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Summary:

Richmond Community Schools, Indiana; School State Program

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Summary:

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Credit Profile		
US$5.0 mil GO bnds ser 2018 dtd 11/01/2018 due 01/15/2025		
Long Term Rating	AA+/Stable	New
Underlying Rating for Credit Program	A/Stable	New

Rationale

S&P Global Ratings assigned its 'AA+' long-term program rating and 'A' underlying rating to Richmond Community Schools, Ind.'s series 2018 general obligation (GO) bonds. The outlook is stable.

Management indicates the series 2018 GO bond proceeds will be used for various renovations and improvement projects to school facilities in addition to technology and equipment purchases.

The 'A' rating is based on the school district's ad valorem tax pledge, and reflects our view of its:

- Strong combined available reserves on a cash basis of accounting,
- History of positive operations, and
- Low overall debt profile with rapid amortization.

Partially offsetting the above strengths in our view are the school corporation's history of overall declines in enrollment, which is the primary determinant of state aid, and economic indicators, which while at levels that we consider adequate, are not commensurate with those of its higher-rated peers.

The school corporation has been pressured in recent years by an overall decline in enrollment, which is the primary determinant of state aid. Management has remained proactive in reducing expenditures in response to the declining enrollment. Reductions include the closure of three elementary schools during the 2012-2013 school year and, more recently, labor cost savings achieved through attrition. We view the school corporation's below average income indicators as a credit weakness. However, the corporation's level of available reserves and moderation in enrollment declines, provide rating stability.

Security

The ad valorem property tax pledge, which secures the corporation's 2018 GO bonds is subject to state circuit-breaker legislation, which caps the property tax burden for taxpayers based on a percent of the real estate parcels' gross assessed value (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 non-debt service funds that receive property taxes. We rate the debt at the same level as our view of the corporation's general

creditworthiness.

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 report on "Indiana School Corp.", published May 16, 2017, on RatingsDirect).

Annual state aid appropriated and allocated for distribution during the state's fiscal year covers maximum annual debt service coverage 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, in the event 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 yet distributed, up to an amount of the debt service shortfall.

Economy

Richmond Community Schools School serves an estimated population of 40,637. Median household and per capita effective buying incomes in the corporation are adequate at 68% and 71% of national levels, respectively. At $54,306 per capita, the 2018 gross AV totals $2.2 billion and in our opinion is adequate. Net AV grew by a total of 0.4% since 2016 to $1.4 billion in 2018. The tax base is diverse, in our view, with the 10 largest taxpayers accounting for approximately 15.4% of net AV.

The school corporation is located in Wayne County in east central Indiana, approximately 72 miles east of Indianapolis, 49 miles west of Dayton, Ohio, and 68 miles northwest of Cincinnati, Ohio. The school corporation's AV has remained relatively stable in recent years and management expects at least stable trends to continue as a result of ongoing development, including both commercial and residential, which we view as likely.

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. Enrollment decreased in each year since 2016, declining to 4,691 students in the 2017-2018 school year. Management projects that enrollment will remain relatively stable over the next couple years as a result of the stability in the local economy in conjunction with an increased emphasis on marketing and community outreach. While we recognize that enrollment declines have moderated in recent years, we expect that further enrollment declines could potentially occur in future years. State aid accounted for 99.0% of general fund revenue in 2017.

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 17% of general fund expenditures at calendar year-end (Dec. 31) 2017. Of that amount, $1.3 million (3.7% of expenditures) is in the general fund, and $4.5 million (12.9% of expenditures) is in the rainy day fund. The corporation reported a surplus operating result of 0.9% of expenditures in 2017.

We expect that the corporation's available reserves will remain strong on a cash basis of accounting over the next few years. Despite declines in enrollment, the school corporation has increased its level of available reserves in each of the past three years, primarily due to conservative budgeting assumptions and proactive expenditure reductions.

The school corporation expects to report an approximately $200,000 increase in its available reserves in fiscal 2018, equal to 0.6% of operating expenditures, and expects to report at least stable balances in fiscal 2019. In the past, the school corporation has implemented a practice of transferring any positive general fund balance to the rainy day fund at the end of the year, which is what led to a slight use of general fund cash in fiscal 2016 in conjunction with an increase in the rainy day balance. The school corporation has a history of conservative budgeting practices and proactive expenditure reductions in response to declining enrollment. During the 2012-2013 school year, the school corporation closed three elementary schools as a result of declining enrollment. Since then, the corporation has achieved additional expenditure reductions in labor costs, which were achieved through attrition. Management indicates that they are close to the right-sized staff for their enrollment, which we view as reasonable. We expect that in the event that enrollment declines persist, that the school corporation will continue to make budgetary adjustments to maintain a strong combined available fund balance.

The state audits school corporations biennially on a cash basis, using a June 30 fiscal year-end. In the interim, schools submit semi-annual financial statements to the state that are reviewed by the Indiana Office of School Finance (IOSF), and then made available as unaudited reports. We base our analysis on these unaudited, state-issued cash reports, but on a Dec. 31, year-end basis. In most cases, schools operate, budget, and report financial performance to their school boards using a calendar year. Therefore, we believe the calendar year-end reports offer a good understanding of each corporation's financial performance and budget position. These unaudited reports prescribe to the state's uniform system of accounting and reporting that all schools are required to follow and, based on the IOSF review and on prior-year comparisons with audits, we have deemed them reliable to serve as a 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:

- Realistic revenue and expenditure assumptions with the use of at least three years of historical data, conservative estimates, and the use of outside sources of information when forecasting trends;
- Monthly reporting to the board of revenue and expenditures compared to budgeted amounts, which includes beginning and ending cash balances by fund;
- No comprehensive formal long-term financial plan past the budgeted year;
- The maintenance of a 10-year, long-term capital plan, which is updated at least annually and identifies funding uses, though identification of funding sources is not comprehensive;
- Formal investment management policy with annual reporting of investment holdings and earnings to the board;
- No formal debt management policy, but it adheres to state limits; and
- Informal target of maintaining combined general fund and rainy day fund balance of at least 8%-10% of operating

expenditures for cash-flow purposes and as a sufficient cushion for any unforeseen budgetary pressures; the school corporation is currently exceeding the target.

Debt

Overall net debt is 2.2% of market value and $1,211 per capita, which we believe to be low. Amortization is rapid, with 100% of the corporation's direct debt scheduled to be retired within 10 years. Despite rapid amortization, debt service carrying charges were only 6.1% of total governmental fund expenditures excluding capital outlay in calendar year 2017, which we consider low.

We understand that the school corporation could potentially issue an additional $5 million within the next two to three years for facility improvement projects.

The school corporation's Series 2013 Ad Valorem Property Tax First Mortgage bonds were privately placed with JPMorgan Chase Bank, N.A. in June 2013. The bonds were issued for $7.75 million, of which $2.01 remains outstanding and will mature in 2019. We recognize that the agreement contains no events of default or covenant violations that we deem nonstandard pursuant to our contingent liquidity criteria.

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 4.3% 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.

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 expectation that the school corporation will maintain combined available reserves at a level that we consider strong on a cash basis of accounting for the next two years. As a result, we do not expect to change the rating during the two-year outlook horizon.

Downside scenario

We could lower the rating if declining enrollment or another budgetary pressure leads to a material decrease in the school corporation's currently strong level of available reserves.

Upside scenario

If the school corporation's economic indicators were to increase significantly in conjunction with maintenance of a strong available fund balance, assuming no deterioration in the corporation's other credit factors, we could raise the rating.

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