

CREDIT OPINION

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Sun Prairie (City of) WI

Update to credit analysis

Summary

[Sun Prairie, WI's](#) (Aa2) credit attributes include a large tax base, located within commuting distance of [Madison WI](#), (Aaa stable), sound financial operations with healthy reserve levels and modest unfunded pension liabilities. These credit attributes are balanced against credit challenges including an elevated debt burden and limited revenue raising ability.

Credit strengths

- » Large tax base within commuting distance of Madison, the [Wisconsin](#) (Aa1 stable) state capital and the flagship campus of the University of Wisconsin
- » Solid financial operations supported by healthy reserves
- » Modest unfunded pension liabilities

Credit challenges

- » Elevated fixed costs and debt burden
- » Some exposure to underperforming tax increment districts (TID)
- » Limited revenue raising flexibility due to state imposed levy limits

Rating outlook

Outlooks are generally not assigned to local government credits with this amount of debt.

Factors that could lead to an upgrade

- » Significant tax base growth
- » Moderation of debt and fixed cost levels

Factors that could lead to a downgrade

- » Growth in debt burden or fixed costs
- » Tax base valuation declines or weakening of resident wealth and income
- » Declines in operating reserves or liquidity

Key indicators

Exhibit 1

Sun Prairie (City of) WI	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value (\$000)	\$2,353,843	\$2,368,669	\$2,413,489	\$2,566,184	\$2,772,246
Population	29,880	30,601	31,174	31,721	33,733
Full Value Per Capita	\$78,777	\$77,405	\$77,420	\$80,899	\$82,182
Median Family Income (% of US Median)	125.4%	117.5%	119.6%	117.5%	117.5%
Finances					
Operating Revenue (\$000)	\$32,171	\$28,590	\$28,291	\$29,053	\$27,677
Fund Balance (\$000)	\$6,686	\$6,834	\$7,314	\$7,711	\$7,952
Cash Balance (\$000)	\$7,562	\$8,365	\$6,428	\$12,714	\$13,179
Fund Balance as a % of Revenues	20.8%	23.9%	25.9%	26.5%	28.7%
Cash Balance as a % of Revenues	23.5%	29.3%	22.7%	43.8%	47.6%
Debt/Pensions					
Net Direct Debt (\$000)	\$67,254	\$76,969	\$74,241	\$80,110	\$77,185
3-Year Average of Moody's ANPL (\$000)	\$3,894	\$5,823	\$8,003	\$11,538	\$12,809
Net Direct Debt / Full Value (%)	2.9%	3.2%	3.1%	3.1%	2.8%
Net Direct Debt / Operating Revenues (x)	2.1x	2.7x	2.6x	2.8x	2.8x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.2%	0.2%	0.3%	0.4%	0.5%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.1x	0.2x	0.3x	0.4x	0.5x

The table above reflects data through the close of fiscal 2017.

Sources: Moody's Investors Service; Sun Prairie audited financial statements

Profile

The city of Sun Prairie is located approximately 10 miles northeast of Madison and covers 12 square miles. The city has an estimated population of 31,721.

Detailed credit considerations

Economy and tax Base: large, affluent tax base northeast of Madison

The city's local economy is expected to remain stable given its favorable location within commuting distance to employment opportunities throughout the Madison region and continued local economic development activity. Located in central [Dane County](#) (Aa1 stable) 10 miles northeast of downtown Madison, the city encompasses approximately 12 square miles. The city's large, \$3 billion tax base increased at an average annual rate of 4.9% per year over the last five years due to a combination of residential, commercial and industrial development. Resident income levels are strong at 118% of the nation. At 2.1% in May 2018, the city's unemployment rate was lower than both the state and nation at 2.6% and 3.6% respectively.

Financial operations and reserves: healthy operating reserves; some TIDs require General Fund support

The city's financial profile is expected to remain sound. The city closed fiscal 2017 with a General Fund surplus of \$298,000, increasing total General Fund reserves to \$13 million or 57.1% of General Fund revenues. Of the total General Fund balance, \$2.8 million was classified as nonspendable, including \$2.1 million in advances to various TIDs. Net of non-spendable and restricted portions, the city's available General Fund balance totaled \$8.2 million in fiscal 2017, or a still healthy 36.2% of General Fund revenues, up from \$7.8 million and 34.9% in fiscal 2016. Across the city's main operating funds (combined General and Debt Service Funds) available operating reserves totaled \$8 million, equivalent to 28.7% of operating fund revenues.

For fiscal 2018, management originally budgeted for a planned spend down of \$450,000 in the General Fund for capital projects, but now anticipates ending the year with a \$100,000 surplus, given a variety of favorable budgetary variances including lower than

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anticipated public works expenditures. It should be noted that due to a recent court judgement this month, it was ordered that the city will be responsible for paying out an estimated \$622,000 for damages. The details are still being determined, but management expects the General Fund will most likely be affected, and the year to date projections cited above could reflect a deficit. Despite potential draws, we expect the General Fund reserve level will remain healthy.

The city's TIDs have needed General Fund support, however, overall advances did decrease slightly, from \$2.3 million in 2016 to \$2.1 million in fiscal 2017. TID #8 and TID #9 accounted for a majority of the interfund advances due to the General Fund at \$1.2 million and \$687,000, respectively. Advances to TID #8 are expected to grow to \$1.5 million by 2024, due to additional capital needs before being fully repaid in 2026. At this juncture, the available fund balance, which is net of these advances, is expected to remain healthy.

LIQUIDITY

The city's liquidity remains sound despite growing interfund advances made to city TID districts. At the close of fiscal 2017, net cash across city operating funds totaled \$13.2 million or 47.6% of operating fund revenues, up from \$12.7 million or 43.8% of revenues in fiscal 2016.

Debt and pensions: elevated debt burden and fixed costs; modest unfunded pension liabilities

The city's debt burden is high, as are fixed costs. Inclusive of a total of \$15.1 million in GO notes and bonds to be issued in September 2018, the city's net direct debt burden is a high 3% of full value or 3.2x operating revenues. The city's high 8.1% overlapping debt burden is largely due to the significant borrowing of [Sun Prairie Area School District](#) (Aa3). Debt service expenditures totaled \$7.1 million or a high 25.6% of 2017 operating fund revenues. Fixed costs, inclusive of debt service, other post-employment benefits (OPEB) and annual pension contributions, totaled \$8.2 million, or a high 29.5% of operating revenue, in fiscal 2017. The city plans to issue approximately \$9.3 million in general obligation (GO) debt in fiscal 2019 in conjunction with its capital improvement plan. Further elevation in the direct or overall debt burden, or in the city's fixed costs, beyond current borrowing plans, could result in downward rating pressure.

Sun Prairie participates in the Wisconsin Retirement System (WRS), a statewide cost sharing plan. The city's employer contributions to WRS in fiscal 2017 were \$1 million or a modest 3.8% of the city's fiscal 2017 operating revenue.

DEBT STRUCTURE

All of the city's debt is fixed rate and long-term. Amortization of existing debt is average with 85.1% of principal set to be retired over the next ten years.

DEBT-RELATED DERIVATIVES

The city has no exposure to debt related derivatives.

PENSIONS AND OPEB

Moody's adjusted net pension liability (ANPL) for Sun Prairie, under our methodology for adjusting reported pension data, was \$13.6 million in fiscal 2017, an increase from the fiscal 2015 of \$12.3 million. Despite the increase in ANPL, Sun Prairie's ANPL remains modest at just 0.5x the city's operating revenue and 0.5% of the full value of the city's tax base.

Moody's ANPL figure reflects the use of a market-based interest rate to value liabilities. The ANPL reflects the allocation of WRS liabilities to participating employers, which is a required reporting standard under GASB effective fiscal 2015. The ANPL is not intended to replace the city's reported liability information but is used to enhance comparability with other rated entities.

Sun Prairie's other post-employment benefits (OPEB) liability reflects a single-employer defined benefit healthcare plan. The city's pay-go contribution was \$18,000 in fiscal 2017, or a very modest 0.1% of operating revenues. As of January 1, 2016, the most recent actuarial valuation date, the plan had an unfunded actuarial accrued liability of \$112,192 or less than 1% of operating revenues.

Management and governance: moderate institutional framework; conservative budgeting practices

Sun Prairie management employs conservative budgeting techniques that have led to a steady increase in General Fund reserves over the last five years. Wisconsin cities have an Institutional Framework score of A, which is moderate. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector's major revenue source, property tax revenue, is subject to a cap that restricts cities from increasing their operating property tax levies except to capture amounts represented by net new construction growth. Revenues and expenditures tend to be predictable. Across the sector, fixed and mandated

costs are generally high. Expenditures are somewhat flexible, as collective bargaining is allowed for public safety employees but is curbed for non-public safety employees.

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