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Ratings

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Summary:

Scott Township, Pennsylvania; General Obligation

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Summary:

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Credit Profile		
US$13.705 mil GO bnds ser 2017 due 08/15/2038		
Long Term Rating	A+/Stable	New
Scott Twp GO		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rationale

S&P Global Ratings assigned its 'A+' long-term rating to Scott Township, Pa.'s series 2017 general obligation (GO) bonds. At the same time, we affirmed our 'A+' long-term rating and underlying rating (SPUR) on the township's existing GO debt. The outlook on all the ratings is stable.

The township's full-faith-and-credit pledge secures the bonds. We understand officials intend to use series 2017 bond proceeds to refund Scott's series 2012 and 2013 GO bonds for net present value savings.

The rating reflects our opinion of the following factors for the township, including its:

- Adequate economy, with 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;
- Weak budgetary performance, with operating deficits in the general fund and at the total governmental fund level in fiscal 2016;
- Strong budgetary flexibility, with an available fund balance that we expect will decrease in the near term from its fiscal 2016 level of 17% of operating expenditures;
- Very strong liquidity, with total government available cash at 20.0% of total governmental fund expenditures and 2.3x governmental debt service, and access to external liquidity we consider strong;
- Very weak debt and contingent liability position, with debt service carrying charges at 8.5% of expenditures and net direct debt that is 111.1% of total governmental fund revenue, as well as exposure to speculative contingent liabilities; and
- Strong institutional framework score.

Adequate economy

We consider Scott Township's economy adequate. The township, with an estimated population of 17,292, is a built-out residential community approximately eight miles south of Pittsburgh in Allegheny County. It is in the Pittsburgh MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 136% of the national level and per capita market value of $48,898. Overall, market value grew by 3.1% over the past year to $845.5 million in 2016. The county unemployment rate was 5.2% in 2016.

The local economic base is somewhat limited, but we understand residents largely commute to the greater Pittsburgh MSA for employment.

Adequate management

We view the township'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.

Financial management strengths include regular budget monitoring with formal reports presented monthly to the board of commissioners. These reports include revenue and expenditure performance and variances in the year to date, as well as investment performance. The township lacks formal management policies pertaining to debt, minimum reserves, and long-range fiscal and capital planning.

Weak budgetary performance

Scott Township's budgetary performance is weak, in our opinion. The township had operating deficits of negative 4.4% of expenditures in the general fund and negative 8.2% across all governmental funds in fiscal 2016.

We have revised the township's budgetary performance to weak from strong due to ongoing operating shortfalls due to planned capital expenditures and spend-down of reserves. Over the past two audited years, the general fund has ended with consecutive operating deficits. During that period, the township has been undertaking capital expenditures that are primarily routine maintenance. It is our understanding that Scott is anticipating further operating deficits as part of its plan to reduce its reserves. Therefore, it will continue to spend on capital and absorb increases in health care benefits and salaries. The township's practice has been to budget for shortfalls that would result in the entire use of its fund balance. However, operations have been consistently more favorable. Nonetheless, we believe the continued drawdowns are a credit concern and could result in negative rating implications.

The fiscal 2017 budget assumes an operating drawdown of about $1.2 million. However, according to management, the general fund may end with an operating deficit of $400,000 to $500,000. Given the expected drawdown, we expect that township's budgetary performance to remain weak.

Should there be further budget drawdowns and we view the budget as structurally imbalanced with no plans to correct, the rating could be lowered by multiple notches.

Strong budgetary flexibility

Scott Township's budgetary flexibility is strong, in our view, with an available fund balance that we expect could decrease in the near term from its fiscal 2016 level of 17% of operating expenditures, or $1.9 million.

The township's budgetary flexibility takes into account our assessment that the available fund balance will likely be reduced. Should fiscal 2017 end with a drawdown of $400,000, the available fund balance will shrink to about $1.5 million, or about 13% of budgeted expenditures.

The township's available fund balance has been decreasing due to a planned drawdown, according to management. As such, the available fund balance has declined from $2.8 million, or 26% of expenditures in 2014 to its current level. We understand that the township is expecting to further draw down on its available fund balance. According to management, the available fund balance could be depleted within the next four years, which we also consider a credit concern. Furthermore, management has not presented a plan for how it will rebuild its reserves. We believe that the current fund balance continues to provide credit support. However, we believe that should reserves continue to decline, resulting in weak-to-very weak budgetary flexibility, we could lower the rating.

Very strong liquidity

In our opinion, Scott Township's liquidity is very strong, with total government available cash at 20.0% of total governmental fund expenditures and 2.3x governmental debt service in 2016. In our view, the township has strong access to external liquidity if necessary.

The township maintenance of its strong access to external liquidity, since it has issued GO bonds frequently in the past 10 years, further enhances our view of its liquidity. It does not currently have investments we consider permissive or aggressive because the entirety of its general fund investments are in The Pennsylvania Local Government Investment Trust and CDs, which we view as low risk.

The township privately placed its $2.6 million series 2015 GO note with Capital One Public Funding LLC and was established through bond ordinance. The note is secured by the township's full faith, credit, and taxing power, is payable from general taxes and revenues, and was used to finance capital expenditures. The note bears a fixed interest rate of 2.96% through maturity. The township may prepay the note at will without penalty. It is our understanding that there are no covenant violations that would result in acceleration of payment.

Very weak debt and contingent liability profile

In our view, Scott Township's debt and contingent liability profile is very weak. Total governmental fund debt service is 8.5% of total governmental fund expenditures, and net direct debt is 111.1.8% of total governmental fund revenue.

The township's debt profile is conservative, with no variable-rate debt outstanding. Scott's overall net debt includes its proportionate share of overlapping debt for the county and school district. It was issued a consent decree from the Environmental Protection Agency (EPA) that highlighted compliance issues that called for capital expenditures to its sewer system that could have resulted in about $15 million in capital expenditures. According to management, the Allegheny County Sewer Authority (Alcosan) has taken over the costs associated the necessary repairs. Therefore, this is no longer viewed as a speculative contingent liability to the township.

Management has indicated that there is a need for storm water improvements that could cost around $2 million.

Scott's combined required pension and actual other postemployment benefit (OPEB) contributions totaled 3.8% of total governmental fund expenditures in 2016. Of that amount, 2.8% represented required contributions to pension obligations, and 0.9% represented OPEB payments. The township made its full annual required pension contribution in 2016.

The township contributes to two defined-benefit pension plans for police and nonuniformed employees. Based on Governmental Accounting Standards Board Statement No. 68, the plans are funded at 82.1%, and 96%, respectively.

The township offers OPEBs to eligible employees. Based on its Dec. 31, 2016 actuarial study, the township's OPEB unfunded actuarial accrued liability totaled $3.5 million and is 0% funded. Management has indicated that it expects to continue to fund this liability on a pay-as-you-go basis.

Strong institutional framework

The institutional framework score for Pennsylvania nonhome-rule cities and all boroughs and townships is strong.

Outlook

The stable outlook is based on Scott's very strong liquidity and still strong budget flexibility despite the recent drawdowns. It also reflects our views that, though the township could further draw on its reserves, within the outlook horizon, it is likely that its budgetary flexibility could remain at least strong or adequate. As such, we do not expect to change the rating within the outlook's two-year period.

Downside scenario

Should there be persistent drawdowns stemming from revenues not being able to absorb recurring expenditures as opposed to cash-funding capital expenditures, leading to further weakened budgetary performance and available reserves with no clear plans to correct, we could lower the rating by multiple notches.

Upside scenario

We could raise the rating if the township's economic metrics, primarily its market value per capita, improve to levels that are more in line with its higher rated peers, coupled with strengthened financial management practices and stable financial operations leading to stronger and sustained budgetary performance and flexibility.

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
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015