

CREDIT OPINION

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Addison (Town of) TX

Update to credit analysis

Summary

The [Town of Addison, TX's](#) (Aaa stable) credit profile is anchored by a regionally important economy north of the [City of Dallas](#) (A1 stable) with a moderately sized and growing tax base. The town's strong financial operations have led to high reserve and liquidity levels despite a slightly higher reliance on economically sensitive sales tax revenue which continue to grow given the town's role as a major job center. Addison's financial position is further strengthened by access to additional liquidity outside the main operating funds. The town has slightly higher debt ratios compared to peers and positively the pension burden is affordable and will not be a drag on credit quality over the next several years.

Credit strengths

- » Sound financial practices evidenced by high reserves
- » Major commercial economic center
- » Income and wealth indicators exceed national levels

Credit challenges

- » Above average reliance on commercial property and sales tax revenues compared to peers
- » Debt levels are slightly elevated compared to peers with slower average repayment

Rating outlook

The stable outlook reflects our expectation that town's management team will continue to maintain balanced operations supported by a stable economy and solid liquidity position which contributes to a stable credit profile over the medium term.

Factors that could lead to an upgrade

- » Not applicable

Factors that could lead to a downgrade

- » Reduction in reserve levels
- » Significant economic decline
- » Sizeable debt issuance absent corresponding tax base growth

Key indicators

Exhibit 1

Addison (Town of) TX

	2017	2018	2019	2020	2021
Economy/Tax Base					
Total Full Value (\$000)	\$4,300,272	\$4,450,534	\$4,725,759	\$4,819,907	\$4,925,943
Population	15,455	15,626	15,302	15,428	16,320
Full Value Per Capita	\$278,245	\$284,816	\$308,833	\$312,413	\$301,835
Median Family Income (% of US Median)	125.4%	119.0%	106.1%	104.8%	104.8%
Finances					
Operating Revenue (\$000)	\$47,377	\$46,938	\$46,861	\$46,721	\$50,444
Fund Balance (\$000)	\$16,742	\$20,634	\$20,102	\$20,053	\$20,219
Cash Balance (\$000)	\$17,448	\$21,065	\$20,111	\$21,353	\$21,713
Fund Balance as a % of Revenues	35.3%	44.0%	42.9%	42.9%	40.1%
Cash Balance as a % of Revenues	36.8%	44.9%	42.9%	45.7%	43.0%
Debt/Pensions					
Net Direct Debt (\$000)	\$77,650	\$72,650	\$68,735	\$95,630	\$103,685
3-Year Average of Moody's ANPL (\$000)	\$67,894	\$59,677	\$53,203	\$61,346	\$74,241
Net Direct Debt / Full Value (%)	1.8%	1.6%	1.5%	2.0%	2.2%
Net Direct Debt / Operating Revenues (x)	1.6x	1.5x	1.5x	2.0x	2.1x
Moody's - ANPL (3-yr average) to Full Value (%)	1.6%	1.3%	1.1%	1.3%	1.6%
Moody's - ANPL (3-yr average) to Revenues (x)	1.4x	1.3x	1.1x	1.3x	1.5x

Sources: US Census Bureau, Addison (Town of) TX's financial statements and Moody's Investors Service

Profile

The Town of Addison is 12 miles north of downtown Dallas in [Dallas County](#) (Aaa stable). The town is home to several office spaces and the economy sees a high concentration of profession jobs with daytime population well over 3 times the nighttime population. The current population estimate is about 17,720.

Detailed credit considerations

Economy and tax base: moderately sized and growing tax base with major job center

The town's position as a major job center will continue to support a moderately growing tax base. Currently valued at \$5.1 billion as of 2022, the town's tax base has grown by an average of 3.4% over the last five years, with an increase of about 5% expected for 2023. Retail, commercial and industrial property account for almost 50% of the base. This number increases to about 60% when including tangible personal, commercial property. Residential property accounts for a smaller but still substantial 34%, including single and multifamily property. Town officials report stable economic conditions with office occupancy rates at about 80%, close to pre-pandemic levels. Although the town has limited land for new development, redevelopment of existing property continues to drive growth. Ongoing development includes multifamily housing and townhomes in Vitruvian Park and a transit oriented development being constructed near a new [Dallas Area Rapid Transit](#) (Aa2 stable) light rail station.

Addison's population grew by about 18% over the past decade according to the American Community Survey and the access to employment both within the city and the greater Dallas area have led to solid median family income at about 105% of the national figure. The large amount of commercial property brings full value per capita to a strong \$330,000. The labor market in Dallas County is on par with the nation with unemployment at 3.6% as of May 2022.

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Financial operations and reserves: high reserve levels with access to non-general fund liquidity

Addison's financial position will remain sound, guided by prudent expenditure management and conservative budgeting practices. For fiscal 2022 (September 30 year end) officials are anticipating a general fund operating surplus of \$2.1 million achieved due to better than budgeted sales tax revenue and conservative expenditure budgeting. The majority of this surplus will be transferred to the Self-Funded Special Projects Fund and Facility Maintenance Fund for future capital expenditures. Fiscal 2021 ended with an available operating fund (combined general and debt service funds) balance of \$20.2 million as of, equivalent to a strong 40% of operating fund revenue. In addition to its high operating fund reserves, the town also maintains additional financial flexibility in the Investment Fund, Self-Funded Streets Projects Fund, and the Self-Funded Special Projects Fund which are projected to have a combined reserves of \$11 million at the end of fiscal 2022. The town also created the Facility Maintenance Internal Service Fund in fiscal 2021 to provide emergency and planned maintenance town facilities that has about \$1 million in reserves. The town was allocated about \$4 million in funds from the American Rescue Plan with three-quarters used to replace lost revenue in the Hotel Fund with the remainder for the Self-Funded Special Projects Fund.

Sales taxes have historically accounting for a meaningful portion of the town's operating fund revenue, accounting for 32% in fiscal 2021, compared to 56% for property taxes. Sales taxes dipped by about 6% from fiscal 2019 to 2020, and increased by about 5% in fiscal 2021. For the current year sales taxes are ahead of budget with about 78% of budget revenue collected through the first eight months of the year.

Liquidity

The town's operating liquidity remained healthy in fiscal 2021 at \$21.7 million, or 43% of operating revenue. Cash levels are expected to improve in line with fund balance trends for fiscal 2022.

Debt and pensions: affordable debt and pensions

The town's debt and pension profile will remain affordable over the next several years supported by a moderately sized tax base and capacity to increase property tax revenues for debt repayment. Including an upcoming sale, the town's net direct debt will reach \$107 million, equivalent to 2.1% of the fiscal 2022 assessed value and 2.1x operating revenue. The town currently has about \$42 million in authorized but unissued debt and plans for annual debt issuance until the authorization is exhausted, with about \$15 million in additional borrowing planned for public infrastructure over the next seven years.

Legal security

The bonds are secured by a direct and continuing annual ad valorem tax, levied on all taxable property within the limits prescribed bylaw.

Debt structure

Principal payout is below similarly rated peers with under three-quarters of principal retired in 10 years. The debt service schedule is largely descending until final maturity in fiscal 2042.

Debt-related derivatives

All of the town's debt is fixed rate and the town is not party to any derivative agreements.

Pensions and OPEB

The town's unfunded pension and other post employment benefits (OPEB) liabilities should remain a manageable portion of town's total leverage. The town provides pension benefits for employees through a nontraditional, joint contributory, hybrid defined benefit plan in the statewide Texas Municipal Retirement System (TMRS), an agent multi-employer public employee retirement system. Addison's adjusted net pension liability (ANPL), based on a 2.52% discount rate, was \$94.4 million in fiscal 2021. By comparison, the town reported a GASB net pension liability of \$2.1 million, based on a 6.75% discount rate; these figures are net of self support from the utility system. Under TMRS plan rules, the town has the flexibility to award cost of living adjustments (COLAs) to employees on an ad hoc basis annually, though the town has not awarded COLAs since 2015. In fiscal 2021, the town's pension contribution of \$2.3 million was ahead of our trend water indicator of \$2 million.

In addition to pension benefits, the town also provides retiree health care (OPEB) benefits to employees. However, the liability is manageable, with our adjusted net OPEB liability equating to just 9% of fiscal 2021 operating revenue. Additionally, total fixed costs (debt service, pension contributions and OPEB contributions) remain manageable at approximately 20% of operating revenue.

ESG considerations

Environmental

Addison is exposed to natural and man made hazards by virtue of its location in the Great Plains per the National Climate Assessment. The town has high risk to water stress resulting in drought like patterns and also has medium risk to heat stress and extreme rainfall. The environmental shift will evolve over the longer term and the town will benefit from long range planning. The town's high reserves will also provide buffer to offset any potential related financial event.

Social

Social considerations are incorporated into the economy and tax base section. Please refer to that section for more detailed credit information.

Governance

The town demonstrates good governance by multiyear capital and financial planning. The town also uses quarterly reviews of major operating funds in combination with a comparison of historical data. Financial practices are governed by conservative assumptions, as well as a historical willingness and ability to raise property tax rates during difficult financial periods, consistent with traits exhibited by a sophisticated management team. Although some of the town's ability to raise taxes will be limited by the most recent legislative change, the town's demonstrated ability for solid financial performance driven by prudent processes and practices will benefit the credit profile. The town maintains a fund balance policy equal to 25% of operations in its major operating funds, but town officials strive for a minimum of 30%.

Texas Cities have an institutional framework score ¹ of "Aa," which is strong. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. Revenues are largely derived from property taxes which tend to be highly stable and predictable, sales taxes which are moderately stable and predictable and other fees. As a result unpredictable revenue fluctuations tend to be minor, or under 5% annually. Cities have a moderate ability to raise revenues because most cities are at the sales tax cap set by state statute. Additionally, property taxes are subject to a statutory cap of \$25 per \$1,000 of assessed values, with no more than \$15 allocated for debt. Although most cities are well under the cap, cities can only increase their property tax revenues by 3.5% on existing property without voter approval on an annual basis; all increases above 3.5% must be approved by voters. Operating expenditures for cities tend to be highly stable and predictable with minor fluctuations under 5% annually. Cities also have a strong ability to reduce expenditures.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 2

Addison (Town of) TX

Scorecard Factors and Subfactors	Measure	Score
Economy/Tax Base (30%) ^[1]		
Tax Base Size: Full Value (in 000s)	\$5,075,396	Aa
Full Value Per Capita	\$328,973	Aaa
Median Family Income (% of US Median)	104.8%	Aa
Notching Factors: ^[2]		
Economic Concentration		Down
Finances (30%)		
Fund Balance as a % of Revenues	40.1%	Aaa
5-Year Dollar Change in Fund Balance as % of Revenues	12.7%	Aa
Cash Balance as a % of Revenues	43.0%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	14.8%	Aa
Notching Factors: ^[2]		
Other Scorecard Adjustment Related to Finances: Additional reserves outside operating funds		Up
Management (20%)		
Institutional Framework	Aa	Aa
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	1.0x	Aa
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	2.1%	A
Net Direct Debt / Operating Revenues (x)	2.1x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	1.5%	Aa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.5x	A
Notching Factors: ^[2]		
Unusually Strong or Weak Security Features		Up
	Scorecard-Indicated Outcome	Aa1
	Assigned Rating	Aaa

[1] Economy measures are based on data from the most recent year available.

[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.

[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication

Source: US Census Bureau, Addison (Town of) TX's financial statements and Moody's Investors Service

Endnotes

- 1 The institutional framework score assesses a municipality's legal ability to match revenues with expenditures based on its constitutionally and legislatively conferred powers and responsibilities. See [US Local Government General Obligation Debt \(July 2020\)](#) methodology report for more details.

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