

2013-2014 Biennial Budget



SECTION B

Budget Message

Final Budget

Under Washington Law, the City Manager presents a balanced annual or biennial budget for the City's upcoming fiscal period for consideration and adoption by the City Council.

Mercer Island's biennial budget serves a number of essential functions. The budget is more than a "checkbook" posting of proposed revenues and expenditures. It is a financial plan that looks out over two-year (operating budget) and six-year (Capital Improvement Program) horizons, balancing planned income and expenses in a fiscally responsible manner. It is a policy plan, guiding and assuring the City's long-term financial health. And, most importantly, it is a detailed description of the goods and services for which the City and its elected officials will be held accountable. It documents the "social contract" between the citizens and their government.

The budget also serves in a broader policy context. It draws upon many City Council decisions and discussions that precede it, and it will leave a legacy of policy influence for future budgets, helping to give the City's finances long-term stability and continuity.

How the Budget is Organized

The Reader's Guide (Section A) at the beginning of the budget document provides a brief overview of how the City's budget is organized.

The budget covers two operating years for all City departments and functions. However, in order to assess revenue and expenditure trends, most budget sections also show actual data for 2011 and forecast data for 2012.

Service Packages

Reflecting the City Council's desire to focus on significant changes in the proposed budget for the coming biennium, City staff has prepared the following departmental "service packages" for 2013-2014: 1) Service Enhancement Requests, and 2) Service Reduction Proposals.

This budgeting approach recognizes that most of the services provided by a city extend from one year to the next, especially in a city that isn't growing. Consequently, the scope of the budget review process is narrowed to notable increases and decreases in each department's operating budget. In addition, the City Council will review the changes to each department's "base" (i.e. ongoing) budget. These changes are broken down into two major components: 1) general inflationary increases, and 2) other significant changes. Within the latter component, "prior year one-time costs" are called out collectively as a decrease, because they will not be re-budgeted in 2013-2014 within each department's "base" budget. If such a cost needs to be budgeted again in 2013-2014 and it is \$10,000 or more, it will be proposed as a service enhancement request.

Service package detail sheets are provided in Section K. They are summarized later in this Budget Message.

Priorities of Government

Over the past three biennia, the City has shown how it spends its resources against the City Council's stated or implied priorities. The Council has sought this information so that it can better understand and consider tradeoff decisions among and across services and cost centers.

Budget Message

In 2004, using a process loosely based on the State of Washington’s “Priorities of Government,” the City Council adopted six City priorities to serve as a filter through which significant changes to City services and programs could be evaluated:

1. **The community will be safe.**
2. **The community will support effective, efficient, sustainable and legal delivery of public services.**
3. **The community will support reliable public infrastructure and protect its considerable public investments (e.g. water, sewer, storm water utilities, streets, parks, and buildings).**
4. **The community will support attractive, high quality neighborhood and business environments.**
5. **The community will support a broad range of recreational, cultural, health and educational opportunities.**
6. **The community will support open and informed public involvement processes within the structure of representative, democratic decision making.**

A complete listing of the priorities and their sub-priorities can be found in Appendix A at the end of the Budget Message.

The proposed 2013-2014 Budget continues to confirm what was discovered back in 2004 with the development of the 2004-2005 Budget, namely that:

- The City spends most of its resources on its highest priority services and projects.
- The City provides the highest General Fund tax support for its highest priority services—police; fire; infrastructure maintenance (streets and parks); and administrative services that ensure the legal and efficient running of the City like Finance, Human Resources, City Attorney’s Office, and City Manager’s Office.
- The services that are least tax-supported from the General Fund are those for which the City can “sell” the service through user fees and utility rates (recreation, youth and family counseling, development permits, and utility services).
- The services for which the City has some of its most accurate data on individuals served are those services most associated with user fees. Those services are also often associated with active and supportive constituencies (recreation programs, leagues, seniors, and school-related groups).
- The City spends comparatively less in services aimed at public information and public involvement.

How Service Reductions were Selected

In determining which services to reduce, the City’s Management Team was guided by the following:

1. Focus primarily on General Fund services—those services primarily supported by taxes, particularly those tax revenues that have shown significant reductions.
2. Avoid service reductions that already are associated with significant fee revenue or external grant support.

3. Utilize the Council's adopted Priorities of Government.
4. Determine whether a specific service is mandatory, essential or discretionary.
5. Take into account the community's satisfaction with City services as expressed in the biennial citizen survey.
6. Demonstrate a significant expenditure reduction in salary and benefit costs before seeking revenue increases.

While sorting through the over 140 individual City services for potential service reductions is difficult, the Management Team was able to maintain basic health and safety functions of the City. In nearly every case, services are reduced in quantity or quality but not completely eliminated. As in the previous biennium, the areas for recommended service reductions most often occur in discretionary municipal functions—neither mandated by state law nor essential to the proper, legal functioning of the City. The Management Team focused on the “business case” for maintaining, reducing or eliminating specific programs. Although the relative popularity of programs was not a significant factor in the staff’s analysis, it is assumed that it will be a factor in the City Council’s review of the budget.

Performance Measures

This biennial budget will continue to identify key performance measures that can be tracked through the budget period. Performance measures are linked to the City’s budgetary resources (inputs) and to the City Council’s values (outputs and outcomes) as expressed in the City Priorities. By tracking performance measures over time, the City hopes to create an ongoing link between its stated goals and priorities and how resources are applied. Periodic reporting of performance objectives and results will be presented to the City Council and community via the “MI Dashboard Report” compiled by the Finance Department.

Financial Status

Due to a long history of constraining expenditure growth, conservatively estimating revenues, and maintaining a sizeable debt capacity, the City’s financial condition remains solid. This statement is validated by Moody’s Aa1 LTGO bond rating of the City in 2011, which along with Seattle, Bellevue, and Redmond is the highest rating in the state. Nevertheless, the City’s finances have become increasingly sensitive to fluctuations in the regional and national economy that are beyond its control. The economic recession coupled with the effects of taxpayer initiatives have had significant impacts on some City revenue streams—most notably sales tax, real estate excise tax, utility tax and property tax receipts. Reduced revenues and stagnate economic growth have produced significant downward pressure on employee compensation and benefits. These expenditure and revenue trends are discussed below.

Key Expenditure Trends

- **Employee Wages & Benefits** – Over the last three and half years, the City has implemented a number of measures to slow and stop employee wage and benefit growth. Although the City is constrained by union contract terms, it has been successful in implementing the measures via voluntary agreements from each of its unions:

Budget Message

- 0% cost-of-living adjustments (or equivalent reduction) for Commissioned Police (first half of 2010), Firefighter (2010 and 2011), AFSCME (2010 and 2011), and Unrepresented employees (2010 and 2011);
 - Rolling hiring freezes on all vacancies,
 - Discontinuance of market-based wage adjustments for Unrepresented, AFSCME, and Police Support employees in 2009, 2010, and 2011;
 - Discontinuance of pay-for-performance program for Unrepresented employees in 2009.
- **Health Care Costs** – The City continues to benefit from long-standing practices of employees sharing in their health care costs. The City also strives to move all remaining employee groups toward lower-cost PPO health care plans. Most employees pay 30% of health care premium costs for their spouses and dependents. In total, the City's employees pay about 20% of total premium costs. Listed below is a comparison of the 2012 monthly health care costs (i.e. medical, dental, and vision) to cover a family of four at the City of Mercer Island and other Puget Sound cities, ranked by total premium cost (from lowest to highest) and noting the employer's and employee's share.

City	Total Premium Cost	Employer's Cost	Employee's Cost	% of Total Cost Paid by Employee
Mercer Island	\$1,950	\$1,558	\$392	20.10%
Kirkland	\$1,987	\$1,987	\$0	0.00%
Lynnwood	\$2,004	\$1,866	\$138	6.89%
Auburn	\$2,007	\$1,957	\$50	2.49%
SeaTac	\$2,008	\$1,873	\$135	6.72%
Sammamish	\$2,008	\$1,973	\$35	1.74%
Bothell	\$2,012	\$1,749	\$263	13.07%
Renton	\$2,023	\$1,927	\$96	4.75%
Issaquah	\$2,067	\$1,949	\$118	5.71%

- **Development Review Staffing** – Starting in 2008, development activity locally and regionally slowed measurably from the record pace experienced over the middle part of the decade. In 2009-2010, residential development slowed down 33% from 2005-2006 levels (as measured by the number of building permits issued). Town Center and other commercial/multi-family development slowed as well, reducing the need for development review personnel and contracted labor.

Recognizing the development downturn, the City reduced its contracted in-house staff by 3.0 FTE's in the 2009-2010 biennium. In 2011-2012, the City further reduced its budget for contracted outside labor (planners, engineers and plans examiners) by about \$290,000. It consolidated many of the reduced contracted services into one contracted in-house position in order to meet basic permit review obligations. Overall, the Development Services Department continues to maintain permit review turnaround time targets, albeit with substantially reduced resources.

Overall, the pace of expenditure growth in the General Fund has been minimal in 2009-2011, averaging 0.7% per year. Expenditure growth in 2012 is projected to be about 2.0%. Adjusted for inflation, the City's General Fund expenditures have dropped to 2007 levels—this in spite of the run-up in development activity at the height of the “housing bubble” and the Council's interests in parks and open

space maintenance. Up until the 2011-2012 biennium, the City had not reduced any services provided to the taxpayers/residents.

When looked at from a longer perspective, the City's General Fund expenditure growth, adjusted for inflation (CPI-U Seattle/Tacoma First Half), has increased by an average of 1.6% per year over the last ten years and has actually shrunk by an average of .03% per year over the last six years.

General Fund Expenditures 2001-2014 (in Millions)



Key Revenue Trends

Citizen Initiatives

- Initiative 695 (Motor Vehicle Excise Tax Repeal)** – With the Legislature’s 2000 enactment of Initiative 695, the City experienced a loss of approximately \$1.1 million per year in annual Motor Vehicle Excise Taxes (via sales tax equalization)—approximately 9% of General Fund revenues. The City continues to adjust to this loss of General Fund revenue through a mixture of constrained expenditures and growth in more volatile revenues, such as sales taxes and permit fees.
- Initiative 747 (Property Tax Limitation)** – Further constraining revenues, the City’s single largest source, property taxes, saw relatively low growth during the early part of the decade. Since passage of Initiative 747 in 2001, the City has been limited to annual property tax increases of 1%. Throughout the past ten years, the cost of basic services has increased at an average of 5.0% per year. In three of the past seven years, the City Council increased the property tax 1% but refunded 1% back to taxpayers from year-end revenue surplus in the General Fund. In 2007 and 2011, the City Council approved a slight increase in property taxes above the 1% threshold using “banked capacity” to generate a long-term funding stream for fire apparatus replacement and for the LEOFF I long-term care liability. In 2009, the City Council voted to maintain a 0% optional property tax increase as an alternative to a 1% property tax decrease.

Budget Message

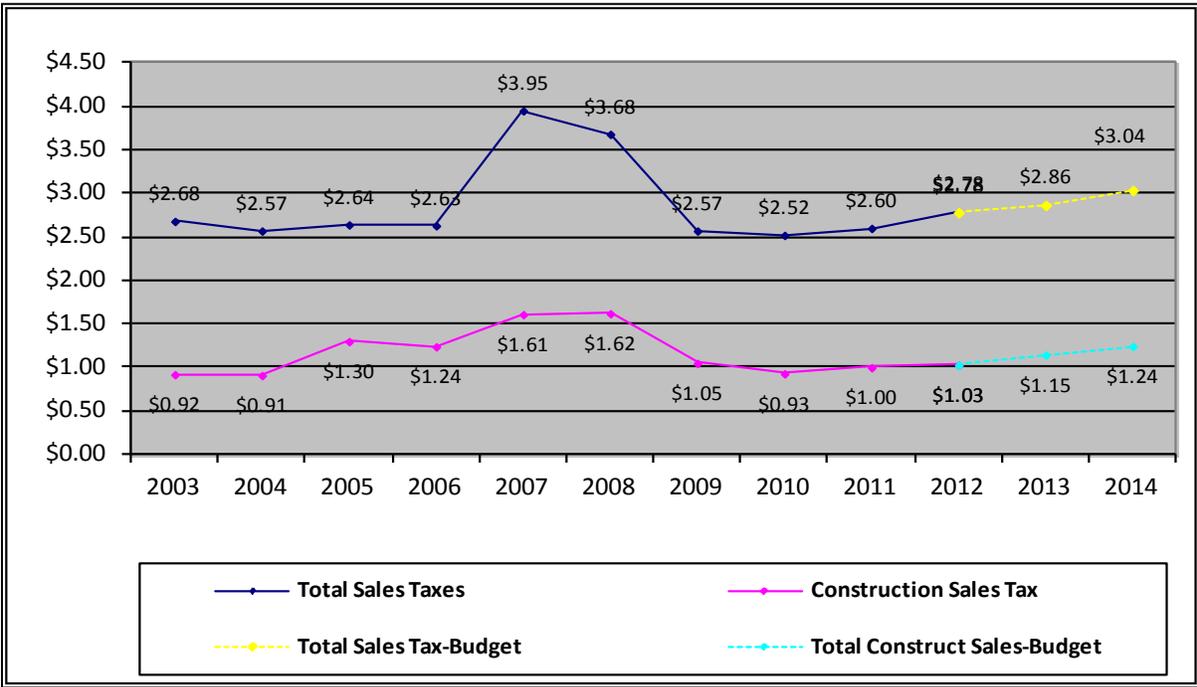
- Initiatives 1183 (Privatization of Liquor Sales)** – Initiative 1183 was approved by Washington's voters in November 2011, thereby "privatizing" the retail sales of spirits and ending the state's monopoly on liquor sales. The initiative ended the previous liquor profits and excise taxes from which the City received approximately \$269,000 per year and replaced them with a license fee which should equal liquor profits and excise tax revenues by 2014. Locally, City staff estimate a net reduction in liquor-related revenues of \$50,000 in 2013 (over 2011 levels) and \$0 in 2014.

Sales Tax

The recession and its aftermath have generated a significant reduction in sales tax receipts, particularly in the area of construction sales tax. The City experienced a cumulative reduction of \$1.26 million in construction-related sales tax in 2009 and 2010 compared to 2008. Looking forward, Finance staff are forecasting a \$534,000 increase in total sales revenue in 2013-2014 over 2011-2012. Truly, the bottom fell out of the construction industry on Mercer Island and elsewhere over the last four years. On the positive side, Town Center projects at Aviara and The Mercer Phase 2 have provided a needed uptick in construction-related sales tax. Permit activity in the Town Center and residential zones is expected to increase in the 2013-2014 biennium, generating over \$210,000 in additional construction sales tax in 2014 relative to 2012.

The graph below displays actual and projected total sales tax revenues as well as construction-related sales tax revenues for 2003-2014.

Sales Tax 2003-2014 (in Millions)

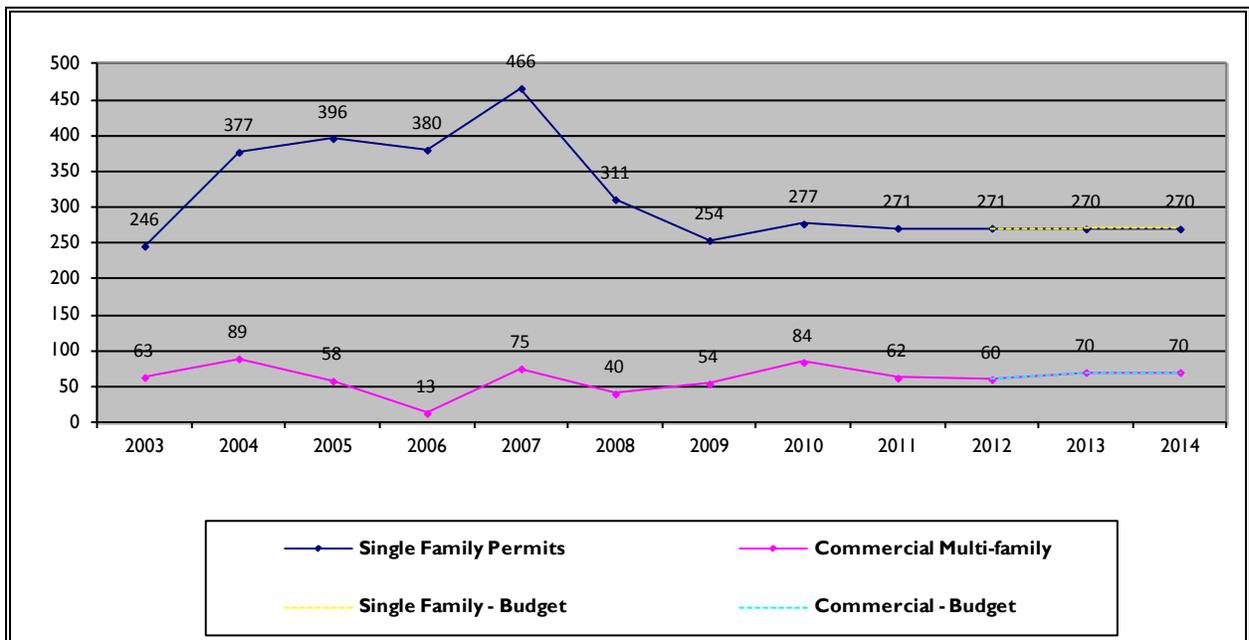


Development Services (Permit Processing)

Between 1999 and 2007, the City saw a significant increase in single-family home development/remodeling and commercial construction. In 2000, the Development Services Group (DSG) processed a record 2,937 land use, single family, commercial, and over-the-counter permits. That pace increased to 3,110 total permits in 2005. In 2006, building construction valuation peaked at almost \$96.0 million. In what many economists have since labeled the "housing bubble," these increases were largely driven by low cost financing for home remodels, new construction and the redevelopment of the Town Center. To provide some additional context, key development statistics for 2003-2012 (along with biennial projections) are presented below.

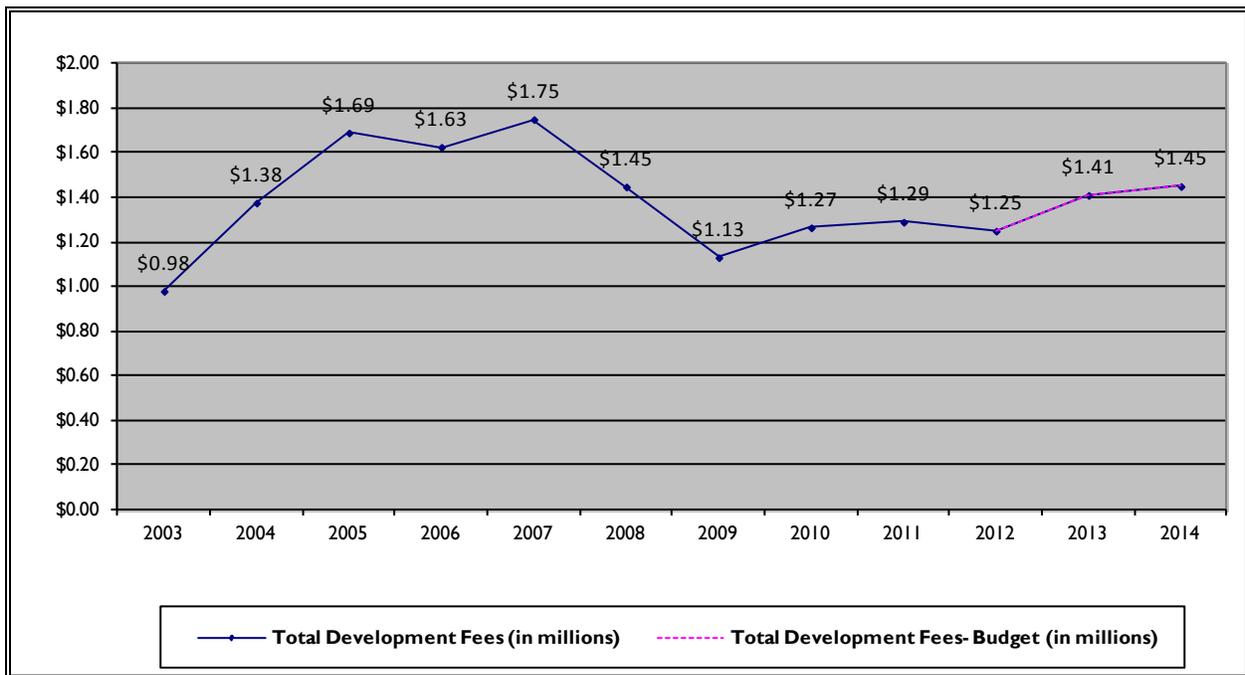
Development Statistics	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Single Family Residential Permits Issued	246	377	396	380	466	311	254	277	271	271	270	270
Commercial/Multi-Family Permits Issued	63	89	58	13	75	40	54	84	62	60	70	70
Over the Counter Permits Issued	1,896	2,465	2,656	2,609	2,587	1,995	1,586	1,770	1,752	1,700	1,700	1,700
Total Building Valuation (\$mill.)	\$26.7	\$93.5	\$80.1	\$95.9	\$86.3	\$40.2	\$30.9	\$51.6	\$60.5	\$50.0	\$50.0	\$50.0
Total Development Fees (\$mill.)	\$0.98	\$1.38	\$1.69	\$1.62	\$1.75	\$1.45	\$1.13	\$1.27	\$1.29	\$1.25	\$1.41	\$1.45

Building Permits 2003-2014



Budget Message

Total Development Fees 2003-2014 (in Millions)



Compared to the peak year of 2007, single family residential permits declined over 45% in 2009. Similarly, new building valuations dropped over 64% in 2009 relative to 2007. Given these decreases, the 2009-2010 Budget included a number of staffing reductions to reset the “core staff” complement. DSG’s “contingent staff” (i.e. contract employees) were reduced by 3.0 FTE’s. In the 2011-2012 budget, DSG further reduced its contracted external labor by about \$290,000. The department consolidated much of the remaining work by retaining an existing contract Plans Examiner position. For the 2013-2014 biennium, permit activity is expected to increase by over 600 total permits and \$20 million in building valuations. Permit revenue is expected to increase by \$170,000 in 2013 and by \$210,000 in 2014 over 2012 levels. As a result, and in recognition that the base amount of permit review work will increase, the Plans Examiner position will be shifted to permanent, regular FTE status.

See Development Review Fees policy in Section C (Budget Policies) for more details.

Budget Summary

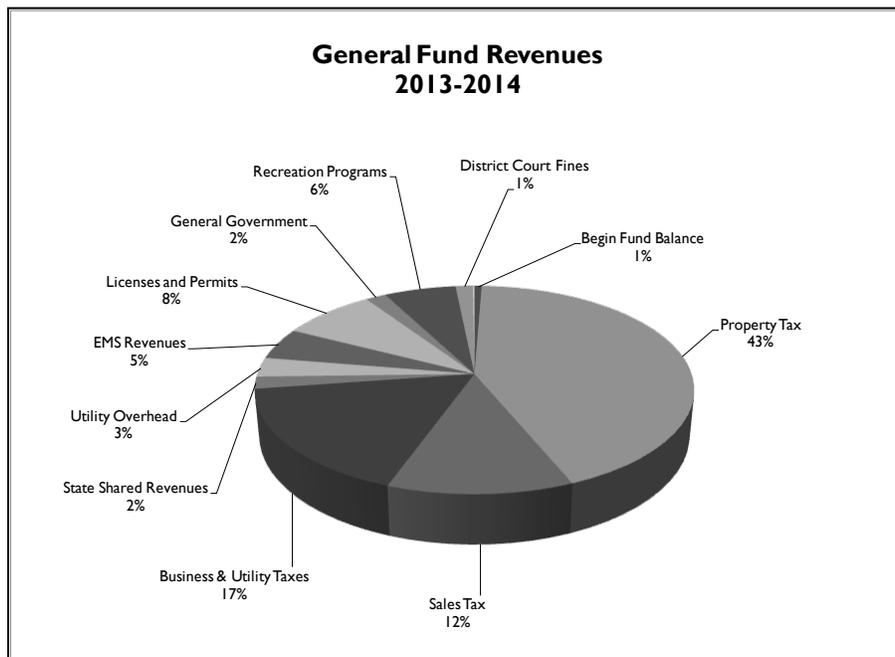
At its highest level of generalization, the 2013-2014 Budget can best be summarized in the following ways:

- General Fund expenditures continue to be constrained by modest General Fund revenue growth. In the 2011-2012 Budget, the City reduced General Fund expenditures by over \$2.3 million per year—nearly all of which is ongoing. Beginning in 2012 (especially the second half), single family residential and mixed use development picked up significantly on the Island, resulting in increased construction sales tax revenues and development fees. Overall, the proposed budget is a “maintenance of effort” budget.

- By making the difficult expenditure decisions two years ago, the City is better positioned to make a few strategic investments in the 2013-2014 operating and capital budgets—key among them are communications, sustainability, utility infrastructure and technology management.
- The proposed budget relies on a mix of non-service budget reductions, small reductions in selected discretionary services, continued constraints on staff salary increases, as well as the optional 1% property tax increase.
- In spite of the significant reductions in spending over the last few years, a structural imbalance still exists between expenditure growth and revenue growth. Because Mercer Island is disproportionately reliant on the property tax, which is limited to an annual 1% increase, the City will ultimately need to add a new revenue source in order to provide the services Mercer Islanders have come to expect. Consistent with Council direction, this budget proposes to extend the existing utility tax to the City’s water, sewer and storm water utilities in order to bridge the projected, remaining deficit.

General Fund – Revenue Sources

Reflecting the recent trends mentioned above, the General Fund continues to receive nearly all of its operating revenues from the same tax sources in approximately the same proportions as previous years, with the exception of property tax and sales tax. Total budgeted General Fund resources for 2013 and 2014 are \$24,335,781 and \$25,327,183, respectively. A breakdown of the budgeted major revenue sources for 2013-2014 is provided below.



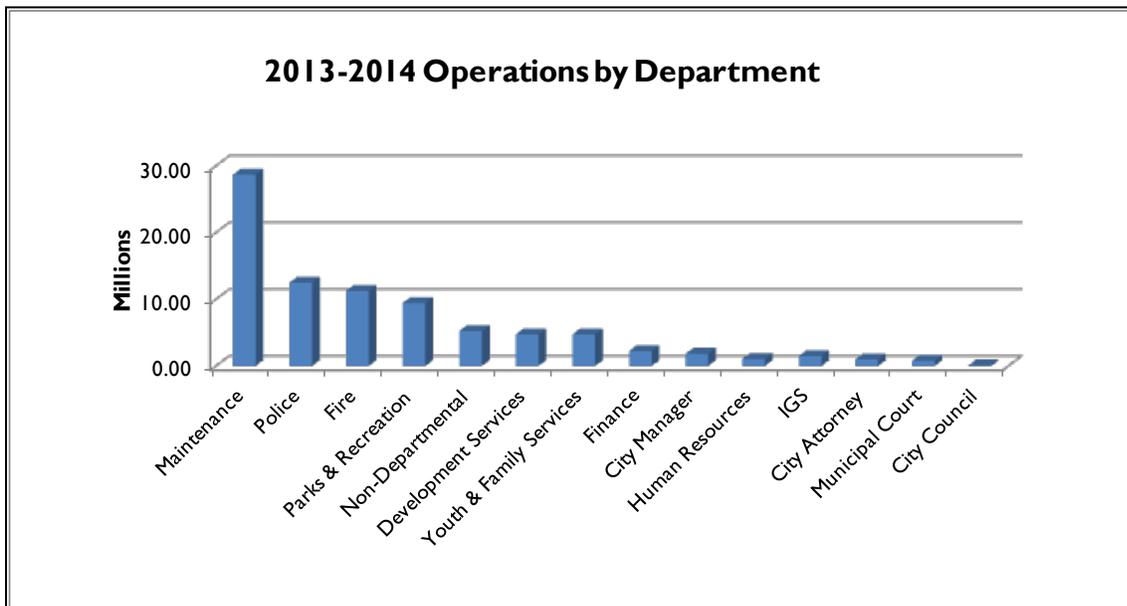
Another way of looking at General Fund tax revenues is to compare the average monthly impact of the property, utility, and sales taxes paid by a typical Mercer Island household (assumes a \$700,000 home and a family of 4) to the City (i.e. not the state, county, port, or school district) to the average monthly Puget Sound Energy, Comcast, Verizon, and City utility (i.e. water, sewer, storm water, and EMS) bills paid by that typical household. This comparison is provided in Appendix B at the end of the Budget Message. The City services those taxes pay for include the following:

Budget Message

- 24/7 police, fire suppression, and emergency medical aid services
- Street, roadside, median, sidewalk, and path maintenance
- Park, ballfield, and trail maintenance
- Recreation program support
- Youth & Family Services program support
- Public meetings and records management
- Public building maintenance (City Hall, Maintenance Building, Community Center, Luther Burbank Administration Building, and 2 Fire Stations)
- Community (i.e. land use) planning

Department Operating Budgets

The City continues to dedicate the largest portions of its resources to Public Safety (police, fire, and emergency medical services) and Maintenance. As shown below, the combined operating budgets for these areas account for \$52.4 million, or 62%, of total operating expenditures for the 2013-2014 biennium.



Staffing

Reflecting only the organization's most pressing staffing needs given the current economic environment, the City's 2013-2014 staffing model will see a net increase of 2.82 FTEs in total "regular" and "contract" positions. Staffing changes are listed below.

New Position Reductions

- Reduce Assistant City Attorney to 0.75 FTE – 0.25 FTE reduction
- Reduce Paralegal to 0.5 FTE and reclassify position – 0.5 FTE reduction
- Reduce Judicial hours from 33 to 28 hours per week – 0.13 FTE reduction
- Reduce Parks Manager, which was left vacant in 2011-2012, by 0.5 FTE and distribute remaining 0.5 FTE to two part-time Parks employees – 0.5 FTE reduction

New or Expanded Positions

- IGS position – Help Desk – 1.0 FTE increase
- Expand Communications Coordinator position (0.6 FTE) to encompass Sustainability Coordination function – 0.4 FTE increase
- YFS Thrift Shop Production Lead – paid from Thrift Shop revenues – 1.0 FTE (contract) increase
- YFS Administrative Assistant – convert casual labor into permanent, regular position – 0.8 FTE (contract) increase
- MICEC Nights/Weekends – convert casual labor into permanent, regular position – 1.0 FTE (contract) increase

Conversion of Contract to Permanent Positions

- Convert Deputy City Clerk from one-time contract in 2011-2012 to permanent, regular position – no net FTE increase
- Convert Parks and Recreation Facility Scheduler from ongoing contract (6 years) to permanent, regular position – no net FTE increase
- Convert Plans Examiner from ongoing contract (6 years) to permanent, regular position – no net FTE increase
- Convert Storm Water Project Engineer from ongoing contract (6 years) to permanent, regular position – no net FTE increase

The staffing changes made as part of the 2011-2012 Budget are summarized below and will continue through the 2013-2014 biennium.

Continuing 2011-2012 Reductions in “Regular” Employees

- Right-of-Way Maintenance – 1.0 FTE reduction
- Transportation Manager – 1.0 FTE reduction
- Court Administrator – 0.5 FTE reduction
- Police Records Clerk – 0.5 FTE reduction
- Police Patrol "Hire Ahead" position – 1.0 FTE reduction
- MIYFS Development Coordinator – 0.5 FTE reduction
- MIYFS VOICE Coordinator – 0.5 FTE reduction

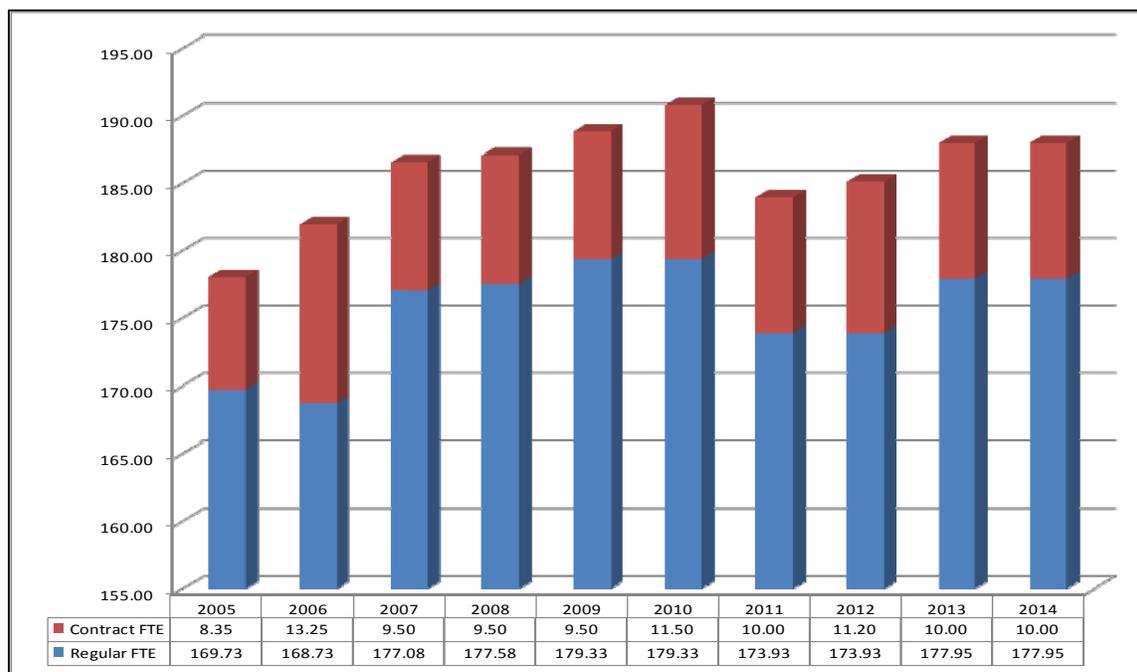
Budget Message

Continuing 2011-2012 Reductions in “Contract” Employees

- ROW Arborist (contract) – 0.5 FTE reduction
- Recreation Coordinator (contract) – 1.0 FTE reduction
- Fire Marshal (contract) – 1.0 FTE reduction
- Facilities Project Manager – 1.0 FTE reduction
- CIP Administrative Support – 0.5 FTE reduction
- CIP Project Manager – 1.0 FTE reduction

The total number of regular (i.e. ongoing) and contract employees approved for the period 2005-2012 and proposed for 2013-2014 is displayed below.

**10 Year Staffing (FTEs) History
2005-2014**



Biennial Budget Issues & Initiatives

Entering the biennial budget process, the City faces a \$1.19 million deficit in 2013 and a \$1.48 million deficit in 2014. Driven by significantly lower revenues from the previous two biennia, the City must reduce expenditures, increase revenues or both. Largely following the wishes of the City Council as voiced at its June 2012 Mini-Planning Session, the proposed 2013-2014 Budget relies on a balance of expenditure reductions, an optional 1.0% property tax increase, and the institution of a utility tax on the City’s water, sewer, and storm water utilities. The table on the following page summarizes the balancing strategy proposed in the General Fund Budget.

Budget Balancing Strategy General Fund

Description	2013	2014
Projected Deficit	(1,189,622)	(1,479,373)
Plus Expenditure Reductions:		
Non-Service Level Reductions	395,059	404,464
Service Level Reductions	60,000	60,000
General Fund Subsidy Reductions	190,655	317,913
Less Service Enhancements:		
Ongoing Costs	(199,330)	(213,739)
One-Time Costs	-	(70,000)
Plus New/Increased Revenues:		
Ongoing:		
1% Optional Property Tax Increase	106,471	108,535
Utility Tax Increase (Water, Sewer & Storm Water)	425,000	625,000
Utility Rate Increases (Sustainability position)	56,421	58,305
MICEC Room Rental Revenues	15,000	21,600
One-Time:		
Available Cash (One Time), 12/31/12	140,346	167,295
Balance	0	0

In total, General Fund expenditure reductions amount to \$645,714 in 2013 and \$645,015 in 2014. This is over and above the more than \$2.3 million in expenditure reductions made in the 2011-2012 biennium, which are ongoing in 2013-2014. These 2011-2012 expenditure reductions are listed in Appendix C at the end of the Budget Message. The expenditure reductions are organized as follows:

Non-Service Level Reductions, Service Level Reductions, and General Fund Subsidy Reductions. A detailed explanation of the proposed budget reductions follows.

In terms of new revenues, the proposed 2013-2014 Budget is balanced assuming a 1.0% increase in property taxes, the institution of utility taxes on City-owned utilities, and modest increases in utility rates and MICEC room rental fees. In total, ongoing revenues increase by \$602,892 in 2013 and \$813,440 in 2014.

Non-Service Level Reductions

Before seeking service reduction proposals from City departments, the Finance Director and City Manager asked Department Directors and their staff members to identify reductions in their budgets that would not reduce service to the public but would reduce reliance on the cash-strapped General Fund. In all, departments identified \$395,059 in ongoing, non-service level reductions in 2013, which are listed in the following table.

Budget Message

2013 Non-Service Level Reductions

Decrease in WCIA liability insurance premium	\$137,362	Reduced judicial hours	\$21,814
Pay-for-performance (non-union employees)	60,000	Solid waste professional services	18,400
Revised ILA with MISD for elementary fields	45,000	General government office supplies	12,140
Reduce police patrol overtime	27,976	Eliminate CPI-W increase for MICEC subsidy	10,000
LEOFF I retiree medical premiums	27,470	City Attorney's Office dues and subscriptions	8,000
City Attorney's Office re-organization	21,897	Recreation services	5,000
		Total	\$395,059

Service Reduction Packages

Parks & Recreation

- Parks Maintenance LOS B to C** – This reduction would re-designate certain parks from level-of-service “B” to level of service “C” maintenance thereby reducing the number of seasonal and full-time worker hours needed for overall park maintenance. The affected parks will be Groveland Beach, First Hill Park, Ellis Pond, Clarke Beach, Slater Park, Secret Park, Rotary Park, Roanoke Park and Pioneer Park. In general, level “C” Parks are visited only once per week to pick up litter and mow the turf. Maintenance issues and response is triggered by park inspections and citizen concerns. The routine tasks that would be eliminated include routine maintenance of buildings and furniture, weeding, pruning, fertilization, and trail clearing and repairs. This was a proposed, ongoing reduction in the 2011-2012 Budget, which the Council partially restored using \$60,000 in one-time funding each year.

*This package will reduce the General Fund budget by **\$60,000 in 2013 and 2014.***

- Parks Manager (reduce by 0.5 FTE)** – This position was left vacant in 2011-2012 to help balance the budget. It is proposed that it be reduced by 0.5 FTE, with the remaining 0.5 FTE distributed equally between two part-time Parks Maintenance employees. The remaining responsibilities of the Parks Manager position will continue to be absorbed by the Parks Superintendent.

*This proposal will reduce the General Fund budget by **\$51,800 in 2013 and \$54,147 in 2014.***

- Summer Celebration Fireworks (continuing reduction from 2011-2012)** – Each year, Summer Celebration includes a fireworks display as part of a community picnic at Luther Burbank Park. As was done in the 2011-2012 Budget, this reduction is made with the hopes that private fund raising can replace City General Fund support.

*This ongoing reduction continues to save the General Fund **\$24,000 in 2013 and 2014.***

- Performing Arts Programs/Special Events (continuing reduction from 2011-2012)** – This proposal resulted in a reduced level of service in Arts Council programming including impacts to: Mostly Music in the Park, Shakespeare in the Park, Outdoor Summer Films, Spring Egg Hunt, Arts Council Winter Dance, Family Valentine Winter Dance and the Volunteer Recognition Party. These programs are wholly funded by the General Fund and are discretionary programs that generate little or no fee revenue. This was a proposed, ongoing

reduction in the 2011-2012 Budget, which the Council temporarily restored provided that staff could generate the needed funding through donations and sponsorships.

This ongoing reduction continues to save the General Fund \$13,000 in 2013 and 2014.

General Fund Subsidy Reductions

- **Project Management Support to CIP Fund** – Every biennium the Finance staff reviews the budgeted allocation of CIP project managers and the actual hours charged to CIP projects. Particular attention is paid to those staff budgeted in the General Fund. In reviewing the current 2011-2012 biennium, it was determined that the budgeted allocation of certain staff in the Maintenance Department, the Parks and Recreation Department and the IGS Team needed to be adjusted going forward in order to eliminate these General Fund “subsidies”. This will have no impact on the budgeted CIP projects in 2013-2014, since project management costs are already included in the total budgeted cost of each CIP project.

This action will save the General Fund \$93,173 in 2013 and \$97,203 in 2014.

- **Shift Street Sweeping Costs to Storm Water Fund** – Historically, street sweeping has been funded in the Maintenance Department’s Right-of-Way (ROW) Team budget. Some of the ROW Team’s maintenance activities have been financed by the General Fund (e.g. hazardous tree removal). Others have been financed by the Street Fund (e.g. asphalt patching.) And yet others have been financed by the Storm Water Fund (e.g. ditch maintenance). Street sweeping removes oils, heavy metals, siltation and other pollutants from the street right-of-ways before they enter the storm drainage system. On the basis that street sweeping is primarily a water quality improvement activity and is required as part of the City’s NPDES water quality permit, this budget proposes to finance the activity fully from the Storm Water Fund. The City’s Utility Board has reviewed this proposal and recommends it to the City Council.

This action will save the General Fund \$97,482 in 2013 and \$100,710 in 2014.

- **Reduce Youth & Family Services (YFS) annual subsidy** – Prior to the 2011-2012 biennium, the General Fund subsidy of YFS was \$465,000 per year. Thrift Shop sales growth made it possible to reduce the annual subsidy by \$145,000 to \$320,000 in the 2011-2012 Budget. It is proposed that the annual subsidy be reduced again by \$120,000 to \$200,000 beginning in 2014, which would be fully offset by increased Thrift Shop revenues.

This action will save the General Fund \$120,000 in 2014.

Service Enhancement Packages

City Manager’s Office

- **IGS Computer Support Technician** – The Information and Geographic Services (IGS) Team is seeking 1.0 new FTE to support existing IT systems and support City business needs. In 1997 and again in 2007, the City conducted an IT Strategic Plan, using industry experts to assist the City in assessing its resources and risks. The experts concluded in both studies that the City fell far short of industry standards for IT support. Best practices recommend IT staffing levels at 3%-5% of total employees. Mercer Island is currently at 1.4%. Based on these ratios, the City could justify adding 2 FTE’s—this proposal seeks only one. IGS continues to see risks increasing for

Budget Message

system and business failures. The position will be supervised by the IGS Manager.

*This package will increase the General Fund budget by **\$44,511 in 2013 and \$46,640 in 2014** (the total cost, which is allocated among multiple funds, is \$69,328 in 2013 and \$72,640 in 2014).*

- **Deputy City Clerk** – At the Mini-Planning Session in June 2011, the Council discussed the priorities for using the Sewer Lake Line project savings. After discussion, the Council was convinced that new resources were needed in the City Clerk's Office, especially as it relates to public records management. The Council appropriated \$60,000 from Sewer Lake Line project savings in October 2011 and combined it with the savings from the unfilled Communications Coordinator position in order to fund a Deputy City Clerk position for the remainder of the biennium. The position is included in the proposed 2013-2014 Budget as a permanent, regular FTE to help the City Clerk continue to meet the legal requirements of the Office. The position will reside in the City Manager's Office and will be supervised by the City Clerk and Deputy City Manager.

*This package will increase the General Fund budget by **\$87,339 in 2013 and \$91,170 in 2014**.*

- **Sustainability Coordinator** – In early 2012, the Mayor appointed and the Council confirmed a Sustainability Task Force whose purpose was to develop policy guidance for the City and community in the realm of sustainable practices, program and services. The Task Force completed its work in the summer of 2012 and submitted its final report in September 2012. Among its recommendations was a proposal to hire a "Sustainability Coordinator" whose job it would be to coordinate and advance the sustainability programs, services and projects of the City. Given the clear need for public education and engagement in sustainability efforts, it is proposed that a service package request for an additional 0.4 FTE be combined with the currently vacant Communications Coordinator position (0.6 FTE) to create a full-time Communications/Sustainability Coordinator, which would be split 50/50 between the Communications and Sustainability functions. The Sustainability portion of the position (0.5 FTE) would be split 50/50 between the General Fund (0.25 FTE) and the Storm Water Fund (0.25 FTE). In terms of funding, the additional 0.4 FTE requested would be paid for by utility rates and allocated to each utility as follows: Water Fund (0.05 FTE), Sewer Fund (0.05 FTE), and Storm Water Fund (0.3 FTE). Most of the financial impact is on the Storm Water Fund, accounting for 2.3% (\$40,529) of the 5.1% proposed rate increase. The Utility Board has endorsed this proposal. The position will reside in the City Manager's Office and will be supervised by the Deputy City Manager.

*This package will increase the Water, Sewer, and Storm Water Fund budgets collectively by **\$56,421 in 2013 and \$58,305 in 2014**. There is no net impact on the General Fund.*

Youth & Family Services

- **Thrift Shop Production Lead (1.0 contract FTE)** – This is a new position that has been staffed over the years by several work study students. Over the last year and a half, work study hours have been reduced at the state and federal level. The position will advance the collection and sales of Thrift Shops goods. The cost of the position is funded by Thrift Shop revenues.

*This package does not increase the General Fund budget. The cost of the 1.0 contract FTE to the Youth & Family Services Fund is **\$44,795 in 2013 and \$47,247 in 2014**.*

- **Administrative Assistant (0.8 contract FTE)** – This is a new position that has been staffed over the years by several work study students. As noted above for the Thrift Shop Production Lead, work study hours have been significantly reduced at the state and federal level. As a result, this proposal consolidates existing, budgeted casual labor hours and funds a 0.8 contract FTE to provide reception services at the Luther Burbank front counter as well as a host of additional administrative support services to eleven Youth and Family Services staff. The net cost of the position is funded by Thrift Shop revenues.

*This package does not increase the General Fund budget. The net cost of the 0.8 contract FTE to the Youth & Family Services Fund is **\$11,817 in 2013 and \$12,742 in 2014.***

Parks & Recreation

- **MICEC Staffing Model** – This proposal re-structures the MICEC’s staffing model, shifting from part-time hourly staff to a higher-skilled Lead position. The Center has struggled to maintain a body of lower paid part-time staff members that are willing to work night-time and weekends consistently. Customer service quality and quantity have suffered. The Lead position will add consistency, continuity and quality services. The position costs will be recovered by room rental fees. See MICEC fee increases in the following section.

*This package will increase the General Fund budget by **\$15,000 in 2013 and \$21,600 in 2014.** The increases are financed by MICEC room rental fee increases.*

New/Enhanced Revenues

Property Tax – 1% Optional Increase

Mercer Island continues to be highly dependent upon the property tax for funding its basic services (43% of total revenues in 2013-2014). Generally, Mercer Island and other “bedroom communities” have a lower reliance on sales tax receipts and, consequently, a higher reliance on local property taxes. Given the volatility of retail sales tax revenues, especially construction-related sales tax, and development fees, the proposed 2013-2014 Budget assumes a 1% Council-approved property tax increase generating \$106,471 in 2013 and \$108,535 in 2014.

See Property Tax policy in Section C (Budget Policies) for more details.

Utility Taxes – City-Owned Utilities

Under state law, cities are granted the authority by a vote of the City Council to enact a tax of up to 6% of gross receipts on private and public utilities operating in their jurisdiction. The tax rate can be higher with voter approval. The City currently imposes a 6% utility tax on electricity, natural gas, solid waste, cable television and telephones. AWC reports that 188 Washington cities impose utility taxes of some kind. Many cities apply the utility tax to publicly-provided utilities—water (145 cities), sewer (135) and storm water (60). Sixteen cities in King County impose a utility tax on one or more public utilities. In King County, public utility tax rates range from as high as 15.5% (Seattle) to as low as 5% (Bothell), The average utility tax rate among King County cities is 7.1%.

Utility tax revenues comprise the second largest (17%) of the City's basic revenue streams behind property taxes. In 2011, actual utility tax revenues were \$3,477,156.

Budget Message

At its Mini-Planning Session in June 2012, a majority of the City Council indicated its willingness to consider extending the utility tax to the three City-owned utilities—water, sanitary sewer and storm water. The Council indicated that it would assume, for discussion purposes, enacting a utility tax at levels that would address one-half of the forecasted deficit. At the time, one-half of the deficit was estimated to be \$450,000 in 2013 and \$650,000 in 2014. For the proposed 2013-2014 Budget, staff was able to reduce those amounts to \$425,000 in 2013 and \$625,000 in 2014. As a result, staff prepared the budget assuming a new utility tax of 3.4% in 2013 and 5.0% in 2014. The chart below summarizes the tax and revenue implications:

Utility Tax	2013	2014
Tax Rate on Water, Sewer, Storm Water Utilities	3.4%	5.0%
Annual Revenue Generated	\$ 425,000	\$ 625,000
Percent of Proposed General Fund Budget	1.7%	2.5%
Percent of Projected General Fund Deficit	35.7%	42.2%
Monthly Utility Bill Impact	\$ 4.25	\$ 6.25
Annual Utility Bill Impact	\$ 51.00	\$ 75.00

Fee/Sales Increases

In order to balance the biennial budget without over-reliance on reserves or service reductions, the following fee increases are also proposed:

- Community Center Rental Fees** – Rental rates have been the focus of review by the City Council for several years, generally with the goal of maximizing local use of the facility while minimizing General Fund operational subsidies. Although these two goals sometimes conflict, staff has worked to balance realistic market-based rental rates with citizen expectations for reasonable access to the facility.

These MICEC rental rate increases will generate new General Fund revenue of \$15,000 in 2013 and \$21,600 in 2014.

- MIYFS Thrift Shop** – The Mercer Island Youth & Family Services Thrift Shop was created to generate financial support for social service programs at MIYFS. Through the re-sale of donated household goods, the Thrift Shop continues to grow in activity and sales, with \$1.13 million in gross sales revenue projected in 2012. Because the Thrift Shop has significantly surpassed sales goals in 2011-2012, staff believes that the General Fund subsidy to the YFS Fund can be reduced from \$320,000 to \$200,000 beginning in 2014. In other words, the Thrift Shop is expected to generate an additional \$120,000 in gross sales revenue over and above the 2012 budgeted amount in 2014. See YFS Financing policy in Section C (Budget Policies).

This increase in sales will generate new revenue to the YFS Fund of \$120,000 in 2014.

“Rainy Day” (Contingency) Fund

The City’s Contingency Fund Policy sets a reserve balance goal of 10% of General Fund expenditures. At the end of 2012, the Contingency Fund balance is projected to be \$2,344,335. The approved 2011-2012 Budget assumed that the “Rainy Day” fund would need to be tapped for \$786,466 to balance the General Fund budget. However, staff did not tap the “Rainy Day” fund in 2011 and does not anticipate

needing to tap it in 2012. As a result, the Contingency Fund is fully funded at adopted policy level. In addition, the proposed 2013-2014 Budget is balanced without reliance on the "Rainy Day" Fund.

Transportation Benefit District (TBD)

A TBD is a quasi-municipal corporation and independent taxing district created for the purpose of acquiring, constructing, improving, providing and funding transportation improvements. The improvements can be for maintenance of City streets, investments in high capacity transportation, public transportation, pedestrian and bicycle improvements and transportation demand management. A TBD can also fund the operation, maintenance, and preservation of existing streets and trails.

In Mercer Island's case, it would be created and governed by the City Council. While there are multiple revenue options available, the most common is a \$20 annual vehicle fee. This can be enacted by a vote of the City Council. An amount above \$20 would require voter approval. A \$20 annual fee would generate approximately \$350,000 per year. Since rules allowing TBD's were amended in 2005, TBD's have been created in Bellingham, Burien, Des Moines, Edmonds, Lake Forest Park, Liberty Lake, Olympia, Point Roberts, Prosser, Sequim, Snoqualmie and University Place.

Although allowed, the City Manager does not recommend using a Transportation Benefit District to restore General Fund revenues. The proposed 2013-2014 Budget does not rely upon a TBD to be balanced. Instead, the TBD is offered to the City Council as a tool to address financing transportation projects that have challenged the Council in the last two biennia. Those project and service areas include:

- Residential street overlay funding
- Transit services from south end to north end transit center (e.g. "Jitney" project)
- Traffic calming (planning and implementation)
- Implementation of Pedestrian & Bicycle Plan
- Commuter parking/transit oriented development planning

In order to maintain expenditure and project levels in the City's Street Fund, a new source of revenue will be required. The City Manager recommends the City Council seriously consider this source at the mid-biennial budget review in November 2013.

Additional Revenue Options

While not proposed in this biennial budget, the following revenue tools are available to the City Council and/or voters:

- **"Banked Capacity"** – The City Council has the authority to raise property taxes by almost \$146,000 by a vote of the Council. This authority derives from past property tax setting capacity granted by the state legislature, of which the City opted to take less than the maximum increase.
- **Levy Lid Lift** – With voter approval, the City could raise property taxes for operations and/or capital purposes. A 1% increase would generate approximately \$108,000 in 2014.

Budget Message

Sustainability

Since the early 1990's, the City has been a regional leader in resource conservation. The City has experienced significant success in recycling and solid waste stream diversion, water conservation, storm water quality improvements, building energy efficiencies, and invasive species removal.

Early in 2012, the Mayor appointed a Citizens Sustainability Task Force with the purpose of developing policy guidance for the City and City Council on sustainable services, practices, projects and programs. The City Council received the Task Force recommendations in the summer of 2012 with the understanding that City staff would begin the task of merging policy guidance from the Task Force Report with biennial budget implementation detail.

The Budget document contains an updated Budget Policy on Sustainability (Section C) and a detailed discussion of sustainable programs, services and projects in the biennium. To be sure, most items contained in the list (and in the budget) are service and programs that the City has supported for a number of years.

One program that is new to the budget was identified as the highest priority of the Task Force—creation of a Sustainability Coordinator position at the City. Acknowledging that the City still faces challenging financial times, the proposed 2013-2014 Budget combines the currently vacant Communications Coordinator position (0.6 FTE) with a new service package request for an addition 0.4 FTE to create a full-time Communications/Sustainability Coordinator, which would be split 50/50 between the Communications and Sustainability functions. Since movement to sustainable practices in the community necessarily relies on public communication efforts, these two functions seemed to be a natural for combining.

The City will continue to be active in sustainable activities, particularly where the activity generates savings in capital investment and operations costs. In the 2011-2012 biennium, the City was active in the following areas:

- **Fleet Operations** – Reduce green house emissions and fuel consumption through acquisition policies and operational best practices.
- **Healthy Neighborhoods** – Implement the Bicycle & Pedestrian Plan, facilitating greater reliance on human powered transportation.
- **Water Quality** – Identify and implement Low Impact Development projects through regional grant fund sources.
- **Energy & Resource Conservation** – Continue recycling goals, water conservation, and partnership with Puget Sound Energy for a Resource Conservation Manager to oversee energy conservation efforts by City staff.
- **Grass Roots Efforts** – Partner with the Green Ribbon Commission to advocate for voluntary energy savings and emissions reductions in local homes and businesses.

In 2013-2014, the City will be active in the following areas (see the Sustainability policy in Section C for a complete listing).

Development Services

- Implement Full Service e-Permitting; eliminates paper plans and in-person trips to the City.
- Conduct review of tree and vegetation removal on development sites.

- Assist applicants with “green” building projects on private property.
- Remove unwarranted regulatory barriers to Green building and Low Impact Development projects.
- Implement the national Pollution Discharge Elimination System Phase 2 Permit.
- Conduct Critical Areas Ordinance permit reviews.
- Update and administer the Shoreline Master Program.

Parks & Recreation

- Remove invasive species from public forests; plant new native trees and shrubs.
- Conduct sustainability education programs – Letterboxing, Adventure Playground, Leap for Green, National Trail Days.
- Reduce water consumption through use of “smart” water clocks (irrigation).
- Implement turf rehabilitation practices to reduce water consumption and weeds (herbicide use).
- Use phosphate-free fertilizers to improve storm water run-off quality.
- Implement “integrated pest management” plan; drastically reduce use of herbicides.
- Use high efficiency heat and light systems at Community center.
- Provide for composting at Summer Celebration and Community Center.

Maintenance

- Continue to reduce silt entering Lake Washington through drainage basin improvements.
- Improve water quality (zinc and copper) entering Lake Washington through enhanced monitoring, measurement, public education, potential pre-treatment projects, Best Management Practices and Low Impact Development.
- Conversion of ditches into bio-swales.
- Recycle asphalt as streets are reconditioned and resurfaced.
- Continue stepped up street sweeping.

Youth & Family Services

- Make unused/unsold produce (from Farmers Market to MIYFS Food Pantry) available to needy families.
- Deliver food that has not been distributed at the MIYFS Food Pantry to Northwest Harvest.
- Provide low cost counseling services to local youth and families. Provide access to employment services, emergency family rent/clothing/school supply assistance.
- Provide access to youth volunteer program to undertake sustainable projects through agencies such as Earth Corps, King Conservation District, Mountains to Sound Greenway, Nature Consortium, and Mercer Island Farmer’s Market.

The costs for most of these activities will be covered by savings generated from higher resource efficiencies and one-time funding, as needed. In addition, coordination and public education efforts will be overseen by the Communications/Sustainability Coordinator position proposed in this Budget. See Sustainability policy in Section C (Budget Policies) for more details.

Utility Rates

The proposed 2013-2014 utility rates will have been fully reviewed by the Utility Board in October 2012. To date, the Board has reviewed and made a recommendation on the 2013-2014 sewer and storm water rates.

Budget Message

- **Water Rates** – An 8.0% increase is recommended for 2013 and 2014. For a single family residential customer, that translates into a \$5.64 increase in the average bi-monthly bill (based on a bi-monthly usage of 16 ccf). As in past years, the rate increase is driven largely by capital improvement needs of the system. In the 2013-2014 biennium, the staff and Utility Board will continue to focus on upsizing water mains that do not meet the City’s flow capacity standards. In addition to capital improvement needs, the rate increase maintains needed cash flows in light of lower than expected water sales. As water customers conserve on usage, water rates must increase to cover the utility’s fixed costs. The Utility Board will review and make a recommendation on the proposed 2013-2014 rate increases at its October 2012 meeting.
- **Sanitary Sewer Rates** – This covers the City’s portion of operating and maintaining the sanitary sewer system and equals about 50% of the total bi-monthly sewer bill paid by the average single family residential customer. The other 50% is the Sewage Treatment charge (discussed below). For 2004-2012, the City Council approved significant annual increases in the “sewer line maintenance” rate in order to fund the repair and replacement of the lake line along the northwest shore of Mercer Island. The proposed rate increase for 2013-2014 is largely driven by the capital reinvestment needs of the system, after being held to a minimum during construction of the Sewer Lake Line replacement project. At the September 2012 meeting, the Utility Board unanimously recommended a 9.5% increase for 2013 and 2014. This represents a \$5.83 increase to the average single family residential customer’s bi-monthly sewer bill in 2013.
- **Sewage Treatment Rate** – This is a “pass through” charge assessed by King County, which will increase by 10.2% in 2013 and 0% in 2014. This represents a \$7.38 increase in the bi-monthly bill for an average single family residential customer and is driven largely by the costs to finance the Brightwater sewage treatment plant.
- **Storm Water Rates** – The Utility Board unanimously recommends a 5.1% increase for 2013 and 2014. This translates into a \$1.53 increase in the 2013 bi-monthly bill of all single family residential customers. The new storm water rates will cover all costs associated with street sweeping, which were previously charged to the General Fund, as well as ongoing capital and operating activities related to the drainage system. Water quality improvements continue to be a major thrust of the Storm Water Utility.
- **Emergency Medical Service (EMS) Rates** – Emergency Medical Service rates for 2013 are tied to the current (2012) average cost (salaries and benefits only) of four firefighters, who were hired back in 1996 to provide capacity to handle simultaneous EMS calls. For 2013, staff is recommending that the rates be increased by 12.7%, which equates to a \$0.91 increase on an average single family residential customer’s bi-monthly bill. This increase represents a “true up” adjustment, which happens once every two years, to re-tie the rates (with a one year lag) to the current average cost of the four firefighters. A 4.3% increase is projected for 2014. The Utility Board will review and make a recommendation on the proposed 2013-2014 rate increases at its October 2012 meeting.

Sustainability Coordinator – As mentioned previously, the Sustainability Task Force strongly recommends funding a position to advance sustainable practices at the City. This budget proposes to combine the previously budgeted Communications Coordinator and the newly proposed Sustainability Coordinator functions into one full time position. Agreeing with the Task Force, the Utility Board recommends funding that portion of the Sustainability Coordinator position that supports sustainable practices in the utilities with utility rates. As a result, proposed utility rates include \$56,421 in 2013 and \$58,305 in 2014 for the position.

Taken together, the total (i.e. water, sewer, storm water, and EMS) bi-monthly utility bill for the average single family residential customer will go up by 8.8% in 2013 and 5.5% in 2014, which equates to a \$21.29 and \$14.53 increase respectively, as noted in the following table.

Description	2012	2013	2014
Mercer Island bi-monthly bill	\$241.19	\$262.48	\$277.01
Rate increase over prior year	5.9%	8.8%	5.5%
Dollar increase over prior year	\$13.39	\$21.29	\$14.53

Every two years the Association of Washington Cities conducts a Tax and User Fee Survey. For 2012, the water, sewer, and storm water bi-monthly utility rates for Mercer Island and the King County average (for the 20 cities/districts that responded to the survey) are presented in the table below. The comparison assumes an average 16 ccf of water usage per bi-monthly billing period.

Jurisdiction	Water	Sewer Maintenance (City)	Sewage Treatment (King Co.)	Storm Water	Total
Mercer Island	\$70.40	\$61.51	\$72.20	\$29.92	\$234.03
King County average	\$77.55	\$95.10	\$72.20	\$25.64	\$270.49

Relative to the King County average, Mercer Island's bi-monthly utility bill, excluding the EMS utility, is 13.5% less in 2012 for a single family residential customer using 16 ccf of water.

See Section F (Utility Funds Summary) for additional detail.

Capital Improvement Program

The 2013-2014 Capital Budget is part of the broader six-year Capital Improvement Program (CIP). The policy basis for the CIP is explained in detail in Section C (Budget Policies). Actual project details and financing strategies are also detailed in Section H (Capital Improvement Program). Listed below are the key issues and initiatives associated with the proposed CIP.

Financing Strategies

The CIP continues to be largely a pay-as-you-go program. Utility rates cover all capital expenditures for water, sewer, and storm water facilities. Public building, streets, trails, and parks capital maintenance are supported in whole or in part by real estate excise tax receipts. Major technology system and public safety equipment costs are funded by General Fund revenues. Finally, fleet and computer replacements are funded by annual contributions to their respective sinking funds. In addition to REET revenues, the Street Fund receives revenues from the local portion of the fuel tax.

Projected fund balances (shown in thousands) are presented in the following table for all CIP-related funds. They exclude reserves dedicated for specific purposes (e.g. all-weather field sinking fund in the Capital Improvement Fund). The six-year CIP draws down fund balances, with the Street Fund going negative in 2015-2018 and the Sewer Fund going negative in 2013-2015. For the Street Fund, the negative balance means that there is no money available for capital projects. For the Sewer Fund, the negative balance is not a significant concern, because it has an operating and capital reserve which can temporarily and comfortably fund a modest deficit up to \$200,000. The Street Fund doesn't have an

Budget Message

operating or capital reserve. Drawing down the fund balances like this, especially in the Street Fund, represents a calculated risk in order to take advantage of a continuing favorable bid environment. The Council opted to take the same calculated risk in the 2011-2012 Budget, which has worked out well with the negative 2013-2014 balances originally projected in the Street Fund and Capital Improvement Fund back in 2010 not coming to fruition. Absent a better than projected improvement in 2013-2014 REET receipts and/or a new revenue source, the CIP projects planned for 2015-2016 in the Street Fund will need to be scaled back dramatically and pushed out to future years.

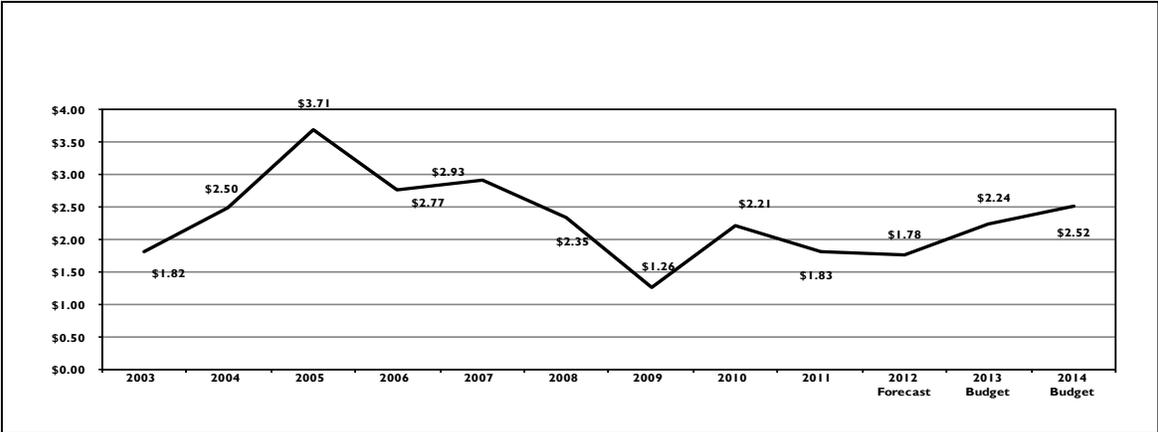
Fund	2012 Forecast	2013 Forecast	2014 Forecast	2015 Forecast	2016 Forecast	2017 Forecast	2018 Forecast
Street	1,340	616	219	(588)	(959)	(1,337)	(1,982)
Capital Improvement	1,474	1,293	1,078	333	277	(78)	(541)
Technology & Equip.	398	249	148	95	69	25	(77)
Water	2,183	351	316	337	192	(13)	15
Sewer	456	(146)	(74)	(183)	23	(79)	176
Storm Water	1,968	1,225	575	492	399	181	(1)

Real Estate Excise Tax

The Real Estate Excise Tax (REET) is the main revenue source to the Street Fund and the Capital Improvement Fund. REET revenues have been volatile over the last 10 years. During 2003-2007, the City experienced unprecedented levels of REET revenue due to a boost in the number of home sales amidst a low interest rate environment.

In 2008, the nation and the Puget Sound region experienced a major contraction in the housing market. As a result, the number of home sales on Mercer Island dropped from 608 homes in 2004, which represented the peak sales year, to 265 homes in 2008. Average home sales prices declined from a high of \$1.24 million in 2008 to \$854,000 a year later. Since 2008, real estate activity has improved slowly, with 400 sales projected in 2012 at a projected average sales price of \$900,000. By 2014, the number of home sales is forecast to reach 470 with an average sales price of \$1,020,000. Actual and forecasted REET revenues for the period of 2003-2014 are shown in the chart below.

Real Estate Excise Tax 2003-2014 (in Millions)



Project Management

The City's adopted CIP policy states, “whenever possible, capital projects will be scheduled and completed in the same year [for which funding is approved]”. In addition, City staff has made it a consistent practice to show how all CIP projects will account for their project management expenses in their project budgets. Project management staffing will come from staff or otherwise be outsourced at skill levels and quantities to design and construct CIP projects in the timeframes approved by the City Council. Because the number and complexity of utility and street capital projects is outpacing the capacity of the City’s small engineering staff, an additional contract engineering technician position is planned. The engineering technician has basic engineering skills but is not professionally licensed and will be compensated at a significantly lower rate than an engineering consultant or a staff engineer. Because the City already includes project management costs in the total budgeted cost of a capital project, there is no additional cost impact to the CIP. The technician would perform work otherwise done by the engineer. The addition of this position will improve efficiency in project management and provide a more cost effective means to ensure that projects continue to be implemented within budget and on time.

Parks and Open Spaces

- **Luther Burbank Playground Replacement** – Design and construction of a new playground for Luther Burbank Park is proposed for the biennium. A public process will be initiated to obtain public input during the design of the new facilities. Private donations are actively being sought to provide a portion of the funding for the project.

Streets, Pedestrian and Bicycle Facilities

The proposed 2013-2014 Budget includes \$4.4 million in roads, streets, and pedestrian/bicycle improvements. Among them are the following projects for the biennium:

- **Arterial Streets** – The primary project for the biennium is Phase 2 of the re-surfacing of Island Crest Way (SE 40th to Merrimount Drive). The City will also continue its modest arterial street preservation program.
- **Residential Streets** – The biennial allocation for residential overlays is \$1.2 million, which includes both standard hot mix overlays and the new use of cost effective chip seals.
- **Roadside Shoulders** – Shoulder improvements along East Mercer Way will continue in 2013-2014.
- **Pedestrian and Bicycle Facilities** – A North-South bike route from Southeast 62nd Street, south of Island Crest Park, to Island Park Elementary will be installed in 2013. In addition, the Safe Routes to School program will continue at \$100,000 of funding, and other small PBF Plan projects will be implemented (\$45,000).

Utilities

- **Sewer** – Modernization of Pump Station 14 is planned for 2013 at an estimated cost of \$375,000. The pump station is antiquated (parts are no longer available) and safety concerns exist about operating the station in compliance with current safety regulations. A portion of the sewer line along East Mercer Way (5600 block) needs to be replaced in 2014 at an estimated cost of \$500,000. In addition, staff will continue to focus on telemetry improvements, pump station repairs and emergency generator replacements. An update to the 20-year capital plan in the General Sewer System Plan is scheduled for 2014.

Budget Message

- **Storm Water** – In 2013-2014, the City will begin a program of installing two or three water quality treatment devices per year to reduce pollutants entering Lake Washington. The City will also undertake a systematic investigation to identify and remedy sources of dissolved copper and zinc in Basins 10 and 32b. The City plans to construct improvements for Sub-Basins 4, 6, and 27 at an estimated cost of \$1.04 million and an extension to the First Hill drainage system. In addition, the City plans to undertake replacement of the aging/undersized portions of the East Seattle drainage system.
- **Water** – The City will continue with its annual water main upsizing, pressure reducing valve, meter and hydrant replacement programs. Projects include system improvements and/or main replacements along a portion of Island Crest Way and 85th Ave, Sandy Cove, Mercerwood Drive, and 88th Ave. and 86th Ave. An update to the Water System Plan is scheduled for 2014.

Other Projects

- **Sustainability Investment** – Initial seed funding (\$50,000) is proposed to further the City's sustainability goals. Operation and maintenance savings from funded projects (i.e. reduced energy costs) will be tracked and re-invested in additional sustainability projects.
- **Fire Station 92** – If the proposed levy is approved by voters this November, final design of a replacement for Fire Station 92 will be completed in 2013, and construction would be completed by early 2015.
- **Thrift Shop/Mercerdale Park Planning** – In order to thoughtfully develop proposed capital projects to serve the needs of both the Thrift Shop and Mercerdale Park, the City plans to complete a mini-master plan in 2013. The plan will include schematic and conceptual design for accommodating a remodeled or new Thrift Shop, park improvements, site planning, parking inventory, capital improvement projects, financing and cost estimates. The planning process will include public meetings and other opportunities for citizen input.
- **Technology** – Technology projects for the biennium include completing computer equipment replacements and implementing necessary server software and financial system upgrades.

Acknowledgements

Each budget development cycle represents a major planning, analysis and coordination effort by City staff. The process begins in March and continues through September, concurrently with delivery of all other public services to the City's many customers.

Once again, we recognize the dedication and hard work that all staff put into the budget process. In particular, Finance Director Chip Corder, Deputy Finance Director Francie Lake, and Accounting Manager Lajuan Tuttle have all demonstrated the expertise and professionalism for which Mercer Island has become known. Others involved in the writing, proof-reading and production of the budget document include City Clerk Ali Spietz and Deputy City Manager Noel Treat. For all these fine efforts, the City Manager expresses his sincerest thanks.

Postscript

In October-December 2012, the City Council reviewed the 2013-2014 Preliminary Budget proposed by the City Manager. After directing staff to make a number of adjustments, the City Council adopted the 2013-2014 Final Budget on December 3, 2012. These adjustments are summarized by fund and broken down as follows: 1) expenditure adjustments, and 2) revenue adjustments.

General Fund	2013	2014
Expenditure Adjustments		
Made by Council:		
Move street sweeping costs (0.75 FTE, street sweeper & 1 vehicle) from Storm Water Fund back to General Fund	\$100,500	\$103,728
Restore parks maintenance level of service (ongoing)	60,000	60,000
Restore Groveland Beach lifeguards (ongoing)	26,000	26,000
Restore Arts Council programs for 2 years	13,000	13,000
Keep Right-of-Way position vacant for 2 years	-85,679	-92,481
Made by Staff:		
Reduce budgeted employee benefits per actual 2013 medical, dental, vision, and L&I rates	-98,436	-117,130
Reduce budgeted employee COLA per First Half 2012 CPI-W	-9,488	-9,240
Cut biennial citizen survey		-15,000
Minor corrections (salaries & benefits)	-1,187	283
Total Expenditure Adjustments	\$4,710	-\$30,840
Revenue Adjustments		
Made by Council:		
One-time transfer from 1% for the Arts Fund for Arts Council programs	\$11,000	\$11,000
Increase sponsorships/donations for Arts Council programs	2,000	2,000
Made by Staff:		
Reduce interfund administrative charges to Water, Sewer, and Storm Water Funds per changes to departmental budgets in General Fund	-4,472	-4,916
Reduce electric/gas utility tax estimates to re-balance fund	-21,371	-21,371
Adjust budgeted beginning fund balance between 2013 and 2014	17,553	-17,553
Total Revenue Adjustments	\$4,710	-\$30,840

Budget Message

Street Fund	2013	2014
Expenditure Adjustments		
Made by Council:		
Push construction portion of Island Crest Way Resurfacing Phase 2 project out to 2015-2016		-\$1,078,000
Made by Staff:		
Use design portion of Island Crest Way Resurfacing Phase 2 project for road preservation in 2013-2014 (split 50/50 between both years)	-\$50,000	50,000
Minor corrections (salaries, benefits & fleet rates)	-922	-998
Total Expenditure Adjustments	-\$50,922	-\$1,028,998
Revenue Adjustments		
Made by Staff:		
Adjust budgeted beginning fund balance to re-balance fund	-\$50,922	-\$432,927
Total Revenue Adjustments	-\$50,922	-\$432,927

Criminal Justice Fund	2013	2014
Expenditure Adjustments		
Made by Staff:		
Minor corrections (salaries & benefits)	-\$2,238	-\$2,475
Total Expenditure Adjustments	-\$2,238	-\$2,475
Revenue Adjustments		
Made by Staff:		
Adjust budgeted beginning fund balance to re-balance fund	-\$2,238	-\$2,475
Total Revenue Adjustments	-\$2,238	-\$2,475

Budget Message

Beautification Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Staff:		
Eliminate interfund transfer to Capital Improvement Fund for Thrift Shop Site Planning project (due to narrowed scope)	-\$12,500	
Minor corrections (salaries & benefits)	693	\$2,109
Total Expenditure Adjustments	-\$11,807	\$2,109
<u>Revenue Adjustments</u>		
Made by Staff:		
Adjust budgeted beginning fund balance to re-balance fund	-\$12,500	
Total Revenue Adjustments	-\$12,500	

1% for the Arts Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Council:		
One-time transfer to General Fund for Arts Council programs	\$11,000	\$11,000
Total Expenditure Adjustments	\$11,000	\$11,000
<u>Revenue Adjustments</u>		
Made by Staff:		
Reduce funding from CIP projects that were pushed out to 2015-2016 or beyond	-\$14,000	-\$12,000
Adjust budgeted beginning fund balance to re-balance fund	19,000	6,000
Total Revenue Adjustments	\$5,000	-\$6,000

Budget Message

Youth & Family Services Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Staff:		
Increase interfund transfer to Capital Improvement Fund for Thrift Shop Site Planning project (for full amount of project)	\$12,500	
Minor corrections (salaries, benefits & fleet rates)	-7,334	-\$7,966
Total Expenditure Adjustments	\$5,166	-\$7,966
<u>Revenue Adjustments</u>		
Made by Staff:		
Adjust budgeted beginning fund balance to re-balance fund	\$5,166	-\$7,966
Total Revenue Adjustments	\$5,166	-\$7,966

Bond Redemption (Non-Voted) Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Staff:		
Debt service on South Fire Station & Fire Rescue Truck bonds (per 9 year levy lid lift approved by voters on 11/6/12)	\$662,000	\$662,000
Total Expenditure Adjustments	\$662,000	\$662,000
<u>Revenue Adjustments</u>		
Made by Staff:		
9 year levy lid lift approved by voters on 11/6/12	\$662,000	\$662,000
Total Revenue Adjustments	\$662,000	\$662,000

Budget Message

Capital Improvement Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Staff:		
Eliminate South Fire Station Building Repairs project because South Fire Station & Fire Rescue Truck levy lid lift passed on 11/6/12	-\$62,000	-\$51,000
Minor correction (Parks capital replacement projects)	-1,000	
Total Expenditure Adjustments	-\$63,000	-\$51,000
<u>Revenue Adjustments</u>		
Made by Staff:		
Interfund transfer from Fire Station No. 92 Construction Fund (reimbursement of pre-design costs incurred before levy lid lift vote)	\$100,000	
Minor correction (interfund transfer from YFS Fund)	-500	
Adjust budgeted beginning fund balance to re-balance fund	-100,856	-\$51,000
Total Revenue Adjustments	-\$1,356	-\$51,000

Fire Station No. 92 Construction Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Staff:		
Construction costs for South Fire Station	\$4,703,000	
Interfund transfer to Capital Improvement Fund (reimbursement of pre-design costs incurred before levy lid lift vote)	100,000	
Total Expenditure Adjustments	\$4,803,000	
<u>Revenue Adjustments</u>		
Made by Staff:		
Recognize LTGO bond proceeds related to construction of South Fire Station (per 9 year levy lid lift approved by voters on 11/6/12)	\$4,803,000	
Total Revenue Adjustments	\$4,803,000	

Budget Message

Water Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Council:		
Push Island Crest Way & 85 th Avenue Water System Improvements project out to 2015-2016	-\$1,596,000	
Made by Staff:		
Reduce interfund administrative charges to Water Fund per changes to departmental budgets in General Fund	-2,223	-\$2,474
Minor corrections (salaries, benefits & fleet rates)	-286	-1,902
Total Expenditure Adjustments	-\$1,598,509	-\$4,376
<u>Revenue Adjustments</u>		
Made by Staff:		
Reduce water utility rates	-\$174,898	-\$404,203
Adjust budgeted beginning fund balance to re-balance fund	-1,375,774	399,827
Total Revenue Adjustments	-\$1,550,672	-\$4,376

Sewer Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Council:		
Push East Mercer Way Sewer Replacement project out to 2015-2016		-\$500,000
Made by Staff:		
Reduce interfund administrative charges to Water Fund per changes to departmental budgets in General Fund	-\$2,223	-2,474
Minor corrections (salaries, benefits & fleet rates)	-3,453	-4,627
Total Expenditure Adjustments	-\$5,676	-\$507,101
<u>Revenue Adjustments</u>		
Made by Staff:		
Reduce sewer utility rates	-\$174,207	-\$306,049
Adjust budgeted beginning fund balance to re-balance fund	168,531	
Total Revenue Adjustments	-\$5,676	-\$306,049

Budget Message

Storm Water Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Council:		
Push First Hill Drainage System Extension project out beyond 2018	-\$425,000	
Move street sweeping costs (0.75 FTE, street sweeper & 1 vehicle) from Storm Water Fund back to General Fund	-114,834	-\$118,062
Made by Staff:		
Reduce interfund administrative charges to Storm Water Fund per changes to departmental budgets in General Fund	-495	-551
Minor corrections (salaries & benefits)	-21,777	-21,778
Total Expenditure Adjustments	-\$562,106	-\$140,391
<u>Revenue Adjustments</u>		
Made by Staff:		
Reduce storm water utility rates	-\$67,537	-\$139,328
Adjust budgeted beginning fund balance to re-balance fund	-494,569	-1,063
Total Revenue Adjustments	-\$562,106	-\$140,391

Equipment Rental Fund	2013	2014
<u>Expenditure Adjustments</u>		
Made by Staff:		
Minor corrections (salaries, benefits & fleet rates)	-\$1,352	-\$1,571
Total Expenditure Adjustments	-\$1,352	-\$1,571
<u>Revenue Adjustments</u>		
Made by Staff:		
Reduce vehicle replacement charges	-\$2,458	-\$2,458
Total Revenue Adjustments	-\$2,458	-\$2,458

Budget Message

Computer Equipment Fund	2013	2014
Expenditure Adjustments		
Made by Staff:		
Minor corrections (salaries & benefits)	-\$2,448	-\$2,580
Total Expenditure Adjustments	-\$2,448	-\$2,580

A summary of how the 2013-2014 General Fund budget was ultimately balanced by the Council is presented in the table below.

Balancing the General Fund Budget	2013	2014
Projected deficit	-\$1,189,622	-\$1,479,373
Plus expenditure reductions	680,004	852,217
Less service enhancements (one-time & ongoing)	-238,330	-322,739
Plus new/enhanced revenues:		
Utility tax on City's water, sewer & storm water utilities (3.9% in 2013 & 5.3% in 2014)	425,000	625,000
1% optional property tax increase	106,471	108,535
Fee/charge increases	58,578	66,618
Plus available beginning fund balance	157,899	149,742
Balance	\$0	\$0

Appendix A

Priorities – Mercer Island City Services

I. The community will be safe.

- 1.1 {
 - Make timely and effective responses to crime.
 - Make timely and effective responses to fire.
 - Make timely and effective responses to medical emergencies.
 - Crime is investigated and prosecuted.
- 1.2 {
 - Buildings are safely built.
 - The transportation system is safely built and operated.
 - The City's drinking water will be safe.
- 1.3 {
 - Crime is prevented.
 - Fires are prevented.
 - Mental and physical health problems are prevented.
 - Emergency responses are planned for.

2. The community will support effective, efficient, sustainable and legal delivery of public services.

- 2.1 {
 - The City Council will have the information and forums necessary for making well-considered and informed decisions.
 - The decisions of the City Council will be implemented.
- 2.2 {
 - The City will comply with and enforce all applicable laws and ordinances.
 - The City will account for its expenditures and revenues and manage its finances according to all applicable laws and ordinances.
 - The City will provide for judicial services.
- 2.3 {
 - The City will continually evaluate and improve upon the effectiveness and efficiency of its services.

3. The community will support reliable public infrastructure and protect its considerable public investments (e.g. water, sewer, storm water utilities, streets, parks, buildings).

- 3.1 {
 - The City will operate and maintain its infrastructure to assure continuous, reliable and safe service.
 - The City will repair and replace its infrastructure before it fails.
- 3.2 {
 - The City will maintain its infrastructure to prevent failure and extend its useful life.

Budget Message

4. The community will support attractive, high quality neighborhood and business environments.

- 4.1 {
 - Public and private physical features such as streams, shorelines, ponds, forests/trees, lakes, parks, open spaces, trails and hillsides will be protected.
 - Land development regulations are applied and enforced.
 - Building design regulations are applied and enforced.
- 4.2 {
 - Parks, trails and open spaces are provided and maintained.
 - Developed public rights of ways will be used and maintained.

5. The community will support a broad range of recreational, cultural, health and educational opportunities.

- 5.1 {
 - The City will assist its least advantaged citizens with the basic necessities of food, shelter and health care.
- 5.2 {
 - The City will support mental and physical health services for all segments of the community.
- 5.3 {
 - The City will support the education of all segments of the community.
- 5.4 {
 - The City will provide recreational, cultural and community service programs for children and teens.
 - The City will provide recreational, cultural and social service programs for senior citizens.
 - The City will provide recreational, cultural and social service programs for adults.

6. Community will support open and informed public involvement processes within the structure of representative, democratic decision making.

- 6.1 {
 - The City Council will make decisions on behalf of the community.
- 6.2 {
 - The City will generate and disseminate public information to the community on the issues that confront the community and about the services and programs it provides.
- 6.3 {
 - The City will receive information and opinions from citizens, businesses and other interested parties during the course of its policy making and delivery of its services.

Appendix B

Comparing 2012 Monthly Tax Burden to 2012 Monthly Utility Bills For a Typical Mercer Island Household (\$700K Home & Family of 4)

2012 Average Monthly Bill	Amount
Puget Sound Energy (electricity & gas)*	\$195
Verizon (cellular telephone)*	\$180
Comcast (cable TV, high speed internet, and digital voice)*	\$180
City taxes (property, utility & sales taxes)	\$131
City utility charges (water, sewer, storm water & EMS)*	\$121

* Excludes state and local taxes and cable franchise fee.

City Taxes Fund the Following:

- 24/7 police, fire suppression, and emergency medical aid services
- Street, roadside, median, sidewalk, and path maintenance
- Park, ballfield, and trail maintenance
- Public building maintenance
- Recreation program support
- Youth & Family Services program support
- Public meetings and records management
- Community (i.e. land use) planning

City Utility Charges Fund the Following:

- Water storage, distribution, and maintenance
- Sewer collection, treatment, and maintenance
- Storm and surface water management
- Utility infrastructure replacement
- Staffing capacity (i.e. 4 firefighters) to respond to simultaneous emergency medical calls

Appendix C Expenditure Reductions Made in 2011-2012 General Fund Budget

	2011	2012
Expenditure Reductions (No Service Level Impact):		
2010 service packages & other one-time costs	665,773	665,773
Miscellaneous ongoing cost reductions	410,999	410,999
Reduced annual General Fund subsidy of YFS	145,000	145,000
No COLA in 2011	127,000	127,000
Expiration of Yakima Jail contract	103,460	103,460
Reduced annual technology CIP funding	100,000	100,000
Adjusted budgeted employee healthcare costs to actual rates	73,534	73,534
Subtotal	1,625,766	1,625,766
Service Level Reductions (Positions):		
Leave Parks Maintenance Manager (1.0 FTE) vacant for 2 yrs	90,352	93,744
Eliminate Transportation Manager (0.75 FTE)	87,353	90,538
Eliminate ROW Trial Maintenance position (1.0 FTE)	84,217	87,565
Eliminate Fire Marshal (1.0 FTE)	80,475	81,450
Reduce Communications Coordinator (0.4 FTE)	50,319	52,314
Reduce Court Administrator (0.5 FTE)	49,553	51,445
Eliminate Facilities Maintenance Tech (0.5 FTE)	42,866	44,579
Reduce Police Records Tech (0.5 FTE)	38,257	39,862
Subtotal	523,392	541,497
Service Level Reductions (Other):		
Reduced miscellaneous professional services	50,000	50,000
Reduced expenditure contingency	31,021	37,995
Reduced Recreation Program instructors	26,572	26,572
Eliminate Summer Celebration fireworks & evening events	24,500	24,500
Eliminate Groveland Beach lifeguard program	24,200	24,200
Eliminate ROW casual labor	12,150	12,150
Subtotal	168,443	175,417
Total Reductions	2,317,601	2,342,680