Chambersburg Area School District, PA

New Issue: Moody's assigns Aa3 to Chambersburg ASD, PA's $9.8M GO bonds

Summary Rating Rationale
Moody's Investors Service has assigned a Aa3 underlying rating to Chambersburg Area School District, PA's $9.8 million General Obligation Bonds, Series A of 2016. Moody's maintains an Aa3 underlying and Baa1 enhanced rating on the district's $148 million in outstanding general obligation debt. Both the underlying and enhanced rating have negative outlooks.

The Aa3 underlying rating incorporates the district’s large tax base, adequate, yet declining, reserves that are augmented by other funds, and a higher than average debt position with slow payout.

The Baa1 enhanced rating applies to the district’s outstanding bond series and reflects the availability of state aid for debt service obligations in light of the commonwealth’s chronically late budgets and the lack of clarity surrounding the intercept program’s mechanical feasibility in the absence of an approved and implemented budget.

Credit Strengths
» Sizeable and stable tax base
» Strong population growth
» Reserves outside of General Fund operations

Credit Challenges
» Growing expenditure pressures related to employee pension benefits
» Planned draws on reserves limiting financial flexibility
» Above average debt burden with slow payout

Rating Outlook
The negative outlook factors the district’s recent narrowing of available reserves and liquidity. The outlook also considers the district’s limited revenue raising ability and increasing fixed costs such as employee pensions and benefits, which will remain a challenge as the district works to restore structural balance and improve reserves and liquidity.
The enhanced rating has a negative outlook which is based both on the outlook for the commonwealth and the ongoing uncertainty surrounding its ability to fund the intercept programs during budget stalemates.

**Factors that Could Lead to an Upgrade (removal of the negative outlook)**

» Considerable tax base expansion and improvement of the district’s demographic profile

» Improved General Fund reserve and liquidity levels

**Factors that Could Lead to a Downgrade**

» Structurally imbalanced operations, resulting in narrowing of available reserves and liquidity

» Inability to meet 2016 projections

» Increased debt burden

**Key Indicators**

### Exhibit 1

<table>
<thead>
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<tbody>
<tr>
<td><strong>Economy/Tax Base</strong></td>
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<tr>
<td>Total Full Value ($000)</td>
<td>$5,032,104</td>
<td>$4,703,449</td>
<td>$4,574,614</td>
<td>$4,686,104</td>
<td>$5,145,347</td>
</tr>
<tr>
<td>Full Value Per Capita</td>
<td>$76,597</td>
<td>$70,695</td>
<td>$68,218</td>
<td>$69,492</td>
<td>$76,302</td>
</tr>
<tr>
<td>Median Family Income (% of US Median)</td>
<td>N/A</td>
<td>94.6%</td>
<td>94.6%</td>
<td>94.6%</td>
<td>94.6%</td>
</tr>
<tr>
<td><strong>Finances</strong></td>
<td></td>
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<tr>
<td>Operating Revenue ($000)</td>
<td>$107,433</td>
<td>$107,068</td>
<td>$110,218</td>
<td>$111,555</td>
<td>$116,449</td>
</tr>
<tr>
<td>Fund Balance as a % of Revenues</td>
<td>15.1%</td>
<td>19.0%</td>
<td>17.0%</td>
<td>12.3%</td>
<td>8.2%</td>
</tr>
<tr>
<td>Cash Balance as a % of Revenues</td>
<td>11.9%</td>
<td>13.1%</td>
<td>12.7%</td>
<td>11.4%</td>
<td>10.0%</td>
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<td><strong>Debt/Pensions</strong></td>
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<tr>
<td>Net Direct Debt ($000)</td>
<td>$137,729</td>
<td>$144,415</td>
<td>$141,550</td>
<td>$139,820</td>
<td>$145,650</td>
</tr>
<tr>
<td>Net Direct Debt / Operating Revenues</td>
<td>1.3x</td>
<td>1.3x</td>
<td>1.3x</td>
<td>1.3x</td>
<td>1.3x</td>
</tr>
<tr>
<td>Net Direct Debt / Full Value (%)</td>
<td>2.7%</td>
<td>3.1%</td>
<td>3.1%</td>
<td>3.0%</td>
<td>2.8%</td>
</tr>
<tr>
<td>Moody’s - adjusted Net Pension Liability (3-yr average) to Revenues (%)</td>
<td>N/A</td>
<td>0.7x</td>
<td>0.8x</td>
<td>1.0x</td>
<td>1.2x</td>
</tr>
<tr>
<td>Moody’s - adjusted Net Pension Liability (3-yr average) to Full Value (%)</td>
<td>N/A</td>
<td>1.5%</td>
<td>2.0%</td>
<td>2.5%</td>
<td>2.7%</td>
</tr>
</tbody>
</table>

Source: Moody’s Investors Service

**Detailed Rating Considerations**

**Pennsylvania School Enhancement Program**

The district Series 2014AA, 2015AA, 2015SA and 2016 bonds maintain a Baa1 enhanced rating. However, all of district’s debt is enhanced on a post-default basis by the Pennsylvania School District Enhancement Program. In the case of nonpayment of debt service by a school district, the Secretary of Education of the Commonwealth of Pennsylvania (Aa3 negative) is required to directly remit appropriated state aid to bondholders to cure the deficiency. Payments can be accelerated within the current fiscal year and all forms of state aid are interceptable. In fiscal 2015, state aid net of pension and charter payments covered debt service 2.9 times.

**Economy and Tax Base: Sizeable Tax Base Benefitting from Population Growth**

The district’s $5.1 billion tax base will remain relatively stable, given a history of strong population growth. Located in Franklin County, close to the Maryland border, the district benefits from its location along the Interstate-81 corridor, a major thoroughfare that continues to spur commercial and light industrial development. Five-year average compound growth in assessed valuation totaled 1.1%.
between fiscal 2011 and fiscal 2016, reflecting modest development. Both commercial and residential development are expected to continue as available land in this traditionally agricultural district remains abundant. Officials report no recent changes to the district’s top ten taxpayers, which represent 7.5% of total assessed value in fiscal 2016. The district’s wealth levels are below state and national averages, and full value per capita is $70,789.

Financial Operations and Reserves: Adequate Financial Operations Bolstered by Outside Reserves with Planned Draws
The district’s financial operations will remain sound despite narrowing in recent years given the existence of additional reserves outside of the General Fund. The district decreased its available General Fund reserves to $9.5 million, or 8.2% of revenues in fiscal 2015, down from $20.3 million, or 19.0% of revenues in fiscal 2012. Available General Fund balance includes Capital Reserve Fund reserves, which totaled $2.3 million as of fiscal 2015 year end.

The fiscal 2016 budget includes a $2 million fund balance appropriation and a 3.7% property tax rate increase, the maximum allowable under the Act 1 Index plus exceptions. Based on year-to-date results, management anticipates ending the year with a $1.7 million reserve draw. Continued declines will continue to pressure the district’s financial position and could result in further negative rating action.

The district was not significantly affected by the state budget impasse as the district’s primary revenue sources are local taxes, including real estate taxes and earned income taxes, which cumulatively represented 64.5% of total revenues in fiscal 2015.

Liquidity
The district’s cash reserves remain satisfactory despite recent draws. Cash reserves at the end of fiscal 2015 were $11.6 million, or 10% of revenues, down from a six-year high of $14.1 million, or 13.1% of revenues in fiscal 2012.

Debt and Pensions: Manageable Debt and Pensions
The district’s debt burden of 3.7% of full value will remain manageable despite potential additional planned borrowing and overlapping debt obligations. The district’s long-term capital plan over the next five years contemplates approximately $15 million of additional long-term debt issuance for elementary school expansion and renovations.

Debt Structure
Principal amortization is below average, with 36.2% repaid in 10 years as a result of the district’s recent borrowings to finance long life assets including three elementary schools and a high school.

Debt-Related Derivatives
All debt is fixed rate and the district is not party to any interest rate swap agreements.

Pensions and OPEB
The district contributes to the Pennsylvania State Public School Employees Retirement System, a multi-employer, defined benefit retirement plan administered by the Commonwealth of Pennsylvania (Aa3 negative). The district’s annual required contribution (ARC) for the plan was $10.3 million in fiscal 2015, or 8.6% of operating expenditures. The district’s adjusted net pension liability, under Moody’s methodology for adjusting reported pension data, is $147 million, or a below average 1.2 times operating revenues. Moody’s uses the adjusted net pension liability to improve comparability of reported pension liabilities. The adjustments are not intended to replace the district’s reported liability information, but to improve comparability with other rated entities. We determined the district’s share of liability for the state-run plan in proportion to its contributions to the plan. Total fixed costs for pension, current-year post-employment benefits (OPEB), and debt service summed to $20.6 million, or a manageable 17.3% of operating expenditures in fiscal 2015.

Management and Governance
Despite maintaining satisfactory reserves in the General Fund and other funds, reliance on appropriated reserves to balance the budget have weakened the district’s financial position in recent years. Continued use of reserves to balance the budget would result in negative credit pressure.

Pennsylvania school districts have an institutional framework score of ‘A’ or moderate. Revenues are comprised of local property taxes and state aid, which is determined by the state funding formula. School district property taxes are subject to the Act 1 cap, which makes raising new revenues in a weak economic environment more difficult, although improvements in the Act 1 index, driven by the
CPI, could generate additional operating flexibility. Expenditures are somewhat predictable, and, to an extent, can be cut in response to revenue declines.

**Legal Security**
Bonds are secured by a general obligation limited tax pledge as they are not exempt from Act 1.

**Use of Proceeds**
Proceeds of this issuance will refund portions of the Series 2011 bonds.

**Obligor Profile**
The district is located in northeastern Franklin County and is composed of the Borough of Chambersburg (Aa3) and the Townships of Greene, Hamilton, Letterkenny, and Lurgan. The K-12 district operates thirteen elementary schools, two middle schools, one high school, and a Career Magnet School.

**Methodology**
The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

**Ratings**

<table>
<thead>
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<th>Exhibit 2</th>
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<tr>
<td><strong>Chambersburg Area School District, PA</strong></td>
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<tr>
<td><strong>Issue</strong></td>
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<tr>
<td>General Obligation Bonds, Series A of 2016</td>
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<tr>
<td>Rating Type</td>
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<tr>
<td>Sale Amount</td>
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<tr>
<td>Expected Sale Date</td>
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<td>Rating Description</td>
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*Source: Moody’s Investors Service*
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