City of Sacramento
City Council
915 I Street, Sacramento, CA, 95814
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Meeting Date: **5/22/2012** **Report Type:** Staff/Discussion

Title: FY2012/13 Budget Restructuring and Fleet Equipment Financing Pilot

Report ID: 2012-00445

Location: Citywide

Recommendation: Pass a Motion authorizing the City Manager and the City Treasurer or their respective designees to implement a Fleet Equipment Financing Pilot Program beginning in Fiscal Year 2012/13, and make adjustments to the Parks Planning and Development Services staffing, and implement associated budgetary changes to be reflected in the FY2012/13 approved operating budget.

Contact: Mark Prestwich, Special Projects Manager, (916) 808-5380, Office of the City Manager; Reina Schwartz, Director of General Services, (916) 808-7195, General Services; Max Fernandez, Director of Community Development Department, (916) 808-7940

Presenter: Reina Schwartz, Director of General Services, (916) 808-7195; Max Fernandez, Director of Community Development Department, (916) 808-7940; Leyne Milstein, Director of Finance Department, (916) 808-8491.

Department: General Services Dept / City Managers Office
Division: Fleet Management Admin
Dept ID: 13001311

Attachments:

1-Description/Analysis
2-Attachment 1-Operating Cost Per Gallon
3-Attachment 2-Proposed General Plan
4-Attachment 3-Appropriation Changes

City Attorney Review
Approved as to Form
Lan Wang
5/16/2012 3:12:41 PM

City Treasurer Review
Reviewed for Impact on Cash and Debt
Russell Fehr
5/7/2012 10:28:58 AM

Approvals/Acknowledgements

Department Director or Designee: Reina Schwartz - 5/15/2012 4:53:25 PM

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Description/Analysis

Issue: Ongoing efforts to identify efficiencies and cost-savings have resulted in two additional opportunities for City Council consideration that are currently not included in the FY2012/13 Proposed Budget.

First, the Department of General Services, Fleet Management Division (Fleet Division) and their customer departments have an ongoing need to budget for regularly scheduled equipment replacements. The City's fleet is comprised of 2,371 vehicles with a current estimated replacement value of $150 million. The FY2012/13 Proposed Budget includes a $3.6 million General Fund appropriation to replace 115 vehicles. Based on a review of financing options, staff recommends implementing a five-year pilot program that would move away from the outright cash purchase method of procuring vehicles and equipment to a debt financing approach such as leasing or lease purchasing. This proposal does not include a change in practice for Public Works and non-General Fund operations.

The pilot program would use a blended approach of debt financing and cash purchases. The expected savings in FY2012/13 are $3.1 million. These funds can be used to offset the cost of the Department of Parks and Recreation (DPR) budget rightsizing proposal below ($800,000) as well as provide resources necessary to backfill the difference in the value of savings associated with any successful employee labor group agreements versus the department-specific reductions included in the Proposed Budget.

The second recommendation relates to DPR's capital improvement project (CIP) design, delivery and administration costs. Over the last four years, DPR's project delivery function has become increasingly dependent upon developer impact fees and reimbursements from project funds to design, construct and improve parks. An analysis completed by Management Partners has demonstrated that the cost burden of the currently budgeted overhead rate for the Park Planning and Development Services (PPDS) division of DPR is out of line with the cost recovery of other City departments (300% versus 180%). In addition, budget to actual results at FY2010/11 have revealed that this artificially high overhead rate is not achievable and, as such, required a backfill with General Funds to close the budget.

The proposed reduction in indirect overhead rates resulting from the staffing changes in the PPDS proposal will increase funding available for CIP brick and mortar parks projects. While PPDS will return approximately $180,000 in reimbursable staff expenses to the General Fund in FY2012/13 resulting in a more reasonable overhead rate of recovery, this action effectively reduces budgeted General Fund reimbursable staff costs by approximately $800,000 in order to right-size the overhead rate and improve the sustainability of this function.

Policy Considerations: The Fleet financing proposal will allow the City to pay the capital costs of vehicles as they are used rather than upfront, freeing up resources over the next several budget years. It is estimated that this change will result in General Fund savings of $3 million in FY2012/13 and cumulative General Fund savings of $4-4.5 million for the five-year financing pilot. It is important to note that the annual financing cost for the FY2012/13 vehicle purchases is estimated at $1 million. However, due to the timing of the financing, only half of this cost will be incurred during the FY2012/13 fiscal year.

While the interest charges incurred will increase the cost of acquiring vehicles though a loan or lease purchase, those additional costs are typically mitigated by lower overall life cycle costs for vehicles as they are replaced at the end of their established life cycle. Interest costs are usually more than offset by higher vehicle residual values and lower vehicle operating and maintenance costs resulting from an effective fleet replacement program. A review of the City's historical maintenance and repair costs presented in Attachment 1 shows that costs rise dramatically as the equipment exceeds its useful life.

The proposed PPDS action will result in additional CIP funds for actual project costs by reducing staffing by 4.0 full-time equivalent (FTE) positions to support a lower and more reasonable and achievable indirect overhead rate charged to the parks projects. The services affected by the reductions (labor compliance, contracting, inspection, and administrative and fiscal services) will be absorbed within the Department, insourced to other departments, or outsourced.

Environmental Considerations:

California Environmental Quality Act (CEQA): The proposed action does not have the potential for causing a significant adverse effect on the environment and is therefore exempt under CEQA Guidelines, Section 15061(b)(3).

Sustainability: Renewing the City's fleet more regularly will allow the City to accelerate the achievement of sustainability goals related to the fleet including reduced greenhouse gas emissions, increased fuel efficiency and reduced dependence on foreign oil.

Commission/Committee Action: Not applicable

Rationale for Recommendation: The City currently pays for the majority of fleet equipment acquisitions through the outright cash purchase wherein the full purchase price of each asset is paid up front, at the time of its acquisition. Utilizing a hybrid debt financing/cash purchase approach will allow the City to pay the capital costs of vehicles as they are used rather than before they are used. In transitioning to a debt capital financing approach, it is estimated that the city will free up $3 million in General Funds in the FY2012/13 operating budget and up to $4-4.5 million in General Funds over the five-year financing pilot. Annually staff will review the overall impact of the pilot program to determine the benefits to the budget and may include modifications based on actual financing costs in future years.

The PPDS proposal will reduce the City's indirect overhead rates to achievable levels consistent with other City departments and increase the amount of funding available for DPR CIP projects.

Financial Considerations: The FY2012/13 Proposed Budget includes a $3.6 million General Fund appropriation to replace 115 vehicles that have reached the end of their useful lives. In order to address General Fund constraints, 22 non-emergency vehicles, with estimated replacement costs of $0.7 million, were deferred by increasing vehicle replacement criteria by 20% and not included in the Proposed Budget. The pilot financing will provide sufficient funding to include the replacement of these 22 vehicles on schedule.

At the request of Fleet Division and Budget Office staff, City Treasurer's Office (CTO) staff calculated estimated costs over the initial five-year financing pilot. CTO staff utilized the total General Fund vehicle replacement need in each year from FY2012/13-FY2016/17 and completed different sensitivity analysis models based on varying interest rate levels to calculate estimated debt service obligations in each year of the five-year pilot. Although it would be difficult to predict with certainty the level of short-term interest rates associated with lease financings that will be entered into in future years, Attachment 2 is provided as a conservative overview of potential financing costs based on a “high” cost of borrowing (5%) relative to low short-term interest rate levels as of April 2012. As a note, City lease financings in the late 1990s and early 2000s had interest rates around 7% as opposed to lease financings in early 2012 which achieved interest rates around 3%.

Based on the estimated financing costs and savings attributable to reduced operations and maintenance costs and higher residual values on vehicles, there is the potential for General Fund savings to be realized during the course of the proposed five-year pilot.

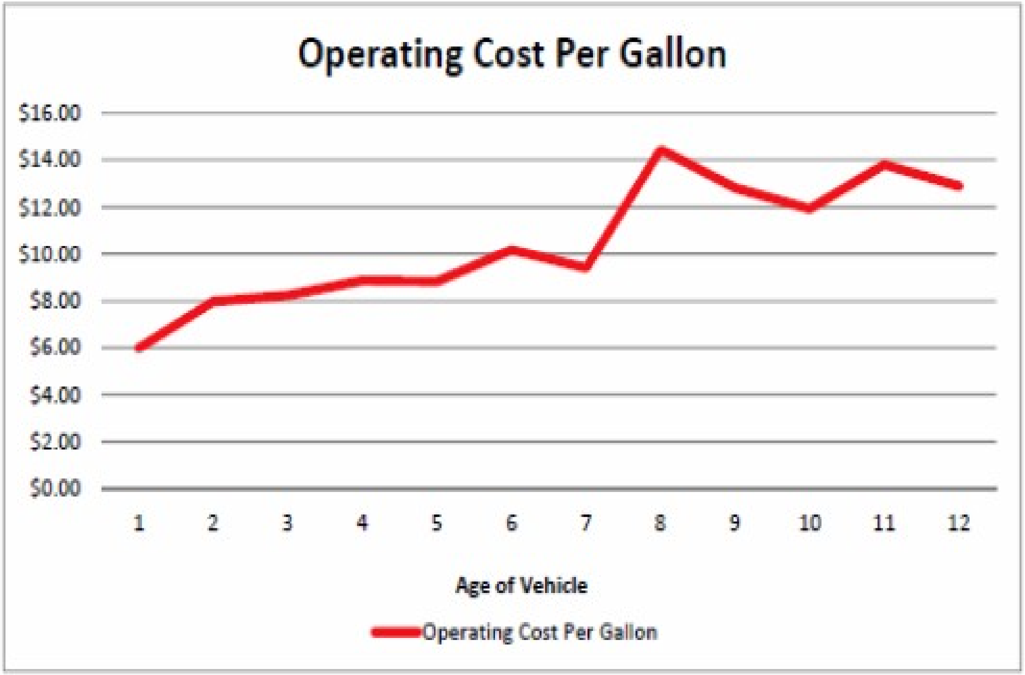
If the five-year pilot is approved by Council, there will be a need for a programmatic review after three years of the realized savings attributable to reduced operations and maintenance costs and higher residual values as well as the need to evaluate short-term interest rates at that point in time to determine the feasibility of continuing to lease finance City Fleet vehicles or revert to a debt or cash-based approach.

The proposed right-sizing of PPDS includes a reduction in staffing of 4.0 full-time equivalent (FTE) positions to support a lower indirect overhead rate charged to the parks projects. The services affected by the reductions (labor compliance, contracting, inspection, and administrative and fiscal services) will be absorbed within the Department as well as insourced from other departments or outsourced as necessary. Including the reduction of positions within the division, the rightsizing of PPDS will cost the General Fund $800,000.

A summary of the adjustments necessary to implement the recommendations included in this report is included as Attachment 3 and will be incorporated into the final Budget Resolution. It is important to note that two of the positions proposed to be eliminated in the PPDS right-sizing have also been included as part of DPR’s budget reductions and will not be added back should the City reach agreement with the affected employee groups.

Emerging Small Business Development (ESBD): No goods or services are being purchased as a result of this report.

Attachment 1



Operating Cost Per Gallon (City of Sacramento)

Age of Vehicle	Vehicle Count	Operating Cost Per Unit	Operating Cost Per Gallon	Percent CPG Change from Previous Age
1	58	$ 13,301.09	$6.00	-
2	135	$ 19,816.33	$7.98	33%
3	269	$ 8,136.20	$8.23	3%
4	154	$ 11,034.41	$8.87	8%
5	150	$ 9,155.83	$8.82	-1%
6	189	$ 12,400.82	$10.18	15%
7	165	$ 8,501.02	$9.40	-8%
8	164	$ 18,091.59	$14.45	54%
9	110	$ 13,786.26	$12.81	-11%
10	127	$ 6,484.37	$11.93	-7%
11	31	$ 17,725.69	$13.80	16%
12	41	$ 6,280.56	$12.89	-7%

These calculations include only units that were active and in-service for 12 months during 2011

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Proposed General Fund City Fleet Replacement Financing

Projection of Debt Service Obligations - *with Pay-Go*

ATTACHMENT 2
As of 5.14.12

Agency ID	Department	Fiscal Year 2013	Fiscal Year 2014 [2]	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	FY13-17 Total
11000	Police	304,894	1,475,943	990,081	1,480,321	1,709,413	5,960,653
12000	Fire	40,614	81,227	133,835	223,750	274,172	753,598
13000	DGS	12,023	146,703	28,098	40,266	69,567	296,657
17000	CC&L	-	-	1,023	7,458	12,869	21,350
19000	Parks	98,613	220,346	274,848	447,400	575,910	1,617,117
21000	Comm Dev	-	23,120	20,539	46,428	74,309	164,396
	TOTAL Cash Needed	**456,144**	**1,947,339**	**1,448,425**	**2,245,623**	**2,716,241**	**8,813,771**

Assumptions:

1) Assumed financing rate is **5.00%**.
2) The **5.000%** interest rate is the applied financing rate for each of the lease financings between FY13 - FY17 **except FY14 (Pay-Go)**.
3) Each lease financing will encompass a single tranche financing for that given fiscal year.
4) Term of each lease = 5 years
5) None of the leases are optionally redeemed prior to the respective final maturities.
6) Estimated lease financing needs for each fiscal year is based on DGS - Fleet 10-year replacement data as of 3/5/12 (revised on 5/11/12).
7) Public Works (Agency ID 15000) will fund their own vehicle replacements as opposed to lease finance their vehicles.

SOURCES:
Fleet leasing figures = DGS, Fleet Division
Modeling = Office of the City Treasurer

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Attachment 3

Appropriation Changes

- Reduce funding for General Fund fleet replacement by $3.6 million
- Increase debt service by $500,000 to reflect implementation of a pilot debt-financing program
- Decrease PPDS reimbursement budget by up to $800,000
- Designate $2.3 million to backfill General Fund department reductions should the City be successful in reaching agreement with employee groups

Staffing Changes

- Eliminate 4.0 FTE in PPDS
    - 1.0 Administrative Officer (SCXEA)
    - 1.0 Administrative Analyst (SCXEA)
    - 1.0 Senior Accountant Auditor (SCXEA)
    - 1.0 Construction Inspector III (Local 39)