Prince William County, despite being the unofficial foreclosure capital of Virginia, has achieved outstanding accuracy in its annual revenue forecast during the current, economic recession. While most jurisdictions were reducing budgets due to revenue shortfalls during Fiscal Year 2009 (FY2009), Prince William County actually ended the fiscal year with a $4.8 million general revenue surplus (a variance of 0.6% from the adopted budget). This was accomplished despite experiencing over 13,000 foreclosures between calendar years 2006-2009 which accounted for nearly 10% of the County's total housing stock. Prince William County is also anticipating an accurate revenue forecast for FY2010 as current projections again indicate a small, revenue shortfall of $4.2 million and another variance of less than one percent (0.6%) compared to the adopted general revenue budget.

These outstanding accomplishments during uncertain economic times are due to Prince William County's revenue forecasting process. The County's value driven process utilizes internal and external partnerships to develop a multi-year revenue forecast used in developing an annual Five Year Fiscal Plan. Internal partnerships include collaboration by representatives on Prince William County's Revenue Committee, which is comprised of cross-functional County government agencies such as the Finance Department, development service agencies, and a representative from the County's School system.

The Revenue Committee also relies on external partnerships to identify new economic issues and trends not readily apparent through the internal partnerships. External partnerships with the Prince William Association of Realtors provide the Revenue Committee with updates on the County's real estate market. Other important external partners include representatives from the Virginia Department of Taxation and the Federal Reserve Bank of Richmond who discuss the Commonwealth's budget as well as the state and federal economy. These external partnerships help Prince William County identify and adapt its revenue forecasting process to changing economic developments in the community. One example of this adaptation is the creation of a 'real estate dashboard,' which is used to evaluate the County's multi-faceted real estate market due its high foreclosure rate. Due to the collaborative nature of the revenue forecasting process, Prince William County has been able to evolve and effectively manage its budget during exceptionally difficult economic circumstances.

Prince William County

Revenue Forecasting Process

Accurate, Multi-Year Revenue Forecasting During Recessionary Times

June 1, 2010

Overview:

Prince William County, despite being the unofficial foreclosure capital of Virginia, has achieved outstanding accuracy in its annual revenue forecast during the current, economic recession. While most jurisdictions were reducing budgets due to revenue shortfalls during Fiscal Year 2009 (FY2009), Prince William County actually ended the fiscal year with a $4.8 million general revenue surplus (a variance of 0.6% from the adopted budget). This was accomplished despite experiencing over 13,000 foreclosures between calendar years 2006-2009 which accounted for nearly 10% of the County's total housing stock. Prince William County is also anticipating an accurate revenue forecast for FY2010 as current projections again indicate a small, revenue shortfall of $4.2 million and another variance of less than one percent (0.6%) compared to the adopted general revenue budget.

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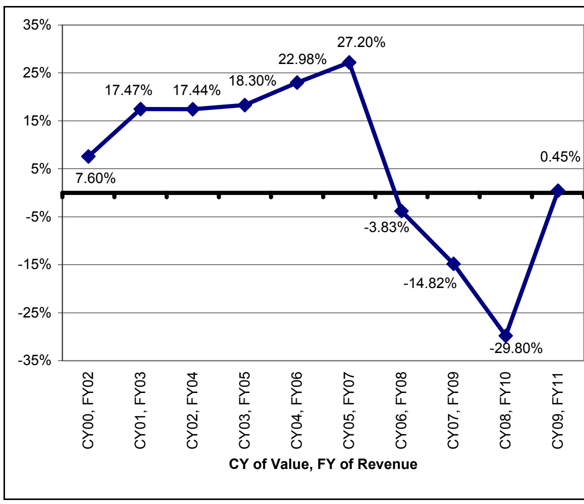
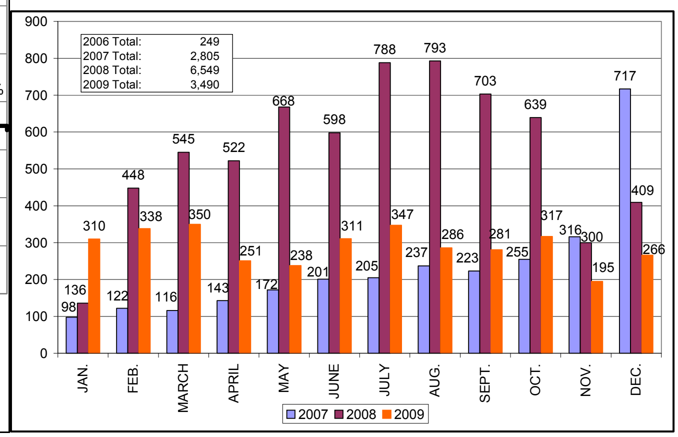
Background:

During the past seven years, Prince William County experienced its most volatile real estate market in history. After five consecutive years of double digit appreciation rates during 2001-2005 fueled by low mortgage rates and easily available credit, the County's real estate market collapsed in 2006-2008 as foreclosures flooded the market.

Annual Real Estate Market Value



Prince William County Foreclosures



Prince William County experienced over 13,000 foreclosures from 2006-2009. Subsequent sales of bank owned property caused the average residential home in the County to decline nearly 30% during calendar year 2008 alone as banks rushed to clear depreciating assets from their ledgers. In December 2008, an astonishing 88% of all residential sales in Prince William County were either bank sales or short sales. Prince William County's foreclosure rates approached levels experienced in states such as Florida, California, and Nevada.

The collapse of the County's real estate market and construction industry had a devastating impact on the local economy. It directly impacted the County's real estate tax revenue which is the largest source of County revenue and comprises 66% of total general revenue. It also had direct impacts on revenue sources such as recordation and deeds taxes, both of which plummeted along with the real estate market.

Other County revenue sources were indirectly impacted by the economic recession. Personal property tax revenue levied on vehicles and business equipment is the County's second largest revenue source, which accounts for 16% of total general revenue. The collapse of the credit markets initiated by subprime defaults had a devastating impact on new car sales during 2008 and 2009. Used car values for trucks and sport utility vehicles plummeted in the wake of $4.00/ gallon gas in 2008 in addition to incentives offered by new car dealerships frantically trying to move increasing inventories.

Although Prince William County was unable to stop these market forces from occurring, it did utilize an effective process to:

- identify these economic events as they occurred through constant monitoring;
- adapt to new developments such as foreclosure trends;
- gain a better understanding of market dynamics that impact the County by establishing new, collaborative partnerships.

Solution:

Prince William County utilized its existing revenue forecasting process to gain a better understanding of current economic dynamics through internal and external partnerships. It is important to note that the revenue forecasting process is not an annual event, but the culmination of ongoing monitoring activities by County staff in the Finance Department as well as other agencies.

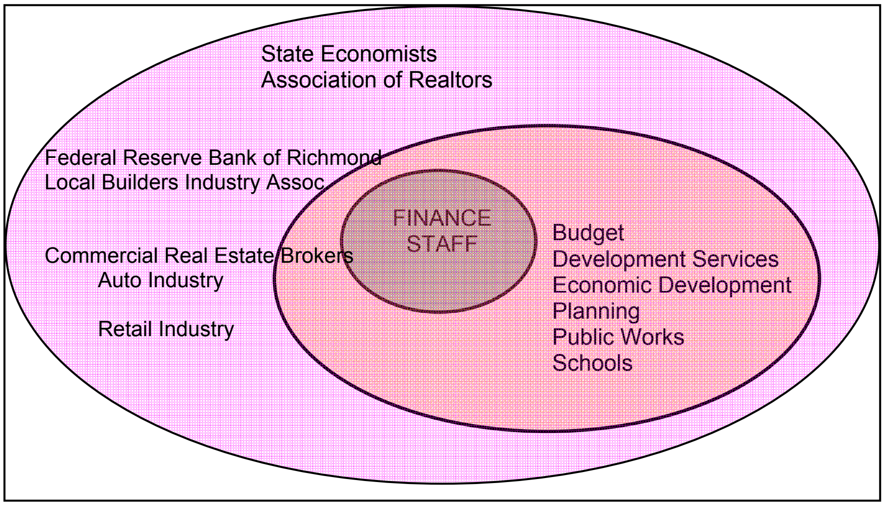
The County's five year revenue forecast process works within a framework of policies intended to ensure fiscal stability. Prince William County is required to develop a multi-year revenue projection in accordance with the County's Financial and Program Planning Ordinance included in the County code. A multi-year forecast ensures that new government programs are not initiated during the first or second year of the five year fiscal plan if they are not sustainable by the revenue forecast in the fourth or fifth year. In addition, the County's Principles of Sound Financial Management requires quarterly reporting of current year revenue which forms the basis of the following year's revenue forecast. This ongoing monitoring mechanism also provides an early warning system in the event revenues are not tracking with the adopted budget. The Principles of Sound Financial Management also requires a balanced five-year fiscal plan based on the multi-year revenue forecast developed by the County's Revenue Committee.

The Prince William County Revenue Committee is comprised of County staff from multiple agencies, not just the Finance Department, in addition to a representative from the County school system. Internal partnerships within the Revenue Committee include input from development agencies such as the Planning Office, Development Services, and Public Works. These development agencies are critical because they provide front line insight to development trends in the County such as rezonings to higher densities or permit activity by developers. Economic Development is another internal partner on the Revenue Committee that provides critical, detailed insight into what kind of commercial development is occurring in the County as well as data on vacancy and rental rates, thus impacting commercial real estate projections.

The Revenue Committee also reaches out to external partnerships to gain better insight into economic trends including the real estate market and automobile industry – the two largest sources of County revenue. The Prince William Association of Realtors in addition to the local Builders Industry Association provides invaluable information to the Revenue Committee on the status of the current real estate market in the County. They provide general market statistic metrics such as "average number of days on market" and "ratio of active listings to monthly sales (also known as months of inventory)." More importantly, the realtors and builders provide anecdotal evidence of the markets strengths or weaknesses that would otherwise be overlooked by merely looking at data from the County's Assessments Office. As a result, the Revenue Committee learned from the Builders Industry Association that banks are now requiring builders to provide upwards of 40-50% equity in their projects in order to secure a loan from a bank. As a consequence, builders are not initiating projects and this is reflected in the County's real estate drivers in the revenue forecast.

Another external partnership of the Revenue Committee is the insight provided by state economists from the Virginia Department of Taxation as well as representatives from the Federal Reserve Bank of Richmond. The Revenue Committee and these economists enjoy a symbiotic relationship where the economists discuss the state and federal economy by presenting topics such as unemployment rates and interest rate projections that impact the overall real estate market. The County, in turn, provides foreclosure data to the economists who are interested in high foreclosure areas such as Prince William County.

The automobile and retail industry is yet another external partnership of the County's Revenue Committee. Prince William County uses the National Automobile Dealers Association's (NADA) trade-in values as the basis of issuing personal property tax bills. Representatives from NADA have presented automobile market trends to the Revenue Committee and helped it understand where values were headed in the future based on sales volume, dealers' incentives, and interest rates. In the past, representatives from local automobile dealerships presented the local flavor of sales volume and future trends such as the advent of hybrid vehicles. Lastly, managers of local shopping centers and malls have collaborated with the Revenue Committee to provide retail sales trends including vacancy rates and sales volume of retail developments. This provides insight into the County's third leading general revenue source – sales tax revenue. The following chart summarizes the internal and external partnerships used by the Revenue Committee in developing the annual, five-year revenue forecast:



The information derived from the Revenue Committee's internal and external partnerships enabled it to develop a 'real estate market dashboard,' which is used to evaluate the County's real estate market. The following dashboard is essential to evaluating revenue drivers used to develop a multi-year revenue forecast from real estate tax revenue:

- Monthly Change in Average Monthly Sales Ratio
- Banks Sales Prices vs. Current January 1 Assessed Values
- Monthly Sales Volume
- Foreclosures
- Inventory of Foreclosed Homes
- Bank Sales
- Real Estate Market Metrics
  - Number of Days on Market
  - Active Listings to Sales Ratio

The aforementioned real estate dashboard is required because any of the components viewed in isolation can lead an analyst to the wrong conclusion of the overall real estate condition. For example, the County's current real estate market metrics are all trending in a positive way and could lead someone to conclude that the County's real estate market has rebounded and is a "seller's market" <u>if viewed by it alone</u>. However, other components in the dashboard, such as the inventory of foreclosed homes and monthly foreclosures, are trending in a negative direction although improving. The benefit of the dashboard is that it enables a comprehensive analysis of a complex market by considering all factors in totality.

Another important point is that the dashboard is constantly evolving in response to information gleaned from the Revenue Committee's internal and external partners. For example, Prince William County did not even track foreclosures five years ago. After foreclosures began to explode during the first half of calendar year 2006 (relative to prior years), the County's Assessments Office (an internal partner) notified the Director of Finance and the foreclosure rate was added to the dashboard. As bank sales dominated Prince William County's real estate market, other items were added to the real estate dashboard such as "bank sales prices vs. January 1 assessed values." Please refer to the attached series of slides presenting data on each item included in the real estate dashboard as well as the County's overall revenue forecasting process.

After meeting with external partners, the Revenue Committee develops a five-year revenue forecast based on tax policy direction provided by the elected Board of County Supervisors. The five-year revenue forecast and revenue driver assumptions for each general revenue source are published for reference and context as revenues are reviewed monthly during the new fiscal year. It also includes a review of the national, state, and local economy during the past year based on the collaboration with the Revenue Committee's internal and external partners. The latest "Prince William County Adopted Projections of General County Revenue for Fiscal Years 2011-2015" is also attached for reference.

The collaborative, evolving nature of Prince William County's revenue forecasting process has produced results during the most trying economic circumstances experienced in decades. During the past four fiscal years, the County has enjoyed accurate revenue forecasts, all with variance of less than one percent, as seen in the table below:

	Variance from Adopted Budget	Pct. Variance
FY2007	$2,320,141	0.33%
FY2008	($5,956,880)	-0.81%
FY2009	$4,809,929	0.62%
FY2010 (Projected)	($4,200,000)	-0.57%