City of Alexandria, Virginia

MEMORANDUM

DATE: APRIL 20, 2005

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: JAMES K. HARTMANN, CITY MANAGER

SUBJECT: BUDGET MEMO # 82: AUTOMATIC TRIGGER TO REDUCE REAL ESTATE TAX RATE

This is in response to Councilman Gaines' question whether the City has the ability to create a policy whereby assessment increases automatically trigger a reduction in the tax rate in order to generate the same amount of revenue so that increases in assessments do not automatically raise additional revenue and real estate tax bills.

Nothing in the Virginia statutes or the City charter would prevent the Council from adopting a policy directive. However, it would have to be implemented annually through the City Manager's proposed budget and Council's subsequent approval of the budget and setting of the real estate tax rate. Of course, by statute Council does have to approve a balanced budget each year, so such a self-imposed restriction, if adhered to by the Council during any particular budget year deliberation, would have to be matched by an equivalent restraint in expenditures.

There are several technical questions that would have to be addressed before such a policy were adopted. For instance, would an allowance be made for added assessments due to new construction, so that the additional tax revenue due to new construction could be added to the budget, while only the additional revenue to be gained by increases in assessments would be negated by a reduction in the tax rate. Would the effects of ordinary inflation be considered in allowing for an increase in total real estate tax revenues? Would the effects of population growth be considered? Would the Council provide a procedure for an override of the real estate tax rate calculated by this method in order to fund programs and activities that Council wished to fund? Would that procedure require a simple majority or a super majority?

Staff is sympathetic to the need to temper the increasing reliance on increases in residential real estate taxes to fund the budget. However, staff does not recommend such a course of action for four basic reasons:

1. Council's deliberations on the budget each and every year reflect a balancing of the needs of the community with the community's ability to afford meeting those needs. Each year

presents a different set of circumstances that require the Council's judgement on how to balance the budget.

2. The City faces statutory limitations on its ability to diversify its revenue sources beyond the real estate tax. Those other sources of revenue are often at the mercy of economic and regional trends and pressures outside of the City's control. When those other revenue sources are growing at a robust rate, the need for real estate tax revenues is less and real estate tax rates can be more easily lowered. When those other revenue sources are declining or stagnant, the City may need to rely proportionately more on real estate tax revenues.

3. The real estate tax rate is a crucial variable in determining the budget for any fiscal year. If it is locked in at a particular level too early in the budget process, or made difficult to change, the unintended consequences on meeting the many needs of residents for a wide variety of City services will be unpredictable and may be significant.

4. The history of formulaic, automation rigid tax or assessment limitation policies is not positive. Whether it be Proposition 13 in California, the TRIM limitations in Prince Georges County, MD, Colorado's TABOR (Taxpayer Bill of Rights) laws, or Massachusetts Proposition 2.5, over time these laws have hamstrung and damaged the ability of State and local governments to meet their resident's needs (see budget memo #14).

While automatic triggers are likely to cause more problems than solutions, there are processes by which Council could provide more fiscal policy guidance at the beginning of its budget process each year (such as at Council's fall retreat). This budget and tax policy guidance option has been raised by Council recently and will be the subject of a forthcoming budget memo.