Arlington County Civic Federation
Revenues & Expenditures Committee
Report & Recommendations
Arlington County Bond Referenda for 2008

On July 22, 2008, the Arlington County Board approved four separate bond referenda totaling $170.225M for consideration by the voters on November 4, 2008.

The Revenues & Expenditures Committee has reviewed the proposed bonds and is pleased to submit its report and recommendations for consideration by the full ACCF membership. This report does not specifically deal with the School Bond for $99.425M; the School Bond is covered by a separate report from the ACCF Schools Committee.

The three "County-side" bond referenda on the November ballot are as follows:

- METRO $10,000,000
- Community Infrastructure $10,800,000
- Utilities $50,000,000

This report will briefly describe each of these three bond packages, and then will make some global observations on the overall status of County indebtedness. We will close with our recommendations on the three bonds.

I. METRO ($10M)

In 2004, the Washington Metropolitan Area Transit Authority (WMATA) Board of Directors received approval from METRO's seven contributing jurisdictions for a 6-year, $3B capital improvement program, usually referred to as "Metro Matters," to fund certain priority capital needs of the regional transit system through FY2010. Metro Matters contained a wide variety of capital projects, including facility and system upgrades to support the operation of 8-car trains, acquisition of new buses and escalator rebuilds.

Notable accomplishments since the inception of Metro Matters include the 8-car train initiative (all lines are expected to have 50% 8-car trains soon) and a reduction in the bus fleet age (from 10 to 7 years).

Arlington's share of the overall cost of this program was determined by a master agreement between METRO's participating jurisdictions, as approved by the County Board in 2004.

Arlington's overall capital obligation to METRO for FY09-10 is set at $32.7M, $10M of which is covered by the current bond request. The remaining $22.7M of Arlington's share is projected to come from the Commonwealth of Virginia. Any reductions in the Commonwealth's contribution would have to be covered at the local level, by either additional bonding or PAYG funds.

Funding METRO capital requirements will be an on-going obligation for Arlington. We note that the County's FY09-14 Capital Improvement Program (the CIP) anticipates future bond requests of $20M in 2010 and $15M in 2012.

None of the funding discussed here is related to the Dulles/Silver Line rail extension.

II. Community Infrastructure ($10.8M)

This bond proposal has two components - $9.0M for Neighborhood Conservation (NC) projects and $1.8M for capital improvements at the Career Center.

Excluding the 2008 bond for NC, the program currently has available funding of $9.9M, consisting primarily of unsold bonding authority from 2004 & 2006. All but $218K of this amount has been obligated to specific projects, including a 10% cost overrun reserve. Over 75% of the projects deal with street improvements and lighting.

The 2008 NC bond would fund the next three funding rounds (spring & fall of 2009; spring of 2010) of NC projects.

The $1.8M for the Career Center will fund the County share of capital improvements (including major mechanical, electrical, plumbing and fire protection systems). Additional funding is included in the Schools Bond for these projects. These capital improvements are being proposed at this time, since the adopted six-year CIP does not provide funding for any full scale reconstruction of the Career Center.

III. Utilities ($50.0M)

This bond proposal is designed to provide funding to complete the upgrades to the Water Pollution Control Plant (the WPCP). The construction and financing of this project is complicated, with multiple funding sources, including some where the amount of funds provided are still not determined with absolute certainty.

From inception, the total project cost is now $568M. Construction is now about 60% complete, and the vast majority of the project has been contracted for. The $568M figure also includes a contingency. County staff is confident that the project will be completed at or under the current budget.

To-date, the largest source of funding has been the Virginia Revolving Loan Fund, which provides municipalities long-term funding at rates about 100 basis points below those that would be available through general obligation bonds. $230M from VRLF has already been drawn. An additional $60M will be requested in 2010 and 2011.

The second largest source of funds is local bonding. The $50M bond referendum this fall would bring total local bond funding up to $126M.

Next, our local partners in the project (Fairfax, Falls Church and Alexandria) will be contributing a total of $89M.

Lastly, Arlington has an agreement with the Virginia Department of Environmental Quality for a Water Quality Investment Fund grant total of $96M. Since the amount of the grant that will ultimately be received is dependent upon competing projects throughout Virginia and budgetary issues, staff is only anticipating $63M of this grant being funded. These funds do not have to be repaid.

Any grant funding received over and above $63M would lower the amount of local bond funds needed for completion of the project. Per the wording of the actual ballot referendum, any leftover funds can be used for other water and sewer system capital needs.

This huge capital project and its related debt service will continue to drive increases in the water/sewer rate for several more years. Staff currently projects increases of 13-15% for FY10 and an additional 9% in FY11, after which the debt service requirements should stabilize.

IV. Some Global Observations

Much has been written and discussed regarding County debt levels, debt service and capital project selection in the past several years. These discussions have stemmed from an extended period of rather aggressive capital spending by both the County and the Schools and debt service levels that have approached the usually cited benchmarks for maintaining the County's triple/AAA bond rating, now complicated by the prospect of declining revenue growth, due to the real estate slow down. Growth in annual debt service has been cited as a "budget driver" (i.e., a line item going up more than the budget as a whole) for many years now.

In response to these concerns, the County Board adopted a new financial policy during this year's budget process. In essence, it added a fourth leg to already existing debt limit policies. To quote the policy: "Debt service growth over the six year projection (of the CIP) should not exceed the average ten-year historical revenue growth."

For the current CIP cycle, this figure would have been 6.9%. In recent years, the growth in debt service has been appreciably higher (FY91-96, 15.8%; FY97-02, 8.7%; FY03-08, 9.0%).

It should be noted that the current CIP limited average debt service growth to 4% over its six-year period. As the County Manager argued in his report, the ten-year average of 6.9% is distorted by the real estate value run-up from 2001 to 2006, and "…there is no basis on which to project an increase of this magnitude during the next six years."

It is this new "ten-year revenue growth" test, as reduced in light of recent conditions, which has set the outer limits for bonded debt in the current CIP. As the County Manager described it, "This is to ensure that debt does not consume an increasing share of the budget – which it has in recent years."

We feel it noteworthy to further quote the County Manager's Board Report for the CIP adoption:

> *"There is a high probability that during the next six years, the County Board will have to consider a combination of real estate rate increases and/or service reductions in order to maintain a balanced budget" – July 17, 2008 Report, pg. 6.*
>
> *"Modest tax rate increases to sustain at least a 4% growth in revenue are highly probable. Spending constraints and/or modest service reductions are also probable in the next two fiscal years" – July 17, 2008 Report, Att. C, pg. 8.*

V. Our Recommendations

Overall, the Revenues & Expenditures Committee recommends that the Civic Federation support a "yes" vote on each of the three County bonds.

Within the context of our recommendation, we note several concerns.

One, we have concern about the general construction of the ballot language, which is usually described as being intentionally “broad” to allow flexibility in the ultimate use of bond funds.

The Community Infrastructure language describes the requested bond funding as being for “the cost of various capital projects for County facilities and infrastructure.” We would have liked to see more specific language, particularly mentioning NC projects.

Similarly, the inclusion of projects beyond the WPCP in the Utilities bond language gives us some pause. While we acknowledge the uncertainty of other funding sources as described elsewhere in this report, we would have preferred to have seen the bond language be limited to the WCPC construction only.

At the risk of stating the obvious, a caution also needs to be raised due to the current disarray in our capital markets. Arlington’s next regularly scheduled bond sales would occur in the spring of 2009. What the condition of the municipal bond market will be at that time is impossible to know. The available interest rates, even with Arlington’s triple/AAA rating, and even the availability of long-term bond funding at any price, are relatively unknown in the current climate. What effect these considerations could potentially have on our future bond sales is impossible to predict at this time. Suffice it to say, capital projects with approved bonding authority could possibly need to be delayed and/or scaled back, depending on the condition of the bond market.

Lastly, we would like to acknowledge the help of the County’s Management & Finance staff, who (as always) promptly and professionally responded to our inquiries on various subjects discussed in this report.

Respectfully submitted:

ACCF Revenues & Expenditures Committee
Jerry Auten
Burt Bostwick
Frank Emerson
Wayne Kubicki
Roye Lowry
Roger Morton
Tim Wise