STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

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## Summary:

# San Diego Community Facilities District No. 2 (Santaluz) Improvement Area 1, California; Special Assessments


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| *Long Term Rating* | BBB+/Stable | Affirmed |

## Rationale

Standard & Poor's Ratings Services affirmed its 'BBB+' rating on San Diego Community Facilities District No. 2 (Santaluz) Improvement Area 1, Calif.'s series 2011A special tax refunding bonds. The outlook is stable.

The rating reflects what we view as:

- A calculated adequate 16:1 direct and overlapping value-to-lien (VTL) ratio after reductions in assessed value (AV) in the past few years;
- A large 16% of the levy from properties without improvement value and VTL below 10:1; and
- Only adequate coverage of 1.1x annual debt service from special tax revenue, including from property without improvement value.

The preceding credit weaknesses are offset in part by what we consider:

- A diverse, primarily residential district in San Diego;
- An improved tax collection rate in the past couple of years; and
- A closed parity lien except for refunding purposes.

The bonds are secured by special taxes collected from real property in the district, net of administrative expenses.

San Diego Community Facilities District No. 2 is 20 miles northeast of downtown San Diego, and encompasses 2,546 gross acres. The district is primarily residential and levied a special tax on 996 parcels in fiscal 2014 with 84% of the special tax levy from completed parcels.

We calculate the district's direct and overlapping VTL ratio as a whole is about 16:1 in fiscal 2014, reflecting what we consider a relatively large amount of district debt. The direct VTL in fiscal 2014 is 23:1. In fiscal 2014, district AV remains relatively stable at about $1.09 billion, just a slight increase from its 2013 value. While the obligation to pay special taxes is unrelated to AV, AV does drive VTL ratios on the properties.

In our view, given the primarily residential composition of the district, the tax base is diverse, with the top 10 taxpayers consisting of 6.5% of the special taxes. The leading taxpayer, a golf course, comprises only 2.7% of the fiscal 2014 special tax levy.

Special tax rates vary across parcels based on square footage. The fiscal 2013 actual special tax ranged from $1,588 for a parcel under 1,750 square feet to $8,040 for a residential custom lot; the corresponding assigned maximum rates range from $2,140- $10,830. An "undeveloped" property, as defined by the rate and method, is property owned by owners in the business of home building. The assigned maximum special tax for an undeveloped lot is very high, in our view, at $22,969; there are 13 undeveloped parcels left in the district. While the district has not levied special taxes on undeveloped property as defined by the rate and method, the 2014 special tax levy is imposed on parcels that are vacant and undeveloped and owned by nonhomebuilders. Given the level of unimproved property, about 16% of the fiscal 2014 levy is generated by properties with a direct VTL under 10:1, which we consider weak.

The median AV for improved single-family homes in the district is about $1 million. For noncustom homes in the district and custom homes with improvement value, a sample total median overlapping effective tax rate represents about 1.5% of value.

About 2% of the first installment of the tax levy was delinquent as of December 2013; however, substantially all of the previous-year delinquencies had been collected. We understand the district has historically set the actual levy based on historical delinquency rates, estimated administrative fees, and debt service.

The district's 2014 levy represents 63% of its maximum levy. The maximum tax levy would generate $6.2 million, which would cover annual debt service in each year by about 1.5x. However, officials estimate a lower practical levy given state law that limits the levy increase to 10% on residential owners as a result of delinquencies. Assuming the district was to levy at 1.1x annual debt service, it could withstand a 13.75% delinquency rate over the life of the bonds with the use of the debt service reserve.

Median household effective buying income for San Diego is what we view as strong, at 117% of the national levels. Unemployment for the city was 6.9% in March 2014.

## Outlook

The stable outlook reflects our view of the district's diversity and strong median incomes, which we believe will likely provide support for continued good collections and coverage. Given the level of unimproved properties in the district, we are unlikely to raise the rating in the next two years. If development in the long-term causes AV in the district to increase such that debt ratios moderate, we could raise the rating. If delinquency rates were to return to the higher levels seen in previous years, or if AV values fall significantly, we could lower the rating.

## Related Criteria And Research

### Related Criteria

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

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