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From: Julie Herlands, AICP, Vice President, TischlerBise

Date: May 11, 2017

RE: Portsmouth, Virginia, Comprehensive Plan: Fiscal Forces and Trends

Current Budget

The City of Portsmouth provides core public services to its residents and businesses through the General Fund. The General Fund budget is approximately \$240 million. The City uses other governmental funds that are separate from the General Fund to account for funding for specific/limited purposes. These funds may be funded by City revenues but are also typically funded from other sources such as the state or federal governments.

Major Governmental Funds	Minor Governmental Funds
General Fund	Special Revenue Funds
Debt Service Fund	Community Development Fund
Capital Improvements Fund	Cemetery Fund

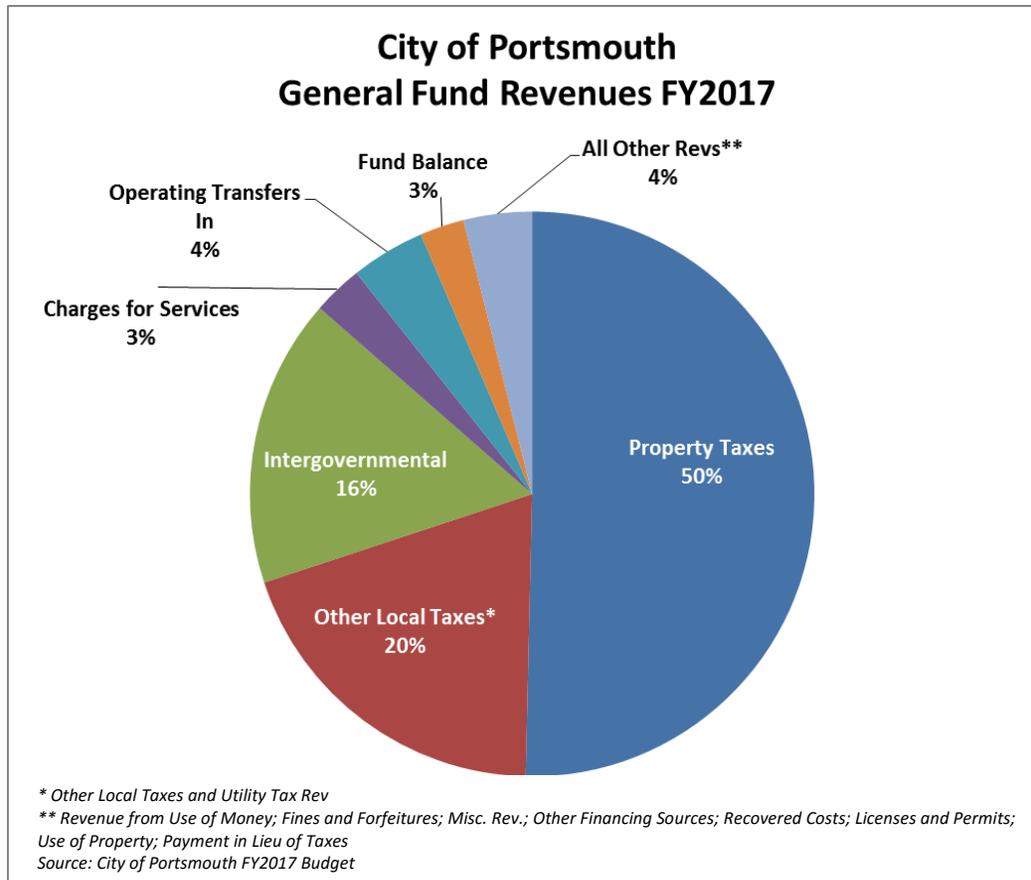
Other funds include:

- Enterprise Funds (Major Funds: Public Utility Fund, Parking Authority Fund; Minor Funds: Port Facility and Economic Development Fund, Waste Management, Golf Fund), which are for services that are operated like a business and generate sufficient revenues to cover commensurate expenditures.
- Internal Service Funds are for services that are provided between departments and are accounted for in four separate funds (City Garage Fund, Information Technology Fund, Risk Management, and Health Insurance and OPEB Fund).

Revenue Sources

The main revenue source in the City of Portsmouth is property taxes followed by other local taxes (includes: business and occupational license, cigarette, licensing, lodging, meals, and sales taxes). This is a typical Virginia revenue profile with half or more of General Fund revenues from property taxes. Other local taxes are sales taxes and business and professional occupational licenses (BPOL).

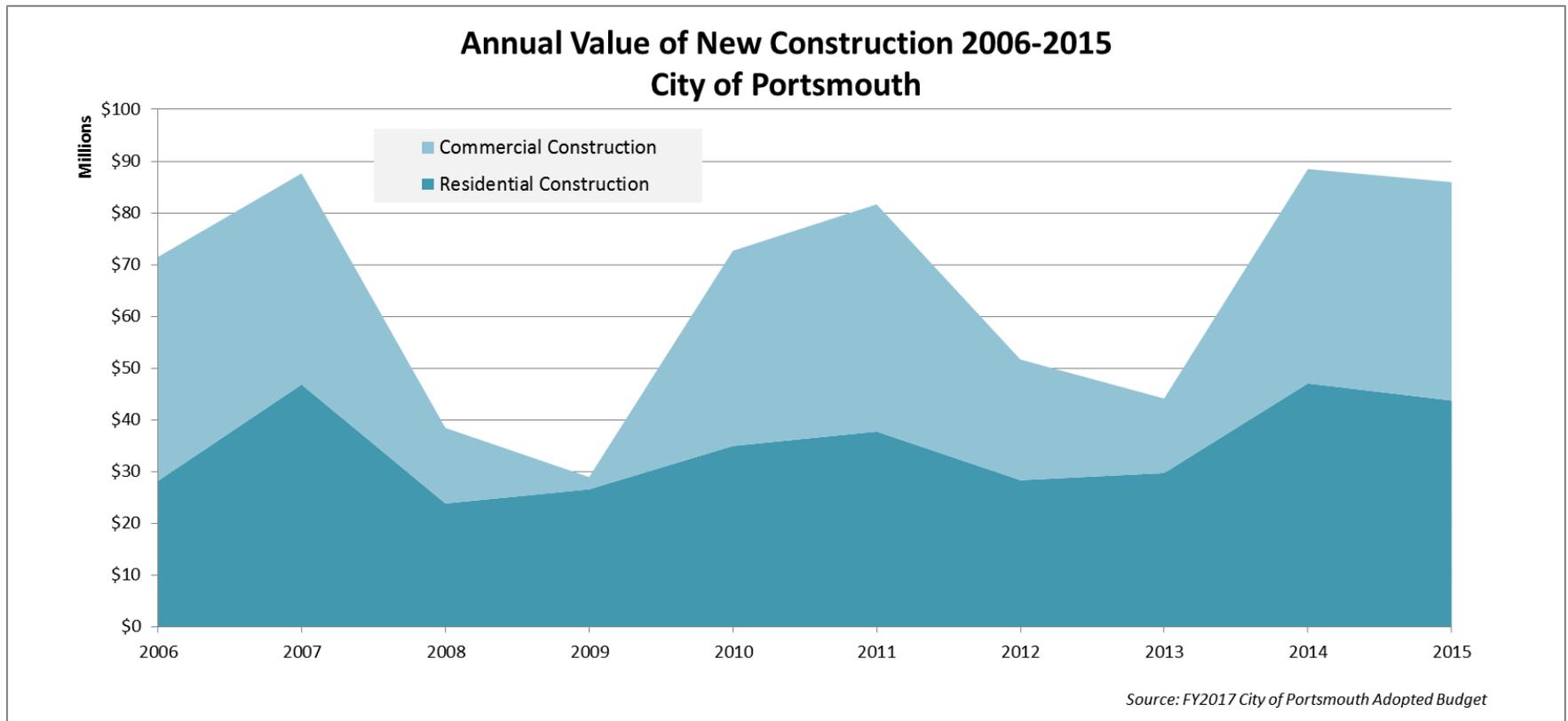
Figure 1. City of Portsmouth FY2017 General Fund Revenues



Construction Activity and Value

Value of new construction has fluctuated over the past 10 years with high points in 2007 and 2014 and a low point in 2009. Average growth is approximately \$65 million (in current dollars/not adjusted for inflation). Construction activity continued through the troughs of the recession and has increased through the recovery period for the most part. Commercial activity tends to be “lumpier” than residential activity, with sharper peaks and valleys, as one would expect given the nature of commercial construction.

Figure 2. City of Portsmouth Construction Activity (2006-2015)

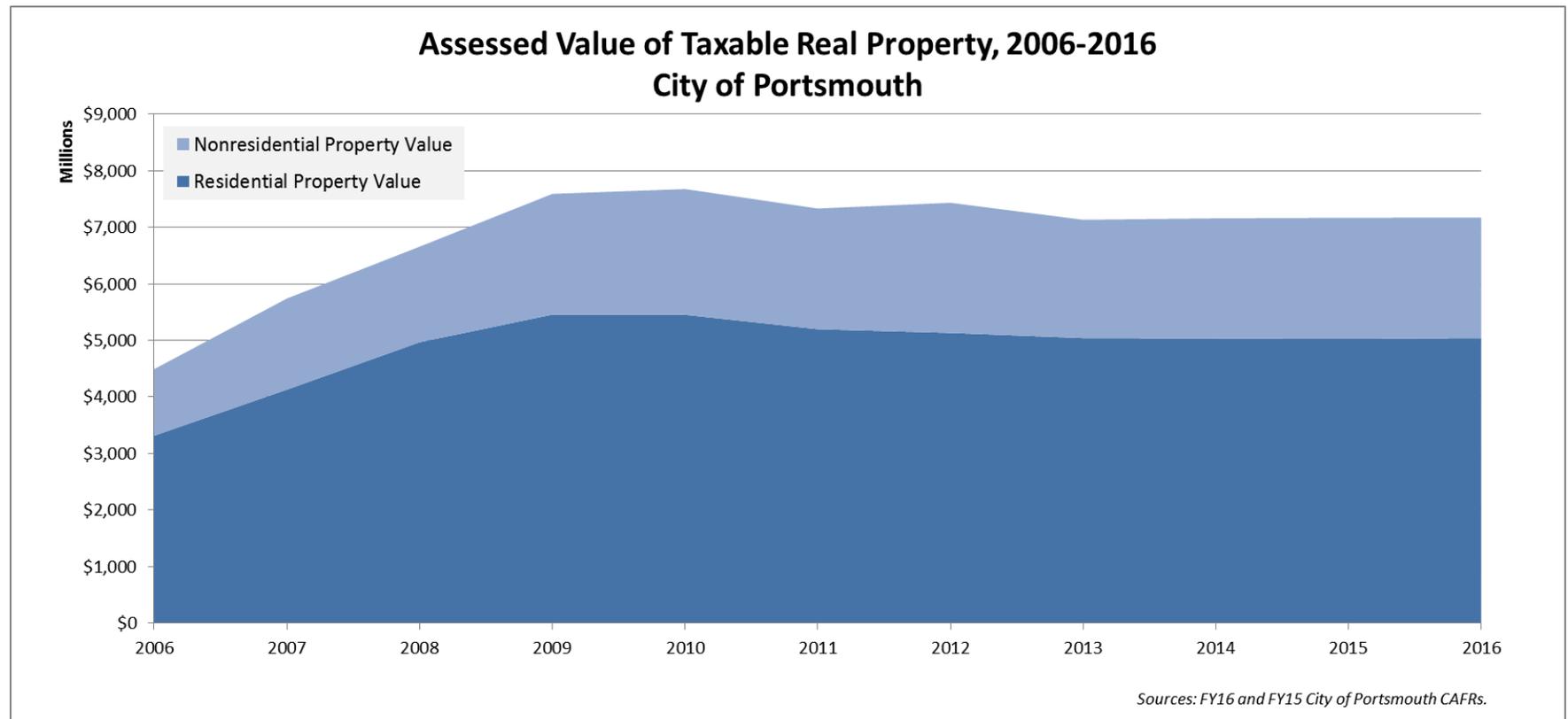


Property Values

A significant portion of the City of Portsmouth's real property base is non-taxable. As of the City Assessor's report in February 2017, of a total of \$12.8 billion in real property value in the City, **43 percent or \$5.5 billion** is non-taxable.

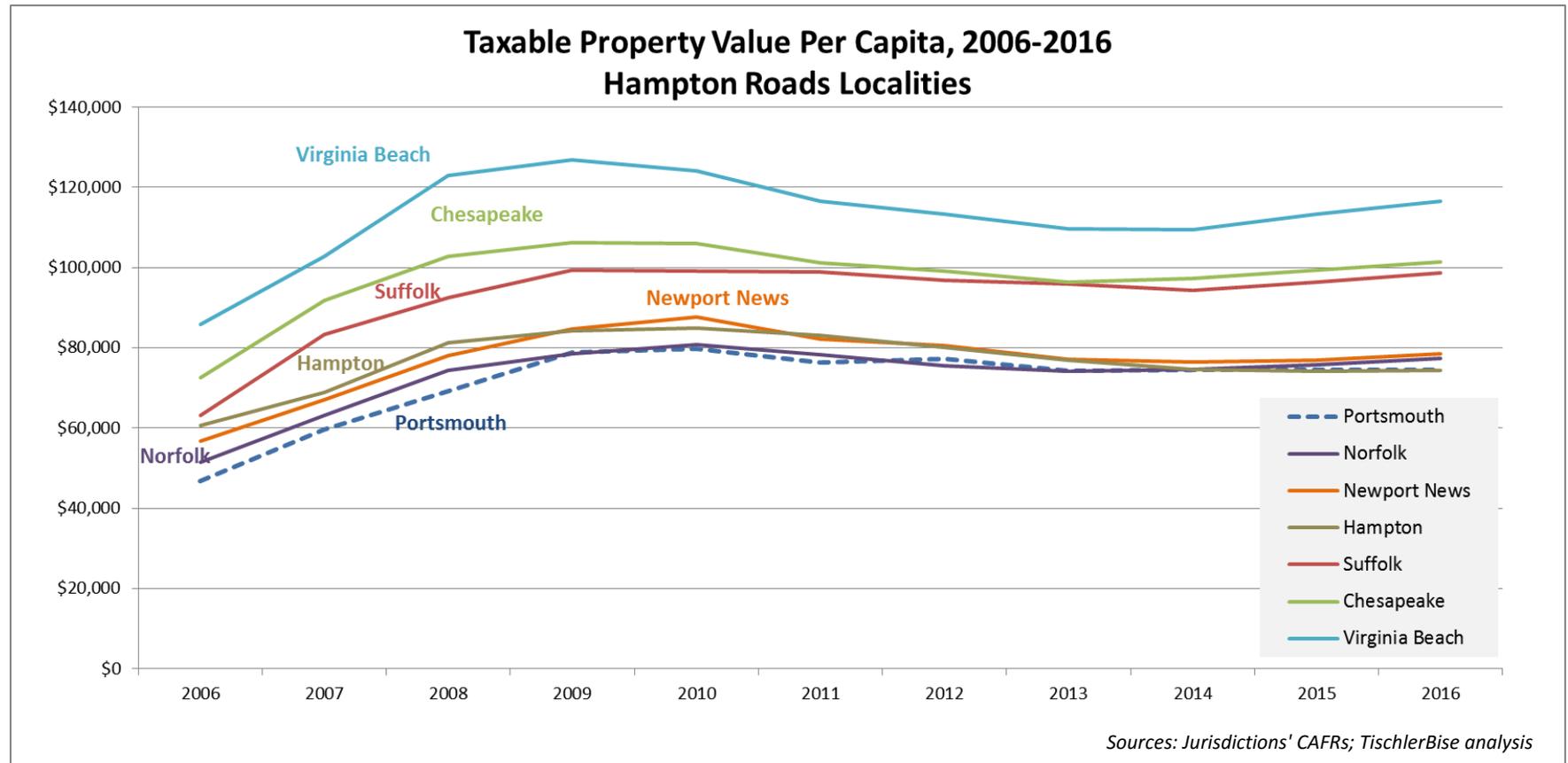
The value of Portsmouth's taxable real property base has plateaued in recent years after a growth prior to the Recession. Value peaked in 2010 at \$7.7 billion. Assessed value of taxable property in 2016 is \$7.2 billion. Residential values peaked in 2009 and have not returned to that level. Nonresidential values peaked in 2012 but have decreased in recent years. See Figure 3.

Figure 3. City of Portsmouth Real Property Assessed Value Trends (2006-2016)



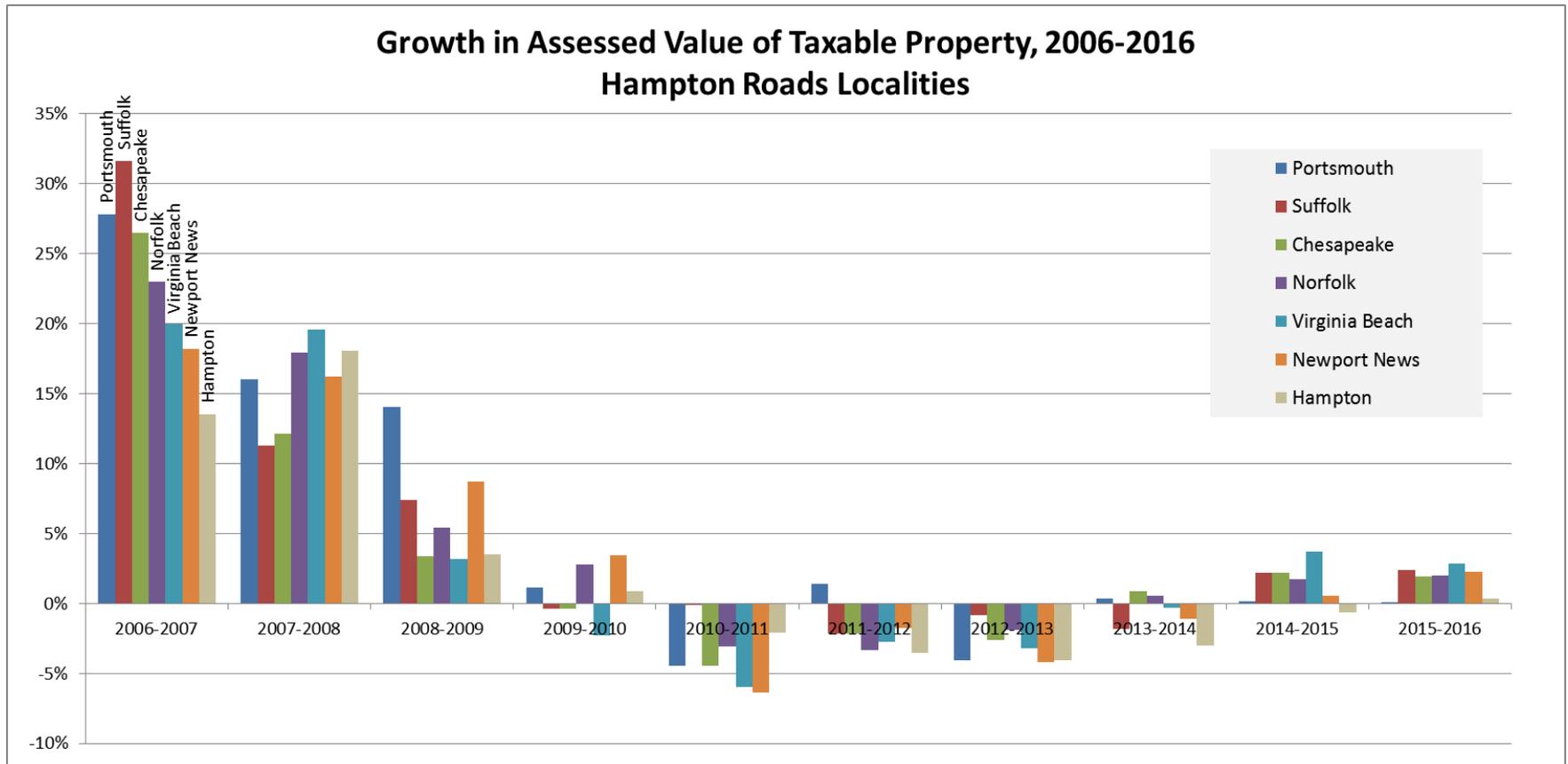
The City of Portsmouth consistently ranks at the bottom of per capita valuation among Hampton Roads’ localities due to the large share of non-taxable property. However, in recent years, per capita values have increased in the City from being the lowest in the region in 2006 with a relatively large spread of 45 percent from highest to lowest—to being clustered among the bottom four jurisdictions, with less of a spread between Portsmouth’s per capita value to the highest value (36 percent compared to 45 percent).

Figure 4. Comparison of Taxable Property Value per Capita in Portsmouth and Other Hampton Roads Jurisdictions



The City of Portsmouth is similar to other Hampton Roads’ jurisdictions regarding the recent flattening of property values. Minimal appreciation has occurred in the past two years after significant valuation growth before the Recession and decreases in value post-Recession. While some loss in value occurred, the Hampton Roads localities did not experience the deep double-digit losses in value experienced in some other areas of the country. Additionally, the City of Portsmouth only experienced two periods of decreased property values over this time period, unlike other localities in Hampton Roads. A comparison of property value changes is shown below in Figure 5.

Figure 5. Comparison of Property Value Growth and Decline in Portsmouth and Other Hampton Roads Jurisdictions



Fiscal Stress

The Commission on Local Government developed an index to measure “fiscal stress” of local governments in the Commonwealth of Virginia. They have produced this index since Fiscal Year 2002, providing a long-term view of fiscal pressures for the City of Portsmouth as well as how the City compares to other jurisdictions in the Hampton Roads region.¹

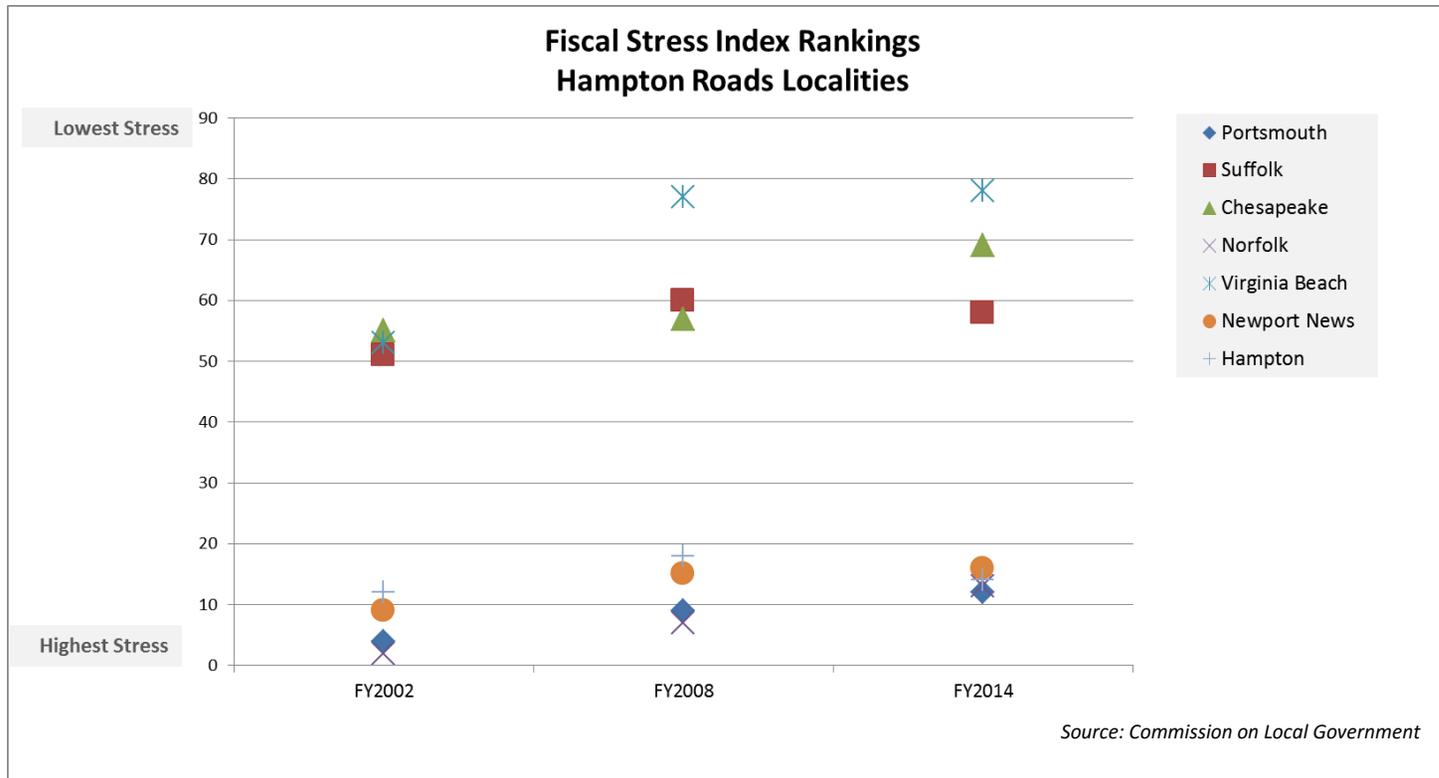
The Fiscal Stress Index uses a statistical average of relative stress scores based on revenue capacity per capita, revenue effort, and median household income of Virginia’s 95 counties and 38 cities.² It illustrates a locality’s ability to **generate additional local revenues from its current tax base relative to the rest of the Commonwealth**. Once the index is calculated, counties and cities are ranked 1 through 133, with 1 representing the most fiscal stress and 133 the least.³

¹ *Report on Comparative Revenue Capacity, Revenue Effort, and Fiscal Stress of Virginia’s Cities and Counties*, Commission on Local Government, May 2016. Reports from FY2014 (latest available), 2007/08, and 2001/02 consulted. Available at <http://www.dhcd.virginia.gov/index.php/commission-on-local-government/fiscal-stress-in-virginia-local-government.html>

² Revenue capacity is a computation of how much revenue a jurisdiction could generate if it taxed its population at statewide average rates. Revenue effort is a ratio of actual tax collections by a locality to its computed revenue capacity. Median household income represents the level at which exactly half of the households in a jurisdiction earn more and the other half earns less.

³ The number of independent jurisdictions decreased from 134 in FY2002 to 133 in FY2014.

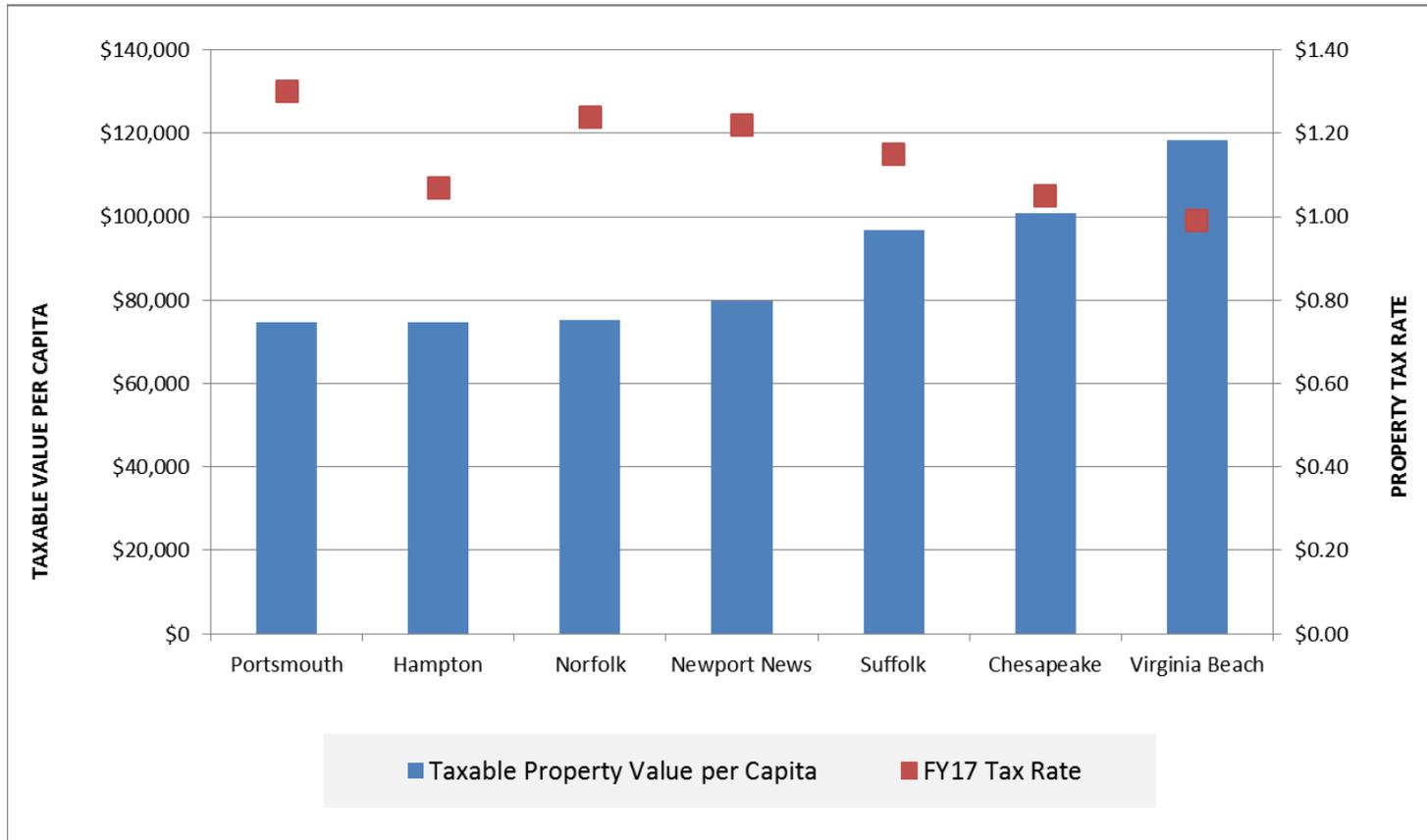
Figure 6. Fiscal Stress Index for Portsmouth and Other Localities in Hampton Roads



- The City of Portsmouth consistently ranks as a “High Fiscal Stress” locality, along with Hampton, Newport News, and Norfolk.
- “Above Average Fiscal Stress” localities in the region are Chesapeake and Suffolk.
- Virginia Beach is classified as “Below Average Fiscal Stress” in FY2014, which is an improvement from FY2002 when it was identified as Above Average Stress.
- Statewide, a higher percentage of *cities* experience above average fiscal stress when compared to *counties*.
- While the City of Portsmouth has improved its position relative to other jurisdictions since 2002, the City continues to experience fiscal stress, particularly when it comes to revenue capacity.

This challenge is further illustrated when comparing the City of Portsmouth’s tax base and property tax rate compared to other jurisdictions in the Hampton Roads region. Portsmouth has the lowest per capita property value and the highest property tax rate in Hampton Roads. This illustrates the challenges brought about by a large amount of tax-exempt property in the City.

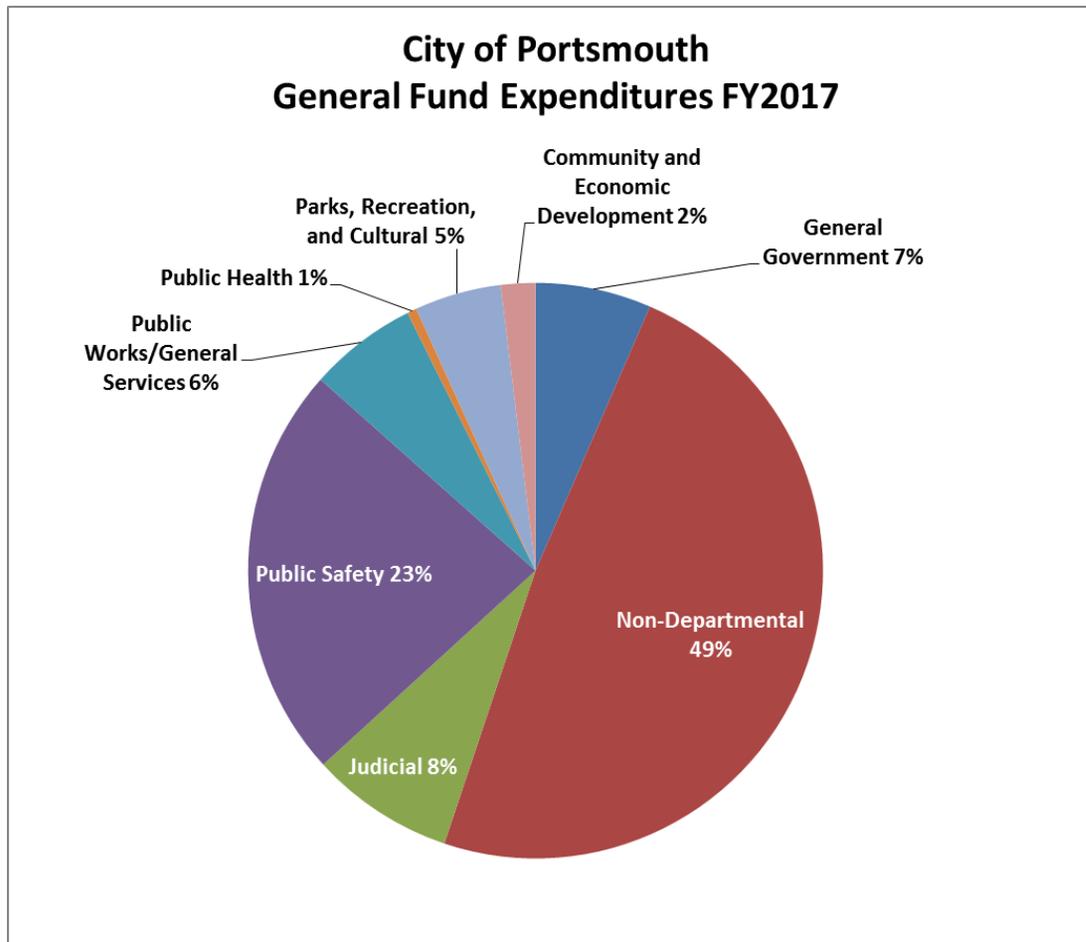
Figure 7. Real Property Tax Rates Compared to Real Property Values for Portsmouth and Other Localities in Hampton Roads



Expenditures

The single largest expenditure for the City is non-departmental expenditures, the majority of which are for the City's contribution to the school system and debt service payments. The next largest expense is for public safety (police and fire combined) then judicial services, general government, and public works. Like revenue structure, this expenditure profile is relatively typical for Virginia communities. Most Virginia jurisdictions spend approximately 50 to 60 percent of their budgets for schools followed by public safety.

Figure 8. City of Portsmouth FY2017 General Fund Expenditures



Population in the City of Portsmouth has remained relatively stable over the past 10 years at around 96,000. During the same period, per capita expenditures have also remained relatively flat. Given revenue capacity limitations in the City, the amount of revenue available for services is constrained. Despite per capita expenditures remaining stable during this time period, the number of full-time equivalent (FTE) employees (in all funds) decreased from a peak of approximately 2,240 to 1,550. This reflects a decrease in levels of service of FTEs per 1,000 residents as shown below in Figure 9.

Figure 9. City of Portsmouth Expenditures and FTEs per Capita, FY2010-FY2017

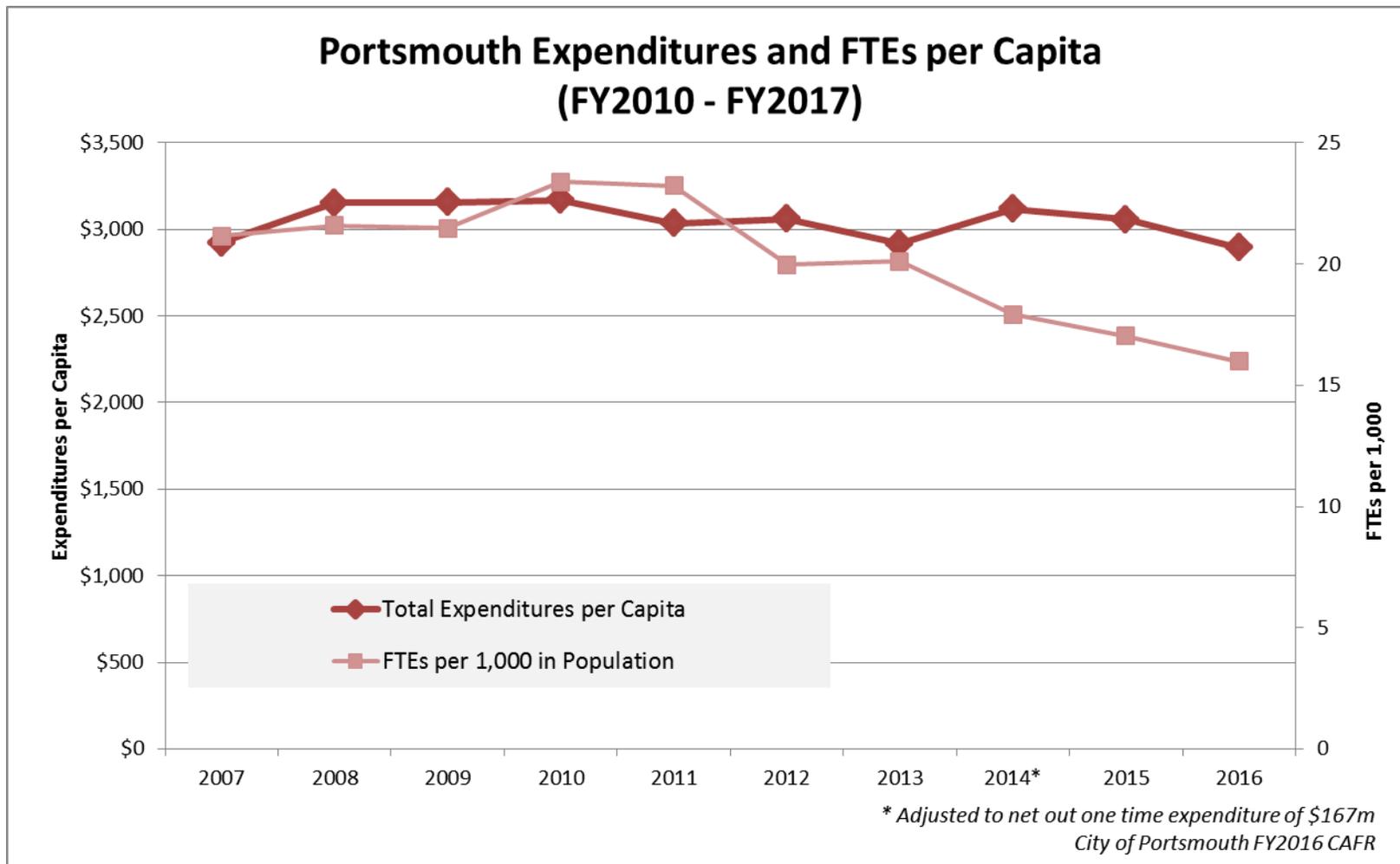
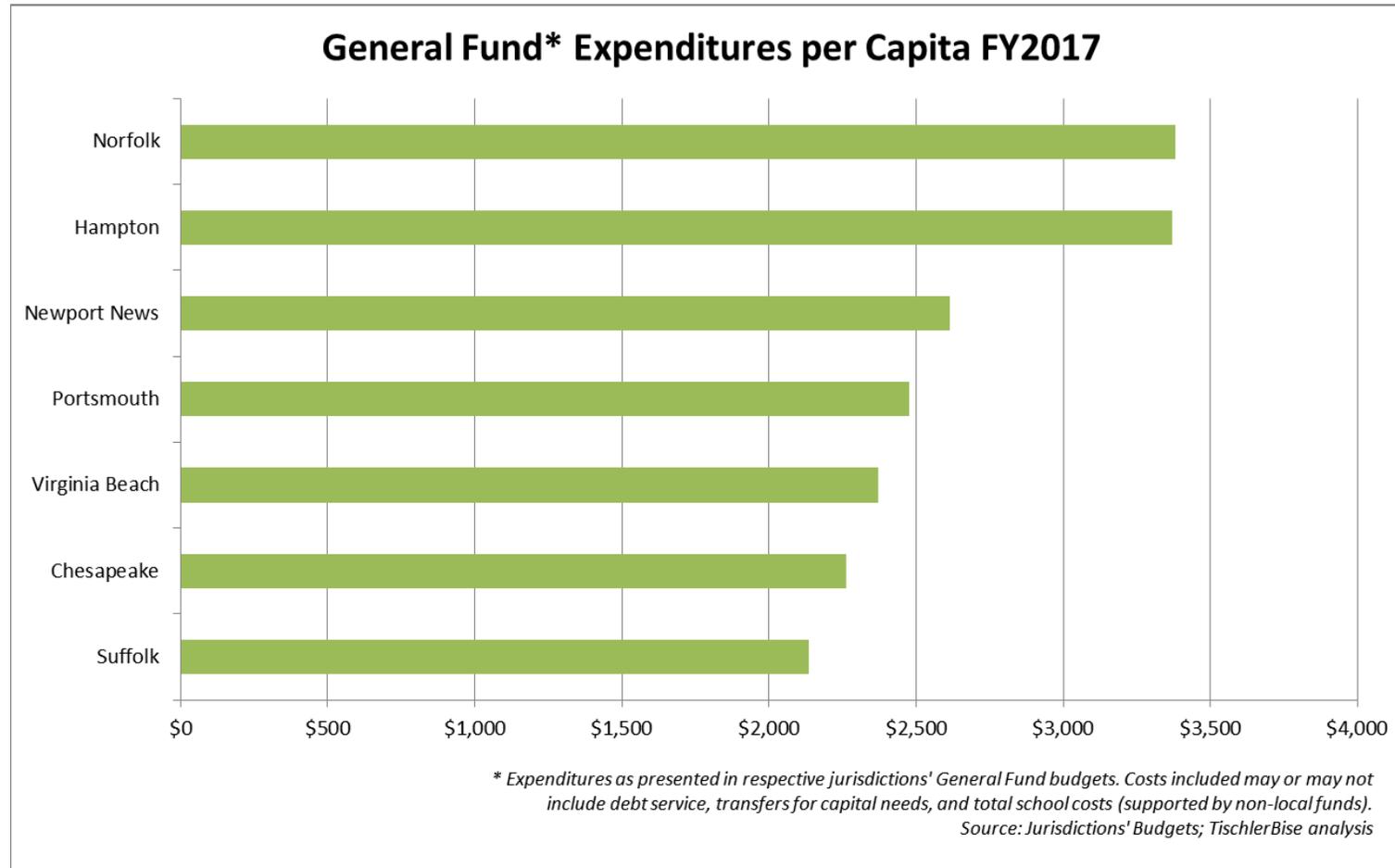


Figure 10 compares per capita General Fund expenditures in the City of Portsmouth to other Hampton Roads localities. As shown, the City of Portsmouth is the median of the group at \$2,475 per person. Only the cities of Norfolk and Hampton spend over \$3,000 per capita for General Fund services.⁴

Figure 10. General Fund Expenditures per Capita in the City of Portsmouth and Other Localities in Hampton Roads



⁴ As noted on Figure 10, expenses shown are those that are included in the respective localities' General Fund budgets. This may or may not include debt service, transfers for capital needs, and total school costs (including those costs supported by non-local funds). For these reasons, these comparisons should be viewed with this understanding and used with the above caveats.

Infrastructure

As noted above, population has remained flat in the City over the past 10 years. During the same period, the City has not added significant amounts of infrastructure (with the exceptions of park facilities and storm sewers). Unlike jurisdictions that expand into greenfields (and may annex adjacent properties), the City of Portsmouth is landlocked and, like all cities in Virginia, not able to annex property. This can be seen as beneficial from a fiscal perspective in that infrastructure is not expanding beyond what is needed to serve development or beyond the revenues available to maintain it.

Figure 11. City of Portsmouth Infrastructure Indicators, 2007 to 2016

	2007	2016
Streets (miles)	398	398
Signalized Intersections	130	122
Parks Acreage	402	588
Water Mains (miles)	543	626
Sanitary Sewers(miles)	437	438
Storm Sewers (miles)	159	250
Police Stations	1	1
Fire Stations	8	8

Source: City of Portsmouth FY2016 CAFR

Fiscal Considerations

As the City updates its Comprehensive Plan, it is a good opportunity to investigate how land uses and development patterns might help the City achieve fiscal sustainability. The key challenge for the City at this time is expanding the real property tax base to mitigate the effects of non-taxable property in the City. Recent redevelopment efforts are encouraging and further investigation into the fiscal impacts of those land uses may be worthwhile.

Some factors to consider when thinking about fiscal impacts from different types of land uses are: the local revenue structure, local levels of service, capacity of existing infrastructure, as well as the demographic and market characteristics of new growth.

- **Local Revenue Structure:** A key factor is local revenue structure. In Portsmouth, property tax is a main revenue source followed by sales taxes. Because of this, taxable property values are often the key driver for fiscal impacts in Virginia localities.
- **Levels of Service:** Another important factor in the fiscal equation is the levels of service currently being provided in a community. Existing levels of service is defined as the facility or service standard currently being funded through the budget. Examples of level of service standards are pupil teacher ratios (i.e., 1 teacher per 24 students), parkland per capita, etc. This is an important factor since levels of service generally vary from community to community.
- **Capacity of Existing Infrastructure:** The capacity of existing infrastructure in a community also has a bearing on the fiscal sustainability. For example, a community may have the capacity to absorb a large number of additional vehicle trips on its existing road network or may be significantly under capacity with regards to high school enrollment. In either of these situations, accounting for existing capacities in facilities and levels of usage may have positive fiscal impacts given that existing facilities might be able to absorb growth over time without making additional infrastructure investments. This excess capacity could result in lower capital costs over time. This is an important factor in the fiscal equation, since the largest cost associated with capital facilities are the annual operating costs, which typically account for approximately 80 percent of a community's budget.

- Demographic and Market Characteristics of New Growth:** Next to a community’s revenue structure, no other factor has as great an impact on the net fiscal results as the demographic and market characteristics of different land uses. Examples of demographic and market variables for residential development include average household sizes, pupil generation rates, market value of housing units, trip generation rates, density per acre, and average household income. Important demographic and market characteristics for nonresidential development include square feet per employee, trip generation rates, market values per square foot, sales per square foot (retail), and floor area ratio. For the City of Portsmouth, redevelopment into higher density residential development has the potential to be fiscally beneficial with smaller multifamily housing units that do not generate significant numbers of public school students.

An example from the City of Falls Church is provided illustrating the difference in student generation rates by type and size of a housing unit with a special emphasis on multifamily units given this is the source of most new housing growth in the City. The key driver for the City is the **size of the unit and whether the unit is renter- or owner-occupied**. Larger rental units tend to yield more public school students than smaller, owner-occupied units.

Figure 12. Example of Variation in Demographic Characteristics: Student Generation Rates for Multifamily Units

