

# RatingsDirect®

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## Groton Town, Massachusetts; General Obligation

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## Summary:

# Groton Town, Massachusetts; General Obligation

### Credit Profile

US\$7.765 mil GO mun purp loan of 2018 bnds due 11/15/2039

<i>Long Term Rating</i>	AAA/Stable	New
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Groton Twn GO rfdg bnds

<i>Long Term Rating</i>	AAA/Stable	Affirmed
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#### **Groton Twn GO**

<i>Unenhanced Rating</i>	AAA(SPUR)/Stable	Affirmed
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Many issues are enhanced by bond insurance.

## Rationale

S&P Global ratings assigned its 'AAA' long-term rating to Groton Town, Mass. series 2018 general obligation (GO) municipal-purpose loan bonds. At the same time, we affirmed our 'AAA' rating on the town's outstanding GO debt. The outlook is stable.

The town's full-faith-and-credit pledge, subject to limitations of Proposition 2-1/2, secures the series 2018 GO bonds. However, we note that the town voted to exempt a portion of the series 2018 bonds from Proposition 2-1/2 levy limitations. Despite limitations imposed by the commonwealth levy limit law on a portion of the bonds, we did not make a rating distinction between the limited-tax GO pledge and Groton's general creditworthiness because the tax limitation imposed on the town's ability to raise revenue and the fungibility of those resources is already embedded in our analysis of its financial and economic conditions.

Groton's GO debt is eligible to be rated above the sovereign because we believe the town can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), Groton has a predominantly locally derived revenue source, with approximately 86.5% of general fund revenue coming from property taxes. The town also has independent taxing authority and independent treasury management from the federal government.

We understand that town officials intend to use proceeds from the bonds to permanently finance various capital improvement projects.

The long-term rating reflects Groton's comprehensive budget development process and emphasis on long-term capital and financial planning, which continues to yield consistent and positive budgetary performance and maintenance of strong budgetary flexibility. At the same time, we believe its pension and OPEB cost profile will remain a fiscal pressure over the long-term, which could compel Groton to make more challenging budget adjustments to realize balanced operations under more constrained economic and fiscal conditions. However, we view management's tight

control of operating expenditures and the town's forecast for favorable local tax base growth trends to continue that will likely support its capacity to raise revenue that alleviates potential increases to retirement cost pressures beyond the outlook period. Therefore, we do not expect Groton's overall credit quality to diminish in the near term.

The rating reflects our opinion of the following factors for Groton, specifically its:

- 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 slight operating surpluses in the general fund and at the total governmental fund level in fiscal 2017;
- Strong budgetary flexibility, with an available fund balance in fiscal 2017 of 14.3% of operating expenditures;
- Very strong liquidity, with total government available cash at 48.1% of total governmental fund expenditures and 10.3x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability position, with debt service carrying charges at 4.7% of expenditures and net direct debt that is 48.5% 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 Groton's economy very strong. The 32 square-mile town, with an estimated population of 11,603, is located in Middlesex County in the Boston-Cambridge-Newton MSA, which we consider broad and diverse. The town has a projected per capita effective buying income of 170% of the national level and per capita market value of \$143,767. Overall, the town's market value grew by 0.8% over the past year to \$1.7 billion in 2018. The county unemployment rate was 3% in 2017.

Groton is a primarily residential community approximately 18 miles west from Lowell and 42 miles northwest from Boston. While many residents commute to nearby regional employment centers, including Lowell and Boston, as well as southern New Hampshire, management reports ongoing residential and commercial development in Groton. The local economic base features employers in government, health care, education, business and commercial services, and commercial retail. The town's leading employers are Deluxe Forms (600 employees); the Groton-Dunstable Regional School District (430); Hollingsworth and Vose (235) and Seven Hills Hospital (180).

Residential property makes up 94% of total assessed value (AV), while commercial and industrial combined account for about 4.5% of total taxable AV. The town has seen modest annual increases in total AV over the past three years, reaching \$1.7 billion in 2018. Management anticipates that residential developers plan to build new single-family and town home residences throughout the community. In addition, one developer has submitted preliminary plans to construct 90 new apartment units. Town officials also indicate that several commercial projects are in various stages of planning and construction. Notably, the Groton Inn—a historic hotel that was closed following a fire in 2011—has undergone redevelopment into a hotel and restaurant. The Groton Inn project is completed and has become one of the town's leading employers and taxpayers.

Due to Groton's stable and primarily residential tax base, in conjunction with new development and access to a broad and diverse Boston MSA, we expect the economy to remain very strong through the two-year outlook period.

### **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.

Key budget development and monitoring practices are set forth in the town charter, and include Groton's use of three years of historical data to build annual revenue and expenditure assumptions. In preparation of its annual budget, management works alongside department managers to review annual operation requests and prioritize operating expenditures. Finance officials closely monitor tax base growth to estimate changes in local tax revenue and the tax rate. During each fiscal year, Groton monitors the budget regularly, reporting budget-to-actual results to the board of finance and Board of Selectmen quarterly. Furthermore, Groton maintains a formal investment policy that adheres to state statutes governing investments and officials report earnings and holdings quarterly.

In accordance with its town charter, Groton also maintains a strong focus on long-term capital planning, evidenced by a five-year capital improvement plan (CIP) that identifies projects and costs across all departments. The town updates its CIP annually and details pay-as-you-go funding and bond financing of all capital projects. Groton also develops a comprehensive five-year financial forecast in its budget development process, which features a sensitivity analysis of key revenue and expenditure assumptions, which allows the town to manage decisions and changes related to future operations, capital projects, and debt service.

Furthermore, management has historically met and sustained reserves in accordance with its fund balance policy. The formal policy calls for its general fund stabilization balance to be maintained at a minimum of 5% of annual operating expenditures. The policy indicates that this minimum reserve target assists with managing cash flows in the event of a revenue shortfall and unexpected changes in expenditures. The town also adopted a formal debt management policy that sets forth guidelines for issuing debt and measurable debt affordability benchmarks. The policy limits annual debt service to 5% or less of operating expenditures.

### **Strong budgetary performance**

Groton's budgetary performance is strong in our opinion. The town had slight operating surpluses of 0.7% of expenditures in the general fund and of 0.5% across all governmental funds in fiscal 2017. Our analysis accounts for net transfers in to the general fund from other government funds, and adjusts for capital expenditures paid with bond proceeds.

We expect Groton to maintain strong budgetary performance over the next several years, largely due to its comprehensive budgeting development and monitoring framework, coupled with its manageable expenditure and fixed-cost profile. Furthermore, the town benefits from an overall stable and strong property and motor vehicle excise tax base, which generated a combined 91.8% of general fund revenue in fiscal 2017. In addition, tax collections have remained strong with collections exceeding 98.3% over the past five years. Intergovernmental (state) sources represent the second-highest share of general fund revenue at 2.6%, while charges for services constitute about 1.6%. We note that favorable local and state economic environment has supported steady and predictable performance among these primary revenue sources over the last several years.

Net of operating adjustments, Groton reported positive year-end general fund performance for fiscal 2017, which management attributed to better-than-budgeted property and excise tax receipts, as well as licenses, fees, and other departmental revenue. At the same time, the town recognized cost savings, totaling \$1.29 million from unexpended department appropriations from its general government, public safety, and employee benefit line items due to tight control of these expenditures throughout the fiscal year.

Groton approved a balanced \$36.99 million general fund budget for fiscal 2018, which reflects a 4.9% increase over the prior fiscal year. While the town budgeted for higher costs related to adjustments for salary, benefits, and debt service, management built conservatively local revenue projections and implemented various measures to control expenditures that officials expect will outperform the budget at fiscal year-end. Based on unaudited year-end results for June 30, 2018, the town conservatively estimates to realize a \$2.2 million operating surplus.

Furthermore, Groton adopted a nearly \$38.25 million operating budget for fiscal 2019. We note that the town settled contracts with its seven collective bargaining units through 2021, and management indicates that these contracts will not have a substantial impact on future budgets, which reduces a potential area of cost uncertainty. Although early in the current budget year, officials generally expect local revenues to outperform the budget, and the town will continue to identify and adjust expenditures as necessary to produce at least balanced results at fiscal year-end. Therefore, we believe Groton is likely to maintain stable and strong performance over our two-year outlook period.

### **Strong budgetary flexibility**

Groton's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2017 of 14.3% of operating expenditures, or \$5 million.

In accordance with its town charter, its formal reserve policy stipulates that the town maintain a general fund stabilization reserve minimum of at least 5% of current year operating expenditures. Although we do not incorporate additional reserves into our calculation of the town's flexibility, we note that Groton maintains a Municipal Capital Stabilization reserve at 1.5% of the current town budget and an Excess and Deficiency (E&D) reserve fund minimum of 1% of the current town budget. Groton has historically built and sustained reserves in excess of these amounts.

Due to strong and positive budgetary performance over the past three fiscal years, Groton improved its reserve position to approximately \$5 million from \$3.6 million in fiscal 2015. Based on management's expectation that the town will maintain positive operating performance in fiscal 2018, and at least balanced operations for fiscal 2019, we do not expect its very strong overall flexibility position to deteriorate over the next two years.

### **Very strong liquidity**

In our opinion, Groton's liquidity is very strong, with total government available cash at 48.1% of total governmental fund expenditures and 10.3x governmental debt service in 2017. In our view, the town has strong access to external liquidity if necessary.

Groton is a regular market participant that has issued debt frequently over the past 20 years, including GO bonds and short-term BANs. The town has no variable-rate or direct-purchase debt, and management has confirmed it has no contingent liquidity risks from financial instruments with payment provisions that change on the occurrence of certain events. Town investments are subject to commonwealth laws, and Groton invests its cash in low-risk assets with

original maturities of one year or less, including the Massachusetts Municipal Depository Trust, money markets, and short-term certificates of deposit. For these reasons, the town's available cash position remains strong and stable, and we expect its liquidity profile to remain very strong over the next two years.

### **Very strong debt and contingent liability profile**

In our view, Groton's debt and contingent liability profile is very strong. Total governmental fund debt service is 4.7% of total governmental fund expenditures, and net direct debt is 48.5% 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.

After this issuance, Groton will have \$21.95 million of total direct debt outstanding, of which \$1.1 million are short-term notes. In addition, its proportionate share of overlapping debt is \$7.2 million related to Groton-Dunstable Regional School District and other overlapping entities. As outlined in its capital improvement plan, the town could issue about \$5 million in additional debt over the next two years to finance a new senior center and approximately \$1.8 million in pay-as-you-go capital financing. Given its low overall net debt ratios, however, we do not expect our assessment of its debt profile to weaken.

Groton's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 6.1% of total governmental fund expenditures in 2017. Of that amount, 5% represented required contributions to pension obligations, and 1.1% represented OPEB payments. The town made its full annual required pension contribution in 2017.

Groton participates in the Middlesex County Retirement System, a cost-sharing, multiple-employer, defined-benefit plan. Based on the last actuarial valuation (Dec. 31, 2016), the town's proportionate share of the net pension liability was \$21.9 million (using a discount rate of 7.75%). The retirement plan's fund ratio was 45.5% as of Dec. 31, 2016. According to officials, the town expects to make its full contractually required contributions over the next two years, as it has historically done. While we view the plan's discount rate to be high relative to national averages and its funding ratio as very low, we do not view these costs as a near-term credit pressure as the town demonstrates significant capacity to absorb increases to these fixed costs.

However, management notes that the system has a plan in place to decrease the discount rate at regular intervals; it was adjusted to 7.75% (from 7.857%) in the most recent actuarial valuation. A decrease in the discount rate assumption could increase Groton outstanding liability and the annual required contribution. Although the town is estimating an increase in the pension contribution for the current budget year, we will continue to monitor if potential changes to the overall liability or annual contributions begin to pressure the operating budget.

The town also offers OPEBs to retirees and has contributed \$414,059, or 39% of its annual OPEB contribution. It began funding an OPEB trust in 2013 to address future OPEB liabilities. According to the board's formal policy, after the pension liability is funded fully in 2035, the town plans to contribute the savings from the lower pension assessment to pay toward the OPEB trust account. As of July 1, 2018, the town had a net OPEB liability of nearly \$9.93 million. Similar to its pensions, we believe the town's OPEB costs are currently manageable; however, should costs increase and pressure the budget, we could revise our view of its OPEB liability.

## **Strong institutional framework**

The institutional framework score for Massachusetts municipalities is strong.

## **Outlook**

The stable outlook reflects S&P Global Ratings' expectation that Groton's will sustain very strong economic metrics and management conditions that have contributed to stable and overall predictable budgetary performance over the last three years. As a result, we believe Groton will likely maintain its very strong flexibility and liquidity that stabilizes its financial profile. Over the next two years, steady economic development should continue to support steady tax base growth and provide additional future tax revenue, which will likely ensure a stable budgetary environment. For these reasons, we do not expect to change the rating within the two-year outlook horizon.

However, if budgetary performance were to deteriorate—due to pressure from growing fixed costs or otherwise—leading to a significant deterioration in reserves or liquidity, 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

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 column.

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