HARRIS COUNTY DEPARTMENT OF EDUCATION, TX
Public K-12 School Districts
TX

Opinion

NEW YORK, June 16, 2014 --Moody's Investors Service has upgraded the Harris County Department of Education's, TX general obligation rating to Aaa from Aa1 affecting $5.75 million in outstanding rated debt. The bonds are direct obligations of the Department, payable from a limited property tax rate.

Concurrently, Moody's has upgraded to Aa2 from Aa3 $15.2 million in outstanding lease revenue bonds issued by the Harris County Department of Education Public Facility Corporation which are payable from rental payments received from the Department. The Aa2 rating reflects the Department's obligation to pay subject to annual appropriation. The rating reflects the nature of the assets financed, which include a parking garage, conference center, and a warehouse facility.

SUMMARY RATING RATIONALE

The Aaa rating reflects the Department's margin under the tax capacity, as well as the large and diverse economy that continues to drive taxable value growth. The rating also reflects strong operating performance and large financial reserves. Also considered is the department's dependence on interlocal agreements with local-area school districts, and the modest debt profile.

The two notch rating distinction between the general obligation limited tax and the lease revenue bonds reflects the appropriation risk, and the non-essentiality of the assets being financed including a parking garage, conference center, and a warehouse facility.

STRENGTHS

Strong economic driving increases in taxable value
Additional unused property taxing margin
Conservative budgeting practices and stable financial performance with large reserves

CHALLENGES

Exposure to volatile oil and gas industry
Dependence on local area school district's for large portion of revenue

DETAILED CREDIT DISCUSSION

HISTORY OF STABLE OPERATIONS AND AMPLE RESERVES; TAX CAPACITY REMAINS

The Department works to serve the needs of learners of all ages through many different educational programs including educational alternatives for students with special educational needs, adult continuing education services, and pre-school programs for economically-disadvantaged children. The Department also contracts with local area school districts for cooperative services ranging from records management to printing. The Department is exposed to some risk through the yearly interlocal agreements issued with local school districts, but the risk is mitigated by the essentiality of services provided and the stable positions of the districts which include Houston ISD (GO rated Aaa/STA), Spring ISD (GO rated Aa3/Stable), and Pasadena ISD (GO rated Aa2/NOO). The Department budgets conservatively and works to achieve self-sustainability in each of the programs offered.
The Department ended fiscal 2013 with an operating surplus of $3.0 million, improving the already sizeable fund balance to $24.8 million or 53.3% of revenues. Department revenues are based primarily on customer fees and charges (48%) through interlocal agreements that the Department manages with the local area school districts, and property tax revenues (40%). The Department maintains significant taxing margin under the $0.10 per $1,000 taxing limitation, levying 65% of the maximum, with plans to slightly reduce the tax rate for fiscal 2015. The tax capacity remains a strength of the credit, serving as a mitigating factor to the dependence on interlocal agreements. For fiscal 2014, the Department is projecting a slight deficit of approximately $230,000 due to one-time capital expenditures and technology purchases. Despite the draw, we expect ample reserves will be maintained over time given limited capital needs, and conservative budgeting

STRONG ECONOMY CONTINUES TO DRIVE TAXABLE VALUE GROWTH

The Department is coterminous with Harris County, which is the fourth largest county by population in the U.S., and encompasses the City of Houston (Aa2/STA), which serves as a global leadership center for oil and gas. The March 2014 Moody's Economy.com report states that Houston's economy is steadily expanding, with employment in a wide range of service industries, particularly IT and professional services. The report states that expansion will remain strong and above-average population growth and expansion in energy, health-related and distribution industries will help propel above-average gains. Population grew 20.3%, to 4.1 million from 2000 to 2010.

Assessed value grew to $289 billion for the Department in fiscal 2014, an increase of 5.0% from fiscal 2013. Assessed values are projected to display strong growth for fiscal 2015, growing an additional 4-5%. We expect taxable values to continue to increase providing a large and stable tax base for the Department. The unemployment rate in the county as of April 2014 was 4.7%, compared to 4.7% for the state and 5.9% nationally over the same time period.

MODEST DEBT PROFILE WITH RAPID AMORTIZATION

The Department's debt profile is very modest, with debt outstanding of $21 million. Debt obligations are approximately 8.1% of all operating expenditures for the Department. The Department develops and maintains a five-year capital improvement plan, and currently plans to use existing fund balance for one-time purchases. Principal retirement is excellent with 100% of principal retired in 10 years.

Budgetary pressure due to the Department's participation in the Texas Teachers Retirement System (TRS) pension plan is expected to remain minimal in the near term. The State of Texas (Aaa/stable) makes most of the employer pension contributions on behalf of the district annually. As a result, the district's net fiscal 2012 share of TRS unfunded pension liabilities, allocated by Moody's, consist of an estimated $11.9 million, given the size of the district's required contribution relative to plan-wide contributions. Moody's adjusted net pension liability (ANPL) for the district, under our methodology for adjusting reported pension data, is $44.1 million. This liability is equal to 0.99x annual operating revenues. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the district's reported contribution information, or the reported liability information of the statewide cost-sharing plans, but to improve comparability with other rated entities. For more information on Moody's insights on employee pensions and the related credit impact on companies, governments, and other entities across the globe, please visit Moody's on Pensions at www.moodys.com/pensions.

WHAT COULD MAKE THE RATING GO UP: N/A

WHAT COULD MAKE THE RATING GO DOWN

Weakened financial position

Weakening of the economic profile

KEY STATISTICS

FY 2014 Full Value: $289.4 Billion
FY 2014 Full Value Per Capita: $68,027
Median Family Income as % of US: 93.9%
FY 2013 Operating Fund Balance as % of Revenues: 53.28%
5-Year Dollar Change in Fund Balance as % of Revenues: 19.34%

FY 2013 Operating Funds Cash Balance as % of Revenues: 39.48%

5-Year Dollar Change in Cash Balance as % of Revenues: 8.83%

Institutional Framework: A

5-Year Average Operating Revenues/Operating Expenditures: 1.04x

Net Direct Debt as % of Full Value: 0.01%

Net Direct Debt / Operating Revenues: 0.45x

3-Year Average ANPL as % of Full Value: 0.01%

3-Year Average ANPL/Operating Revenues: 0.81x

The principal methodology used in rating the general obligation debt was US Local Government General Obligation Debt published in January 2014. The principal methodology used in rating was The Fundamentals of Credit Analysis for Lease-Backed Municipal Obligations published in December 2011. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody’s rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody’s legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

Analysts

Nathan Louder
Lead Analyst
Public Finance Group
Moody’s Investors Service

Adebola Kushimo
Additional Contact
Public Finance Group
Moody’s Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653
Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail clients. It would be dangerous for "retail clients" to make any investment decision based on MOODY'S credit rating. If in doubt you should contact your financial or other professional adviser.