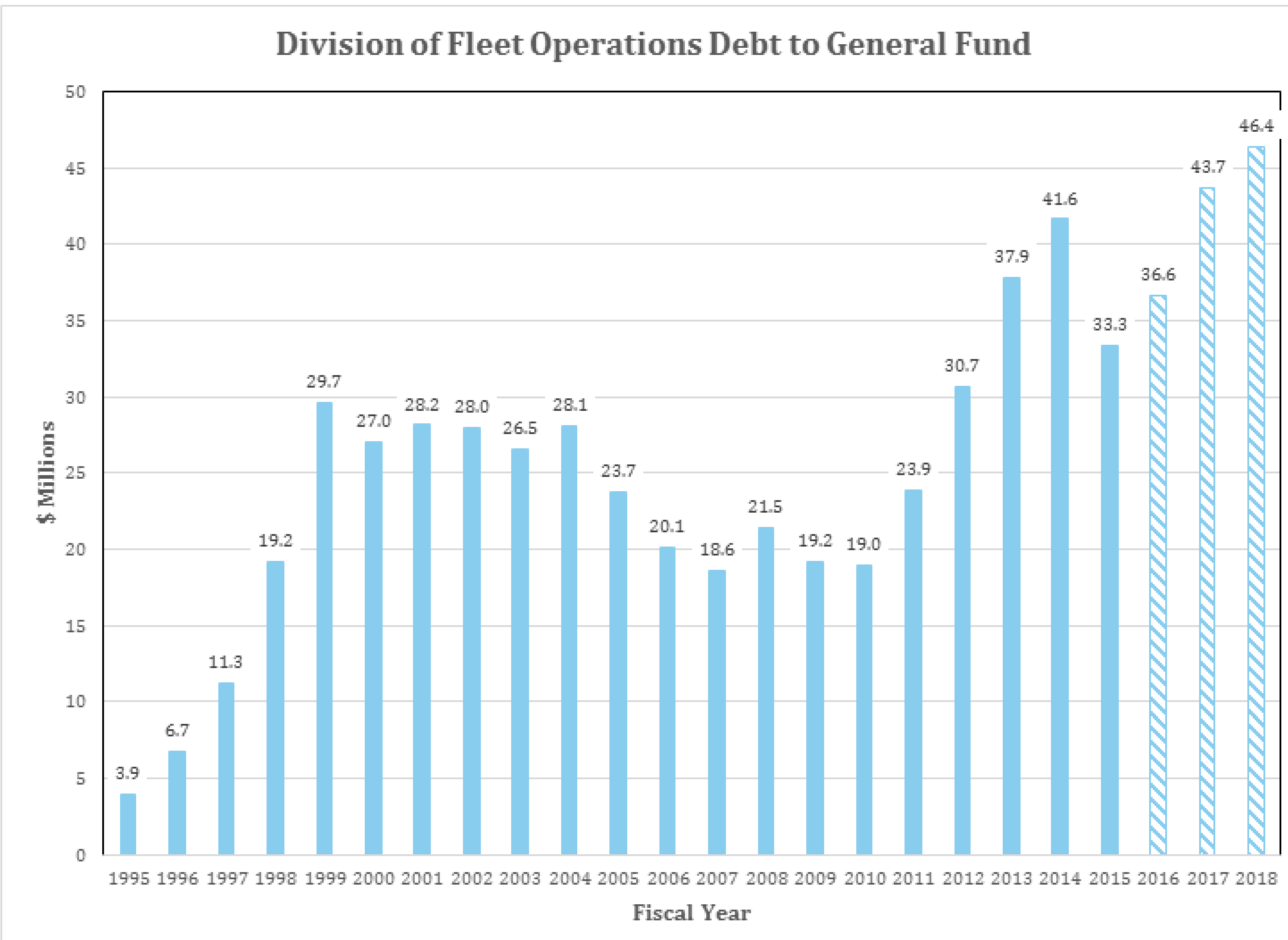
Fiscal Highlights

Division of Fleet Operations General Fund Borrowing - Brian Wikle

The Division of Fleet Operations was established as an internal service fund (ISF) in FY 1997. As an ISF, Fleet does not receive a General Fund appropriation; rather, it receives Dedicated Credits by charging customer state agencies for its services. Statute allows ISFs to incur long-term debt from the General Fund to eliminate negative working capital and to acquire capital assets.

The figure below depicts Fleets (and its predecessors) debt from FY 1995 through FY 2015. It also shows the division's projection of debt for FY 2016, FY 2017, and FY 2018. The increase in projected debt is due primarily to timing of purchases. The division has purchased an average of 660 vehicles per year since FY 2000. In FY 2015, the division purchased just 325 vehicles, but in the ensuing three years Fleet projects that it will purchase an above average number of vehicles.



The debt is due largely to three issues: (1) Fleet has historically under recovered on fuel charges, (2) Fleet has historically under recovered on maintenance costs, and (3) Fleet's lease rates have not been sufficient to cover the purchase cost of replacement vehicles. The fuel under charge is no longer an issue as, effective FY 2016, customer agencies are charged at cost for fuel. Fleet has adjusted the per mile rate charged to agencies, and it is now receiving sufficient revenue through the charge to cover maintenance costs. Finally, the division is taking measures and exploring options to reduce its need to borrow when purchasing replacement vehicles. However, due to federal rules regarding expenditures of federal funds by state agencies, the division has not included an inflationary adjustment in lease rates. Consequently, it would be difficult for the division to eliminate the need to borrow from the General Fund.

A number of options are available regarding Fleet's accumulated debt and/or borrowing such as the options explained below.

Option 1 - maintain the status quo. Regulations for ISFs allow the agency to have debt of up to 90 percent of the net book value of the agency's capital assets, and Fleet's debt is within this allowable limit. If the division were to continue its current practices, its debt to the General Fund should grow by the inflationary amount for purchases of replacement vehicles, but the debt should not grow beyond the legal limit.

Option 2 - appropriate to eliminate the current debt. The current debt plus projected additional debt could be retired through an ongoing appropriation of about $8 million for the next five fiscal years. In practicality, the appropriation would be a one-time hit to the budget as Fleet would return the money to the funding source (e.g. General Fund) and it would then be available for the next year's appropriation. This option alone would not eliminate Fleet's need to borrow as it does not address the financing gap that results from collecting on contract prices while not factoring in inflation.

Option 3 - build an inflationary factor into lease rates. The formula for lease rates could be modified to include an inflationary adjustment. Given a correct adjustment, Fleet should have sufficient cash to purchase replacement vehicles without having to borrow from the General Fund. However, federal rules allow collection based on a vehicles purchase price, so including an inflationary adjustment would be seen by the federal government as an overcharge, and the State would have to reimburse the federal government the amount of the overcharge each year.

Option 4 - continue the current model and appropriate to cover inflation. Absent an explicit inflation adjustment in the formula for lease rates, Fleet is knowingly under collecting in terms of financing replacement vehicles. The under collection could be mitigated through an annual appropriation.