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CREDIT OPINION
7 August 2020

New Issue

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Cook County C.C.S.D. 15 (Palatine), IL

Update to credit analysis

Summary

Cook County C.C.S.D 15 (Palatine), IL's (Aa2) credit characteristics include a sizeable tax base located in Cook County (A2 stable) with above average income levels. Financial operations are healthy, with strong reserve and liquidity levels and moderate reliance on the State of Illinois (Baa3 negative) for operating revenue. The debt burden is low, but the district has outstanding borrowing need. Like all districts in the state, there is contingent risk associated with state support for contributions to an underfunded Teachers Retirement system.

We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. We do not see any material immediate credit risks for the district. We do not see any material immediate credit risks for the district as additional expenditures have been minimal and the district has realized savings due to the closure of district buildings. Favorably, the state of Illinois does not plan on reductions in state aid to school districts at this time. The situation surrounding the coronavirus is rapidly evolving and the longer term impact will depend on both the severity and duration of the crisis. If our view of the credit quality of the district changes, we will update our opinion at that time.

Credit strengths

» Sizeable tax base located in the Chicago (Ba1 stable) metropolitan area

» Healthy financial position with strong reserve and liquidity levels

Credit challenges

» Contingent risk associated with reliance on state support for pension contributions to an underfunded statewide teachers' pension plan

Rating outlook

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

Factors that could lead to an upgrade

» Growth in available reserves and unrestricted liquidity

» Strengthening of resident income indices

Factors that could lead to a downgrade

» Narrowing of district reserves and available liquidity

» Significant growth in the district's debt or pension burden

Key indicators

Exhibit 1

Cook County C.C.S.D. 15 (Palatine), IL	2015	2016	2017	2018	2019
Economy/Tax Base					
Total Full Value ($000)	$9,150,396	$10,595,521	$10,655,913	$10,387,415	$11,700,032
Population	119,710	119,702	119,677	119,285	119,710
Full Value Per Capita	$76,438	$88,516	$89,039	$89,332	$86,771
Median Family Income (% of US Median)	139.0%	144.0%	143.2%	138.1%	138.1%
Finances					
Operating Revenue ($000)	$189,138	$193,821	$219,385	$223,527	$202,044
Fund Balance ($000)	$59,536	$56,271	$61,796	$64,576	$63,532
Cash Balance ($000)	$67,221	$65,899	$66,562	$73,377	$71,762
Fund Balance as a % of Revenues	31.5%	29.0%	28.2%	28.9%	31.4%
Cash Balance as a % of Revenues	35.5%	34.0%	30.3%	32.8%	35.5%
Debt/Pensions					
Net Direct Debt ($000)	$31,903	$43,087	$48,157	$44,301	$40,234
3-Year Average of Moody's ANPL ($000)	$82,280	$87,521	$103,293	$102,915	$97,530
Net Direct Debt / Full Value (%)	0.3%	0.4%	0.5%	0.4%	0.4%
Net Direct Debt / Operating Revenues (x)	0.2x	0.2x	0.2x	0.2x	0.2x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.9%	0.8%	1.0%	1.0%	0.9%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.4x	0.5x	0.5x	0.5x	0.5x

The table above reflects dated through fiscal 2019
Source: Audited financial statements; US Census Bureau, Moody's Investors Service

Profile

Located in Cook County, approximately 25 miles northwest of Chicago, the district serves a majority of the Village of Palatine (Aa2 negative), the City of Rolling Meadows, and small portions of five other communities. The district provides K-8 education for 11,691 students in a community of over 119,000 residents.

Detailed credit considerations

Economy and tax base: sizeable tax base located within Chicago Metropolitan Area

The coronavirus is driving an unprecedented economic slowdown. We currently forecast US GDP to decline significantly during 2020 with a gradual recovery commencing toward the end of the year. Local governments with the highest exposure to tourism, hospitality, healthcare, retail, and oil and gas could suffer particularly severe impacts. The district's employment base is closely tied the larger Chicago metropolitan economy with residents commuting throughout the metropolitan area via commuter rail service and Interstates 90, 290 and 355. As of June 2020 unemployment in Cook County had surged to 17%, which is higher than the national rate of 11% though not out of line with increases in other counties with a large urban center. The unemployment rate within the district may be significantly different given a median family income equal of 138% of the national level.

Located in Cook County, the district serves a majority of the Village of Palatine, as well as the City of Rolling Meadows, in addition to smaller portions of five other communities. The district's large $11.7 billion tax base increased at an average annual rate of 5% over the last five years, mainly due to residential and commercial development. The base is primarily residential with minimal concentration as the top ten taxpayers comprise just 5.5% of assessed value. As of now, management reports that development is still continuing, however coronavirus is rapidly evolving and the longer-term impact will depend on both the severity and duration of the crisis.

Finances and liquidity: Healthy financial position with strong reserve levels

The district's finances are expected to remain healthy, supported by conservative practices that have led to strong reserves. For fiscal 2020 the district budgeted for a $3 million draw across operating funds (combined education, operations and maintenance, debt service, transportation, Illinois municipal retirement fund and working cash funds), but due to expenditure savings, officials estimate the year ended with balanced operations. As result of recent fiscal challenges, the state's budget weakens funding for schools including only flat funding instead of the increase called for under the state funding formula. The district has only relatively moderate dependence on state revenue, which accounts for a little over 10% of operating revenue. Therefore, despite the weakening of state funding, the budget for fiscal 2021 is expected to be balanced.

The district is currently in tier 2 under the state of Illinois' evidence based funding model which was passed in fiscal 2018. Under this model, districts in tier 1 receive the majority of any increase in state funding with tier 2 districts next in line, while tier 3 and 4 districts are unlikely to receive any significant growth in funding. The district has additional exposure to the state through pension contributions made by the state on-behalf, which was equivalent to 17% of fiscal 2019 revenues. Available operating fund balance totaled $63.5 million for fiscal 2019, a healthy 31% of revenues.

Property taxes are the largest revenue source totaling 62% of fiscal 2019 revenue and are anticipated to have limited disruptions. The district currently levies below operating rate caps, however, the district is subject to the Property Tax Extension Limitation Law (PTELL), which limits the annual growth in taxes to the lesser of 5% or percentage increase in the Consumer Price Index (CPI).

Liquidity

The district closed fiscal 2019 with a net cash balance of $71.8 million, or a strong 36% of revenues.

Debt and pensions modest debt profile with plans for additional borrowing

The district's debt burden may increase materially based on potential outstanding capital project, but should remain moderate given fast principal amortization and very little debt currently outstanding. The contingent risk associated with exposure to a poorly funded state pension plan is a credit challenge across the sector. Net direct debt of the district will total $46.1 million, equal to a low 0.4% of full value and 0.2x of fiscal 2019 revenue. Going forward the district will need to address facility needs, which may include a combination of borrowing and cash financing.

The Moody's three year adjusted net pension liability (ANPL) for the district is $97.5 million, equal to a low 0.5x operating revenue and 0.9% of full value. The modest pension liability reflects that the state currently funds the majority of teacher pensions on behalf of local school districts. The district's fixed costs, inclusive of debt service, pension and other post employment benefit (OPEB) contributions were 4.5% of fiscal 2019 operating revenue.

Legal security

The district's outstanding debt is secured by the district's GOLT pledge that is supported by a dedicated property tax levy that is unlimited as to rate, but limited by the district's DSEB.

Debt structure

All debt is fixed rate, with 100% of principal scheduled to be repaid in ten years. GOLT debt is secured by the debt service extension base (DSEB) which totals just over $6.1 million for fiscal 2021. The MADS is $6.4 million slightly higher than the current DSEB of $6.1 million. Assuming no growth the shortfall would be $276,000 while under 1.5% growth projected there would be no shortfall. If there were shortfalls, the district would utilize available reserves.

Debt-related derivatives

The district is not a party to any derivative agreements.

Pensions and OPEB

The state currently assumes responsibility for funding the majority teacher pensions on behalf of local school districts. Given the large unfunded liabilities for teacher pensions across the state, a reduction in this support by the state represents a contingent risk for all local school districts. District teachers participate in the Teachers Retirement System (TRS) of Illinois, while other staff participate in the Illinois Municipal Retirement Fund (IMRF), an agent multiple-employer plan. Very high unfunded pension liabilities are a significant drag on the state's credit quality, and TRS represents a material portion of the state's total pension burden.

Like its other pension systems, the State of Illinois contributes to TRS using a very back loaded and annually rising payment schedule. These rising costs have played a significant role in the state's ongoing budget challenges. Certain state legislators and the past two governors have considered shifting pension costs to Illinois schools and universities for a number of years, but to date have shown no inclination toward forcing local districts to pay for accumulated unfunded liabilities. Typically the proposals call for shifting current year benefit accruals to local districts, called "normal cost" or "service cost," over the course of anywhere between the next four years to over a decade.

OPEB obligations do not represent a material credit risk for the district. The district operates a single-employer retiree medical plan. The district's net OPEB liability at the close of fiscal 2019 was $98 million. Moody's adjusted net OPEB liability, which is similar to our adjustments to pension liabilities, totals $90.2 million equivalent to 2.2x operating revenue. The district made a $1.3 million pay-as-you-go contribution in fiscal 2019, equal to 0.7% of operating revenue.

ESG considerations

Environmental

Environmental considerations are a modest factor in the district's credit profile at this time. According to data of Moody's affiliate, Four Twenty Seven, the district, is located in an area at high risk for heat stress. The firm measures heat stress as the relative change in both the frequency and severity of hot days, as well as average temperature. The biggest impact of heat exposure for most Midwest issuers will be to agriculture based economies. Cook County also has relatively high exposure to extreme rainfall events compared to counties nationally. Flooding throughout the county will be relieved by the Tunnel and Reservoir Plan (TARP) currently underway through the Metropolitan Water Reclamation District of Greater Chicago (Aa2 stable).

Social

Social considerations impact the district's credit profile. We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. The district's tax base is large and benefits from it favorable location within the Chicago metropolitan area as detailed in the Economy and Tax Base section. Overall district demographics are above average, and unemployment rates are above both the state and median averages. The district is in the process of determining whether students will return to school full-time in the fall with safety measures and restrictions, or continue remote learning. For fiscal 2021 the district estimates there could be an additional $1 million in expenses related to staff. The district received $1.6 million in CARES Act funding, which it expects may absorb some of these additional costs.

Governance

The district's management practices are strong with conservative budgeting practices and forward looking planning. The district does not have a formal fund balance but maintains a target of minimum of 25% fund balance as a percentage of expenditures.

Illinois school districts have an institutional framework score [1] of "A", which is moderate. School districts have moderate revenue-raising ability since they are subject to tax caps, but districts can seek voter approval for additional local property tax funding. Revenue predictability is disparate across the state: revenue for property tax dependent districts are very stable, while revenue for state aid dependent districts are less stable. Strong public sector unions somewhat limit districts' expenditure reduction ability. Still, districts have some cost-cutting ability given manageable fixed costs which are primarily debt service expenditures, as the state currently assumes most pension costs for most Illinois public school districts. Expenditures consist primarily of personnel costs, which are highly predictable.

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.

Cook County C.C.S.D. 15 (Palatine), IL

Scorecard Factors and Subfactors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$11,700,032	Aa
Full Value Per Capita	$97,736	Aa
Median Family Income (% of US Median)	138.1%	Aa
Finances (30%)		
Fund Balance as a % of Revenues	31.4%	Aaa
5-Year Dollar Change in Fund Balance as % of Revenues	2.4%	A
Cash Balance as a % of Revenues	35.5%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	0.9%	A
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	1.0x	A
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	0.4%	Aaa
Net Direct Debt / Operating Revenues (x)	0.2x	Aaa
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	0.8%	Aaa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	0.5x	Aa
Notching Factors:[2]		
Other Scorecard Adjustment Related to Debt/Pensions: Contingent risk associated with state pension support		Down
	Scorecard-Indicated Outcome	Aa3
	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 dated July 29, 2020.
[3] Standardized adjustments are outlined in the latest GO Methodology Scorecard Inputs publication.
Source: Issuer's audited financial statements; US Census Bureau

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.

REPORT NUMBER 1240697

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