

**2012 Report on Rhode Island's
Local Government Debt
To the
Public Finance Management Board**

September 2013

State of Rhode Island and Providence Plantations

OFFICE OF THE GENERAL TREASURER

**GINA M. RAIMONDO
GENERAL TREASURER**

September 2013

Members of the Rhode Island Public Finance Management Board

Mr. Richard Licht, Director of Administration, State of Rhode Island
The Honorable A. Ralph Mollis, Secretary of State, State of Rhode Island
Mr. W. Lincoln Mossop, Jr., Public Member
Mr. Robert A. Mancini, Public Member
Mr. Edward F. Yazbak, Public Member
Mr. Steven Filippi, Public Member
Mr. Thomas M. Bruce, III, Public Member

Dear Members of the Board:

Enclosed is the 2012 Report on Rhode Island's Local Government Debt. This review of municipal debt is undertaken by the Public Finance Management Board ("PFMB") and is in compliance with Section 42-10.1-4.

Rhode Island officials recognize that the levels of local debt are significant in relation to the State's overall debt picture. The State has assumed debt for some functions that other states may have delegated to the local governmental level. Given this fact, local debt levels are lower than national averages and compare favorably to Standard & Poor's benchmarks. The comparison is less favorable for certain communities when pension obligations are included.

In continuing its commitment to municipalities, the General Assembly, with the support of Treasury, created the Municipal Road and Bridge Revolving Fund this past legislative session. Establishing a predictable, innovative and cost-saving alternative for cities and towns to finance their road and bridge improvements is an important cornerstone to building a vibrant economy for our state. The Rhode Island Clean Water Finance Agency administers this program with the support of the Rhode Island Department of Transportation.

The compiled municipal debt data shows:

- The average debt per capita for Rhode Island's cities and towns in FY12 was \$1,673 and has been categorized by Standard & Poor's as a low to moderate debt burden.
- The compound annual growth rate (CAGR) in local debt from FY07-12 (below) was partially balanced by a smaller 2.9% CAGR in State debt during the same period.
- During the period FY07-12, general obligation debt and capital leases grew at a CAGR of 3.3% a decrease from the CAGR of 4.9% from FY06-11.
- Total long-term obligations, which include not only general obligation debt and capital leases, but also accrued vacation time, unfunded claims, and accrued pension liabilities, also grew. During the period FY07-12 total long-term obligations grew at a CAGR of 6.7% a decrease from the CAGR of 6.9% from FY06-11.

The information in this report was derived from the fiscal year 2007 through 2012 comprehensive annual financial reports of the state's 39 municipalities, the Office of Municipal Affairs, the R.I. Division of Taxation, the United States Census Bureau, and Moody's Investors Service, Inc. We rely on the municipalities' audited financials, as well as, the opinion of their independent auditors as to the compliance with generally accepted auditing standards and government auditing standards. This report offers no further opinion as to the information's accuracy or compliance.

This local debt report is a supplement to the Report on Debt Management to the Public Finance Management Board, the "State Debt Report". The State Debt Report reviewed all of the State's outstanding debt, analyzed projected debt levels and made recommendations for future debt practices. To review a copy of this report, please contact my office or download the report from our web site (www.treasury.ri.gov).

Sincerely,

A handwritten signature in black ink that reads "Gina Raimondo". The signature is written in a cursive style with a loop at the end of the last name.

Gina M. Raimondo
General Treasurer

PUBLIC FINANCE MANAGEMENT BOARD

Date: September 30, 2013

To: Honorable Chair and Members of the Public Finance Management Board

From: Chris Feisthamel, Chief Operating Officer
Paul Goslin, Debt Analyst

Subject: Public Finance Management Board (“PFMB”)
Debt Report Update: Rhode Island’s Local Government Debt

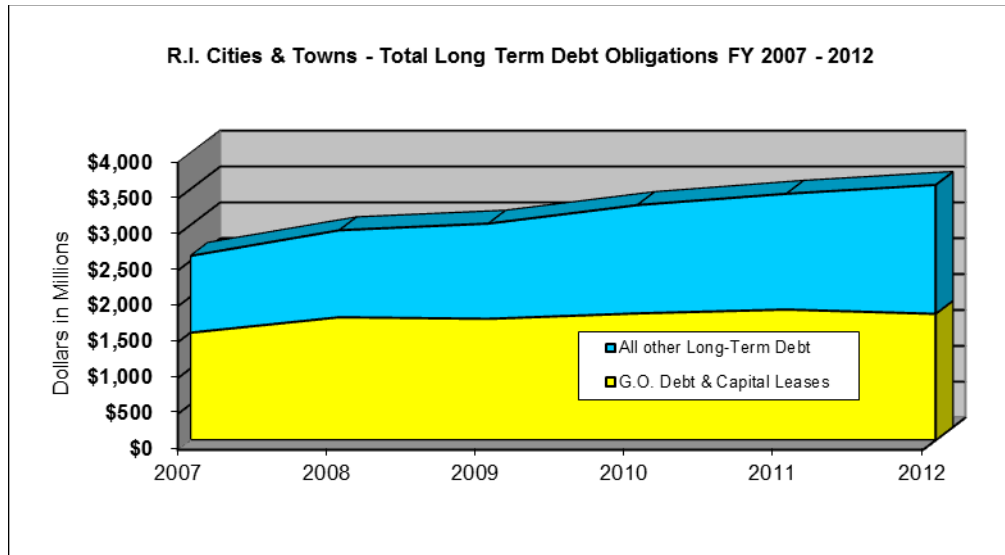
In September 2013, the PFMB published its annual Report on Debt Management (“State Debt Report”). This State Debt Report provides a comprehensive review of State, State Agency and Quasi-Public Corporation debt. According to **R.I.G.L. §42-10.1**, the PFMB’s comprehensive annual debt review is to also include an analysis of the State’s local governmental unit debt. This memorandum provides the required summary analysis of the debt profiles of Rhode Island’s cities and towns.

Rhode Island’s high level of State debt is partially the result of certain governmental functions being assumed at the State level, which in other states might be delegated to the local or county governmental level. Examples of this include the State’s convention center and correctional facilities. This argument implies that Rhode Island’s local governments should be relieved of a significant debt burden relative to municipalities in other states. This continues to be true for the majority of Rhode Island cities and towns.

The principal findings of this report are summarized below:

Growth of Long-Term Obligations of RI Cities and Towns is Stabilizing

As shown in the following graph, total long-term obligations have increased from \$2.57 billion in 2007, to \$3.56 billion in 2012, which represents an annual compound growth rate of 6.73%. General obligation (G.O.) debt and capital leases, which comprise the largest components of total long-term debt, increased by \$262.8 million from a total of \$1.5 billion in 2007 to \$1.76 billion in 2012. R.I. cities and towns total G.O. debt and capital leases grew at a compound annual growth rate of 3.28%. The State’s compound annual growth rate was 2.91%, in line with the 2.22% growth rate of RI’s personal income over this period. The local governments with the fastest compound annual debt growth rates since 2007 include North Smithfield (46.6%), East Greenwich (45.7%), Narragansett (19.9%) and Richmond (14.0%). In terms of absolute dollar growth, several cities and towns have added significantly to their outstanding debt in the last five years. These include the following cities: Providence (\$99.5 million), Woonsocket (\$71.2 million), East Greenwich (\$54.2 million), North Smithfield (\$29.7 million) and Westerly (\$18.6 million). It should be noted that many of the bonds were issued for school purposes for which the municipalities receive state aid. Over the same period, sixteen municipalities have reduced outstanding debt, most notably, Warwick (-\$20.8 million) and South Kingstown (-\$16.5 million).



The local governments with the most G.O. and capital lease debt include Providence (\$582.8 million), Woonsocket (\$192.8 million), Cranston (\$85.4 million), Westerly (\$84.6 million) and East Greenwich (\$63.9 million). The communities with the lowest debt levels outstanding include Foster (\$48,533), Little Compton (\$689,884) and Exeter (\$1,255,420).

Additional debt has been issued in most cases to fund investment in infrastructure, such as schools, roads, water supply, waste water treatment systems and community development. As previously noted, a revolving fund for local roads and bridges improvements was designed by the Office of the General Treasurer and the General Assembly during the 2013 legislative session. This program will be administered by RI Clean Water Finance Agency and supported by RIDOT.

Debt growth rates might appear to be high for certain cities or towns because they may have had minimal amounts of G.O. debt and capital leases outstanding in 2007. The town of Foster, for example, had outstanding G.O. debt and capital leases in 2007 of only \$47,879 (see Appendix B). An increase from such a nominal level of debt outstanding would necessarily show a high rate of growth, but might not necessarily be a significant increase in absolute dollars. For this reason, it is important to look at absolute dollar growth, as well as the annual growth rate of debt.

Analysis of debt levels relative to population trends is also important. Estimates provided by the Rhode Island Division of Statewide Planning for 2005 and 2010 indicate a decrease in the compound annual growth rate of -0.93%.

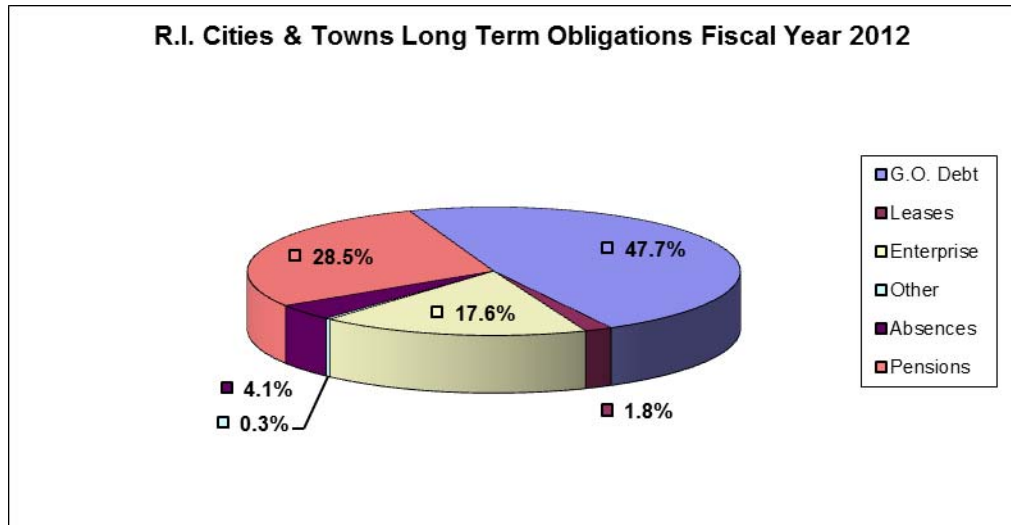
General Obligation Debt Accounts for 47.7% of Total Long-Term Obligations

The definition of long-term obligations has been expanded in recent years to include unfunded judgments, claims and accrued pension liability as well as accrued vacations, absences and deferred compensation along with G.O. bonds, loans and notes, and capital leases. As shown in the chart on the following page, most long-term obligations consist of G.O. bonds, loans and notes payable (\$1.70 billion or 47.7% of total debt) typically approved by voter referendum.

The second largest category at 28.5% is unfunded claims, judgments and accrued pension liability debt (\$1,013.1 million). Pressure to incur additional debt was somewhat relieved when the General Assembly passed the Rhode Island Retirement Security Act (RIRSA) on November 17, 2011. The changes to various state-administered retirement plans not only reduced the unfunded liability and the actuarially required contribution but served to

improve the overall debt and liability picture for those municipal plans in the Municipal Employee Retirement System (MERS)

The next largest obligation was the enterprise fund debt, which typically is self-supporting at 17.6% (\$626.4 million). Absences, vacations and deferred compensation, represent 4.1% of long-term obligations and capital leases represent 1.8%. Finally, other debt, (\$11.8 million), includes items such as provisions for landfill closure costs, special purpose bonds or other types of debt.



Statewide figures for non-general obligation debt are somewhat skewed, as only a handful of cities and towns comprise the majority of this type of debt. The City of Warwick accounts for 19.1% of all outstanding enterprise fund debt, while Pawtucket has 16.8% of all enterprise debt. Both communities' enterprise fund debt is self-supporting from water or wastewater revenues. Providence represents 31.9% of the unfunded claims, judgments and accrued pension liability, followed by the City of Pawtucket (15.0%) and Cranston (10.2%).

Tax-Supported Debt Capacity Ratios

Summary financial data was obtained from the FY07-12 audited financial statements of each city and town. The FY12 audited financial statements are the most current available for all cities and towns. Population figures are based on the official 2010 census figures from the U. S. Census Bureau, Washington, D.C. and the R.I. Division of Statewide Planning. Property valuations are based on the equalized weighted assessed full valuations of each city and town, averaged from 2009 - 2011.

In general, population and property valuation data may lag actual conditions by several years. Despite the lag in available data, it provides a relevant analysis that allows for comparative debt ratio analysis.

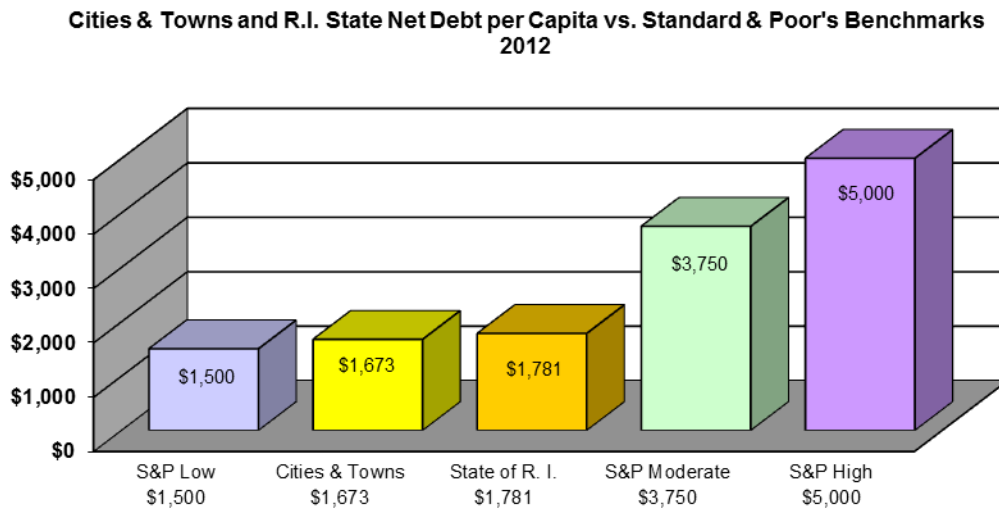
To analyze the relative debt burden for cities and towns, we examined certain debt ratios, which revealed the following:

Tax-Supported Debt Per Capita on the Rise

As shown in the chart on the following page, the average debt per capita for RI's cities and towns is \$1,673, which is categorized by Standard and Poor's as "low" to "moderate" debt burden. In prior years R.I. cities and

towns were categorized as having a “low” debt burden. The cities and towns with the highest debt per capita include areas of the state with relatively low population, such as New Shoreham (\$20,070) and East Greenwich (\$4,860). However, relatively high population does not necessarily mean low debt per capita. Two cities with high absolute debt also had high debt per capita relative to the other communities: Woonsocket (\$4,682) and Providence (\$3,273). The communities with the lowest debt per capita were Foster (\$11), Exeter (\$195) and Little Compton (\$198). It should be noted that the debt per capita includes all school debt and does not reflect the reduction in debt burden due to the State School Construction Aid. Some towns participate in regional school districts (Foster/Glocester, Exeter/West Greenwich and CHARIHO) and share school debt with the other district communities.

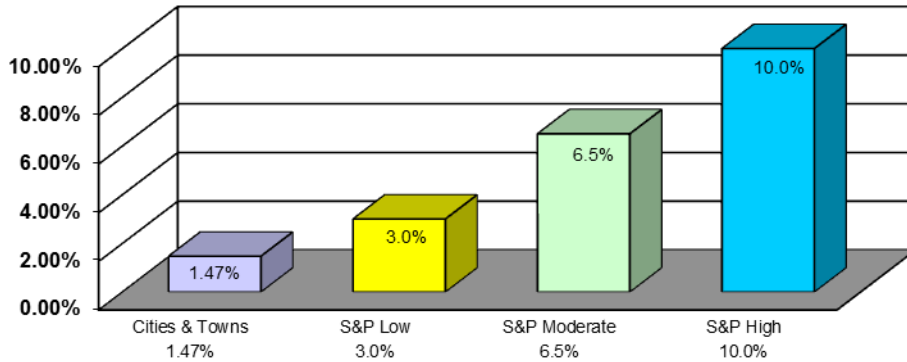
S&P’s benchmarks for Debt per Capita along with R.I. Cities and Towns debt levels are shown in the graph below.



Tax-Supported Debt as a Percent of Property Valuation Compares Favorably to S&P Benchmarks

Debt as a percent of property valuation is a measure often cited by the rating agencies as an indication of ability to incur indebtedness. Treasury has attempted to measure property wealth through the equalized weighted assessed full valuation, averaged over a three-year period 2009 - 2011. The Rhode Island Department of Administration, Office of Municipal Affairs provided property valuation figures. Taking this property valuation estimate as a percentage of outstanding debt reveals that the statewide average is 1.47%, well below the S&P benchmark range of 3.0% - 6.0%. Woonsocket (14.2%), Providence (8.1%) and Central Falls (6.8%), carry the highest debt burden by this measure. Foster (0.01%), Little Compton (0.03%) and Exeter (0.11%) have the lowest ratios. The equalized weighted assessed valuation is adjusted for the median family income in each city and town. Therefore, it is not directly comparable to the S&P market value calculation; however, it provides a closer comparison than the actual assessed valuation. S&P’s benchmarks for overall net debt to market value as compared to the Rhode Island Cities and Towns debt to equalized full valuation are represented in the chart below.

**R.I. Cities & Towns Debt to Market Value vs. Standard & Poor's Benchmarks
2012**



Tax-Supported Debt as a Percent of Adjusted Gross Income is within PFMB Guideline Range

Personal income is often compared to debt as a measure of affordability. However, personal income is tracked by the federal government by region, not by city or town. For this reason, the Rhode Island Division of Taxation extracted information from the State taxation database to determine the level of reported adjusted gross income by city and town for 2011. Treasury then computed the ratio of local debt to adjusted gross income. The statewide average was 6.82% in 2012. The State's net debt to personal income ratio was 4.0% in FY12, below the PFMB's guideline range of 5% to 6%. The cities and towns with the highest ratios included New Shoreham (61.3%), Woonsocket (31.2%) and Providence (19.1%). The cities and towns with the lowest ratios included Foster (0.03%), Little Compton (0.55%) and Exeter (0.66%).

Debt Burden of Cities and Towns

From the data obtained, all Rhode Island cities and towns were analyzed based on six debt factors. Three of the factors were based on FY12 financial statements and three were based on growth from FY07-12. Please see Appendix A. The debt factors include:

Net Debt Growth by Net Dollar Change - examines the increase or decrease in the total long-term debt on an absolute basis.

Net Debt Compound Annual Growth Rate - examines the rate of increase or decrease in the amount of long-term debt on a percentage basis.

Debt as a Percentage of Equalized Weighted Assessed Valuations - ranks long-term debt as a percentage of the assessed property values. Because property valuation is not standardized across the State, a three-year average from 2009 to 2011 was used.

Dollar Change in Debt per Capita - examines the increase or decrease in the amount of debt for each city or town divided by the population.

Debt as a Percentage of Adjusted Gross Income - determines debt affordability based on the income of tax paying residents.

Debt per Capita - total long-term debt of each city or town divided by the population.

Economic growth typically requires added public investment in the form of debt for infrastructure improvements. Also, certain cities and towns may be infrequent borrowers, which might serve to spike the results upward, if compared within a limited time frame and the city or town in question has recently financed a major project (between 2007 and 2012, for example). In addition, special circumstances not explained by the rankings would include bonds issued for tax synchronization or school bonds subject to state reimbursement.

Other Categories of Long-Term Obligations on Upward Trend

Two other categories of long-term obligations are not considered to be G.O. debt. These include (1) absences, vacation and deferred compensation and (2) unfunded claims, judgments and accrued pension liabilities. Our data indicates that the 2012 total impact of these obligations was \$1.160 billion, which is 32.6% of the total of all long-term obligations. This represents a 96.8% increase from 2007 when these obligations totaled \$589.3 million or 22.9% of all long-term obligations. The Cities of Johnston and Central Falls have a disproportionate share of their total long-term debt categorized as unfunded claims, judgments and accrued pension liability at 67.8% and 65.0% respectively. The total of all non-general obligation debt has increased from \$1.071 billion or 41.7% of total long-term debt in 2007 to \$1.798 billion or 50.5% of total long-term debt in 2012. While significant, part of this increase may be attributable to the implementation of GASB Statement 45. This accounting standard requires municipal governments to report the liability associated with post employment benefits to retirees, including health insurance.

Conclusion

The average debt per capita for Rhode Island's cities and towns is in the low to moderate range based on S&P's benchmarks for local government debt, while the percentage of debt to property valuation for Rhode Island's cities and towns is lower than S&P's benchmarks. For this reason, this analysis validates by quantification at least one of the State Debt Report assumptions for relatively high State debt. However, it should be noted that (1) debt growth rates are not uniform across Rhode Island local governments; (2) other long-term obligations also have a significant financial impact on Rhode Island's cities and towns; and (3) the compound annual growth rate of total long-term local government debt (6.7%) is three times the rate of inflation (2.2%) as measured by the consumer price index (CPI) for the Northeast during the period 2007 – 2012. These three factors should be of continuing interest to the Board, as the financial condition of cities and towns has a substantial, if indirect, impact on the State government.

Treasury extends its thanks to the Division of Taxation, the Office of Municipal Affairs, the Division of Statewide Planning and the State's financial adviser, First Southwest Company, for their help in gathering the statistical data used to compile this report.

Attachments

Appendix A	Ranking of RI Municipalities Based on Six Debt Factors
Appendix B	City and Town Financial Data
Appendix C	Description of RI Property Valuation Methodology
Appendix D	Standard and Poor's Key G.O. Ratio Credit Ranges, April 2008 Moody's Special Comment – 2011 Local Government Medians
Appendix E	RI Municipal Credit Ratings, September 2013
Appendix F	Summary of Debt Issuances