

# RatingsDirect®

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**Summary:**

## Kankakee Valley School Corp., Indiana; School State Program

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## Summary:

# Kankakee Valley School Corp., Indiana; School State Program

### Credit Profile

US\$8.0 mil GO bnds ser 2018 due 01/15/2030

<i>Long Term Rating</i>	AA+/Stable	New
<i>Underlying Rating for Credit Program</i>	A+/Stable	New

#### **Kankakee Valley Wheatfield School Building Corporation, Indiana**

Kankakee Vy Sch Corp, Indiana

Kankakee Valley Wheatfield School Building Corporation SCHSTPR

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

#### **Kankakee Vy Middle Sch Bldg Corp, Indiana**

Kankakee Vy Sch Corp, Indiana

Kankakee Vy Middle Sch Bldg Corp (Kankakee Vy Sch Corp) GO State Credit Enhancement

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

## Rationale

S&P Global Ratings has assigned its 'AA+' long-term rating and 'A+' underlying rating to Kankakee Valley School Corp., Ind.'s series 2018 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA+' long-term rating and 'A+' underlying rating on existing debt issued for the school corporation. The outlook is stable.

Officials will use the 2018 bond proceeds to finance renovations and improvements to Kankakee Valley High School, including the construction of athletic facilities.

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.

The 'A+' rating is based on an ad valorem property tax pledge. The ad valorem property tax pledge 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. This can, and often does, reduce the total tax levy. The levy to cover debt service, however, is statutorily protected, allowing the district to distribute circuit-breaker losses first across non-debt service funds that receive property taxes.

Lease rental payments made by the school corporation directly to the trustee secure the existing bonds. Rentals are payable from revenue from ad valorem taxes against all taxable property within the school corporation's boundaries. The ad valorem property tax levy is not subject to annual appropriation under Indiana law. However, there is abatement risk, as the district is required to abate lease rentals in the event the leased premises are not available for use. This risk is mitigated, in our view, by the lease's requirement that the district maintain at least two years of lease interruption insurance as well as casualty insurance equal to full replacement cost.

We rate the limited-tax GO and lease debt at the same level as our view of the school district's general creditworthiness, given that ad valorem taxes are collected from the district's entire tax base and because of a lack of limitations on the fungibility of resources available for debt service.

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

- Adequate-to-good income levels and very strong per capita market values;
- Prudent financial management practices that support a very strong financial position, factoring in unrestricted general fund, and rainy day fund reserves; and
- Relatively stable enrollment trend.

Partially offsetting these strengths are the district's elevated debt service carrying charges, albeit due to rapid amortization, and concentrated tax base.

### **Economy**

Kankakee Valley School Corp. serves an estimated population of 20,469. In our opinion, median household effective buying income (EBI) is good at 105% of the national level, but per capita EBI is adequate at 85%. At \$94,383 per capita, the 2018 gross AV totaling \$1.9 billion is, in our opinion, very strong. Net AV grew by a total of 2.1% since 2016 to \$1.4 billion in 2018. The tax base is moderately concentrated, in our view, with the 10 largest taxpayers accounting for approximately 37.6% of net AV.

The school district is in Jasper County and is approximately 20 miles northeast of Rensselaer, the retail and industrial center and county seat. It consists of the townships of Keener, Wheatfield, Union, Kankakee, and Walker, as well as the towns of Wheatfield and Demotte. The school district's proximity to Lake County and Rensselaer provides residents access to a wider array of employment, educational, and recreational opportunities. In 2017, Jasper County unemployment averaged 4.3%, in between the state and national rates of 3.5% and 4.4%, respectively.

The district's largest taxpayer is Northern Indiana Public Service Co. (NIPSCO), an electric utility company that accounts for 29.6% of the district's total net AV. NIPSCO operates a coal-fired power plant in the district. In 2016, the utility announced it plans to close two of its four coal-fired units by the end of 2023. We understand that NIPSCO may potentially replace the coal-fired units with alternative energy sources, which we believe could mitigate some of the effect on the district's tax base. If there were a significant reduction in the district's AV due to this closure, the tax burden would shift to other district taxpayers, which could be a credit stress. The school district indicates it will work to reduce future debt service payments in order to alleviate the burden on other taxpayers. Given that the closure of the plant is outside of our two-year outlook horizon, we do not view it as an immediate credit risk.

## **Finances**

General fund operations of Indiana school districts rely almost entirely on state tuition support, determined on a per-pupil basis. Consequently, under the current formula, enrollment trends and the amount of aid the state appropriates are the key drivers of general fund revenue. Other core operating services such as transportation, bus replacement, and capital are accounted for in separate funds outside of the general fund. These funds are supported by local property taxes, which may be impacted by circuit breaker tax caps. In 2017, circuit breaker losses totaled only \$11,000.

State aid accounted for 97.9% of the district's general fund revenue in 2017. Student enrollment totaled 3,368 for the 2017-2018 school year, having decreased by 4.0% since 2013. Management attributes the decline to lower birth rates, but notes that elementary classes have begun to level out, which we believe could be an indication of enrollment stabilization. In recent years, actual enrollment has come in on target with projections.

The district's available cash reserve of \$12.5 million (which consists of the combined general and rainy day funds) is very strong on a cash basis of accounting, in our view, at 56% of general fund expenditures at calendar year-end (Dec. 31) 2017. Of that amount, \$8.2 million (37% of expenditures) is in the general fund, and \$4.3 million (19% of expenditures) is in the rainy day fund. The district reported a surplus operating result of 1.3% of expenditures in 2017.

Despite the decline in enrollment, Kankakee Valley has been able to post surpluses in its general fund every year since the Great Recession. As a result, the district has increased its general fund reserves to levels that we consider very strong. According to management, recent surpluses have been supported by increases in per pupil state funding and revenue generated through the district's career and technical education program. Teacher salaries were also frozen for a six-year period ending in 2016, which helped control costs. A new two-year contract in 2017 increased salaries and gave a one-time stipend to teachers, but the district was still able to post a surplus in 2017, albeit a smaller one than in previous years. The district has also increased its rainy day cash balance through transfers from its capital projects and transportation funds, as well as through a county distributed local income tax. For calendar 2018, the district expects small increases in both the general and rainy day fund cash balances. The district has no plans to significantly spend down reserves over the next few years. We view the very strong reserve position as a credit strength as it provides cushion against future budgetary pressures, including the partial closure of NIPSCO's coal-fired power plant.

The state audits school districts 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 district'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 district's management practices standard under our Financial Management Assessment methodology, indicating the finance department maintains adequate policies in some but not all key areas.

Management prepares its in-house budget using historical trend analysis and some outside sources of information. The board receives a monthly general fund cash flow report, which doesn't outline budget-to-actual results, but it does show a comparison to historical years. The board can amend the budget at any time if necessary. The district adheres to state investment and debt guidelines. Management actively monitors investments, and the board receives an annual investment report. A three-year capital projects fund plan is a requirement of the school district's annual budget, and management updates the plan before budget preparation each year. The district doesn't do any long-term financial forecasting. Lastly, the district has written goals to maintain a minimum general fund cash balance equal to 17% of expenditures and a minimum rainy day fund cash balance of \$2.5 million.

### **Debt**

At 3.0% of market value and \$2,874 per capita, overall net debt is moderate, in our view. Amortization is rapid, with 85% of the district's direct debt scheduled to be retired within 10 years. Debt service carrying charges were 17.7% of total governmental fund expenditures excluding capital outlay in calendar year 2017, which we consider elevated.

The district plans to issue about \$15 million of additional debt in 2019 to finance various capital improvements. We believe the district's overall net debt burden will remain moderate.

### **Pension and other postemployment benefits liabilities**

Non-certified staff are covered by a defined contribution pension plan. For teachers, the school district contributes to the Indiana State Teachers' 1996 account (TRF '96).. This is a cost-sharing, multiple-employer defined benefit retirement plan (the plans share all risks and costs, including benefit costs, proportionately by the participating employers). Some employees are also covered under the Indiana Teacher's Pre-1996 account. The state has assumed the entire liability of this account, which it funds on a pay-as-you-go basis and the school district is not obligated to make payments to this account.

The district continues to pay 100% of its required actuarially determined pension contributions. The 2017 payment was equal to 2.7% of total funds' expenditures.

As of June 30, 2017, the TRF '96 fund was 90.4% funded in accordance with Governmental Accounting Standards Board Statements Nos. 67 and 68. We view the plan's 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 plan's strong funded ratio, reasonable actuarial assumptions, and low historical contribution requirements for plan participants, we don't expect the district's required pension costs to increase significantly in the medium term.

The school district allows employees to remain on its health care plan upon retirement, but retirees pay the full amount of their premiums. As a result, there is only an implicit liability to the school district.

## Outlook

The stable outlook on the 'AA+' program rating reflects our view of the strength of the Indiana state aid intercept program. The rating is set one notch below and moves in tandem with the state issuer credit rating.

The stable outlook on the 'A+' underlying rating reflects our expectation the district will maintain very strong available cash reserves. We do not expect to change the rating in the two-year outlook horizon, because we believe the district's strong reserve position provides sufficient cushion in the event of unforeseen budgetary stresses.

### Downside scenario

We could lower the rating if the district were to significantly draw down its reserves over the next two years or if there are unexpected or accelerated impacts from the partial closure of the NIPSCO power plant.

### Upside scenario

Although unlikely in outlook horizon, we could raise the rating if the district's taxpayer concentration improves.

#### Ratings Detail (As Of June 14, 2018)

Kankakee Vy Sch Corp GO bnds ser 2018 due 01/15/2030

<i>Long Term Rating</i>	AA+/Stable	Rating Assigned
<i>Underlying Rating for Credit Program</i>	A+/Stable	Rating Assigned

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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