State of the Cities

Fall 2009 Report
An update on the fiscal health of cities and towns



State of the Cities Report Fall 2009

The Mission of the Association of Washington Cities is to SERVE our member cities and towns through advocacy, education and services.

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Weathering the Great Recession—An introduction

Throughout the last decade, Washington's cities and towns have stretched revenues to meet the most basic, critical community services. But as 2008 came to a close, many cities were feeling the effects of an unprecedented economic downturn and resources became tighter. As budgets were developed for fiscal year 2009, these cities reported making cuts in areas such as infrastructure, a reduction in workforce, and narrowed scope of services.

As we entered 2009, Washington's economic conditions continued to deteriorate. In many communities, new housing development came to a halt, sales tax revenues shrunk, and property assessed valuation declined for the first time in living memory. Unemployment continues to be high. Uncertainty in the banking world created a credit freeze that stifled growth and required many cities to change investment strategies.

For many cities, revenues dropped below the worst-case predictions. To cope, these cities drew down reserves, re-opened budgets to cut more deeply, and made painful choices about where to allocate dwindling resources to serve citizens.

Weathering this storm – and wondering how long it will last – has preoccupied city leaders across the state. This report chronicles what cities are experiencing and how they are coping. Taken as a whole, this information brings into focus the toll this recession is taking on the vital infrastructure – physical, social, economic and civic – that citizens depend on city governments to provide. At the same time, it also shows the resilience, determination, and creativity that city leaders are bringing to the challenge of surviving this severe recession.

Glenn Johnson
President, AWC Board of Directors
Mayor, City of Pullman

"We're in very challenging times. As we start to see some of the good signs of the economy we'll still be feeling the fallouts of the downturn."

~John Hodgson, Chief Administrative Officer, Kent

State of the Cities research methodology

From Krupp, with a population of 60, to Seattle, with a population of 600,000, Washington is home to 281 cities, each with its own unique history, economy and civic culture.

The *State of the Cities* is an ongoing research project designed to communicate the trends and fiscal conditions that affect Washington's cities. Last year's report, *Assessing the Health of Washington's Communities*, presented a comprehensive analysis of our cities' fiscal conditions in 2008, the previous four years and what city officials envisioned for the future.

This report examines how cities coped with the recession this past year. To identify trends and implemented strategies, cities are grouped in 14 clusters, characterized by similarities in:

- Population size;
- Population growth over the last ten years;
- Per capita property assessed value; and
- Per capita sales tax revenue.

These 14 city clusters offer the best analysis for capturing basic similarities and differences in resources and needs.

Cities' structural imbalance compounded by the recession

Even in economic boom times, many Washington cities had a hard time meeting local needs. Several factors combined to trap cities in a structural imbalance where the costs of essential services rise faster than revenues. The recession compounded this imbalance.

Factors contributing to this imbalance include:

- The high costs of important services that cities must pay for – street maintenance and construction, public safety services, emergency management systems, and health care for employees – rise faster than inflation.
- Cities are charged with meeting state and federal mandates. These requirements can include meeting new and more stringent environmental standards and tougher criminal sentencing laws. While citizens and municipal officials often support the intent of these mandates, they can be accompanied by serious costs.
- Property tax, a critical city revenue source, is limited by law to an annual increase of only one percent or the rate of inflation, whichever is less. In most years, this means the allowable increase doesn't keep up with actual costs.
- The sales tax – one of the more volatile city revenue sources – usually nosedives during a recession. This can have severe consequences for city services, including the very services that people need most in hard times.
- Utility and business tax revenues also decline when the economy slows.

"If revenue restrictions don't change, or if the economy gets worse, there will be a very negative impact in a very short time. Expenses are simply rising faster than revenues. If this continues, we will have to decrease our services – contrary to what people in the community want."

John Caulfield, City Manager, Mountlake Terrace

continued on page 5

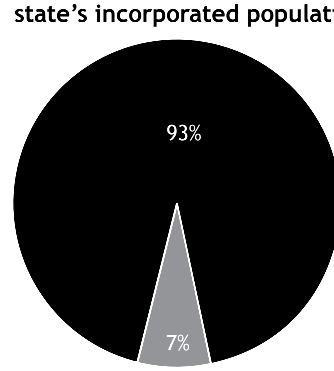
More information about each city cluster can be found on page 4, in the Appendix and on the AWC website.

This report is based primarily on information collected from survey results and interviews. Two online surveys were sent to city officials in June 2009 to elicit specific information about cities' fiscal conditions and various recession coping strategies. One was completed primarily by city managers or mayors; the second was completed primarily by finance directors or clerk/treasurers.

As used in this report, the word "cities" applies to all 281 cities and towns.

Additional data and previous *State of the Cities* reports are available at www.awcnet.org/stateofthecities.

77% of cities took one and/or two of the surveys used for this report, representing 93% of the state's incorporated population



State of the Cities Cluster Characteristics

Non-Metro Area Cities*

Regional Centers – Cluster 1
These large cities in Washington's more rural areas offer the greatest economic opportunities to their residents. However, responding cities indicate the local economy worsened in the past year and they are less able to meet financial needs in 2009 compared to four years ago. *Examples: Centralia, Pullman*

Rural Commercial Centers – Cluster 2
These cities tend to have substantially more commercial activity than their non-metro neighbors. Although many will re-open their budgets before the end of the year to deal with reduced revenues, only half indicate local economic conditions have worsened in the past year. *Examples: East Wenatchee, Shelton*

Tourism Hubs – Cluster 3
Compared to other city clusters, these tourist-based cities have not witnessed economic decline to the same degree. While the majority report being less able to meet financial needs now than in the past (and envision the same for the future), three-quarters have not seen local economic conditions worsen. *Examples: Chelan, Port Townsend*

Light Industrial Hubs/Natural Resources – Cluster 4
These communities, relying on natural resources and/or manufacturing for economic wellbeing, entered tough economic times long ago. In 2004, more than 80 percent reported being less able to meet financial needs compared to five years ago. Only 27 percent report the same for 2009 compared to four years ago. *Examples: Coulee City, Montesano*

Small Residential – Cluster 5
Varying in character from quaint towns to small cities, these communities have relatively low property values and commercial activity, but experienced moderate growth over the past decade. More than 80 percent indicate they will be less likely to meet financial needs in 2010. *Examples: South Cle Elum, North Bonneville*

Rural Communities – Cluster 6
Collectively, these communities have the smallest median operating budgets and populations of any other city cluster. More than half of these officials report the local economy has worsened and more than half will re-open their budget or decreased expenditures due to a reduction in revenues before the end of the year. *Examples: Palouse, Pe Ell*

A list of each city cluster and city membership can be found in the Appendix. More information about each cluster is also available at www.awcnet.org/stateofthecities.

* Clusters one through six contain cities located in non-metro areas as defined by the 2000 U.S. Census. Clusters seven through 14 include cities located in metro areas.

Metro Area Cities*

Largest Cities – Cluster 14
These cities are the state's largest population centers. City officials report experiencing economic decline in the past year and all anticipate they will be less able to meet fiscal needs in 2010. *Examples: Tacoma, Vancouver*

Large Commercial Centers – Cluster 13
Ranging in population, these cities are some of the state's strongest retail centers. Nearly all indicate the local economy has worsened in the past year, requiring the city to re-open the budget or decrease expenditures due to decreased revenues by the end of 2009. *Examples: Lynnwood, Tukwila*

Medium Commercial Centers – Cluster 12
Many of the cities in this group are defined by moderate retail and manufacturing activity. All responding city officials report being less able to meet needs in 2009 than four years ago. More than half anticipate things getting worse next year and nearly 80 percent anticipate greater decline in the ability to meet financial needs in 2013. *Examples: Federal Way, Kennewick*

Small Commercial Centers – Cluster 11
Most of these cities maintain a small town feel, but also generate a significant amount of retail/commercial activity. Because of this reliance on retail activity, more than 80 percent indicate their economy has worsened in the past year. *Examples: Sumner, Yelm*

Mixed Resources – Cluster 10
Characteristics in these communities vary. Most cities experienced high population growth in recent years, putting pressure on municipal services. These city officials report deteriorated economic conditions within the past year; however, only two-thirds indicate being less able to meet financial needs now compared to four years ago. *Examples: Redmond, Issaquah*

High Income Residential – Cluster 9
The cities within this cluster are distinctly residential, with neighborhoods that include the homes of some of the state's wealthiest residents. Whereas city officials from these communities have mixed reports about the extent to which the local economy has changed, all anticipate being less able to meet financial needs in the next four years. *Examples: Clyde Hill, Hunts Point*

Residential – Cluster 8
These suburban communities are prominent neighbors of large urban centers and most experienced a great deal of growth over the past decade. More than 90 percent of these cities report their local economic conditions have worsened, and more than 80 percent report they are less likely to meet financial needs now than four years ago. *Examples: Camas, Maple Valley*

Urban Outskirts – Cluster 7
Many of these communities display a rural character, but are in close proximity to urban centers. Similar to cluster 4, 90 percent reported they were less able to meet financial needs in 2004 compared to five years ago. Only 44 percent report the same about 2009 compared to four years ago. *Examples: Grandview, Steilacoom*

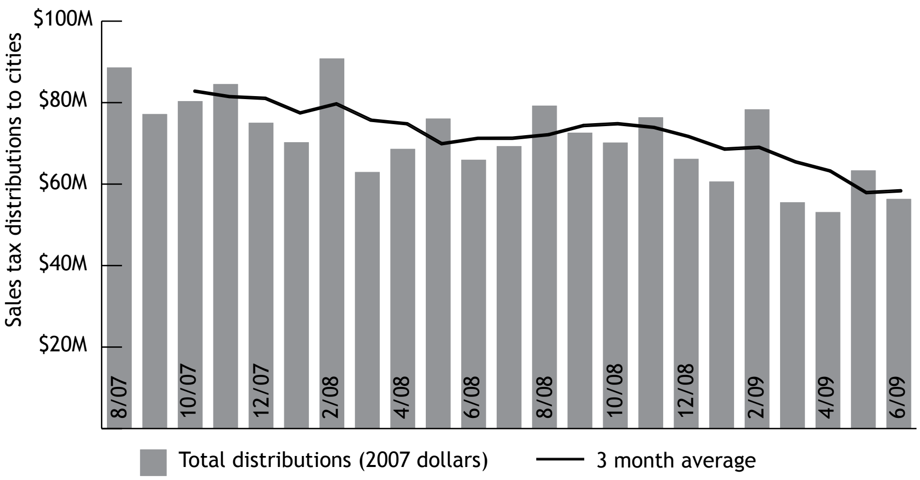
Cities are required by law to balance the budget. This means that infrastructure maintenance and programs desired by the community can go unfunded. And at times service cuts are necessary.

This structural imbalance is not unique to Washington's cities. A national survey of city finance officers found that as 2008 came to a close, cities' general fund expenditures grew nearly five percent, while revenue growth was only 3.4 percent. These city finance officials forecasted the same scenario for fiscal year 2009, with revenues declining nearly a half percent and spending increasing 2.5 percent within the year (figures adjusted for inflation).[1]

> We're having quite a revenue shortfall from retail sales being down and we're really nervous.
>
> *Karen Clifton, City Treasurer, Union Gap*

Today many cities' revenues have declined so precipitously that finance directors regard it as "good news" when local revenues level off and are no longer in free fall. And these officials still wonder whether their city has hit bottom.

As the economy declined, city sales tax revenues are one of the many city revenue sources that fell



Source: Department of Revenue

Note: Amounts shown do not include mitigation funds some cities receive to offset the impacts of the streamlined sales tax.

> The bad news is that our community is highly dependent upon auto sales. The good news is that because auto sales dropped so quickly and so steeply, the red light went on really fast.
>
> *~Steven Marcotte, Finance Director, Fife*

[1] Christopher Hoene and Michael Pagano, "City Fiscal Conditions in 2009", Research brief on America's cities, September 2009

Cities provide mandated, essential services

Cities provide services that are defined by state and federal law – services that are vital to health, safety and economic activity:

- Cities employ 63 percent of the state's local law enforcement and fire personnel.
- Over 25 percent of the state's traffic flows on city-constructed and maintained streets.
- Water, sewer and stormwater systems provide dependable utility services for millions of urban residents and businesses, and protect our environment and water quality.
- Parks, libraries, senior centers and recreation activities keep communities healthy.
- Permitting and licensing ensure safe buildings and livable communities.

These are the systems and services that keep Washington open for business. Developing and maintaining these services is vital to growing and sustaining a healthy economy. When even one service is lacking, Washington's competitiveness is in danger.

"Our community wants to build a park, but you have to ask the question 'Can I take care of it in ten years?' It's really insidious because even though we might have the money today for a project, we may not have it in the future."

~Mary Ann Duncan-Cole, City Administrator, Stevenson

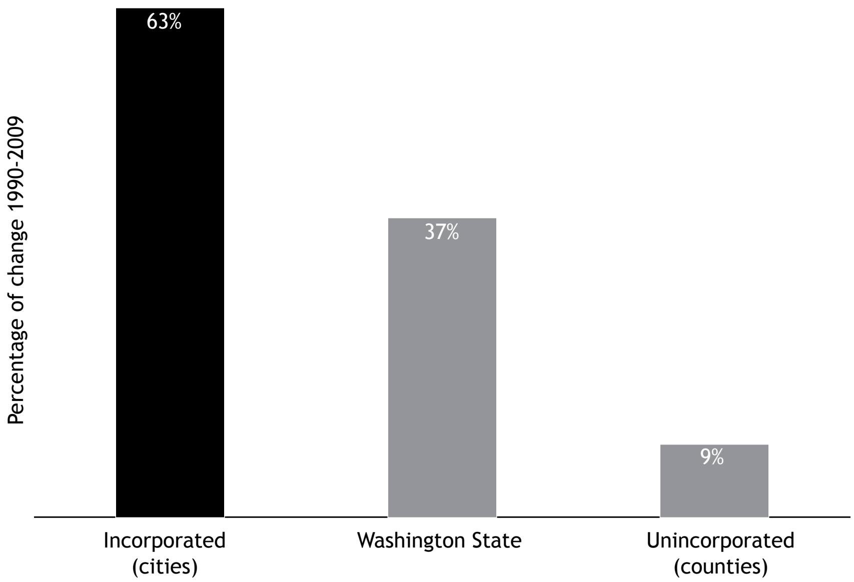
"We have parks, but no recreation program. The library is full, but it is only open a couple of days a week. The problem our community faces is funding these critical services when most of the residents are living in poverty."

~Ramona Fonseca, Mayor, Granger

Cities are home to a growing proportion of Washington's people

Cities are the state's social, cultural and economic centers. They are home to more than four million people – 62 percent of the state's population.

Since the adoption of the Growth Management Act, city population has grown far more than unincorporated areas or the state as a whole



The GMA requires 217 cities to plan for and accommodate growth. To serve growing city populations, cities strive to:

- Provide reliable, environmentally-sound infrastructure systems;
- Maintain low crime rates;
- Nurture vibrant economic centers;
- Provide parks and recreation services;
- Maintain open spaces;
- Plan for affordable housing and a growing workforce; and
- Manage the impacts of growth on the environment.

Accommodating population growth defined in state law creates fiscal pressure on city governments.

Cities experiencing new residential development during the housing boom received one-time revenues – sales and property tax on new construction and real estate excise tax. Although many of these tax revenues were one-time increases, the majority of government service demands created by this growth are ongoing.

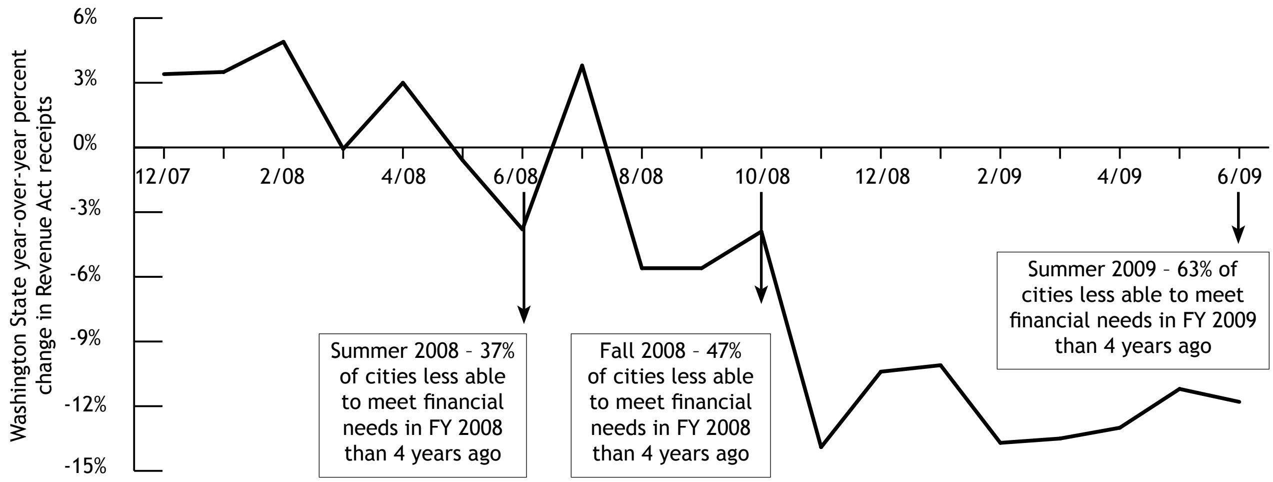
"Public safety remains a core priority. Yet key police and fire initiatives have been curtailed due to the recession. In 2010 we expect to closely examine – along with community members – the question of how we can continue to provide quality, affordable public safety services in the years ahead despite population and service area growth."

~Dan Pike, Mayor, Bellingham

Struggling to meet community needs

As the national, statewide and local economies decline, cities have fewer resources to meet local community needs. While in summer 2008, 37 percent of cities indicated they were less able to meet financial needs than in the past, that figure grew to 63 percent in summer 2009.

As the statewide economy deteriorates, the percentage of cities less able to meet the needs of their community grows



Note: Revenue Act receipts include: retail sales, business and occupation, use, public utility, tobacco products; not corrected for inflation

Source: Department of Revenue

The recession's effects are uneven

Metropolitan areas are hardest hit

Responses to the State of the Cities surveys showed that cities in metropolitan areas were generally harder hit by the recession than those in rural areas. Larger, more urban cities often have a larger sales tax base or grew more rapidly during the recent housing boom. The economic boom and revenues associated with growth allowed many of these communities to continue providing basic city services in spite of tax-lowering measures imposed in the early part of this decade.

Some cities never experienced the economic boom

Other cities didn't experience the boom of the last decade, and subsequently didn't feel the recession's impacts to the same degree. These mostly small and rural communities are more property tax-dependent, and were some of the proportionately larger recipients of sales tax equalization prior to its demise in 2000, when the Legislature repealed the Motor Vehicle Excise Tax (MVET) after voters approved Initiative 695. In the first years following this action, the Legislature provided some "backfill" of that lost MVET revenue, but the majority of this state funding diminished over time. These cities responded by methodically cutting services and have survived on minimal revenues ever since.

Some other cities – mostly smaller – experience the same structural imbalance as their peers, but are fortunate to host a growing industry, a successful company, or some other welcomed economic growth.

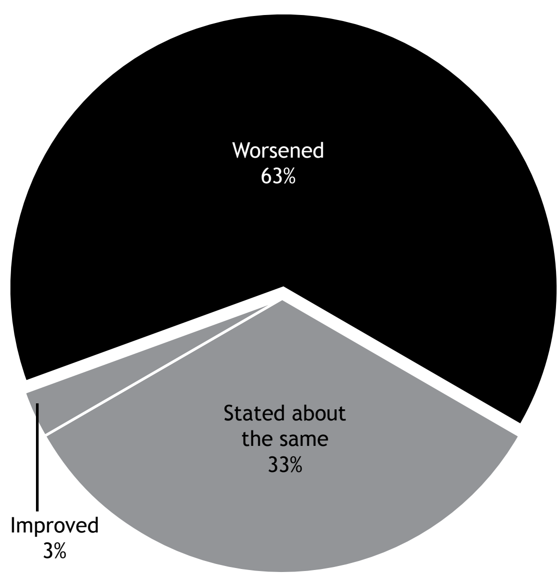
Most cities are suffering more because of the recession

Overall, 63 percent of cities report that since the summer of 2008, their local economy worsened. These cities generally share these characteristics:

- The majority are in metropolitan counties;
- Many depend on commercial activity; and
- Most had high levels of growth and development in the last few years.

Following the adoption of city budgets in fall 2008, many of these cities saw revenues plunge below already pessimistic revenue projections. Budget amendments were required to scale back services even further than planned.

More than 3 in 5 cities indicate local economic conditions have worsened between summer 2008 and 2009



Percent of cities within each cluster indicating *worsened* when asked about the change in economic conditions between summer 2008 and 2009

Non-Metro Area Clusters	
Regional Centers (Cluster 1)	100%
Rural Commercial Centers (Cluster 2)	50%
Tourism Hubs (Cluster 3)	25%
Light Industrial/Natural Resources Hubs (Cluster 4)	27%
Small Residential (Cluster 5)	57%
Rural Communities (Cluster 6)	54%
Metro Area Clusters	
Urban Outskirts (Cluster 7)	45%
Residential (Cluster 8)	93%
High Income Residential (Cluster 9)	50%
Mixed Resources (Cluster 10)	100%
Small Commercial Centers (Cluster 11)	83%
Medium Commercial Centers (Cluster 12)	70%
Large Commercial Centers (Cluster 13)	88%
Largest Cities (Cluster 14)	100%

City cluster shaded when 70% or more of respondents within cluster indicated that local economic conditions *worsened*. More information about each city cluster can be found on page 4 or in the Appendix.

Thirty-three percent of cities reported that their economies stayed about the same between summer 2008 and 2009. These are often smaller, more rural cities. Some of these cities didn't experience the housing boom or rapid growth of the past decade, some saw fiscal deterioration long before the recession hit, and others are still fortunate to have a steady economy.

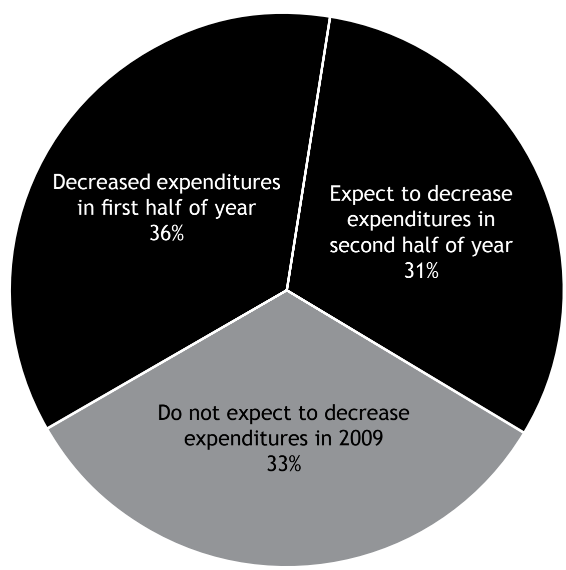
> "We have felt the effects from the economic downturn, but we have an industrial area that has saved our bacon. Firms in the industrial area pay good wages and have kept employment levels high."
>
> *~Chuck Blum, Mayor, Woodland*

Only three percent of cities reported that their economies improved in the past year. These are small cities, with an average population of 5400. In many cases, one large construction project or new retail development can significantly impact these cities' resources. Cities also attributed the economic improvement to growing tourism and available and affordable industrial land.

Cities are cutting essential services and capital investments

The deteriorating economy forced cities to cut services and capital investments. Sixty-seven percent of cities are expected to make budget cuts before this budget cycle ends. Thirty-six percent of cities reported taking action in the first half of the year because revenues were coming in below projections and another 31 percent said they expected to make additional cuts before the end of this year.

By the end of 2009 two-thirds of cities will either re-open the budget or decrease expenditures due to a reduction in revenues

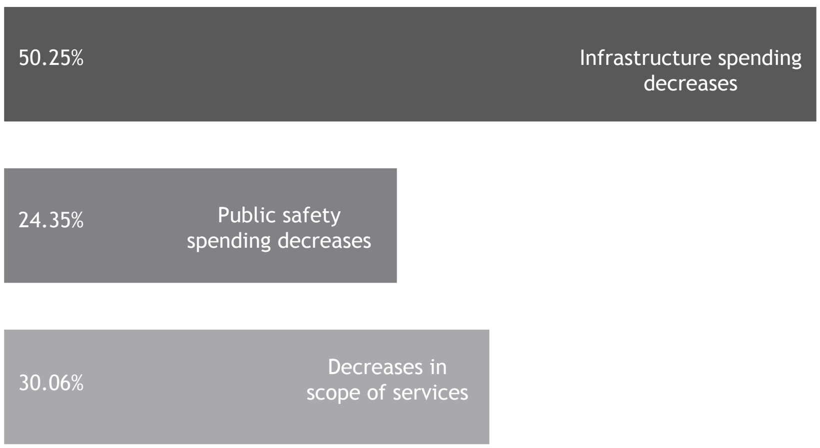


The largest spending decreases have been in infrastructure and general government spending. At the beginning of 2009, 50 percent of cities decreased infrastructure spending, and 51 percent decreased general government spending.

Of the cities re-opening already adopted budgets in 2009, 60 percent have or will cut infrastructure spending and 80 percent will cut general government spending. Infrastructure spending typically includes streets, parks and capital facilities. General government typically includes financial services and permitting, but can also include health and safety services like animal control, and parks and recreation services.

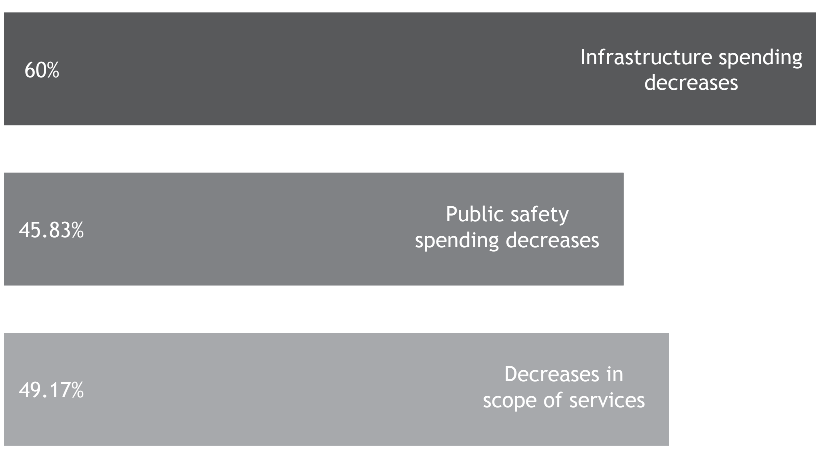
> We're having significant difficulty maintaining acceptable service levels and capital investments. We don't have the funds for new street construction and improvements beyond next year. Our fire stations need an investment of $30 million or more to meet basic seismic standards. And we lack the funds to develop many of our parks.
>
> *~Pat McDonnell, City Manager, Vancouver*

Actions taken in fall 2008 to balance 2009 city budgets



Source: AWC City Budget Survey, January 2009

Actions taken in 2009 by cities either re-opening the budget or expecting to



> Our services are pretty basic—there's not a lot of extras. We have an activities center with a three-quarters FTE running it. There just aren't a lot of luxuries we can give up.
>
> *~Katrina Asay, Mayor, Milton*

Although many city services and departments suffered cuts, most cities' largest cuts are in general administration, police, street maintenance, permitting/planning, and parks

	Biggest cut in **dollars***	Biggest cut **relative to dept's overall budget***
General administration	36.5%	40.0%
Police	30.8%	19.0%
Streets	30.8%	16.2%
Permitting/planning	27.9%	25.7%
Parks	24.0%	10.4%

*Of the cities that cut services (56% of total), percentage of cities responding for each category. Some cities indicated more than one department.

These are cuts cities work hard to avoid. Cities try to minimize the impacts to citizens and businesses, but the slow erosion of services will be noticed over time.

- Cuts to police departments have included layoffs and elimination of various positions including patrol officers. It has also included the deferral of purchasing new vehicles and equipment.
- Street overlay and repair projects have been deferred across the state, resulting in significant cost increases down the road.
- Decreased funding for parks and recreation has impacted programming, maintenance as well as capital upkeep. This includes a reduction in hours for local museums, libraries and aquatics centers.
- As a reflection of decreased development, permit counter hours have been shortened, open jobs left vacant and staff laid off. When the economy improves and residential and commercial development picks up, cities will be hard pressed to meet local demands.

Cuts to these essential city services are detrimental to a community's economic vitality, particularly in the long term. Innovation and economic growth occur in areas that attract a critical mass of creative talent. Communities must compete to recruit businesses and workers.

It is imperative that cities create and maintain the communities where workers want to live and businesses want to locate. This requires providing essentials like a sound transportation system. Amenities like parks and community centers are also necessary. Low crime rates and a general sense of security are critical. Permitting and planning services enforce certain standards that reflect a community's character, ensure safety through building codes and protect the environment.

Cutting city services may meet a short-term financial need. But the long-term consequences of deferred investments can be significantly more costly.

> We've reduced bodies in our fire department to the point that if there's more than one call at a time, we're unable to respond to it.
>
> *~Ed Hildreth, Councilmember, Tumwater*

Cutting staff costs

Nearly three out of five dollars of cities' operating budgets are spent on employee salaries and benefits. City employees provide the services that define local government: they fight fires, maintain public safety, ensure that new buildings are safe, maintain parks, build and maintain streets, provide safe drinking water, and staff community centers. Today, cuts are being made in staff functions.

Many cities are leaving vacant positions open or permanently reducing staff levels. Other cities are reducing salaries, hours, or contributions to deferred compensation and health insurance in addition to layoffs or in an attempt to avoid them. In many cities, cuts are felt by all employees, in every department.

Cities reported a variety of actions to cut staff costs:

- Forty-three percent of cities froze hiring, either when adopting the 2009 budget or in subsequent months. An additional eight percent plan to do so in the second half of 2009.
- Twenty-five percent of cities laid off employees in the first months of 2009; 14 percent as part of their 2009 budget, and another 11 percent after the budget was adopted. An additional seven percent plan layoffs later this year.

City clusters most likely to report cuts in staffing were those most severely affected by the recession

	Employee hiring freeze		Employee layoffs	
	% of cities that froze hiring with adoption of 2009 budget or during first half of year	Total % of cities implementing or planning a hiring freeze in 2009	% of cities that laid off employees with adoption of 2009 budget or during first half of year	Total % of cities implementing or planning layoffs in 2009
All cities	43.2%	51.4%	25%	31.8%
Non-Metro Area Clusters				
Regional Centers (Cluster 1)	66.7%	83.3%	50.0%	50.0%
Rural Commercial Centers (Cluster 2)	33.3%	33.3%	33.3%	33.3%
Tourism Hubs (Cluster 3)	25.0%	62.5%	12.5%	12.5%
Light Industrial/ Natural Resources Hubs (Cluster 4)	18.2%	27.3%	9.1%	9.1%
Small Residential (Cluster 5)	28.6%	28.6%	14.3%	14.3%
Rural Communities (Cluster 6)	15.4%	23.1%	15.4%	19.2%
Metro Area Clusters				
Urban Outskirts (Cluster 7)	37.5%	37.5%	12.5%	16.7%
Residential (Cluster 8)	73.3%	86.7%	26.7%	53.3%
High Income Residential (Cluster 9)	25.0%	25.0%	0.0%	0.0%
Mixed Resources (Cluster 10)	100.0%	100.0%	100.0%	100.0%
Small Commercial Centers (Cluster 11)	58.3%	66.7%	66.7%	66.7%
Medium Commercial Centers (Cluster 12)	80.0%	80.0%	44.4%	44.4%
Large Commercial Centers (Cluster 13)	87.5%	87.5%	0.0%	37.5%
Largest Cities (Cluster 14)	33.3%	66.7%	50.0%	66.7%

City clusters are shaded to reflect those clusters where a larger percentage of cities have laid off employees or froze hiring. More information about each cluster can be found on page 4 or in the Appendix.

Spending down reserves

Good fiscal management means putting money in reserves during good times, and using it in hard times. This is exactly what many cities did during the middle part of this decade when growth was strong. But seldom are cities' reserve funds sufficient enough to plug the gaping budget holes caused by this recession. And since no one knows when recovery will take place, many city officials are hesitant to exhaust reserve funds in one year.

Reserves traditionally are the first line of defense against cuts in essential city services. Fifty-five percent of cities report an increase in the use of ending cash balances over the previous four years. Thirty-five percent report using more operating reserves and another 35 percent report using more capital reserves.

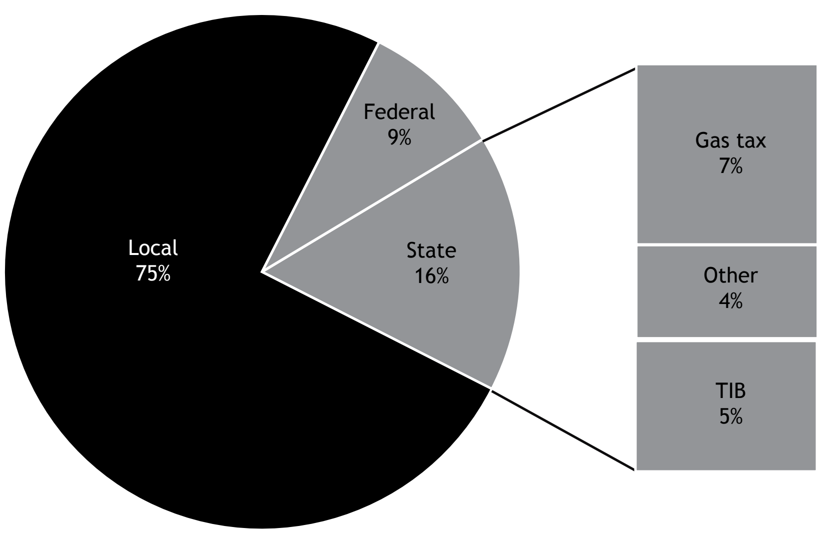
> "We don't want to use all our reserves because they are a one-time resource. We just don't want to see them eliminated."
>
> *~Diane Supler, Deputy City Administrator, Sumner*

Deferring vital infrastructure investments

When a park closes, or the response time to an emergency takes a while, people notice. But deferring maintenance on city streets can often go unnoticed for quite some time. This kind of infrastructure investment lacks the passionate advocates that many cities have for parks, senior centers, and public safety services.

Cities also lack a substantial dedicated revenue source for street construction and maintenance. As a general rule, $3 of every $4 allocated to city transportation comes from local resources. The remaining $1 comes from state dedicated gas taxes and federal or state grants.

Three-quarters of city street funding comes from local resources



Source: Washington State Department of Transportation, 2007

Although the gas tax is an important source of revenue for city streets, collectively cities receive less than three cents of the 37½ cents levied per gallon. After the two most recent state gas tax increases, cities received an additional half cent, which is roughly $16 million a year. This $16 million increase is allocated among all cities on a per capita basis – equaling about $4 per city resident. However, a typical urban city street improvement project costs approximately $16 million for just one mile.

Over 30 percent of cities making cuts report that the street department received the biggest cut in dollars in this year's budget. The result of this deficit is deteriorating street infrastructure.

> "The one area everyone is struggling with is in money for streets and sidewalks. Revenues we get from the gas tax just aren't enough. We fix potholes, but that's it."
>
> *~Brian Shay, City Administrator, Hoquiam*

Redirected and declining state infrastructure funding hits cities hard

Because of a projected $9 billion budget deficit during the 2009 legislative session, the state Legislature used capital resources to shore up the general fund. This included transfers from the Public Works Trust Fund and the Local Toxics Control Account to the general fund, as well as a reduction to the Community Economic Revitalization Board.

The trust fund is a critical loan funding source for many local government infrastructure projects such as drinking water, sanitary sewer, stormwater and streets. Traditionally, cities received approximately 56 percent of these funds, which would have totaled roughly $206 million of the $368 million transferred to the state general fund for the 2009-11 biennium. Since the beginning of the decade, requests for loan assistance from the Public Works Board have consistently exceeded available funds. Between 2000 and 2008, the fund was only able to grant an average of 55 percent of the dollars requested. A tremendous need still exists for this assistance program.

Two temporary public works grant programs were included in the 2009-11 state biennial budget. The capital budget included $9.5 million for small communities in rural counties and $9.5 million for urban vitality. But appropriations for these programs are at levels far below the traditional loan program and the need is far greater than the resources available.

In summer 2009, the Public Works Board received 109 applications from cities, requesting $67 million, for the $9.5 million available from the small communities in rural counties program (in total 209 applicants requested $137 million). Fifty applications from cities, requesting $37 million, were submitted for the $9.5 million available in urban vitality grants (a total of 60 applicants requested $201 million).

In addition, the Transportation Improvement Board's (TIB) ability to partner in funding local street infrastructure projects is reduced due to declining gas tax receipts. Some of the TIB's programs have been postponed to the extent that its executive director has predicted "corridor" grant funding will not be available for at least the next four years.

The federal American Reinvestment and Recovery Act (ARRA) has provided some assistance to city infrastructure projects, but to date the net gain is below the infusion of assistance the trust fund and other redirected state funds would have provided.

Funds distributed through ARRA include:

- Highway projects – over $95 million to 81 cities for projects that address high priority highway preservation and safety needs, as well as projects that address capacity, multi modal and freight needs;
- Drinking water projects – over $27 million to ten cities for capital improvements to water systems; and
- Water quality projects – over $58 million to 13 cities for water pollution control infrastructure, including the upgrade and expansion of wastewater, reclaimed water and stormwater facilities.

While these funds are helpful, substantial infrastructure investments are needed:

- In 2008, 52 percent of cities reported delayed or reduced spending on capital development projects in the past six years;
- Sixty percent of cities also expected to delay or reduce spending on future capital projects; and
- Nearly 40 percent of cities report a decrease in the capital budget for 2009.

> "Not only are TIB grants and PWTF loans more competitive than ever, our fuel tax collections and REET revenues are shrinking. This has a compounding negative impact on our ability to maintain critical infrastructure."
>
> *~Greg Cuoio, City Manager, Lacey*

Conclusion

Cities in Washington are doing all they can to rise to the recession's challenges, but it is an uphill struggle. The underlying fiscal imbalance of city budgets must be remedied to create a sound foundation for economic recovery and growth.

Cities are working hard to weather the immediate crisis. But far too many essential investments are being deferred, and the long-term result will be a legacy of deteriorating infrastructure that acts as a brake on economic recovery and growth.

Cities need the immediate and active partnership and support of the state and federal government to prevent this deterioration. And in the long term, cities need a focused and sustained re-examination of how city governments are funded. Together, we must find a new funding system for city services that is sustainable, adequate, and capable of promoting economic growth and prosperity.

> "We need to ensure that we're providing the best services at the lowest costs to our citizens. The state should begin the conversation with cities of how we best fund and provide mandated and citizen-desired services."
>
> *~Karen Rogers, Councilmember, Port Angeles*

Recommendations

All levels of government are partners in providing services to citizens. And all levels of government are accountable for positioning our state for economic recovery and preparing for the population growth we know is coming. Together, state and local governments must keep Washington competitive in the national and worldwide markets, encouraging economic growth by investing in the infrastructure needed to accommodate it.

Although the economy is expected to begin improving this next year, consumer spending is likely to remain low, and unemployment is expected to rise. These factors will continue to constrain both city and state resources. However, now is the time to invest in our local communities. This is the only way to nurture and accelerate economic recovery.

Recommendations for state action:

Provide critical infrastructure assistance

To meet mandates and service levels, cities need state assistance.

- Ninety-seven percent of cities believe that increasing state funding to local governments for infrastructure (capital projects) would be helpful.
- Another 84 percent indicate that state funding for environmental protection/restoration is needed to help cities meet their primary obligations for protecting the environment, especially by providing quality infrastructure systems, including improved stormwater management.

Cities depend upon important infrastructure assistance programs such as the Public Works Trust Fund, the Transportation Improvement Board, the Community Economic Revitalization Board and more. It is critical the state partner with cities to ensure development of the infrastructure systems that keep our state economy vibrant.

Grant cities greater flexibility with existing revenues

Cities need the same discretion the state has to focus on critical needs, especially in hard times.

- Eighty-seven percent of cities say that allowing cities greater flexibility with all existing revenues – both operating and capital – would help them adapt funding to unique local needs.

This includes removal of non-supplant requirements that encourage unsustainable growth. When revenues dip, like now, cities need to have full access of funds to sustain ongoing programs. Cities must be able to allocate resources the way the local community desires.

Help cities nurture local economies with new and enhanced economic development programs

Cities play a vital role in accelerating the state's economic recovery, because they are the industrial, commercial and retail centers of growth. When the state helps cities with economic development, the result is more revenue for both the state and local governments. This kind of investment is needed right now, so that Washington's communities will be poised to benefit from and increase the pace of economic recovery.

Recommendations for city action:

Many cities are already rising to today's challenges by throwing open the doors to creative, expanded dialogue with citizens, employees, unions, school districts and other partners. These conversations identify local strengths and assets, set priorities, and find consensus on ways to share hardship while protecting cherished community values. Cities that engage in these conversations can share important lessons.

Work with citizens and employees to find strategies to weather the crisis and prioritize services

Cities foster positive relationships with unions and staff by being transparent about the state of their budgets, and asking for feedback and help from all levels of the organization. Staff and unions are a valuable source of ideas for improving efficiency and ways to minimize layoffs and service cutbacks.

By working together, cities and their staffs develop creative and flexible options for employees – furloughs, salary reductions and changes in work week schedules. When employees help choose how budget cuts impact them, it builds morale and reduces fear during tough and frightening economic times.

Many local jurisdictions are also holding more public hearings, sending out surveys and asking citizens to weigh in on city priorities.

Partner with neighboring cities, local businesses, school districts and others to maintain services

Many long-term partnerships are helping cities sustain services such as drinking water, online permitting, and public safety. While partnerships do not always provide immediate short-term solutions for budget shortages, they are a long-term strategy for providing high quality services shared among neighboring communities.

Nurture economic development

Although hard times tempt people to hunker down and focus on the negative, the opposite is what is needed. Now is the time to get in position to maximize the benefits of the recovery, and to find creative ways to stimulate and speed economic growth. Cities are pursuing a variety of nurturing strategies.

Some local governments are changing ordinances that regulate zoning and parking codes to encourage renovation in downtown or historic areas, and to bring more mixed use activity to city centers. Others are relying upon existing multi-jurisdictional economic development councils that help smaller local governments stimulate economic development in ways they couldn't have achieved acting individually. Cities are also offering economic incentives and more flexibility to developers. Some regions are updating or altering transportation plans to encourage more economic growth.

These examples illustrate the potential for cities to build on their underlying strengths, collaborate with allies, and build a strong foundation for economic recovery.

Case Studies

Cities nurture local economies

Many cities throughout the state rely on the diversity of their local economies as a way to stimulate economic sustainability. Cities are pursuing new and well-tested strategies to encourage economic development including:

- Building and maintaining infrastructure systems;
- Streamlining permitting processes for commercial and residential development;
- Offering economic incentives; and
- Revising ordinances and parking codes.

City officials understand how critical a solid infrastructure system is in encouraging local economic development. Cities that want to attract new development must invest in streets, water/sewer systems, parks and community centers. Responding to a survey for the 2007 State of the Cities report on economic development, ninety-four percent of city officials recognized infrastructure as an important economic development tool.

Covington invested heavily in infrastructure over the last few years and hired an economic development manager. They are currently working on a plan that will rezone their downtown and create a new town center.

Kennewick maintains an emphasis on basic city infrastructure to help the city accommodate businesses wanting to move there. The city council dedicates most of their optional sales tax revenues to support capital improvements – usually street system improvements – which helps retain local high tech business. Bob Hammond, Kennewick city manager, also notes that having good schools and public safety services are all part of this critical infrastructure. "A city's infrastructure is such an important piece of local government. If this starts to fail, it becomes a deterrent when business owners consider where they want to move their business."

Multi-jurisdictional economic development councils nurture and revitalize local business relationships and activity. Stevenson's participation in an economic development commission composed of nearby cities, the county and port enabled the city to encourage economic development and have a presence advocating at the state and federal levels.

Montesano hired a consultant, and together with its Chamber of Commerce, planning commission and Council of Government, is preparing a detailed capital facilities plan and downtown development standards and regulations.

Mixed-use areas promote diverse and thriving city centers. Hoquiam changed zoning ordinances to allow mixed use in the downtown area. This includes allowing apartments above the first floor of commercial buildings, which led to the development of two apartment projects in unused spaces. Hoquiam also adopted a local historic preservation ordinance that gave tax incentives for restoration projects, leading to the renovation of the city's largest downtown commercial building.

Cities offering incentives, greater flexibility and streamlined permitting processes have experienced success attracting developers and business. For example, Zillah expanded uses in planned developments and gave more flexibility to developers. They adopted theme-based standards and worked with developers to streamline them.

Kent's city council recently approved property tax abatement for multifamily residential projects with mixed use in the downtown area. The pre-existing property tax incentive was for owner occupied residences, and now extends to rentals.

Puyallup is also seeing positive results from the property tax abatement offered for residential units in their downtown core. Two developments were built with 50 condos above businesses such as coffee shops, restaurants and a bank. This is bringing residents, jobs and commercial activity into the same area. The city is also pursuing transit oriented developments.

"A city's infrastructure is such an important piece of local government. If this starts to fail, it becomes a deterrent when business owners consider where they want to move their business."

~Bob Hammond, City Manager, Kennewick

Cities partnering to provide excellent services

Multi-jurisdictional partnerships among governments are a time-honored strategy that can improve efficiency and hold down costs. Today, these partnerships are a vital and growing part of cities' creative responses to both the structural imbalance that results from expenses rising faster than revenues and the recession that compounded budget woes.

Some recently-created partnerships deliver immediate alternative service-delivery benefits, helping cities continue some services through the economic downturn, and resulting in savings, greater efficiencies, sustained services and greater public trust. While some of these innovative solutions have helped cities manage resources in a tough fiscal environment, they haven't always solved long-term funding problems or achieved ongoing, sustainable funding for remaining local government programs.

Common partnerships include public safety, parks and recreation, animal control, permitting, and, for small cities, staffing. These partnerships are especially successful in areas with a critical mass of residents and where jurisdictions are close together.

"It is a prudent exercise to take a look at ways you can collaborate." notes Gary Crutchfield, City Manager of Pasco. "You can reduce costs or improve the service levels with the same costs."

Leading by example

Many local governments have become experts at collaboration and partnership-building in areas ranging from public safety to general administration to infrastructure.

- The Pullman-Moscow Airport is funded by the cities of Pullman and Moscow, Washington State University, Latah County and the Port of Whitman County. Major capital projects at the airport would not have been possible without funding from multiple entities. "Economies of scale is the name of the game," says John Sherman, city supervisor of Pullman. "It is a necessity to collaborate when you don't have funds."

- Rivercom dispatching center is a collaboration of the cities of Wenatchee, East Wenatchee and Douglas and Chelan counties. Rivercom serves about 28 agencies including rural fire departments, ambulance companies, police and fire. They are about to celebrate six years of successful partnership.

- The Valley Regional Fire Authority (VRFA), established in 2007, joins the resources of the Auburn and Pacific fire departments to provide fire services to the communities of Algona, Auburn and Pacific. With the recent annexations of the Lea Hill and West Hill areas, and a contract to service King County Fire District 31, the VRFA provides service to approximately 77,000 citizens, covering nearly 40 square miles. "Forming a partnership with the cities of Auburn and Algona to create the Valley Regional Fire Authority has been a great benefit for the citizens of Pacific," says Pamela Nelson, Finance Director of Pacific.

- Pasco, Kennewick and Richland formed an animal control agreement 11 years ago. Pasco purchased and fixed up the old animal shelter. That debt is being repaid through an operating agreement between all three cities. They contract with a private entity to operate the animal control, and it is overseen by a board with staff members representing each city. This reduced Pasco's costs about 25 percent and decreased the number of citizen complaints.

- The eCityGov Alliance is an inter-local collaboration of 39 cities and other local government agencies in the Puget Sound region that provides cross boundary web service portals for citizens and businesses that include: MyBuildingPermit.com, NWMAPS.net, MyParksAndRecreation.com and NWProperty.net.

- Yakima, Sunnyside, Union Gap and Yakima County partner to carry out Washington State Phase II NPDES Stormwater Permit requirements. In 2005, a regional Stormwater Policy Group (RSPG) was formed to oversee municipal efforts to comply with permit requirements. An intergovernmental agreement was signed in 2007 after a comprehensive report outlined that savings would be realized through a regional approach to compliance. The RSPG has continued to meet as needed, and the cooperative effort has been a model for other areas looking to share scarce resources and achieve better results at a lower overall cost.

- Port Angeles established a new park district in cooperation with the county. The effort was led by an active citizen group and supported by the city and county. This allowed the public pool to remain open and the city was able to balance their budget for this year because of the $360,000 in savings from not being primarily responsible for pool operations.

- Some cities share staff as a way to maintain the most basic services. Stevenson and North Bonneville have shared a building inspector for many years. Edgewood and Buckley began sharing their building inspector this year. "Zillah has an interlocal agreement with Toppenish, Wapato and Granger that enables us to help each other whether it's with equipment or personnel," says Zillah Mayor Gary Clark.

Personnel cuts unavoidable despite collaborative efforts

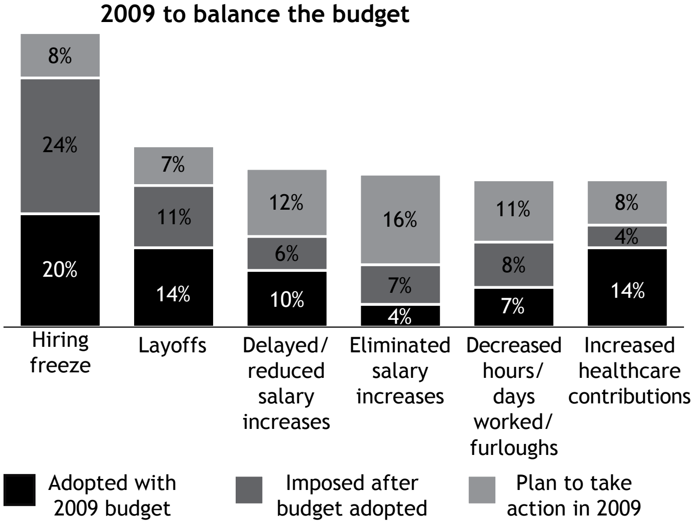
When the recession hit Washington state, many cities had to make cuts to their largest expense area—personnel. By summer 2009, 43 percent of cities had frozen hiring; one in four cities had laid off employees; and nearly 20 percent of cities required increased employee contributions for health care. An economic downturn of this magnitude has required responses from city halls that are both drastic and innovative.

These cutbacks will not go unnoticed.

- Bellingham used several ways to solicit ideas reducing expenses, including employee and resident surveys. The city also had a task force of department leaders and council members analyze budget-cutting ideas and make recommendations to the Mayor on how deficit targets could be assigned to departments and service areas. Between January 2008 and October 1, 2009, Bellingham eliminated more than 50 FTE positions, 18 of which were layoffs. These cuts have affected all departments and city services, including reductions in library, park and pool hours, recreation program elimination, permit center staffing reductions, postponement or elimination of capital projects and technology initiatives, and much more.

- Bremerton's offices are open five days a week, but in the main city hall building, counter services are no longer available to the public on Fridays. This was done to accommodate budget cuts that resulted in furloughs and reduced staff and it impacts various departments differently. Having the front counters closed gives staff time to catch up on work, but it means the public can't make payments to the city or apply for building permits or business licenses on Fridays.

Staffing, compensation and benefit actions taken in 2009 to balance the budget



Working with employees to find solutions

Although layoffs are sometimes inevitable, cities recognize that it's costly and difficult to hire and train new employees. Therefore, many are employing additional cost-cutting strategies that allow them to keep valuable, trained staff whenever possible.

Cities are also engaging staff in collaborative processes to identify cuts. Employees have been consulted about the cuts that directly affect them—such as increased contributions to health insurance and mandatory furloughs. They have also been engaged in identifying ways to cut costs and create efficiencies to avoid more layoffs.

City officials say that communication with unions, department leadership and other employee groups has been critical. In some instances, this strengthened relationships among management, union leaders and employees.

Many city officials emphasize the need to work with employees to identify where cuts should be made, and where efficiencies could be identified. "Lots of communication is important," says David Webster, Chief Administrative Officer of Bellingham. "We shared detailed information, surveyed employee groups, and held many meetings with employees and union leaders throughout 2009. This has helped increase trust and ease stress as much as possible under such trying circumstances. I believe it helped us achieve some concessions from bargaining units and assisted employees at all levels of the organization understand the need for these difficult actions."

"Communication and fairness" are keys to successful relationships with unions, says John Hodgson, chief administrative officer with Kent. "We've given our unions an opportunity to be part of solutions by contributing their ideas."

Many cities asked employees to propose budget cuts for their departments, developing trust between management and employees, and giving people choices about how budget reductions affect them. Several city officials indicated that this collaboration and transparency keeps morale strong, and identifies creative ways to save money.

In Camas, sanitation staff figured out a better and cheaper way to set out and size garbage cans in the parks. This cut billing to the parks fund about $8,000 to $10,000 a year. City administrator Lloyd Halverson says, "Symbolically and in terms of morale, the fact that staff identified this efficiency is just as important as the dollars saved."

Appendix

Appendix: Washington cities by cluster

(as designated for State of the Cities reports)

Regional Centers (Cluster 1)

- Anacortes
- Centralia
- Ellensburg
- Longview
- Moses Lake
- Mount Vernon
- Port Angeles
- Pullman
- Walla Walla
- Wenatchee

Rural Commercial Centers (Cluster 2)

- Aberdeen
- Chehalis
- Colville
- East Wenatchee*
- Ephrata
- Grand Coulee
- Kelso
- Morton*
- Napavine*
- Okanogan
- Omak
- Oroville
- Quincy
- Sedro-Woolley*
- Shelton
- Tonasket
- Twisp
- Woodland*

Tourism Hubs (Cluster 3)

- Burlington
- Chelan
- Cle Elum
- Friday Harbor
- La Conner
- Leavenworth
- Long Beach
- Ocean Shores
- Port Townsend
- Sequim
- Stevenson
- Westport*
- Winthrop

Natural Resources/ Light Industrial Hubs (Cluster 4)

- Bingen
- Brewster*
- Cathlamet*
- Chewelah
- Colfax
- Conconully
- Concrete
- Coulee City
- Elma
- Forks
- Goldendale*
- Ilwaco
- Kalama*
- Montesano
- Mossyrock
- Newport
- Othello*
- Pateros
- Raymond
- Republic
- Ritzville*
- Roslyn*
- Springdale
- St. John
- Toledo
- Uniontown

Small Residential (Cluster 5)

- Albion
- Cashmere
- Castle Rock
- Colton
- Cosmopolis
- Coulee Dam
- Davenport
- Electric City
- Entiat
- Krupp
- Lind
- Metaline Falls*
- North Bonneville
- Prescott
- Reardan
- Rock Island
- South Cle Elum
- White Salmon

Rural Communities (Cluster 6)

- Almira
- Asotin
- Bridgeport
- Clarkston
- College Place
- Creston
- Cusick
- Dayton
- Elmer City
- Endicott
- Farmington
- Garfield
- George
- Hamilton
- Harrington
- Hartline
- Hatton
- Hoquiam
- Ione
- Kettle Falls
- Kittitas
- LaCrosse
- Lamont
- Lyman
- Malden
- Mansfield
- Marcus
- Mattawa
- McCleary
- Metaline
- Nespelem
- Northport
- Oakesdale
- Oakville
- Odessa
- Palouse
- Pe Ell
- Pomeroy
- Riverside
- Rosalia
- Royal City
- Soap Lake
- South Bend
- Sprague
- Starbuck
- Tekoa
- Vader
- Waitsburg
- Warden
- Washtucna
- Waterville
- Wilbur
- Wilson Creek
- Winlock

* Cities that changed cluster membership from 2005 to 2009. More information can be found on AWC's website, www.awcnet.org/stateofthecites.

Urban Outskirts (Cluster 7)
- Airway Heights
- Algona
- Battle Ground
- Benton City
- Buckley
- Bucoda
- Carbonado
- Carnation*
- Cheney
- Connell
- Coupeville
- Darrington
- Deer Park
- Eatonville
- Everson
- Fairfield
- Ferndale
- Gold Bar
- Grandview
- Granger
- Granite Falls
- Harrah
- Index
- Kahlotus
- Latah
- Lynden
- Mabton
- Medical Lake
- Mesa
- Millwood
- Milton
- Moxee
- Naches
- Nooksack
- Orting
- Pacific
- Prosser
- Rainier
- Rockford
- Roy
- Ruston
- Selah
- South Prairie
- Spangle
- Steilacoom
- Sultan
- Sumas*
- Sunnyside*
- Tenino
- Tieton
- Toppenish
- Wapato
- Washougal
- Waverly
- Wilkeson
- Yacolt
- Zillah

Residential (Cluster 8)
- Bainbridge Island
- Beaux Arts Village*
- Black Diamond
- Bonney Lake
- Brier
- Camas
- Covington
- Des Moines
- Duvall
- Edgewood
- Edmonds
- Fircrest
- Kenmore
- La Center
- Lake Forest Park
- Lake Stevens
- Maple Valley
- Marysville
- Mercer Island*
- Mill Creek
- Mountlake Terrace
- Mukilteo
- Newcastle
- Normandy Park
- Sammamish
- Shoreline
- University Place
- West Richland

High Income Residential (Cluster 9)
- Clyde Hill
- Hunts Point
- Medina
- Woodway
- Yarrow Point

Mixed Resource Cities (Cluster 10)
- Arlington
- Issaquah
- Redmond
- Snoqualmie
- Tumwater*
- Woodinville

Small Commercial Centers (Cluster 11)
- Blaine
- DuPont
- Gig Harbor
- Langley
- Liberty Lake
- Monroe*
- North Bend*
- Port Orchard
- Poulsbo
- Ridgefield*
- Skykomish
- Snohomish
- Stanwood
- Sumner
- Union Gap
- Yelm

Commercial Centers (Cluster 12)
- Bellingham*
- Bremerton
- Burien
- Enumclaw
- Federal Way
- Kennewick
- Lacey
- Lakewood
- Oak Harbor
- Pasco
- Richland*
- Spokane Valley*
- Yakima*

Large Commercial Centers (Cluster 13)
- Auburn
- Bothell*
- Fife
- Kent
- Kirkland*
- Lynnwood
- Olympia
- Puyallup
- Renton
- SeaTac
- Tukwila

Largest Cities (Cluster 14)
- Bellevue
- Everett
- Seattle
- Spokane
- Tacoma
- Vancouver

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