



HISTORIC  
**F R A N K L I N**  
T E N N E S S E E

# City of Franklin Credit Scorecard & Debt Management Policy

Prepared for the City of Franklin, TN  
March 10, 2016



Public Financial Management, Inc.  
530 Oak Court Drive  
Suite 160  
Memphis, TN 38117  
[www.pfm.com](http://www.pfm.com)

# Recap and Update

---

## Recap

- In September 2015, PFM presented to the Board of Mayor and Alderman (BOMA) the Moody's and Standard & Poor's local government criteria .
- In November 2015, PFM presented the City's indicative scorecard results to the BOMA.

## Update

- PFM has updated the City's indicative scorecard results based on the City's FY 2015 CAFR.
- With this information, we have proposed modifications/modernizations to the City's Debt Management Policy.

# Existing Debt Management Policy – Debt Affordability

The City's Debt Management Policy was adopted in June 2009 and addresses Debt Affordability in section V through the following ratios:

- *Debt Service as % of Operating Expenditures;*
- *Debt Per Capita; Per Capita Debt/Per Capita Income;*
- *Debt as % of Property Tax Base (Taxable or Market Value);*
- *Overall Debt as % of Property Tax Base (includes overlapping debt)*

Two of the metrics and the benchmarking used to set such metrics.

Debt Affordability Ratios	Benchmarks
<b>(I.) Total Budget Resources:</b>	
1. Debt Service as a Percent of Operating Expenditures – <i>Measures debt liability relative to total budget resources</i>	<b>Total GO Debt</b> <b>&lt; 12%</b> <b>Less Self-Supporting Debt</b> <b>&lt; 8%</b>
Supporting Data	S&P (04/08) cites < 8% as low, 8%-15% as moderate Moody's, 2008 AAA Cities, Population 50k-100k Median @ 8.97%
Brentwood @	11.40%
Germantown @	8.00%
<b>Franklin - Total GO Debt @</b>	<b>9.78%</b>
<b>Franklin - Less Self-Supporting @</b>	<b>4.77%</b>
Chattanooga @ [AA/AA+]	9.14%
Clarksville @ [Aa3]	17.05%
Murfreesboro @ [A1]	17.31%
Alpharetta, GA @	21.00%
Dublin, OH @	11.37%
Naperville, IL @	6.69%
<b>(II.) Wealth and Income of Community:</b>	
2. Direct Debt Per Capita – <i>Measures net debt to population</i>	<b>&lt; \$2,000</b>
Supporting Data	S&P (4/08) cites < \$1,000 as very low, \$1,000-\$2,000 as low and \$2,000-\$3,000 as moderate
Brentwood @	\$ 669.70
Germantown @	\$ 535.30
<b>Franklin - Total GO Debt @</b>	<b>\$ 1,442.88</b>
<b>Franklin - Less Self-Supporting @</b>	<b>\$ 799.01</b>
Chattanooga @ [AA/AA+]	\$ 566.84
Clarksville @ [Aa3]	\$ 383.30
Murfreesboro @ [A1]	\$ 1,865.21
Alpharetta, GA @	\$ 941.43
Dublin, OH @	\$ 999.90
Naperville, IL @	\$ 587.40



# Moody's Scorecard Results (as of June 30, 2015)

- The final scores for each metric are assigned a numerical value, and averaged according to their individual weighting.
- Franklin's overall indicated current rating is **Aa1**.
- The indicated rating is one component of Moody's overall rating process, and may not always be the final rating an entity receives due to qualitative "below the line" adjustments.

## Current Score Estimates

Category	Weight	Indicated Rating
Economy/Tax Base	30%	1.45
Fund Balance	15%	1.14
Cash Balance	15%	1.89
Management	20%	1.42
Direct Debt	10%	2.55
Pension Liability	10%	1.75
Indicated Rating Score	100%	1.60
<b>Indicated Rating</b>	<b>-</b>	<b>Aa1</b>

Indicated Rating	Overall Weighted Score	Indicated Rating	Overall Weighted Score
Aaa	0.5 to 1.5	Baa2	3.83 to 4.17
Aa1	1.5 to 1.83	Baa3	4.17 to 4.50
Aa2	1.83 to 2.17	Ba1	4.50 to 4.83
Aa3	2.17 to 2.5	Ba2	4.83 to 5.17
A1	2.50 to 2.83	Ba3	5.17 to 5.50
A2	2.83 to 3.17	B1	5.50 to 5.83
A3	3.17 to 3.5	B2	5.83 to 6.17
Baa1	3.50 to 3.83	B3	6.17 to 6.50

# Moody's Scorecard Results - Other Considerations

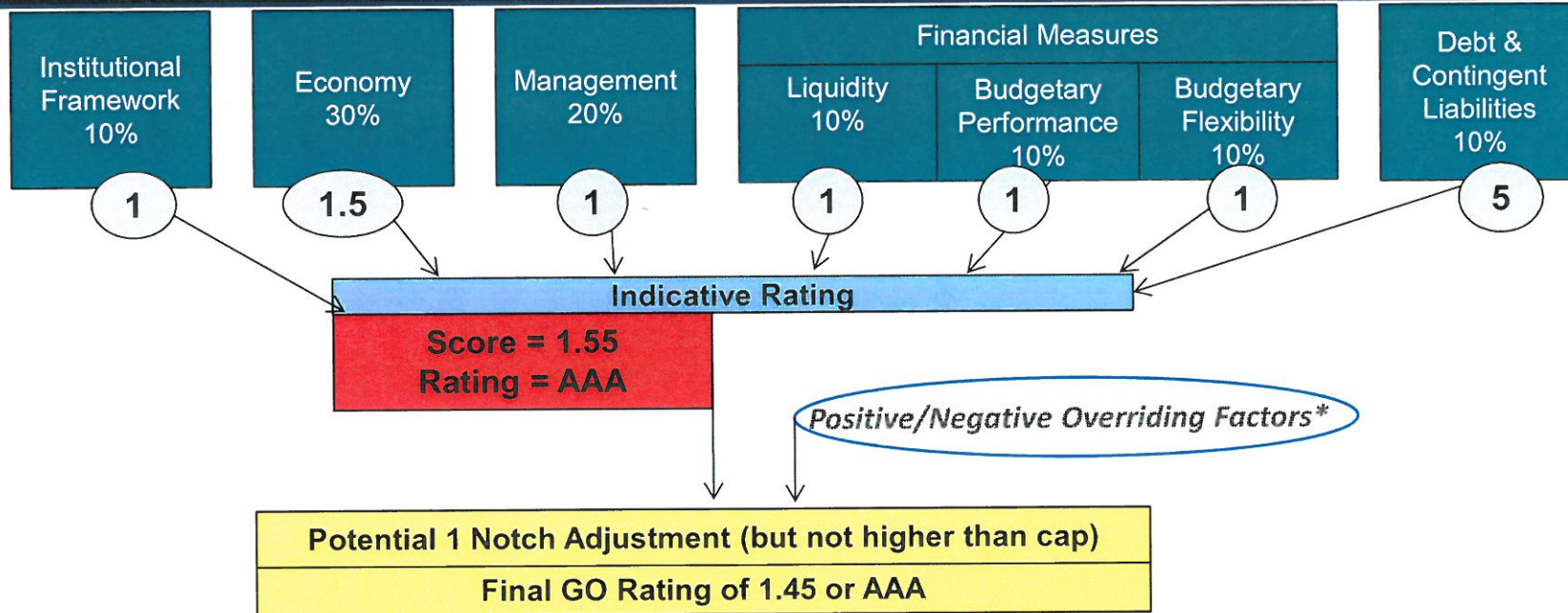
---

- A number of other factors do not appear on the scorecard or as a below-the-line adjustment, but are considered in our ratings and are frequent topics of discussion in our analysis\*.
  - Per capita income
  - Composition of workforce/employment opportunities
  - Proportion of tax base that is vacant or exempt from taxes
  - Median home value
  - Trend of real estate values
  - Population trends
  - Property tax appeals outstanding
  - Unusually significant tax base declines or growth

\*Other Considerations on page 11 of Moody's Rating Methodology: US Local Government General Obligation Debt



# S&P Indicative Score (as of June 30, 2015)



## Indicative Rating Outcomes Resulting From The Weighted Average Of Seven Factors

Factor Score Weighted Average	Indicative Rating
1.00 – 1.64	AAA
1.65 – 1.94	AA+
1.95 – 2.34	AA
2.35 – 2.84	AA-
2.85 – 3.24	A+
3.25 – 3.64	A
3.65 – 3.94	A-
3.95 – 4.24	BBB+
4.25 – 4.54	BBB
4.55 – 4.74	BBB-

\*The rating listed is approximate, and is subject to change based on incorporation of the overriding factors, qualitative considerations, and Standard and Poor's own interpretation of the methodology and its components. For more information on Positive/Negative Overriding Factors please see slide 14.

# Proposed Updates to the Debt Management Policy

---

- The scorecard concept should be used as a tool to understand the factors and weights that impact an issuer's credit rating.
- The City's current Debt Management Policy include several affordability metrics:
  1. Debt Service as % of Operating Expenditures
  2. Debt Per Capita
  3. Per Capita Debt/Per Capita Income
  4. Debt as % of Property Tax Base (Taxable or Market Value)
  5. Overall Debt as % of Property Tax Base (includes overlapping debt)
- Proposal for modernizing the Debt Management Policy based on the rating agencies criteria:
  1. Direct debt as a % of Full Value  $\leq 1.75\%$
  2. Direct debt of Operating Revenues of  $\leq 3.00X$
  3. Total Governmental Funds Debt Service as % of expenditures of  $\leq 25\%$
- Proposal to annually calculate the City's indicative ratings per Moody's and S&P's local government criteria
- Proposal to bi-annually review the City's indicative ratings along with peer cities

---

# Appendix



# Moody's Scorecard and Below-the-Line Adjustments

## **Economy/Tax Base (30% of total score):**

- Institutional presence (positive)
- Regional economic center (positive)
- Economic concentration (negative)
- Outsized unemployment or poverty levels (negative)

## **Finances (30% of total score):**

- Outsized enterprise of contingent liability risk (negative)
- Unusually volatile revenue structure (negative)

## **Management (20% of total score):**

- State oversight or support (positive or negative)
- Unusually strong or weak budget management and planning (positive or negative)

## **Debt/Pension (20% of total score):**

- Unusually strong or weak security features (positive or negative)
- Unusual risk posed by debt structure (negative)
- History of missed debt service payments (negative)

Scorecard Category	Weight
Economy/Tax Base	30%
Finances	30%
Management	20%
Debt/Pensions	20%

# Moody's Economy/Tax Base Score

- Franklin's score in the Economy/Tax Base Section is 1.45 (Aaa)
  - The tax base size of \$11.4B receives a rating of **Aa**.
  - The tax base per capita of \$161,642 receives a rating of **Aaa**.
  - The median family income as a percentage of the US Median of 157.31% receives a rating of **Aaa**.

Scorecard Category	Weight
Economy/Tax Base	30%
Finances	30%
Management	20%
Debt/Pensions	20%

Economy/Tax Base							
	Aaa	Aa	A	Baa	Ba	B and Below	Weight
Tax Base Size: Full Value	>\$12B	\$12B ≥ n > \$1.4B	\$1.4B ≥ n > \$240M	\$240M ≥ n > \$120M	\$120M ≥ n > \$60M	≤ \$60M	10%
Tax Base per Capita	>\$150,000	\$150,000 ≥ n > \$65,000	\$65,000 ≥ n > \$35,000	\$35,000 ≥ n > \$20,000	\$20,000 ≥ n > \$10,000	≤ \$10,000	10%
Median Family Income as a % of U.S. Median	>150% of US median	150% to 90% of US median	90% to 70% of US median	70% to 50% of US median	50% to 40% of US median	≤ 40% of US median	10%

# Moody's Finances Score

Scorecard Category	Weight
Economy/Tax Base	30%
Finances	30%
Management	20%
Debt/Pensions	20%

- Franklin's score in the Finances Section is 1.52 (Aa1)
  - The fund balance as a percentage of revenues of 56.20% receives a rating of **Aaa**.
  - The 5-year dollar change in fund balance as a percentage of revenues of 14.62% receives a rating of **Aa**.
  - The cash balance as a percentage of revenues of 33.16% receives a rating of **Aaa**.
  - The 5-year dollar change in cash balance as a percentage of revenues of -2.75% receives a rating of **Baa**.

Finances							
	Aaa	Aa	A	Baa	Ba	B and Below	Weight
Fund Balance as % of Revenues	>30.0%	30.0% ≥ n > 15.0%	15.0% ≥ n > 5.0%	5.0% ≥ n > 0.0%	0.0% ≥ n > -2.5%	≤ -2.5%	10%
5-Year Dollar Change in Fund Balance as % of Revenues	>25.0%	25.0% ≥ n > 10.0%	10.0% ≥ n > 0.0%	0.0% ≥ n > -10.0%	-10.0% ≥ n > -18.0%	≤ -18.0%	10%
Cash Balance as % of Revenues	>25.0%	25.0% ≥ n > 10.0%	10.0% ≥ n > 5.0%	5.0% ≥ n > 0.0%	0.0% ≥ n > -2.5%	≤ -2.5%	10%
5-Year Dollar Change in Cash Balance as % of Revenues	>25.0%	25.0% ≥ n > 10.0%	10.0% ≥ n > 0.0%	0.0% ≥ n > -10.0%	-10.0% ≥ n > -18.0%	≤ -18.0%	5%



# Moody's Management Score

- Franklin's score in the Management Section is 1.42 (Aaa)
  - The 5-year average of operating revenues of 1.04X of operating expenditures receives a rating of **Aa**.
  - The institutional framework score is **Aaa**.

Scorecard Category	Weight
Economy/Tax Base	30%
Finances	30%
Management	20%
Debt/Pensions	20%

Management							
	Aaa	Aa	A	Baa	Ba	B and Below	Weight
Institutional Framework	Very strong legal ability to match resources with spending	Strong legal ability to match resources with spending	Moderate legal ability to match resources with spending	Limited legal ability to match resources with spending	Poor legal ability to match resources with spending	Very poor legal ability to match resources with spending	10%
Operating History: 5-Year Average of Operating Revenues/ Operating Expenditures	>1.05x	1.05x ≥ n > 1.02x	1.02x ≥ n > 0.98x	0.98x ≥ n > 0.95x	0.95x ≥ n > 0.92x	≤ 0.92x	10%

# Moody's Debt/Pensions Score

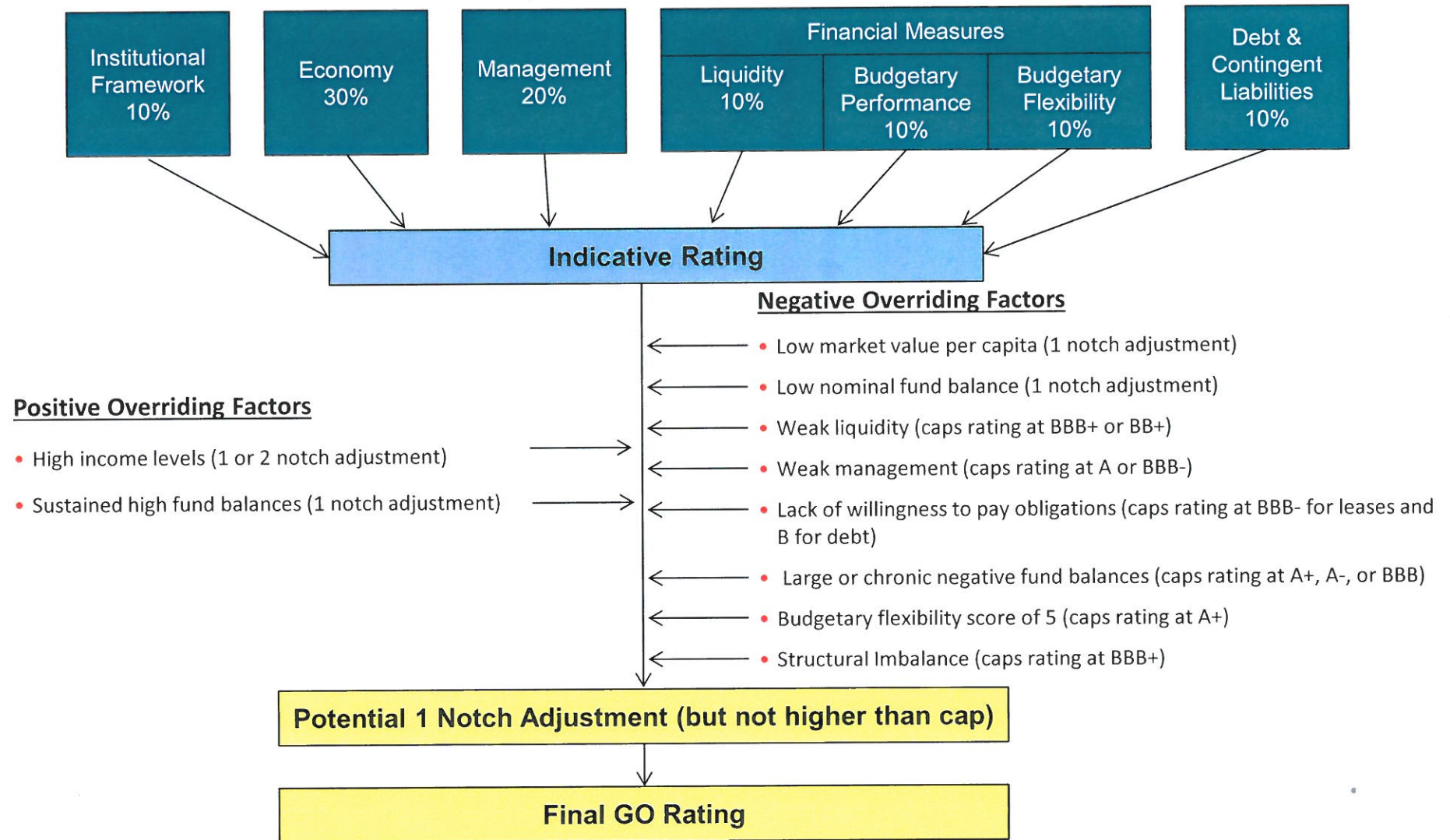
- Franklin's score in the Debt/Pensions Section is 2.15 (Aa2)
  - The net direct debt as a percentage of full value of 1.24% receives a rating of **Aa**.
  - The net direct debt 2.08x of operating revenues receives a rating of **A**.
  - The 3-year average of Moody's Adjusted Net Pension Liability as a percentage of full value of 0.47% receives a rating of **Aaa**.
  - The 3-year average of Moody's Adjusted Net Pension Liability of 0.79x of operating revenues receives a rating of **Aa**.

Scorecard Category	Weight
Economy/Tax Base	30%
Finances	30%
Management	20%
Debt/Pensions	20%

Debt/Pensions							
	Aaa	Aa	A	Baa	Ba	B and Below	Weight
Net Direct Debt/Full Value	<0.75%	0.75% ≤ n < 1.75%	1.75% ≤ n < 4.00%	4.00% ≤ n < 10.00%	10.00% ≤ n < 15.00%	≥ 15.00%	5%
Net Direct Debt/Operating Revenues	<0.33x	0.33x ≤ n < 0.67x	0.67x ≤ n < 3.00x	3.00x ≤ n < 5.00x	5.00x ≤ n < 7.00x	≥ 7.00x	5%
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value	<0.90%	0.90% ≤ n < 2.10%	2.10% ≤ n < 4.80%	4.80% ≤ n < 12.00%	12.00% ≤ n < 18.00%	≥ 18.00%	5%
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues	<0.40x	0.40x ≤ n < 0.80x	0.80x ≤ n < 3.60x	3.60x ≤ n < 6.00x	6.00x ≤ n < 8.40x	≥ 8.40x	5%



# S&P Analytical Framework & Overriding Factors



Source: S&P's U.S. Local Governments General Obligations Ratings: Methodology and Assumptions, September, 2013.



# S&P Institutional Framework (10%)

---

- Institutional Framework (Score: 1)
  - All Local Governments in Tennessee have the same score for this factor.
  - The full list of institutional framework scores for state and client type combinations was released by S&P on September 12, 2013.

Score Range	Institutional Framework Score
1 - 1.5	1 (Very Strong)
1.75 - 2.75	2 (Strong)
3 - 3.75	3 (Adequate)
4 - 4.5	4 (Weak)
4.75 - 5	5 (Very Weak)

# S&P Economy (30%)

- Economic Score (Score: 1.5)
  - Current market value per capita is \$161,642
  - Projected per capita effective buying income is 162.59% of the U.S.

	Market Value/ Capita				
Projected Per Capita EBI as % of US	>\$195,000	\$195,000-\$100,000	\$100,000-\$80,000	\$80,000-\$55,000	<\$55,000
> 150	1	1.5	2	2.5	3
110-150	1.5	2	2.5	3	3.5
85-110	2	2.5	3	3.5	4
70-85	2.5	3	3.5	4	4.5
<70	3	3.5	4	4.5	5

# S&P Management (20%)

- Management Score (Score: 1)

- Based on the most recent S&P report on the Franklin, TN dated March 23, 2015, S&P characterizes the financial management practices “strong” under its FMA methodology, which equates to a score of 1.

Rounded Score	Characteristics
1	FMA score of "Strong" and none of the factors in score 5 are present
2	FMA score of "Good" and none of the factors in score 5 are present
3	FMA score of "Standard" and none of the factors in score 5 are present
4	<ul style="list-style-type: none"> <li>• There is a financial reporting statement that has a material negative impact</li> <li>• Any of the conditions in score 5 existed in the past 3 years</li> <li>• The structural imbalance override condition exists or has existed within the past 3 years</li> <li>• Very high debt, pension, or OPEB burden</li> </ul>
5	<p>Regardless of FMA score, any of the following is present:</p> <ul style="list-style-type: none"> <li>• A Management team that lacks relevant skills resulting in a weak capacity for planning, monitoring, and management</li> <li>• An auditor has delivered a going concern opinion</li> <li>• The government has shown an unwillingness to support a debt or capital lease obligation</li> <li>• The government is actively considering bankruptcy in the near term</li> <li>• Any of the conditions in score 5 existed in the past 3 years</li> <li>• The structural imbalance override condition exists or has existed within the past 3 years</li> <li>• Very high debt, pension, or OPEB burden</li> </ul>



## S&P Budgetary Flexibility (10%)

- Financial Measures: Budgetary Flexibility Score (Score: 1)
  - Available Fund Balance to General Fund Expenditures ratio is  $\$38,219,753 / \$57,489,269 = 75.17\%$

	Available Fund Balance as a % of Expenditures				
%	>15	8-15	4-8	1-4	<1
Score	1	2	3	4	5

# S&P Budgetary Performance (10%)

- Financial Measures: Budgetary Performance Score (Score: 1)
  - Total governmental funds net result: net total governmental funds / governmental expenditures is ( $\$12,248,781 / \$79,599,702 = 15.39\%$ )
  - General Fund net result: General Fund Operating Balance / General Fund Expenditures (including transfers) is  $\$3,182,797 / \$50,843,243 = 6.26\%$

	Total Governmental Funds Net Result (%)				
General Fund Net Result (%)	>-1	-1 to -5	-5 to -10	-10 to -15	< -15
Limited (>5)	1	2	3	4	5
Balanced (-1 to 5)	2	2	3	4	5
Pressured (<-1)	3	2	3	4	5

# S&P Liquidity (10%)

- Financial Measures: Liquidity Score (Score: 1)
  - Total government cash / total governmental funds debt service is  $\$37,674,481 / \$12,244,986 = 307.67\%$
  - Total cash / total governmental funds expenditures is  $\$37,674,481 / \$79,599,702 = 47.33\%$

	Total Governmental Cash as % of Total Governmental Funds Debt Service				
Total Cash as a % of Total Governmental Funds Expenditures	>120	120-100	100-80	80-40	<40
>15	1	2	3	4	5
8-15	2	2	3	4	5
4-8	3	2	3	4	5
1-4	4	2	3	4	5
<1	5	2	3	4	5



# S&P Debt & Contingent Liability (10%)

- Debt and Contingent Liability (Score: 5)
  - Total governmental funds debt service / expenditures →  $\$12,244,986 / \$79,599,702 = 15.38\%$
  - Net direct debt / total governmental funds revenue →  $\$141,546,047 / \$91,848,483 = 154.11\%$

Total Governmental Funds DS as % of Total Governmental Funds Expenditures	Net Direct Debt as % of Total Governmental Funds Revenue				
	>30	30-60	60-120	120-180	>180
<8	1	2	3	4	5
8-15	2	3	4	4	5
15-25	3	4	5	5	5
25-35	4	4	5	5	5
>35	4	5	5	5	5

# Approach to Analysis

---

## DISCLAIMER FOR OVERVIEW OF MOODY'S INVESTORS SERVICE REVISED METHODOLOGY FOR LOCAL GOVERNMENT GENERAL OBLIGATION DEBT:

- The calculations included in this document are based on PFM's interpretation of Moody's revised methodology for U.S. local governments general obligation debt as detailed in the July 24th, 2014 Moody's Investors Service publication. Calculations and supporting data do not represent actual figures nor are they definitive representations of Moody's final calculations. Calculations do not include the application of Moody's qualitative considerations or below-the-line adjustments. Calculations are subject to change based on changes to the underlying data. Results are estimates only and should not be used for actual reporting or assumptions regarding Moody's calculations. Resultant figures are not confirmed by Moody's and are indicative interpretations only.

## DISCLAIMER FOR OVERVIEW OF STANDARD AND POOR'S PROPOSED CHANGES TO LOCAL GOVERNMENT RATINGS METHODOLOGY:

- The calculations included in this document are based on PFM's interpretation of Standard and Poor's adjustments to U.S. local governments general obligation bond rating methodology as detailed in the September 12, 2013 Standard and Poor's publication. Calculations and supporting data do not represent actual figures nor are they definitive representations of Standard and Poor's final calculations. Calculations do not include the application of Standard and Poor's qualitative considerations or overriding factors. Calculations are subject to change based on changes to the underlying data. Results are estimates only and should not be used for actual reporting or assumptions regarding Standard and Poor's calculations. Resultant figures are not confirmed by Standard and Poor's and are indicative interpretations only.