



BUSINESS OF THE CITY COUNCIL CITY OF MERCER ISLAND

AB 5676
April 7, 2020
Regular Business

AGENDA BILL INFORMATION

TITLE:	AB 5676: Financial Report: 2019 Year-End and COVID-19 Impacts	<input type="checkbox"/> Discussion Only
RECOMMENDED ACTION:	Receive Staff's update, suspend City Council Rules of Procedure 6.3, and adopt Ordinance No. 20-06, amending the 2019 – 2020 Biennial Budget.	<input checked="" type="checkbox"/> Action Needed: <input checked="" type="checkbox"/> Motion <input checked="" type="checkbox"/> Ordinance <input type="checkbox"/> Resolution

DEPARTMENT:	Finance
STAFF:	Matthew Mornick, Interim Finance Director
COUNCIL LIAISON:	n/a
EXHIBITS:	1. Fourth Quarter 2019 Financial Status Report 2. Ordinance No. 20-06
CITY COUNCIL PRIORITY:	n/a

AMOUNT OF EXPENDITURE	\$ 159,094
AMOUNT BUDGETED	\$ Choose an item.
APPROPRIATION REQUIRED	\$ 159,094

SUMMARY

EXECUTIVE SUMMARY

Staff has been working with unflinching commitment and care to analyze the financial impacts to the City's budget as a result of the ongoing coronavirus pandemic. Early indicators signal a recession deeper than 2008, with a potential swift recovery unless economic damage is both severe and long-lasting. Impacts to the City's General Fund and Youth and Family Services (YFS) Fund are severe. Staff has projected revenue impacts through the end of 2020 and is working to address an estimated \$1.5 million General Fund revenue shortfall in the Parks and Recreation department and a \$1.6 million Youth and Family Service Fund revenue shortfall. Below outlines what staff know given the latest information, current critical thinking, and potential next steps for the City.

BACKGROUND

2019 Year in Review

The fourth quarter 2019 Financial Status Update is attached and is meant to inform Council as it enters the FY 2020-2021 Biennial budget process. Since Council's Mid-biennial Budget Review on November 19, 2019 ([AB 5633](#)) – which conveyed how 2019 budget expenditures were tracking through the year – the 2019 year-end assessment confirms budget actuals aligned with budget estimates. The City expended 96 percent of 2019

budgeted expenditures, ending the year with a balanced budget, and a contingency fund balance of \$4.1 million.

Overall, \$32.4 million in General Fund revenues met budget estimates at the end of the fourth quarter of 2019. Information for each revenue source is outlined in detail in Exhibit 1. Total General Fund expenditures of \$31.3 million at year-end were within budget estimates. The General Fund’s 2019 year-end fund balance amounted to \$6.9 million. Setting aside the \$3.9 million portion tied to restricted uses, the remaining \$3.04 million available fund balance is the result of an unappropriated budget surplus over the past three fiscal years.

At year-end all three utility funds were within expected norms for operating revenues and expenditures. Total revenues in the Water, Sewer, and Stormwater utility funds exceeded 2019 budget estimates by 7.2 percent. Expenditures in the utility funds were 38 percent below budget estimates, primarily due to vacant positions filled below cost estimates, savings in repair and maintenance service contracts, and lower than expected utility usage at City facilities. Fund balances at year-end are listed below:

Fund	Balance
Water Utility Fund	\$15.3 million
Sewer Utility Fund	\$6.1 million
Storm Water Utility Fund	\$4.8 million

Though actual revenues for all other City funds came in 5 percent below 2019 budget estimates, expenditures were notably underbudget. Variances are specific to each fund and fall within expected norms, however, in general, incremental progress with professional service contracts and capital project delays speak to expenditure underspending.

2019-2020 BUDGET AMENDING ORDINANCE

The requested budget adjustments to the 2019-2020 adopted budget are included in the attached budget amending ordinance (Exhibit 2). Budget amendments include:

1. Amending the Fleet Fund by \$32,917 for the purchase of the hydraulic driven drop-in sander, previously approved as [AB 5662](#).
2. Amending the Youth and Family Services Fund by \$54,624 to restore the 0.5 FTE Geriatric Specialist for 2020 through a donation from the Youth and Family Services Foundation, previously approved as [AB 5641](#).
3. Amending the Youth and Family Services Fund by \$37,373 by appropriating all of the proceeds from HB 1406 to the Emergency Assistance Program for housing and rent assistance.*
4. Amending the Capital Improvement Fund by \$26,680 to account for a King County Flood Control Grant for the Lincoln Landing project.
5. Amending the General Fund by \$7,500 to account for revenue received from the Washington Health Care Authority.

*The City Council previously authorized allocation of HB 1405 funds to the ARCH Housing Trust Fund (\$16,232) and the remaining balance to the YFS Emergency Assistance Fund ([AB 5655](#)). Given the circumstances facing the Mercer Island community due to the coronavirus pandemic, the City Manager recommends the proceeds from HB 1406 be fully allocated to emergency assistance for housing and rent.

This change will also necessitate the following City Council authorizations:

- Reduction of the ARCH Housing Trust Fund allocation from \$50,000 to \$33,768 for 2020
- Allocation of \$16,232 from the General Fund to the ARCH Administrative Budget for 2020

FISCAL AND ENVIRONMENTAL CONDITIONS IN 2020

Staff has been working with the utmost commitment and care to assess and analyze the financial impacts to the City’s budget as a result of the ongoing coronavirus pandemic. Below outlines what staff know given the latest information, current critical thinking, and potential next steps for the City.

Early indicators signal a recession deeper than 2008, with a caveat the recovery will look different, perhaps V-shaped given the recession is catalyzed by a global pandemic and not necessarily a structural matter. Once measures to stem the coronavirus spread are lifted, staff agree with regional economic forecaster’s prediction of a potentially robust regional recovery. Pent up demand for goods and services will stimulate business activity and a hopeful return to normalcy. However, depending on the length of the pandemic, the recession could lead to a more U- or L-shaped recovery, if economic damage is both severe and long-lasting.

The Governor’s Stay Home, Stay Healthy order was extended to May 4. Car manufacturers announced they will remain closed until at least mid-April. Further guidance from the Governor indicates most construction is non-essential except emergency repairs and those that “further a public purpose.” Police and Community Planning and Development staff worked with residential and commercial businesses to ensure non-essential private construction has ceased on Mercer Island.

All non-essential retail stores in Washington are closed. Revenues at the hotels that remain open are down about 90 percent. Restaurants that choose to remain open only offer takeout service.

On March 28, the Governor released guidance to confirm real estate activities and mortgage lending are essential activities, yet limits in-person meetings, open houses, and the manner in which appraisals and assessments are conducted. On March 31, the Case-Shiller index (a national home price index) indicated year-over-year growth of 5.1 percent, but recent anecdotes suggest significant change. The Multiple Listing Service indicated new listings in the three-county area fell 58 percent two days after the stay home order was issued.

Other indicators showed the impact of the extensive drop in revenues that is now leading to furloughs and unemployment. The 3,300 percent increase in claims in King County the week ending March 21 was followed by a 3,900 percent increase the week ending March 28. The impact has been especially large in accommodation and food service, up 7,150 percent the week of March 28 after a 13,600 percent increase the week prior. With people committed to the Stay Home, Stay Healthy directive, Metro reported ridership is down roughly 70 percent.

Phase three of the federal stimulus program was signed by the President Friday, March 30. The \$2 trillion dollar legislation includes forgivable loans to small businesses (those of 500 employees or less with additional help for those in food service and accommodation), state fiscal aid, additional federal spending, and taxpayer payments relief via extended filing deadlines and additional loss provisions.

Relief Measures for the Mercer Island Business Community

Staff collaborated with the Mercer Island Chamber of Commerce, local business owners, and City Council to coordinate resources, outreach, and City support for small businesses. This work includes:

- Assigning a staff person to oversee coordination with the business community in response to the pandemic.

- Pending Council direction at the April 7 City Council meeting, business and occupation tax deadlines for the first and second quarter of 2020 would be extended to October 31, 2020.
- Dedicating a Let's Talk page to share updates and resources for businesses impacted by the coronavirus pandemic.
- Distributing relief, planning, and other resources from the state, county, and federal government including focused efforts to communicate guidelines and application processes for the US Small Business Administration's (SBA) Economic Injury Disaster Loan and the CARES Act Paycheck Protection Program.
- Developing and deploying marketing for local retailers and eateries. Campaigns include "Take-Out Tuesday" and "Shop Local and Spend Like It Matters" launched by April 1.
- Implementing "Food Priority Pick-up Zones" in Town Center to provide safe and easy access for picking up take-out orders from local restaurants.
- Regularly connecting with business owners to hear concerns/needs and identifying other ways to provide emergency response support via additional outreach assistance or policy development.

In response to the growing concern among residents and local businesses, the City also instituted relief measures for water utility customers. To avoid an undue burden during the coronavirus, the City has a variety of payment plan options for customers in need. Further, the City will not disconnect customers for non-payment during this time, nor will late fees be issued to customers unable to pay their bills on-time.

Budgetary Impacts

Impacts to the City's General Fund and Youth and Family Services (YFS) Fund are severe. Staff has estimated revenue impacts through the end of 2020 and are working to mitigate the following potential losses:

- Up to \$1.5 million General Fund revenue shortfall in the Parks and Recreation department.
- Up to \$1.6 million Youth and Family Service Fund revenue shortfall.

Because the duration of this pandemic is unknown, as well as how long businesses will be closed, several assumptions are guiding impacts to General Fund and YFS Fund revenues. As new information of the pandemic's duration comes to light, staff will better predict the full impact of this emergency. As staff remain responsive to the evolving situation, financial assumptions are as follows:

- Non-essential businesses will be shut down until May 4.
- When businesses re-open, it will take time to return to normalcy.
- We expect very little sales tax to be remitted during March and April given the Stay Home, Stay Healthy order.
- Sales tax revenue is received two months after it is earned. We will not know the true impacts on sales tax until May and June.
- Property tax deadlines have been extended to June 1 for residential and commercial properties who pay property taxes themselves (property taxes paid through mortgage companies will still be required to be remitted on time). It is unknown how many taxpayers pay property taxes themselves in the City, but payment delays will affect the City's cash flows.
- Uncertainty regarding utility customer payments will impact utility revenues and corresponding utility tax revenues.
- Impacts of lost and deferred revenue may create cash flow issues, creating a heavy reliance on General Fund balance and Contingency Fund reserves to meet monthly cash flow commitments.

Lost revenue includes resources lost due to businesses and programming closures. With information to date, the following chart estimates lost revenue through May. March has been calculated as a partial month because systematic closures did not occur until mid-month. This does not include numerous other small revenue sources such as interest earnings, donations, court fines, permits, licenses, etc. The full impacts to March revenue will not be known until the latter part of May.

Projected Lost Revenue	March	April	May
Youth and Family Services			
Counseling Fees	4,051	1,560	3,325
Voice Program	-	50,450	37,500
Thrift Shop	117,500	153,292	171,992
YFS Fund	121,551	205,302	212,817
Parks and Recreation			
MICEC	63,344	66,184	74,728
Recreation Programs	35,681	46,356	38,257
Park and Facility Rentals	14,852	12,748	21,895
Sales Tax			
Construction	36,575	139,273	76,555
Retail & Wholesale Trade	26,913	46,101	41,913
Telecommunications	-	-	-
Finance/Insurance/Real Estate	-	-	-
Professional, Scientific, and Technical Services	-	-	-
Administrative and Support Services	-	-	-
Food Services and Drinking Places	8,046	12,075	9,509
All Other Sectors	-	-	-
General Fund	185,412	322,737	262,857
Total Projected Revenue Losses	306,962	528,039	475,674

Collectively, these lost revenue impacts are immediate and have forced swift and difficult decisions. The City is made up of 195 full-time staff with 54 contract and seasonal staff. By the end of March, the City released 1 full-time employee and 39 seasonal and casual employees in the Parks and Recreation, Youth and Family Services, and Public Works departments. Additional workforce reductions will be needed to offset the loss of revenue.

The Governor’s Stay Home, Stay Healthy order was preceded by the pre-emptive closure of City facilities, including the Mercer Island Community Center (MICEC). Revenues associated with the MICEC as well as field rentals and recreation programs have ceased. Staff assume resulting revenues will not return until August at the earliest, with a slow recovery through the fall and winter season into 2020.

The Thrift Shop is a primary revenue driver for the Youth and Family Services Fund. Monthly revenues vary between \$120,000 - \$220,000 per month, depending on the season. With the Stay Home, Stay Healthy order, the Thrift Shop closed mid-March, requiring immediate use of the Youth and Family Services Fund reserves. In-person Counseling services were also disrupted mid-March. YFS Staff responded swiftly with implementing video-conference counseling for at-risk youth and families. VOICE programming has also been canceled for the year.

General sales tax is collected monthly with a two-month delay. Based on forecasting estimates from City collections in prior years, staff anticipates significant losses in the construction, retail & wholesale trade, and food services sectors through May, slow to recover to former levels through the remainder of the year.

Delayed revenue includes resources the City will likely receive once economic activity has returned to normal. It is unknown when the delayed revenue will be received by the City. With a high rate of unemployment caused by businesses closing, City utilities are waiving late fees and not shutting off utilities to customers until the emergency is over. This follows practices among other utility providers in the region. This could result in utility customers, including businesses, paying their bills out of typical billing cycles, which would result in a delay in receiving utility revenue and utility tax revenue.

As noted above, an extension for property tax payments was granted to June 1 for residential and commercial property owners that pay the tax themselves. Business and occupation tax payments for quarterly tax filers is anticipated to be extended to October 31, pending authorization by the City Council.

Other reasons revenue receipts may be delayed include:

- City permit counter currently closed to new permits, though still processing existing projects' permits
- Potential new businesses are not opening during this pandemic
- Businesses that are granted permission to defer tax payments without penalty

At this moment and still relatively early in the current pandemic, staff is unable to predict when delayed revenue will be received. Staff is preparing for significant cash flow interruptions and will need to rely on the City's contingency reserve and General Fund balance to fill gaps as they arise. If required, the City can take a low-interest loan from a City utility fund to meet monthly financial commitments.

27th Pay Period

The City processes payroll every other week, which translates to 26 payroll cycles each year. About every 10 years there is a 27th pay period. The next is scheduled to occur 12/31/2020. The 27th payroll was not included in the 2019-20 biennial budget. The dollar impact is estimated to be \$700K to the General Fund, further impacting the City's cash flow through 2020.

Steps Forward

Staff is investigating several cost saving measures. While not all of these may come to fruition for a variety of reasons, these include:

- Implementing a hiring freeze for vacant positions through 2020 **(implemented)**.
- Eliminating all professional training and related travel through 2020 **(implemented)**.
- Shutting off utilities to closed city facilities **(implemented – buildings powered down)**.
- Suspending non-essential contracts, particularly in the general fund **(review in progress)**.
- Additional workforce reductions through layoffs, furloughs, salary reductions etc. **(review in progress)**.
- Reduced park maintenance operations (e.g. irrigation, mowing etc.) and operating costs in all City funds **(review in progress)**.
- Identifying potential transfers from the general fund that could be delayed or eliminated **(review in progress)**.
- Tracking federal and state resources to supplement staffing costs to staff providing services deemed non-essential by the Governor's recent order.
- Initiating discussions with labor partners to explore other ways to close the budget gap.

Decisions here forward will have a lasting impact on the City organization and community at large. City leadership, employees, and labor partners recognize the difficult choices ahead. It is clear staff understands

the serious nature of the financial issues facing the City as they remain steadfast in their work to provide essential public services and are working to find pragmatic solutions to the address the financial challenges.

RECOMMENDATION

1. Suspend the City Council Rules of Procedure 6.3, requiring a second reading for an ordinance.
2. Adopt Ordinance No. 20-06, amending the 2019 – 2020 Biennial Budget.
3. Reduce the ARCH Housing Trust Fund allocation from \$50,000 to \$33,768 for 2020
4. Allocate \$16,232 from the General Fund to the ARCH Administrative Budget for 2020