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**Summary:**

## Virginia Public School Authority Prince William County; Appropriations; General Obligation

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## Summary:

# Virginia Public School Authority Prince William County; Appropriations; General Obligation

### Credit Profile

US\$89.885 mil spl oblig sch fing bnds (Prince William Cnty) ser 2020 dtd 10/15/2020 due 10/01/2040		
<i>Long Term Rating</i>	AAA/Stable	New
US\$46.07 mil facs rev and rfdg bnds (Prince William Cnty) ser 2020A dtd 10/29/2020 due 10/01/2040		
<i>Long Term Rating</i>	AA+/Stable	New

## Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to the Virginia Public School Authority's series 2020 special obligation school financing bonds issued on behalf of Prince William County. At the same time, S&P Global Ratings assigned its 'AA+' long term rating to the Industrial Development Authority of the County of Prince William's series 2020A facilities revenue and refunding bonds (court facilities projects) based on the county's appropriation obligation. The outlook is stable.

The series 2020 special obligation bonds are an obligation of the county and secured by revenue it collects from ad valorem taxes, which are unlimited as to rate or amount. Bond proceeds will fund various capital school improvement projects.

The series 2020A facilities revenue and refunding bonds are secured by basic payments equal to debt service made by Prince William County under the installment purchase contract with the authority. Although basic payments are subject to annual appropriation, the county pledges its best effort to seek the appropriation's inclusion in the annual budget. Proceeds will fund improvements to certain county facilities and refund certain maturities outstanding to lower overall debt service costs estimated at 10.3% of the refunded par amount.

### Credit overview

Prince William County's sophisticated management team has closely monitored the effect of stay-at-home orders to control the community spread of COVID-19 on its operations and factored further economic weakness stemming from the recession into its budget for fiscal 2021. We believe that the management team's robust planning initiatives and well-embedded long-term financial forecasting underpins the 'AAA' rating and will sustain its credit quality despite the economic disruption underway and more broadly outlined in S&P Global Economics' macroeconomic outlook detailed in the report "The U.S. Faces A Longer And Slower Climb From The Bottom," published June 25, 2020 on RatingsDirect.

The stable outlook reflects our view of the county's economic diversity that benefits from its proximity to Washington,

D.C., and the affordability of the area as compared with its neighbors located a little closer to the district. Although the population growth has led to substantial capital needs, we believe the county's overall fixed costs (including debt service, pension, and other postemployment benefits) remain manageable at 14.2% of total governmental expenditures in fiscal 2019. We believe management's conservative financial assumptions and spending discipline will result in ongoing budgetary stability and maintenance of very strong reserves.

Prince William County's GO bonds are eligible to be rated above the sovereign because we believe the county can maintain better credit characteristics than the U.S. in a stress scenario. The county's revenue is predominantly locally derived, with most of general fund revenue derived from local property taxes. (See "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions," published Nov. 19, 2013.)

The rating reflects our assessment of the county's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area;
- Very strong management, with strong financial policies and practices under our financial management assessment methodology;
- Adequate budgetary performance, with a surplus of 1.4% in the general fund but a slight operating deficit at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 19% of operating expenditures;
- Very strong liquidity, with total government available cash at 63% of total governmental fund expenditures and 5.9x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 10.6% of expenditures and net direct debt that is 87.3% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value and rapid amortization, with 71% of debt scheduled to be retired in 10 years; and
- Very strong institutional framework score.

### **Environmental, social, and governance factors**

We believe the county's governance is above that of the sector given the long-term planning initiatives that management undertakes to mitigate risk to its financial operations and infrastructure, particularly when facing a period of economic weakness. Furthermore, in our view, social risks are below those of the sector and as compared with Northern Virginia peers given the demographic trends and housing affordability that we believe support the county's economic development efforts and tax base expansion. Finally, we evaluated the county's environmental risks and believe they are in line with the sector.

## **Stable Outlook**

### **Downside scenario**

In the unlikely event that Prince William County were to utilize reserves to bridge a long period of imbalance between revenue and expenditures leading to substantially lower flexibility, we could lower the rating.

## **Credit Opinion**

### **Very strong economy**

We consider the county's economy very strong. Prince William County, with an estimated population of 465,498, is located in the Washington-Arlington-Alexandria metropolitan statistical area, which we consider broad and diverse. The county has a projected per capita effective buying income of 130% of the national level and per capita market value of \$145,249. Overall, the county's market value grew by 6.0% over the past year to \$67.6 billion in 2019.

Prince William County is located in northern Virginia about 25 miles southwest of Washington, D.C. The region's economic expansion has spurred significant population growth, with the county becoming the commonwealth's second-most populous with generally a more affordable cost of living than some of its neighboring counties. Population increased 44% from 2000 to 2010 according to the U.S. Census with current projections showing a subsequent increase of 16.3% to the current 467,478. We understand that population is projected to reach 529,600 by 2030 as land within the county transitions from rural and agricultural to suburban and residential.

The economic strength is derived from the stabilizing military component from the Marine Corps Base Quantico and Fort Belvoir, located just outside the county's limits. The installations have gained about 30,000 relocated personnel as a result of the U.S. military's Base Realignment and Closure in 2005. The realignment also attracted several defense contractors to the county. Nevertheless, Prince William County continues to diversify its employment base with recent development focused on data centers, high-tech, and bio-tech industries as well as advanced logistics and manufacturing facilities.

In response to COVID-19, the county is supporting its local businesses through various programs including direct financial assistance, marketing campaigns, and matching employers with resources to prepare for reopening and keeping employees safe. Furthermore, a task force consisting of industry and business leaders was created to accelerate recovery. As a result, despite the potential for a temporary deceleration of the county's economic growth, we believe over the long term the county's economy will remain very strong.

### **Very strong management**

We view the county's management as very strong, with strong financial policies and practices under our financial management assessment methodology, indicating our view that financial practices are strong, well embedded, and likely sustainable.

In 1988, the county adopted the Principles of Sound Financial Management (PSFM), which guide its financial management practices and policies. The PSFM is regularly updated and requires quarterly reporting of budget-to-actual results to the board of supervisors. Furthermore, the principles outline a five-year budget plan, annually adopted by the board of county supervisors and integrated with the capital improvement plan (CIP). The five-year budget plan must be balanced in all years without appropriating the unassigned general fund balance. Other features of the plan include an annually updated six-year CIP that identifies all funding sources. Furthermore, a formal debt management policy delineates limiting debt service for tax-supported debt to 10% of annual revenue and total issued debt to 3% of net assessed value. The county's formal investment policy mandates quarterly reporting to the governing body and a formal fund balance policy requiring maintenance of the unassigned general fund balance at

7.5% of general fund revenue, a revenue stabilization fund at 2.0% of general fund revenue, and a capital reserve equal to 2.0% of current capital projects fund appropriations in the CIP.

In addition, the county has enacted various resiliency and preparedness measures, including investment in technology modernization as well cybersecurity prevention and remediation. In addition to technology modernization capital expenditures, cybersecurity prevention includes duplicate infrastructure, migration of data redundancy to the cloud and off-premise solutions, mandated employee education, robust internal audit testing, and other proprietary security solutions.

### **Adequate budgetary performance**

We reflect Prince William County's budgetary performance as adequate, which takes into consideration the potential budgetary challenges arising from the pandemic and recession and could affect budgetary balance in fiscal 2021, particularly given the uncertainty of the economic fallout. The county had a surplus result in the general fund of 1.4% of expenditures but a slight deficit result across all governmental funds of about 1.0% in fiscal 2019.

We adjust the county's audited results to reflect recurring transfers in and out of the general fund, including some transfers to enterprise funds as well as removing expenditures financed with bond proceeds to fund one-time capital projects.

The county has an excellent history of conservative budgeting and forecasting practices, supported by well-adhered-to fiscal policies. These policies and practices help Prince William County maintain fiscally balanced operations and the ability to fund a substantial amount of one-time expenses on a pay-as-you-go basis. The budget is primarily supported by property taxes (about 85.0%), sales taxes (6.4%), and other taxes (8.8%).

The county ended fiscal 2019 with positive revenue and expenditure variances leading to an operating surplus of \$20 million (1.7% of expenditures) prior to transfers out. Following transfers out of \$67.0 million, including \$43.2 million to capital projects, the operating surplus was \$1.5 million. General positive variances in most revenue categories as well as the county's tight control of expenditures led to the positive result.

Prior to the effects of COVID-19, the county's fiscal 2020 revenue was trending well above budget expectations. However, following the onset of the pandemic, management revisited the revenue forecast and derived alternate optimistic and pessimistic year-end estimates. Despite some weakness in investment income (19.8% below the adopted budget), most revenue collections were above the adopted budget and officials anticipate that general revenue will exceed the forecast by \$10.5 million (or about 1%). Furthermore, despite approximately \$4.9 million spent through June 30, 2020 on the county's COVID-19 response, including purchasing personal protective equipment, cleaning supplies, and technology equipment to ensure the workforce can work remotely, officials report that cost containment measures will lead to expenditure savings of \$17 million for fiscal 2020. In addition, the county received about \$82 million from the state's allocation of Coronavirus Aid, Relief, and Economic Security (CARES) Act money as well as other grant funding, which will cover expenditures and provide resources to support the community and business recovery.

The fiscal 2021 general fund budget totals \$1.3 billion when including the school board transfer, and for a subsequent year does not include an increase to the real estate tax rate. The budget includes other modest fee increases and will

increase the school transfer by \$18.1 million (3.0%). Officials will continue to monitor the effects of COVID-19 and will adjust expenditure controls accordingly to ensure maintenance of reserves and budgetary balance.

### **Very strong budgetary flexibility**

Prince William County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 17.8% of operating expenditures, or \$221.7 million. The available fund balance consists of \$185.3 million (16.2% of expenditures) in the general fund and \$36.4 million (3.2% of expenditures) that is outside the general fund but legally available for operations. Over the past three years, the total available fund balance has remained consistent overall, totaling 20% of expenditures in 2018 and 20% in 2017.

Total available reserves include the assigned and unassigned portions of the general fund balance as well as the committed portion, which contains the revenue stabilization reserve, equal to 2% of general fund revenue, and reserves for capital. In addition, reserves in the fire levy fund are legally available to cover public safety costs in the general fund with board approval. Management also cites a number of other reserve set-asides in its internal services funds, including reserves for health insurance, workers compensation, self-insurance, and intracounty services that total \$66.4 million and that provide additional financial flexibility.

With reserves expected to remain unchanged or increase at fiscal year-end 2020, we believe the county is well positioned to absorb potential revenue loss in fiscal 2021 as a result of the recession. Furthermore, we believe the county's annual transfer to the capital projects fund to cover pay-as-you-go capital spending could be reduced to provide resources to cover operating costs.

### **Very strong liquidity**

In our opinion, Prince William County's liquidity is very strong, with total government available cash at 63% of total governmental fund expenditures and 5.9x governmental debt service in 2019. We believe the county has strong access to external liquidity given its regular issuance of debt over the past 20 years. Management has confirmed it has no contingent liquidity risks from financial instruments with payment provisions that change upon certain events. In addition, the county holds no investments that we deem aggressive. Furthermore, officials have prioritized conservation of cash given the potential for revenue dislocation stemming from the pandemic.

### **Strong debt and contingent liability profile**

In our view, Prince William County's debt and contingent liability profile is strong. Total governmental fund debt service is 10.6% of total governmental fund expenditures, and net direct debt is 87.3% of total governmental fund revenue. Overall net debt is low at 1.7% of market value, and approximately 71% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

Following the transactions, the county will have about \$1.2 billion in net direct debt outstanding. Despite the sizable debt outstanding, the county keeps debt service costs manageable by relying significantly on pay-as-you-go capital spending. In fiscal 2019, the county cash-funded \$30.0 million in capital projects with \$45.8 million in the capital projects fund balance remaining at year end (in excess of the \$12.7 million required by its policy). The fiscal 2019 transfer into the fund was \$13 million, providing ample financial flexibility to continue capital investment despite the potential for lower revenue collections in fiscal 2021.

County voters overwhelmingly approved a referendum in November 2019 totaling \$396 million, consisting of \$355 million for roads/mobility and \$41 million for parks. The county expects to issue the authorized debt incrementally in fiscal years 2022 to 2029. Nevertheless, we do not expect Prince William County's debt profile to materially deteriorate given rapid amortization of existing debt and sizable pay-as-you-go spending.

### **Pension and other postemployment benefit (OPEB) liabilities**

We do not view pension and OPEB liabilities as an immediate source of credit pressure, because required contributions make up a modest 3.6% of total governmental expenditures. If required contributions were to escalate during the next few fiscal years, which we do not expect, we believe the county could easily absorb higher costs as a result of its sizable reserves and other flexibility afforded by its large pay-as-you-go capital program.

As of June 30, 2019, the county participated in the following retirement plans:

- County and school board employees participate in the Virginia Retirement System: 87.6% funded, with a net pension liability of \$159.7 million
- A supplemental pension plan for public safety employees: 101.25% funded, with a net pension asset
- A length-of-service award program for volunteer firefighters: 61.3% funded, with a net pension liability of \$11.5 million. The funded ratio decreased as a result of a change in the discount rate to 3% from 6%, which we view as prudent.
- The county also offers OPEB to its employees, and established a trust fund in 2009 that contained \$87.2 million as of June 30, 2019. As of July 1, 2019 Prince William County's OPEB liability was 61.6% funded with a total liability of \$81 million.

We generally view the assumptions governing the Virginia Retirement System as conservative with a discount rate of 7% and a closed amortization period. The county's contributions nearly met our minimum funding progress level and exceeded our static funding metric, indicating that the county is making good progress meeting its current and future liabilities. As a result, we do not expect plan contributions to change materially over the next couple of years.

### **Very strong institutional framework**

The institutional framework score for Virginia counties is very strong.

## **Related Research**

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2019 Update Of Institutional Framework For U.S. Local Governments

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