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Ratings

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Summary:

Washoe County School District, Nevada; General Obligation; School State Program

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Washoe County School District, Nevada; General Obligation; School State Program

Credit Profile		
US$85.0 mil sch imp bnds ser 2018 due 10/01/2048		
Long Term Rating	AA/Stable	New
Washoe Cnty Sch Dist GO		
Long Term Rating	AA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA' long-term rating to Washoe County School District, Nev.'s series 2018 general obligation (GO) school improvement bonds (par amount: $85 million). At the same time, S&P Global Ratings affirmed its 'AA' long-term rating and underlying rating (SPUR) on the district's existing GO debt. The outlook is stable.

Some of the district's bonds outstanding are eligible for, and participate in, the Nevada School District Bond Guarantee program, supported by the constitutional pledge of the Nevada permanent school fund's assets.

In our view, the district still holds a strong overall financial position, despite recent budgetary challenges largely stemming from declining expenditure flexibility. Management attributes some of the deficit spending to increased costs for special education. Dating back to 2011, the district has reduced its audited general fund balances by $28 million. District officials have taken steps to becoming balanced long term, including implementing a priority-based budgeting practice and analyzing all budget line items closely. Although management has implemented budgetary actions to address the deficits, the district is still expecting to close out 2019 with another deficit. We expect management to shorten the deficit gap by the end of the fiscal year, as it has done historically.

Security and purpose

The district's full-faith-and-credit pledge to levy a sufficient ad valorem tax to cover debt service secures the GO bonds. The levy is subject to the state's constitutional limit of $3.64 per $100 of assessed value (AV). The total overlapping tax rate in fiscal 2018 was $3.66, but two cents of the state rate is exempt from the $3.64 cap. These levels are consistent with historical levels. The 2018 bonds are additionally secured by a lien on a 0.54% sales and use tax imposed within Washoe County. Although the sales tax revenue provides sufficient maximum annual debt service coverage on the series 2018 bonds, we consider the district's full-faith-and-credit pledge to be the stronger of the two revenue pledges. Proceeds from the series 2018 bonds will be used to construct new schools and to pay the costs of issuance. The district has approximately $762 million in debt outstanding.

Credit fundamentals

The ratings reflect our view of the district's:

- Broad and diverse tax base, along with good AV growth recently, leading to extremely strong market value per capita;

- Enrollment growth in recent years, which management expects will continue;
- History of strong to very strong general fund balances; and
- Low debt per capita and as a percentage of market value.

Partly offsetting the above strengths, in our view, are the district's operating deficits in recent years, leading to modest fund balance declines and the need for management to make budget cuts.

Economy

The district is coterminous with Washoe County, which is the state's second-most populous county, having roughly 456,000 residents. The county's largest cities are Reno and Sparks, so the local economy centers on tourism and gaming. However, the health care, education services, and industrial sectors have been growing. The district is the county's leading employer, followed by the University of Nevada. Income levels are good, in our view, with median household and per capita effective buying incomes at 101% and 97% of the national averages, respectively. The county's employment gains have increased steadily in recent years, and the unemployment rate in 2017 was 4.2%. The county's unemployment rate is averaging 3.9% through August of 2018.

The district's total $48.2 billion market value in fiscal 2019 is extremely strong, in our view, at roughly $106,000 per capita. AV growth has been strong recently, with AV increasing by an average of 6.5% a year for five years to $16.9 billion in 2018. Roughly 3.1% of AV comes from the 10 largest taxpayers, representing a very diverse tax base, in our opinion. Management expects the area to continue to experience AV growth as commercial and residential development continue. Moreover, northern Nevada is seeing sizable investments from large companies like Tesla Inc. and Apple. District officials believe these investments will continue to contribute to AV, population, and enrollment growth in the next several years.

Enrollment

Nevada school district enrollment count is based on average daily enrollment (ADE), which takes into account student enrollment for the whole school year. Furthermore, if ADE had decreased 5% or more from the same quarter of the immediately preceding school year, the larger enrollment from the current or preceding school year would be used. Funding is determined by the Nevada Equity Allocation Model, which takes into account demographic characteristics of each district, weighted average costs of operations, salaries and benefits, transportation, and district wealth. Enrollment has remained relatively flat in the last three years, but the district experienced some modest growth in years prior. Since 2012, enrollment has increased by an aggregate 2.7% to 63,914 students in 2018. Officials expect enrollment to grow in the coming years, but is currently budgeting for a modest ADE decline to 63,876 in 2019.

Finances

Despite facing recent external and internal fiscal challenges, through a difficult state funding environment, limited expenditure flexibility, and recent lawsuit settlements, the district's financial profile remains strong, in our view. Officials previously set aside money for previous lawsuit settlements, and we do not expect major payments for lawsuits in the near term. The district ended fiscal years 2014 and 2015 with surpluses of $5.6 million and $2.4 million, respectively, which management attributed to stronger-than-anticipated revenue, additional cost-saving measures, and lower overall expenditures. More recently, the district has experienced operational deficits, largely as a result of salary increases, additional contributions to special education programs, and lower-than-expected enrollment. In fiscal 2017, the district reported a deficit operating result of roughly $10 million (2.5% of expenditures). Management attributes the fiscal 2017 deficit to larger transfers out of the general fund for planned increases in special education funding. The district's available fund balance of $42.2 million is strong, in our view, at 10.5% of general fund expenditures at fiscal year-end (June 30) 2017. Despite the deficit, the district ended the year better than budgeted, which it has historically done; officials originally budgeted for an operating loss of roughly $24 million. We understand that the shortfall required management to utilize unassigned fund balances to open up the 2018 school year.

The district concluded fiscal 2018 (the most recent audited year) better than budgeted, but ultimately did experience another operating deficit. Originally, the district budgeted for a $22.7 million shortfall, and ended the year with a modest $2.4 million loss (less than 1% of expenditures). According to officials, board-approved budget cuts and steady revenue growth were the large reasons for ending the year almost balanced. We note that district officials did not cut a significant amount of staff to balance the budget, and instead increased class sizes, reduced fleet vehicle purchases and routes, and scaled down textbook costs. As of June 30, 2018, the district's available fund balance is strong at 9.5% of general fund expenditures, totaling roughly $40 million. The fiscal 2019 budget reflects a $7.5 million operating deficit, but we believe management may ultimately shorten the deficit gap, as it has done historically, and could likely end 2019 balanced.

In November 2016, residents of Washoe County approved initiative WC-1, which imposed a sales and use tax of 0.54% to fund capital projects of the school district. The sales tax does not have a sunset date, and in the last 12 months, collections are averaging $3.7 million per month, or a total of $44 million. District officials are budgeting to end the year with roughly $45.8 million in sales tax revenue. In addition, management anticipates that the tax revenue will alleviate many of the capacity concerns for the district's schools, and also ease the potential future pressure on the general fund to support ongoing capital needs.

Management

We consider the district's financial practices good under our Financial Management Assessment (FMA) methodology, indicating our view that financial practices exist in most areas but that governance officials might not formalize or regularly monitor all of them.

The district's financial practices include the following:

- The district uses outside sources to make projections and to create assumptions for both revenue and expenditures as well as for enrollment projections.
- The district provides monthly budget-to-actual updates to the board and can make changes when needed.
- The district follows state guidelines for long-term financial planning and has two-year projections.
- The district has a three-year capital plan and associates money with projects.
- The district has an investment management policy and provides holdings and earnings information to the board on a quarterly basis.
- The district has a debt management policy that it reviews annually. The plan does not allow swaps or variable-rate

debt.

- The district has a policy of maintaining a minimum of 2% of expenditures in the general fund reserve, although its practice has been to maintain a minimum of about 8% to 10% of expenditures.

Debt

Overall net debt is 2% of market value and $2,146 per capita, which we believe to be low. Amortization is average, with 54% of the district's direct debt scheduled to be retired within 10 years. The debt service carrying charge was 7.9% of total governmental fund expenditures excluding capital outlay in fiscal 2017, which we consider moderate. District officials believe the issuance of the 2018 bonds, along with additional revenue from the new sales tax, will be sufficient to cover capital needs for the remainder of fiscal 2019. However, we note that the district could issue additional debt in fiscal 2020. In August 2017, the district issued GO bonds that were privately placed and not rated. The debt issuance includes no acceleration provisions, so we understand that an acceleration of full payment is not likely to occur. The aggregate amount of the debt totaled approximately $3.1 million, and the district holds sufficient reserves, cash on hand, and time to tap external liquidity to handle the total amount of the privately placed debt.

The district participates in the Public Employees Retirement System of the State of Nevada, and in fiscal 2017 paid its full required contribution of $90.4 million, or 13.4% of total governmental expenditures, toward its pension obligations. Using updated reporting standards in accordance with Governmental Accounting Standards Board Statement Nos. 67 and 68, the district's proportionate share of the net pension liability was $734 million as of June 30, 2017: 74% funded, using its fiduciary net position as a percentage of the total pension liability. The district participates in three plans for its other postemployment benefits (OPEBs) and contributed $2.2 million, or 0.3% of total governmental expenditures, toward its OPEB obligations in fiscal 2017. Combined pension and OPEB carrying charges totaled 13.7% of total governmental fund expenditures in 2017.

Outlook

The stable outlook reflects our opinion of the district's growing economy and tax base growth in recent years, which we expect to continue in the near term. The stable outlook also reflects our anticipation that the district will maintain at least good to strong available reserves, despite some budget challenges in recent years. Furthermore, the stable outlook reflects management's close budget monitoring and good overall financial policies, which we anticipate will contribute to reducing the district's current budget deficits projected in fiscal 2019.

Downside scenario

Should the district continue to utilize available reserves to help balance the budget, leading to a decline in fund balances to levels we no longer consider strong, we could lower the ratings.

Upside scenario

If the district is able to sustain operational surpluses for multiple years, leading to increased and maintained reserves at very strong levels, we could raise the ratings.

Ratings Detail (As Of November 2, 2018)

Ratings Detail (As Of November 2, 2018) (cont.)		
Washoe Cnty Sch Dist GO		
Long Term Rating	AA/Stable	Affirmed
Washoe Cnty Sch Dist GO		
Long Term Rating	AA/Stable	Affirmed
Washoe Cnty Sch Dist GO bnds		
Long Term Rating	AAA/Stable	Current
Underlying Rating for Credit Program	AA/Stable	Affirmed
Washoe Cnty Sch Dist GO (ltd tax) sch imp and rfdg bnds		
Long Term Rating	AA/Stable	Affirmed
Washoe Cnty Sch Dist GO (AGM)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Washoe Cnty Sch Dist GO		
Unenhanced Rating	AA(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 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.