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Oak Park (Village of) IL

Update to credit analysis

Summary

Oak Park, IL's (A1) economic profile is stable and supported by the village's ties to the City of Chicago and strong residential income. The village's broad legal authority to raise local revenues as a home rule unit of government is also a key credit strength. These strengths are balanced against credit challenges that include narrow operating liquidity and very high pension and fixed cost burdens relative to most US local governments. The village's unfunded pension burden is very high and growing despite rising pension contributions that account for a large share of annual operating revenue.

In addition to general obligation debt, the village has issued bonds secured by local and state shared sales taxes. The rating on these bonds is heavily influenced by the village's general obligation credit profile. At the same time, the sales tax trend is stable and pledged taxes provide strong coverage of debt service.

Credit strengths

- Large and affluent tax base closely tied to Chicago (Ba1 negative) economy
- Broad legal authority to raise local taxes and fees without voter approval
- Strong coverage of debt service on bonds secured by sales taxes

Credit challenges

- Improved but still narrow operating liquidity
- Very high and growing pension and fixed cost burdens

Rating outlook

Outlooks are generally not applied to local governments with this amount of debt.

Factors that could lead to an upgrade

- Sustained improvement in operating fund balance and liquidity
- Moderated leverage and fixed cost burden

Factors that could lead to a downgrade

- Growth in village leverage or fixed costs
- Narrow fund balance or operating liquidity

Key indicators

Exhibit 1

Oak Park (Village of) IL	2012	2013	2014	2015	2016
Economy/Tax Base					
Total Full Value ($000)	$4,795,507	$4,414,903	$4,111,760	$4,153,171	$4,007,332
Population	51,781	51,902	51,988	52,080	52,080
Full Value Per Capita	$92,611	$85,062	$79,091	$79,746	$77,245
Median Family Income (% of US Median)	163.5%	169.6%	170.0%	172.6%	172.6%
Finances					
Operating Revenue ($000)	$49,400	$52,621	$54,341	$55,728	$59,687
Fund Balance ($000)	$3,238	$5,675	$5,964	$5,865	$10,768
Cash Balance ($000)	$177	$918	$45	$1,289	$6,836
Fund Balance as a % of Revenues	6.6%	10.8%	11.0%	10.5%	18.0%
Cash Balance as a % of Revenues	0.4%	1.7%	0.1%	2.3%	11.5%
Debt/Pensions					
Net Direct Debt ($000)	$77,284	$83,490	$77,646	$80,822	$101,597
3-Year Average of Moody's ANPL ($000)	$167,466	$189,166	$216,753	$255,657	$297,751
Net Direct Debt / Operating Revenues (x)	1.6x	1.6x	1.4x	1.5x	1.7x
Net Direct Debt / Full Value (%)	1.6%	1.9%	1.9%	1.9%	2.5%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	3.4x	3.6x	4.0x	4.6x	5.0x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	3.5%	4.3%	5.3%	6.2%	7.4%

Source: Village's audited financial statement, Moody's Investors Service and the US Census

Profile

The Village of Oak Park lies along Chicago's western border and is home to an estimated population of 52,100.

Detailed credit considerations

Economy and tax base: affluent, mature base borders Chicago

Oak Park's high income, metro Chicago base will remain a key credit strength for some time. The village borders Chicago to the west and is closely connected to the latter's central business district via the regional expressway and rail system. Oak Park also contains its own vibrant commercial sector and an employment base anchored by West Suburban Hospital Medical Center and Rush Oak Park Hospital. The village's tax base is currently valued at $4.2 billion, or 25% below its prerecessionary peak. However, village officials anticipate additional growth of 20% to 25% with the triennial reassessment in 2018.

Financial operations and reserves: despite improvements, operating liquidity remains limited

Despite operational improvements, the village's reserves will remain limited relative to similarly rated governments. The village closed fiscal 2016 with a general fund operating surplus of $841,000. When incorporating transfers and proceeds from the sale of village assets, available general fund reserves increased by $3.2 million to $8.5 million and 15.5% of general fund revenue. General fund reserves have improved in recent years due to the repayment of interfund loans from the village's parking enterprise and significant reductions in expenditures such as payroll. Back in 2007, village's parking fund owed the general fund $10.4 million. Presently, this interfund loan is down to $1.9 million.

The combined available general and debt service fund balance was an adequate 18% of revenue in 2016. The village adopted a balanced fiscal 2017 budget. The year closed on December 31, 2017 and the village estimates recording a surplus of between $300,000 and $1 million. The village's fiscal 2018 budget reflects a modest operating deficit that it expects to close by the end of the year with positive variances.

The village pledges collection of its home rule and state shared sales taxes to repayment of certain outstanding bonds. Fiscal 2016 sales taxes covered currently scheduled maximum annual debt service 5.2x.

LIQUIDITY

Operating liquidity improved significantly in fiscal 2016 after repayment of some interfund loans. However, liquidity remains below fund balance due to outstanding interfund receivables in the general fund.

Across all governmental funds, available cash totaled $30.0 million and a healthy 39% of governmental revenues. Net of $9.3 million and $5.6 million within the village's Madison Street TIF and non-major capital project funds, available governmental liquidity was $14.4 million and 19% of governmental revenue.

Debt and pensions: high debt and pension burdens are key credit weaknesses

Oak Park carries very high leverage and this will remain a credit challenge. The village's net direct debt burden of 2.8% of full valuation and 1.9x operating revenue includes bonds it is preparing to sell while also excluding bonds actively repaid by its water and sewer enterprise.

The village's three-year average Moody's adjusted net pension liability (ANPL) climbed to 5.0x revenue in fiscal 2016 from 3.4x revenue in fiscal 2012. The ANPL is our measure of a local government's pension burden that uses a market-based interest rate to value accrued liabilities.

Fixed costs, consisting of debt service and retirement plan contributions, were a high 30% of operating revenue in 2016 and will likely grow in the coming years.

DEBT STRUCTURE

All debt of the village is fixed rate. Debt service level and 60% of principal is set to be retired over the next ten years. The village has $9 million of sales tax bonds outstanding, which carry an additional bonds test of 1.5x debt service. The village is responsible for transferring pledged sales taxes to the bond trustee.

DEBT-RELATED DERIVATIVES

The village has no derivative exposure.

PENSIONS AND OPEB

Oak Park manages two single-employer, defined benefit pension plans and is also a member of the Illinois Municipal Retirement Fund (IMRF), a defined benefit, multi-employer agent plan. Key sources of growth in the village's pension burden in recent years include investment returns that have fallen short of plan assumptions, changes in mortality assumptions, and village contributions that, while closely conforming with actuarially determined contributions, have not been sufficient to fully cover annual interest accruals on accumulated unfunded liabilities.

Net of enterprise support, Oak Park's fiscal 2016 pension contribution was $10 million and a high 16.8% of operating revenue. The village's public safety plans are by far the largest of its plans, and Oak Park contributed $8.5 million to the public safety plans in fiscal 2016. This public safety plan contribution was $2.8 million short of the amount necessary to forestall growth in the plans' reported net pension liabilities assuming other plan assumptions hold, that is, tread water.[1]

The gap between the village's public safety pension contributions and the two plans' aggregate 'tread water' needs was nearly 4% of revenue in fiscal 2016. This was up from 3% of revenue in fiscal 2015. The village reportedly increased public safety plan contributions $2.2 million in fiscal 2017, which could bring the total payment close to the level of treading water.

A pension plan's 'tread water' indicator, as calculated by Moody's, is heavily influenced by its reported discount rate. The village's two single employer plans use a discount rate of 6.5%, which is lower than that used by most US public pension plans. Still, pension contributions that tread water will not necessarily reduce a local government's ANPL. Furthermore, even if Oak Park reaches a tread water funding level in its public safety plans, the village will likely be using over 20% of annual revenue to make pension payments. This is a high funding burden among US local governments and a potential source of budgetary strain.

Unfunded OPEB liabilities do not pose a credit challenge to the village. Oak Park has a modest OPEB unfunded actuarial accrued liability of $10.4 million and 0.2x operating revenue. The village's pay-go contribution in fiscal 2016 was 0.9% of revenue.

Management and governance: moderate institutional framework enhanced by broad legal authority to raise local revenue

Illinois cities have an Institutional Framework score of A, or moderate. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. Revenue-raising ability is moderate overall but varies considerably. Home rule entities, like Oak Park, have substantial revenue-raising authority. The village can raise various local taxes and fees without approval by voters or the state. Expenditures are moderately predictable but cities have limited ability to reduce them given costs for pension benefits that enjoy strong constitutional protections. Revenue predictability is moderate, with varying dependence on property, sales, and stated distributed income taxes.

Endnotes

1 Our "tread water" indicator measures the annual government contribution required to prevent reported net pension liabilities from growing, given the entity's actuarial assumptions. An annual government contribution that treads water equals the sum of employer service cost and interest on the reported net pension liability at the start of the fiscal year. A pension plan that receives an employer contribution equal to tread water will end the year with an unchanged net pension liability relative to the beginning of the year if all plan assumptions hold. Net liabilities may decrease or increase in a given year due to factors other than the contribution amount, such as investment performance that exceeds or falls short of a plan's assumed rate of return. Still, higher contributions will always reduce unfunded liabilities faster, or will allow unfunded liabilities to grow more slowly than lower contributions. The degree to which contributions fall below the "tread water" indicator can help quantify a structural operating imbalance stemming from pensions, even under reported assumptions. A contribution below the "tread water" level in effect suppresses expenditures by leaving an implied interest on net pension liabilities unpaid, akin to borrowing at the assumed rate of return for operations.

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