

Discussion Materials Prepared for the City of Richmond, Virginia



Debt Capacity and Affordability Briefing

March 10, 2022



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Background



- Davenport & Company LLC, (“Davenport”) was initially engaged as Financial Advisor by the City of Richmond (the “City”) in 2000.
 - Since 2000, we have advised the City on its Debt Capacity and Affordability, as well as, provided comprehensive and holistic financial advisory services that have assisted the City in achieving a total of 11 Credit Rating upgrades resulting in the following Credit Ratings today:

National Credit Rating Agency	G.O. Bond Rating	Utility Revenue Bond Rating
Fitch Ratings	AA+	AA
Moody’s Investors Service	Aa1	Aa1
S&P Global	AA+	AA

- In addition, the City’s adherence to Strong Financial (Debt and Fund Balance) Policy Guidelines and Structurally Balanced Budgeting have been key factors in strengthening its finances and Credit Ratings.

Goals & Objectives of this Briefing



- As the City begins in earnest the FY 2023 Budget deliberations, Davenport has been tasked with presenting this Briefing on the City's Debt Capacity and Debt Affordability.
 - These two concepts are interrelated AND equally as important for the City in multi-year, long-term planning.

- What is Debt Capacity?
 - Debt Capacity is an evaluation of the amount of Planned Debt that could be issued by the City without violating the City's Debt Management Policies. It answers the question:
 - Will the City remain in compliance with its Debt Policy Guidelines?

- What is Debt Affordability?
 - Debt Affordability is an evaluation of the projected Budgetary cash flow impact of New Debt Service – It answers the questions:
 - Does the City have the ability to pay for New Debt Service from Existing Budgeted Revenues for Debt Service? – OR -
 - Does the City need to increase the approximate \$87 Million Budget for Debt Service? AND, if so, by how much?

Debt Capacity | Governance by Debt Management Policies



- The City has historically planned its Future CIP and Debt Issuances based on strict adherence to its Debt Capacity, which is governed by its Debt Management Policies, which are:
 - Tax Supported Debt vs. Total Assessed Taxable Valuation shall not exceed 3.75%.
 - Total Tax Supported Debt Service shall not exceed 10% of the Total Budget.
 - The City’s 10–Year payout ratio of Tax Supported Debt shall not be less than 60%.

- A Key Consideration that is also taken into account in planning Future CIP and Debt Issuances is the impact of City Council’s *Prior Bond Authorizations But Not Issued (CIP) – these amounts have not been spent and the related G.O. Debt has not yet been issued.*
 - The City has approximately \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned) that are to be funded by Planned G.O. Debt.

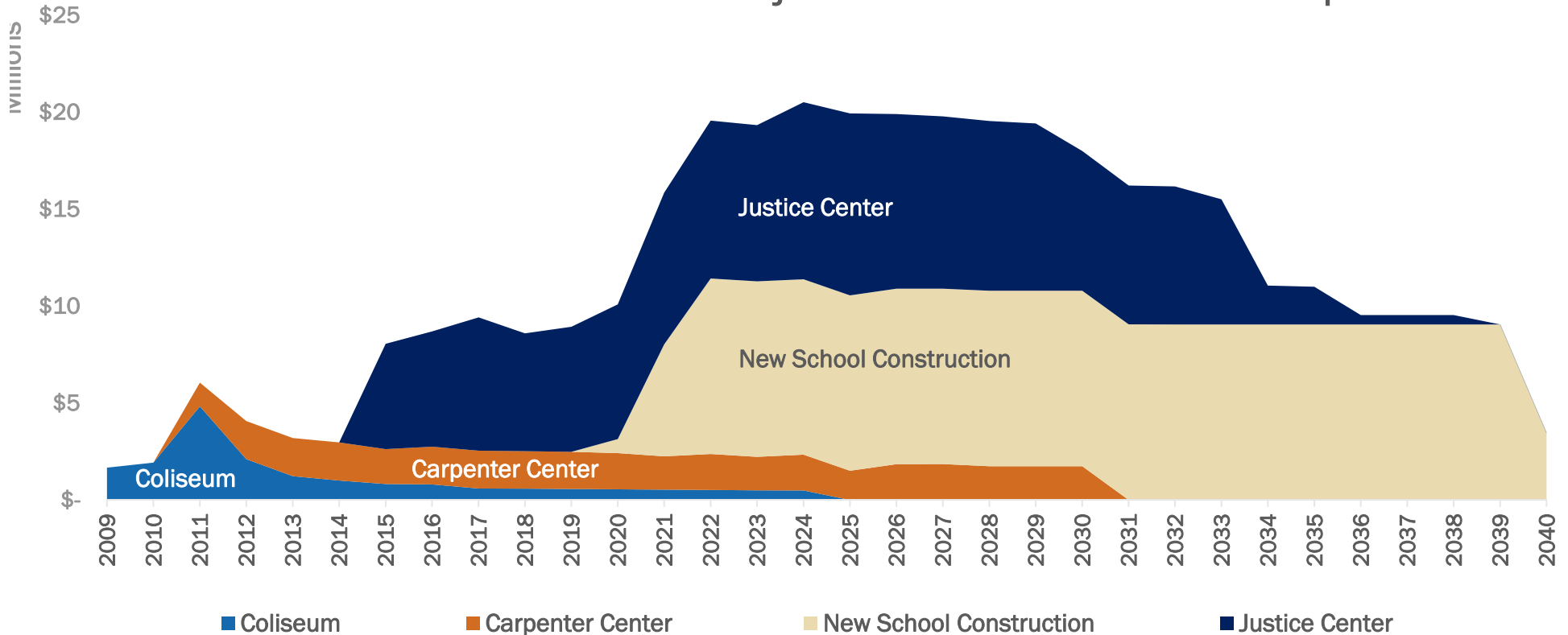
- *The City has been Fiscally Responsible by planning its 5-year debt funded CIP to ensure compliance with its Debt Management policies.*
 - *The debt funded CIP decisions made today impact the City for years to come.*
 - *Fiscally Responsible CIP planning should also reserve Debt Capacity for unforeseen circumstances and future long-term needs.*

Decisions Made Today Have Long-Term Impacts



- The debt funded CIP decisions made today have long-term impacts to the City for years to come.

Debt Service of Selected Projects Shown for Illustrative Purposes



Project	Authorization	Amount	Payoff
Coliseum	FY 2001	\$8.7M	FY2024
Carpenter Center	FY 2007-2010	\$22.9M	FY2030
Justice Center	FY 2010-2014	\$137.6M	FY2038
New School	FY 2019	\$150.0M	FY2040

- Cardinal Elementary
- Marsh Elementary
- River City Middle

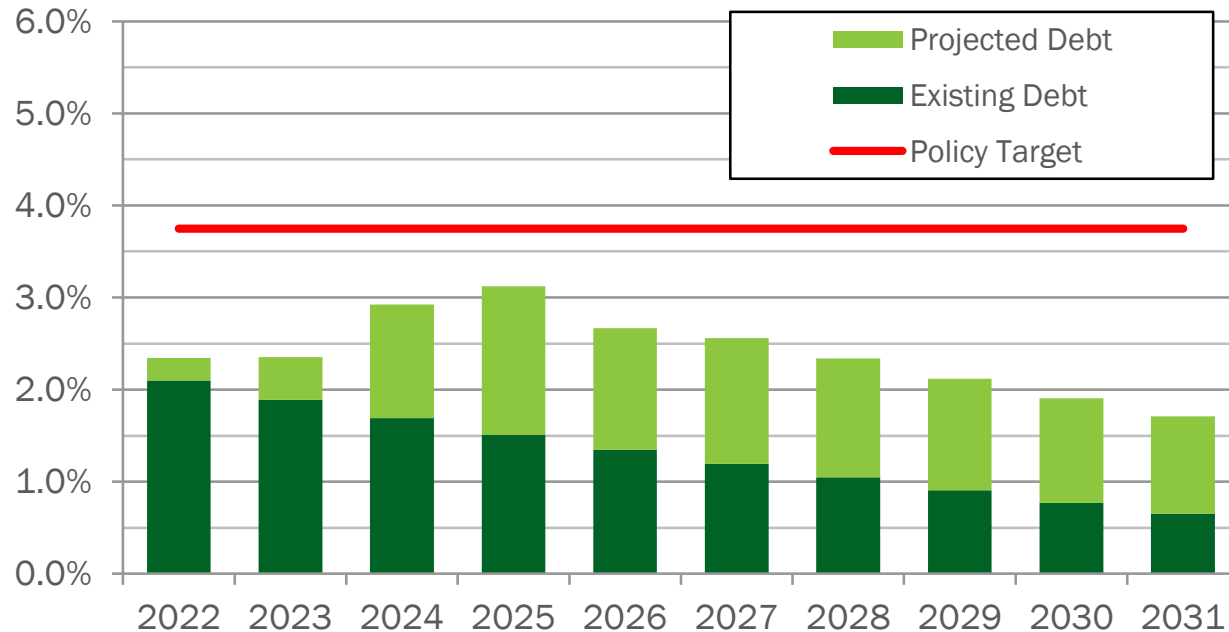
Note: This graph does not represent the total annual debt service of the City.

Tax Supported Debt vs. Total Assessed Taxable Valuation | Policy Impact



- Debt Policy: Tax Supported Debt vs. Total Assessed Taxable Valuation shall not exceed 3.75%.
 - After the issuance of G.O. Debt for the \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned) the City is projected to remain in compliance with this Policy.

Debt vs Total Assessed Valuation



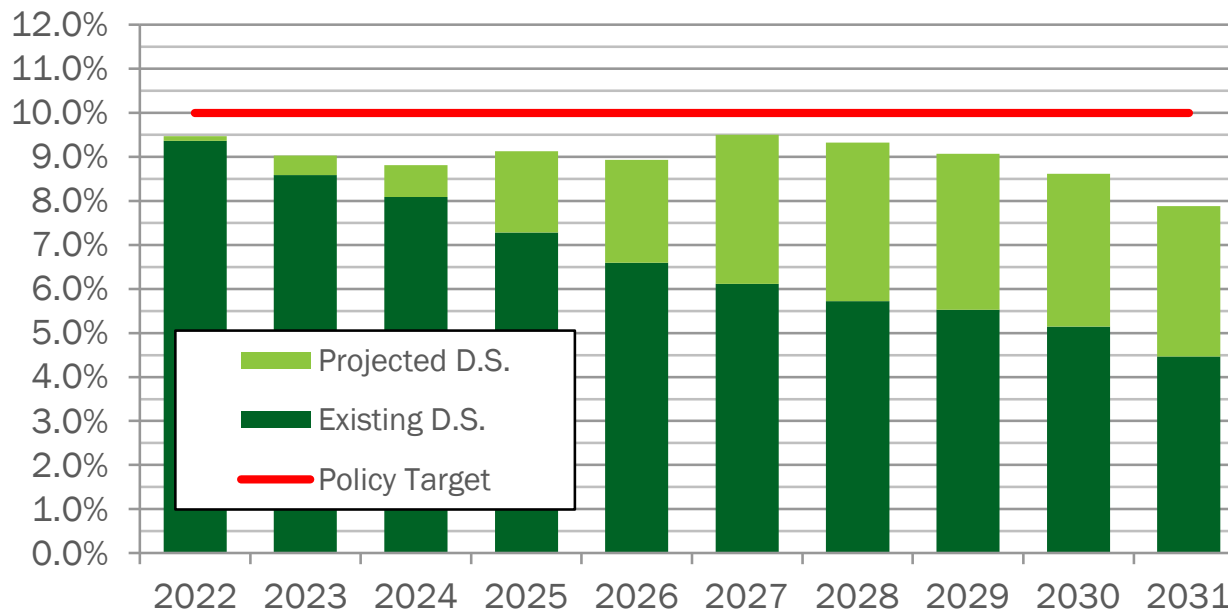
- The City’s projected ratios have historically remained well below this Policy Target.

Tax Supported Debt Service vs. Budget | Policy Impact



- Debt Policy: Total Tax Supported Debt Service shall not exceed 10% of the Total Budget.
 - After the issuance of G.O. Debt for the \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned) the City is projected to remain in compliance with this Policy.

Debt Service vs Budget



– This Policy has historically served as the “governor” of the City’s CIP and the City has programmed its CIP Authorization and G.O. Bond issuances based on this 10% Policy Target.

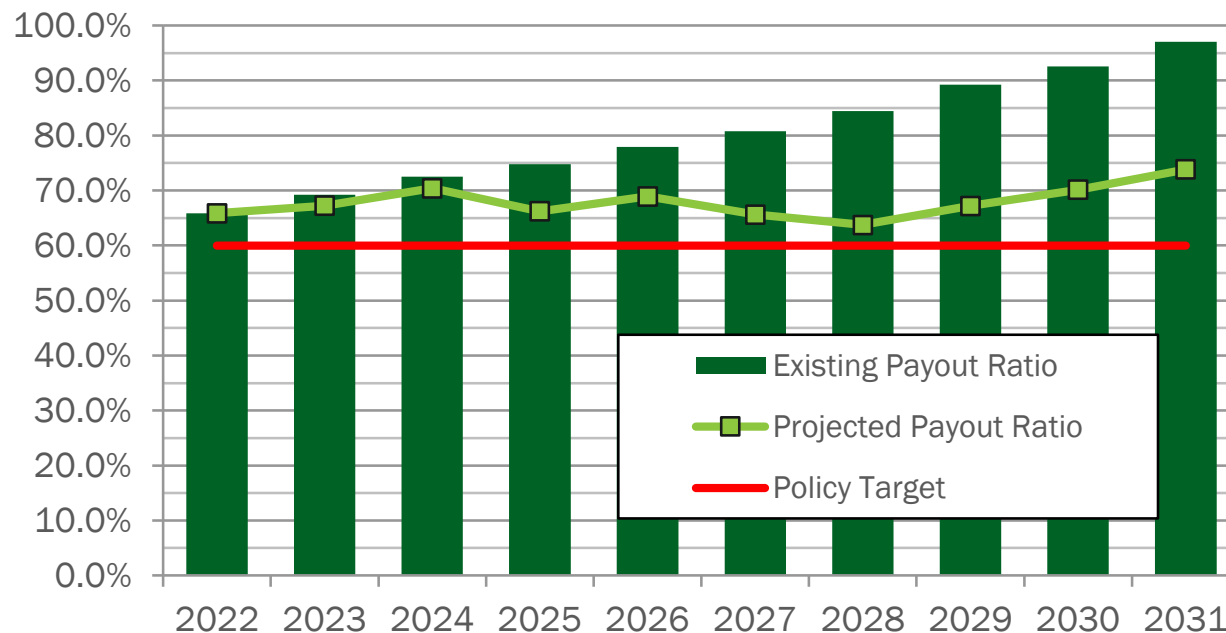
– *This Policy does not address the Debt Affordability – meaning the ability to pay for New Debt Service from Existing Budgeted Revenues for Debt Service.*

10-Year Payout Ratio | Policy Impact



- Debt Policy: The City's 10-Year payout ratio of Tax Supported Debt shall not be less than 60%.
 - After the issuance of G.O. Debt for the \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned) the City is projected to remain in compliance with this Policy.

10-Year Payout Ratio



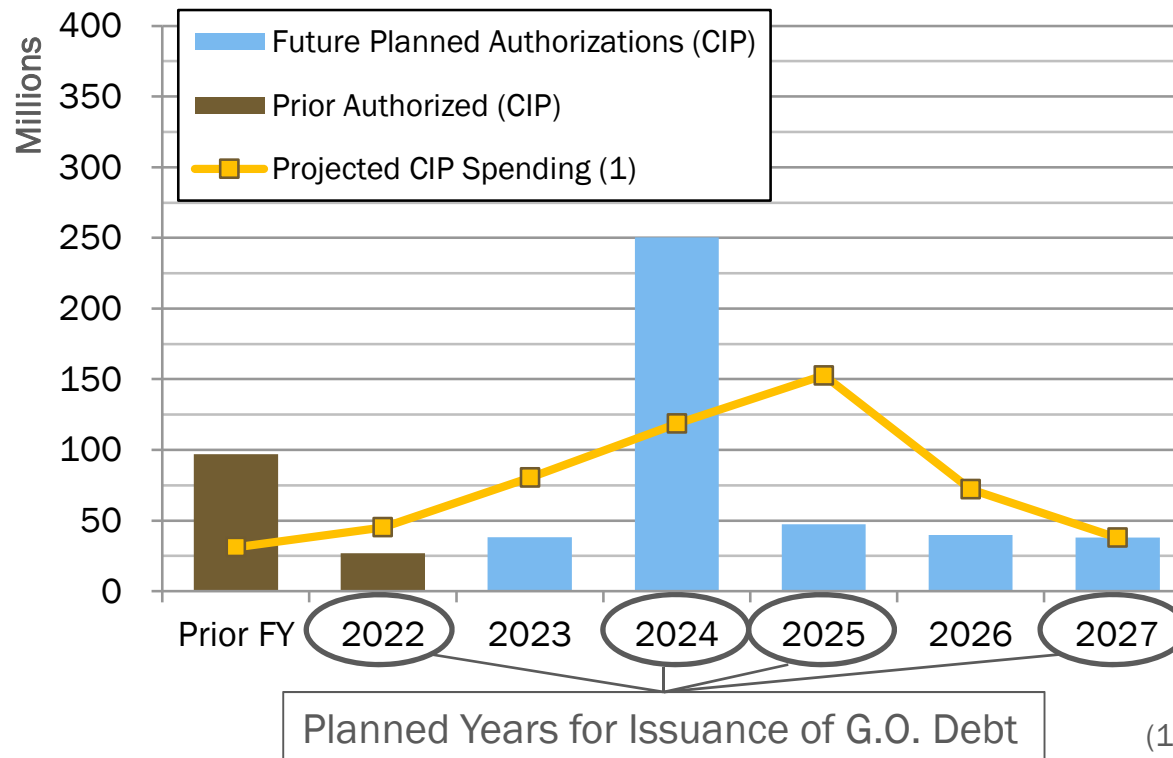
- This Policy measures how fast the City repays its debt. The 60% Policy Target means that the City structures its debt such that approximately 60% of outstanding tax supported debt will be repaid in 10 years, which is considered strong.

Total Projected Authorizations | Projected CIP Spending



- The \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned) vs. Projected CIP Spending is shown below.
 - The City has historically authorized CIP G.O. Debt faster than it can be spent.
 - The City is working to align these planning areas with the Capital Planning Program, which will assist in bringing spending, authorizations and bond issuance in line.

Total Authorizations vs Projected Spending



(1) Source: Department of Finance.

Capital Planning Program



- Goals and Objectives: The goal of the Capital Planning Program (the “Program”) is to better align the City’s Capital Improvement Plan (CIP) planning process with “Best Practices” of highly rated local governments.
- The Capital Planning Program will be funded initially with a \$10 Million Line of Credit.
- The Program will be used to fund advanced planning and design and to evaluate high priority projects for potential future funding.
- Advanced feasibility and planning work will help the City better define project scopes, which will result in more precise cost estimates and allow the Administration and City Council to make more informed decisions about the timing and overall costs of capital projects.
- The Program will also better enable the City to match its Bond Authorizations to spending and related debt issuances.

Debt Affordability



- The City has historically been able to increase its Debt Service Budget over time to support its Planned G.O. Bond issuances.

- In FY 2022, the City budgeted approximately \$86.5 Million in Local Revenues to repay long-term Tax Supported Debt Service.
 - This figure does not include G.O. Debt repaid by Enterprise Related Funds (i.e. Utilities, Parking, Stormwater), Debt repaid by dedicated non-local revenues (i.e. Stone Brewery) or Equipment Notes repaid/charged to other funds.

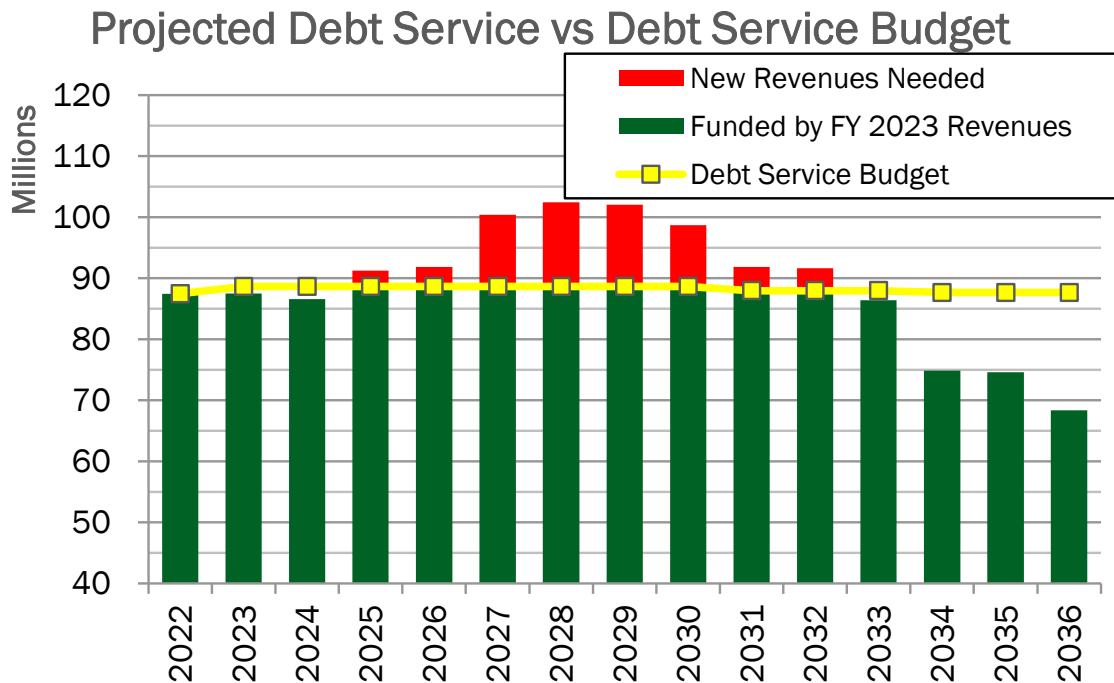
- In FY 2023, the City’s Local Revenues needed for the repayment long-term Tax Supported Debt Service is estimated to approximate \$87.7 Million. This figure takes into account the following:
 - Projected increase in New Debt Service of approximately \$3.1 Million, which is offset by a decline in Existing Debt Service of \$1.8 Million from FY 2022.

- The City is projected to eventually need additional new revenues to repay its Planned G.O. Debt Issuances as shown on the next two pages.

Projected New Revenues Needed | Planned G.O. Debt



- The graph below highlights the Projected New Revenues needed to support Planned G.O. Debt based on the \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned).
 - On/about FY 2025, the City will need approximately \$3 Million in new Revenues to repay projected increasing Debt Service (Equivalent of 1¢ Real Estate Tax Rate Impact).
 - By FY 2028, the City will need approximately \$14 Million in new Revenues to repay projected increasing Debt Service (Equivalent of 4.5¢ Real Estate Tax Rate Impact).



- 1¢ on the City’s Real Estate Tax Rate generates approximately \$3.1 Million in recurring revenues, which supports about \$40 Million of 20-year G.O. Bonds.
- A Credit Rating increase from AA+ to AAA would result in about \$50,000 reduction in interest costs for each \$50 Million of G.O. Bonds borrowed.

Projected New Revenues Needed | Supporting Detail



- The table below highlights the Projected New Revenues needed to support Planned G.O. Debt based on the \$537.7 Million of Total Projected Authorizations for CIP (Prior and Future Planned).

Fiscal Year	Total Existing and Projected Debt Service	Debt Service Budget	Debt Service Budget Surplus (Shortfall)	Projected New Revenues Needed
				62,411,507
2022	87,471,916	87,471,916	0	0
2023	87,487,128	88,670,360	1,183,232	0
2024	86,571,458	88,670,360	2,098,902	0
2025	91,257,668	88,670,360	(2,587,308)	2,587,308
2026	91,884,845	88,670,360	(3,214,485)	3,214,485
2027	100,449,489	88,670,360	(11,779,129)	11,779,129
2028	102,446,689	88,670,360	(13,776,329)	13,776,329
2029	102,036,160	88,670,360	(13,365,800)	13,365,800
2030	98,707,176	88,670,360	(10,036,816)	10,036,816
2031	91,877,844	87,959,859	(3,917,985)	3,917,985
2032	91,693,513	87,959,859	(3,733,654)	3,733,654
2033	86,421,878	87,959,859	1,537,981	0
2034	74,867,822	87,679,734	12,811,912	0
2035	74,617,819	87,679,734	13,061,915	0
2036	68,383,094	87,679,734	19,296,640	0



- Cash Funding of CIP – The practice of budgeting recurring General Fund Revenues for pay-as-you-go capital is considered a “Best Practice” of local governments.
 - The City has historically not budgeted any significant dollars toward Cash Funding of CIP.

- This practice better enables the City to have structurally balanced budgets with a cushion for unforeseen circumstances (either for revenue shortfalls or emergency expenditure increases).
 - The National Credit Rating Agencies view this practice positively as it provides the City with flexibility in the budget if spending needs to be redirected in a particular year.
 - To the extent the revenues are not used for pay-as-you-go capital, they can be used to bolster Unassigned Fund Balance or other fund other reserves, if necessary.
 - Applying recurring revenues toward pay-as-you-go capital has positive ripple effects with respect to the City’s debt burden by:
 - Helping to keep borrowing levels down,
 - Reducing pressure on the City’s debt ratios, and
 - Reducing cash flow pressures related to debt service.

Other Topics/Considerations | Importance of Revenue Flexibility

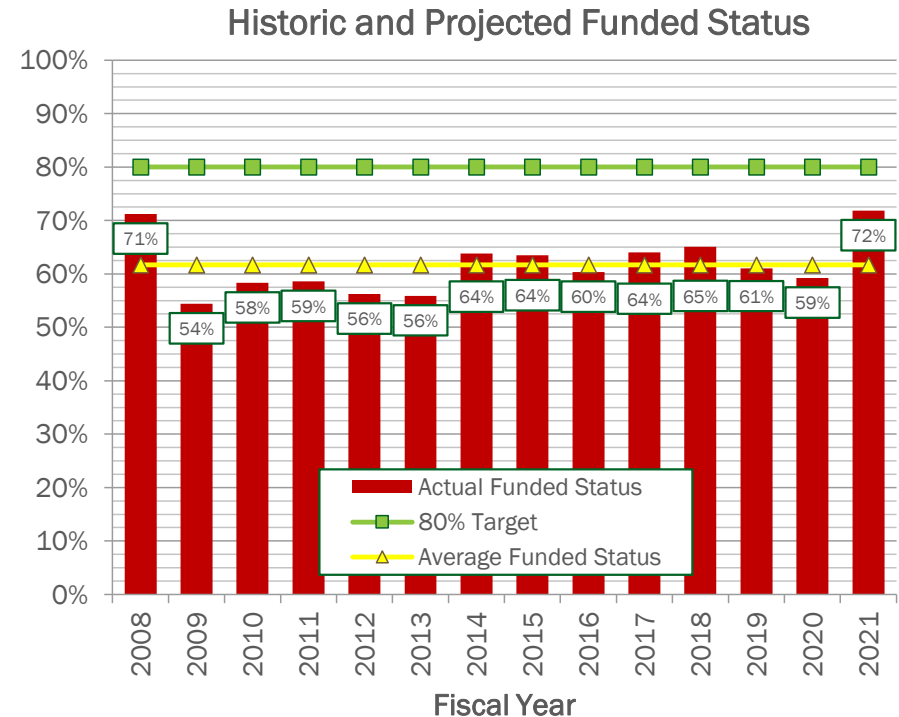


- The National Credit Rating Agencies (Fitch in particular) view revenue flexibility as a credit strength. Revenue Flexibility is an important factor in the evaluation of the City's credit ratings.
- Virginia localities, in general, have more flexibility with revenues than those in other states (i.e. no cap on general property tax rates, no statutory laws governing use of local general fund dollars).
- Designating certain revenues for specific purposes may be helpful in funding specific or targeted needs.
 - However, too many designations may result in unduly constraining the City's ability to fund its most essential priorities; and
 - They may also limit the City's ability to flexibly shift revenues and resources to fund other unforeseen needs as they arise.
- Maintaining the maximum level of Revenue Flexibility enables the City to optimally budget its resources and address its priorities as they evolve over time.

Other Topics/Considerations | Richmond Retirement System Funded Status



- From FY 2020 to FY 2021, the RRS Funded Status increased from 59.2% to 71.8%.
 - This increase was due to a record 23.7% investment return.
- Since 2008, the Richmond Retirement System’s (RRS) funded status has averaged 61.7%
 - This level is well below the “80% Target” that is considered the minimum threshold for healthy pension systems.
- COLA adjustments are not recommended for a pension system with a funded status below the 80% minimum threshold for healthy pension systems.
 - In addition, before implementing a COLA the City should fully analyze the impact on future actuarially determined contribution requirements.



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