

CITY OF SALEM, OREGON
BUILDING AND SAFETY FUND
FIVE-YEAR FINANCIAL FORECAST
FISCAL YEARS 2014-15 THROUGH 2018-19

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EXECUTIVE SUMMARY

The Building and Safety Fund continues to ensure public safety while providing predictable, efficient, and friendly service. Building and Safety provides plan review, permitting and inspection of residential and commercial construction, non-construction permits and regulatory licenses.

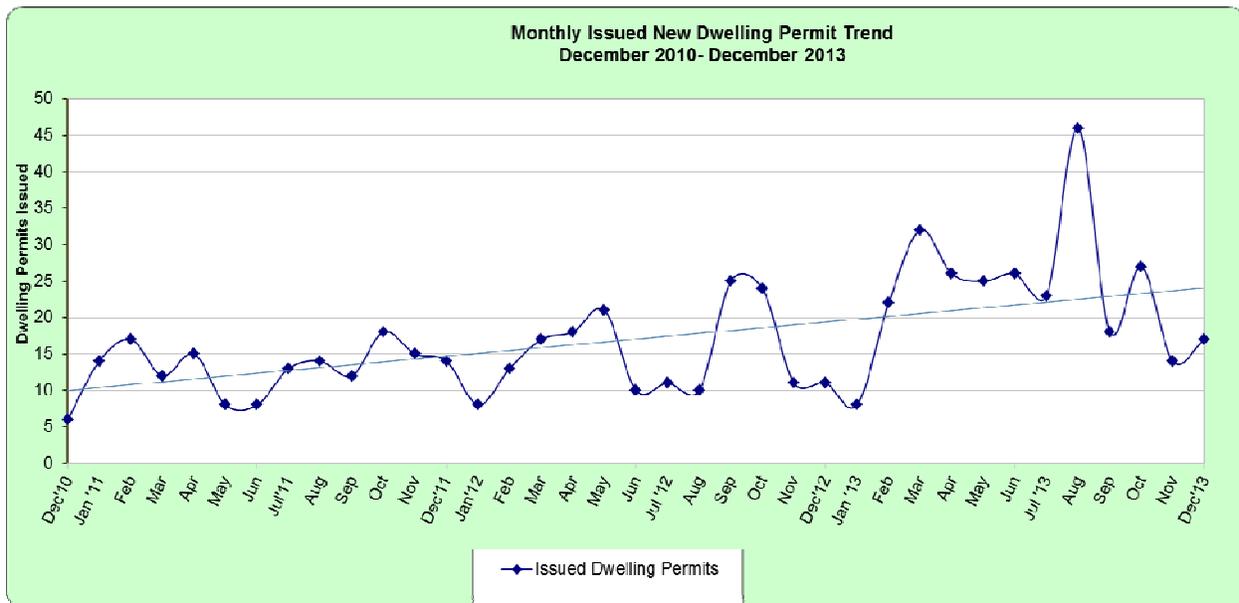
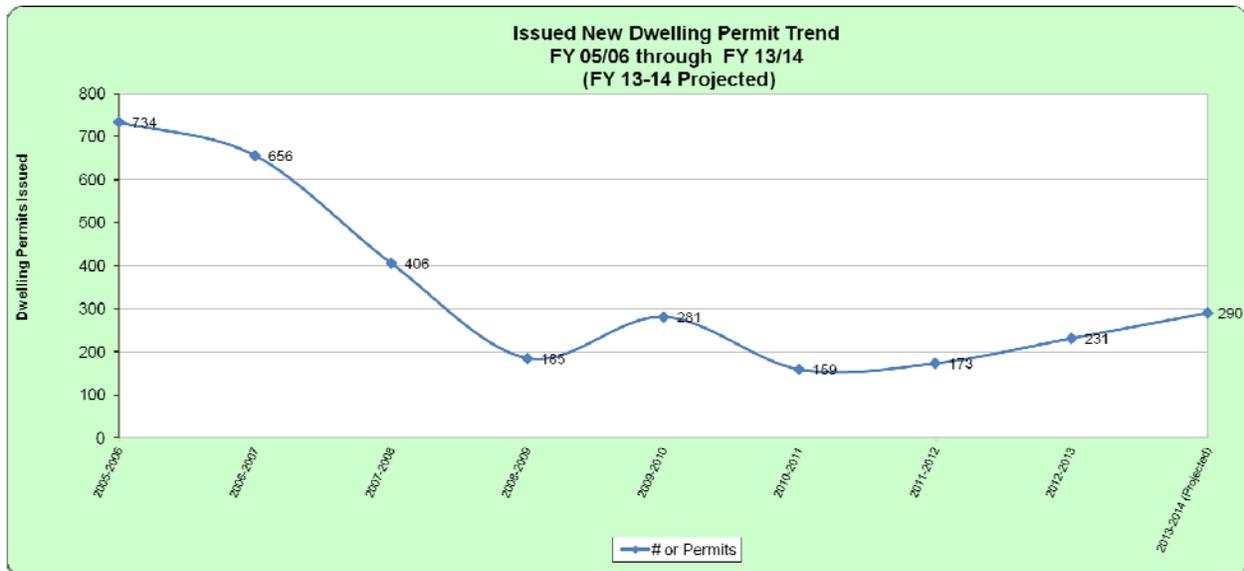
Since permitting activity reached a low point in FY 2010-11, it has shown a steady increase each year. FY 2013-14 projections of new dwelling permits issued show gains of 25.5 percent over FY 2012-13. Permitting revenues account for 94 percent of the total received in the Building and Safety Fund, the financial outlook is positive. Most economists are projecting slow but steady growth. Revenue and activity indicators within the Building and Safety Fund are consistent with this projection.

Highlights of the forecast include:

- An estimated 2 percent annual increase in revenues to account for increased permitting activity.
- Increased customer demand may require additional staffing to ensure the timely delivery of service.

ECONOMIC OUTLOOK

While permit activity has not recovered to pre-recession levels, the activity has begun to show a sustained “slow and steady” recovery as many economic indicators and state economists have predicted.



- Permitting activity for new dwelling permits decreased drastically leading up to the 2008 recession.
- After hitting a low point in FY 2008-09 (185 permits), there was an uptick in activity for FY 2009-10 (281 permits) driven by multiple incentives for first time home buyers.

- After the expiration of the incentives, FY 2010-11 permits declined below the FY 2008-09 levels (to 159 permits).
- FY 2011-12 permits increased 8.8 percent over FY 2010-11 (to 173 from 159).
- FY 2012-13 permits increased 33.5 percent over FY 2011-12 (to 231 from 173).
- FY 2013-14 permits total 145 through December with 290 projected for year-end, if this trend continues, for an additional 25.5 percent increase over FY 2012-13.

FORECAST RESULTS

The Building and Safety Fund forecast provides a view into the financial impact of typical operating decisions and service priorities in relation to projected business activity through FY 2018-19. This view is influenced by management decisions to increase staffing levels to accommodate the expected increase in workflow. Additionally, the forecast uses the same assumptions for expenditure activity over five years as the City's General Fund. Primary drivers of expense increases include wages, PERS, health care costs, energy costs, technology improvements, and inflationary increases. Tables for the expenditure assumptions are included in the appendix section of this report. It is important to note that the information provided in this forecast is not a prediction of what will occur, but a view of what could occur if all the forecast assumptions are realized.

The forecast presented this year is provided in two schedules. Schedule A carries forward current service levels while Schedule B recognizes the potential of continuing PERS savings in the out years of the projection. Each of the schedules provide for an additional position to more effectively meet customer demand. In both cases the fund is able to present a balanced budget over the forecast period with ending working capital exceeding the requirements of the fund created in City Council Policy C-10. Schedule A projects the working capital to grow to \$4.67 million over the forecast period. Schedule B projects the working capital to grow to \$5.17 million.

Values are in millions and have been rounded to the nearest ten thousand. The schedules build out the forecasted years using the projected FY 2013-14 as the base year. The base year uses currently available information on revenues received as of December 2013 to re-project revenue trends and adjust the base for known ongoing service level changes.

Schedule A-Building and Safety Fund Financial Forecast through FY 2018-19
(in millions)

RESOURCES	FY 13-14 Budget	FY 13-14 Projected	FY 14-15 Forecast	FY 15-16 Forecast	FY 16-17 Forecast	FY 17-18 Forecast	FY 18-19 Forecast
Beginning Working Capital	\$ 3.38	\$ 3.76	\$ 4.15	\$ 4.20	\$ 4.35	\$ 4.49	\$ 4.60
Current Year Revenue	<u>\$ 3.03</u>	<u>\$ 3.54</u>	<u>\$ 3.61</u>	<u>\$ 3.68</u>	<u>\$ 3.76</u>	<u>\$ 3.83</u>	<u>\$ 3.91</u>
TOTAL RESOURCES	<u>\$ 6.41</u>	<u>\$ 7.30</u>	<u>\$ 7.76</u>	<u>\$ 7.88</u>	<u>\$ 8.10</u>	<u>\$ 8.32</u>	<u>\$ 8.51</u>
EXPENDITURES							
Base Expenditures	\$ 3.51	\$ 3.15	\$ 3.93	\$ 3.83	\$ 3.91	\$ 4.02	\$ 4.07
Less:							
Unspent Contingency		\$ -	\$ (0.30)	\$ (0.30)	\$ (0.30)	\$ (0.30)	\$ (0.30)
Anticipated Expenditure Savings		\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Anticipated PERS Savings		\$ -	\$ (0.07)	\$ -	\$ -	\$ -	\$ -
Permanent Reductions Required			\$ -	\$ -	\$ -	\$ -	\$ -
Ongoing Prior Year Reductions				\$ -	\$ -	\$ -	\$ -
NET TOTAL EXPENDITURES	<u>\$ 3.51</u>	<u>\$ 3.15</u>	<u>\$ 3.57</u>	<u>\$ 3.53</u>	<u>\$ 3.61</u>	<u>\$ 3.72</u>	<u>\$ 3.77</u>
Estimated Ending Working Capital	<u>\$ 2.89</u>	<u>\$ 4.15</u>	<u>\$ 4.20</u>	<u>\$ 4.35</u>	<u>\$ 4.49</u>	<u>\$ 4.60</u>	<u>\$ 4.74</u>
Service Stabilization Reserve	1.61	1.61	1.82	1.77	1.81	1.86	1.89
Capital Asset Reserve	0.65	0.65	0.65	0.65	0.65	0.65	0.65
EWC in Excess of Reserve Funds	<u>\$ 0.64</u>	<u>\$ 1.90</u>	<u>\$ 1.73</u>	<u>\$ 1.93</u>	<u>\$ 2.03</u>	<u>\$ 2.09</u>	<u>\$ 2.20</u>

Excludes Reappropriations and Carryovers

Schedule B-Building and Safety Fund Budget Balancing Scenario with PERS Savings through FY 2018-19
(in millions)

RESOURCES	\$ 5.00 FY 13-14 Budget	\$ 7.00 FY 13-14 Projected	\$ 8.00 FY 14-15 Forecast	\$ 9.00 FY 15-16 Forecast	\$ 10.00 FY 16-17 Forecast	\$ 11.00 FY 17-18 Forecast	\$ 12.00 FY 18-19 Forecast
Beginning Working Capital	\$ 3.38	\$ 3.76	\$ 4.15	\$ 4.20	\$ 4.43	\$ 4.66	\$ 4.90
Current Year Revenue	<u>\$ 3.03</u>	<u>\$ 3.54</u>	<u>\$ 3.61</u>	<u>\$ 3.68</u>	<u>\$ 3.76</u>	<u>\$ 3.83</u>	<u>\$ 3.91</u>
TOTAL RESOURCES	<u>\$ 6.41</u>	<u>\$ 7.30</u>	<u>\$ 7.76</u>	<u>\$ 7.88</u>	<u>\$ 8.19</u>	<u>\$ 8.49</u>	<u>\$ 8.81</u>
EXPENDITURES							
Base Expenditures	\$ 3.51	\$ 3.15	\$ 3.93	\$ 3.83	\$ 3.91	\$ 4.02	\$ 4.07
Less:							
Unspent Contingency		\$ -	\$ (0.30)	\$ (0.30)	\$ (0.30)	\$ (0.30)	\$ (0.30)
Anticipated Expenditure Savings		\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Anticipated PERS Savings		\$ -	\$ (0.07)	\$ (0.08)	\$ (0.08)	\$ (0.13)	\$ (0.13)
Permanent Reductions Required			\$ -	\$ -	\$ -	\$ -	\$ -
Ongoing Prior Year Reductions				\$ -	\$ -	\$ -	\$ -
NET TOTAL EXPENDITURES	<u>\$ 3.51</u>	<u>\$ 3.15</u>	<u>\$ 3.57</u>	<u>\$ 3.45</u>	<u>\$ 3.53</u>	<u>\$ 3.59</u>	<u>\$ 3.64</u>
Estimated Ending Working Capital	<u>\$ 2.89</u>	<u>\$ 4.15</u>	<u>\$ 4.20</u>	<u>\$ 4.43</u>	<u>\$ 4.66</u>	<u>\$ 4.90</u>	<u>\$ 5.17</u>
Service Stabilization Reserve	1.61	1.61	1.82	1.77	1.81	1.86	1.89
Capital Asset Reserve	0.65	0.65	0.65	0.65	0.65	0.65	0.65
EWC in Excess of Reserve Funds	<u>\$ 0.64</u>	<u>\$ 1.90</u>	<u>\$ 1.73</u>	<u>\$ 2.01</u>	<u>\$ 2.20</u>	<u>\$ 2.39</u>	<u>\$ 2.63</u>

Excludes Reappropriations and Carryovers

REVENUE FORECAST

Building permit data shows activity has stabilized and moved into a period of slow growth. The good news is housing permit applications are on the rise and valuations are increasing for both residential and commercial projects. This is consistent with economist Tim Duy's prediction that slow, steady growth will continue. Based on this report and information from the National Homebuilders Association, a 2 percent increase in revenues has been applied each year.

Table1	Fiscal Year				
Revenue By Source	2014-15	2015-16	2016-17	2017-18	2018-19
Permits	\$ 3.40	\$ 3.46	\$ 3.53	\$ 3.60	\$ 3.68
Other	0.05	0.05	0.05	0.05	0.05
Intrafund-Budgeted Transfer	0.17	0.17	0.17	0.18	0.18
Total Current Revenue	3.61	3.68	3.76	3.83	3.91

EXPENDITURE FORECAST

The expenditure forecast is developed based on “most likely” increases in the cost of goods and services. When available, it uses known expenditure information such as, labor agreements, vendor contracts, PERS rate, health care cost increases, and inflation factors. The assumption tables for all expenditures are included in the appendix.

Table 2 summarizes the five-year expenditure forecast by expense category for Schedule B. Increased rates for PERS obligations for current employees prompt increases in personal services for both FY 2015-16 and FY 2017-18. The area of the table with italicized text demonstrates the effect on base expenditures of anticipated savings (including potential PERS savings) and unspent contingency in the “Total Net Expenditures” row.

Table 2-Schedule B Expenditures	Fiscal Year				
	2014-15	2015-16	2016-17	2017-18	2018-19
Expenditure Categories					
Personal Services	\$ 2.52	\$ 2.64	\$ 2.69	\$ 2.80	\$ 2.85
Materials & Services	1.11	0.90	0.93	0.92	0.92
Capital Outlay	-	-	-	-	-
Subtotal Operating Expenditures	3.63	3.53	3.61	3.72	3.77
Transfers	-	-	-	-	-
Contingency	0.30	0.30	0.30	0.30	0.30
Total Base Expenditures	3.93	3.83	3.91	4.02	4.07
Less:					
<i>Unspent Contingency</i>	(0.30)	(0.30)	(0.30)	(0.30)	(0.30)
<i>Anticipated Expenditure Savings</i>	-	-	-	-	-
<i>Anticipated PERS Savings</i>	(0.07)	(0.08)	(0.08)	(0.13)	(0.13)
<i>Permanent Reductions Required</i>	-	-	-	-	-
<i>Ongoing Prior Year Reductions</i>		-	-	-	-
Total Net Expenditures	3.57	3.45	3.53	3.59	3.64

FINANCIAL FORECAST RISKS AND RANKINGS

Risks to Revenue Forecast

The forecast acknowledges that there are risks associated with sustaining the resources needed to fund current and future services. Each identified risk is evaluated on the degree it will impact service delivery and assists in determining courses of action to be taken over the five-year period. The identified risk to the Building and Safety Fund's resources is summarized below:

Permit Revenue—Building permit revenue accounts for 94 percent of all revenue of the Building and Safety Fund. As such, changes in this revenue source can have a drastic effect on fund revenues overall. From the peak of new dwelling (SFD/Duplex) permits issued in FY 2005-06 of 734, annual activity decreased 78 percent to 159 permits issued in FY 2010-11. Activity appears to have stabilized and begun to show a modest increase year-over-year which is consistent with state economists' projections.

Risk Factor Ranking—HIGH

Because this revenue is derived from activity that is influenced primarily by outside sources (supply/demand, consumer confidence, credit availability, economic health) and represents such a large percentage of the total revenue for the fund, even slight swings in this revenue source can have drastic effects. Activity is measured on a monthly basis and economic trends are reviewed to help ensure the City can respond to changes accordingly.

Risks to Expenditure Forecast

This summary presents risks to the expenditure forecast by evaluating the degree by which service delivery may be impacted. This assessment assists in determining actions to be taken over the five-year period.

PERS Employer Rate Increases—A great deal of change has occurred in the investment market and through state legislation in the past year that may influence future PERS employer rates. The advisory PERS rates for the 2015-2017 rating period have declined from 2013 projections. This is due to the legislative reforms now in effect and the higher than expected investment returns on the PERS portfolio for 2013. While both of these factors are favorable for employers, the legislative reforms are not without challenges. In addition, Governor Kitzhaber has made it clear that with the passage of the 2013 reform bills further PERS legislative changes are now “off the table” for the remainder of his term.

Lawsuits have been filed on SB 822 and SB 861 and a decision by the Oregon Supreme Court may not be known until summer. The decision could possibly impact the current rate relief of 4.4 percent now in effect as well as rates going forward should these bills be ruled unconstitutional. Because of this uncertainty, the forecast assumes a 22 percent PERS rate increase in FY 2015-16 and FY 2017-18 for all three tiers based on the current year base rates, which do not include the 4.4 percent rate relief.

Below is a table of the rates by tier for comparison, rates are adjusted every two years to meet pension funding requirements. See Appendix for a complete table of PERS related expenses.

PERS Employer Contribution Rates					Projected Rate	
Table 3	FY 07-08	FY 09-10	FY 11-12	FY 13-14	FY 15-16	FY 17-18
Tier 1 and 2	8.65%	6.12%	12.93%	19.06%	23.25%	28.37%
OPSRP General Service	8.96%	4.37%	9.14%	14.68%	17.91%	21.85%
OPSRP Fire and Police	12.23%	7.08%	11.85%	17.41%	21.24%	25.91%

Risk Factor Ranking–HIGH

The lawsuit outcomes will have an immediate impact on employer rates. Should the legislation be declared unconstitutional, it is anticipated that the PERS Board will recover the needed contributions by increasing future rates. The forecast assumes a higher increase in rates than the PERS advisory rates for this reason

Health Care Costs–Health care rates are developed annually with the assistance of a consultant knowledgeable in the industry. The rate analysis is based on a review of national and statewide health care cost trends, legislated health care reforms, the required cash reserves to meet obligations year-over-year and the City’s claims activity from previous years. The rate of increase for health benefits premium costs is assumed to decline over the five-year period; see Appendix for the detailed assumption table. The Patient Protection and Affordable Care Act program for transitional reinsurance premium charged on employer plans is included in the calculated rates.

Risk Factor Ranking–MEDIUM

Health care costs could be higher or lower depending on a variety of factors, which are difficult to predict, including increased costs in the health care industry, the amount of filed claims, and future impacts associated with the Patient Protection and Affordable Care Act.

Labor Agreements–Approximately 78 percent of Building and Safety’s workforce is represented by AFSCME. Approximately 76 percent of Building and Safety’s service costs are personnel related, making labor agreements a significant cost driver. The wage increase associated with the most recent agreement is incorporated into the forecast. For the years beyond the term of these agreements an assumed 1 percent wage increase is used. A 2 percent increase is assumed in the first year of the forecast for non-represented employees with 1 percent used in the remaining four years. The increased rate is intended to project the impact of correcting potential inequities in pay relationships between supervisors and the represented staff they supervise, as well as align compensation for some non-represented classifications with the average salary for comparable jobs.

Risk Factor Ranking—MEDIUM

The AFSCME labor agreement has been ratified and will expire on June 30, 2015. The risks associated with increased costs from future labor negotiations beyond FY 2014-15 are difficult to measure at this time.

Inflation—The Bureau of Labor Statistics reported in August that the Consumer Price Index-All Urban Consumers (CPI-U) for the Portland-Salem, OR-WA area (not seasonally adjusted) increased 1.3 percent in the first half of 2013 for an annual change of 2.2 percent. The increase was influenced primarily by higher prices for shelter (1.8 percent) and food (1.7 percent). Energy prices declined 1.1 percent since the second half of 2012; natural gas (-4.2 percent), followed by electricity (-1.6 percent) and gasoline (-0.4 percent). For purposes of this forecast, 1.2 percent was used as the inflation factor on general goods and services.

Risk Factor Ranking—LOW

Inflation is expected to remain relatively low over the forecast period for the goods and services that the City purchases. Energy price fluctuations will be monitored but are not anticipated to be significant risks at this time.

Over the five-year forecast period risk factors with medium rankings will be monitored and action will be taken should they begin to move to a higher risk status. All high ranking risks are monitored closely and when possible, steps will be taken to lower the City's exposure.

Forecast Risk Revenue	Ranking	Percent Total Revenue
Permit Revenue	HIGH	94%

Forecast Risk Expenditures	Ranking	Percent Total Expense
PERS Employer Rate Increases	HIGH	8%
Health Care Costs	MEDIUM	9%
Labor Agreements/Salary Costs	MEDIUM	38%
Inflation	LOW	

APPENDIX

EXPENDITURE ASSUMPTION TABLE

	FY 14-15 % Increase	FY 15-16 % Increase	FY 16-17 % Increase	FY 17-18 % Increase	FY 18-19 % Increase
WAGE PROJECTIONS					
Market adjustment-AFSCME	1.50%	1.00%	1.00%	1.00%	1.00%
Market adjustment-Police (SPEU)	1.00%	1.00%	1.00%	1.00%	1.00%
Market adjustment-Fire (IAFF)	0.00%	1.50%	1.00%	1.00%	1.00%
Market adjustment-Non-represented	2.00%	1.00%	1.00%	1.00%	1.00%

ANNUAL PERCENTAGE CHANGE IN BENEFIT PROJECTIONS

Health-all other	10.00%	8.00%	5.00%	5.00%	5.00%
Dental	7.00%	5.80%	3.80%	3.00%	3.00%
Vision	16.00%	10.00%	5.00%	3.00%	3.00%
Worker's compensation	4.30%	5.00%	5.00%	5.00%	5.00%
Life insurance	8.70%	1.00%	1.00%	1.00%	1.00%
Disability insurance	28.00%	2.00%	2.00%	2.00%	2.00%
Retirement-Employer Tier 1 and 2	0.00%	22.00%	0.00%	22.00%	0.00%
Retirement-Employer-OPSRP General	0.00%	22.00%	0.00%	22.00%	0.00%
Retirement-Employer-OPSRP Police and Fire	0.00%	22.00%	0.00%	22.00%	0.00%

PERS RATE ON ELIGIBLE EARNINGS

Retirement-Employer Tier 1 and 2	19.06%	23.25%	23.25%	28.37%	28.37%
Retirement-Employer-OPSRP General	14.68%	17.91%	17.91%	21.85%	21.85%
Retirement-Employer-OPSRP Police and Fire	17.41%	21.24%	21.24%	25.91%	25.91%

MATERIALS AND SERVICES

Base	1.20%	1.20%	1.20%	1.20%	1.20%
Postage	4.00%	1.20%	1.20%	1.20%	1.20%
Natural gas	1.00%	1.00%	1.00%	1.00%	1.00%
Electricity	2.20%	2.00%	2.00%	2.00%	2.00%
Radio Communications	0.00%	0.00%	0.00%	0.00%	0.00%
Motor Pool (Fleet Services)	2.80%	1.20%	1.20%	1.20%	1.20%
Liability Insurance	0.00%	0.00%	0.00%	0.00%	0.00%