

CITY COUNCIL AGENDA ITEM

CITY OF SHORELINE, WASHINGTON

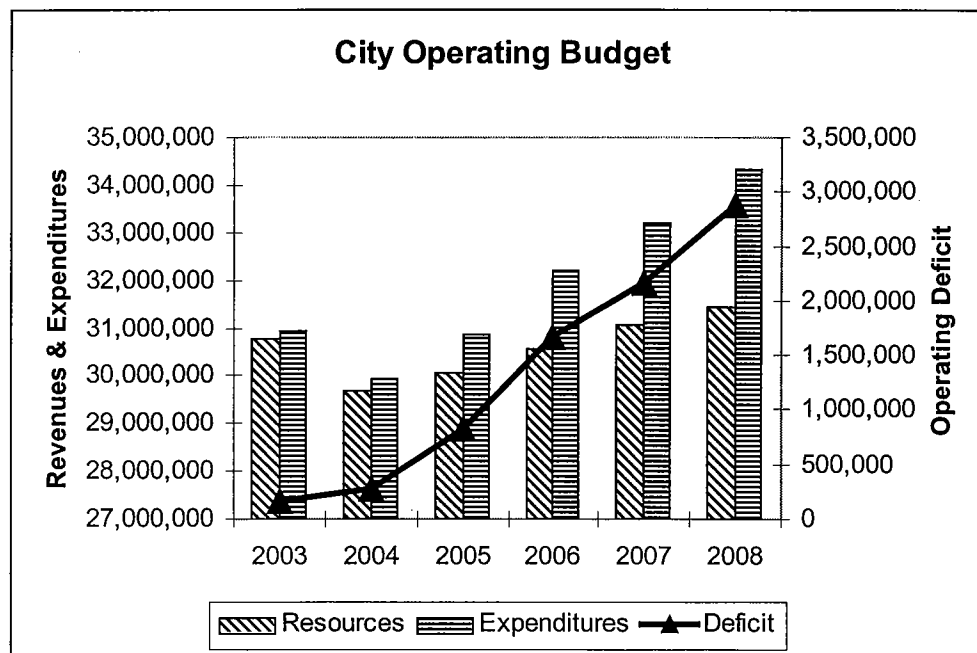
AGENDA TITLE: 2003 Budget Development Update
DEPARTMENT: Finance
PRESENTED BY: Debbie Tarry, Finance Director

PROBLEM/ISSUE STATEMENT:

Staff is currently in the process of developing the 2003 Proposed Budget. Traditionally the City Council has held a budget and planning retreat in August each year. In order to better facilitate goal setting and policy direction in the budget planning process, the Council's Retreat was held in April of 2002. As a result of this change, the financial information shared at the April retreat was not as extensive as that provided in prior years. This workshop will provide an opportunity to provide an update of the financial projections for 2003 and beyond and some of the primary issues that will need to be addressed during the 2003 budget deliberations for the City's operating budget which includes the General Fund, City Street Fund, and the Development Services Fund.

FINANCIAL IMPACT:

As of September 6, 2002, the preliminary 2003 budget has a \$158,000 operating deficit for 2003. This is still preliminary and subject to change as more revenue and expenditure information is gathered. Although staff is confident that we will bring the operating budget into balance prior to the submission of the Proposed Budget, the long-term operating budget is projected to have a deficit each year through 2008. The following graph reflects the long-term projections and the annual operating deficit.



RECOMMENDATION

No action is required by the City Council. This item is for informational purposes and to provide the City Council with preliminary 2003 budget information.

Approved By: City Manager  City Attorney 

INTRODUCTION

Staff is preparing the 2003 Proposed Budget and updating financial indicators and projections as part of the process. This workshop will provide an opportunity for staff to share with the City Council the latest financial projections, along with a discussion on some of the major policy issues that will need to be discussed during the 2003 budget workshop reviews. The Council 2003 budget schedule is as follows:

Budget Development Update	September 16
Transmittal of Proposed 2003 Budget	October 21
Budget Review Workshop	November 4
Public Hearing on Revenue Sources & Property Tax	November 12
Adoption of 2003 Property Tax Levy	November 25
Additional Budget Review Workshops	November 18 & 25, December 2
Budget Adoption	December 9

BACKGROUND

The City Council held a goal setting retreat in April 2002. At this retreat very preliminary information was shared with the Council regarding budget projections for 2003 and beyond. Preliminary indicators were that there would not be additional monies for new programs or increased service levels in 2003 without making reductions in current services, and in fact, it was anticipated that there would be an operating deficit (General Fund, Development Services, & Streets) before considering any new services or programs. Anticipating that this may be the case, the City Council discussed both revenue enhancement and expenditure reduction alternatives.

In May, the Finance Department issued its preliminary budget projections for 2003 which included a projected \$700,000 operating deficit. Since that time the City Manager's Office has been negotiating an agreement with Ronald Wastewater District that will result in an additional \$350,000 franchise fee revenue in 2003. This would reduce the preliminary deficit estimate to \$350,000.

On July 1st the Council reviewed alternative revenue sources, that were identified at the April retreat. The Council consensus was not to pursue implementation of alternative revenue sources for 2003, with the exception of implementation of a Business Registration program, which would be revenue neutral.

Departments submitted their 2003 budget requests on July 22nd. The Finance Department has been reviewing those budget requests, along with the City Manager, to assure that the requests are within the base allocation for each department and support the City Council and City Manager goals. Based on this review and update of financial projections it appears that there is approximately a \$158,000 operating deficit for 2003. This is prior to any consideration for new programs, personnel, or services. As a result of the projected deficit, departments have been asked to identify program reductions that would equate to 2% of their budgets and any resulting service level impacts. The City Manager's Office will be working with departments to identify service impacts and evaluate reduction impacts on operations before finalizing any recommended

reductions. Any supplemental budget items that are proposed to be funded will require additional expenditure reductions or revenue supported options.

Although the current focus is balancing the 2003 budget, the reality is that the City's long-term projections show continued deficits in future years. If the current economic trends continue through 2004 and 2005, the City will not be able to maintain current service levels in the absence of additional revenue sources or significant changes in operational procedures. The following table is the updated operating projections for the City for 2003 through 2008.

	Preliminary 2003	Projected 2004	Projected 2005	Projected 2006	Projected 2007	Projected 2008
Resources	\$30,768,090	\$29,664,052	\$30,046,607	\$30,542,219	\$31,047,132	\$31,447,464
Expenditures	\$30,925,765	\$29,937,677	\$30,873,156	\$32,201,405	\$33,216,390	\$34,326,616
Deficit	\$157,676	\$273,624	\$826,548	\$1,659,186	\$2,169,258	\$2,879,153
Fund Balance	\$6,814,436	\$6,502,750	\$5,744,117	\$4,154,884	\$2,057,678	-\$747,263

Staff will provide an update of the long-term financial projections at this workshop.

DISCUSSION

Some of the primary factors affecting the 2003 budget and the 2004-2008 long-range forecasts include:

GENERAL FUND

Revenues

General Fund operating revenues are projected to fall by approximately 4% from 2002 to 2003. This is largely a result of the reduction of the Motor Vehicle Excise Tax backfill from \$1.5 million in 2002 to \$148,000 in 2003. This revenue source will be eliminated entirely after 2003. The City had relied on \$500,000 of this revenue to support operations.

A description of the most significant revenue trends for 2003 is discussed below.

Property Tax Revenues: Property tax revenues are projected to grow by 2% in 2003. Approximately half of this growth is a result of projected new construction within the City. In November 2001, Initiative 747 was passed by a vote of the people in Washington State. This initiative limited property tax levy increases, beginning in year 2002, to 1% plus new construction without voter approval. If the City would have used the Implicit Price Deflator as the basis for property tax levy increases, property tax revenues would have been approximately \$1.7 million greater over the next five years.

Sales Tax Revenues: The nation and the Puget Sound Region went into recession during 2001. This has contributed to flat or negative growth in taxable sales. The City of Shoreline had experienced 8.5% average annual growth in sales tax revenues for years 1996 through 2000. For years 2001 through 2003, the average annual growth is .8%, a significant drop from previous years, and below inflationary measures. The current projection for 2003 is for sales tax to grow by 1% over 2002 levels. Staff is

continuing to monitor this activity to see if 2003 projections can be raised. A recent release of the economic forecast for the Puget Sound Region projected taxable retail sales to grow by 3.1% in 2003 and 4.8% in 2004.

The City also receives criminal justice sales tax, which is collected county-wide and then distributed on a per capita basis. County-wide sales tax revenues have been below 2001 levels by nearly 10%. For this reason 2002 collections are projected to be less than budget by approximately \$134,000 and total approximately \$995,000. Preliminary projections are for 2003 collections to grow by .5% to \$1,000,000.

Utility Taxes & Franchise Fees: Overall utility tax and franchise fee revenues are projected to grow by 13% from 2002 to 2003. The largest component of this change is the anticipated increase in sewer franchise fees, \$350,000 greater than 2002, from Ronald Wastewater District. Collection of this revenue is dependent on finalizing negotiations with the District. Excluding the sewer franchise fee revenue, utility tax and franchise fee revenue is projected to grow by 5%, \$220,000. This is primarily a result of projected fee increases and increased collection as a result of audit efforts.

Gambling Tax: In 2002 gambling tax collections are approximately 3% behind budget and below 2001 collections for the same period. Because of this trend the preliminary 2003 projections do not include any growth from this revenue source.

Investment Interest: Investment interest is projected to be significantly below budget in 2002, with actual collections projected at \$250,000 compared to budgeted revenues of \$558,725, a 55% decline. 2003 collections are expected to remain flat in 2003, as the City will have approximately the same amount of invested cash and there has been no indication that investment rates are going to change significantly.

Expenditures

Personnel: Personnel expenditures represent approximately 23% of the General Fund budget. Excluding any changes in personnel levels, personnel costs are projected to increase by approximately 4.8%, \$302,000. This is primarily based on anticipated step increases for employees who are not at the top of their salary range, an anticipated market adjustment of 2%, a projected 17% increase in the city's health insurance premium rates, and notification of a probable 1% increase in the employer contribution to the State retirement system. The City's long-term forecast projects personnel costs to increase by approximately 4% annually.

Police Contract: The police contract with King County is projected to increase by approximately \$400,000, 5.8%, in 2003. This is primarily a result of anticipated labor cost increases and some increased service allocation of centralized services (i.e., communications center, canine, major crime unit, etc.).

Jail: As a result of the jail negotiations during 2002 and a decreased activity level, the budget for jail services for 2003 is projected to decrease by approximately 9%, \$89,000 from 2002 levels.

Capital Funding: The City currently allocates approximately \$1.4 million of general fund revenues on an annual basis to fund capital projects. This policy may need to be

evaluated in the future, as operating revenues will not be sufficient to support current service levels.

Fund Balance

The General Fund currently has a healthy fund balance based on conservative budget planning by the City Council. The 2002 projected ending fund balance for the General and General Reserve Funds combined total \$7.5 million, nearly 29% of General Fund revenues. The adopted 2003-2008 Capital Improvement Program included the use of \$1 million of this fund balance for the City Hall project. Although this fund balance is healthy, the City should not rely on the fund balance to balance it's operating budget over the long-term.

CITY STREET FUND

The City Street Fund receives approximately 48% of its resources from Gas Tax and Vehicle License Fees and the remaining 52% from General Fund Revenues. Both gas tax and license fee collections have remained fairly flat, therefore requiring an additional allocation of general revenues to provide sufficient resources to provide the day-to-day maintenance of the City's streets. This maintenance does not include the long-term pavement management program.

The long-term projections for this fund indicate that either the City will need to allocate additional general fund revenues for street operations or develop alternative revenues to maintain service levels, especially as some of the capital projects are completed and increased service levels are required to adequately maintain the improvements. In the absence of these options it is likely that service levels will need to be reduced. For the short-term the fund has adequate reserves.

On September 23rd, the City Council will be considering whether to oppose Initiative 776 (I-776) and/or support Referendum 51. The passage of I-776 would eliminate the motor vehicle license fee in King County. This license fee is the \$15 per vehicle fee paid by City residents. The passage of I-776 would eliminate nearly \$500,000 in annual revenue received by the City Street Fund (nearly 20% of the fund revenue). This action would significantly change the long-term forecast for the fund and the service levels provided by the City.

DEVELOPMENT SERVICES FUND

The Development Services Fund receives approximately 60% of its revenues from fees and 40% from General Fund revenues. Fee collections related to building permits and plan check fees have been dropping since 2001. This corresponds with the timing of the recession and may be indicative of the changes in the Development Code that required larger lot sizes for single family home development. Historically economic slumps have resulted in three year down turns in permit activity followed by five to seven years of expansion. Currently the City has a policy to maintain a minimum fund balance within the Development Services Fund of 5%. Due to the direct correlation between permit revenue and economic cycles, staff may recommend that this minimum be increased to 15% in order to build reserves for an economic downturn. The current reserve levels are at 35%.

Staff will need to continue to monitor development activity during the next year. If activity continues to be in a downward cycle, then expenditure levels will need to be further evaluated.

SUMMARY

Staff will continue to monitor economic forecasts and their impacts on the City's revenue and expenditure trends as the 2003 Proposed Budget is prepared. At the workshop staff will provide any additional updates for the City's operating budget projections for 2003 – 2008.

RECOMMENDATION

No action is required by the City Council. This item is for informational purposes and to provide the City Council with preliminary 2003 budget information.