

**Philadelphia Authority For Industrial
Development
Green Woods Charter School; Charter
Schools**

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Credit Profile

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Series 2012A&B

Long Term Rating

BB/Stable

Affirmed

Rationale

S&P Global Ratings affirmed its 'BB' rating on Philadelphia Authority for Industrial Development's series 2012A (tax-exempt) and 2012B (taxable) revenue bonds, issued for Green Woods Charter School (Green Woods). The outlook is stable.

We assessed Green Woods' enterprise profile as adequate, characterized by stable and modest enrollment, healthy demand, and solid academics, offsetting a high degree of management transition over the past year and the volatile funding environment affecting all Philadelphia charter schools. We assessed the school's financial profile as vulnerable, characterized by its small operating base, growing unrestricted reserves, high debt burden and slim maximum annual debt service (MADS) coverage, reflecting the school's substantial debt relative to its size.

The 'BB' rating reflects our view of the school's:

- High MADS burden and sufficient MADS coverage based on fiscal 2016 audited results, with some improvement in recent years;
- Volatile per-pupil funding, with an unexpected cut towards the end of fiscal 2016 and a large increase expected for fiscal 2017, though there is the potential that cuts could occur at any time;
- Operating deficit in fiscal 2016, offset by its history of generally stable operating performance and expected improvement in fiscal 2017;
- Number of management and board transitions over the past year, though the team remains proactive in its oversight and we expect stabilization in the near-term;
- Inherent uncertainty associated with charter renewals, given that the final maturity of the bonds exceeds the charter's term.

Partly offsetting the aforementioned credit factors, in our view, are the school's:

- Good liquidity for the rating category, with 67 days' cash on hand as of fiscal year-end 2016;
- Healthy and growing demand, supported by a solid waiting list, good retention, and niche position, with a dynamic and specialized curriculum;
- Above-average aggregate test scores compared with commonwealth and local school district results; and
- History of successful charter renewals, coupled with a working relationship with the charter authorizer and no

notable concerns as the school awaits charter renewal over the next few months.

Green Woods, located in northwest Philadelphia, began operations in the 2002-2003 school year as a kindergarten-through-fifth grade school with an initial enrollment of 123 and currently serves 675 students in kindergarten through eighth grade. The school's curriculum stresses using the environment as an integrated context for learning, with a specific focus on science, ecology, and nature as a foundation for teaching all academic subjects.

Green Woods used the series 2012 revenue bond proceeds to build its current facility, which includes a multi-acre outdoor environmental learning lab, complete with areas designed to align with the environmentally oriented curriculum. It also has three science rooms, a science lab, art rooms, music rooms, and flex space. The bonds are a general obligation of the school, payable from any legally available funds generated or held by Green Woods. Securing the bonds is a first-mortgage lien on the new facility and a debt service reserve fund (DRSF) funded at MADS. As of June 30, 2016, Green Woods had \$18.4 million in long-term debt outstanding.

Outlook

The stable outlook reflects our view that over the one-year outlook period, the school will likely maintain steady enrollment, healthy demand, and despite a volatile state funding environment, return to positive operations with improved MADS coverage and steady liquidity. It also reflects our expectation that the school's charter will be renewed over the next few months, and that it will manage operations to meet its annual debt service payments and sustain MADS coverage above 1x.

Downside scenario

We could consider a negative rating action if the strained funding environment pressure operations, such that MADS coverage remains below 1x, or the school's unrestricted reserves are significantly depleted.

Upside scenario

Credit factors that could lead to a positive rating action include sustained improvement in MADS coverage and a substantially moderated debt burden, with steady enrollment, operations and liquidity, to offset the current funding environment challenges.

Enterprise Profile

Economic fundamentals

Philadelphia County's school-age population is healthy at just under 530,000, but is expected to decline modestly in the near-term, with projections indicating a decline of 0.8% through 2022.

Industry risk

Industry risk addresses the charter school sector's overall cyclical and competitive risk and growth by applying various stress scenarios and evaluating barriers to entry, levels and trends of profitability, substitution risk, and growth trends observed in the industry. We believe the charter school sector represents a moderately high credit risk when compared with other industries and sectors.

Market position

We view Green Woods' enrollment and demand profile as solid and stable, as evidenced by steady headcount, a sound waiting list, and healthy retention. Total headcount of 675 students is steady with prior year and capped based on the school's facility size and charter cap. Green Woods has met or surpassed enrollment targets thus far and we expect enrollment will remain at current levels for the near future. The school's waiting list, which is purged annually, is robust at 958 students or 142% of enrollment, for fall 2016. Management indicates demand has increased as the new building has attracted interested in the community. Retention remains good at 94%, and teacher retention is also very high. Approximately 18% to 19% of all students receive free or reduced-price lunches, and approximately 10% are special education students. Management does not expect these percentages to change dramatically in the near future.

Green Woods has consistently demonstrated academic excellence, with the most recent Pennsylvania System of School Assessment results showing a high percentage of advanced scores in math, reading and science, notwithstanding significant enrollment growth in recent years. Green Woods' test scores far exceed the School District of Philadelphia (SDP), and comparable commonwealth benchmarks. Green Woods' above-average test scores and its growing demand lend credibility to the school's approach, in our view.

The SDP, as the charter authorizer, provides academic and financial oversight. The district granted the initial five-year charter in 2002, and has since renewed it twice, most recently in early May 2012, extending through June 2017. The district also approved a charter modification in 2011, increasing Green Woods' enrollment cap to 675 from 225. The school reports a working relationship with the authorizer, with both parties indicating there are no immediate concerns at this time. We understand the school is generally meeting all current authorizer expectations and as such, expect a successful renewal over the next few months.

Pennsylvania charter schools receive per-pupil revenues from their respective local school districts based on a per-pupil subsidy formula the commonwealth has created for each district. Funding has fluctuated in recent years, with large cuts, followed by increases. In fiscal 2015, the per-pupil funding cut was compounded by a legislative change through which charter schools also lost the state reimbursement for its contribution to the Public School Employees Retirement System, an amount equal to 9% of Green Woods' fiscal 2016 operations. Management offset the fiscal 2015 cuts with accelerated enrollment growth and implemented an alternative 403(b) plan for new hires to reduce future pension exposure. In fiscal 2016, funding was cut unexpectedly toward the end of the year. While funding is expected to remain stable or increase in the near-term, the potential for future cuts remains a possibility. Given the funding environment and its impact on financial performance, the statutory framework assessment reflects our view that this could negatively impact the school's ability to meet its debt service obligations over time. While we believe management plans prudently with conservative budgets including contingencies, we expect funding levels could remain volatile and pose a long-term credit risk.

Management and governance

Over the past year, there has been significant and unexpected transition in Green Woods' leadership, including a new interim chief executive officer (CEO), board turnover, and new contracted financial management firm. We understand these changes were unrelated but have required significant time and effort on the part of the school's current leadership team.

In March 2016, Green Woods' founder and CEO left the school; we understand from the board that this was a mutual decision and in the best interest of the school's long-term success. At that time, the board engaged an interim CEO, Dr. Leroy Nunery, who formerly operated a consulting practice to provide these types of services for charter schools. The board is searching for a permanent CEO, expected to be finalized by fall 2017. Currently, Green Woods is governed by a small three-member volunteer board of trustees, with a fourth member expected to be confirmed this week. Management notes the small board size was a consequence of routine turnover and resignations due to personal reasons, which happened to occur around the same time and while the board was focused on stabilizing school leadership. As a result, the board delayed its focus on recruiting new members, but expects to build back up to closer to six members of the next few months. While we view the current board as limited in its size, oversight continues to be active and we would view the addition of members with diverse backgrounds as planned favorably. Finally, in December 2016, Green Woods transitioned to a new financial management firm, OmniVest Management Services LLC, following a request for proposals and search process. OmniVest provides services supporting budgeting, accounting, cash management, and audit preparation.

At this time, we continue to view management as capable, though the high degree of transition and small current board size are limiting factors. Management indicates discussions are underway to develop a comprehensive long-term school sustainability plan to further support operational stability. At this time, there are no plans for school expansion or replication, but there may be long-term growth plans that develop from the strategic visioning process, according to management. These plans would require approval from the SDP.

Financial Profile

Financial performance

The school's operations have historically been characterized as break-even, and have fluctuated between modest surpluses and deficits in recent years. For fiscal 2016, adjusted for the impact of GASB 68, Green Woods posted a deficit of \$308,000, primarily driven by the sharp funding cut towards the end of the fiscal year. The school posted a 21% EBIDA margin or net revenues available for debt service of \$1.38 million, which contributed to slim MADS coverage of 1x for fiscal 2016. For fiscal 2017, Green Woods is budgeting for a modest surplus, based on flat enrollment and per-pupil funding, which should support improved MADS coverage. We understand interim performance is tracking to budgeted expectations.

In line with our Dec. 15, 2015, publication "Incorporating GASB 68: Evaluating Pension Obligations Under Standard & Poor's Higher Education and Charter School Criteria," we have made certain adjustments to the financial statements of public colleges and universities and certain public charter schools for financial results beginning with the fiscal year end June 30, 2015, to enhance analytical clarity regarding the economic substance of the funding of liabilities, expenses and deferred inflows and outflows of resources associated with pension plan obligations, and a change in accounting principle as detailed in GASB 68, "Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27." We believe these adjustments enhance analytical clarity from a credit perspective and result in more comparable financial metrics as long as states continue to be able and willing to fund these pension liabilities.

Liquidity and financial flexibility

Positive bottom lines have supported a good liquidity position for the school. As of June 30, 2016, unrestricted cash was approximately \$1.2 million, or 67 days' cash on hand, which we view as good for the rating level. While unrestricted reserves have grown, days' cash on hand has moderated, primarily due to the school's growing expense base. Unrestricted reserves to debt for fiscal 2016 was 6.4%, which we view as limited, but not inconsistent with similarly rated peers. We expect continued breakeven to positive operating performance should assist the school in maintaining a steady liquidity position.

Debt burden

As of June 30, 2016, Green Woods had \$18.4 million in long-term debt outstanding, including the \$18 million series 2012 bonds, a \$47,000 capital lease, and a \$300,000 note payable. In May 2015, the school learned that additional soil remediation work would be necessary at the school site, which will cost just over \$500,000. Green Woods secured a loan through the Environmental Protection Agency's (EPA) Brownfields Program with the Philadelphia Authority for Industrial Development. This would provide for a seven-year \$400,000 loan at 1% and a \$100,000 grant, which is expected to cover almost all of the necessary site work. There are no payment provisions that change upon the occurrence of certain events and no restrictive financial or non-financial covenants associated with this loan; as such, we do not view this as contingent debt. MADS of \$1.38 million translates to what we consider a high burden of 20.5% of revenues. Debt to capitalization, at 97%, reflects the school's high leverage position. In addition, Green Woods' debt per student is high relative to comparable peer schools. We understand the school does not have any additional debt plans or significant capital needs. Assuming Green Woods' can maintain stable to improving operations, we expect these debt burden metrics to moderate incrementally over time.

Financial policies

The school meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, while there may be some areas of risk, the organization's overall financial policies are not likely to negatively affect its future ability to pay debt service. Our analysis of financial policies includes a review of the organization's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure and a comparison of these policies with comparable providers.

Legal provisions

A gross revenue pledge and a mortgage on the new facility secure the 2012A and 2012B bonds, along with a DSRF funded at MADS. The school has pledged to comply with certain financial covenants that include maintaining historical debt service coverage at 1.1x or higher for each fiscal year (starting in fiscal 2015), and an unrestricted cash balance of no less than 30 days' cash on hand. Failure to meet these covenants requires engaging a management consultant, but does not constitute a technical default unless coverage falls below 1x, or the days' cash on hand covenant is violated for any two consecutive fiscal years starting in fiscal 2016. The bond documents also provide for a \$300,000 repair and replacement fund effective July 2014, to be funded at \$5,000 per month thereafter. An additional bonds test calls for prior- and current-year coverage of 1.25x pro forma MADS, or two years of projected 1.25x coverage of pro forma MADS. Management is working with bondholders to secure approval for the line of credit and EPA loan described earlier.

Green Woods Charter School, Pa. Financial Statistics

	--Fiscal year ended June 30--				Medians for 'BB' rated charter schools
	2017	2016	2015	2014	2015
Enrollment					
Total headcount	675	677	658	466	882
Total waiting list	958	1,001	951	930	MNR
Waiting list as % of enrollment	141.9	147.9	144.5	199.6	10.9
Financial performance					
Total revenues (\$000s)	N.A.	6,738	6,440	5,247	MNR
Total expenses (\$000s)	N.A.	7,046	6,256	5,135	MNR
EBIDA (\$000s)	N.A.	1,381	1,856	1,202	MNR
EBIDA margin (%)	N.A.	20.50	28.82	22.91	10.10
Excess revenues over expenses (\$000s)	N.A.	(308)	184	112	MNR
Excess income margin (%)	N.A.	(4.57)	2.86	2.13	1.5
Lease adjusted annual debt service coverage (x)	N.A.	1.07	1.41	1.46	1.2
Lease adjusted annual debt service burden (% total revenues)	N.A.	19.2	20.4	15.7	MNR
Lease adjusted annual debt service burden (% total expenses)	N.A.	18.4	21.0	16.0	MNR
MADS (\$000s)	N.A.	1,381	1,325	1,325	1,525
Lease adjusted MADS coverage (x)	N.A.	1.00	1.40	0.91	1.2
Lease adjusted MADS burden (% total revenues)	N.A.	20.5	20.6	25.3	MNR
Lease adjusted MADS burden (% total expenses)	N.A.	19.6	21.2	25.8	14.60
Total revenue per student (\$)	N.A.	9,953	9,787	11,260	MNR
Balance Sheet Metrics					
Days' cash on hand	N.A.	67.1	61.3	74.8	58.00
Total long-term debt (\$000s)	N.A.	18,384	18,369	18,628	MNR
Unrestricted reserves to debt (%)	N.A.	6.4	5.2	5.3	9.8
Unrestricted net assets as % of expenses	N.A.	8.1	7.4	7.7	13.1
General fund balance (\$000s)	N.A.	202	239	301	MNR
Debt to capitalization (%)	N.A.	97.2	97.7	98.0	MNR
Debt per student (\$)	N.A.	26,582	27,480	39,418	13,598

N.A.--not available. N/A--not applicable. MNR--median not reported. MADS--maximum annual debt service.

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