Central Virginia Transportation Authority

PFM Presentation to the Finance Committee

April 12, 2023

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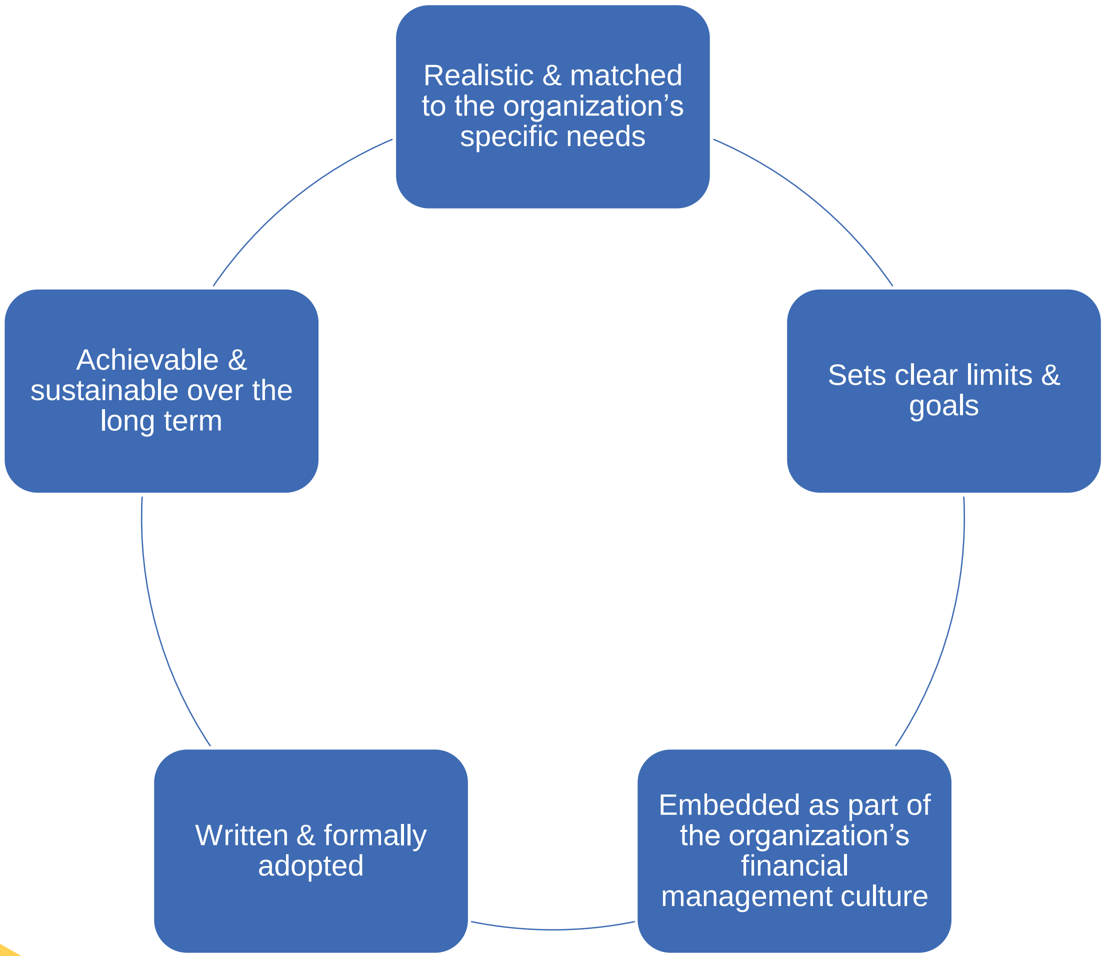
Presentation Overview

- Objective: Provide information only, no action required
- Review elements of debt and reserve policies
- Next steps
- Q&A

Elements of Effective Policies

CVTA adopted its existing Financial Policies and Procedures in February of 2021.



CVTA’s Existing Financial Policies and Procedures

- CVTA’s existing Policies cover the following:
  - Establish CVTA’s roles and responsibilities
  - Establish framework for strong internal controls and processes
  - Ensure proper management, review, and approval of financial transactions
  - Achieve operational efficiencies through standardization of practices
- Currently, CVTA’s Policies do not include any debt policies
  - Inclusion of debt policies is a best financial management practice
  - Debt policies ensure long term affordability of debt and supports high credit ratings
- PFM recommends a revision & update to the existing Policies to include:
  - Debt service coverage requirement
  - Working capital reserve requirement

How to Evaluate CVTA's Debt Affordability

- Most of CVTA's member localities use a debt service as % of Budget (expenditures or revenues) and a debt to assessed value ratio to measure its General Obligation Bonds debt capacity
- The industry standard ratio used to evaluate dedicated tax backed bonds and revenue bonds is known as a debt service coverage (DSC) ratio
- The DSC is a ratio of net revenue available for debt service in a given year divided by annual debt service
  - 35% of CVTA Revenues for regional purposes (or a portion of the regional revenues that is pledged) would be in numerator
  - Often times evaluated with maximum annual debt service ("MADS") in the denominator

$$\textbf{Debt Service Coverage} = \frac{\text{35\% of CVTA Revenues}}{\text{Annual Debt Service (or Maximum Annual Debt Service)}} = \frac{\$70\text{M}}{\$35\text{M}} = 2.0 \text{ times (x)}$$

- High ratings typically follow higher coverage, all other factors held equal

CVTA Debt Service Coverage Policy Recommendation

- PFM recommends that of the CVTA's regional revenues, that the Authority only pledge and use **sales tax revenues** to pay debt service on any bonds that are issued
- Subsequently, the numerator of the debt service coverage policy should be sales tax revenues only
- As for the level, PFM recommends a 2.0x minimum coverage requirement
- Proposed language to be inserted under the CVTA Financial Policies Regional Revenue (35% Funds) section:

The ratio of <u>sales tax revenues</u> portion of the annual Regional CVTA Funds to annual senior lien debt service will be a minimum of 2.0 times.

Comparable Structures

If CVTA's targets a minimum debt coverage of 2.0x, the Authority will likely be rated in the AA-category. At 2.0x coverage ratio, CVTA can issue approximately $300 million in debt.

	NVTA Senior Lien	HRTAC Senior Lien	I-81 Senior Lien
Pledged Revenues	Sales ($270m)	Sales ($146m) & fuels ($55m)	Fuels ($71m)
Moody's/S&P/Fitch	Aa1/AA+/AA+	Aa2/AA/NR (long term bonds)	Aa1/AA-/NR
As of Date	*June 2020*	*April 2022*	*July 2021*
Select Features			
Additional Bonds Test (Historical Rev./Max. Annual Debt Service)	2.0x	2.0x	2.0x

Working Capital Reserve – Background

- A working capital reserve is dollars set aside to help achieve financial stability and flexibility, and provide a cushion against unexpected events that could impact cash flow
- Under CVTA's Regional Project Selection & Allocation Framework, the Authority has adopted a general programming methodology that only allocates a certain targeted % of funds to projects to cover cost increases and allow for project selection in the future
- PFM views this as a planning and programming guidance/practice, as opposed to a reserve
- PFM recommends removal of references to "reserve" in describing this practice in the Regional Project Selection & Allocation Framework to promote clarity and distinction from the Authority's working capital reserve

Working Capital Reserve – Background

- Since CVTA is a regional planning organization that provides funding opportunities, and the Authority does not implement or construct projects, the primary purpose of the working capital reserve would be help CVTA manage its cash flow based on timing mismatches between revenue receipt and the disbursement of funds
- Examples include:
  - Actual Regional Revenues are less than projected
  - Requests for disbursement of funds occur sooner than expected

Working Capital Reserve Recommendation

- CVTA's Financial Policies states "Fund or maintain a Working Capital Reserve in an amount determine by CVTA Finance Committee"
- Define the working capital reserve requirements in the existing Financial Policies and Procedures
  - Initially set at an amount equal to 3 months of the budgeted, annual Regional CVTA funds, which equal to approximately $17 million
- To be reevaluated once project expenditures occur, and standard project agreements are approved, by June 30, 2025
- Proposed language to be inserted under the CVTA Financial Policies Regional Revenue (35% Funds) section:

CVTA will maintain a Working Capital Reserve equal to at least 3 months of the budgeted, annual Regional CVTA Funds. If tapped, the Chief Financial Staff of the CVTA will develop a plan to restore the Working Capital Reserve to its minimum level over a period not to exceed 18 months. The Authority will revisit the level of this reserve no later than June 30, 2025, to reflect its actual cash flow patterns and expenditure reimbursements.

Working Capital Reserve – Possible Funding Strategy

- Consider utilizing investment earnings from Regional Revenues
  - YTD through 2/28/2023 (6 months) total $1.9 million*
  - If the investment earnings on the Regional Revenues remain in line for the remainder of the FY, total earnings may be close to $4 million
- Consider using any actual Regional Revenues that came in over forecasted amount
  - YTD through 2/28/2023 (6 months) collected $37.2 million*
  - Forecasted FY 2023 Regional Revenues total $67.5 million*
  - Actual FY 2022 Regional Revenues totaled $72 million*
  - If actual FY 2023 Regional Revenues come in close to FY 2022 levels, $4.5 million is available
- The Authority can allocate the remaining dollars necessary to fully fund the working capital reserve at its next six-year planning cycle
- CVTA could also fully fund the working capital reserve as part of its next debt issuance by identifying a project (planned to be funded with cash) to fund with bonds, creating cash flow to fully fund the working capital reserve

*Source: CVTA.

Next Steps

- Solicit feedback from member localities
- Briefing to the Board, if desired
- Consider requesting confidential, indicative ratings from rating agencies

Q & A