ARLINGTON COUNTY, VIRGINIA

County Board Agenda Item
Meeting of October 23, 2010

DATE: October 15, 2010

SUBJECT: Fiscal Year (FY) 2012 Financial Forecast and Budget Guidance

C. M. RECOMMENDATIONS:

1) Receive the County Manager's Budget Forecast for Fiscal Year 2012.

2) Provide budget guidance for Fiscal Year 2012.

ISSUE: Providing guidance to the Manager in developing a spending plan for Fiscal Year 2012 that protects our community values while ensuring our long-term financial sustainability.

SUMMARY: As described in the Manager's September 28, 2010 presentation to the Board, the FY 2012 forecast is better than the one we faced this time last year. Real estate revenues are currently projected to increase slightly at current tax rates, while a number of expense pressures grow. The County and Schools are projecting expense increases for FY 2012, that, when combined with revenue projections, will lead to a budget gap of between $25 and $35 million for FY 2012 were current services maintained.

Current projections rely on incomplete revenue data and preliminary costs estimates. Projections will change as more data are available and further analysis is completed. Cost estimates could increase and revenue projections could decrease, exacerbating the problem; or estimates could also improve. These projections are based on staff's best analysis with limited information.

Closing a gap of this size, after several years of program cuts, will require a thoughtful balancing of tax and fee increases and potential service reductions that will be noticeable to the community.

DISCUSSION:

Revenue Projections

Overall, Arlington revenues are expected to increase $13.8 million above the FY 2011 adopted budget. This growth assumes approximately 2% positive growth in real estate tax revenue due to

County Manager: BMD/GA

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Staff: Mark Schwartz, Director, Department of Management and Finance
Richard Stephenson, Budget Director, Department of Management and Finance

1% assessment appreciation in CY 2011 and 3% assessment appreciation in CY 2012. Other tax and non-tax revenues show slight growth over FY 2011 levels. The County share of the tax and non-tax revenue increase is approximately $8.3 million. The Schools share, based on the current revenue sharing agreement, is $5.5 million. The following table outlines current revenue estimates for FY 2012 projected at this time.

	FY 2011 Adopted Budget (in millions)	**FY 2012 Projected (in millions)**	**% Change Adopted FY11 to Projected FY12**	**$ Change Adopted FY11 to Projected FY12**
LOCAL TAXES				
Real Estate Tax	$505.1	$514.7	1.9%	$9.6
Personal Property	94.0	94.5	0.5%	0.5
Business Tax (BPOL)	59.6	59.6	-	-
Sales Tax	36.4	37.5	3.0%	1.1
Transient Occupancy Tax	21.5	22.1	2.8%	0.6
Meals Tax	29.4	30.3	3.1%	0.9
Other Taxes	35.6	35.8	0.6%	0.2
Sub-total taxes	**$781.6**	**$794.5**	**1.7%**	**$12.9**
NON-TAX REVENUE				
License, Permits & Fees	$9.4	$9.5	1.1%	$0.1
Fines, Interest, Misc.	23.1	23.1	-	-
Charges for Services	44.5	45.3	1.8%	0.8
State	63.2	63.2	-	-
Federal	18.3	18.3	-	-
Transfers in	3.0	3.0	-	-
Sub-total non-taxes	**$161.5**	**$162.4**	**0.6%**	**$0.9**
TOTAL REVENUE (Excluding Fund Balance)	**$943.1**	**$956.90**	**1.5%**	**$13.80**

Real Estate Tax. Current projections for real estate assessment changes in January 2011 have the total tax base increasing 1% over CY 2010. This percent change assumes a flat residential market and a slightly positive commercial market. A 3% tax base increase in the out year (CY 2012) is also incorporated into FY 2012 real estate tax projections, accounting for new construction and assessment increases. More precise figures will not be available until January, when the Department of Real Estate Assessment completes the annual assessment process. The estimates at this time are made based on very limited data.

Personal Property Tax. FY 2011 personal property tax revenue, which includes both business tangible and motor vehicle personal property tax, is expected to increase slightly. As more data on vehicle prices and purchases is received and analyzed, this projection will be revised.

Business, Professional and Occupational License Tax (BPOL). BPOL tax revenue is generated by taxes levied on entities doing business in the County and is based on a percentage of gross receipts or a fixed fee. After experiencing modest increases in BPOL in FY 2009 and FY 2010, the FY 2011 BPOL revenue budget was increased. For FY 2012 BPOL revenue is projected to remain flat. Actual FY 2011 revenues will not be available until the third quarter of the fiscal year.

Other Local Tax Revenues:

- **Sales Tax, Meals Tax, Transient Occupancy Tax:** These three large tax revenue sources are expected to increase approximately 3% over the adopted FY 2011 level.
- **Car Rental Tax, Recordation Tax, Utility Taxes:** These other major local taxes are expected to remain relatively flat in FY 2012.

Non-Tax Fees and Miscellaneous Revenue. Revenues in this category are levied to offset the cost of licensing certain trades, interest income, charges for services, and fine revenue. For FY 2011 these categories are expected to increase approximately 1.2%.

Intergovernmental Revenues. This category includes state and federal revenue received by the County. Arlington receives funds from the Commonwealth of Virginia for a variety of state-mandated and supported functions and services. The County also receives a portion of some revenues collected by the state. Most federal revenue is received in the form of grants. In FY 2012, intergovernmental revenue is expected to be flat or negative, reflecting a continued slowdown in state revenue and flat growth in federal funds. It is likely that this category may be revised based on General Assembly actions during the upcoming legislative session.

Expense Projections

As described to the Board on September 28, 2010, the expense pressures facing the County include a number of costs that can not be avoided. These added expenses include:

- Retirement Fund (up to $5.7 million)
- Other Post Employment Benefits ($2.1 million)
- School Transfer ($5.5 million from increased tax revenues)
- New Facilities ($2.5 million)

Retirement Fund: The County is committed to having a fully funded retirement fund. An updated actuarial study will not be available until the end of October but if the County is required to increase funding to the retirement fund to continue Board policy to fully fund its financial obligations the increase in FY 2012 could be up to $5.7 million.

Other Post Employment Benefits (OPEB): The increase in the actuarial funding requirement to meet the annual required contribution for FY 2012 is $2.1 million. This is based on an actuarial assessment completed in August 2010.

School Transfer: The Schools share in local tax revenue increases. Based on projected revenue increases for FY 2012, the schools would be entitled to an additional $5.5 million, as an expense transfer, in FY 2012 for their school operating needs.

New Facilities: There are several projects that have been approved by the County Board over the last few years that will begin operations in FY 2012 and require funds for operation.

- Mary Marshall Assisted Living Facility: Located in south Arlington off Washington Blvd., the Mary Marshall facility will serve up to 52 residents in this assisted living supportive housing. Additional funds needed in FY 2012 are approximately $1.6 million (net). This covers ¾ of the 2012 fiscal year; the facility is projected to open in the second quarter of FY 2012.

- Long Bridge Phase II: Long Bridge Park, formerly North Tract, will have multi-purpose athletic fields which will be in operation in FY 2012. The estimated maintenance and upkeep for these fields is $0.2 million.
- Fire Station 3: This fire station located in Cherrydale will be open in FY 2012 and require operating and maintenance funding of approximately $0.2 million for full year funding.
- Columbia Pike Garage (Penrose): The County entered into an agreement with Columbia Station LLC to construct a garage on Columbia Pike. The County's annual payment to the developer is approximately $0.5 million. It is anticipated that a portion of this cost will be offset by parking meter revenue.

Another set of expenses are also anticipated. These include:

- Employee compensation ($4.0 million)
- Health care cost share with employees ($3.0 million)
- Inflationary costs for providing existing current services ($5.2 million)

Employee Compensation: The County has 3,231.53 full-time equivalent funded positions approved in the FY 2011 General Fund budget. These positions account for 56% of the County's general fund operating budget. Compensation will be among the challenging issues in FY 2012, as the Board weighs maintaining competitive compensation against other competing priorities. The cost of employee steps in FY 2012 is approximately $3.0 million with an additional $1.0 million needed to permanently buyback the furlough day which is included in the adopted FY 2011 budget. This additional $4.0 million in employee compensation does not address the current compensation shortfalls for various job classifications when compared to Alexandria and Fairfax.

Health Care: Healthcare costs continue to rise for employees and employers. Current projections for normal inflation and the increase in costs expected from recent federal legislation are 10%. If the County shares in the rising cost of healthcare in FY 2012 the projected cost increase is $3.0 million. This would maintain the approximate split between County and employee of 79% / 21% respectively.

Inflationary Costs for Continuing Services: The cost of doing business and providing services in FY 2012 is expected to increase due to normal inflationary pressures. Rent on County leased facilities increase annually along with many other contractual services. Budget planning forecast projects an increase of $5.2 million for contractual increase in FY 2012 for providing the same level of services to the community as is provided in FY 2011.

One-Time Costs Expected in FY 2012: Due to projected attrition for public safety there will be additional recruit classes required in FY 2012 above the normally budgeted amount. It is anticipated that there will be additional one-time costs of at least $1.0 million. If however the County Board adopts the Manager's recommendation in the FY 2010 Closeout board report (prior board item) this cost would be funded and would reduce the projected revenue and expenditure gap by $1.0 million.

Other Non-personnel Cost Adjustments:

- Metro: The County's contribution to Metro is not expected to change significantly from the FY 2011 adopted level.
- Debt Service: Based on projected debt issuance and projected interest rates in FY 2012, the projected debt service is estimated to be slightly less in FY 2012 than the adopted FY 2011 budget.
- Maintenance Capital (PAYG): Ongoing funding projected for FY 2012 based on the adopted FY 2011 budget is $7.0 million. The spring of CY 2010 the County Board adopted the FY 2011 – FY 2016 capital improvement plan which planned for a PAYG funding need of $14.5 million. The difference ($7.5 million) is not included in the projected funding gap of $14.2 at this time.

Revenue / Expense Projection at Current Tax Rates **($'s in million)**	
REVENUE INCREASE	**$13.8**
<u>Expense Pressures</u>	
Retirement	($5.7)
Other Post Employment Benefits (OPEB)	(2.1)
School Transfer (portion of increase in local tax revenue)	(5.5)
New Facilities	(2.5)
Sub-total	**($15.8)**
Employee Compensation (steps)	($4.0)
Healthcare	(3.0)
Inflationary Cost for Continuing Services	(5.2)
Sub-total	**($12.2)**
Total Expenditure Increase	**($28.0)**
Funding Gap at Current Tax Rates (revenue increase – expense forecast)	**($14.2)**

Schools: The County is expected to transfer approximately $5.5 million to the Schools based on the current Revenue Sharing Agreement for the increase in local tax revenue projected. In addition there will be an additional amount required per the Revenue Sharing Agreement based on the change in School enrollment. Recently received School enrollment changes show an increase in the student population of 1,008 students. This enrollment increase results in an increase to the Schools transfer of $8.6 million in addition to the $5.5 million planned in the County's expense/revenue gap discussion at current tax rates.

Summary

The budget is where the County Board translates the vision, values and polices of the community into action. Every year the development and adoption of the County's operating budget is challenging because our desires for the community exceed resources available. The FY 2012 budget will be difficult in light of revenue growth lagging behind historical averages and the expense pressures facing the County. We will be required to focus more on priority needs than discretionary desires that enhance Arlington as a place to live and work. As the County positions itself for the economic recovery, it will be necessary to adopt a strategic balance between the fundamental services that local government deliver with the programs that are so important to Arlington residents and the community at large. The creation and adoption of the County budget is always about striking a balance; obviously a financial balance, but also a service balance.