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## Summary:

# Canton, Massachusetts; General Obligation

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## Summary:

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### Credit Profile

US\$12.57 mil GO mun purp loan of 2020 bnds dtd 05/20/2020 due 05/15/2045

<i>Long Term Rating</i>	AAA/Stable	New
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Canton GO

<i>Long Term Rating</i>	AAA/Stable	Affirmed
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## Rating Action

S&P Global Ratings assigned its 'AAA' rating and stable outlook to the Town of Canton, Mass.' series 2020 general obligation (GO) municipal-purpose loan bonds (totaling \$12.57 million) and affirmed its 'AAA' rating, with a stable outlook, on the town's existing GO debt.

Canton's full-faith-and-credit pledge, subject to Proposition 2 1/2 limitations, secures the GO debt. Despite commonwealth levy-limit laws, we did not make a rating distinction between the town's limited-tax GO pledge and general creditworthiness because our analysis of Canton's financial and economic conditions already includes the tax limitation imposed on the town's revenue-raising ability.

Under our criteria, "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions," published Nov. 19, 2013, on RatingsDirect, we rate Canton higher than the sovereign because we believe the town can maintain better credit characteristics than the nation in a stress scenario based on its predominantly locally derived revenue base and our view that pledged revenue supporting bond debt service is at limited risk of negative sovereign intervention. In 2019, local property taxes generated 73% of revenue, which demonstrated a lack of dependence on central government revenue.

We understand that proceeds from the 2020 bonds will be used to fund various capital items.

### Credit overview

The rating reflects our view of the town's very strong economy, supported by a wealthy property tax base and high income. In addition, the town's maintenance of very strong budgetary flexibility, with available reserves averaging more than 17% in the past three fiscal years, is due to positive financial performance and strong management, supporting our view of the rating. While the scope of economic and financial challenges posed by the COVID-19 pandemic remains unknown, we believe a prolonged disruption could weaken the town's local economy and potentially impact revenues received from the state. (For more information, see "All U.S. Public Finance Sector Outlooks Are Now Negative," published April 1, 2020, on RatingsDirect.) However, due to strong management conditions and historically consistent positive results, we expect management to make the necessary budgetary adjustments to maintain balanced operations. Although we think retirement liabilities and costs could pressure the long-term budget, we expect management will likely manage these costs appropriately due to its conservative budgeting and active funding of an other postemployment benefits (OPEB) trust fund. Therefore, we do not expect to

change the rating within the outlook period.

The rating further reflects our opinion of the town'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;
- Adequate budgetary performance, with balanced operating results in the general fund and a slight operating surplus at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 19% of operating expenditures;
- Very strong liquidity, with total government available cash at 26.7% of total governmental fund expenditures and 6.6x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability profile, with debt service carrying charges at 4.1% of expenditures and net direct debt that is 47.7% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value and rapid amortization, with 74.2% of debt scheduled to be retired in 10 years, but a large pension and OPEB obligation; and
- Strong institutional framework score.

## Stable Outlook

### Downside scenario

We could lower the rating if finances were to deteriorate significantly or the town were to experience budgetary pressure due to low pension funding, especially given potential market volatility during the current economic recession, leading to a draw down on reserves.

## Credit Opinion

### Very strong economy

We consider Canton's economy very strong. The town, with an estimated population of 23,444, is located in Norfolk 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 175% of the national level and per capita market value of \$223,347. Overall, Canton's market value grew by 5.0% over the past year to \$5.2 billion in 2020. The county unemployment rate was 3.0% in 2018.

Canton is a suburban, primarily residential community 15 miles south of Boston. The town's location along Route 128 and Interstate 95 and two commuter-rail train stations provide local residents with easy access to numerous employment centers, including downtown Boston; the Route 128 high-tech corridor; and Providence, R.I.

Assessed value continues to grow due to a healthy real estate market and ongoing development. Royall Development LLC is completing a new hotel that is expected to open in the fall of 2020 and generate approximately \$500,000 annually in new growth taxes and \$350,000 in hotel excise taxes. Canton Holdings LLC is currently in the process of

redeveloping the former Plymouth Rubber site and creating 304 residential units (16 townhouse units and 288 garden-style units). A 60,000 -square-foot Top Golf development is also under construction. It is estimated that this facility will create up to 500 new jobs, including 125 full-time positions, while generating an estimated \$700,000 in yearly property tax revenue and \$75,000 in meals tax revenue. Canton is also making improvements to the highway system that serves the town and the region. Massachusetts Department of Transportation has committed more than \$20 million to rehabilitate Route 138 from Stoughton to Milton in 2022 and has awarded a \$55 million construction contract to rehabilitate the I-95/ Dedham Street corridor.

In addition, Canton has been actively improving and expanding infrastructure to support new developments and the expansion of its commercial and industrial sectors. Therefore, we expect the town's economy to remain very strong.

The COVID-19 pandemic, in our view, presents an evolving credit risk that could accelerate volatility. We understand that the situation will remain fluid in the short term, and will watch for latent credit stressors for the town, including deterioration in economic and financial performance. Given Canton's stable residential tax base, we believe any economic effects related to COVID-19 will be felt over the long term. (For more information, see "An Already Historic U.S. Downturn Now Looks Even Worse," published April 16, 2020)

### **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.

In developing the budget, the town uses conservative assumptions grounded in historical trend analysis and careful state-aid and local-tax-revenue tracking. Management regularly monitors budgetary performance and presents monthly reports to department heads and the town administrator. Management also performs a five-year budget forecast and communicates the results to department heads. Canton maintains a five-year capital improvement program that identifies funding sources, as well as a reserve target to keep the assigned fund balance above 15% of budgeted expenditures, which the town has adhered to since fiscal 2017. Canton follows the commonwealth's investment policy and monitors and reports investments monthly. It does not have a formal debt policy.

Furthermore, the town has taken steps to mitigate exposure to cyber-related risks, and it has been addressing concerns related to climate change that could directly affect taxable properties. In addition to adopting an energy reduction plan, fuel-efficient vehicle policy, and a municipal vulnerability preparedness plan, the town has also made several changes to zoning bylaws and subdivision rules and regulations to enable and encourage low-impact development and "green" infrastructure storm water solutions. Canton has also been awarded a grant from the Municipal Vulnerability Preparedness grant program to do a hydrological study of the town's storm water infrastructure and flood prone areas to come up with targeted solutions and public outreach and education programs. Finally, Canton is home to the Southern Sky Renewable solar facility, one of the largest solar photovoltaic facilities in Massachusetts. It was installed in 2012 and currently a minimum of 31% of the town's electrical consumption is offset by this facility.

### **Adequate budgetary performance**

Canton's budgetary performance is adequate in our opinion. The town had balanced operating results in the general fund of 0.4% of expenditures, and slight surplus results across all governmental funds of 1.0% in fiscal 2019. General

fund operating results of the town have been stable over the last three years, with a result of 2.0% in 2018 and a result of 2.4% in 2017.

Fiscal 2019 results include adjustments for one-time capital expenditures paid for with bond proceeds. According to management, the fiscal 2019 positive performance was primarily due to overall conservative budgeting that led to higher-than-anticipated revenues. Some of these better performing revenue items included motor vehicle excise taxes, tax titles, and property taxes.

The town's fiscal 2020 budget totals \$100.1 million, which represents a 2.7% increase over the previous year. Officials indicate budget-to-actuals are tracking favorably and they do not expect any major revenue and expenditure changes for the remainder of fiscal 2020 due to COVID-19. Officials indicate that they have halted projects and that current COVID-19-related costs remain very small. In addition, the finance committee has a \$700,000 operational reserve fund that can be used to absorb any unexpected pandemic-related expenses. Officials do not currently expect any major delinquencies from the last set of property tax revenue and pushed the collection period to June from May; the town collects these revenues quarterly.

Looking ahead, while Canton has not yet completed its fiscal 2021 budget, which it is in the process of doing, we do not anticipate a significant change in its revenue or expense profile. Officials indicate that they are considering a reduction in expenditures due to COVID-19 impacts. In addition, town officials are developing a more aggressive spending reduction option should there be any changes to the already proposed fiscal 2021 state aid levels.

The town's stable revenue profile is predictable with property taxes accounting for 72.8% of general fund revenue followed by intergovernmental revenue at 17.7%. Therefore, we expect budgetary performance will likely remain strong.

### **Very strong budgetary flexibility**

Canton's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 19% of operating expenditures, or \$19.2 million. Over the past three years, the total available fund balance has remained at a consistent level overall, totaling 19% of expenditures in 2018 and 18% in 2017.

The town has consistently maintained very strong reserves over the past three years. Although management indicates Canton may use about \$1.2 million in free cash reserves by fiscal year-end 2020 to fund the school special education reserve and for capital purposes, we expect its budgetary flexibility to remain very strong. In addition, the town has a reserve target of maintaining its unassigned fund balance at 15% of expenditures and does not expect to drawdown below these levels.

### **Very strong liquidity**

In our opinion, Canton's liquidity is very strong, with total government available cash at 26.7% of total governmental fund expenditures and 6.6x governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

We believe the town has strong access to external liquidity, as evidenced by regular GO debt issuances. Canton 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 strong debt and contingent liability profile**

In our view, Canton's debt and contingent liability profile is very strong. Total governmental fund debt service is 4.1% of total governmental fund expenditures, and net direct debt is 47.7% of total governmental fund revenue. Overall net debt is low at 1.1% of market value, and approximately 74.2% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

With this issuance, the town will have about \$53.7 million in total direct debt. Canton is expecting to issue an additional \$11.1 million in debt over the next two years to finance various capital improvement projects. We do not expect this to have a material effect on our view of its debt profile.

### **Pension and other postemployment benefit obligations**

- In our opinion, a credit weakness is Canton's large pension and OPEB obligation. 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.

Canton participates in the following pension and OPEB plans as of June 30, 2019:

- Norfolk County Retirement System (NCRS), a cost-sharing, multiple-employer defined-benefit pension plan, which is 58.4% funded, with the town's net pension liability at \$48.8 million.
- Town of Canton OPEB plan, a single-employer, defined-benefit health care plan that provides medical, dental, and life insurance to current and future retirees, their dependents and beneficiaries. The OPEB plan is funded on a pay-as-you-go basis, and at fiscal-year-end had a funded ratio of 5.88% and a net OPEB liability of \$83.5 million.

The town's combined required pension and actual OPEB contributions totaled 8.5% of total governmental fund expenditures in 2019. Of that amount, 4.6% represented required contributions to pension obligations, and 3.9% represented OPEB payments. Canton made its full annual required pension contribution in 2019. The funded ratio of the largest pension plan is 58.3%. 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.

Canton also provides OPEB to retirees. It has set up an OPEB trust to prefund the liability, which we view as positive. The OPEB trust has a \$5.83 million balance. The town expects to budget \$1.05 million to the OPEB trust for fiscal 2021. In addition, when the NCRS plan is fully funded in 2029, the town will shift those pension assessment savings to OPEB funding. Although we recognize that management is attempting to mitigate the risks associated with the large pension and OPEB obligation and that costs are currently manageable, we believe unfunded liabilities will likely

remain a challenge since costs continue to grow and pressure the long-term budget.

### Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

## 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
- 2019 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of April 29, 2020)		
Canton Twn st qual go rfdg bnds		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Canton Twn GO mun purp loan bnds ser 2017 dtd 03/16/2017 due 06/15/2037		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Canton Twn GO mun purp loan bnds (Tax-exempt)		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Canton Twn GO (MBIA) (National)		
<i>Unenhanced Rating</i>	AAA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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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