City of Salem, Oregon

Transportation

Five-Year Financial Forecast

Fiscal Years 2014-15 through 2018-19

Linda Norris, City Manager

Peter Fernandez, P.E., Public Works Director

Prepared By:

Administrative Services Department
Deborah Bond, Director
David Lacy, Management Analyst II

Public Works Department
Mark Becktel, Transportation Services Manager
Vickie Clarke, Budget Analyst

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EXECUTIVE SUMMARY

The Public Works Department's Transportation Services Division supports the operation and maintenance of the City's streets, traffic signals, streetlights, and sidewalks. The Transportation Services component of the Public Works Fund (Fund 155) provides the financial structure for the department to respond to City Council goals that address long term support of community needs for public safety, livability, environmental health, and economic development.

Despite the nation's slow and steady recovery from the recession, the fiscal capacity of Transportation Services to continue provision of its core responsibilities is compromised. The growing gap between available resources and anticipated expenditures is so significant that this forecast demonstrates the equivalent of $1 million in service reductions over the five-year period. The key message of this forecast is the ongoing imbalance between the current revenue sources supporting Transportation Services and the cost of providing those services. Immediate service reductions or an additional revenue source is needed to prevent working capital from being depleted by the second year of the forecast. In regard to our fiduciary responsibility to maintain core transportation services and ensure adequate beginning working capital, steps must be taken in 2014 to address the revenue for this fund.

FORECAST RESULTS

This five-year forecast is an analysis of the Transportation Services component of the City's Public Works Fund based upon current and reasonable economic assumptions. It provides a view of the financial impact of the City's services, priorities, and policies within the context of national, state, and local economic factors; emerging vehicle technologies; worldwide and regional petroleum supplies and prices; consumer behavior; and the growth in primary revenue sources, of which state highway fund revenues provide 60 percent of Transportation Services' total resources. The forecast includes a variety of assumptions for expenditure activity over five years. The primary drivers of expense increases include wages, PERS and health care costs, energy costs, and inflationary increases on contracted goods and services. The tables for the expenditure assumptions are included in the appendix.

The primary funding source for Transportation Services is the City's monthly allocation of state highway fund revenues, which include motor vehicle fuel taxes; heavy commercial vehicle weight/mile taxes; and title, licensing, and registration fees from the Department of Motor Vehicles (DMV). The statewide motor vehicle fuel tax is currently 30 cents per gallon of retail fuel sold. The City's allocation is based on a per capita distribution of the portion allocated to cities. Salem's current share of the city apportionment is 5.8 percent. As the fuel tax revenue is based on the amount of gallons sold, revenues are sensitive to economic factors such as the regional price and availability of fuel, incorporation of fuel-efficient vehicle technologies, and consumer behavior.

The Oregon Department of Transportation (ODOT) provides a four-year forecast of state highway fund revenues in June and December of each year. The City uses the ODOT forecast to calculate its anticipated allocation of state highway fund revenues. Based on historical performance, the City currently budgets its revenue and expenditures to 97 percent of ODOT's forecasted revenue amount for Salem, which we have found to be a more realistic prediction. The June 2013 ODOT revenue forecast reduces the rate of growth for current fiscal year revenues and from that reduced base estimates a 1.7 percent increase in state highway fund revenues for Salem in FY 2014-15. The state predicts one year of accelerated growth to 3.4 percent in FY 2015-16, then slows the growth rate to 1.4 percent over the final two years of its forecast. The City's five-year forecast continues the 1.4 percent increase in state highway fund revenues through FY 2018-19. The growth factors from the state's forecast demonstrate a re-evaluation and lowering of prior year estimates.

The forecast is presented in two schedules; the values are in millions and have been rounded to the nearest hundred thousand. Each schedule builds out the forecasted years using the Projected FY 2013-2014 column as the base year. The base year uses currently available revenue received to re-project revenue trends and adjusts the expenditure base for known on-going service level changes. For consistency, both schedules employ an expenditure savings rate of 3 percent. While this is slightly below the historical rate of savings for the fund, it aligns with the assumption that permanent reductions in expenditure budgets will have a corresponding impact on the capacity to save. This forecast also demonstrates the discontinuation of a General Fund revenue transfer to support street maintenance.

Current Service Level–Schedule A

Schedule A presents the challenges Transportation Services faces to maintain current service levels over the five-year forecast period. It is based on the service level represented by Transportation Services' FY 2013-14 budget projection.

Schedule A reflects the positive impact of $500,000 in offsetting revenue from the City's Construction Fund for sidewalk reconstruction and replacement during FY 2014-15 and FY 2015-16. This work was authorized by the City Council as projects identified to be built using savings from the 2008 Streets and Bridges General Obligation Bond. Despite this infusion from the bond, projected growth in service costs and continued slow to no growth in primary transportation revenue sources will deplete working capital to $0.7 million by the end of FY 2014-15. This is 44 percent of the targeted fund balance of two months of total state highway fund revenue ($1.6 million). This results in insufficient funding for a balanced budget by the second year of the forecast. Our goal is to maintain beginning working capital equivalent to two months of state highway fund revenues.

SCHEDULE A– FY 2014-15 Five-Year Transportation Services Financial Forecast

(Values in Millions)	**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**
RESOURCES							
Beginning Working Capital	$ 1.3	$ 1.8	$ 1.3	$ 0.7	$ 0.1	$ 0.0	$ 0. 0
Current Year Revenues	12.2	10.9	11.2	11.6	11.5	11.7	11.9
TOTAL RESOURCES	**13.4**	**12.7**	**12.5**	**12.3**	**11.5**	**11.7**	**11.9**
EXPENDITURES							
Base Expenditures	12.2	12.1	12.6	13.0	13.1	13.6	13.9
Less:							
Unspent Contingency		(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)
Anticipated Expense Savings		(0.4)	(0.3)	(0.4)	(0.4)	(0.4)	(0.4)
Anticipated PERS Savings		0.0	(0.1)	0.0	0.0	0.0	0.0
TOTAL NET EXPENDITURES	**12.2**	**11.3**	**11.8**	**12.3**	**12.4**	**12.9**	**13.1**
Estimated Ending Working Capital	**$ 1.3**	**$ 1.3**	**$ 0.7**	**$ 0.1**	**$ (0.9)**	**$ (1.1)**	**$ (1.3)**

Budget Balancing Scenario-Schedule B

A budget balancing solution requires approximately $800,000 in reductions to ongoing service levels in FY 2014-15 and potential additional reductions in years three through five of the forecast period. The outcome of the reductions in FY 2014-15 allows the fund to stabilize immediately and gain a little ground in FY 2015-16. However, the reduction of these core services will have a negative impact on the community's transportation system.

FY 2014-15 data in Schedule B reflects approximately $100,000 in savings derived from legislated PERS rate relief also recorded in Schedule A. The budget balancing scenario includes the impact of reduced PERS rate assumptions beginning in FY 2015-16, which are based upon recent PERS Board advisory information.

To achieve the level of savings needed in FY 2014-15, position eliminations and curtailed paving activities for local residential streets will be required. The budget balancing scenario focuses resources on state-mandated safety requirements for the operation of traffic signals and streetlights and maintenance and installation of signage plus limited levels of maintenance for arterial and collector streets. Permanent reductions over the five-year period equal $1 million. The necessary reductions and re-focusing of services will provide for an ending working capital of $1.6 million in FY 2018-19. This amount represents the desired reserve, which is equivalent to two months of total state highway fund revenues.

SCHEDULE B–Transportation Services Budget Balancing Scenario Through FY 2018-19

(Values in Millions)	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
RESOURCES							
Beginning Working Capital	$ 1.3	$ 1.8	$ 1.3	$ 1.5	$ 1.5	$ 1.6	$ 1.6
Current Year Revenues	12.2	10.9	11.2	11.6	11.5	11.7	11.9
TOTAL RESOURCES	**13.4**	**12.7**	**12.5**	**13.1**	**13.0**	**13.3**	**13.5**
EXPENDITURES							
Base Expenditures	12.2	12.1	12.6	13.0	13.1	13.6	13.9
Less:							
Unspent Contingency		(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)
Anticipated Expense Savings		(0.4)	(0.3)	(0.4)	(0.4)	(0.4)	(0.4)
Permanent Reductions			(0.8)	0.0	(0.2)	(0.1)	(0.1)
Ongoing Permanent Reductions			0.0	(0.6)	(0.6)	(0.8)	(0.9)
Anticipated PERS Savings			(0.1)	(0.1)	(0.1)	(0.2)	(0.2)
TOTAL NET EXPENDITURES	**12.2**	**11.3**	**11.0**	**11.6**	**11.4**	**11.7**	**11.9**
Estimated Ending Working Capital	**$ 1.3**	**$ 1.3**	**$ 1.5**	**$ 1.5**	**$ 1.6**	**$ 1.6**	**$ 1.6**

Note: Expenditure reductions demonstrated in Schedule B during FY 14-15 may occur over the two-year period including FY 15-16.

REVENUE FORECAST

The revenue forecast is developed using conservative growth expectations for Transportation Services' revenue sources. It uses current revenues and does not assume new or unrealized revenues in the forecasted amounts. Approximately 68 percent of Transportation Services' revenues (excluding beginning working capital) come from state highway fund revenue. Table 1 summarizes the five-year revenue forecast by revenue source. This table demonstrates only those revenues used to support Transportation Services. It does not include State highway fund revenues that are used to support Parks Operations' maintenance of the City's street trees and landscaping in the public rights of way.

Table 1 (in millions)	**Fiscal Year**				
Revenue By Source	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
State Highway Revenue (net funding for Parks)	$ 7.62	$ 7.88	$ 7.97	$ 8.06	$ 8.15
Intra City Billings and Transfers	2.85	3.00	2.74	2.89	2.97
Federal Grants	.36	.36	.36	.37	.37
All Other Sources	.35	.37	.38	.39	.40
Total Current Revenue	$11.18	$11.61	$11.45	$11.72	$11.89

EXPENDITURE FORECAST

The expenditure forecast is developed based on anticipated increases in the cost of labor, materials, and capital. When available, it uses known expenditure information such as labor agreements, vendor contracts, PERS rates, health care cost increases, and inflation factors. Future costs associated with higher PERS obligations for current employees are included. Table 2 summarizes the five-year expenditure forecast by expense category for Schedule B. The assumption tables for all expenditures are included in the appendix.

Table 2– Schedule B Expenditures	**Fiscal Year**				
Expenditure Categories	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Personal Services	$5.3	$5.6	$5.7	$6.0	$6.1
Materials and Services	6.1	6.3	6.5	6.7	6.8
Capital Outlay	0.0	0.0	0.0	0.0	0.0
Subtotal Operating Expenditures	**11.4**	**11.9**	**12.2**	**12.7**	**12.9**
Contingency	0.4	0.4	0.4	0.4	0.4
Transfer	0.8	0.8	0.6	0.6	0.6
Total Base Expenditures	**12.6**	**13.0**	**13.1**	**13.6**	**13.9**
Less:					
Unspent Contingency	*(0.4)*	*(0.4)*	*(0.4)*	*(0.4)*	*(0.4)*
Anticipated Savings	*(0.3)*	*(0.4)*	*(0.4)*	*(0.4)*	*(0.4)*
Permanent Reductions	*(0.8)*	*0.0*	*(0.2)*	*(0.1)*	*(0.1)*
Ongoing Permanent Reductions		*(0.6)*	*(0.6)*	*(0.8)*	*(0.9)*
Anticipated PERS Savings	*(0.1)*	*(0.1)*	*(0.1)*	*(0.2)*	*(0.2)*
Total Net Expenditures	***$11.0***	***$11.6***	***$11.4***	***$11.7***	***$11.9***

FINANCIAL FORECAST RISKS AND RANKINGS

Risks to Revenue Forecast

The forecast acknowledges that without additional revenue, Transportation Services will be unable to sustain the current level of services, now and into the future. Each identified risk is evaluated on the degree it will impact service delivery. These evaluations of existing and potential resources assist in determining actions to be taken over the five-year period to ensure a balanced budget. The most significant risk to Transportation Services' resources is summarized below.

State Highway Fund Revenue–Transportation Services' primary revenue source is the City's allocation of state highway fund revenues– a revenue source over which the City has little or no control. Revenues are impacted by worldwide, national, and regional factors including the availability of fuels, prices, transport costs, refinery capacity, vehicle technology, and consumer behavior. The amount and allocation of motor vehicle fuel taxes and DMV fees is determined by the state legislature. Actual receipts have not kept pace with original ODOT forecasts published after adoption of the Oregon Jobs and Transportation Act in 2009, which raised the motor fuel tax by five cents beginning in January 2011. ODOT has reduced its forecasted growth percentages for the state highway fund four times since June 2010. The June 2013 ODOT forecast reduced December 2012 projections by 1.8 percent for the current fiscal year. The ongoing risk to the City is any loss between forecasted revenues and actual receipts.

> Risk Factor Ranking–HIGH
> State highway fund revenue can be subject to changes in legislation, technology, petroleum supplies, prices, and consumer behavior. Because it is the primary revenue source for transportation, potential changes need to be monitored and, in the case of legislative challenges, defended.

Risks to Expenditure Forecast

This summary presents risks to the expenditure forecast by evaluating the degree by which each identified risk will impact service delivery. 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 percentage points 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 percentage point 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 A 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– The City's 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 A 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 Transportation Services' workforce is represented by the AFSCME labor union. Approximately 43 percent of Transportation Services expenses are personnel related making labor agreements a significant cost driver. The wage increase associated with the most recent AFSCME agreement is incorporated in the forecast. For the years beyond the term of the agreement 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 agreement 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
State Highway Fund	HIGH	68.2%

Forecast Risk–Expenditures	Ranking	Percent Total Expense
PERS Employer Rate Increases	HIGH	4.1%
Health Care Costs	MEDIUM	6.5%
Labor Agreements/Salary Costs	MEDIUM	21.5%
Inflation	LOW	

EXPENDITURE ASSUMPTION TABLE

WAGE PROJECTIONS	FY 14-15 % Increase	FY 15-16 % Increase	FY 16-17 % Increase	FY 17-18 % Increase	FY 18-19 % Increase
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%