

Memorandum

To: County Board of Arlington, Virginia **Date:** April 4, 2017
From: Mark Schwartz, County Manager
Subject: Mid-year / 3rd Quarter Review of Fiscal Year 2017

Summary

This report summarizes the status of changes to the Fiscal Year (FY) 2017 budget and adjustments to Fiscal Year 2018 from the estimates provided in the County Manager's Proposed Budget. The latest analysis of the County's revenues and expenses for FY 2017 indicates that the FY 2017 budget will be balanced at fiscal year-end and \$3.8 million in additional one-time funds will be available for County Board consideration. In addition, minor adjustments have been made to the projections for FY 2018. For purposes of completing work on the pending budget, the Manager recommends that the \$3.8 million in FY 2017 funds be set aside by the Board for either land acquisition, as a cushion against potential Federal fund reductions, or one-time tax relief. The Manager also recommends allocating the additional \$0.2 million in ongoing funds for FY 2018 as an offset to the proposed two cent tax increase. (Summaries of these proposals are found at the end of this report).

	FY 2017 Incremental Change Over Adopted Budget (One- Time) (\$ millions)	FY 2018 Incremental Change Over Budget (Ongoing) (\$ millions)	FY 2018 Incremental Change Over Budget (One- Time) (\$ millions)
Revenue			
Real Estate Tax Revenue (at Current Tax Rates & net of Crystal City & Columbia Pike Tax Increment Financing Areas)	(\$0.4)		
Personal Property	1.9		
BPOL	4.5		
Other Tax Revenue	1.5		
Sub-Total Taxes (0.8% change)	\$7.5		
Non-Tax Revenue	2.3	\$0.2	\$(0.2)
Total Revenue	\$9.8	\$0.2	\$(0.2)
Expense Adjustments			
Debt Service Savings	\$0.7		

TOTAL MID-YEAR/ 3rd Qtr. FUNDS AVAILABLE	\$10.5		
Transfer to Schools (46.6% share of tax revenue)	(3.5)		
County Share of Mid-Year/3rd Qtr. Funds	\$7.0		
Proposed Allocations Made as Part of Proposed FY 2018 Budget in February 2017	(2.8)		
AHIF Portion of Recordation Tax Per County Board Historical Practice	(0.4)		
BALANCE AVAILABLE, April 2017	\$3.8	\$0.2	\$(0.2)

FY 2017:

The most significant source of one-time funding in the current year (beyond that assumed at budget adoption in April 2016) is due to additional Business, Professional & Occupational License (BPOL) tax revenues. The majority of those taxes are received in mid-March 2017 through early April 2017. Full details are provided in the table on page five. Total tax revenue changes \$7.5 million, which represents only a 0.8% change from the adopted budget.

In February, as part of the proposed budget, some of these revenue changes (\$2.8 million) were identified. The \$2.8 million includes unexpected reimbursements and debt service repayments not budgeted in FY 2017. The Manager’s proposed budget allocated these funds to priority service areas including paving, land acquisition, and the Lee Highway initiative.

FY 2018:

Only one minor adjustment is recommended to the FY 2018 revenue projections included in the FY 2018 Proposed Budget released in February 2017. This adjustment adds an additional \$0.2 million in ongoing monies in FY 2018 and removes \$0.2 million in one-time money reflecting action taken by the state General Assembly to remove funding for a one-time bonus for a number of the County’s courts and constitutional offices and instead adding ongoing funding that was unanticipated.

Revenues

Fiscal Year 2017 revenues are estimated to be \$9.8 million higher than the FY 2017 budget due to:

- \$7.5 million increase in tax revenues and
- \$2.3 million increase in non-tax revenues (some of which were anticipated as part of the FY 2018 budget process).

Revenue Summary – Fiscal Year 2017	Incremental +/- Over Budget (\$ millions)
Tax Revenue:	
Real Estate (at existing tax rate)	(\$0.4)
Personal Property	1.9
BPOL	4.5
Sales Tax	0.8
Transient Occupancy Tax	(0.3)
Car Rental	0.5
Recordation	1.0
Cigarette	(0.2)
Communications	(0.3)
Total Tax Revenue Change	\$7.5
Non-Tax Revenue:	
License, Permits, Fees, and Charges for Service	0.4
Fines & Interest	1.2
Miscellaneous Revenue	0.9
State	(0.2)
Non-Tax Revenue Change	\$2.3
Total Projected Revenue Increase*	\$9.8
* Net of Crystal City, Potomac Yard, and Pentagon City and Columbia Pike Tax Increment Financing Area allocations	
Note: Numbers may not add due to rounding.	

Real Estate –Actual real estate tax revenue at the current tax rate is projected to be lower for FY 2017 than the adopted budget due to a variety of factors. Base real estate tax revenue at the current tax rate is slightly higher due to small growth in the overall assessment tax base for CY 2017 from projected amounts in the FY 2017 adopted budget. As announced in January 2017, assessments increased 3.0%. At existing tax rates, this generates \$1.7 million above the FY 2017 budget. Offsetting this increase are higher than budgeted real estate refunds (\$1.3 million) and lower than budgeted penalty and interest revenue (\$0.1 million).

In addition to the offsetting costs of real estate tax refunds and lower penalty and interest income, the allocation of revenues to the Crystal City, Potomac Yard, and Pentagon City Tax Increment Financing Area (Crystal City TIF) is higher than projected due to the increase in assessed values (up 5.6 percent) in the Crystal City area. This requires additional monies to be set aside for the Crystal City TIF (\$1.0 million). The Columbia Pike Tax Increment Financing Area (Columbia Pike TIF),

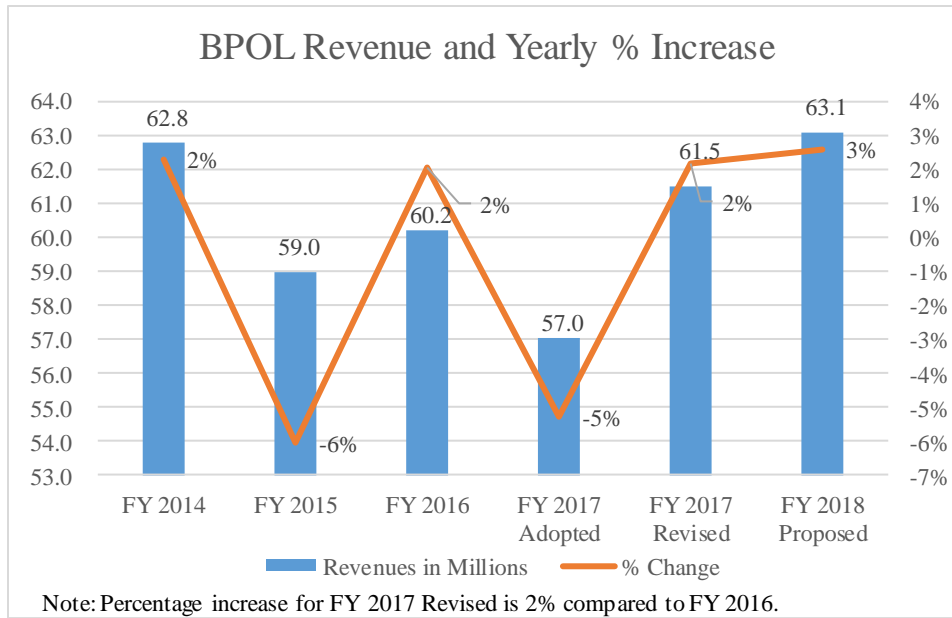
however, has slightly lower revised revenue projections (\$0.4 million). The FY 2017 adopted budget for the Columbia Pike TIF mistakenly included additional assessed value which artificially increased the revenue budget to the area in FY 2017. After adjusting the assessment base to reflect the correct allocation to the Columbia Pike TIF and factoring in the CY 2017 assessment changes, the FY 2017 allocation generates an additional \$0.4 million to the General Fund.

Advertised Real Estate Tax Rate Increase of \$.02/\$100 of assessed value: One-time funds which would be generated if the County Board was to adopt a real estate tax rate higher than the current rate are not included in the real estate tax revenue projections included in this Mid-Year/3rd Quarter report. The County Manager has included an assumption of one-time funds from a one-penny increase in the tax rate (\$3.7 million), which are included in the FY 2018 Proposed Budget.

County Manager Recommendation to Adjust the Crystal City TIF Allocation from 33% to 30%: Not included in the real estate tax revenue projections is the one-time revenue which would be available to the General Fund (\$0.3 million) if the County Board adjusts the Crystal City TIF Allocation from 33% to 30%. The County Manager has included this recommendation in the FY 2018 Proposed Budget; splitting the revenue based on the Principles of Revenue Sharing with APS (53.4% County / 46.6% Schools).

Personal Property – Both vehicle personal property and business tangibles revenue are trending higher than the FY 2017 budgeted levels with revenue received through February already \$1.2 million over budget. This tax revenue is forecasted to be \$2.2 million (2%) over budget by fiscal year end, partially offset by higher than anticipated refunds (\$0.3 million).

Business, Professional, and Occupational License Tax (BPOL) – BPOL tax revenue receipts continue to show growth through the end of March 2017. The majority of this tax revenue is received mid-March through early April. The Manager, as highlighted at the beginning of the budget process in February, noted the anticipated recovery of BPOL tax revenue and the alleviation of prior year worries of BPOL filing adjustments due to changes in the business reporting allowances for certain business types. The anticipated recovery of BPOL revenues for FY 2018 has already been included in forecast estimates in the FY 2018 Proposed Budget. The chart on the following page shows BPOL revenue (actual, budget, and revised) with the FY 2018 estimate.



Other Local Taxes: Increase \$1.5 million

- Sales tax revenue has grown slightly more than anticipated and is expected to be \$0.8 million above budget.
- While we continue to see increased hotel daily rates and slightly higher occupancy rates, Transient Occupancy has not grown as much as expected in FY 2017.
- Car Rental tax revenue has been strong and is projected to exceed the FY 2017 budget by \$0.5 million.
- Recordation tax is trending above budget; note that \$0.4 million of the \$1.0 million of additional revenue anticipated is allocated to AHIF.
- Cigarette and Communications taxes are trending slightly lower than budget.

County Non-Tax revenues are projected to increase by \$2.3 million. Highlights include:

- **Licenses, Permits, Fees, and Charges for Service** are anticipated to be \$0.4 million above budget due to higher than anticipated parking meter, Fire system testing, and engineering fee revenue offset by lower ambulance and ART transportation route revenue.
- **Fines and Interest** are expected to be \$1.2 million above budget due to higher interest earnings and bond payments (\$3.2 million), offset by lower parking ticket and other fine revenue (\$2.0 million).
- **Miscellaneous Revenue** was received in FY 2017 for cost reimbursements from the Derecho storm in 2012 (\$0.3 million) and a one-time reimbursement from Verizon for County right-of-way fees (\$0.6 million).
- **State** revenue is reduced by \$0.2 million primarily due to a reduction in Compensation Board revenue (\$0.5 million) resulting from the state not meeting revenue targets this year, partially offset by higher than anticipated Grantor’s Tax revenue (\$0.1 million) and prisoner expense reimbursement (\$0.2 million).

Expenditures

Most County departments and programs are projected to spend at or below their FY 2017 authorized levels. Several departments are experiencing specific expenditure pressures as outlined below and may exceed appropriations by the close of the fiscal year:

- Fire Department – due to overtime, callback pay, and leave payouts;
- Sheriff’s Office – due primarily to overtime costs;
- Circuit Court Judiciary – due to overtime and non-personnel operating costs associated with furniture for the jury boxes;
- County Manager’s Office and Management & Finance – due to new employee salaries that are higher than budgeted and leave payouts.

Expenditure Adjustments

- Departmental Savings – As noted above, most County departments are projected to spend at or below their FY 2017 authorized levels. In FY 2016, departmental operating savings totaled \$6.4 million, or approximately one-percent of department operating budgets (after adjusting for grant carryover and restricted funding), the lowest amount of savings in recent years. We anticipate that departmental savings will be less in FY 2017 due to several reasons, including higher staffing levels as the hiring slowdown has lifted and more stringent budget monitoring and close-out processes. Very few projects were approved for funding at close-out, and departments have been reallocating base budget dollars to fund those projects and other priorities, as discussed during the FY 2018 budget process.
- Health Care – Healthcare costs for the County are currently trending at budget and no adjustments are anticipated at this time. However, these costs can swing suddenly depending on one or two significant individual healthcare events.
- Early Retirement Buyout – The County Manager authorized an early retirement buyout program in January 2017 to create organizational flexibility as the FY 2018 budget was being developed and seventeen employees took the option. The program generates one-time costs that are incurred from employees cashing out leave balances they have accrued. For FY 2017, it is estimated that there will be an insignificant net cost to the County since many of these positions are being held vacant to offset the unbudgeted cost of the leave balances and potentially create savings into FY 2018.
- Debt Service savings of \$0.7 million (one-time) are due to refinancing outstanding bonds last summer and updated cashflow projections for previously approved capital projects.
- Metro - Staff is closely monitoring Metro’s budget deliberations and the impact that Metro’s budget could have on future fiscal years. We are not anticipating any impact on the FY 2017 budget. However, future years are much more uncertain and current projections show substantial funding needs in FY 2019 and FY 2020. The additional funding needs for FY 2018 for Metro have been funded in the FY 2018 Proposed budget through a 1 cent increase on the real estate tax rate and utilizing additional funding from NVTC.
- Snow Related Expenditures – Unlike FY 2016 when there were significant costs for snow related expenditures, the FY 2017 budget should be able to meet expected costs. Although

the recent snow related costs have not been finalized, the Department of Environmental Services should be able to absorb the cost of all snow related activity in their FY 2017 base budget.

Schools

Expense Transfers – As mentioned in the summary section above, the County Manager included \$0.7 million in one-time funds to Schools in the Proposed Budget. Based on higher tax revenue forecasted and the Principles of Revenue Sharing, Schools would receive an additional \$2.9 million for total one-time funding of \$3.5 million. The County is not projecting any additional tax revenue at current tax rates. However, if the County Board were to increase the real estate tax rate to something above the current rate then additional one-time funding would be realized to split between County & Schools.

School Funding Summary – FY 2017 & FY 2018

Funding to Schools	Ongoing (\$ millions)	One-Time (\$ millions)
County Manager’s Proposed Budget	\$478.3	\$0.7
Additional Mid-Year/ 3 rd Qtr tax Adjustments	-	2.9
Total Transfer to Schools	\$478.3	\$3.5
Additional Funding NOT Included in Superintendent Proposed Budget		
Total Additional Funding to Schools	\$-	\$2.9

Affordable Housing Investment Fund

FY 2017 projections for Recordation tax are higher than budgeted. The County Board earmarked a portion of recordation tax revenue to AHIF when the rate increased from \$0.05 to \$0.0833 in FY 2005. Based on the Board adopted funding allocations for recordation tax the amount which would be allocated to AHIF totals \$0.4 million above the adopted FY 2017 budget. It should be noted that the County Manager included an additional \$2.2 million in one-time funding in the FY 2018 Proposed Budget to allow for level funding of AHIF with FY 2017 and to address the projected commitments in the AHIF pipeline.

FY 2017 One-Time Funds: Alternative Proposals for Use

The unanticipated \$3.8 million in one-time funds available could be used to either enhance the level of funds for land acquisition, increase reserves in anticipation of Federal funding reductions, or alternatively, be used for one-time tax relief. A short description is offered for each alternative.

Land Acquisition: The County Board may wish to set aside the \$3.8 million in unanticipated revenues for the acquisition of land in the County. For example, there is not currently PAYG or GO bond funding available in non-parks land acquisition, since all available non-park acquisition balances were reallocated to property acquisitions and temporary facilities for Fire Station

8. Similarly, total balances for park land acquisition are currently budgeted at \$1.83 million and include both PAYG and GO bond fund sources. The FY 2018 County Manager's Proposed Budget allocated \$1.9 million for either open space or non-parks land acquisition. Additional dollars for land acquisition could provide a significant source of funds to enable the County to purchase parcels as opportunities arise.

Federal Funding Reductions: To mitigate any decreases in Federal revenue in FY 2018 the County Board may wish to allocate additional funding to the Economic and Revenue Stabilization contingent and designate it for replacing lost Federal grants and aid. The President's budget, as proposed, may result in decreased Federal revenue, grants, and aid to the County. In the FY 2018 budget Arlington County is estimated to receive \$15 million in Federal funding, mostly for social services programs. In addition, the County receives Community Development Block Grants (CDBG), direct transportation funding, as well as pass through funding received from the State. These programs may be at risk for reduction or elimination when federal budget deliberations are concluded. Setting aside additional funding in the Economic and Revenue Stabilization Contingent would ensure Arlington is prepared in the event there are Federal funding reductions in FY 2018 and ensure our existing service levels to the most vulnerable in the community remain the same in FY 2018.

One-Time Tax Relief: The County Board may wish to provide one-time tax relief to residents with the \$3.8 million in unexpected revenues. A number of tax/fee reductions are available to the County, however; providing direct tax relief to taxpayers is limited due to restrictions by the Commonwealth of Virginia. Below are options for providing relief to taxpayers with a brief explanation of taxpayers affected and the mechanism for providing relief.

Personal Property Vehicle Tax: The County could reduce a portion of the local tax burden through increasing the amount of personal property tax relief for vehicle owners. Through the Personal Property Tax Relief Act (PPTRA), the County receives a set amount of \$31.3 million as a fixed block grant for vehicle tax reductions from the State, and distributes the funding to qualifying vehicle values below \$20,000. Currently the State's block grant pays the tax on the first \$3,000 in value of conventional vehicles and 28% of the tax on the value from \$3,001 to \$20,000. The County Board could use the one-time funds available to increase the percentage of tax relief on vehicles between \$3,001 to \$20,000. In CY 2016 there were approximately 112,000 vehicles which would benefit from an adjustment to the percentage of relief provided on vehicle value between \$3,000 and \$20,000. Relief would total approximately \$13 per vehicle (assuming the average vehicle assessment).

Utility Tax Rates: The residential and/or commercial tax rate could be adjusted for FY 2018. The rate would need to be increased the following fiscal year to avoid ongoing funding issues. Relief by reducing this tax rate would impact residential occupants (any occupant responsible for paying utilities) and/or commercial owners/tenants responsible for paying utilities. The tax rate structure varies for residential and commercial accounts. If the County Board were to only apply the \$3.8 million in tax relief to residential users, the tax bills for residents could be suspended for 2 years (residential utility revenue = \$1.8 million per year). This would be a savings of approximately \$12 per electric and gas customer per year. If commercial customers were applied tax relief in a proportionate

amount to residential customers, then the residential customer would only receive \$2 in tax relief per year.

Some points for additional consideration: Each option available to the County Board affects different groups of residents and taxpayers. Of the options listed above, implementation of tax relief through a reduction in the Personal Property Tax is the simplest to administer for FY 2018 and the easiest to adjust in the following fiscal year. Regardless of an option chosen, clear communication with taxpayers is recommended to avoid potential confusion with any one-time tax relief program.

FY 2018 Ongoing Funding Adjustments

As described above, there is only one minor adjustment recommended to FY 2018 revenue projections. This adjustment adds an additional \$0.2 million in ongoing monies in FY 2018 and removes \$0.2 million in one-time money reflecting funding changes the General Assembly made to a number of the County's courts and constitutional offices.

In addition, if the County Board increases ART fares by \$0.25 commensurate with the pending increase to Metro fares, additional revenue would be generated. This revenue however is anticipated to be offset due to recent lower ART revenue ridership trends. An estimate of potential revenue for FY 2018 assuming the County Board increases ART fare revenue will be provided with the "Chairman's Mark" spreadsheet provided to the County Board for budget adoption.