Office of Management & Finance

December 2010 Five-Year Forecast

for the City of Portland General Fund

This document presents the City of Portland's Five-Year Financial Forecast. Table 1 below summarizes discretionary General Fund resources and expense requirements through FY 2015-16. As shown in Table 1, the City is projected to have the resources necessary to maintain expenses at the current service level in FY 2011-12. However, it should be noted that, as shown at the bottom of Table 1, we project deficits in the out-years of the forecast if one-time spending remains at the current level each year.

TABLE 1. Discretionary General Fund Five-Year Forecast ($millions)

	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16
Discretionary Resources	*$382.9*	*$397.6*	*$420.4*	*$446.3*	*$468.8*	*$488.0*
Budget Requirements	*$381.1*	*$376.0*	*$392.6*	*$411.0*	*$429.0*	*$446.8*
Accumulated Surplus/(Deficit)	***$1.9***	***$21.7***	***$27.8***	***$35.3***	***$39.8***	***$41.2***
Continued Unfunded Ongoing	$0.0	$10.5	$10.9	$11.3	$11.8	$12.4
Accumulated Surplus/(Deficit)	***$1.9***	***$11.2***	***$6.7***	***$3.3***	***-$3.8***	***-$14.4***

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Figure 1 illustrates the cumulative impact of continuing the existing level of one-time expenses throughout the five-year forecast horizon. The second bar in each fiscal year shows the surpluses/(deficits) with the assumption that approximately $10.5 million in one-time expenses are continued, including inflation, each year of the five-year forecast. As illustrated, cuts would be necessary beginning in year four.

FIGURE 1. Discretionary General Fund Forecast Cumulative Ending Surplus/(Deficit) Scenarios

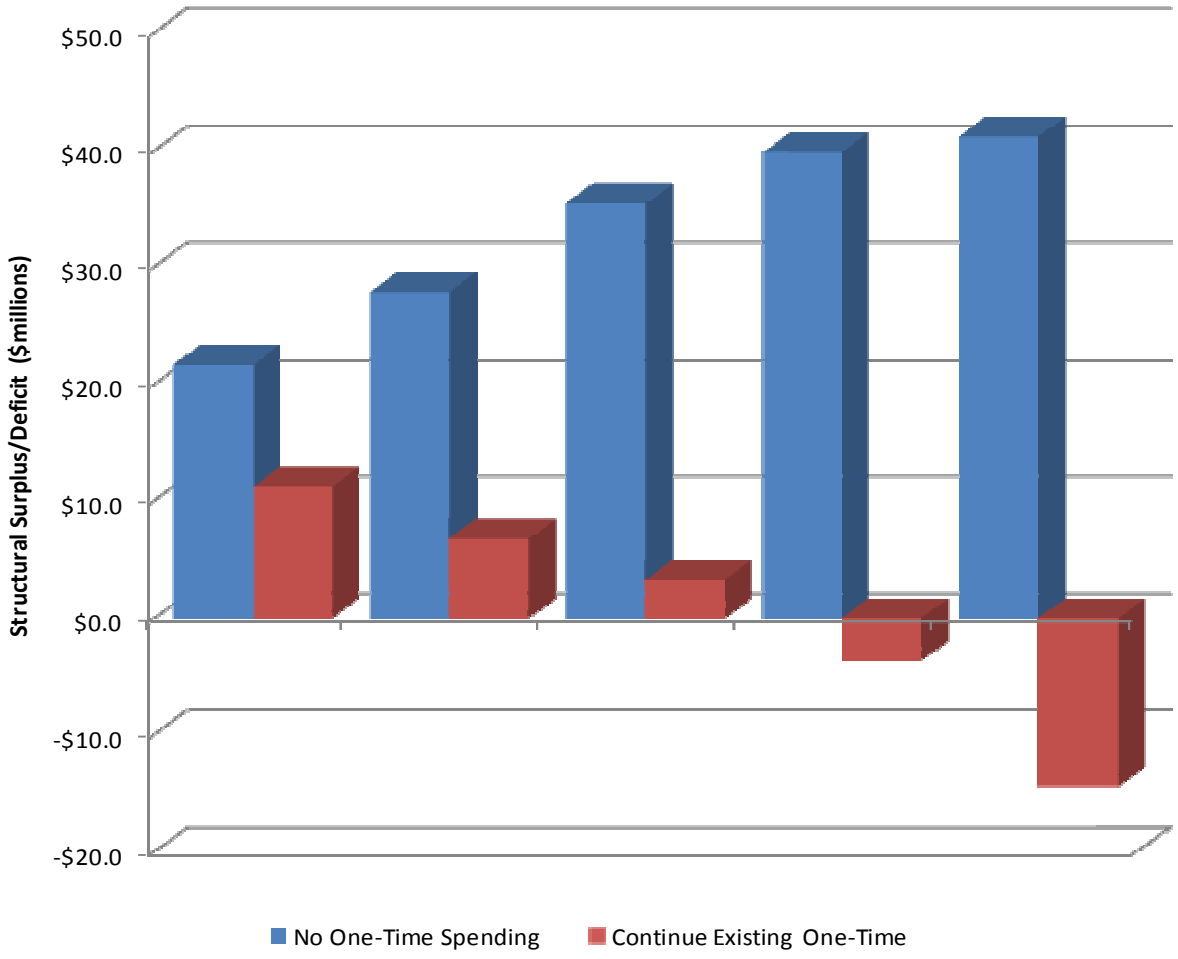


Table 2 shows the five-year resource and expenditure forecast along with a proposed allocation of resources in each year of the forecast. Though resources exist to make a larger portion of spending ongoing for the five-year forecast, this is only a result of one-time revenues that are being spread over five years. The City is realizing a $16.8 million accrual adjustment, as well as $3.9 million carried forward by Council from the FY 2009-10 ending balance. In order to avoid cuts in year six, these one-time resources are appropriately reflected as one-time spending.

TABLE 2. Discretionary General Fund Five-Year Forecast with New Spending ($millions)

	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16
Discretionary Resources	*$382.9*	*$397.6*	*$405.9*	*$424.0*	*$439.7*	*$452.5*
Expenses						
Bureaus & Programs	$341.6	$355.2	$370.0	$385.0	$402.4	$420.5
Capital Set-Aside	$2.4	$0.0	$0.0	$0.0	$0.0	$0.0
Planned One-Time	$17.4	$0.2	$0.2	$0.2	$0.2	$0.2
New One-Time	*$0.0*	*$13.5*	*$6.5*	*$5.4*	*$5.0*	*$4.0*
Council Set-Asides	$19.7	$20.5	$23.9	$27.4	$28.0	$27.8
Additional On-Going Spending	*$0.0*	*$1.5*	*$0.0*	*$0.0*	*$0.0*	*$0.0*
Budget Requirements	*$381.1*	*$391.0*	*$400.6*	*$418.0*	*$435.6*	*$452.5*
Required for Five-Year Balancing	$1.9	$6.7	$5.2	$6.0	$4.1	$0.0
Surplus/(Deficit)	***$0.0***	***$0.0***	***$0.0***	***$0.0***	***$0.0***	***$0.0***

DISCRETIONARY GENERAL FUND RESOURCES

Roughly 90% of discretionary General Fund revenue (excluding beginning fund balance) comes from three sources: property taxes, business licenses, and utility licenses/franchise fees. Most of the remainder comes from transient lodging taxes and state shared revenues, which are comprised of the City's share of state-collected liquor and cigarette revenues. Interest income, transfers, and various small miscellaneous sources round out the City's discretionary General Fund revenue sources. Table 3 summarizes the forecasts for each of these General Fund revenue sources over the five-year forecast horizon.

The forecast assumes a prolonged slow economic recovery. Additionally, the property tax forecast was lowered by $1 million each year beginning in FY 2011-12 due to the county withholding funds pending the outcome of a large property tax appeal. Business License revenue growth is expected to be healthy in FY 2010-11 in particular, due to large corporate profits in the near-term. This assumption, coupled with the fact that business license revenue also ended FY 2009-10 approximately $4 million higher than expected, resulted in a $6 million increase in business license revenue over the previous forecast. Meanwhile, slow consumer spending will limit lodging tax revenue over the life of the forecast. Finally, because the growth in Utility License/Franchise Fee revenue in FY 2009-10 was largely due to two large, one-time audit recoveries, the forecast for this revenue source is somewhat restrained.

TABLE 3. Discretionary General Fund Resource Five-Year Forecast ($millions)

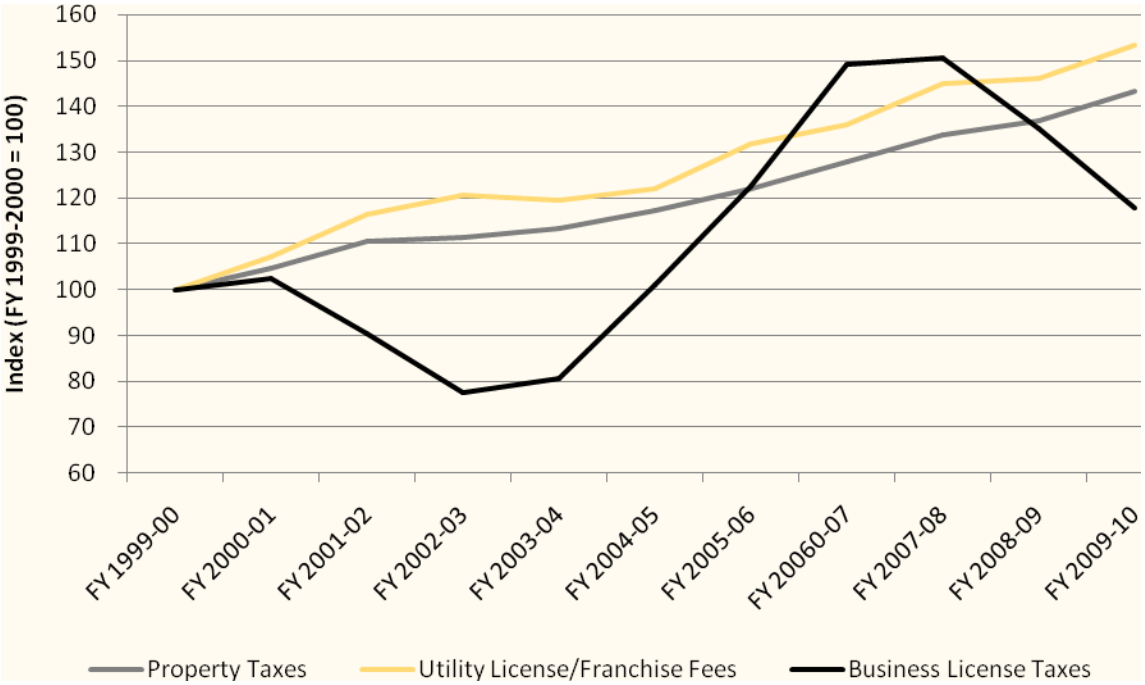
	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16
Beginning Balance	$21.3	$30.1	$18.4	$17.2	$18.6	$17.2
Revenues						
Property Taxes	$193.4	$199.1	$205.3	$211.7	$218.2	$224.9
Transient Lodging	$13.8	$14.7	$15.4	$16.0	$16.6	$17.2
Business Licenses	$63.1	$66.5	$75.0	$83.3	$86.6	$90.5
Utility License/Franchise	$68.4	$70.5	$74.4	$77.6	$81.0	$83.8
State Revenues	$12.1	$12.3	$12.5	$12.7	$12.8	$12.9
Interest Income	$1.3	$1.1	$1.4	$1.9	$2.3	$2.3
Transfers	$6.8	$0.6	$0.6	$0.6	$0.6	$0.6
Miscellaneous	$2.6	$2.7	$2.8	$2.9	$3.0	$3.1
Discretionary Resources	*$382.9*	*$397.6*	*$405.9*	*$424.0*	*$439.7*	*$452.5*

Due to voter-approved changes to property tax laws in the 1990s (i.e., Measures 5 and 50), property taxes have become a slow-growing, stable revenue source. Regardless of the economy, property taxes to the City have grown by between 0.7% and 5.8% annually since 1998. It should be noted that should the housing downturn continue for several more years, it could create significant downward pressure on these revenues due to compression.

With two seemingly random exceptions, utility license and franchise fee (ULF) revenue has grown in all but two years – 1975 and 2004 – since 1970. These revenues are generally stable because they are at least in part demographic (i.e., as the City adds households, it also adds demand for energy, cable TV, etc.). Also, demand for the services that drive these revenues are somewhat shielded from economic conditions. For example, demand for home heating is a much greater function of winter weather conditions than of changes in the economy.

In contrast to property taxes and ULF revenue, business license revenue is the City's largest revenue source that is directly tied to broad economic conditions. Thus, the City sees large increases in receipts during expansions and sharp declines in economic slowdowns and recessions. These fluctuations in business license revenue are the largest driver of budget variability over the short term and, therefore, provide the greatest near-term risk to this forecast. Figure 2 below illustrates the relative volatility of business license revenue compared to property taxes and ULF revenue. The figure shows how each source has grown since FY 1999-00.

FIGURE 2. Revenue Volatility from Largest General Fund Sources



Revenue Risks

It should be noted that this forecast represents a conservative expectation of revenue flows. However, significant risks remain related to the City's General Fund revenue source. Many of these risks are summarized below.

- *Economic Conditions/"Double-Dip" Recession* – While the forecast is built on the expectation of slow economic growth, it does not assume that the U.S. will see what is referred to as a "double-dip" recession. Should the economy deteriorate rapidly, especially in the near-term, the City could realize lower revenue, particularly in business licenses.

- *Audit Recoveries* – The forecast assumes no audit recoveries in Utility License/Franchise Fee revenue because these revenues are viewed as particularly unstable and one-time in nature. To the extent that the City recovers revenue through this avenue, revenues will exceed the forecast.

- *Property Tax Issues* – There are two distinct risks related to the City's property tax revenue, with both related to tax compression. Though too complex to go into great detail here, the two risks relate to real market real estate values and additional voter-approved levies. Should real estate prices continue to decline significantly, or voters approve addition permanent property tax levies – such as a library levy that was made possible in the November 2010 election – the City could see lower-than-expected property tax revenue.

- *General Government Budget Issues* – Large budget deficits at the state and local level could result in lower revenues (or increased costs) to the city. The City currently receives a little over $12 million in state-shared revenue related to cigarette and liquor sales.

DISCRETIONARY GENERAL FUND EXPENSES

The forecast for General Fund expenses is driven largely by a variety of inflation factors, as well as policy decisions. The forecast assumes a 1.0% cost-of-living adjustment (COLA) for personal services for FY 2011-12. This is based on the local CPI-W put out by the Bureau of Labor Statistics (BLS). It is an estimate based on the annualized rate seen for the first half of the current calendar year. The actual cost associated with the COLA will be determined in February when the BLS publishes actual figures for 2010. Additionally, the forecast incorporates various other minor adjustments, such as those related to lower expectations for costs associated with the City's pension obligation bonds. Finally, because the City balances its budget over the entire five-year forecast, it is expected that some resources in some years will be required to go unspent in order to balance in future years. The summary of these factors is displayed in Table 4.

TABLE 4. Discretionary General Fund Expense Five-Year Forecast ($millions)

	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16
Expenses						
Bureaus & Programs	$341.6	$355.2	$370.0	$385.0	$402.4	$420.5
Capital Set-Aside	$2.4	$0.0	$0.0	$0.0	$0.0	$0.0
Planned One-Time	$17.4	$0.2	$0.2	$0.2	$0.2	$0.2
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Council Set-Asides	$19.7	$20.5	$23.9	$27.4	$28.0	$27.8
Additional On-Going Spending	*$0.0*	*$1.5*	*$0.0*	*$0.0*	*$0.0*	*$0.0*
Budget Requirements	*$381.1*	*$391.0*	*$400.6*	*$418.0*	*$435.6*	*$452.5*
Required for Five-Year Balancing	$1.9	$6.7	$5.2	$6.0	$4.1	$0.0

Expense Risks

The following summarizes significant risks to the current forecast as they relate to expenses. To the extent that the expectations for any of these factors differ from what is realized, the forecast is at risk.

- *Continue One-time Expenses* – As discussed earlier, there are not enough resources to continue funding all of the currently one-time funded programs throughout the five-year forecast. Should these expenses be expanded, there could be a greater need for cuts in the event of a revenue downturn.

- *Inflation* – Inflation has been muted recently and the expectation is that there simply is not enough demand in the system to see dramatic increases in the near-term. Because a large majority of the forecast is based on inflation expectations, the exposure to the forecast from deviations in inflation could significantly move in either direction.

- *Benefit Costs* – Large increases in health care benefits and PERS costs are incorporated in the forecast; however the actual costs could be higher or lower depending on a variety of difficult-to-forecast measures (e.g., financial market activity).

- *Unsettled/Future Labor Contracts* – Because the vast majority of City costs are related to personnel and most of those costs are driven by labor agreements, there is significant risk associated with increase cost from future labor negotiations.

- *Public Safety Requirements* – Costs related to Police and Fire account for well over half of discretionary General Fund spending. Demands for these services could drive City expenses higher.