



**BUSINESS OF THE CITY COUNCIL  
CITY OF MERCER ISLAND**

**AB 6251  
April 25, 2023  
Regular Business**

**AGENDA BILL INFORMATION**

<b>TITLE:</b>	AB 6251: Financial Status Update: FY 2022 Year-End and Budget Amending Ordinance	<input type="checkbox"/> Discussion Only <input checked="" type="checkbox"/> Action Needed: <input type="checkbox"/> Motion <input checked="" type="checkbox"/> Ordinance <input type="checkbox"/> Resolution
<b>RECOMMENDED ACTION:</b>	Receive the fiscal year 2022 Year-end Financial Status Update and adopt Ordinance No. 23-05, amending the 2023-2024 Biennial Budget.	

<b>DEPARTMENT:</b>	Finance
<b>STAFF:</b>	Matt Mornick, Finance Director LaJuan Tuttle, Deputy Finance Director Ben Schumacher, Financial Analyst
<b>COUNCIL LIAISON:</b>	n/a
<b>EXHIBITS:</b>	1. Financial Status Update – FY 2022 Year-End – Updated 4/18/2023 2. Ordinance No. 23-05 2023-2024 Budget Amendments
<b>CITY COUNCIL PRIORITY:</b>	4. Focus efforts and actions to be an environmentally and fiscally sustainable, connected, and diverse community.

**EXECUTIVE SUMMARY**

This agenda bill summarizes the City’s financial position at the end of fiscal year (FY) 2022.

- Detailed analysis across all Funds is provided in the FY 2022 Year-End Financial Status Update (Exhibit 1). This includes revenue actuals, expenditure actuals, and budget amendments adopted by the City Council from January 1 through December 31, 2022.
- At the end of FY 2022, the fund balance in the City’s General Fund is \$12.7 M. Of this amount, \$11.2 M is committed due to prior City Council actions, including restricted uses and appropriations based on established financial policies.
- The remaining surplus of \$1.5 M represents the available unassigned Fund Balance in the General Fund. This surplus is the result of better than anticipated general sales tax revenues and savings from departmental budgets.
- Ordinance No. 23-05 (Exhibit 2) outlines staff’s recommendations to amend the 2023-2024 Biennial Budget across all Funds based on the continuation of work from the prior biennium which is not yet complete.

**ISSUE/DISCUSSION**

*Financial Status Update: FY 2022 Year in Review*

During the biennial budget workshops this past fall, the City Council received a revenue forecast ([AB 6145](#)) as well as the third quarter Financial Status Update for FY 2022 ([AB 6185](#)). At the time, General Fund expenditures and revenues were tracking within budget expectations. However, crosscurrents in the regional

economy indicated new economic pressures. Inflation for the first half of FY 2022 jumped to 8.6% (CPI-W for Seattle-Tacoma-Bellevue), a significant increase when compared to 3.3% for the same period the year prior.

Historically, inflationary pressures of this magnitude, when coupled with high unemployment, indicate a looming recession. However, during this period the unemployment rate in King County was markedly low at 2.7%.

To control inflation, the Federal Reserve pursued increases in the federal funds target rates throughout 2022 and into 2023. Changes in the federal funds target rates are the Federal Reserve’s primary tool to implement monetary policy. Increases to the federal funds target rates, by design, are intended to slow the economy.

On this basis, staff anticipated the slowing of growth with a gradual return to growth rates akin to pre-pandemic levels. This slowdown occurred among certain City revenues such as real estate excise tax (REET), but not among others such as general sales tax revenues, interest earnings, and license, permit, and zoning fee revenues.

General Fund Balance

The Fund Balance in the General Fund at the end of FY 2022 is \$12.7 M. Of this, \$11.2 M is reserved based on prior City Council actions.

The remaining \$1.5 M unassigned fund balance represents the year-end surplus in the General Fund. This surplus is due to better than anticipated general sales tax revenues and savings from department expenditure budgets.

<b>GENERAL FUND (\$ in thousands)</b>		<b>AMOUNT</b>
<b>RESERVED</b>		
<b>NON-SPENDABLE</b>		
Petty cash		\$2
Inventory of supplies		121
<b>RESTRICTED</b>		
Law enforcement restricted		82
DSG technology fee reserve		46
Customer deposits		42
Deferred development fee revenue		554
Permit fee revenue surplus		303
<b>COMMITTED</b>		
LEOFF I long-term care reserve		2,335
Compensated absences reserve		751
WSDOT lease deposit		742
Emerging Innovations Reserve		0
Unearned recreation revenue		175
<b>ASSIGNED</b>		
Sound Transit December 2022 settlement		2,100
Expenditure carryovers to 2023 budget		75
Budgeted fund balance-2023-2024 budget		3,881
Expenditure control budgeting reserve		16
<b>RESERVED SUBTOTAL</b>		<b>\$11,222</b>
<b>UNASSIGNED - AVAILABLE BALANCE</b>		<b>\$1,523</b>
<b>TOTAL FUND BALANCE</b>		<b>\$12,746</b>

General Fund Revenues

Most of the City’s revenues performed as expected. Revenues associated with general sales tax, licensing, permit and zoning fees, and interest earnings exceeded budget expectations. At the same time, Municipal Court and Parks and Recreation revenues underperformed budget expectations (see Exhibit 1).

At year-end, the City received \$6.6 M in general sales tax revenues, exceeding the budget expectations by over \$1.5 M. Given inflationary pressures are largely passed onto consumers through price increases, staff

anticipated a marginal increase in sales tax revenues followed by restrained consumer spending because of the federal fund rate increases. Data through year-end indicates no such shift in consumer spending occurred.

From July through December, the City generated \$3.1 M in general sales tax, roughly \$300,000 more than the same period in 2021. All business sectors surpassed FY 2021 revenue totals.

License, permit, and zoning fees outperformed budget expectations, largely due to improved administration of development services, an updated fee schedule, and deferred revenues collections on a handful of commercial and residential projects earlier in the year. Unspent revenues tied to development service fees amounted to just over \$300,000 in FY 2022. This surplus is restricted fund balance in the General Fund set aside strictly for permit-related service provision.

**General Fund Expenditures**

At the end of FY 2022, General Fund expenditures were \$1.6 M underbudget. Of this amount, over \$1.1 M is salary and benefit savings due to vacancies and staff turnover throughout the year. Filling vacancies was difficult in 2022 and many positions were vacant for several months before they were filled, resulting in higher than anticipated budget savings. In addition, contractual services were underspent by \$0.6 M, which was primarily due to underspending on professional services related to collective bargaining, Human Resources legal support, and a delayed start to the financial management software implementation project.

<b>GENERAL FUND EXPENDITURES</b> <i>(\$ in millions)</i>	<b>FY 2022</b> <b>AMENDED</b> <b>BUDGET</b>	<b>% of TOTAL</b> <b>AMENDED</b> <b>BUDGET</b>	<b>FY 2021</b> <b>YEAR-END</b> <b>ACTUALS</b>	<b>FY 2022</b> <b>YEAR-END</b> <b>ACTUALS</b>	<b>FY 2022</b> <b>BUDGET V</b> <b>ACTUALS</b>
Salaries & Benefits	23.90	67%	21.08	22.79	1.11
Supplies	0.99	3%	0.63	0.93	0.06
Contract Services	3.95	11%	3.69	3.37	0.57
Other Services & Charges	5.58	16%	5.24	5.74	-0.16
Interfund Transfers Out	1.05	3%	0.74	1.06	-0.01
<b>TOTAL EXPENDITURES</b>	<b>\$35.47</b>	<b>100%</b>	<b>\$31.38</b>	<b>\$33.90</b>	<b>\$1.57</b>

**Other Fund Revenues**

Real Estate Excise Tax (REET) is the primary revenue source for both the Steet Fund and Capital Improvement Fund. It is currently split into two revenue streams – REET-1 and REET-2 – each with restricted uses per State law.

Total REET revenues for 2022 were \$4.04 million, on par with budget expectations. REET revenues experienced a notable slowdown in the latter part of FY 2022. The lower-than-expected returns can be attributed to a historically low number of property sales in the last four months of 2022 when compared to prior years. There were 227 less home sales recorded in 2022 compared to 2021.

FY 2022 Carryforward Requests

Budget carryforwards relate to uncompleted projects, programs, contracts, or purchases that were authorized during the 2021-2022 biennial budget, but not spent by December 2022. Within a biennium, the funding and the expenditure authority are automatically “carried forward” to the second year of the budget. Between biennium, staff presents carryforward requests to the City Council for review and approval, as outlined in Exhibit 2. These include resources such as cash and grants that were obligated, but unspent in the previous budget period.

GENERAL FUND	AMOUNT
(\$ in thousands)	
<b>Operating Carry-Forwards</b>	
Court Audio-Visual Grant	\$42
Comprehensive Plan	\$67
BLS Core Services	\$4
MIH Start-up Funding	\$212
Port of Seattle Grant	\$45
MI Chamber of Commerce	\$7
Climate Action	\$63
<b>TOTAL</b>	<b>\$440</b>

A list of the operating carry-forward requests is included in the table above, totaling \$440,209 in the General Fund. An additional \$14.4 M across other Funds is recommended to carryforward into FY 2023, for a total of \$14.9 M in carryforward needs (see Exhibit 2).

Disposition of Fund Balance & the April 25 Planning Session

Adequate fund balance is a key element of the City's financial management policies. In times when prudent management yields year-end savings, the City’s financial policies (see Resolution No. [1602](#)) provide guidance on how to strategically use Fund balances. Examples include replenishing operating reserves to target levels, buffering against economic pressures such as the current pace of inflation, investing in one-time work items, or addressing long-term risks such as a correction to the real estate market activity. The \$1.5 M General Fund year-end surplus represents one-time savings in-line with recent prior year-end financial outcomes.

During the City Council planning session on April 25, 2023, staff will review policies related to the disposition of year-end savings, outline economic challenges in the near-term, and present the list of deferred budget proposals from the October 18, 2022 Biennial Budget workshop (see [AB 6169](#)).

**RECOMMENDED ACTION**

Adopt Ordinance No. 23-05, amending the 2023-2024 Biennial Budget.