

RatingsDirect®

Summary:

Arvin Union School District, California; General Obligation

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Credit Profile

US\$4.1 mil GO bnds (Election Of 2014) ser 2019C due 11/01/2048

Long Term Rating

A/Stable

New

Arvin Un Sch Dist GO

Unenhanced Rating

A(SPUR)/Stable

Affirmed

Rationale

S&P Global Ratings assigned its 'A' long-term rating to Arvin Union School District, Calif.'s \$4.1 million series 2019C (election of 2014) general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'A' underlying rating (SPUR) on the district's GO bonds outstanding. The outlook is stable.

Security and use of proceeds

Unlimited ad valorem taxes levied on taxable property within the district secure the GO bonds. The county's board of supervisors has the power and obligation to levy these taxes at the request of the district for the bonds' repayment. We understand proceeds from the series 2019C bonds will be used to finance the construction, acquisition, furnishing, and equipping of district facilities.

Credit overview

Though the district's local economy has grown in recent history, particularly in assessed value (AV), it remains somewhat limited due to adequate-to-low incomes and concentrated tax base. Despite these factors, the district receives favorable revenue treatment under the state funding. While the district has had a trend of deficits in recent history, it has maintained an available fund balance we consider very strong. With expected near balanced operations in fiscal 2019 and budgeted positive general fund result in fiscal 2020, we expect the district to maintain very strong available reserves in the near future.

The rating further reflects our view of the district's:

- Steady AV growth in recent history,
- Favorable revenue treatment under the state funding formula, and
- Trend of very strong available fund balance reserves.

Partially offsetting these factors, in our opinion, is the district's adequate-to-low income indicators and concentrated tax base.

Economy

Arvin Union School District serves an estimated population of 20,806 and is about 19 miles southeast of Bakersfield, located in the southern portion of the Central Valley. The district encompasses Arvin and certain other unincorporated areas of southeastern Kern County. The local economy is largely based on agriculture, but district residents have access to employment opportunities in Bakersfield.

Although AV experienced declines during the recession, in fiscal 2017 it surpassed its pre-recession level. Totaling \$1.5 billion in 2020, we consider AV to be strong at \$72,535 per capita. Roughly 47.9% of AV is associated with the 10 largest taxpayers, representing a concentrated tax base in our opinion. About half of this concentration is attributed to the Pastoria Energy facility (21% of AV), which opened in 2005 and generates power from naturally occurring steam vents. Other large taxpayers include the National Cement Co. of California (9.1% of AV), the Tejon Ranch (6.4%), and Anthony Vineyards Inc. (3.7%).

In our opinion, median household effective buying income (EBI) is adequate at 71% of the national level, but per capita EBI is low at 36%. The district's agrarian economy can lead to substantial swings in employment rates, with unemployment reaching nearly 40% in fiscal 2010, before dropping to 7.9% in fiscal 2019. This represents an unemployment rate roughly twice the state and national averages. We note, however, that these shifts in employment have not contributed to significant changes in the size of the local population.

Finances

General purpose funding for California school districts is determined by a formula based primarily on average daily attendance (ADA), grade levels served, and share of students served that are English language-learners, low to moderate income, or foster youth. This share is known as the district's "unduplicated count". Most school districts are funded through a combination of state general fund revenue and local property tax revenue, up to the amount determined by formula. For these districts, increases or decreases in ADA can lead to increases or decreases, respectively, in general purpose funding under the formula. Unduplicated students account for 97% of the district's student population, generating 41% more revenue than if the district had no unduplicated students, which provides some additional financial flexibility, though it also entails mandated spending to increase or improve services for targeted students in proportion to supplemental funding. Enrollment had been declining since 2013 and had cumulatively decreased by 9.7% through 2018 but started increasing in 2018 and continued through 2019. Estimated ADA in fiscal 2020 is 2,978.

Despite this strong revenue growth, the district has experienced a series of deficits in six of the seven post-recessionary years. A deficit of \$1.1 million (2.7% of expenditures) was realized in fiscal 2017 and a more modest deficit of \$500,000 (1.3%) was realized in fiscal 2018. These drawdowns were largely attributed to a growth in salaries and benefits, with certificated and classified salary expenditures growing by 21.1% and 35.7%, respectively, from 2014 to 2018. However, the district also regularly makes significant one-time expenditures, such as by spending \$2.5 million (6.7%) on books and supplies in fiscal 2018. If needed, we believe that the district could reduce these one-time expenditures if its revenue were to decline in the future. The district's available fund balance reserve totaled 16.4% of general fund expenditures in fiscal 2018, a level we consider very strong.

Unaudited actuals for fiscal 2019 indicate nominal deficit of approximately \$189,000, or less than 1% of expenditures

after a transfer of \$500,000 to its fund 17, which we consider available. With this result, its available fund balance reserve totaled \$7.75 million, or 18.8% of expenditures. Looking forward, the district does not expect major cost pressures and has budgeted for a positive result in fiscal 2020.

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. Highlights include:

- Requirement to provide revenue and expenditures projections and underlying assumptions, which include ADA changes, contract settlements, and cost-of-living adjustments. The district uses historical data to forecast revenue and expenditures and relies on guidance from its financial oversight agency to forecast state revenue assumptions;
- Budget-to-actuals presented to the board on interim basis: first interim, second interim, and estimated/budget adoption during the year, while additional budget items are presented to the board throughout the year;
- Financial forecast for the current and subsequent two fiscal years;
- Lack of an updated formal capital plan;
- Mandatory investments in a county pool, which is managed under a comprehensive policy and quarterly reports to the board by management on holdings and performance; and
- A debt policy, in compliance with California Senate Bill 1029, that defines debt issuance guidelines for areas such as amount, oversight, structure, timing, and type, but lacks specific numerical constraints; and
- Formal board policy to maintain 17% minimum unassigned fund balance policy, tied to protection against revenue shortfalls or unpredicted one-time expenditures, which the district expects to meet in fiscal 2019.

Debt

Inclusive of this issue, overlapping and direct totaled \$56.2 million. Overall debt is moderate at \$2,693 per capita and 3.7% of market value. Amortization is slower than average, with 31% of the district's direct debt scheduled to be retired within 10 years. Debt service carrying charges were 4.0% of total governmental fund expenditures excluding capital outlay in fiscal 2018, which we consider low. After issuance of the series 2019C, the district will have approximately \$15.9 million remaining from two separate measures, \$11.6 million from a 2018 election and \$4.3 million from a 2014 election. The district does not anticipate issuing any additional debt in the next 12-18 months.

Pension and other postemployment benefit (OPEB) liabilities

We do not view pension and OPEB liabilities as a near-term source of credit pressure for the district despite lower funding levels and our expectation that costs will increase.

While the district's pension contributions for are set to increase for the next few years, the statutory funding policy for the district's larger pension plan mitigates the risk of dramatic cost escalation contributions because the state is required to absorb most of any needed future cost increases.

The district participates in the following plans as of June 30, 2018:

- California State Teachers Retirement System (CalSTRS): 71% funded with a net pension liability of \$22.9 million;
- California Public Employees Retirement System (CalPERS): 71% funded with a net pension liability of \$10.1 million;

- Single-employer pay-as-you-go OPEB plan with a net OPEB liability of \$5.4 million.

The district paid its full required contribution of \$3.0 million toward its pension obligations in fiscal 2018, or 6.2% of total governmental expenditures. The district's actual 2018 statutorily required CalSTRS contributions fell short of both static funding and minimum funding progress, indicating the district's pension liability increased. However, the statutory funding plan requires the state, which is responsible for about a third of all districts' pension liabilities, as well as districts to increase their contribution rates through 2021 to achieve full funding by 2046. Given that legal discretion for CalSTRS to increase rates to address new unfunded liability caps district contributions only slightly above the 2021 level, we believe the state will absorb most rate increases, limiting future cost increases to districts. However, if current actuarial assumptions are not realized existing authority to increase state contributions may not be sufficient to eliminate new unfunded liabilities generated before 2046 without additional increases to district contribution rates beyond the existing legal limit.

For more on our view of California school district pension liabilities, see our analysis "Thanks To A Strong Economy, California's School Districts Can Face Continued Pension Increases--Though Will This Last?" published Nov. 8, 2018.

Outlook

The stable outlook reflects the district's expected stable enrollment trend, which is the primary driver of revenue, and our expectation the district will be able to maintain very strong available reserves. We do not anticipate changing the rating during the outlook's two-year horizon.

Upside scenario

Should the district's local economy diversify and improve, particularly in local incomes, while the district maintains very strong available reserves, we could raise the rating.

Downside scenario

Should the district demonstrate structural imbalance, resulting in available reserves we no longer consider very strong, we could lower the rating.

Ratings Detail (As Of November 15, 2019)

Arvin Un Sch Dist GO (AGM) <i>Unenhanced Rating</i>	A(SPUR)/Stable	Affirmed
Arvin Un Sch Dist GO (ASSURED GTY) <i>Unenhanced Rating</i>	A(SPUR)/Stable	Affirmed
Arvin Un Sch Dist GO (MAC) <i>Unenhanced Rating</i>	A(SPUR)/Stable	Affirmed
Arvin Un Sch Dist GO (MCA) <i>Unenhanced Rating</i>	A(SPUR)/Stable	Affirmed

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

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