City of Chicago

Annual Financial Analysis 2013

Mayor Rahm Emanuel

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Letter from the Mayor

Fellow Chicagoans,

Thank you for your interest in the City of Chicago's 2013 Annual Financial Analysis. This document presents an overview of the City's revenues and expenditures, as well as other areas that impact the overall financial state of the City.

Over the last two years we have worked diligently to implement lasting structural reforms that have cut our annual budget deficit in half while improving both the quality and efficiency of City services. The decreasing size of the deficit is the result of reforms such as the introduction of managed competitions to guarantee the best price for the highest quality City services, the transition to grid garbage collection, the review and renegotiation of major contractual costs, and the implementation of a wellness program for City employees and other reforms that have reduced the City's healthcare costs. Meanwhile, an equally important part of our financial plan is maintaining and strengthening our reserves. Over the last two years, we have added resources to our rainy day fund as a commitment to our long-term financial health.

These reforms, however, can only get us so far. Until we pass meaningful pension reform in Springfield, the outlook for future years is unsustainable. As outlined in this report, the need for action is immediate so that we can continue to make the critical investments we need today while building the economic foundation for tomorrow.

Publishing this report provides Chicagoans with access to the information they need to evaluate the City's financial performance and participate in the citywide discussions that will inform the 2014 budget. I welcome the opportunity to engage with Chicagoans in a collaborative process through which we can create a budget that reflects our values: a commitment to new jobs and growing opportunity, delivering the City services that taxpayers deserve, a public safety system that provides all residents across the city with a real sense of security, and ensuring that Chicago continues to be a great place to live, work, and raise a family.

Rahm Emanuel

Rahm Emanuel
Mayor

Annual Financial Analysis
2013

Introduction

Executive Summary

Executive Order No. 2011-7 directs the City of Chicago's Office of Budget and Management to issue, each year, a long-term financial analysis that provides a framework for the development of the City's annual budget and guides the City's financial and operational decisions.

The City's Annual Financial Analysis is completed based on the critical understanding that to protect the health and safety of all Chicagoans, strengthen communities and neighborhoods, maintain infrastructure and public spaces, and foster a vibrant local economy, the City must be in strong financial health. The only way to secure and maintain the fiscal health of the City is to plan for the future with a clear view of the past.

This Annual Financial Analysis takes an informed and long-term approach to financial planning, evaluating the City's past revenues, expenditures, policies, and programs in light of conditions driving the broader economy and other factors impacting the City's future finances.

The history and future of each major component of the City's overall finances, as outlined below, are discussed in detail in the following pages. The City's current fiscal outlook shows both the progress that has been made towards bringing operating expenses in line with revenues, and the continuing pressure placed on City finances by growing wages and long-term obligations such as pension payments. The projected corporate fund budget gap for 2014 is $338.7 million. This is expected to grow to $1.16 billion by 2016, due in large part to ballooning obligations under current pension legislation.

This Annual Financial Analysis is divided into the following sections:

- **Financial History Review.** This section describes the revenue sources of the City's corporate fund, property tax levy, special revenue funds, and enterprise funds and the ways in which this revenue has been spent over the past 10 years. This section pays particular attention to how the City's sources of revenue have fluctuated with the economy, and to those expenses that make up the bulk of the City's operating budget, such as salaries and wages, employee benefits, and contractual services.
- **Three-Year Financial Forecast.** This section provides projected revenues and expenditures for 2014 and discusses the anticipated corporate fund budget gap, which is currently estimated at $339 million. While progress has been made in the past two budgets, this continuing structural deficit highlights the fact that there is still work to be done and difficult decisions to be made. This section also examines three different scenarios for 2015 and 2016 – a 'current outlook', a 'positive outlook', and a 'negative outlook' – each presenting a forecast based on potential future revenues and expenditures and outlining the impact of future debt and pension obligations on City finances.
- **Long-Term Asset Lease and Reserve Funds.** This section describes the manner in which funds generated by the City's long-term lease of the Skyway and the parking meter system have been spent and the City's historic and present levels of reserve funds. Since 2012, only interest earned on reserve funds has been transferred into the City's corporate fund and additional deposits have been made into these reserves.
- **Capital Investments.** This section describes the City's capital improvement program, details the City's capital uses of its bond proceeds over the past 10 years, and summarizes the City's capital improvement plan for the next five years.
- **TIF.** This section details revenues from the City's tax increment financing program and the manner in which those funds have been spent over the past 10 years. It also looks forward at projected TIF revenues and programming for the coming years.
- **Debt.** This section examines the City's total outstanding debt, including general obligation bonds, revenue bonds, and short-term debt instruments. It also outlines the City's debt service payments over the past 10 years and the coming three years.
- **Pensions.** This section provides an in-depth discussion of the pension system, the growing unfunded liabilities of the City's four pension funds, and the resulting impact on City finances.

Primer on City Finances

City Fund Structure

The City organizes its budget by funds, each of which is accounted for separately, with its own sources of revenue and types of expenditures:

- **Corporate Fund.** The corporate fund is the City's general operating fund and supports many essential City services and activities, such as police and fire protection, emergency management, trash collection, and public health programs. Corporate fund revenues come primarily from a variety of local and intergovernmental taxes, fees, and fines.
- **Special Revenue Funds.** The City's special revenue funds are used to account for revenue from specific sources that by law are designated to finance particular functions, such as road repair, snow removal, the library system, and special events and tourism promotion.
- **Enterprise Funds.** The City's enterprise funds include the water fund, the sewer fund, and a separate fund for each of the City's major airports. These funds are self-supporting, in that each fund derives its revenue from charges and associated user fees.
- **Grant Funds.** Grant funding, largely from the state and federal governments, makes up a significant and recurring source of revenue for the City and is utilized to provide a range of City services, from community development and youth services to infrastructure improvement.
- **Property Tax Funds.** The City receives property tax revenue through its levy and through its TIF program. The City uses revenue from its property tax levy to pay its employee pension contributions and debt service obligations, as well as to fund the library system. TIF revenue is utilized for projects in designated TIF districts.
- **Capital Funds.** Capital improvements to the City's infrastructure and facilities are funded largely with the proceeds of bond issuances and state and federal grant funds.
- **Reserve Funds.** Reserve funds, such as those established in connection with the long-term lease of City assets, function as an economic safety net to mitigate current and future risks such as unexpected contingencies, emergencies, or revenue shortfalls. These funds are not included in the City's annual operating budget.

Annual Financial Analysis 2013

Financial History Review

The revenue and expenditure information contained herein is based on the City's audited Consolidated Annual Financial Report (CAFR) and the audited Basic Financial Statements for the City's enterprise funds. The revenue and expenditure information presented herein may vary slightly from that printed in the City's CAFR due to accounting adjustments made over time.

Corporate Fund Revenue

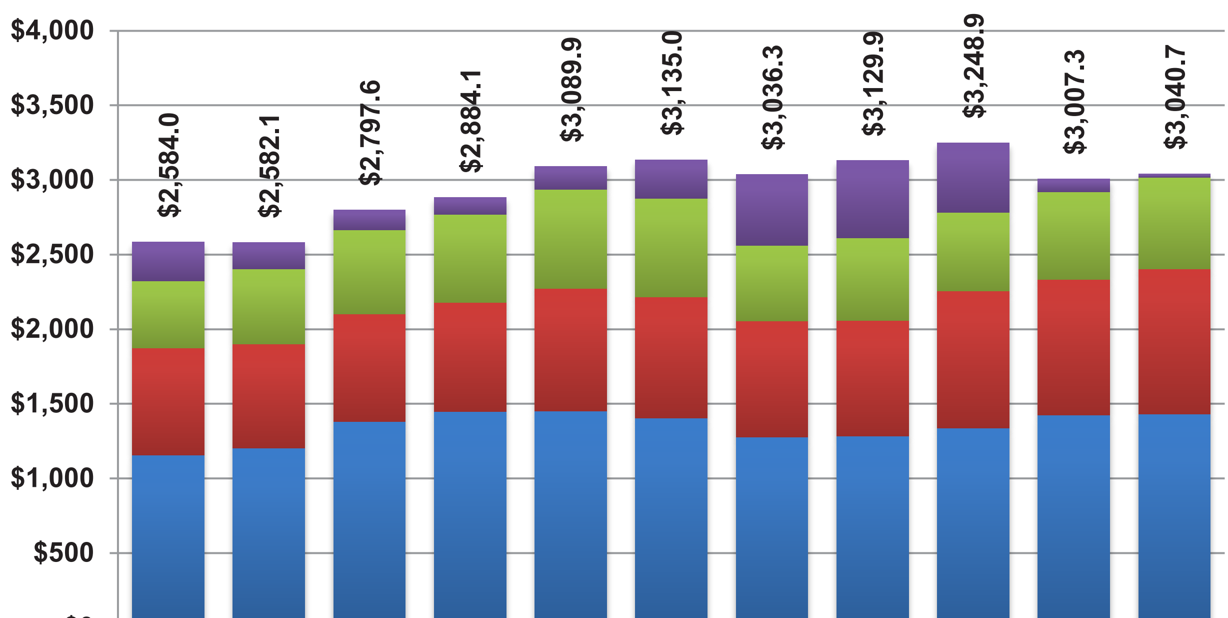
This section discusses the overall trends in the sources of corporate fund revenue and the City's relative reliance on each over the course of the past 10 years. Corporate fund revenues come from four main sources:

- Local tax revenue, which consists of taxes collected by the City, including utility, transaction, transportation, recreation, and business taxes.
- Intergovernmental tax revenue, which consists of the City's share of the Illinois state sales and use taxes, income tax, and personal property replacement tax.
- Non-tax revenue, which consists of charges for licenses, permits, and services; fees and fines; the proceeds from land and material sales and leases; and transfers to the corporate fund from the City's special revenue and enterprise funds for services provided to those funds.
- Proceeds and transfers in, which consist of amounts transferred into the corporate fund from outside sources, including proceeds from financings and transfers from the City's asset lease reserve funds.

Over the past 10 years, total corporate fund revenues experienced relatively steady growth with the exception of a decrease following the financial crisis and economic downturn in 2008. What is more telling than the aggregate amount of corporate fund revenue, however, are the differences in the sources of this revenue over the years. The relative amounts coming from taxes, non-tax revenues, and various outside sources differ each year, and changed significantly with the onset of the recession in 2008. Recurring and economically sensitive sources of revenue shrank as a percentage of overall revenues, while the City subsidized its corporate fund budget with transfers from non-recurring sources of revenue such as funds from the long-term lease of the Skyway and the parking meter system and proceeds from financing transactions.

TOTAL CORPORATE FUND REVENUE BY SOURCE[1]

$ Millions



	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013 YE Est
Proceeds & Transfers In	261.8	180.1	133.3	115.1	154.5	259.3	474.6	519.0	467.6	86.6	22.4
Intergovernmental Taxes	449.2	501.8	563.2	592.2	662.7	659.3	508.6	553.8	525.2	587.6	616.9
Non-Tax Revenue	717.0	698.2	722.5	730.0	822.6	814.0	777.8	773.3	921.1	907.8	970.2
Local Taxes	1,156.0	1,202.0	1,378.6	1,446.8	1,450.1	1,402.4	1,275.3	1,283.8	1,335.0	1,425.3	1,431.2
Total	2,584.0	2,582.1	2,797.6	2,884.1	3,089.9	3,135.0	3,036.3	3,129.9	3,248.9	3,007.3	3,040.7

[1]Data does not include fund balance.

Financial History Review

Between 2003 and 2007, an average of 67 percent of total corporate fund revenues were derived from local and intergovernmental tax revenues. Beginning in 2008, these revenues began to decline both in dollar amount and as a percentage of total revenues, decreasing to 59 percent in 2009. By 2011, local and intergovernmental taxes made up only 57 percent of total corporate fund revenues.

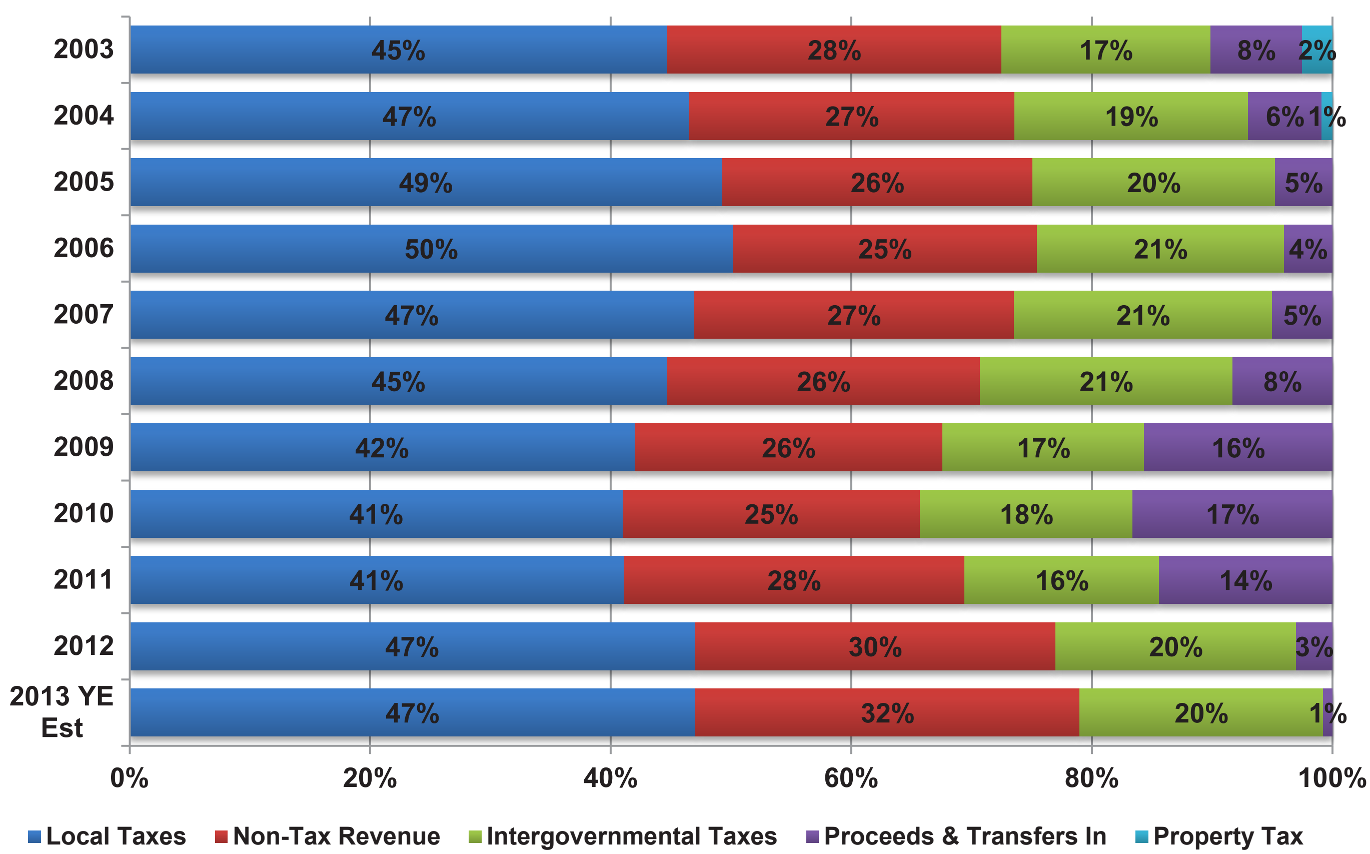
As these economically-sensitive revenues declined, the City did not decrease expenditures to match these shrinking revenues, but instead increasingly utilized transfers into the corporate fund from outside sources. Between 2003 and 2007, such transfers constituted an average of 6 percent of corporate fund revenues each year and came largely from investment income on general obligation bond proceeds and other financing transactions. In 2005, the City began to use proceeds from the long-term lease of the Skyway to supplement its operating budget, and in 2008 proceeds from the long-term lease of the parking meter system also began to subsidize the operating budget. In the period from 2009 through 2011, an average of $487 million each year, or 16 percent of corporate fund revenues, came from such one-time resources.

The 2012 budget began the process of aligning expenditures with real revenues through efficiencies, targeted cuts, and select revenue enhancements. In 2012, 67 percent of corporate fund revenues came from local and intergovernmental taxes, 30 percent from recurring non-tax revenues, and only 3 percent from other proceeds and transfers into the fund. Due to new reforms, the lasting effects of changes made in 2012, and continued economic growth, it is anticipated that the relative proportion of recurring revenues to the corporate fund will continue to increase in 2013.

Following is a more detailed discussion of the individual revenue sources that make up the major categories of corporate fund revenue discussed above and how each has performed over the course of the last decade and is expected to end the current year.

CORPORATE FUND REVENUES

as a percentage of total corporate fund revenue



Financial History Review

Local Tax Revenue

Local taxes include taxes on the purchase of utility services, real estate and other transactions, fuel and garage parking, and certain recreation and business activities.

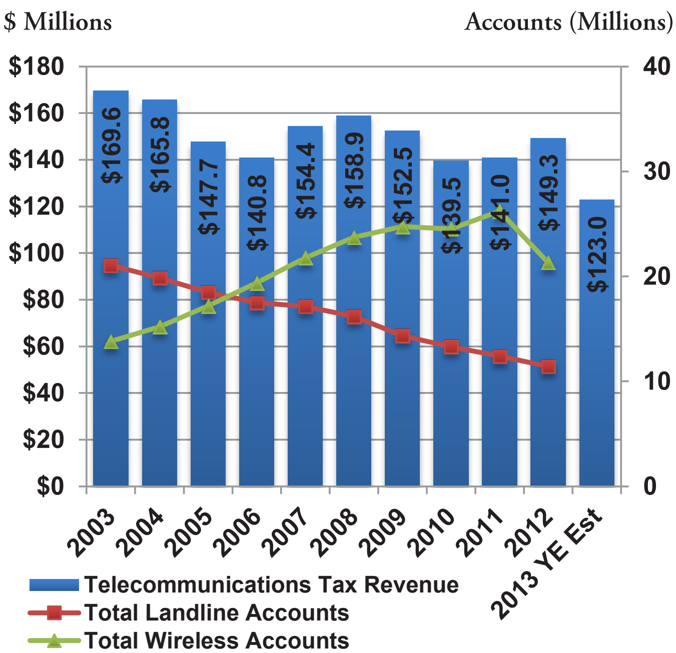
Public Utility Taxes

Public utility taxes consist of taxes on the purchase of telecommunications services, electricity, natural gas, and cable television. These combined taxes have constituted 14 percent to 18 percent of total corporate fund revenues over the past 10 years. In 2003, public utility taxes generated $467.7 million, accounting for 18 percent of total corporate fund revenues. In 2008, these taxes peaked at $524.8 million, dropping to $462.5 million in 2012. The 2013 year-end estimate for total public utility tax revenue is $454.8 million. The reasons for these fluctuations are discussed below with respect to each individual tax.

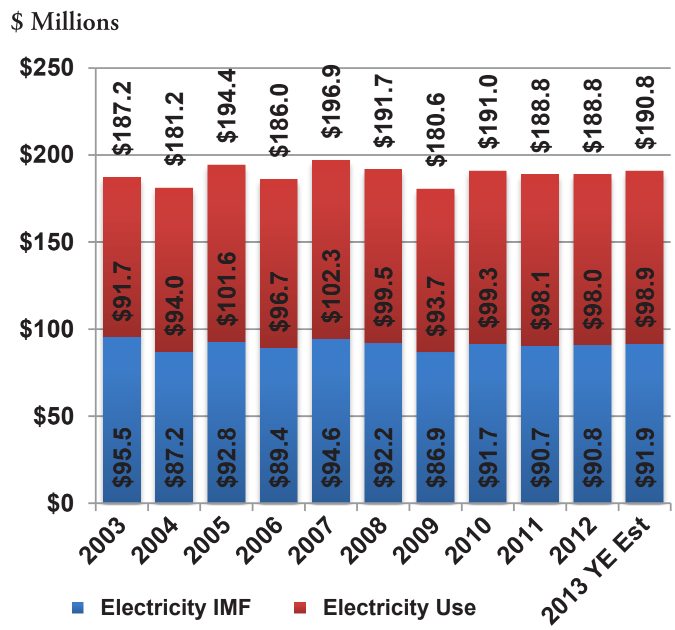
Revenue from **telecommunications taxes**, which are levied on charges for telephone services in the city, has declined over the past decade, reflecting trends in the industry and consumer preferences. In 2003, telecommunications taxes generated $169.6 million, accounting for 7 percent of total corporate fund revenues. Through 2005, landlines generated the majority of this revenue stream, with cell phone usage taking over as the larger driver of this revenue source in 2006. By 2012, telecommunications tax revenue had dropped to $149.3 million, accounting for 5 percent of total corporate fund revenues. The overall decline in revenues is due in part to the continuing reduction in the use of landlines as more customers choose to have only wireless services or use online communication services such as Skype. In addition, federal law exempts most wireless data services, such as mobile broadband, from taxation, and consequently, growth in the market for such wireless services has not resulted in increased telecommunications tax revenues for the City. Telecommunications taxes are expected to yield $123.0 million in 2013, with a portion of the decline from 2012 levels due to credits being paid to certain telecom service providers for taxes charged on services that were later determined to be non-taxable under the federal Internet Freedom Act.

The City's **electricity use tax** and **electricity infrastructure maintenance fee** are charged based on the number of kilowatt hours of electricity used. Revenues from electricity taxes are highly dependent upon weather conditions, particularly summer temperatures, because electricity is used to cool homes and buildings. Electricity rates, conservation efforts, and technological changes that contribute to energy efficiency also affect the amount of electricity used and thus City revenue from these taxes. Electricity tax revenues have constituted 6 to 8 percent of total corporate fund revenues

TELECOMMUNICATIONS TAX REVENUE

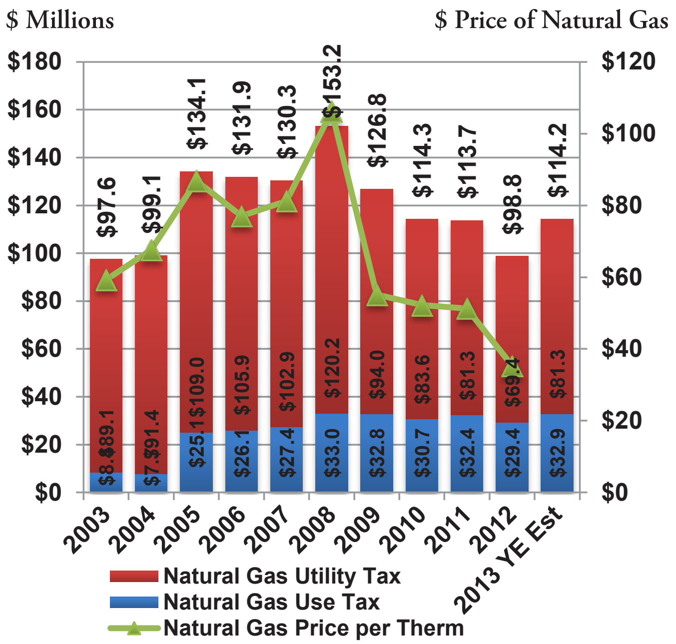


ELECTRICITY TAX REVENUE



Financial History Review

NATURAL GAS TAX REVENUE



over the past 10 years, averaging $188.7 million each year. In 2003, electricity taxes generated $187.2 million, accounting for 8 percent of total corporate fund revenues. In 2012, electricity taxes generated $188.8 million, accounting for 6 percent of total corporate fund revenues. The increasing use of energy-efficient equipment has affected this revenue stream in recent years and is expected to continue to impact the growth of these revenues going forward, with 2013 year-end estimates at $190.8 million.

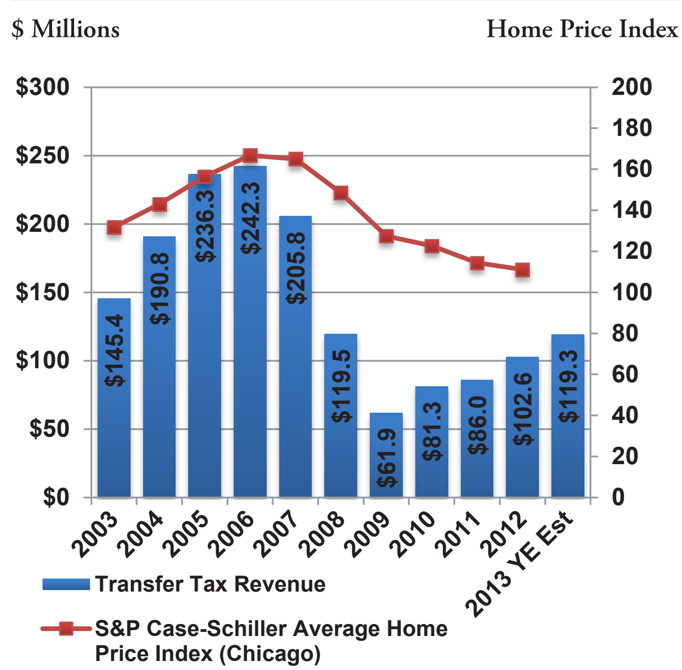
The City imposes two natural gas-related taxes. The **natural gas utility tax** is an 8 percent tax imposed on the purchase price of natural gas. The **natural gas use tax** is imposed at a rate of 6.3 cents per therm on entities not subject to the natural gas utility tax. As with electricity taxes, natural gas tax collections are highly dependent upon weather conditions and price. Natural gas is used to heat homes and buildings, and thus colder weather increases consumption and associated tax revenues. In 2003, natural gas-related taxes generated $97.6 million, accounting for 3 percent of total corporate fund revenues. Natural gas prices during 2008 were historically high, averaging 106.2 cents per therm, and City revenues from related taxes spiked to $153.2 million in that year. Prices dropped to an average of 55.1 cents per therm during 2009 and then to an average of 35.3 cents per therm in 2012. In 2012, natural gas taxes generated $98.8 million, accounting for 3 percent of total corporate fund revenues. Prices have begun to rebound from the steep drop seen in recent years, with natural gas prices up 30 percent over 2012 during the first half of 2013. Rising prices, together with a colder winter than 2012 contributing to increased usage, are expected to result in increased natural gas tax revenues in 2013.

Cable television tax revenue, which makes up only a small portion of corporate fund revenue, grew from $13.3 million in 2003 to $25.5 million in 2012, with 2013 year-end estimates at $26.8 million. Steady growth is expected to continue for this revenue source due in part to industry growth, including the rise of on-demand and pay-per-view channels.

Transaction Taxes

Transaction taxes include taxes on the transfer of real estate, the lease or rental of personal property, and the short-term lease of motor vehicles within the city. Combined transaction taxes have constituted 6 to 12 percent of total corporate fund revenues over the past 10 years. Fluctuations in these revenue sources track closely with the economy and the real estate market. The 2013 year-end estimate for total transaction tax revenue is $263.1 million, or 9 percent of corporate fund revenues for the year.

REAL PROPERTY TRANSFER TAX REVENUE

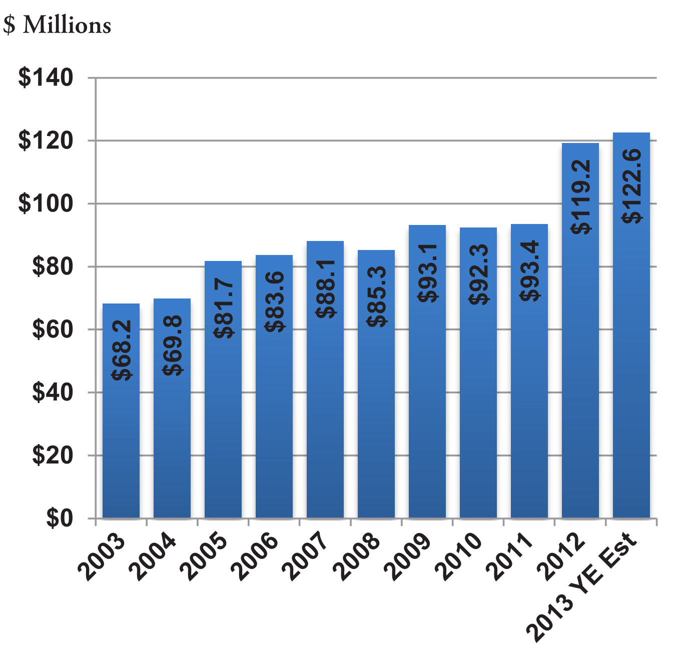


Financial History Review

In the years leading up to the recession, **real property transfer tax** collections reached record levels, increasing from $145.4 million in 2003 to peak at $242.3 million in 2006. The decline in the real estate market drove these collections down to $61.9 million in 2009. 2010 and 2011 saw slight increases in real property transfer tax revenue to $81.3 million and $86.0 million, respectively, due in large part to increased commercial real estate activity. The residential real estate market, however, was slower to recover and just began to show sustained growth in 2012. Home sales in 2012 were up by 23 percent from 2011, bringing overall real property transfer tax revenues to $102.6 million last year. During the first six months of 2013, existing home sales continued to grow, up 21 percent over 2012, and home prices also started to recover, with home prices up 15 percent over 2012. The recovering housing market, in combination with continued commercial real estate activity, is expected to drive real property transfer tax revenues up again in 2013 to an anticipated $119.3 million.

As with other transaction tax revenues, collections of **personal property lease transaction taxes**, imposed on the lease or rental of personal property at a rate of 8 percent of the lease or rental price, suffered due to the recession's impact on personal and business consumption, experiencing only slow overall growth over the past decade. In 2003, taxes on the lease or rental of personal property generated $90.8 million, accounting for 4 percent of total corporate fund revenues. In 2008, there was an increase in the tax rate from 6 to 8 percent and personal property lease transaction taxes generated $119.3 million. These revenues dropped to $108.4 million in 2010 but increased again in 2011 to $123.5 million due largely to enforcement collections. Growth continued into 2012 with revenues at $132.5 million, accounting for 4 percent of total corporate fund revenues. 2013 year-end estimates for this revenue source are at $137.7 million, anticipating steady growth in line with increasing consumer confidence and continued enforcement efforts.

GARAGE TAX REVENUE



Transportation Taxes

Transportation taxes include taxes on garage parking, vehicle fuel, and hired ground transportation. Total transportation tax revenues grew from $136.6 million, or 5 percent of total corporate fund revenues, in 2003 to $177.9 million, or 6 percent of total corporate fund revenues, in 2012, and is expected to finish 2013 at $180.7 million.

Garage taxes have consistently made up the largest portion of this category. Rate adjustments in 2005, 2009, and 2012 contributed to greater revenue growth in those years, with an overall increase from $68.2 million in 2003 to $119.2 million in 2012. The City changed this tax from a tiered rate structure to a percentage-based rate effective July 1, 2013. The change is expected to be revenue neutral for the City, as the effective tax rate for economy parking was cut while the rate for premium garages and valet services increased. The impact on the price of garage parking will depend on whether garage operators chose to pass on the savings or increases to parkers, as the tax is levied on the operators. The City anticipates $122.6 million in garage tax revenues in 2013.

Vehicle fuel tax revenues declined from $60.0 million in 2003 to $49.8 million in 2012, due largely to declines in fuel consumption as gasoline prices rose and fuel-efficient vehicles became more prevalent. Vehicle fuel tax revenues are expected to hold approximately even with 2012 levels in 2013.

Recreation Taxes

Recreation taxes include taxes on amusement activities and devices, the mooring of boats, liquor, cigarettes, non-alcoholic beverages, and off-track betting. In 2003, recreation taxes generated $85.9 million for the City, accounting for 3 percent of total corporate fund revenues. By 2012, this had grown to $163.2 million, accounting for 5 percent of total corporate fund revenues. The City anticipates that overall recreation tax revenue will increase to $163.4 million in 2013.

Amusement taxes apply to most large sporting events, theater, and musical performances in the city, and generated $37.6 million in 2003, growing to $87.8 million in 2012. The overall increase in these revenues was due in part to 1 percent rate increases in each of 2005 and 2009. Amusement tax revenues also vary significantly from year to year based on the relative success of Chicago's professional sports teams and ticket prices for such sporting events. The City anticipates $88.6 million in amusement tax revenue in 2013, with decreases in both ticket sales and prices by the Cubs and Sox being offset by playoff appearances by the Bulls and Blackhawks.

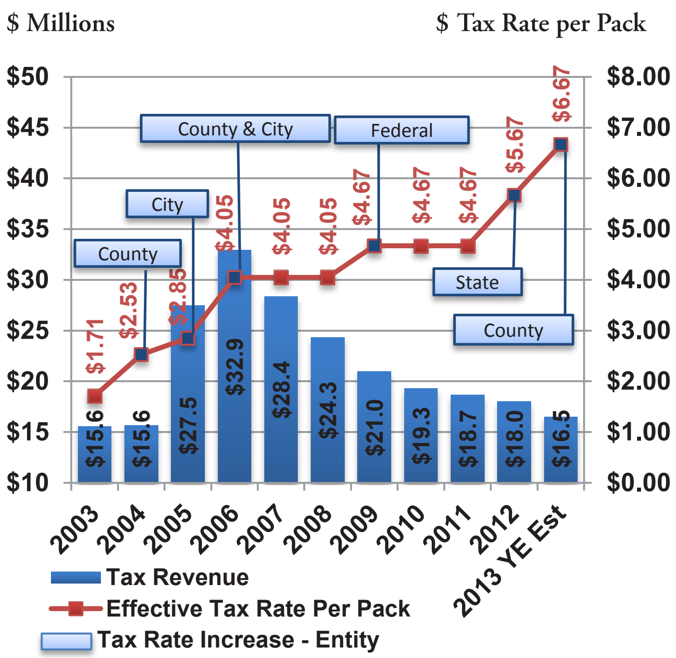
Cigarette tax revenues increased from $15.6 million to $32.9 million between 2004 and 2006, due largely to increases in the City cigarette tax rate in 2005 and 2006, but have fallen steadily since that time to $18.0 million in 2012. These declines can be attributed in part to a decline in smoking in the overall population and in part to increases in prices and tax rates discouraging purchases of cigarettes in the city. The continuing impact of these factors, as well as the potential impact of a proposed increase in the federal tax rate, is expected to result in a further decrease in these revenues to $16.5 million in 2013.

Liquor tax revenue, in contrast, has increased significantly over the past 10 years, from $18.4 million in 2003 to $32.6 million in 2012 and an anticipated $33.0 million in 2013, due to increases in both activity and the tax rate. Revenue from taxes on the purchase of **non-alcoholic beverages** saw slight year-over-year increases for most of the past decade, with a significant jump from $11.5 million in 2007 to $18.8 million in 2008, with the addition of the tax on bottled water. The 2013 year-end estimate for non-alcoholic beverage tax revenue is $22.7 million.

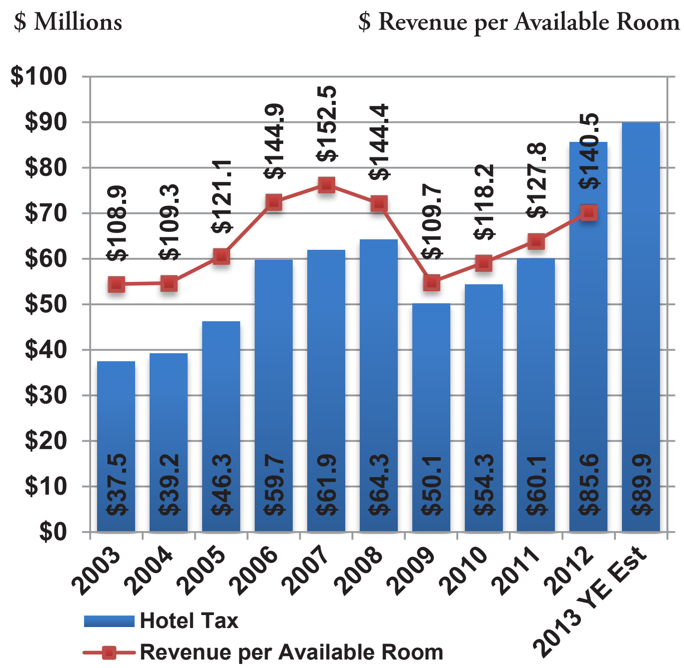
Business Taxes

Business taxes consist of taxes on hotel accommodations and the employers' expense tax. After high growth years in the mid-2000s, these taxes peaked at $92.3 million in 2008 and then decreased by 14 percent to $79.6 million in 2009. In 2010 and 2011, business tax revenues grew slightly but did not return to pre-recession levels. Current business tax revenues show the effect of the phasing out of the employers' expense tax and the increase in the hotel accommodations tax rate, both of which were effective as of 2012.

CIGARETTE TAX REVENUE AND RATE INCREASES



HOTEL ACCOMMODATIONS TAX REVENUE



Revenues from the **hotel accommodations tax** experienced a sharp decline in 2009 and remained low into early 2011, coinciding with the recession's impact on tourism, business for general merchandise purchases in Chicago travel, and convention attendance. In 2007, the revenue per available room, a key metric that accounts for both occupancy and room price, averaged $152.5, and hotel tax revenues were $61.9 million. By 2009, revenue per available room had declined by 28 percent to $109.7, and hotel tax revenues dropped by 19 percent to $50.1 million. The second half of 2011, however, saw hotel sales and related tax revenues begin to bounce back, and strong growth continued into 2012 with average revenue per available room at $140.5 for the year. Hotel tax revenues finished 2012 at $85.6 million, reflecting both the continued climb in local hotel sales and the increase in the hotel accommodations tax rate from 3.5 percent to 4.5 percent. With occupancy up 2 percent and revenue per available room up 7 percent over 2012 during the first half of the year, the City anticipates hotel tax revenues of $89.9 million in 2013, accounting for 3 percent of total corporate fund revenues.

As part of the 2012 budget and as a key component of encouraging business development and job creation in Chicago, the Mayor delivered on his campaign pledge to phase out the **employers' expense tax**. This tax, which had historically been levied on businesses with more than 50 employees at a rate of $4 per employee per month, generated an average of $23.4 million per year between 2003 and 2011. This tax was reduced by 50 percent, to $2 per employee, in 2012. Revenue declined accordingly, to $17.9 million in 2012 and an anticipated $11.4 million in 2013. The tax will be completely eliminated at the end of 2013.

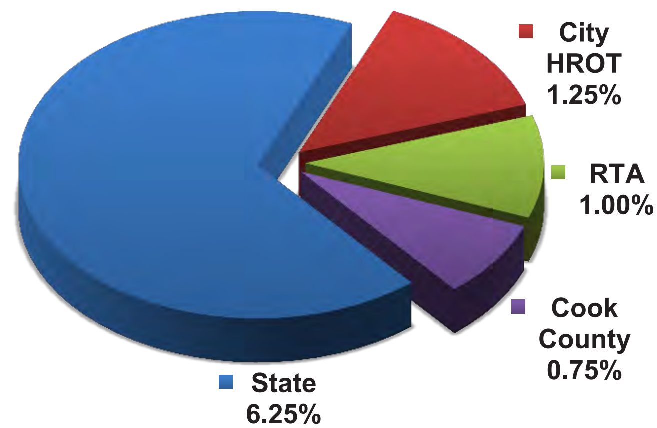
Intergovernmental Tax Revenue

Intergovernmental tax revenues consist of the City's share of the Illinois state sales and use taxes, income tax, and personal property replacement tax.

Sales and Use Taxes

The City's sales and use tax revenue is generated through the Chicago Home Rule Occupation and Use Tax (HROT) and the Municipal Retailer Occupation and Use Tax (MROT). The City imposes the HROT at a rate of 1.25 percent on the retail sale of general merchandise, excluding most sales of food and medicine. The HROT also applies to property

COMPOSITION OF TOTAL SALES TAX RATE



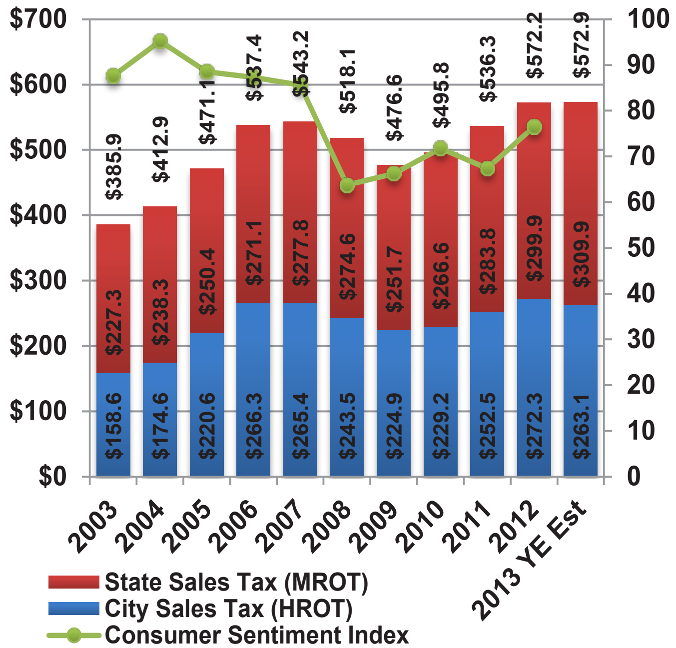
purchased for use in the City from a vendor located outside the City at a rate of 1.25 percent for titled personal property and at a rate of 1 percent for non-titled personal property. Unlike the HROT, the 1 percent MROT, which is imposed by the State on behalf of municipalities and included in the 6.25 percent State rate shown in the chart above, applies to qualifying food and drug purchases.

General merchandise purchases in the City are subject to a combined sales tax rate that includes, in addition to the City HROT and the State rate, a Regional Transportation Authority (RTA) and Cook County sales tax. The total combined rate was 9.75 percent from July of 2010 through the end of 2011 but was reduced to 9.25 percent as of January 1, 2013, when the County rolled back its portion of the 2010 sales tax increase.

Revenue from the HROT and MROT have accounted for an average of approximately 17 percent of total corporate fund revenues over the past 10 years. From 2004 to 2007, HROT and MROT collections grew an average of 9 percent per year, peaking at $543.2 million in 2007. Beginning in the fall of 2008, sales tax receipts began a year-over-year average decline of 8.9 percent each month for the next 17 months, with 2009 revenues at only $476.6 million. During 2010, a small growth trend emerged due largely to the State's tax amnesty program, but it was not until 2012 that revenues reached pre-recession levels again, finishing the year at $572.2 million. Moderate growth is expected to continue into 2013 as retail sales numbers continue to improve; however, the amount of sales tax revenue flowing into the corporate fund is expected to remain approximately

SALES TAX REVENUE

$ Millions Consumer Sentiment Index



even with 2012 levels at $572.9 million, as an increasing proportion of the City's gross sales tax revenue is used to pay debt service on sales tax bonds issued to fund capital projects.

State Income Tax

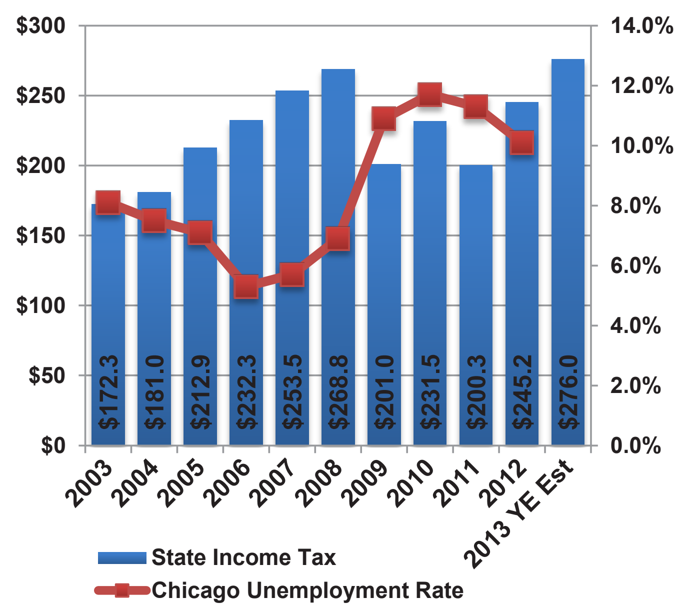
Like sales and use taxes, state income tax revenues experienced growth in pre-recession years and then declined with the economy in the years following 2007. From 2004 to 2007, City income tax revenues grew an average of 10 percent per year, reaching $268.8 million in 2008. Income tax revenue dropped 25 percent to $201.0 million in 2009, rebounded slightly in 2010 to $231.5 million, but then dropped again in 2011 due to a combination of factors, including continued high unemployment rates, the decline in population under the 2010 Census, the federal 'depreciation bonus rule', and a delay in state distributions, all discussed in greater detail below.[2]

In 2011, the city's unemployment rate peaked at 11.3 percent, depressing income tax revenues. At the same time, income tax distributions to the City from the State were adjusted to account for the population count from the 2010 Census. Chicago's decline in population resulted in a decrease in City income tax revenues by 5.8 percent from 2010 levels. City income tax revenues were also negatively impacted by federal depreciation tax bonuses for capital equipment aimed at incentivizing economic growth.[3]

A significant portion of the drop in City income tax revenues in 2011 was attributable to the substantial delay in the State's distribution of income tax revenues to the City, with monthly payments received an average of 120 days after the payment amounts were finalized. While this does not affect the aggregate amount of City income tax revenues, it has a negative impact on the City's cashflow. Because amounts received after March cannot be accounted as revenue for the preceding budget year, only 11 months' worth of income

INCOME TAX REVENUE

$ Millions Unemployment Rate



[2] Also in 2011, the State increased the personal income tax rate from 3 percent to 5 percent and the corporate income tax rate from 4.8 percent to 7 percent. However, municipalities did not receive a share of this increase because the State, concurrently with increasing tax rates, reduced the percentage of total income tax receipts that flow into the Local Government Distribution Fund (LGDF; the fund from which municipalities are paid their share of state income tax revenue). Distributions to the LGDF were decreased from 10 percent of both personal and corporate income tax revenue to 6 percent of personal income tax receipts and 6.86 percent of corporate income tax receipts. If municipalities had received the historic 10 percent local share, the City would have received additional revenue of more than $50 per resident per year beginning in 2011.

[3] The federal depreciation bonus rule was adopted as part of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 and significantly reduced the corporate tax base. The Act provided a 100 percent depreciation bonus for capital equipment placed in service between September 8, 2010 and December 31, 2011, and a 50 percent depreciation bonus for capital equipment placed in service between December 31, 2011 and December 31, 2012. By affecting the State's definition of "income," this legislation caused a decrease in the City's income tax revenues.

tax payments could be booked as revenue in 2011. In 2012, due to the timing of State distributions to catch up on back payments owed to the City, 13 payments were booked as revenue for the year. In addition, beginning in the second half of 2011 and continuing through 2012, income tax collections gained momentum, ending 2012 at $245.2 million.

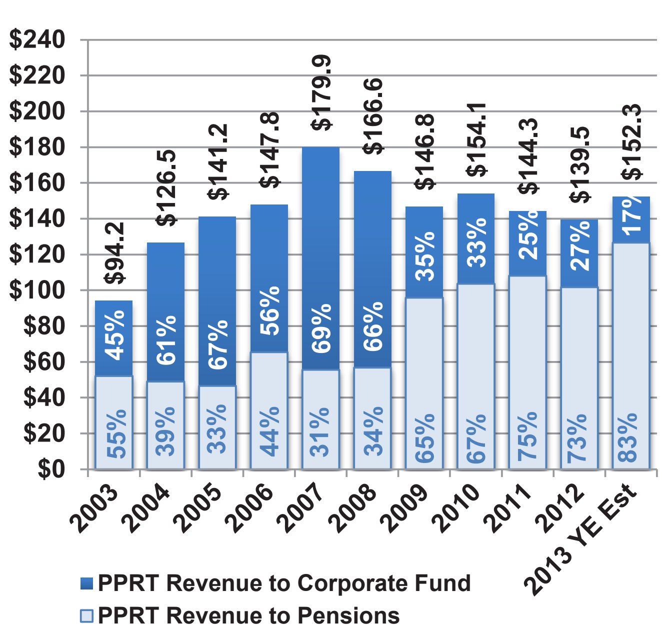
It is anticipated that the City will again receive 13 monthly distributions in 2013 as the State continues to catch up on back-payments, and that income tax revenues will finish the year at $276.0 million. Growth over 2012 is due in part to the stabilizing economy, but revenues are also being pushed upward by a one-time surge in payments seen in April associated with businesses and individuals selling assets or receiving early dividends or bonuses in 2012 in anticipation of higher federal tax rates.

Personal Property Replacement Tax

The personal property replacement tax (PPRT) is levied on corporations, partnerships, and utility companies, based on income. The tax is collected by the State and paid to local governments in order to replace revenues that were lost when the State eliminated the authority of local governments to collect personal property taxes on business entities. The City has historically utilized its PPRT revenue in part to support the corporate fund and in part to pay for the City's employee pension contributions.

PPRT REVENUE

$ Millions



Because PPRT is an income-based tax, these revenues have generally followed the same patterns as income tax revenues, growing through 2008 and then declining during the recession years. However, the anticipated uptick in these revenues with the recovering economy has been negated in part by legislation enacted by the State in 2011 that allows the State to divert PPRT revenue away from municipalities to pay State Board of Education regional superintendents and other state officials. These diversions reduced net PPRT revenues to the City beginning in 2011.

Corporate fund revenue from this tax is also being impacted by the City's growing pension obligations. As a growing portion of PPRT revenue was used to pay for the City's employee pension contributions, the amount of PPRT revenue flowing into the corporate fund decreased by 66 percent between 2008 and 2012, from $109.7 million to $37.6 million, and the City expects that $25.7 million in PPRT revenue will flow into the corporate fund in 2013.

Non-Tax Revenues

Non-tax revenues consist of revenue from licenses and permits; fines, forfeitures and penalties; fees for services; leases, rentals, and sales; interest; and other revenue.

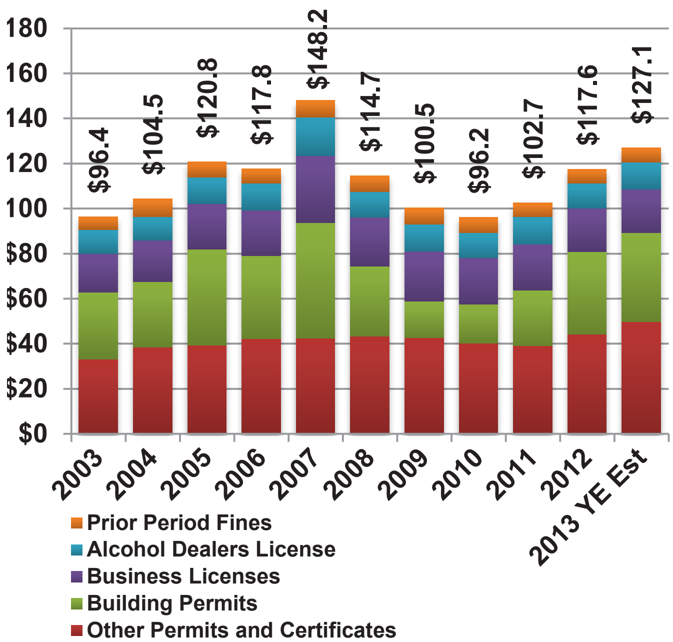
License and Permit Fees

License and permit-related revenue is generated through fees for business licenses, building permits, and various other licenses and permits. License and permit activity often reflects economic health, with more construction commencing and businesses starting up when the economy is strong. In 2003, license and permit revenue was $96.4 million, increasing to $148.2 million in 2007, and then falling to $96.2 million in 2010. The sharp decrease between 2007 and 2008 was also due in part to the transition to a two-year cycle for business licensing. Since 2010, license and permit fee revenues have increased slightly each year and are expected to generate $127.1 million in 2013, back up to 11 percent above 2008 revenues.

Prior to the recession, building permit revenue accounted for the largest portion of overall license and permit revenues – contributing $51.4 million in 2007. As construction activity in Chicago declined during the recession, revenue from such permits decreased to $24.5 million in 2011, down 52 percent from the 2007 high. Permit activity and related

LICENSE AND PERMIT FEE REVENUE

$ Millions



revenues began to recover in 2012, and activity is expected to increase again in 2013 as the real estate market continues to rebound, taking anticipated building permit revenue up to $39.4 million.

Fines, Forfeitures, and Penalties

Fines, forfeitures, and penalties include parking tickets, red-light camera tickets, and fines for items such as building code violations. These revenues have increased steadily over the past decade, from $177.9 million in 2003 to $290.8 million in 2012, accounting for 10 percent of total 2012 corporate fund revenue. This steady upward trend is in part the result of the increased use of technology, including the installation of red-light cameras, the implementation of on-line bill payment systems, and additional parking enforcement field technology. Increases in fine and penalty rates and improved debt collection have also impacted overall fine, forfeiture, and penalty revenues. In 2013, fines, forfeitures, and penalties are expected to generate $324.6 million.

Charges for Services

Charges for services include revenues generated by charging for activities such as inspections, public information requests, police services, and other services for private benefit. In 2003, these activities generated $65.2 million, increasing to $124.6 million in 2012, due largely to increased reimbursement for police services and improved emergency medical service collections. Such services are projected to generate $116.0 million in 2013, accounting for 4 percent of total corporate fund revenue.

Leases, Rentals, and Sales

Revenues generated by the lease or sale of City-owned land, impounded vehicles, and other personal property account for a small percentage of overall corporate fund revenue. In recent years, the City has implemented an online auction system for the sale of unneeded surplus materials and equipment, increasing the efficiency of this process and enhancing opportunities for coordination between City departments.

These revenues vary from year to year based on the inventory of City property to be leased or sold and the market for such property, and have ranged from $34.5 million to $10.7 million per year over the past decade. In 2012, lease and sale income was $14.7 million, at the lower end of the historic range due in part to the amount of City land that was sold over the course of the year. The City anticipates that total lease and sale revenues will be $23.3 million in 2013, due in part to an increase in scheduled payments under the City's contract for bus shelter advertising.

Internal Service Earnings

Internal service earnings are transfers to the corporate fund for services provided to other City funds and agencies, such as police, fire, and sanitation services provided to the City's enterprise funds. Such transfers constitute an average of 10 percent of corporate fund revenues, and have ranged from $250 million to $310 million over the past 10 years.

Proceeds and Transfers In

Property Taxes

No revenue from the property tax levy currently flows into the City's corporate fund, as these funds are used entirely for payment of the City's debt service and pension obligations. The last year that any property tax revenue flowed into the corporate fund was 2004. The use of the City's property tax revenue is discussed in greater detail in the Property Tax section of this document.

Other Proceeds and Transfers In

As the recession negatively impacted economically-sensitive revenues beginning in 2008, the City increasingly used non-recurring revenue sources to fill the annual corporate fund budget gap. Between 2003 and 2007, these transfers constituted an average of 6 percent of corporate fund revenues each year, and came largely from investment income on general obligation bond proceeds and other financing transactions. In 2005, the City began to use proceeds from the long-term lease of the Skyway, and in 2008 proceeds from the long-term lease of the parking meter system began to subsidize the operating budget. In the period from 2009 through 2011, an average of $487 million each year, or 16 percent of corporate fund revenues, came from such non-recurring revenue sources. The 2012 and 2013 budgets made significant progress towards aligning expenses with real revenues. The City anticipates reducing the use of such proceeds and transfers to approximately 1 percent of total corporate fund revenues in 2013.

Corporate Fund Expenditures

Since 2003, total corporate fund expenditures have ranged from a low of $2.6 billion in 2004 to a high of $3.1 billion in 2008. Generally, the relative proportion of total corporate fund spending devoted to different activities and expense types has remained fairly consistent over the years. These activities and spending patterns are discussed in detail below.

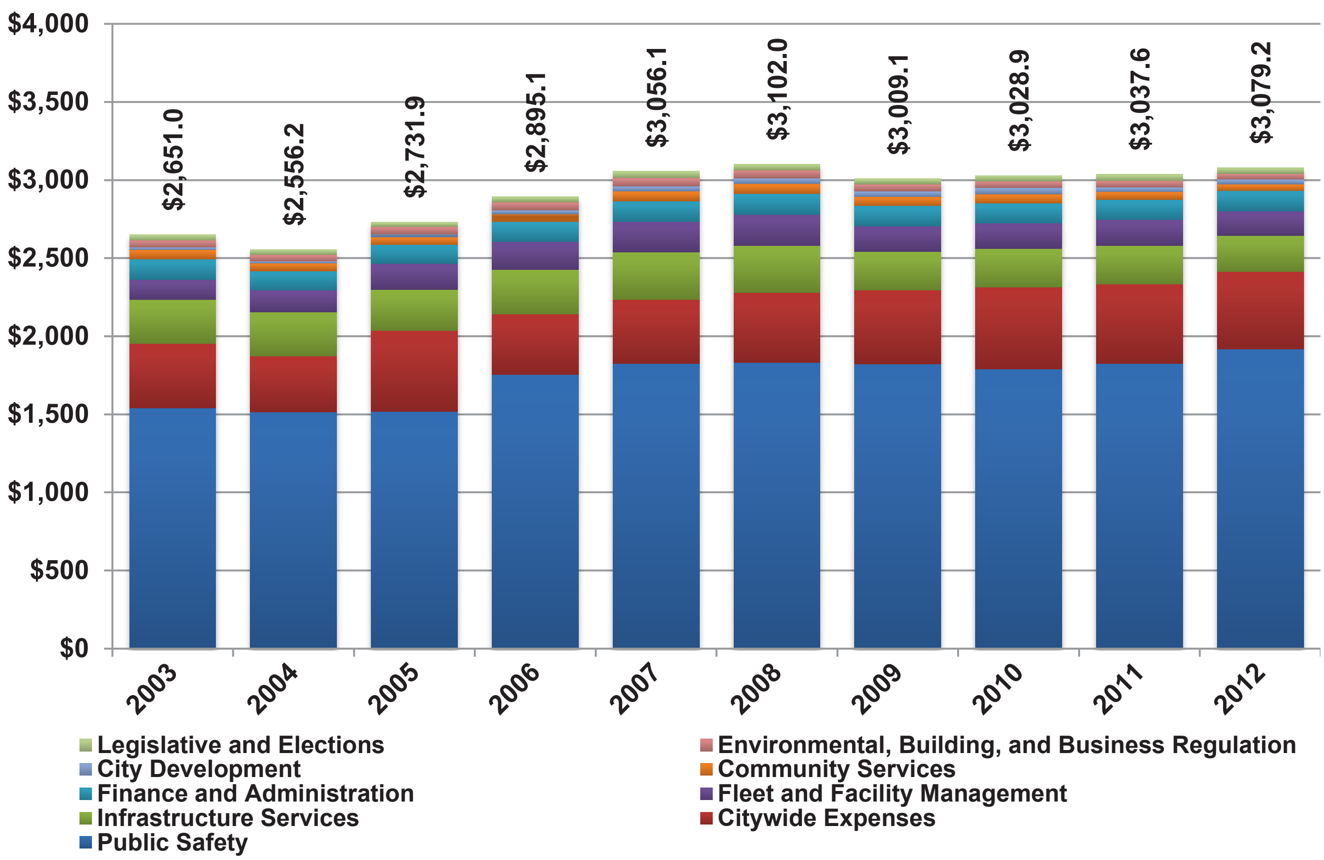
Spending by City Service [4]

Public Safety

Each year, the largest portion of corporate fund spending is dedicated to public safety functions, with police services representing an average of 41 percent, the Fire Department

SPENDING BY CITY SERVICE

$ Millions



[4] Over the years, a number of City departments have been combined or merged into new or existing departments. References in this section to specific existing departments and the resources dedicated to them include predecessor departments and the resources dedicated to those functions in the past.

Financial History Review

16 percent, and the Office of Emergency Management and Communications 3 percent, of total corporate fund expenditures. As spending has been reduced in other areas, public safety has grown as a percentage of the corporate fund budget, from 58 percent in 2003 to 62 percent in 2012.

Infrastructure Services

Infrastructure services provided by the Department of Streets and Sanitation and the Department of Transportation have averaged approximately 9 percent of annual corporate fund expenditures over the past 10 years. These funds are used to collect the City's recycling and waste; trim trees and remove graffiti; build, repair, and maintain Chicago's streets, sidewalks, and bridges; and complete the planning and engineering behind this infrastructure.

Much of the City's major infrastructure construction is funded through state and federal grants and general obligation bond financing, and thus is not represented as a corporate fund expenditure. These funds and the projects they support are discussed in more detail in the Capital Investments section of this document.

The City's waste collection and recycling costs grew steadily from 2006 through 2011, largely as a result of increasing personnel expenses, which are the principal driver of waste management expenditures and are subject to collective bargaining. Over the past two years, the City has implemented changes that increase the efficiency of its waste collection and recycling programs at the same time as improving the quality of these services.

In 2011, the City initiated a competitive bidding process for the provision of recycling services, and today, private companies are delivering recycling services in some parts of Chicago while other neighborhoods are being served by City crews. Based on performance to-date and the current price of commodities, it is projected that the total annual cost for citywide recycling will be 29 percent less than the program would have cost without the competition. These savings are being put towards the citywide expansion of blue cart recycling services, which will be complete by the fall of this year.

In 2012, the City began the transition from ward-by-ward to grid-based collection of waste. Under the ward-based system, Chicago's cost of waste collection and disposal was significantly more than in most major metropolitan areas. The transition to a more logical and efficient system of garbage collection with borders based on main streets and natural boundaries was completed in April of 2013. This change will save approximately $18 million annually, enabling the City to redirect resources to support other essential services, including the expansion of blue cart recycling.

City Development

City development activities, including planning and zoning; the promotion of retail, industrial, and commercial projects; and support for affordable housing, have represented an average of 1 percent of corporate fund expenditures since 2003. A significant portion of these activities are funded through state and federal grants and thus not represented as corporate fund expenditures; these funds and the projects they support are discussed in more detail in the Grants section of this document. The Department of Cultural Affairs and Special Events, which manages the promotion of tourism, cultural planning, and coordination of special events, is supported almost entirely by the City's hotel tax and special events fund, discussed in the following section.

Community Services

Each year, approximately 2 percent of corporate fund resources are dedicated to providing community services through the Department of Family and Support Services, the Department of Public Health, and the Mayor's Office for People with Disabilities. These departments are heavily grant-funded, and receive, on average, over $500 million in grant funding each year in addition to these corporate fund resources. The services provided through these funds are discussed in greater detail in the Grants section of this document.

Environmental, Building, and Business Regulation

On average, the regulation of businesses and the building industry, together with environmental initiatives, has accounted for 2 percent of annual corporate fund spending. This includes the activities of the Department of Buildings, which ensures the safety of residential and commercial buildings in Chicago by enforcing design, construction, and maintenance standards and promoting conservation and rehabilitation through permitting and inspection processes, as well as functions performed by the Department of Business Affairs and Consumer Protection, such as business licensing and support and consumer protection activities, including the regulation of the taxicab industry.

Fleet and Facility Management, Finance, and Administration

The support functions necessary to provide essential City services, including accounting, contract management, legal advice, administrative services, and technology and systems expertise, consistently account for 4 percent of the corporate fund budget. An additional 6 percent of the corporate fund budget is dedicated to managing the repair and maintenance of City vehicles and facilities, from police cars to libraries to fire stations to street sweepers.

Citywide Expenses

Citywide expenses include employee benefits and other costs that are budgeted separately from the City's operational departments. These expenses, which have constituted an average of 16 percent of corporate fund spending over the past decade, are discussed in greater detail in the Workforce section of this document.

Spending by Expense Type

Personnel

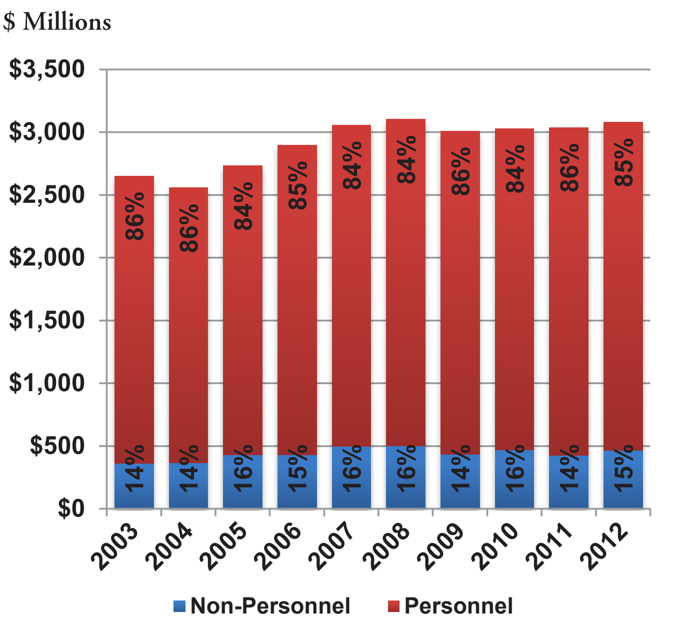
Across all departments and City services, personnel-related expenditures have and will continue to make up the largest portion of the corporate fund budget, with 73 percent of total 2003 to 2012 corporate fund expenditures on salaries and wages, and an additional 10 percent of corporate fund expenditures during those years on employee healthcare costs. These personnel-related expenses and the trends and factors that affect them are discussed on a citywide basis in the Workforce section of this document.

Contractual Services

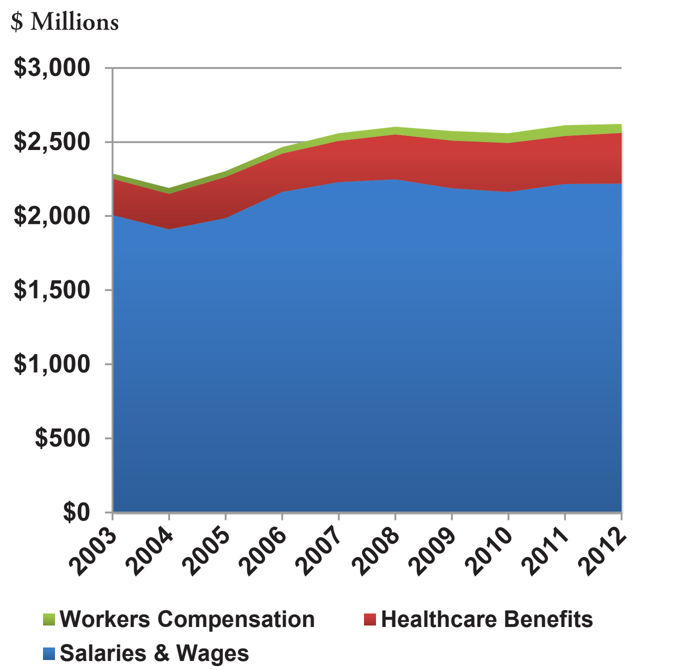
Contractual service expenditures include the cost of information technology systems, maintenance, and licensing; tipping fees for waste disposal; property rental; custodial services for City facilities; and landscaping, engineering, and other professional service contracts. On average, contractual services account for 10 percent, or approximately $288 million, of corporate fund expenditures each year. Between 2003 and 2007, corporate fund contractual services spending grew an average of approximately 7 percent each year, with spending then declining at an average rate of 2 percent each year between 2007 and 2011. In 2012, these expenditures decreased by more than 3 percent from 2011 levels.

As government, businesses, and residents increasingly utilize technology to conduct business and communicate, the City's technology-related costs have increased. In 2003, technology-related costs accounted for 18 percent, or $45.6 million, of all contractual services expenses, increasing to 22

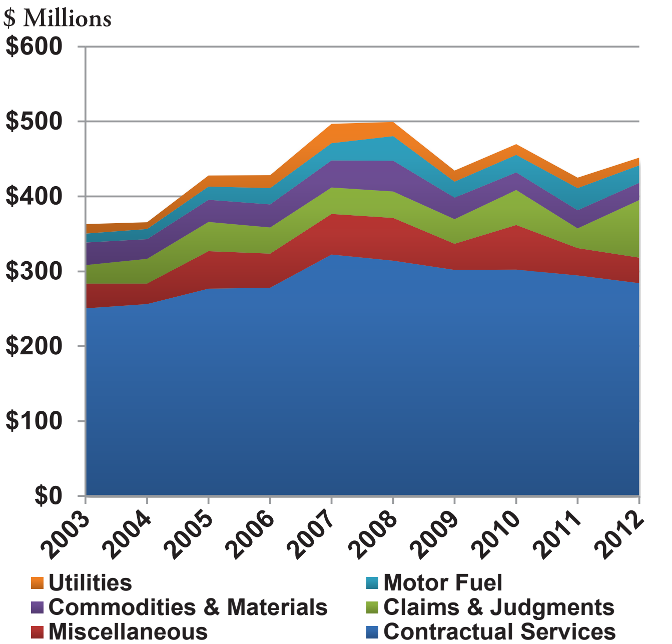
CORPORATE FUND EXPENDITURES



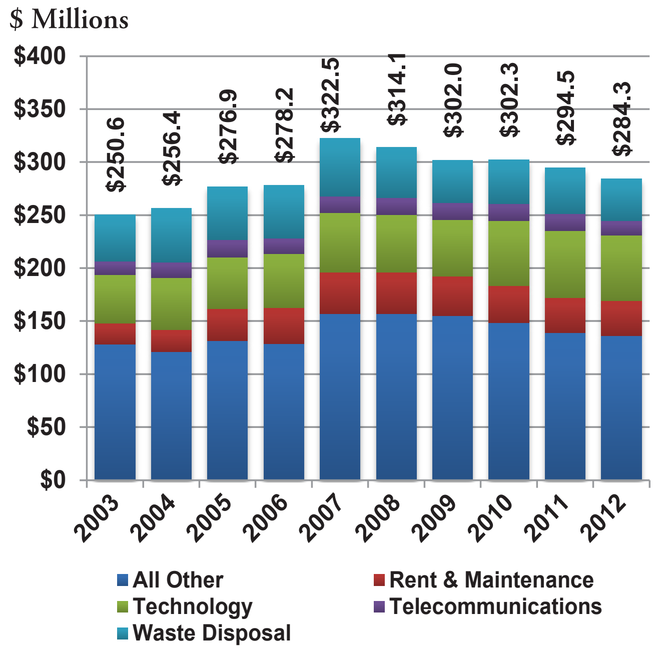
PERSONNEL EXPENDITURES



NON-PERSONNEL EXPENDITURES



CONTRACTUAL SERVICES EXPENDITURES



percent, or $61.8 million, in 2012.[5] Similarly, as telephones have shifted from landlines to mobile over the past decade, the City has appropriately adjusted its telecommunication expenditures to reflect the shift in technology, by spending more on mobile communication and less on landline based systems. As a result of managing these costs, the City remains approximately level with 2003 expenditures in this category. In 2012, overall corporate fund telecommunications expenses were $13.6 million, compared to $13.0 million in 2003.

Tipping fees for waste disposal (the price charged for the delivery of solid waste to landfill, recycling, or other disposal facilities) peaked in 2007 at $54.6 million and have decreased since that time. The initial decrease was due in part to the end of the blue bag recycling program, which resulted in significantly reduced tipping fees related to the mechanical sorting of recyclables.

In 2003 and 2004, the City received a rent abatement for one of its largest rental properties, resulting in lower than normal property rental and building services expenses in those years - averaging $20.2 million, or 8 percent of corporate fund contractual services expenses. These expenses increased in 2005 with the end of that abatement and grew thereafter with increasing rental costs and cost of building services, and by 2008 were $38.9 million, or 12.4 percent of contractual services expenses. Since 2008, rental and related expenses have decreased to $32.8 million as the City reduces the number of properties that it leases.

At the end of 2013, the City's lease at 33 N. LaSalle will expire. Instead of renewing this lease, the City has undertaken a major consolidation and reorganization of City department office space that will lead to more than $4 million in annual savings while grouping similar functions together in order to increase efficiencies and facilitate beneficial coordination. Significant improvements to City Hall will be completed in conjunction with the consolidation, enabling the City to maximize the utilization of this City-owned space. The City estimates that the cost of the consolidation and renovation will total approximately $12 million, which will be paid for with the lease savings and fully recouped within three years.

Commodities and Materials

Expenditures for commodities and materials followed a similar pattern to those for contractual services, but on a much smaller scale. On average, commodities and materials have accounted for approximately 1 percent, or $29.3 million, of corporate fund expenditures each year. Between 2003 and 2008, corporate fund spending on commodities

[5] In addition to corporate fund resources, the City utilizes proceeds of general obligation bonds to finance certain information technology expenses, as further discussed in the Debt section of this document.

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and materials grew at an average rate of 7 percent each year. These expenditures then decreased at an average annual rate of 13 percent between 2008 and 2012, as spending was reduced on items such as office supplies, small tools, electrical supplies, and repair parts for vehicles and other equipment.

Utilities

Market prices have been the primary driver of the City's utility expenditures, which have made up 0.33 percent to 0.85 percent of annual corporate fund expenditures since 2003. Rising energy prices drove up the cost of electricity and natural gas between 2004 and 2007.

In order to reduce its utility costs, energy use, and environmental footprint, the City has undertaken a number of initiatives in recent years to improve its energy efficiency. Specifically, the City has installed more energy-efficient LED traffic and street lights and retrofitted lighting and energy systems at various City properties. Improved use of technology and monitoring has enabled the City to ensure that building system controls are calibrated and operating as intended and to more effectively analyze trends to inform decisions on energy purchasing. In addition to these measures, the City also signed a multi-year price agreement for electricity in 2010, which helped lock-in lower energy prices. These initiatives, together with broader trends in energy prices, including record low natural gas prices in 2012, resulted in a decline in corporate fund utilities expenditures from $25.9 million in 2007 to $10.1 million in 2012.

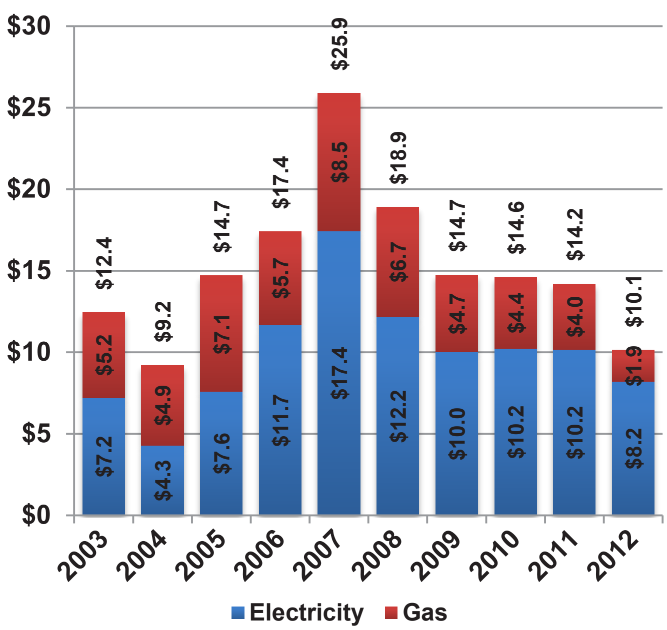
Motor Vehicle Fuel

Rising fuel prices and significant spikes in the oil market have caused City fuel expenditures to increase, much as they have increased gasoline prices for Chicago families. On average, between 2003 and 2008, the City's corporate fund motor fuel expenditures grew at a rate of 23 percent per year, rising from $12 million in 2003 to $33 million in 2008. In 2009, declining prices brought corporate fund fuel expenditures back down to $21 million, but fuel expenditures climbed again in 2010 and grew to $23.6 million in 2012.

In recognition of steadily rising fuel prices and the environmental impact of its gasoline and diesel fuel usage, the City has implemented a number of initiatives in recent years to reduce the City's vehicle fleet and curtail fuel usage. In 2011, the City ended its shared lease program, contracted with Zipcar to provide City employees with access to short-term vehicles, and began utilizing Zipcar reservation technology to facilitate the efficient use of City pool vehicles. The City has also increased the proportion of its fleet that operates on alternative fuel. Currently, the City utilizes over 2,200 electric, hybrid, and alternative fuel vehicles, including police vehicles, light-duty trucks for street work, and larger trucks for completing electrical work and tree trimming.

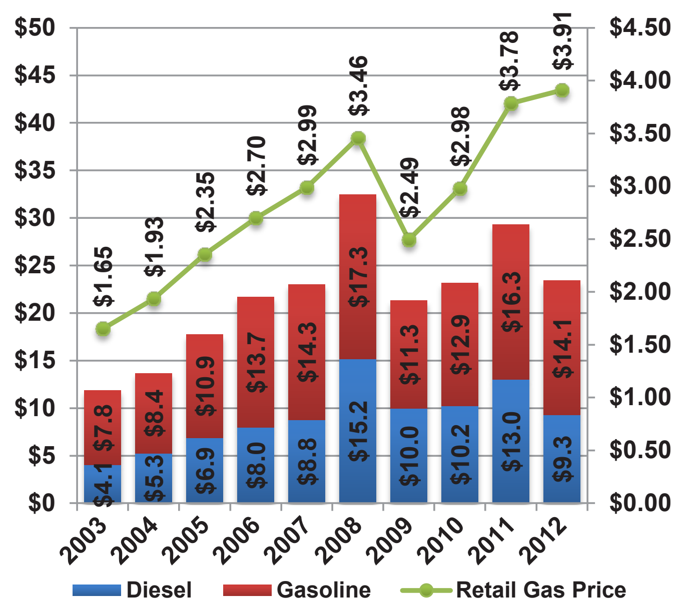
UTILITY EXPENDITURES

$ Millions



MOTOR FUEL EXPENDITURES

$ Millions $ Retail Gas Price



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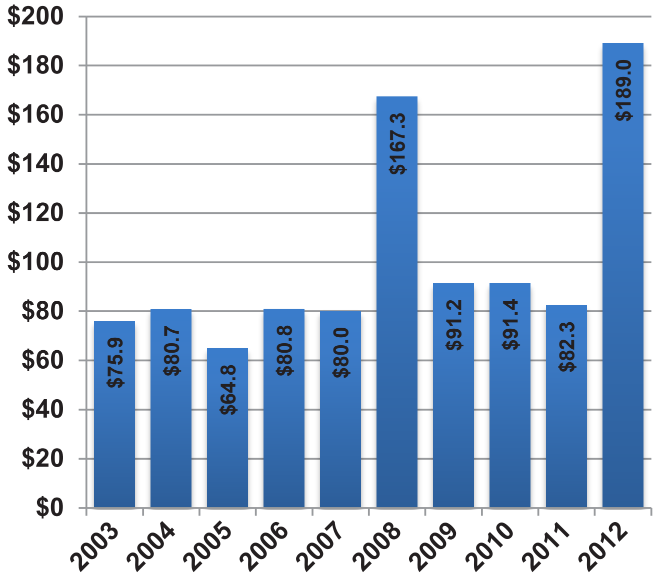
SETTLEMENT & JUDGMENT EXPENSES

$ Millions



Settlements and Judgments

Each year, the City uses both corporate fund resources and bond proceeds to pay for expenses incurred in connection with claims and judgments against the City. Expenses in excess of the amount budgeted on the corporate fund are paid with bond proceeds. The amounts presented in the chart above represent the City's total claim and judgment-related expenses, including both local fund and bond-funded expenses.

The City's total claim and judgment-related expenses, which have ranged from $64.8 million to $189.0 million over the past 10 years, vary from year-to-year depending upon the volume and nature of claims filed and settled, the value of judgments entered, and the extent to which the City utilizes outside legal counsel to address these claims. Claims related to one year are often not settled until years later, and judgments are often paid out over a number of years, so the distribution of expenses is not necessarily representative of the events or activities of that year. Relatively high expenses in 2012 are attributable in part to the verdict of the *Lewis* case regarding the disparate impact of a test administered to applicants to the Chicago Fire Department in 1995, which resulted in the payment of $51.5 million to plaintiffs, $13.3 million to the pension fund for employee contributions, and $8.1 million in additional legal costs for the City.

On average, over the past decade, between 60 and 70 percent of the City's claim and judgment expenses each year have been attributable to police-related litigation. There has recently been a reduction in the number of intentional police misconduct cases filed against the City, from over 550 in 2009 to an average of 265 cases per year for the past three years.

Each year, the City utilizes outside counsel as special counsel to represent the City in unique matters in which there is no in-house expertise, when there are insufficient in-house resources, or where there is a conflict that requires separate representation. The annual cost of these outside legal resources has averaged $22 million over the last eight years. In 2011, the City took measures to reduce these costs by right-sizing the number of in-house attorneys and engaging some of the top law firms in Chicago to handle matters on a pro-bono basis. The right-sizing of the Law Department has resulted in the reduction of outside counsel engagements, reducing expenses over the long-term, and the engagement of pro bono counsel has saved approximately $10.2 million in legal fees over the past 18 months.

Special Revenue Funds

Vehicle Tax Fund

The vehicle tax fund receives revenue from vehicle sticker sales, impoundment fees, abandoned auto towing fees, pavement cut fees, commercial refuse container fees, and state and federal grants and other funds for the maintenance of the public way. These funds are used to pay for street repair and maintenance throughout Chicago.

Since 2003, revenue from impoundment fees has averaged $12.6 million per year, pavement cut fees $4.8 million per year, and sale of impounded autos $5.4 million per year, without significant fluctuation from year to year. Proceeds from the sale of City vehicle stickers have consistently made up the largest part of total vehicle tax fund revenue, gradually increasing from $90.3 million in 2003 to $99.9 million in 2011 and then increasing to $115.5 million in 2012 with the increase in the price of vehicle stickers. These revenues also grew as a percentage of total fund revenue, from 64 percent in 2003 to 73 percent in 2012.

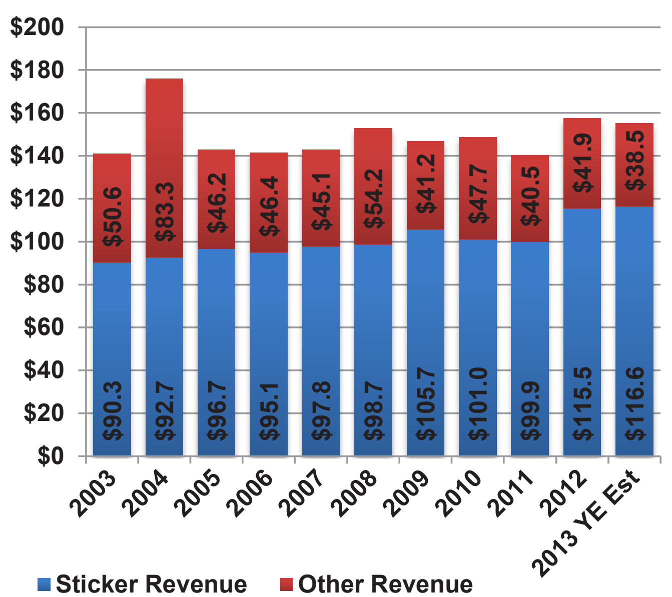
Over the past 10 years, annual resources available to the vehicle tax fund have generally ranged from $119 million to $165 million, and for much of the past decade, this fund has operated at a deficit, as revenues, in particular those from state, federal, and other City funds, consistently came in below budgeted levels, and street repair and maintenance expenses outpaced those revenues. A negative fund balance was carried over into each year from 2003 through 2010, peaking with a negative balance of $33.8 million carried into 2008. This amount has decreased each year since 2008 as the City has worked to more realistically assess the resources that will flow into the fund and manage spending accordingly. A positive balance will be carried into 2013, and the City will continue to budget this fund in a manner that prevents the build-up of operating deficits like those seen in prior years.

Vehicle tax fund expenditures are dependent on the amount, type, and cost of performing street repair and maintenance activities in a given year. Year-to-year variations in total expenditures also reflect the resources available to complete such work. For example, over-spending in 2003 and 2007 resulted in significant deficits carried into the following year, reducing the resources available in that year, as is evident in the drop in spending in each of 2004 and 2008. The City's efforts to stabilize this fund are apparent in more recent years, in which spending has been relatively constant and more closely in line with revenues.

Spending on contractual services steadily decreased between 2003 and 2009, due in part to decreases in tipping fees for waste disposal, and has since held at approximately $22.9

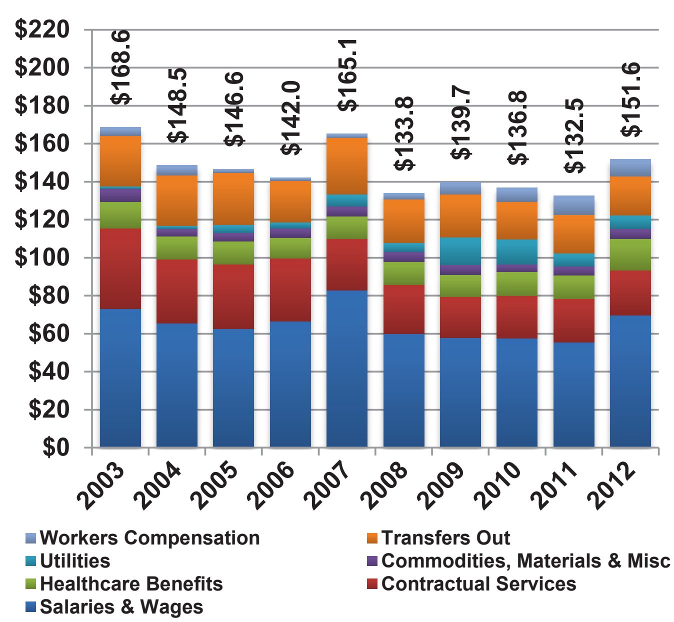
VEHICLE TAX FUND REVENUE

$ Millions



VEHICLE TAX FUND EXPENDITURES

$ Millions



million per year. The vehicle tax fund in the past supported the disposal of waste deposited on the public way from a variety of sources, including waste from street sweeping, refuse from receptacles on commercial streets, litter remaining on the public way following parades and special events, and debris from vacant lots, underpasses, viaducts, and expressway frontages. Over the course of the past decade, a greater portion of these activities have been moved onto the corporate fund, resulting in a corresponding decrease in contractual waste disposal expenses on the vehicle tax fund.

Utility expenses for street light electricity on this fund decreased after 2010, when the City signed a multi-year price agreement for electricity that helped lock-in lower energy prices. Workers' compensation costs on the vehicle tax fund increased in recent years as the City more accurately allocated the cost of claims associated with the street repair and maintenance work supported by this fund.

Motor Fuel Tax Fund

Motor fuel tax fund (MFT fund) revenues are generated primarily through a 19 cent per gallon tax on motor fuel (21.5 cents per gallon on diesel) imposed by the State, of which the City receives a distributive share. Similar to the vehicle tax fund, MFT fund revenue is used for street repair and maintenance. The MFT fund, however, also has a budget for expenditures specifically related to winter weather events.

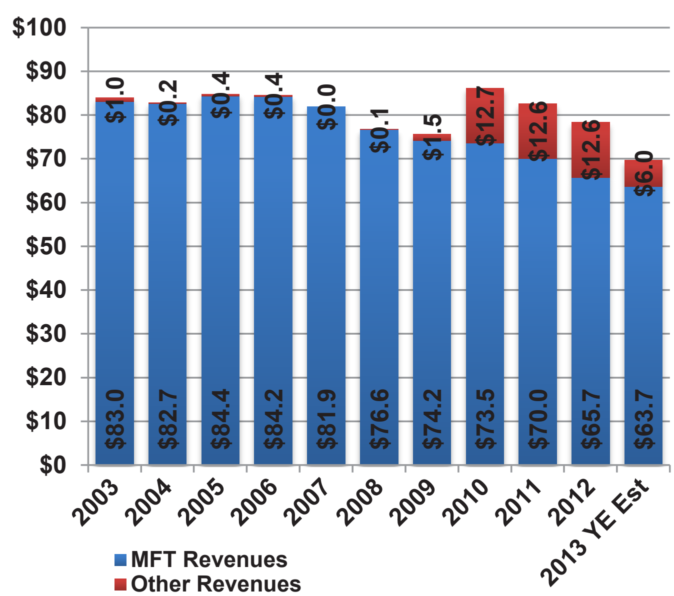
Annual motor fuel tax revenue fluctuates with the price of fuel and the overall economy. Increases in the cost of fuel tend to result in declines in usage – people drive less when the price of gas is high. People also tend to tighten spending on gas during economic downturns. Consequently, revenues from motor fuel taxes have decreased as the price of fuel has increased and in recent years as the recession affected consumer spending. The movement towards more fuel efficient vehicles has also impacted fuel consumption in recent years. Motor fuel tax revenue decreased from $83.0 million in 2003 to $65.7 million in 2012, and is expected to decrease further in 2013. From 2010 through 2012, the City received $12.5 million each year from the State's "Illinois Jobs Now!" plan, which was allocated to the MFT fund. Based on the State's budget for this fiscal year, the City expects to receive these funds through 2014.

The MFT fund has been operating at a deficit for seven of the past 10 years, with expenditures from the fund often greater than revenues coming in from motor fuel taxes. This deficit has been the result of a number of factors, including the sensitivity of motor fuel tax revenues to the price of gas and the economy, and the inherent difficulty of predicting fund expenditures due to the volatility of Chicago weather. The fund carried a negative balance of $35.6 million into 2009, $39.8 million into 2010, and $10.4 million into 2011. By realistically estimating revenues and assessing the City's ability to control these expenses, this deficit was eliminated and the City carried a positive balance into each of 2012 and 2013. Carryover such as this assists in mitigating the effect of future fluctuations in the price of fuel or unpredictable weather events, building up reserves for high snow years.

Expenditures for this fund cannot be categorized like those for other funds because accounting for this fund is performed on a project rather than a fund level. Similar to the vehicle tax fund, year-to-year variations in total motor fuel tax fund expenditures reflect both annual needs and the resources available to complete projects. Projects supported by this fund include street and traffic light maintenance, bridge and pavement maintenance, and snow and ice removal. In addition, a portion of these funds is transferred to the CTA to support the Chicago transportation system. Debt service on motor fuel tax revenue bonds, the proceeds of which fund the construction of road-related improvements, is also paid out of this fund.

MOTOR FUEL TAX FUND REVENUE

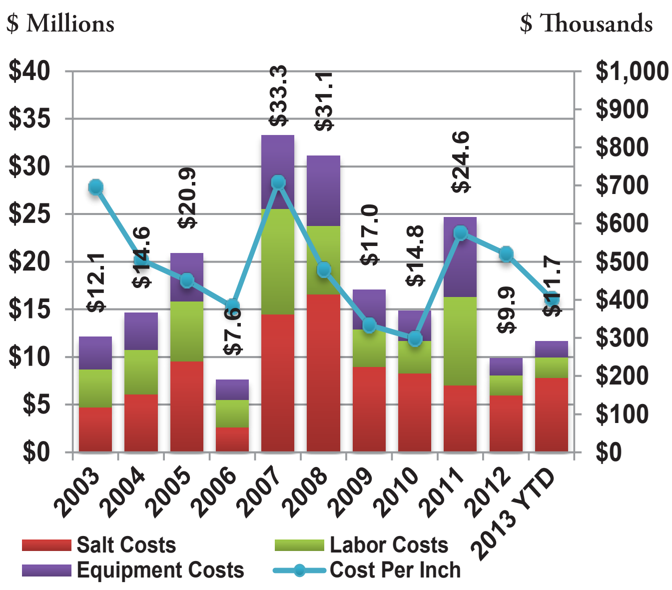
$ Millions



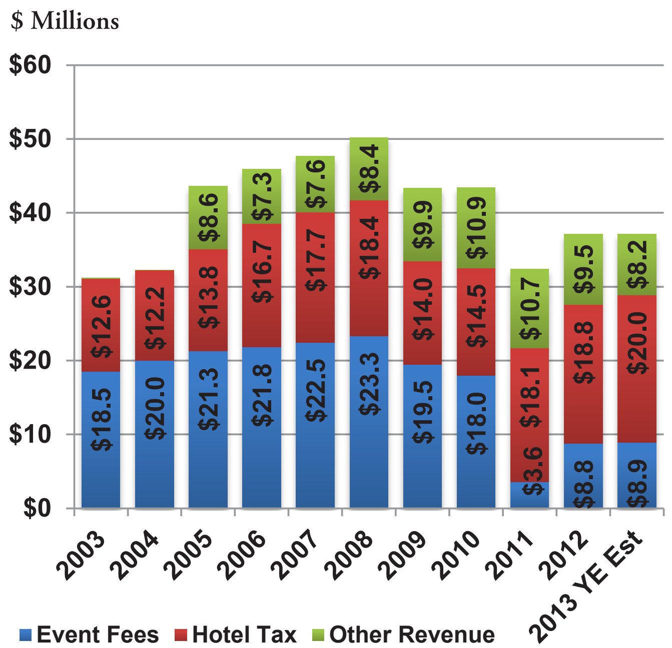
A primary driver of MFT fund expenditures is the annual cost of snow and ice removal. The funds required for these activities vary greatly from year to year depending on winter weather conditions. For example, the February 2011 snowstorm alone cost the City more than was spent on snow removal during the entire year in 2009 or 2010. By contrast, 2012 expenditures were $1.3 million under budget as a result of warmer temperatures and less snowfall.

In a typical year, about 55 to 60 percent of winter weather-related expenditures are used to purchase salt for ice control on city streets. The remainder of the City's winter weather costs are for labor and equipment. Labor costs declined in 2009 and 2010 as a result of the Coalition of Union Public Employees (COUPE) amendment that was effective from mid-2009 through mid-2011, under which certain unions representing non-sworn employees agreed to earn compensatory time in lieu of overtime pay, enabling the City to temporarily reduce labor costs by not paying overtime rates for employees working on snow removal. Labor costs increased again in 2011 with salary increases under collective bargaining agreements and the expiration and after-effects of the COUPE amendment.

WINTER WEATHER COSTS



EVENT FEE & HOTEL TAX REVENUE



Special Events and Hotel Operators' Occupation Tax Fund [6]

The special events and hotel operators' occupation tax fund supports the promotion of tourism and cultural and recreational activities in Chicago. These activities are funded primarily through the hotel operators' occupation tax, a State-authorized tax imposed on hotel operators at a rate of 1 percent of gross receipts, and revenue from recreation fees in connection with special events.

This fund's revenues are tied to local convention business, tourism to Chicago, and the success of the City's special events. The recession's negative impact on each of these affected the fund's revenue. Both hotel operators' occupation tax revenues and recreation fee revenues saw a general pattern of growth between 2003 and 2008, from $12.6 million to $18.4 million and from $18.5 million to $23.3 million, respectively, followed by a drop in 2009 with the downturn in the economy. Hotel tax revenue began to pick up again in 2011, reaching $18.8 million in 2012 and an anticipated $20.0 million in 2013. Revenue from special events recreation fees decreased in 2011 because the operation of the Taste of Chicago was transferred to the Chicago Park District for that year. With the return of the Taste of Chicago

[6] Historically, these two revenue sources were accounted for in separate funds. The City merged the two funds in 2011 while merging the Department of Cultural Affairs, which oversees the Office of Tourism, with the Mayor's Office of Special Events.

to City operation, recreation fee revenue was $8.8 million in 2012 and is expected to hold approximately even with that level in 2013.

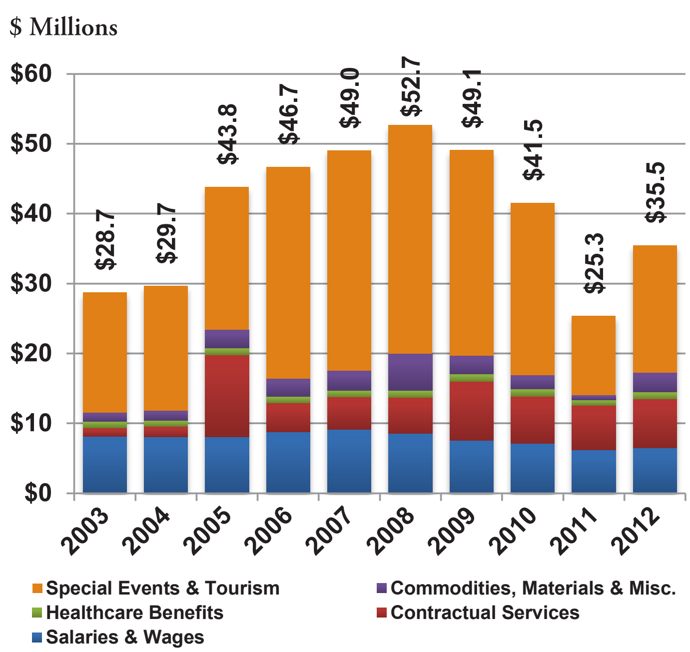
Expenditures from this fund reflect the City's changing approach to events and tourism promotion, as well as broader factors that have affected City spending generally. Major fluctuations in the amounts spent on special events and tourism-related activities can be tied to specific changes in City operations. The almost 50 percent increase in special events and tourism expenditures in 2006 was due in large part to the movement of expenses associated with the operation and management of Millennium Park from the corporate fund to this fund. Special events and tourism expenditures then decreased by more than 50 percent between 2010 and 2011, from $24.7 million to $11.3 million, due to the transfer of the Taste of Chicago to the Chicago Park District and the end of funding for the Chicago Convention and Tourism Bureau (CCTB), a non-City entity that had previously received City funding to conduct its activities. In 2012, the Taste of Chicago returned to City operation and the CCTB was merged with the tourism portion of the Chicago Office of Tourism and Culture to form Choose Chicago, which focuses on promoting travel to Chicago.

Overlying these specific changes to special events and tourism expenses are broader trends. Both revenues to this fund and expenditures from this fund are highly economically sensitive; people are less likely to travel and spend money on recreational events during recessionary periods, and City spending on related activities is likely to be cut when budgets are tightened. Accordingly, personnel costs, as well as spending on items such as commodities and materials, saw increases in the years leading up to 2008, followed by reductions in the post-recession years.

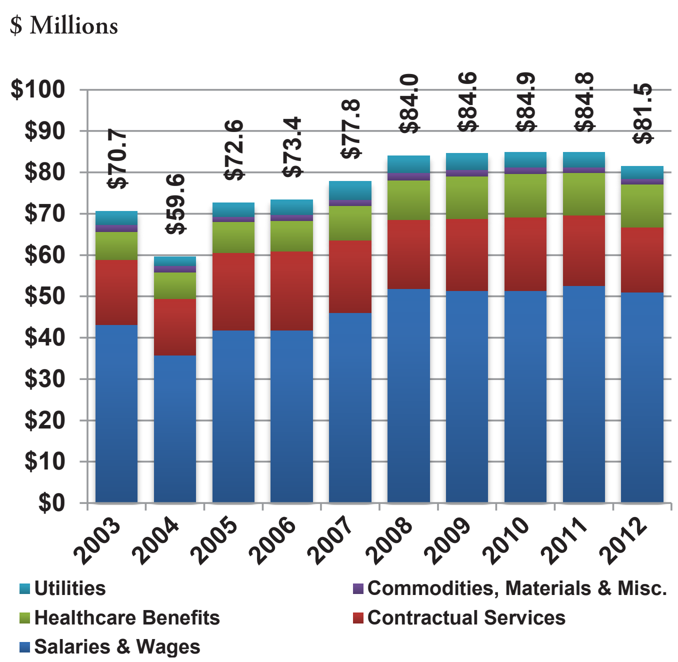
Library Funds

The City maintains segregated funds to support the maintenance and operations of the Chicago Public Library system and its central, regional, and branch locations. Revenue to these funds comes primarily from property taxes and an annual subsidy from the City's corporate fund. In 2008, an $83.4 million portion of the City's property tax levy was dedicated to the library system.[7] The corporate fund subsidy to the library system increased between 2005 and 2008 and then decreased with the allocation of the library's portion of the property tax levy. Since 2008, the

SPECIAL EVENTS AND HOTEL TAX FUND EXPENDITURES



LIBRARY FUND EXPENDITURES



[7] The City's overall property tax levy is discussed in greater detail in the Property Tax section of this document. In the City's 2012 levy, the library's portion of the levy was increased to $83.5 million. In 2013, $5.3 million of the library's portion of the levy is budgeted to pay pension contributions for employees of the library system and $4.3 million of the library levy is allocated to pay debt service related to capital improvements to library facilities.

library fund's corporate subsidy has averaged approximately $13.2 million each year. The remainder of revenue to these funds comes from income from the rental of library facilities, library fines, interest earnings, and transfers in from other funds.

Library fund expenditures have been affected by many of the general trends affecting overall City spending, as well as certain library-specific factors. Total library fund expenditures decreased in 2004, largely as a result of cost savings initiatives in connection with Citywide budget reductions, including layoffs, early retirement incentives, restrictions on hiring, and tightened contractual spending. However, in 2005, overall fund expenditures increased back above 2003 levels as spending restrictions loosened and a number of branch openings, renovations, and expansions were completed.
As in the corporate fund, personnel costs make up the largest portion of library fund expenses, and while a slight decrease was seen in 2012, these costs have generally increased over the past 10 years, due in part to salary increases under collective bargaining agreements and the growing cost of healthcare. Contractual services expenditures have remained relatively constant in recent years, and consist largely of property rental costs for library facilities that are not City-owned and property maintenance and building services expenses for the Harold Washington Library Center and branch libraries, which decreased slightly in 2012.

CTA Real Property Transfer Tax Fund

In 2008, a supplemental tax on real estate transfers was adopted for the purpose of providing financial assistance to the CTA and this fund was established to receive the proceeds from that tax, which are then transferred to the CTA. Because this fund's revenue is generated through real estate transfers, revenue levels remained relatively stagnant due to slow real estate activity during the first three years following its inception, averaging $29.5 million annually. In 2012, revenues increased to $40.8 million, and revenues are expected to increase again to $47.2 million in 2013.

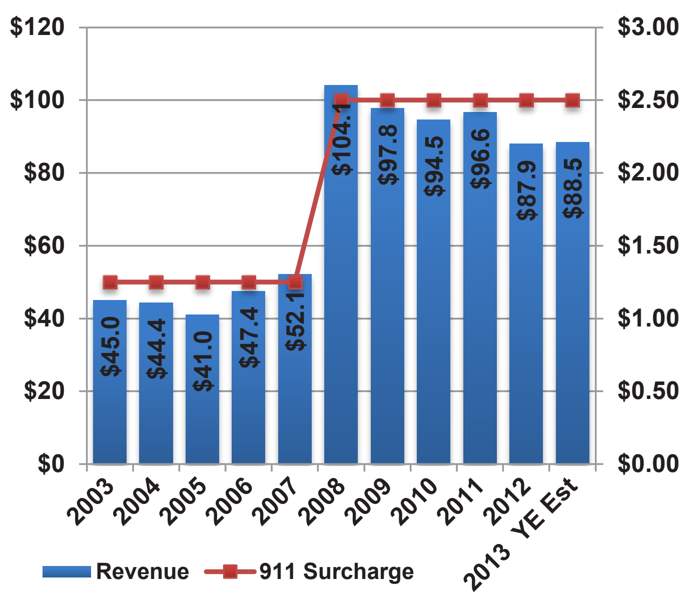
Emergency Communications Funds

The City maintains segregated funds to support the maintenance and operation of the Office of Emergency Management and Communications (OEMC) and to pay debt service on bonds issued to fund the construction of the City's 911 call center.[8] Revenue to these emergency communications funds comes through the collection of the emergency telephone system surcharge on all billed subscribers of telecommunications services within the City.

The surcharge was levied at a rate of $1.25 per month per landline and wireless connection until 2008, in which year the rate was increased to $2.50 and revenues increased accordingly. Total revenue to this fund has, however, been negatively affected by the recent reduction in the use of landlines as more customers choose to have only wireless services, as discussed above with respect to corporate fund telecommunications tax revenues. In addition, beginning in 2012, the emergency telephone system surcharge on prepaid wireless services such as calling cards and 'pay-as-you-go' phones was changed from $2.50 per transaction to a rate of 7 percent of the cost of the service, pursuant to state legislation. This change further reduced revenues to the emergency communications fund, which are down from a

EMERGENCY COMMUNICATIONS REVENUE AND SURCHARGE

$ Millions



[8] OEMC is not funded exclusively through the emergency telephone system surcharge but receives funding from corporate and other revenue sources as well. Corporate fund resources and grant funds are used to fund 911-related expenses above revenue from the emergency telephone system surcharge, as well as the other functions of the OEMC, including traffic management, homeland security, and administration.

peak of $104.1 million in 2008 to $87.9 million in 2012, with 2013 year-end estimates at $88.5 million.

Each year, the City uses a portion of the revenue from the emergency telephone system surcharge to pay debt service due on 911 call center bonds, and then transfers the remaining revenue to the corporate fund to be used for expenses specifically related to the 911-related operations of the OEMC.

ENTERPRISE FUNDS

The City's enterprise funds support the operation, maintenance, and capital programs of the City's water and sewer systems and O'Hare and Midway Airports.[9] These self-supporting funds operate like commercial enterprises, in that each pays expenses with revenue derived from charges and user fees for the services it supports.

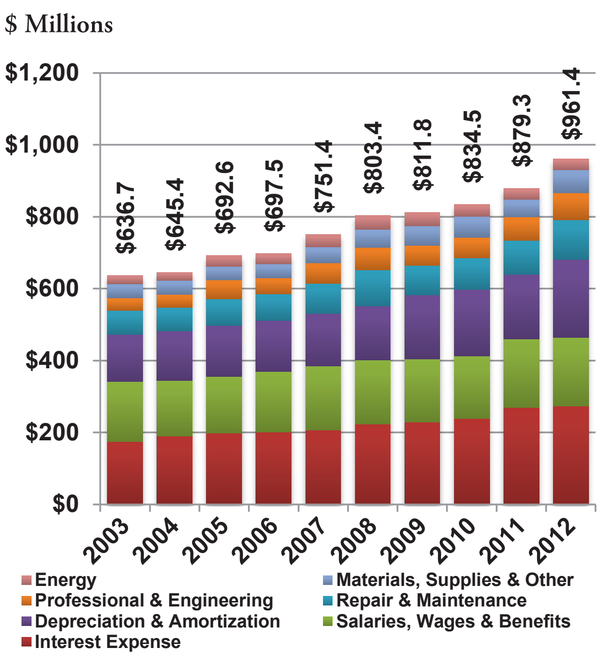
O'Hare and Midway Airport Funds

O'Hare and Midway airport operations are funded through landing fees, terminal rent, and other fees paid by airlines, as well as non-airline sources, such as charges for parking and revenues from concessions in the terminals. The amount that the airlines pay each year is established at each airport essentially on a residual basis – the airlines are charged the amount that is needed to pay for operating expenses and debt service after taking into account non-airline revenues. While capital improvement costs are budgeted separately from the City's corporate and special revenue funds, capital costs for the City's airports are included in the overall budgets of these self-supporting funds.

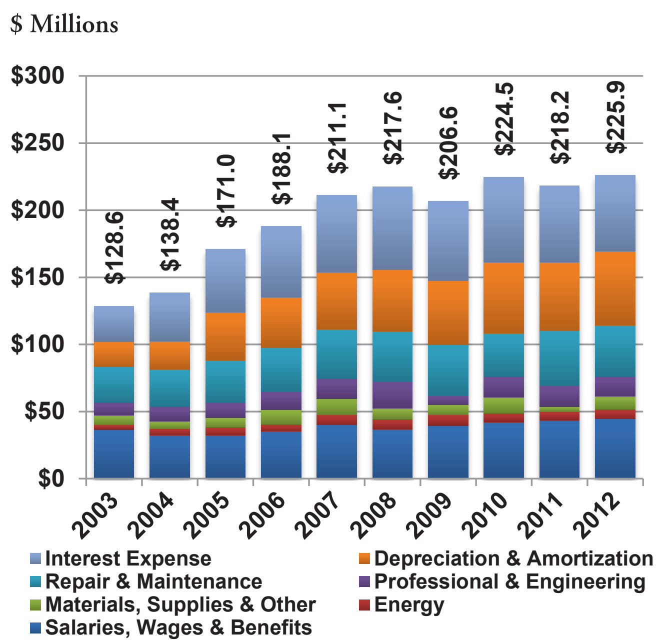
Aviation fund revenues and expenditures reflect the schedule of capital improvement programs at the airports and the health of the travel industry, as well as factors that impact Citywide expenses. Both the O'Hare fund and the Midway fund grew steadily over the past decade, with a slowing in this growth between 2008 and 2009, as the overall economy contracted. The O'Hare fund grew at an average annualized rate of 5.3 percent, from $636.7 million in 2003 to $961.4 million in 2012, and the Midway fund grew at an average annualized rate of 7.3 percent, from $128.6 million in 2003 to $225.9 million in 2012. Both funds are expected to increase again in 2013, to $960.8 million and $228.7 million, respectively.

This overall growth is in part a function of growth at the airports, including expansions, renovations, and increased services. As capital improvement projects such as the O'Hare Modernization Program move forward, interest payments on bonds issued to fund those projects increase, and depreciation expenses associated with those improvements increase in later years. On average, since 2003, interest payments on bonds issued to fund capital improvements at the airports has constituted 29 percent of total O'Hare fund expenses and 27 percent of total Midway fund expenses. In addition, expansions and improvements require greater spending on professional and engineering services, as well as increased repair, maintenance, and other operational needs for the added space or facilities.

O'HARE AIRPORT FUND



MIDWAY AIRPORT FUND



[9] Prior to the long-term lease of the Skyway in 2005, the City maintained a separate enterprise fund for Skyway revenues and expenses. The reserve funds associated with the proceeds from that lease transaction are discussed in detail in the Long-Term Asset Lease and Reserve Funds section of this document.

Financial History Review

Salaries, wages, and employee benefits make up the largest portion of the aviation funds' operating expenses and have increased due to many of the same factors affecting overall City personnel costs, including salary and wage increases under collective bargaining agreements and the increasing cost of healthcare. Personnel expenses for both the O'Hare and Midway funds grew at an average annualized rate of 2 percent between 2003 and 2012.[10] However, during the same years, these expenses decreased as a percentage of total aviation fund expenses, from 27 percent in 2003 to 20 percent in 2012, as aviation fund interest payments and depreciation costs increased. Energy expenses for the airports have followed similar patterns as seen in Citywide utility and fuel costs, reflecting market prices and efficiency initiatives.

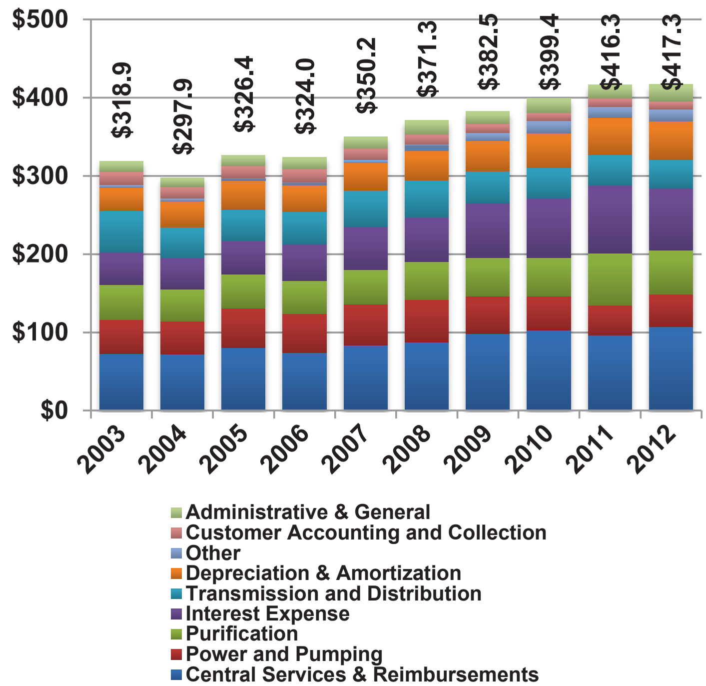
Water and Sewer Funds

The City's water and sewer funds are supported primarily through water and sewer user fees (the revenue obtained from water bills and the sewer surcharge on water bills).[11] These revenues are used to repair, maintain, and improve the City's water and sewer systems. Like the City's aviation funds, capital investment costs for the City's water and sewer systems are included in the water and sewer fund budgets. Overall water and sewer fund expenditures are affected by capital improvement programs, the repair and maintenance needs of the systems, and general factors that impact Citywide expenses.

Total fund expenditures were relatively steady from 2003 through 2006, with a slight drop in operating costs in 2004 attributable in part to early retirement incentives and reductions in personnel expenses. Increases in operating expenses since 2006 reflect increases in personnel expenses and increased spending on the repair and maintenance of the systems. However, much of the overall fund growth that began in 2007 has been due to increased interest expenses, which grew at an average rate of 11 percent per year, from $74.3 million in 2006 to $133.7 million in 2012, following water and sewer revenue bond issuances in 2006, 2008, 2010, and 2012. Proceeds from these bonds are used for the construction and repair of water and sewer lines and related facilities, as further discussed in the Capital Investment section of this document.

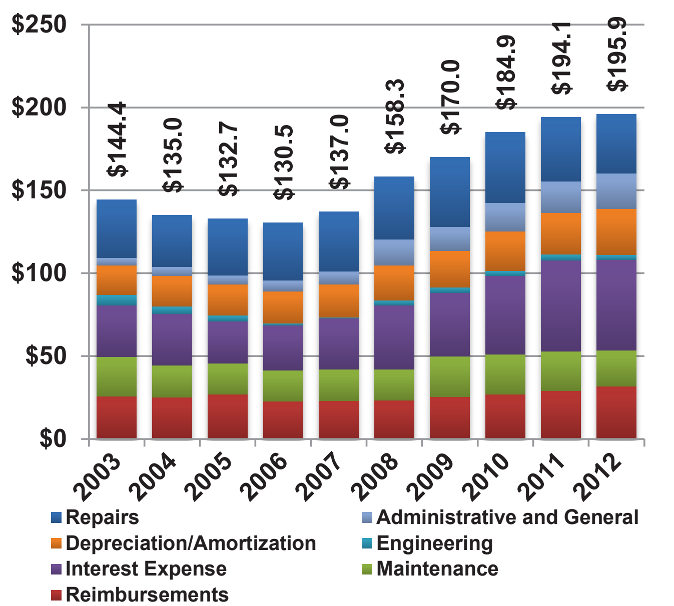
WATER FUND

$ Millions



SEWER FUND

$ Millions



[10] There was a greater than average increase in personnel expenses on the O'Hare fund in 2011, due to retroactive payments required under collective bargaining agreements.

[11] The water fund and sewer fund are segregated funds separate from each other. Water fund revenue is used to support the water system, and sewer fund revenue is used to support the sewer system.

Financial History Review

During the last three years, the City spent more than $65 million repairing leaks in the water and sewer systems and restoring the streets, sidewalks, and other infrastructure damaged as a result of those leaks. These numbers do not include the expenses incurred by businesses and homeowners to repair damage to their property caused by flooding or other expensive inconveniences caused by the failures of water and sewer systems.

In order to address the underlying causes of these system failures, the 2012 budget included a water rate increase from 0.373 cents per gallon to 0.474 cents per gallon, increasing to 0.762 cents per gallon over the next three years. These increases have enabled the City to undertake an accelerated capital program that will bring Chicago's water and sewer systems up to date. Details about the repairs and upgrades being completed as a part of this program can be found in the Capital Investment section of this document. This rate increase brings Chicago in line with national averages for water fees, and the improvements funded will not only protect health and safety by ensuring the delivery of clean water today and in the future, but will also boost the economy by creating jobs and prevent the need for higher fees later by curbing the further deterioration of these systems.

Grant Funding

Grant funding is a significant and recurring source of revenue for the City, constituting an average of 21 percent of the City's annual budget over the past 10 years. The City receives grant funds from federal and state agencies, foundations, and other private entities, and utilizes these funds to provide essential services, support community programs, and complete capital improvements.

Sources of Grant Funding: 2003 - 2012

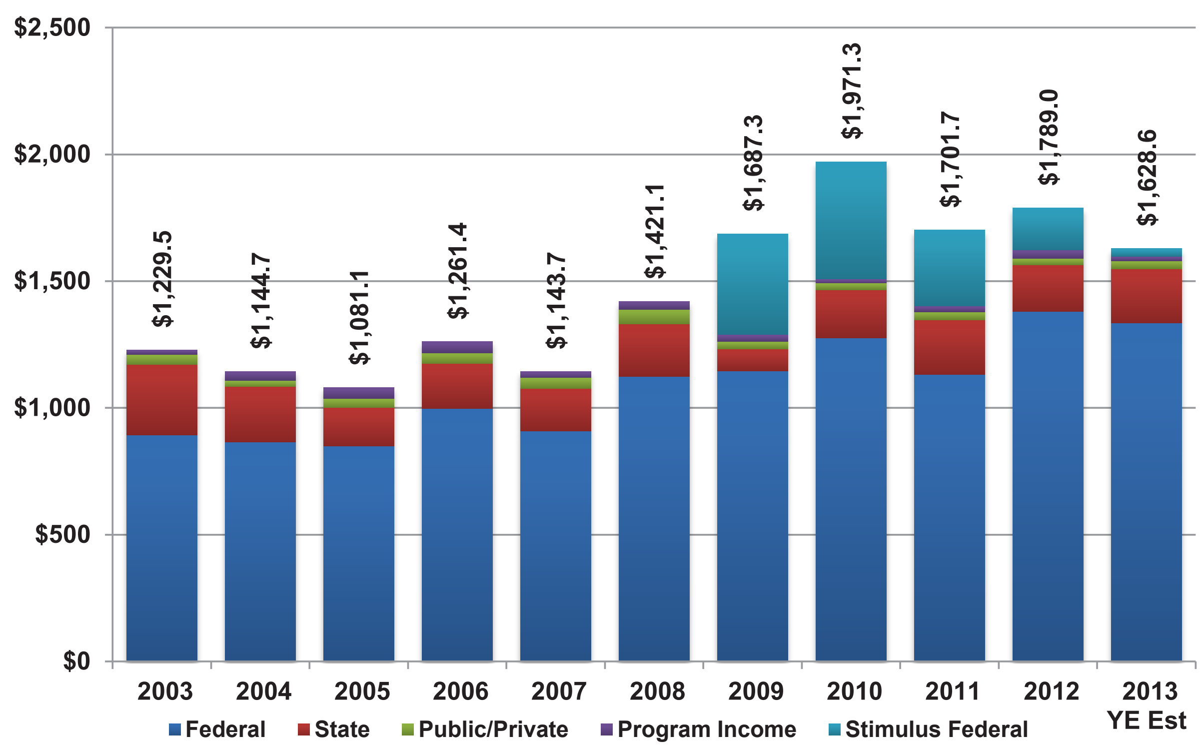
Grant funding has provided an average of $1.45 billion each year over the past decade. The level of grant funding varies from year to year with the availability of grants that meet City needs and the City's ability to obtain those grants. Average annual funding increased in 2009 due to the inflow of stimulus funding from the Federal American Reinvestment and Recovery Act (ARRA).[12] Smaller year-to-year fluctuations in the City's grant funding are often attributable to the timing of large grant-funded transportation and infrastructure projects.

During this period, the City's grant funding has been composed of approximately 82 percent federal funding (including ARRA funding), 13 percent state funding, and 3 percent private funding and donations. In addition, certain of the City's grant-funded programs generate income from user fees or sales, such as charges for health services or payments on home rehabilitation loans. Such income is directed back towards grant programming and has averaged $29.6 million, or 2 percent of total grant funding, per year.

Grants are received on varying fiscal year time periods and may be awarded for multiple years, depending on the goals and fiscal calendar of the grantor. For example, grants from the federal government often follow an October to September fiscal year and are intended to be used to support programs for an extended period of time. State grants typically follow a July to June fiscal year. The City allocates grant funds in adherence with grantor timetables or similar specifications. Therefore, although grant dollars are awarded in a certain year, grants that are intended for use over a longer period of time may not necessarily be fully used in that year. The City

GRANT FUNDING SOURCES[13]

$ Millions



[12] ARRA funding consists of one-time grants to be used for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, affordable housing, and state and local fiscal stabilization.

[13] Due to limitations in available data, 2003 through 2005 reflect the grant funding appropriated in the City's annual budget. For years 2006 through 2012, actual grant funding received is shown. For 2013, anticipated grant funding is presented.

budgets the entire grant award in the year it is anticipated, and amounts remaining at the end of that year are carried over into the next year's budget. The charts in this section reflect the total available grant funds in a given year, including any carryover funds from the prior year.

Uses of Grant Funding: 2003 - 2012

Grant funding supports a wide variety of City services and functions. The graph below presents the amount of grant funding dedicated to different program types over the past 10 years, and each program category is further described below.

Finance and Administration

The Office of Budget and Management, the Department of Innovation and Technology, the Department of Finance, and the Department of Law each receive grant funds to fulfill finance and administration functions for the City. During the past decade, an average of $25.3 million per year, or 2 percent of the City's total grant funding, has been dedicated to these functions. Though these departments do not receive large amounts of grant funding, there was an increase in 2011 and 2012 due to ARRA funding for broadband, high-speed internet, and fiber connections.

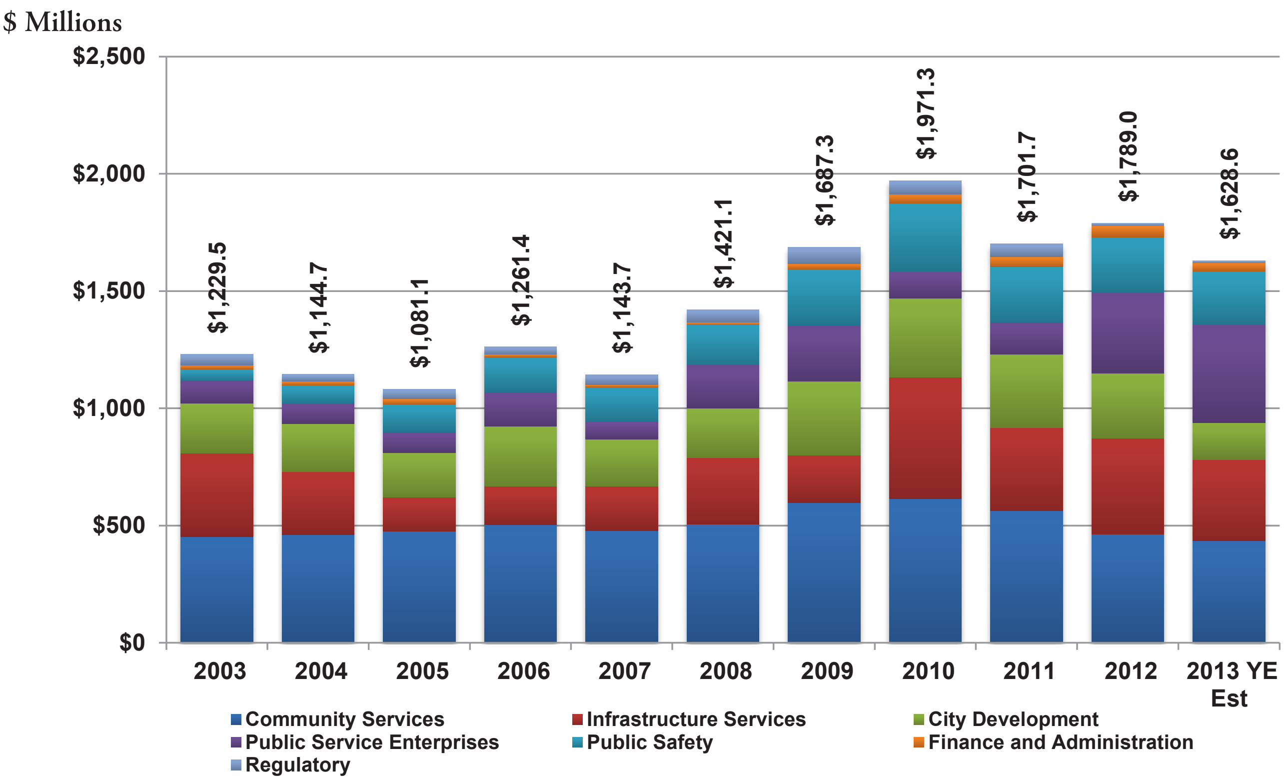
City Development

The Department of Housing and Economic Development and the Department of Cultural Affairs and Special Events are the primary recipients of grant funding. During the past 10 years, an average of $251.6 million per year, or 17 percent of the City's total grant funding, has been dedicated to city development uses. Grant funding in this area increased in 2009 through 2011 due largely to the receipt of $169 million in Neighborhood Stabilization Program funding to bring vacant foreclosed homes up to code and increase home occupation in target areas, and additional HOME Investment Partnership program funds, which provide financial assistance to affordable housing developers, homebuyers, and community-based organizations. Funding for the HOME program was reduced by 51 percent during 2011 and 2012, contributing to an overall decrease in city development funding.

Community Services

Grant funding supports many of the community services provided through the Department of Family and Support Services, the Department of Public Health, the Chicago Public Libraries, and the Mayor's Office for People with

GRANT FUNDING USES[14]



[14] Due to limitations in available data, 2003 through 2005 reflect the allocated programmatic usage of appropriated funds for each year. For years 2006 through 2012, allocated programmatic usage of actual grant funding received is shown. For 2013, allocated programmatic usage of anticipated grant funding is presented.

Disabilities. During the past 10 years, an average of $511.6 million per year, or 35 percent of the City's total grant funding, has been dedicated to community services.

Community services programs are directed towards a wide range of activities, including boosting the economy by creating jobs, increasing vital services for residents, fostering workforce development, providing child care, and operating homelessness and prisoner re-entry programs. As ARRA funds decrease, grant funding for community services has declined accordingly.

Public Safety

Collectively, the Office of Emergency Management and Communications, the Police Department, and the Fire Department have received an average of $170.9 million per year, or 12 percent of the City's total grant funding, over the past decade. Over the years, grant funding for these public safety departments has grown significantly, from $48.1 million in 2003 to $236.9 million in 2012. A significant part of this funding comes from the Urban Areas Security Initiative, which has provided $295.9 million in funding since its initiation to address the planning, organization, equipment, and training needs of high-threat, high-density urban areas in preventing and responding to acts of terrorism.

Regulatory

The majority of the City's regulatory grant funding is for conservation or environmental programs such as weatherization, electric vehicle support, and alternative fuel development, and is managed largely by the Department of Fleet and Facilities Management. In addition, small amounts of grant funding are dedicated to initiatives within the Department of Buildings, the Department of Business Affairs and Consumer Protection, and Animal Care and Control. During the past 10 years, an average of $43.3 million per year, or 3 percent of the City's total grant funding, has been dedicated to regulatory functions.

Infrastructure Services

The Department of Streets and Sanitation and the Chicago Department of Transportation (CDOT) receive grant funding to repair, maintain, and construct City infrastructure. During the past 10 years, an average of $288.9 million per year, or 20 percent of the City's total grant funding, has been dedicated to infrastructure services.

CDOT receives the most grant funding of any City department, as many of the major City transportation-related projects are funded through state or federal grants. In addition, a significant portion of CDOT's grant funding comes from the federal Congestion Mitigation Air Quality program and is allocated towards projects that will contribute to the attainment of national ambient air quality standards in designated non-attainment areas. Grant funding for infrastructure work fluctuates from year to year depending on the number of larger infrastructure projects, such as highways, bridges, streetscapes, and CTA stations, that are underway, as well as the availability of state and federal funds for such projects.

Public Service Enterprise

The Department of Aviation is the primary recipient of public service enterprise grant funding, due to its largely grant funded airport improvement programs. During the past 10 years, an average of $151.5 million per year, or 10 percent of the City's total grant funding, has been dedicated to the public service enterprises, with more than 99 percent of that amount for the Departments of Aviation. As with all infrastructure grants, funding levels fluctuate from year to year based on the type and size of projects undertaken at the airports, including the O'Hare Modernization Program.

Grant Funding Going Forward

In response to the recession, federal stimulus programs such as ARRA increased the amount of grant funding the City received. With the scheduled phase-out of ARRA funding, recent federal and state budgetary restrictions, and the federal sequester, the City expects to see its federal funding decrease to pre-2009 levels by the end of 2013; additional details on the impact of these reductions are discussed below. In contrast, funding for the City's public safety and infrastructure departments is expected to remain relatively stable in 2013 with some normal fluctuation due to the timing of larger infrastructure projects. For example, the Department of Aviation is expected to receive an increase of approximately $75 million, for continuing capital improvement projects at the airports.

The majority of ARRA funding came to an end in 2012, and the resulting reductions in grant funding have been primarily in community services and city development grants, which are expected to experience a net decrease of more than $150 million from 2009 levels by the end of 2013. Over the past couple of years, some of the most important grants received by the City, such as the Community Development Block

Grant (CDBG) and the HOME Investment Partnership Grant (HOME) have seen reductions in funding due to decreased federal spending. Since 2010, CDBG funding has been reduced by 19 percent (or $17 million) and HOME by 50 percent (or $16 million). Although the City has been able to augment spending on these programs through allocations from the Human Infrastructure Funds set up with proceeds from the lease of the Chicago Skyway and parking meter system, these resources are dwindling along with federal dollars. In addition, ARRA funding for broadband, high-speed internet, and fiber connections came to an end this year, resulting in a drop in finance and administration-related grant funding.

Spending cuts from the federal sequester, also, have had a direct impact on the City's grant funding. In 2013, both the Department of Family and Support Services and the Department of Public Health received less federal funding than in previous years, including Head Start, which lost $6.5 million; the Emergency Solutions Grant (ESG), which lost $1.3 million, or 20 percent from its prior year allocation; and the Community Service Block Grant, which lost $1.3 million. These grants are used to fund programs that provide assistance to some of the city's most vulnerable residents such as children under the age of 5 from low-income families, families at risk of eviction, and the homeless. Despite the loss of grant dollars, the City continues to provide essential services and ensure that the residents who rely on these services receive the assistance they need. While the full impact of the federal sequester may not be known until the upcoming year when the new federal grant fiscal year begins, the City is consistently monitoring developments in this area and will respond accordingly to any future reductions in grant allocations.

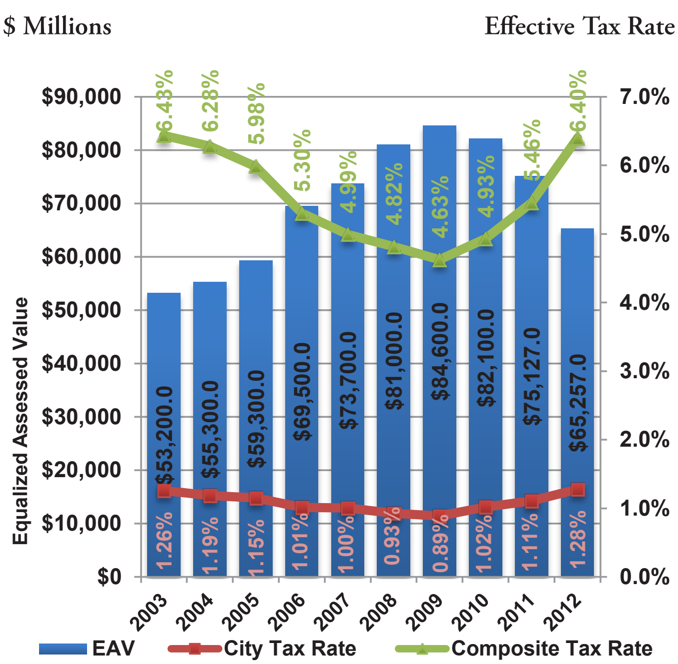
Property Tax Funds

Property taxes make up a significant portion of City revenues and are one of the most frequently discussed sources of revenue. The City's total property tax-derived revenue is made up of two basic components – the City property tax levy and tax increment financing (TIF) revenue. Revenue from the City's levy can be used for general citywide services or expenses. TIF revenue, however, must be utilized for specific types of expenses in specific areas. This section discusses each of these sources of property tax revenue and how it is used by the City.

City Property Tax Levy

The City is one of several taxing districts reflected on a Chicago resident's property tax bill. A taxing district is a unit of government with the authority to levy for property taxes. In addition to the City, examples of taxing districts with jurisdiction in Chicago and that appear on a typical property tax bill are the Metropolitan Water Reclamation District, Cook County, Chicago Public Schools, and the Chicago Park District. Currently, approximately 20 percent of a property taxpayer's total bill is allocated to the City.

EQUALIZED ASSESSED VALUE AND TAX RATES



Cook County administers and collects property taxes on behalf of all taxing districts in the amount of each district's levy. A taxing district's levy is simply the amount of property tax revenue that the district requests for the year.[15] The City's levy has remained relatively constant over the past decade, with the exception of an increase in 2008 to create a portion of the levy dedicated to the library system.

The County determines the amount billed to an individual taxpayer on behalf of a taxing district such as the City based on the taxing district's levy; the value of the property in the district (known as the aggregate equalized assessed value (EAV)), subtracting the value of any property tax exemptions and incremental EAV for property located in a TIF; and the EAV of the taxpayer's property.

The County divides the district's levy by the district's aggregate EAV in order to determine the district's tax rate, which, for the City, was 1.279 percent in 2012.

$$\text{District's Tax Rate} = \frac{\text{District's Requested Levy}}{\text{Aggregate EAV of the District}}$$

The County determines a tax rate for each district, and the sum of these tax rates for all taxing districts is the composite property tax rate, or the total rate that a taxpayer sees on their property tax bill. The 2012 composite property tax rate for a taxpayer in Chicago was 6.396 percent.

This composite tax rate is applied to the EAV of each taxpayer's property, and the result is the dollar amount that the taxpayer must pay in a given year.

$$\text{Composite Tax Rate} \times \text{EAV of Taxpayer's Property} = \text{Amount of Property Taxes Owed}$$

Property values are reassessed by the County every three years, based on three prior years of sales. The City's aggregate EAV, which reflects the taxable value of all property located in the city limits, grew steadily for much of the past decade, but declined in recent years due to the recession. As the City's levy remained relatively constant and the aggregate EAV of property in the city limits increased during the early to mid-2000s, the property tax rate for Chicago taxpayers steadily decreased. The City tax rate was 1.452 percent, with a 7.277 percent composite rate, in 2002. By 2009,

[15] For many districts, this levy amount is limited by State legislation that places a cap on the amount that the district can request and extend. The City, however, is not subject to this State-mandated cap on the amount that it levies. Property tax bills are sent and paid one year in arrears, so the bills received by taxpayers in 2013 reflect 2012 tax rates and valuations.

the City rate had decreased by almost one-third to 0.986 percent, with the composite rate down to 4.627 percent. However, in recent years, EAVs have reflected the decline in the real estate market brought on by the recession. In 2010, the City's EAV declined 3 percent from 2009 levels, and in 2011, the EAV decreased by an additional 8.5 percent from 2010 levels. Due to the timing of reassessment by the County, it is likely that EAVs will decline further as valuations continue to reflect recessionary sales. As the EAV decreases and the levy stays relatively constant, the City tax rate increases. This is reflected in the 2012 City property tax rate and the composite tax rate of 1.279 percent and 6.396 percent, respectively, which are still significantly below the 2002 rate but up from more recent years.

None of this fluctuation in EAVs and tax rates, however, has an impact on the amount of property tax revenue the City receives in a given year. The City's property tax revenue is simply the amount that it requests in each year's levy.

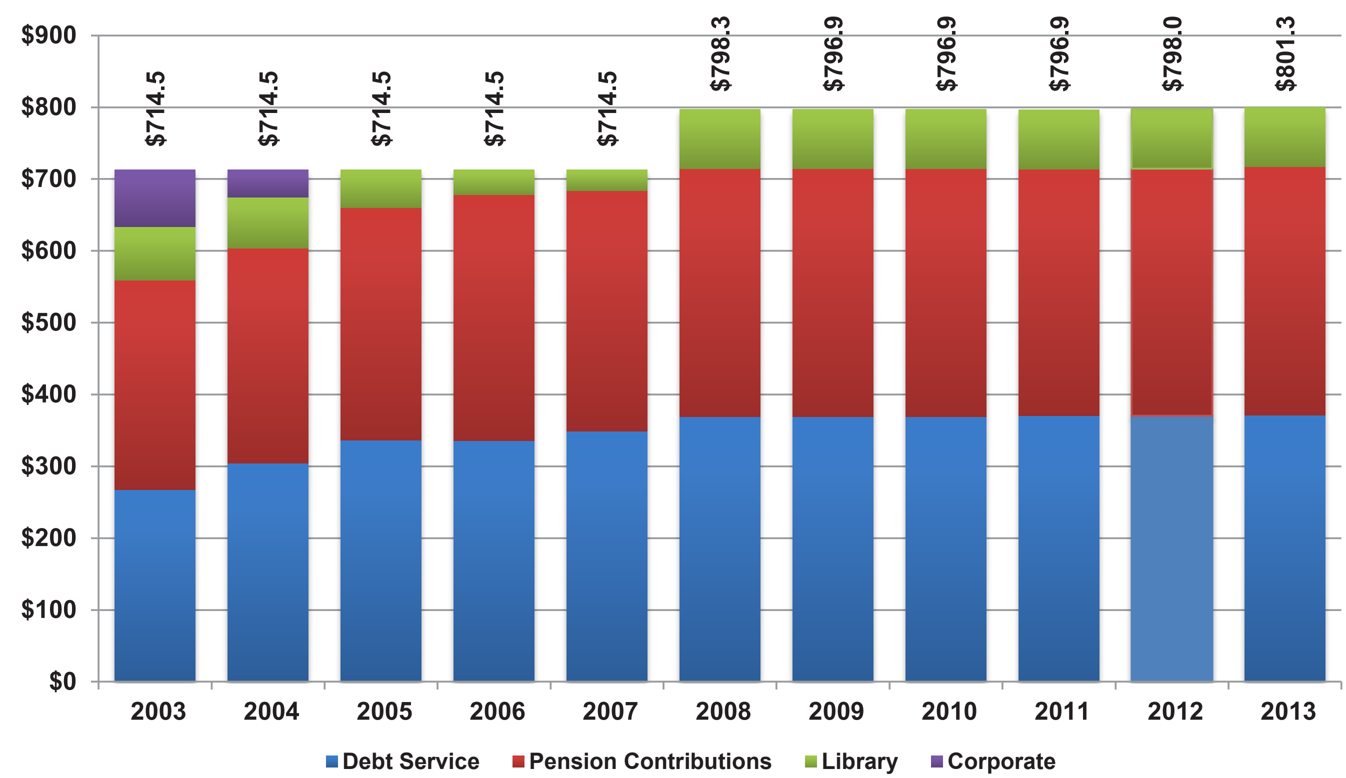
Use of City Levy Revenues

The City levy is divided into two components – a portion used for general City purposes and a portion specifically dedicated to fund the Chicago Public Libraries.[16] In 2008, the library portion of the levy was set at $83.4 million. The use of the library portion of the City levy is discussed in greater detail in the Special Revenue Fund section of this document.

The revenue from the City levy that is not allocated to the library system has been utilized primarily to pay the City's debt service and employee pension contributions. In the past, surplus property tax revenue was transferred to the City's corporate fund to support City services and activities. As the City's debt service and pension expenses have grown, all of the City's property tax revenues are being used to cover these payments. No property tax revenue has flowed into the corporate fund in almost 10 years.

PROPERTY TAX REVENUE AND ALLOCATION

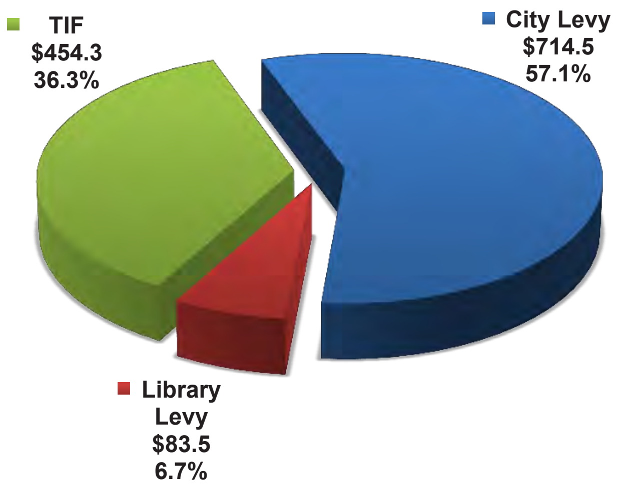
$ Millions



[16] An additional $37 million portion of the City's levy is dedicated to the payment of bonds issued in 1999 and 2007 by the City on behalf of the City Colleges of Chicago. This amount is sometimes discussed as a part of the overall City property tax levy. However, because the City Colleges function as a separate governmental unit and do not receive any additional funding or subsidies from the corporate fund, this portion of the City's levy is not discussed in detail here.

2012 PROPERTY TAX REVENUE

$ Millions



The chart on the prior page shows the way in which property tax revenues were appropriated from 2003 through 2013. In each of those years, and to an increasing extent each year, a portion of the pension contributions were paid with PPRT revenue and a portion of the long-term debt service was covered using other resources. Going forward, the total amount of long-term general obligation debt service and employee pension contributions will continue to exceed the current City levy, and other revenue sources must be redirected to make up this differential. The City's pension and debt obligations are discussed in greater detail in the last two sections of this document.

TIF Revenue

Discussion of the City's property tax revenue has historically focused on the City levy; however, substantial amounts of property-tax-derived revenue also come through the City's tax increment financing (TIF) program. Chicago's TIF program began in 1984 with the goal of promoting business, industrial, and residential development in areas of the City that struggled to attract or retain housing, jobs, or commercial activity. The program is governed by a state law that allows municipalities to capture property tax revenues derived from the EAV growth above the base EAV that existed before an area was designated as a TIF district, and use that money (the tax increment) for community projects, public improvements, and incentives to attract private investment to the area. The baseline EAV at the time the TIF district was designated is still a part of the tax base for the purposes of the levy, but revenue from the incremental EAV beyond that baseline must be reinvested into the area and cannot be used for other general City purposes. The intention is that the effective use of tax increment helps expand the tax base, thus increasing the amount of tax increment generated in the district for re-investment within the district, ultimately increasing the property tax base after the TIF district has ended.

When a TIF district expires or terminates, the incremental EAV of the district becomes a part of the aggregate EAV that is available to all taxing districts. Taxing districts, including the City, have the ability to recover their portion of the revenue from the incremental EAV by adding it to their levy following a TIF district's dissolution. By doing so, the City increases the resources available to support citywide expenses without increasing the tax burden on Chicago residents. This practice, which was recommended in the report of the TIF reform panel, yielded $1.1 million in 2012 from three TIF districts. In 2013, the City recovered a portion of the incremental EAV from the termination or expiration of 12 TIF districts, totaling $3.3 million, and will utilize these property tax dollars to fund pension obligations and City services.

Historic and anticipated TIF revenue and the use of these funds, as well as the City's ongoing TIF reform initiatives, are discussed in detail in the TIF section of this document.

City Workforce

Many of the services that the City provides – from police protection to fire fighting to street paving to library assistance – are made possible by City employees. The City workforce is made up of front-line service providers like police and librarians, as well as employees providing the logistical, planning, and administrative support necessary to deliver those essential services. The costs associated with this workforce comprise the majority of the City's expenses.

Personnel-related expenditures, including salaries and wages, health care, overtime pay, workers' compensation, and unemployment compensation, vary from fund to fund with a Citywide average of 78 percent of total expenditures across all local funds over the past 10 years. Historically, this proportion has been higher in the corporate fund, averaging of 85 percent of corporate fund expenditures. Salaries and wages alone have historically accounted for an average of 67 percent of City expenses each year, with employee healthcare accounting for an average of 9 percent each year.

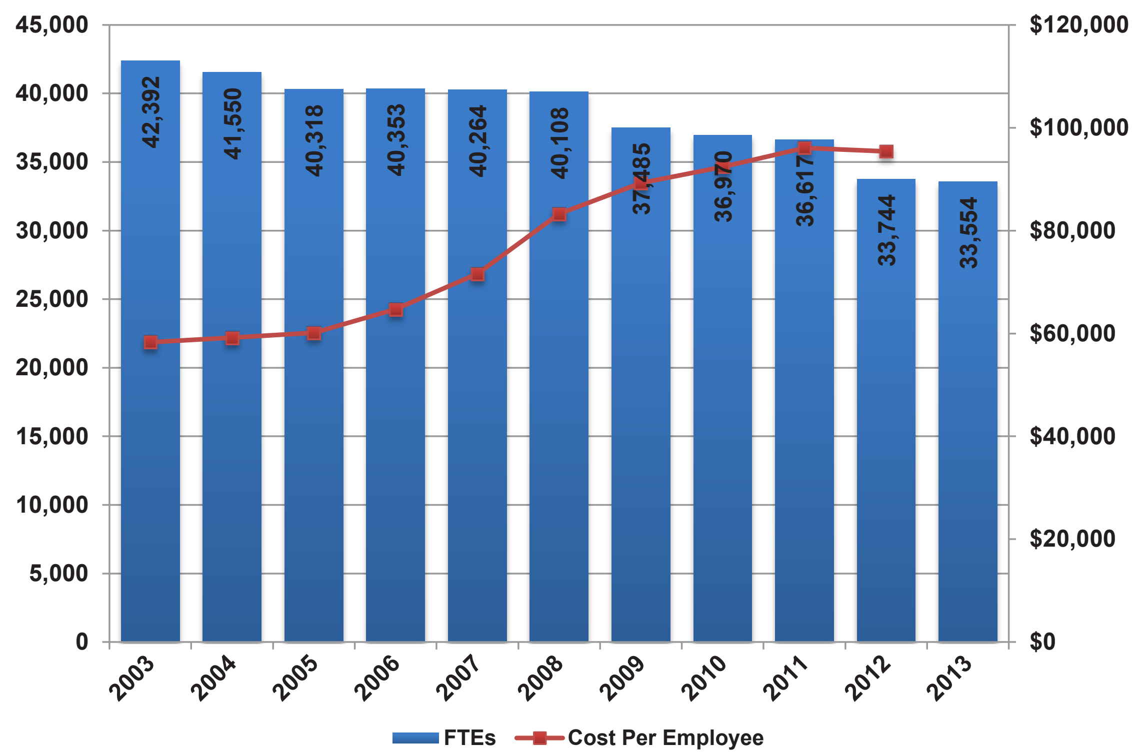
The public safety departments account for the largest portion of personnel expenses on the corporate fund, and have not experienced reductions to the extent that other segments of the workforce have. From 2003 through 2012, public safety salaries and wages accounted for an average of 77 percent of total corporate fund salary and wage expenses, with that percentage increasing from 74 percent in 2003 to 80 percent in 2012. Today, public safety positions make up 61 percent of the City workforce, up from 54 percent in 2003.

The City has steadily decreased its workforce across all funds from 40,506 positions (42,392 full-time equivalents, or FTEs) in 2003 to 32,420 positions (33,554 FTEs) in 2013, a decrease of approximately 20 percent, or 8,086 positions (8,837 FTEs). However, despite this reduction in the workforce, the City's total personnel costs increased by 15 percent between 2003 and 2012, with salary and wage expenses increasing by 11 percent and healthcare costs by 38 percent. The City's average annual cost per employee increased from $58,299 in 2003 to $95,406 in 2012.

Union Workforce

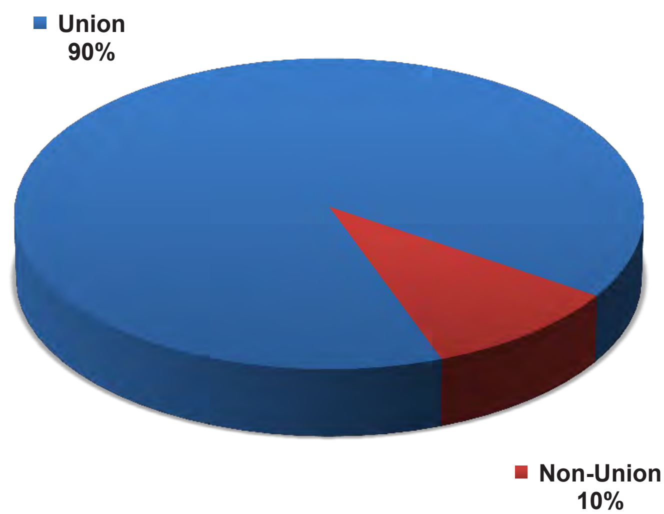
The increase in personnel expenses over the past decade has been due primarily to salary increases resulting from contractual obligations under collective bargaining agreements with the unions that represent the vast majority of City employees. Today, 90 percent of City positions are

CITY WORKFORCE AND COST PER EMPLOYEE



represented by a union, up from 87 percent in 2003. As the overall number of City positions has decreased, the relative proportion of union positions has increased. Since 2003, the number of non-union positions, which are primarily management positions, has been reduced by 40 percent, from 5,142 to 3,103 (5,397 to 3,355 FTEs), while the number of union positions has been reduced by 17 percent, from 35,364 to 29,317 (36,994 to 30,199 FTEs).

2013 CITY WORKFORCE, UNION VS. NON-UNION



The City is party to collective bargaining agreements with more than 40 different unions. The two bargaining units representing the largest number of City positions are the Fraternal Order of Police and the Chicago Firefighters Union, currently with 16,043 combined sworn public safety positions. When police captains, lieutenants, and sergeants are included, the number of unionized public safety positions comes to 17,482.

The next largest group of positions is associated with the Coalition of Union Public Employees (COUPE), which currently represents 6,260 trades positions (6,780 FTEs). The American Federation of State, County, and Municipal Employees (AFSCME) is the fourth largest group, representing 3,485 positions (3,630 FTEs) that provide administrative support for City government and services, and the Service Employees International Union (SEIU) currently represents 1,901 public safety civilian positions (2105, FTEs), such as traffic control aides, detention aides, and police communication operators.

The collective bargaining agreements with each of these major unions include regular salary increases, resulting in higher personnel costs each year. During the period from 2003 through 2006, collective bargaining agreements with COUPE and AFSCME provided average salary increases of more than 3 percent each year, and those with the police and fire unions provided average salary increases of more than 4 percent each year.[17] The most recent collective bargaining agreements with the police and fire unions included a 10 percent salary increase between 2007 and 2012. Those with COUPE and AFSCME included a 16 percent increase between 2007 and 2012. The current SEIU agreement, which was finalized in August of 2012, includes a 6 percent increase between 2011 and 2016. These increases are in addition to the raises based on time in service that most employees receive. Historically, non-union positions received salary increases equal to those negotiated for civilian (non-sworn) positions; however, since 2009, non-represented positions have not received any such increases.

A number of the City's collective bargaining agreements are currently pending negotiation, including those with the police and fire unions; police captains, lieutenants, and sergeants; AFSCME; and the unions representing City nurses.

Healthcare Costs

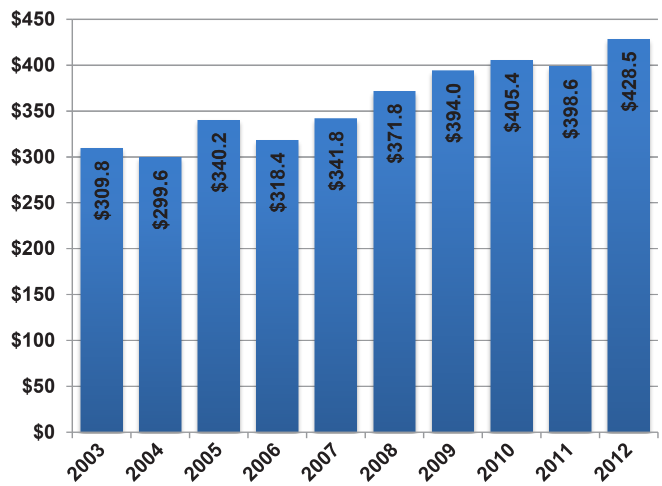
A significant share of the City's budget is spent on healthcare coverage, including medical, dental, and vision care, for current City employees and City retirees. Specifically, this pool of covered lives includes City employees, City retirees, and the spouses and dependents of both. Like many other large cities and private sector companies, the City self-funds its health plans, meaning that it generally pays for covered healthcare services rather than pay premiums to a third-party insurer. Due to the large number of covered lives, it is generally more cost-effective for the City to self-fund such expenses.

[17] These salary increases affect negotiated rate positions only; wages for positions paid on an hourly basis increase pursuant to the prevailing rate.

Between 2003 and 2012, the City's healthcare costs rose from $309.8 million to $428.5 million, with only two exceptions to the overall pattern of growth shown in the chart below. The decrease in costs from 2005 to 2006 was due in large part to significant plan design changes, including adjustments to the formula for employee healthcare contributions, and the slight decrease in 2011 was in part a result of savings generated through initiatives implemented during the second half of 2011 and various insurance premium reconciliations.

CITYWIDE HEALTHCARE COSTS

$ Millions



The significant net increase over the past decade can be attributed to several main factors – the makeup of the City's workforce and retiree population, the increased utilization of prescriptions and health care services, the rising cost of healthcare services, and changing state and federal coverage requirements.

Between 2003 and 2012, the aggregate number of covered lives under City healthcare plans decreased by more than 13 percent, from 134,626 to 116,114. However, during that same time period, the number of active City employees enrolled decreased by approximately 18 percent while the number of retirees enrolled increased by approximately 15 percent. With this change in the makeup of covered lives came an increase in the average age of beneficiaries of City healthcare plans, from 40 in 2003 to 47 in 2012, and older individuals generally require larger annual healthcare expenditures. In addition, as life expectancies increase, the duration of coverage lengthens, further increasing the City's healthcare expenditures.

National industry trends have also driven the City's costs upward. The per capita cost of healthcare in the U.S. has risen significantly since 2003, and as more specialty medications and more expensive technologies are utilized with greater frequency, costs increase. A thorough analysis of industry-wide trends is beyond the scope of this report, but the City's increasing healthcare expenditures clearly correspond with the growing price of healthcare nationwide. Between 2003 and 2012, the City's healthcare costs increased by 38 percent, only slightly above the 34 percent increase in the consumer price index for medical care during the same years.

The healthcare industry is currently in a state of significant flux; however, the City expects that the trends seen in recent years will continue into the future, as the demographics of beneficiaries continue to shift and the per-employee cost of providing healthcare continues to increase. In order to contain these costs in the long-term and improve the overall health and well-being of its workforce, in 2012, the City implemented a wellness program for employees and their families.

The City's wellness program provides a wide range of services and utilizes individualized assessments and screenings to ensure that participants are engaged in programs most appropriate for their needs. By encouraging employees and their families to proactively address areas of immediate concern, such as hypertension, high cholesterol, smoking, and diabetes, the City aims to reduce the healthcare costs that such conditions often necessitate if left untreated. In the first year of implementation, 84 percent of those eligible to participate, enrolled in the program, making it the largest municipal wellness program in the country.

Overtime Management

Since 2003, the City's public safety, infrastructure, and public service enterprise departments have accounted for 96 percent of Citywide overtime expenditures. Between 2007 and 2011, the City decreased its overtime expenditures across all funds by 27 percent. Multiple factors facilitated this decrease, with the primary driver being the 2009 agreement with the COUPE unions, under which the unions agreed to earn compensatory time instead of being paid for overtime hours. The COUPE agreement expired in mid-2011. In 2012, total overtime expenses for the City increased from 2011 levels. An increase was seen in infrastructure services overtime, attributable in part to the expiration of the COUPE agreement, and an increase was also seen in the public safety departments.

The City continues to strategically manage the usage of overtime. In making decisions surrounding overtime management, the City evaluates the cost of utilizing overtime to provide critical City services in relation to the cost of hiring additional employees. Because there are significant incremental costs associated with hiring new employees, including healthcare benefits and pension contributions, in many cases utilizing overtime hours is a preferable alternative because it is more cost effective. Decisions are made based on the seasonality, type, and long-term consistency of the work that must be completed.

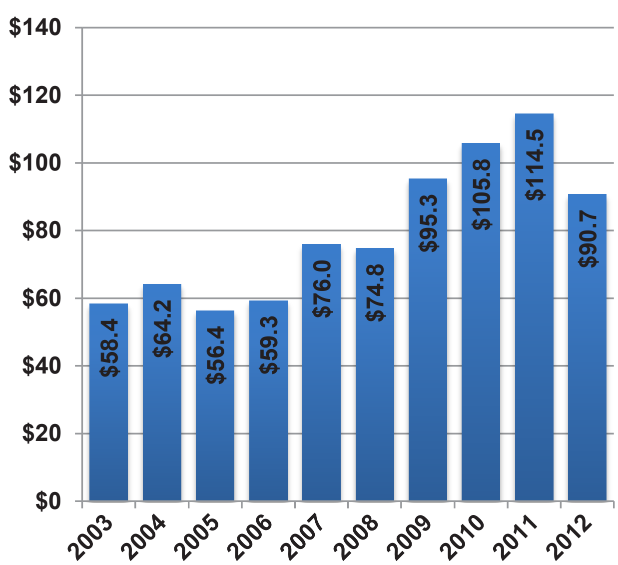
Workers' Compensation

The City's workers' compensation costs rose from $58.4 million to $114.5 million between 2003 and 2011, and then decreased to $90.7 million in 2012. These costs include medical expenses, payments for lost time, and the costs of case resolution associated with employees who are injured while on duty working for the City. A number of factors contributed to the growth in workers' compensation costs over the past decade. As discussed above, medical costs nationwide have risen significantly over the past decade, increasing the cost of treating injured employees. In addition, salaries and wages have increased, driving up the price of lost time that must be compensated by the City. Furthermore, due to the downturn in the economy, employees who cannot return to their original position due to their injuries have been less able to find other employment, increasing the length of lost time that must be compensated and thus the total cost of such payments.

Over the past year, the City has identified a number of opportunities to reform the policies and practices surrounding workers' compensation to reduce these costs. The City has re-assessed its medical billing review process, worked to increase investigations to prevent fraud and implement successful return-to-work programs for injured employees, and pursued more active case management, all of which contributed to decreased costs in 2012.

CITYWIDE WORKERS' COMPENSATION

$ Millions



Annual Financial Analysis
2013

Financial Forecast

Financial Forecast

INTRODUCTION

This section includes a discussion of the City's 2013 year-end estimates, 2014 preliminary budget projections, and three revenue and expenditure scenarios for the years 2015 and 2016 – a base outlook, a positive outlook, and a negative outlook. These projections are based on historical revenue and expenditure data, current economic trends and conditions, and other known factors that are anticipated to have an impact on the City's finances. The purpose of this analysis is to ensure that the 2014 budget is formulated with a clear understanding of the City's current financial state and an informed view of future conditions and the long-term fiscal consequences of today's decisions.

This forecast focuses primarily on the corporate fund, as this fund not only accounts for most of the basic services provided by the City, but also has historically experienced the largest disparity between revenues and expenditures. A summary of the projections for the City's major special revenue and enterprise funds is included at the end of this section.

GENERAL ECONOMIC CONSIDERATIONS

Both nationally and locally, key economic indicators suggest moderate yet sustained growth in the coming year. The national economy continues to expand, led by improving home prices, increased consumer spending, and a stronger stock market. Through the first quarter, home prices rose at their fastest pace in seven years, and retail sales through June were up 4 percent from 2012. U.S. GDP, a measure of total domestic economic production, continued to improve with a 1.8 percent rise relative to the final quarter of 2012. The Consumer Sentiment Index rose to 84.1 in June and has been higher in the past two months than at any time since 2007. All of these signs of progress occurred even as federal payroll taxes rose and unemployment rates remained high.

Locally, economic trends have mirrored many of the national patterns. During the first six months of 2013, existing home sales were up 21 percent and median home prices up 15 percent over the same period in 2012. In addition, the commercial real estate market has remained strong, evidenced by the sale of high-priced buildings in the downtown area. Local consumer spending has increased, and tourism and the growing service industry continue to be a highlight of the local economy. Last year, the number of visitors to Chicago rose by more than 6 percent from 2011, nearing the 2007 record high of 46.3 million. During the first six months of 2013, hotel occupancy rates were up 2 percent from 2012 and average daily room rates were up 5 percent from 2012.

These broader economic factors are accounted for to the extent possible in the following projections. The 2014 projections and the base outlook for 2015-2016 present what is currently viewed as the most likely scenario. The positive and negative outlooks for 2015-2016 provide insight into how changes in the economy and other related factors might affect the City's finances over the next three years.

2013 CORPORATE FUND YEAR-END ESTIMATES

2013 Year-End Revenues

Total corporate fund resources for 2013 are estimated to end the year at $3.22 billion. This includes $177.0 million carried over from prior years, which was included in the 2013 budget and is attributable in part to the effective controls, cuts, and initiatives implemented during the course of 2011 and 2012.

Corporate fund revenues are expected to finish the year approximately 1.8 percent, or $56 million, above 2013 budgeted revenues. These year-end estimates reflect increases in many of the City's economically sensitive and tourism-driven revenues, as well as the anticipated receipt of an additional monthly income tax distribution from the State as they catch up from delays in payments seen in recent years. Major categories of revenue and trends are discussed below, and year-end estimates for each individual revenue source are discussed in the Financial History Review section of this document.

Utility tax revenues are expected to come in just above budget for the year as natural gas prices and usage rebound from 2012 lows, offsetting the continued decline in telecommunications tax revenue due in part to changing consumer preferences and industry trends. Transportation-related taxes, including the garage tax and vehicle fuel tax, are similarly tied to prices and consumer patterns, as people tend to drive and park less when gas prices are high. Revenues from these taxes are anticipated to finish 2013 at budget, as fuel prices have dropped from 2012 levels but remain relatively high.

The City's economically-sensitive taxes are expected to finish 2013 strong across the board. Real property transfer tax revenues are expected to come in more than 25 percent above budget for the year as the commercial real estate market continues to perform well and the housing market shows significant improvement over 2012 in both sales and prices. Growth is being projected for the City's sales tax and lease tax revenues as well, as consumer confidence reached a five-year high in the second quarter of 2013; these consumer-driven taxes are expected to outperform budgeted expectations by 2 percent and 11 percent, respectively. Both corporate and individual income tax revenues are expected to end 2013 significantly above budget, due to the anticipated additional monthly distribution in back-payment from the State, coupled with the stabilizing economy and certain one-time collections associated with businesses and individuals selling assets or receiving dividends or bonuses in 2012 in anticipation of higher federal tax rates.

Increasing tourism and business travel are expected to push hotel tax revenue above projections of growth for the year, building on gains seen throughout 2012. Tourism is also expected to bolster amusement tax revenues, which are estimated to end the year just over budget, with decreases in both ticket sales and prices by the Cubs and Sox being offset by playoff appearances by the Bulls and Blackhawks. Other recreation tax revenues are expected to finish the year slightly above budget, despite the decline in cigarette tax revenues that is anticipated due to the increases in the State and County cigarette tax rates.

The City's non-tax revenues also reflect the economic upturn, with fee revenue from business licenses, building permits, and other licenses and permits all anticipated to end 2013 above budgeted expectations. Income from the lease or rental of City-owned property is expected to come in similarly strong for the year. Revenues from fines, forfeitures, and penalties are expected to come in just below budget for the year.

2013 Year-End Expenditures

Corporate fund expenditures are currently expected to end the year at $3.22 billion, over 2013 budgeted expenditures but still within anticipated corporate fund resources for the year. These estimates are based on year-to-date spending, incorporating payroll trends, market pricing for relevant commodities, and any known changes or events that have or are anticipated to occur during the remainder of 2013.

Decisions are made throughout the course of the year in response to new or changing needs and citywide priorities. The anticipated overage is attributable to the decision to increase police hours on the streets during the course of 2013, resulting in increased overtime expenses for the Police Department. Aside from this variance, 2013 spending has been largely in line with budgeted expectations for the year.

It is currently projected that the City's corporate fund will finish the year with revenues and expenditures approximately even. However, numerous factors impact the City's revenues and expenditures, and these estimates may change as the year progresses. The City will continue to closely monitor its

2013-2014 PROJECTED EXPENDITURES AND REVENUES

$ Millions

	2013 YE Est.	2014 Projected
Revenue	$3,217.7	$3,016.9
Expenditure	$ 3,217.0	$3,355.6
Budget Surplus/(Deficit)	**$0.7**	**($338.7)**

revenues and expenses, and updates will be published in the City's quarterly budget reports.

2014 CORPORATE FUND PROJECTIONS

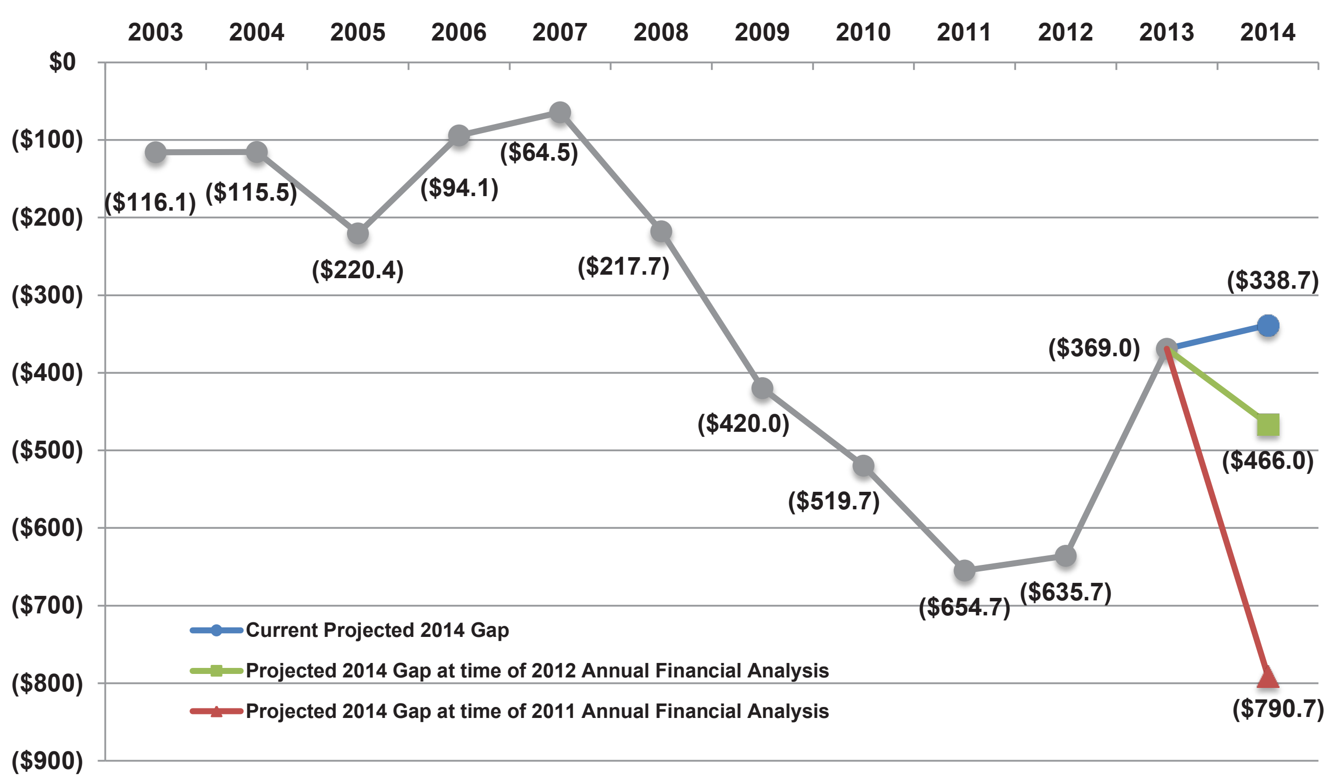
The difference between revenues and expenditures anticipated by the City in its preliminary corporate fund budget estimates each year is commonly referred to as the 'gap'. Based on current revenue and expenditure projections, the City estimates a 2014 corporate fund gap of $338.7 million. This projected gap is much smaller than those seen during the recession years and substantially less than was projected for 2014 in the City's 2011 and 2012 Annual Financial Analysis, but still a significant shortfall. The decreasing size of the gap is the result of the recovering economy's impact on revenues, as well as the real and lasting changes made as part of the past two budgets, such as the introduction of managed competitions to guarantee the best price for the highest quality City services, the transition to grid-based garbage collection, the review and renegotiation of major contractual costs, and the implementation of a wellness program for City employees and other reforms that have reduced the City's healthcare costs. However, the persistent existence of a substantial corporate fund shortfall makes clear that many of the challenges underlying the long-standing structural deficit remain.

Corporate Fund Revenues

Corporate fund resources are projected to decrease almost 6 percent from the 2013 year-end estimate of $3.22 billion to $3.02 billion in 2014. A portion of the decrease in total corporate fund resources between 2013 and 2014 reflects the difference in the amount carried over from prior years; corporate fund resources for 2013 include $177.0 million carried over from prior years, while 2014 projections assume that the City will not carry over any balance from 2013 into 2014. In addition, the employers' expense tax will be completely eliminated as of January 1, 2014, fulfilling the Mayor's pledge to phase out the tax as a key component of encouraging business development and job creation in Chicago. For most other revenue sources, 2014 estimates reflect the continuation of trends seen in 2013.

CORPORATE FUND PRELIMINARY GAP

$ Millions



Financial Forecast

Overall utility tax revenues are expected to stay flat with 2013 levels in 2014, as electricity tax revenues increase modestly and cable television tax revenues increase more rapidly with industry expansion. Projections anticipate that natural gas tax revenues will experience some growth as prices continue to stabilize. Telecommunications tax revenues are expected to decrease from 2013 levels as the number of landlines decrease at a faster rate than the number of wireless accounts increase and as the City completes the payment of certain credits to telecom service providers for taxes charged on services that were later determined to be non-taxable.

Garage tax revenues are expected to experience moderate growth in 2014 even as fuel prices remain high, based on recent upticks in the number of parkers in city garages. Vehicle fuel tax revenues, however, are impacted more directly by the price of fuel and are expected to decline slightly in 2014 with decreased consumer usage.

Many of the City's largest and most economically sensitive sources of revenue have now returned to pre-recession levels, and a conservative approach to increases is taken in the 2014 projections in line with the assumption that the economy will continue to experience moderate growth. Real property transfer tax revenues are projected to increase again in 2014 as the housing market continues to improve, and growth on a strong 2013 base is expected for both sales and lease tax revenues, reflecting increasing consumer confidence. The City anticipates that monthly income tax collections will increase slightly in 2014 with the economy, but total 2014 income tax revenues will be below 2013 levels, because of the extra monthly distribution expected in 2013 due to prior year payment delays.

Amusement and hotel tax revenues are expected to grow again in 2014, reflecting increases in tourism and business travel, with a number of new hotels slated to open and a strong convention calendar. Other recreation tax revenue trends seen in 2013 are expected to carry into 2014, with moderate increases in liquor and non-alcoholic beverage sales offsetting declines in cigarette tax revenues.

REVENUE CORPORATE FUND, $ Millions	2013 YE Est.	2014 Projected
Tax Revenue		
Utility Taxes and Fees	$454.8	$453.9
Transaction Taxes	263.1	270.0
Transportation Taxes	180.7	184.2
Recreation Taxes	163.4	164.3
Business Taxes	106.1	100.1
Sales and Use Taxes	572.9	588.2
Income Tax, PPRT & Other Intergovernmental	307.1	280.3
Total Tax Revenue	**2,048.1**	**2,041.0**
Non-Tax Revenue		
Licenses and Permits	127.1	130.6
Fines, Forfeitures and Penalties	324.6	349.7
Charges for Services	116.0	116.2
Municipal Parking	9.6	9.6
Leases, Rentals and Sales	23.3	20.8
Reimbursement, Interest & Other	369.6	334.2
Total Non-Tax Revenue	**970.2**	**961.1**
Proceeds and Transfers In	**22.4**	**14.8**
Total Revenue	**3,040.7**	**3,016.9**
Appropriated Prior Year Fund Balance	177.0	0.0
Total Projected Resources	**$3,217.7**	**$3,016.9**

Financial Forecast

EXPENDITURES CORPORATE FUND, $ Millions	2013 YE Est.	2014 Projected
Salaries and Wages	$2,367.3	$2,458.7
Healthcare Benefits	359.4	381.5
Worker's Compensation	61.8	65.1
Contractual Services	294.5	305.8
Commodities and Materials	24.1	24.5
Utilities	10.6	10.8
Motor Fuel	24.7	26.7
Claims, Refunds, Judgments, and Legal Fees	29.0	33.4
Miscellaneous	31.0	34.5
Transfers Out	14.6	14.6
Total Projected Expenditures	**$3,217.0**	**$3,355.6**

The City's non-tax revenues are expected to hold relatively even with 2013 levels. Revenue from business license fees will likely drop slightly due to the two-year renewal cycle for licenses, while building permit-related revenue is expected to increase as the number of construction and improvement projects pick up with the improving real estate market. Revenue from fines, forfeitures, and penalties is projected to increase with the full implementation of automated speed enforcement in select locations near parks and schools throughout the city.

Corporate Fund Expenditures

2014 expenditure projections grow over 2013 anticipated year-end expenditures by approximately $139 million, or 4 percent, to $3.36 billion. These projections are based on 2013 year-end estimates, adjusted for anticipated changes such as salaries and wages governed by collective bargaining agreements, increased fuel expenses to accommodate the potential continued increase in gas prices, and costs associated with the coming year's election cycle and the first full year of citywide recycling.

These expenditure projections assume that no substantive changes are made to City operations or the cost of City services. No cost-savings initiatives are incorporated into these estimates. Cost-savings initiatives are being developed by the City and will be included in the 2014 budget recommendation submitted to the City Council in October.

As has been the case throughout the past decade, the bulk of the projected increase in expenses in 2014 is in personnel costs. Between 2003 and 2012, the number of employees on the corporate fund decreased by 17 percent. During that same period, however, corporate fund salary and wage expenditures increased by more than 10 percent and healthcare costs by more than 40 percent. Citywide, the average annual cost per employee when all benefits are included increased by more than 50 percent between 2003 and 2012. Reforms and controls on hiring have been implemented to reduce this growth in expenses, but these costs will continue to drive corporate fund increases in the coming years.

2015-2016 CORPORATE FUND OUTLOOKS

The following three scenarios project budget gaps for the years 2015 and 2016 for the City's corporate fund based on different revenue and expenditure outlooks. Even under optimistic projections, the City will continue to experience a sizable operating budget shortfall in these years.

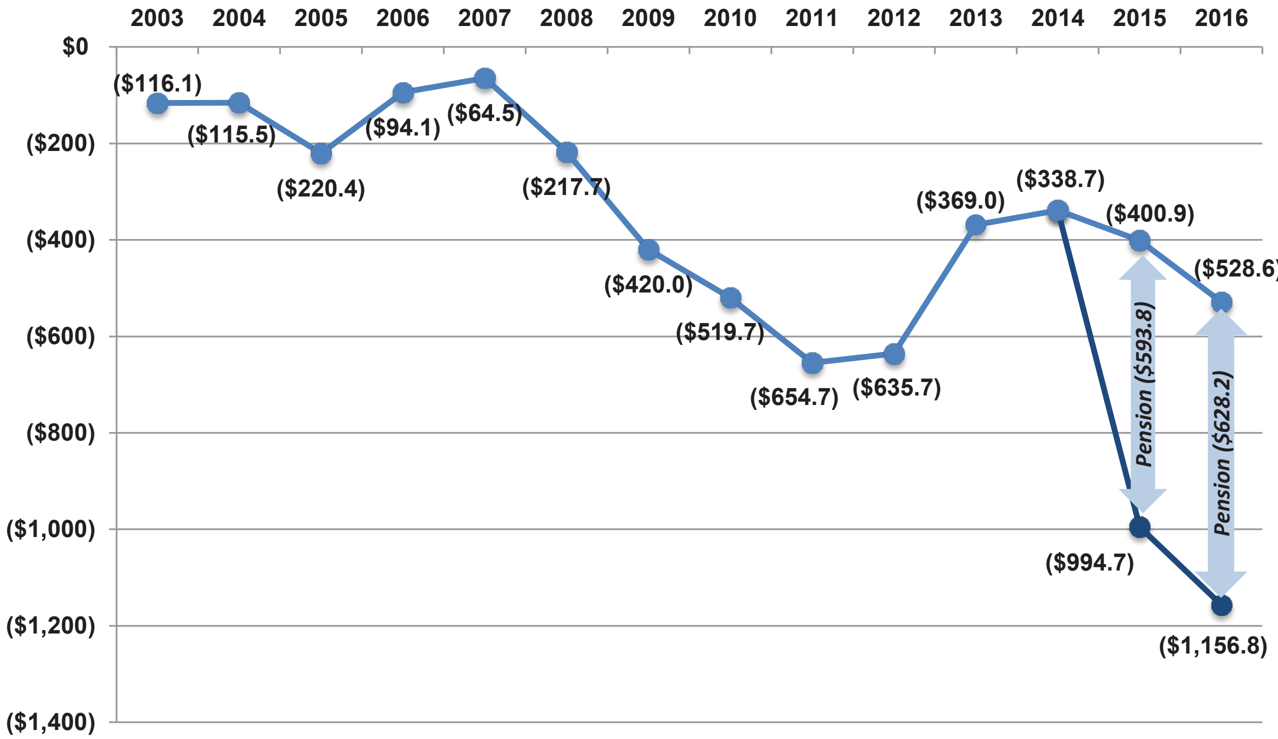
However, the recurring deficit in the City's operating funds is only a part of the full financial picture for the coming years. The City's pension obligations have been growing for many years, but will hit a turning point in 2015 that will significantly impact City finances. This issue is summarized here and discussed in more detail in the Pension section of this document.

The City's 2015 budget must accommodate a large spike in pension obligations pursuant to legislation passed by the State in 2010, under which the City will be statutorily required to contribute an actuarially-determined amount sufficient to bring the PABF and FABF to a 90 percent funding level by 2040.[18] Under this law, the

[18] P.A. 96-1495. Note also that the City's annual contribution is based on the contribution made by the employee two years prior. For example, in 2013, the City is matching (at the applicable rate) the contribution made by the employee in 2011. Because the City's contributions are paid largely with property tax proceeds, contributions are budgeted in the levy year, and paid to the funds in the following year, when property tax collections are received. Contributions are discussed here in terms of the year in which they are budgeted.

2014-16 PROJECTED GAP

$ Millions



City's statutory pension contributions will increase from an estimated $479.5 million in 2013 to approximately $1.07 billion in 2015 and $1.11 billion in 2016.

The City's property tax levy has historically been the primary revenue source for the payment of both pension and debt obligations, with the balance coming from PPRT revenue in the case of pension contributions. Beginning in 2015, these expenses will far exceed the revenue sources currently used to fund them. As a result, these costs can no longer be segregated from the City's operating budget. The forecast below incorporates pension obligations into the projected gaps for budget years 2015 and 2016.

Further, while the City's debt service obligations will experience only normal growth in line with anticipated issuances over the coming years, general obligation debt service obligations that impact the corporate fund will increase significantly from current levels in future years due to growth from anticipated issuances and the way in which the City's debt is structured.

Base Outlook

The base outlook projects corporate fund revenue growth of 2 percent over 2014 in 2015 and revenues holding even with 2015 in 2016, resulting in total corporate fund revenues of $3.08 billion in each year. These projections are based on the continuation of similar trends as presented above with respect to 2014 for most revenue sources, including utility taxes, recreation and amusement taxes, transportation-related taxes, sales and lease taxes, and most non-tax revenues. However, adjustments have been made to account for anticipated variations in some cases. A lower rate of growth in real property transfer tax revenue is expected in 2015 and 2016 than seen in 2013 and 2014, as the market stabilizes following rapid growth during the recovery years. Hotel tax revenue growth is expected to similarly moderate in 2016. In addition, following growth in 2015, income tax revenues are projected to decrease in 2016 with the scheduled expiration of the State's income tax rate increase, which was passed as a temporary measure in 2011.[19]

[19] Effective as of February of 2011, the State's personal income tax rate was increased to 5 percent from 3 percent and the corporate income tax rate was increased to 7 percent from 4.8 percent. However, municipalities did not receive a share of this increase because the State, concurrently with increasing tax rates, reduced the percentage of total income tax receipts that flow into the Local Government Distribution Fund (LGDF). Even though the City did not receive a share of the revenue from the increased tax rate, the City anticipates that its income tax revenues will decrease upon the expiration of the increase, due to the structure of distributions to the LGDF under the law following the expiration of the increase.

2015-2016 PROJECTED GAP

$ Millions

	2015	2016
Positive Outlook	($820.7)	($917.8)
Base Outlook	($994.7)	($1,156.8)
Negative Outlook	($1,255.9)	($1,532.0)

While corporate fund revenues are projected to experience a net 2 percent increase over the next two years, corporate fund operating expenditures are projected to outpace that growth at an average annual rate of 3.7 percent during the same period, to $3.48 billion in 2015 and $3.61 billion in 2016. Under this base outlook, most categories of expenditures, including contractual services, worker's compensation, motor fuel, and utilities, are assumed to grow at their long-term historical average.[20] Less predictable expenditures, such as settlement and judgment-related expenses, are held roughly flat at their historic annual average. Salary and wage and healthcare expenditures, by far the largest portion of the City's operating expenses, are projected based on the assumption that the number of full-time equivalent positions will remain approximately flat, or, put differently, that no significant hiring, layoffs, or vacancy eliminations will occur, and that salaries and wages for those positions will experience growth in line with long-term historical trends.

Under this scenario of realistic revenue projections and modest growth in expenditures, the City's corporate fund operating expenses surpass anticipated revenues by $400.9 million in 2015 and $528.6 million in 2016. When the pension costs discussed above are included, the projected gaps for 2015 and 2016 grow to $994.7 million and $1.16 billion, respectively.

Negative Outlook

The negative outlook presents a picture of City finances in the context of relatively stagnant economic conditions and incorporates the occurrence of other factors that have the potential to negatively affect City finances. Under this scenario, revenues experience no growth from projected 2014 revenues in 2015, followed by a decrease of 2 percent in 2016, resulting in total corporate fund revenues of $2.93 billion in 2015 and $2.87 billion in 2016. This assumes that utility tax revenues decline as natural gas and electricity tax revenues, which are highly sensitive to price and weather fluctuations, decrease, and as telecommunications tax revenues fall more sharply as data services replace telecommunications subscriptions. This outlook also assumes that fuel prices remain high and that conservation and fuel efficiency efforts increase, reducing transportation tax revenues accordingly. A tepid economy and cautious consumer sentiment would lead to tightened spending on retail goods, entertainment, and tourism, resulting in stagnant amusement, hotel, and sales and lease tax revenues. In addition, if unemployment remains elevated, income tax revenues would likely experience only a slight increase in 2015 and then decrease in 2016 with the expiration of the State income tax rate increase. While this outlook projects some growth in real property transfer tax revenue, it is at a slower rate, incorporating the possibility that the housing market recovery is not sustained at its current pace. Similarly, the pace of new business and building starts would slow with the economy, leaving license and permit fee revenues flat, contributing to non-tax revenues that hold relatively even with 2014 levels.

Assuming a similarly negative outlook for expenditures, in which City spending increases more rapidly over the next three years, corporate fund operating expenditures would significantly outpace revenues, growing at an annualized rate of 5.1 percent to $3.59 billion in 2015 and $3.78 billion in 2016. Under this scenario, most categories of expenditures are grown at the rate seen during their fastest period of historical growth in the past decade, which generally occurred during the pre-recession years. Certain less predictable cost categories are held at their 2003-2012 peak levels. Projected salary and wage and healthcare expenditures assume that the number of full-time equivalent positions will be held constant, as in the base case scenario, but that the cost of these positions grows at an increased rate, illustrating the potential effects of costly collective bargaining agreements or similar contingencies.

[20] Long-term historical averages and growth rates are calculated based on the years 2003 through 2012, the years for which the City has detailed and accessible expenditure data.

Under the negative outlook, the City's operating budget shortfall would grow to $662.1 million in 2015 and $903.9 million in 2016. When pension costs are included, the projected gaps for 2015 and 2016 grow to $1.26 billion and $1.53 billion, respectively.

Positive Outlook

The positive outlook assumes that the economy improves at a slightly faster pace over the next three years and that other factors shift in ways that bolster City finances. Under this scenario, revenues increase 3 percent over 2014 levels in 2015, and then by an additional 1 percent in 2016, resulting in total corporate fund revenues of $3.16 billion in 2015 and $3.19 billion in 2016. This scenario assumes that natural gas prices increase and that the decline in telecommunications tax revenue slows, contributing to stronger overall utility tax revenue growth. Under these projections, positive economic movement leads to greater growth in areas where moderate growth was predicted under the base outlook, such as recreation and amusement taxes, sales and lease taxes, and business license and building permit-related revenues. Continued strong growth in tourism and the housing market would further increase hotel and real property transfer tax revenues. In addition, as employment numbers and corporate profits improve with the economy, income tax revenues would increase; however, the expiration of the State income tax rate increase would still have a negative impact on these revenues in 2016. Non-tax revenues continue 2014 trends under this scenario, with a slight uptick in fine and penalty revenue assuming increased collection rates and a boost from additional interest earned on the City's reserve funds.

Under this positive outlook, the City is able to limit its future spending to an annual growth rate of 2.7 percent, with total corporate fund expenditures growing to $3.39 billion in 2015 and $3.48 billion in 2016. Under this outlook, expenditures for motor fuel and utilities remain flat at current levels, while spending on costs such as contractual services and commodities and materials grow very slightly over current levels. More volatile cost categories are generally held at their historical annual averages. This scenario assumes the number of full-time equivalent positions is again held constant but that salaries and wages and healthcare costs for these positions are contained and experience a lower rate of growth going forward.

Under this outlook, the City would see smaller but still substantial operating shortfalls of $226.9 million in 2015 and $289.6 million in 2016. When pension costs are included, the projected gaps for 2015 and 2016 grow to $820.7 million and $917.8 million, respectively.

Conclusion

Even under optimistic projections, the City will continue to experience a sizable annual operating budget shortfall for several years. This is in part a product of the City's long-standing structural deficit and makes evident the need to continue the difficult process of reforming government to bring operating costs in line with revenues in 2014 and beyond. However, the legacy cost of pension obligations more than doubles the size of the City's projected gap in 2015 and 2016. Substantive pension reform could significantly reduce the impact of these costs on the City's budget over the coming years; however, such action must occur at the State level, as the City's pension funds are governed by state law. The City's pension reform efforts are discussed on the final page of this document.

Financial Forecast

Outlook for Special Revenue Funds

Vehicle Tax Fund

The City anticipates that revenue from the sale of vehicle stickers will finish 2013 at $116.6 million, in line with budgeted expectations, and then increase slightly from 2013 year-end estimates to $118.9 million in 2014 as the price of stickers increases with the Consumer Price Index (CPI). City ordinance provides that the price of vehicle stickers be adjusted every other year based on the current CPI. The 2015 and 2016 projections assume that vehicle registrations hold relatively even with 2014 levels, resulting in revenues of $118.9 million in 2015 and then increasing to $121.3 million in 2016, reflecting an anticipated CPI increase. Other revenues to this fund, including impoundment fees, abandoned auto towing fees, pavement cut fees, and commercial refuse container fees, are expected to remain approximately at 2013 levels through 2016.

Motor Fuel Tax Fund

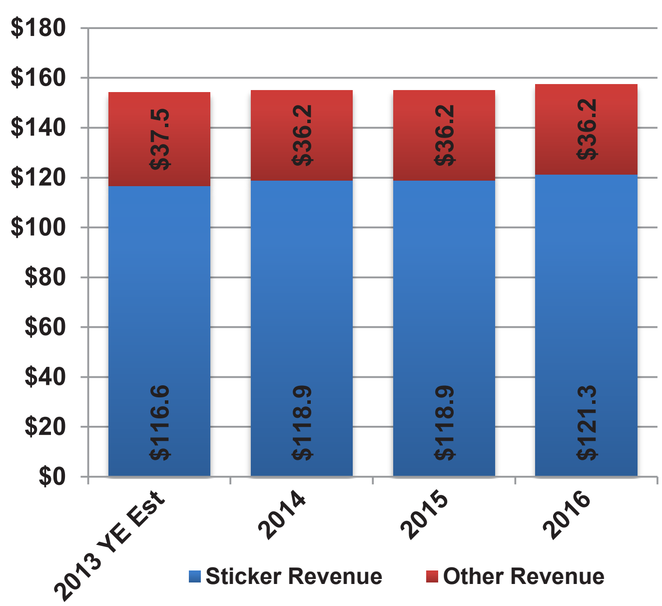
It is estimated that the City's revenues from motor fuel taxes will end 2013 at $63.7 million, in line with budgeted levels but a 3 percent decrease from 2012 motor fuel tax revenues. The anticipated decrease is due to the continuation of trends seen in recent years as increases in the price of fuel have affected consumer sales and fuel efficient vehicles become more common. Projections for the next three years assume that these factors will continue to drive declines in fuel usage and that motor fuel tax revenues will decrease accordingly, dropping to $56.4 million by 2016.

In addition, the State's "Illinois Jobs Now!" program is scheduled to end after 2014. Funds received by the City through this program have flowed into the motor fuel tax fund since 2010, providing approximately $12.5 million each year. The fund's overall revenues are expected to decrease in 2015 as a result of the end of this program.

In 2013, the City issued a new series of motor fuel tax revenue bonds to the federal government at a low interest rate through the U.S. Department of Transportation's Transportation Infrastructure Finance Innovation Act (TIFIA) program to fund the expansion of the Chicago Riverwalk, which is discussed in more detail in the Capital Investment section of this document. Beginning in 2014, in addition to motor fuel tax revenue, revenue from fees charged to tour boat operators in the city and other revenues related to the new Riverwalk will flow into the motor fuel tax fund and will secure the City's motor fuel tax revenue bonds.

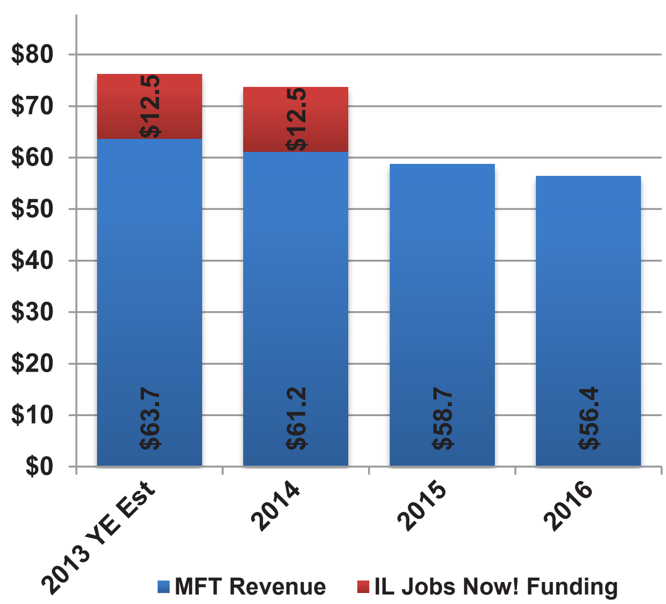
PROJECTED VEHICLE TAX FUND REVENUES

$ Millions



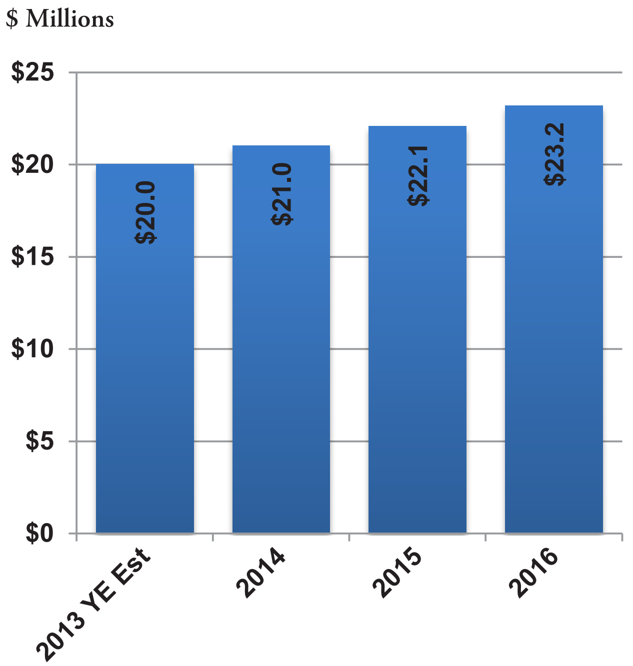
PROJECTED MOTOR FUEL TAX REVENUES

$ Millions

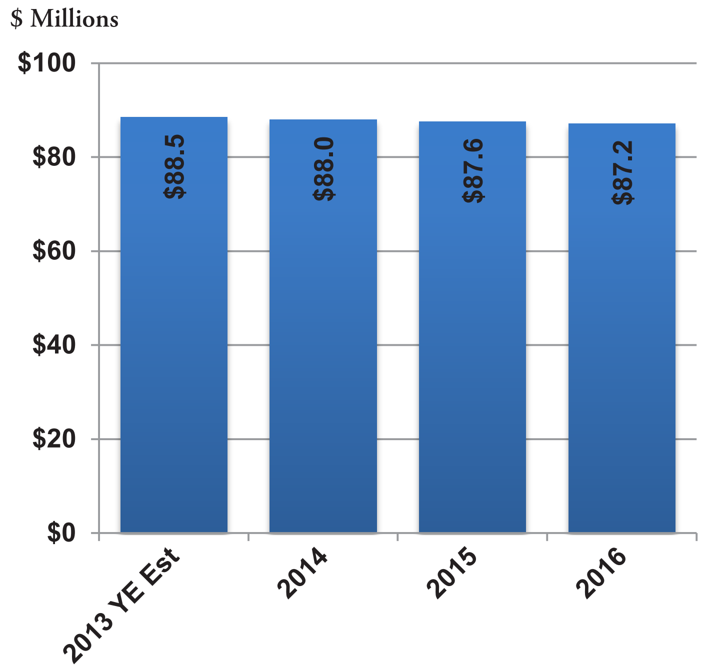


Financial Forecast

PROJECTED HOTEL TAX REVENUE



PROJECTED EMERGENCY COMMUNICATIONS SURCHARGE REVENUE



Special Events and Hotel Operators' Occupation Tax Fund

Tourism, convention, and business travel to Chicago has grown consistently over the past two years, and hotel tax revenues to this fund are expected to end the year 4 percent above budgeted expectations and 6 percent above 2012 revenues, at $20.0 million. Industry forecasts predict that this growth will continue into the coming years, with revenue per available room increasing by 6 to 10 percent each year, and hotel occupancy rates increasing through 2016. Based on these industry estimates and a strong local convention calendar, the City anticipates that hotel tax revenues will experience steady growth over the next three years, increasing the resources available to fund cultural and recreational activities in the city.

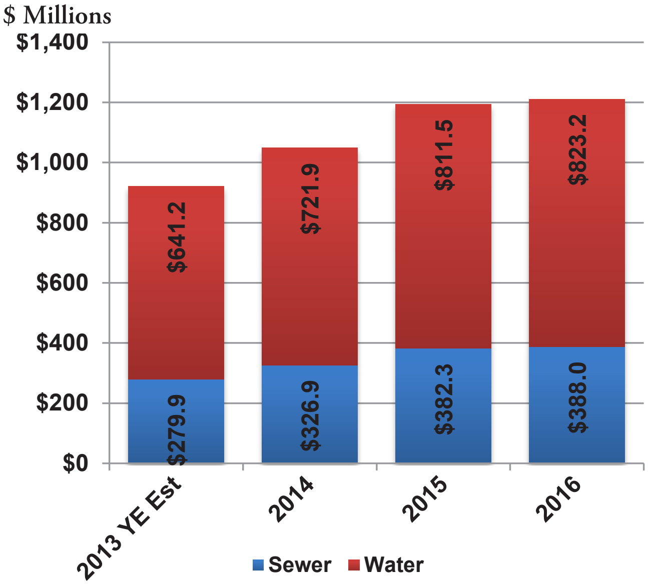
Emergency Communications Funds

The City estimates that total revenue to this fund will finish 2013 at $88.5 million, just slightly below budgeted levels for the year. Revenues from the emergency telephone system surcharge are impacted by the same factors that affect all of the City's telecommunications-related revenue sources, and it is anticipated that this fund's revenues will decline slightly each year through 2016 as the number of landlines decreases more rapidly than the number of wireless accounts increases.

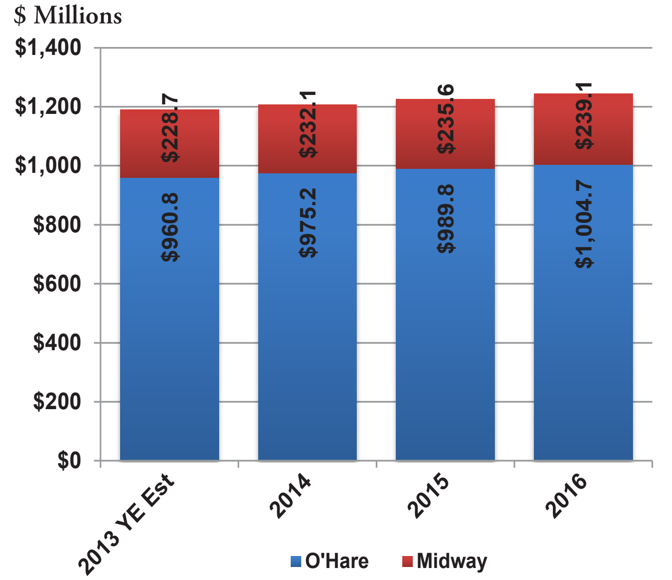
These funds are used for 911-related expenses of the OEMC, including paying debt service on bonds issued to construct the City's 911 call center. To the extent these expenses outpace revenues from the surcharge, costs will be covered with corporate funding.

Financial Forecast

PROJECTED WATER AND SEWER FUND RESOURCES



PROJECTED AVIATION FUND RESOURCES



Outlook for Enterprise Funds

Water and Sewer Funds

Revenues to the water and sewer funds are expected to increase over the next three years in line with the rate increase enacted as part of the 2012 budget. The repairs and upgrades funded with the revenue from these rate increases are discussed in the Capital Investment section of this document. These three-year projections also account for anticipated population changes, as well as the likelihood of increased conservation efforts and meter installations over the coming years.

Aviation Funds

The 2014 estimates for the O'Hare and Midway Airport funds anticipate that revenues, which are set at a level necessary to pay debt service and support the operations of the airports, will increase from 2013 levels by approximately 2 percent to $975.2 million and $232.1 million, respectively. The City projects that similar growth will continue into 2015 and 2016 as the airports move forward with capital projects and other improvements necessary to accommodate increased tourism and business travel.

Annual Financial Analysis 2013

Long-Term Asset Lease And Reserve Funds

Long-Term Asset Lease And Reserve Funds

Introduction

Reserves, commonly referred to as 'rainy day funds', are funds that the City sets aside as an economic safety net to mitigate current and future risks such as unexpected contingencies, emergencies, or revenue shortfalls. These funds are not included in the City's annual operating budget.

The City maintains a number of separate reserve funds – a water rate stabilization fund, a sewer rate stabilization fund, and a series of reserve funds established in connection with the long-term lease of City assets. The asset lease reserve funds function as the City's general, or corporate fund, reserves. This section discusses the City's various reserve funds, as well as the use of proceeds from the City's long-term asset leases. The use of these asset lease funds to subsidize the City's operating budget is discussed in greater detail in the Financial History Review section of this document.

Water and Sewer Rate Stabilization Funds

The City's water fund and sewer fund both maintain rate stabilization funds. These funds are reserved to ensure that the City's water and sewer systems would remain financially solvent in the case of a catastrophic event, in which case the funds would be used to finance operations and make necessary repairs for a short period. A decision is made each year regarding the amount that will be deposited into the rate stabilization funds based on the resources available and the appropriate level of reserves for the water and sewer funds.

The balance of the water rate stabilization fund was relatively constant, at just over $50 million, from 2003 through 2009. In 2010, approximately $10 million was deposited into the fund to bring its balance to just over $60 million, and the fund remained at this level through 2011. In 2012, $13.5 million was deposited into the fund to bring its balance to approximately $75 million.

The balance of the sewer rate stabilization fund steadily increased over time. In 2003, the balance of the fund was approximately $8 million. By 2010, the balance had increased to over $25 million, and the fund remained at that level through 2011. Following the 2012 deposit, this fund's balance was approximately $31 million.

Asset Lease Reserves[21]

Midway Airport Security Funds

In 2008, the City entered into an agreement with a private company for the long-term lease of Midway Airport. The private company failed to consummate the transaction and surrendered its $126.1 million security deposit to the City in 2009. $13.1 million of this amount was used to pay various fees associated with the proposed lease transaction, $33 million was used to pay off existing debt, and $40 million was transferred to the corporate fund for use in 2009. The remaining $40 million was transferred to the corporate fund in two $20 million transfers, one in 2010 and the second in 2011.

Skyway and Parking Meter Lease Funds

In 2005, the City entered into a 99-year lease of the Chicago Skyway, under which a private company was granted the right to operate and collect tolls from the Skyway. In return, the City received an upfront payment of $1.83 billion. Approximately $850 million of this amount was used to pay off existing debt, including $446.3 million to refund the Skyway bonds outstanding at the time of the transaction. In 2009, the City entered into a 75-year lease of its metered parking system, under which a private company was granted the right to operate and collect revenue from the parking meter system and the City received an upfront payment of $1.15 billion. Both of these transactions resulted in the establishment of a long-term reserve fund, a mid-term reserve fund, and a human infrastructure fund. An additional "budget stabilization" fund was established in connection with the parking meter lease transaction.

Long-Term Reserves

The City established a $500 million long-term reserve with a portion of the proceeds of the Chicago Skyway lease. The principal of this reserve fund was intended to supplement corporate fund reserves, with interest earnings to be used for City operating expenses. These funds have been utilized as planned - the principal balance remains $500 million

[21] In legal terms, the City's parking meter agreement is a concession and not a lease; however, for ease of reference the term lease is used in this document for both the Skyway and parking meter agreements.

Long-Term Asset Lease And Reserve Funds

and the earned interest has been transferred to the corporate fund each year, with the dollar amount of the transfer reflecting variations in interest rates.

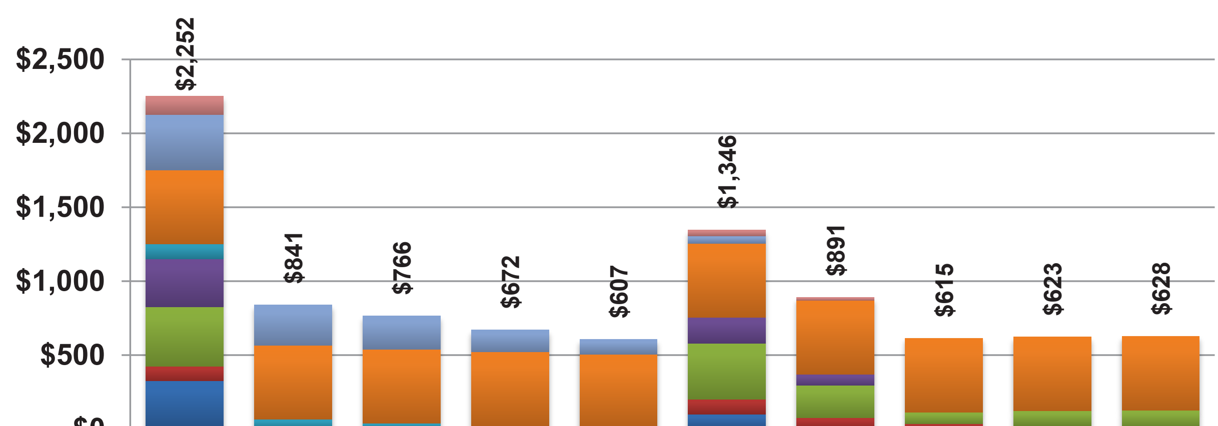
The City established a $400 million long-term reserve with the proceeds of the parking meter lease. This fund was created to replace revenues that would have been generated from parking meters by transferring interest earnings on the fund to the corporate fund, with the principal remaining intact at $400 million. The fund was initially intended to generate $20 million each year based on a 5 percent interest rate earnings assumption. However, starting in 2009, the City began utilizing these long-term reserve funds to subsidize the City's operating budget. In 2009, $20 million was transferred to the corporate fund, and $160 million was used for City operating expenses in 2010. The 2011 budget included a $140 million transfer from this fund for operating purposes. Utilizing these funds reduced the principal balance substantially below the initial deposit and accordingly reduced the interest earnings generated by the fund. The original ordinance establishing the fund directed that an annual transfer of $20 million be made from the fund into the corporate fund to replace lost meter revenue. However, in order to maintain these important reserves, the City amended the ordinance in 2012 to state that only interest generated from the fund, and not principal, may be used for this purpose. In addition, the City began to rebuild these reserves with a $20 million deposit into the fund in 2012 and a $15 million deposit budgeted in 2013.

Mid-Term Reserves and Budget Stabilization Fund

The City also established mid-term reserve funds of $375 million and $325 million, respectively, with proceeds from the Skyway and parking meter leases. Both of these funds were created to supplement corporate fund revenues. The Skyway mid-term reserve fund has been drawn upon as scheduled, with the principal depleted in 2010 and the approximately $50 million in accumulated interest transferred from this

ASSET LEASE FUND BALANCES[22]

$ Millions

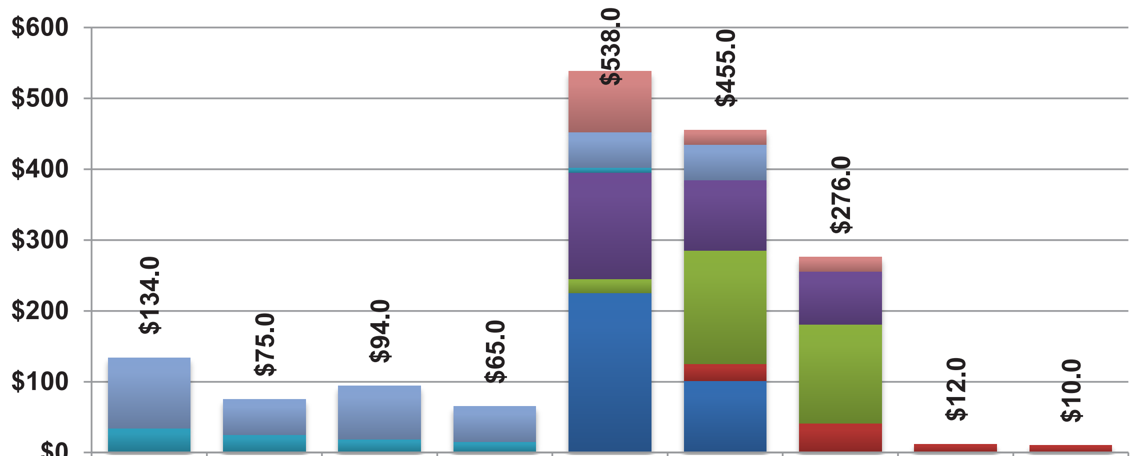


	Deposit	2005	2006	2007	2008	2009	2010	2011	2012	2013 Budget
Midway Security	$126					$40	$20	$0	$0	$0
Skyway Mid-Term	$375	$275	$225	$150	$100	$50	$0	$0	$0	$0
Skyway Long-Term	$500	$500	$500	$500	$500	$500	$500	$500	$500	$500
Skyway Human Infrastructure	$100	$66	$41	$22	$7	$0	$0	$0	$0	$0
PM Mid-Term	$325					$175	$75	$0	$0	$0
PM Long-Term	$400					$380	$220	$80	$100	$115
PM Human Infrastructure	$100					$100	$76	$35	$23	$13
PM Budget Stabilization	$326					$101	$0	$0	$0	$0
Total	$2,252	$841	$766	$672	$607	$1,346	$891	$615	$623	$628

[22] The amounts in these charts represent the principal of the respective funds; interest is not included in either the fund balance or the transferred amounts.

TRANSFERS TO CORPORATE FUND[22, 23]

$ Millions



	2005	2006	2007	2008	2009	2010	2011	2012	2013 Budget
Midway Security	$0	$0	$0	$0	$86	$20	$20	$0	$0
Skyway Mid-Term	$100	$50	$75	$50	$50	$50	$0	$0	$0
Skyway Long-Term	$0	$0	$0	$0	$0	$0	$0	$0	$0
Skyway Human Infrastructure	$34	$25	$19	$15	$7	$0	$0	$0	$0
PM Mid-Term	$0	$0	$0	$0	$150	$100	$75	$0	$0
PM Long-Term	$0	$0	$0	$0	$20	$160	$140	$0	$0
PM Human Infrastructure	$0	$0	$0	$0	$0	$24	$41	$12	$10
PM Budget Stabilization	$0	$0	$0	$0	$225	$101	$0	$0	$0
Total	$134	$75	$94	$65	$538	$455	$276	$12	$10

fund to the corporate fund in 2011. The parking meter mid-term reserve fund has been drawn on an accelerated schedule and was also fully spent at the end of 2011. The ordinance establishing the parking meter mid-term reserve fund set forth the intention to utilize $150 million of these funds in 2009, $50 million in 2010, $50 million in 2011, and $100 million in 2012. However, $150 million was used in 2009, $100 million was used in 2010, and the remaining principal balance of $75 million, together with any interest generated on the fund, was transferred to the corporate fund in 2011.

The parking meter budget stabilization fund was established to assist the City in weathering the national economic downturn occurring at the time of the closing of the parking meter lease transaction. $326.4 million was initially deposited into the fund and the principal was fully utilized by the end of 2010. A small amount (approximately $600,000) of interest remained in the fund and was transferred to the parking meter long term reserve fund in 2012.

Human Infrastructure Reserve Funds

The City set aside $100 million of the proceeds from each of the Skyway and the parking meter lease transactions to be used to fund programs to improve the quality of life in Chicago neighborhoods. The principal of the Skyway human infrastructure fund was fully utilized by the end of 2009, and the remaining interest in the fund was utilized in 2011. The principal balance of the parking meter human infrastructure fund as of year-end 2012 was approximately $23 million, $10.2 million of which is budgeted for human infrastructure programs in 2013.

Proceeds from these funds have been used for a variety of programs aimed at providing resources to the City's

[23] The transfers presented in this chart include amounts utilized to cover transaction costs for the respective lease. The amount transferred from the Skyway mid-term reserve fund in 2005 includes $50 million transferred upon the closing of the transaction in 2004. In 2009, $50 million was transferred from parking meter mid-term reserve fund directly into the corporate fund; an additional $100 million was used to redeem commercial paper that the City issued in December of 2008 to advance the proceeds of the parking meter lease transaction. Amounts transferred from the human infrastructure funds include amounts transferred directly to delegate agencies providing services.

businesses, homeowners, and residents most in need, including:

- Training and employing currently unemployed Chicagoans in technology sector jobs;
- Providing home-delivered meals to senior citizens;
- Enabling the continued development of multi-family affordable housing;
- Offering rent and home-heating subsidies to low income families;
- Funding after-school and summer educational, recreational, and job-training programs for youth;
- Increasing access to capital and other resources for small businesses;
- Maintaining shelter, food, and supportive services for the City's homeless, seniors, and at-risk populations.

Asset Lease Funds Going Forward

At the end of 2012, the aggregate principal balance in the City's asset lease reserve funds was approximately $628 million. The majority of this amount is the $500 million in the Skyway long-term reserve fund, with an additional $13 million in the parking meter human infrastructure fund and $115 million in the parking meter long-term reserve fund.

The 2012 budget phased out the practice of transferring principal from these reserves to subsidize the City's operating budget. Only the interest earned on the long-term reserve funds will be transferred to the corporate fund on a going-forward basis. In addition, as discussed above, the City has begun to rebuild these funds by depositing $20 million into the City's long-term reserves in 2012, with an additional $15 million deposit planned for 2013.

Annual Financial Analysis 2013

Capital Investments

Capital Investments

Introduction

The City's capital improvement program funds the replacement, improvement, and construction of the City's infrastructure and facilities. Capital projects involve improvements with useful lives greater than one year, such as roads, sewer and water lines, buildings, bike paths, and green spaces. Funding for the capital improvement program comes from general obligation bonds, motor fuel tax revenue bonds, water and sewer revenue bonds, state and federal funding, tax increment financing, and private funding through public/private ventures.

Planning for capital improvements is an ongoing and forward-looking process. The City consistently reviews its capital priorities and evaluates whether to repair and improve existing assets or construct and acquire new assets based on the relative cost effectiveness and service implications of each option.

Capital Investment: 2003-2012

This discussion of the City's capital program over the past 10 years will focus on the use of general obligation bond and motor fuel tax bond funds, as these funding sources are the most relevant to City residents as taxpayers and as users of City infrastructure.[24] General obligation bonds are the primary source of City-controlled funds for capital improvements and the only source of citywide capital funding that is financed through property taxes. Motor fuel tax revenue bonds have been financed through taxes on fuel and are used for the construction of road-related improvements such as streets, lighting, and traffic signals.

Local Bond-Funded Capital Outlay

From 2003 to 2012, the City utilized proceeds from the issuance of general obligation bonds and motor fuel tax bonds (together, local bonds) to fund $2.1 billion of its capital program. These bonds are utilized to support a wide variety of project types, including:[25]

- Greening, such as streetscaping projects, green ways, medians, trees, fountains, community gardens, neighborhood parks, wetlands, and other natural areas.
- Facilities, such as the improvement and construction of City buildings and operating facilities, police and fire stations, health clinics, senior centers, and libraries.
- Infrastructure, such as the construction and maintenance of streets, viaducts, alleys, lighting, ramps, sidewalks, bridge improvements, traffic signals, bike lanes, and shoreline work.
- Aldermanic menu projects, which are selected by aldermen, each of whom is allotted $1.32 million of general obligation bond funding to be spent at their discretion on a specific menu of improvements in their respective wards. Over the past seven years, these funds have been used primarily for sidewalks, residential street resurfacing, street lighting, and curb and gutter replacement, with portions of these funds contributed to the Park District ($13.5 million), Chicago Public Schools ($2.6 million), and the Chicago Transit Authority ($500,000).

The high level of activity in 2003 coincides with the issuance of the Neighborhoods Alive bonds, a supplemental general obligation bond series issued over four years (beginning in 2000) and used primarily to fund the construction of municipal facilities such as libraries and police and fire stations. A series of motor fuel tax revenue bonds was also issued in 2003, the proceeds of which funded various road-related projects. The increase in bond-financed capital outlay in 2008 reflects a large library bond issuance in that year, as well as a second issuance of motor fuel tax bonds. Local bond-funded capital improvements generally decreased over the past 10 years as the debt service associated with past bond issuances has grown and the City has made efforts to cut overall costs.

Water and Sewer Bond-Funded Capital Outlay

Water and sewer bond funds are used for the construction and repair of water and sewer lines and related facilities and are financed through water and sewer user fees, respectively. Water and sewer revenue bonds are issued every other year.

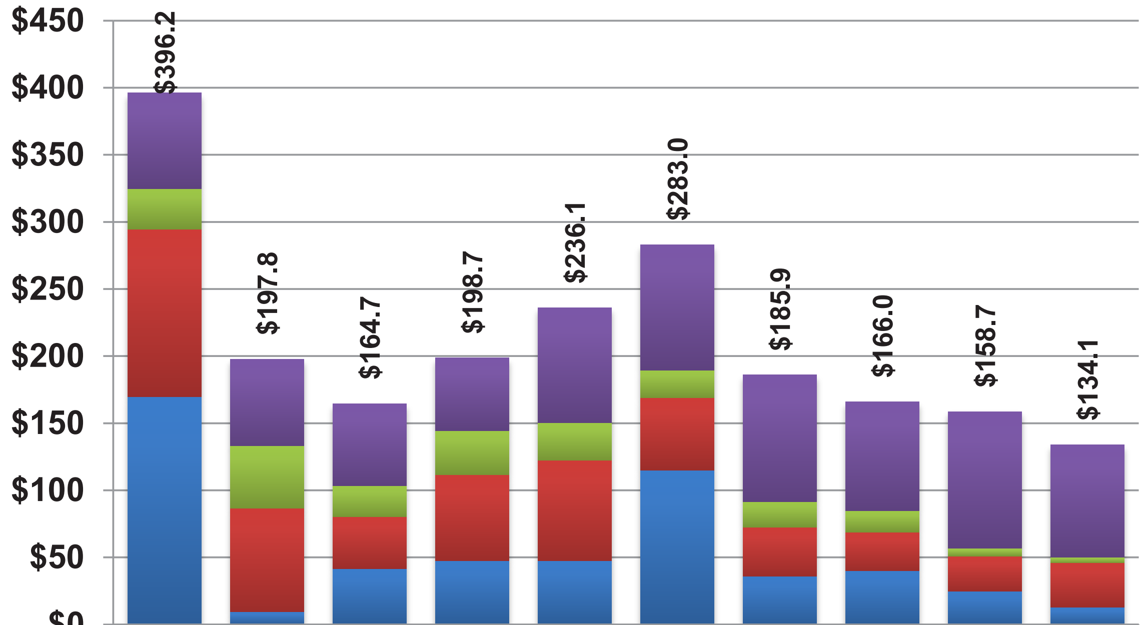
[24] State and federal grant funding for capital improvements and capital funding for Midway and O'Hare Airports are discussed only on a going-forward basis. TIF funding is addressed in the following section of this document.

[25] General obligation bonds have also funded a limited number of other uses, which are discussed separately in the Debt section of this document.

CAPITAL INVESTMENTS

CAPITAL USES OF LOCAL BOND FUNDING

$ Millions



	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Ald. Menu	$71.4	$64.7	$61.2	$54.2	$85.9	$93.4	$94.4	$81.4	$102.0	$84.0
Greening	$30.4	$46.5	$23.3	$32.7	$28.0	$20.7	$19.0	$15.7	$5.8	$4.2
Infrastructure	$124.9	$77.2	$38.6	$64.3	$74.8	$54.0	$36.8	$28.9	$26.0	$33.1
Facilities	$169.5	$9.4	$41.6	$47.4	$47.3	$114.9	$35.8	$40.0	$24.9	$12.7
Total	$396.2	$197.8	$164.7	$198.7	$236.1	$283.0	$185.9	$166.0	$158.7	$134.1

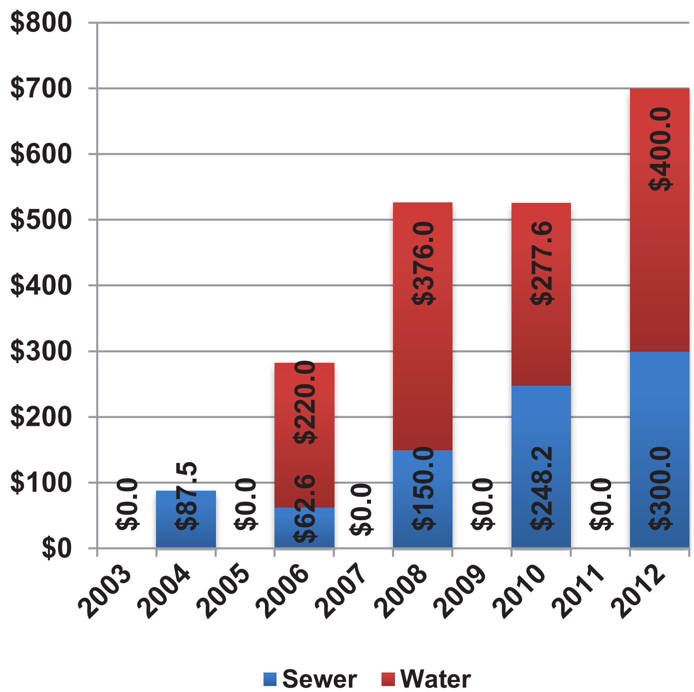
From 2003 to 2012, the City issued $2.1 billion in water and sewer revenue bonds, with fluctuations in the amount of issuances reflecting the City's choices regarding water and sewer system needs and repair priorities.

An aggressive program to modernize and rebuild much of the City's water and sewer infrastructure was initiated in 2012 to address the deteriorated state of the City's water and sewer system, which was costing taxpayers tens of millions of dollars each year. During the last three years, the City spent more than $65 million repairing leaks in the water and sewer systems and restoring the streets, sidewalks, and other infrastructure damaged as a result of these leaks.

In 2012, the City's Department of Water Management replaced 87 miles of water and sewer mains, re-lined 47 miles of sewers, and began construction on major pumping station improvements. This work will improve service, save money, promote sound environmental and water stewardship and ensure a fresh and affordable supply of water for future generations.

WATER AND SEWER BOND ISSUANCES

$ Millions



Capital Investments

Capital Improvement Program: 2013 - 2017

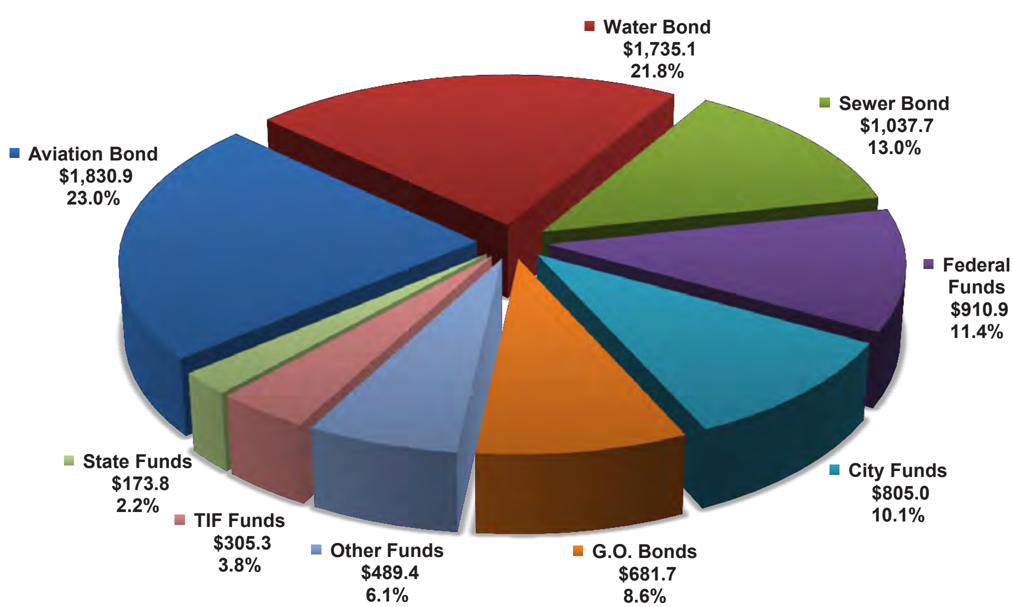
The City's capital improvement program recommends a total of $7.97 billion in capital improvements over the next five years. The charts in this section present the anticipated sources of capital funding and the proposed uses of capital funding for this five-year period. Details regarding the allocation, funding source, timing, and scope of each capital improvement project planned through 2017 are available on the City's website.

Major capital projects moving forward during the next five years include:

- Total realignment of the street and rail crossings in the 130th Street and Torrence Avenue area, eliminating at-grade vehicle and railway crossings through the construction of three new railroad bridges and connecting Brainard Avenue to 130th Street to improve traffic flow, decrease delays caused by freight crossings, and enable more efficient operations at the nearby Ford Motor Company assembly plant; the project will also incorporate improved drainage and pump systems and a mixed use path for pedestrians and cyclists.
- Reconfiguration of the six-way intersection at Damen, Fullerton, and Elston streets, which sees 70,000 vehicles each day and currently experiences a high volume of traffic accidents each year.
- The 606 elevated park and trail system, including the new Bloomingdale Trail bike path, transforming a 2.7 mile stretch of unused elevated railway line into a multi-use linear park with five connected ground-level neighborhood parks.
- Construction of a new elevated CTA station at the Cermak stop on the Green Line, featuring grade level station house facilities, an auxiliary exit to the north side of 23rd Street, and direct transfers to buses on Cermak Road, facilitating convenient access to both McCormick Place and the growing local community.
- Continuation of the long-term rehabilitation of the City's aging water and sewer system; this decade-long initiative will replace 880 miles of century-old water pipes, reline or rebuild more than 750 miles of sewer lines, reline 140,000 sewer structures, and upgrade four of the original steam-power pumping stations.
- The Chicago Riverwalk, spanning west from State Street and incorporating recreational educational, restaurant, and commercial components, which will be funded in part through a loan from the U.S. Department of Transportation's Transportation Infrastructure Finance Innovation Act program.

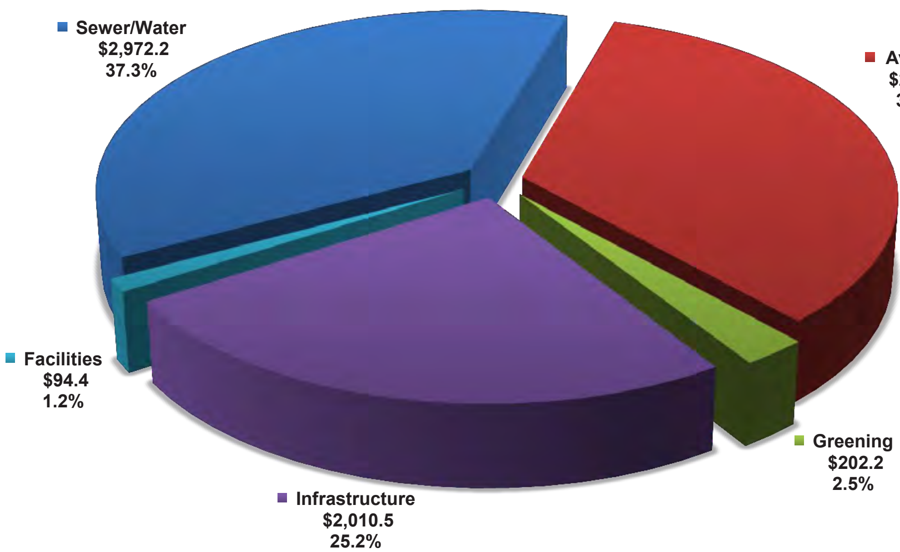
CAPITAL FUNDING SOURCES, 2013-2017

$ Millions



CAPITAL FUNDING USES, 2013-2017

$ Millions



Annual Financial Analysis 2013

TIF

TIF

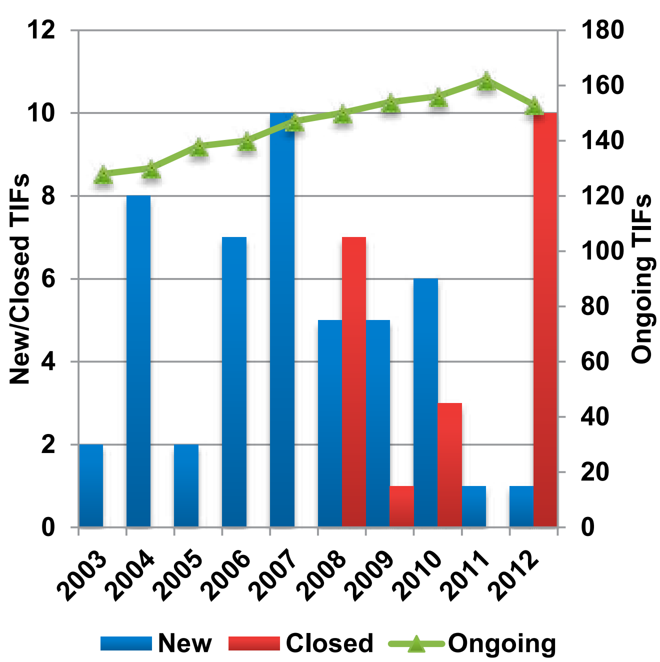
Introduction

Chicago's Tax Increment Financing (TIF) program began in 1984 with the goal of promoting business, industrial, and residential development in areas of the city that struggled to attract or retain housing, jobs, or commercial activity. The program is governed by a state law allowing municipalities to capture property tax revenues derived from the incremental equalized assessed value (EAV) above the base EAV that existed before an area was designated as a TIF district (the tax increment) and use that money for community projects, public improvements, and incentives to attract private investment to the area. The intention is that the effective use of tax increment funds helps expand the tax base, thus increasing the amount of tax increment generated in the district for re-investment within the district and ultimately increasing the property tax base for taxing districts.

The amount of data and information available to the public regarding the City's TIF program is steadily increasing. Currently, the following information is available online:

TIF DISTRICTS CITYWIDE

total districts and number created and closed[26]



- A redevelopment plan for each TIF district. The redevelopment plan provides the basis for designating an area a TIF, including the area's history, the existing land use at the time the TIF was designated, and the factors that qualified the area as eligible for tax increment financing. The plan also states the goals and objectives for the TIF and outlines the redevelopment budget.
- Redevelopment agreements (RDAs). An RDA exists for each project in a TIF that involves a private developer. The RDA includes the name of the developer and the terms of the agreement, the amount of TIF assistance, and the start and end dates of the agreement.
- Annual financial reports. These documents include the audited financial statements required by state statute; each year, one such report must be submitted to the State Comptroller for each TIF district.
- Projection reports. These reports provide estimates of TIF revenues and obligations over a three-year period for each district generating incremental tax revenue.
- The TIF portal. This online portal provides an interactive map-based view of TIF districts by ward and the projects located in each TIF.
- TIF policy guidelines and applications for TIF assistance.
- Maps of the City's TIF districts by geographic area, as well as of each individual TIF district.

In addition, through the City's data portal, detailed financial information is provided in a searchable format, including the data used to create the projection reports noted above; balance sheets showing detailed statements of revenues, expenditures, and changes in fund balances over the previous year; and over 10 years of revenue and expenditure data for each district.

TIF Revenue: 2003-2012

At the start of 2003, the City had 128 TIF districts, 118 of which were generating incremental tax revenue. Between 2003 and 2011, the City created 46 new TIF districts, and in 2012, one new district was created. During the 2003-2012

[26] Closings occur on December 31 of the year in which they are shown, and are generally discussed as part of the following year's budget.

TIF

period, the City repealed four districts pursuant to state law and terminated ten others. In most cases, the statutory term of a TIF is 24 years, and six districts have expired to date. The City received incremental property tax collections from 153 of its 164 TIF districts in 2012, totaling $454.3 million. The chart below presents the total revenue received by the City's TIF districts over the past 10 years.

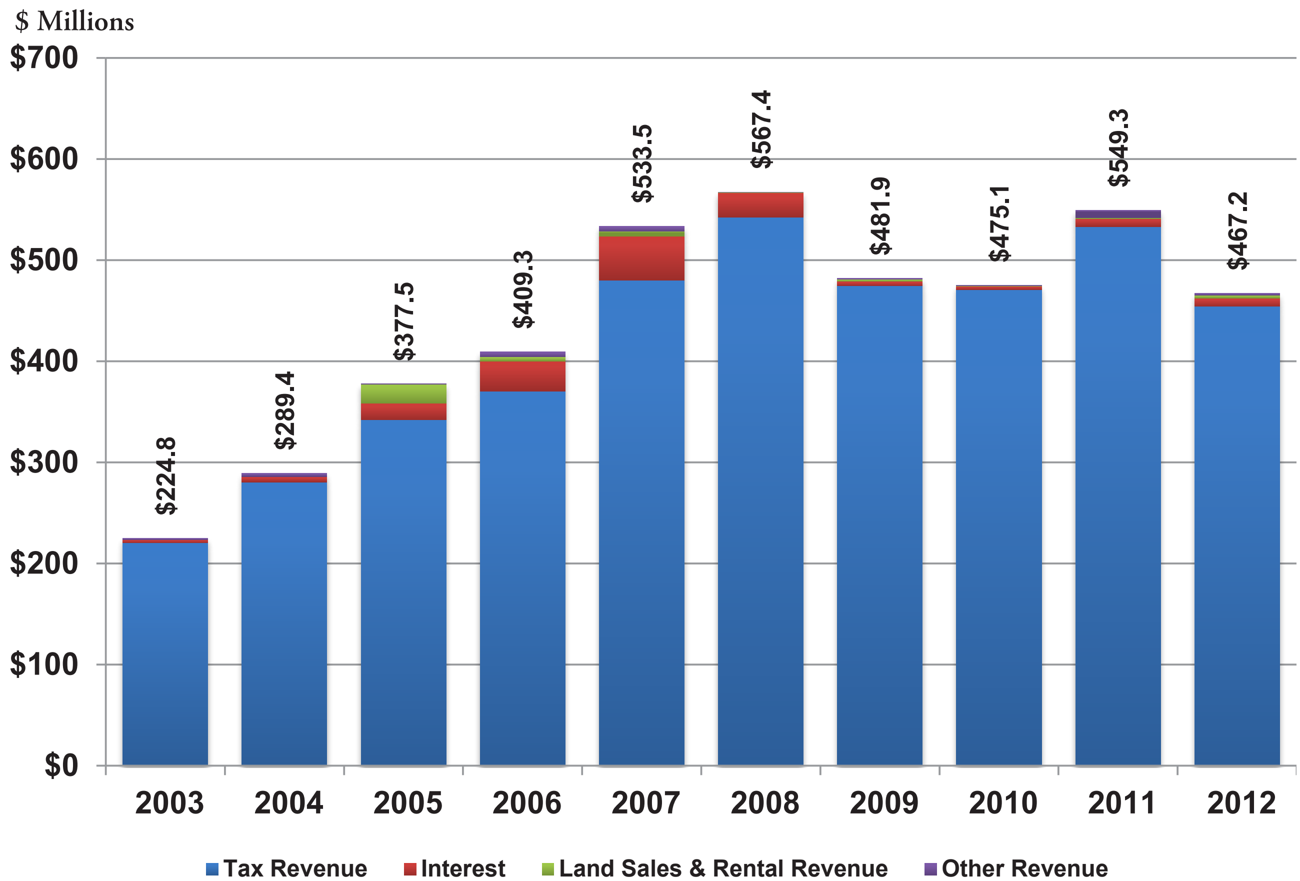
The total amount of TIF revenue grew steadily from 2003 through 2008 as new TIFs were added and as property values in TIF districts increased in line with the trend seen in property values citywide. The first TIF district to expire was the largest TIF district designated to date, the Central Loop TIF. The expiration of that district in 2008 explains the decline in TIF revenues in 2009.

The increase in revenues seen in 2011 is attributable in part to the increase in the composite tax rate in that year. As explained in the Property Tax section of this document, the composite tax rate in Chicago increased as property values began to reflect the decline in the real estate market brought on by the recession.[27] In each TIF district, the amount of TIF revenue depends on the amount of incremental EAV in the district and the composite tax rate, which is applied to the EAV in the district. In 2011, on a citywide basis, the increase in the tax rate outweighed any decrease in EAV in the city's TIF districts, resulting in increased TIF revenues. In 2012, however, the relative impact of the decrease in EAVs began to outweigh the impact of the increase in the tax rate, and overall TIF revenues decreased.

TIF Project Bonds and Notes

The City has funded certain TIF projects by issuing bonds and notes, the proceeds of which are used to pay for TIF-eligible improvements in the districts. The debt service on

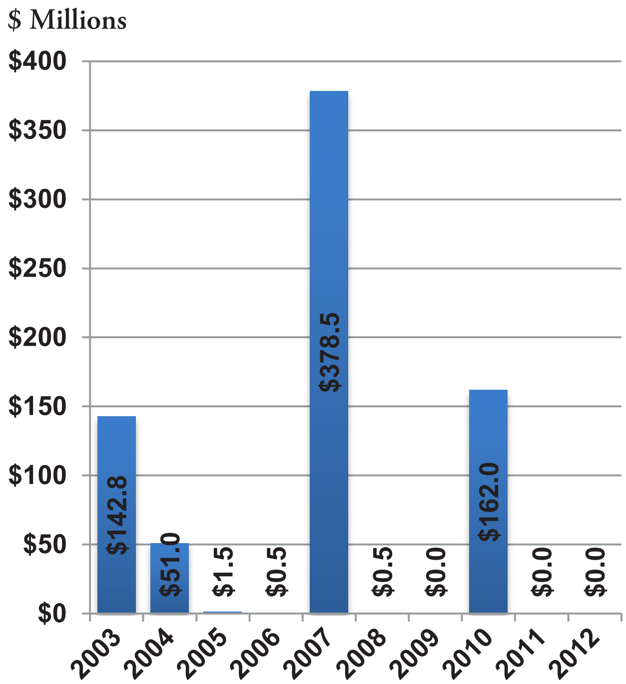
TIF REVENUE BY SOURCE[28]



[27] Property values are reassessed by the County every three years, based on three prior years of sales. Due to the timing of reassessment, EAVs did not begin to reflect recessionary sales and valuations immediately following the economic downturn. When EAVs decrease and levies stay relatively the same, tax rates increase.

[28] The amounts in the chart represent the increment from taxes levied in the prior year, as this revenue is collected during the subsequent year. Note that the tax revenue amounts include not only property tax increment dollars, but also a small amount of "sales tax increment" revenue collected in certain TIF districts. Sales tax increments were authorized in a limited number of TIFs and have been disallowed in new TIFs since 1999. Sales tax increment revenue contributed approximately $1.4 million to $2.5 million to total TIF revenues each year during the 2003 to 2012 period.

TIF BOND ISSUANCES



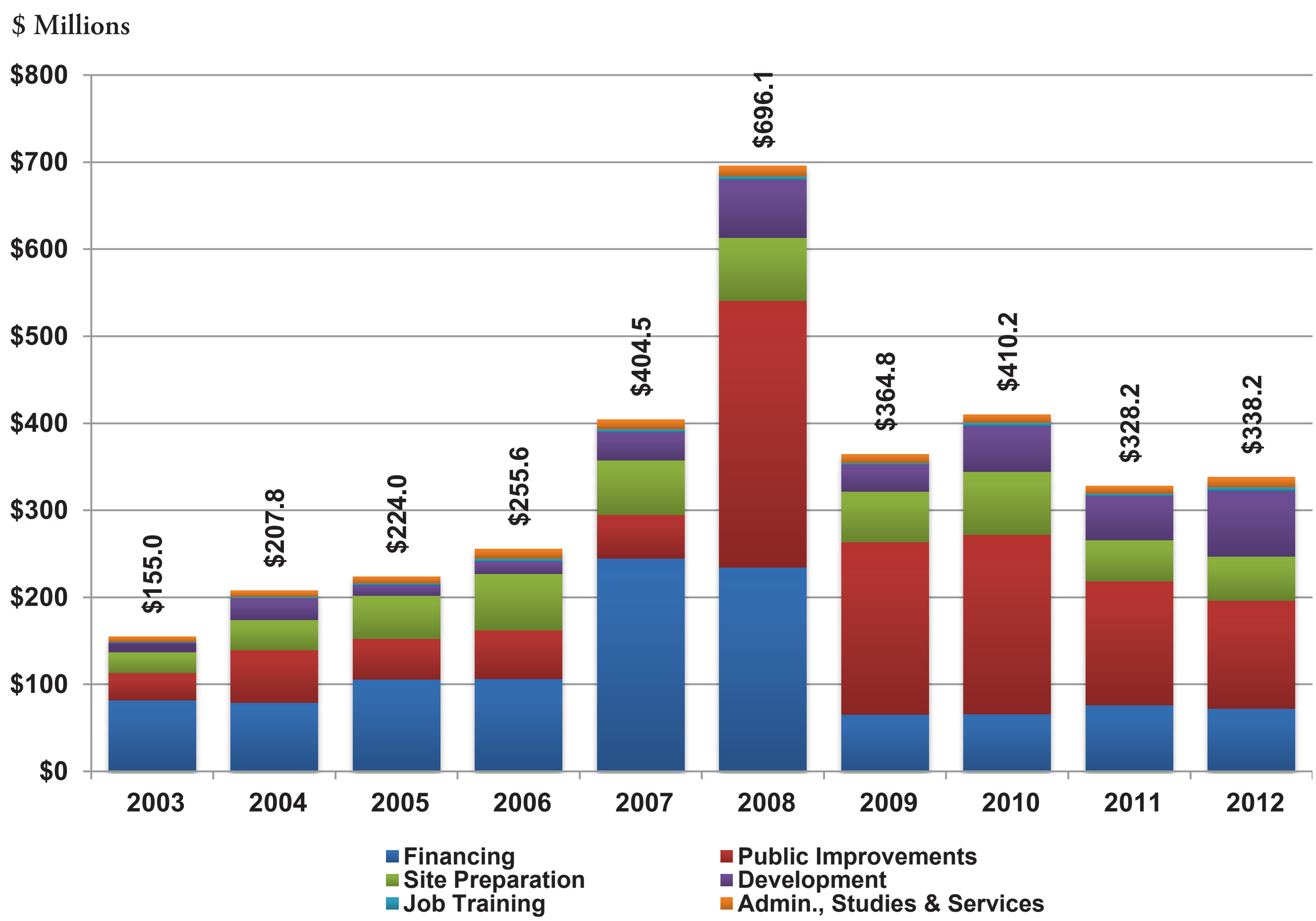
these bonds and notes is then paid with subsequent TIF revenue. Such financing allows the City to undertake larger projects sooner, rather than having to wait for annual TIF revenues to accumulate. The chart to the left shows the years in which bonds were issued and the amounts thereof.

As reflected in the chart, the City issued bonds for large TIF projects in the Central Loop district in 2003 and the Pilsen Industrial Corridor district in 2004. In 2007 and 2010, the City issued bonds as part of the Modern Schools Across Chicago program (MSAC), which is discussed in more detail below.

TIF Expenditures: 2003-2012

Between 2003 and 2012, the City spent $3.38 billion in TIF funds (including the proceeds from bonds issued to fund TIF projects) on a range of projects in TIF districts across Chicago. The chart below details the way in which these funds were spent, with expenditures categorized as follows:

TIF EXPENDITURES[29]



[29] This chart represents an accounting view of TIF expenditures. This information is taken from the annual financial reports for each TIF and may vary slightly from projection reports or similar available information.

- Financing, which consists of debt service on bonds and notes issued to finance public improvements.
- Public Improvements, including the construction of and improvements to schools, parks and open spaces, and infrastructure such as streets, sidewalks, and lighting.
- Site Preparation, which includes property assembly, demolition, environmental, and relocation in preparation for development.
- Administration, including the cost of studies, program administration, and professional services.
- Development, which includes the construction of low income housing, rehabilitation of existing homes and buildings, commercial developments, and reimbursements to private developers for approved redevelopment projects.
- Job Training, which consists of the cost of employment training programs.

During this period, approximately 36 percent of the City's TIF spending, or $1.22 billion, was for public improvements, and approximately 35 percent, or $1.13 billion, was for debt service, largely to finance public improvements. Approximately $1.27 billion was dedicated to projects undertaken in collaboration with private developers. Such development projects include hospitals, affordable housing, retail and grocery stores, and the preservation of historic buildings. The City estimates that private developers spend approximately five dollars for each TIF dollar provided by the City.

The increase in public improvement spending seen in 2008 was driven largely by MSAC projects. The increase in development spending in that same year was related largely to projects in the Central Loop TIF, and the growth in development spending seen after 2009 reflects a range of projects in various TIFs citywide. The decrease in debt service costs between 2008 and 2009 was due in large part to the expiration of the Central Loop TIF and the retirement of outstanding debt associated with that TIF.

Under certain circumstances, the City may transfer TIF revenue from one district to an immediately adjacent TIF district for a specific project. Such transfers have traditionally been used for larger projects, such as schools or parks. For example, inter-TIF transfers have been used to pay debt service on bonds issued to fund school construction and renovations, including MSAC projects, as well as to fund projects at Taylor Lauridsen and Blackwelder Parks and the new Cermak Station on the CTA Green Line. Between 2003 and 2012, a total of $329.6 million was transferred between TIFs. Information regarding proposed transfers is made available on the City's website prior to transfer.

TIF Funding Provided to Sister Agencies

Since the start of its TIF program, the City has provided or is committed to providing $1.20 billion to CPS for school-related projects, $302.5 million to the Park District for park and open space projects, and $228.0 million to the CTA for track and station renovations and related projects.

TIF funding provided to CPS for school-related projects to date has benefitted 58 schools in 35 TIF districts citywide. This funding supports capital work at schools in TIF districts, including Back of the Yards College Preparatory High School, William Jones College Preparatory High School, Hernandez Middle School, Westinghouse High School, Albany Park Academy, Mather High School, West Ridge Elementary, Prieto Elementary, Skinner Elementary, South Shore High School, National Teachers Academy, Senn High School, Chase High School, Jose De Diego Elementary, and Juarez High School. A significant portion of the TIF funds provided by the City to CPS has been through MSAC, a capital improvement program established to fund the construction and renovation of 23 schools over seven years. The City has committed to providing $763.1 million in TIF funds to MSAC over the life of the program. This is in addition to other support provided by the City to CPS, such as crossing guards, police services, and funding for a portion of CPS pension contributions.

TIF Surpluses and Closings

Surplus Declaration

Under certain circumstances, the City will declare a portion of the funds in a TIF as surplus, returning the proportionate share of the funds to the applicable local taxing districts. In 2012, $82.9 million was declared as surplus during the budget process, and $25.0 million was declared as surplus during the 2013 budget process. Such surplus declaration is pursuant to a policy to consistently return unneeded TIF

TIF

revenues to the taxing districts according to set criteria, as recommended by the TIF reform panel. In the past two years, the City has declared a surplus when the TIF district is older than three years, projected obligations will not exceed projected revenues, funds are not limited by ordinance or reliance on adjacent TIF funding, and TIF funds available for programming (funds not committed to current or future projects in a particular TIF) exceed approximately $2 million.

The table below indicates the amount of money returned to local taxing districts since 2009 as surplus, either from existing TIF districts through the declaration of a surplus or from those that have closed through expiration, termination, or repeal. During this time, the City has received approximately 20 percent, the Park District approximately 6 percent, and CPS approximately 52 percent of all surplus dollars, with slight yearly variations based on each district's applicable share of the tax rate.

The City's TIFs had an aggregate balance of $1.71 billion at the close of 2012. However, $1.53 billion of this balance is reserved for payments due in connection with current or planned projects. Of the remaining funds, a portion is reserved to fund project costs in TIF districts where revenues are declining, in the event that annual revenues are insufficient to pay future obligations.

TIF SURPLUS

$ Millions, declared and from TIFs closed in prior years

	2009	2010	2011	2012	2013
Declared	$0.0	$0.0	$188.0	$82.9	$25.0
Expiration	$15.4	$0.02	$15.1	$13.7	$8.4
Repeal	$2.3	$0.0	$73.3	$0.0	$0.5
Termination	$6.9	$0.02	$0.0	$0.0	$9.6
Total	**$24.6**	**$0.04**	**$276.4**	**$96.6**	**$43.5**

Correction issued August 12, 2013: The table above has been revised from that originally published to reflect corrected historical data.

TIF Closings

There are a number of ways in which TIF districts come to a close:

- A TIF district expires automatically after 23 or 24 years, depending on when it was established.
- The City can terminate a TIF district before its planned expiration if it has achieved all of its goals or if an extended period of inactivity or lack of investment has indicated that additional development is unlikely.
- The City must repeal a TIF district if no substantial redevelopment activity has been initiated during the first seven years of the district's existence.

As part of ongoing reforms to the City's TIF program, the City closed ten TIF districts at the end of 2012; one expired, seven were terminated, and two were repealed. The City continues to evaluate the performance of each TIF district and will consider additional terminations as appropriate going forward, in accordance with the recommendations of the TIF reform panel.

After a TIF district ends, the incremental EAV of the district becomes a part of the aggregate EAV that is available to all taxing districts. Taxing districts, including the City, have the ability to recover their portion of the revenue from the incremental EAV by adding it to their levy following a TIF district's dissolution. Amounts recovered through this practice are not subject to the State-mandated property tax cap that applies to certain districts, including CPS. This practice is further discussed in the Property Tax section of this document.

TIF Program Going Forward

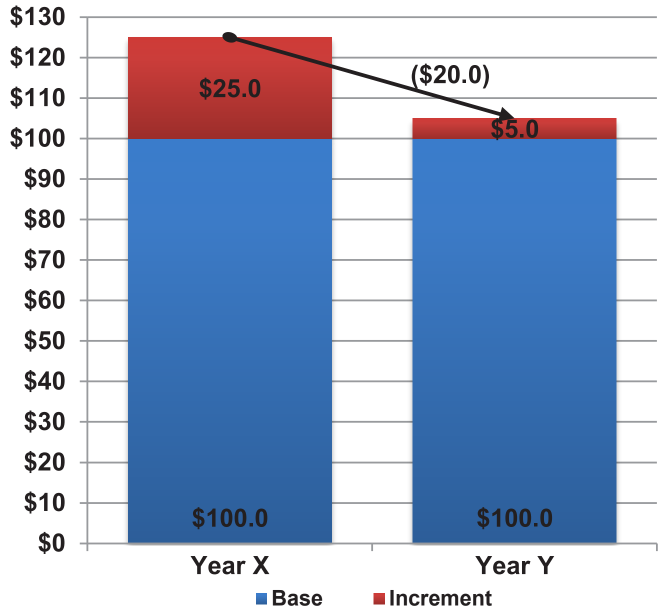
The City generates projection reports for each TIF district that provide a snapshot of the financial health of the TIF and are critical in assessing the TIFs' ability to fund future projects. Over the past year, the City's ability to develop accurate projections has increased due to improved coordination and data sharing with Cook County. With more complete and current information, the City has been able to more closely monitor property value changes and better understand and anticipate current and future trends that may impact TIF revenues. Currently, the City tracks ongoing property assessments across seven townships and compares new assessed values to previous values to gauge trends and estimate rates for the tax year.

As discussed above, EAVs in the City's TIF districts declined in line with the decline in property values across the city following the recession. Due to the County's assessment schedule, which looks at sales for the three preceding years when assessing property values, the negative impact on TIF revenues was felt in 2012. TIF revenue is especially sensitive to such declines in value, as the amount of revenue that a TIF generates depends on the incremental EAV in the

TIF

EXAMPLE OF REDUCED EAV ON TIF INCREMENT

$ Millions



Assume a TIF district's total EAV in Year X is $125 million, of which $100 million is base EAV and $25 million is incremental EAV. If in Year Y the total EAV declines to $105 million, then the base EAV will remain at $100 million while the incremental EAV is reduced to $5 million.

district (the EAV above the base EAV that existed before the area was designated as a TIF district). The incremental EAV, and thus TIF revenues, absorb the impact of a decline in property values before the decline impacts any of the base EAV. This is illustrated in the chart above.

Property values in some parts of the City are slowly recovering while values in other areas continue to decline. However, due to the method of reassessment by the County, assessments for the upcoming years will continue to include years in which property values were depressed. Consequently, citywide EAV will continue to decrease or stagnate before starting to reflect the positive growth currently being seen in the market. Citywide EAV peaked in 2010 at $84.6 billion and has since declined to approximately $65.3 billion, a 23 percent decrease.

In the past year alone, the EAV in TIF districts dropped by $1 billion, mirroring the downward trend seen in EAVs citywide, and declining EAVs will continue to impact revenue in a significant number of TIFs across the city in the coming years. These declines translate into less revenue to fund public projects and developments in affected TIF districts. Newer TIFs created just before the recession have a high base EAV and little incremental EAV; these TIFs are particularly vulnerable to declining EAVs.

In the upcoming years, some TIFs will not generate any revenue because the EAV of the district has fallen below the district's base EAV, and a number of TIFs will have obligations in connection with past or ongoing projects that exceed anticipated TIF revenues. To address these anticipated shortfalls, the City is holding back current revenues in certain TIF districts to be utilized to meet future obligations in the affected TIF districts.

Eight TIF districts are set to expire over the next three years – New West and Stockyards Industrial Commercial in 2013; 95th Street & Stony Island, Near South, and Roosevelt/Homan in 2014; and Sanitary Drainage & Ship Canal, Stockyards Southeast Quadrant Industrial, and Read/Dunning in 2015. These expirations will reduce program-wide revenues and expenditures accordingly.

Annual Financial Analysis 2013

Debt

Debt

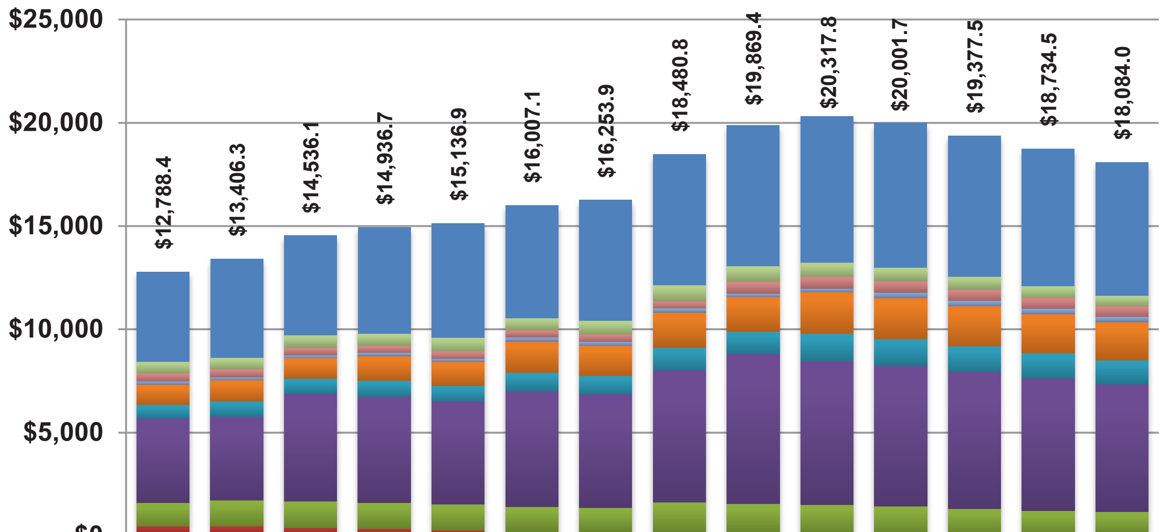
Long-Term Debt

The City finances certain of its operating and capital expenditures through the issuance of bonds. Each type of bond is paid from a particular source of revenue.

- Property tax funded general obligation bonds, funded with property tax revenue, are issued annually to pay for capital projects and equipment, settlements and judgments, and certain employment and pension obligations.[30]
- Other general obligation bonds, which make up a small subset of the City's general obligation bonds, are funded with other sources of revenue and are issued to pay for specific related purposes For example, revenue from the 911 call surcharge is used to fund bonds for the construction of the City's 911 call center.
- Sales tax revenue bonds, funded with sales tax revenue, are issued to pay for general City infrastructure projects.
- Motor fuel tax revenue bonds, funded with motor fuel tax revenue, are issued to pay for road and highway projects.[31]
- TIF bonds, funded with TIF revenue, are issued to pay for redevelopment projects in TIF districts.
- Water and sewer revenue bonds, funded with revenue from water and sewer fees, are issued

OUTSTANDING LONG-TERM DEBT[32]

$ Millions



	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Property Tax Funded G.O. Bonds	$4,362	$4,796	$4,835	$5,161	$5,536	$5,474	$5,849	$6,345	$6,818	$7,078	$7,005	$6,833	$6,650	$6,456
Non-Property Tax Funded G.O. Bonds	$559	$549	$587	$556	$672	$576	$643	$767	$734	$696	$656	$614	$561	$504
Sales Tax Revenue Bonds	$381	$374	$363	$361	$353	$343	$356	$355	$577	$566	$554	$542	$528	$515
Motor Fuel Tax Revenue Bonds	$162	$160	$156	$151	$147	$209	$204	$199	$193	$187	$282	$276	$270	$266
Water Revenue Bonds	$984	$1,004	$991	$1,193	$1,164	$1,499	$1,460	$1,698	$1,656	$2,012	$1,971	$1,928	$1,885	$1,832
Sewer Revenue Bonds	$654	$747	$732	$771	$755	$901	$877	$1,099	$1,072	$1,320	$1,284	$1,248	$1,209	$1,169
O'Hare Revenue Bonds	$4,097	$4,048	$5,214	$5,150	$4,995	$5,603	$5,506	$6,404	$7,260	$6,971	$6,810	$6,623	$6,433	$6,187
Midway Revenue Bonds	$1,139	$1,279	$1,272	$1,258	$1,244	$1,207	$1,185	$1,461	$1,435	$1,383	$1,359	$1,249	$1,142	$1,112
TIF Bonds	$449	$448	$387	$335	$272	$195	$175	$153	$124	$106	$80	$65	$56	$44
Total	$12,788	$13,406	$14,536	$14,937	$15,137	$16,007	$16,254	$18,481	$19,869	$20,318	$20,002	$19,377	$18,734	$18,084

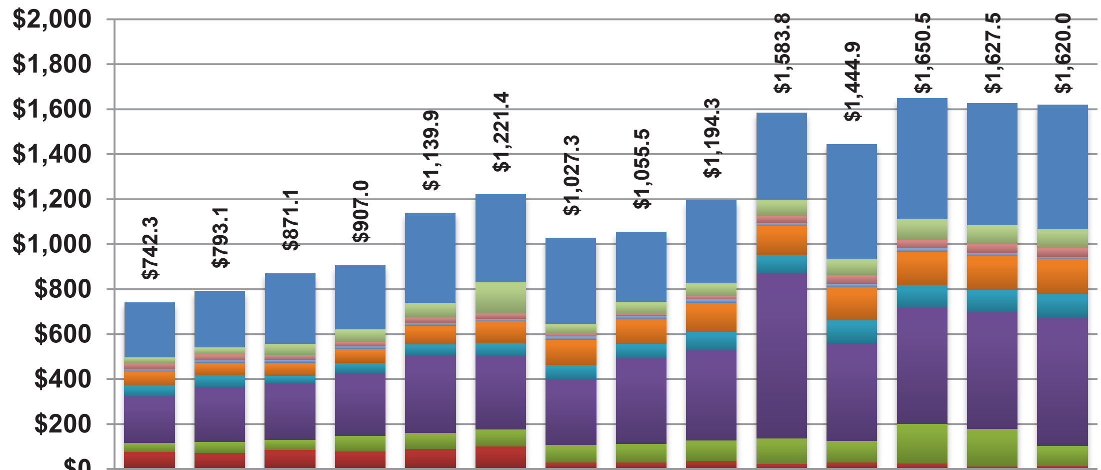
[30] This category includes bonds issued by the City on behalf of the City Colleges of Chicago in 1999 and 2007.

[31] In 2013, the City expects to issue a series of motor fuel tax revenue bonds to the federal government at a low interest rate through the U.S. Department of Transportation's Transportation Infrastructure Finance Innovation Act (TIFIA) program to fund the expansion of the Chicago Riverwalk. Beginning in 2014, in addition to motor fuel tax revenue, revenue from fees charged to tour boat operators in the city and other revenues related to the new Riverwalk, will secure the City's motor fuel tax revenue bonds.

[32] The City's 2013 general obligation bonds have not yet been issued. The amounts presented in this section do not include the issuance of any new bonds in 2013 or future years. Last year's Outstanding Long-Term Debt chart included the 2012 water revenue bond issuance in budget year 2011; this amount has been moved to 2012 in the chart above.

LONG-TERM DEBT SERVICE PAYMENTS[32]

$ Millions



	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Property Tax Funded G.O. Bonds	$243	$250	$312	$284	$400	$390	$381	$311	$368	$386	$511	$538	$541	$550
Non Property Tax Funded G.O. Bonds	$27	$32	$50	$55	$64	$137	$42	$56	$56	$69	$69	$92	$84	$85
Sales Tax Revenue Bonds	$26	$26	$22	$19	$26	$25	$13	$5	$15	$33	$39	$39	$39	$39
Motor Fuel Tax Revenue Bonds	$11	$11	$12	$12	$12	$11	$16	$16	$16	$16	$16	$16	$17	$13
Water Revenue Bonds	$63	$56	$57	$61	$82	$96	$110	$110	$127	$128	$148	$148	$148	$155
Sewer Revenue Bonds	$48	$52	$35	$48	$50	$58	$64	$64	$82	$82	$100	$100	$100	$100
O'Hare Revenue Bonds	$208	$243	$251	$279	$345	$326	$292	$380	$401	$732	$436	$517	$519	$574
Midway Revenue Bonds	$39	$48	$45	$68	$71	$74	$77	$82	$91	$114	$95	$176	$167	$89
TIF Bonds	$78	$74	$86	$80	$91	$103	$32	$32	$38	$24	$31	$27	$13	$15
Total	$742	$793	$871	$907	$1,140	$1,221	$1,027	$1,056	$1,194	$1,584	$1,445	$1,650	$1,627	$1,620

every other year to pay for capital projects for the water and sewer systems, respectively.

- O'Hare and Midway revenue bonds, funded with revenue from airport operations, are issued to pay for terminal and airfield improvements.

The City's debt level increased steadily for much of the past 10 years, reaching a high in 2012 of approximately $20.3 billion. The bulk of this debt was used to fund capital projects across the City, but portions have also been used to pay "working capital" expenses such as median maintenance, irrigation, and plantings; retroactive salary and pension payments (resulting from union contract re-negotiations); and costs incurred in connection with settlements and judgments against the City.

In addition, a portion of the City's general obligation bond issuance is used to finance certain equipment purchases, such as technology equipment, vehicles, fire safety equipment, and similar items. The use of general obligation bond proceeds for the purchase of equipment has generally decreased in recent years - peaking in 2006 at $111.7 million and decreasing to $68 million in 2012 - as the City has made efforts to cut overall costs.

Debt service paid primarily with taxpayer dollars (excluding debt payments for O'Hare and Midway airport improvement programs, which are paid with user fees imposed on airlines) totaled approximately $738.3 million in 2012. This amount is anticipated to increase to $914.0 million in 2013. Even if no new long-term debt is issued, and assuming no refinancings, these debt service payments will continue to increase through 2016. The City uses refunding and restructuring as part of its debt management strategy. As discussed above in the Financial Forecast section, a substantial portion of the City's property tax dollars are used to pay this debt service.

Short-Term Debt

In addition to the long-term debt discussed above, the City issues certain types of short-term debt to address various operating, liquidity, and capital needs, including:

Debt

- Commercial paper notes are issued to satisfy cash flow needs of the City on a limited basis to fund building and site maintenance and operations for the City's libraries for a short period of time until property tax revenues are collected.
- Commercial paper notes are used as an interim financing mechanism for corporate, water, O'Hare and Midway fund projects for a period of time until long-term bonds are issued.
- During the period between 2005 and 2011, approximately $29.3 million in commercial paper was issued to fund the maintenance and operation of Millennium Park; the City has allocated $2 million towards paying off this Millennium Park debt in 2013 and plans to continue to allocate funds each year going forward to making such payments.
- Short-term financing is being used to fund the consolidation and reorganization of City offices and the renovation of portions of City Hall in order to better facilitate the day-to-day functions of City departments, increase the City's utilization of its owned space, and save money on lease expenses. The City currently leases multiple floors at 33 N. LaSalle Street at an annual cost of $4.4 million. That lease terminates at the end of 2013, and the City will not renew the lease but instead shift departments from this space to City Hall or other City office space. The total cost of the consolidations and renovations is estimated at $12 million, which will be recouped within the first three years with these lease savings.

Annual Financial Analysis
2013

Pensions

Pensions

The City's Pension Funds

Illinois State law establishes retirement plans for all public employees in the State, including those employed by the City. The basis of these retirement plans are pension funds, into which employees and their employers contribute, and from which retirement benefits are paid. City employees participate in one of four such defined-benefit pension plans:[33]

- the Municipal Employees' Annuity and Benefit Fund (MEABF), which covers most civil servant employees of the City, as well as non-teacher employees of the Chicago Public School system;
- the Laborers' and Retirement Board Employees' Annuity and Benefit Fund (LABF), which covers City employees who are members of certain unions;
- the Firemen's Annuity and Benefit Fund (FABF), which covers the City's sworn firefighters and paramedics; and
- the Policemen's Annuity and Benefit Fund (PABF), which covers the City's sworn police officers, captains, lieutenants, and sergeants.

These pension funds and the contributions and benefits under each are regulated by the Illinois Pension Code. Each City employee contributes a statutorily-determined amount to their pension during each year that they are employed by the City. The City then contributes a statutorily-determined multiple of the employee contribution, with the multiplier varying by pension fund.[34]

These contributions are then invested by the pension funds in a variety of stocks and other assets, in accordance with the Illinois Pension Code. The return on these investments, together with the cumulative amount of employee and City contributions into the pension fund, make up the total assets of the fund. Once an employee has served a certain number of years and reached a certain age (these requirements vary depending upon the fund), they can retire and begin to receive retirement benefits paid out of these assets.

STATE-MANDATED PENSION CONTRIBUTIONS[34]

as a percentage of pay, as of 2013

	FABF	PABF	LABF	MEABF
Employee Contribution	9.125%	9.00%	8.50%	8.50%
City Multiplier	2.26	2.00	1.00	1.25
City Contribution	20.62%	18.00%	8.50%	10.63%
Total Contribution	**29.75%**	**27.00%**	**17.00%**	**19.13%**

[33] Separate pension funds exist for employees of the Chicago Transit Authority, the Chicago Park District, and teachers at the Chicago Public Schools. Those pension funds are not discussed in this document, as this Annual Financial Analysis does not address the finances of the City's sister agencies.

[34] The City's annual contribution is based on the contribution made by the employee two years prior. For example, in 2013, the City is matching (at the applicable rate) the contribution made by the employee in 2011. Because the City's contributions are paid largely with property tax proceeds, contributions are budgeted in the levy year, and paid to the funds in the following year, when property tax collections are received. Contributions are discussed here in terms of the year in which they are budgeted.

The Unfunded Pension Liability

A pension fund is said to be 'fully funded' when its total assets are sufficient to cover the projected future benefits that the Pension Code requires it pay to the employees that contributed into the fund. If the fund's total assets are not sufficient to cover the future benefits, it is said to have an 'unfunded liability.' The unfunded liability is the difference between the fund's total assets and the value of the future benefits it must pay.[35] At present, all four of the City's pension funds carry significant unfunded liabilities, as shown in the table below.

FUNDING STATUS OF CITY PENSION FUNDS

$ Millions, as of December 31, 2012

	Total Assets	Accrued Actuarial Liability	Unfunded Liability	Funding Level
MEABF	$5,183	$13,367	$8,455	38%
LABF	$1,371	$2,375	$1,004	58%
FABF	$1,032	$4,066	$3,034	25%
PABF	$3,213	$10,221	$7,007	31%
Total	**$10,779**	**$30,299**	**$19,500**	**36%**

The current funding status of the pension funds is the result of the statutory framework on which the pension system is based and the political and economic factors that have acted upon that framework. As discussed above, the Illinois Pension Code mandates that each participating employee contribute a percentage of their pay each year, and that the City contribute a fixed multiple of that same percentage. This formula is static; the contribution percentages do not change to adjust for changes in the economy affecting returns on pension fund investments, changes in the demographics of retiring employees, or changes in the benefits promised to employees. As each of these factors changed over the years, the contribution formula remained the same, contributing to today's unfunded liability.

Economic Downturns

Two major economic events significantly affected the health of the City's pension funds. When the dotcom bubble burst in 2000, the assets of the pension funds shrank significantly due to market losses. From 2000 to 2002, the four funds went from approximately 87 percent funded to approximately 62 percent funded, due primarily to investment losses. Investment performance improved in the mid-2000s, but this growth was on a smaller pool of money due to prior losses, so even in years with high investment returns, the overall funding level remained at around 61 to 66 percent.

Then, in 2007 and 2008, the real estate-driven market crash took the City's pension funds, collectively, from approximately 62 percent funded to approximately 38 percent funded. With this low base of assets on which to earn interest, it is virtually impossible that investment returns alone will be sufficient to restore the funds to health – for the MEABF, for example, it would require a consistent annual return on investment of more than 13.5 percent a year for the next 50 years to bring the fund back to financial stability.

Changes in Benefits

Over time, additional benefits have accrued under or been written into the Illinois Pension Code. Most notably, automatic cost-of-living adjustments written into the Pension Code have significantly increased the cost of benefits. These adjustments provide annual increases in pension payments regardless of whether or to what extent the cost-of-living actually increases. Legislation passed by the State in 2010 eliminated these automatic cost-of-living adjustments for employees hired on or after January 1, 2011, for all four funds, and instead tied cost-of-living adjustments to the consumer price index.[36] However, all employees and retirees hired before that date continue to receive the automatic annual increases, which vary by fund, with FABF and PABF under one scheme and MEABF and LABF under another. Employees hired prior to 2011 and participating in the FABF or PABF receive annual cost-of-living adjustments at a simple rate (either 3 percent or 1.5 percent) based on the original annuity payment to the retiree. Employees hired prior to 2011 and participating in the LABF or MEABF

[35] The unfunded liability is determined on an actuarial basis. It is an as-of-date calculation, which assumes a certain discount rate and considers the present value of the liability for benefits earned through the valuation date.

[36] P.A. 96-0889 and P.A. 96-1495..

receive annual cost-of-living adjustments at a 3 percent compound rate, meaning that each year their benefits payment increases 3 percent over the prior year's benefits payment.

In addition to the automatic cost-of-living adjustments, through to a lesser degree, changes to the Pension Code also increased the total cost of benefits owed. Amongst other changes, certain benefit minimums were raised, the definition of pensionable pay was made more inclusive, and some healthcare benefits were increased.

Workforce and Retiree Demographics

In addition to investment losses and benefit increases, the makeup of the City's workforce and retirees has added to the unfunded liability. The statutorily-set contribution percentages did not change to account for shifts in basic demographic factors such as the lifespan of retirees, and as retirees live longer, they collect benefits longer, and the projected future benefits costs of the pension funds increase. Adding to this, as the City took measures to incentivize early retirement to help balance the City's budget, employees retired and thus stopped paying into the pension funds and started collecting from the pension funds sooner than would otherwise have been expected. This affected the pension funds' balances on both sides - contributions decreased while benefit costs increased.

Conclusion

In summary, a series of severe economic events occurred over the course of the past twelve years, but the pension system's funding mechanisms were vulnerable from the very beginning. The system was not set up to automatically adjust for investment losses or increased benefit payments, and lawmakers did not take action to address the situation with cuts to benefits or increases in contribution requirements. The result of this disconnect is a total unfunded pension liability of $19.5 billion across the four pension funds. This unfunded liability will grow to more than $24.5 billion by the start of 2017 if nothing is done to address the situation, and the MEABF will likely exhaust its assets in or around 2024, with the LABF following around 2027.[37]

Effect of the Unfunded Liability on City Finances

Throughout the life of the pension funds, each year, employees and the City have contributed the statutorily-required amounts into these funds. For the reasons discussed above, the statutorily-required contributions, even as they steadily grew, fell far short of covering the future benefits that are owed to retirees.

Pursuant to legislation passed by the State in 2010, beginning in 2015, the City will be statutorily required to contribute an actuarially-determined amount sufficient to bring the PABF and FABF to a 90 percent funding level by 2040.[38] No such legislation has been passed with respect to the LABF or MEABF. The chart at the bottom of the following page sets forth the City's historic contributions and statutorily-required contributions through 2020 under current law, accounting for the recently enacted PABF and FABF funding requirements. The chart at the top of the following page shows what the City's required contributions would be if funding requirements similar to those legislated for the FABF and PABF were enacted for the LABF and MEABF.

Even under current law, without any requirement to fully fund the LABF or MEABF, the City's total required contributions will grow from an anticipated $479.5 million in 2013 to $1.07 billion in 2015, and increase steadily to $1.26 billion in 2020. If similar funding requirements were enacted for the LABF and MEABF, the City's required contributions would grow to $1.68 billion in 2015, and to $1.97 billion in 2020. To put these amounts into context, the additional pension contributions that will be required in 2015 under current law is equal to the annual cost of keeping 4,300 police officers on the street or over 3,750 firefighters on duty; this amount could fund the resurfacing of almost 16,000 city blocks, and is more than six times the annual operating budget for the entire Chicago Public Library system.

The City's current property tax levy is $801.3 million. The levy has historically been the primary revenue source for the payment of pension obligations, with the balance

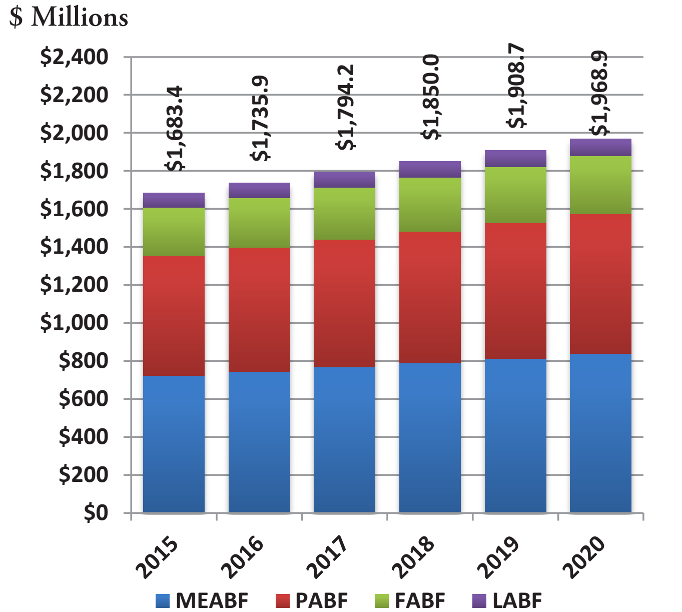
[37] These projections assume an average annual rate of return on assets of 7.50 percent for the LABF and MEABF, 8.00 percent for the FABF, and 7.75 percent for the PABF.

[38] P.A. 96-1495.

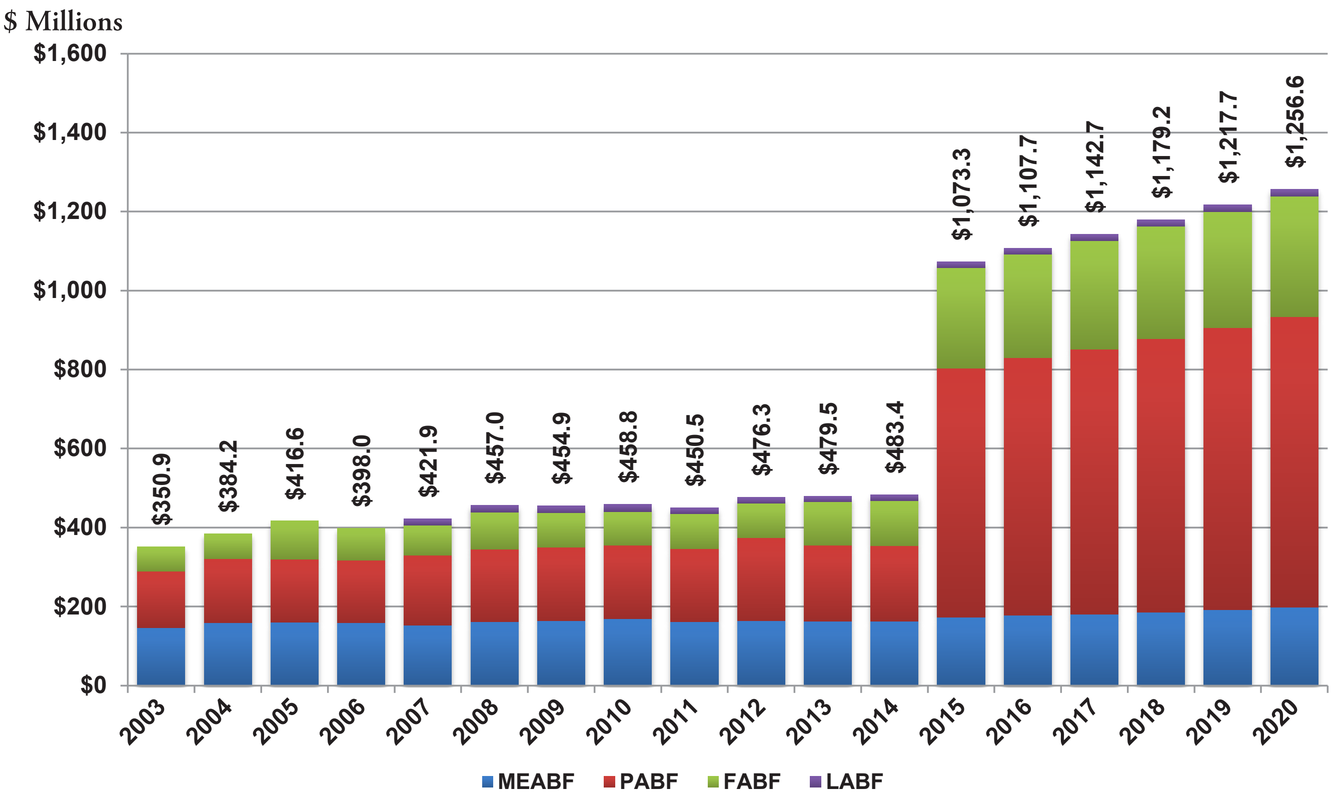
coming from PPRT revenue. Already, as the City's pension contributions have grown, the amount of property tax and PPRT revenue available to the corporate fund for general use has decreased substantially.[39] No property tax revenue has flowed into the corporate fund in recent years, and the amount of PPRT revenue flowing into the corporate fund decreased by 70 percent between 2007 and 2012 due to increasing pension contributions. The amounts required to fully fund the pension system would far outpace these revenues.

This situation puts the retirees, the taxpayers, and every service that the City currently provides at risk. The amounts required to fully fund the City's pension funds under the current system cannot be paid using existing revenue sources without drastically reducing critical City services, including public safety. In order to continue to cover pension costs primarily using property tax revenues, the City would

ALL FUNDS 90 PERCENT FUNDING[40]



HISTORIC AND PROJECTED PENSION CONTRIBUTIONS[40]



39 In recent years, City pension contributions have steadily increased. Though the City has made significant staff reductions, the growth of its pension contributions has not slowed, largely because the staff reductions did not significantly affect police and fire payroll, which constitute a majority of the City's workforce and receive a higher statutory rate of pension contribution from the City.

40 All projections are provided by the pension funds and are based on actuarial assumptions regarding future conditions, which are subject to numerous political, economic, and other factors; while reported projections are the best estimates available at this time, these should be viewed as approximate.

need to increase its 2015 property tax levy by approximately $600 million, significantly increasing the bill of every Chicago taxpayer. As a result, the City is faced with three basic options - institute large tax increases, aggressively reduce City services, or seek fundamental reform of the pension system.

Pension Reform

Given the size of the unfunded liability and the dollar amount that would be required to fully fund, even over many years, tax increases and service reductions cannot be the complete answer. The solution to the pension problem needs to be comprehensive and coordinated, and because the City's pensions are governed by state law, the solution will necessarily include changes to those laws. Governor Quinn and state legislators put forward a number of proposals to address the overall pension issue during 2012 and 2013, but action has yet to be taken.

Mayor Emanuel traveled to Springfield in May of 2012 to deliver a series of pension reform proposals to state legislators and continues to be engaged in this process. The Mayor's proposals acknowledge that major changes must be made in order to protect both the interests of Chicago taxpayers and the retirement security of its workforce. Cost-of-living adjustments at the current rate are unsustainable. Increased employee contributions need to be phased in, and retirement ages are out of line with reality and do not account for longer life expectancies. In addition, the Mayor's proposal includes offering more retirement security choices to new employees, in line with private sector practices. The City remains actively involved in discussions with the Governor and state legislators to ensure that balanced and responsible reform of the pension system occurs.

CITY OF CHICAGO
MAYOR RAHM EMANUEL

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