

RatingsDirect®

Summary:

**South Vermillion Community School
Corp., Indiana**

**South Vermillion Middle 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

Table Of Contents

Rationale

Outlook

Summary:

South Vermillion Community School Corp., Indiana

South Vermillion Middle School Building Corp.; School State Program

Credit Profile

US\$4.575 mil 1st mtg bnds (South Vermillion Comnty Sch Corp) ser 2018 due 01/15/2029

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

Rationale

S&P Global Ratings assigned its 'AA+' long-term program rating and 'A' underlying rating to South Vermillion Middle School Building Corp., Ind.'s series 2018 ad valorem first-mortgage bonds issued on behalf of South Vermillion Community School Corp., (the school corporation). At the same time, we affirmed our 'AA+' long-term rating on the school corporation's existing ad valorem first-mortgage bonds. The outlook on all the ratings is stable.

The school corporation's overall credit quality is demonstrated by its recent trend of sustaining stable and strong cash reserves that is likely to support ongoing rating stability. In addition, the local economy is also stable due to the stable employment bases within and surrounding the school corporation. In our opinion, however, the rating is constrained by potential negative effects of declines in enrollment on its cash reserves due to its reliance on state aid revenues.

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

- Primarily rural but stable local economy, with adequate incomes, that benefits from broader neighboring communities;
- Strong combined available reserves on a cash basis of accounting; and
- Low overall debt profile with rapid amortization.

The above strengths are offset, in our view by the school corporation's:

- Reliance on state aid revenues and history of demonstrated enrollment decline;
- Moderately concentrated tax base; and
- Adequate but below-average incomes.

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 16, 2017, on RatingsDirect).

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

The series 2018 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 corporations expects to use the bond proceeds from the series 2018 bonds to finance a high school auxiliary gymnasium project, which includes all or part of general facility expansion, improvement, renovation, and equipping projects at existing school facilities.

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 is already occupied and the lease allows payments to be made during construction.

The ad valorem property tax pledge on 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 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 nondebt service funds that receive property taxes. Despite the limitations, we rate the limited-tax GO debt at the same level as our view of the district's general creditworthiness as expressed in the rating on unlimited-tax GO bonds.

Economy

South Vermillion Community Schools serves an estimated population of 11,367 and covers approximately 100.3 square miles in Vermillion County in west-central Indiana. The county is on the Illinois border and is approximately seven miles east of Danville, Ill. Given the proximity to Danville, many residents make the commute for employment opportunities. Vigo County, which a neighboring county, has a broader economic and employment base with employment sectors such as health care, education, and government. The county itself also provides employment opportunities with the leading employer being Eli Lilly & Co. (350 employees), which is also its largest taxpayer, accounting for 20.5% of net assessed valuation (NAV). Although the school corporation has access to a vast

employment base, in our opinion, incomes are only adequate at 81% and 76% of national levels, respectively as measured by median household and per capita effective buying incomes. Both Vigo and Vermillion counties are slated to take on additional industrial development that could boost economic diversity and maintain stability.

The tax base is primarily agriculture based and has seen recent declines in its NAV that could reflect the changes in agricultural land valuations. The declines, however, have been marginal but if they continue, it could weaken the economy. NAV totals \$432 million in 2018 and has come down by 1% since 2016. Gross AV also declined by 1% during the same period and totaled \$669 million. At \$58,929 per capita, the 2018 gross AV is strong, in our opinion.

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 has declined historically, which we understand is due to lower birthrates and the mature nature of the economy. In 2016 and 2017, however, the trend reversed due to changes in how kindergarten students are accounted for. Based on 2018-2019 numbers (1,643), there is a slight decline and projections indicates consistent drops. However, management is anticipating it is likely to remain flat. In our opinion, we expect that further declines are possible. State aid accounted for 99.3% of general fund revenue in 2017.

The corporation's available general fund cash reserve of \$1.9 million is strong on a cash basis of accounting, in our view, at 16% of general fund expenditures at calendar year-end (Dec. 31) 2017. The cash reserves have been increasing in recent years only due to consecutive operating surpluses achieved over the past three years, according to management, because of savings from staff attrition. In 2015, general fund cash reserves were reported at only \$759,000, or 6.9% of expenditures.

We also observed that these increases occurred during periods of stable enrollment growth and future attritional savings but may not be sufficient to offset falling enrollment in later periods.

The school corporation expects to report an increase in its cash reserves to about \$1.9 million by the end of fiscal 2018. Therefore, we expect cash reserves to remain strong and continue to support the rating.

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 consider 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 strong revenue and expenditure assumptions for annual budgeting, which takes into account

six-year historical trends. Monthly budget-to-actual reports are provided to the board but they only identify appropriations and are not comprehensive. Other highlights include an investment policy with annual investment reports to the board, a three- to four-year capital projects fund plan, and an informal fund balance target of 10% of operating expenditures in reserves. The district does not have long-term financial projections or a debt management policy.

Debt

Overall net debt is 2.0% of market value and \$1,198 per capita, which we believe to be low. Amortization is rapid, with 92% of the corporation's direct debt scheduled to be retired within 10 years. Despite rapid amortization, debt service carrying charges were only 9.5% of total governmental fund expenditures (excluding capital outlay) in calendar year 2017, which we consider moderate.

We understand that the school corporation does not have any plans to issue additional debt within the next three years.

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.

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 corporation will likely make the necessary budgetary adjustments and maintain general fund available reserves at a level that we consider strong on a cash basis of accounting for the next two years. It also reflects our views that the stability of the economy is likely to continue provide credit support. As a result, we do not expect to change the rating during the two-year outlook horizon.

Downside scenario

We could lower the rating should enrollment decline and the school corporation is unable to make the timely budgetary adjustments to avoid deterioration of its cash reserves.

Upside scenario

If the school corporation's economic indicators were to increase to levels commensurate with those of its higher-rated peers in conjunction with strengthened cash reserves, we could raise the rating.

Ratings Detail (As Of October 11, 2018)		
South Vermillion Comnty Sch Corp SCHSTPR		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
South Vermillion Middle Sch Bldg Corp, Indiana		
South Vermillion Comnty Sch Corp, Indiana		
South Vermillion Middle Sch Bldg Corp (South Vermillion Comnty Sch Corp) SCHSTPR		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

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 on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2018 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.