

RatingsDirect®

Summary:

Wa-Nee Community School, Indiana; General Obligation; School State Program

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Table Of Contents

Rationale

Outlook

Summary:

Wa-Nee Community School, Indiana; General Obligation; School State Program

Credit Profile

US\$7.075 mil GO bonds ser 2018 dtd 11/20/2018 due 01/15/2024

Long Term Rating AA+/Stable New

Underlying Rating for Credit Program A/Stable New

Wa-Nee Comnty Sch Bldg Corp, Indiana

Wa-Nee Comnty Sch, Indiana

Wa-Nee Comnty Sch Bldg Corp (Wa-Nee Comnty Sch) Ad Valorem prop tax first mtg bonds (Wa-Nee Comnty Sch) ser 2016 due 01/15/2031

Long Term Rating AA+/Stable Current

Underlying Rating for Credit Program A/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' long-term program rating and 'A' underlying rating to Wa-Nee Community Schools, Ind.'s series 2018 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA+' long-term program rating and 'A' underlying rating on the school corporation's outstanding 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 energy efficiency and savings projects.

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

- Local economy, which has stabilized after several years of volatility in the manufacturing sector;
- Strong market value per capita;
- Strong general fund reserves, albeit on a cash basis of accounting; and
- Moderate overall debt burden.

Partially offsetting the above strengths in our view are the school corporation's income indicators, which while at levels that we consider adequate to good, are not commensurate with those of its higher-rated peers and plan to utilize its rainy day fund balance in future years to fund retirement benefit obligations.

The school corporation has benefitted in recent years from relatively stable enrollment, which is the primary determinant of state aid. As a result, the school corporation has increased its combined general and rainy cash balances to a level that we consider strong as a percentage of its operating budget. We view the school corporation's economic reliance on somewhat more volatile manufacturing industry as a credit weakness. However, the

corporation's level of available reserves and history of stable enrollment provide rating stability.

Security

The ad valorem property tax pledge, which secures the corporation's 2018 GO bonds and other outstanding debt 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.

Other outstanding first mortgage bonds are secured by lease rental payments paid directly to an independent trustee pursuant to a trust indenture between the building corporation and the trustee and a lease between the school corporation and the building corporation. Rent is payable from ad valorem taxes against all taxable property within the corporation's boundaries, and rental payments are not subject to annual appropriation under Indiana law. Lease payments are subject to abatement if the leased property is damaged or destroyed, though abatement risk is mitigated by lease provisions requiring the corporation to maintain rental value insurance sufficient to cover two years' rent and property or casualty insurance sufficient to cover the full replacement cost of the leased property.

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

Wa-Nee Community School serves an estimated population of 20,974. In our opinion, median household effective buying income (EBI) is good at 104% of the national level, but per capita EBI is adequate at 78%. At \$71,491 per capita, the 2018 gross AV totaling \$1.5 billion is, in our opinion, strong. Net AV grew by a total of 8.5% since 2016 to \$1.0 billion in 2018. The tax base is very diverse, in our view, with the 10 largest taxpayers accounting for approximately 10.9% of net AV.

The school corporation is located approximately 20 to 30 miles southeast of South Bend where it encompasses 144 square miles across Elkhart (108 square miles) and Kosciusko (36 square miles) counties, including a portion of the city of Goshen. The Elkhart County economy hosts an array of recreational vehicle production companies, including Forest

River, one of the area's largest employers (with about 6,400 workers throughout the county), plus many other large industrial and service-based facilities. County employment relies heavily on a somewhat volatile manufacturing industry, with 41% of the workforce employed in the field. Layoffs during the recession contributed to, in our view, very high county unemployment, but in recent years the local economy has improved. The Elkhart County average unemployment rate peaked at 17.9% in 2009 and declined steadily thereafter to 2.5% in 2017. The school corporation's AV has increased in recent years and management expects slight growth to continue as a result of ongoing economic expansion, 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. In 2018, enrollment came in at 3,056 students. Enrollment decreased slightly overall from 2014 to 2018. Student enrollment has remained relatively stable in recent years, decreasing by 1.1% since 2014 to 3,056 students for the 2017-2018 school year. Management expects overall enrollment stability to continue, which we view as likely. The school corporation is a net gainer from open enrollment, gaining approximately 70 more students than it loses each year. State aid accounted for 97.3% of general fund revenue in 2017.

The corporation's available cash reserve of \$6.2 million (which consists of the combined general and rainy day funds) is strong on a cash basis of accounting in our view, at 34% of general fund expenditures at calendar year-end (Dec. 31) 2017. Of that amount, \$3.5 million (19% of expenditures) is in the general fund, and \$2.7 million (14.6% of expenditures) is in the rainy day fund. Management indicated that while the rainy day balance could be made available if required, the balance has been earmarked for the purpose of funding the district's outstanding postemployment benefits liability. The corporation reported a surplus operating result of 4.8% of expenditures in 2017.

Additionally, the school corporation plans to go to voters in November 2018 for approval of an operating referendum. If passed, the referendum would result in an additional \$1 million annually for the school corporation in each of the following eight years. We recognize that the school corporation is not budgeting for additional referendum revenues, rather, referendum revenues, if successful, would be utilized for various education and special education offerings, including the hiring of additional positions. We do not view the school corporation's budgetary performance as reliant on the outcome of the referendum vote. Due in part to relatively stable enrollment in conjunction with conservative budgeting practices, we expect that the corporation's available reserves will remain strong on a cash basis of accounting over the next few years.

In fiscal 2018, the school corporation expects to report at least a \$6.49 million available balance across its general and rainy day funds, a level that we consider strong on a cash basis at 35.0% of operating expenditures, due primarily to savings achieved through attrition. The corporation expects for at least balanced operating results to continue in fiscal 2019, which due to the corporation's expenditure reduction measures and conservative budgeting practices, we consider likely. We recognize that the operating surplus in fiscal 2017 was due primarily to labor cost reductions achieved through attrition in addition to several positive budgetary variances which include taking an insurance holiday and higher per pupil funding. We understand that the school corporation does not currently have any plans to significantly spend down its general fund reserves, but recognize that the rainy day balance, earmarked for future funding of postemployment benefits, is expected to begin being spent down in fiscal 2022 or fiscal 2023.

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 three to five years of historical data, conservative estimates, and the use of outside sources of information when forecasting trends;
- Quarterly reporting to the board of comprehensive budget to actual results, with the ability to amend the budget as needed;
- No comprehensive formal long-term financial plan past the budgeted year;
- The maintenance of a three-year, state-mandated capital plan, but no longer-term and comprehensive plan;
- Formal investment management policy with quarterly reporting of investment holdings and earnings to the board;
- No formal debt management policy, but adhering to statutory limitations; and
- Informal policy of maintaining combined general fund and rainy day fund balance of at least 20% of operating expenditures for cash-flow purposes and as a sufficient cushion for any unforeseen budgetary pressures; the school corporation is currently exceeding this target.

Debt

Overall net debt is 3.1% of market value and \$2,227 per capita, which we believe to be moderate. With 76% of the corporation's direct debt scheduled to be retired within 10 years, amortization is rapid. Debt service carrying charges were 16.3% of total governmental fund expenditures excluding capital outlay in calendar year 2017, which we consider elevated.

We understand that the district does not currently have any plans to issue additional debt and management also confirms it has no contingent liquidity risks from financial instruments with payment provisions that change upon certain events.

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 3.8% 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.

The school corporation provides other postemployment benefits to eligible employees in the form of additional compensation and health insurance. The school corporation's 457 Plan covers pension benefits for early retirement bridge, severance benefit, and accumulated sick days. The plan's total liability is estimated at \$4.6 million as of the most recent July 1, 2015 actuarial study. We understand that the school corporation has earmarked its rainy day fund balance to fund its postemployment benefit liabilities. In addition, the school corporation maintains a \$940,000 current deposit to fund future plan benefits. The school corporation paid \$139,000 in other postemployment benefits in 2017, equivalent to 0.7% of operating expenditures.

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.

Upside scenario

If the school corporation were to maintain its currently strong level of available reserves, assuming no deterioration in other credit factors, we could raise the rating.

Downside scenario

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

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 for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found

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