



# **Rating Criteria, Pension Analysis and Revenue Diversity**

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# Overview

- Four basic factors in tax-backed credit analysis
- Role of pensions in credit analysis
- How does revenue diversity affect a credit profile?

# Debt

- Affordability / debt service coverage
- Exposure to short-term debt, variable-rate debt, derivatives, etc.
- Future capital needs
- Pension & OPEB



# Pension / OPEB Liabilities

Not directly included in an issuer's debt ratios.

OPEBs are legally softer obligations and in most cases, subject to modification by the government.

Focus of pension analysis:

- Magnitude of unfunded actuarial accrued liability (UAAL)
- Funded ratio
- Actuarial and other assumptions
- Measures of affordability

# Pension / OPEB Liabilities

## Credit positives:

- Well-funded pension plans
- Consistent funding of actuarially determined annually required contribution (ARC)
- Effective efforts to reduce liability over time

## Credit concerns:

- High or increasing unfunded liability
- Annual contributions below the ARC
- Limited ability to modify future entitlements

# Economy

- Depth and breadth of employment base
- Education & income levels
- Quality of life attraction
- Tax base composition



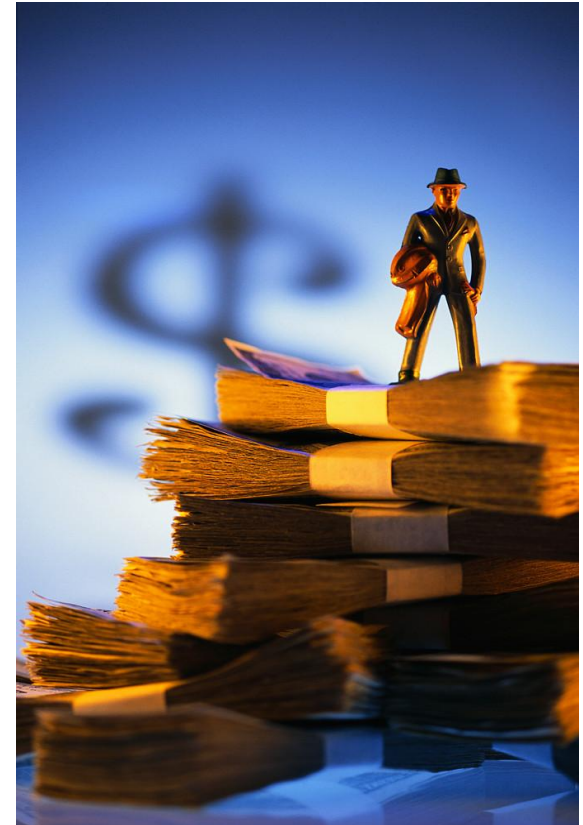
# Management

- Institutionalized and Prudent Policies
- Budget Practices
- Clear Vision
- Ability to Adapt



# Finances

- Revenue and expense composition and trends
- Structurally balanced operations
- Liquidity / cash flow
- Prudent unrestricted reserves
- Contingency planning
- Investment policies and practices





# Revenue Diversity and Volatility

- Property Taxes
  - Predictable revenue source
  - Sound collection rates in Virginia
  - Stronger wealth indicators = Greater affordability
  - Politically difficult to adjust levy
  - Charter caps

# Revenue Diversity and Volatility

- Economically Sensitive Revenues (i.e. sales or hotel taxes)
  - Captures economic activity
  - More politically achievable
  - Less predictable
  - Impacted by economic or weather related events

# References

- Tax-Supported Rating Criteria, August 15, 2011
- U.S. Local Government Tax-Supported Rating Criteria, August 15, 2011
- Enhancing the Analysis of U.S. State and Local Government Pension Obligations, February 17, 2011
- The Reporting of U.S. State and Local Government Pension Obligations, February 23, 2011
- Improving Comparability of State Liabilities: Combined State Debt and Pension Metric, March 28, 2012

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