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Texas Southmost College District; Junior/Community College

Primary Credit Analyst:
Bianca Gaytan-Burrell, Dallas (1) 214-871-1416; bianca.gaytan-burrell@standardandpoors.com

Secondary Contact:
Shivani Singh, New York (1) 212-438-3120; shivani.singh@standardandpoors.com

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Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services affirmed its 'A' long-term rating and underlying rating (SPUR) on Texas Southmost College District's (TSCD) existing revenue bonds. The outlook is positive.

The rating reflects our view of the district's solid financial resources and positive operations on a full-accrual basis that are consistent with the 'A' rating category. We believe the college district has made substantial progress on mitigating the financial, operational, and enterprise risks identified as a result of the dissolution of the partnership with the University of Texas Brownsville (UTB). The fiscal 2014 audit was the first year that TSCD operated as a separate entity--enrollment, tuition, state appropriations, and the expense base are now entirely representative of just TSCD--and the college district posted a strong surplus. The college district also continues to work through the accreditation process as a stand-alone institution with the Southern Association of Colleges and Schools Commission on Colleges and reports favorable progress. The longer trend of operating performance and enrollment, coupled with the result of the accreditation process, will be key factors in our analysis for an upgrade.

More specifically, the rating reflects our opinion of TSCD's:

- Strong financial resources for the rating category with fiscal 2014 adjusted unrestricted net assets equal to 83.7% of adjusted operating expenses and 314% of total revenue debt;
- History of modest surpluses on a full-accrual basis;
- Diverse revenue stream with tuition, state appropriations, and property taxes;
- Strong growth in its tax base, coupled with flexibility in its voted operating tax rate and a diverse economic base; and
- Nimble management team.

Partly offsetting the aforementioned strengths, in our view, are the district's:

- Lack of a long-term enrollment and operating performance trend as a stand-alone entity, though the first year yielded positive results with an increase in enrollment and a strong operating surplus; and
- Lack of formal policies related to long-term financial planning and debt management although management reports that it is starting a facility master plan.

TSCD was established in 1926; in 1991, the Texas legislature approved the partnership with UTB and the college district, whereby both entities operated with a consolidated administrative and academic structure under the direction of UTB. In 2011, the TSCD and the University of Texas System (of which UTB is a campus) voted to dissolve the existing partnership, and each institution has since cooperated to achieve separate accreditation and a targeted partnership termination by 2015. The transition teams of both institutions achieved operational separation in fall 2013. For more information related to the terms of the property sharing agreement, which remains intact, see our report published June 9, 2014 on RatingsDirect.

Outlook

The positive outlook reflects our anticipation that, during the next two years, enrollment will continue to grow, operations will be positive on a full-accrual basis, and financial resources will remain strong for the rating category. We could raise the rating if we see a longer trend of solid operating surpluses and financial resource ratios, stable-to-growing enrollment, formalization of long-term planning and budgeting, and stand-alone accreditation. We could revise the outlook to stable if enrollment fails to meet projections, resulting in a trend deficit on a full-accrual basis, if additional revenue debt is issued that would weaken financial resources, or in case of a delay in the stand-alone accreditation.

Enterprise Profile

Organization

TSCD is in the Rio Grande Valley in Cameron County, which contains the Los Fresnos Independent School District, Brownsville Independent School District, and Point Isabel Independent School District. Fall 2013 marked the start of TSCD's first year of enrollment as a stand-alone entity, and a total of 2,632 full-time equivalent (FTE) students enrolled. Enrollment increased for fall 2014 with 2,704 FTE students. Although fall 2015 enrollment is not finalized, management reports another increase that is in line with projections. We believe that enrollment could vary somewhat as the college rightsizes, and that it is also contingent on the local economy. However, two positive factors could provide long-term stability, in our view. First, the district is the low-cost provider in the area with a tuition of about $4,000 for the 2014-2015 academic year (based on 30 credit hours), which we believe could make it an attractive option, particularly for an area with low wealth and income indicators. Second, as UTB merges with University of Texas Pan American in 2015 and becomes the University of Texas at the Rio Grande Valley (UTRGV), it may reevaluate its admission requirements. As an open-admission institution, TSCD will potentially be a transfer-student provider to the UTRGV and will also admit those students who are not academically qualified to attend.

Management

TSCD is governed by the elected seven-member board of trustees that are charged with policymaking and supervisory functions. Dr. Tercero was hired by the board of trustees in 2011 and has nimbly led the institution through the transition since then.

The finance department, in our opinion, maintains adequate policies in some, but not all, key areas. Officials monitor the budget monthly and make adjustments as needed. The district has a written, in-depth, and conservative investment policy, and makes monthly updates to the governing body. However, management does not have a formal debt management policy, which we do not view as a best practice. The district lacks a capital improvement plan, but management reports that it intends to complete a formal master plan in 2015. Although management made progress on the short-term objectives related to becoming a stand-alone institution, we believe that long-term budgeting and financial planning are important for TSCD's operational stability.

Financial Profile

Operations

Historically, the district has had positive operations on a full-accrual basis. For fiscal 2014, the college posted an operating surplus on a full-accrual basis of $24.6 million, compared with $5.6 million in fiscal 2013. The surplus was due to some of the settlement payments that UTB made as a result of the dissolution that totaled about $17 million. Management expects a similar surplus for fiscal 2015, and maintenance of the positive operations on a full-accrual basis will be key in our consideration of an upgrade. Fiscal 2014 operating revenue was diverse, in our view, with tuition, fees, and auxiliary revenue accounting for 18.3%, state appropriations 9.4%, property taxes 24.3%, and UTB payment 22.5%.

As state appropriations are based on enrollment, the appropriation for the 2014-2015 biennium decreased relative to the enrollment decline as a stand-alone entity. The college received $6.8 million for each year of the biennium, whereas it received $6.1 million for each year of the 2016-2017 biennium. We anticipate that management will make the budget adjustments it deems necessary as it rightsizes the college.

Local economy

The tax base has increased by a cumulative 8.8% since fiscal 2010 to $11.4 billion in fiscal 2015. We believe the tax base is very diverse, with the leading taxpayers accounting for about 3% of total assessed value (AV). We view county per capita effective buying income (EBI) as low at 54% of the national average and medium household EBI as adequate at 70% of the national level. District market value is adequate, in our opinion, at about $54,948 per capita.

The district's operations and maintenance tax rate has a voter-imposed limit of 35 cents per $100 of AV, and the district's debt service tax rate has a state-imposed limit of 50 cents per $100 of AV. Currently, the operating and debt service tax rates are 10.098 cents and 6.312 cents per $100 of AV, respectively, which allows for additional revenue flexibility if needed.

Financial resources and debt

Unrestricted net assets (UNA) continue to increase partly as a result of the cash payment received from UTB as part of the land agreement. At fiscal year-end Aug. 31, 2014, the district had $40.6 million in UNA, an increase from $15.5 million in 2013 and $12.2 million in 2012. Including debt service reserves, fiscal 2014 UNA improved to $50.5 million, which is equal to 83.7% of adjusted operating expenses, a strong 314.2% of revenue debt, and an adequate 63.0% of total debt, including separately secured GO debt.

The district has $64 million of GO bonds and $16 million of revenue bonds. As part of the dissolution agreement, UTB continues to pay the dedicated fee that secures the series 2006 wellness center bonds. The revenue bonds are secured by 25% of tuition, bookstore revenue, parking revenue, and investment income. Management reports that tuition pledged includes that from TSCD students only, and that it has made arrangements with UTB for the bookstore and parking. Gross debt service coverage by pledged revenue is an adequate 1.6x, which is consistent with expectations. A restricted fund balance for the wellness center revenue bonds provides MADS coverage of more than 3x, providing an additional resource. Revenue debt remains manageable, in our view, with a maximum annual debt service equal to approximately 3% of fiscal 2014 expenses. TSCD does not expect to issue new money revenue or GO debt within the next two years.

Related Criteria And Research

Related Criteria

USPF Criteria: Higher Education, June 19, 2007