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CREDIT OPINION
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Cook County C.C.S.D. 21 (Wheeling), IL

Update to credit analysis following removal of negative outlook

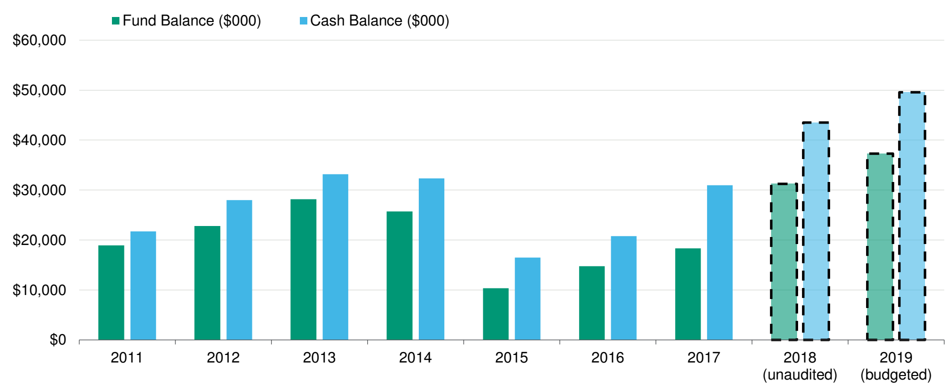
Summary

Cook County CCSD 21 (Wheeling), IL's (Aa3) credit profile is characterized by a low debt burden, large tax base, and above average income levels. The district also has a relatively narrow reserve position compared to its Aa3-rated peers that has improved since fiscal 2015 and is expected to increase substantially over the next two fiscal years (see exhibit 1). Further, the district is exposed to contingent liability risk associated with reliance on state contributions to a poorly funded State of Illinois (Baa3 stable) teacher's retirement system.

On August 22, 2018 we removed the negative outlook on the district.

Exhibit 1

Wheeling 21's fund balance and cash has improved since fiscal 2015 and is projected to add nearly $20 million by fiscal 2019



Source: Cook County CCSD 21 (Wheeling) audited financial statements, Moody's Financial Ratio Analysis

Credit strengths

» Low debt burden

» Large tax base with above average resident income levels

» Significant expenditure cuts resulted in consecutive operating surpluses

Credit challenges

» Narrow reserve position relative to the district's Aa3 peers

» Exposure to potential state shift of pension funding

Rating outlook

Outlooks are usually not assigned to local governments with this amount of debt.

Factors that could lead to an upgrade

» Significant improvement in financial reserves

» Expansion of the district's tax base and strengthening of resident income indices

Factors that could lead to a downgrade

» Further deterioration of the district's reserves

» Growth in the district's debt or pension burdens

Key indicators

Exhibit 2

Cook County C.C.S.D. 21 (Wheeling), IL	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value ($000)	$4,720,208	$4,800,892	$4,800,892	$4,666,798	$5,386,676
Population	65,140	66,232	66,565	67,456	67,456
Full Value Per Capita	$72,463	$72,486	$72,123	$69,183	$79,855
Median Family Income (% of US Median)	112.0%	115.8%	114.9%	118.2%	118.2%
Finances					
Operating Revenue ($000)	$120,297	$118,890	$109,156	$140,178	$149,632
Fund Balance ($000)	$28,177	$25,728	$10,327	$14,769	$18,339
Cash Balance ($000)	$33,177	$32,314	$16,491	$20,759	$30,994
Fund Balance as a % of Revenues	23.4%	21.6%	9.5%	10.5%	12.3%
Cash Balance as a % of Revenues	27.6%	27.2%	15.1%	14.8%	20.7%
Debt/Pensions					
Net Direct Debt ($000)	$47,819	$44,396	$41,287	$37,907	$34,337
3-Year Average of Moody's ANPL ($000)	$40,728	$38,428	$42,828	$48,587	$59,140
Net Direct Debt / Full Value (%)	1.0%	0.9%	0.9%	0.8%	0.6%
Net Direct Debt / Operating Revenues (x)	0.4x	0.4x	0.4x	0.3x	0.2x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.9%	0.8%	0.9%	1.0%	1.1%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.3x	0.3x	0.4x	0.3x	0.4x

Source: Cook County CCSD 21 (Wheeling), IL audited financial statements, US Census Bureau, Moody's Financial Ratio Analysis

Profile

Located approximately 30 miles northwest of Chicago (Ba1 stable), the prekindergarten through eighth grade district serves a number of communities in northwest Cook County (A2 stable), including the villages of Arlington Heights (Aa1), Buffalo Grove (Aaa negative), Mount Prospect, Northbrook (Aaa negative), Wheeling, and the City of Prospect Heights (Aa3). Enrollment for the 2017-2018 school year was 6,514 and population within the district is estimated at 67,456.

Detailed credit considerations

Economy and tax base: large residential tax base in northwest Chicago suburbs

We expect the district's $5.4 billion tax base will remain a credit strength at the current rating level given its significant size and above average resident income indices. Following five years of equalized assessed valuation (EAV) declines that shaved 38% off of the district's tax base, growth has resumed including a 15% increase in fiscal 2017. District officials report modest increase of 0.9% in fiscal 2018. Residential property comprises 61.3% of equalized assessed valuation with the remainder of the tax base primarily split between commercial and industrial uses. Income levels exceed the nation as the district's median family income is estimated at 118.2% of the national median. As of May 2018, the unemployment rate of 3.4% in Cook County was on par with the state rate and national rates. The district's poverty rate is below average at 10%, compared to a state rate of 14% and national rate of 15.1%.

Financial operations and reserves: recent and projected growth of fund balance

While currently limited, we expect the district's financial position will continue to improve, driven by reductions in expenditures and improved state funding. The district's fund balance declined to a low of $10.3 million across operating funds (inclusive of general, debt service, transportation, retirement, and working cash funds) at the close of fiscal 2015, but the district has improved to close fiscal 2017 with a much stronger $18.3 million in operating fund balance, representing a still below average 12.3% of fiscal 2017 operating revenue. The district's recent operating surpluses of $4.3 million in fiscal 2016 and $3.8 million in fiscal 2017 are primarily the result of expenditure savings due to staffing reductions and savings from health insurance plan changes. The district has also benefited from favorable improvements in the amounts and timing of state aid. The district's reserve position is also impacted by the deferral of June property tax receipts to the following fiscal year. The deferral results in a material variance between the cash and fund balance figures. Many districts in the state elect not to defer the payment resulting in a higher fund balance relative to those that defer the payment.

Management reports to have ended fiscal 2018 with an unaudited operating surplus of $12.5 million improving available fund balance to $31.2 million before accruals. The fiscal 2019 budget calls for another operating surplus of $7.3 million. If fully realized the budgeted surplus would grow operating fund balance to $38.5 million. The reported operating surplus in fiscal 2018 and budgeted operating surplus in fiscal 2019 are both the result of staffing cuts and health insurance savings that began in fiscal 2016 and are ongoing.

LIQUIDITY

The district closed fiscal 2017 with $31 million in cash across major operating funds, equivalent to a solid 20.7% of fiscal 2017 operating revenue.

Debt and pensions: modest debt and pension burdens

The district's leverage is expected to remain modest, despite plans to issue debt in early 2019. The district's net debt burden was $34.3 million at the close of fiscal 2017, equivalent to a low 0.6% of taxable full value and 0.2x operating revenue. The school board voted in favor of placing a $69 million building bond referendum on the November 2018 ballot. If it passes, the district plans to issue $45 million in early 2019 to begin a variety of projects across the district, including projects to improve safety and security, air conditioning, enhanced learning environments, energy efficiency, and infrastructure. The remainder of the debt would be issued at a later date depending on the timing and completion of the first phase of capital projects. As planned, this issuance will not have a material impact on the district's net debt burden.

The Moody's three-year adjusted net pension liability (ANPL) for the district, our measure of a local government's pension burden, is $59.1 million. With an ANPL that equals 1.1% of taxable full value and 0.4x operating revenue, the burden is relatively low. However, the modest ANPL reflects the fact that the state is primarily responsible for funding teacher pension costs for most Illinois school districts. The district's fixed costs (inclusive of debt service, pension contributions, and other post employment benefits) totaled $7.6 million, or a modest 5.1% of fiscal 2017 operating revenue.

DEBT STRUCTURE

All of the district's debt is fixed rate and amortizes over the long term. Principal repayment is average, with 87% scheduled to be retired within 10 years.

DEBT-RELATED DERIVATIVES

The district is not a party to any derivative agreements.

PENSIONS AND OPEB

The state has primary responsibility for funding teacher pensions through payments made on behalf of school districts. District teachers participate in the TRS (Teachers' Retirement System) of the State of Illinois, a multi-employer, cost-sharing defined benefit pension plan. Non-teaching district employees participate in the Illinois Municipal Retirement Fund (IMRF), an agent multi-employer plan. The state's fiscal 2017 contribution to TRS was just 65.2% of the amount needed for the plan to tread water[1]. Based on current funding practices, we expect unfunded liabilities of TRS on both a reported and Moody's-adjusted basis to grow, necessitating further growth in state contributions. The district's contribution to IMRF was stronger at 247.9% of tread water.

In July 2017, the state passed legislation to shift responsibility for new employees' pensions to school districts in order to provide itself budgetary relief under its statutory pension funding approach. While limited for now, the impact of this change will increase as employees hired after the change grow to comprise a greater portion of district staff. Districts are responsible for the entire accrued liability associated with employees hired once TRS implements the Tier 3 plan, meaning they must fund any unfunded liabilities associated with these employees that materialize in the future if pension assets do not perform as projected. Unless it acts to shift costs further, the State of Illinois retains responsibility for the bulk of pension costs associated with employees hired previously.

Management and governance: moderate institutional framework; significant staff reductions

Illinois school districts 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. 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, although Wheeling 21 has made significant staff reductions over the past two years, eliminating 47 full time equivalent positions to save over $6 million across fiscal 2017 and fiscal 2018. Still, districts have some cost-cutting ability given manageable fixed costs, as the state currently assumes most pension costs. Expenditures consist primarily of personnel costs, which are highly predictable.

Property taxes are the largest revenue source for Wheeling 21 at 58% of fiscal 2017 operating revenues. State aid accounted for 8% of the district's fiscal 2017 operating revenue. The district has additional exposure to the state with 27.9% of the operating revenue comprised of on-behalf pension payments bringing the total state support to 35.9% of operating revenues. The district is subject to the Property tax Extension Limitation Law (PTELL), which limits annual growth in the district's levy to the lesser of 5% of the percentage increase in the Consumer Price Index, plus new construction.

Endnotes

1 Our "tread water" indicator measures the annual government contribution required to prevent reported net pension liabilities from growing, given the entity's actuarial assumptions. An annual government contribution that treads water equals the sum of employer service cost and interest on the reported net pension liability at the start of the fiscal year. A pension plan that receives an employer contribution equal to tread water will end the year with an unchanged net pension liability relative to the beginning of the year if all plan assumptions hold. Net liabilities may decrease or increase in a given year due to factors other than the contribution amount, such as investment performance that exceeds or falls short of a plan's assumed rate of return. Still, higher contributions will always reduce unfunded liabilities faster, or will allow unfunded liabilities to grow more slowly than lower contributions. The degree to which contributions fall below the "tread water" indicator can help quantify a structural operating imbalance stemming from pensions, even under reported assumptions. A contribution below the "tread water" level in effect suppresses expenditures by leaving implied interest on net pension liabilities unpaid, akin to borrowing at the assumed rate of investment return for operations. For additional detail behind the "tread water" indicator, see our April 2016 report, "FAQ: Improved GASB Pension Disclosure Does Not Eliminate Need for Adjustments."

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