Moody's
INVESTORS SERVICE

Rating Update: **MOODY'S DOWNGRADES CITY OF BURLINGTON'S (VT) GO BOND RATING TO A2 FROM Aa3 AND REMOVES CITY FROM WATCHLIST FOR POSSIBLE DOWNGRADE; NEGATIVE OUTLOOK ASSIGNED**

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APPROXIMATELY $87 MILLION OF OUTSTANDING PARITY DEBT AFFECTED

Burlington (City of) VT
Municipality
VT

Opinion

NEW YORK, Jul 9, 2010 -- Moody's Investors Service has downgraded to A2 from Aa3 the City of Burlington's (VT) general obligation bond rating, affecting approximately $87 million in outstanding parity debt. The bonds are secured by a general obligation unlimited tax pledge. Concurrently, Moody's has downgraded the city's outstanding A1-rated Certificates of Participation (COPs) to A3 and its outstanding A2-rated COPs to Baa1, affecting $4 million and $10.4 million in outstanding COPs, respectively. The downgrade incorporates the city's reduced liquidity resulting from the use of its pooled cash account to finance the expansion of Burlington Telecom (BT), the city's telecommunications enterprise. The rating also factors the city's inability, through BT operations, to make successive lease payments to CitiCapital, resulting in draws on the debt service reserve fund (DSRF) to fund debt service. The negative outlook reflects the possibility of further downward rating movement over the near term. While the city is actively pursuing a viable solution for the telecommunications system there remains a high degree of uncertainty regarding the city's ability to place the enterprise on a more sustainable path and ultimately repay the funds owed to the city's pooled cash account.

GROWTH OF INTERFUND LOAN AND MISSED LEASE PAYMENTS IMPACT CREDIT PROFILE; UNCERTAINTY REMAINS REGARDING PROSPECTS FOR REPAYMENT TO POOLED CASH FROM BURLINGTON TELECOM

The city's fiscal 2009 financial statements (as of 6/30) include an amount of negative $15.05 million due to the city's pooled cash account from BT. Subsequently, this amount has grown to approximately $17 million. Importantly, the amount due to the pooled cash account has not grown beyond this level as the city is currently prohibited from making any additional draws on the pooled cash account to fund BT obligations, following a Vermont Public Service Board ruling. The increase in the liability at the end of the fiscal year represents a substantial $7.3 million or 85% increase from the negative $8.6 million balance at the end of fiscal 2008 and a 212% increase since the end of fiscal 2007. The amount due from BT is the result of a prolonged period of support from the city's pooled cash account to fund the citywide build out of the telecommunications system, which is currently behind schedule. Despite the city's efforts, the telecommunications system has been unsuccessful at generating the cash flows necessary to self-fund its operating, capital and debt expenses or to achieve a realistic refinancing plan to repay the interfund loan due to the pooled cash account. The city has historically included the General Fund and the airport enterprise, among other smaller accounts, in its pooled cash management program.

Importantly, at negative $17 million the interfund borrowing represents a sizable 192% of the city's fiscal 2009 General Fund balance of $8.8 million and 218% of the combined General Fund and School Fund balance. Of note, the School Fund maintains a negative $1.06 million fund balance position. As noted in the city's audited financial statements the amount due to the pooled cash account may be addressed with a General Fund transfer if it cannot be demonstrated that the interfund loan can be fully or partially repaid within a reasonable time frame. Assuming the General Fund fully reflects this interfund loan and adjusting fund balance for the illiquid nature of the receivable, the city's Moody's adjusted General Fund reserve position declines to a pro-forma negative 16% of General Fund revenues from its current positive level of 17.6% of revenues.

The city has missed two $386,000 scheduled lease payments, which were due on 17th of February and May to CitiCapital. The lease payments, which relate to the telecommunications enterprise, were suspended following a Public Service Board ruling preventing the city from utilizing any additional funds from its pooled cash account to fund telecommunications related obligations. CitiCapital has utilized a $1 million DSRF to make up the shortfall thus far, although the remaining balance of the DSRF would be insufficient to make the next August payment in full. The city and CitiCapital are currently in negotiations regarding the city's outstanding delinquency and the status of future lease payments. Remedies in the event of default include possession of the assets and acceleration of the current year's lease payments, although neither option has been exercised. Importantly, the circumstances of non-payment on the lease are due primarily to the ruling by the Vermont Public Service Board prohibiting the city from utilizing its pooled cash account to fund BT obligations rather than an unwillingness of the city to fund its debt obligations.

Future rating action will continue to depend on the city's ability to produce a viable plan to place the telecommunications system on a more sustainable path and provide additional detail on the prospects for the system to meet its obligations, including repayment of the interfund loan. Additionally, given the city's reliance on cash flow borrowing Moody's will continue to monitor the city's cash position, its ability to meet day-to-day operating requirements and general fund debt service payments, and how a potential default of their outstanding telecom lease obligation would impact operations of the enterprise.

Outlook

Burlington's credit outlook is negative reflecting Moody's expectation that BT will remain challenged to pay back the pooled cash account in the medium term, continued uncertainty regarding future BT operating results, and the potential impact on the city's General Fund should BT fail to demonstrate an ability to repay the obligation.

What could move the rating UP (remove the negative outlook):

-Reduction or elimination of the amount due from BT to the pooled cash account

What could move the rating DOWN:

-Inability to make meaningful progress towards repayment of the interfund loan

-Lack of a viable plan to place the telecommunications system on a more sustainable path or growth on the negative net asset position of the Telecom Fund

-Structurally imbalanced General or School Fund operations, reducing the city's financial flexibility

RATING METHODOLOGIES USED AND LAST RATING ACTION TAKEN

The principal methodology used in rating the City of Burlington (VT) was Moody's "General Obligation Bonds Issued by U.S. Local Governments," published in October, 2009 and available on www.moodys.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

The last rating action with respect to the City of Burlington (VT) was on March 9, 2010 when the city's municipal finance scale general obligation rating was downgraded to A2 and the city was placed under review for possible downgrade. That rating was subsequently recalibrated to Aa3/under review for possible downgrade May 1, 2010.

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