CITY OF ASHLAND

Council Communication

AFN Debt Service Alternatives for the City

Meeting Date:	May 2, 2006	Primary Staff Contact:	Lee Tuneberg
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Approval:	Gino Grimaldi	E-mail:	
		Estimated Time:	45 Minutes

Statement:

This communication provides Council with information on potential resources for paying the City's debt obligations relating to Ashland Fiber Network.

Background:

The City has $15.5 million outstanding in full faith and credit revenue bonds for the construction and operation of the fiber network to date. A "full faith and credit" obligation makes it an obligation of the City, not just the utility, and gives maximum flexibility on the revenue streams used to pay the debt. In this case, we look first to AFN revenues but can utilize any other legal sources necessary.

The approximate distribution of this debt is $9.0 million in capital costs and $6.5 million in operating losses. Debt service on these bonds is interest only in the first few years with the first principal payment occurring in July 2007. FY 2006-07 semiannual payments will total $866,000, then $1,056,000 and $1,299,000 in the following two years. Annual payments will level off at about $1.43 million in FY 2009-10.

Recently, AFN has been able to generate enough revenue to cover operational expenses but not meet debt service requirements. Depreciation and capital refresh costs are also largely under-funded. To this point, internal borrowing or subsidies have provided the additional funds needed to meet AFN shortfalls. Without significant changes in revenue streams and/or costs for AFN it is unlikely that rate increases for existing services can make up the shortfall.

In early FY 2005-06, Council approved and then repealed a $7.50 per account per month surcharge that would have generated approximately $900,000 per year to meet short-term debt service needs of AFN. A surcharge would need to grow to $12.00 per account per month to pay annual debt service when it levels off, and possibly more if other expenses are to be subsidized or if some accounts are exempted from paying a part of the surcharge.

The surcharge was repealed in that it presented problems in fairness of application and collection. Council asked for alternatives to the surcharge and this report provides some other ways the City could meet this obligation. Many of these alternate ways have been discussed before and may include conflicts with other City goals or programs that are being discussed. The December 6, 2005, Council Communication provided some of the requested information and applicable data has been summarized here.

Below is a list of other ways to meet the fiscal requirements besides using the surcharge on electric accounts:

a. Annually transfer operational subsidies from other funds, in turn, minimizing fund balances and resulting in other increases such as utility charges.

b. Divert part, or all, of the existing BPA surcharge from the Electric Fund to the Telecommunications Fund or the Food & Beverage tax from Parks and Wastewater funds. The BPA Surcharge revenue source currently represents approximately $1.1 million in FY 2006 projections to end of year. The FY 2006-07 Proposed Budget includes the surcharge being eliminated in favor of a 10% electric rate increase with a net affect on the customer of a 2% increase. This change still includes many of the same issues as the proposed AFN surcharge.

c. Changing the allocation of the Food & Beverage Tax revenue has been suggested. Approximately $1.5 million will be generated in FY 2006 for paying the debt on the wastewater treatment plant and $375,000 for open space. Diverting this tax will greatly impact the Open Space program and/or sewer rates. Sewer rates could increase 50% if the tax revenue was totally eliminated. Wastewater SDC charges could be adjusted to somewhat minimize the impact to the utility bill.

d. Severely reduce or eliminate the $450,000 to $500,000 Internal Service Fund charge to the Telecommunications Fund freeing monies to go toward debt service. The internal service costs are shared among end user funds, allocated based upon a set of criteria that attempts to fairly prorate internal expenses. AFN is a smaller fund and pays less than all the other utilities. An "incremental" approach to internal charges (attempting to only recover the additional costs attributable to the newest service) could be the basis for justifying a much smaller charge to AFN, resulting in a reduced amount of costs to be covered by rates. All things being equal, this would result in other funds paying more for internal services or a potential shortfall in the Central Service Fund and possible cutbacks in services city-wide.

e. Cutting specific programs or projects from other departmental budgets to transfer funds to AFN. The amount to be generated through savings is limited by the cuts employed. The fiscal impact varies depending on what is cut and could only be determined by the managing department. For example:

- In the other funds, identify open positions to be eliminated generating a subsidy transfer to AFN.
- Identify AFN as an economic tool and award grant monies from the Transient Occupancy Tax (TOT) revenue to the Telecommunications Fund. Of the estimated $1.5 million revenue in the FY 2006-07 Proposed Budget, a minimum of $215,456 must be spent on tourism and the rest (approximately $290,000) has been allocated per resolution 2004-32. The remaining two thirds of the revenue (about $1,000,000) is general tax revenue to the General Fund. Any variation would require a change in resolution(s) and will either deprive other economic or cultural groups of grant money or impact the balancing of the General Fund Budget if the other 2/3 portion of the TOT revenue is directed to AFN.

f. Limiting overall expenses in other departments and funds to generate an internal subsidy via operational transfer. An example is limiting Material & Services Budget growth to 2% rather than 3% and shifting the difference to fund transfers which could generate up to $297,000 but will have the same impact as transferring fund balances from "healthy funds" and may still result in added rate and fee increases in other funds.

g. Cap revenue growth (resources) in other funds and provide the increased revenue amount (related to increased activities rather than rate increases) as a subsidy to AFN. Like other subsidies or transfers, this will eventually result in a reduction in other services, lower fund balances or possible increases in other rates or fees to balance other funds. The assumption here is that other funds can provide needed services at acceptable levels with less revenue or less operational expenses.

h. Selling idle properties that are considered surplus and using the money for AFN debt service. This is limited by the value of the properties the City is willing to sell. Each sale is a one-time infusion of cash. In 2004 Council reviewed an inventory of unused land and some of them could be sold with the proceeds being used to pay off bonds or reserved for debt service. This removes the "positive" impact sales revenue would have on another recipient fund.

i. Property taxes increase. Currently, the City leaves nearly $0.57 (over $960,000 in revenue) in taxing authority un-levied each year. Property taxes could be used to pay part of the debt service on the full faith and credit bonds or

to fund AFN operations. Doing so will remove or reduce the "reserve" of monies between the existing tax levies and the maximum authority. The amount to be paid by taxes as opposed to fees or a surcharge may require a policy on how the money is to be generated based upon how the annual debt service amount is to be split.

One perspective is to establish a surcharge at a small amount (average of $2 - $4 per utility bill with commercial utility accounts paying more) and the remainder coming from property tax and other fees to meet total debt service. Another way is to equate property tax to the portion of the debt service relating to the construction cost of the asset or to the operating losses included in the debt.

Example: Use property taxes to pay for past AFN operating losses. The estimated operating loss portion of AFN's debt service is 42% ($6.5 million/$15.5 million). Forty-two percent of the "level" annual debt service ($1.43 million * 42%) is $600,600 and that would require an additional levy of $.355/$1000. This would leave $.215/$1000 or approximately $363,000 in tax revenue for other purposes or un-levied. In FY 2006-07, 42% of the $866,000 debt service is $364,000 and that also equates to about $.215/$1000 of assessed value as an increase in the tax rate reducing the $.57/$1000 of assessed value available to $.355 unused. The amount of other revenue needed from fees and charges would be 58% or $502,000. That equates to a $4.20 surcharge per utility bill per month. A comparison is attached with these perspectives and a comparison of the debt impact of the options considered by the committee.

j. Employ other revenue streams to meet requirements. These alternatives will require considerable work, public input and possibly participation through a vote. Potential new revenues include:

- Gas tax - Other agencies are implementing this tax because visitors help pay.
- Sales Tax - Ashland has this on prepared food but a new one could be broader based.
- Income Tax - Being considered throughout the state for various purposes.
- Entertainment Tax - A ticket tax has been considered many times but not implemented in Ashland.

The net result for most of the items above is a direct or indirect subsidy to AFN. New revenues that are paid by visitors may be more palatable to citizens but there is no intuitive correlation between a new gas or sales tax to a fiber optic network and related services like there is between the TOT or F&B taxes and tourism, Parks and Wastewater Treatment.

There are other, more lengthy steps that could be taken to reduce the impact of AFN's debt on the City. Foundations to raise contributions, intergovernmental agreements to share costs, outsourcing or expanding operations, etc. may be possible in the long run but cannot be developed as part of the annual budget process or without direction from Council.

An attachment of alternative revenue sources is attached.

In summary, there is little chance that a change in AFN operations will completely resolve debt service requirements. The alternatives provided should be evaluated in a context recognizing that all or a significant part of the debt service will need to paid for by other sources than those generated through AFN operations.

If AFN operations can pay for everything but debt service, then the amount needed in FY 2006-07 is the $866,000. However, cash must be available July 15, 2006, to pay the interest amount of approximately $433,000. By June 30, 2006, Council may need to transfer funds to assure adequate balances to make the cash payment early the next month.

A comparison of the original options is attached to show how a combination of revenue sources could be (would need to be) employed depending on the chosen path.

Related City Policies:

None

Council Options:
Direct staff on the action desired based upon Council discussion.

Staff Recommendation:
Council identify which revenue streams staff should work on to ensure the debt service payments are made.

Potential Motions:
Council moves to direct staff to incorporate _____ alternate revenue streams in the FY 2006-07 budget to pay the AFN debt service.

Attachments:
AFN Debt Service Alternatives
AFN Dept Payment Options – Impact to Pay Debt & AFN Options Scenarios

AFN Debt Service Alternatives
May 2, 2006

	Item	Potential	Comment
a	Ad hoc Operating Transfers	To be determined	Amount will fluctuate and is unreliable year to year
b	Divert other revenue streams	$1,100,000	BPA Surcharge revenue is currently 10% of Electric rate revenue
		$1,800,000	Food & Beverage Tax: 1% = $360,000
c	Reduce Internal Charges to AFN	$500,000	Requires other funds to pay more or reduce services/staff
d	Eliminate programs in other funds	To be determined	Parks activities, band, grants, etc. May negatively impact other services being provided
e	Limit expenses	$297,000	1% of City's total Materials & Services for FY 2005-06 May negatively impact other services being provided
f	Cap revenue growth	To be determined	Similar to tax increment financing May negatively impact other services being provided
g	Sell property	$1,500,000	Strawberry Lane parcels partially committed
		$2,000,000	900 Acres across I-5
		To be determined	Other miscellaneous lands
h	Raise property taxes	$900,000	Will reduce ability to use these funds to balance the budget
i	Create other local revenues:		Requires further study for estimates to be made
	Gas tax		Other agencies are implementing
	Sales tax		In addition to existing prepared food tax.
	Income tax		Being considered by other agencies
	Entertainment tax		$1/ticket - Live performances; could extend to movies & videos

Utility Bill Surcharge Calculation
On Electric Rate Code
By Percentage and/or Flat Fee with Cap

Rate Code	Customer Count	FY 2005-06 Average Revenue/Month	Average		Average % Charge	Max per Acct	Revenue Percentage Basis	Revenue Charge Basis	Monthly Revenue w/ Cap
R01	9,284	$ 472,065.00	$ 50.85	5.00%	$ 2.54	$ 3.00	$ 23,603.25	$ 27,852.00	$ 23,603.25
R04	84	$ 3,743.00	$ 44.56	5.00%	$ 2.23	$ 3.00	$ 187.15	$ 252.00	$ 187.15
C01	1,050	$ 182,473.00	$ 173.78	5.00%	$ 8.69	$ 10.00	$ 9,123.65	$ 10,500.00	$ 9,123.65
C03	206	$ 108,578.00	$ 527.08	5.00%	$ 26.35	$ 25.00	$ 5,428.90	$ 5,150.00	$ 5,150.00
G01	76	$ 17,404.00	$ 229.00	5.00%	$ 11.45	$ 15.00	$ 870.20	$ 1,140.00	$ 870.20
G03	16	$ 10,778.00	$ 673.63	5.00%	$ 33.68	$ 25.00	$ 538.90	$ 400.00	$ 400.00
G50	1	$ 42,091.00	$ 42,091.00	5.00%	$ 2,104.55	$ 100.00	$ 2,104.55	$ 100.00	$ 100.00
M01	50	$ 5,027.00	$ 100.54	5.00%	$ 5.03	$ 5.00	$ 251.35	$ 250.00	$ 250.00
M03	15	$ 22,059.00	$ 1,470.60	5.00%	$ 73.53	$ 50.00	$ 1,102.95	$ 750.00	$ 750.00
							$ 43,210.90	**$ 46,394.00**	**$ 40,434.25**
	Annualized						**$ 518,530.80**	**$ 556,728.00**	**$ 485,211.00**

Rate Code	Customer Count	FY 2005-06 Average Revenue/Month	Average		Average % Charge	Max per Acct	Revenue Percentage Basis	Revenue Charge Basis	Monthly Revenue w/ Cap
R01	9,284	$ 472,065.00	$ 50.85	3.00%	$ 1.53	$ 3.00	$ 14,161.95	$ 27,852.00	$ 14,161.95
R04	84	$ 3,743.00	$ 44.56	3.00%	$ 1.34	$ 3.00	$ 112.29	$ 252.00	$ 112.29
C01	1,050	$ 182,473.00	$ 173.78	3.00%	$ 5.21	$ 10.00	$ 5,474.19	$ 10,500.00	$ 5,474.19
C03	206	$ 108,578.00	$ 527.08	3.00%	$ 15.81	$ 25.00	$ 3,257.34	$ 5,150.00	$ 3,257.34
G01	76	$ 17,404.00	$ 229.00	3.00%	$ 6.87	$ 15.00	$ 522.12	$ 1,140.00	$ 522.12
G03	16	$ 10,778.00	$ 673.63	3.00%	$ 20.21	$ 25.00	$ 323.34	$ 400.00	$ 323.34
G50	1	$ 42,091.00	$ 42,091.00	3.00%	$ 1,262.73	$ 100.00	$ 1,262.73	$ 100.00	$ 100.00
M01	50	$ 5,027.00	$ 100.54	3.00%	$ 3.02	$ 5.00	$ 150.81	$ 250.00	$ 150.81
M03	15	$ 22,059.00	$ 1,470.60	3.00%	$ 44.12	$ 50.00	$ 661.77	$ 750.00	$ 661.77
							$ 25,926.54	**$ 46,394.00**	**$ 24,763.81**
	Annualized						**$ 311,118.48**	**$ 556,728.00**	**$ 297,165.72**

Rate Code	Customer Count	FY 2005-06 Average Revenue/Month	Average		Average % Charge	Max per Acct	Revenue Percentage Basis	Revenue Charge Basis	Monthly Revenue w/ Cap
R01	9,284	$ 472,065.00	$ 50.85	10.00%	$ 5.08	**$ 4.00**	$ 47,206.50	$ 37,136.00	$ 37,136.00
R04	84	$ 3,743.00	$ 44.56	10.00%	$ 4.46	**$ 4.00**	$ 374.30	$ 336.00	$ 336.00
C01	1,050	$ 182,473.00	$ 173.78	10.00%	$ 17.38	**$ 15.00**	$ 18,247.30	$ 15,750.00	$ 15,750.00
C03	206	$ 108,578.00	$ 527.08	10.00%	$ 52.71	**$ 40.00**	$ 10,857.80	$ 8,240.00	$ 8,240.00
G01	76	$ 17,404.00	$ 229.00	10.00%	$ 22.90	**$ 25.00**	$ 1,740.40	$ 1,900.00	$ 1,740.40
G03	16	$ 10,778.00	$ 673.63	10.00%	$ 67.36	**$ 50.00**	$ 1,077.80	$ 800.00	$ 800.00
G50	1	$ 42,091.00	$ 42,091.00	10.00%	$ 4,209.10	**$ 100.00**	$ 4,209.10	$ 100.00	$ 100.00
M01	50	$ 5,027.00	$ 100.54	10.00%	$ 10.05	**$ 10.00**	$ 502.70	$ 500.00	$ 500.00
M03	15	$ 22,059.00	$ 1,470.60	10.00%	$ 147.06	**$ 50.00**	$ 2,205.90	$ 750.00	$ 750.00
							$ 86,421.80	**$ 65,512.00**	**$ 65,352.40**
	Annualized						**$ 1,037,061.60**	**$ 786,144.00**	**$ 784,228.80**

Rate Code	Customer Count	FY 2004-05 Average Revenue/Month	Average		Average % Charge	Max per Acct	Revenue Percentage Basis	Revenue Charge Basis	Monthly Revenue w/ Cap
R01	9,128	$ 413,955.60	$ 45.35	5.00%	$ 2.27	$ 5.00	$ 20,697.78	$ 45,640.00	$ 20,697.78
R04	58	$ 3,601.20	$ 62.09	5.00%	$ 3.10	$ 10.00	$ 180.06	$ 580.00	$ 180.06
C01	1,040	$ 170,028.69	$ 163.49	5.00%	$ 8.17	$ 25.00	$ 8,501.43	$ 26,000.00	$ 8,501.43
C03	198	$ 91,789.00	$ 463.58	5.00%	$ 23.18	$ 100.00	$ 4,589.45	$ 19,800.00	$ 4,589.45
G01	75	$ 15,583.23	$ 207.78	5.00%	$ 10.39	$ 25.00	$ 779.16	$ 1,875.00	$ 779.16
G03	15	$ 9,122.91	$ 608.19	5.00%	$ 30.41	$ 100.00	$ 456.15	$ 1,500.00	$ 456.15
G50	1	$ 39,098.90	$ 39,098.90	5.00%	$ 1,954.94	$ 200.00	$ 1,954.94	$ 200.00	$ 200.00
M01	48	$ 4,603.31	$ 95.90	5.00%	$ 4.80	$ 25.00	$ 230.17	$ 1,200.00	$ 230.17
M03	15	$ 21,149.18	$ 1,409.95	5.00%	$ 70.50	$ 100.00	$ 1,057.46	$ 1,500.00	$ 1,057.46
							$ 38,446.60	**$ 98,295.00**	**$ 36,691.66**
	Annualized						**$ 461,359.21**	**$ 1,179,540.00**	**$ 440,299.87**