

This Management's Discussion and Analysis ("MD&A") is intended to provide a narrative overview and analysis of the financial activities of the State College Area School District (the "District") for the year ended June 30, 2019. The District's financial performance is discussed and analyzed within the context of the financial statements and the disclosures that follow. This discussion focuses on the District's financial performance as a whole; readers should also review the basic financial statements and the notes thereto to enhance their understanding of the District's financial performance.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements.

Government-Wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business. These statements are prepared using the accrual basis of accounting. The focus of these statements is long-term.

The statement of net deficit presents information on all of the District's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statement of activities presents information showing how the District's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused compensated absences).

The governmental-wide financial statements distinguish functions of the District that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a portion of their costs through user fees and charges (business-type activities). The governmental activities include all of the District's instructional programs and support services except for its food service operation, which is considered a business-type activity.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of fund financial statements is short term. Fund financial statements are prepared using the modified accrual basis of accounting.

Governmental Funds

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the District's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the District's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The District maintains four individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the District's major funds, which are the General Fund, Capital Reserve Fund, and the Capital Projects Fund. The District's non-major fund, the Debt Service Fund, is reported separately.

Proprietary Funds

The District accounts for its food service operation in a proprietary fund, which reports the same functions presented as the business-type activity in the government-wide financial statements. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail.

Notes to Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Government-Wide Financial Analysis
Condensed Statements of Net Deficit
June 30, 2019 and 2018

	Condensed Statements of Net Deficit					
	Governmental Activities		Business-Type Activity		Total	
	2019	2018	2019	2018	2019	2018
Assets and Deferred Outflows of Resources						
Current and other assets	\$ 122,074,838	\$ 172,745,273	\$ 280,644	\$ 255,558	\$ 122,355,482	\$ 173,000,831
Noncurrent assets	271,515,193	209,334,147	161,774	127,301	271,676,967	209,461,448
Deferred outflows of resources	41,344,169	42,824,597	813,486	859,180	42,157,655	43,683,777
Total	<u>\$ 434,934,200</u>	<u>\$ 424,904,017</u>	<u>\$ 1,255,904</u>	<u>\$ 1,242,039</u>	<u>\$ 436,190,104</u>	<u>\$ 426,146,056</u>
Liabilities, Deferred Inflows of Resources and Net Deficit						
Current liabilities	\$ 36,777,747	\$ 36,146,431	\$ 154,058	\$ 148,255	\$ 36,931,805	\$ 36,294,686
Long-term liabilities:						
Due within one year	7,730,000	7,335,000	-	-	7,730,000	7,335,000
Due after one year	457,524,786	465,400,869	4,996,440	5,122,844	462,521,226	470,523,713
Total liabilities	<u>502,032,533</u>	<u>508,882,300</u>	<u>5,150,498</u>	<u>5,271,099</u>	<u>507,183,031</u>	<u>514,153,399</u>
Deferred inflows of resources	3,990,448	2,092,014	93,407	42,986	4,083,855	2,135,000
Net deficit:						
Net investment in capital assets	73,553,369	55,776,274	161,774	127,301	73,715,143	55,903,575
Restricted	-	82,908	-	-	-	82,908
Unrestricted	(144,642,150)	(141,929,479)	(4,149,775)	(4,199,347)	(148,791,925)	(146,128,826)
Total net deficit	<u>(71,088,781)</u>	<u>(86,070,297)</u>	<u>(3,988,001)</u>	<u>(4,072,046)</u>	<u>(75,076,782)</u>	<u>(90,142,343)</u>
Total	<u>\$ 434,934,200</u>	<u>\$ 424,904,017</u>	<u>\$ 1,255,904</u>	<u>\$ 1,242,039</u>	<u>\$ 436,190,104</u>	<u>\$ 426,146,056</u>

Condensed Statements of Activities
For the Year Ended
June 30, 2019 and 2018

	Condensed Statements of Activities					
	Governmental Activities		Business-Type Activity		Total	
	2019	2018	2019	2018	2019	2018
Revenues:						
Program revenues:						
Charges for services	\$ 1,595,642	\$ 1,614,736	\$ 2,708,464	\$ 2,566,886	\$ 4,304,106	\$ 4,181,622
Operating grants and contributions	21,540,675	20,559,988	1,535,168	1,409,506	23,075,843	21,969,494
Capital grants	6,799,671	-	-	-	6,799,671	-
General revenues:						
Taxes levied, net	126,225,922	120,752,937	-	-	126,225,922	120,752,937
Grants, subsidies and contributions not restricted	9,344,307	9,148,206	-	-	9,344,307	9,148,206
Other	3,897,576	2,609,288	-	-	3,897,576	2,609,288
Total revenues	169,403,793	154,685,155	4,243,632	3,976,392	173,647,425	158,661,547
Program Expenses:						
Instruction	91,248,469	89,814,795	-	-	91,248,469	89,814,795
Instructional student support	13,000,519	12,082,049	-	-	13,000,519	12,082,049
Administration and financial support services	16,188,122	15,645,891	-	-	16,188,122	15,645,891
Operation and maintenance of plant services	16,464,476	15,447,993	-	-	16,464,476	15,447,993
Pupil transportation	6,550,189	6,466,839	-	-	6,550,189	6,466,839
Student activities	2,868,956	2,815,891	-	-	2,868,956	2,815,891
Community services	94,904	86,998	-	-	94,904	86,998
Interest on long-term debt	6,501,461	6,982,183	-	-	6,501,461	6,982,183
Unallocated depreciation	373,934	374,410	-	-	373,934	374,410
Loss on disposal of capital assets	1,131,247	3,560,839	-	29,527	1,131,247	3,590,366
Food service	-	-	4,159,587	4,139,415	4,159,587	4,139,415
Total program expenses	154,422,277	153,277,888	4,159,587	4,168,942	158,581,864	157,446,830
Change in net position	14,981,516	1,407,267	84,045	(192,550)	15,065,561	1,214,717
Net deficit, beginning, as previously reported	(86,070,297)	(75,479,221)	(4,072,046)	(3,564,277)	(90,142,343)	(79,043,498)
Effect of adoption of GASB No. 75	-	(11,998,343)	-	(315,219)	-	(12,313,562)
As restated	(86,070,297)	(87,477,564)	(4,072,046)	(3,879,496)	(90,142,343)	(91,357,060)
Net deficit, ending	\$ (71,088,781)	\$ (86,070,297)	\$ (3,988,001)	\$ (4,072,046)	\$ (75,076,782)	\$ (90,142,343)

Total net position of the District increased \$15,065,561 in 2019. Net position of governmental activities increased by \$14,981,516, while net position of the business-type activity increased \$84,045.

The District had \$154,422,277 in expenses related to governmental activities in 2019; only \$29,935,988 of these expenses were offset by program-specific charges for services, grants or contributions. General revenues (primarily taxes and state subsidies) of \$139,467,805 also provided for these programs. The \$14,981,516 increase in governmental activities net position represents the excess of revenues over expenses.

In the District's business-type activity, net position increased by \$84,045 as a result of the net income of the food service operation.

The June 30, 2019, government-wide financial statements reflect the District's estimated share of the PSERS liability and related deferred outflows and inflows of resources, as required under GASB 68. GASB 75 was adopted in 2018, as required, replacing GASB 45 to include the liability and deferred outflows and inflows of resources related to postemployment benefits other than pension (OPEB), primarily health insurance. Below is a schedule showing the impact of GASB 68 and 75 on the unrestricted net position as of June 30, 2018 and 2019.

	<u>Total Net Position</u>	<u>GASB 68 and 75 (Pension and OPEB Impact)</u>	<u>Total Excluding GASB 68 and 75 Impact</u>	<u>Unrestricted Net Position Excluding GASB 68 and 75 Impact</u>
Governmental Activities:				
At June 30, 2018	\$ (86,070,297)	\$ (206,052,621)	\$ 119,982,324	\$ 64,123,142
Change in net position	<u>14,981,516</u>	<u>(8,391,137)</u>	<u>23,372,653</u>	<u>658,313</u>
Ending at June 30, 2019	<u>\$ (71,088,781)</u>	<u>\$ (214,443,758)</u>	<u>\$ 143,354,977</u>	<u>\$ 64,781,455</u>
Business-Type Activities:				
At June 30, 2018	\$ (4,072,046)	\$ (4,262,961)	\$ 190,915	\$ 63,614
Change in net position	<u>84,045</u>	<u>3,064</u>	<u>80,981</u>	<u>46,508</u>
Ending at June 30, 2019	<u>\$ (3,988,001)</u>	<u>\$ (4,259,897)</u>	<u>\$ 271,896</u>	<u>\$ 110,122</u>

As of June 30, 2019, excluding the impact of changes in position recorded based on GASB 68 and 75, \$64,781,455 of unrestricted net position of the \$143,354,977 of total net position was available to meet the District's ongoing obligations to employees and creditors for governmental activities. The remaining net position of \$73,553,369, is invested in capital assets and restricted for capital projects and debt service.

Financial Analysis of the Governmental Funds

General Fund

Revenues

Revenues for the 2018 - 2019 fiscal year were \$167,122,998 compared to \$153,159,772 for the previous fiscal year. The revenues are derived from three main sources, as follows:

	<u>2018 - 2019</u>	<u>2017 - 2018</u>	<u>Change Increase (Decrease)</u>	<u>% Change</u>
Local sources	\$ 130,199,415	\$ 124,215,479	\$ 5,983,936	4.8 %
State sources	35,452,532	27,351,253	8,101,279	30.0 %
Federal sources	<u>1,471,051</u>	<u>1,593,040</u>	<u>(121,989)</u>	<u>(7.7) %</u>
Total	<u>\$ 167,122,998</u>	<u>\$ 153,159,772</u>	<u>\$ 13,963,226</u>	<u>9.1 %</u>

Local revenues are derived primarily from levying taxes such as real estate tax, earned income tax and real estate transfer tax. Local revenues increased \$5,983,936 primarily related to increases in real estate taxes. Real estate taxes, including supplemental tax billings, increased \$4,091,790 with approximately \$2,393,000 related to an increase in the millage rate from 44.1468 mills to 45.206 mills per \$1,000 of assessed value. Rebates totaling \$84,220 offset real estate tax revenue. The District implemented a Supplemental Tax Rebate Program in the 2015-2016 fiscal year, which provides property tax rebates to senior citizens, widows, widowers and disabled persons who meet certain income eligibility guidelines and who are homeowners. Realty transfer tax and earned income tax increased approximately \$604,000 and \$518,000, respectively. Investment earnings increased \$621,570 and tuition increased \$118,000 related to expansion of the District's Community Education Extended Learning Program.

State revenues are derived primarily from state subsidies for basic education, special education, vocational education, and transportation. State revenues also include a 50% reimbursement for social security and retirement costs. State revenues increased \$8,101,279. The District received Alternative and Clean Energy grants from the Pennsylvania Department of Community & Economic Development ("DCED") totaling \$6,799,671 which will fund a portion of three elementary construction projects and the high school construction project. Reimbursement for retirement costs increased approximately \$759,000 due to an increase in salaries and an increase in the employer contribution rate for the state's retirement plan. Basic Education increased \$196,700 related to an increase in state funding, vocational education subsidy increased \$139,550, and social security reimbursement increased \$106,190. Additional state revenue of \$65,000 was awarded from the Pennsylvania Department of Education (PDE) safe schools grant in 2018-19.

Federal revenues include primarily Title I, II, III and IV grants and the School Based ACCESS program.

Expenditures

Expenditures and other financing uses for the 2018 - 2019 fiscal year were \$167,197,657 compared to the 2017 - 2018 fiscal year of \$155,112,430 or a 7.8% increase. The following table shows the expenditures by object category:

	<u>2018 - 2019</u>	<u>2017 - 2018</u>	<u>Change Increase (Decrease)</u>	<u>% Change</u>	
Salaries and benefits	\$ 111,414,106	\$ 106,955,676	\$ 4,458,430	4.2	%
Professional services	3,150,563	3,022,010	128,553	4.3	%
Purchased property services	1,781,117	1,287,090	494,027	38.4	%
Other purchased services	12,479,055	12,671,679	(192,624)	(1.5)	%
Supplies	7,015,063	6,261,850	753,213	12.0	%
Property	1,008,955	1,015,525	(6,570)	(0.6)	%
Other objects	283,622	333,012	(49,390)	(14.8)	%
Other uses of funds	30,065,176	23,565,588	6,499,588	27.6	%
Total	<u>\$ 167,197,657</u>	<u>\$ 155,112,430</u>	<u>\$ 12,085,227</u>	7.8	%

Salaries and benefits increased \$4,458,430. Salary expense increased approximately \$2,900,000, and benefits increased approximately \$1,560,000, primarily related to a \$1,450,000 increase in retirement expense.

The increase in purchased property services is related to the mold repair remediation in multiple school buildings. The increase in supplies and equipment includes the costs associated with change in the elementary school day of approximately \$398,000. Other purchased services decreased related to charter school expense.

Other uses of funds increased \$6,499,588 primarily related to the transfer of DCED grants totaling \$6,799,671 to the capital project fund. The transfer to the capital reserve fund increased approximately \$212,000. Debt services decreased approximately \$426,000 due to the final interest rate swap payment in 2017-18.

The District budgeted approximately \$1,600,000 for the implementation of the change in the school day to fund staffing, curriculum and transportation costs. Actual costs for the implementation of the change in school day were within 2% of budget.

Capital Reserve Fund

The Capital Reserve Fund is used to account for transfers from the General Fund that are to be used to fund future capital projects or debt service. The Capital Reserve fund balance as of June 30, 2019 is \$65,352,256.

Capital Projects Fund

The Capital Projects Fund is used to account for capital projects of the District. The District spent \$65,199,086 for such projects in 2018-2019. The majority of expenditures in 2018-2019 related to the high school and three elementary school building projects. Other projects included renovation and improvements throughout the District. The Capital Projects fund balance is \$4,787,854 at June 30, 2019. Restricted cash of \$19,025,902 at June 30, 2019 represents bond funds available to fund the remaining portion of both the high school and the three elementary building projects.

General Fund Budgetary Highlights

The District prepares a budget each year for its General Fund according to Pennsylvania law. The budget complied with all applicable state laws and financial policies approved by the School Board of Education.

The General Fund's originally-approved budget for 2019 included \$158,110,347 of revenues and \$158,873,467 of expenditures. The budget was amended by \$359,442 for additional grants and related expenditures.

The actual revenues for 2019 were \$8,653,209 greater than the final budget. Local revenues were \$3,777,783 greater than budget primarily due to favorable variances in real estate tax revenue of \$610,100, earned income tax revenue of \$558,600, real estate transfer tax revenue of \$876,200, and interest on investments of \$1,019,700. State revenues were \$4,912,081 greater than budget primarily related to receipt of DCED grants that were anticipated in the 2019-20 fiscal year. Federal revenues were less than budget by \$36,655.

Actual expenditures, excluding transfers to the Capital Reserve fund, were \$1,429,460 greater than the amended budget. Positive budget variances include salary expense and related benefits, which were lower than budget primarily due to the impact of turnover and vacant positions. Healthcare expense was also lower than budget related to variances in membership and coverage levels. Budgetary reserves of approximately \$415,000 were not utilized and the budgeted transfer to Food Service fund was not required based on better than budgeted financial results. Charter school expense is less than amended budget by approximately \$1 million due to a reduction in the number of charter school students. Transfers to the Capital Reserve fund exceeded budget by \$6,535,289 as the result of higher than anticipated revenues, and lower than anticipated expenses.

Capital Assets

The District's investment in capital assets for its governmental and business-type activity as of June 30, 2019 is summarized below (see details in Note 7 to the financial statements).

	<u>Governmental Activities</u>	<u>Business-Type Activity</u>	<u>Total</u>
Land, buildings and improvements	\$ 276,899,568	\$ -	\$ 276,899,568
Equipment and other capital assets	49,171,897	1,120,522	50,292,419
Construction in progress	34,089,486	-	34,089,486
 Total	 360,160,951	 1,120,522	 361,281,473
 Accumulated depreciation	 (88,645,758)	 (958,748)	 (89,604,506)
 Net	 <u>\$ 271,515,193</u>	 <u>\$ 161,774</u>	 <u>\$ 271,676,967</u>

Long-Term Debt

At June 30, 2019, the District had long-term debt of \$199,220,000 (see details in Note 9 to the financial statements) issued, authorized and outstanding, including referendum debt of \$69,585,000 related to the District's High School Project. Debt issued based on a voter referendum is excluded when comparing to the legal limit of debt. Debt that is not related to the referendum of \$129,635,000 is significantly below the legal limit of \$352,295,238.

Factors Expected to Have an Effect on Future Operations

The assessed value used for the 2020 budget preparation is approximately \$2.36 billion, which is up approximately \$28 million, or 1% from 2019. Amounts available for appropriation in the General Fund budget for 2019-2020 are \$163,938,230, an increase of approximately 3.2% over the 2018-2019 original budget of \$158,873,467. The property tax rate will increase 1.95% to 46.088 mills. The District will use this increase in revenues to finance programs currently offered and to fund teaching and psychological staff to meet student educational and support needs and anticipated enrollment increases, expanded online learning programs, support positions related to facilities and other non-recurring capital expenses.

The State College community is dedicated to ensuring that all students acquire the necessary skills and knowledge to enhance and develop their unique capabilities. Education is an investment in the future that requires a partnership between schools and the entire community. The District is committed to using its resources wisely and to delivering quality educational programs.

The District continually strives to enhance the cost-effectiveness of its operations, and of its program delivery, without sacrificing quality. The District's financial planning process includes a multi-year budget that is updated annually and can be found in the budget document. The multi-year budget projects revenues and expenses using historical results and future expectations.

Referendum/Property Tax Relief - Special Session Act 1 of 2006

Act 1 of 2006 limited the ability of School Districts to raise taxes above an inflationary index. It also gave Districts the option of asking voters if they wanted to increase income taxes to decrease property taxes. In the 2007 primary election, 498 school districts were required to propose a referendum question asking voters to authorize an increase in the Earned Income Tax or authorize a Personal Income Tax in order to provide property tax reductions through the homestead and farmstead exclusion. The referendum question proposed for the State College Area School District was to increase the EIT by .7% for a total EIT rate of 1.65%. This referendum was defeated by voters.

School districts are now governed by back-end referendum requirements for increases in property tax rates. School districts are prohibited from increasing their tax rates above the annual inflationary percentage and must place referendum questions before the voters to approve further increases. Exceptions for rate increases above the index without going to referendum exist for special education costs, retirement rate changes, debt issuances, and certain other limited areas. The Act 1 Index for 2018-2019 is 2.4%.

Installment payments for real estate tax bills also went into effect beginning in 2007. All school districts, except Philadelphia and Pittsburgh, were required to offer homestead and farmstead property owners the option to pay their property taxes in installments. School districts are required to notify homestead and farmstead property owners of this option as part of their property tax bills. A taxpayer who elects this option and who is delinquent by more than ten days on two or more installment payments will be ineligible for the installment option in the following year.

Strategic Plan

The PDE requires all school districts to develop a plan to prioritize goals, focusing on improving student learning in accordance with its community's experiences and desires. The 2018-2023 strategic plan was created based on input from a broad cross-section of the State College Area School District community and included formation of a steering committee of 72 students, parents, teachers, administrators, district staff, board members, community/higher education partners and community representatives.

The strategic plan and its annual updates are required to be submitted to PDE each year.

District Growth

DecisionInsite, enrollment impact specialists, were engaged to provide enrollment projections for the District. DecisionInsite used historical enrollment data, recent trends and projected new residential development to forecast student enrollment from 2016 to 2026. Both moderate and conservative projections forecast an increase in enrollment of approximately 1% to 2%, respectively, across the forecasted period. Enrollment projections were updated in 2019 and annually thereafter.

District Wide Facilities Master Plan

The District completed a Facilities Master Plan in the spring of 2009. Since that time, the District has completed the first phase of the Master Plan at the elementary level. The next phase included the construction and renovations at the high school. The total cost, to date, net of DCED grants is estimated at \$139 million, with \$85 million being funded with referendum debt bonds issued in July 2017. Work on the project began in 2015 culminating with occupancy planned for the 2019-20 school year.

The District began a Facilities Master Plan Elementary Update in April of 2016 to take advantage of external funding resources through DCED and reimbursement of debt service expenses through the PDE PlanCon process. Construction began in January 2018 at Radio Park, Corl Street and Spring Creek elementary schools. Phased occupancy at Radio Park and Corl Street schools occurred in the 2018-2019 year with full occupancy for all schools planned for the 2019-20 school year.

Contact the District's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Business Office.