



CITY OF STAMFORD  
OFFICE OF ADMINISTRATION

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December 15, 2003

Dannel P. Malloy, Mayor  
The Members of the Board of Finance

Ladies and Gentlemen:

Section 8-20-3 of the Charter of the City of Stamford requires me to report annually upon the amount and nature of expenditures that, in my opinion, the City may incur safely for capital projects during each of the next six succeeding years, and the effect of such expenditures upon the General Fund budgets for each of those years. I am pleased to transmit my report herewith.

INTRODUCTION

In analyzing the amount of debt that the City may safely incur, we must consider several distinct factors. Among the items that must be considered are the following:

- Capital Needs of the Community
- Legal Debt Limitations
- Impact of the Proposed Plan on Debt Position & Credit Rating
- Impact of the Plan on Future Operating Budgets
- Level of Authorized But Unissued Debt
- Projected Drawdown Schedule and Financing Strategy
- Alternative Funding Options

After considering each of the above factors, I am recommending a maximum six-year capital-spending plan, net of direct grants and non-general obligation (GO) bond financing sources, of \$192,000,000. This is \$12 million (6.7%) more than was recommended in the last two years. This increase is supported by the conservative projections detailed later in this report. The underlying bases for this increased capacity are the City's long-term fiscal responsibility in the area of debt management, combined with historically low interest rates achieved in recent borrowings – significantly lower than earlier projections had assumed.

School construction projects are anticipated to comprise the largest single portion of the City's capital budget in the coming years. To meet these on-going requirements, I am recommending that \$32.0 million be authorized in each year of the six year plan. To the

extent that projects are funded with current tax revenues (pay-as-you-go financing), with grants or with proceeds from the Capital Non-Recurring Fund, this will reduce the amount that must be bonded and provides additional financial capacity to assume higher levels of gross capital spending. This recommendation is, in my opinion, sustainable within our existing budget. I do caution, however, that some trends may undermine our debt capacity in the future. We must recognize that future stagnation of the grand list or cuts in state aid, especially school construction reimbursements, will have a negative effect on our capacity to fund capital improvements by any method. In addition, the troubling growth rate in education costs may, if unchecked, will constrain our ability to support our capital program in the future, particularly given the size of the Board of Education's capital requests.

## NEW ISSUES

### A) WPCA Revenue-Backed Debt

This fall, the City, on behalf of the Stamford Water Pollution Control Authority issued \$12.5 million in revenue bonds to finance sewer improvements other than the treatment plant upgrade. That major project, which will cost approximately \$105 million and is well underway now, will be financed by grants and loans from the State's Clean Water Fund (CWF). The 2% CWF loans for the upgrade are also secured with a revenue pledge of sewer fees, rather than the full faith and credit pledge that secures the City's General Obligation debt. The change to revenue-backed debt was undertaken because financing sewer projects as general obligations of the City would crowd out other necessary capital improvements. By using a revenue pledge of WPCA user fees, we can exclude WPCA debt from our calculation of the City's safe debt limit.

The issuance of revenue bonds for the WPCA marks an important step for that entity, ensuring that decisions about sewer and treatment upgrades will be based on environmental, health, and engineering impacts and not on competition from schools and other public improvements for scarce capital resources.

### B) Changes to State Law Regarding School Construction

Public Act 02-6 of the May Special Session made a significant change to the State school construction program. Under this new law, the State Board of Education now *requires* that we demonstrate that at least the full local share of any project for which we will be seeking State reimbursement has been appropriated before the State will accept the school building grant application. As a result, it is advisable to change our appropriation practice with respect to school construction projects that are eligible for this partial State reimbursement. Continuing with our historical practice of appropriating large projects over multiple years will risk our reimbursements from the state, now about 20% of eligible projects.

For this reason, I am recommending that we begin making a distinction between our annual capital spending authorization for purposes of compliance with the local Safe Debt Limit, and our annual capital appropriation provided for in the City's capital budget. In order to maximize State grant reimbursement, I would recommend that the City's annual capital budget include the full amount necessary to complete each school

project upon the initiation of the project. This change will not impact projects that have already been approved.

However, since in practice it will typically still take several years to complete each school project, I do not believe that the proposed change outlined above requires us to modify the annual Safe Debt Limit recommendation. I suggest that in the case of school construction projects for which we intend to seek State reimbursement, the Capital Budget include a drawdown schedule indicating how much will be spent in which fiscal years. The drawdown amount, rather than the total appropriation, would then count toward the safe debt limit in that year. In essence, for Safe Debt Limit purposes, we will recognize appropriations for school projects over the expected term of construction.

## **ANALYSIS OF DEBT LIMIT RECOMMENDATION**

### **A) Capital Needs of the Community**

The capital needs of the City are of primary importance in developing a recommended spending plan. Just as it is inappropriate to propose capital spending simply because of a perceived excess in capital capacity, so too is it inappropriate to establish a "safe debt limit" without consideration for the City's essential capital needs. High school enrollments are stressing the capacity of our existing schools already, and the construction of additional classroom space to address that growing problem is slated for next year. There are capacity problems within the elementary schools as well. Additionally, the City must commit funding to ensure adequate maintenance of its infrastructure. Significant capital projects in the six-year plan include Board of Education building additions and refurbishment, sewers, bridges, street and roadway reconstruction, and other facilities upgrades. Favorable debt ratios are meaningless, if they come at the expense of deferred maintenance, or if long term investments are not made in projects which reduce operating costs or foster economic growth.

The capital plan over the last few years has been larger than was the case in the early 1990's. As a consequence, the City's total indebtedness grew to its current level of about \$300 million. I expect stable debt at that level for the next 6 years and beyond if this recommendation is accepted. This recommendation reflects the City's continuing need to invest adequately in its capital facilities.

Under the recommended six-year capital spending program, the City's long-term outstanding indebtedness will increase by \$23.0 million, or 8.1% between June 2004 and June 2010. The City's general obligation indebtedness will reach \$310 million by July 1, 2010.

### **B) Legal Debt Limitations**

The State of Connecticut imposes legal limits on the amount of debt that the City is authorized to issue. Under Connecticut General Statutes, municipalities are not permitted to incur indebtedness through the issuance of bonds that will cause aggregate indebtedness by class to exceed the following:

General Purposes:	2.25 times annual receipts from taxation
School Purposes:	4.50 times annual receipts from taxation
Sewer Purposes:	3.75 times annual receipts from taxation
Urban Renewal Purposes:	3.25 times annual receipts from taxation
Pension Obligation Bonds	3.00 times annual receipts from taxation
Total - All Purposes:	7.00 times annual receipts from taxation

Under these statutory limits, the City is permitted to incur indebtedness in excess of \$1.7 billion. From a practical standpoint, however, the City could never approach this level of indebtedness. If the City were to incur this magnitude of debt we would surely find our credit rating in the junk bond category and we would be saddled with annual debt service payments of \$150 million per year. For this reason, the legal debt limit in Connecticut is of no practical consequence for the City of Stamford.

**C) Impact of the Proposed Plan on Debt Position & Credit Rating**

Stamford is in elite company with a triple A bond rating—the highest available—from both major rating agencies. Only one hundred thirty-four (134) municipal issuers in the country carry a Aaa general obligation bond rating from Moody’s Investors Service, and only sixty-one (61) local governments carry a AAA rating from Standard & Poor’s.

The importance of maintaining Stamford’s triple-A rating is financial as well as symbolic. The table below compares the annual debt service costs of the proposed capital program at the current rating with the costs if Stamford were downgraded to double-A.

**Debt Service Costs of Proposed Capital Program at AA Rating compared to AAA Rating**

	FY06	FY07	FY08	FY09	FY10	Total
AA	3,353,037	6,443,379	9,545,353	12,633,116	15,702,721	47,677,605
AAA	3,304,737	6,352,921	9,414,789	12,464,816	15,499,053	47,036,316
difference	48,300	90,458	130,563	168,300	203,668	641,289

Note: This cost would increase until FY2024, when the additional cost would be \$483,000.

Based on 15 basis-point spread between AA and AAA borrowing costs.

In assigning credit ratings, the rating agencies analyze four broad rating factors in a community: Economic Factors (wealth levels, tax base, employment, regional economy, etc.); Financial Factors (operating results, financial reserves, contingent obligations, etc.); Administrative Factors (experience of the management team, financial management track record, etc.); and Debt Factors (debt as a % of full value, per capita debt, debt service as a % of budget, etc.) Both Moody’s and Standard & Poor’s have described Stamford’s debt position as moderate in their most recent ratings. Both agencies viewed the segregation of sewer-related borrowing into revenue-backed debt as positive to our debt position.

The City’s capital plan must recognize the importance of debt factors in the evaluation of the City’s credit by the rating agencies. Provided below is a comparison of

Stamford's ratios with selected cities in Connecticut and with selected other triple A cities in the country

### Debt Ratio Benchmarks

City	S&P Rating	Population	Per Capita Debt	Debt to FMV	DS as % of Expenditures	Undesignated FB as a % of Expenditures
Stamford (As of 12/01/03)	AAA	119,850	2,239	1.12%	8.36%	0.0%

\* The Charter of the City of Stamford prohibits the City from maintaining an undesignated fund balance

Connecticut Benchmarks - extracted from State of Connecticut, Office of Policy & Management, Fiscal Indicators Report, 1998-2002						
City	S&P Rating	Population	Per Capita Debt	Debt to FMV	DS as % of Expenditures	Undesignated FB as a % of Expenditures
Bridgeport	BBB+	140,104	4,585	12.0%	13.1%	7.9%
Hartford	A	124,558	1,305	2.8%	5.5%	5.0%
New Haven	A-	124,176	3,079	7.6%	9.1%	4.9%
Waterbury	BBB-	107,883	1,525	3.5%	3.4%	1.8%
Norwalk	AAA	84,127	1,657	11.3%	7.6%	5.6%
Danbury	AA	76,917	763	0.9%	4.7%	7.8%
Greenwich	AAA	61,784	653	0.2%	2.8%	2.6%
West Hartford	AAA	61,365	1,451	1.5%	7.6%	7.4%
Fairfield	AAA	57,715	1,733	9.6%	6.1%	5.4%
<b>Average</b>		<b>93,181</b>	<b>1,861</b>	<b>5.5%</b>	<b>6.7%</b>	<b>5.4%</b>

### National Benchmarks - Information provided by Webster Bank - Source: Annual Review of AAA Rated Municipalities, Standard & Poor's Rating Service, September 2003

City	S&P Rating	Population	Per Capita Debt	Debt to FMV	DS as % of Expenditures	Undesignated FB as a % of Expenditures
Alexandria, VA	AAA	128,283	1,319	1.2%	3.0%	34.0%
Cambridge, MA	AAA	101,355	705	0.4%	4.0%	11.0%
Charlotte, NC	AAA	604,676	2,679	2.7%	23.0%	16.0%
Greensboro, NC	AAA	223,891	1,120	1.5%	9.0%	23.0%
Irving, TX	AAA	194,407	4,942	6.6%	12.0%	16.0%
Minneapolis, MN	AAA	382,618	2,701	4.0%	24.0%	7.8%
Naperville, IL	AAA	128,358	2,922	3.1%	9.0%	32.0%
Omaha, NE	AAA	390,007	1,984	4.1%	22.0%	5.0%
<b>Average</b>		<b>239,288</b>	<b>2,041</b>	<b>2.6%</b>	<b>11.8%</b>	<b>16.1%</b>

While Stamford's per capita debt is above the average for medium sized cities in the State of Connecticut, it is lower than a number of the AAA-rated national benchmarks. It should also be noted that Stamford's population is lower than the average population of the other AAA rated communities. As noted in Exhibit A, the recommended capital plan will cause Stamford's per capita debt to increase to just \$2,502 by FY 2009-10, above the average for the national triple A benchmarks this year. However, wealth levels that are significantly higher than the state and national averages mitigate Stamford's per capita debt levels. Additionally, Stamford's per capita income of \$34,987 is 22% higher than the \$28,766 level for the State of Connecticut. All of these benchmarks are a reflection of Stamford's unique characteristics as an important

regional business center with a relatively small population, above average wealth levels, and high property values.

The single most important debt ratio for rating agencies is debt as a percentage of full market value of all taxable property in the municipality. By this measure, Stamford compares very well. The City's large and diverse tax base results in an extremely favorable 1.12% ratio. This is significantly lower than the average of 2.6% for the AAA rated cities illustrated in the chart. Over the life of the recommended capital plan, this ratio is expected to remain relatively constant, in the range of 1.2 percent. Projected changes in this ratio are outlined in Exhibit A. Although no one single ratio determines a credit rating, the City should seek to maintain this ratio at this level.

The third ratio listed above is debt service as a percent of expenditures. The City is currently slightly below 10%, and the recommended capital plan projects this to peak at approximately 10.22%. Ratios between 5 - 10% are generally considered moderate and anything over 15% is considered high. Although Stamford's ratios are in the high end of the moderate range, they are lower than a number of the other individual triple A-rated cities including Charlotte, NC (23.0%), Irving, TX (12.0%) and Minneapolis, MN (24.0%). Stamford should seek to keep this ratio at or near the 10% range. Projected debt service as a percent of budget for the next six years is outlined in Exhibit B.

The final ratio noted above is undesignated fund balance (accumulated surplus) as a percent of operating expenses. Although this is not a debt ratio, it is a critical financial measure that the rating agencies use to gauge the ability of a municipality to deal with unexpected financial emergencies and unfavorable operating events (natural disasters, economic slowdowns, etc). The City Charter in Stamford does not permit the City to maintain an undesignated fund balance, and this prohibition is a perennial concern of rating analysts. In general, the rating agencies anticipate that triple A credits will maintain an undesignated fund balance in the range of 5-10% of annual operations, and many of our benchmarks have fund balances well in excess of this range. The Charter Revision Commission is considering changes to allow the maintenance of a reasonable operating reserve. I strongly recommend that the Commission, the Board of Representatives, and Stamford voters approve such changes in the coming year.

#### **D. Impact of the Plan on Future Operating Budgets**

When approving capital spending plans it is important to realize that this spending results in a direct impact on the City's future operating budgets and tax rates. Not only must future taxpayers fund the original appropriation, but also it must be repaid with interest. The recommended plan will result in the City's annual debt service payable from the City's general fund increasing from approximately \$28.0 million in FY 2003-04 to \$41.5 million in FY 2009-10 (the level is lower in the current year because of the impact of two refundings in the last 9 months.) Based on the City's current grand list, and taking a conservative approach that assumes modest future growth of 0.5% per year and interest rates rising from 5% to 6% between 2004-05 and 2008-09, this \$13.5 million increase equates to approximately 1 mill over 6 years. Note that these interest rate assumptions are sharply more conservative than in prior reports, which had assumed level interest rates at 5% over 6 years.

## **E. Authorized But Unissued Debt**

The City currently has approximately \$126.2 million of Authorized but Unissued Debt (prior capital authorizations which have not yet been financed). We anticipate that approximately \$44.6 million of this amount will ultimately need to be bonded by the City, with the remaining portion funded through various grants. We project that the City will spend most of this authorization in the next twenty-four (24) months. Our plan assumes permanent financing of these appropriations in the fall of 2004 and 2005.

## **F. Projected Drawdown Schedule and Financing Strategy**

Determining the likely drawdown schedule for any new authorizations plays a significant role in the development of a financing strategy, and ultimately determines when the City budget will be affected by new capital projects. For analysis purposes, we have made some general assumptions concerning the speed with which new authorizations will be expended. We have assumed that the City will require 70% of the locally-financed portion within one year of authorization, an additional 20% within two years of authorization, and the final 10% within three years of authorization.

Exhibit C presents a Proposed Financing Schedule for both the Authorized But Unissued Debt, and the proposed new debt contained in the recommended capital plan. The financing plan is consistent with the anticipated drawdown schedules. The plan makes use of level principal serial bonds issued with a twenty (20) year maturity.

**Grant-Funded Projects-** It is obviously preferable for the City to finance needed capital projects from grants, when grant funding is available for this purpose. Projects, which are funded from grants or from current revenue generally, should not be counted when considering the funding recommendations contained in this report. Many major school construction projects are eligible for a school building subsidy in the range of 25%. The state-financed portion of these projects is excluded from the City's safe debt limit calculation.

**Pay-as-you-go Financing** - Financing a portion of the City's capital projects with current revenue is a financially prudent and conservative financing practice. Most triple A credits finance at least a portion of their capital plan through a pay-as-you-go mechanism. Any significant expansion in the size of the City's gross capital budget would certainly require that a major commitment be made to the use of pay-as-you-go financing. By way of comparison, the City of Alexandria, VA (one of our triple A benchmarks) has a six-year capital plan which is roughly the same size as Stamford's. In FY 2001, the City of Alexandria's general fund contributed \$21.9 million toward its capital program. Although adding a significant pay-as-you-go financing component in Stamford's FY 2004-05 operating budget is not likely to be possible, it would be highly desirable to direct some portion of future operating surpluses to support the City's capital financing needs.

## **Short Term Debt**

The projects included in the City's capital program over time include items with various useful lives, while debt is issued over twenty-year terms. On average, the lives of the assets and the duration of the debt are relatively well matched, but for some items the life may be significantly shorter than 20 years. At the same time, the interest rates required to support short-term debt are considerably lower than long-term rates. It may be advantageous to bifurcate the capital program in the future to include a separate financing method for those capital assets with useful lives of ten years or less, such as fire apparatus and other specialty vehicles, revaluations, and capital equipment. Some items, such as police vehicles that are now funded out of the operating budget would be appropriately financed through a short-term debt program.

The impact of such a change on the City's Safe Debt Limit would be positive. There would be no long-term budget impact to acquiring new short-term debt, while the pressure on the long-term capital program will be minimized. Because of the lower interest costs, and the shorter duration, it will be possible to increase the overall level of indebtedness without materially changing the impact on the General Fund.

### CONCLUSION

I hope that the observations made in this report are helpful to the various bodies responsible for the approval of the City's capital budget and six year capital plan. The recommended funding level of \$192.0 million over the next six years is a conservative plan that balances the City's significant capital needs within our financial capability to assume new debt. While this plan will increase the City's outstanding indebtedness modestly and will result in an additional debt service burden, I believe the City can accommodate this additional debt without jeopardizing its financial position or excellent credit rating.

Respectfully Submitted,



Benjamin Barnes  
Director of Administration

TOTAL PROJECTED GENERAL OBLIGATION DEBT

FY 2003-04 THROUGH 2009-10

Description	FY 2003-04	FY 2004-05	FY 2005-06	FY 2006-07	FY 2007-08	FY 2008-09	FY 2009-10
Debt: Beginning of FY*	268,380,686	284,566,456	293,464,109	298,373,844	302,341,914	305,747,726	307,586,214
Plus: Debt Issued 11/1/03	35,000,000						
Less: <u>Amortization - Existing Debt</u>							
Long Term Bonded Debt	(18,480,000)	(22,965,000)	(22,855,000)	(22,425,000)	(21,405,000)	(21,390,000)	(21,380,000)
Clean Water Fund Debt (GO)	(334,230)	(337,347)	(340,528)	(343,772)	(347,083)	(350,459)	(350,459)
Plus: <u>Proposed New Debt</u>							
Long Term Debt	0	32,200,000	29,800,000	30,000,000	30,000,000	30,000,000	30,000,000
Less: <u>Amortization - Proposed Debt</u>							
Long Term Debt	0	0	(1,694,737)	(3,263,158)	(4,842,105)	(6,421,053)	(5,610,000)
Projected Debt: End of FY	<u>284,566,456</u>	<u>293,464,109</u>	<u>298,373,844</u>	<u>302,341,914</u>	<u>305,747,726</u>	<u>307,586,214</u>	<u>310,245,755</u>
Projected Per Capita Debt	2,239	2,399	2,445	2,469	2,487	2,496	2,502
Debt as a % of Fair Market Value	1.12%	1.17%	1.18%	1.18%	1.17%	1.16%	1.14%

\* Includes outstanding GO bonded debt for schools, public improvements, and for sewers (\$18.3 million financed prior to 2003), plus \$5.1 million in Permanent Loan Obligations to the State Clean Water Fund which rely on a GO pledge.

NOTES:

1. FY02-03 population estimated at 117,083. Population assumed to increase 1/2 of 1% per year.
2. FMV estimated at \$23.9 billion in FY03-04. FMV assumed to increase at 2% annually.

**PROJECTED ANNUAL GENERAL OBLIGATION DEBT SERVICE PAYMENTS**

FY 2003-04 THROUGH FY 2009-10

	<u>FY 2003-04</u>	<u>FY 2004-05</u>	<u>FY 2005-06</u>	<u>FY 2006-07</u>	<u>FY 2007-08</u>	<u>FY 2008-09</u>	<u>FY 2009-10</u>
<u>Debt Service Payments</u>							
Current GO Bond Debt Service	31,063,492	37,295,591	35,473,165	34,006,153	31,953,681	30,878,034	29,799,503
Clean Water Fund Obligations (GO)	436,006	432,410	428,815	425,219	421,624	418,028	413,447
Proposed Capital Program	0	0	3,304,737	6,352,921	9,414,789	12,464,816	15,499,053
<b>Subtotal - Long Term Debt Service</b>	<u>31,499,498</u>	<u>37,728,001</u>	<u>39,206,717</u>	<u>40,784,293</u>	<u>41,790,094</u>	<u>43,760,878</u>	<u>45,712,002</u>
Subtotal - Short Term Debt Service	<u>322,292</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
<b>TOTAL DEBT SERVICE</b>	<u>31,821,790</u>	<u>37,728,001</u>	<u>39,206,717</u>	<u>40,784,293</u>	<u>41,790,094</u>	<u>43,760,878</u>	<u>45,712,002</u>
Debt Service Allocated to Other Funds	3,794,531	3,622,464	3,759,720	3,970,227	3,969,803	4,182,240	4,169,880
Net Debt Service to General Fund	<u>\$28,027,259</u>	<u>\$34,105,537</u>	<u>\$35,446,997</u>	<u>\$36,814,066</u>	<u>\$37,820,291</u>	<u>\$39,578,637</u>	<u>\$41,542,122</u>
Net Debt Service as % of General Fund Expenditures	8.48%	9.97%	10.01%	10.05%	9.97%	10.08%	10.22%

**NOTES:**

1. FY03-04 expenditures based on budget; assumed to increase at 3.5% per year.
2. Assumes level principal option and interest rates rising from 5% to 6% in 2008-09

**CITY OF STAMFORD  
PROPOSED FINANCING SCHEDULE**

DESCRIPTION	FY 2003-04	FY 2004-05	FY 2005-06	FY 2006-07	FY 2007-08	FY 2008-09	FY 2009-10
Recommended Capital Budget	28,000,000	30,000,000	30,000,000	30,000,000	30,000,000	30,000,000	208,000,000
<u>Authorized But Unissued Debt:</u>							
BONDS - 10/2003, 10/2004, 10/2005	35,000,000	5,600,000	2,800,000				
<u>Proposed Capital Program:</u>							
BONDS - 10/2004		26,600,000					
BONDS - 10/2005			29,800,000				
BONDS - 10/2006				30,000,000			
BONDS - 10/2007					30,000,000		
BONDS - 10/2008						30,000,000	
BONDS - 10/2009							30,000,000
<b>TOTAL BONDS BY FISCAL YEAR</b>	<b>35,000,000</b>	<b>32,200,000</b>	<b>29,800,000</b>	<b>30,000,000</b>	<b>30,000,000</b>	<b>30,000,000</b>	<b>30,000,000</b>

Note: Schedule assumes steady project financing requirements. If these requirements fluctuate, or if favorable market conditions arise, the City may opt to issue Bond Anticipation Notes in advance of bond issues, or in order to postpone bond issues. The City Charter limits BANs to one year maturity.