Rating Action

S&P Global Ratings assigned its 'AA+' long-term rating to Credit River Township, Minn.'s series 2021A general obligation (GO) bonds. At the same time, we affirmed our 'AA+' rating on the township's existing GO debt. The outlook is stable.

The bonds are secured by the township's full faith credit and resources pledge, and an agreement to levy ad valorem property taxes without limit to rate or amount. Officials intend to pay debt service with special assessments, sewer subordinate service district fees, and ad valorem property taxes, but the rating is based on the unlimited ad valorem tax pledge. Proceeds will be used to finance various capital improvement and street projects, as well as improvements to community sewage treatment systems.

Credit overview

Situated as a southern outer-ring suburb of the Twin Cities, Credit River Township is a primarily residential community with high wealth, that gains economic and employment benefits from its location within the greater metropolitan statistical area (MSA). Currently, the township is in its final stages of incorporation and, following an election in June 2021, we expect it to be fully incorporated into the City of Credit River. Given that the township already adheres to many practices that we would expect from a city of its size, in addition to its already strong credit profile, we do not expect the incorporation to have any substantial effect on our rating.

Aside from certain preliminary costs associated with the incorporation that have led to general fund deficits in past years, the township's budget has remained stable overall. Further strengthening its financial profile is a historically high level of available reserves, which averaged 296% over the last three years. While a majority of these funds are held outside of the general fund, we still consider this a strength given the availability of these funds for operations based on a board decision. The stable rating outlook reflects our expectation that with operations remaining stable through the current year, reserves should remain at levels that are in line with those of peers; additionally, the township maintains a favorable debt profile and a strong economic profile, so we expect the rating to remain stable over the near term, even when considering the upcoming incorporation.

The 'AA+' rating reflects our assessment of the township'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 2020, which closed with operating deficits in the general fund and at the total governmental fund level in fiscal 2020;
- Very strong budgetary flexibility, with a high available fund balance in fiscal 2020 of 193% of operating expenditures;
- Very strong liquidity, with total government available cash at 145.2% of total governmental fund expenditures and 9.7x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 14.9% of expenditures and net direct debt that is 120.6% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 96.3% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Environmental, social, and governance factors

The rating also incorporates our view of the health and safety risks posed by the COVID-19 pandemic, which we consider social risk factors; absent the implications of COVID-19, we consider the city's social risks to be in line with those of the sector. We also view environmental and governance risks as being in line with our view of the sector as a whole.

Stable Outlook

Upside scenario

We could raise the rating if the local economy continues to expand and diversify, in addition to the township increasing and maintaining its general fund reserves well above levels that we consider nominally low.

Downside scenario

We could lower the rating if operations falter, causing combined reserves to decrease substantially, specifically if they fall below $500,000 due to planned or unplanned draws.

Credit Opinion

Very strong economy

We consider Credit River Township's economy very strong. The township, with a population of 5,572, is in Scott County, in the Minneapolis-St. Paul-Bloomington MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 155% of the national level and per capita market value of $188,887. Overall, market value grew by 3.1% over the past year to $1.1 billion in 2019.

The COVID-19 pandemic had essentially no effect on the township's economy; most residents work within the greater Twin Cities MSA and were able to shift to working remotely. Development has also fared well, with multiple new residential developments continuing, as the demand for housing remains strong. Unemployment at the county level peaked in May 2020 at 11.8%, but has since fallen to 4.1% (in March). (For more information on COVID-19's effect on the U.S. public finance sector, please see "Economic Outlook U.S. Q2 2021: Let The Good Times Roll," published March 24, 2021, on RatingsDirect). Residences make up most of the tax base, accounting for 93% for total net tax capacity. Given the township's continued growth and development, even throughout the pandemic, coupled with its proximity to the Twin Cities, we believe that our view of the local economy will remain very strong.

Strong management

We view the township'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 its revenue and expenditure assumptions for its annual budgets, Credit River examines multiple years of historical data to create its line-item budget. Management provides monthly reports to the board on budget-to-actual performance and investment holdings. The township has a formally adopted investment policy, that mirrors state guidelines. It also maintains rolling five-year long-term plans for capital and for the general fund. Its formal fund balance policy requires the maintenance of reserves between 33%-66% of operating expenditures, but the board likes to keep them above 50% for contingency purposes. The township lacks a formalized debt management policy.

Adequate budgetary performance

Credit River Township's budgetary performance is adequate, in our opinion. The township had operating deficits of 4.6% of expenditures in the general fund and 1.8% across all governmental funds in fiscal 2020. Our assessment accounts for the fact that we expect budgetary results could improve from 2020 results in the near term. In our analysis of budgetary performance, we removed one-time expenditures funded with bond proceeds.

While the township's operations have been mixed in recent years, showing two general fund deficits in the last three audited years, we understand that these draws have been due to one-time costs associated with the process to incorporate. Now that it is in the final stages of completing full incorporation, we expect to see the increased costs cease. Outside of these one-off expenses, the township's budget has been very stable.

Results for fiscal 2020 account for the receipt of roughly $423,000 in CARES Act funding, a portion of which was used within the fiscal year to invest in townwide broadband projects, as well as health and safety expenses. The fiscal year

2021 budget calls for a roughly $116,000 surplus (or 9.8% of expenditures) and, based on current tracking, management expects year-end (Dec. 31) results to be closely in line with the budget. The township additionally expects to get around $640,000 in American Rescue Plan (ARP) money, which is not included in budgetary projections.

The general fund benefits from a revenue structure that has historically been stable and predictable, consisting mostly of property taxes (62%); in fiscal 2020, intergovernmental revenue jumped significantly, accounting for 32% of general fund revenue due to the receipt of CARES Act money. We expect this amount to fall back to prior levels (nearly zero) in the budget and forthcoming years. We believe the township is well-placed to manage expenditures and make appropriate budgetary adjustments to maintain structural balance, even as debt costs rise within the next two years.

Very strong budgetary flexibility

Credit River Township's budgetary flexibility is very strong, in our view, with a high available fund balance in fiscal 2020 of 193% of operating expenditures, or $2.2 million. We expect the available fund balance to remain above 75% of expenditures for the current and next fiscal years, which we view as a positive credit factor. The available fund balance includes $511,000 (45.6% of expenditures) in the general fund and $1.7 million (148%) that is outside the general fund but legally available for operations.

We included road and bridge and capital improvement fund reserves as available given that both are available for general fund operations. We understand reserves are not earmarked for any projects and are available for operations and transfers back to the general fund at the township's discretion. (Revenues match or exceed expenditures in the road fund.) In fiscal 2020, general fund reserves alone made up 46% of general fund expenditures, but we expect this to increase in fiscal 2021 as the board opted to shift funds over from the road and bridge fund to get reserves back in line with its informal 50% target. Even given the small draws on general fund reserves in recent years, we expect that the township will maintain very strong budgetary flexibility.

Very strong liquidity

In our opinion, Credit River Township's liquidity is very strong, with total government available cash at 145.2% of total governmental fund expenditures and 9.7x governmental debt service in 2020. In our view, the township has strong access to external liquidity if necessary. Its $4.4 million in available cash and investments (after removing unspent bond proceeds) were held solely in bank deposits, so the township does not have any aggressive investments. It also does not have any contingent liquidity risk that could come due in the near term. It has issued GO debt multiple times within the past 20 years, supporting our view that it has strong access to external liquidity if needed. We believe that it has sufficient cash levels and will maintain a very strong liquidity profile.

Strong debt and contingent liability profile

In our view, Credit River Township's debt and contingent liability profile is strong. Total governmental fund debt service is 14.9% of total governmental fund expenditures, and net direct debt is 120.6% of total governmental fund revenue. Overall net debt is low at 2.9% of market value, and approximately 96.3% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors. Direct debt is calculated at $3.6 million. Typically, the township issues new-money GO debt every three years to keep up with projects in its capital plan. Given its history of maintaining a consistent debt profile with these regular issuances, we expect our view of its debt profile to remain unchanged over the near term.

Pensions and other postemployment benefits

Credit River Township's pension contributions totaled 0.2% of total governmental fund expenditures in 2020. The township made its full required pension contribution in 2020. It does not offer any other postemployment benefits.

We do not believe that pension liabilities represent a medium-term credit pressure, as contributions are only a modest share of the budget, and we believe the township has the capacity to absorb higher costs without pressuring operations. Credit River Township participates in one multiple-employer, defined-benefit pension plan that has seen recent improvements in funded status, though planwide statutory contributions have regularly fallen short of actuarial recommendations. Along with certain plan-specific actuarial assumptions and methods, this introduces some long-term risk of funding volatility and cost acceleration.

The township participates in the following plan:

- Minnesota General Employees Retirement Fund (GERF): 79.1% funded (as of June 30, 2020) with a township proportionate share of the plan's net pension liability of $66,000.

Total contributions to GERF were 89% of our minimum funding progress metric and were slightly above static funding. Annual contributions are based on a statutory formula that has typically produced contributions lower than the actuarially determined contribution for each plan. In our view, this increases the risk of underfunding over time if the state legislature does not make adjustments to offset future funding shortfalls. Other key risks include a 7.5% investment rate-of-return assumption (for both plans) that indicates some exposure to cost acceleration as a result of market volatility, and an amortization method that significantly defers contributions through a lengthy, closed 30-year amortization period based on a level 3.25% payroll growth assumption. Regardless, costs remain only a modest share of total spending, and we believe they are unlikely to pressure the township's medium-term operational health.

Strong institutional framework

The institutional framework score for Minnesota towns/townships with an annual audit in compliance with generally accepted accounting principles required by state statute is strong. After incorporation, we expect the institutional framework score to remain strong.