S&P Global
Ratings

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Summary:

Tarrant County College District, Texas; General Obligation

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US$352.615 mil GO bnds ser 2022 dtd 07/01/2022 due 08/15/2042		
Long Term Rating	AAA/Stable	New
Tarrant Cnty Coll Dist GO bnds ser 2020 due 07/01/2040		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to the Tarrant County College District (TCCD), Texas' approximately $352 million series 2022 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AAA' rating on the district's GO bonds outstanding. The outlook is stable. Following this issuance, total GO-supported long-term debt will be approximately $608 million.

The bonds are payable from an ad valorem tax levied on all taxable property within the system's taxing boundaries, within the limits prescribed by law. The system's tax rate is capped at 70 cents per $100 of assessed value (AV), with no more than 50 cents allowed for debt service and the remaining 20 cents for operations. We view the limited-tax GO debt pledge to be on par with the district's general creditworthiness because there is no significant limitation on resource fungibility available to the district. The district's total tax rate is currently only 13 cents, with 12 cents allocated for maintenance and operations and 1 cent for debt service. Officials will use the bond proceeds to make capital improvements to existing campuses across the district.

Tarrant County College System's GO bonds are eligible to be rated above the sovereign because we believe the system can maintain better credit characteristics than the U.S. in a stress scenario. Under our "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" criteria, published Nov. 19, 2013, U.S. local governments are considered to have moderate sensitivity to country risk. The system's GO pledge is the primary source of security on the debt; this severely limits the possibility of negative sovereign intervention in the payment of the debt or in the operations of the system. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management, and no history of government intervention.

Credit overview

With a population of more than 2 million, the college serves a diverse student base with expansive course offerings. While the college has seen double-digit declines in student enrollment over the past two years, largely attributable to the COVID-19 pandemic, officials report that early indications are that fall enrollment for 2022 could recover to pre-pandemic levels. Given the limited dependence on tuition revenues, the college maintained positive operating

results, sustaining an exceptionally strong financial profile despite the pandemic's influence on enrollment. This has partially been attributable to growing tax revenues as well as sizable federal stimulus funds. While the district's debt burden is somewhat elevated, and poised to increase further with additional issuance planned under the existing 2019 bond authorization, we believe that debt costs will remain manageable. Given this, we expect overall rating stability throughout our outlook horizon.

The 'AAA' rating further reflects the district's:

- Participation in the Dallas-Fort Worth-Arlington metropolitan statistical area's (MSA) deep and diverse economy;
- Good revenue diversity, with most revenues tied to property taxes, tuition and fees, and state appropriations;
- Solid financial flexibility from substantial operating-tax-rate capacity, competitive tuition rates, and a healthy, growing tax base; and
- Good management, with likely sustainable financial practices and practices under our Financial Management Assessment (FMA) methodology.

We believe these strengths are partially offset by the district's moderate-to-high overall debt burden and slower-than-average amortization.

Environmental, social, and governance

We view the risks posed by COVID-19 to public health and safety as a social risk under our environmental, social, and governance factors. Like peers, the district faces elevated social risks because of the uncertainty of the duration of the pandemic and its potential effects on instructional modes and enrollment even with a ramp-up in vaccinations across the U.S. Despite the elevated social risk, we believe the district's environmental and governance risks as being neutral considerations in our credit rating analysis.

Stable Outlook

Downside scenario

We could lower the rating should the college experience substantial economic or financial deterioration, leading to a significant or sustained decline in reserves or liquidity. Substantial debt issuances, such that it reduces the college's financial flexibility, could also result in a negative rating action.

Credit Opinion

Sustained tax base and population growth, driven by regional importance of Dallas-Fort Worth MSA

Tarrant County College System, serving more than 2 million residents, is coterminous with Tarrant County--the state's third-most-populous county. The district's six campus (five physical and a virtual campus) are strategically positioned throughout the county to serve one of the fastest-growing regions in the state, with healthy tax base expansion due largely to access to and participation in the rapidly growing Dallas-Fort Worth-Arlington MSA economy, which we consider to be broad and diverse. The county's employment base includes corporate operations, life science, logistics, entertainment, health care, manufacturing, and natural gas. Tarrant County is also home to higher education

institutions, which, according to management, maintain a solid educational partnership with TCCD. While the college experienced steady enrollment trends prior to the pandemic, fall headcount enrollment declined in each of the past three years. Fall 2021 enrollment of 40,562 reflects approximately a 20% decline compared with fall 2018 enrollment, which officials largely attribute to the pandemic. However, early indications are that fall 2022 enrollment should show a positive trend to near pre-pandemic levels, based on students already enrolled for fall compared to the same period last year. While considerable uncertainty related to the ongoing pandemic exists, we believe that the college's enrollment will rebound in the near term and population trends and added programs should result in longer-term growth.

While the pandemic negatively influenced the college's enrollment (and tuition revenues), the system's already large property tax base continued to grow rapidly. Taxable AV more than doubled over the past ten years, aided by more than double-digit growth in three of the past four years. Fiscal 2022 AV reached $253 billion, with preliminary valuations for 2023 expected to continue the trend of double-digit increases. With substantial development underway in the residential, commercial, and industrial sectors, officials conservatively indicate that AV growth will continue for the medium term, although the college's forecast assumes only 3% growth in out-years. We believe the growth will likely outpace these estimates in the future.

Despite the pandemic's adverse impact on enrollment, strong operational surpluses were sustained

The system's financial performance has historically been solid, in our view, and the strong performance has accelerated, largely aided by federal stimulus over the past few years. The district reported surpluses in each of the past five years. We believe that the surpluses are primarily supported by the college's demonstrated history of conservative budgeting, and we do not expect this trend will deviate over the next several years.

Financially, the system benefits from a diverse and substantial revenue base, with a history of generating what we consider healthy operating surpluses on a full-accrual basis. Full-accrual surpluses have accelerated the past two years, amounting to $55.9 million (12.7% operating surplus) and $74.7 million (16.7% operating surplus) for fiscal years 2020 and 2021, respectively. While the college's budget is balanced for fiscal 2022, we expect it will once again outperform its budget. Based on conversations with management, despite a nearly 13% drop in fall enrollment figures, the budget is trending favorably year-to-date. This is partially due to Higher Education Emergency Relief Funds (HEERF) that have offset tuition-related losses as well as supplementing the college's operating expenses. Combining these federal funds with salary and expense savings, the college is forecasting a full-accrual surplus again in fiscal 2022, although it will likely come in lower than the outsized surplus realized in 2021.

Fiscal 2021 major revenue sources consisted of property taxes (about 53%), state aid (16%), and gross tuition revenue (5%). We note that tuition revenue is down compared with previous years, due to the pandemic, but it is more than offset by federal grant revenue that accounted for 24% of revenues during the year. The fiscal year closed with $235.3 million in unrestricted net assets (UNA), but after adjusting for the net pension liability (approximately $71 million) and net OPEB liability (about $162 million), including deferred outflows and inflows, we view the system's adjusted UNA at approximately $427.5 million. This represents a very strong adjusted UNA-to-operations ratio of 106.7%, in our view. In addition, we view the system's liquidity as very strong, with year-end cash and short-term investments (net of unspent bond proceeds) of nearly $380 million, equal to about 344 days' of total operating expenditures, excluding

depreciation. This is well above the board's formal target of maintaining 180 days' unrestricted liquidity. While the college will use approximately $88 million in accumulated reserves (over a five-year period) to implement a new enterprise resource planning software, we don't expect this will materially affect the college's reserves or liquidity. While the college faces inflationary pressures, notably higher wage demands, we expect that the fiscal 2023 budget will be conservatively balanced, in line with previous budgets. Given these expectations, we don't anticipate that the colleges exceptionally strong financial profile will deteriorate.

Good financial management practices and policies

Key budgeting practices include management's use of three-to-five years of historical information to form its revenue and expenditure assumptions. In preparation of its annual budget, the system consults various outside sources, including appraisal districts to estimate AV growth and demographic information to calculate enrollment growth. The college district also reviews enrollment projections with local school districts, and it evaluates changes to student tuition and fees. In addition, TCCD incorporates adjustments to annual debt service, new facility funding (included as buildings that are completed/opened), state benefit increases, and new faculty and benefit increases. In addition, management meets with campus administrators to discuss capital, program, and personnel needs, as well as performance goals and incentives.

During each fiscal year, officials monitor budgetary performance regularly, delivering monthly budget-to-actual reports to the board of trustees. On an as-needed basis, management recommends budget amendments to address expenditure reclassifications and supplemental appropriations, which the board must approve. In addition, the district has a written investment policy with strong internal controls, and management provides a monthly summary to elected officials that details holdings and performance, as well as a more comprehensive quarterly performance report. Officials maintain a five-year financial model to provide insight into its operations related to new facilities and future conditions affecting the budget. The college also regularly updates its bond funded CIP, which identifies projects by department, costs, and funding sources. Officials report that a 10-year master plan is being developed and will be presented to the board for review later this year.

We note that, subsequent to our last review, the college adopted a formalized debt management policy and a reserve and liquidity policy. The debt policy provides written guidelines for various types of debt issuances allowed and maximum maturity and amortization of debt, while also prohibiting the use of interest-rate swaps and derivatives. The policy calls for the monitoring of several debt-affordability metrics, although there are no minimums specified. The unrestricted reserve and liquidity policy specifies a minimum unrestricted balance equal to six months of operations, with excess reserves available for one-time purposes.

Moderately elevated debt profile with plans for additional borrowing, although annual costs should remain manageable

The district's electorate authorized $825 million in GO debt in 2019, and the series 2022 bonds represent the second tranche under this authorization. Following this issuance, the district will have approximately $125 million in remaining authorization, which it expects to issue within the next three years. Pro forma overall net debt, including overlapping entities, is, in our view, high on a per capita basis at about $5,531, but moderate on a market value basis at approximately 5.3%. Amortization is slower than average, with approximately 40% of principal retired during 10 years with level debt service through maturity.

The district participates in the Texas Teachers' Retirement System, which was 89% funded at Aug. 31, 2021. The district's proportionate share of the collective net pension liability equals about $71.5 million. In fiscal 2021, the district paid its full required contribution of about $4.9 million, or less than 1% of expenditures, toward its pension obligations.

Under a special-funding situation, the state contributes a sizable share of the employer's contribution and carries responsibility for the employer's proportionate share of the unfunded liability. Since the district makes statutory contributions typically lower than actuarially determined contributions (ADC), fiscal 2021 contributions were below minimal funding progress, but they exceeded our static funding metric. Furthermore, the plan's 30-year, level-dollar, open-amortization schedule will result in slow funding progress, even if actual contributions meet ADC, and we believe the 7.25% discount rate leads to contribution volatility.

Despite that, we do not view pension and OPEB liabilities as an immediate credit pressure, because required contributions currently account for a small portion of the district's budget. We do not expect this will increase significantly during the next few fiscal years.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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