

Memorandum

To: City Council

From: Scott Hugill, Interim City Manager

Date: November 25, 2013

Subject: 2013 Third Quarter Financial Report

Introduction

As part of its fiduciary responsibility to the community, the City Council has chosen to review the City's finances each quarter. These quarterly reviews look at revenues and expenditures of each operating fund, as well as reserve balances and changes in the local and regional economy that have an effect on long-term financial planning.

Reviewing the City's finances on a regular basis, and posting the review on the City's website, highlights two of the City Council's six adopted goals:

- Protect and enhance the City's financial health and stability while maintaining appropriate and essential public services in a cost effective manner.
- Develop and implement more effective communication and outreach with the community.

A presentation at the November 25 City Council meeting will include a look at financial data, as well as performance measures that are tracked on a quarterly basis. This 2013 Third Quarter review looks at the following funds in terms of their performance year-to-date, as well as any unique performance during the quarter itself:

- General Fund
- Debt Service Fund
- Recreation Fund
- Fleet Management Fund
- Capital Improvement Fund
- Street Fund
- Street Construction Fund
- Water Utility Fund
- Wastewater (Sewer) Utility Fund
- Stormwater Utility Fund

Overall, the City's finances remain solidly in line with the adopted Six-Year Financial Forecast by holding expenditures to the limits of revenues, and identifying economic trends early so that the City can adjust accordingly to maintain flexibility.

To provide an idea of all the programs and services in the General Fund, the funds are detailed below in reverse order to whittle down to what the General Fund covers by highlighting other programs first.

Water Utility Fund

The first three funds in this report are the City's utilities (water, wastewater and stormwater) which are referred to as "enterprise funds." Like a business enterprise, these funds cover their own costs from user rates and fees, without financial subsidies from other funds. Under Washington law, utility funds can be used only for utility-related purposes.

The City's utility rates are made up of three components: The first portion of rates is used to cover the cost of operating and maintaining the utility. The second portion of rates goes to pay debt on funds previously borrowed to make repairs and upgrades. The last portion of rates goes towards replacing and upgrading the system.

The Water Utility Fund covers the expense of providing potable water to the community. The City purchases its water wholesale from the Alderwood Water and Wastewater District, which receives the water from the City of Everett.

The Water Utility Fund covers the cost of maintaining, replacing and upgrading 79 miles of water mains, three water reservoirs, 850 hydrants, 2,700 system valves and 5,900 service connections. The Fund is also responsible for administering a cross-connection and backflow prevention program and routine sampling of the water to insure all standards are met.

During a typical third quarter, the Water Utility Fund will see higher revenues than the other quarters of the year as customers use more water for lawns and landscaping during these drier summer months. At the same time, the Fund will typically see higher expenses than the other quarters of the year as the summer months are the height of the construction season when the City is paying contractors to repair and replace portions of the Utility's infrastructure.

Despite a dry summer the City saw lower-than-budgeted water consumption. Revenues in the Water Utility Fund are at 65% of the Revised 2013 Budget as of the end of the third quarter; typically, revenues would be 75% of budget or higher at the end of third quarter.

There are at least two explanations for the lower-than-budgeted water consumption:

- The replacement of virtually all residential water meters over the past two years has eliminated a lot of leaks that were occurring through the older meters; and
- The Ballinger Golf Course used a large amount of water for irrigation of the greens. With the closure of the Course, water consumption has been reduced.

Expenditures, not including debt service payments, total 70% of the Revised 2013 Budget at the end of the third quarter. Water construction projects that will not be completed in 2013 were approved for budget modification carryovers to 2014 at the November 18 City Council meeting.

Wastewater (Sewer) Utility Fund

The Wastewater Utility Fund covers the expense of providing sanitary sewer service to the community. This involves the maintenance, repair, replacement and upgrade of a sewer collection system that includes approximately 70 miles of mains and 30 miles of laterals, four lift stations and 1,400 manholes.

The majority of wastewater treatment services are provided by the Wastewater Treatment Plant in Edmonds, of which Mountlake Terrace is part-owner. Smaller amounts of wastewater flows to King County METRO via Brier and Shoreline.

Although Wastewater Utility Fund revenues are steady throughout the year (rates are typically based on a flat rate derived from a customer's lowest water use of the year), expenses are typically higher in the third quarter than the other quarters of the year due to construction to repair and replace portions of the Utility's infrastructure during the summer months.

As of the end of the third quarter, wastewater service revenues were at 71% of the Revised 2013 Budget. Other wastewater revenues, which include connection fees for new developments, have exceeded the annual budget by almost \$30,000 at the end of the third quarter, due to the new developments in the City.

Wastewater operating expenses, not including debt service payments, total 68% of the Revised 2013 Budget at the end of the third quarter. Wastewater construction projects that will not be completed in 2013 were approved for budget modification carryovers to 2014 at the November 18 City Council meeting.

Stormwater Utility Fund

The Stormwater Utility Fund covers the cost of maintaining the City's natural and developed storm and surface water conveyance system in a manner that protects water quality, enhances habitat, controls flooding, and complies with state and federal regulatory requirements. This includes public education and outreach, inspection of commercial and multifamily housing sites for proper operation and maintenance of stormwater treatment and control facilities, identification of illicit discharges to the storm water system, spill cleanup response for accidental discharges, and a water quality monitoring program for Lake Ballinger. These actions come about under regulatory requirements through the National Pollution Discharge Elimination System (NPDES) Phase II permit issued by the Washington State Department of Ecology.

As with the Wastewater Utility Fund, most revenue to the Stormwater Utility Fund is based on a flat rate, and is therefore steady throughout the year. Also like the Wastewater Utility Fund, the expenses are typically higher because the City is paying contractors to repair and replace portions of the Utility's infrastructure during the summer months.

Stormwater Revenues totaled \$1,179,138 or 68% of the Revised 2013 Budget at the end of the third quarter.

Stormwater expenses, not including debt service payments, totaled 72% of the Revised 2013 Budget at the end of the third quarter.

While Operating Revenues exceeded Operating Expenses by \$164,349 at the end of the third quarter, this gap will decrease by year-end once a debt service payment is made on December 1, with the amount of revenue-to-expenses being closer to the budgeted amount of \$52,699 at the end of the year.

The Town Center Regional Storm Water Facility project, with a budget of \$1,240,000 in 2013, was advertised and opened to bidders in November. The award of the contract for this project will be reviewed at the December 2 City Council meeting. Other storm water projects that will not be completed in 2013 were approved for budget modification carryovers to 2014 at the November 18 council meeting.

Street Construction Fund

The Street Construction Fund covers capital construction projects to provide, preserve, and improve street, pedestrian, bicycle, and traffic control facilities. The ongoing revenue sources for this fund are a portion of the City's allocation of the Motor Vehicle Fuel Tax, traffic impact fees and interest that accrues on funds in the account. Additional funding is provided by state and federal grants and appropriations, loan proceeds, interagency financial participation, and real estate excise tax (REET).

Because these funds are restricted by law to be used only for street **construction**, and not street **maintenance**, they are kept in a fund that is separate from other funds.

The capital projects supported by the fund are those identified in the Transportation Capital Facilities and Improvement Program (TCFIP) and the Transportation Improvement Program (TIP). The typical projects include street pavement overlays and seal coats, sidewalk and sidewalk ramp construction, bicycle route signing and striping, street reconstruction, and traffic control system upgrades and installations.

Revenues in the Street Construction Fund are transferred in on an as-needed basis to cover engineering and construction costs. A typical third quarter in the Street Construction Fund will see higher expenditures than the other quarters of the year, as it is the height of the construction season.

At this time, construction revenues and expenditures are consistent with budgeted programs in the TIP and TCFIP.

Street Operating Fund

The Street Operating Fund covers the maintenance of the City's public right-of-ways, including streets, sidewalks, traffic signals, street lighting and signage. This involves maintenance to more than 60 miles of City streets, 400 City-owned street lights, 15 traffic signals, 3,000 signs, 50 miles of sidewalk, and the maintenance of all crosswalks and other pavement markings.

Vegetation maintenance is another significant responsibility, including the mowing of more than 19 miles of planting strips.

Higher expenditures are incurred during the third quarter, when compared to the other quarters of the year, as more work is completed during the summer months. For example, contract work for restriping roads and crosswalks can only occur during dry weather, and is therefore scheduled for the third quarter.

The 2013 third quarter represents the first quarter in which the County's Road Impact Fee from the Southwest Recycling and Transfer Station (SWRTS) is no longer being paid on a quarterly basis. The quarterly fee was discontinued as of June 30, and replaced with a new agreement that calls for a larger \$200,000 mitigation payment in 2014.

Street Operating Fund revenues are at 70% of the 2013 budget as of the end of third quarter, rather than the typical 75% anticipated at the end of the third quarter. This is due to Motor Vehicle Fuel Tax being only 71% of budget due to less fuel consumption.

Street Operating Fund expenditures through the third quarter represent 65% of the total 2013 budget. Expenditures are less than the anticipated 75% at the end of the third quarter because invoices from Snohomish County for road work projects had not been received nor paid by September 30.

There will be some Street Operating Fund expenditure savings in 2013, but the ending fund balance will be very close to budget at the end of 2013 due to the projected decreased revenue.

Fleet Management Fund

The Fleet Management Fund covers the cost of maintaining, repairing and replacing vehicles and equipment. The Fleet Management Fund receives its revenue from charges to other funds (e.g., charging the Water Utility Fund for maintain maintenance vehicles), as well as charges to the Cities of Brier and Shoreline for maintenance to their vehicles.

Total operating revenues in the Fleet Management Fund through the third quarter are at 65% of the 2013 Revised Budget. These revenues will be closer to 100% of the budget by the end of the year, because Fleet Maintenance overhead costs are not allocated to the user departments until the end of the year after all expenditures are recorded.

The sale of surplus vehicles and other equipment totals \$70,226 through the end of the third quarter, or 76% of the Revised 2013 Budget. In early November (the fourth quarter) additional vehicles and equipment were sold at auction and generated an additional \$28,012 in revenue. As a result, by the end of the year, sales of surplus vehicles and equipment will exceed the annual budget of \$90,000 by over \$8,000.

Expenditures total 72% of the 2013 Revised Budget at the end of the third quarter. The budget to replace equipment in 2013 would have been exceeded by approximately \$70,000 by year-end due to the need to purchase equipment to maintain Ballinger Park, including a large Toro

Mower. However, a budget amendment of \$70,000 to fund these additional purchases was approved by the Council on November 18.

Capital Improvement Project (CIP) Fund

The City defines a “capital” project to be any project or purchase that has a cost of more than \$5,000 and has an estimated useful life of three years or more. The Capital Improvement Project (CIP) Fund covers these capital projects or purchases that are not covered in other funds. Examples of projects covered in the CIP Fund include public safety equipment, recreation and park improvements, and information technology purchases. (Utility and street improvements are not included in the CIP Fund because those capital improvements are covered in other Funds specific to their funding restrictions.)

The CIP Fund is funded in part from the General Fund based on the long-term capital budget needs of the various City departments and the Recreation programs. Revenues also include transfers from the Real Estate Excise Tax (REET) and unreserved Strategic Reserve Funds and investment interest.

With the exception of grant-funded projects or purchases, activity in the CIP Fund has declined over the course of the recession as the City’s limited funds are used for maintaining programs and services rather than replacing capital. That aside, however, the City continues to receive grant dollars for park improvements and expansion, leveraging relatively small amounts of the community’s dollars into larger improvements funded from other sources. One example of this is the Emergency Operations Center (EOC), which is mostly funded by a Federal grant.

Both the revenues from the Grant and the Capital Expenditures budgets were approved to carryover to 2014 with the 2014 Budget Modifications that were approved on November 18.

Recreation Fund

The Recreation Fund covers the revenues and expenditures of the City’s award-winning recreation services, including Aquatics, Athletics/Fitness, Youth and General Recreation Programs. The Fund has a target of recovering 83 percent of its overall cost through user fees; the remaining 17 percent of the cost for recreation programs is funded by the General Fund.

A typical third quarter in the Recreation Fund will see the highest level of revenues and expenditures of the year, as the July-September period reflects the height of activity in terms of pool use, youth camps, and sport leagues.

Total operating revenues through the third quarter are 71% of the Revised 2013 Budget.

- Revenues from Aquatics programs are at 65% of budget, with Recreation swim only at 58% of the 2013 budget. Swim instruction revenues total \$609,475, or over 69% of the total budget.

- Athletic Fitness program revenues are at 82% of the budget as of the end of the third quarter. Most of these revenues are seasonal, such as softball and field rentals.
- Youth program revenues through the third quarter are at 76% of the annual budget. A large portion of these revenues are from summer youth programs.

Total Recreation Operating Expenditures at the end of the third quarter are at 71% of the Revised 2013 Budget, which is consistent with the Operating Revenues.

As of the end of the third quarter, the Recreation Fund has achieved a cost recovery ratio of 88% before debt service costs, and 82% after the cost of debt service, which is just under the budgeted 83% cost recovery percentage.

While the Recreation Fund has ended the third quarter with a balance of \$27,520 (which is \$14,043 over the budgeted ending fund balance). The Fund will end the year close to the budgeted ending fund balance and General Fund subsidy.

Debt Service Fund

The Debt Service Fund accounts for the payment of principal and interest on general long-term debt used to pay for public improvements.

In 2013, two-thirds of the City's Real Estate Excise Tax (REET) revenues are transferred to the Debt Service Fund to pay for the City's debt payments. Additional funding for debt comes from the General Fund and the Recreation Fund.

During this third quarter, the Debt Service Fund saw two changes:

- On October 8, 2013 the City refinanced the Bond Anticipation Note (BAN) that was used to pay the Interim City Hall rent. The budget to pay this debt off over the next seven years is included in the City's Modified 2014 Budget and is also included in the City's Six Year Financial Forecast.
- On October 24, 2013 the City refinanced older debt from 2001 and 2003 resulting in a savings of \$45,000 in 2014. This will reduce the transfer required from the General Fund by \$45,000. in 2014., This is part of the Budget Modifications approved by the City Council on November 18.

The expenditures in the debt service fund are on schedule with the debt service payments due in 2013.

General Fund

After accounting for utility, street, capital, recreation, and debt, the remaining City programs are covered in the General Fund.

General Fund revenues, which can fund virtually anything the City is legally able to do, include:

- Property Tax-General
- Property Tax-EMS
- Sales Tax
- Legislative Backfill
- Utility Tax-Gas
- Utility Tax-Garbage
- Utility Tax/ Franchise-Cable
- Utility Tax-Telephone
- Utility Tax-Electric
- Utility Tax-Water/Sewer/Storm
- Admission Tax-Theatre
- Gambling Tax-Bingo/Pulltab
- Gambling Tax-Mini Casino
- Business Licenses
- Building Permits
- Engineering Fees
- Planning, Zoning, Subdivision Permits
- Animal License
- Liquor Excise Tax
- Liquor Board Profits
- Motor Vehicle Tax Criminal Just.
- Grants
- Payments from Other Governments
- PUD Privilege Tax
- Golf Course Contract
- Emergency Medical Service Transport
- Solid Waste Admin Fee
- Off duty Officers Reimbursement
- Home Detention
- Records Charge
- Passport Filing
- Housing Authority
- Other Charges for Service
- Fines and Forfeitures

In Mountlake Terrace, these revenues are used to pay for the following programs:

- City Council
- City Manager
- Administrative Services
- Community & Economic Development
- Fire (contracted through Fire District 1)
- Municipal Court (Snohomish County)
- Parks & Property Management
- Police

Revenues during a typical third quarter are marked by lower utility tax revenue from electricity and gas utilities, as the warmer months of July-September result in less need for heating homes. Unique to General Fund revenues during the 2013 third quarter was the closure of the Palace Casino on September 30, marking the likelihood the City will be under the \$1,200,000 annual gambling tax revenue forecast at the end of the year.

As of the third quarter of 2013, other General Fund revenues stand as follows:

- Property tax revenue reflects 75% of what the City has levied for collection in 2013. However the actual property tax receipts come primarily in May and November, one month after the April 30 and October 31 tax payment deadlines. The City will have collected 100% of its property tax levies by the end of 2013.
- Sales tax collected through the third quarter have exceeded our projections, coming in at 78% of the budget. This increase in sales tax represents an improvement to the economy, including increases in construction activity within the City. If this trend continues, we are forecasting that sales tax will be over budget by approximately \$100,000 at the end of 2013.

- Utility taxes are slightly under budget, at 71% of the total. We anticipate utility tax revenues to be close to budget by the end of 2013, as the colder weather sets in and gas and electric utility tax revenues increase.
- Gambling tax revenues are at 76% of the budget as of the end of the third quarter. However, as noted above, the closure of the Palace Casino on September 30 is likely to mean the City will be under the \$1,200,000 annual budget at the end of the fourth quarter of 2013.
- Building permit revenues have already exceeded the annual budget by almost \$40,000. Combined with the other development services fees, the revenues are over 80% of the annual budget of \$579,000. This is a reflection of development activity picking up.

All other General Fund Revenues are as projected through third quarter, with total operating revenues at 74% of the 2013 Revised Budget.

Total General Fund Operating Expenditures are under budget, at 72% of the \$14,394,327 2013 Revised Budget.

Overall, we project that the City will end 2013 with an ending fund balance of \$1,352,461, which is \$125,422 over the adopted ending fund balance. This amount represents costs savings achieved in 2013 as well as increased sales tax revenue during the year. These additional dollars are included in the 2014 Modified Beginning Fund Balance Budget in order to pay a portion of the 2014 rent on Interim City Hall.

Conclusion

As has been the norm for Mountlake Terrace over the past several years, the City's third quarter finances highlight two things: (1) the City remains on target financially in providing cost-effective services, programs and projects identified by the Mountlake Terrace community; and (2) the City Council has adhered to a policy of ensuring these programs and projects will be able to be maintained for years to come by living with our financial means.