

## CREDIT OPINION

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# Sussex (Village of) WI Sewer Enterprise

## Update to credit analysis

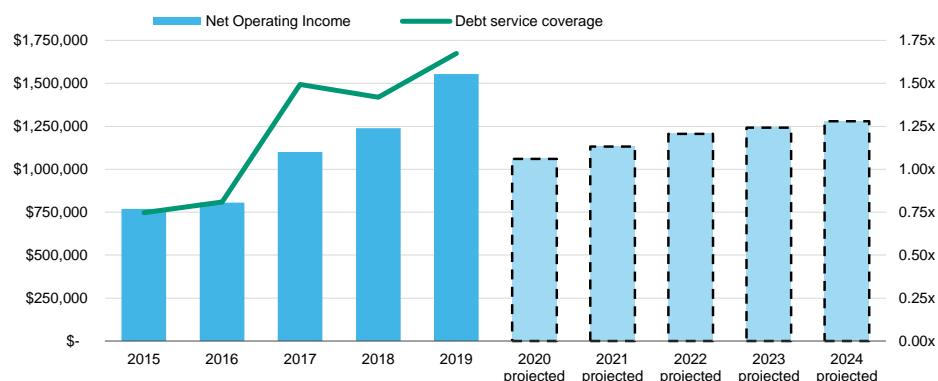
### Summary

The [Village of Sussex, WI Sewer Enterprise](#) (Aa3) has a modestly sized system and healthy income levels within the service area, as well as updated infrastructure with adequate capacity and a moderate debt burden. The enterprise is financially sound with strong cash reserves and adequate and stable debt service coverage.

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 Village of Sussex, WI Sewer Enterprise. However, the situation surrounding 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 sewer enterprise changes, we will update our opinion at that time.

Exhibit 1

**Increasing net operating income will decline in 2020 following fee decreases, but management projects to maintain sufficient debt service coverage as fee increases are gradually phased back in**



Source: Village of Sussex audited financial statements and budget projections

### Credit strengths

- » Affluent, residential customer base
- » Very strong liquidity
- » Independent rate-setting authority

## Credit challenges

- » Modestly sized system
- » Below average but adequate debt service coverage

## Rating outlook

Moody's does not typically assign outlooks to local governments with this amount of debt.

## Factors that could lead to an upgrade

- » Significant expansion of the customer base and steady growth in operating revenue
- » Improved liquidity on a nominal basis
- » Moderation of the debt burden

## Factors that could lead to a downgrade

- » Material declines in debt service coverage or liquidity
- » Substantial growth in leverage

## Key indicators

Exhibit 2

Village of Sussex, WI Sewer Enterprise

System Characteristics					
Asset Condition (Net Fixed Assets / Annual Depreciation)	33 years				
System Size - O&M (in \$000s)	\$1,311				
Service Area Wealth: MFI % of US median	143.1%				
Legal Provisions					
Rate Covenant (x)	1.25				
Debt Service Reserve Requirement	DSRF funded at lesser of standard 3-prong test (Aa)				
Management					
Rate Management	A				
Regulatory Compliance and Capital Planning	A				
Financial Strength					
	2015	2016	2017	2018	2019
Operating Revenue (\$000)	\$1,936	\$2,087	\$2,426	\$2,671	\$2,865
System Size - O&M (\$000)	\$1,167	\$1,281	\$1,326	\$1,431	\$1,311
Net Revenues (\$000)	\$769	\$806	\$1,099	\$1,240	\$1,554
Net Funded Debt (\$000)	\$5,990	\$4,877	\$4,502	\$6,343	\$5,816
Annual Debt Service (\$000)	\$1,029	\$996	\$736	\$874	\$929
Annual Debt Service Coverage (x)	0.7x	0.8x	1.5x	1.4x	1.7x
Cash on Hand	326 days	333 days	307 days	406 days	253 days
Debt to Operating Revenues (x)	3.1x	2.3x	1.9x	2.4x	2.0x

Source: Village of Sussex audited financial statements, US Census Bureau, Moody's Investors Service

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## Profile

The [Village of Sussex](#) (Aa2) is located in southeastern [Wisconsin](#) (Aa1 stable), approximately 19 miles northwest of the [City of Milwaukee](#) (A1 negative) and nine miles north of the [City of Waukesha](#) (Aa2). The sewer enterprise is composed of a conveyance system and treatment facility. Waste is conveyed to the treatment facility by gravity and nine lift stations, made up of 44 miles of underground piping, nine lift stations and two receiving stations and treatment facility. The enterprise's 5.1 MGD treatment facility has an average flow of 2.2 MGD and serves the Village of Lannon, Lisbon Sanitary District #1, Richmond School District and a portion of the [Village of Menomonee Falls](#) (Aa2 stable).

## Detailed credit considerations

### Service area and system characteristics: modestly sized system with affluent service 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. Sussex is not highly exposed to any of these sectors and officials report a very limited slowdown in some economic activity throughout the village. Furthermore, the village is home to Sussex IM, an injection molding firm that manufactures hand sanitizer containers and is expanding to meet increased demand.

The service area of the sewer enterprise expands beyond the village boundaries, but remains more modestly sized than that of peers. The system benefits from strong resident economic characteristics and will continue its steady growth as the village continues to add residents and businesses. Income, measured by a median family income in the village that is 143.1% of the national median and wealth, measured by a full value per capita of \$133,000, are both strong. The poverty rate is also low at just 5.8%, compared to 11.9% in the state and 14.1% nationwide.

The customer base grew at a compound annual rate of 0.5% over the last five years and is stable with a base that is 91% residential. The customer base is moderately concentrated with nearly a quarter of billings coming from the Top 10 customers. This is due primarily to Nature's Path Foods, the top user, which accounts for approximately 15%. Management reports that operations at the village's largest businesses are stable.

### Debt service coverage and liquidity: adequate debt service coverage and strong liquidity will continue

Debt service coverage will decline modestly in 2020 following a fee decrease in the sewer enterprise, although management projects the system to have adequate net revenue to meet its debt service needs. Net sewer revenue has posted adequate debt service coverage each of the last two years after raising rates to accommodate debt service associated with an issuance in 2018. In fiscal 2019 debt service coverage increased to 1.7x. Other communities that are served by the sewer enterprise reimburse Sussex for 53% of debt service payments for the enterprise's 2007 Clean Water Fund loan. This loan financed capital projects to increase the system's capacity and allow it to serve the additional communities. The village reports that excluding those payments and payments in lieu of taxes, coverage of senior lien debt was 4x in fiscal 2019.

## LIQUIDITY

Cash reserves in the sewer enterprise remain sound despite a decrease in 2019. The system added to its reserves in 2019 before an interfund loan to the stormwater enterprise narrowed the unrestricted cash position decreased to \$910,000, which remains healthy at 253 days of expenditures. The village also maintains strong liquidity across all governmental funds, closing fiscal 2019 with \$13.4 million in cash, equivalent to 111% of governmental operating revenue.

### Debt and legal covenants: moderate leverage of net sewer revenue

The enterprise's moderate debt burden will remain stable as the village scales down its infrastructure projects. Inclusive of a planned sale in June 2020, sewer enterprise debt will increase to 2.4x fiscal 2019 net revenue. The outstanding senior lien sewer revenue bonds carry a debt service reserve fund requirement equal to the lesser of 10% of the proceeds of the bonds, maximum annual debt service or 125% of average annual debt service. Additional security to outstanding senior lien sewer revenue bonds includes a service to the village provision in which the village pledges to support the systems as essential public services. This entails the village paying reasonable costs and value for services to maintain revenue sufficient to generate debt service coverage of at least 1.25x. The village's operating support is subject to appropriation.

**DEBT STRUCTURE**

All of the enterprise's debt is fixed rate and long term. Debt service on the revenue bonds is secured by net revenue of the sewer enterprise after payment of operation and maintenance expenses and are a first lien on the net revenue of the enterprise.

**DEBT-RELATED DERIVATIVES**

The village is not a party to any debt-related derivatives.

**PENSIONS AND OPEB**

Utility employees participate in the Wisconsin Retirement System (WRS), a multi-employer cost-sharing defined benefit pension plan. During fiscal 2019 the Village of Sussex made contributions of \$215,000 to WRS, of which \$38,000 came from the sewer enterprise. These pension contributions represent a minor 1.3% of operating revenue.

**ESG considerations**

[Similar to the overall US local government sector](#), the Village of Sussex has low exposure to environmental risks. According to data from Moody's affiliate Four Twenty Seven, the village's aggregate exposure to the projected rate of change of five climate risk factors ranks average for the 3,142 municipalities it tracks. Of the climate risks evaluated, the village's highest risk is related to water stress or an increase in drought-like patterns, testing the ability of water supply to meet demand. These changes will have the greatest impact on water intensive facilities, such as those involved in manufacturing and energy production. The [Sussex, WI Water Enterprise's](#) (Aa3) largest customer, [Quad/Graphics, Inc](#) (B1 negative), only comprises 3.5% of water billings.

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The village board sets sewer rates independently and has made modest annual increases that range from 1% to 3% each of the last five years. Management plans to continue with a similar strategy to maintain strong debt service coverage. The village is in the final year of an eight year capital plan and has approved a 10 year capital plan for the period from 2021 through 2030.

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