

# **RatingsDirect®**

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## **Summary:**

# **Yountville, California; Appropriations; General Obligation**

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## **Table Of Contents**

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Rating Action

Stable Outlook

Credit Opinion

Related Research

## Summary:

# Yountville, California; Appropriations; General Obligation

### Credit Profile

Yountville (town of) ICR

*Long Term Rating*

AA/Stable

Downgraded

#### **Yountville Fin Auth, California**

Yountville, California

Yountville Fin Auth (Yountville (town of)) lse rev rfdg bnds (Yountville (town of)) ser 2017 dtd 10/24/2017 due 10/01/2039

*Long Term Rating*

AA-/Stable

Downgraded

Yountville Fin Auth (Yountville)

*Long Term Rating*

AA-/Stable

Downgraded

### Rating Action

S&P Global Ratings lowered its issuer credit rating (ICR) to 'AA' from 'AA+' on the Town of Yountville, Calif., and lowered its long-term rating to 'AA-' from 'AA' on the town's lease revenue bonds outstanding. The outlook is stable.

The bonds are secured by lease payments by the Town of Yountville, as lessee, to the Yountville Finance Authority, as lessor, for the use and possession of the leased assets. Consistent with our "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" criteria, published Nov. 20, 2019, on RatingsDirect, we rate these obligations one notch lower than the city's general creditworthiness to account for the appropriation risk associated with the lease payments. The town has covenanted to budget and appropriate annual lease payments for various properties' use. Payments are triple net, without right of set-offs, and the town is responsible for maintenance, taxes, and utilities. Payments may be abated in the event of damage to, or the destruction of, the leased assets. To mitigate abatement risk in such a case, the town has covenanted to maintain rental interruption insurance coverage equal to 24 months of maximum annual debt service.

### Credit overview

The rating action is based on our view of the Town of Yountville's transient occupancy tax (TOT) and sales taxes, which account for 68% of the town's operating revenue, are cyclical and volatile in nature, and have suffered from business closures as a result of the COVID-19 pandemic and recent wildfires in the region. The town experienced significant loss in TOT revenue in fiscal 2020 and projects similar losses in fiscal 2021. Yountville is located in the heart of Napa Valley's wine country with affluent residents and year-round tourism that has contributed to historically strong TOT performance and allowed the town to build very strong reserves in excess of 75% of general fund expenditures. Although the town has very strong reserves and budgetary flexibility, its 2021 budget no longer reflects reserves in excess of 75% of general fund expenditures. Given the uncertainty of the pandemic, large reliance on TOT revenue, and weaker TOT collections compared with prior years, we believe that the town will not sustain reserves of

excess of 75% of expenditures and may experience additional budget shortfalls for the current and possibly next fiscal year, which would make it no longer comparable to higher-rated peers given the town's overall credit profile.

The ratings further reflect our view of the town's:

- Adequate economy, with projected per capita effective buying income at 140% and market value per capita of \$361,781, although a concentrated local tax base slightly limits this;
- Strong management, with good financial policies and practices under our financial management assessment methodology;
- Weak budgetary performance, with a slight operating deficit in the general fund but an operating surplus at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 62% of adjusted operating expenditures. We note that adjusted operating expenditures include recurring transfers out;
- Very strong liquidity, with total government available cash at 1.6x total governmental fund expenditures and 22.0x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 7.4% of expenditures and net direct debt that is 71.4% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value; and
- Adequate institutional framework score.

### **Environmental, social, and governance factors**

We analyzed the town's environmental, social, and governance risks relative to its economy, management, financial measures, and debt and liabilities profile. We believe that the town has elevated exposure to environmental risks, with earthquakes and wildfires--including the Glass and LNU Lightning Complex fires within the county--the most prominent. We think a newer building stock, most of which has been subject to improvements to the state's building codes as earthquake hazards to buildings became better known, partly mitigates the town's seismic risk. In addition, we believe the town has elevated social risks associated with the dependency on tourism, which accounts for a large percentage of its TOT and sales tax revenue amid business closures as a result of the pandemic. Finally, we also reviewed governance risks and consider them in line with the sector standard. The rating incorporates our view of the health and safety risks posed by the COVID-19 pandemic. Absent the implications of COVID-19, we consider the town's social risks in line with the sector standard.

## **Stable Outlook**

### **Downside scenario**

We could lower the rating if the town's operating revenue continues to substantially decline given its tourism-driven economy, while available fund balance and liquidity decrease to levels no longer comparable with those of similarly rated peers.

## **Upside scenario**

We could raise the ratings if the town's available fund balance strengthens further and is sustained at more than 75% of general fund operating expenditures.

## **Credit Opinion**

### **Adequate economy**

We consider Yountville's economy adequate. The town, with an estimated population of 2,962, is located in Napa County. The town has a projected per capita effective buying income of 140% of the national level and per capita market value of \$361,781. Overall, the town's market value grew by 3.2% over the past year to \$1.1 billion in 2021. Constraining Yountville's economy is a concentrated local tax base, with the 10 largest taxpayers accounting for 43.1% of the total tax base. The top taxpayer makes up 18.2% of total assessed value (AV). Vintage Estate LLC is a 22-acre estate that includes Vintage House, Villagio Inn & Spa, and the Pavilion, a popular wedding venue. While the top 10 taxpayers are concentrated in hotels, we do not expect any loss in top taxpayers to materially affect the town's tax base. Although the county's unemployment rate rose sharply and peaked at 16.1% in April 2020, it subsequently declined to 8.3% for August 2020.

Located in the heart of Napa County, the Town of Yountville is a wine and culinary destination for Bay Area residents and tourists from around the world. Thus, its tax and economic base is very tourism-based, including hotels, high-end resorts, restaurants, and wineries. The tax base was resilient, with increasing TOT revenue through the Great Recession, but suffered from closures and shelter-in-place orders as a result of the COVID-19 pandemic and recent wildfires. However, the town's historically strong TOT performance allowed it to build reserves to very strong levels with very strong budgetary flexibility to help mitigate the TOT revenue shortfalls in fiscal years 2020 and 2021.

For more information on our view of the U.S. economy, see our report "Staying Home For The Holidays," published Dec. 2, 2020, on RatingsDirect.

### **Strong management**

We view the town's management as strong, with good financial policies and practices under our financial management assessment methodology, indicating our view that financial practices exist in most areas but that governance officials might not formalize or monitor all of them on a regular basis.

Our view of the town's financial policies and practices reflects the following:

- Strong and well-grounded revenue and expenditure assumptions with historical assumptions and use of various sources for its tax revenue,
- Monthly budget-to-actual reporting to the council with the ability to amend budgets as needed,
- A lack of long-term financial planning,
- Maintenance of a rolling, five-year comprehensive capital improvement plan,
- A formal investment policy with quarterly reporting of performance and holdings to the council,
- A formal debt management policy,

- A formal reserve policy that includes a minimum revenue stabilization reserve at 25% of TOT revenue budget and an emergency reserve at 20% of the general fund expenditure budget.

### **Weak budgetary performance**

We view Yountville's budgetary performance as weak as a result of weaker operating performance in recent audited years following multiple years of strong results, mainly as a result of recurring interfund transfers out. In fiscal 2019 the town had a slight deficit operating result in the general fund of 1.5% of adjusted expenditures that includes \$4 million in interfund transfers out to its emergency reserve and revenue stabilization funds, but a surplus result across all governmental funds of 15.9%. Based on the town's actual results for fiscal 2020, we anticipate that the general fund will yield a net operating surplus of 6.7%, or \$573,000, that includes transfers out. The town adopted a budget for fiscal 2021 with another net operating surplus of approximately 2.3%. The adopted budget includes cost savings of eliminating the community faculties manager position, other reorganization of the parks and recreation department, suspension of interfund transfers out to its other funds and reserves, and maintenance of internal services. We understand the town is using \$1 million from its revenue stabilization fund to support its budgeted expenditures for fiscal 2021 as a result of TOT revenue that is expected to be lower than in prior years. We note that adjusted operating expenditures include transfers out.

Our assessment accounts for our view of the cyclical and volatile nature of TOT and sales revenue, and that budgetary results could improve given the town's willingness to adjust budgets and use its set-aside reserves to mitigate potentially weaker TOT and sales tax revenue performance in fiscal 2021 as a result of a weaker economic environment and the uncertainties associated with the COVID-19 pandemic.

TOT and sales taxes accounted for approximately 68% of the town's general fund revenue in fiscal 2019, and property taxes for approximately 13%, having collectively increased in each of the past several years. Primarily as a result of its tourism tax base, we consider the city's TOT and sales taxes moderately concentrated revenue sources. Fiscal 2020 TOT collections experienced a loss of 19%, or \$1.3 million, of the budgeted \$7 million, and for fiscal 2021 management projects a loss of \$1.8 million in TOT revenue of the budgeted \$5.3 million and a loss of \$300,000 in sales tax revenue. According to the town's most recent available financial report, dated Oct. 31, 2020, TOT collections are at 13% of budget compared with the prior year's financial report dated Oct. 31, 2019, when TOT collections were at 25% of budget. Management is aware of the cyclical and volatile nature of the TOT and sales tax revenue, which was experienced during the 2017 wildfires. As a result, the town increased its reserve balances in its emergency reserve and revenue stabilization funds to prepare for an economic downturn or a major disaster.

### **Very strong budgetary flexibility**

Yountville's budgetary flexibility is very strong, in our view, with available reserves in fiscal 2019 of 62% of adjusted operating expenditures, or \$8.2 million (which includes approximately \$4 million in the emergency reserve and revenue stabilization funds). We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor. We note that adjusted operating expenditures include recurring transfers out.

The town maintains very strong reserves and estimates that it will end fiscal 2020 with approximately \$7.5 million, or 88% of general fund operating expenditures, in available reserves. The town's fiscal 2021 adopted budget shows very

strong 73.4% available reserves, or approximately \$6.8 million. We understand the town is using approximately \$1 million in its revenue stabilization fund to help balance its budgeted general fund expenditures for fiscal 2021. In our opinion, the town's very strong available reserves continue to be a credit strength. Given the town's formal reserve policies and history of maintaining reserves at levels well above the minimum requirements, we expect budgetary flexibility to remain very strong.

### **Very strong liquidity**

In our opinion, Yountville's liquidity is very strong, with total government available cash at 1.6x total governmental fund expenditures and 22.0x governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

The town's investments are in the local agency investment fund, which we view as nonaggressive. Based on past issuance of debt, we believe that the issuer has strong access to capital markets to provide for liquidity needs if necessary, including lease revenue bonds in 2008 and 2013. We do not anticipate a change in the town's liquidity ratios. We understand the town entered into a private placement with Westamerica for \$2.3 million in June 2020 to refinance its 2013 lease revenue bonds, and we do not view this as a remote contingent liability.

### **Strong debt and contingent liability profile**

In our view, Yountville's debt and contingent liability profile is strong. Total governmental fund debt service is 7.4% of total governmental fund expenditures, and net direct debt is 71.4% of total governmental fund revenue. Overall net debt is low at 2.3% of market value, which is, in our view, a positive credit factor. We understand that the town has no debt plans.

### **Pension and other postemployment benefit (OPEB) liabilities**

- In our view, the town's pension and OPEB liability is manageable, and we do not believe that it will be a source of significant budgetary pressure.
- The town established an irrevocable Section 115 OPEB Trust with Public Agency Retirement Services, and as of June 30, 2019, the trust had a balance of approximately \$4.2 million to help reduce future liabilities.

The town participated in the following plans funded as of June 30, 2019:

- CalPERS cost-sharing multiple-employer defined benefit pension plan: \$3.9 million in net liability, and 75% funded
- Single-employer defined benefit health care OPEB plan: \$1.2 million in net liability, and 78% funded

Yountville's required pension and actual OPEB contributions totaled 13.6% of total governmental fund expenditures in 2019, with 4.8% representing required contributions to pension obligations and 8.8% representing OPEB payments.

The town made its full annual required pension contribution.

In our view, a discount rate higher than our 6% guideline could lead to contribution volatility, but we view CalPERS' recent funding changes to a 20-year, level dollar amortization approach for new gains and losses, in line with our guidelines, as positive for credit quality. While this will lead to more immediate contribution increases, a shorter amortization period that no longer defers costs will provide a faster funding recovery following years of poor investment performance and upward revisions to the liability. Contributions to the OPEB liability are made on a

pay-as-you-go basis, but as a result of previous contributions the town has nearly fully funded the liability.

### **Adequate institutional framework**

The institutional framework score for California municipalities not required to submit a federal single audit is adequate.

## **Related Research**

- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2020 Update Of Institutional Framework For U.S. Local Governments

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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