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The Proposed Pittsburgh Parking Lease: A Look at the Numbers

As the Mayor takes his case for leasing the parking garages, lots, and meters to the public he has to wonder if at least one of the interested companies will see sufficient earnings potential from a long term lease to justify an offer of $300 million the City hopes to get. This is the amount needed to cover the Parking Authority's outstanding bond debt of about $100 million and provide $200 million for the City's pension funds.

The immediate question is: Why would a company offer $300 million to enter into a long term lease of the Parking Authority's nearly 19,000 parking spaces that are valued at $121 million in 2009 and generated about $7 million more operating revenue than operating expenses?

A look at the Authority's most recent balance sheet provides some insight into the factors a bidder for the lease will have to consider.

In 2009, the Authority generated just under $34 million in receipts from parking facilities, meters, and commercial rentals. Those are the possible money-making operations under consideration in the lease agreement. Revenues from residential parking permits and the parking court are excluded. It is unlikely the lessee will continue to operate the court. The $34 million represents the starting revenue point for the bidders to work from.

On the expense side there were $27 million in outlays related to personnel, operations, and depreciation. We exclude $2 million in costs related to the parking court. Bear in mind that almost $8 million in parking taxes collected and remitted are included in revenues and expenses.

Net non-operating revenues are $0.6 million. Out of the total of nearly $8 million in net revenue, the Authority pays $4.8 million in debt service and $1.1 million in a payment in lieu of taxes to the City. Of course, the lessee would pay neither of these. Thus, operating income facing the lessee based on 2009 Parking Authority numbers is about $8 million. Capital expenses are not accounted for but could absorb several million each year. How much bidders believe they can enhance revenues or cut costs will be a key element in the bids submitted.

Recall that the Mayor is hoping the lessee will offer an up-front payment to the City for the value of leasing the system, and we'll assume that the payment will be the aforementioned target of $300 million: $100 million to retire the Authority's debt and $200 million for the pension funds, enough to get a funded ratio of 50 percent and avoid a state takeover of administering the funds.

Consider the broad calculations facing the bidders. In order to cover a debt service payment on the $300 million, or to pay itself for the opportunity cost of the investment, the lessee will have to earn enough to cover the needed annual payments on that amount as well as all the other costs related to operating the parking system. Assuming conservatively an annual cost of 7.26 percent (based on an interest rate of 6 percent amortized over 30 years), the annual payments to finance the $300 million will be $21.8 million, and that does not contemplate any profits above the recovery of opportunity costs or to make debt service payments.

In addition to this annual payment, the lessee will incur operating expenses including employee compensation, utilities, insurance, security, maintenance, etc. These expenses—based on the Parking Authority's recent numbers—will be about $19 million initially ($27 million less the $8 million paid in parking taxes). Some cost reductions might be possible in future years but substantial reductions could take a while. The lessee will also have to pay property taxes and payroll preparation taxes the Parking Authority does not have to pay. Assuming the County's assessed value for the parking facilities is somewhere close to the $121 million shown in the Authority's financial report, the lessee will owe $3.6 million in total property taxes to the County, City, and Pittsburgh Schools.

All told, likely out of pocket expenses for the lessee, not including the parking tax, will be about $45 million a year. And this is just to break even. How much parking revenue will be required to cover the $45 million and the parking tax owed to the City? A parking tax rate of 40 percent means the lessee will owe the City 28.57 percent of parking revenues collected. Therefore, the lessee will need $63 million in gross revenue to net $45 million after the parking tax is paid.

Presently, the Parking Authority is bringing in roughly $34 million a year. How a lessee could hope to get from $34 million in parking revenue to $63 million presents an enormously difficult problem. Clearly, large increases in parking rates and/or big jumps in the numbers of patrons will be necessary to produce the 85 percent revenue increase.

For every million dollars in expenses the lessee can cut, the needed gross revenue will be lowered by $1.4 million, so a $5 million reduction in costs would lower the needed gross parking revenue to $56 million, still 65 percent higher than the $34 million currently generated by the Parking Authority. The cost reductions could be produced by savings in operating costs or by obtaining a lower interest rate on borrowings.

For example, obtaining a bond rate of 5 percent, instead of the 6 percent assumed above, would lower bond payments from $21.8 million to $19.5 million. This reduction would lower the break even parking revenue by $3.2 million.

Still, the central point is that it will be very difficult to generate adequate parking revenue to get to break even for the lessee. Parking rate increases of 65 to 85 percent are simply not going to happen. At those levels, the number of parkers at the lessee's facilities would begin to fall. A garage now charging $11 a day would have to raise the daily rate to $18 to $20. A $13 dollar daily rate would have to rise from $21 to $24. That's extraordinarily unlikely to occur. Note that a doubling of hourly rates on meters would produce only $6 million more revenue and will not significantly reduce the needed rate hikes at garages and lots.

So, the question. Is it reasonable to expect any bidder will come up with a $300 million offer?

Obviously, this is a very tall order. Unless there is a company willing to absorb major losses in the early years in hopes of making the parking network profitable some years in the future, it appears the $300 million desired bid is just too rich. Is modification of the desired up-front payment in the offing?

Alternatively, the City might consider lowering the parking tax rate to, say 20 percent. In that case, the increase in parking rates could be limited to 40 percent, a much more manageable figure, especially in light of the fact that much of the Parking Authority's current pricing advantage derives from the fact that it pays no property or payroll preparation taxes as privately owned garages have to do. Lowering the parking tax would go a long way to making the City attractive to people who want to come to the City for business or attend events.

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