

## MEMORANDUM

TO: Mayor Mike Rosen, City of Edmonds, WA

FROM: The Mayor's Blue-Ribbon Panel

SUBJECT: Executive Summary - Recommendations and Conclusions

DATE: June 28, 2024

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This memorandum represents our recommendations and conclusions as we complete the tasks that you have asked of us in our work with the City of Edmonds (City). We appreciate your support for this work, the openness to our questions and the transparency with which you and your staff have approached these challenging issues.

### **Our Charge**

You convened the "Mayor's Blue-Ribbon Panel" (the Panel) in response to the Edmond's City Council's declaration of a "fiscal emergency" in the context of their financial policies. In forming the Panel you asked that we:

1. Ascertain the City's financial condition with a focus on the City's General Fund,
2. Determine how the City found itself with this problem,
3. Make recommendations with regard to correcting the situation,
4. Make recommendations for the City's financial and budgetary practices that would help return the City to long-term financial health.

### **Our Methods**

The Mayor and Panel determined to use the Government Finance Officers Association (GFOA) Fiscal First Aid methodology. This is a "12 step" process and serves as the construct for the "12 Step Project Plan" which is one of the work products attached to this memorandum. The Panel worked through the topics and issues that the 12-step approach raises. This represents a very comprehensive method to evaluate issues such as this. The Panel's work included reviewing past and current budgets, requested and reviewed additional deeper analytics of certain expenses (professional services, employee additions, compensation, etc.), review of the fire & EMS service options, and various "what if scenarios".

The topics and issues incorporated into the 12-step approach led the Panel to investigate many and numerous elements of the City's fiscal planning and management practices.

### **Specific Responses to the Charge to the Panel**

1. Ascertain the condition of the City's financial condition with a focus on the City's General Fund,  
The City's actual ending fund balance in the General Fund at the end of 2023 is \$2.492 million. This is compared to the budget estimate of \$3.047 million.
2. Determine how the City found itself with this problem,  
As illustrated in the table below, expenditures were in excess of revenues in years 2020 through 2023 by a total of \$13.9 million. More information about the details of this element

is both below in this memo and in the original memo dated February 20, 2024.

ACTUAL (thousands)	Final Budget 2019	Actual 2019	Final Budget 2020	Actual 2020	Final Budget 2021	Actual 2021	Final Budget 2022	Actual 2022	Final Budget 2023	Actual* 2023
Revenues	41,113	42,263	42,576	40,937	42,190	43,697	45,080	41,637	52,599	50,005
Expenditures	44,151	41,212	46,693	43,332	45,864	41,726	53,791	45,422	63,984	59,677
FB effect	(3,038)	1,051	(4,117)	(2,395)	(3,674)	1,971	(8,711)	(3,785)	(11,385)	(9,672)
* unaudited / preliminary										
Revenue differences		1,150		(1,639)		1,507		(3,443)		(2,594)

Budget deficits have continued with current expenditures in the 2024 budget being approximately \$12.5 million more than expected revenues as illustrated in the table below.

Decisions	Impact (millions)
RFA funding from ARPA	\$6.25
Contra-Account*	3.20
Sub-Total “Problem”	\$9.45
Additional Unbudgeted Impacts	
Examples: Negotiated union contract, additional police cars and technology, replenishing deferred bldg. maintenance fund, library repairs, new financial software, staff additions, staff salaries	3.05
Revised Sub-total “Problem”	\$12.50
Used Reserve Funds **	\$8.00

\* The non-departmental budget included an off-set to authorized expenditures, a negative budget amount of \$3.2 million which represented open staff positions at the time, as a budget balancing action.

\*\* Reserve Funds to be replenished up to required Reserve Funds levels as prescribed by current City Council policy

3. Make recommendations with regard to correcting the situation - See below
4. Make recommendations for the City’s financial and budgetary practices that would help return the City to long-term financial health - See below and the detailed Fiscal First Aid 12 Step Project Plan.

**Summary of Observations and Recommendations**

The following is a summary of our observations and recommendations. More detail on each is found in the attachments. The attachments include:

1. Fiscal First Aid 12 Step Project Plan – this describes the responses of the Panel in the context of the GFOA’s detailed Fiscal First Aid 12 step methodology elements. This Plan has attachments as well which document answers to certain questions within the Project Plan.
2. Strategic Approach to Fiscal Resiliency – A series of recommendations for future steps to help resolve the current fiscal emergency and set the stage for assuring the City avoids similar problems in the future.
3. Financial Health Model – A financial planning model that provides historical context and enables modeling various alternative approaches to financial planning for the future. The

Panel recommends that the City makes a habit of evaluating decisions of significance that have fiscal implications with this model.

**Observations –**

**Fund Balances in the General Fund are Far Below Required Policy Targets.** The City finds itself with fund balances in its General Fund below policy target levels largely due to additions to authorized expenditures which occurred in the 2022 and 2023 budget processes. Additionally, these increased expenditures were augmented with additional authorized expenditures in budget amendments in both years. Revenues were not increased nor were sources of funding for the budgeted increases in expenditures identified at the time of the proposed budget amendments. As a result, expenditure budgets have exceeded revenue estimates by almost \$20 million during the most recent two-year period.

**Revenue Estimates Were Overstated.** Revenue estimates were overstated in 2020, 2022 and 2023 in a cumulative amount of \$7.6 million. Revenue estimates are the basis for balancing a budget against authorized expenditures. Therefore, if it weren't for staff underspending the authorized budgets, deficits in these three years could have been as high as \$27.6 million. Spending was less than budgeted amounts by \$16 million during these three years which meant that expenditures exceeded revenues by \$11.6 million – still a significant problem.

**Sufficient Information Was Not Available to the Council to Make Proper Decisions.** Revenue estimates were not adequately documented which limited the potential for scrutiny of the estimates. Long-range forecasts were provided but contained no insights into the assumptions (which proved to be unrealistic). Inadequate documentation and discussion occurred when budget amendments were proposed. Amendments in 2020-2023 amounted to a net increase of expenditures above revised revenues of \$11.3 million.

**The Budget Process and Related Software Systems are Antiquated.** The City has been embarking on an update to their core financial systems for years (the system was purchased by another company in 2004 and subsequently discontinued). The City financially committed to a contemporary budget development and transparency system two years ago but never implemented the software. The software subscription costs are being paid by the City with no benefit from the systems. No centralized procurement systems are in place. No methods to evaluate the effectiveness of City programs using program metrics exists. An apparent lack of collaboration within City operations at several levels likely contributed to inefficient services to the community.

**Recommendations** – A detailed series of recommendations are incorporated into the project documents attached to this memorandum.

The current budget imbalance needs to be resolved with a combination of:

1. **New sources of non-tax revenues:** Red light cameras, increased fees, and other revenue increases,
2. **Expense reductions:** head count reductions, furloughs, professional service and other non-compensation reductions,

3. **New taxes:** The 1% annual increase for EMS, and GF should be done for 2025 and 2026. Additional property levy for GF and / or joining SCF will require a vote and would not impact the revenues until 2026.

(Note: with the lag of significant revenue increases until 2025, The Panel recommends “bridging” the 2025 budget with borrowing internally from available surplus resources in other City funds).

**A summary of detailed recommendations include:**

1. Continue generic treatments already implemented
  - a. Scrutinize hiring and limit to only essential positions;
  - b. Monitor overtime use and limit as appropriate;
  - c. Evaluate transfers to reserve replacement funds until fiscal stability is achieved;
  - d. Scrutinize expenditures above a prescribed threshold, currently at a recommended \$1,000;
  - e. Do not increase budget authority (amendments) without a corresponding increase in anticipated revenues unless absolutely necessary;
2. Develop a Financial Health Model
  - a. Such a model has been developed by the Panel and is attached,
  - b. Determine if it is in the community’s best interest to have relatively high reserve level targets for the City’s general government, especially in the context of the current challenge to rebuild them;
3. Develop and evaluate a monthly cash-flow model
  - a. Such a model is developed and is now in use by the Finance Committee;
4. Develop financial policies that clarify boundaries and guidelines
  - a. Certain financial policies have been developed and are being considered by the Finance Committee;
  - b. Develop citywide procurement policies that improve the efficiency, clarify City systems and improve accountability,
  - c. Once policies are in place, illustrate the status of compliance in future budgets and determine how best to hold parties accountable for compliance;
5. Incorporate future operating budget impacts into the evaluation of capital improvements and ensure adequate resources will be available to support the operations and maintenance of capital improvements before they are approved;
6. Utilize a contemporary approach to budget development such as Priority Based Budgeting (PBB)
  - a. Incorporate a method to stratify City programs to inform budget choices and stop or reduce low priority services,
  - b. Improve internal collaboration,
  - c. Obtain objective evaluations of the value to City programs and related costs to the community,
  - d. Scrutinize certain expenditures using a “zero-based” model (do not assume the current level of funding is correct),
  - e. Develop performance measures that enable evaluation of the effectiveness of City programs and incorporate into the budget process;
7. Evaluate revenues in the context of the “price of government” (POG)

- a. Emphasize the taxpayer / ratepayer perspective when evaluating alternative revenue scenarios,
  - b. Improve transparency in revenue forecast estimates;
  - c. Understand the level of general government subsidy for each City program,
  - d. Determine if the available general government revenues are sufficient to provide for the desired service levels where gaps exist between program revenues and program costs,
  - e. Evaluate current City assets and determine the most effective means of meeting the City's needs with these assets (some might be sold, consolidated or repurposed),
  - f. Propose enhancing general government revenues if necessary;
8. Make updating related technology a priority;
  9. Evaluate the degree to which maintenance has been deferred on City assets such as buildings, roadways and systems,
    - a. Consider a funding strategy that maintains City assets properly,
    - b. Develop a bond strategy to address the long-term capital needs of the City;
  10. Incorporate risk assessment and management while implementing these recommendations
    - a. The level of change being recommended is high which increases risk,
    - b. The nature of the changes are complex and increase risk,
    - c. Insufficient training and technology tools are in place which raises risk;
  11. Develop a communication plan to achieve a high level of transparency of this work and the implementation of recommendations
    - a. Consider establishing a standing City commission or committee to observe and advise the City on financial matters,
    - b. Rebuild public trust in the City's ability to manage fiscal health.
  12. Evaluate if costs (including payroll) are being incurred in the general fund to oversee and supervise activities of other funds, such as the utility funds. Such costs should be transferred to the specific fund and then considered in determining needed revenue of the specific fund
  13. Investments:
    - a. Review performance returns of each of the cities investments and strive to increase returns without incurring more risk. Example, A substantial balance until very recently was invested in the Snohomish County LGIP earning less than half the rate of the Washington State LGIP at 5.41%.
  14. Budgeting and future year forecasts should include investment in capital expenditures that are anticipated to be funded by general fund revenues.
  15. Capital Budgets, including all funding sources and impacts on general and other funds ongoing maintenance of such investments should be forecast for a 5 year period and updated each budget cycle.

A significant community service involves fire and Emergency Medical Services (EMS). The City has moved from an in-house model to a contract with the South Snohomish County Regional Fire Authority (RFA). While the contract has become more expensive over time the RFA has determined that the contract payments are insufficient to cover the costs. Consequently, the RFA provided notice that the contract would be terminated at the end of 2025. While this is a significant

community service and a large budgetary expense, the Panel does not believe the problems it was asked to evaluate were significantly impacted by the contract with the RFA. The Panel recommends that these matters be resolved independently of each other.

**Conclusion**

It was appropriate for the City Council to declare a fiscal emergency last October. The severe depletion of the City’s fund balances and reserves is a legitimate concern. The degree of the financial challenges that the City is facing should not be underestimated. The work to restore financial stability will be difficult and it will be important for the administration and the Council to do the difficult work in a timely fashion to achieve that goal. The impact on taxpayers and ratepayers could be significant if the City chooses to propose revenue increases and the impacts of services level reductions need to be weighed should the City include expenditure reductions. These decisions should be considered carefully.

Even though the complexity of the fiscal emergency presented a significant challenge to the panel to conduct its work in a timely and thorough manner, we were determined to be systematic and complete in our efforts.

In closing, we want to express our appreciation for the support and space provided in order for us to complete these tasks and we encourage the City to stay diligent in its efforts to improve the long-term fiscal health of our City. Edmonds has a lot to offer and we recognize this can only be realized with a fiscally strong and stable city government.

**Attachments:**

1. Strategic Approach to Fiscal Resiliency
2. Fiscal First Aid 12 Step Project Plan
3. Financial Health Model
4. Memorandum to Mayor Rosen from Mike Bailey  
re: Report of Findings to Date (February 20, 2024)
5. “Price of Government” descriptions
6. Blue-Ribbon Panel Members