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## Summary:
# Cortland, New York; General Obligation

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**Summary:**

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| Cortland GO (AGM) | | |
| *Unenhanced Rating* | BBB+(SPUR)/Positive | Upgraded |

Many issues are enhanced by bond insurance.

## Rationale

Standard & Poor's Ratings Services has raised its underlying rating (SPUR) on the City of Cortland, N.Y.'s general obligation (GO) debt to 'BBB+' from 'BBB' based on its assessment of the city's very strong financial performance estimated for fiscal 2010. The outlook is positive based on our expectation that structural changes implemented by management will allow the city to maintain sound financial operations.

The 'BBB+' SPUR reflects what we view to be weakness in the city's:

- Low-to-adequate income levels and low per capita market valuation;
- Recent history of negative year-end fund balances; and
- Sizable other postemployment benefit (OPEB) liability.

However, in our view, these weaknesses are somewhat offset by the city's:

- Proximity to the economies of Syracuse, Ithaca, and Binghamton, N.Y., and roughly average unemployment levels;
- Very strong financial results estimated for fiscal 2010, coupled with structural changes implemented by management that should allow the city to maintain sound financial operations; and
- Low-to-moderate debt burden with above-average principal amortization.

The city's full faith and credit pledge secures the city's outstanding GO debt.

Cortland has closed three of the past four audited fiscal years with negative unreserved general fund balances. In fiscal 2008, a $451,000 decrease in the city's general fund balance resulted in a year-end balance of negative $307,000, with an unreserved general fund balance of negative $427,000, or negative 2.5% of general fund expenditures. The decrease was driven primarily by a $913,000 shortfall in property taxes.

Since 2008, however, new management has taken steps to improve the city's financial results, such as implementing an in rem foreclosure process to its tax collection procedure, whereby after three years delinquent the city may auction properties for unpaid taxes. In addition to producing direct revenue, the tax sale process has significantly improved current-year property tax collections. In 2009, the year of tax sale implementation, current-year collections improved to 95.9% compared with 94.2% and 94.6% in 2007 and 2008, respectively. In 2010, the current-year collection rate improved another 1.3 percentage points to 97.2%. Officials have also pursued health insurance alternatives for all city employees.

In fiscal 2009, the city produced a $158,000 general fund increase, driven by $577,000 of expenditure savings;

despite the improvement, the fund balance remained in deficit at negative $149,000, with an unreserved fund balance of negative $293,000. General fund cash at the close of the fiscal year totaled $460,000, or 10 days' cash, which we consider low.

For the close of fiscal 2010, the city's draft financial statements show a sizable $1.94 million increase in the total general fund. The unreserved general fund balance is estimated to have increased $1.8 million to positive $1.5 million, or 9% of estimated general fund expenditures, which we would consider strong. Furthermore, unrestricted general fund cash is estimated at $2.99 million for the Dec. 31 close of the year, equal to 66 days' cash, which we would consider good. Modest revenue shortfalls in departmental income ($220,000) were far outweighed by positive revenue variances for real estate property taxes ($1.23 million) and nonproperty tax items (primarily sales taxes, $378,000). State aid showed a variance of $410,000, primarily because a state highway grant was recorded in the city's capital projects; the variance was offset by a corresponding positive transportation expenditure variance, as the expenditures related to the grant were reported in the capital projects fund. Also contributing to the sizable estimated increase was a positive expenditure variance for employee benefits ($294,000), which reflected staff retirements.

Standard & Poor's still considers Cortland's financial management practices "standard" under its Financial Management Assessment (FMA) methodology, indicating the finance department maintains adequate policies in some, but not all, key areas. However, we have adjusted our budget assumptions assessment to standard from vulnerable, reflecting the city's improved budgeting practices over the past two years. According to management, the city is in the process of drafting new financial policies and plans to reinstitute five-year capital planning. With a new finance director assuming control in the coming months, we will continue to monitor the city's financial management policies and practices and adjust our assessment accordingly.

Cortland is located in central New York State and is the seat of Cortland County (A+/Stable). The city is roughly 37 miles south of Syracuse, 21 miles northeast of Ithaca, and 42 miles north of Binghamton. The city's population has been stable over the past five years, totaling 18,644 in 2010. Residents have access to the employment bases of Syracuse, Ithaca, and Binghamton, though most work within the city itself. Leading city employers include State University of New York (SUNY) Cortland (1100 employees), Cortland Regional Medical Center (850), and Pall Trinity Micro Corp. (manufacturer of industrial filters and filtration systems, 816). Unemployment rates within the Cortland micropolitan area have historically trended very slightly above state and national levels; in 2010, the unemployment rate averaged 9.1%, slightly lower than the nation's 9.6% but slightly higher than the state's 8.6%.

In our opinion, city wealth and income levels remain low to adequate, but we recognize that the proportionately large student population somewhat skews these metrics (of the 7,200 who attend SUNY Cortland, about 3,000 live in the city). After increasing 31% for fiscal 2009 due to a revaluation, the city's total assessed value (AV) decreased 0.6% for fiscal 2010 and increased just 0.1% for fiscal 2011. The 2011 AV totals about $523 million; corresponding full market value increased a modest 2.2% for fiscal 2011 to $539 million, or a low $28,900 per capita. Median household effective buying income is 66% of the U.S. level, which we consider adequate, while per capita effective buying income is 62% of the U.S. level, which we consider low.

The city's debt burden is, in our opinion, low to moderate. We consider overall net debt low at $1,260 per capita, but moderate at 4.4% of market value. Debt service carrying charges have been moderate, averaging 11.4% over the past three audited fiscal years. The city's principal amortization schedule is front-loaded, allowing for above-average amortization of 77% of principal through 2021 and 100% through 2031. The city has identified potential capital projects at City Hall and its fire station with a potential cost of $6 million to $7 million, but no plans have been formalized nor have any of the projects been authorized as yet.

The city participates in the state Local Employees' Retirement System and the state's Local Police and Fire Retirement System. The city is current on all of its contributions to the respective systems. The city also offers its employees other postemployment benefits, for which is has an unfunded liability of $49.5 million, nearly six times its covered payroll. The city pays for such benefits on a pay-as-you-go basis; in 2010 it contributed an estimated $1.6 million, roughly 36% of the actuarially determined annual required contribution. Management is currently investigating potential health plan design changes that may lower the OPEB liability.

## Outlook

The positive outlook reflects our expectation that the rating could be raised sometime in the next two years based on the very strong financial results estimated for fiscal 2011 and the structural changes implemented by management, which should allow for continually sound financial operations. If incoming management continues the trend of stable to positive financial operations, we could raise the rating one to two notches. Strengthening of the city's financial policies and practices could also contribute to a one- to two-notch upgrade.

## Related Criteria And Research

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: Key General Obligation Ratio Credit Ranges – Analysis Vs. Reality, April 2, 2008

Complete ratings information is available to subscribers of RatingsDirect on the Global Credit Portal at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.