

February 8, 2011

City Manager's Message

To the Honorable Mayor and Members of City Council:
It is my pleasure to transmit the Proposed Fiscal Year 2012 Operating Budget and the Proposed FY 2012-2021 Capital Improvement Program. The submission of these documents marks my last proposed budget to you as City Manager. It has been a challenging, exciting, and instructive experience managing the City's finances over the last six years.

The FY 2012 Proposed Operating and Capital Budgets represent a culmination of years of effort to redesign our approach to fiscal planning, make our budgeting processes more inclusive and transparent, and improve upon our strategic decision-making. These fiscal recommendations to you were developed using the same framework employed by City Council to craft the City's Strategic Plan. Focusing on the goals of the City as defined by Council and the community, cross-departmental staff teams have worked for several months to recommend where taxpayer resources are best invested to accomplish our objectives and realize our goals, while still working within a constrained resource environment.

The work has been challenging to all involved. Several years of economic downturn has created some desire for service expansion to those residents facing economic hardships, calls to reverse recent budget reductions deemed necessary during the past few years, plans to meet delayed City organizational needs as well as pressures for City infrastructure and facility improvements. Regardless, we are circumspect in our requests for resources and mindful of the fact that we are only now beginning to see the early signs of growth and expansion.

This budget is based on cautious optimism. We are optimistic that the financial tide has turned. We are cautious in that we cannot project a rapid recovery. Rather we must base our plans on an expected slow and measured improvement in our local economy.

Over the years we have redesigned our approach to fiscal planning, making our budgeting processes more inclusive and transparent, and improving upon our strategic decision-making

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This budget is based on cautious optimism -- the financial tide has turned but we cannot project a rapid recovery.

City Manager's Message

No tax rate increases and no new programmatic reductions

The budget contains numerous cost saving and efficiencies in all City operations.

The proposed operating budget is balanced without the necessity of increases in tax rates, fees, fines or service charges, and without the necessity of new programmatic reductions. The budget contains numerous cost saving and efficiencies in all City operations. Of particular impact are the provisions for increased cost sharing by employees of retirement and health care benefits.

This result did not occur by chance. We have kept our financial reserves, when compared against City financial policy guidelines, strong. We finished FY 2010 in the black, and we will similarly finish FY 2011 with a surplus due to the turnaround in our real estate values. Our current revenue projections from last October appear to be on target for the remainder of FY 2011. We do not have to pay now for past budget gimmicks. In past budgets we have not used one-time revenue sources to fund ongoing expenses; neither do we propose doing so in this budget. We also have not relied on temporary one-time expenditure reductions, such as furloughs or delays in pension funding. The programmatic reductions taken in past years were difficult. We took \$9 million spending reductions mid-year in FY 2009, \$38 million in FY 2010, and \$23 million in FY 2011. These necessary budget choices are now yielding cumulative savings. We expect those savings will continue in the years to come.

City Council Fiscal Guidance and Budget Highlights

FY 2012 budget in accord with the guidance provided by City Council

City operational expenses increasing a modest 3.2%

Few programmatic increases – all directly support City Council strategic goals and initiatives

I am proposing a FY 2012 budget in accord with the guidance provided in City Council Resolution #2426. This budget does not increase any General Fund tax rate. The increase in City operational expenses, exclusive of subsidies for transit operations, the Schools transfer, and debt service and cash for capital projects, is a modest 3.2%.

Few programmatic increases are included in the proposal, and those that are included directly support City Council strategic goals and initiatives. Per City Council guidance, we have held level overall staffing funded by General Fund revenues. In some instances, there are increases to programs and services offered for Council consideration. These are presented as options to be considered above the base budget proposal. In accordance with Resolution #2426, these options are ranked in order of priority preference. These options also are linked to City strategic goals and objectives.

City Manager's Message

Significant operational savings by having employees share a greater portion of the cost of their benefits

This budget achieves significant operational savings by having our employees to share a greater portion of the cost of their benefits. The budget proposes continuing our previously announced policy of gradually increasing the minimum City employee share of health insurance premiums. Also, the budget proposes a 1% minimum in the employee share of the cost of City supplemental retirement benefits, as well as a 1 percentage point increase in Police Officer and Firefighter pension contributions. I should note that City Council has already formed an ad hoc Retirement Benefit Advisory Group to review current practices and look into the possible need for additional long range changes in retirement defined benefit plans. This Group will report back next fall in time for consideration of its recommendations in the next budget cycle.

Some increases in salaries to mitigate additional benefit cost sharing and provide a more competitive salary structure

To mitigate the negative impacts of additional benefit cost sharing on employee's compensation and to provide employees with a fair, regionally competitive salary structure, the proposed budget provides funding for increases in salaries. The budget sets aside \$0.7 million in funds for the first year of a three year program to implement pay adjustments to be competitive with neighboring jurisdictions. It also provides funding for merit-based step increases for qualified City employees, but no across-the-board pay increases for the fourth year in a row.

4.1% increase in operating funds for the Schools

City Council's direction to share with the public schools a funding increase equal to the overall increase in the budget will result in a 4.1% increase in the amount of monies provided ACPS. As you know, the Schools have considerable discretion in how they may use these funds. I understand budget choices that meet this overall fiscal guideline are being prepared by the Superintendent for School Board consideration and adoption on February 24th.

No more borrowing and cash capital from current General Fund revenues than was contained in last year's approved CIP

As Council directed, the proposed CIP funding plan assumes no more borrowing and cash capital from current General Fund revenues than was contained in last year's approved CIP. As a result, a total of \$158 million is committed to ACPS capital projects, the same amount provided in last year's approved plan. This amount is far less than the \$372 million proposed by the Superintendent. Funding designated for City related projects is primarily focused on the maintenance of existing City facilities and infrastructure. A modest amount of funding provides for expansion or reconstruction projects.

City Manager's Message

A Transportation Add-on Tax on commercial properties is proposed of 12.5 cents for transportation improvements

A Transportation Add-on Tax on commercial properties is proposed to begin in FY 2012. This proposal would levy an additional 12.5 cents per \$100 tax on real property used for commercial purposes. A comprehensive 10 year plan proposes to use these funds to achieve a wide variety of necessary transportation improvements benefitting all parts of Alexandria. Continued population and economic growth in the region and in Alexandria places increased stress on the City's transportation network each year.

The capital budget includes revenues and expenditures related to the construction of a Metrorail station in Potomac Yard

As part of this proposal and as requested by City Council, business license taxes are proposed to be reduced to partially offset the cost impact of this tax on the business community.

The capital budget for the first time includes revenues and expenditures related to the construction of a Metrorail station in Potomac Yard as approved by City Council in June 2010. To begin funding the early stages of the project, a 20 cent per \$100 tax on real estate is proposed for the Tier 1 part of the Special Service Tax District of Potomac Yard (west of the railroad tracks), which was created just two months ago by City Council. The CIP 10 year plan also includes a section showing the financial plans for the Potomac Yard Metrorail station.

The largest rate of growth (12.1%) is for debt service and pay-as-you go financing of the Capital Improvement Program (CIP).

As one can see from the following chart summarizing changes in the proposed Operating Budget, the largest rate of growth is for debt service and pay-as-you go financing of the Capital Improvement Program (CIP). The 12.1% rate of growth is a result of increased borrowing for capital projects in the last two budget cycles.

FY 2012 Proposed General Fund Base Operating Budget

Millions of Dollars

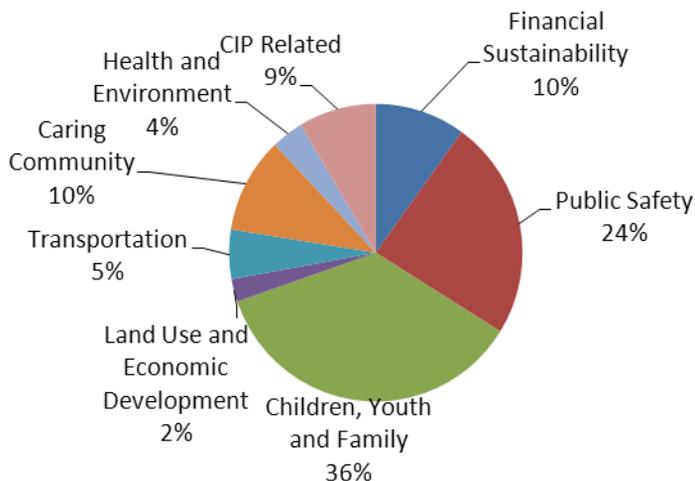
| | FY 2010 Actual | FY 2011 Approved | FY 2012 Proposed | \$ Chg FY11/12 | % Chg FY11/12 |
|------------------------------|-------------------|---------------------|---------------------|-------------------|------------------|
| City Operating | 304.8 | 305.5 | 315.4 | 9.9 | 3.2% |
| Transit Subsidies | 13.1 | 16.0 | 15.9 | (0.1) | -0.9% |
| Capital Program Funding | 39.5 | 42.2 | 47.3 | 5.1 | 12.1% |
| City Total | 357.3 | 363.7 | 378.6 | 14.9 | 4.1% |
| ACPS | 164.6 | 167.9 | 174.8 | 6.9 | 4.1% |
| City & ACPS Total | 521.9 | 531.6 | 553.4 | 21.8 | 4.1% |

City Manager's Message

The majority of funding (60%) is for two strategic goal areas: public safety and children youth and families

The City's General Fund Operating budget can be divided into the seven strategic goal areas (plus funding for capital projects (CIP-related)). The majority of funding (60%) is for two strategic goal areas: public safety and children youth and families (a category which includes the transfer to the Schools).

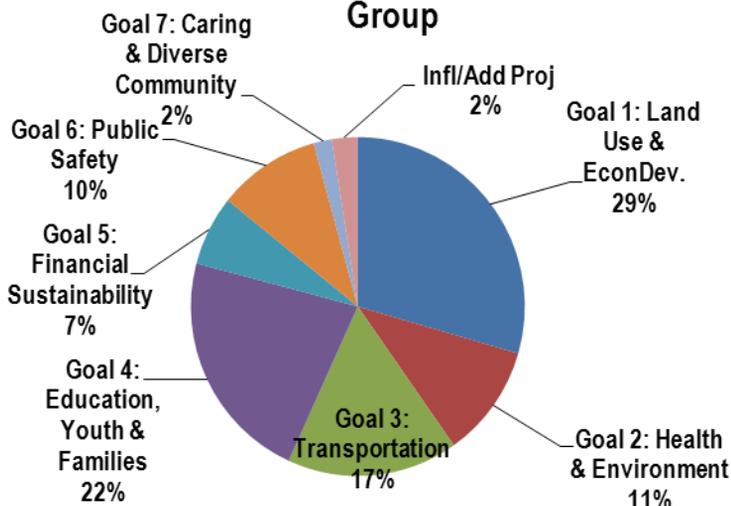
FY 2012 General Fund Operating Budget by Strategic Goal Area



The largest share of the CIP (29%) is for land use and economic development, a category that includes the Potomac Yard Metrorail station project.

The City's Capital Improvement Program is also divided by strategic goal groups below. The largest share of the CIP (29%) is for land use and economic development, a category that includes the Potomac Yard Metrorail station project. The transportation share (without the effects of the Transportation Add-On tax) is another 17%. Goal 4, which includes Schools capital projects is the second largest category over the 10 years at 22%.

Proposed FY 2012 - 2021 CIP by Strategic Goal Group



City Manager's Message

Notable proposed changes to City programs and public service delivery efforts are described in the budget overview that immediately follows this message.

As I have suggested above, some cautious optimism about the City's fiscal condition is warranted. We are in considerably better financial shape than most state and local governments nationwide and only a few of our neighbors can come close to matching our current financial condition. The investment in our economic development structure and strategy over the past few years is now beginning to yield results. We are well positioned to achieve the measure of financial sustainability we all desire, and we are poised to have an operating budget and capital improvement program that is structurally balanced for the long term.

We must continue to work together responsibly as we emerge from this financial crisis with a long term perspective and strategy. As Council has directed, we will work this spring to develop a 10 year blueprint for linking the strategic plan – its goals, objectives and initiatives – to future budgets. This Operating Budget and Capital Improvement Program for FY 2012 is only a first step in developing a 10 year blueprint for both a long term, strategic focus on financial sustainability and maintaining the high quality of life enjoyed by Alexandrians.

Sincerely,

James K. Hartmann
City Manager

We are in considerably better financial shape than most state and local governments nationwide

Only a few of our neighbors can come close to matching our current financial condition

We must continue to work together responsibly as we emerge from this financial crisis with a long term perspective and strategy.

Attachment

Compliance with City Council Guidance in Resolution #2426

This Proposed Operating Budget and Capital Improvement Program is in accord with all guidance provided by City Council in Resolution #2426.

- Section 1. There is no increase in the real estate tax rate of \$97.8 cents.
- Section 2. The General Fund Operating Base Budget of 4.1% is balanced without any increase in tax rates.
- Section 3. The transfer to the Alexandria City Public Schools increases at the same rate as that rate of increase in total General Fund Operating budget revenues (4.1%).
- Section 4. A Transportation Add-On tax on commercial property is proposed of 12.5 cents in addition to the base budget. A partial offset in the Business, Professional and Occupation License tax is proposed of \$1.625 million and \$0.375 million increase in support for economic development activities in support of business is proposed as part of the base budget, contingent on passage of a Transportation Add-On tax.
- Section 5. The budget proposes continuation of the other dedicated portions of the real estate tax without change, including portions dedicated to Storm Water Infrastructure Improvements, Open Space Trust Fund, and Affordable Housing purposes.
- Section 6. The budget does not propose an increase in any other tax rates except the Transportation Add-On tax.
- Section 7. Although allowed by the resolution, the budget proposes no increases in fees and service charges.
- Section 8. City staffing levels do not increase except for those substantially funded by non-General Fund revenues (grants or other special revenue sources) as allowed by section 8.
- Section 9. The base budget includes funding for merit/step increases for eligible employees including an additional step.

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- Section 10. The budget does not include funding for an across-the-board salary schedule adjustment for either City or Schools staff.
- Section 11. The budget does include \$0.7 million as initial funding in FY 2012 as part of a 3 year phase-in of the implementation of competitive pay adjustments called for by the City's compensation philosophy.
- Section 12. The budget continues to implement the multi-year plan to phase-in a 20% minimum employee contribution for health care premiums. In FY 2012 that minimum is proposed to be 16%.
- Section 13. The budget proposes a minimum 1% employee contribution for retirement from all employees, and a 1% increase (from 8% to 9%) for retirement and disability benefits for police officers and fire fighters.
- Section 14. The City Council has by Resolution #2432 formed an Ad Hoc Retirement Benefit Advisory Group to look at the need for any future changes to defined benefit pension plans created under the authority of the City Council.
- Section 15. The budget contains numerous cost saving and efficiencies in all City operations. Of particular impact are the provisions for increased cost sharing by employees of retirement and health care benefits.
- Section 16 a. The CIP provides specific estimates for FY 2012 through FY 2017 and preliminary estimates for FY 2018 through FY 2021.
- Section 16 b. The CIP uses no more General Fund cash capital from current year revenues than planned for FY 2013 through FY 2020.
- Section 16 c. The CIP uses no more debt issuance than that planned for FY 2012 through FY 2020 in the Approved FY 2011 – FY 2020 CIP, except for debt financed by various other sources of dedicated revenues (e.g., grants, special revenues)

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- Sections 16 d and e. The budget proposes a one time use for funding the CIP of \$11.0 million of the FY 2010 operating budget surplus as well as an additional \$6.0 million of expected FY 2011 operating budget surplus.
- Section 16 f. The CIP provides specific descriptions of projects that can be funded within recommended levels of funding and their costs are estimated for all years. (Note: the Schools CIP has not yet (as of February 8, 2011) been approved by the School Board. Specific descriptions of ACPS capital projects will be provided after the School Board adopts its proposed CIP.)
- Section 17. The CIP has \$0.9 million in funding assumed from the sale/lease of capital assets.
- Section 18. Although not submitted as part of this budget, City staff are continuing work on an incentive program to encourage City employees to develop and implement efficiency cost saving ideas. This program will be presented to Council this fiscal year for its consideration.

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