

Letter from Chief Financial Officer

I am the chief financial officer of the City of South Bend, Indiana. This letter is in support of the use of the bond rating test to demonstrate financial responsibility for taking corrective action and compensating third parties for bodily injury and property damage caused by sudden accidental releases and nonsudden accidental releases in the amount of at least one million dollars (\$1,000,000) per occurrence and one million dollars (\$1,000,000) annual aggregate arising from operating (an) underground storage tank(s).

Underground storage tanks at the following facilities are assured by this bond rating test: 701 West Sample Street, South Bend, IN 46619 and 3113 Riverside Drive, South Bend, IN 46628.

The details of the issue date, maturity, outstanding amount, bond rating, and bond rating agency of all outstanding bond issues that are being used by the City of South Bend to demonstrate financial responsibility are as follows:

Issue Date:	Maturity Date:	Outstanding Amount:	Bond Rating:	Rating Agency
3/29/2018	1/15/2038	\$4,700,000	AA	S&P

The total outstanding obligation of \$4,700,000, excluding refunded bond issues, exceeds the minimum amount of one million dollars (\$1,000,000). All outstanding general obligation bonds issued by this government that have been rated by Moody's or Standard & Poor's are rated as at least investment grade (Moody's Baa or Standard & Poor's BBB) based on the most recent ratings published within the last twelve (12) months. Neither rating service has provided notification within the last twelve (12) months of downgrading of bond ratings below investment grade or of withdrawal of bond rating other than for repayment of outstanding bond issues.

I hereby certify that the wording of this letter is identical to the wording specified in 329 IAC 9-8-14(d) as such regulations were constituted on the date shown immediately below.

Dated:

12/26/2019

Signed:


Daniel Parker
City Controller


Certification of Financial Responsibility

The City of South Bend hereby certifies that it is in compliance with the requirements of 329 IAC 9-8.

The financial assurance mechanism(s) used to demonstrate financial responsibility under 329 IAC 9-8 is (are) as follows:

<u>Type of Mechanism:</u>	Local Government Bond Rating Test
<u>Name of Issuer:</u>	City of South Bend:
<u>Amount of Coverage:</u>	\$1,000,000
<u>Effective Period of Coverage:</u>	Perpetual
<u>Type of Coverage:</u>	Taking corrective action and compensating third parties for bodily injury and property damage caused by accidental releases


Date: 12/30/2019



Daniel Parker
City Controller, City of South Bend

Witnessed by:

Date: 12/30/2019



Signature

Benjamin J. Dougherty

Name of Witness

RatingsDirect®

Summary:

South Bend, Indiana; General Obligation; General Obligation Equivalent Security

Primary Credit Analyst:

Anna Uboytseva, Chicago (1) 312-233-7067; anna.uboytseva@spglobal.com

Secondary Contact:

Benjamin D Gallovic, Chicago 312.233.7070; benjamin.gallovic@spglobal.com

Table Of Contents

Rationale

Outlook

Related Research

Summary:

South Bend, Indiana; General Obligation; General Obligation Equivalent Security

Credit Profile

US\$5.43 mil GO bnds ser 2018 due 01/15/2038

Long Term Rating AA/Stable New

South Bend Bldg Corp, Indiana

South Bend, Indiana

South Bend Bldg Corp (South Bend) GO

Long Term Rating AA/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AA' long-term rating to South Bend, Ind.'s \$5.43 million general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA' rating on existing ad valorem property tax-supported debt issued by and on behalf of the city. The outlook is stable.

Securing the bonds are ad valorem property taxes on all taxable property within city limits. South Bend expects to pay debt service from emergency medical service revenues, local income tax revenues, and tax increment finance revenues from the River East Development Area, although these revenue sources are not formally pledged to the bonds. The city will fund a debt service reserve fund that meets the three-prong test requirements with bond proceeds and will use proceeds to build a new fire station and a small training center.

The ad valorem property tax pledge is subject to state circuit-breaker legislation, which caps the property tax burden for taxpayers based on a percent of the real estate parcels' gross assessed value. This can, and often does, reduce the total tax levy. The levy to cover debt service, however, is statutorily protected, allowing South Bend to distribute circuit-breaker losses first across nondebt service funds that receive property taxes. We rate this debt at the same level as our view of the city's general creditworthiness. . We affirmed the 'AA' rating on the existing lease rental bonds. The levy of taxes to pay rentals is not subject to annual appropriation under Indiana law. However, lease payments are subject to abatement risk, because the city is required to abate lease rentals in the event the leased property is not available for use. Mitigating abatement risk, in our view, are the lease requiring the city to maintain at least two years of lease interruption insurance and casualty insurance equal to the full replacement cost of the damaged equipment. There is no construction risk, because the project is complete and occupied.

The 'AA' ratings further reflect the following rating factors for the city:

- Weak economy, with projected per capita effective buying income at 67.0% and market value per capita of \$45,626, though that is advantageously gaining from a local stabilizing institutional influence;
- Strong management, with good financial policies and practices under our Financial Management Assessment

methodology;

- Adequate budgetary performance, with a slight operating surplus in the general fund but an operating deficit at the total governmental fund level in fiscal 2016;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 77% of operating expenditures;
- Very strong liquidity, with total government available cash at 20.4% of total governmental fund expenditures and 1.8x governmental debt service, and access to external liquidity we consider exceptional;
- Adequate debt and contingent liability position, with debt service carrying charges at 11.5% of expenditures and net direct debt that is 108.4% of total governmental fund revenue, as well as rapid amortization, with 68.2% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Weak economy

South Bend, with an estimated population of 100,785, is located in St. Joseph County, in north central Indiana. It is the fourth-largest city in the State of Indiana.

South Bend has a substantial health care, manufacturing, and higher education presence. The city is home to several colleges and universities, most notably the University of Notre Dame, which employs more than 6,000 people and has a student body of about 12,300. This presence is a stabilizing factor for the economy, although it suppresses, to an extent, both incomes and market value per capita, in our opinion. South Bend has a projected per capita effective buying income of 67% of the national level and per capita market value of \$45,626.

The city's economy is growing moderately. Indiana's first, tribal casino, a sizable, entertainment complex, opened its doors in early January 2018. South Bend is focusing its efforts on strategic investments into smaller technology companies; it expects over \$200 million in private investments to support 700 new jobs. A former Studebaker assembly plant will be remodeled and converted into a large technology campus over the next 10 years as a part of the large-scale, \$160 million project. Notre Dame is working with the city on several partnerships that could bring high-tech jobs. As well, numerous apartment complexes, hotels and residential units are under construction.

The local unemployment rate usually exceeds the state and national rates, but the regional economy generally moves in tandem with the broad national economy; it was at 4.5% in 2016. The city's wealth and income levels, however, are persistently below average and continue to slip, likely due to the shortage of high-paying jobs in the area. Therefore, despite ongoing economic development, we anticipate income and market value metrics will remain at levels we consider weak in the near future.

Strong management

We view the city's management as strong, with good financial policies and practices under our Financial Management Assessment methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them regularly.

Officials review several years of historical data when forming the budgets and much of the revenues are certified in advance by the Department of Local Government Finance. South Bend's budgets are forward-looking, comprehensive, and detailed. Long-term financial forecasting and a comprehensive long-term capital improvement plan are integral

parts of the city's budgeting process. The council sees monthly reports that contain budget-to-actuals and investment holdings. South Bend has debt and investment policies and has adopted reserve policies for all its funds, including a minimum 25% of expenditures policy for the general fund. We believe these are well-established policies and practices, which will continue to support a strong management profile in the near future.

Adequate budgetary performance

We have adjusted financial data to better portray what we view as a more accurate depiction of the city's recurring activity by adding recurring, below-the-line general fund transfers in and out, and removing one-time revenue and spending. In addition, our analysis considers South Bend's public safety local option income tax and county option income tax (COIT) funds as part of the general fund, given that the services rendered in these funds are highly comparable to what we consider basic general fund operations.

The city reports its financial results according to generally accepted accounting principles (GAAP), unlike the vast majority of Indiana municipalities, which report on a cash basis of accounting. The Indiana State Board of Accounts has audited the 2016 Comprehensive Annual Financial Report (with a Dec. 31 year-end).

South Bend's budgetary performance will remain adequate in our opinion. The city had slight surplus operating results in the general fund of 0.6% of expenditures, but a deficit result across all governmental funds of negative 1.6% in fiscal 2016. It budgeted for small operating deficits or essentially break-even results across the general and total government funds for 2017 and 2018. While the 2017 audit is ongoing, officials report South Bend ended 2017 with a \$2 million general fund surplus. The city adopted a full costing model for internal services, allocating administrative and technology and innovation costs to each department. This allocation strategy encouraged departments to get a better grasp of their actual needs, yielding cost savings in various departments in 2017.

South Bend's budgets are structure-balanced. Key revenue categories (the general fund derives 47.0% of its revenue from property taxes, 20.0% from income taxes, and about 5.5% from utility in lieu of taxes payments) are trending positive due to higher property assessments and collection rates and expenditures are mostly under control.

Of note, the city's revenue losses caused by circuit breakers are projected to increase \$12 million (an estimated 36% increase) by 2020, the year when some debt exemptions from property tax caps are set to expire. This decrease will likely translate to an approximately \$3 million general fund deficit beginning 2020. Management is aware of this and developing strategies to address the matter. The city's robust accumulated reserves (\$64 million) and a practice of proactive budget adjustments would allow South Bend to deal with the upcoming fiscal issues efficiently, in our opinion. Nevertheless, the looming revenue reduction is substantial, and the current forecast does not anticipate any unforeseen economic events. We will monitor the situation and could take a negative rating action if the city's finances start to weaken.

Very strong budgetary flexibility

South Bend's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 77% of operating expenditures, or \$64.0 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor. The balance includes \$41.9 million (50.3% of expenditures) in the general fund and \$22.1 million (26% of expenditures) that is outside the general fund but legally available for operations.

As noted, the general fund includes the city's public safety local option income tax and COIT funds, while the nongeneral available funds include the city's rainy day fund and county economic development income tax. While reserves might decline modestly based on planned spending, we expect they will remain very strong.

Very strong liquidity

In our opinion, South Bend's liquidity is very strong, with total government available cash at 20.4% of total governmental fund expenditures and 1.8x governmental debt service in 2016. The numbers do not include \$154 million in investments that the city also possessed at the end of 2016; however, it could convert some of the investments to liquid assets quickly.

South Bend has issued bonds frequently during the past 15 years, including bonds backed by ad valorem property, hotel and motel, and income taxes, plus water and sewer revenue bonds. The city does not have a permissive investment profile. We anticipate liquidity will remain very strong, despite potential drawdowns.

Adequate debt and contingent liability profile

In our view, South Bend's debt and contingent liability profile is adequate. Total governmental fund debt service is 11.5% of total governmental fund expenditures, and net direct debt is 108.4% of total governmental fund revenue. Approximately 68.2% of the direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor.

The city's debt issuance plans include \$12 million in special benefits and tax increment supported debt.

One of the key challenges South Bend is facing, in our opinion, is the need to comply with the federal mandate to reduce the amount of untreated wastewater overflowing into the St. Joseph River, which the city estimates will cost \$700 million on top of the \$150 million that it has already spent on the project. Although the project will be likely be paid with water and sewer fees, it could hurt South Bend's finances (debt could more than double and the project could require governmental funds support). To avoid this, the city's engineers developed an alternative plan that could save it \$500 million, and are discussing details with federal agencies.

Some of South Bend's obligations were privately placed, including \$3.5 million in series 2017 taxable economic development revenue bonds, \$25 million in 2017 taxable economic development revenue bonds (Studebaker Project), and \$27.5 million in 2015 sewage works revenue refunding bonds. We have determined the obligations do not contain any unusual covenants, acceleration provisions, or mandatory tender days that could negatively affect the city's liquidity.

South Bend's combined required pension and actual other postemployment benefits contributions totaled 5.8% of total governmental fund expenditures in 2016. The city made its full annual required pension contribution in 2016.

South Bend contributes to two plans administered by the state: Indiana Public Employees' Retirement Fund (PERF) and the 1977 Police Officers' and Firefighters' Retirement Fund ('77 Fund). These plans are cost-sharing, multiemployer defined benefit plans (the plans share all risks and costs, including benefit costs, proportionately by the participating employers). As of Dec. 31, 2016, the city reported a liability of \$25 million for its proportionate share of the PERF net pension liability. The net pension liabilities for 1977 police officers' and firefighters' pension and disability fund were moderate, at \$3 million, because these plans are almost 100% funded. South Bend's largest plan, PERF, was

76.6% funded in 2017 (based on Governmental Accounting Standards Board Statements No. 67 and 68). The funded ratio is slightly below the recommended 80% level; however, the assumptions built into the valuations are reasonable. Therefore, we expect pension costs to remain low and manageable in the next few years.

The city also sponsors a retiree health care plan, and pays 70% of police and fire member premiums. Civilian employees can buy into the plan, but must cover 100% of premiums. The city uses a pay-as-you-go approach for retiree health care and the annual costs are rather small.

Strong institutional framework

The institutional framework score for Indiana municipalities is strong.

Outlook

The stable outlook reflects our view of South Bend's consistently very strong available reserve position and predictable and transparent financial profile supported by strong management practices. The city's robust accumulated reserves and a practice of proactive budget adjustments would allow South Bend to deal with looming revenue losses efficiently, in our opinion. We expect the city's finances to remain stable during our two-year outlook period, therefore we don't expect to raise or lower the rating.

Downside scenario

If South Bend were to experience budget pressures and its performance starts to deteriorate during our two-year outlook horizon, we could lower the ratings. We could also lower the rating if the city's debt burden increases significantly.

Upside scenario

We do not expect to raise the rating in the next two years because income levels in South Bend are well below national averages and continue to slip despite the new developments. Beyond then, if incomes and market value per capita improve and all other credit metrics are stable or improve, we could raise the rating.

Related Research

- 2017 Update Of Institutional Framework For U.S. Local Governments
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014

Ratings Detail (As Of March 13, 2018)

South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed

Ratings Detail (As Of March 13, 2018) (cont.)

South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
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<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend pk dist bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend Redev Auth, Indiana		
South Bend, Indiana		
South Bend Redev Auth (South Bend) GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend Redev Auth (South Bend) GOEQUIV		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend Redev Auth (South Bend) GOEQUIV		
<i>Long Term Rating</i>	AA/Stable	Affirmed
South Bend Redev Dist, Indiana		
South Bend, Indiana		
South Bend Redev Dist (South Bend) GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed

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