



MAY 2020 COVID-19 STRESS TEST ON OPERATING REVENUES AND 10 YFSM UPDATE

Executive Summary – Impacts and Response:

Council received a report of staff's preliminary estimate of the potential financial impacts at its meeting on April 20, 2020 (April update). This report contains the first update to that preliminary estimate including a scenario from our 10 Year Financial Sustainability Model (10YFSM) that incorporates factors from the Puget Sound Economic Forecaster at Western Washington University (PSEF) April Update. PSEF will be providing its next economic update in late-June that will serve as the foundation for the 10 YFSM upon which the 2021-2022 proposed biennial budget will be developed. We anticipate that next forecast will be influenced by actual experience; however, there will be much that remains unknown. Staff will continue to monitor actual experience closely in order to respond as quickly as possible should greater-than-anticipated losses be realized. The following is a high-level summary of the impacts and planned response, which is discussed in detail in this report:

	2020	2021	2022
Previously Forecast Surplus	\$0.874M	\$0.817M	\$0.785M
- Forecast Revenue Loss	(\$7.591M)	(\$2.530M)	(\$1.727M)
- Forecast Expenditure Increase	\$0.000M	(\$0.273M)	(\$0.325M)
+ Implemented Expenditure Containment	\$0.527M	\$0.000M	\$0.000M
= Forecast Operating Budget Shortfall	(\$6.189M)	(\$1.986M)	(\$1.267M)
+ Strategies to Address Shortfall*:			
2019 Revenue Surplus	\$3.000M		
2019-2020 One-Time Supplemental and Operating Expenditure Reductions	\$3.641M		
Ongoing Operating Expenditure Reductions	\$0.000M		
Use of Revenue Stabilization Fund	\$0.000M		

The Strategy to address the 2020 shortfall uses a variety of one-time tools and the details are found on page 7 of this report. Ongoing strategies to address forecast shortfalls will be identified during the 2021-2022 biennial budget process and presented as part of the proposed budget.

Modeling Using a Stress Test:

Assessing the impact and being able to effectively model revenues is essential for the City Council to take the necessary immediate and long-term actions to maintain financial sustainability. As discussed in the April update the City began its evaluation of economic impacts by evaluating the following potential recovery scenarios:

Little "v" Recovery

- Rebound is swift, but not easy
- Short-term, quick fixes could bridge the gap to recovery

Big "V" Recovery

- Downturn is deeper, but bounce back is rapid
- Short-term bridge strategies apply

"L" Recovery

- Recovery is stalled by deeper economic woes
- Long-term transformation strategies needed ASAP

Real GDP numbers for the first quarter were just released and reported a 4.8 percent real GDP decline in the first estimate indicating that we are in recession. The Fed's modeling forecast nearly 47 million Americans losing their jobs temporarily in the second quarter. We already know that Washington lost over 550,000 jobs in March and April with unemployment of 15.4% for April. Within the three zip codes that mainly encompass Shoreline (98133, 98155, 98177), but do overlap with other cities, there have been over 15,000 initial filings for unemployment. As of May 9, Shoreline's unemployment rate is estimated to be 14.7% to 24.4%.

Economists are now predicting that the recovery will take on the "L" shape with economic activity. However, each revenue source is impacted and will recover differently, and this and future updates of the 10 YFSM takes these stress factors into consideration. The update for the budget process will include incorporating changes to the projected revenue and expenditure forecast based upon updated economic indicators and actual experience.

While this update incorporates additional sources of data, we caution that there continues to be a hefty dose of uncertainty built into this forecast that will later be revised as actual data provides a greater indication of the local impact of a socially distanced economy. Some anticipated impacts that are not addressed in this update include the Fall 2020 and 2021 impacts on parks and recreation program revenues, as well as impacts on gambling tax, and gas tax revenues through the next biennium. We monitor these revenue streams closely.

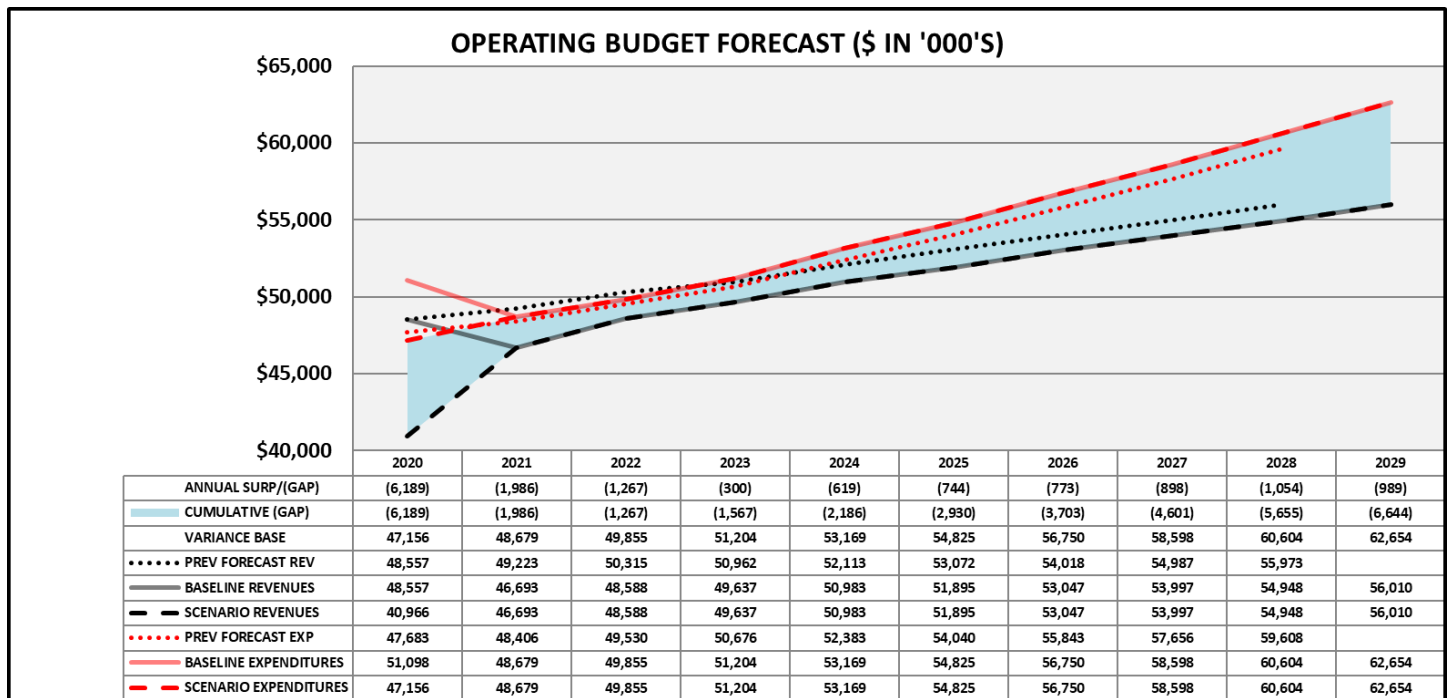


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May 2020 COVID-19 Stress Test and 10 YFSM Update:

The current plan for 2020, as included in the adopted budget through Ordinance No. 883, provides a surplus of approximately \$0.9 million with revenues of \$48.6 million, ongoing expenditures of \$47.7 million, and the use of \$3.4 million of fund balance supporting one-time expenditures. This preliminary update of the forecast *Scenario Revenues* line in the chart below reveals an anticipated \$7.6 million loss of budgeted revenues. However, with operating revenues falling to \$41.0 million, there is a shortfall of \$6.2 million from operating expenditures currently planned to be reduced to \$47.2 million. The 2021-2022 biennium was forecast to provide a surplus of \$1.6 million but this update forecasts a \$4.9 million loss of revenue resulting in a shortfall of \$3.3 million.

This update does not anticipate the result of a successful levy lid lift in 2022 for the six-year period of 2023-2028. A successful levy lid lift in 2022 resetting the levy rate at \$1.51/\$1,000 assessed valuation (a \$0.32, or 27%, increase from the forecast levy rate for 2023) would balance 2023-2028. Staff have identified a plan to address the shortfall for 2020. Should Council choose to use the Revenue Stabilization Fund to backfill the 2021-2022 shortfall, the levy rate would likely need to be set at a higher rate since that would be the only revenue source available to replenish the Revenue Stabilization Fund as required by the City's Financial Policies.



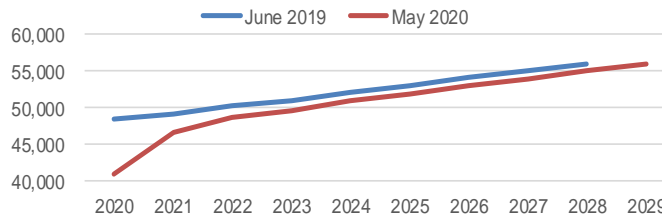


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The table and chart below compares ongoing operating revenues forecast (\$ in '000's):

Projection	2020	2021	2022	2023	2024
June 2019	48,557	49,223	50,315	50,962	52,113
May 2020	40,966	46,693	48,588	49,637	50,983
Change	(7,591)	(2,530)	(1,727)	(1,325)	(1,130)

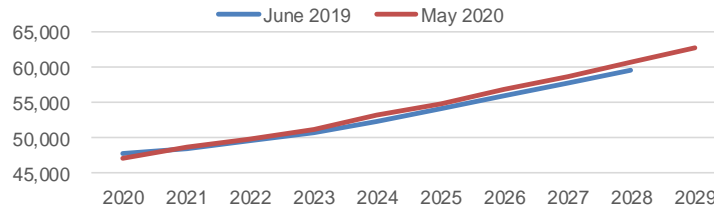
Projection	2025	2026	2027	2028	2029
June 2019	53,072	54,018	54,987	55,973	#N/A
May 2020	51,895	53,047	53,997	54,948	56,010 #
Change	(1,177)	(971)	(990)	(1,025)	#N/A



The table and chart below compares ongoing operating expenditures forecast (\$ in '000's):

Projection	2020	2021	2022	2023	2024
June 2019	47,683	48,406	49,530	50,676	52,383
May 2020	47,156	48,679	49,855	51,204	53,169
Change	(527)	273	325	528	786

Projection	2025	2026	2027	2028	2029
June 2019	54,040	55,843	57,656	59,608	#N/A
May 2020	54,825	56,750	58,598	60,604	62,654
Change	784	907	942	996	#N/A



Long-Term Budget Trends and Assumption in the 10 YFSM:

Below are some of the major assumptions used in the most recent projections:

- Property Tax:** Property tax, while considered relatively stable, is subject to each property owners' ability to pay so staff anticipates the City will experience a greater-than-historical level of delinquencies. Therefore, staff has incorporated a 10% delinquency factor for 2020 collections, which results in an estimated \$1.39 million shortfall in 2020. The forecast for property tax has decreased from the previous forecast based upon the updated inflation, assessed valuation and new construction assumptions for King County.
 - Inflation:** The levy lid lift approved by Shoreline voters limits the growth in the annual property tax levy to the rate of inflation plus new construction. Previously, inflation was forecast at 2.4% in 2021 and 2.2% in 2022. Inflation is now forecast at 2.1% in 2021 and 2.3% in 2022. This serves to reduce the amount to which the levy is forecast to grow prior to the addition of new construction assessed valuation. Once the levy lid lift expires in 2022, the annual levy will only be allowed to grow by new construction plus the statutory 1.0% limit.
 - Assessed Valuation:** Previously, the City's assessed valuation was forecast to increase 4.5% in 2021 and 3.0% in 2022. The City's assessed valuation is now forecast to increase by 1.7% in 2021 and 0.6% in 2022. This will not have much effect on the property tax levy forecast as there is enough room in between the existing levy rate and \$1.60 limit to allow for adjustment of the levy rate caused by this less-than-previously-forecast assessed value.
 - New Construction:** New construction valuation for 2021 and 2022 is forecast to be \$63.7 million for 2021 and \$68.6 million for 2022. It is important this is approximately 50% of the amount of new construction added to the rolls in the 2019-2020 biennium.

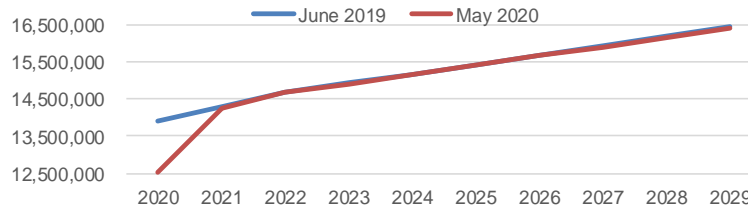


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The assumption presented above result in property tax revenue that is forecast to increase by 2.4% in 2021 and 2.9% in 2022, with average increases of 1.8% for 2021-2028. Below is a comparison of the June 2019 forecast to the April 2020 forecast:

Projection	2020	2021	2022	2023	2024
June 2019	13,916,110	14,296,409	14,695,970	14,929,986	15,169,878
May 2020	12,524,499	14,253,900	14,666,273	14,903,486	15,145,894
Change	(1,391,611)	(42,509)	(29,698)	(26,500)	(23,984)

Projection	2025	2026	2027	2028	2029
June 2019	15,416,484	15,667,227	15,921,235	16,180,351	16,438,580
May 2020	15,396,660	15,647,983	15,900,139	16,154,116	16,404,381
Change	(19,824)	(19,245)	(21,096)	(26,234)	(34,199)



- **Sales, Business & Occupation, and Gambling Taxes:** The significant downturn in business activity resulting from closing businesses or severely restricting operations is resulting in decreased state and local tax revenues (e.g., Sales, Local Criminal Justice Sales, Business & Occupation, and Gambling taxes).
 - **Sales Tax:** The projection for sales tax for 2020 has decreased from the previous forecast based upon the updated retail sales growth assumptions for the Puget Sound region. Taxable retail sales throughout the Puget Sound region and King County are expected to decline from the 2019 level by 13.6% and 16.5%, respectively. Staff's forecasting practice assumes that most of the Retail Trade sector's activity will change at 75% of the growth assumptions for the Puget Sound region.

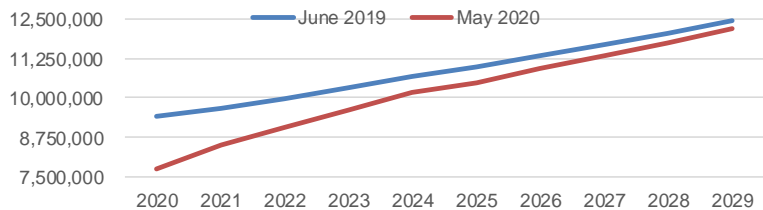
When comparing 2019 and 2020, the budget for 2020 anticipated growth in Retail Trade sales tax and total sales tax collections of 3.0% and 3.2%, respectively. The previous forecast anticipated growth from 2019 in Retail Trade sales tax by 4.1% but a decline in total sales tax collections by 6.5%, largely reflective of an anticipated decline in Construction sales tax collections from the high level we were experiencing at that point in 2019. The April 2020 forecast reveals an estimated decline of 12.9% and 29.5%, respectively.

Projection	2020	2021	2022	2023	2024
June 2019	9,391,258	9,669,234	9,981,484	10,303,041	10,648,610
May 2020	7,713,646	8,472,404	9,066,678	9,615,337	10,183,432
Change	(1,677,612)	(1,196,830)	(914,806)	(687,704)	(465,178)

Projection	2025	2026	2027	2028	2029
June 2019	10,991,380	11,338,099	11,694,615	12,062,599	12,442,252
May 2020	10,448,330	10,908,593	11,323,026	11,738,238	12,166,224
Change	(543,049)	(429,507)	(371,589)	(324,361)	(276,029)

A more relevant comparison worthy of discussion is the results from the April 2020 forecast to the previous forecast for 2020. It is anticipated that 2020 collections will come in 17.9% less, which results in an estimated \$1.68 million shortfall.

To the right is a comparison of the June 2019 forecast to the April 2020 forecast for Sales Tax.

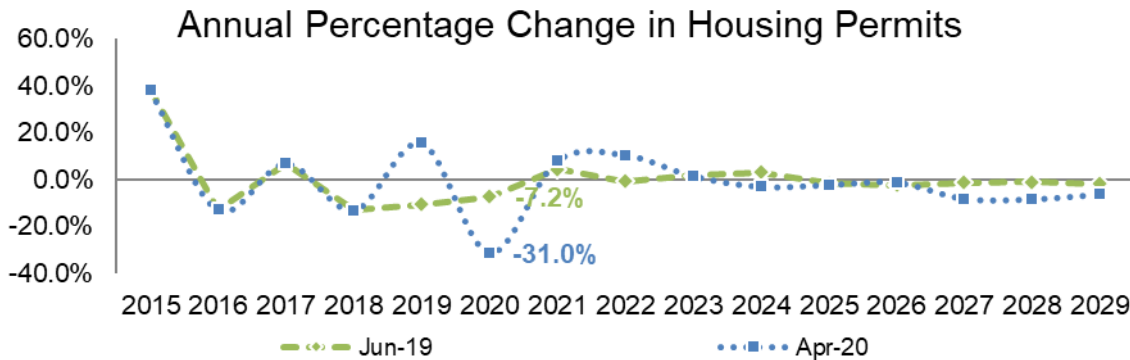


- **Local Criminal Justice Sales Tax:** King County taxable retail sales are expected to be 21.2% less than previously forecast, which results in an estimated \$0.35 million shortfall.
- **Business & Occupation Tax:** Staff anticipates that Business & Occupation Tax collections will experience a shortfall like that for Sales Tax of \$0.19 million.
- **Gambling Tax:** The closure of gaming establishments for much of the second quarter and anticipation that, were the economy to reopen this summer, that there will be a slow return to the normal level of activity in third and fourth quarters results in an estimated shortfall of \$1.05 million.

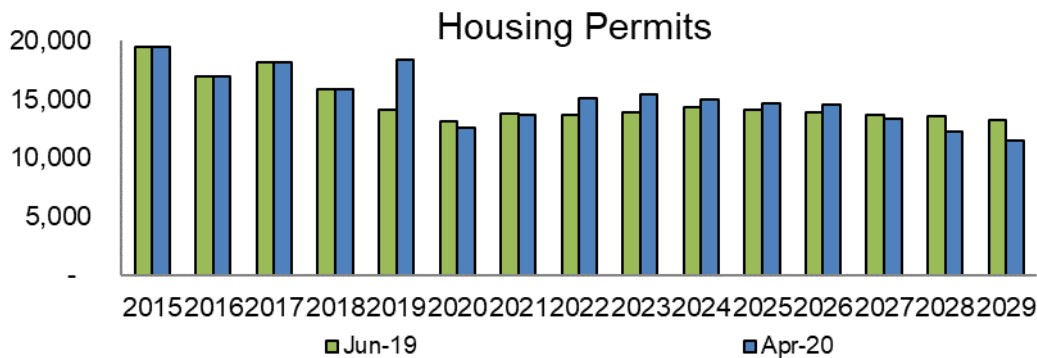


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- Recreation and Aquatics:** The closure of the City's recreation facilities for the months of March through May is estimated to result in a loss of registration and rental revenue of \$0.375 million, which is partially offset by a \$0.134 million of directly related expenditure reductions. Summer programming planned for the months of June through August has been cancelled. Staff estimates a loss of revenue totaling \$0.840 million, which is partially offset by directly related expenditure reductions totaling \$0.393 million. Staff are analyzing the impact of the decisions to cancel summer celebrations, neighborhood events, and recreation classes, as well as the redesign and limiting of participants for summer day camps. This forecast includes a preliminary net revenue loss of \$0.688 million.
- Housing Permits:** The June 2019 forecast assumed the number of permits issued in 2020 would be 7.2% less than that forecast for 2019. Updated assumptions for the April 2020 forecast anticipate a 10.8% year-over-year decrease. The number of housing permits issued in 2019 came in 28.9% more than that forecast in June 2019. This indicates that updated assumptions for the April 2020 forecast anticipate a 31.0% decrease from 2019.



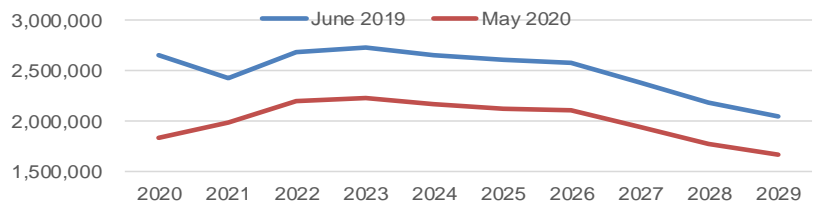
The April 2020 forecast still anticipates fewer housing permits to be issued each year through 2029 as compared to any of the past five years. Staff are continuing to evaluate options for forecasting the impact of COVID-19 on future permitting revenues.



Development fees will likely be impacted in the near-term by the closure of City Hall but may also be impacted in the long-term if the ability to finance development projects is curtailed. Not related to COVID are anticipated permits for affordable housing and Deep Green projects that will have significant reductions in permit fees that are not yet incorporated into the forecast. To the right is a comparison of the June 2019 forecast to the May 2020 forecast for development revenue:

Projection	2020	2021	2022	2023	2024
June 2019	2,649,483	2,426,540	2,685,173	2,730,829	2,653,032
May 2020	1,827,358	1,977,967	2,188,789	2,226,005	2,162,590
Change	(822,125)	(448,573)	(496,384)	(504,824)	(490,442)

Projection	2025	2026	2027	2028	2029
June 2019	2,598,993	2,572,688	2,368,454	2,175,741	2,044,320
May 2020	2,118,541	2,097,099	1,930,619	1,773,531	1,666,405
Change	(480,452)	(475,590)	(437,835)	(402,210)	(377,915)





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- Fuel Tax:** Revenue from Fuel Tax is based on the number of gallons sold, not the dollar value of the sales. Therefore, the 2020 distribution will be impacted in the near-term by the Stay Home – Stay Healthy Order but may also be impacted in the long-term like the decline in consumption experienced during the Great Recession. Fuel Tax distributions to Shoreline are anticipated to be 29.2% less than previously forecast, which results in an estimated shortfall of \$0.640 million.

Impacts on Cash Flow:

Staff continue to monitor cash flow closely. April property tax collections were not noticeably impacted by the extension for tax filing primarily due to the large reliance on escrow accounts. Potential impacts are more likely anticipated in October. Sales Tax receipts experience a two-month lag, so impacts are not yet apparent. The City remains in a strong cash position and anticipates being able to manage any short-term cash flow impacts.

Non-Operating Fund Impacts:

The City's Capital Funds rely heavily on Real Estate Excise Tax (REET) to fund Transportation, Parks and General Capital Projects. Comparing updated modeling of potential REET impacts to the forecast presented in the City's 2019-2024 Capital Improvement Program reveals a potential for collection greater than that previously forecast for 2020 and 2021 of approximately \$0.510 million but a shortfall of \$0.951 million for 2022-2024. Collections from the City's Voted Transportation Benefit District (TBD) Sales Tax, which funds the expansion of the City's Sidewalk system, may come in less by \$491,000. While this impact is not anticipated to affect Shoreline's ability to cover debt service on the bonds that were issued in 2019 or the commitment complete specifically identified projects, it will likely reduce the amount of sidewalk expansion Shoreline can finance in the future.

Summary and City Response:

In summary, as a result of the impacts of the COVID-19 pandemic and the Stay Home – Stay Healthy Order, Shoreline's 2020 operating revenues may experience a loss of \$7.6 million, or 15.6%, of budgeted operating revenues. Because the budget anticipated a surplus, the actual budget shortfall is forecasted at \$6.2 million. The City is planning to use a combination of strategies to address the shortfall including revenue collected in excess of budget, 2019 expenditure savings, and anticipated 2020 expenditure savings including to reductions in travel and training, and operating and project related expenditures that are impacted by the COVID-19 response. Our current plan (details in table) appears to adequately address the forecasted budget deficit and provide approximately \$0.4 million safety net for changes to in the forecast.

Shoreline is fortunate that, due to the strong financial policies adopted by Council, it is in a good position from a cash and reserve perspective with sufficient fund balance for the General Fund that exceeds reserve targets as well as a fully funded Revenue Stabilization Fund, commonly referred to as a rainy-day reserve. Despite this strong position, the current forecast clearly reflects that impacts will be felt for several years to come. To that end, we are preparing our 2021-2022 budget with the anticipation that some ongoing reductions will be necessary and that use of the revenue stabilization fund is likely. Council guidance and full discussion of the options and plan to maintain long term financial sustainability will be a major focus of the 2021-2022 budget process.

COVID 19 Impact Action Plan	2020
Forecasted Operating Budget Shortfall	\$6,200,000
Additional Estimated Costs Related to COVID -19	\$1,700,000
Estimated Total Impact	\$7,900,000

Strategies to Address Shortfall

2019-20 One-Time Supplemental and Operational Expenditure Reductions

2019 Jail Housing Savings	(568,000)
2019 Unspent Operational Contingency	(884,439)
2019 Unspent Insurance Reserve	(255,000)
2019 Departmental Savings	(589,425)
2019-20 One Time Supplemental Request Reductions/Deferrals	(705,147)
2020 Anticipated Savings/Expenditure Reductions	
Contingency	(20,000)
Fuel Savings	(30,000)
Professional Services	(61,000)
Anticipated Project Savings	(200,000)
Special Events	(74,382)
Street Light Electricity	(105,000)
Travel & Training	(131,094)
Miscellaneous	(17,250)
	<u>(638,726)</u>

2019-20 One-Time Supplemental and Operational Expenditure Reductions Total (3,640,737)

2019-20 Revenues/Resources

2019 Operating Revenues Surplus	(3,000,000)
2020 Anticipated FEMA/CARES reimbursement*	(1,700,000)
Total 2019-20 Revenues/Resources	(4,700,000)

Total Strategies to Address 2020 Shortfall (8,340,737)

Balance of Shortfall to fill/ (Surplus over Shortfall) **(440,737)**

*Assumes that CARES Relief Funding will cover costs that FEMA will not cover (Premium Pay, PPE, Community & Business Support, etc)