

# **Public Sector Vehicle Financing**

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Mercury Associates Inc.

The word "MERCURY" is displayed in a large, bold, sans-serif font. The letters are white with a blue gradient and a subtle drop shadow, giving them a three-dimensional appearance as if they are floating above a dark blue surface.

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<b>Presentation</b>
<ul style="list-style-type: none"><li>■ Historical Perspective</li><li>■ Fleet Financial Management</li><li>■ Vehicle Financing Alternatives</li><li>■ Public Sector Applications</li><li>■ Q &amp; A</li></ul>
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<b>Vehicle Fleet Financing</b>						
<table border="1"><tr><td>Commercial Fleets</td><td>Government Fleets</td></tr><tr><td>75%</td><td>90%</td></tr><tr><td>Financed/Leased</td><td>Cash Paid/Owned</td></tr></table>	Commercial Fleets	Government Fleets	75%	90%	Financed/Leased	Cash Paid/Owned
Commercial Fleets	Government Fleets					
75%	90%					
Financed/Leased	Cash Paid/Owned					
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<b>Fleet Financing – Government Trends</b>					
<table border="1"><tr><td>Fiscal Constraints</td></tr><tr><td>↓</td></tr><tr><td>Lack of Vehicle Replacement Funding</td></tr><tr><td>↓</td></tr><tr><td>Rethink Financing Methods</td></tr></table>	Fiscal Constraints	↓	Lack of Vehicle Replacement Funding	↓	Rethink Financing Methods
Fiscal Constraints					
↓					
Lack of Vehicle Replacement Funding					
↓					
Rethink Financing Methods					
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<h2>Fleet Financial Management</h2>
<p><i>Combining fleet knowledge and financial expertise to make decisions effecting direct and indirect fleet costs</i></p>
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<h2>Fleet Financial Management</h2>
 <p>Costs</p>
 <p>Time</p>
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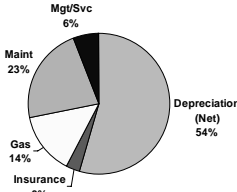
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<h2>Fleet Cost Components</h2>												
 <table border="1"><thead><tr><th>Component</th><th>Percentage</th></tr></thead><tbody><tr><td>Depreciation (Net)</td><td>54%</td></tr><tr><td>Maint</td><td>23%</td></tr><tr><td>Gas</td><td>14%</td></tr><tr><td>Mgt/Svc</td><td>6%</td></tr><tr><td>Insurance</td><td>3%</td></tr></tbody></table>	Component	Percentage	Depreciation (Net)	54%	Maint	23%	Gas	14%	Mgt/Svc	6%	Insurance	3%
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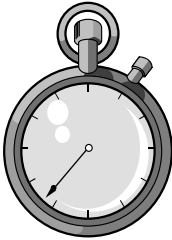
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### Fleet Time Components

- Driver
- Department
- Company Support



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### Fleet Financial Management

 Largest Expense Category  
- Net Cost of Vehicle

 Significant Time Category  
- Driver Downtime

} Key to Financial Management

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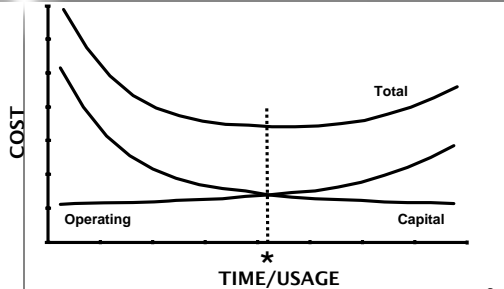
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### When should vehicles be replaced?



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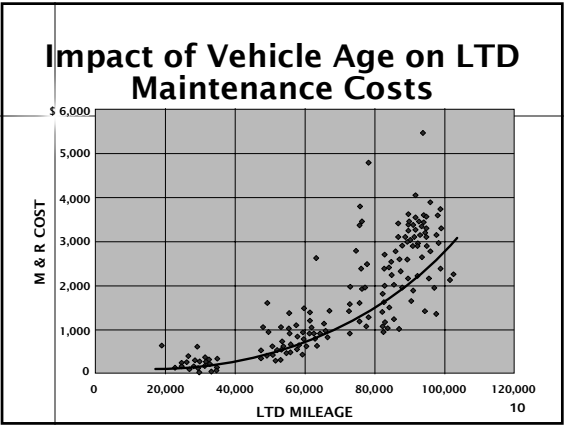
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### Indirect Costs of an Aging Fleet

- Reduced employee productivity
- Reduced employee safety, client, inmate, public safety
- Tarnished public image

⊞ INABILITY TO PROVIDE REQUIRED SERVICES

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### Costs of Lost Productivity

Number of vehicles in the fleet	19,700
Work days per year	240
Vehicle work days per year	4,728,000
Vehicle days out of service @ 5 percent downtime rate	236,400
Lost employee productivity <i>per year</i> @ 2 hours per day of vehicle downtime	472,800
FTE employees worth of lost productivity at 1,500 productive hours per employee per year	315
FTE costs <i>per year</i> @ \$50,000 per FTE employee to cover lost productivity	<b>\$15,760,000</b>

12

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	Why Don't Government Agencies Practice Effective Fleet Replacement?
	Organizations usually fail to replace vehicles in a timely manner due to <b><i>a lack of willingness to commit funds</i></b> <b><i>Not</i></b> <b>A lack of understanding of life cycle cost principles</b>

13

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	<b>Key Truths About Fleet Replacement Funding Levels</b>
	<ul style="list-style-type: none"><li>■ Funding requirements are determined by financing method(s) used.</li><li>■ Financing methods are not equal in terms of the ease with which an organization can commit funds to the replacement of fleet assets.</li></ul>

14

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	<b>Vehicle Financing Alternatives</b>
	3 Basic Methods  <b>Cash</b> <b>Savings</b> <b>"Debt"</b>

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<b>CASH: <i>Pay for vehicle in full at time it is acquired</i></b>
<ul style="list-style-type: none"><li>■ Advantages<ul style="list-style-type: none"><li>- Government Sector "tradition"</li><li>- Interest not charged or recognized (perceived advantage only)</li></ul></li></ul>
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<b>CASH: <i>Pay for vehicle in full at time it is acquired</i></b>
<ul style="list-style-type: none"><li>■ Disadvantages<ul style="list-style-type: none"><li>- Difficult to reliably obtain annual funding requirements</li><li>- Almost always leads to sub-optimal replacement decision making</li><li>- Cost of having a vehicle is transparent and ignored by vehicle users</li><li>- Requires detailed accounting</li></ul></li></ul>
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<b>SAVINGS: <i>Pay as you go via contributions to a replacement fund</i></b>
<ul style="list-style-type: none"><li>■ Advantages<ul style="list-style-type: none"><li>- Permits vehicles to be paid for incrementally</li><li>- Provides relatively smooth annual funding requirements.</li><li>- Greater annual funding reliability</li><li>- Less of an annual target for capital appropriation decision makers</li><li>- If costs passed to users, payment of regular charges for the use of each vehicle encourages more optimal fleet size</li></ul></li></ul>
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	<p><b>SAVINGS: <i>Pay as you go via contributions to a replacement fund</i></b></p>
	<ul style="list-style-type: none"> <li>■ <b>Disadvantages</b> <ul style="list-style-type: none"> <li>- Requires rigorous and administratively complex reserve fund management</li> <li>- Cash in the reserve fund to purchase replacement vehicles is subject to being "raided" when budget dollars get tight.</li> <li>- The size of reserve fund balances are limited by OMB Circulars A-87 and A-21</li> <li>- Replacement reserve funds are prohibitively expensive to establish if there already is a large backlog of fleet replacement needs</li> <li>- Fleet growth (additions to meet service demands) requires influx of capital</li> </ul> </li> </ul>
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	<p><b>"Debt": <i>Pay as you go via borrowing funds from the capital markets</i></b></p>
	<p style="text-align: center;"><b>Examples of Debt Financing</b></p> <ul style="list-style-type: none"> <li>■ Government General Obligation (Bonds, Certificates of Participation)</li> <li>■ Commercial Loans</li> <li>■ Lease – Purchase (Capital Lease)</li> <li>■ Operating Lease</li> <li>■ Closed End Lease</li> </ul>
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	<p><b>"Debt": <i>Pay as you go via borrowing funds from the capital markets</i></b></p>
	<ul style="list-style-type: none"> <li>■ <b>Advantages:</b> <ul style="list-style-type: none"> <li>- Capital costs of vehicle paid over time</li> <li>- <i>Reduces</i> the annual need for fleet replacement funding requests that compete for capital budget dollars</li> <li>- If costs passed to users, payment of regular charges for the use of each vehicle encourages more optimal fleet size</li> </ul> </li> </ul>
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	<p><b>"Debt": Pay as you go via borrowing funds from the capital markets</b></p>
	<ul style="list-style-type: none"> <li>■ <b>Advantages - continued</b> <ul style="list-style-type: none"> <li>- Provides for easier budget planning and processing as a set amount annually is required</li> <li>- Minimizes year-to-year volatility in replacement funding requirements</li> <li>- Provides for some flexibility to respond to program needs for additional vehicles without requirement of up front capitol.</li> </ul> </li> </ul>
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	<p><b>"Debt": Pay as you go via borrowing funds from the capital markets</b></p>
	<ul style="list-style-type: none"> <li>■ <b>Added Advantages of EXTERNAL Debt Financing</b> <ul style="list-style-type: none"> <li>- Moves financing of vehicles into business arena (out of political arena)</li> <li>- Eliminates use of internal resources, and associated competition for them</li> <li>- Ensures RELIABLE funding and control of timing</li> <li>- Addresses replacement backlogs and new needs without need for influx of capital</li> </ul> </li> </ul>
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	<p><b>"Debt": Pay as you go via borrowing funds from the capital markets</b></p>
	<ul style="list-style-type: none"> <li>■ <b>Disadvantages</b> <ul style="list-style-type: none"> <li>- Smooth budget cycle requires rigorous replacement cycle parameter management to balance remaining loan or lease balance and resale</li> </ul> </li> <li>■ <b>Perceived Disadvantages</b> <ul style="list-style-type: none"> <li>- Cost of Borrowing (Interest)</li> <li>- Ownership of Vehicles</li> <li>- Management Control</li> </ul> </li> </ul>
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**"Debt": Pay as you go via borrowing funds from the capital markets**

- **Cost of Borrowing (Interest)**
  - No money is free
  - Costs of not replacing much higher
- **Ownership**
  - Holding title does not provide operational advantage
  - Purchase or continued use can be provided for

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**"Debt": Pay as you go via borrowing funds from the capital markets**

- **Management Control**
  - Control of fleet and related services remains with organization, ensured via RFP details
  - Partnering with leasing company brings expertise and administrative economies of scale to the table

26

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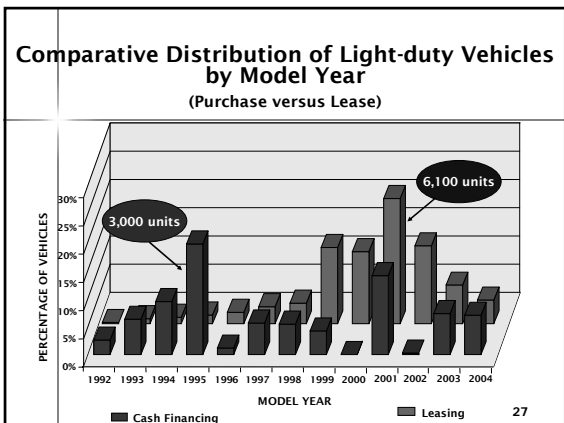
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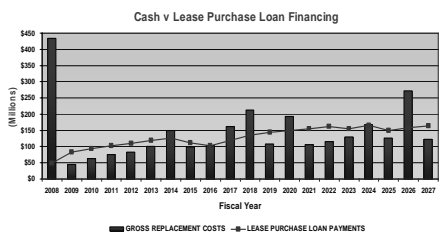
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### Replacement Backlog



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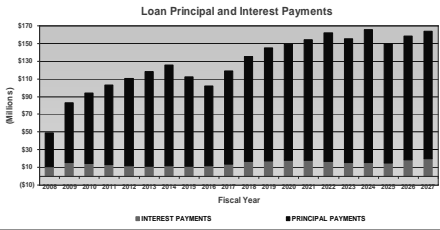
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### Interest Impact



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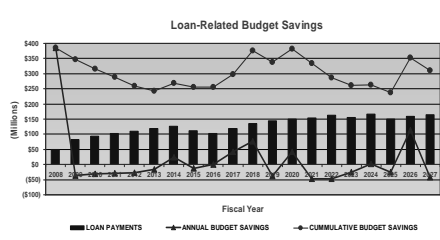
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### Budget Savings



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	<h2>MI Experience</h2>
	<ul style="list-style-type: none"> <li>■ In Late 1980's Smooth Funding From Revolving Fund Not Realized Due To             <ul style="list-style-type: none"> <li>- Rate Setting Decision Making (Replacement Cost Gap)</li> <li>- Significant Growth (Fleet Consolidation)</li> </ul> </li> <li>■ Revolving Fund Deficit Growing</li> <li>■ Developed Team to Review Financial Alternatives             <ul style="list-style-type: none"> <li>- Senior Official Support</li> <li>- Key Expertise/Leader Involvement</li> </ul> </li> <li>■ Review/Analysis Recommended Open End Lease and Acquisition/Disposal Services</li> </ul>
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	<h2>MI Experience</h2>
	<ul style="list-style-type: none"> <li>■ RFP for Acquisition, Disposal, Finance Awarded 1989</li> <li>■ Political, Legislative, Public, and Customer Reaction Management Required</li> </ul>
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	<h2>MI Experience</h2>
	<ul style="list-style-type: none"> <li>■ Benefits Realized             <ul style="list-style-type: none"> <li>- Eliminated Cash Drain</li> <li>- Optimized Depreciation Management</li> <li>- Addressed needs for growth</li> <li>- Brought Expertise and Economies of Scale from Fleet Service Provider to State</li> <li>- Maximized Federal Reimbursement</li> <li>- Decrease Administrative Support Needs</li> </ul> </li> </ul>
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	<h2>MI Experience</h2>
	<ul style="list-style-type: none"><li>■ Open end lease and fleet management services bid multiple times since 1989</li><li>■ Expanded Contracted Services (Maintenance/Gas) –Varied over Time</li><li>■ Engaged Mercury Associates (consultants) in 2005 to do a independent fleet best practices review – Direction Supported</li><li>■ Contract Bid and Awarded in 2005</li></ul>
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	<h2>Summary</h2>
	<ul style="list-style-type: none"><li>■ Effective Fleet Replacement<ul style="list-style-type: none"><li>– Key to Fleet Financial Management</li><li>– Linked to Reliable Financing Method</li></ul></li><li>■ Debt Financing<ul style="list-style-type: none"><li>■ Long Used in Private Sector/Gaining in Use in Public Sector</li><li>■ Provides Reliable Source of Funds for Fleets</li><li>■ Type of Financing Can Be Tailored to Your Organization</li></ul></li></ul>
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	<h2>Contact Information</h2>
	<p>Kathe Rushford Carter Senior Associate, Mercury Associates Inc 231 330-8931 E Mail: <a href="mailto:kcarter@mercury-assoc.com">kcarter@mercury-assoc.com</a></p>
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