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Summary:

Oakland Redevelopment Agency, California; Tax Increment

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Summary:

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Credit Profile		
Oakland Redev Agy 2nd lien tax alloc bnds (RZEDBs) (Broadway/Macarthur/San Pablo Redev Proj)		
Long Term Rating	A-/Negative	Outlook Revised

Rationale

Standard & Poor's Ratings Services revised its outlook to negative from stable and affirmed its 'A+' long-term rating on the Oakland Redevelopment Agency (RDA), Calif.'s series 2006C and 2006C-T (MacArthur/Broadway/San Pablo project areas) tax allocation bonds (TABs). At the same time, Standard & Poor's also revised its outlook to negative and affirmed its 'A-' long-term rating on the agency's series 2010-T second-lien tax allocation revenue bonds (TARBs; MacArthur/Broadway/San Pablo Redevelopment Project). The outlook revision is based on our view of the multiple years of assessed value (AV) decline due to a large reassessment and the removal of a hospital off of the tax rolls, reducing coverage on both liens.

The rating reflects our view of the agency's:

- Recent two-year AV loss representing about 27%, or about $335 million, from fiscal 2013 and a reduction of maximum annual debt service (MADS) coverage for both the senior lien, to 2.48x, and the subordinate lien, to 1.71x as a result of the loss;
- The project area's concentrated taxpayer base, with the top 10 taxpayers accounting for 34% of incremental AV in fiscal 2015; and
- Moderate volatility ratio of 0.41.

Partly offsetting the above strengths, in our view, are the successor agency (SA)'s:

- Strong income indicators with projected 2018 per capita effective buying income of 120% of the national level and access to the Bay Area regional economy; and
- Primarily residential and commercial tax base.

The series 2006C and 2006C-TE bonds are secured by tax increment revenue collected from the agency's MacArthur/Broadway/San Pablo project area net of the 20% required to be set aside for low- and moderate-income housing projects. All statutory pass-through payments have been subordinated to debt service. The series 2010-T bonds are secured by second-lien tax increment revenues from the MacArthur/Broadway/San Pablo Project, net of low- and moderate-income housing set-asides. Upon the successful closing of the series 2015 TARBs, the rating on the 2006C-TE TABs is subject to discontinuation.

The 676-acre MacArthur/Broadway/San Pablo Project encompasses two noncontiguous areas along the major commercial corridors of Telegraph/Broadway and San Pablo avenues in northern Oakland. The project area was

formed relatively recently, in July 2000. Taxable property comprises a mix of land uses, the majority of which are residential (48% of fiscal 2011 AV) and commercial (39%); industrial uses are minimal (4%). Multifamily uses make up the majority of the residential portion (34% of total AV), with the largest single grouping in five-plus-unit multifamily/condominium residences. The MacArthur/Broadway portion is located adjacent to a major BART transit station, as well as intersecting freeways that provide quick access to San Francisco and the greater Bay Area.

Pledged tax increment revenue for the merged project area totaled $3.79 million in fiscal 2014, a 19.5% decrease from $4.7 million in fiscal 2013. In addition, the fiscal 2015 pledged revenue also declined 23.9% to $2.88 million. The value losses within the Broadway/MacArthur/San Pablo project are related to variations in value among the several medical facilities located in the project area. Specifically to fiscal 2014, a loss of value totaling $476.7 million was reflected in the tax roll due to the fact that the county assessor had not properly applied real estate exemptions in fiscal 2013 but did apply these exemptions for 2014. In fiscal 2015, the loss is due to the fact that property owned by Sutter East Bay Hospitals valued at over $182 million was listed as taxable for 2014 but is listed as almost entirely tax exempt for 2015. The combined two-year pledged revenue loss represented about 38% or about $1.82 million.

Pledged tax increment revenues, based on the fiscal 2015 AV and the debt service schedule for the senior lien, provide strong annual MADS coverage of 2.48x, but a decrease from 3.25x MADS in fiscal 2014 and 4.04x MADS in fiscal 2013. In addition, pledged tax increment revenues, based on the fiscal 2015 AV and the debt service schedule for the subordinate lien, provide good annual MADS coverage of 1.71x, a decrease from 2.24x MADS in fiscal 2014 and 1.9x MADS in fiscal 2013.

Total AV for the project area mirrored the declining tax increment growth trend, having declined $169,000 in fiscal 2015 and $168,000 in fiscal 2014. The combined two-year AV loss represented about 27%, or about $335 million, from fiscal 2013. As a result of the reassessment and hospital shift off the tax rolls, fiscal 2015 AV is below the fiscal 2012 AV level of $917 million. The project area's taxpayer base is concentrated, in our view, with the top 10 taxpayers constituting about 34% of the project area's incremental AV in fiscal 2015. The base-to-total project area AV volatility ratio of 0.41 suggests moderately high tax-increment revenue sensitivity to overall AV fluctuations. At the current annual MADS coverage of 2.48x for the senior lien, and given the moderately high volatility figure, we calculate that the project area could withstand a decline of 35.5% of total AV before MADS coverage fell below 1x. We note that this would cover the loss of the top 10 taxpayers.

The subordinate-lien additional bonds test (ABT) requires 1.25x MADS coverage for all senior and subordinate bonds, based on revenue from the most recent tax rolls (based on AV), including allowances for completed construction and transfers of ownership, as well as revenue from interest rate subsidies. For coverage at the ABT of 1.25x MADS, we calculate that the project area could withstand a 11.9% drop in AV or the loss of the top taxpayer before falling below 1x MADS coverage.

The SA is reporting 136 pending assessment appeals within the project area. The total value under appeal is $84.4 million, or about 9.4% of total fiscal 2015 AV. Based on the historical success rate, which we note may be inflated due to the economic recession appeal data that is backed into the historical data, the SA estimates that about 25 of the 136 appeals will be allowed in fiscal 2016 with a total AV reduction of about $14 million, or a modest 2.6% of fiscal 2015 AV.

The City of Oakland is acting as SA to the former redevelopment agency after the state legislature and a subsequent court ruling dissolved all redevelopment agencies in California in February 2012, pursuant to Assembly Bill (AB) x1 26 and subsequent amending legislation, AB 1484. AB x1 26 and AB 1484 provide an SA and its oversight board with the ability to issue refunding debt. AB 1484 also provides that bonds issued post-dissolution maintain the same validity as those issued pre-dissolution and include provisions that make it possible, in practice, to issue refunding debt. The law requires an SA to receive approval from its oversight board and the state Department of Finance before it can issue refunding bonds. The SA has received its finding of completion, which allows it to reinstate previously rejected loans, spend bond proceeds, and create a long-range property management plan. AB x1 26 and AB 1484 require SA and oversight officials to adhere to deadlines for requesting debt service payment amounts and subordinating pass-through payments, when necessary. Since the law limits the SA revenue to payment on enforceable obligations, and since it requires more proactive management than under the pre-dissolution flow of funds, we believe an agency's debt management practices after dissolution become more important to credit quality. We note that the agency is requesting debt service on an annual basis and reserving across the recognized obligation payment schedule period.

Dissolution legislation permits the SA to issue debt only for certain purposes, such as paying or amending an enforceable obligation, generating savings, or flattening spikes in debt service. The bond indenture does not allow for additional senior debt on the pledged tax revenue for the senior lien; however, it does allow for additional parity debt as long as the annual debt service is lower than the current debt service schedule and the final maturity does not exceed the current maturity. The subordinate lien has a 1.25x ABT. The bonds have a debt service reserve that is funded at a level equal to the least of MADS, 125% of the average aggregate annual debt service (AADS) requirement, or 10% of the bond proceeds; however, AADS and MADS are adjusted to reflect debt service net of the interest rate subsidy.

We consider Oakland's economy very strong. With an estimated population of 404,400, the city is located in Alameda County in the San Francisco-Oakland-Hayward Metropolitan Statistical Area, which we consider broad and diverse. The county unemployment rate was 7.4% in 2013 and preliminary 2014 data suggest that it edged down to 5.9% for 2014. The city has a projected 2018 per capita effective buying income of 120% of the U.S. level, which we consider strong; however, the median household is 100%, or a good level in our view. The per capita market value is $117,900, an extremely strong level in our view. The city is experiencing a surge in economic activity, with a 5.8% AV increase overall to $47.7 billion in 2015 after a 5.1% increase in fiscal 2014. Although we understand that much of this growth represents spillover activity from the robust information technology clusters in Silicon Valley and San Francisco, we believe that the city is well placed geographically to absorb growth as an increasing number of real estate projects become economically viable.

Outlook

The negative outlook is based on our view of the multiple years of AV decline in the project area due to a large reassessment and the removal of a hospital off of the tax rolls, reducing coverage on both liens. We could lower the rating if coverage declines further. We could revise the outlook to stable if coverage were to increase for multiple years and the concentration among the top 10 taxpayers were to decrease.

Related Criteria And Research

Related Criteria

USPF Criteria: Special-Purpose Districts, June 14, 2007

Related Research

U.S. State And Local Government Credit Conditions Forecast, April 2, 2015

Ratings Detail (As Of June 5, 2015)		
Oakland Redev Agy (Broadway/MacArthur/San Pablo Redev Proj Areas) tax incr (AMBAC)		
Unenhanced Rating	A+(SPUR)/Negative	Outlook Revised
Many issues are enhanced by bond insurance.		

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