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Richmond, California Richmond Joint Powers Financing Authority; Appropriations; General Obligation; Note

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Credit Profile		
US$7.659 mil 2011-12 TRANs due 10/31/2012		
Short Term Rating	SP-1+	New
Richmond ICR		
Long Term Rating	A+/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'SP-1+' short-term rating to Richmond, Calif.'s series 2011-2012 tax and revenue anticipation notes (TRANs). In addition, Standard & Poor's affirmed its 'A+' issuer credit rating (ICR) and 'A' long-term rating on the Richmond Joint Powers Financing Authority's series 2009 lease revenue refunding bonds, which are an obligation of the city. The outlook on the long-term ratings is stable.

The rating on the TRANs reflects our view of the city's:

- Strong underlying general credit characteristics ('A+' ICR);
- Structural provisions that include early set-asides of pledged revenues;
- Strong pro forma debt service coverage of 1.6x at note maturity; and
- Access to additional liquidity sources that boost coverage at maturity to a very strong 6.1x.

The notes are secured by unrestricted taxes, income, revenue, cash receipts, and other general fund money that the city receives for the general fund during fiscal 2012 or attributable to fiscal 2012. We understand that the city plans to use note proceeds to fund seasonal cash deficits during the fiscal year.

Management projects that the city's general fund will hold $4.5 million on the TRANs' Oct. 31, 2011 maturity, which would cover TRANs principal and interest by 1.6x, which we consider good. At covenanted set-aside dates and fiscal year-end, coverage is higher:

- January 2012 (20% of principal): 9.1x
- February 2012 (20% of principal): 8.4x
- April 2012 (60% of principal and full interest): 3.3x
- June 2012: 2.1x

In addition, management anticipates that the city will be able to temporarily tap other funds during the fiscal year for cash flow needs. Should these sources total $35.2 million, as management anticipates, combined available resources would bring coverage at maturity to 6.1x, which we consider very strong.

The 'A' long-term rating reflects our opinion of the city's:

- Significant local job base, as well as access to broad employment opportunities throughout the Bay Area;

- Record of maintaining a strong-to-very-strong financial position; and
- Strong management policies and practices.

Partially offsetting these strengths is our view of the city's:

- Revenue structure that has substantial exposure to a single petroleum products manufacturer;
- Moderate-to-high debt burden.

The 'A+' ICR represents our view of the city's full faith and credit, including unlimited ad valorem taxing power. The 'A' appropriation rating represents our view of a pledge of lease payments made by the city, as lessee, to the authority, as lessor, for the use of city facilities. The city has covenanted to budget and appropriate for lease payments during the life of the obligations.

The city encompasses a population of 103,661 in the northern portion of the San Francisco Bay Area. A break-bulk port and major oil refining facilities anchor a regional logistics and industrial cluster, and residents have good regional freeway and commuter rail access to other jobs centers, including San Francisco, located 18 miles to the southwest. We consider income indicators to be good, with median household and per capita effective buying incomes at 104% and 90% of the U.S. levels, respectively. Similar to much of the state, the city's total assessed value (AV) has declined in recent years, by a 7.4% average annual rate from its fiscal 2009 peak to $10.8 billion, although this includes a 5.7% rebound for fiscal 2012. We consider the city's taxpayer base to be concentrated, with the 10 largest taxpayers making up 28% of AV and Chevron USA, a unit of Chevron Corp. ('AA/Stable/A-1' ICR), representing 23%.

We consider the city's financial position to be strong following a decline from a peak in fiscal 2006. During the five fiscal years through 2010, the city's unreserved general fund balance declined to 12.1% of general fund expenditures, or $14.8 million, from 41% at the end of fiscal 2006. Management estimates that its available general fund balance rose to 14.2% for fiscal 2011, and has budgeted for a small $828,000 overall deficit in fiscal 2012. Based, in part, on stronger-than-expected AV growth and a property sale, management expects this deficit to close during the fiscal year.

Also aiding financial performance in fiscal 2012, in our view, are two factors. First, the city entered into a multiyear settlement with Chevron in May 2010 that stemmed from a voter-approved but court-invalidated tax on manufacturers. The settlement provides for Chevron to pay to the city $10 million in fiscal 2012 and, including a separate one-time $5 million payment for retroactive utility user taxes, the company will generate on top of regular tax payments the equivalent of 12% of general fund expenditures in settlement payments to the city for the fiscal year regardless of its level of production within the city. Second, management reports that the city made major adjustments to its expenditures midway through fiscal 2011 that will largely carry forward to fiscal 2012. These included 20% departmental reductions and freezing of most positions, but the city has budgeted to increase its police staff by 4% for fiscal 2012.

We consider the city's financial management "strong" under our Financial Management Assessment (FMA) methodology. An FMA of "strong" indicates our view that practices are strong, well embedded, and likely sustainable.

Combined direct and overlapping debt is high, in our view, at 9.8% of market value and $10,247 per capita, inclusive of tax increment obligations. Excluding pension obligation bonds, the city's debt ratios are still high, at

8.6% and $8,948, respectively. We understand that the city has no plans to issue long-term debt.

Outlook

The stable outlook on the ICR and lease revenue bond rating reflects our view that the spending reductions that the city is carrying forward into fiscal 2012 and the settlement with Chevron will help the city to balance its operations during our two-year outlook horizon. However, given the city's reliance on Chevron and the potential for volatility, a revenue disruption that causes the city's available reserves to fall below strong levels could lead us to lower the rating. We do not expect to raise our ratings during our outlook horizon due to the city's concentrated revenue profile and high debt burden.

TRANs Assumptions: Rebound In Taxes

The city's cash flow projections show a virtual holding pattern for fiscal 2012, with a 0.1% increase in pre-TRANs and interfund borrowing receipts and a 1.2% increase in pre-TRANs and interfund borrowing disbursements. Management projects that the city's largest receipts category, utility users tax, will grow by 4.9% for the year and that its property tax receipts will decline by 2.1% due to the combination of rising AV but a successful property tax appeal by Chevron. Management projects sales tax receipts to rise by 11.1%, but we understand that about half of this increase represents receipts on accruals from fiscal 2011. Largely offsetting these tax receipts rises is the city's pause in transfers back to the general fund of prior years' set-asides for future other postemployment benefits costs. Management reports that the county's 9.8% projected increase in salaries and benefits reflects primarily the inclusion of public works and information technology departments into the general fund and pension contribution increases but generally flat compensation levels.

Management reports that the city will hold note repayment funds in short-term investments under its internal policies and state law. In practice this will likely consist of investments managed by the California Local Agency Investment Fund.

Chevron Continues To Represent A Major Tax Generator

The city's largest taxpayer, Chevron USA, makes up 23% of total AV, which we consider to be significant, and has a history of appealing its valuations, which we understand are set by the county assessor based on a complex income-driven formula. The petroleum products manufacturer's most recent successful appeal, in September 2009, reduced its total AV by a combined $1.2 billion for fiscal 2005 through 2007. We understand that the revenue effect was a loss of $2.3 million to the city and that a pending lawsuit by overlapping local governments could add another $8.4 million in make-up payments allocated to the city. We understand that Chevron has pending appeals to reduce its AV attributable to fiscal 2008 through 2011.

Chevron also successfully challenged voter-approved Measure T, which increased business license taxes on the company and other manufacturing businesses in the city. We understand that the city set aside revenues under the law after the company filed suit in February 2009. Following a December 2009 trial court decision that overturned the law, the city entered into an agreement with Chevron in May 2010 that provides for the company to pay $114 million over 15 years, starting with $10 million annual payments in fiscals 2011 and 2012, and a three-year period of $13 million annual payments. These settlement payments, combined with a $5 million one-time retroactive utility users' tax settlement and ongoing utility users' tax payments ($20 million in fiscal 2011) make Chevron's non-property tax payments significant in our view, at the equivalent of 28% of expenditures for fiscal 2012.

Debt Derivative Profile: Very Low Risk

We have assigned a Debt Derivative Profile overall score of '1.5' on a four-point scale, with '1' representing the lowest risk. The overall score of '1.5' reflects our view that the city's swap portfolio reflects a very low credit risk due to the following factors:

- Highly rated swap counterparties;
- A low degree of involuntary termination risk due to a moderate ratings trigger spread; and
- Very strong management practices, including formalized swap and debt management policies.

The city's combined swap notional amount attached to general fund obligations (consisting of the city's series 2007 lease revenue refunding bonds) is $84.5 million and the city has, through a swap agreement with Royal Bank of Canada (AA-/Stable/A-1+), fully fixed its variable-rate exposure. The floating- to fixed-rate swap term for the 2007 swap expires in 2037. The city receives 68% of LIBOR and pays a fixed rate of 3.657%. In our view, the swaps have a remote likelihood of involuntary termination from a lowered rating on debt over the term of the swap.

The city has also entered into forward swap agreements with JPMorgan Chase Co. (A+/Stable/A-1) that are attributable to the city's privately placed series 2005B-1 and 2005B-2 taxable pension funding bonds and take effect in August 2013 and August 2023, respectively. We understand that these will synthetically fix the city's rates on these obligations upon their conversion to index rate.

Financial Management Assessment: 'Strong'

Under our framework, an FMA of "strong" indicates our view that practices are strong, well embedded, and likely sustainable. Key policies include monthly reporting of financial and investment results to the city council including variance analyses and procedures for midyear budget adjustments if management deems doing so necessary. We understand that the city has suspended multiyear financial planning but has done so historically, and management reports will relaunch for the fiscal 2013 budget cycle. The city uses an outside consultant to help forecast sales taxes, and relies on internal expertise from its housing authority and redevelopment agency to forecast development. A five-year capital improvement plan is formally updated annually and identifies most funding sources. The city's debt policy requires that debt service supported by the general fund be no more than 10% of general fund revenues and the policy governs the use of swaps. The city seeks to maintain a general fund cash balance of at least 7% of expenditures to fund at least one month of operations in the event of a revenue disruption or spike in expenditures related to unexpected events, such as a natural disaster. The city plans to build this reserve to 15% upon a sustained return to revenue growth.

Pension System And Other Postemployment Benefits

The city issued pension obligation bonds in December 2005 in the amount of $115 million to fund its projected $107 million unfunded accrued actuarial liability (UAAL) as of June 30, 2005 in the state-managed Public Employees Retirement System (PERS). Management reports that the city's employees began covering their portion of pension contributions in the same year, which we have observed is uncommon among the cities with debt that we rate. Consequently, funded ratios for its two plans were virtually 100% at the end of fiscal 2010 despite recent PERS investment losses. The city is also one of only 12 in California that is authorized to assess a pension override tax that can be used for annually required pension expenditures, relieving the general fund from having to make these outlays.

The city also managed three closed plans, which were collectively funded at 34% of their actuarially accrued liabilities as of July 1, 2009. The city's contributed 180% of the annually required contribution rate to its largest, the Police and Firemen's Plan, which has an unfunded actuarial accrued liability (UAAL) of $21.9 million. Its contribution rate was 80% for its general plan, which had a UAAL of $4.1 million on July 1, 2009 and 127% for a single-retiree plan, which had a UAAL of $557,000 on the same date.

The city reported its actuarially accrued other post-employment benefits liability at $76.1 million as of July 1, 2009. Management reports that the city reverted to a pay-as-you-go funding approach in fiscal 2010 as a result of budgetary stress and that this payment represented 37% of the annual required contribution and 2.4% of general fund expenditures in fiscal 2010.

Related Criteria And Research

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: Key General Obligation Ratio Credit Ranges – Analysis Vs. Reality, April 2, 2008
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007
- USPF Criteria: Short-Term Debt, June 15, 2007
- USPF Criteria: Debt Derivative Profile Scores, March 27, 2006

Ratings Detail (As Of October 25, 2011)		
Richmond 2011-12 TRANs due 10/31/2012		
Short Term Rating	SP-1+	Affirmed
Richmond Jt Pwrs Fin Auth, California		
Richmond, California		
Richmond Jt Pwrs Fin Auth (Richmond) lse rev bnds (Point Potrero) ser 2009A		
Long Term Rating	A/Stable	Affirmed
Richmond Jt Pwrs Fin Auth (Richmond) rfdg ser 95 A		
Long Term Rating	A/Stable	Affirmed
Richmond Jt Pwrs Fin Auth (Richmond) taxable lse rev bnds (Point Potrero) ser 2009B		
Long Term Rating	A/Stable	Affirmed
Richmond Jt Pwrs Fin Auth (Richmond) (Civic Ctr) ser 2009 (ASSURED GTY)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.