EXHIBIT NO. 1

27
11-23-04

# City of Alexandria, Virginia

## MEMORANDUM

DATE: NOVEMBER 19, 2004

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: PHILIP SUNDERLAND, CITY MANAGER PS

SUBJECT: CONSIDERATION OF A POLICY REQUIRING FISCAL IMPACT ANALYSES FOR PROPOSED MAJOR DEVELOPMENT PROJECTS WITH SIGNIFICANT FISCAL IMPACTS

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**ISSUE:** Whether or not fiscal impact analyses should be undertaken on proposed major development projects.

**RECOMMENDATION:** That City Council consider whether to adopt as City policy, or as a one-year pilot program, the preparation of Fiscal Impact Analyses, as detailed in this report, for proposed major development projects in the City.

**INTRODUCTION:** This docket item is in response to the request by Councilman Krupicka and Councilman Smedberg for the City to consider providing additional fiscal impact analyses for major new development projects in Alexandria. It explores the best uses of fiscal analyses, highlights the main issues of this process, and suggests a methodology for estimating project fiscal impact.

Fiscal impact studies come in various sizes and shapes, from the very complex to the very simple and straightforward. As they become more complex, deviating from directly measurable revenues and costs, they become increasingly subjective, and, depending upon the complexity of the subjective assumptions made, offer less and less reliability. Oftentimes, from the experience of other jurisdictions, they can generate new controversy, whatever the approach taken, and can give a false sense of precision.

Fiscal impact analyses are most useful for large projects or for project financings. Fiscal impact analyses have been used in the past by the City on very large projects, such as Cameron Station, USPTO and Potomac Yard, and will be used on the Landmark Mall redevelopment project. Fiscal analyses at these large project levels are more useful than analyses at the smaller project level. Smaller scale analyses are highly subjective and, therefore, are of relatively limited value.

Should Council wish to include a Fiscal Impact Analysis component in the review of major new development projects, such an analysis should only focus on the primary direct financial impacts to the City, and should not try to determine potential secondary or indirect benefits or costs that might financially affect the City. Such an analysis would look mostly at net new revenues to the

City and, in so doing, would consider only direct, measurable costs. We would suggest the following overall approach.

- The analysis should be kept simple. It should be limited to direct on-site generated project revenues (i.e., from real estate taxes, personal property taxes, utility taxes, transient taxes, sales taxes, meals taxes, and other consumer and business taxes). On the cost side, the analysis would only include City costs that are a unique and direct consequence of the project.

- We do not propose attempting to measure a project's indirect costs on City operating agencies, such as schools, public safety, recreation, and so forth. These incremental costs are usually not material and cannot be measured with any degree of precision, even with great effort. Nor do we propose that the analysis address the cost effects on general City services in the nature of overhead and operating costs, or long-term capital improvements that are not specifically identified as a unique consequence of the project being examined.

- We do not propose attempting to predict a project's *indirect* revenue impacts, such as anticipated off-site sales taxes from new residents or employees, or miscellaneous fees and payments (e.g., parking revenue) because this requires numerous, non-quantifiable assumptions.

- The approach, therefore, would measure what a given project actually and directly produces or requires, and thereby would provide information that is concise and usable.

**DISCUSSION:** Currently, the review of development projects includes a detailed analysis of a project's potential impacts, such as on open space, urban design, storm water management, neighborhood compatibility, traffic congestion and the transportation system. Where an adverse impact is found that results from the project, mitigating requirements are added as a project condition, such as an additional traffic lane or signal. In most cases, contributions towards affordable housing and open space are negotiated as part of the project review. Thus, the City benefits are balanced on a qualitative basis with the project's adverse community impacts. It is important to consider and balance all consequences of a project, positive and negative, and, in this regard, the fiscal consequences of a project constitute another factor to consider.

<u>HOW AND WHY COMMUNITIES MEASURE FISCAL IMPACTS</u>: A Fiscal Impact Analysis is a tool to estimate the financial impacts on the City of a defined development – on both the revenue side (tax revenue) and the cost side (operating and capital expenditures). The Fiscal Impact Analysis (FIA) we propose (in the event Council determines to require FIAs) would use pre-set, standardized spreadsheets initially framed by City staff, but with data initially provided by the applicant, to measure the future potential revenue and costs associated with a new development.

Typically, localities use FIAs as a basis for determining or legitimizing impact fees or cash proffers – fees assigned to new developments to cover the increased costs they are expected to cause local governments to incur.

FIAs are used extensively in states where impact fees are legally authorized, but Virginia law does not give the City the authority to mandate impact fees beyond water and sewer capacity charge fees. The use of FIAs in Virginia is usually in conjunction with a major up-zoning, which entails the determination of appropriate significant proffers (generally for schools and recreation in rapidly expanding suburban areas) for new residential developments.

For suburban development, localities usually use FIA studies as a "kid-meter" to determine how many children from a proposed new development can be expected to attend public schools. The localities use major rezonings as leverage in such instances. Thus, in effect, FIAs help localities capture part of the economic value of major up-zonings and use it to pay for the increased government costs that are directly attributable to the increased development allowed by the rezoning.

City staff contacted several Virginia localities about their use of fiscal studies, with the following results:

- Many localities use FIAs for "greenfield" rezoning approvals and/or for determining proffers, particularly for large residential developments in fast-growing areas. Such localities include Chesterfield County, Albemarle County, Frederick County, and the City of Chesapeake.

- Virginia Beach has used FIAs to effectively create a minimum value for new home construction in one semi-rural portion of the City.

- City staff have not located another built-out urban locality in Virginia that uses FIAs on a regular basis. Use is often on a case-by-case basis for major projects such as very large commercial developments, convention centers and sports facilities.

If not used in the formulation of impact fees or proffers, FIAs can give a general indication of the fiscal costs and benefits of a given development. This information can sometimes be useful when used in tandem with other quantitative and qualitative information. No matter how complex, a FIA cannot provide a simple "Yes" or "No" answer as to whether a given development will benefit the City.

There's a point at which a Fiscal Impact Analysis becomes too complex, and local governments sometimes waste valuable time in trying to capture every cost and revenue line item. In this instance, simpler is better – dealing with only the most dramatic and significant sources of impacts will provide the City with a useful estimate of impacts. Measuring impacts beyond these major sources will encounter much uncertainty in estimating base data. It is difficult to achieve great precision when these uncertainties are large.

RECOMMENDED FISCAL ANALYSIS: There are two aspects to the Fiscal Impact Analysis we would recommend, the **Revenue Side** and the **Cost Side**.

- **REVENUE SIDE:** The revenue side is income generated to the City that directly results from the new development, offset by any revenue that the property in question currently produces and that the new development will eliminate. This includes annual taxes (real estate, business taxes, etc.) and fees that are applied to the buildings or occupants. Following is a listing of revenue sources we would recommend be included in a City FIA; also provided is a list of sources we would recommend not be included in a FIA.

    - **Recommended: Residential-based Tax Revenue** (real estate tax, vehicle personal property tax, consumer utility taxes), and **Business-based Tax Revenue** (business license tax and business personal property tax). Should an analysis of another type of use (e.g., restaurant, retail, and hotel) be needed, the calculations would be modified accordingly and other local taxes added, such as sales, transient occupancy and meals taxes.

    - **Not Recommended:** Indirect tax revenue sources such as sales taxes (generated off-site by residents' or employees' purchases), revenue related to a project's construction phase, and miscellaneous non-material fees and payments (e.g., parking revenue).

- **COST SIDE:** The cost side reflects expenses borne by the City in order to provide services and infrastructure, made necessary by the new development, offset by any City expenses arising from property in question that will be eliminated by the new development. Following is a listing of the recommended and non-recommended cost sources:

    - **Recommended: Direct operating and capital cost impacts**. These are the costs of providing services and new or expanded infrastructure that are clearly and directly triggered by the given development. They are costs that can be measured without making potentially controversial speculative assumptions.

    - **Not Recommended:** City incremental operating cost impacts. These include non-material impacts on specific services, and non-material. incremental demands placed on capital improvements. Other costs, such as general city administration, are also not recommended. In general, the increased costs of providing City services, such as public safety, schools, and street maintenance, would not be counted unless the development was so large (such as the future development of Landmark Mall) that the costs of added City services (such as police coverage) were truly material and measurable.

This kind of analysis is aimed at evaluating only those revenues and costs that have a directly measurable relationship to the development activity. We believe that more detailed studies would be too subjective and less reliable, in addition to requiring extensive staff time (or hiring of outside consultants) that could be used in other ways.

<u>FISCAL IMPACT ANALYSIS MODEL</u>: The FIA we would propose would, for most projects, use a standardized spreadsheet approach involving the use of formulas that are based on measurable, or otherwise defined, assumptions. The use of a pre-established model expedites the FIA process, assures greater uniformity among different projects being analyzed, and is crucial to devising a reasonably objective approach to measuring impacts.

This FIA model would take into account ongoing revenues and costs. The assumptions of the model (e.g., demographic and fiscal data) can and would be changed as new information becomes available. The FIA would be a joint project of Planning and Zoning, OMB and Finance, who would develop general unit measures (e.g., real estate taxes per square foot of office) and the model structure.

<u>APPLICATION OF FIA MODEL</u>: For consistency between different projects, City staff would perform the FIA, as opposed to having developers or outside consultants do the work. The approach would be to develop a standardized model that can be modified as necessary to address individual projects. A work sheet would be prepared for developers to submit specific information needed to evaluate specific projects.

Spreadsheet templates would calculate these impacts. The templates would allow for the input of a relatively small amount of data, and the resulting fiscal impacts would be quickly calculated. Individual templates would be used for residential, office, retail and other development.

Planning and Zoning would be the staff contact with developers on the FIA, with OMB advising and providing the final certification of the FIA numbers. The results of the FIA would be included in Planning and Zoning reports (starting in January 2005) on major development projects that are provided to the Planning Commission and City Council.

<u>EXISTING SITUATION</u>: The analysis would include a summary of what the property being examined is *currently* "contributing" to City revenues and expenses. In all instances, this would include examining revenues from real estate taxes and estimating any existing utility or residential-based taxes. Other revenue sources (such as business license taxes) would be examined if such information is available (such as business taxes). However, to avoid disclosing confidential data regarding individual businesses, such information may not be obtainable in all cases. As a result, averages or other proxy measures and estimates (such as sales tax revenues based on City-wide average retail sales per square foot) may need to be used.

MINIMUM PROJECT THRESHOLDS: As stated earlier, a fiscal analysis is most useful for very large development projects. The suggested minimum threshold would be projects that contain at least 250 units for residential projects and 250,000 gross square feet for office and other commercial space. Using projects from the past decade as a guide, below is an estimate of the number of such sized projects that have come on line in Alexandria in a typical year.

| **Threshold** | **# of Projects per Year** |
|---|---|
| 250,000 SF of commercial development | 1 to 2 projects |
| 250 residential units | 1 to 2 projects |

PROJECTED TIME FRAME: The fiscal impact model would project annual impacts for when the project has achieved full buildout and is fully operational. This avoids the complexities of factoring in phases of development that can obscure a project's benefits and/or costs.

DOLLAR AMOUNTS: All dollar amounts would be kept in current-year dollars. This makes the calculations easier to judge, and avoids introducing additional variables into the equation, such as inflation or discount rates, that are quite speculative and subject to manipulation to achieve desired outcomes.

**FISCAL IMPACT:** At this time, the FIA process and model, as proposed, can be handled with existing City staff and appropriated budget resources. However, if the FIAs were expanded beyond the scope described above, additional budget contract resources and possibly additional staff would be required.

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