

Summary:

Scarborough Town, Maine; General Obligation

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Credit Profile

US\$7.78 mil GO bonds ser 2019 dtd 06/20/2019 due 11/01/2039

Long Term Rating AA+/Stable New

Scarborough Twn GO

Long Term Rating AA+/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' rating to Scarborough, Maine's series 2019 general obligation (GO) bonds and affirmed its 'AA+' rating on the town's existing GO debt. The outlook on all ratings is stable.

Supporting Scarborough's general creditworthiness is its stable economy, with access to the Portland metropolitan statistical area (MSA). The town has also maintained strong reserve levels over the past three years. We expect the town to maintain its strong budgetary flexibility through balanced financial operations and making the necessary budgetary adjustments to avoid a material drawdown on reserves. In addition, we expect its fixed costs to remain manageable given the town's limited capital needs and well-funded pension plans.

The town's full-faith-and-credit pledge secures the bonds. Scarborough can levy ad valorem property taxes for bond repayment, subject to limitations of the state's LD-1 legislation. We rate the limited-tax GO debt on par with our view of Scarborough'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 intend to use series 2019 bond proceeds for various capital improvement projects.

The rating reflects our opinion of Scarborough's:

- Very strong economy, with access to a broad and diverse MSA;
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could improve in the near term relative to fiscal 2018, which closed with a slight operating deficit in the general fund and an operating deficit at the total governmental fund level in fiscal 2018;
- Strong budgetary flexibility, with an available fund balance in fiscal 2018 of 11.4% of operating expenditures;
- Very strong liquidity, with total government available cash at 19.1% of total governmental fund expenditures and 3.7x governmental debt service, and access to external liquidity that we consider strong;
- Strong debt-and-contingent-liability profile, with debt service carrying charges at 5.2% of expenditures and net

direct debt that is 112.2% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value; and

- Strong institutional framework score.

Very strong economy

We consider Scarborough's economy very strong. The town, with an estimated population of 20,208, is located in Cumberland County in the Portland-South Portland MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 152% of the national level and per capita market value of \$198,550. Overall, the town's market value grew by 6.0% over the past year to \$4.0 billion in 2019. The county unemployment rate was 2.7% in 2018.

The town enjoys direct access to Maine's major arteries (Interstate 95 and I-295 and U.S. Route 1), connecting it to larger employment centers throughout Cumberland County. In addition to access to major markets in the region, Scarborough has a sizable employment base that includes small commercial and industrial businesses. There is no taxpayer concentration, with the 10-leading taxpayers accounting for 8.2% of assessed value (AV). Officials report that Wal-Mart, the town's second-largest taxpayer at about 1% of total AV, is currently appealing its AV. The town is disputing this appeal and expects it to go before the Maine Supreme Judicial Court in the near future. Management indicates it will be able to cover through overlay reserves if needed.

Some leading employers include Scarborough, Hannaford Bros.' corporate headquarters, a U.S. Postal Service distribution center, and Maine Health. According to management, a new 288-unit multifamily luxury residential development along Haigis Parkway is about 75% complete, with many units already being sold. Maine Life Care, a senior citizen retirement community and the town's largest taxpayer, also continues to expand. In addition, the town is helping to foster development in its downtown area with the establishment of a tax increment financing (TIF) district in the area that is expected to experience both commercial and residential development.

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.

Highlights include management's strong focus on financial and capital planning, evidenced by Scarborough's five-year capital improvement plan (CIP), which sets parameters and outlines debt and non-debt financing for all capital projects. The town adheres to its formal investment policy with annual reporting of investments to the town council. Finance officials present monthly variance reports to the town manager and quarterly reports to council. Management budgets conservatively, coupled with at least a four-year historical trend analysis.

Scarborough manages reserves in accordance with its stated policy. Management also maintains, and follows, a formal debt-management policy. The formal reserve policy targets an unassigned fund balance at 10.0% of the budget but not less than 8.3%, which the town has adhered to over the past two years.

Adequate budgetary performance

Scarborough's budgetary performance is adequate, in our opinion. The town had slight deficit operating results in the general fund of 1.3% of expenditures, and deficit results across all governmental funds of 1.8% in fiscal 2018. Our assessment accounts for the fact that we expect budgetary results will improve from fiscal 2018 and remain stable over the short-term.

We adjusted fiscal 2018 performance for recurring transfers and nonrecurring revenue and expenditures under the general fund and total governmental fund. According to the town, the fiscal 2018 general fund drawdown was primarily due to higher-than-anticipated expenditures, including salary costs from retirements and paying out of accruals. In addition, officials indicate the town experienced lower-than-anticipated intergovernmental revenue, including state education subsidies for special education purposes, during the year. For fiscal 2019, officials indicate budget to actuals are currently on target with revenue at 94% of budget and expenditures at 88%. The town has also increased its overlay account in fiscal 2019 by \$350,000 to cover several previous year tax appeals, which are pending final verdict by the superior court. As a result, the town expects to end the year with a general fund surplus and does not anticipate another general fund drawdown.

The town's proposed fiscal 2020 budget is balanced, according to management, and is not expected to deviate greatly from previous year's budget. The town expects to appropriate about \$350,000 of fund balance towards the budget for education purposes and is budgeting for increases in education costs due to higher enrollment. The town also plans to budget to a slight increase in state revenue sharing in line with the governor's proposed budget. As a result, given the town's historically balanced operations and projected positive operating results, we expect the town's budgetary performance to remain at least adequate going forward. However, should the town experience negative financial operations, our assessment of its budgetary performance could weaken.

Property taxes account for 81% of general fund revenue, followed by intergovernmental revenue at 11%. Tax collections remain strong, averaging 99% over the past three years.

Strong budgetary flexibility

Scarborough's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2018 of 11.4% of operating expenditures, or \$9.9 million.

The town has consistently maintained, what we consider, strong budgetary flexibility over the past three fiscal years. Management expects to end fiscal 2019 with an increase in available reserves. In addition, the town has appropriated about \$350,000 toward the fiscal 2020 budget for school department costs. The town has a formal reserve policy that targets maintaining unassigned fund balance at 10.0% of the budget but no less than 8.3%, which it began to adhere to in fiscal 2017.

Scarborough also has an interfund loan receivable of about \$2.7 million in the general fund due from the Haigis Parkway assessment fund. The town holds a restricted fund balance of \$3.2 million to cover current shortfalls in receivables from the assessment fund. Officials indicate the general fund has not experienced any shortfalls in payments and expect to repay the remaining balance within the next two-to-three fiscal years. Therefore, we expect budgetary flexibility to remain, at least, strong.

Very strong liquidity

In our opinion, Scarborough's liquidity is very strong, with total government available cash at 19.1% of total governmental fund expenditures and 3.7x governmental debt service in 2018. In our view, the town has strong access to external liquidity if necessary.

Scarborough has issued GO bonds every year for the past 20 years, supporting its strong access to external liquidity. The town does not currently have investments that we consider permissive or aggressive, because its investments are mainly in governmental funds, including money market funds with maturities of less than one year. In addition, it does not have any contingent-liquidity risks from financial instruments with payment provisions that change upon the occurrence of certain events. Therefore, we expect liquidity to remain very strong.

Strong debt-and-contingent-liability profile

In our view, Scarborough's debt-and-contingent-liability profile is strong. Total governmental fund debt service is 5.2% of total governmental fund expenditures, and net direct debt is 112.2% of total governmental fund revenue. Overall net debt is low at 2.8% of market value, which is in our view a positive credit factor.

With this issuance, Scarborough will have about \$103 million of total direct debt outstanding. Officials plan to issue about \$5 million of additional debt annually over the next two years for various capital improvement projects as existing debt expires. Even with this additional debt, we expect the town's debt profile to remain strong. However, should overall net debt increase above 3% of market value and cause debt ratios to weaken, we believe the town's debt profile could weaken.

Scarborough's pension contributions totaled 2.1% of total governmental fund expenditures in 2018. The town made its full annual required pension contribution in 2018.

Scarborough contributes to the State Employee and Teacher Plan (SET) for school department employees and the Participating Local District Consolidated Plan (PLD), defined-benefit pension plans under the Maine Public Employees' Retirement System. The town also participates in the International City Manager's Assn. (ICMA) money-purchase plan, a defined-contribution plan. The town's proportionate share of the net pension liability for the PLD plan totaled \$6.5 million as of fiscal 2018, which assumes a 6.875% rate of return and is 86.4% funded as of fiscal 2018. The SET plan is 80.78% funded using an assumed rate of return of 6.875%, with the town's proportionate share of the net pension liability totaling \$552,792 as of fiscal 2018. Scarborough matches up to 6.0% of employee contributions to the ICMA plan. In addition, it provides OPEB as an implicit rate subsidy to retirees. Overall, we expect the town's retirement costs to remain manageable going forward.

Strong institutional framework

The institutional framework score for Maine municipalities is strong.

Outlook

The stable outlook reflects our opinion of Scarborough's very strong economy and liquidity. The town's strong budgetary flexibility, management conditions, and debt profile further support the rating. We expect officials will continue to manage the budget accordingly and maintain the town's strong budgetary flexibility and, at least, an

adequate debt profile. Therefore, we do not expect to change the rating in our two-year outlook horizon.

Downside scenario

If financial performance deteriorates, leading to a continuous reduction of reserves and weakening of budgetary flexibility or if the debt profile weakens, we could lower the rating.

Upside scenario

Although unlikely, if the town increases reserves comparable with those of higher-rated peers, consistently through strong budgetary performance while sustaining a strong debt and contingent liability profile, coupled with a very strong economy, we could raise the rating.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- 2018 Update Of Institutional Framework For U.S. Local Governments

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