

TUMWATER CITY COUNCIL WORKSESSION
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CONVENE: 7:00 p.m.

PRESENT: Mayor Ralph Osgood, Councilmembers Pete Kmet, Judith Hoefling, Ed Hildreth, Neil McClanahan, Joan Cathey, Bruce Zeller, and Ed Stanley.

Staff: City Administrator Doug Baker, Finance Director Jim Hendrickson, City Attorney Karen Kirkpatrick, Planning and Facilities Director Michael Matlock, Police Chief John Stines, Parks and Recreation Director Chuck Denney, Human Resources Director Eric Trimble, Public Works Director Jay Eaton, Fire Chief John Carpenter, and Recording Secretary Valerie Gow.

Others: John Fedor and Betsy Murphy, citizens.

BUDGET WORKSHOP: Mayor Osgood commented that the overview will provide a substantial amount of information. Efforts have been undertaken by the administration to ensure the budget is balanced at the end of 2009, as well as through 2010 in projecting revenues and expenditures. To get there, reductions and eliminations have occurred. There have been no staff layoffs but some positions have been moved from the General Fund to positions supported by utility accounts. Other positions remain vacant and there have been some program eliminations. The goal is to reduce expenditures where possible and pursue frugal efforts to reduce costs while maintaining a level of service and not losing staff.

Director Hendrickson provided a budget presentation on the status of the budget. The effort began in January when the first position was not filled based on expectations of what could occur in 2009. In February, as the fourth quarter information was released, it became apparent that the decline was beginning to occur. The recent quarterly report released by the Economic Forecast Council revealed that the fourth quarter of 2008 was the worst quarter of decline on a year-to-year basis ever.

Director Hendrickson reviewed the beginning balance for 2009 as estimated in November 2008. There are several areas where there were surprises, such as sales tax higher than expected as well as higher Business and Occupation (B&O) tax. Development permit fees were above the budgeted amount. The major reduction in expenditures was because the labor contract with the Police Department was not secured and funds budgeted for 2008 were not expended. There were other areas in reduced expenditures as well. The \$108,000 reduction in services, contracts, and supplies was from administration's direction to department directors to reduce expenditures as it became apparent the economy was beginning to worsen. The City anticipated ending 2008 with \$1,990,304 in the ending fund balance but actually ended with \$2,689,266. The difference was \$698,961, which will result in a 2009 amendment to the budget.

Councilmember Kmet asked whether the \$698,961 is above the City's reserve. Director Hendrickson affirmed it is in addition to the City's 8% contingency reserve.

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Director Hendrickson reviewed a chart on sales tax revenue by source in the following categories:

- Retail Trade
- Wholesale Trade
- Manufacturing
- Construction
- Accommodations & Food Service
- Professional Services, Recreation, and Other

February sales tax receipts are higher than anticipated. Accommodations and restaurant sales have been climbing because of additional openings of restaurants in the City. He noted the spike in the “other” category occurring in June follows the state’s budget cycle.

Director Hendrickson reviewed the detail of sales tax for each category of sales from 2007 to the current date. A downturn trend began in September 2008 in retail sales tax. However, January 2009 exceeded January 2008 in retail sales tax. In the near term, the retail trade sector is showing some hopeful signs. February sales tax was received in April, as there is a two-month delay in receiving sales tax revenue from the state.

Accommodation and food service includes restaurants, catering businesses, and drinking establishments. Receipts in 2008 exceeded sales in 2007 except in December because of the weather. January 2009 shows a continuing increase in tax receipts. Director Hendrickson noted retail trade sales tax is the City’s major source of sales tax revenue.

Wholesale trade sales tax includes computer businesses, computer equipment wholesalers, electronic parts suppliers, lumber and plywood, industrial machinery, and industrial supplies. The revenue has been a fairly steady income stream and is typically more unpredictable. Since November 2008, the trend has been lower until February 2009, when it increased. A spike in June 2007 was caused by a major sale of computer equipment by one manufacturer.

Professional services, recreation, and miscellaneous sales tax is a catch-all category and includes businesses such as computer programmers, veterinary clinics, advertising, janitorial services, locksmiths, temporary services, athletic clubs, bowling alleys, golf courses, and activities related to the sale of goods by government agencies. It’s a consistent source of revenue and has been declining since September 2008. In February 2009, sales increased.

Manufacturing trade sales tax includes sales of machinery manufacturers, printing businesses, and wood products firms. The sector has dropped significantly since July 2008 and it appears manufacturing sales tax has been affected by the streamlined sales tax rules.

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Construction trade sales tax includes the construction building industry of residential and commercial construction and associated specialty contractors serving the construction industry. Construction sales tax remained fairly strong throughout 2007, but began to decline in October 2008, which continues until today. However, February 2009 sales exceeded February 2007 sales.

Director Hendrickson responded to questions regarding optimism in sales tax trends and noted that across all sectors, sales tax collections are experiencing a decrease. It's difficult to glean which sectors are performing better from the state's economic forecast because so many types of state revenue sources are included. However, retail trade is separated representing auto sales, furniture, and other retail sales, which are experiencing a major downturn. The actual figures for March sales will not be received until the end of May.

Councilmember Kmet commented that he often asks retailers about customer traffic and sales when he's purchasing items. The response has been positive in that retailers are beginning to see an increase in customer traffic and that sales are beginning to pick up.

Director Hendrickson said during January, February, and March 2009, the City received 10.4%, 16.4%, and 17.3% less than the same months in the prior year, respectively. However, in April, the figure is 5.7%, which is an incredible improvement in just one month of sales. It changes the yearly trend line somewhat. However, accounting for sales through April and trending it out over the year at an average of 12.8% below what was received in 2008, the City will experience approximately a \$500,000 gap from the original budget for 2009. April receipts reflect sales occurring in February.

Director Hendrickson reviewed a graph representing straight-line trend of B&O tax with cumulative receipts through March 2009. The first quarter of B&O tax for 2009 is due at the end of April. Receipts for the fourth quarter in 2008 reflect a 19% reduction from the prior year for the same period. At that rate, the trend line reflects a reduction of \$200,000 from the original budget for 2009.

Director Hendrickson said he is projecting a \$500,000 reduction in sales tax revenue, \$200,000 reduction in B&O tax, and Director Gellenbeck is suggesting lowering the budget expectations for permit revenues by an additional \$100,000. In 2008, the City received over \$1.2 million in permit fees. The 2009 budget was \$750,000 to compensate for the economy. Current activities provide more evidence that the City should reduce the budget another \$100,000.

During the final meeting in 2008, the City Council entered into an agreement with Thurston County Medic I to take over the SPRINT unit in Rochester. The contract added four paramedics on staff with two more planned to join by the

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middle of the year adding approximately \$750,000 to salaries and benefits to the Fire Department and an increase in intergovernmental revenue by the same amount, as the City is compensated 100% for the contract.

Interfund transfers are down by \$186,542. The Asset Fund or ER&R Fund has over \$6 million in assets maintained by the fund and rented to all departments. The City manages over 150 computer workstations and laptops, 30 printers and numerous network servers, switches, and routers for a functioning network, 26 fully equipped police cars and other administration pool vehicles, 35 trucks, and a number of pieces of heavy equipment. In examining areas to reduce costs, department directors were polled concerning a request to lengthen the life of all equipment by one year. There were no major issues reported with the suggestion and subsequently the City moved forward to extend the life of all equipment by one year as well as reduce the cost of most computer workstations by \$500 given the advances in technology compared to the actual needs of most of the users. Consequently, expenditures can be reduced by \$175,000 in rent back in the General Fund to the Internal Service Fund and another reduction to Utility Funds of approximately \$50,000.

Expenditures for salaries and benefits, supplies, and services and contracts were reduced by over \$330,000 by department directors including the loss of \$140,000 in new temporary help for facilities and the street departments. Director Hendrickson reviewed some of the reductions. For example, janitorial services for the City were reduced by eliminating service one day a week.

Director Hendrickson reviewed the reduction in salaries and benefits of approximately \$511,000 by freezing one unfilled position in Finance, two positions in the Police Department, one position in the Fire Department, and four positions in Development Services. This amount is separate from the aforementioned reductions. Most of the positions will remain budgeted in the General Fund but will remain unfilled. However, three staff members have moved to Public Works positions and their labor costs will need to be amended from the General Fund and into Public Works temporarily until the positions are unfrozen and filled. The overall savings to the General Fund this year is \$511,000.

Councilmember Kmet questioned the sustainability of the Utility Funds absorbing the three positions transferred from the General Fund. Director Hendrickson said one of the positions filled a vacant position in Public Works Operations. Public Works Director Eaton added that one of the other positions filled a slot as an inspector in the transportation construction fund.

Director Hendrickson reviewed a summary of actions proposed for 2009:

- Carry forward savings of approximately \$700,000 from 2008 consisting of higher than estimate revenue in sales tax, B&O tax, and Development fees combined with efforts taken since mid-2008 by all departments to

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reduce expenditures in anticipation of future needs as the extent of the budget challenge became apparent.

- Reduce revenue expectations for sales tax, B&O tax, and development fees, reducing revenue by approximately \$700,000 in 2009.
- Adjust the budget for Medic One SPRINT. Cost-neutral adjustment.
- Extend the life of all Equipment Rental assets by one year and reducing replacement cost for most computers. Annual savings of approximately \$175,000 in 2009.
- Line item review by department directors recommending reductions in the budget of approximately \$330,000 in 2009.
- Freeze vacated positions for the remainder of the year saving \$511,000 in 2009.
- Factor in an anticipated reduction in PERS contributions from a pending bill in the Legislature that will reduce benefit costs by \$70,000 in second half of 2009.

Results of actions in 2009 budget will allow for preserving the 8% cash reserve and savings of approximately \$935,000 as carrying forward to 2010.

Proposed further actions for 2010 include:

- Maintain the same expectations for sales tax, B&O tax, and development fees as in 2009.
- Adjust for additional Medic One SPRINT staff (one additional member factored in). Cost-neutral adjustment.
- Savings from adjustments in Equipment Rental assets will continue at a similar rate of \$175,000.
- Line item reductions recommended by department directors in 2009 will continue in 2010, saving \$230,000
- Freeze on vacated positions will continue through 2010. Savings of approximately \$675,000.
- Anticipated PERS contribution reduction savings in 2010 of approximately \$140,000.

Most revenues unchanged from 2009 to remain conservative and expenditures maintained at 2009 levels with few exceptions that are based on wage and benefit increases.

Director Hendrickson reviewed a budget graph of the aforementioned adjustments representing the General Fund for 2010. The ending fund balance from 2009 is projected to be \$934,801, which is above the 8% contingency. Based on the ending fund balance, expenditures, and revenue, the 2010 beginning budget is a negative \$555,923.

Director Hendrickson provided a review of the forecasted assumptions for some of the major revenue and expenditure accounts.

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Other actions for consideration include:

- Retain half of the utility tax from the General Government fund of the Capital Facilities Plan in the General Fund.
- Transfer funds from the City Hall Cumulative Reserve Fund to General Fund.
- Increase in City-owned Utilities (Water, Sanitary Sewer, Storm Drainage) utility tax.
- Increase in Business & Occupation Tax.
- Transportation Benefit District.
- Reduction in services
- Others?

Within the General Governmental fund of the Capital Facilities Plan, the proposed projects for no funding include:

- Historic Preservation Commission and Park Board funding of \$35,000.

Projects moved to future years include:

- "T" Street Park of \$40,000 (2009) and \$366,000 (2011)
- Historical Park Improvements of \$25,000
- City Hall Roof Replacement of \$250,000
- Pioneer Park Riverbank Stabilization/Trail Restoration of \$70,000

This action will free up sufficient funds to retain half of the utility tax and transfer it to the General Fund and leave the remaining half in the CFP.

City Administrator Baker commented on the possibility of moving the Phase 3 Pioneer Park project to future years, which essentially represents one baseball field and some parking to future years. Director Hendrickson reported the project cost includes Park impact fees and \$254,000 in cash.

Councilmember Kmet added that the project also includes wetland mitigation. There is a risk if the project does not move forward because of permitting requirements involving a shoreline permit. The project has already been delayed by many years.

Director Hendrickson referred to the transfer of funds from the City Hall Cumulative Reserve Fund to the General Fund. The Cumulative Reserve Fund was created by an ordinance in 1997 with the purpose to be a bank of funds to be used for City Hall repairs. With a motion by the Council, the funds could be transferred to the General Fund to maintain services during the economic crisis. The \$250,000 project in the CFP for City Hall Roof Replacement is funded by a transfer from the Cumulative Reserve Fund to the CFP. By retaining the funds in the fund and an additional balance of \$50,000, the proposal is to transfer

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\$300,000 to the General Fund.

Director Hendrickson said based on the aforementioned strategies, 2010 would end with a surplus of \$269,340 in revenue than in forecasted expenditures, which is more than the amount necessary to maintain the 8% reserve. That is less than 1/10th of the total budget. Other factors will also need to be considered, such as retirement cash outs and other expenses.

Director Hendrickson described other possible budget scenarios if revenues continue to decline. Other options available for consideration include an increase in the City's utility tax, which can be increased without a ballot measure. Any utility tax beyond 6% requires a vote of citizens. The Council could consider a possible increase in B&O tax. There has been some discussion about the potential for a Transportation Benefit District. Other options include reduction in services.

Director Hendrickson reviewed a study of utility tax rate increases and the amount that could be generated based on specific percentages and the effect on a typical residential utility account. A number of cities have recently raised utility taxes.

Councilmember Kmet asked about other measures cities are taking to close the budget gap. Director Hendrickson said many cities are implementing cuts in services and staff. Some are closing offices for a day. He believes that the City of Gig Harbor reduced its workweek.

The Council reviewed an analysis of a potential B&O rate increase and a list of all cities assessing B&O tax. The City charges 1/10th of one percent for manufacturing, retail, and wholesale, and 2/10ths of one percent for the service industry. Over three-quarters of businesses in Tumwater fall into the lower percentage rate. The average rate for the state is .0016%. Neighboring jurisdictions assess .001%. The only change since 2008 was in the City of Ruston.

Councilmember Kmet asked whether an increase in B&O tax is subject to a public referendum. Director Hendrickson advised that it is a councilmanic action subject to a public referendum.

Discussion followed on utility tax and whether it's subject to a public referendum. City Attorney Kirkpatrick advised that she doesn't believe utility tax is subject to a public referendum.

Director Hendrickson reported an increase in B&O tax from .001% to .0015% would result in an additional \$411,525 in tax. The maximum rate of collection is .002%.

Other options include a potential levy lid lift of approximately \$1 million

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through an increase in property tax. The cost would be approximately \$11.12 annually on a \$275,000 home and \$12.13 annually on a \$300,000 home.

Mayor Osgood complimented staff for their efforts to date and work on the budget. The budget does include the elimination of the Tumwater Harvest Festival of approximately \$45,000. Although the community festival is important, the event consumes a great deal of resources.

Councilmember Kmet commented on the practice of the City continually spending down the Hotel/Motel Tax reserve. The City may reach a point where it will no longer have the funds to maintain its historic program. Mayor Osgood noted that when the Tyee Hotel was in business, the City maintained a \$250,000 fund balance in the Hotel/Motel fund. The City utilized the interest to help fund historic programs. However, the reserve was expended when the Tyee closed and expenditures annually are based on projected revenue the City receives in lodging tax.

Councilmember Hoefling asked about the mechanism for paying back utility taxes that have been transferred to the General Fund. Mayor Osgood advised that any funds borrowed from utility accounts are required to be reimbursed with interest. There is no choice. However, there is no requirement to pay back utility tax as it's up to the discretion of the Council as to how the tax is allocated.

Councilmember Kmet pointed out that deferring utility tax from the CFP results in deferring maintenance and delays the development of parks and other important projects. Each time the City defers a park project the City loses credibility.

Mayor Osgood commented on an option that should be seriously considered by the Council, which is a levy lid lift requiring a public vote. The amount of funds generated from a levy lid lift would generate sufficient funds for the City during this economic downturn. Councilmanic increases in B&O or utility tax would generate less revenue than a levy lid lift.

Councilmember Stanley commented on the difficulty of passing a tax increase in today's environment. Mayor Osgood said although he doesn't disagree, if the City develops the right package, voters might pass an increase. A simple majority is required to pass a levy lid lift.

Councilmember Hildreth said B&O tax is a problem for businesses because it's assessed on gross receipts without regard to expenditures. Businesses are struggling in today's economy. Doubling the tax on revenue in today's economy is not something he would recommend. With respect to a levy lid lift, many people are losing their home. Even with a small increase, it will increase the strain on homeowners. Those issues need to be examined during the process of considering an increase.

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Councilmember McClanahan commented on the potential loss of state jobs in Thurston County and the resulting impacts to the local economy.

Councilmember Kmet said his concerns regarding B&O and utility tax is because it involves a councilmanic action. Those increases need to be considered as an absolute last resort. He agreed with pursuing a levy lid lift and giving the voters the option of increasing their taxes. The City continues to lose revenue through its tax base. The advantage of a property tax levy is that it is sustained over time building a better foundation for the future. It is also less regressive than other taxes. The City is on the edge through freezing positions and reducing expenditures to the extent possible. The City is at the breaking point as service needs continue to increase. It's prudent to ask the voters for a tax increase.

Mayor Osgood said he is somewhat fearful of 2011 and 2012 because the City's revenue base continues to decrease each year. Utilization of the City's 8% reserve is telling in terms of the City's budget. The City hasn't had a major tax increase in many years.

Mayor Osgood asked the Council for input on a potential tax increase or other taxing options.

Councilmember Zeller said he could support a levy lid lift, but is not sure it would pass. People are still scared and worried about making next months bills. Citizens would likely pass an increase in a better financial climate, but not today. He said he's not supportive of increasing B&O tax primarily because within the next five to six years, the Legislature will eliminate the tax. He suggested retaining a possible increase in utility tax as an emergency reserve, and if needed then increase the tax. He suggested utilizing all other tax resources before pursuing a levy lid lift. He complimented staff on efforts to reduce expenditures and assessing the City's needs. He said he is concerned about the lack of revenue for police and fire positions and as the economy improves, filling those positions should be one of the first things the City should do through a levy lid lift. He said he would prefer monitoring the situation over the next several months to determine what occurs in terms of revenue.

Councilmember Hoefling said she's anxious to view the March tax receipts to see if the trend in increased sales tax continues. Her big concern with a levy lid lift is putting the City in the same situation as Thurston County where police and fire are such a larger proportion of the General Fund budget, the remaining budget suffers when there is an economic downturn. She said she's concerned where the increased revenue from a levy lid lift would be utilized and if the City did pursue the measure, the public would assume it would go automatically to fund public safety. She spoke against raising B&O tax because when she often speaks to small business owners and the subject of

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B&O tax is not a positive conversation because it's burdensome on small business. She recommended retaining an increase on utility tax as a future option. If receipts continue to reflect a downward trend, a levy lift lid is likely the only option, but the message must be conveyed properly through the assistance of a consultant to ensure a successful ballot measure.

Councilmember Stanley agreed the Legislature is heading in the direction of eliminating B&O tax within the next several years. He spoke against an increase by the City. People are in the mode of entrenchment and are not voting for tax increases. If the City contemplates a ballot measure, it would be prudent to conduct some advance polling to ascertain some reasonable expectation that the measure would pass. He said he doesn't want to spend thousands of dollars on a failed ballot measure. The City needs to be careful and take a measured approach to see if it can be successful.

Councilmember Cathey voiced comments similar to the comments of Councilmembers Stanley and Zeller. She agreed any levy lid lift must be well thought and planned. The tax climate is not good, as people will not approve a tax increase to save jobs when they are losing their jobs and homes.

Councilmember McClanahan acknowledged Director Hendrickson for the excellent presentation. There are differences between Thurston County and the City because the county expended its reserve and hired more employees. The City is in better shape thanks to the work of the Mayor and staff. He agreed with other Councilmembers regarding B&O tax, because the tax is not friendly to business. An increase in utility tax should be held in reserve. A levy lid lift is likely the best way to proceed, but it will be difficult in this economic climate. The City needs to explore options.

Councilmember Kmet commented on the importance of the entire Council supporting a levy lid lift if the Council moves forward on a ballot measure.

Councilmember Hoefling said she believes the only way to pass a levy lid lift is for public safety.

Councilmember Hildreth questioned the City's budget status if the Council elects not to pursue a ballot measure. Mayor Osgood said the community is supportive of the City and values its police and firefighters. With much work and effort the City has a good chance of passing a levy lid lift while acknowledging that it isn't without a great deal of difficulty. He favors a levy lid lift rather than other tax increases because it's up to the voters to decide. It's important to give the voters a chance. If the measure is on the 2009 November ballot, revenue would not be received by the City until early 2011. The critical timeframe for a measure is the November ballot; otherwise it will be too late for the City. There is a legitimate reason to consider a November 2009 ballot measure.

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Mayor Osgood reviewed some of the budget reduction recommendations for confirmation from the Council:

- Extending life expectancy of equipment by a year within the ER&R Fund. *Concurrence by the Council.*
- Reducing janitorial service by eliminating service on Wednesdays. *Concurrence by the Council.*
- Elimination of the Tumwater Harvest Festival. *Concurrence by the Council with regret.*
- Delay Phase 3 – Pioneer Park project. *The Council discussed the project at length. The project is funded 70% with impact fees and approximately \$250,000 of General Fund money. Councilmember Kmet advocated for moving forward with the project because 70% of the project is paid by growth, the time consuming and the burdensome process undertaken by staff to obtain permits, previous delays to the project, and the likelihood that a delay will entail many more years of delay and cost the City twice as much in costs. The US Army Corps of Engineer's permit expires at the end of 2009. Director Denney noted that the Corps permit has already been extended twice, and Corps officials have not responded to his telephone calls. Mayor Osgood reported the City is currently soliciting for construction bids. At that point, the Council will need to decide whether to move forward. Several Councilmembers supported delaying the project*

Director Eaton advised the Council of the recent filing of bankruptcy action by the general contractor for the Littlerock Road Improvement Project.

Councilmember Kmet suggested scheduling a Budget Committee meeting to discuss possible tax increase proposals.

ADJOURNMENT:

With there being no further business, Mayor Osgood adjourned the meeting at 9:14 p.m.

Prepared by: Valerie L. Gow, Recording Secretary/President
Puget Sound Meeting Services