Rationale

S&P Global Ratings affirmed its 'AA' rating on Centennial School District, Pa.'s general obligation (GO) debt outstanding. The outlook is stable.

The bonds are secured by the full faith and credit pledge of the school district. While the security pledge on the series 2009A bonds is subject to the Act 1 index and considered limited tax, the series 2009B and 2010A bonds are exempt since they were issued prior June 2006, when Act 1 was established.

The Act 1 Index under Pennsylvania commonwealth statute restricts a district's ability to raise the tax levy higher than a certain index, which the Pennsylvania Department of Education determines. 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 our rating on the unlimited-tax GO bonds. We are rating the district's limited-tax GO debt based on the application of our criteria, titled "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" (published Jan. 22, 2018, on RatingsDirect).

The ratings reflect our opinion of the district's:

- Stable property tax base with access to a strong employment base;
- Consistently strong financial position;
- Good financial management practices under our Financial Management Assessment (FMA) methodology, and
- Moderate net debt per capita.

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

- Budgetary pressure related to increasing debt and pensions; and
- General Fund Reserve levels and Economic Indicators, while at levels we consider strong, are lower than its higher-rated peers.

Economy

Centennial School District serves an estimated population of 48,323 in southwestern Bucks County, approximately 17 miles north of Philadelphia. Significant employment opportunities both countywide and in Philadelphia enhance the district's economy. Median household and per capita effective buying incomes in the district are strong at 124% and 117% of national levels, respectively.

In our opinion, the district's total $4.6 billion market value in 2017 is very strong at $95,640 per capita. Assessed value (AV) has remained stable at $545.6 million in 2017. The area of the district is primarily built-out; however, management notes new construction of homes from previous sold land by the district, and anticipates modest growth in AVs. The tax base is very diverse, in our view, with the 10 largest taxpayers accounting for approximately 4.9% of AV.

Enrollment totaled 5,475 in fiscal 2018 and has seen an approximately 2% decline since 2014, which reflects lower birth rates. Management implemented a full-day kindergarten for 2017-2018, along with updating the schedules of high school students to an eight-period block. As a result, according to management, staff positions that would have been eliminated through attrition and enrollment declines were able to be re-deployed. The contracts with teachers are valid until June 2020.

Finances

We consider the district's finances strong. The district has what we consider a strong record of conservative budgeting, forecasting deficits but ending the fiscal year with general fund surpluses. It has had audited general fund surpluses in five of the past six years from fiscal years 2012-2017.

For fiscal 2019, the district is budgeted for a deficit of $500,000 (for contingency), but expects to maintain at least balanced operations. It will seek Act 1 exemptions and anticipates continued strong performance from health care plans.

For projected fiscal 2018, the district anticipates close to balanced operations (expecting the likely range to be between a $250,000 deficit and a $225,000 surplus). Over fiscal 2018, management noted very strong revenues from interim tax collections, but these were partially offset by updates from the Pennsylvania Department of Education on how it calculates charter school tuition rates (the amount of students attending charter schools in the area tends to be around 60). Additionally, there were some elementary school grades with larger class sizes that necessitated some long-term substitute teachers or splitting up some classes into sections.

For audited fiscal 2017, the district had a general fund surplus after transfers of $348,000, or 0.3% of expenditures. It had higher revenues partially due to PlanCon (reimbursements from the commonwealth for construction projects). Additionally, it reduced expenditures by altering pharmacy benefits, including implementing pre-authorizations for certain drugs and migrating to a more cost-effective platform.

The surplus results in audited fiscal years 2016 and 2017 allowed the district to increase its available fund balances approximately 9% since 2015 (which includes committed amounts that are available for general operating with board approval). The current level of $10.7 million is strong, in our view, at 9.7% of general fund expenditures at fiscal year-end (June 30) 2017.

Management

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

Highlights include management's five years (with an emphasis on the last three) of historical data for revenue and expenditure assumptions. Management provides budget-to-actual results to the board monthly with the ability to amend. The district maintains both long-term, five-year capital and financial plans. It also maintains a debt management policy in regard to post-issuance compliance.

The district’s investment policy calls for monthly reporting on investment holdings. Management also maintains a formal reserve policy that calls for keeping 5%-8% of general fund expenditures, which it is currently meeting; management chose this policy for cash-flow purposes and to guard against unforeseen expenditures.

Debt

Overall net debt is 4.7% of market value and $4,669 per capita, which we believe to be moderate. Amortization is slow, with 34% of the district's direct debt scheduled to be retired within 10 years. Debt service carrying charges were 8.3% of total governmental fund expenditures excluding capital outlay in fiscal 2017, which we consider moderate currently, however due to back loaded payments, this cost could increase in the future in our opinion. We have confirmed that the district does not have any privately-placed debt outstanding.

Pension and other-postemployment-benefit liabilities

All Pennsylvania school districts participate in the commonwealth's Public School Employees' Retirement System (PSERS). Pension costs have been a budget stress for this district and almost all commonwealth districts. While contribution rates have somewhat leveled off, we believe pension costs will likely present budgetary challenges.

In fiscal 2017, the district paid its full required contribution of $16.0 million, or 13.3% of total governmental expenditures, toward its pension obligations. It also paid $111,000, or approximately 0.1% of total governmental expenditures, toward its other postemployment benefit (OPEB) obligations in fiscal 2017. The combined pension and OPEB carrying charge totaled 13.4% of total governmental fund expenditures in fiscal 2017.

In accordance with Governmental Accounting Standards Board Statement No. 67, PSERS’ net pension liability was $49.4 billion at June 30, 2017; the funded ratio, which consists of PSERS’ fiduciary net position as a percentage of the total pension liability, was 50.1%, lower than the fiscal 2016 funding level of 54.4%. The district's proportion of the net PSERS liability, as of the most recent actuarial valuation, was $205.1 million. The share reflects statutorily required contributions related to all reporting units' statutorily required contributions for the measurement period.

Outlook

The stable outlook reflects S&P Global Ratings' opinion that it will likely not change the rating during the two-year outlook period because it believes the district will likely maintain strong budgetary performance and flexibility through general fund reserves.

Downside scenario

We could lower the rating if fund balance reserves were to weaken for any reason to levels we no longer consider commensurate with the rating.

Upside scenario

We could raise the rating if economic metrics, such as median household income levels, were to improve, coupled with higher general fund reserves that we consider commensurate with higher rated peers.