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## Summary:

# Lambertville, New Jersey; General Obligation

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## Summary:

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### Credit Profile

Lambertville GO bnds		
<i>Long Term Rating</i>	AA/Negative	Outlook Revised
Lambertville GO (AGM)		
<i>Unenhanced Rating</i>	AA(SPUR)/Negative	Outlook Revised

Many issues are enhanced by bond insurance.

## Rating Action

S&P Global Ratings revised its outlook to negative from stable and affirmed its 'AA' long-term rating on Lambertville, N.J.'s general obligation (GO) debt outstanding.

The township's full-faith-and-credit pledge and agreement to levy ad valorem property taxes, without limitation as to rate or amount, secure the bonds.

The outlook revision reflects what we view as weakened budgetary performance and reduced financial flexibility following consecutive negative operating results, reserve drawdowns, and cash balance deterioration in recent years. In our view, there is a one-in-three chance that the township will be unable to regenerate both cash and current fund reserves to levels that are comparable at the 'AA' rating level within the next two years, and that its fixed costs will remain high in relation to those of peers at the current rating level. We understand that unaudited estimates for fiscal 2021 project increases in cash and fund balance; however, should management be unsuccessful in restoring and sustaining balances to levels that we view as more commensurate with the current rating, we could lower the rating.

### Credit overview

Lambertville's strong economic indicators support our rating. However, we believe that use of reserves in recent years has weakened the township's financial flexibility and may no longer be strong enough to support the rating. Officials expect a reversal in the recent trend of fund balance usage, with 2021 expectations stronger than the prior five years, and project a fund balance increase to levels closer in line with the city's \$1.0 million target minimum. However, a high overall carrying charge reflects pressure on the budget for the township's fixed costs, including debt, pensions, and other postemployment benefits (OPEBs), which totaled 35% in fiscal 2020. If management is unable to adjust the budget to address these costs, particularly given the currently limited flexibility of the city's finances, we could lower the rating. Given the relatively small size of the budget, even small revenue or expenditure shifts have a larger effect on operational performance and, as a result, reserve and cash levels. We will monitor progress over our two-year outlook horizon to determine if the township's overall financial profile remains comparable with that of 'AA' peers.

The rating further reflects our assessment of the township's:

- Weakened financial position following several years of fund balance use, leading to an available fund balance that, while still at a level we consider strong, is on the verge of nominally low levels;

- Growing tax base, anchored by its location within the New York MSA, with above-average wealth and income metrics;
- Standard financial policies and practices under our Financial Management Assessment (FMA) methodology, and strong institutional framework; and
- Very weak debt and liabilities profile with elevated debt levels, and high pension and OPEB costs.

### **Environmental, social, and governance**

We consider Lambertville's environmental risks slightly elevated, owing mainly to hurricane exposure. However, the township has an emergency management team and planning in place to help mitigate against these elevated risks. Hurricane Ida did cause significant damages to personal and public property, but received timely reimbursements from the Federal Emergency Management Agency for storm-related costs. We view governance risks as being generally in line with those of peers, although pension funding discipline and assumption choices at the state level will likely lead to elevated and volatile costs for the township. We consider social risks in line with our view of the sector standard.

## **Negative Outlook**

### **Downside scenario**

We could lower the rating, potentially by multiple notches, if the township is unsuccessful in its restoration and maintenance of reserves and liquidity at levels we view as supportive of the 'AA' rating.

### **Return to stable scenario**

We could revise the outlook back to stable if the township is able to take actions that show a demonstrated commitment to maintain stronger reserve and cash levels through positive operations.

## **Credit Opinion**

### **Recent history of expenditures outpacing revenues and consistent use of fund balance**

In fiscal 2020, officials appropriated \$400,000 of reserves to balance the budget. The township's operating expenditures exceeded operating revenues by approximately \$128,000, or 2.0%. We adjusted its financial performance to exclude a COVID-19 special emergency revenue item of \$395,000 authorized to offset revenue losses related to the pandemic. As a result of 2020 operating performance, current fund reserves fell to \$726,000 at fiscal year-end (or 11.3% of operating expenditures). This comes after several years of current fund balance decreases from a high point of \$1.1 million in 2015 (or 21.6%), and have shown annual decreases since. In addition to fund balance decreases, cash levels have also fallen in recent years, ending at \$702,000 in fiscal 2020. Management noted that both cash and reserves levels are robust in other funds, for example, within the capital fund; however, we do not consider capital fund balances available for operations. Given audited results for fiscal 2020, both cash and reserves are not at levels we consider comparable at the current rating level.

For fiscal 2021, management reports positive operational performance. The initial budget called for an appropriation of \$293,000 to balance the budget, but now, given year-end actual results, management expects a full regeneration of surplus. Estimates for both cash and reserves are improved compared to fiscal 2020: Current fund balance is expected

to increase to \$1.0 million and cash is likely to total \$2.0 million. In addition, Lambertville was awarded roughly \$400,000 total in American Rescue Plan Act funds, half of which has been received but not spent, with the remainder expected in mid-2022. While these estimates are certainly positive and should help improve our view of the township's financial metrics, if the 2021 audit shows results different than preliminary expectations, and if future years lead to continued low levels of cash and reserves that are not comparable at the rating level, we could lower the rating.

Property taxes make up nearly 47% of operating revenue while miscellaneous revenue accounts for the bulk of the remainder.

### **Growing tax base with access to opportunities in various metropolitan areas**

Lambertville is in western New Jersey, approximately ten miles north of Trenton, on the Delaware River. Its location, roughly 40 miles north of Philadelphia and roughly 70 mile south of New York, provides residents with significant employment opportunities, in addition to what is available in neighboring Trenton and the county. The tax base is primarily residential, which accounted for 80% of assessed value in 2020, followed by commercial values at 15%. Due to continued reinvestment in existing properties and housing redevelopment, management expects continued growth within the tax base. It reports that there are no outstanding appeals that will affect the current tax revenue assessments.

### **Standard financial management assessment, without formal long-term planning and financial policies**

Financial management strengths include regular budget monitoring with formal monthly reports to the council. Additional practices include the development of a three-year capital improvement plan, with identified funding sources, which management reviews annually. The township does not have debt management or long-term financial forecasting. It maintains an adopted cash management plan that specifies permitted investments, which conforms to state guidelines. Its informal fund balance target is to regenerate surplus to approximately \$1 million annually. Management is aware that reserves have fallen below this target in recent years, although estimates for fiscal 2021 show an increase in reserves that is back in line with the target.

### **Relatively weak debt profile, with costs relative to the budget, but rapid amortization; significant pension and OPEB liabilities**

Lambertville has roughly \$13.2 million in direct debt outstanding, including a \$3.8 million bond anticipation note, issued in April 2021. Management has begun work on a longer-term plan for capital investments, including any needs remaining unaddressed post-Hurricane Ida; however, it has noted that it is too early in the process to determine the amount or timing of potential bonding that will be included in that plan. Future debt plans are expected to be layered in to amortize with existing debt to maintain flat costs.

In our view, the township's debt service carrying charges are elevated, making up nearly 23% of the budget in fiscal 2020. When combined with pension and OPEB payments, fixed costs totaled 35%, which is higher than we typically see at the rating level, and could lead to additional budget pressure if not addressed.

#### **Pension and OPEBs**

We view pension and OPEB liabilities as source of credit pressure for Lambertville, given that costs that are currently a large portion of the budget, combined with the lack of a mechanism to keep them from rising. While funding policies

somewhat mitigate the risks of escalating contributions for local governments because of low plan-funded ratios, the township could face escalating pension costs should the state not follow its schedule of increasing pension contributions.

Furthermore, OPEB liabilities are funded on a pay-as-you-go basis, which, given claims volatility as well as medical cost and demographic trends, is likely to lead to escalating costs. While the township has some legal flexibility to alter OPEB benefits, it is unable to prefund these costs, increasing the risk these benefits could create budgetary pressure.

Lambertville participated in the following plans as of Dec. 31, 2020:

- Police and Firemen's Retirement System (PFRS): 59% funded, with a proportional share of the net pension liability (NPL) equal to \$2.5 million; and
- Public Employees' Retirement System (PERS): 43% funded, with a proportional share of the NPL equal to \$1.7 million.

Although the township funds 100% of the actuarially determined contribution (ADC), contributions remain short of static and minimal funding progress, in part due to poor assumptions and methodologies, but also due to New Jersey's historic underfunding of the state's portion of the ADC. The plans' 30-year, level-dollar, open amortization schedule will result in slow funding progress. For more details and information on these risks, see "New Jersey Pension Funding: State Actions Reverberate At The Local Level," published Dec. 12, 2018, on RatingsDirect. Although the state did not make up for lottery contribution shortfalls in fiscal 2020, its adopted fiscal 2022 budget includes pension funding exceeding the full ADC for the first time in 25 years, which we view positively.

Lambertville also provides OPEBs to eligible retirees through the State Health Benefits Program, a cost-sharing, multiple-employer defined-benefit postemployment health care plan administered by the state. These benefits are funded on a pay-as-you-go basis with no mechanism in place that allows for prefunding, limiting the township's ability to plan for these costs. In 2019, the latest valuation year available, Lambertville contributed \$445,000 toward its obligation and carried a net OPEB liability of \$5.6 million.

### Strong institutional framework

The institutional framework score for New Jersey municipalities is strong.

Lambertville, NJ -- Key Credit Metrics				
	Most recent	Historical information		
		2020	2019	2018
<b>Very strong economy</b>				
Projected per capita EBI % of U.S.	173			
Market value per capita (\$)	232,335			
Population		3,720	3,744	3,740
County unemployment rate(%)		7.2		
Market value (\$000)	864,288	818,923	807,745	
Ten largest taxpayers % of taxable value	6.0			

## Lambertville, NJ -- Key Credit Metrics (cont.)

	Most recent	Historical information		
		2020	2019	2018
<b>Weak budgetary performance</b>				
Operating fund result % of expenditures	(8.1)	(0.9)	(2.0)	
Total governmental fund result % of expenditures	(8.1)	(0.9)	(2.0)	
<b>Strong budgetary flexibility</b>				
Available reserves % of operating expenditures	11.3	15.6	18.2	
Total available reserves (\$000)	726	846	892	
<b>Strong liquidity</b>				
Total government cash % of governmental fund expenditures	11	22	45	
Total government cash % of governmental fund debt service	48	88	201	
<b>Adequate management</b>				
Financial Management Assessment	Standard			
<b>Very weak debt &amp; long-term liabilities</b>				
Debt service % of governmental fund expenditures	22.5	24.5	22.5	
Net direct debt % of governmental fund revenue	218			
Overall net debt % of market value	2.5			
Direct debt 10-year amortization (%)	89			
Required pension contribution % of governmental fund expenditures	5.2			
OPEB actual contribution % of governmental fund expenditures	6.9			
<b>Strong institutional framework</b>				

EBI--Effective buying income. OPEB--Other postemployment benefits.

## 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
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

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