

Fitch Affirms Woonsocket, RI's GOs at 'B'; Outlook Stable

Written by Australian Business

NEW YORK--([BUSINESS WIRE](#))--Fitch Ratings has taken the following action on the city of Woonsocket, RI's (the city) outstanding general obligation (GO) bonds:

--\$109 million GO bonds affirmed at 'B'.

The Rating Outlook is Stable.

SECURITY

The bonds are general obligations of the city and are backed by its full faith and credit and unlimited taxing power.

KEY RATING DRIVERS

PROGRESS IN STABILIZING FINANCES: The city has made progress in stabilizing the city's finances, including decreases in the cumulative general and school fund negative balances, and improved liquidity position.

CITY BENEFITS FROM STATE OVERSIGHT: Fitch views state oversight of the city via the Budget Commission positively given the severity of the city's fiscal challenges. The commission's support in restructuring city finances and stabilizing liquidity continues to be key to the city's fiscal recovery.

CONTINUED FINANCIAL CHALLENGES; LIQUIDITY CONCERNS: The city faces ongoing fiscal pressure driven by a weak but improving economy, limited financial flexibility, and continued negative combined city and school fund balances. Liquidity remains an issue, although it has been addressed in the near term through another advance of state aid.

WEAK EMPLOYMENT AND DEMOGRAPHICS: City demographics are weak with high unemployment levels, low income levels, and declining population.

HIGH DEBT AND RETIREE COSTS: Debt levels are above average and total carrying costs for pensions, OPEB, and debt service are high.

RATING SENSITIVITIES

LIQUIDITY STABILIZATION: The demonstrated ability of the city to adequately address cash flow needs, with decreased reliance on state aid advances, would lessen Fitch's concerns about stressed liquidity and the city's ability to meet its financial obligations in a timely manner.

ABILITY TO ADDRESS CUMULATIVE NEGATIVE ENDING BALANCES: The ability to address cumulative school and city negative ending balances adequately as planned would likely lead to a rating upgrade.

CREDIT PROFILE

Woonsocket is located 15 miles outside of Providence. The city's population of about 41,000 in 2013 has declined by 5% since 2000.

FINANCIAL IMPROVEMENT UNDER MULTI-YEAR DEFICIT REDUCTION PLAN

In 2013, the city developed a multi-year plan to reduce and ultimately eliminate cumulative school and city fund negative balances. Major components of the plan required state legislative approval, including pension-related initiatives and a \$2.5 million supplemental property tax bill. The plan also includes employee and retiree health care

savings initiatives. The plan assumes annual reductions in the cumulative school and city negative balances, with a positive ending balance achieved by fiscal 2016.

Budget estimates a year ago indicated a fiscal year end 2013 cumulative city and school fund negative ending balance of approximately \$8.2 million, or 6% of expenditures. Audited figures for fiscal year 2013, however, show a much smaller negative balance of \$3.2 million (2.2%). The bulk of the variance relates to lower personnel costs (salary and benefits), as the budget for fiscal year 2013 assumed a number of staffing positions that were not filled. The city also experienced lower than budgeted spending in other areas. The unrestricted portion of the ending balance was a negative \$3.5 million or 2.4% of expenditures and transfers out.

Based on preliminary estimates for fiscal 2014, the combined general and school fund operating surplus totals about \$4.9, with \$2 million planned to be used for deficit reduction and the remainder dedicated to capital spending needs. The city projects a cumulative general and school fund negative ending balance of \$1.2 million (1%) at the end of fiscal 2014, reflecting a positive undesignated general fund balance of \$1.3 million and a negative undesignated school fund balance of \$2.5 million.

For fiscal 2015, the combined cumulative general and school fund year-end balance is projected at a negative \$1.2 million reflecting balanced school fund operations and a modest general fund surplus. The fiscal 2015 budget assumes revenue growth of about 2% driven by higher property tax collections and increased state education revenue resulting from the implementation of full-day kindergarten. The tax levy increase is 4.8%, with the excess above the state cap of 4% permitted by state legislative approval due to the addition of Landmark Hospital to the tax base. Expenditure growth of 4.0% is expected, reflecting increased staffing, planning and development, public works, and pension actuarially required contribution (ARC) funding costs.

STATE AID ADVANCES CONTINUE

In recent years, city cash flow has been strained, requiring interfund borrowing, state aid advances, and property tax pre-payment for stabilization. In fiscal 2013, the state advanced to July 2012 \$12.4 million in school aid originally scheduled for April through June 2013. In addition, the city benefitted from a prepayment by CVS Corporation in June 2013 of its \$2.8 million fiscal year 2014 property tax bill. CVS is the city's largest

taxpayer.

Current fiscal year 2014 combined city and school cash flows show positive monthly ending cash balances, with the June 2014 ending cash balance estimated at \$4 million. The state again advanced school aid (\$12.8 million) to July 2013 from the originally scheduled April through June 2014 payments. The city also relied on interfund borrowing (\$2 million, repaid in August 2013). The city has about \$2.8 million (vs. \$7 million a year ago) in deferred payments (30 to 45 days overdue) but expects to catch up with the payments by August 2014. Fiscal year 2015 combined city and school cash flow projections assume another, though lower, state aid advance (\$8.9 million), which has been approved for July 2014, derived from the advance of May and June 2015 payments, and \$2 million in interfund borrowing to be repaid by November 2014. The June 2015 ending cash balance is estimated at about \$500,000, reflecting, in part, repayment of prior year payment deferrals.

PENDING LITIGATION

The city faces three significant pending lawsuits which could negatively affect finances. First, a suit challenging the implementation of the 2013 \$2.5 million supplemental tax has been filed and the city expects arguments to be heard in the case in the fall. Second, a group representing police department retirees has filed a legal challenge to retiree savings initiatives implemented as part of the multi-year deficit reduction plan. A potential adverse ruling could result in a \$3.4 million liability to the city and school funds. Management has indicated that settlement discussions and negotiations with retirees are ongoing. Last, WP Woonsocket Associates, LLC, one of the city's top taxpayers (1% of TAV in fiscal 2013 or about \$550,000 in tax revenue), is challenging its valuation as overstated.

LONGER-TERM FINANCIAL CHALLENGES

The combined city and school funds face ongoing financial challenges, with continued negative balances and liquidity strain, though cash flow issues are being addressed in the near term through another advance of state aid. However, Fitch believes that budget commission oversight has led to more effective fiscal management. The Budget Commission approved a multi-year plan to reduce and ultimately eliminate projected cumulative school and city operating deficits. Major components of the plan were employee

and retiree health care savings initiatives, some of which required negotiated union contract revisions. As a back-up in case union concessions were not received, the Commission was able to enact these revisions by resolution for the unions whose contracts had expired. In addition, the Budget Commission used its authority to advance state aid to the city, stabilizing the city's liquidity position.

The city's revenue-raising flexibility is limited due to a statutory annual tax cap levy of 4% over the prior year's levy. The city has been able to exceed the tax cap limit in certain years with city council and state legislative approval, but there is no assurance this would be consistently approved.

WEAK SOCIOECONOMIC INDICATORS

The city's unemployment rate has declined, but continues to be elevated at 8.8% for April 2014, compared to 7.8% for the state and 5.9% for the nation. Employment was flat in 2013, but April year-over-year figures show growth of 1.1%. Median household income of \$39,329 and per capita money income of \$21,316 are below average at 70% and 72% of state averages, respectively.

Woonsocket benefits from the presence of CVS Caremark Corporation, which maintains its headquarters in the city. CVS is the city's largest employer (about 3,000 workers), and the largest taxpayer, making up about 6.8% of the city's taxable assessed value (TAV).

Landmark Hospital, the city's second largest employer (1,000 workers) was purchased by Prime Healthcare Services in 2013. The sale converted the hospital into a taxable entity. The city expects the addition of the hospital to tax base to add about \$900,000 to fiscal 2015 tax revenues.

HIGH DEBT RATIOS AND UNDERFUNDED PENSIONS

Overall fiscal 2013 debt ratios are generally high, net of debt service reimbursements

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on the city's public school revenue bonds issued by the Rhode Island Health and Education Building Corporation, with debt-to-market value at 6.3% and debt per capita more mid-range at \$2,867. Annual debt service as a percentage of governmental spending was a high 14.3% in fiscal 2013. The city has no near-term debt issuance plans. The fiscal 2014 and 2015 budgets include pay-go spending on firefighting, public works, and school capital projects. A portion of school and general fund surpluses was dedicated to capital spending, in part to address deferred capital needs. Pressure to address deferred capital spending will likely continue in the near term.

The city-administered police and fire pension plan is funded at a low 59%, assuming a 7.5% rate of return, with an unfunded liability of \$34 million at July 1, 2013 or 1.8% of market value. The 2013 funded ratio declines to an estimated 56% using a Fitch-adjusted 7% rate of return. The city has historically underfunded the ARC for the city-administered pension plan. Funding in fiscal years 2013 and 2012 represented about 28% of the ARC in those years. As part of its multi-year plan, the city has funded 100% of the \$3.5 million ARC for fiscal 2014, an increase of \$2.5 million in fiscal 2014, and has budgeted 100% funding (\$3.8 million) for fiscal 2015. Total pension ARC, OPEB pay-go and debt service payments were high at about 26% of fiscal year 2013 operational spending.

Additional information is available at 'www.fitchratings.com'.

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, National Association of Realtors.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria' (Aug. 14, 2012);

--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012)

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Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015

U.S. Local Government Tax-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685314

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