March 18, 2011

HUNTER MILL BUDGET ADVISORY COMMITTEE FOR FY2012
REPORT AND RECOMMENDATIONS

Executive Summary

The Hunter Mill Budget Advisory Committee ("Committee") was appointed by Supervisor Catherine Hudgins in November 2010. Supervisor Hudgins asked the Committee to examine the Fairfax County budget and to provide input on how the County Board of Supervisors should address the FY 2012 budget.

Since then, the Board of Supervisors advertised the maximum FY2012 tax rates at the FY2011 levels; the County Executive announced his FY2012 Budget Plan; and the School Board adopted its budget proposal. According to the County Executive, the advertised tax rates for real estate, personal property and other local taxes will produce approximately $102.8 million of additional revenues in FY2012 over the Adopted Budget Plan for FY2011. From this, the County Executive proposes to expend approximately $68.2 million, mostly to address fixed obligations. That would leave available funds for discretionary expenditures or for tax reductions of approximately $30 million.

As discussed more fully below, the Hunter Mill Budget Advisory Committee recommends that the Board of Supervisors

- Approve FY2012 tax rates at the advertised levels.
- Use the available funds balance and additional revenues that may become available to:
    - Cover additional costs or revenue losses imposed on Fairfax County by the State or by the Federal government in their ongoing budget processes;
    - Reward employees with some enhancement of their compensation;
    - Invest in improved energy efficiency;
    - Provide all-day kindergarten;
    - Meet other funding needs, such as the retirement system and deferred maintenance.
- Continue to pursue efficiency improvements and cost savings such as those implemented in the "smart savings" programs of prior years.

Looking longer term, the County should undertake a comprehensive review of retirement benefits and compensation. Given reports of other jurisdictions' problems, citizens want to be reassured that the retirement system is sound and that the costs, benefits and risks are fairly allocated between employees and citizens. This Committee does not pre-judge the outcome of that review. It notes, however, that any shift from the current system may require salary adjustments to keep employees whole and to keep overall compensation competitive.
Also, the County needs to proceed expeditiously to prepare for the coming of the Silver Line, which will reach Tysons and Reston East/Wiehle Avenue in 2013. Infrastructure needs to be planned and built; and funding plans, including requirements for developer contributions, must be implemented to support the infrastructure. Key decisions will be needed in FY2012.

Background

The Hunter Mill Budget Advisory Committee for FY2012 consists of 14 citizens who live in the Hunter Mill District. Members of the Committee are volunteers who came into the process with varying backgrounds and with open minds. The Committee members are: William Penniman (Chair), Amanda Andere, Deloris Bailey, Hank Chao, Laurie DiRocco, Susannah Frazier, Pat Hynes, Pam Konde, Barb Loving, Kathleen Driscoll McKee, Guru Nagaraja, Carl Pletzke, Marion Stillson, and Cathy Vivona.

Supervisor Hudgins met with the Committee on November 12, 2010. Thereafter, Committee meetings were held during most weeks from early December until mid-March 2011. Given the complexity of the Fairfax County budget, Committee members faced a considerable challenge. Several members volunteered to examine particular aspects of the County's revenues and expenditures and its budgetary process.

Committee Comments and Recommendations

The Fairfax County budget has been under heightened scrutiny for the last several years. The recession has significantly affected the County's revenues and constrained its actions. These fiscal restraints have pressured the County into undertaking a close look at expenditures throughout the County government in each of its recent budget cycles.

Under the circumstances, the Hunter Mill Budget Advisory Committee has been hard pressed to identify specific additional budget cuts that are needed or appropriate for FY2012, though it assumes that savings can still be achieved in some areas. Consequently, the following comments and recommendations are sometimes general and sometimes address longer term budget objectives which are not capable of being implemented in FY2012.

A. Revenues

1. FY2012

Like the County, the Committee is confined to working within the advertised tax rates for FY2012, which were approved by the Board of Supervisors on February 22, 2011. Those rates are equal to the rates in effect in FY2011.

Due to improvements in underlying values, it is forecast that, assuming a continuation of the current tax rates, the County's FY2012 revenues are likely to exceed FY2011 revenues by approximately $100 million. On the other hand, the County Executive expects expenditures to increase by approximately $70 million even if the transfer to the Fairfax County School system is held constant. According to his February 22 presentation to the Board of Supervisors, the combination of advertised tax rates and cost increases, will leave the Board of Supervisors approximately $30 million to use or hold for future unfunded requirements.

The Committee recommends that the Board of Supervisors not reduce the FY2012 tax rates below the advertised levels. It should use the projected $30 million and additional amounts that may become available in order to

- mitigate costs or revenue losses resulting from actions by Congress or Virginia,
- benefit employees,
- implement all-day kindergarten,
- invest in energy efficiency to reduce future operating costs,
- meet other funding needs, such as capital projects on which the County has fallen behind (*e.g*., deferred maintenance) or by doing more to return the employee retirement reserves to the 90%+ "corridor" that the County deems to be prudent.

If money is left over at the end of the year, such amounts can be carried forward.

2. Looking Ahead

Fairfax County is overly dependent on real estate taxes, a revenue source that is vulnerable to periodic downturns and difficult-to-forecast recoveries. To date, the State legislature has narrowly restricted Fairfax County's flexibility to raise revenues in ways other than the real estate tax rate. Looking to the future, the County should continue its efforts to persuade the legislature to permit increased County taxes or fees, particularly from sources that do not follow the same cycles as real estate values. Diversifying revenue sources will help to mitigate dramatic revenue losses that result from dependence on a single source, such as the real estate tax. Among the revenue opportunities that should be pursued before the legislature are the ability to raise gasoline/diesel fuel taxes, a meals tax, higher taxes on transients (*e.g.*, hotels, rental cars), or a surcharge on the Virginia income tax. If results are not achieved in the Virginia legislature, the County should pursue a meals tax referendum in 2012, possibly with the revenues dedicated to education.

Even implementing red light cameras is restrained by current legislation. Despite the constraints, Fairfax should install (or activate) and operate such cameras at dangerous intersections to the extent permitted by current law. Although the prospects of significant revenues are small, the public safety benefits would potentially be significant.

We understand that fees for using facilities and services and fines for county violations have been re-examined in the last couple of years. While we do not make a specific recommendation to re-examine them at this time, they should be examined periodically.

B. Expenditures for FY2012 (and beyond)

As noted above, this Committee's report does not specify particular expenditures that should be cut or programs to be eliminated from the proposed FY2012 budget. However, as set forth below, the Committee does make several expense-related recommendations. As will be evident, some of these are long term in nature while others can be implemented in FY2012.

1. Mitigating Cost Shifts or Revenue Losses Attributable to State or Federal Actions

The County's FY2012 budget and programs remain at risk due to budgetary actions still to be taken by Congress and the Virginia legislature. Threatened cuts could affect the County in a number of ways, including in the areas of health, human services, housing, transportation and education. In some cases, the upstream funding may disappear but not the underlying mandates or needs. The County needs to have flexibility to address these contingencies.

2. County Salaries

The Committee members are concerned that County employees will face a third year of a salary freezes in FY2012. This concern applies to uniformed and civilian employees of the County and to FCPS employees. In some areas, Fairfax County's pay appears to have fallen behind neighboring jurisdictions. While the Nation has been facing hard times, Fairfax County has done *relatively* well. For example, its unemployment rate is well below the national average and its real estate values are beginning to rise again. Also, although inflation has been relatively low, it has not been (nor is it likely to be) negligible, and Fairfax is a particularly expensive county in which to live and work.

This Committee believes that the Board of Supervisors should find a way to recognize and reward the contributions by County employees, and that all categories of employees, not just school employees, should receive some form of additional compensation. Unfortunately, the "available" dollars identified by the County Executive seriously crimp the potential for regular salary increases. Options that should be considered by the Board include bonuses, salary/step increases, additional paid leave, or health contribution holidays. The Committee is also concerned that there be parity of treatment for County and FCPS employees, and efforts should be made by the County and FCPS to achieve that result. It is hoped that the Board will assure employees of its commitment to resuming normal salary increases in FY2013 (at least absent an extraordinary reversal of economic fortune).

3. Benefits

Benefits raise a host of complex economic and equitable issues. It is unrealistic to think that wage-benefits packages can intelligently be revised between now and adoption of the FY2012 budget unless they have already been closely studied and the results of those studies discussed with employees prior to adoption of any significant changes. One issue that can be addressed now, however, is that the County should make substantial contributions to the retirement system in FY2012 (and in subsequent years) in order to return the retirement system to the previously approved reserve "corridor" as soon as possible.

The Committee understands that the County is currently conducting a review of its retirement system. Such a review must reflect the total compensation package as it is clear that assurance of a reliable retirement plan affects employees demands' for higher current salaries. Particular areas to consider include the following:

Retirement packages. The debate over defined contribution and defined benefits packages is politically hot at the moment. Some government (and private) entities overpromised retirement benefits without adequately funding them, and they now face financial difficulties. Fairfax County residents want reasonable assurances that they will not face a future funding crisis similar to what some other local and state governments reportedly face.

Review of the retirement issue requires a balancing of interests, and this Committee does not prejudge the outcome of a retirement program review. On the one hand, assuming they are managed and funded appropriately, defined benefits plans can be mutually beneficial for employer and employee, and they can be a significant tool for recruiting and retaining employees even with lower current salaries. The advantage to the employee of a defined benefits plan is substantial, since it provides security and protects individual retirees from market swings that can devastate an individual's retirement plans. Short-term market fluctuations can be better borne by the County, whose portfolio is designed and regularly funded for the long-term, than by an individual, particularly one who faces a market drop close to or during retirement. On the other hand, a defined contributions plan would limit the potential costs and downside investment risks borne by the County and taxpayers, and it would reduce temptations to shift risks to future taxpayers by underfunding a plan in the near term. Potential savings from shifting retirement investment risks to employees, however, may be offset by the need to adjust salaries upward in order to keep employees whole and keep the overall pay package competitive. Thus, all factors need to be considered, and existing commitments to employees need to be honored.

While Fairfax County appears to have prudently managed its retirement system, the sharp market declines of 2007-2009 have still not been fully offset by subsequent market increases, and future stock and bond market appreciation is likely to be slower than in the past. As would be expected after a bruising market decline, additional County contributions are needed to restore the retirement plan to the safe actuarial "corridor" identified by County policies. (The County Executive has proposed an additional contribution of $15 million in FY2012, but further contributions in FY2012 or beyond may be warranted.) A timely return to the safe "corridor" is important for risk management.

As part of its review, consideration should be given to a number of options for adjusting benefits in concert with a total equitable compensation package. The review should also consider adjusting the details of the County's defined benefits retirement plans, not just a binary choice between defined benefits and contribution systems. Possibilities to consider might include a mix of defined contributions and defined benefits; later vesting and/or retirement dates; adjusting employer-employee contributions; adjusting the COLA component particularly after a period of time when the retirees' activities are likely to be reduced in any event; less generous payouts for new employees who leave early (*e.g.* an escalating percentage used in the multiplier for years of service).

Contributions by Uniformed and Police Employees

Uniformed (Fire) and Police Department employees are treated differently when it comes to contributions to their retirement plans. In the past, the members of the Police pension plan were contributing 12% of the wages to their plan while the Uniformed members were contributing about 7%. Over the years, the Police contribution was lowered to 10% while the Uniformed are still paying 7%. We suggest that the Police contributions be lowered to 9% in FY2012 and the Uniformed be raised to 8% which would have a minimal impact on the FY2012 budget. The two plans should be equalized in FY2013 at some figure such as 8.5%.

Accumulated Leave

The Committee suggests that the County should reconsider its policies on accumulated sick leave. Allowing employees to accumulate large sick leave balances, which are tacked on as additional time at the end of a career, seems unduly costly to the County, and it is not likely to be critical factor in attracting or retaining employees.

4. Energy Efficiency Investments and Management Practices

Energy efficiency improvements can save money for the County and for taxpayers in the near and long-term. Much like new revenues, saving money through increased efficiency frees up funds that can be used for employees or services; and, such savings can also be used to mitigate future tax and fee increases. More efficient use of energy also has many indirect benefits to the public, including reduced harm to health, property and the environment from air and water pollution and reduced dependence on foreign energy sources. Such externalities are real, but are often not quantified or considered when energy choices are made.

While some energy efficiency gains can be achieved through simple management decisions (*e.g.*, adjusting building temperatures), other gains require investments in equipment, software, buildings or employees. Absent express requirements or a clear assignment of responsibility, it is too easy to let efficiency investments be overlooked or set aside, particularly when funds are tight or when attention strays. Thus, despite admirable pronouncements in its energy policies and Cool Counties commitments, it appears that Fairfax County is not doing all that it reasonably could to benefit taxpayers or the environment. Because of the higher cost of retrofits, investments that are not made when the opportunity is first presented can drive up costs and environmental side-effects for the life of a facility. In the case of buildings, the higher costs can last for 50 or more years. Rising and volatile energy prices—which we are seeing again—can undermine County budgets, as well as waste taxpayers' money.

This Committee recommends three key policies to capture the potential savings from energy efficiency.

First, the County should require employees to identify and catalogue all potential energy saving actions whose costs are less than the value of the savings that will be achieved by implementing them. Plans for operations, for building construction, refurbishment or repair, and for vehicle and equipment replacement should explicitly state the options and the direct and indirect costs and savings that would be achieved by implementing each option over the life of those investments. At least quarterly reports should be submitted to the Board of Supervisor, the County Executive, and the public, which explicitly identify the available options, the decisions made or to be made, and the direct and indirect costs and savings that could result from each option. Such a public "scorecard" would help shape decisional awareness and help reduce waste.

Second, the County should appoint a *countywide* Energy Manager with responsibility (a) for reviewing the upcoming and past actions of each County agency, (b) for insisting that energy savings be implemented where viable, and (c) for reporting to the Board and the public about what has and has not been accomplished and what new policies should be implemented in the future. The countywide Energy Manager should also have the ability to pursue energy management contracts under which third parties put up the capital and manage energy-saving and alternative energy investments in exchange for a payment out of the future stream of savings. Currently, despite a committee, responsibility in this area is dispersed among various departments. Just as the Board of Supervisors created an internal auditor position, appointing an overall Energy Manager would help to assure that savings are the primary responsibility of at least one County official, instead of simply being one of many issues that a variety of officials consider.

Third, the Board of Supervisors should consider committing minimum, on-going funding to making money-saving investments in energy efficiency. Possibilities include: (a) a revolving fund could be established under which a portion of the money saved in a given year would be pooled to fund new projects in subsequent years; (b) the County could commit a specified amount—*e.g.*, 1 or 2 cents of the tax rate—as capital for energy efficiency investments that produce net benefits over time; (c) at a minimum, the budget for each fiscal year should have a section that explicitly identifies potential energy saving investments that are expected to be available in the fiscal year and how the budget does (or does not) accommodate them.

5. Other Potential Cost Savings

While energy savings are one potential source of savings that will benefit taxpayers, information technology also offers potential savings. IT opportunities need to remain at the forefront of County planning and should continue to be vigorously pursued where benefits can be achieved.

Similarly, the County and FCPS have achieved on-going savings through the "smart savings" initiatives. These programs sought to reduce costs by consolidating duplicative operations in the County government, including the public schools. The County and FCPS should continue to pursue these efforts. County and FCPS transportation systems may present such an opportunity.

Consolidated management of retirement programs may also offer savings. Currently, the County operates multiple retirement plans (police, fire and general employees). We have been advised that these plans are separately managed and administered. Even assuming it continues to

implement separate retirement plans, the County should explore whether it can achieve meaningful savings by consolidating the administration and investment management functions.

6. Dulles Corridor Infrastructure Needs

The Silver Line will open in late 2013 through Tysons to the Reston East/Wiehle Avenue Station. A few years later, Phase 2 of the Silver Line will extend to Dulles Airport. The County is encouraging transit-oriented development around each of the Metro stations in Tysons and Reston. Such development will add large populations of new workers and residents and substantial demands for new infrastructure (roads, highway crossings, schools, public safety, recreation, etc.).

Timely planning, funding and construction of infrastructure will be needed to meet these new demands. Developers should be expected to make significant contributions to those construction efforts, since they will benefit from timely infrastructure and some of the infrastructure will be on their property. Allocations of costs and responsibilities between the County and developers need to be resolved soon so that timely work can be initiated. The Committee urges the County to accelerate its planning and infrastructure decisions for both Tysons and Reston and to include adequate funding in the FY2012 budget to address these issues.

7. The FCPS Budget

This Committee recognizes that the School Board has considerable independence from the County Board of Supervisors, so the Committee has not attempted to address the details of the FCPS budget. However, there are two issues on which this Committee comments.

All-Day Kindergarten. All-day kindergarten should be implemented in the remaining 37 schools as soon as possible. Kindergarten now implements an "academic" program; it is not just "playtime". Although the 37 schools that lack all-day kindergarten are not considered "Title I" schools, all children in those schools will benefit from the added instruction and socialization, and many individual children have as much need for all-day kindergarten as children in "Title I" schools. Saying that the County will implement all-day kindergarten at the remaining schools at some indefinite date in the future will not help the children who are passed by in the meanwhile.

The Board of Supervisors should convey to FCPS that implementation of all-day kindergarten is a high priority for the County. If there is any question about the availability of FCPS' funding for all-day kindergarten, the Board of Supervisors should commit that money available at carryover will be transferred to FCPS to offset such costs in whole or in part provided that all-day kindergarten is implemented in FY2012.

Salaries. This Committee recognizes the School Board's desire to raise salaries for teachers and other school employees. On the other hand, we are concerned about the adverse morale impact if school employees receive increases when other County employees do not. An effort should be made to coordinate the actions of the School Board and the Board of Supervisors so that all employees are rewarded in some way within existing budget limitations.