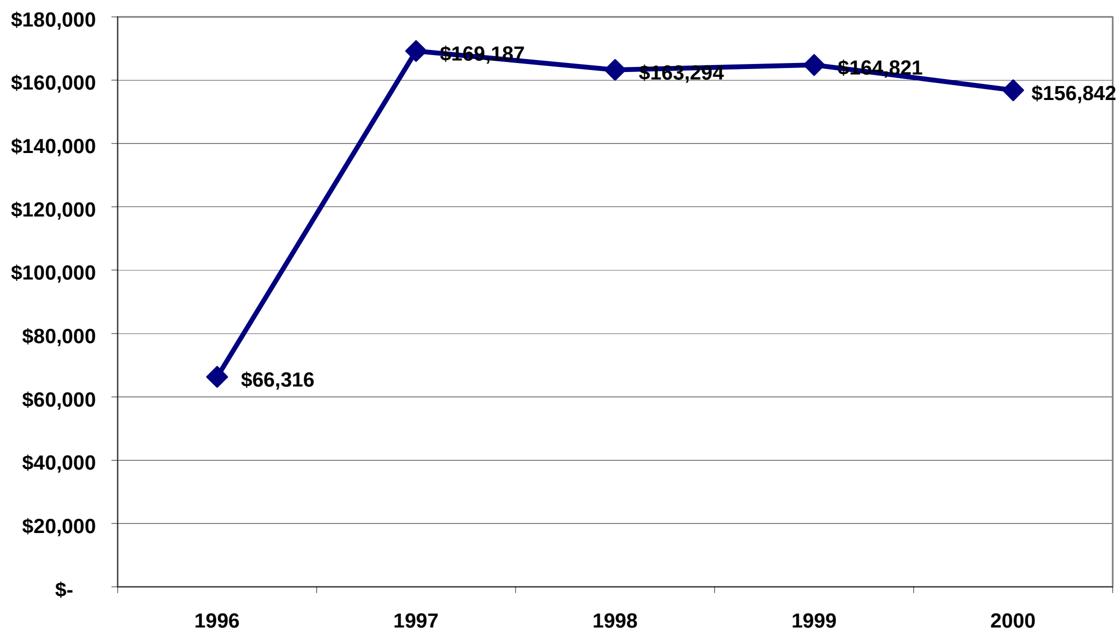


[5] The discussion of Chicago Park District's pension fund trends is drawn from Myer Blank. *Status of Local Pension Funding* (Chicago: Civic Federation, 2001).

Unfunded Liabilities

Unfunded liabilities are the dollar value of pension liabilities not covered by assets. As the exhibit below shows, unfunded liabilities for the MWRD's pension fund totaled approximately $156 million in FY2000. This was a substantial 137% increase since FY1996. Much of the increase came between FY1996 and FY1997, when unfunded liabilities rose by over $102 million, a 155% increase. Between FY1999 to FY2000, unfunded liabilities fell by almost $8 million.

UNFUNDED PENSION LIABILITIES:
FY96-FY00 ($000s)

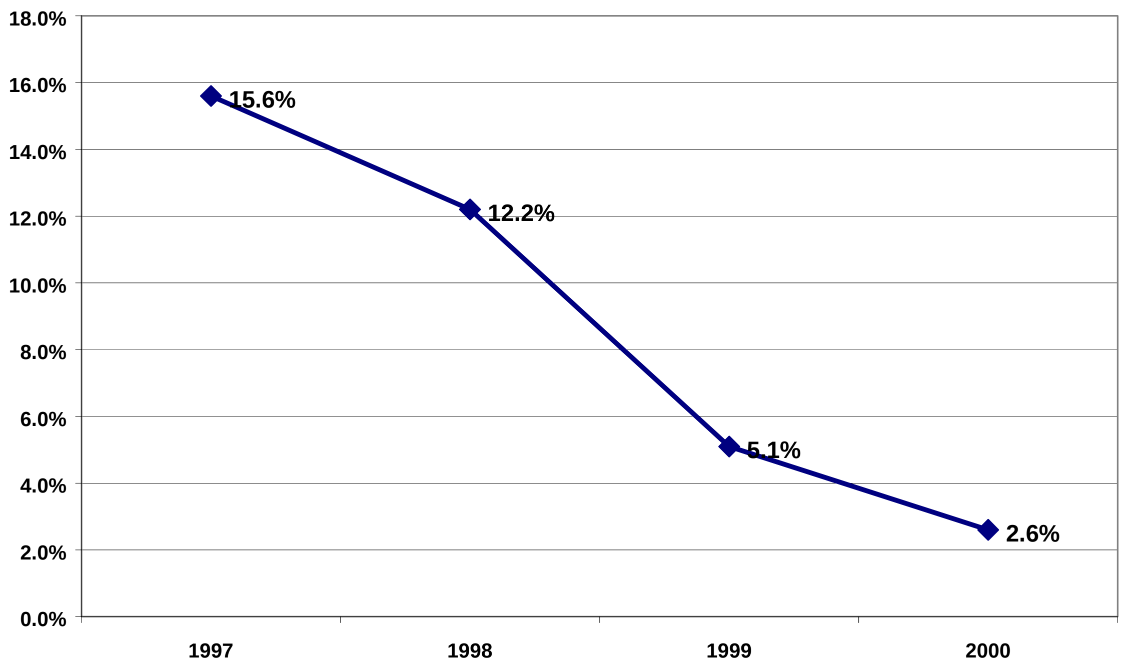


Investment Rates of Return

Investment returns for the MWRD pension fund fell sharply between FY1997 and FY2000 because of declining financial markets, as the following exhibit illustrates. The Fund's rate of return fell from 15.6% in FY1997 to just 2.6% in FY2000. Investment income typically provides a significant portion (over 50%) of the funding for pension funds.

Clearly, investment income is down sharply from the boom years of the 1990s. However, this is not necessarily a cause for concern at this time. Because the stock market has increased in value over the long-term, the pension funds' investment income (which is derived largely from stock market investments) is likely to rise over time as well. It is also important to note that the MWRD's pension fund currently is well funded.

MWRD PENSION FUND INVESTMENT RATES OF RETURN: FY97-FY00



Debt Trends

The Civic Federation has employed two measures of debt for purposes of this analysis: short-term debt trends and long-term debt per capita trends.

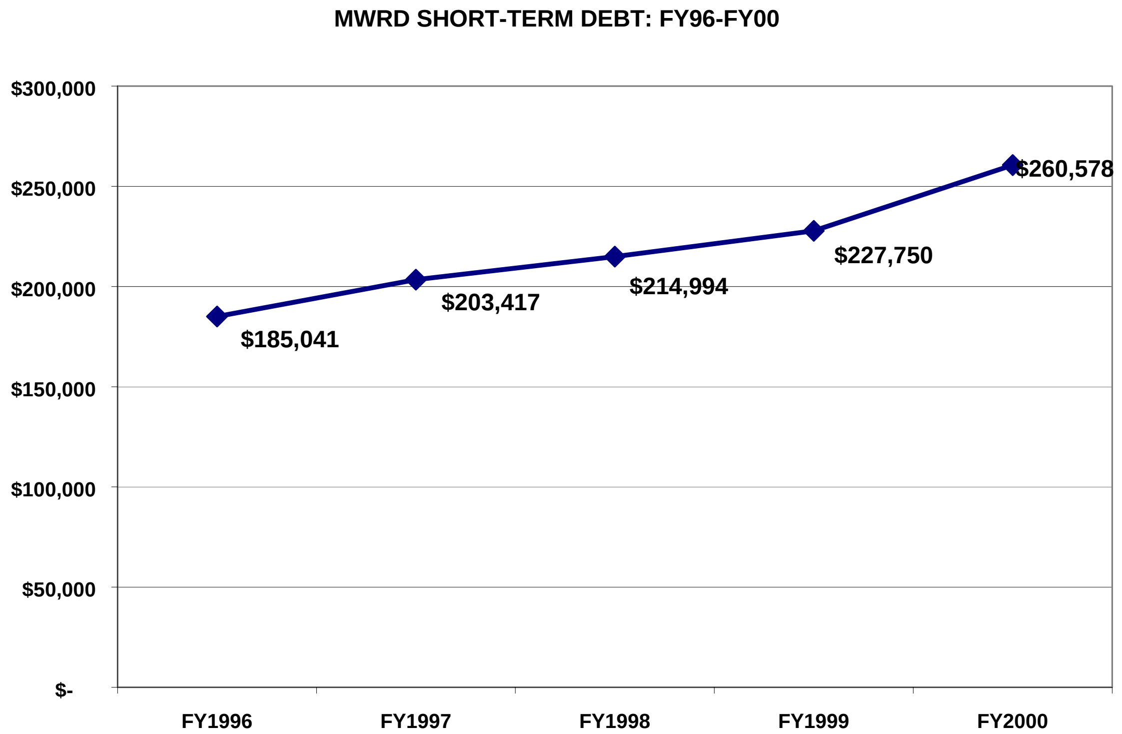
Short-Term Debt Trends

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 future financial difficulties. It is a measure of budgetary solvency, that is, a government's ability to generate enough revenue over the course of a normal budgetary period to meet its expenditures and prevent deficits.

Short-term debt in the General and Special Revenue Funds includes obligations such as accounts payable, contracts payable, deposits, interest payable, interest, due to other funds, and liabilities from restricted assets. In sum, it includes all liabilities except accrued salaries and wages, accrued payroll, compensated absences and long-term debt.

The exhibit below shows that the MWRD's short-term debt obligations grew rapidly over the 5 years of this analysis. It rose from $185 million to $260 million, a steep 41%

increase. This increasing trend bears watching, particularly as short-term debt rose slowly between FY1993 and FY1998.[6]

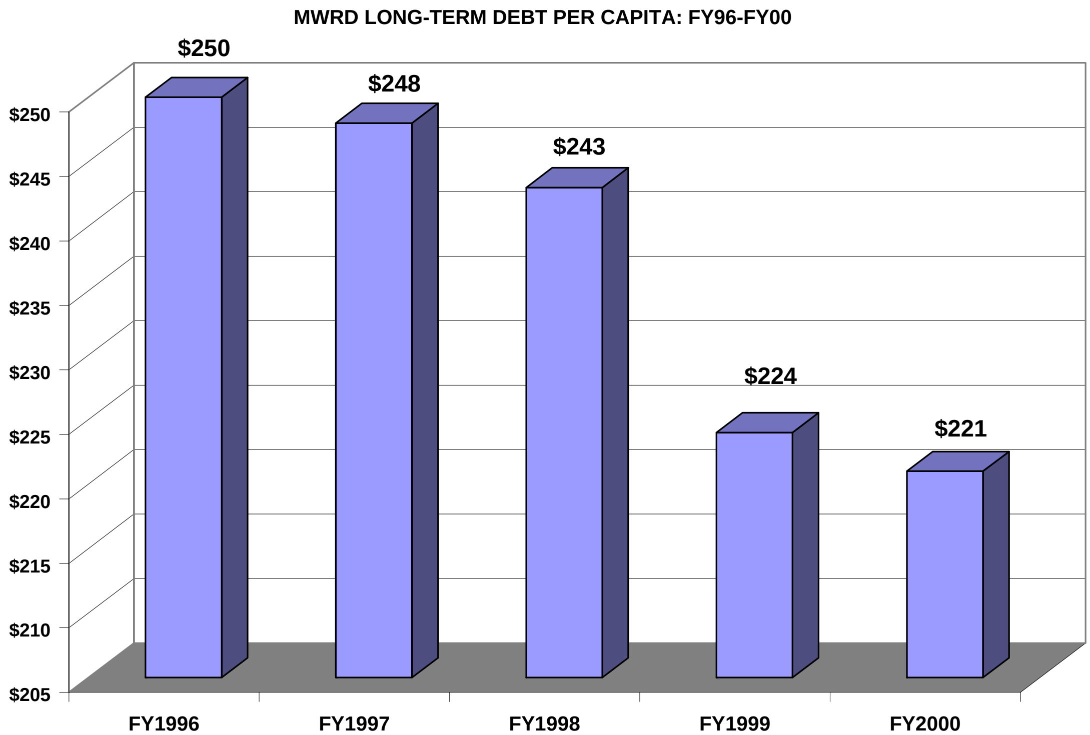


Long-Term Debt Per Capita

Long-term debt per capita is a measure of a government's ability to maintain its current financial policies. This long-term debt analysis takes the total liabilities in the General Long-Term Obligations Account Group and divides them by population. The MWRD's long-term debt includes general obligation bonds payable, capital leases payable, compensated absences, claims and judgments payable, and worker's compensation. Increases in this indicator bear watching as a potential sign of increasing financial risk.

MWRD long-term debt per capita decreased by 11% between FY1996 and FY2000, falling from $250 to $221. During the same period, the Consumer Price Index for the Chicago metropolitan region rose by 18.5%. Total long-term debt decreased from $1.3 billion to $1.1 billion, falling in each one of the 5 years. The drop in long-term debt is a positive indicator.

[6] See Short-term debt analysis in The Civic Federation. *Waterways for Our Future: Governance and Finance*. May 2000.



IV. SUMMARY

The Civic Federation opposes the property tax increase proposed in the MWRD's FY2002 budget. We believe in this time of recession all local governments, including the MWRD should avoid tax hikes. We urge the MWRD to consider entering into a joint purchasing agreement for health insurance with other local governments and to consider reducing its historically very large fund balances.

Respectfully Submitted,

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