

RatingsDirect®

Brookside Charter School, Missouri; Charter Schools

Primary Credit Analyst:

Brian J Marshall, Farmers Branch (1) 214-871-1414; brian.marshall@spglobal.com

Secondary Contact:

Beatriz Peguero, New York (1) 212-438-2164; beatriz.peguero@spglobal.com

Table Of Contents

Rating Action

Stable One-Year Outlook

Credit Opinion

Enterprise Profile

Financial Profile

Brookside Charter School, Missouri; Charter Schools

Credit Profile		
ICR		
<i>Long Term Rating</i>	BB/Stable	New

Rating Action

S&P Global Ratings assigned its 'BB' issuer credit rating (ICR) to Brookside Charter School, Mo. The outlook is stable.

The charter school has no public debt outstanding. However, management plans to secure a \$5.5 million equitable facilities fund (EFF) loan on June 30, 2020, to refinance the notes outstanding through the New Market Tax Credit (NMTC) Program. After the refinancing, the school's debt outstanding will be \$5.5 million in fiscal 2020.

Because of the COVID-19 outbreak and given broader public safety concerns, the Missouri governor declared a state of emergency the week of March 9, 2020. Management has responded to the crisis by distributing laptops and hotspots to every student, so that online learning can continue through the duration of the crisis. This technology was already paid for, so Brookside will not incur unbudgeted technology costs associated with the outbreak in fiscal 2020. Since 100% of Brookside students qualify for free and subsidized lunches, management is trying to find a safe way to distribute food to students while facilities remain closed. A high level of uncertainty remains regarding the duration and extent of the impact from the COVID-19 outbreak and the related effects on our rated entities' performance, including the ability to continue classes, enrollment, and state funding. We believe the current pandemic and economic uncertainties could hamper Brookside's already slim operating performance should a material amount of unplanned expenses arise, although the impact on state, federal funding, and emergency reimbursements are unknown at present. We will closely monitor developments for potential credit effects on Brookside and take appropriate actions as deemed necessary.

Credit overview

We assess Brookside's enterprise profile as adequate, characterized by stable and growing enrollment, sufficient academics, a tenured management team, and favorable charter standing. These strengths are somewhat offset by the school's moderate enrollment, which we do not expect to materially vary in the foreseeable future and leaves financial operations susceptible to potential enrollment fluctuations. However, we assess Brookside's financial profile as vulnerable, with a history of negative operating margins, weak lease-adjusted maximum annual debt service (MADS) coverage, and a small revenue base, resulting from the school's moderate enrollment. The school's adequate liquidity for the rating level and low debt burden, aided by the imminent refinancing, somewhat offset these weaknesses. We believe that, combined, these credit factors lead to a stand-alone credit profile of 'bb' and a rating of 'BB'.

The 'BB' rating reflects our view of Brookside's:

- Moderate enrollment size and limited waitlist, which makes financial operations susceptible to potential enrollment

fluctuations;

- Recurring operating deficits and weak lease-adjusted MADS coverage, although we expect pro forma MADS coverage and fiscal 2020 margins to improve; and
- The inherent uncertainty associated with charter renewals, given that the final maturity of the school's debt exceeds the current charter's term, requiring multiple charter renewals.

Partially offsetting the above weaknesses, in our opinion, are the school's:

- Long 18-year operating history and a series of charter renewals, including a five-year term awarded by Brookside's current authorizer, the Missouri Charter Public School Commission;
- Adequate academics that consistently outperform the local unaccredited Kansas City Public School District (KCPS), coupled with attractive extracurricular activities;
- Low pro forma debt burden; and
- Ample liquidity compared with that of similarly rated peers, although the school could face pressures to weighted-average liquidity in fiscal 2021, attributable in part to deferred maintenance.

The stable outlook reflects our expectations that over the one-year outlook period, Brookside will continue to expand its enrollment, yield slim but improving margins, and produce adequate lease-adjusted MADS coverage near fiscal 2019 levels.

Brookside Charter School is a single-site public charter school located in southeast Kansas City, Missouri. The school currently serves 741 students from kindergarten to grade 8 (PK-8), growing from just 85 students at its opening in fall 2002. The school's enrollment growth can be attributed to improving academics that outpace the unaccredited KCPS in almost every grade. Brookside also offers many extracurricular activities not afforded to students of the school district.

Management refinanced three facility loans in 2012 through the new market tax credit program. Notes A and B of the notes payable will be refinanced by EFF on June 30, 2020. Note C will be forgiven, as will the school's sinking fund, which is common for NMTC refinancing. The new EFF loan will result in at least \$200,000 of interest-rate savings through the life of the loan. Management aims to use the loan savings to stabilize historically volatile operations.

Environmental, social, and governance factors

We analyzed Brookside's environmental, social, and governance risks relative to its market position, management and governance, and financial performance, and determined that all are in line with our view of the sector standard.

Stable One-Year Outlook

Downside scenario

We could consider a negative rating action if the school's coverage and margins were to weaken to historical levels despite the savings associated with Brookside's new loan or if liquidity significantly drops below the rating level.

Although we think that Brookside has taken proactive steps to address COVID-19 and that it understands the virus to

be a global risk, we could consider a negative rating action during the outlook period should unforeseen pressures related to the pandemic materially affect the school's demand, finances, or trajectory

Upside scenario

We could consider a positive rating action, although unlikely over the outlook period, as a result of the school's uneven operating history, if Brookfield's enrollment continues to grow in line with management's expectations while it increases coverage and operating margins to levels that are in line with those of higher-rated peers.

Credit Opinion

Enterprise Profile

Economic fundamentals

Brookside is located in Jackson County, Mo. The county's minor population is moderate, at 228,000 students. However, the county has consistently experienced a negative growth rate over the past three years. The minor population growth rate is expected to continue to decline at a rate of 1% over the next five years.

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

Brookside's enrollment has been historically moderate, which poses an ongoing risk to the credit's stability. In fall 2019, enrollment rose to 741 students from 545 students in fall 2016. Although the school's three-year growth rate was very strong for fall 2019 at 10.8%, we expect Brookside's growth to moderate as the school nears its facility capacity of 810 students. Management plans to reach this facility capacity by fall 2024. Since management does not foresee any expansion or replication plans in the near future, the school's enrollment level is likely to remain vulnerable.

We deem the school's waitlist as highly vulnerable, averaging 22.5% of enrollment over the past three years. This is a credit negative, in our opinion, as a strong waitlist could offset some pressures stemming from the school's small enrollment size. Although on paper the school's waitlist improved in fall 2019 to 218 students, this figure is inflated because the majority of students on the waitlist are slated for kindergarten, with few students vying for spots in the other grades. Management does not have plans to increase the waitlist at present.

Brookside has historically experienced volatile student retention rates, which constrain our view of the demand profile. Student retention ranged from 68%-75% over the past four years. Management attributes student attrition to families moving away from the area due, in part, to the unaccredited local high schools. Management's goal is to improve retention rates to 82% and considers this is an achievable goal given their projected favorable market share bolstered by failing KCPS high schools and despite concerns about affordable housing in the area, and the transient demographic. We will continue to monitor retention trends and view sustained improved retention rates as a healthy

demand credit factor.

Offsetting the school's weak demand and competitions metrics are its improving academic outcomes, particularly compared with the local district. Brookside students have outperformed KCPS over the past three years, reducing the number of grades each year that do not measure up to district averages. Brookside fails to reach or pass state averages. However, this is expected, because the demographic Brookside serves does not mirror that of the state. Brookside operates in and draws students from the lowest-earning zip code in Kansas City, with 100% of students at Brookside qualifying for free and subsidized lunches. Moreover, the school offers unique extracurricular activities, such as Girls Who Code, Alpha Omega, Gamma Girls, and International Language Club. It also provides opportunities to disadvantaged youth in Kansas City who otherwise would not have access to KCPS schools.

Brookside is authorized or sponsored by the Missouri Charter Public School Commission, a body devoted solely to authorizing charter schools in the state. The commission has sponsored the school since 2018, when its previous sponsor, the University of Missouri Kansas City (UMKC), ceased sponsoring charter schools. UMKC had authorized Brookside since its transition to a charter school in 2002. It awarded the school 10-year terms, with no gaps in the charter renewal. Brookside's current charter term under the commission is for five years, expiring in 2022, the longest charter term awarded by the commission. The authorizer reports a positive relationship with the school and, in our view, the charter is currently in good standing.

The statutory framework assessment reflects our opinion that, while there might be some areas of risk, the framework is not likely to impair Brookside's future ability to pay debt service. In Missouri, the majority of public school operating funding comes from the state. Therefore, charter schools are almost entirely dependent on the state for operating revenue, which is subject to annual appropriation by the state legislature. We expect modest annual increases in state funding, about 2%, in the near term.

Management and governance

Brookside's senior management team remains stable. The current superintendent has been with the school for 10 years, with a previous career in teaching and directing in surrounding districts. The two principals are highly seasoned as well, with master's degrees in instruction and educational administration. The current management team has a history of increasing the school's enrollment, introducing co-teaching, and improving Brookside's academic performance. Although management lacks a background in finance and operations, it has prudently sought two partnerships to supplement its experience, which we view favorably. Two years ago, the school began a partnership with EdOps, a firm that helps schools better understand their financial position and fine-tune reporting. The organization has helped counsel management on how to control expenses, comparing these with other charter schools in Missouri and across the country. Management's contract with EdOps is currently five years, though management has plans to renew this relationship. The school also partners with Innovare Social Innovation Partners to help provide data-driven results to education. Brookside's SchoolSmart Kansas City grant is paying for this contract for three years.

The school is governed by a seven-member board at present, two more members than the minimum number allowed in Brookside's bylaws. The board represents a healthy mix of backgrounds: business and technology leaders, community leaders, educators, and one parent. Management notes that it is continually seeking different skill sets for the board, but has no plans to add members. Currently, the board is working with SchoolSmart, a local nonprofit that

invests in Kansas City public schools, to develop a database and dashboard that could serve as a source for potential new members in the future. Board members meet monthly and serve two-year terms. Overall, we view both management and the board as sufficient and expect no significant changes in the next few years.

Financial Profile

We analyze the materiality, strategy, and funding of pension and other postemployment benefits (OPEB) plans separately from our analysis of a school's long-term debt ratios or operating margin. Consequently, we might make certain adjustments to the calculations of debt ratios or operating margins for schools with substantial multiple-employer, cost-sharing, defined-benefit pension plans or OPEB plans to separate out the net pension liability or noncash expense accrual. In our view, these adjustments enhance analytical clarity from a credit perspective and result in more comparable debt and operating metrics across accounting methods.

Financial performance

Brookside's financial operations have historically been extremely vulnerable, with repeated negative operations. Over the past few fiscal years, the school's excess income margins have averaged negative 6.31%, with a startling excess income margin of negative 14.31% in fiscal 2017. The school's deficits are in part explained by vulnerable levels of revenue, caused by overall modest enrollment figures. We do not expect revenues to improve considerably, given management's current facility cap of 810 students.

Negative operations have also been caused by uncontrolled expenses, particularly the interest and sinking fund costs associated with the school's NMTC. This has resulted in extremely weak pro forma lease-adjusted MADS coverage at negative 0.44x for fiscal 2017 and 0.90x for fiscal 2018. Pro forma lease-adjusted MADS improved in fiscal 2019 to 2.80x coverage; however, this recent improvement is in part tied to a grant award from SchoolSmart that was first recognized in fiscal 2019. Without this grant award, lease-adjusted MADS coverage for fiscal 2019 is similar to fiscal 2018, at 0.94x coverage. The SchoolSmart grant will expire in three years, potentially pressuring funds available for debt service in fiscal 2022. Although management aims to increase enrollment, and the school will save more than \$200,000 a year in interest with the more favorable refunding loan, we need to see a trend contrary to the school's operating history before assessing operations any higher. Management plans to achieve a \$20,000 surplus in fiscal 2020, which we would view favorably but would not materially change the school's financial performance ratios.

Liquidity and financial flexibility

Brookside's balance sheet remains adequate for the rating level. The school's days' cash on hand has been increasing steadily over the past three fiscal years, growing to 105 days' cash in fiscal 2019 from about 79 days' cash in fiscal 2017. The academy has no near-term expansion or replication plans; however, the school could draw on reserves for capital expenditure projects in the near term, since it is no longer spending loan proceeds on its HVAC replacement. Management will also use reserves of about \$300,000 to pay its last sinking fund payment in fiscal 2020. Management's internal benchmark is to keep days' cash above 60 days, although it expects reserves will drop to 46 days' cash in fiscal 2020. Nevertheless, given a one-year horizon for noninvestment-grade credits, we expect days' cash on hand to remain adequate in the outlook period. We will continue to monitor any plans to draw down cash in fiscal 2021.

Unrestricted reserves-to-pro forma debt was 48.9% in fiscal 2019, which we view as more than sufficient for the 'BB' rating level. As of June 30, 2019, Brookside had approximately \$2.5 million in unrestricted cash reserves, which is more than in previous years and in line with similarly rated peers.

Debt burden

As of June 30, 2019, Brookside had \$10.23 million in debt, which consisted of three notes payable through the NMTC program for its existing property. With the EFF refinancing loan dated June 30, 2020, the school's debt outstanding is expected to drop to \$5.5 million in fiscal 2020. The EFF loan will total \$5.5 million, refinancing two of the three outstanding notes payable. Both the third note payable and the NMTC loan's accumulated sinking fund will be forgiven, totaling approximately \$4.23 million, as is common with NMTC deals. After the school's final sinking fund payment of about \$300,000 in fiscal 2020, Brookside's debt outstanding will consist solely of the 2020 \$5.5 million loan.

The school's pro forma lease-adjusted MADS burden is low for fiscal 2019, at 3.2%. The lease-adjusted MADS burden improved from an adequate 5.1% with the school's new loan savings. We expect this ratio will remain strong.

Unlike most charter schools, the organization's pro forma debt-to-capitalization ratio shows less leverage on its balance sheet. For fiscal 2019, the ratio was 55.0%, which we view as adequate. The school has no additional contingent liabilities or off-balance-sheet debt, and we understand the school has no additional debt plans. We expect these ratios to improve gradually over time.

Brookside's EFF loan covenants include debt service coverage and days' cash on hand requirements. Brookside must maintain at least 1.10x coverage for each fiscal year, commencing with fiscal 2021, the first fiscal year after loan closing. A failure to reach 1.10x coverage would require the school to contact an independent management consultant to improve financial operations. Any coverage below 1.00x coverage is considered an event of default. Given Brookside's negative and volatile operating history, we will continue to monitor the school's financial outcomes year-over-year to ensure it is compliant with these coverage covenants. Brookside must also maintain days' cash on hand at or above 45 days' cash in fiscal 2021, 50 days' cash in fiscal 2022, and 60 days' cash for each year thereafter.

Financial policies

Brookside meets standard annual disclosure requirements. The financial policies assessment reflects our opinion that, while there might 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 Brookside's financial reporting and disclosure, investment allocation and liquidity, debt profile, contingent liabilities, and legal structure, and a comparison of these policies with those of similar institutions.

Brookside Charter School--Enterprise And Financial Statistics

	--Fiscal year ended June 30--				--Medians for 'BB' rated charter schools--
	2020	2019	2018	2017	2018
Enrollment					
Total headcount	741	683	630	545	956
Total waiting list	218	122	95	N.A.	MNR
Waiting list as % of enrollment	29.4	17.9	15.1	N.A.	22.6

Brookside Charter School--Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--				--Medians for 'BB' rated charter schools--
	2020	2019	2018	2017	2018
Financial performance					
Accounting standard	N.A.	FASB	FASB	FASB	N.A.
Total revenues (\$000s)	N.A.	9,317	7,844	6,974	9,039
Total expenses (\$000s)	N.A.	9,413	8,514	7,972	MNR
EBIDA (\$000s)	N.A.	782	213	(131)	MNR
EBIDA margin (%)	N.A.	8.4	2.7	(1.9)	14.3
Excess revenues over expenses (\$000s)	N.A.	(96)	(670)	(998)	MNR
Excess income margin (%)	N.A.	(1)	(8.5)	(14.3)	2.3
Operating lease expense	N.A.	47	54	N.A.	MNR
Pension/OPEB adjustments (\$)	N.A.	N.A.	N.A.	N.A.	MNR
Lease-adjusted annual debt service (\$)	N.A.	479	501	436	MNR
Lease-adjusted annual debt service coverage (x)	N.A.	1.73	0.53	(0.30)	MNR
Lease-adjusted annual debt service burden (% total revenues)	N.A.	5.1	6.4	6.3	MNR
MADS (\$000s) (change to lease-adjusted MADS)	N.A.	N.A.	N.A.	N.A.	1,324
Lease-adjusted MADS coverage (x)	N.A.	N.A.	N.A.	N.A.	1.20
Lease-adjusted MADS burden (% total revenues)	N.A.	N.A.	N.A.	N.A.	13.6
Pro forma MADS (\$000s)	N.A.	296	296	296	MNR
Pro forma lease-adjusted MADS coverage (x)	N.A.	2.80	0.90	(0.44)	MNR
Pro forma lease-adjusted MADS burden (% total revenues)	N.A.	3.2	3.8	4.2	MNR
Total revenue per student (\$)	N.A.	13,641.3	12,450.8	12,796.3	MNR
Balance-sheet metrics					
Unrestricted reserves (\$)	N.A.	2,561	2,028	1,618	MNR
Days' cash on hand	N.A.	104.92	92.41	78.89	72.00
Total long-term debt (\$000s)	N.A.	10,230	10,230	10,230	MNR
Unrestricted reserves to debt (%)	N.A.	25.0	19.7	15.6	11.9
Unrestricted net assets as % of expenses	N.A.	50.6	57.3	70.3	17.2
Debt to capitalization (%)	N.A.	69.4	69.2	66.3	91
Debt per student (\$)	N.A.	14,991	16,344	19,018	16,811
Pro forma metrics					
Pro forma unrestricted reserves (\$000s)	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma days' cash on hand	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma long-term debt (\$000s)	N.A.	5,500	5,500	5,500	MNR
Pro forma unrestricted reserves to debt (%)	N.A.	N.A.	N.A.	N.A.	MNR
Pro forma debt to capitalization (%)	N.A.	55	54	51	MNR

Brookside Charter School--Enterprise And Financial Statistics (cont.)

	--Fiscal year ended June 30--				--Medians for 'BB' rated charter schools--
	2020	2019	2018	2017	2018
Pro forma debt per student (\$)	N.A.	8,053	8,730	10,092	MNR

N.A.--Not available. MNR--Median not reported. MADS--Maximum annual debt service. Operating lease expense--Annual amount paid in facilities/capital lease payments; excludes equipment/nonfacility lease payments and excludes payments related to principal and interest on bonds. Net revenue available for debt service = EBIDA + operating lease expense. Lease-adjusted MADS coverage = (net revenue available for debt service + operating lease expense) / (lease-adjusted MADS). Total expenses include pension and OPEB adjustments. Pension and OPEB adjustments = reconciling adjustments made to financial information to account for differences in GASB 68 and GASB 75.

Copyright © 2020 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.