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## Summary:

# Brockton, Massachusetts; General Obligation; Non-School State Programs; Note

**Primary Credit Analyst:**
Christina Marin, Boston 617-530-8312; christina.marin@spglobal.com

**Secondary Contact:**
Victor M Medeiros, Boston (1) 617-530-8305; victor.medeiros@spglobal.com

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| Credit Profile | | |
|---|---|---|
| US$11.568 mil GO BANs ser 2017 dtd 06/07/2017 due 06/29/2018 | | |
| *Short Term Rating* | SP-1+ | New |
| Brockton GO muni purp loan of 2014 bnds due 08/15/2034 | | |
| *Long Term Rating* | AA-/Stable | Affirmed |
| Brockton GO st qual rfdg bnds | | |
| *Long Term Rating* | AA/Negative | Affirmed |
| *Underlying Rating for Credit Program* | AA-/Stable | Affirmed |
| **Brockton GO** | | |
| *Unenhanced Rating* | AA-(SPUR)/Stable | Affirmed |

Many issues are enhanced by bond insurance.

## Rationale

S&P Global Ratings assigned its 'SP-1+' short-term rating to the City of Brockton, Mass.'s bond anticipation notes (BANs). The short-term rating reflects our view that Brockton maintains a very strong capacity to pay principal and interest when the notes come due. The city maintains what we view as a low market risk profile because it has strong legal authority to issue long-term debt to take out the notes and is a frequent issuer that regularly provides ongoing disclosure to market participants.

At the same time, we affirmed our 'AA-' underlying rating on the city's general obligation (GO) bonds outstanding. We recently revised the outlook on the underlying rating to stable from positive, reflecting Brockton's return to positive operating results in fiscal years 2015 and 2016, following several years of negative operations and declining reserves. While we recognize that the city's budgetary environment remains challenged, Brockton's economy has seen some new growth that has aided revenues. Furthermore, management has demonstrated the ability to make the needed expenditure adjustments to avoid prolonged fiscal imbalances. While we do anticipate rising service level or pension and other postemployment benefit (OPEB) costs to challenge budgetary operations, we note that a recent decision by one of the city's largest departments to substantially reduce staffing levels, underscores management's overall capacity and willingness to align spending and ongoing revenues long term without substantially reducing reserves.

S&P Global Ratings also affirmed its 'AA' long-term rating, and negative outlook, on certain state qualified bonds. The long-term rating on the bonds supported by the Commonwealth of Massachusetts qualified bond program moves in tandem with the long-term GO rating on the commonwealth. The outlook on the program rating is negative, reflecting a decline in reserves at the state level.

The city's full-faith-and-credit pledge, subject to limitations of Proposition 2 1/2, secures the BANs and bonds outstanding. Despite limitations imposed by the commonwealth levy limit law, we did not make a rating distinction for the limited-tax GO pledge due to Brockton's flexibility under the levy limit.

The long-term rating reflects what we view as Brockton's:

- Adequate economy, with projected per capita effective buying income at 77.9% and market value per capita of $70,781, although that is advantageously gaining from access to a broad and diverse metropolitan statistical area (MSA);
- Adequate management, with "standard" financial policies and practices under our financial management assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could deteriorate in the near term relative to fiscal 2016, which closed with operating surpluses in the general fund and at the total governmental fund level;
- Adequate budgetary flexibility, with an available fund balance in fiscal 2016 of 14.2% of operating expenditures, as well as limited capacity to raise revenues due to consistent and ongoing political resistance;
- Very strong liquidity, with total government available cash at 25.2% of total governmental fund expenditures and 7.6x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability position, with debt service carrying charges at 3.3% of expenditures and net direct debt that is 27.1% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value and rapid amortization, with 80.5% of debt scheduled to be retired in 10 years, but a large pension and OPEB obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

### Adequate economy

We consider Brockton's economy adequate. The city, with an estimated population of 94,497, is located in Plymouth County in the Boston-Cambridge-Newton MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 77.9% of the national level and per capita market value of $70,781. Overall, the city's market value grew by 9.6% over the past year to $6.7 billion in 2017. The county unemployment rate was 3.9% in 2016.

Brockton is 20 miles south of Boston, along State Route 24. The city has what we consider good access to Boston, with three commuter rail stations and access to Interstate 93 and Route 128-Interstate 95. We understand that the city recently launched the Brockton Initiative, with the help of Mass Development and other local real estate investors, to transform the city into a more transit-oriented economic base. Although this plan is in its preliminary stages, we believe that new tax base growth is imperative to Brockton's future economic and financial stability.

The city's leading employers include:

- City of Brockton (2,700 employees);
- Signature Health (2,500); and
- Caritas Good Samaritan Medical Center (1,800).

We believe the city's economic characteristics will remain adequate in the next two years given the modest trends in per capita income and property tax base growth.

### Adequate management

We view the city's management as adequate, with "standard" financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some but not all key areas.

Brockton's strengths, based on our assessment, include conservative revenue and expenditure assumptions demonstrated by positive budget-to-actual variances on an audited basis, and strong oversight in terms of monitoring progress against the budget during the year with detailed spending reports for the first two quarters and every two months thereafter. At the same time, management maintains long-term projections for general fund revenues and expenditures. However, the city lacks formal reserve and liquidity policies, aside from what it is legally restricted to maintain as an emergency reserve, and has no debt management policy or comprehensive long-term capital planning. The city follows state guidelines for its investment policy and reports holdings and earnings annually.

We have observed a political resistance to raising revenues, which has led to a persistent budgetary gap. If city officials are unable to implement a plan to restore structural balance, this would signal a weak management environment.

### Adequate budgetary performance

Brockton's budgetary performance is adequate in our opinion. The city had operating surpluses of 2.6% of expenditures in the general fund and of 2.6% across all governmental funds in fiscal 2016. Our assessment accounts for our expectation that budgetary results could moderate somewhat from 2016 results in the near term.

The city had four consecutive deficits before 2014, but operations have stabilized with positive operating results in the general fund and total governmental funds in 2015 and 2016. Recent operations have been aided by conservative revenue and expenditure estimates. In 2016, revenues outperformed budgetary amounts by $10.6 million, led by increases to local fees and charges and surplus overlay accounts. Expenditures also had a positive variance, driven by lower costs in public safety, and pension and fringe benefits.

For fiscal 2017, the city is estimating similar results to that of previous years, but officials note that budgeting challenges ensue. State revenue growth, particularly as it pertains to schools, is not sufficient enough to cover the increasing service costs. Furthermore, costs associated with pension and OPEB liabilities are becoming an increasing percentage of the budget.

While the city has shown the ability to course correct through sizable teacher layoffs, we expect Brockton's budgetary performance to remain strained. If the city cannot keep expenditures in line with sluggish revenue growth, it could return to deficit operations, prompting us to reconsider our rating. However, given measures taken by management to control costs, we expect our assessment of the city's budgetary performance to remain at least adequate over the next two years.

### Adequate budgetary flexibility

Brockton's budgetary flexibility is adequate, in our view, with an available fund balance in fiscal 2016 of 14.2% of operating expenditures, or $51.4 million. Negatively affecting budgetary flexibility, in our view, is limited capacity to raise revenues due to consistent and ongoing political resistance.

Our calculation above includes the addition of $16.6 million in committed fund balances, which are available for general fund operations.

The city maintains an unused levy capacity nearing $2.8 million that could provide some additional revenues to meet service demands; however, we note there has been political resistance in the past to increasing tax revenues. This has resulted in revenue pressures and a subsequent trend of declining available reserves. Nevertheless, Brockton has shown the ability to avoid persistent budgetary imbalances with the willingness to make budgetary cuts through staff layoffs.

We expect reserves will remain pressured due to the difficult budgeting environment; however, we do not expect sizable draws on reserves over the next few years. The city is expecting to close fiscal 2017 with similar results to past years. Therefore, our assessment of its budgetary flexibility will likely remain adequate over our outlook period.

### Very strong liquidity

In our opinion, Brockton's liquidity is very strong, with total government available cash at 25.2% of total governmental fund expenditures and 7.6x governmental debt service in 2016. In our view, the city has strong access to external liquidity if necessary.

Brockton's liquidity profile is expected to remain very strong because we don't anticipate any significant deterioration of cash balances. Our calculation excludes restricted cash balances in the city's other governmental funds. We believe that Brockton's frequent debt issuances, including GO bonds and BANs, illustrate strong market access and external liquidity. Furthermore, Brockton has consistently maintained very strong liquidity across all city funds; and despite past declines to general fund reserves, liquidity metrics have remained strong in our view.

### Very strong debt and contingent liability profile

In our view, Brockton's debt and contingent liability profile is very strong. Total governmental fund debt service is 3.3% of total governmental fund expenditures, and net direct debt is 27.1% of total governmental fund revenue. Overall net debt is low at 1.8% of market value, and approximately 80.5% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

Brockton has about $192 million in total direct debt; of that amount, we calculate about $66.1 million as self-supporting enterprise debt from water and sewer funds. We understand the city has deferred maintenance and will likely issue new debt for various capital equipment purchases and capital projects. However, we do not expect the size of any new debt offerings to materially weaken the city's current debt metrics.

We note that the city had been embroiled in a $68 million lawsuit with Brockton Power Co. LLC since 2012. The issue was recently resolved by a settlement between the parties, and we understand this will not have a financial impact on the city. We no longer consider this lawsuit to be a speculative contingent liability.

In our opinion, a credit weakness is Brockton's large pension and OPEB obligation, without a plan in place that we think will sufficiently address the obligation. The city's combined required pension and actual OPEB contributions totaled 7.8% of total governmental fund expenditures in 2016. Of that amount, 4.3% represented required contributions to pension obligations, and 3.5% represented OPEB payments. Brockton made its full annual required pension contribution in 2016.

City employees are part of the Brockton Contributory Retirement System, a cost-sharing, multiple-employer defined benefit plan. As of 2016, the plan was funded at a below-average level. The plan's net pension liability totaled $238.4

million. Its net position as a percent of the total pension liability was 59.6%. We note that the discount rate and underlying assumptions are also fairly optimistic. Brockton's investment rate of return is set at 8%, which is now a level above industry standards. This will likely lead to additional pension cost increases because market returns have generally not kept up with underlying assumptions. The city's funding schedule runs through 2033; as such, we anticipate pension cost to escalate at an accelerating pace.

Brockton also provides OPEB to its retirees. It pays this liability on a pay-as-you go basis and the liability is fairly large at $495.5 million. The city has not created a trust fund, nor has it set aside money toward the liability.

Given the size of this liability, we believe costs will continue to increase and over time strain operations. Total fixed charges (debt service, pension, and OPEB costs) represent 11.1% of expenditures. While currently at a relatively low level, we would expect these costs to rise.

### Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

## Outlook

The stable outlook reflects S&P Global Ratings' opinion of Brockton's growing tax base, strong reserve levels, and recent trend of positive operations in 2015 and 2016. The outlook is further supported by the city's ability and willingness to make expenditure reductions. Also supporting the stable rating is the city's very strong liquidity and expectations that cash balances will remain strong. For these reasons, we don't expect to change the rating within our two-year outlook horizon.

### Downside scenario

If the city's financial performance reverts back to weak and budgetary reserves deteriorate as a result, then we could lower the rating.

### Upside scenario

While not anticipated over our outlook horizon, if budgetary performance improves to strong levels, and budgetary concerns associated with pension and OPEB subside, we could raise 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
- 2016 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 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.