

**SULTAN PLANNING BOARD
AGENDA ITEM COVER SHEET**

ITEM NO: Discussion – 1

DATE: May 6, 2008

SUBJECT: Preliminary Capital Facility Budget Revenue Sources

CONTACT PERSON: Deborah Knight, City Administrator

ISSUE:

The issue before the City Council and Planning Board is to review the revenues available to finance needed capital improvements to meet adopted level of service standards. The Preliminary Capital Financial Resources presentation (Attachment A) provides:

1. An inventory of existing fiscal resources and evaluates the current and future fiscal capacity to finance capital facilities.
2. A needs analysis estimating total financial resources available to provide alternative levels of service
3. A strategy to finance capital facilities needed to support the land use plan (The financial strategy will be presented on May 13, 2008)

The Growth Management Act requires that any community which cannot demonstrate the financial ability to accommodate its planned growth must reexamine its land use patterns or its financing plans. This is where the rubber meets the road. The city must be able to afford its preferred level of service standards or change its land use or financing plan.

STAFF RECOMMENDATION:

1. Evaluate current and future fiscal capacity to finance capital facilities
2. Review total financial resources available and compare resources to alternative levels of service
3. Discuss long-range strategies to finance capital facilities needed to support the land use plan.

BACKGROUND:

For the last two months, the City Council and Planning Board have identified level of service standards and discussed preferred alternatives for water, sewer, stormwater, parks and transportation facilities to address the issues identified by the Central Puget Sound Growth Management Hearings Board in Fallgatter V, Fallgatter VIII, and Fallgatter IX.

In its final decision and order in Fallgatter IX on the Capital Facilities Plan, the Board found:

- The Capital Facilities Plan does not demonstrate adequate sewer facilities will be available within the planning period to serve the unsewered population
- The Capital Facilities Plan fails to provide an adequate needs assessment (i.e. current needs, future needs, and expected levels of services) for water, sewer and stormwater facilities.
- The Capital Facilities Plan does not incorporate local adopted levels of service.
- **Identified funding is lacking to serve the adopted level of service. The City cannot rely on future development to provide major infrastructure such as sewer.**

SUMMARY:

The Preliminary Capital Financial Resources presentation looks at the revenues available to service the preferred level of service standards identified by the City Council. Early impressions of the City's financial resources to support capital funding:

- General Fund operating revenues will be needed for operations.
- While there will be substantial funds from city capital revenues, it will not be to meet needs.
- Grants can only supplement city revenues.
- While there is substantial debt capacity, the potential amount that can be generated will be constrained by voter approval.
- The funding strategy will need to rely heavily developer financing for facility extensions into undeveloped areas.

Sources of Capital Funding

There are three primary sources of revenue for the Capital Facilities Plan: 1) city funds; 2) debt financing; 3) developer contributions. The Preliminary Capital Financial Resources presentation starts by forecasting City Funds. The analysis assumes no General Fund revenues will be available for the Capital Facilities Plan. General Fund revenues will be used for operations.

Key variables include:

<i>Key Variable Table</i>	<i>Base Forecast</i>
Inflation Rate	3.5%
Appreciation Rate	6.0%
Construction Escalation Rate	5.0%
Average Property Tax Increase	1.0%
City Inside Utility Tax	6.0%
Interest Rate	4.5%
Street Fund Share of Property Tax	13.0%
Building Permit Income	2,000.00
Initial Water System Development Charge / ERU	5,254.00
Initial Sewer System Development Charge / ERU	9,106.00
Sales per sq ft new commercial	1.75
Commercial Construction Costs /sq ft	250.00
Initial Park Impact Fee	3,415.00
Initial Transportation Impact Fee	1,837.00

City Sources of Revenue

There are six sources of City revenue for the Capital Facilities Plan:

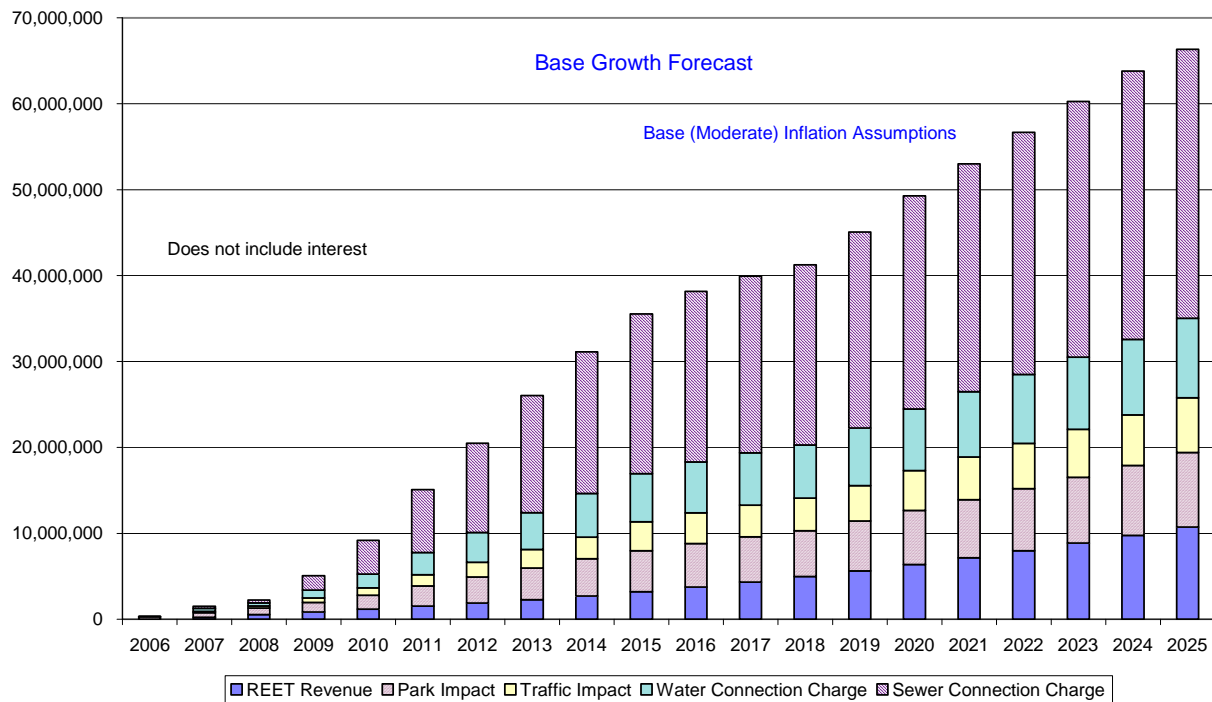
Base (Moderate) Inflation Assumptions		
Capital Revenue Capacity		
2008 Dollars	<i>2015</i>	<i>2025</i>
Annual Income		
REET Revenue	501,179	965,301
Park Impact	462,639	532,428
Traffic Impact	820,022	494,260
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Total	4,754,750	3,203,993
Cumulative Potential		
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Sewer Operations	1,384,464	5,268,121
Total	36,060,531	70,727,246
Cumulative Potential Interest if not Spent	2,958,777	9,562,467
Levy Lift Potential		
Potential Capital Bond	3,011,510	9,544,846

Assumptions

2007 Dollars	
Base Growth Forecast	
Base (Moderate) Inflation Assumptions	
Annual Deflator (Construction Escalator)	5.0%
Interest Rate on Investments	4.5%
Interest Rate on Bonds	4.5%

In 2008 Dollars:
Adjusted for Inflation

City of Sultan, Washington Fiscal Capacity Analysis
Capital Funds Fund Forecast by Year
Source: DPS



Debt Financing

The second source of revenue is debt financing through levy capacity. Following are descriptions of some of the major debt financing options along with a discussion of important issues related to each.

1. **General Obligation Bonds** - Backed by the full faith and credit of the city . Bondholders have legal claim on general income of the city if default occurs. There are two types:

A. **Councilmanic Bonds** (Limited Tax General Obligation Bonds)

May be issued by a vote of city council. Backed by general fund revenues because voters have not been asked to pay increased property taxes. May be used for any city purpose. Does not have to be capital.

B. **Unlimited General Obligation Bonds**

Backed by the full faith and credit of the local government.

Must be approved by a 60% majority of the voters, turnout must be 40 percent of those voting in the last general election. Raises property tax to pay for projects. Only used for capital purposes. Limits to amount of debt that can be issued.

Debt limits:

Three pots of 2 1/2% of assessed valuation each: (1) general government purposes, (2) municipally owned water, sewer and electric utilities, and (3) open space and parks. Pots two and three are voted, must be 60% yes, 40 percent turnout.

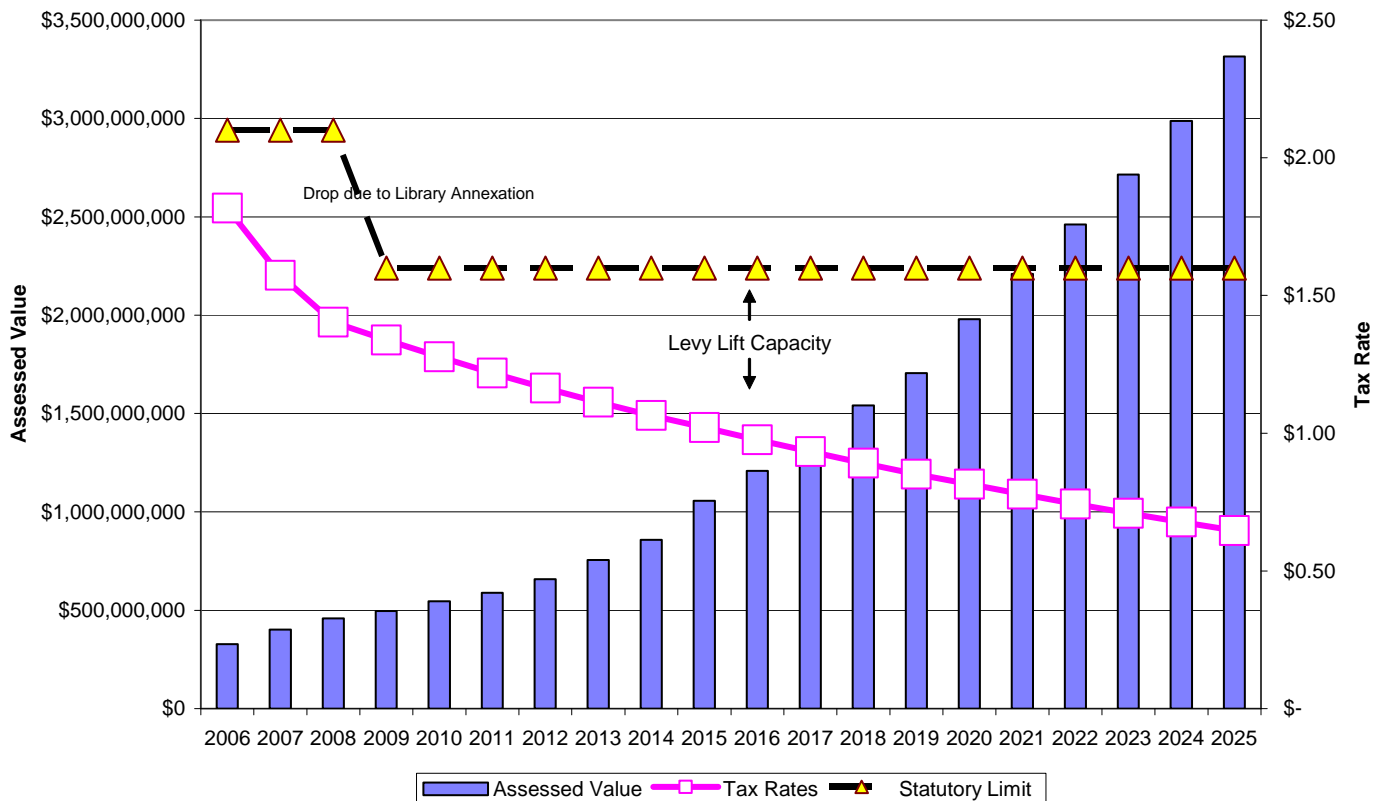
Pot 1 is a mixture of voted and non voted. 1 1/2% is limit of non voted, or councilmanic bonds.

Most cities have more debt capacity that they can use. Political limits are often tougher - willingness to pay may be greater than ability to pay. Most communities do not issue debt to their full legal capacity.

City of Sultan, Washington Fiscal Capacity Analysis

Assessed Value and Property Tax Rates

Source: DPS



**Inside (Councilmanic) Levy Capacity
Existing Revenue Authority or with 50% Voter Approval**

	2010	2015	2020	2025
Ultimate Authority with existing revenue or voter approval:				
Assessed Value	\$ 544,985,769.09	\$ 1,056,687,690.89	\$ 1,978,831,438.55	\$3,315,197,477
Inside Dept Capacity (1.5% of AV)	\$ 8,174,786.54	\$ 15,850,315.36	\$ 29,682,471.58	\$49,727,962
Current Value (2008 Dollars)	\$ 7,061,687.97	\$ 10,728,117.34	\$ 15,741,248.42	\$20,662,995
Voter Approval:				
Tax Rate per Thousand AV	\$ 1.28	\$ 1.02	\$ 0.81	\$0.65
Statutory Tax Rate	\$ 1.60	\$ 1.60	\$ 1.60	\$1.60
Difference	\$ 0.32	\$ 0.58	\$ 0.79	\$0.95
Annual Revenue Capacity	\$ 175,927.69	\$ 612,120.06	\$ 1,554,170.69	\$3,160,197
Capital Potential (nominal Dollars)	1,278,781.49	4,449,372.45	11,296,941.16	\$22,970,810
Current Value (2008 Dollars)	\$ 1,104,659.53	\$ 3,011,510.41	\$ 5,991,009.09	\$9,544,846
Assumptions				
Interest Rate				4.5%
Term (Years)				9
Property Value Appreciation				6.0%
Construction Inflater				5.0%
Limit Factor				1.0%

**Excess Levy:
Voter Approval Requirement: 60%**

Assessed Value	\$544,985,769	\$1,056,687,691	\$1,978,831,439	\$3,315,197,477
Tier 1 Limit (General)	\$13,624,644	\$26,417,192	\$49,470,786	\$82,879,937
Tier 1 Limit in Addition To Inside Levy	\$5,449,858	\$10,566,877	\$19,788,314	\$33,151,975
Debt Service	\$418,964	\$812,341	\$1,521,249	\$2,548,596
Tax Rate per Thousand AV	\$0.77	\$0.77	\$0.77	\$0.77
Current Value of Construction (2008 Dollars)	\$4,915,459	\$7,152,078	\$10,494,166	\$13,775,330
Tier 2 Limit (Utilities)	\$13,624,644	\$26,417,192	\$49,470,786	\$82,879,937
Debt Service	\$1,047,410	\$2,030,852	\$3,803,123	\$6,371,490
Tax Rate per Thousand AV	\$1.92	\$1.92	\$1.92	\$1.92
Current Value of Construction (2008 Dollars)	\$12,288,648	\$17,880,196	\$26,235,414	\$34,438,326
Tier 3 Limit (Parks and Open Space)	\$13,624,644	\$26,417,192	\$49,470,786	\$82,879,937
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Developer Financing

While substantial revenues are generated for capital facilities using city resources and debt capacity, this amount is not sufficient to finance needed facilities. Anticipated costs are greater than the forecasted revenues.

- Transportation costs in the Transportation Element exceed \$160 million
- REET and impact fees only generate \$17 million over the planning period
- It is unlikely that either grants and/or bonds can make up the difference

Developer improvements through direct construction, local improvement districts, impact fees, and voluntary agreements can close the gap between future needs and financing available through city revenue sources and/or debt service.

The challenge is to balance the need for developer financing without discouraging development too much. For example, raising the transportation impact fee from the current level of \$1,837 to \$7,000 can close the gap and finance the majority of capacity projects in the transportation element. However, a \$7,000 impact fee could make certain projects unfeasible.

The City Council and Planning Board will need to discuss various developer financing strategies and provide direction to staff and consultants in order to prepare long-range strategies to finance capital facilities needed to support the land use plan.

DISCUSSION:

¹A capital facilities plan includes inventories of existing facilities showing both “location” and “capacity”, a forecast of future needs, the proposed location and capacity of new facilities, and a six-year plan to finance facilities from identified funding sources.

Where “probable funding” falls short of meeting “existing needs” the land use element is reassessed to ensure that the land use element, capital facilities element and financing plan are coordinated and consistent.

The link between a community’s financing capability, adequate capital facilities and the ability of facilities to meet “existing needs” based on the land use plan is the heart of the growth management act. Finding the balance between these competing forces is a challenge.

¹ A Short Course in Local Planning – Washington State Department of Community Trade and Economic Development

The challenge in capital facilities planning is to identify affordable and appropriate levels of service for the community. LOS measures the quality and quantity of services that are delivered in a community.

If the services are too high, a community cannot afford to make the needed investments. If the service levels are set too low, the quality of life in the community could deteriorate. Levels of service reflect a community's values and willingness to pay for public facilities.

If population increases exceed a community's ability to provide capital facilities, it must reexamine land use plans to reestablish a reasonable balance. The key is "concurrency" at the planning or development regulation level.

Concurrency at the regulatory level is specified in the capital facilities element of the comprehensive plan. Local communities are to:

- Inventory existing facilities
- Forecast future needs
- Locate and size future facilities
- Project funding capabilities
- Reassess land use plans if funding capabilities are inadequate

To accomplish this task, a community must:

1. Establish level of service standards
2. Measure the degree to which the community does not meet the LOS under present conditions
3. Measure the cost to the community of paying for existing deficiencies, and the cost of extending or upgrading facilities to meet new demands.

The GMA's mandate for concurrency demands that communities face reality. Communities that cannot or will not provide adequate financing will not meet this test. Communities are required to identify appropriate levels of service to meet lower budgets or reassess their land use plans to find ways to decrease demands for public facilities.

FISCAL IMPACT:

This is an introduction to revenues available to finance needed capital improvements to meet adopted level of service standards.

A strategy to finance capital facilities needed to support the land use plan and the financial impacts will be the focus of the joint meeting on May 13, 2008.

Next steps include:

- Comparing potential revenues to unconstrained needs.
- Recommending realistic measures to make up deficit, including but not necessarily limited to:
 - General adjustments to rates, fees and charges.
 - Allocation of REET between needs.
 - Policies regarding developer financing.
 - Revise level of service or project needs list.
- Recommend overall 2025 Financing Strategy.
- Recommend Six Year Financial Plan based on strategy.

RECOMMENDATION:

1. Evaluate current and future fiscal capacity to finance capital facilities
2. Review total financial resources available and compare resources to alternative levels of service
3. Discuss long-range strategies to finance capital facilities needed to support the land use plan.

ATTACHMENTS

A – Preliminary Capital Financial Resources presentation

Preliminary Capital Financial Resources

City of Sultan Washington

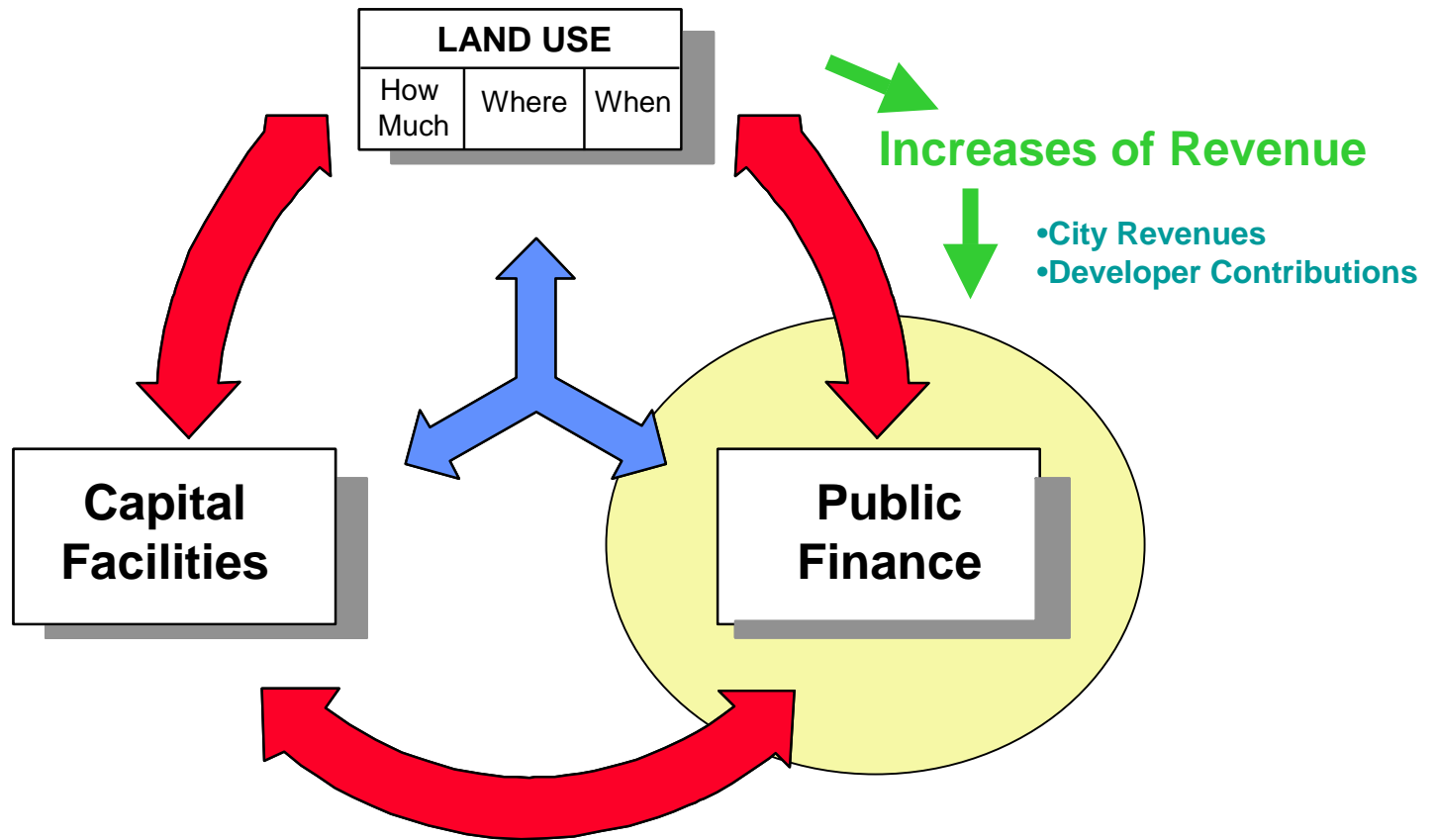
April 15, 2008

Dugan Planning Services



Fiscal Part of the Program

- An inventory of existing fiscal resources.
 - Evaluate current and future fiscal capacity to finance capital facilities.
- Will be followed by a needs analysis.
 - **Estimate Total Financial Resources Available**
 - Compare Resources to alternative levels of service.
- Then develop a strategy to finance capital facilities needed to support the land use plan.
 - Long Range Strategy that describes how the comprehensive plan can be financed.
 - Six year Financial Program (CIP).



Resources

- **City Funds**
 - Estimated by forecasting
- **Grants**
 - Past history and realistic estimates
- **Developer Financing**
 - Appropriateness of different projects to be financed by developers (directly or indirectly)

Forecast Approach

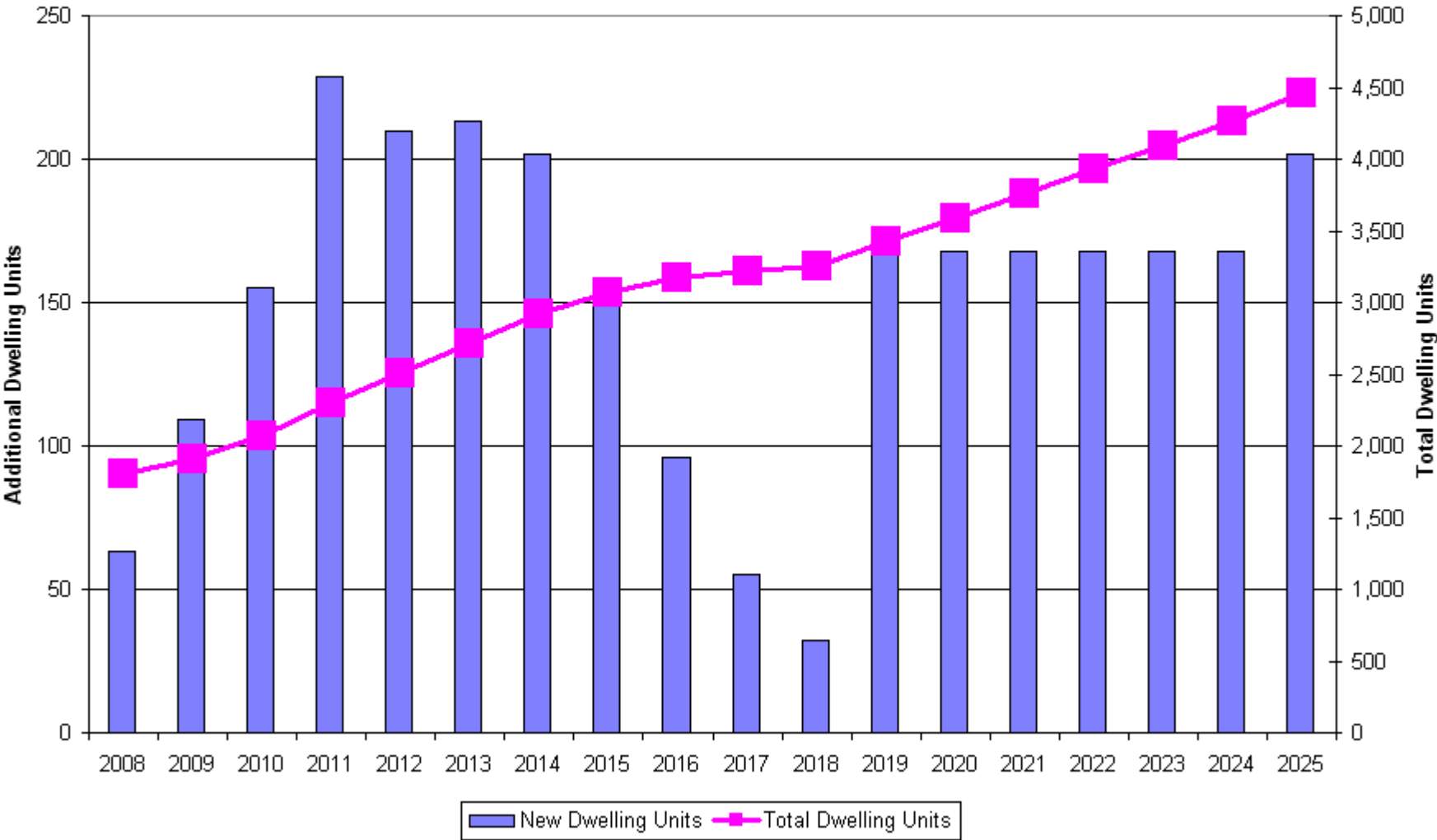
- Forecast each fund
- Apply a wide Range of Assumptions
 - The development planned in the comprehensive plan
 - Residential and non-residential
 - Other factors
 - Staffing patterns
 - Inflation factors
 - Business trends and opportunities

Key Variables

<i>Key Variable Table</i>	<i>Base Forecast</i>
Inflation Rate	3.5%
Appreciation Rate	6.0%
Construction Escalation Rate	5.0%
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City of Sultan, Washington Fiscal Capacity Analysis
Forecasted Growth for Financial Planning
 Source: City of Sultan and DPS



Forecast from “pipeline” development information and population estimates in needs report



Implications of Growth on General Fund

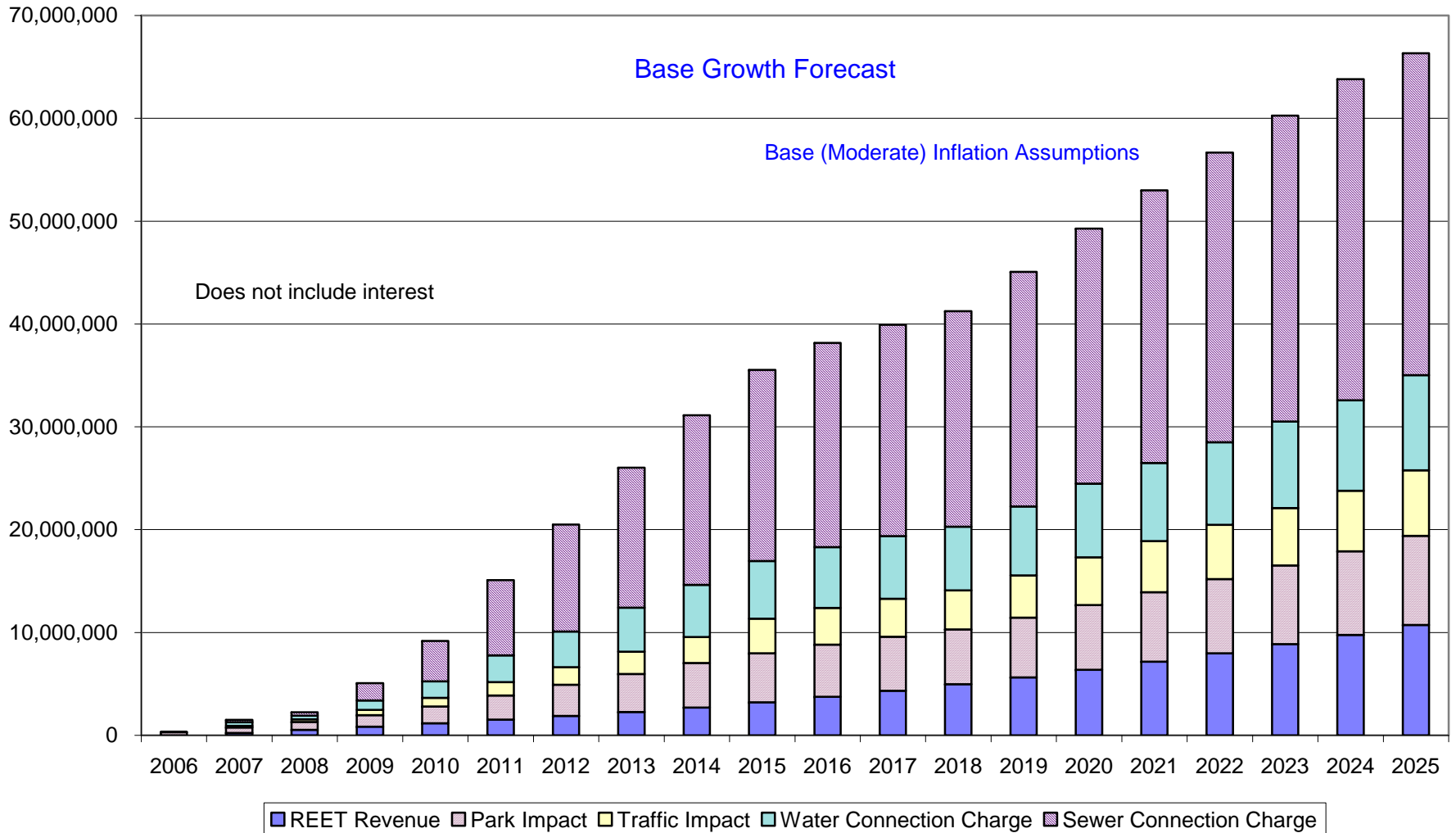
- The general fund is dependent on growth.
 - Property taxes from new construction.
 - Sales taxes on construction activity.
- The growth forecasted can improve the general fund financial impact if current levels of service are not raised.
 - All of the improved financial condition would be used if police levels of service were raised to 2.5 officers per thousand.
- No General Fund Revenue will be available for Capital—it will all be needed for operations.

Implications of Growth on Other Operating Funds

- Street fund will need continual attention since revenue capacity is constrained.
- Water fund will need rate adjustments to meet on-going needs.
- Recent rate increases seem to have positioned the sewer fund to meet its operational needs
 - Although there are near term cash flow issues from connection charges to cover debt service.

In 2008 Dollars:
Adjusted for Inflation

City of Sultan, Washington Fiscal Capacity Analysis
Capital Funds Fund Forecast by Year
Source: DPS



Note: Does not include any sewer plant construction

Base (Moderate) Inflation Assumptions**Capital Revenue Capacity**

2008 Dollars	<i>2015</i>	<i>2025</i>
Annual Income		
REET Revenue	501,179	965,301
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Levy Lift Potential		
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Assumptions

2007 Dollars

Base Growth Forecast

Base (Moderate) Inflation Assumptions

Annual Deflator (Construction Escalator) 5.0%

Interest Rate on Investments 4.5%

Interest Rate on Bonds 4.5%

Note: sewer connection charges are assumed to continue after 2013 at \$20,086/ERU as recommended by rate study for 2013.

Water charge forecasted at current rate adjusted for inflation.



Prospects

- While substantial revenues will be generated for capital facilities, this amount will not be sufficient to finance needed facilities.
- Costs are much greater than the forecasted revenues—for example;
 - Transportation costs in the Transportation Element exceed \$160 Million.
 - But REET and Impact fees would as forecasted generate only \$17 million.
 - Similar differences in other systems.
- Will need to consider
 - **Grants.**
 - **Debt financing.**
 - **Developer financing.**

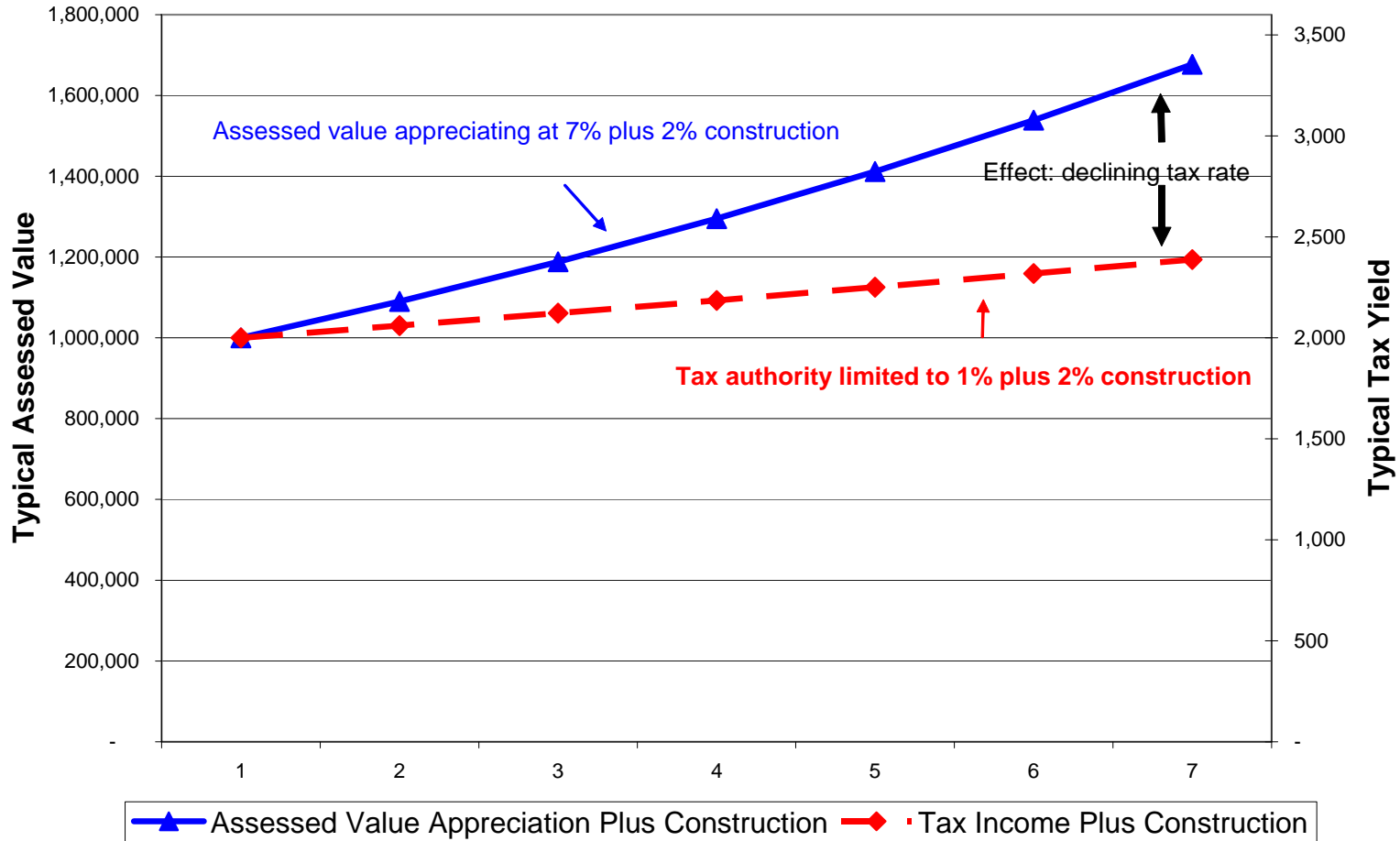
Grants

- Limited Potential.
 - Highly competitive.
 - Declining availability.
 - Requires timely matching funds.
- City likely to be most competitive for capacity, needs related to Highway 2, safety improvements and for addressing some deficiencies.
- Can help, but best thought of as supplemental source of funds for some types of projects.

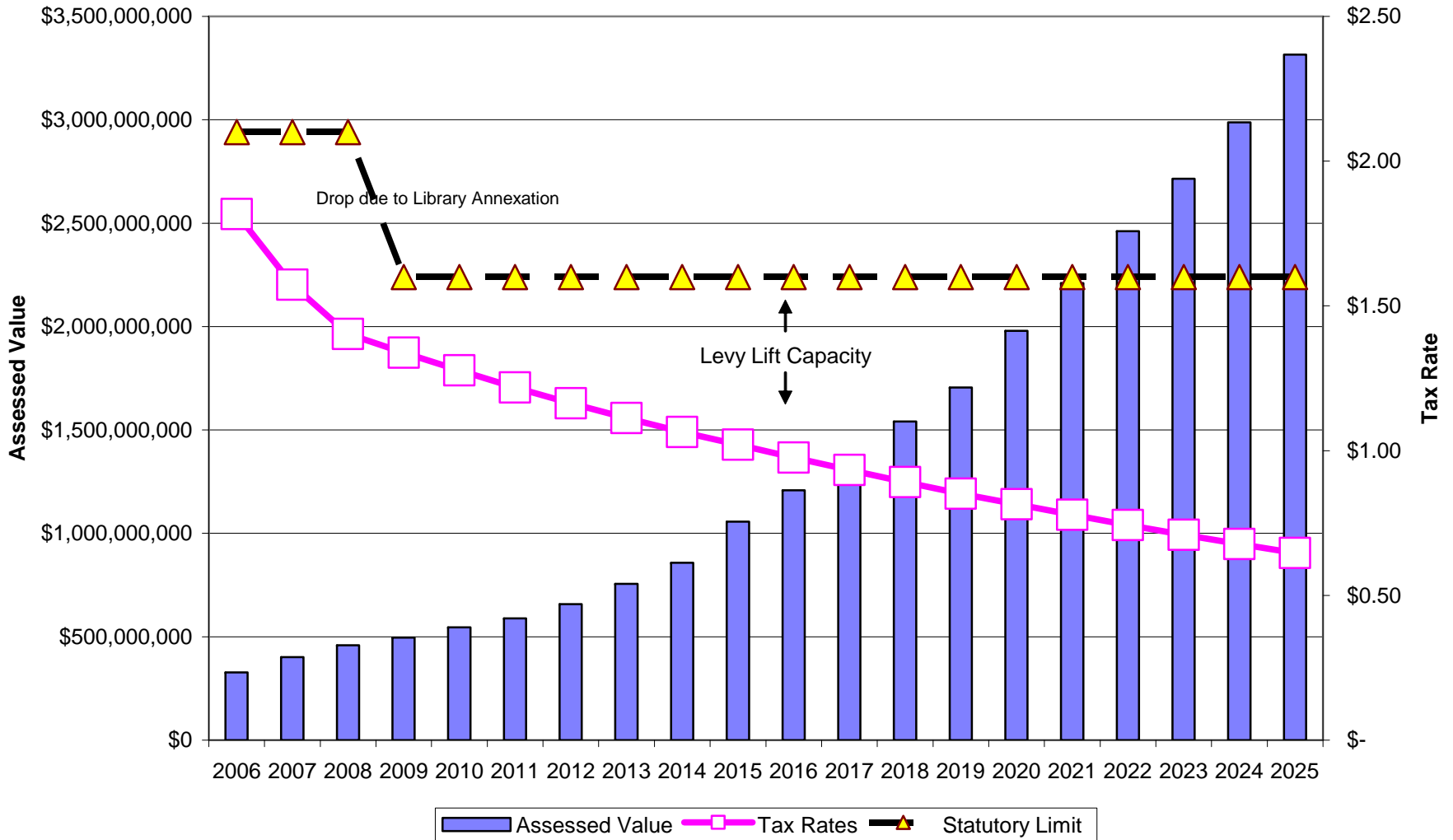
Debt Financing Options

- GO Debt (backed by property value of city—usual from paid from property taxes).
 - **Excess Levy.**
 - 60% Approval for additional revenue
 - **Inside (or Councilmanic) Levy.**
 - If from existing revenue authority, no vote needed.
 - 50% approval for property taxes within “levy lid.”
- Revenue Bonds (backed by the value of an “enterprise”—usually a utility).
 - Retired by revenues from existing revenue authority—usually utility rates or charges.
- Special Assessments (backed by property values within a assessment district).
 - Retired by special assessments based on “benefit.”

How Property Taxes Work



City of Sultan, Washington Fiscal Capacity Analysis
Assessed Value and Property Tax Rates
 Source: DPS



**Inside (Councilmanic) Levy Capacity
Existing Revenue Authority or with 50% Voter Approval**

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Need for Developer Financing

- Existing revenue authority will only meet a small portion of total need.
- Grants can only supplement that amount.
- Unlikely that voters will approve high enough levies to make up difference for total amount

Approaches to Developer Financing

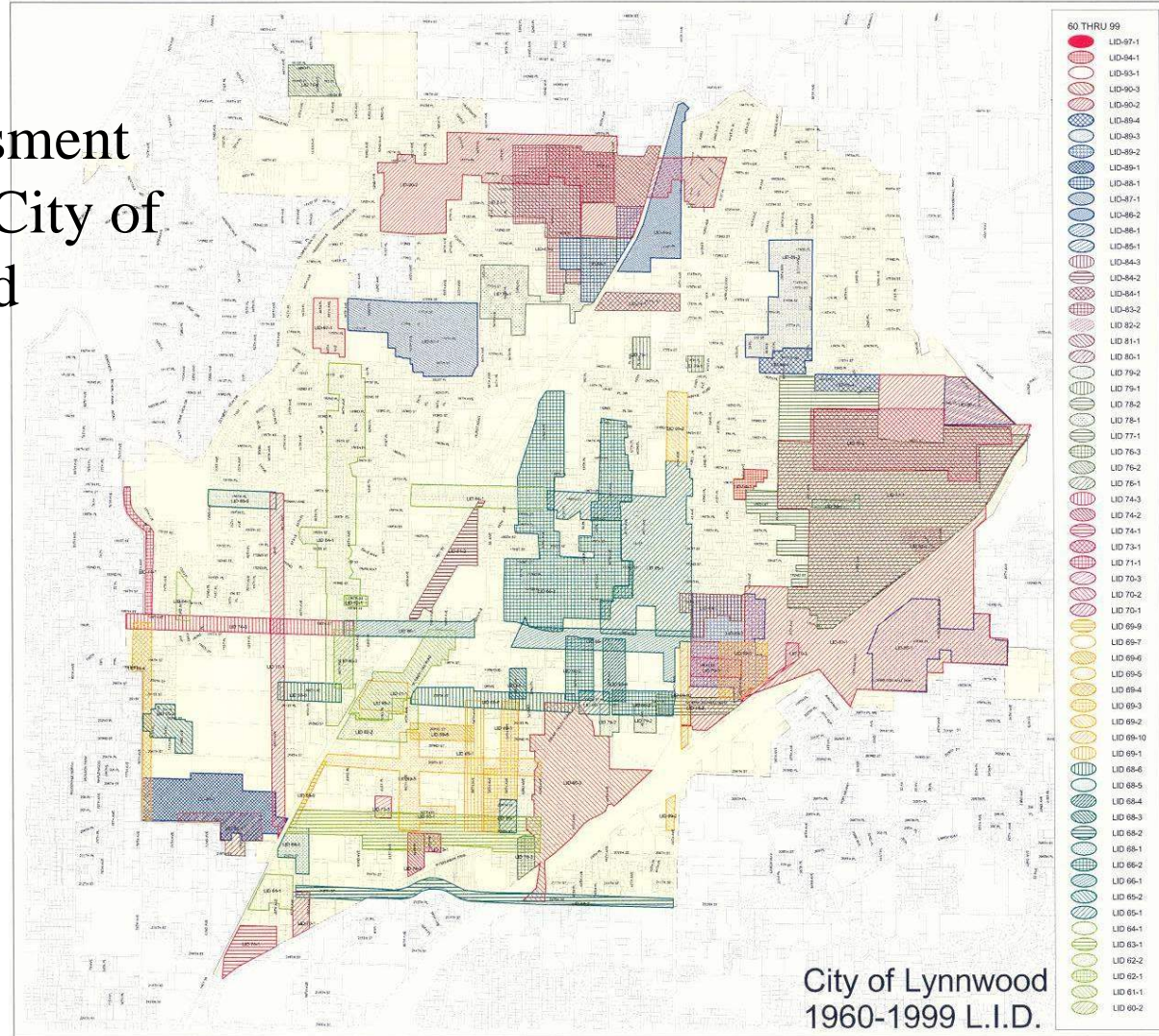
- **Feasibility**
 - Public facilities may be needed to make development projects feasible.
- **Benefit**
 - Public Facilities may add value to property.
- **Impact**
 - Development may create the need to expand the capacity of public facilities.

Nothing New About Developer Contributions

- All of the infrastructure of large developments are commonly built by the original developers.
- Much of many city park systems came as part of subdivisions or donations to enhance market appeal (Auburn).
- Much of the infrastructure in the Green River Valley industrial areas was financed by LID in the 70s and 80s.
- In many cities as much as 60 to 70% of the utilities may have been provided by developer contributions.
- 1930s have been referred to as the heydays for special assessment districts.

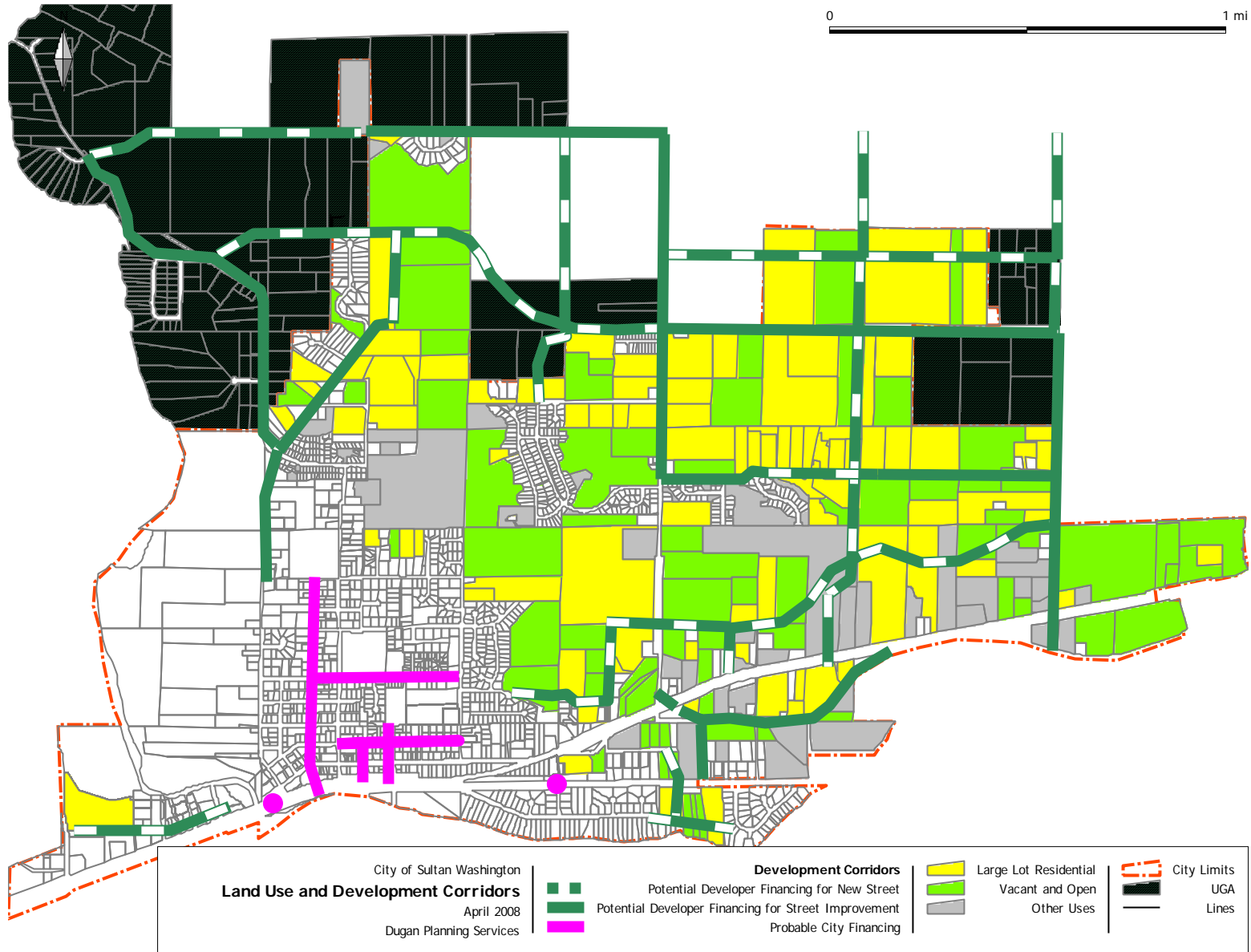
Nothing new about developer contributions

Special Assessment Districts in the City of Lynnwood

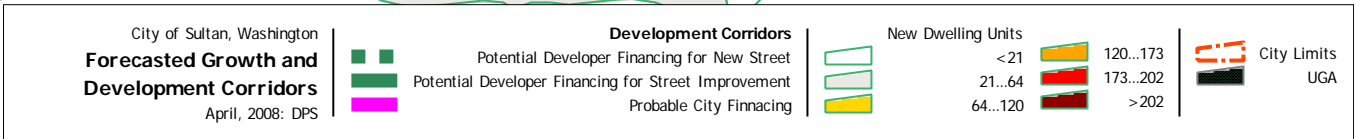
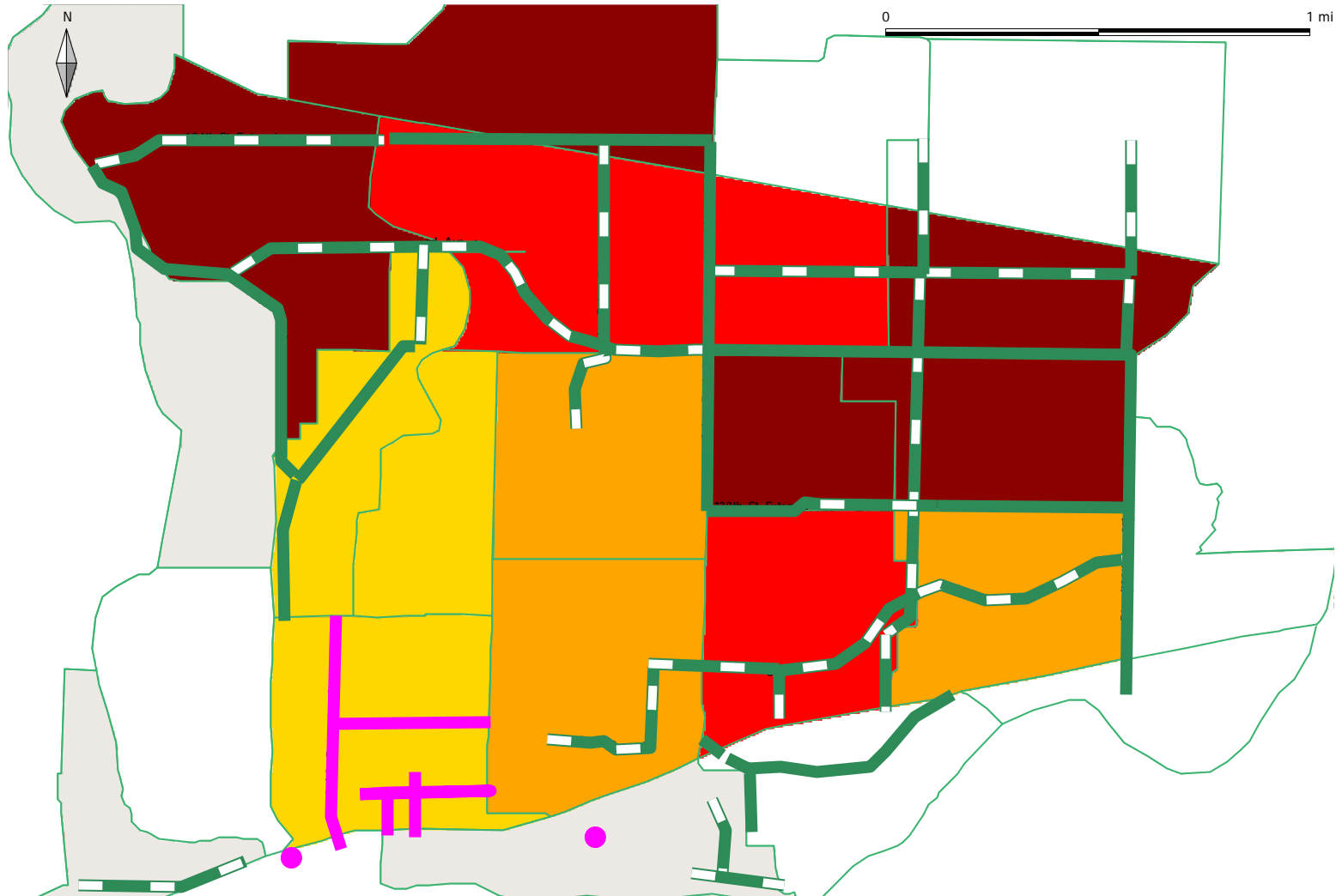


Main Developer Financing Tools

- Direct Construction
 - Developer extension agreements
 - Late-comers Agreements
- Local Improvement Districts
- Impact Fees
- Case by case mitigation
 - Voluntary Agreements
 - Agreements to participate



For illustration purposes only.



For illustration purposes only.

Major Challenge For Developer Contributions

- Development is needed to provide revenue to support on-going operations.
- But developer financing is needed to fund necessary facilities to support development.
- **Therefore the dilemma and challenge is how to balance the need for developer financing without discouraging development too much.**

Summary

- General operating revenues will be needed for operations.
- While there will be substantial funds from city capital revenues, it will not be to meet needs.
- Grants can only supplement city revenues.
- While there is substantial debt capacity, the potential amount that can be generated will be constrained by voter approval.
- The funding strategy will need to rely heavily developer financing for facility extensions into undeveloped areas.

Next

- Compare potential revenues to unconstrained needs.
- Recommend **realistic measures** to make up deficit, including but not necessarily limited to:
 - General adjustments to rates, fees and charges.
 - Allocation of REET between needs.
 - Policies regarding developer financing.
 - Revise **level of service or project needs** list.
- Recommend overall **2025 Financing Strategy**.
- Recommend Six Year Financial Plan based on strategy.