

2003 Proposed Budget Transmittal Letter

October 21, 2002

Honorable Mayor, City Council, and Shoreline Residents:

I am pleased to present the 2003 Proposed Budget. This document presents the overall plan for allocating the resources of the City to a variety of programs necessary to support the community's physical security, enhance the quality of life, and maintain and develop facilities, parks, roads, and storm drainage.

In preparing the proposed budget, I have been particularly mindful of the Council's direction outlined at the budget and planning retreat held earlier this year. This budget supports the Community Vision, Values and Critical Success Factors, and 2002-2003 Council Work Plan developed by the City Council at this retreat. Consistent with this direction and input, the proposed budget places primary emphasis on maintaining current services, investing in capital projects to enhance the facility, transportation, and surface water systems throughout the City, and implementing a program to enhance economic development within our community.

The 2003 Proposed Budget reflects the first year of a trend in which our financial forecasts show expenditure growth will outpace revenue growth. Shoreline, like the rest of the Puget Sound area, faces greater financial constraints this year than in any previous year since incorporation. Despite these constraints, we are able to present a balanced budget with no new tax revenue sources that maintains the services provided by the City and increases some service levels of high priority to our community.

The proposed 2003 budget is designed to benefit the City's financial planning by:

- Emphasizing long-range financial and service level planning
- Concentrating on long-term policies rather than incremental service needs
- Recognizing the long-term implications of expenditure decisions

The 2003 Proposed Budget provides resources and services for the coming year, and also raises important financial planning issues the Council and staff will need to address in the next two years.

The remainder of this letter focuses on budget highlights for 2003 and the budget issues that will challenge the City over the next five to six years.

Budget Organization

The budget is organized to focus on financial data at a summary level and detail, and explains City operations, policies, and goals. The budget begins with this transmittal letter to provide an overview of the budget and future financial issues. Following this letter are the vision, values, and goals established by the City Council and staff. The budget includes an Executive Summary focusing on organization-wide information and the Operating Budget section organized by department and operating divisions. Within each department section, we have identified key accomplishments for year 2002 and key objectives for 2003. Each

section highlights significant changes in resources that will result in department service level changes. Key changes are also listed later in this letter.

In 2001, the City committed to the long-term process of measuring its operational effectiveness and efficiency using performance measures. Five departments are participating in the initial performance measure program: City Manager's Office, City Attorney's Office, Customer Service, Finance, and the Police Department. The 2003 proposed budget contains the estimated measurement results for 2002. This data will be used as a base to provide a comparison for future year activities.

The 2003-2008 Capital Improvement Program (CIP) provides the long range plans for roads, parks, facilities and surface drainage. The CIP was adopted in July 2002. Since that time the City Council has approved a public arts funding policy. As a result of this policy, an estimated \$40,000 will be generated for public art enhancements in 2003. Since this policy was adopted after the adoption of the CIP, the public art costs have been included in the 2003 proposed budget, but are not reflected in the CIP document.

Appendices are provided that contain salary and benefit summaries, a glossary and other information that may be helpful to the reader.

Budget Highlights

The City's 2003 proposed budget is balanced in all funds and totals \$44.5 million. The following table summarizes the 2003 proposed budget and provides a comparison to 2002 budgeted expenditures. The proposed 2003 budget is 1.4% more than the 2002 Amended Budget. The City's operating fund expenditures decreased \$1.55 million, or 4.4%, from 2002 to 2003, while the capital expenditures are projected to increase by \$2.3 million, or 27.1%. The increase in capital expenditures is related to moving forward on major transportation system projects within the City's CIP.

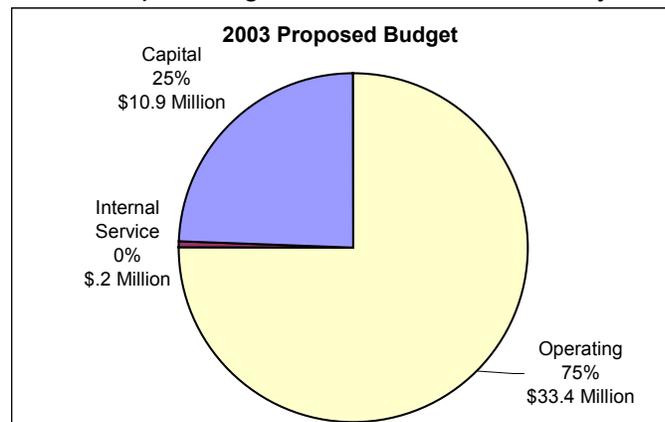
Fund	2003 Proposed Budget				2002 Amended Budget	02 - '03 % Change
	Beginning Fund Balance	Revenue	Expenditures	Ending Fund Balance	Expenditures	
Operating Funds:						
General Fund	6,044,020	24,344,972	25,790,325	4,598,667	27,018,730	-4.5%
General Reserve	1,601,729	167,370	0	1,769,099	0	n/a
Streets	469,567	2,829,220	2,926,874	371,913	3,585,011	-18.4%
Surface Water Management	2,135,490	2,528,888	2,734,438	1,929,940	2,345,524	16.6%
Development Services	370,559	1,754,470	1,859,545	265,484	1,914,731	-2.9%
Unemployment	61,406	10,000	10,000	61,406	8,259	21.1%
Code Abatement	85,030	100,000	100,000	85,030	100,000	0.0%
Public Art Fund	0	40,465	0	40,465	0	
Asset Seizure	28,522	23,650	23,650	28,522	25,000	-5.4%
Sub-Total Operating Funds	10,796,323	31,799,035	33,444,832	9,150,526	34,997,255	-4.4%
Internal Service Funds:						
Equipment Replacement	848,349	290,062	148,111	990,300	275,000	-46.1%
Vehicle Operations & Maintenance	62,807	41,500	55,000	49,307	70,000	-21.4%
Sub-Total Internal Service Funds	911,156	345,062	203,111	1,053,107	345,000	-41.1%

Fund	2003 Proposed Budget			2002 Amended Budget		02 - '03 % Change
	Beginning Fund Balance	Revenue	Expenditures	Ending Fund Balance	Expenditures	
Capital Funds:						
Arterial Streets	0	358,905	358,905	0	369,042	-2.7%
General Capital	3,854,938	2,041,017	1,925,120	3,970,835	3,313,260	-41.9%
Roads Capital	12,934,167	5,473,945	7,642,012	10,766,100	4,242,649	80.1%
Surface Water Capital	2,285,406	1,411,224	965,750	2,730,880	645,038	49.7%
Sub-Total Capital Funds	20,296,516	9,285,091	10,891,787	18,689,820	8,569,989	27.1%
Total City Budget	30,781,990	41,415,688	44,539,730	27,657,948	43,912,244	1.4%

The budget is divided into three parts: Operating, Internal Service and Capital.

The City's operating budget represents the cost of providing services to the Community.

The capital budget represents the cost of making improvements to the City's facilities, parks, transportation, and surface water systems. Internal service funds transfers between operating funds for maintenance and replacement of City equipment. The total 2003 operating budget is \$33.4 million. This is \$1.55 million or 4.4% below the 2002 amended budget.



Major changes within the City's budget include the following:

- ◆ **Personnel Costs:** The 2003 proposed budget includes \$560,000, a 6.2%, increase in personnel costs. The major changes in personnel costs include a combination of the following:
 - ◆ New positions (\$289,000). This is reflected as an increase in salary and benefit costs to the City, although the net budget impact is only \$55,000. To offset the cost of the new positions, one vacant position was eliminated (Utility Coordinator) and some of the planned professional service contract costs programmed within capital project budgets were reduced. The resulting flexibility will increase responsiveness to capital project schedules.
 - ◆ Market salary adjustments (\$101,000)
 - ◆ Budgeted step increases (\$133,000)
 - ◆ Increased aquatics extra-help (\$56,000) offset by increased programming revenue.
 - ◆ Projected benefit cost increases (\$178,043) related to health insurance premiums, worker's compensation costs, and state retirement contributions
 - ◆ More accurate allocation of capital project-related salary and benefits, resulting in an operating budget reduction (\$216,000).

- ◆ **Public Safety Costs:** The City will not see an increase in public safety costs. Jail contract costs are expected to be \$84,000 less than those budgeted for 2002. This is a result of using the Yakima County jail instead of the King County jail for some extended prisoner stays. The City's police contract is budgeted to increase by \$77,765, or 1.1%. This is a result of changing the method by which the City purchases canine services to a call-out basis. This change reduced anticipated cost increases by \$117,000
- ◆ **2003 Base Budget Adjustments:** The 2002 budget contains approximately \$1.5 million in either one-time expenditures or 2001 carry-over expenditures. These items were removed in the 2003 proposed budget.
- ◆ **Program Reductions:** 2003 on-going program costs were reduced by approximately \$187,000 to balance the budget and in anticipation of future year operating deficits. The primary reductions include elimination of funding for sub-area plan development and reduction in technology plan implementation costs. The technology implementation plan reductions should not significantly impact the overall technology implementation strategy.
- ◆ **One-time Expenditures:** The 2003 proposed budget includes \$1.08 million in one-time costs. \$1 million represents the use of General Fund reserves for the City Hall project and \$77,000 allocated for the purchase of two maintenance vehicles and one-time costs related to new staff positions.
- ◆ **Miscellaneous Cost Increases:** Miscellaneous cost increases include anticipated increases in utilities, maintenance contracts, and liability insurance. These increases total approximately \$61,000.

The capital budget includes resources that are allocated for completion of projects that enhance the City's facilities, parks, transportation, and surface water management systems.

Economic Outlook

The following table lists some of the major economic indicators for the United States and the State of Washington that were issued in September 2002.

Forecast Indicators	1998	1999	2000	2001	2002	2003	2004	2005
United States								
Real Gross Domestic Product % Change	4.4%	4.1%	4.4%	1.8%	0.8%	3.2%	3.5%	3.0%
Real Personal Income % Change	5.1%	4.7%	3.9%	3.8%	0.8%	2.4%	2.2%	2.7%
Unemployment Rate	4.7%	4.4%	4.1%	4.2%	5.5%	6.1%	5.6%	5.1%
Wage & Salary Employment % Change	2.7%	2.5%	2.5%	1.3%	-0.8%	0.3%	2.1%	1.9%
Housing Starts % Change	5.0%	8.4%	-1.3%	-4.1%	4.4%	-3.4%	0.7%	0.4%
Consumer Price Index	1.8%	1.7%	2.9%	3.4%	1.8%	2.7%	3.0%	2.7%
Washington State								
Real Personal Income	6.4%	6.1%	5.9%	1.4%	0.5%	1.0%	1.7%	2.9%
Unemployment Rate	4.6%	4.8%	4.9%	5.7%	7.0%	7.1%	6.8%	6.4%
Wage & Salary Employment % Change	3.8%	2.5%	2.4%	1.2%	-2.1%	-0.5%	1.8%	2.3%
Housing Starts % Change	18.6%	-0.4%	-13.1%	3.4%	-5.4%	0.5%	-2.1%	1.9%
Seattle Consumer Price Index	2.9%	3.0%	3.2%	4.0%	2.7%	2.4%	2.5%	2.4%

Source: Washington State Economic and Revenue Forecast Council

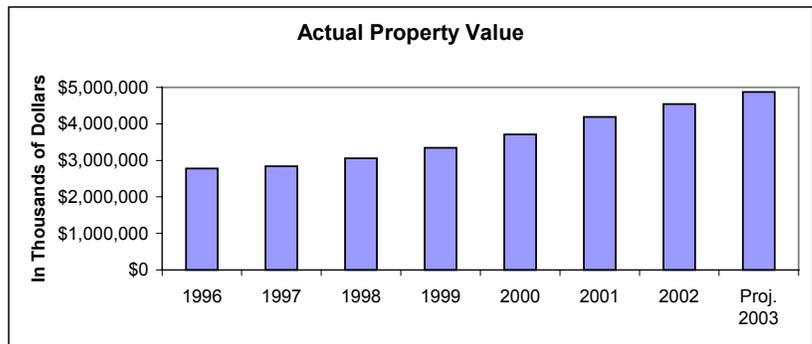
The nation and the Puget Sound region saw a dramatic economic decline in 2001 and 2002. Although indications are that the national economy is emerging from recession, the Puget Sound economy is still struggling. Local economists agree that the economic recovery in the Puget Sound region will lag behind the National recovery. Employment in the Puget

Sound region is unlikely to return to its pre-recession peak until 2005. Housing starts are projected to have negative or minimal growth over the next few years. One bright spot is retail sales activity is projected to grow at a more normal growth rate by 2004.

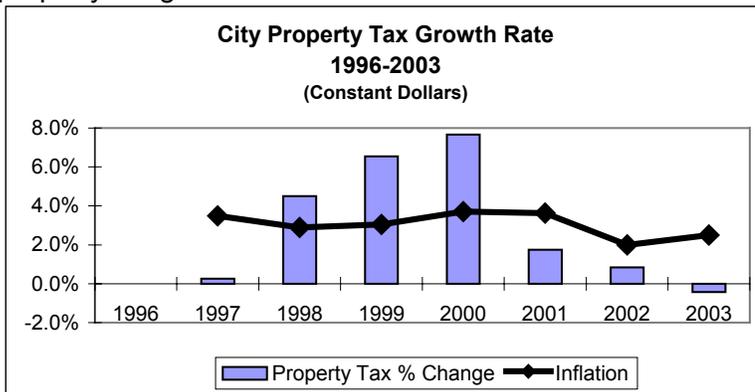
The bleak economic outlook for the Puget Sound region for 2003 has reinforced the need to be conservative in our revenue forecasting. Overall the City's operating revenues are projected to decline 3.3% in 2003. In 2002 the State Legislature eliminated the Motor Vehicle Excise Tax (MVET) backfill, of which the City was eligible to receive \$1.5 million. Sales tax is projected to grow at a meager 1% in 2003. As a result of Initiative 747 (I-747) and reduced development activity, property tax revenues will grow by less than 2%.

Utility taxes and franchise fees are the one bright spot in the City's revenue forecast. Utility taxes are projected to grow by 13% as a result of increased collections from telephone and garbage utilities. On the other hand, utility tax collections from Puget Sound Energy (natural gas) are declining as a result of lower utility rates. Franchise fees are projected to increase by \$725,000, or 43%, primarily a result of a franchise agreement between the Ronald Wastewater District and the City. This agreement provides an additional \$350,000 in franchise fees to be distributed to the City in 2003. The agreement includes annual growth in 2004 of \$50,000 and 3% annual growth thereafter. The remaining increase in franchise fees is a result of collections from Seattle City Light. Seattle City Light had significant rate increases in 2001 as a result of changes in electric markets. In order to deal with the skyrocketing power prices, Seattle City Light applied a surcharge to its rates to repay the money borrowed. These surcharges are scheduled to end in mid-2004. As a result, the City is treating these surcharges as one-time monies.

Each year, the King County Assessor provides the assessed value of property in the City. Since 1996, the City's assessed value has increased 75%. When the assessed values are adjusted for inflation, the increase is 42%, equating to an average annual increase of 5.2%.



Property taxes represent 23% of the City's operating revenue. The proposed 2003 budget includes a 1% property tax levy increase, with an additional .7% of property tax revenue generated from new construction. The 1% levy increase is the annual limit as a result of the passage of I-747 by voters in 2002. Although the 2003 proposed budget provides for increased property tax revenues on a real basis, when adjusted for inflation, the City has had property tax revenue growth below inflation since 2001 and in 2003 will have negative property tax growth.



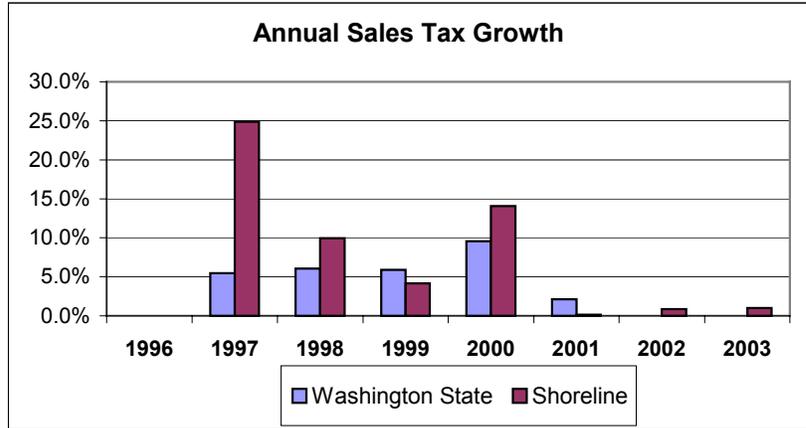
The projected tax levy rate for 2003 is \$1.36 per \$1,000 valuation, a reduction from the 2002 rate of \$1.44 per \$1,000 valuation. The owner of a home valued at \$220,000 in

2002 will see the City portion of their property tax increase by approximately \$1.85 in 2003.

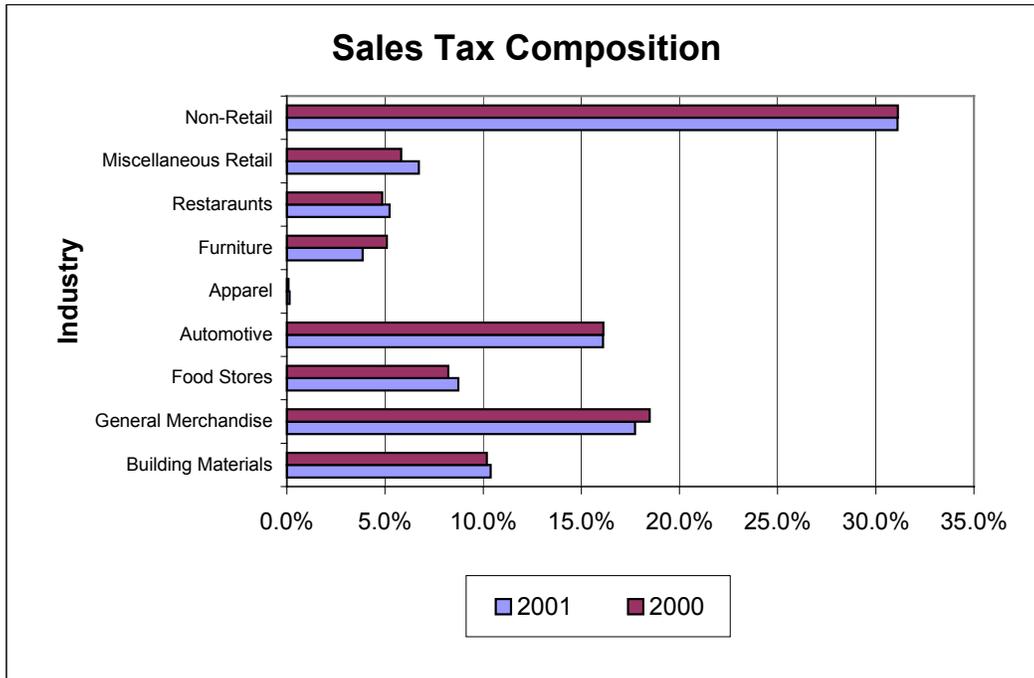
Sales tax, the second largest revenue source for City operations, totals \$5.2 million for 2003.

The City is seeing some growth in sales tax collections, although the growth level is significantly lower than the growth in previous years. As of the end of July 2002, the City's 2002 sales tax growth

compared to 2001 is only 1.8%. Annual growth since 1996 averaged 7.9%. In fact the overall growth in sales tax from 2002 to 2003 is projected to be only 1%.

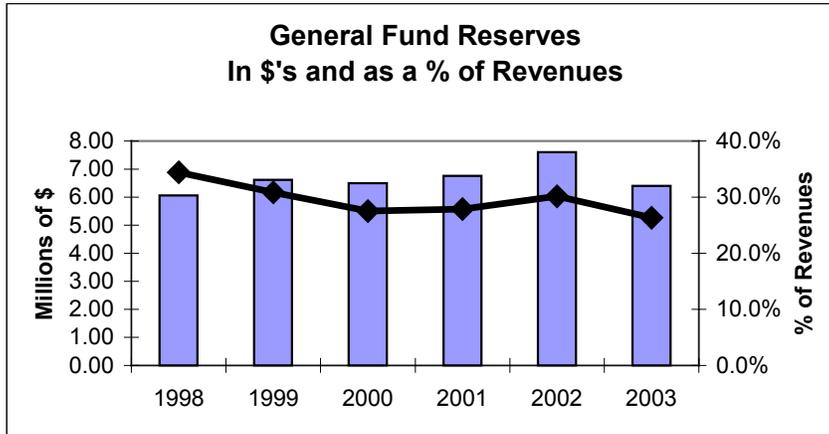


Although the sales tax growth rate in Shoreline is minimal, the City has fared much better than many other cities in the Puget Sound region. Many cities have seen negative sales tax growth over the last two years. Shoreline's tax base consists largely of basic consumer goods. Automobiles are the most significant luxury item in the Shoreline sales tax base, and these sales will need to be monitored throughout the next year.



Reserves

The City saves a portion of its revenues in reserve funds. These funds are used to continue providing services when the economy weakens, to cover one-time expenditure needs and to



meet unforeseen emergencies. To demonstrate prudent financial management, Council adopted a policy of maintaining general reserves (General Fund and General Reserve Fund) at 10% of operating revenues. At the end of 2003, the City's general reserves are projected to total \$6.4 million or 26.3% of

projected General Fund operating revenues. The drop in reserves from 2002 to 2003 is the result of the planned use of \$1.6 million in reserves for 2003. \$1 million of reserves will be used for the City Hall project, \$505,000 is budgeted for emergency contingencies, and the remaining \$77,000 is for the one-time purchase of two maintenance vehicles and start-up costs for new staff positions.

Fee Adjustments

To continue the City Council's 1999 action to systematically review and adjust all service fees, the proposed 2003 budget includes inflationary adjustments to land use and non-building permit fees in the community development and public works areas. The hourly rate used to generate development fees will increase from \$119 to \$121. Building permits are based on the most recent edition of the Uniform Building Code adopted in the State Building Code, which provides for inflationary increases. Recreation class fees will continue to be based on the cost of providing the class plus an overhead charge. The 2003 recreational rental fees have been converted from a per event fee to a per hour fee. This will not change the fee a user pays, but more consistently matches the method in which rentals are booked and accounted for. Aquatic fees have been increased based on market comparisons to other jurisdictions. These increases are anticipated to generate less than \$5,000 in additional revenue.

The most significant fee change is a recommended 20% increase in surface water fees. The fee increase is needed to provide resources for the operation and maintenance of the City's storm sewer system and to support drainage improvement projects in the Capital Improvement Plan. King County implemented a similar increase in 2001. This fee increase will result in residential rates going from \$85 per year to \$102 per year. The CIP includes funding for a Surface Water Master Plan that will establish the long-term revenue needs for the storm sewer system. The proposed 2003 fee schedule is included in the Appendix of this budget document.

Operating Service Level and Expenditure Recommendations

In preparing the 2003 budget, a base was established for operating departments to provide the same service levels as provided in 2002. The 2002 adopted operating budget served as the starting point of developing the 2003 base budget. The 2002 adopted budget contained \$1.5 million in non-recurring expenditures in such areas as the technology plan, one-time

expenditures, and carry-over items from 2001. Finance staff identified approximately \$600,000 in known expenditure increases that need to be funded in order to provide the same services in 2003 as in 2002. The major areas of change in expenditures are as follows:

- **Police Contract:** The City contracts for police services through the King County Sheriff's Office. This contract will increase by \$77,765 or 1%. One of the primary reasons for the low growth rate is the City will be changing the method used to purchase canine services from support services to call-out purchase. Traditionally the City has purchased these services as "support services" resulting in a canine unit almost always stationed in Shoreline. The 2003 projected cost for purchasing this service in this manner is \$150,000. The City averaged 200 canine calls per year over the last three years. The per call cost of this service is \$168. Using the average of 200 calls at the \$168 rate, the call-out cost of purchasing canine services should be \$33,600, a \$116,000 savings. A significant change in service level is not expected as there are mutual agreements with surrounding cities that have canine units, but the City could be in a situation in which either there is a significant time delay or a canine unit is not available for response. If the change in purchase method of canine services had not been made, the police contract would have increased by \$194,000 or 2.8%. This is still an exceptionally low rate of increase.
- **Personnel Services:** The importance and value of our current employees cannot be overemphasized. The budget reflects employee salaries and benefits consistent with the City's compensation policy. Based on the results of a survey of comparable jurisdictions, the proposed budget includes a recommended market adjustment of 1.4%, a 17% increase in the health care insurance premium allowance, a 1% increase in state retirement contributions for six months, and provision for anticipated merit increases. The total budget impact of these changes is \$412,000, or a 4.5% increase in personnel costs compared with 2002 salaries and benefits.

Offsetting these increases is an improvement in the method of allocating staff to operating and capital projects. As a result of these improvements, salaries were not duplicated in the operating and capital budgets. This resulted in a reduction of \$216,000 of budgeted salaries for project engineering staff.

- **Utilities, Maintenance & Facilities:** These costs are anticipated to increase by \$25,000.
- **Liability & Property Insurance:** The City's liability and property insurance premiums are determined by a combination of worker hours, loss experience, and insurance rates. The City's worker hours have increased significantly over the last three years, as well as the fact that the insurance industry is experiencing significant increases in premium costs. The City's liability and insurance premiums are expected to increase by \$15,000 from 2002 to 2003.

Once the base budget was developed and balanced, it was determined that there was approximately \$126,000 available to provide new or enhanced services on an ongoing basis. Our long-term projections show annual operating budget deficits starting in 2004. With this in mind, I knew that we needed to make attempts to limit new, ongoing commitments and to examine our expenditures for possible reductions. This became even more evident when, in the first week of October, Puget Sound Energy announced another 12.5% reduction in natural gas rates; as a result we reduced our natural gas utility tax revenue projections by \$162,000.

The 2003 proposed budget includes increased service levels in the areas of traffic engineering, capital project support, traffic enforcement and legal services. Reductions in funding for sub-area planning, technology plan oversight training, contingency funding for professional services and street crime investigation are also included. The net impact of these budget changes is a \$180,000 reduction in on-going operating costs. These changes are described in more detail below:

- **Traffic Engineering (Net Budget Impact – \$14,000 Savings):** One of the City's priorities has been to increase the service levels in the area of traffic engineering. This is crucial to the implementation of the City's CIP and general transportation plan. The City has traditionally purchased these services from King County or through professional services contracts. The 2003 proposed budget recommends funding for a Traffic Engineer and a Traffic Engineering Technician. The total cost of these positions for 2003 is \$138,000 (\$131,000 on-going, \$7,000 one-time). The net budget impact is actually a net savings of \$14,000. This is a result of the elimination of the Utility Coordinator position (currently vacant) and reduction in contract services.
- **Capital Project Support (Net Budget Impact - \$5,400):** One of the Council's top priorities is the completion of projects in the City's CIP. In order to assist with the attainment of this goal the 2003 proposed budget includes an Engineering Technician fully funded within the CIP and an Administrative Assistant dedicated to the Aurora and Interurban Trail projects. Both of these positions will be funded with existing CIP dollars and will be eligible to be charged against any appropriate grants. The cost of these positions is \$121,000, with \$15,000 representing one-time costs.
- **Legal Services (Net Budget Impact - \$39,000):** The City has operated with a single attorney in the City's Attorney Office since incorporation, supplemented with external contracts. Although we have excellent staff in this position, the City's need for more legal assistance has been demonstrated by increased litigation, increased environmental concerns with project implementation, and the increased activity level of all departments. In order to meet the City's needs, I am recommending we hire a .75 FTE Assistant City Attorney. The total cost of this position is \$66,000. Part of the cost will be offset by a \$27,000 reduction in contract services. We believe some of the services previously contracted out will be completed in-house at a lower cost and more responsive to department timelines.
- **Traffic Enforcement (Net Budget Impact - \$1,682):** The 2003 proposed budget recommends eliminating one street crime detective and increasing the patrol unit by one position. This would leave a Street Crime unit of two detectives and one sergeant and increase the number of officers dedicated to traffic enforcement from three to four. There is currently one vacant street crime detective position. The street crime unit has been very successful in reducing street crime activities and as a result the number of narcotic activity reports has substantially declined. For this reason, although the shift in resources will impact the Street Crimes unit, I don't believe it will have a negative impact on our community. The increase in resources for traffic enforcement is consistent with Council and community desire for greater traffic enforcement.
- **Operation Budget Reductions (Net Budget Impact - Savings of \$280,000):** Major budget reductions include eliminating funding for sub-area plans (\$75,000), reducing technology plan training (\$20,000), and reducing records management software project costs (\$60,000). The changes in the technology plan should not negatively impact the projects to be implemented through that program. Other reductions include reducing

funding for contract services in the areas of code enforcement, on-call biologist services, and street sweeping services, for a total of \$30,000. As was previously discussed the change in purchase method for canine services will save the City between \$90,000 and \$116,000 in 2003.

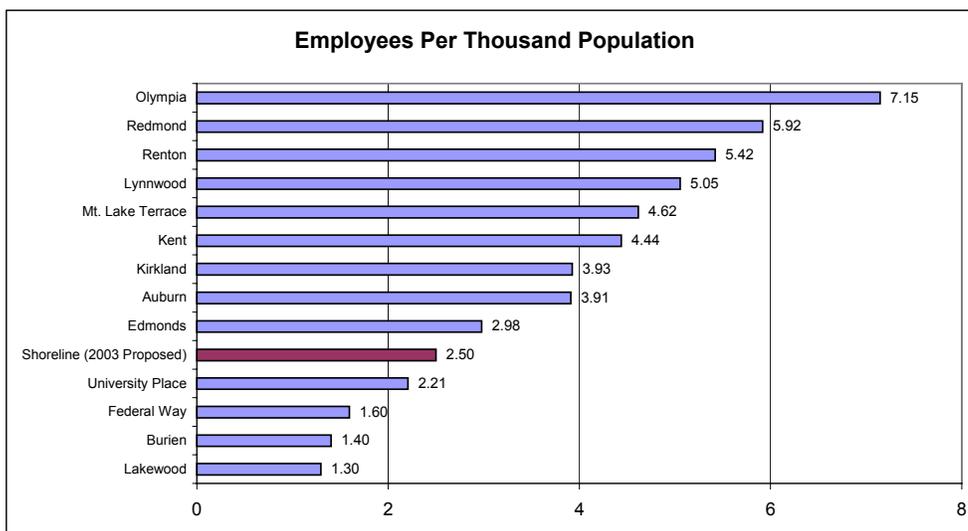
Additional detailed information on 2003 service level changes can be found within the individual department sections of this budget document.

State of Washington and King County Impacts

The State and King County are again facing budget deficits. In 2001 the State Legislature eliminated the Motor Vehicle Excise Tax backfill monies to cities. Shoreline was eligible for approximately \$1.5 million in backfill funds, of which \$500,000 had been programmed for on-going operations. In 2002, the County reduced funding for human services, resulting in increased requests to the City to replace this funding. The City allocated an additional \$100,000 on a one-time basis in 2002 to help meet these needs. This additional \$100,000 in funding is not included in the 2003 proposed budget. The County has notified the City that they will terminate our Municipal Court agreement in 2004. The City is working with other jurisdictions to determine the most appropriate way to provide these services. The City may see additional impacts as a result of the State and County budget deficits, but it should be noted that Shoreline residents continue to contribute a large part of their tax dollars to the County and State.

Staffing

The 2003 proposed budget provides funding for 133.15 regular full-time equivalent (FTE) positions. Of these, 4.75 FTEs represent new positions discussed above (Traffic Engineer, Engineer Technician (2), Administrative Assistant, Assistant City Attorney). With the addition of these positions, the City's ratio of employees per 1000 population is only 2.5. As the graph below depicts, a comparison of staffing to population ratio, based on year 2002 information, still shows the City of Shoreline staffing significantly below comparable cities.



These ratios have been adjusted to **exclude** fire, police, special program and utility personnel from comparable cities.

One-Time Expenditures

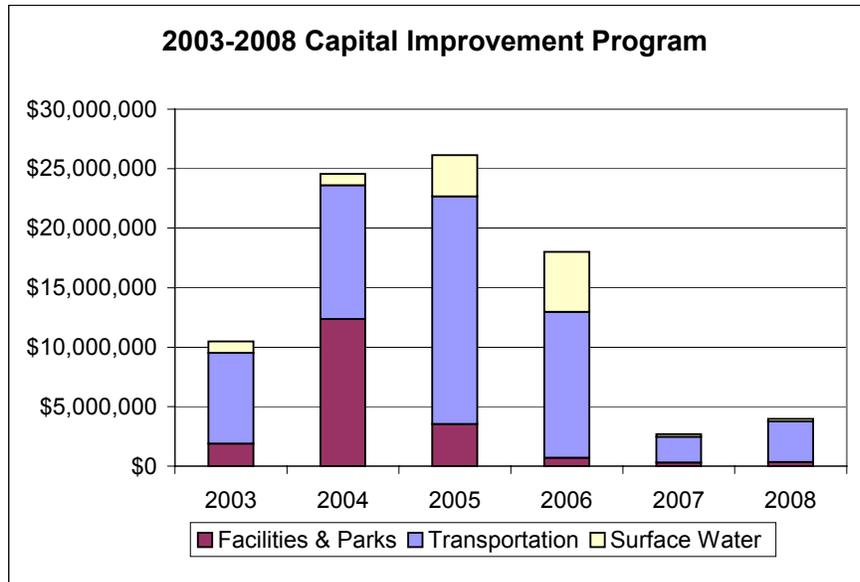
The 2003 proposed budget includes \$1.077 million in one-time expenditures. The largest portion is the allocation of \$1 million in General Fund reserves to the City Hall project, included in the City's CIP. This will provide a total of \$4 million in cash that can be applied toward this project. Other one-time expenditures total \$77,000 and include the cost for two

maintenance vehicles (\$51,000) and funding for start-up costs for the new positions previously discussed (\$26,500).

Capital Budget

The total Capital Improvement Program (CIP) for 2003 is \$10.5 million, and for the 2003-2008 CIP is \$85.5 million. The CIP covers projects over \$10,000 and includes buildings, land acquisition, park facilities, road and transportation projects, and drainage system improvements. Much of the capital improvement activity is funded through contributions from the General Fund, Real Estate Excise Tax (REET), federal grants, and Public Works Trust Fund loans.

This chart provides a breakdown of the allocation of capital dollars for 2003 through 2008. The change in capital dollars can vary significantly from year to year based on available resources to complete projects and the impact of completed capital projects on the City's operating budget.



Following are highlights from the proposed 2003-2008 CIP projects that are either in progress or will be completed in 2003. Additional information on the CIP may be found in the Capital Improvement Program section of this budget document.

- The 2003-2008 CIP includes funding for the acquisition of a City Hall. Current estimated acquisition cost is \$15.1 million. This is a preliminary estimate, as the project is still in the early planning stages. In 2002, the City will determine space needs and site selection criteria. The design phase should be completed in 2003, with construction beginning in 2004.
- Implementing a Gateway Master Plan to enhance community identity is goal number nine on the Council's 2002-2003 work plan. A total of \$300,000 is provided in the CIP for implementation of this plan, with \$100,000 allocated in 2003.
- The CIP contains funding for several master plans including an update of the City's Recreation and Open Space Plan, Facilities Plan and Transportation and Surface Water System. The total amount for these projects is \$650,000, with \$450,000 allocated in 2003.
- Complete the renovation of the Spartan Gym through a joint agreement with the Shoreline School District. The total expected project costs to the City are \$650,000.
- Develop a master plan for improvements to Cromwell Park. Projected total improvement costs will be \$505,000 with \$35,000 being expended in 2003.
- Annual preservation projects for roads and sidewalks is funded at \$900,000 annually.

- The most significant transportation projects continue to be the Interurban Trail, Aurora Corridor, and 15th Avenue NE Improvements.
 - The Interurban Trail project totals \$5.2 million with \$2.9 million funded in 2003. Of the total \$5.2 million, approximately \$3.2 million will be funded through grants and other agency participation, with the remaining \$2 million funded from City resources.
 - Part of the Interurban Trail will include an overhead pedestrian crossing. This project is estimated to cost \$3.6 million, with \$500,000 to be spent in 2003. This project will be 93% funded by grants.
 - The Aurora Corridor, 145th-165th project, totals \$30.8 million with the expectation that \$1.7 million will be funded in 2003. Of the total \$30.8 million, approximately \$17.9 million will be funded through grants and other agency participation, with the remaining \$12.9 million funded from City resources.
 - The 15th Avenue improvement project totals \$6.5 million, with the expectation that \$900,000 will be funded in 2003. This project is primarily being funded with City resources.
- The City has two major surface water drainage improvement projects: Ronald Bog and 3rd Avenue NW. These projects will be funded with Public Works Trust Fund loans with repayment coming from the surface water fees assessed on all property owners in the City.
 - The Ronald Bog Drainage Improvement project is expected to total \$6.2 million, with \$500,000 funded in 2003. This project should be completed in 2006.
 - The 3rd Avenue NW Drainage Improvement project is expected to total \$3.5 million with \$100,000 funded in 2003. This project should be completed in 2006.

Other Budget Issues

Health Care Premiums: The City has seen double digit increases in the cost of health insurance premiums over the last two years with rate increases of 13% in 2002 and 17% in 2003. The City will spend approximately \$1.2 million on health insurance coverage for employees in 2003. This represents approximately 3.5% of the City's operating budget. This is an important benefit for employees and represents approximately 13% of the City's personnel costs. The City is committed to providing a competitive compensation package in order to retain a professional and committed workforce, but at the same time the City must balance personnel costs with its ability to pay. During 2003 I will be working with employees to identify options for providing health care coverage and how the City and its employees can equitably share in this cost.

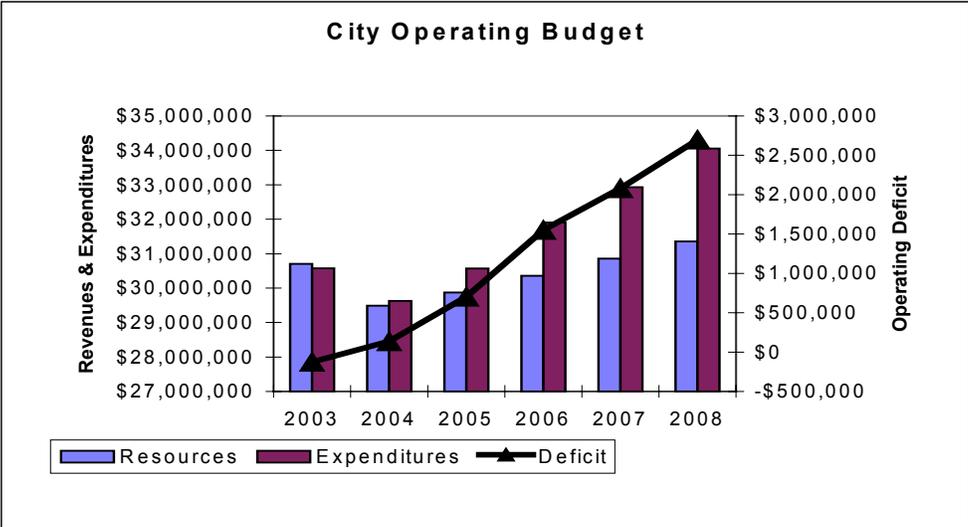
Initiative 776: The Secretary of State has certified Initiative 776 (I-776) to be on the November 5 general election. Passage of I-776 would eliminate the local \$15 vehicle license fee collected by King County and distributed to cities based on a per capita formula. This would eliminate approximately \$500,000 in annual revenue for the City that is currently dedicated for transportation system maintenance and improvements. This revenue represents approximately 30% of the funding for the direct costs of our street operations budget. If passed the initiative goes into effect in December 2002. Since the vehicle license fee is restricted to transportation system expenditures, the City would need to reduce these costs by approximately \$500,000 per year beginning in 2003. It is likely that the City would need to reduce the resources currently allocated to annual road preservation and sidewalk programs, reduce street sweeping activities, consider street lighting options and reduce resources for the City's tree maintenance program.

Our Financial Condition and Future Challenges

The City's current financial condition is excellent. Over the last five years, the City's revenue collections have exceeded expenditures as a result of conservative financial planning, efficient management, restraint from using budget savings as a way to fund on-going operations and modest budget increases. The City is well positioned to respond to changes in the economy, but, at the same time, a prolonged decline in revenues would require the City to reevaluate its service in order to maintain a strong financial position.

Although the City reviews the long-term position of all funds, the primary focus is on the long-term financial position of the City's operating budget. The City is entering a time-period in which annual expenditure growth is projected to outpace annual revenue growth. The following graph depicts projected annual revenues, expenditures, and operating budget surpluses or deficits for 2003 through 2008 using the following assumptions:

- **Property Tax Revenues:** Annual increase of 2% (1% levy and 1% new construction)
- **Sales Tax Revenues:** Annual increase of 2%
- **Utility Tax Revenues:** Annual changes vary between one and three percent annually, depending on the utility,.
- **Other Revenues:** Annual changes vary, between zero and three percent annually depending on the source.
- **Expenditures:** Future year expenditures use the 2003 proposed budget as a base. Future years provide for an overall increase in personnel costs of 4%, a 5% annual increase in police contract costs and a 4% annual increase in jail contract costs, a 5% annual increase in park and public works maintenance and beginning in 2005 an additional \$320,000 per year for facility occupation costs. In 2004 the technology plan has been reduced to \$300,000 annually and in 2007 this amount drops to \$250,000 annually. No additional staffing positions are included.
- **Capital Improvement Program Projects:** The long-term projections take into account the projected operating impact of the CIP projects.
- **Transfers to Capital:** An equivalent to the gambling tax received in excess of a 7% tax rate is transferred from the General Fund for capital purposes. This amounts to nearly \$1 million dollars annually. Also any revenues collected from utility taxes that are considered "surcharges" are treated as one-time revenues and transferred to capital funds.



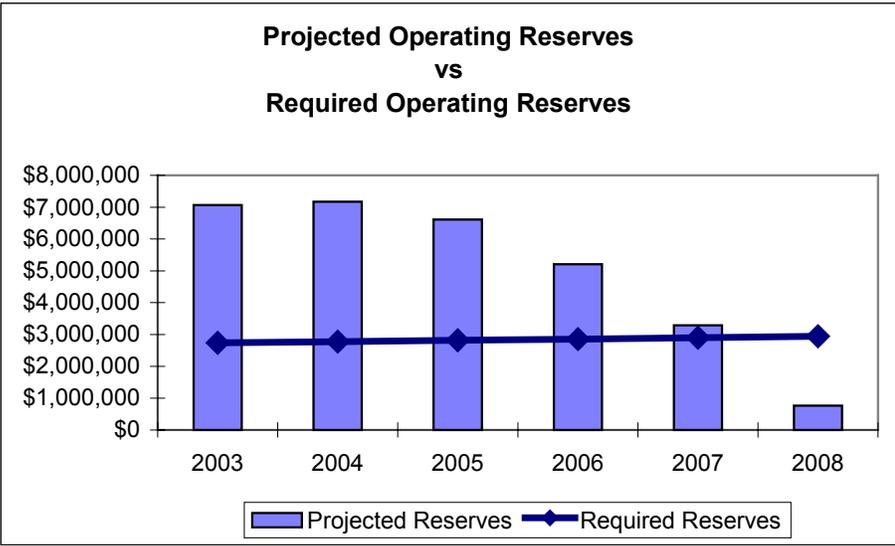
An operating budget surplus or deficit can be defined as the difference between annual on-going revenues and annual on-going expenditures. The City's budget policies

dictate that the operating budget be balanced on-going revenue sources, unless a policy decision is made to use reserves in an emergency or as a one-time event.

As seen in this graph, the City has an operating surplus in 2003 of approximately \$130,000, but in 2004 the City is projecting an operating deficit of \$135,000. This trend continues into the future with annual deficits increasing significantly starting in 2005.

In 2002, the Council began a review of alternative revenue sources. The proposed 2003 budget does not include any new revenue sources reflecting Council consensus. The 2003 proposed budget contains some resource priority changes and reductions in operating expenditures from previous years. As the City looks forward to 2004 and beyond choices will need to be made on how to balance the budget with either additional revenue sources, additional expenditure reductions, or a combination of the two.

Although long-term projections are somewhat sobering, as a result of the Council's conservative financial management, our reserve levels are sufficient to give the City time to



make the required policy decisions. This graph provides the long-term impact of reserves assuming the projected operating budget deficits.

As can be seen from the graph, the operating reserve requirements are met through 2007. Although this is the case, the City can not use its reserves

to balance its operating budget for the long-term. Staff will continue to monitor revenues and expenditures and evaluate services in the context of maintaining a healthy long-term financial position.

Conclusion

This budget is an effort to comprehensively address the City's service and capital investment needs for 2003. It does not satisfy all the demands placed on the City, but it addresses the top priorities identified by the Council. It does this through conservative revenue estimates, proposing a property tax levy within the confines of I-747, and limiting expenditure growth. The proposed budget provides employees with a compensation package in line with policies established by the City Council.

In presenting the proposed budget to the Council, I would like to acknowledge and express appreciation to the City Leadership Team and their staff for their willingness to submit realistic budget requests and develop alternatives to meet the Council priorities. I would also like to thank the Finance Department for its assistance in preparing this budget. Finally, I would like to thank you, the Council, for the policy direction you have provided for service delivery to our community.

Respectfully submitted,

Steven C. Burkett
City Manager