City of Alexandria, Virginia

MEMORANDUM

DATE: APRIL 21, 2014

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

THROUGH: RASHAD M. YOUNG, CITY MANAGER

FROM: NELSIE L. SMITH, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

SUBJECT: BUDGET MEMO #31: BUDGET AND FISCAL AFFAIRS ADVISORY COMMITTEE REVIEW OF THE FY 2015 PROPOSED BUDGET

The Budget and Fiscal Affairs Advisory Committee (BFAAC) has completed its analysis of the FY 2015 City Manager's Proposed Budget for Council's consideration. This is in accordance with the Committee's mission to:

1) Examine the city's budget procedures and process and ways of improving such procedures and process, including participation by the public therein;
2) Examine the forecast of future revenue and expenditure requirements and the effect on the several taxes and fees levied by the city and burden of taxation imposed on Alexandria citizens and business organizations; and
3) Evaluate the comparative tax, revenue and expenditure levels in Alexandria with those in neighboring jurisdictions and the effect of such differences on the ability of Alexandria to attract new residents and economic development.

BFAAC will discuss this report (attached) with City Council at the budget work session on April 24, 2014.

City of Alexandria, Virginia
Budget and Fiscal Affairs
Advisory Committee

Report on the City Manager's Proposed Budget for Fiscal Year 2015

John J. Renner, II, Chairman
Margaret S. Gullen, Vice-Chairwoman
Engin Artemel
David P. Baker
Dak Hardwick
Jean Sun Kim
Benjamin Klein
Patrice Linehan, Secretary
Laurie MacNamara
Len Rubenstein
Brent Simer
Clarence Tong
Michael Wenk

TABLE OF CONTENTS

EXECUTIVE SUMMARY 3

I. REVENUES AND OUTLOOK 8

A. Residential Tax and Fee Burden Issues 8

B. Commercial Tax Base 10

C. Options to Grow Revenue Base 15

II. FY 2015 BUDGET PROCESS 17

A. *Results Alexandria* 17

B. Performance Criteria and Needs-based Budgeting 21

C. Budget Alignment with the Alexandria City Public Schools (ACPS) 23

D. Budgetary Impact of "Add-Deletes" 24

III. THE PROPOSED OPERATING BUDGET 25

A. Retiree Life Insurance 25

B. Employee Health Insurance 26

C. Non-Profit Partnerships 27

IV. THE PROPOSED CAPITAL IMPROVEMENT PROGRAM 29

A. Overview 29

B. Analysis of the FY 2015 CIP Process 29

C. ACPS and the CIP Process 30

D. CIP Programs Impact on Specific Projects 31

V. LONG-RANGE FINANCIAL PLANNING, FUTURE FORECASTS, AND DEBT BURDEN ISSUES 34

A. Long-Range Financial Plan 34

B. Future Forecasts and Tax Rate Projection 34

C. Debt Policy Guidelines 35

EXECUTIVE SUMMARY

REVENUES AND OUTLOOK

- **BFAAC encourages Council to closely monitor the residential tax and fee burden as a percentage of average household income.**

- **BFAAC recommends Council also track the residential tax and fee burden for households with incomes below the average.**

- **BFAAC recommends the City Manager track the residential tax and fee burden and include the metrics in the City Manager's annual proposed budget submission to Council.**

- **Any increase in fees or taxes should be carefully considered, particularly with income levels remaining flat.**

- **BFAAC encourages Council to develop metrics to track the commercial tax and fee burden. While BFAAC recognizes it will be a challenge to identify common metrics for the wide range of businesses in the City, BFAAC encourages Council to start with metrics appropriate for the types of businesses the City is hoping to attract in the coming five years.**

- **BFAAC cautions Council to continue monitoring the declining percentage of commercial (excluding commercial multi-family) assessments relative to residential and multi-family assessments. If the goal is to obtain a 50/50 balance, Council should work with Alexandria Economic Development Partnership (AEDP), Planning and Zoning, and other stakeholders to develop a tactical plan to grow the commercial base under the City's land use plans.**

- **BFAAC commends the City staff for developing a five-year financial plan and forecasting model, and recommends the development of a long-term revenue plan to guide decision-making.**

- **BFAAC recommends enriching the forecasting model with additional data that will permit more sensitive analysis of the revenue impact of policy decisions over the longer-term.**

- **BFAAC encourages Council to undertake policy and administrative actions designed to stimulate business activity in the City.**

- **BFAAC recommends Council provide AEDP with the resources to proactively attract businesses to the City and the appropriate authority to utilize economic development incentives.**

- **BFAAC encourages Council to consider alternative revenue sources and recommends a further review be conducted to determine the merits of a Payment In Lieu Of Taxes (PILOT) initiative or special assessment approach.**

- **BFAAC recognizes the important services nonprofit organizations provide and urges Council to proceed cautiously.**

FY 2015 BUDGET PROCESS

- **BFAAC is encouraged by the ongoing transition to *Results Alexandria* and believes the process that the new system is using to determine City budget levels is an improvement over previous budget development tools.**

- **BFAAC believes that the *AlexStat* system holds great promise in delivering accurate analytical information to City decision makers in order to make informed budgetary choices.**

- **BFAAC is concerned the scope of *Results Alexandria* is not consistent across focus areas.**

- **BFAAC believes that organizations that receive any City funding, even if they fall outside the scope of *Results Alexandria*, should have metrics, targets and goals that can be easily communicated to Alexandria's taxpayers.**

- **BFAAC strongly encourages Council to closely examine city expenditures not subject to the *Results Alexandria* performance metrics and demand a high level of budgetary rigor for those entities receiving city funding, but not directly accountable to the City Manager.**

- **BFAAC commends the City Manager for including performance criteria in evaluation for budgeting and other purposes.**

- **BFAAC urges Council to direct the City Manager's proposed budget for FY 2016 include identification of needs for services and the percentage of need met in current programs and proposed spending.**

- **BFAAC notes that the budget development process of the Alexandria City Public Schools (ACPS) and the City are misaligned.**

- **BFAAC believes, and has stated in previous reports, that this misalignment creates an untenable situation during the annual budget discussions and one that can be avoided by both elected bodies.**

- **BFAAC urges the Council and School Board to rectify the misalignment in order to avoid an adversarial relationship between the bodies.**

- **BFAAC reiterates and strongly recommends the realignment of the City and ACPS budget development processes.**

- **BFAAC has been briefed on a new "add-delete" procedure, whereby initial council member "add-deletes" to the City Manager's budget will be scored against a five-**

year forecast in order to see both long-term costs and / or savings associated with those changes.

- **BFAAC is encouraged by this new "add-delete" procedure and looks forward to the results of the long-term projections of "add-deletes," as it will add another layer of data from which council members may make budgetary decisions.**

THE PROPOSED OPERATING BUDGET

- **BFAAC encourages the City to examine alternatives that prevent imposing an immediate cut of City funded retiree life insurance premiums.**

- **BFAAC is concerned that the advantages of a City-sponsored plan with negotiated group rates will be lost after March 2015, which could adversely affect life insurance premiums and eligibility of City retirees.**

- **BFAAC commends the City for negotiating a new Medicare Advantage health plan that provides cost savings to Medicare-eligible retirees. Combined with a similarly structured Kaiser Medicare health plan, both plans may provide a means to off-set additional costs to employees if the City gradually phases out City-paid retiree life insurance premiums.**

- **BFAAC recommends that in the anticipated review of employee health plans Council carefully assess proposed changes in plan design, particularly those that appear to deviate substantially from health plan design in neighboring jurisdictions in a manner that imposes substantial new out of pocket costs on employees, whether they are low or high users of health care services.**

- **BFAAC recommends Council ask the City Manager to review alternatives to current plan design to assure that Alexandria's plans are competitive with those in neighboring jurisdictions and are equitable, especially for lower-paid employees.**

- **BFAAC recommends that alternatives to deductibles and high hospitalization co-payments be explored.**

- **BFAAC is pleased that the City staff has accepted and has begun implementing most of the Alexandria Fund for Human Services (AFHS) Review Committee's recommendations.**

- **BFAAC supports the Review Committee's recommendation to improve oversight and performance measures and will continue to monitor efforts by the City to implement stronger performance management measures.**

- **BFAAC supports the City's efforts in implementing a new policy not to allow City service contractors to apply for AFHS award funding to provide the same service for which it is contracted. City service contractors can still apply for AFHS funding to provide a different service.**

THE PROPOSED CAPITAL IMPROVEMENT PROGRAM (CIP)

- **BFAAC strongly supports the changes and efforts that have been made to improve the CIP budget.**

- **BFAAC encourages continued refinement by City staff to the CIP budget process in the FY 2016 budget cycle.**

- **All CIP projects (new and previously approved) should be ranked.**

- **BFAAC believes that in any significant revenue downturn, the CIP should not necessarily be held harmless. All CIP projects should be on the table as the City looks to balance short-term gaps in the operations budget with the need to sustain long-term investments through the CIP program.**

- **BFAAC recommends the Office of Management and Budget explore what other municipalities are doing to fund major CIP related efforts and consider options which may also fit in future CIP funding.**

- **BFAAC recognizes the Alexandria City Public Schools (ACPS) is working to improve its budget process and notes the City and ACPS have made progress regarding shared services to maintain and enhance CIP investments.**

- **BFAAC believes that there is a unique collaborative opportunity to refocus and refine the ACPS budget process and encourages continued efforts in this area.**

- **BFAAC encourages the City to review the *Results Alexandria* budget framework with ACPS in more detail and urge the school division to adopt a well-defined process for evaluating program performance, demonstrating how the City's investment in ACPS contributes to improvements in student learning and the general well-being of the City.**

- **BFAAC believes that CIP programs and projects should concentrate primarily on building the City's revenue base, addressing federal mandates and maintaining long term health and welfare of the City. BFAAC encourages City Council to fund CIP projects where the City can get "the biggest bang for the buck." City Council should give priority to Potomac Yard Metro, waterfront re-development, complying with the U.S. Environmental Protection Agency (USEPA) storm water management regulations, and mitigation of flash flooding.**

- **BFAAC believes the City should continue to fund the station through a variety of funding sources and continue ranking the Potomac Yard Metro Station as a critical investment in the economic viability of Alexandria.**

- **BFAAC applauds the City's efforts to fund the Potomac Yard Metro station through a variety of funding sources, including the recent application for Northern Virginia Transportation Authority funds.**

- **BFAAC recommends that all waterfront-related projects requiring capital improvement expenditures within the next 10 years be identified by placeholder project descriptions in the CIP.**

- **BFAAC continues to be concerned about the eventual cost of complying with new storm water management regulations.**

- **BFAAC observes the total cost of storm water/sewer challenges are not obvious from the current CIP and is concerned the CIP acknowledges that mid- to long-term costs are not yet taken into account.**

- **BFAAC recommends that the entire cost be calculated and that funding sources be identified. BFAAC also recommends studying how other similar jurisdictions are dealing with these issues and the magnitude of costs they have identified.**

LONG-RANGE FINANCIAL PLANNING, FUTURE FORECASTS, AND DEBT BURDEN ISSUES

- **BFAAC believes additional long-range forecasting information is critical to ensuring accurate multi-year forecasting, applauds the Office of Management and Budget for its efforts to obtain this data, and encourages additional data inputs, as determined by city staff, be included in future multi-year projections.**

- **BFAAC strongly cautions Council on future Council imposed tax rate increases in light of the need to balance the city budget over the duration of the five-year financial forecast.**

- **BFAAC recommends Council not raise the current debt policy targets and limits.**

- **BFAAC finds borrowing in excess of the City's debt policy guidelines acceptable only if the projects to be funded are essential to achieve strategic goals and result in significant long-term benefit to the City or represent the City's commitment to fulfill a prior obligation.**

- **BFAAC encourages Council to review the merits of cash vs. debt financing for capital projects and the potential effect on the annual operating budget.**

- **BFAAC recommends Council review the current debt policy guidelines and consider setting a new target based on the overall size of capital investments (cash capital and debt service) relative to the General Fund.**

I. REVENUES AND OUTLOOK

The City relies on the following sources of revenue: Residential Real Estate Tax, Commercial Real Estate Tax, other local taxes, non-tax revenue, and Federal and State revenue. Real estate taxes still account for a majority of the City's revenue (58.1 percent), with the commercial share continuing to decline. This section looks at the key revenue sources and recommends Council develop a long-term, balanced revenue plan.

A. Residential Tax and Fee Burden Issues

In 2011, Council requested BFAAC work with City staff to explore the development of new metrics to more fully track the City-imposed financial burdens on residents *and* businesses. While BFAAC now has a better picture of the residential burden (see Table I below), BFAAC still lacks data to assess the tax and fee burden on businesses.

In its 2013 report to Council, BFAAC noted the overall residential tax and fee burden had increased from 4.7 percent in FY 2011 to 5.0 percent in FY 2012[1]. As shown in Table I, the residential tax and fee burden is continuing to increase. In FY 2014, residential taxes and fees are expected to account for 5.3 percent of average household income and increase to 5.5 percent if the FY 2015 proposed budget is enacted.

BFAAC encourages Council to closely monitor this trend, particularly as additional fees or tax increases are considered. BFAAC also recommends these metrics be included in the City Manager's annual budget submission to Council. BFAAC notes the data in Table I looks at the tax and fee burden as a percentage of average household income. Going forward, BFAAC encourages City staff to also track the relative tax and fee burden for households with incomes below the average.

BFAAC recognizes the challenge of developing similar metrics for the wide range of businesses in the City, but this data would be invaluable as the City works to more effectively attract and retain businesses. The lack of these metrics makes it challenging for Council to measure how competitive the City might be when businesses are considering locating in Alexandria. As a starting point, BFAAC encourages Council to identify transparent and accurate measurements for the types of businesses the City is hoping to attract in the coming five years (*e.g.*, Alexandria Economic Development Partnership focus areas: business services, information technology and defense and security industries).

[1] Budget and Fiscal Affairs Advisory Committee review of the FY 2014 proposed budget, April 12, 2013, pages 8-9 (https://www.alexandriava.gov/uploadedFiles/budget/info/budget2014/memos/BM19BFAACReport.pdf).

Table I: Tax and Fee Burden as a Percent of Household Income in Alexandria[2]

	Actual FY 2010	Actual FY 2011	Actual FY 2012	Actual FY 2013	Approved FY 2014 *(Estimated)*	Proposed FY 2015 *(Estimated)*
Mean Household Income*	$110,485	$112,947	$110,919	$110,967	$111,016	$111,064
Fees and Taxes						
Real Estate Tax	$4,255	$4,380	$4,523	$4,575	$4,885	$5,091
Personal Property Tax	$225	$256	$303	$337	$351	$370
Trash Removal Fee	$331	$336	$336	$336	$328	$328
Decal Fee	$51	$53	$56	$53	$53	$53
Utility tax on Natural Gas	$23	$23	$22	$23	$24	$24
Utility tax on electricity	$31	$31	$30	$29	$31	$31
Utility tax on water	$24	$27	$24	$27	$25	$25
Communication Sales and Use Tax	$147	$150	$142	$142	$144	$141
Sanitary Sewer Maintenance Fee	$28	$60	$54	$57	$61	$61
Total	**$5,114**	**$5,316**	**$5,491**	**$5,579**	**$5,902**	**$6,123**
% of mean household income	**4.6%**	**4.7%**	**5.0%**	**5.0%**	**5.3%**	**5.5%**

*Data from the American Community Survey, published by the Census Bureau (1-year estimates).

FY 2013 assumes increase in personal income of 0.04% in 2012 based on the compound average growth rate FY 2008-12.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC encourages Council to closely monitor the residential tax and fee burden as a percentage of average household income.**
- **BFAAC recommends Council also track the residential tax and fee burden for households with incomes below the average.**
- **BFAAC recommends the City Manager track the residential tax and fee burden and include the metrics in the City Manager's annual proposed budget submission to Council.**
- **Any increase in fees or taxes should be carefully considered, particularly with income levels remaining flat.**

[2] Data in Table provided by City staff at the request of BFAAC.

B. Commercial Tax Base

BFAAC's FY 2013 and FY 2014 reports noted the continued and growing imbalance between residential and commercial property tax revenues. Although the commercial share in CY 2014 is expected to account for 43.4 percent of property tax revenue, as BFAAC has previously noted, when multifamily housing is counted on the residential side, the commercial share falls to 25.9 percent.[3]

Chart I: Percentage of Real Estate Assessments by Property Type (CY 2013 and 2014)[4]

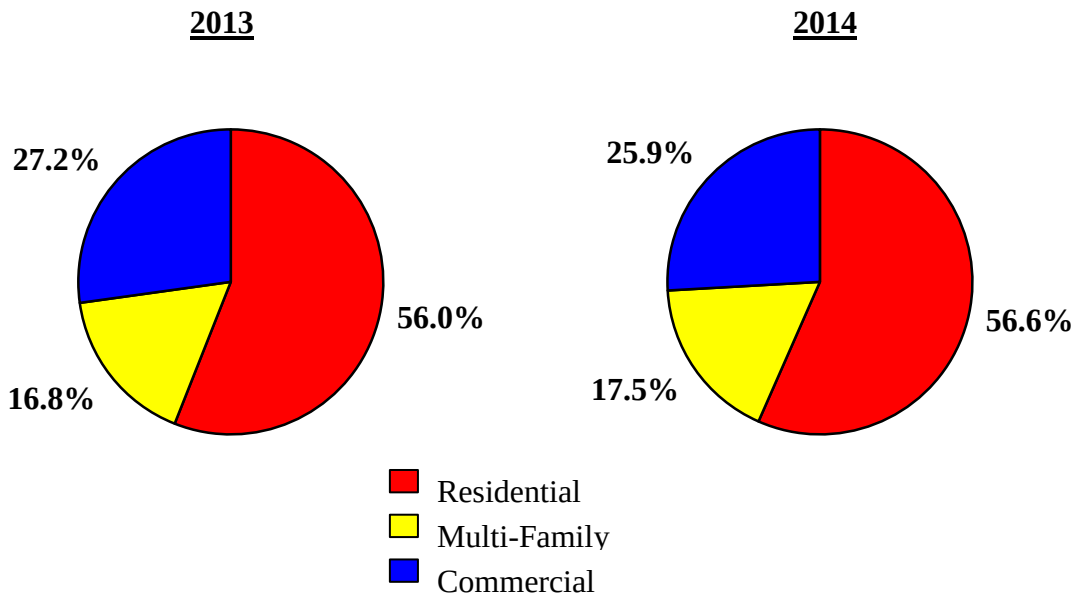
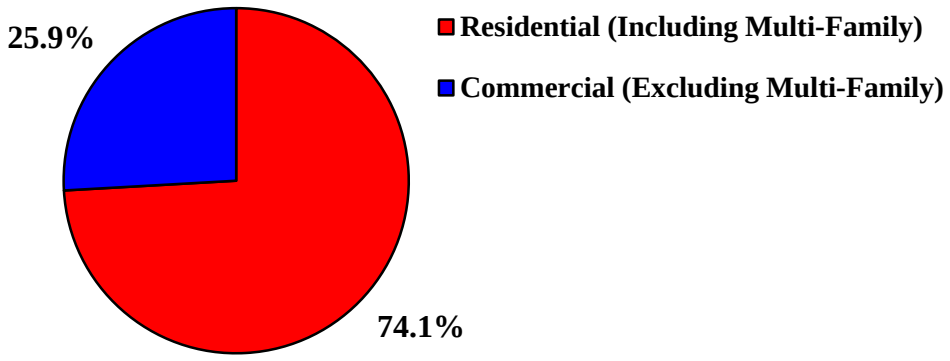


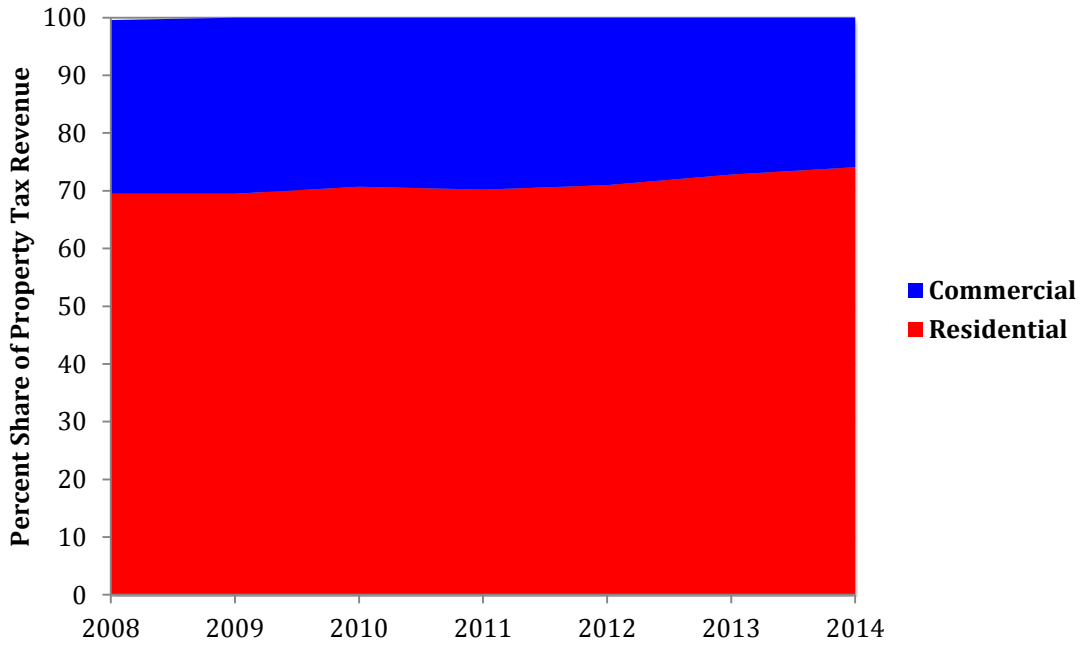
Chart II: Percentage of Real Estate Assessments by Property Type with Multi-Family Counted as Residential Property (CY 2014)[5]



[3] City of Alexandria Proposed FY15 Operating Budget, 6.9.
[4] Ibid.
[5] Ibid.

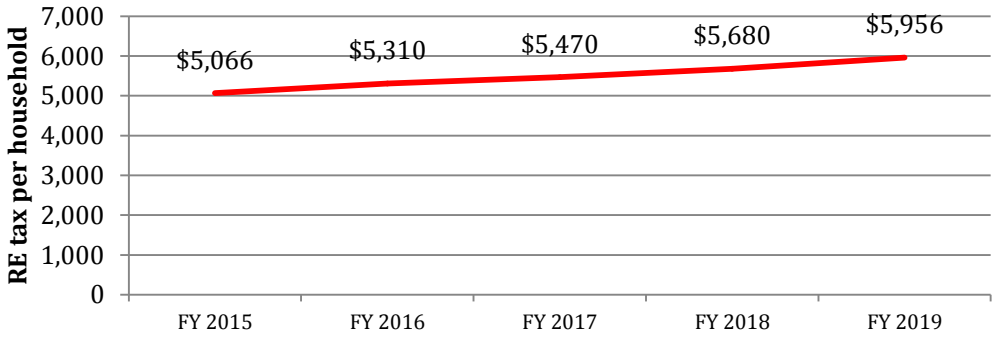
BFAAC notes the commercial share of property tax revenue has steadily declined since 2011. The commercial share has dropped by 4.2 percent since CY 2011 (from 30.1 percent to 25.9 percent) and 1.3 percent from CY 2013 to CY 2014 (from 27.2 percent to 25.9 percent).

Chart III: Percentage of Real Estate Assessments by Property Type (CY 2008-14) with Multi-Family Counted as Residential Property[6]



The drop in commercial revenue continues to place a greater burden on residents to fund the City's operations. As illustrated in Chart IV below, if the commercial base does not grow, the average resident's property tax bill would need to increase by nearly $900 over the next five years to sustain current City services. [7]

Chart IV: Average Real Estate Tax Per Household Necessary to Sustain Current Services (No Change in Policy)

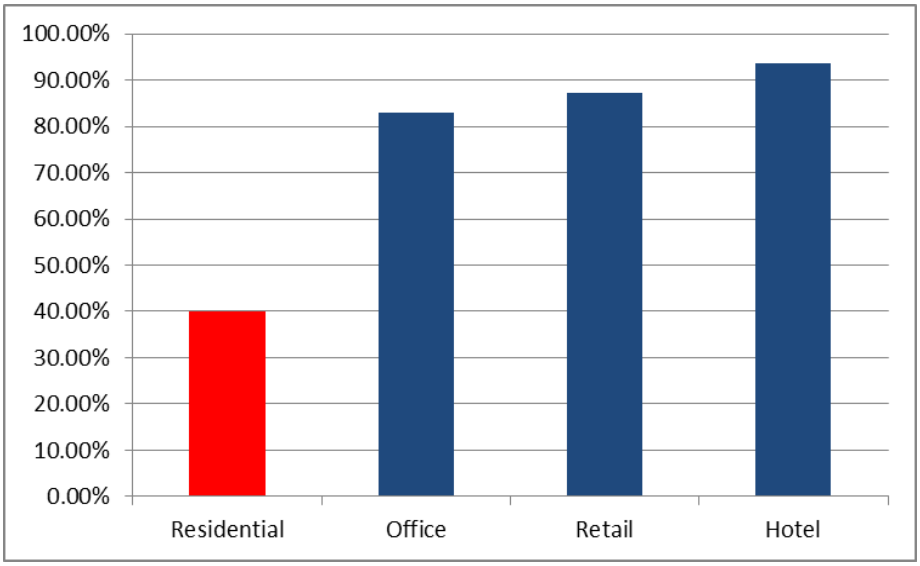


[6] Ibid.

[7] Chart developed by City Staff at the request of BFAAC.

As reported last year, commercial development generates far more revenue for the City net of operating and capital costs than residential development (Chart V below). BFAAC continues to urge Council to explore further the challenges of commercial development in Alexandria. Whether it is the tax rate, lack of public transportation or type of office space (Class A vs. Class B) in desirable locations, BFAAC encourages Council to identify the key challenges and take action to make commercial development a priority.

Chart V: Percent of Tax Dollars Generated Net of City and School Operating and Capital Costs by Property Type[8]



BFAAC commends City staff for implementing a five-year financial plan and forecasting model for better decision-making. This effort proves particularly critical in understanding the long-term revenue picture and the impact of policy decisions on the City's revenue base. With the systemic imbalance between the residential and commercial tax bases, policy decisions will have a net positive revenue impact only if sustained over time. BFAAC recommends including a long-term revenue strategy as part of the new financial plan. A long-term revenue strategy, addressing a five-year time horizon at the minimum, will establish the foundation for the City's future fiscal stability.

A long-term revenue plan would address the residential/commercial tax base imbalance by quantifying the challenges behind stimulating business activity, and estimating the resulting business tax revenue. In June 2013, Council approved a request from Councilmembers Lovain, Smedberg, and Wilson to form a study group to make recommendations on, among other actions, changes to the Business Professional Occupation License (BPOL) tax, the business personal property tax, or "any other revenue stream that will promote business growth and align to the City's strategic economic development objectives."[9] The City Manager subsequently formed the Business Tax Reform Task Force (BTRTF), whose report is being delivered to Council contemporaneously with BFAAC's report. Analyzing a wealth of business activity data, the BTRTF found, over the past decade and prior to the start of the Great Recession in 2008-09, business activity in Alexandria has declined. As a consequence,

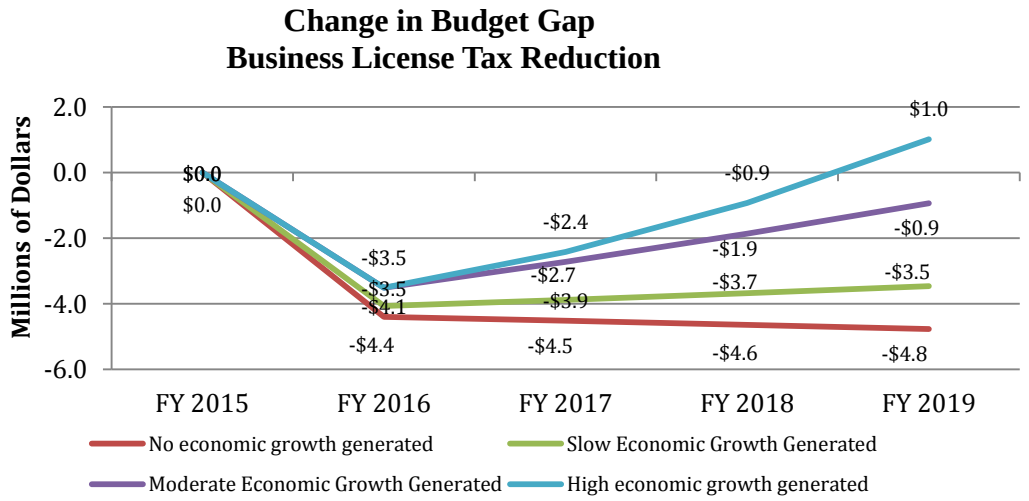
[8] AEDP provided data (2013) at the request of BFAAC.
[9] City of Alexandria Memorandum "Business Tax Reform," June 25, 2013, p. 2.

business tax revenues have stagnated at below pre-recession levels.[10] Given this stagnation, BFAAC encourages Council to consider policy and administrative actions to significantly shift the ratio of residential and commercial shares of the tax base.

BFAAC examined the revenue and cost implications of the BTRTF's recommendation to reduce the BPOL tax rate across all impacted business categories by one cent below Arlington's corresponding rates (over a two year period). The BTRTF recommended this reduction as part of a larger package of recommendations to stimulate business activity in Alexandria by making the City a comparatively more attractive place to do business.[11]

City staff used the five-year forecasting model to assess the impact of more robust business activity resulting from the BTRTF-proposed BPOL tax reduction (beginning in FY 2016 versus the BTRTF's recommended FY 2015) and consequent higher business tax revenues. Although the forecasting model should be refined to better gauge the sensitivity of business activity to policy changes, the budget gap scenarios show increased economic growth can narrow the existing residential-commercial tax base gap. Under various growth scenarios the budget gap could increase to $4.8M by FY 2019, but it could also close completely should sufficient economic growth, spurred by additional policy and administrative initiatives along with other factors, occur (see Chart VI below).

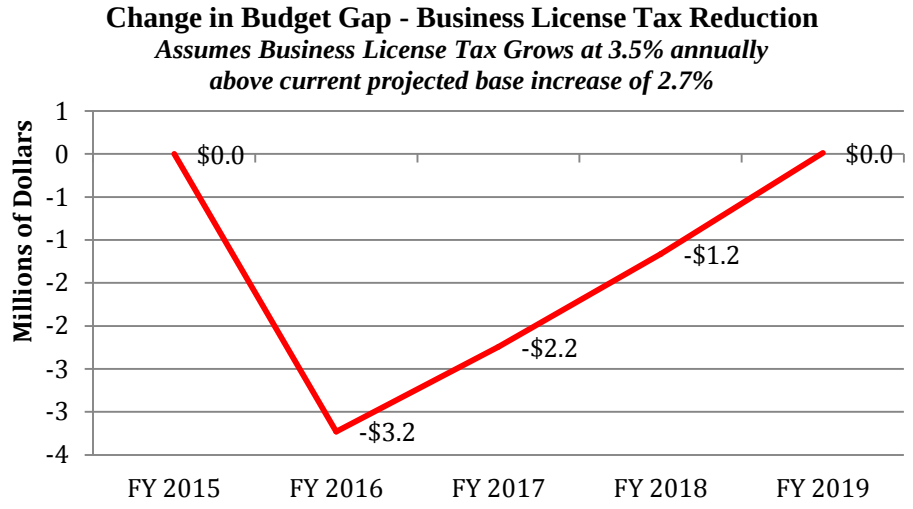
Chart VI: Change in Budget Gap with Economic Growth Scenarios, FY 2015 - 2019 with Reduction in BPOL Tax Rates to One Cent Below Arlington's Rates Initiated in FY 2016[12]



Although the model presents a diverse revenue picture for the slow, moderate, and high growth scenarios, the budget gap is reduced under each scenario over time, indicating that such a tax rate reduction is projected to spur expanded business activity. To fully offset the cost of the proposed BPOL reduction by FY 2019, business license tax must grow at 3.5 percent annually above the current projected base increase of 2.7 percent (see Chart VII below).

[10] City of Alexandria Business Tax Reform Task Force Final Report, February 19, 2014, p. 4.
[11] City of Alexandria Business Tax Reform Task Force Final Report, February 19, 2014, p.16.
[12] Ibid.

Chart VII: Change in Budget Gap, FY 2015 - 2019 with Reduction in BPOL Tax Rates to One Cent Below Arlington's Rates Initiated in FY 2016[13]



The above analysis further underscores the need for a long-term revenue plan and a sustained commitment to implementing the plan. Expanding the City's commercial base will increase revenue generated from the commercial portion of real estate tax and reduce the burden on the residential share of real estate tax to fund City operations. As the FY 2015 Operating Budget reflects, a low rate of economic growth will require a significant increase in the residents tax rate (to 1.22 cents per $100 of assessed value) by FY 2019 to maintain budget balance, while a high rate of economic growth, through an expanded business base, is projected to result in a lower residential tax rate over the same period.[14] The systemic nature of the residential-commercial tax base imbalance necessitates both a near-term start and a long-term commitment to sustained policy and administrative changes.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC encourages Council to develop metrics to track the commercial tax and fee burden. While BFAAC recognizes it will be a challenge to identify common metrics for the wide range of businesses in the City, BFAAC encourages Council to start with metrics appropriate for the types of businesses the City is hoping to attract in the coming five years.**

- **BFAAC cautions Council to continue monitoring the declining percentage of commercial (excluding commercial multi-family) assessments relative to residential and multi-family assessments. If the goal is to obtain a 50/50 balance, Council should work with Alexandria Economic Development Partnership (AEDP), Planning and Zoning, and other stakeholders to develop a tactical plan to grow the commercial base under the City's land use plans.**

[13] City of Alexandria, "BPOL Scenarios," Analysis Conducted for BFAAC, March 28, 2014.
[14] "Forecast Scenarios," City of Alexandria FY 2015 Proposed Budget, p. 5.6.

- **BFAAC commends the City staff for developing a five-year financial plan and forecasting model, and recommends the development of a long-term revenue plan to guide decision-making.**

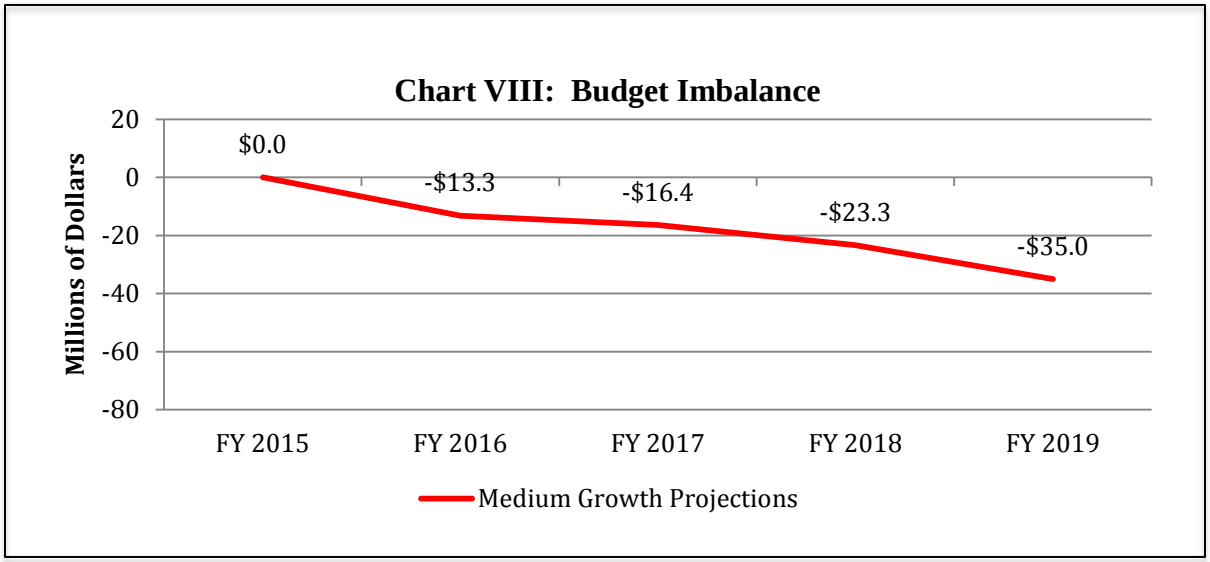
- **BFAAC recommends enriching the forecasting model with additional data that will permit more sensitive analysis of the revenue impact of policy decisions over the longer-term.**

- **BFAAC encourages Council to undertake policy and administrative actions designed to stimulate business activity in the City.**

- **BFAAC recommends Council provide AEDP with the resources to proactively attract businesses to the City and the appropriate authority to utilize economic development incentives.**

C. Options to Grow Revenue Base

The City's revenue picture is not expected to improve in the short-term. Under a medium growth scenario, costs will outpace revenues each year from FY 2016-2019 (Chart VIII below).



The Council is faced with three options to address this gap: cut operating costs, increase revenue (taxes and fees), or grow the base. BFAAC recognizes there is no easy option. As discussed, BFAAC recommends a long-term effort to grow the commercial base and reduce the burden on residents to fund the City's operating costs.

Growing the commercial tax base will not be easy – it will not happen quickly and will likely increases costs in the short- to medium-term. In the short-term, the main tools available to Council continue to be spending reductions and revenue increases. As illustrated in Chart VIII above, even maintaining existing services would require a substantial increase in the average resident's property tax bill. BFAAC encourages Council to consider alternative revenue sources, including a Payment In Lieu Of Taxes (PILOT) initiative and special assessments for public works projects.

PILOTs are voluntary payments made by tax-exempt organizations to partially make up for the loss in property tax revenue that tax-exempt organizations do not otherwise pay. A 2010 review found PILOTS are used by more than 117 municipalities in 18 states.[15] While PILOTs can take many forms, they are generally voluntary, one-time agreements that are negotiated between tax exempt organizations (usually hospitals, private schools, large non-profit organizations, etc.) and municipalities.[16]

Alexandria has $206 million in property owned by hospitals, $401 million by private schools and faculty residences, and $315 million by charities. Although PILOTs have the potential to raise revenue to help offset the cost of City services provided to tax-exempt organizations, any PILOT program should be carefully considered and narrowly targeted. Just like the City, many nonprofits are facing difficult financial times, and PILOT payments may reduce the capacity of tax-exempt organizations to meet their missions. PILOTS may also make it harder for the City to retain and grow its vibrant base of tax-exempt organizations. If Council decides to consider a PILOT initiative, additional research would need to be conducted to determine the City's authority in this area.

One of the criticism of PILOTs is they are ad-hoc and there is often a large variance in the level or participation by tax-exempt organizations. An alternative approach would be utilizing a special assessment or user fee that would be applied to the existing tax base and potentially targeted types of tax-exempt organizations. For example, revenue for trash collection and road maintenance could be collected as a fee instead of through the property tax. [17] Such a fee could also be limited to short-term public works costs such as sewer repairs.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC encourages Council to consider alternative revenue sources and recommends a further review be conducted to determine the merits of a PILOT initiative or special assessment approach.**

- **BFAAC recognizes the important services nonprofit organizations provide and urges Council to proceed cautiously.**

[15] Kenyon, Daphne A. and Langley, Adam H. 2010. *Payments in lieu of taxes: Balancing municipal and nonprofit interests.* Cambridge, MA: Lincoln Institute of Land Policy.
[16] Kenyon, Daphne A. and Langley, Adam H. 2011. *The Municipal Fiscal Crisis and Payments in Lieu of Taxes by Nonprofits.* Cambridge, MA: Lincoln Institute of Land Policy.
[17] Ibid.

II. FY 2015 BUDGET PROCESS

A. *Results Alexandria*

On April 5, 2012, Council received the annual report from BFAAC, detailing BFAAC's observations regarding the FY 2013 Alexandria City Budget. During BFAAC's discussion of the City's Long Range Budget Outlook, BFAAC noted the need for cost containment throughout the city in order to slow the growth of operating budget costs. BFAAC encouraged the city to examine additional areas for cost containment in order to enhance efficiencies and improve service delivery.[18]

In October 2012, the City introduced *Results Alexandria*, a performance management system that emphasized three key areas in order to focus resources and achieve results: accountability, transparency, and informed decision-making.[19] *Results Alexandria* is designed to be a cyclical quality improvement process with six different decision stages that allows the City to "allocate resources toward programs that help achieve common outcomes and reset performance targets to reflect changing levels of investment."[20]

In FY 2015, as part of *Results Alexandria*, BFAAC observes the City moving to a grouping of functions within four "Focus Areas" to achieve maximum return on city investments:

- Focus Area #1 - Accountable, Effective, and Well-Managed Government;
- Focus Area #2 - Healthy and Thriving Residents;
- Focus Area #3 - Livable, Green & Prospering City, and;
- Focus Area #4 - Safe, Secure, and Just Community

BFAAC has been briefed by the City Manager and the Budget Director on the transition to *Results Alexandria*, which BFAAC understands is an ongoing effort. Given BFAAC's past recommendations for better performance measures as a means to evaluate the efficiency, effectiveness, and prioritization of City expenditures and to achieve cost control, BFAAC is encouraged by the ongoing transition to *Results Alexandria*. BFAAC believes the process that the new system is using to determine City budget levels is an improvement over previous budget development tools.

Of particular note, BFAAC is quite interested in *AlexStat* which, according to the proposed budget:

> *(O)ffers a standardized, analytic approach to improving performance within the City by: focusing leaders' attention on issues critical to the success of the City Strategic Plan, City Manager's Performance Plan, and Department Work Plans; providing rigorous analysis of performance data; creating a forum to understand and discuss the effectiveness of core City services; and prompting, monitoring, and tracking action on recommendations.*[21]

---

[18] Budget Memo #27, BFAAC Review of the Proposed FY 13 Budget, p. 6, April 2, 2013.
[19] FY 2015 City Manger's Proposed Budget, p. 3.3.
[20] FY 2015 City Manager's Proposed Budget, p. 3.5.
[21] FY 2015 City Manager's Proposed Budget, p. 3.4.

BFAAC believes that the *AlexStat* system holds great promise in delivering accurate analytical information to City decision makers in order to support more informed budgetary choices. BFAAC looks forward to information generated by *AlexStat* as it examines future budget proposals.

Given the promise of *Results Alexandria*, BFAAC is concerned that the scope of *Results Alexandria* is not consistent across focus areas. Although all entities receiving city funds were engaged in the budget development process in some manner, only those city departments reporting directly to the City Manager were subject to the *Results Alexandria* performance measurement process. According the City's Office of Management and Budget (OMB), over 20 different entities that do not report directly to the City Manager but do receive some level of City funding did not have *Results Alexandria* performance metrics applied to their budgets. Thus, of the City's $634.8 million dollar budget, $220.5 million, or roughly 35% of total city expenditures, was not subject to the performance metrics required by *Results Alexandria*. Chart IX details the application of the *Results Alexandria* performance measurement process across focus areas.

While BFAAC understands some organizations receiving city funds are not subject to the *Results Alexandria* performance measurement process (e.g., Washington Metro Area Transit Authority), BFAAC nevertheless believes that organizations that receive any city funding should have metrics, targets and goals that can be easily communicated to Alexandria's taxpayers. In addition, since 35% of Alexandria's budget is not under the direct control of the City Manager, the accounting of those expenditures to the citizens falls directly onto Council to ensure those funds are managed.

BFAAC strongly encourages Council to closely examine city expenditures not subject to the *Results Alexandria* performance metrics and demand a high level of budgetary rigor for those entities receiving city funding, but not directly accountable to the City Manager. Unless 100% of Alexandria's budget can be accurately measured and evaluated, *Results Alexandria* will only give Council a partial picture into the overall financial health of the City and be a results assessment tool for only approximately 65% of Alexandria's budget.

Chart IX – *Results Alexandria* Participation by Focus Area

Focus Area	Participating Fully (Dept. Work Plan + Performance Measures for Programs)		Partial Participation (Performance Measures for budget book only)		Not Participating (No Dept. Work Plan, No Measures)	
Accountable, Effective and Well-Managed Government	City Attorney	$2,768,749	Non-Departmental	$87,023,075	City Council	$515,815
	City Clerk and Clerk of Council	$425,944			Animal Welfare League of Alexandria	$1,064,255
	City Manager	$2,083,690				
	Communications	$2,213,928				
	Finance (including Real Estate)	$13,519,701				
	General Services	$12,550,922				
	Human Resources	$3,933,587				
	ITS	$9,348,392				
	Performance & Accountability (including Internal Audit)	$863,882				
	Management and Budget	$1,265,046				
Healthy and Thriving Residents	Community and Human Services	$48,448,558			ACPS	$190,611,472
	Health	$6,144,044			Northern Virginia Community College	$11,877
	Library	$6,658,057			Alexandria Fund for Human Services Grantees (through DCHS)	$1,921,430
	Recreation, Parks & Cultural Activities	$20,761,260			Arts Grantees (through RPCA)	$177,730
					Other Health (Coroner's Office, ANHSI, INOVA, Dental Services, Coroner's Office)	$1,765,350
Livable, Green and Prospering City	Code Administration	$120,000	Small Business Development Center (SBDC)	$279,225	DASH	$11,142,000
	Housing	$2,438,468			DOT Paratransit	$1,330,328
	Historic Alexandria	$2,913,433			King Street Trolley	$1,025,000
	Planning and Zoning	$6,322,919			Virginia Railway Express (VRE)	$133,894
	Project Implementation	$2,053,865			WMATA	$6,375,156
	Transportation and Environmental Services	$31,443,110			Other Economic Development Activities	$167,000
	Alexandria Economic Development Partnership (AEDP)	$1,463,277				
	Alexanddria Convention and Visitior Association (ACVA)	$3,197,353				
Safe, Secure and Just Community	Court Service Unit	$1,542,654	Circuit Court	$1,578,593	Adult Probation and Parole	$289,071
	Emergency Communications	$7,197,239	General District Court	$62,452	Alternative Community Service Program	$20,000
	Fire	$43,806,789	Juvenile and Domestic Relations District Court	$36,129	Northern Virginia Criminal Justice Traning Academy	$571,949
	Human Rights	$703,818	Commonwealth Attorney	$2,761,293	Northern Virginia Juvenile Detention Home	$1,287,435
	Police	$55,445,255	Clerk of Circuit Court	$1,616,542	Office of the Magistrate	$158,174
	Sheriff	$30,072,886	Law Library	$0	Peumansend Regional Jail	$421,289
			Registrar of Voters	$1,275,660	Office of the Public Defender	$529,791
					Sheltercare Program	$972,299
Totals		$319,706,826		$94,632,969		$220,491,315
$634,831,110						

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC is encouraged by the ongoing transition to *Results Alexandria* and believes the process that the new system is using to determine City budget levels is an improvement over previous budget development tools.**

- **BFAAC believes that the *AlexStat* system holds great promise in delivering accurate analytical information to City decision makers in order to make informed budgetary choices.**

- **BFAAC is concerned the scope of *Results Alexandria* is not consistent across focus areas.**

- **BFAAC believes that organizations that receive any City funding, even if they fall outside the scope of *Results Alexandria*, should have metrics, targets and goals that can be easily communicated to Alexandria's taxpayers.**

- **BFAAC strongly encourages Council to closely examine city expenditures not subject to the *Results Alexandria* performance metrics and demand a high level of budgetary rigor for those entities receiving city funding, but not directly accountable to the City Manager.**

B. Performance Criteria and Needs-based Budgeting

The City Manager's proposed budget introduces the use of performance criteria for each program area, providing information on service use and in some cases their impact and effectiveness. BFAAC commends the City Manager for the adoption of performance criteria for assessing the value of City services.

As management tools, performance criteria are an important addition to the City's ability to assure quality and effectiveness of services. From a budget perspective, they can be helpful as well. If a service is shown to not be used or is ineffective, it may be a candidate for either greater investment or elimination.

These performance criteria do not, however, address a concern BFAAC has had for many years, which is how to set priorities within departments and focus areas and across them. In order to set priorities and to make informed decisions, it is important to *identify the extent of the need for a service and the extent to which the proposed budget and staffing meets identified need.* Performance criteria are not designed to serve this critical budget decision-making function.

Information on need and the extent to which need is met does not eliminate budget choices because it will be impossible to meet all service needs. But, a greater understanding of the need would provide citizens and Council a basis to make decisions on an acceptable service level. In some cases, Council could expect that 100% of need is met; in others, a small percentage of need met would suffice.

This year's budget demonstrates the importance of needs-based criteria as a complement to performance criteria. For example, it would be helpful to know how many individuals are in need or meet eligibility criteria for detox services, Head Start, adult protective services, residential placement for persons with intellectual facilities, compared to how many receive such services. In park operations and capital improvement, there are performance criteria for visits for parks, but it could be helpful to know the numbers or acres of parks considered acceptable for a population of Alexandria's size and where the City stands on that measure.

Because this information has not been available, Council has often had to make difficult decisions on service enhancements and reductions without knowing fully whether the decisions are in accordance with the City's goals, values and policies. In our current environment of severe budget constraints, knowing the extent of need and the current level of need met should be considered an essential foundation for making budget decisions.

For example, the City Manager proposes to eliminate three fire marshal positions. Performance criteria indicate that the proposed decrease will reduce the number of fires/hazards investigated by almost half. In evaluating this proposed reduction, it would be helpful to Council to know whether the proposal is based on a judgment that the City does not need to have the number of investigations carried out this year, or whether it represents a recommendation to meet only half the need for investigations. Need could be assessed either directly, by patterns of hazards or fires over time, or by proxy measures, such as extent of commercial development.

Decisions on enhancements could be more informed with needs-based presentations. For example, the City Manager proposes to increase funding for the King Street trolley by $195,000 to begin trolley operations to 10 a.m. instead of 11:30 a.m. and also to expand operating hours later on weekends. Although from a performance standpoint, increasing hours will increase ridership, as the City Manager explains, a key question is the extent of need for increased ridership in the hours contemplated, as measured by criteria such as tax revenues generated and attractiveness of the City. If the answer is that the significant expense will have only a marginal impact on meeting needs, or that most of the need is already being met, Council might decide to spend the funds on services where percentage of met need is much lower.

This needs-based approach would help Council address a question BFAAC has often raised in the past about setting priorities within and across areas of the strategic plan. For example, if an increased expenditure results in a marginal increase in needs met, or that Council was satisfied with meeting a certain level of need, an enhancement would be a low priority. By contrast, if a reduction significantly lowered the percentage of need met in a program Council deems of great importance, it might be inclined not to make the reduction.

BFAAC recognizes that for some programs need assessments will be very difficult. In others however, information is available either from knowledge within the City or community (e.g., how many older adults are in need of support services, the demand for Head Start) or can be gleaned from national standards on a population's basis.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC commends the City Manager for including performance criteria in evaluation for budgeting and other purposes.**

- **BFAAC urges Council to direct the City Manager's proposed budget for FY 2016 include identification of needs for services and the percentage of need met in current programs and proposed spending.**

C. Budget Alignment with the Alexandria City Public Schools (ACPS)

In the FY 2012 BFAAC report, BFAAC wrote:

> *Overall, BFAAC is concerned about the process and timeline by which ACPS delivers a capital improvement program and an operating budget to City Council. While we acknowledge some of the constraints on the development of an annual operating budget by ACPS, we believe those constraints should not necessarily preclude the timely preparation of a school budget.*[22]

In the FY 2013 budget development process, the Alexandria School Board again did not deliver a school budget to the City Manager prior to the budget presentation to Council and the Alexandria taxpayers. As a result, in the FY 2013 BFAAC report to Council, BFAAC reiterated its concern and "recommend Council not proceed with any school budget deliberations in future fiscal years without the receipt of a capital improvement program and an operating budget from ACPS by the City Manager before he presents his budget to Council." [23]

In both FY 2014 and FY 2015, this practice continued. For FY 2015, City Manager Young released his budget to Council on February 25, yet the Alexandria School Board did not approve its budget until March 5. Further, BFAAC observes that the Alexandria School Board's own "FY 2015 Budget Calendar" did not attempt to align with the City Manager's budget development process, but operated outside the budget development timeline set by the City Manager in fall 2013.[24] This dual budget development process has resulted in a $2.7 million dollar shortfall in the ACPS operating budget request and an approximate $37 million dollar shortfall in the capital improvement program request. The ACPS shortfall now must be addressed by Council.

Having noted this budget process misalignment for at least four budget cycles, BFAAC continues to reiterate that this is simply an unacceptable budget practice. Considering the pattern has been repeated for several fiscal years, the delivery of an ACPS budget after the City Manager's presentation to Council is now accepted as standard operating procedure and an expected part of the budget deliberation process. BFAAC believes, and has stated in previous reports, that this misalignment creates an untenable situation during the annual budget discussions and one that can be avoided by both elected bodies.

---

[22] FY 2012 BFACC Report to City Council, p. 10.
[23] FY 2013 BFAAC Report to City Council, p. 8.
[24] FY 2015 Budget Calendar for ACPS, http://www.acps.k12.va.us/budgets/op2015/budget-calendar.pdf.

Further, BFAAC urges the Council and School Board to rectify the misalignment in order to avoid an adversarial relationship between the bodies. During joint work sessions between Council and the School Board this year, BFAAC members have observed both Council and School Board members arguing over levels of funding that, frankly, could have been resolved had the School Board and Council been more coordinated as their budgets were in development. Since BFAAC first observed the budget development misalignment four years ago, BFAAC believes the process has not improved but has only exasperated an already difficult budget discussion.

Given the reality that resources will continue to be constrained in the future, BFAAC reiterates and strongly recommends the realignment of the city and school division's budget development process.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC notes that the budget development processes of the Alexandria City Public Schools and the City are misaligned.**

- **BFAAC believes, and has stated in previous reports, that this misalignment creates an untenable situation during the annual budget discussions and one that can be avoided by both elected bodies.**

- **BFAAC urges the Council and School Board to rectify the misalignment in order to avoid an adversarial relationship between the bodies.**

- **BFAAC reiterates and strongly recommends the realignment of the City and ACPS budget development processes.**

D. Budgetary Impact of "Add-Deletes"

OMB has briefed BFAAC on a new procedure regarding councilmember "add-deletes." For the first time ever, initial councilmember "add-deletes" to the City Manager's budget will be evaluated against a five-year forecast in order to see both long-term costs and / or savings associated with those changes. BFAAC is encouraged by this new "add-delete" procedure and looks forward to the results of the long-term projections of "add-deletes," as it will add another layer of data from which councilmembers may make budgetary decisions.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC has been briefed on a new "add-delete" procedure, whereby initial councilmember "add-deletes" to the City Manager's budget will be scored against a five-year forecast in order to see both long-term costs and/or savings associated with those changes.**

- **BFAAC is encouraged by this new "add-delete" procedure and looks forward to the results of the long-term projections of "add-deletes," as it will add another layer of data from which councilmembers may make budgetary decisions.**

III. THE PROPOSED OPERATING BUDGET

A. Retiree Life Insurance

The City Manager's Proposed FY 2015 Budget shifts the cost of retiree life insurance premiums from the City to the retiree. The annual cost to the City to provide this benefit is $264,598.[25] There is also an Other Post Employment Benefit (OPEB) actuarial liability of $12 million that must be funded if retiree life insurance premiums continue to be paid by the City. This discussion focuses only on premiums paid for retirees and not those provided for active employees. OMB estimates the average cost per retiree to keep existing coverage is $21 per month, ranging from a low of $0.48 to a high of $88.57 per month.[26]

Since 1979, the City has provided life insurance coverage for retired employees.[27] They have also allowed employees to purchase additional insurance at pooled rates. The benefit and premium is reduced by 25% at age 65, then 10% per year until the participant reaches age 70, at which time the total calculation is 25% of the original benefit and premium amount. Eligibility for coverage is limited to retirees who were full-time City employees, were hired by the City before July 1, 2009, and are receiving a pension from the Virginia Retirement System (VRS), City of Alexandria Supplemental Retirement Plan (SRP), or Alexandria Firefighters and Police Officers Pension Plan (FPOPP). Employees hired on or after July 1, 2009, are not eligible for City-funded life insurance when they retire.

Although the City reports that present levels of coverage for retirees will not be adversely affected by this proposal, BFAAC notes there is potential risk that current preferred group rates might change when the City's contract with the provider expires in March 2015. BFAAC does not know yet whether the City intends to renegotiate the present contract when it expires, or whether there is reason or incentive for either the City or the provider to do so once the payment of premiums is transferred to retirees. If individual retiree eligibility is reevaluated without City involvement and group rates are no longer available, some retirees could be required to pay higher premiums because of age or other reasons. Others may lose their eligibility altogether because of disqualifying off-duty injury or disability incurred during their careers with the City.

There are currently 1,043 retirees covered by the City's group life insurance policy. 658 of covered retirees are 60 years of age and older. The annual premium cost to the City for this group is approximately $150,000. The remaining $114,598 of the annual premium cost to the City funds 385 retirees under the age of 60. 1,911 current employees hired before July 1, 2009, remain eligible for this benefit if they retire from active service meeting the current eligibility requirements.

The City notes that as of January 1, 2014, 203 Medicare-eligible retirees have chosen to participate in a new Medicare Advantage health plan that will reportedly reduce their health care premiums and eliminate deductibles.[28] Kaiser has offered a similar plan with comparable premiums for several years. The inference from City staff is that these savings will more than offset the cost that retirees 65 years of age and older will pay to continue their life insurance

[25] FY 2015 Budget Memo # 3, Retiree Life Insurance.
[26] Ibid.
[27] Source: OMB E-mail Communication to BFAAC, March 19, 2014.
[28] FY 2015 Budget Memo # 3, Retiree Life Insurance

benefits. BFAAC commends the City for negotiating this plan with UnitedHealthcare. Assuming that projected cost savings are accurate for the new Medicare Advantage Health Plan (MAHP) and similarly structured Kaiser Medicare Health Plan, both may provide a means to offset the additional costs to employees if the City gradually phases out City-paid life insurance premiums, and transfers the cost of these premiums to each retiree who enrolls in either the MAHP or Kaiser Plans.

Pension pay rates are an important component of any retirement compensation package as are the companion benefits. They are often viewed by retirees as economic promises made by the City to employees who decide to join the workforce, promises that employees plan on during long careers, and well into retirement. This view was first presented to Council in the 2011 Ad Hoc Retirement Benefit Advisory Group Report, which stated that whether one accepts or does not accept the validity of employee expectations based on earlier actions by the City or Council, "the fact of these expectations needs to be taken into account in considering changes to employee pension coverage."[29] BFAAC agrees, attaches significant weight to long-standing retirement benefits promised to employees at time of hire, and encourages the City to examine alternatives that prevent imposing an immediate cut of City funded retiree life insurance premiums.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC encourages the City to examine alternatives that prevent imposing an immediate cut of City funded retiree life insurance premiums.**

- **BFAAC is concerned that the advantages of a City-sponsored plan with negotiated group rates will be lost after March 2015, which could adversely affect life insurance premiums and eligibility of City retirees.**

- **BFAAC commends the City for negotiating a new Medicare Advantage health plan that provides cost savings to Medicare-eligible retirees. Combined with a similarly structured Kaiser Medicare health plan, both plans may provide a means to off-set additional costs to employees if the City gradually phases out City-paid retiree life insurance premiums.**

B. Employee Health Insurance

In BFAAC's FY 2014 report, BFAAC strongly urged the City Manager not to institute a health insurance change for City employees that imposed substantial new deductibles and co-payments, whether they are low or high users of services, and that he consider alternatives to deductibles and high hospitalization co-payments.

However, the proposed health plan changes were adopted, and BFAAC's and employees' concerns were addressed by a $750,000 pay supplement to employees in FY 2014 due to a health plan redesign. In FY 2015, the City Manager proposes to leave the plan design changes BFAAC found problematic in place and proposed not to renew the supplement.

[29] AD HOC Retirement Advisory Group Report, November 11, 2011, pg.69

The City Manager has informed BFAAC that in the coming year, staff will review health coverage offerings again and make changes to conform to the Affordable Care Act, which has a July 1, 2015 implementation date for the City. The City has also hired a new broker, Aon Hewitt, to provide expertise in plan design options and to manage the competitive bidding process for health insurance products. Additionally, the City Manager has informed BFAAC that the City is actively pursuing establishment of a no-deductible HMO option with Kaiser for the FY 2015 open enrollment period.

In considering future plans and plan design, BFAAC urges Council and the City Manager to follow the recommendations in BFAAC's report last year on plan design, particularly regarding employee co-pays and deductibles.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC recommends that in the anticipated review of employee health plans Council carefully assess proposed changes in plan design, particularly those that appear to deviate substantially from health plan design in neighboring jurisdictions in a manner that imposes substantial new out of pocket costs on employees, whether they are low or high users of health care services.**

- **BFAAC recommends Council ask the City Manager to review alternatives to current plan design to assure that Alexandria's plans are competitive with those in neighboring jurisdictions and are equitable, especially for lower-paid employees.**

- **BFAAC recommends that alternatives to deductibles and high hospitalization co-payments be explored.**

C. Non-Profit Partnerships

The City of Alexandria has had a long-standing relationship with the non-profit community. In recent years, through the Alexandria Fund for Human Services (AFHS), the City has provided grant awards of approximately two million dollars to support local non-profits providing services to underserved communities in Alexandria, particularly youth and families.

After Council discussions on the direction of AFHS, in July 2013, City staff appointed a Review Committee composed of Alexandria residents to examine the work of AFHS. This Review Committee examined the AFHS grant application and award process, performance measurement and monitoring, alignment with the City's Strategic Plan and community indicators, and other topics. Over the summer, the AFHS Review Committee sought input from Alexandria's non-profit community about how it felt AFHS was working for their organizations. The Review Committee presented a report with findings and recommendations to the City Manager in November 2013 and later presented its report to Council.

The AFHS Review Committee offered ten recommendations for strengthening the AFHS and better aligning awards with the City's Strategic Plan.[30]

[30] Report of the Alexandria Fund for Human Services Review Committee, November 2013, Pg. iv.

On November 25, 2013, Council subsequently included language in Resolution 2586 "Setting Guidance for FY 2015 General Fund Operating Budget and Capital Improvement Program for FY 2015 – FY 2024"[31] directing the City Manager to incorporate the recommendations of the AFHS Review Committee in the proposed budget.

BFAAC is pleased that the City staff has accepted and has begun implementing most of the Review Committee's recommendations. As the City's budget becomes increasingly tight, it is especially important that city funds for grant awards be more aligned with the City's Strategic Plan, the City Manager's Performance Plan and other Council approved planning documents.

BFAAC understands one of the main issues raised by Alexandria non-profit stakeholders is maintaining a multi-year grant award for recipients, and concurs with the City that moving to a three-year grant award term starting in FY 2016 would enhance service by ensuring program continuity over a longer period of time. Of course, with longer grant award periods, the City's oversight, monitoring, and measuring of grant performance will need to be robust to ensure taxpayer dollars are well spent. BFAAC supports the AFHS Review Committee recommendation to improve oversight and performance measures, and will continue to monitor efforts by the City to implement stronger performance management measures.

Finally, the AFHS Review Committee found during its review process that some City service contractors received AFHS funding awards to supplement their funding for the same service. The Review Committee found this 'double-dipping' phenomenon troubling since it was not always clear to grant reviewers that a particular organization was already the recipient of a City contract. The AFHS Review Committee urged the City to provide greater transparency into its financial awards to contractors and grant recipients. BFAAC supports the City's efforts in implementing a new policy not to allow City service contractors to apply for AFHS award funding to provide the same service for which it is contracted. City service contractors can still apply for AFHS funding to provide a different service.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC is pleased that the City staff has accepted and has begun implementing most of the AFHS Review Committee's recommendations.**

- **BFAAC supports the Review Committee's recommendation to improve oversight and performance measures and will continue to monitor efforts by the City to implement stronger performance management measures.**

- **BFAAC supports the City's efforts in implementing a new policy not to allow City service contractors to apply for AFHS award funding to provide the same service for which it is contracted. City service contractors can still apply for AFHS funding to provide a different service.**

[31] City of Alexandria, "Setting Guidance for FY 2015 General Fund Operating Budget and Capital Improvement Program for FY 2015 – FY 2024," Pg. 3.

IV. THE PROPOSED CAPITAL IMPROVEMENT PROGRAM

A. Overview

BFAAC commends the City Manager and OMB for taking past BFAAC recommendations into consideration in the development of the FY 2015 budget. BFAAC believes the FY 2015 Capital Improvement Program (CIP) formulation and presentation deserve high marks and supports the direction that the CIP budget presentation is heading.

The CIP project priority setting process is more understandable, and BFAAC is pleased efforts are being made to anticipate the impact CIP projects have on the operating budget. The CIP's impact on the operating budget can be substantial especially when major CIP projects come on-line.

BFAAC observes that the CIP ranking process has been refined. Evaluation criteria with which each project is ranked is provided in Appendix C and project priority rankings for 181 projects out of a total of 225 are included in Appendix D.[32] BFAAC commends the City Manager for clearly outlining the CIP budget priorities. Project descriptions and justifications are improved and clearly cited. The linkage to the City's strategic plan and the City Manager's Performance Plan are better outlined, and BFAAC appreciates the greater concentration on outcome targets.

<u>OBSERVATIONS AND RECOMMENDATIONS:</u>

- **BFAAC strongly supports the changes and efforts that have been made to improve the CIP budget.**

- **BFAAC encourages continued refinement by City staff to the CIP budget process in the FY 2016 budget cycle.**

B. Analysis of the FY 2015 CIP Process

1. Project Priority Ranking

In BFAAC's view, one of the most critical budget tools to make informed budget decisions is ranking CIP projects in relation to each project's impact, need, and benefit to the public. BFAAC strongly supports the City Manager's priority ranking efforts.

BFAAC recommends that the overview of the CIP rankings also include an aggregate ranking of the major program categories which the CIP projects support, especially for the given budget year (FY 2015) - e.g., transportation, recreation and parks, IT plan, community development, sanitary sewers/storm water, public buildings, ACPS (capacity and non-capacity), courts, fire and police.

The rationale for not funding some higher ranked programs over lower ranked programs should be addressed in a footnote to the project ranking appendix. For example, in

[32] City of Alexandria, Virginia, Proposed FY 2015-2024 Capital Improvement Program, Appendix C: Project Evaluation Criteria (p. 16-9 and p. 16-10) and Appendix D: Project Rankings (p. 16-11 through p. 16-15).

Transportation, a materials yard security program is ranked higher than public art acquisition. Yet, public art requisition is funded for $3.5 million, and the security program is not funded. CIP should make reference in a footnote as to what additional criteria/factors to those articulated in the Appendix C were used in making the decision not to fund certain higher ranked projects.

BFAAC recommends that projects already approved prior to FY 2015 also be ranked. There are 49 current projects out of 225 that are not ranked. If there were to be a significant revenue shortfall, these previously approved projects as well as the current proposed projects should not necessarily be held harmless.

2. Financial Models That Address Similar CIP Projects

BFAAC recommends the City should explore alternative funding sources and mechanisms that other jurisdictions use to fund major CIP programs aside from additional real estate taxes (e.g., storm water enterprise fund; surtax on state income tax; developer share; equitable fees for all properties (limited or no exemptions)).

<u>OBSERVATIONS AND RECOMMENDATIONS</u>:

- **All CIP projects (new and previously approved) should be ranked.**

- **BFAAC believes that in any significant revenue downturn, the CIP should not necessarily be held harmless. All CIP projects should be on the table as the City looks to balance short-term gaps in the operations budget with the need to sustain long-term investments through the CIP program.**

- **BFAAC recommends OMB explore what other municipalities are doing to fund major CIP related efforts and consider options which may also fit in future CIP funding.**

C. ACPS and the CIP Process

BFAAC has struggled with the ACPS portion of the City's budget. BFAAC observes that the joint work sessions between Council and ACPS leadership do not seem to address the key issues raised by the ACPS budget request. Examples include items such as a $36.4 million dollar difference in CIP calculations between the City Manager's and the School Superintendent's budgets; past reprogramming of funds; and disagreement on the cost assessments related to building maintenance and new construction.

The joint Long Range Educational Facilities Planning work group can play an important role in building consensus on CIP planning to: accommodate rising student enrollment; evaluate the adequacy of existing buildings for delivering educational programs and services; and augment facilities in ways that contribute to the City's overall public space.

BFAAC recognizes ACPS is working to improve its budget process and notes the City and ACPS have made progress regarding shared services to maintain and enhance CIP investments. BFAAC believes that there is a unique collaborative opportunity to refocus and refine the ACPS budget process and encourages continued efforts in this area.

As BFAAC previously noted we believe the *Results Alexandria* program instituted by the City has greatly improved the City's budget process. BFAAC encourages the City to review the *Results Alexandria* budget framework with ACPS in more detail and urges the school division to adopt a well-defined process for evaluating program performance, demonstrating how the City's investment in ACPS contributes to improvements in student learning and the general well-being of the City.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC recognizes ACPS is working to improve its budget process and notes the City and ACPS have made progress regarding shared services to maintain and enhance CIP investments.**

- **BFAAC believes that there is a unique collaborative opportunity to refocus and refine the ACPS budget process and encourages continued efforts in this area.**

- **BFAAC encourages the City to review the *Results Alexandria* budget framework with ACPS in more detail and urge the school division to adopt a well-defined process for evaluating program performance, demonstrating how the City's investment in ACPS contributes to improvements in student learning and the general well-being of the City.**

D. CIP Programs Impact on Specific Projects

BFAAC believes that CIP programs and projects should concentrate primarily on building the City's revenue base, addressing federal mandates and maintaining the long term health and welfare of the City. BFAAC encourages City Council to fund CIP projects where the City can get "the biggest bang for the buck." City Council should pay particular attention to Potomac Yard Metro, waterfront re-development, complying with the U.S. Environmental Protection Agency (USEPA) storm water management regulations, and mitigation of flash flooding.

In light of the budget impact of specific, long-term projects currently under discussion in Alexandria, BFAAC offers the following observations:

1. Potomac Yard Metro Station

BFAAC wrote at length about the proposed Potomac Yard Metro Station in the FY 2014 report to Council. As was stated last year, BFAAC continues to support the City's efforts to promote construction of an infill Metro station to serve the Potomac Yard and Del Ray neighborhoods and a future commercial town center.

BFAAC applauds the City's efforts to fund the station through a variety of funding sources, including the recent application for Northern Virginia Transportation Authority funds, a new source that was previously unavailable. BFAAC believes the City should continue to fund the station through a variety of funding sources and continue ranking the Potomac Yard Metro Station as a critical investment in the economic viability of Alexandria.

2. Federal Storm Water Sewer Compliance

BFAAC continues to be concerned about the cost of complying with new storm water management regulations promulgated by the USEPA including the expenses that will result from the need to separate the City's large network of combined sewers. BFAAC observes the total cost of storm water/sewer challenges are not obvious from the current CIP and is concerned the CIP acknowledges that mid- to long-term costs are not yet taken into account.

BFAAC recommends that the entire cost be calculated and that funding sources for Federal storm water sewer compliance be identified. BFAAC also recommends studying how other similar jurisdictions are dealing with these issues and the magnitude of costs they have identified.

3. Waterfront

As a result of the adoption of the Waterfront Small Area Plan, the need for flood prevention, and anticipated new development on the waterfront, a large number of individual projects will be identified and their cost impact will be analyzed over the next few years. Many projects will require support through the capital improvements budget in the areas of flood control and mitigation; construction of new docks and piers; construction of landscape elements including sidewalks, plazas, gardens, and lighting; and construction of public buildings. It is unknown today what the cost of these projects will be, as the supporting studies are still underway and recommendations have not yet been adopted.

BFAAC recommends that all projects requiring capital improvement expenditures within the next 10 years be identified by placeholder project descriptions in the CIP. BFAAC recommends the project description include a description of the project, where it fits within the Small Area Plan, its likely timeframe, implementation challenges, and a general cost estimate.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC believes that CIP programs and projects should concentrate primarily on building the City's revenue base, addressing federal mandates and maintaining long term health and welfare of the City. BFAAC encourages City Council to fund CIP projects where the City can get "the biggest bang for the buck." City Council should give priority to Potomac Yard Metro, waterfront re-development, complying with the USEPA storm water management regulations, and mitigation of flash flooding.**

- **BFAAC believes the City should continue to fund the station through a variety of funding sources and continue ranking the Potomac Yard Metro Station as a critical investment in the economic viability of Alexandria.**

- **BFAAC applauds the City's efforts to fund the Potomac Yard Metro station through a variety of funding sources, including the recent application for Northern Virginia Transportation Authority funds.**

- **BFAAC recommends that all Waterfront-related projects requiring capital improvement expenditures within the next 10 years be identified by placeholder project descriptions in the CIP.**

- **BFAAC continues to be concerned about the eventual cost of complying with new storm water management regulations.**

- **BFAAC observes the total cost of storm water / sewer challenges are not obvious from the current CIP and is concerned the CIP acknowledges that mid- to long-term costs are not yet taken into account.**
- **BFAAC recommends that the entire cost be calculated and that funding sources be identified. BFAAC also recommends studying how other similar jurisdictions are dealing with these issues and the magnitude of costs they have identified.**

V. LONG-RANGE FINANCIAL PLANNING, FUTURE FORECASTS, AND DEBT BURDEN ISSUES

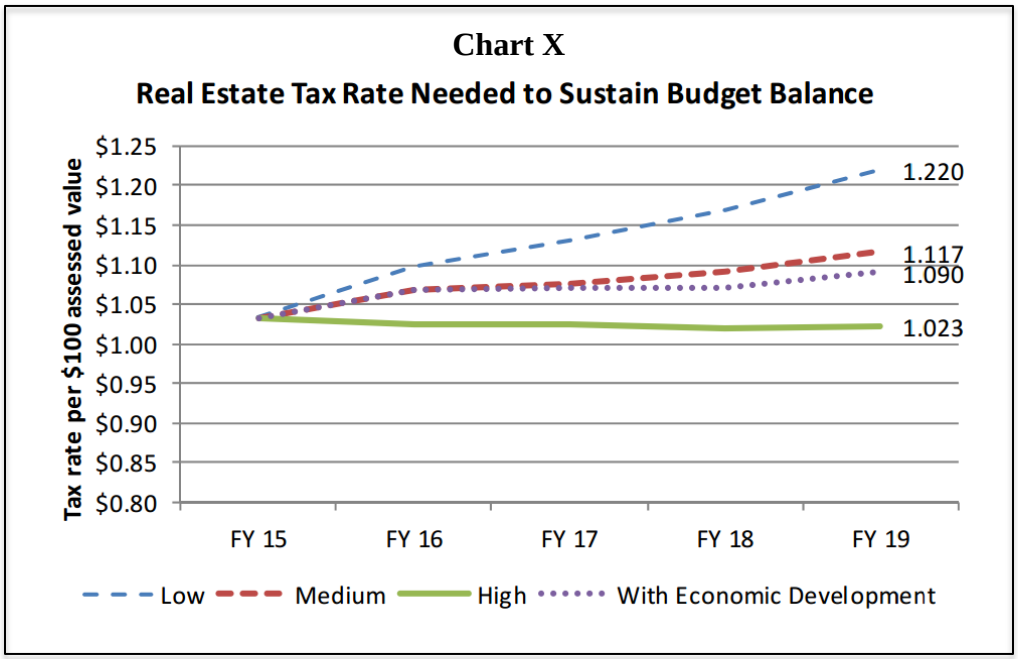
A. Long-Range Financial Plan

As the City continues to improve the budget development and evaluation process, one of the areas of focus is in multi-year revenue and expenditure projections. Traditionally, the City Manager's budget has included projections for high, medium and low growth, and these projections allowed Council and City staff the ability to roughly anticipate future surpluses and shortages. This year, however, BFAAC notes an increased emphasis on the data included in the multi-year forecast.

Of particular note, the new forecast model now includes "the impact of the operating budget of projects in the CIP, the impact on future operating budgets of past and current policy changes, and a more detailed estimate of the future economic growth based on specific land use and development plans underway or under consideration."[33] BFAAC believes this information is critical to ensuring accurate multi-year forecasting, applauds the Office of Management and Budget for its efforts to obtain this data, and encourages additional data inputs, as determined by city staff, be included in future multi-year projections.

B. Future Forecasts and Tax Rate Projection

Given that the City has focused on its multi-year revenue and expenditure projections, one of the advantages of better data for forecasting is the ability to project the required tax rate to balance the city budget under various growth scenarios. In examining the high, medium and low growth scenarios, City staff has projected the necessary tax rate to be paid by taxpayers and the results are illuminating.



With the impact of future revenues from new development included in the projection, excluding the high growth scenario, City Council will be forced to raise the real estate tax

[33] FY 2015 City Manager's Proposed Budget, p. 5.1.

rate every year in order to sustain a balanced budget for FY 2016 through FY 2019. Given that Alexandria has historically not achieved the high growth scenario, it is reasonable to assume that Council will need to consider tax rate increases, on top of increases from real estate assessments; every year it considers a budget over the five-year forecast horizon.

With this information in hand, BFAAC recommends Council be mindful of future Council imposed tax rate increases. Since taxpayers will likely see increased taxes from rising property values already, adjusting the tax rate up to balance the budget is, in essence, asking Alexandria citizens to pay twice. BFAAC will continue to monitor the trend in the real estate tax needed to balance the budget and encourages Council to carefully consider future tax rate changes in light of improved future forecasting data.

C. Debt Policy Guidelines

BFAAC has long supported adherence to City debt policy guidelines as an important tool in promoting financial discipline and ensuring maintenance of Alexandria's AAA/Aaa bond rating. The guidelines include three benchmarks against which the magnitude of borrowing can be assessed for its impact on the City's fiscal condition: (1) debt as a percent of real property assessed value; (2) debt service as a percent of general government expenditures; and (3) debt as a percent of personal income. For each of these benchmarks, the City sets both targets and limits.

In its last four reports, BFAAC noted that at some point over the ten-year budget window, all three metrics approach or exceed the limits. BFAAC reiterates its concern that this borrowing trajectory will crowd out operating budgets.

When the Potomac Yard Metro station and the sanitary sewer upgrades are <u>included</u> the City will <u>exceed its limits</u> for debt service as a percent of general government expenditures and debt service as a percent of personal income in FY 2016 and beyond. However, without the Potomac Yard Metro Station and when excluding exempt Sanitary Sewer debt, the City does stay within the debt limits for each category in each year of the 10-year plan. City staff has informed Council and rating agencies of the City's plan to do this, and both have supported the Potomac Yard Metro Station plan to date.

As in prior years, BFAAC finds borrowing in excess of the City's debt policy guidelines acceptable only if the projects to be funded are essential to achieving strategic goals, resulting in significant long-term benefit to the City, or representing the City's commitment to fulfill a prior obligation.

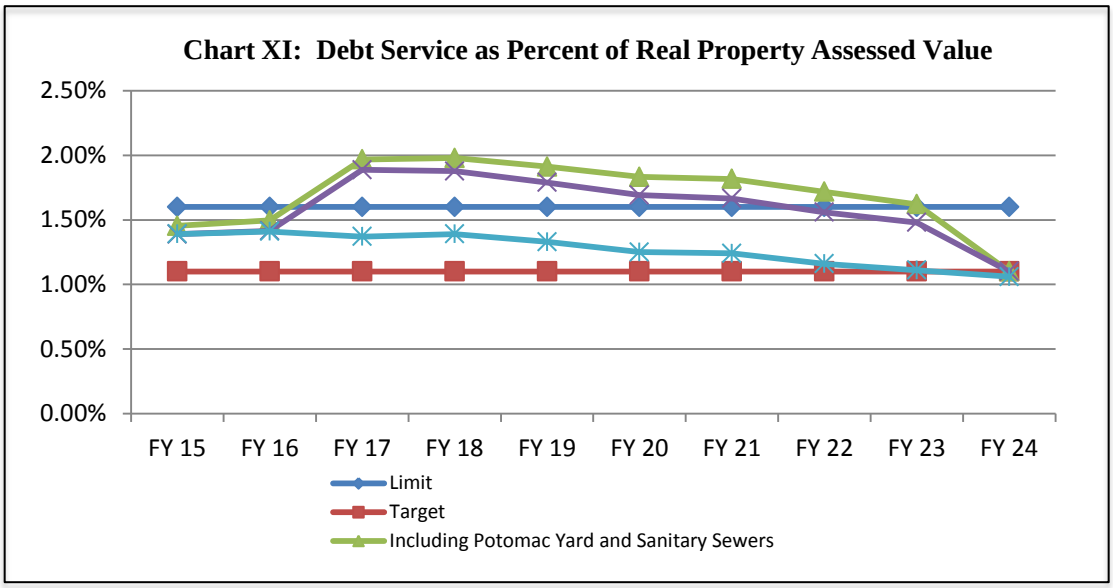


Chart XI: Debt Service as Percent of Real Property Assessed Value
2.50%
2.00%
1.50%
1.00%
0.50%
0.00%
FY 15
FY 16
FY 17
FY 18
FY 19
FY 20
FY 21
FY 22
FY 23
FY 24
Limit
Target
Including Potomac Yard and Sanitary Sewers

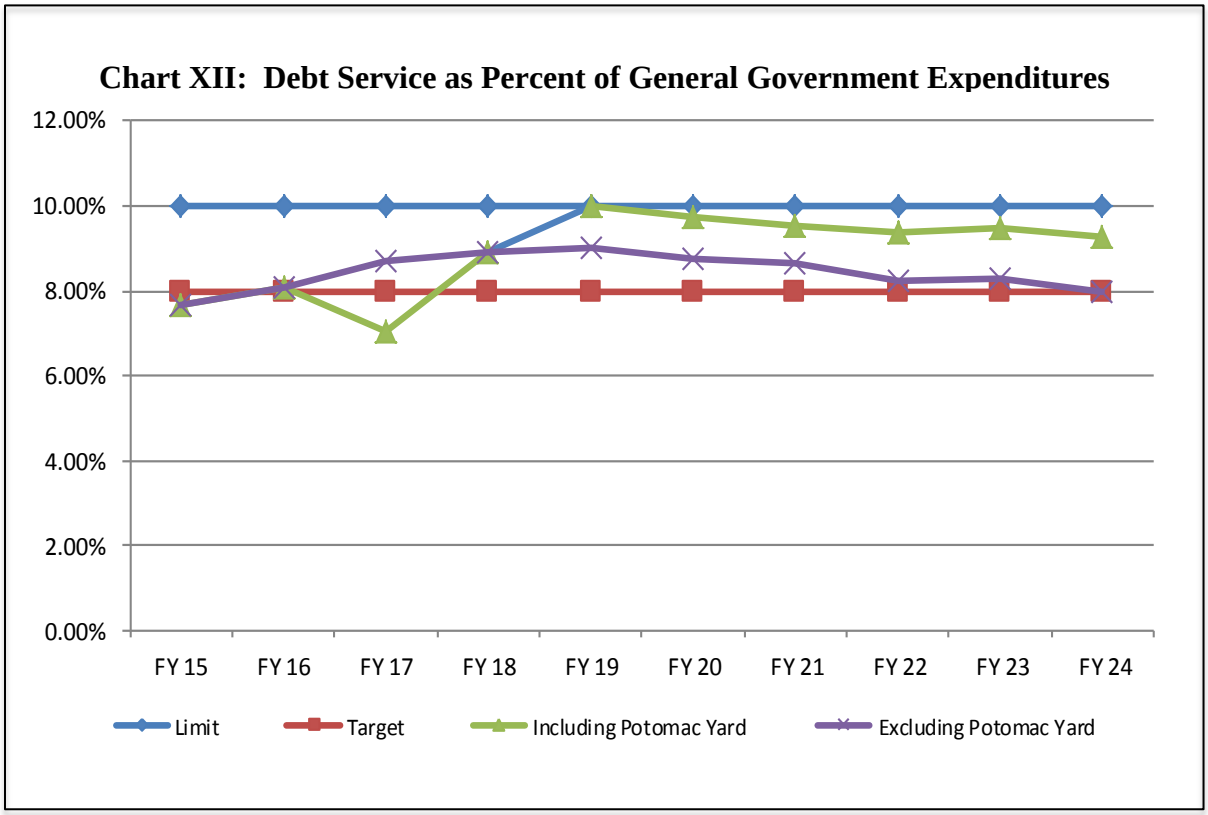
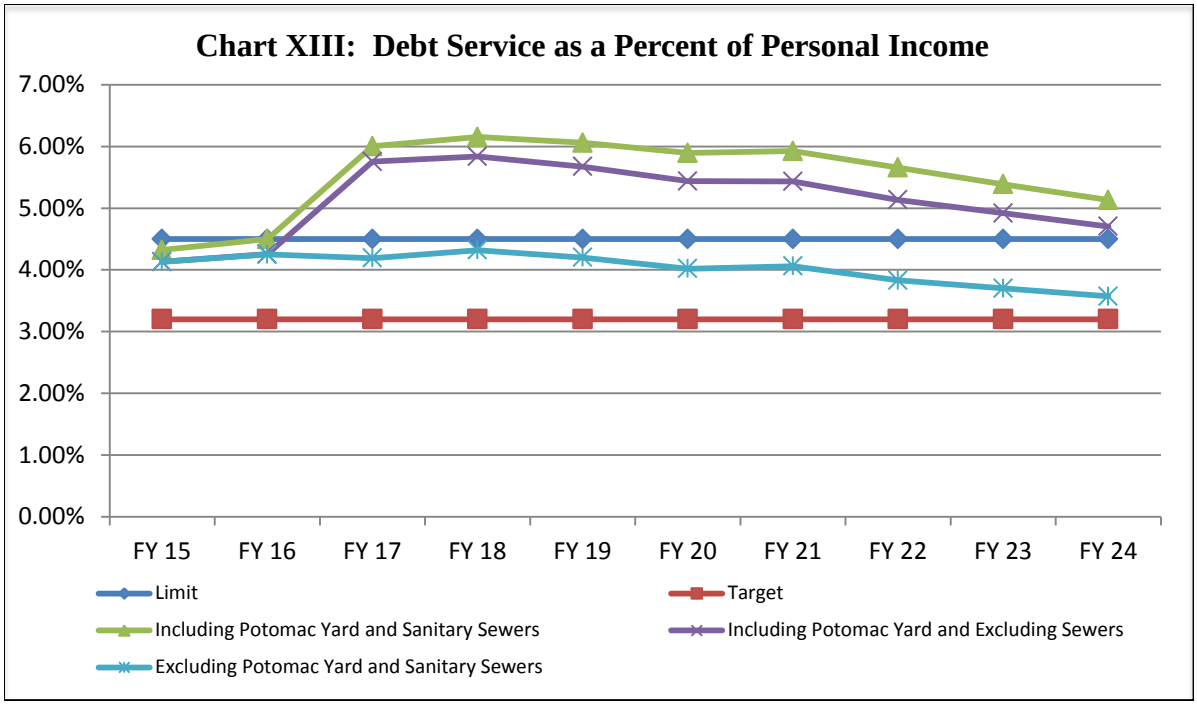
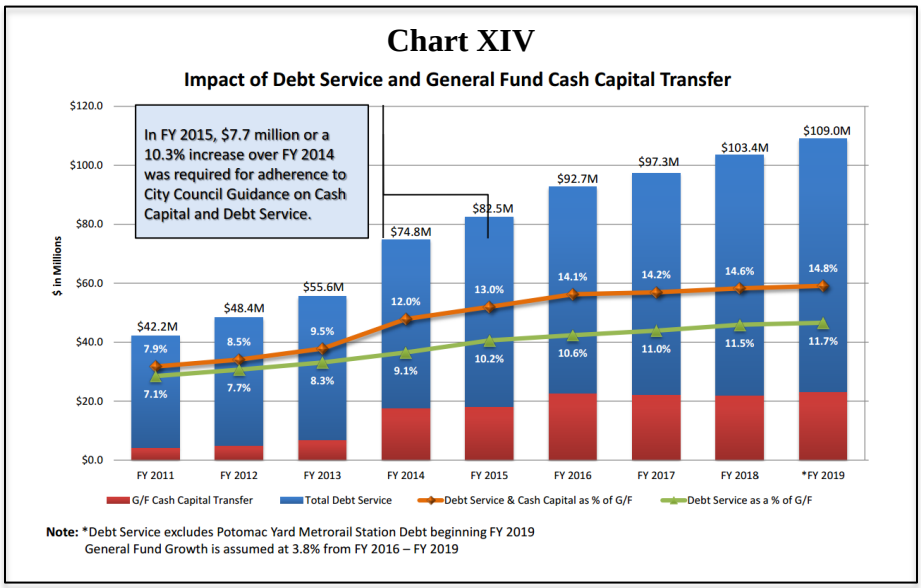


Chart XII: Debt Service as Percent of General Government Expenditures
12.00%
10.00%
8.00%
6.00%
4.00%
2.00%
0.00%
FY 15
FY 16
FY 17
FY 18
FY 19
FY 20
FY 21
FY 22
FY 23
FY 24
Limit
Target
Including Potomac Yard
Excluding Potomac Yard



BFAAC encourages Council to consider developing better tools to look at the operational impacts of long-term capital investments. As shown in Chart XIV below, in FY 2015 debt service and cash capital account for $82.5 million – 13 percent of the General Fund. The amount of money dedicated to debt service and cash capital as a percent of the General Fund has steadily increased, and BFAAC is concerned this trend is not sustainable. Although the City's current debt limit is relatively conservative, raising the debt limit will not address the long-term trend of growth in the cash capital and debt service costs relative to the General Fund.



BFAAC encourages Council to review the merits of cash vs. debt financing for capital projects and the potential effect on the annual operating budget. BFAAC also recommends Council review the current debt policy guidelines and consider setting a new target based on

the overall size of capital investments (cash capital and debt service) relative to the General Fund.

OBSERVATIONS AND RECOMMENDATIONS:

- **BFAAC believes additional long-range forecasting information is critical to ensuring accurate multi-year forecasting, applauds the Office of Management and Budget for its efforts to obtain this data, and encourages additional data inputs, as determined by city staff, be included in future multi-year projections.**

- **BFAAC strongly cautions Council on future Council imposed tax rate increases in light of the need to balance the city budget over the duration of the five-year financial forecast.**

- **BFAAC recommends Council not raise the current debt policy targets and limits.**

- **BFAAC finds borrowing in excess of the City's debt policy guidelines acceptable only if the projects to be funded are essential to achieve strategic goals and result in significant long-term benefit to the City or represent the City's commitment to fulfill a prior obligation.**

- **BFAAC encourages Council to review the merits of cash vs. debt financing for capital projects and the potential effect on the annual operating budget.**

- **BFAAC recommends Council review the current debt policy guidelines and consider setting a new target based on the overall size of capital investments (cash capital and debt service) relative to the General Fund.**