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## 2014 BUDGET OVERVIEW

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This budget section is preceded by the Mayor's Message, which is delivered to the City Council at the first budget hearing. The Mayor's Message is intended to be read in concert with this overview section.

### **2014 Financial Overview**

#### **Total City**

The City's Operating Budget is comprised of 57 separate funds, each with a unique purpose. The budget funds day-to-day expenditures for a variety of services. Among these are police and fire protection, water and sewer services, transit, street maintenance, parks and the library, debt service, and support services. These basic services are funded by user fees, taxes, permits, grants, state-shared revenues and other charges. The budget can vary greatly from year to year depending on construction projects and equipment replacement schedules. As summarized below, the total City expenditure budget increased by \$4.7 million between 2013 and 2014.

<b><u>Expenditure Budget</u></b>	<b><u>Adopted 2013</u></b>	<b><u>Adopted 2014</u></b>	<b><u>% Increase (Decrease)</u></b>
General Government	\$ 111,699,407	\$ 113,196,643	1.3%
Special Revenue Funds	31,888,217	24,719,293	-22.5%
Debt Service	2,239,000	1,975,708	-11.8%
Enterprise Funds	161,144,356	170,150,913	5.6%
Internal Service Funds	29,382,283	30,414,899	3.5%
Police & Fire Pension Funds	<u>5,350,654</u>	<u>5,908,398</u>	<u>10.4%</u>
Total Expenditure Budget	\$ 341,703,917	\$ 346,365,854	1.4%

The total City revenue budget increased \$22.8 million, excluding beginning fund balances, from \$311.8 million in 2013 to \$334.6 million in 2014. The City's ending fund balance budgets decreased by \$1.0 million from \$157.2 million in 2013 to \$156.2 million in 2014.

Additional information on the revenue, expenditure, and fund balance changes for various funds can be found in the Financial Summary section of the budget.

#### **General Government**

The City's Five-Year Outlook financial model functions as a key tool in the general government budget development process. As the budget develops, all changes are processed through the Outlook to forecast the five-year impacts. The City maintains a fund balance policy that limits operating expenses to operating revenues and targets the General Government Fund balance at 20% of operating revenues.

At the beginning of the budget process, the model projected a \$10.4 million operating deficit for 2014. Subsequent revisions to the revenue forecast and expenditure budget eliminated the projected deficit, bringing 2014 operating expenditures in line with operating revenues.

The primary guidelines used for the annual budget development were as follows:

- Adhere to sound fiscal management practices
- No new programs without new offsetting revenue or an equal reduction elsewhere in the budget
- Maintain, to the extent possible, the current level of public services

These guidelines carried forward from 2013 as the City confronted yet another unusually challenging budget year. The chief constraints facing the City budget for the year 2014 included:

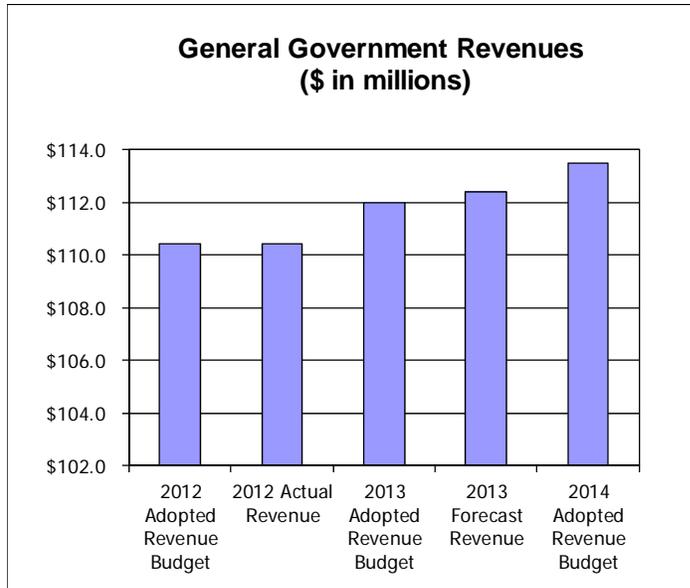
- Significant reduction in utility tax and state shared revenues
- Limit on property tax revenue growth to 1% on the base, plus adjustments for new construction and annexations
- Higher employee health care and PERS/LEOFF retirement funding costs
- Additional costs related to the Affordable Care Act

Major changes to balance the 2014 budget are listed below.

<b>2014 Budget Balancing</b>	
2014 Estimated Annual Deficit as of 12/01/12	\$ (10,431,851)
<b>BUDGET CHANGES:</b>	
Revenue adjustments:	
B&O tax	(316,140)
Sales tax	614,749
Utility taxes (natural gas, telephone, electric, cable)	(750,885)
State shared revenue	(164,435)
Net all other revenues	(4,077)
Labor adjustments:	
Adjust for CPI impact on COLAs	977,310
Benefit adjustments (medical, dental, vision, retirement)	(129,935)
Eliminate 9 vacant positions	734,527
Increase vacancies held open	560,769
Estimate for Affordable Care Act	(160,000)
Other adjustments (position changes, step increases)	(157,358)
Expenditure adjustments:	
Reduce utility costs (GenGov departments and street lights)	125,025
Eliminate hydrant rental	235,498
Reduce Parks' projects budget	184,133
Net all other expenditure adjustments	(37,379)
Pension and reserve contribution adjustments:	
Suspend 2014's annual police and fire pension reserve contribution	2,833,786
Reduce MVD reserve contribution	649,477
Prefund 2014 expenditures using 2012 & 2013 under expenditures:	
General Government's (GG) tort liability reserve contribution	1,008,484
GG General Insurance Premiums	850,000
GG Workers' Compensation reserve contribution	1,472,709
GG Unemployment reserve contribution	161,038
MVD Reserve contribution	744,555
Overlay contribution	1,000,000
Total Budget Changes:	<u>\$ 10,431,851</u>
Revised Annual Balance	<u>\$ -</u>

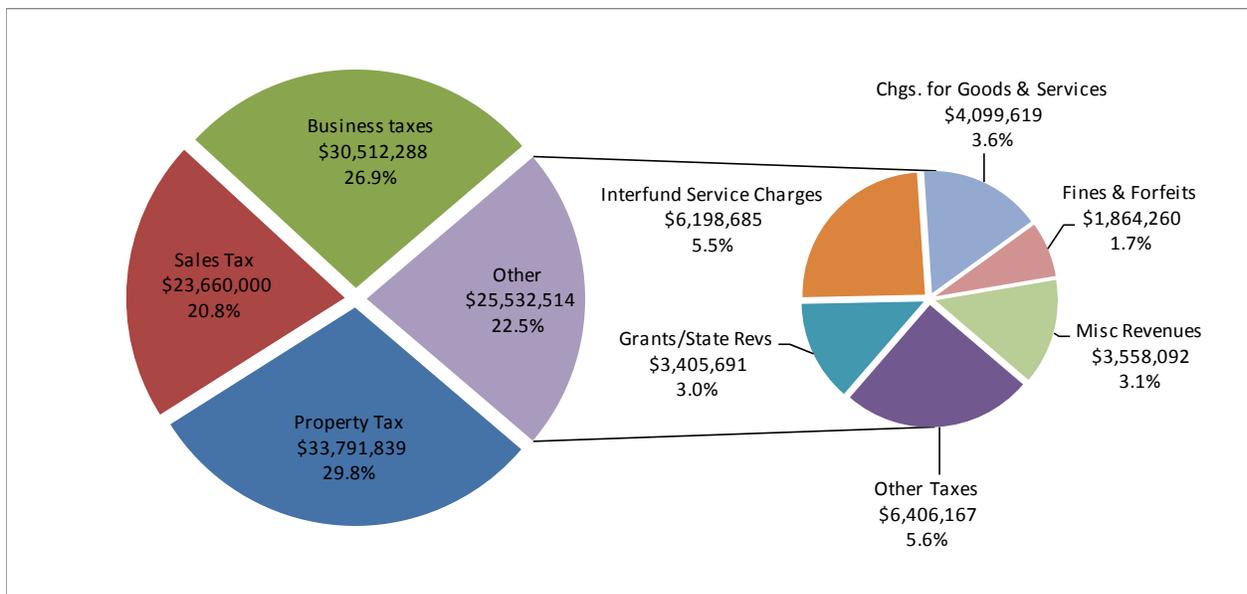
**General Government Revenues**

The 2014 general government revenue budget, excluding beginning fund balance, is \$113.5 million - a 1.0% increase over the 2013 year-end forecast. It provides for an ending fund balance of \$22.7 million, or 20% of operating revenues, and maintains compliance with the City's fund balance policy.



Everett strives to maintain a diverse and stable revenue base to shelter public services from short-term fluctuations in any one revenue source. The current economic development activities are helping to move the City toward a more balanced revenue base, as shown in the graph below.

**General Government Revenue Sources**



### **Special Revenue Funds**

The City has 17 Special Revenue Funds which account for the proceeds of specific revenue sources that are restricted for specific expenditure purposes. These funds are related to General Government operations. Budget details can be found in the Special Revenue section of this document. Items of note include:

- The Hotel/Motel tax fund made \$150,000 in grants available to support and promote tourism within the City for the second year in a row.
- The EMS Division of the Fire Department has a \$7.6 million operating budget that is funded by a property tax levy and transport fees. Voters reaffirmed their commitment to the paramedic program by approving a levy lift to increase the EMS levy rate to the maximum permissible rate of \$0.50 per \$1,000 assessed valuation in April 2010. While the restoration of the levy rate raised the allowable collections for 2011, subsequent reductions in assessed value and the \$0.50 levy rate ceiling resulted in a decrease in property taxes for 2012 and 2013. The City is able to regain a portion of the voter approved EMS levy in 2014 as assessed values increased.
- A position was eliminated through attrition from Fund 197 – Community Housing Improvement Program and Housing and Community Development Projects due to reductions in federal grant funding.

### **Enterprise Funds**

The City has seven enterprise funds that are mainly self-supporting and expected to operate like private businesses. Items of note include:

**Utilities (Water, Sewer and Surface Water Management):** Overall, service revenues are projected to increase by approximately 12.8% for 2014. The increase is necessary to address the City's capital replacement and improvement programs and to finance inflation-based cost increases in operations and maintenance. The increase also offsets the revenue shortfall resulting from the Kimberly-Clark mill moving out of Everett. The estimated impact to the average residential customer is approximately \$5.22 per month for water, filtration, sewer, and surface water combined. However, even with this increase the utility's rates still compare favorably to neighboring utility agencies. In addition, Utilities issued \$62.1 million of revenue bonds in 2013 to ensure cash flow for capital replacement and improvement projects.

An increase in Utilities' current service expense level is projected at \$2.6 million, which is primarily a \$1.0 million increase in personnel and medical costs, a \$0.9 million increase in interfund professional services, a \$0.8 million of new and replacement vehicles and a \$0.5 million increased internal taxes. The increase will be counterbalanced by a reduction of both \$0.4 million in debt service costs and \$0.5 million of repairs and maintenance in 2014.

The 2014 budget includes three additional full time employees: a Communication Technician, a Utility Laborer and a Water Quality Process Analyst. The Communication Technician will support the warehouse and city crew communication system activities, the Water Quality Process Analyst will be responsible primarily for monitoring and managing the water quality in our source water reservoirs, and the new Utility Laborer, along with two Street Department Utility Laborers who have been temporarily assigned to Utilities, will work on the inspection and cleaning of all catch basins, retention basins, storage vaults, ditches, culverts, and manholes, for compliance with Department of Ecology Phase II Stormwater regulations.

The Utility Department strives to maintain a balance between preserving essential services for its customers while minimizing the cost of service. We continue to invest in our future, efficiently manage our resources, and provide a high level of service to City residents and purveyors.

**Transit Fund:** Everett Transit implemented a 15% overall service reduction in September 2012. The effect was a significant reduction in overtime expense in 2013. Sales tax revenue enjoyed a small uptick, increasing 5% from 2012 to 2013. With total operating revenues 2% over budget and total operating expenses 7% below budget, cost reductions in service and other areas resulted in total operating expenses being 1% less than total operating revenues.

Everett Transit implemented a 25 cent across the board fare increase in January 2013. Although total ridership decreased 18% from 2012 to 2103, fare revenue was only 2% below budget.

Everett Transit continues to upgrade its fleets of fixed route and paratransit vehicles with the assistance of federal grant funds. Twelve vehicles were replaced in the first six months of 2013. Seven fixed route diesel buses, some more than 20 years old, were replaced by diesel-electric hybrid buses that have a >25% improved fuel economy. Five gasoline paratransit vans were replaced with more fuel-efficient, modern clean-diesel-powered vans. Transit also continues to make bus stop and shelter improvements along major corridors within the City with the assistance of federal grants.

Transit coordinates services with sister agencies to facilitate regional travel for the residents of its service area, including support of the bus rapid transit (SWIFT) service along Evergreen Way within the City limits as well as the seamless fare service provided by One Regional Card for All (ORCA). Within the ORCA system, special pricing plans are available to employers, schools, and social service agencies through Business Accounts aimed at encouraging commute trip reduction and improving the environmental footprint of the City.

### **Capital Expenditures**

The total budgeted capital expenditures by major category for 2014 are listed below. Further detail can be found in the Capital Improvement Program section of this document.

#### **2014 Budgeted Capital Expenditures**

<b>Category</b>	<b>Included in Operating Budget</b>	<b>Included in Capital Budget</b>	<b>Total</b>	<b>Percent of Total</b>
General Government	\$ 5,766,315	\$ 1,858,716	\$ 7,625,031	11.2%
Transit	773,095	-	773,095	1.1%
Parks & Recreation	540,270	962,465	1,502,735	2.2%
Transportation	3,880,282	5,767,878	9,648,160	14.2%
Utilities	2,083,600	46,416,400	48,500,000	71.3%
<b>TOTAL</b>	<b>\$ 13,043,562</b>	<b>\$ 55,005,459</b>	<b>\$ 68,049,021</b>	

### **Economic Environment**

The national and local economy declined severely from 2008 through 2009. The depth and length of this recession and its impact on the local economy is still ongoing. Although it has been determined that the national recession ended in June 2009, local economists believe that our region's economy bottomed out in early 2010. Since then, we have seen modest improvement in some areas but further decline in others. We expect similar performance in 2014.

Construction permitting was sluggish in 2013 compared to 2012. As shown in the table on the next page, the City experienced a decline in the number of permits issued in all but one category. Moderate growth is expected in 2014.

Slow growth is anticipated for home prices and sales in 2014. Local indicators suggest a more balanced housing market with home price gains coming back in line with historical trends as more inventory comes up for sale. Final site selection for Boeing's 777X wing assembly will likely have an impact on home sales and prices in Snohomish County.

<b>City of Everett Local Housing Industry Indicators</b>			
	<u>2012</u>	<u>2013</u>	<u>Change</u>
<u>City of Everett Construction:</u>			
Single Family Permits	99	62	-37.4%
Single Family Valuation	\$ 19,846,770	\$ 14,831,700	-25.3%
Multi-Family Permits (Units)	-	1	
Multi-Family Valuations	\$ -	\$ 13,916,948	
Commercial Permits	9	5	-44.4%
Commercial Valuations	\$ 50,192,877	\$ 14,287,510	-71.5%
Residential Alterations	254	233	-8.3%
Residential Alterations Valuation	\$ 4,527,094	\$ 5,125,975	13.2%
Commercial Alterations	314	267	-15.0%
Commercial Alterations Valuation	\$ 59,484,263	\$ 36,123,982	-39.3%
Sources: City of Everett Engineering Department			

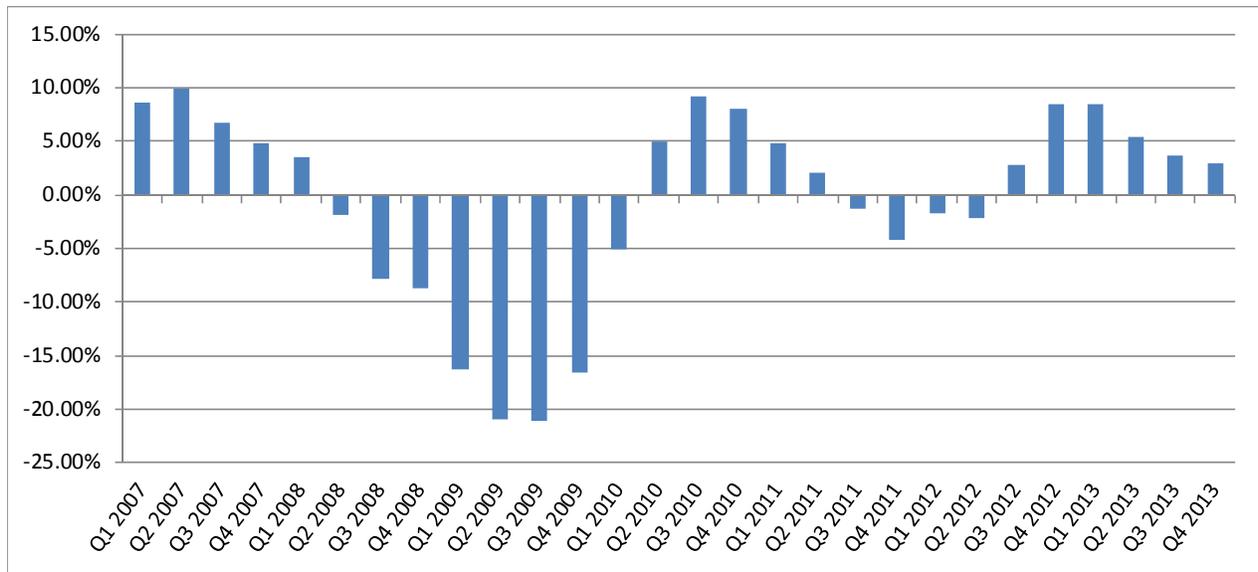
As of December 2013, the unemployment rate in Snohomish County was 5.3%. Employment is expected to grow slowly throughout 2014.

Snohomish County Unemployment Rate (not seasonally-adjusted)	Dec 2009	Dec 2010	Dec 2011	Dec 2012	Dec 2013	% Change 12-13
	10.8%	10.0%	8.2%	6.6%	5.3%	-19.7%
Source: Washington State Employment Security Department						

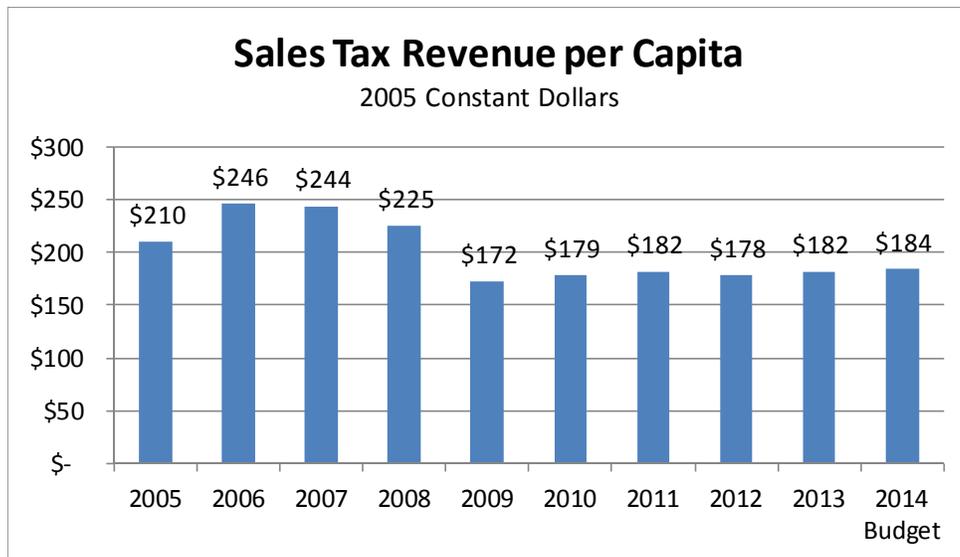
The City's three largest sources of tax revenue are property tax, sales tax, and business & occupation tax. Property taxes are limited to 1% annual growth in Washington State. Because the City's regular levy rate is well under the legal limit, declining property values have not affected property tax revenues. In contrast, the struggling economy has had a marked impact on sales tax revenues.

The City began to see noticeable declines in sales tax in mid-2008, after experiencing extraordinary growth in 2006 and 2007. As shown in the chart below, sales tax revenues declined for eight consecutive quarters starting in June 2008. This trend began to turn around, beginning April 2010, with increases every quarter for five quarters. However, another dip occurred in mid-2011 through much of 2012. Starting September 2012, activity began to increase again, with a return to positive performance in the last two quarters of 2012. Sales tax revenues are expected to grow by 3.0% in 2014 and continue at this pace for the next few years.

### Sales Tax Annual Quarter over Prior Year Quarter % Change



The sales tax revenue per capita is shown in the chart below with annual sales tax revenue translated into constant dollars so that the impact of inflation is removed. There was a substantial decrease between 2006 and 2009 in the taxes available to provide services to our residents. Adjusted for inflation and population growth, we expect that real taxable retail sales may not fully recover for several more years.

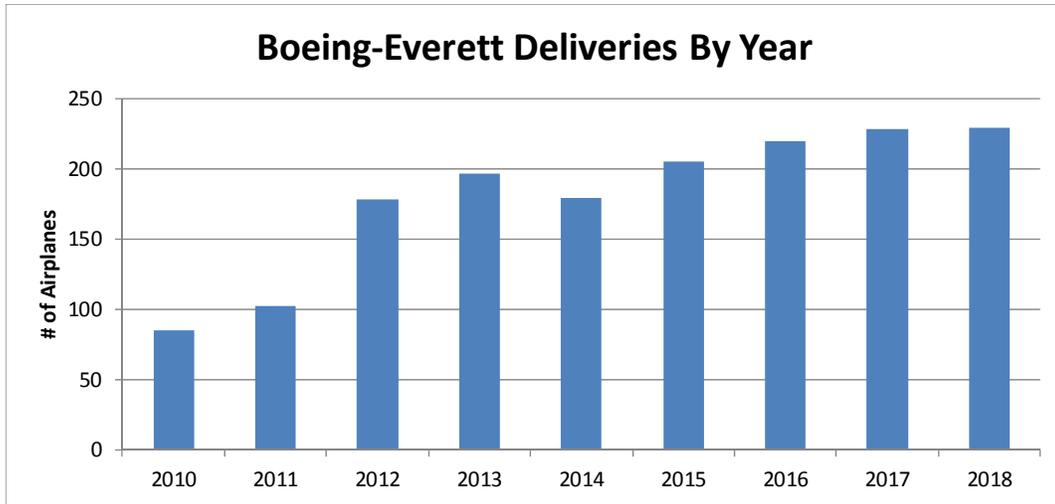


The chart below breaks out sales tax into major categories and shows variances in activity between 2012 and 2013. All categories but Construction and Food Services showed a healthy gain. The Construction category is down due to several larger projects coming to a close. Based on permit activity, construction is expected to remain fairly flat for 2014.

The City's largest business category, Retail Sales, is expected to grow 4.3% in 2014 over the 2013 budget.

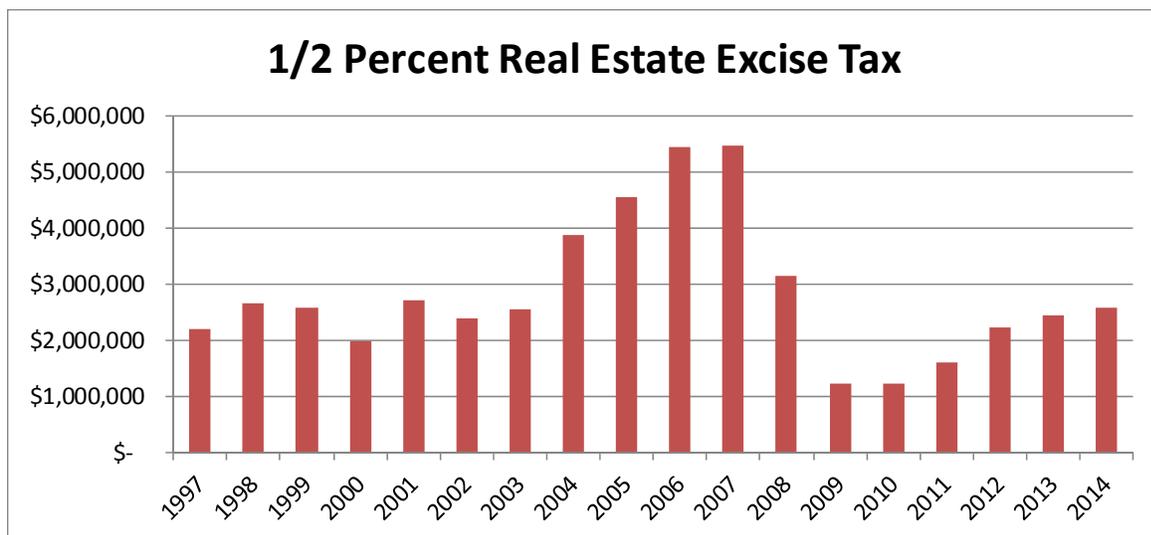
<b>Sales Tax Revenue</b>		
<b>Category:</b>	<b>% Change 2012-2013</b>	<b>Category as % of 2013 Retail Sales</b>
Manufacturing	4.2%	6.5%
Wholesale	6.7%	8.2%
Information	6.2%	4.8%
Food Services/Accomod.	1.0%	9.2%
<b>Retail</b>	<b>5.8%</b>	<b>45.1%</b>
All Other Categories	9.8%	15.0%
Construction	-0.1%	11.3%
<b>Total Sales Tax</b>	<b>5.2%</b>	<b>100.0%</b>
<b>Retail Sales:</b>		
<u>Areas of Strength</u>		
Motor Vehicle	13.5%	31.7%
General Merchandise	0.8%	24.4%
Food & Beverage Stores	3.6%	5.8%
Building/Garden	10.6%	5.5%
Clothing	5.9%	3.9%
Sporting Goods	4.7%	3.5%
Nonstore Retailers	7.4%	3.3%
Health/Personal Care	3.0%	3.0%
Furniture	13.2%	2.9%
Gas Stations	8.9%	2.7%
<u>Areas of Weakness</u>		
Electronics	-6.5%	5.3%
Misc Retailers	-0.5%	8.0%
<b>Total Retail Sales Tax</b>	<b>5.8%</b>	<b>100.0%</b>

The City's 2013 business and occupation tax, which is based on gross business receipts, came in 9.0% over 2012 as a result of Boeing's 787 airplane deliveries, which are expected to remain strong for the next several years. The chart below shows actual and forecast airplane deliveries for a nine year period. Boeing builds or assembles 747's, 767's, 777's and 787's in Everett.



Monthly real estate excise tax (REET) receipts (0.5% of the value of real estate transactions) represent a vital funding source for park and road projects and debt service payments. The following chart illustrates the impact of the Great Recession on REET revenues, beginning with a precipitous drop in 2008 that was followed by an additional large decline in 2009.

Collections began improving in 2011 and continued strong in 2013 with revenues coming in 34% higher than originally budgeted. Based on indications that the housing market will remain steady, 2014 collections are budgeted to grow by 5.5% over 2013 collections.



## **City of Everett - 2014 Priorities and Current Initiatives**

The City of Everett current initiatives focus on keeping our City services strong while preparing for future opportunities.

### **1. Foundation of a Great Community**

- **Financial Health**

The City continues to live within its means and is maintaining compliance with the fund balance policy. However, while we have developed balanced budgets for 2009 through 2014, maintained essential services, and minimized service reductions, some of the adjustments (deferred reserve contributions, deferred maintenance projects) are not sustainable for the long term.

Significant factors impacting the City's ability to maintain its current operating budget include:

- Six years of depressed revenues while costs of services continue to rise;
- The permanent loss of about \$1.0M in the General Fund and over \$2.0M in the Utility Fund when a major manufacturer closed its doors in 2012;
- A significant shift in our sales tax base as large retail centers have opened to the north and east of Everett;
- The state permanently reducing state shared revenues;
- Property tax limited to 1% growth; and
- A reduced B&O manufacturing tax rate to entice Boeing to build the 787 here.

As noted in the Mayor's message, department directors have been asked to take a comprehensive look at city business and develop options and recommendations for restoring structural balance to the City's general government budget.

Everett's general obligation and revenue debt rating were reaffirmed by Standard & Poor's at AA+ in September 2012 and January 2013, respectively. This rating means Everett taxpayers likely will pay lower interest rates on bonds issued for capital improvements than they would have if the City held a lower credit rating.

- **Public Safety**

The Police Department has completed a new strategic plan that lays a blueprint for police operations and service delivery over the next five years.

Construction for a much-needed new municipal court was completed in 2013. The Residential Graffiti Removal Program continues into its sixth year in 2014. The Fire Administration building seismic retrofit, which is funded primarily with grant funds, will be completed in 2014.

- **Streets**

The City will make a \$9.6 million investment in streets in 2014. Projects include the annual overlay program, completing the Evergreen Way Bus Rapid Transit project, and the replacement of the Broadway Bridge at Hewitt Avenue.

- **Water/Sewer Utilities**

Over the next decade, the City will spend more than \$550 million to improve drinking water and wastewater systems to meet growth demands and regulatory requirements. The City provides drinking water to more than 550,000 people in Everett and Snohomish County, and sewer service to more than 140,000 people in Everett and adjacent areas.

## 2. Investment and Redevelopment

- Current large projects in the planning stages or underway in Everett include:
  - The Everett Community College expansion, which will conclude with a doubling of the campus size by 2015.
  - The Farmer's Market and residential living project.
  - Boeing's north tower office building.
  - The new Marriott Courtyard Hotel on surplus City property.
- Economic Development Focus
  - The fundamentals for a strong and increasingly diverse economy exist in Everett, including aerospace, Naval Station Everett, the health care community, the Port of Everett, and the SW Everett light industrial area.
  - Saltchuk is completing due diligence to locate a boat repair and construction facility at in the site formally held by KC. It should bring more than 250 family-wage jobs.
  - Residential construction is expected to begin in the Riverfront area in Spring 2014 with more than 200 homes completed by 2015.
  - The City participates in the Economic Alliance—a consolidation of Snohomish County's economic development organizations.
- Higher Education
  - Bringing a four-year university to Everett is in the forefront of our goals for this community. The City believes that Everett is the best location for a new four-year university that will provide the upper-division and advanced-degree access that our students, families, and employers seek. Everett and Snohomish County continue to be among the most under-served areas of the state.
  - In 2011, the City was successful in obtaining legislation to transfer operation and administration of the University Center of North Puget Sound to Washington State University. WSU took over University Center in 2013. Nearly 600 students are expected to enroll at the University Center in 2014 with enrollment increasing to 1,100 by 2018.
  - Design and plans to expand University Center are underway with \$10 million from the State Legislature. Additional funding is being sought for construction.
- Commercial Air at Paine Field
  - The City supports the development of commercial flights at Paine Field. A 2008 study showed that the City could attract more and larger high-tech businesses if commercial air service were more convenient. The study also said that regularly scheduled passenger flights could stimulate tourism and other economic development in the region.
- Navy
  - Naval Station Everett (NSE) is the homeport for the USS Nimitz and a number of other classes of ships. The base currently has approximately 6,000 employees. Over the next few years, all three frigates currently stationed at NSE will be replaced by destroyers, increasing base population by approximately 325 sailors.

## 3. Improving our Quality of Life

- Parks
  - In 2011 the City completed a master plan for Senator Henry M. Jackson Park. Phase One of the plan began on the west side of the park in 2013, with expected completion in 2014.

- Community Events

The City will continue popular community events such as Sorticulture, Music in the Parks, Jetty Island Days, and Cinema Under the Stars.

### **Other Planning Processes**

In addition to the five-year outlook budget model, the capital improvement plan, and the economic development plan, the City of Everett has numerous boards, commissions, and committees that play a role in helping to plan for the City's future. These include, but are not limited to: Animal Control Board, Council of Neighborhoods, Cultural Commission, Diversity Advisory Board, Historical Commission, Housing & Community Development Board, Housing Authority, Human Needs Advisory Committee, Library Board, Lodging Tax Advisory Board, Parks Commission, Planning Commission, Public Facilities District Board, Salary Commission, Senior Center Advisory Board, Transportation Advisory Committee, Tree Committee, Mayor's Youth Council, Neighborhood Associations and various ad hoc committees. These groups mainly have an advisory role to the City, and were created either by code or assignment.

### **The Future – Principal Issues Facing the City**

There are a number of issues facing the City of Everett that present significant challenges or opportunities as we look to future years. These include legislative changes, regulatory changes, world events, and economic factors. This section describes and updates these subjects for events occurring subsequent to the November/December budget hearings.

#### **The Economy**

The Consumer Price Index (CPI) has a significant impact on the City budget. City bargaining unit cost-of-living adjustments and many other City contracts are tied to CPI. The June 2012 to June 2013 CPI percent change resulted in a 1.4% CPI-based wage increase for union employees with current contracts for the 2014 calendar year. Appointive employees and elected officials also received a 1.4% cost-of-living increase for 2014. The five-year budget assumes low CPI growth for 2014 and a moderate growth in CPI for all future years.

#### **Boeing Production**

The Boeing Co. delivered its first 787 Dreamliner jet in September of 2011. In October 2009, Boeing announced that it would set up a second production line for the 787 Dreamliner in South Carolina. Since the dawn of the jet age, virtually all Boeing airliners have been assembled in either Everett or Renton, Washington. The City and State intend to work together to ensure that Washington State remains the center of aerospace manufacturing, both nationally and internationally. The set up of the second production line outside of Everett is not expected to have an impact on the current strategic outlook. 787 production will be at full capacity for many years, contributing to a stable business environment for our community.

In 2011, the Pentagon awarded the contract for the U.S. Air Force Aerial Tanker Program to the Boeing Company. The tankers will be assembled in Everett, supporting 9,000 jobs in our state, providing \$400 million in economic benefits and supporting some 70 suppliers across the state. The contract will provide orders for the first 179 tankers.

In 2013, Boeing initiated a nation-wide competition to select a site to build the new 777x. In response, the legislature voted in a tax incentive package and the Machinists Union approved an eight-year contract to position Washington State as the preferred location. Based on those actions, Boeing selected The Puget Sound as the preferred site for the next generation 777, securing the presence of the aerospace industry and thousands of family wage jobs in this area for many years to come.

**B&O Tax Credit**

In March 2010 the City amended the Business and Occupation tax ordinance by adding a tax credit for expansions that create 50 or more new jobs within four quarters. The taxpayer may claim a credit of one thousand dollars per new position, subject to a cap of \$500,000 per taxpayer. The added positions must remain filled for at least three years.

**State of Washington/U.S. Government**

The City receives various state-shared revenues including Streamlined Sales Tax Mitigation, Criminal Justice Assistance, Liquor Revolving Account, Liquor Excise Tax Account, and Motor Vehicle Fuel Tax; and various operating program grants, mainly related to public safety; and some capital grants. The state's budget constraints have resulted in reduced revenue sharing and fewer available grants for 2014.

The U.S government also provides grant funding for City programs, mainly in the areas of road construction, transit and Community Housing Improvement Program (CHIP) funding. Like the state, the federal government has also had to cut back the number and size of grants it makes available to local jurisdictions.

Together, the reduction in state shared revenues and state and federal grants will force the City to rely more heavily on already strained local revenues to support operations and capital investments, and ultimately make difficult decisions regarding the City's ability to maintain current service levels.

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