

CITY OF BELLEVUE
CITY COUNCIL

Summary Minutes of Budget Workshop

March 26, 2018
6:00 p.m.

Public Safety Training Center
Bellevue, Washington

PRESENT: Mayor Chelminiak, Deputy Mayor Robinson, and Councilmembers Lee, Nieuwenhuis, Robertson, Stokes, and Zahn

ABSENT: None.

1. Budget Workshop

(a) Introduction and Overview

The meeting was called to order at 6:03 p.m., with Mayor Chelminiak presiding. He thanked BTV staff for videotaping the meeting, which will be posted on the City's website for the public to view.

Mayor Chelminiak said the City's budget is the most important policy document considered and approved by the Council. He said tonight's session is informational and an opportunity for the Council to raise questions and to provide feedback for future discussions.

Noting two new Councilmembers, Mayor Chelminiak said it took him two budget cycles to achieve comfort with the process. He said the focus of tonight's workshop is to provide an overview of the budget process, an update on the financial forecast, and a look at the longer term financial picture. Depending on the time remaining, the discussion will move forward to address the Utilities budget, results of the City's budget survey, and a preview of the Capital Investment Program (CIP) Plan.

Mayor Chelminiak noted there will be additional opportunities for continued briefings and discussions throughout the year.

(b) Budget Process, Calendar, and Public Engagement

City Manager Brad Miyake said state law requires the City Manager to prepare a budget for Council direction. He said staff is looking for early input to help shape the proposed budget and to address the long-term General Fund financial challenges and Utilities rates. The Council will

resume budget discussions in April. In the interim, staff briefings will be made available as desired by the Council. He thanked Deputy City Manager Kate Berens for her work related to the budget and tonight's presentation.

Finance Director Toni Call reviewed the budget process and calendar for the remainder of the year. The City Manager will present his proposed budget to the Council in October, and the Council will take formal action on the 2019-2020 budget and the 2019-2025 CIP Plan in December. Ms. Call noted that budget proposals will fall into the following Council-directed Budget Outcomes: 1) Economic Growth and Competitiveness, 2) Improved Mobility and Connectivity, 3) Safe Community, 4) Responsive Government, 5) Quality Neighborhoods and Innovative, Vibrant and Caring Community, and 6) Healthy and Sustainable Environment.

Reviewing the public engagement process, Ms. Call said there will be three public hearings (June, July, November) as well as a number of Council discussions during regular meetings. The Boards and Commissions are also involved in the budget process.

(c) General Fund Forecast and Longer Range Financial Information

Ms. Call presented the General Fund Forecast and highlighted key revenue sources. Expenditures exceed revenues by \$2 million beginning in 2022, and the gap grows to \$8 million in 2024. Key drivers of the increase in expenditures include the obligation to fund the LEOFF 1 (Law Enforcement Officer Fire Fighter) fund beginning in 2019, costs related to the opening of Fire Station 10 in 2022, and the 2022 expiration of the sales tax credit related to the Eastgate annexation. The forecast includes marketplace sales tax collections of approximately \$1 million in 2018, which increase to \$2.4 million in 2024. That tax is new and applies to online retail sales, and current revenue estimates are preliminary.

The primary drivers of increased revenues relate to sales tax and business and occupation (B&O) tax collections, as well as the emerging changes in the overall revenue structure. Expenditure drivers include known events (e.g., LEOFF 1, Fire Station 10), growth impacts, and the City's policy to maintain service levels.

Ms. Call highlighted sales tax revenue projections from 2019 to 2024 for Bellevue, Seattle, King County, and Washington State. Bellevue's major sectors contributing to sales tax collections are retail sales (28 percent), construction (20 percent), auto sales (16 percent), and all other business sectors (36 percent). Bellevue's sales tax growth is estimated at 4.4 percent in 2019, 4.9 percent in 2020, 4 percent in 2021, 4.3 percent in 2022, 4.9 percent in 2023, and 4.5 percent in 2024. Ms. Call noted that construction sales tax revenues can fluctuate significantly.

The City's revenue structure is comprised of the sales tax, B&O tax, property tax, utility taxes, and miscellaneous revenues. Sales tax and B&O tax projections provide 42 percent of the revenues from 2019 to 2024, compared to 39 percent in 2017. Ms. Call cautioned of the potential decrease in those revenues, however, in the case of an economic recession. The percentage of property tax revenues in overall revenues has decreased from approximately 25 percent to 18 percent (2018) over the past eight years.

Continuing, Ms. Call commented on the growth imbalance between expenditures and revenues. The average annual growth in overall expenditures is 4.1 percent. Personnel costs represent approximately 60 percent of expenditures and increase annually by an average of 4.2 percent. While the average annual growth in overall revenues is 3.2 percent, sales tax and B&O tax revenues have an average annual increase of 4.5 percent.

Looking at the next steps, Ms. Call said that, while the General Fund forecast shows an imbalance by 2023, there is time to manage expenditures and revenues as the budget is developed. Options for addressing the imbalance are to increase revenues and/or decrease expenditures. She said the Council's policy of building reserves provides time to study and consider solutions.

Ms. Call noted that General Fund reserves dip below the 15-percent threshold by 2022-2023 if no adjustments are made. She explained how adjustments to revenues and/or expenditures can maintain reserves at the 15-percent level from 2021 through 2024.

Ms. Call said the management of expenditures includes a focus on innovation and challenging the status quo, potential redundancies and efficiencies, near-term investments to create savings, and the use of technology. Examples include mobile technology to increase efficiencies in site inspections by the Parks and Community Services Department and the Transportation Department's 2011 investment in energy-saving LED street lights. The return on investment for the LED lights is an annual savings of \$200,000 for electricity. Additional examples include outsourcing commercial driving training and the purchase of a power post hole digging tool for \$500 that saves 30 minutes of labor for every post hole. Ms. Call noted that small efficiencies by departments add up, and staff is always looking for new opportunities to gain efficiencies.

Revenue strategies include potential increases in the property tax, B&O tax, admissions tax, and utility taxes. New sources to consider include special districts, a property tax for Fire personnel pensions and LEOFF 1 benefits, and a parking tax.

Referring to the different scenarios described above for maintaining the 15-percent reserves level [Slide 17 of presentation], Councilmember Robertson said she would like to see a similar analysis assuming the annual statutory one-percent property tax increase as a way to help maintain reserves. Ms. Call said staff will provide that analysis and noted that the property tax generates approximately \$500,000 annually.

Councilmember Robertson requested information on the statutory tax rates for each utility (e.g., water, sewer, storm water).

Referring to Councilmember Lee regarding the scenarios for maintaining a minimum of 15 percent reserves [Slide 17], Ms. Call said a net gain of \$1 million each year in 2019, 2020, and 2021 keeps the reserves above 15 percent until 2024. Beyond that point, reserves would be likely to dip below 15 percent. Ms. Call said staff could run a model that will show what it would take to maintain reserve levels at 15 percent or above beyond 2024.

Responding to Mayor Chelminiak, Ms. Call confirmed that reserves were down to nearly 10 percent in 2011 coming out of the recession, despite the elimination of approximately 100 full-time staff positions.

Deputy Mayor Robinson questioned the reliability of a financial model beyond 2024. Ms. Call concurred that the margin of error increases as the time horizon expands. However, projections for today from three years ago are fairly accurate.

Councilmember Zahn said she appreciates the sensitivity analysis regarding reserves. She noted it would be helpful to take the graph back 2-3 years to better understanding the trend.

Noting that personnel costs make up approximately 60 percent of operating costs, Ms. Zahn expressed an interest in the impacts of succession planning with an aging workforce as well as the implications of potential changes related to health care plans.

Responding to Councilmember Nieuwenhuis regarding the revenue structure, Ms. Call confirmed that the property tax does not increase at the same rate as other taxes or inflation. In further response, Ms. Call said current staffing is approximately at pre-recession levels.

Councilmember Robertson asked to discuss, during a future meeting, any actions that are planned to decrease personnel costs, particularly in the areas of health care benefits and pensions. She questioned the impact of business real estate transactions on the real estate excise tax (REET) collections and how that money could be used. She wondered whether the revenues could be applied toward the City's LOEFF 1 obligation.

Mayor Chelminiak cautioned that the use of REET collections is limited by state law to specific purposes, which he believes is primarily capital expenditures. Ms. Call said the current Council policy splits REET revenues between Transportation CIP and Parks CIP projects.

(d) Budget Survey and Business Survey Highlights

Ms. Call introduced Micah Phillips, Performance Measurement Program Coordinator, to present the results of the City's budget survey and business survey. The current budget survey was conducted from January 15 to February 11, 2018, and the full report will be completed by the end of April.

Mr. Phillips noted that the overall ranking of budget outcomes based on community priorities continues to be: 1) Improved Mobility, 2) Safe Community, 3) Healthy and Sustainable Environment, 4) Responsive Government, 5) Innovative, Vibrant, and Caring Community, 6) Quality Neighborhoods, and 7) Economic Growth and Competitiveness. When asked about the biggest problem that Bellevue is facing, 44 percent of the respondents identified traffic, 15 percent identified affordable housing and property values, 11 percent noted too much growth/congestion, nine percent identified human and social services (including homelessness), and seven percent noted public transportation.

Responding to questions about taxes and the funding of City services and facilities, the percentage of respondents willing to pay more to increase service levels decreased from 36

percent in 2016 to 29 percent in 2018. Approximately one-third of the respondents in both 2016 and 2018 indicated they are willing to pay more to support the increased cost of current service levels. For 2018, 20 percent of the respondents indicated they are not willing to pay more taxes even if the City must reduce service levels, and 12 percent said they are willing to reduce services in order to pay lower taxes.

Mr. Phillips described the quadrant analysis of how to best allocate resources based on the survey results, with services falling into one of the four quadrants based on the level of perceived importance and the satisfaction of the performance of those services: 1) above-average importance and above-average satisfaction, 2) above-average importance and below-average satisfaction, 3) below-average importance and below-average satisfaction, and 4) below-average importance and above-average satisfaction. The result of where services fall into the quadrant analysis has remained relatively unchanged for a number of years.

Next, Mr. Phillips reviewed the 2017 business survey results, which were previously presented to the Council in October 2017. Overall, the results are considered very positive. A total of 994 interviews were completed for the survey (796 online and 198 via telephone). The focus was on five business sectors: 1) business services, 2) information technology, 3) retail, 4) tourism, and 5) other. One question asked of businesses was their perspective of Bellevue as a place to operate a business, and the results were consistently positive across the five industries surveyed. Three-quarters of the businesses indicated that Bellevue is a somewhat or significantly better place to operate a business when compared to other cities, and 90 percent feel that Bellevue's economy is better than other cities in the Puget Sound region.

(e) Utilities Financial Policies and Rates Forecast

Nav Otal, Utilities Director, presented information regarding utilities financial policies, rate design, and the 2019-2024 early outlook utility rates forecast. She noted the challenges of the utilities business (i.e., fixed costs, services are not scalable, rates are the primary source of revenue, and the long-term operating horizon). Three sets of policies apply to utility rates: capital investment policies, rate management policies, and rate structure policies. Capital investment policies address long-term financial planning, intergenerational equity, and maintaining renewal and replacement reserves. Rate management policies address the funding levels needed to meet current and future expenses, gradual and uniform rate changes, pass-through wholesale costs, use of savings and one-time revenues, and the frequency of rate increases. Rate structure policies encompass cost of service, full cost recovery, rate equity and uniformity, rate assistance, and other policy objectives (e.g., water conservation).

Councilmember Zahn referred to the chart based on the 75-year renewal and replacement funding model, and questioned whether the information could be provided for each separate utility. Ms. Otal said staff will provide more information for future presentations.

Moving to the topic of utility rate design, Ms. Otal said the current water rate structure was adopted by the Council in 2015. It is based on the cost-of-service study findings, and key rate design objectives include equity for each customer class, revenue stability, affordable core water service, water conservation, and administrative efficiency.

Ms. Otal described the four rate tiers for single-family household water consumption. She said the model has been tested and compared to other options, and has been found to be equitable. She said summer water rates are higher due primarily to irrigation. She noted that the cost of a \$1 bottle of water equates to the cost of 100 gallons of water delivered by the public utility.

Moving on to sewer and storm water rates, Ms. Otal said sewer rates were last updated in 2004 and storm water rates were updated in 1996. She said cost-of-service studies are underway to generate rate design recommendations later this year. The Environmental Services Commission will review the rates and make recommendations for the budget.

Responding to Deputy Mayor Robinson, Ms. Otal said that peak usage of water occurs in the summer due primarily to irrigation. She noted that the Cascade Water Alliance has detailed data regarding overall usage.

Councilmember Nieuwenhuis said he appreciates the modeling used by the City and the proactive management of the utilities reserves. Responding to Mr. Nieuwenhuis regarding the rate increase in 2010, Ms. Otal acknowledged that the rate model did not anticipate that water conservation would continue to reduce consumption to current levels, especially given the projected population growth. The 2015 rate study was a response to examine customer profiles to better understand updated consumption patterns.

Responding to Councilmember Robertson, Ms. Otal said the pending implementation of advanced metering infrastructure (AMI) is financed by reserves and not through rate increases. In further response, Ms. Otal said the cost of purchased water is fixed due to agreements with the Cascade Water Alliance. Approximately 40 percent of the water utility's costs are for the purchase of water.

Ms. Robertson recalled that, when she served as liaison to the Environmental Services Commission, she was concerned about equity when the residential rate tier system was introduced. She said the tier system disproportionately burdens larger families. She would like the Environmental Services Commission to review the rate structure. She suggested that households with relatively low water usage are not paying the proportionate share of the fixed costs, while larger families are paying more than their fair share of fixed costs.

Councilmember Robertson said she would like to see further analysis of the residential tiers structure to determine how many people live in the average household and the average water usage per person. She opined that the tier structure is punitive for larger households. From a process perspective, Ms. Robertson questioned what would be needed to initiate further study.

Mayor Chelminiak noted that it would be a question for the Council about whether to review the residential rate tier structure.

Ms. Otal said the rate study completed two years ago followed industry standards and addressed both fixed and water volume charges. She said Bellevue has the highest recovery of fixed costs in the area. Kirkland, Issaquah, Mercer Island, and Seattle all receive higher revenue based on water volume charges. With the exception of Kirkland, neighboring cities charge more for water

than Bellevue. Ms. Otal said Bellevue's rate structure is based on industry standards. She noted that, any time costs are shifted from volume-based to fixed charges, a different group of customers is impacted. If the City wanted to subsidize high water users by adjusting fixed charges for all customers, low water users would end up paying more. Ms. Otal said that is counter to the principles of equity and conservation. In further response to Councilmember Robertson, Ms. Otal said no utility covers all of its fixed costs.

Responding to Councilmember Robertson, City Manager Miyake indicated that staff would need to develop a proposal of the resources needed to complete a new rate structure study before the Council decided how to proceed.

Responding to Councilmember Lee, Ms. Otal said the water rate tiers were determined based on a study conducted by a consultant following industry standards and using Bellevue data.

Councilmember Stokes recalled extensive review of the tiered rate structure by the Environmental Services Commission in 2012-2013, when he served as Council liaison to the commission. He said the number of people in the community who are questioning the model is relatively small, and he would not support an extensive review at this time. Mr. Stokes questioned how the discussion of utility rates relates to the broader budget discussion.

Ms. Otal said utility rates are adopted every two years. However, a full study of utility rate structures is expensive and is not typically conducted as a component of the biennial budget process. Councilmember Stokes said he was not interested in a review of the water utility rate structure at this time.

Responding to Councilmember Zahn, Ms. Otal said that usage of the rate assistance program has been relatively flat over the past several years. In further response, Ms. Otal said water usage trends are typically reviewed by decade, which is one reason that rate structures are not frequently reviewed. Ms. Otal said staff could provide information from 10-15 years ago to demonstrate trends.

Deputy Mayor Robinson said she was not interested in a review of the rate structure at this time. She noted there are agencies (e.g., Hopelink) that provide rate relief programs in addition to what is offered by the City.

Councilmember Robertson shared information indicating that average daily water use is 80-100 gallons per person, and noted why she believes the structure of the four rate tiers hurts larger families. She would like more information on per person water usage in Bellevue and how the rate structure affects families.

Mayor Chelminiak said he is not interested in revisiting the rate structure. He noted that water conservation can be managed within households, especially in the use of water for irrigation.

At 7:59 p.m., Mayor Chelminiak declared a short break. The meeting resumed at 8:11 p.m.

Ms. Otal presented the 2019-2024 Early Outlook Utility Rates Forecast. The forecast assumptions include maintaining current service levels and a lean budget, while acknowledging that costs are increasing beyond the level of inflation (i.e., wholesale costs, aging infrastructure, higher construction costs). Budget priorities focus on sustainable, high-quality utilities services as well as predictability in rates. She noted that utility rates pay for wholesale water, taxes and support services, wastewater treatment, Capital Investment Program (CIP) support, and local operations.

Ms. Otal said staff began reviewing the utilities budget with the Environmental Services Commission in January, and the Commission is currently reviewing the CIP budget.

The 2019-2024 Utility Rates Forecast includes water, sewer, and storm water rates. Ms. Otal said the typical residential monthly utilities bill reflects wholesale, CIP, renewal and replacement, taxes, and operations costs. Ms. Otal compared Bellevue with neighboring jurisdictions and noted that Bellevue's combined water, sewer and storm water rates are competitive within the region.

Councilmember Zahn said she appreciated receiving the comparison with other jurisdictions during her Council onboarding. She said it would be helpful to see a historical comparison of the rates. She said it would be interesting to see what the 2018 water bill example would look like in 2024.

Mayor Chelminiak said Deputy Mayor Robinson would be participating in a Bellevue Sister Cities trip to Yao, Japan. He noted a Council consensus to excuse her absence from the April 2 meeting.

(f) General 2019-2025 Capital Investment Program (CIP) Plan

Ms. Call introduced discussion of the general 2019-2025 Capital Investment Program (CIP) by highlighting the policies and practices used to build the seven-year CIP Plan. The City will see the first payment toward the TIFIA (Transportation Infrastructure Finance and Innovation Act) loan in 2024-2025, with an estimated annual payment of \$5.2 million. The CIP Plan adjusts the revenue forecasts to be in line with the General Fund operating forecast, maintains existing facilities and infrastructure before building new facilities, and continues all voted levies. After debt service payments and projects that maintain existing infrastructure, 2024-2025 available funding is estimated at \$38 million for restricted levy discrete projects (Fire, Parks, Neighborhood Transportation) and \$56 million for non-levy discrete projects.

Responding to Mayor Chelminiak, Ms. Call confirmed that the TIFIA loan is based on the federal government reimbursing the City, in the form of a loan, as it spends money on certain transportation projects. Mr. Chelminiak requested a list of the projects funded/reimbursed by the TIFIA loan as they occur. Ms. Call said the projects are anticipated to be completed by 2022.

Mayor Chelminiak requested information on the allowed uses of REET (real estate excise tax) collections under state law. Noting that the City's current policy splits REET revenues between the Transportation CIP Plan and the Parks CIP Plan, he said it would be helpful to see other options to consider.

Councilmember Robertson requested information on the transient occupancy tax (TOT) forecast. Ms. Call noted that the current operating agreement with the Bellevue Convention Center Authority (Meydenbauer Convention Center) limits the uses of TOT collections. She will provide more information. Mayor Chelminiak noted that the BCCA bonds will be paid off in 2024.

Responding to Deputy Mayor Robinson, Ms. Call said the longest option for beginning to repay the TIFIA loan would have been five years following substantial completion of the projects. However, the loan agreement reached between the City and the U.S. Department of Transportation established the first payment to occur in 2024.

In further response to Ms. Robinson, Ms. Call said staff will provide additional information on transportation impact fees for a future discussion.

Councilmember Zahn noted that the transportation needs list exceeds available funds. Responding to Ms. Zahn, Ms. Call said staff will provide a list of recent grants and pending grant applications. Ms. Zahn said it would be helpful to determine whether there are other partners the City could work with to provide needed projects.

Mayor Chelminiak noted that Councilmember Robertson will continue to be actively involved with the Puget Sound Regional Council (PSRC) Transportation Policy Board.

Responding to Deputy Mayor Robinson, Ms. Call said impact fees can be used only for capacity projects. Staff will provide more information.

Councilmember Lee concurred with Councilmember Robertson's concern about the utility rate structure and encouraged further discussion about the related issues as well as public education to help people understand the rates and fixed costs. Mayor Chelminiak noted that the total funds needed to maintain the utilities will be fixed, so if rates become lower for some, they will increase for others.

Councilmember Stokes concurred with the suggestion for enhanced public education, including the comparison of Bellevue's rates with other agencies' utility rates. However, he does not want to open up the risk of degrading the City's infrastructure and long-term services for the benefit of a short-term rate decrease.

Councilmember Zahn said she would like to revisit the broader issue of cost efficiencies (e.g., LED street lights, remote technology) and innovation. She questioned whether there are programs in place to award staff for innovative programs and solutions. Mr. Miyake said staff will follow up with related information for a future meeting.

Responding to Mayor Chelminiak, Mr. Miyake said it would be best to discuss any potential revenue changes for the 2019-2020 General Fund budget during the April-May timeframe.

Councilmember Stokes noted for the public that the budget is an important policy document that provides the tool for implementing the Council Vision and community priorities.

Mayor Chelminiak suggested that Councilmembers request staff briefings within their areas of interest. He encouraged a focus on the policy level throughout budget discussions versus diving into operational details. He said the goal is to adopt the best budget for residents and businesses.

At 8:58 p.m., Mayor Chelminiak declared the meeting adjourned.

Kyle Stannert, CMC
City Clerk

/kaw