

# Indianapolis, Indiana

## New Issue Report

### Ratings

Long-Term Issuer Default Rating AAA

### New Issues

\$610,495,000 Indianapolis-Marion County Building Authority (the Building Authority) Community Justice Campus Lease Rental Revenue Bonds, Series 2019A

AAA

\$12,570,000 Indianapolis-Marion County Building Authority (the Building Authority) Community Justice Campus Lease Rental Revenue Bonds, Series 2019B

AAA

### Outstanding Debt

Indianapolis Local Public Improvement Bond Bank (IN) Taxable Bond Bank Refunding Bonds

AAA

### Rating Outlook

Stable

### New Issue Summary

**Sale Date:** April 4, 2019.

**Series:** \$610,495,000 Indianapolis-Marion County Building Authority (the Building Authority) Community Justice Campus Lease Rental Revenue Bonds, Series 2019A; \$12,600,000 Indianapolis-Marion County Building Authority (the Building Authority) Community Justice Campus Lease Rental Revenue Bonds, Series 2019B.

**Purpose:** Series 2019A: to fund a consolidated county detention center to replace existing correctional facilities and a county courthouse that combines civil, criminal, juvenile and probate courts in one building (and capitalized interest through April 1, 2022).

Series 2019B: to fund an assessment and intervention center to serve as a facility for providing temporary shelter, case assessment and treatment referral services (and capitalized interest through Jan. 15, 2020).

**Security:** Limited obligation of the Indianapolis Local Public Improvement Bond Bank. The series 2019A lease rental payments are payable from an irrevocable pledge of the city/county local income tax revenues. The series 2019B lease rental payments are payable from an irrevocable pledge of ad valorem property tax levied on all taxable property within the county.

### Analytical Conclusion

The 'AAA' rating on the series 2019A lease rental revenue bonds reflects the solid pledged income tax revenue growth prospects driven by the expanding local economy, including positive growth trends in population, employment and personal income. The dedicated tax revenue structure provides ample financial resilience in the event of a moderate economic downturn and incorporates strong legal protections to mitigate abatement risks.

The 'AAA' rating on the series 2019B lease revenue bonds, payable from ad valorem property taxes, reflects Indianapolis' strong underlying credit strength. The city maintains substantial independent revenue-raising ability, solid expenditure flexibility, a low long-term liability burden and the highest level of financial resilience. The city/county plans to capitalize interest on the bonds through the projected construction completion date. Additionally, the city/county will maintain two years of rental interruption insurance to mitigate abatement risks post completion.

**Economic Resource Base:** Indianapolis is the largest city in the state of Indiana, with a diverse economy bolstered by its role as the state capital. The estimated 2017 population of 863,002 reflects a 5% increase since the 2010 census. The city is home to numerous industries including pharmaceuticals, health services, logistics, manufacturing and other professional services. Major taxpayers include Eli Lilly and Company, Federal Express and American United Life Insurance Company. The largest employers, Health Services Indiana University Health, St Vincent Hospital and Eli Lilly Company, employ approximately 23,000, 17,000 and 11,000, respectively.

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**Rating History (IDR)**

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	2/11/19
AAA	Review - No Action	Stable	12/15/17
AAA	Revised	Stable	4/30/10
AA+	Downgraded	Stable	8/13/09
AAA	Affirmed	Stable	1/19/05
AAA	Assigned	—	4/19/89

**Key Rating Drivers**

**Revenue Framework: 'aaa'**

Indianapolis' revenue growth is expected to remain above the rate of inflation, as it has historically, based on ongoing expansion in the local economy. The city has significant ability to increase local income taxes to ensure ongoing fiscal stability.

**Expenditure Framework: 'aa'**

Fitch believes that the city's natural rate of expenditure growth will be above revenue growth based on spending demands for employee salary and benefits. The city has solid capacity to cut spending if necessary, due to moderate carrying costs for debt service and pension obligations and a labor environment that provides flexibility to management.

**Long-Term Liability Burden: 'aaa'**

The city's long-term liability burden, including pension liabilities and overall debt, is low relative to personal income.

**Operating Performance: 'aaa'**

The city has exceptionally strong gap-closing capacity and solid general fund reserves to manage through a moderate economic downturn. Fitch expects the city to maintain the highest financial resilience through downturns.

**Rating Sensitivities**

**Strong Operating Performance:** The 'AAA' GO ratings are sensitive to the city's continued willingness to maintain strong financial flexibility. While not anticipated, sharp declines in reserves could potentially pressure the current rating.

**Pledged Income Tax Revenue Declines:** The 'AAA' rating on the series 2019A bonds is sensitive to large and sustained pledged revenue declines, beyond the range of historical experience and Fitch's expectations. Significant declines could pressure the revenue bond rating.

**Credit Profile**

The city's net taxable assessed valuation (NAV) has steadily improved over the past several years, after limited growth from 2008 through 2014. There was a 6% cumulative increase in NAV in 2018 and 2019, due in large part to residential and commercial development. The city reports ongoing mixed-use developments, including the Waterside District development that includes plans for 1,350 new residential units, 629 hotel rooms and significant office and retail space along the White River. The downtown area is expected to benefit from redevelopment projects that will convert the former Coca Cola bottling plant and the historic AT&T Building to mixed-use developments.

The city's unemployment rate has been trending below the U.S. rate since 2015, and continued job growth is likely given the expansion of the technology sector within the local economy. Salesforce, Inc. currently has 1,400 employees, and plans to add 800 new jobs to its workforce by 2021. In 2018, Infosys Tech Hub (an IT company) announced plans for a \$245 million expansion at the site of the former Indianapolis International Airport, which is anticipated to create 3,000 new jobs in the next three years. Additionally, Fed Ex is in the midst of a \$1.5 billion expansion at the Indianapolis airport, which will add 20 new commercial gates by 2023.

**Related Research**

[Fitch Rates \\$623MM Indianapolis Local PIB Bond Bank, IN Lease Revenue Bonds 'AAA'; Outlook Stable \(March 2019\)](#)

**Related Criteria**

[U.S. Public Finance Tax-Supported Rating Criteria \(April 2018\)](#)

## Revenue Framework

A majority of the city's general fund revenues are derived from local sources including property and income taxes, which accounted for approximately 63% of total general fund revenue in 2017. Intergovernmental revenue accounted for approximately 19% of general fund revenue, followed by charges for services at almost 12%.

Fitch believes that natural revenue growth will continue to perform above the rate of inflation, as it has historically. The city has seen growth in the property tax levy as a result of NAV increases in recent years after limited growth due to recessionary pressures, coupled with the implementation of a state tax cap. The "circuit breaker" tax cap limits property tax rates to a percentage of gross assessed value depending on the property classification. The rates for homestead properties are capped at 1%; rates for residential properties that are not homesteads, agricultural property or nursing homes are capped at 2%; and commercial, industrial and personal property rates are capped at 3%. All residential properties accounted for 44% of 2017 total NAV, and commercial, industrial and personal properties accounted for 54%.

Ongoing income tax revenue gains reflect economic growth attributable to the uptick in employment and personal income. Estimated revenue growth for 2018 was approximately 3%, and Fitch anticipates natural tax revenue growth will continue to exceed the rate of inflation based on the trend of steady population growth and ongoing economic development.

Fitch views the city's ability to independently increase revenue as significant. The city-county council has the ability to increase local income tax rates to a maximum rate of 2.75% from the current 1.97%. Local income tax increases can be imposed by the County Income Tax Council (CITC), where the city-county council has over 90% of the voting representation.

## Expenditure Framework

The largest portion of the city's general fund expenditures is dedicated to public safety, including criminal justice, police and fire service. The remaining expenditures are for public works, culture and recreation and capital expenditures.

Fitch expects the natural pace of expenditure growth to exceed revenue growth absent policy action. The city's growth in expenditures is largely driven by employee salary and benefit costs, which account for approximately 60% of general fund expenditures. The average increase in employee salaries and benefits has grown at a pace above inflation, and Fitch expects this trend to continue.

Despite wage and benefit pressures, Fitch believes the city's flexibility of main expenditure items is solid. Management continues to curtail spending pressures by managing the size of the workforce, mainly through employee attrition and by carefully managing service contracts. Union agreements are not subject to binding arbitration, and management has strong control over staffing levels. By state statute, the city controller has the flexibility to reduce an agency budget if revenues are less than budgeted expenditures; the controller reportedly rarely needs to use this power.

Carrying costs for debt service, annual pension costs (excluding state reimbursements for pre-1977 pension plans) and other post-employment benefits (OPEB) contributions accounted for 17% of governmental expenditures in 2017. Since 2009, the state has reimbursed the city for the annual pension payments for the pre-1977 police and fire pension plans. Capital projects funded within the general fund provide additional expenditure flexibility, because the city can

delay projects for budgetary relief (as was done during the last recession). In 2017, the city used \$21 million, or 3% of general fund expenditures, on capital projects.

### Long-Term Liability Burden

The city's long-term liabilities are low with the combined net pension liability and overall debt at about 6% of personal income. The majority of the long-term liability burden is direct debt. The city's future borrowing plans include \$90 million in revenue bonds for road projects, to be issued in phases through 2020; these bonds are payable from county motor vehicle excise surtaxes, county wheel taxes and gasoline taxes. Fitch expects the direct debt burden to increase but remain relatively low compared to the city's economic resource base given its growing economy.

The city participates in four separate pension plans: two pre-1977 police and firefighter pension plans, the 1977 Police and Firefighters Statutory plan (statutory) for employees hired after April 1977 and the Indiana Public Employees Retirement Fund (PERF), which covers all other employees. As of Jan. 1, 2017, the city changed the PERF plan from a defined benefit plan to a defined contribution plan for all new civilian employees to minimize future growth in the net pension liability over time.

In 2009, the state began reimbursing the city's annual pension contributions for its pre-1977 plan to help offset the future liability. Despite this reimbursement, the pre-1977 pension plans' net pension liabilities are reported on the city's statement of net assets and included in Fitch's long-term liability burden assessment. The total net assets to accrued total pension liabilities ratio for all four plans combined was approximately 58% as of June 30, 2017, using an adjusted 6% rate of return assumption.

The net other post-employment benefits (OPEB) liability as of Dec. 31, 2017 was \$204 million, or 0.5% of personal income. The city funds OPEB on a pay-as-you-go basis.

### Operating Performance

The city's financial resilience is strong, given ample available general fund reserves, solid ability to independently increase revenues and solid expenditure flexibility. For details, see Scenario Analysis, page 6.

The city has strong financial policies and has made consistent efforts to maintain healthy financial operations. For example, management increased local income taxes to offset property tax losses in the city's operating funds following the Great Recession. Additionally, the city actively manages expenditure pressures through a variety of measures that include outsourcing services, renegotiating existing service contracts and eliminating positions through attrition. General fund results were strong in 2016 and 2017, and resulted in healthy general fund surpluses. The unrestricted general fund balance was \$178 million at year-end 2017, almost 28% of general fund expenditures and well above the 17% available fund balance policy target.

The city reports strong revenue collections for 2018, and the 2019 budget assumes that local tax revenue growth will increase 6% on a budgetary basis due to improved economic conditions within the tax base. The 2019 budget is balanced without the use of general fund reserves to fund operations. Fitch expects the city's financial operations to remain strong given its strong inherent budgetary flexibility, ample available reserves and formalized fund balance policy.

***Dedicated Tax Key Rating Drivers***

Fitch believes that the series 2019A bonds' pledged income tax revenue growth prospects will remain solid based on the ongoing expansion in the local tax base. Pledged revenues provide ample financial cushion in the event of a moderate economic downturn, and the bonds have strong legal and structural protections.

***Dedicated Tax Credit Profile***

The 2019A bonds are payable from local income tax (LIT) that consists of three components: the county option income tax (COIT), which can be used for any lawful purpose, a public safety income tax (PSIT) authorized for public safety and a local option income tax for levy freeze (LOIT), which is used to replace property tax levy growth. The current LIT rate is 1.9718%, and the maximum allowable is 2.75%. If the rate is at the maximum allowable rate, it would generate an additional \$133 million. The city/county maintains the independent legal ability to increase the tax rate, given that the city/county council holds over 90% voting representation.

The LIT collection process gives the city/county ample time to make budget adjustments in the event of revenue declines. The state provides a certified distribution, based on collections from two years prior, by October for the following calendar year. The state collects the income tax revenue on behalf of each county and holds the revenue in individual trust accounts, which are transferred monthly based on the state's certified distribution. The state maintains a balance of the certified distribution in the trust account for each year and, when the balance exceeds 15%, makes supplemental distributions based on the balance from two years prior. In the event of overpayment in any given year, the state may reduce the certified distribution in the following years to recover the shortfall.

The lease carries an unconditional obligation for the city/county to pay rent as long as the facility is available for use and occupancy. To mitigate the risk of construction delays, the city/county plans to use bond proceeds to capitalize interest for six months beyond the projected completion date. The legal protections also include a debt service reserve fund (DSRF) requirement at the maximum annual debt service (MADS; approximately \$38.6 million), funded with bond proceeds and a revenue stabilization fund (RSF) funded at three months of MADS (approximately \$9.6 million). If drawn upon, both the DSRF and RSF feature a replenishment mechanism to be maintained through the life of the bonds during non-abatement periods.

Additionally, the city and county community justice campus fund (CJC) and the lifecycle reserve fund will provide additional liquidity, subject to appropriation. The CJC's current balance is approximately \$12 million but expected to grow to an estimated \$43 million by 2021, and the lifecycle reserve is expected to be \$15.5 million by 2024. To counter abatement risks post-completion, the city/county maintains two years of rental interruption insurance.

***Revenue Stream Sensitivity***

Fitch believes that the pledged income tax revenues provide the highest level of financial resilience in a moderate economic downturn. To evaluate the sensitivity of the dedicated revenue stream to cyclical declines, Fitch considers both revenue sensitivity results (using a 1% decline in national GDP scenario) and the largest decline in revenues over the period covered by the revenue sensitivity analysis. Fitch's analysis focuses on maximum leverage at the 3.0x ABT, although the city/county council does not have plans to issue additional parity debt at this time. The scenario indicates a potential 6.7% revenue decline under a moderate

economic downturn. The largest actual peak to trough decline was 20.6%; however, Fitch believes the revenue volatility is overstated due to the certified distribution process that provides supplemental distributions in some years.

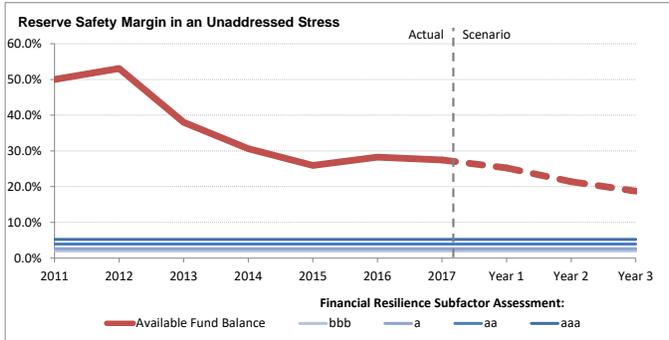
In 2019, the state certified approximately \$336 million in LIT, which provides over 8.7x coverage of MADS; this cushion could withstand an 88% decline and still provide 1.0x coverage of MADS. Assuming debt issuance up to the 3.0x ABT, the revenue stream can withstand a 67% decline while still maintaining sum sufficient coverage of MADS. This is equivalent to almost 10.0x the scenario result and more than 3.0x the worst actual decline in pledged LIT revenues. The city/county does not currently plan to issue additional debt under this structure.

### **Dedicated Revenue Stream Details**

Fitch believes that the city/county LIT revenue growth prospects will remain solid, based on the trend of steady population growth and ongoing economic development. The city/county portion of the state-certified LIT revenues increased 3% and 6% for 2018 and 2019, respectively. Given the ongoing expansion in the local economy, Fitch anticipates that, absent policy action, natural revenue growth prospects will continue to exceed the rate of inflation based on current and historical trends.

Indianapolis (IN)

Scenario Analysis



Analyst Interpretation of Scenario Results:

The city's financial resilience is strong, given ample available general fund reserves, solid ability to independently increase revenues and solid expenditure flexibility. In June 2016, the city passed an ordinance to maintain the unrestricted general fund balance at 17% of general fund expenditures, which Fitch believes is consistent with the current rating level. General fund reserves have historically exceeded the 17% target despite the regular use of reserves for capital expenditures. Fitch anticipates that the city would continue to maintain reserve levels above the 'aaa' reserve safety margin in a moderate economic stress scenario.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(2.6%)	0.3%	3.2%
Inherent Budget Flexibility	Superior		

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2011	2012	2013	2014	2015	2016	2017	Year 1	Year 2	Year 3
Total Revenues	617,212	530,320	507,965	536,786	558,943	623,698	607,567	591,697	593,396	612,301
% Change in Revenues	-	(14.1%)	(4.2%)	5.7%	4.1%	11.6%	(2.6%)	(2.6%)	0.3%	3.2%
Total Expenditures	640,678	591,342	621,646	624,154	642,276	611,871	640,448	653,257	666,322	679,649
% Change in Expenditures	-	(7.7%)	5.1%	0.4%	2.9%	(4.7%)	4.7%	2.0%	2.0%	2.0%
Transfers In and Other Sources	27,897	43,303	51,577	36,498	68,815	55,809	60,379	58,802	58,971	60,849
Transfers Out and Other Uses	62,409	5,945	5,900	5,102	6,749	6,897	8,295	8,461	8,630	8,803
Net Transfers	(34,512)	37,358	45,677	31,396	62,066	48,912	52,084	50,341	50,341	52,047
Bond Proceeds and Other One-Time Uses	-	5,945	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	(57,978)	(23,664)	(68,004)	(55,972)	(21,267)	60,739	19,203	(11,219)	(22,586)	(15,301)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	(8.2%)	(4.0%)	(10.8%)	(8.9%)	(3.3%)	9.8%	3.0%	(1.7%)	(3.3%)	(2.2%)
Unrestricted/Unreserved Fund Balance (General Fund)	351,457	313,773	238,463	192,678	168,174	174,765	178,146	166,927	144,341	129,041
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	351,457	313,773	238,463	192,678	168,174	174,765	178,146	166,927	144,341	129,041
Combined Available Fund Bal. (% of Expend. and Transfers Out)	50.0%	53.1%	38.0%	30.6%	25.9%	28.2%	27.5%	25.2%	21.4%	18.7%
Reserve Safety Margins	Inherent Budget Flexibility									
	Minimal		Limited		Midrange		High		Superior	
Reserve Safety Margin (aaa)	41.8%		20.9%		13.1%		7.8%		5.2%	
Reserve Safety Margin (aa)	31.3%		15.7%		10.4%		6.5%		3.9%	
Reserve Safety Margin (a)	20.9%		10.4%		6.5%		3.9%		2.6%	
Reserve Safety Margin (bbb)	7.8%		5.2%		3.9%		2.6%		2.0%	

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

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