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Summary:

Sheffield Village, Ohio; General Obligation

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Summary:

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Credit Profile		
Sheffield Village GO		
Long Term Rating	AA/Stable	Upgraded

Rationale

S&P Global Ratings raised its long-term rating to 'AA' from 'AA-' on Sheffield Village, Ohio's series 2014A limited-tax general obligation (GO) various purpose improvement and refunding bonds. The outlook is stable.

The rating action reflects our view of the village's economic growth, which has led to a stronger financial position, and limited future debt needs. Sheffield Village is a small suburb of Cleveland, located along Interstate-90 in the Lorain County growth corridor. Given its location, the village has experienced development in recent years, particularly in the commercial sector, which has bolstered its income tax base and led to strong budgetary performance and flexibility. We anticipate growth to continue but remain manageable from an operational and capital perspective, which helps to ensure fiscal stability. At the same time, we anticipate that the village will maintain reserves above its informal target of $1 million to mitigate unexpected pressures or events. The village's debt profile is also a credit strength, with a rapid repayment structure, decreasing debt service payments, and no need for significant new debt. While we don't anticipate changing the rating in the next two years, we believe that the village's finances could demonstrate fluctuations given the village's concentrated income tax base and small budget.

The village's full faith and credit and an agreement to levy ad valorem property taxes within the 10-mill limitation secure the limited-tax bonds. We rate the limited-tax GO debt at the same level as our view of the village's general creditworthiness, as reflected by the village's unlimited-tax GO pledge.

The 'AA' rating reflects our view of the village's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Adequate management, with standard financial policies and practices under our financial management assessment methodology;
- Strong budgetary performance, with operating results that we expect could improve in the near term relative to fiscal 2018, which closed with an operating deficit in the general fund but an operating surplus at the total governmental fund level;
- Strong budgetary flexibility, with an available cash reserve in fiscal 2018 of 20% of operating expenditures;
- Very strong liquidity, with total government available cash at 26.9% of total governmental fund expenditures and 4.4x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability position, with debt service carrying charges at 6.1% of expenditures and net direct debt that is 38.6% of total governmental fund revenue, as well as rapid amortization, with 94.6% of debt

scheduled to be retired in 10 years; and

- Strong institutional framework score.

Very strong economy

We consider Sheffield's economy very strong. The village, with an estimated population of 4,318, is located in Lorain County in the Cleveland-Elyria MSA, which we consider broad and diverse. Sheffield Village is 25 miles southwest of Cleveland. The village has a projected per capita effective buying income of 121% of the national level and per capita market value of $107,218. Overall, the village's market value grew by 1% over the past year to $463 million in 2018. The county unemployment rate was 5.4%.

Given that Ohio villages rely on municipal income taxes to fund operations, their employment base is an important credit factor. While many residents commute, the district also has some large employers such as Ford Motor Co. Officials report that operations at the Ford plant have been stable. Other leading employers include University Hospitals Health System and Sheffield-Sheffield Lake City School District. In 2018, the 10 largest employers in the village accounted for 35% of the village's income tax revenue. Given the village's location along Interstate-90 in Lorain County, which is one of the faster-growing counties in the region, the village's employment base has been expanding in recent years, which we believe will diversify its income tax base in the years to come.

Adequate management

We view the village's management as adequate, with standard financial policies and practices under our financial management assessment methodology, indicating our view that the finance department maintains adequate policies in some but not all key areas.

Management uses historical trend analysis and outside sources of information to formulate budget assumptions. Given that income tax revenue is the village's largest revenue source, the management performs audits of every business in the village, and has regular discussions with leading employers. The council receives monthly budget-to-actual reports, and the budget can be amended as needed. The village does not maintain formal long-term financial forecasts or capital plans, but informally the finance team does try to project out three to five years. The village has adopted state guidelines for investment and debt management. While it lacks a formalized reserve policy, both management and council have historically aimed to maintain general fund reserves above $1 million. Because the village's budget has grown, management may target $1.3 million to $1.5 million hereafter.

Strong budgetary performance

Sheffield's budgetary performance is strong, in our opinion. The village had a deficit operating result in the general fund of 1.7% of expenditures but a surplus result across all governmental funds of 5.7% in fiscal 2018. Our assessment accounts for our expectation that budgetary results could improve in the near term.

Income taxes account for roughly half of Sheffield's governmental revenue, and this revenue has shown consistent growth in recent years. From 2015 to 2018, income tax revenue grew at an annual average rate of 4.6%. The village conservatively budgeted for flat growth in 2019, but management reports that actual collections are trending well above the prior-year result. Given conservative assumptions, the original 2019 general fund budget reflected a 3.4% deficit. However, given the positive income tax trend, management expects to end the year with at least balanced operations, which we believe is a reasonable assumption.

The deficit in 2018 was largely due to a larger transfer out of the general fund than is typical. The village regularly makes transfers out for capital and debt service costs, though the size of the transfers varies year to year. In 2018, the transfer out of $830,000 was the largest in the past six years and included funds for matching grant projects, street resurfacing, debt service, and a new fire truck. A total of $160,000 of the transfer was to cover debt service in the French Creek tax increment financing fund. Management reports that recent development in this tax increment financing has reduced the general fund subsidy and should completely eliminate it by 2022. In 2019, the village is budgeting for only a $400,000 transfer out of the general fund.

We anticipate that budgetary performance will remain strong. Further economic development should continue to bolster the village's revenue base without significantly increasing the village's service needs. According to management, the recent economic growth has not caused operational or capital pressures, as infrastructure needs have largely been grant funded, and the village has not needed to substantially increase staffing levels. Furthermore, the village's geographic footprint is relatively small, so we believe that further growth should be manageable.

Strong budgetary flexibility

Sheffield's budgetary flexibility is strong, in our view, with an available cash reserve in fiscal 2018 of 20% of operating expenditures, or $1.2 million. Negatively affecting budgetary flexibility, in our view, is Sheffield's use of cash accounting, which reduces clarity about the amount of funds that are truly available.

Given positive income tax trends, management expects to add to reserves in fiscal 2019. Although the village's reserve target of $1 million is not formalized, we believe that management will adjust the budget as it deems necessary to adhere to this target, as it historically has done. The village's 2016 audit reflected an ending cash balance of less than $1 million, but management attributes this to a short-term advance to the village's capital projects fund that was quickly repaid in 2017.

Very strong liquidity

In our opinion, Sheffield's liquidity is very strong, with total government available cash at 26.9% of total governmental fund expenditures and 4.4x governmental debt service in 2018.

The village held $2.1 million in unrestricted cash and investments at the end of 2018. We believe that it has strong access to external liquidity because it has issued various types of debt, which demonstrates access to capital markets. We do not expect its cash position, with respect to its total governmental expenditures and debt service, to change much during the next two years, and we expect the cash position to remain very strong. We understand that the village has no potential contingent liabilities, including alternative financings, that could weaken its cash position.

Very strong debt and contingent liability profile

In our view, Sheffield's debt and contingent liability profile is very strong. Total governmental fund debt service is 6.1% of total governmental fund expenditures, and net direct debt is 38.6% of total governmental fund revenue.

The village may issue approximately $1.5 million for a new service department building, but otherwise has no additional debt plans. According to management, the village's priority is to pay off its existing debt. Approximately 94.6% of the direct debt is scheduled to be repaid within 10 years, which is, in our view, a positive credit factor.

Sheffield's required pension and actual other postemployment benefits (OPEB) contributions totaled 7.7% of total governmental fund expenditures in 2018. The village made its full annual required pension contribution.

Eligible village employees participate in either the Ohio Public Employees Retirement System (OPERS) or the Ohio Police and Fire Pension Fund (OP&F), both multiple-employer, cost-sharing state retirement systems. Employees participate in a choice of defined benefit, defined contribution, or combined plans. Other postemployment benefits are provided through the state plans.

Per Government Accounting Standards Board (GASB) Statement No. 68 standards, employers with benefits administered through cost-sharing, multiple-employer pension plans such as OPERS and OP&F must report their proportionate share of the net pension liability. The funded ratio, which consists of the plan fiduciary net position as a proportion of the total pension liability, was 84.7% for OPERS and 70.9% for OP&F.

In our opinion, the funded ratios for the two plans are inflated as a result of what we consider optimistic actuarial assumptions, such as above-average discount rates. We note that the underfunded pensions could likely lead to an increase in contributions if not adequately addressed by the state. In this scenario, we believe that the village is well positioned to manage any increases without significant budget stress given the village's very strong financial position and the relatively small percentage of contributions in its budget.

Strong institutional framework

The institutional framework score for Ohio townships and villages is strong.

Outlook

The stable outlook reflects our expectation that Sheffield Village will maintain strong budgetary performance and flexibility, with reserves above its informal target of $1 million; thus, we do not expect the rating to change over the two-year outlook period. The village's participation in the broad and diverse Cleveland-Elyria MSA lends stability to the rating.

Downside scenario

We could lower the rating if the village's income tax revenue significantly drops, as a result of either a recession or loss of major employer, if reserves were to significantly decrease, or if the village were to issue substantial debt.

Upside scenario

We could raise the rating if the village's economic metrics improve to levels commensurate with those of higher-rated peers, if its income tax base diversifies, and if the village builds reserves on a sustainable basis.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015

- 2018 Update Of Institutional Framework For U.S. Local Governments