House Appropriations Committee Retreat

Update on Capital Outlay & Debt Capacity

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Update on Capital Outlay & Debt Capacity

- Basis of Commonwealth's Debt Capacity
- Current Status of Commonwealth Debt Capacity
- Comparative Data
- Capital Outlay History & Actions
- Issues for 2018-2020 Biennium

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Virginia Constitution

- Article X, Section 9 provides for the issuance of debt
  - Sections 9(a), 9(b) & 9(c) provide the Full Faith and Credit of the Commonwealth
- 9 (a) debt is reserved to meet emergencies
- 9 (b) debt is often referred to as general obligation or GO debt and requires voter approval
- 9 (c) debt is for revenue-producing capital projects and is authorized by 2/3 vote of the General Assembly
  - Self-supporting in nature; the Governor is required to certify that pledged revenues are sufficient
  - For example, dorm and dining hall projects
  - Because it has the Full Faith and Credit of the Commonwealth, this debt receives the highest (AAA) rating from the three rating agencies (Moodys, S & P and Fitch)

Virginia Constitution

- Section 9(d)
  - Authorized by the General Assembly
  - Does not provide Full Faith and Credit
    - Rated as AA debt but actual interest rate has been very close to AAA-rated debt in recent years
    - Repaid from both GF and NGF including auxiliary enterprises and local governments
  - Issued by Commonwealth agencies, institutions and authorities. For example,
    - Virginia College Building Authority (VCBA)
    - Virginia Public Building Authority (VPBA)
    - Commonwealth Transportation Board
    - Virginia Housing Development Authority

Debt Limitations

- Constitution sets limits for 9(a), 9(b) and 9(c) debt
- 9(b) GO debt limits:
  - Total 9(b) GO debt is limited to approximately 115% of average annual income tax and sales tax revenues of prior three fiscal years
  - General Assembly can only authorize up to 25% of the total 9(b) GO limit over a four-year period
  - Debt must mature at the lower of either 30 years or useful life of the project
  - Debt payments are structures with level principal
- 9(c) debt is limited to the same 115% of average annual income tax and sales tax revenues of prior three fiscal years
- 9(d) debt technically has no limitations placed on it by the Virginia Constitution

Commonwealth Policy on Debt Capacity

- In the early 1990s the Commonwealth developed its current debt policy
  - 1990: Appropriation Act required development of a plan for the coordination of the Commonwealth's borrowing
  - 1991: Executive Order 38 established the Debt Capacity Advisory Committee (DCAC)
  - 1994: DCAC statutorily established (Chapter 43, 1994 Acts of Assembly)
- DCAC established the policy of limiting tax-supported debt to 5% of revenues
  - Debt service payments are made or ultimately pledged to be made from general funds
  - Corresponds to rating agency definition
- In 2010, the DCAC retained the 5% limit but presents capacity using the ten-year average capacity ("smoothing" method)
  - Debt capacity was linked with the new six-year capital outlay planning process
  - All three rating agencies viewed the changes as a positive debt management practice

Debt Capacity Advisory Committee

- Comprised of:
  - Secretary of Finance
  - State Treasurer
  - DPB Director
  - Auditor of Public Accounts
  - JLARC Director
  - Two citizen members appointed by the Governor
  - State Comptroller
  - Staff Directors for House Appropriations and Senate Finance Committees
- Committee annually reviews Commonwealth's tax-supported debt and submits to the Governor and to the General Assembly an <u>advisory, non-binding estimate</u> of the maximum amount of new tax-supported debt that prudently may be authorized for the next biennium

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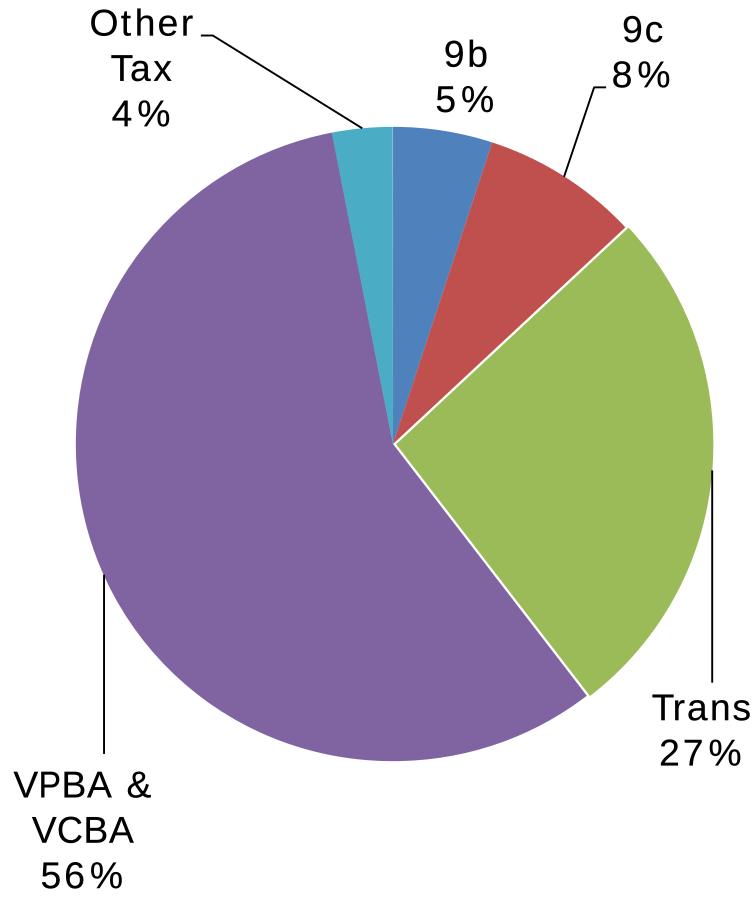
Commonwealth Debt Capacity
DCAC Model

- DCAC Model using the following assumptions over a ten-year planning horizon:
  - Actual debt service on all issued tax-supported debt including capital leases and regional jails
  - Currently authorized but not yet issued tax-supported debt
  - 20-year bonds with level debt service payments except for 9(b) which assumes level principal
  - Blended revenues which include general fund, state revenues in the TTF, & ABC profit transfers
    - Official forecasts excluding Lottery funds
    - TTF revenues do not include Highway Maintenance & Operating Funds, Federal grants, or toll revenues
  - Interest rates for all GO debt is based on the <u>**Bond Buyer 11 Bond Index**</u>
    - 9(d) debt assumed at 25 basis points higher

Current Outstanding Tax-Supported Debt as of June 30, 2016

- Total outstanding tax-supported debt in the debt capacity model is about $11.3 billion
- Tax-supported debt is where the debt service payment is made or ultimately pledged to be made from general government funds & corresponds to the rating agency definitions



Source: Debt Capacity Advisory Committee

Debt Authorized but Not Issued

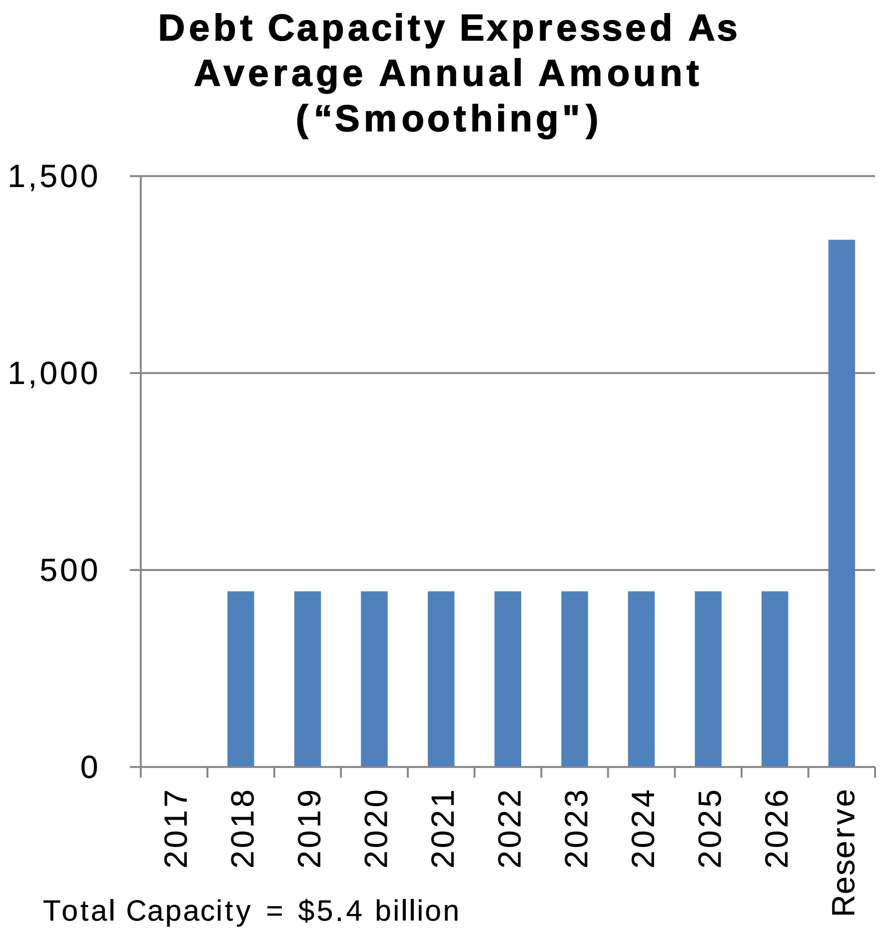
as of December 2016

- As of December 2016, there was approximately $5.3 billion in all forms of tax-supported debt authorized but not yet issued
  - $3.5 billion in Virginia Public Building Authority (VPBA) & Virginia College Building Authority (VCBA) debt
    - This reflects the significant investment made in the 2016 Session
    - This includes about $169 million of HEETF equipment allocations and project equipment
  - About 35% of the debt in pipeline is transportation related
    - $887.3 million in 9(d) transportation bonds
    - $595.7 million for Route 58
    - $24.7 million No. Va. Transportation District Program
    - $350.0 million in VPBA bonds for Port Authority expansion

DCAC Model Results

December 2016

- The chart on the right shows the ten-year debt capacity under the “smoothing” approach adopted by the DCAC
- Annual debt capacity is about $446 million per year
- Total debt capacity is $5.4 billion over the ten-year period which includes holding $1.3 billion the total capacity in reserve
- This assumes all previously authorized debt, including the 2016 Session, as part of the calculation
- Debt capacity is impacted by changes in revenue and interest rates
  - $100 million change in revenue per year impacts the debt capacity by about $6.0 million per year
  - Interest rate changes of 100 basis points can impact the debt capacity by about $60 million



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Net Tax-Supported Debt as Percent of State Domestic Product

- According to the Moody's 2017 State Debt Medians Report, since 2015, Virginia's NTSD as percent of State GDP has ranged between about 2.49% and 2.60%
  - That places Virginia about 20^{th} in the nation over those three years
- The average of all states has ranged between 2.64% and 2.74% over that same period

Net Tax-Supported Debt as Percent of Personal Income and Per Capita

- According to the Moody’s 2017 State Debt Medians Report, Virginia’s NTSD as percent of Personal Income is 2.9%
  - That places Virginia about 20th or 21st in the nation
  - The average of all states is 3.0%
- Virginia’s NTSD Per Capita is $1,486 or 19th in the nation
  - The average per capita NTSD is $1,473

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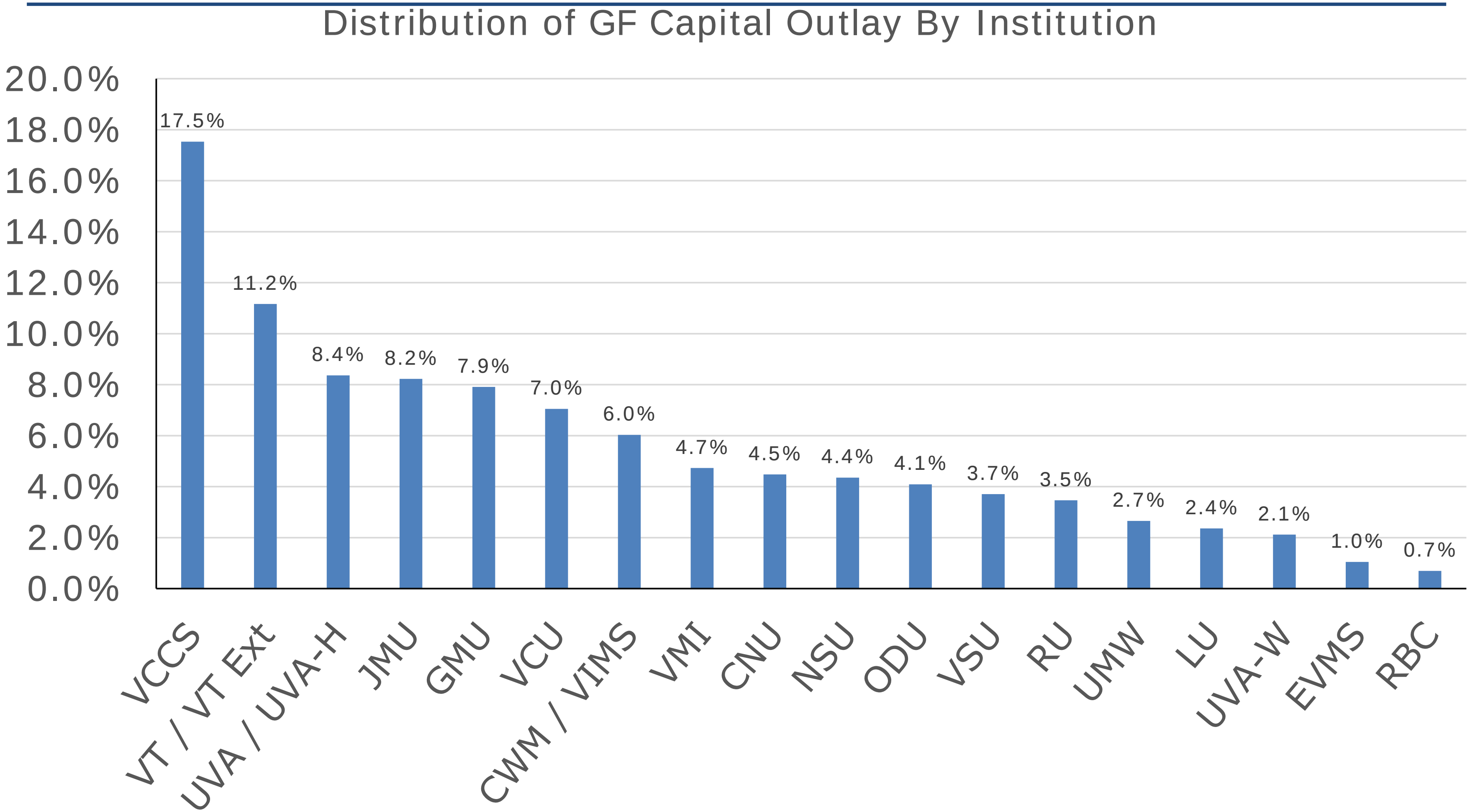
Higher Education Capital Outlay History 2002 to 2018

- Colleges and Universities have spent almost $12 billion from **<u>all fund sources</u>** for capital projects including capital maintenance reserve since 2002
  - That is an average of $700 million per year
  - Represents about 72% of all capital spending in Virginia
  - General fund & GF-bonds funded about 52% or about $6.2 billion of all higher education capital including maintenance reserve
- E & G projects for new construction, renovation and improvements to instruction, research & admin space comprise about 58% of the total capital spending since 2002
  - General fund & GF-supported bonds funded almost 80% of those projects
- Auxiliary Enterprise projects comprise about 31% of the total capital spending, Capital Maintenance Reserve about 5.4%, Property Acquisitions about 2.7% and Other (primarily UVA Hospital) about 2.4%

Higher Education Capital Outlay History
2002 to 2018



Rest of State Government Capital Outlay History 2002 to 2018

- The remaining areas of state government have spent about $4.7 billion from all fund sources for capital projects including capital maintenance reserve since 2002
  - This represents about 28% of all capital spending
  - This excludes Highway, Rail & Transit in Transportation
- Projects for new construction, renovation and improvements comprise about 86% of the total capital spending since 2002
  - General fund & GF-supported bonds funded almost 63% of those projects
  - NGF, primarily driven by Port Authority, funded about 26% and Federal funds about 11%
- Capital Maintenance Reserve projects comprise about 8% of the total capital spending and Property Acquisitions about 6%

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Issues for the 2018-2020 Biennium

- 2016 Capital Program
  - 21 projects already approved for planning
  - Estimated project values based on previous agency requests total about $800 million from all fund sources
    - Detailed planning and BCOM review will result in a more refined estimate
- Capital maintenance reserve
  - Significant deferred maintenance requirements across state government
  - Major building systems are in need of repair and replacement
- Emergency projects
  - Mainly building systems related to HVAC, roofs and electrical & mechanical systems such as:
    - DOC heating & mechanical systems at Red Onion & Sussex
    - Life Safety Repairs in DBHDS
- Project supplements
  - Evidence of increased pricing in recent bids