METROPOLITAN EXPOSITION RECREATION COMMISSION

Resolution No. 11-05

Approving the Metropolitan Exposition Recreation Commission ("MERC") 2011-2012 Budget, the MERC Reserve Policy, Rental Rate increases for the Portland Center for the Performing Arts ("PCPA") and the Portland Metropolitan Exposition Center ("Expo") for FY 2011-12, Re-Designation of the Expo Center Phase Three Expo Master Plan User Fee and recommending the payment of the Oregon Convention Center ("OCC") Street Car LID through financing by Metro.

WHEREAS, pursuant to Section 6.01.50 of the Metro Code, MERC must prepare and approve a budget by resolution and;

WHEREAS, the MERC Budget Committee has met in public meetings for the purpose of creating the MERC 2011-2012 budget and recommends approval of the budget attached as Exhibit A to this Resolution and;

WHEREAS, the MERC Budget Committee has reviewed the MERC Reserve Policy attached as Exhibit B to this Resolution and recommends its approval to the Commission and;

WHEREAS, the MERC Budget Committee has included rental rate increases for the PCPA and the Expo in the MERC 2011-2012 budget and recommends the increases attached as Exhibit C, and;

WHEREAS, the MERC Budget Committee as part of the budget process reviewed the user fees for the Expo and recommends the user fee designated for Phase III construction at the Expo be used for operations, see Exhibit D, and that the existing reserve for Phase III will become part of the new Capital/Business Strategy Reserve pursuant to new MERC Reserve Policy; and

WHEREAS, the MERC Budget Committee recommends that OCC finance the Street Car LID assessment and work with the Metro Council on financing options.

BE IT THEREFORE RESOLVED, that the Metropolitan Exposition Recreation Commission:

1. Approves the MERC fiscal year 2011-2012 budget attached as Exhibit A and transmits it to the Metro Chief Operating Officer for submission to the Metro Council for inclusion in the Metro budget for the fiscal year 2011-2012;
2. Approves the MERC Reserve Policy attached as Exhibit B;
3. Approves the rental rate increases for the PCPA and the Expo for FY 11-12 in accordance with Exhibit C;
4. Approves the re-designation of the Expo Center Phase III construction user fee for operations, see Exhibit D, and making the existing reserve part of the new Capital/Business Strategy Reserve pursuant to the new MERC Reserve Policy; and

5. Recommends that OCC finance the Street Car LID assessment and directs the Metro Chief Operating Officer to work with the Metro Council on financing options.

Passed by the Commission on March 2, 2011.

Chair

Secretary/Treasurer

Approved as to Form:
Daniel B. Cooper, Metro Attorney

By:
Nathan A. Schwartz Sykes, Senior Attorney

MERC Staff Report

Agenda Item/Issue: Approving the Metropolitan Exposition Recreation Commission ("MERC") 2011-2012 Budget, the MERC Reserve Policy, Rental Rate increases for the Portland Center for the Performing Arts ("PCPA") and the Portland Metropolitan Exposition Center ("Expo") for FY 2011-12, Re-Designation of the Expo Center Phase Three Expo Master Plan User Fee and recommending the payment of the Oregon Convention Center ("OCC") Street Car LID through financing by Metro.

Resolution No.: 11-05

Presented By: Judie Hammerstad
Teri Dresler
Cynthia Hill

Date: March 2, 2011

Background and Analysis:

Approval of Resolution 11-05 would implement the following actions:

1. Approves the MERC fiscal year 2011-2012 budget attached as Exhibit A and transmits it to the Metro Chief Operating Officer for submission to the Metro Council for inclusion in the Metro budget for the fiscal year 2011-2012;
2. Approves the MERC Reserve Policy attached as Exhibit B;
3. Approves the rental rate increases for the PCPA and the Expo for FY 11-12 in accordance with Exhibit C;
4. Approves the re-designation of the Expo Center Phase III construction user fee for operations, see Exhibit D, and making the existing reserve part of the new Capital/Business Strategy Reserve pursuant to the new MERC Reserve Policy. The user fees collected annually range from $150 thousand to $200 thousand. The accumulated balance in the Reserve for Phase 3 as of June 30, 2010 was $1,166,039. This amount is included in the new Capital/Business Strategy Reserve in the proposed budget.
5. Recommends that OCC finance the Street Car LID assessment and directs the Metro Chief Operating Officer to work with the Metro Council on financing options. The OCC assessment for Eastside Streetcar Local Improvement District (LID) is $2 million. The current estimate for completion of the project is late 2011-12 or early 2012-13, which is when the assessment will occur.

The Budget Committee, consisting of MERC Commissioners Hammerstad (Chair), Haruyama and Erickson met three times to review the budget in detail and the recommended Reserve Policy.

"Exhibit A" includes a letter from Judie Hammerstad, MERC Commissioner and Teri Dresler, Visitor Venues General Manager, describing the business outlook and the major issues and challenges we faced in the development of the FY 2011-12 proposed budget.

Fiscal Impact:

Total Revenues and Transfers $43,289,300
Total Expenditures $ 42,218,999
Fund Equity Transfers $3,158,261
Net Decrease to Fund Balance $2,087,960

Recommendation: The MERC Commission Budget Committee recommends adoption of Resolution 11-05:

1. Approves the MERC fiscal year 2011-2012 budget attached as Exhibit A and transmits it to the Metro Chief Operating Officer for submission to the Metro Council for inclusion in the Metro budget for the fiscal year 2011-2012;
2. Approves the MERC Reserve Policy attached as Exhibit B;
3. Approves the rental rate increases for the PCPA and the Expo in accordance with Exhibit C;
4. Approves the re-designation of the Expo Center Phase III construction user fee for operations, see Exhibit D, and making the existing reserve part of the new Capital/Business Strategy Reserve pursuant to the new MERC Reserve Policy; and
5. Recommends that OCC finance the Street Car LID assessment and directs the Metro Chief Operating Officer to work with the Metro Council on financing options.



600 NE Grand Ave.
Portland, OR 97232
503-797-1780

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EXHIBIT A to Resolution 11-05

To: MERC Commission

From: Judie Hammerstad, Budget Committee Chair
Teri Dresler, General Manager Visitor Venues

Date: March 2, 2011

Subject: Transmittal of Proposed FY 2011 – 12 MERC Budget

The proposed FY 2011 – 12 MERC budget is attached to this memorandum as prepared and recommended by the MERC Budget Committee. The committee met three times and, over the course of these meetings, learned from venue directors the challenges and opportunities each venue faces in the coming year. This background context was essential to the committee's understanding of the expenditure requests and revenue forecasts for each venue.

In addition to preparing the budget recommendation, the committee was tasked with making a recommendation on a reserves policy for MERC. If approved as part of the recommended budget, this new financial policy will continue MERC's practice of sound financial management, creating contingency and renewal and replacement reserves as well as a reserve fund for strategic business initiatives and new capital projects.

Anticipated savings from efficiencies generated as a result of the MERC/Metro Business Practices Study, as well as budget reductions proposed by Metro Chief Operating Officer Michael Jordan, reduced overall costs and contributed to the decrease in overhead costs paid to Metro by the venues.
The committee's recommended budget is being presented to the Commission on March 2, 2011 for approval and then will be forwarded to the Metro Council for its review and approval in a process beginning on April 7, 2011. If the Council proposes amendments to the budget, those will be brought back to the Commission for consideration in April / May.

Economic Climate

- In Fiscal Year 2011 – 12, the Oregon Convention Center's booked business for national conventions reflects the downturn experienced in 2008 – 09 when associations would have typically booked meetings for the 2012 – 13, but either held off or planned smaller, local meetings. Business in the coming year will reflect these decisions through a decrease in national conventions by seven compared to the current year. The OCC sales staff has been challenged with retooling their sales techniques to match these new industry realities. While this team has been successful in booking short-term business that tends to be local or regional by nature, it is the large national convention business that generates the majority of OCC's revenue. Tax revenue from transient lodging taxes is expected to continue its climb back from the low of two years ago. Hotel bookings are up, indicating that the public is starting to travel again for both business and leisure.

- While public shows in FY 2010 – 11 have stabilized a bit for the Portland Expo Center, attendance remains soft. Two show producers intend to add back space in the upcoming year, after scaling down in recent years, in hopes that the public is ready to spend again. We are cautiously optimistic that the worst is over and a slow growth back to our baseline is occurring. The addition of the West Delta Bar & Grill as Expo's only food and beverage location, with seating and tables, has proven to be a very positive revenue addition for its first two months of operation. We look forward to continued growth in revenues from the West Delta Bar & Grill.

- A strong Broadway season is expected again at the Portland Center for Performing Arts with an additional week of Broadway shows on the schedule for the FY 2011 - 12 season. The resident companies are holding their share of the entertainment audience through creative use of highly popular feature artists. This will be the second budget where PCPA has seen a decrease in transient lodging tax revenue due to the limit on increases allowed year over year in the intergovernmental agreement (IGA). When the lodging industry experienced a sharp decrease in 2008 – 09, tax income dropped dramatically, and though recovery has been positive this past year for the lodging industry, PCPA has also begun its recovery , but in a limited manner, due to the terms of the IGA. Overall, PCPA expects a very successful FY 2011 – 12.

Major Budget Impacts for Fiscal Year 2011 – 2012

- Establishing reserve funds as defined in the MERC reserve policy. These funds include a strategic reserve, a contingency reserve, a stabilization reserve, and renewal and replacement reserve. A report on the reserve policy is attached to this packet.

- Venue directors have taken have taken a tough look at their expenditure budgets in light of the anticipated revenue horizon and have made reductions where necessary. One FTE is proposed as a budget reduction. Due to thoughtful management of venue budgets over the past few years, the venues are lean operations without any excess in their budgets.

- The MERC / Metro Business Practices Study recommended outcomes are being implemented fully in the FY 2011 – 12 proposed budget. Impacts to the MERC administration budget reflect a decrease in personal services costs as some staff has been shifted to centralized work groups within Metro. Costs for those staff will be allocated back to the MERC venues. Other impacts to the budget from the implementation of the business study are reflected in reduced materials and services spending realized as the result of more efficient practices agency-wide.

- Metro Chief Operating Officer Michael Jordan has proposed a set of agency-wide budget reductions primarily related to the costs associated with employees. These proposed reductions have assisted greatly in arriving at a balanced budget proposal.

- The budget includes a $3,067,917 for the national sales contract with Travel Portland. This amount reflects a 1% increase from the FY 2010 – 11 contract.

Policy considerations included in the Fiscal Year 2001 – 2012 Proposed Budget

- Approval of the MERC Reserve Policy.
- Approval of rental rate increases for PCPA and Expo.
- Approval to re-designate the Expo Phase III construction user fee for operations, thereby making the existing reserve part of the new Capital/Business Strategy Reserve pursuant to the new MERC Reserve Policy.
- Recommendation that OCC staff pursue an inter-agency financial agreement to finance the Street Car LID assessment of $2 million anticipated in late fall 2012.

The Budget Committee is recommending that the Commission address two key budget policy issues in the next year:

- An examination of the financial operating model for Expo Center and the Oregon Convention Center needs to be conducted with an eye to the long-term financial sustainability of the current business models (with or without a convention center hotel).

- A long-term solution to the budget gap created by the reduction in transient lodging taxes received by PCPA needs to be found.

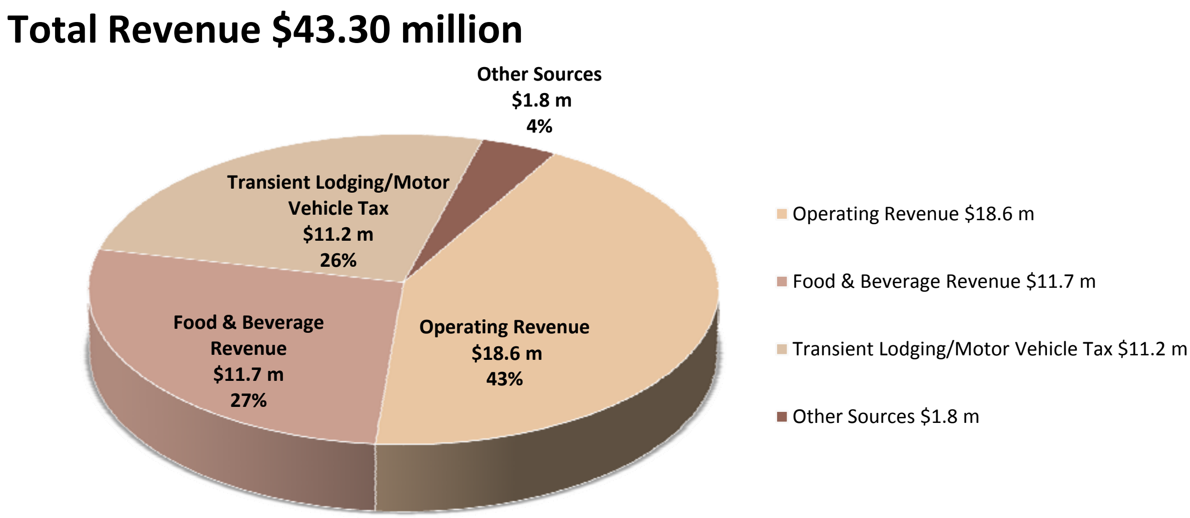
We would like to thank the Metro Finance and Regulatory Services staff who researched and prepared the recommendations for the proposed MERC reserve policy. Thanks go to Cynthia Hill, MERC budget and finance manager who kept us all on track with packets of information for each meeting and countless revisions to the ever changing balances on spreadsheets. A big thank you to the three venue directors who dove in to help present a balanced budget and respond to a multitude of requests for information about their business units. The proposed budget and reserve policy provides the venues with the financial resources needed to achieve excellence in customer service while maintaining the venues in a manner that delivers on our promise to the region to operate world-class facilities.

And finally, thank you to the MERC Budget Committee members, Commissioners Cynthia Haruyama and Chris Erickson for their diligence in reading the reams of financial information and their engaged participation in the Budget Committee.

Overview

FY 2011-12 Budget

Included in this exhibit is a high level overview of revenues, expenditures, and the fund balance.



Revenue

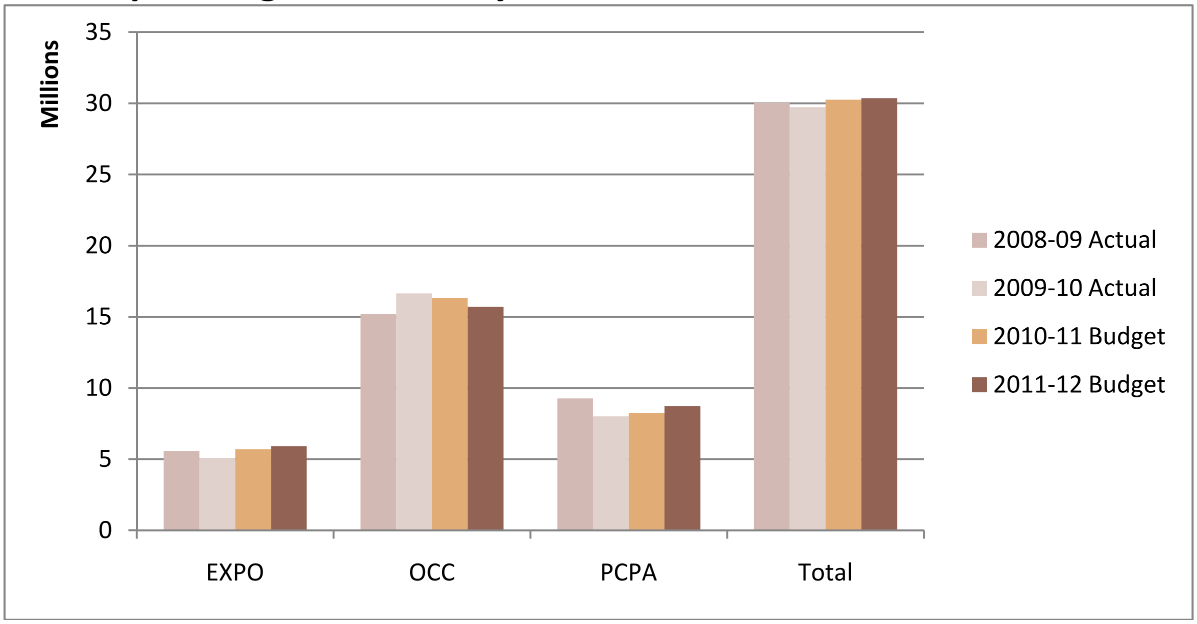
Overall operating Revenue, excluding Food & Beverage, is $18 million, a slight increase over the FY 2010-11 Budget. Operating revenue includes the cost of renting facilities, equipment and providing services to clients and attendees, and the revenue generated by business operations.

- Expo $3.9 million operating revenue is 2.9% greater than FY 2010-11 budget
  - Attendance is conservatively projected to be flat.
- OCC $7.7 million operating revenue, 2.43% less than FY 2010-11 budget
  - Thirty national/regional conventions are booked in FY 2011-12 reflecting a decrease of seven.
- PCPA $7.0 million operating revenue is 3.8% greater than FY 2010-11 budget
  - Strong Broadway season with 12.5 weeks compared to 13 weeks in FY 2010-11 with four of those weeks being a blockbuster and seven weeks being high grossing with full capacity attendance.

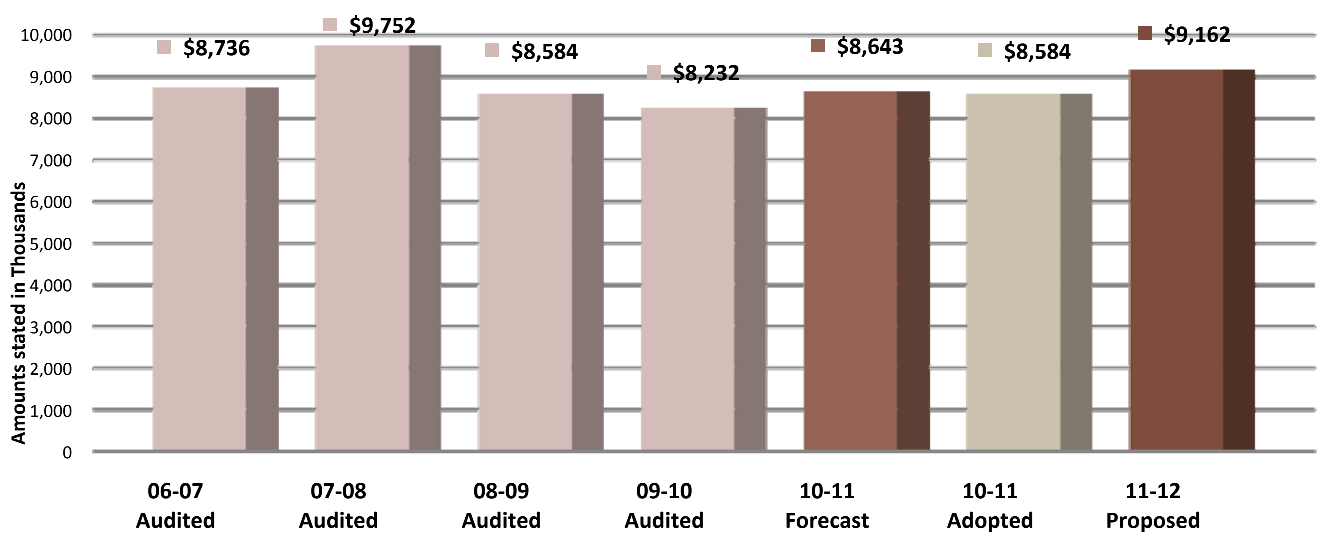
Food & Beverage Revenues are flat compared to FY 2010-11 budgets at $11.7 million

- EXPO anticipates food and beverage revenue will improve by $100 thousand over that budgeted in FY 11 with a full year operation of the West Delta Bar & Grill.
- OCC budget reflects a decrease in food and beverage revenues with fewer conventions.
- PCPA revenue increases due to the strong Broadway Series.

Total Operating Revenues by Venue (including Food & Beverage)



Transient Lodging Tax (Excise 3%)

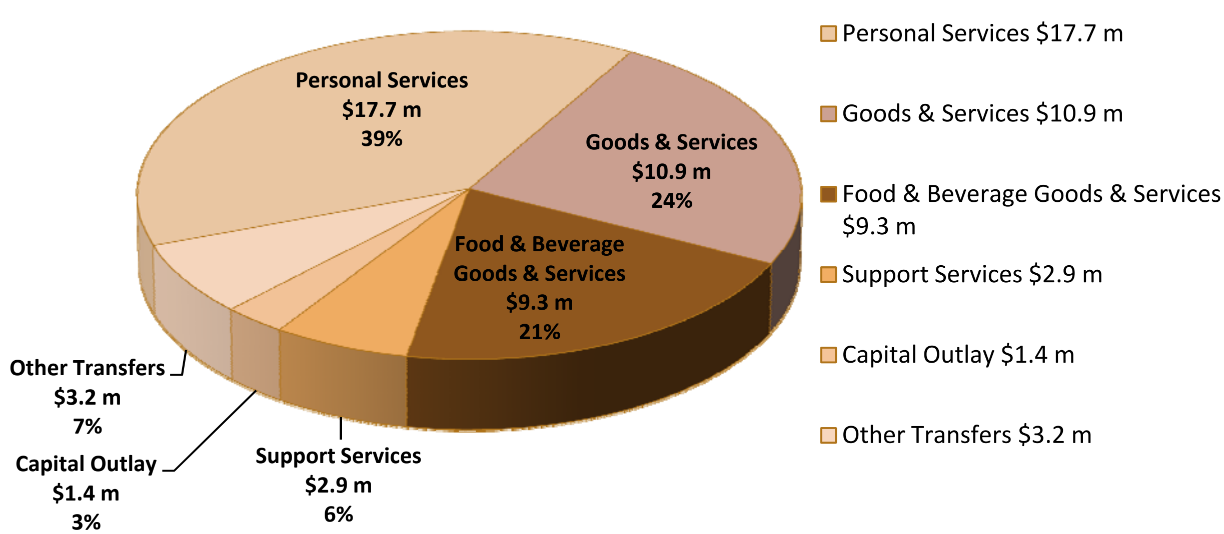


Non - Operating Revenues

- Transient Lodging and Motor Vehicle Tax budget totals $11.2 million. Recent lodging industry occupancy and room rate data show significant growth in FY 2010-11.
- PCPA has experienced a reduced allocation as the tax code requires OCC to receive the greater of CPI or the increase in tax receipts. The PCPA base is now $925 thousand compared to $1.2 million in previous years.
- Transient Lodging Tax (TLT) 3% Excise Tax budgeted to increase 6% at $9.2 million.
  - OCC $8.3 million
  - PCPA $ .9 million

- Visitor Development Trust Account (VDI Buckets) includes operational support for OCC and PCPA and enhanced marketing support passed through to Travel Portland. Expo Center does not receive operational support from the intergovernmental agreement.
    - VDI Bucket 4 – The OCC request is $960,000 which includes the following three components
        - Travel Portland VDI Single Hotel Marketing Portland as a destination is $160 thousand approved June 6, 2008
        - Travel Portland marketing alternatives to a headquarter hotel is $250 thousand
        - OCC support is $550 thousand
    - VDI Bucket 5 - Enhanced marketing $425 thousand (Pass through to Travel Portland)
    - VDI Bucket 8 - PCPA operational support- $607 thousand
- City of Portland Contribution of $784 thousand to PCPA increases by CPI.
    -
- Investment Earnings are estimated at .50% by Metro's Investment Manager
- Interfund Transfers In
    - $480 thousand incoming transfer from Metro Tourism Opportunity and Competitiveness Account (MTOCA). Four proposed capital projects included in the OCC Five Year Capital Plan are proposed to be funded by this source.

Total Expenditures $45.4 million



Expenditures

Personal Services

- The MERC Fund includes 186.2 Full time employees and approximately 300 part time employees.
- PCPA - Increase part time Marketing & Promotions Coordinator II position to full-time. The increased cost is $25,879

- PCPA - Add a full-time Utility Lead – to assume 40 hours previously worked by part-time utility workers $28,183
- PCPA - Re-organization within the operations department resulted in the elimination of 1.00 FTE Maintenance and Construction Supervisor for a savings of $93,606
- Administration – changes are described below in the MERC Administration section.

Goods & Services

- Project carry-over of $100 thousand for building maintenance repair to preserve the parapet exterior on the Arlene Schnitzer Concert Hall. An additional $70 thousand is included to fund unanticipated costs associated with this project.
- ARAMARK food & beverage expenses $9.3 million for the consolidated MERC Fund
- National Marketing Contract with Travel Portland remains flat at $3.1 million

MERC Administration and Metro Support Indirect & Direct Support

- MERC Administration decrease 23%
    - This total is allocated to individual venues using FY 2010-11 personal services as the factor.
    - The MERC / Metro Business Practices Study recommended outcomes are implemented in the FY 2011–12 proposed budget. The result is a decrease of 4.8 FTE.
- Metro Indirect Cost/Support Services transfer is 8.61% greater than current year.
    - This total is allocated to individual venues using FY 2010-11 personal services as the factor.
- Metro Risk Management Services
    - Includes property Insurance, liability and workers' compensation
- Direct transfer of $78 thousand to the Metro Office of the COO for 50% of Policy Advisor
    - This position provides direct support to the MERC Venues on major projects

Fund Equity Transfers Transfers

Fund Equity Transfers & Debt includes transfers of resources to other funds. The current budget includes the transfer of the accumulated PERS Reserve to the General Fund, the transfer to the Bond fund for the Expo Debt, a transfer from PCPA to the Metro Renewal & Replacement Fund.

- Transfer the accumulated PERS Reserve $1.9 million to the Metro General Fund
- PERS bond recovery: Metro makes an annual debt service payment for limited tax pension bonds sold in 2005 to address the PERS unfunded actuarial liability. All Metro departments have been paying approximately 3 percent of its personal services costs as an ongoing expense to fund the debt payment. To mitigate the significant increase in PERS rates beginning July 1, 2011, Metro will use accumulated PERS reserves to fund the debt payment. This saves MERC about $358,918 in FY 2011-12.
- Debt Service transfer to Metro Bond Fund
    - EXPO transfers the annual bond payment for Hall D Replacement ($1.2 million) funded from operating revenue and unrestricted fund balance
- Transfer $10.8 thousand to Metro general fund renewal & replacement to replace time clocks at PCPA.

Five Year Capital Plan

- The five year Capital plan includes all projects and capital purchases over $10 thousand
- The chart below identifies the FY 2011-12 projects $100 thousand and greater which are included in the Metro Capital Improvement Plan.

Description	*Project Type*	*2011-12*
OCC - Electrical Sub Metering	New Capital/Sustainability	200,000
OCC - Permanent Automatic AV Screens in all Meeting Rooms	Revenue Generating	195,000
PCPA - Arlene Schnitzer Concert Hall & Hatfield HVAC Controls Replacemer	Renewal & Replacement	130,000
Expo - Structural Issue Hall E	Renewal & Replacement	100,000
Total Visitor Venues (MERC Fund)		***625,000***

Fund Balance

The proposed budget includes the implementation of the Reserve Policy. The Final Report and Recommendations are included in "Exhibit B". The chart below reflects a summary of the fund balance and reserves by venue.

Summary of FY 2011-12 Fund Balances and Allocations to Reserves

	Expo	OCC	PCPA	Admin	MERC
Projected FY 2011-12 Balances**	**$4,427,328**	**$7,779,594**	**$7,891,570**	**$827,751**	**$20,926,243**
Reserve Targets					
Restricted					
Expo Phase 3	-	-	-	-	-
PERS	-	-	-	-	-
Subtotal	**-**	**-**	**-**	**-**	**-**
Contingency					
Working Capital	-	-	-	-	-
Operating Contingency	364,000	1,540,000	300,000	95,335	2,299,335
Stabilization	186,000	260,000	174,500	-	620,500
Subtotal	**550,000**	**1,800,000**	**474,500**	**95,335**	**2,919,835**
Accumulation					
Renewal & Replacement	925,000	5,325,779	5,595,000	732,416	12,578,195
New Capital / Business Strategy**	2,952,328	653,815	1,822,070	-	5,428,213
Subtotal	**3,877,328**	**5,979,594**	**7,417,070**	**732,416**	**18,006,408**
Sum of Reserve Targets	**$4,427,328**	**$7,779,594**	**$7,891,570**	**$827,751**	**$20,926,243**

Note

These figures reflect proposed uses of fund balances in the FY 2011-12 budget as of March 2, 2011 The new capital and business strategy figure is the balance remaining after funding other reserves.

Use of Fund Balance Included in the FY 2011-12 Budget

The transfer of $1.9 million PERS Reserve accounts for a major portion of the decrease to fund balance. Use of fund balance by venues is listed below:

- Expo Center

Net of Operations	$1,251,207
Net Fund Equity Transfers & Debt	(1,365,096)
Net Capital – Fund balance – New Capital/Business Strategy Reserve	(275,000)
Net Increase/Decrease Fund Balance	(388,889)

- Oregon Convention Center

Net of Operations	$321,988
Net Fund Equity Transfers & Debt	(1,004,018)
Net Capital – Projects funded from the annual MTOCA Transfer from Metro General Fund and accumulated fund balance designated for capital from PY Transient Lodging Tax Receipts	(246,000)
Net Increase/Decrease Fund Balance	(928,030)

- Portland Center for Performing Arts

Net of Operations	$18.106
Net Fund Equity Transfers & Debt	(614,408)
Net Capital – Projects funded from PCPA Foundation Donation	n/a
Net Increase/Decrease Fund Balance	(596,302)

600 NE Grand Ave.
Portland, OR 97232
503-797-1780
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Date: March 2, 2011

To: MERC Commission

From: Judie Hammerstad, Chair
MERC Budget Committee

Subject: Approval of Reserves Study and Recommendation

The Budget Committee, as part of its FY 2011-12 budget assignment, completed its review of the MERC Reserve report and recommends that the MERC Commission approve the designation of specific types of reserves, effective immediately. The FY 2011-12 budget proposal implements these reserves at the amounts shown on the attached table. Each year the budget will be prepared using these categories, adjusting as needed to meet the target required.

By adopting these categories and the FY 2011-12 budget proposal, we are confirming our good instincts about the strategic fund balance, now defined by specific categories with rigorous analysis. The contingency is calculated to withstand a major economic event every ten years. The contingency and stabilization reserve together are sized to withstand a major economic event lasting more than one year, unfortunately something we are familiar with. The renewal and replacement needs of all three facilities are funded for the next five years with modest and predictable annual contributions, based on the initial plans provided by the venue directors. Over the next three years the venues will validate and improve these plans to extend the funding strategy for the longer term. We are recommending that the accumulated reserves for Expo Phase 3 be included as part of the new capital/business strategy reserve. The surcharge will continue to be collected and available for Expo Center operations.

The chart below summarizes the principal findings by reserve type; the attached table displays how the reserves are presented in the proposed budget. The full report describes in detail how the targets were developed using historical data.

RECOMMENDATION SUMMARY

Designated Reserve Type	Description	Significant Findings
Restricted	Established to satisfy external obligations. currently: Expo Phase 3 PERS Reserves	Expo Phase 3 can be classified for capital or business strategy. PERS reserve will follow Metro direction; current direction is to use accumulated reserves to relieve annual PERS bond payments.
Working Capital	Provides liquidity to cover timing differences between payables and receipts.	Not required. Utilize Metro's resources for working capital rather than setting aside a portion of the MERC fund balance for this purpose. The cost of this strategy is minimal, and frees up $3.95 million for renewal and replacement.
Contingency	Annual operating "insurance"; provides funds to cover unexpected, within-year revenue shortfalls or cost spikes; there if you need it, but you don't plan to spend from it. There is a direct trade-off between risk and the size of the operating contingency: the smaller the reserve, the higher the risk and vice versa.	Consistent with current contingency plan. Sized for a "10 year event": there is a chance the reserve would be completely exhausted once every decade. Appropriated and available for spending during the year by budget amendment; requires both resolution of Commission and Metro ordinance.
Stabilization	The source of funds to replenish the operating contingency the year following a revenue or cost shock, thereby avoiding the need to dip into the next year's budget to fund the operating contingency.	The operating contingency and stabilization reserve together are sized for a major economic disruption spread over more than one year. Recommended because the effects of such shocks are not usually confined to one year for MERC venues. Unappropriated and available only in the succeeding budget year.
Renewal and Replacement	Supports the existing asset base; steady annual deposits to smooth cycles of higher and lower spending. Accumulation reserve, works like savings account, building up with the	Based on 10-year proforma with 5-year focus (5-year CIP adopted annually). Annual outlays are based on schedules prepared by each venue which will be refined and adjusted over next three years as experience grows. Based on current schedules, additional resources will

Designated Reserve Type	Description	Significant Findings
	intention of spending. The greater the initial designation, the smaller the annual contribution and vice versa.	be needed after Year 5. OCC: TLT capital funds are available for R&R or new capital PCPA: does not consider Friends of PCPA resources which may be source of some part of annual contribution.
New Capital/ Business Strategy	New capital: accumulation reserve; funding source for new capital acquisition; an alternative to borrowing. Uses of funds are governed in principle by a capital plan. Business Strategy: non-recurring costs of pursuing business Strategies, Continuity, and Opportunities Uses of funds are guided in principle by a business or strategic plan.	Overlaps the concept of the "strategic fund balance In this study, the amount available for these reserves is the fund balance that remains after all of the other reserves have been funded. It was outside the scope of this study to determine if this amount is adequate; that finding could emerge in conjunction with development of a business or strategic plan. Recommend that the amount be appropriated and available for spending during the year by budget amendment; requires both resolution of Commission and Metro ordinance.

Attachments: Reserve designation by Venue
Reserves Study Report

Report and Recommendations on MERC Financial Reserves

Final Report

March 2, 2011

Prepared For

Michael Jordan, Chief Operating Officer, Metro

MERC Commission

Elisa Dozono, Chair
Ray Leary, Vice Chair
Judie Hammerstad, Secretary Treasurer
Chris Erickson
Terry Goldman
Cynthia Haruyama
Karis Stoudamire-Phillips

Project Team

Margo Norton, Finance and Regulatory Services Director
Cynthia Hill, MERC Budget Manager
Douglas Anderson, Policy and Compliance Manager, FRS

The project team extends its thanks to the MERC executive team for its assistance without which this study would not have been possible:

Teri Dresler, General Manager, Metro Visitor Venues
Chris Bailey, Executive Director, Portland Expo Center
Jeff Blosser, Executive Director, Oregon Convention Center
Robyn Williams, Executive Director, Portland Center for the Performing Arts
Lisa Brown, Executive Assistant

Introduction

The objectives of this study are to identify the types of reserves that are appropriate for MERC, and to analyze independently the funding needs (targets) for each of those reserves.

This information will assist decision makers in allocating the current fund balance among specific and targeted business needs. It will also help MERC assess the adequacy of its fund balance, and provide planning targets for the future – especially in cases where a particular reserve falls short of its funding goals.

As an immediate benefit, this study will provide decision makers with a better sense of options, priorities and risks when considering drawing on the fund balance for various uses. In particular, the results of this study should help inform development of budgets, both for FY 2011-12 and in the future.

This study can also help inform planning and management of decisions and activities that affect, or are affected by, the reserves – such as the projects and schedules for renewal and replacement of existing assets.

The results of this study should also increase the transparency of MERC's financial condition and provide MERC and Metro with a firmer foundation for explaining or discussing current and future needs with stakeholders and decision makers inside and outside Metro.

Contents

One

Reserve Concepts and Appropriate Reserves for MERC

"Reserves" are the portions of the MERC Fund balance that are set aside for specific, or "designated" purposes. Any portion of the fund balance that is not reserved is "undesignated."

At the most basic level, reserves serve only one purpose: to support the business objectives of the organization. It is good practice to identify the reserves that are needed for each organization, quantify the target size of each reserve, and to adopt policies governing funding, uses, and priorities. The policies and targets should reflect the characteristics of the operating and capital budgets, the organization's appetite for risk, opportunity costs, management objectives, and the strategic direction of the organization.

There are three classes of reserves that provide an organizing framework for any discussion of reserves: restricted, contingency and accumulation. Below, the specific reserves recommended for MERC are described under each class.

Restricted Reserves are set aside to satisfy external obligations such as law or covenant. These same obligations usually govern the sources and uses of funds, and often specify the size of the reserve.

For MERC the project team initially defined the following as restricted:

- Expo Phase 3
- PERS

Contingency Reserves are like insurance: they are there if needed, but no expenditures are planned from them.

For MERC the project team recommends the following contingencies.

- Working Capital: provides liquidity to cover time delays between payables and receipts.
- Operating Contingency: covers the operating budget against cost spikes and revenue slumps.
- Stabilization Reserve *(new concept for MERC)*: backs up the operating contingency.

Accumulation Reserves are financial management tools that act like savings accounts: small periodic deposits grow (that is, accumulate) to an amount sufficient to cover planned future expenditures.

For MERC the project team recommends the following accumulators.

- Renewal & Replacement: the source of funds for renewal and replacement capital outlay.
- New Capital: the source of funds for new capital acquisition.
- Business Strategy: a source of funds for non-recurring costs of pursuing business strategies, continuity and opportunities. *(Overlaps MERC's current "Strategic Fund Balance" concept.)*

Two

Summary of Findings and Results

Table 1 shows the projected FY 2011-12 balances and target funding levels recommended for the contingency reserves and renewal and replacement at each venue. The figures shown for new capital and business strategy are the balances that remain after the other reserves have been fully funded. The new capital and business strategy amounts are not necessarily funding targets, as explained in the text following the table.

Table 1
Recommended Reserve Targets
FY 2011-12

	Expo	OCC	PCPA	Admin	MERC Fund
FY 2011-12 Balances	**$4,427,328**	**$7,779,594**	**$7,891,570**	**$827,751**	**$20,926,243**
Contingency					
Working Capital	—	—	—	—	—
Operating Contingency	364,000	1,540,000	300,000	95,335	2,299,335
Stabilization	186,000	260,000	174,500	—	620,500
Subtotal	**550,000**	**1,800,000**	**474,500**	**95,335**	**2,919,835**
Accumulation					
Renewal & Replacement	925,000	5,325,779	5,595,000	732,416	12,578,195
New Capital* / Business Strategy*	2,952,328	653,815	1,822,070		5,428,213
Subtotal	**3,877,328**	**5,979,594**	**7,417,070**	**732,416**	**18,006,408**
Sum of Reserve Targets	**$4,427,328**	**$7,779,594**	**$7,891,570**	**$827,751**	**$20,926,243**

*The new capital and business strategy figures are the balances remaining after funding other reserves at the recommended targets.

Overview. The operating contingencies and stabilization reserves together are sized to withstand a combination of cost spikes and revenue slumps that amount to a "twenty year event" spread over two fiscal years. The renewal and replacement reserves, together with annual deposits described later in this report, are sufficient to fund the next five years of known renewal and replacement needs at all three venues. This provides MERC with sufficient time to develop renewal and replacement plans that are financially sustainable in the long run. This study recommends that MERC utilize the resources of Metro for its working capital needs rather than earmark a portion of the MERC Fund balance for this purpose. Accordingly, the working capital reserves are not shown as funded. It was outside the scope of this study to determine targets for the new capital and business strategy reserves, as management considerations and long-term objectives drive those needs more than technical factors. Funding levels for these two reserves could emerge in conjunction with development of a strategic business plan.

From a glance at the table it is clear that the current fund balance is adequate to support all contingency and renewal and replacement accounts at their target levels, subject to the assumptions and limits set forth in this report.

General Comments

- **PERS**. The PERS reserves in all Metro funds including MERC will be centralized in FY 2011-12 to service PERS debt next year and over the near term. Accordingly, the MERC PERS reserves are not shown in Table 1.

- **Operating Contingencies and Stabilization Reserves.** As mentioned above, combined, these accounts are sized to cover a “twenty year event” at each venue. This means, at the recommended levels, there is a chance that these reserves would be *completely exhausted, without relying on any cost management efforts*, once every twenty years. In statistical terms, there is 95 percent confidence that such a reserve will be adequate to cover cost and revenue shocks from year-to-year. Stabilization reserves, which back up the operating contingencies, are a new concept for MERC. These are recommended because cost and revenue shocks are not typically confined to a single year’s impact at MERC. Over time, the size of these contingencies may be adjusted according to experience and decision-makers’ choice between risk and the opportunity cost of holding funds in reserve.

- **Renewal and Replacement Reserves.** The main challenge for renewal and replacement at MERC is the especially heavy series of projects programmed for the next three to four years. The renewal and replacement accounts, together with annual deposits described later in this report, are sufficient to fund the next five years of planned renewal and replacement outlays. It is important that MERC utilize this time to review its asset base and develop renewal and replacement plans that are sustainable in the long run.

- Targets for the **New Capital and Business Strategy Reserves** were not specifically addressed in this study, as funding is driven more by management and strategic considerations than technical factors, and MERC’s capital acquisition and business plans are not sufficiently developed at this time to guide a formal technical analysis. However, by objectively sizing all of the fundamental reserves – working capital, operating contingencies, and renewal and replacement – this study provides MERC with a better handle on the amount of the total fund balance that remains available for new capital and business strategy execution in the near term. It is an open question at this whether these reserves – especially business strategy – can be managed as accumulation reserves (that is, funded by periodic planned deposits), or whether funding would come from operating surpluses when available.

Venue-Specific Comments

Expo

- The fund balance appears adequate to support all reserves as specified in this memo, including a sizeable amount for new capital and business strategy.

- If subsequent review uncovers additional renewal and replacement needs, Expo's fund balance appears able to accommodate an expansion of the reserve.

- The study team found that the original purpose of the Phase 3 reserve overlaps the new capital and business strategy concepts set forth in this report. The study team recommends that MERC review the original objectives and constraints for this reserve to determine if they warrant revision. In Table 1 the Phase 3 Reserve balance is folded into new capital and business strategy line.

- The recommended operating contingency is higher than the largest experience-based operating deficit during the last 15 years at Expo. This is probably a result of aggressive cost management during lean years in the past.

OCC

- While resources are adequate to fully fund the contingencies and the next five years of planned renewal and replacement outlays, the amount remaining for new capital appears too low for an operation having the size and business needs of OCC. From the perspective of this study, funding for new capital is one of the principal challenges facing OCC.

- Because of the heavy renewal and replacement schedule in the next three to four years and the wide variation in subsequent outlays, OCC would benefit from scheduling its renewal and replacement projects more evenly over time. This would allow for a mild reduction in the annual deposit needed to keep project expenditures covered.

PCPA

- The fund balance appears adequate to support all reserves as specified in this report, including an amount for new capital and business strategy.

- The amount of renewal and replacement funding is amplified by the heavy project schedule over the next several years and high variability of outlays after that. As with OCC, PCPA's renewal and replacement *pro forma* would benefit from scheduling projects more evenly over time.

- The recommended operating contingency at PCPA is the only reserve that is smaller than current practice. If decision makers are uncomfortable with the subjective risk of downsizing this reserve, they might note that the recommended operating contingency and stabilization reserve combined are almost exactly the current level of funding.

- Implementation of capital funding management and policies will need to be tailored to the requirements and practices of the Friends. However, this does not affect the underlying design principles for the capital reserves.

Three

Detailed Analysis and Discussion

Restricted Reserves

Funding of the two restricted reserves at MERC – Expo Phase 3 and PERS – depend on year-to-year factors: fee revenue in the case of Expo Phase 3, and personal services costs and budget policies of the Metro Council in the case of PERS. Neither of these reserves have specific targets.

PERS. The Metro Council will consider centralizing all PERS reserves in FY 2011-12. The funds will be used to cover each department's 3 percent payment debt payment next year, and the balance applied to debt service payments in the near future. Accordingly, the PERS reserves will disappear from the MERC Fund after FY 2011-12.

The **Phase 3 Reserve** was established in 2002 by MERC Commission Resolution 02-31, which also authorized a 6 percent user fee on exhibitors. The resolution included the restriction that "all net user fee revenue and expenditures will be identified and accrued for use strictly associated with the Expo Phase 3 construction project." The stated purpose of the Phase 3 Reserve overlaps the new capital and business strategy concepts set forth in this report. The MERC Commission may wish to review this reserve to determine if it still serves the original purpose and whether the funds could be made available for a broader range of capital planning and projects. In this study, the Phase 3 Reserve balance is treated as part of the new capital and business strategy amounts.

Working Capital

Concept. A working capital account is essentially an internal short-term loan fund that provides the liquidity to cover any time lag between receivables and payables. As working capital must be held in cash or cash equivalent form, the opportunity cost (that is, the return on the funds in their most productive alternative use) can be high. Some organizations utilize an external line of credit to satisfy working capital needs. Large organizations usually pool funds from several operating units to take advantage of different patterns of receipts and outlays over the course of the year.

Method and results. MERC's working capital needs are driven entirely by the timing of payables and receivables at each venue, and are shown in Table 2.

Table 2
Working Capital Needs by Venue

Expo	OCC	PCPA	Total
$525,000	$2,330,000	$1.095,000	$3,950,000

Each venue would have to reserve these amounts if working capital were to be managed individually for each venue. If working capital were managed at the fund level, MERC could take advantage of the differences in timing of cash flows among the venues to reduce the reserve by as much as $400,000 from the total above. Pooling would have no effect on the venues' account balances, as each venue would "own" the same amount of working capital at the end of the year as at the beginning.

However, the best option – and the recommendation of this study – would be for MERC to utilize the resources of Metro as a whole for its working capital. The cost to MERC would be trivial – the amount of foregone interest earnings on the amounts that are used for working capital and therefore not available for investment at any given time. This is essentially an interest payment that MERC would incur in any case if it managed the fund itself.

Implementation. All of Metro's various fund balances are already managed centrally, including the MERC Fund, so this recommendation would not entail any change in practice. Rather, it formally identifies an arrangement that provides MERC with a degree of certainty over the use of $3.95 million for purposes other than working capital.

Operating Contingency and Stabilization Reserve

Concept. An operating contingency backs up the annual operating budget. It provides funding to cover unexpected revenue losses or cost spikes. It is like an insurance policy – there if you need it – but you don't *plan* to spend from it. It is not a substitute for operating revenue beyond one or two years. If a change in financial situation persists, then the organization needs to adapt to the new situation; it cannot rely on contingency funds in the long run. With a properly sized and fully funded operating contingency, cost reductions become an optional, not a required, management response to short-term revenue shortfalls and cost spikes.

Because the operating contingency is essentially insurance, the size of the reserve is often described in terms of probabilities and confidence levels. This provides decision makers with explicit measures to balance their tolerance for risk with the opportunity costs of holding the reserve. For example, a risk averse organization might opt for a large reserve. But this comes with a high opportunity cost, measured by the return that can be realized on the funds in the most productive alternative use. There is a direct trade off between risk and opportunity cost when sizing the operating contingency: the smaller the reserve the higher the risk of underinsuring the operating budget, but the lower the opportunity cost. And vice versa for a large reserve.

Design criteria and assumptions. In practice, most organizations respond to unexpected cost spikes or revenue slumps with a combination of draws from contingency and cost management. *A key design criterion for this project is to size the contingencies assuming no reduction of costs in response to a cost or revenue shock*. This will provide MERC with flexibility to determine the appropriate response whenever a cost or revenue shock occurs in the future. If MERC were to establish formal cost management protocols as a matter of policy in partial response to cost or revenue shocks, the contingency targets could be downsized.

A conventional starting point for contingency analysis is to consider reserves that are sized to withstand a 10-year event. That is, there is a chance that the reserve would be *completely exhausted*, without relying on any cost management efforts, once every ten years. In statistical terms, there is 90 percent confidence that such a reserve will be adequate from year-to-year. Based on MERC's operating history this is a reasonable actuarial level. If decision makers decide that the opportunity costs of the resulting reserves are too high or the organization is willing to accept more risk, the reserve can be downsized to reach, say, an 80 or 85 percent confidence level (5- and 7-year events, respectively). Or if the organization is more risk averse, the reserve can be upsized to, say, 95 percent confidence (that is, to withstand a 20-year event).

To provide context for the results and discussion that follow, Table 3 (next page) shows the frequency and magnitude of operating deficits during the last 15 years. An operating deficit is defined as a situation in which current revenue does not fully cover current costs.

Table 3
Historical Operating Deficits by Venue
FY 1995-96 to 2009-10

Venue	Number of Deficits, Last 15 Years	Average Deficit	Largest Deficit Amount	Largest Deficit Year
Expo	5	$205,000	$324,000	2008-09
OCC	6	1,139,000	1,880,000	2001-02
PCPA	3	338,000	905,000	1999-00

Note: historical operating surpluses and deficits have been adjusted to account for controllable and extraordinary one-time events, such as the transfer of $9 million from OCC to Expo in FY 1996-97 and the $5.74 million of VDI expansion revenue to OCC in FY 2000-01. *Source*: historical MERC financial reports.

Assumptions and methodology. Other factors affect the size of the operating contingency in addition to the organization's tolerance for risk. These are the size of the operating budget, the magnitude of potential cost and revenue shocks, and the cost structure of the venues (represented in this study by the ratio of fixed to variable costs). The specific assumptions for these factors are described in this section.

For MERC, "event-related" costs and revenues are reasonable proxies for variable costs and revenues, and "non-event related" are reasonable proxies for fixed. MERC financial reports identify event and non-event amounts. The project team constructed a simple economic model of each venue from recent operating budget data, FY 2005-6 to FY 2009-10. Because cost structures differ, each venue will have different reactions to cost spikes or revenue slumps. For example, Expo is highly sensitive to variations in event activity because 95 percent of its operating revenue is derived from events while two-thirds of its costs are fixed. PCPA is relatively less sensitive to fluctuations in events because its structure allows it to shed event-related costs more readily than the other two venues.

The variances around these cost models were derived from the last 15 years of operating budgets by venue, FY 1995-96 to FY 2009-10. Historical operating surpluses and deficits were adjusted to account for controllable and extraordinary one-time events, such as the transfer of $9 million from OCC to Expo in FY 1996-97 and the $5.74 million of VDI expansion revenue to OCC in FY 2000-01.

The magnitude of potential cost and revenue shocks are based on MERC managers' historical experience with extreme (although not necessarily worst-case) situations. The cost models were "shocked" with various combinations of reductions in event activity (up to 15 percent), reductions in non-event revenue (up to 6 percent), and across-the-board increases in costs (up to 5 percent) for each venue. Historical variances were used to calculate the risks associated with these combinations, which in turn inform the options for target sizes of the reserves.

Results are shown in Table 4 on the next page. The reserves needed to reach 95 percent confidence are shown for comparison, and as background for the discussion of stabilization reserves that follows.

Table 4
Operating Contingencies by Venue
Comparison of Reserve Levels at 90 and 95 Percent Confidence Levels
(10- and 20-year events, respectively)

	Reserve Amounts		
Venue	90% Confidence	95% Confidence	Difference
Expo	$364,000	$550,000	$186,000
Percent of budget	*6.4%*	*9.7%*	*3.3%*
OCC	$1.54 million	$1.80 million	$260,000
Percent of budget	*6.4%*	*7.5%*	*1.1%*
PCPA	$300,000	$474,500	$174,500
Percent of budget	*3.0%*	*4.6%*	*1.6%*

Implementation. To avoid a detailed study each year, the operating contingency can be set to the percentages of the operating budget shown in Table 4 above. These amounts should be contingent appropriations in each annual budget. That way, the funds can be made available with a budgetary action by the Metro Council if needed during the year.

Comments. Metro's default policy is to set aside 4 percent of the operating budget as contingency. MERC's current practice follows this policy. The resulting adopted FY 2010-11 contingencies are $250,000, $1,066,623 and $471,840 for Expo, OCC and PCPA, respectively. Based on the same analysis as above, these amounts provide confidence at the 83.5 percent, 83 percent and 94.9 percent levels, respectively.

Most organizations find that technically-determined operating contingencies are larger than implemented in practice. This is mainly because almost every organization responds to cost shocks with a combination of cost management and draws from reserves. As stated in the Design Criteria section, the recommended contingencies cover the operating budget (at the stated confidence) assuming no management of costs. If MERC were to establish cost management protocols as a matter of policy in partial response to cost or revenue shocks, the contingency targets could be downsized.

In interpreting these numbers, the reader should keep in mind a basic tenet of statistics: probabilities are just that. It is possible that a 10 year event could happen twice or more in a decade. But it is also possible that it won't happen for 20 or more years.

Stabilization Reserve

The types of revenue shocks to which MERC is most sensitive tend to persist for more than one year. Accordingly, the study team recommends that MERC establish stabilization reserves to back up the operating contingency. A stabilization reserve is not appropriated for the budget, but its funds are used to restore any shortfall in the operating contingency in the subsequent year. The study team further recommends that MERC fund its stabilization reserves at the level shown in the "Difference" column of Table 3. This would mean that the operating contingencies and stabilization reserves together are sized to withstand a combination of cost spikes and revenue slumps that amount to a "twenty year event" spread over two fiscal years.

Renewal & Replacement

Concept. The renewal and replacement reserve serves as the source-of-funds for all renewal and replacement outlays. With a properly-sized and managed reserve, there is no need to budget for renewal and replacement from current operating revenue. Each venue would look to its current cash flow only to make an annual or periodic deposit into the reserve account. Implementation might need to be modified for PCPA where the Friends provide a major source of capital funding. But the overall principle still holds.

There is a tradeoff between the size of the initial balance of the reserve and the size of the periodic deposits into the account. A higher initial balance allows lower periodic payments, and vice versa. The choice of the initial balance and the size of periodic deposits depend on the amount of resources available when the reserve is established, and the amount of revenue that will be available for the periodic deposits over time.

Design criteria. The reserves are sized to meet two design criteria: (1) each year's beginning account balance should be sufficient to cover that year's expected outlays, including a contingency for cost overruns; and (2) the periodic deposits should be relatively stable or at least predictable, and feasible. The sufficiency of the account balance each year is measured by the coverage ratio, which is simply the beginning balance[*] divided by the annual outlay. A coverage of 100 percent means there are exactly enough funds available for projected costs. Ideally, coverage should be at least 105 percent to provide a contingency for cost overruns in some of the projects. Contingencies for cost overruns that stem from acceleration (that is, projects that must be initiated ahead of schedule) are described in the "implementation" section below.

The challenge. Table 5 (next page) shows actual capital outlays during the previous two and five years by venue. According to MERC financial staff, the historical amounts are dominated, or exclusively, expenditures for renewal and replacement. The figures demonstrate the renewal and replacement funding challenges at MERC. A glance at the "2-Year Window" section shows that OCC's average *pro forma* outlay will almost triple between the last two and the next two years, from $832,000 to $2.3 million per year. (Big ticket items such as roofing and carpet drive these numbers.) Over the next five years the average *pro forma* outlay almost doubles, from $900,000 to more than $1.6 million per year (see "5-Year Window" in the table). At PCPA the outlays quintuple in the two-year window, from less than a quarter of a million dollars to almost $1.25 million per year. The five-year average more than triples from $405,000 to $1.43 million. At Expo the next five year average is up almost two and a half times the size of the last five-years. Outlays at all three venues are highly variable from year-to-year after that.

The challenge for design of the renewal and replacement accounts is to determine reasonable initial balances, which when supplemented by affordable periodic deposits, fully fund the renewal and replacement needs.

[*] The beginning balance includes the periodic deposit which is assumed to be credited at the beginning of the year.

Table 5

Average Annual Capital Outlays by Venue

FY 2005-06—FY 2009-10 and FY 2011-12—FY 2015-16

	Average Annual Outlays (2-Year Window)		Average Annual Outlays (5-Year Window)	
Venue	Last 2 Years	Next 2 Years	Last 5 Years	Next 5 Years
Expo	159,800	147,800	84,700	203,700
OCC	832,000	2,295,500	898,500	1,631,500
PCPA	242,800	1,212,700	404,800	1,433,400
Admin	129,700	60,200	178,200	188,900
MERC	1,364,300	3,716,200	1,566,200	3,457,500

Sources

History: MERC revenue and expense reports

Projections: renewal and replacement *pro formas* provided by each venue.

Assumptions and methodology. This analysis started with identification of feasible annual deposits. Because each venue has demonstrated that it can afford the historical outlays in Table 5, this study assumes that these same amounts could be converted to reserve deposits – once the reserve itself becomes the source of funds for the actual capital expenditures. The study aimed for coverages (the ratio of beginning balance to planned outlay) of 105 percent each year. The future outlays are based on renewal and replacement plans provided by each venue (and updated for this study). Rounding out the assumptions, a 0.6 percent near term rate of return on the account balance, growing to 5 percent by 2017; and a 3 percent per year rate of cost inflation were used in the study.

Results. Options that meet the design criteria for the next five years are summarized in Table 6 on the next page. Because of the very high outlays that are programmed during the next 3 to 4 years and the highly variable outlays after that, it is not possible to meet all of the design criteria over a longer term time frame such as 10 or more years. However, subject to the assumptions of the study, the recommendations in Table 6 provide full funding for the next 5 years, which provides MERC with time to review and revise its renewal and replacement outlays and resources. This planning work should take place over the next 2 to 3 years to allow for timely implementation. See the “Comment” column in Table 6 for venue-specific recommendations.

Table 6
Renewal and Replacement Funding
FY 2011-12 through FY 2015-16

Venue	FY 2011-12 Balance	Annual Deposit*	Minimum Coverage	Comment
Expo	$925,000	$85,000	85%**	Expo should complete a review and revision of its R&R plan in time for the FY 2013-14 budget at the latest, as the $85,000 deposits are not sufficient to sustain planned outlays past FY 2014-15.
OCC	$5,325,779	$875,000	105%	OCC should complete a review and revision of its R&R plan in time for the FY 2016-17 budget at the latest, as the $875,000 deposits are not sufficient to sustain planned outlays past FY 2017-18.
PCPA	$5,595,000	$240,000	105%	PCPA should complete a review and revision of its R&R plan in time for the FY 2014-15 budget at the latest, as the $240,000 deposits are not sufficient to sustain planned outlays past FY 2015-16.
Admin	$732,416	/***/	106%	If Admin resumes increasing its deposit by $5,000 per year beginning in FY 2019-20, funding is sustainable in the long run.

* Deposits commence in FY 2012-13; no deposit is assumed in the transition year, FY 2011-12.
** Coverage would fall below 100% in FY 2015-16, based on Expo's current renewal and replacement outlay plan.
*** $42,500 in FY 2012-13, to increase by $5,000 each year until the annual deposit reaches $62,500.

Implementation. The renewal and replacement plans should be actively managed on an ongoing basis, including a periodic, independent assessment of asset conditions and replacement costs.* In each annual budget, the full amount of the next year's plan should be appropriated for expenditure. Unspent funds should be returned to the reserve; and if material, may be considered as an offset to the next periodic deposit.

As a contingency against acceleration of future projects, a portion, say 10 to 20 percent, of the second year's plan should be appropriated as contingency. That way, the funds can be made available with a budget amendment by the Metro Council if needed during the year.

Comments. As suggested above, the main funding challenges in the immediate future are the major outlays planned over the next three to four. After that, the variation in outlays becomes the issue. At OCC, for example, the expenditures range from zero (in three different years) to as much as $3 million in a single year. These factors tend to drive up the size of the annual deposits compared with the requirements of a smoother trajectory of expenditures over time.

* This is not just good practice, but also a requirement of Metro's Capital Asset Management Policies.

New Capital and Business Strategy

New Capital

Concepts. A new capital reserve is analogous to the renewal and replacement reserve. It is a funding source for new capital acquisitions; an alternative to borrowing. Like the renewal and replacement reserve, it is a management tool to smooth the financial effect of uneven capital outlays, and acts like a savings account: you build up the reserve with the intention of spending it.

Design criteria would follow those described for renewal and replacement, but be based on an acquisition plan for new capital. The capital plan, in turn, is often driven by the business plan.

Business Strategy

Concept. This reserve would cover non-recurring costs of pursuing business strategies, continuity and opportunities. Examples:

- <u>Strategy</u>. Funding the research or soft costs of expanding or adding a business line.
- <u>Continuity</u>. If gaps emerge during budget development, and it does not make good business sense to cut costs to fill those gaps, then the business strategy reserve is an appropriate place to turn for funding *(conventionally, "budget balancing")*.
- <u>Opportunity</u>. If unforeseen opportunities arise requiring, say, seed money in order to move forward, then the business strategy reserve is an appropriate source of funds.

Design Criteria. If the concept of a business strategy reserve proves useful, the design criteria will depend on its purpose.

Results. Targets for the new capital and business strategy reserves were not specifically addressed in this study, as funding is driven more by management and strategic considerations than technical factors, and MERC's capital acquisition and business plans are not sufficiently developed at this time to guide a formal technical analysis.

Comments

- The amount that may be ***available*** for new capital and business strategies in FY 2011-12 is the fund balance that remains after all of the other reserves have been funded. These figures were shown in Table 1. However, without a review of business plans, opportunities, threats, and priorities, it is not possible to define how much is ***needed*** for new capital and business strategy/development.
- These reserves fulfill part of MERC's current "strategic fund balance" concept.
- As the business line between new capital and strategy can sometimes be gray, MERC may find it useful to develop policies that govern fungibility between these uses.
- As a matter of practicality MERC may need to fund its business strategy needs with operating surpluses as available, rather than strictly as an accumulation reserve that builds to a specific target.

EXHIBIT C
MERC Resolution 11-07
March 2, 2011

Proposed FY 2011-12 Rental Rate Increases for the Portland Center for the Performing Arts (PCPA) and the Portland Exposition Center (Expo).

EXPO CENTER

In 2002, facility rental rates effective July 1, 2003 were established that included square footage discounts when exhibit halls were rented in certain combinations; consequently, the greater the total of exhibit hall square footage rented, the greater the facility rental discount. Discounts ranged from as little as 4% to as much as 27% when all exhibit halls were rented.

During development of the proposed Fiscal Year 2011-12 budget and in consideration of increasing expenditures as well as significant long-term financial obligations, staff determined to review the long established discounts toward decreasing those discounts over time and increasing revenue accordingly. As part of this internal review, staff also surveyed the facility rental rates of several other venues to determine the Expo Center's competitive placement in the region. From a strict cost per square foot perspective, the Expo Center remains very competitive with prime space rates ranging from $.05 to $.07 per square foot.

The proposed Fiscal Year 2011-2012 budget generally provides for a 3% rental rate increase for most locations and a 6% increase for 5 of the 7 combined exhibit hall locations thereby beginning to reduce the discounts.

In collaboration with facility users, staff will continue to review the reduction of discounts and other rental rate considerations toward development of multi-year rental rate recommendations for Commission consideration.

PCPA

In 1995, the Commission established criteria that would allow for four tiers of rental rates at PCPA facilities-resident company, preferred non-profit, non-profit and commercial. In 1998, the Commission approved an extension of these same rates for three more years through June 2001.

In June 2002, the Commission approved an increase of rental rates by CPI for every year beginning July 1, 2002 for all PCPA users. At the time CPI was running at 3% and continued to do so for several years so this became the standard annual increase for all rent.

In June 2009, the Commission approved a "0%" increase for the PCPA resident companies and non-profit user groups for FY 10 and FY11, but allowed increases by CPI or a minimum of 3% in FY12 and FY13.

PCPA would like to increase rental rates by a minimum of 3% for commercial users in spite of a CPI that is below 3%. As the resident companies and non-profits return to the minimum 3% increase for these groups, staff is requesting the Commission approve a 3% increase in rental rates for FY 2011-12 for commercial users of PCPA facilities.

Fiscal Year 2011-2012 Facility Rental Rates

Facility Rental Rates / Ticketed

Locations	Fiscal Year FY 11	Fiscal Year FY 12	Dollar Increase	Percentage Increase
Exhibit Halls				
A	2,350	2,400	50	2%
B	1,850	1,900	50	3%
C	3,050	3,125	75	2%
D1	2,475	2,550	75	3%
D2	2,475	2,550	75	3%
D	4,950	5,100	150	3%
E1	3,675	3,775	100	3%
E2	3,675	3,775	100	3%
E	7,350	7,550	200	3%
Combined Exhibit Halls				
ABCD	10,850	11,500	650	6%
ABCDE	15,500	16,500	1,000	6%
ABC	7,000	7,075	75	1%
AB	3,900	4,150	250	6%
AC	5,200	5,325	125	2%
CDE	12,825	13,600	775	6%
DE	10,725	11,375	650	6%
Meeting Rooms				
A101	195	200	5	3%
D101	130	135	5	4%
D102	105	110	5	5%
D201	350	355	5	1%
D202-3	390	400	10	3%
D202-4	585	600	15	3%
D202	195	200	5	3%
D203-4	390	400	10	3%
D203	195	200	5	3%
D204	195	200	5	3%
D205	135	140	5	4%
E101-2	310	320	10	3%
E101	140	145	5	4%
E102	170	175	5	3%
D101-2	235	240	5	2%
D201-4	935	950	15	2%
D201-5	1,070	1,100	30	3%

Fiscal Year 2011-2012 Facility Rental Rates

Facility Rental Rates / Ticketed

Locations	Fiscal Year FY 11	Fiscal Year FY 12	Dollar Increase	Percentage Increase
Miscellaneous				
Connector	320	320	0	0%
East Hall	580	600	20	3%
A Lobby	385	385	0	0%
A Lounge	185	185	0	0%
D Lobby	1,695	1,695	0	0%
E Lobby	1,900	1,900	0	0%
D Lounge	500	500	0	0%
All Parking Lots	16,071	16,071	0	0%
Boneyard	310	320	10	3%
Lower Parking Lot 1 East	1,466	1,466	0	0%
Lower Parking Lot 1 West	2,772	2,772	0	0%
Lower Parking Lot 1-2-3	9,138	9,138	0	0%
Lower Parking Lot 1-2	6,198	6,198	0	0%
Lower Parking Lot 1	4,238	4,238	0	0%
Lower Parking Lot 1W-2-3	7,672	7,672	0	0%
Lower Parking Lot 1W-2	4,732	4,732	0	0%
Lower Parking Lot 2	1,960	1,960	0	0%
Lower Parking Lot 3	2,940	2,940	0	0%
Upper Parking Lot 1-2-3-4	6,933	6,933	0	0%
Upper Parking Lot 1-2-3	3,376	3,376	0	0%
Upper Parking Lot 1-2	2,584	2,584	0	0%
Upper Parking Lot 1	1,720	1,720	0	0%
Upper Parking Lot 2-3	1,656	1,656	0	0%
Upper Parking Lot 2	864	864	0	0%
Upper Parking Lot 3	792	792	0	0%
Upper Parking Lot 4 South	420	420	0	0%
Upper Parking Lot 4	3,557	3,557	0	0%
Upper Parking Lot Plaza	310	320	10	3%

Fiscal Year 2011-2012 Facility Rental Rates

Facility Rental Rates / Non-Ticketed

Locations	Fiscal Year FY 11	Fiscal Year FY 12	Dollar Increase	Percentage Increase
Exhibit Halls				
A	2,875	2,950	75	3%
B	2,150	2,200	50	2%
C	3,600	3,700	100	3%
D1	2,950	3,035	85	3%
D2	2,950	3,035	85	3%
D	5,900	6,075	175	3%
E1	4,325	4,450	125	3%
E2	4,325	4,450	125	3%
E	8,650	8,900	250	3%
Combined Exhibit Halls				
ABCD	12,950	13,725	775	6%
ABCDE	18,225	19,325	1,100	6%
ABC	8,300	8,550	250	3%
AB	4,725	5,000	275	6%
AC	6,275	6,450	175	3%
CDE	15,225	16,150	925	6%
DE	12,650	13,400	750	6%
Meeting Rooms				
A101	195	200	5	3%
D101	130	135	5	4%
D102	105	110	5	5%
D201	350	355	5	1%
D202-3	390	400	10	3%
D202-4	585	600	15	3%
D202	195	200	5	3%
D203-4	390	400	10	3%
D203	195	200	5	3%
D204	195	200	5	3%
D205	135	140	5	4%
E101-2	310	320	10	3%
E101	140	145	5	4%
E102	170	175	5	3%
D101-2	235	240	5	2%
D201-4	935	950	15	2%
D201-5	1,070	1,100	30	3%

Fiscal Year 2011-2012 Facility Rental Rates

Facility Rental Rates / Non-Ticketed

Locations	Fiscal Year FY 11	Fiscal Year FY 12	Dollar Increase	Percentage Increase
Miscellaneous				
Connector	320	320	0	0%
East Hall	670	690	20	3%
A Lobby	410	410	0	0%
A Lounge	200	200	0	0%
D Lobby	1,775	1,775	0	0%
E Lobby	2,000	2,000	0	0%
D Lounge	500	500	0	0%
All Parking Lots	16,071	16,071	0	0%
Boneyard	310	320	10	3%
Lower Parking Lot 1 East	1,466	1,466	0	0%
Lower Parking Lot 1 West	2,772	2,772	0	0%
Lower Parking Lot 1-2-3	9,138	9,138	0	0%
Lower Parking Lot 1-2	6,198	6,198	0	0%
Lower Parking Lot 1	4,238	4,238	0	0%
Lower Parking Lot 1W-2-3	7,672	7,672	0	0%
Lower Parking Lot 1W-2	4,732	4,732	0	0%
Lower Parking Lot 2	1,960	1,960	0	0%
Lower Parking Lot 3	2,940	2,940	0	0%
Upper Parking Lot 1-2-3-4	6,933	6,933	0	0%
Upper Parking Lot 1-2-3	3,376	3,376	0	0%
Upper Parking Lot 1-2	2,584	2,584	0	0%
Upper Parking Lot 1	1,720	1,720	0	0%
Upper Parking Lot 2-3	1,656	1,656	0	0%
Upper Parking Lot 2	864	864	0	0%
Upper Parking Lot 3	792	792	0	0%
Upper Parking Lot 4 South	420	420	0	0%
Upper Parking Lot 4	3,557	3,557	0	0%
Upper Parking Lot Plaza	310	320	10	3%

PCPA Rental Rates

	2010/2011 Keller	2011/2012 Keller		2010/2011 ASCH	2011/2012 ASCH		2010/2011 Newmark	2011/2012 Newmark
Tier 1 - Commercial Rates								
Performance - Evening	3,935 vs 8%	4,055 vs 8%		3,935 vs 8%	4,055 vs 8%		1,350	1,390
Rehearsal/Load-in Day	1,965	2,025		1,965	2,025		735	760
Tier 2 - Non-Profit Rates								
Performance - Evening	3,340 vs 5%	3,440 vs 5%		3,340 vs 5%	3,440 vs 5%		1,135	1,170
Rehearsal/Load-in Day	1,675	1,725		1,675	1,725		685	705
Tier 3 - Featured/Non-Profit -- Jefferson Dancers, MYS, Singing Tree, PA&L, PICA, WB								
Performance - Evening	1,855	1,910		1,855	1,910		640	660
Rehearsal/Load-in Day	925	955		925	955		350	360
Tier 4 - Principal/Resident - OBT, OCT, OSO, POA, PYP, TOJ								
Performance - Evening	780	805		780	805		295	305
Rehearsal/Load-in Day	370	380		370	380		155	160

	2010/2011 Winningstad	2011/2012 Winningstad		2010/2011 Brunish	2011/2012 Brunish
Tier 1 - Commercial Rates					
Performance - Evening	760	785		760	785
Rehearsal/Load-in Day	390	400		390	400
Tier 2 - Non-Profit Rates					
Performance - Evening	650	670		355	365
Rehearsal/Load-in Day	370	380		190	195
Tier 3 - Featured/Non-Profit -- Jefferson Dancers, MYS, Singing Tree, PA&L, PICA, WB					
Performance - Evening	355	365		NA	NA
Rehearsal/Load-in Day	185	190		NA	NA
Tier 4 - Principal/Resident - OBT, OCT, OSO, POA, PYP, TOJ					
Performance - Evening	155	160		110	115
Rehearsal/Load-in Day	115	120		85	90

METROPOLITAN EXPOSITION-RECREATION COMMISSION

Resolution No. 02-31

For the purpose of approving the implementation of a user fee and facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06 at the Portland Metropolitan Exposition Center.

WHEREAS, the Commission adopted a five-year strategic plan and program that identifies goals and strategies for each of its business units through 2006 to include, in part, the development of a plan and approval of percentage rental or user fees and the approval of facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06 at the Portland Metropolitan Exposition Center; and

WHEREAS, in collaboration with staff, the Ad Hoc Expo Center Licensee Committee and the Expo Center Advisory Committee have reviewed and recommended the implementation of a user fee and facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06.

BE IT THEREFORE RESOLVED that the Metropolitan Exposition-Recreation Commission approves the implementation of the following user fees and facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06 at the Portland Metropolitan Exposition Center:

1. Effective July 1, 2003, a user fee of 6% of ticket sales, with a minimum of $.50 per ticket, will be assessed;
2. All user fee revenue and expenditures will be identified and accrued for use strictly associated with the Expo Phase III construction project;
3. The Commission assures that it will not increase the user fee without first holding a public review process and receiving comments by the Expo Advisory Committee;
4. Events that both sell fewer than 3,000 tickets and generate gross ticket sales of less than $15,000, run of show, are exempt from the application of a user fee;
5. Facility rental rates for user fee events for Fiscal Year 2003-04 through Fiscal Year 2005-06 are established as shown on attached; and
6. Facility rental rates for non-ticketed and user fee exempt events for Fiscal Year 2003-04 through Fiscal Year 2005-06 are established as shown on attached Exhibit B.

Passed by the Commission on September 25, 2002.

Chair

Secretary-Treasurer

Approved As To Form:
Daniel B. Cooper, General Counsel

By:

Lisa Umscheid
Senior Assistant Counsel

Exhibit A

Facility Rental Rates
Ticketed Events with User Fee

Locations	Fiscal Year 2003-2004	Fiscal Year 2004-2005	Fiscal Year 2005-2006
Exhibit Halls			
A	$1,900	$2,000	$2,050
B	$1,450	$1,525	$1,575
C	$2,400	$2,550	$2,625
D	$3,850	$4,100	$4,200
D1	$1,925	$2,050	$2,100
D2	$1,925	$2,050	$2,100
E	$5,700	$6,050	$6,250
E1	$2,850	$3,025	$3,125
E2	$2,850	$3,025	$3,125
Exhibit Halls in Combination			
AB	$3,100	$3,275	$3,375
ABC	$5,500	$5,825	$6,000
ABCD	$8,500	$9,000	$9,275
ABCDE	$12,000	$12,700	$13,075
CDE	$10,000	$10,600	$10,900
DE	$8,350	$8,850	$9,125
Meeting Rooms			
D 101	$100	$105	$110
D 102	$75	$80	$85
D 103	$200	$210	$215
D 201	$275	$300	$310
D 202	$150	$160	$165
D 203	$150	$160	$165
D 204	$150	$160	$165
D 205	$100	$110	$115
E 101	$105	$110	$115
E 102	$125	$135	$140
VIP Room	$105	$110	$115
Miscellaneous			
Connector	$235	$250	$260
Exterior	$250	$265	
$275			
Hall A Lobby	$315	$335	$345
Hall D Lobby	$1,350	$1,425	$1,470
Hall E Lobby	$1,525	$1,625	$1,675
Lounge	$150	$160	$165

Exhibit B

Facility Rental Rates
Non-Ticketed & User Fee Exempt Events

Locations	Fiscal Year 2003-2004	Fiscal Year 2004-2005	Fiscal Year 2005-2006
Exhibit Halls			
A	$2,325	$2,400	$2,475
B	$1,775	$1,825	$1,875
C	$2,950	$3,050	$3,150
D	$4,750	$4,900	$5,050
D1	$2,375	$2,450	$2,525
D2	$2,375	$2,450	$2,525
E	$7,000	$7,200	$7,400
E1	$3,500	$3,600	$3,700
E2	$3,500	$3,600	$3,700
Exhibit Halls in Combination			
AB	$3,800	$3,900	$4,025
ABC	$6,700	$6,900	$7,100
ABCD	$10,375	$10,675	$11,000
ABCDE	$14,625	$15,050	$15,500
CDE	$12,200	$12,550	$12,925
DE	$10200	$10,500	$10,800
Meeting Rooms			
D 101	$105	$110	$115
D 102	$80	$85	$90
D 103	$210	$215	$220
D 201	$300	$310	$320
D 202	$160	$165	$170
D 203	$160	$165	$170
D 204	$160	$165	$170
D 205	$110	$115	$120
E 101	$110	$115	$120
E 102	$135	$140	$145
VIP Room	$110	$115	$120
Miscellaneous			
Connector	$250	$260	$270
Exterior	$265	$275	$285
Hall A Lobby	$335	$345	$355
Hall D Lobby	$1,425	$1,470	$1,515
Hall E Lobby	$1,625	$1,675	$1,725
Lounge	$160	$165	$170

MERC Staff Report

Agenda item/Issue: Approving the implementation of a user fee and facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06 at the Portland Metropolitan Exposition Center.

Resolution No.: 02-31

Date: September 25, 2002 **Presented by:** Chris Bailey

Background: The Commission adopted a five-year strategic plan and program that identifies goals and strategies for each of its business units through 2006. The purpose of this resolution, therefore, is to secure the Commission's approval to implement two of the Expo Center strategies contained within the program.

Goal 2.c of the Expo Center's program primarily provides for 1.) the approval of parking fees for Fiscal Years 2002-03 and 2003-04; 2.) the creation of an ad hoc Expo Center licensee committee; 3.) the development of a plan and approval of percentage rental or user fees; and 4.) the approval of facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06.

Parking fees for Fiscal Years 2002-03 and 2003-04 were approved by the Commission in January 2002 and the establishment of an ad hoc Expo Center licensee committee was accomplished at the May 2002 Expo Center Advisory Committee meeting.

In collaboration with staff, the Ad Hoc Expo Center Licensee Committee then participated in several work sessions associated with developing recommendations related to the two remaining strategies. Upon completion, the committee then reported their findings and recommendations to the Expo Center Advisory Committee in August 2002.

The Ad Hoc Committee report included the following comments and recommendations regarding the two strategies:

<u>Development of a plan and approval of percentage rental or user fees</u>

The Ad Hoc Expo Licensee Committee recognizes the Strategic Plan/Implementation documents and the significance of beginning to secure funds towards the Phase III construction project while concurrently maintaining financial stability for the facilities.

In reviewing the percentage rental and user fee analysis worksheets, it is readily apparent that the application of a user fee is far more productive in achieving the desired result.

However, it is equally evident and strongly recommended that event producers have sufficient notice to consider and budget for such a fee; that all net user fee revenue and expenditures must be distinct, secured and only associated with Phase III; assurance that the fees will not be adjusted without public review; and that a conditional waiver will exempt certain events from application of a user fee thereby minimizing the loss of those events due to an aggregate financial impact.

Approval of facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06.

As a fully self-supporting public facility, the committee is aware that the Expo Center experiences operational cost increases as well as non-operational increases in support costs and debt service. The committee is further aware that rental rates represent a major resource and that they were last approved to be effective April 2001.

In reviewing the proposed increases, the committee concurs that the methodology is fundamentally valid in projecting future rental rates. However, the committee is equally sensitive to the aggregate impact on users of the Expo Center in simultaneously applying both a user fee and rental increases.

Recommendation:
In consideration of the foregoing, the Ad Hoc Expo Licensee Committee recommends approval in applying a user fee and increasing facility rental rates contingent upon the following stipulations:

- *Effective July 1, 2003, a 6% of ticket sales with a minimum of $.50 per ticket sold User Fee will be assessed;*

- *All net user fee revenue and expenditures will be identified and accrued for use strictly associated with the Expo Phase III construction project;*

- *The Commission assures that it will not increase the user fee calculation elements without first executing a public review process and receiving comments by the Expo Advisory Committee;*

- *Events that do not sell at least 3,000 tickets and generate a gross sale of $15,000, run of show, are exempt from the application of a user fee;*

- *Facility rental rates for user fee events will remain at the current rate through Fiscal Year 2003-04; will increase by approximately 6% for Fiscal Year 2004-05 and approximately 3% for Fiscal Year 2005-06; and*

- *Facility rental rates for non-ticketed and user fee exempt events will increase by approximately 6% for Fiscal Year 2003-04, 3% for Fiscal Year 2004-05 and 3% for Fiscal Year 2005-06.*

The Expo Center Advisory Committee concurred with the Ad Hoc Committee recommendations and are mutually recommending that the Commission approve the implementation of a user fee and facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06 based upon the noted conditions.

A letter of notification has been distributed to approximately fifty Expo Center licensees advising of the process, recommendations and further solicits their written comments or clarifying questions.

Recommendation: Staff recommends that the Commission approve the implementation of a user fee and facility rental rates for Fiscal Years 2003-04, 2004-05 and 2005-06 at the Portland Metropolitan Exposition Center, to include the noted conditions.