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Ratings

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Summary:

St. Vrain Valley School District No. RE-1J, Colorado; General Obligation; School State Program

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Credit Profile		
US$60.34 mil GO bnds ser 2018 due 12/15/2027		
Long Term Rating	AA+/Stable	New
Underlying Rating for Credit Program	AA+/Stable	New
St Vrain Vy Sch Dist #RE-1J GO		
Underlying Rating for Credit Program	AA+/Stable	Upgraded
Unenhanced Rating	AA+(SPUR)/Stable	Upgraded

Rationale

S&P Global Ratings raised its long-term rating and underlying rating to 'AA+' from 'AA' on St. Vrain Valley School District No. RE-1J, Colo.'s existing general obligation (GO) bonds. In addition, S&P Global Ratings assigned its 'AA+' long-term rating and underlying rating to the district's series 2018 GO bonds (estimated $60.34 million par amount). The outlook is stable.

The rating action is based on our view of the district's very strong financial profile, supported by consecutive operational surpluses for over a decade and maintenance of very strong reserves, despite expected drawdowns in fiscal 2019. The rating action also reflects the district's extremely strong tax base, which continues to grow through valuation increases and new construction. Adding to the district's credit strength are two fixed mill levy overrides, which provide additional revenue as assessed value (AV) in the district increases. Finally, the rating action reflects the strong enrollment growth in recent years coupled with meticulous capital spending, allowing the district to capture additional students in the near term without any severe capacity constraints.

Security and purpose

The district's full faith and credit secures the GO bonds. All taxable property in the district is subject to an unlimited ad valorem property tax to pay debt service on the bonds. On Nov. 8, 2016, district voters approved the issuance of bonds in an amount not to exceed $260.34 million. The series 2018 GO bonds are the second and final installment of the authorization, and proceeds will be used to fund capital improvements to school facilities and pay the costs of issuance. Upon issuance of the series 2018 bonds, the district will have approximately $591 million in debt outstanding.

In addition to the district's own credit quality, the state aid withholding provision created under Colorado Revised Statutes, Section 22-41-110, provides additional security. Under this provision, if the school district reports that it will not make full payment on the bonds, the state treasurer will forward to the paying agent the amount necessary in immediately available funds to be applied only to debt service.

Credit fundamentals

The ratings reflect our view of the district's:

- Large and diverse economic base, coupled with strong to very strong income indicators and access to the broad and diverse Denver and Boulder metropolitan statistical areas (MSAs);
- Maintenance of very strong available fund balances, along with positive general fund results in consecutive audited fiscal years;
- Additional revenue flexibility through fixed mill levy overrides, which helps the district lower its reliance on state funding;
- Continued trend of enrollment increases in a growing community;
- Strong financial management policies and procedures; and
- Low overall debt as a percentage of district market value.

Partly offsetting the above strengths, in our view, are:

- The state funding formula, which limits the district's revenue-raising ability;
- The district's planned spenddowns of reserves in fiscal 2019, albeit somewhat modest; and
- The district's relatively low state pension funded level, which could lead to future pressure on the district's operating performance.

Economy and district overview

St. Vrain Valley School District No. RE-1J serves an estimated population of 176,000, primarily in northeast Boulder County, including Longmont, and small portions of Broomfield, Weld, and Larimer counties. The area economy centers on biotechnology, high-tech manufacturing, alternative energy research, and higher education stemming from the presence of the University of Colorado at Boulder. The district currently operates 57 schools and programs, and is the seventh-largest school district in Colorado by enrollment. The district's proximity to Denver and Boulder, coupled with extensive residential and commercial development activity, has led to good growth in the district in recent years. According to our calculations, the district's population has increased an estimated 18% in the last 10 years.

The district's access to the Denver and Boulder MSAs provides significant benefit to the district's base of employment. District incomes are strong to very strong, in our opinion, with per capita and median household effective buying income at 122% and 136% of the national levels, respectively. The Boulder County unemployment rate in 2017 averaged 2.4%, which was below state (2.8%) and national (4.4%) figures during that time. Boulder County's unemployment rate is averaging 2.6% through July of 2018. Major employment industries within the county include jobs in professional and technical services, health services, education, and manufacturing. Leading employers in the area include the district itself (3,543 employees), Medtronic PLC--medical devices and products (2,460), Boulder Community Health (2,410), and CenturyLink--communication and internet systems (2,360).

Tax base

Property values in Colorado are assessed every two years to reflect an 18-month lag in market activity. We note 2018 was a nonreassessment year, and therefore, property in Colorado will be reassessed toward the end of the school district's 2019 fiscal year (this will ultimately reflect market activity for the period of July 1, 2017, to June 30, 2018). Despite 2018 being a non-reassessment year, the district still experienced 7% growth in AV from the prior year, totaling $3.46 billion (preliminary, to be officially certified in December 2018), largely due to new residential construction and additional oil and gas production. Corresponding actual value is an estimated $28.6 billion, or, in our view, an extremely strong $163,000 per capita. In the three years prior to 2018, aggregate AV in the district grew by 33%. The tax base is also diverse, in our view, with the 10 largest taxpayers accounting for 17.4% of AV. The largest taxpayer, Kerr-McGee Oil & Gas Onshore, accounts for roughly 7.2% of district AV. The second- and third-largest taxpayers are also oil and gas companies--Crestone Peak Resources and Extraction Oil & Gas LLC, representing approximately 3.4% and 2.2% of total AV in the district, respectively. Given the oil and gas presence within the tax base, the performance of the top contributors and national oil prices can cause AV fluctuations. The majority of the district's tax base is residential, as residential property accounts for about 47.3% of total AV, while commercial property (21.2%), oil and gas (17.5%), and industrial property (7.3%) account for the majority of the remainder.

Looking ahead, we are anticipating continued AV growth at or near the historical trend, largely due to expected home price appreciation and stable demand for housing given this influx of new residents into the region. The greater region continues to attract young, highly skilled professionals, as well as employers, to a growing knowledge-based economy that has helped make the greater region one of the strongest in the country. For additional information, please see our U.S. state and local government credit conditions forecast, published July 26, 2018, on RatingsDirect.

Enrollment

Student enrollment drives operating revenue under the state funding system. The pupil count for districts with declining enrollment is the greatest of a two-year, three-year, four-year, or five-year average of the October counts. So although annual pupil count fluctuations have no material effect on finances, continuing declining enrollment could lead to a material decrease in revenue. With favorable economic trends, district enrollment increased by an annual average of 2.8% in the 2010 to 2017 school years. In 2018, enrollment saw additional growth of 3.2% to 32,421 students. Management attributes the increase to overall growth in the area, as well as new programs and facilities attracting out-of-district transfer students. The district conducts annual in-house demographer reports, and according to management, recent projections are showing growth of at least 350 students during fiscal 2019. Given the strong residential development and continued population growth, management is budgeting for enrollment growth beyond 2019.

Finances

In our opinion, the district's financial position is very strong, reflected by audited general fund surpluses dating back to 2003, in addition to very strong available fund balances. In fiscal 2017, the district reported a surplus operating result of 5.5% of expenditures, increasing available reserves to $97.8 million (36% of expenditures). This amount does not include the 3% Taxpayer's Bill of Rights (TABOR) reserve, which is restricted. Management attributes the continued operational success to gradual increases in state funding, good growth in property tax revenue, an overall conservative budgeting approach, and successful mill levy override campaigns in prior years. Since 2012, the year of the latest mill levy override passage, the district is averaging over 7% revenue growth year over year. The district depends primarily on state aid (50%) and property taxes (41%) for general fund revenue. The district ended fiscal 2017 with total government available cash and investments of $372 million, or 47% of total governmental fund expenditures.

The district has added financial flexibility from mill levy overrides, which the electorate approved in 2008 and 2012 to fund technology replacement and staff recruitment and retention. The mill levy overrides are fixed mill rates, meaning that as AV grows, the district receives additional revenue, rather than only seeing a set dollar amount every year. Colorado statutes restrict the amount of the mill levy override to 25% of a district's total program funding. In 2017, the district's approved mill levy overrides provided an additional $40 million of tax revenue annually, or roughly 20% of total program funding. Given the strong AV growth recently, the district's overrides provide 28% more property tax revenue as opposed to 2012; they produced about $31.3 million in 2012. There is no sunset date for any of the approved mill levy overrides.

According to fiscal 2018 estimates, the district expects to close out 2018 with a $7.4 million general fund surplus (approximately 2.6% of 2018 estimated expenditures), which is about $13.7 higher than original budget projections. According to officials, the projected surplus is largely due to lower salary and benefits provided from unfilled positions, along with cost savings from supplies and materials. The district is budgeting to end the fiscal 2019 school year with a $9 million deficit, largely due to some one-time costs associated with opening new school facilities. According to management, the district anticipates ending slightly better than budgeted, and it has historically done so. Furthermore, given the recent bond authorization spending, we do not expect large transfers out of the general fund for capital expenditures.

Financial Management Assessment

We consider the district's management practices strong under our financial management assessment (FMA) methodology. An FMA of strong indicates our view that practices are strong, well embedded, and likely sustainable.

Highlights of the district's practices and policies include the following:

- The district uses outside sources to estimate projections and to create assumptions for both revenues and expenditures, along with extensive internal enrollment projections.
- The district provides budget-to-actual updates to the board eight times a year and can make changes when needed.
- The district maintains a five-year long-term financial plan that is updated throughout the year.
- The district has a robust facilities plan reassessing facilities and projects over 10 years, looked at annually.
- The district has an investment management policy, and holdings and earnings are provided to the board multiple times a year.
- The district has a debt management policy to help guide financing decisions.
- The district has a 2% minimum reserve policy (above the 3% TABOR reserve) and a target goal range of 20% to 25%, both of which it is adhering to.

Debt, pension, and other postemployment benefit (OPEB) liabilities

After the issuance of the series 2018 bonds, we expect the district's debt levels to be moderate on a per capita basis, at $3,961, and low as a percentage of market value, at 2.4%. With 54% of the district's direct debt scheduled to be retired within 10 years, amortization is average. The debt service carrying charge was 11.3% of total governmental fund expenditures excluding capital outlay in fiscal 2017, which we consider moderate. The series 2018 GO bonds are the second and final installment of the authorization, and the district does not have any near-term plans to return to voters for a new authorization.

The district participates in the Public Employees' Retirement Assn. of Colorado (PERA) to administer its pensions. In fiscal 2017, the district made its full $29.8 million (7.8% of total governmental expenditures) required contribution to PERA. In fiscal 2017, the district also paid $1.7 million, or 0.4% of total governmental expenditures, toward its OPEB obligations. Combined pension and OPEB carrying charges totaled 8.2% of total governmental fund expenditures in 2017. The district's proportionate share of the net pension liability in fiscal 2017, per the new Governmental Accounting Standards Board reporting standards, is about $1.06 billion, representing about 275% of total governmental funds expenditures, a level that we view as high.

Colorado's legislature passed Senate Bill 18-200, which outlines adopted changes to the state's PERA system to restore it to full funding within 30 years. Some of the changes from Senate Bill 18-200 are expected to reduce the unfunded liability--$57.7 billion as of Dec. 31, 2017--and pay it off sooner than envisioned in the most recent valuation report. These changes include a 2% increase in contribution rates for most employees, a 0.25% increase in nonlocal government employers' contribution rates, and a direct annual allocation of $225 million from the state's general fund to PERA beginning in fiscal 2019. Increases to employee and employer contributions are limited to 0.5% annually, or a cumulative 2% above statutory rates. Given the already moderately high pension carrying charges for St. Vrain Valley School District, the additional contribution rate increases could create some budget pressure. According to management, additional increases are factored into long-term financial projections, and the district is expecting near-term increases of only $200,000 in 2019.

Amendment 73

Amendment 73 is a ballot proposal that aims to increase public education funding in the state largely through raising incremental income taxes and the state corporate tax rate. If passed, the amendment would increase individual income taxes for residents making more than $150,000 a year, with the highest graduated rate increasing by 3.62% for earners above $500,000 annually. The proposal would also increase the state corporate tax rate by 1.37%. Additionally, it would create a "Quality Public Education Fund," which would be held by the state and would be exempt from TABOR. (In 1992, Colorado residents approved TABOR, a set of constitutional provisions aimed at limiting overall revenue growth for state and local governments.) The proposed ballot language would not allow the state to use the money to offset general fund appropriations for K-12 education. In total, the Colorado Legislative Council estimates Amendment 73 would generate an additional $1.6 billion for public education by fiscal 2020. We believe passage of Amendment 73 would be a credit positive for Colorado school districts, as the measure is estimated to increase the statewide base per-pupil funding by over 10% by 2020, in addition to providing money for programs like special education, English-language proficiency, at-risk students, and full-day kindergarten.

Outlook

The stable outlook reflects our view of the district's strong economy with participation in the broad and diverse Denver and Boulder economies, in addition to a strong tax base that we expect will continue to grow. The stable outlook also reflects the district's history of strong operational performances and maintenance of very strong reserves, which we believe will be sustained in the near term. Moreover, the outlook reflects the district's additional revenue flexibility through mill levy overrides and management's strong policies and practices. We do not anticipate raising the ratings during the two-year outlook horizon.

Upside scenario

We could raise the ratings if the economy continues to improve, the district can obtain more revenue flexibility through additional voter-approved mill levy overrides (continuing the reduction of reliance from state funding sources), and pension funded levels improve to more sustainable levels.

Downside scenario

Should we come to view the district's operations as having become structurally imbalanced and its reserve levels fall below the district's policy-mandated level, we could lower the ratings.

Ratings Detail (As Of September 14, 2018)		
St Vrain Vy Sch Dist #RE-1J GO bnds		
Long Term Rating	AA+/Stable	Upgraded
Underlying Rating for Credit Program	AA+/Stable	Upgraded
St Vrain Vy Sch Dist #RE-1J GO bnds ser 2016C due 12/15/2036		
Long Term Rating	AA+/Stable	Upgraded
Underlying Rating for Credit Program	AA+/Stable	Upgraded
St Vrain Vy Sch Dist #RE-1J GO rfdg bnds		
Long Term Rating	AA+/Stable	Upgraded
Underlying Rating for Credit Program	AA+/Stable	Upgraded
St Vrain Vy Sch Dist #RE-1J SCHSTPR		
Long Term Rating	AA+/Stable	Upgraded
Underlying Rating for Credit Program	AA+/Stable	Upgraded

Many issues are enhanced by bond insurance.

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.