BUSINESS OF THE CITY COUNCIL
CITY OF MERCER ISLAND

AB 6997
September 15, 2026
Regular Business

AGENDA BILL INFORMATION

TITLE:	AB 6997: 2027-2028 Preliminary Biennial Budget Financial Forecast and Budget Amending Ordinance	☐ Discussion Only ☒ Action Needed: ☐ Motion ☒ Ordinance ☐ Resolution
RECOMMENDED ACTION:	Adopt Ordinance No. 26-08, amending the 2025-2026 Biennial Budget.	

DEPARTMENT:	Finance
STAFF:	Matthew Mornick, Finance Director LaJuan Tuttle, Deputy Finance Director Ben Schumacher, Financial Analyst II
COUNCIL LIAISON:	n/a
EXHIBITS:	1. 2027-2028 Preliminary Biennial Budget Financial Forecast 2. Budget Amending Ordinance No. 26-08
CITY COUNCIL PRIORITY:	4. Focus efforts and actions to be an environmentally and fiscally sustainable, connected, and diverse community.

AMOUNT OF EXPENDITURE	$ n/a
AMOUNT BUDGETED	$ n/a
APPROPRIATION REQUIRED	$ n/a

EXECUTIVE SUMMARY

This agenda item provides an updated financial forecast for the City's primary operating funds – the General Fund and Youth and Family Services (YFS) Fund – and the Capital Improvement and Contingency Funds from Q2 2026 through 2032 (Exhibit 1).

- Each year, an updated revenue forecast is presented to the City Council to establish baseline revenues to inform City Council policy decisions for the next two years and beyond.
- Although financial projections extend through 2032, revenue estimates for 2027 and 2028 establish spending limits for the 2027–2028 Preliminary Biennial Budget, scheduled for City Council and community review later this month.
- As projected in May 2025 (AB 6680), the City will enter a period of deficit spending in its primary operating funds in 2027. Expenditures in the General and YFS Funds are projected to outpace revenues in both 2027 and 2028. While prior-year savings are proposed to temporarily bridge operations through the upcoming biennium, a permanent funding solution will be required by 2028 to maintain current municipal service levels.
- This financial forecast coincides with a broader regional slowdown and growing state budget pressures. According to the Washington State Economic and Revenue Forecast Council June 2026 Forecast, statewide economic growth has moderated. Slow job creation statewide, low personal

income growth, and persistent inflation have reduced revenue estimates in the 2025-2027 state budget.
- Regional data from the King County Office of Economic and Financial Analysis July 2026 economic and revenue forecast reflects similar headwinds, marked by rising inflation and slow real estate activity.
- Local real estate excise tax (REET) collections remain low in Mercer Island and the neighboring region following a prolonged period of high interest rates and relatively low property transactions.
- To help balance competing priorities, safeguard the City's long-term financial position, and guide strategic investments for Mercer Island, the 2027-2028 Preliminary Biennial Budget Financial Forecast ("forecast") provides the City Council with an up-to-date outlook of the City's long-term financial position (Exhibit 1). Staff will release the 2027-2028 Preliminary Biennial Budget later this month.
- Although the General Fund remains balanced through 2026, the forecast projects a $700,000 deficit in 2027 and a $1.7 million deficit in 2028. Maintaining current service levels will require drawing down the unassigned fund balance in the General Fund – from $5.1 million at year-end 2025 to $2.3 million by 2028.
- Outside of Thrift Shop revenues and funding from the Mercer Island Youth and Family Service (MIYFS) Foundation, the YFS Fund relies on operating fund balance and the General Fund. With the YFS operating fund balance anticipated to be fully exhausted in 2028, the General Fund annual contribution is proposed to steadily increase from $350,000 in 2026 to $1.07 million in 2028. Utilizing one-time General Fund unassigned fund balance maintains service levels in 2027-2028 while the City Council evaluates long-term funding options.
- Following a 15-year $7.7 million peak in 2021, the Capital Improvement Fund's primary revenue – Real Estate Excise Tax (REET) revenues – experienced a sharp downward swing in 2022, leading to a sustained reduction in resources for streets, parks, open space, and facilities that has persisted through the second quarter of 2026. The City Council reconvened the Finance Ad Hoc Committee (AB 6856) in February 2026 to assess the competing needs between parks, open space, and facilities funded by the Capital Improvement Fund and prioritize limited resources for critical project work in 2027 and 2028. More information will be shared on the capital fund recommendations later this year.
- Ordinance No. 26-08 (Exhibit 2) formalizes all previously approved City Council adjustments to the 2025-2026 Biennial Budget made through September 1, 2026.

BACKGROUND

The past six years mark one of the most uncharacteristic periods in the City's financial history. During the onset of the COVID-19 pandemic, the City instituted immediate cost-saving measures to stabilize government operations. Facing significant economic uncertainty in 2021, the City Council unanimously adopted new financial management policies to establish clear direction for the prudent use of finite public resources, with a shared focus on the City's long-term financial goals.

These policies successfully guided the City out of the pandemic, reshaped municipal operations, and resulted in many accomplishments; a few are summarized below:

- **Voter-Approved Investments:** Voters approved a Parks Levy lid lift in 2022 to fund ongoing playground replacements, park maintenance, Luther Burbank Park maintenance, and open space management.
- **Infrastructure Upgrades:** The City Council directed use of one-time federal funding (e.g., American Rescue Plan Act) towards completing major capital investments across City streets and parks, while advancing once-in-a-generation upgrades to critical underground utilities.

- **Modernized Technology:** Replaced antiquated software with streamlined, modern financial and human resource systems.
- **Resilient Drinking Water Access**: Replaced aging infrastructure in the water distribution system while advancing a new locally controlled seismically resilient water supply line for the island.
- **Luther Burbank Waterfront Improvements**: Moving construction forward on a massive multiyear project to replace aging docks, improve shoreline habitat, and improve public ADA access along Lake Washington.

The City Council also set aside year-over-year savings in the Municipal Facility Replacement Fund – a dedicated reserve created following the closure of City Hall. By September 2025, these savings enabled the strategic purchase of a 22,000 square-foot office building at 9655 SE 36th Street, adjacent to the City Hall campus. The new facility will provide workspace for City staff and will improve community access to services. Planning work is underway on the necessary retrofits for the facility.

Throughout this period fiscal pressures remained. As part of the 2025-2026 biennial budget process, staff presented an early long-term financial outlook (AB 6680) alerting the City Council to emerging structural challenges with the City's financial position. Driven by persistent inflation, rising labor and operational costs, and limited growth in the City's tax revenues, annual operating expenditures were projected to outpace revenues in 2027.

ISSUE/DISCUSSION

FINANCIAL FORECAST

The 2027-2028 Preliminary Biennial Budget Financial Forecast presents the City's projected financial position through 2032 (Exhibit 1).

Within the General Fund, revenues are projected to increase by 4.4% annually between 2026 and 2028, whereas baseline expenditures are projected to increase 6.1% annually over the same timeframe. While the General Fund is structurally sound through 2026, an operating deficit emerges in 2027 and widens in 2028.

The General Fund's unassigned fund balance – estimated at $4.8 million at year-end 2026 – is proposed to bridge operations across the 2027–2028 biennium. By the end of 2028, the unassigned fund balance is projected to be $2.3 million in the General Fund.

A similar structural deficit is projected in the YFS Fund. The forecast for the YFS Fund projects a $915,000 operating deficit in 2027 that grows to $1.13 million in 2028. To stabilize youth and family services programs through the upcoming biennium, the forecast assumes the operating fund balance for the YFS fund will bridge operations until fully spent in next two years. This requires an increased annual interfund contribution from the General Fund, rising from $350,000 in 2026 to $477,000 in 2027, and growing to $1.07 million in 2028.

Meanwhile, the Capital Improvement Fund has struggled with competing infrastructure demands when Real Estate Excise Tax (REET) revenues – the City's primary resource for capital improvements – remains sluggish due the passive real estate market. To balance the Capital Improvement Fund, investments in 2027 and 2028 have been sequenced and scaled back to focus on active priority projects, essential facility maintenance, and grant-matched initiatives.

Although financial projections extend through 2032, projections establish baseline spending limits for the 2027–2028 Preliminary Biennial Budget, scheduled for City Council and community review later this month. To that end, the financial forecast lays the foundation for the next biennial budget. It provides the City Council with the information needed to make policy decisions and establish budget priorities for 2027 and 2028.

ORDINANCE NO. 26-08

In addition to beginning the policy discussion on the 2027-2028 Preliminary Biennial Budget, Exhibit 2 outlines budget adjustments approved by the City Council and the resulting financial impacts. Budget amending ordinances are presented quarterly to account for adjustments throughout the year. Many of the adjustments in Exhibit 2 tie to recent City Council decisions at the September 1, 2026 Council meeting.

NEXT STEPS

At the end of September, the City Council will receive the 2027-2028 Preliminary Biennial Budget. October kicks off the budget workshops where the City Council will review the capital budget, two-year work plan, and operating budgets. The preliminary budget development schedule is summarized below.

Date	Topic
October 6, 2026	Introduction to the Preliminary Budget and Overview of the Six-Year Capital Improvement Program
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 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.

Looking ahead, the City Council will establish the 2027–2028 work plan as part of the adoption of the biennial budget. That work plan will include a focused effort to evaluate and develop long-term strategies to address the City's ongoing structural deficit and strengthen the City's financial position. This work will provide the Council with the information and options necessary to make thoughtful, deliberate decisions about how best to align available resources with community priorities and service expectations over the long term.

RECOMMENDED ACTION

Adopt Ordinance No. 26-08, amending the 2025-2026 Biennial Budget.