

*City of Alexandria, Virginia*

*Oral(a)*  
*5-8-01*

MEMORANDUM

DATE: MAY 10, 2001

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: PHILIP SUNDERLAND, CITY MANAGER *PS*

SUBJECT: PROPOSED LEGISLATION RELATED TO DELAYING THE REIMBURSEMENT OF PERSONAL PROPERTY TAXES TO LOCAL GOVERNMENTS

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At the Tuesday night May 8 City Council meeting, Council discussed legislation that had been recently discussed by the General Assembly which would have delayed the reimbursement of personal property taxes to local governments. Council's concern about the legislation was communicated to the City's legislative delegation, the Virginia Municipal League (VML) and others. VML was able to use the City's concerns in their efforts to defeat this legislation.

This legislation would have negatively impacted local governments in Virginia, and would have set a dangerous precedent of altering the process of reimbursing local governments substantial funds for personal property tax relief. As part of its efforts to communicate local government concerns to the Senate and House leadership, on Wednesday VML asked City staff to quickly produce a short written analysis of the impacts of the legislation on local governments in Virginia. That analysis, which VML used in its successful efforts, is attached. In addition, City staff was able to obtain and pass on to VML serious concerns about the legislation from senior bond rating staff at Standard & Poor's.

Attachment: Implications of Proposals to Delay Reimbursement of Personal Property Taxes to Local Governments

cc: Mark Jinks, Assistant City Manager  
Daniel Neckel, Director, Finance  
Bernard Caton, Legislative Director



# Implications of Proposals to Delay Reimbursement of Personal Property Taxes to Local Governments

## **Credit Implications**

- Any delay in reimbursement under the PPTRA program will have negative credit implications on all local governments. This is because the amounts of reimbursement are material to local government budgets. More so, this is because it calls into question the long term the stability of the state's reimbursement of PPTRA.
- At credit rating meetings between localities and the bond rating agencies over the last few years, the stability and the prompt payment of the state under PPTRA has been discussed and the rating agencies have been assured that payment was not a problem.
- The delay in reimbursement could cause cash flow borrowing for local governments. Cash flow borrowing is viewed as a negative credit factor by the bond rating agencies
- Negative credit implications mean that it could keep the locality from getting an upgrade or could be one of the factors in a downgrade. The cash flow borrowing would be noted in the credit write-ups issued by the bond rating agencies and the research departments of investment banks. This negative impacts the interest rates that jurisdictions would have to pay on bonds issued.
- A delay in reimbursement (switching the fiscal year of some of the reimbursement) will negatively impact the state's credit analysis by bond rating agencies and the investment banks. A triple-A rated state has sound financial management and does not resort to questionable budget and accounting tactics to balance budgets. The experience of New York State, Pennsylvania, the District of Columbia and the Tennessee are a testament to this fact as all of these states - and the local governments within them - have had credit issues arise as the result of resorting to budget tactics that cause cash flow borrowing.

## **Accounting and Cash Flow Implications**

- The attempt to shift to a future fiscal year a current year liability is one that General Accepted Accounting Principles (GAAP) indicate cannot be done in this circumstance. The state should budget and recognize the expense and liability when occurred (i.e., in the same year).
- If the state does not recognize its liability and in the year in which it has occurred, it will be in violation of GAAP standards. Bond rating agencies expect states and local

governments to follow GAAP.

- If the state does not recognize its liability, it also is sending tacit approval to local governments to not follow GAAP and be “creative” in accounting practices. This would reverse a two decade long series of accounting standards improvements in local governments in Virginia. Any reversal also sends a signal to the bond rating agencies and to the investment community that the local government finances are less sound or well managed than is currently perceived.
- The Governmental Accounting Standards Board (GASB) Statement #34 and other GASB standards, which the state and local governments have or now are now implementing require the liability incurred in one year to be recognized in that year.
- Most localities in Virginia do not do cash flow borrowing - in fact it is rare.
- Given that the size of personal property tax revenues is material, local governments have often scheduled their debt service payments (particularly the annual principal payment) around their key tax revenue due dates. A shift to a later PPTRA reimbursement (more important at the 70% and 100% levels) may put a locality in a situation where it does not have the cash to make debt service obligations on the dates that a locality may have obligated itself to pay debt service.
- Depending on when the personal property taxes are due, the delay in reimbursement could cause a significant cash flow problem for a locality. In particular if it causes cash flow borrowing, and that borrowing crosses fiscal years, then it means to the investment community, and to the public, that a locality did not have sufficient funds to pay for its fiscal year expenditures (for the fiscal year that is ending). The generally accepted practice is that cash flow borrowing is paid back by the end of a state or local government’s fiscal year.
- The proposed amendments to 4-107, which would have the state reimburse local governments before the end of a fiscal year, solves only the issue of having the cash flow borrowing on the books at the end of the fiscal year. It does not address any other of the issues that have been raised, as GAAP and GASB standards would require that the reimbursement expense by the state prior to the end of the fiscal year be recorded as an expense of the fiscal year in which the reimbursement occurred, and not be deferred as an expense of the subsequent fiscal year. The state cannot “open its books” early as the date of the start of the fiscal year is intended to be a specific accounting measurement period and not fudged by starting early.
- Cash flow borrowing is not a simple undertaking for a local government (as it is often much like a bond sale), will divert staff attention from current duties and will result in additional administrative costs (such as legal costs).
- While the local governments may be held harmless for direct interest lost in not getting

the state reimbursement in two days (current practice), they will also lose interest by having to shorten their investment portfolio maturities by buying shorter term securities that almost always bear lower interest rates . This will need to be done because of the uncertainty of when the state will reimburse.

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58.1-3526 C. Except as provided by subsection B of § 58.1-3528, upon full payment of the tangible personal property tax levied on a qualifying vehicle, less the amount of the deduction, as described in subsection B of this section, the treasurer shall make a request to the Commonwealth for payment of the amount equal to the amount specified in subdivisions B 2 through B 5 of § 58.1-3524 for the qualifying vehicle. Such request shall include a summary of the information appearing on the related tangible personal property tax bill. The summary information to be included in the request and the form of such request shall be prescribed by the Comptroller. Upon receipt of such information, the Comptroller shall issue the proper warrant for payment by the State Treasurer. If the Comptroller determines that a treasurer is unable to provide the summary information, he shall issue a warrant for payment to such treasurer in an amount equal to the estimate made by the Department under § 58.1-3529. Provided that the request for payment is received by the deadlines established and in the format prescribed by the Comptroller, he shall issue the warrant for payment no later than thirty days after the due date for such taxes, together with payment of interest on such amount from the date two business days after the receipt of the request from the treasurer until paid at a rate established by the Virginia Resources Authority for revenue anticipation loans to localities. The Virginia Resources Authority may make revenue anticipation loans to localities in anticipation of payments from the State Treasurer pursuant to this section. Principal and interest on such loans shall be repayable in full immediately upon receipt by the locality of payment from the State Treasurer.