

CITY OF BELLEVUE
CITY COUNCIL

Summary Minutes of Extended Study Session

April 26, 2010
6:00 p.m.

Council Conference Room 1E-113
Bellevue, Washington

PRESENT: Mayor Davidson, Deputy Mayor Lee, and Councilmembers Balducci, Chelminiak, Degginger, Robertson, and Wallace

ABSENT: None.

1. Executive Session

The meeting was called to order at 6:05 p.m., with Mayor Davidson presiding. There was no Executive Session.

Mayor Davidson noted that Councilmember Balducci would be joining the meeting momentarily.

2. Budget One Workshop

- (a) Presentation of the Healthy and Sustainable Environment; Economic Growth and Competitiveness; and Responsive Government Outcomes

City Manager Steve Sarkozy explained that the items to be discussed tonight are some of the building blocks for establishing the General Fund budget and Capital Investment Program (CIP) Plan.

Nav Otal, Budget One Project Manager, briefly reviewed the process to date, and noted that the staff Results Teams will complete their presentations tonight. Departments will respond to the Requests for Results from the outcome teams by submitting proposals. She noted concerns raised by Councilmembers during previous presentations about the desire to see more tangible community indicators related to the outcome factors. Ms. Otal said each outcome category will now have community indicators which reflect citizen feedback (e.g., percent of residents who feel Bellevue is a safe community) as well as key performance indicators (e.g., crime rates).

Doug Dossett, Web Developer, provided the presentation for the Healthy and Sustainable Environment Results Team. Factors within this outcome category are water resources, clean living environment, nature space, clean air, and conservation. Mr. Dossett acknowledged that this outcome area overlaps other outcome areas. Departments have been asked to keep this outcome area in mind in preparing their proposals, regardless of which outcome Results Team will review their proposals. Mr. Dossett briefly reviewed the factors, strategies, and community indicators.

Responding to Councilmember Degginger, Mr. Dossett said he has spent approximately 128 hours as team lead over the past five to six weeks.

Paul Inghram, Comprehensive Planning Manager, noted that he has spent approximately 110 hours on this budget assignment. He provided the presentation for the Economic Growth and Competitiveness Results Team. Key factors for this outcome are people and partnerships; community policy, planning and development; infrastructure; quality of community; and City brand. Mr. Inghram reviewed these factors and the corresponding community indicators.

[Councilmember Balducci arrived at 6:20 p.m.]

Deputy Mayor Lee stated that economic growth and competitiveness is an area of particular interest for him. Responding to Mr. Lee, Mr. Inghram commented on the importance of both a favorable business environment and a community that grows in ways that add value to the overall quality of life.

Deputy Mayor Lee noted that K-12 education is very important in terms of community health, which he feels should be included within this outcome area. Diversity is a component of economic growth and competitiveness as well. Mr. Lee said that economic development is a fundamental underlying component of a safe and healthy community, which he feels should be emphasized.

Mr. Inghram confirmed that schools are listed as sub-factors for this outcome area. He agreed with the suggestion to add diversity as well.

Councilmember Robertson suggested that diversity should be added as a sub-factor under the City brand factor. Other aspects of competitiveness for Bellevue are the cultural and natural environments.

Ms. Otal concurred with comments regarding the overlap of outcome areas, noting that staff has tried to balance capturing everything without being overly redundant.

Carol Helland, Land Use Director, presented for the Responsive Government Results Team. She explained that the factors and community indicators for this outcome area are based on surveys indicating the community's priorities and values. Factors are community connections, strategic leadership, engaged workforce, exceptional service, and stewards of the public trust. Ms. Helland noted that she has spent 118 hours as the lead for this Results Team.

Councilmember Balducci stated that this outcome area has potentially the most noticeable impact to the Council, because it will hear from citizens if City services and programs are not meeting their needs. She noted that she is still trying to understand how the templates of factors and community indicators (i.e., cause and effect maps) will be used to prioritize proposals. Ms. Balducci expressed an interest in more details about this outcome area, because Responsive Government is closely linked to the Council's role. She commented on the importance of ongoing communication between staff and the Council, which has a direct impact on the Council's workload.

Ms. Balducci suggested a review of the Neighborhood Enhancement Program (NEP), which has received some criticism for the types of projects that have been completed. She noted that this is an important program in terms of community involvement in making decisions about projects, and she feels this should be included under the Responsive Government outcome.

Councilmember Wallace thanked staff for their hard work in this effort. With regard to the Responsive Government outcome he feels it is about more than just listening, but also about responding and incorporating input into decision making. He suggested that there should be more of a feedback loop in certain areas in order to balance priorities and demands that are important to residents and workers. He noted that there are more employees within the community than residents.

Responding to the Council, Ms. Otal said staff's prioritized proposals will be discussed with the Council in July. The proposals will be posted to the Intranet in June and be available for review by the Council.

(b) Financial Forecast

Finance Director Jan Hawn opened discussion regarding 2009 financial performance data and the 2010 financial outlook.

Jonathan Swift, Budget Manager, said the three themes of the financial update are that the resource picture is not as strong as in past years, the demand for capital projects has grown, and there is a funding gap between the budget and the City's needs. He recalled that the Council's last financial forecast presentation was in January 2010.

Mr. Swift reviewed 2009 revenues, noting significant under-performance of the sales tax and business and occupation (B&O) tax. General Fund revenues were approximately \$12 million under budget, which is consistent with other municipal governments at this time. General Fund tax collections were lower in 2009 than in 2008. Mr. Swift explained that real estate excise tax (REET) collections were approximately 60 percent lower than budgeted, with residential transactions dropping from 3,400 in 2008 to 1,400 in 2009. Mr. Swift recalled early actions in 2009 to reduce spending, defer certain maintenance projects, and to not fill vacant staff positions.

Turning to the 2010 General Fund outlook, Mr. Swift said tax collections are expected to improve modestly over 2009 but remain lower than the adopted budget by \$15 million. Lower state pension rates and no cost of living pay increases will help somewhat. Cost containment measures will remain in place through 2010. Mr. Swift explained that the financial forecast provides an update on available revenues and an insight into long-term financial viability. An updated financial forecast will be provided in September, which will take into account the changes to be made to services and programs as Council's budget discussions move forward.

Responding to Councilmember Degginger, Mr. Swift clarified that staff will update the financial forecast in September to reflect the City Manager's proposed budget.

Mr. Swift said the economic outlook is a slow recovery over several years, with housing recovery as a critical component. Home and retail sales are increasing slowly, but credit is not widely available. Mr. Swift noted that housing drives consumption, retail sales, and employment. Employment is expected to recover more slowly than after previous recessions. Retail sales tax collections are expected to recover to 2007 levels by 2013.

Responding to Councilmember Wallace, Mr. Swift explained that the recovery rate for taxable retail sales is slower than past recovery performance.

Responding to Councilmember Balducci, Mr. Swift said retail sales tax collections from the Bravern are anticipated to be approximately \$600,000 this year. The City's total sales tax collections for all funds will be \$40 million to \$45 million.

Continuing, Mr. Swift reported that staff is predicting a two-year budget gap for 2011-2012 of \$20 million. This gap does not close over the seven-year forecast period. However, it narrows to \$4.3 million by 2016. Mr. Swift recalled that the January 2010 forecast projected a gap of \$17 million for 2011-2012.

Responding to Mayor Davidson, Mr. Swift said that major expenditures are health benefits costs and salary costs. Inflation is expected to remain modest, and NORCOM is expected to reduce Bellevue's long-term costs.

Mr. Swift next reviewed the Capital Investment Program (CIP) forecast results, which include both the Base CIP and the Mobility and Infrastructure Initiative. The forecast includes only adopted tax rates, fees, and appropriations, as well as adopted elements of the Mobility and Infrastructure Initiative. It does not include planned, but not adopted, projects, and it does not account for the potential results of the ranking of budget proposals by Results Teams.

For the Base CIP alone, expenditures are expected to exceed revenues by approximately \$11 million for the 2011-2017 forecast period. This does not include any major, new discrete projects or other high-priority projects.

Responding to Councilmember Degginger, Mr. Swift said examples of discrete projects are Northup Way, while the City's overlay program is an ongoing program and the largest CIP

program. Additional examples of ongoing programs include sidewalks, curb and gutter, Parks property acquisitions, and major maintenance for public safety and Parks facilities. In further response, Mr. Swift said the \$6 million in Parks maintenance and operations (M&O) is not in the CIP budget, but in the operating budget. He clarified that Council has the discretion to place this item in either the General Fund or CIP Plan.

Responding to Councilmember Degginger, Mr. Swift confirmed that the \$6 million for Parks Department maintenance and operations is not reflected in the CIP budget. It is reflected in the General Fund/Operating Budget, and is paid from the CIP allocation.

Councilmember Chelminiak questioned what is paid for on the operating side out of capital revenues that shows up on the operating side for maintenance and operations. Mr. Swift said maintenance and operations expenditures include grass mowing, janitorial services, and other ongoing services.

Jason Bentosino, Assistant Budget Manager, acknowledged that the CIP M&O component is not reflected in the Base CIP, but is located in the operating budget. This component represents approximately \$8 million annually and is funded by sales tax revenues.

Mr. Swift responded to additional questions of clarification regarding the 2011-2017 CIP forecast graph.

Responding to Councilmember Balducci, Mr. Swift confirmed that the 2011-2017 forecast shows everything in the 2009-2015 CIP Plan, without the projects expected to be completed by the end of 2010.

Responding to Councilmember Wallace, Mr. Swift said the forecast assumes that projects scheduled for completion by the end of 2010 will be completed. The other assumption is that the City would carry a line of credit borrowing forward and would repay it over the course of the seven-year CIP Plan.

Responding to Councilmember Chelminiak, Mr. Swift said that City Hall debt is separate from the CIP budget, and debt service payments are approximately \$7 million per year. He explained that sales tax, B&O, and other general CIP revenues are distributed directly to the debt service fund.

Mr. Sarkozy noted that more information on M&O budgeting and City Hall debt will be covered later in the presentation.

Continuing, Mr. Swift explained that CIP project costs have been decreased to reflect the favorable bidding environment. In terms of the CIP tax forecast, sales and B&O tax collections have been lowered to reflect the recession. However, REET collections have been revised upward to reflect projections of a recovering housing market.

Responding to Councilmember Wallace, Mr. Swift explained that REET projections are based on the Puget Sound economic forecast.

Councilmember Robertson observed that the CIP Plan deficit is greater in the first few years than in the last few years. She would like to see a cost-benefit analysis of the ability for borrowing to stabilize the CIP revenue flow. She questioned whether the current lower project bids could offset the cost of borrowing. She noted the need to have cost-benefit analyses built into the City budgeting process.

Mr. Swift said staff has explored this issue and will provide additional analysis for the Council. He cautioned that everything depends on the state of the economy. Within the current favorable bidding environment, it makes sense to borrow upfront because long-term inflationary costs will outpace short-term costs. The City currently has a line of credit at one percent, which is lower than the inflation rate. Mr. Swift said there is still some risk involved, because the debt will be repaid over a longer time period.

City Manager Sarkozy stated staff is looking at using the line of credit in the short term to stabilize project delivery within the seven-year CIP Plan. For the longer term, the City is looking at the potential of debt financing at the current low rates to provide some opportunities for project delivery beyond the current CIP Plan.

Mr. Swift reviewed forecast results for the Mobility and Infrastructure Initiative, which includes a limited set of adopted projects at this point, totaling \$10.2 million. The overall cost estimate for the plan has not changed since the January 2010 update. Revenues include current impact fee rates, local revitalization funding (NE 4th Street project), anticipated grants, and the initial property tax increase adopted in 2008.

Mr. Swift said the Mobility and Infrastructure Initiative forecast does not include \$285 million in planned projects or several revenues including Local Improvement District (LID) bonds (\$56 million) and the majority of property tax supported bonds (\$95 million).

Mr. Swift summarized that a \$20 million deficit is projected for the 2011-2012 General Fund. For the Base CIP, even with no new projects, the deficit is projected to be \$11 million. The Mobility and Infrastructure Initiative has a significant revenue shortfall as well.

Responding to Councilmember Chelminiak, Mr. Swift observed that from a financial policy perspective, when distributions of the CIP Plan are fixed to debt service, the volatility of the tax stream has a much more negative effect. Over time, the Base CIP has received a much lower percentage of the total sales tax than the General Fund. In 2006-07, the split was roughly 40 percent to the CIP Plan and 60 percent to the General Fund. The split in this forecast is 30 percent to the CIP and 70 percent to the General Fund.

In further response to Mr. Chelminiak, Ms. Hawn said the budget book includes graphs that clearly show the impact of the recession in lowering the overall base, portions going to M&O

versus debt, and what is left over for the CIP Plan. These will be reviewed later in the presentation.

Councilmember Balducci noted the ongoing increase in health care costs, which is a significant expenditure. She would like to see a history of the cost growth rate as well as actions taken by the City to control costs. She is interested in considering ways to make a more meaningful reduction in these costs.

Councilmember Degginger questioned how sales tax revenues are split between the General Fund and the General CIP. Mr. Swift explained that the initial policy established by the Council was to split the revenues evenly between the two budgets. When capital projects were complete, a distribution from the General CIP to the General Fund occur to cover only maintenance costs for the facilities, and not personnel, programming, or services costs. Over time, that distribution has changed to a 70 percent General Fund and 30 percent General CIP split. Mr. Swift noted that the percentages vary year to year, but the distribution from the General CIP to the General Fund increases over time at the rate of inflation and when new projects are completed.

Responding to Councilmember Degginger, Mr. Sarkozy said the policy and practice could be changed to simplify the transfer of M&O funds, and to maintain a primary commitment to the maintenance of existing facilities.

Mayor Davidson recalled that the Council has been aware of the M&O transfer and that eventually more sales tax revenue would be distributed to the General Fund.

Councilmember Degginger stated that in the time he has served on the Council, the Council has never designated fixed percentages of the sales tax distributions to the General Fund and General CIP. He referred to a page in the budget book with a question about the optimal split of tax revenue between the operating and capital budgets. He noted that it says nothing about the M&O transfer or the rate of inflation. Mr. Degginger commented that information appears to be missing in terms of framing the policy discussion on this issue.

At 7:45 p.m., Mayor Davidson declared a short break. The meeting reconvened at 7:56 p.m.

(c) Financial Policies

City Manager Sarkozy stated that this discussion is intended to get into the underlying policies of the budget.

Ms. Hawn opened staff's presentation, noting that this topic is an extension of the Council's retreat discussions in January. Overall, the financial policies have served the City well over the years, and they have provided the fiscal stability needed to meet policy objectives.

Ms. Hawn reviewed the City's key revenue policy and guiding principles. She described the 2009-2010 adopted General Fund resources, which reflect a mix of tax revenues (i.e., sales tax, B&O tax, property tax, utility tax), licenses and fees, intergovernmental revenues, and other

resources. She noted that property taxes and utility taxes are considered relatively stable, while the sales tax and B&O tax are economically sensitive. She reviewed a graph demonstrating a roughly 60-40 split of economically sensitive revenues versus stable revenues from 2003 through 2017. Adopted CIP resources include sales tax, B&O tax, REET, and Other Resources. All three taxes are economically sensitive, while grants and other funding are considered relatively stable, when available.

Responding to Councilmember Chelminiak, Ms. Hawn said Other Resources include the Parks levy, grants, gas tax revenue, impact fees, and the City's line of credit. She clarified that the property tax cannot be used to pay for bonds. The property tax goes to the General Fund, and sales tax is used to repay debt service.

Responding to Councilmember Robertson, Ms. Hawn said that in addition to monies that come into the General CIP and General Fund, there are Utilities funds and other funds that receive revenue.

Ms. Hawn commented that when the economy has been strong, the economically sensitive taxes have allowed the Council to make some important investments in the community. However, the recession has had a significant negative effect on these revenues.

Ms. Hawn noted that an underlying principle of the revenue policy is to remain economically competitive. She reviewed comparison information demonstrating that Bellevue's property tax rate of \$1.06 per \$1,000 assessed valuation (\$0.94 regular levy and \$0.12 voted levy) is the lowest in the region. She reviewed a graph reflecting the decline in Bellevue's property tax rate since 2000, which was due to the Council's decision to not use its banked property tax capacity. The increase reflected for 2010 is based solely on the drop in assessed valuation of 9.6 percent.

Councilmember Robertson asked for a graph depicting how assessed valuation has grown over time in relation to growth in the City's budget. Ms. Hawn said staff will provide this information.

Responding to Councilmember Degginger regarding the 29 percent of Other Resources for the 2009-2015 General CIP, Ms. Hawn said this includes \$24 million from the Parks levy, intergovernmental revenues of \$21.5 million, a \$40 million line of credit, and remaining revenues from the gas tax, grants, and impact fees. Mr. Degginger asked staff to provide a breakdown of these resources for the past five years or so.

Councilmember Wallace requested a comparison of total property taxes paid by Bellevue and other cities, including school district, county, and other property taxes. Ms. Hawn said staff will provide that information.

Responding to Councilmember Chelminiak, Ms. Hawn said apartments are included in the commercial assessed valuation, and condominiums are included in the residential assessed valuation.

Ms. Hawn reviewed a comparison of 2010 B&O tax rates in Bellevue and other cities. For retail sales, Bellevue's rate is higher than some of the smaller cities, but lower than Seattle's rate. For services, Bellevue's B&O tax rate is significantly lower than Seattle and Tacoma. Ms. Hawn noted that some B&O tax revenues are used to fund major capital needs that provide infrastructure for the business community.

Responding to Mayor Davidson, Ms. Hawn said Bellevue's maximum B&O capacity is 0.2 percent. Mr. Sarkozy noted that Bellevue has the existing capacity for a 0.05 percent increase. Bellevue's current rate is 0.1496 percent.

Ms. Hawn reviewed a comparison of the 2010 business tax burden on small, medium, and large businesses in Bellevue and other cities.

Responding to Councilmember Chelminiak, Ms. Hawn said the table compares the B&O tax burden, using other taxes such as a head tax or square footage tax for the cities that do not have a B&O tax. Ms. Hawn confirmed that the comparison does not account for Bellevue's low utility tax and low property tax.

Councilmember Robertson expressed an interest in a comparison of the total tax burden for Bellevue versus other cities. She reported on complaints from business owners who have had to pay B&O taxes even when they did not make a profit. She asked why the B&O tax is based on gross receipts.

Ms. Hawn explained that there is an exemption for businesses with less than roughly \$140,000 in gross receipts. The exemption level is adjusted annually for inflation, and approximately 75 percent of Bellevue businesses do not pay the B&O tax.

Continuing the presentation, Ms. Hawn reviewed a comparison of electricity, gas, water and wastewater utilities tax rates, noting that Bellevue's rates are favorable in all categories.

Ms. Hawn summarized that staff recommends maintaining the current revenue mix and evaluating potential changes within the context of the budget proposals.

Responding to Councilmember Degginger, Ms. Hawn confirmed that staff is attempting to adjust the expenditure side of the budget at this point.

Mayor Davidson stated that this is a starting point for planning purposes. However, revenue policies will be revisited as the Council reviews budget proposals and expenditures.

Noting the volatility of certain taxes, Councilmember Degginger suggested considering the mix of revenues and reviewing whether they will help achieve the goal of stability.

Mayor Davidson noted that this volatility has worked to the City's advantage in the past, and Mr. Degginger concurred. Mr. Degginger further suggested looking at the mix of revenues not only

from the standpoint of fluctuations in the economy, but also in terms of what this means as an economic signal in the overall community.

Councilmember Wallace said it would be helpful to be able to compare total utility taxes for an average Bellevue household with taxes in neighboring jurisdictions.

Councilmember Chelminiak referred to the existing guiding principle that the revenue policy should provide financial sustainability. He observed that the current policy is not achieving this goal.

Mayor Davidson commented that discussion about the revenue mix and sustainability should keep long-term effectiveness in mind.

Councilmember Degginger agreed that the Council should examine both revenues and expenditures. However, he encouraged that revenue policy be discussed soon in the process in order to provide the opportunity for the community to provide input and feedback. He does not want to wait until the fall to have this discussion.

Mayor Davidson noted the difficulty in discussing both revenues and expenditures, because they are intertwined.

Mr. Sarkozy stated that the budget process is intended to have a number of feedback loops in which the Council reconsiders policies as it gains more information. The next significant component of the budget process will be the programmatic proposals to be presented in July, along with an evaluation of how they compare to available revenues. Mr. Sarkozy suggested that information at that point about which proposals fall below the funding line will be a good time for the Council to address revenues as well as expenditures.

Councilmember Balducci said it would be helpful to know how Bellevue compares to other jurisdictions in terms of the mix of stable and more volatile revenue sources. She stated that this is a separate issue from the task of balancing the budget by adjusting expenditures and/or revenues. Ms. Balducci suggested this would help to best determine the desirable long-term policies, recognizing the effect of the current, significant economic recession.

Mr. Sarkozy stated that Bellevue has lower property tax and utility tax rates than other jurisdictions, and these are the more stable revenue sources. Ms. Balducci reiterated that it would be helpful to know what percentage of other cities' total revenues are comprised of these stable resources.

Councilmember Chelminiak observed that in terms of competitiveness, it is important to consider which cities provide appropriate comparisons for Bellevue. Bellevue is building large buildings while other jurisdictions have different types of development. Some cities rely almost solely on property taxes as a funding source.

Councilmember Wallace said he would like to look at the property tax. He questioned whether the revenue forecast includes the assumption that the property tax remains flat.

Ms. Hawn stated that revenues are added for new construction only. She clarified that the City actually adopts a levy amount, and not a specific property tax rate. In further response to Mr. Wallace, Ms. Hawn said staff's forecast assumes no adjustment to the property tax levy, although a one percent adjustment is allowed by law. Council has the discretion to make this decision, however.

Responding to Councilmember Wallace, Councilmember Chelminiak said that I-1033 capped government expenditures to the inflation level. The allowable annual property tax increase of one percent plus growth is a voter-approved law.

Councilmember Wallace said he would like an analysis of the additional tax revenue that would be generated if Bellevue took the one percent plus growth property tax adjustment, versus the tax revenue that would be generated with only a growth-based adjustment.

Mayor Davidson stated that the Council typically votes on the property tax levy later in the budget process

Councilmember Wallace observed that the property tax levy would have to be adjusted in some way in order to change the revenue mix.

Councilmember Degginger concurred that this is the time to consider different scenarios and their potential impacts for the community. He encouraged addressing this earlier in the budget process than has been done in the past.

Councilmember Chelminiak said there are two issues, long-term financial policies and balancing the budget in the current down economy. He feels it is important to look at the long-term picture now, rather than waiting until the fall. The City is not currently meeting the principle of financial sustainability.

Mr. Sarkozy commented that the Council has asked for information, some of which involve data sources outside of the City. Staff will pull this together and get back to the Council as soon as possible.

Councilmember Degginger stated that there is a tremendous amount of information, both data and policy-related items, in the materials provided to the Council over the weekend.

Ms. Hawn continued the presentation by introducing the reserves policy. Reserves are maintained to address natural catastrophes or counter-cyclical growth, cash flow, future obligations, mandated requirements, and asset replacement. Policy issues include: 1) What are the appropriate reserves targets?, 2) Should some or all of the funds be considered in aggregate for setting targets?, and 3) When should reserves be used, and if used should there be a timeframe for restoring to target levels?

Carla Beauclair, Assistant Budget Manager, reviewed the four types of reserves: 1) Council-directed, adopted by ordinance or resolution (63 percent), 2) Best practices, based on expert opinions and/or practices recommended by professional organizations (17 percent), 3) Actuarially or administrator recommended (63 percent), and 4) Legally restricted/mandated (3 percent). Some reserves overlap categories, but they have been separated based on their primary purpose for this discussion.

Ms. Beauclair recalled that several years ago the Council made a decision to pre-fund some of the LEOFF I (Law Enforcement Officers and Fire Fighters) medical retirement expenses. Bellevue is one of two cities that currently does this. While this is a Council-directed policy, it is placed in the third category based on periodic actuarial analyses about the City's liability in this regard.

Councilmember Chelminiak said Bellevue's total LEOFF 1 Fund is approximately half of the actuarial liability, and most cities fund that in their ongoing budgets.

Mayor Davidson recalled that in the past, the Council decided to place excess revenues into the LEOFF I Fund.

Responding to Deputy Mayor Lee, Ms. Beauclair said the LEOFF I fund is funded every year, and it is used to pay medical costs. In further response, she said the unfunded liability has grown significantly. Mr. Lee expressed concern that reserves might not be adequate.

Ms. Hawn explained that LEOFF I was originally funded with \$20 million, which was thought to be fully funded at the time. However, with the drop in interest rates and increase in medical costs, the unfunded liability has increased.

Responding to Councilmember Chelminiak, Ms. Beauclair said she will provide information about the City's annual contribution to the LEOFF I Fund.

Councilmember Balducci stated that this is an area in which the City may be at a disadvantage because while Bellevue is funding its liability, other jurisdictions are advocating for the State to step in with funding. She feels the City is being prudent in its funding. However, she suggested holding off on fully funding LEOFF I, pending potential future action by the State.

Responding to Councilmember Degginger, Ms. Hawn said staff will provide more detailed information about the Best Practices reserves, and particularly the information technology reserve fund.

Mayor Davidson stated that reserves are somewhat of a hedge against the City's aversion to debt. Mr. Sarkozy concurred, and briefly explained how asset reserves are calculated.

Councilmember Degginger questioned the difference between the information technology operations reserve and the information technology asset replacement reserve. He asked why

large capital software replacement requests have come before the Council, rather than being paid out of the operations reserve. Responding to Mr. Degginger, Ms. Hawn said that funding an example such as providing Windows 7 to all employees is not provided through the CIP budget. As another example, Mr. Sarkozy said the replacement of computers at employees' desks is funded by the asset replacement reserve.

Resuming the presentation, Ms. Hawn reviewed General Fund reserves. She recalled that in 2008, the Council adopted a 15-percent target for the General Fund reserve, and the Rainy Day Fund was combined with this reserve. The reserve is currently at 11 percent of the General Fund. However, all General Fund reserves total 38 percent of the General Fund budget. Ms. Hawn said that Aaa-rated cities of Bellevue's size typically have 20 to 30 percent in General Fund reserves.

Responding to Councilmember Chelminiak, Ms. Hawn said the LEOFF 1 Fund would be part of the General Fund budget if the City decided to switch to a pay-as-you-go basis. In further response, she said that credit ratings are based not only on reserve levels but also on overall debt and the current business environment. Mr. Chelminiak opined that everything should be up for consideration in terms of responding to the need to balance the budget.

Mr. Sarkozy explained that while reserves are not the only criteria for rating agencies, they do look at the ability to repay debt. This has not been a big issue for Bellevue, because it has limited its involvement in debt issuance. However, if the Council chooses to utilize debt on a long-term basis, this would be an important factor in evaluating whether reserve levels are sufficient.

Ms. Hawn said staff recommends maintaining current reserve levels, while also evaluating potential changes within the context of budget proposals and further research regarding possibly aggregating reserves targets.

Ms. Hawn reviewed the CIP policy and posed the following policy questions: 1) What is the optimal split of tax revenues between the operating and capital budgets?, 2) What are the appropriate types of expenditures to be charged to the CIP Plan?, and 3) Should ongoing maintenance costs continue to be funded from a portion of the sales tax dedicated to the CIP Plan, or should the costs be funded from another source?

Ms. Hawn recalled the pie chart showing adopted CIP resources, and noted that Other Resources includes the Parks Levy, in addition to grants and other sources mentioned earlier. She reviewed a comparison of capital funding sources between Bellevue and other cities.

Mr. Bentosino reviewed what the City buys with its CIP budget. Transportation and Parks make up more than 70 percent of the adopted CIP Plan. He reviewed the M&O distribution to the General Fund, which corresponds with the CIP expenditures. The 2009-2015 CIP Plan has \$71.9 million in M&O costs. These are reduced to \$58.3 million through the property tax adjustments in the Supplemental CIP and the Mobility and Infrastructure Initiative plans.

Responding to Councilmember Degginger, Mr. Bentosino said he can provide information since 2003 regarding M&O costs associated with specific CIP projects.

Mr. Bentosino explained that for the new Budget One process, staff is directed to include full cycle costs in their proposals. This includes the cost of capital projects as well as ongoing M&O costs.

Responding to Councilmember Wallace, Mr. Sarkozy said CIP projects have corresponding ongoing M&O funding from the CIP budget. However, there are items in the General Fund that predate this policy.

Responding to Councilmember Robertson, Ms. Hawn said a separate Facilities Fund would cover replacing a broken window at City Hall, as an example. Mr. Bentosino noted, however, that the replacement of a roof at a community center would come from CIP M&O funding. In further response to Ms. Robertson, Mr. Bentosino said refurbishing floors at a community center would be paid from the Facilities Fund, while janitorial services are funded from CIP M&O monies.

Councilmember Balducci observed that this discussion points to key policy issues. As long as M&O funding is provided in the CIP Plan, the amount of money available for capital projects decreases. She suggested looking at different ways of accounting for M&O costs that might provide better control over these costs. In addition, she suggests looking at how these costs are funded and considering whether a dedicated funding source for M&O costs should be designated.

Deputy Mayor Lee said he is not sure about wanting to get into micro-managing the details of project costs and how they are allocated between the capital and operating budgets. However, he sees the value of providing maintenance and operations funding when CIP projects are established. He suggested identifying an approximate percentage for the appropriate M&O funding level. He is more concerned about total M&O costs, and less concerned about whether M&O costs are placed in the CIP budget or the General Fund.

Ms. Hawn continued the CIP policy presentation, describing the increase in debt service into the future related to financing for the new City Hall.

Responding to Mayor Davidson, Ms. Hawn said debt related to the Convention Center is repaid through TOT (Transient Occupancy Tax, aka the Hotel/Motel Tax) collections.

Ms. Hawn reviewed a list of studies funded in the CIP Plan, which is information that was requested by the Council. Studies in the CIP Plan are typically, although not always, linked to the ultimate construction of a project or projects.

Mr. Bentosino reviewed, in response to previous questions from the Council, M&O costs by department as well as the primary drivers of these costs.

Responding to Councilmember Chelminiak, Mr. Bentosino said the street overlay program is funded as an individual CIP project. It is the City's largest ongoing program in the CIP Plan, and is not funded as part of the M&O transfer.

Ms. Hawn recalled that the Council asked staff to identify a potential transition plan for handling M&O budgeting, and she reviewed possible scenarios for this transition.

Councilmember Robertson suggested a longer term transitional approach, perhaps even over a ten-year period, if the Council chooses to make a change.

Responding to Councilmember Wallace, Ms. Hawn clarified that M&O costs are currently reflected in the General Fund and supported by sales tax. As M&O costs have increased over time, the amount of available CIP funding has gone down due to the transfer of CIP funds to the General Fund to cover M&O costs.

Councilmember Balducci observed that this is essentially an issue of transparency in terms of clearly identifying the M&O costs associated with specific projects.

Councilmember Wallace questioned why the City does not permanently assign M&O costs to the operating budget if it would be more transparent to do so.

Mr. Sarkozy said staff and the Council have been struggling with this issue for years. The City has continued with this traditional practice in wanting to be consistent over time. He acknowledged that this approach makes a relatively simple accounting practice more difficult than it needs to be. While the result is fewer dollars available in the CIP for new projects, the City must maintain its current facilities as well.

Councilmember Chelminiak believes it is more than a transparency issue. He noted that residents appreciate that the City maintains its parks and other facilities to a high standard. At the same time, residents question why projects always have to be "gold plated." He suggested that if operating costs can be effectively reduced in certain areas, M&O funding should be returned to the CIP budget. Mr. Chelminiak questioned the need for a dedicated funding source for M&O costs. He reiterated that the issue is about more than an accounting practice, but also about which approach provides an incentive for competing for CIP funds within the budget process.

Deputy Mayor Lee said he appreciates this discussion, as it responds to the Council's concerns for a number of years.

Ms. Hawn completed the CIP policy review by responding to the Council's previous question about the impact of not increasing property tax revenue. This results in the loss over time of \$85 million in bond monies from the CIP Plan.

Mayor Davidson stated that discussion of the debt policy will be postponed to a future date.

(d) Other Fund Financial Forecasts

[Postponed.]

(e) Appendices – Financial Policies

[Postponed.]

At 9:52 p.m., Mayor Davidson declared the meeting adjourned.

Myrna L. Basich, MMC
City Clerk

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