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Summary:

Topsfield, Massachusetts; General Obligation

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US\$4.766 mil GO muni purp loan bnds ser 2017 due 10/15/2042

Long Term Rating

AA+/Stable

New

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to Topsfield, Mass.' 2017 general obligation (GO) bonds. The outlook is stable.

The town's full faith and credit pledge secures the bonds. The town voted to exclude debt service related to the town hall remodeling project from the provisions of Massachusetts Proposition 2-1/2. The remaining bonds are subject to Proposition 2-1/2 and are therefore a limited general obligation. However, due to the town's revenue-raising ability, we have not made a rating distinction between the limited and unlimited nature of pledge.

Proceeds of the bonds will be used for a number of capital projects, including remodeling town hall; purchasing vehicles; and infrastructure repair, including water mains. While the bonds are GOs of the town, the community intends to raise the necessary water user charges and fund the debt service related to the water main project through its water enterprise fund.

We base the long-term rating on our local GO criteria, reflecting our assessment of the following factors for Topsfield, including its:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with "good" financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with slight operating surpluses in the general fund and at the total governmental fund level in fiscal 2016;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 16% of operating expenditures;
- Very strong liquidity, with total government available cash at 35.0% of total governmental fund expenditures and 18.5x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 1.9% of expenditures and net direct debt that is 56.2% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value, but significant medium-term debt plans; and
- Strong institutional framework score.

Very strong economy

We consider Topsfield's economy very strong. The town, with an estimated population of 6,356, is a primarily residential community, approximately 25 miles north of Boston and adjacent to Interstate 95 in Essex County. It is in the Boston-Cambridge-Newton MSA, which we consider to be broad and diverse. The town has a projected per capita

effective buying income of 189% of the national level and per capita market value of \$204,346. Overall, market value grew by 2.5% over the past year to \$1.3 billion in 2017. The county unemployment rate was 3.8% in 2016.

While many residents commute to Boston, the town maintains a small commercial and industrial base, representing approximately 4.5% and 1.4% of total assessed value (AV), respectively. The largest employers within its borders are Masconomet Health Care, Fairview Machine Co., and Harmony Health. Additionally, the town is known for its annual Topsfield Fair, a 200-year-old, week-plus long agricultural fair. Recent development includes a new, 30-unit, age 55-plus housing project. Town management also notes that there is interest in redeveloping several existing commercial properties.

Given its location near Boston, along with easy access via I-95, we expect that Topsfield will continue to benefit from its proximity to and location within the MSA. While new development and redevelopment may add modestly to the tax base, we anticipate that the underlying wealth and income metrics will remain very strong over the next two years due to the stable residential base.

Strong management

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

Topsfield's management strives to produce accurate financial and budgetary projections, resulting in predictable and stable year-end financial results. To this end, management partnered with the Collins Center at the University of Massachusetts, Boston to enhance existing financial management policies. This partnership has produced a detailed five-year financial plan, which expands in both detail and scope the five-year plan the town has used in years past. Additionally, Topsfield improved its five-year 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 day. The town follows state law on investments, and formally presents performance updates at year-end. It has a draft debt management policy, which management anticipates being formally adopted as part of the fiscal 2019 budget process. Finally, while the town does not have a target for general fund reserves, it does maintain targets for annual certified free cash (\$750,000) and the stabilization reserve fund (\$100,000), as well as targets for various other reserve funds, such as workers' compensation. An update on the reserve fund balance policy is also expected to be adopted later this year.

Strong budgetary performance

Topsfield's budgetary performance is strong in our opinion. The town had slight operating surpluses of 0.6% of expenditures in the general fund and of 1.4% across all governmental funds in fiscal 2016. General fund operating results of the town have been stable over the last three years, with a result of 1.2% in 2015 and a result of 2.2% in 2014.

Topsfield posted a third consecutive positive general fund operating result in fiscal 2016. Management credits a

conservative budgeting style, along with nonproperty tax local revenues coming in over budget in fiscal 2016, for the balanced results. We adjusted general fund results to account for annual operating transfers from the water enterprise fund and nonmajor governmental funds, as well as a debt service reimbursement from the library's trust fund. Additionally, we also accounted for the enterprise transfer in and the expenditure of previously received bond anticipation note (BANs) proceeds in the total governmental funds net result.

When fiscal 2017 results are finalized, management expects to report general fund results similar to, and likely better than, fiscal 2016. Management notes that it, in coordination with the town's labor unions, has sought cost savings in health care, with estimated annual savings between \$100,000-\$150,000 annually. Additionally, management conducted a pay classification study, to bring additional structure and predictability to the town's personnel costs. It believes these efforts will continue to allow the town to produce balanced budgets and results in fiscal 2018 and beyond. Management notes that there is a need for investment in the town's physical capital, but expects to address these through careful debt management and budgeting; to that end, the town's annual budget includes a \$300,000 line-item for pay-as-you-go capital needs, which management expects will reduce borrowing.

Local property taxes accounted for approximately 80% of general fund revenues in fiscal 2016, while intergovernmental revenues were approximately 12%. Given the prevalence of locally derived revenues and management's record of producing balanced operating results, we expect that Topsfield will maintain adequate budgetary performance over the next two fiscal years.

Very strong budgetary flexibility

Topsfield's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 16% of operating expenditures, or \$4.2 million.

Topsfield has maintained an available fund balance in excess of 15% of expenditures in each of the past three fiscal years. Management does not expect to draw down on fund balance in the foreseeable future. While it has a target of \$750,000 for certified free cash, it does not have a formal or informal target for unassigned or assigned general funds. Town management aims for \$600,000, or approximately 2.3% of fiscal 2016 expenditures, in unused levy capacity each year, increasing budgetary flexibility. We expect that Topsfield's available fund balance will remain very strong, given management's budgetary planning and history of maintaining very strong reserves.

Very strong liquidity

In our opinion, Topsfield's liquidity is very strong, with total government available cash at 35.0% of total governmental fund expenditures and 18.5x governmental debt service in 2016. In our view, the town has strong access to external liquidity if necessary.

Topsfield is a regular market participant that has issued debt frequently over the past several years. 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 over the next two years.

Strong debt and contingent liability profile

In our view, Topsfield's debt and contingent liability profile is strong. Total governmental fund debt service is 1.9% of total governmental fund expenditures, and net direct debt is 56.2% of total governmental fund revenue. Overall net debt is low at 1.5% of market value, which is, in our view, a positive credit factor. Negatively affecting our view of the town's debt profile are its significant medium-term debt plans.

Following this issuance, the town will have approximately \$16.2 million in net direct debt, which includes \$9.5 million in BANs. We removed from the debt total \$610,000 in water enterprise debt, which is fully self-supporting through user fees. Management anticipates that in the next two years, Topsfield will issue \$4 million in debt for a water treatment project, which it expects will be supported by user charges, as well as \$5 million for a school roofing project.

Topsfield's combined required pension and actual other postemployment benefit (OPEB) contributions totaled 4.9% of total governmental fund expenditures in 2016. Of that amount, 3.2% represented required contributions to pension obligations, and 1.7% represented OPEB payments. The town made 100% of its annual required pension contribution in 2016.

The town provides pension benefits to eligible employees through the Essex Regional Retirement system, a cost-sharing multiemployer defined-benefit pension system. For the Jan. 1, 2014 valuation, using an 8.0% discount rate, the town had a proportionate net pension liability of \$12.5 million. This discount rate will be reduced for the next valuation, which management anticipates will add approximately \$1 million to the net pension liability. Topsfield has paid its actuarially determined contribution (ADC) each of the past three fiscal years and anticipates continuing to do so.

Topsfield also provides OPEBs 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 July 1, 2015 valuation, the trust had an actuarial value of approximately \$343,000. The unfunded actuarial accrued liability is \$18 million. While the town does not have a funding schedule for the unfunded liability, management budgets for a \$100,000 transfer into the trust annually.

While the town expects to add debt within the next two years, we do not anticipate significant budgetary pressure from the additional debt burden. Additionally, while 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. While it is unlikely that the OPEB trust will meaningfully reduce the OPEB liability over the next several years, we expect pay-as-you-go OPEB costs to pressure 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 management team, supported by very strong wealth and income levels, will continue to produce balanced operating results. We do not expect to change the rating within our two-year outlook horizon.

Upside scenario

We could raise the rating if Topsfield's management continues to update the documents produced in conjunction with the Collins Center, leading to increased budgetary performance and reserves, while managing growth and capital-related pressures on the town's budget.

Downside scenario

We could lower the rating if budgetary performance were to weaken, straining reserves.

Related Criteria And 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

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 for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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