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Summary:

# Northvale, New Jersey; General Obligation

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## Table Of Contents

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| Credit Profile | | |
|---|---|---|
| US$5.685 mil gen imp bnds dtd 11/01/2019 due 11/01/2030 | | |
| *Long Term Rating* | AA/Stable | New |
| Northvale Boro GO | | |
| *Long Term Rating* | AA/Stable | Affirmed |

## Rationale

S&P Global Ratings assigned its 'AA' rating to Northvale, N.J.'s series 2019 general obligation (GO) general improvement bonds and affirmed its 'AA' rating on the borough's existing GO debt. The outlook is stable.

### Credit overview

Northvale's strong residential economy underpins its credit strength, supported by its access to the Manhattan and North New Jersey employment markets. Large overtime payouts and salary costs from a new position in fiscal year 2018 led to the borough drawing down $324,000 of its $832,000 in fund balance and issuing emergency notes, leading to an available fund balance position of just 5.7% of current fund expenditures. We understand operations have corrected in fiscal 2019, and we expect to see at least break-even results from a new administration. The borough has multiple potential opportunities to rebuild fund balance over the next two years, including the sale of borough-owned property to developers. A relatively strong long-term liability profile also affords it extra flexibility to strengthen its financial position. Over the next two years, we expect the borough will follow through on officials' stated intention to increase current fund balance at least back to the informal target of 10% of current fund expenditures.

The long-term rating reflects our assessment of the borough's:

- Very strong 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 a fund balance drawdown in the current fund in fiscal 2018;
- Adequate budgetary flexibility, with an available fund balance in fiscal 2018 of 5.7% of operating expenditures;
- Very strong liquidity, with total government available cash at 11.6% of current fund expenditures and 142.3% of governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 8.2% of expenditures and net direct debt that is 89.6% of current fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 66.5% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

### Security and use of proceeds

The borough's full faith and credit, including the requirement to levy ad valorem taxes on all taxable property within its borders without limitation as to rate or amount, secures debt service on the bonds. The proceeds of the $5.685 million bonds will be used to permanently finance $5.2 million of the borough's $6.6 million outstanding bond anticipation notes (BANs) and fund $511,000 of unfunded improvements.

### Very strong economy

We consider Northvale's economy very strong. The borough, with an estimated population of 4,967, is in Bergen County in the New York-Newark-Jersey City MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 133% of the national level and per capita market value of $199,207. Overall, market value grew by 1.8% over the past year to $989.5 million in 2018. The county unemployment rate was 3.4% in 2018.

The borough is mostly residential, accounting for approximately 68% of the assessed value. Industrial accounts for an additional 21%, and commercial 9%. There are several residential development projects in progress, including an 89-townhouse development called Northvale Greens and an additional development with duplex-style units proposed elsewhere in the borough. A new CubeSmart self-storage facility is currently in the construction phase; construction costs are expected to total $6 million. These developments should marginally increase the size of the tax base and allow the borough to generate additional revenue.

One of the borough's major taxpayers has filed a tax appeal, which we expect will result in a required settlement payment that could be in excess of $300,000 sometime in fiscal year 2019 or 2020. We understand the borough may request the state grant it the ability to finance the settlement period over two-to-three years.

### Adequate management

We believe the borough's management conditions are adequate, with standard financial practices under our FMA methodology, indicating our opinion that the government maintains adequate policies in some, but not all, key areas.

Management attempts to budget conservatively and examines two years of historical data to form expenditure assumptions, although we note that the borough has not consistently replenished all fund balance utilized in the budget. The governing body receives monthly budget-to-actual reports and makes budgetary transfers in the last two months of the year. The borough produces a three-year capital improvement plan as part of its budget process, although it does not produce a long-term financial plan. It adopts a cash management plan at the beginning of every year, and officials report cash balances on a regular basis. The borough does not have debt issuance or formal reserve policies. Officials informally want to maintain fund balance of at least 10% of expenditures, although current levels are approximately half that level.

### Weak budgetary performance

Northvale's budgetary performance is weak, in our opinion. Current fund operations drew down fund balance by 5.9% of expenditures in fiscal 2018.

The borough appropriated $665,000 of current fund balance into the budget as a revenue source, and only replenished $378,000 of that during fiscal 2018, even though the intention was to regenerate the entire amount. The year's budget reduced two Department of Public Works (DPW) positions and the addition of a fleet manager position, which had the dual effect of adding salary costs and requiring significant DPW overtime payouts. Public safety costs were also above budget related to expenditure choices and federal reimbursements, also leading to significant overtime payouts. Update documents show that ten of the borough's major spending line items required emergency authorizations, totaling $240,000 and prompting the borough to issue short-term notes that have since been repaid.

We believe the fiscal 2019 budget, which ends Dec. 31, likely incorporates better assumptions and expenditure choices than the ones that led to poor results for 2018. It utilizes $273,000 of fund balance in the budget, down from $665,000. Expenditures are performing well, and are expected to replenish $200,000-$300,000 of this amount by year-end. Revenues are also performing well in 2019, including unanticipated miscellaneous revenues that are so far $50,000 above expectations. We believe that if the borough is required to make a tax appeal settlement payment over the next year, it will be able to take advantage of a state law allowing it to raise tax revenues to finance the payment over several years. The district does not fund a reserve for tax appeals. We believe the pending settlement or judgment has the potential to weaken performance in 2019 and beyond.

Historically, Northvale's performance has remained around break-even over the past decade. The borough's revenue mix has historically been stable. We calculate that 78% of current fund revenues are from property taxes, and only 7% are from state aid. A new management team has stated that reducing deferred charges and rebuilding fund balance is a top priority. We will continue to monitor Northvale's performance, with continued fund balance drawdowns potentially triggering a downgrade.

### Adequate budgetary flexibility

Northvale's budgetary flexibility is adequate, in our view, with an available fund balance in fiscal 2018 of 5.7% of operating expenditures, or $508,000.

We exclude deferred charges from over-expenditures and special emergency authorizations from available fund balance because, New Jersey accounting nuance aside, the borough effectively used fund balance to finance these expenditures. We expect that fund balance will remain at least at this level at year-end 2019, supported by our view that performance may improve.

Management intends to sell a subdivided property over the next one-to-two years and use those funds to rebuild current fund balance. We estimate the sale could improve available fund balance to approximately 10% of expenditures, in line with the informal reserve target. On the other hand, further decreases in current fund balance would likely lead us to consider reserves nominally low and pressure the credit rating.

### Very strong liquidity

In our opinion, Northvale's liquidity is very strong, with total government available cash at 11.6% of current fund expenditures and 142.3% of governmental debt service in 2018. In our view, the borough has strong access to external liquidity if necessary.

The borough does not report any direct-purchase debt or contingent liabilities with tender options or immediate acceleration risk. Its investments are not what we consider aggressive as they consist of bank deposits.

### Strong debt and contingent liabilities profile

In our view, Northvale's debt and contingent liability profile is strong. Debt service is 8.2% of current fund expenditures, and net direct debt is 89.6% of current fund revenue. Overall net debt is low at 1.4% of market value, and approximately 66.5% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

Following this issuance, we calculate that the borough will have approximately $8 million in outstanding direct debt. We understand that it will likely continue to issue BANs in amounts not significantly exceeding principal payments on outstanding debt so that debt overall will not increase dramatically. Therefore we do not expect to change our view of the borough's debt.

Northvale's pension contributions totaled 6.5% of current fund expenditures in 2018. The borough made its full annual required pension contribution in 2018. It does not offer other postemployment benefits.

Northvale participates in the cost-sharing, multiple-employer Police and Firemen's Retirement System (PFRS) and Public Employees Retirement System (PERS). The reported plan fiduciary net position as a percentage of the total pension liability was 57.91% for PFRS and 40.45% for PERS as of June 30, 2018. While funding policies somewhat mitigate the risks for local governments of escalating contributions as a result of low plan funded ratios, Northvale could face escalating pension costs should the state not follow its schedule of increasing pension contributions. For more information on these risks, see our report "New Jersey Pension Funding: State Actions Reverberate At The Local Level," published Dec. 12, 2018 on RatingsDirect.

The borough's proportionate share of each plan's liability was about $3.1 million for PERS and $6.6 million for PFRS as of Dec. 31, 2018. As required by state statute, it paid its full annually required contribution to these plans. We believe that contributions may escalate during our outlook period despite the borough's best efforts to control costs.

### Strong institutional framework

We consider the institutional framework score for New Jersey municipalities to be strong.

## Outlook

The stable outlook reflects our expectation that Northvale will leverage its very strong tax base and better control costs to ensure balanced operations. Economic factors and low long-term liabilities, in our opinion, provide continued strength. Therefore, we do not expect to change our rating in the next two years.

### Downside scenario

We will consider lowering the rating if current fund balance continues to decrease, especially if performance indicates that budgets are not structurally balanced.

### Upside scenario

While unlikely, we could consider raising the rating if the borough maintained significantly higher fund balance while implementing financial policies and planning practices we consider likely to prevent future performance downturns.

## Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015