US Public Finance
Weekly Credit Outlook
DECEMBER 17, 2015

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Los Angeles Approves Labor Contract Providing Long-Term Pension Savings

On December 8, the Los Angeles (Aa2 stable) City Council approved a three-year labor agreement with the Coalition of Unions, which represents 17,000 civilian employees, or 52% of the city's workforce. The agreement is credit positive for the city because it ends uncertainty surrounding litigation over the 2012 pension reforms it implemented. The deal also establishes multiple years of salary cost certainty at levels below the city's baseline projections.

The agreement calls for a projected $5.2 billion in current present value pension savings over 30 years, according to city estimates. That amount is less than the projected savings of $6.9 billion in the 2012 pension reforms. But, the new labor deal ends litigation filed by unions against the city that could have wiped out savings entirely.

Besides the pension savings, the new agreement calls for an additional $11.6 billion in savings related to salary costs. The total $16.8 billion in savings is a crucial aspect in the city's plan to attain long-term structural balance in its roughly $5.4 billion General Fund budget.

Under the new labor contract, the city must undo its 2012 pension reforms, which had placed employees hired on or after July 1, 2013 in a lower "Tier 2" for pension benefits. Under the agreement, all Tier 2 employees' accrued benefits for past service will be retroactively increased to Tier 1 levels, increasing accrued liabilities by an estimated $18 million as of June 30, 2015, and their future service will also accrue at Tier 1 levels. The unfunded liabilities increase is relatively modest considering the reported unfunded actuarial accrued liability (UAAL) was estimated to be $5.3 billion at the end of fiscal 2014, the most recent year for which this figure is available.

New employees hired at the new Tier 3 level will accrue benefits at levels specified for a new "Tier 3." Tier 3 benefits are less expensive for the city than Tier 1, but more expensive than the provisions provided under Tier 2. Further, Tier 3 benefits do not contain the same level of risk-sharing provisions as the Tier 2 benefits. For example, employees in Tier 2 were responsible for 75% of normal costs, and half of the cost to finance Tier 2 unfunded liabilities. As a result, both the city and Tier 2 employees shared the risks associated with investment performance. Similar to Tier 1 employees, the city assumes all investment performance risk for Tier 3 employees.

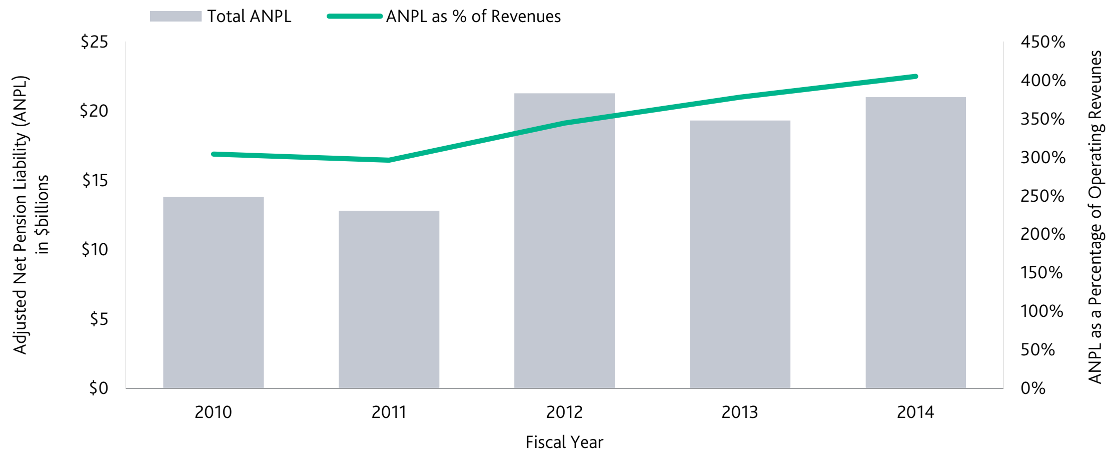
Beyond pension reform savings, the new labor agreement also includes salary provisions that would save the city an additional $11.6 billion over 30 years via compensation changes, compared to a baseline assumption based on historical rates of salary increase. These provisions include a 0% pay increase for 17 of the 19 labor groups covered by the contract through fiscal 2017 and a 2% bump in fiscal 2018 for all groups. The contract also generates savings with the addition of several steps to the civilian pay structure.

While the city projects saving a combined $16.8 billion in pension and other costs over a 30-year period, it will bear a modest $196 million in up-front costs under the new contract. These costs will delay the city's projected achievement of structural balance by one year to 2019. About 10% of the costs are associated with the elimination of the 2012 pension reforms, specifically the closure of the 2012 Tier 2 pension plan and the movement of employees hired since July 1, 2013 to the Tier 1 pension plan. The movement of the Tier 2 pension eligible workers to Tier 1 is projected to grow the city's UAAL for the Los Angeles City Employees' Retirement System (LACERs) by $18 million.

The labor contract's projected pension relief is particularly important for Los Angeles because the city has an unusually high pension burden and pension contributions account for a relatively high 24% of the city's fiscal 2014 General Fund expenditures. The Moody's adjusted net pension liability (ANPL) was $21 billion in fiscal 2014, or 405% of operating revenues (see Exhibit). Los Angeles' ANPL as a percentage of operating revenues places it as the third highest among the 50 largest local governments in the US and roughly twice the average of 200% for the group. Moody's ANPL is a standardized measure of the unfunded portion of a pension liability.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

EXHIBIT
Los Angeles Pension Liabilities Are Growing



Source: City of Los Angeles CAFRs and Moody's Investors Service

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Stockton Pensions Prevail over Debt in Franklin Templeton's Appeal of Stockton's Bankruptcy Exit Plan

On December 4, Franklin Templeton Investments lost its legal challenge to Stockton, CA's (lease revenue Ba2 stable) bankruptcy exit plan approved in October 2014. The investment firm had argued that its recovery on the city's 2009 A certificates of participation (COPs) should be far higher in large part because retiree pension benefits were untouched. Franklin's total recovery on the 2009 A COPs was about 17.5%, but more significantly it was only about 1% on the $30.5 million unsecured portion of this obligation. The 2009 A COPs were significantly more impaired in the bankruptcy than the city's five other outstanding bond transactions. The decision is credit negative for investors in unsecured local government debt because it leaves in place a bankruptcy plan that significantly impairs such debt while leaving unsecured pensions intact.

While Franklin could choose to appeal, the court's decision to affirm Stockton's plan will likely have far-reaching repercussions for any local government that files for bankruptcy in the nine states covered by the Ninth Circuit's jurisdiction, and possibly beyond. The implication of this decision is that a distressed city considering bankruptcy can pursue a restructuring that relies primarily on debt reduction and fails to adjust pensions. Although unsecured bondholders and retirees have equivalent legal status, pensioners may have higher standing as a practical matter. Additionally, we expect retiree healthcare benefits to be an important factor in negotiations among creditors along with pensions and debt. A key component in the court's rationale for approving a plan that spared pensions was the city's 99% cut in retiree health care benefits.

When Judge Christopher Klein concluded Stockton's bankruptcy process in October 2014, he also ruled that notwithstanding their legal protections pensions can be impaired in Chapter 9. The court confirmed the city's plan of adjustment, which left pensions unimpaired, while most of the city's other major creditors received significant cuts in principal repayment. This approach to debt and pensions was also used in the Vallejo, CA (unrated) bankruptcy and then later repeated in San Bernardino, CA (unrated). With the failure of Franklin's appeal, on top of Vallejo's bankruptcy outcome and the proposed San Bernardino plan of adjustment, we believe that cities in Chapter 9 facing the choice of reducing pensions or cutting debt will now be even more likely to chose to disproportionately cut debt.

Stockton did make significant cuts in employee compensation and almost entirely eliminated its retiree health care obligations. These appear to have been major factors in the court's rationale for determining that the city's plan was equitable. In Vallejo, the bankruptcy plan called for reductions in debt and similarly, significant reductions in health care liabilities, while pension liabilities were also left intact. In the San Bernardino bankruptcy exit plan released in May 2015, the city proposes to pay 100% of its unfunded pension liability to CalPERS, while eliminating 99% of the principal value of its pension obligation bonds (POBs). Like Stockton and Vallejo, San Bernardino faces rising pension costs in the future.

In Stockton, investors received an approximate 50% recovery overall, which includes both lease revenue bonds and pension obligation debt. Franklin Templeton received a total recovery from all sources of about 17.5%, which includes a 1% recovery on the portion of its claim that was unsecured. Bondholder recoveries in Vallejo were approximately 60%. In Stockton, POBs received a 41% recovery, while San Bernardino is proposing a 1% recovery on POBs. San Bernardino's secured lease-revenue bondholders would not be impaired. Ultimate recovery rates for San Bernardino's bondholders may change before the court confirms the plan.

Stockton's bankruptcy plan illustrates the difficulties investors face when confronted with a local government that has both high pension and large retiree health care (Other Post-Employment Benefits, OPEBs) liabilities. The court's decision to approve the city's plan conflated the legally separate claims of pensions and OPEBs in determining whether to confirm the plan of adjustment. The court made the point

that the plan was fair to investors because recovery rates for retirees must be viewed in terms of the recovery for pensions and OPEBs combined. By combining these two distinct classes of claims to arrive at a calculation of losses for retirees, the court provides a justification for eliminating OPEBs while keeping pensions .

Since Stockton emerged from bankruptcy, the city's financial position has significantly improved, resulting in two rating upgrades to its lease revenue debt. While Stockton's revenues have declined by 5% since the end of fiscal 2008, the city has managed to cut expenditures by more than three times that, resulting in five years of consecutive surpluses and a general fund balance equal to 28% of revenues (FY 2014). Together with the city's other expenditure reductions and new sales tax, management forecasts, on an unaudited budget basis, a strong surplus in FY 2015 of approximately $23 million, which exceeds the city's original budget projection by $12.2 million. This strong financial trend will likely continue through FY 2016.

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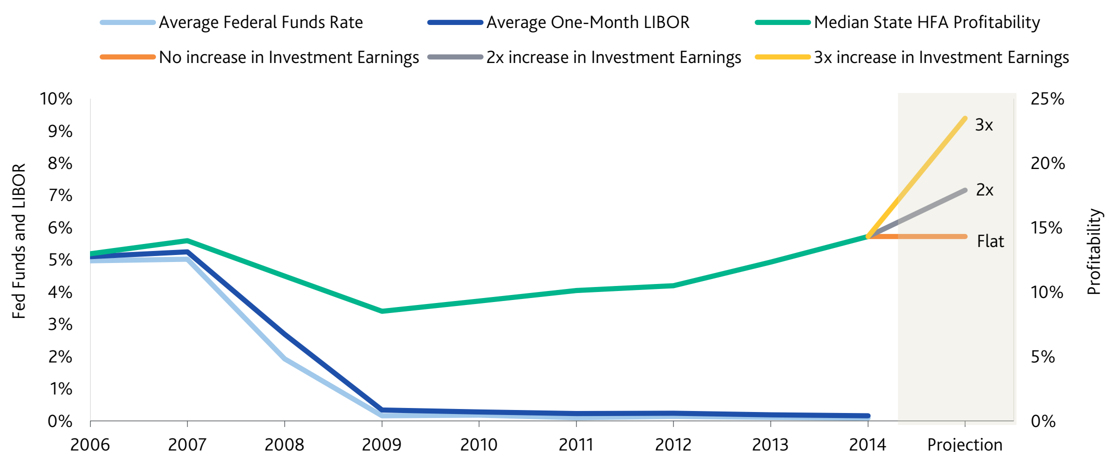
Federal Reserve's Rate Hike Decision Is Credit Positive for Housing Finance Agencies

On December 16, the Federal Reserve raised the short-term interest rate to 0.25% after leaving it at near zero since December 2008. Although the increase is minimal, the Fed's decision is credit positive for housing finance agencies (HFAs) because higher interest rates boost their investment earnings and drive profit margins, while presenting opportunities to grow loan portfolios and rebuild balance sheets.

As of fiscal year-end 2014, roughly 7% of HFAs' assets were held in cash and cash equivalents, which will immediately benefit as the higher short-term interest rates lead to greater investment earnings. Historically, HFA profitability has tracked investment rates closely. Between 2007 and 2009, the steep drop in interest rates led to a decline in HFA profitability. Since then, low interest rates have remained a drag, but HFA profitability has recovered due to earnings from selling mortgage-backed securities in the secondary market and savings from bond refundings. Now, the higher short-term interest rates will boost investment earnings and increase profit margins further. We project HFA profitability will increase by 4% if investment income doubles the 2014 level, and by 8% if investment income triples (in Exhibit 1).

EXHIBIT 1

Higher Investment Earnings Will Lead to Increased HFA Profitability

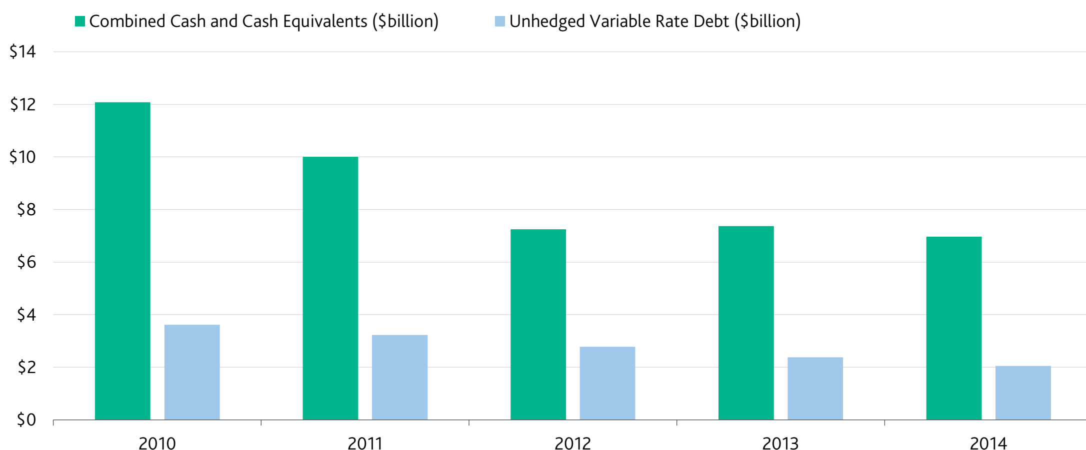


Source: Moody's adjusted audited state HFA financial statements for 38 HFAs, and Federal Reserve Board

As interest rates rise, HFAs will be challenged by higher interest expense on their unhedged variable-rate debt. As of December 2014, about 21% of HFA debt was variable rate, of which 2% was unhedged. However, increased investment earnings on cash held by HFAs will partially offset the impact of the higher interest costs. Cash can also be used to redeem variable-rate bonds if interest rates become too high. As shown in Exhibit 2, the cash and cash equivalents HFAs had in 2014 were equal to three times the amount of unhedged variable rate debt.

EXHIBIT 2

Cash Mitigates Interest Rate Risk of HFAs' Unhedged Variable Rate Debt



Source: Moody's adjusted audited State HFA financial statements for 38 HFAs

Another advantage of higher interest rates is the lowering of HFAs' swap termination costs, thereby providing greater financial flexibility.

From a long-term perspective, higher mortgage rates (close to 6% or higher) would also allow HFAs to grow their loan portfolios. While mortgage rates are not immediately impacted by the short-term interest rates, changes in short-term rates paint the path forward for long-term mortgage rates. Demand for HFA mortgages is driven by the attractiveness of rates on HFA loans relative to those on conventional mortgages.

With rates on conventional mortgages so low, HFAs have found it difficult to originate loans over the past six years. An increase in interest rates can mean fewer borrowers are able to obtain a lower interest rate from a conventional mortgage lender than they can from an HFA. Higher loan originations coupled with issuance of tax-exempt bonds would rebuild HFA balance sheets and further strengthen the sector credit profile. In the last few years, HFAs have financed loans primarily through selling mortgage-backed securities in the secondary market rather than bond financing.

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Illinois' Release of Revenues Is Credit Positive for Chicago and Other Local Governments

On December 7, Illinois (Baa1 negative) Governor Bruce Rauner signed SB 2309, which released state motor fuel taxes (MFT), casino gaming funds and other revenues that had not been distributed to local governments since this past summer because of the absence of an adopted full state budget for the fiscal year ending June 2016. The release is credit positive for Illinois cities and counties including the City of Chicago (Ba1 negative), which carries debt secured by MFT revenue (bonds rated Ba1 negative). The distributions (see Exhibit 1) will have the most significant benefit for Chicago and the small number of local governments that depend on casino gaming distributions.

EXHIBIT 1
Illinois' SB 2309 Local Government Allocations

Revenue Allocated	Funds Released
Motor Fuel Tax Fund Payments	$583 million
Use Tax Payments	$340 million
911 Centers	$154 million
Casino and Video Gaming Revenue Sharing	$145 million

Source: Illinois Municipal League

Chicago is the only rated city that issues bonds primarily backed by the MFT without an additional property tax security. Chicago's MFT revenue bonds are secured by 75% of its annual MFT allocation. Since the state ceased distributions of motor fuel taxes in August, Chicago assumed responsibility for making monthly deposits with the bond trustee using unspent motor fuel tax collections received through July 2015. The city made its final deposit for the January 1, 2016 debt payment in November. The release of MFT revenues will allow Chicago to use current-year allocations to cover the next debt payment due in July 2016.

Casino gaming revenues are a significant revenue source for the handful of municipalities that are eligible for distributions (see Exhibit 2). All four cities that we rate and which receive casino revenue distributions maintain healthy reserves (they reported operating fund balances of more than 25% of revenues as of fiscal 2014) that have bridged the delay in payments. The City of Des Plaines (Aa2), which received the largest total gaming distributions in 2014, adopted a conservative policy to use gaming receipts only for capital expenditures and early debt retirement.

EXHIBIT 2
Casino Gaming Distributions to Illinois Cities

	Rating	Gaming Distributions as a Percent of 2014 Revenues	2014 Gaming Distribution, $ Thousands
Metropolis	Unrated	51.4%	$4,752
Des Plaines	Aa2	27.6%	$24,793
East Peoria	Unrated	19.8%	$5,699
Joliet	Aa2	11.6%	$18,811
Alton	Unrated	10.3%	$3,476
Elgin	Aa1 stable	8.4%	$9,961
Rock Island	Aa2	7.1%	$4,907
Aurora	Unrated	4.7%	$7,444

Note: The City of Des Plaines must remit back to the state the first $10 million of distributions and share the 40% of the remaining proceeds to benefitting communities. Netting transfers from the revenue and expenses, gaming distributions composed 12% of the city's revenues. The City of East St. Louis received $7.0 million in 2014 gaming distributions, but the city's audit is not yet available.

Sources: Illinois Gaming Board, the cities' audited financial statements and Moody's Investors Service

Most of the revenues released by SB 2309 were not primary operating revenue streams. The principal revenue streams that the state shares with local governments, income taxes and sales taxes, continued to flow before SB 2309, even in the absence of a state budget. Under Mr. Rauner's fiscal 2016 budget proposal, which the legislature did not pass, local governments would have had their state-shared income tax distributions cut in half. The potential for income tax distribution cuts or other reductions remains a credit negative for Illinois local governments given the state's deteriorating financial operations.

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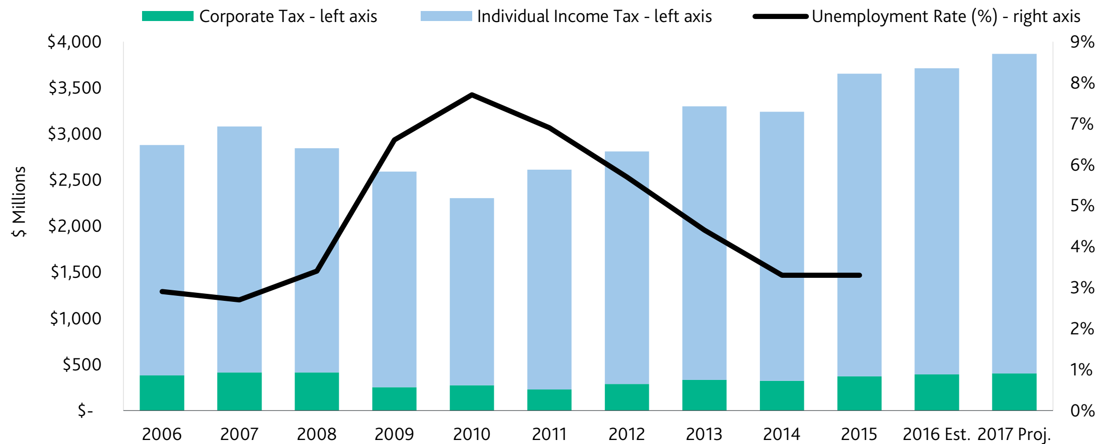
Utah's Budget Proposal Is Credit Positive for School Districts

On December 11, Utah (Aaa stable) Governor Gary Herbert released his proposed budget for the fiscal year ending June 30, 2017, which would increase state funding for K-12 education by 8.1% to $3.1 billion. Growth in state support is credit positive for Utah school districts, which, on average, rely on state funding for approximately 60% of their general revenues. The increased funding, which the state Legislature will address next month with the rest of the budget, would provide additional revenues to support school operations.

Projected growth in the state's personal income and corporate tax revenues drive the proposed state funding increase. Per the state constitution, these revenues are used entirely for K-12 education as well as colleges and universities (see Exhibit 1). The school funding formula for K-12 education (known as the "minimum school program") increased by 5.9% in the fiscal year ending June 30, 2016.

EXHIBIT 1

Revenues for K-12 Education Are Growing Amid Economic Expansion



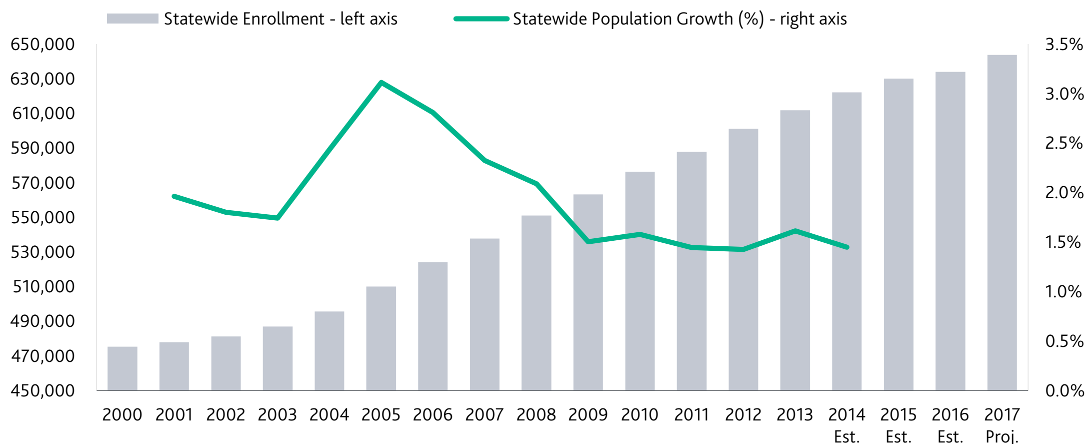
Source: State of Utah; Office of the Governor

These cyclical tax revenues are growing due to an expanding economy. Statewide payroll growth has doubled the nationwide rate this year, according to Moody's Analytics. The state's unemployment rate remains consistently low and was only 3.3% as of September 2015, according to the US Bureau of Labor Statistics.

In-migration supports Utah's enrollment and total population growth as the strong economy attracts working families (see Exhibit 2). Demographics also indicate that the state has relatively large families. The governor's K-12 funding proposal includes $112 million for projected statewide enrollment growth of 1.5% (nearly 9,700 students) for the upcoming 2016-17 school year, as well as stronger-than-expected enrollment growth in the current year.

EXHIBIT 2

K-12 Enrollment Is Growing Due to the Strong Economy and Demographics



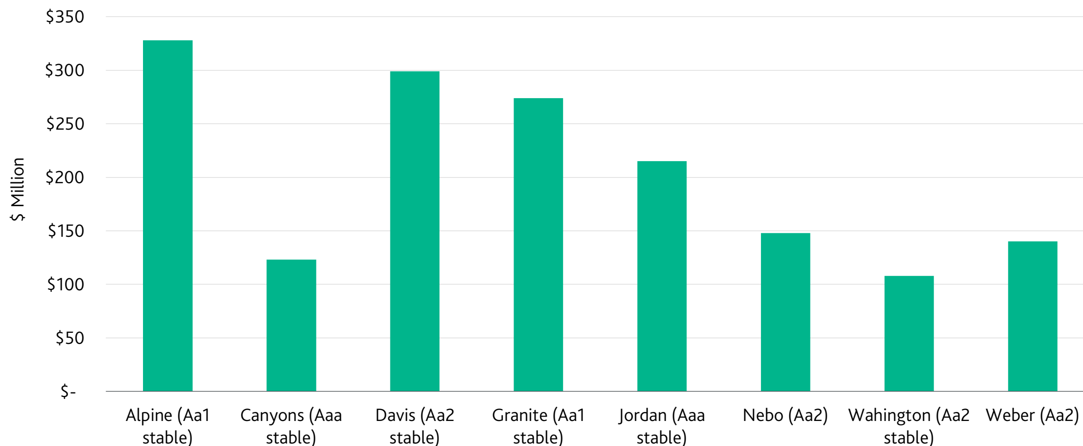
Sources: Utah State Office of Education; Office of the Governor; US Census Bureau

Utah's school funding formula also includes local property taxes that would provide an additional $783 million for K-12 education in fiscal 2017 under the governor's proposal. Property taxes under the formula supplement funding for districts with a relatively low tax base per student.

The biggest recipients of formula funding are expected to benefit the most under the governor's budget proposal (see Exhibit 3). These districts have relied on state support for, on average, two-thirds of their general revenues, which is moderately above the norm for districts.

EXHIBIT 3

Largest Recipients of K-12 State Funding Would Benefit the Most in Fiscal 2017



Sources: Utah State Office of Education estimates for the minimum school program for fiscal 2016

School districts also collect several local tax levies as well as federal funds outside of the state funding formula. The state estimates that discretionary property taxes levied by districts currently provide $1.3 billion of locally controlled funding for districts. Districts have reportedly $675 million of discretionary and unused tax authority available under current state law for operations and capital needs. Districts would also receive approximately $519 million of targeted federal funds in fiscal 2017, as projected in the governor's proposal.

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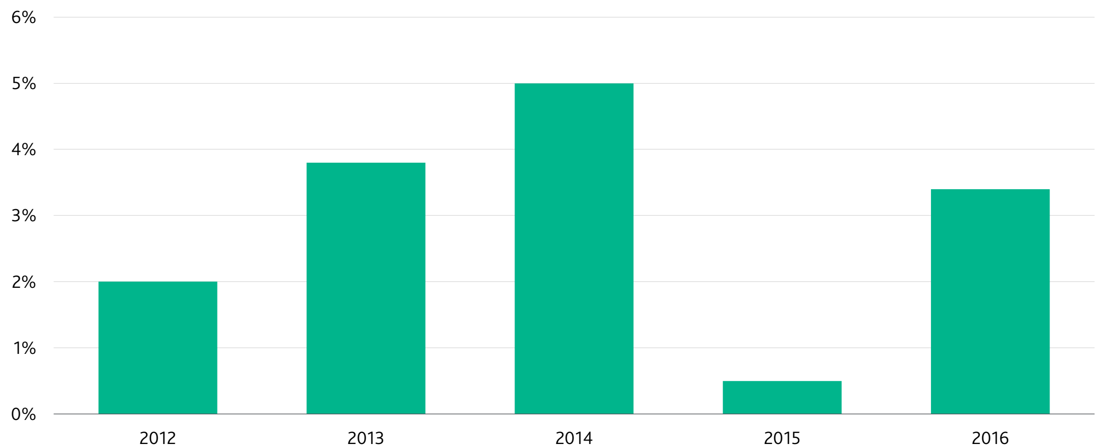
Department of Defense Substantially Increases Housing Allowance for Service Members, a Credit Positive for Military Housing Sector

On December 15, the US Department of Defense (DOD) announced that the Basic Allowance for Housing (BAH) will increase by a 3.4% average in 2016, a credit positive for privatized military housing developers and bondholders. The increase is substantially higher than last year's 0.5% bump and likely to increase revenues for a housing project, leading to growth in a financing's debt service coverage ratios.

The BAH, which provides military service members with an allowance to cover the cost of housing, is the primary revenue stream for privatized military housing developers and, in turn, bondholders. Military personnel who choose to live in privatized military housing pledge their BAH payments directly to the project in lieu of monthly rent payments. As a result, the annual setting of BAH levels is a critical credit event that directly affects the ability of developers to pay debt service to the bondholders.

Not only is the 3.4% increase effective January 1, 2016 substantially higher than last year's BAH increase, but it exceeds the average 2.9% annual increase over the past five years (see Exhibit). Notably, 2016 marks the second phase of a five-year plan approved by Congress that effectively lowers BAH payments to military housing projects. Under the plan, service members receiving the BAH will pay an amount equal to 2% of their housing costs in 2016 out of pocket. All things being equal, without the cost-sharing initiative, the 3.4% BAH increase would be closer to 5%.

Basic Allowance for Housing to Exceed Five-Year Average in 2016



Source: US Department of Defense

While the 3.4% increase is credit positive for the sector overall, the amount is a national average. The DOD establishes specific BAH rates for each military base, reflecting characteristics of the local real estate market and the funding levels can deviate significantly from the national rate. In addition, BAH rates vary based on the pay grades of the service members who occupy the housing. Therefore, the credit effect of the 2016 BAH on individual financings may differ from the national trend.

For example, among the 24 military housing financings we rate, the BAH affecting the projects averaged a 2.2% increase. Six of the transactions were impacted by *decreases* ranging from 0.3% to 8.5% and the remaining 18 by increases ranging from 0.1% to 9.1%. Total debt outstanding for the 24 projects is $9.5 billion.

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Alabama Community College System to Consolidate Seven Colleges in Credit Positive Development

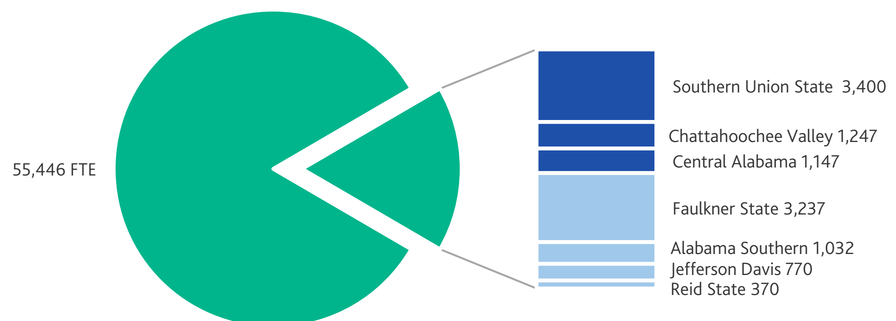
On December 10, the Alabama Community College System (ACCS, A1 stable) Board approved a proposal to consolidate seven of its 26 community colleges. This is a credit positive response to five years of declining enrollment and also indicates a fresh approach taken by a newly constituted independent Board of Trustees. Previously, ACCS did not have its own board but was under the supervision of the State Department of Education. Reducing the number of institutions should also begin to simplify a complex system with decentralized financial systems and reporting. Management does not intend to close any campuses. However, the consolidation should reduce overhead expenses significantly. The system's board will likely consider additional consolidations over time.

The ACCS proposed restructuring follows our predictions of increased consolidations, as well as mergers and closures, in a low enrollment and revenue growth environment nationally. To date, the University System of Georgia (Aa2 stable) has been the most aggressive and successful in combining colleges to redirect more resources to the classroom. Earlier this year, Arkansas State University (A1 stable) successfully merged with Mid-South Community College. However, other proposed mergers have not proceeded due to logistical and financial issues or community concerns. Consolidations of public colleges within a strong system structure will be more likely than those of stand-alone institutions.

The current round of proposed consolidations at ACCS reflects several factors including geographic proximity and senior leadership vacancies. Each of the two umbrella colleges will enroll approximately 10% of the system's overall enrollment (see Exhibit). The consolidation process will take time, including local hearings, review by the Alabama Commission on Higher Education and requiring accreditor approval.

- Central Alabama Community College and Faulkner State Community College will be the umbrella organizations under the proposed consolidations.
- Central Alabama will consolidate with Southern Union Community College and Chattahoochee Valley Community College.
- Faulkner State will consolidate with Alabama Southern Community College, Jefferson Davis Community College and Reid State Technical College.

EXHIBIT 1
Consolidating Colleges Will Comprise 20% of the System's 55,000 Full-Time Equivalent Student Enrollment (Fall 2014)



Source: Alabama Community College System

System leadership intends for the consolidations to yield efficiency enhancement. Most of the 26 colleges within the system are quite small with median enrollment below 1,800 full-time equivalent students. By combining overhead and administrative fixed costs, management aims to devote an increasing share of resources more directly to educational services and programs. Over the last decade, the system's operating expenses have been growing more quickly than operating revenue. While the colleges have been able to increase tuition pricing, leadership wants to maintain affordable access requiring increasing focus on efficient use of resources.

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Brown County, WI and Green Bay Score with Excess Lambeau Field Sales Tax Revenue

By December 31, Brown County, WI (Aaa), Green Bay (Aa2) and 23 other municipalities will share $18 million in excess tax revenues under legislation signed by Wisconsin (Aa2 positive) Governor Scott Walker. The county will receive 25%, or $4.4 million, of the funds. County municipalities will divide the remainder, apportioned by population, with Green Bay receiving the highest share at $5.5 million (see Exhibit). The unanticipated, one-time disbursement is credit positive because it offers an opportunity to pay debt service, among other purposes. The funds became available when a special district had surplus funds after it finished collecting sales taxes for upgrades to Lambeau Field, home of the NFL's Green Bay Packers.

The county will use its full $4.4 million, equivalent to 2.3% of its operating budget, to redevelop land around the Brown County Veterans Memorial Arena. Municipalities can consider lowering property taxes, making debt service payments and backing economic development projects with their allocations. The legislation prohibits use of the funds for general purposes.

Excess Sales Tax Revenue a Boon to County and Local Governments

Governments Receiving Largest Amounts of Funds

Government	Rating	Estimated Amount of Disbursement ($ thousands)	Amount of GO Debt outstanding ($ thousands)	Fiscal 2014 Operating Revenues ($ thousands)	FY 2014 % of Revenues
Green Bay	Aa2	$5,460	$114,981	$100,440	5.4%
Brown County	Aaa	$4,400	$108,542	$187,725	2.3%
De Pere	Aa2	$1,261	$32,745	$20,711	6.1%
Howard Village	Unrated	$975	$10,130	$7,548	12.9%
Ashwaubenon Village	Aa1	$879	$31,760	$16,847	5.2%
Bellevue Village	Aa2	$770	$24,260	$8,149	9.4%
Allouez Village	Aa2	$719	$22,915	$7,917	9.1%
Suamico Village	Aa3	$604	$19,742	$7,519	8.0%
Hobart Village	Unrated	$397	$24,858	$3,726	10.6%
Ledgeview Township	Unrated	$383	$10,625	$3,194	12.0%
Lawrence Township	Unrated	$242	$7,008	$2,421	10.0%

Source: State of Wisconsin, Moody's Investors Service

In September 2000, county voters approved a 0.5% sales tax increase for the Green Bay-Brown County Professional Football Stadium District for renovation, operations and maintenance at Lambeau Field. Collections began November 1, 2000. The stadium district issued $150 million in sales tax revenue-backed debt in 2001. Annual sales tax collections, which averaged $20 million per year, were used to fully retire the debt in 2011.

The stadium district continued to collect the tax to go towards operational expenses and to fully fund all legal requirements. All such obligations were met on April 1, 2015, and the district continued collecting the sales tax for 120 days before it expired on September 30, 2015. The taxes collected during that time led to the $18 million surplus.

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Kentucky Supreme Court Upholds Public Library Districts' Property Taxes

On December 10, the Kentucky (Aa2 stable) Supreme Court denied a motion for discretionary review challenging public library districts' ability to raise property taxes without voter approval. The court's rejection of a motion for discretionary review is credit positive for 11 Moody's-rated districts because they will avoid major funding shortfalls by having to roll back property tax rates.

Library districts depend on local property tax revenues to fund nearly all of their annual operating expenditures. In fiscal 2014, property taxes accounted for an average 91.4% of districts' total operating fund revenues. If the state Supreme Court had reviewed and overturned the appellate court ruling, a rollback scenario would have cut library districts' property tax revenues by an average of 40%.

On March 20, the Kentucky Court of Appeals unanimously reversed two lower court decisions and upheld library districts' ability to increase property tax revenues in a similar manner as cities, counties and other special districts. The original lawsuits were filed by residents of Campbell County (Aa2) and Kenton County (Aa2). The state Supreme Court let stand the appellate court's ruling that prospectively, if a library district created by a petition of the voters seeks to increase its property tax levy by more than 4% annually, it must obtain approval by a petition of the voters. A 4% increase of the property tax levy should be sufficient to cover growth of the operating budget under normal circumstances.

Property Tax Rollback Would Severely Strain Kentucky Library Districts' Primary Revenue Source

Library District	Rating	Potential Operating Revenue Decline Under Rollback[1]	Property Taxes % of Fiscal 2014 Operating Revenues
PIKE COUNTY LIBRARY DISTRICT	Aa3	-68.0%	94.1%
BULLITT COUNTY LIBRARY DISTRICT	Aa3	-59.9%	93.9%
ALLEN COUNTY PUBLIC LIBRARY DISTRICT	A1	-56.4%	94.7%
NELSON COUNTY PUBLIC LIBRARY DISTRICT	Aa3	-53.0%	93.4%
BOYLE COUNTY LIBRARY DISTRICT	A1	-48.9%	91.7%
KENTON COUNTY PUBLIC LIBRARY DISTRICT	Aa1	-43.4%	92.5%
LAWRENCE COUNTY PUBLIC LIBRARY DISTRICT	A1	-41.8%	85.8%
LAUREL COUNTY PUBLIC LIBRARY DISTRICT	Aa3	-30.6%	81.7%
CLARK COUNTY PUBLIC LIBRARY DISTRICT	Aa3	-25.9%	89.3%[2]
MEADE COUNTY PUBLIC LIBRARY DISTRICT	A1	-7.5%	91.9%
PULASKI COUNTY PUBLIC LIBRARY DISTRICT	A1	-4.4%	94.0%

1 Assumes tax rate approved by petition applies to real property only. Represents the product of property taxes as a percentage total annual operating revenues and the percentage tax rate decline from the districts' fiscal 2014 real estate tax rate to the rollback tax rate.

2 Represents fiscal 2013 data.

Source: Districts' legal records, audited financial statements, Kentucky Department of Revenue

RESEARCH HIGHLIGHTS

Aging Baby Boomers to Drive Growth in State HFA Rental Programs

State housing finance agencies (HFAs) will capitalize as demand for affordable rental housing grows among aging baby boomers. Americans 65 and older are a rapidly expanding demographic group. Though most seniors will continue to be homeowners, an influx of renters will significantly increase HFA profitability. Still, HFAs will need to navigate declining federal subsidies to developments targeting seniors.

US State Government: States Have Time to Prepare for ACA's 'Cadillac Tax'

The Affordable Care Act's 40% excise tax on high-cost employer-sponsored health plans will not materially affect most state government employee health costs until several years after the tax is implemented in calendar 2018. States offering their employees and retirees the most generous coverage will bear the greatest impact of the levy, dubbed the "Cadillac tax". When the tax first bites during fiscal 2018, it will affect only a handful of state governments, and most governments will have time to adjust employee benefits to minimize their exposure.

Environmental Risks and Developments: Paris Agreement Advances Adoption of Carbon Regulations; Credit Impact to Rise

The Paris Agreement will advance the adoption of carbon and other greenhouse gas emission regulations, with increasing credit implications for many sectors globally. Our analysis finds three sectors – unregulated power generation, coal mining and coal terminals – with very high credit exposure to carbon regulations. The credit implications for these sectors will grow from increased regulation in the absence of substantial counter-balancing initiatives. A further 11 sectors – including independent oil and gas exploration and production, automobile manufacturers and steel – have high exposure to carbon regulations, and increasing adoption will likely constitute a material credit risk over time.

Federal Reserve's First Rate Hike in Nine Years Will Have Limited Credit Implications

The US Federal Reserve raised interest rates for the first time in nine years on December 16, but it will not have immediate, direct credit implications for our rated financial institutions, corporates, the US government, municipals, utilities and structured finance instruments. Rates will still be historically low and the pace of tightening gradual. A rate hike will imply that the Fed sees sustainable growth in the US economy, strength in the labor market and modest inflation ahead. However, we expect that policymakers will proceed cautiously, keeping a close eye on the US economy and its ability to withstand tighter monetary conditions.

Ports – US: 2016 Outlook – Container Volume Growth Supports Stable Outlook

Our stable outlook for the US ports industry is based on our expectation that US container volume will rise 3%-4% in 2016, supported by continued economic growth in the US and, to a lesser extent, low freight rates and stable labor conditions. Moody's Macroeconomic Board expects that the US economy will grow 2%-3% in both 2015 and 2016. Although weaker global demand and the strong US dollar have weakened export activity, the US is a net importer with an improving economy, which we believe will support US consumption and hence cargo demand at US ports.

Airports – US: 2016 Outlook – Enplanement Growth Drives Positive Outlook

We expect that airlines will continue to add seats in 2016 as the major airlines replace small planes with new, larger planes and as smaller airlines add new planes. Higher-than-expected seat capacity on US airlines, combined with continued growth in the US economy, has resulted in enplanement growth of almost 5% in 2015 through September, exceeding the upper range of our expectations of up to 4% growth in 2015.

RATING CHANGE HIGHLIGHTS

Bon Secours Health System, Inc. Upgraded to A2; Outlook Stable

Dec 10 – We upgraded to A2 from A3 the ratings assigned to Bon Secours Health System, Inc.'s (BSHSI) bonds, affecting $761 million. The outlook is stable. The upgrade follows the transition of the System's Charity market to a joint venture, which represents a significant economic event for BSHSI and is transformative to the system's operating profile, which should strengthen in the future. It also reflects BSHSI's large size, strong governance oversight and enterprise risk management practices, notable deleveraging over the last several years, and adequate and improving balance sheet metrics.

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