DEBT CAPACITY ADVISORY COMMITTEE
COMMONWEALTH OF VIRGINIA
October 8, 2014

10:30 A.M.
TREASURY BOARD CONFERENCE ROOM
James Monroe Building
101 North 14th Street, 3rd Floor
Richmond, Virginia 23219

Members Present:	Richard D. Brown, Chairman William K. Butler Elizabeth B. Daley Manju S. Ganeriwala Martha S. Mavredes Ronald L. Tillett Daniel S. Timberlake Robert P. Vaughn David A. Von Moll
Members Absent:	Harold E. Greer
Others Present:	Evelyn R. Whitley, Department of the Treasury Bradley L. Jones, Department of the Treasury Sherwanda Cawthorn, Department of the Treasury Janet A. Aylor, Deputy Secretary of Finance Neil Miller, Deputy Secretary of Finance Jason Powell, Senate Finance Committee Tony Maggio, House Appropriations Committee Chriss Whyte, Vectre Corporation Jeanine Black, Department of the Treasury Leslie English, Department of the Treasury Michael Walsh, Department of the Treasury

Call to Order and Opening Remarks

Chairman Brown called the meeting to order at 10:35 a.m. and welcomed everyone to the Debt Capacity Advisory Committee ("DCAC" or the "Committee") meeting.

Public Comment Period and Approval of Minutes

Chairman Brown asked if there were any public comments. Hearing none, he asked the Committee for a motion to approve the minutes of the December 2013 meeting. Ms. Ganeriwala made a motion to approve the minutes. The motion was seconded by Mr. Vaughn and it was approved unanimously.

Discussion of the Commonwealth's August 2014 Revenue Forecast

Chairman Brown gave the Committee an overview of the fiscal year 2014 revenue collection results and the August 2014 revised revenue forecast. Committee members were provided with a handout (Exhibit 1), which contained four pages from his August 15, 2014 presentation to the Joint Money Committees. Chairman Brown discussed two major causes for the decrease in revenues, withholding and non-withholding revenue collections. He explained that withholding revenues declined 0.6 percent, or $66 million, in 2014 compared to the prior year. However, the 2014 revenue shortfall totaling $437.8 million was mainly due to a decrease of 13.7%, or $401.1 million, in non-withholding revenue collections. Chairman Brown further explained that the decrease in non-withholding revenue is related to capital gains and the federal tax changes that went into effect in calendar year 2013. As for withholding tax revenues, Chairman Brown explained Virginia job growth was also an issue, mainly in the changing composition of the labor force. Chairman Brown explained there were losses of professional business category jobs in Northern Virginia and the Tidewater area. He added that with those losses, Virginia needs to grow exponentially in education, leisure, and retail to make up for those high wage jobs. Chairman Brown then directed the Committee to the remaining pages of the handout. The expectations of the Joint Advisory Board of Economists ("JABE") were mentioned as a comparison to what was actually used in the official forecast. Chairman Brown then briefly reviewed the results of the August 2014 General Fund forecast for fiscal years 2015 and 2016, which revealed a $2 billion revenue shortfall for the two year period.

Chairman Brown asked if there were any questions. Hearing none he requested Treasury staff provide a review of the model results.

Staff Review of Model Results Incorporating August 2014 Revenue Forecast

Mr. Jones proceeded to review the model results. Before reviewing the October 2014 results, Mr. Jones reminded the Committee what the model results looked like in December 2013. A handout of the 2013 base model (Exhibit 2) and the 2013 average model (Exhibit 3) were provided to the Committee. Mr. Jones explained that based on the model, $560 million was estimated to be the capacity and that amount was included in the letter to the Governor and General Assembly. He added that the Committee's letter cautioned that interest rates are anticipated to rise and this will cause a decline in capacity. Mr. Jones reminded the Committee that when $560 million was applied to the average model solution, debt service as a percentage of revenues exceeded the 5% threshold in five years with a peak of 5.42% in 2017. Mr. Jones asked if there were any questions about the report adopted in December.

Following the discussion of the December 2013 model, a handout of the October 2014 base model (Exhibit 4) and the October 2014 average model (Exhibit 5) were provided to the Committee. Mr. Jones explained that the October model provides the Committee with an estimate of capacity given the General Fund reforecast and the October model result will likely be an early indicator of the result to be presented in December's report. He continued that December's model will have changes in the revenue forecast, as the General Fund forecast is subject to additional changes and the Transportation Trust Fund ("TTF") and Healthcare forecasts have to be updated from December 2013. Additionally, interest rate assumptions may change, although it is expected that the rate will be similar to last year's model rate of 4.17%. Mr. Jones stated that there will be changes to the issuance assumptions and that capital lease amounts will be revised once the 2014 Comprehensive Annual Financial Report ("CAFR") is released.

Mr. Vaughn asked if there had been any updates to the authorized but unissued debt and whether the newly authorized debt was included in the issuance assumptions. Chairman Brown confirmed that the October 2014 model includes all authorized debt, but that the issuance assumptions will be revised between now and December. Mr. Vaughn then asked how the recently authorized $300 million VPBA project is taken into account. Ms. Whitley said it is included in the model's authorized debt but it is not assumed to be issued this year. Chairman Brown then reiterated that revenue forecasts will be updated for the Governor's final budget in December and the model will also be updated with interest rates and revised issuance assumptions.

Mr. Tillett asked staff to provide an indication of how much interest rates might change and impact the model result and how any new issuances might also impact the model result between now and December. Neither Mr. Jones nor Ms. Whitley could anticipate the exact change interest rates might cause, but they speculated the change would be minor given the interest rate factor is based on a 12-quarter average and rates have been low throughout the prior period and this year. Ms. Whitley continued by stating that issuance assumptions may get spread out once draw schedules are reviewed. Mr. Tillett then asked if we were to issue any of the authorized debt before December would the issuance be at a lower rate than what was built in the model, thus providing more capacity? Mr. Jones confirmed that the rate achieved on the issuance would possibly be lower than the model rate, but informed the Committee that it would have no change on the current year's model since the model only considers actual debt service for debt issued through June of the prior fiscal year and the rest is modeled. Chairman Brown stated that other than the few items mentioned, the Committee should not see significant changes in December. Mr. Butler asked if the current model is a worst case scenario and should we see things look a little better in December. Chairman Brown stated all new debt and the revenue reforecast have been accounted for, so that statement is probably true.

Mr. Jones proceeded to review the October 2014 model results and said the October model has capacity of $428 million. He then reviewed the average solution which incorporates $428 million per year. He explained that the average model solution projects debt service as a percentage of blended revenues to exceed the 5% threshold in 7 of years modeled, with a peak of 5.71% in 2017. Ms. Daley asked for confirmation that according to the base model and not the average, no additional debt could be issued in 2016. Chairman Brown confirmed the statement. Ms. Daley asked when the average model was adopted were any types of caps on exceeding the 5%

threshold adopted? Chairman Brown stated no caps were established. Mr. Jones asked if there were any further questions; hearing none, Mr. Jones asked Secretary Brown to continue with any additional DCAC business.

Chairman Brown asked if there were any other actions to be taken. It was discussed that the meeting was informational for the Committee and actions would wait until the December recommendation. Mr. Tillett asked, since the new numbers take capacity above 5% a little more than before, would this be a concern for the rating agencies? He added that he noticed Virginia received a little push back from rating agencies in a recent ratings report. He continued, does the amount of time over 5% give any concerns or was debt capacity even discussed with rating agencies? Chairman Brown replied that in his discussions with rating agencies, they were more focused on Virginia's economy and the revenue adjustments. He added that there were no questions from the rating agencies regarding debt capacity. Mr. Tillett then commented that while debt capacity has declined, interest rates remain at historical lows and this is a great time for issuers to move forward with projects at low interest rates. Mr. Vaughn invited a member of the public, Tony Maggio, to address the Committee. Mr. Maggio commented that while the Commitee has focused on the 5% threshold being exceeded under the average base model, the level and number of years 5% is exceeded is based on the assumption that $428 million is actually authorized and issued each year. He continued his comments by stating that actual debt service on debt issued through June 30, 2014 doesn't cause the 5% threshold to be exceeded. He stated that only when authorized and unissued debt is included is the 5% threshold exceeded prior to adding on newly assumed capacity. He concluded his comments by stating the level and number of years 5% would potentially be exceeded is dependent on issuance assumptions regarding authorized and unissued debt. Chairman Brown acknowledged there is still a large amount of authorized and unissued debt and informed the Committee that issuance assumptions will be reviewed and revised before the December meeting.

Other Business

Chairman Brown asked the Committee members if there was anything else that needed to be brought before the group.

With no further business, the meeting adjourned at 11:05 a.m.

Exhibits may be obtained by contacting the Department of Treasury at (804) 225-2142.