

CITY OF ALEXANDRIA, VIRGINIA
FINANCIAL MANAGEMENT SELF-ASSESSMENT
USING
STANDARD AND POORS
RATING CRITERIA

June 2009

Revenue and Expenditure Assumptions

Are the organization's financial assumptions and projections realistic and well grounded both from long-term and recent trend perspectives?

- Conservative revenue forecasting and expenditure management is the practice, so as to make the question “how much of a surplus” rather than “is there is going to be a surplus.”
 - Recent trend analysis used to update current year and subsequent year revenue projections in January and again in April prior to passage of budget in May for fiscal year beginning July 1.
 - If during the fiscal year, economy appears to be varying from budget assumptions, management tools are implemented to manage expenditures.
- Multi-year forecasting required by City Council adopted Debt Related Financial Policy Guidelines since 1987.
 - Multi-year forecasts are produced for three revenue growth scenarios and included in the proposed and approved operating budgets.
 - Budget Long Range Forecasts use reasonable range of revenue trend estimates and expenditure trend estimates.
 - Long Range Forecasts updated annually.
 - Projections in long range forecast based on historical trend analysis.
- Outside information used in assessing strength of economy and tax base.
 - Regional economic and commercial real estate forecasts provided to the City quarterly by Delta Associates and used in revenue projections and budget planning.

- Regional economic and fiscal information (such as that produced by the George Mason University Center for Regional Analysis) monitored and used as an influencer of revenue projections and budget recommendation decisions.
- Multiple City agencies tasked with collecting and sharing economic and fiscal data with City financial and policy managers.
- City Manager conducts quarterly economic discussions with key business community leaders

Budget Amendments and Updates

Are there procedures for reviewing and amending the budget based on updated information and actual performance to ensure financial targets are met?

- Monthly financial reporting is required by the City Charter, and as a result a Monthly Financial Report is presented to City Council each month. Nine months of the year it is presented at a Council meeting, and also posted on the City’s web site.
 - Monthly Financial Report contains an analysis of the economy, revenue trends and expenditure patterns, as well as contains selected historical economic indicators
- Debt Related Financial Policy Guidelines prohibit City Council from amending the City Manager’s revenue projections.
 - In month prior to budget adoption, a full detailed analysis of each revenue source is undertaken and current and subsequent fiscal year revenue budgets are adjusted accordingly by the City Manager.
- Management when revenue trends warranted has mandated expenditure curtailment or budget sequestration by operating departments.
 - City Departments submit monthly expenditure forecasts for the last half of the fiscal year.
 - These reports are used to take any necessary actions through the transfer of resources between departments, to reduce expenditures, or to make supplemental appropriations from fund balances designated for certain contingencies (e.g. fuel price increases).

Long Term Financial Planning

Does Management have a long-term financial plan that allows them to identify future revenues and expenditures as well as address upcoming issues that might affect these?

- Debt Related Financial Policy Guidelines require the long range operating budget forecasts go out 6 years (budget year plus 5).
- These forecasts incorporate the results of the 6 year Capital Improvement Program and the funding plan (debt, cash capital, and other sources of revenue) for those capital expenditures.
- Interactive model created to examine what ifs. Sensitivity analysis of impact of different rates of growth in salaries and benefits shown.
- Forecasts used at Council Retreat in November to set budget guidance.
- Forecasts have been used to look at impact on operating budget of options during consideration of future CIPs.
- Council has created Strategic Plan with a Vision for Alexandria in 2015 and Goals for the period 2004 to 2009. New Strategic Plan to be developed by incoming Council this fall.
- Business plans are begin created to link that Strategic Plan more tightly with the very detailed performance based budget that contains approximately 165 programs and 470 activities.

Long Term Capital Planning

Has the organization created a long-term capital improvement program?

- Six year CIP (budget year plus 5 years) approved annually by City Council.
- CIP presents all known capital needs over the period, and prioritizes between those needs that can be funded through reasonable levels of cash capital, debt and special revenues, and those that are unfunded at the moment, and put on a “wait list” for possible future funding.
- CIP funding linked to operating budget (simultaneously considered and passed by City Council).
- CIP future funding linked to 6 year long range forecast, which includes cash capital and debt service costs over that time period from approved CIP.

- The City also maintains a separate equipment replacement fund that is primarily used to fund the replacement of vehicles and other heavy equipment through regular depreciation charges to the annual operating budget.
- The City also maintains a similar, separate computer replacement fund used to replace and modernize desk top computer equipment.

Investment Management Policies

Has the organization established policies pertaining to investments, such as the selection of financial institutions for services and transactions; risk assessment; investment objectives; investment maturities and volatility; portfolio diversification; safekeeping and custody; and investment performance reporting, benchmarking and disclosure?

- Formal written investment policies exist for short-term investments.
- As of July 1, 2008 the City started using the Commonwealth of Virginia's Local Government Investment Pool.
- Formal written investment policies exist for long-term (i.e., pension fund) investments.
- Actuarial assumptions reviewed annually.
- Financial consultant employed to monitor performance of long-term investments and investment managers.
- Primary bank for City day-to-day revenue collection, check writing, and other banking services is competitively selected.
- Formal asset allocation policies for long term investment created after studies of risk and returns were evaluated have been adopted and are in place
- Financial reporting on investments created and issued quarterly to pension board and to City staff.

Debt Management Policies

Has the organization established policies pertaining to the issuance of debt, such as projects that may or may not be funded with debt (including economic development projects); maturity and debt service structure; use of security and pledges, credit enhancement, and derivatives; and debt refunding guidelines?

- Debt Related Financial Policy Guidelines were adopted by the City Council in 1987, and have been formally amended when appropriate. The adopted debt policy guidelines that provide target and limits for the following debt ratios:
 - Debt as a percent of fair market value of real property (target 1.1%; limit 1.6%)
 - Debt as a percent of total personal income (target 3.2%; limit 4.5%)
 - Debt Services as a percent of general government expenditures. (target 8.0%; limit 10%.)
- Debt ratio performance is recalculated at the beginning of the budget process to frame the capital planning discussion, and are rerun simultaneous to capital project decision making to ensure debt policies are followed.
- Practice is to keep CIP at least 1/4 cash funded.
- City's debt issuance practices have been to issue fixed rate general obligation bonds with an aggressive payback period.
- Swaps and variable rate debt have not been authorized by City Council
- Debt policy guidelines also establish specific policies and expectations related to financial and debt management:
 - CIP will rely on current revenue, including fund balance, to finance its short-lived and maintenance oriented capital improvements.
 - City believes in funding a significant portion of CIP on pay-as-you-go basis
 - The priority to consider when additional General Fund revenues are available at the end of the fiscal year would be a designation within fund balance for pay-as-you-go capital.
 - The City will not issue tax or revenue anticipation notes to fund ongoing governmental operations.
 - The City manages its cash in a fashion that will prevent borrowing to meet working capital needs.
 - The City will not issuing bond anticipation notes (BAN) for a period of longer than 2 years.

- If BAN issued, will be converted to long-term bond or redeemed, but it will not be rolled over.
- The City's CIP states what type of projects are eligible for inclusion in the CIP.
 - "Expenditure of more than \$10,000 that acquires, expands, repairs, or rehabilitates a physical asset with a useful life of at least three years. It does not include day-to-day maintenance expenditures such as custodial or janitorial services, painting, minor (less than \$10,000) carpentry, electrical and plumbing repairs, or repair or routine replacement of fixtures or furniture."

Reserve and Liquidity Policies

Has the organization established a formalized operating reserve policy, which takes into account the government's cash flow/operating requirements and the historic volatility of revenues and expenditures through economic cycles?

- Debt Related Financial Policy Guidelines established by City Council states that:
 - The City will maintain at an unreserved fund balance of at least 10% of general fund revenues.
 - The City will maintain a target of 5.5% and a minimum of 4.0% undesignated fund balance as a percent of general fund revenues.
 - These two ratios compare favorably with the reserve balances maintained by other triple A rated jurisdictions of similar size in the Metropolitan Washington area.
 - The City will not finance recurring operations from the General Fund equity balance for periods longer than two years as confirmed by the audited financial statements.
 - If the audited financial statements confirm that recurring operations have been financed from the General Fund equity balance for periods longer than two years, the next ensuing budget will rely on any General Fund equity balance.
 - With the exception of the unreserved fund balance minimum, the City has conformed to these guidelines, first established in 1987, over the years.

- The unreserved fund balance will be below the 10% minimum limit at the end of FY 2009. (It is estimated to be at 9.0%.) This situation is caused in large part by the spend-down of \$7.4 million in prior year surpluses for one-time expenditures such as cash capital contributions, and a \$4.2 million initial down payment to the new post-retirement benefits trust fund (OPEB). These amounts will decline in FY 2010 to \$2.3 million for cash capital and \$3.1 million for OPEB. Staff believes that going below this ratio, while of long-term concern, is an appropriate financial management response to the current recession caused revenue shortfall, given the City's overall financial health, the strength of our undesignated fund balance ratio (5.6% of general fund revenues and above the target of 5.5% and significantly above the limit of 4.0%), and underlying economic fundamentals.
- Annual cash flow projections undertaken to determine liquidity needs and to insure sufficient cash is on hand or reasonably accessible to meet expenditure needs
- Revenues and Expenditures monitored monthly, and actions taken if revenues and expenditures vary materially from the adopted budget.

On June 13, 2008, Standard and Poor's issued a document describing its Top 10 Management Characteristics of Highly Rated Credits In U.S. Public Finance. Many of those characteristics repeat what was previously listed in its financial management assessment public finance criteria issued in June of 2006 and discussed above. However, there are a couple of additional characteristics mentioned in this newer document.

Prioritized Spending Plans and Established Contingency Plans for Operating Budgets

It is good public policy to have contingency plans and options to address budget imbalance when it occurs. This would include an analysis of the following:

- **What part of the budget is discretionary;**
- **What spending areas can be legally or practically reduced;**
- **The time frame necessary to achieve reductions of various programs;**
- **Where revenue flexibility exists; and**
- **A course of action on the revenue side under various economic scenarios.**

Our activity in this regard can be summarized as follows:

- We have restructured the City’s budget through the Managing for Results Initiative to show approximately 165 programs and 470 activities.
 - For each activity the cost, and number of employee positions are shown, as well as measures of output, efficiency and quality of service.
 - We believe this transparent display of budget information allows City Council and the public to see and evaluate the relative value of City programs and activities at a level of detail that would permit, if necessary, the hard choices that may need to be made if the City’s revenue outlook deteriorates.

- City Council has reformed the budget process in order to provide guidance to City staff in the fall of each year that sets clear expectations and provides a transparent process. These policies and procedures should help us address future budget challenges.
 - The reformed budget process, first adopted in May of 2005, gives Council a mechanism to review the budget outlook in the fall and set specific parameters for the City staff in development of the proposed budget and Capital Improvement Program.
 - These reforms have been fine tuned over the last few budgets and are working well through the conclusion of the Fiscal Year 2009 budget process.

- We have been conducting efficiency and best practices studies of individual departments and programs through outside consultants.
 - These studies have identified some relatively modest efficiency savings (in the range of hundreds of thousands of dollars in each study) as well as program improvements (sometimes costing nearly as much).
 - These studies, and others to come, allow us to examine each department and program in the depth required to find true efficiencies and to benchmark ourselves against best practices found in other comparable jurisdictions.

- A key study is underway of the City’s Personnel Classification and Compensation policies and procedures. The pay and benefits provided to City and Schools employees constitute the single largest type of expense of City government.

- We must ensure that pay and benefits are adequate to attract and keep an excellent workforce, but our future financial sustainability requires us to be prudent in our pay and benefits decisions so that we both compete in the regional labor market for our employees and recognize our financial limitations.
 - This study of City employee pay and benefits was used to inform Council in its deliberations on the FY 2010 budget and will be finished before preparation of the FY 2011 budget.
- We are closely monitoring our revenues, expenditures and staffing levels during the fiscal year.
 - City staff has provided Council with detailed monthly expenditure and revenue status reports for many years.
 - Given its transitional nature and high degree of uncertainty, we have been closely monitoring sales and values in the real estate market, as well as other key revenue trends, such as interest earnings.
 - We have internal reports that monitor citywide and departmental on-board staffing levels compared with authorized staffing levels.
 - We also ask departments to periodically project their spending through the end of the fiscal year and have measures in place to ensure orderly year-end spending practices.
- We have already been increasing the amount of vacancy savings captured in our budget process.
 - In the FY 2010 proposed budget we have maintained vacancy savings in department budgets of \$5.92 million. This compares with \$3.1 million taken out of the FY 2005 budget.
 - These vacancy savings have been taken very precisely to reflect both the size and past experience of each department with turnover and actual vacancy savings in prior years.
 - We have instituted a procedure for the City Manager to review individual vacancies on City Staff before allowing action to proceed to fill those

- City Council has the ability through the monthly Capital Improvement Program allocation docket items to control capital spending.
 - Each of the months that Council is in session, City Staff presents a request for Council to release (“allocate”) funds for upcoming CIP projects that are ready to go.
 - Combined with this monthly allocation process, as City Staff begin to adopt the discipline required by the phased approval process for major CIP projects, City Council and the City Manager have had the ability to slow down the pace of capital spending.

- We continue to maintain adequate undesignated fund balances that are available to ensure a final backstop against an unexpected major decline in revenues in FY 2009.
 - Our current estimated undesignated fund balance of \$29.7 million is 5.6 percent of FY 2009 General Fund Revenues. This number includes a \$4.3 million set aside specifically as a “FY 2010 Revenue Shortfall Reserve” intended to provide a cushion against possible further deterioration in revenues beyond what is already projected. This ratio is slightly above City Council’s Target of 5.5 percent and well above the limit of 4.0 percent.
 - This balance is sufficient protection, in the highly unlikely case the above measures, or other measures which may be needed to be crafted and implemented, are not sufficient to protect us against further deterioration in the economy.
 - Using this fund balance would be a last resort, and ultimately we will make sure there are no major, sudden dislocations of services.

Long-Term Planning for All Liabilities of Government

Long-term planning for all liabilities of a government, including pension obligations, other post employment benefits and other contingent obligations would be optimal and allow for comprehensive assessment of future budgetary risks.

- The City has recently instituted a plan, including the creation of a trust fund for funding Other Post Employment Benefits (health and life insurance).
 - According to the most recent actuary study, the estimated unfunded liability of \$123.5 million (both City and Schools) requires an estimated \$17 million annual required contribution assuming a 7.5% annual return to the trust fund.
 - Beginning in FY 2009, the City and Schools have begun a process to reach that level of annual required contribution by FY 2013.
 - The City will gradually draw down and deposit in the trust \$10.7 million designated in fund balance for this purpose.
 - Gradually, the city will increase its level of new funding from \$1.4 million (in the approved FY 2009 budget) to \$2.5 million and eventually to \$3.9 million a year in FY 2013.
 - Together with current pay-go contributions and cost pool subsidy amounts with active employees, the percent of the annual contribution funded will start at 86% in FY 2009 and reach 100% by FY 2010.
 - The Schools will create a separate trust for OPEB funds and they have budgeted \$0.8 million in FY 2009 in new funds for this purpose, \$1.6 million in FY 2010 and will gradually increase that to \$4.0 million a year in FY 2013 to reach their required annual contribution level.
- Other actions have been taken to control OPEB costs.
 - The City previously had established a fixed dollar contribution of \$260 a month (in lieu of % of premium) for retiree health benefits.
 - Also, the City has changed the policy so that for new employees this benefit will be graduated by length of service.
- The City has examined the level of life insurance provided to its retired employees and decided to eliminate this benefit for new employees hired after June 30, 2009.
- The City of Alexandria's budget does not contain many component units operating outside of the primary general government budget that pose a financial risk to the City's fiscal condition.
 - Only three component units are outside of the primary government budget, the Schools, the Library and the locally operated bus transit company.

- Each of them receives the bulk of their funding from the City through annual appropriations controlled by Council and do not have the power to enter into debt obligations on their own.

Effective Management and Information Systems

Investing in systems that improve the efficiency and effectiveness of a government unit and enhance overall service delivery is a positive financial management tool. Investment in financial management and information technology infrastructure has been significant during the past decade. To the extent that these changes improve financial reporting and monitoring capabilities, they enhance transparency and are viewed as a positive credit factor.

- The City of Alexandria prepares an annual information technology plan as part of its annual Capital Improvement Program.
 - This plan is a 6 year plan of information systems for public access, financial and human resource management, geographic information systems, public safety systems, recreation systems, and other program specific systems.
 - It also provides 6 year plan for basis information infrastructure projects, such as local area network services, wide area network services, and enterprise services.
- The City of Alexandria also maintains a computer replacement fund that charges depreciation to the users so that timely replacement and modernization of desk top computer equipment can occur on a regular cycle.
- The City is looking at the replacement of its financial and human resource management systems over the course of the next several years.

Economic Development Strategy

Economic development programs have expanded rapidly over the last 20 years. The question for state and local governments now is not whether there should be a formal economic development program, but rather how significant a resource commitment should be dedicated to running these programs and offering incentives. These are clearly government policy decisions involving cost benefit analysis that are generally outside the credit rating process. However, if these economic development programs and strategies create employment, enhance diversification, and general solid income growth, they could have a positive effect on a government credit rating over the long-term. To the extent that there is a net revenue benefit to

the government, it could also be a positive credit factor. Economic development strategies have increasingly become regional in nature and there has been a more coordinated approach between state and local governments.

- On December 15, 2007, the City adopted, in principal the recommendations of a blue ribbon Economic Sustainability Work Group.
- The Work Group created an Economic Vision
 - A 21st Century, knowledge based, creative class, diverse community with a high quality of life.
 - A place where business can locate and grow.
 - A place where planning and land use encourage smart fiscal practices with historic preservation.
 - Where City government is responsive to all.
 - Where taxes generated by commercial activities fund community needs and help reduce taxes paid by residents and local businesses.
- The Work Group identified strategies for achieving that vision.
 - Close-in urban location
 - Low unemployment
 - High per capital and household income
 - High quality of life
 - Strong demand for housing
 - Well-educated population
 - Low crime
 - Tax base growth strong
 - Wide range of government services
 - Historic preservation
 - Top AAA/Aaa bond ratings
- The Work Group make over 100 recommendations covering a wide range of topic areas. The Work Group organized the recommendations into 10 key topic areas.
 - Metrorail
 - Commercial Economic Activity
 - Potomac Waterfront Potential
 - Landmark Mall
 - Leveraging the City's Assets
 - Travel and Tourism
 - Focus of Economic Development Activities
 - Responsiveness of City Bureaucracy and City Processes
 - Organization and Vision and Performance of Economic Development Functions
 - Tax Structure

- Council approved the establishment of an Economic Sustainability Implementation Monitoring Committee to ensure that these recommendations are addressed. The Committee will
 - Receive regular reports from City departments and economic development-related agencies on the status of implementation of the recommendations.
 - Advise on implementation priorities, as well as assist in developing implementation strategies and monitoring the status of implementation.
 - Advise on outcome and impact metrics of economic development activities.
 - Provide periodic reports to Council, and
 - Monitor and review the status of the implementation of the recommendations of Small Business Task Force.