

CITY OF BELLEVUE
CITY COUNCIL

Summary Minutes of Special Meeting

April 8, 2024
6:00 p.m.

Bellevue Botanical Garden
Bellevue, Washington

PRESENT: Mayor Robinson, Deputy Mayor Malakoutian and Councilmembers Hamilton, Lee, Nieuwenhuis, Stokes and Zahn

ABSENT: None.

1. Call to Order

The meeting was called to order at 6:03 p.m., with Mayor Robinson presiding.

City Clerk Charmaine Arredondo called the roll and all Councilmembers were present.

2. Workshop

(a) Introduction - Financial Strategy and Budget Process Workshop

Acting City Manager Diane Carlson said that as she prepares to develop the budget over the coming months, she is looking ahead beyond the next two years to the next 20 years. She said the City's policies have served the organization and community well but have not been reviewed in a number of years. She said staff is focused on maintaining excellent services for existing and new residents and businesses and providing investments that support growth.

Ms. Carlson said staff will discuss the foundational elements of the City's fiscal approach, including the benefits of the strategic use of debt. Three specific areas for consideration to update are the financial strategy guiding principles, role and use of debt, and revenue policy including investment waterfall prioritization.

Ms. Carlson said staff will create a list throughout the discussion of Council questions and requests for additional information.

(b) Overview of Financial System

John Resha, Chief Financial Officer and Director, Finance and Asset Management (FAM) Department, said the budget process is underway with staff developing proposals for existing and new investments. From May to June, the multi-department budget evaluation team will review and rank the proposals before the Council budget workshop in June or July. The City Manager will release the preliminary budget in late September and Council adoption of the budget is

slated for late November. Mr. Resha said the City's financial system includes funds and accounting, financial planning, revenues, debt, reserves, operations, capital, biennial budget, and financial reporting, all of which are governed and guided by strategies, policies and processes. He said the strategic framework comprised of the Council Vision and strategic target areas helps to shape and guide the City's outcomes.

(c) Financial Strategy Guiding Principles

Mr. Resha presented draft conceptual financial strategy guiding principles for the Council's consideration. He said staff is requesting feedback to determine whether they are on the right track and whether there are other principles that should be included. The first of five guiding principles is transparency and clarity. Mr. Resha said that understanding the City's resources and financial processes and procedures is critical for the Council, the public and staff to effectively engage and to ensure accountability. The financial strategy should be approachable and clearly aligned with the City's priorities.

Mr. Resha said the second guiding principle addresses stewardship and integrity. As core values for the City, stewardship and integrity should be central to the financial strategy. Stewardship protects the City's resources with diligent oversight and strategic planning. Integrity serves as the ethical foundation with an emphasis on responsibility, truth, open communication and compliance with applicable regulations and statutes.

The third guiding principle relates to best practices and standardization. Mr. Resha said that grounding the financial strategy in industry best practices and a unified standard should result in advancing the City's outcomes. He noted that applying and reinforcing best practices is central to a sound financial strategy.

Responding to Councilmember Zahn, Mr. Resha said the Government Finance Officers Association (GFOA) best practices and Government Accounting Standards Board (GASB) provide key guidance for the City. He said new knowledge and technologies are incorporated into best practices on an ongoing basis.

The fourth guiding principle addresses minimizing risk and seizing opportunities. Mr. Resha said risk is inherent in any financial planning and management. However, the financial strategy should minimize risks within the City's risk tolerance. Mr. Resha said that risks bring opportunities, and the financial strategy should reflect the balancing of risk minimization with those opportunities that provide reasonable short- and long-term benefits.

The fifth guiding principle is that the financial strategy should be actionable and adaptable to evolving challenges with regular evaluation to identify possible improvements and appropriate adjustments. Mr. Resha said the financial strategy should be responsive to broader environmental conditions and provide actionable information to the Council, the public and City staff.

Councilmember Nieuwenhuis concurred with the value of being nimble. Referring to risk and opportunities, he asked how staff will assess good risks versus poor risks and how it will be different from how staff has assessed risks in the past. Mr. Resha said the process of risk analysis

contains a number of pieces including assessing risk appetite, risk tolerance, evaluations and discussions related to enterprise risk. Mr. Resha said the assessment starts with determining the financial risk for the cost-benefit analysis. He said the City utilizes its financial advisor to conduct that type of risk analysis on an ongoing basis. He suggested having a future conversation about enterprise risk management.

Deputy Mayor Malakoutian suggested changing the language from minimize risk to responsible risk management.

Mayor Robinson said minimize risk implies a choice to accept risk while responsible risk management implies managing a risk.

Mr. Resha suggested focusing for now on the concept of how to think about the City's approach to balance risks, commitments to the community, and stewardship. He said those concepts are essential for risk management.

Councilmember Lee suggested incorporating the word appropriate when referring to risk.

Councilmember Stokes said assessing risks is not just about taking actions that might have risks but also the risks associated with a lack of action.

Mr. Resha concurred and noted that risks can include legal risks, financial risks, operational risks or political risks.

Councilmember Zahn said that every decision has a risk and it is important to be transparent about the rationale underlying decisions.

Mayor Robinson summarized the Council's comments to minimize and manage appropriate risks and to consider the continuum of near-, mid- and long-term risks.

Mr. Resha asked whether the Council would like to add guiding principles to the City's Comprehensive Financial Policies and Procedures.

Councilmember Lee suggested reflecting the concept of innovation in the guiding principles. Mr. Resha said innovation does show up in the City's finances as staff thinks about investments and operations.

Deputy Mayor Malakoutian suggested including the concept of innovation within the adaptable and actionable guiding principle.

Mayor Robinson reiterated the question about whether the guiding principles should be part of the Comprehensive Financial Policies and Procedures or whether they should be practical guidelines for staff. She noted a Council consensus in support of including guiding principles.

Responding to Councilmember Zahn, Mr. Resha said he might challenge her statement that innovation and standards are two ends of a continuum. Mr. Resha said core standards are needed

to evenly evaluate and be prepared to respond quickly. He suggested that innovation and core standards are strong partners.

Councilmember Stokes said it is important to balance risks with opportunities and other objectives.

Councilmember Lee reiterated the importance of considering appropriate risks versus all risks.

(d) Role and Use of Debt

Mr. Resha acknowledged that there can be risks associated with debt. However, he suggested risk should be evaluated in an appropriate fashion. He said the current policy environment focuses on looking only at short-term risk and cash flow over the two-year operations budget or seven-year Capital Investment Program (CIP) Plan. He said the City currently has three debt components: City Hall, Meydenbauer Convention Center and Transportation Infrastructure Finance and Innovation Act (TIFIA) loans. He said the City uses debt primarily for capital projects (i.e., acquisition, construction) and the current growth rate in construction costs is 7.6 percent. When coupled with the increasing cost of land, the City needs to consider when and how to invest.

Mr. Resha said the City's current approach for a project needed in 10 years is to build up revenues to finance the project before moving forward with the project. If a shorter or mid-term debt instrument is used, investments can be made in today's dollars versus dollars 10 years from now. The result can be the ability to construct the project at approximately half the cost.

Mr. Resha said the City's financial advisor assists with preparing bond sales and wants to ensure the City does not harm its financial position within the investment community. He said the targeted debt ratio for government is approximately 2.0, which means \$2.00 of revenue for every dollar of debt service to be repaid. He said the City currently has substantially better coverage than that. He said the State caps the City's ability to take on debt at approximately \$6 million, which is higher than what the City would currently consider. A 2.0 debt service coverage ratio for a 20-year bond equates to \$2 billion to \$3 billion of capacity, far more than what the City would ever consider.

Mr. Resha said that while debt comes with a cost, it can also save the City money in the long term. He asked whether the strategic use of debt should be considered. He noted that conservative financial planning and management has put the City in a good place. However, he encouraged being thoughtful about how to get the best value from financial resources. He noted that the City's debt policies were established in the 1980s and 1990s, when there were a number of broader financial crises and regulatory changes. He said interest rates were high as well with mortgage rates as high as 13-15 percent. Mr. Resha said those policies were the right approach at that time for Bellevue as a smaller, suburban community. However, current growth and economic factors might make a different approach more appropriate.

Mayor Robinson said Amazon and Microsoft have provided large, low-interest loans to housing agencies to create affordable housing. She asked whether the City has ever considered that

approach or, for example, to provide a low-interest loan to KidsQuest Children's Museum for their expansion. Mr. Resha said staff would need to research the rules around that practice.

Deputy Mayor Malakoutian expressed support for broadening the use of debt. However, he asked how the City can avoid excessive borrowing that could have adverse, long-term generational impacts. Mr. Resha said for the City to self-bond or take out loans, a Council action would be required and the City would have an oversight role. There is fiduciary oversight from the agencies that sell the bonds. In addition, CIP projects are required to identify revenue sources.

Mayor Robinson said the question for the Council's consideration is whether the debt policy should shift to provide the strategic use of debt while maintaining a debt service coverage ratio of no less than 2.0.

Councilmember Zahn said she supports the concept. She agreed with the importance of keeping pace with growth and avoiding being too risk-averse. She said the City needs to be sure it is using debt instruments to advance priorities and to leverage value, with value being benefit divided by cost. She asked whether the City should set a guiding principle to maintain a certain bond rating. Mr. Resha said the current policy guides the City toward maintaining its AAA bond rating.

Councilmember Stokes expressed support for considering debt from a new perspective for the City.

Councilmember Hamilton expressed support for the strategic use of debt, especially given the City's current low level of debt.

Councilmember Lee said Bellevue has always been fiscally responsible and carried little debt, which is the basis for the AAA bond rating. He said it is important to be able to take advantage of opportunities and to continue to plan for growth. He said the question is whether debt is a good tool for the City to use. He said he always favors having more tools. However, the tool to use depends on the vision for the future. Mr. Lee said he believes in a pay-as-you-go approach, which has benefited the City. However, he said the use of debt for City Hall and transportation projects has been beneficial as well.

Councilmember Zahn said she would want to see the return-on-investment analysis of using debt.

Councilmember Stokes expressed support for the strategic use of debt to keep pace with growth and increasing needs within the community.

Mayor Robinson noted a general Council consensus in support of setting a policy to maintain a debt service coverage ratio of no less than 2.0.

At 7:05 p.m., Mayor Robinson declared a short break. The meeting resumed at approximately 7:15 p.m.

Mr. Resha stated his understanding that the Council supports considering the strategic use of debt. He said the specific debt service coverage ratio and other details can be discussed at a later time.

Councilmember Nieuwenhuis said that since the proposed approach to debt is a deviation from the City's longtime practice, he would encourage additional outreach to educate the public about why the City is considering a change.

(e) City Revenues

Mr. Resha said one-third of the City's revenues is generated by utility rates. Sales tax revenue, both general and special, make up 21 percent of overall revenues, and the business and occupation (B&O) tax represents 11 percent of revenues. He noted that the sales tax and B&O tax are sensitive to economic conditions and can fluctuate by greater than five percent within a given period. He said property tax revenues are the most stable resource and represent eight percent of overall revenues. The real estate excise tax (REET) represents four percent of revenues. Under state restrictions, REET 1 tax revenues must be used for capital projects and REET 2 revenues must be used for transportation and parks capital projects. Historically, the City has dedicated REET 1 revenues to transportation projects and REET 2 revenues to parks projects.

For general sales tax revenues, the City's practice has been to allocate 25 percent to capital projects and 75 percent for operating costs. State restrictions limit the use of special sales tax revenues to affordable housing and public safety. For B&O tax revenues, 21 percent goes to capital projects and six percent goes to transportation capital projects.

Mr. Resha said most of the City's practices date from the 1980s and 1990s, when the City's budget was substantially smaller and there was an interest in providing sufficient capital funding. At this point, the revenue streams are so large that revenues for capital projects represented \$140 million in the last biennium budget. He recalled the need to reduce operational costs related to the COVID-19 pandemic and said staff is asking the Council to consider deviating from the longtime practice to shift more capital funding to the operations budget. Mr. Resha recalled the decrease in funding for transportation maintenance activities due to lower revenues during the pandemic.

Mr. Resha said the City spends approximately 70 percent of its resources on operating costs and 30 percent on capital needs. Within that 30 percent, a portion is what he referred to as putting it in the bank for the future. He suggested looking at where the City stores that money and how it can make the money visible to the public for its specific protected use. He said the current practice essentially makes decisions before the staff and Council prepare the budget. Mr. Resha said he does not think the decisions would be significantly different. However, it could be beneficial to have the option of thinking differently about the split between operating and capital costs.

Mr. Resha said the sales tax and B&O tax are the most volatile revenues. However, even in the most volatile years the revenues have remained relatively stable. Mr. Resha noted the need for a better understanding of reserves in order for the Council to evaluate the volatility and the types of reserves that would mitigate the volatility.

Mayor Robinson said utility rate revenues are a large percentage of the revenues because the City is engaged in a major replacement of infrastructure over the coming years. She asked whether Mr. Resha anticipates that utility rates could decrease after some of the larger projects are completed. Mr. Resha said it is important to think about a 40-75 year horizon to smooth rates as much as possible. He said the strategic use of debt in the long-term plans could be one way to help smooth rates over time.

Responding to Councilmember Zahn, Mr. Resha suggested a future discussion regarding reserve levels and policies.

Councilmember Lee expressed concern about utility rates and noted that they are largely dependent on regional costs that the City does not control, especially for water.

(f) Enhanced Investment Waterfall

Mr. Resha said staff has been thinking about guardrails to ensure staff understands the community's and the Council's priorities. He described staff's use of the investment waterfall for capital projects to maintain current assets first before proposing new investments. He said he has used the investment waterfall approach at other organizations.

Mayor Robinson said the issue for the Council to consider is whether the investment waterfall should be used to guide all revenues or capital revenues only.

Mr. Resha described the five priority areas of the investment waterfall: 1) debt, 2) maintain assets and services, 3) meet growth demands, 4) plan for new assets to meet future growth, and 5) invest in new programs, services, assets and pilot projects. He said the City maintains its assets at a higher level than most industry standards and Bellevue taxpayers expect high-quality services. He said the investment waterfall is a framework to guide investments and to ensure that the most important priorities are supported.

Councilmember Lee referred to the fourth priority, item (B): Financially plan for services to support and maintain growth. He suggested adding "enhance" growth. For the fifth priority, he suggested adding a reference to innovation.

Councilmember Stokes expressed support for the investment waterfall framework.

Councilmember Nieuwenhuis concurred.

Councilmember Zahn said she likes the flexibility reflected in the investment waterfall framework. She asked whether staff envisions identifying short, medium and long-term investments. Mr. Resha said the City currently has short, medium and long-term financial plans.

The short-term plan is the current financial plan and the next 4-6 years and the mid-term plan is the 10-year CIP Plan. He said the CIP Plan is changing from a seven-year term to a 10-year term. Mr. Resha said staff is looking at bringing the City's long-range financial plans (e.g., utilities, transportation and other infrastructure) together to better plan for longer term investments.

Mayor Robinson expressed support for Councilmember Lee's suggestion about adding innovation to the fifth priority and said she would also like to see a reference to testing. However, she acknowledged that a pilot program is a form of testing.

Ms. Robinson referred to the second priority, item (D) identified as optional: Maintain the City's assets and services at a defined premium/alternative level. She suggested there should be a prioritization of high to low versus a defined premium level. Mr. Resha said staff wrestled with that issue and understands that more work is needed to parse out the difference. Ms. Robinson encouraged staff to consider a prioritization approach as an option.

Mayor Robinson noted a consensus in support of the general investment waterfall framework.

(g) Budget Process

Mr. Resha said staff will return in June for a budget workshop with the Council for further engagement on key questions, policies and the economic forecast. Staff anticipates discussion of the City Manager's preliminary budget on September 17 and department budget presentations will be scheduled through mid-October. The first budget public hearing is slated for September 24. The amended preliminary budget will be discussed and the second budget hearing will be held on November 12. Budget adoption is tentatively set for November 19. Mr. Resha said that under state law, revenues must be adopted by November 30.

Mr. Resha said staff is engaged and listening as they prepare the budget proposals in coordination with the City Manager.

(h) Changes and Potential Changes in Comprehensive Financial Policies and Processes for 2025-2026

Mr. Resha highlighted the last page of the meeting materials that lists changes and potential changes in the Comprehensive Financial Policies and Processes. The three potential changes were discussed tonight: 1) whether guiding principles should be added to the Comprehensive Financial Policies and Processes, 2) whether the strategic use of debt should be considered, and 3) whether the investment waterfall should be used to guide all revenues or capital only.

Responding to Mayor Robinson, City Manager Carlson encouraged Councilmembers to reach out to her or Mr. Resha with additional questions or comments. Mr. Resha said staff will hold another round of briefings with individual Councilmembers before the budget workshop this summer and again before the final budget is prepared.

Councilmember Lee concurred with Councilmember Nieuwenhuis's comment earlier in the discussion about educating the public about the changes in the budget approach. Responding to

Mr. Lee, Ms. Carlson suggested that staff follow up with him for further discussion about changes in the financial strategic framework.

Responding to Councilmember Zahn, Ms. Carlson said staff will return on April 16 to discuss and request Council approval of the priorities and strategic target areas discussed during the Council retreat. Councilmember Zahn suggested it would be important to provide an opportunity for the public to react to the proposed priorities.

Responding to Ms. Zahn, Mr. Resha said an early budget development public hearing will be held in June around the same time as the Council's budget workshop. He noted that the two public hearings required by state law will be held on September 24 and November 12.

Mayor Robinson thanked Mr. Resha and all staff involved in preparing the information and presentation.

17. Adjournment

At 8:37 p.m., Mayor Robinson declared the meeting adjourned.

Charmaine Arredondo, CMC
City Clerk

/kaw