

RatingsDirect®

Summary:

Stephenville Independent School District, Texas; School State Program

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| <i>Long Term Rating</i> | AAA/Stable | Current |
| <i>Underlying Rating for Credit Program</i> | AA-/Stable | Upgraded |
| Stephenville Indpt Sch Dist PSF | | |
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| <i>Underlying Rating for Credit Program</i> | AA-/Stable | Upgraded |

Rationale

Standard & Poor's Ratings Services raised its underlying rating for credit program on Stephenville Independent School District, Texas' general obligation (GO) debt one notch to 'AA-' from 'A+'. The outlook is stable.

The upgrade reflects our opinion of the district's maintenance of its very strong reserves, as well as the improvement in our assessment of the district's financial management practices and policies.

The underlying rating reflects our opinion of the district's:

- Very strong finances;
- "Good" financial management practices and policies under our Financial Management Assessment (FMA) methodology; and
- Successful tax ratification election, which will increase operating revenue.

We believe somewhat offsetting these strengths are, what we consider, the district's:

- Adequate income, and
- Moderate debt with extended amortization.

An unlimited ad valorem tax, levied on all taxable property in the district, secures the bonds.

Management

We consider the district's financial management practices "good" under our FMA methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

We revised the FMA for the district to "good" from "standard" based on our understanding of the district's informal financial plan and formally adopted fund balance policy. Accordingly, the informal financial plan forecasts revenue and expenditures five years in advance with comprehensive assumptions that account for wage increases, AV growth, enrollment trends, and state aid. In addition, the district adopted a formal fund balance policy on Aug. 15, 2011, that

states it will maintain 25% of operating expenditures in total fund balance and 18.25% in unassigned fund balance, which the district currently exceeds.

In terms of revenue and expenditure assumptions, management prepares its budgets based on conservative revenue, expenditure, and enrollment trends. Officials monitor the budget monthly and make adjustments as needed. The district has a written, in-depth, and conservative investment policy; it makes monthly updates to the governing body. Management does not currently have a debt management policy or a long-term capital plan.

Finances

A wealth equalization formula, based on property value and average daily attendance (property wealth per student), determines state funding for all school districts. Therefore, increases or decreases in average daily attendance (enrollment) can lead to increases or decreases, respectively, in the amount of state revenue a district receives. Enrollment totaled 3,552 students in 2015.

Enrollment has been fairly stable over the past three years, increasing by a cumulative 2.7% during that span. Management expects similar growth to continue over the next two years to three years.

The district's available fund balance of \$7.2 million was very strong, in our view, at 26% of general fund expenditures at fiscal year-end Aug. 31, 2014. The district reported a surplus operating result of 1.8% of expenditures in 2014. The district depends primarily on property taxes (52.3%) for general fund revenue, followed by state aid (43.5%).

We consider finances very strong. Through conservative budgeting, the district has reported surplus general fund operations in four of the past five fiscal years. For fiscal 2015, unaudited actual results indicate a \$1.9 million addition to fund balance. Management, however, attributes roughly \$1.6 million of surplus proceeds to one-time receipts related to insurance recovery and the sale of land. Actual operations, net of these one-time items, provide an addition of approximately \$320,000 to fund balance. At Nov. 3, 2015, the district successfully passed a tax ratification election, which will effectively raise the operations-and-maintenance (O&M) tax rate by 13 cents to \$1.17 per \$100 of assessed value (AV) and reduce the debt service tax rate by the same amount to six cents per \$100 of AV. While the total direct tax rate of \$1.23 per \$100 of AV remains the same, additional revenue from the raised O&M rate provides greater financial flexibility to address wage increases and technology needs. Due to the successful election, the fiscal 2016 adopted budget indicates operations will provide a \$1.01 million general fund surplus at fiscal year-end.

Economy

Stephenville Independent School District serves an estimated population of 24,336. The median household effective buying income in the district is 80% of the national average and the per capita effective buying income in the district is 85% of the national average, both of which we consider adequate. The district's total \$1.5 billion market value in 2015 is strong, in our view, at \$61,482 per capita. Net taxable AV grew by a total of 9.5% since 2013 to \$1.5 billion in 2015. The 10 leading taxpayers make up an estimated 13.2% of net taxable AV in the tax base, which we consider very diverse.

The district is approximately 60 miles to the west and south of the Dallas-Fort Worth metropolitan area. Stephenville serves as Erath County's seat for the surrounding communities; the city is the hub for county medical, retail, industrial, and education services. Agriculture, manufacturing, and service industries continue to support the local economy.

Tarleton State University, a member of the Texas A & M System, provides further economic stability as the leading employer. In fall 2014, Tarleton's student enrollment was approaching 12,000. County unemployment was 4.5% in July 2015.

Debt

Overall net debt is 3.3% of market value and \$2,000 per capita, which we believe to be moderate. With 43% of the district's direct debt scheduled to be retired within 10 years, amortization is slower than average. Debt service carrying charges were 7.9% of total governmental fund expenditures excluding capital outlay in fiscal 2014, which we consider low.

We understand the district does not currently plan to issue additional debt during the next two years. Officials indicate there is potential for a future bond election in 2018, but there is currently no definitive size or schedule for the possible election.

Pension and other postemployment benefit liabilities

The district paid its total annual required contribution of \$243,000 to its pension obligations in fiscal 2014, or 0.6% of total governmental expenditures. In fiscal 2014, the district also paid \$99,000, or 0.2% of total governmental expenditures, to its other postemployment benefit (OPEB) obligations. The combined pension and OPEB carrying charge totaled 0.8% of total governmental fund expenditures in 2014.

The district participates in the Texas Teachers' Retirement System, which the state administers. The district has historically met its contribution requirements in full, and we believe management will likely continue to meet its required contributions.

Outlook

The stable outlook reflects Standard & Poor's opinion that the district will likely sustain its very strong finances through stable state support and additional revenue derived from the tax ratification election. We also expect enrollment to remain fairly stable during the two-year outlook period.

Upside scenario

While we do not expect it to occur, we could raise the rating if economic expansion were to result in significantly improved wealth and income and if management were to reduce overall debt.

Downside scenario

We, however, could lower the rating if overall finances were to deteriorate, resulting in a decrease in fund balance below the district's formal fund balance policy.

Related Criteria And Research

Related Criteria

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: Key General Obligation Ratio Credit Ranges – Analysis Vs. Reality, April 2, 2008

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- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

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