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Summary:

Moreno Valley Community Redevelopment Agency, California; Tax Increment

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Credit Profile		
Moreno Vy Comnty Redev Agy tax incr		
Unenhanced Rating	A-(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

Rationale

Standard & Poor's Ratings Services affirmed its 'A-' long-term rating and underlying rating (SPUR) on Moreno Valley Community Redevelopment Agency (RDA), Calif.'s series 2007A tax allocation bonds. The outlook is stable.

The ratings reflect our view of:

- The large 4,676-acre project area made up primarily of residential uses, combined with the area's participation in the Inland Empire economy;
- Good coverage of maximum annual debt service (MADS) for senior and subordinate debt service (including the series 2007A bonds) at 1.75x MADS based on fiscal 2016 assessed value (AV); and
- Recent growth in AV, which has caused coverage to improve during the past four fiscal years.

Offsetting factors include our opinion of the bonds' unrated debt service reserve (DSR) surety, combined with cash management practices that, while sufficient to meet semiannual debt service requirements, violate bond indenture provisions and increase liquidity risk.

The series 2007A bonds are secured by tax increment revenues from the project area, net of housing set-asides and pass-through payments, and on a subordinate basis to payments made to the city under the Agency Towngate Agreement for the Towngate CFD bonds. The series 2007A bonds have a DSR fund by an Ambac Assurance Corporation surety bond.

The agency has pledged tax increment revenue on a senior basis to the 2007A bonds under the Agency Towngate Agreement, which provides for payment of the CFD 1987-1 special tax bonds. This prior lien on tax increment revenues is closed. MADS on the combined obligations occurs in 2038, while the agency's senior obligation due under the Agency Towngate Agreement expires in fiscal 2023.

Coverage of combined MADS is good, in our view, at 1.75x in fiscal 2016. Coverage has increased since fiscal 2012, as has AV, which has grown by an average of 4.3% annually; however, coverage remains below 2011 levels due in part to step-ups in agency pass-through payments, together with the loss of certain unpledged tax revenue attributable to city pension override levy, which the agency no longer received following dissolution. We expect the agency's primarily residential tax base to continue to grow, albeit at a more moderate pace, along with new commercial and industrial development in the area, particularly in the expanding warehouse and logistics sector. The volatility ratio of 0.20 indicates that tax increment revenue is moderately sensitive to changes in AV. Based on current MADS coverage and volatility, we calculate that the agency could withstand the loss of its top 10 taxpayers before coverage on the bonds dropped below 1x.

The city of Moreno Valley is acting as successor agency (SA) to the former Community RDA after the state legislature and a subsequent court ruling dissolved all RDAs in California in February 2012. The agency has completed and resolved all required due diligence reviews by the state Dept. of Finance, and has received its finding of completion. The State Controller's Office asset transfer review found that the former RDA improperly transferred $298,000 to the city in 2011, and the SA reports that it will comply with the controller's order to reverse the transfer. Recent cleanup legislation (State Bill 107) clarified that cumulative tax increment limitations no longer apply to SAs.

California's RDA dissolution law requires SA and oversight officials to adhere to deadlines for requesting debt service payment amounts on recognized obligation payment schedules (ROPS) to receive tax revenue. Since the law limits the SA revenue to payment on enforceable obligations on its ROPS, and since it requires more proactive management than under the predissolution flow of funds, we believe an SA's debt management practices and DSRs after dissolution become more important to credit quality. The SA has been requesting debt service on its semiannual ROPS as it becomes due, which we consider to be out of compliance with indenture provisions requiring it to set aside full annual debt service with the trustee before releasing pledged revenue to pay other obligations. To date, semiannual requests have provided more than sufficient cash to cover debt service. The 2007A bonds have a DSR funded with a surety policy from Ambac Assurance Corp. In our view, the lack of a rated surety provider increases the chance that a cash flow interruption could lead to a missed payment on the bonds

Dissolution law permits the SA to issue indebtedness only for limited purposes, such as paying or amending an enforceable obligation, generating savings, or flattening spikes in debt service. Although the agency has enforceable obligations for which it could issue additional debt under dissolution law, we believe additional debt is unlikely, based on conversations with management. Furthermore, we understand that the agency will seek a Last and Final ROPS in fiscal 2017, which precludes additional debt issuance. The bond documents do have an additional bonds test.

The Moreno Valley Redevelopment Project encompasses 4,676 acres, or approximately 14% of the city of Moreno Valley. The tax base is moderately concentrated, in our view, with the 10 largest taxpayers making up 25% of incremental AV and 20% of total AV in fiscal 2016. Moreno Valley (population: 200,000) is located 12 miles southeast of the city of Riverside in the Inland Empire. In our view, the city has moderate median household income, at 101% of the national level. The project area is primarily residential (50%), and it lost a combined total of 14% of AV during the recent recession.

As of the most recent disclosure (fiscal 2014), outstanding taxpayer appeals in the project area totaled $133 million, or 4.7% of incremental AV. Based on historical reduction rates, management estimates that only $7.6 million in value will be lost due to successful appeals, which we consider modest, at 0.9% of incremental AV.

Outlook

The stable outlook reflects our expectation that the agency will continue monitor projected revenues and manage debt repayment to minimize the chance of a draw on the DSR. The stable outlook further reflects our expectation that AV will remain stable, or possibly improve, during the two-year outlook horizon.

Upside scenario

Although we do not expect to do so during the next two years in light of the agency's DSR, we could raise the ratings over the long term if AV growth should result in significantly stronger coverage and more tax base diversity than those of similarly rated peers, and if the agency effectively closes its parity lien through the Last and Final ROPS process.

Downside scenario

Should large taxpayer appeals or unrelated AV declines cause coverage to deteriorate, we could lower the rating. Although we do not expect to do so, we could lower the rating multiple notches should the agency's cash flow management practices weaken or should coverage on the bonds fall below a strong level, given the lack of an investment-grade reserve surety provider.

Related Criteria And Research

Related Criteria

- USPF Criteria: Special-Purpose Districts, June 14, 2007
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

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