The Loudoun County FY2020 Budget – Context and Implications

The main headlines underscored in February's rollout of the LC FY2020 budget were:

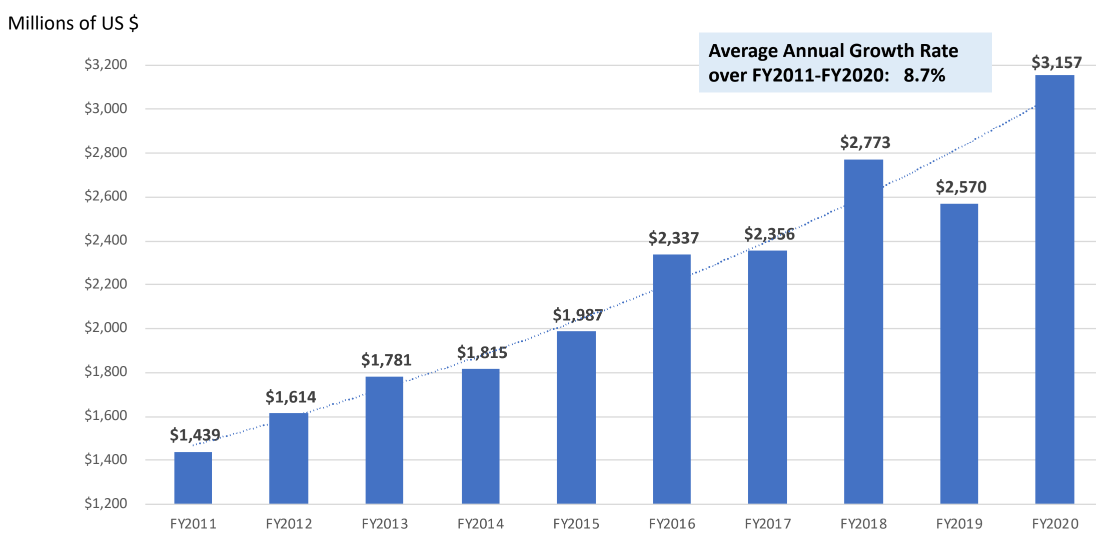
1. The tax rate on real personal property (the 'real estate tax') will fall by 4 cents to $1.045;
2. Prepared at this rate, "the proposed budget is designed to address the needs of our growing organization and community"; and
3. The LCPS adopted budget request is fully funded by the County budget at this tax rate.

But the two-volume budget document of 907 pages tells much more.

Total appropriations growth is record-rivaling

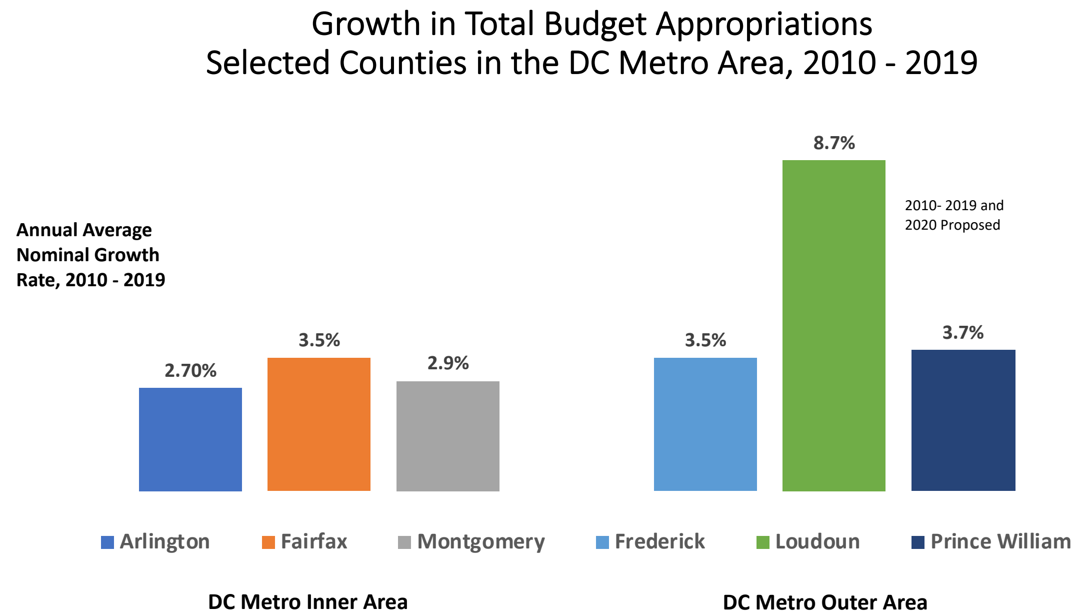
The proposed budget reveals an eye-popping 23% increase over FY2019 in Total Budget Appropriations: that is, $587 million more than last year's $2,570 million. This is the largest annual increase in 15 years (FY2005 = +26%). It is more than double the galloping long-term average annual growth of 10% since FY2000 and nearly triple the average rate since FY2011.

Loudoun County Total Appropriations Budget
Values and Average Growth Rate, FY2011 - FY2020 (proposed)



Sources: Loudoun County Adopted Budgets, FY2011-FY2019 and proposed FY2020 Budget

The budget aggravates a longer-term trend in which the average growth in Loudoun's total public budget appropriations runs at more than twice the rate of both major inner area and outer area counties in the Washington DC Metro area.



Sources: Annual Adopted Budgets of each County

Operating expenditures and debt service costs will accelerate beyond FY2015-FY2019 rates

Government operating appropriations will surpass the already strident growth rates of 7.1% annual average over FY2015-FY2019 with a jump in FY2020 of 8.6%:

- The Government's general operating expenditures will grow by 9.5%, driven by a 5% hike in employee compensation, a nearly equivalent increase for 'targeted individual adjustments' and 193 new government positions; and

- The County's contribution to the School Fund will rise by 8.2% to fully fund the budget request of LCPS.

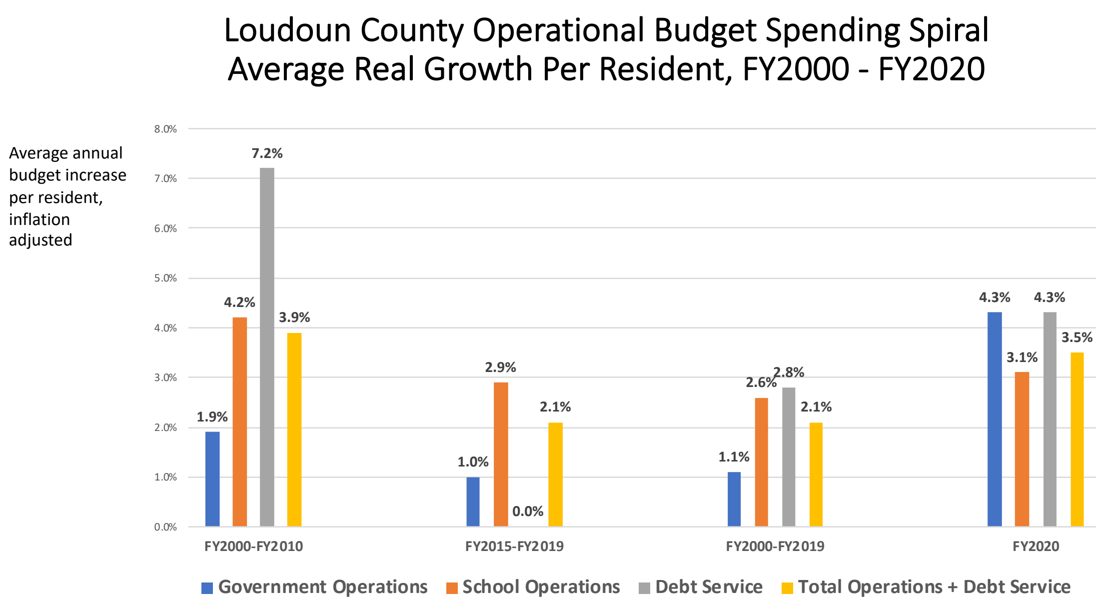
Debt service appropriations are scheduled to rise by 9.5% to $224 million, or double the average rate of the last four years.

Within the Amended Six-Year FY2019-2024 CIP, though the total has not changed significantly from last year, the FY2020 expenditure portion will jumped by $141 million, or 41%, due in particular to the $59 million expansion in transportation (14 new projects) and $120 million for additional school investments.

Continuing strong demographic pressures and per resident hikes are responsible

Demographic pressure - the County Government's continuing expansive housing policies result in about 11,000 additional residents every year. This annual average of about 2.8%, remains about *threefold the average population growth rate of the Washington DC Metro area and* drives up government and school operating costs accordingly.

Operational spending spiral per resident – above and beyond new residents, the FY2020 proposed budget continues Loudoun's operational spending spiral: government and school operating budgets together will *rise about 3.4 % per resident in real terms* (that is, adjusted for expected inflation), exceeding a two-decade old average pattern of 2.0% per year.



Sources: Loudoun County Adopted Budgets, FY2011-FY2019 and proposed FY2020 Budget

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Data centers, debt and the NVTA will pay for rapid expenditure growth

The total growth in government and school operating expenditure over FY2019-2020 of $158 million in all will be covered by $104 million in additional personal property taxes, essentially from data centers, and by $54 million from real property taxes and other local sources.

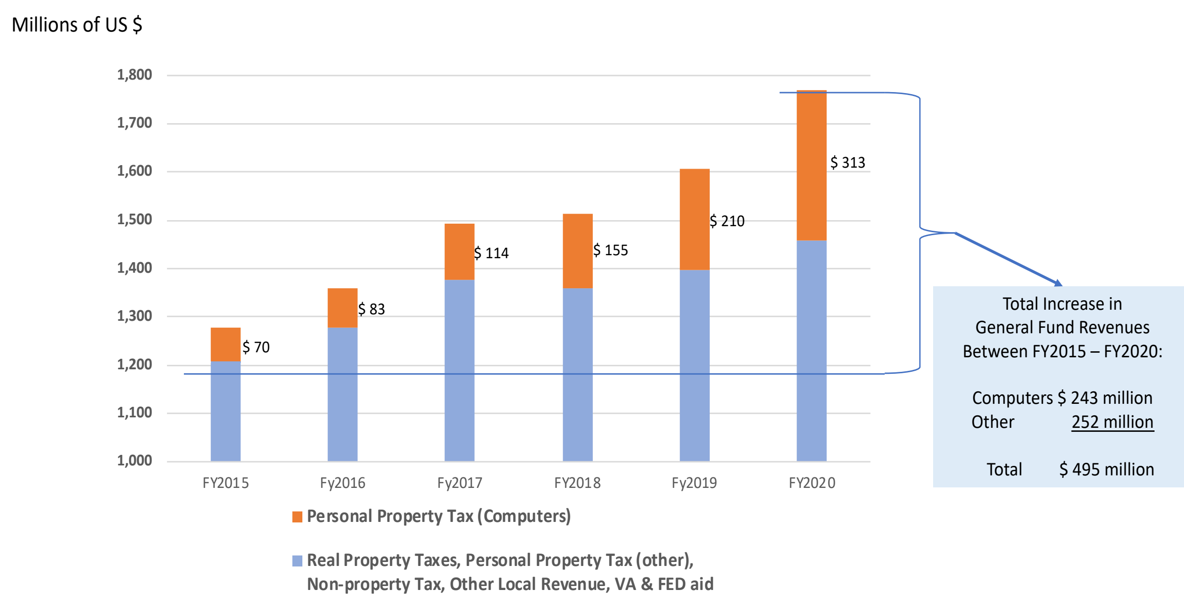
The total increment in FY2020 capital expenditures of $141 million will be financed mainly by a combination of $89 million more in new debt issues more funding from the NVTA.

Implication 1 - This deepens the dependency on a temporarily fast-growth data center sector

The FY2020 budget raises the County's fiscal risk bar with its combination of (1) growth by nearly 50% in personal property tax revenues stoked new data center development, and (2) the appropriation of these funds to support growth in essentially *non-discretionary* operational budget activities for government services and schools.

The risk is not so much a concentration of data centers personal property taxes in total budget resources – they have grown from 5.5% to 13.0% of total General Fund revenues between FY2015-FY2020. It is that FY2020 continues a six-year trend in which *data centers have met fully one-half of the total growth in public budget bill*. This dependency for new funding leaves the County exposed, fiscally and physically, to broader shifting corporate and global technological trends that may require jarring fiscal adjustments to close fiscal gaps.

Loudoun County – Additions to General Fund Revenues
From Personal Property Taxes (computers) and Other Sources, FY2015 - FY2020



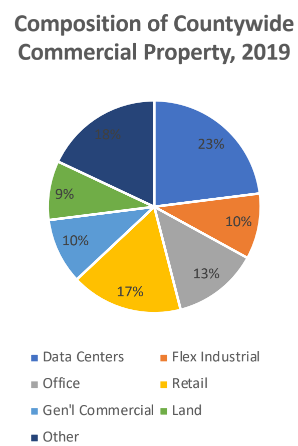
Sources: Loudoun County Adopted Budgets, FY2011-FY2019 and proposed FY2020 Budget

Implication 2 – risks to the broader business community and fiscal revenues

The data center fiscal risk is exacerbated by other business risks. Unlike neighboring areas such as Fairfax VA, Montgomery MD and DC with substantially larger economies and higher average skill profiles and earnings levels, Loudoun's economic composition is disproportionately weighted toward construction, niche manufacturing, retail and wholesale trading, transportation and warehousing. Its non-information economy has shown a tendency to grow at much the same rate as County's annual population as reflected in land use (square feet). Between 2010 and 2016, it averaged 1% to 4% per year depending on business type, with an overall average of 2.4% per year.

Loudoun's Non-Data Center Economy
Growth in Space by Business Type, 2000-2016

Growth in Commercial Property, 2000 - 2016			
% Annual Average Increase in Square Feet	2000-2016	2000-2010	2011-2016
Total	**4.7%**	**5.5%**	**3.4%**
Low Density Office	2.2%	3.1%	0.9%
Flex Industrial	3.7%	3.5%	3.9%
Retail	5.0%	6.7%	2.5%
Other	4.6%	5.5%	3.4%
Total Non-Data Center	**3.9%**	**5.0%**	**2.4%**
Data Centers			17.5%
Source: 2012 and 2017 Fiscal Impact Committee Guidelines			



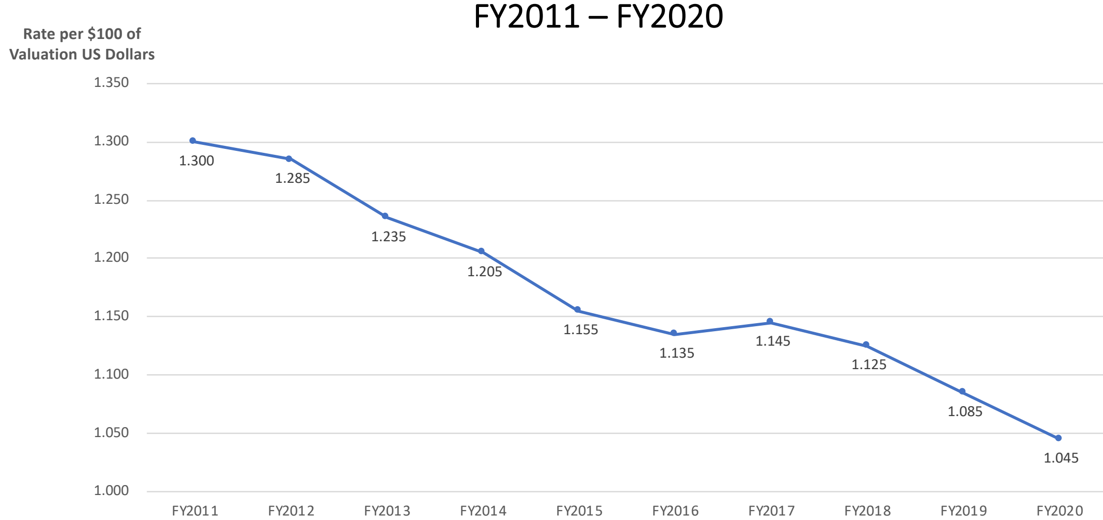
The future prospects of this community are not improved, and may well be undermined, by the County's embrace of data centers, given particularly their growing land use, high utility demands for water and energy, and effects on land values – Government property valuation reports show unusually high increases in commercial property values: 5.9% for 2017 and 6.9% in 2018, up sharply from an average of 1.7% over the previous three years.

Fiscally, Loudoun's non-data center business community contributes in total about 16% of the real property tax base. Rough math shows that it will contribute about $144 million of the total of $909 million in real property tax revenues budgets for the General Fund in FY2020. From a risk perspective, it is reasonable to expect this community to continue to help defray homeowners real property tax bill as the overall regional economy grows. However, it seems highly unrealistic to expect, especially in the shorter-term, that it will be able to step into the fiscal shoes of data centers.

Implication 3 – the unsustainable, growth-dependent real property tax policy persists

Under the BOS 'equalized tax rate' policy, Loudoun's real property tax rate continues its long decline since FY2011. The real estate tax rate will fall by 3.7% from $1.085 to $1.045 per $100 of real property value. This enable the average homeowner tax bill to remain stagnant in today's dollars at $5,100, and to continue its fall in 2010 dollars to about $4,365.

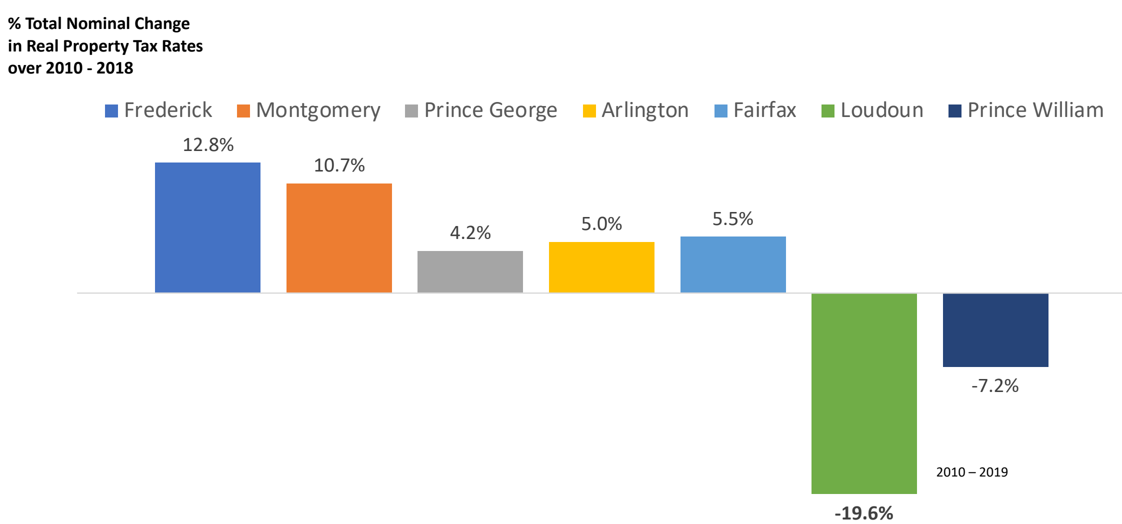
Loudoun County – Real Property Tax Rates
FY2011 – FY2020



Source: Loudoun County FY2000 – FY2019 Adopted Budgets; FY2020 Proposed Budget

This policy also continues to be quite unique among larger counties in the Washington DC metro area, which tend to make partial or complete corrections for the annual rate of inflation.

Total Change in Real Property Tax Rates
Selected Counties in the DC Metro Area, 2010 - 2018

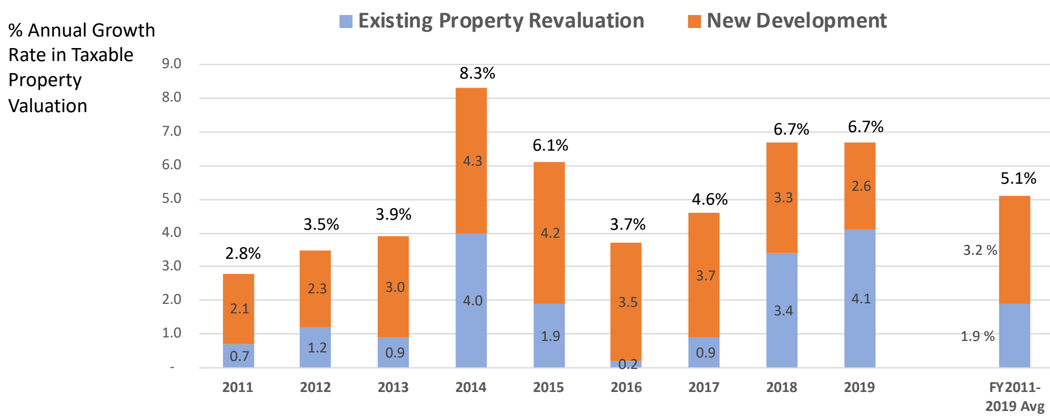


Sources: Annual Adopted Budgets of each County

Further, the real property tax rate calculations continue the BOS 'hooked on growth' policy of depending upon substantial growth in new development to expand the real property tax and revenue base in order to pay for high rates of budget expenditure growth.

The chart below illustrates this trend over the past 10 years, in which on average only 37% of the growth in the real property tax base has come from the revaluation of existing property. And this number is elevated by the softer housing market trend over 2017-2018, which has tended to (fortunately for existing homeowners) raise the revaluation rate. Even so, new development was a very essential element in enabling the County to boost the real property tax base by 6.7% per year in both the 2018 and 2019 valuation.

Loudoun County – Growth in the Real Property Tax Base
From Existing Property vs New Development, 2011 - 2019



% Existing Property Revaluation / Total Valuation Growth	2011	2012	2013	2014	2015	2016	2017	2018	2019		2011-2019 Avg
	25%	34%	23%	48%	31%	5%	20%	51%	61%		37%

Sources: Loudoun County Adopted Budgets, FY2011-FY2019 and proposed FY2020 Budget

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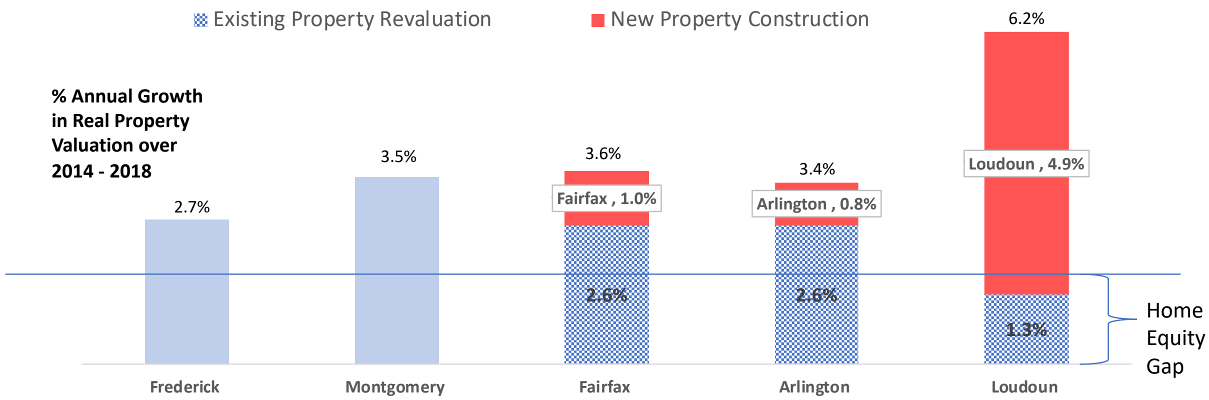
This real property tax policy, while effectively lowering a homeowners' real property tax bill on one hand, continues the practice of indirectly imposing on the other hand a 'growth tax' on existing residents. This tax takes the form, in particular, of additional housing sprawl, traffic congestion and extended waiting times, school crowding, air pollution and other environmental degradation, diminished green space, chaotic infrastructure construction, and crowding out of services for health, family, parks and recreations.

In the longer run, if not sooner, this unsustainable hooked on growth policy is likely to evolve into a more limited annual expansion of the property tax base and, either a reduction in the overall rate of budget expenditure growth to fit it, a rise in real property taxes, or a combination of both. This, in essence, is what is reflected elsewhere in the cross-county tax rate chart above and, given more limited data availability, is suggested in the chart below on the sources of growth in real property valuation in Fairfax and Arlington counties.

Real Property Budget Revenue Sources
Selected Counties in the DC Metro Area, 2014 - 2018



Growth of Existing Property Revaluation as Share of Growth of Total Real Property Valuation	Fairfax	Arlington	Loudoun
	72%	**76%**	**21%**

Sources: Annual Adopted Budgets of each County

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