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TO: Bellingham City Council and the Bellingham Community

FROM: Mayor Dan Pike

DATE: October 3, 2011

RE: 2012 Preliminary Budget

Overview

The purpose of any budget is to specify an organization's spending plan for a fiscal period and to demonstrate how it will continue to fulfill its mission and vision. Formed around the Council's adopted *Legacies and Strategic Commitments* and the performance metrics that will validate our progress or lack thereof, this budget continues fundamental services and prioritizes support of key programs and initiatives that will help us achieve our goals.

It is a budget that is balanced and will not rely in 2012 on use of General Fund reserves.

Since late 2007, our community – like most across the nation—has struggled under the weight of the national recession. During those years, with the City Council's concurrence, we have been restrained in our spending and prudent in the use of established reserves to navigate our way through the hardest economic times in 70 years, while also keeping intact most of the services and programs our citizens depend on and value.

As painful as the past few years have been, it is important for us to maintain two perspectives.

First, we are emerging from the deepest depths of this recession in better shape than many, if not most. Despite the curtailing of hours of operation or elimination of some programs, loss of some of our colleagues to reductions in force, and stagnation of salaries and wages of many others, as a community we are strong. Among the signs of our competitive advantage are:

- Addition to our tourism capacity through planned construction of two new hotels in the city, bringing nearly 300 additional rooms into our inventory;

- Construction of several new mixed-use and other housing projects in downtown by private development and through the work of Bellingham's Public Development Authority;
- Independently verified new heights in customer satisfaction with our Permit Center
- A growing list of more than 170 businesses assisted through our Office of Business Relations & Economic Development, including Index Sensors, which will add some 50 jobs to our market once fully relocated;
- Expansion of existing major local employers, such as Heath Tecna, Blue Sea Systems and Costco;
- Construction access to the waterfront district begun and buildings on the site deemed least probable for viability coming down to make way for the next generation;
- Progress on clean up of several historical sites to expand our recreational spaces and provide land for commerce;
- National rankings as the "best of" too numerous to mention here;
- Unprecedented regional, national and international attention and patronage of the Whatcom Museum
- A revered and growing parks, trail and open space system
- A library teeming with engaged adults and brimming with youngsters well on their way to becoming lifelong learners.

We need to celebrate these accomplishments, especially in these times. A significant ingredient of pulling out of a recession is psychological. I hope we will all keep the above list of good news (and many other items not included) in mind as we move forward. Bellingham is still on the move.

Second, we need to accentuate the positive but also remain vigilant. Things are looking up somewhat as the burden of the recession has lessened noticeably –though not entirely—in the past year, and revenues climb slowly up from their devastating lows. Despite recent growth, we do not yet have a pace of economic expansion that exceeds the cumulative growth rate in our government's structural expenses, especially when national health care inflation continues to run at three or more times the rate of the general cost of living.

Just sustaining what we have as a government is, therefore, an ongoing challenge. For many citizens, financial difficulties also continue. Citizens want and need services but are hard-pressed to pay more for them.

In 2012, we will have the benefit of the debt on the Deemer Road fire station rolling off our books, thereby reducing the City's share of the local collective property tax bill. I am proposing, therefore, that we take the statutorily allowed 1% increase in the property tax levy to maintain City services. With the Deemer Road property tax levy retirement, taking the 1% will keep 2012's taxation on the average home virtually the same as 2011's and possibly even a few dollars lower. This will accomplish the objective of meeting the public's desire for and right to essential services, plus our strong community values surrounding our quality of life amenities, yet without making residents pay more property tax.

After years of departmental cuts, and a projected uptick in inflation to more than 3%, to not take the allowed amount would mean more staff losses and corresponding further reduction in services to the public, or tapping for another year into reserves.

Furthermore, per the RCW, not taking the allowed increase could pose a serious “cliff” in property tax revenues a few years down the road, when our current voter-approved levy lift for Greenways expires. Per the RCW 84.55.050(5), once a voter-approved lift expires, the city’s tax rate returns to its highest “regular” levy rate under the annually allowed one percent inflator formula.

It is all of these potentially negative service implications and creation of a financial handcuff for future councils that I believe make the allowed 1% property tax increase at least worthy of Council and community consideration. Though times are still tough for many households and businesses, let’s discuss whether the taxation increment is a fair, least regressive burden to impose as we stretch for our collective goals. Again, even with the one percent increment, the City’s portion of the local property tax bills –which is less than a quarter of the total bill—will stay the same for 2012 or go down slightly on an average home, if assessed in value similar to 2011.

With or without a small increase in the property tax, this balanced budget that I lay before you remains feasible almost exclusively due to additional capital and operational austerity in 2012. Once again, department heads have had to make very difficult choices. Happily, in contrast to the past few years, that austerity does not include sizeable reductions in force. Where most positions are being removed or redefined, it is due to select re-organizations to achieve longer-term objectives or improve customer service. In those cases, deleted positions are frequently replaced with positions of either different or more flexible classifications. In other cases, positions will be shared by departments to meet similar, mutual needs with less expense.

When all is said and done, the \$64.8 million in General Fund revenues captured in this Preliminary Budget and the \$193.7 million in overall new spending power will join with bond-derived capital reserves to permit our government to successfully focus on its mission, which is:

Support safe, satisfying and prosperous community life by providing the citizens of Bellingham with quality, cost-effective services that meet today’s needs and form a strong foundation for the future.

A Few Items that will Warrant Monitoring During Budget Deliberations

Though in financial terms the skies above us are showing some signs of a slow clearing, clouds remain. We will look forward to discussing with the City Council the following contextual items that could affect our future, if not this proposed balanced budget:

1. As I draft this budget message, new forecasts for State of Washington biennial revenues are expected to be \$1.4 billion worse than projected. The Governor is convening another special session of the Legislature to tackle the deficit but also has authority to do her own across-the-board reductions. It is unknown at this time if or how state government's next phase of expense reduction will affect our spending plan for 2012.
2. The U.S. Congress has before it a recent "jobs plan" from the President. It contains numerous elements that would affect workforce and other taxation, funding for state and local capital projects, etc. Its passage is uncertain, as are its specific possibilities for assisting us locally.
3. Unemployment rates, though better in our area than many parts of the state and nation, have remained largely unchanged in the most recent figures. With our coffers' heavy reliance on consumer spending and the construction industry, this stagnation tempers our recovery momentum.
4. Canadian consumers have enjoyed several years of comparative advantage in their dollar's strength over ours. As a county contiguous to the lower mainland of British Columbia, we have indisputably benefitted from their desire to shop and conduct other transactions in our area. At the same time, the Canadian economy has now reported its second quarter of contraction and may very well be headed for recessionary times. This warrants careful monitoring, especially if a significant recession to the north would occur well before the U.S. recovery gains full traction.
5. As always, factors which are not directly in our control, such as health care inflation, will continue to put pressure on our resources. These include costs associated with additional phases of national health care reform as they occur in the next several years.
6. As the past few years have starkly reinforced, being linked to global economic forces can have tremendous upsides and downsides. World markets remain unsettled. A recent poll of economists found that one in three believe there is still a good chance that the U.S. could experience the start of another recessionary period before 2012 expires.

These and other reasons are why we have successfully strived to avoid further use of General Fund reserves in balancing this budget; our "rainy days" may not be over and we may need our reserves to assure our resiliency. And, we must also keep in mind that any new labor settlements during 2012 must also be paid for from reserves.

Despite this austerity and these uncertainties, this proposed spending plan keeps current service levels afloat, even though staffing levels will improve little next year from the decade-low levels we hit last year. Where positions are increased in FTE or number, fee-for-service revenues or other cost savings have minimized the impact to the bottom line as much as possible.

Budget Development Standards

Though modest improvement in primary revenue streams (e.g. Sales and Use Tax, Business & Occupation tax, etc.) has assisted the formation of this budget for core city services and Council goal-driven initiatives, on the expense side, except for where beyond our control, outlays are often at or below the budget levels of several years ago.

Similar to 2011, we reviewed proposed 2012 departmental expense submissions with five primary criteria or filters applied:

- Does the work contribute measurably to execution of the City Council Legacies and Strategic Commitments?
- Does it help us meet our core responsibility to protect the public's safety, including safety in our homes and businesses, on our streets, in the water we provide, etc.?
- Does it contribute to maintaining and safeguarding our capital assets?
- Does it leverage third party (e.g. other governmental or private grant) resources?
- Will further reduction in expenditure present risks that are equal to or larger than the potential dollars saved in the near-term?

Departments were asked to uphold these priorities while first presenting expenditures that were no more than 101% of their 2011 Adopted Budget. This first-pass direction included meeting their spending target while absorbing increased health care and other benefit costs, and-- unless covered by negotiated concessions-- contractual salary or wage increases as well.

Our experienced departmental leaders and budgeteers struggled mightily with this charge, in particular because 2012's actions are coming after four years of already deep cuts. In the end, not all departments were treated equally, but I believe they were treated equitably based on departmental size, our Legacies, data on the success rates of service delivery, and the dimensions of prior years' cuts. Many of the options I have **not** selected for inclusion involved steep additional cuts in staffing, including public safety.

Areas of Emphasis, Key Changes or New Directions for 2012

Because continuation of core services is front and center in this budget, new or expanded initiatives are few in number when compared to prior years. With or without new elements, this Preliminary Budget will assure continued focus on:

- Nursing our economy back to health through removal of barriers and collaboration with business;
- Partnering with the Washington Department of Ecology, county government, local water districts and our citizens to remain focused on improving the status of Lake Whatcom;

- Continuing reclamation of historically damaged lands for recreational and economic purposes, such as the waterfront district, Cornwall landfill, Boulevard Park, Little Squalicum Creek and others;
- Staying ahead of invasive species that could threaten several of our waterways and water treatment system;
- Redeveloping City-owned parcels so they rejoin the tax rolls and/or meet other important community needs;
- Maintaining and improving our capital assets so they remain viable for generations to come and minimizing their impact on the planet;
- Carrying our weight in making sure our most vulnerable citizens have access to resources and services; and
- Being transparent about our progress on the Council's Legacies and Strategic Commitments as we make our performance metrics consistently available and visible to the public and those who otherwise fund our work.

Many additional and more specific deliverables are described in each department's 2012 objectives found elsewhere in this document.

Bellingham's Financial Resiliency

The 2012 Preliminary Budget will send another clear message to onlookers that Bellingham is serious about keeping our financial house in order and protective of all that makes our area attractive for living, working and recreating.

We enter 2012 with our Limited General Obligation bond rating upgraded by Standard and Poor, and a reaffirmation of our Moody's AA2 rating for Revenue Bonds. Overall, the city has a strong credit position for our utilities' debt.

This year's budget anticipates an ending General Fund available reserve of \$8.9 million or 14% of 2012 operating expenditures. The reserve consists of \$7.8 million set aside to meet the council's approved target reserve level and \$1.1 million of undesignated reserves. In total, the City budget forecasts more than \$98 million dollars in estimated ending reserve accounts of all types. While these sums might appear to be bountiful, it is important to note that the General Fund Reserve, for example, if on target at the end of the year, will constitute only about seven (7) weeks of operating expenses. In addition to meeting legal and financial obligations, the General Fund reserve is set aside to help the city weather financial impacts that could come from unforeseen emergencies or economic disruptions. Most of the other reserves on hand have restricted uses.

Budgeted Staffing Changes’ Impact on Comparable Ratios

As previously described, the City’s 2011 Adopted and Revised Budgets further reduced the size of our workforce. To meet some Council directives, such as daily operation of the Post Point incinerators as part of a biochemical oxygen demand (BOD) strategy, we also added some positions by budget ordinance since passage of that budget.

The equivalent of .5 FTE will be lost for an incumbent employee as a reduction in force action for 2012. Others will be redefined to meet the needs of new business models or other mandates. With the positions added by ordinance since passage of the 2011 budget and the revisions proposed for 2012, we will see a slight uptick in employee count.

The 2011 Adopted Budget authorized 842.2 Full Time Equivalent (FTE) positions, inclusive of temporary or seasonal workers. The 2012 preliminary budget, which captures those added by ordinance during 2011 and any plans for 2012, reflects an increase in budgeted positions of 5.2 to a total of 847.4 FTEs, calculated as follows:

BUDGETED FTEs	
2011 Budgeted FTEs	842.2
Net FTEs added by ordinance in 2011	2.5
FTEs added for 2012	7.2
Elimination of vacant positions	(2.9)
Reduction in force	(0.5)
Net increase in hours for budgeted positions, including non-benefited labor	0.9
Decrease in hours for Limited Term positions ending in 2012	(0.8)
Net FTE savings for delayed hire of budgeted positions	(1.2)
2012 Budgeted FTEs	847.4
Net Increase	5.2

These changes mean the City’s workforce is still down 68.9 FTEs since the 2008 budget was adopted, or 7.5%. In addition, several departments will continue to function with some of their authorized strength “frozen” as vacancies until we feel it is prudent to authorize their filling.

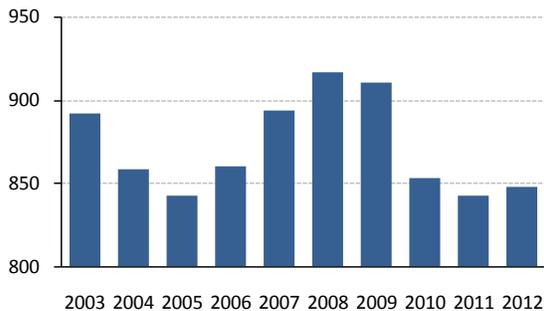
The table below compares the requested number of FTEs for 2012 to prior years’ adopted budget levels. With these net changes, the City’s staff to thousand population ratio of 10.4 is below the level

budgeted over the past decade, including 2005, when another significant reduction in force was implemented. At the same time, we will continue to operate at a level of staffing stretched but sufficient for our existing or reduced service needs.

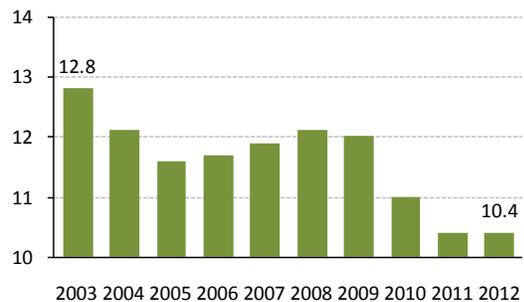
10 YEAR HISTORY OF BUDGETED POSITIONS IN FULL TIME EQUIVALENTS FROM ADOPTED BUDGETS

Employee Group	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Elected Mayor (and Finance Director through 2007)	2.0	2.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
Elected City Council	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
Elected Municipal Judge	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Non-Represented Employee Grp	78.6	77.4	77.1	79.9	83.9	90.8	87.0	80.1	77.0	78.6
Supervisors and Professionals	100.6	101.7	104.9	103.4	108.6	107.8	106.0	100.0	97.5	97.0
Professional Librarians	8.3	8.0	8.0	8.0	8.0	8.0	8.0	6.3	7.0	6.7
Emergency Med Svcs Dispatch	11.0	11.0	12.0	12.0	12.0	13.0	13.0	13.0	13.0	13.0
Fire Supervisors	8.0	7.3	7.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
Firefighters	129.7	129.3	122.5	126.0	132.0	135.0	133.0	129.0	133.0	133.0
Police	98.0	95.4	95.1	100.0	102.0	102.0	106.0	99.7	101.0	101.0
WHAT COMM Dispatch	23.0	23.0	23.0	23.0	26.0	26.0	26.0	26.0	26.0	26.0
Non-Uniformed	355.7	334.4	323.5	327.3	336.5	352.1	351.6	319.8	310.1	314.9
TOTAL REGULAR	822.9	797.5	783.1	797.6	827.0	851.7	847.6	790.9	781.6	787.2
Temporary Labor	69.1	60.9	59.2	62.2	66.6	64.6	62.6	62.0	60.6	60.2
TOTAL PAID WORKFORCE	892.0	858.4	842.3	859.8	893.6	916.3	910.2	852.9	842.2	847.4

TOTAL BUDGETED POSITIONS



FTE's per 1,000 City Population



Source for population estimates – State of Washington Office of Financial Management

While I must confess to some concern that some departments are too thinly staffed, which presents some risk to our obligations and goals, I do not think it is prudent to add larger numbers of positions than those proposed until we are certain that a second recession and other threats are well behind us. In the interim, our departments will continue to collaborate to provide risk management redundancy where feasible and our skilled department heads will keep us apprised of any new or emerging threats that might need action as the year progresses.

In short, despite a smaller workforce, our citizens can expect that the City will continue its proud tradition of providing quality basic and desirable enrichment services, while we also maintain momentum on managing growth, redeveloping the waterfront, moving Lake Whatcom back toward health, bringing jobs and economic development to our community,

strengthening and expanding cherished cultural facilities, maintaining our engagement of neighborhoods, and building or maintaining key capital infrastructure.

Summary

We can now see signs that better times again lie ahead for our community. Our economic progress may lag in pace behind our hopes, but a new healthier direction is afoot. Until our economy expands at a rate that outpaces growth in structural expenses, we will need to remain frugal, collaborative and innovative.

Guided by the City Council's Legacies and Strategic Commitments, we will continue to partner with our citizen advisory boards, commissions, peer governments, and of course, the public, to demonstrably make progress toward our goals. Though the pace of change may be somewhat tempered by our lack of resources, we are on the right track. This budget assures we stay the course.

I remain honored to work alongside our skilled City employees, policy makers and volunteers to implement our collective vision and I thank one and all for your hard work and dedication in delivering community services. I am particularly proud of the teamwork that Department Heads have exhibited and the additional innovations their teams are working together to nurture for the coming days of our organization.

I would like to specifically acknowledge Budget Manager, Brian Henshaw, Finance Director, John Carter and budget staff members Patricia Starcher and Karla Buckingham, as well as the entire Finance Department team, for the many long hours required to produce a spending plan of this complexity and scope. Like most departments, they, too are short-staffed but have rallied for another year of quality work.

This spending plan is but another chapter in Bellingham's story. I remain confident that our story will remain the envy of many and one that will bring to our citizens, staff and visitors in 2012 a year of increasing prosperity. With due diligence, team work and creativity we will take advantage of what the next year provides us, and put it to use for a stronger community and future.

Sincerely,

A handwritten signature in black ink, appearing to read "Dan Pike". The signature is stylized with a large initial "D" and a long, sweeping underline.

Dan Pike, Mayor