

# RatingsDirect®

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## Summary:

### Spencer-Owen Community School Corp. Indiana Owen Valley High School Building Corp.; School State Program

#### Primary Credit Analyst:

Moreen T Skyers-Gibbs, New York (1) 212-438-1734; moreen.skyers-gibbs@spglobal.com

#### Secondary Contact:

Benjamin D Gallovic, Chicago + 1 (312) 233 7070; benjamin.gallovic@spglobal.com

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## Summary:

# Spencer-Owen Community School Corp. Indiana Owen Valley High School Building Corp.; School State Program

### Credit Profile

US\$5.0 mil ad valorem property tax first mtg bnds ser 2019 due 01/15/2030

<i>Long Term Rating</i>	AA+/Stable	New
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<i>Underlying Rating for Credit Program</i>	A/Stable	New
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#### **Owen Vy High Sch Bldg Corp, Indiana**

Spencer-Owen Comnty Schs, Indiana

Owen Vy High Sch Bldg Corp (Spencer-Owen Comnty Schs) ad valorem prop tax 1st mtg rfdg bnds

<i>Long Term Rating</i>	AA+/Stable	Affirmed
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<i>Underlying Rating for Credit Program</i>	A/Stable	Affirmed
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#### **Spencer-Owen Fac Imp Corp, Indiana**

Spencer-Owen Comnty Schs, Indiana

Spencer-Owen Fac Imp Corp SCHSTPR

<i>Long Term Rating</i>	AA+/Stable	Affirmed
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<i>Underlying Rating for Credit Program</i>	A/Stable	Affirmed
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## Rationale

S&P Global Ratings has assigned its 'A' underlying rating and 'AA+' enhanced program rating to Owen Valley High School Building Corp., Ind.'s series 2019 ad valorem property tax first-mortgage bonds, issued on behalf of Spencer-Owen Community School Corp. At the same time, we affirmed our existing 'A' underlying and 'AA+' program ratings on first-mortgage bonds issued by the building corporation on behalf of the school corporation. The outlook for all ratings is stable.

In our opinion, the school's creditworthiness continues to be supported by its strong cash reserves, which have increased annually over the past three years despite enrollment declines. However, enrollment is a key determinant of operating revenues and with the sharp enrollment decline in 2019, it is likely that state aid could be reduced, which would place potential pressures on operations. The school's ability to mitigate this without exhibiting any deterioration in its cash reserves will continue to support the current underlying rating. We believe that its low debt burden and lack of significant debt needs provide additional credit support. However, we also believe that while stable, the economic indicators are below that of its higher rated peers and are a limiting rating factor.

The 'A' underlying rating reflects our view of the school corporation's:

- Stable local economy with access to the nearby Bloomington metropolitan area;

- Strong available operating reserves (on a cash basis of accounting) between the general and rainy day funds;
- Low overall net debt burden on a per capita basis and moderate debt burden as a share of gross assessed value (AV).

Offsetting the above strengths, in our view, are the corporation's overall trend of declining enrollment, which is a key determinant of operating revenues for Indiana school districts, as well as its below-average, though adequate, economic indicators.

## **Security**

The 'AA+' rating is based on our state credit enhancement criteria, and reflects our assessment of the strength of the Indiana state aid intercept structure (as found in Section 20-48-1-11 of the Indiana Code). All school corporations can benefit from this statute without specific state qualification. However, in the absence of certain state aid coverage levels and bond terms, the statute may not provide sufficiently strong support in increasing the likelihood of payment in full and on time. For these reasons, we review state aid coverage and bond terms (see our report on "Indiana School Corp.," published May 15, 2017, on RatingsDirect).

Annual state aid appropriated and allocated for distribution during the state's fiscal year covers maximum annual debt service (MADS) by at least 2x, and appropriated, but not yet distributed state aid covers maximum semiannual debt service by at least 1x. The bond terms require the school corporation to transfer payments to an independent trustee, registrar, or paying agent at least five business days in advance of the debt service due dates; and this third party has immediate notification and claimant responsibilities to the state treasurer, if a debt service transfer is not made on time or is insufficient. On notification, the treasurer will advance to the claimant any state aid that has been appropriated for allocation, but not distributed, up to an amount of the debt service shortfall.

The series 2019 bonds are issued pursuant to a trust indenture between the school building corporation and the trustee, and a lease between the school building corporation as lessor and school corporation as lessee. Lease rentals paid by the school building corporation directly to the trustee secure the bonds. Rentals are payable from ad valorem taxes against all taxable property within the school corporation's boundaries.

The school corporation expects to use the bond proceeds from the series 2019 bonds to finance various renovations and improvements to its elementary school buildings.

The ad valorem property tax levy is not subject to annual appropriation under Indiana law. However, there is abatement risk, as the school corporation is required to abate lease rentals if the leased premises are not available for use. This risk is mitigated, in our view, by the lease requiring the district to maintain at least two years of lease interruption insurance, as well as casualty insurance equal to full replacement cost. Additionally, we do not consider there to be construction risk as the leased premises are already occupied and the lease allows payments to be made during construction.

The ad valorem property tax pledge securing the bonds is subject to state circuit-breaker legislation, which caps the property tax burden for taxpayers based on a percentage of the real estate parcels' gross AV. This can, and often does, reduce the total tax levy. The levy to cover debt service, however, is statutorily protected, allowing the school corporation to distribute circuit-breaker losses first across nondebt service funds that receive property taxes. Despite

the limitations, we rate this debt at the same level as our view of the district's general creditworthiness.

## **Economy**

Spencer-Owen Community Schools serves an estimated population of 17,338 and encompasses approximately 340 square miles in south-central Indiana's Owen County, about 55 miles southwest of Indianapolis and 18 miles northwest of Bloomington. Much of the district is comprised of agricultural land.

The school corporation's top employers include two medical device manufacturers—Boston Scientific Corp. and Cook Urological Inc.—that employ 900 and 700, respectively. It is our understanding that Boston Scientific will be expanding its facility and will add about 350 additional jobs. Other top employers include the corporation itself (374), Trilogy Health Services LLC (nursing home, 100), and Babb's Supervalu (grocery store, 100). Countywide unemployment has remained higher than state levels in recent years and was 4.4% in 2017.

Median household and per capita effective buying incomes in the corporation are adequate at 83% and 77% of national levels, respectively. While, adequate, however, they are below those of its higher rated peers and constrain the rating. Gross AV totaled \$992.3 million in 2018, which we consider strong at \$57,230 per capita. Net AV grew by a total of 3.5% since 2016 to \$629.4 million in 2019. The 10 largest taxpayers make up an estimated 8.5% of net AV, which we consider very diverse.

The economy is stable and is likely to remain so.

## **Finances**

General fund operations of Indiana school corporations rely almost entirely on state tuition support, which is determined on a per-pupil basis. As a result, operating revenue is very sensitive to enrollment fluctuations. State aid accounted for 94.9% of general fund revenue in 2017. Enrollment decreased in each year from 2015 to 2019, which the school corporation attributes to its transient population and low overall birthrate. Over the past three years, however, despite enrollment declines that resulted in lower revenues, the general fund has operated with consecutive operating surpluses. This, according to the school corporation, was due to prior years of right-sizing the budget by eliminating several positions as well as attrition. However, enrollment for 2019 totaled 2,363 and reflects a nearly 4% drop. This in comparison to prior years represents a significant drop and could result in budgetary pressures.

Beginning in fiscal 2019, the general fund will be replaced with an education fund and most non-instructional service funds will be replaced by an operations fund. The school corporation believes that this change will provide more financial flexibility as previous general fund expenditures will be transferred to the operations fund. Based on the 2019 calendar year budget, the education fund totals \$17.8 million and the school corporation anticipates positive operations.

Estimates for the general fund in calendar year 2018 indicate another operating surplus of \$562,000, increasing the general fund to \$3.2 million. The rainy day fund also grew to \$3.8 million in 2018. Therefore, available cash reserves are slated to increase to \$7 million, or about 40% of general fund expenditures.

The corporation's available cash reserve of \$5.8 million (which consists of the combined general and rainy day funds) is strong on a cash basis of accounting, in our view, at 33% of general fund expenditures at calendar year-end (Dec. 31) 2017. Of that amount, \$2.7 million (15.0% of expenditures) is in the general fund, and \$3.2 million (18%) is in the rainy

day fund. The corporation reported a surplus operating result of 2.0% of expenditures in 2017.

The state audits school corporations biennially on a cash basis, using a June 30 fiscal year-end, although they operate, budget, and report financial performance to their school boards for the calendar year and submit annual Dec. 31 year-end cash basis financial statements to the state. We believe that the resulting state-issued (although unaudited) Dec. 31 year-end cash statements offer a better understanding of each corporation's financial performance and, accordingly, we use these reports as the basis of our analysis.

## **Management**

We consider the corporation's management practices standard under our Financial Management Assessment methodology, indicating the finance department maintains adequate policies in some, but not all, key areas.

Highlights include conservative revenue and expenditure assumptions for annual budgeting. The school typically under-budgets its revenues and over-budgets its expenditures. It also takes into account historical trends. However, in our opinion, although we understand that the budget-to-actual is monitored on a monthly basis by the administration, it is provided to the board only on an annual basis. Therefore, in our opinion, the school lacks frequent budget reporting to the board. An informal reserve target is in place to maintain a minimum of 8% of cash reserves in the general fund. Management does not maintain a multiyear financial plan. Its formalized multiyear capital projections only look out three years.

## **Debt**

Overall net debt is low, in our opinion, at 2.5% of market value and \$1,432 per capita. With 98% of the corporation's direct debt scheduled to be retired within 10 years, amortization is rapid. Debt service carrying charges were 13.0% of total governmental fund expenditures (excluding capital outlay) in calendar year 2017, which we consider moderate.

According to management, the school corporation does not have additional debt plans at this time.

## **Pension and other postemployment benefit liabilities**

The school corporation contributes to two retirement plans administered by the state: the Indiana State Teachers' 1996 account (TRF '96) and the Public Employees' Retirement Fund (PERF). These are both cost-sharing, multiple-employer defined-benefit retirement plans (the plans share all risks and costs, including benefit costs, proportionately by the participating employers). Certain employees are also covered under the Indiana Teacher's Pre-1996 account (TRF Pre-'96). The state has assumed the entire liability of this account, which it funds on a pay-as-you-go basis and the school corporation is not obligated to make payments to this account.

The school corporation continues to pay 100% of its required pension contributions (which are actuarially determined); the 2017 payment was equal to 3.7% of total funds' expenditures.

As of June 30, 2017, the TRF '96 fund was 90.4% funded and PERF was 76.6% funded in accordance with Governmental Accounting Standards Board (GASB) Nos. 67 and 68. We view the plans' actuarial assumptions, including this assumed rate of return of 6.75%, as generally reasonable because they are slightly more conservative than the national average. Considering the plans' strong funded ratios, reasonable actuarial assumptions, and low historical contribution requirements for plan participants, we do not expect the school corporation's required pension costs to increase significantly in the medium term.

It is our understanding that the school corporation does not have any costs associated with health care benefits for its retirees.

## **Outlook**

The stable outlook on the long-term rating reflects the outlook on the state of Indiana and moves in tandem with the state.

The stable outlook on the underlying rating reflects our views that the school is likely to maintain available reserves at a level that we consider strong on a cash basis of accounting for the next two years given its conservative budgeting practices. It also reflects our expectation that the district will likely continue to make the necessary budgetary adjustments to mitigate deterioration of its cash reserves due to enrollment loss. In addition, it reflects our views that the stability of the economy is likely to continue providing credit support. As a result, we do not expect to change the rating during the two-year outlook horizon.

### **Downside scenario**

We believe that a lower rating is possible if the school were to experience any unforeseen cost pressures, resulting in material deterioration in its cash reserves.

### **Upside scenario**

If the school corporation's economic indicators were to improve to levels commensurate with those of its higher-rated peers, coupled with sustained or strengthened cash reserves to levels that we consider strong enough to offset the below-average economy, we could raise the rating.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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