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MEMORANDUM

Exhibit A

**TO:** Mayor Ted Wheeler  
Commissioner Chloe Eudaly  
Commissioner Nick Fish  
Commissioner Amanda Fritz  
Commissioner Dan Saltzman  
City Auditor Mary Hull-Caballero

**FROM:** Ken Rust, Chief Financial Officer *KLR*

**DATE:** September 6, 2017

**COPIES:** Tom Rinehart, Chief Administrative Officer  
Andrew Scott, City Budget Office Director

**SUBJECT:** Build Portland

Last week the City Council convened a work session to discuss the City's ongoing infrastructure needs and a program proposal (Build Portland) that could be implemented to help address those needs. At the work session, information was shared that documented the need for additional investment in the City's infrastructure, and how those funding needs have increased over time. The issue of infrastructure funding is not a new one. In fact, it is one that has been consistently recognized by OMF and bureau financial managers for more than twenty years both in the form of annual operating and capital budgets and reports prepared and presented to City Council, and more recently in presentations on long-term fiscal health that have accompanied the City's Comprehensive Annual Financial Report that City Council accepts each year. The City's chronic underfunding of infrastructure is the result of a combination of factors including inadequate dedicated resources, competing City and Council priorities for limited financial resources, and bureau decisions that in many cases have favored programs and/or new projects at the expense of capital repair and replacement.

The City needs to make a long-term commitment to providing additional resources to funding its infrastructure backlog if it does not want to see further deterioration in the capacity of that infrastructure to serve businesses and residents of the City. Recent actions by City Council to dedicate a portion of excess one-time funds to infrastructure funding, along with recent voter approval of a gas tax increase, a Parks General Obligation (G.O.) bond measure and an Affordable Housing G.O. bond measure are important and significant steps in the right direction. However, these efforts by themselves are insufficient to fully address the infrastructure funding needs facing the City.

The Build Portland proposal, which looks to capture expected future property tax revenues that the City's General Fund will receive as existing urban renewal districts expire ("boomerang revenues"), could be a meaningful contributor to infrastructure funding. However, there are a number of questions and

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concerns, many of which were not identified or discussed at the work session, that need to be considered and addressed so that the proposal produces the intended result: improved stewardship of the City's capital assets and stronger long-term fiscal health and resiliency.

## FINANCIAL POLICY IMPACTS

The City has developed a broad range of financial management policies to guide financial decision-making and to help ensure predictable financial operating results over time. These Comprehensive Financial Management Policies are integral to the City's financial management and form a foundational cornerstone of the City's credit ratings. Proposals like Build Portland need to fit within these policies or else those policies, if appropriate, need to be amended or modified. The current Build Portland proposal has the potential of violating two of the City's financial management policies: FIN 2.04, and the City's Debt Management Policy.

**FIN 2.04-Budget.** One provision of this policy with respect to General Discretionary Revenues, which includes property taxes, reads as follows: "Unless otherwise stated explicitly by the Council, the City shall not dedicate discretionary revenues for specific purposes in the General Fund. This shall preserve the ability of the Council to determine the best use of available revenues to meet changing service requirements."

Historically, the City has been very reluctant to dedicate or "earmark" discretionary General Fund revenues. This preserves flexibility to deal with future unforeseen events and keeps from binding future Council's to decisions made by their predecessors. To implement a proposal like Build Portland, the City Council will need to take an affirmative, explicit action and should do so with a full understanding of the impacts and precedent that such an action entails.

**Debt Management Policy.** The Build Portland proposal intersects this policy in two areas:

1. **Rapidity of Debt Repayment.** This provision states that City borrowings should strive to repay at least 40% of the principal amount of the borrowing within 10 years. The initial financing of the Build Portland proposal, because it envisions a bond sale well before significant boomerang revenues are received, defers principal payment for six years and results in only 23 percent of principal being repaid within 10 years. This deferred principal structure also results in higher interest costs totaling about \$4.8 million more than a conventional level debt structure that would satisfy this debt policy requirement. Because Build Portland obligations will be backed by the General Fund, and the capacity to fund this and other obligations is limited, rapidity of debt repayment is a significant concern as it helps to ensure sufficient capacity to fund City capital projects in a prudent and timely manner.
2. **Debt Authorization for Capital Projects.** This provision states that no City debt will be issued unless it is a capital project included in the City's adopted CIP. Based on earlier discussions, some of the projects being considered for Build Portland funding include street maintenance and pavement overlays. However, depending on the exact nature of these projects they may not meet accounting definitions as a capital improvement and therefore could not be debt financed.

## LEGACY LIABILITIES



At the work session, most of the discussion on infrastructure needs involved the Parks Bureau and PBOT. While the needs of these two bureaus are significant, there are other infrastructure liabilities that are facing the City that notably were not discussed: Portland Harbor and Columbia River Levees. These two items represent "legacy liabilities" associated with past practices, activities, and systems that have not been part of the City's traditional capital planning processes. Collectively, these two items could result in capital liabilities to the City of \$150-200 million or more. Ultimately, these costs will be spread to several City bureaus including PBOT and General Fund bureaus. It would be prudent to include these legacy liabilities, some of which will come with a legal obligation to perform, in any discussion about future capital funding.

## OTHER INFRASTRUCTURE LIABILITIES

In addition to the need to fund Legacy Liabilities, there are other City bureaus facing infrastructure and facilities funding needs including the City's public safety agencies (Police, Fire, BOEC, and POEM), OMF, and the Portland Housing Bureau. The Build Portland proposal is currently silent on these needs and they should be included in any comprehensive plan that intends to address the City's capital funding needs.

## RISKS

The Build Portland proposal is based on current projections of boomerang revenues and assumes that the current property tax system and plans for existing urban renewal districts do not change. These assumptions are critical to the amount and timing of future property tax revenues and introduce inherent risks to a program that is solely dependent on those future revenues to repay program indebtedness. A summary of the risks that will be need to be addressed and managed if the program is implemented are summarized below.

- **Changes to Oregon's property tax system** that affect permanent rate levies, basis of taxation (Real Market Value vs. Assessed Value), compression, etc.
- **Changes to ORS 457 (urban renewal)** relating to sharing of tax increment revenues, determination of consolidated billing rate, and other diversions of tax increment revenues currently being considered to address statewide funding shortfalls (i.e., PERS)
- **Increases in urban renewal district maximum indebtedness** that delay the return of assessed value to overlapping taxing districts, including the City.
- **Reducing the boundaries** of existing urban renewal areas prior to expiration of those districts.
- **Slower than forecast assessed value growth** that delays the repayment/defeasance of outstanding and proposed debt.
- **Higher than forecast interest rates on future long term urban renewal bonds** that result in delay the repayment/defeasance of debt expected to be issued in coming years.
- **Timing of sale of Post Office property**, the proceeds of which will be used to repay the \$36 million General Fund-backed line of credit used to fund River District projects.

Because of the risks described above, the City should limit any Build Portland borrowings to amounts that are fully payable from boomerang revenues that have, in fact, been returned to the General Fund and not based on future expected revenues that have not yet been realized.

### **ORGANIZATIONAL CAPACITY**

Currently, City bureaus are engaged in the planning, implementation, and management of capital construction projects to an extent and scale never experienced in the City's history. By all accounts, this high level of project implementation will continue for the foreseeable future and could well accelerate with recent decisions by the Water Bureau to build a water treatment facility and plans by BES to double its annual CIP outlays. This has stressed existing organizational capacity to deliver projects to its limits and beyond.

The Build Portland proposal assumes an early financing totaling \$50 million for additional capital projects, yet it is unclear whether there is capacity in benefitting bureaus to manage additional workload much less in central service organizations like Procurement which play an integral role in project delivery. These very real constraints need to be carefully considered to avoid over promising and under delivering, and could well result in changing the timing and funding of projects to a more realistic and manageable level.

### **FUNDING SUBSTITUTION**

A key goal of Build Portland is to address the City's infrastructure backlog by creating an ongoing, dedicated source of funding to assist with that effort. This is critical to making headway on that backlog and must be viewed as "additive" to financial resources the City and bureaus are already contributing to that effort. To ensure that this is the case there needs to be clear policy and measurement of that effort, and bureaus cannot be allowed to substitute Build Portland funds for monies that they already and would otherwise contribute to infrastructure. This is a very real concern, has happened in the past, and, if not explicitly addressed upfront, will result in a missed opportunity to make meaningful improvements to capital funding.

### **LEVERAGING INVESTMENTS WITH OTHER GOVERNMENTS**

It was touched on very briefly at the work session but is important to note that other governments (school districts and Multnomah County), will be experiencing boomerang revenues as well. Although boomerang revenues received by school districts may only serve to offset state funding, amounts received by Multnomah County, which will largely mirror the amounts expected to be received by the City, will be available to be spent as additional discretionary funds. Consequently, it may be possible for the City and the County to work together in a way that leverages these boomerang revenues in a manner that helps to further increase benefits to citizens.

**SUMMARY**

The expiration of the City's existing urban renewal districts over the next twenty years provides a once-in-a-generation opportunity to utilize boomerang revenues to address funding issues like infrastructure that historically have suffered from chronic underfunding. However, capital funding needs are but one of many financial challenges that will be facing the City in the future. Consequently, it is critical that the City retain flexibility and capacity to deal with unforeseen events as it looks at ways to bolster infrastructure funding.

There are questions, policy concerns, and risks that need further consideration and analysis before that plan is finalized, approved and implemented and the Council Resolution to proceed with developing the proposal into a plan should direct that they be included in that effort. By so doing, the City has the best chance to ensure that Build Portland delivers on its promise; improved stewardship of the City's capital assets and stronger long-term fiscal health and resiliency.