

# RatingsDirect®

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## Summary:

# Topsfield, Massachusetts; General Obligation

### Primary Credit Analyst:

Rahul Jain, New York + 1 (212) 438 1202; rahul.jain@spglobal.com

### Secondary Contact:

Christian Richards, Boston (1) 617-530-8325; christian.richards@spglobal.com

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### Credit Profile

US\$13.5 mil GO bnds due 03/01/2044

<i>Long Term Rating</i>	AAA/Stable	New
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Topsfield GO muni purp loan bnds ser 2017 due 10/15/2042

<i>Long Term Rating</i>	AAA/Stable	Upgraded
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Topsfield Internal/confidential credit estimate

<i>Long Term Rating</i>	AAA/Stable	Upgraded
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## Rationale

S&P Global Ratings raised its long-term and underlying ratings on the 'Town of Topsfield, Mass.' general obligation (GO) debt to 'AAA' from 'AA+'. At the same time, S&P Global Ratings assigned its 'AAA' long-term rating to the town's series 2019 GO municipal purpose loan bonds. The outlook on all ratings is stable.

The upgrade reflects our view of the town's consistent operating surpluses supporting continued reserve growth amid a rising debt burden, underpinned by a formalization of its management practices and policies on debt management and reserves in December 2018, which provide a strategy for maintaining the town's financial health. 2018 audited results portray a sustained commitment to increasing funds set aside for the payment of long-term liabilities, including other postemployment benefits (OPEB), while managing to its largest operating surplus over the last five years. In addition, we expect surplus results will continue in fiscal 2019, inclusive of amounts budgeted for reserve set-aside.

The town's full faith and credit pledge secures the bonds. The town's bonds are subject to Proposition 2-1/2 and are therefore a limited GO. However, due to the town's revenue-raising ability and fungibility of those resources, we have not made a rating distinction between the limited and unlimited nature of the pledge. Bond proceeds will be used to permanently finance approximately \$6 million, \$4 million, and \$3.5 million in bond anticipation notes for a town hall remodeling and addition, water treatment facility, and school roof replacement, respectively, the first and third of which are excluded from the state's Proposition 2-1/2 debt service levy limitations. While the bonds are GOs of the town, Topsfield intends to raise the necessary water-user charges and fund the debt service related to the water treatment facility project through its water enterprise fund. We also note that based on the expected payment of debt service through water revenues, the debt does not count toward the town's Proposition 2-1/2 debt cap.

The long-term rating further reflects Topsfield's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level

in fiscal 2018; Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 18% of operating expenditures;

- Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 18% of operating expenditures;
- Very strong liquidity, with total government available cash at 83.8% of total governmental fund expenditures and 30.5x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 2.7% of expenditures and net direct debt that is 90.0% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

### **Very strong economy**

We consider Topsfield's economy very strong. The town, with an estimated population of 6,441, is located in Essex County in the Boston-Cambridge-Newton, MA-NH MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 199% of the national level and per capita market value of \$218,691. Overall, the town's market value grew by 3.4% over the past year to \$1.4 billion in 2019. The county unemployment rate was 3.8% in 2017.

The town is mainly residential (92.4% of property value) and serves as a commuter suburb to Boston; however, it maintains a small commercial and industrial base, representing approximately 4.8% and 1.3% of total assessed value, respectively. The largest employers are Masconomet Health Care, Fairview Machine Co., and Harmony Health. Unemployment rates have traditionally been lower than state and national trends. The largest seasonal employer is the Essex Agricultural Society, which manages the Topsfield Fair.

The town is known for its annual Topsfield Fair, a 200-year-old, week-plus-long agricultural fair that is the oldest in the country. The fair swells local employment each fall. Despite its mature nature, Topsfield has experienced some recent development, including a number of multi-family residential and commercial projects. Management reports continued interest in parcels throughout the town, including along underdeveloped corridors, such as Perkins Row. Building permit revenues reflect associated commercial and residential development in fiscal 2017, with physical assets to come online in the near term.

### **Very strong management**

We view the town's management as very strong, with strong financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

We recently revised Topsfield's FMA to strong from good. The improvement reflects the town's adoption of additional financial policy guidelines that formalize existing practices, codifying the town's approach to managing debt and establishing and maintaining reserves. The guidelines, which were approved in December 2018, set targeted levels for debt service, overall debt burden, as well as reserve levels for free cash, stabilization fund, and capital stabilization. The debt management policy also recommends excluding large projects from Proposition 2-1#?#2 and requires preparation of an annual update to capital planning documents. The adoption of the guidelines serves as the culmination of a recent liaison with the Collins Center at the University of Massachusetts Boston and highlights

management's continued efforts to strengthen management practices in support of fiscal stability.

Topsfield's management strives to produce accurate financial and budgetary projections, resulting in predictable and stable year-end financial results. Its partnership with Collins also produced a detailed five-year financial plan, which expands the plan the town had used in years past. In addition, Topsfield enhanced its capital improvement plan, which includes five years of funding sources for all identified capital projects.

These documents, along with multiyear revenue and expenditure analysis, are the basis for the budgeting process. Monthly updates on year-to-date performance are reviewed by the finance committee. If a department identifies a deficit in an expenditure category, it can request a reserve fund transfer from the finance committee. Should a transfer be required from another budgeted source, voters can approve the transfer at the annual town meeting. Topsfield follows state law on investments, and formally presents performance updates at year-end. It has a debt management policy and maintains targets for annual certified free cash of 3% of last year's tax levy after expenditures and the stabilization reserve fund of 5% of last year's tax levy, as well as targets for various other reserve funds, such as compensated absences.

### **Strong budgetary performance**

Topsfield's budgetary performance is strong in our opinion. The town had slight surplus operating surpluses of 3.8% of expenditures in the general fund and of 6.2% across total governmental funds in fiscal 2018. General fund operating results have been stable in the past five years.

Topsfield continues to post operating surpluses, after regular transfers out for capital and its OPEB trust, which we include in our assessment of results given their recurring nature. Audit results from 2018 show the strongest surplus result in the last five years, inclusive of a continuation of transfers out for capital and the OPEB trust.

The town has experienced sustained positive revenue variance while experiencing minimal or positive variance among expense line items, including education. Management has worked with its employees to find recurring health care savings and reviewed pay classifications and trend data support a 0% health care rate increase for the town. Local property taxes accounted for approximately 80% of general fund revenues in fiscal 2018, while intergovernmental revenues were approximately 13%. We adjust general fund results to account for annual operating transfers from the water enterprise fund and nonmajor governmental funds. We also accounted for the enterprise transfer in and the expenditure in the total governmental funds net result.

Fiscal 2018 results show positive variance among all major line items, including building permit, fine, and other non-property tax revenues. The surplus includes a one-time \$400,000 for acquired land and deposits into the stabilization and capital stabilization fund. Topsfield's 2019 budget was balanced and increased the expected appropriation into the OPEB trust to \$300,000; year-to-date results show the town is likely to successfully set aside funds for reserves while still operating to a surplus. Town officials do not expect significant deviation from the current trend for fiscal 2020.

### **Very strong budgetary flexibility**

Topsfield's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2018 of 18% of operating expenditures, or \$5.2 million. Over the past three years, the total available fund balance has risen steadily,

totaling 17% of expenditures in 2017 and 16% in 2016.

The town has conservatively managed to sustain operating surpluses, including the largest of the last five years in 2018, and plans to provide set-asides for pay-as-you-go capital in its financial plan, which provides additional spending flexibility. These management actions support our belief Topsfield will maintain reserves of more than 15%, which we consider very strong, over the near term. The town has also reviewed its policies and is considering raising its informal target for free cash based on year-end levels in recent years. All labor contracts run through fiscal 2020 and do not pose concerns of retroactive payment.

### **Very strong liquidity**

In our opinion, Topsfield's liquidity is very strong, with total government available cash at 83.8% of total governmental fund expenditures and 30.5x governmental debt service in 2018. In our view, the town has strong access to external liquidity if necessary.

Topsfield is a regular market participant that has issued bonds and notes frequently over the past several years. Our view of liquidity is adjusted for cash held in the Gould trust. It does not have any variable-rate or direct-purchase debt, nor does it have any contingent liquidity risks from financial instruments with payment provisions that change on the occurrence of certain events. We expect Topsfield's liquidity to remain very strong.

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

In our view, Topsfield's debt and contingent liability profile is strong. Total governmental fund debt service is 2.7% of total governmental fund expenditures, and net direct debt is 90.0% 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.

As the town permanently finances most of its bond anticipation notes--which made up about 80% of debt outstanding at the end of fiscal 2018--we expect carrying charges to rise as a share of expenditures, but not to exceed more than 6%, a figure we believe remains manageable within the budget profile and does not change our view of the debt profile in the future. In November of this year, Topsfield anticipates issuing approximately \$6.7 million, which is expected to be the only remaining issuance through fiscal 2021. Of the new money debt, about \$2.7 million will be for water-related capital projects. The town's water enterprise debt is fully self-supporting and we expect future water-related issuance to also be self-supporting.

Topsfield's combined required pension and actual OPEB contributions totaled 5.3% of total governmental fund expenditures in 2018. Of that amount, 3.4% represented required contributions to pension obligations, and 1.9% represented OPEB payments. The town made 100% of its annual required pension contribution in 2018.

The town provides pension benefits to eligible employees through the Essex Regional Retirement System, a cost-sharing, multiple-employer, defined-benefit pension system. For the Jan. 1, 2018 valuation, it had a proportionate net pension liability of \$13.6 million. Topsfield has paid its actuarially determined contribution (ADC) consistently, including in each of the past five fiscal years, and anticipates continuing to do so.

Topsfield also provides OPEB in the form of partially town-paid health care for eligible employees. It established an OPEB trust to begin pre-funding benefits, and as of the June 30, 2017 valuation, the trust had an actuarial value of approximately \$599,000. The town expects the amount in trust to be closer to \$1 million as of Sept 1, 2018. The total

OPEB liability was \$14.6 million as of June 30, 2017, prior to netting out the fiduciary net position. Management said its latest valuation report shows a decline in this liability of \$3.7 million, most attributable to a change in the discount rate. The town has a funding strategy to increase the current \$300,000 annual OPEB contribution by \$20,000 annually until the contribution reaches \$500,000 annually. Once the pension liability has been fully funded, the town expects to allocate the amount that had been previously spent on pension liability to be applied to the OPEB trust.

While the town expects to add debt within the next two years, we do not anticipate significant budgetary pressure from the additional debt burden. Furthermore, although the reduction in the discount rate increased the net pension liability and increased the ADC, we expect that Topsfield will continue to budget for and fully fund any increased pension costs. If the town is able to contribute to its OPEB trust, as planned over the next few years, it may begin to meaningfully reduce the OPEB liability in the next several years; however, we believe pay-as-you-go OPEB and trust contributions remain a potential area of pressure on the budget.

### **Strong institutional framework**

The institutional framework score for Massachusetts municipalities is strong.

## **Outlook**

The stable outlook reflects S&P Global Ratings' expectation that Topsfield's very strong management practices and policies, supported by very strong wealth and income levels, will continue to produce balanced operating results, with maintenance of very strong budgetary flexibility and liquidity levels. For these reasons, we do not expect to change the rating within our two-year outlook horizon.

### **Downside scenario**

However, if budgetary performance were to weaken, either on a sustained basis or due to a significant event, straining reserves or available cash, we could lower the rating.

## **Related Research**

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- Local Government Pension And Other Postemployment Benefits Analysis: A Closer Look, Nov.8, 2017
- 2018 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

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