S&P Global
Ratings

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Summary:
Bullard, Texas; General Obligation

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Summary:

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Credit Profile		
US$1.8 mil comb tax & rev certs of oblig ser 2021 dtd 07/01/2021 due 08/15/2048		
Long Term Rating	A/Stable	New

Rating Action

S&P Global Ratings assigned its 'A' long-term rating to the City of Bullard, Texas' approximately $1.8 million series 2021 combination tax and revenue certificates of obligation. The outlook is stable.

The certificates are secured by revenue from an annual ad valorem tax on all taxable property in the city and by a surplus revenue pledge of the city's waterworks and sewer system after all other expenses are paid. We rate the certificates based on the city's general obligation (GO) pledge as we don't have sufficient information to rate the revenue pledge.

The maximum allowable rate for general law cities in Texas is $1.50 per $100 of assessed value (AV) for all purposes. In fiscal 2021, the city levied 59.56 cents per $100 of AV, with 30.15 cents dedicated to debt service.

We do not differentiate between the city's limited-tax GO debt and its general creditworthiness given that the ad valorem tax is not derived from a measurably narrower tax base and that there are no limitations on the fungibility of resources.

Proceeds from the certificates will fund the planning and design of a wastewater treatment plant.

Credit overview

Aided by its proximity to Tyler and demand for housing in the area, Bullard's economy grew through the COVID-19 pandemic. Despite an economic slowdown during the initial shutdowns last year, the tax base and major revenue sources saw healthy increases in fiscal 2020 and the growth is gaining momentum, with several hundred homes slated to be added to the tax rolls in the next three years.

Given ongoing development, which is not expected to abate in the near term, Bullard's main challenges include providing sufficient infrastructure and meeting an increasing demand for services, while operating within revenue constraints of Senate Bill 2, which limits annual ad valorem revenue growth. We believe there could be some operating challenges related to the growth as the city lacks basic financial-management practices related to long-term planning and operating reserves in particular, and its fixed charges are very high, limiting expenditure flexibility. We consider Bullard's debt burden a weakness that will continue to be a constraining factor, especially with the city planning on issuing about $18 million in new debt in the next two years, which will increase its net direct-debt burden to nearly 700% of total governmental funds revenue, significantly above that of peers.

The rating reflects our opinion of the city's:

- Adequate economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Adequate management, with standard financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could weaken in the near term relative to fiscal 2020, which closed with a slight operating surplus in the general fund and an operating surplus at the total governmental fund level in fiscal 2020;
- Strong budgetary flexibility, with an available fund balance in fiscal 2020 of 8.5% of operating expenditures but that is low on a nominal basis at $197,000;
- Very strong liquidity, with total government available cash at 55.6% of total governmental fund expenditures and 1.9x governmental debt service;
- Weak debt and contingent liability profile, with debt service carrying charges at 29.3% of expenditures and net direct debt that is 198.5% of total governmental fund revenue, but rapid amortization, with 78.2% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Environmental, social, and governance (ESG) factors

We analyzed the city's ESG risks relative to its economy, management, financial measures, and debt and liability profile, and determined that all are in line with our view of the sector standard. We note that the growth the city is experiencing will continually increase demand for services and infrastructure, and the lack of financial policies in many areas could pose a risk if the growth is not managed to control the increasing budget and especially the rising debt burden and fixed costs.

Stable Outlook

Downside scenario

Should performance weaken, whether as a result of one-time items or recurring revenue and expenditure imbalance, resulting in deterioration of the city's flexibility or liquidity, we could lower the rating.

Upside scenario

We could raise the rating if the city increases and maintains available fund balance well above levels that we consider nominally low, coupled with the adoption of formalized financial management policies and significant moderation of its debt profile.

Credit Opinion

Adequate economy

We consider Bullard's economy adequate. The city, with an estimated population of 4,282, is in Cherokee and Smith counties in the Tyler MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 73.8% of the national level and per capita market value of $88,040. Overall, the city's market value grew by 18.7% over the past year to $377.0 million in 2021. The weight-averaged unemployment rate of the counties was 6.8% in 2020.

Bullard is a small community about 15 miles south of Tyler. The city is mostly residential and has experienced significant population growth over the past two decades, which management attributes to a desirable local school district as well as its distance to Tyler and Jacksonville, which provide for an easy work commute.

Officials report ongoing residential development, with several new subdivisions under construction that will add more than 300 homes in the next three years, as well as new phases in existing subdivisions.

Commercial developments include a new nursing home that opened last year, a fast-food restaurant, and a new car wash currently under construction.

Given ongoing development and the availability of land, we expect the tax base will grow. Assessed value growth averaged about 8%-10% annually and management does not expect it to abate. Preliminary tax roll information from Smith County, where the majority of Bullard is located, indicates 8.4% growth, consistent with management expectations.

The debt service tax rate analysis conducted in conjunction with the current debt issuance assumed a 10% AV growth in fiscal 2022 and a 5% growth annually for the following consecutive seven years. Given the recent trends, these assumptions may be prudent though we note some risk exists if they do not materialize as the city needs to levy higher tax rates than projected.

Adequate management

We view the city's management as adequate, with standard financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some but not all key areas.

Highlights of management's practices include:

- Several years of historical trend analysis when preparing the budget;
- Budget amendments done at the end of each year for expenditures only, if needed; and
- Budget-to-actual reports provided to the council monthly.

The city follows state investment guidelines. The council does not receive investment reports since the only investments are debt proceeds invested in state pools. Bullard does not maintain long-term financial or capital plans and the city does not have a reserve or debt management policy.

Adequate budgetary performance

Bullard's budgetary performance is adequate, in our opinion. The city had slight surplus operating results in the general fund of 0.6% of expenditures, and surplus results across all governmental funds 3.8% in fiscal 2020. General fund operating results have been stable, at 2.1% in 2019 and 1.9% in 2018.

Overall, the city's financial performance remained stable over the past three years after adjusting for recurring transfers and capital expenditures funded with bond and grant proceeds. The city's primary general fund revenues in fiscal 2020 were property taxes (40%), sales taxes (18%), and franchise fees (9%). Recurring transfers are made annually into the general fund from the city's utility fund and included in our ratios. The transfer was $383,000 in fiscal 2020, or 16% of adjusted revenues.

Officials attribute the operating results to conservative budget assumptions and revenues exceeding expectations. Given the city's growth, property, and sales-tax revenues continue to grow. In fiscal 2020, property and sales-tax revenues increased approximately 9% and 23%, respectively, from 2019. The city did not receive any CARES Act funds in fiscal 2020.

For fiscal 2021, the city expects a surplus of approximately $200,000 due to positive revenue and expenditure trends. The city is slated to receive about $812,000 in American Rescue Plan Act funds, but they have not finalized plans on how those funds will be spent.

For future budgets, management projects continued budget growth given the city's growth but it expects Bullard to produce at least balanced operations well within the constraints of ad valorem tax limitations and officials would like to increase general fund reserves to eventually be in line with those of peers in the state.

We note that available fund balance was negative as recently as fiscal 2016 after Bullard posted deficits in 2013 and 2014 due to expenses for street improvements. Given the small budget size, even small performance fluctuations on a nominal basis, such as unplanned capital expenditures, can lead to large percentage fluctuations. This potential volatility is incorporated into our assessment of performance.

Strong budgetary flexibility

Bullard's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2020 of 8.5% of operating expenditures. The city's reserves are low on a nominal basis at $197,000, which we view as vulnerably low and a negative credit factor.

With the projected general fund surplus, reserves could see a significant boost at fiscal year-end 2021, but we believe they will remain below $500,000, or what we consider nominally low levels.

The narrow available reserve position in the general fund represents a significant vulnerability as it leaves very little flexibility to manage any fiscal challenges. Future credit reviews will focus on the city's ability to build up reserves. Any declines in fund balance could result in a negative rating pressure.

Very strong liquidity

In our opinion, Bullard's liquidity is very strong, with total government available cash at 55.6% of total governmental fund expenditures and 1.9x governmental debt service in 2020. In our view, the city has satisfactory access to external liquidity if necessary.

We anticipate that liquidity will remain very strong over the outlook horizon, but we note that the general fund only had about $140,000 in cash at fiscal year-end 2020 and most cash was held in the utility fund ($1 million) and the debt service fund (about $550,000).

The city's only investments are bond proceeds held in highly rated investments pools, which we do not consider to be aggressive.

The city has several private placements outstanding with the total principal of about $4.5 million, which accounts for 71% of total direct debt. The privately placed bonds, notes, and certificates of obligation do not pose a contingent liquidity risk, in our view, as legal provisions do not include unusual default or acceleration clauses.

Weak debt and contingent liability profile

In our view, Bullard's debt and contingent liability profile is weak. Total governmental fund debt service is 29.3% of total governmental fund expenditures, and net direct debt is 198.5% of total governmental fund revenue. Approximately 78.2% of the direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor.

City officials anticipate issuing about $18.6 million in additional new debt within two years for the construction of the wastewater treatment plant.

The city indicates that eventually, once the customer base grows sufficiently to generate higher utility revenues, both the 2021 certificates and the planned debt could be supported by the utility fund. According to our criteria, once the utility fund pays the debt, we will give self-support credit but only once there is a three-year track record of the utility fund making debt service payments.

Until the debt is self-supported, the current and the planned issuances will result in a significant increase in net direct debt as a percent of total governmental funds revenue to levels well above those of peers, which limits upward rating potential. An additional weakness are the city's high fixed costs compared with those of peers. Debt service payments will increase with this issuance and the additional debt planned, although the increase in fixed costs might not be material as a percent of expenditures given the city's growing budget.

Pension and other postemployment benefits liabilities

Bullard's pension contributions totaled 4.0% of total governmental fund expenditures in 2020. The city made its full required pension contribution in 2020.

We do not view pension and other postemployment benefits (OPEB) liabilities as an immediate credit risk. While current contributions are manageable, we anticipate these costs will increase given amortization and payroll growth assumptions. However, we believe Bullard has sufficient budgetary flexibility and liquidity to address these costs.

The city participates in the following plans:

- Texas Municipal Retirement System (TMRS), a nontraditional, joint contributory, hybrid defined benefit pension plan administered by the state. An actuary determines the contribution rate annually. Bullard's net pension liability was $593,000 as of Dec. 31, 2019, and the plan's funded ratio was 77.30%, assuming a 6.75% discount rate. Fiscal 2020 actual contributions fell short of minimum funding progress and our static funding metric, which indicates lack of funding progress. In addition, we expect progress toward full funding will be slower given the plan's amortization basis of level percent using a payroll growth assumption of 2.75%.
- TMRS defined benefit OPEB plan, a voluntary program that provides group-term life insurance coverage. The total liability is $39,765 and is funded on a pay-as-you-go basis.

Strong institutional framework

The institutional framework score for Texas municipalities is strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2020 Update Of Institutional Framework For U.S. Local Governments