

LONG TERM FINANCIAL STRATEGY

CITY OF OLYMPIA



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TABLE OF CONTENTS

Summary	ii
Background	1
Olympia Faces a Problem	1
Purpose of the Long Term Financial Strategy	2
How the Strategy was Developed	2
How the Strategy is to be Used	4
The Foundation	5
Key Financial Principles	5
Continuous Improvement	6
The Guidelines	8
What should the city do every year, whether the financial forecast is positive or negative?	8
What should the city do in the following year's budget when the financial forecast is positive?	9
What should the city do in the following year's budget when the financial forecast is negative?	11
Summary of Opinion Survey Results	14
Top Future Priorities	17
Long Term Financial Forecast	19
Appendices:	
A. Review of Systemic Issues	
B. Opinion Survey Results	

SUMMARY

It will become increasingly challenging to maintain the City's current high service standards, meet the growing obligations of a growing community, as well as further improve our quality of life. Obligations have been growing faster than revenues. The annual gap between resources and the cost of current service levels may be nearly \$5 million by 2004.

The Long Term Financial Strategy (LTFS) is an approach to sustaining high quality services, setting priorities, and making them happen. Its focus is on the General Fund Operating Budget, though it recognizes the link with the Capital budget – general fund dollars are also spent on capital projects, and capital projects also have operating costs. It does not include the utilities budget, though there is a link there as well, through the utility tax. The purpose of the LTFS is to look forward five to six years and provide guidance to the annual budget process.

KEY FINANCIAL PRINCIPLES (Not listed in a priority order.)

1. **Make trade-offs:** Do not initiate major new services without either a) ensuring that revenue to pay for the service can be sustained over time, or b) making trade-offs of existing services.
2. **Do it well:** If the City cannot deliver a service well, the service will not be provided at all.
3. **Focus programs on Olympia residents and businesses.** However, do not exclude others from participating in these programs as well.
4. **Preserve physical infrastructure:** Give priority to maintaining existing infrastructure.
5. **Use unexpected one-time revenues for one-time costs or reserves:** One-time revenues – or revenues above projections – will be used strategically to fund prioritized capital projects, e.g., the bridge, pavement management, open space, etc. The City will also take into account follow-on costs, such as increased operation and maintenance.
6. **Invest in employees:** The City will invest in employees and provide resources to maximize their productivity.
7. **Pursue innovative approaches to service delivery:** Continue to implement operational efficiencies and cost saving measures in achieving community values. Pursue partnerships and cost sharing strategies with others.
8. **Contract in/Contract out:** Consider alternative service delivery to maximize efficiency and effectiveness.

SUMMARY, CONTINUED

9. Maintain capacity to respond to emerging community needs.
10. Pursue entrepreneurial initiatives.
11. Address unfunded liabilities.
12. Selectively recover costs: On a selective basis, have those who use a service pay the full cost.
13. Recognize the connection between the operating budget and the capital budget.

CONTINUOUS IMPROVEMENT

1. At all times, maximize efficiencies while achieving community values.
2. Involve citizens in financial decisions.
3. Update the Long Term Financial Strategy annually.

THE GUIDELINES

- I. What should the City do every year, whether the financial forecast is positive or negative?
 - C. Increase operating cost recovery.
 - D. Pursue cost sharing.
- II. What should the City do in the following year's budget when the financial forecast is positive?
 - A. Assess the situation.
 - B. Maintain adequate reserves.
 - C. Use one-time revenues only for one-time expenses.
 - D. Use recurring revenues for recurring costs OR for one-time expenses.
 - E. Stay faithful to City goals over the long run.
 - F. Think carefully when considering revenue cuts.
 - G. Think long term
- III. What should the City do in the following year's budget when the financial forecast is negative?
 - A. Assess the situation.
 - B. Use reserves sparingly.
 - C. Reduce services.
 - D. Continue to think carefully when considering tax increases.

BACKGROUND

OLYMPIA FACES A PROBLEM

The City of Olympia is experiencing a widening gap between growth in revenues and growth in expenditures. In 1998 the City Council asked, "Why is this happening?" Is this just a temporary condition? Or is this a sign of fundamental weaknesses in our system of governance? Is the problem caused by limits on the City's ability to raise needed revenues? Is it because of escalating service obligations (or desires)? Is it some combination?

The Council's one major goal for 1999 was to address this issue by developing this Long Term Financial Strategy. They set certain parameters. They would not re-hash the policies for Olympia's future that are set forth in the Comprehensive Plan. The cost of the effort would be limited to no more than \$100,000. They would complete it during 1999, in time to provide direction to the year 2000 budget. It would be a Council-driven policy-setting exercise, not a staff project. It would include a focused public involvement process.

The project began with an analysis of the nature of the problem. The City examined recent and long-term trends of revenues and expenditures. Considering both inflation and population growth 1993-1998, the City is slowly losing ground. Population has grown 7.0%, while spending has grown 6.7% and revenues only 5.3% in inflation-adjusted dollars. Looked at on a per capita basis, the City has held the line on spending, but revenues still have not quite kept up.

By early 1999 it was clear that it would become increasingly challenging to maintain the City's current high service standards, meet the growing obligations of a growing community, as well as further improve our quality of life. Olympia's five-year financial forecast projects a growing gap between resources and needs. The gap may be nearly \$5 million annually by 2004.

Why do we have this projected gap? Basically, growing population, service demands, and unfunded mandates handed down by the state or federal government¹ are causing expenditures to grow rapidly. The City must also respond to emerging needs, such as replacing the Fourth Avenue Bridge. Meanwhile, lagging personal incomes and legal limitations on revenues (e.g., Referendum 47 and Initiative 695) ensure only slow growth in city resources. (See Appendix B: Review of Systemic Issues.)

¹Some examples include stricter drunk driving laws, added juvenile justice requirements, and new requirements for mandatory jail time. In the last five years, Olympia's budget for incarceration costs has doubled.

PURPOSE OF THE LONG TERM FINANCIAL STRATEGY

The Long Term Financial Strategy (LTFS) is an approach to sustaining high quality services, setting priorities, and making them happen. Its focus is on the General Fund Operating Budget, though it recognizes the link with the Capital budget – general fund dollars are also spent on capital projects, and capital projects also have operating costs. It does not include the utilities budget, though there is a link there as well, through the utility tax. Its purpose is to look forward five to six years and provide guidance to the annual budget process.

The LTFS helps identify how the public's money will be managed. The Key Financial Principles and the Strategy Guidelines will be instructive in years when the financial forecast is positive, as well as when the financial forecast is negative. It will also be useful in dealing with other financial matters such as unanticipated funding requests.

The Long Term Financial Strategy also helps inform the public about the City Council's priorities and the approach that will be used to manage the City's resources.

HOW THE STRATEGY WAS DEVELOPED

The Council worked on the LTFS in a series of work sessions throughout the year. Most were four hours long, on evenings devoted solely to this topic.

The first work session was held March 18. The Council shared with each other their desired outcomes and issues for the project. Staff provided forecast of projected revenues and expenditures to the year 2004. Staff also analyzed the systemic difficulties that indicate a growing gap between revenues and service costs. Finally, the Council identified their key future priorities for the coming years: projects or services they felt it was critical for the City to do – or do more of – in the next six years. They did not prioritize this initial list.

CHRONOLOGY OF EVENTS

- March 18: Financial Forecast
Systemic Issues
Top Future Priorities, part I**
- May 6: Revenue Options
Potential Service Cuts, part I
Key Financial Principles
Public Involvement Plan, part I**
- June 16: Public Involvement Plan, part II
Top Future Priorities, part II
Potential Service Cuts, part II
Questionnaire Topics**
- July-Sept: Meetings with Small Groups
Opinion Survey
Public Open House**
- Oct. 5: Review Public Feedback**
- Oct. 12: Direction for Draft LTFS**
- Nov. 11: Review Draft LTFS**
- Jan. 11, 2000: Approve Final LTFS**

The second work session was May 6. Staff updated the Council on financial trends. Staff also provided analysis of the City's possible sources for revenue increases, such as higher user fees and unused taxing authority. Council reviewed potential ways to increase revenues, and decided to leave all sources on the list for the time being, awaiting public feedback before removing any from further consideration. Next they considered the broad range of City services and their costs, as well as potential areas for service cuts. The Council added some areas to the list to examine for potential cuts, and removed others from further consideration. They identified Key Financial Principles to use in setting priorities and funding projects and services. Finally, they outlined the public involvement process to incorporate into the LTFS project.

At the third work session on June 16 the Council received another financial update, then focused on public involvement. They trimmed the list of top future priorities, and reaffirmed the Key Financial Principles. They further refined the list of potential service cuts. Finally, they determined questions on which they wanted public feedback, and the process for getting it. Council also began discussing the form the final LTFS document might take.

During July, August, and September the Council engaged in dialogue with the public about the LTFS. Meetings were held between council members and business groups, environmental groups, neighborhood associations, city advisory boards, and others. On September 16 the Council held an open house for the general public, which was rebroadcast on cable television.

Along with newspaper coverage, the City placed a full page ad with background information and a survey for readers to clip and send in. The survey was also directly distributed to the small groups of stakeholders in their meetings, and to any who asked for it, including city employees. Nearly 400 surveys were returned. About half were from the newspaper, and half from the direct distribution. Respondents offered their opinions on:

- ◆ which current city services were most (and least) important to them;
- ◆ where to look first for potential service cuts;
- ◆ which future priorities were most (and least) important to them;
- ◆ most (and least) preferred strategies for balancing the budget; and
- ◆ most (and least) preferred ways to raise revenues.

On October 5 the Council reviewed survey responses and reviewed the messages they had been hearing at the small group discussions, in the open house, and in the community.

On October 12 the Council reviewed a detailed outline for the Long Term Financial Strategy, including proposed guidelines for budget decisions during prosperous years, and for budget decisions during lean years. The Council gave direction for a preliminary draft document, for their review at their November 11 budget work

session. At that work session they gave final direction for revisions to the draft document. The final document was adopted early in the new millennium, January 11, 2000.

HOW THE STRATEGY IS TO BE USED

The Long Term Financial Strategy is not intended to be a "blueprint" or a substitute for the annual budget. It is a "strategy" which in the first year will be used to evaluate and make decisions about the Year 2000 Budget.

In future years the Long Term Financial Strategy will be updated as part of the mid-year budget work session. At that point the City Council provides direction to the City Manager on preparing the next year's budget. Updating the Long Term Financial Strategy will include an update of both the multi-year and one-year financial forecast. It will be a chance to review and confirm or change priorities, assess future costs required to sustain the current service level, and address unfunded liabilities.

The key for the Long Term Financial Strategy is that it provides a multi-year perspective when making short term decisions, especially in the annual Budget.

Every year the City Council will need to make budget decisions that account for current circumstances. In order to achieve long-term goals, these annual decisions must be made in the context of sound practices of city financial management. These practices are the foundation of the Long Term Financial Strategy. They consist of two parts: 1) the *key financial principles* for the Council's annual budget decisions, and 2) a commitment to *continuous improvement* in the effective management of the City's resources.

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9. **Maintain capacity to respond to emerging community needs.**
10. **Pursue entrepreneurial initiatives.**
11. **Address unfunded liabilities.**
12. **Selectively recover costs:** On a selective basis, have those who use a service

pay the full cost.

13. **Recognize the connection between the operating budget and the capital budget.**

CONTINUOUS IMPROVEMENT

At the core of the City's Long Term Financial Strategy is a continuing commitment to wisely manage public funds. That commitment is carried out through the City's continuous improvement efforts, which have yielded significant cost-savings over the past several years. Achieving continuous improvement has several components:

- I. **At all times, maximize efficiencies while achieving community values.**

Beginning in 1992, the City committed to doing an in-depth efficiency review of at least two major programs or services each year. The 1992 effort included evaluating the City's entire Solid Waste Collection program, including recycling. Later efficiency assessments have included the jail/court system, building energy efficiencies, the engineering permit process, information systems staffing levels and project prioritization, and janitorial services. Each review has resulted in savings of time or money for the City, as well as improved service delivery to the public.

Also, each year City employees track and report other improvements in the efficiency of City operations. In 1999 that list included nearly 90 different program or service changes that resulted in significant efficiencies for the community.

These efficiency improvements have enabled Olympia to hold the line on per capita expenditures while improving and expanding city services to meet the City's growing and evolving needs. To maximize efficiencies while achieving community values, the City will:

- A. **Continue program assessments (e.g., "performance auditing").**
 1. **Continue to pick two programs to focus on each year.**
 2. **Continue to pursue operational efficiencies and document them in the annual budget.**
 3. **Pursue steps toward performance measurement (benchmarking).**
- B. **Pursue comparison with other organizations for "best practices" for both efficiency and effectiveness.**

- II. **Involve citizens in financial decisions.**

Difficult budget decisions involve hard choices among competing needs. It is the responsibility of the Council to make these decisions based on the values of the community. Olympia benefits greatly from the active involvement of citizens in discussing the array of policy issues facing the community. The City will continue to provide opportunities for citizens to share their views with the Council on:

- A. Setting budget priorities; and
- B. Selecting strategies to achieve the priorities.

Some public involvement will be needed near the middle of the year, so the Council has citizen feedback prior to giving the city manager direction for preparing the draft annual budget. Once the draft budget is released, additional opportunities for comment will be provided.

III. Update the Long Term Financial Strategy annually.

The Long Term Financial Strategy is partly a solid foundation, and partly a moving target. The principles and guidelines for wise management of public resources are the solid foundation. But the evolving community needs and financial forecasts provide a moving target. Consequently, the City must update the LTFS annually:

- A. Update the long-term financial forecast.

The City's revenue sources are a mix of the stable (e.g., federal and state shared revenues) and volatile (e.g., sales tax). Likewise, the City's service obligations are constantly evolving as the community grows, and the state and federal governments assign new responsibilities to the City. Even without changing service obligations, inflation impacts the City budget just as it impacts household budgets. Sound financial planning requires the City to do its best to anticipate long term trends, always looking five to six years into the future.

- B. Update the next year's financial forecast.

This is a normal part of the budget process. This will be done in mid-year as the Council sets direction for the draft budget, and in the fall, as part of the final budget decision-making.

- C. Confirm or revise priorities.

Over time, some goals will be accomplished and can be checked off the list. New ones will emerge. Others will be on-going. Many will require a dedicated effort over many years to be realized.

The Long Term Financial Strategy *guidelines* will help the Council make budget decisions that 1) maintain high quality City services, and 2) advance toward long-range goals – through both good times and bad. The most effective way for the City to achieve its long term goals will be to make financial decisions as in the context of a strategy that adjusts to changing conditions. Thus guidelines are organized into three groups:

- ◆ Actions to take as a standard operating approach;
- ◆ Actions to take when the financial forecast is positive; and
- ◆ Actions to take when the financial forecast is negative.

A "positive" financial forecast is defined to mean that enough revenue is anticipated to 1) meet increased costs to sustain the current service level and 2) address unfunded liabilities identified by the City Council. A "negative" financial forecast is defined to mean there is not enough revenue.

I. WHAT SHOULD THE CITY DO EVERY YEAR, WHETHER THE FINANCIAL FORECAST IS POSITIVE OR NEGATIVE?

A. Increase operating cost recovery.

Cost recovery means charging those who use a service to pay at least a portion of the public cost for that benefit (i.e., user fees). It is also a way of metering both supply of and demand for services. Cost recovery is a preferred way of raising revenue since it applies to those who use the service and does not pass on public cost to those who do not use the service. By charging fees to service users, scarce public dollars can be used to sustain existing programs or to help support future priorities.

Toward greater cost recovery, the City will:

1. Review and determine which services are or are not recovering the full cost of providing them.
2. Decide by policy what the appropriate cost recovery percentage should be for each.
3. Decide by policy whether cost recovery should include indirect and overhead costs for each.
4. Determine what, if any, special circumstances exist that bear upon cost recovery for each such service. Examples include ability to pay (e.g., recreation services for low income children), or whether there is some general benefit to the public as a whole (e.g., providing free pre-submission conferences for developers to identify problems early).

B. Pursue cost sharing.

Another way to address the City's long term financial needs is to share the responsibility for particular services with other agencies or parties. While this approach depends on the willingness and ability of others to accept responsibility, it calls for Olympia to assess its role in providing services that benefit others.

The public has suggested some examples of services to assess. They include the Capitol Shuttle, community events, and downtown sidewalk sweeping.

II. WHAT SHOULD THE CITY DO IN THE FOLLOWING YEAR'S BUDGET WHEN THE FINANCIAL FORECAST IS POSITIVE?

A. Assess the situation.

Determine whether the situation is short-term or long-term.

1. If it is a short term condition, treat added revenue as one-time only.
2. If it is likely to be a long term condition, determine how much of the added revenue can reasonably be considered recurring.

B. Maintain adequate reserves.

1. Ensure reserves are adequate to meet the City's reserve policies
 - a. 10% General Fund emergency reserve
 - b. Additional reserve to respond to probable demands or opportunities of an uncertain magnitude (e.g., storm damage or grant matching funds)
2. If not adequate, increase reserves

C. Use one-time revenues only for one-time expenses.

One-time revenues are "windfalls." They are not a reliable source for capital projects or services that require on-going funding. Relying on windfalls would undermine the City's ability to sustain current service levels in the future, or take away money needed to fund the Council's most important future priorities.

1. DO:
 - a. Bank the revenue for a designated future need (e.g., a new bridge)

- b. Temporarily speed up progress toward long term goals (e.g., speed up pavement repair schedule)
 - c. Fund *one-time* expenses, either capital (e.g., park improvements) or services (e.g., police accountability study)
- 2. DO NOT:
 - a. Restore, expand, or add new on-going programs if the long-range forecast shows that the positive revenue situation cannot be sustained
 - b. Reduce on-going tax rates based on a one-time windfall
- D. Use recurring revenues for recurring costs OR for one-time expenses.

Examples:

- 1. Use for one-time expenses (either capital or services) temporarily, until the revenue is needed for recurring expenses (e.g., use utility tax for bike lane construction until it is needed for maintenance of new parks)
 - 2. Use for debt service for a capital project (e.g., a library)
 - 3. Use for expanded service levels (e.g., improved community oriented policing)
 - 4. Bank the added revenues to provide for future needs (e.g., start building a fund to reduce the budget impact of future expansion of medic services to Lilly Road)
- E. Stay faithful to City goals over the long run.
- Set goals for service levels and capital projects, and be faithful to them over the long run. Do not use growing revenues to fund *other* new or expanded services, without first determining:
- 1. Revenues will be enough to accommodate the new or expanded services *in addition to*
 - a. sustaining existing service levels (or restoring them, if previously cut), and
 - b. achieving priority capital projects; OR
 - 2. The new or expanded services are more important than existing goals, service levels and/or capital projects (if so, revise the goals or adjust the service levels); AND

3. The new or expanded services are more beneficial to Olympia citizens than tax or fee decreases.

F. Think carefully when considering revenue cuts.

1. Determine whether the positive financial forecast is reliably recurring.
2. Weigh the importance of reducing taxes or fees against
 - a. the ability to sustain services, and
 - b. the ability to achieve future priorities.

G. Think long term.

Even with a positive revenue forecast for a single year, the desire to maintain or expand services, or achieve high priorities, may require more revenue than is available. In this case, use the guidelines for a negative financial forecast.

III. WHAT SHOULD THE CITY DO IN THE FOLLOWING YEAR'S BUDGET WHEN THE FINANCIAL FORECAST IS NEGATIVE?

A. Assess the situation.

Determine whether the situation is short-term or long-term.

1. If it is a short term condition, short term solutions such as use of reserves may be most appropriate.
2. If it is likely to be a long term condition, adopt a strategy that can be sustained over time, such as reducing expenses or finding a replacement revenue source.

B. Use reserves sparingly.

1. Use reserves only
 - a. if the condition is short term, OR
 - b. the reserve policy is revised, reducing it below 10%. This would be a one-time use of revenue, and should be used only for one-time costs.
2. Before drawing down the General Fund emergency reserve, ensure there are sufficient other reserves to respond to probable demands or opportunities of an uncertain magnitude (e.g., storm damage or grant matching funds).

C. Reduce Services.

Consider the following when evaluating service reductions to deal with a negative financial forecast:

1. Retain, and *do not cut* core service levels. During 2000, the Council will continue to evaluate and define "core" service levels. (See also the principles for maximizing efficiency, in the section on Continuous Improvement earlier.)
2. DO NOT reduce services "across the board." Rather, focus on specific services for reduction or elimination.
3. Reduce involvement in those services that are better performed by others and which are not Olympia's "niche."
4. Actively seek public feedback when evaluating which services to reduce.
5. In evaluating service reductions, include cost/benefit evaluation. Determine who and how many benefit, compared to the cost of providing the service.
6. Avoid reductions that degrade a service to the level where it is ineffective. Rather, follow the principle that if the City cannot deliver the service well, it will not provide it at all.
7. Start no new or expanded services without sufficient
 - a. on-going added revenue (perhaps generated by the service itself), or
 - b. offsetting reductions in expenses.
8. Make no reductions that would impair contractual obligations, including debt service on outstanding bonds.
9. Make no reductions that would impair the City's credit or bond rating.

D. Continue to think carefully when considering tax and fee increases.

1. Evaluate other alternatives first. Look for the least burdensome approach to making ends meet.
2. In some circumstances, increased taxes or fees may be needed to maintain essential services, or desired by voters to fund a new project. If so, consider the following:
 - a. Take into account the limited ability to pay of those on fixed low

incomes. In a regressive tax system such as in Washington, any increase in taxes or fees could disproportionately burden these people. Minimize such effects. (See also the discussion in Appendix B: Review of Systemic Issues, regarding the inelastic nature of municipal revenue sources in Washington State.)

- b. If possible, link increases in taxes or fees to:
 - (1) specific projects or a specific use such as maintenance of new capital facilities (as was done with the utility tax, dedicated temporarily for bike lanes, then in the long run for future park maintenance), public safety (e.g., 0.1% sales tax for law and justice), etc.
 - (2) the need to preserve basic city services or capital improvements
- c. Consider voter approved bonds or tax overrides for large one-time capital projects, where
 - (1) there is no other funding source,
 - (2) there is an indication of public support, and
 - (3) there is an advocacy group.
- d. Consider using voted bonds for major capital projects so future users will also pay toward the costs. (Though not a tax increase, use of councilmanic bonds also ensures that future users help pay toward costs.)
- e. Consider re-allocating earmarked revenue to address revised priorities (this strategy would not actually be a tax increase, but rather a shift in spending).
- f. Aim for a tax structure that is stable and predictable for the taxpayer. Avoid one that fluctuates widely and is hard to plan for in the household or business budget.
- g. Consider the timelines of other overlapping jurisdictions (e.g., school districts) when planning to propose a bond or tax override to the voters.

SUMMARY OF OPINION SURVEY RESULTS

BACKGROUND

During August and September 1999 the City conducted an informal survey of public opinions. Respondents could identify their affiliations with various groups. The survey was distributed in two ways: 1) as a form published in The Olympian to be cut out and returned, and 2) as a form distributed directly to interested parties. The survey was not scientifically conducted, and should be considered simply a general indication of public sentiment. Respondents were self-selected, rather than randomly selected. Hence they likely are weighted toward people with strong feelings about City programs or City taxes, either pro or con. There is also no guarantee that the respondents live or own businesses in Olympia. Even so, the zip codes of the respondents at least somewhat reflect those of the Olympia population. There were nearly 400 responses. Roughly half the surveys returned were from the newspaper, the other half from the direct distribution.

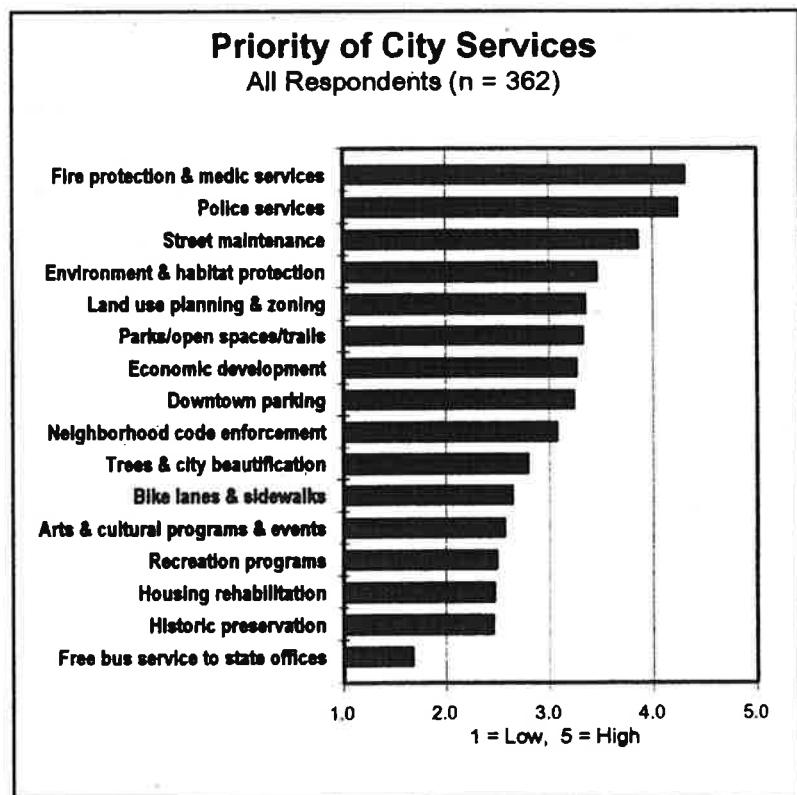
GENERAL OBSERVATIONS

The survey told us respondents value the traditional functions of the City highly: police and fire protection, and provision of basic infrastructure such as streets and parks. They also value the City's environmental quality. Survey respondents told us that these are the places to focus services in the future as well. Not surprisingly, these services account for the vast majority of the City's current budget and work force as well.

Support is greatest for services directed at the broadest segments of the public, and least for those directed at smaller groups of users (e.g., the Capitol Shuttle).

PRIORITY OF CITY SERVICES

The survey asked respondents to identify how important to them were the various City services on a list of broad categories. We converted their responses into an index (five points for "high", three for "medium", and one for "low").



Not surprisingly, respondents put their highest priority on the traditional services of cities: public safety and infrastructure. To this community, environmental quality, land use planning, and parks are also very important. In general, one can see that respondents consider that nearly all City services are important to their quality of life; i.e., of high or medium priority.

How do different groups (neighborhood association members, business owners, advisory board members, and unaffiliated) see these priorities? Police, fire, and street maintenance are in everyone's top five. Environmental protection and parks are in everyone's top half of the list. The Capitol Shuttle is everyone's lowest. Economic development and downtown parking are more important to business owners than to the other groups. Nearly everything is pretty darned important to our advisory board members.

WHERE TO LOOK FIRST FOR CUTS

Given the respondents' service priorities, if the City needed to balance the budget by cutting services, what areas should the City look in first? The City asked this of respondents not so much to identify specific programs to cut, but to get a sense of people's values. This was goal was communicated to respondents.

The detailed list is in the appendix to this document. Different respondents had different priorities, but there was some consistency. What do the different groups think? Five activities show up on the top-ten lists for all the groups: 1) free bus service to State offices, 2) adult sports, 3) City newsletter in the Olympian, 4) tourism advertising, and 5) free services for community events.

FUTURE PRIORITIES

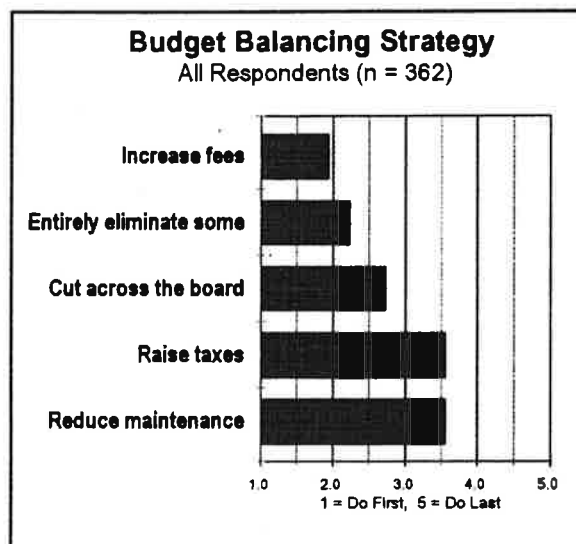
The Council prepared a list of possible new priorities for the City in the next few years. Survey respondents were asked to identify which of them they might consider important enough to support even if they required additional taxes or fees.

Citizens have a very practical bent in their priorities. The first three are basic transportation projects: street repair, the Fourth Avenue Bridge, and a downtown parking structure. Next is maintaining existing public buildings, replacing the aging library we have outgrown, and using technology upgrades and equipment replacement to maintain City efficiency. Not far behind is new police facilities and the city hall they are housed in, and parks and open space for future needs. There is a very close alignment between this order of priority and the initial order of priority indicated by the Council straw vote at their March 18 work session.

BUDGET BALANCING STRATEGY

If the City needed to cut spending or raise taxes or fees, either to balance the budget for existing services, or to free funds to add new priorities, how should they do it? The easiest strategy to carry out would be to trim a little everywhere. But it would run the risk of treating high priority services identically to low priority ones. Or, whole programs or services could be dropped. Or, maintenance spending could be reduced, fees increased, or general taxes increased. The survey asked respondents for their favored approach. They were asked to prioritize the five approaches, first through last.

The favorite was increasing user fees to make more programs more nearly self-supporting. This is consistent with the response regarding reducing adult sports program costs.



Cutting all programs across the board was less favored than setting priorities among programs and eliminating some. The favored strategy would be consistent with the Council's Key Financial Principle that the City should eliminate whole programs rather than reduce their funding below levels needed to be effective (i.e., do it well or don't do it at all).

Antipathy to taxes is very high. It pretty much equals reluctance to allow deferred maintenance to harm the existing investment in City roads and facilities.

This order of priority is widely shared

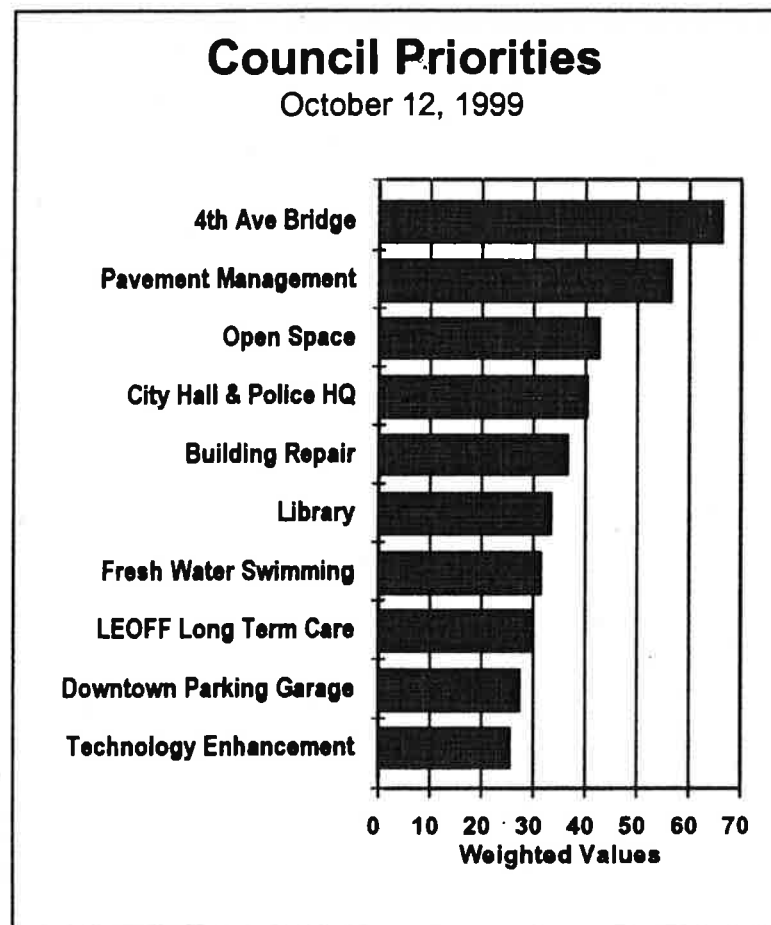
among all the groups.

STRATEGIES TO PAY FOR MAJOR PROJECTS

If the City had to raise revenues or make trade-offs to pay for major projects, which approaches would be preferred? Respondents said clearly (80%) they would want the chance to vote on it. Half the respondents would wish such projects to be funded by cutting current programs. Next was a voted sales tax, then other taxes and fees, then raising the business and occupation tax. Raising the property tax is the least favored.

TOP FUTURE PRIORITIES

In addition to maintaining a high quality of public services, the City must respond to emerging needs. The following are the Council's top ten future priorities as of their straw vote October 12. They are listed in order of priority, weighted according to their importance. Given the City's long term financial constraints, it is likely that only a few of the top priorities can be pursued in the next five to six years.

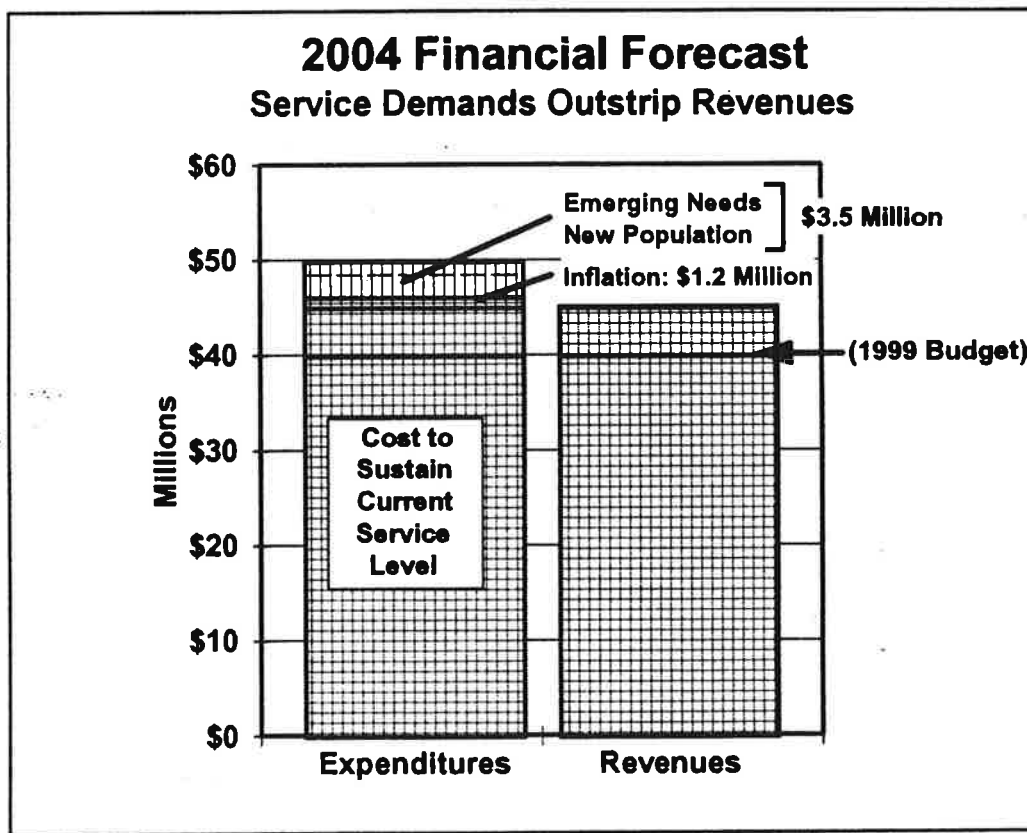


LONG TERM FINANCIAL FORECAST

Part of a long range strategy is developing revenue and expense projections. What will the gap between revenues and expenditures be by the year 2004? What is the cost just to maintain existing services? How big does the deficit grow if we add expenses to maintain current service levels for a growing population, plus a new bridge, increased street maintenance or more open space? We began by projecting where we will be by the year 2004 just to maintain current services.

This methodology does not add any new programs or services. We took the number to maintain existing services and then added the per capita increase. The per capita increase plus the cost to maintain existing services compared to the revenues generates a \$4.75 million gap. The gap creates a "decision zone." Do we cut existing services, raise revenues or change any of these assumptions?

Note: With the passage of Initiative 695, there will need to be a substantial reexamination of the forecast. This will have to take place during 2000. The Year 2000 budget forecast reflects loss of Motor Vehicle Excise Tax (MVET) funds, but subsequent years in the following table do not show the loss of MVET or retarded growth in other revenues.



LONG TERM FINANCIAL FORECAST

Population Estimate 39,070 40,210 41,075 41,940 42,805 43,670 44,535

Summary of Projected Expenditures Governmental Funds

	1998 Budget	1999	2000 Forecast	2001	2002	2003	2004
Salaries	\$20,225,699	\$21,088,687	\$21,721,348	\$22,844,729	\$23,530,071	\$24,235,973	\$24,963,053
Personnel Benefits	\$4,317,684	\$4,484,815	\$4,619,359	\$5,081,941	\$5,234,399	\$5,391,431	\$5,553,174
Supplies	\$1,486,744	\$1,611,106	\$1,667,495	\$1,706,802	\$1,766,540	\$1,828,369	\$1,892,362
Other Services & Charges	\$5,485,703	\$6,113,184	\$6,479,975	\$6,193,631	\$6,565,249	\$6,959,164	\$7,376,713
Intergovernmental Services	\$1,860,290	\$2,091,855	\$2,146,448	\$2,194,458	\$2,254,181	\$2,426,890	\$2,391,159
Interfund Payments	\$1,865,160	\$1,961,149	\$2,078,818	\$2,209,216	\$2,341,769	\$2,482,275	\$2,631,212
Capital Outlay	\$17,000	\$24,920	\$50,000	\$50,000	\$50,000	\$50,000	\$50,000
Debt Service	\$2,256,596	\$1,662,360	\$1,402,206	\$975,000	\$900,000	\$900,000	\$479,955
Operating Transfers Out	\$835,064	\$875,598	\$875,000	\$875,000	\$875,000	\$875,000	\$875,000
TOTAL	\$38,349,940	\$39,913,674	\$41,040,649	\$42,130,777	\$43,517,209	\$45,149,102	\$46,212,627

Summary of Projected Revenue

	1998 Budget	1999	2000 Forecast	2001	2002	2003	2004
Taxes	\$27,499,331	\$28,043,530	\$28,604,401	\$29,374,636	\$29,962,129	\$30,561,372	\$31,172,599
Licenses & Permits	\$877,250	\$980,176	\$1,024,284	\$1,642,698	\$1,716,620	\$1,793,868	\$1,874,592
Intergovernmental	\$2,546,712	\$2,491,261	\$2,500,000	\$2,633,296	\$2,633,296	\$2,633,296	\$2,633,296
Charges for Services	\$5,087,377	\$5,815,055	\$6,047,657	\$6,329,519	\$6,582,700	\$6,846,008	\$7,119,848
Fine & Forfeit	\$577,000	\$703,500	\$724,605	\$736,450	\$758,544	\$781,300	\$804,739
Interest Earnings	\$393,750	\$386,070	\$350,000	\$350,000	\$350,000	\$350,000	\$350,000
Other Revenue	\$935,856	\$1,026,090	\$1,046,612	\$986,162	\$1,005,885	\$1,026,002	\$1,046,522
Use of Fund Balance	\$432,664	\$467,992		\$42,052,761	\$43,009,173	\$43,991,845	\$45,001,596
TOTAL	\$38,349,940	\$39,913,674	\$40,297,559	\$42,052,761	\$43,009,173	\$43,991,845	\$45,001,596
Revenues over (under) Expenditures	\$0	\$0	-\$743,090	-\$78,016	-\$508,036	-\$1,157,257	-\$1,211,031
Estimated Cumulative Cost of Growth				-\$868,500	-\$1,750,000	-\$2,640,845	-\$3,540,000
Total Deficit				-\$946,516	-\$2,258,036	-\$3,798,102	-\$4,751,031

REVIEW OF SYSTEMIC ISSUES (Appendix A)

The City of Olympia is experiencing a widening gap between growth in revenues and growth in expenditures. The Budget Committee asked, "Why is this happening?" Is this just a brief rain squall? Will the sun come out again after we finish bailing a wee bit of water from our ship of state? Or is this a sign that our tax system itself has fundamental weaknesses — i.e., our ship has a leak that will not go away until the hole is plugged? Is the problem caused by limits on the City's ability to raise needed revenues? Is it because of escalating service obligations (or desires)? Is it some combination? This issue paper is organized with increasing detail; only true policy "wonks" need read to the very end.

EXECUTIVE SUMMARY

Staff examined recent and long-term trends of revenues and expenditures. Considering both inflation and population growth 1993-1998, the City is slowly losing ground. Population has grown 7.0%, while spending has grown 6.7% and revenues only 5.3% in inflation-adjusted dollars. Looked at on a per capita basis, the City has held the line on spending, but revenues still have not quite kept up.

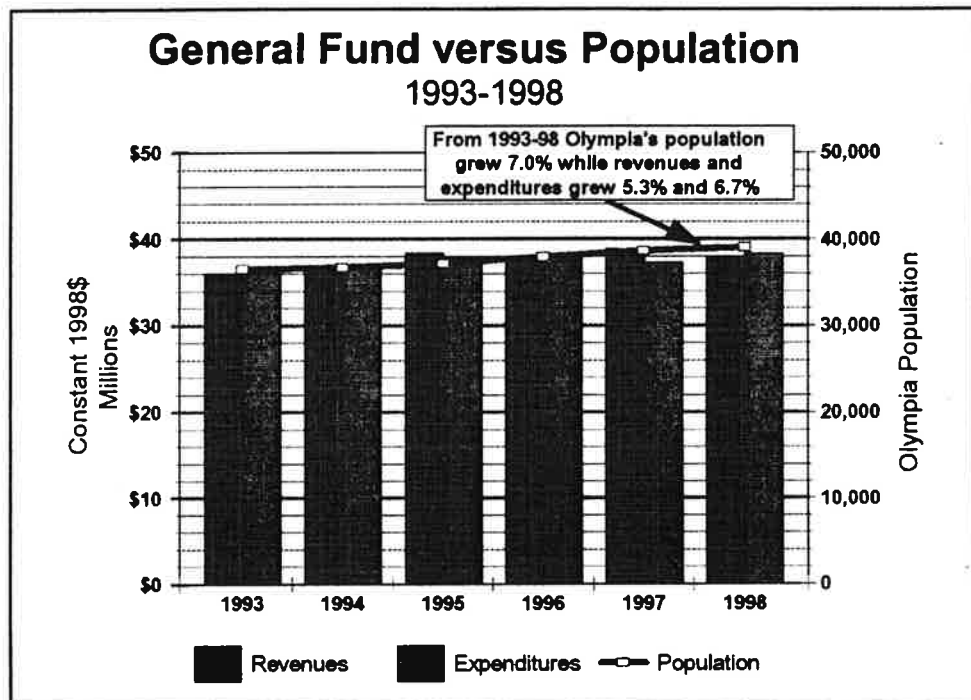


Figure 1

To get a sense of long-term trends, staff analyzed the effect today's tax rules would have had if they had gone into effect in 1985. Because its impacts accumulate with each passing year, by 1998 Referendum 47 would have resulted in \$1.6 million dollars lower collections in that budget year alone. It also puts pressure on cities to encourage growth, since each year's new construction is exempt from the limit on increased collections.

The Budget Committee asked how well Olympia's tax revenues grow with growth in the local economy. Growth in the economy can be measured by growth in total personal income. Since 1990, our total tax revenues have grown only a little slower — 99% as fast as annual total income growth. On a *per-person* basis, however, personal income is slowly growing while tax revenues are slowly falling. This bodes ill for the future. It suggests increasing trouble keeping up with service demands from a growing population.

At the direction of the Budget Committee, staff interviewed ten economists for their opinions on the health of the system by which local governments are funded. They included economists at universities, in government, and in the private sector. Most agreed that there are systemic problems in the limited revenues available to local governments versus the rapidly growing responsibilities. An example would be the trend of imposing limits on revenue generation (e.g., Referendum 47) while at the same time imposing “unfunded mandates” of added service responsibilities (e.g., stricter DUI laws, new juvenile justice procedures, etc.).

Staff was also asked to seek opinions on the proposition that it was (or was not) appropriate for a city's revenues and expenditures to grow along with growth in the local economy, as measured by personal income. On this there was no consensus. Some said yes, it is important for revenues to grow reliably as the local economy grows. Also, as a community's prosperity increases, people expect a higher quality of goods and services. Expectations of their local government rise, just as in other aspects of their lives. In some communities they want more parks, in some more police patrols, in others a higher level of street maintenance, and so on. Other respondents said no, as incomes rise, people need less from their local government, and prefer to see it stick to just the most basic services. They also noted technical limitations in using per capita income as the measure.

BACKGROUND DISCUSSION

RECENT TRENDS IN REVENUES AND EXPENDITURES

Most commonly, people look at the growth in revenues and expenditures in the dollars raised and spent during the year in question. They tend to compare the dollars raised and spent in 1988, for example, directly with the dollars raised and spent in 1998. This is not appropriate. Everyone knows what inflation is, and that the value of a dollar in 1998 is less than what it was in 1988. Hence, the comparison should be made with *inflation-adjusted* — or “constant” — dollars. Otherwise you are comparing apples with oranges. This report uses the Seattle Consumer Price Index (CPI) as the inflation index by which to adjust annual comparisons of dollar amounts. The Seattle CPI most closely reflects the increases in expenses for labor and materials that the City faces.

A realistic comparison also requires consideration of changes in the city’s population. When a new baby enters a household, the family’s responsibilities and expenses grow. The same holds for a community when its population grows. Thus the comparison of spending over the years should be done on a *per-person* — or “per capita” — basis. There are other measures that define the growth in obligations, but this is the easiest to use consistently over

time on an annual basis. Growth in population also brings some growth in revenues, but the revenues may or may not keep up with the population growth.

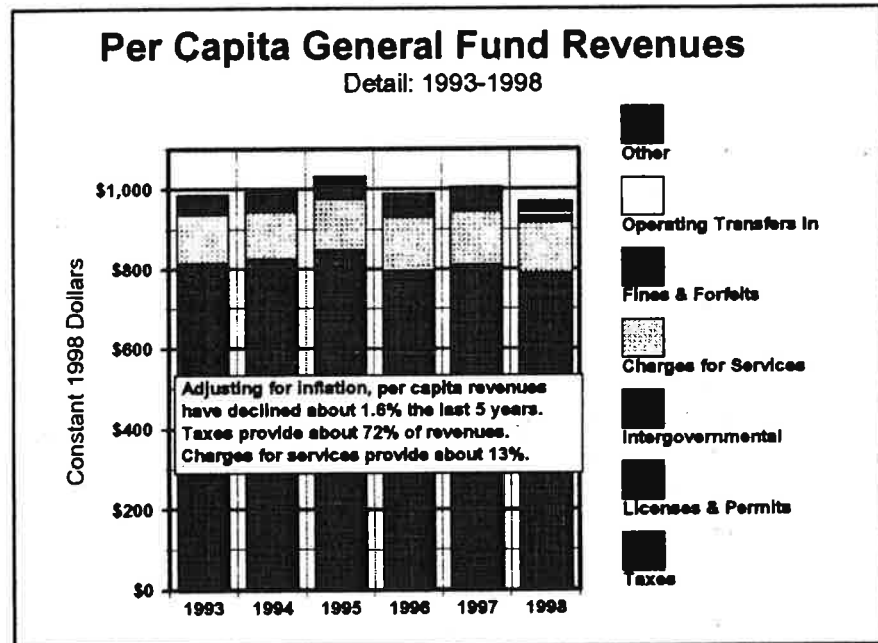


Figure 2

Looking at the trends, Figure 1 shows that Olympia has grown in population by 7.0% from 1993 to 1998. Meanwhile, its General Fund expenditures have grown by 6.7%, and its General Fund revenues by 5.3% on a constant-dollar basis. On a per capita basis, spending has *declined* 0.2%, while revenues have declined still further: 1.6%. Where are the revenues from and what are the expenditures on?

Figure 2 shows that taxes provide about 72% of the revenues. Charges for services (mostly court costs and development review fees) bring about 13%. Intergovernmental transfers — mainly state and federal grants and revenue allocations — account for about 8%, but their share fluctuates, and has been declining.

Figure 3 shows that the City's largest expense is personnel costs: salaries and benefits. This is typical of a government agency, since it is a service industry. Personnel costs have grown from about 60% of the expenditures to 64% over the period. They also have risen slightly faster than inflation. This is not because employees are receiving salary increases above inflation. Olympia's salary levels have

actually grown *slower* than the Seattle CPI, because labor contracts have been based on a blend of the Seattle CPI and the lower U.S. CPI.

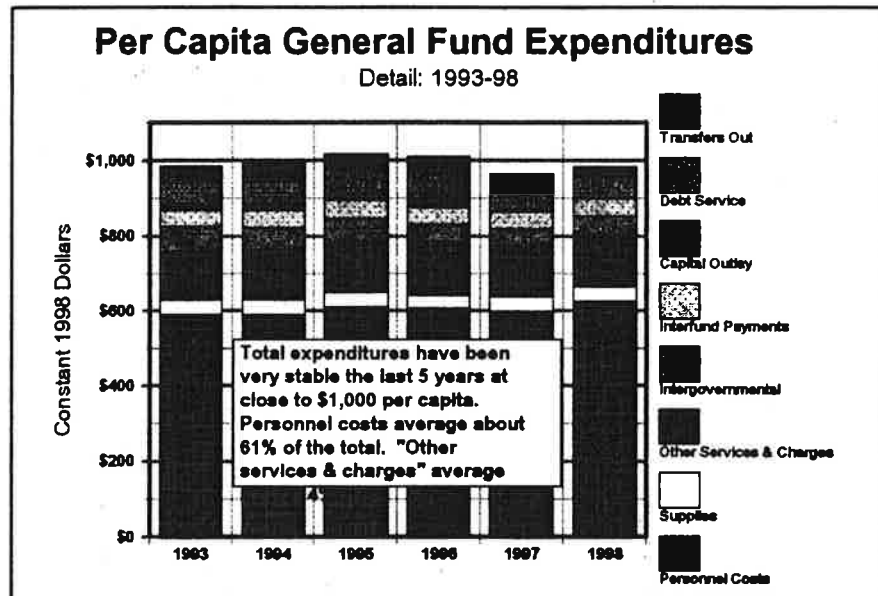


Figure 3

Rather, the growth in personnel costs has come from expanded service levels. Some examples include the Downtown Walking Patrol, transferring several fire fighters from the McLane Fire District to the City, creating the Day Reporting Center for the Municipal Court, increasing park maintenance workers, adding an after-school program for middle school students, and adding a commute trip reduction coordinator.

LONG TERM TAX REVENUE TRENDS

If revenues have fallen behind population growth over the short term, is this merely a momentary experience, or is it part of a long-term trend? To get some idea, we can look at what the City's revenues *would have been* over some historical period if current tax rates and current tax laws had been in effect during the whole time. Again, this must be adjusted for inflation and for population growth.

Cities rely primarily on four major sources of tax revenues: property taxes, sales taxes, utility taxes, and business and occupation taxes. Other taxes account for a small added

amount. These include gambling taxes, admissions taxes and hotel/motel taxes.

There have been several major changes in local government taxing authority over the last 25 years. In 1974 the legislature enacted a lid on local government property tax increases. They limited collections from existing development to a growth rate of no more than six percent over the previous year. Tax collected from new construction could be added to that. In 1982 cities and counties were allowed to increase their sales tax rate from 0.5% to 1.0%; nearly every city and county in Washington did so, including our local ones.

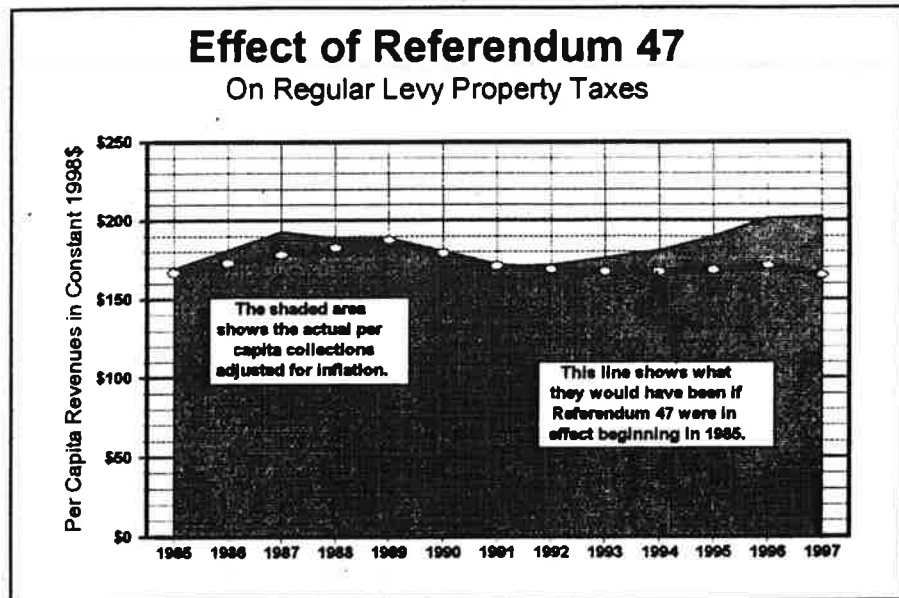


Figure 4

Most recently, Referendum 47 has added another limit on property tax revenues. The effect is shown in Figures 4 through 6. Local governments may increase collections no more than the lesser of six percent or the rate of inflation (unless they declare a special need, by a majority vote of the legislative body). Since the rate of inflation has not exceeded six percent since the early 1980s, local governments can no longer collect as

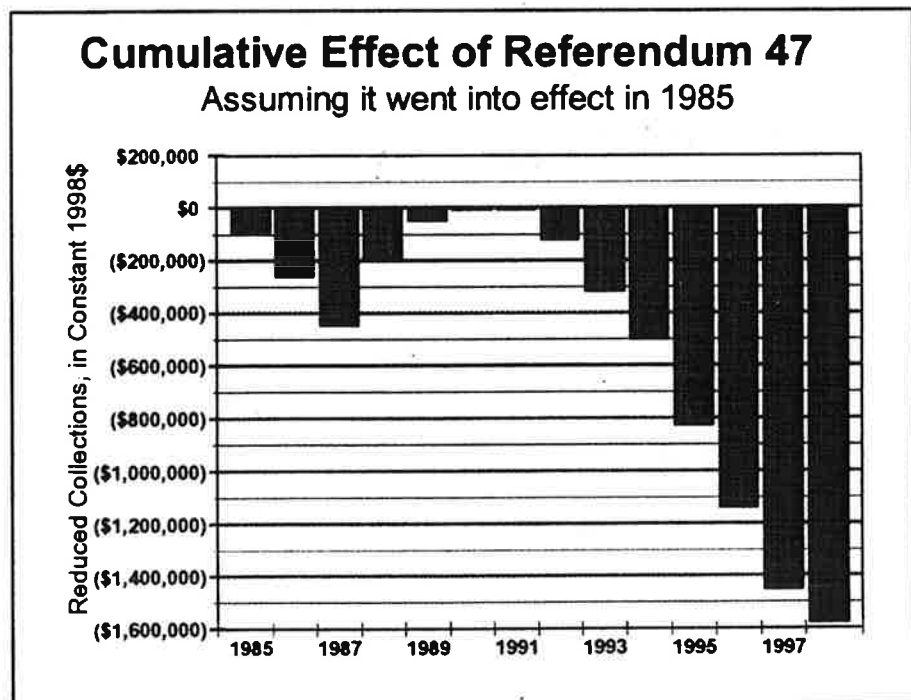


Figure 5

much in property taxes. The effect of Referendum 47 on tax collections is cumulative: each year's tax receipts are limited by those of the previous year. If Referendum 47 had gone into effect in 1985 instead of in 1997, it would have generated a considerable impact by today. In the 1998 budget year alone, the City would have collected roughly \$1.6 million dollars less in property taxes.

The effect of Referendum 47 can be looked at in two ways. Obviously it greatly reduces regular levy property tax collections over time. If property taxes were a small share of City revenues, this might not be so important. But because property taxes are a large share of total tax revenues, the impact is quite dramatic. The cumulative affect of Referendum 47 will be a major factor in future years.

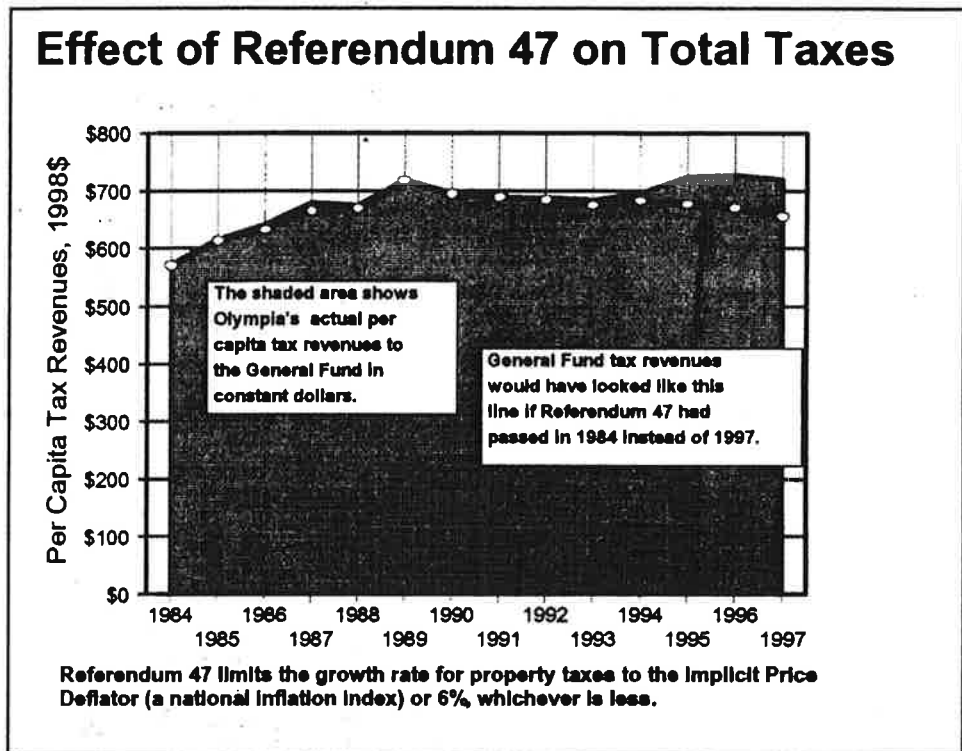


Figure 6

WHAT IS THE "IMPLICIT PRICE DEFLATOR," AND WHY IS IT USED BY REFERENDUM 47?

There are two families of inflation indexes used by economists. The best-known is the Consumer Price Index (CPI). It tracks the changing *price* of a fixed "market basket" of goods and services purchased by a "typical" urban consumer. There are also CPIs for subcategories of goods and services, such as construction or medical costs.

For Referendum 47, the rate of inflation is defined by the less well-known "Implicit Price Deflator" (IPD). The IPD is a national index that takes into account both changes in *prices* and changes in consumer *spending habits*. For example, a rising cost of beef may cause consumers to substitute chicken. The IPD accounts for the switch automatically,

while the CPI does so only through formal periodic revisions. For this reason, many economists consider the IPD a better indicator of changes in the actual cost of living. The IPD is primarily used for analyzing changes in the national economy, such as growth in the Gross Domestic Product, the balance of trade, and so on.

The two indices are typically very similar, since the IPD uses the CPIs for individual commodities (e.g., chicken) to capture the changes in prices. The major drawback to using the IPD is that it is a national index, while inflation is typically experienced differently from one local market to another.

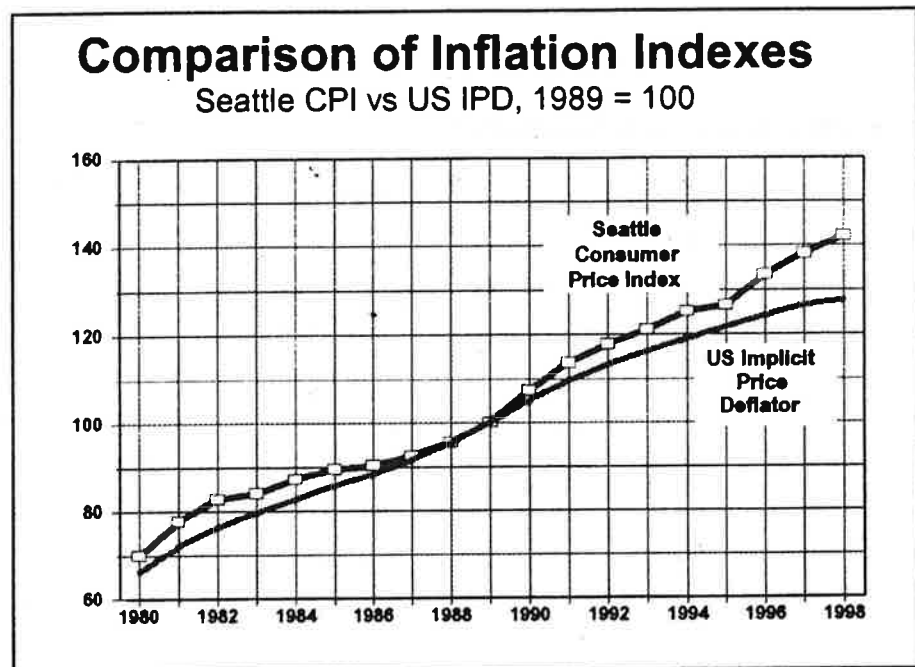


Figure 7

Therefore the CPI is calculated separately for many metropolitan areas, including the Seattle area (since 1915, in fact). Thurston County is included in the area covered by the Seattle CPI data. The Seattle CPI partly forms the basis for cost-of-living adjustments in labor contracts throughout the public and private sectors in western Washington. The IPD may suitably track nation-wide changes in the cost of living, but it does less well at accounting for changes in Olympia's costs of providing services.

Since 1989, the Seattle CPI has risen faster than the national IPD. Our stronger economy has pushed local prices more rapidly upward, particularly for housing.

EFFECT OF GROWTH ON TAX COLLECTIONS

Referendum 47, and the 6% levy lid, limit the total regular levy property tax collections allowed from current development. If, for example, local property values increase by 5% but the IPD only goes up 2%, property tax collections can go up only 2%. Each year's new construction is exempted from the lid. This exemption makes sense, since growth brings with it increased service demands.

But this situation also puts pressure on local governments to encourage growth as one of few available means to increase revenues. Figure 5 shows that for 1990 and 1991 regular levy property tax collections would have been the same with or without Referendum 47. This is because of rapid growth in the property tax base in the years immediately before.

HOW WELL DOES OLYMPIA'S REVENUE BASE TRACK GROWTH IN THE LOCAL ECONOMY?

One commonly-used measure of the size of the local economy is "total personal income" — i.e., the total income to all persons in the community from all sources. The income includes wages and salaries, proprietors' income, interest and dividend income, retirement payments, and so on. When adjusted for inflation, rising total personal income indicates a growing economy.

Due to consumer spending habits and the structure of the local government tax system, rising total personal income in the community may not translate into equivalent increases in tax revenues. Economists use the term "elasticity" to discuss this. If, for example, an X percent increase in total personal income results in an X percent or greater increase in tax revenues, that tax source is defined as having an "elasticity value" of 1.0 or greater. Tax sources with an elasticity of 1.0 or greater are said to be "elastic." Those with elasticity of less than 1.0 are said to be "inelastic."

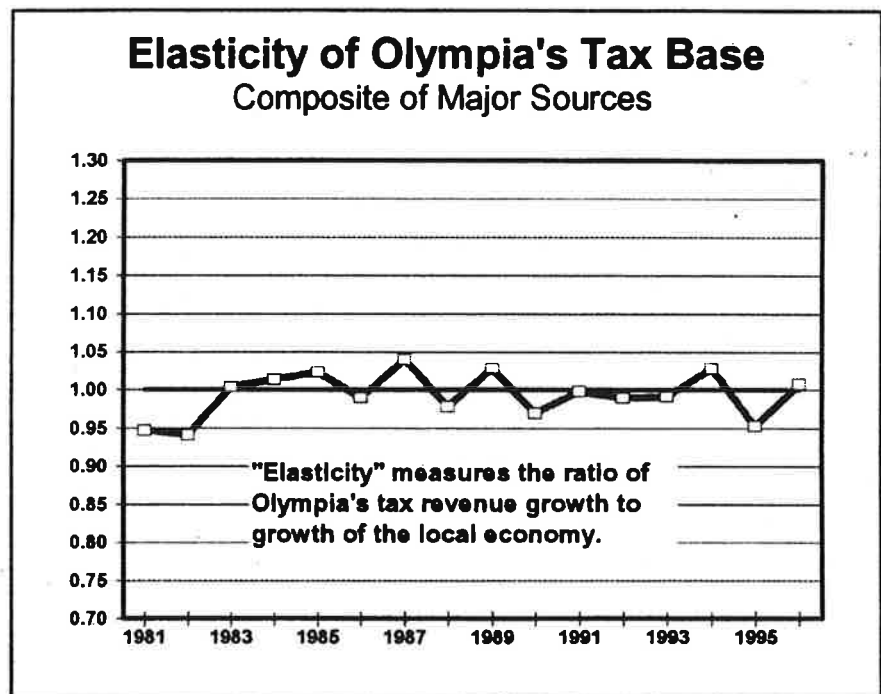


Figure 8

With an elasticity value of .99 for the period 1990-96, Olympia's tax revenue system is only very slightly on the inelastic side. This means that, on average, a 10.0% increase in total personal income for Olympia residents would deliver a 9.9% increase in tax revenues to the City. Though small, this difference compounds over time. If a growing economy leads citizens to have rising expectations of local government services, this

could lead to rising frustration.

Another way to look at this relationship is with “per capita personal income,” the total personal income divided by the total number of persons. This is a measure of economic prosperity. Given today’s tax structure (including Referendum 47), growth in Olympia’s per capita tax revenue during the late 1980s would have roughly paralleled growth in per capita income. Since about 1989, however, per capita tax revenue would have fallen even while per capita income rose. This does not bode well for the future.

COMMENTS FROM ECONOMISTS

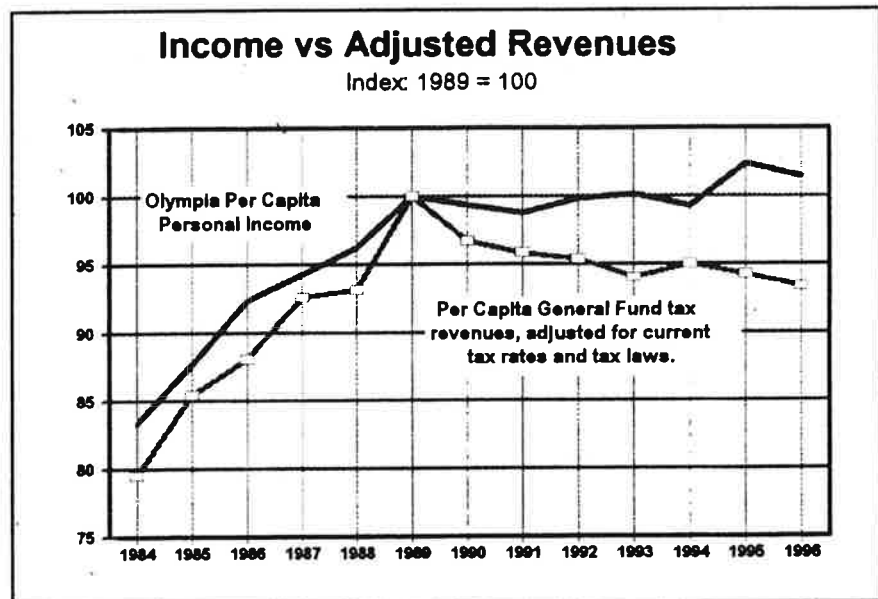


Figure 9

At the direction of the Budget Committee, staff interviewed a variety of economists for their views on the tax system supporting local governments. The basic question we asked of all of them was, “Is there a systemic problem in the revenue system supporting local governments?” We spoke with: Todd Herreid and Rick Judd, Washington Department of Transportation; Bret Bertolin, Washington Office of the Forecast Council; Judy Cox, Municipal Research and Service Center; Richard King, Lehman Brothers, Inc.; Kent Ennis, Arizona Joint Operations and Budget Commission; Miguel Montiel and Lou Weschler, Arizona State University School of Public Affairs; and Larry Gerry of the Public Administration program at The Evergreen State College. In addition, we reviewed several reports on local government finance in Washington.

There was a general consensus that the system of local government finance does have some structural weaknesses, though the scale of the problem is hard to define. One economist observed that municipal revenues almost always tend to fall short of expenditures over time; an indication of people’s unlimited wants compared to limited means. Another noted that it may be difficult for us to establish a tax structure that can handle an increase in service demand for a number of reasons specific to Olympia, including the State as the city’s major employer; property tax exemptions for public lands; and population growth.

Revenues. Gas and property taxes are growing slower than inflation. Property taxes are

limited by a national indicator of inflation, rather than a local one. Gas tax is distributed on a population basis that may or may not relate to need. One economist advises that cities should be “banking” future revenues by authorizing property tax capacity. State shared revenues is another variable to consider. If the state shares revenues based on incorporated city population, but the city provides services to unincorporated areas, there exists a revenue/expenditure imbalance.

Expenditures. Revenues are not keeping up with expenses because unfunded mandates drive up expenses. These mandates are a reflection of the trend, beginning in the 1980s, of shifting the burden of delivering services from the federal level to the state and local levels. Changes in DUI legislation, juvenile justice and transportation costs all impact the expense side of the ledger, but not the revenue. Incarceration rates that seem to rise uncontrollably also dramatically increase costs of the justice system. Labor, welfare, and medical expenses are also increasing faster than inflation.

General Economic Environment. Moody’s and Standard and Poor’s municipal bond rating agencies consider the Washington economy to be the most diverse that it has been in the last 25 years. They believe it will remain strong for the foreseeable future. They recently raised Seattle’s rating to AAA (one of only a dozen US cities with a AAA rating).

SUMMARY OF REPORTS ON LOCAL GOVERNMENT FINANCE

Final Report of the Washington State Local Governance Study Commission, "The Quiet Crisis of Local Governance in Washington." January 1988

The Legislature created the Local Governance Study Commission in 1985. The Commission was charged with analyzing the problems of local governments and making recommendations to the Governor and Legislature for their solution. One of the problems identified by the Commission was that local governments' revenues are not adequate to their service responsibilities.

According to the Commission revenue sources in Washington were stagnating. The federal government had recently eliminated general revenue-sharing and cut back a number of grant programs. The differing economic and political contexts across the state provided local governments with different revenue-raising capabilities. At times, local governments competed with each other to raise revenue from the same sources. There was also a lack of "fit" between revenue sources and service capabilities. Finally, the federal and state governments continued to expect or require local governments to meet high performance standards, but did not always provide financial assistance to do the job.

Governor's Committee on Washington's Financial Future, "Report to the Governor: A Financial Plan for Washington." January 1989

This report examined the state and local government financing system and made a variety of recommendations for tax system reform. It built on the report of the Local Governance Study Commission. Governor Booth Gardner charged his Committee with developing basic principles, values, and long-term financial goals to guide future tax and spending policies. Finally, he charged them with preparing specific tax and spending reform recommendations.

The report includes a substantial analysis of the relationship between the state's economy and its tax system. It notes that "over time, state and local tax collections tend to increase at a rate that approximates the growth in the overall economy... History teaches that the total demand for government services does not significantly decline when the economy is performing well and unemployment is low. The public has come to expect more in the way of public programs as personal incomes rise, particularly for better education programs and infrastructure improvements." (page 6-11)

The report found that the tax system at the time did a poor-to-middling job of tracking economic growth. Elasticity was estimated at 0.85 for state sources, 0.99 for local sources (when special levies are included), and 0.89 for state and local taxes combined.

The Local Government Subcommittee developed four general principles against which they evaluated the then-current tax and spending systems:

- “The respective roles of state and local governments should be clearly defined, adequate revenue sources should be linked to responsibilities at the appropriate service level and, if the state requires local governments to provide certain services, the state must provide reasonably available access to adequate revenues to meet those program requirements.
- “The state should provide a local government tax system which will allow local governments flexibility to generate revenue, including broad local government tax options that allow communities to determine for themselves the type and level of their taxes.
- “For discretionary programs at the local level, the citizens and local government of a community should have flexibility to determine the type and quality of local programs/services and the structure and level of local revenue sources to fund those local programs.
- “For basic government services at the local level, there should be a reasonable amount of local revenue effort and state equalization of local revenues in order to respond to the diversity of local capacity and service needs.”

The Subcommittee concluded: “The current local government fiscal structure does not fare well when measured against these principles. Local government revenue sources are severely restricted” (page 8-8).

Since then the state legislature has provided a number of optional new taxing authorities to local governments, mostly in connection with the Growth Management Act. These include impact fees, increased real estate excise tax, voter-approved sales tax for law and justice expenses, increase in motor vehicle registration fees (counties only), and voter-approved gas tax rider (counties only). On the other hand, the legislature also provided Referendum 47, further limiting property taxes.

SOME TECHNICAL CONSIDERATIONS REGARDING WEALTH vs INCOME DATA

Stock and other assets like property are “wealth” rather than “income” — i.e., dollar revenue to a household. One state government economist cautioned that state personal income data in Washington is distorted by Microsoft and other King county computer industries. Much of this software industry income is converted into “wealth” in the form of housing but not into other disposable income items — hence it would not show up in increased sales tax revenues, though it would affect property tax revenues. The Microsoft wealth is not shared much outside of King and Snohomish counties. Often in these wealthy households, the higher the personal income, the *less* reliance on

government services for schools, parks or personal security.

Another viewpoint: Richard King of Lehman Brothers, Inc. shared a research report of theirs on the role of the “wealth effect” on consumer spending patterns. In particular, the article examines the effect of the stock market boom on consumer spending. This article suggests the contrary — i.e., that increased wealth would have at least some small effect on retail sales and hence tax collections.

In brief, national economic models predict consumer spending primarily based on projections of income and of interest rates. For most people, their wealth is tied up in the family house and car (or cars). An increase in the market value of their home has very little effect on their disposable income spending.

Households in the highest income levels, however, have a larger share of their assets in stocks and bonds. When those assets increase in value, consumer spending by upper income households does increase. This is known as the “wealth effect” on spending. National economic models estimate that for every dollar increase in wealth in the economy as a whole, there is a four-cent increase in consumer spending.

The largest share of the total wealth is held by upper income groups — in 1995, 43% of the nation’s wealth was held by the 9% of family households with annual income of \$100,000 or more. Hence most of the added spending from the “wealth effect” is by that group. That group also puts their added spending toward a different collection of goods and services than would lower- or middle-income family households.

The article suggests that this effect may be evolving in the 1990s. During this decade, the proportion of families holding stocks has grown from about one-third to about one-half. With more families benefitting from the booming stock market, there is evidence that the size of the wealth effect may now be five cents on the dollar instead of four.

This has two implications for using per capita income to evaluate what our revenues “ought to be.” One, per capita income does not take into account the changing patterns of wealth and their potential effects on the revenue base. Two, per capita income might not be a good predictor for sales tax revenues, because it might be *too low*, not too high as suggested by another analyst above. Of course, that would assume that Olympia’s share of wealthy households mirrored national patterns, and that spending by wealthy households in Olympia did the same.

APPENDIX B: OPINION SURVEY RESULTS

BACKGROUND. During August and September 1999 the City conducted an informal survey of public opinions on financing issues. The survey was distributed in two ways: 1) as a form published in *The Olympian* to be cut out and returned, and 2) as a form distributed directly to interested parties. The groups receiving direct distribution included neighborhood associations, City boards and commissions, business owners (such as the Olympia Master Builders and the Downtown Association), and various civic and environmental groups. Most got their copies when Council members visited their group, or from other group members who picked up extras. Individuals could also pick them up at City Hall. City employees were also offered the opportunity to respond. Roughly half the surveys returned were from the newspaper, the other half from the direct distribution.

LIMITATIONS OF THE SURVEY. The survey was not scientifically conducted, and should be considered simply a general indication of public sentiment. Respondents were self-selected rather than randomly selected. Hence they likely are weighted toward people with strong feelings about City programs or City taxes, either pro or con. Questions were not tested in advance to identify possible areas of confusion.

There is also no guarantee that the respondents live or own businesses in Olympia. Respondents were asked their zip code for tabulation purposes. Some reported a zip code for local post office boxes (98507), and some gave no zip code. Some reported zip codes for locations outside Olympia, and some were outside Thurston county, even as far away as Portland. Even so, the zip codes of the respondents at least somewhat reflect those of the Olympia population:

Zip Code	April 1, 1999		Survey	
	Number	Percent	Number	Percent
98501	15,465	39%	117	32%
98502	12,837	33%	81	22%
98503	90	0.2%	10	3%
98506	9,450	24%	58	16%
98512	1,351	3%	18	5%
98516	209	1%	4	1%
Other	0	0%	74	20%
Total	39,402		362	

The data has been analyzed for sub-groups (e.g., business owners) as well as the total.

The data analyzed in this report covers the 362 questionnaires received by September 23. Since then 20 more have been received. Their responses are not included in the totals reflected here; however, they show the same major trends as the others, and would not change the conclusions reported here. No doubt a few more will come in as well. We will add their results later, and the full tabulation will be available to those who wish it.

GENERAL OBSERVATIONS

Although the survey is not reliable to the level of a scientifically designed random sample survey, it provides valuable insights and will be a very useful tool. There is a substantial degree of consistency in the responses to the survey. This consistency increases confidence that the responses are a valid reflection of sentiment among many members of the community. The consistency is both in the responses among different groups, and in the responses to different questions that are related to each other.

The survey tells us respondents value the traditional functions of the City highly: police and fire protection, and provision of basic infrastructure such as streets and parks. They also value the City's environmental quality. Survey respondents are telling us that these are the places to focus services in the future as well.

Not surprisingly, these services account for the vast majority of the City's current budget and work force as well.

Support is greatest for services directed at the broadest segments of the public, and least for those directed at smaller groups of users (e.g., the Capitol Shuttle).

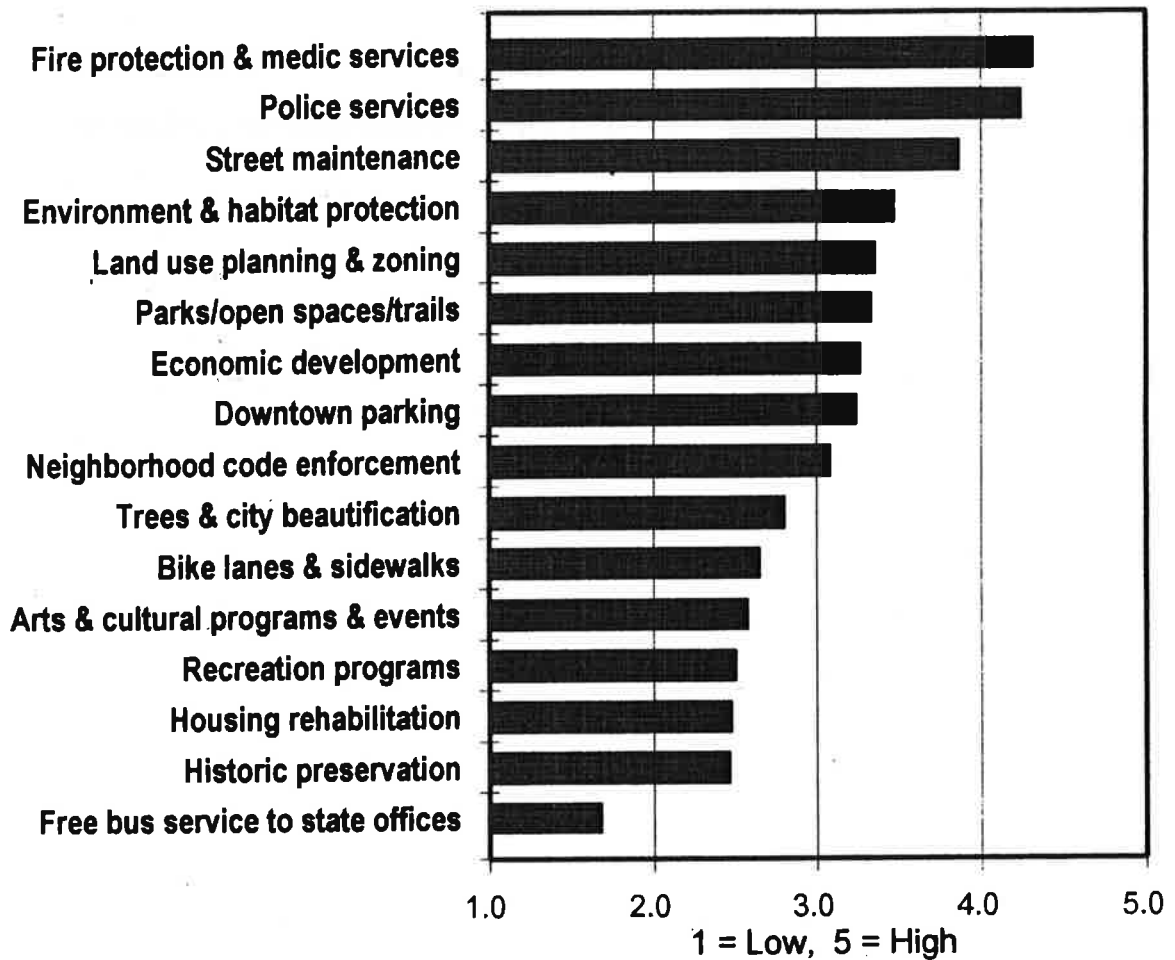
There is a high level of internal consistency of the responses. For example, the Capitol Shuttle, which provides free bus service between State office locations, is identified as a low priority by most respondents, and is favored by most respondents as a service to look at first for cost-saving cuts. Likewise, police and fire services are a high priority, and not generally favored as a place to look first for cost-saving cuts.

PRIORITY OF CITY SERVICES

The survey asked respondents to identify, by broad category, how important to them were the various services provided by the City. They were asked to rate them high, medium, or low. For purposes of this analysis, we converted their responses into an index, with "high" allotted five points, "medium" three, and "low" one. The results appear as follows:

Priority of City Services

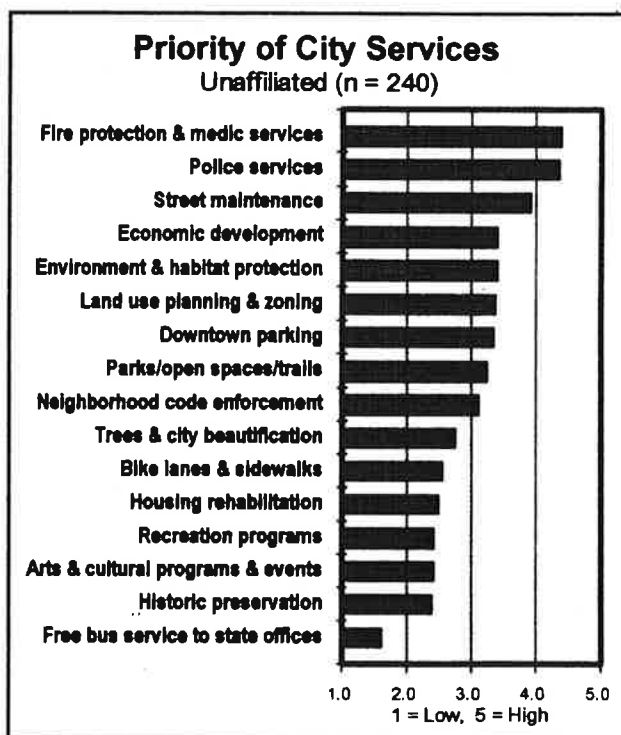
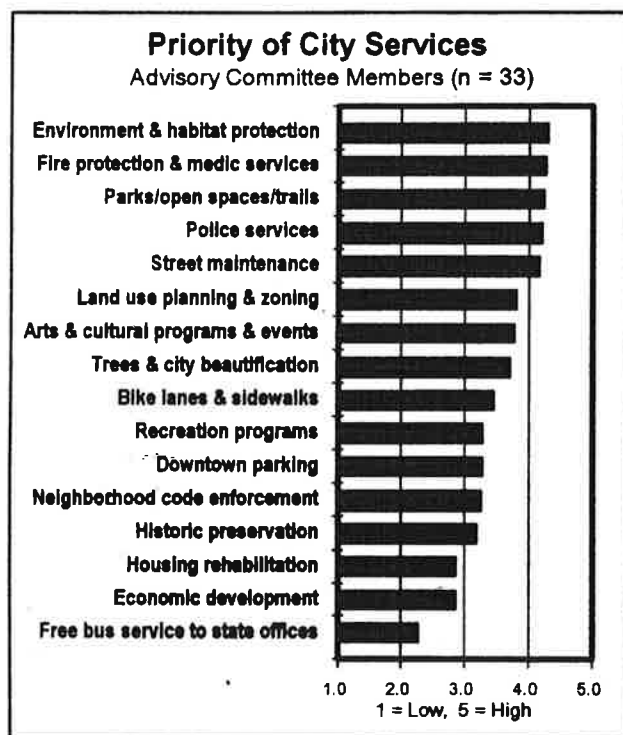
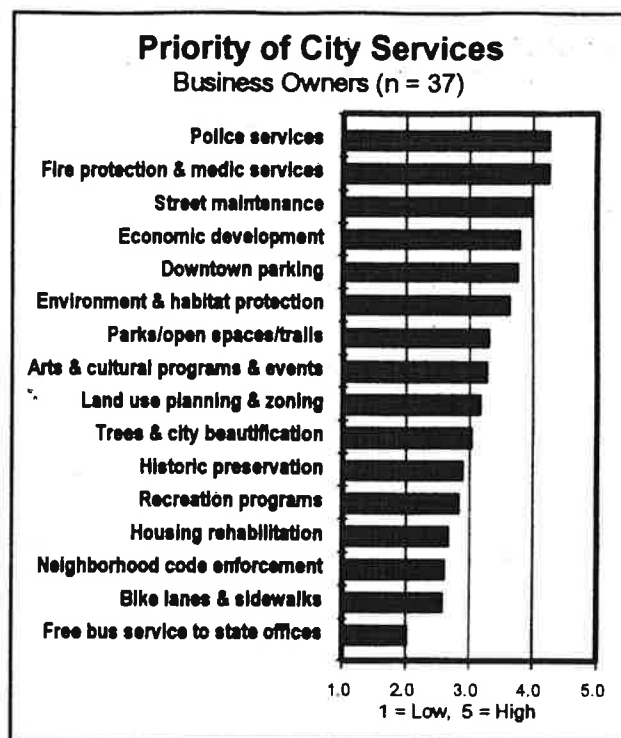
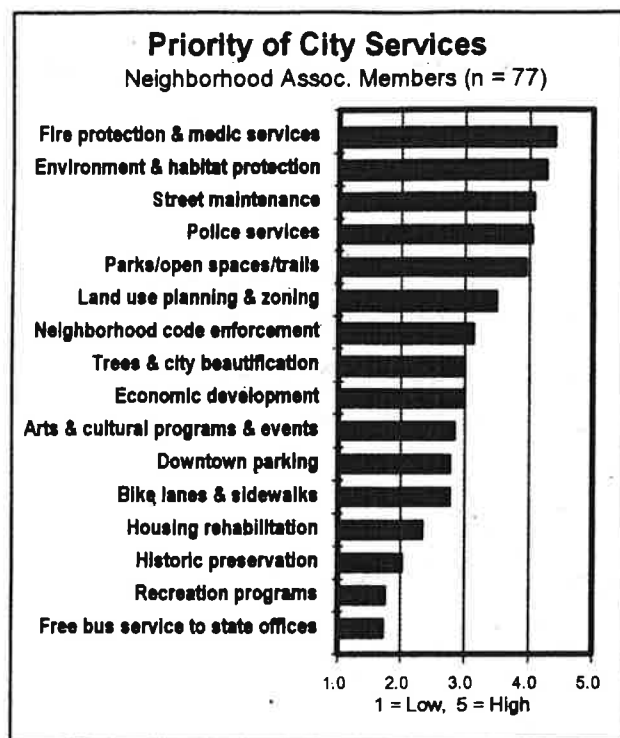
All Respondents (n = 362)



Not surprisingly, respondents put their highest priority on the traditional services of cities: public safety and infrastructure. To this community, environmental quality, land use planning, and parks are also very important. Although economic development is not a primary focus of City programs, it too was ranked above average in priority.

The only service that clearly ranked low was the free Capitol Shuttle. In general, one can see that respondents consider that nearly all City services are important to their quality of life; i.e., of high or medium priority.

How do different groups see these priorities? Are their views similar or different?



Police, fire, and street maintenance are in everyone's top five. Environmental protection and parks are in everyone's top half of the list. The Capitol Shuttle is everyone's lowest. Economic development and downtown parking are more

important to business owners than to the other groups. Nearly *everything* is pretty darned important to our advisory committee members.

There are also some modest surprises. Both arts programs and historic preservation are more important to business owners than to neighborhood association members. These are programs that are very active in the Downtown, and many of the business owners responding to the survey are from the Downtown.

WHERE TO LOOK FIRST FOR CUTS

Given the respondents' service priorities, if the City needed to balance the budget by cutting services, what areas should the City look in first? The City asked this of respondents not so much to identify specific programs to cut, but to get a sense of people's values. This was goal was communicated to respondents. In meetings with interest groups, most people expressed how hard it was to legitimately identify a program for cuts without detailed information about what the program does, who benefits from it, what it costs, and so on.

The list of potential areas to look for program cuts was identified by the City Council in a work session in May. Staff had provided summary information about the wide variety of City programs and services, the costs of each, and the impacts of various levels of cuts. Although it was a mountain of material, it was not the detailed data that would be evaluated at budget-setting time to make final decisions. This information was of course not available to survey respondents, and could influence their choices of priorities. Hence the intention that the responses be used mainly to identify values rather than drive actual commitments to specific program cuts.

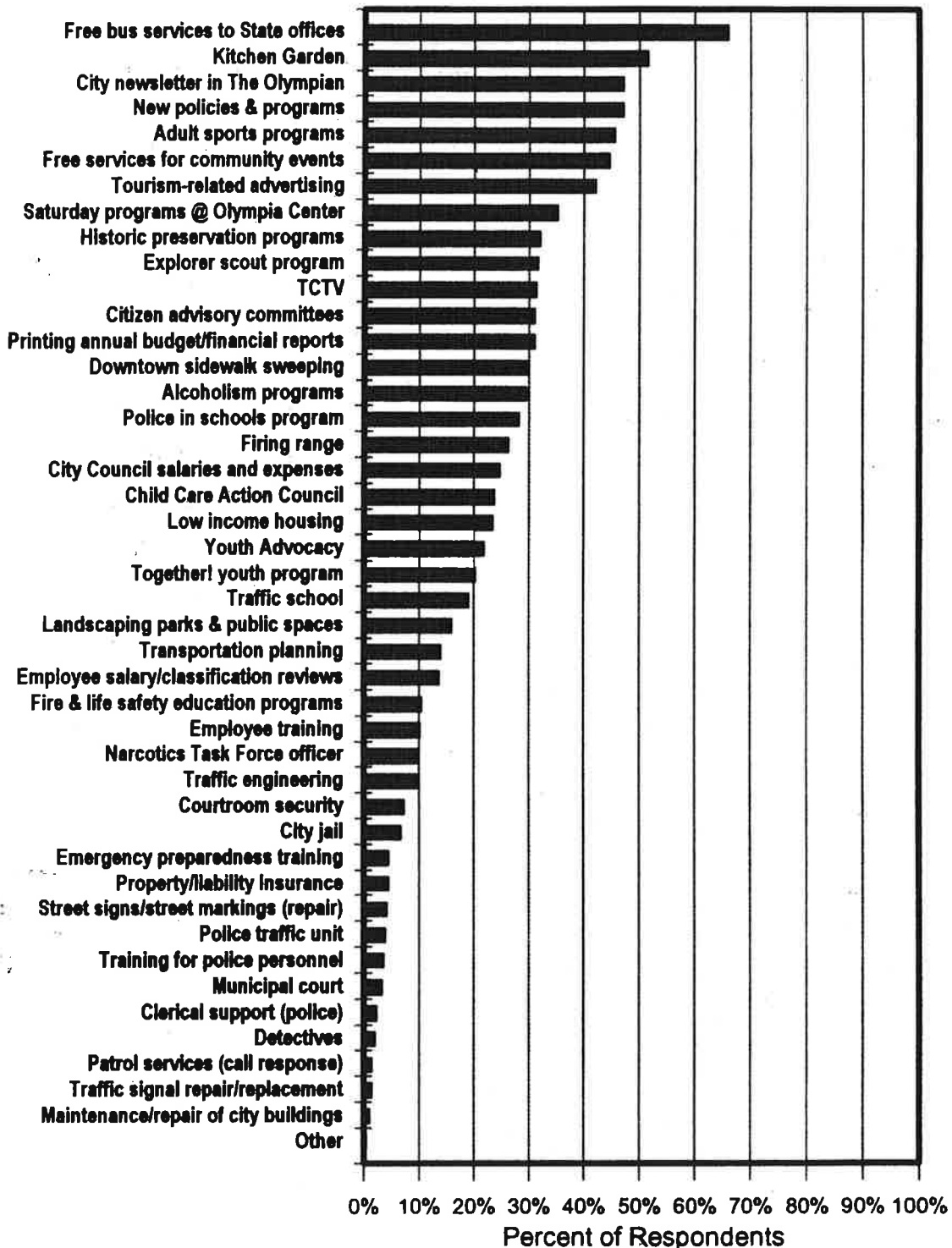
Survey respondents also were encouraged to give ideas relating to cost recovery, such as user fees in particular programs. Some programs on the list represent areas that respondents suggested a higher level of cost recovery. One example: higher fees for adult sports programs could recover a higher proportion of total costs. These fees now recover direct costs, but not indirect ones.

In other cases, feedback from the open house and meetings with interest groups clarifies what the raw data shows. For example, many recommended that the City look at its spending on the City newsletter in the Olympian for cost savings not because of a discomfort with communication, but rather as part of a suggested switch to using a web site on the Internet to perform the function instead.

Following is the overall priority list from all the respondents, and the top ten choices from the different sub-groups.

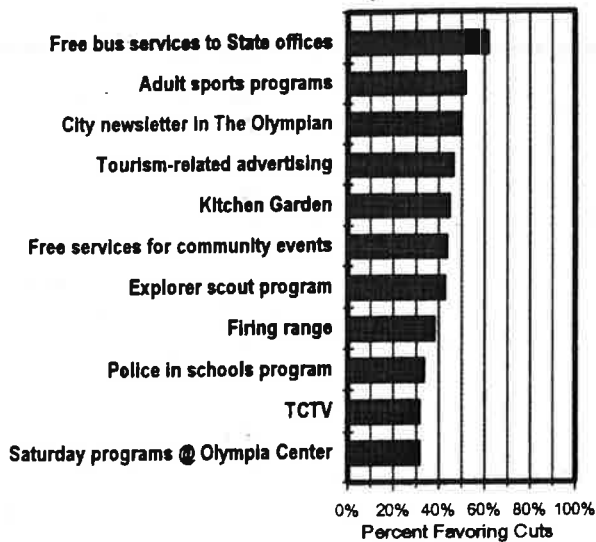
Where to Look for Cuts

All Respondents



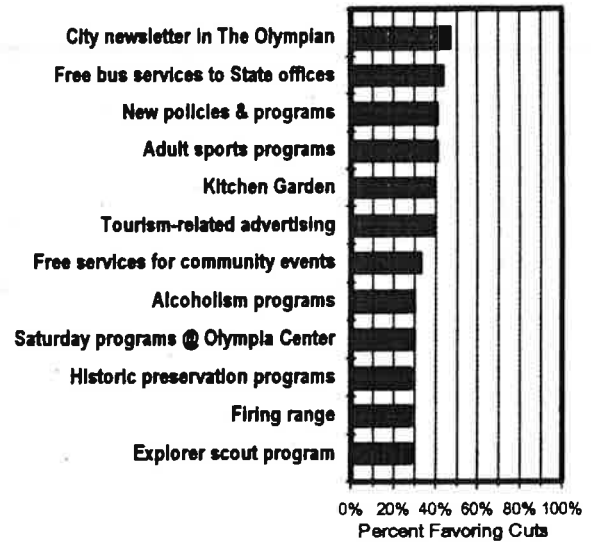
Where to Look First for Cuts

Neighborhood Assoc Members (n = 77)



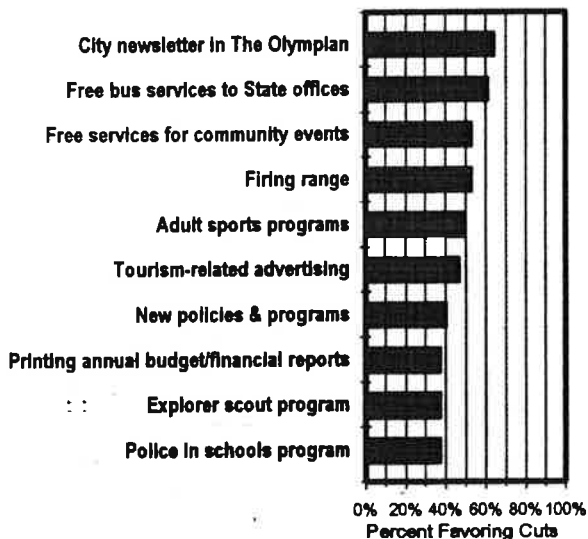
Where to Look First for Cuts

Business Owners (n = 37)



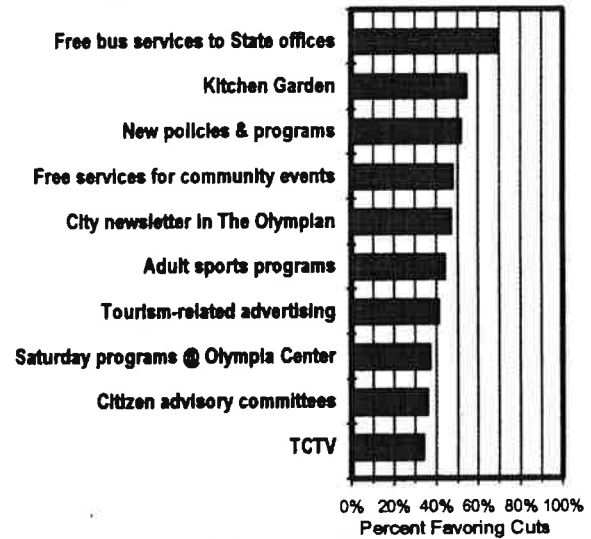
Where to Look First for Cuts

Advisory Committee Members (n = 33)



Where to Look First for Cuts

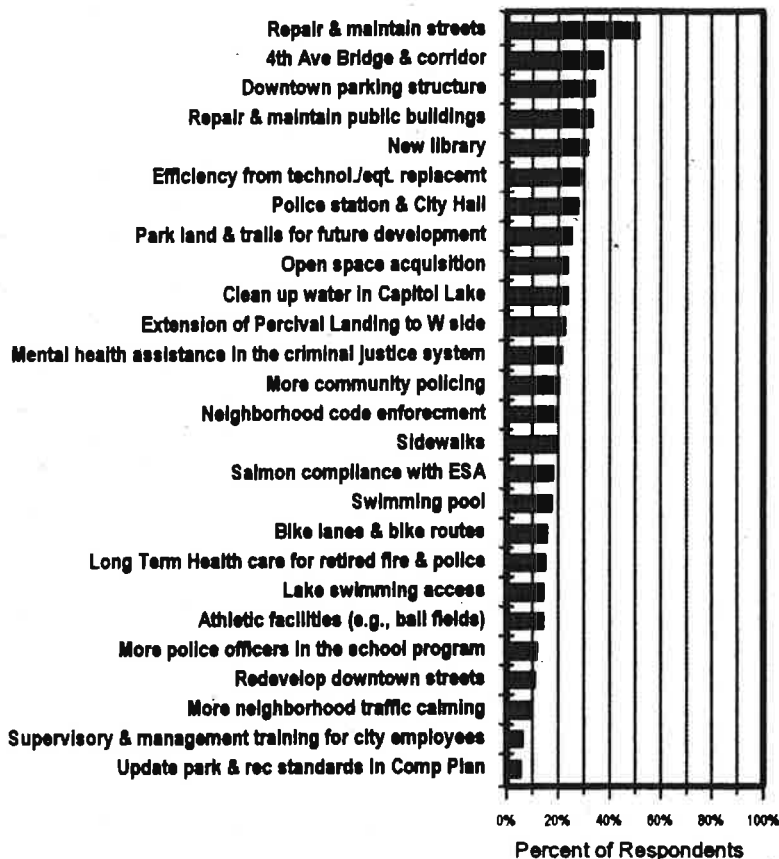
Unaffiliated (n = 240)



WHAT DO THE DIFFERENT GROUPS THINK? Five activities show up on the top-ten lists for all the groups: 1) free bus service to State offices, 2) adult sports, 3) City newsletter in the Olympian, 4) tourism advertising, and 5) free services for community events.

New Priorities

All Respondents (n = 364)



NEW PRIORITIES

Over time, the community's needs evolve. New priorities arise. Existing services and new priorities must be balanced against each other.

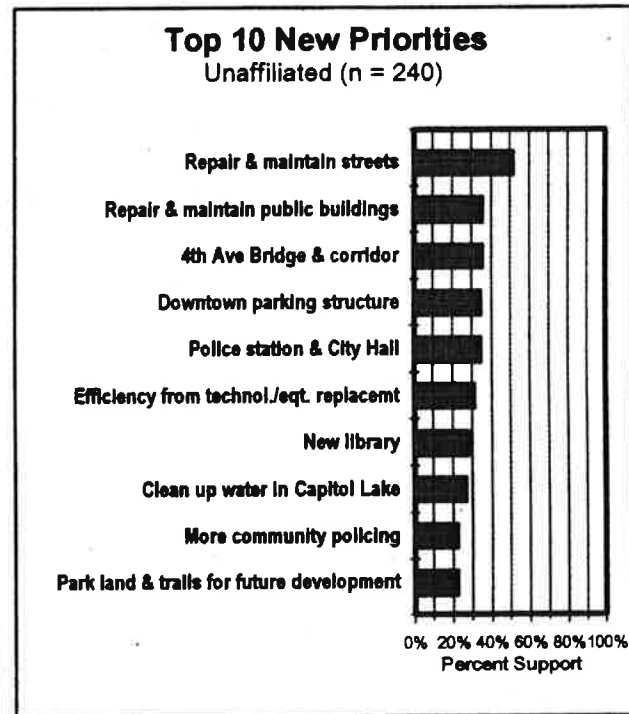
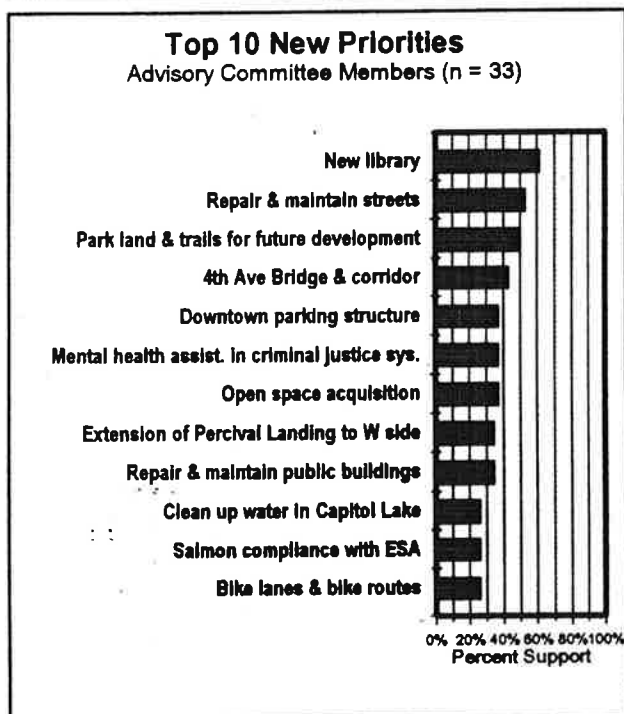
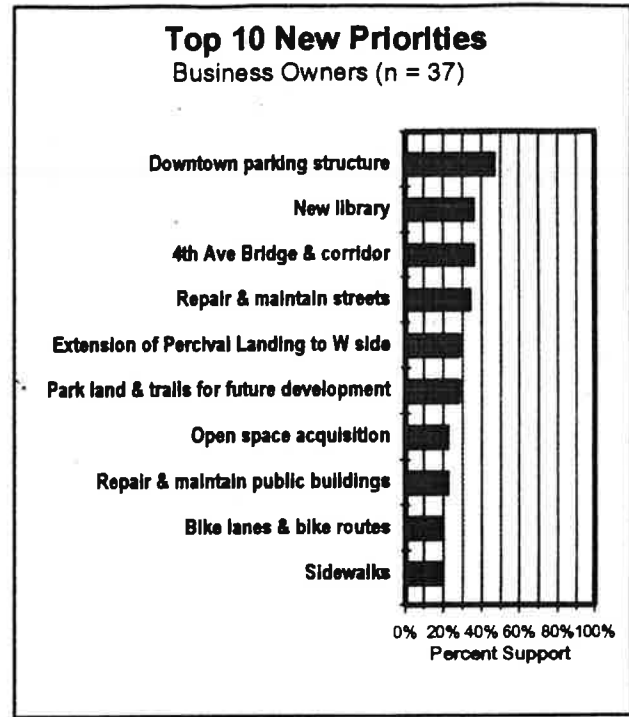
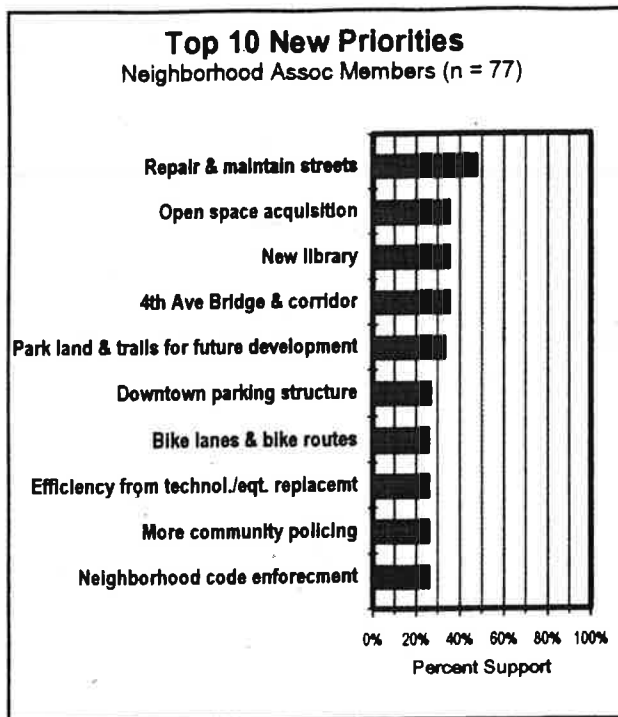
In times of growing resources, new priorities might be added without having to cut existing services. But in times of resource limits, trade-offs may be required. Which are the most important new priorities? Are some new priorities more important than some existing services?

The Council prepared a list of possible new priorities for the City in the next few years. Survey respondents were asked to identify which

of them they might consider important enough to support even if they required additional taxes or fees.

Citizens have a very practical bent in their priorities. The first three are basic transportation projects: street repair, a bridge, and a parking structure. Next is maintaining existing public buildings, replacing the aging library we have outgrown, and using technology upgrades and equipment replacement to maintain City efficiency. Not far behind is new police facilities and the city hall they are housed in, and parks and open space for future needs. There is a very close alignment between this order of priority and the initial order of priority indicated by a Council straw vote at their May work session.

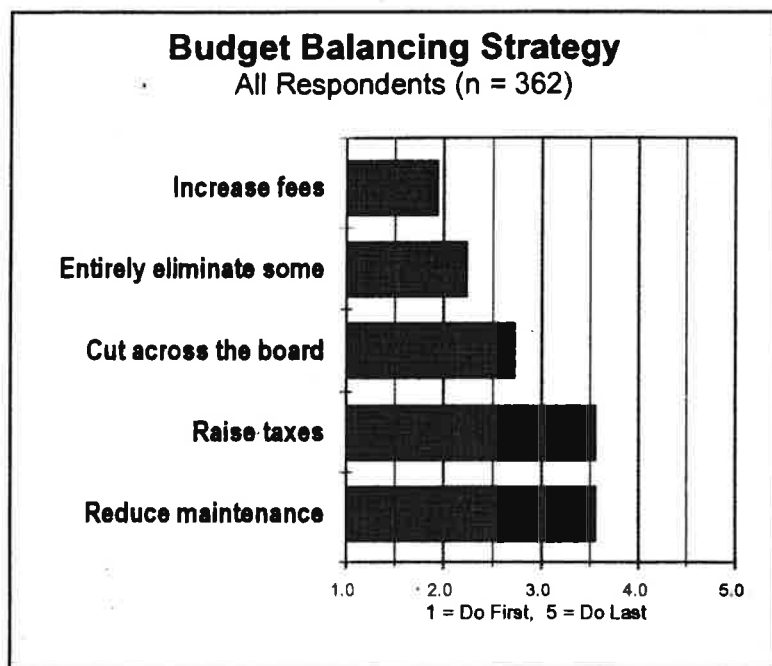
PRIORITIES AMONG THE DIFFERENT GROUPS. There is much agreement. Some items are on all the top 10 lists (next page): 1) Repair and maintain streets, 2) 4th Avenue Bridge, 3) Downtown parking structure, 4) new library, and 5) park land and trails for the future.



There are also differences among the groups. Not surprisingly, a Downtown parking garage is number one with respondents who are business owners, heavily weighted in this survey by Downtown businesses. A new police station and city hall was in the top ten only for the unaffiliated, but since they are the vast majority of respondents, it makes it into the top ten overall.

BUDGET BALANCING STRATEGY

If the City needed to cut spending or raise taxes or fees, either to balance the budget for existing services, or to free funds to add new priorities, how should they do it? The easiest strategy to carry out would be to trim a little everywhere. But it would run the risk of treating high priority services identically to low priority ones. Or, whole programs or services could be dropped. Or, maintenance spending could be reduced, fees increased, or general taxes increased. The survey asked respondents for their favored approach. They were asked to identify which of five approaches to do first, which last, numbered one through five.



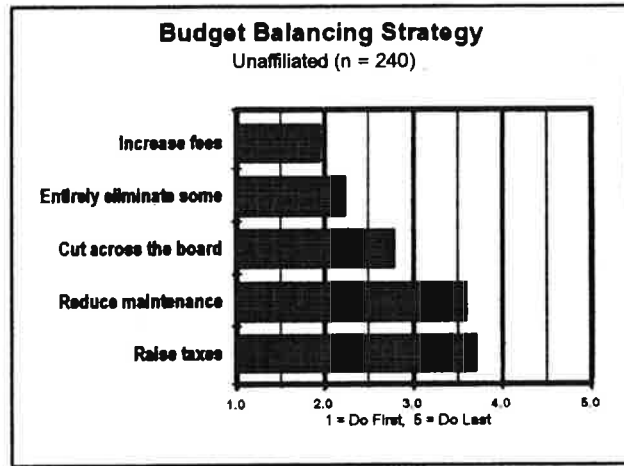
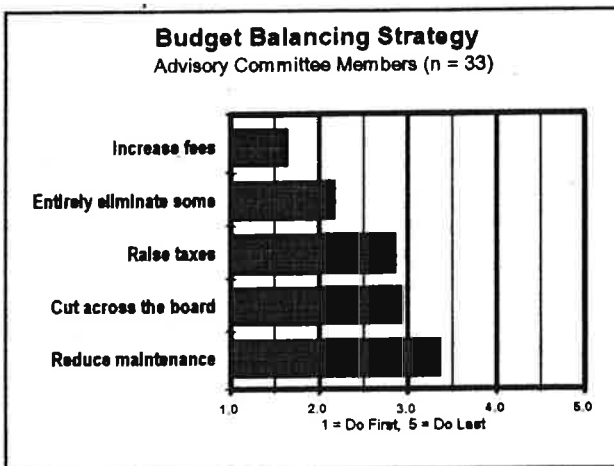
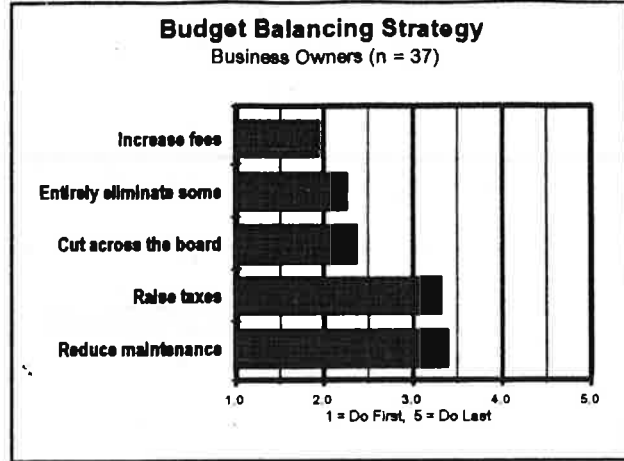
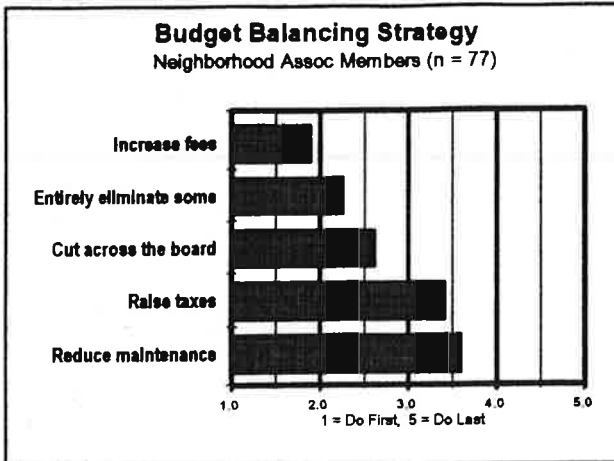
The favorite was increasing user fees to make more programs more nearly self-supporting. This is consistent with the response regarding adult sports programs.

Cutting all programs across the board was less favored than setting priorities among programs and eliminating some. The favored strategy would be consistent with the Council's draft financial principle that the City should eliminate whole programs rather than reduce their funding below levels needed to be effective (i.e., do it well

or don't do it at all).

Antipathy to taxes is very high. It pretty much equals reluctance to allow deferred maintenance to harm the existing investment in City roads and facilities.

This order of priority is widely shared among all the groups (see next page).



There is a high level of agreement among the various groups. Increase fees first. Entirely eliminate programs rather than cut across the board. Don't defer maintenance if you can avoid it.

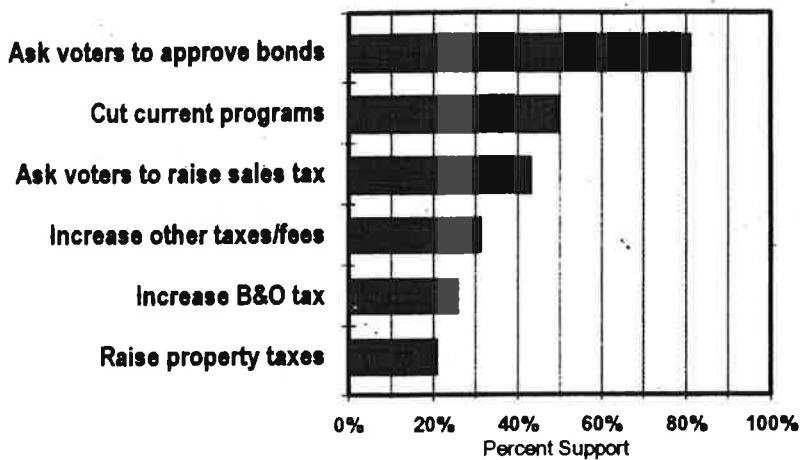
Some differences: the advisory committees *very strongly* prefer increasing fees, and they are comparatively comfortable with raising taxes. The unaffiliated are so strongly opposed to higher taxes that they would even rather cut back on maintenance.

STRATEGIES TO PAY FOR MAJOR PROJECTS

If the City had to raise revenues or make trade-offs to pay for major projects (e.g., 4th Avenue Bridge, swimming pool, etc.), which approaches would be preferred? The clear message is that people would want the opportunity to vote on it -- 80% favored that approach. Half the respondents would wish such projects to be funded by cutting current programs.

Strategy for Major Projects

All Respondents (n = 362)



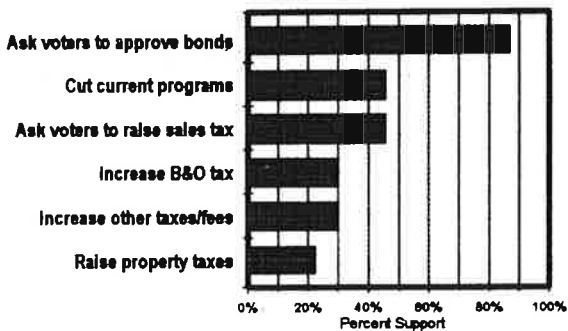
The least favorite option is raising the property tax, clearly a very unpopular tax.

There is clear agreement among the various groups on bond proposals as the first choice. After that, their priorities vary, often widely.

All but the advisory committees put program cuts in second priority, and a voted sales tax in third place.

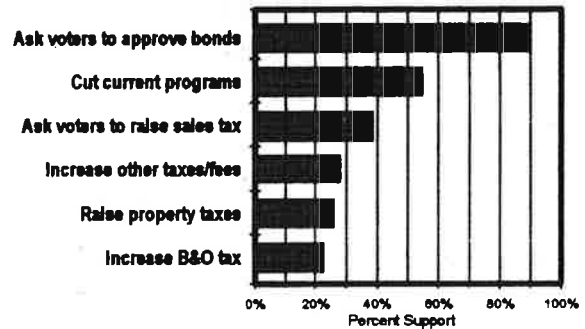
Strategy for Major Projects

Neighborhood Assoc Members (n = 77)



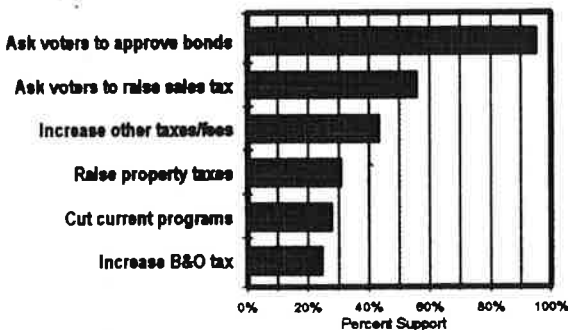
Strategy for Major Projects

Business Owners (n = 37)



Strategy for Major Projects

Advisory Committee Members (n = 33)



Strategy for Major Projects

Unaffiliated (n = 240)

