

# Financial Status Report Focus on City Reserves

City of Petersburg, Virginia



July 21, 2020



# Topics to be Addressed

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- Background.
- Why Unassigned Fund Balance (or “Reserves”) Matters.
- History of the City of Petersburg’s Unassigned Fund Balance (Reserve) levels.
- Staff Recommended Policy
- Fund Balance Comparatives.
- Credit Rating Agency/GFOA Commentary.
- Next Steps.



# Background

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- The City of Petersburg (The “City”) established a series of Financial Policy Guidelines which included Unassigned Fund Balance (or “Reserve”) levels in 2014.
- Certain of these policies in particular, Unassigned Fund Balance (Reserve) levels were not adhered to in the subsequent years until FY2017.
- The policies also called for a structurally balanced budget wherein recurring revenues are sufficient to meet all recurring expenditures.
- Over the past 3 years, the City fiscal health has rebounded and as such Unassigned Fund Balance (Reserve) levels have dramatically improved.
- Under the current administration the City has had 2 Credit Rating Upgrades with the goal of additional upgrades to come.
- As discussed further herein, the City is proposing certain enhancements to strengthen its Unassigned Fund Balance (Reserve) levels so that its Credit Rating will continue to improve.



# Why Unassigned Fund Balance Matters

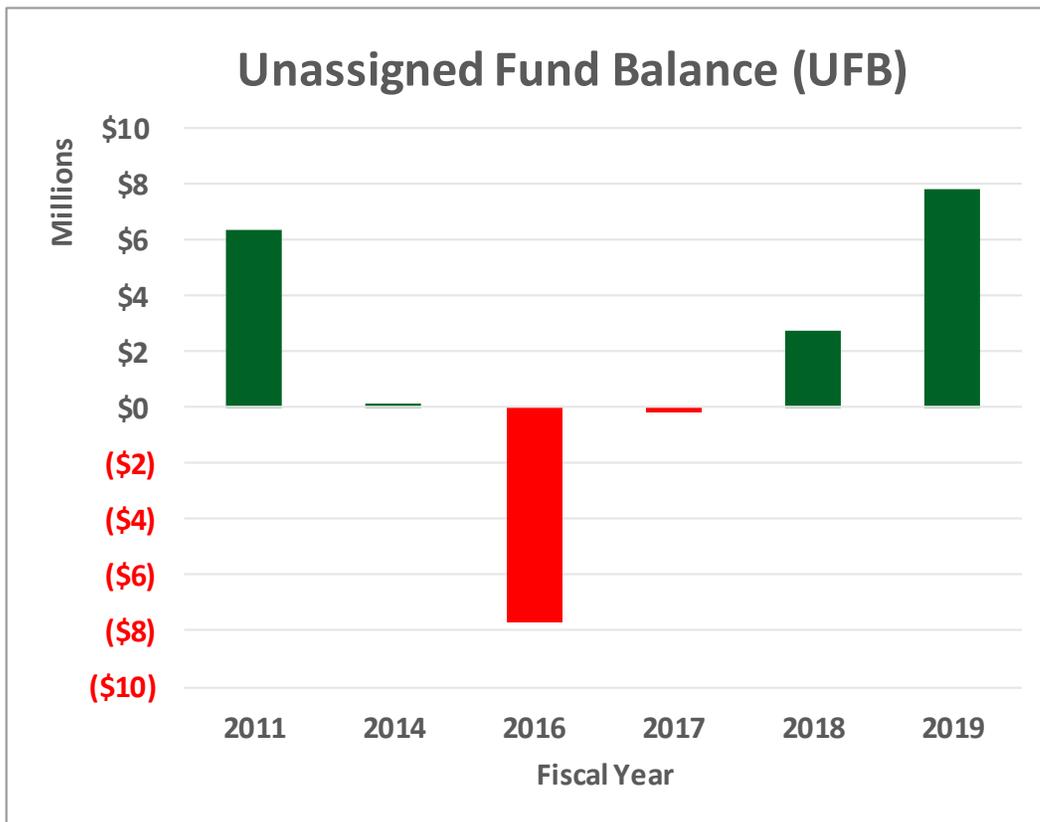
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- Allows the City to avoid Tax Anticipation Notes (“TANs”) /Revenue Anticipation Notes (“RANs”), which are costly.
- Enables the City to earn interest income, which helps the General Fund and alleviates pressure on tax rate(s).
- Serves as the single most important factor for credit ratings.
- Enables the City to borrow at lower interest rates, which in turn, provides for lower debt service and potential refunding opportunities for debt service savings.
- Excess Unassigned Fund Balance can be used for one-time capital investment and economic development purposes.



# History of Petersburg's Unassigned Fund Balance

- Over the past 3 years, the City fiscal health has rebounded and as such Unassigned Fund Balance (Reserve) levels have dramatically improved.



FY	UFB Amount (\$mil)	UFB % of Expenditures	S&P Credit Rating
2011	\$6.4	7.9%	A+
2014	\$0.2	0.2%	BBB
2016	(\$7.7)	(10.8%)	BB
2017	(\$0.1)	(0.2%)	BB
2018	\$2.8	3.8%	BB+
2019	\$7.9	10.3%	BBB-



# Existing Unassigned Fund Balance Policy

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- Key Tenets - Unassigned Fund Balance shall:
  - Be comprised of liquid cash and investments.
  - Consist of a sufficient amount to meet the City’s cash flow needs and allow the City to avoid the use of TANs/RANs (i.e. cash flow borrowing).
  - Allow for a margin of safety against unforeseen expenditures.
  - Not be used for annual recurring expenditures, except in the event of unforeseen emergency circumstances.
  
- Existing Unassigned Fund Balance target level/approach to funding:
  - The City shall target an Annual Budgeted Amount of a minimum of \$750,000 each year toward rebuilding the Unassigned Fund Balance until it reaches an amount that is sufficient to eliminate the need for annual RANs (the “Minimum Initial Target”).
    - To the extent the City has additional operating surplus after all expenditures and the Annual Budgeted Amount, the City shall apply a minimum of 50% toward the Unassigned Fund Balance.
  - After the Minimum Initial Target is reached, the City shall plan to increase Unassigned Fund Balance so that it is not less than 10% of its General Fund and School Component Unit Operating Expenditures.



# Staff Recommended Unassigned Fund Balance Policy

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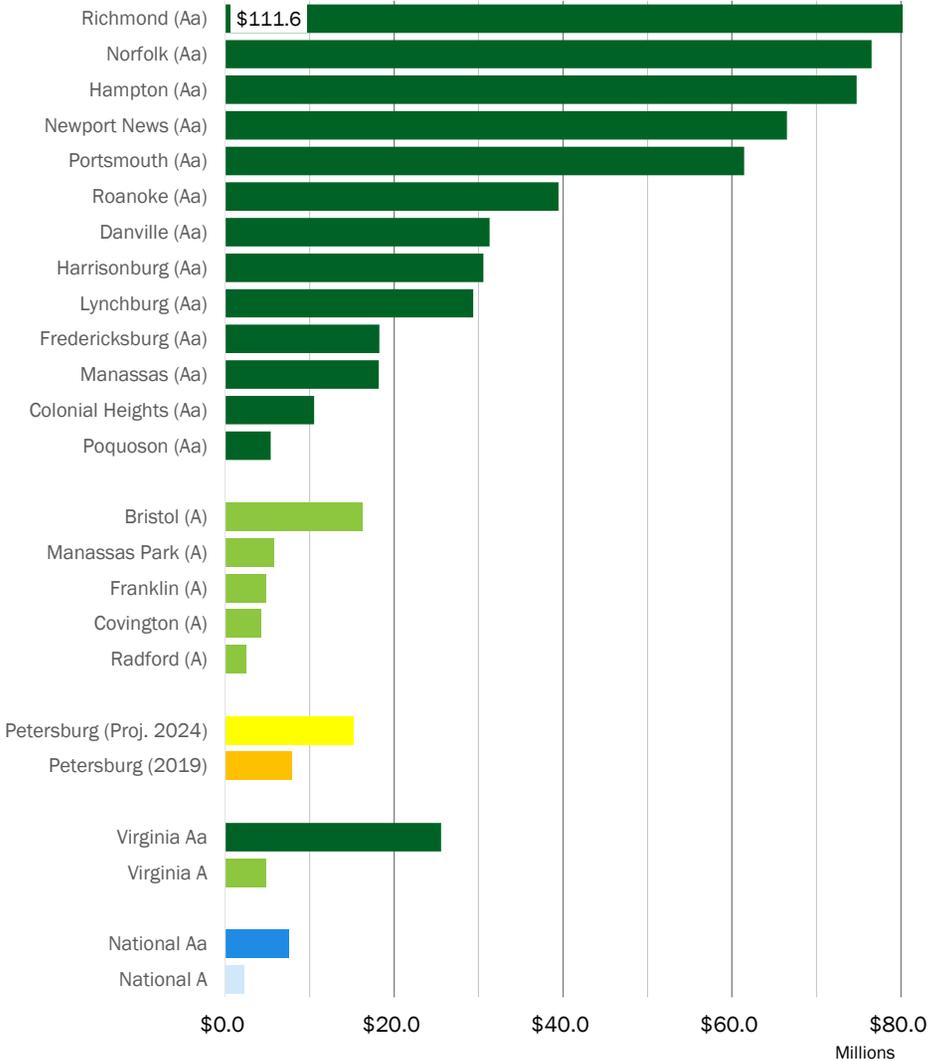
- Staff Recommended Unassigned Fund Balance target level/approach to funding:
  - The City shall have a Minimum Initial Target Unassigned Fund Balance that represents 30 days of its General Fund Operating Expenditures.
    - The budget will include \$1 Million annually toward the Unassigned Fund Balance; Upon reaching the Minimum Initial Target the City shall budget \$500,000 toward Fund Balance Replenishment and \$500,000 toward Pay-Go Capital Projects.
  - Within 3 years following the City meeting the Minimum Initial Target, the City shall increase the Unassigned Fund Balance to a level that represents 60 days of its General Fund Operating Expenditures.



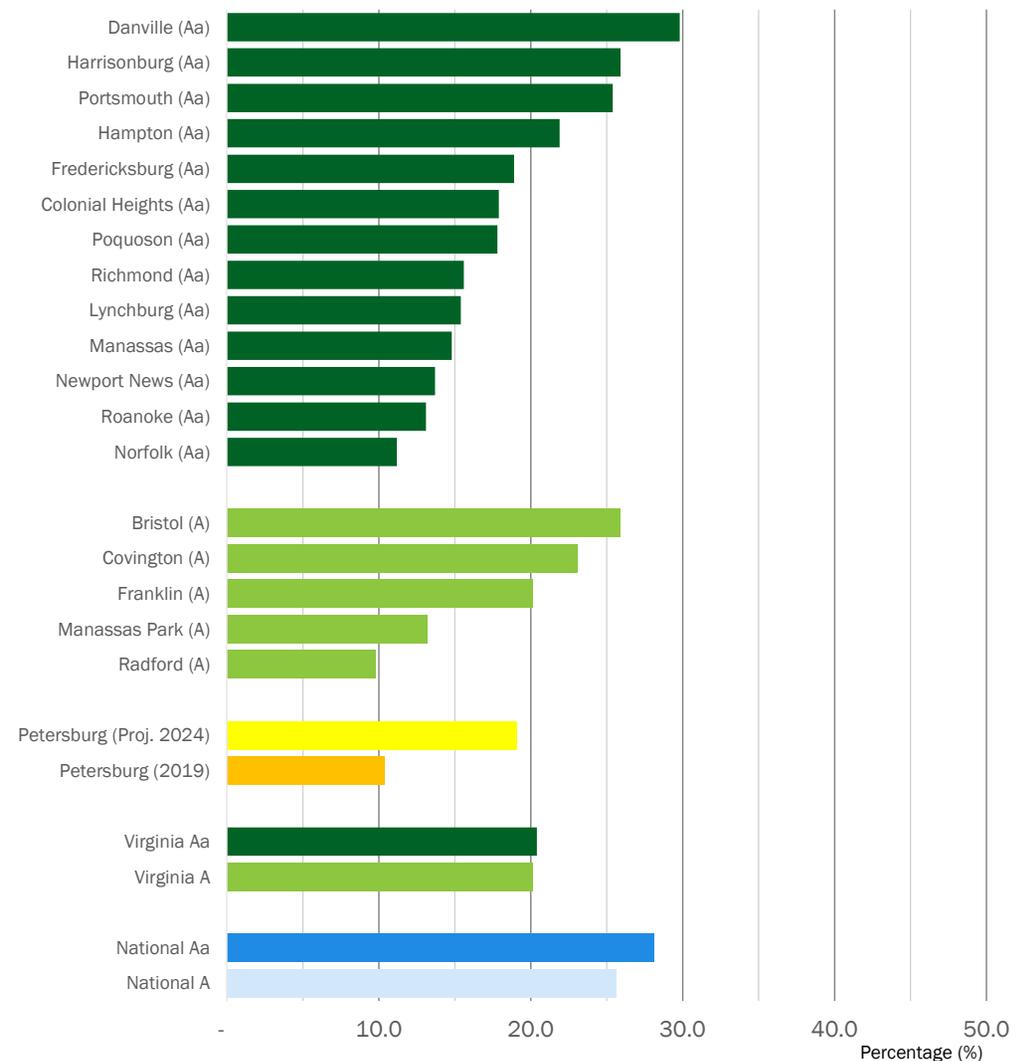
# Peer Comparison | Unassigned Fund Balance

- The City's FY 2019 and Projected FY 2024 Unassigned Fund Balance levels are compared with selected "Aa" and "A" rated cities below.

Unassigned Fund Balance (\$)



Unassigned Fund Balance as a % of General Fund Revenues



# Rating Agency Methodology | Moody's



## Moody's Rating Methodology

Category	Rating Percentage	Short-Term Control	Long Term Control
1. Economy / Tax Base	30%		✓
2. Finances	30%	✓	✓
3. Management	20%	✓	✓
4. Debt / Pensions	20%	✓	✓

- Finances (i.e. Fund/Cash Balances and trends) is the single most important criteria from the Credit Rating Agency's perspective and comprise 30% of the credit rating evaluation.

# Rating Agency Methodology Updates | S&P



## S&P Rating Methodology

Category	Rating Percentage	Short-Term Control	Long Term Control
1. Institutional Framework	10%		✓
2. Economy	30%		✓
3. Management	20%	✓	✓
4. Budgetary Flexibility	10%	✓	✓
5. Budgetary Performance	10%	✓	✓
6. Liquidity	10%	✓	✓
7. Debt and Contingent Liabilities	10%	✓	✓

- Budgetary Flexibility/Liquidity (i.e. Fund/Cash Balances) are collectively 20% of the credit rating evaluation and are critical factors from the Credit Rating Agency's perspective.



# GFOA Commentary on Fund Balance (Reserves)

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- GFOA recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund.
  
- The adequacy of unrestricted fund balance in the general fund should be assessed based upon a government's own specific circumstances.
  
- GFOA recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures.
  
- Furthermore, a government's particular situation often may require a level of unrestricted fund balance in the general fund significantly in excess of this recommended minimum level.
  - Such measures should be applied within the context of long-term forecasting.



# Next Steps

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- City Council approval of revised formal Financial Policy Guidelines.
- City and Davenport to work toward implementing RAN, including evaluation of cash flow projections and estimated RAN size, with the goal of RAN funding by October 2020.
- City and Davenport to continue evaluation of the Utility Enterprise Fund to include an updated recommendation for the Utility's capital funding needs.
- Heading into the 2<sup>nd</sup> half of FY 2021, provide a strategic recommendation for capital expenditures and a borrowing strategy with necessary user rates and charges so as to maintain the self-supporting operations of the Utility Enterprise Fund in keeping with industry-wide "Best Practices".

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