**Attachment C**
**MTC-ABAG Merger Study**
**Financial Forecast**

As part of the MTC-ABAG Merger Study, Management Partners performed a third-party six-year financial forecast (FY 2014-15 through FY 2021-22) for both agencies under two scenarios.

1. *Funding Framework for 2014 (Funding Framework).* The first six-year forecast is based on the funding framework described in a June 18, 2014 memo from the MTC executive director entitled Revised Funding Agreement for MTC/ABAG Joint Planning, Research and Administrative Facilities. That memo set forth a Funding Framework that would guide future funding agreements for continued MTC support of the ABAG planning function. Amounts paid by MTC on behalf of ABAG for tenant improvements to the new San Francisco offices to which MTC and ABAG will soon be moving are included as part of this Funding Framework.
2. *Implementation of MTC Resolution 4210.* The second forecast examines the impact on both agencies following the implementation of MTC Resolution 4210. The "Principles for Functional Consolidation" in Attachment A to Resolution 4210 state in part:

    > *Beginning July 1, 2016, MTC shall offer positions at equal or better compensation to 13 ABAG planners through a right of first refusal retention process, and together with MTC's planning department, shall create an integrated regional planning department…*

Both financial forecasts are included in the attached PowerPoint slides, which will be presented at the March 25 meeting of the Joint Committee.

## *Assumptions*

Each agency provided historical financial data, estimates of their future revenue and expense growth, and data on the cost of employee salaries and benefits. Grant-funded agencies, by their very nature, are not in control of the funding they receive from outside sources. Management Partners assumed a continuation of current funding levels with inflationary growth, based on input from both agencies. Personnel costs were trended using existing labor MOUs and future inflationary growth. Pension costs were predicated on CalPERS' 2014 valuation and six-year forecast, taking into account a continued transition of payroll over time from "Classic" to "PEPRA" status. A modest recession was assumed in 2017 that would affect Transit Development Act (TDA) sales tax collections, with a recovery over the ensuing two years.

For MTC's budget forecast, only their operating budget, Proposition 84 funding passed through to ABAG, and that portion of their long-term federal grants that historically has been allocated to meet part of the funding commitment to ABAG under the 2014 Funding Framework was used. Debt service and capital spending for MTC and their affiliated agencies was excluded. ABAG's annual operating budget served as the basis for their forecast.

In both the MTC and ABAG forecasts, reference is made to Governmental Accounting Standards Board (GASB) 68 and the requirement to include the present value of unfunded pension liabilities on the balance sheet, rather than identifying it in the footnotes to annual financial statements. This requirement does not affect the cash available to meet current budgetary commitments.

## *MTC Financial Forecast*

Under a continuation of the 2014 Funding Framework, MTC's total reserves are projected to decrease from $36.7 million in FY 2014-15 to $32.1 million in FY 2021-22. The agency's unrestricted balance decreases from $23.1 million in FY 2014-15 to $14.6 million in FY 2021-22. (This is before taking into account a GASB 68 unfunded pension liability of $16 million in FY 2014-15, which is assumed to decline over the next 30 years.) This shortfall is manageable given the level of MTC reserves, and can also be addressed through corrective actions phased in over the coming years. The reasons for this ongoing decline in balance are primarily:

- Increased pension costs, with annual unfunded liability costs increasing from $1.3 million in FY 2014-15 to $2.8 million by FY 2021-22, and
- Loss of Proposition 84 grant funding that has been passed through to ABAG in lieu of a comparable amount of funding from other MTC sources. This loss averages $640,000 annually starting FY 2016-17.

Following implementation of Resolution 4210, MTC will add approximately $2.4 million in salary, benefit, and other post-employment benefits (OPEB) costs for the 13 planning positons, and another $1.2 million in indirect costs. This $3.6 million, combined with $1.75 million in transition funding and tenant improvements, results in an increase of approximately $1 million annually compared with $4.3 million in commitments under the 2014 Funding Framework. Transition funding of $1.2 million would continue through FY 2021-22, the same year in which funding of ABAG tenant improvements for the new San Francisco offices terminates. As a result, MTC's total reserves are projected to decline from $36.7 million in FY 2014-15 to $26.5 million in FY 2021-22. The agency's unrestricted balance declines from $23.1 million in FY 2014-15 to $9.0million in FY 2021-22 (before GASB 68). The reason for this net ongoing decline in balance is that MTC will be paying both transition funding to ABAG and the cost of the 13 new planners over the five-year period of FY 2016-17 through FY 2020-21.

## *ABAG Financial Forecast*

Under a continuation of the 2014 Funding Framework, ABAG's total reserves are projected to decline from $1.8 million in FY 2014-15 (5% of total expense) to $57,000 in FY 2021-22 (0.1% of total expense). (This is before taking into account the GASB 68 unfunded pension liability of $11.8 million in FY 2014-15, which is assumed to decline over the next 30 years.) The reasons for this ongoing decline in balance are primarily labor costs, especially increased pension costs, with annual unfunded liability costs increasing from $822,000 in FY 2014-15 to $1.7 million by FY 2021-22. This existing structural shortfall, however, is believed to be manageable with corrective actions phased in over the coming years. The current $1.8 million balance represents a low reserve for an agency highly dependent on grants, contracts and service programs. The Government Finance Officers' Association (GFOA) recommends a standard of two months operating expense, which for ABAG would be about 16.7%. For this analysis, the 2014 Funding Framework is assumed to be ongoing, although it only extends through FY 2020-21 by existing contract.

Following the implementation of MTC Resolution 4210, 13 planning positions are proposed to be reassigned to MTC for an expense reduction of approximately $2.4 million in salary, benefit and OPEB costs. Additionally, $1.1 million in indirect costs currently allocated to the existing MTC contract would no longer be available. MTC funding for planning services would be reduced from $3.8 million to $1.2 million, a loss of $2.6 million. The unfunded pension liability costs assigned to the 13 positions ($230,000 annually) must still be paid to CalPERS, so these costs are effectively reallocated over fewer remaining positions. This will result in a net overall annual budget shortfall of $440,000 in FY 2016-17.

After the transition funding ends in FY 2021-22, the net loss will rise to $1.7 million. Without any corrective action, the combined impact of the preexisting structural shortfall and the implementation of MTC Resolution 4210 would reduce ABAG's available fund balance from $1.8 million in FY 2014-15 to a $4.0 million deficit in FY 2021-22 (before GASB 68).

Additionally, the post MTC Resolution 4210 financial forecast assumes that ABAG would be able to increase its indirect cost rate from 45% to 65% on a smaller direct-cost basis. This would likely have significant, but varying impacts on or responses from granting agencies and other ABAG service providers such as:

- An inability to pass on a higher rate due to contractual agreement;
- An acceptance of the higher indirect costs, which may result in commensurate cuts in direct costs funded by the grant; or
- An increase in revenue to fund current direct costs as well as higher indirect costs. (This is the least likely to occur.)

It was not part of the scope of this project to analyze options in depth to address the financial issues that we believe will emerge for ABAG under the current Funding Framework (manageable) and after the implementation of MTC Resolution 4210 (more significant). We have, however, provided some possible avenues in the presentation slides.