Moody's
INVESTORS SERVICE

Rating Update: Moody's revises outlook on Woonsocket, RI's GO rating to stable

Global Credit Research - 26 Jun 2014

Affirms B3 on $216.9M in outstanding long-term debt

WOONSOCKET (CITY OF) RI
Cities (including Towns, Villages and Townships)
RI

Opinion

NEW YORK, June 26, 2014 --Moody's Investors Service has affirmed the City of Woonsocket's (RI) B3 general obligation unlimited tax rating, affecting $216.9 million of outstanding debt, including GO-secured debt issued through the Rhode Island Health and Education Building Corporation (RIHEBC). At this time, Moody's has revised the outlook to stable from negative.

SUMMARY RATING RATIONALE

The B3 rating reflects an accumulated operating deficit and annual liquidity shortages, despite the issuance of deficit funding bonds in fiscal 2011 and a state-appointed budget commission. State oversight has provided the city with advances of future state aid and helped pass a supplemental property tax levy in fiscal 2013. The rating also factors a high debt burden with large, unfunded pension and OPEB liabilities.

The stable outlook reflects recent progress that the city has made in implementing substantial operating expenditure cuts while simultaneously raising revenues to eliminate the large accumulated deficit and obtain structural balance in accordance with the newly adopted deficit reduction plan. The stable outlook also considers the city's improved liquidity given recent expenditure cuts and its ability to borrow from other funds and advance state aid.

STRENGTHS

-State-appointed oversight commission with ability to advance state aid revenue

-Recent stabilization in the city's operating funds

CHALLENGES

-Ongoing liquidity strain necessitates state aid advances

-Very high debt burden and unfunded pension and OPEB liabilities

-High fixed costs

DETAILED CREDIT DISCUSSION

BUDGET COMMISSION MITIGATING ACCUMULATED DEFICIT AND DEPLETED LIQUIDITY

The city experienced a decade of annual operating deficits through fiscal 2012, resulting from School Fund deficits, rising debt service, increasing pension costs, significant state aid cuts and a stagnating regional economy. Under the state-appointed budget commission, the city generated an operating surplus in fiscal 2013 and projects another surplus in fiscal 2014. The city reduced the total accumulated operating deficit (includes General and School Funds) to $3.2 million, or -2.5% of operating revenues in fiscal 2013, from $6.5 million, or -5.3% of revenues in fiscal 2012.

In July of 2013, the state legislature approved a $2.5 million supplemental tax levy to address the city's liquidity strain. The city had expected a significant cash deficit just days before the $4.8 million debt service payment on its pension obligation bonds came due on July 15, the second such shortfall in two years. The budget commission, made up of 5 members including the Mayor, City Council President, and three appointees by the State Director of

Revenue, will again request an advance of $8.9 million of state aid in early July 2014 (originally scheduled to be paid in May and June of 2015). This advance is reduced from the $12 million of state aid (originally scheduled for April, May and June of fiscal 2014) that the state advanced in July of 2013. The acceleration of future aid alleviates near term liquidity needs, but also narrows liquidity in the latter half of the fiscal year. The city also borrowed $2 million from its sewer funds this month, which it plans to pay back in November. The city has not accessed the market for cash flow borrowing.

The fiscal 2013 budget was adopted with a 3.9% property tax levy increase and a $7 million funding gap, which the city expected to address through personnel and other expenditure cuts. Although the full potential of the supplemental levy was not recognized in time, the city ran an operating funds surplus of $3 million. A General Fund deficit of $2.7 million deficit was largely due to a year-end transfer to the School Fund to reduce its accumulated deficit. The additional funding contributed to a School Fund surplus of $5.7 million, as did increased state aid and expenditure savings for unfilled positions. Total operating revenues were primarily comprised of property taxes (46.4%) and state aid (46.4%).

The fiscal 2014 budget included a 4% levy increase and assumes savings from health care benefit reductions and a pension COLA freeze on the city's police and fire pension plan. Although the city has obtained settlement agreements with six of its seven bargaining units that include cuts to benefits, one public safety union has not accepted the terms. Its contract expires on June 30, 2014. Management projects a $2 million operating surplus by year end, further reducing the accumulated deficit. The operating surplus includes a $1 million surplus in the General Fund and a $1 million surplus in the School Fund, both generated through the use of health insurance expenditure cuts, agreements reached with six of the City's seven bargaining units, and a combination of agreements and budget commission enactments for retirees.

The fiscal 2015 budget includes a 4.8% levy increase and was passed in adherence with the budget commission's five-year plan, which aims to eliminate the accumulated deficit by fiscal 2017.

TAX BASE GROWTH EXPECTED TO REMAIN SLOW

Located 15 miles north of the City of Providence (rated Baa1 stable), growth in the city's tax base is expected to lag, reflecting the slow pace of economic recovery in the region and the city's high 8.8% unemployment rate as of April 2014. The city's $1.6 billion tax base experienced a substantial 29% reduction in full values from fiscal 2009 through fiscal 2015, reflecting a decline in home values. The CVS/Caremark Corporation (rated Baa1 stable) is the city's largest employer, providing 5,780 jobs and contributing 4.2% of assessed value; the company completed a $40 million expansion in fiscal 2010. Landmark Medical Center, the city's second largest employer, has been acquired by a private hospital corporation and will be added to the city's tax rolls in fiscal 2015, adding an estimated $900,000 of property tax revenue in fiscal year 2015, which is expected to increase in fiscal year 2016 and beyond after the completion of $40 million in upgrades. Overall, the top ten taxpayers represent a slightly concentrated 9.4% of the city's assessed value. Wealth and income indices remain below state and national medians, with median family income representing 75.6% of the US median. The city's poverty rate is high at 19.4% and full value per capita is also below the state level at $39,035.

SUBSTANTIAL DEBT POSITION LARGELY REFLECTIVE OF OUTSTANDING PENSION AND DEFICIT BONDS

The city's high 11.8% direct debt burden largely reflects $90 million in Pension Obligation Bonds (POBs), Series 2002 and $11.5 million of deficit bonds issued in 2011. Debt burden will remain elevated given slow amortization of principal (44.3% retired within 10 years), reflecting the principal retirement schedule of the POBs. Net of 74% state aid reimbursement on eligible school-related debt, the adjusted debt burden is a still-high 7.9% of full value. Debt service comprised a significant 15.1% of operating expenditures in fiscal 2013 and adjusts down to 12.7% of operating expenses net of school construction aid. The city plans to issue an estimated $30 million of revenue bonds through the Rhode Island Clean Water state revolving fund over the next three years to fund water and sewer facility upgrades; debt service is expected to be self-supporting through user fees. All of the city's outstanding debt is fixed rate and the city is not party to any derivative agreements.

The city maintains five separate pension plans with a combined adjusted net pension liability, under Moody's methodology for adjusting reported pension data, of $253 million, equivalent to a substantial 12.5% of full value or 1.8 times operating revenues. Moody's uses the adjusted net pension liability to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities. The city's locally administered Police and Fire Pension Plan reported a funded ratio of 59% as of July 2013, and is classified as "at risk" by the State Auditor General's office. The city issued $90 million of pension obligation bonds (POBs) in 2002, and the plan maintained a funding ratio of

101% through fiscal 2008. Four years of severe underfunding, beginning in 2008 and compounded by poor investment performance, reduced funding status to 57% as of the 2012 actuarial valuation. The city funded 100% of its $3.4 million ARC in fiscal 2014 and plans to continue full funding in future years.

The city finances its Other Post Employee Benefits (OPEB) on a pay-as-you-go basis, amounting to $4.4 million, or 3.7% of operating expenditures for both the city and schools in fiscal 2013. Woonsocket's unfunded OPEB liability is sizeable at $205 million, one of the largest unfunded liabilities in the state, and is expected to be reduced considerably during future valuations given recent changes to healthcare benefits.

OUTLOOK

The stable outlook reflects recent progress that the city has made in implementing substantial operating expenditure cuts while simultaneously raising revenues to eliminate the large accumulated deficit and obtain structural balance in accordance with the newly adopted deficit reduction plan. The stable outlook also considers the city's improved liquidity given recent expenditure cuts and its ability to borrow from other funds and advance state aid.

WHAT COULD MAKE THE RATING GO UP:

- Improvement in liquidity and reduced dependence on state aid advances

- Sustained elimination of accumulated deficit in the Operating Funds

- Progress toward reducing the large unfunded pension liability

WHAT COULD MAKE THE RATING GO DOWN:

- Inability to secure state aid advances in the event of future liquidity shortfalls

- Continued severe liquidity strain

- Deepening of the accumulated operating deficit

KEY STATISTICS:

Full Value, Fiscal 2015: $1.6 billion

Full Value Per Capita, Fiscal 2014: $39,035

Median Family Income as % of US Median (2012 American Community Survey): 75.6%

Fund Balance as % of Revenues, Fiscal 2013: -2.7%

5-Year Dollar Change in Fund Balance as % of Revenues: -2.58%

Cash Balance as % of Revenues, Fiscal 2013: 4.24%

5-Year Dollar Change in Cash Balance as % of Revenues: 3.27%

Institutional Framework: "A"

5-Year Average Operating Revenues / Operating Expenditures: 0.99x

Net Direct Debt as % of Full Value: 11.8%

Net Direct Debt / Operating Revenues: 1.52x

3-Year Average ANPL as % of Assessed Value: 16.65%

3-Year Average ANPL / Operating Revenues: 2.1x

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

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MOODY'S
INVESTORS SERVICE

FitchRatings

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

Ratings Endorsement Policy
10 Jul 2013 4:34 PM (EDT)

Fitch Ratings-New York-10 July 2013: Fitch Ratings has taken the following action on the City of Woonsocket RI's (the city) outstanding general obligation (GO) bonds:

--$115 million GO bonds affirmed at 'B'.

The Rating Outlook has been revised to Stable from Negative.

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 IMPLEMENTING FISCAL STABILIZATION INITIATIVES: The revision in the Outlook to Stable from Negative reflects progress in implementing key objectives in a five-year deficit reduction plan including labor concessions and a supplemental tax levy approved by the state legislature.

CITY BENEFITS FROM STATE OVERSIGHT: Fitch views state oversight of the city via the Budget Commission (the commission) positively, though an indication of the severity of the city's fiscal problems. The commission's support in restructuring city finances and stabilizing liquidity will continue to be key to the city's fiscal recovery.

CONTINUED FINANCIAL CONSTRAINTS; LIQUIDITY CONCERNS: The low 'B' rating reflects the city's continued fiscal pressure driven by a weak economy, prior exposure to school deficits with minimal budget control, the state-wide property tax cap, and underfunding of retiree obligations. Liquidity remains an issue, although in the near term, has been addressed 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 pay-go, 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.

ABILITY TO ADDRESS CUMULATIVE OPERATING DEFICITS: The ability to address school and city accumulated operating deficits adequately as planned would lead to a rating upgrade.

CREDIT PROFILE

Woonsocket is located 15 miles outside of Providence. The city's population of 41,000 in 2012 has declined by about 5% since 2000.

MULTI-YEAR DEFICIT REDUCTION PLAN ESSENTIALLY ON TRACK

The city developed a five-year plan to reduce and ultimately eliminate projected cumulative school and city operating deficits by fiscal year 2017. Major components of the plan were reliant on state legislative approval, including city pension-related legislation that lengthened the pension plan's amortization schedule (approved earlier this month), and a supplemental tax bill expected to yield an estimated $2.5 million in additional annual revenue (about 2% of fiscal 2012 general fund revenue). The supplemental tax bill was also approved but amended to be conditional on the achievement of $3.75 million in savings related to union concessions and retiree savings. The city is currently projecting $4.7 million in such savings, representing 6.5% of fiscal 2012 expenditures and transfers out.

The deficit reduction plan assumed employee and retiree health care savings, some of which related to union contract revisions that needed to be negotiated. As a back-up in case concessions were not received, the commission enacted these revisions by resolution for the six (out of a total of seven) municipal unions whose contracts expired on July 1, 2013. Concessions were ultimately gained from five of the seven municipal unions. Negotiations continue with the police and fire fighter unions, and a legal challenge to the commission's attempt to implement retiree savings via resolution has been filed by a small police department retiree group.

The plan also assumed increased savings from departmental reorganization and consolidation and increased charges for trash collections. The plan's estimated state aid levels were based on the governor's proposed fiscal 2014 budget plan. The final state budget featured lower state aid revenues than projected in the deficit reduction plan, which contributed to a larger fiscal year 2014 cumulative operating deficit than originally estimated in the deficit reduction plan.

Current budget estimates appear reasonable and, assuming implementation of the city's five-year deficit reduction plan excluding savings associated with the fire fighter union concessions, indicate a fiscal year 2013 cumulative city and school fund deficit of approximately $8.2 million, or 6% of expenditures. The cumulative deficit declines to $7.1 million in fiscal year 2014 and, under full implementation of the plan, operations would yield a positive position by fiscal year 2017. Final deficit figures, however, will depend on actual revenue and expenditure performance, the outcome of remaining negotiations with the fire fighter union, and any potential impact from legal challenges.

SECOND YEAR OF STATE AID ADVANCE

Preliminary combined city and school cash flows absent the impact of any of the deficit reduction plan initiatives or the state aid advance indicated a positive monthly ending cash balance from June 2013 through August 2013. The city's cash position benefitted highly from a prepayment by CVS Corporation in June of its $2.8 million fiscal year 2014 property tax bill. CVS is the city's largest taxpayer. In addition, the city slowed payments on vendor obligations but expects to catch up with overdue payments (about $7 million) by August 2013. Even with these provisions, the city still needed the state aid advance by early July to cover a mid-July deficit following the city's $4.7 million debt service payment due on the 15th. The debt service payment was actually made earlier, on July 8th.

Based on the preliminary cash flows, monthly ending cash balances are positive through April 2014 following the state aid advance, but the projected fiscal year end June 30, 2014 balance shows a cash deficit estimated at $8 million. Fitch expects that the final cash balance figure will likely improve from the $8 million deficit projection, reflecting the impact of the deficit reduction plan components that have been successfully implemented and the supplemental tax levy. Even with deficit reduction measures and the supplemental tax levy in place, the city may require some additional liquidity support, with options available to the city including issuance of tax anticipation notes, payment deferrals, advanced state aid or tax payments.

FISCAL YEARS 2011 AND 2012 PLAGUED BY SCHOOL FUND DEFICITS

Following significant cuts in state aid and a weak economy, Woonsocket has been hurt over the last three years by overspending by school department officials. The city's budget, as in all Rhode Island communities, is generally exposed to school budget deficits with little control over school budget adoption. School expenditure needs have driven increased overall spending leading to growing operating deficits. While the general fund ended fiscal year 2011 positively (unrestricted fund balance of $2.4 million or 3.1% of general fund spending) after prior year deficits, the unrestricted school fund balance was a negative $3 million (4.6% of school fund spending).

City and school officials labored to compile accurate fiscal year 2012 cash flow and expenditure information for the school fund, which again ended the year in a deficit position. The fiscal year 2012 school fund unrestricted deficit balance totaled $9.8 million (14.2% of spending). The general fund unrestricted balance was positive at $2.6 million or 3.7% of spending.

LONGER-TERM FINANCIAL CHALLENGES

Fitch has been concerned about the ability of the city and school department to implement changes that will meaningfully improve financial stability given that prior efforts have not always yielded intended results. However, Fitch believes commission oversight, recent closer integration of city and school operations, and a developed and largely implemented deficit reduction plan could lead to more effective fiscal management.

The city's revenue raising flexibility is limited due to statutory annual tax cap levy of 4% over the prior year's levy. The city was able to exceed the tax cap limit in fiscal year 2011 with approval by 4/5ths of city council to make up for cuts in state aid revenues.

WEAK SOCIOECONOMIC INDICATORS

The city's unemployment rate continues to be elevated at 11.4% for May 2013, as compared to 9.2% for the state and 7.3% for the nation. Employment was flat in 2012 after prior year declines, but May year over year figures show growth of 1.4%. Between 2000 and 2012, the city's population declined by about 5%, while the state's increased by less than 1% and the nation's grew by about 11.5%.

Woonsocket benefits from the presence of CVS Caremark Corporation, which maintains its headquarters in the city. CVS is the city's largest employer, with about 3,000 workers, and the largest taxpayer (4% of taxable assessed value). 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.

HIGH DEBT RATIOS AND UNDER-FUNDED PENSIONS

Overall debt ratios are generally high, net of debt service reimbursements on the city's public school revenue bonds issued by the Rhode Island Health and Education Building Corporation, with debt to market value at 5.6% and debt per capita more mid-range at $3,053. Annual debt service as a percentage of operational spending was a high 14% in fiscal year 2012.

The city administered police and fire pension plan is funded at a low 57%, assuming a 7.5% rate of return, with an unfunded liability of $43 million at July 1, 2012 or 2% of market value. The 2012 funded ratio declines to 54% using a Fitch-adjusted 7% rate of return estimate. The city has historically underfunded the actuarially required contribution (ARC) for the city administered pension plan. Funding in fiscal years 2012 and 2011 represented 28% and 36% of the ARC in those years, respectively. Total pension ARC, OPEB pay-go and debt service payments were high at 26% of fiscal year 2012 operational spending.

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In addition to the sources of information identified in Fitch'sTax-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).

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria
U.S. Local Government Tax-Supported Rating Criteria

Additional Disclosure
Solicitation Status

FitchRatings

Fitch Downgrades Woonsocket, RI's GOs to 'B'; Outlook Negative

Ratings Endorsement Policy

31 May 2012 4:40 PM (EDT)

Fitch Ratings-New York-31 May 2012: Fitch Ratings takes the following rating action on the City of Woonsocket, RI's (the city) outstanding general obligation (GO) bonds:

--$118 million GO bonds downgraded to 'B' from 'BB-';

The Rating Outlook is Negative.

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

CONTINUED SCHOOL FUND DEFICIT OPERATIONS: The downgrade to 'B' from 'BB-' reflects financial stress due to ongoing school fund deficit operations and liquidity issues, which the city sought to alleviate with a proposed supplemental tax bill that has now stalled in the state legislature. Supplemental tax proceeds were meant to cover significant school cashflow needs through June 30th and support fiscal year 2013. The city is projecting a cumulative negative school fund balance at the end of fiscal 2012 of about $10 million or 7.6% of general fund and school fund spending. Alternatives to address current year liquidity issues and the cumulative budget deficits are still to be determined.

NEGATIVE OUTLOOK: The Negative Outlook reflects the likelihood of continued long-term fiscal pressure as the city attempts to bring its finances back into balance. Fitch views the implementation of a state Budget Commission positively, as it may provide greater options to address the city's school fund fiscal imbalance. Fitch will continue to monitor the credit and take rating action as appropriate.

INTERNAL CONTROL DEFICIENCIES: Deficiencies in internal fiscal controls of the school department, an autonomous division of the city, led to a fiscal year 2011 school fund deficit of $2.7 million, contrary to prior reported estimates of a positive ending balance. The significant projected deficit for fiscal 2012 surfaced precipitously and well into the fiscal year, further indicating deficiencies in financial management.

LIMITED REVENUE GENERATING FLEXIBILITY: Revenue generation is reliant primarily on property taxes, currently at high levels. The city council has shown willingness to tax at the maximum level in the past, and has attempted to implement a supplemental increase in the tax levy for the current fiscal year.

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

HIGH DEBT RATIOS AND UNDER-FUNDED PENSIONS: Debt levels are above-average and the city administered pension plan is funded at a low 61%, as of July 2011.

CREDIT PROFILE

CITY FACES CRITICAL SCHOOL FUND CASH NEEDS
Through May, school cashflow needs have been managed by prioritizing payments, reliance on expedited state aid payments, and city general fund assistance. Over $6 million in vendor invoices currently remain outstanding. The city council approved a supplemental tax levy to address school cash flow needs, against which the city would issue tax anticipation notes.

Both the tax levy and the TANs issuance require state legislative approval. While the supplemental tax bill was approved by the state Senate and House Finance Committee earlier this month, it stalled when the House of Representatives voted to send it back to committee last week. The fate of the bill is uncertain. At this point, even a potential positive vote may not come in time to assist with current fiscal year cash needs.

Earlier this week, the city council voted to request the implementation of state Budget Commission oversight over city and school department finances. The state approved the request, and the Budget Commission is scheduled to begin meetings at the end of the week. The Commission has the authority to expedite approximately $3.3 million in state school aid due at the end of June and intends to address this request at its meeting this week. Management has indicated it plans to use these funds to cover payroll needs through the month of June, though total school cash needs will exceed available resources.

FINANCIAL OPERATIONS PLAGUED BY SCHOOL FUND DEFICITS
For the last three years, Woonsocket has been hurt by significant cuts in state aid, a weak economy, and overspending by school department officials. It appeared that the city was on track towards financial stability when it issued $11.5 million in deficit financing bonds in March of last year. The city was projecting a small surplus in its general fund and school officials were projecting balanced operations for fiscal year 2011.

While the general fund ended fiscal year 2011 positively with an unrestricted fund balance (the sum of the unassigned, assigned, and committed fund balances under GASB 54) of $2.4 million or about 3.1% of general fund spending, the unrestricted school fund balance was a negative $3 million (4.6% of school fund spending). The deficit was related largely to personnel spending without corresponding resources to cover the expenditures, according to city management.

In December 2011, city officials reported that revenues were not going to be sufficient to meet the school fund's fiscal 2012 budget. An accurate estimate was not available at the time due to poor internal reporting practices. City and school officials worked to compile accurate current year cash flow and expenditure information for the school fund and in March presented budget figures indicating an estimated $7.3 million school fund deficit for the current fiscal year. The deficit is sizable, representing about 11% of school fund spending and 5% of total general fund and school fund spending. Based on current estimates, this figure has increased to about $7.5 million. In addition to the projected deficit, the school fund faced ongoing liquidity concerns. The city estimated monthly school fund cash deficits of about $1 to $1.5 million in the current fiscal year.

LONGER-TERM FINANCIAL CHALLENGES
The city faces a significant structural budget imbalance and will need to pursue means in addition to the proposed supplemental tax, which may be revived by the Budget Commission, to bring spending in line with revenues. Fitch remains concerned about the ability of the city and school department to implement changes that will meaningfully improve financial stability given that prior efforts have not always yielded intended results. However, the establishment of Budget Commission oversight is a positive development that may provide greater and more effective fiscal solutions. The city is looking to implement further program cuts, departmental consolidations, and may seek waivers on state mandated expenditures. In addition, currently pending state legislation related to pensions, school aid, and municipal fiscal relief could reduce tax levy pressures.

The city's revenue raising flexibility is limited due to statewide annual limits on property tax levies. The city was able to exceed the statewide property tax levy cap limit in fiscal year 2011 with approval by 4/5ths of city council to make up for cuts in state aid revenues. To offset declines in city revenues in recent years, the city has been cutting expenses in all areas, including reduced payroll costs through attrition, furlough days, reduced salaries, and unpaid vacation days. In addition, the city has been working with its unions to reduce labor costs. Despite these efforts the city is again in a position of needing a financing solution to its operating problems after having issued the aforementioned deficit financing in 2011.

WEAK SOCIOECONOMIC INDICATORS
Woonsocket, located 15 miles outside of Providence, has a population of 41,186 and a tax base of about $1.8 billion. The city benefits from the presence of CVS Caremark Corporation, which maintains its headquarters in the city and is the city's largest employer with about 5,780 workers. Median household income of $38,265 and per capita income of $20,242 are below average at 70% and 71% of state averages, respectively.

The city's unemployment rate continues to be elevated at 13% for April 2012, which is up from 12.8% a year prior, although the city's labor force has declined by 1.8% over that period. Between 2000 and 2010, the city's population declined by about 5%, while the state's increased by less than 1% and the nation's grew by about 10%.

HIGH DEBT RATIOS AND UNDER-FUNDED PENSIONS
Overall debt levels are high at $3,265 per capita and 7.6% of market value. These levels are net of state debt service reimbursements on the city's public school revenue bonds issued by the Rhode Island Health and Education Building Corporation and include the city's 2002 GO pension bonds.

The city administered pension plan is funded at a low 61%, assuming a 7.5% rate of return, with an unfunded liability of $42 million at July 1, 2011. The funded ratio declines even further to 58% using a Fitch-adjusted 7% rate of return. The city's OPEB liability as of July 1, 2011 was equal to a high $127 million and the school department's OPEB liability was $47 million; both amounts include assumptions of a 4% investment rate of return.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

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. 15, 2011);
--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 15, 2011).

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria
U.S. Local Government Tax-Supported Rating Criteria

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Summary:
Rhode Island Clean Water Finance Agency
Woonsocket; Water/Sewer

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Summary:

Rhode Island Clean Water Finance Agency Woonsocket; Water/Sewer

Credit Profile

Rationale

Standard & Poor's Ratings Services assigned its 'A-' long-term rating to Woonsocket, R.I.'s 2014 Rhode Island Clean Water Finance Agency (RICWFA) loan issued for the city's wastewater system. The outlook is stable.

The rating reflects our assessment of the system's:

- Relatively stable and diverse customer base;
- Affordable rates relative to service area wealth levels and automatic annual rate increases that we expect will allow the system to maintain adequate total debt service coverage (DSC; Standard & Poor's calculated),while addressing increasing debt service requirements; and
- Recent improvement in liquidity position to a level that we consider good and that we expect will remain so.

Offsetting these strengths is our view of the system's:

- Service area economy that has declining population trends, above-average unemployment rates, and adequate, but below-average wealth levels;
- High leverage, which we expect will remain so from this borrowing and another borrowing planned next year to address a consent agreement; and
- Weak bond provisions that include an unlimited rolling 1.25 rate covenant and additional bonds test.

Net revenues of the city's sewer system secure the loan.

Woonsocket entered into a consent agreement with the Rhode Island Department of Environmental Management (RIDEM) in February 2011 to improve its wastewater treatment facility to meet current effluent limits for total nitrogen and phosphorus. In March 2012, the city entered into a modified consent agreement with RIDEM that provides an extension to 2015 for plant operation. This borrowing is the second of three planned borrowings from RICWFA to fund the upgrades. In addition to the $10 million borrowing the city did in 2013 and this $20 million borrowing, Woonsocket expects to do another borrowing in the amount of $10 million next year to complete the work necessary to address the consent decree. The system, in our opinion, has adequate capacity, with a total treatment capacity of 16.0 million gallons per day (mgd), compared with average daily flow of 5.0 mgd and peak daily flow of 12.0 mgd in fiscal 2013.

Despite the weak economic fundamentals of the system's service area, its customer base (92% residential and 8% commercial) has been relatively stable, with nearly 8,400 retail customers. We attribute this relative stability to a customer base we consider diverse, with the top 10 customers representing 15.57% of total sewer system revenues in fiscal 2013. Wholesale customers accounted for 8.9% of total sewer system revenues in fiscal 2013.

We consider the system's rates affordable relative to service area wealth levels. The average monthly residential wastewater bill based on 8,000 gallons using current rates is a fixed rate by unit. A monthly residential sewer bill is $28.69, which is 1.1% of the city's 2012 median household effective buying income of $31,105. City council approved annual rate increases of 11% in fiscal years 2013 and 2014 and 5% in fiscal years 2015 and 2016. Such rate increases are automatic, which we view as a credit strength. The last rate increase (11%) occurred on Jan. 1, 2014 and did not affect the wholesale customers. Woonsocket is amending its contracts with its three wholesale customers--North Smithfield, Blackstone, and Bellingham--whereby it will adjust rates for these three communities such that their payments will be sufficient to cover operating and debt service expenses related to components of the sewer system that services these communities.

As a result of recent rate increases, the system's total DSC ratios (Standard & Poor's calculated), based on audited results, improved to 1.68x in fiscal 2013, which we consider strong, from 1.04x in fiscal 2011, which we consider adequate. Our DSC calculations include the debt service for the system's senior debt and subordinate capital lease obligations and do not include prior-year surpluses, which are allowed in satisfying the 1.25x requirement under the indenture. We expect total DSC (excluding prior-year surpluses of about $1.5 million for fiscal 2014 to about $4.7 million for fiscal 2017) to gradually return to levels we consider adequate. More specifically, total DSC is projected to decline to about 1.06x in fiscal 2017 from about 1.59x in fiscal 2014, reflecting increasing debt service requirements from last year's borrowing, this borrowing, and another borrowing planned for next year; modest to no growth; constant sewer flows; and automatic annual rate increases of 11% in fiscal 2014 and 5% in fiscal years 2015 and 2016. We consider these projections reasonable.

In our view, the system has a good liquidity position that we expect will remain so. The system's unrestricted cash balances improved in the past three fiscal years, increasing to a good, in our opinion, $4.1 million for fiscal year ended June 30, 2013 from about $1.5 million for fiscal year ended June 30, 2011. The fiscal 2013 liquidity position provided 168 days' cash on hand. As of Dec. 31, 2013, management reported an unaudited unrestricted cash balance of $5.0 million. Management does not expect to draw down the system's liquidity position in the next few years.

We consider the sewer system's economic fundamentals weak; they include declining population trends, above-average unemployment rates, and adequate, but below-average wealth levels. From 2007 to 2012, the city's population declined 7.7%, while the state's population declined 2.4% and the nation's increased 4.0%. As of October 2013, Woonsocket's unemployment rate was 10.1%, down from the average 12.3% for 2012, higher than the state and national averages of 8.5% and 7.0%, respectively, for October 2013; and 10.4% and 8.1%, respectively, for 2012. The city's 2012 median household effective buying income was 75% of the national average.

The city budgets approximately $200,000 each year for improvements to the wastewater system for the regional wastewater fund. It also budgets approximately $400,000 per year for sewer capital improvements for the user charge fund. It does not have a multiyear capital plan. The capital improvement program through 2015 consists of the wastewater treatment facility upgrade. Funding will come from the three RICWFA loans, including one issued last year, this borrowing, and another next year. Debt service will be covered by automatic rate increases approved by the city council. Before this borrowing we consider the sewer system's debt burden high, with a debt to plant ratio of about 96%, and we expect it will remain high as a result of this new money borrowing and another new money borrowing planned next year. For fiscal year ended June 30, 2013, the system had approximately $26.4 million outstanding, consisting of about $15.8 million of senior-lien debt and capital lease obligations totaling about $10.6 million. Although the wastewater fund revenues are not pledged to this lease, and such obligations are not on par with the system's senior-lien debt and the 2014 loan, which will also be on par with the system's senior-lien debt, the city pays the debt service for such lease from the wastewater revenues. As a result, we factor the lease obligation in assessing the system's debt levels and DSC. Other than Woonsocket's wastewater capital lease obligations, as described above, all wastewater system debt is through RICWFA. The system has no variable-rate debt, swaps, or direct purchase obligations outstanding.

We view the bond provisions as weak, including an unlimited rolling 1.25x rate covenant and unlimited projected rolling 1.25x additional bonds test. The loan is secured by net revenues of the city's sewer system. A debt service reserve funded to the lesser of 125% average annual debt service, 10% of par, or maximum annual debt service additionally secures the loan. The flow of funds is closed. Although Woonsocket had to issue $10.5 million of deficit bonds in 2010 to address financial difficulties, it has not taken excess money away from the wastewater system to address its structural problems. We don't expect the city to use excess money from the sewer system to address any financial difficulties it might have. Management operates the system such that it satisfies the requirements under the master trust indenture and RICWFA loan documents. Management has no informal or formal DSC targets or minimum unrestricted cash balance targets at this time. The lack of such policies or guidelines is offset by automatic annual rate increases and the system's historical financial performance, which has produced adequate total DSC and liquidity.

Outlook

The stable outlook reflects our expectation that management will adjust rates as needed to maintain adequate total DSC (Standard & Poor's calculated) and an adequate liquidity position. We don't expect to raise the rating within the two-year outlook period, given the system's high debt load, future borrowing plans, and limited economic base. We could lower the rating during the outlook period if total DSC (Standard & Poor's-calculated) is insufficient or the system's liquidity position materially erodes.

Related Criteria And Research

Related Criteria

- USPF Criteria: Key Water And Sewer Utility Credit Ratio Ranges, Sept. 15, 2008
- USPF Criteria: Standard & Poor's Revises Criteria For Rating Water, Sewer, And Drainage Utility Revenue Bonds, Sept. 15, 2008

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