

CITY COUNCIL AGENDA ITEM
CITY OF SHORELINE, WASHINGTON

AGENDA TITLE: Long-Term Financial Strategy DEPARTMENT: Finance PRESENTED BY: Debbie Tarry, Finance Director
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PROBLEM/ISSUE STATEMENT:

Based on current assumptions, the City's long-term financial projections show that there will be budget gaps starting in 2008. The City's financial policies require that annual operating budgets be balanced between on-going revenues and expenditures. The City Council and staff have been monitoring the long-term projections for several years and have taken steps to maintain balanced operating budgets through service efficiencies and base budget reductions. These steps have resulted in a very lean, yet effective budget to provide on-going government services.

In order for the City to continue to provide the same level of services in the future, as is funded in the 2007 budget, additional resources will need to be approved. If additional resources are not approved then the City will need to reduce services through the reduction of City programs.

Two "short-term" resource options (2008-2009) that were discussed with the City Council during the long-term financial strategy retreat on January 29, 2007 were an increase in the cable utility tax from 1% to 6% and a 6% contract payment on the distribution portion of the Seattle City Light (SCL) electric revenues. In addition to these two revenue recommendations staff will recommend approximately \$125,000 in base budget changes starting in mid 2007. This includes expenditure reductions and fee changes.

During the Council's long-term financial strategy retreat Council and staff discussed pursuing a property tax levy-lid lift vote in 2009 to be effective in 2010 to address the long-term budget gaps. Staff will be working with Council to develop a process to work with a citizen's group to pursue the viability of this proposal.

FINANCIAL IMPACT:

The City's most recent update to the 2007-2012 long-term financial projections show the following budget gaps for 2008-2012:

Expenditure Assumption	Operating Fund Projections					
	2007-	100%		Others	99%	
	2008	Base Projections				
	2007	2008	2009	2010	2011	2012
Annual Revenues	28,360,125	28,905,523	29,995,972	30,481,365	31,027,130	31,696,699
Annual Expenditures	28,360,126	29,667,329	31,131,885	32,358,554	33,911,172	35,238,606
Annual (Budget Gap)/Surplus	(0)	(761,806)	(1,135,913)	(1,877,189)	(2,884,042)	(3,541,908)

In order to close the projected gaps the City needs to identify approximately \$1.2 million in additional revenue sources, expenditures reductions, or a combination of these, for 2008-2009.

The following short-term (2008-2009) solution is recommended by staff:

Proposed Item	2007	2008	2009
Base Budget Changes	\$ 39,000	\$ 125,000	\$ 125,000
Cable Utility Tax*	250,000	500,000	512,844
SCL Distribution Contract Fee**	-	206,250	550,000
Enhanced Human Service (utility assistance) Contribution	-	(25,000)	(25,000)
Net Budget Change	\$ 289,000	\$ 806,250	\$ 1,162,844
Projected Budget Gap	\$ -	\$ (761,805)	\$ (1,135,913)
Budget Change Over (Under) Projected Gap	\$ 289,000	\$ 44,445	\$ 26,931
*Effective Date 7/1/07			
**Effective Date 3% on 4/1/08 and 6% on 1/1/09			

RECOMMENDATION

Although no action is required this evening, staff recommends that Council direct staff to bring back an ordinance to increase the cable utility tax from 1% to 6% and that Council approve a motion to authorize the City Manager to notify Seattle City Light of its intent to collect a contract fee on the distribution portion of electric revenues generated from Shoreline rate payers. Staff proposes that Council take these actions at the Council meeting on March 19, 2007.

Approved By: City Manager *Jm* City Attorney _____

INTRODUCTION

The City's long-term financial projections indicate budget gaps starting in 2008 and continuing into future years. In order to continue providing the same level of essential services to the Shoreline community it will be necessary to implement new revenue sources. Staff has recommended that the Council authorize an increase in the cable utility tax rate from 1% to 6%. Also staff is recommending that the Council authorize the City Manager to notify Seattle City Light (SCL) of the City's intent to collect a contract fee on the distribution portion of electric revenues collected from Shoreline rate payers. In addition to this staff is recommending approximately \$78,000 in base budget reductions, to be effective mid-2007, and \$47,000 in revenue changes as a result of fee adjustments to facility rentals, adult recreation programs, and right-of-way permits in 2008.

BACKGROUND

The City's financial policies require that staff prepare six-year financial forecasts. This allows the City Council to monitor the ability of the City to provide services on an on-going basis and not over commit resources. During the last few years the forecasts have shown that the City would experience budget gaps as expenditure growth outpaces revenue growth.

The last few years the City has been able to close any projected gaps as a result of unexpected revenues (i.e., correction in how the water contract payment from Seattle Public Utilities was calculated), efficiencies and service delivery changes (e.g., jail contract with Yakima, change in employee health benefits, change in method for police canine services), or base budget reductions. As a result of these efforts the City's operating budget is very lean with very little contingency left within the annually adopted budget. Given this if the City is going to provide the same level of services on an on-going basis it is necessary to implement new revenue resources.

Why the Gap?

Basically the projected long-term budget gaps are a result of revenues not keeping pace with the cost of base expenditures such as fuel, supplies, jail contract, cost of living adjustments, etc.

Revenues

The City has four primary sources of revenue to support the City's operating budget:

- Property Tax
- Sales Tax (Local Sales Tax and Criminal Justice Per Capita Sales Tax)
- Utility Revenues (Utility Tax, Franchise Fees, and Utility Contract Payments)
- Gambling Tax

In addition to these revenue sources there are various fees and charges that are collected for specific services such as recreational activities and building and development related revenues. Also the City receives some revenues on a per capita basis from the State of Washington (liquor profits, liquor excise tax, and fuel taxes) and investment interest.

A review of the four primary operating revenue sources shows that most of these revenue sources have either grown at a low rate or have experienced declines as a result of market conditions.

Property Tax: Since the passage of I-747 property tax growth is limited to an annual 1% levy increase plus any new construction. This has resulted in average annual real property tax revenue growth of 1.6%, approximately 1% below the average inflationary growth for the same period. As a result the City's property tax levy rate has fallen since 2000. The City's maximum legal property tax levy rate is \$1.60. In 2007 the City's property tax levy rate is \$1.10 with future projected rates falling to \$1 or less by 2010. In 2007 property tax revenue represents 25.3% of the City's operating revenues and totals approximately \$7 million. Future growth is projected to remain at approximately 1.6% annually.

Sales Tax: A combination of both locally generated sales tax and criminal justice dedicated sales tax revenue represents approximately 27%, \$7.5 million, of the City's operating revenues. Over the last seven years locally generated sale tax has grown on average 3.3% annually, approximately 1% greater than inflation for the same period of time. Future locally generated sales tax is projected to grow annually on average at approximately the same pace, even though inflation is projected at a greater rate. Criminal justice sales tax is projected to grow at a slightly higher annual rate, 4.4%. This is primarily because criminal justice sales tax is collected on a county-wide basis and then distributed to cities on a per capita basis. Sales tax on a county-wide basis is projected to increase more rapidly than sales tax within the City of Shoreline.

One bright spot is the possibility of the positive impact that streamlined sales tax may have for the City. It is hoped that the State legislature will approve the State's participation in the streamlined sales tax project during the 2007 legislative session. The Department of Revenue has projected that Shoreline would see a \$120,000 positive revenue impact starting in 2009 if the project is approved.

Utility Related Revenues:

- **Utility Taxes:** Utility tax revenues represent approximately 11.5%, \$3.2 million, of the City's operating revenues. Utility taxes are collected on natural gas (6%), cable (1%), surface water (6%), and garbage (6%). Currently the City has a program that allows low-income and seniors who qualify for low-income utility rates to be exempt from the City's utility tax on natural gas and garbage. Seniors with low-incomes can also qualify for a 50% reduction in the City's surface water fees and resulting surface water utility tax. The City implemented a utility tax on natural gas, cable, and garbage in 1999 as a result of the elimination of the Motor Vehicle Excise Tax (MVET) which provided the funding for sales tax equalization. At that time the City received nearly \$2 million in sales tax equalization. Changes in utility tax collections are generally reflective of inflationary levels.
- **Franchise Fees:** The City collects a 5% franchise fee on cable revenues. Cable franchise revenues represent approximately 1.8%, \$0.5 million, of the City's operating budget revenues. Revenue growth in this area is primarily dependent on changes in the cable rates.

- **Utility Contract Fees:** Utility contract payments represent 8%, \$2.2 million, of the City's operating revenues. The City collects a utility contract fee from the following utilities:
 - *Electricity:* The City currently collects a 6% contract payment from Seattle City Light (SCL) on electric revenues generated on the power portion of the utility rate. The power portion of the electric revenues generated from Shoreline residents represent approximately 65% of the total electric revenues generated from Shoreline rate payers. The contract payment from these revenues is approximately \$1 million annually. Growth in this revenue source is dependent on changes in the power portion of the electric rate. This portion of the electric rate is expected to remain flat over the next two to three years.
 - *Water:* The City collects a contract fee from both Seattle Public Utilities and from the Shoreline Water District. This contract payment is approximately equal to 6% of the water revenues generated from Shoreline rate payers. Revenue generated from these contract payments total approximately \$0.5 million annually. Changes in revenue from this source is dependent on rate changes for water.
 - *Sewer:* The City collects a utility contract payment from the Ronald Wastewater District. This contract payment totals approximately \$655,000 annually. This revenue source grows 3% annually.

Gambling Tax: The City collects gambling tax from card rooms, pull-tabs, and bingo. In 2006 the City saw a 18% reduction in the gambling tax collected to support general operations. In addition the City's primary bingo establishment discontinued operations in 2006 and pull-tab related tax has dropped significantly. As a result of these changes gambling tax revenues used to support the City's operating budget has fallen by nearly 24%, over \$511,000, annually. At this time there is no indication that the gambling activity level within Shoreline will return to former levels.

Revenue Summary: These four primary revenue comprise over 80% of the revenues used to provide on-going operational services to the Shoreline community. The City's 2007-2012 financial forecast projects overall operating revenue to grow on average at 2.33% for the next five years. More specific information regarding the long-term projection of revenues can be found in the 2007-2012 Operating Budget Financial Forecast (Attachment A) following this staff report.

Expenditures

The City's three primary operating type expenditures include:

- **Personnel:** Salary and benefit costs for the City's employees.
- **Intergovernmental:** Although this category would include any contracts with other governmental agencies it primarily represents the costs for jail services and the City's contract with King County for police services.
- **Services and Charges:** Includes a variety of expenditures such as utilities (electricity, water, natural gas, street lights, telephone), contributions to agencies to provide human services, maintenance services such as landscape maintenance and janitorial services, liability insurance, lease and debt service costs for City Hall and other facilities, printing, postage, memberships and dues

to both city-wide organizations (i.e., Association of Washington Cities, Puget Sound Regional Council, Suburban Cities Association, etc.) and professional organizations, training and costs related to training such as travel and registrations.

Personnel: Overall personnel costs comprise 40% of the City's operating expenditures. Personnel costs are projected to increase on average by 4.6% annually.

Salary costs are projected to grow by 4.2% annually. This increase is linked to the City's compensation policy. The City's salary ranges are adjusted annually to reflect inflationary market adjustments based on 90% of the consumer price index. In addition to this the City has a six-step salary plan within each salary range. Employees who are below the sixth step of a salary range are eligible to receive an annual step increase (4%) based on satisfactory performance. Approximately 50% of the City's employees are eligible for a step increase annually.

Benefit costs are primarily driven by two factors: health premium costs and changes to the contribution rate for the Washington State Public Employees Retirement System (PERS). Health benefit costs are projected to increase by 7.5% annually. PERS contribution rates are set by the State Legislature. Historically the PERS employer contribution rate has averaged 5.5%. Even though this is the case, the legislature approved substantial decreases in the contribution rate in the early 2000's as a result of large investment interest revenues, in fact in 2004 the contribution rate was less than 2%. As the nation experienced a recession and investment returns began to fall, the State actuary had to recommend that rates be increased to fully fund future pension obligations. Currently the employer contribution rate is projected to increase from 3.69% in 2007 to 8.7% by July 2010.

Intergovernmental: Overall intergovernmental costs comprise 37% of the City's operating expenditures. Intergovernmental costs are projected to increase on average by 4.7% annually. As stated earlier, the primary component of intergovernmental expenditures are the jail and police contracts.

Jail costs are projected to increase annually by 5.6%, assuming no additional increase in jail activity levels. Increases are contained within the City's contracts with King County, Yakima County and Issaquah. Attachment A contains more details on the historical changes in jail activity levels.

The major cost component of the City's police contract is personnel. The police contract is projected to increase 5% annually, assuming no change in personnel levels.

Services & Charges: Services and charges represent 20% of the City's operating expenditures. Services and charges are projected to increase on average by 4.5% annually. The primary drivers for these costs are inflation and increased service levels.

Utilities and other services tend to increase as a result of inflation. Also as the City completes certain capital improvements (i.e., facilities, parks or roads projects) there is often an expectation of increased maintenance levels. These costs have been included in future projected costs based on anticipated projects within the City's capital

improvement program. Other costs driven by inflation include human service contributions.

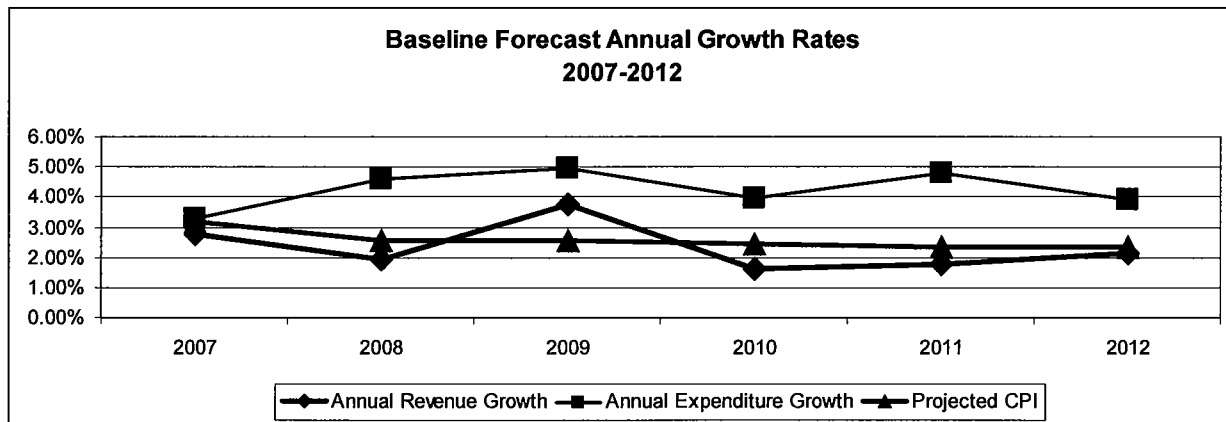
Other services and charges are projected to remain flat such as dues, memberships, and training related costs.

Expenditure Summary: These three categories represent approximately 97% of the City's operating expenditures. Overall expenditures are projected to increase annually by 4.24%. This is approximately 2% more than the annual change in revenues.

Why the Gap Summary

As stated at the beginning of this section, the primary reason for the projected budget gaps is that future base expenditure increases are projected to outpace revenue growth. The following chart summarizes the projected changes.

	2007	2008	2009	2010	2011	2012	Average
Annual Revenue Growth	2.74%	1.92%	3.77%	1.62%	1.79%	2.16%	2.33%
Annual Expenditure Growth	3.27%	4.61%	4.94%	3.94%	4.80%	3.91%	4.24%
Projected CPI	3.20%	2.57%	2.55%	2.44%	2.34%	2.33%	2.57%



Reserves

The City has three types of reserves:

- **Reserves that are legally restricted for a specific purpose:** These reserves are monies that have been accumulated to be used for a specific purpose and legally cannot be used for general operational purposes. These reserves primarily represent the City's savings that are to be used for capital improvements, surface water, and city street maintenance. These reserves totaled approximately \$27.4 million at the end of 2006 and represent approximately 70% of the City's total reserves. The largest reserves in this category are for the construction of City Hall, construction of transportation/road improvement projects, and operation and capital reserves in the surface water utility. The primary revenues that have contributed to these reserves are real estate excise tax, surface water utility fees, and one-time budget savings.
- **Reserves that are designated for a specific purpose:** These are reserves that are earmarked for specific purposes. The origination of the reserves in most

cases came from the general fund, but have been set-aside for specific obligations. These include equipment replacement, unemployment, code abatement, and the 1% for art program. These reserves totaled approximately \$1.9 million at the end of 2006 and represent 5% of the City's total reserves.

- **Unreserved/undesignated operating reserves:** These reserves are established to provide the City stabilization during unforeseen emergencies, temporary economic downturns, and a contingency for unplanned budget expenditures. The City's emergency reserves were approximately \$9.7 million at the end of 2006 and represent approximately 25% of the City's total reserves.

Staff is recommending that Council consider revising the policy for establishing emergency reserves. Primarily staff is recommending that the City's reserve policy focus on the need to establish a revenue stabilization reserve "rainy day account", a minimum reserve to manage cash-flow, and a budget contingency reserve component. It is anticipated that the total reserve to meet these needs will be between \$9 and \$9.5 million. Staff will bring a recommended policy to Council in late March or early April.

ALTERNATIVES ANALYSIS

During the Long-Term Financial Strategy Retreat on January 29, 2007, the City Council considered a number of ideas on how to close the projected future budget gaps. These included:

- Providing opportunities for both employees and citizens to identify ways that the City could gain efficiencies and therefore reduce on-going operating costs.
- Reducing the General Fund contribution to capital projects. Some Council members specifically did not want this reduction to reduce funding for the priority sidewalk program.
- Sponsoring budget town hall meetings
- Increase grant opportunities or use grants to off-set the reduction in capital contribution.
- Increase sponsorship revenues for community events such as Celebrate Shoreline and/or increase advertising revenues by allowing advertising on benches or backstops.
- Increase fees of revenue generating programs to reduce the tax subsidy of the programs
- Reductions to the existing budget in the areas of travel, memberships and dues, special events, and contributions to the arts and museum.
- Develop more intergovernmental partnerships that may reduce costs
- Implementation of a business registration program
- Increasing sales tax revenues through enhanced business retention and economic development efforts
- Implementing additional revenue sources such as cable utility tax and SCL contract payment on the distribution portion of the electric revenues
- Long-term consideration of a property tax levy lid lift.

There was general consensus among the Council that closing the gap strictly with expenditures reductions would not be the recommended option. This would result in the elimination of City services to the community. Based on the feedback the City has

received from the budget and program prioritization workshops completed in 2004-2005, the Citizen's survey, and directly from constituents, it seems that most citizens do not want the City to eliminate existing programs. In fact in some areas there is pressure to increase service levels such as in police services, code abatement, sidewalk maintenance, street lighting, maintenance of City parks, human services and availability of walking and biking trails.

In examining the possibilities to close the projected budget gap for both the short-term and the long-term there was consensus to pursue the following:

Short-Term

- Increase the cable utility tax rate from 1% to 6%
- Implement the Seattle City Light distribution contract payment at 3% in 2008 and an additional 3% in 2009
- Reduce the General Fund contribution to capital
- Review the existing budget for any further cost savings
- Provide opportunities for employees and citizens to identify additional budget efficiencies
- Develop a citizen communication plan regarding the City's long-term financial strategy

Long-Term

- Pursue with a citizen committee the possibility of a levy lid lift (election in 2009)
- Implement the business registration program
- Review the possibility of impact fees

NEXT STEPS

Staff has identified the following items that Council should consider in implementing the City's long-term financial strategy.

Implementing the Short-Term Strategy

Base Budget Changes (\$125,000)

Staff is recommending that Council consider \$125,000 in base operating budget reductions starting in mid 2007. This change would come from approximately \$78,000 in additional base budget reductions and \$47,000 in additional revenues from fee increases.

Base budget reductions will come from the following areas:

Expenditure Reductions

Lobbyist Services	5,000.00	
Parks Maintenance Extra-Help	10,000.00	
Contribution to Facility Long-Term Maintenance	40,000.00	
Travel, Registrations, Dues	13,000.00	
Police Overtime for Neighborhood Traffic Safety	10,000.00	
Total		78,000.00

This base budget reductions will become effective July 1, 2007.

Staff is also reviewing the City's fees and will be considering fee increases in the areas of adult recreation, facility rentals, and right-of-way fees for 2008. The proposed fee changes are projected to generate an additional \$47,000 in operational revenues.

Cable Utility Tax (\$500,000 annually)

The City currently levies a 1% utility tax on cable TV. The utility tax rate on cable TV is governed by the Cable Communications Policy Act of 1984. It requires that the utility rate not be "unduly discriminatory against cable operators and subscribers." Since the City has set all its utility tax rates at six percent, the rate on cable TV could go up to six percent also without being "unduly discriminatory." Although there is no required timeline to implement an increase in the cable utility tax, it is likely that it would take 60 to 90 days for the cable provider to bill all accounts at the increased utility tax rate.

A five percent increase in the cable utility tax would generate approximately \$500,000 in annual revenue. The average residential monthly cable fee is \$57. Implementing an additional 5% of utility tax would cost the average residential customer approximately \$2.83 monthly, or \$34 annually.

The City does collect a 5% franchise fee from the cable provider on total cable revenues. An increase in the utility tax rate would result in a slight increase in franchise fee revenue, approximately \$24,000 annually.

The City Council will need to adopt an ordinance to increase the cable utility tax rate. If there continues to be Council consensus to increase the cable utility tax rate, staff will place an ordinance to increase the cable utility tax rate effective July 1, 2007, on the March 19, 2007, Council agenda.

Attachment B is a list of comparable cities and the utility tax and franchise fee rates that they assess on cable revenues.

Seattle City Light Contract Payment on "Distribution" Portion of the Electricity Utility Rates (Full 6% implementation - \$550,000 annually)

The current franchise agreement between the City and Seattle City Light (SCL) provides that the City receive a 6% contract payment on the power portion of the electricity revenues, but not on the distribution portion. The franchise agreement does allow the City to collect a contract payment, up to 6%, on the distribution portion. In order to do this the City must give a one year notice to SCL. The franchise agreement allows SCL to collect a surcharge on the power portion of rates from our residents, implemented at the same time as the contract fee, but not the distribution portion. Based on recent data provided from SCL for 2001 through 2004, the distribution portion of the electric revenues collected within Shoreline represent 32% of total revenues. Assuming that this revenue allocation has remained constant for 2005 and 2006, it is estimated that a 6% contract payment on the distribution portion of SCL rates would generate approximately \$550,000 of revenue annually.

Assuming an average residential electric charge of \$70 per month, the implementation of the 6% contract payment on the distribution portion of the charge would increase the rate payer's overall bill by approximately \$1.35 per month or slightly more than \$16 per year. Since the full 6% rate would not be in effect until 2009 the rate payer would have

an impact of half this amount, \$0.67 per month or slightly more than \$8 annually in 2008 for a household.

In 2004 the City of Tukwila implemented a contract payment on the distribution portion of the SCL revenues. Tukwila implemented the 6% payment over a three (3) year period.

Seattle City Light does provide reduced rates for low-income and elderly disabled residential rate payers. There are approximately 750 households within Shoreline that are participating in this program at this time. To qualify for the residential low-income rates the household annual income cannot exceed 200% of the poverty level for the number of individuals in the household. To qualify for the residential elderly or disabled rates the household income does not exceed 70% of the Washington State median income for the number of individuals in the household. The electric rates for ratepayers that qualify for these programs are 50% less than the regular rate for base charges and approximately 60% less for energy usage charges.

Shoreline also allows Shoreline residents that qualify for the SCL low-income to be exempt from the City's utility tax on natural gas and garbage. There are currently 150 households participating in this program.

Staff is recommending that as part of the implementation of contract payment on the distribution portion of SCL revenues, that the Council designate \$25,000 of the new revenue be used to enhance the City's human service funding to an agency that provides funds to help residents pay their utility bills. If authorized by the City Council, staff will work with an appropriate human service agency to implement this program.

The City's contract with SCL requires that the City give SCL one years notice to implement the contract payment on the distribution portion of the SCL revenues. Staff recommends that the Council vote by motion, on March 19th, to authorize the City Manager to notify SCL of the City's intent to implement a 3% contract payment on distribution revenues effective March 1, 2008, and the full 6% effective January 1, 2009.

Citizen and Employee Input

Staff will continue to develop opportunities to provide information to the community on the City's budget and long-term financial strategy. This will include articles in Currents and information available on the City's web-site. In addition to this staff will develop additional opportunities for citizens to provide feedback on the City's budget that may include a community workshop, town hall meeting, and ways to communicate efficiency ideas from citizens.

Implementing the Long-Term Strategy

As Council has discussed, undertaking a property tax levy lid lift will require working closely with the community to understand the level of support or concerns that residents may have regarding the City's long-term strategy, their desire for both current and enhanced service levels, and the level of funding that the community is willing to support. It is also imperative that Council, as a whole, support the prospect of placing a levy lid lift on the ballot in 2009. If Council is in support of proceeding with this strategy, staff will develop a proposed citizen's committee process to determine the feasibility of a

levy-lid lift in 2009. In order to maintain current service levels it is likely that the levy rate would need to be proposed at \$1.25. If the Council and community wish to increase services over existing levels a higher rate would need to be considered. Each 10 cent increase in the levy rate would yield approximately \$750,000 in 2010.

Staff will also do further research on the feasibility of implementing impact fees. If it makes sense for the City to implement such fees it will likely be a component of the 2008 budget process.

Staff brought forth a business registration program last year, but it was not approved by Council, staff will wait for Council direction to proceed with a business registration program.

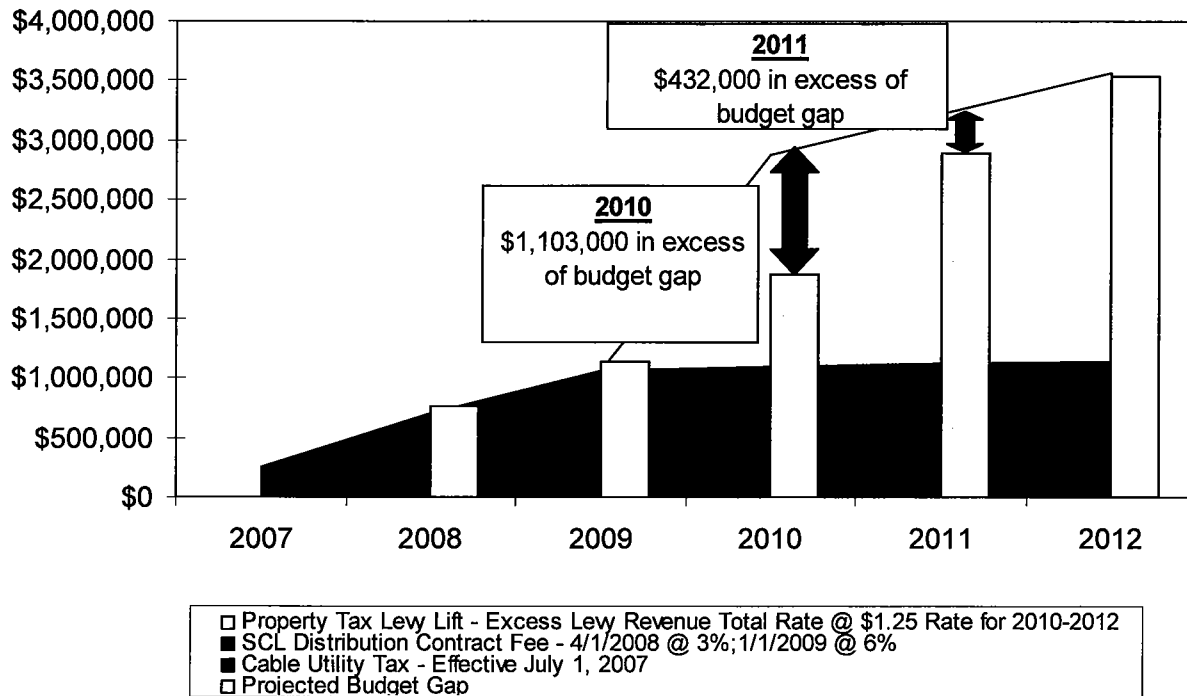
Financial Strategy Summary

Over the last few years the City has been able to provide services and increase some service levels to the community as a result of finding service efficiencies and making base budget reductions. In 2008 the City will not be able to continue providing the same level of services unless additional revenues are authorized. The City has monitored the long-term financial projections for several years and has anticipated that this would be necessary during this time period.

Fortunately the City Council has been prudent and the City has a variety of revenue sources that could be implemented to continue the provision of government services. As staff and Council have discussed the most likely options for the short-term (2008-2009) are an increase in the cable utility tax rate from 1% to 6% and the implementation of a 3% contract payment on the distribution portion electric revenues in 2008 and an additional 3% in 2009. In addition to this staff is recommending approximately \$125,000 in base budget changes as a result of both expenditure reductions and fee increases.

In the long-term (2010 and beyond) it is likely that an increase in the property tax levy will be necessary to maintain service levels.

The following chart compares projected budget gaps to the proposed short-term and long-term strategies.



Proposed Item	2007	2008	2009	2010	2011	2012
Base Budget Changes	\$39,000	\$125,000	\$125,000	\$125,000	\$125,000	\$125,000
Cable Utility Tax*	250,000	500,000	512,844	525,922	538,787	551,378
SCL Distribution Contract Fee**	0	206,250	550,000	564,026	577,801	591,325
Enhanced Human Service (utility assistance) Contribution	0	(25,000)	(25,000)	(25,000)	(25,000)	(25,000)
Property Tax Levy Lid Lift Rate @ \$1.25 for 2010-2012	0	0	0	1,790,809	2,099,579	2,425,530
Net Budget Change	\$289,000	\$806,250	\$1,162,844	\$2,980,757	\$3,316,167	\$3,668,233
Projected Budget Gap	\$0	(\$761,805)	(\$1,135,913)	(\$1,877,189)	(\$2,884,042)	(\$3,541,908)
Budget Change Over (Under) Projected Gap	\$289,000	\$44,445	\$26,931	\$1,103,568	\$432,125	\$126,325
*Effective Date 7/1/07						
**Effective Date 3% on 4/1/08 and 6% on 1/1/09						

RECOMMENDATION

Although no action is required this evening, staff recommends that Council direct staff to bring back an ordinance to increase the cable utility tax from 1% to 6% and that Council approve a motion to authorize the City Manager to notify Seattle City Light of its intent to collect a contract fee on the distribution portion of electric revenues generated from Shoreline rate payers. Staff proposes that Council take these actions at the Council meeting on March 19, 2007.

ATTACHMENTS

Attachment A – 2007-2012 Operating Budget Financial Forecast

Attachment B – Comparable Cities Cable Utility Tax and Franchise Fee Rates

City of Shoreline, Washington

2007-2012 Operating Budget Financial Forecast

Background & Purpose

The National Advisory Council on State and Local Budgeting (NACSLB) has endorsed the forecasting of revenues and the forecasting of expenditures in their Recommended Budget Practices. The Government Finance Officers Association (GFOA) recognizes the importance of combining the forecasting of revenues and the forecasting of expenditures into a single financial forecast. GFOA recommends that each government entity have a financial planning process that assesses long-term financial implications of current and proposed policies, programs, and assumptions that develop appropriate strategies to achieve its goals. The forecast should extend at least three to five years beyond the budget period and should be regularly monitored and periodically updated. The forecast, along with its underlying assumptions and methodology, should be clearly stated and made available to participants in the budget process.

A key component in determining future options, potential problems, and opportunities is the forecast of revenues and expenditures. Revenue and expenditure forecasting does the following:

- Provides an understanding of available funding;
- Evaluates financial risk;
- Assesses the level at which capital investment can be made;
- Identifies future commitments and resource demands; and
- Identifies the key variables that cause change in the level of revenue.

As with any forecasting process, assumptions are made based on historical experience, current trends, and known future changes. Forecasts are usually based on conservative assumptions in that revenues should not be forecast based on maximum growth potential and expenditures should not be forecast based on the minimum growth in expenditures.

The City's financial policies and state law require that the City adopt a balanced budget. This being the case, even though forecasts may project budget deficits, the City would not be able to operate in a budget deficit position on an on-going basis. This is one of the reasons for long-term forecasts, to plan for changes that must occur in order to maintain a balanced budget.

Forecasts and the Budget

The purpose of the long-range financial forecast is to give an early indication of the budget position for the next few years. This forecast is the first step that staff takes in projecting the financial resources that will be available for providing services and for projecting the cost of the current levels of service. As more information is learned during the year and prior to the formal budget process, the forecasts will be updated and the information incorporated into the City's annual budget. The 2007 forecast is equal to the adopted 2007 budget. There are some items that have changed or are expected to change that will affect the 2007 budget, primarily PERS, street lights, and jail, that are discussed in this forecast.

ATTACHMENT A

2007-2012 Operating Budget Financial Forecast

2007-2012 Baseline Operating Budget Forecast

OPERATING BUDGET FORECAST SIX YEAR FORECAST

	2007 Forecast	2008 Forecast	2009 Forecast	2010 Forecast	2011 Forecast	2012 Forecast
Beginning Fund Balance	\$ 10,185,740	\$ 10,185,740	\$ 9,423,934	\$ 8,288,021	\$ 6,410,832	\$ 3,526,790
Revenues:						
Taxes:						
Property	7,066,510	7,236,228	7,354,368	7,472,371	7,590,275	7,708,113
Sales and Use	7,474,500	7,876,148	8,314,216	8,609,667	8,923,328	9,288,888
Gambling	2,134,500	2,273,090	2,264,765	2,256,856	2,249,343	2,242,205
Utility	3,215,000	3,299,269	3,376,192	3,452,782	3,529,057	3,606,810
Other	672	672	672	672	672	672
Franchise/Utility Contract Payments	2,750,595	2,814,030	2,878,659	2,942,917	3,006,838	3,072,020
Licenses and Permits	947,865	956,297	927,199	862,158	822,522	822,676
Intergovernmental	1,772,375	1,823,620	1,854,058	1,884,515	1,914,470	1,944,899
Charges for Services	1,593,750	1,548,539	1,547,870	1,521,119	1,511,993	1,531,451
Fines and Forfeitures	10,000	10,000	10,000	10,000	10,000	10,000
Interest Income	426,355	385,000	385,000	385,000	385,000	385,000
Miscellaneous Revenues	451,732	166,360	166,702	167,036	167,363	167,692
Total Revenue	27,843,854	28,389,253	29,079,701	29,565,094	30,110,860	30,780,427
Operating Expenditures						
Salaries & Benefits	10,738,990	11,349,079	11,821,486	12,364,802	12,905,744	13,471,352
Supplies	643,468	643,501	637,083	637,099	637,115	637,132
Services & Charges	5,505,003	5,566,011	6,451,444	6,601,184	7,041,090	7,202,669
Intergovernmental	9,943,818	10,395,956	10,800,582	11,334,473	11,894,956	12,483,600
Interfund	260,858	263,857	264,242	267,211	270,126	273,095
Debt Service	0	-	-	-	-	-
Other	0	-	-	-	-	-
Capital Outlay	114,000	7,500	7,425	7,425	7,425	7,425
Total Operating Expenditures	27,206,137	28,225,904	29,982,262	31,212,194	32,756,456	34,075,274
Revenue Over (Under) Expenditures	637,718	163,349	(902,561)	(1,647,100)	(2,645,597)	(3,294,847)
Other Financial Sources (Uses)						
Operating Transfers In	516,271	516,271	916,271	916,271	916,271	916,271
Transfers Out	1,153,989	1,441,426	1,149,624	1,146,360	1,154,716	1,163,332
Net Budget Surplus (Gap)	(0)	(761,805)	(1,135,913)	(1,877,189)	(2,884,042)	(3,541,908)
Ending Fund Balance	\$ 10,185,740	\$ 9,423,934	\$ 8,288,021	\$ 6,410,832	\$ 3,526,790	\$ (15,118)
Assumptions						
Inflation	3.20%	2.57%	2.55%	2.44%	2.34%	2.33%
Annual Sales & Use Tax Change	5.93%	5.18%	4.05%	3.38%	3.53%	3.98%
General Fees & Licenses Increase	2.40%	1.93%	1.91%	1.83%	1.76%	1.75%
Investment Interest Rate	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Building Permit Change	-1.60%	1.00%	-5.60%	-12.60%	-9.00%	-0.60%
Revenue Collection	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
PERS Employer Contribution Rate	5.74%	7.42%	8.45%	8.69%	8.70%	8.70%
Health Benefit Escalator	7.50%	7.50%	7.50%	7.50%	7.50%	7.50%
Regular Salary Escalator	4.88%	4.31%	4.30%	4.20%	4.11%	4.10%
Police Contract Escalator	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Expenditure Percentage	100.00%	100.00%	99.00%	99.00%	99.00%	99.00%
New Maintenance Costs for Completed Capital Projects	\$ 175,706	\$ 5,000	\$ -	\$ -	\$ 292,712	\$ -

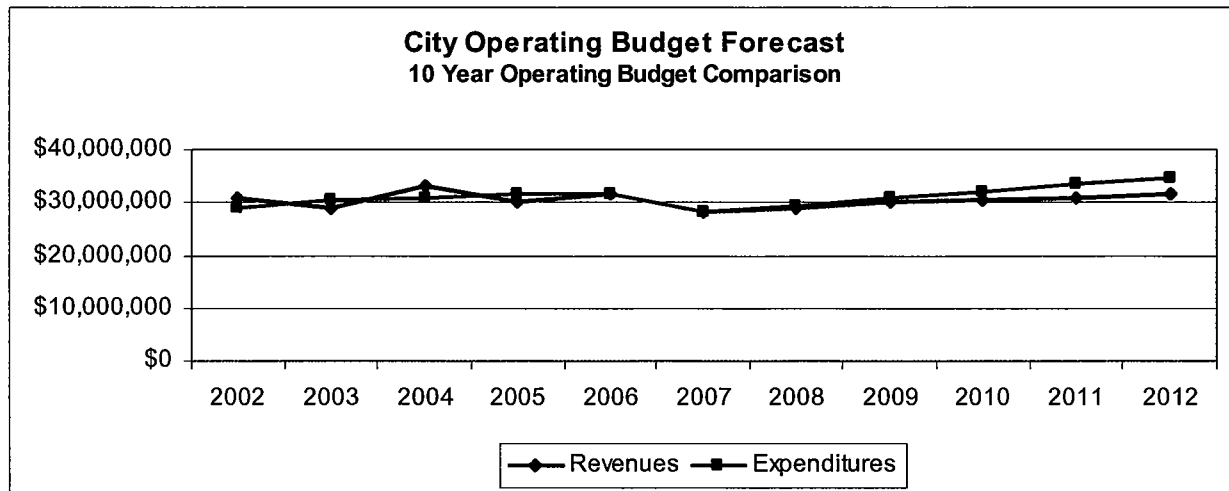
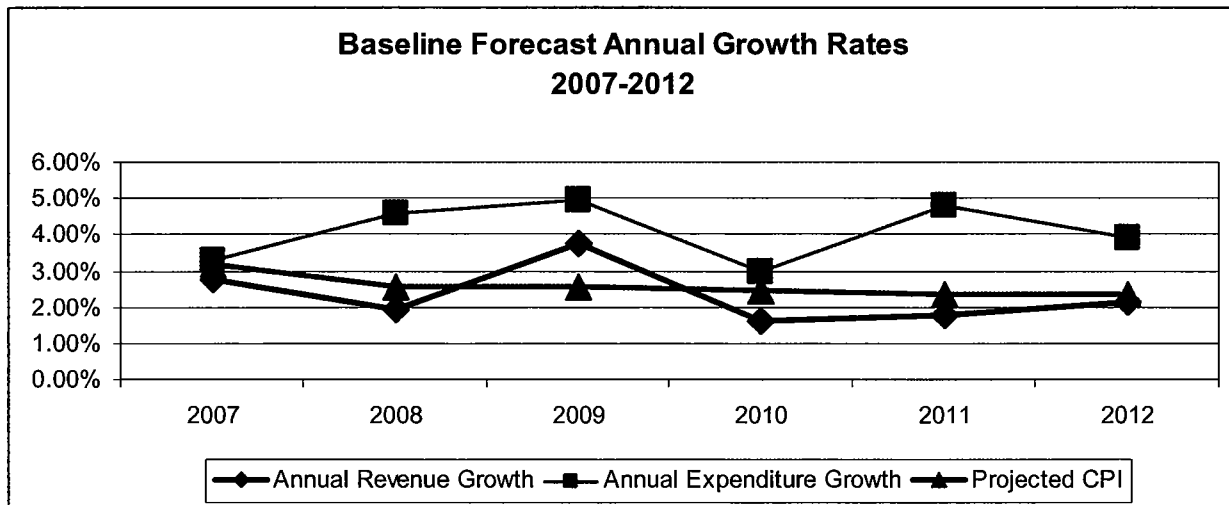
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2007-2012 Operating Budget Financial Forecast

The six-year operating budget financial forecast shows an anticipated 2008 budget gap of approximately \$ 762,000 and a 2009 budget gap of \$1.1 million. Future annual budget gaps grow to \$3.5 million by 2012. This trend is reflective of previous forecasts.

The projected budget gaps indicate a long-term structural imbalance between revenues and expenditures. This is primarily because annual expenditure growth is projected to outpace annual revenue growth. Over the six-year period of 2007-2012 the operating revenues are projected to grow an average of 2.33% annually while expenditures are projected to grow an average of 4.24% annually. Inflation, as measured by the consumer price index, is projected to average 2.57% over the next six years.

	2007	2008	2009	2010	2011	2012	Avg
Annual Revenue Growth	2.74%	1.92%	3.77%	1.62%	1.79%	2.16%	2.33%
Annual Expenditure Growth	3.27%	4.61%	4.94%	3.94%	4.80%	3.91%	4.24%
Projected CPI	3.20%	2.57%	2.55%	2.44%	2.34%	2.33%	2.57%



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2007-2012 Operating Budget Financial Forecast

Historically the City has always balanced annual expenditures with annual revenues. Any surpluses that have resulted from previous years' revenues exceeding expenditures have been allocated for one-time expenditures such as capital projects. The previous graph provides both an historical comparison of revenues and expenditures along with the forecast for 2007 through 2012.

Changes Since the September 2006 Forecast

The September 2006 Base Forecast projected a \$416,000 operating budget gap for 2008, with the annual budget gaps growing in future years. This base forecast projects a larger gap for 2008, but the trend for growing budget gaps in the future remains. Although the trends continue to be the same between the two forecasts, there are some significant changes since September 2006. The changes include the following:

Revenue Changes

Sales Tax: The City receives sales tax directly as a result of sales activity that occurs within Shoreline and from the County-wide 0.1% criminal justice sales tax. It appears that the Puget Sound economy is continuing to expand and all forecasts are for retail sales to grow at a greater rate than previous forecasts for the next two years. The Puget Sound Economic Forecaster published their newest 10 year economic forecast for the Puget Sound region in December 2006. Although the City tends to have a lower overall growth rate in sales tax than the Puget Sound region as a whole during times of expansion and a lower decline in sales tax during times of recession, staff does use this source as a guideline. As a result of the newest Puget Sound economic forecast, projections by the State, and the overall economic health of our region, staff has raised the projected sales tax growth rates for the next six years.

	2007	2008	2009	2010	2011	2012
Annual Growth Rate - 9/2006	4.10%	4.65%	4.58%	3.90%	3.98%	3.98%
Annual Growth Rate - 1/2007		5.18%	4.05%	3.38%	3.53%	3.98%

In addition to the update to the sales tax growth rates, this forecast includes projected sales tax growth from the streamlined sales tax initiative. It is hoped that the legislature will adopt the streamlined sales tax plan along with full mitigation for cities negatively impacted by the change in sales tax sourcing rules during the 2006 legislative session. The Department of Revenue finished updating revenue projections from streamlined sales tax in early January. The City of Shoreline is projected to receive an additional \$120,000 in sales tax annually starting in 2009. This amount grows slightly in future years.

Streamlined Sales Tax	2007	2008	2009	2010	2011	2012
AWC Projections 1/07	-	-	119,500	137,600	145,500	154,100

Property Tax:: Property tax projections have been updated to reflect the final assessed valuation and new construction for 2007 received from King County. The final new construction amount for 2007 resulted in an annual increase in expected property tax of approximately \$50,000.

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2007-2012 Operating Budget Financial Forecast

Business License: The September 2006 forecast included \$90,000 annually in business license revenue. Since the Council decided not to implement a business license program, this revenue has been removed from this forecast.

Expenditure Changes

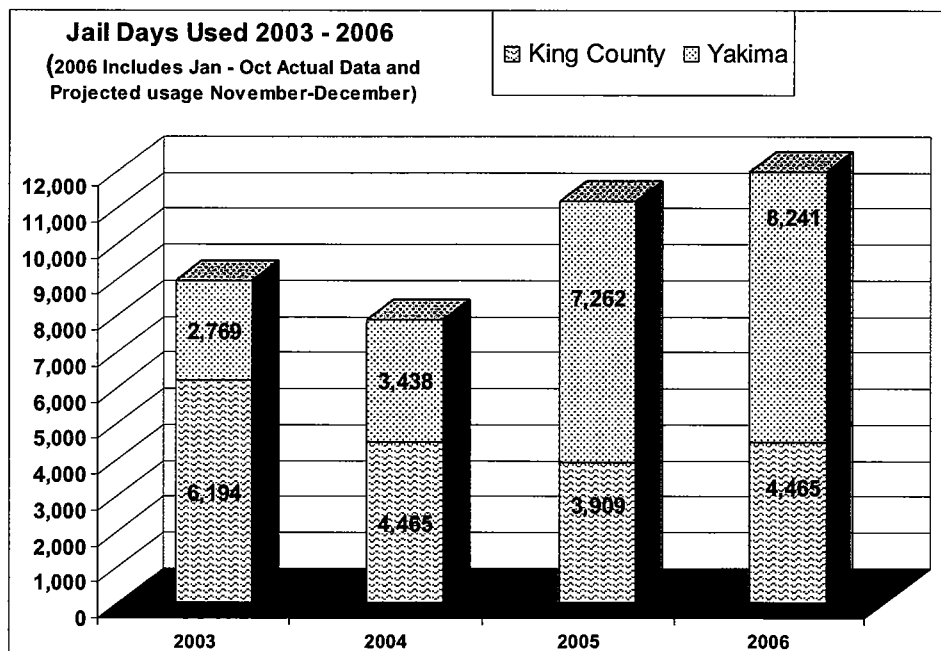
Public Employee Retirement System (PERS) employer contribution rates: In November 2006 the Pension Funding Council (PFC) adopted revised PERS rates for 2007-2009 and the State Actuary updated projections for 2009-2013. The adopted rates include funding for the gain-sharing provisions for both Plan 1 and Plan 3 of the PERS system. Although the Pension Funding Council has adopted the recommended rates for 2007-2009, it is the State Legislature who ultimately adopts the contribution rates. This forecast reflects the most recent rates adopted by the PFC and projected by the State Actuary. The following chart compares the employer contribution rates used in the September 2006 long-range forecast and the rates we are now using in this long-range forecast.

	2007	2008	2009	2010	2011	2012
PERS Employer Contribution Rate - 4/2006	5.74%	6.79%	7.55%	7.48%	7.48%	7.48%
PERS Employer Contribution Rate - 1/2007	5.74%	7.42%	8.45%	8.69%	8.70%	8.70%

As was shared with Council during the budget process, if the State Legislature approves funding for gain-sharing for 2007, the City's 2007 contribution rate will be closer to 6.01%. This will result in 2007 contributions increasing by approximately \$28,000.

As a result of the projected increase in contribution rates, the City's PERS employer contributions from the General and City Street funds will increase by approximately \$60,000 in 2008, \$74,000 in 2009, and \$104,000 in 2010, as compared to the projections in the September 2006 forecast.

Jail: In August 2005 there was a large increase in the number of bed days that the City was utilizing through the jail contracts with King County, Yakima, and Issaquah. This trend has



continued throughout 2006. As of January 24, 2007, we have not received the King County bills for November and December 2006, but the trends for both Yakima and Issaquah were for increased usage during November and December 2006.

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2007-2012 Operating Budget Financial Forecast

The previous chart demonstrates the increase in jail usage from 2003 to 2006. There has been no indication that the increased jail usage trend will reverse. As a result we are forecasting future jail activity to be in line with the usage of 2005 and 2006.

The chart below provides a comparison between the September 2006 and the current forecast for jail costs. The 2007 amount reflects budgeted amounts. If we have the same level of activity in 2007 as in 2006, then the projected actual 2007 jail costs could be \$76,000 higher than the budget.

	2007	2008	2009	2010	2011	2012
Jail - 9/2006	1,225,217	1,245,191	1,312,433	1,383,326	1,458,069	1,536,873
Jail - 1/2007	1,225,217	1,302,111	1,372,199	1,446,080	1,523,962	1,606,060
Difference	0	56,920	59,766	59,754	65,893	69,187

Street Lights: As discussed during the 2007 budget process Seattle City Light (SCL) was considering an increase in the street light rate for 2007. Since there was a great deal of uncertainty regarding the action that SCL and the City of Seattle would take in regards to the street light rates, the 2007 budget did not include an increase in cost. We now know that the Seattle City Council approved a 50% increase in street light rates effective January 1, 2007. The impact of this change is projected to increase the City's annual street light costs by \$79,000 for all existing street lights that the City is paying for. In addition to this, there are 300 street lights that are still in dispute. If the City does become responsible for these additional street lights then it would mean an additional \$31,000, a \$110,000 increase to the cost budgeted for 2007. The 2007 budget for street lights is \$183,000 and the projected actual cost is approximately \$285,000. This forecast includes the street light rate increase for years 2008 through 2012.

Baseline Forecast Overview

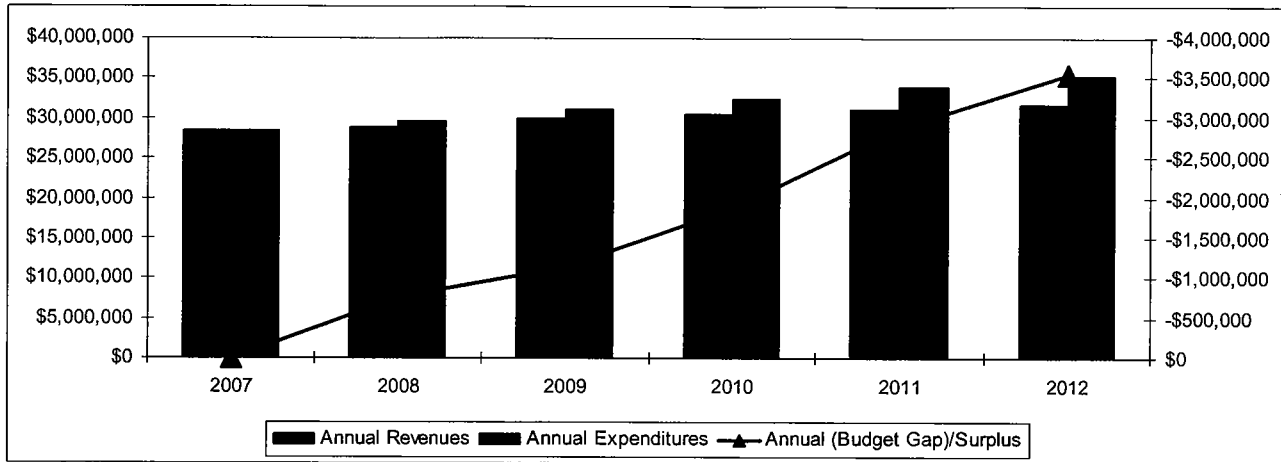
Based on current trends and if there are no changes in revenue and expenditure forecasts, the City's baseline forecast projects an operating budget gap for 2008 and budget gaps continuing for each of the next five years. This trend has stayed consistent during the last few forecast updates. It should be noted that the later years of any forecast are less certain than the earlier years.

The following table and graph demonstrates the City's operating budget baseline financial forecast for 2007-2012.

Expenditure Assumption	Operating Fund Projections					
	2007- 2008		100%	Others	99%	
	Base Projections					
	2007	2008	2009	2010	2011	2012
Annual Revenues	28,360,125	28,905,523	29,995,972	30,481,365	31,027,130	31,696,699
Annual Expenditures	28,360,126	29,667,329	31,131,885	32,358,554	33,911,172	35,238,606
Annual (Gap)/Surplus	(0)	(761,806)	(1,135,913)	(1,877,189)	(2,884,042)	(3,541,908)

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2007-2012 Operating Budget Financial Forecast



Other Scenarios

When there are assumptions that have a distinct possibility to be different than the assumptions in the base forecast, alternative forecasts may be developed. At this time the only assumption that could change the forecast significantly would be that of jail usage.

Operating Budget Description

The City's operating budget is defined as the combination of the City's General and City Street funds. Together, these funds support the general operations that the City provides to its residents and business operators on a daily basis. These include public safety, enforcement of local codes, park and facility maintenance, recreation and cultural activities, street and right-of-way maintenance, planning and community development, development plan review and building construction inspection, community communications, and support services.

Since the operating budget includes multiple funds, there may be questions as to the reasoning for combining the General and Street Funds. The primary reason for combining these two funds is that they are dependent on general tax support. For example, the Street Fund is charged for General Fund overhead support (facility space, support services, utilities, etc.) and at the same time the General Fund allocates a portion of general revenues to the Street Fund to maintain a positive operating position. To balance the Street Fund, approximately \$1.6 million a year in general revenue sources is required. Although from an accounting perspective we are required to maintain two separate funds, in order to simplify the long-term financial analysis of City operations, we have consolidated the two funds and eliminated the interfund transfer of monies.

Capital Improvement Program Impacts

Capital Improvement Program: This forecast focuses on the City's operating budget. Although this is the focus there is some interrelationship. Completion of capital projects many times leads to additional operating costs. For those projects within the current six-year Capital Improvement Program we have included operational impacts into our forecasts.

Forecast Assumptions

The City's budget policies require that on-going expenditures be balanced with on-going revenues. For this reason the six-year financial projections show either a budget surplus or a gap by comparing the annual projected revenues against the annual projected expenditures. There is

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2007-2012 Operating Budget Financial Forecast

no consideration given for available reserves, as reserves are not considered an on-going revenue source.

Revenue Assumptions

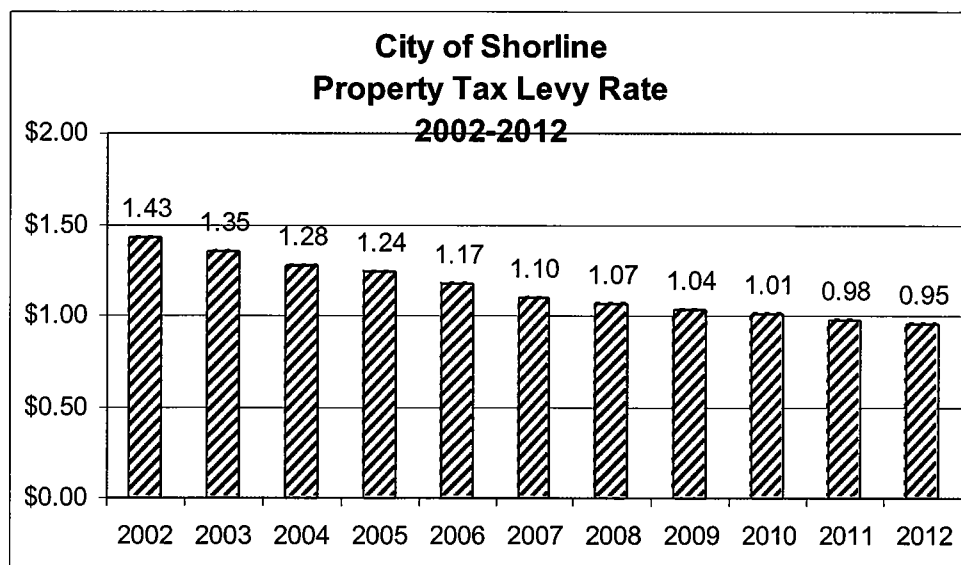
Baseline: Overall revenues are projected to grow by an average of 2.3% annually over the next six years.

The following is more specific information on the most significant operating revenue sources.

Property Tax

Baseline: This assumption does not include any impact of the possible passage of a future property tax reduction initiatives. Property tax growth is limited to an annual 1% levy increase (I-747 limitation) and an annual average of \$43 million in new construction. This results in average annual real property tax revenue growth of 1.6%.

The City's property tax rate is projected to continue to fall over the next six years, as assessed valuation growth outpaces levy increases. The following graph provides the projected tax levy rate for the City through 2012. The City's maximum property tax levy rate is \$1.60. The 2007 property tax rate is \$1.10 and the rate is projected to fall to \$1.07 in 2008.



Each additional 10 cents in property tax levy equates to approximately \$650,000 in property tax revenue. At this time the City has approximately \$.50 in property tax levy capacity equating to approximately \$3.2 million in annual revenue.

Sales Tax

Baseline: Two prominent regional economists, Dick Conway and Doug Pederson, produce a quarterly publication *The Puget Sound Economic Forecaster*. Each year their March issue includes a 10 year Puget Sound economic forecast update. Staff relies on the work that these economists do to help project population, retail sales, and building permit trends. Traditionally Shoreline does not experience the full retail sales growth rates that may be experienced by other localities within the Puget Sound region during periods of growth, but neither do we experience the full decline in retail sales that these same places may experience during a recession. As a result, the City's long-range forecast projects Shoreline's growth at approximately 75% of the

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2007-2012 Operating Budget Financial Forecast

Puget Sound Region as a whole. The following chart compares the Economic Forecaster Puget Sound Region forecast for retail sales growth and the growth factors used in the City's 2007-2012 financial forecast.

	2007	2008	2009	2010	2011	2012
Economic Forecaster Projections 12/2006	7.90%	6.90%	5.40%	4.50%	4.70%	5.30%
City Forecast Annual Growth Rate	5.93%	5.18%	4.05%	3.38%	3.53%	3.98%

Gambling Tax

Baseline: This forecast assumes that card room gambling gross receipts are approximately 20% less in 2007 and beyond than they had been in 2005. This is reflective of the activity level that has been experienced to date in 2006 and was used in preparing the 2007 budget.

The tax rate is assumed to return from 7% to 10% effective April 1, 2007, and remain at the 10% level for all remaining years. This is the same assumption used in developing the 2007 budget. All forecast scenarios assume the continuation of the Council's policy to allocate card room gambling tax revenues generated over a 7% tax rate towards capital. This results in approximately 30% of the City's gambling tax being allocated for capital purposes. Primarily the allocation towards capital funds the pavement management program and contributes towards the City's sidewalk program.

The following chart shows the annual projected card room gambling tax, the amount transferred for capital purposes, and the amount that remains in the General Fund for operational purposes.

	2007	2008	2009	2010	2011	2012
Projected card room gambling tax	1,949,000	2,106,089	2,106,089	2,106,089	2,106,089	2,106,089
Transfer for Capital Purposes	474,075	631,827	631,827	631,827	631,827	631,827
Amount Used for Operational Purposes	1,473,925	1,474,262	1,474,262	1,474,262	1,474,262	1,474,262

Pull-tab related gambling tax revenue has been declining annually. This forecast assumes that this decline will continue over the next few years.

Utility Tax and Franchise Fees

Baseline: Utility tax and franchise revenue increases have been linked to projected inflationary increases. Usually utilities structure their rates to recapture inflation related increases. These increases average approximately 2% annually over the next six years.

Seattle City Light Contract Payment

Baseline: The Seattle City Light (SCL) contract payment is made based on 6% of the power portion of the electric revenue generated from Shoreline rate payers. The 2007-2012 has left the annual base revenue at \$1,000,000 with inflationary increases during the six year period.

Permit Revenue

Baseline: The long-term financial forecast is based on the long-term permit activity forecast for King County from the Puget Sound Economic Forecaster. Over the next few years building

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2007-2012 Operating Budget Financial Forecast

permit activity is projected to decline slightly. We will continue to monitor to determine if projections for King County are reflective of Shoreline activity levels.

Revenue Source	2007	2008	2009	2010	2011	2012
Permits-Building & Structures	455,000	459,550	433,815	379,154	345,031	342,960
Permits-Build/Strict - Plumbing	30,935	31,244	29,495	25,778	23,458	23,318
Mechanical Fees/Permits	65,000	65,650	61,974	54,165	49,290	48,994
Land Use Fees/Permits	230,000	230,000	230,000	230,000	230,000	230,000
Fire System Fees/Permits	13,400	13,534	12,776	11,166	10,161	10,100
Inspection Service-Plumbing	78,000	78,780	74,368	64,998	59,148	58,793
Plan Check Fees	395,000	327,200	308,876	269,958	245,662	244,188
Environmental Review(SEPA/EIS)	25,000	25,482	25,969	26,445	26,909	27,379
Total	1,292,335	1,231,440	1,177,273	1,061,665	989,659	985,733
Economic Forecaster Permit Activity Projections	-1.6%	1.0%	-5.6%	-12.6%	-9.0%	-0.6%

Transfers Into the General Fund

The City receives approximately \$550,000 annually from the capital and surface water funds for overhead charges. The overhead charges represent the capital and surface water share of facility, administration, finance, information technology, legal, and city clerk related charges.

In 2009 and beyond the transfers into the general fund include \$400,000 annually in real estate excise tax (REET) to go towards the debt service payment of City Hall.

Expenditure Assumptions:

Overall expenditures are projected to increase an average of 4.09% annually over the next six years. The six-year forecast assumes that the City will maintain current services and service levels.

Expenditure Rate:

Baseline: As has been the City's experience, it is highly unlikely that 100% of the City's operating budget will be expended in a given year. In 2005 the General Fund expenditure rate was 98% of projected expenditures. The long-term forecast assumes a 100% expenditure rate for 2007 and 2008 and 99% for the remaining years.

Inflation

Baseline: Inflation is projected to average 2.57% annually over the next six years. Inflation is used to project expenditure increases related to salaries, professional service contracts, and intergovernmental contract increases. The following chart reflects the inflationary projections for the next six years.

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	2007	2008	2009	2010	2011	2012	Average
Projected CPI	3.20%	2.57%	2.55%	2.44%	2.34%	2.33%	2.57%

Salaries

Baseline: Market rate adjustments are forecasted at 90% of inflation. It is assumed that 50% of staff positions will be eligible for step increases (4% annually) over the next six years, as currently 45% of our regular employees are at the top of their salary range. This also assumes that there will be some turn-over in current staffing and replacement staff may start lower in the salary range than long-term employees.

Benefits

Baseline: The major changes in benefits are expected to occur in health and retirement benefits. This forecast accounts for an annual increase of 7.5% in health benefit costs for the next six years. Health premium cost increases for 2007 averaged 7.9%.

The employer contribution for the Public Employee Retirement System (PERS) is based on the rates approved by the State Legislature. This chart shows the anticipated employer contribution rates through 2012.

	2007	2008	2009	2010	2011	2012
PERS Employer Contribution Rate - 1/2007	5.74%	7.42%	8.45%	8.69%	8.70%	8.70%

Public Safety

Baseline: The police contract is projected to increase by an average of 5% annually over the next six years. Jail costs have been projected based on historical and recent jail bed usage data. The following table summarizes the data used to forecast jail costs over the next six years.

Jail - Details in Jail Info File with/in LT Forecast Directory	2007	2008	2009	2010	2011	2012
KC Misdemeanor Bookings (Last 3 Year Avg)	680	680	680	680	680	680
KC Misdemeanor Maintenance Days (Last 3 Year Avg)	4,400	4,400	4,400	4,400	4,400	4,400
Yakima Misdemeanor Maintenance Days (Avg of 2005 & 2006)	7,874	7,874	7,874	7,874	7,874	7,874
Unused Bed Days	0	0	0	0	0	0
Issaquah Misdemeanor Maintenance Days (Annualize 2006)	1,233	1,233	1,233	1,233	1,233	1,233
\$ Cost of KC Misdemeanor Bookings	197.23	208.67	220.77	233.58	247.13	261.46
\$ Cost of KC Misdemeanor Maintenance Days	103.29	109.29	115.62	122.33	129.43	136.93
\$ Cost of Yakima Misdemeanor Maintenance Days	71.48	75.05	78.80	82.74	86.88	91.22
\$ Unused Bed Days	0.00	0.00	0.00	0.00	0.00	0.00
\$ Cost of Issaquah Misdemeanor Maintenance Days	68.25	71.66	75.25	79.01	82.96	87.11

Capital

City Hall: All forecast scenarios assume that the City will construct a new City Hall and that debt service payments will begin in 2009. Currently we are estimating annual occupancy costs (debt service/maintenance & operations) to total between \$1.1 and \$1.3 million dollars annually. As approved by the City Council, \$400,000 of Real Estate Excise Tax will be dedicated towards the debt service costs for City Hall starting in 2009.

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2007-2012 Operating Budget Financial Forecast

Operating Transfers Out

Baseline: The 2007-2012 continues to implement Council Policy by allocating a portion of the City's general revenues to fund capital improvements. The forecast also continues build the fund balance of the General Reserve Fund to the 37.5 cents per \$1,000 valuation that is allowed by Washington State Statute. In addition to these allocations, general revenues are allocated for equipment replacement, anticipated unemployment claims and funding for the major maintenance of the City's facilities. This allocation of funds is done through an operating transfer from the General Fund to the fund that accounts for the corresponding types of expenditures. The table below shows the operating transfers that are part of the 2007-2012 forecast.

	2007	2008	2009	2010	2011	2012
Transfer to Unemployment	10,000	10,000	10,000	10,000	10,000	10,000
Equipment Replacement	100,000	100,000	100,000	100,000	100,000	100,000
Roads Capital - Gambling Tax	474,083	631,827	631,827	631,827	631,827	631,827
General Reserve Transfer	0	114,111	118,675	123,422	128,359	133,494
Roads Capital - Sidewalk & Street Overlay	138,919	142,488	146,121	149,690	153,194	156,762
Long-Term Repair & Replace On-going	143,000	143,000	143,000	143,000	143,000	143,000
One-Time General Capital Transfer	288,000	300,000	0	0	0	0
Total Operating Transfers Out	1,153,989	1,441,426	1,149,624	1,157,939	1,166,380	1,175,083

*It should be noted that the summary forecast on page 2 of this documents shows operating transfers for years 2010 through 2012 at 99% of the total. This reflects the anticipated expenditure rate.

General Reserve Fund

Baseline: The General Reserve Fund was established to accumulate monies to be used for emergencies or to moderate economic changes. The amount of reserves that can be accumulated in this fund are limited by state law to \$0.375 per \$1,000 of assessed valuation. Since the City's assessed valuation has continued to increase, and this trend is projected to continue, the amount of the reserve has continued to increase. The reserve increases by transferring general fund revenues to the reserve fund. The long-term forecast continues this policy and an annual average of \$123,000 of operating resources are transferred from the operating budget to the General Reserve Fund. The projected 2006 ending fund balance for the General Reserve fund is \$2.3 million. The General Reserve fund is not adequate to hedge the City against an economic downturn and/or unexpected emergencies.

General Fund Reserve Levels:

The 2006 projected ending fund balance for the General and General Reserve Funds combined totals \$9.6 million, approximately 30% of General Fund revenues. Although reserves can be used to help ease "short-term" economic changes, they cannot be used to balance the City's operating budget for the "long-term". In fact, the City's financial policies state that the budget needs to balance on-going expenditures with on-going resources. Reserves are not considered "on-going resources". This being the case, the City would not use reserves to balance the operating budget on a long-term basis, but the \$9.5 million in reserves would cover the annual budget gaps through 2011.

The City's financial policies require that the City maintain a minimum General Fund reserve level of 10% of general fund revenues. The General Fund reserve is defined as the combination of the General Fund ending fund balance and the General Reserve Fund ending fund balance.

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2007-2012 Operating Budget Financial Forecast

The City's General Fund reserve level is projected to be \$9.6 million at the end of 2006, or 30% of General Fund on-going revenues.

As was stated earlier, the long-term forecast does not assume the use of reserves to close operating budget gaps. If reserves were used to close the projected gaps, the City would have enough to balance the operating budget for the next five years. Since reserves are not considered recurring revenues, the City would be in a very precarious financial situation beginning in 2012 with a budget gap projected at nearly \$3.2 million and no general fund reserves. The real purpose of the reserves is to help address declines in economically sensitive revenues, shifts in revenue sources that are out of the City's control, or to cover cash flow needs which alleviates the need for short-term borrowing. Reserves are available to provide the City with more operating flexibility.

The level of reserves is not mandated by law, but rather is a decision that each jurisdiction makes based on the elasticity of their revenue sources, their cash flows, and their local economy. Moody's Investors Service, who provides bond ratings to many cities and counties throughout the State of Washington, have reported that their clients have reserve levels that range from the teens to close to 50%. Bond issuers outside of the State of Washington often have reserves at significantly higher levels.

Potential Future Impacts

Fire Hydrants: Currently the City is involved in litigation, with a number of other cities and Seattle Public Utilities (SPU), regarding the financial responsibility of fire hydrants. Currently SPU and the Shoreline Water District have the financial responsibility to pay for fire hydrants through water assessment rates. Prior to 2005 SPU embedded the cost of providing fire hydrants and fire flow in the water rates paid by their retail customers. As a result of Washington State Supreme Court action that prevented Seattle City Light from recovering the costs of street lights on public streets through general electric rates, SPU did not feel it appropriate to continue the assessment of fire hydrant and fire flow in their retail water rates. As a result they established separate rates to recover the costs.

SPU initially billed the Fire Districts for these costs in 2005. The Fire Districts refused payment. SPU then billed the cities for these costs. To date the cities (Burien, Kenmore, Lake Forest Park, and Tukwila) have also refused payment while waiting resolution through the legal system.

SPU has estimated the 2006 impact to the City of Shoreline would be \$207,000. Since SPU only provides approximately ½ of the City with water and the Shoreline Water District provides the other half of the City with water, staff has estimated that total fire hydrant and fire flow costs within the City of Shoreline could be \$400,000 to \$500,000 annually. The City has not incorporated these costs into its budget or the long-term financial forecast.

Balancing Prior Year Budgets

In light of the long-term forecasts, our focus over the last few years has been on cost containment, expenditure reductions and improving service efficiencies. Some of our successes include:

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- In 2003 an employee group developed an alternative health benefit policy. As a result of this policy change, the City's health benefit costs in 2006 were \$313,000 less than would have been budgeted under the previous policy.
- We have initiated agreements with Yakima County and Issaquah to house prisoners at a lower rate than is charged by King County.
- We have changed the way we pay for Police Department canine services by purchasing this on a call-out basis instead of having a dedicated unit. This has resulted in annual savings of \$100,000.
- Departments absorbed \$167,000 in baseline budget reductions in 2005 and an additional \$169,000 in baseline reductions for 2007. This was done by reviewing historical expenditure practices and eliminating budget authority that had not been spent in consecutive years.

Since 2003 these changes have equated to \$730,000 in annual expenditures that have been reduced from the City's baseline budget.

In addition to these cost saving measures the City has developed more efficient service delivery methods without increasing budget costs, while enhancing service levels. Examples include:

- In-house athletic field maintenance as opposed to continuing with contract services.
- In-house provision of street sweeping services versus private and County contract.

Balancing Future Budgets

Staff will continue to update assumptions and the City's long-range operating forecast throughout the year as more information is available. This may result in some changes in the long-range forecasts, but it is unlikely that these changes will significantly change the trend of expenditure growth outpacing future revenue growth.

In order to balance future budgets it will be necessary to either reduce expenditures, increase revenues or some of both. During recent years some general operating expenditure reductions have been made, and many of the City's operating costs have been held constant over the last few years. At this time it appears unlikely that additional operating expenditure reductions could be made without either eliminating a specific service or reducing levels of service.

There are three primary revenue enhancement options available to the City for future budgets. The first would be to exercise the City's option to assess the Seattle City Light (SCL) contract payment on the distribution portion of the revenue generated by the Shoreline ratepayers. The City's franchise agreement with SCL allows the implementation of a contract payment of up to 6% of the distribution portion of the electric revenues from Shoreline. SCL is allowed to pass this charge on to Shoreline rate payers. The 6% assessment on the distribution revenues is estimated to generate approximately \$550,000 annually. The City of Tukwila exercised this option with SCL in 2004 and phased in the 6% distribution assessment over the last 3 years.

The second would be implementation of the remaining 5% utility tax authority on the cable utility. Currently the City has a 1% utility tax and a 5% franchise fee on cable. Legally the City can levy a utility tax up to 6% on cable. Each additional one percent is projected to generate approximately \$100,000 in annual revenue, for a total of \$500,000 if the full 5% was implemented.

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A third revenue option is a property tax levy lid lift. As was discussed in the property tax portion of the forecast assumptions, the City's property tax levy rate has fallen since 2002. This is a result of assessed valuation growing more rapidly than the City's property tax levy increases. In 2007 the City's levy rate is approximately \$1.10 per \$1,000 valuation. Statutorily the City could assess up to \$1.60 per \$1,000 valuation. Each 10 cents in property tax levy equate to approximately \$650,000 in annual revenue. A levy lid lift has to be approved by a majority of the Shoreline voters.

Conclusion

Based on the assumptions described above, the City's operating budget is projected to have budget gaps starting in 2008 and into the future. Although the City's long-term projections reflect annual operating gaps, this does not mean that the City will actually operate in a deficit position. Rather, the long-term projections help staff and the City Council anticipate the need to develop long-term solutions to bring the annual operating budget into balance. Although reserves can be used to help ease short-term budget deficits, the projections show that the operating budget has long-term issues that need to be addressed in order to balance the budget on an on-going basis.

The reason for the budget gaps is basically a result of the long-term expenditure growth outpacing long-term revenue growth. Although operating expenditures are projected to increase modestly over the next six years, the growth is slightly greater than projected inflation and greater than projected revenue growth. Revenue growth is projected to be less than inflation for four out of the next six years.

Staff will continue to update the long-range forecast as the City starts its annual budget process. The forecast should be considered a dynamic process as it may change as additional information becomes available. As the City Council considers priorities for the next year and the long-term, the development of a strategy to maintain the City's long-term financial stability must be considered.

ATTACHMENT B

City	Cable TV Utility Tax	Cable TV Franchise
Auburn	No	5.00%
Bellevue	4.80%	5.00%
Burien	6.00%	5.00%
Everett	No	5.00%
Federal Way	6.00%	5.00%
Kent	No	5.00%
Kirkland	6.00%	5.00%
Lake Forest Park		5.00%
Lynnwood	No	5.00%
Mercer Island	7.00%	5.00%
Mountlake Terrace	5.00%	5.00%
Mukilteo	6.00%	5.00%
Olympia	No	
Redmond	No	5.00%
Renton	6.00%	5.00%
Sammamish	No	5.00%
SeaTac	No	5.00%
Tacoma	8.00%	5.00%
University Place	6.00%	5.00%
Woodinville	No	5.00%
Woodway	6.00%	5.00%

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