

RatingsDirect®

Summary:

Sharon, Massachusetts; General Obligation

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Credit Profile

US\$97.86 mil GO mun purpose loan of 2020 bnds due 02/15/2040

Long Term Rating AA/Stable New

Sharon GO

Long Term Rating AA/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AA' rating to Sharon, Mass.' series 2020 general obligation (GO) municipal-purpose loan bonds and affirmed its 'AA' rating on the town's existing debt. The outlook is stable.

Security and use of proceeds

The town's full-faith-and-credit pledge secures the bonds, subject to limitations of Proposition 2-1/2. We rate the limited-tax GO debt on par with our view of Sharon's general creditworthiness, since the ad valorem tax is not derived from a measurably narrower tax base and there are no limitations on the fungibility of resources, which supports our view of the town's overall ability and willingness to pay debt service. Officials plan to use proceeds to fund a new high school and related facilities, a library, and other capital projects and equipment acquisitions. Concurrent with this issuance, the town is also issuing a bond anticipation note (BAN) that we have not been asked to rate.

Credit overview

Sharon is a primarily residential community south of Boston. The town's well-embedded and robust financial management policies and practices have consistently led to predictable and generally positive year-end budgetary variances and positive results on a GAAP basis. We believe the town's large unfunded retirement liabilities and rising debt burden could pressure the budget over the long term, but expect that management will continue to adjust its budget to incorporate these costs.

The long-term rating reflects our view of the following factors for the town:

- 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 an operating surplus in the general fund and a slight operating surplus at the total governmental fund level in fiscal 2019;
- Strong budgetary flexibility, with an available fund balance in fiscal 2019 of 8.9% of operating expenditures;
- Very strong liquidity, with total government available cash at 16.9% of total governmental fund expenditures and 202.3% of governmental debt service, and access to external liquidity we consider strong;
- Very weak debt and contingent liability position, with debt service carrying charges at 8.3% of expenditures and net

direct debt that is 157.4% of total governmental fund revenue, as well as a large pension and other postemployment benefit (OPEB) obligation; and

- Strong institutional framework score.

Very strong economy

We consider Sharon's economy very strong. The town, with a population of 18,163, is an affluent suburban community about 20 miles south of downtown Boston in Norfolk 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 204% of the national level and per capita market value of \$201,460. Overall, market value grew by 5.1% over the past year to \$3.7 billion in 2020. The county unemployment rate was 3.0% in 2018.

Residents benefit from a robust transportation infrastructure that includes convenient highway access to the Route 128 and Interstate 495 corridor and a Massachusetts Bay Transit Authority commuter rail stop in downtown Sharon with direct travel to Boston and Providence, R.I. The town's property tax base continues to grow, primarily reflecting growth in the residential base, which accounts for 93% of total assessed value (AV).

While primarily residential, management notes several commercial developments that will add to the tax base. The town permitted a retail marijuana shop, which will also sell wholesale to other facilities in Massachusetts. In addition to the excise tax, the town will receive funds through a host agreement. Additionally, a shopping plaza has a new owner and is proposing a new development in the existing parking lot. Two solar installations on leased town property will also generate additional revenue.

Due to growth in AV over the past three fiscal years and with new development ongoing, we expect the town's economy will likely remain very strong.

Strong management

We view the town's management as strong, with good financial policies and practices under our FMA methodology, indicating financial policies and practices exist in most areas, but that governance officials have not formalized or may not monitor some of the policies or practices within the methodology.

The town uses three years of revenue and trend data when developing the budget, and we believe it is generally conservative in its budgetary assumptions. Budget-to-actual and investment results are reported quarterly to the board. Management annually updates a formal five-year capital improvement plan that identifies funding sources and which we believe is well incorporated into the budgeting process. The town's formal investment and reserve policy limits unassigned fund balance to 5%-10% of general fund revenue, and it has adhered to this policy historically. There is no formal multiyear financial plan or debt-management policy aside from management's target of maintaining debt service below 5% of expenditures.

Strong budgetary performance

Sharon's budgetary performance is strong, in our opinion. The town had surplus operating results in the general fund of 2.3% of expenditures, and slight surplus results across all governmental funds of 1.1% in fiscal 2019. General fund operating results of the town have been stable over the last three years, with results of 1.0% in 2018 and 2.1% in 2017.

We adjusted the town's budgetary performance to account for recurring transfers into and out of the general fund, as well as for the expenditure of bond proceeds across total governmental funds. Revenues and expenditures across categories incrementally added to positive budgetary variances and generated the positive year-end operating result.

Fiscal 2020 budgeted operating expenditures total \$85.1 million, a 2.7% increase from 2019. Management's budget-to-actual monitoring shows similar variances to 2019, and the town expects to have at least break-even operations at year-end. Management notes that it has worked to right-size through retirements and attrition, and believes the town currently has generally sustainable personnel costs. It identified growing school enrollment as a potential long-term pressure, but at present expects to be able to fully absorb any increasing costs.

We expect the town's budgetary performance to remain strong, in part due to the stable revenue and expenditure profiles. Property taxes accounted for 75% of 2019 general fund audited revenue, followed by intergovernmental revenue at 18% and excise taxes at about 3%. Tax collections have been strong, with current collections exceeding 99% in each of the past three years.

Strong budgetary flexibility

Sharon's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2019 of 8.9% of operating expenditures, or \$7.9 million.

Following a planned drawdown in fiscal 2018 for the high school feasibility study, the town's available reserves rebounded in 2019 due to the strong general fund budgetary performance. We understand it does not have additional plans to use reserves or significantly add to them, and we consequently expect budgetary flexibility to remain strong.

Sharon also maintains about \$2 million in unused levy capacity that equates to about 2.3% of fiscal 2019 budgeted expenditures. We understand that management intends to maintain the current levy capacity through the budgeting process.

Very strong liquidity

In our opinion, Sharon's liquidity is very strong, with total government available cash at 16.9% of total governmental fund expenditures and 202.3% of governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

In our view of the town's liquidity, we excluded cash we believe is restricted, but included general fund investments. We believe the town has strong access to external liquidity, as evidenced by regular GO debt issuances. Sharon does not have any variable-rate or direct-purchase debt. Most of the town's investments are in certificates of deposit, U.S. treasury obligations, and government agencies. We expect liquidity to remain very strong.

Very weak debt and contingent liability profile

In our view, Sharon's debt and contingent liability profile is very weak. Total governmental fund debt service is 8.3% of total governmental fund expenditures, and net direct debt is 157.4% of total governmental fund revenue.

Following this issuance, the town has approximately \$171 million in total direct debt, of which we consider about \$2.6 million to be self-supporting enterprise debt, based on coverage in the three most recent fiscal years. The town also expects to receive approximately \$3.8 million in subsidies from the state.

We understand that the town could issue an additional \$20 million-\$25 million over the next few years to close out its school and library projects, along with about \$2 million annually for capital projects. We do not expect this to have a material effect on our view of its debt profile.

In our opinion, a credit weakness is Sharon's large pension and OPEB obligation. Sharon's combined required pension and actual OPEB contributions totaled 6.0% of total governmental fund expenditures in 2019. Of that amount, 4.0% represented required contributions to pension obligations, and 2.0% represented OPEB payments. The town made its full annual required pension contribution in 2019. The funded ratio of the largest pension plan is 58.4%.

Pension and other postemployment benefits

- In our opinion, a credit weakness is Sharon's large pension and OPEB obligation. Despite costs declining as a percentage of expenditures relative to 2018, we believe the low pension funded ratio, permissive assumptions, and large OPEB liability collectively result in a liability profile likely to pressure the operating budget, particularly if assumptions are not met.
- While the use of an actuarially determined contribution (ADC) is a positive, we believe some of the assumptions used to build the pension ADC reflect what we view as slightly weak assumptions and methodologies, which we believe increases the risk of unexpected contribution escalations.
- The town funds OPEB liabilities on a pay-as-you-go basis, although it is prefunding the obligation. It has a net OPEB liability of \$84.8 million, and the trust is 1.1% funded, as of June 30, 2019.

As of June 30, 2019, the town participates in the following pension plan:

- Norfolk County Retirement System: 50.4% funded with a \$52.8 million proportionate share of the net pension liability.

Sharon's combined required pension and actual OPEB contributions totaled 6.0% of total governmental fund expenditures in 2019. Of that amount, 4.0% represented required contributions to pension obligations, and 2.0% represented OPEB payments. The town's actual OPEB contribution declined by nearly a third, or \$914,000, from 2018 to 2019, helping reduce the total cost and as a percentage of expenditures, as the pension contribution increased \$357,000, and total expenditures grew.

The Norfolk County Retirement System is a cost-sharing, multiple-employer system. We believe the discount rate remains high at 7.75%, along with permissible mortality tables, and optimistic payroll growth assumptions. The system made progress in both our static and minimum funding progress calculations, indicating it addressed both the current costs and unfunded liabilities. The system's closed, nine-year amortization schedule is a positive, leading to full funding ahead of the state's 2040 pension funding deadline. However, we believe that to meet this timeline, the system maintains assumptions we view as more likely to lead to contribution volatility.

We believe pension and OPEB costs are currently manageable, but the total outstanding liability and funding assumptions are likely to lead to contribution volatility and increasing costs. If costs remain low and the pension system were to adopt increasingly conservative assumptions, along with the town making material progress in funding its OPEB liability, our view of the town's retirement profile could improve.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion of Sharon's very strong economy with access to the Boston MSA, and stable financial operations with strong management conditions. We believe the town's unfunded retirement liabilities could pressure its finances over the longer term. We do not expect to change the rating within the two-year outlook horizon.

Upside scenario

Should the town significantly improve reserve levels through positive financial performance to help offset what we view as large unfunded pension and OPEB liabilities, or if it significantly reduced the unfunded retirement liabilities, we could raise the rating.

Downside scenario

If available reserves were to weaken due to negative financial performance with no plan to correct and restore fund balance, we could lower the rating.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019

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