DEBT SERVICE FUNDS

Debt Service Funds are used to account for the accumulation of resources for and the payment of long-term debt principal, interest, and related costs. These funds are expendable each fiscal year to handle debt-service payments. Long-term debt financing is reserved solely for funding capital projects such as school construction and renovation.

FY2009 - FY2011 Summary of Debt Service Funds
(In Millions)

	FY2009 Actual	FY2010 Budget	FY2011 Budget
Beginning-Year Fund Balance	$451.0	$426.9	$478.8
Reserved for Debt Service	(451.0)	(344.9)	(426.8)
Fund balance to be appropriated	0.0	82.0	52.0
Revenues:			
Property taxes	29.2	11.8	11.8
PPRT	55.7	55.7	53.8
State General State Aid	178.7	195.7	218.2
State CDB reimbursement	0.0	30.0	34.0
Other local (City IGA)	34.6	124.5	96.7
Federal interest subsidy	0.0	0.0	10.9
Total Revenue	298.2	417.7	425.4
Expenditures:			
Principal payments	80.3	169.3	138.5
Interest payments	213.0	325.3	330.1
Fees	7.9	5.1	8.8
Total Appropriation	301.2	499.7	477.4
Other Financing Sources/(Uses)	(21.1)	0.0	0.0
End-of-Year Fund Balance	$426.9	$344.9	$426.8

The FY2011 Proposed Budget recommends a total appropriation of $477.4 million for Debt Service Funds to pay for alternate general-obligation bonds and PBC leases, a decrease of $22.3 million from the FY2010 budget of $499.7 million. The decline is the result of the Board's efforts to minimize the debt-service costs by capitalizing interest for the bonds issued in FY2010. The Board will make every effort to issue bonds at minimum cost by choosing the most cost efficient bond structure or delaying bond issuance, if necessary. Included in the appropriation is $64.0 million for the proposed new $600.0 million bonds for FY2011 and for the delayed $400.0 million scheduled for FY2010. These are anticipated to be issued in FY2011.

(1) FUNDING SOURCES FOR DEBT SERVICE PAYMENTS

CPS uses a variety of funding sources to pay for its long-term bonds. The FY2011 debt service requires a total resource of $477.4 million. The prior-year fund balance of $52.0 million will support two bond payments: $40.0 million for PBC lease payments and $12.0 million for a QZAB payment due in January, 2011. Property tax revenues will add $11.8 million to the $40.0 million fund balance for a total debt payment of $51.8 million for the PBC bonds. PPRT of $53.8 million will partially or wholly support payments for six bonds. The City of Chicago will contribute $96.7 million from a separate property-tax levy or tax-increment financing funds for bonds issued based on the Inter-Governmental Agreements. General State Aid will supply $218.2 million for mostly alternate revenue bonds. The federal government will send an estimated $10.9 million for the interest subsidy for Build-America bonds. To reduce the debt burden on General State Aid, reimbursement of $34.0 million from the Capital Development Board will go toward the new debt-service payment in FY2011.

(2) LEGAL DEBT LIMIT AND DEBT BURDEN

As of June 30, 2010, the Board had approximately $4.6 billion of total debt principal outstanding, which consists of $4.2 billion of principal in alternate revenue bonds and $386.4 million of principal in PBC bonds. By June 30, 2010, the total principal outstanding will increase to $5.3 billion. The total debt in alternate revenue bonds will increase to $4.9 billion, while the principal balance in PBC leases will decline to $359.2 million. None of these totals includes interest payments or fees related with these bonds.

The Illinois School Code imposes a statutory limit of 13.8% on the ratio of the total outstanding property-tax-supported debt that a school district may borrow compared with a school district's equalized assessed value. Since 1996, the Board has issued alternate revenue bonds to provide funds for new school construction and renovation. Because property-tax levies are not extended to support these debt issues, the alternate revenue bonds do not count against the legal debt limit imposed by the Illinois School Code. At the end of FY2009, the Board's ratio of total outstanding property-tax-supported debt to equalized assessed value was 0.6%, well below the legal debt limit of 13.8%, and it is expected to be similar in FY2010.

As a result of these school construction and renovation projects, the Board's per capita debt burden has increased significantly in the last decade. Debt per capita is derived by dividing the total bonded debt by the population of the City of Chicago. According to the Chicago Public Schools' FY2009 Comprehensive Annual Financial Report, debt per capita in FY2000 was $712; by FY2009, debt per capita reached $1,458.

Another way of measuring the total debt burden is by dividing annual debt-service expenditures by operating-fund expenditures. Based on this method, the debt burden for FY2009 was 6.4% of operating expenditures. For FY2010, debt-service payments are estimated at 8.4% of total operating expenditures. With the proposed bond issues, the debt burden is anticipated to increase to 9.2% of operating appropriations in FY2011. The debt obligation for IGA bonds is paid for by the City of Chicago and CPS is not responsible for the federal interest subsidy for the Build America Bonds. Excluding IGA and federal interest payments, the real debt burden to CPS is 7.1% of operating budget in FY2011.

(3) TYPES OF BONDS THE BOARD HAS ISSUED

The Board is authorized by state law to issue notes and bonds and to enter into lease agreements for capital-improvement projects and cash requirements. The Board has been utilizing primarily alternate revenue bonds and PBC leases to finance its capital programs. The following is an explanation of two categories of bonds that the Board has issued:

Alternate Revenue Bonds (Unlimited Tax General Obligation Bonds): The Local Government Debt Reform Act of the State of Illinois, as amended, allows the Board to issue alternate revenue bonds or general obligation bonds payable from a dedicated revenue source subject to certain provisions. The Board is authorized to issue such bonds after adopting an authorizing resolution and satisfying certain public notice publication and petition period requirements in lieu of a voter referendum.

To support construction and renovation of school buildings, the Board has been utilizing mostly alternate revenue bond mechanisms since 1996, and most of these bonds are funded primarily from Personal Property Replacement Taxes, General State Aid revenues, or revenues related to Inter-Governmental Agreements (IGAs) with the City of Chicago.

The IGAs are unique financing arrangements between the CPS and the City of Chicago. The Agreements stipulate that the City of Chicago provides funds to the Board to pay debt service on alternate bonds issued by the Board to finance its Capital Improvement Program. Depending on the Intergovernmental Agreement, the City will provide these funds to the Board by either levying direct annual property taxes or remitting property-tax revenues from certain Tax Increment Financing (TIF) districts.

In 1997, the U.S. Congress adopted the Tax Payer Relief Act, which created Qualified Zone Academy Bonds (QZABs) to provide capital funding for schools in high-poverty areas. These bonds allow local school districts to renovate, rehabilitate, or equip certain high-poverty schools located within a school district. Since 1998, the Board has issued six series of QZABs within the meaning of Section 1397E of the Internal Revenue Code of 1986 as amended. The Chicago Public Schools does not pay interest on the bonds; rather, eligible taxpayers who own the bonds will be entitled to a credit against federal income taxes. The principal of the QZABs is payable at maturity, and the first QZAB which the Board issued in September 1998 will mature in FY2012.

The American Recovery and Reinvestment Act of 2009 (ARRA) created Qualified School Construction Bonds (QSCBs) and Build America Bonds (BABs), which are available to school districts and other governments for the first time. These bonds provide funding for new construction as well as renovation. The ARRA legislation provided that purchasers of QSCBs receive a federal income-tax credit just like QZABs. The U.S. Treasury Department establishes allocation limits and sets a tax-credit rate for QSCBs which substantially offsets the amount of interest schools would ordinarily pay on debt. In December 2009, CPS issued its 2009 QSCB allocation of $254.2 million. In 2010, the Hiring Incentives to Restore Employment (HIRE) Act was passed, which allows QSCB issuers to receive direct subsidy payments from the federal government of up to 100% of the tax-credit rate instead of offering investors a tax credit. The 2010 allocation of QSCBs is $257.1 million for the Chicago Public Schools, which the Board expects to issue in FY2011.

BABs are taxable bonds that can be used to finance a wide range of projects, including construction and modernization of school facilities. The BABs program allows municipal bond issuers in 2009 and 2010 to offer an unlimited amount of taxable debt and to elect either to receive a cash subsidy from the federal government or to provide bondholders with a tax credit. Both the payment and the tax credit would be equal to 35% of the interest paid on the bonds. In September 2009, CPS issued $518.2 million of BABs and elected to receive the direct subsidy. CPS estimates that the QSCB and BABs issued in FY2010 will save approximately $12.5 million per year or a total of $375 million in debt service over the life of the bonds compared to a traditional bond structure. CPS plans to utilize the most economical type of bonds for its issuance of bonds in FY2011.

Debt service for alternate revenue bonds in FY2011 includes the appropriation of $30.0 million for the proposed new $600.0 million bonds and for the delayed $400.0 million bonds scheduled for FY2010, and $354.7 million for existing alternate bonds such as Series 1996, 1997, 1999A, 2000A, 2000BCD, 2001A, 2001C, 2002A, 2003A, 2004A, 2004G, 2005AB, 2006B, 2007D, 2008AB, 2008C, 2009A, 2009B, 2009C, 2009D, 2009EF, 2009G, 2010AB; and swap payments related to the Series 2008AB, 2009A, 2009B, 2009C, 2010AB and a portion of the 2000C issues.

PBC Leases: The lease payments for the Public Building Commission (PBC) are for revenue bonds that the PBC sold to fund capital projects for the schools that the Board is leasing from the PBC. These are the only outstanding bonds that the Board has which rely solely on property-tax levies. The current lease payments relate to PBC bonds issued in 1992, 1993, and refunding bonds issued in 1999. To reduce the tax burden for Chicago residents, the Board has decided to abate property-tax levies required to pay for these bonds by $40.0 million and use the fund balance to pay for the difference in lease payments for FY2011. Debt service required for these PBC bonds amounts to $51.9 million for FY2011.

(4) CREDIT RATINGS AND DEBT MANAGEMENT POLICY

The Debt Management Policy of CPS provides guidance for debt management and capital planning and enhances the Board's ability to manage its debt in a conservative and prudent manner. One of the main goals of the policy is to ensure that CPS maintains the highest possible credit rating among the credit agencies. In FY2010, the credit ratings for CPS remained at AA- by Standard & Poor's. Both Fitch Ratings and Moody's Investors Service recalibrated their ratings to better align municipal and corporate ratings scales, resulting in higher ratings of AA- by Fitch Ratings and Aa2 by Moody's Investors Service. Another main goal of the policy is to stay in compliance with various rules and regulations.

As part of the Debt Management Policy, CPS is authorized to use a number of tools to manage its portfolio of debt. Some of the tools and techniques employed are: refunding of existing debt, using derivative instruments, issuing fixed or variable-rate bonds, and issuing short-term or long-term debt. These tools are used to manage various types of risks, to generate cost savings, and to exchange capital-asset planning. A copy of the Debt Management Policy is available at the Board's website at http://policy.cps.k12.us/documents/404.1.pdf. The table below lists all the outstanding debt as of June 30, 2010:

Debt Outstanding at 6/30/08 Chicago Public Schools	**Closing Date**	**Maturity Date**	**Principal Outstanding At 6/30/10**	**Pledged Funding Source for Debt Service**
PBC Series A of 1992	1/1/92	1/1/2020	$222,425,000	Property Tax
PBC Series A of 1993	4/1/93	12/1/2011	22,685,000	Property Tax
PBC Series B of 1999	3/1/99	7/1/2018	114,105,000	Property Tax
Unlimited Tax G.O. Series 1996	4/25/96	12/1/2012	35,575,000	PPRT
Unlimited Tax G.O. Series 1997	5/7/97	12/1/2012	39,245,000	PPRT
Unlimited Tax G.O. Series 1997A*	12/3/97	12/1/2030	37,985,204	1997 IGA / PPRT
Qualified Zone Academy Bond	9/24/98	9/23/2011	14,000,000	1997 IGA
Unlimited Tax G.O. Series 1998B-1*	10/28/98	12/1/2031	310,889,321	1997 IGA / PPRT
Unlimited Tax G.O. Series 1999A*	2/25/99	12/1/2031	504,686,912	1997 IGA / PPRT
QZAB IDFA 1999A	12/22/99	12/21/2011	12,000,000	State Aid
Unlimited Tax G.O. Series 2000A	7/20/00	12/1/2021	14,160,000	State Aid
Unlimited Tax G.O. Series 2000BC D	9/7/00	3/1/2032	299,400,000	State Aid
QZAB Series 2000E	12/19/00	12/18/2013	13,390,000	State Aid
Unlimited Tax G.O. Series 2001A	3/1/01	12/1/2012	2,990,000	State Aid
QZAB Series 2001B	10/24/01	10/23/2015	9,440,000	State Aid
Unlimited Tax G.O. Series 2001C	12/11/01	12/1/2012	15,075,000	State Aid
Unlimited Tax G.O. Series 2002A	9/24/02	12/1/2022	44,365,000	IGA - TIF
Unlimited Tax G.O. Series 2003A	2/13/03	12/1/2016	47,945,000	State Aid
QZAB Series 2003C	10/28/03	10/27/2017	4,585,000	State Aid
Unlimited Tax G.O. Refunding, Series 2004A	4/6/04	12/1/2020	205,410,000	PPRT / State Aid
Unlimited Tax G.O. Series 2004G	12/1/04	12/1/2022	12,500,000	IGA - TIF
Unlimited Tax G.O. Series 2005AB	6/27/05	12/1/2032	246,180,000	PPRT / State Aid
QZAB Series 2006A	6/7/06	6/1/2021	6,852,800	State Aid
Unlimited Tax G.O. Series 2006B	9/27/06	12/1/2036	340,975,000	State Aid
Unlimited Tax G.O. Series 2007BC	9/4/07	12/1/2024	204,035,000	1997 IGA / PPRT
Unlimited Tax G.O. Series 2007D	12/13/07	12/1/2029	226,190,000	State Aid
Unlimited Tax G.O. Series 2008A	5/13/08	12/1/2030	262,785,000	1997 IGA / PPRT
Unlimited Tax G.O. Series 2008B	5/13/08	3/1/2034	231,050,000	State Aid
Unlimited Tax G.O. Series 2008C	5/1/08	12/1/2032	464,655,000	State Aid
Unlimited Tax G.O. Series 2009A	3/18/09	3/1/2026	130,000,000	State Aid
Unlimited Tax G.O. Series 2009BC	6/25/09	3/1/2031	89,225,000	State Aid
Unlimited Tax G.O. Series 2009D	7/29/09	12/1/2022	71,380,000	State Aid
Unlimited Tax G.O. BAB Series 2009E	9/24/09	12/1/2039	518,210,000	State Aid / Federal Subsidy
Unlimited Tax G.O. Series 2009F	9/24/09	12/1/2016	29,125,000	State Aid / Federal Subsidy

Debt Outstanding at 6/30/08 Chicago Public Schools	Closing Date	Maturity Date	Principal Outstanding At 6/30/10	Pledged Funding Source for Debt Service
QSCB Series 2009G	12/17/09	12/15/2025	254,240,000	State Aid
Unlimited Tax G.O. Series 2010A	2/17/10	3/1/2035	48,910,000	State Aid
Unlimited Tax G.O. Series 2010B	2/17/10	3/1/2036	157,055,000	State Aid
Total Principal Outstanding			**5,263,724,237**	