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ASK ELi: City's AAA Rating? [1]

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Above: East Lansing's Finance Director, Mary Haskell (courtesy City of East Lansing)

An ELi reader wrote to ask:

One city council candidate keeps referring to East Lansing as having achieved a triple A financial rating This has caused us to ponder a number of related questions.

- *What does AAA actually mean? What does it allow East Lansing to do? What could E.L. not do if it lacked this rating?*
- *Is this a bond rating or does it refer to a more general status? (I have heard it referred to as both.)*
- *When did East Lansing achieve this rating? Is there anything new about it? If so, when did we last have a lower rating, and what was it then?*

Thanks for the light you can shed on this subject.

What does the AAA rating mean, and who bestows it?

Private independent rating services issue ratings of cities. The ratings are essentially a credit rating of the City; they indicate how likely the rating service thinks a city is to pay back the principal and interest on a bond on the schedule that is set out at the start. This is why this type of rating is sometimes called a ?bond rating.?

The better the rating, the lower the interest rate we get on our bonds, the less money we spend paying interest on debt.

There are three big ratings firms: Standard & Poor?s, Moody?s, and Fitch. According to Mary Haskell, the Finance Director for the City of East Lansing, the City of East Lansing has a AAA rating from Fitch; see documentation here [2]. Standard & Poor's has given the City of East Lansing a AA+ rating, which is one step below AAA.

The City is not rated by Moody?s; it is common to only have two of the big three ratings. Moreover, as Haskell points out, the City has to pay to be rated, and ?having all three agencies rate us would add unnecessary costs to the size of the bond issue.?

Bonds are used for various projects. Voters of East Lansing elected to do bonds to help fund the Hannah Community Center and the Family Aquatic Center, for example. Our Downtown Development Authority (DDA) also used bonds to buy properties along Evergreen Avenue that were intended to be used in the failed City Center II project. The City is ultimately responsible for paying back the principal and interest on all of these bonds, and if our rating were not so good, we would be paying more in interest.

When did East Lansing achieve its AAA and AA+ ratings?

The Fitch rating: According to Haskell, ?We obtained our AAA rating from Fitch on April 30, 2010. Before that we had a AA+. We had the AA+ since October 21, 2006 when we were upgraded from a AA.?

The Standard & Poor's rating: According to a press release we obtained, Standard & Poor's upgraded East Lansing from a AA to its current AA+ rating in the fall of 2006.

So, in 2006, both Fitch and Standard & Poor's upgraded the rating of the City of East Lansing. In 2010, Fitch further upgraded the City's rating.

Will our unfunded pension liability cause our credit rating to drop?

This is another question that has come up at City Council. National accounting standards are changing in a way that is about to make our large liability to retirees much more visible to people looking at our City?s financial status. Some have been concerned that this might negatively affect our bond rating?something that could then cost us more when the City goes to borrow money.

But the rating agencies have already been looking at that debt, so the accounting standards? change is unlikely to affect our bond rating.

Says Haskell: ?The rating agencies question us in great detail on many aspects of our financial condition, including our pension and OPEB [other post-employment benefits] liabilities, contributions and funding status. They have access to all of our CAFR's [comprehensive annual financial reports], budget documents, and valuation's which of course state the liabilities and funding status in detail. The rating analyst examines our written financial data and we have verbal conference calls to answer their many questions. The analyst then presents their examination conclusions to a committee to justify their rating proposal.?

Haskell adds, ?As far as the amount of the outstanding liability and the booking of the unfunded liability as part of new accounting rules for governments, the agencies have said, it should not impact the rating. Only time will tell if that is really the case.?

Further, ?Both Fitch and S&P are in the process of developing new analytic tools to assess financial health in a prospective manner. The implementation of the new methodology and the impact on current ratings is also unknown at this time."

Our thanks to CoEL Finance Director Mary Haskell for her assistance with answering this reader's question.

Have a question you want to ask ELi to investigate? Contact us? [3]

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