PORTLAND'S FISCAL SUSTAINABILITY AND FINANCIAL CONDITION:
Long-term financial position needs attention

June 2013

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Office of the City Auditor
Portland, Oregon

Winner of the 2013 **Silver** Knighton Award for Best Audit
Association of Local Government Auditors

This report has been developed by the Office of the City Auditor, and is intended for the public. This report is the result of a performance audit, and was not part of the City's annual financial audit on the City's financial statements. Expressions of opinion in the report are not intended to guide prospective investors in securities offered by the City and no decision to invest in such secuirities should be made without referencing the City's audited CAFRs and official disclosure documents relating to a specific security.

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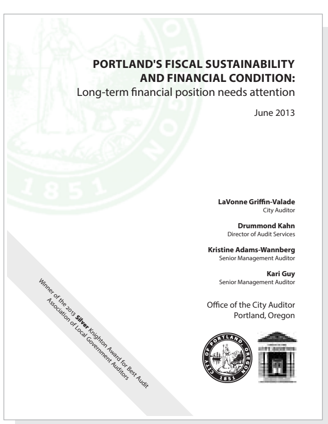

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CITY OF PORTLAND

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June 19, 2013

TO: Mayor Charlie Hales
Commissioner Nick Fish
Commissioner Amanda Fritz
Commissioner Steve Novick
Commissioner Dan Saltzman
Jack Graham, Chief Administrative Officer

SUBJECT: Audit Report - Portland's Fiscal Sustainability and Financial Condition: Long-term financial position needs attention (Report #443)

The City of Portland is a nationally recognized leader in implementation of local government accountability and transparency initiatives. A good example of this is the financial condition report my office has produced for over two decades. Our report reviews the City's current financial position and aspects of future sustainability by tracking financial, economic, and demographic indicators. The report presents 10-year trends and makes recommendations for improvement.

A fiscally sustainable city can meet its financial obligations and support public services on an ongoing basis. It must also be able to withstand economic downturns and finance maintenance and new capital projects without shifting costs to future generations that will not benefit from the services or assets.

We found that the City's financial health is currently stable, due to its diverse revenue base and policies for multi-year financial planning. The City's overall financial position, however, continues to decline. This is due to increasing liabilities, unmet infrastructure maintenance needs, and increasing debt, which weaken the City's ability to provide services on an ongoing basis. These trends are similar to those we identified in our prior Fiscal Sustainability and Financial Condition report, issued in 2011. The trends reported two years ago have continued to worsen.

The City needs to pay attention to its long-term financial position, and my office's biennial Fiscal Sustainability and Financial Condition report should not be the only reminder of the City's financial status. We recommend the Office of Management and Finance assess this on an annual basis and provide Council with options of how the City's financial position could be strengthened. Such a review would inform Council on how best to carry out its service delivery responsibilities using available resources.

LaVonne Griffin-Valade
City Auditor

Audit Team: Drummond Kahn
Kristine Adams-Wannberg
Kari Guy

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SUMMARY

SUMMARY

Findings

Portland's financial health is currently stable, but increasing liabilities, unmet infrastructure maintenance, and increasing debt weaken the City's ability to provide existing levels of service on an ongoing basis. During our audit, we found:

- The City appears to be doing well in the short-term. Its revenue base is diverse, its revenues per resident are increasing, and the number of employees per resident is stable. The City has favorable liquidity and good credit ratings. It also benefits from financial policies that help in multi-year planning.
- The City's longer-term financial position is more problematic. In 8 of the last 10 years, City expenses have been more than revenues. The City's net assets continue to lose ground due to unfunded liabilities and to funding gaps in maintaining infrastructure. Additional infrastructure funding may require more debt if not funded out of current resources.

Water system upgrade

Source: Portland Water Bureau

Recommendations

To improve the City's long-term financial health, we recommend that the Mayor require the Office of Management and Finance (OMF) to provide Council with an annual analysis of how the City's long-term financial position could be strengthened. We further recommend this be an annual presentation to the Council after the completion of the external financial audit, with analysis that includes:

- Development of benchmarks to measure, track, and maintain a strong financial position into the future.
- Evaluation of the contributing factors to the decline in net assets and recommendations from OMF on actions to mitigate the decline.

About the report

To produce this status report on the City of Portland's financial health, we reviewed the City's fiscal sustainability. Fiscal sustainability is tied with the idea of intergenerational equity or fairness and the degree to which *future* taxpayers must pay for *current* policy decisions. To be "fiscally sustainable," the City must be able to pay its bills and provide current services on an ongoing basis. A fiscally sustainable city should also be able to withstand economic downturns and to finance maintenance and new construction projects without shifting costs to future generations that will not benefit from the services or assets.

We evaluated the City's financial health based on a review of trends in several indicators. Nearly all of the warning trend criteria we used were based on criteria published by the International City/County Management Association, City policies, or industry standards. We then used this information to form an overall assessment of the City's financial health.

The key indicators we reviewed, the assessment criteria, the overall trends, and our interpretation are included in the table on the following page.

Investor caveat

This report compares the City of Portland's finances, generally covering a 10-year period, from Fiscal Year 2002-03 (FY 2003) to Fiscal Year 2011-12 (FY 2012). It is important to note that during this timeframe the national recession occurred. Unless otherwise indicated, data presented is from the City's audited Comprehensive Annual Financial Reports (CAFR) and has been adjusted for inflation.

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Key indicators and results

Indicator	Overall 10 year trend	Interpretation
Revenues per resident	↑	OK
Percent of City property tax dollars supporting the General Fund	↓	⚠ Caution
Expenses per resident	↑	⚠ Caution
City employees per 1,000 residents	↔	OK
City outstanding debt principal per resident	↑	⚠ Caution
Credit ratings for outstanding debt	Above minimum City standard for 2012 (except Hydro)	OK
City net assets	↓	⚠ Caution
City liquidity	Above standard of $1 current asset per $1 current liability	OK
Pension and other post employment benefit liabilities	↑	⚠ Caution
Funded ratios for pension liabilities and other post-employment benefits	Mixed - criteria is 80% funded ratio 0% for FPDR and OPEB, 88% for PERS in 2009	⚠ Caution
Asset condition	No trend. 2012 data shows condition varies widely by asset. 39 percent of PBOT assets are in poor condition.	⚠ Caution
Annual funding gap in infrastructure budgets	No trend. 2012 data shows $210 million funding gap.	⚠ Caution

Source: ICMA's *Evaluating Financial Condition: A Handbook for Local Government* for most criteria and Audit Services analysis for overall trends

INDICATORS

REVENUE INDICATORS

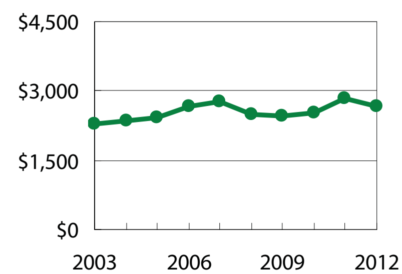
About the indicators

Revenues determine the capacity of a local government to provide services. Below, we show detail on City revenues per resident, City property taxes and utility revenues. Financial information has been adjusted for inflation.

City revenues increased between 2003 and 2012

Total City revenues are up 26 percent from $1.2 billion in 2003 to $1.6 billion in 2012. Portland's population has grown 9 percent during this time. Total revenue per resident increased 16 percent during the 10 years, from $2,292 to $2,656.

Revenue per resident (adjusted)



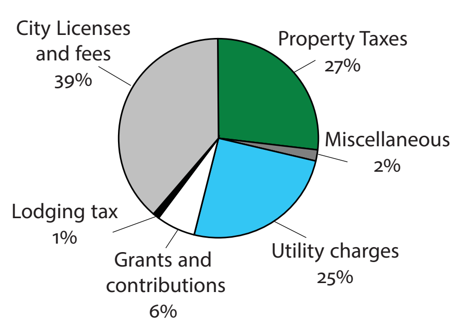
Source: Portland CAFRs and PSU Center for Population Research

Diversified revenue sources help the City weather downturns

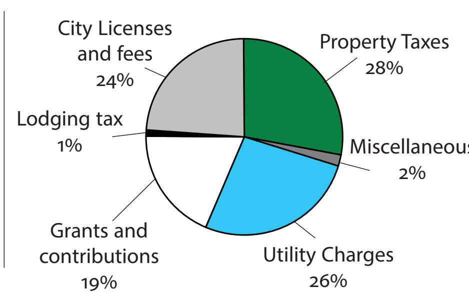
Revenues are diversified between sources that are more stable, such as property taxes and utility charges, and revenues that fluctuate with the economy, such as business licenses and lodging taxes. The composition of City revenues changed from 2003 to 2012, with decreases in more volatile City licenses and fees offset by increased grants and contributions from other governments. One-time capital grants peaked in 2011 with large federal grants for transportation projects such as the Eastside Streetcar line and the realignment of Moody Avenue.

Revenues by source (adjusted)

2003 ($1.2 billion)



2012 ($1.6 billion)



Source: Portland CAFRs

Where each dollar of City property tax goes

Total property taxes going to the City of Portland grew by 27 percent, from $338 million in 2003 to $429 million in 2012. City property taxes pay for a variety of services. The General Fund pays for services such as parks, police, and fire protection. Taxes paid to the Fire and Police Disability and Retirement Fund are used to pay for retirement and disability costs for active and retired police and firefighters. Urban renewal funds collect property taxes to pay off debt incurred for urban renewal area improvements. Voters may also approve property taxes for other purposes, such as special levies or bonds, and those are also deposited in dedicated funds.

The services and obligations of City property tax dollars have shifted over the last 10 years, with an increasing share going to support urban renewal debt, and less going to the General Fund. Property tax revenue to the General Fund grew by 8 percent from 2003 to 2012. During that same time period, property taxes to pay urban renewal debt grew 68 percent.

2003 City property tax dollar ($338 million, adjusted)

2012 City property tax dollar ($429 million, adjusted)

Source: Portland CAFRs

Growing losses due to property tax limits

All general government property taxes must fit within a limit of $10 per $1,000 of real market property value. This includes City of Portland taxes, and also Multnomah County, Metro, Port of Portland, and other taxing districts. If the limit is exceeded, local option levies such as the Children's Levy are reduced first, or 'compressed,' to zero if necessary. If further reductions are needed to reach the limit, all other taxes are reduced on a proportional basis.

Reductions in real market value due to declining home prices, combined with increases in FPDR costs and higher urban renewal taxes, increased compression losses in recent years. In 2012, compression losses were $24 million. In 2013, losses due to compression increased to $30.5 million. The new Library District approved by Multnomah County voters in November 2012 will likely further increase compression losses in 2014.

City property tax losses due to compression (millions, adjusted)

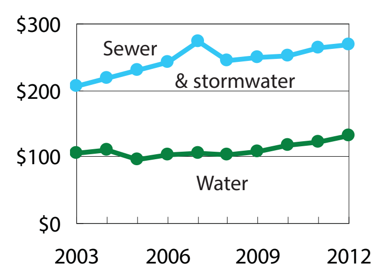
Year	City revenue loss
2003	$10
2004	$24
2005	$21
2006	$17
2007	$15
2008	$14
2009	$10
2010	$14
2011	$17
2012	$24

Source: Tax Supervising and Conservation Commission

Utility revenues increasing

Revenues for sewer and stormwater fees (Environmental Services) increased 30 percent, from $207 million in 2003 to $269 million in 2012. Water revenues increased 23 percent, from $107 million to $131 million over the same period. These revenues are not discretionary and must be spent on water and sewer services.

Utility Revenues 2003-12
(millions, adjusted)



Source: Portland CAFRs

EXPENSE INDICATORS

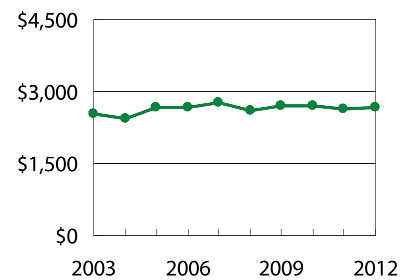
About the indicators

Expense measures a government's cost of providing services. Some common expenses are salaries and wages, pension obligations, and asset depreciation. Below, we show City expense per resident and by service area. We also show how many employees work for the City. Financial information has been adjusted for inflation.

City expense per resident increased since 2003

City expense per Portland resident increased 6 percent from $2,520 in 2003 to $2,661 in 2012. Total City costs increased from $1.4 billion to $1.6 billion, a 15 percent increase.

Expense per resident (adjusted)



Source: Portland CAFRs and PSU Center for Population Research

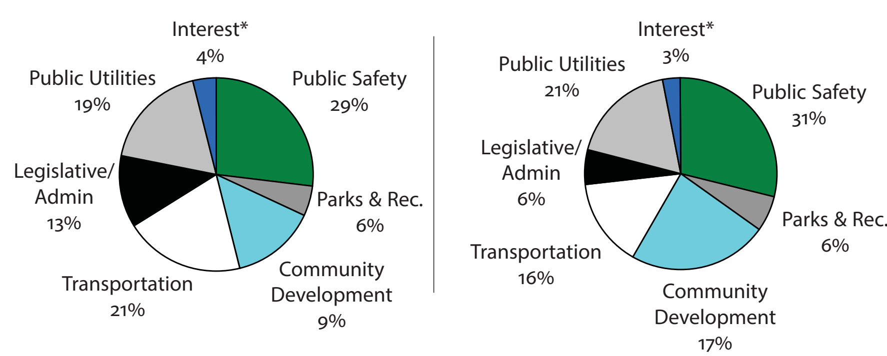
Public safety services remain the single largest City expense

For the last ten years, the City's largest expense by service area was for Public Safety services. These include police, fire, emergency communications, and emergency management functions. In 2012, public safety expenses were $487 million and represented 31 percent of the total City expense. This is a 26 percent increase from 2003, when it was $387 million.

Expense by service area (adjusted)

2003 ($1.1 billion)

2012 ($1.6 billion)



Source: Portland CAFRs

* Interest on long-term debt is for governmental activities only. Interest for business activities (largely public utilities) is included in their respective service area.

Expense by service area (adjusted, millions)

Source: Portland CAFRs

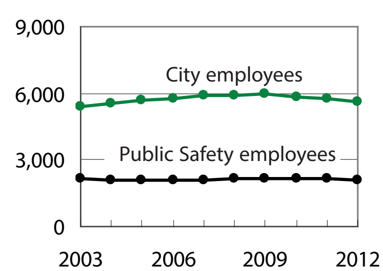
Public Utilities were 21 percent of City expenses in 2012. These water, hydropower, and sewer services combined increased 27 percent from 2003 to 2012, from $254 million to $323 million, respectively.

Community Development has grown to be the City's third largest expense. Some of these expenses include development services, housing, and urban renewal. This service area was $259 million in 2012, representing 17 percent of the City's costs. This is an increase from $125 million in 2003, when it was 9 percent. Some of the change is from a 2010 re-categorization of the Special Finance and Resource Fund from the Legislative/Administration area to Community Development. The fund holds urban renewal bond proceeds.

The number of City employees per resident was steady

Total City employment grew over 10 years, from 5,403 to 5,601 employees. The number of employees per Portland resident remained at about 10 employees per 1,000 residents during the same time period. The number of public safety employees also remained relatively steady at approximately 4 public safety employees per 1,000 residents.

City employees



Source: Portland SAP system, BHR position management system, PDC CAFRs

DEBT INDICATORS

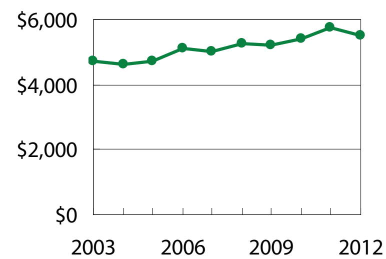
About the indicators

The City borrows money to pay for capital improvements ranging from sewer pipes to computer systems, and to finance urban renewal programs. Below, we show debt per City resident and details on the trends, uses, ratings, and annual debt service costs for various types of City debt. Financial information has been adjusted for inflation.

Debt per resident increased

The City's total outstanding debt increased 26 percent from 2003 to 2012, from $2.6 billion to $3.2 billion. In 2012, the total outstanding debt per resident was $5,496. This is an increase of 16 percent from 2003.

Debt per resident (adjusted)



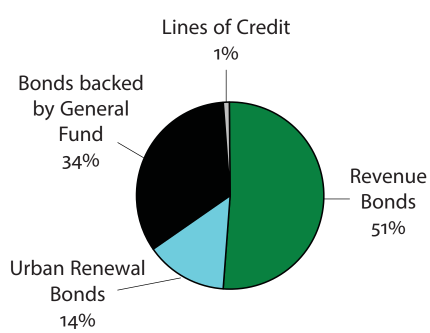
Source: Portland CAFRs and PSU Center for Population Research

The majority of debt is for revenue bonds

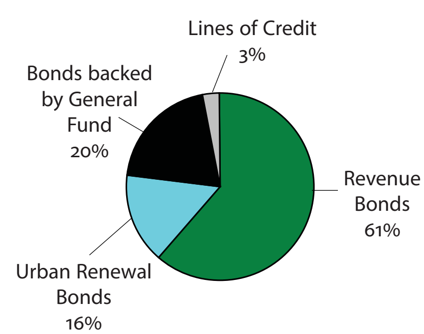
Sixty-one percent of the City's outstanding debt is for revenue bonds. Revenue bonds finance new or improved infrastructure for City services with dedicated revenues. These include water, sewer, gas tax, and hydroelectric power bonds. The assets purchased or improved with these bonds are shown on the City's statement of net assets. Outstanding debt for revenue bonds increased 53 percent from 2003 to 2012, from $1.3 billion to $2.0 billion.

Debt by type (adjusted)

2003 ($2.6 billion)



2012 ($3.2 billion)



Source: Portland CAFRs

Almost all of the revenue bonds are for sewer infrastructure ($1.6 billion) and water system improvements ($0.4 billion). Major water and sewer projects include the Combined Sewer Overflow (the Big Pipe project) and replacement of aging infrastructure.

The City has no specific limit on the amount of revenue bonds it may issue but debt capacity is restricted by existing bond covenants and available repayment resources. City debt policy requires that before a new bond is issued, the City develop a financial plan to show the required rates and charges to support the debt, and the ratepayer impact.

The use of debt backed by City General Funds decreased

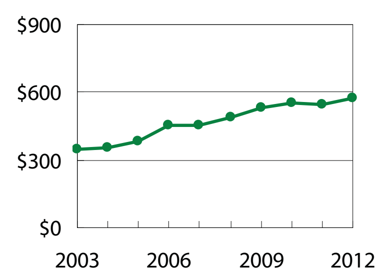
Debt backed by the General Fund includes General Obligation bonds approved by voters, and paid with property taxes as well as bonds paid from other General Fund resources, such as lodging taxes. It also includes bonds to be paid by dedicated revenues such as spectator facilities revenues, with property taxes used as a guarantee. Bonds backed by the General Fund decreased 26 percent from 2003 to 2012, from $875 million to $645 million. General Obligation bonds totaled $71 million in 2012 for fire stations, parks and public safety.

City debt policy limits bonds backed by the General Fund as a percentage of real market value of property within the City. According to OMF, the City has always operated within those limits. OMF noted in 2013 that due to reductions in real market value and planned new debt, the City may come closer to reaching these limits.

Urban renewal debt continues to grow

Urban renewal debt grew 66 percent from 2003 to 2012, from $347 million to $577 million. This debt pays for housing and economic development programs in urban renewal areas, with the expectation that property values will increase due to the investments. The property taxes from this increase in value are used to pay off the debt.

Urban renewal debt
(millions, adjusted)



Source: Portland CAFRs and Office of Management and Finance

2012 Urban renewal debt by area
(millions, adjusted and rounded)

Urban Renewal Area	Debt Outstanding
Convention Center	$103
River District	$82
Interstate Corridor	$76
Downtown Waterfront	$76
South Park Blocks	$62
North Macadam	$60
Airport Way	$37
Central Eastside	$35
Lents	$35
Gateway	$13
TOTAL	**$577**

Source: City of Portland CAFR and Office of Management and Finance

Some investments in urban renewal areas, such as parks or transportation improvements, result in new assets owned by the City. However, other investments, such as business and housing grant and loan programs, result in assets owned by others.

The City sets a limit on the amount of debt that may be issued in each urban renewal area as part of the plan for each area.

How much debt is too much?

City debt policies are consistent with best practices. General Fund-backed debt is within limits set by City policy, and nearly all ratings for outstanding debt meet City policy for a minimum A3 rating (above-average credit quality). About 12 percent of the City's debt has an Aaa rating, including General Obligation Bonds. This is the highest quality grade and means lower borrowing costs. The remaining 88 percent of City debt has lower ratings, ranging from Aa1 to Baa1. This indicates that the rating agencies view the debt as a low credit risk.

Debt Ratings

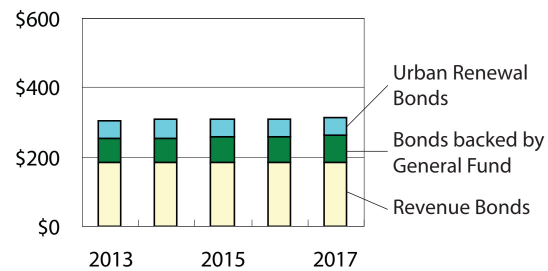
Type	% of City total	Moody's Rating	Credit Quality
General Obligation Bonds	2%	Aaa	Strongest
First Lien Water Revenue Bonds	10%	Aaa	Strongest
Other Full Faith and Credit Obligations	18%	Aa1	Very strong
Other Revenue Bonds	51%	Aa1 to Aa3	Very strong
Urban Renewal Bonds	16%	Aa3 to A2	Very strong to above-average
Lines of Credit	3%	Not rated	Not rated
Hydroelectric Power Bonds	<1%	Baa1	Average

Source: Annual Debt Report FY 2011-12

Debt financing allows the City to spread the costs of large capital projects across multiple years, so future taxpayers who benefit from the project will pay for a portion of the project.

Increasing debt payments, however, put demand on general government revenues and ratepayers. The City must dedicate over $300 million to pay principal and interest on outstanding bonds in each of the next five years, decreasing funds available for other City services, such as maintaining capital assets. Property taxes dedicated to pay off urban renewal area debt service are not available to other taxing districts, such as local school districts. Increases in rates and charges needed to pay off the debt raise the cost of living in Portland.

Projected debt service payments
(millions, adjusted)



Source: Portland CAFRs and Office of Management and Finance

In our 2011 Fiscal Sustainability and Financial Condition report, we recommended that the City develop and monitor measures of Citywide debt, and report this information annually to the City Council. The Office of Management and Finance now prepares an annual debt report with detailed information on bond sales and trends, and includes indicators that look at specific categories of debt. The report notes that a single indicator might provide an incomplete picture of the City's financial health, and that indicators for specific categories of debt provide more useful information, because risks and other conditions vary.

This annual debt report should help City managers determine the true cost of providing services and the best approaches for financing them over the long term, to ensure that the use of debt to fund current projects does not unfairly burden future City residents.

PENSIONS AND OTHER LIABILITIES

About the indicators

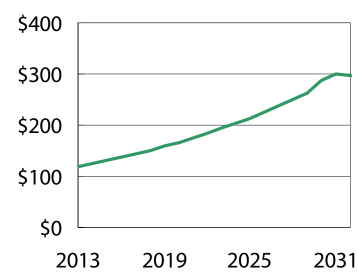
An "unfunded liability" is the current value of future payment obligations for which reserves have not been set aside. Information on pension and post employment benefit liabilities is provided below. Pension and other post-employment financial information was not adjusted for inflation. This is because the actuarial estimates are based on a point in time and calculation assumptions may vary from estimate to estimate.

Fire and Police Disability and Retirement unfunded liabilities will increase taxpayer costs

Portland's Fire and Police Disability and Retirement Fund (FPDR) was created by voters in 1948 for the benefit of sworn officers of the Bureaus of Police and Fire. The fund was set up as a 'pay-as-you-go' retirement system funded by a dedicated property tax levy. The system was changed to a funded retirement plan for new hires by voter-approved Charter amentments in 2006.

Unlike a funded retirement plan, a pay-as-you-go plan does not set aside funds to pay for future benefits. Instead, FPDR must collect sufficient revenues through the dedicated property tax each year to pay the annual costs. Because the plan does not reserve revenues for future retirements, the fund has an unfunded liability. As of June 30, 2012, the unfunded liability was estimated at $2.9 billion. This means that the City has promised future retirement benefits of $2.9 billion without having current funding to support them.

FPDR projected annual costs
(millions, unadjusted)



Source: Milliman

In 2006, voters approved amendments to the City Charter governing the FPDR system. Beginning in 2007, new police officers and firefighters are enrolled in the Oregon Public Employees Retirement System (PERS), a pre-funded retirement plan. Taxpayers now pay for two generations of retirees – funding the pension costs of current retirees, and pre-funding the pensions for police and firefighters hired after 2007.

Pension costs for retirees under the pay-as-you-go plan will likely continue to rise until all of those employees are retired, in 20 to 25 years. Total annual costs for pay-as-you-go and pre-funded retirement plans are estimated to increase from $118 million in 2013 to $296 million in 2032, not adjusted for inflation. Because of uncertainty about future economic conditions, the estimates for later years have greater variability.

In November 2012 voters again approved amendments to the FPDR provisions in the City Charter. The amendments clarified how benefits are calculated, among other changes. In total, the Charter changes were estimated to decrease taxpayer-funded costs by almost $47 million over a 25-year period.

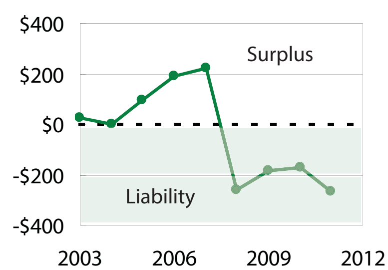
Despite these voter-approved changes, growing FPDR taxes continue to present risks to taxpayers, the City, and other local governments. The FPDR property tax levy is estimated to increase about 39 percent over the next five years. Increases to the tax levy are likely to increase tax compression, decreasing revenue available to other local governments and particularly to special levies such as the Children's Levy.

The FPDR property tax rate is limited by Charter to $2.80 per $1,000 of property value. If the tax rate reaches the limit, any FPDR costs not funded by the FPDR levy must be funded from the City's General Fund. While this risk is small, current models show a 5 percent chance of the tax limit being reached in 2028, growing to almost a 10 percent chance in 2031.

The City's PERS liability funded status is within an acceptable range

All civilian City employees, and nearly all sworn fire and police personnel hired after December 31, 2006, are participants in PERS. PERS is the pre-funded retirement plan for the State of Oregon and many local governments and districts in Oregon.

PERS liability (millions, unadjusted)



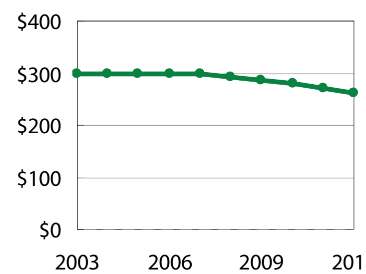
Source: Portland CAFRs and Mercer Inc.

The City's estimated PERS liability as of December 31, 2011 was $265 million. For half of the last decade, the City had no liability with PERS, due to paying the liability in full and covering the obligation with $300 million in pension obligation bonds. However, according to the Office of Management and Finance (OMF), changes, primarily in the investment market among others, created a liability for the City beginning in 2008.

Assumptions used in a liability estimate may differ from those used in prior projections. The estimate helps the City and creditors determine demands on the City's future cash flows. The liability is one of many measures that credit rating agencies consider when assessing City funds' credit-worthiness.

As of June 30, 2012, the City had about $261 million in principal outstanding on the pension bonds, and 17 years of debt service remaining. About half of the debt service is structured with a variable rate and half with a fixed rate. According to OMF the pension debt produces savings over the life of the obligation, compared to what the City would have been charged through PERS.

Pension debt principal
(millions, unadjusted)



Source: Portland CAFRs

One of the most recognized measures of the financial health of a pension plan is the "funded ratio." This ratio is the level of assets in the plan divided by the current value of its liabilities. If a plan were 100 percent funded, its assets plus investment returns would, in theory, be sufficient to pay all the benefits that plan members earned. A plan that is less well funded would run out of money (assets), while still owing benefits to its members.

Many experts find a funded ratio of 80 percent or more to be acceptable for a pension system. A current estimate of the funded ratio was not available. OMF and Mercer Inc., estimated that the City's funded ratio at the end of 2009 was 88 percent.

Lack of pre-funding other post employment benefits increases the City's liabilities

In addition to pension benefits, the City provides other post employment benefits (OPEB) for eligible retirees. These benefits are part of a total compensation package and are used to attract and retain qualified employees. The City does not pay for post-retiree health benefits, but does allow retirees to purchase health insurance at the City's group rate until age 65. This creates an implicit subsidy. The City also contributes toward Medicare companion insurance through the state PERS Retirement Health Insurance Account (PERS-RHIA). These two provisions are required by state statute. In addition, the City pays medical costs, through the Fire and Police Disability and Retirement Fund, for retired police officers and firefighters for service-related disabilities and injuries.

The City's current unfunded liability for insurance continuation and the FPDR subsidy is $110 million, based on a 30 year projection. The liability for the PERS-RHIA is $8 million, based on a 10 year projection. As mentioned, many experts find an 80 percent funded ratio or more to be acceptable. The City's three OPEB benefits have a funded ratio of zero percent.

The City offers OPEB benefits on a pay-as-you-go basis rather than pre-funding the benefits. The pay-as-you-go method is used by many employers who are unable to fund the benefits in advance. The problem is that this method creates a growing liability that is not matched by a dedicated funding source. Council was made aware of this in June 2008, when it accepted a report from OMF on the topic.

2012 OPEB liabilities and ratios
(Industry target is 80%)

	Liability (UAAL, millions)	**Funded Ratio**
Insurance continuation	$105	0%
PERS - RHIA	$8	0%
FPDR Subsidy	$5	0%

Source: City of Portland CAFR, and Milliman

CAPITAL ASSETS INDICATORS

About the indicators

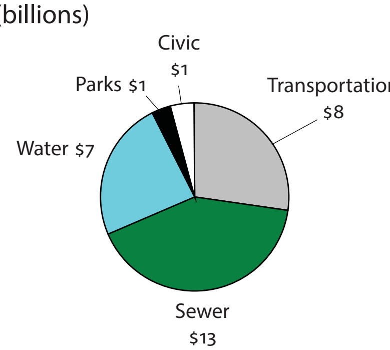
The City uses physical infrastructure to provide services to residents. Some examples are streets and sewer and water lines. How these assets are treated can impact the quality of services residents receive. Good asset management requires investment in regular preventive maintenance. It increases the life of the asset and reduces costs. The risk in not maintaining the City's infrastructure is early failure of assets and increased costs over the life of the assets.

City manages assets worth $30 billion

The City Asset Managers Group presents a Citywide Assets Report to City Council each year. The 2012 report estimates the replacement value of the City's physical infrastructure assets at $30 billion.

The replacement value of assets is a different number than that reported in the City's financial reports and discussed in the net assets section of this report. The financial reports estimate the value of an asset as it declines due to wear and tear over time. The replacement value is an estimate of the money that would be needed to buy or rebuild the asset in the current year. Each bureau has its own methodology for estimating replacement value.

Replacement value of City assets (billions)



Source: 2012 Citywide Assets Report

Condition of City assets varies

The Citywide Assets Report includes estimates of asset condition reported by bureau. The Bureau of Environmental Services reports the highest percentage of assets in good condition (70 percent) for sewer and stormwater infrastructure. The Bureau of Transportation reports the lowest percent of assets in good condition (38 percent) for the streets, sidewalks, bridges, and streetlights.

Bureau estimates of asset condition

	Good	Fair	Poor	To be determined
Civic	52%	36%	3%	8%
Environmental Services	70%	14%	17%	0%
Parks and Recreation	52%	22%	9%	16%
Transportation	38%	24%	39%	0%
Water	51%	34%	16%	0%

Source: 2012 Citywide Assets Report

Funding gaps limit maintenance

The Citywide Assets Report includes an estimate of the annual gap between infrastructure funding needs and funding levels. The funding gap is reported in three categories:

1. Repair and replacement
2. Mandates to improve assets to meet regulatory requirements
3. Capacity increases to address service deficiencies

Like asset value and condition, each bureau has a different methodology for estimating the funding gap. The additional annual funding needed to bring existing assets up to current service levels and meet regulatory mandates is estimated at $210 million.

Only Parks and Environmental Services noted funding gaps to increase capacity. The Parks and Recreation Bureau estimates needing $49 million per year to include new park facilities in underserved areas. Transportation does not estimate any costs to increase capacity, noting that unpaved streets and sidewalks are not maintained by the City.

Annual funding gap (millions)

	Repair, Replacement	Mandate	Capacity	Total
Civic	$17	$0	$0	$17
Environmental Services	$5	$0	$7	$12
Parks and Recreation	$29	$7	$49	$84
Transportation	$141	$0	$0	$141
Water	$11	$1	$0	$12
Total:	$202	$8	$56	$266

Source: 2012 Citywide Assets Report

Resource constraints make it challenging to fund maintenance and replace capital assets. However, as we described in our 2013 *Street Pavement: condition shows need for better stewardship* audit, deferring maintenance leads to higher future costs. In 2008 the City Council added a financial policy that at least 25 percent of General Fund revenue that exceeds budgeted beginning balance will be allocated to infrastructure maintenance or replacement. $2.4 million was allocated in 2011, but there was no surplus in 2012.

While the change to the financial policies is a good step, it does not produce a consistent, permanent funding stream. We continue to support developing a funding strategy for infrastructure maintenance and a budget priority to take care of current assets, before adding new assets.

FINANCIAL AND OPERATING POSITION

About the indicators

Financial position is a government's financial standing at a given point in time, while operating position is a government's ability to balance its budget, to maintain reserves for emergencies, and to have enough money to pay its bills on time. We present net asset and liquidity measures below which represent two measures of the City's financial and operating position.

Net asset data was not adjusted for inflation. This is because the information is based on point in time estimates and the measure includes actuarial estimates with assumptions that change over time. Liquidity data is based on financial data that has been adjusted for inflation.

The City's total net assets decreased since 2003

Net assets are a measure of a government's financial position. Net assets measure the difference between what the government owns (assets) minus what it owes (liabilities). In reality, the City's bills would not come due all at once, and the City is unlikely to sell its streets and water lines to pay for what it owes. What is important, however, is the change in net assets. It indicates how much the City's financial position has improved or worsened as a result of events and transactions made during the period. A decline in net assets means that current costs are being shifted to future taxpayers.

Peninsula outdoor pool

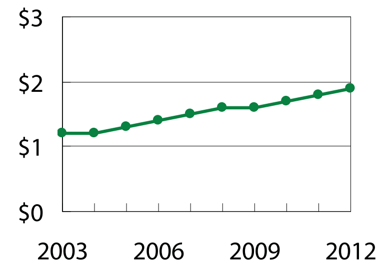
Source: Portland Parks & Recreation

The City's total net assets declined 11 percent from 2003 to 2012, from $3.1 billion to $2.7 billion. Net assets are counted separately for the City's business activities that are supported by rates, such as water and sewer services, and all other governmental activities, such as parks and transportation systems. We include the net assets of the Portland Development Commission with the governmental activities.

Infrastructure investment increased net assets for self-supporting services

Business net assets grew 64 percent from 2003 to 2012, from $1.2 billion to $1.9 billion. Most of this amount, $1.8 million, is invested in capital assets for the water and sewer systems.

Business net assets
(Primarily water and sewer, billions)



Source: Portland CAFRs and PSU Center for Population Research

Sewer treatment tank

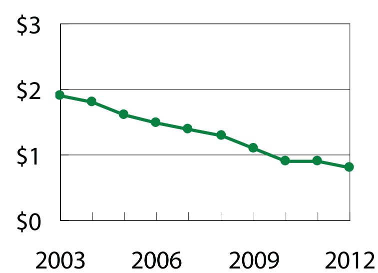
Source: Bureau of Environmental Services

As outstanding water and sewer revenue bonds are paid off and new projects are completed, business net assets should continue to increase.

Declines in governmental net assets indicates worsening financial position

Governmental net assets declined 57 percent from 2003 to 2012, from $1.9 billion to $0.8 billion. The two largest factors in the decline are a decrease in the value of capital assets (primarily transportation infrastructure) and an increase in pension liabilities. Declines in the value of capital assets are due to wear and tear as those assets age (depreciation). Assets declined faster than reinvestment in new or improved assets. Failure to maintain these assets pushes higher costs to future years.

Governmental net assets (billions)



Source: Portland CAFRs and PSU Center for Population Research

A large part of the increase in pension liabilities is because of an accounting rule that makes the City recognize an increasing amount of the Fire and Police Disability and Retirement Fund (FPDR) unfunded pension liability each year in the financial statements. However, the current net assets figure still includes only $1.2 billion of the estimated $2.9 billion of unfunded FPDR pension liability.

If the full FPDR were pension liability were included, the City's net assets for governmental activities would be below zero, at negative $905 million. Beginning in 2015 the City will be required by new accounting rules to include the full FPDR pension liability in the calculation of net assets.

The ongoing decline in governmental net assets means that the City is shifting current costs – for maintaining assets and paying pension costs – to future generations. The change in governmental net assets, and the key reasons for the change, should be analyzed on an annual basis to ensure the City maintains a strong financial condition into the future. This analysis should be presented to Council each year with the report of the external financial auditors.

The Portland Building

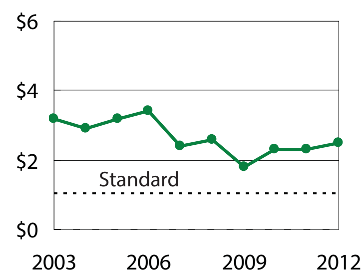
Source: Audit Services Division

City liquidity trended downward, but remained positive over 10 years

Liquidity is the City's ability to pay its short-term bills. It is measured by a ratio of current assets to current liabilities. Current assets include cash and assets that can be converted into cash or used within 12 months (i.e. for inventories and pre-paid expenses). Current liabilities are bills the City intends to pay within 12 months. A low ratio, below 1.0, is a warning trend and may indicate a cash flow problem and the need for short-term borrowing.

City liquidity (including PDC) has varied over time and trended downward. It has, however, stayed above a minimum ratio of 1:1 for the 10 year period.

City liquidity ratio
($1 asset : $1 liability standard)



Source: Portland CAFRs

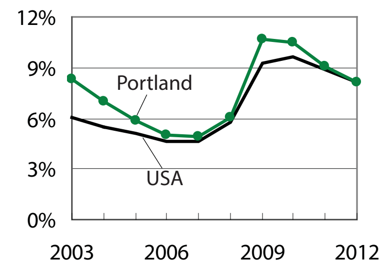
About the indicators

Economic and demographic information highlights community needs and resources. This section presents data on unemployment, jobs, income per resident, property values, and city employment. Financial information has been adjusted for inflation.

The Portland area is continuing a modest economic recovery

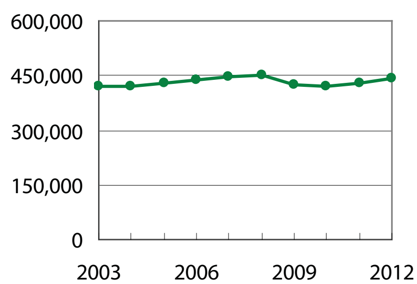
Portland's unemployment rate was about 8 percent in 2012. The rate was higher than the national unemployment rate until 2012, when the rates matched.

Unemployment



Source: U.S. Bureau of Labor Statistics

Jobs in Multnomah County

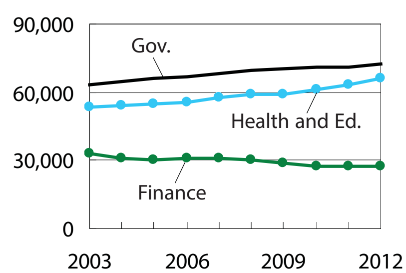


Source: Oregon Department of Employment

There were about 441,000 jobs in Multnomah Country in 2012. This is a 5 percent increase compared to 10 years ago. The number of jobs rose every year from 2003 through 2008. It decreased in 2009 and 2010, but recovered in recent years.

Finance jobs (including real estate positions) decreased the most, from 33,110 jobs in 2003 to 27,182 in 2012. Education and heath services jobs, as well as government jobs (federal, state, and local), have seen the biggest increases of the last 10 years. These sectors combined account for over 21,000 additional jobs from 2003 through 2012.

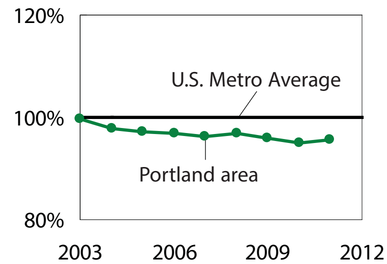
Finance, Health and Education and Government jobs in Multnomah County



Source: Oregon Department of Employment

Since 2004, the Portland area's income per resident was less than the national average for metropolitan areas. Income per resident in the Portland area was $42,066 in 2011 – a slight increase from $41,384 in 2003. The national average increased about 6 percent during the same time, from $41,538 to $43,968. Data for 2012 was not available at the time of publication.

Income per resident
(compared to U.S. metro average)

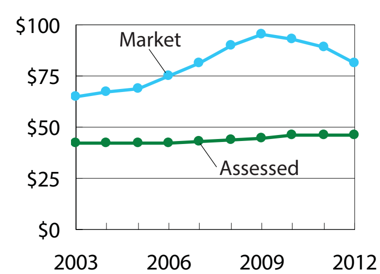


Source: U.S. Bureau of Economic Analysis

Property values are higher than they were 10 years ago

Comparing 2003 values to those in 2012, market values of Portland properties increased 25 percent, from $65 billion to $81 billion, while assessed values increased 10 percent, from $42 billion to $46 billion. The gap between assessed values and market values is due to the limitation set by Measure 50. This 1997 statewide ballot measure limited assessed value growth to 3 percent per year in most properties. The City of Portland's property tax revenues are based on assessed values rather than market values. According to the Office of Management and Finance, because property tax revenues are based on assessed values, the revenues are relatively stable. Non-economic issues such as the establishment of the Multnomah County Library District, however, can decrease property tax revenues to the City.

Total property values
(billions, adjusted)



Source: Multnomah Tax Supervising and Conservation Commission Reports

Population increased over the past 10 years

Portland's population increased about 9 percent over the past 10 years, from 536,180 in 2003 to 585,845 in 2012. In 2012, Portland accounted for about 15 percent of Oregon's total population.

FISCAL DECISION-MAKING CAPACITY

About the indicators

Decision-making capacity is a government's ability to make decisions to keep it financially sound. Among factors that impact this capacity are an entity's form of government, delivery of core services, and its decision-making processes.

Portland's form of government presents benefits and challenges in governing the City

The City of Portland is the last remaining large city in the United States using a commission form of government. In a commission form of government, the elected City Council's legislative functions include adopting the City budget and passing laws, policies, and regulations that govern the City. The Mayor and Commissioners also serve as administrators of City departments, individually overseeing bureaus and carrying out policies. The Mayor assigns departments and bureaus and has discretion to change assignments at will.

Any form of government has strengths and weaknesses. One civic group identified some benefits of the commission form in attracting strong leaders, providing opportunities to implement innovative policies and projects, and providing the public with greater access to City leaders. The 2007 Charter Review Commission, however, identified a number of drawbacks, such as difficulty coordinating service provision, varying levels of bureau responsiveness, and challenges for City Council members in developing citywide strategies and policies.

The City funds some services that may be more appropriate for other jurisdictions to supply

To provide services more efficiently, Multnomah County and Portland agreed in 1983 which jurisdiction would provide particular types of services. As a result, Portland focused on "urban services," such as police, fire, parks, water, sewers, and streets. The County focused on human services and state-mandated responsibilities such as health, social services, elections, tax collection, prosecution and jails.

Over the years, the City funded some services that, in terms of the agreement with the County, may be outside of the City's agreed-upon functions. Some examples are education funding and affordable housing. While funding these services can be worthwhile, it raises questions about inefficient service delivery and public accountability for multiple levels of local government. In our 2013 audit, *Urban Services Policy and Resolution A: Core City services not articulated; 30-year old commitments obsolete*, we recommended the City develop and document a clear list of City responsibilities and update Resolution A and the Urban Services Policy.

City processes are subject to public scrutiny

The public has various ways to inspect how the City spends its resources. State statutes, for example, outline how the City's budget is adopted and amended, as well as the requirements for public hearings. The annual audit of the City's Comprehensive Annual Financial Report (CAFR) is performed by an independent financial auditor. There are also a number of opportunities for residents to volunteer on City advisory boards and commissions.

Comprehensive policies help the City manage its finances

City financial policies guide, and at times restrict, how the City spends its resources. Portland's financial policies meet many best practices established by the Government Finance Officers Association, and they address a number of different subject areas, such as financial planning and budgeting, revenue policies, infrastructure management, and debt management. Some examples of their direction include requiring five-year financial plans for many bureaus and funds, as well as establishing the City's General Reserve Fund and limiting how it may be used.

Indicators

Trend information is relevant for financial analysis. Comparative data can also provide context. We recommend readers be cautious using this information. There are similarities between some governments, but there are also important differences. According to OMF, Portland's FPDR system, for example, makes comparisons challenging. These may require investigation before making conclusions as to a city's relative financial performance.

We provide Portland's 2012 financial information in comparison with the average of six other jurisdictions, Charlotte, NC; Cincinnati, OH; Denver, CO; Kansas City, MO; Sacramento, CA; and Seattle, WA. To be as comparable as possible, the information is based on each jurisdiction's "primary government." For Portland, the financial information does not include the Portland Development Commission, and for other cities it does not include their sub-units, such as visitors' authorities, for example. Because of this, the Portland figures may be different than presented in previous sections of this report.

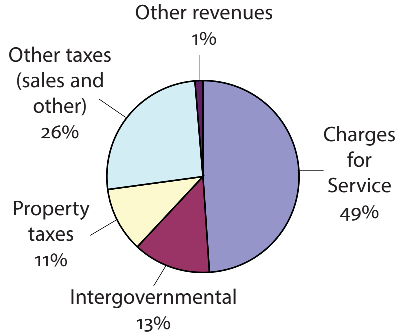
Portland relies more on property taxes and intergovernmental revenues

In 2012, Portland had about $1.5 billion in revenues, compared with the other-city average of $1.6 billion. Revenue per resident was $2,617 in Portland, compared to $3,000 in the other-city average. In both Portland and the other cities, about half of those revenues came from charges for services, such as water and sewer services.

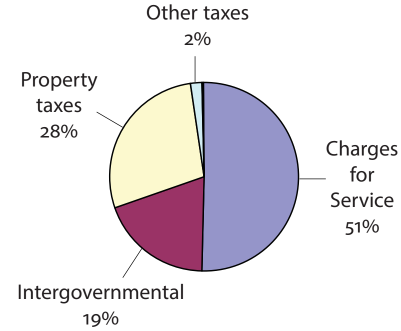
Portland relies more on property taxes and intergovernmental revenues than other cities. The other-city average relies more on other taxes, such as sales and income taxes, in their revenue mixes.

2012 Revenues by source (primary gov)

Other-city average ($1.6 billion)



Portland ($1.5 billion)



Source: Portland and other city CAFRs

Many of Portland's service expenses are comparable to other cities

In 2012, Portland's expenses were $1.6 billion, while the other-city average was about $1.5 billion. Expense per resident was $2,694 for Portland, compared to $2,843 in the other-city average.

Portland has comparable service area expenses for Parks, Legislative and Administrative Functions, and water and sewer utilities. Portland expenses for Parks, Recreation and Culture were 6 percent compared to the comparison-city average of 8 percent. Legislative and Administrative functions were 6 percent, versus the average of 9 percent. Water and sewer expense was 19 percent, compared to 16 percent.

2012 Expense by service area primary gov)

Expense	Other city Avg.	Portland
Public Safety	24%	31%
Transportation & Parking	10%	16%
Parks, Rec & Culture	8%	6%
Public Health	4%	0%
Community Development	6%	19%
Legislative/Administration	9%	6%
Public Utilities (water & sewer)	16%	19%
Other (airports & electric utility)	20%	0%
Interest (Gov. activities only)	3%	3%

Source: Portland and other city CAFRs

Unlike several of the other governments, Portland does not operate an airport or have a public health function. Portland also has more expenses for Community Development (19 percent of total expenses versus 6 percent for the other-city average).

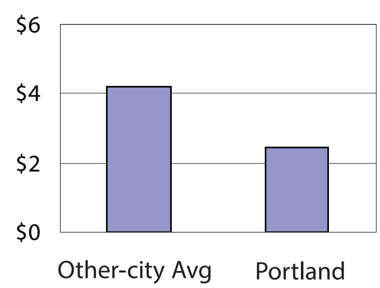
Portland's outstanding debt is slightly higher

Portland had about $3.2 billion in debt principal outstanding in 2012. This is slightly higher than the other-city average of $3 billion. Debt per resident in Portland was $5,544 and $5,241 for the other-city average.

Portland's net assets are less than the other-city average

In 2012, Portland had total net assets of $2.4 billion. The average of the other cities was $4.2 billion. While revenue and expense levels are similar, the other-city average took in more revenues than expenses.

2012 Net assets (billions)



Source: Portland and other city CAFRs

The City should analyze the causes of its declining net assets

Portland's financial condition is currently stable and the City benefits from financial policies that help in multi-year planning. However, several trends appear to be weakening the City's long-term fiscal sustainability. These include:

- City expenses exceeded revenues in eight of the last 10 years. In addition, a shrinking percentage of property tax revenues is available to the General Fund versus funds for other City obligations.
- City net assets continue to lose ground due to growing liabilities and funding gaps in infrastructure maintenance.

Addressing these issues is difficult, but would benefit the City's long-term financial position.

To improve the City's long-term financial health, we recommend that the Mayor require the Office of Management and Finance (OMF) to provide Council with an annual analysis of how the City's long-term financial position could be strengthened. We further recommend this be an annual presentation to the Council after the completion of the external financial audit, with analysis that includes:

- Development of benchmarks to measure, track, and maintain a strong financial position into the future.
- Evaluation of the contributing factors to the decline in net assets and recommendations from OMF on actions to mitigate the decline.

SCOPE AND METHODOLOGY

WHY WE DO A FISCAL SUSTAINABILITY REPORT

Why we do a fiscal sustainability report

This report provides residents and public officials with information on the City of Portland's financial health. While useful information is presented in various City documents, such as the Comprehensive Annual Financial Report (CAFR) and the Adopted Budget, this report is intended to provide financial and demographic information so it can be read and understood by a wide audience. In presenting the measures, we identify both favorable and unfavorable trends in City finances at a high level, and we make recommendations where needed.

The data generally covers a 10-year period, from Fiscal Year 2002-03 (FY 2003) through 2011-12 (FY 2012). City fiscal years run from July 1 to June 30. We also present liability information for the City. In some cases, such as for pension and post-employment benefit liabilities, these are actuarial calculations that represent the present value of costs projected into the future. For example, we present estimates of future spending for the City's Fire and Police Disability and Retirement System, as prepared by their actuaries.

What is fiscal sustainability?

There is currently no universally accepted definition of fiscal sustainability. According to the Governmental Accounting Standards Board (GASB), the term is tied with the idea of inter-generational equity or fairness, which considers the degree to which future generations of taxpayers will have to address the fiscal consequences of current policies. GASB's tentative definition is:

> *Fiscal sustainability is a government's ability and willingness to generate inflows of resources necessary to honor current service commitments and to meet financial obligations as they come due, without transferring financial obligations to future periods that do not result in commensurate benefits.*

A fiscally sustainable city can meet its financial obligations and support public services on an ongoing basis. It can address the effects of fiscal interdependency between governments, withstand economic disruptions, and respond to changes in the underlying environment in which a government operates. A financially stable city collects enough revenue to pay its short and long-term bills and to finance major infrastructure needs without shifting disproportionate costs to future generations. In addition, the concept also includes the governmental structure and willingness to make decisions that will keep the government fiscally sound.

We monitor financial condition and fiscal sustainability by reviewing trends in several areas, such as

- Revenues and expenses
- Net assets and liquidity
- Liabilities, such as outstanding debt, pension, and other post-employment benefit liabilities
- Demographics and economy

Monitoring these areas over time enables public officials and residents to access a city's fiscal sustainability and to identify problem areas that may need attention.

Report scope and methodology

The methodology used in this report is based on *Evaluating Financial Condition: a Handbook for Local Government* by the International City/County Management Association. We also reviewed background information on fiscal sustainability from the Governmental Accounting Standards Board.

The report focuses on Citywide finances. It includes the City of Portland's Governmental Activities and Business Activities. In contrast to prior reports, our methodology also now includes the Portland Development Commission as defined by the annual CAFR. The indicators were selected by the Audit Services Division and were not the result of standard-setting bodies.

Information for the report came primarily from the City's independently audited Comprehensive Annual Financial Reports. Other sources, such as interviews with managers and staff at the Office of Management and Finance and the City Budget Office, were also used. The primary sources for the indicators are listed in the following table.

Primary data sources used

Indicators	**Source** (may be used for multiple indicators)
Revenues • City Revenues • Revenues per resident • Revenues by source • Property Tax	• Portland Comprehensive Annual Financial Reports (CAFRs): o Government-wide Statement of Net Assets o Combining Statement of Revenues, Expenditures, and Changes in Fund Balance for Non Major Governmental Funds o General Fund Schedule of Revenues and Expenditures o Fire and Police Disability and Retirement Fund Schedule of Revenues and Expenditures
Expense • City Expense • Expense per Resident • Expense by Service Area • City Employees	• Portland CAFRs – Government-Wide Statement of Activities • Portland SAP system • Bureau of Human Resources position management system • Portland Development Commission CAFRs
Financial and Operating Position • City Net Assets • City Liquidity	• Portland CAFRs – government-wide Statement of Net Assets
Debt • City Debt • Debt per Resident • Debt by Type • Urban Renewal Debt • Urban Renewal Debt by URA • Projected Debt Service payments	• Portland CAFRs – Schedule of Bond Principal Transactions • Notes to the Financial Statements • Annual Debt Report
Pension & Liabilities • FPDR Projected Annual Costs • PERS Funded Ratio • PERS Liability • Pension Debt Principal • OPEB Liabilities and Ratios	• FPDR Actuarial Valuation and Levy Adequacy Analysis, Jan. 22, 2013 • Milliman Actuarial Valuation Report for the City of Portland, Sept. 28, 2012 • Portland CAFRs o Schedule of Bond Principal Transactions o Notes to the Financial Statements – Other Post Employment Benefits
Capital Assets • Replacement Value of Capital Assets • Condition of Assets • Funding Gaps	• 2012 Citywide Assets Report
Demographic and Economic • Population • Unemployment • Jobs in Multnomah County • Income per resident • Property Values	• Portland State University Center for Population Research • U.S. Bureau of Labor Statistics • State of Oregon, Department of Employment • U.S. Bureau of Economic Analysis • Multnomah Tax Supervising and Conservation Commission Reports

Indicators	**Source** (may be used for multiple indicators)
Other City Comparisons (6-City Averages) • Revenues • Revenues per Resident • Revenues by Source • Expenses • Expenses per Resident • Expense by Service Area • Debt • Debt per Resident • Net assets	• City CAFRs - Charlotte, NC; Cincinnati, OH; Denver, CO; Kansas City, MO; Sacramento, CA; Seattle, WA; Portland, OR o Government-wide Statement of Activities o Ratios of Outstanding Debt by Type • U.S. Census Bureau • U.S. Bureau of Economic Analysis • California Dept. of Finance

In order to account for inflation and unless noted otherwise, we expressed most financial data in constant dollars. We adjusted dollar amounts for each prior year to equal the purchasing power in FY 2011-2012. We used the Portland-Salem Consumer Price Index for All Urban Consumers, as reported by the Bureau of Labor Statistics, U.S. Department of Labor. Unless otherwise stated, financial data are based on the City's fiscal year. In many cases numbers are rounded for ease of use and reporting.

We reviewed information for reasonableness and consistency. We questioned or researched data that was not reasonable or needed additional explanation. We did not, however, audit the accuracy of source documents or the reliability of the data in computer-based systems. As nearly all financial information presented is from the City's CAFRs, we relied on the work performed by the City's external financial auditors.

We chose comparison cities due to their similar population size and government services provided. These are the same jurisdictions used in various audit reports.

Our review of data was not intended to give absolute assurance that all information was free from error. Rather, our intent was to provide reasonable assurance that the reported information presented a fair picture of the City's financial health. In addition, while the report offers financial highlights, it does not thoroughly determine the reasons for negative or positive performance. More analysis may be needed to provide such explanations.

WHY WE DO A FISCAL SUSTAINABILITY REPORT

This report was independently developed by the Office of the City Auditor and is intended for the general public as a high-level report. This report is the result of a performance audit, and was not part of the City's annual financial audit on the City's financial statements. Expressions of opinion in the report are not intended to guide prospective investors in securities offered by the City and no decision to invest in such securities should be made without referencing the City's audited CAFRs and official disclosure documents relating to a specific security.

For more information on the City's finances please visit the following websites:

City of Portland Comprehensive Annual Financial Reports and Annual Debt Reports
http://www.portlandoregon.gov/bfs/

City of Portland Adopted Budgets
http://www.portlandoregon.gov/cbo/

Fire and Police Disability and Retirement Fund Actuarial Valuations
http://www.portlandonline.com/fpdr

Multnomah County local government budgets, indebtedness, property taxes and other financial information
http://tsccmultco.com/

City of Portland Citywide Assets Reports
http://www.portlandoregon.gov/bps

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

RESPONSES TO THE REPORT

Office of Mayor Charlie Hales
City of Portland

June 12, 2013

Dear Auditor Griffin-Valade,

I have reviewed your audit entitled "Portland's Fiscal Sustainability and Financial Condition." Thank you for your staff's work completing its biannual report on this important topic.

The strength and resiliency of the City's financial condition now and in the future is essential to the success of Portland. It ensures that we can continue to provide high-quality City services and maintain and improve our infrastructure. I am proud of the City's Aaa bond rating which it has merited for years, even in the face of the Great Recession and other economic challenges. The City Council and bureaus take very seriously their responsibility as fiscal stewards and the City's financial, economic and budgeting policies reflect this commitment.

I fully support the audit recommendation that Council direct the Office of Management and Finance to prepare an annual analysis of the means by which the City can strengthen its long-term financial position. I will work with my Council colleagues, and with Jack D. Graham, Chief Administrative Officer and director of OMF, and other bureau directors to ensure that such an analysis becomes a reality.

Thank you.

Sincerely,

Mayor Charlie Hales
City of Portland

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CITY OF PORTLAND

OFFICE OF MANAGEMENT AND FINANCE

MEMORANDUM

DATE: June 12, 2013

TO: LaVonne Griffin-Valade, Auditor

CC: Drummond Kahn, Audit Services
Kristine Adams-Wannberg, Audit Services

FROM: Jack D. Graham, Chief Administrative Officer

SUBJECT: 2013 Fiscal Sustainability and Financial Condition Audit

Thank you for the opportunity to review and comment on the 2013 "Portland's Fiscal Sustainability and Financial Condition" audit.

The Office of Management and Finance (OMF) is proud of the City's ability to manage through the recent financial recession and the continued strength of the City's fiscal condition, and credits the prudent fiscal policies and best practices employed by City Council, OMF and City bureaus. OMF concurs with the audit's recommendation that OMF should provide Council with an annual analysis and recommendations on how the City's long-term financial position can be strengthened. Clearly, such an analysis will require engagement of other key bureaus, including the City Budget Office. OMF will be more than pleased to lead such an effort.

OMF agrees that the fiscal challenges facing the City are considerable, including increasing pension liabilities and limited investment in infrastructure maintenance and improvements. We will continue to work with City Council and stakeholders to identify solutions and opportunities to put the City in the best position possible.

We will also continue to communicate and educate the public and professionals alike as to the unique nature of the Fire and Police Disability and Retirement Fund ("FPDR"). While at first glance FPDR can appear as an enormous unfunded liability of the City, the FPDR has a dedicated source of revenue: its voter-approved property tax levy. Per accounting practice, the City cannot "recognize" this revenue, but the levy does in fact provide a reliable and adequate funding source for the annual liabilities of the FPDR system. Importantly, the City Council and voters have recently authorized changes that will additionally decrease the future costs of FPDR.

As you have indicated, the performance audit is intended for the general public. OMF recognizes the difficulty of conveying complex financial information in a simple, easy-to-read format without a loss of accuracy and context. OMF prepares and discloses extensive financial information to potential investors in the City's bonds and produces an Annual Debt Report that provides detail on the City's outstanding debt obligations. We appreciate the prominent positioning of the disclaimer statement in the audit report, so that a reader can understand the purpose and limitations of the performance audit.

Finally, OMF appreciates the addition of comparative information that enhances a reader's ability to understand the broader context within which the City operates. The City's unique form of government, our Aaa bond rating, and the uniqueness of FPDR, as well as other differences highlighted in the audit, make "apples to apples" comparisons between Portland and other cities very challenging. OMF looks forward to working with Audit Services staff to identify and refine the list of municipalities that can be used as "comparables" in future reports and analyses of the City's fiscal sustainability and financial condition.

Thank you for the opportunity to provide input during the development of the audit and the opportunity to review and comment on the final report.

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Portland's Fiscal Sustainability and Financial Condition: Long-term financial position needs attention

Report #443, June 2013

Audit Team: Kristine Adams-Wannberg
Kari Guy

LaVonne Griffin-Valade, City Auditor
Drummond Kahn, Director of Audit Services

Other recent audit reports:

Portland Development Commission: Records management systems in place, but support and direction needed (#442, April 2013)

Public Safety Systems Revitalization Program: Management problems impact cost and schedule goals (#422, April 2013)

Urban Services Policy and Resolution A: Core City services not articulated; 30-year-old commitments obsolete (#433, March 2013)