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# Oswego (Village of) IL

Update to credit analysis

## Summary

The Village of Oswego (Aa2) benefits from strong resident income levels and a healthy financial profile supported by growing reserves and broad legal flexibility to raise revenue. The village's strengths are balanced against its dependence on economically sensitive revenue and above average leverage related to long-term debt and pension burdens. Favorably, the village's local economy and financial performance remained relatively stable throughout the coronavirus pandemic.

## Credit strengths

» Strong resident income levels

» Healthy financial profile supported by growing reserves

» Financial flexibility derived from home rule status

## Credit challenges

» Reliance on economically sensitive sales and state shared income tax revenue

» Above average leverage related to long-term debt and pension burdens

## Rating outlook

Outlooks are typically not assigned to local governments with this amount of debt.

## Factors that could lead to an upgrade

» Significant and sustained growth in the tax base

» Substantial moderation of the debt and pension burdens

## Factors that could lead to a downgrade

» Material and sustained weakening of reserves

» Growth in the village's debt or pension burden

## Key indicators

Exhibit 1

| Oswego (Village of) IL | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|
| Economy/Tax Base | | | | | |
| Total Full Value ($000) | $2,350,876 | $2,495,596 | $2,621,694 | $2,778,992 | $2,922,506 |
| Population | 33,245 | 33,759 | 34,383 | 34,933 | 34,933 |
| Full Value Per Capita | $70,714 | $73,924 | $76,250 | $79,552 | $83,660 |
| Median Family Income (% of US Median) | 152.7% | 156.6% | 152.5% | 148.7% | 148.7% |
| Finances | | | | | |
| Operating Revenue ($000) | $17,505 | $17,909 | $19,310 | $21,588 | $24,759 |
| Fund Balance ($000) | $6,465 | $5,473 | $6,499 | $8,858 | $14,869 |
| Cash Balance ($000) | $3,801 | $2,814 | $4,194 | $6,461 | $12,701 |
| Fund Balance as a % of Revenues | 36.9% | 30.6% | 33.7% | 41.0% | 60.1% |
| Cash Balance as a % of Revenues | 21.7% | 15.7% | 21.7% | 29.9% | 51.3% |
| Debt/Pensions | | | | | |
| Net Direct Debt ($000) | $13,050 | $38,815 | $37,480 | $36,195 | $49,455 |
| 3-Year Average of Moody's ANPL ($000) | $32,393 | $38,742 | $42,719 | $42,609 | $52,293 |
| Net Direct Debt / Full Value (%) | 0.6% | 1.6% | 1.4% | 1.3% | 1.7% |
| Net Direct Debt / Operating Revenues (x) | 0.7x | 2.2x | 1.9x | 1.7x | 2.0x |
| Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%) | 1.4% | 1.6% | 1.6% | 1.5% | 1.8% |
| Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x) | 1.9x | 2.2x | 2.2x | 2.0x | 2.1x |

*Source: US Census Bureau, Oswego (Village of) IL's financial statements and Moody's Investors Service*

## Profile

The Village of Oswego encompasses about 14 square miles and is in Kendall County in northeastern Illinois, approximately 40 miles southwest of downtown Chicago (Ba1 negative). The village's governmental services include administration, building and zoning, community development, public works and public safety. The village also owns and operates a waterworks and sewerage system with 165 miles of water mains, eight wells, and six towers with a total storage capacity of 5.3 million gallons. Sewage treatment is provided by the Fox Metro Water Reclamation District. The village's population totals about 35,000 residents.

## Detailed credit considerations

### Economy and tax base: moderately sized tax base in suburban Chicago

The village's tax base is likely to continue growing given the current levels of development underway coupled with continued strong population growth. The village's current tax base is primarily residential (85%) and it has a small commercial presence (14%). The last six consecutive years of growth have pushed the tax base to just over $3 billion. A combination of market appreciation and new construction is driving the growth. The annual value of building permits have ranged from $40 million to $100 million in recent years, with the current year at about $40 million as of June. Recent residential developments include 61 new single family homes completed in 2021 and a 280 unit luxury apartment building that was recently completed and is about 60% leased. Management estimates that the recent housing developments will add about 2,000 new residents to the village. There is also a $69 million mixed use development underway in the village's downtown.

The village has experienced tremendous population growth in recent decades, as shown by a 244% population growth rate from 1990 to 2000 and a 128% increase from 2000 to 2010. The population reached more than 30,000 by the 2010 census, a level which exceeds the 25,000 population threshold required to achieve home rule status in Illinois. Median family income for the village is strong at about 149% of the national figure.

## Financial operations and reserves: healthy financial profile supported by Home Rule authority

The village's financial operations are expected to remain stable because the village benefits from significant financial flexibility derived from its home rule status. The village's economically sensitive revenue streams were relatively resilient throughout the coronavirus pandemic. The village's fiscal 2021 (April 30 year end) budget reflected a small $44,000 surplus but management notes that the year has performed better than budget and current estimates reflect a surplus of about $2.6 million. The fiscal 2022 budget also reflects a small surplus and, similar to the prior year, is performing better than budget.

The village has a strong operating history with consistent operating surpluses and growing reserves. Most recently, the village closed fiscal 2020 a combined available fund balance to $14.9 million, equal to 60% of revenue across the general fund, motor vehicle sales tax fund and the debt service fund. Rapid population growth has fueled commensurate commercial expansion, bolstering the village's sales tax collections which has been an important factor in the positive financial performance.

The village's primary revenue streams include sales taxes (34%), sate shared revenue (20%) and other taxes (14%). The village's notable reliance on economically sensitive revenue streams is partially mitigated by its financial flexibility as a home-rule unit of government. The village can implement a variety of revenue enhancements and has broad ability to increase property taxes and sales taxes. The village has increased its home rule sales tax rate by 0.75% (to rate of 1.25%) and also increased the local food and beverage tax and the local motor fuel tax in recent years.

### Liquidity

The village closed fiscal 2020 with a net cash position of $12.7 million, equal to 51% of revenue across the general fund, motor vehicle sales tax fund and the debt service fund. The village maintains about $3.8 million in the capital projects fund and $5 million in the water and sewer capital fund, both of which are sources of alternate liquidity should the village need to access additional liquidity for operations.

## Debt and pensions: above average leverage

The village's overall leverage will likely remain above average given the current debt and pension burdens and the relatively slow payout of existing debt. The village's overlapping debt burden is above average at about 6% of full value, largely reflecting substantial school district borrowing in the surrounding area. Inclusive of the village's 2021 general obligation unlimited tax (GOULT) refunding bonds, the net debt burden totals about $52 million, equal to 1.7% of full value and 2.1x revenue. All of the village's direct debt is currently supported by alternate revenue sources, including water and sewer fees, as well as sales and motor fuel tax receipts. The village may issue about $3 million in GOULT bonds to finance parking for Phase II of a downtown development in the next year.

The three year average Moody’s adjusted net pension liability (ANPL) for the village, which incorporates our adjustments to reported pension information, is about $53 million, equal to 1.7% of full value and 2.1x operating revenue. Total fixed costs, inclusive of debt service and retirement contributions, were equal to about 18% of revenue in fiscal 2020.

### Legal security

The GOULT bonds are secured by the village's general obligation unlimited tax pledge to levy a tax unlimited as to rate or amount.

### Debt structure

All of the village's outstanding debt is fixed rate. Principal amortization is below average with a little more than 50% of GO debt retired within 10 years.

### Debt-related derivatives

The village has no debt related derivatives.

### Pensions and OPEB

The village has one single employer public safety pension plans and its non-public safety employees participate in the Illinois Municipal Retirement Fund (IMRF). The village's public safety plan account for a majority of its ANPL. Although the village’s public safety plan is a single employer plan, the village has no control over the benefits because they are established by state statute.

The village's pension contributions amounted to about 7% of its operating revenue in fiscal 2020. The village sizes its annual contributions to achieve a 100% funded ratio by 2040. The state requires cities to fund single employer public safety plans at a rate that will achieve a 90% funded ratio on a reported basis by 2040, which is a relatively weak contribution requirement. While the village's contributions exceeded this requirement, its contributions fell slightly below our “tread water” indicator though the amount was modest compared to the size of the village's operating budget. The tread water indicator represents the contribution required to prevent growth in reported net pension liabilities, if plan assumptions hold. In fiscal 2020, the village's tread water indicator was based on an assumed discount rates of 6.5% for public safety plan and 7.25% for IMRF. The reported discount rate for public safety plan is similar to many other local government pension plans. A lower discount rate tends to push the tread water indicator upward, which can result in a wider gap between the indicator and actual contributions.

OPEB obligations do not represent a material credit risk for the village. The village does not offer explicit OPEB benefits, but allows retired employees to stay on its healthcare plan, creating an implicit rate subsidy. Both on a reported bases and on our adjusted basis, which uses a different discount rate, the village's OPEB liability is less than $2 million.

## ESG considerations

### Environmental

According to data from Moody’s affiliate Four Twenty Seven, Kendall County's environmental hazard scores reflect high risk for the three of the five environmental factors considered including heat stress, water stress and extreme rainfall. Environmental factors have not had a negative impact on the village's credit profile and the strong reserve position and broad revenue raising flexibility will be important mitigating factors should environmental pressures develop going forward. The village's capital improvement plan is updated annually and currently covers fiscal years 2022 through 2041. The proactive and long-term capital planning will support resiliency should environmental factors begin to have a negative impact on the village's credit profile.

### Social

Social considerations support the village's credit profile. The median age of village residents (37) is in line with the state (38) and national (38) medians. The village's population has been growing rapidly since the 1990s, increasing to 35,000 residents in 2019 from less than 4,000 in 1990. Median family incomes are strong, equal to about 149% of the national median.

### Governance

Illinois cities have an institutional framework score [1] of "A," which is moderate. Revenue-raising ability is moderate overall but varies considerably. Non-home rule entities are subject to tax rate limitations. In addition, total operating tax yield for entities subject to the Property Tax Extension Limitation Law (PTELL) is capped to the lesser of 5% or CPI growth, plus new construction. Home rule entities have much greater legal flexibility than the rest of the sector with substantial revenue-raising authority. Revenue predictability is moderate, with varying dependence on property, sales, and state-distributed income taxes. Expenditures are moderately predictable but cities have limited ability to reduce them given strong public sector unions and pension benefits that enjoy strong constitutional protections. Fixed costs are driven mainly by debt service and employer pension contributions. For single employer public safety plans, the State of Illinois requires most entities to make annual pension contributions that cover current benefit accruals, plus an amount designed to achieve a 90% funded ratio by 2040.

The Village operates under the village president/board of trustees form of government. The legislative body consists of the President and a Board of six trustees, all elected on an at-large basis to overlapping four-year terms. The Village Administrator is responsible for the day-to-day affairs of the Village. Oswego's home rule status provides significant financial flexibility as it is not subject to property tax levy limits, has no statutory debt ceiling and has the power to impose a variety of taxes without voter approval. The village has demonstrated a willingness to use its home rule authority, increasing revenue to produce strong financial performance. Furthermore, the village benefits from sound financial planning practices, including a detailed financial forecasting and capital planning process.

## Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 2

**Oswego (Village of) IL**

| Scorecard Factors and Subfactors | Measure | Score |
|---|---|---|
| Economy/Tax Base (30%) [1] | | |
| Tax Base Size: Full Value (in 000s) | $3,036,743 | Aa |
| Full Value Per Capita | $86,931 | Aa |
| Median Family Income (% of US Median) | 148.7% | Aa |
| Finances (30%) | | |
| Fund Balance as a % of Revenues | 60.1% | Aaa |
| 5-Year Dollar Change in Fund Balance as % of Revenues | 29.1% | Aaa |
| Cash Balance as a % of Revenues | 51.3% | Aaa |
| 5-Year Dollar Change in Cash Balance as % of Revenues | 29.5% | Aaa |
| Management (20%) | | |
| Institutional Framework | A | A |
| Operating History: 5-Year Average of Operating Revenues / Operating Expenditures (x) | 1.1x | Aaa |
| Notching Adjustments:[2] | | |
| Other Scorecard Adjustment Related to Management: Home Rule | | Up |
| Debt and Pensions (20%) | | |
| Net Direct Debt / Full Value (%) | 1.7% | Aa |
| Net Direct Debt / Operating Revenues (x) | 2.1x | A |
| 3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%) | 1.7% | Aa |
| 3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x) | 2.1x | A |
| Notching Adjustments:[2] | | |
| Other Scorecard Adjustment Related to Debt and Pensions: High overlapping debt | | Down |
| | Scorecard-Indicated Outcome | Aa1 |
| | Assigned Rating | Aa2 |

1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
*Source: US Census Bureau, audited financial statements and Moody's Investors Service*

## Endnotes

1 The institutional framework score assesses a municipality's legal ability to match revenues with expenditures based on its constitutionally and legislatively conferred powers and responsibilities. See US Local Government General Obligation Debt (July 2020) methodology report for more details.

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