

Gas Well Lease Revenues
Financial Management Policy
Ad Hoc Committee

Work Session
April 30, 2007



Meeting Objectives

- Introductions
- Information
- Committee Charges
- Issues
- Process

Committee Charges

The Gas Well Revenues Financial Management Strategy Ad Hoc Committee is charged with considering and making recommendations to the City Council on the following gas well revenue management strategies and issues:

- 1. Formulate the most prudent financial strategy that maximizes and leverages the positive impact of gas revenues for current and future generations of Fort Worth Citizens.**

Committee Charges Continued

2. Determine the most effective expenditure and investment model to insure that gas revenues provide substantial benefits to the citizenry in perpetuity.

Committee Charges Continued

- 3. Design a productive, effective and dependable endowment management plan that efficiently regulates expenditures of endowment interest and reinvestment of interest to ensure the perpetual growth of the corpus of the endowment funds.**

Committee Charges Continued

- 4. Determine the most fiscally prudent expenditure criteria for application of the expenditure policy.**

Committee Charges Continued

- 5. Review, consider and evaluate Council Proposal No. 265-Amendment to the City Policy Concerning the Allocation of Gas Well Drilling Revenues and Amendments to State Law Concerning the Investment of those Revenues.**

Freedom of Information Act

- Discussion of Provisions of the Act that would affect the Committee.

Background

1. Policy adopted by City Council April 26, 2005 (M&C G14767)
2. Policy incorporated into City's Financial Management Policy September 13, 2005 (M&C G14918)
3. Update and evaluation of Policy on September 12, October 31, and December 12, 2006, March 6, 2007, March 27, 2007

Current Financial Management Policy Revenue Allocations

- Aviation – restricted
- Water & Sewer Fund – restricted
- Lake Worth - restricted
 - Lake – designated to Water & Sewer Fund
 - Dry land – designated to Lake Worth Gas Well Revenue Fund
- General City Properties - designated to Capital Projects Reserve Fund*

*ROW revenues earmarked for streets CIP

Current Revenue Allocations (Continued)

- Park land- bonus dedicated to well park.
Royalties dedicated to citywide park CIP fund [2/3's] and park endowment fund [1/3]
- Nature Center-bonus and royalties completely dedicated to Nature Center
- Park land easements-designated by M&C for park site planning, design and/or development (not currently specified in Policy)

Current Bonus and Royalties Distribution for Parks

Bonus to Well Park - 100%

Royalty Allocation

- 2/3 to Citywide Park CIP Fund
- 1/3 to Citywide Park Endowment Fund*

Endowment Fund Annual Interest

- 75% allocated to Citywide Park CIP Fund
- 25% reinvested into Citywide Park Endowment Fund corpus

*Until Endowment fund reaches \$2 million (staff has recommended that this cap be increased)

Assets Restricted

Mandated

- Aviation – Federal Aviation Administration policy
- Parks – National Park Service and/or Texas Parks and Wildlife Department grant policy. Property deed restrictions

Conditional

- Water & Sewer – Master Ordinance, bond covenants, coverage factors and reserve policy [20%]
- Solid Waste – Enterprise fund policy (earmarked for debt service)
- Golf – Enterprise fund, deed restrictions and property leases

Flexibility in Revenue Restrictions

Amend local policy to provide flexibility in the following:

- Water & Sewer – general assets
- Water & Sewer – Lake Worth assets
- Parks – non grant funded
- Solid Waste
- Golf

WATER AND SEWER FUND GAS WELL REVENUE USE CRITERIA

1. Meet Ordinance & Bond Covenants (required)
2. Maintain Coverage Factors (required)
3. Meet 20% Reserve Policy (required)

Optional Uses

- Revenue shortfall
- Cash-funded Projects
- Match for Street Repairs
- Build Water Endowment Fund

Optional uses criteria – Provided all items listed above are met, on an annual basis any remaining \$ could be transferred to the General Fund if the revenues are declared as “surplus” to the W&S System

RECOMMENDED INVESTMENT POLICY

Amend Subchapter A of Chapter 2256, Texas Government Code (the Public Funds Investment Act):

“an investing entity may invest any money received from the leasing of land owned by the investing entity for oil, gas, or other mineral development in investments described in subsections (1) and (4) of Section 163.005, Property Code.”

Subsections (1) and (4) of Section 163.005 of the Property Code:

“stocks, bonds, debentures, ... shares or interests in regulated investment companies, mutual funds, common trust funds”

This law governs how endowment funds (public and private) may invest their money.

SB 1423

- Pending bill before the legislature regarding the exemption of oil and gas proceeds from the Public Funds Investment Act.
- Current law restricts earning potential of any City sponsored endowment fund.
- The bill would allow the City to create a 501(a) corporation and they would be exempt from federal taxation and the constraints of the Public Funds Investment Act.

Assumptions

- 12,062 Mineral Acres
- 15-20 Year Well Life
- 25% Royalty
- \$5 MCF Market Rate
- 225,000 MCF/Acre Reserve
- 20% Gas Recovery from Reserve

Disclaimers

- Bonus dollars received only after bid award and contract execution
- Royalty dollars received only if gas well successful
- Royalty dollars dependent on gas volume produced and market rates
- All revenues subject to market volatility

Projected Revenues

Currently Restricted Assets

Acreage	Restricted Site	Expenditure Restrictions	Estimated \$ Royalties (20 years)	Estimated Bonus @ \$4500/acre
1794	Aviation	Federal Policy	\$101,000,000	\$8,073,000
965	Water & Sewer-general	Local Policy**	\$54,000,000	\$4,342,000
3,000	Water & Sewer-Lake Worth *	Local Policy**	\$168,000,000	\$13,500,000
559	Solid Waste	Local Policy**	\$31,000,000	\$2,516,000
88	Golf	Local Policy**	\$5,000,000	\$396,000
585	Parks (8 sites)	Federal/state policy	\$33,000,000	\$2,633,000
3,622	Nature Center	Federal/state policy	\$204,000,000	\$16,299,000
	SUBTOTALS:		\$596,000,000	\$47,759,000
10,613	TOTAL: \$643,759,000			

•*Under lake and dry land

•** Subject to master ordinance, bond covenants, coverage factors and/or reserve policy

Current Balance All Assets and Funds \$13,007,156

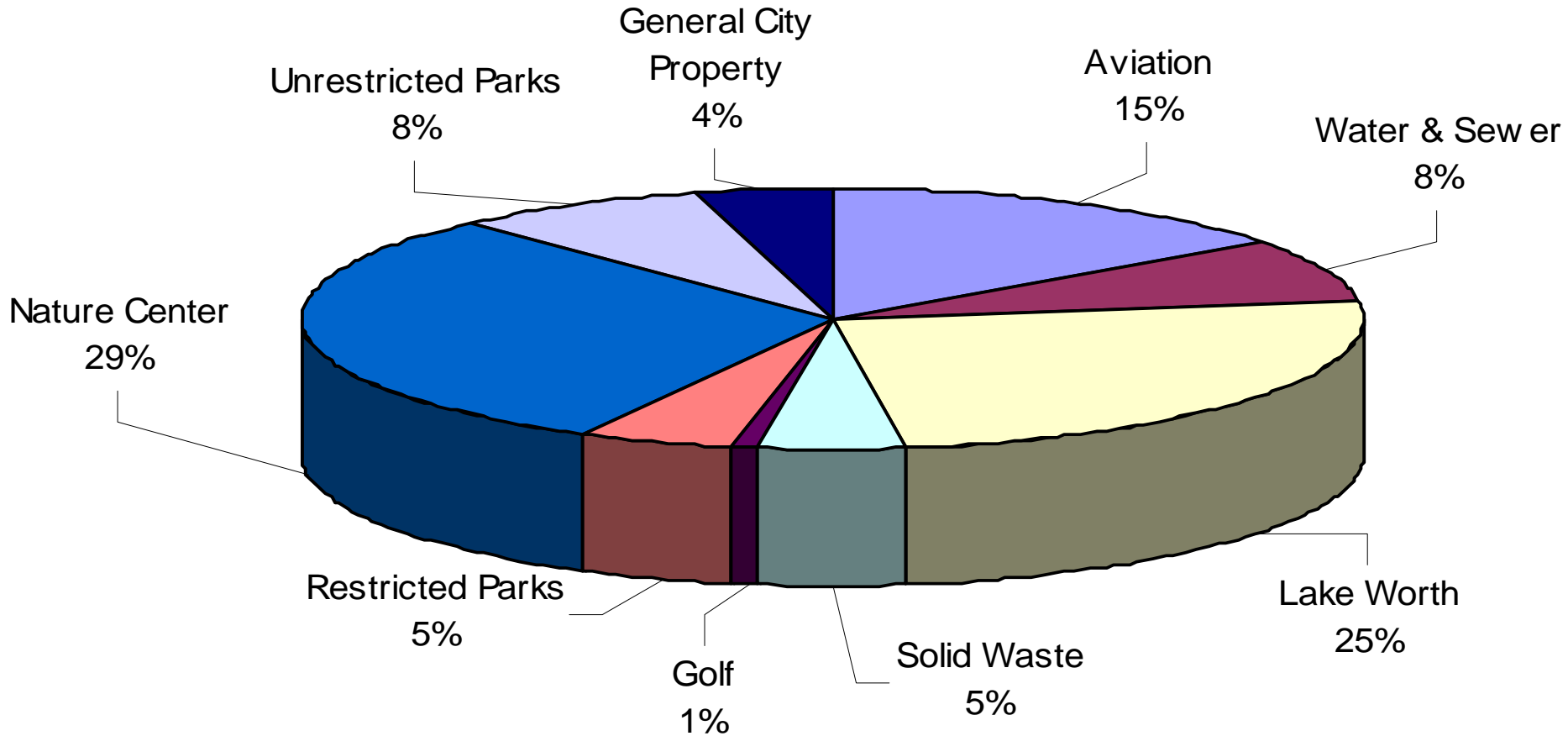
Projected Revenues

Currently Unrestricted Assets

Acreage	Unrestricted Asset	Estimated Royalties (20 years)	Estimated Bonus @ \$4500/acre
949	Parks (6)	\$53,000,000	\$4,271,000
500	General City Property	\$28,000,000	\$2,250,000
1449	SUBTOTALS:	\$81,000,000	\$6,521,000
	TOTAL: \$87,521,000		

Current Balance All Assets and Funds
\$13,007,156

Projected Revenues By Fund/Asset



Twenty (20) Year Estimated Totals

Restricted	\$643,759,000	88%
Unrestricted	\$87,521,000	12%
GRAND TOTAL	\$731,280,000	100%

Current Balance All Assets and Funds
\$13,007,156

Current Gas Revenue Balances

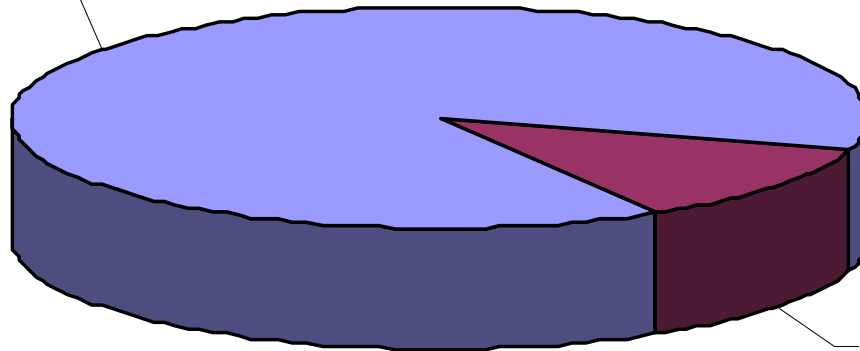
All Funds

Dept	Fund Name	
Aviation	Capital Projects	\$2,725,418
Budget	Capital Project Reserve	\$131,119
Environmental Management	Environmental Management	\$5,879
Parks and Community Services	Park Gas Lease Project	\$5,542,225
Environmental Management	Solid Waste	\$1,012,265
Lake Worth Trust	Lake Worth Trust Fund	\$1,993,611
Special Gift	Special Gift	\$8,190
Transportation and Public Works	Contract Street Maintenance	\$290,682
Water	Water & Sewer	\$932,521
Housing	FW Housing Finance Corp.	\$10,507
Engineering Services Admin Costs	Engineering Services Fund	\$23,851
Environmental Management	Solid Waste Capital Project	\$325,387
Risk Management (Legal Fees)	Risk Management	\$5,500
		\$13,007,155

Estimated Revenues

Grand Total: \$731,281,000

Restricted
\$643,759,000
88%



Unrestricted
\$87,521,000
12%

Current Balance All Assets and Funds \$13,007,156

Flexibility in Revenue Restrictions

Amend local policy to provide flexibility in the following:

- Water & Sewer – general assets
- Water & Sewer – Lake Worth assets
- Parks – non grant funded
- Solid Waste
- Golf

Potential Revised Revenues

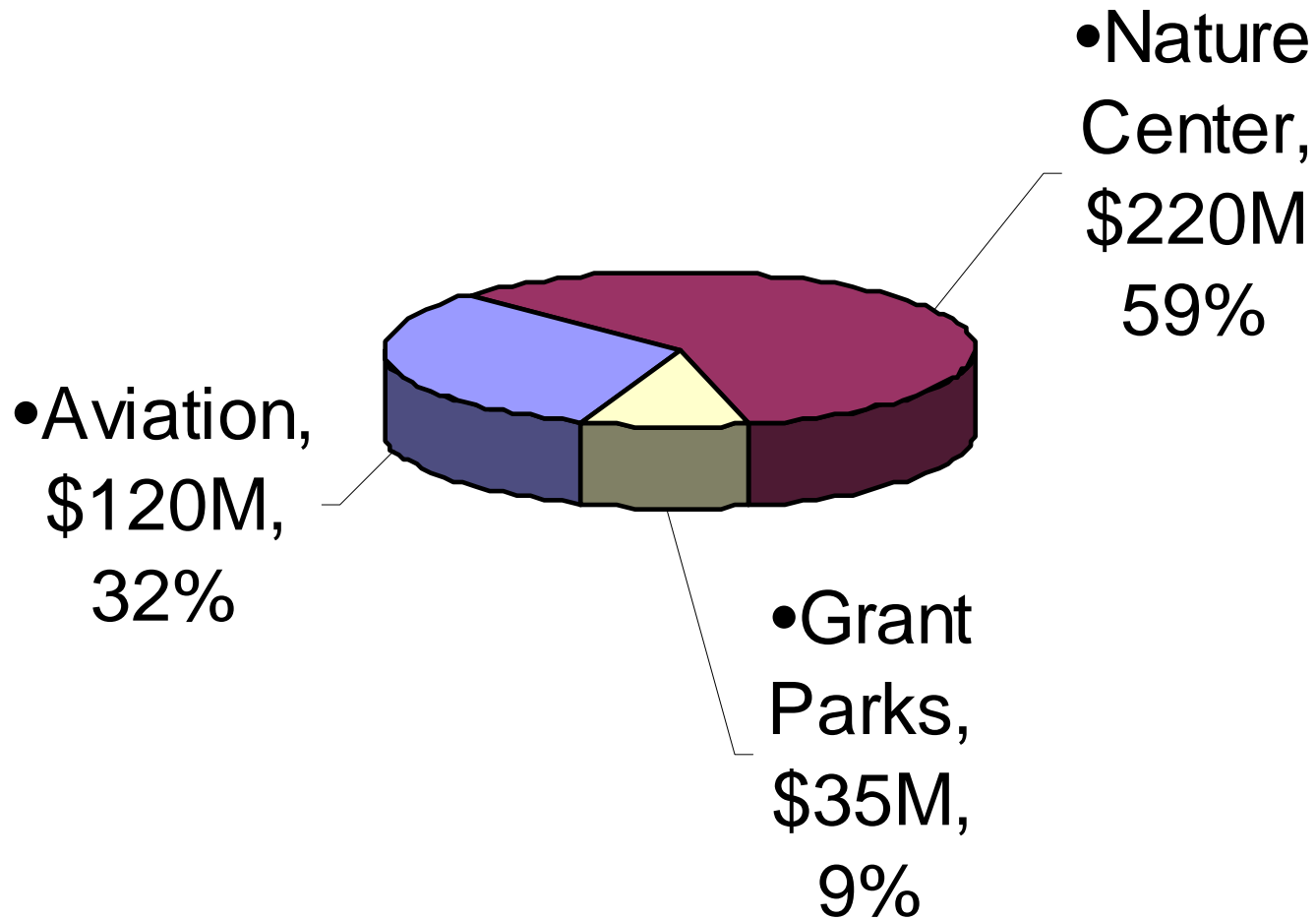
Restricted Assets

• Aviation	\$120M
• Nature Center	\$220M
• Grant Parks	<u>\$ 35M</u>
TOTAL	\$375M

Current Balance All Assets and Funds \$13,007,156

Note: Amounts rounded for illustrative purposes

Restricted Assets

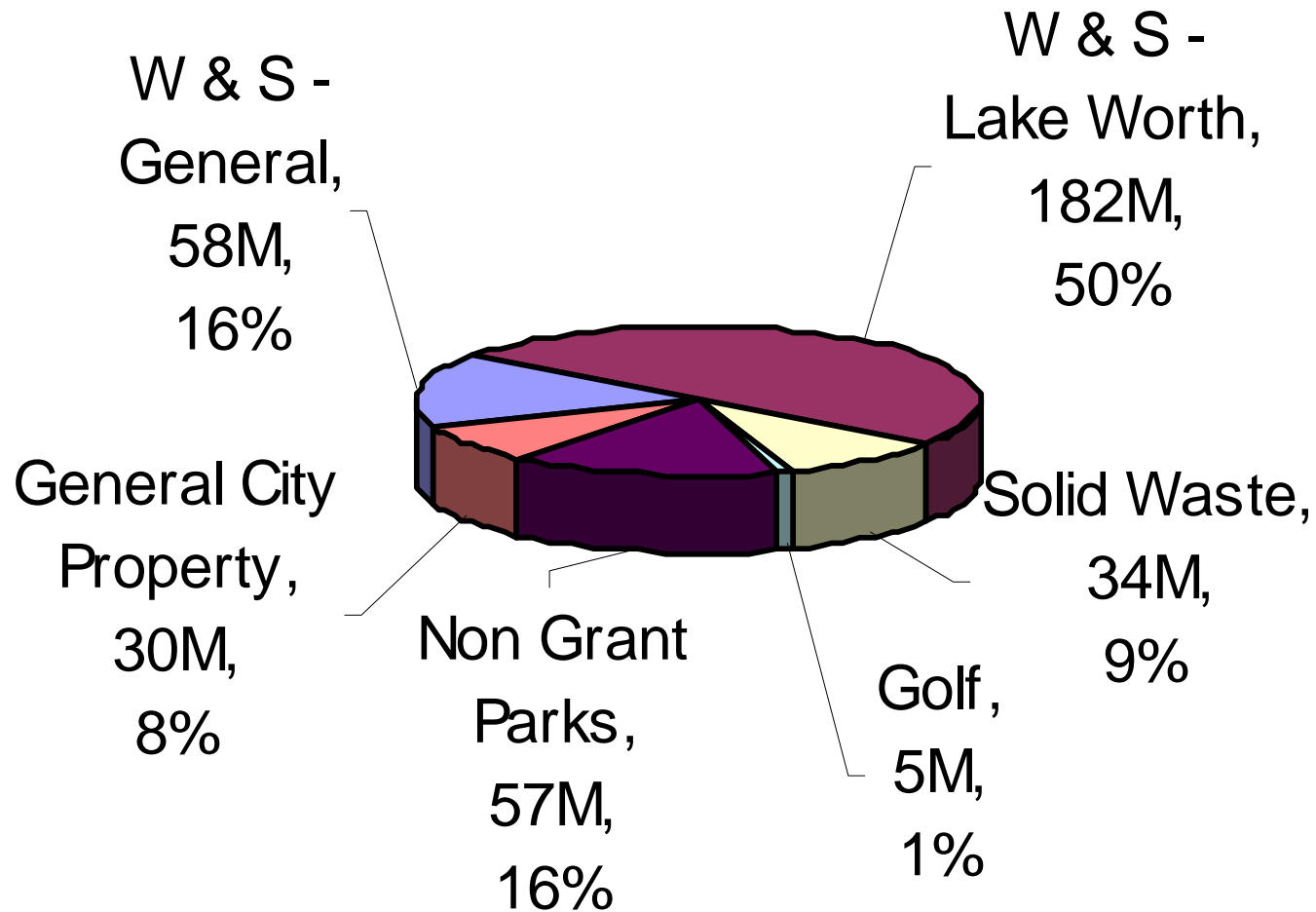


Assets with Potential Flexibility

Current Balance All Assets and Funds \$13,007,156

Note: Amounts rounded for illustrative purposes

Assets with Potential Flexibility



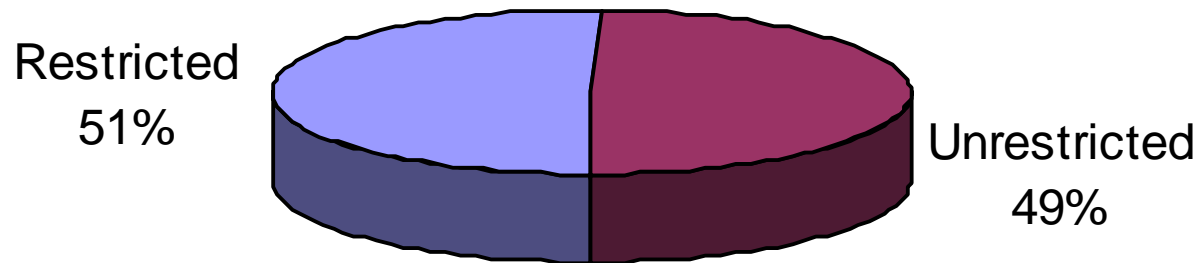
Revised Twenty (20) Year Totals

Restricted	\$375,000,000	51%
Unrestricted	\$366,000,000	49%
GRAND TOTAL	\$741,000,000	100%

Current Balance All Assets and Funds \$13,007,156

Note: Amounts rounded for illustrative purposes

Restricted vs. Unrestricted



City Needs for Future Funding

- GASB 45 liability: 5% of Annual Required Contribution: \$4.1M
- Retirement Fund contribution: \$7.5M =3% total General Fund increase; \$0.0 =3% increase all other funds

- Examples of City CIP needs

- | | |
|----------------------------------------------|----------------|
| • 10 year Capital Plan for Transportation | \$2.8 Billion |
| • Current Park and Recreation Facility Needs | \$367 Million |
| • All City Facilities Needs | \$4.7 Billion* |

* Based on Comprehensive Plan

- | | |
|-----------------------|--------------------|
| • Homeless | To be Determined |
| • Housing Trust Funds | 2 Million Annually |
| • Retirement Fund | 411 Million |

Investment & Use Strategies

Strategies

- Long Term
- Long and Near Term
- Near Term

Considerations

- Current infrastructure needs
- One time unforeseen resource
- Revenue risk and volatility
- Inflation
- Depreciation
- Funds/Asset Restrictions

Investment & Use Strategies (Continued)

Challenges

Balance short term needs with long term investment

Communication of:

- Revenue distribution and expenditure/investment policy
- Restrictions incurred by:
 - Federal and state policies and regulations
 - Bond Covenants, Master Ordinance and Reserve Policy

ISSUES?

- Communication to public and building public support for the Long Term component of any strategy

Mineral Valuations

Certified Tax Role

Year	2003	2004	2005	2006
Property Tax Accounts	345	476	998	1587
Appraised Value	\$33,504,120	\$56,683,790	\$139,170,950	\$314,752,260
Potential Revenue	\$289,811	\$490,315	\$1,203,829	\$2,706,869

Gas Well Valuations Projected

Perryman Group is currently undertaking economic impact study for the FW Chamber that might demonstrate projected increase in valuations [and corresponding tax revenues] for next 10-20 years.

Report is scheduled to be issued May 2007.

Use of Gas Well Tax Revenues from Mineral Valuations

- Due to volatility of tax revenues derived from mineral valuations these revenues should be managed and maintained as “general revenues” and not earmarked to underwrite specific programs or projects including:
 - General operating expenses
 - Debt service
 - Reduce fees for service
 - Reduce the ad valorem tax rate

Effect of Tax Rate Reductions to General Fund Compared to Homeowner

- 1 cent = \$3,400,000/yr
- 2 cents = \$6,800,000/yr
- 3 cents = \$10,200,000/yr

- 0.86 cents on \$100,000 home with 20% homestead exemption = \$688/yr
- 0.85 cents on \$100,000 home with 20% homestead exemption = \$680/yr or \$8 savings
- 0.84 cents on \$100,000 home with 20% homestead exemption = \$672/yr or \$16 savings
- 0.83 cents on \$100,000 home with 20% homestead exemption = \$664/yr or \$24 savings

Recommended Criteria for Use of Gas Well Revenues for Enterprise and General Funds

All Items Cash Funded

- Replenish fund balance reserve (required first)
- Outstanding bond principle lump sum payment
- Capital projects with minimum 10-year useful life
- Grant matches to leverage funds for capital projects
- Capital equipment with at least a 10-year life
- Technology with at least a 5-year useful life
- Equipment/Fleet revolving replacement fund

Recommendations

1. Adopt financial management policy that dedicates approximately half of revenues to one-time capital projects and half to endowment fund(s)
2. Adopt policy that specifies annual review of the Water & Sewer Fund and provided all fund requirements are met, allocate surplus revenues 25% each to W&S and General Fund CIP and W&S and General Fund endowment fund
3. Amend financial policy to earmark unrestricted park revenues for general city facilities and properties and replace well park bonus with grant restricted park funds
4. Amend financial policy to mandate one time capital expenditure criteria

Recommendations (continued)

5. Seek amendments to Public Funds Investment Act and Management of Institutional Funds Act
6. Amend financial management policy to increase the park endowment fund cap from \$2,000,000 to \$10,000,000
7. Adopt financial management policy which requires approval of annual expenditure plans based solely on revenues received
8. Adopt a resolution which stipulates the continuation of scheduled bond programs in accordance with the City's Comprehensive Plan
9. Establish criteria for allocation of gas well revenues for required infrastructure improvements in and around Lake Worth
10. Conduct further legal reviews as determined advisable by the City Attorney, specifically possible deed restricted properties

Recommendations (continued)

- Prudent financial management policy
- One time capital costs and long range financial investments only
- Avoid
 - Debt service
 - Operating expenses
 - Fees for service
 - Ad valorem tax

Council Proposal 265

- 25% of Revenues for immediate (current budget fiscal year) capital infrastructure need
- 25% of the revenues will be allocated to general fund needs and will be used for proportionate reduction of FW Ad Valorem Tax Rate

CP 265

- 50% of the revenues will be allocated to endowment funds to be saved for future generations for ten years. From the eleventh year forward 50% of the subsequent earnings will be used for capital improvement and operations of the respective endowments. The remaining 50% of subsequent earnings will remain in the fund and be reinvested. The proposed endowment funds shall be referred to as the People's Funds, and such endowment funds shall be established in accordance with the assets from which the
- Work to Amend the Public Funds Investment Act to allow investment strategies similar to private endowments but that still limit risk to the fund.

City Manager's Comments on CP 265

- Does not recommend use of gas well and gas well related taxes to pay operating expenses due to the volatility of the revenue source.
- This temporary increase in revenues should be treated as excess above and beyond the base operating and capital budget.
- An Amendment to the Public Funds Investment Act could occur in this session or the next.

City Manager's Comments on CP 265

The following would constitute poor financial policy:

- 1) Reliance upon gas revenues to pay debt service.
- 2) Reliance upon gas revenue to pay operating expenses
- 3) Reducing fees for service based on temporary increases in revenues from gas production.
- 4) Reducing the property tax rate based on a temporary increase in property values related to mineral interests.
- 5) Implementing financial strategies that erode the “real” value asset of the endowment fund principal due to inflation, investment, or spending policies, by not reinvesting a sufficient amount of the interest earned by the fund.

Gas Well Informal Report to City Council #8829 Summary

- Restricted Funds– Parks, Aviation, Nature Center, Water and Sewer, Lake Worth, Golf Enterprise, General City Property.
- Water and Sewer Gas Funds may be used once the master ordinance and bond covenants are met.
- Parks, Aviation, and Nature Center funds use are restricted by State and/or Federal Law due to receipt of Federal or State Grants or Assistance.

Ad Hoc Committee Schedule

- May 21, 2007 Public Forum
- June 25 Committee Meeting
- Work Session with City Council in July or August