Tax Caps, The Property Tax Freeze, and Related Considerations

Scott Anderson
Finance Director
Village of Buffalo Grove

Kyle Harding
Partner
Chapman and Cutler LLP

Anthony Miceli
Senior Vice President
Speer Financial, Inc.

I. Tax Caps

Property Tax Extension Limitation Law (PTELL) a.k.a. "Tax Caps"

- Enacted by the Illinois Legislature
  - 1991 – mandatory for the 5 counties bordering Cook County
  - 1995 – extended mandate to Cook County
  - 1996 – extended as option to all other Illinois counties with voter approval
  - 2016 or 2017 – extended to the entire State?
- Law in 39 of 102 counties, representing approximately 80% of the State's population
- Does not supersede home rule powers (under current law)

PTELL (continued)

- Intent of PTELL is to limit the growth of property taxes
  - Caps the **total dollar amount** certain property taxes may increase from year to year
  - Such property taxes can only increase by CPI or 5% (whichever is less) PLUS any new property added to the tax rolls each year
    - Slows the growth of property taxes when property values and assessments are increasing faster than inflation
    - Increases the growth of property taxes when property values and assessments are increasing slower than inflation
  - Allows taxing districts the flexibility to continue to extend taxes to pay non-referendum bonds in an amount equal to its levy year 1994 extension (or year the Cap was voted in) for non-referendum bonds known as the Debt Service Extension Base or DSEB; DSEB now increases by CPI each year (beginning with levy year 2009)

PTELL (continued)

- PTELL *does not*
  - Cap or limit individual property tax assessments – EAV is not capped
  - Cap or limit individual property tax bills
  - Cap or limit certain special purpose property taxes (such as taxes extended to pay pre-Tax Cap, non-referendum bonds or voter-approved bonds)

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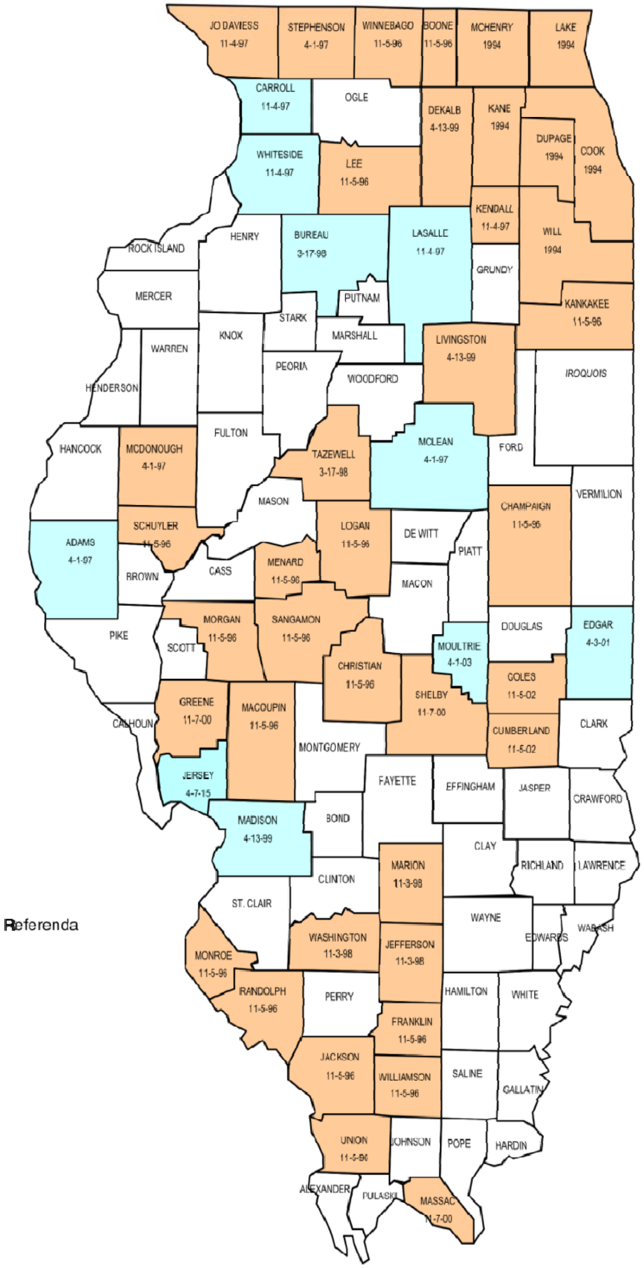
Counties with tax caps:

Boone
Champaign
Christian
Coles
Cook
Cumberland
DeKalb
DuPage
Franklin
Greene
Jackson
Jefferson
Jo Daviess
Kane
Kankakee
Kendall
Lake
Lee
Livingston
Logan
Macoupin
Marion
Massac
McDonough
McHenry
Menard
Monroe
Morgan
Randolph
Sangamon
Schuyler
Shelby
Stephenson
Tazewell
Union
Washington
Will
Williamson
Winnebago

Counties which have defeated Tax Cap Referenda

Adams
Bureau
Carroll
Edgar
Jersey
LaSalle
Madison
McLean
Moultrie
Whiteside

As of April 7, 2015 (Consolidated Election)



PTELL (continued)

- Consumer Price Index (CPI)
  - From Bureau of Labor Statistics
  - “Measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services”
  - % change from December to December
  - Last time CPI over 5% was 1990 (6.1%)
  - 10-year average is 1.9%
  - CPI for levy year 2016 is 0.7%

PTELL (continued)

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
CPI	2.5	4.1	0.1	2.7	1.5	3.0	1.7	1.5	0.8	0.7

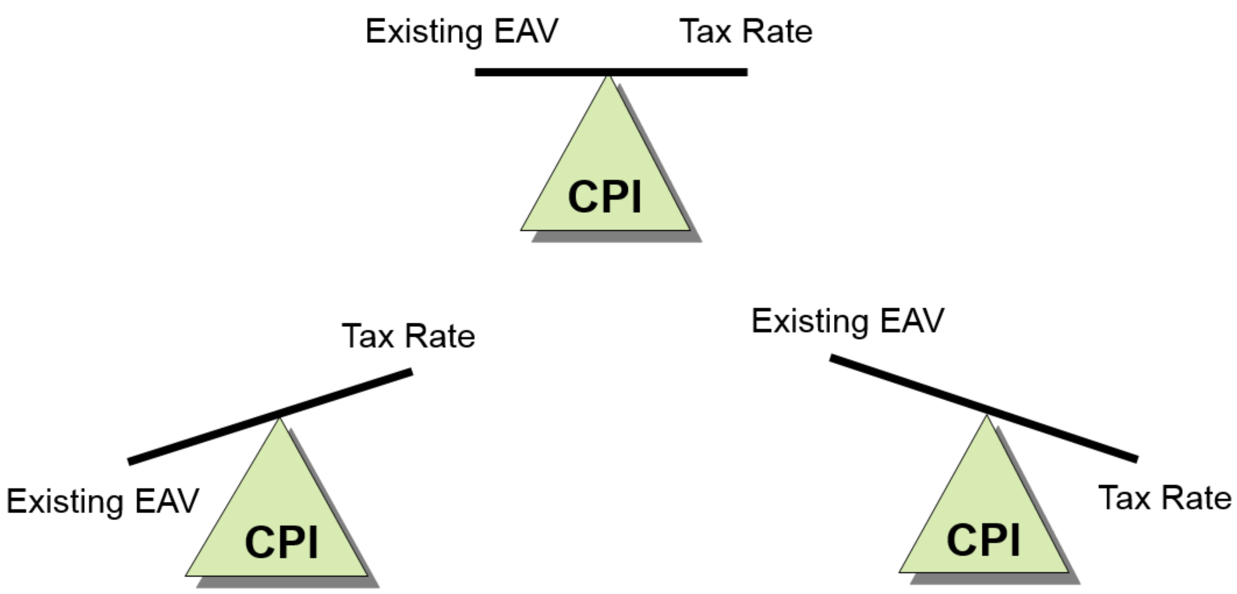
PTELL (continued)

- Limiting Rate Formula
  - Prior Yr Extension x (1+lessor of CPI or 5%)
    Current Year EAV – (New Property and Recovered TIF)
- Some levies are excluded from the Cap; such levies may increase from year-to-year by more than lesser of 5% or CPI
  - Voted bonds, grandfathered (pre-Cap) bonds and alternate bonds
  - Limited bonds (up to amount of DSEB)
- **What can be extended this year is based on what was extended last year**
  - Such maximum amount is known as the “aggregate extension”

Aggregate Extension

- Pie grows by the lesser of 5% or CPI
- Taxing districts can decide how to allocate the pie within statutory maximum rates

EAV Change, CPI and Tax Rate



PTELL Summary

- You are allowed to receive the same amount of money you received last year, ***adjusted for inflation***, provided you levy for it.
  - “New property” and “Recovered TIF” is added on top; you get your full rates against this property
  - New Property: New improvements or additions to existing property on any parcel of real property that increased the assessed value of that real property
- “Same amount of buying power”

II. Property Tax Freeze Legislation

Property Tax Freeze Legislation

- Concept included in Governor Rauner's Turnaround Agenda

  Gov. Rauner: "Property taxes are our number one problem tax, our most uncompetitive tax"

- Proposal: two-year "freeze" on property tax extensions; limit increases to new construction, recovered TIF value and voter-approved rate increases only

- The freeze proposal has been included in numerous bills

- Senate Bill 318, which passed the Senate in August 2015, would effect the freeze by imposing Tax Caps statewide for two years and changing the limiting rate formula for two years as follows:

  - Limiting Rate Formula

    - Prior Yr. Extension x (1 +lessor of CPI or 5% ZERO)

      Current Year EAV – New Property

  - **What can be extended this year is based on what was extended last year**

- Under the Senate Bill 318 Proposal

  - Cook County taxing districts: capped for levy years 2017 (taxes extended in calendar year 2018) and 2018

  - All other taxing districts: capped for levy years 2016 (taxes extended in calendar year 2017) and 2017

III. Property Tax Freeze Legislation and Impact on Debt Issuance

Tax Freeze Legislation Impact on Debt Issuance.

- Illinois Property Tax Limitation Law ("PTELL") is currently in effect for non-home rule units of government in 39 counties.
- Legislation has been introduced, such as SB 318, that would impose PTELL statewide, including on home rule units of government.
- The impact of PTELL limiting the growth of property taxes is not only felt on the operating side of local governments, but also impacts future debt issuance.
  - Limits the total dollar amount of taxes that can be extended to pay non-referendum GO debt.
- The Senate Bill 318 Proposal would not impact the authority for issuers already under PTELL to issue non-referendum GO debt; other tax freeze proposals (such as House Bill 696) would impact borrowing for issuers already under PTELL.

Tax Freeze Legislation Impact on Debt Issuance. (Continued)

- Under PTELL, the total taxes extended to pay non-referendum general obligation bond debt service is limited to an issuer’s Debt Service Extension Base (“DSEB”).
- The DSEB is created the year PTELL goes into effect and is equal to total taxes extended to pay non-referendum bonds in that year.
- Non-referendum GO Bonds issued under PTELL are considered Limited Tax General Obligation Bonds.
  - Property tax is limited as to amount, but unlimited as to rate.
- Non-referendum bonds issued prior to the date PTELL goes into effect would be outside of PTELL, but count against an issuer’s DSEB.
- Referendum approved bonds are outside of PTELL.

Issuance of Non-Referendum Bonds.

- Under PTELL, issuers that wish to issue non-referendum general obligation bonds must limit the annual debt service to their DSEB.
  - Under the SB318 Proposal this would have been in effect for two years, levy years 2016 and 2017 (2017 and 2018 for issuers in Cook County.)
- The bonds are issued as Limited Tax General Obligation Bonds.
- Issuers would also be able to issue non-referendum unlimited tax bonds to refund unlimited tax bonds issued prior to PTELL going into effect.

Debt Service Extension Base.

- The DSEB is created the year PTELL goes into effect and is equal to the total taxes extended for certain non-referendum approved bonds in that year.
- Under the SB318 Proposal the DSEB would have been set by:
  - 2016 Levy for Non-Cook County (Taxes extended in 2017).
  - 2017 Levy for Cook County (Taxes extended in 2018).
- The DSEB grows each year by the lesser of 5% or CPI.
  - The SB 318 Proposal would not impact DSEB growth.
  - HB 696 would eliminate this provision.

Example One

- The example below assumes the tax freeze extends PTELL and establishes the 2017 non-referendum bond extension as the DSEB.
- Assuming no sunset on the tax freeze, this issuer would have significant non-referendum G.O. bonding authority due to its declining annual G.O. debt service.

Levy Year	Bond Year	Current G.O. Debt Service/ Extension	DSEB	DSEB Margin	
2015	2016	$7,240,178			
2016	2017	7,085,500			
2017	2018	7,168,475			***DSEB Established***
2018	2019	7,172,688	$7,168,475	($4,213)	
2019	2020	7,000,575	7,168,475	167,900	
2020	2021	5,497,775	7,168,475	1,670,700	
2021	2022	5,496,550	7,168,475	1,671,925	
2022	2023	5,206,100	7,168,475	1,962,375	
2023	2024	5,207,200	7,168,475	1,961,275	
2024	2025	4,408,250	7,168,475	2,760,225	
2025	2026	3,960,050	7,168,475	3,208,425	
2026	2027	2,410,750	7,168,475	4,757,725	
2027	2028	2,409,450	7,168,475	4,759,025	
2028	2029	2,406,650	7,168,475	4,761,825	
2029	2030	2,407,350	7,168,475	4,761,125	
2030	2031	2,406,400	7,168,475	4,762,075	
2031	2032	2,408,800	7,168,475	4,759,675	
2032	2033	2,409,600	7,168,475	4,758,875	
2033	2034	2,407,200	7,168,475	4,761,275	
2034	2035	2,406,600	7,168,475	4,761,875	
2035	2036	2,407,600	7,168,475	4,760,875	

Example Two

- The example below assumes the tax freeze extends PTELL and establishes the 2017 non-referendum bond extension as the DSEB.
- Assumes the same debt pattern as Example One, except this issuer annually abates a portion of its debt service each year (Approximately 35%).
- Assuming no sunset on the tax freeze, this issuer wouldn't have DSEB capacity until the 2024 levy year.

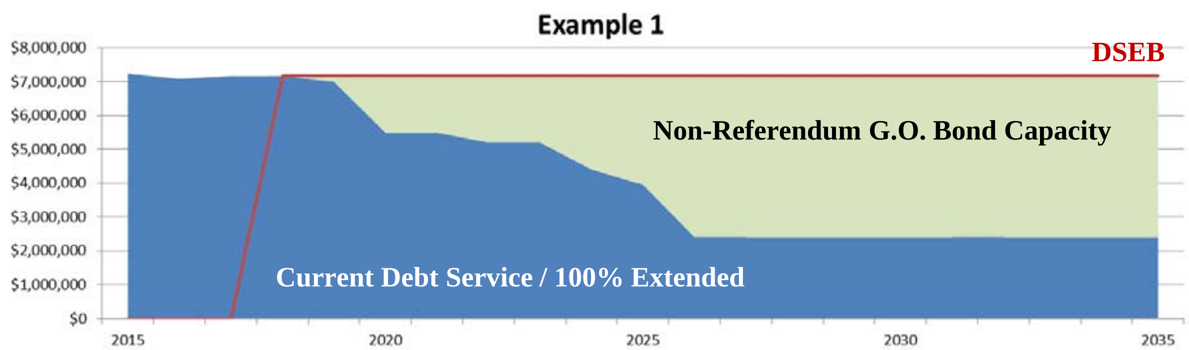
Levy Year	Bond Year	Current G.O. Debt Service	Debt Service Extension (65% of Total)	DSEB	DSEB Margin	
2015	2016	$7,240,178	$4,706,116			
2016	2017	7,085,500	4,605,575			
2017	2018	7,168,475	4,659,509			***DSEB Established***
2018	2019	7,172,688	4,662,247	$4,659,509	($2,513,179)	
2019	2020	7,000,575	4,550,374	4,659,509	(2,341,066)	
2020	2021	5,497,775	3,573,554	4,659,509	(838,266)	
2021	2022	5,496,550	3,572,758	4,659,509	(837,041)	
2022	2023	5,206,100	3,383,965	4,659,509	(546,591)	
2023	2024	5,207,200	3,384,680	4,659,509	(547,691)	
2024	2025	4,408,250	2,865,363	4,659,509	251,259	
2025	2026	3,960,050	2,574,033	4,659,509	699,459	
2026	2027	2,410,750	1,566,988	4,659,509	2,248,759	
2027	2028	2,409,450	1,566,143	4,659,509	2,250,059	
2028	2029	2,406,650	1,564,323	4,659,509	2,252,859	
2029	2030	2,407,350	1,564,778	4,659,509	2,252,159	
2030	2031	2,406,400	1,564,160	4,659,509	2,253,109	
2031	2032	2,408,800	1,565,720	4,659,509	2,250,709	
2032	2033	2,409,600	1,566,240	4,659,509	2,249,909	
2033	2034	2,407,200	1,564,680	4,659,509	2,252,309	
2034	2035	2,406,600	1,564,290	4,659,509	2,252,909	
2035	2036	2,407,600	1,564,940	4,659,509	2,251,909	

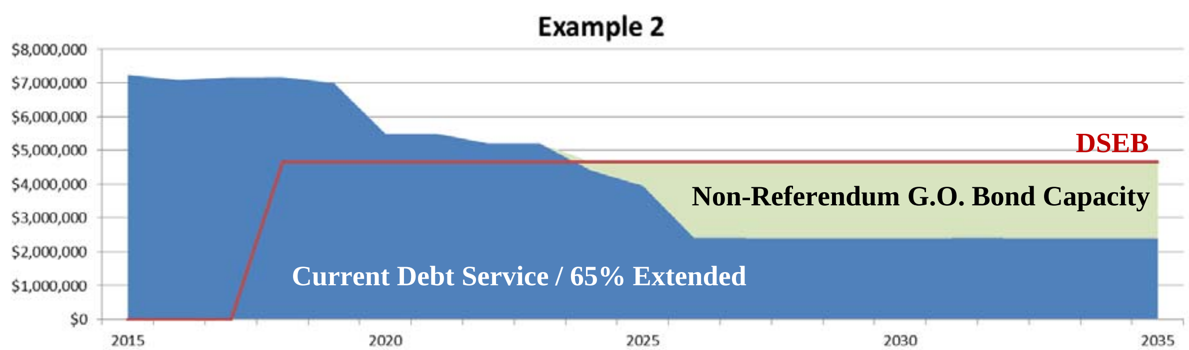
Example Three

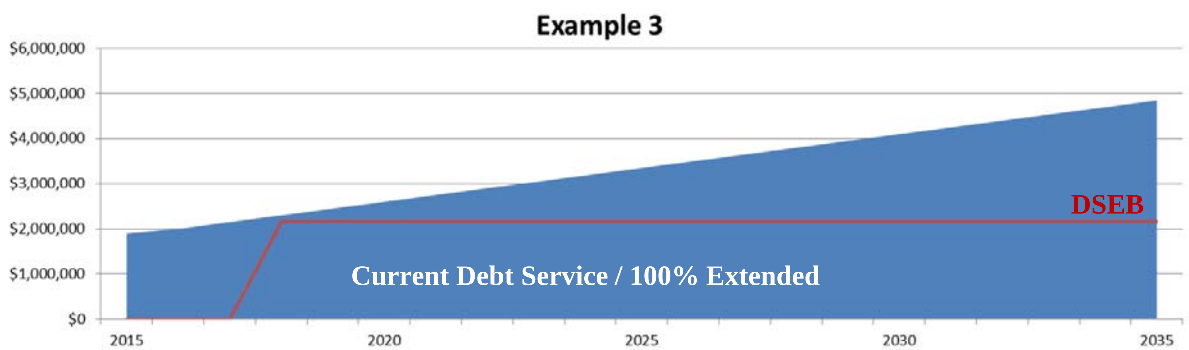
- The example below assumes the tax freeze extends PTELL and establishes the 2017 non-referendum bond extension as the DSEB.
- In the example below, the issuer's debt is increasing annually.
- Assuming no sunset on the tax freeze, this issuer wouldn't have DSEB until its current debt is retired or restructured.

Levy Year	Bond Year	Current G.O. Debt Service/ Extension	DSEB	DSEB Margin	
2015	2016	$1,900,000			
2016	2017	2,000,000			
2017	2018	2,150,000			***DSEB Established***
2018	2019	2,300,000	$2,150,000	($150,000)	
2019	2020	2,450,000	2,150,000	(300,000)	
2020	2021	2,600,000	2,150,000	(450,000)	
2021	2022	2,750,000	2,150,000	(600,000)	
2022	2023	2,900,000	2,150,000	(750,000)	
2023	2024	3,050,000	2,150,000	(900,000)	
2024	2025	3,200,000	2,150,000	(1,050,000)	
2025	2026	3,350,000	2,150,000	(1,200,000)	
2026	2027	3,500,000	2,150,000	(1,350,000)	
2027	2028	3,650,000	2,150,000	(1,500,000)	
2028	2029	3,800,000	2,150,000	(1,650,000)	
2029	2030	3,950,000	2,150,000	(1,800,000)	
2030	2031	4,100,000	2,150,000	(1,950,000)	
2031	2032	4,250,000	2,150,000	(2,100,000)	
2032	2033	4,400,000	2,150,000	(2,250,000)	
2033	2034	4,550,000	2,150,000	(2,400,000)	
2034	2035	4,700,000	2,150,000	(2,550,000)	
2035	2036	4,850,000	2,150,000	(2,700,000)	

Graphical Comparison of Examples







Considerations

- Review your current bond and interest levy.
  - Do you have outstanding bonds that will produce a DSEB?
  - Does your current schedule allow for future bonding capacity?
  - Will the DSEB be sufficient for your future capital needs?

Other Borrowing Options.

- Other non-referendum borrowing options exist for issuers currently subject to PTELL.
  - Debt Certificates:
    - No property tax levy. A general obligation of the issuer payable from operating funds.
    - Generally rated one notch below the issuers G.O. rating.
    - Generally trade at higher interest rates than G.O. bonds because of the lack of property tax backup.
    - No referendum or backdoor referendum required.
  - G.O. Alternate Revenue Source Bonds:
    - A payment source (which may be an enterprise revenue or a general source of funds available to the issuer) must be identified and pledged as the primary security for repayment of the bonds.
    - The bonds are additionally secured by a an unlimited property tax.
    - Tax is abated each year as long as the revenues are sufficient.
    - Requires 1.25x revenue coverage (1.10x for a governmental revenue source).
    - Trade at the same level as general obligation bonds.
    - No direct referendum required, but subject to a 30-day backdoor petition period.

Other Borrowing Options. (continued)

- Other non-referendum borrowing options exist for issuers currently subject to PTELL.
  - Revenue Bonds:
    - Revenue Bonds rely on the sale of a product or service (water, sewage disposal, electricity, etc.) to generate sufficient revenues to pay operating and maintenance expenses and principal and interest on revenue bonds.
    - Payment period cannot be longer than the lesser of 40 years or the useful life of the project.
    - Covenants regarding coverage, rate setting, operating requirements as well as the creation of reserves (Debt Service Reserve).
    - Bond rating is dependent on strength of security, revenue coverage, bond covenants (additional bonds test, debt service reserve requirements, etc.).
    - Generally trade at higher interest rates than general obligation bonds.

IV. How the Tax Freeze Legislation May Effect Your Local Government.

Communicating Financial Impact to Elected Board

- Educate the elected board on SB 318
  - Genesis behind the legislation.
  - Inconsistency of proposal in fixing state financial problems.
    - Capping property tax revenue does nothing to address the state budget issues.
    - Direct impact to local services.
  - Belief in shared financial solutions.
    - "Show them death, they'll accept pain."
  - Review the components of the levy, remind the public the services that are funded through the property tax.

Communication Cont'd

- Project the impact of a property tax freeze on the budget.
  - Show actual dollar impact and translate that cost to service impairment.
  - First step is to align core revenues to core services.
    - The greater the perceived stability of revenue the higher the priority of the service.
      - Corporate Levies = public safety and public works.
    - Acknowledge publically which services may be at risk if property tax levies are frozen.
  - Forecast the impact into future years.
    - General Fund Proforma.
    - Capital Improvement Plan.
    - Review debt schedules – Identify future borrowing needs.

Surviving the Freeze

- Options to Weather the Freeze.
- Debt Options – Referendum vs. Non Referendum.
  - Alternate Revenue Source Bonds.
  - Revenue Bonds.
  - Line of Credit.
  - Issuance of GO Debt in advance of legislation.
- Operating Budget
  - Defer Capital/Reserve Transfers.
  - Increase tax levy in anticipation of a freeze.
  - Modify tax levy to shift funds to Fire Protection (65 ILCS 5/11-7-1, 5/11-7-3) and/or Police Protection (65 ILCS 5/11-1-3, 5/11-1-5.1).
  - Do nothing and bridge shortfall with existing reserves if necessary.

Capitalize on Crisis

- Opportunities Emerge From The Freeze.
  - Assume the freeze has long term implications.
  - Work with collective bargaining units to solve the revenue gap.
  - Review "Corporate Drift" with the elected board and try to eliminate services that have minimal tie-in to organizational mission.
  - Continue to communicate with the stakeholders as to future budget decisions.
  - Never waste a good crisis!