



BUSINESS OF THE CITY COUNCIL CITY OF MERCER ISLAND

AB 7009
October 6, 2026
Regular Business

AGENDA BILL INFORMATION

TITLE:	AB 7009: Introduction to the 2027-2028 Preliminary Biennial Budget and Overview of the 2027-2032 Capital Improvement Program (CIP)	☒ Discussion Only ☐ Action Needed: ☐ Motion ☐ Ordinance ☐ Resolution
RECOMMENDED ACTION:	Receive report and provide initial feedback and questions on the proposed 2027-2032 CIP to inform final development of the biennial budget.	

DEPARTMENT:	Finance Public Works
STAFF:	Jessi Bon, City Manager Matt Mornick, Finance Director Jason Kintner, Chief of Operations
COUNCIL LIAISON:	n/a
EXHIBITS:	1. Preliminary Budget at www.mercerisland.gov/27-28budget
CITY COUNCIL PRIORITY:	4. Focus efforts and actions to be an environmentally and fiscally sustainable, connected, and diverse community.

EXECUTIVE SUMMARY

The purpose of this agenda item is to transmit the 2027-2028 Preliminary Biennial Budget ("Preliminary Budget") and begin the budget review process with the City Council.

- Per Washington State law, the City Manager is required to deliver a balanced Preliminary Budget to the City Council for review and approval. The City Council received the 2027-2028 Preliminary Biennial Budget (Exhibit 1) on September 22, 2026. A copy was filed with the City Clerk and is available [online](#).
- The budget distinguishes between day-to-day operating funds (such as the General, Youth and Family Services, and Development Services Funds) and long-term capital improvement projects. While operating budgets use flexible, unrestricted revenues like property taxes, capital budgets rely almost solely on restricted revenues legally earmarked for specific purposes.
- Across all Funds, the total proposed expenditure budget is \$127 million in 2027 and \$138 million in 2028.
- This phase of the budget review process will focus primarily on the Capital Budget, with a detailed review of the operating budget and two-year work plan scheduled for October 20, 2026. The Capital Budget accounts for the first two years of the City's six-year financial plan that identifies funding for major investments in infrastructure, including facilities, parks, streets, and other public assets (pages E-1 through E-132 of Exhibit 1).
- The proposed 2027-2028 Capital Budget totals \$41.7 million in 2027 (funding 70 projects) and \$48.2 million in 2028 (funding 59 projects). Of the \$89.9 million proposed Capital Budget, less than 1% consists of general government resources from the General Fund. The remaining 99% of capital

funding is legally restricted by state law and local policy (utilizing utility rates, REET, state shared revenues, impact fees, grants, and debt service).

- In February 2026, the City Council reconvened the Finance Ad Hoc Committee to evaluate the potential to change the sequence and scale back capital projects with the goal of redirecting budget resources for facility-related projects. The Committee met twice and helped prioritize limited resources to address immediate capital needs over the next two years but ultimately was unable to identify a substantial sum to reassign to facility projects.
- This is largely due to current economic conditions. Following a year-over-year decline in Real Estate Excise Tax (REET) revenues and the completion of significant outside funding agreements – including the Sound Transit Settlement and ARPA funds – funding available for capital investments is significantly less than prior years.
- Proposed capital investments over the next two years prioritize major upgrades to the City’s sewer conveyance system, a new seismically resilient water supply line, Phase 1 of the Island Crest Way shared-use path, Luther Burbank Park dock and shoreline replacements, Community and Event Center HVAC upgrades, and phased improvements and planning for the new City building at 9655 SE 36th Street (“9655 Building”).
- City Council direction and input on the proposed 2027–2032 CIP is needed to inform development of the final 2027–2028 Biennial Budget.
- The City Council is scheduled to adopt the 2027-2028 Biennial Budget on December 1.

The public is encouraged to provide feedback on the Preliminary Budget and Capital Improvement Program at three scheduled Public Hearings on October 20, November 17, and December 1. Public comment is also invited at all City Council meetings.

BACKGROUND

Every two years, the Mercer Island City Council adopts a financial plan that covers a two-year period, known as a biennium. The City Council received the 2027-2028 Preliminary Biennial Budget (“Preliminary Budget”) on September 22, 2026. A copy was filed with the City Clerk and is available online (Exhibit 1).

The Preliminary Budget is a two-year \$265 million spending plan that supports the broad range of services, programs, initiatives, and capital investments provided by the City. It serves as the primary financial and policy plan, detailing what the City will achieve as outlined in the work plan (pages A-19 through A-24 of Exhibit 1), and how the City will pay for these policy initiatives, operational services, and capital improvements.

To track how these resources are invested, it is important to distinguish between the operating and capital components of the biennial budget. The operating budget establishes what programs and day-to-day operations will be funded in each department within the confines of anticipated municipal revenues. The General Fund (001), Youth and Family Services (YFS) Fund (160), and Development Services Fund (180) finance most of the day-to-day City operations and makeup mostly non-capital related expenses. The City’s enterprise funds for the water, sewer, and stormwater utilities as well as the Street Fund include both operating and capital expenses.

A Capital Budget is the financial plan in the two-year biennial budget that identifies funding for major investments in infrastructure, including facilities, parks, streets, and other public assets. These funds and the capital projects they support are described in detail in Section E of Exhibit 1.

Capital Improvement Program

The City's 2027-2032 Capital Improvement Program (CIP) is the six-year \$182 million financial plan to acquire, expand, or rehabilitate land, technology, buildings, and other major public infrastructure. Although the CIP planning horizon spans six years, funding for the plan is allocated every two years as part of the biennial budget process. When the City Council adopts the 2027-2028 Biennial Budget, they authorize spending in the first two years of the CIP. This authorized spending in 2027 and 2028 makes up the Capital Budget.

The City's operating and capital budgets are separate because they pay for different goods and services, use different resources, and plan for different lengths of time. However, the two budgets are codependent. For example, in September 2025 when the City acquired a new building at 9655 SE 36th Street ("9655 Building") in part with capital budget resources, additional operating budget resources were required to begin operating and maintaining the facility.

This distinction between the operating and capital budgets is further shaped by the legal and policy constraints placed on the City's revenue sources. While the operating budget mostly uses unrestricted revenues – such as property taxes that provide flexibility to fund broad community services – the capital budget relies primarily on restricted revenues that are legally "earmarked" for specific purposes.

Resources Restricted to Capital Funding

The City incorporates a variety of restricted revenues to pay for capital improvements including utility rates, real estate excise taxes (REET), impact fees, state shared revenues, internal service cost allocations, grants, and debt service. The CIP introduction in Section E of Exhibit 1 outlines in detail the City's capital financing strategy and further explains the restrictions placed on these funds.

In the City's recent past, the CIP benefitted from a significant amount of outside funding as well as historically high REET revenues. Following a year-over-year decline in REET revenues and the completion of significant outside funding agreements – including the Sound Transit Settlement and ARPA funds – funding available for capital investments is significantly less than prior years.

2017 Sound Transit Settlement Agreement

In May 2017, the City secured \$10.05 million in mitigation funding from Sound Transit to address East Link light rail impacts and permanent traffic changes on Mercer Island. The funds were allocated via a Settlement Agreement to pre-approved community priorities – including traffic and safety enhancements, transit access, parking improvements, Aubrey Davis Park Master Plan implementation, and specialized light rail emergency services training.

Operating under a strict December 31, 2025 expenditure deadline, the City successfully submitted the final reimbursement invoice to Sound Transit in October 2025, ensuring that all \$10.05 million in mitigation projects – the majority of which supported pedestrian safety, ADA accessibility, and trail connectivity via capital project initiatives – were fully funded by Sound Transit, as detailed in Figure 1.

Figure 1

2017 Sound Transit Settlement Agreement Eligible Uses						
As of December 31, 2025 (\$ in thousands)						
Year	Aubrey Davis Park Planning	Traffic/Safety Enhancements	Emergency Training	Last Mile Solutions	Administrative Overhead	Reimbursement Total
2017	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
2018	-	67	-	-	-	67
2019	-	122	-	33	-	155
2020	-	85	-	1	-	86
2021	-	277	-	-	-	277
2022	-	387	-	-	-	387
2023	50	2,663	23	-	-	2,736
2024	-	1,711	-	189	32	1,932
2025	-	4,320	-	-	90	4,410
TOTAL	\$ 50	\$ 9,632	\$ 23	\$ 223	\$ 122	\$ 10,050

American Rescue Plan Act

The City received \$7.23 million in federal American Rescue Plan Act (ARPA) funds, distributed in two installments in 2021 and 2022.

As summarized in Figure 2, these one-time resources initially stabilized government operations by reopening recreation facilities and restoring maintenance services in parks, public spaces, and rights-of-way during the COVID-19 Pandemic. These funds also provided community relief, funding household utility assistance, local grocery gift cards, emergency support, and youth mental health services in schools.

The City invested the remaining 70% of the City's ARPA funds in critical infrastructure, including City parks, public facilities, and water and sewer systems. Under Council leadership, the City successfully committed and fully expended all funds by December 31, 2024.

Figure 2

Investment of ARPA Funds \$ in thousands	Operating or Capital	2021	2022	2023	2024	Four-Year Total
Pandemic legal Impacts	Operating	\$ 4	\$ 7	\$ -	\$ -	\$ 11
ARPA Program Administration	Operating	-	69	68	74	211
Staffing Support	Operating	-	-	64	114	178
Pandemic Response Supplies	Operating	-	11	2	2	16
Utility Relief Grant Program	Operating	-	33	4	-	37
City Hall Closure Impacts	Capital	-	-	368	1,347	1,715
Facility Planning & Improvements	Capital	-	-	-	1,267	1,267
Parks Maintenance	Capital	122	59	5	5	190
Recreation Restart Initiative	Operating	-	347	-	-	347
Aubrey Davis Park Asphalt Repairs	Capital	-	-	-	35	35
Luther Burbank Sport Courts	Capital	-	-	-	643	643
Bike Skills Park	Capital	-	-	-	303	303
Open Space Improvements	Capital	-	-	-	131	131
Sustainability Initiatives	Capital	-	-	20	119	139
Water and Sewer System Improvements	Capital	-	344	217	110	672
Youth & Family Services	Operating	-	200	522	618	1,341
Total Investment		\$ 126	\$ 1,071	\$ 1,270	\$ 4,768	\$ 7,235

Real Estate Excise Tax (REET) -1 and -2

REET is a 0.5% tax paid by the seller during property transactions. State law restricts its use to street, park, utility, affordable housing, and facility capital investments. Neither REET-1 nor REET-2 may be used for equipment or technology.

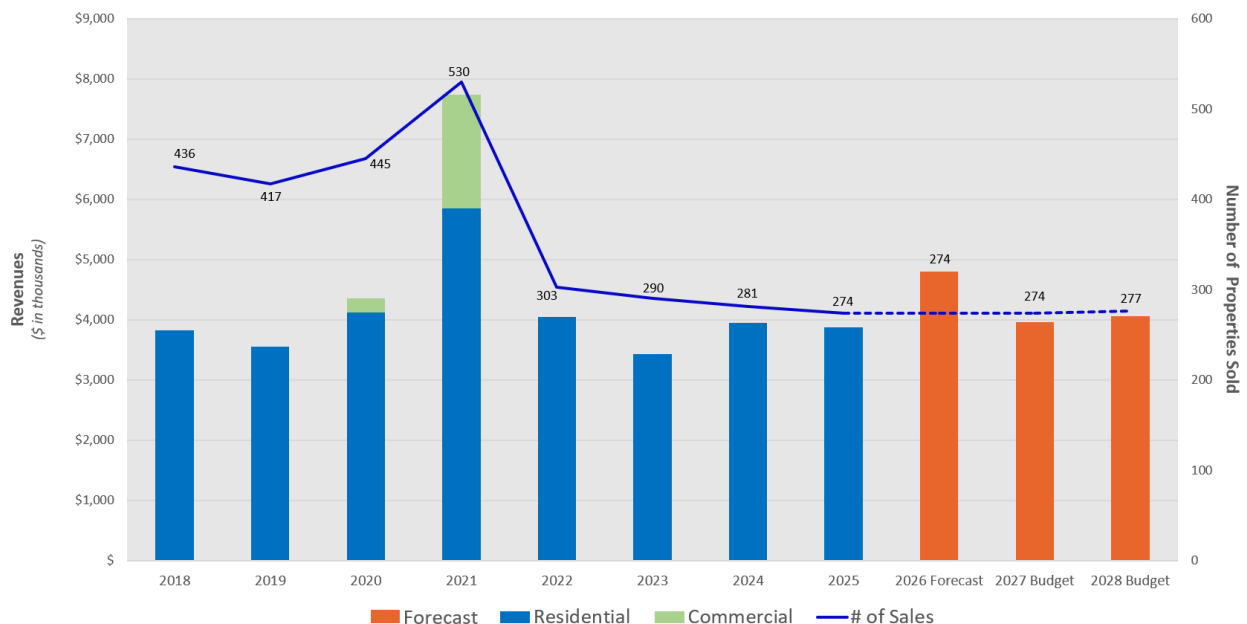
- REET-1 is the first 0.25% tax levied on the property sale price.
- REET-2 is the second 0.25% tax levied on the property sale price.

As the largest source of revenue in the Capital Improvement Fund (320) and Street Fund (110), REET allocations are governed by City Council budget policy as follows:

- All REET-1 revenues are committed to Fund 320 to support parks, open space, public building maintenance projects, and debt service used for the 9655 Building acquisition.
- REET-2 revenues are split, with 10% allocated to Fund 320 and the remaining 90% dedicated to Fund 110 for the construction and maintenance of streets, pedestrian pathways, and bicycle facilities.

Because REET revenue is tied to real estate transaction volumes, it is inherently volatile and fluctuates significantly from year to year. Following a 15-year \$7.7 million peak in 2021, REET revenue experienced a sharp downward swing in 2022, leading to a sustained reduction in revenues that has persisted through the first half of 2026. Figure 3 illustrates the number of property sales each year and the resulting REET revenues from 2018 through 2025, with revenue projections in 2026 – 2028.

Figure 3: Mercer Island Property Sales and Total Revenues
2018-2028



Finance Ad Hoc Committee

The decline in REET revenues and the completion of significant outside funding agreements resulted in a notable reduction of resources restricted to capital investments in streets, parks, open space, and public facilities.

In February 2026, the City Council reconvened the Finance Ad Hoc Committee (“Committee”) that included Mayor Rosenbaum, Councilmember Weiker, and Councilmember Reynolds to evaluate the potential to change the sequence and scale back capital projects with the goal of redirecting budget resources for facility-related projects. From March through August 2026, the Committee met twice and helped prioritize limited resources to address immediate capital needs over the next two years but ultimately was unable to identify a substantial sum to reassign to facility projects.

This is largely due to current economic conditions. Following a year-over-year decline in Real Estate Excise Tax (REET) revenues and the completion of significant outside funding agreements – including the Sound Transit Settlement and ARPA funds – funding available for capital investments is significantly less than prior years. In response, the Committee recommended placing an emphasis on completing active capital projects, keeping critical facilities operational, and competing for outside funding opportunities. Strategies to help balance the City’s primary capital funds from 2027-2032 included:

- **Right-size 2026 resource needs.** Instead of assuming the entire 2026 adopted capital budget would be spent, staff analyzed project schedules to refine actual funding needs through year-end. This approach provided a more accurate beginning fund balance for fiscal year 2027 and identified capital budget savings that could be applied to other capital projects.
- **Sequence and scale back projects.** Because the Capital Improvement Fund (320) is experiencing lower year-over-year revenues than in the recent past, opportunities were pursued to reduce the scope of several projects and strategically sequence work (such as partnering projects with similar areas of work, planning utility work with ROW or park capital projects, etc.). Budget detail for Fund 320 revenues and expenditures are included on pages B-16 and B-17 of Exhibit 1.
- **Work within restricted revenues.** Proposed funding for projects in 2027 and 2028 is tied to resources that are legally restricted for specific uses. For example, while the City budgeted over \$1.1 million for forest and open space investments in 2026 (90.25.0001, 90.25.0006, 90.25.0034), the 2022 Parks Levy only generated \$300,000 for that purpose. REET revenues made up the remaining funding. With reduced resources compared to prior years, open space vegetation management work in 2027-2028 emphasizes continued restoration in existing open spaces rather than expanding this work in new open space areas.
- **Maintain reserves.** Fund 320 and 110 hold several statutorily restricted revenues and baseline funding targets required for stable, ongoing operations. Capital projects are sequenced to ensure reserve targets are met and maintained by the end of 2028 and beyond.

ISSUE/DISCUSSION

Capital Budget

Capital project priorities in the next two years include completing active capital projects, keeping critical facilities operational, and competing for outside funding opportunities.

The capital budget proposes funding for 70 projects in 2027 and 59 projects in 2028, totaling \$89.9 million in capital investments. The proposed capital projects include investments in public facilities, technology, equipment, streets, transportation, parks, and utilities. Figure 4 outlines the total number of projects funded and the corresponding proposed budget by fiscal year, by capital asset category.

Figure 4

Capital Asset Category <i>\$ in millions</i>	Funded Projects (proposed)		Proposed Budget		Total
	2027	2028	2027	2028	
Public Facilities	5	4	\$ 4.3	\$ 3.8	\$ 8.1
Technology	6	6	0.7	0.3	1.1
Equipment	3	3	1.9	1.3	3.2
Streets, Pedestrians, & Bicycle Facilities	12	7	5.6	1.5	7.1
Parks, Recreation, and Open Space	7	7	1.4	2.3	3.6
Sewer Utility	10	8	4.8	22.5	27.3
Stormwater Utility	11	10	2.4	2.5	4.8
Water Utility	16	14	20.7	14.0	34.7
Total	70	59	\$ 41.7	\$ 48.2	\$ 89.9

Outside of routine capital investments, emphasis over the next two years in the Capital Budget includes:

1. Finishing a decade-long waterfront project at Luther Burbank Park that replaces aging docks, improves shoreline habitat, and improves public ADA access along Lake Washington (90.25.0020 in 2026).
2. Replacing and modernizing the antiquated HVAC system (20+ years old) at the City's heavily used Community and Event Center to meet current industry standards (90.05.0002) and address system performance problems.
3. Developing a phased approach that supports near-term occupancy of the 9655 Building while planning for a more comprehensive renovation as future funding becomes available (90.05.0021).
4. Carrying out Phase 1 of the Island Crest Way shared use path (90.20.0040) as well as enhancing pedestrian and ADA improvements along the street corridor following the construction of the new water supply line (90.20.0006 and 90.20.0009).
5. Beginning a multiyear initiative to make once-in-a-generation upgrades to the City's sewer conveyance system including the completion of a comprehensive hydraulic model, upgrading antiquated pump stations and beginning design and permitting for the construction of Lakeline Reach 1 capacity improvements.
6. Completing critical upgrades to the water distribution system including a new locally controlled and seismically resilient water supply line (90.40.0032).
7. Update the Parks, Recreation, and Open Space (PROs) Plan (90.25.0034), Water System Plan (90.40.0035), General Sewer Plan (90.30.0013), and develop Stormwater System Plan (90.35.0022) to guide future capital investments.

Consistent with the City's financial management policies, CIP funding over the next two years relies on existing, available fund balances, projected revenues from real estate excise taxes, state shared revenues, outside debt, and utility rates, along with the prudent use of outside funding including state and federal grants. The General Fund is the sole source for capital investments in technology and equipment.

Of the \$89.9 million proposed CIP, less than 1% makes up general government resources. The remaining 99% of resources that pay for infrastructure improvements are restricted with enforceable limitations as mandated by state law and local policy set by the City Council.

NEXT STEPS

City Council direction and input on the proposed 2027–2032 CIP is needed to inform development of the final 2027–2028 Biennial Budget.

The remaining preliminary budget schedule is summarized below.

Date	Topic
October 20, 2026	Public Hearing: Overview of the 2027-2028 Work Plan and Operating Budget
November 17, 2026	Public Hearing: 2027-2028 Biennial Budget Review, Receive Q3 2026 Financial Status Update and Budget Amending Ordinance, Adopt 2027 Property Tax Ordinances, and Adopt 2027 NORCOM Budget
December 1, 2026	Public Hearing: 2027-2028 Biennial Budget Adoption

The public is encouraged to provide feedback on the 2027-2028 Preliminary Biennial Budget and 2027-2032 CIP at three scheduled Public Hearings on October 20, November 17, and December 1. Public comment is also invited at all City Council meetings.

RECOMMENDED ACTION

Receive the 2027-2028 Preliminary Biennial Budget available at www.mercerisland.gov/27-28budget and provide feedback on the 2027-2032 CIP (see pages E-1 to E-132). No additional action required.