

RatingsDirect®

Summary:

Topsfield, Massachusetts; General Obligation

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Credit Profile

US\$3.5 mil GO wtr bnds ser 2018 due 10/15/2038

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

<i>Long Term Rating</i>	AA+/Stable	Affirmed
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Topsfield Internal/confidential credit estimate

<i>Long Term Rating</i>	AA+/Stable	Affirmed
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Rationale

S&P Global Ratings assigned its 'AA+' long-term and underlying rating to the Town of Topsfield, Mass.'s general obligation (GO) water bonds. At the same time, S&P Global Ratings affirmed its 'AA+' long-term rating on the town's GO debt outstanding. The outlook is stable.

The rating reflects our view of the town's anticipated budgetary surplus in fiscal 2018 and our expectation it will continue to balance results over the near term, while at the same time managing increasing carrying charges associated with its long-term liabilities.

The town's full faith and credit pledge secures the bonds. The 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. We also note that based on the expected payment of debt service through water revenues, the debt does not count towards the town's Proposition 2-1/2 debt cap.

Bond proceeds will be used for a water treatment plant project. 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 treatment facility project through its water enterprise fund.

The long-term rating further reflects Topsfield's:

- 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 a slight operating surplus in the general fund and an operating surplus at the total governmental fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 17% of operating expenditures;
- Very strong liquidity, with total government available cash at 61.1% of total governmental fund expenditures and

31.2x governmental debt service, and access to external liquidity we consider strong;

- Strong debt and contingent liability profile, with debt service carrying charges at 2.0% of expenditures and net direct debt that is 101.0% 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 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 \$211,501. Overall, the town's market value grew by 4.9% over the past year to \$1.4 billion in 2018. The county unemployment rate was 3.8% in 2017.

The town is mainly residential and serves as a commuter suburb to Boston; however, it maintains a small commercial and industrial base, representing approximately 4.5% and 1.4% 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.

In addition, 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, the town has experienced some recent development, including a new, 30-unit, age 55-plus housing project. Management also notes that there is interest in redeveloping several commercial properties and continued residential investment, including along Perkins Row, an underdeveloped portion within town borders. Building permit revenues reflect associated commercial and residential development in fiscal 2017, with physical assets to come online in the near term.

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 the five-year plan the town had used in years past. In addition, Topsfield enhanced 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. Topsfield follows state law on investments, and formally presents performance updates at yearend. It has a draft debt

management policy and while the town does not have a formalized target for general fund reserves, it does maintain targets for annual certified free cash (\$750,000) and the stabilization reserve fund (\$1 million), as well as targets for various other reserve funds, such as compensated absences. Topsfield is reviewing these policies, with the discussion moving to the finance committee and board of selectmen over the next month.

Strong budgetary performance

Topsfield's budgetary performance is strong, in our opinion. The town had slight surplus operating results in the general fund of 0.6% of expenditures, and surplus results across all governmental funds of 3.2% in fiscal 2017. General fund operating results have been stable over the past three years, with a result of 0.6% in 2016 and a result of 1.2% in 2015.

Topsfield continues to post operating surpluses, after regular transfers out for capital and its other postemployment benefits (OPEB) trust, which we include in our assessment of results given their recurring nature. 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. Local property taxes accounted for approximately 77% of general fund revenues in fiscal 2017, 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.

The town expects another surplus in fiscal 2018, with positive variance among all major line items, including building permit, fine, and other non-property tax revenues. The surplus includes a one-time \$500,000 for acquired land and deposits into its stabilization and capital stabilization fund. The town's 2019 budget is balanced and increased the expected appropriation into the town's OPEB trust to \$300,000, from \$100,000 in recent years. Year-to-date results do not show any substantial variance among revenue and expense line items that could negatively affect our view of performance in the coming year.

Very strong budgetary flexibility

Topsfield's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 17% of operating expenditures, or \$4.6 million. Over the past three years, the total available fund balance has remained consistent overall, totaling 16% of expenditures in 2016 and 16% in 2015.

The town has conservatively managed to sustain operating surpluses 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 61.1% of total governmental fund expenditures and 31.2x governmental debt service in 2017. 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. 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 2.0% of total governmental fund expenditures, and net direct debt is 101.0% of total governmental fund revenue. Overall net debt is low at 2.4% of market value, which is, in our view, a positive credit factor.

After the current issuance, almost 80% of the town's debt outstanding will be bond anticipation notes. Based on our discussions with management, our analysis assumes the notes will be permanently financed over the next two fiscal years with a 25-year amortization period for \$6 million associated with the town hall reconstruction and a 20-year takeout for the remainder. These assumptions result in a 10-year amortization of just less than 50%, which we consider average. The town's water enterprise debt is fully self-supporting and we expect future issuance to permanently finance notes will also be self-supporting.

Topsfield's combined required pension and actual OPEB contributions totaled 5.5% of total governmental fund expenditures in 2017. Of that amount, 3.5% represented required contributions to pension obligations, and 2.0% represented OPEB payments. The town made 100% of its annual required pension contribution in 2017.

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, 2016 valuation, using a 7.75% discount rate, down from 8% in the 2014 valuation, it had a proportionate net pension liability of \$13.6 million. Topsfield has paid its actuarially determined contribution (ADC) in each of the past three 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 this figure to be closer to \$1 million as of Sept 1, 2018. The unfunded actuarial accrued liability is \$14.6 million as of June 30, 2017. 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. While the town does not have a funding schedule for the unfunded liability, management has budgeted for a \$100,000 transfer into the trust annually in the past and increased this amount to \$300,000 in fiscal 2019.

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 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 its practices and policies produced in conjunction with the Collins Center, demonstrating its commitment to balanced budgetary performance and reserves, while managing expense growth and budgetary pressure associated with its long-term liabilities.

Downside scenario

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

Related Research

- 2017 Update Of Institutional Framework For U.S. Local Governments
- 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

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