ANALYSIS OF THE
THE CHICAGO PUBLIC SCHOOLS
FY2004 PROPOSED BUDGET

Prepared By:
The Civic Federation
June 20, 2003

INTRODUCTION

The Civic Federation recently concluded an analysis of financial issues related to the Chicago Public Schools proposed FY2004 budget. Based upon that review and a consideration of some key issues that we believe will have an impact in the future upon the District's long-term financial condition, we would like to offer the following comments. At this time, we would also like to commend Management and Budget Director John Maiorca and his staff for their hard work and effort in preparing this budget and their willingness to provide the Civic Federation with a briefing and answers to our follow up questions.

The Civic Federation was pleased that Chief Executive Officer Arne Duncan and the CPS leadership were successful in convincing Governor Blagojevich and the General Assembly to increase their commitment to public education funding by increasing the foundation level to $4,810. We hope that this is the beginning of a serious multi-year effort to fulfill the State's commitment to assume its primary responsibility for education funding and reduce Illinois' historic and burdensome overreliance on property taxes to fund our schools.

We commend the Chicago Public Schools for providing full funding for its charter schools and we are encouraged that enrollment in the District's charter schools is expected to top 10,000 next year. We have long supported the charter school movement and are encouraged that Governor Blagojevich has signed legislation expanding the number of charter schools in Chicago from 15 to 30. It is our hope that the two new charter schools opening this year will be joined by others and continue to serve as an important laboratory for both educational curriculum advancements and management efficiencies.

The Civic Federation would also like to congratulate the CPS for pursuing efforts to generate budgetary savings by joining with 6 other local governments to request proposals for the provision of joint prescription drug benefits to their employees. On January 28, 2003, the seven local governments took a historic first step when they jointly put out to bid the purchase of the prescription drug benefits for their combined 270,000 employees, spouses and children. The contracts for the 2.5 million prescriptions are expected to provide dramatic savings. At a time when Chicago's local governments have faced rising health care costs and two years of deficits from slow revenue growth, pooling government resources to maximize purchasing power and minimize costs is a responsible way to conserve taxpayer dollars.

The Civic Federation also appreciates the difficulties the Chicago School District faces in its efforts to maintain critical programs in a time of recession, attempting to balance the needs of children with serious fiscal constraints. However, the Civic Federation is disappointed with some of the strategies the District appears to be using to craft the FY2004 budget.

Although the FY2004 budget includes over $70 million in new state funds and $90 million in new federal funds, we are disappointed that rather than cut non-essential or redundant programs, the budget includes a $36 million property tax increase and makes only a minimal 30-position reduction in a total headcount of 47,319. Although the proposed FY2004 budget for Central Office staff will see a reduction of 144, this represents a total cut of only 11 jobs since the CPS reform administration's first budget in FY1996 when there were 1,192 Central Office positions.

Increasing property taxes to the maximum amount allowed by tax caps should not be viewed as a justifiable tradition at the CPS. The District has increased its property tax extension to the maximum amount allowed in 6 of the past 7 tax years, more times than any other major taxing body in Cook County. The District's average property tax increase since FY1995 has been 3.29%. This compares to a 1.6% average increase for the City of Chicago, a 1% average increase for the Chicago Park District and a 1.1% average increase for Cook County. Since 1995, the CPS portion of a typical tax bill has increased by 75%, from approximately $800 to $1400.

We are concerned that in this time of economic recession, the Chicago Public Schools is not recognizing the hardship created by increasing taxes. Greater efforts must be made to reduce spending through implementation of cost saving efficiencies and reductions. The proposed CPS budget for FY2004 dramatically contrasts with other local governments that have made painful choices to reduce headcount and hold the line on taxes. In 2003, other local governments in Cook County took the following gap-closing actions:

- The *City of Chicago* laid off 200 employees and eliminated 1000 vacancies, continued a hiring freeze and overtime cutbacks for savings of $30 million, cut $21 million in non-personnel areas and saved $7 million through departmental consolidations;
- *Cook County* eliminated 357 positions and froze its property tax levy at the 2002 level;
- The *Chicago Park District* eliminated 180 full and part-time positions, cut tax subsidies to cultural institutions by $1.1 million and reduced contractual service spending by $3.8 million; and
- The *Forest Preserve District of Cook County* eliminated 473 positions.

The City of Chicago has already announced that further staff reductions may be necessary this year to balance its budget. We urge the Chicago Public Schools administration to follow Mayor Daley and President Stroger's leadership and bring greater attention to improving the efficiency and reducing the cost of the over 17,000 non-teaching positions.

In summary, the Civic Federation commends the CPS leadership for their continuing efforts to bring educational innovations and increased resources to local classrooms. However, we urge the leadership of the CPS to follow the lead of Mayor Daley and other major local government leaders and focus efforts on devising bold and innovative strategies that markedly improve the quality of government service and reduce the cost of non-classroom functions. Stronger efforts should be made to reduce the size of the central bureaucracy and the 17,000 non-teaching staff at the Chicago Public Schools.

FINANCIAL ISSUES AND TRENDS

This section provides summaries of key issues likely to have an impact on the Chicago Public Schools' financial situation in the forthcoming fiscal year as well as expenditure, appropriation and revenue trends.

FY2004 Budget Highlights: 2.4% Property Tax Increase, 30 Jobs Cut

The Chicago Public Schools has proposed a FY2004 budget of $4.8 billion. The budget will be over $200 million larger than in FY2003. The District has projected a deficit of over $190 million this year.

The CPS is using a number of gap-closing measures in its FY2004 budget, including:

- A property tax increase of $36 million;
- $70 million increase in state aid;
- $23 million saved from eliminating 450 positions;
- Non-personnel spending reductions of $12 million to $15 million; and
- $48.7 million transferred from the District's reserve funds.

The CPS estimates that $35 million will be saved in FY2004 from administration cost reductions and 450 layoffs. However, the $35 million is not a net saving because the funds will be redirected to other programs. The administrative cost-cutting actions taken include: closing five schools with low enrollments, consolidating four others into two, tightening purchasing procedures, departmental mergers and reducing utility costs. The 450 layoffs include 300 on the Chicago Public Schools payroll and 150 who worked for privatized janitorial firms.[1]

The FY2004 budget includes several new spending initiatives. $440 million is designated for new capital spending. The $35 million saved from the cuts outlined above will be used to fund the expansion of several initiatives. Some of these include:

- 1,350 new full day pre-school slots;
- Over 6,000 new classroom slots to relieve overcrowding;
- 18 new schools, including charter schools;
- Expanded programs in the Chicago Reading Initiative;
- The new Chicago Math and Science Initiative;
- The Step Up summer program, a voluntary math and English program for incoming freshmen;
- Expanded summer school for high school students;
- 6,000 summer jobs (1,000 student increase from last year);
- Additional funding for high school security;
- A new Department of Post-Secondary Education;
- A new office of Principal Development;
- Expanding the Summer Fellows program; and
- A new student information system to consolidate test scores, grades, health and attendance records.

The Chicago School District has 437,618 students enrolled in 600 schools. Over 284,000 of those students attend elementary schools and 99,000 are enrolled in high schools. The remaining 53,000 pupils attend pre-school or kindergarten programs.[2]

How do the Chicago Public School District's gap-closing actions compare to other large urban school districts around the nation? The following bullets provide a sample.

Houston:

- $160 million deficit
- 360 central administration positions eliminated
- 100 vacancies eliminated
- Outsourcing painting work, downsizing the warehouse

Los Angeles:

- $440 million in cuts during FY03
- $400 million deficit FY2004
- 10% cut at central administration, 1.6% cut in the schools

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[1] *Chicago Tribune*, "Schools to Raise Taxes, Cut 450 Jobs," June 10, 2003.
[2] 2001 figures from CPS Web site – www.cps.k12.il.us/atAGlance.html.

- Increased efficiencies in purchasing, human resources and business functions
- 3-day furlough for central office managers

New York City:

- $650 million in cuts during FY03
- $130 million cut in FY2004
- Reduced construction costs by 29%
- $30 million in private contributions to train people

Philadelphia:

- $65 million deficit
- Facilities operations efficiencies - $14 million
- Reducing Workmen's Compensation Claims - $9.5 million
- Eliminating Non-School Vacancies - $8.5 million
- Reducing Personal Services Contracts - $6.6 million

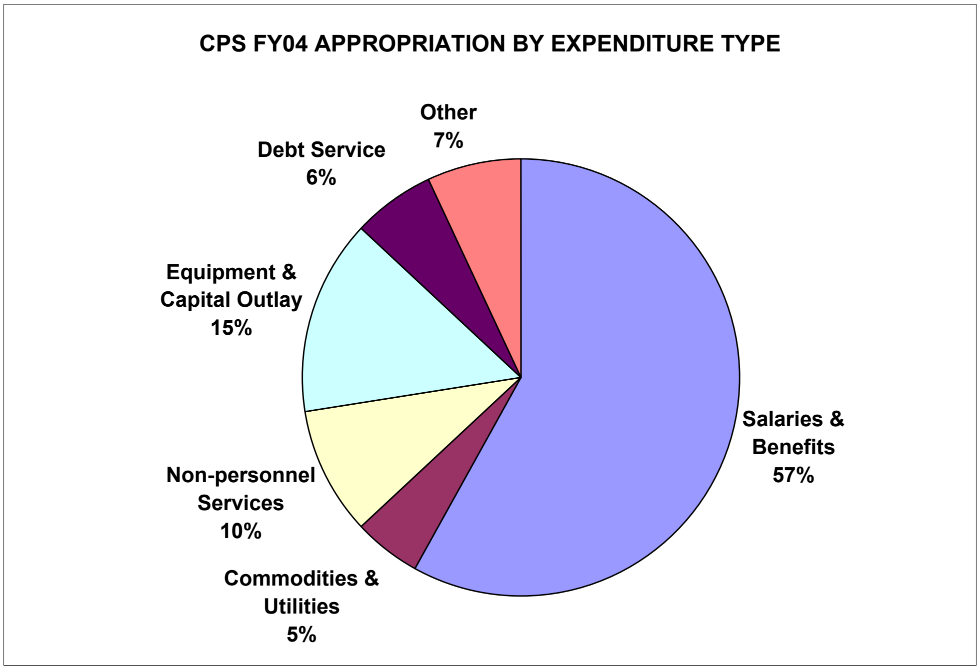
Appropriations and Expenditures

The FY2004 Chicago Public Schools budget proposes a total appropriation of $4.8 billion. This is a 4.3% increase from the previous year's appropriation of $4.6 billion. Approximately 58% of the appropriations are earmarked for salaries and benefits. $1.7 billion or 36% of the total is reserved for teachers' salaries, while $481 million is proposed for non-teacher salaries. $579 million is allocated for employee benefits expenses. This represents a 10% increase from the previous year.

CPS APPROPRIATIONS BY EXPENDITURE TYPE: FY03 & FY04 All Funds			
Expenditure Type	**FY03**	**FY04**	**% Change**
Teacher Salaries	$ 1,691.5	$ 1,741.0	2.9%
Non-Teacher Salaries	$ 475.0	$ 481.3	1.3%
Employee Benefits	$ 525.0	$ 579.0	10.3%
Subtotal Compensation	**$ 2,691.0**	**$ 2,801.3**	**4.1%**
Commodities & Utilities	$ 231.5	$ 231.9	0.2%
Non-personnel Services	$ 457.0	$ 457.8	0.2%
Equipment/Capital Outlay	$ 683.5	$ 704.2	3.0%
Debt Service	$ 270.5	$ 287.3	6.2%
Other	$ 286.0	$ 335.2	17.2%
TOTAL	**$ 4,619.5**	**$ 4,817.7**	**4.3%**

Sources: FY2003 and FY2004 Budgets

The next exhibit shows the breakdown by percentage of expenditure types in the FY2004 budget. The largest single portion of the FY2004 appropriation is earmarked for salaries and benefits. 57% of the total, or $2.8 billion, will be used for teacher salaries, non-teacher compensation and employee benefits.



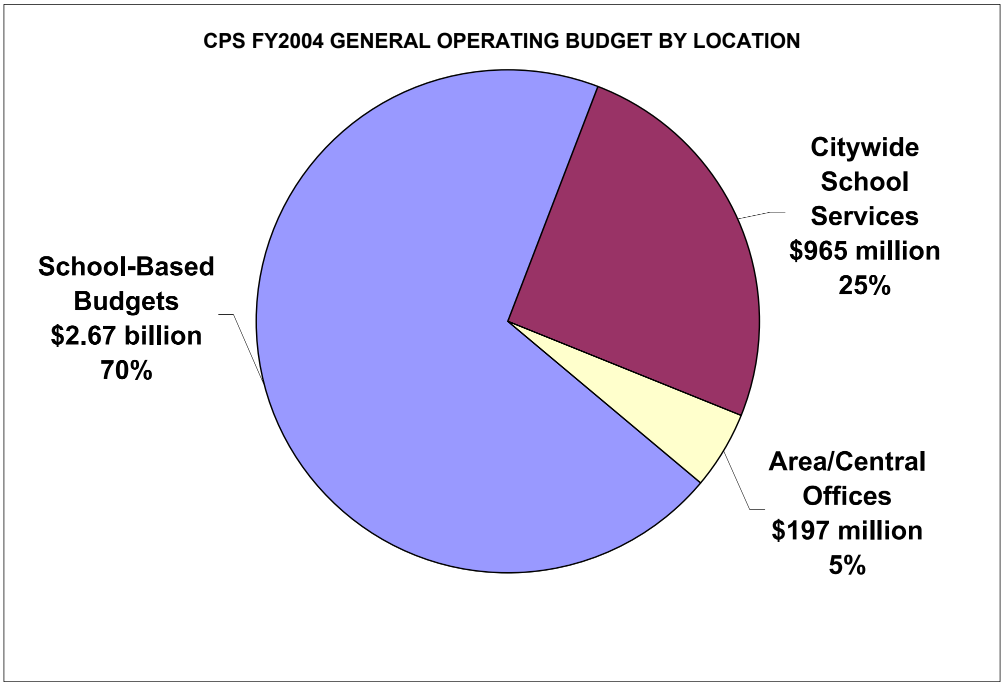
Changes in General Operating Fund appropriations by function are presented in the following exhibit. The FY2004 budget includes increases for instructional functions of $262 million, a 12% rise from FY2003. Regular instructional program will receive the biggest boost, a 19%, or $264 million increase. Vocational and Special Needs instructional programs, however, will be cut by 5%, from $287 million to $271 million.

Non-instructional programs will be cut this year. Support services will be cut by 2%, while community services will face a large 22% reduction. The State of Illinois had proposed elimination of the annual $65 million contribution to the Teachers' pension fund this year. However, the Board of Education has indicated that it will have adequate resources to meet its pension obligations this fiscal year because of the $30.6 million in Department of Commerce and Economic Opportunity construction funds and an estimated $34.4 million in additional funds the legislature provided that were not in the Governor's original FY2004 budget proposal.[3]

CPS APPROPRIATIONS BY FUNCTION General Operating Fund			
FUNCTION	**FY03**	**FY04**	**% CHANGE**
Instruction-Regular Programs	$ 1,424,734,731	$ 1,689,710,343	19%
Instruction-Special Education	$ 446,063,009	$ 459,719,328	3%
Instruction-Voc Ed & Special Needs	$ 287,152,727	$ 271,466,908	-5%
SUBTOTAL INSTRUCTION	**$ 2,157,950,467**	**$ 2,420,896,579**	**12%**
SUPPORTING SERVICES	$ 1,327,377,662	$ 1,295,557,012	-2%
COMMUNITY SERVICES	$ 56,144,581	$ 43,731,859	-22%
STATE REV. PENSION ADJUST.	$ 65,045,000	$ -	-100%
OTHER	$ 71,669,312	$ 80,485,420	12%
GRAND TOTAL	**$ 3,678,187,022**	**$ 3,840,670,870**	**4%**

[3] Chicago Public Schools FY2004 Budget, p. 53.

Almost $2.7 billion, or 70%, of the CPS General Operating budget will be used for elementary and high school budgets. 25% will be earmarked for Citywide School Services, which assigns resources to serve multiple school locations such as special education teachers, security personnel and maintenance workers. In addition, debt service payments, Workers' Compensation payments, tort liability and the CPS share of teachers' pension fund contributions are budgeted in Citywide units.

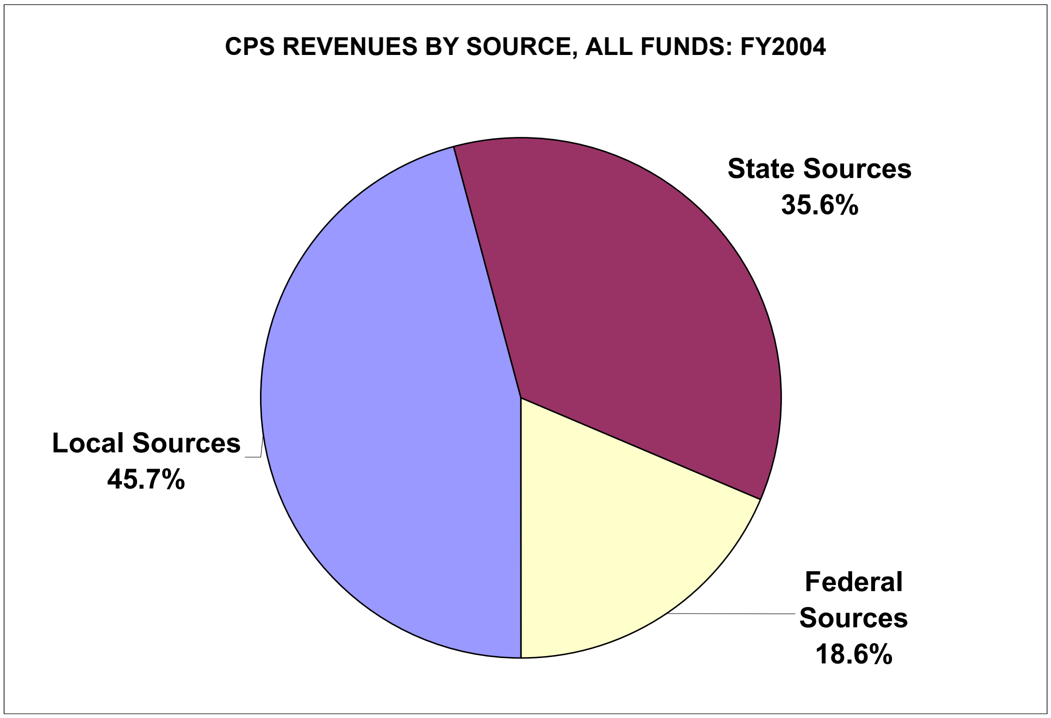


5-Year Appropriation Trends: Appropriations Increase by 21%.

Since FY2000, CPS appropriations have risen from $3.9 billion to $4.8 billion, a 21% increase. The largest percentage increase in that 5-year period was for debt service, which rose by 87%, from $53 million to $287 million. This reflects the District's aggressive capital program over the past several years. A correlated category, equipment and capital outlay increased by 38%, from $511 million to $704 million. During the period analyzed, compensation (salaries and benefits) rose by 16%.

Revenue Trends

The projected sources of Chicago Public School revenues for all funds in FY2004 are shown below. The largest source of funding is local revenues such as property taxes, which represents 45.7% or $1.9 billion of all revenues. State sources generate 35.5% or nearly $1.5 billion. Federal funds will be the third-largest revenue source at 18.6% of the total.



The next exhibit compares the Chicago Public Schools' FY2003 and FY2004 estimated resources and revenues for its General Operating Funds. The General Operating Funds include the District's General and Special Revenue Funds. Overall, CPS revenues are projected to grow by 8.5%, from $3.5 billion to $3.8 billion. This represents a $299 million increase.

In FY2004, the District's own-source revenues are expected to increase only slightly, by 1.9% or $31 million. Most of the increase can be attributed to revenues from the 2.4% property tax hike. The CPS will also tap into $73.7 of the District's fund balance in FY2004.

State revenues will increase at nearly the same rate as local resources, with a projected 2% rise. This will boost state support by $25 million. Federal support will increase by the greatest amount in FY2004, rising from $574 million to $779 million, a 35.7% increase.

CPS MAJOR RESOURCES & REVENUES: GENERAL OPERATING FUNDS			
Resources:	**Est. FY2003**	**Est. FY2004**	**% Change**
Total Beginning Fund Balance	$ 246.0	$ 234.9	-4.5%
Designated Fund Balance	$ (209.9)	$ (161.3)	-23.2%
Available for Appropriation	$ 36.1	$ 73.7	104.2%
Revenue Sources:			
Property Taxes	$ 1,488.5	$ 1,524.7	2.4%
PPRT	$ 48.4	$ 50.9	5.2%
Misc. Revenue/Non Revenues Sources	$ 100.9	$ 93.4	-7.4%
Subtotal Local Revenue	**$ 1,637.8**	**$ 1,669.1**	1.9%
General State Aid (GSA)	$ 481.5	$ 552.1	14.7%
Supplemental GSA	$ 261.0	$ 261.0	0.0%
State Aid Pension	$ 65.0	$ -	-100.0%
Other State	$ 485.9	$ 505.8	4.1%
Subtotal State	**$ 1,293.4**	**$ 1,318.9**	2.0%
ESEA Title I	$ 190.7	$ 274.5	43.9%
Lunchroom,Medicaid, Other	$ 176.9	$ 193.2	9.2%
Public Law: Special Education	$ 78.8	$ 90.1	14.3%
Federal Other	$ 127.7	$ 221.2	73.2%
Subtotal Federal	**$ 574.1**	**$ 779.0**	**35.7%**
GRAND TOTAL	**$ 3,541.4**	**$ 3,840.7**	**8.5%**

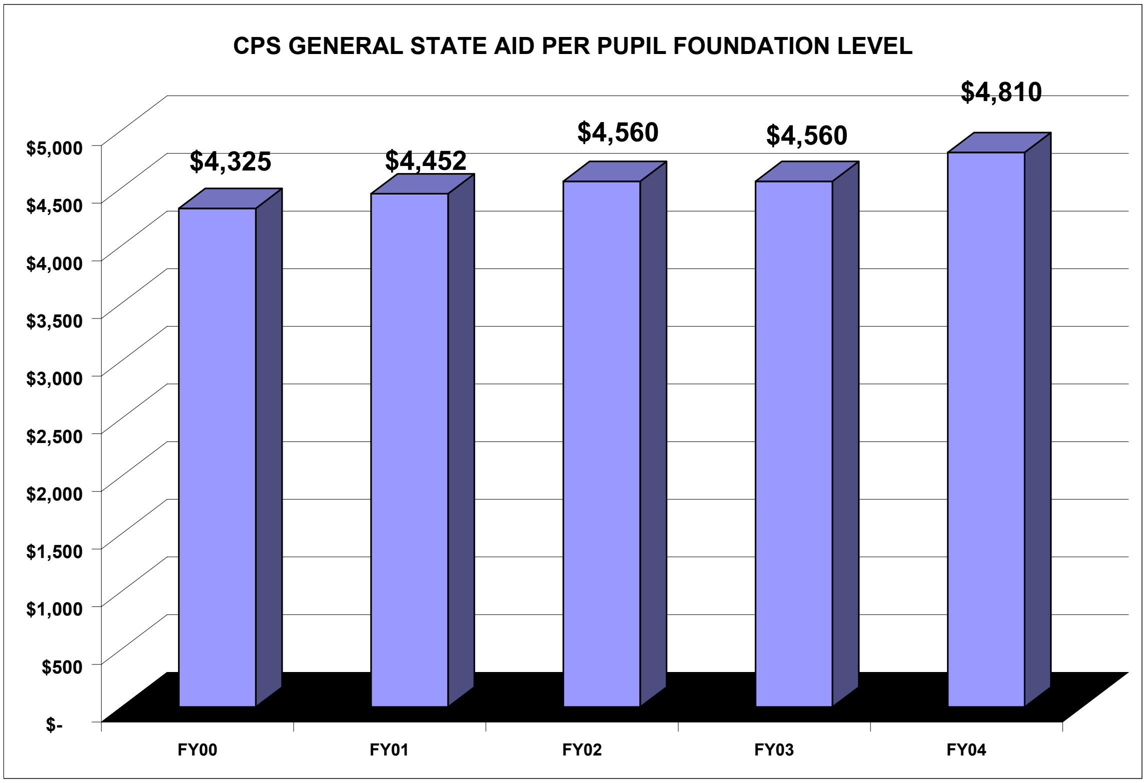
The assumptions used to project major revenue sources in the FY2004 budget include:

- Property Taxes will be increased to the 2.4% tax cap limit.
- Personal Property Replacement Tax (PPRT) projections are conservative, based on estimates of 4.3% growth in corporate taxes and 2.4% growth rate in invested capital taxes.
- State Categorical Program revenues are based on the K-12 appropriations approved by the General Assembly.
- The increase in General State Aid is based on the increase in the state foundation level from to $4,810. Supplemental General State Aid is based on the new poverty counts and formula adopted by the General Assembly.
- State Pension Aid has been eliminated in the FY2004 State budget. The CPS will be required to fund that $65 million contribution from its own resources.
- The gross Medicaid Reimbursement in FY2004 will be $36 million.
- Federal Revenue estimates are based upon the federal FY 2003 appropriation plus balances carried over from the prior fiscal year.

General State Aid to Increase to $4,810 per Pupil in FY2004

The Chicago Public Schools bases its FY2004 budget on legislation approved by the Illinois General Assembly and currently awaiting final action by Governor Blagojevich. The District expects to receive $30.6 million from the Department of Commerce and Economic Opportunity for capital projects as well as $100 million additional capital dollars from the statewide school capital program. General State Aid (GSA) is boosted in the FY2004 state budget from $4,560 to

$4,810 per pupil. This 5.5%, $250 per student increase is the first since FY2001. Since FY2000, GSA has increased by 11%.



Property Tax Levy Trends: Levy to Increase 2.4% in FY2004

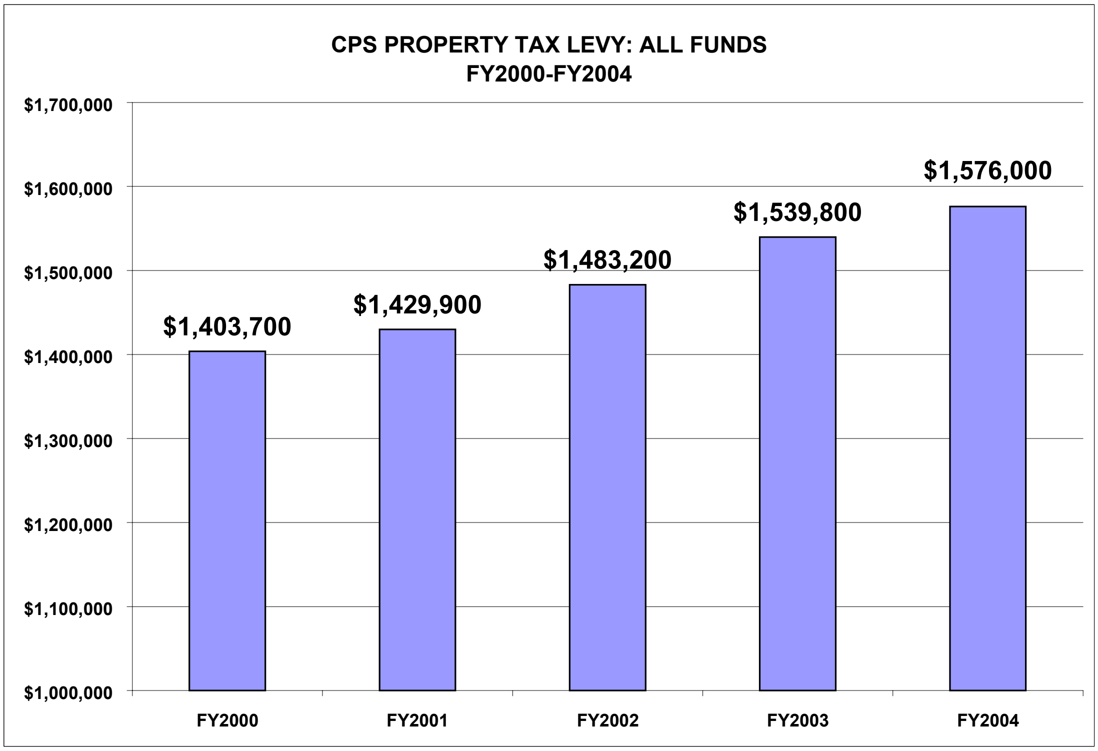
The Chicago Public Schools property tax levy for all funds is projected to increase by 2.4%, or $36 million, to $1.57 billion in FY2004. This is a $36.2 million increase. Property tax increases are limited to the rate of inflation or 5%, whichever is less, under the terms of the Illinois Property Tax Extension Limitation Law. This year, the Board of Education proposes to tax at the maximum limit allowed by the tax cap law.

Under the tax cap law, the increase in the property tax levy for tax year 2002 is limited to the inflation rate of 1.6%. The 0.8% additional increase, or $11 million of the $36 million total increase, is based upon the District's anticipation of the value of new property. The tax cap exempts the value of new buildings or additions to existing buildings from the limitation on the property tax levy.

The District argues that the average property tax increase for a typical Chicago homeowner will be $9 for a $100,000 home. However, there are several problems with this calculation. First, the median price of a home in Chicago is $170,000, according to the Chicago Association of Realtors. Second, the $9 figure is based on a projected increase of $25 million only and does not include the additional $11 million increase permitted under the tax cap law for "new" property. Therefore, the rate of tax increase should be based on the entire $36 million increase. A more precise rate of the tax increase per average home in 2004 would be $25 to $30, based on a $170,000 home and the entire $36 million levy increase.

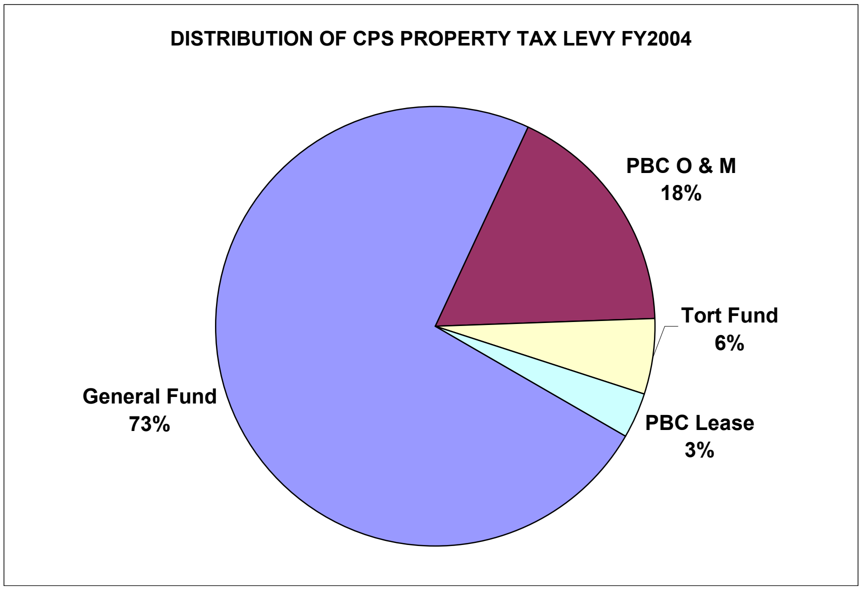
Since 1995, the CPS portion of a typical tax bill has increased by 60%, from approximately $800 to $1400. Adjusted for inflation, the increase is $350, or a rise of 45%.[4] These calculations are based on an average home price of $115,000 in 1995 and $170,000 in 2004.

97% of property tax levy funds in the FY2004 budget are earmarked for General Operating purposes. Since FY2000, the levy has increased by 12.3%.



The next exhibit shows the proposed distribution of property tax revenues by purpose in FY2004. 73% or $1.1 billion of the levy is earmarked for the General Fund to finance CPS operations. The second largest amount, $278 million is set-aside for the Public Building Commission Operations and Maintenance (PBC O & M) Fund, which supports the repair and maintenance of CPS buildings. 6% of the levy will be used for the Workers and Unemployment Compensation Tort Immunity Fund and 3% for Public Building Commission lease rental payments.

[4] The Consumer Price Index in the period 1995 to 2003 has risen by 9%.



Personnel Trends

The Chicago Public Schools propose to eliminate 450 positions in the FY2004 budget for a savings of $35 million. 300 of these positions are on the CPS payroll and 150 are janitorial workers employed under privatization contracts.

Since FY2000, the Chicago Public Schools have added 2,295 employees, a 5% increase. 79% of these additional employees, or 1,875 employees, were located in the schools. The percentage of Central Office employees during that same period increased by 10%, from 1,075 to 1,181. Citywide positions, which include employees for systemwide functions as well as teachers and employees who serve multiple school locations, rose by 18% between FY2000 and FY2004, from 2,779 to 3,279.

CPS BUDGETED POSITIONS BY LOCATION: FY00-FY04

Location	FY00	FY01	FY02	FY03	FY04	Change FY04-FY00
Schools	41,170	41,603	42,635	43,045	42,859	1,689
Citywide	2,779	3,056	3,363	3,019	3,279	500
Central	1,075	1,223	1,278	1,325	1,181	106
TOTAL	**45,024**	**45,882**	**47,276**	**47,389**	**47,319**	**2,295**

A closer look at the changes between the FY2003 and FY2004 budgets for personnel shows that a net total of 70 positions will be eliminated. 186 positions are scheduled to be cut in the schools and 144 in the Central Office. However, 260 positions will be added to the Citywide units.

CHANGE IN CPS BUDGETED POSITIONS BY LOCATION: FY03 & FY04				
Location	FY03	FY04	Increase	% Change
Schools	43,045	42,859	(186)	-0.4%
Citywide	3,019	3,279	260	8.6%
Central	1,325	1,181	(144)	-10.9%
TOTAL	47,389	47,319	(70)	-0.1%

The next chart shows changes in personnel by location since FY1996, the first budget proposed under the school reform law. It shows that during that time period, personnel in an all divisions grew by 3.7% or 1,696 positions. The Central Office was reduced by only 11 positions between FY1996 and FY2004. The number of position in the Citywide unit has increased by 112%, from 1,547 positions to 3,279.

Changes In CPS Personnel: FY1996 to FY2004

	Schools	Citywide	Central	Total
FY1996	42,884	1,547	1,192	45,623
FY1997	42,404	1,532	1,180	45,116
FY1998	41,566	2,396	998	44,960
FY1999	41,176	2,560	991	44,727
FY2000	41,170	2,779	1,075	45,024
FY2001	41,603	3,056	1,223	45,882
FY2002	42,635	3,363	1,278	47,276
FY2003	43,045	3,019	1,325	47,389
FY2004	42,859	3,279	1,181	47,319
Change	(25)	1,732	(11)	1,696
% Change	-0.1%	112.0%	-0.9%	3.7%

Source: Chicago Public Schools Budgets

Current Fund Balance Ratio

The current fund balance ratio was devised by The Civic Federation to measure a government's ability to meet its financial obligations over time, long enough to convert illiquid assets to cash. It is calculated by dividing General Operating Fund expenditures by the *unreserved* fund balances in that fund. Historic trends are presented below for the Chicago Public Schools for FY1998 through FY2002. Ratios under 10% are categorized as "Low' while ratios between 10% and 25% are categorized as "Adequate."

Between FY1998 and FY2002, the CPS General Operating fund balance rose from $221 million to $209 million, a decline of 5%. The current fund balance ratio in FY2002 was 6%, which the Civic Federation rates as low. However, the 6% ratio falls within the Government Finance Officers Association recommendation that governments maintain an unreserved fund balance of no less than 5% to 15% of General Fund operating revenues or 1-2 months of operating expenditures.[5]

CHICAGO PUBLIC SCHOOLS CURRENT FUND BALANCE RATIO: FY97-FY01				
Fiscal Year	**Unreserved Fund Balance**	**Expenditures**	**Ratio**	**Rating**
FY1998	$ 221,997,000	$ 2,914,667,000	7.6%	Low
FY1999	$ 288,255,000	$ 3,060,728,000	9.4%	Low
FY2000	$ 393,057,000	$ 3,184,502,000	12.3%	Adequate
FY2001	$ 201,520,000	$ 3,353,119,000	6.0%	Low
FY2002	$ 209,883,000	$ 3,493,886,000	6.0%	Low

Short and Long-Term Debt Trends

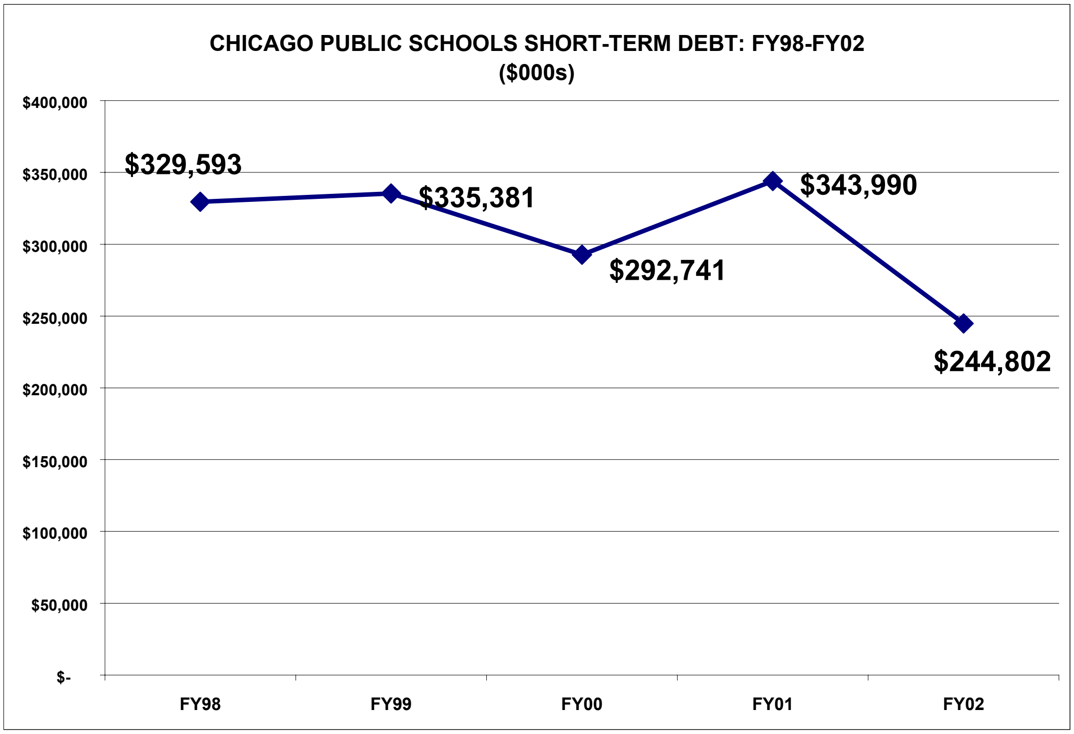
The Civic Federation has employed two measures of debt for purposes of this analysis: short-term debt trends and long-term debt per capita trends.

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. For purposes of this analysis, short-term debt in the Governmental Funds includes obligations such as accounts payable and other accrued liabilities.[6]

The exhibit below presents the Chicago Public Schools short-term debt trends for Fiscal Years 1998 through 2002. It shows that the Board of Education's short-term debt obligations fell by 26% or $84 million during the 5-year period analyzed, from $329 million to $244 million. Between FY1998 and FY2002, short-term debt fell by nearly $100 million, a substantial decrease. This decrease is a positive indicator.

[5] Government Finance Officers Association. Recommended Practice on Appropriate Level of Unreserved Fund Balance in the General Fund (2002). The CPS is a special purpose, not a general purpose government, but its size and the relative stability o its revenue stream make it prudent for the CPS to maintain adequate reserves.
[6] In order to provide consistent comparisons, long-term liabilities due within one year, which are reported in the Statement of Net Assets beginning in FY2001 as a requirement of the new GASB No. 34 reporting model, were not included in the trend analysis



Long-Term Debt Trends CPS Debt Burden Relatively High

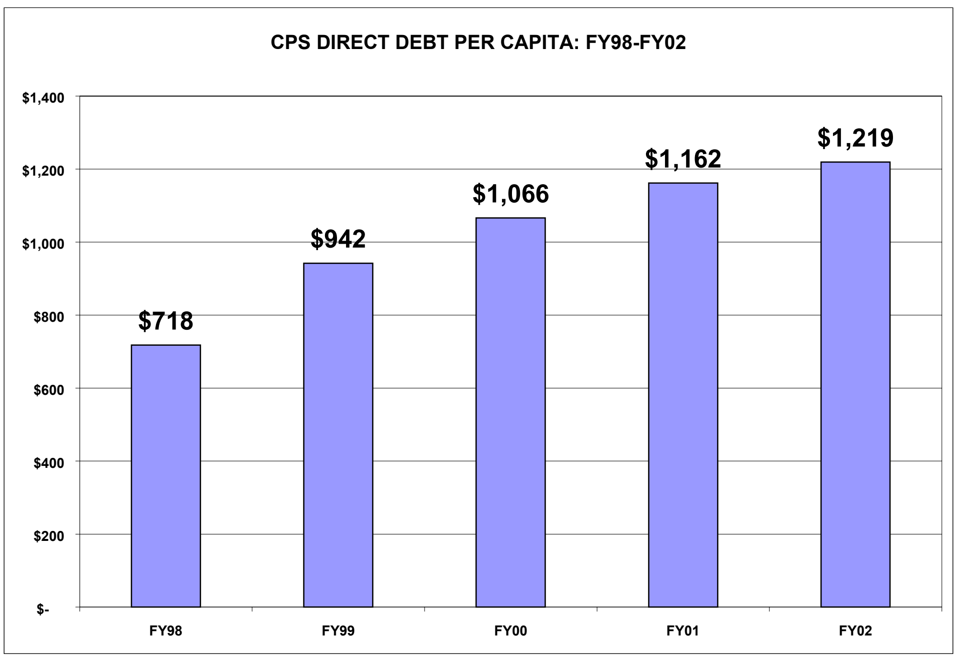
The following exhibit compares total CPS direct debt with overlapping debt reported by seven other major Cook County governments with boundaries coterminous with the Chicago School District or located partially within its boundaries. These governments are: the City of Chicago, Cook County, the Forest Preserve District of Cook County, the Metropolitan Water Reclamation District, the Chicago Park District, the City Colleges of Chicago and the School Finance Authority. Rating agencies and other financial analysts commonly monitor overlapping debt trends as an affordability indicator when governments consider debt issuance. Between FY1998 and FY2002, overlapping debt increased by 46% at the same time CPS debt rose by 75%. Total debt from all eight major governments rose by 54%. Thus, the rate of increase in Board of Education debt far outstripped increases for the other governments in the region.

CPS Direct Debt vs. Overlapping Debt: FY98-FY02
($000s)

	CPS	Overlapping	CPS + Overlapping
FY98	1,998,137	5,118,069	7,116,206
FY99	2,622,764	5,314,047	7,936,811
FY00	2,967,555	5,481,771	8,449,326
FY00	3,342,000	6,349,982	9,691,982
FY02	3,492,000	7,463,728	10,955,728
% Increase	**75%**	**46%**	**54%**

The next exhibit presents historic direct debt per capita figures. Direct debt per capita is a measure of a government's ability to maintain its current financial policies. This analysis takes the Chicago Public Schools total direct debt amount per year and divides it by population. Direct debt includes bonds, leases securing Public Building Commission bonds, asbestos abatement loans from the U.S. Environmental Protection Agency and capitalized leases. It excludes other long-term obligations such as accrued pension obligations, accrued sick pay benefits, tort liabilities and accrued workers' compensation claims. Sharp increases bear watching as a potential sign of increasing financial risk.

Direct debt per capita increased by 70% between FY1998 and FY2002, from $718 to $1219. It has increased in each of those years. During that same time period, Chicago's population rose by 4%. Much of the increase is due to the fact that the CPS has engaged on a large capital construction program over the past several years. $2 billion in additional capital improvements are planned over the next five years, although full funding has not yet been secured. The State has recently authorized school construction grants of $185 million that will be used for CPS capital projects over the next two years [7]



Moody's Investors Services notes that the CPS direct debt burden is currently above average for a large urban school district at 2.5% of the full value of real property in the District (a common benchmark used for assessing debt burden). Compared to a sample of other large urban school districts, CPS debt burden ranks higher than Houston, Minneapolis and Los Angeles, but lower than Miami-Dade.

[7] Moody's Investors Service on Chicago Board of Education, January 17, 2003

Selected Urban School District Direct Debt Burden	
Miami-Dade	2.6%
CHICAGO	**2.5%**
Houston	2.0%
Minneapolis	1.8%
Los Angeles	1.7%

Source: Moody's Investor Services

The overlapping debt burden of governments with binaries coterminous to the CPS is 7.5% of full value, reflecting large bond issues by the City of Chicago and Cook County. However, even with the above average direct burden, Moody's has assigned an A2 underlying rating for the Chicago School District's General Obligation debt while Standard & Poor's gives the CPS an A+ rating. The rating reflects the District's diverse tax base and improved financial condition due to good management and increases in state and federal funding. Moody's rates the outlook for CPS general obligation debt as stable.[8]

Teachers' Pension Fund Trends

Chicago public school teachers are enrolled in the Public School Teachers' Pension and Retirement System of Chicago. All non-teaching employees are enrolled in the City of Chicago's Municipal Employees' Annuity and Benefit Fund. The data presented below are for the Teachers' Pension Fund only.

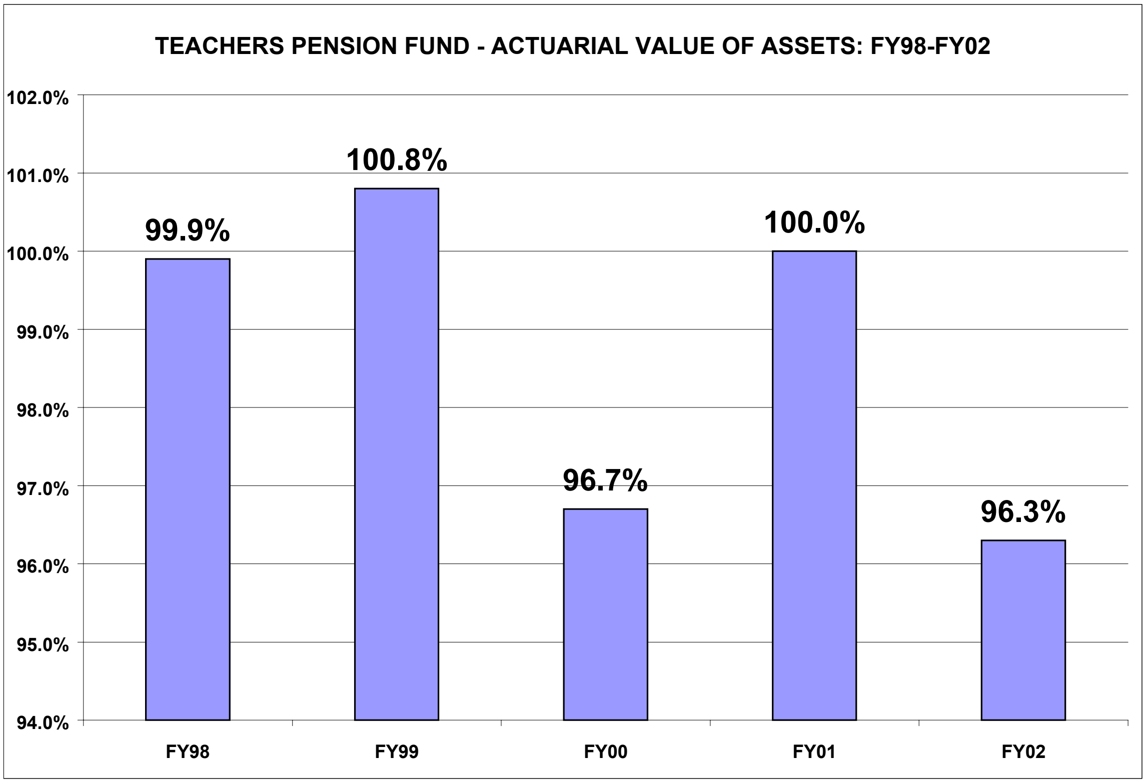
The Civic Federation used three measures to present a multi-year evaluation of the fiscal health of the Teachers' pension fund: funded ratios, the investment rate of return and the value of unfunded liabilities.

Funded Ratios – Actuarial Value of Assets

The following exhibit shows the funded ratio for the Chicago Public Schools Teachers' 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.

[8] Moody's Investors Service on Chicago Board of Education, January 17, 2003. See also Standard & Poor's. Research: Illinois School Districts Compared 2003, April 30, 2003.

The funded ratio for the Teachers' Pension Fund averaged 99% between FY1996 and FY2000. Thus, the Chicago Public Schools had more than adequate assets to cover pension liabilities in the long term during this period.



Unfunded Pension Liabilities

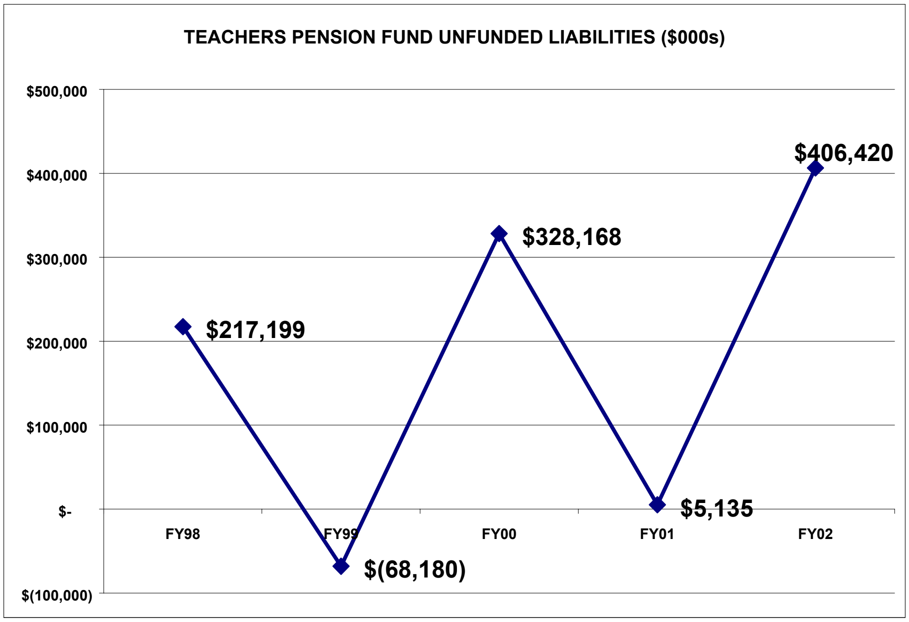
Unfunded liabilities are the dollar value of pension liabilities not covered by assets. As the exhibit below shows, unfunded liabilities for the Chicago Public Schools Teachers' pension fund totaled approximately $406 million in FY2002. This was a $401 million increase since FY2001 and an 87% increase since FY1998. This large increase in unfunded liability was due to:

- → Employer contribution being less than normal cost plus interest on the unfunded liability ($101 million)
- → Separate accounting for Health Insurance Fund ($54 million)
- → Investment Return lower than assumed ($163 million)
- → Changes in Benefits ($71 million)
- → Other Sources ($148 million)

These increases totaled approximately $537 million. $137 million was then subtracted from that figure because salary increases were lower than originally assumed and the $5 million in unfunded liability from FY2001 added in to yield a total unfunded liability of $406 million.[9]

[9] Public School Teachers' Pension and Retirement Fund of Chicago. *107th Comprehensive Annual Financial Report, June 30, 2002*, p. 71.

In FY1999, the pension fund was funded at rates above 100%. Thus, the figure shown in the exhibit for that year is negative.



Investment Rates of Return

Investment returns for the Chicago Public Schools Teachers pension fund increased by 3.5% in FY2002, reversing four years of decline due to the ongoing effects of the current recession. In FY2001, the fund experienced a negative 1.6% rate of return. Since FY1998, the Teachers Pension Fund investment rate of return has fallen from a robust 18.2% to 3.5%, an 81% drop. However, the improvement in the FY2002 is a positive sign.