STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

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Summary:

East Lansing School District, Michigan; School State Program

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Summary:

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Credit Profile		
East Lansing Sch Dist rfdg bnds (GO - unltd tax) (federally taxable)		
Long Term Rating	AA-/Positive	Current
Underlying Rating for Credit Program	AA-/Stable	Affirmed
East Lansing Sch Dist SCHSTPR		
Long Term Rating	AA-/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services has revised its outlook to stable from negative and affirmed its 'AA-' underlying rating on East Lansing School District, Mich.'s existing general obligation (GO) bonds.

The revised outlook reflects the district's recent and projected improved budgetary performance, which should help it to increase its general fund reserves.

A pledge of the district's full-faith-credit-and-resources and an agreement to levy ad valorem property taxes without limit to rate or amount secure the outstanding bonds.

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

- Participation in the diverse economy of the Lansing-East Lansing metropolitan area;
- Stable enrollment, which directly affects the district's finances because of the state funding formula;
- Good general fund balance level despite some drawdowns but district posted surplus in 2015 and expects another surplus in 2016; and
- Low to moderate overall debt burden.

Limiting credit considerations are:

- Adequate, but below average, income level, which is influenced by the presence of a large number of Michigan State University students;
- Elevated debt service carrying charges, which reflects rapid amortization; and
- Low funded pension, which could lead to future budgetary pressures.

In our opinion, the district's overall financial profile has been somewhat inconsistent as the general fund has used and added to its reserve base over the past five years but overall has maintained what we would consider good reserves (7.3% of operating expenditures as of June 30, 2015).

Management has indicated it expects to adopt a budget for fiscal 2017 that will call for a slight use of reserves but officials have indicated it has no plans to materially spend down its reserves over the next few years. For fiscal 2016, the original budget called for a use of $120,000 of reserves but through the first six months of the year the district now expects to materially add to its reserves with a projected surplus of nearly $1.2 million. Officials cite receiving more students than originally budgeted for as the main reason for the projected increase in reserves as well as underestimating the state foundation level it would receive on a per pupil basis. If the surplus of $1.2 million does occur it would put reserves at about 11% of operating expenditures.

The last audit on June 30, 2015, yielded a surplus of $367,607 that increased the available general fund balance to $2.6 million, or 7.3% of operating expenditures, which we consider good. State aid represented nearly 65% of the total general fund revenues while property taxes contributed about 23%. The district had budgeted a use of $187,000 (first revision) of reserves but typically is conservative in its assumptions when it produces the original budget. Officials cite savings on employee health benefits as the main reason for the turnaround.

The 14.4-square-mile district is located mainly in the city of East Lansing in Ingham County and also serves residents in Clinton County. The estimated number of residents that the district serves is 56,019. With the state capital in neighboring Lansing, the economy is dominated by state employment. In addition, with the presence of Michigan State University (MSU)--the largest employer in East Lansing--the income indicators are affected. The average unemployment rate in calendar 2014 for Ingham County is 6%, which is lower than the state rate of 7.2% for the same time period.

We consider the district's per capita and median household effective buying income (EBI) to be adequate, but below average--due to MSU--at 73% when compared with the national average. Taxable valuation slightly increased for the second year in a row to $1.05 million for fiscal 2015 and management expects a 2.5% increase for 2016. The total market value of $2.5 million equated to $44,170 per capita for fiscal 2015, which we view as adequate. We consider the property tax base very diverse, with the 10 leading taxpayers accounting for 10% of taxable valuation.

Overall the district's enrollment has remained stable with slight gains and losses over the last six years but for fiscal 2016, the district gained nearly 4% from fiscal 2015 to 3,642 students. Officials have indicated that on an unaudited basis, the district has received about 52 more than it originally predicted and it attributes it to expansion of the school of choice program. Officials stated that enrollment should remain at about the 3,650 student mark for the next five years. The district participates in the school of choice program, whose students represent about 23% of the current student population. Officials maintain that it typically has breakeven results for students that enter and leave the district each year.

Standard & Poor's considers the district's financial management practices "standard" under its Financial Management Assessment methodology, indicating the finance department maintains adequate policies in some, but not all, key areas. The district performs a line by line budget approach with three years of historical information. The budget can be amended as needed and the board is updated a few times per year with a "budget to actual" report. The district does not have a formal long-term financial plan. The district does not have a formal long-term capital plan but meets annually to discuss the most pressing needs and have a replacement plan for its technology needs. The district has a sinking fund, the purpose of which is to alleviate some pressure on the general fund, and which will be up for voter renewal in fiscal 2018. The district has its own investment policy and annually reports the performance and holdings of its investments. There is no official debt management policy but the district adheres to state guidelines. Officials state that there is an official reserve policy to maintain reserves between 10% and 15% of operating expenditures so as to ensure cash flow throughout the year. The district is currently not meeting this policy.

We consider the district's overall debt low at $1,664 per capita and more moderate at 3.9% of market value. We also consider debt service carrying charges elevated at 16% of fiscal 2015 expenditures. Amortization is rapid, with the district planning to retire 70% of debt over the next 10 years. Management has confirmed that the district has no alternative financing obligations. It is our understanding that the district doesn't have official plans to issue debt but is discussing a possible bond vote for November 2016, which could range between $20 million and $50 million for improvements to its elementary school buildings.

The district participates in Michigan's Public School Employees' Retirement System (MPSERS) and contributed $5.4 million to the plan in fiscal 2015. All retirees participating in MPSERS receive postemployment health care benefits, which are also funded by the district's total contributions to the plan. The combined pension and other postemployment benefit contributions equaled nearly 12.5% of total government expenditures in fiscal 2015, which we consider high.

The district contributes to MPSERS, a cost-sharing multiple-employer pension plan administered by the state, for pension benefits and the vast majority of its OPEB benefits. State statute establishes and may amend MPSERS benefit provisions. For our calculation purposes, we considered the district's statutorily determined contribution its required pension contribution. Per Government Accounting Standards Board (GASB) 68 standards, which the district implemented for its financial statements ended June 30, 2015, employers with benefits administered through cost-sharing multiple-employer pension plans such as MPSERS must report their proportionate share of the net pension liability.

The net pension liability for the MPSERS plan as of Sept. 30, 2014, (last actuarial) was $22 billion and the funded ratio, which consists of the plan fiduciary net position as a proportion of the total pension liability, was 66.2%. The district's proportion of the net MPSERS liability as of the most recent actuarial valuation (Sept. 30, 2014) was $48.5 million or 0.22017 percent. The district's proportionate share of the net pension liability is based on statutory required contributions in relation to all reporting units' statutorily required contributions for the measurement period.

The district does not expect its postretirement carrying charges to increase substantially in the next two to three years and the state held required contribution rates flat for fiscal 2016; however, consistently low pension funded ratios could likely lead to an eventual increase in contributions and potential budget stress.

Outlook

The stable outlook on the underlying rating reflects our expectation that the district will continue to make the necessary adjustments to maintain at least good reserves, and to maintain its low to moderate debt profile and as such we do not expect the rating to change during our two-year outlook period.

Upside scenario

A higher underlying rating is possible if the district can build its reserves to a level that we feel is commensurate with higher rated peers as well as an improvement in the economic income indicators.

Downside scenario

A lower underlying rating is possible if the budgetary performance materially deteriorates and negative affects the district's reserves.

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
- 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

Related Research

Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015

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